VERITY Investments, Inc.

# Market Commentary and Outlook

MAR. 31, 2011

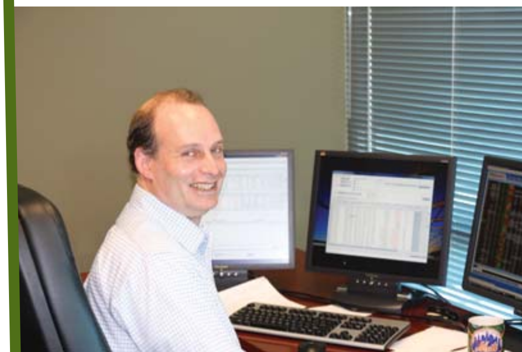
CORE ALLOCATION

INDEPENDENT ADVICE ACTIVE MANAGEMENT

**Target Allocation by Asset Class / Strategy**

- 56.5% Equities - Domestic & Foreign
- 16.5% Gold, Energy & Commodity Related
- 5.0% Merger Arbitrage
- 8.5% Equities - Short (Leveraged 200%)
- 4.0% Bonds
- 7.5% Bonds - Short
- 2.0% Cash

Q1 of 2011 was characterized by several notable market events. The S&P 500 traded at double the price established at the bear market bottom in March 2009; gold made new all time highs over $1400/ounce; and crude oil once again pushed above $100/barrel, more than triple the $32 price at which it traded barely two years ago.



**Brian Kurtzer**
*Portfolio Manager*

By the end of the quarter however, equally stunning world events appeared to be the prime drivers of most markets, resulting in the strong likelihood that prognostications for immediate or longer time frames will be subject to reevaluation at a moment's notice as dictated by the current news cycle. In other words, in an environment where the true fundamentals underlying specific markets had already in many instances taken a back seat to global and regional macro concerns, Q1 2011 served to exacerbate this trend. In this context it is easy to understand the market's wild sentiment swings from extreme optimism to extreme pessimism and back again over short periods of time.

While many market participants were probably feeling a growing lack of clarity as the quarter progressed, we welcomed the opportunity to tactically enhance some of the positions related to our stronger investing convictions at attractive prices. In the process, we were able to better position ourselves for the quarters and years ahead.

As 2011 began,there seemed to be a consensus among the "financial talking heads" that the appropriate stance for the year was to invest in U.S. large cap stocks while paring back allocations to emerging markets. There was also a fairly strong chorus urging that it was finally time to recognize that gold was in dangerous bubble territory.

For much of the quarter, U.S. large cap did in fact outperform both small cap and emerging markets. While not necessarily bearish on U.S. stocks, we continue to believe the better long term opportunities are in emerging markets, so we used the relative weakness to increase our positions, notably adding an allocation to Russia, as well. We also continue to overweight small cap stocks, believing they will do well if the bull market continues, and from the quarter's mid-March lows the small cap Russell 2000 outperformed the larger cap S&P 500, with 8.7% gains compared to gains of 6.2%. Notably, emerging markets in general outperformed both indexes over this period.

Our allocations to oil exporting emerging market counties such as Russia, Columbia and Mexico have no doubt benefited from the explosive rise in oil prises, but these countries also have other fundamental merits. While there have been dramatic gains in all energy related investments during the first quarter, the most significant driver of the oil market appears to be the continuing events in the Middle East, the resolution of which will likely remain unknown for quite some time.

Our targeted commodity related investments in grains and agricultural companies appear to have a very strong underlying bullish trend. After a sharp mid-quarter decline, grains recovered aggressively over the last 2 weeks following a bullish USDA report. All of our investments in the sector ultimately realized gains for the quarter, with our most heavily weighted ag company, Archer Daniels Midland, up 20%.

Gold also initially proved the "experts" correct; however, the decline lasted only for the first three weeks of January. The subsequent rally saw our gold ETF (GLD) close out the quarter with slight gains after a 9.4% rise from January's low. We continue to believe that our gold holdings provide important portfolio insurance and represent a sound investment in an asset that acts like one of the only stable currencies in the world, rather than as the beneficiary of an investment bubble. For now, most of the central banks in the world appear to believe in that assessment as well, which we take as strong confirmation that this powerful bull market may have further to go.

A short position that essentially is targeted at the developed countries in Europe, as well as Japan, continues to be maintained, although at a reduced weighting from prior quarters. We believe this position has and will remain an effective hedge, and will work to diminish portfolio volatility. It is hard to look at the devastating events in Japan as anything other than a monumental human tragedy. But the economic reality is that a country that had already been on a path toward the most severe sovereign debt crisis in the world will now be challenged to a greater degree. Only in developed Europe could the problem potentially be worse.

Finally, as the debate over U.S. government spending and debt creation heats up, there is an ever present risk that the trend of rising long term U.S. Treasury yields which began last August could accelerate severely, particularly if the Fed's quantitative easing program truly ends in June. Regardless, over the course of time we expect significantly higher long term rates and will continue to maintain a position that profits when those rates rise, essentially the equivalent of shorting U.S. Treasuries. We anticipate adding to the positon during intermittent shorter term periods of strength in the Treasury bond market. This stance does not mean that we will completely refrain from investing in yield based securities. For example, through the Aberdeen Asia Pacific Income Fund (first quarter total return of 4.22%), we continue to seek exposure to the bonds of countries, such as Australia, which we believe are behaving in a fiscally prudent manner.

As we move further into 2011, it is likely that we will face increasingly volatile markets. However, we believe that by continuing to seize opportunity in a disciplined manner within our targeted investments, we may be able to use market turmoil to our great advantage. There will be quarters where we trail various market indexes, but we believe this approach will allow us to continue to create more reliable growth over time.