

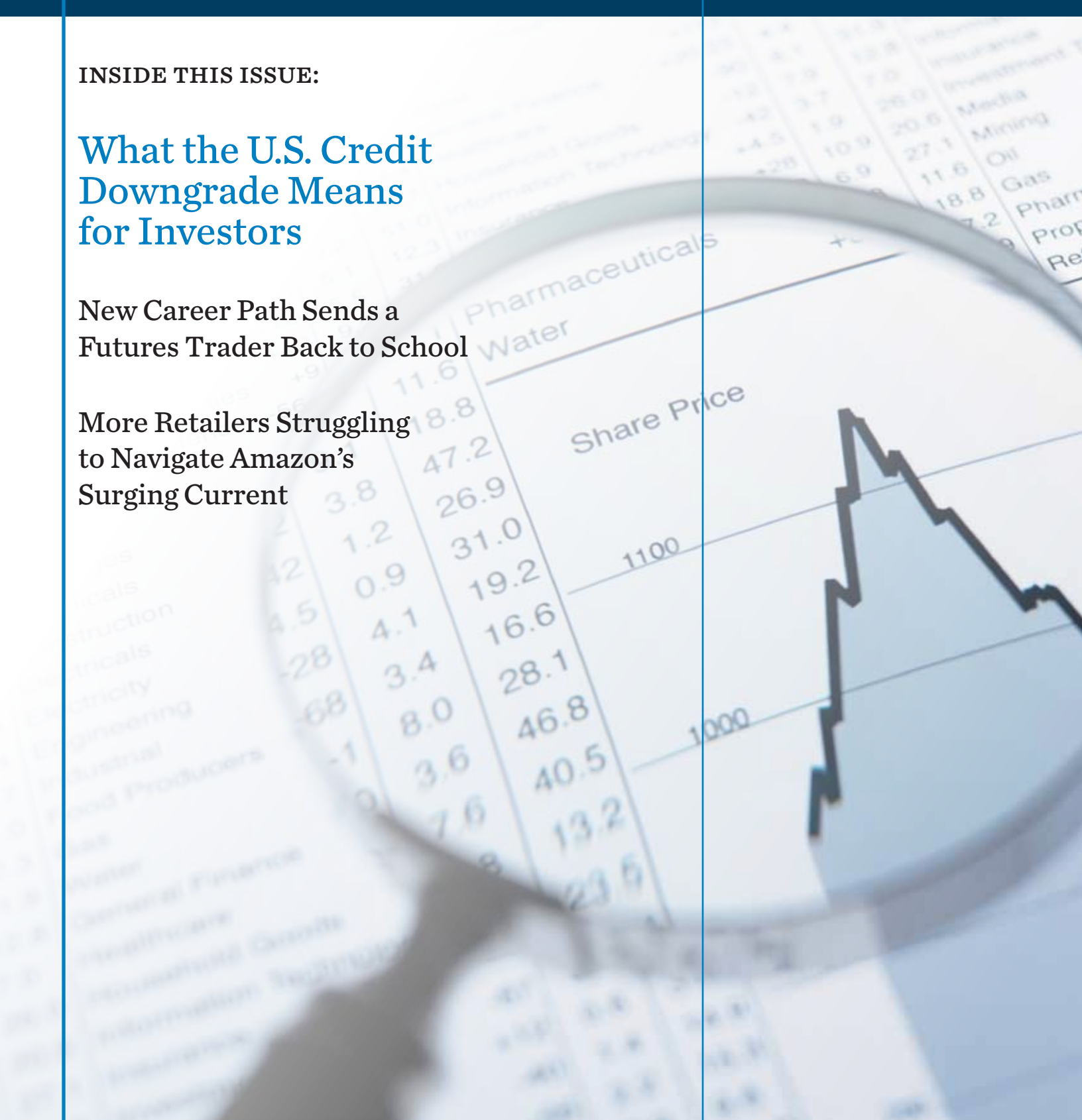
# Client Focus

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### A New Exterior, But the Same Foundation

When you picked up this issue of *Client Focus*, you may have noticed a new look and feel to the magazine's layout. The updated layout of *Client Focus* is one of many design-related changes we will roll out during the next few months.

We have streamlined our logo, which you can see on the cover of this issue, and we will unveil a redesigned website later this fall. With *Client Focus*, the website, and all of our new materials, our goal is to make them not only look nicer, but also more useful and engaging for our clients.

When we designed our new logo and visual system, we wanted it to be symbolic of who and what William Blair & Company is today: a company that draws on a rigorous work ethic and deep intellectual capital to help our clients meet the evolving challenges and opportunities of a dynamic global marketplace.

Another key element of our firm's identity is financial stability. We employ no financial leverage in our business, and we have no third-party debt on our balance sheet; all of the equity comes from capital provided by our principal-owners. This stability allows us to remain singularly focused on our clients' needs through all types of market conditions.

I encourage you to review a copy of our consolidated statement of financial condition, which is available online or through the mail. (See the back page of *Client Focus* for more information.) Although we are required by law to make this information available, we believe it is important for our clients to understand the financial foundation of our business model.

On a final, more somber note, we recently commemorated the 10th anniversary of September 11. Thankfully, no William Blair employees lost their lives that day, but many of us lost friends, clients, and business colleagues. While the anniversary reminded us of the terrible losses suffered that day, it also reminded us of the courage of the first responders and the sacrifice of those who serve our country around the world. I hope we were all able to take time to reflect on the principles that unite us and light the way for a more peaceful tomorrow.

Sincerely,

A handwritten signature in black ink, appearing to read 'John Ettelson'. The signature is fluid and cursive, with a large initial 'J' and 'E'.

John Ettelson  
PRESIDENT AND CEO

# What the U.S. Credit Downgrade Means for Investors

A William Blair & Company roundtable examines the aftereffects and implications of S&P's historic downgrade of the U.S. credit rating

When Standard & Poor's downgraded U.S. long-term debt from AAA to AA+ on August 5, it injected a powerful dose of uncertainty into financial markets, which were already grappling with the European debt crisis, U.S. efforts to lower the federal deficit, and increasing signs of slowing economic growth across the globe. Stock markets responded with an unprecedented stretch of volatility the following week, as the Dow Jones Industrial Average fell 635 points on August 8, rose 430 points on August 9, fell 520 points on August 10, and rose 423 points on August 11.

Amid this uncertain environment, William Blair hosted a webinar on August 18, during which a panel of the company's fixed-income and equity experts addressed some of the most pressing questions raised by the downgrade and the heightened volatility.

## What effect did S&P's downgrade have on fixed-income markets and the United States' creditworthiness in the eyes of investors?

*Jim McKinney, head of Debt Capital Markets:* I think the downgrade of the U.S. government by S&P was no surprise. Their concerns were well-telegraphed in the market, and the timing and the outcome were pretty generally expected and built into the market. What really surprised us is when we came in Monday morning (August 8), and we had this subsequent rally in the Treasury market. The real irony is that the United States was downgraded, and U.S. Treasury yields actually went down.

Not even S&P's historic downgrade of U.S. long-term debt on August 5 could halt the sharp decline in Treasury yields that began in late July.

*Chris Vincent, head of the Fixed Income Group in Investment Management:* It is important to keep in mind that while the U.S. long-term rating was downgraded, it maintained its AAA rating for short-term debt. This is a critical distinction because economic growth and the functioning of our financial system depend on these short-term funding markets. >>

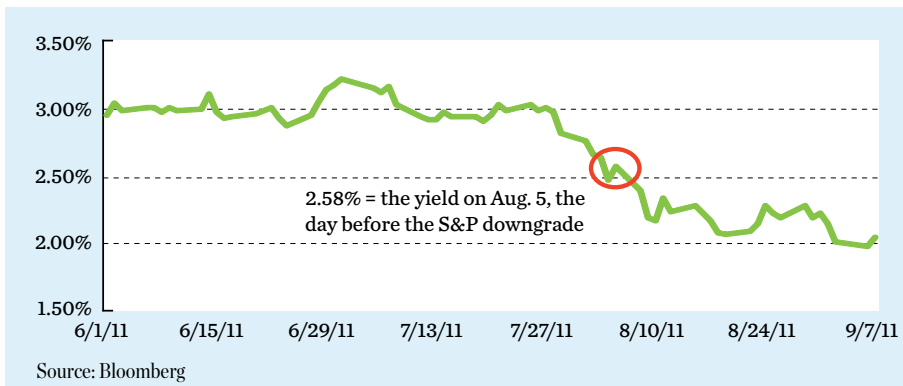
“I think the bigger ‘downgrade’ actually occurred at the end of July when the estimates of GDP growth were revised downward. ... The way out of a negative fiscal situation is economic growth.”

-Chris Vincent, William Blair & Company



## 10-Year Treasury Yield

Not even S&P's historic downgrade of U.S. long-term debt on August 5 could halt the sharp decline in Treasury yields that began in late July.



The downgrade was not about the ability or the willingness of the U.S. government to pay its debts. The U.S. dollar remains the reserve currency of the global economy. It is the most liquid, transparent market in the world.

I think the bigger “downgrade” actually occurred at the end of July when the estimates of GDP growth were revised downward. This is the more important downgrade. The way out of a negative fiscal situation is economic growth; growth will solve a lot of problems in terms of tax receipts and the deficit.

**What is your outlook for the U.S. economy? How real is the danger of another recession?**

*Brian Singer, head of Global Macro Strategies in Investment Management:* We are in a slow-growth environment that is likely to be sustained. But the fears are probably overstated with respect to the potential for a double-dip recession.

This doesn't mean it won't happen, but the fears are probably overstated.

Certainty is very important to growth. The debate over the federal deficit and the need to address the demographic shift that is occurring as the baby boom generation enters retirement have created a great deal of uncertainty in the United States. When the deficit-reduction panel in Congress puts forth its final recommendations this fall, I think that will go a long way in providing certainty and clarity, which in turn will help bolster consumer confidence and business spending.

*Chris Vincent:* I agree that we are going to experience a period of below-normal growth. It may even be considered a so-called growth recession. Unemployment is going to remain high. The charts that gauge investment-grade yield spreads (see page 4) are forecasting about a 50/50 chance of

recession. I would say the odds of a recession are actually lower than that. I think we will have positive growth, and I think we may actually have slightly better trend growth in the second half of 2011.

*Jim McKinney:* With interest rates already nearing 0%, the Federal Reserve does not have many arrows left in its quiver to stimulate the economy. So we are looking at an extended period of slow growth. What we need to get the economy jumpstarted is more confidence and spending by consumers. There has definitely been a psychological shift among consumers since the 2008 recession. People today are only buying things they need, not things they want.

**The recent market volatility is reminding many people of the financial crisis of 2008. How do the current economic and market environments compare with 2008?**

*Chris Vincent:* Investment-grade spreads (the difference in yields of investment-grade corporate bonds and U.S. Treasury securities) are a very good gauge of the amount of stress in the economy and the financial system. Over the past few weeks, we have seen some widening in spreads, but the reality is that they are nowhere near where they were in the midst of the financial crisis. The situation is much better, and our financial institutions are much healthier.

*Brian Singer:* Risk attitudes have changed significantly as a result of the 2008 crisis, and this has exacerbated

“The downgrade of the U.S. government by S&P was no surprise. ... The real irony is that the U.S. got downgraded, and U.S. Treasury yields actually went down.”

-Jim McKinney, William Blair & Company

the short-term volatility. Investors have become more active in making preemptive trades at any hint of downside risk and more aggressive on the upside in an attempt to recoup losses from 2008. This intensifies the short-term volatility as investors sell on the way down and buy on the way up.

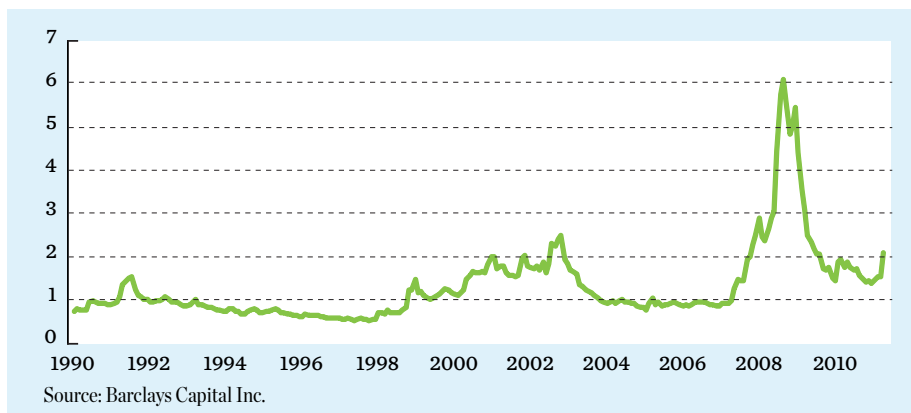
#### What opportunities has the recent volatility created for investors?

**Jim McKinney:** The values in fixed income are away from Treasuries because there is a fear factor that is driving the market for Treasuries. I think there are a lot of good values in preferred stocks. There are plenty of preferreds that yield more than 7%. Municipal-bond yields are still very attractive and have hardly gone down at all; many of them still offer an after-tax yield in the high-6% range. The market I would be cautious with and the one that has widened out the most is the junk-bond market. There are some very good yields out there, but I would be careful of the bonds you pick.

**Brian Singer:** In frenetic environments like the one we are currently experiencing, it is important for long-term investors to focus on the tides of fundamental value rather than the waves and ripples of market behavior. The indiscriminate buying and selling this summer has driven prices farther from their fundamental values, and this has created a large opportunity set for investors. The S&P 500, which is an index of large-cap U.S. stocks, is still well below its fundamental value, but not nearly as far below as it was in 2008. We are seeing an extremely attractive opportunity set with European stocks as investors react to the debt situations in the countries collectively known as the PIIGS (Portugal, Italy, Ireland, Greece, and Spain).

#### U.S. Corporate Investment-Grade Option-Adjusted Spread (OAS)

The yield spread between investment-grade corporate bonds and Treasury bonds is viewed as a good measure of the amount of stress in the financial system. Spreads have increased this summer, but they are nowhere near 2008 levels.



## Hear the Full Conversation

To listen to a replay of the August 18 webinar on the credit downgrade, go to [williamblair.com/PWM-resources](http://williamblair.com/PWM-resources). Here you can listen to replays of all previous webinars and download financial planning resources, including our new white paper “Balancing Retirement with Wealth Transfer Goals” and our update on the estate-tax elections for 2010.

This information has been prepared solely for informational purposes and is not intended to provide, or should not be relied on for, accounting, legal, or tax or investment advice. Please consult with your tax and/or legal advisor regarding your individual circumstances.

# New Career Path Sends a Futures Trader Back to School

## MATT MCGUIRE'S IDEA OF A

perfect day is taking a train to downtown Chicago and touring the city's art museums and galleries. Unfortunately, that is not something the father of four, sports coach, and student-teacher has much time for these days.

While Matt may not have much free time to browse The Art Institute of Chicago or the Museum of Contemporary Art, he might soon be bringing students to these museums as part of his new career. After retiring early from his work as a futures trader, Matt is set to launch a second career as an art teacher.

Growing up as one of four boys in suburban Hinsdale, Matt followed in his father's footsteps as a competitive swimmer. His father swam at Fenwick High School and then at the University of Michigan, where he competed in the NCAA finals. As the team's captain, Matt led Fenwick to a second-place

finish at the state finals and went on to swim at Indian River Junior College in Florida, a school well known for training Olympic swimmers.

Upon returning to Chicago after college, Matt worked for two years with his father, a broker at the Chicago Mercantile Exchange. Over the next few years, Matt worked for several brokerage firms, where he learned the industry and advanced his career before returning to the floor as a spread broker in 1992. Two years later, he bought his own seat on the floor.

He traded stock index spreads before migrating to the Eurodollar pit, where he traded Eurodollar spreads. "The energy, the fraternity, and even the stress were addictive," he says. "It was a boom time, and many people were successful far beyond what they could imagine."

Matt credits three people with keeping him grounded during these heady times: his wife, his father, and John Newhouse, who served as director of the Chicago Mercantile Exchange. Matt says both men, who he counts as mentors, had strength of character and were conservative in their work.

He says his wife, Anne, played an essential role in helping him deal with the stress of life on the trading floor. "It was because of my wife that I was able to leave work behind at the end of the day, and return to it the next day with renewed purpose," Matt says. "She kept our lifestyle conservative, which kept the pressure off of me."

Despite the success he enjoyed as a trader, the job became less interesting for Matt once the dynamic human interaction and decision-making that defined the trading pits' open-outcry system were replaced by computers and electronic trading. "Anything having to do with math and trading



## GETTING TO KNOW: MATT MCGUIRE

**PERSONAL:** Matt and his wife, Anne, live in LaGrange, Illinois and have four children. He followed in his father's footsteps by swimming competitively in high school and college. He coaches swimming and lacrosse at Fenwick High School.

**CAREER PATH:** After owning a seat on the floor of the Chicago Mercantile Exchange and trading Eurodollar spreads, Matt left the trading business in his early 40s and is about to start his career as an arts teacher.

**"It was because of my wife that I was able to leave work behind at the end of the day, and return to it the next day with renewed purpose."**

“Anything having to do with math and trading was being overtaken by computers. The game was changing and it was time for me to make a change.”

was being overtaken by computers,” he says. “The game was changing, and it was time for me to make a change.”

Matt left the trading business and began a short-lived career selling industrial lighting; he eventually took classes in welding and art. These classes inspired him to return to school full-time to earn a teaching degree.

“Imagine entering a college classroom at age 43,” Matt says. Although the transition to life as a student was daunting, Matt managed the full course load along with his responsibilities as a father. He is in his final weeks of student teaching and will graduate in January 2012 with a double major in art and art education, with qualifications to teach fine arts for all grade levels.

In addition to studying and student-teaching, McGuire also coaches. Matt’s brother Luke is the head boys swimming coach at Fenwick, and he recruited Matt to help with the team and assigned him responsibility for the 5:30 a.m. practices. In the spring, Matt moves from the pool to the lacrosse field to coach Fenwick’s varsity girls’ team. “Lacrosse is an entirely different discipline than swimming, and coaching girls is a far different undertaking than coaching boys,” Matt says. “I have been fortunate to coach swimming with my brother and also coach two of my children in lacrosse at Fenwick, first as an assistant of the boys’ team and now as head coach of the varsity girls’ team.”

Joe Tabet, Matt’s financial advisor at William Blair, says Matt’s career path and diverse experiences will be an asset for his future students. “Matt is a combination of a disciplined and driven athlete, a successful businessman, and an educator—a true renaissance man,” Joe says. “He has made a conscious and hard-earned decision to redirect his life to share his love of the arts with his students.”

One should not assume that the listed client approves or disapproves of William Blair & Company or the advisory services provided.

## EQUITY RESEARCH

# More retailers struggling to navigate Amazon’s surging current

Analyst Mark Miller finds that Amazon.com’s price advantage has traditional retailers playing defense.

With online shopping engrained as a way of life for today’s consumers, William Blair & Company equity research analyst Mark Miller set out to study the impact Amazon is having on traditional retailers.

To measure the product offerings and prices of Amazon and other retailers, Miller, who was named to both *The Wall Street Journal’s* and *Financial Times/StarMine’s* top analyst lists in 2011, along with analyst Daniel Hofkin and senior associate Eric Walania, randomly selected 100 items from 24 retailers, including Wal-Mart, Target, Best Buy, Walgreen, Costco, PetSmart, and Vitamin Shoppe. Of these 2,400 items, the analysts found that 47% were also available on Amazon. For these overlapping items, Amazon’s prices were 11% below retail store prices once Amazon’s shipping charges and sales tax advantages were factored in.

At present, Amazon and other online-only retailers are required to collect sales tax only in states where the company has a physical presence. With state and local sales taxes combining to reach up to 10% in some cities, the sales tax exclusion is a distinct advantage for Amazon. But the company would have lower prices even if its sales-tax advantage were eliminated, Miller said. “We found that Amazon.com still has a midsingle-digit price discount, and nearly half (48%) of all the overlapping items would still be less expensive >>

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## » EQUITY RESEARCH

at Amazon, even if the company had to collect taxes," Miller said.

Not all retailers have equal exposure to the risk posed by Amazon. Miller said companies that skew toward higher-ticket, branded items are more vulnerable to losing customers to Amazon. Conversely, companies that offer less expensive items or perishable goods; convenient, smaller-format stores; and other value-added features, such as loyalty programs or experiential shopping, face a lower-than-average threat from Amazon.

The companies included in the study are employing an array of approaches to their own e-commerce operations, which highlights the lack of a generally accepted strategy in the retail industry, Miller said. These approaches include selling products directly on Amazon as well as on the company's own website, matching Amazon's prices on request, and offering in-store pick-up of items bought online.

*To receive a copy of Miller's research report on Amazon.com or reports on the more than 500 quality growth companies covered by William Blair's equity research analysts, please contact your William Blair representative. Visit [williamblair.com/ResearchCoverage](http://williamblair.com/ResearchCoverage) for a full list of the company's coverage universe and all disclosures.*

## CLIENT SERVICE

### Now Available: William Blair's Consolidated Statement of Financial Condition

William Blair & Company's semiannual consolidated statement of financial condition as of June 30, 2011, is now available for clients to review. You can view the statement online at [williamblair.com/financial.asp](http://williamblair.com/financial.asp); you may also request a hard copy by calling +1 800 621 0687 and requesting extension 5001.

As a registered broker-dealer subject to the Securities Exchange Act of 1934, William Blair's net capital must be at least equal to the greater of \$1 million or 2% of aggregate debit items arising from customer transactions. As of June 30, 2011, and July 31, 2011, the firm's regulatory net capital of \$100.8 million and \$116.8 million was 189% and 251%, respectively, of aggregate debit items.

For additional information about the consolidated statement of financial condition or to review the firm's most recent annual audit report, please contact your William Blair representative.

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