Review *and* Outlook

Second Quarter 2011

Market Overview

After a strong start to the year, performance of the financial markets was muted in the second quarter following the reemergence of sovereign debt concerns in Europe and reports of disappointing U.S. economic data.

In Europe, Portugal and Greece each required financial aid packages in excess of $100 billion from their Eurozone neighbors in order to remain solvent. Meanwhile in the U.S., natural disasters including wild fires, floods and tornados helped to compound the effects of slower than anticipated job growth and economic activity.

In light of these headwinds, volatility spiked for risk oriented investments as short-term investors sold stocks and commodities in favor of bonds. The Dow Jones Industrial Average started the quarter off strong with a rally of nearly 4% in April, but the gain was quickly erased as the index declined 7% over the next six weeks. This losing streak was the longest for the Dow since October of 2002. Equities then whipsawed in the final week of the quarter with the Dow and S&P 500 each gaining more than 5%.

Including dividends, large cap stocks narrowly outperformed small and mid cap stocks in the second quarter as the S&P 500 gained 0.1% versus declines of 1.6% and 0.7% for small and mid cap respectively. Developed international stocks were the top performers this quarter as the EAFE index gained 1.8% including dividends. Emerging market stocks declined 1.1% on continued fears about rising food and energy costs.

Higher volatility also caused a sector leadership change during the second quarter. All ten sectors of the S&P 500 were positive in the first quarter led by strength in cyclical growth areas such as energy, industrials and materials. In contrast, the second quarter had only five sectors in positive territory which were led by more defensive sectors including healthcare (+7.3), utilities (+5.0) and consumer staples (+4.5).

Within Broadway portfolios, some top performing stocks for the quarter included: Nike Inc. +18.9%, Thermo Fisher Scientific +15.9%, Novartis AG +12.4%, Costco Wholesale Corp +10.8% and PPL Corp +10.0%.

Commodities also sold off in the second quarter following concerns that demand from China, India and Brazil – some of the largest consumers of commodities – may be waning as government officials attempt to slow economic growth to avoid overheating. The Dow Jones UBS Commodity Index, which measures a basket of 19 commodities, fell 6.7% in the second quarter after a 4.4% rise in the first three months of the year.

A large part of the decline in commodities was an 11% drop in the price of oil. After rising above $100 a barrel in the first quarter oil experienced single-day price drops of 8.6%, 5.5% and 4.6% during May and June. According to Bloomberg News, this was the worst performance for oil since 2008.

Gold prices also retreated briefly after reaching an all time high of $1,556.70/oz. on May 2nd to settle at $1,502.30/oz. The yellow metal rose 4.4% for the quarter in response to ongoing global economic concerns and is on pace to rise for an eleventh straight year.

Bond returns outpaced those of stocks and commodities for the quarter as Treasuries gained 2.4% and corporate bonds rose 1.9% as measured by the Bank of America corporate debt index. Despite paltry yields and expectations that interest rates will rise investors continued to pour money into bonds and bond funds this year. As of June 22, bond funds had received inflows of $63 billion compared to $8 billion of outflows for stock funds.

Economic Review

Sentiment about the economy swung from optimism about global expansion in the first quarter to concern over the extent of a soft patch in May. The combination of rising inflation and a high single-digit unemployment rate have begun to impede the expansion that started over two years ago.

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Retail sales declined for the first time this year in May as record commodity prices caused consumers to limit purchases. The Consumer Price Index rose again in May and is up 3.6% compared with a year ago. Record prices this year for wheat, corn, cotton and oil, which are essential elements in food, clothing and gasoline, have hit consumer pocket books hard. Even after the decline in commodities this quarter, the price of corn was up 78% versus a year ago and oil had risen 26% in the past year.

Consumer spending has also been hampered by a sustained high level of unemployment. The U.S. economy added a paltry 43,000 jobs in May and June combined, after averaging 150,000 jobs a month for the prior six months. The Labor Department reported the unemployment rate rose to 9.2% in June, up from 9.1% in May and registered its third monthly increase.

The Federal Reserve's dual mandate of achieving maximum employment and maintaining stable prices has proven to be an elusive target after the recession. In a public statement after their June meeting the Federal Open Market Committee remarked, "The economic recovery is continuing at a moderate pace, though somewhat more slowly than the Committee had expected" and Chairman Bernanke called the rate of job growth "frustratingly" slow.

Record amounts of stimulus including more than $2 trillion in quantitative easing and record low target lending rates since December 2008 have stoked inflation, but done little to spark job growth. With the most recent round of quantitative easing having ended on June 30th, the financial markets will be watching closely to see if the economy is stable enough to grow on its own without the crutch provided by government stimulus.

While several headwinds to economic growth remain, there are reasons to be positive about the second half of 2011. Effects from natural disasters in the U.S. and supply-chain disruptions from the Japanese earthquakes are subsiding. In addition, in late June we received encouraging data on the manufacturing sector as the ISM factory index unexpectedly rose to 55.3 from 53.5 the prior month (index values greater than 50 indicate expansion).

Lastly, there was positive news from the freight/shipping sector which is sometimes seen as a proxy for economic activity. FedEx Corp reported stronger than expected earnings from package volume growth. Their CEO, Fred Smith, projected expansion in the second half of the year and remarked, "The near-term softness in the economy will be temporary as fuel prices have retreated from their April highs and the Japanese economy recovers."

Portfolio Spotlight: Emerging Market Currency

Broadway's Investment Management Group is a strong believer that emerging market countries will continue to be a major driver of global economic expansion for years to come.

In addition to investing in emerging stock and bond markets, we believe emerging currency funds are an effective way to add exposure to these developing countries - with only one-third of the volatility of emerging market stocks.

Some positive attributes of investing in emerging currencies in a diversified portfolio include:

- A hedge against a decline in the value of the U.S. dollar.
- Portfolio diversification from low correlation to traditional developed market assets.
- Emerging currencies are often valued at a discount relative to their long-run purchasing power and are poised to appreciate as their economies mature.

Index	YTD	1 Year	3 Years
Dow Jones	8.6%	30.4%	6.1%
S&P 500 Index	6.0%	30.7%	3.3%
MSCI EAFE*	5.3%	31.0%	-1.23%

*EAFE = Europe, Australia, & Far East International Index

2 Year Treasury Bond Yield as of 6/30/11	0.46%
2 Year Muni Bond (AAA) Yield as of 6/30/11	0.43%

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