Market Update

Evergreen Investments™

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In This Issue:

- Market Performance
- U.S. Economy
- Federal Reserve

Market Performance

Equities continued to struggle last month, as the Dow Jones Industrial Average and the S&P 500 Index experienced their worst January performance ever. Investors were constantly bombarded with negative news relative to the recession and its impact on corporate profitability. In addition, confidence was further weakened by what at times appeared to be a dithering policy response to the financial crisis from Washington. Equities of all sizes and shapes were punished, with the largest losses experienced in the small cap and values indexes. International markets were also hit hard as economies in both developed and emerging countries remained weak. In the fixed income markets, high yield bonds have bounced off the extreme weakness experienced last year and municipal securities climbed higher. Concerns over increased issuance sent Treasury yields up for the month. Oil pulled back on concerns of global weakness while gold and the dollar rose. See Chart 1 for more details of Market Performance.

U.S. Economy

Economic reports continue to suggest a severe recession. While fourth quarter Real GDP declined by a less than expected -3.8%, the worst reading in 26 years, a surprising build-up in inventories masked some of the weakness. Excluding the stocking of shelves, the economy contracted by -5.1% for the period ending in December. The weakness was broad-based, as personal consumption declined in excess of -3.0% for the second consecutive quarter, and business investment on equipment and software plunged at an annual rate of -28%, the worst pullback in 50 years! Exports, which had boosted growth over the past year, declined at nearly a 20% annual rate, as trade was punished by the combination of a stronger dollar and weaker global demand. Government spending was the only input that contributed positively to output, rising +1.9% last quarter.

Unfortunately, the data for this quarter do not look much better. Layoff announcements have accelerated in recent weeks, further pressuring personal consumption and business investment. Moreover, the housing market continues to struggle, with new home sales falling to a record-low last month and sales of existing homes hovering at the lowest levels in more than ten years. The S&P Case Schiller Home Price Index of the 20 largest metropolitan areas also shows a record decline of -18.2% over the past twelve months. See Chart 2.

We continue to believe that the current period (fourth quarter of 2008 and the first quarter of 2009) will prove to be the worst part of the recession. The credit freeze following the collapse of Lehman Brothers last fall has begun to show signs of a thaw, as interbank lending rates have improved dramatically. Yet the real key will be the willingness of banks to lend to consumers and businesses in the coming months. It is our hope that the combination of the steep yield curve

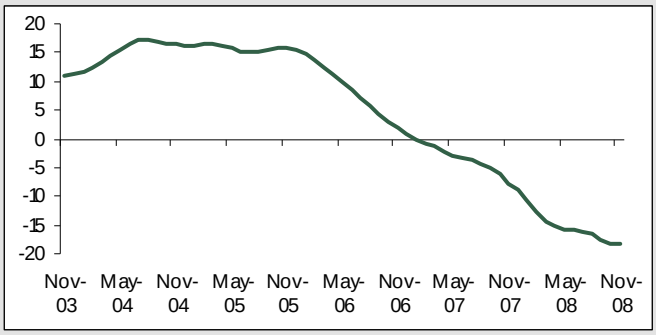
1. Market Performance as of 1/30/09

EQUITIES	1/30/09 LEVEL	January TOTAL RETURN	2008 TOTAL RETURN
Dow Jones Industrials	8,000.86	-8.6	-31.9
S&P 500	825.88	-8.4	-37.0
NASDAQ	1,476.42	-6.4	-40.5
Russell 2000	443.53	-11.1	-33.8
S&P MidCap	498.68	-7.3	-36.2
Russell 1000 Growth	353.11	-4.8	-38.4
Russell 1000 Value	430.08	-11.5	-36.8
MSCI EAFE	1,115.14	-9.8	-43.4
MSCI (Emerging Markets)	529.53	-6.5	-53.3
FIXED INCOME	**1/30/09 YIELD**	**January TOTAL RETURN**	**2008 TOTAL RETURN**
10-Year Treasury	2.84	-4.6	20.1
Lehman Aggregate	4.31	-0.9	5.2
Lehman Municipal	4.02	3.7	-2.5
Lehman Corporate	7.29	0.5	-4.9
Lehman High Yield	17.88	6.0	-26.2
Lehman Mortgage	4.07	0.2	8.3
Lehman Global ex. US	2.33	-4.6	9.4
COMMODITIES & CURRENCIES	**1/30/09 LEVEL**	**January TOTAL RETURN**	**2008 TOTAL RETURN**
CRB Index	220.37	-4.0	-40.0
Crude Oil - WTI	41.68	-6.5	-53.5
Gold	928.40	5.0	5.9
Trade Weighted Dollar	86.46	5.2	7.1

Source: Factset, Bloomberg, Lehman Brothers, Evergreen Investments.
*Total Return includes price appreciation & dividend income for equities.

Past performance is not indicative of future results. It is not possible to invest directly in an index.

2. Case Schiller Home Price Index - Y/Y % Change



Source: Baseline

(enabling banks to borrow-short and lend-long on a profitable basis) and the policy response out of Washington (not off to a great start in 2009) will result in gradual improvement in economic activity as the year progresses. It should also be noted that we suspect this "improvement" will likely be marked by a protracted period (2-3 quarters) where the economic data is simply "less-bad" than prior periods before what we expect to be more sustainable gains toward the end of the year.

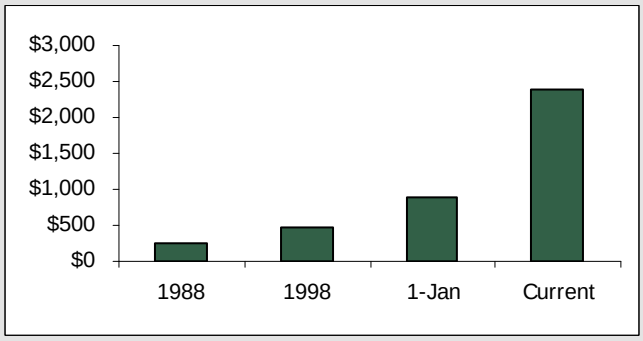
Federal Reserve

The central bank kept its target for the benchmark overnight lending rate near zero at the conclusion of the Federal Open Market Committee (FOMC) meeting last week and stated it was prepared to take additional steps, including the potential purchase of long-term Treasuries, in order to get credit flowing again. Monetary policymakers warned of slowing growth, both domestically and globally, as well as the risks of falling prices. This threat has been a major reason for the exceptionally low level of interest rates as the Fed attempts to combat the deflationary forces building throughout the global economy.

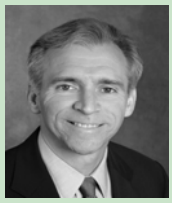
We continue to highlight the Fed's extraordinary response to the current economic and financial crisis. In addition to reducing the federal funds rate by more than 500 basis points within the past eighteen months, Fed Chairman Ben Bernanke has overseen the creation of several innovative lending facilities intended to free up credit within the system by taking on a variety of credit instruments (mortgage-backed securities, asset-backed securities, commercial paper) heretofore presumed "unworthy" of the Fed's balance sheet. Indeed, after taking approximately 20 years to triple the size of its balance sheet, the Fed nearly tripled it yet again over the past several months. See Chart 3.

Though everyone may not agree with these innovative policy steps (due to the potential for rising inflationary pressures) we believe the Fed is one area in Washington that has displayed a willingness to adapt and confront the financial crisis. We agree that current policy will likely ignite inflationary pressures down the line, but the current battle must first contain deflation and the severe recession. The combination of falling homes prices, a rising unemployment rate, and global economic weakness will likely serve as powerful disinflationary forces in the coming year. Inflation will return, but we suspect this is a second-half 2010 story, as domestic and global economies regain their traction. At that point, we expect monetary policy to be just as aggressive in the tightening of policy as they've been on accommodation. In the meanwhile, we hope that the rest of leadership in Washington manages to act with the forcefulness and conviction of the Fed when dealing with the critical issues of TARP II, the creation of a "bad bank," asset guarantees, and economic stimulus.

3. Federal Reserve Balance Sheet as of 12/31/08



Source: Strategas Research Partners



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John is a Managing Director and Chief Market Analyst for Evergreen Investments. A member of the firm's Investment Strategy Committee, John uses a top-down, macro-economic approach in his analysis of the financial markets. He has been featured in various media outlets, including CNBC, BusinessWeek, CNN-Money, Bloomberg News and The Wall Street Journal.