outlook & strategy

june 2010

June was a volatile month for risk assets, and markets ended on a decisively downbeat note. The decline in global equities may reflect a growing belief that the world's economic rebound is slowing decisively. Immediate sources of concern include Chinese monetary tightening, a disappointing US jobs picture, stagnant eurozone retail sales and fears of eurozone banking weakness. Longer term worries are chiefly focused on the effects of fiscal contraction. Most G-20 countries plan to tighten fiscal policy next year. The UK is a poster child, with approximately 2% of GDP in deficit cuts planned.

We see the immediate slowdown in global growth as a result of a step-down in the pace of inventory accumulation. Anecdotal evidence indicates that many companies now see inventories and production in line with final demand, so output no longer needs to exceed final sales. This has shifted attention to the global consumer, who appears to remain cautious, except in China and Brazil. A key disappointment has been the US initial job claims data, which implied about 100,000 net new private jobs created per month. While this level does not indicate a recession, it also does not appear to be on pace to reduce the unemployment rate. We believe the US is seen as having another "jobless recovery."

With economic momentum downshifting, Treasurys rallied and equities sold off. Commodity currencies also weakened. A key risk for commodity currencies is likely to be the pace of Chinese construction in the wake of that government's spring credit tightening (M2 has slowed from 29% year-over-year to approximately 21%).

As deleveraging looks well-advanced, we believe indications of continued growth in the world economy could surprise the markets. So we remained buyers of peripheral currencies and spread products on weakness. These have tended to be small purchases as secondary bond market liquidity in names we favor has not been deep. Our duration strategy remained broadly neutral to the respective benchmarks.

In an exception to this view, we eliminated any exposure to the Indian rupee. Indian inflation figures could imply significant future interest rate hikes, and we see the Indian equity market as vulnerable.

China's decision to allow the renminbi to creep higher versus the US dollar is consistent with our non-Japan Asian currency overweightings. We do not expect the renminbi to strengthen dramatically and sold our non-deliverable forward foreign exchange contracts in that currency into the post-announcement euphoria. We maintained Korean, Indonesian and Malaysian positions since we believe Asian growth should be better relative to other countries.

government bond markets- developed countries

june 2010

UNITED STATES

The US bond markets were dominated by risk aversion in the second quarter as concerns about Greece's ability to finance its deficits blossomed into broader concerns about the euro and the strength of the European banking system. In addition, US economic data came in weaker than expected throughout May and June following strong gains in prior months. Notably, private nonfarm payroll growth slowed to 41,000 in May after adding an average of 200,000 new jobs per month in March and April. Retail sales followed a similar pattern, slowing sharply in May. Auto sales appeared more stable, with estimated growth of 4% in the second quarter. In a healthy sign, incomes continued to climb throughout the quarter due to a combination of elements including more hours worked, higher wages and job growth. Combined with the slower spending growth, the net result was a 4% saving rate, the highest since September 2009. Manufacturing and capital expenditures remained strong throughout the second quarter, while the housing market fell abruptly in response to the end of government stimulus from the new home buyer tax credit. Lastly, core inflation continued to slow during the second quarter. The Federal Open Market Committee commented on this development for the first time on June 23 noting that "underlying inflation has trended lower." During the second quarter the yield curve flattened by 48 basis points. The 2- to 10-year spread fell from 281 to 233 basis points. The entire yield curve fell, but more strongly on the long end. The 2-year yield fell 41 basis points (1.02% to 0.61%) while the 10-year yield fell 90 basis points (3.83% to 2.93%). Overall, the US government bond market rose 4.61% in the second quarter of 2010.

EUROPE

Euro area economic indicators continued to take a back seat to fiscal and political dynamics. Most indicators released in May suggested continued modest expansion in prior months, although the market priced in expectations for an extended period of weaker growth going forward. Banks facing heightened funding difficulties maintained tight credit conditions for consumers and corporations. After the joint European Union/International Monetary Fund aid package for Greece failed to reverse market sentiment regarding several euro area members, the EU created a €750 billion package that would be available to all members, not just Greece. After intensifying speculation that the European Central Bank (ECB) should undertake quantitative easing, the ECB instituted purchases of euro area government bonds, although they fully offset the liquidity impact. Intra-European Monetary Union government bond spreads remained volatile. Money markets also showed signs of strain. The ECB reinstated its dollar swap with the US Federal Reserve, and again began providing dollar liquidity for European banks. Banks put increasing amounts on deposit at the ECB rather than engage in interbank lending. Sovereign ratings remained under pressure and Moody's downgraded Portugal. German authorities banned naked short selling of key German equities, in an apparently unilateral decision that was met with mixed reaction from euro area partners. The Spanish government announced additional austerity measures, cutting public wages by 5%. The Italian government also introduced €24 billion in fresh austerity measures. Flight to quality flows continued to support German government bonds. The overall euro area government bond market returned +0.06% in the second quarter; Germany returned +4.1%, Greece -18.0%, and Spain -4.5%.

UNITED KINGDOM

Although data suggested moderate improvement in the UK economy, the outlook for recovery became less certain given the market's lowered global growth expectations. The *Purchasing Managers Index* reflected gradual economic expansion, and industrial and manufacturing production improved slowly. The consumer outlook remained difficult and confidence turned down in light of tight credit conditions and high unemployment. Housing sector data were mixed, although most showed slow growth in mortgage lending and single-digit annual house price appreciation. Despite excess capacity, inflation was above the Bank of England's 2% target and 3% limit. Although inflation appeared "sticky," the Bank of England (BoE) maintained its belief that inflation would fall back toward its target later in 2010. The BoE held rates unchanged at 0.5%, although one Monetary Policy Committee member dissented, preferring higher rates given the inflation readings. Fiscal policy was a key focus during the quarter. Markets priced the risk of policy inaction if the early

UNITED KINGDOM continued

May election failed to produce an outright winner (a "hung parliament"). While this was the outcome, several days of negotiations produced a Conservative-Liberal Democrat coalition government and an agreed set of policies. The new government introduced immediate modest fiscal tightening and published a fresh budget for 2010-2011 late in the quarter. The new budget included more aggressive spending cuts and revenue measures than the last government's plans, generally addressing rating agency concerns about fiscal profligacy and taking pressure off the UK's AAA credit rating. The risk premium in gilts declined and sterling appreciated. In the quarter, 2-year yields rallied 41 basis points and 10-year yields rallied 58 basis points to flatten the benchmark yield curve from 278 basis points to 261 basis points, however, it remained near record steep levels. The UK market returned +4.6%.

JAPAN

Japanese economic indicators were mixed in the second quarter as strong Asian demand continued to grease the wheels of recovery in Japan's export sector while the domestic economy began to show signs of stagnation as quarter end approached. Industrial production moderated throughout the quarter as China's efforts to cool its domestic economy might have filtered through to Japanese production. May industrial production rose 20.2% year-over-year decelerating from 31.8% year-over-year in March, while the April trade balance narrowed from 1 trillion to just over 850 billion yen. The jobless rate unexpectedly rose again in May from 5.1% to 5.2% and the job-to-applicant ratio deteriorated to 0.50 from 0.48. The second quarter also saw an intensification of deflationary conditions as May core *Consumer Price Index* (*CPI*) fell -1.6% year-over-year from -1.1% year-over-year in March. The Japanese consumer appeared to show signs of retrenchment anew in the second quarter as retail trade fell 2.0% month-over-month and household spending fell 0.7% year-over-year, both far worse than expected. Though the Japanese economy remained mired in uncertainty, as long as the Asian economic engine continues to power ahead, we believe Japan should do well as the caboose. Alas, there are signs that the locomotive may be showing signs of deceleration. The local government bond market returned 2.34% in the second quarter.

CANADA

Though the Canadian economy ran white-hot for most of the second quarter, signs emerged in late June of some moderation in the economic environment. Responding to the early second quarter strength, the Bank of Canada (BoC) hiked its overnight rate to 0.50% on June 1, becoming the first G7 nation to begin normalizing interest rates. The BoC's accompanying statement was cautious, saying "further moves would be weighed carefully" against growth in Canada and elsewhere. The bank's tone was in line with other global central banks that have begun to remove stimulus. Policymakers want to normalize rates without stoking currency appreciation and thus are incentivized to provide cautious outlooks for rate hikes going forward. The Canadian economy added 67,000 jobs in May, in line with expectations while the unemployment rate ticked up modestly to 8.1%. Retail sales, wholesale sales and April GDP came in on the low end of expectations but one month does not a trend make. Further evidence is needed to ascertain if we are in the midst of a moderation in Canadian activity. The core *CPI* remained contained in May, moderating to 1.8% year-over-year from 1.9% year-over-year in April. Though still below the BoC's 2% target, the bank will be closely monitoring this measure in the months to come. The Canadian bond market returned 3.75% in the second quarter.

NORWAY

The Norges bank (the central bank of Norway) hiked its overnight deposit rate to 2% in the second quarter. While the increase was largely expected by the market, we had expected the Norges to remain on hold given developments in Greece and recent strength in the Norwegian krone, particularly against the euro. The statement accompanying the decision communicated that "the global economy is rebounding" and "oil and other commodity prices have increased." Though policy makers considered leaving rates unchanged, it was concluded that Greece was unlikely to derail the European economy, at least in the near term. The Norges felt compelled to act largely due to continued house price

NORWAY continued

gains (house prices rose 3.4% in the first quarter and are above pre-crisis levels) though will likely take a cautious approach to further interest rate hikes given the prospect for further krone strength. Unemployment remained at a euro-wide best, moving to 2.7% in May from 3.0% in April while underlying *CPI* surprised modestly to the downside at 1.5% year-over- year. The Norwegian government bond market returned 2.61% in the second quarter.

AUSTRALIA

While still accelerating, the pace of economic growth in Australia appeared to be moderating. Economic data softened during the quarter and business and consumer sentiment appeared to be feeling the effects of the six rate hikes implemented during this cycle. During the second quarter, the Reserve Bank of Australia (RBA) raised rates 25 basis points in April and in May, before pausing in June and stating that "rates are appropriate for the near term." First quarter GDP rose 0.5% for the quarter and 2.9% year-over-year. The unemployment rate continued to improve, falling to 5.2% in May. Household lending rose 0.7% in May and business lending rose 0.4% for the month, an improvement from the large contraction seen for most of last year. Consumer lending fell 0.5% in May as the effects of the rate hikes filtered through. On the political front, Prime Minister Rudd resigned just prior to a vote of confidence in the Labor Party, making way for the party to elect Deputy Prime Minister Julia Gilliard as the new Prime Minister. So far, this leadership change has helped Labor in the polls. A general election must be held by April 2011 but is likely to occur before the end of 2010. The change in command puts into question the proposed Resource Super Profits Tax. A watering down of this proposal would hit government revenues since the budget released last month assumed the tax would be passed. The Australian government bond market returned 1.52% for the month of June and 4.26% for the second quarter.

NEW ZEALAND

The Reserve Bank of New Zealand (RBNZ) began a tightening cycle in June, raising the official cash rate by 25 basis points to 2.75%. The RBNZ made it clear that this was the first in an extended series of hikes to come and stated that "the further removal of stimulus will be reviewed in light of economic and financial market developments." Reported during the second quarter, first quarter GDP was 0.6% and 1.9% year-over-year. New Zealand's recovery remained export led, aided by strong global demand for the country's commodities. Key export industries during the quarter were mining, agriculture, forestry and metal products and machinery manufacturing. Fonterra, a New Zealand dairy co-operative, recently announced a near record payment to dairy farmers. New Zealand recorded a trade surplus in May of NZ$814 million due to strong export prices and weak consumer imports. The terms-of-trade index rose 5.9%, recording the largest quarterly increase since 1976. The labor market recorded significant progress as the unemployment rate fell from 7.1% at the end of the year to 6.0%. The government budget, released in May, delivered much of what the markets had expected on tax reform and should be fiscally neutral over the long term. The New Zealand government bond market returned 1.26% in June and 3.37% in the second quarter.

government bond markets-developed countries

june 2010

DEVELOPED MARKET GOVERNMENT BOND PERFORMANCE

LOCAL MARKET	ONE MONTH CHANGE	THREE MONTH CHANGE	SIX MONTH CHANGE	NINE MONTH CHANGE	ONE YEAR CHANGE
Denmark	0.61%	5.59%	9.10%	8.99%	11.85%
New Zealand	1.26%	3.37%	5.69%	6.39%	8.38%
Sweden	0.03%	3.36%	5.39%	6.83%	8.18%
United Kingdom	1.53%	4.63%	5.77%	3.60%	7.27%
Australian	1.52%	4.26%	4.92%	5.66%	7.10%
Switzerland	0.34%	2.40%	3.56%	4.72%	6.94%
United State	1.83%	4.61%	5.77%	4.41%	6.57%
Norway	-0.35%	2.61%	4.90%	6.32%	5.92%
Eurozone	-0.80%	0.06%	2.24%	2.29%	5.20%
Canada	1.25%	3.75%	4.65%	3.84%	4.78%
Singapore	1.62%	3.43%	3.38%	3.33%	4.15%
Japan	1.19%	2.34%	2.20%	2.70%	3.45%

Local returns; Citigroup

corporate bonds-investment grade credit (local currency)

june 2010

UNITED STATES

The second quarter of the year proved to be very difficult for US investment grade credit. The positive momentum that began in March and continued through April ended abruptly in May, which led to corporates strongly underperforming governments. Investment grade credit outpaced governments during June on a total return basis, albeit only slightly. Continued sovereign concerns in Europe, uncertainty regarding financial sector regulation, concerns about China's tightening and economic slowdown, the BP oil spill and tensions in Korea, among other concerns, led to significantly elevated investor risk aversion during the quarter. Spreads widened by 48 basis points, and ended June 19 basis points wider year-to-date. Interestingly, the spread widening was primarily due to the significant rally in Treasury yields, as investment grade corporate bond prices actually rose from tight spreads in mid-April. Going forward, a gradually improving economic picture and signs of stabilization in the fiscal position of European sovereigns would likely be needed before the outlook for investment grade corporate spreads can improve. During the second quarter, defensive sectors such as aerospace/defense, diversified manufacturing, and consumer products performed the best, as the risk trade came off hurriedly during May. Underperforming sectors included energy, homebuilders and telecommunication. Energy names underperformed dramatically over the period on the continuously negative news related to the Gulf oil spill, while many telecommunication names suffered as a result of the European sovereign crisis. As one would expect given the heightened level of risk aversion, lower quality credit fared the worst during the quarter. Despite this weak performance, we continued to have a favorable view of spread product, as investor interest in the asset class remained a positive technical, spreads were more attractive, and our base case expectation was for the global economy to gradually improve. That being said, we are closely monitoring European sovereign issues and related contagion effects to the broader market. We are continuing to search for opportunities that we believe can offer solid long-term value.

EUROPE

In euroland, a similar story developed during the quarter in investment grade. Corporates underperformed governments by a wide margin during the period as investors shunned risk on the aforementioned concerns. Corporate spreads widened by 58 bps versus German bunds from April to June, as investors withdrew from risk assets and bund rates rallied. German, French, and Dutch government bonds performed very well during the quarter due to their perceived safe haven status, while the government bonds of Greece, Portugal, Spain and Italy posted weak performance. Stabilization of the fiscal positions in the 'Club Med' countries, further clarity on European banking exposures, and properly functioning interbank lending markets will likely be necessary before the bid returns to these markets. On a sector basis, the best performers during the quarter were media non-cable, pharmaceuticals and tobacco, while lower tier insurers and banks, as well as metals & mining companies underperformed. Concerns regarding the exposure of banks and insurance companies to troubled European countries sparked a selloff across financial paper, especially lower-quality issues. Looking ahead, we will continue to closely monitor the delicate sovereign situations in Greece and Spain, among others, and the potential contagion effect on corporates.

UNITED KINGDOM

The UK investment grade market performed in-line with other major corporate markets during the quarter, underperforming gilts significantly. Spreads widened by 54 bps during the period and ended June slightly wider than they were at the beginning of 2010. Similar to the euro market, insurance, banks and metals & mining were the worst performing industries, while more defensive areas in general were the outperformers. The "risk trade" was off across markets during the month of June and the UK market was no exception. We continued to selectively add to our corporate exposure buying companies that we deemed offered relative value.

corporate bonds-investment grade credit (local currency)

june 2010

	ONE MONTH CHANGE	THREE MONTH CHANGE	SIX MONTH CHANGE	NINE MONTH CHANGE	ONE YEAR CHANGE
US Investment Grade Corporate	2.13%	3.42%	5.79%	7.22%	**15.92%**
Aaa	2.58%	6.27%	8.18%	6.77%	**12.12%**
Aa	1.91%	3.09%	4.92%	5.48%	**11.82%**
A	2.40%	3.78%	5.88%	6.85%	**15.22%**
Baa	1.91%	3.10%	6.05%	8.47%	**18.67%**
US Governments	1.83%	4.61%	5.77%	4.41%	**6.57%**
	ONE MONTH CHANGE	THREE MONTH CHANGE	SIX MONTH CHANGE	NINE MONTH CHANGE	ONE YEAR CHANGE
European Investment Grade Corporate	0.23%	0.26%	3.54%	5.31%	**11.88%**
Aaa	0.24%	1.83%	4.62%	5.43%	**9.72%**
Aa	0.27%	1.06%	3.61%	4.85%	**9.22%**
A	0.30%	0.25%	3.56%	5.32%	**12.17%**
Baa	0.08%	-0.59%	3.40%	5.88%	**14.87%**
Euro Governments	-0.80%	0.06%	2.24%	2.29%	**5.20%**
	ONE MONTH CHANGE	THREE MONTH CHANGE	SIX MONTH CHANGE	NINE MONTH CHANGE	ONE YEAR CHANGE
Sterling Investment Grade Corporate	0.86%	0.90%	5.71%	6.54%	**18.77%**
Aaa	0.88%	2.86%	5.46%	4.63%	**10.04%**
Aa	1.09%	2.02%	5.52%	5.74%	**14.96%**
A	0.94%	0.63%	5.45%	6.12%	**18.41%**
Baa	0.54%	0.48%	6.49%	8.30%	**23.98%**
UK Governments	1.53%	4.63%	5.77%	3.60%	**7.27%**

Source: Barclays Capital

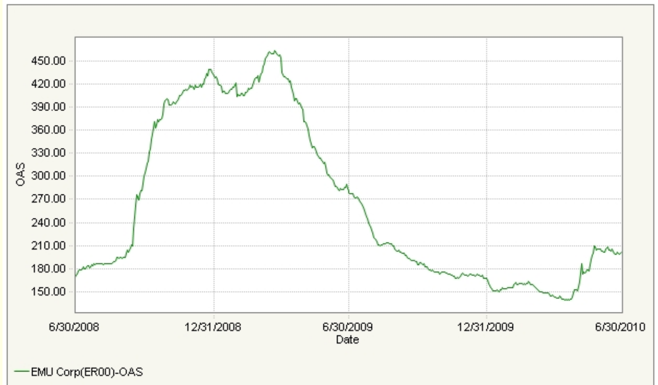
corporate bonds-investment grade credit (local currency)

june 2010

US INVESTMENT GRADE CORPORATE OPTION-ADJUSTED SPREAD

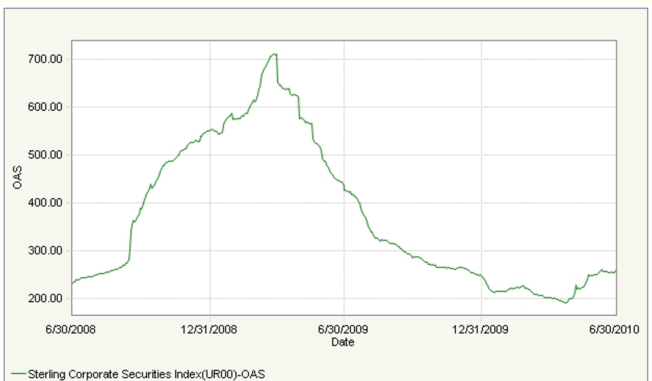
	High	Low	Begin Pt.	End Pt.	Avg	Std. Dev.
US Corp Master(C0A0)-OAS	656	151	274	209	348	163.12
	12/5/2008	4/21/2010	6/30/2008	6/30/2010	-	-

EMU INVESTMENT GRADE NON-FINANCIAL CORPORATE OPTION-ADJUSTED SPREAD



	High	Low	Begin Pt.	End Pt.	Avg	Std. Dev.
EMU Corp(ER00)-OAS	463	139	169	201	262	106.21
	3/20/2009	4/15/2010	6/30/2008	6/30/2010	-	-

UK INVESTMENT GRADE CORPORATE OPTION-ADJUSTED SPREAD



	High	Low	Begin Pt.	End Pt.	Avg	Std. Dev.
Sterling Corporate Securities Index(UR00)-OAS	712	192	232	260	372	150.51
	3/30/2009	4/23/2010	6/30/2008	6/30/2010	-	-

Source: Merrill Lynch; Spread measured in basis points.

high yield

june 2010

The US high yield market had a very difficult second quarter as risk assets sold off on a plethora of concerns, chiefly the sovereign issues plaguing Europe, a tightening of Chinese bank lending, the Gulf oil spill and tensions in Korea. The US high yield market posted a total return of -0.11% and an excess returns versus governments of -3.86%. High yield bond spreads widened by 129 basis points during the period and prices dropped by approximately 2.5 points on average. The asset class experienced fund outflows throughout May and the first half of June, but more recently flows have turned positive.

Looking ahead, we would expect volatility to continue as the sovereign situations across Europe continue to unfold and the outlook for global growth remains clouded. Notable outperformers during the second quarter included airlines and pharmaceuticals, while insurance, banking, and technology underperformed. Unsurprisingly, lower quality credits fared the worst during the selloff. With the backup in spreads during the quarter, the high yield sector appears to offer more value, but issue selection remains critical. That said, the market continues to face a number of challenges (economic uncertainty, sovereign contagion), leading us to tread cautiously in the space while looking for companies that we believe can offer compelling relative value.

	ONE MONTH CHANGE	THREE MONTH CHANGE	SIX MONTH CHANGE	NINE MONTH CHANGE	ONE YEAR CHANGE
US Corp High Yield	1.24%	-0.11%	4.51%	10.99%	26.77%
Ba	1.52%	0.44%	4.96%	9.96%	22.15%
B	1.19%	0.02%	3.56%	8.49%	19.67%
Caa	0.85%	-1.36%	3.83%	12.87%	36.09%
Ca-D	1.08%	-1.41%	10.97%	27.45%	71.77%
NR	-0.24%	-4.35%	1.40%	8.16%	21.19%

Source: Barclays Capital Markets.

US HIGH YIELD CORPORATE OPTION-ADJUSTED SPREAD

	High	Low	Begin Pt.	End Pt.	Avg	Std. Dev.
US High Yield Master II (H0A0)-OAS	2182	542	735	713	1068	452.15
	12/15/2008	4/26/2010	6/30/2008	6/30/2010	-	-

Source: Merrill Lynch; Spread measured in basis points.

LOOMIS | SAYLES

currency

june 2010

The **US dollar** strengthened more than 6% in the second quarter continuing its meaningful first quarter gains as doubts about the global economy spurred risk liquidation and therefore US dollar buying. The European debt crisis was the main catalyst for risk aversion although other risk negative events occurred during the month (China tightening, Australian mining tax, German ban on short selling, Korean tensions, Middle East tensions, US regulatory reform, the BP oil spill, etc.). Equities also sold off during the period as investors pulled back amid concerns about harsh European austerity measures leading to slower global growth. Though consensus expectations for mild positive global and US growth remained, concerns about a possible double dip recession in Europe and the US gained traction.

The commodity currencies were negatively impacted during the quarter on fears that global growth and thus commodity demand could be slowing. In addition to China's announced measures to reign in credit growth and speculation, fears about 1930s-style tax hikes and spending cuts throughout the developed world led to fears about dramatically slower economic activity and thus commodity demand in the second half of 2010. The *CRB Commodity Index* fell nearly 5.5% in the second quarter as Australia's announced mining tax in May appears to have exacerbated already fragile market sentiment. Investor skittishness saw the **Australian, Canadian and New Zealand dollars** fall 8.3%, 4.6% and 3.6% respectively.

The **Japanese yen** strengthened nearly 6% during the quarter as the flight from equities into bonds collapsed the US-Japan 10-year bond yield differential and caused the unwind of carry trades. The second quarter saw beleaguered Prime Minister Hatoyama resign amidst dismal approval ratings. His successor, finance minister Naoto Kan, favors a weaker yen, but is not expected to encourage the Bank of Japan to reemploy quantitative easing unless the yen were to strengthen markedly. Japanese economic conditions have improved, though the country's growth remains inexorably tethered to its export sector.

Asian currencies were mixed in the second quarter amid offsetting forces. An announcement by the government that it was prepared to resume its measured strengthening of the **Chinese renminbi** initially buoyed Asian currencies, but doubts about the immediateness of the impact saw exuberance wane. Concerns about global growth also weighed on the Asian currency complex as those currencies are often seen as growth proxies. The **South Korean won** was a laggard amidst tension with its northern neighbor, falling 8%.

The **euro** continued to decline, falling 9.4% as sovereign concerns persisted. Despite the European Union's one trillion US dollar aid package for Greece and other European states, the market perceived the action as coming too late and without enough details. Pan European austerity plans are being announced, although specifics remain fleeting.

The **UK pound sterling** rose smartly following the country's election. The conservatives emerged as the winners and pledged to take measures to reduce the UK's runaway budget. The pound rose 2.8% in June though was down 1.6% for the quarter.

currency

june 2010

CURRENCY	ONE MONTH CHANGE	THREE MONTH CHANGE	SIX MONTH CHANGE	NINE MONTH CHANGE	ONE YEAR CHANGE
USD Index	**-0.66%**	**6.10%**	**10.48%**	**12.22%**	**7.35%**
Canadian Dollar	-1.82%	-4.57%	-1.01%	0.53%	9.25%
Japanese Yen	3.20%	5.70%	5.20%	1.45%	8.97%
New Zealand Dollar	0.62%	-3.64%	-5.27%	-5.32%	6.04%
Thai Baht	0.34%	-0.22%	2.96%	3.18%	5.08%
Australian Dollar	-0.60%	-8.33%	-6.34%	-4.76%	4.27%
Singapore Dollar	0.02%	-0.03%	-0.13%	0.74%	3.43%
Norwegian Krone	-0.60%	-8.57%	-10.86%	-11.18%	-1.05%
Swedish Krona	0.21%	-7.38%	-8.13%	-10.69%	-1.18%
UK Pound	2.80%	-1.57%	-7.58%	-6.49%	-9.19%
Euro	-0.55%	-9.42%	-14.55%	-16.41%	-12.79%
Danish Krone	-0.69%	-9.47%	-14.62%	-16.46%	-12.82%

Source: Bloomberg

emerging markets

june 2010

After a constructive first quarter, the second quarter was volatile — up in April, down in May and back up again in June. As a result, emerging markets debt ended June only slightly above March levels. News from the European Union, Greece, Spain and China contributed to the volatility. When there is no clear trend, the market can interpret data as positively or negatively. However, market indecisiveness notwithstanding, we remained constructive on the emerging market sector. As long as the economies of developed countries are at a relative standstill, interest rates will likely be low. This environment should create a natural demand for emerging market assets. Since September 2009, there have been only two weeks of outflows from emerging market mutual funds according to AMG Data Services. Therefore, we think the sector's technicals and the fundamentals are favorable.

EXTERNAL MARKETS

The *JP Morgan EMBI Global Index* was up 2.01% in June and 1.16% in the second quarter. For the first half of 2010, the return was 5.37%. The best performing countries during the quarter were in Latin America: Belize (9.32%), Panama (4.68%), Peru (4.27%) and Mexico (4.03%). The European countries were the weakest geographic region with Hungary (-5.74%) and Bulgaria (-2.87%) in the negative column. Venezuelan bonds were the worst performers by far this quarter (-11.61%) as investors reacted to increasingly desperate moves by the Chavez government.

	ONE MONTH	THREE MONTHS	SIX MONTHS	NINE MONTHS	ONE YEAR	YEAR-TO-DATE
JPM EMBI Global	**2.01%**	**1.16%**	**5.37%**	**6.98%**	**17.90%**	**5.37%**
JPM EMBIG Spread Change	**16**	**97**	**64**	**21**	**(75)**	**(366)**
Argentina	2.49%	-5.50%	-1.79%	8.26%	44.56%	-1.79%
Belize	3.46%	9.32%	39.58%	42.29%	62.06%	39.58%
Brazil	2.15%	3.16%	5.50%	5.75%	13.71%	5.50%
Bulgaria	0.87%	-2.87%	0.31%	2.73%	15.57%	0.31%
Chile	3.05%	3.90%	4.24%	5.29%	9.91%	4.24%
China	0.56%	3.11%	5.08%	5.72%	9.62%	5.08%
Colombia	3.50%	3.37%	7.22%	6.52%	15.84%	7.22%
Dom Rep	4.51%	3.98%	7.55%	12.32%	36.72%	7.55%
Ecuador	-0.18%	-2.79%	-0.36%	8.71%	35.03%	-0.36%
Egypt	0.27%	0.14%	0.32%	1.84%	5.00%	0.32%
El Salvador	2.48%	1.46%	8.49%	9.13%	24.65%	8.49%
Gabon	1.22%	-0.89%	5.03%	9.00%	31.44%	5.03%

emerging markets

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	ONE MONTH	THREE MONTHS	SIX MONTHS	NINE MONTHS	ONE YEAR	YEAR-TO-DATE
JPM EMBI Global	**2.01%**	**1.16%**	**5.37%**	**6.98%**	**17.90%**	**5.37%**
JPM EMBIG Spread Change	**16**	**97**	**64**	**21**	**(75)**	**(366)**
Georgia	1.64%	1.33%	5.64%	13.28%	34.74%	5.64%
Ghana	1.93%	-2.17%	6.38%	11.33%	39.24%	6.38%
Hungary	-2.62%	-5.74%	-1.75%	-0.04%	12.65%	-1.75%
Indonesia	2.41%	2.74%	6.46%	9.83%	26.61%	6.46%
Iraq	1.53%	3.91%	9.95%	14.74%	38.26%	9.95%
Jamaica	1.95%	0.00%	36.22%	27.11%	29.34%	36.22%
Kazakhstan	3.76%	-2.88%	6.15%	10.65%	33.27%	6.15%
Lebanon	0.73%	1.62%	5.76%	11.07%	17.58%	5.76%
Malaysia	1.64%	3.15%	5.13%	5.89%	9.17%	5.13%
Mexico	3.56%	4.03%	8.40%	9.14%	16.64%	8.40%
Pakistan	1.47%	-0.24%	15.29%	11.24%	46.64%	15.29%
Panama	1.37%	4.68%	6.69%	6.32%	17.12%	6.69%
Peru	2.91%	4.27%	7.50%	7.26%	18.29%	7.50%
Philippines	0.91%	3.22%	5.65%	8.15%	16.50%	5.65%
Poland	0.47%	0.29%	2.75%	2.47%	9.59%	2.75%
Russia	1.40%	-1.34%	2.63%	7.16%	19.13%	2.63%
Serbia	1.42%	-1.79%	1.11%	2.63%	18.53%	1.11%
South Africa	2.83%	3.47%	4.78%	6.56%	15.48%	4.78%
Sri Lanka	1.56%	0.75%	3.43%	10.43%	23.02%	3.43%
Tunisia	0.16%	0.64%	4.06%	4.14%	8.77%	4.06%
Turkey	0.86%	2.16%	3.47%	7.96%	16.14%	3.47%
Ukraine	1.62%	0.98%	23.54%	22.17%	41.96%	23.54%
Uruguay	3.77%	3.53%	9.87%	13.71%	25.44%	9.87%
Venezuela	3.14%	-11.61%	-0.05%	-7.22%	15.67%	-0.05%
Vietnam	1.12%	2.71%	7.97%	6.96%	17.52%	7.97%
EMBI Spread	358					294*

**Spread as of 06/30/10; Source: JP Morgan Chase; Bloomberg*

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LOCAL MARKETS

The local currency emerging markets reflected increasing investor concerns about Europe and the appreciation story of the Chinese renminbi. While performance for this sector was still positive year-to-date at 3.36%, second quarter performance was negative for the local currency index (-1.98%). However, there was a wide dispersion in returns by geographic region in the quarter. Asia gained 3.91% helped by Indonesia's 5.44% return, while the European region lost 10.06% hurt by Poland's -15.54% return.

EM LOCAL (IN USD)	ONE MONTH	THREE MONTHS	SIX MONTHS	NINE MONTHS	ONE YEAR	YEAR-TO-DATE
GBI-EM	0.99%	-1.98%	3.36%	6.29%	15.48%	3.36%
GBI-EM Asia	3.22%	3.91%	12.07%	14.99%	22.45%	12.07%
GBI-EM Europe	-2.04%	-10.06%	-6.85%	-5.37%	7.22%	-6.85%
GBI-EM Latin America	2.80%	2.01%	7.55%	11.84%	20.01%	7.55%
GBI-EM Middle East/Africa	-0.97%	-3.21%	1.19%	5.23%	10.38%	1.19%
GBI-EM Argentina	5.96%	1.73%	0.38%	20.27%	85.76%	0.38%
GBI-EM Brazil	2.57%	1.50%	2.99%	7.54%	21.12%	54.68%
GBI-EM Chile	-2.22%	-1.73%	-2.40%	5.01%	3.57%	-2.40%
GBI-EM Colombia	5.78%	8.27%	18.85%	21.98%	43.88%	18.85%
GBI-EM Egypt	-0.82%	-1.74%	0.50%	2.01%	8.62%	0.50%
GBI-EM Indonesia	5.59%	5.44%	17.61%	24.16%	42.73%	17.61%
GBI-EM Malaysia	2.39%	2.13%	8.73%	10.45%	14.27%	8.73%
GBI-EM Peru	0.68%	-0.35%	-0.33%	1.22%	10.86%	-0.33%
GBI-EM Poland	-2.31%	-15.54%	-11.89%	-9.52%	1.35%	-11.89%
GBI-EM Russia	-0.60%	-4.37%	4.36%	12.44%	20.34%	4.36%
GBI-EM Slovakia	-0.26%	-7.81%	-11.79%	-11.18%	-2.87%	-11.79%
GBI-EM South Africa	-0.98%	-3.26%	1.19%	5.31%	10.40%	1.19%
GBI-EM Thailand	1.70%	4.11%	10.07%	11.06%	13.17%	10.07%
GBI-EM Turkey	0.25%	-1.05%	0.76%	1.99%	14.13%	0.24%

**Spread as of 06/30/10; In US dollars; Source: JP Morgan Chase; Bloomberg*