

Market Update

August 2011 Review

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A Summer to Forget

This summer was one we will all likely try to forget rather quickly, due to an earthquake on the East Coast, a hurricane that ripped through the Northeast and a stock market that has been steadily bleeding all summer. The Dow Jones Industrial Average ("DJIA") has not had a positive month since April and August was no different. The beginning of the month was filled with uncertainty and fear as investors anxiously awaited the United States Government's decision on the debt ceiling and the possibility of a credit downgrade loomed in the back of their minds. This led to sharp declines during the first ten days of the month as the DJIA fell 11.6% from the close of August 1st to the close of August 10th.

As expected, in the final hour, the decision was made to raise the limit, thereby avoiding a default on U.S. government debt. However, despite raising the debt limit, credit rating agency Standard and Poor's announced the downgrade of long term United States debt from AAA to AA+. Even with a lower credit rating, demand for U.S. Treasuries remained strong as the Barclays US Aggregate Govt-Treasury-Long Index rose almost 9% during August. The broad based Barclays Aggregate Bond Index also had a positive month, returning 1.5% which added to strong returns year-to-date.

Domestic equity markets trimmed some of the losses as markets turned up in the second half of the month. The blue chip DJIA ended down almost 4% for the month but remained in the black for the year, returning 2.1% year-to-date. The S&P 500 Index fared slightly worse as the index fell 5.4% in August.

Given the political tension in the House and Senate, the downgrade of U.S. debt and the volatility in the markets, it is no surprise that the Conference Board's Consumer Confidence Index fell from 59.2 in July to 44.5 in August, the lowest reading since April 2009. The unemployment situation continues to weigh on the minds of consumers as job creation in August was abysmal. The unemployment rate remained unchanged at 9.1% as only 17,000 jobs were created in the private sector, offsetting the 17,000 jobs lost in the public sector. Not only was there no job creation in August, but July's job creation total was revised down to 85,000 from 117,000. With consumers making up 70% of GDP, the labor market clearly needs to turn around for this economy to get back on track.

	August	YTD
DJIA	-3.96%	2.14%
S&P 500	-5.43%	-1.77%
NASDAQ	-6.28%	-2.16%
MSCI EAFE	-9.02%	-5.66%
MSCI Emerging Markets	-8.90%	-8.31%
Barclays Aggregate	1.46%	5.88%
Barclays Corp High Yield	-4.00%	1.94%

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While corporate profits are still the bright spot in the economy with after-tax profits growing at 3.3% in the second quarter, corporations remain reluctant to hire with so much uncertainty about the economy going forward. That said, company balance sheets continue to have excess amounts of cash, a good indicator that future spending on capital expenditures and/or hiring is a possibility once corporations feel more comfortable with where this economy is headed.

While U.S. economic data was not all that favorable in the month of August, neither was global data. Trouble continued in Japan as Moody's downgraded Japanese debt to Aa3, its fourth highest rating. Economic growth was also sluggish around the world as many countries reported slower growth during the second quarter compared to earlier in the year. Germany, currently Europe's strongest economy, reported slower growth while emerging countries such as India and Brazil also slowed in the second quarter.

The biggest issue overseas seemed to be the debt problems that continue to plague Europe. The European Central Bank continued to purchase Italian and Spanish bonds in order to keep yields from spiking, while concerns in Europe prompted talks of developing a "euro bond" which would be backed by the nations in the European Union. In the wake of the recent downgrades, Germany has not supported the "euro bond" as the country focuses on keeping their debt rated AAA. In an effort to calm the turbulent financial markets, four European nations temporarily banned short selling; however, international markets as measured by the MSCI EAFE Index declined 9.0% in August. Emerging countries fared slightly better than developed countries as the MSCI Emerging Markets Index fell 8.9%.

Although the consensus outlook seems grim, Federal Reserve Chairman Ben Bernanke reassured the nation that there are still a few tools in his bag of tricks. He claimed that although these tools are not necessarily needed now, measures can be taken that will hopefully send us back to stable market conditions when the time is right. The real question is: when will the time be "right" and how much can the government help our situation? With interest rates unable to go lower and government debt at an all time high, it is hard to imagine that our government has the power to pull us out of another potential crisis. However, we have seen over the past few months that a little good news goes a long way in the minds of the average investor so it may not take much to restore confidence to the masses.

Definitions & Disclosures:

An index is a measure of value changes in a representative grouping of stocks, bonds, or other securities. Indexes are used primarily for comparative performance measurement and as a gauge of movements in financial markets. You cannot invest directly in an index and, for comparative purposes; they do not reflect the effect of the various fees inherent in actual investment vehicles.

The S&P 500 Index is a market value weighted index showing the change in the aggregate market value of 500 U.S. stocks. It is a commonly used measure of stock market total return performance.

The Dow Jones Industrial Average is a price weighted index comprised of 30 actively traded blue chip stocks; primarily industrial companies, but including some service oriented firms.

The NASDAQ Composite Index is a market-value weighted index that measures all domestic and non-U.S.-based securities listed on the NASDAQ Stock Market.

Gross Domestic Product (GDP) is the market value of the goods and services produced by labor and property in the U.S. It is comprised of consumer and government purchases, net exports of goods and services, and private domestic investments. The Commerce Department releases figures for GDP on a quarterly basis. Inflation adjusted GDP (or real GDP) is used to measure growth of the U.S. economy.

The MSCI Europe and Australasia, Far East Equity Index (EAFE) is a market capitalization weighted unmanaged index developed by Morgan Stanley Capital International to measure approximately 1,100 securities in 21 major overseas stock markets. It is a commonly used measure for foreign stock market performance.

The Barclays Capital U.S. Aggregate Index covers the U.S. Dollar denominated investment grade, fixed-rate, taxable bond market of SEC-registered securities.

The Barclays Capital U.S. Corporate High Yield Index covers the U.S. Dollar denominated, non-investment grade, fixed income, taxable corporate bond market. Securities are classified as high-yield if the middle rating of Moody's Fitch, and S&P is Ba1/BB+/BB+ or below.

The MSCI Emerging Markets Index (EM) is a free-float-adjusted market-capitalization index developed by Morgan Stanley Capital International. It is designed to measure the equity market performance of 26 emerging market countries.