

QUARTERLY INVESTMENT REVIEW

SECOND QUARTER 2011



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MARKETS OVERVIEW

Second Quarter 2011

- Despite weaker-than-expected economic data in the US and Europe's sovereign debt crisis, equity markets around the world were little changed in the second quarter. The broad US market was flat for the quarter.
- In US dollar terms, the overall performance in other developed markets was slightly positive, but that positive performance was entirely due to currency fluctuations. As in most of the past few quarters, there was much dispersion in performance at the individual country level. Greece, which once again had to be bailed out by the European Union and the International Monetary Fund to avoid defaulting on its sovereign debt, had sharply negative returns for the quarter. At the other end of the spectrum, New Zealand and core European countries such as Germany and France had strong positive returns. The US dollar lost ground against all major currencies, which helped the dollar-denominated returns of developed market equities.
- Emerging markets had negative returns and trailed developed markets in the quarter. As in developed markets, there was much dispersion in the performance of different emerging markets. Indonesia and other small emerging markets in Asia did well. On the other hand, some of the largest emerging countries such as China, Brazil, India, and Russia had sharply negative returns and were among the worst performers. The US dollar also lost ground against the main emerging market currencies, which contributed positively to the dollar-denominated returns of emerging market equities.
- Value stocks underperformed growth stocks across all market capitalization segments in the US and in other developed markets. In emerging markets, however, value stocks had mixed performance relative to growth stocks: small cap value outperformed small cap growth, while large cap value underperformed large cap growth. Along the market capitalization dimension, small caps underperformed large caps in the US and in other developed markets, but not in emerging markets.
- Most fixed income securities had excellent returns, especially inflation-protected securities.
- Real estate securities had strong returns and excellent performance relative to other asset classes.

Three Years as of June 30, 2011

- Equity markets around the world had mixed performance in the three years that ended in June. In US dollar terms, developed non-US markets, which had negative returns, were the worst performers. On the other hand, the US equity market, and especially emerging markets, had positive but below-average performance. In the US, the value effect was negative across all market capitalization segments. On the other hand, the value effect was positive across all market capitalization segments, especially among small cap stocks, in developed non-US markets and in emerging markets. With regard to the size effect, small cap stocks greatly outperformed large cap stocks in the US, in developed non-US markets, and in emerging markets.
- The US dollar had mixed performance against major currencies. It sharply depreciated against the yen, Swiss franc, and the Canadian and Australian dollars, but appreciated against the British pound and the euro. As a result, currency fluctuations had a small positive impact of around 0.8% per year on the dollar-denominated returns of developed market equities.
- The US dollar also had mixed performance against the main emerging markets' currencies, and the net impact of currency fluctuations on the dollar-denominated returns of emerging markets strategies was even more muted, approximately 0.4% per year.
- Fixed income delivered annual returns that ranged from 2.0% to 6.5%.
- Real estate securities in the US had positive returns over the three-year period that ended in June and outperformed the broad US equity market. On the other hand, real estate securities in other developed markets had very weak but positive returns and were one of the worst-performing asset classes.

US STOCKS

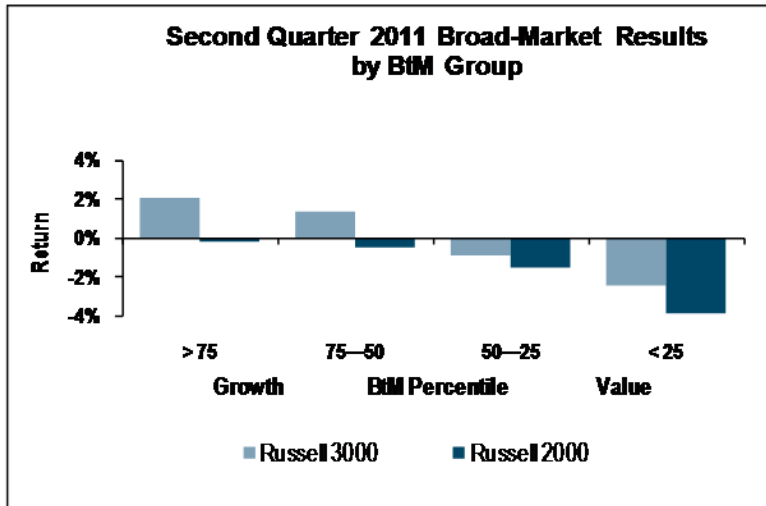
- After a first quarter with very strong performance that continued into April, the US equity market saw a sharp reversal in early May that lasted until the middle of June, as growing concerns about the economic recovery in the US and the sovereign debt crisis in Europe led investors away from risky assets. However, the quarter ended with a very strong rally in the last week of June, as investors reacted positively to better-than-expected economic data in the US and the announcement of another bailout package for Greece that allows that country (at least, temporarily) to avoid defaulting on its debt. The daily volatility of the US market remained moderate. The percentage of trading days with big market movements (defined as days during which the broad US market moved by more than 1% in absolute value) was 25%, compared to about 21% in the first quarter.
- Another measure of volatility, the Chicago Board Option Exchange's VIX, which measures the volatility of the S&P 500 Index and has a historical average of around 20, stood at approximately 18 at the beginning of the quarter and increased to slightly above 20 at the end of the second quarter. Quarterly returns for the broad US market, as measured by the Russell 3000 Index, were flat. Asset class returns ranged from -2.7% for small cap value stocks to 0.8% for large cap growth stocks. The strongest sectors were health care and consumer staples, while the weakest ones were financials and energy.
- Value had poor performance relative to growth in the second quarter in all market capitalization segments. Using the Russell Indexes as proxies, small cap value stocks (Russell 2000 Value) underperformed small cap growth stocks (Russell 2000 Growth) by 2.1% in the second quarter. Large cap value stocks (Russell 1000 Value) underperformed large cap growth stocks (Russell 1000 Growth) by 1.3% in the quarter. Over the three-year period that ended June 30, the Russell 2000 Value Index underperformed the Russell 2000 Growth Index by 1.3% annualized, while the Russell 1000 Value Index underperformed the Russell 1000 Growth Index by 2.7% annualized.
- Along the market capitalization dimension, small caps (Russell 2000) underperformed large caps (Russell 1000) by 1.7% in the second quarter. Over the three-year period that ended in June, however, small cap stocks outperformed large cap stocks by 4.1% on an annualized basis.

As of June 30, 2011	Return (%)		
	Second Quarter	One Year	Three Years Annualized
Russell 3000	(0.03)	32.37	4.00
Russell 2500	(0.59)	39.28	8.18
Russell 2000	(1.61)	37.41	7.77
Russell 2000 Value	(2.65)	31.35	7.09
Russell 2000 Growth	(0.59)	43.50	8.35
Russell Micro Cap	(3.48)	32.70	6.48
Russell 1000	0.12	31.93	3.68
Russell 1000 Value	(0.50)	28.94	2.28
Russell 1000 Growth	0.76	35.01	5.02

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US STOCKS

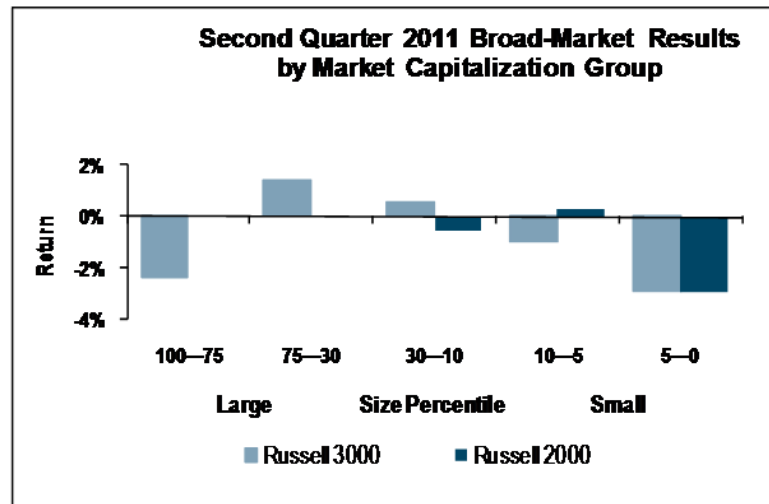
- A look at the determinants of equity performance—relative price and market capitalization—provides some insight into the sources of returns. Historically, value stocks, as measured by the ratio of book-to-market equity (BtM), have outperformed growth stocks, but that was not the case in the second quarter.



- For the Russell 3000 Index and the Russell 2000 Index, the best performance came from deep growth stocks in the 75th–100th BtM percentile range, while the worst performance came from deep value stocks in the 0–25th BtM percentile range.

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- For the Russell 3000 Index, the best performance came from the smaller stocks in the large cap universe, those in the 30th–75th market capitalization percentile range, while the worst performance came from micro cap stocks in the 0–5th market capitalization percentile range.
- For the Russell 2000 Index, the best performance came from the larger stocks in the small cap universe, those in the 5th–10th market capitalization range, while the worst performance came from the smallest stocks in the small cap universe, those in the 0–5th market capitalization percentile range.



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NON-US STOCKS

- After an excellent April, developed non-US equity markets saw a sharp reversal in early May that lasted for almost the rest of the quarter, as growing concerns about the global economic recovery and the sovereign debt crisis in Europe led investors away from risky assets. But following the announcement of another bailout package for Greece in late June that allowed that country to avoid defaulting on its debt (at least, temporarily), developed non-US markets rallied strongly in the last week of June and finished the quarter with a slightly positive return in US dollar terms. That positive return, however, was entirely due to the impact of currency fluctuations. The dollar-denominated quarterly return for developed markets, as measured by the MSCI World ex USA Index (net dividends), was 0.9%.
- As in most of the past few quarters, there was much variation in performance at the country and asset class levels. For instance, the difference in the quarter between the best-performing developed market, New Zealand, and the worst-performing one, Greece, was about 26% (9.8% vs. -16.1%).
- Commodity-rich countries such as Norway, Canada, and Australia, which were negatively impacted by the sharp fall in commodity prices, also did very poorly in the quarter.
- On the other hand, Germany, where the economic recovery has been very robust, and other core European countries such as Switzerland and France had outstanding returns in the quarter.
- The weakness of the US dollar against most major currencies aided developed market equity returns for US investors. The US dollar's depreciation ranged from 9.3% against the Swiss franc to 0.1% against the British pound in the quarter. The overall impact of currency fluctuations between the US dollar and developed-country currencies was to increase the dollar-denominated returns of developed market equities by about 2.2%.
- Energy and information technology were the worst-performing sectors in the quarter, while health care and consumer staples were the top performers.

Non-US Equity Returns

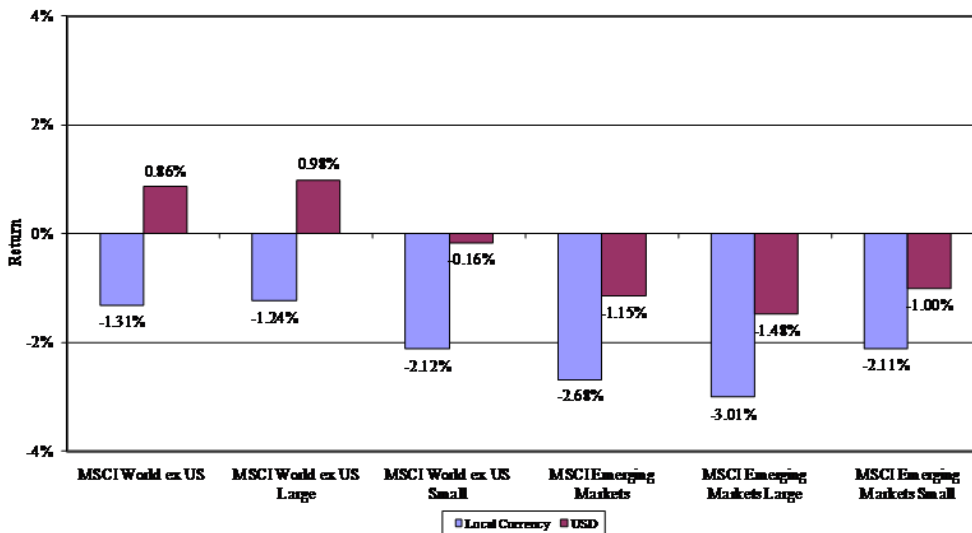
As of June 30, 2011	Return (%)		
	Second Quarter	One Year	Three Years Annualized
MSCI EAFE Small Cap	0.85	36.41	3.26
MSCI World ex USA Small	(0.16)	37.05	3.72
MSCI EAFE	1.56	30.36	(1.77)
MSCI World ex USA	0.86	30.33	(1.56)
MSCI EAFE Value	0.98	29.35	(1.74)
MSCI EAFE Growth	2.11	31.25	(1.85)
MSCI Emerging Markets	(1.15)	27.80	4.22
MSCI Emerging Markets Small	(1.00)	25.22	11.93

MSCI indices are total returns net of foreign withholding taxes on dividends. MSCI data copyright MSCI 2011, all rights reserved. Indices are not available for direct investment; their performance does not reflect the expenses associated with the management of an actual portfolio. Past performance is not a guarantee of future results.

NON-US STOCKS

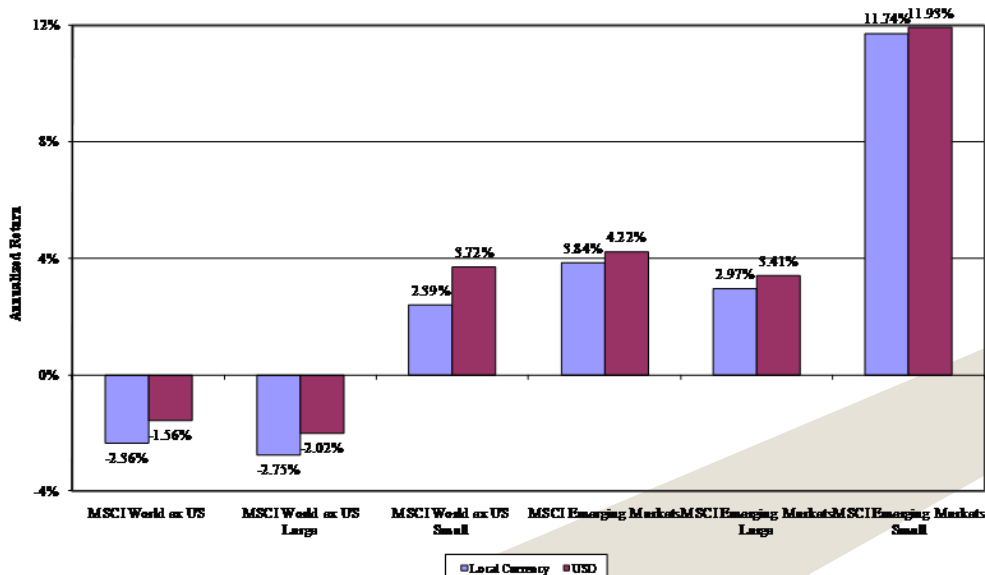
- Using the MSCI World ex USA Index and its sector and country segments as proxies, value stocks in developed markets underperformed growth stocks across both size categories in the quarter. Small cap value stocks (MSCI World ex USA Small Cap Value) underperformed small cap growth stocks (MSCI World ex USA Small Cap Growth) by 1.0%, while large cap value stocks (MSCI World ex USA Large Cap Value) underperformed large cap growth stocks (MSCI World ex USA Large Cap Growth) by 0.7%.
- Over the three-year period through June 30, however, the value effect was positive in large and small cap stocks. Large cap value stocks outperformed large cap growth stocks by 0.8% on an annualized basis, while small cap value stocks outperformed small cap growth stocks by 3.0% annualized.
- Along the market capitalization dimension, small caps (MSCI World ex USA Small Cap) underperformed large caps (MSCI World ex USA Large Cap) by 1.1% in the quarter. However, over the three-year period that ended in June, small cap stocks outperformed large cap stocks by an annualized 5.7%.

**Second Quarter Currency Effects on Non-US Equity Returns
As of June 30, 2011**



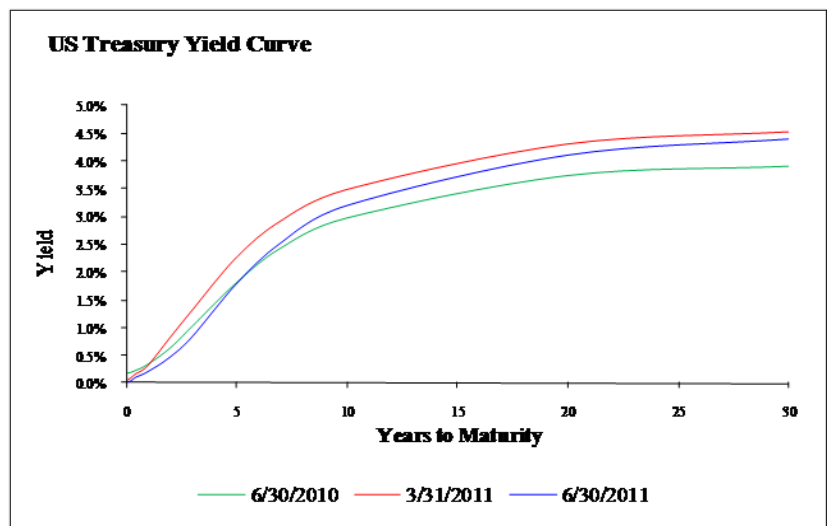
MSCI indices are total returns net of foreign withholding taxes on dividends. MSCI data copyright MSCI 2011, all rights reserved. Indices are not available for direct investment; their performance does not reflect the expenses associated with the management of an actual portfolio. Past performance is not a guarantee of future results.

**Three-Year Currency Effects on Non-US Equity Returns
As of June 30, 2011**



BONDS

- The Federal Open Market Committee maintained its target range for the federal funds rate between 0.00% and 0.25% in the second quarter, and reaffirmed its goal to maintain that target at very low levels for an extended period.
- In addition, the FOMC decided during its second-quarter meetings to complete the purchase of \$600 billion of long-term Treasury bonds by the end of the second quarter.
- However, even as it indicated that economic activity slowed in the second quarter, the FOMC did not announce any new plans to extend its asset-purchasing programs any further in the foreseeable future.
- As a result of the Fed's quantitative easing program, the Federal Reserve's balance sheet, currently the main focus of monetary policy actions, expanded from about \$2.67 trillion at the end of March to about \$2.91 trillion at the end of June.
- Yields on very short-term Treasury bills fell slightly in the second quarter relative to the end of the first quarter, while yields on longer-term Treasury securities fell more sharply, as investors rushed to the safety of US Treasury securities in light of weak economic data in the US and concerns about Europe's ability to resolve its sovereign-debt crisis. As a result, the yield curve flattened. The difference in yield between ten-year Treasury bonds and one-month US Treasury bills was 317 basis points at the end of the second quarter, compared with 342 basis points at the end of March. Compared to June 2010, however, yields were higher at intermediate- and long-term maturities, as was the difference in yield between ten-year Treasury bonds and one-month US Treasury bills. Relative to the second quarter of 2010, the yield curve steepened in the second quarter of 2011.



As of June 30, 2011

Index Returns	Return (%)		
	Second Quarter	One Year	Three Years Annualized
Merrill Lynch Three-Month US T-Bill	0.04	0.16	0.42
Merrill Lynch One-Year US Treasury Note	0.20	0.67	1.57
Citigroup World Government Bond 1-3 Years	0.49	0.70	2.74
Barclays Capital US Government Bond	2.22	2.26	5.09
Merrill Lynch US Treasury/Agency 1-5 Years	1.42	2.10	3.97
Citigroup World Government Bond 1-5 Years	0.84	0.87	3.51
Barclays Capital US TIPS	3.66	7.74	5.28

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REAL ESTATE INVESTMENT TRUSTS (REITs)

- Real estate securities had strong returns in the second quarter and excellent performance relative to other asset classes. In the US and in other developed markets, they were the top-performing asset class.

As of June 30, 2011

Index Returns	Return (%)		
	Second Quarter	One Year	Three Years Annualized
Dow Jones US Select REIT	3.97	34.95	4.71
S&P Global ex US REIT	5.01	42.82	1.82
S&P Global REIT	4.22	37.78	3.65

Dow Jones data (formerly Dow Jones Wilshire) provided by Dow Jones Indexes. S&P/Citigroup data is gross dividends, provided by Standard & Poor's Index Services Group. Indices are not available for direct investment; their performance does not reflect the expenses associated with the management of an actual portfolio. Past performance is not a guarantee of future results.