

2011

JUNE

ASSET ALLOCATION UPDATE

*From the Desk of Our Chief Investment Officer***David L. Donabedian**
Chief Investment Officer

Dave Donabedian is chief investment officer of Atlantic Trust, returning to the firm in 2009 after serving as chief investment officer for Ashbridge Investment Management, LLC, from 2006 to 2009. As a leading investment expert in our industry, Dave frequently appears on television networks, such as CNBC, and provides insights in publications, such as *Baron's*. Previously, from 1996 to 2006, Dave worked with Atlantic Trust as managing director and chief economist. Dave received a B.S. in economics and a B.A. with honors from The Wharton School at the University of Pennsylvania. He subsequently earned an M.B.A. from Columbia University Graduate School of Business.

Atlantic Trust's Asset Allocation Committee (AAC) met recently and decided to leave current asset allocation targets in place. However, there was a notable increase in caution regarding the financial markets outlook.

This sense of caution was motivated by two factors: first, an acknowledgement of how far the recovery in the price of risk assets has come in the past two years; and second, some less auspicious fundamental developments in recent weeks.

Recovery from the Depths

	Total Return 3/9/09–5/31/11
S&P 500 Index	106%
Russell 2000 Index (Small Cap)	151%
MSCI EAFE Index (Developed Country Int'l)	104%
MSCI Emerging Markets Index	143%
Dow Jones-UBS Commodity Index	59%
Barclays High Yield Bond Index	96%
Barclays U.S. Investment Grade Corporate Bond Index	35%

Source: Bloomberg, LP, as of 5/31/2011. For index descriptions, see page 4.

The factors that have driven equity prices higher since last summer's correction—easy money and ample liquidity (QE2, a strengthening economic expansion and a clear upward path for corporate earnings)—all feel a bit less robust now. Recent developments include:

- **Generally weaker economic reports in the U.S. and around the world.** The downshift to 1.8% GDP growth in the first quarter and subsequent reports point to a slowdown in the path of U.S. expansion. The Chinese economy continues to struggle with a sub-optimal mix of slowing growth and uncomfortably high inflation.
- **Deepening and spreading of the eurozone sovereign debt crisis.** The inability of Greece to achieve its fiscal targets, along with the increased burden of bailouts for Ireland and Portugal, have led to increased dissension between

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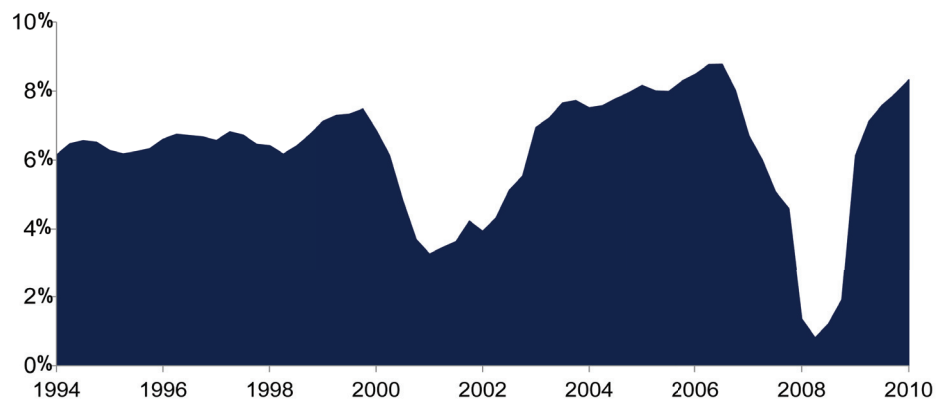
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the rich eurozone countries and the European Central Bank on the best way forward. There is increased talk of a Greek default or restructuring and further questions about the viability of current membership of the euro currency. Meanwhile, Spain, Italy and Belgium all face greater scrutiny in the months ahead, given significant deficits and potential funding issues.

- **“Don’t fight the Fed” has been the right investment strategy, but the QE2 policy is drawing to a close.** The focus going forward will likely be on how and when the various stages of unwinding and tightening begin. This does not mean that monetary policy will be restrictive, but the extent of liquidity support for markets from governmental institutions has peaked. Meanwhile, most other central banks in the world are in tightening mode.
- **Progress on a bipartisan federal deficit/debt reduction plan has lost momentum.** As a result, worries over passage of a debt ceiling extension and the theoretical “default” of the U.S. government will probably be an overhang for investor sentiment in the next two months.
- **First quarter profits were strong, but company guidance has become more cautious.** At the same time that CEO/CFO earnings guidance has become more conservative and the economy has lagged a bit, industry analysts continue to upwardly revise EPS estimates for the rest of this year and into 2012. Current forecasts call for 18% EPS growth in the second half of 2011 and 13.5% in 2012. As profit margins approach all-time highs, there is concern that these expectations are on the optimistic side and may require downward adjustment in the future.

Over the last year, we have recommended increasing allocation to hedged strategies, income-oriented investments and the more conservative large-cap end of the equity markets.

S&P 500 Operating Profit Margins



Source: Strategas, as of 12/31/2010

Atlantic Trust Recommendations

So, with no shortage of things to worry about, why not reduce our recommended exposure to equities, commodities, emerging markets and other, more volatile asset classes? First, it is the sense of the AAC that our existing allocations are already somewhat conservative. Over the last year, we have recommended increasing allocation to hedged strategies, income-oriented investments and the more conservative large-cap end of the equity markets.

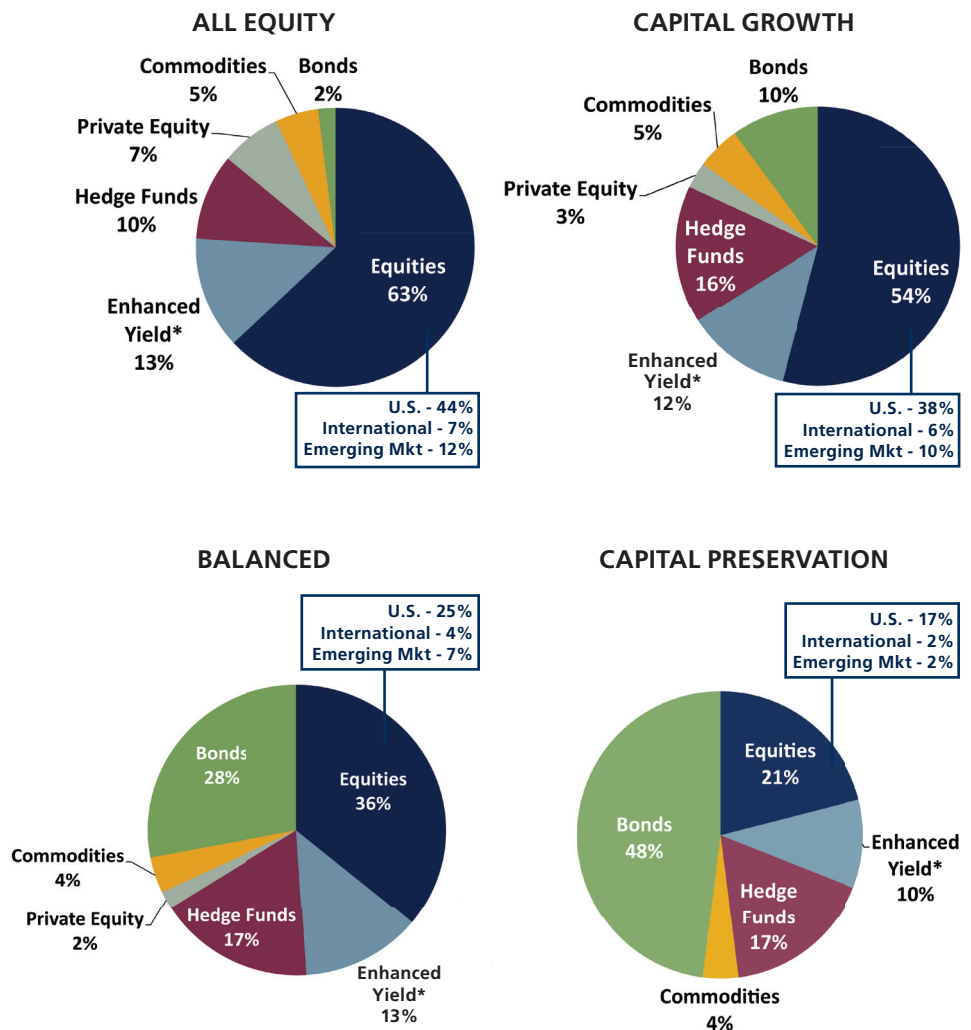
Our strongest recommendation is to rebalance portfolios where risk assets have run higher than target based on price performance. Furthermore, we believe it is an opportune time to raise hedge fund allocations up to recommended levels.

While the previously discussed issues create a more challenging environment, we expect the global economic recovery and cyclical bull market in equities to survive.

A trading range—featuring more volatility than direction—is a distinct possibility for the next few months. While the previously discussed issues create a more challenging environment, we expect the global economic recovery and cyclical bull market in equities to survive. Despite only a modest sell-off in May, investor sentiment has turned more cautious, which we view as positive. Earnings expectations seem a bit too rosy, but even a more subdued EPS growth rate leaves us in a reasonably-valued market. We are also struck by the lack of compelling competition for capital from investment grade fixed income and money markets. Yields remain very low, corporate and muni spreads have tightened and expected future returns are at the low end of historical ranges.

As always, the most important asset allocation discussion is between you and your relationship manager. While the AAC works hard to identify general opportunities for return enhancement and risk reduction, every client portfolio is managed to address customized objectives. Therefore, some of the recommendations referenced above, and the asset allocation models illustrated below, may not be appropriate for your specific situation, so please speak with your relationship manager.

Asset Allocation Committee Model Recommendations



*Enhanced yield includes Master Limited Partnerships (MLPs), equity income, emerging market debt and floating rate senior debt. Source: Atlantic Trust, 05/2011

Index descriptions for "Recovery From the Depths" table (page 1): The S&P 500 Index, a market value weighted index, consists of 500 U.S. stocks chosen for market size, liquidity and industry group representation. The Russell 2000 Index measures the performance of the 2,000 smallest companies in the Russell 3000 index. The MSCI EAFE Index is a free float-adjusted market capitalization index designed to developed market equity performance, excluding the U.S. and Canada. The MSCI Emerging Markets Index is a free float-adjusted market capitalization index that is designed to measure equity market performance in the global emerging markets. The Dow Jones-UBS Commodity Index is composed of commodities traded on U.S. exchanges, with the exception of aluminum, nickel and zinc, which trade on the London Metal Exchange (LME). The Barclays Capital High Yield Index includes publicly issued U.S. dollar denominated, noninvestment grade, fixed-rate, taxable corporate bonds that have a remaining maturity of at least one year. The Barclays Capital U.S. Investment Grade Bond Index measures the performance of the investment grade corporate bond market.

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