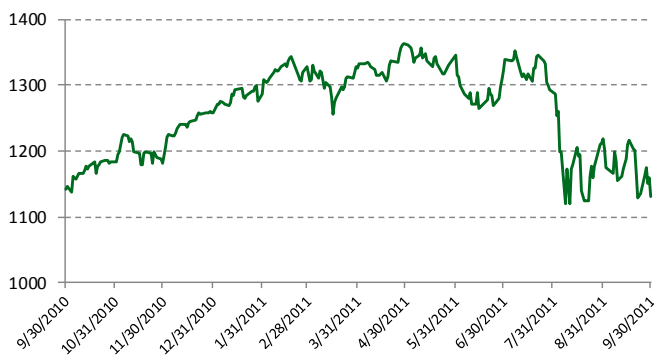




Financial Review

After displaying some signs of weakness earlier in the year, global equity markets sold off aggressively in the third quarter. The S&P 500 Index fell 13.9 percent during the quarter, marking its worst quarterly performance since the fourth quarter of 2008. Higher-risk areas of the market were hit even harder. The international developed market index (EAFE) declined 19.0 percent, while the U.S. small cap index (Russell 2000) and the emerging market index plunged 21.9 percent and 22.6 percent, respectively. The outsized equity market declines were driven in large part by a crisis in confidence among investors, as prior concerns over an extended period of anemic growth shifted toward the more daunting prospect of an outright recession.

S&P 500 Performance



At this point, it remains unclear whether the U.S. economy is heading into (or is already in) another recession. The United States appeared to be on the path toward a self-sustaining economic recovery earlier in the year, but that foundation started to crack as fears of economic contagion from the

European credit crisis continued to escalate. With confidence in the safety and solvency of European government debt continuing to deteriorate, the health of Europe's banking system is now in jeopardy. The cascading effects of a European banking meltdown on the rest of the global economy could be severe, to say the least, which explains the market's heightened state of anxiety. The European Central Bank and other policymakers have been moving more aggressively of late to stem the crisis through debt restructuring and austerity measures, but the situation remains a difficult one to ameliorate quickly, and waning confidence in the market is complicating matters further.

On this side of the pond, the Fed recently ramped up its own efforts to promote a stronger domestic recovery by instituting "Operation Twist." Under this round of monetary accommodation, the Fed will purchase \$400 billion of long-term Treasuries (maturities of six to 30 years) and finance this operation with sales of an equal amount of short-duration Treasuries (three-year maturities or less). The hope is that this will bring down long-term borrowing costs and spur increased economic activity. The plan appears to have already achieved the first of the Fed's two objectives, as the 10-year Treasury rate and 30-year mortgage rate fell to record lows following the program's announcement. Interest rates were already near historically low levels, however, so it is still unclear whether or not the further decline in borrowing costs will spark a material increase in corporate investment or housing market activity.

Recent monetary stimulus programs have had limited success in driving economic recovery, and this latest iteration is unlikely to be different in our view. The markets are now in the regrettable position of relying on policymakers and politicians to make the deep structural and fiscal policy changes needed to stave off financial calamity. Fortunately, there is now heightened awareness of the severity of overleveraged sovereign balance sheets and an increased sense of responsibility in American and European political circles to address the problem. As was the case during the credit crisis of 2008 and 2009, we believe policymakers will ultimately make the proper decisions to stabilize the current crisis, which will inject renewed confidence back into the market.

The prospect of financial turmoil has elevated fear and uncertainty in the current market to levels not seen since late 2008. While we acknowledge the economic environment remains precarious and will require close monitoring, there is no better time to take on risk than when others are shunning it. At current valuation levels, we think the equity markets offer compelling risk-adjusted return opportunities. The S&P 500 Index was trading at just 10.1 times projected 2012 earnings at the end of the third quarter. That is an exceptionally low multiple compared with the S&P 500 Index's long-term average earnings multiple of 16.4. While current 2012 earnings estimates are likely too high, we expect those projections to fall as global GDP forecasts continue to shrink. That said, earnings would have to come in nearly 40 percent below current estimates to bring the S&P 500 back to its historic earnings multiple. While such a substantial decline is not out of the realm of possibility if an acute global recession begins, we believe corporate earnings will prove much more resilient than what is currently being priced into the market.

As a result, we plan to continue to look for mispriced securities to deploy some of the excess cash we've been holding for this occasion conservatively and opportunistically.

Core Equity Portfolio

During the quarter, we initiated positions in Hasbro, MetLife, PepsiCo and U.S. Bancorp.

Hasbro (HAS) is the second-largest maker of toys and games in the United States (behind Mattel), with an extensive portfolio of brands that includes Nerf, Playskool, Play-Doh, Tonka, Transformers, G.I. Joe, My Little Pony, Monopoly, Trivial Pursuit and Scrabble. The company also launched a children's cable channel (The HUB) in late 2010, which broadcasts television programming based on Hasbro's toy and game brands. While not a significant profit center in and of itself, we believe this venture will drive considerable revenue expansion for Hasbro since entertainment-backed brands have exhibited substantially higher growth rates in recent years than non-entertainment-themed toys and games. In addition to selling its own brands, we see compelling opportunities for Hasbro to leverage its long-term merchandise licensing rights to the brands of several key partners (Sesame Street, Star Wars and Marvel Comics) in the coming years.

MetLife (MET) is the largest life insurer in the United States. The company acquired AIG's American Life Insurance Company in 2010, which tripled the size of MetLife's international business. By increasing its international exposure, MetLife will recognize higher growth and higher margins as the company writes insurance in less efficient, less regulated markets. Given its limited European exposure (less than 5 percent) and solid

balance sheet, we believe MetLife is well-positioned to ride out the current economic storm and will ultimately be rewarded on the other side for its revamped above-average growth profile.

PepsiCo (PEP) operates beverage, snack and food businesses worldwide. We believe the company's stable business model and strong portfolio of brands will do well in a domestic economy with little to no growth, but it also provides exposure to the fast-growing emerging markets. In addition, we like that PepsiCo has a sound balance sheet and cash flow profile to support its 3 percent-plus dividend yield, which is particularly attractive in this cycle of exceptionally low interest rates.

U.S. Bancorp (USB) is one of the country's largest financial institutions. It is an exceptionally well-managed bank with a diverse earnings stream and conservative risk management. This is highlighted by the fact that the company did not experience a single quarterly loss in the recent financial crisis. Despite its stable risk profile and operating history, the company's shares have sold off aggressively with the rest of the banking sector. We believe the magnitude of U.S. Bancorp's decline was unfounded and think the stock offers an attractive opportunity at its depressed valuation.

To make the purchases mentioned above, we exited our positions in Nestle, Baxter and QLogic.

Nestle (NSRGY) is the world's largest food producer. We liked the stability of the packaged food company's product portfolio, as well as its growth prospects. After the shares climbed above our valuation target, however,

we decided to sell our stake in the company to raise cash that we could put to work in a more attractive opportunity.

Baxter (BAX) manufactures products to treat immune disorders and other chronic and acute medical conditions. We continue to believe select areas of the health care sector will offer enticing returns during the coming years. This was our smallest health care position in the portfolio, however, and, based on our growth projections going forward, we believed the stock offered limited near-term upside at its current valuation levels.

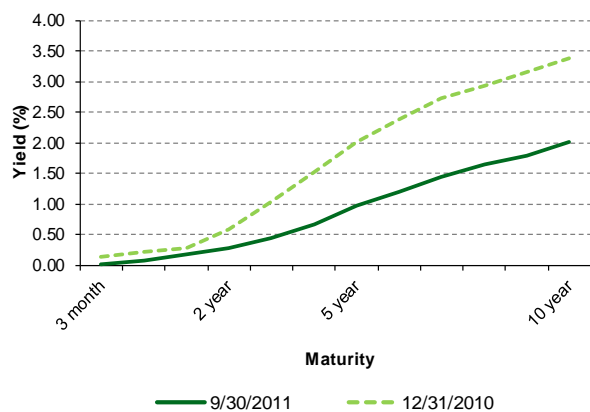
QLogic (QLGC) was a technology investment we made in the network infrastructure hardware space to capitalize on increases in data storage needs and growth in server virtualization, or cloud computing. While we continue to believe in the underlying thesis of this investment, we ultimately decided the growth opportunity at QLogic was inferior to other prospective investments.

Fixed Income Markets

Yields on fixed income securities dropped significantly in the third quarter, as investors aggressively shifted assets toward less risky investments. The combination of a sovereign debt crisis in Europe, political dysfunction in Washington, weakening economic data in the United States and the Federal Reserve's move to purchase longer-term treasuries all contributed to the demand for the perceived safety of U.S. treasuries. Yields on 10-year treasury bonds finished the quarter at 2.01 percent, a decline of 129 basis points from June.

September 30, 2011

Treasury Yield Curve



The shift in the treasury yield curve did not fully impact all sectors of the bond market, with municipal and corporate bond spreads becoming particularly attractive in mid- and longer-term maturities (five to 10 years).

Alternative Investments

Event-Driven and **Credit** strategies preserved capital much better than equity markets, but were not immune from the turmoil that hit capital markets. Credit spreads widened, reflecting investors' desire to reduce risk assets from their portfolios. At today's prices, base case return assumptions for event-driven trades are better than the optimistic scenarios only a few weeks back.

During times of steep market declines, prices fall in unison, making it very difficult to add value through stock selection. Only **Equity Long/Short** managers that had significantly cut gross and net exposure prior to the market downturn were able to preserve capital. Managers used the quarter's volatility to increase exposure in higher-conviction names and add to positions that performed better than their industry groups and the overall market.

While **Real Estate** and **Private Equity** are both likely to experience an initial decline in deal activity, real estate investors may benefit as mortgage financing becomes more attractive with lower interest rates. Furthermore, the decline in public equity valuation levels may lead to additional interest on behalf of management teams and private equity funds to take companies private.

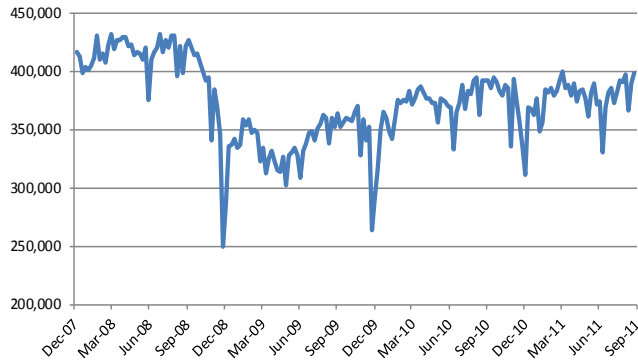
One Year Economic Overview

		Sep 2011	Sep 2010
Stock Market			
S&P 500 Index	▼	1,131.42	1,141.20
Russell 2000 Index	▼	644.16	676.14
Fixed Income Yields			
3-Month Treasuries	▼	0.02%	0.14%
5-Year Treasuries	▼	0.96	1.26
10-Year Treasuries	▼	2.01	2.54
30-Year Treasuries	▼	2.95	3.70
Inflation Monitor			
CPI-Trailing 12-Month Growth	▲	3.7%	1.1%
CPI-(Excluding Food/Energy)	▲	2.1	0.8
Market Expectations*	↔	1.9	1.9
Gold (per ounce)	▲	\$1,623.97	\$1,308.35
Crude Oil (per barrel)	▼	79.20	79.97

*Comparison of yields for 10-Year Treasury and 10-Year TIPS

Economic Barometers

North American Railcar Originations¹



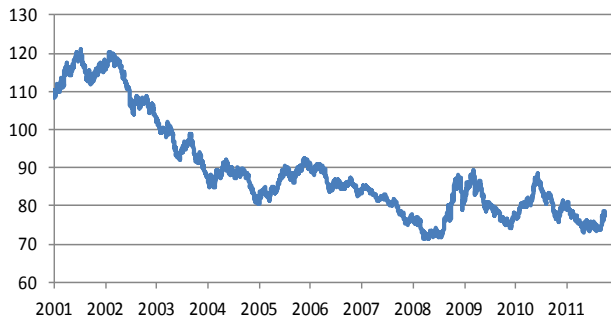
1 - A measure of economic activity

Baltic Dry Index (BDI)²



2 - A measure of global ocean shipping rates

The U.S. Dollar Index (USDIX)³



3 - The USDIX measures the international value of the U.S. dollar against six major world currencies

Baa Corporate Bond Spreads Over 10-Year U.S. Treasuries⁴



4 - Measures bond investors' appetite for risk