Monthly Investment Update

First National Bank
Investment Management & Trust

October 2009

Highlights

September has historically been the worst performing month in the stock market, but a correction did not occur in 2009.[1] Equity returns continued their upward move with the riskier asset classes (small cap & international) outperforming large capitalization stocks. The global economy continues to show additional signs that the recession is ending. Over the last month, economists have increased their second half GDP forecast from 2.1% to 2.7% in the U.S.[2] Fixed income returns were also positive in September, especially corporate and municipal bonds. Commodities also participated in the rally with gold reaching an all time high on October 8th of $1,056 per 100 ounce.[3]

1. Brown Brothers Harriman, 2. Bloomberg, 3. Bloomberg

Asset Class	Index	9/30/09	Total Return 1 Month	Total Return 3 Month	Total Return YTD	Total Return 1 Year
Domestic Equities	Dow Jones Industrial Average	9,712	2.43%	15.82%	13.49%	-7.37%
	S&P 500	1,057	3.73%	15.61%	19.26%	-6.91%
	S&P 400 Mid-Cap	691	5.72%	19.98%	30.14%	-3.11%
	Russell 2000	604	5.77%	19.28%	22.42%	-9.52%
International Equities	EAFE Index	1,553	3.85%	19.55%	29.23%	3.48%
Fixed Income	Barclays Capital Intermediate Gov/Cr	-	0.85%	3.25%	4.92%	10.01%
	Barclays Capital7 Yr Muni	-	2.30%	5.10%	8.31%	12.51%

Source: Bloomberg

Market Update

Equities:

The momentum in the stock market was broad based in September with small caps reporting the strongest returns (Russell 2000 Index up 5.8%). The small cap performance was closely followed by mid caps, which returned 5.7% for the month and is now up over 30% year-to-date. In addition to resumption of economic growth, earnings revisions continue to be positive and supported stock market gains. According to ISI, the First Call Earnings Revisions Index moved to another new high of 67% in early October. This increase is typically a good omen for third quarter earnings reports. On a sector basis, all ten major industries were positive in September with economic sensitive industries leading the market. Particularly strong returns were reported in industrials, consumer discretionary and basic materials. Utilities and health care, which are typically classified as defensive areas, lagged the market advance.

Source of Data: Bloomberg

Fixed Income:

Bonds also reported positive performance in September. On the taxable side, corporate and high yield bonds led the market. For the month, investment grade corporate bonds were up 1.8% and high yield bonds were up 5.7%. U.S. government bond returns were also positive in September, 0.7%. Year-to-date returns for 2009 are the exact opposite of 2008 with corporate bonds significantly outperforming government bonds. Overall, the Barclay's Capital U.S. Intermediate Government Credit Index is up 4.9% so far in 2009. Future fixed income returns may be more subdued as the current yield of this index is 2.7%. In the tax-exempt market, municipal bonds were strong this month. Year-to-date returns are now 8.3% for the Barclays Capital 7 Year Municipal Bond Index. Similar to the taxable fixed income market, yields are fairly low with the current yield on this index also 2.7%

Source of Data: Barclay's Capital

Bottom Line

As a result of the improvement in the global economy and high level of productivity gains from cost cutting, companies have been reporting better than expected earnings. This trend is expected to continue in the 3rd quarter. Equities have been responding positively to the surprise in earnings. Future stock market gains are tied to the continuation of economic growth and better sales trends. There are several risks to the sustainability of the economy. The first is the high level of unemployment. For a sustainable economic recovery, we need to see job creation. Although initial unemployment claims are trending down, we have not seen net job creation. Second, the credit problems in the banking industry continue, especially with commercial real estate loans. The tight credit condition may be an impediment to sustainable economic growth.

Investment Team

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*These individuals make up Tributary Capital Management. Tributary Capital Management provides sub-investment advisory services to Investment Management & Trust clients.