

MONTHLY REVIEW—AUGUST 2011

MARKET INDEXES

Index	1 Month	3 Months	Year to Date	Trailing 1 Year
<u>Domestic Equity (Large Cap)</u>				
Russell 1000 (Core)	(5.76)	(9.41)	(1.93)	19.06
Russell 1000 Growth	(5.28)	(7.57)	0.18	23.96
Russell 1000 Value	(6.24)	(11.21)	(3.99)	14.37
<u>Domestic Equity (Small/Mid Cap)</u>				
Russell 2500 (Core)	(8.19)	(13.63)	(4.56)	22.16
Russell 2500 Growth	(8.19)	(13.34)	(2.70)	27.82
Russell 2500 Value	(8.18)	(13.89)	(6.23)	17.28
<u>International Equity</u>				
MSCI World ex US (Core)	(8.45)	(11.25)	(5.72)	10.73
MSCI World ex US Growth	(7.98)	(10.24)	(5.13)	13.48
MSCI World ex US Value	(8.94)	(12.26)	(6.31)	7.92
MSCI Emerging Markets	(8.94)	(10.74)	(8.55)	9.07
<u>Domestic REITs</u>				
NAREIT All Equity	(5.60)	(7.54)	5.53	18.44
<u>Commodities</u>				
Dow Jones-UBS Commodity	1.00	(1.25)	1.30	25.85
<u>Domestic Fixed Income</u>				
Barclays U.S. Aggregate	1.46	2.77	5.88	4.61

ECONOMIC INDICATORS

	Most Recent	Year-to-Date	Trailing 1 Year
U.S. Dollar (July)	-0.6%	-5.1%	-9.0%
Housing Prices (June)	1.1%	-0.7%	-3.8%
Consumer Sentiment (level)	55.7	74.5	68.9
Retail Sales (July)	0.5%	3.7%	8.6%
Job Gains/Losses (July)	117,000	930,000	1,258,000
Inflation (July)	0.1%	3.1%	3.6%

August was a challenging month for financial markets as investors shifted their focus to the weak economic recovery, and the fiscal imbalances in both the US and Europe. Up until Standard & Poor's downgrade of the US long-term sovereign credit rating, the market's response to these emerging risks had generally been more muted.

However, after the US debt downgrade on August 5th, investors immediately focused their attention on the fundamental problems faced by the US: high unemployment, crushing debt, a weak housing market and a potential recession. During the month, Commerce Department figures showed that the US economy grew at a 1 percent annual rate from April through June after a 0.4 percent gain in the prior quarter. This capped the weakest six months of the recovery since it began in mid-2009. Also during the month, consumer senti-

ment plunged to the lowest level since May 1980, adding to concern that weak employment gains and volatility in the stock market will prompt households to retrench and hinder a recovery that Fed policy makers said was already advancing "considerably slower" than projected.

In order to combat slowing growth, the Federal Reserve announced that it decided to hold its key interest rate at near zero until mid-2013. At the August 26th annual Fed symposium in Jackson Hole, Fed Chairman Bernanke said the economy wasn't deteriorating enough to warrant any immediate stimulus and the central bank still had tools to stimulate growth. However, with the selloff in equities during August, investors are starting to realize that the central bankers have for the most part run out of options to stimulate growth or prevent a downward spiral into a global recession. Many major market indices have now given back all of their positive performance for 2011 and have slipped into negative territory.

On the positive side, equity valuations appear reasonable, corporate profitability remains strong, credit markets are accommodative and interest rates are low. These factors would normally provide strong support for equities and corporate events such as mergers and acquisitions. However, there are also deep macro concerns such as the prospect of sovereign defaults and a tepid economic recovery supported only by government intervention and increased debt. Systematic risks and volatility will likely remain high across risky assets for the foreseeable future as the government policy responses to the current economic growth situation and high unemployment rate have largely been unsuccessful.

Given the generalized nature of the economic downturn and the associated selloff in most major equity markets, most institutional portfolios struggled during August. Bonds were generally positive during the month, despite the downgrade of US debt. Commodities (DJ-UBS Commodities Index) were also positive, as gold advanced to new highs, while oil tugged the index in an opposite direction. Hedging strategies having very low or negative correlations to the traditional equity markets also proved successful in many cases. LT&A's clients are increasing the use of such strategies in an attempt to mitigate the risk associated with portfolios whose fate has too often been linked tightly to the direction of the public equity markets.