

MONTHLY MARKET REVIEW

August 2011

U.S. Economy

After several months of relative clarity to the near-term outlook for Federal Reserve policy, the significant, sustained slowdown in the economy this year has created new speculation and uncertainty about further possible easing measures, especially given the low likelihood of additional fiscal stimulus.

During the first half of the year, the Fed was still conducting its QE2 (quantitative easing) program of direct purchases of U.S. Treasury securities, creating a steady and predictable month-to-month easing program. As QE2 was coming to an end in June, the Fed was still sticking to the position that the slowdown in the U.S. economy was "transitory" and attributable to a short-term spike in energy prices and the earthquake in Japan. As the third quarter began, the economic slowdown proved to be less "transitory" and more sustained, sparking calls for additional stimulus.

Amid a high level of disagreement among the members of the Federal Reserve Open Market Committee, the Fed made a significant change to its policy statement following its August 9 meeting, stating that "economic conditions...are likely to warrant exceptionally low levels for the federal funds rate at least through mid-2013," essentially committing to keep short-term interest rates at 0% for the next two years. The change was in response to the sustained economic weakness, which proved the Fed's previous economic forecast wrong. While seemingly intended to give further certainty and clarity to the Fed's policy over the next few years, the ultimate goal was to bring down longer-term interest rates further out on the yield curve. Longer-term interest rates are essentially a reflection of expectations for future short-term interest rates, so following the Fed's statement, longer-dated Treasury yields declined significantly. The five-year Treasury yield is now less than 0.90%, down from 1.35% at the beginning of July, while the ten-year Treasury yield has fallen to less than 2% from 2.82% at the end of July. The decision was not without controversy, as three of the ten members of the FOMC dissented from the Fed statement, the most in nearly 20 years. While these members are worried about igniting inflation, the meeting minutes reveal that other members argued for more stimulus via further asset purchases.

The shift toward trying even harder to drive down longer-term interest rates has increased speculation about further Fed actions. The Fed did announce that it will add an extra day to its September meeting in order to "allow a fuller discussion" of the economy. Some market pundits have taken the combination of the Fed's attempts to talk down longer-term interest rates with a two-year commitment to short rates and the extension of its meeting to include an extra day as a sign that additional stimulus may be announced at the meeting, including a possible QE3, or at least an extension of the duration of the bonds on the Fed's balance sheet. Federal Reserve Chairman Ben Bernanke has remarked that the Fed could increase the maturity of its \$1.7 trillion Treasury portfolio as a means of further stimulus. Such a move would require actually buying longer duration Treasury securities in an attempt to drive long-term interest rates lower. Other ideas floated by Fed members include more explicitly stated targets for inflation or the unemployment rate, such that as long as inflation is below some set level, policy would remain accommodative if the unemployment were above a set level.

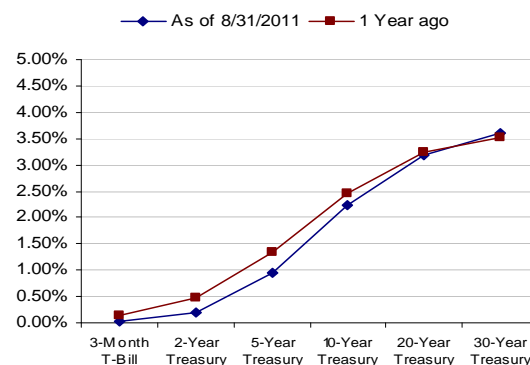
Regardless of the outcome of its September meeting, with the economy clearly slowing and fiscal stimulus unlikely, the Federal (*cont'd on page 2*)

Market Data

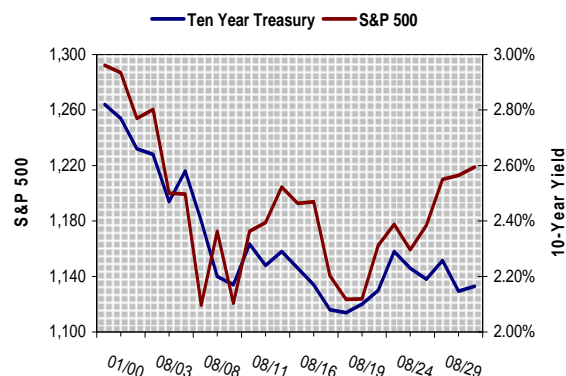
Change in Price

Equity Indices	8.31.11 Close	1-Month		YTD		1-Year	
		Pts.	%	Pts.	%	Pts.	%
Dow Jones Ind. Avg	11613.50	-529.70	-4.36%	36.00	0.31%	1598.80	15.96%
S&P 500	1218.89	-73.39	-5.68%	-38.75	-3.08%	169.56	16.16%
Nasdaq Composite	2579.46	-176.92	-6.42%	-73.41	-2.77%	465.43	22.02%
Commodities							
Oil: \$ Per Barrel	88.81	-6.89	-7.20%	-2.57	-2.81%	16.89	23.48%
Gold: \$ Per Ounce	1829.30	201.00	12.34%	407.90	28.70%	580.30	46.46%
Currencies							
\$ per € (euro)	1.44	0.00	-0.15%	0.10	7.39%	0.17	13.38%
¥ (yen) per \$	76.66	-0.10	-0.13%	-4.50	-5.54%	-7.55	-8.97%
\$ per £ (pound)	1.63	-0.02	-1.05%	0.06	4.09%	0.09	5.88%

U.S. Treasury Yields:



Intra-Month Markets



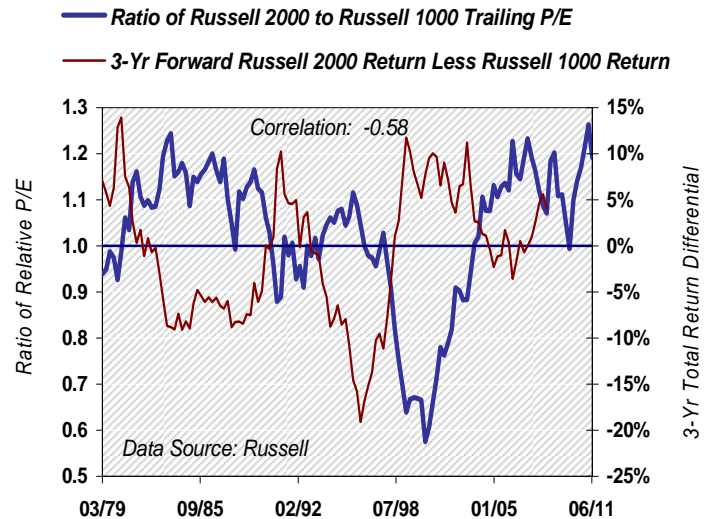
U.S. Economy (cont'd)

Reserve's monetary policy is likely to be more fluid and dynamic over the coming months when compared to the relatively steady and mechanical execution of QE2 during the first half of the year.

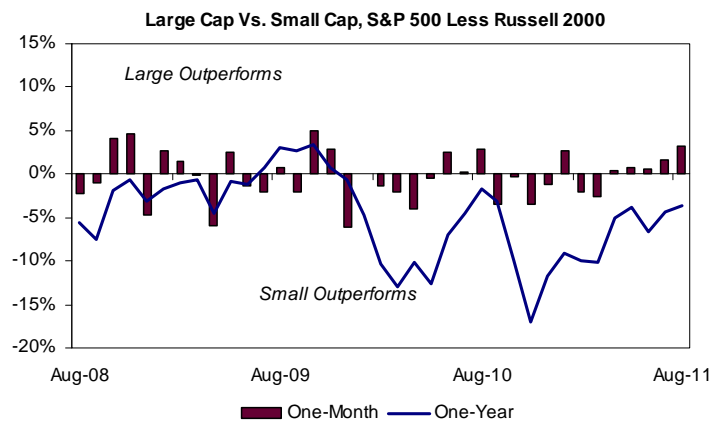
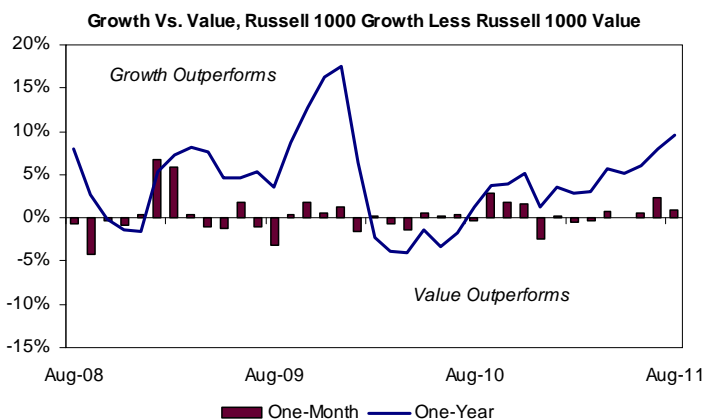
U.S. Equities

The S&P 500 index declined 5.43% in August, falling for four straight months for the first time since March 2008. For the year, the index is now down 1.77%. The small-cap Russell 2000 index lagged large-cap indices for the fifth straight month, declining 8.70% in August. Over the last 12 months, large-cap stocks still trail small-cap stocks by 3.69%. The broad Russell 1000 Growth index fell 5.28% in August, ahead of its Value counterpart's 6.24% drop. Over the last 12 months, the Russell 1000 Growth index is ahead by 9.59%, the largest 12-month gap since late 2009.

The significant run of small-cap stocks in recent years has left valuations at a historically high level versus large-cap stocks. As of 7/31/2011, the Russell 2000's price-to-earnings ratio (P/E), excluding negative earnings, was 16.69, compared to the large-cap Russell 1000's P/E of 13.89. Those valuations put the Russell 2000's P/E at a level 20% higher than that of the Russell 1000, creating a Russell 2000 / Russell 1000 Valuation factor of 1.20X, and suggesting that small-cap stock valuations are high relative to large-cap stock valuations. While this factor is down from 1.26X in March, it is still well above its long-term average of just 1.03X. Historically, when this factor has been high, the cheaper large-cap stock sector has tended to perform better than its small-cap stock counterpart over the ensuing three years. There have been 43 quarter-ends since the inception of the Russell indices through mid-2008 in which the small-cap-to-large-cap valuation ratio was higher than 1.10X. In 33 of the those 43 instances, large-cap stocks outperformed small-cap stocks over the next three-year period of time. Across all 43 instances, large-cap outperformed small-cap stocks by an annualized 4% on average over the next three year period of time. This inverse relationship between high relative valuation and subsequent low relative returns can be seen in a historical chart of the relative valuation versus forward three-year returns (see chart). Thus, current relative valuation levels suggest that large-cap stocks are more likely to outperform small-cap stocks over the next three years than not.



The charts below illustrate the relative rolling returns of growth vs. value stocks and large-cap vs. small-cap stocks.



Index	Asset Class	1 Mo	3 Mo	YTD	1 Yr	3 Yr	5 Yr	10 Yr
Wilshire 5000	All-Cap Core	(5.95)	(9.59)	(2.60)	19.01	1.25	1.56	3.82
S&P 500	Large-Cap Core	(5.43)	(8.90)	(1.77)	18.50	0.54	0.78	2.70
S&P 500/Citigroup Growth	Large-Cap Growth	(4.75)	(6.48)	1.13	23.64	3.13	3.32	2.20
S&P 500/Citigroup Value	Large-Cap Value	(6.18)	(11.44)	(4.79)	13.37	(2.18)	(1.86)	3.00
S&P 400	Mid-Cap Core	(7.11)	(12.22)	(2.72)	22.89	4.00	4.65	7.28
S&P 600	Small-Cap Core	(7.67)	(12.25)	(3.90)	24.44	2.07	2.65	7.01
Russell 1000	Large-Cap Core	(5.76)	(9.41)	(1.93)	19.06	0.84	1.11	3.16
Russell 1000 Growth	Large-Cap Growth	(5.28)	(7.57)	0.18	23.96	3.08	3.75	2.71
Russell 1000 Value	Large-Cap Value	(6.24)	(11.21)	(3.99)	14.37	(1.45)	(1.62)	3.41

U.S. Equities (cont'd)

Index	Asset Class	1 Mo	3 Mo	YTD	1 Yr	3 Yr	5 Yr	10 Yr
Russell Midcap	Mid-Cap Core	(6.88)	(12.13)	(3.00)	21.29	2.95	2.99	7.16
Russell Midcap Growth	Mid-Cap Growth	(6.82)	(11.74)	(1.71)	25.61	3.80	4.28	5.90
Russell Midcap Value	Mid-Cap Value	(6.93)	(12.50)	(4.18)	17.51	2.04	1.36	7.50
Russell 2500	SMID-Cap Core	(8.19)	(13.63)	(4.56)	22.16	2.58	2.76	6.82
Russell 2500 Growth	SMID-Cap Growth	(8.19)	(13.34)	(2.70)	27.82	3.63	4.58	5.74
Russell 2500 Value	SMID-Cap Value	(8.18)	(13.89)	(6.23)	17.28	1.56	0.77	7.19
Russell 2000	Small-Cap Core	(8.70)	(14.03)	(6.54)	22.19	0.83	1.53	5.85
Russell 2000 Growth	Small-Cap Growth	(8.57)	(14.03)	(4.60)	27.54	2.14	3.59	4.89
Russell 2000 Value	Small-Cap Value	(8.83)	(14.02)	(8.52)	16.86	(0.57)	(0.62)	6.46
Russell Micro Cap	Micro Cap Core	(10.48)	(15.51)	(10.39)	19.73	(0.81)	(2.02)	5.02
NAREIT Composite Index	REITS	(4.85)	(7.17)	5.05	18.18	2.47	(0.48)	9.31

U.S. Fixed Income

Treasuries rallied in August for their strongest monthly return since the financial crises in 2008 as the Barclays Treasury index gained 2.78% despite Standard & Poor's credit downgrade of U.S. debt to AA+ on August 5th. While credit downgrades typically result in higher interest rates and falling prices for the issuer, investors still consider U.S. debt as a safe haven investment relative to other current credit options around the world. With increasing concerns over slowing global economic growth, investors piled into Treasuries driving rates lower as the ten-year Treasury yield fell 0.60% to a level of 2.23% and the 30-year Treasury fell 0.52% to just 3.60%.

The Barclays Aggregate index gained 1.46% in August as spread-sector performance trailed the Treasury market. Within the Aggregate, the CMBS sector returned -1.74% and trailed duration-matched Treasuries by 3.08%. Credit sector saw a small gain of 0.36%, but trailed duration-matched Treasuries by 2.97%. Higher risk/lower rated bonds were shunned during the month as the Barclays High Yield index declined 4.00% and the High-Yield Loans index plunged 4.70%.

Index	Asset Class	1 Mo	3 Mo	YTD	1 Yr	3 Yr	5 Yr	10 Yr
Citigroup 3-Month T-Bill	Cash	0.00	0.01	0.07	0.12	0.25	1.70	1.95
Barclays 1-3 Year U.S. Treasury	Short Treasuries	0.36	0.67	1.50	1.52	2.71	3.97	3.50
Barclays 1-3 Yr Govt/Credit	Short Govt/Credit Bonds	0.18	0.50	1.55	1.74	3.42	4.30	3.86
Barclays Intern. Aggregate	Intern. Core Bonds	1.06	2.21	5.02	4.45	6.78	6.33	5.46
Barclays Intern. Govt/Credit	Intern. Govt/Credit Bonds	1.07	2.34	5.04	4.01	6.32	6.11	5.29
Barclays Aggregate	Core Bonds	1.46	2.77	5.88	4.62	7.23	6.56	5.71
Barclays Long Govt/Credit	Long Govt/Credit Bonds	4.46	7.03	12.63	5.57	11.00	8.48	7.57
Barclays Government	Government Bonds	2.54	3.94	6.48	4.04	6.05	6.43	5.46
Barclays Credit	Corporate Bonds	0.36	2.03	6.28	4.98	9.15	6.91	6.22
Barclays Mortgage	Mortgage-Backed Bonds	1.25	2.28	5.12	4.98	7.23	6.80	5.75
Barclays US TIPS	TIPS	0.81	5.61	10.85	10.79	6.81	7.19	7.26
Barclays Municipals	Municipal Bonds	1.71	3.11	7.29	2.66	6.00	4.94	4.95
Barclays High Yield	High Yield Bonds	(4.00)	(3.84)	1.94	8.39	11.95	8.10	8.39
Merrill Lynch All U.S. Convertible	Convertible Securities	(5.82)	(9.70)	(3.93)	8.97	5.15	3.62	5.08

International

Euro-area manufacturing contracted in August as the Markit Economics manufacturing gauge fell to 49.0 from 50.4 in August. Gauges for non-euro areas such as England and Sweden also read below 50 (readings below 50 indicate contraction). Economic growth in the euro-area was lower in the second quarter than economists expected as GDP rose 0.2%, after increasing 0.8% during the first quarter. European confidence in the economic outlook dropped sharply in August to levels seen during the 2008 crisis. Sentiment amongst European manufacturers and services, as well as consumer confidence, all declined.

The European Central Bank purchased 43 billion euro's of Italian and Spanish bonds in August in an attempt to allow those countries to refinance debt at more favorable interest rates. The initial results were positive as Italy's ten-year bond yield dropped from 6% to 5%. However, Italy's planned austerity package has been unraveling under political pressure, leaving a wider funding gap as pension costs may not be lowered and taxes not increased, sending interest rates right back to levels prior to the ECB bond buying spree. Italy also has 46 billion euros of maturing bonds in September, accounting for more than half of all euro-area maturities.

An index of Chinese manufacturing stood at 50.9 in August, near a 29-month low, while similar gauges for South Korea and Taiwan fell below 50, according to Markit Economics. Brazil's industrial production rose slightly in July from June, but contracted 0.3% over the past year. In a surprise move, Brazil's central bank cut their benchmark interest rate over concerns that a (cont'd on page 4)

International (cont'd)

“substantial deterioration in the global economy may be prolonged”, according to the bank’s statement. The central bank forecasts growth to be 3.9% this year after the economy expanded 7.5% in 2010.

<i>Index</i>	<i>Asset Class</i>	<i>1 Mo</i>	<i>3 Mo</i>	<i>YTD</i>	<i>1 Yr</i>	<i>3 Yr</i>	<i>5 Yr</i>	<i>10 Yr</i>
International Equities								
MSCI World	Global Developed Mkt Equity	(7.00)	(10.08)	(3.53)	15.06	(0.71)	0.35	4.22
MSCI EAFE	Intl Developed Market Equity	(9.02)	(11.55)	(5.66)	10.50	(2.50)	(1.01)	5.41
MSCI Europe	European Equity	(10.01)	(14.67)	(4.69)	10.61	(3.67)	(1.12)	5.46
MSCI Japan	Japanese Equity	(8.13)	(3.47)	(9.32)	6.39	(3.39)	(4.78)	2.06
MSCI Pacific	Pacific Equity	(7.09)	(5.06)	(7.07)	10.70	0.19	(0.73)	5.33
MSCI Emerging Markets	Emerging Market Equity	(8.90)	(10.60)	(8.31)	9.40	5.36	8.72	16.29
International Fixed Income								
Barclays Global Aggregate	Global Invest. Grade Bonds	1.27	3.44	7.89	8.96	7.76	7.35	7.21
Citigroup World Government Bond	Intl Developed Market Bonds	2.07	4.63	8.59	9.22	7.99	7.90	7.72
JP Morgan EMBI+	Emerging Market Bonds	0.93	4.35	8.18	7.61	10.62	8.90	11.02

Alternative Investments

<i>Index</i>	<i>Asset Class</i>	<i>1 Mo</i>	<i>3 Mo</i>	<i>YTD</i>	<i>1 Yr</i>	<i>3 Yr</i>	<i>5 Yr</i>	<i>10 Yr</i>
Goldman Sachs Commodity Ind.	Commodities	(1.85)	(4.80)	3.27	27.06	(15.96)	(5.00)	3.62
HFRI Equity Hedge	HF - Equity Long/Short	(4.11)	(5.57)	(3.42)	7.88	2.15	2.58	5.31
HFRI Equity Mkt Neutral	HF - Equity Market Neutral	(0.94)	(1.41)	0.06	3.32	(0.58)	1.11	2.56
HFRI Convert Arb	HF - Convertible Arbitrage	(2.39)	(4.38)	(2.62)	3.74	8.79	5.04	5.34
HFRI Distressed Sec	HF - Distressed Securities	(4.31)	(4.96)	(0.48)	6.00	4.13	3.58	8.81
HFRI Event Driven	HF - Event Driven Strategies	(3.71)	(4.90)	(0.92)	6.50	4.31	4.17	7.22
HFRI Fixed Income	HF - Fixed Income Strategies	(0.09)	(0.50)	1.57	7.20	6.22	3.75	5.88
HFRI Macro	HF - Macro Strategies	0.12	0.22	(0.30)	7.22	4.75	6.38	8.05