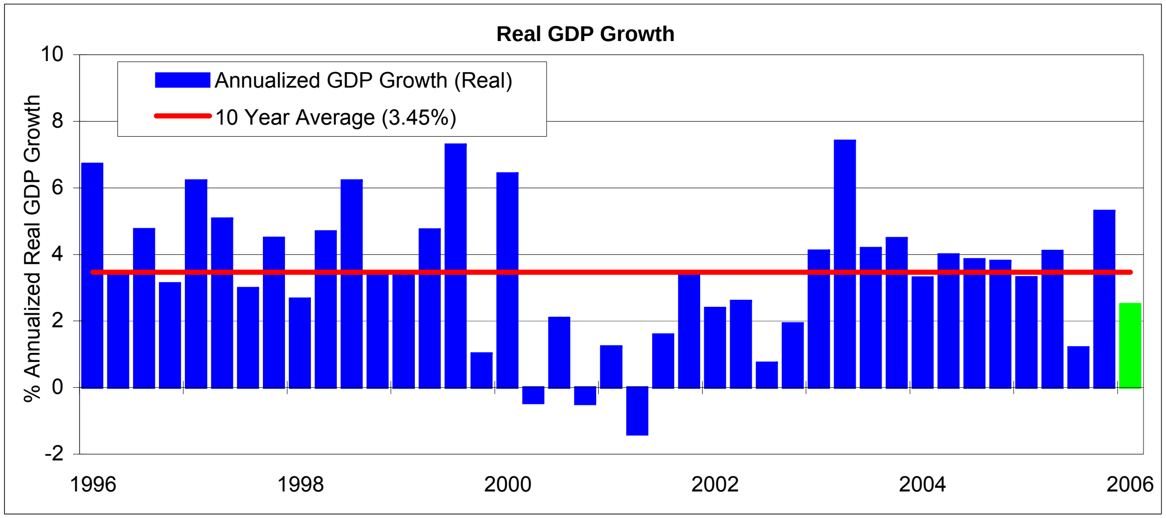
Economic Growth

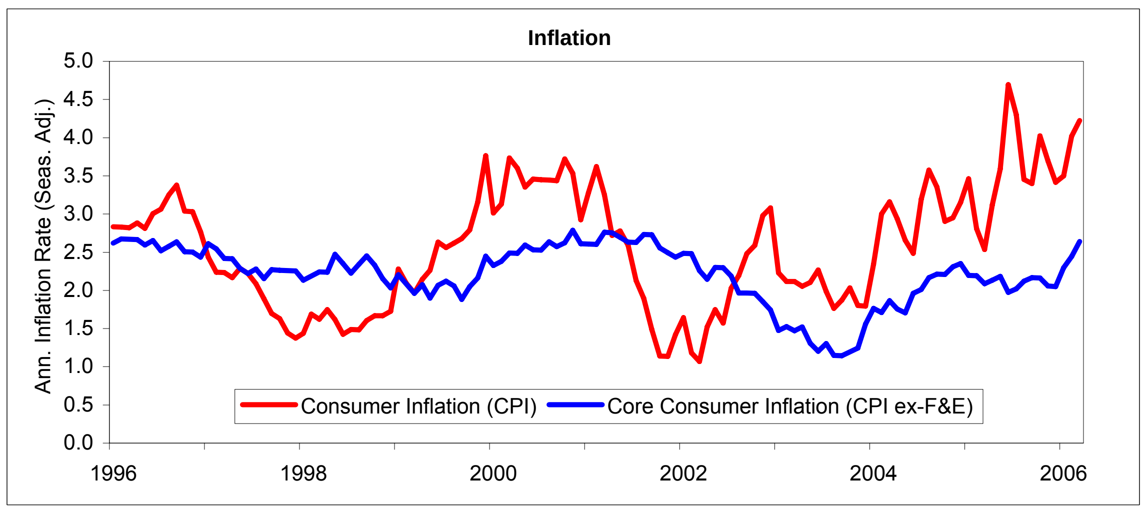


Source: Bureau of Economic Analysis. Green indicates preliminary estimate.

- The final estimate of first quarter 2006 real GDP growth was revised upward to 5.6% from 5.3%. The largest factor in the upward adjustment was a lower negative drag from net exports, generated by slower growth in imports.
- Data released from the Commerce Department revealed a preliminary GDP rate of 2.5% for the second quarter. Many economists also expect slower growth in the second half of 2006, around 2.9% (real, annualized).
- Consumer spending and the housing outlook are areas of concern for the economy. For consumers, rising mortgage interest payments and higher energy prices may stymie spending.

Inflation

- The June 0.3% increase in core consumer prices (excluding food and energy) marked the fourth straight month at that pace.
- The Labor Department's consumer price report showed that core consumer prices are 2.6% higher than a year ago. Over the past three months, overall consumer prices (excluding food and energy) have risen 3.6%.
- June marked the first decline in energy prices since February, but rising shelter costs continued to spur inflation.



Source: Bureau of Labor Statistics; Federal Reserve Bank of St. Louis

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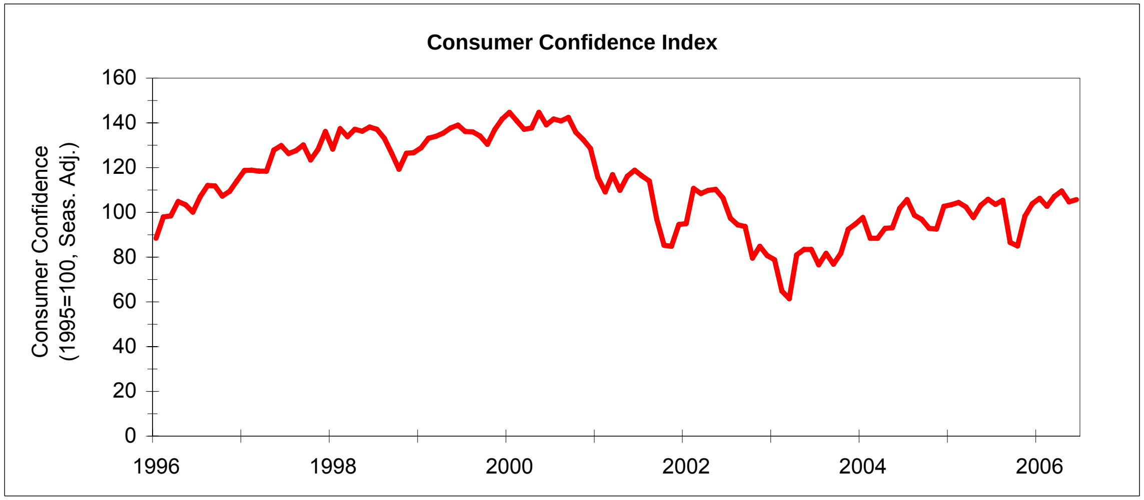
Consumer Confidence

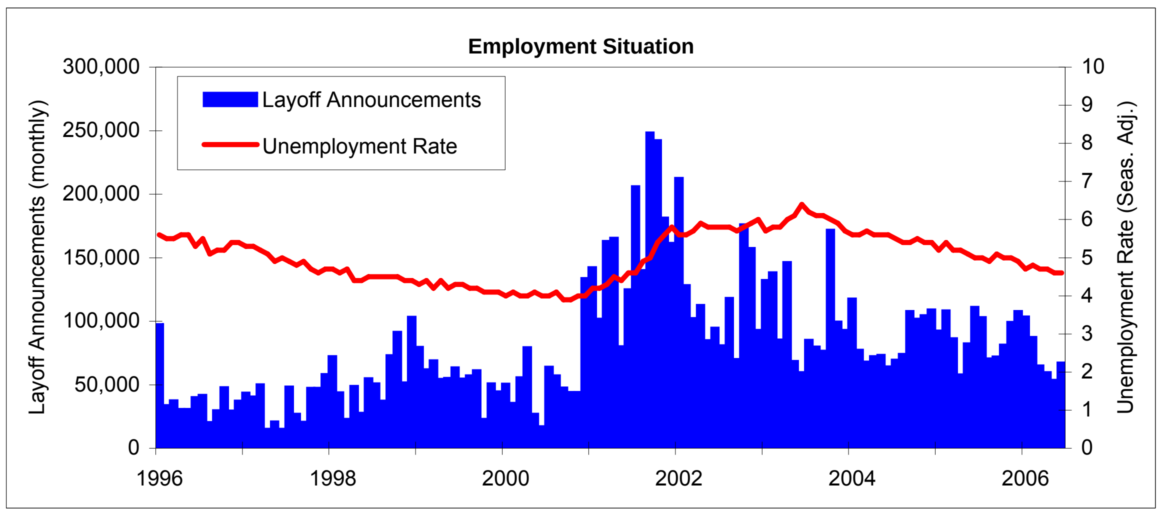


Source: The Conference Board

- The Consumer Confidence Index was mostly flat in the second quarter. Consumers remain concerned about the short-term outlook.
- The Conference Board's survey of 100 CEOs and business leaders revealed that CEOs are growing more pessimistic, with only 21% of business leaders expecting economic conditions to improve in the coming months.
- Of the executives surveyed, 75% anticipate increased profits over the next year. Those in the non-durable goods industries are the most optimistic with 80% expecting higher profits, while only 66% of leaders in the service industry foresee profit growth.

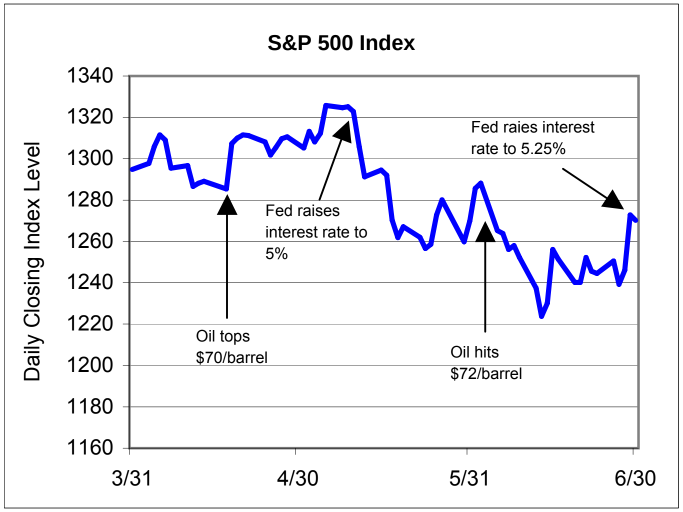
Employment Situation

- The U.S. unemployment rate remained relatively unchanged in the second quarter at 4.6%, compared to 4.7% at the end of the first quarter.
- According to the Labor Department, job growth was below expectations for each month of the second quarter, which may be a signal that economic growth is decelerating. Non-farm payrolls grew by 121,000 in June, 92,000 in May, and 112,000 in April.
- At quarter-end, average hourly earnings were up 3.9% from a year earlier, the fastest year-to-year growth since June 2001.



Source: Bureau of Labor Statistics; Challenger, Gray & Christmas, Inc.

US Stock Market Highlights



Source: Yahoo! Finance

Sector Performance

	Quarter	Year
Consumer Disc.	(0.6)	3.0
Consumer Staples	2.9	8.1
Energy	4.1	24.4
Financials	(0.1)	12.5
Health Care	(5.1)	(1.2)
Industrials	0.1	14.4
Info. Technology	(9.9)	0.9
Materials	(0.3)	21.2
Telecom. Services	(0.6)	10.4
Utilities	5.8	6.0

- The S&P 500 Index finished the quarter at 1270.2, down 1.4% for the quarter but still up 2.7% for 2006.
- Stocks have been volatile, especially the Nasdaq Composite. During April it was up more than 7.0% but it gave up all of those gains in May and June, finishing the quarter down 7.2%.
- Mergers and acquisitions activity continued to be strong as deal-making produced the third most active quarter since 1985. Among the deals announced include Wachovia's $25B offer for Golden West Financial and Johnson & Johnson's deal for Pfizer's Consumer Healthcare division.

Equity Market Performance

- Small cap continued to outperform large cap for the year, with the Russell 2000 up 8.2% for 2006, outpacing the Russell 1000 by 540 basis points.
- Value has outperformed growth in both the large cap and small cap spaces both in the second quarter and year-to-date. Over one year, however, small cap growth and value have been even at 14.6%.
- Concerns with energy prices led to increased volatility during the quarter. The Chicago Board of Options' Volatility Index (VIX), a key measure of market expectations of near-term volatility, reached its highest level since March 2004.

	Quarter	YTD	One Yr	Three Yrs	Five Yrs	Ten Yrs
Core Index Performance:						
Standard & Poor's 500	(1.4)	2.7	8.6	11.2	2.5	8.3
S&P 500 Equal Weighted	(2.1)	4.0	11.9	16.8	8.0	11.3
Dow Jones Industrial Average	0.9	5.2	11.1	9.9	3.4	9.1
Russell 1000	(1.7)	2.8	9.1	12.0	3.1	8.6
Russell 2000	(5.0)	8.2	14.6	18.7	8.5	9.1
Russell 3000	(2.0)	3.2	9.6	12.6	3.5	8.5
Russell Mid Cap	(2.6)	4.9	13.7	19.9	9.9	12.1
Style Index Performance:						
Russell 1000 Growth	(3.9)	(0.9)	6.1	8.4	(0.8)	5.4
Russell 1000 Value	0.6	6.5	12.1	15.7	6.9	10.9
Russell 2000 Growth	(7.3)	6.1	14.6	16.3	3.5	4.1
Russell 2000 Value	(2.7)	10.4	14.6	21.0	13.1	13.3

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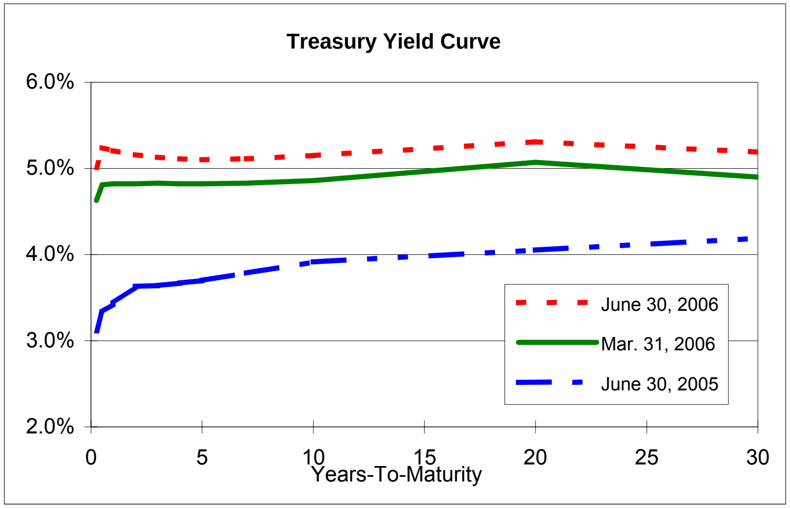
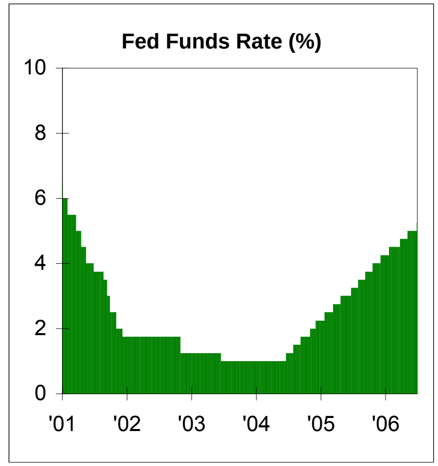
Interest Rate Environment



Source: State Street Corp.



Source: Federal Reserve

- The Federal Reserve raised its short-term interest rate target for the 16th and 17th consecutive times. The 25 basis point increase on the final day of the quarter lifted the fed funds rate to 5.25%.
- On July 19th, Fed Chairman Bernanke told the Senate Banking Committee that he saw signs of moderating economic growth and an ease in inflation, indicating a possible end to interest rate raises.

Bond Markets

- In the bond sector, yields on Treasuries finished the quarter higher, though the yield curve stayed essentially flat with the two-year treasury at 5.158% and the ten-year treasury at 5.145%.
- Debt issuance continued to be strong as companies eagarly locked in bonds at low rates before imminent Fed rate increases pushed bond yields higher. Issuance of investment-grade bonds in the U.S. hit its second-highest total on record at $22.9 billion. Issuance of high-yield debt also boomed, reaching its highest level since 2004.

	Quarter	YTD	One Yr	Three Yrs	Five Yrs	Ten Yrs
Index Performance:						
LB Aggregate	(0.1)	(0.7)	(0.8)	2.1	5.0	6.2
LB US TIPS	0.5	(1.8)	(1.7)	3.8	7.0	n/a
90 Day US Treasury Bills	1.2	2.2	4.0	2.4	2.3	3.8
Maturity Evaluation:						
LB 1-3 Yr Treasury	0.6	1.0	1.8	1.4	3.1	n/a
LB Intermediate Treasury	0.5	0.5	0.9	1.1	3.5	5.0
LB Long Treasury	(0.3)	(2.1)	(3.1)	0.7	4.9	n/a
Issuer Performance:						
LB Intermediate Agency	0.3	0.4	0.6	1.6	4.5	5.8
LB U.S. Credit	(0.4)	(1.6)	(2.1)	2.0	5.7	6.5
LB Mortgage	0.0	(0.1)	0.4	2.9	4.7	6.1
LB High Yield	0.3	3.2	4.8	8.6	8.7	6.5
JPM Emerg. Mkts Bond Index	(2.4)	(0.7)	5.3	10.2	11.4	11.9
Non-US Gov't Bond (Hedged)	0.0	(0.9)	0.2	3.1	4.3	6.8

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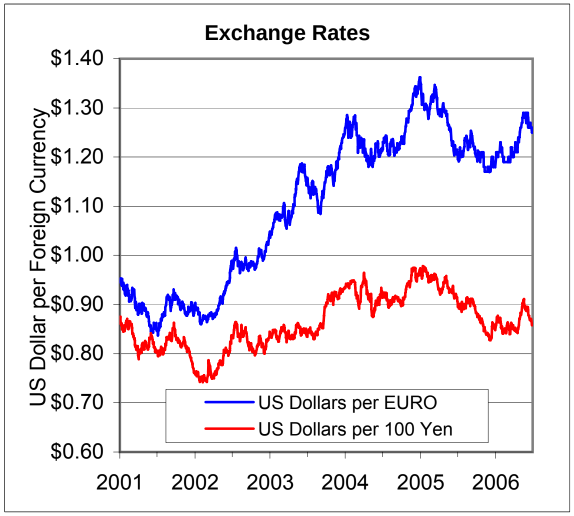
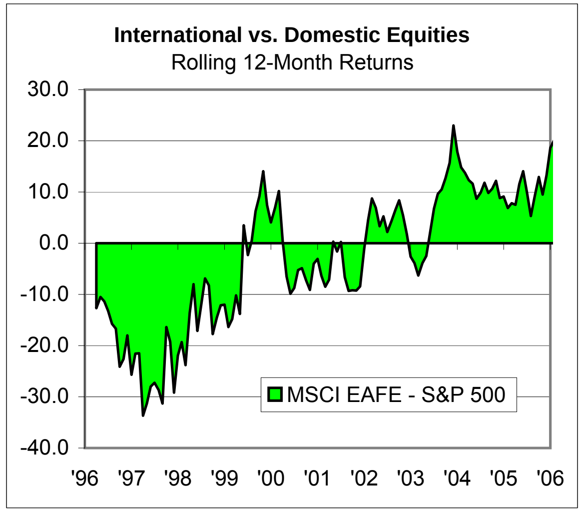
International Market Environment



Source: Federal Reserve Bank, Daily Press



Source: Ibbotson

- The U.S. Dollar Index, which trades on the New York Board of Trade and measures the dollar's performance against a trade-weighted basket of six major currencies, fell 5.1% in the quarter. The euro strengthened 5.5%, while the yen was 2.9% stronger against the dollar.
- Much of the dollar's decline occurred during the last two days of June, falling more than 1% after the Fed raised the interest rate to 5.25%.
- International stocks outperformed domestic stocks by 250 basis points during the quarter. Over the last three years, the MSCI EAFE Index has beat the S&P 500 Index by over 13%, annualized.

International Equity Market Performance

- Global equities suffered during the second quarter due to fears of inflation and higher interest rates in the United States.
- The MSCI Japan fell 4.6% during the quarter. Japan is poised to see interest rates rise this year for the first time in a decade. In Europe, the European Central Bank raised rates to 2.75%.
- Emerging markets stocks fell 4% over the quarter in a volatile market. Stocks touched an all-time high on May 8 and then lost 24%, declining steadily over the following five weeks before rallying in the final two weeks of the quarter. Year to date through 30 June, the MSCI Emerging Markets Index returned 7%.

	Quarter	YTD	One Yr	Three Yrs	Five Yrs	Ten Yrs
Broad Index Performance:						
MSCI EAFE	0.9	10.5	27.1	24.4	10.4	6.8
MSCI World	(0.3)	6.4	17.5	17.4	6.2	7.4
MSCI EAFE ex. Japan	2.8	13.5	24.7	24.3	11.5	9.8
MSCI Emerging Markets	(4.3)	7.3	35.9	34.8	21.5	n/a
MSCI EAFE Small Cap	(3.7)	6.6	28.8	33.1	18.9	n/a
Style Index Performance:						
MSCI EAFE Growth	0.4	9.6	26.3	21.4	8.5	4.2
MSCI EAFE Value	1.5	11.5	27.8	27.4	12.4	9.2
Regional Index Performance:						
MSCI Europe ex-UK	1.8	14.2	27.8	25.5	11.4	10.9
MSCI United Kingdom	4.9	13.6	20.9	21.3	n/a	n/a
MSCI Japan	(4.6)	2.0	36.0	25.2	n/a	n/a
MSCI Asia	(2.0)	7.5	28.4	28.7	n/a	n/a
MSCI Latin America	(3.1)	12.1	51.2	48.7	24.4	14.0

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Alpha & Beta

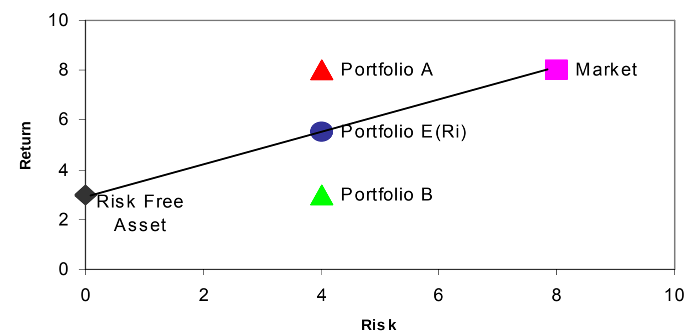
- Generally speaking, alpha is an investment manager's value added over an index fund (beta).
- Technically speaking, it is the error term in the Capital Asset Pricing Model (CAPM), or the portion of portfolio return not explained by the market factor.

$$E(R_i) = R_f + \beta * (R_m - R_f) + \alpha$$

Equation says….

Expected Return of Portfolio	=	Risk-free rate (think: treasury securities) + Some amount of market return depending on the portfolio's risk exposure + Some active management value added.

Hypothetical Example:
Capital Asset Pricing Model



CAPM Beta is the measure of systematic risk in a portfolio that is attributable to the general market. Beta measures how a portfolio fluctuates with respect to the market benchmark.
CAPM Alpha is the risk-adjusted (adjusted for market risk--beta) excess return with respect to the benchmark.

Costs

- When evaluating investment manager fees, it is important to focus on how much you pay for alpha.

Example:

3 Year Return of…		**Cost of….**	
Manager A	24.24%	Manager A	0.52%
Benchmark	21.77%	Benchmark (Index Fund)	0.08%
Excess Return	2.47%	Active Management (Mgr A - Index)	0.44%
CAPM Alpha	2.81%		

Excess Return to Active Management Fee Value	**5.61**
CAPM Alpha to Active Management Fee Value	**6.39**

Notes: Excess return may sometimes be used as a proxy for alpha from CAPM. A zero value means it is an index fund. The higher the number the better "value". A negative value means that you are paying for negative excess returns.