"Advancing Your Investments"
NEW ENGLAND PENSION CONSULTANTS

To: NEPC Clients

From: NEPC Asset Allocation Committee

Date: August 7, 2007

Subject: Is the cycle of fear and greed turning again?

We know that investment markets can be like the arc of a pendulum: fear and greed dominate investor psychology at the points where cycles reverse. Greed dominated the markets in early 2000 right before their epic correction. In 2002, fear dominated as global equities were about to compound at almost 20% per year for the next four years. As the arc of fear reached its peak in 2002, NEPC noted the enormous opportunities that had arisen in international and emerging markets, global bonds, and anything credit related. We correctly positioned our client portfolios for the rebound and we have enjoyed five years without a meaningful pullback along the way.

Understanding the power of cycles, we've developed a growing unease over the last year that things had gone too well and too easily, for too long. With excellent gains in the bank, we focused our 2007 Asset Allocation Letter on reducing risk. We noted that volatility was historically low and compensation for taking risk, e.g., credit spreads, had become non-existent. The path of action was clear: we recommended reducing risk by diversifying away from equities while maintaining returns through "better beta" portfolios and alternative investments, especially hedge fund and "cash plus" investment strategies.

Many clients have heeded our message. Equity allocations are down, alternative investments are up, and liability hedging is in place for those pension clients wishing to stabilize their funded status. We feel comfortable that these portfolios are better prepared for the transition of greed into fear. As professional investors, we know there will be ups and downs in markets. We also know that the biggest mistakes are often made at the extreme of the pendulum's arc. While it is our job to mitigate the impact of declining markets while participating in favorable markets, neither we nor anyone else can call the swing back of the pendulum's arc perfectly. We may have been early, but fundamentals will prevail in the longer run.

Despite media coverage regarding a credit crisis, hedge fund blowups, and sub-prime mortgage contagion, well-diversified portfolios have weathered the credit market correction better than one would think. As expected, risk and volatility have made their way back into the market, causing some losses in July (see table on page 2) but year-to-date returns remain in positive territory for most asset classes.

Stocks	July	2007 YTD
S&P 500	-3.1%	3.6%
Russell 2000	-6.8%	-0.8%
MSCI EAFE (net)	-1.5%	9.1%
MSCI Em Mkt (net)	5.3%	23.8%

Bonds / Hedge Funds	July	2007 YTD
LB Aggregate	0.8%	1.8%
LB High Yield	-3.5%	-0.8%
Salomon WGBI	3.0%	2.6%
HFRI Fund-of-Funds	0.5%	8.4%

Despite the broad market returns, there have been some isolated but fairly significant losses in specific funds or market subsectors. And there is still reason for caution. Significant imbalances were created over the past few years and as volatility increases and greed turns to fear, there will inevitably be more dislocations before the markets stabilize, particularly in areas that have employed excessive leverage.

Successful investing is about the management of risk, particularly as the arc of the pendulum reaches its peak. We see extensive evidence that diversified portfolios consistently weather the storm better than those that are heavily concentrated in traditional stocks and bonds. Asset class diversification is critical to help balance broad market swings. Diversification at the strategy and manager level is designed to reduce the impact that any single event or manager can have on the total portfolio. Disciplined rebalancing is useful in managing risk and in taking emotion out of the picture at both ends of the pendulum's swing.

We recognize that the media covers "events" more aggressively than continued excellence, and that market turbulence and related stories about hedge fund manager blow-ups create worry for our clients and their constituencies. That said, our clients have weathered the current credit crisis well, particularly those who have diversified their portfolios into alternative assets. In fact, our initial findings suggest that virtually all of our hedge fund placements have outperformed traditional stocks and bonds in 2007.

Our focus as your investment consultant is to help you choose the most appropriate course to meet your investment goals. We also recognize that we need to help guide you through the inevitable turbulent times. To date, our clients have performed far better than the media's negative hype would suggest.

Should problems in the sub-prime markets extend to other markets, opportunities will present themselves to the disciplined and prepared investor. For all the talk about the implosion of some hedge funds, many are overlooking the fact that other hedge funds are buying their assets for cents on the dollar. In times of stress, there will be selling at any price. The mispricing that occurs when the pendulum is at an extreme, either dominated by fear or greed, gives the long-term investor significant opportunities to benefit through sound investment principles.

We appreciate the opportunity to work with you and are honored by the trust that you put in us as your investment consultant. We promise to continue striving to retain your trust.