

Capital Markets Commentary

1st Quarter 2009



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After a viciously painful 2008, the stock market continued its decline in the first months of 2009. After a poor January, the market sold off dramatically in February as investors lacked conviction that new Treasury Secretary Timothy Geitner would harness an effective and well-coordinated plan to help find a way out of this mess. By early March, the market had declined another 25%, on top of a nearly 40% decline in 2008. Then the bedeviled bounced off of the 666 level on the S&P 500 Index and rallied strongly in the last several weeks of the quarter, making March one of the strongest months in recent history. This can be seen in the chart below, which shows the S&P 500 during the first three months of 2009 (source: bigcharts.com). Still, stocks returned -11.7% in the first quarter, as measured by the S&P 500. The NASDAQ composite returned -3.1% in the first quarter, performing much better than the S&P 500 and the Dow Jones Industrial Average (DJIA) return of -13.3%. The current string of losses marks the longest consecutive string of quarterly declines in the stock market since it declined for six consecutive quarters in 1969-1970.

In a historically significant moment, Barack Obama was sworn into office in January. The inauguration was one of the most widely viewed in history, and Mr. Obama entered the White House with one of the highest approval ratings of a newly elected president since Ronald Reagan took office in 1980. However, on this historic day the market dropped by 4%, the biggest decline ever on Inauguration Day. According to the Wall St. Journal, President Obama took office during the worst first quarter performance in the DJIA since 1939, and the worst under a new president in 90 years.

Of the 30 components in the DJIA, only three were able to post a gain in the first quarter: IBM (up 15%), Intel and Home Depot (up about 2% each). On the other hand, the worst performing components were both financial companies, Citigroup (down 62%) and Bank of America (down 51%). The two "generals" in the DJIA were also very weak performers, GE and GM each down more than 35% in the first quarter. Concerns over the potential breadth and depth of difficulties in the financing arm of GE led to a significant decline, and GM's sales continued to lag and the company looked to the U.S. Government once more for additional support to avert a bankruptcy filing. As a result, GE's CEO was dropped from Barron's list of most admired CEO's, and GM's CEO was asked by government officials to immediately step down in March 2009. He complied with the request, based on a statement issued by General Motors.



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Market Sector Performance

From a sector performance standpoint, Technology, Materials and Telecom were the three best performing S&P sectors. The poorest performing sector was Financials, down nearly 30%. Financials continued to face investor uncertainty over the potentially ineffective government-backed programs and looming toxic assets, which made it very difficult to develop a positive investment thesis for purchasing equity of many financial institutions. Other sectors also performing poorly in the first quarter included industrials and energy.

Top performing industries on a year-to-date basis through March 31, 2009 included Wireless, Internet/Catalog Retail, Internet Software & Services, Communication Equipment and Computers & Peripherals, each up at least 8% for the first quarter. Bottom performing industries included Commercial Banks, Office Equipment, Consumer Finance, Building Materials, and REITs, each losing 30% or more during the first three months of 2009.

Russell Index Performance

The first quarter of 2009 was yet another quarter that was marked by negative returns, based on the Russell 1000, Russell Mid Cap, and Russell 2000 indices, as well as their Value and Growth counterparts. Small Cap Value equities experienced the quarter's largest losses, down nearly 20%. On the other hand, Mid Cap Growth stocks experienced a loss of just 3.4% in the quarter.

Along the Value/Growth axis, growth stock performance was much better than value-based investing in the first quarter, as technology and growth-oriented companies were among the first to turn around. In Q1, from a capitalization standpoint, Mid Cap stocks fared slightly better than Large Cap and did significantly better than Small Cap equities. *(source: Russell Investments)*

Sector Performance Table	Q1-2009	2008
Information Technology	4.0%	-43.7%
Materials	-2.8%	-47.1%
Health Care	-8.5%	-24.5%
Telecommunications	-8.5%	-33.6%
Consumer Discretionary	-8.6%	-34.7%
Consumer Staples	-11.3%	-17.7%
S&P 500 Index	-11.7%	-37.0%
Utilities	-11.9%	-31.6%
Energy	-12.1%	-35.9%
Industrials	-21.8%	-41.5%
Financials	-29.5%	-56.9%

(source: Standard & Poor's)

Q1 Russell U.S. Equity Returns (%)

	Value	Blend	Growth
Large Cap	-16.8	-10.5	-4.1
Mid Cap	-14.7	-9.0	-3.4
Small Cap	-19.6	-14.9	-9.7

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Domestic Economy

The U.S. economy continued to languish in the first quarter of 2009. Job losses continued to mount, and late in March ADP, who provides payroll processing to roughly one out of every six workers in the U.S., reported that 742,000 private sector jobs were lost. This was the worst figure in the nine-year history of the ADP jobs report. On a macroeconomic basis, according to the U.S. Bureau of Labor Statistics, the national unemployment rate stood at 8.1% in February 2009. There were several states in the Union that reported more than 10% unemployment, including California, Michigan and Nevada. States with relatively lower unemployment rates of 5% or lower were Wyoming, Nebraska, Iowa and The Dakotas.

U.S. Fixed Income Markets

The U.S. fixed income market stabilized somewhat during the first quarter of 2009, following the very rocky last three and one-half months of 2008 after the bankruptcy of Lehman Bros. The yield curve remained positively sloped and actually steepened in the first quarter, with short rates still at their lowest level in generations. The yield on the 10-year Treasury note stood at 2.73% on March 31, 2009 an increase from the 2.07% level at the beginning of 2009.

The U.S. high yield market had a good bounce in the first quarter, and gained approximately 5% in the quarter after declining by more than 25% in 2008. Some fixed income investors sought bargains in the high yield market after spreads widened to all-time high levels in late 2008.

The Federal Reserve Board kept interest rates unchanged during their two meetings that took place during the first quarter. The target Fed Funds rate remains at the range of zero to 0.25%. In the press release dated March 18, 2009, the Fed indicated that:

“In these circumstances, the Federal Reserve will employ all available tools to promote economic recovery and to preserve price stability. The Committee will maintain the target range for the federal funds rate at 0 to 1/4 percent and anticipates that economic conditions are likely to warrant exceptionally low levels of the federal funds rate for an extended period. To provide greater support to mortgage lending and housing markets, the Committee decided today to increase the size of the Federal Reserve’s balance sheet further by purchasing up to an additional \$750 billion of agency mortgage-backed securities, bringing its total purchases of these securities to up to \$1.25 trillion this year, and to increase its purchases of agency debt this year by up to \$100 billion to a total of up to \$200 billion.” (source: Federal Reserve Board)

It seems as though the Federal Reserve was one of the only major institutional investors to have an appetite for risky securities and a willingness to house a deteriorating balance sheet.

International Equities

The MSCI EAFE Index declined by 13.9% in the first quarter. The global economic slowdown manifested itself in many countries with declining asset values and anemic economic growth, increasing unemployment, and a cloudy outlook for future prospects. The EAFE Growth Index returned -12.3%, outperforming its counterpart EAFE Value, which returned -15.5%. Looking at U.S. dollar-based performance of particular developed countries, the best performing foreign stock markets in the first quarter were Norway, Hong Kong, Sweden and Canada. Performance was the worst in Spain, Germany, Italy and Finland. Incidentally, the U.S. was near the middle of the group. Observing dollar-based returns in emerging stock markets, the best quarterly performance was in Chile, Brazil, Russia and Taiwan, each up 8% or more. On the contrary, performance lagged in Mexico, Argentina and Hungary, down 14% or more as measured in U.S. dollars.

Currency Rates

Despite the potentially inflationary monetary policy being employed as part of the massive government-led bailout and stimulus package, the dollar rallied versus major foreign currencies in the first quarter. Global investors showed a desire to hold U.S. Dollars over the Euro and the Japanese Yen.

At the end of the first quarter, the dollar was worth just less than 100 Japanese Yen, up from a level of about 90 Yen at the end of 2008. In terms of the Euro, it took \$1.34 to buy 1 Euro at the end of the first quarter, down from approximately \$1.40 at the end of 2008. There was less relative movement in the U.S. dollar versus the Pound Sterling and the Canadian Dollar. The British Pound was worth \$1.47 at the end of the first quarter of 2009, up slightly from \$1.45 at the end of 2008. The Canadian dollar was relatively unchanged from its level at the beginning of the year at approximately \$0.80 USD. However during the latter part of March the dollar declined as talk of a concerted decision by major central banks to hold other currencies over the greenback spooked investors and caused dollars to be sold in favor of other mainstream currencies.

Real Estate

The trend of declining residential real estate prices continued in the first quarter, as foreclosure rates have continued to be above historical levels and the overabundance of inventory of unsold homes is challenging the balance of supply and demand. According to the S&P/Case-Shiller Home Price Index, based on 12-month performance data through January 2009, the worst three major metropolitan areas were Phoenix, Las Vegas and San Francisco, each of which declined more than 30%. On a positive note, the best relative performance over the same timeframe were the real estate markets in Dallas, Denver and Cleveland, each down approximately 5%.

To quote from the S&P press release dated March 31, 2009, "Home prices, which peaked in mid-2006, continued their decline in 2009. There are very few bright spots that one can see in the data. Most of the nation appears to remain on a downward path, with all of the 20 metro areas reporting annual declines, and nine of the [metro areas] falling more than 20% in the last year."

Oil and Commodities

The price of a troy ounce of gold reached \$1,000 during the first quarter, as investors sought its safe haven amidst turmoil in many capital markets. The spot price of gold ended the quarter at approximately \$915, as there was some erosion in the degree of fear and uncertainty in other capital markets. Crude oil, after dipping below \$35 per barrel a few weeks before New Year, climbed back above the \$50/barrel level in March 2009. Still, it remains significantly below the lofty levels experienced last summer, when a barrel of West Texas Intermediate Crude fetched more than \$140.

Commodity prices, as measured by the Reuters/Jeffries CRB index of 19 commodities, fell 6.3% during the first quarter. Biggest declines were experienced in natural gas, nickel and wheat, whereas the largest gains were in gasoline, copper and hogs. Global demand collapsed in Japan, Europe and of course the U.S., and, according to Bloomberg, aggregate global growth may decline for the first time since World War II.

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Index Returns Since 2000, Sorted From Best to Worst

INDEX	ASSET CLASS	2000	2001	2002	2003	2004	2005	2006	2007	2008	YTD
Russell 1000 Value	Large Value	22.8%	14.0%	10.3%	48.5%	23.7%	14.0%	26.9%	11.8%	5.2%	5.3%
Russell 1000	Large Blend	19.2%	8.4%	1.7%	47.3%	22.3%	12.7%	23.5%	11.6%	1.8%	0.1%
Russell 1000 Growth	Large Growth	11.6%	4.5%	-1.9%	46.0%	20.7%	12.7%	22.3%	11.4%	-20.7%	0.0%
Russell Midcap Value	Mid Value	8.3%	4.1%	-9.2%	42.7%	20.2%	12.1%	20.7%	9.6%	-26.2%	-3.4%
Russell Midcap	Mid Blend	7.0%	2.5%	-9.6%	40.1%	18.3%	10.0%	20.2%	7.1%	-28.9%	-4.1%
Russell Midcap Growth	Mid Growth	6.0%	2.3%	-11.4%	39.2%	16.5%	7.1%	18.4%	7.0%	-33.8%	-5.8%
Russell 2000 Value	Small Value	-1.2%	-3.7%	-15.5%	38.1%	15.5%	6.3%	15.5%	6.1%	-36.9%	-9.0%
Russell 2000	Small Blend	-3.0%	-5.6%	-15.7%	33.8%	15.3%	5.3%	15.3%	5.8%	-37.6%	-9.7%
Russell 2000 Growth	Small Growth	-5.1%	-5.6%	-16.2%	30.0%	14.3%	4.7%	13.4%	5.6%	-38.4%	-10.5%
MSCI World Index	Global Eq.	-7.8%	-9.2%	-19.5%	29.9%	11.4%	4.5%	11.8%	4.7%	-38.4%	-11.8%
MSCI EAFE Index	Int'l Equity	-11.8%	-12.5%	-20.5%	29.8%	10.9%	4.2%	11.2%	2.2%	-38.5%	-13.9%
Barclays Aggregate Bond Index	Intermed. Bond	-12.9%	-16.5%	-21.7%	28.2%	8.3%	3.9%	10.7%	-0.2%	-40.3%	-14.9%
Merrill Lynch High Yield Index	High Yield Bond	-14.0%	-20.2%	-27.4%	19.3%	6.3%	3.0%	9.1%	-1.4%	-41.5%	-14.9%
Balanced (60/40)-Rebal. Yearly	Balanced	-22.4%	-20.4%	-27.9%	4.1%	4.3%	2.7%	4.8%	-1.6%	-43.1%	-16.8%
Citigroup 3-month T-bill	Cash Equiv.	-22.4%	-21.2%	-30.3%	1.1%	1.2%	2.4%	4.3%	-9.8%	-44.3%	-19.6%

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