

Hedge Fund Market Commentary – August 2009

The market appears to know only one direction lately, confounding the efforts of commentators to sound interesting and informative. As Exhibit 1 below indicates, most market sectors generated strong returns in August. Emerging market equities were the exception, posting a slight loss due to a sharp sell-off on the last day of the month. Economic data continue to improve, and though revenues are down on weak consumer spending, cost-cutting has bolstered corporate profits.

Exhibit 1: 2009 Market Performance

Index	August	YTD 2009	FYTD*	Calendar 2008
Equity				
Dow Jones 5000	3.6%	16.7%	11.7%	-37.2%
S&P 500	3.6%	15.0%	11.5%	-37.0%
Russell 2000	2.9%	15.8%	12.8%	-33.8%
MSCI EAFE	5.5%	24.8%	15.1%	-43.1%
MSCI Emerging Mkts	-0.4%	50.5%	10.9%	-53.5%
DJ REIT	14.6%	10.0%	26.6%	-39.2%
S&P 500 Financials	13.0%	18.8%	23.0%	-56.6%
Fixed Income				
Barclays Aggregate	1.0%	4.6%	2.7%	5.2%
Barclays Treasuries	0.9%	-3.1%	1.3%	20.1%
Barclays TIPS	0.9%	7.2%	1.0%	-2.4%
Barclays High Yield	1.9%	41.0%	8.1%	-26.2%
Barclays Bank Loan	1.9%	43.7%	6.7%	-29.5%
AAA ABX (Subprime)	-3.6%	-25.9%	10.7%	-43.2%
Barclays Municipals	1.7%	10.1%	3.4%	-2.5%
3 mo.Libor	0.1%	7.2%	6.6%	3.1%
Alternative				
DJ UBS Commodity	2.6%	7.4%	2.6%	-35.7%
Hedge Funds				
HFRI Fund of Funds**	1.0%	7.9%	2.5%	-21.4%
HFRI Fund Weighted**	1.6%	14.1%	4.2%	-19.0%
CS/Tremont	2.4%	9.7%	2.4%	-19.1%

* Fiscal YTD from June 30, 2009

** Hedge Fund Research, Inc. ("HFR") is the source and owner of the HFR data contained or reflected in this report and all trademarks related thereto.

Hedge funds continue to benefit from the rising markets. The HFRI Fund Weighted Index earned an estimated 1.6% in August while the HFRI Fund-of-Funds Index returned 1.0%. For the calendar year-to-date, the HFRI Fund Weighted Index is up 14.1% and the HFRI Fund-of-Funds Index is up 7.9%. The more market neutral and lower equity orientation of fund-of-funds likely explains the lower HFRI Fund-of-Funds Index return for the calendar year.

Some of the best returns came from credit funds, which enjoyed another month of spread tightening and increasing activity in capital markets. Managers that underperformed included those with lower net exposures and those with a volatility tilt. Exhibit 2 shows the performance of different hedge fund strategies, as defined by HFRI and CS/Tremont. Global Macro, the darling strategy of 2008, lagged the indices again in August.

Exhibit 2: Hedge Fund Performance by Major Strategy Category

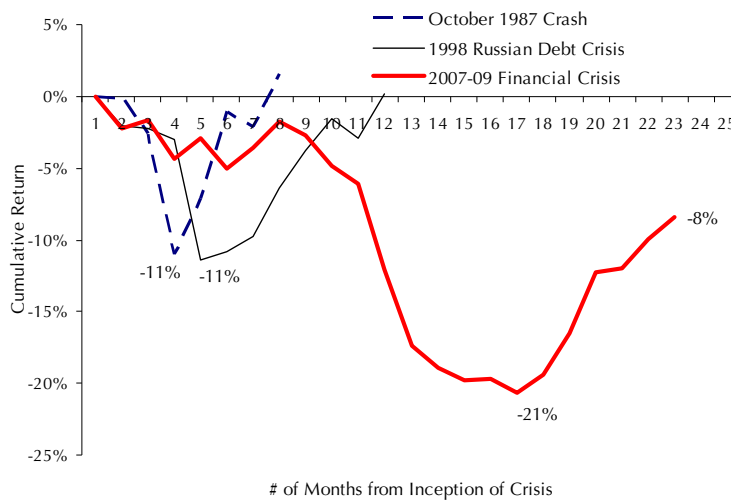
Strategy Indexes	August	YTD 2009	FYTD*	Calendar 2008
Arbitrage/Relative Value				
HFRI**	1.8%	17.8%	4.6%	-18.0%
CS/Tremont-Convert	3.4%	35.6%	9.4%	-31.6%
CS/Tremont-Fixed Income	2.4%	18.7%	6.1%	-28.8%
Event Driven				
HFRI	2.7%	16.1%	5.7%	-21.8%
CS/Tremont	2.5%	11.8%	4.8%	-17.7%
Equity Long/Short				
HFRI	1.8%	17.8%	5.1%	-26.7%
CS/Tremont	1.4%	13.0%	4.5%	-19.8%
Global Macro/CTA				
HFRI	0.9%	2.7%	1.5%	4.8%
CS/Tremont-Macro	0.9%	6.2%	2.7%	-4.6%
CS/Tremont-Managed Futures	0.8%	-7.1%	0.4%	18.3%
Multi-Strategy				
HFRI	2.8%	19.0%	5.7%	-20.3%
CS/Tremont	1.9%	17.8%	4.9%	-23.6%

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Exhibit 3 compares hedge fund performance for the current crisis with the prior two worst drawdown periods for hedge funds. The bad news is that this is by far the worse drawdown period for hedge funds. The good news is that if the markets don't reverse course hedge fund indices have a reasonable chance of fully recovering their November 2007 high water mark by the end of this year or the first quarter of 2010.

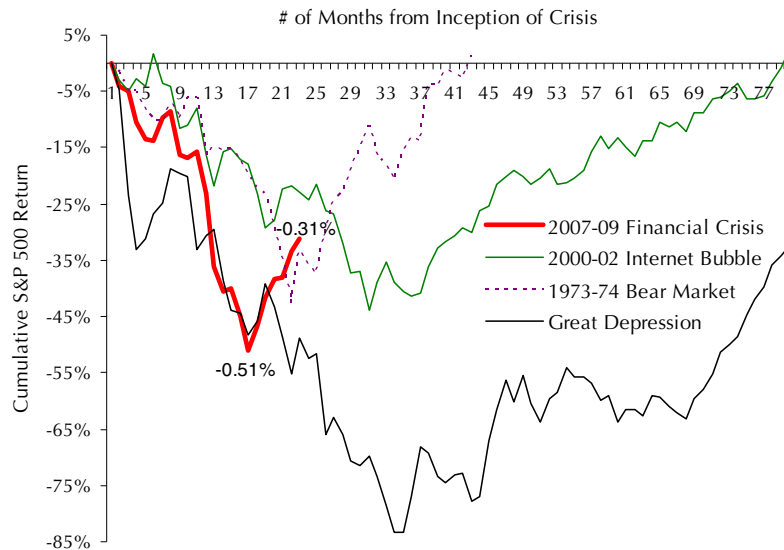
Exhibit 3: Comparison of Most Severe Hedge Fund Drawdowns



Stocks, by comparison, likely have a much longer way to go to fully recover their losses. Exhibit 4 compares the four worst stock market drawdowns, measured by the S&P 500 Index. After

falling 51%, and then recovering 41% from the March low, the S&P 500 Index is still down 31% from its November 2007 high water mark. Mathematically, it will require another 45% cumulative return from August 31st to fully recover. Our own forecast is that it may take as much as five years to reach that hurdle.

Exhibit 3: Comparison of Most Severe Stock Market Drawdowns



Eli Sokolov
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