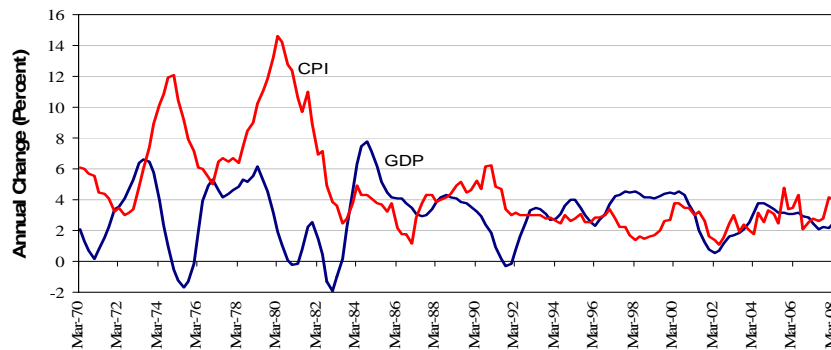


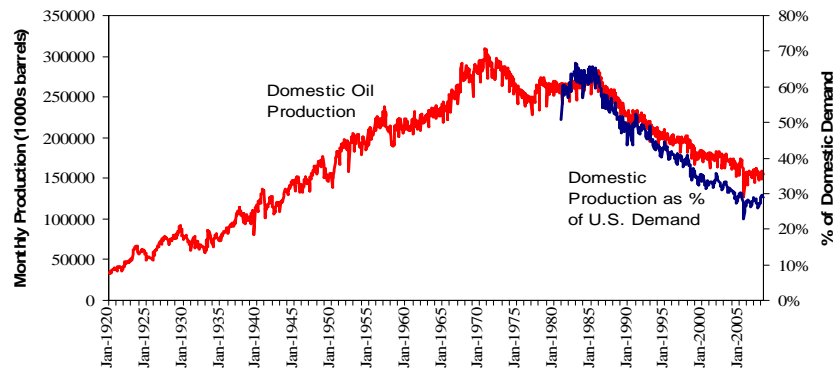
CAPITAL MARKETS REVIEW

Economy

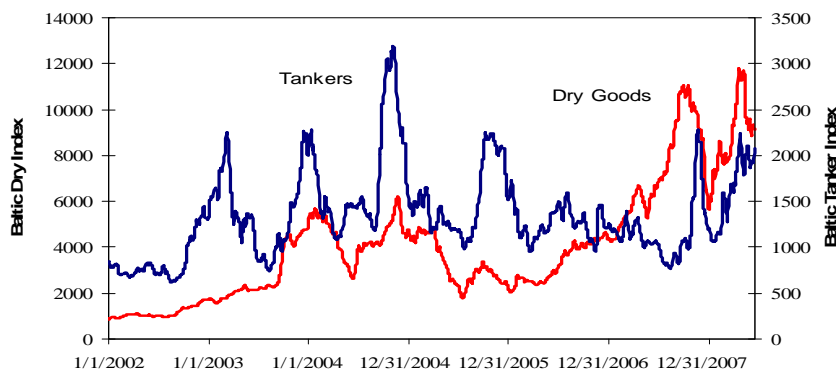
Rising Inflation and Slowing GDP



U.S. Oil Production Remains in Decline



Rising Shipping Costs



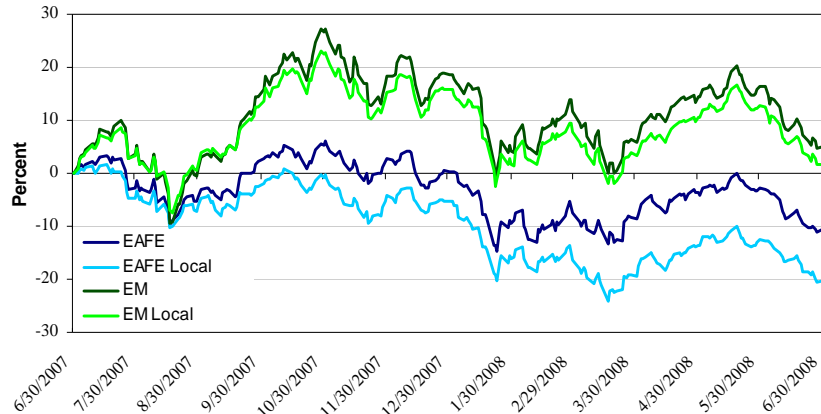
US Economy Continues Anemic Growth

- Growth in the second quarter remained subdued, as uncertainty about energy prices weighed heavily on consumers and businesses.
- The Federal Reserve lowered interest rates to 2.0%, while signaling an end to the string of cuts. Inflation accelerated at a 7.9% annual rate during the quarter, reflecting rising energy, food, and import costs. Year-over-year prices rose by 4.9%. The core inflation rate remained lower at 2.4% year-over-year, reflective of lower clothing, computer, and housing costs, while excluding the basic necessities of food and energy.
- Congress passed a massive farm bill, overriding a veto by President Bush. The \$300 billion bill included provisions for ethanol production, crop price supports, loan guarantees, and a myriad of handouts, while doing little to provide relief for rising food prices.
- High agricultural commodity prices prompted farmers to plant more acreage of corn and soybeans than expected. Offsetting the potential price contraction expected from the increased supply, floods in the Midwest destroyed spring plantings, diminishing potential harvest yields this autumn.
- As crude oil surpassed \$140/barrel, driven by the belief that demand will continue to increase while supplies remain near-constant, the debate over domestic production grew. With imports at over 70% of total demand, and domestic production at levels last seen in 1950, public opinion swung further in favor of allowing expanded oil drilling within the U.S. and its coastal waters.
- Record fuel prices punished airlines, which resorted to trimming fleets and imposing higher charges on passengers. Rail transports continued to prosper, as they benefitted from increased exports and ethanol production, which are most efficiently carried by rail. Container shipments continued to increase, straining overseas shipping capacity, and adding to the costs of foreign production of U.S.-bound goods. Several manufacturers announced plans to reintroduce production in the U.S., as the cost-benefit gap evaporated with higher transportation costs.
- International governments struggled with political upheaval following cuts in oil subsidies, which kept fuel prices substantially below actual costs. Inflation in Asia and Europe continued to rise, increasing the likelihood of rising interest rates in upcoming quarters.

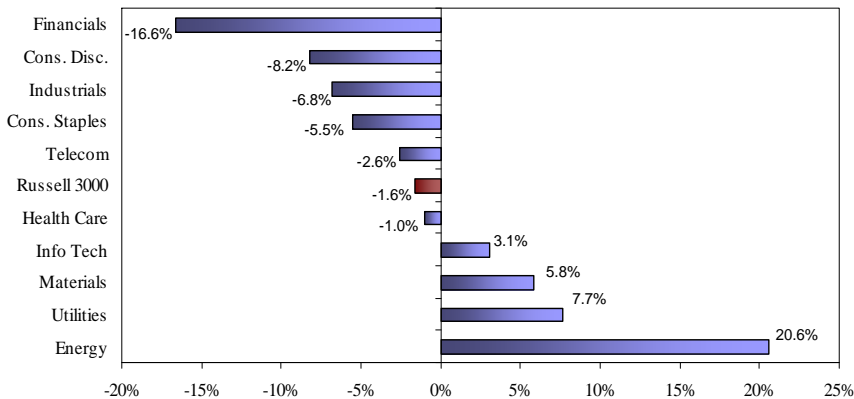
CAPITAL MARKETS REVIEW

Equities

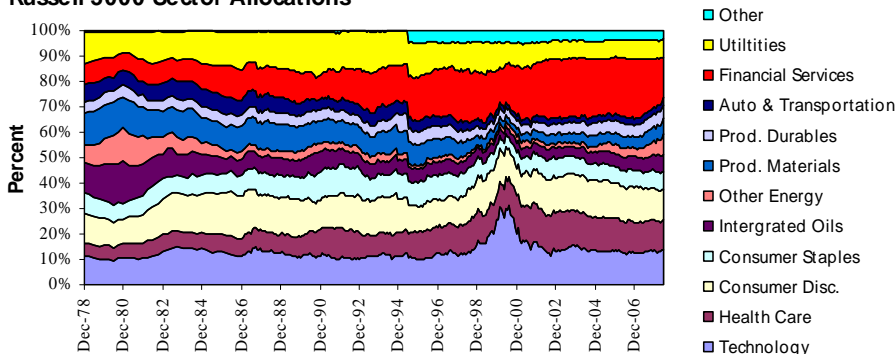
Cumulative Return Since June 30, 2007



2nd Quarter 2008 Sector Returns



Russell 3000 Sector Allocations



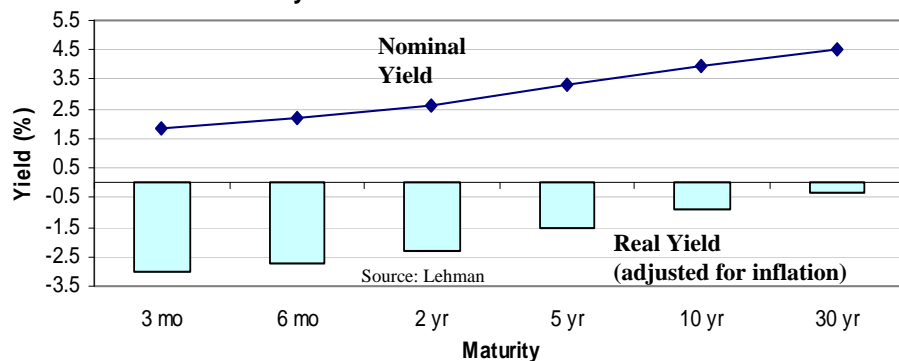
U.S. Stock Returns Edge Closer to Bear Territory

- Positive equity market returns in April and May quickly evaporated in June, as oil and commodity prices continued upward despite a global economic slowdown. The S&P 500 fell 2.7% during the second quarter, bringing the year to date loss to 11.9%. Since the October 9, 2007 peak, the S&P 500 has declined 18.2%, on the verge of bear market territory, defined as a market decline of 20% or more. Valuations have become more attractive with the S&P 500 trading at approximately 18x and 14x, including and excluding negative earnings. Inflation concerns may, however, place further pressure on valuations.
- Small and mid cap stock indices were mostly positive, with only the small cap value style declining for the quarter. The Russell Midcap Index returned 2.7% while the Russell 2000 returned 0.6%. Growth companies outperformed value companies (1.2% vs. -5.3% for the R1000 Growth and R1000 Value, respectively), as financial stock, fell dramatically on negative news and deteriorating fundamentals. Financial stocks account for 25% of the Value Index but only 4% of the Growth Index.
- Sector returns were mixed for the quarter. Information technology (+3.1%) recovered from the previous quarter's drubbing as companies like Apple bounced back from earlier losses. Energy and utilities were the strong performers for the quarter returning 20.6% and 7.7%, respectively, as commodity prices benefited these sectors. Financials (-16.6%) and consumer discretionary (-8.2%) stocks, however, suffered as weakness in both sectors weighed heavily on stock prices. Finance, which peaked at 22% of the market in the third quarter of 2006, now represents just 14% of the stock market.
- Developed foreign markets returned -2.3% in U.S. dollar terms and -0.9% in local terms during the second quarter. Natural resource rich countries were the best performers with Canada (+10.5%), Norway (+10.8%), and Australia (+3.4%) all providing attractive absolute returns. Amid continued inflation concerns, the ECB indicated they would likely increase rates in July by 0.25%, bringing their key rate to 5.25%. This news raised concerns of stymied future growth and markets traded lower.
- Emerging market equities were volatile during the second quarter with the distribution of returns ranging from +34.2% for Argentina to -20.0% for India. As with developed countries, emerging countries that are resource-rich fared better than those that are not. Brazil and Russia rebounded from their first quarter losses to return 17.7% and 9.8%, respectively, during the second quarter. Regionally, Latin America performed strongly, gaining 10.1%, whereas the Asia-Pacific region struggled, losing 9.7% for the quarter.

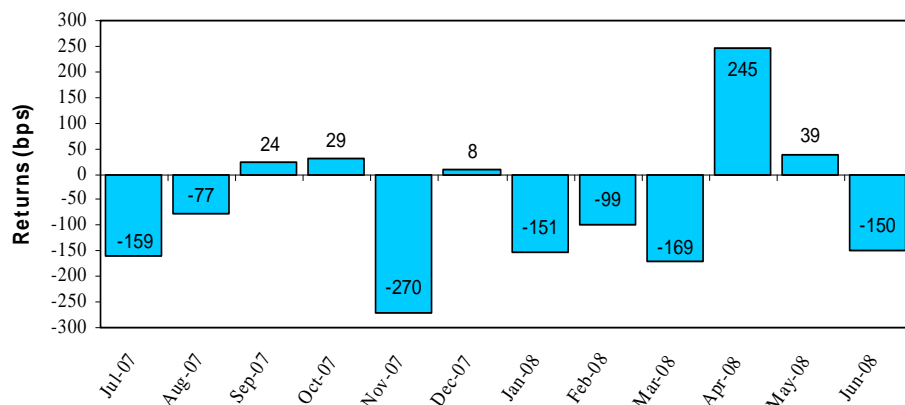
CAPITAL MARKETS REVIEW

Fixed Income

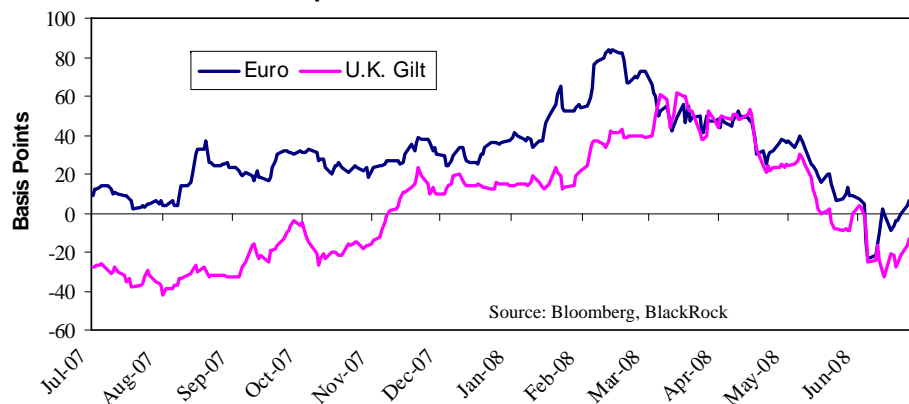
Nominal vs. Real Treasury Yields



LB Credit Index Excess Returns to Treasuries



Two- to Ten-Year Yield Spreads: Euro and U.K. Gilts



Fragile Confidence Leads to Volatile Quarter

- The Lehman Brothers Aggregate Bond Index declined 1.0% during the second quarter, bringing its year to date return to 1.1%. Liquidity and confidence in the market improved after the Fed's unprecedented actions in March, causing all spread sectors to outperform Treasuries in April and May. However, a weakening economic environment, increasing inflation and rising mortgage delinquency rates led to a Treasury rally and a sharp retrenchment in spread sectors in June. Despite June's reversal, Treasuries ended the quarter with a return of -2.1%, underperforming all spread sectors.
- Investment grade corporate bonds saw another difficult quarter as they declined by 0.9%. While the Fed's confidence-boosting measures led the sector to its strongest-ever excess return against Treasuries for the month of April, weak economic data coupled with additional multi-billion dollar writedowns at several large financial firms led the sector to negative returns in May and June.
- The high yield sector returned 1.8% during the quarter, outperforming all other sectors of the market. Relatively strong balance sheets and a default rate that remains low by historical standards combined with an increased yield premium made the sector attractive for many market participants. Amongst high yield securities, CCC-rated issues performed the best with a 4.3% return, while those securities rated most speculative (CC-D) declined by 14.5%.
- The mortgage-backed securities sector continued to see pressure from both fundamental and technical factors during the quarter, as the sector returned -0.5%. Delinquencies that continued to surpass expectations caused MBS spreads to widen, while balance sheet deleveraging as well as SIV and CDO liquidations also negatively impacted prices. The asset-backed securities sector returned -0.8%, as the poor performance of subprime home equity loans continued to weigh on the sector.
- Commercial mortgage-backed securities returned 0.8% during the quarter, outperforming all other investment grade sectors. The technical pressures that caused CMBS to be the worst-performing sector in the first quarter reversed, as shorts on the sector's synthetic index were covered and fundamental, long-oriented investors moved into the market. The sector's performance was also aided by scant new supply, as there was a 91% reduction in CMBS issuance in the first half of 2008 from a year earlier.
- Inflation concerns and the hawkish rhetoric of central banks had negative effects on bond markets around the globe, as hedged non-US developed market bonds returned -2.4%. Emerging market debt also suffered from the higher yields demanded by investors to compensate for accelerating inflation, returning -0.8% during the quarter. Despite the increase in yields, appreciation of emerging currencies against the dollar led locally-denominated EM debt to return 3.9%.

CAPITAL MARKETS REVIEW

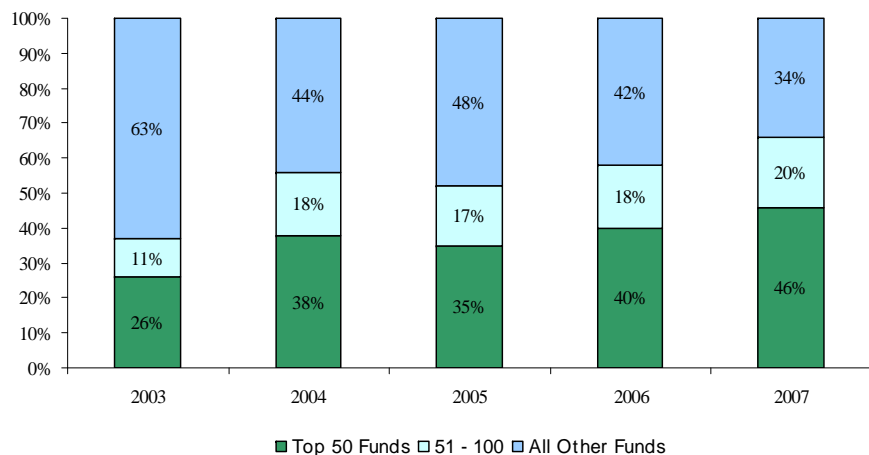
Hedge Funds

Hedge Fund Performance Results June 30, 2008

Style	Second Quarter	Year to Date
Convertible Arbitrage	-0.6%	-6.8%
Distressed Securities	2.6%	-1.4%
Equity Hedge	2.6%	-3.5%
Equity Market Neutral	3.0%	2.8%
Macro	2.6%	6.8%
Merger Arbitrage	1.5%	-0.3%
Fund of Funds	1.8%	-2.5%

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Global Industry Assets Under Management



Sources: Absolute Return, Alpha, Morgan Stanley estimates.

Hedge Funds Protect Capital during June; Largest Managers Continue to Attract Assets

- Similar to equities, hedge fund strategies generated solid returns during the first half of the second quarter. While June was a dismal month for equities as witnessed by the S&P 500 Index's 8.4% decline, most hedge fund strategies suffered minimal losses. The HFR Fund of Funds Index fell only 1.0% in June. The overall result was a second quarter loss of 2.7% for the S&P 500 Index versus a gain of 1.8% for the Fund of Funds Index. HFR data shows that in aggregate, hedge funds offered significant protection during the difficult equity and credit markets of 2008.
- Most hedge fund strategies finished in positive territory at the end of the quarter. Long-biased equity managers were the top-performers during April and May fueled by the global equity rally, but many suffered losses in June. Equity-oriented hedge funds that were able to generate positive returns for the month generally did so through success on the short side.
- Macro managers continued their strong run of performance through the second quarter by exploiting the surge in energy and other commodity prices, and through profitable currency trades. Macro managers have performed considerably well year to date, returning 6.8% through June.
- After five straight months of negative returns, distressed debt managers posted gains during April, May, and June, for a solid second-quarter return of 2.6%.
- The concentration of assets managed by the largest hedge funds is increasing rapidly, as depicted in the chart to the left. It is estimated that the eleven largest hedge funds controlled almost \$350 billion of the \$1.9 trillion in hedge fund assets at the beginning of 2008. This shift likely stems from investors' increased preference for well-established, institutional quality firms. Additionally, the number of new fund launches has been decreasing in recent years. Reuters reported that approximately three dozen U.S. hedge funds were launched so far this year, 50% less than the same period last year. It is getting harder for small funds to raise capital due to investor concern about the operational risk associated with new firms.
- According to Eurekahedge, approximately \$5 billion of net assets flowed into hedge fund strategies during the second quarter, most of that during the month of June. Macro-oriented and multi-strategy managers experienced the largest inflows.

CAPITAL MARKETS REVIEW

Private Equity

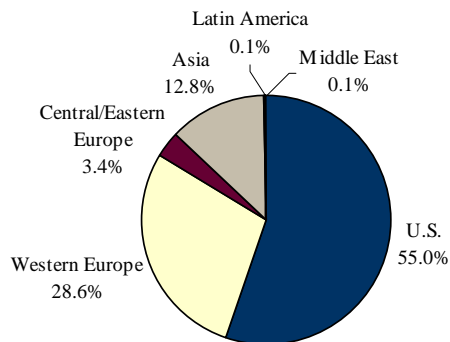
Investment Horizon Returns as of 3/31/08

Fund Type	3 Months	1 Year	3 Years	5 Years	10 Years	20 Years
Early/Seed VC	-0.8%	10.6%	4.9%	4.8%	34.0%	21.2%
Balanced VC	-5.4%	8.8%	13.1%	12.7%	14.8%	14.6%
Later Stage VC	-0.4%	30.4%	13.1%	11.1%	8.6%	14.6%
All Venture	-2.5%	13.3%	9.5%	9.1%	17.2%	16.8%
Small Buyouts	-0.8%	15.0%	7.0%	9.4%	4.8%	12.5%
Med Buyouts	-1.0%	19.0%	10.9%	12.2%	8.3%	12.4%
Large Buyouts	-0.3%	16.8%	8.5%	14.1%	6.7%	12.3%
Mega Buyouts	-2.6%	10.0%	14.4%	16.8%	8.4%	11.9%
All Buyouts	-2.4%	10.8%	13.0%	15.6%	7.9%	12.1%
Mezzanine	4.1%	18.4%	5.1%	5.5%	6.1%	8.2%
All Priv Equity	-2.6%	12.9%	12.3%	13.5%	9.9%	13.5%
S&P 500	-9.4%	-5.1%	5.9%	11.3%	3.5%	11.0%
Russell 2000	-9.9%	-13.0%	5.1%	14.9%	5.0%	9.8%

Source: Thomson Financial Venture Economics & National Venture Capital Assn.

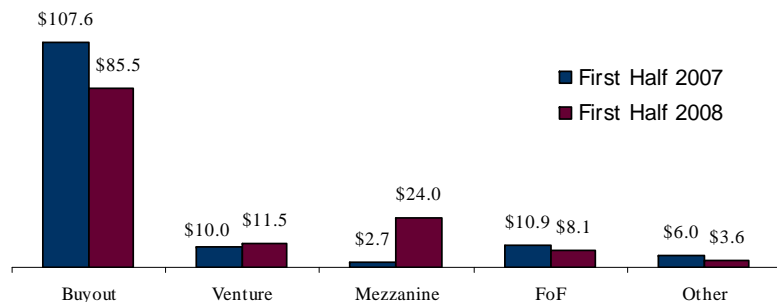
Note: Data is continuously updated and is therefore subject to change.

Anticipated Limited Partner Investments



Source: Private Equity Funds-of-Funds State of the Market, 2008 Edition

Fundraising by Sector



Source: Private Equity Analyst, July 10, 2008

Deal Flow Feels the Effect of the Credit Crunch

- Nearly all sectors posted negative returns during the past quarter. The exception was mezzanine debt funds, which managed to advance 4.1%. As the credit markets came to virtual lockdown, mezzanine lenders were able to provide capital at favorable terms. Despite the unfavorable market conditions, private equity still fared better than the broad public equity markets over both the short and long-term.
- Buyout and venture markets are feeling the effects of the credit crunch. In the first half of 2008, buyout deal volume totaled \$125 billion, down from \$528 billion in the first half of 2007. On the venture side, just 57 initial public offerings were filed in the first half of 2008, down from 147 during the first six months of 2007. Of the 57 IPO's filed in 2008, 44 have been withdrawn due to unfavorable market conditions.
- The rising price of oil and greater emphasis on a green environment has led to record-setting levels of investment in clean technology. During 2007, investors committed a total of \$8.5 billion to the clean-tech space in both buyout and venture capital, up from \$7.1 billion in 2006. Clean technology is now the third largest sector of the venture market, behind software and life sciences.
- Fund-of-funds in the market today remain focused on the U.S. and Europe. But an increasing amount, \$3.6 billion, is being sought for Asian specific funds-of-funds.
- In the first half of 2008, U.S. private equity firms raised less than they did in the first half of 2007. This is the first decline in fundraising since 2003. Firms raised \$132.7 billion across 185 funds, 3% shy of the \$137.2 billion first half record set by 199 funds last year. Buyout firms raised \$85.5 billion across 75 funds, down 20% from one year ago. Strong fundraising in the mezzanine sector helped offset weakness in the buyout sector.

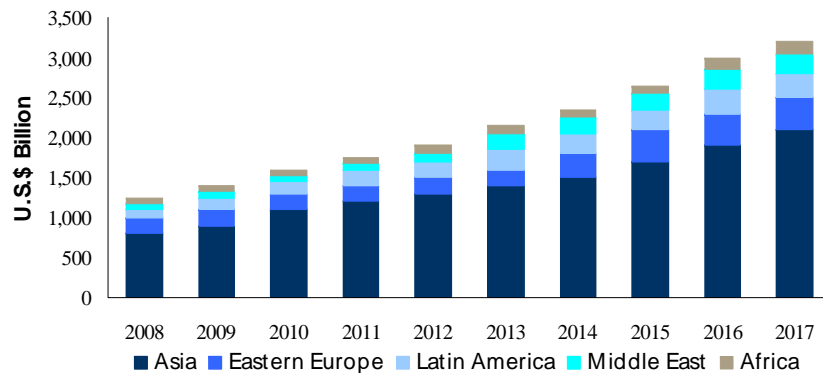
CAPITAL MARKETS REVIEW

Real Assets

Returns as of March 31, 2008

	3 Mon.	1 Yr.	3 Yrs.	5 Yrs.	10 Yrs.
NCREIF	1.6%	13.6%	16.8%	15.1%	12.6%
Apartments	1.3%	9.6%	14.7%	13.5%	12.3%
Industrials	1.4%	13.0%	16.9%	14.3%	12.7%
Office	2.0%	17.5%	19.2%	15.4%	12.6%
Retail	1.4%	11.6%	14.4%	17.0%	13.5%
Hotel	1.4%	15.6%	20.0%	15.3%	10.6%
East	1.6%	13.7%	17.4%	16.2%	13.7%
Midwest	1.0%	11.2%	12.4%	11.6%	9.9%
South	2.1%	12.0%	15.4%	13.5%	11.0%
West	1.5%	15.2%	18.5%	16.3%	13.8%

Infrastructure Spending in Developing Countries



Source: World Bank, Global Insight, Morgan Stanley Research Estimates.

DJ-AIG Commodity Index Components Total Return Ending June 30, 2008

Allocation	Segment	3 Months	YTD	1 year
31%	Energy	35.0%	55.6%	75.9%
17%	Industrial Metals	-3.8%	14.8%	-3.8%
8%	Precious Metals	0.6%	11.6%	40.3%
20%	Grains	18.7%	26.3%	70.4%
7%	Livestock	8.1%	-8.2%	-17.9%
9%	Petroleum	38.6%	47.0%	96.1%
8%	Softs	3.1%	1.9%	11.1%
100%	Total Market	16.1%	27.2%	41.6%

Real Estate Begins to Slow, While Commodities Soar

- Private real estate markets slowed during the first quarter of 2008 and experienced their lowest quarterly return in six years. During the quarter, the NCREIF Property Index gained a modest 1.6% signifying that credit market turmoil and a slow economy may result in downward pricing of commercial properties. For the trailing one-year period ended March 31, 2008, the NCREIF Property Index return was still relatively strong at 13.6%, due to stellar performance during 2007.
- The return differences among property types narrowed during the quarter. Office properties continued to outpace other property types, but also experienced a slowdown from previous quarters; returning 2.0%. Closely following were industrials, hotel, and retail properties, that all returned 1.4%. Apartment properties (+1.3%) continued to have the weakest relative returns and have trailed the NCREIF Property Index for the last nine consecutive quarters, as the economy and employment growth have slowed.
- Publicly-traded REITs, which stabilized in April and May, fell along with the rest of the market in June and ended the second quarter with a return of -5.1%. Year-to-date, the NAREIT Index has declined -5.5%.
- There was one significant transaction in the REIT market during the quarter. Boston Properties acquired the General Motors building and three additional office towers in New York City from Macklowe Properties for \$4 billion.
- Commodities were one of the few market segments to prosper in a period of significant price volatility. They have performed well despite a global economic slowdown due to strong demand from emerging markets and constrained supply. Estimates of infrastructure spending in developing countries total \$21.7 trillion over the next ten years.
- The DJ-AIG Commodity Index surged 16.1% during the second quarter, bringing year-to-date gains to 27.2% and trailing one-year results to 41.6%. Performance continued to be driven by the energy (+35.0%) and petroleum (+38.6%) sectors, as well as grains (+18.7%). The energy and petroleum sectors have returned an astounding 75.9% and 96.1%, respectively, over the trailing one-year period.
- The up tick in commodity prices for both food and energy has had significant consequences around the globe, resulting in public demonstrations and potential legislation to prevent “speculators” from investing in commodities and commodity futures. Many major airlines have banded together to lobby for additional transparency and disclosure in the oil markets by asking customers to contact Congress to encourage market reform.

CAPITAL MARKETS REVIEW

Index Returns

As of June 30, 2008

(Percentage Return)

	1 Quarter	Year To Date	1 Year	2 Years	3 Years	5 Years	7 Years	10 Years
Domestic Equity Indices								
Dow Jones Wilshire 5000	-1.5	-11.0	-12.5	2.7	5.1	8.8	3.7	3.6
S&P 500	-2.7	-11.9	-13.1	2.4	4.4	7.6	2.5	2.9
Russell 1000 Index	-1.9	-11.2	-12.4	2.7	4.8	8.2	3.0	3.4
Russell 1000 Growth Index	1.2	-9.1	-6.0	5.8	5.9	7.3	1.1	1.0
Russell 1000 Value Index	-5.3	-13.6	-18.8	-0.5	3.5	8.9	4.7	4.9
Russell Midcap Index	2.7	-7.6	-11.2	3.6	6.8	13.1	8.1	8.1
Russell Midcap Growth Index	4.6	-6.8	-6.4	5.8	8.2	12.3	5.1	5.6
Russell Midcap Value Index	0.1	-8.6	-17.1	0.6	5.0	13.0	9.3	8.4
Russell 2000 Index	0.6	-9.4	-16.2	-1.2	3.8	10.3	5.6	5.5
Russell 2000 Growth Index	4.5	-8.9	-10.8	2.1	6.1	10.4	3.1	2.8
Russell 2000 Value Index	-3.5	-9.8	-21.6	-4.6	1.4	10.0	7.7	7.5
International Equity Indices								
MSCI EAFE	-2.3	-11.0	-10.6	6.5	12.8	16.7	9.0	5.8
MSCI EAFE Growth Index	0.0	-8.1	-4.4	9.4	14.7	16.3	8.5	4.1
MSCI EAFE Value Index	-4.6	-13.8	-16.6	3.6	10.9	17.0	9.4	7.3
MSCI EAFE Small Cap	-4.5	-10.5	-18.6	0.9	9.4	19.0	13.2	N/A
MSCI AC World Index	-1.6	-10.7	-9.3	6.6	10.3	13.1	6.5	4.9
MSCI AC World ex US	-1.1	-10.2	-6.6	10.0	15.7	18.9	11.0	7.4
MSCI Emerging Markets Index	-0.8	-11.6	4.9	23.5	27.5	30.1	22.1	15.5
Fixed Income Indices								
Barclays Capital Aggregate	-1.0	1.1	7.1	6.6	4.1	3.9	5.4	5.7
Barclays Capital U.S. Government/Credit	-1.5	1.0	7.2	6.6	3.8	3.6	5.6	5.7
Barcap Intermediate U.S. Government/Credit	-1.5	1.4	7.4	6.6	4.3	3.5	5.2	5.5
Barclays Capital U.S. Long Government/Credit	-1.5	-0.7	6.8	6.9	2.2	4.0	6.8	6.3
Barclays Capital US Corp: High Yield	1.8	-1.3	-2.3	4.4	4.5	6.9	7.5	4.9
Merrill Lynch 1-3 Year Treasury	-0.9	2.1	7.3	6.2	4.7	3.3	4.0	4.7
Merrill Lynch 3 Month US T-Bill	0.3	1.2	3.6	4.4	4.3	3.2	2.9	3.6
Citigroup Non-U.S. World Government Bond	-4.7	5.7	18.7	10.2	6.7	7.1	9.8	6.7
Real Estate								
Dow Jones Wilshire REIT	-5.4	-3.4	-15.3	-2.7	4.9	14.5	13.1	11.3

Returns for periods greater than one year are annualized.