

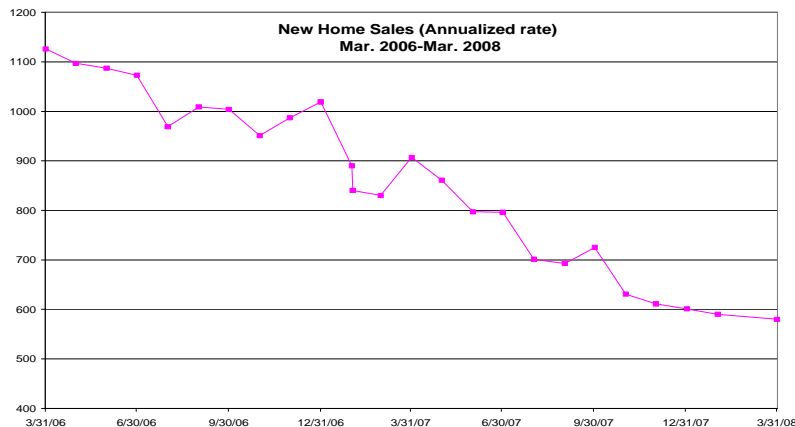


Quarterly Economic Report – 1st Quarter 2008

“Outlook and Strategy”

As we began 2008, news on the economy shifted from showing a slowing economy into much more severe territory where it is now accepted that the US is in a recession and the only questions that remain are how deep we will fall and how long will it last.

With asset devaluation in the housing market worsening in the quarter, it led to a crisis in confidence over collateralization and damaged the ability of some financial institutions to meet their borrowing needs. This lack of confidence also caused skittish investors to withdraw their investments from some “leveraged” mutual funds which ultimately forced several of these funds to declare insolvency and culminated with the failure of the 4th largest investment firm in the United States, Bear Stearns & Co.



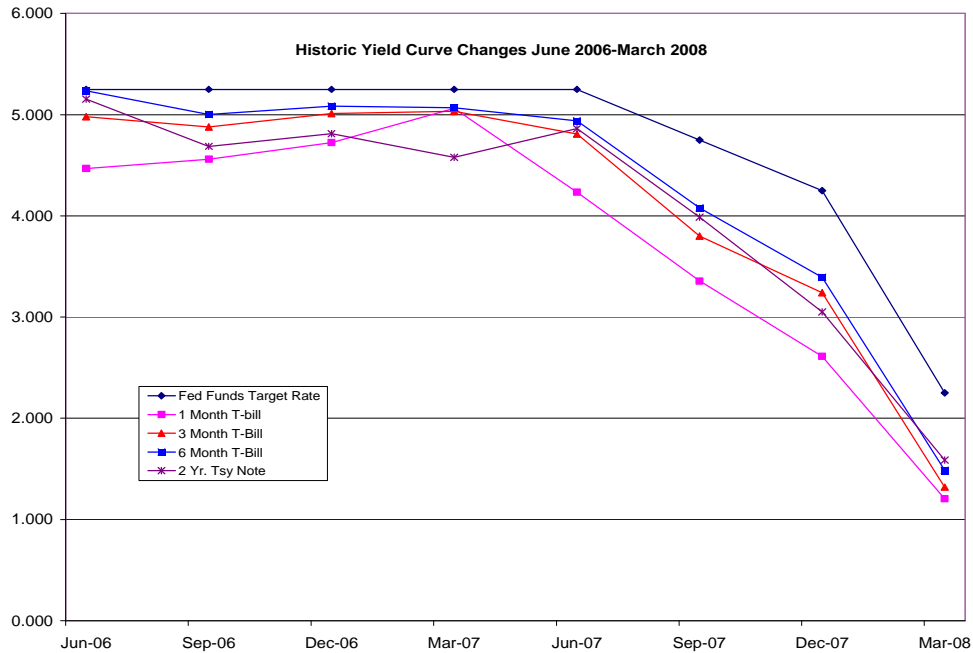
During this period of concern, investment dollars flooded the US Treasury market pushing yields on the 3 month T-Bill to below .65%, a level not seen since 1958.

The Federal Reserve Bank, through its Open Market Committee, created several new financing mechanisms in an attempt to avoid any further “runs on the bank”. Most recently, they have announced that Primary Dealers (of which Bear Stearns was one) can have the same borrowing privileges at the Fed discount window as a bank and any borrowings would be kept “anonymous” to avoid the perception of financial problems.

Employment reports had remained fairly strong through most of 2007, but since the beginning of this year we have seen a string of reports that show rising unemployment and three consecutive monthly declines in Non-Farm Payrolls. This lack of job creation is another sign of the lack of confidence over growth in the economy for the near term.

Energy prices have made all time record highs as demand for refined products remains strong and a weak US Dollar raises the net cost of delivery. Additionally, as interest rates have moved lower, the cost of financing speculative positions has dropped which encouraged trading in commodities such as crude oil and gold.

Yields on short term US Treasuries have returned to more normalized levels as the expanded presence of the Federal Reserve Bank as a “lender of last resort” has removed some fears from investors. Also, by the end of March, market activity shows that bond investors now believe the end of the cycle of easing of monetary policy may be in sight. Whereas earlier in the quarter there was case being made for a return to the 1.00% Fed Funds target rate we saw in 2001, the markets now point to the 1.50%-1.75% range as the stopping point. The shape of the yield curve, especially in the short end, has moved from a steep inversion to a flattening line and appears to be headed to a positive or normal slope over the next few months.



This is a good sign that current expectations are for a short and shallow recession in this country. We would not expect any tightening of monetary policy until well after the November elections unless there is a further surge in energy prices. The early stages of a recovery will be carefully watched for sustainability and then for the emergence of inflationary pressures, but this is not likely to be seen until sometime in 2009.