



EAGLE GLOBAL ADVISORS

MARKET REVIEW AND OUTLOOK —2ND QUARTER 2010

MARKET OVERVIEW

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Equity markets declined sharply in the quarter on concerns that the world economic expansion is faltering. In the U.S., the S&P 500 declined 11.4% for the quarter, bringing the year-to-date return into negative territory, down 6.7%. Equity markets outside of the U.S. also performed poorly and were additionally hurt by weakness in foreign currencies. The MSCI EAFE index delivered a negative 14.0% total return for the quarter, bringing its year-to-date return to negative 13.2%. Interest rates fell sharply during the quarter leading to positive returns for fixed income instruments.

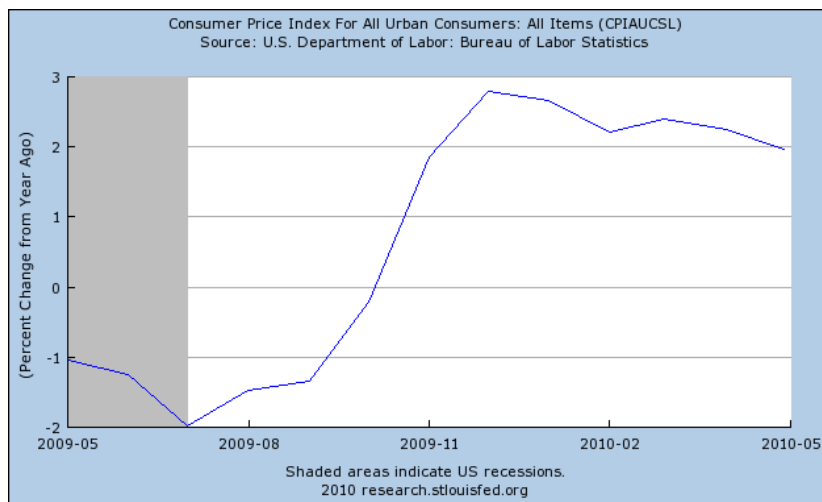
ECONOMY *A PAUSE THAT REFRESHES OR SIGNS OF A “DOUBLE DIP”?*

The 2.7% GDP growth for the first quarter of 2010 presented a sharp slowdown from the 5.6% growth rate of the prior quarter. Retail sales, housing purchases, industrial investment and other economic data reported during the quarter generally showed positive numbers but confirmed a slowing of the rate of growth of economic activity. These signs of slowing have prompted much concern about whether the economy might be sliding into another recession, the dreaded “double dip”. Alternatively, some see these statistics as evidence of a normal slowing of the rate of growth following a sharp rebound from the bottom of an economic cycle. Our view tends towards the latter perspective; at the current time we believe that the U.S. economy has merely slowed its rate of growth and we do not currently see the danger signs of a recession. Some of the positive indicators that we follow show that the economy is still in expansion mode: 1) a steeply positive interest rate yield curve, 2) positive consumer sentiment, 3) expanding workforce and hours of employment, 4) steady commodity prices, and 5) positive purchasing manager surveys.

Bears on the economy argue that the expansion so far has depended on government stimulus and that as this stimulus is being withdrawn the economy will fall back into recession. They further argue that the usual drivers of an economic rebound will peter out this time around. Housing, which is usually strong out of a recession, looks relatively weak since the economy is still working off excess inventory built during the housing boom. Non-residential construction and autos, while they have rebounded from their lows, also look less robust than prior rebounds. However, consumer spending has proved to be more resilient than many had expected, and improvements in the job market should help to continue that trend. Also, capital spending is starting to pick up, and while we do not expect that it will be as robust as in prior rebounds, backlogs in some industries and deferred maintenance should underpin further capital expenditure. Also the U.S. is experiencing a very strong upturn in export growth powered by demand from the newly developing emerging markets. All in all, we expect the U.S. economy to expand at a 2% to 3% rate for the rest of this year.

INFLATION *INFLATIONARY PRESSURES ARE WANING.*

Inflation continues to be low, and inflationary pressures look to be waning. The latest statistics showed the Consumer Price Index actually falling in April and May. In May, the CPI was only 2.0% higher than a year ago, and the core inflation rate (excluding food and energy) increased at a more muted 0.9% rate in that time period. The Producer Price Index for finished goods also showed moderation in the past three months, and is still relatively low. Low capacity utilization (74%) and high unemployment (9.5%) indicate considerable slack in the economy which should put downward



pressure on prices and wages. The Federal Reserve Open Market Committee asserted in its June statement that “with substantial resource slack continuing to restrain cost pressures and longer-term inflation expectations stable, inflation is likely to remain subdued for some time.”

CORPORATE PROFITS *PROFITS ARE REBOUNDED.*

Earnings in the second quarter of 2010 are expected to be up about 16% from the depressed level of last year, with the greatest contributions to growth coming from the Materials, Information Technology, and Energy sectors. In contrast, Telecom Services, Utilities, and Consumer Staples are expected to post flat to modestly up earnings this quarter versus the same period a year ago. For the full year, Starmine expects that the S&P 500 will post \$82.17 per share earnings, up about 32% from last year. (Starmine’s estimate comes from aggregating what individual analysts expect the companies in the S&P 500 to earn in this period.) With the S&P 500 at 1,060 as of this writing, that puts the market at 12.9 times expected earnings for this calendar year. Financials are expected to see the biggest rebound in 2010, followed by Materials and Energy. In contrast, Telecom Services, Utilities and Consumer Staples are expected to have the more modest earnings growth.

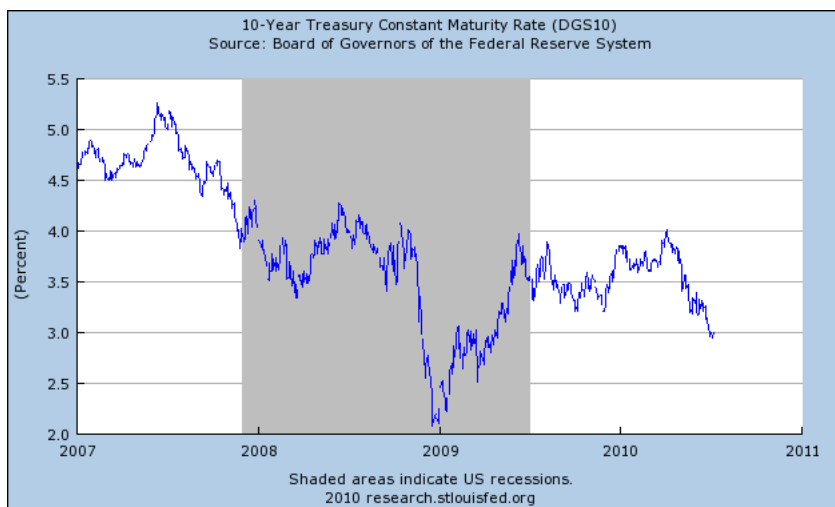
INTEREST RATES *LONG TREASURY RATES FELL, SHARPLY.*

Short rates stayed extraordinarily low in the quarter while long rates fell on concerns about the economy. The Federal Reserve Board continues to take extraordinary steps to keep interest rates and credit spreads low. The Fed maintains a target range for the federal funds rate of 0.0% to 0.25% and continues to employ a number of unprecedented measures to keep the financial system liquid, although these measures are starting to be removed. While many expected longer rates to rise from their historically low levels, the big surprise of the quarter was the sharp fall in long rates. From 3.8% at the beginning of the quarter, the 10-year Treasury bond yield fell to 3.0% at the end of the quarter, and has dipped below 3% at times.

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INTEREST RATES

Still, with short rates so low, the yield curve (as measured by the difference between fed funds rate and the 10-year Treasury) is relatively steep and is consistent with continued economic rebound.



INTERNATIONAL *SIGNS OF REBOUND IN THE WORLD ECONOMY.*

Current indications are that most major economies of the world are in rebound mode propelled in large part by the upturn in the U.S. and strong growth in the Emerging Markets. However, the focus since April has been about the possibility of things going wrong with the world economic recovery. Developments raising concerns about future economic conditions include: 1) a rising chorus of calls for fiscal restraint in Europe, Japan, and the U.S., 2) a Chinese economic slowdown, 3) stress in the eurozone banking system, 4) concerns over sovereign debts, and 5) indications of a slowing rate of growth. While it was expected that a number of countries facing sovereign debt issues like Greece, Ireland, and Spain would tighten their belts with lower government spending and higher taxes, the fiscal austerity bug has also been caught in countries not immediately affected by the debt crisis like the U.K., Germany, Japan, and the U.S. In the U.K., a coalition government took power after a parliamentary election ousted the Labour Party; the first order of business for the new government was to present a very austere budget proposing cuts to a wide range of social services. Likewise Germany is considering an austere government budget, and the ruling party in Japan is campaigning on a platform of fiscal restraint in a run up to elections this summer. Combined with political forces in the U.S. stalemating any additional stimulus here, this adds up to a global movement to fiscal restraint at a time when the world economy is still recovering from the financial crisis. Additionally, the Chinese government has intensified its measures to slow property speculation and construction, which is having a significant impact on that sector of their economy.

INVESTMENT STRATEGY

DOMESTIC EQUITY *U.S. EQUITIES SELL OFF SHARPLY.*

U.S. stocks exhibited poor returns in the second quarter, more than wiping out the gains from the first quarter on concerns of a weakening economy. Declines were most pronounced in the Materials, Financials, Industrials, and Information Technology sectors while the Consumer Staples, Utilities, and Telecom Services sectors relatively outperformed. Eagle portfolios slightly underperformed the market averages; our portfolios benefitted from an overweight to Consumer Staples and an underweight to Financials as well as higher cash holdings than usual; however, poor stock performance in the Information Technology and Industrial sectors

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DOMESTIC EQUITY *CONTINUED*

outweighed good stock selection in the Materials and Financial sectors. Many multinationals that we own have seen their earnings downgraded due to the strength in the dollar. As foreign currencies have fallen, the profits that these multinationals earn overseas diminish less when translated into dollars. Over time we believe there are many macroeconomic factors that should lead to a weaker dollar, and that this currency head wind should turn into a tail wind for these multinationals at some point. During the quarter we increased our cash balances and our holdings in the Material and Consumer Discretionary sectors while we reduced our exposure to the Financial, Industrial, and Health Care sectors. Top performing stocks for the quarter include: Hasbro, Temple Inland, General Mills, and Kansas City Southern. Disappointments for the quarter include: Ebay, Manitowoc, JC Penny, and Microsoft. Most recent purchases/adds: Apple, Bank of America, Cleveland Cliffs, Hanesbrands, Occidental Petroleum, and V F Corp. Most recent sales/trims: Annaly Capital, Delta Airlines, Everest Re, Flextronics, MDC Holdings, Sandridge Energy, Seagate, and Zimmer Holdings.

INTERNATIONAL EQUITY *INTERNATIONAL EQUITIES ALSO SLIDE.*

International equities also had a poor quarter compounded by weakness in the euro and other currencies relative to the dollar. Our portfolios were relatively well positioned in the quarter with their sector and country exposures; unfortunately some specific stock picks undermined our performance. For the quarter, defensive sectors like Consumer Staples and Health Care outperformed; we were overweight these sectors and our stock selection also benefitted the portfolio. Our portfolio was also helped by our exposure to Emerging Markets and our underweight to Financials; unfortunately our stock exposures in these sectors were more sensitive to cyclical factors and as sentiment soured on the world economic cycle, our holdings underperformed. Our belief is that the current scare on world growth is overdone; we do not subscribe to the “double dip” scenario at this time, and we look for markets to reflect this as time goes by. Top performing stocks for the quarter include: AstraZeneca, Bank of China (Hong Kong), Nestle, and Keppel. Disappointments for the quarter include: ArcelorMittal, Central European Distribution Corp, Mitsui & Co, and Societe Generale. Most recent purchases/adds: BNP Paribas, Canon, Focus Media, Nidec, and Volvo. Most recent sales/trims: Banco Santander, National Bank of Greece, Rio Tinto, Sterlite, and Tenaris.

FIXED INCOME *INFLATION CONCERNS FADE AND BONDS RALLY.*

Long-term interest rates, as measured by the 10-year Treasury, ended the quarter sharply lower than where they began, at 3.0% down from 3.8% at the end of March. Expansive policy by the Fed maintained short-term rates at exceptionally low levels. While corporate bond spreads widened as concerns about credit quality rose, overall rates were down in sympathy with Treasury rates. We remain concerned that as the U.S. economy continues to expand while the financing needs of the government are increasing that rates on bonds will ultimately rise. Therefore we are maintaining a relatively short duration in our bond portfolios and emphasizing exposure to high quality corporates. Municipal bond yields are still attractive relative to U.S. Treasury yields and also represent value.