

SEPTEMBER 2009 QUARTERLY RESEARCH CONFERENCE CALL

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»» Why Even Look at Macroeconomics?

It's a Philosophical Issue on How Best to Add Value to a Portfolio

| Alpha | Asset Allocation |
|--|--|
| 5-10% of Returns | 90-95% of Returns |
| Non-Systematic (or Diversifiable Risk) | Systematic (or Non-Diversifiable Risk) |
| Not systematically rewarded | Systematically rewarded |
| <i>Random & Unpredictable</i> | <i>Predictable Over Time</i> |

Classical Consulting Mantra

90-95% of Time on Alpha
5-10% of Time on Asset Allocation



Our Approach

90-95% of Time on Asset Allocation
5-10% of Time on Alpha

Macroeconomic conditions are inextricably linked to the factors that drive asset class returns:

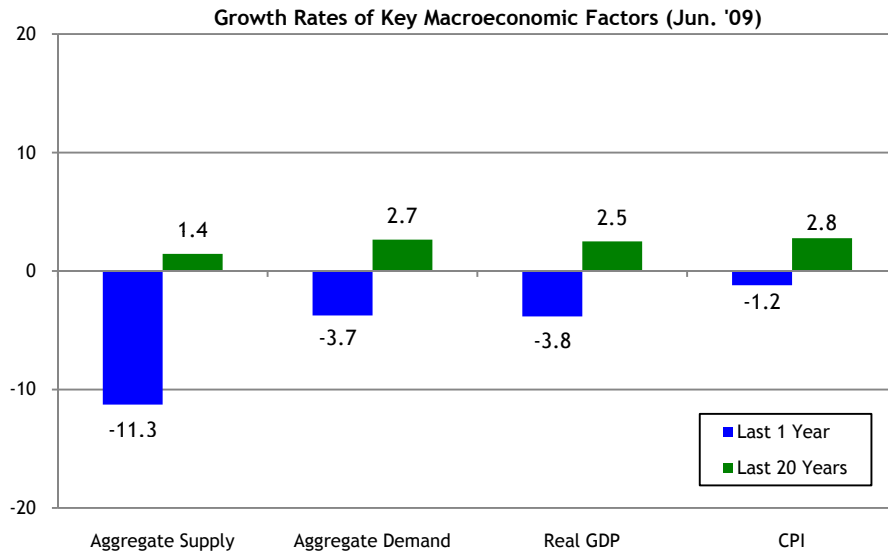
PE Ratios
EPS Growth Rates
Interest Rates
Credit Spreads
Inflation

Ignoring macroeconomics is akin to going through the asset allocation process with blinders on!

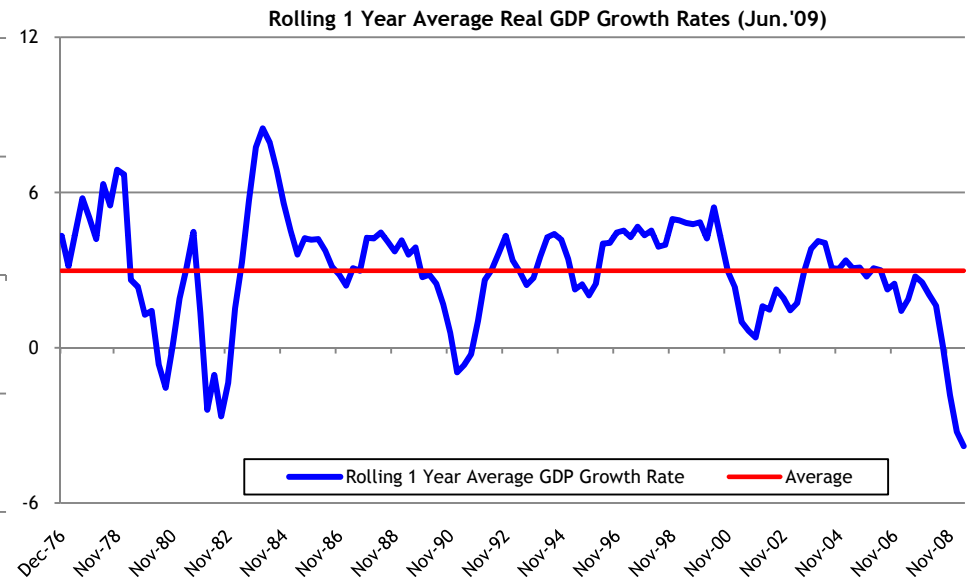
»» Brief Overview of Call

1. A Brief Snapshot of the Economy - A Recovery Forthcoming?
2. What is the Government Telling Us to Expect?
3. How are We Going to Get There?
4. What if Things Don't Go According to Plan?
5. What Could the Side Effects Be?
6. How Might GDP be Affected Going Forward?
7. What are the General Implications for Asset Allocation?

» Setting the Stage for an Economic Rebound (and inflation)

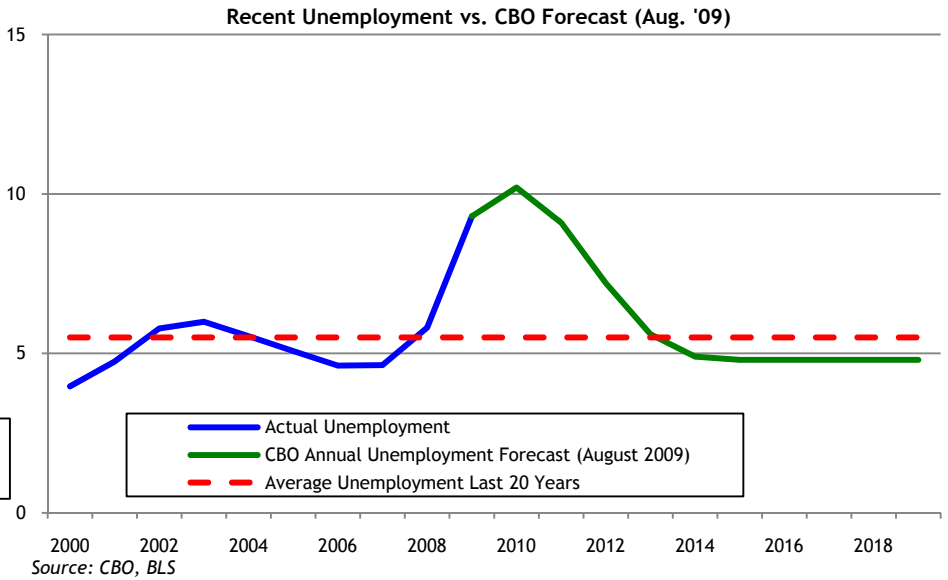
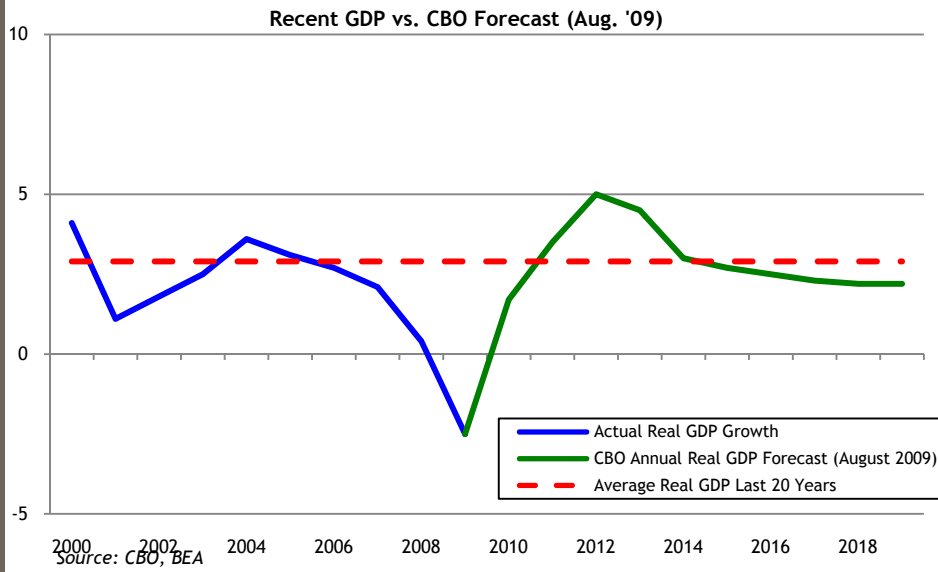


Source: Federal Reserve, BLS, BEA, Wurts & Associates



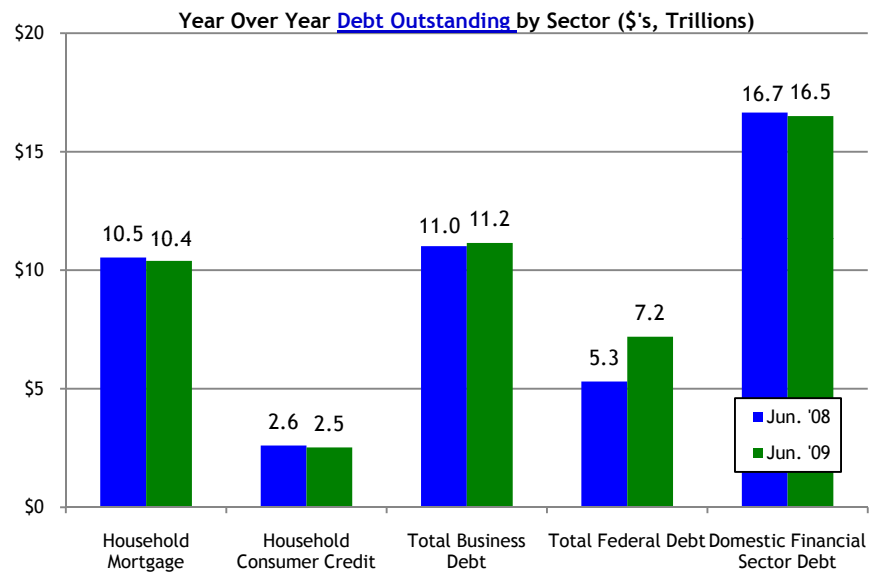
Source: BEA, Wurts & Associates

» What is the CBO Forecasting for Our Economy?

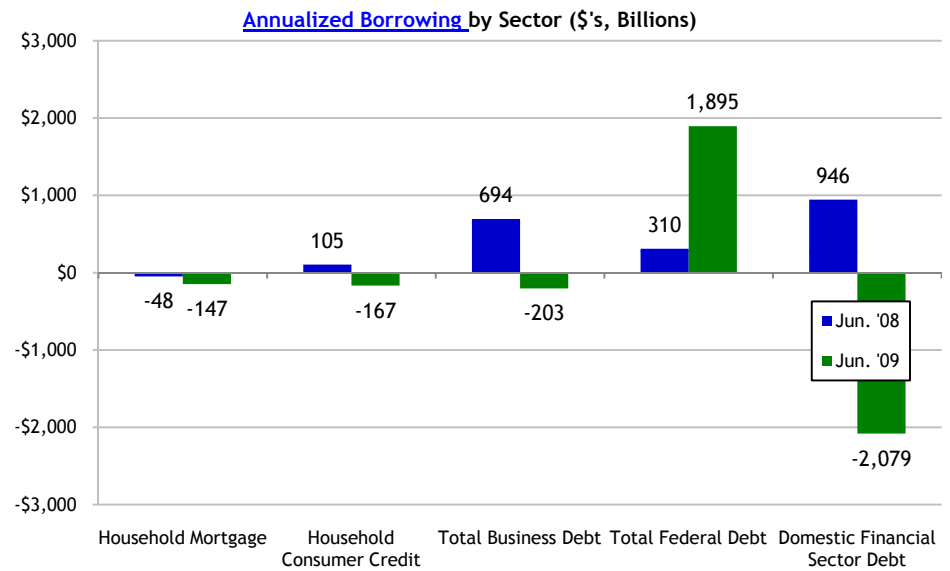


OK. How are we going to get there...and at what cost?

» The Government Continues to Supplant Lost Leverage

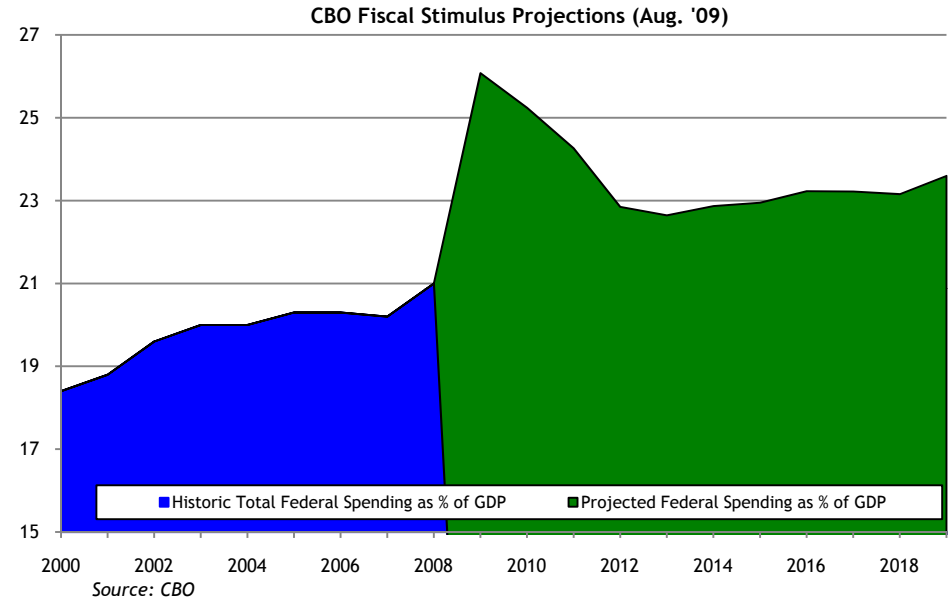
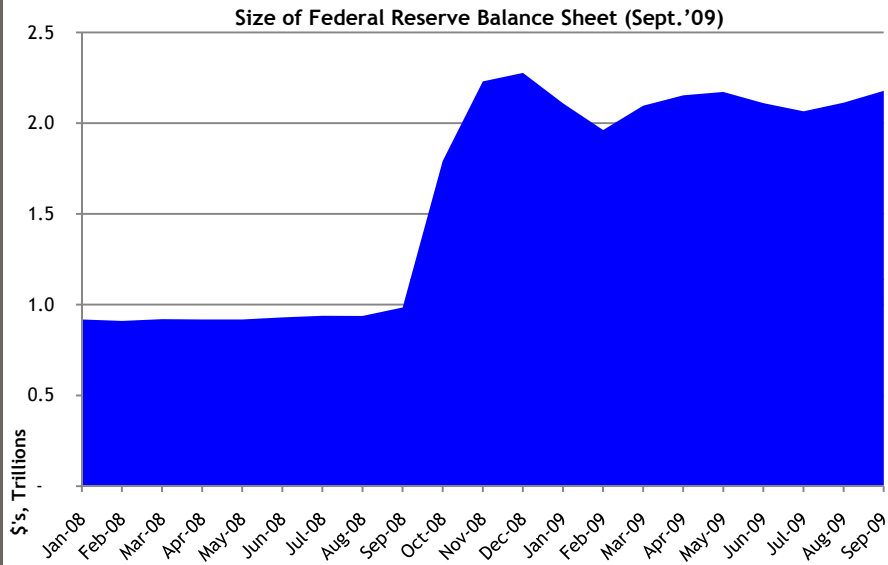


Source: Federal Reserve

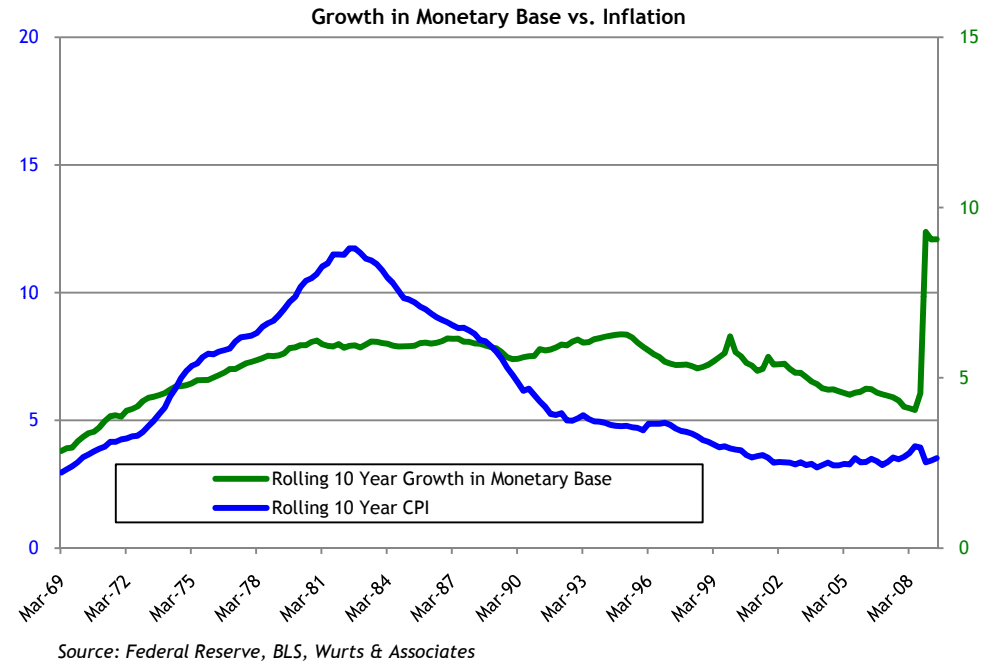
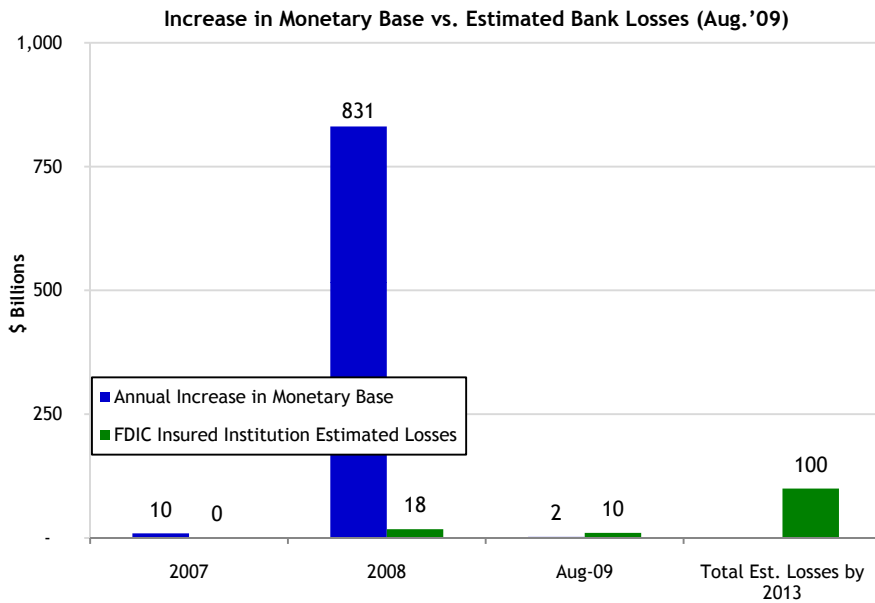


Source: Federal Reserve

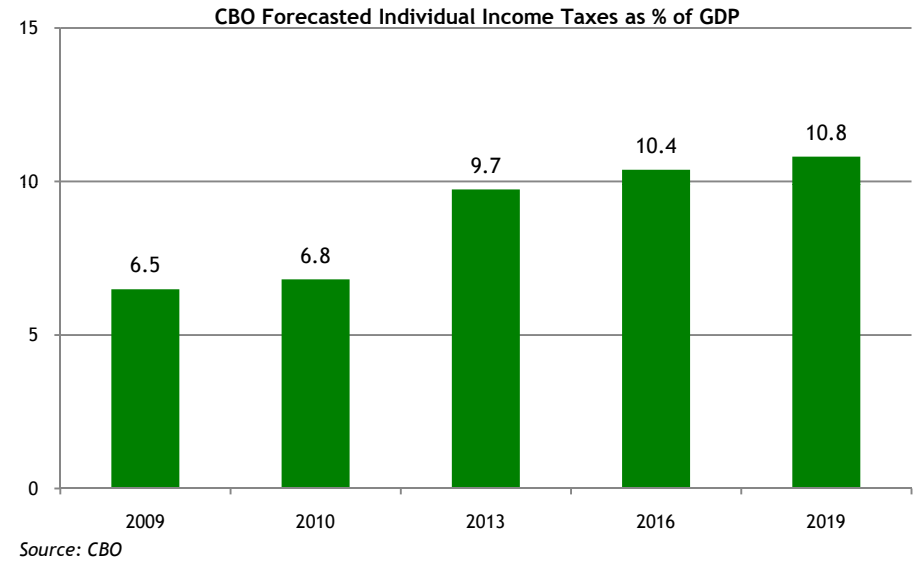
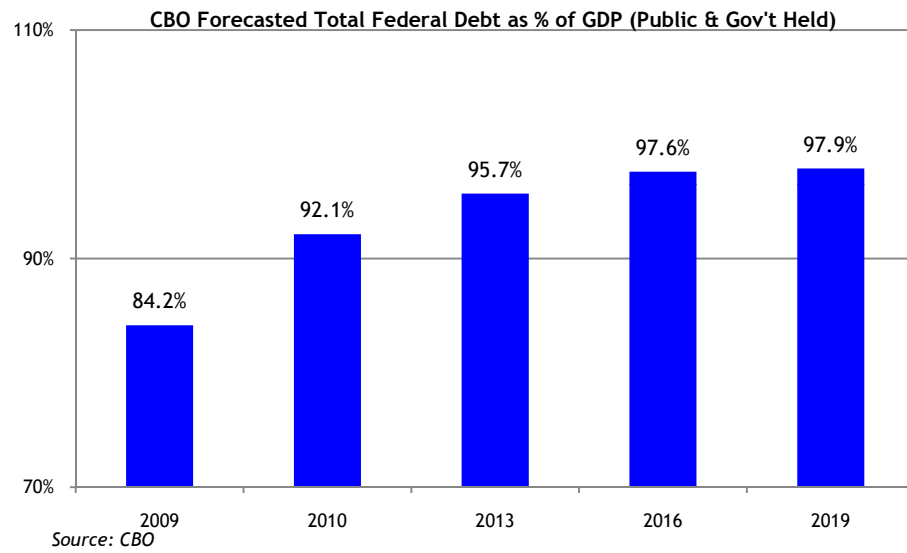
» The Amount of Government Stimulus is Just Staggering



» Growth in Money Supply is Doing More than Filling in Holes

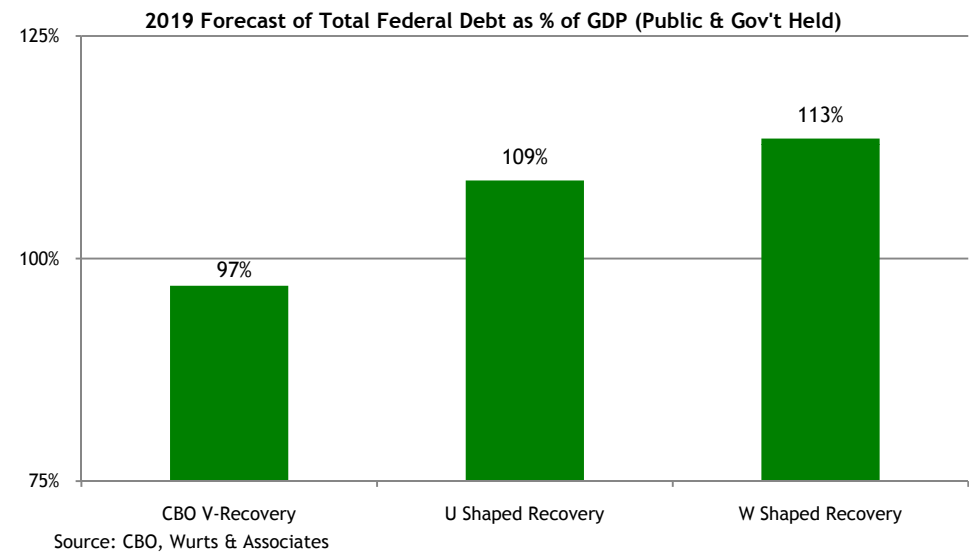
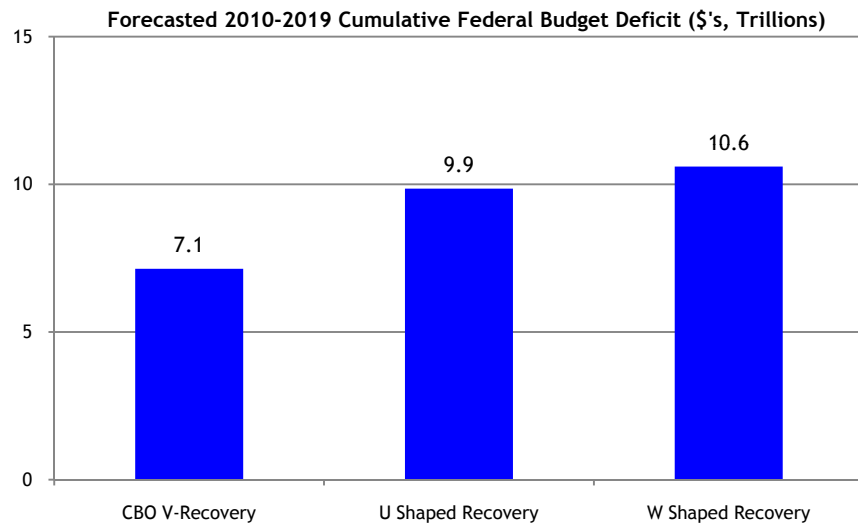


» The Side Effects Cannot Be Taken Lightly



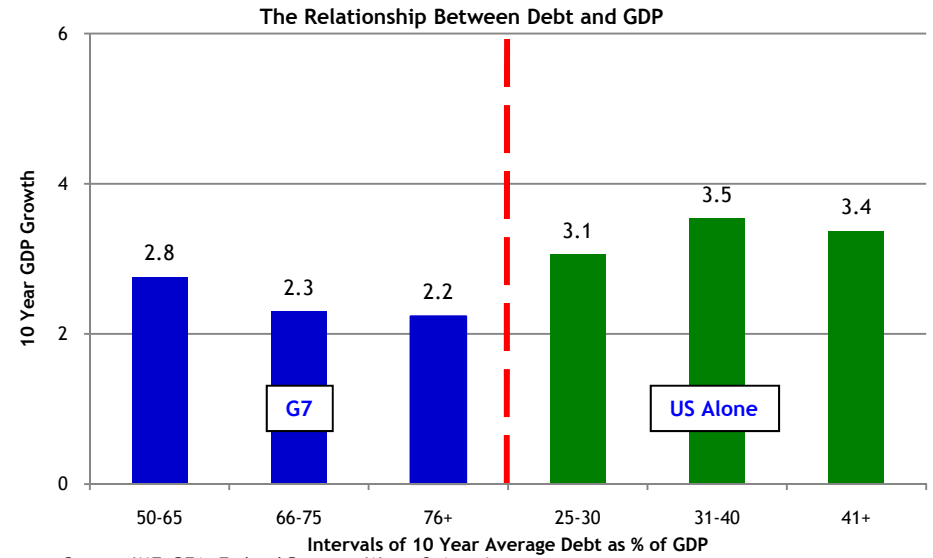
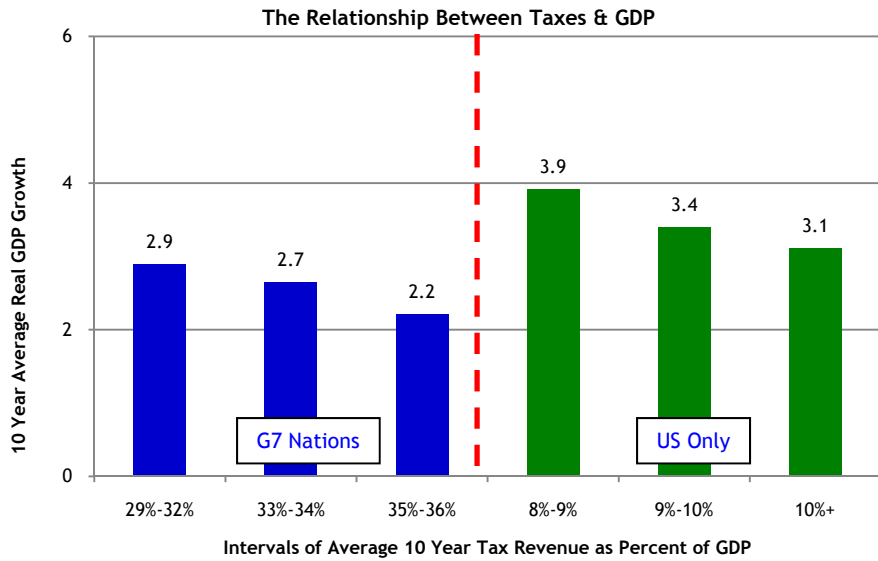
» What if Things Don't Go According to Plan?

| Avg. GDP Growth | |
|-----------------|------|
| V | 3.7% |
| U | 2.9% |
| W | 2.5% |

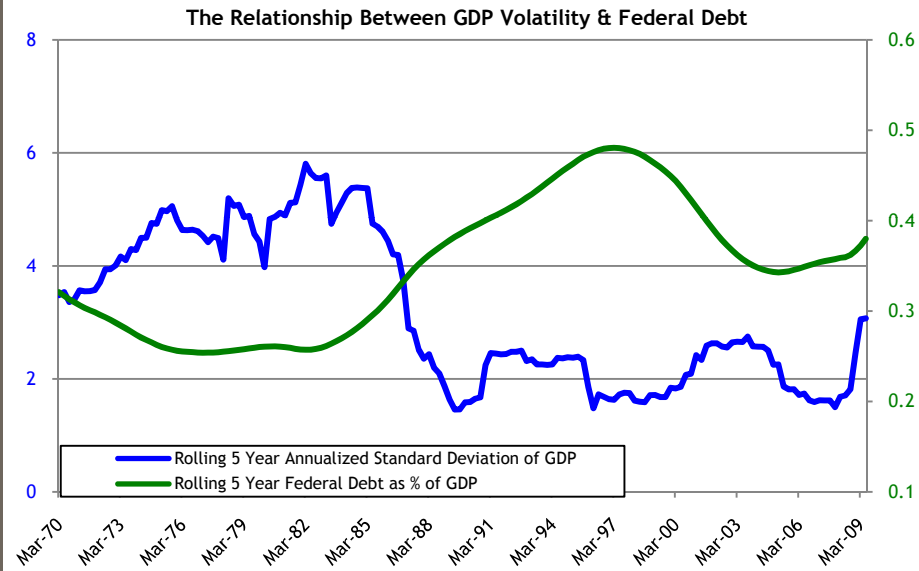


Well the societal balance sheet is worse off.

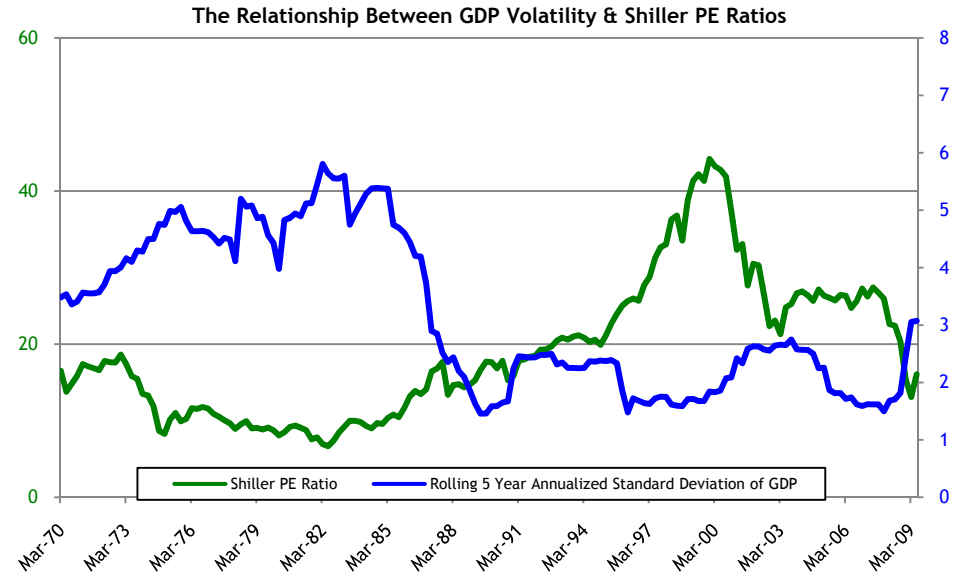
Let's Not Forget About How Debt and Taxes May Affect GDP



» On the Bright Side However...

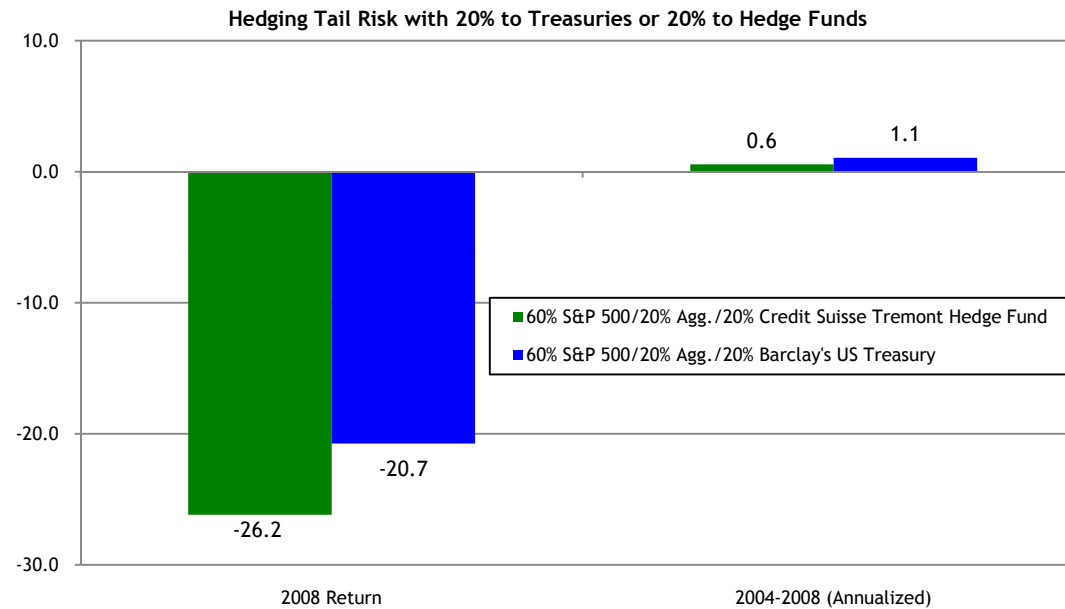


Source: BEA, Federal Reserve, Wurts & Associates



Source: BEA, Shiller Wurts & Associates

» The Best Protection Against Tail Events?

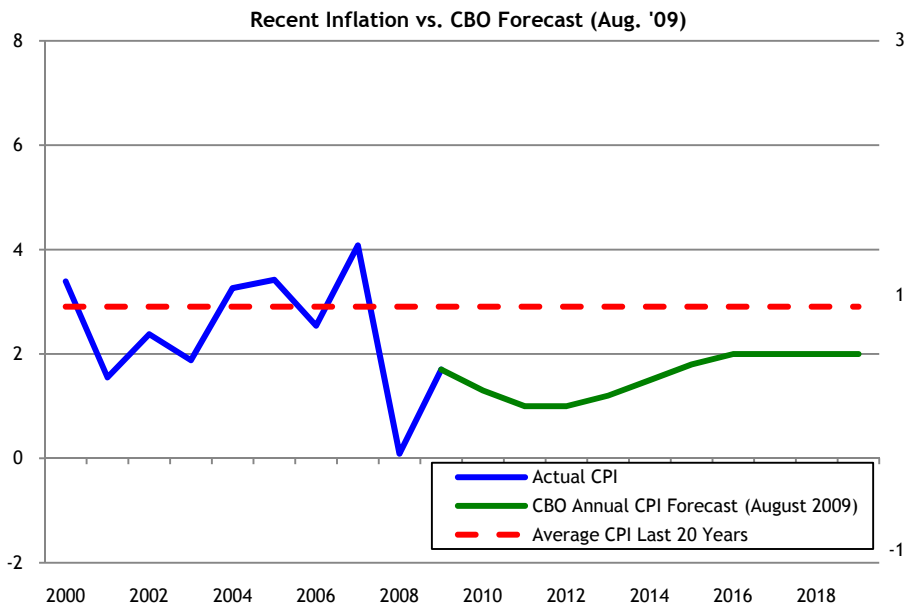


Source: Ibbotson

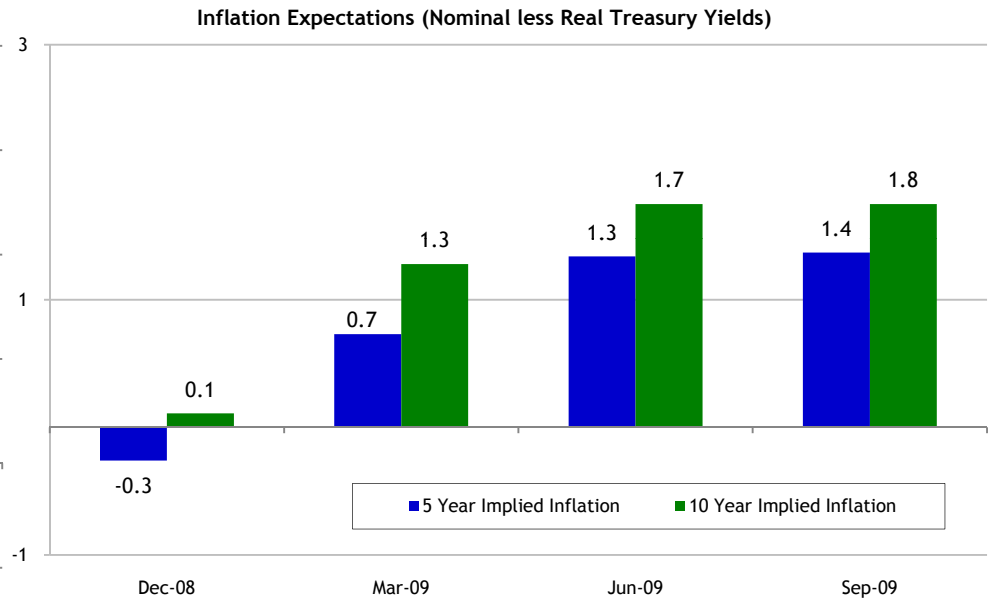
A hedge is something that goes up when everything else goes down

Not something that goes down less.

» Inflationary Expectations Seem Too Low

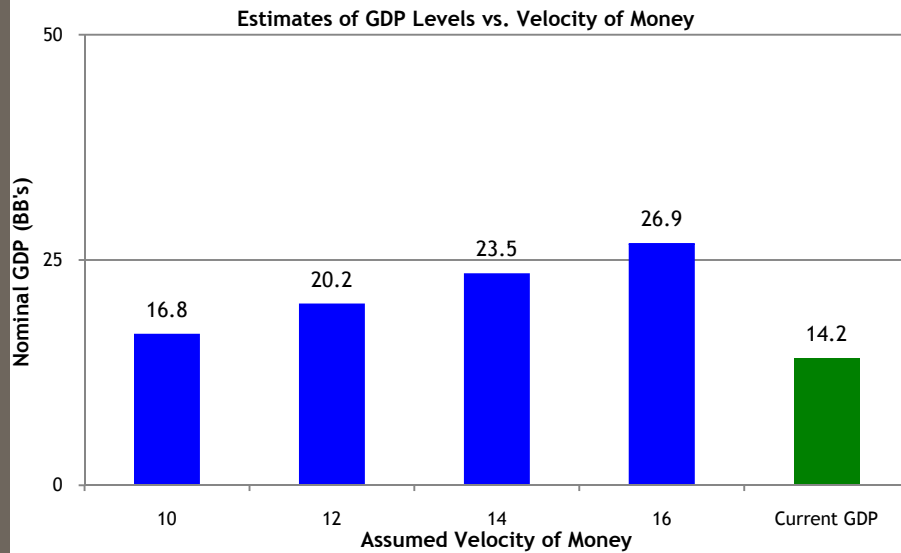


Source: CBO, BLS

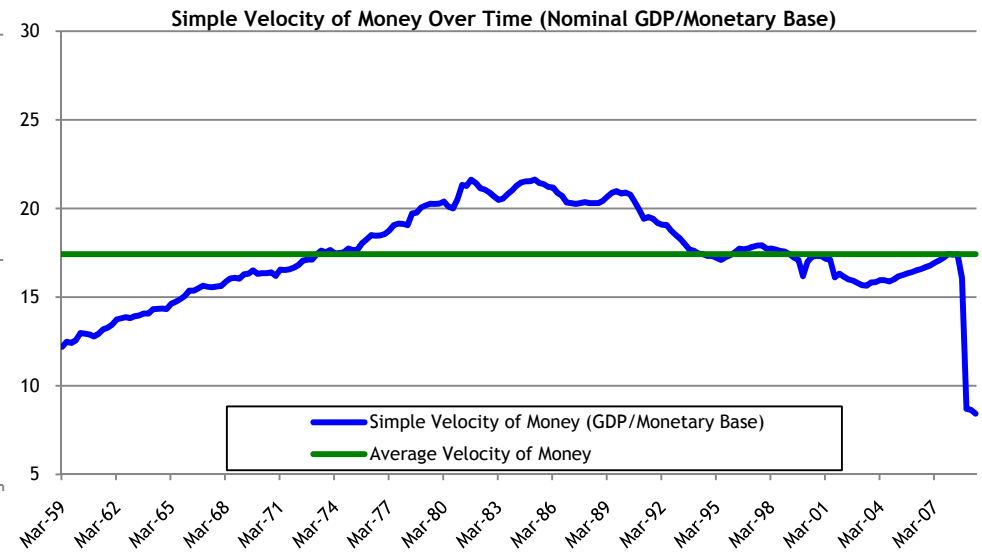


Source: Federal Reserve, Wurts & Associates

» Beyond Other Stimulus, Velocity of Money is a Concern

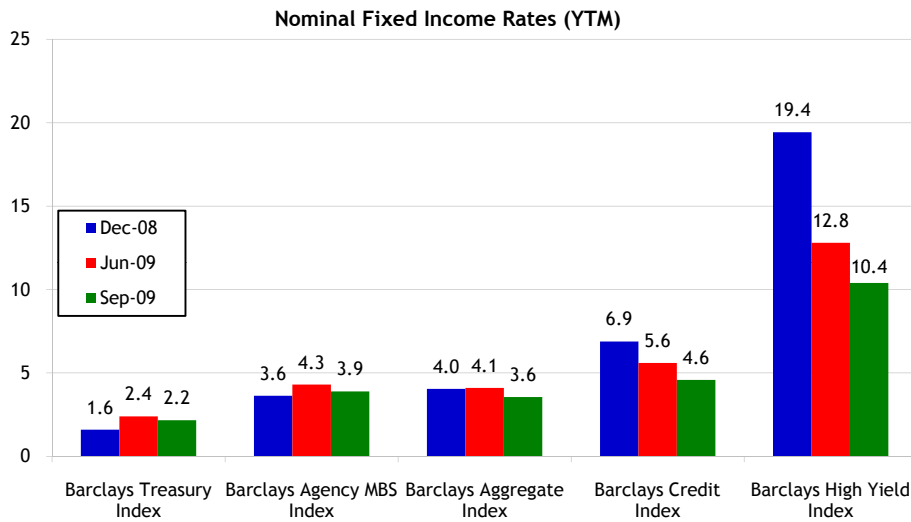


Source: Federal Reserve, BEA, Wurts & Associates

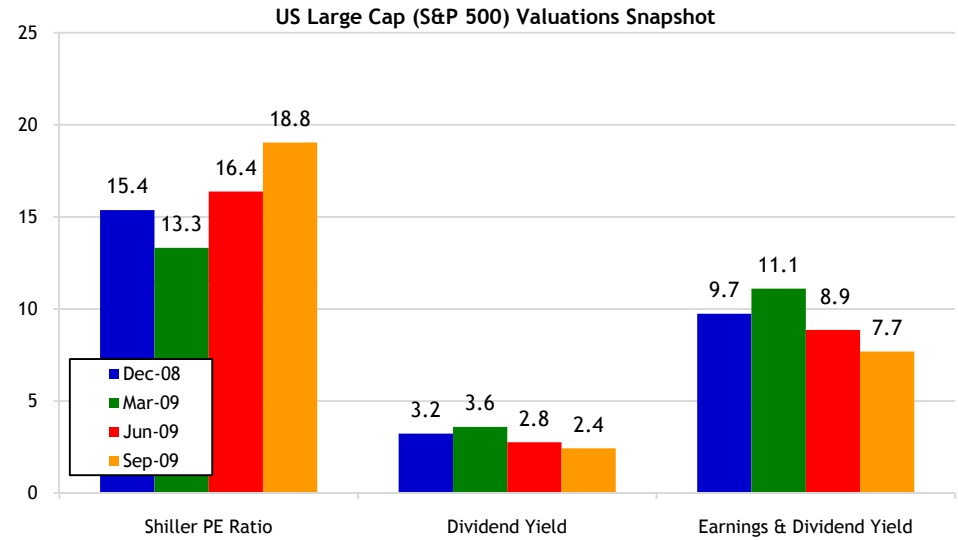


Source: Federal Reserve, BEA, Wurts & Associates

» A Quick Snapshot of Capital Markets Opportunities



Source: Barclays



Source: Yale/Shiller, Wurts & Associates

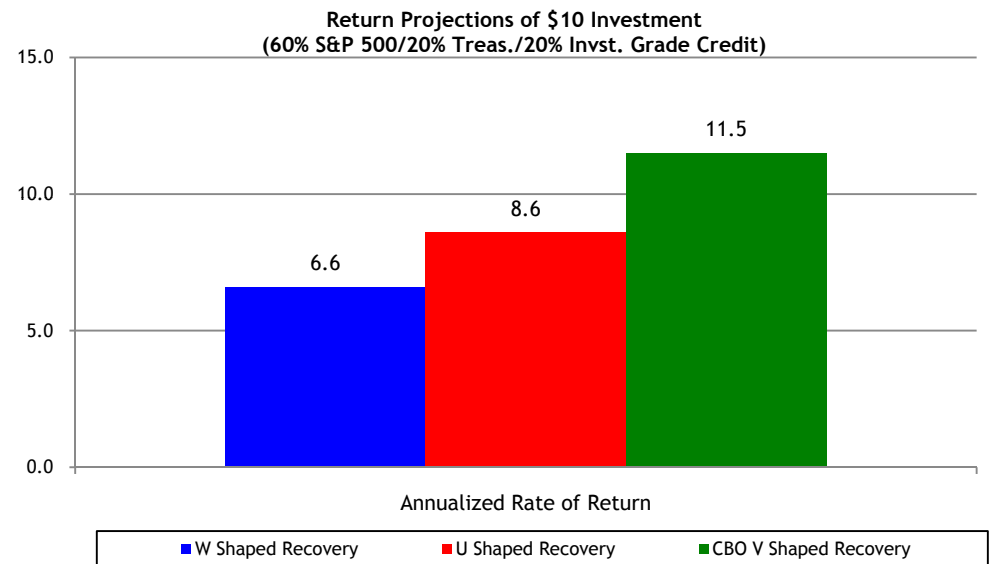
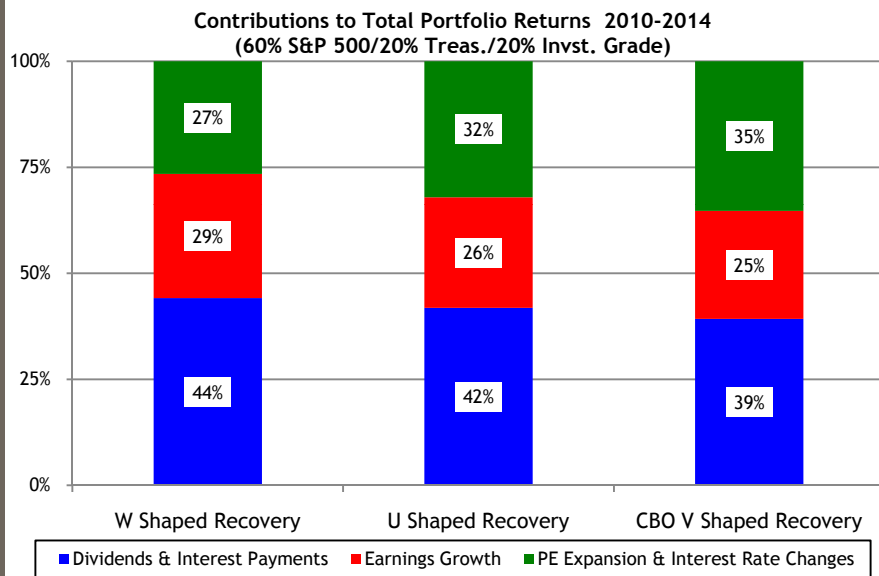
» Don't Forget GDP Growth Drives Key Risk Factors

Generalized Economic Scenario Assumptions (2010-14)

| | 3rd QTR Levels | CBO V Shaped Recovery | U Shaped Recovery | W Shaped Recovery |
|---|----------------|-----------------------|-------------------|-------------------|
| Shiller PE Ratio | 18 | 25 | 22 | 20 |
| 10 Year Treasury YTM | 3.25 | 5.5 | 4.5 | 4.0 |
| Barclay's Credit - Spread to Treasuries | 2.5 | 0.5 | 1.0 | 2.0 |
| Earnings Growth/Avg. GDP Forecast | - | 4.1% | 2.4% | 1.8% |

Note: Inflation assumed to be 2.5% for all scenarios; Wurts proprietary assumptions.

General Implications on Strategy Through Scenario Analysis



» Concluding Thoughts

- A strong v-shaped recovery just doesn't seem likely...but GDP will still grow
- However the cost of recovery will likely work against strong economic growth for some time
- Higher societal leverage may engender stability, but also the chances of “fat tails”
- The best defense against tail events is liquidity and being able to reallocate
- Equities and credit continue to offer fairly attractive rates of return
- However, a weaker economy means weaker capital market valuations
- So excessive risk taking is not likely to result in desired risk adjusted returns
- The optimal environment for levered alternative strategies is unlikely going forward
- A more normal appetite for risk is advised...defensive posturing seems unnecessary
- Use inflation to your advantage or protect against its arrival