MURRAY
INVESTMENT MANAGEMENT

3rd Quarter 2010 Update

Economic Review

The U.S. economy grew a modest 1.7% in the 2nd quarter, which is below long-term potential. The bright spot for 2nd quarter GDP was that business spending on equipment and software was up over 20%; consumer spending rose 2.2%. 3rd quarter GDP will be announced in late October.

In a September release, the National Bureau of Economic Research ("NBER") officially called an end to the recession stating that a "trough in business activity occurred in the U.S. economy in June 2009. The trough marks the end of the recession that began in December 2007 and the beginning of an expansion." The 18 month recession was the longest since the recession that began in August 1929, but we are currently over a year into the new expansion.

During the quarter, the Federal Reserve kept interest rates in the 0% - .25% range but downgraded its economic outlook. In September, the Fed noted that it is "prepared to provide additional accommodation if needed to support the economic recovery and to return inflation, over time, to levels consistent with its mandate." Noting a concern about deflation was a major shift from the very recent discussion of potential inflationary pressures.

The U.S. employment situation has seen very little notable change. With the August unemployment rate at 9.6% and minimal expectations for job growth, a weak jobs picture remains a key stumbling block for an economy that is largely driven by consumer spending.

In addition, the Financial Regulation Bill was passed by Congress during the quarter ushering in sweeping regulations for consumers, banks, insurance companies and others. The long-term impact of this bill is yet to be determined.

Overall, top-line (Revenue) growth was lighter than expected when corporations reported their 2nd quarter earnings. Earnings growth, however, was generally very strong largely driven by cost cutting and increased productivity.

Equity Market Performance

	3Q10	YTD
S&P 500	11.29%	3.89%
MSCI EAFE (International index net return)	16.48%	1.07%

Domestic equity markets (as represented by the S&P 500) were in see-saw mode during the quarter with the tail-end months (July and September) producing very strong performance while August was weak. The strong quarterly performance placed the S&P 500 in positive territory for the year after a tough first half of 2010.

The broad International markets posted very strong results (MSCI EAFE up over 16%) and outperformed U.S. markets during the quarter. Domestic markets have, however, outperformed International for the year. Emerging International markets have been particularly strong this year and during the quarter.

Bond Market Performance

	3Q10	YTD
BarCap US Aggregate Bond (Broad Bond Market)	2.48%	7.94%
BarCap Municipal	3.40%	6.83%
BarCap US Corporate	4.71%	10.77%
BarCap US Corporate High Yield	6.71%	11.53%
BarCap US Treasury Long	5.21%	19.10%

The broad bond market continued to post solid gains while interest rates remain at historically low levels. Interestingly, U.S. High Yield bonds and U.S. Treasuries are among the strongest performers year to date.

Economic Outlook

With the Chairman of the Federal Reserve calling the economic outlook "unusually uncertain," the short-term direction of the economy is very much in question. Many, however, expect that the economy will continue to grow at a moderate pace.

Several factors are currently weighing on the economy:

1) Consumer de-leveraging
2) Government Policy
3) Unemployment

The Consumer de-leveraging (debt reduction) process ultimately leads to increased savings and less consumer spending. With this dynamic, economic growth is somewhat constrained as consumer spending drives so much of our GDP. Since expanding credit (increased debt) fueled consumer spending and faster GDP growth during the first part of this decade, deleveraging will likely do the opposite. This is a necessary part of the process to get the U.S. economy back on a path of long-term sustainable growth. This process could take some time to unfold and will likely lead to below trend economic growth over the next several years. Much like

Sources: bls.gov, Morningstar, BEA.gov, CNBC.com, NBER.org, standardandpoors.com and federalreserve.gov.
The performance data shown represents past performance, which is not a guarantee of future results.
Return data is as of 09/30/2010. Except as noted, index returns are Total Returns.

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consumers, the U.S. government must also face its massive debt problem in the near future.

Also weighing on the economy is the lack of guidance / direction that businesses and consumers are getting from the U.S. Government. Specifically, the direction that the Government will take on taxes and further regulations is leading to a great deal of uncertainty for business owners. Companies are reluctant to hire and invest when they don't know what the future holds on these fronts. Many business owners are taking a wait-and-see approach to hiring and capital spending, both of which painfully slow the economy.

The upcoming November elections will give us more guidance on what to expect regarding taxes and other agenda items that the Obama administration is proposing. Many argue that a more balanced Congress (not dominated by one party) will be a favorable outcome for both the economy and the equity markets.

Joblessness continues to plague the economy, and there's increasing concern about the length that workers are remaining unemployed. The longer people are out of work, the more likely that their skills erode as the dynamics of the marketplace change. The jobs reports released over the next several months will give more clarity on this issue.

As the year progresses, expect to hear increased rhetoric regarding the possibility of additional quantitative easing ("QE2") from the Federal Reserve. The Fed meets again in early November, and its statement could have market moving impact.

Market Outlook

Equity market performance in the 3rd was very strong, but investors should not expect double-digit quarterly performance going forward. Since the rally in the 3rd Quarter was somewhat based on the possibility of additional Fed easing, we have to be cautious about the long-term sustainability of such a rally.

That being said, the broad domestic equity markets appear to be reasonably priced and could have further room to grow. Further market strength will be somewhat dependent upon the sustainability of corporate earnings growth. The guidance that companies provide during the 3rd quarter earnings season will be monitored closely with specific focus on revenue growth expectations.

In the Fixed Income space, there is growing concern that too much money has moved into the bond markets, driving rates down and prices up – specifically in U.S. Treasuries. Short-term rates are at historically low levels with the next significant move likely to be higher. But with inflation subdued and economic growth moderate, it does not appear that rates are heading higher in the short term.

Texas Monthly Magazine

For the second year in a row, Sam Murray was named a Five Star Wealth Manager by Texas Monthly Magazine for overall satisfaction. This distinction was awarded to less than 2 percent of the wealth managers in the Houston area.

Murray Investment Management

If you would like help with establishing an investment plan or would like to schedule a portfolio review, please give us a call. Also, please pass along our name to anyone that may be in need of investment advice.

Sources: bls.gov, Morningstar, BEA.gov, CNBC.com, NBER.org, standardandpoors.com and federalreserve.gov.
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