Several of the concerns expressed in our June note are being realized sooner than even we expected. Along with the S&P downgrade of U.S. debt and the violent fluctuations of equity markets, we thought further comment was warranted. Put simply, we are more negative today than even one month ago. Financial markets are given to overreaction, but the problems we face are very real.

In order of importance to near term market direction we would identify the following:

- The economy
- European sovereign debt problems; and
- The implications of the U.S. debt downgrade

<u>The Economy</u>

The recent downward revisions to previously reported U.S. GDP were, to say the least, stunning. Combine that with the continuing low growth of employment, and the need to cut spending to deal with the debt and budget deficit make the chances of a new recession in the next 12 – 18 months more probable.

<u>Europe</u>

Solving the issues in Europe, within the context of the current Common Market structure, is hard to imagine. A system that attempts to have one monetary policy but diverse fiscal policies seems doomed to failure.

<u>U.S. Downgrade</u>

While the downgrade of U.S. debt has somewhat modest near term implications, the longer term effects on the interest costs at all levels of governments and who will continue to purchase U.S. notes and bonds are not to be ignored. It is a strange world, in our view, that reacts to the U.S. downgrade by buying more Treasuries.

The current stalemate in Washington, lack of leadership and refusal to deal with the longer term budget and debt issues give us grave concern.

<u>Summary</u>

With a more negative view on the market and expectations of increased volatility, we have increased the level of writing covered calls and purchasing protective puts which we believe will mitigate downside somewhat against weaker markets.