



VERITY
Asset Management

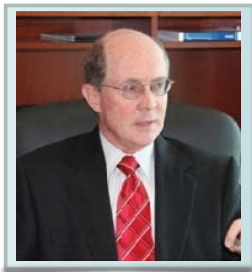
Market Commentary and Outlook

Core Allocation

June 30, 2012

INDEPENDENT ADVICE

ACTIVE MANAGEMENT



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I'm sure you're tired of hearing it from every direction, and you've heard it repeatedly from us: *As we scan the global economic landscape, it's tough out there – very tough – and extraordinarily dangerous.* So, rather than belabor the obvious, let's devote this issue to peering under the hood of the investment process we're employing to build tangible value as the world works its way through these conditions.

Target Allocation by Asset Class / Strategy

54.0%	Equities - Domestic & Foreign
23.0%	Gold, Energy & Commodity Related
5.0%	Merger Arbitrage
6.5%	Equities - Short (Leveraged 200%)
6.0%	Bonds - Foreign
5.5%	Cash

As noted in our fourth quarter, 2011 Market Commentary, "... periods of high volatility create opportunities to expand exposure to investment themes ... at attractive valuations." Some of the positions we expanded during the turmoil of the fall and winter bore fruit during second quarter, as the Core portfolio was resilient, holding on to virtually its entire first quarter gain despite a 3% decline in the S&P 500. Let's look a little more closely at some of the components of our process:

A) Identify investment themes with strong fundamental underpinnings.

Particularly in this type environment, it is crucial to identify segments of the world markets which appear positioned to weather severe market weakness and recover to new heights over an intermediate to longer time horizon. There will be shorter term trading opportunities - we very recently added a 3% position in Crude Oil as oil prices fell into the upper \$70's, with a goal of selling at a profit over a short time frame – but more enduring fundamentals underlie most of the positions in the portfolio.

Price, underlying economic and/or market trends, and various other factors are critical components of the selection process, and we could elaborate extensively if space permitted, but briefly, our primary themes include:

- Biotechnology – creative, sometimes revolutionary development on the frontiers of medical science.
- Emerging markets – in particular, countries with sound sovereign balance sheets and positive demographic momentum (the opposite of most of the developed world).
- Grains – world population is growing as arable land is being depleted.
- Agricultural stocks – attractive valuations available in a core economic sector.
- Water Resources – the most fundamental of resources faces expanding populations and growing challenges to supply.
- Crippling structural challenges in Europe & Japan – shorting those markets provides a hedge against broad market risk.
- Gold and gold mining shares – among other considerations, insurance against global currency debasement.

B) Diversify purposefully and effectively by selecting assets which do not closely correlate.

Despite our care, we will not always be "right" in our selection of themes. And even when we are, it may not look or feel that way during severe price corrections. So, to reduce both portfolio volatility and overall risk, we try to avoid selecting investments which closely correlate (by consistently moving in the same direction at the same time). Two *perfectly* correlated assets would have a correlation of 1.00. Assets with a correlation of 0.70 or greater could thus be considered *highly* correlated, while assets with a correlation close to 0.00 would be considered to be *uncorrelated*, or completely independent of one another in their movements. (*Negatively* correlated assets tend to move in opposite directions from one another.)

Correlations among the various positions in the Core portfolio based upon the past 3 years are quite remarkably low. There are 15 primary holdings in the portfolio. Water is highly correlated with China and Mexico; Water is also highly correlated with Biotech. Two of the Agriculture stocks (Mosaic and Potash) are highly correlated with one another, and the two Gold-related positions are also highly correlated. Otherwise, there are no correlations greater than 0.70 among any of the primary holdings, as is illustrated in the chart below.

Investment Name	1	2	3	4	5	6	7	8	9	10	11	12	13	14	15
iShares Nasdaq Biotechnology	1	0.79	0.23	0.29	-0.72	0.54	0.58	0.10	0.30	0.52	0.42	0.69	0.29	0.22	0.47
PowerShares Water Resources	0.79	1	0.42	0.41	-0.83	0.44	0.75	0.18	0.38	0.51	0.53	0.86	0.39	0.29	0.69
iPath DJ-UBS Grains TR Sub-Idx ETN	0.23	0.42	1	0.37	-0.53	0.46	0.48	0.39	0.25	0.38	0.65	0.55	0.33	0.50	0.44
U.S. Global Investors Gold and Prec Mtls	0.29	0.41	0.37	1	-0.40	0.53	0.54	0.85	0.27	0.41	0.39	0.49	0.30	0.38	0.42
ProFunds UltraShort Intl Inv	-0.72	-0.83	-0.53	-0.40	1	-0.56	-0.75	-0.26	-0.47	-0.64	-0.65	-0.88	-0.52	-0.43	-0.67
Aberdeen Asia-Pacific Income Fund	0.54	0.44	0.46	0.53	-0.56	1	0.53	0.41	0.48	0.57	0.41	0.52	0.28	0.41	0.41
iShares FTSE China 25 Index Fund	0.58	0.75	0.48	0.54	-0.75	0.53	1	0.42	0.23	0.60	0.60	0.80	0.47	0.40	0.68
SPDR Gold Shares	0.10	0.18	0.39	0.85	-0.26	0.41	0.42	1	0.09	0.30	0.33	0.37	0.20	0.33	0.25
Arbitrage R	0.30	0.38	0.25	0.27	-0.47	0.48	0.23	0.09	1	0.36	0.29	0.35	0.26	0.36	0.49
Global X FTSE Colombia 20 ETF	0.52	0.51	0.38	0.41	-0.64	0.57	0.60	0.30	0.36	1	0.51	0.50	0.41	0.41	0.31
Mosaic Co	0.42	0.53	0.65	0.39	-0.65	0.41	0.60	0.33	0.29	0.51	1	0.66	0.59	0.81	0.30
iShares MSCI Mexico Investable Mkt Idx	0.69	0.86	0.55	0.49	-0.88	0.52	0.80	0.37	0.35	0.50	0.66	1	0.33	0.41	0.63
Archer-Daniels Midland Company	0.29	0.39	0.33	0.30	-0.52	0.28	0.47	0.20	0.26	0.41	0.59	0.33	1	0.45	0.42
Potash Corporation of Saskatchewan, Inc.	0.22	0.29	0.50	0.38	-0.43	0.41	0.40	0.33	0.36	0.41	0.81	0.41	0.45	1	0.16
iPath S&P GSCI Crude Oil TR Index ETN	0.47	0.69	0.44	0.42	-0.67	0.41	0.68	0.25	0.49	0.31	0.30	0.63	0.42	0.16	1

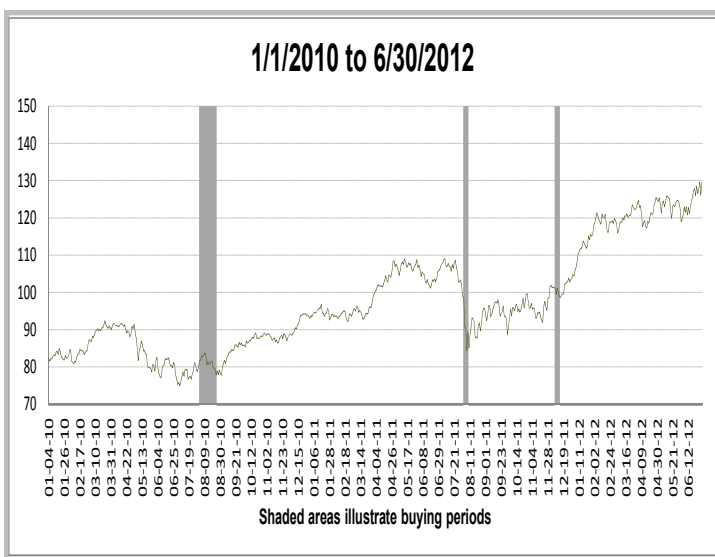
This chart was constructed using data from Morningstar Advisor Workstation SM Office Edition.

Historical information of this nature cannot be used blindly. Correlation patterns change over time, and correlations tend to become very high during periods of panic, as demonstrated during the fall of 2008. However, consideration for the tendency of different assets to behave with relative independence over time can add significantly to portfolio stability and the probability of successful results.

C) Add value by shopping for additional shares when the market has punished them and they are “on sale”.

That’s so easy to say, and so easy to identify in retrospect by the armchair quarterbacks out there. But day by day, in the heat of the process, it takes both skill and discipline. Even then, there will be mistakes, such as waiting too long for a big “sale” that never comes, or getting a “great” price on something that later proves to be simply an awful investment.

The chart below illustrates the concept. So long as our ongoing assessment is favorable, we may seek to add shares during periods of weakness, regardless of the short term trend. There are no guarantees, but, over time, careful execution of this principle has the potential to add material value to your portfolio.



This chart was constructed using data from Yahoo Finance.

We’ve said it many times, but it bears repeating: Our portfolios will not by design track any market, domestic or foreign. They are designed, and, as investing conditions change, they are modified, with the objective of maximizing the probability that each investor’s portfolio will effectively weather market upheavals and achieve a sound and successful outcome, regardless of individual market patterns.

We encourage you to review earlier editions of our Market Commentary, which may be found on our website at http://verityinvest.com/investment_management/commentary. Please feel free to contact us for more detailed information and insight into our process and our current thinking about market risks and opportunities.

This material contains forward looking statements. There is no guarantee these outcomes will be achieved. All investing involves risk of loss, and there is no guarantee that strategies that have been successful in the past will be similarly successful in the future.