

Hedge Fund Market Commentary – June 2010

Economic signals were generally negative in June and included disappointing growth numbers from China, weakness in domestic retail sales, and private job growth below expectations. Collectively, the news raised new concerns about the prospects for recovery and pushed large capitalization U.S. stocks down 5% and small-cap stocks down almost 8%. Non-U.S. developed market stocks fared better, losing only 1%, as investors provided support to European markets which had been disproportionately affected on sovereign debt concerns. European financials, which had lost 22% through May, fell less than 1% in June. High yield spreads widened slightly, though total returns were positive on falling Treasury yields and coupon income. Floating rate high yield bank loans, which are much less sensitive to interest rates than high yield bonds, lost only 50 basis points.

Exhibit 1: 2010 Market Performance

Index	June	YTD 2010	FYTD*	Calendar 2009	Calendar 2008
Equity					
Dow Jones 5000	-5.5%	-5.6%	16.2%	28.6%	-37.2%
S&P 500	-5.2%	-6.7%	14.4%	26.5%	-37.0%
Russell 2000	-7.8%	-1.9%	21.5%	27.2%	-33.8%
MSCI EAFE	-1.0%	-12.9%	6.4%	32.5%	-43.1%
MSCI Emerging Mkts	-0.7%	-6.1%	23.4%	78.3%	-53.5%
DJ REIT	-5.4%	5.3%	55.7%	28.5%	-39.2%
S&P 500 Financials	-5.9%	-3.7%	16.9%	17.2%	-56.6%
Fixed Income					
Barclays Aggregate	1.6%	5.3%	9.5%	5.9%	5.2%
Barclays Treasuries	1.9%	5.9%	6.7%	-3.6%	20.1%
Barclays TIPS	1.4%	4.4%	9.5%	11.4%	-2.4%
Barclays High Yield	1.2%	4.5%	26.8%	58.2%	-26.2%
Barclays Bank Loan	-0.5%	2.7%	17.3%	53.8%	-29.5%
AAA ABX (Subprime)	0.3%	16.7%	60.8%	-7.8%	-43.2%
Barclays Municipals	0.1%	3.3%	9.6%	12.9%	-2.5%
3 mo.Libor	0.0%	0.2%	0.3%	0.7%	3.1%
Alternative					
DJ UBS Commodity	0.3%	-9.6%	2.7%	18.9%	-35.7%
Hedge Funds					
HFRI Fund of Funds**	-1.1%	-1.4%	4.5%	11.5%	-21.4%
HFRI Fund Weighted**	-0.8%	-0.2%	9.3%	20.0%	-19.0%
Dow Jones Credit Suisse	-0.9%	0.6%	11.3%	18.6%	-19.1%

* Fiscal YTD from June 30, 2009

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Hedge funds fell again in May, declining -0.9% according to the Dow Jones Credit Suisse ("DJ/CS") Index. Funds of funds lost -1.1% according to early estimates from HFRI. A breakdown of hedge fund performance by strategy is shown in Exhibit 2.

Equity long/short and event driven funds were the worst performers, down -2.3% and -2.0% respectively, according to DJ/CS. HFRI, which samples a broader universe of hedge funds and gives greater weight to smaller hedge funds, reported similar results. Equity long/short funds, which on average maintain a net long bias, once again were forced to swim upstream against falling share prices. Event driven funds were primarily affected by losses in credit-oriented funds, with risk arbitrage funds slightly positive. Distressed funds were down -1.5% amid credit markets which witnessed both volatility and unfavorable disparity, with lower rated debt under-performing

higher rated debt. For many distressed funds, long portfolios are tilted toward junk-rated debt which is subject to forced selling by traditional bond investors, while the short portfolios are more oriented toward investment-grade credits and credit indices, which outperformed for the month.

Exhibit 2: Hedge Fund Performance by Major Strategy Category

Strategy Indexes	June	YTD 2010	FYTD*	Calendar 2009	Calendar 2008
Arbitrage/Relative Value					
HFRI**	0.4%	3.7%	15.7%	25.8%	-18.0%
Dow Jones CS-Convert	0.0%	2.6%	22.0%	47.3%	-31.6%
Dow Jones CS-Fixed Income	0.9%	5.5%	20.2%	27.4%	-28.8%
Event Driven					
HFRI	-1.1%	2.4%	16.5%	25.0%	-21.8%
Dow Jones Credit Suisse	-2.0%	1.4%	14.5%	20.4%	-17.7%
Equity Long/Short					
HFRI	-1.5%	-1.6%	9.4%	24.6%	-26.7%
Dow Jones Credit Suisse	-2.3%	-3.4%	6.6%	19.5%	-19.8%
Global Macro/CTA					
HFRI	-0.2%	-1.3%	1.6%	4.3%	4.8%
Dow Jones CS-Macro	0.5%	4.2%	12.4%	11.6%	-4.6%
Dow Jones CS-Managed Futures	0.5%	0.4%	1.3%	-6.6%	18.3%
Multi-Strategy					
HFRI	-0.6%	4.0%	15.6%	24.6%	-20.3%
Dow Jones Credit Suisse	-0.8%	0.5%	11.6%	24.6%	-23.6%

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June closes the fiscal year for most endowments and public pension systems. Early indications are that most institutions will report returns in the 10% to 14% range. Unlike last year (fiscal 2009) when traditional equity oriented portfolios experienced losses of 20% or more, these portfolios are likely to be the better performers in the just completed 2010 fiscal year, as public equities, with the exception of EAFE stocks, performed well. Viewed as a substitute for equities, larger absolute return allocations generally helped limit losses last year, but were somewhat dilutive in the 2010 fiscal year. However, hedge funds saw a wide dispersion in returns and some portfolios will benefit from strong hedge fund selection that may boost overall portfolio returns to the top of the range.

Eli Sokolov
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