VANTAGE CONSULTING GROUP
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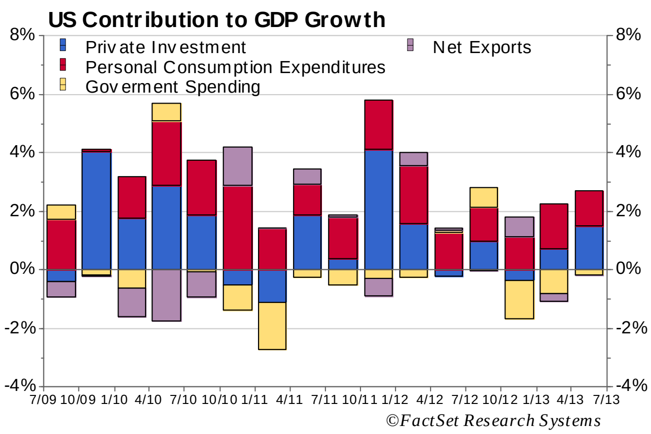
Market Review

August 2013

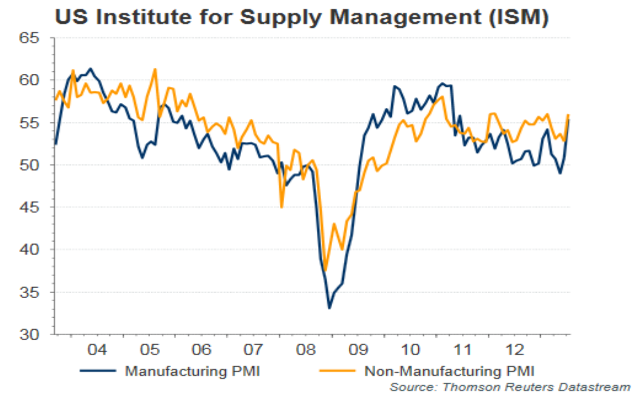
Economic Review

U.S. real GDP growth in the 2nd quarter of 2013 was revised to 2.5% from 1.7%. Positive contributions to the upward revision came almost entirely from net exports, as U.S. exports' contribution to GDP came in at the highest level since 2010. In addition to exports, U.S. GDP continues to see positive contributions from personal consumption expenditures and non-residential fixed investment. Contraction in government spending is the largest negative contribution to GDP.



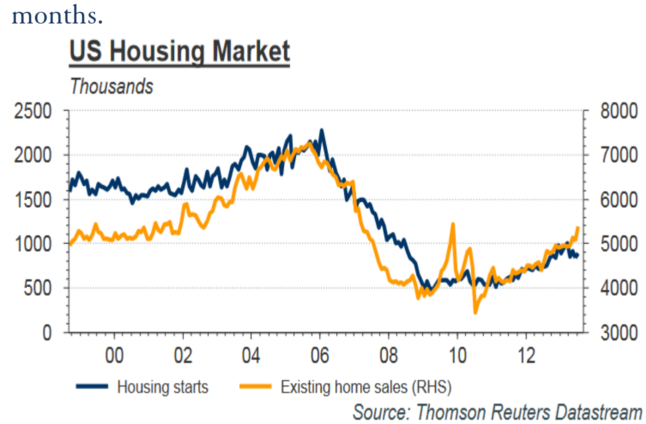
The U.S. labor market delivered mixed results in August, as the impact of a weak U.S. recovery and regulatory uncertainty continue to impede steady job growth. Jobless claims fell to a near 5-year low in August, with applications for benefits falling to a four-week average of 331,250. Employers added 169,000 jobs last month vs. 173,000 expected, and have added an average of 192,000 per month in 2013. The Labor Department revised July's jobs figures down to 104,000 from a reported 162,000. The headline unemployment rate eased down to 7.3%, though this is mostly due to a lower labor participation rate. The participation rate was down to 63.2% in August, the lowest reading since August 1978.

The U.S. Institute for Supply Management (ISM) data showed surprising strength, as improvements in the housing market and in manufacturing signaled potential for a strengthening in the economic recovery. The Manufacturing Purchasing Managers Index (PMI) surged to 55.4 in July from 50.9 in June. New Orders increased in July by 6.4 percentage points to 58.3%, and the Production Index was up 11.6 percentage points to 65%. The Employment Index climbed to 54.4%, from 48.7 and the Prices Index, which measures raw material costs, fell 3.5 percentage points to 49.0%. The Non-Manufacturing PMI rose to 56 from 52.2. A reading above 50 indicates expansion, while a reading below 50 indicates contraction.



The Consumer Price Index (CPI) rose 0.2% in July, primarily driven by increases in housing and energy prices. The CPI has increased 2% for the last twelve months. Core CPI (CPI ex food and energy) increased 0.2% month over month and 1.7% on a yearly basis. Personal Consumption Expenditures (PCE) rose 1.4% y/y in July compared to a 1.3% increase in June. Core PCE (PCE ex food and energy), the Fed's preferred indicator for gauging inflation, increased 1.2% y/y. The 5 Year/5 Year forward breakeven inflation rate closed at 2.38% in August, a 7 basis points decline from July.

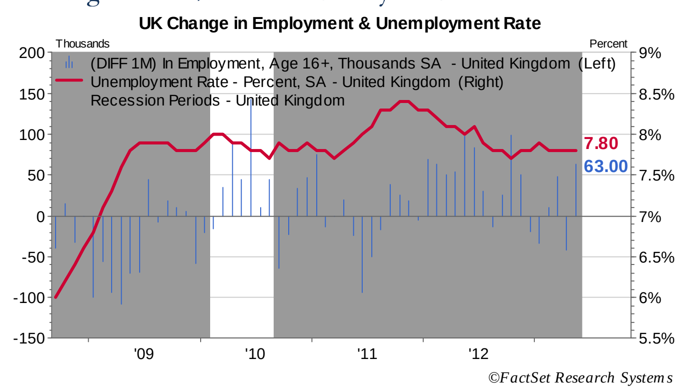
Housing data were disappointing in August, as rising interest rates slowed the recovery in the U.S. housing market. Pending home sales, which track existing-home contract signings, fell 1.3% in July, falling for the second consecutive month. Overall mortgage applications have plunged 53% since May 3, including a fall in refinancing applications of 64.1% and a decline in purchase applications of 14.1%. Home prices across 20 large U.S. cities grew by 0.9% in June, according to the S&P Case-Shiller Home Price Index. The Index is up over 12% over the last 12 months.



The Federal Open Market Committee left monetary policy unchanged in August and indicated broad support for Chairman Ben Bernanke's tapering timeline. The Committee reaffirmed its position to leave Quantitative

Easing unchanged in the short-term, though most members felt it may be appropriate to begin reducing purchases soon. The Committee did have some level of disagreement over the impact of higher long-term interest rates on the recovery.

The European economy showed some signs of strengthening in August. UK real GDP grew at 0.6% (sequential) during the second quarter vs. 0.3% (sequential) in the prior quarter. The July UK services PMI came in higher than expected at 60.2 (+3.3 from June), the highest reading since 2006. Their manufacturing PMI rose from 52.5 in June to 54.6 in July. The Bank of England kept policy unchanged, but gave an explicit forward guidance by pledging to keep its benchmark interest rates low and the bond purchase program intact until UK's jobless rate fell to 7%. The current unemployment rate in UK has remained unchanged at 7.8% since February 2013.



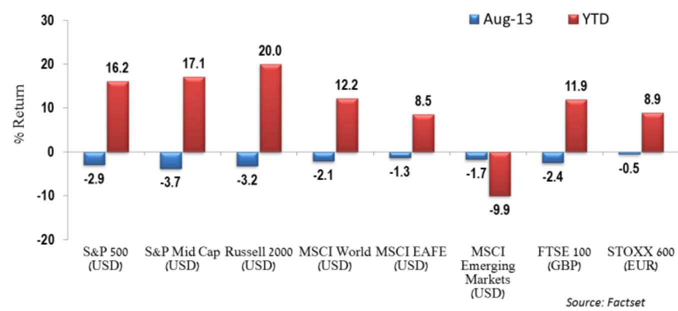
After posting six consecutive quarters of economic contraction, the Eurozone finally posted a positive economic number. Real GDP grew at +0.3% (1.1% a.r.) on a sequential basis in the second quarter. The July Eurozone manufacturing PMI came in at 50.3, the first time above 50 since July 2011. The European Central Bank kept its policy rate on hold at 0.5% and stated that its monetary policy will remain accommodative for as long as necessary.

Equity Markets

Equity markets fell across the board in August, as continued tension in the Middle East and Federal Reserve tapering speculation weighed on stocks. The S&P 500 fell 2.9% in August, returning a negative month for only the second time in 2013. Domestic Mid and Small Cap stocks performed worse, each falling over 3%. International stocks fell in August as well, as the MSCI World Index and the EAFE Index each lost over 1%. Emerging Markets (EM) fell 1.7%, and continue to lag other indices year-to-date. The FTSE 100 and STOXX 600 indices, the main benchmarks for British and Eurozone stocks, lost 2.4% and 0.5% in August, respectively.

Stocks continue to be highly reactive to announcements surrounding the Federal Reserve's stimulus programs. Speculation that the Federal Reserve may taper bond purchases continues to unnerve the markets. The lack of clarity regarding Federal Reserve Chairman Ben Bernanke's replacement in January is another factor weighing heavily on markets. The two top candidates are former Treasury Secretary Larry Summers and former San Francisco Fed President Janet Yellen. While Yellen is categorically viewed as dovish, Summers has recently made anti-stimulus comments. In addition, markets were further unsettled by civil unrest in Middle Eastern countries such as Egypt and Syria, and increasing prospects of U.S. military involvement.

Equity Market Performance



Bond Markets

U.S. Treasury Bonds as measured by the Barclays US Government Bond Index declined 0.5% in July, extending its YTD loss to 2.6%. Treasury markets rallied in late August, with 30-year Treasury yields declining over 20 bps, on concern over potential military action by U.S. against Syria. In spite of this rally, Treasury yields finished August higher. Credit spreads widened marginally as demand for credit mostly offset geo-political risks and taper-induced interest rate volatility. The credit index option adjusted spread (OAS) closed at 135 basis points, 3 points higher than the June close. High yield bonds suffered another month of negative returns, primarily due to higher treasury yields as high yield spreads remained unchanged. The Barclays U.S. Corporate High Yield Index fell by 0.6%, trimming its YTD gain to 2.7%.

The yields on the 10-year and 30-year U.S. Treasury Bonds increased 20 and 6 bps respectively. The 10-year Bond closed at 2.78%, while the 30-year Bond closed at 3.70%. The yield on German 10-year benchmark bonds increased 18 bps to close July at 1.85%. The yield on UK 10-year benchmark bonds climbed 23 bps to close at 2.59%.

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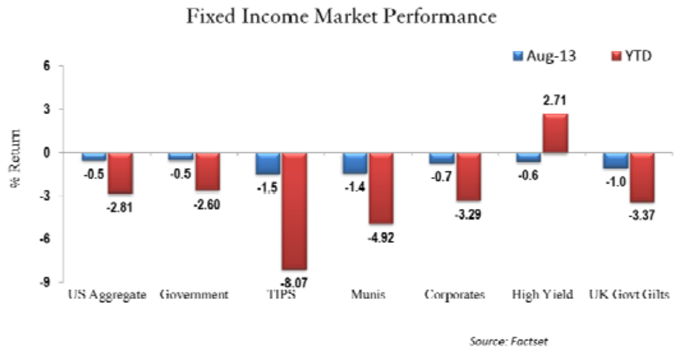


Commodities

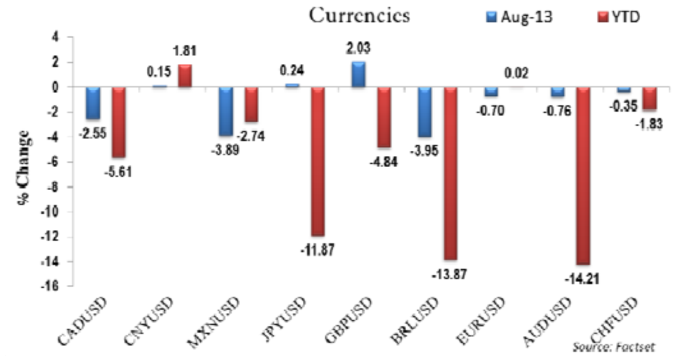
The S&P GSCI Total Return Index, a gauge of 24 leading raw materials, gained 3.38% in August, as Energy prices continued to rebound and Precious Metals rose sharply for a second straight month. The Precious Metals sub-index, which remains down 17.9% in 2013, rallied 7.89% in August and has advanced 14.7% in the last two months. The Petroleum and Energy sub-indices each gained over 3.9%, as continued turmoil in Egypt and new concerns about a U.S. engagement in Syria sent oil and refined product prices higher. The Softs sub-index, which tracks crops such as coffee, sugar, and grains, was the only sub-index to post a negative month, down 2.55%. As soft commodities are a major component of emerging economies' exports, the continued depreciation in Emerging Market currencies has put downward pressure on soft commodity prices.

Silver posted the largest gain for any individual commodity, up 19.5% in August. Gold also had a strong month in August, gaining over 6.3%. Precious Metals rallied as equity markets sold off during the month, amid speculation of changes in Federal Reserve leadership and stimulus policy. Soybeans gained 12.5% in August, as heat and drought concerns raised supply concerns for next harvest. Crude Oil rose 3% in August, and Brent Crude rose 5.78%.

The Emerging Market currency crisis has had a significant impact on the price of export crops from emerging economies. Coffee fell 4% in August and is down 24.9% in 2013, with most of the decline occurring after the May announcement of Federal Reserve tapering. Similarly, Sugar fell 3.7% in August and is down almost 18% this year. Wheat fell 3.5% in August, as better than expected crop yields from some European markets boosted supply forecasts and sent prices lower.

Currency

The US Dollar Index, a measure of the Dollar against six trading partners, gained 0.8% to close at 82.09, bringing the YTD gain to 2.9%. The Euro depreciated 0.7% against the US Dollar to close at 1.3186 USD/Euro. The British Pound rallied 2.03% against the US Dollar on better than expected economic news, to close at 1.5469 USD/GBP.



Emerging economies with large current account deficits saw their currencies depreciate significantly. Current account deficits, financed by capital inflows, widened as foreign investors sold emerging market assets as these became relatively less attractive. Rising crude oil prices threaten to exacerbate the current account deficit in countries like India, which imports nearly 80% of its oil. The currencies of Brazil, India, Turkey, and Indonesia depreciated significantly over the last three months. The Indian Rupee depreciated over 22% since May (8.7% in August) and hit record lows against the US Dollar. The inaugural speech during the first week of September by Raghuram Rajan, the newly installed governor of the Reserve Bank of India, was received positively by the markets. The Brazilian central bank increased its benchmark interest rates by 50 bps in an effort to stem currency depreciation and keep the inflationary expectations in check.