



HANLON
INVESTMENT MANAGEMENT, INC.

Market Commentary

February 20, 2008

The type of market action that we have been experiencing of late, where rallies are short lived and reversals tend to come intra-day, is indicative of a bear market. There is an unquestionable level of uncertainty that investors have in the current market environment. Rallies don't last very long because investors are looking for selling opportunities. Most market indices are off their mid-January lows, but the inability of the market to mount a stronger countertrend rally from such an oversold level raises questions about what may happen when the next shoe drops in the ongoing credit saga. And there will be another shoe to drop.

Two new reports released this morning, CPI and housing starts, continue to show the challenges facing the Fed. Leading Indicators and unemployment claims will be released tomorrow. The CPI showed that inflation remains a concern, which is a negative for "paper assets" such as stocks, while the housing economy remains depressed. Commodity prices are skyrocketing as witnessed yesterday when oil closed above "par" (\$100 per barrel) for the first time ever. While the market would like the Fed to continue lowering interest rates, the possibility of a recession now appears to be the primary concern of most investors, giving less influence to what the Fed does. I believe and our research has uncovered that we are already in a recession. Many investors are convinced that the economy has just slowed and will avoid a deep or protracted recession. If new data indicates a significantly increased chance of a recession, another wave of investors will sell stocks and move to the sidelines.

Every time the stock market drops, many market pundits have continued to recommend that investors buy, buy, buy. I don't know what they are supposed to *buy with* since those same pundits never said to sell when the market started to decline last October. If the major indices drop below the January lows (or the February lows in the case of the NASDAQ indices), some investors who have held throughout this bear market downtrend so far will be reminded of the last recession and decide to limit their losses. The S&P 500 Index would have to gain 17%+ just to get back to where it was at the market top in October 2007.

Stock market technicals continue to be weak. All the major domestic and international stock indices are trading below standard measures of moving averages (20 day, 50 day, 100 day, and 200 day). Market breadth is also weak, with the advance - decline lines showing no strength and the up volume versus down volume measurements flat to down. New 52 week highs are relatively non-existent. Technically and breadth wise this market is in poor health and cautious investing is best.

From a valuation perspective there is wide spread belief that the S&P 500 Index companies will only earn about \$70.00 in 2008, down from a previously forecasted approximately \$97.00. If that is the case then the S&P 500 Index is currently trading at a "forward" P/E ratio of 19+, derived by dividing the current S&P 500 Index price of 1,350 by \$70.00. 19 is not the type of P/E ratio that starts a new bull market.

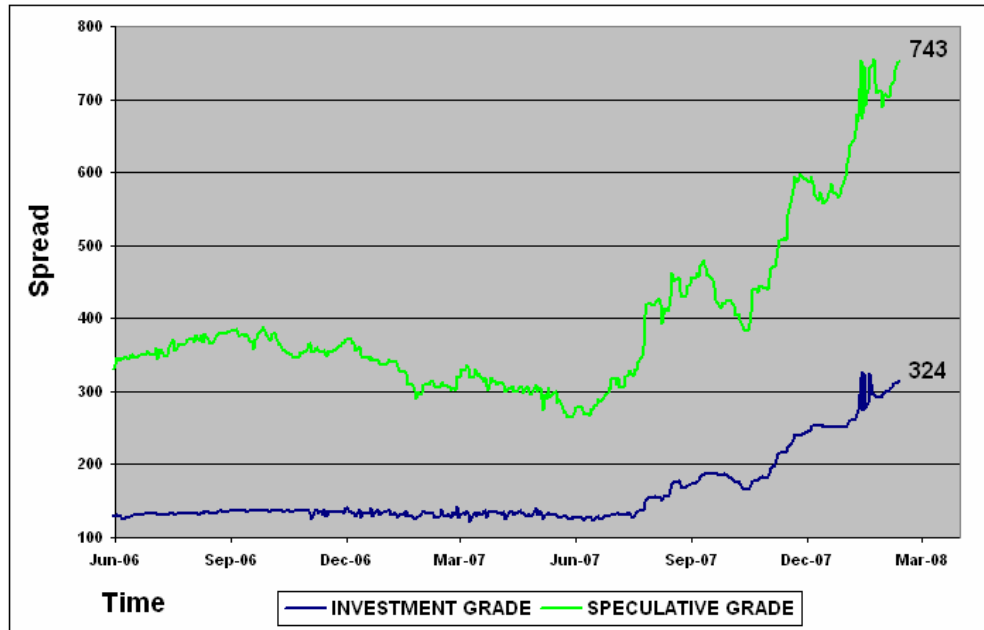
Risk control is essential in bear markets. I don't know when this bear market will end or how much more stocks will drop (if any) before a new bull market develops, but I am confident that we will be able to pick up on the change in the market environment shortly after the bottom develops. In the current environment, avoiding any sharp sell-offs is more important than catching the initial up-leg of a new uptrend.

With respect to high yield bonds, the chart below tells the story. Clearly one can see that the market is anticipating considerable increases in defaults as interest rate spreads have risen to 743 bps when comparing rates on high yield bonds as compared to high quality (US Gov't) bonds of similar duration.



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Bond spreads are created utilizing data from the Merrill Lynch website. The Investment Grade Spread represents the US Corp 7-10 Yr minus the US Treasury Master. The Speculative Grade Spread represents the US High Yield Master minus the US Treasury Master. They cannot be invested in directly without incurring costs and fees. This is not a recommendation for investment. Hanlon Investment Management, Inc. ("HIM") is an SEC registered investment adviser with its principal place of business in the State of New Jersey. Hanlon and its representatives are in compliance with the current registration requirements imposed upon registered investment advisers by those states in which Hanlon maintains clients. HIM may only transact business in those states in which it is registered, or qualifies for an exemption or exclusion from notice filing requirements. For information pertaining to the registration status of HIM, please contact HIM or refer to the Investment Adviser Public Disclosure website, www.adviserinfo.sec.gov.

Sooner or later there will be a very good investment opportunity. There is potential, making absolutely no guarantees or projections here now, that we will ultimately be presented with an environment that results in 20-30% up moves in both stocks and high yield bonds. That is typical of the action that occurs after a significant drop in stocks and high yields. We are monitoring and hopeful that moment is not far off, but in the meantime money markets look real good, for now.

Thank you,

Sean Hanlon, CFP®
CEO and CIO

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