BEACON'S POINT: LESSON EARNED

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CONFIDENTIAL – PROPRIETARY

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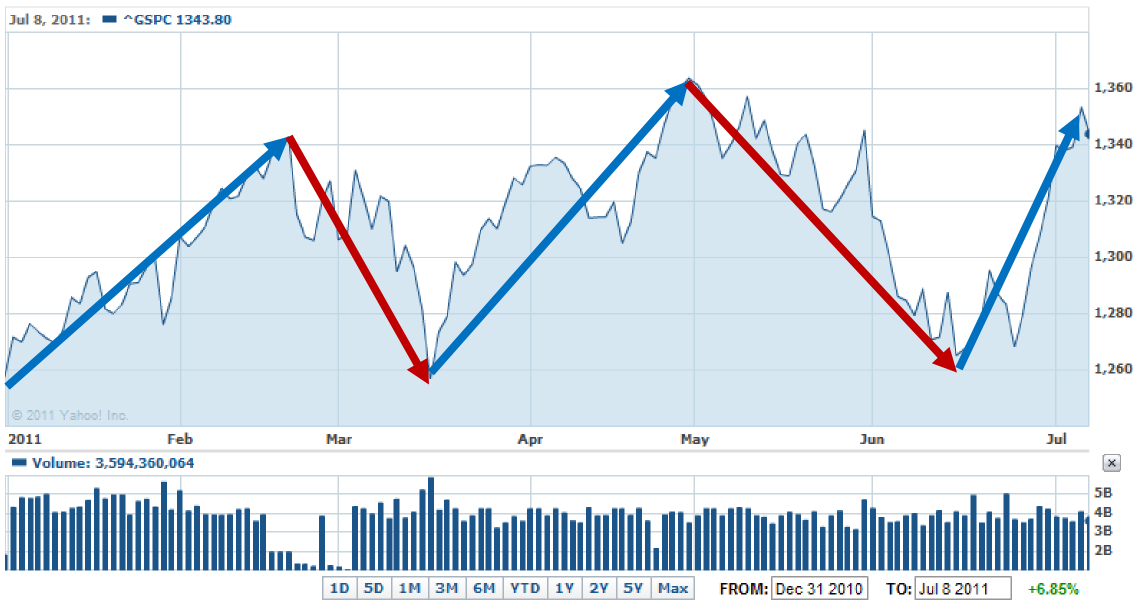
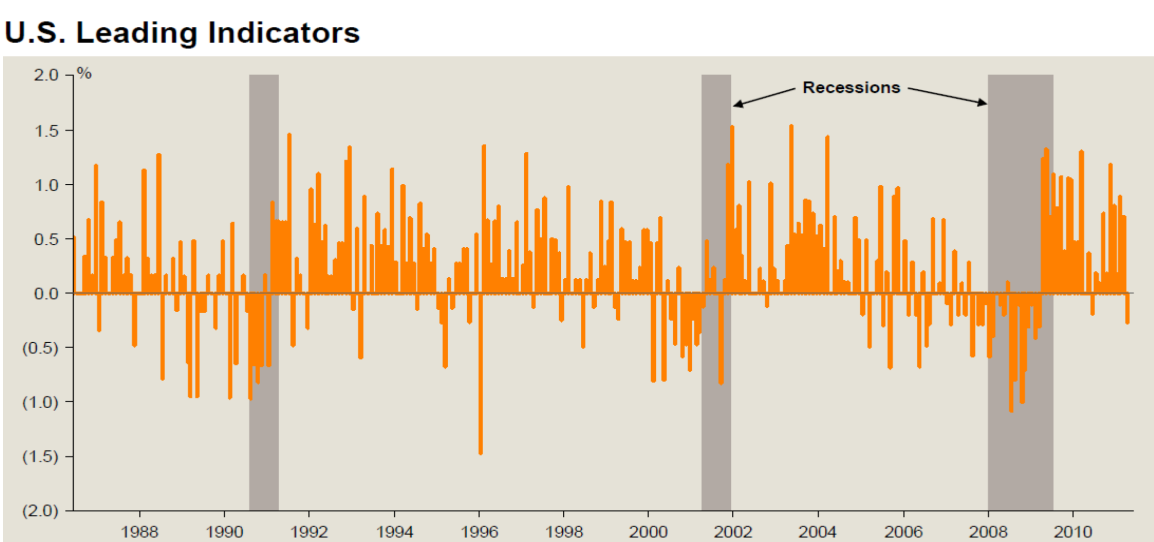
Lesson Earned

Financial markets seem unable to make up their mind, turning from pessimism to optimism on a dime, and leaving investors anxious, dazed, and frustrated. One of the biggest challenges for market participants is staying disciplined and not making long-term decisions based on short-term volatility and sudden price swings. As shown below, in the span of just six months, the S&P 500 Index experienced three separate legs up (+6.8%, +8.5%, and +6.9%) and two retracements (-6.4% and -6.5%). Whether or not we are in the midst of another correction since July 7th remains to be seen.



Source: Yahoo Finance

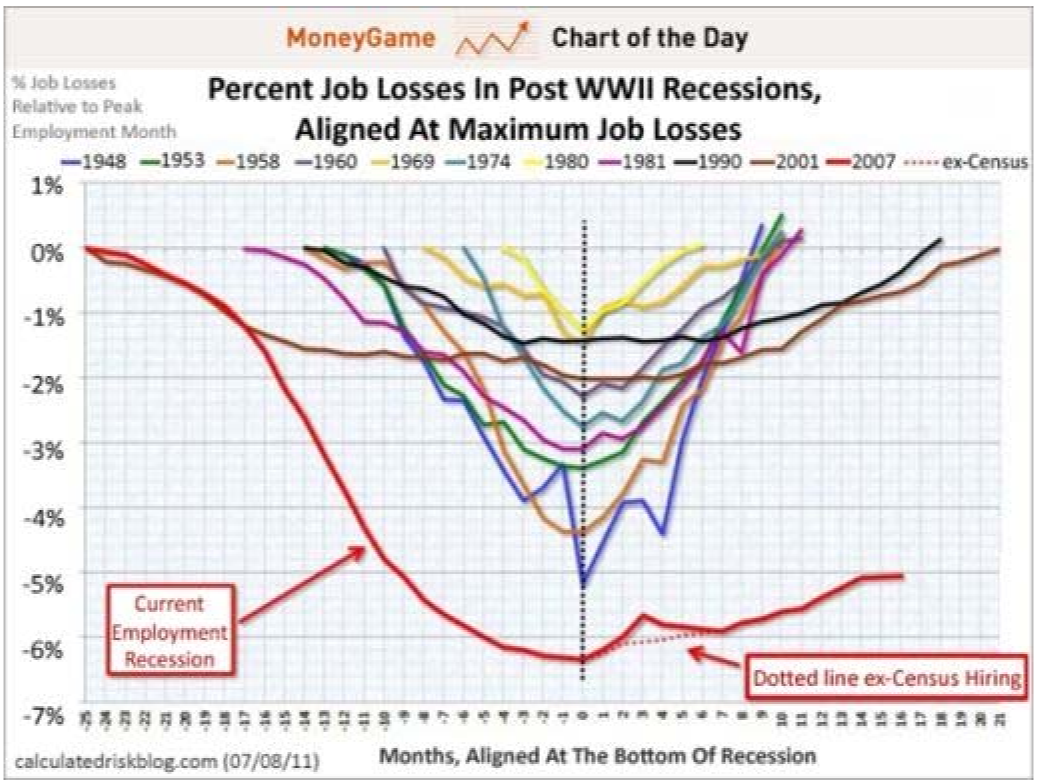
The summer months brought not only spectacular 4th of July fireworks, but a long list of issues clouding up the global economic and investment horizon. June 30th marked the end of the Fed's QE2 program, which many feared could destabilize credit and financial asset markets in the U.S. At the same time, the index of Leading Indicators fell below zero, indicating, at a minimum, a slowdown in the pace of the economic recovery.



Source: ING Global Perspectives

Never content to be out of the limelight, Washington DC is enveloped in crucial debates about ballooning budget deficits (on pace to reach $1.5 trillion in fiscal 2011) and the debt ceiling as the August 2nd deadline approaches. It is very possible that the two Congressional parties use up all their time until then to argue, battle, and politicize the issue before reaching a last-minute compromise and agreement. General expectations are for a deal that reduces spending by $2 trillion over the next decade and an increase in the debt ceiling by an equal amount. Volatility in the bond and currency markets is likely to be elevated leading up to the early August deadline.

The housing market's continued challenges are, by now, widely recognized and priced into the market. On the other hand, many had hoped that the job market was turning a corner. However, the latest U.S. employment report came in well below expectations - the U.S. economy added just 18,000 jobs in June and the unemployment rate ticked up to 9.2%. This exacerbates what was already the worst employment recession in our country's post WWII history, as shown in the exhibit below.

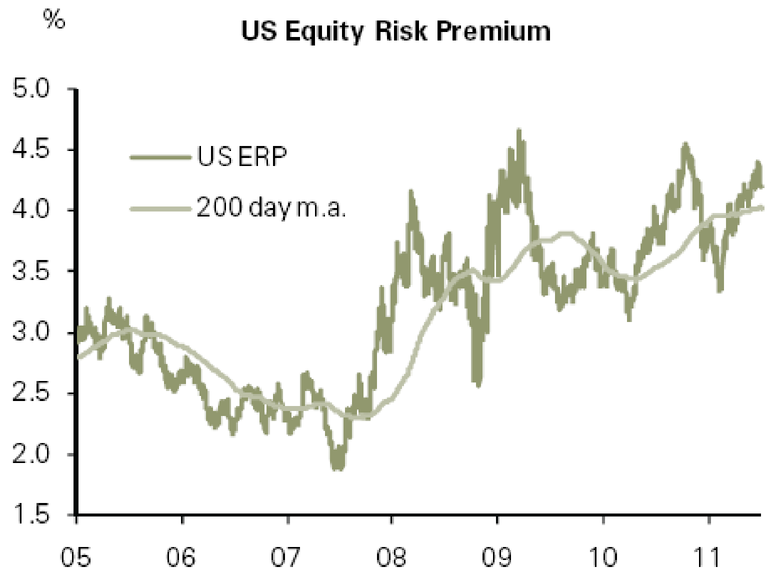


Source: Business Insider, Calculated Risk Blog

Across the pond, Europe continues to struggle with a sovereign debt crisis centered in Greece, but threatening to spread to other PIIGS countries. In recent days, Italy and Spain became the latest hot spots in the Euro debt drama, with developments still unfolding as we write this letter. Wells Fargo's Jeremy Ryan points out that Italy and Spain "have much larger economies than Greece and would thus have much more worrisome consequences should they be unable to service their debts. The spreads on Spanish and Italian 10-year debt hit euro-era record-level spreads against the benchmark German bonds, as investors demanded a much higher risk premium". Furthermore, although energy and food prices have retreated from recent highs, inflation measures in the developing world have not yet stabilized enough to give policy makers an excuse to stop tightening.

Despite these short-term uncertainties, there are several encouraging signs on the economic front, both domestically and internationally, including:

- The overall financial climate remains, on balance, accommodating for the world economy.
- Global M&A activity is vigorous and provides support for financial markets.
- The temporary disruptions in the global supply chain caused by the Japan disasters have begun to ease.
- Global corporations continue to report profit growth, although the pace of growth may prove uneven.
- The manufacturing sector in the U.S. is posting very solid results.
- In the U.S., even after the end of QE2, the expansion in credit continues.
- Commodity prices have pulled back significantly.
- The equity risk premium, including in the U.S. market (shown below) is still attractive.



Source: Goldman Sachs Asset Management

Undoubtedly, it has been an interesting first half of the year. The VIX Volatility Index has ranged from a high of 29.40 to a low of 14.60 during the YTD period. It currently hovers around the 20.00 level. Commenting on the market dynamics of the past several months, Jensen Investment Management stated that "levels of stock market volatility increased... and investor sentiment seemed to shift with each news headline." Equity markets, in particular, seemed to gain momentum rather quickly, then lose it even more quickly. With this up-and-down pattern, many market participants have fallen victim to extrapolating trends (either upward or downward) and reacting to short-term impulses.

Through hundreds of years of collective investment industry experience, Beacon Pointe professionals have learned - and earned - an invaluable lesson, which has become the core tenet of our investment philosophy and strategy. Successfully and consistently timing the market is virtually impossible to do and in some cases becomes a recipe for disaster. Investing with a mind towards your long-term goals and sticking with your discipline produces significantly better results than trading in reaction to short-term price fluctuations. And finally, identifying and entrusting the management of your portfolio with experienced, intelligent, and prudent investors, such as the ones recommended by Beacon Pointe, places you in the best position for both preservation and growth of your capital and the achievement of your investment goals.

Please feel free to call Beacon Pointe at 949-718-1600 should you need additional information or have any questions.