

Market Commentary

Perspectives from Wilshire Consulting

Second Quarter 2008

Economic Highlights

Interest Rates: After lowering the Fed Funds rate by a quarter-point to 2% in April, the Fed kept rates unchanged in their June meeting. Despite the Fed's additional easing, 10-year Treasury yields moved notably higher; entering the quarter at 3.45% and closing as high as 4.27% on June 13th before ending the quarter at 3.99%.

GDP: Real GDP grew 1% in the first quarter, refuting calls by many economists that the U.S. had entered into a recession in early 2008. However, coupled with soft GDP growth of 0.6% in Q4 2007, the first quarter GDP stats confirmed that the economy has slowed.

Source: Commerce Dept.

Inflation: Commodity prices continued to soar during the quarter with oil prices in particular grabbing the national spotlight. The price for a barrel of oil rose 38.7%, spiking from \$101.58 to \$140 in the quarter. CPI reflected the impact of rising food and energy costs as it increased from the 2% to 4% range over the past year (see nearby chart). Those of us who neither eat food nor consume energy can take great comfort in Core CPI holding firm near 2%.

Source: Bureau of Labor Statistics, NYMEX

Employment: May brought the largest one-month jump in unemployment since Feb 1986, as the jobless rate went from 5.0% to 5.5%, reaching its highest level since Oct 2004.

Source: Bureau of Labor Statistics

Housing: Home prices fell further with the S&P Case-Shiller index off -8.2% YTD through April.

Source: S&P

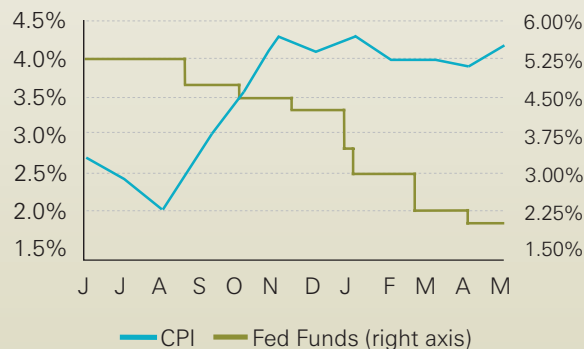
The U.S. Equity Market

After posting an impressive 7.18% return through the first two months of the quarter, the U.S. equity market suffered its worst monthly loss since a -10.03% sell-off in Sept 2002 with the Dow Jones Wilshire 5000SM retreating -8.14% in June. The -1.55% return in the 2nd quarter furthered a dismal -9.52% pullback during the first three months of the year to bring market losses to -10.92% through the midpoint of 2008; its worst first-half return since a -12.59% drop in the first half of 1974. Credit stress and deleveraging continued to weigh heavily on the Financial sector, which, combined with a surge in commodity prices to dizzying heights, dragged the overall stock market lower.

U.S. Equity	MTD (%)	QTD (%)	YTD (%)	1 Year (%)
Dow Jones Wilshire 5000 SM	-8.14	-1.55	-10.92	-12.53
S&P 500	-8.43	-2.73	-11.91	-13.12
Dow Jones Wilshire 4500	-7.50	2.19	-7.85	-11.41
U.S. Equity by Size/Style	MTD (%)	QTD (%)	YTD (%)	1 Year (%)
Dow Jones Wilshire 2500	-8.15	-1.53	-10.86	-12.30
Dow Jones Wilshire – Large Cap	-8.12	-1.76	-11.03	-11.78
Dow Jones Wilshire Large Growth	-6.53	2.65	-7.51	-4.90
Dow Jones Wilshire Large Value	-9.96	-6.59	-14.93	-18.84
Dow Jones Wilshire – Small Cap	-8.42	0.32	-9.35	-15.83
Dow Jones Wilshire Small Growth	-5.87	5.06	-7.57	-11.10
Dow Jones Wilshire Small Value	-11.13	-4.49	-11.17	-20.56
Dow Jones Wilshire Microcap	-7.38	-2.49	-14.71	-25.64

Small- and mid-capitalization stocks held up well during the quarter with the DJ Wilshire 4500 Index having a positive return of 2.19%, versus a -1.76% decline for the DJ Wilshire Large-Cap Index. Large value stocks suffered the heaviest losses due to their significant exposure to Financials; with the DJ Wilshire Large Value Index off -6.59%.

The relative quarterly performance of industries encapsulated a general economic trend that has been in place since last year; commodity-based stocks, benefiting from a sharp increase in commodity prices, performed best. Oil & Gas and Basic Materials led all groups with quarterly gains of 18.07% and 13.90%, respectively. Conversely, consumer stocks were hurt by the inflationary tax on consumers, driving the Consumer Goods industry down -8.65%. Only Financials did worse with a -15.43% return for the quarter, bringing their slide over the past year to -37.16%.



In an effort to combat a slowing U.S. economy and tight credit conditions, the Fed has been aggressive in lowering the Fed Funds rate from 5.25% to 2%. As the nearby chart demonstrates, CPI inflation has doubled from the 2% to 4% range since the Fed's easing cycle began last summer. The Fed is now in a "wait and see" posture as it examines whether the broader economic slowdown will alleviate inflationary pressures that are beginning to spread from headline CPI to consumer expectations or whether a more hawkish posture is needed.

The Non-U.S. **Equity Market**

Foreign equity markets had recouped over half of their first quarter losses before large declines in June resulted in an overall negative quarter for diversified portfolios. Returns in local currency were better in developed markets as the U.S. dollar strengthened, particularly versus the Yen. Similar to the U.S., most European markets suffered during the second quarter from an uncertain economic outlook and inflation concerns. The Japanese equity market, although down in June, ended the quarter in positive territory mainly from strong returns from the Industrials sector.

	USD (%)				Local Currency (%)			
	MTD	QTD	YTD	1 Year	MTD	QTD	YTD	1 Year
Non-U.S. Equity								
MSCI AC World ex US	-8.22	-1.12	-10.16	-6.64	-8.58	-0.28	-13.65	-15.01
MSCI EAFE	-8.18	-2.25	-10.96	-10.61	-8.89	-0.88	-15.70	-20.25
MSCI Europe	-8.70	-4.15	-12.41	-11.34	-9.80	-3.55	-17.00	-20.11
MSCI Pacific	-7.02	2.15	-7.62	-9.00	-6.90	5.38	-12.64	-20.47
MSCI Japan	-6.82	2.47	-5.53	-12.04	-6.43	9.13	-10.36	-24.50
MSCI EM (Emerging Markets)	-9.97	-0.86	-11.76	4.63	-9.88	-1.56	-12.39	1.40

The Fixed **Income Market**

The Federal Reserve's Open Market Committee cut the Fed Funds rate just once this quarter by 25 basis points. The U.S. yield curve was on a steady climb during the quarter before pulling back, still finishing higher than March-end. It is no surprise, then, that long duration bonds underperformed their shorter-term counterparts. On the decline for much of the quarter were corporate bond spreads. Although spreads started to push higher during the second half of June, the Lehman U.S. Credit outperformed the Aggregate Index and high yield bonds were up during the quarter.

U.S. Fixed Income	MTD (%)	QTD (%)	YTD (%)	1 Year (%)
Lehman U.S. Aggregate	-0.08	-1.02	1.13	7.12
Lehman 1-3 Year Govt.	0.24	-0.84	2.11	7.07
Lehman Long Term Treasury	1.71	-2.22	1.66	12.65
Lehman U.S. Credit	-0.53	-0.90	-0.48	3.81
Lehman U.S. Corporate High Yield	-2.80	1.76	-1.31	-2.26
Lehman U.S. TIPS	1.53	-0.28	4.88	15.09
Non-US Fixed Income	MTD (%)	QTD (%)	YTD (%)	1 Year (%)
Lehman Global Aggregate	0.09	-2.91	3.53	12.90
Lehman Global Aggregate (Hedged)	-0.32	-1.77	0.08	4.96
Lehman Non-U.S. Govt.	0.25	-4.68	5.20	17.48
Lehman Non-U.S. Govt. (Hedged)	-0.30	-2.29	-0.19	4.53

The Real Estate & **Commodity Markets**

Real estate securities advanced during the first part of the quarter due to growing investor confidence that the worst of the global credit crises was over only to fall sharply by quarter-end due to rising oil prices, inflation fears and continued problems in the Financials sector. The clear winners from this otherwise desolate news are commodity investments. Almost every commodity experienced large price increase during the quarter – except copper, which was up but by a modest amount. The oil-heavy S&P GSCI Index was up a staggering 28.65% for the quarter and 75.98% over the past year.

Real Estate / Commodity	MTD (%)	QTD (%)	YTD (%)	1 Year (%)
Dow Jones Wilshire U.S. REI	-11.09	-5.41	-3.41	-15.42
Dow Jones Wilshire Non-U.S. REI	-11.32	-9.10	-15.36	-24.12
Dow Jones Wilshire Global RESI	-11.22	-7.52	-10.51	-20.54
Dow Jones AIG Commodity (DJ-AIG)	9.10	16.08	27.22	41.56
Goldman Sachs Commodity (GSCI)	9.22	28.65	41.42	75.98

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