ECONOMIC & INVESTMENT SUMMARY

As of June 30, 2009

ECONOMIC ACTIVITY

- The economy continues to contract, but at a much slower pace than the previous two quarters. Gross Domestic Product (GDP) most likely shrank for the second quarter of 2009 by an annual rate of about 1% versus a 6% average contraction for the last quarter of 2008 and the first quarter of 2009. Job losses decelerated during the quarter from their 700 thousand per month peak in January 2009.
- The recession has been severe, but signs are emerging of stabilization. The length, about eighteen months, is quite long compared to other slowdowns. The depth has also been brutal. Industrial production, one measure of economic activity fell by 18% from its peak.
- The business contraction is still in the category of a deep recession and looks to avert anything close to the Great Depression. By contrast, the Great Depression lasted 43 months and resulted in a drop in industrial production of 53%.
- Various gauges of economic activity point to signs of stabilization, but at rates still consistent with a recessionary environment. The economy is expected to lose over 300 thousand jobs per month for the next several months and consumer demand for durable goods is expected to be soft despite some signs of life.

INTEREST RATES

- Yields on treasury bonds bucked the trend of the last several quarters and drifted higher. The yield on the ten-year U.S. Treasury bond began the quarter at 2.21% and rose to 2.68% by quarter-end. This was despite an announcement by the Federal Reserve that they would begin buying long term treasury securities. On the afternoon of the FED announcement the ten-year treasury yield dropped from 3% to 2.5%.

STOCK MARKET

- As we enter the dog days of summer, and as people spend time outdoors and go on family vacations less time is spent watching equity markets. That being said, it still has been a busy quarter both for domestic and global equity markets. The beginning of the 2nd quarter started where the 1st quarter ended as markets continued to make back some of the negative returns and finally turn positive for the year. This has led most market pundits to argue that the S&P 500 had put in a bottom on March 9 and is stabilizing.
- We are monitoring the ever increasing government intervention in the free markets, and it has become necessary to keep a sharp eye. The federal government has been an aggressive player in the resolution of the Chrysler and GM bankruptcies dictating much of the outcome. Additionally, three major overhauls formulated during this quarter are greatly affecting the long-term outlook of some sectors. There are bills in congress to drastically change healthcare, financial regulation, and carbon emissions. These future increases in spending are competing with the Federal Reserves initiative to maintain low interest rates attempting to jump start the housing market and fuel economic recovery. It has raised the fear of significant inflation which can be a negative to stock valuations and returns.
- The 2nd quarter should provide reasonable insight on what the future holds for our own economy as it will become the “Show Me” quarter for company earnings and economic statistics which should confirm economic stabilization. We are incrementally starting to add to equities as we see growing opportunities for investments in and outside U.S. domestic markets. China has certainly become a major impact in the global economy, and one can see the surge of commodity prices in the first six months of the year. China made the decision to invest heavily in their infrastructure which resulted in increased demand for raw materials and industrial products worldwide..

ABOUT THE INVESTMENT ADVISOR

1st Source Corporation Investment Advisors, Inc., a wholly owned subsidiary of 1st Source Bank. 1st Source has been managing money for its clients since 1936 and currently manages approximately $3.0 billion in assets.

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