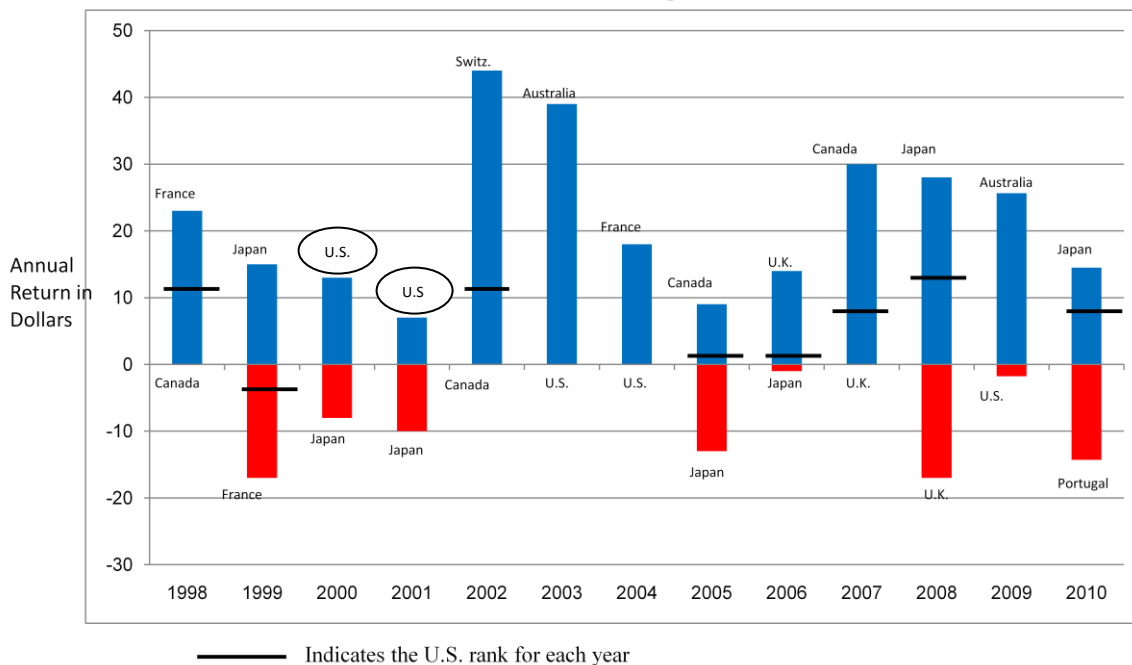


Opportunities in Non-Dollar Fixed Income Securities

The investment objective with non-dollar fixed income securities is to attain an excess return versus similar duration to US Treasury issues. The total return is comprised of interest income, price change of the bond and change in the foreign currency vis-à-vis the US dollar. Returns in this sector have the potential to enhance the returns earned in the traditional USD fixed income sectors. For example, since 1998 there have been only two years where the US market outperformed the rest of the Citigroup World Government Bond Index (see chart below).

Global Bond Markets Annual Returns
1998 Thru August 2010



In addition, non-dollar investments offer greater diversification, greater selection and lower risk. The US represents only 28% of the Citigroup Index (see table below).

Composition of Citigroup WGBI as of August 2010

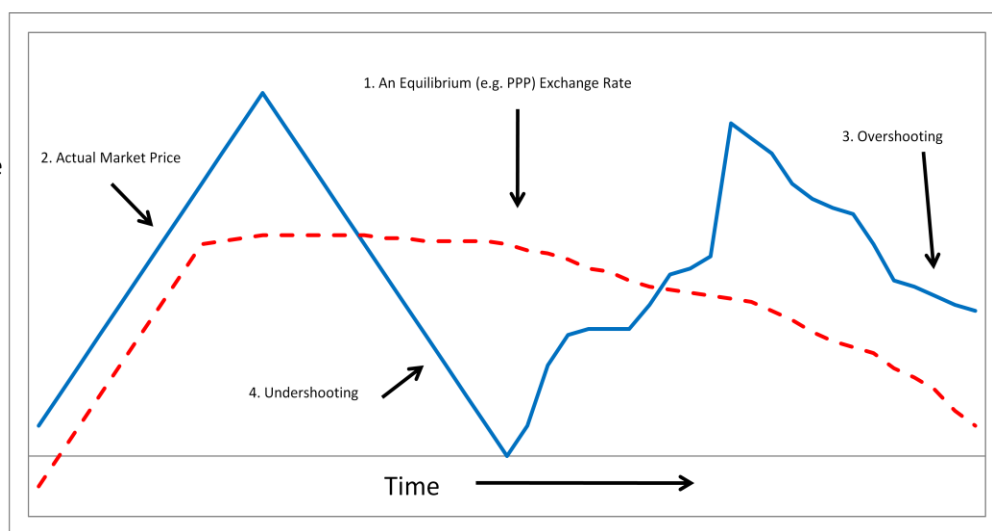
Country	%
Japan	30.57%
U.S.	28.21%
Italy	7.31%
Germany	6.77%
France	6.70%
United Kingdom	5.39%
Canada	1.99%
Belgium	1.97%
Netherlands	1.71%
Miscellaneous	9.38%

We believe that a reliable risk premium is embedded in the currency market, which can be exploited to add value. More importantly, the currency risk premium is uncorrelated to the risk premiums of stocks and bonds. Currency transactions approximate \$3 trillion on a daily basis. This implies exceptional liquidity and low transaction costs.

We utilize high quality credits when investing in non-dollar fixed income securities. This helps minimize credit risk that otherwise would be present. In addition to high quality credits, we use short duration/maturity issues. This has the effect of reducing interest rate risk. By minimizing credit and interest rate risk we are able to structure the investment so that the greater part of the return is from the foreign currency changes versus the USD. Currencies utilized include the Group of 7, Swiss franc and Australian dollar.

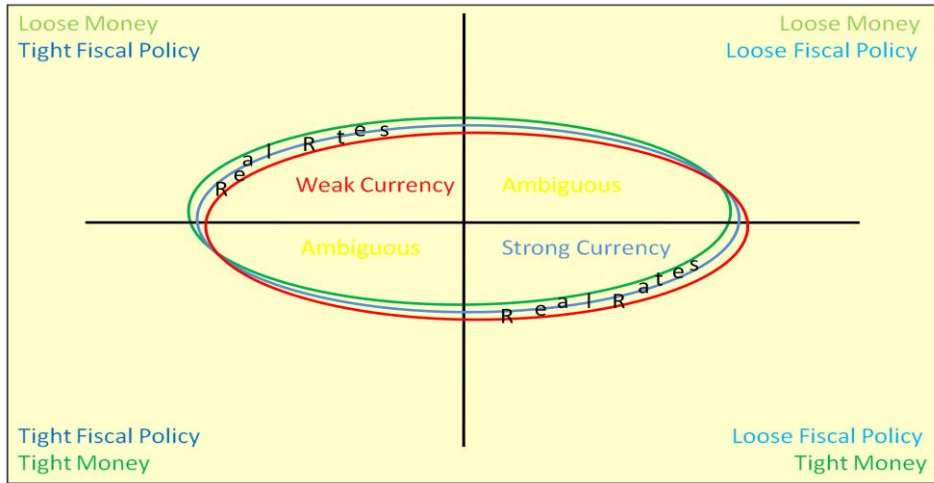
Exchange rate determination can be analyzed using several variables. Variables monitored include interest rate differentials, trade and fiscal balances, money supply and purchasing power parity. The consensus view is that the greater a country's interest rate differential versus other countries the stronger its currency. However, there are numerous instances where the US interest rate differential increases while the US dollar index weakens and vice versa. Also, a weak balance of payments is associated with a relatively weaker currency. However, issues arise such as which balance (trade or current account) to choose. Trade depends on income and prices and, as a result, it raises the issue of whether one should just focus on domestic policies. In addition, there is the question of causality and whether foreign exchange levels affect the trade position or vice versa.

The process we follow is to use purchasing power parity (PPP) to separate out equilibrium from disequilibrium positions. PPP takes into account the goods and services that a country's currency actually buys at home. We monitor the actual exchange rate vis-à-vis an equilibrium exchange rate to identify levels that overshoot and/or undershoot the equilibrium (see below).



We then concentrate on the disequilibrium movements. We have found that movements away from the trend are highly sensitive to the interaction of fiscal policy and monetary policy and real interest rates. A combination of a loose fiscal policy and a tight monetary policy generally results in a strong currency and vice versa. For example, during the Reagan Administration a combination of tax cuts and a buildup of the defense structure resulted in a loose fiscal policy. At the same time, monetary policy was tight due to Fed Chairman Volcker's policy of squeezing very high inflation from the economy. This combination of loose fiscal policy/tight

monetary policy certainly played a role in the strong dollar during this period. The trade weighted dollar increased approximately 50% from 1980 to 1985 (see below).



A more recent example of this process and the potential returns available are reflected in the performance of the Canadian dollar. The attached graph traces the value of the CAD versus the USD during the last year. Several elements argued for a stronger CAD versus the USD. The Canadian banking system was in much better shape than a number of the global economies and as a result their financial system and economy weathered the 2008 financial implosion much better than others. In particular, Canada did not have the speculation in residential real estate that occurred in other countries. In addition, as a “commodity” currency the CAD has benefitted from the strength of both the metals and energy sectors. The government of Canada runs a very small trade deficit. GDP for the last 12 months is running at a relatively strong 3.8%. This has caused the Bank of Canada to be concerned about potential inflationary pressures and they have raised their central bank rate twice (June and July 2010). This relatively tighter monetary policy has been one of the major factors supporting a stronger Canadian dollar. As a result, the CAD has appreciated 5.82% during the last year versus the USD-rising from 0.91 to 0.963. The Canadian two-year government has a total return of 5.81% over the last year in USD terms versus the 2-year US Treasury total return of 1.19%.

CAD / USD
8/13/09 - 8/13/10

