



ATLANTIC TRUST

PRIVATE WEALTH MANAGEMENT

Economic and Investment Overview
Fourth Quarter 2011

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Economy

- Global growth is under pressure
- Recession in Europe, slow growth in U.S.
- Emerging economies slowing, but strong relative to developed economies
- Budget politics in U.S. and Europe will impact consumer and business confidence

Equities

- S&P 500 down 13.9% in Q3; Europe and emerging markets were even worse*
- U.S. equities inexpensive, but earnings slowdown likely
- European stocks struggle with major macro issues: Too much sovereign debt and no economic growth
- Emerging market stocks cheap, plus monetary policy to turn more supportive in many countries

* Source: Bloomberg L.P., as of 9/30/11.

Past performance is not a guarantee of future results.

Bonds

- Q3: Strong returns for high-quality U.S. fixed income
- Safe haven effect and weaker economic news were the catalysts
- Fed's "Operation Twist" flattened the yield curve
- Credit spreads widened in Q3 as recession risks rose

Asset Allocation Themes

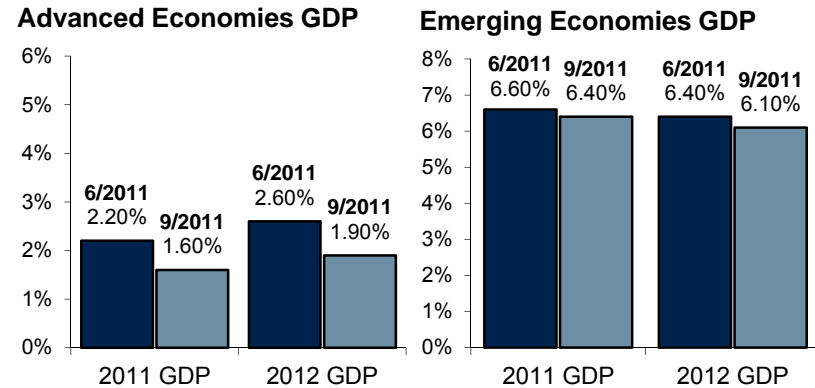
- U.S. Equities: **Large-cap** stocks represent the best quality and value
- **Minimize eurozone** exposure in favor of U.S. and emerging markets
- **Enhanced yield** strategies attractive after Q3 selloff: EM and senior bank debt, energy MLPs and diversified equity income
- **Hedge funds:** Directional funds suffered in Q3 from high correlations; overweight non-directional strategies

“The global economy is in a dangerous new phase.”*

- The outlook for global economic growth has dimmed in recent weeks. Forecasts for the rest of this year and 2012 have been downgraded across the globe.
- There are strong recession signals emitting from Europe. The sovereign debt crisis has put pressure on the European banking system and crushed consumer and business confidence. Meanwhile, fiscal and monetary policies in Europe remain restrictive.
- Activity in the U.S. has also lagged. Rising pessimism by businesses and consumers has caused the economy to hit stall speed. It is our best estimate that recession will be avoided, but slow growth is the best-case scenario for well into 2012.
- Economic prospects in emerging countries have been dented by lower exports to the stagnant developed economies. Furthermore, China’s tight monetary policy has slowed domestic activity in that bellwether economy. Nevertheless, the *relative* growth advantage for the emerging economies has actually widened.

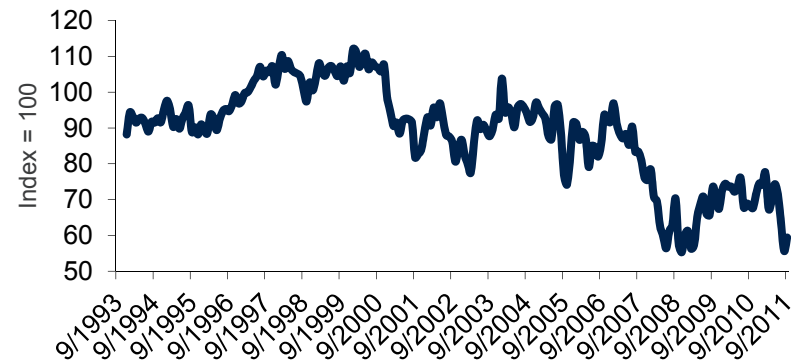
* International Monetary Fund's *World Economic Outlook*, 9/11

Growth Forecasts Revised Down



Source: International Monetary Fund, as of 09/11

Consumers Are Depressed and Worried

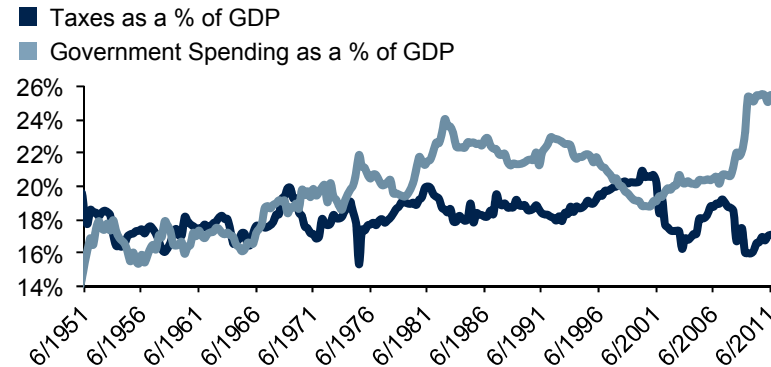


Source: University of Michigan, Consumer Sentiment Survey, as of 09/30/11

Political discord hampering fiscal and monetary policies

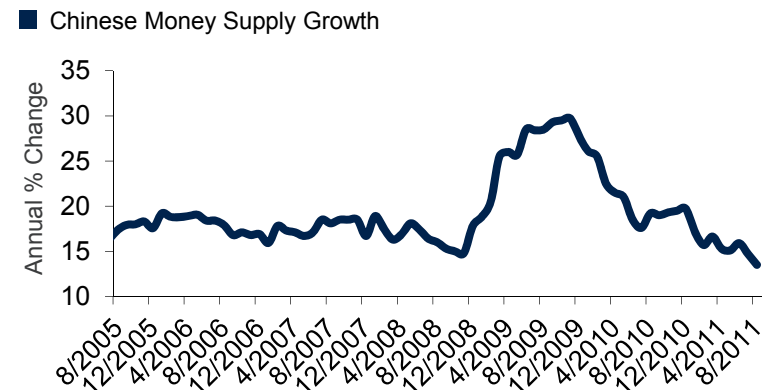
- The S&P downgrade of U.S. Treasury debt put an exclamation point on the issue of policymakers' inability to solve fiscal and economic issues. At the moment, there is no bipartisan path to an agreement on either stimulating the economy or producing material long-term deficit reduction.
- Europe's crisis is exacerbated by two factors: the bureaucratic decision-making process of the European Union (EU) and a central bank that is resistant to pro-growth policies. The need for 17 separate countries to agree on moves to tame sovereign debt contagion most likely means that the crisis atmosphere will persist for at least the rest of this year. Meanwhile, the European Central Bank (ECB) is behind the curve in setting monetary policy for a recession and in easing liquidity issues related to the banking system.
- Policy actions in China may hold the most promise. China has imposed restrictive monetary and regulatory policies to slow the economy and tame rising inflation. Those policies have taken hold, and with the recent decline in commodity prices, the authorities may have the flexibility to ease policy and make sure that a soft landing does not turn into a hard landing. This policy change would be welcome for global equity markets.

Massive Gap Between Taxes and Spending



Source: Ned Davis Research, as of 6/30/11

Chinese Economy Cooling Down

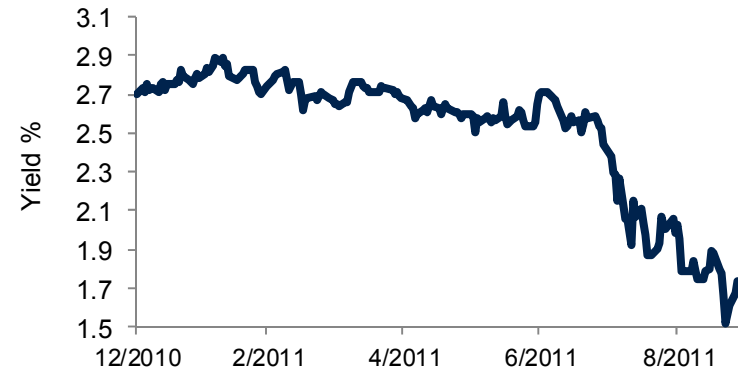


Source: Bloomberg L.P., as of 8/31/11

Operation Twist

- The Fed announced a plan to further ease monetary conditions in the face of recent economic weakness. Dubbed “Operation Twist,” a reference to similar policy moves used by the Fed and the U.S. Treasury in the early 1960s, the Fed will swap \$400 billion of short-dated Treasuries for an equal amount of longer-dated bonds. If all goes well, the Treasury yield curve will flatten and holders of long Treasury bonds will be enticed to look for other investment opportunities, like commercial loans or riskier categories of debt.
- The market had been anticipating this type of action from the Fed and had already flattened the yield curve by nearly 100 basis points leading up to the Fed’s September 21 meeting.
- Twist could be very beneficial to the Treasury, as it rolls maturing bills and notes into longer securities, but the benefits to corporate borrowers have been offset by wider yield spreads over Treasuries. The net result is more expensive cost of credit for non-government borrowers. This outcome blunts the impact of “Operation Twist” and may eventually lead to more aggressive monetary accommodation.

A Flatter Yield Curve : 10-year Minus 2-year Treasury



High-yield Corporate Bonds: Rising Borrowing Costs



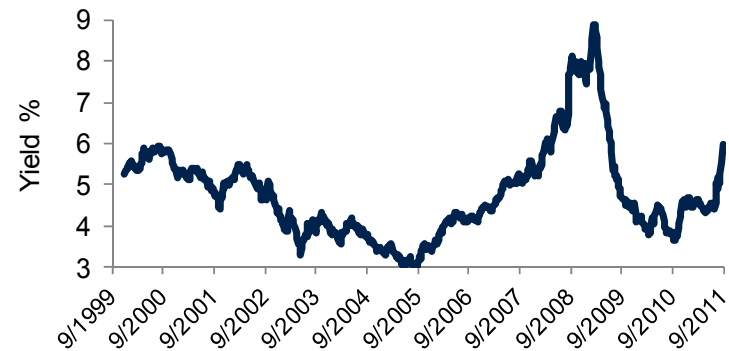
Source for both charts: Bloomberg L.P., Barclays Capital, as of 09/11

European contagion

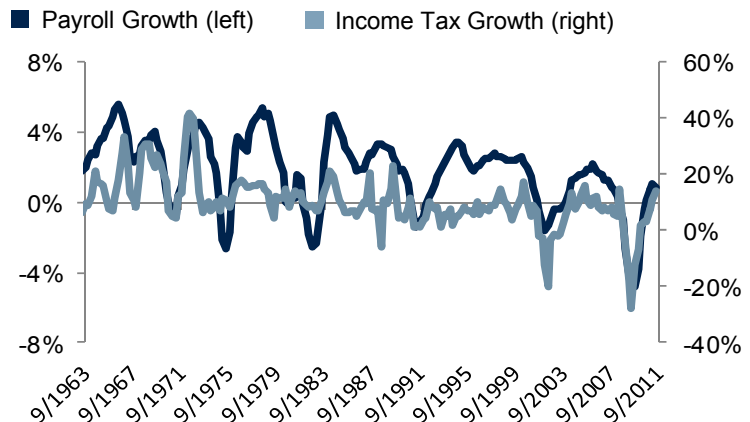
- The policy response out of Europe continues to be excruciatingly slow and ineffective. While members of the EU vote on expanding the size of the European Financial Stability Facility (EFSF), bank lending has become more strained and has infected most areas of the capital markets and the real economy.*
- Access to credit for European financial borrowers is now the most expensive it has been since the 2008/2009 crisis and will likely force painful deleveraging in the coming quarters and years.
- Several global central banks have stepped in to provide dollar funding to European financial borrowers who have found few buyers for their commercial paper in recent weeks.
- Correlations for many risky segments of the credit markets have risen due, in part, to the rising probability of euro fallout. Domestic high-yield credit spreads ballooned in August and emerging market currencies tumbled in September. Municipal bonds have been relatively safe, but they could come under renewed pressure if domestic unemployment edges higher in the coming months.

* EFSF has a mandate to safeguard financial stability in the Euro zone.

Higher Cost of Credit in Europe
Euro Financial Corporate Bond Yield



Job Growth Key for States' Fiscal Health

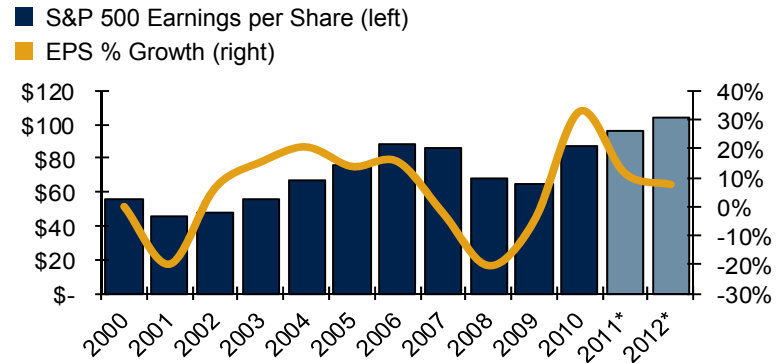


Source : Bureau of Labor Statistics, Bureau of Economic Analysis, Barclays Capital , 9/11

Corporate fundamentals...what's next?

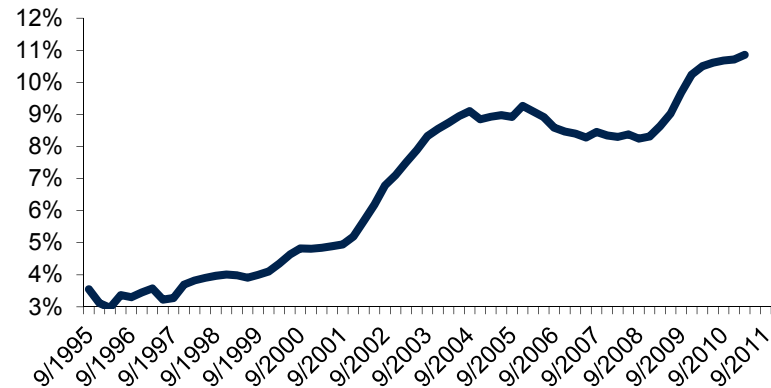
- The corporate earnings recovery remains significant as S&P 500 profits are on track to meet analysts' expectations, and are likely to exceed peak earnings of 2006 by the end of this year.
- Despite the sharp rebound in corporate profits, the economy has not performed as many economists forecast, with GDP growing less than 1% at an annualized rate for the first half of 2011. Lingering unemployment, excessive cash on corporate balance sheets and lack of policy direction may be structural headwinds to meaningful corporate profit growth going forward.
- Conversely, corporate fundamentals are in better position now than they were headed into peak earnings of 2006. If a global slowdown were to occur, companies with strong balance sheets and operating leverage could become opportunistic and return capital to shareholders by way of stock repurchases, dividend increases, special dividends or through M&A. Similarly, if structural issues can be resolved and an economic slowdown is avoided, "healthy" companies would be in better position to grow profits meaningfully in any continued economic expansion.

Profit Expectations Still on the Rise



Source: Thomson Financial, as of 9/30/11. *Forecasted growth

Cash as a Percent of Total Corporate Assets

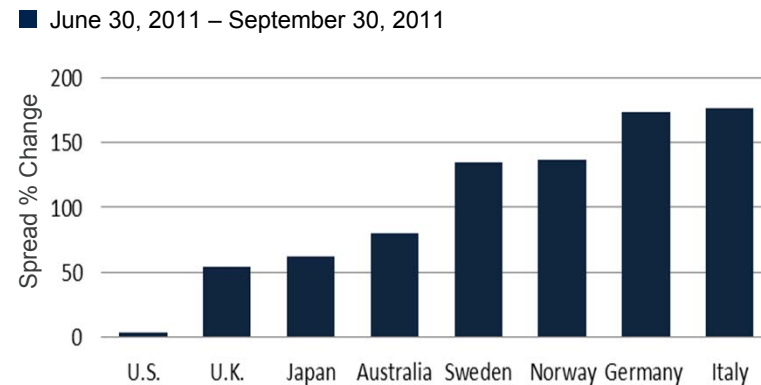


Source: Strategas, as of 6/30/11

The situation in Europe...unresolved

- Sharp downward revisions to the strength of recovery in several major economies, particularly in the developed world, has increased volatility and driven down the prices of risky assets during the period.
- The market's concerns about growth were intensified by the belief that monetary and fiscal policies had only a limited chance of stimulating the global economy. Negative news about macroeconomic conditions were compounded by concerns about periphery-euro sovereign debt issues spreading from Greece, Ireland, Portugal, Italy and Spain to the perceived "safe havens" of Germany and France via the banking system.
- Over this period, world (except U.S.) equity prices declined by 19% on average, with larger falls, surprisingly in emerging market economies and slightly smaller falls in the developed markets. Large declines in prices of cyclically sensitive assets pulled down average prices.*

Rising Cost to Ensure Against Government Defaults Change in Credit Default Swap Yield Spreads



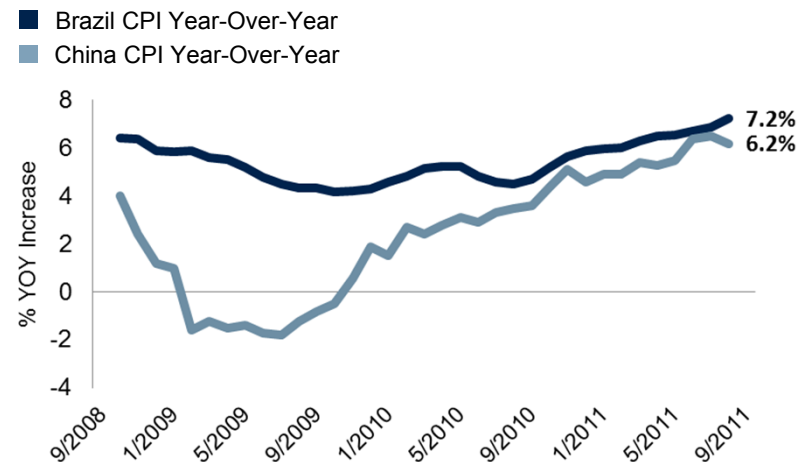
Source: Bloomberg L.P., as of 9/30/11

* Bloomberg L.P., as of 9/30/2011

Emerging markets tackle inflation and slower growth

- Emerging market economies have decelerated over the past several months, due in large part to:
 - Reduction in purchasing power, resulting from elevated agriculture commodity prices (inflation)
 - Lagged effects from monetary policy tightening, in place over the past several quarters (specifically salient in China and Brazil)
 - Weakening end markets in the developed world have hurt net exports at the margin
- Concerns surrounding inflation led emerging market central banks to take action. Some central banks raised interest rates during the period, including in China and India. The People's Bank of China further tightened monetary policy by broadening the scope of reserve requirements after inflation reached a three-year high of 6.5% in July. In contrast, the central bank of Brazil, despite inflationary concerns, *cut* policy rates in reaction to signs of slower growth.

Inflation Concerns: China and Brazil



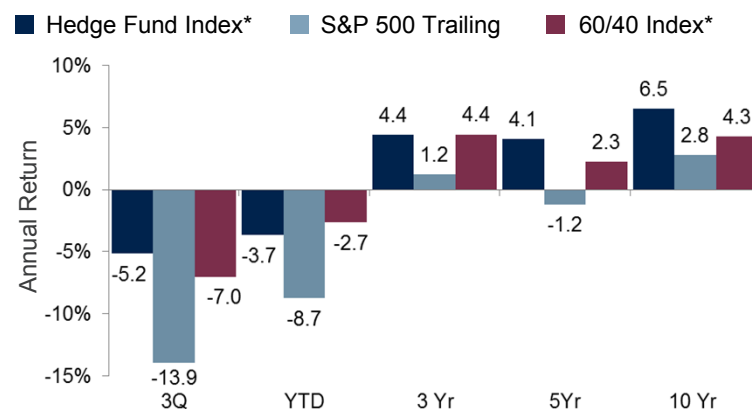
Source: Bloomberg L.P., 9/30/11

Navigating volatility with fewer drawdowns...

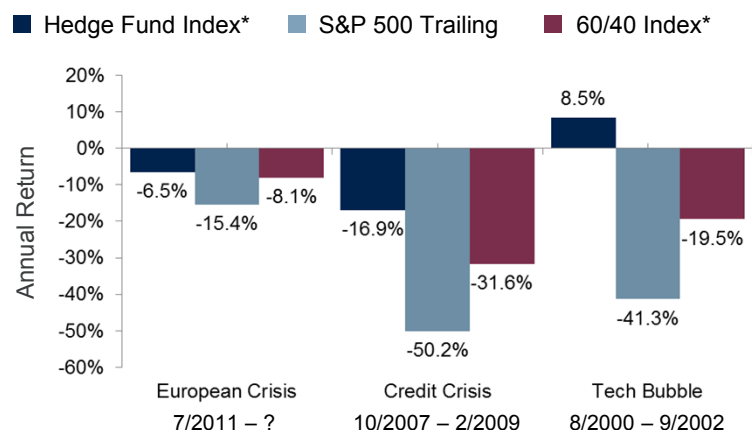
- For the third quarter, hedge funds returned an estimated -5.2% compared to -13.9% for the S&P 500 Index and -7% for a diversified 60/40 index.*
- Volatility and correlations were higher through the quarter across all asset classes—equities, credit, commodities and FX—as indiscriminate selling occurred.
- Financial and cyclical sectors were generally hit hard as analysts began revising earnings estimates downward to reflect a slowdown in global growth, and due to fiscal policy issues in the U.S. and Europe.
- Hedge funds navigated this volatile period by tactically managing risk and preventing massive drawdowns, which is the key reason this asset class has outperformed over the longer run.
- A “stress” period performance study illustrates hedge funds have continued to maintain a similar risk return profile. We continue to recommend having appropriate allocation to hedge funds in client portfolios, especially during times of distress.
- Managers have appropriately reduced portfolio exposure by raising cash and have become less optimistic on near-term prospects for global growth; however, most remain optimistic on valuations going forward.

* Hedge fund performance calculated using Dow Jones Credit Suisse Hedge Fund Index for monthly data. Intra month data is estimated using Dow Jones Credit Suisse Core Hedge Fund indices. Diversified 60/40 index consists of 60% allocation to S&P 500 Index and 40% allocation to Barclays U.S. Aggregate Index.

Historical Track Record



“Stress” Period Performance



Source for both charts:
Bloomberg L.P., as of 9/30/11