



Quarterly Economic and Capital Market Commentary

Second Quarter 2011

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Overview: Don't Be Too Discouraged by Slow Growth.

The U.S. economy is faced with significant structural headwinds that have made for a sluggish recovery – this is not new news. Recent lackluster economic news has reignited the debate as to whether a double-dip recession is on the horizon. We remind readers of two of our long standing views: first, the economy will recover, albeit at its own pace. The recession was largely a result of a significant shock to the financial system, which essentially ensured a slow recovery. Second, with a smaller margin for error on the downside, this has been, and will remain, a risk-filled recovery. Foreclosures continue to plague the housing market, state and local governments continue to shed jobs at a brisk pace, and policymakers have exhausted their options for additional stimulus, if necessary. Add to this list the global risks related to European sovereign debt, unrest in the Middle East, China's attempt to orchestrate a soft landing, and violent swings in commodity prices. All of this highlights the risk-filled environment that the economy faces.

We actually are optimistic that we will see a reacceleration in economic growth in the second half of 2011. The disaster in Japan created a larger disruption to the global industrial base than most realized. We now see global industrial activity poised for a rebound as inventories are rebuilt. Consumer spending levels have also remained resilient, banks continue to (ever so slightly) ease lending standards, and corporate confidence and earnings growth remain high. The labor market experienced a downturn in May, but we believe the longer-term trend in jobs growth should remain positive. Overall, we think a pickup in economic growth in the second half of the year is likely and we are expecting to

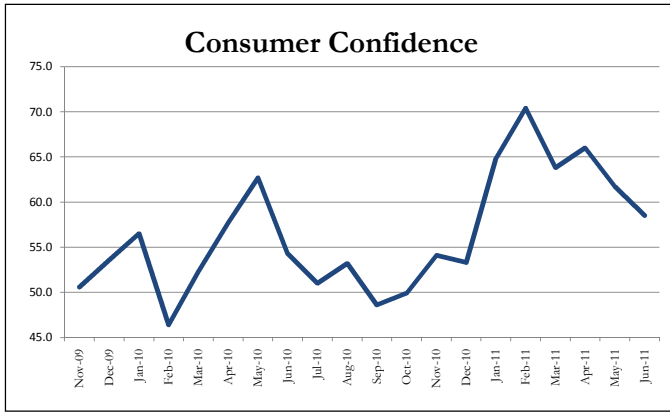
see gross domestic product growth of around 2.5% for the second quarter of 2011 and around 3% for the second half of 2011.

Retail Sales: Consumers Remain Cautious. Retail sales fell 0.2% in May. Core retail sales (excluding more volatile autos and gas) advanced 0.3%. The decline was due to slumping auto sales. This really is not surprising given the sharp rise in gas prices and the tsunami in Japan. Spending also remained weak at furniture and electronics stores. This weakness in spending for big-ticket items is a clear warning that household budgets are being stretched and consumers are cutting back on major discretionary purchases. However, it should not be interpreted as a dramatic swing in consumer sentiment.

We are hopeful retail sales will accelerate from their currently subdued pace in the second half if the following two conditions materialize: gasoline prices remain stable and the job picture resumes its gradual improvement which will firm up consumer confidence.

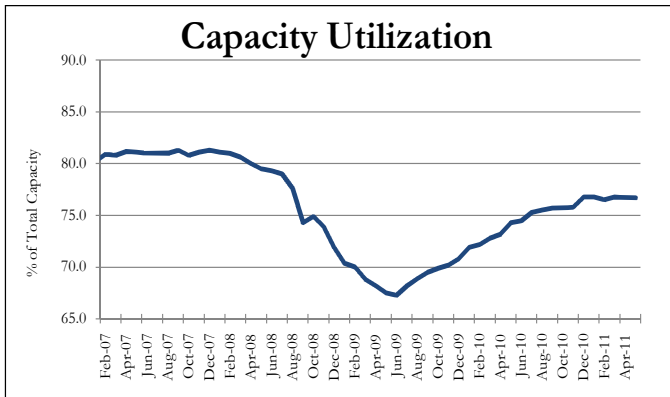
Consumer confidence: Pullback to More Cautious Tone.

Consumer confidence hit a 7-month low in June, dropping to 58.5 from 61.7 in May (*See Consumer Confidence chart, next page*). This is lower than we had expected. Consumers have come down hard from their post-recession euphoria earlier in the year, and now they just cannot seem to shake off their doubts. This is because job market prospects seem bleak and the news media have been amplifying these negative signals. Furthermore, debt ceiling discussions and resulting public political tensions in Washington and Europe over sovereign debt issues are keeping public sentiment on edge.



Industrial production: Slow But Positive Expansion.

Industrial production rose ever so slightly in May. Manufacturing, which accounts for three quarters of the overall index, posted a monthly gain of 0.4%. Capacity utilization remained unchanged from April at 76.7% and now stands about 4% below its historical average (See *Capacity Utilization chart below*). The ISM Manufacturing Index declined in May to 53.5, 6.9 points lower than April. The index has now declined for three straight months. All ten sub-indexes recorded declines in May, underscoring the moderation in the pace of manufacturing activity. Despite the sharp deceleration, the overall index remains above the 50-mark, indicating manufacturing expansion. While manufacturing experienced a sharp rebound in the early stages of the recovery, it is not unusual for the sector to consolidate some of the gains and slow down later. The basic message here is that the factories continue to expand although the pace of expansion has moderated.

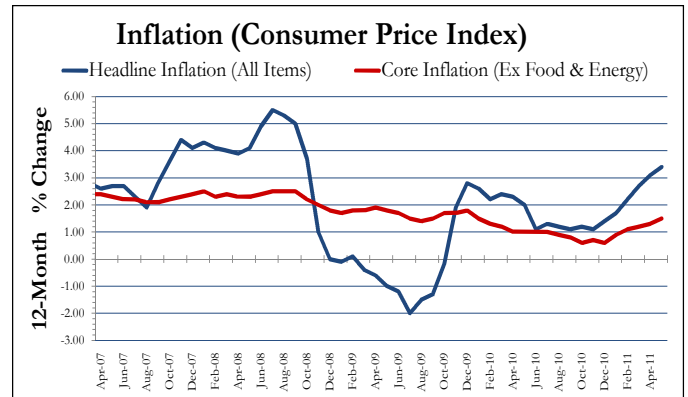


Housing: Continued Struggles. Housing will continue to be the key domestic downside risk to our economic outlook. The ongoing troubles in the housing market were apparent in May's housing data. Existing home sales, which account for more than 90% of the market, declined by about 4% to

their lowest level since the beginning of the year, and new home sales decreased by about 2%. At the same time, with distressed sales continuing to weigh on prices, the S&P Case-Schiller index reached fresh lows in the first quarter of 2011. As long as home prices are declining, there can only be limited improvement in household balance sheets.

There are a number of reasons to be encouraged somewhat about the long-run prospects for housing. In the near term, supply issues will dominate the outlook, no question. Adding the inventory of existing homes to the shadow inventory of potential foreclosures, it will take well over a year at the current sales pace to clear the excess inventory of homes. However, do not forget that every month the U.S. adds more new jobs, the prospects for improved home sales brighten. Furthermore, we cannot ignore the fact there is virtually no new supply entering the market through construction – the number of new homes being built is barely above the number of homes lost to demolition each year. This fact, coupled with falling delinquency rates means that the stock of foreclosures is starting to recede and progress in clearing the housing market is being made.

Inflation: Core Inflation Moderate. The U.S. Consumer Price Index (CPI) advanced 0.2% in May leading to an annual inflation rate of 3.5%. The core CPI inched up 0.2% which translates into an annual core inflation of 1.5% (See *Inflation chart below*). We expect core inflation to average close to 2% in 2011. A slowly declining unemployment rate will keep real wages under check. This will restrain unit labor costs, defusing one of the possible catalysts for higher inflation.



Labor Market: Short Term Setback. Non-farm payrolls rose by just 54,000 in May compared to the 200,000 plus pace seen during the previous three months. Government payrolls dropped by 29,000, mainly due to cuts in state and local jobs. The unemployment rate rose to 9.1% from 9.0% in

April. This modest increase is not unexpected as previously discouraged workers continue to return to the job market, swelling the labor pool.

Recent initial jobless claims remain stuck above the 400,000 mark suggesting fairly lackluster job growth in the next two months. Sluggish job numbers also highlight the fragile nature of the U.S. economic recovery and its limited capacity to absorb shocks. However, as long as energy prices return to a reasonable level and remain somewhat stable and manufacturing disruptions created by Japan's earthquake recede, we remain cautiously optimistic that job growth will move back above the 200,000 level during the second half of 2011.

Federal Reserve Board: Remains Accommodative. The highly anticipated Federal Open Market Committee's statement in June acknowledged that underlying inflation is no longer perceived as "subdued." As the Federal Reserve comes to the end of its second asset purchase program (QE2), this change in the Fed's tone and language was an important signal to the markets and highlighted that core inflation is gradually inching higher. While some are calling for a third formal round of quantitative easing we believe additional monetary stimulus is not warranted. The cost-benefit tradeoff has turned less attractive towards additional stimulus as more stimulus could contribute to the mispricing of risk in financial markets. What is more, the QE2 program was effective in shifting the economy from a deflationary to an inflationary mode. It also prodded investors to take on more risk and thereby increase asset prices. At this point, with inflation on the upswing and long-run inflation expectations no longer flashing deflation fears, the Fed will end this program

European Sovereign Debt: Ongoing Concern. The European sovereign debt crisis remains a major risk to the global economic outlook. A second financial assistance program that would allow Greece to continue consolidating its fiscal position without the need to issue debt for the next three years has just been approved by the EU-IMF. The first EU-IMF program assumed Greece would have to raise approximately €53 billion over the next two years. Greek progress towards fiscal consolidation has fallen short of expectations – due to sharp contraction in economic activity – causing it to miss most of the conditional targets imposed in the first program. This has generated market skepticism – ourselves included – regarding the ability of Greece to

honor its debt obligations under the original terms. As we have been saying nearly since this crisis began Greece will eventually have to restructure its debt.

How that event takes place is extremely difficult to predict because, among other things, it has to do more with politics than with economics. Consequently, there is a vast range of alternative scenarios which could play out depending on the timing and the characteristics of the restructuring. In the mean time, there will be plenty of tension surrounding this issue to roil the markets.

Economic Outlook: Yes, a Soft Patch, But Tailwinds Will Prevail. The current slowing in economic growth is due to a number of factors including the sovereign debt problem in Europe, rising energy costs due to political unrest in the Middle East, slowing economic growth in the leading emerging markets and supply chain disruptions following Japan's earthquake. In the U.S., a rash of poor weather has also contributed to slower economic growth. Some of these headwinds are temporary and need to be recognized as such. Remember, the combination of all of these factors have not caused a break in growing economic activity, just a slowing. A number of forces remain important positive tailwinds to economic expansion including accommodative monetary and fiscal policies, high levels of liquidity, strong profit growth and reasonable equity valuations and growing corporate earnings. In addition, industrial production levels have started to increase as inventories drop. On balance, we expect these positive forces to prevail, but that may take some time and will unfold unevenly, meaning that continued investment patience is required.

An additional issue that has some investors concerned is the ongoing debate over potentially raising the debt ceiling and what it will mean for spending levels. An inability to raise the debt ceiling by the end of July certainly would lead to higher interest rates and a drop in the value of the dollar. Unfortunately, we believe the debate/negotiations among lawmakers in Washington, D.C. will go down to the wire but the debt ceiling will ultimately be raised. That increase will be part of a broader agreement on spending cuts over the long term. We expect to see modest cuts in defense spending, a cap on discretionary spending levels and some cuts in second-tier entitlement programs, but no meaningful cuts in core entitlement programs like Medicaid, Medicare or Social Security given the magnitude of the social change required and the election cycle in 2012.

U.S. economic growth slowed considerably in the first half of this year. The moderation was due in part to temporary factors that have since eased or will abate in the coming months. As a result, economic growth is likely to rebound in the second half of the year. Nonetheless, the economic recovery will remain constrained by the more long lasting legacies of the financial crisis. In particular, while progress is being slowly made in the housing market, it will take several years and unfortunately additional home price declines to clear the market of its excess inventory. Moreover, the need to rein in public spending is rapidly approaching. In an environment of slow economic progress and a still elevated unemployment rate, monetary policy is likely to remain accommodative over the next several quarters. Yet, as long as the economy continues to move forward, the need for emergency measures also diminishes. No doubt we are in a risk-filled recovery, but also one in which gradual progress is a major theme.

The balance of risk in the global markets is tilted to the downside, with a disorderly resolution to the Greek debt crisis playing a key role in our risk assessment. Other risk factors include a sharp economic slowdown or debt crisis in China, another spike in crude oil prices due to geopolitical concerns in the Middle East, and accelerating inflation in the emerging markets. On the upside, a faster restoration of Japanese industrial production and a decline in crude oil prices due to the ebbing of geopolitical turmoil could help to shift the global economy into a higher gear.

The macro environment of slow-but-positive growth, low inflation and easy monetary policy remains conducive to higher equity prices, but investors are unable to look past near-term risks. Corporate earnings have been strong, and we are approaching the beginning of the second-quarter earnings season, but expectations have drifted lower due to weakness in the financial sector. The question, then, is what it will take to get the markets back on track? We are calling for a reacceleration in U.S. economic growth in the second half of 2011. Should that happen, it would reassure investors that the global recovery will persist, which would help stock prices to again move higher.

See Index Performance table, next page.

The equity markets demonstrated remarkable resiliency in the second quarter of 2011, fending off a series of disappointing news items and finishing the quarter with a positive surge. For the quarter, the results were mixed both here and abroad.

More defensive asset classes and sectors generally outperformed. In short, it was a “risk off” quarter. The S&P 500 Index was essentially unchanged for the period, gaining 0.10%. Growth indices generally outperformed value, and large cap stocks outperformed small caps.

Defensive economic sectors like Consumer Staples, Telecom/Utilities and Healthcare led the way amid signs of slowing economic growth. Previous market leaders tied to economic expansion like Industrials, Technology, Materials and Energy paused. The Financial sector continues to be under pressure.

International developed markets outperformed the U.S., posting positive returns while emerging market economies like China, India and Brazil contracted as policy makers in these countries continued to raise interest rates and reserve requirements. Energy dependent Russia cooled as oil prices contracted during the quarter. Europe, posted almost a 3% gain as it grapples with its internal debt problems.

Fixed income market segments posted positive total returns for the quarter. U.S. Treasury bonds posted a positive return as interest rates continue to remain low. Corporate credit also posted a positive return. In another example of “risk off”, High yield bonds lagged investment grade bonds in the period. Interestingly, municipal bonds led the way as value-oriented investors take advantage of what appears to be an oversold market. TIPS continued their advance as signs of inflation picked up. International bonds posted solid gains as the USD continues to slide in world currency markets in the face of a looming debt ceiling crisis.

Other Matters

In accordance with SEC regulations, we request that you contact us in the event that there have been any material changes in your financial circumstances or investment objectives, or if you wish to impose any reasonable restrictions on the management of your accounts or modify existing restrictions on the management of your accounts.

Index Performance as of June 30, 2011

	1 Month	QTD	YTD	1 Year	5 Year
Russell					
3000 Growth Index	-1.50	0.64	6.98	35.68	5.36
3000 Index	-1.80	-0.03	6.35	32.37	3.35
3000 Value Index	-2.08	-0.68	5.74	29.13	1.23
1000 Growth Index	-1.43	0.76	6.83	35.01	5.33
1000 Index	-1.75	0.12	6.37	31.93	3.30
1000 Value Index	-2.05	-0.50	5.92	28.94	1.15
Mid-Cap Growth Index	-1.60	1.61	9.59	43.25	6.28
Mid-Cap Index	-2.09	0.42	8.08	38.47	5.30
Mid-Cap Value Index	-2.57	-0.69	6.69	34.28	4.01
2000 Growth Index	-2.14	-0.59	8.59	43.50	5.79
2000 Index	-2.31	-1.61	6.21	37.41	4.08
2000 Value Index	-2.46	-2.65	3.77	31.35	2.24
S&P 500					
Consumer Discretionary	-0.19	3.45	8.33	40.52	5.48
Consumer Staples	-2.44	5.25	7.91	26.67	8.37
Energy	-1.88	-4.63	11.39	52.83	7.87
Financials	-2.80	-5.92	-3.06	12.84	-11.74
Health Care	-1.12	7.87	13.93	28.54	5.34
Industrials	-0.64	-0.67	8.03	38.07	3.35
Information Technology	-2.61	-1.37	2.06	25.75	6.73
Materials	-0.23	-0.88	3.62	45.34	6.80
Telecommunication Services	-1.27	2.11	7.06	39.01	5.35
Utilities	-0.10	6.14	9.06	23.86	4.79
Other U.S. Equity					
Dow Jones Industrial Avg	-1.10	1.42	8.59	30.37	4.97
MSCI USA	-1.70	0.21	6.18	31.47	3.17
Wilshire 5000 (Full Cap)	-1.70	-0.09	5.90	32.05	3.68
International Equity - Broad Market					
MSCI EAFE	-1.23	1.83	5.35	30.93	1.96
MSCI Emerging Markets	-1.50	-1.04	1.03	28.17	11.75
MSCI Frontier Markets	-0.87	0.02	-5.40	16.76	NA
MSCI AC World	-1.54	0.44	4.99	30.77	3.70
MSCI AC World ex USA	-1.42	0.61	4.11	30.27	4.14
MSCI AC Asia ex Japan	-2.27	0.09	1.30	26.02	11.81
International Equity - Country Region					
MSCI Brazil	-0.31	-4.04	-1.49	24.20	18.53
MSCI BRIC	-1.16	-3.33	-0.18	19.52	12.24
MSCI China	-3.67	-1.75	1.09	12.72	15.80
MSCI Europe	-1.89	2.85	9.59	36.82	2.63
MSCI India	1.77	-3.55	-8.48	7.99	13.55
MSCI Japan	1.47	0.18	-4.68	13.18	-3.64
MSCI EM Latin America	-0.33	-2.48	-1.57	26.32	16.75
MSCI Russia	0.46	-5.35	10.07	45.43	0.70
Fixed Income					
BC Aggregate Bond	-0.29	2.29	2.72	3.90	6.52
Merrill Lynch 3-month T-Bill	0.01	0.04	0.08	0.16	2.00
BC Government	-0.30	2.22	2.14	2.26	6.09
BC Credit Bond	-0.73	2.50	3.41	6.20	7.03
BC High Yield Corporate Bond	-0.97	1.05	4.97	15.63	9.30
BC Muni Bond	0.51	4.06	4.59	3.64	4.97
BC TIPS	0.81	3.66	5.81	7.74	6.91
BofA ML Global Broad Market Ex USD	0.30	3.64	5.49	15.22	7.49
BofA ML Global Broad Market	0.04	3.05	4.28	10.08	7.07
BofA ML Emerging Market Credit	1.46	3.70	7.77	19.26	10.92
Alternative Investments					
NAREIT Equity REIT Index	-3.07	2.90	10.61	34.08	2.61
DJ-UBS US Commodity Index	-5.04	-6.73	-2.58	25.91	-0.05