HENNESSEE GROUP LLC
HEDGE FUND ADVISORY
YOUR STRATEGIC PARTNER IN HEDGE FUND INVESTING

HENNESSEE
HEDGE FUND REVIEW®

JANUARY 2009
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	DEC	YTD
Hennessee Hedge Fund Index	+0.51%	-19.15%
S&P 500	+0.78%	-38.49%
Long/Short Equity	+0.31%	-18.34%
Arbitrage/Event Driven	+1.00%	-18.57%
Global/Macro	+0.61%	-20.72%
Percentage of Hedge Fund Managers Outperforming the:		
S&P 500	45%	87%

Top (3) Performing:	DEC		YTD
Convertible Arbitrage	+3.90%	Short Biased	+26.31%
Telecom & Media	+3.80%	Macro	+3.37%
International	+2.76%	Merger Arbitrage	-0.87%

Bottom (3) Performing:	DEC		YTD
Europe	-1.05%	Emerging Markets	-30.01%
Short Biased	-0.93%	Latin America	-27.48%
Event Driven	-0.60%	Distressed	-26.30%

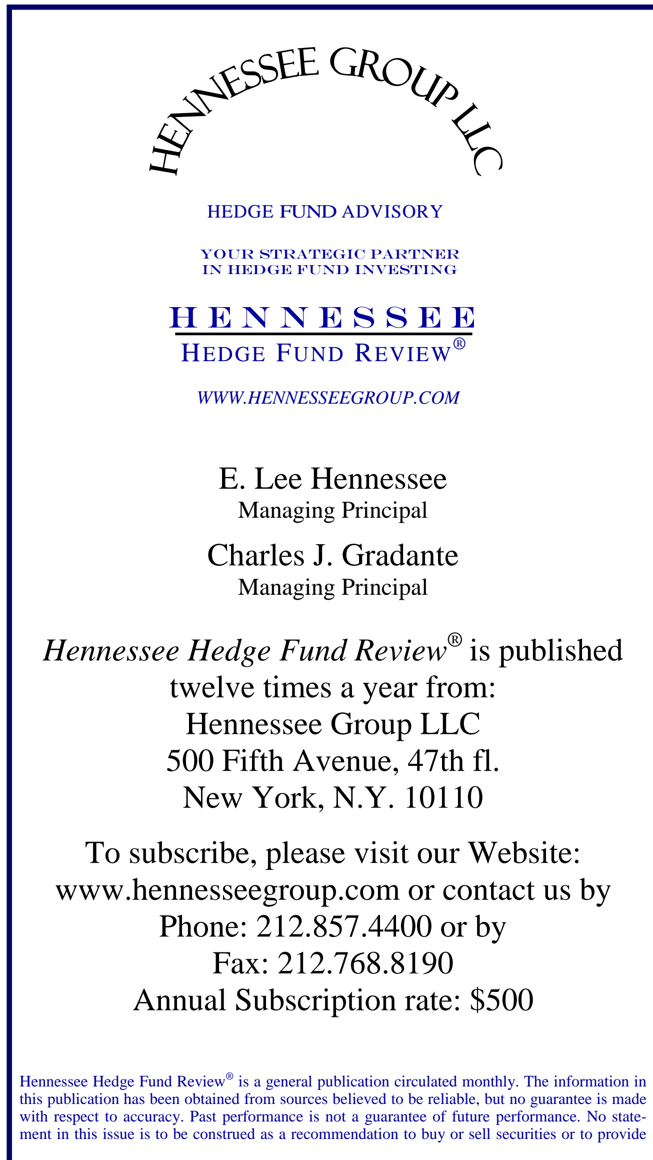
MARKET SUMMARY - 2008

The financial markets experienced one of their worst years in history in 2008. **What started out as a serious credit crunch in the summer of 2007 evolved into a much broader financial crisis that resulted in a widespread economic slowdown and massive sell-off across nearly every asset class in 2008.** Equities and commodities experienced the most significant declines, followed closely by high yield debt. Conversely, U.S. Treasuries and gold benefited from the increasingly risk averse nature of investors as the year progressed.

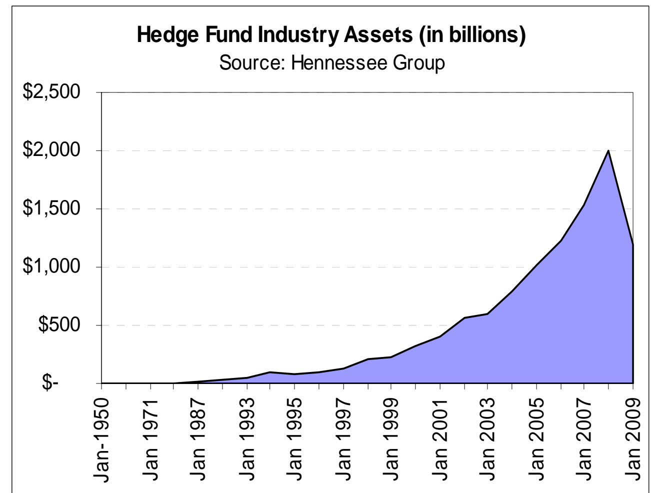
The S&P 500 Index finished 2008 down -38.5%, while the Russell 2000 Index (small cap stocks) closed the year off -33.8%. International stocks didn't fare any better in 2008 as the MSCI EAFE Index lost -43.4% and the MSCI Emerging Markets Index fell -53.3%. The fixed income markets experienced mixed results for the year as the Barclay Aggregate Bond Index gained +5.2% (attributed to positive performance of Treasuries) while the Barclay High Yield Index lost -26.2%. **The 10 Year Treasury gained an extraordinary +20.1% in 2008.**

Concerns of a global recession grew as the year progressed and led to a sharp sell-off in commodities. The CRB Index lost -40.0% in 2008. Crude oil (WTI) finished the year trading at $44.60 a barrel, down -53.5% from the start of the year. Conversely, gold benefited from the flight to quality and gained +5.8% for the year.

The Hennessee Hedge Fund Index gained +0.51% during the month of December, however finished 2008 down -19.15%. While from an absolute return perspective hedge funds disappointed in 2008; both on a relative and risk-adjusted basis, they continued to outperform their traditional counterparts and are therefore likely to remain a top priority among Investment Committees heading into 2009.

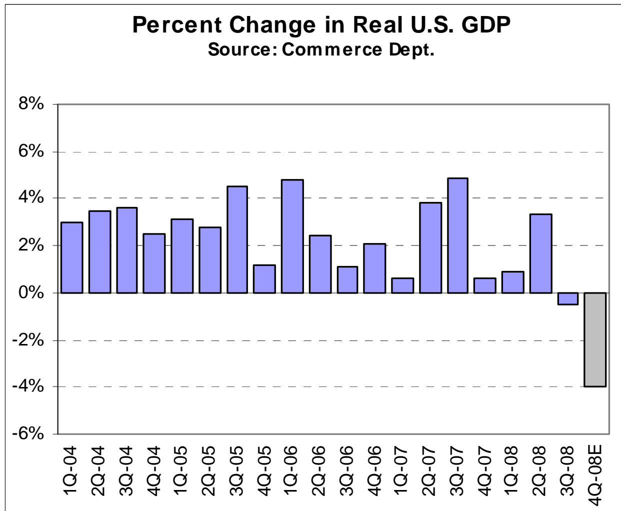


That said, 2008 did present some challenges for hedge funds. Disgruntled investors issued a record amount of redemptions in the latter parts of the year. **With the average hedge fund down -19% for the year and redemptions of approximately 25%, The Hennessee Group believes the hedge fund industry could be 50% smaller heading into 2009.** In addition to suffering from a record amount of redemptions, they will also have to work to restore the image of the industry. A number of high profile funds liquidated or froze redemptions at the behest of investors and the industry was hit with its largest ponzi scheme in history. Initial estimates indicate hedge fund investors could have lost up to $50 billion in the fraud revealed in mid-December. **In light of these developments, it is widely believed the hedge fund industry will see a number of changes in the coming year, particularly with regards to increased levels of transparency and regulation.**

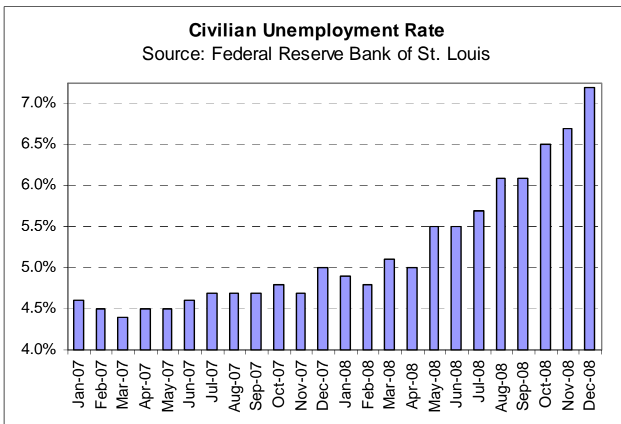


The U.S. economy held up fairly well in the first half of 2008 due in large part to exports and fiscal stimulus. However, as the housing market deteriorated and the unemployment situation worsened, the economy slowed significantly in the latter part of the year. The third quarter experienced a decline in GDP growth of -0.5% due in large part to the weakening consumer.

In addition, the National Bureau of Economic Research (NBER) announced late in the year that the U.S. economy had officially entered a recession in the fourth quarter of 2007. **Most economists believe the U.S. economy could contract by as much as -4.0% in the fourth quarter and will likely remain mired in a deep recession through the first half of 2009.**



The employment situation worsened throughout the year with the most recent report indicating 524,000 jobs were lost in December. Overall, employers announced 2,589,000 job cuts in 2008, the largest annual total since 1945. The unemployment rate finished the year at 7.2%, up from 4.7% at the beginning of 2008. **Economists believe the unemployment rate could exceed 8.0% in the latter parts of 2009 as economic conditions are likely to further deteriorate.**

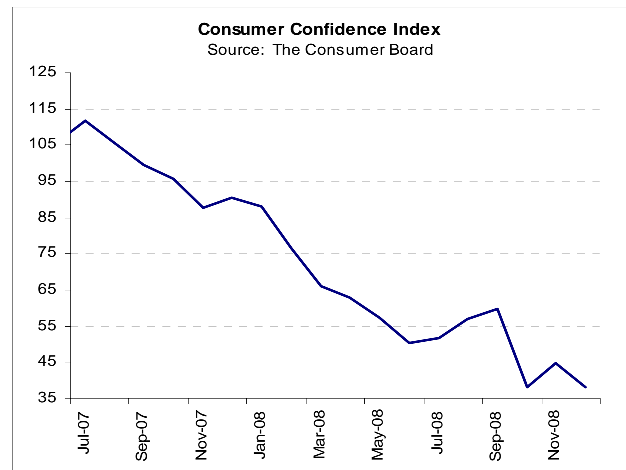


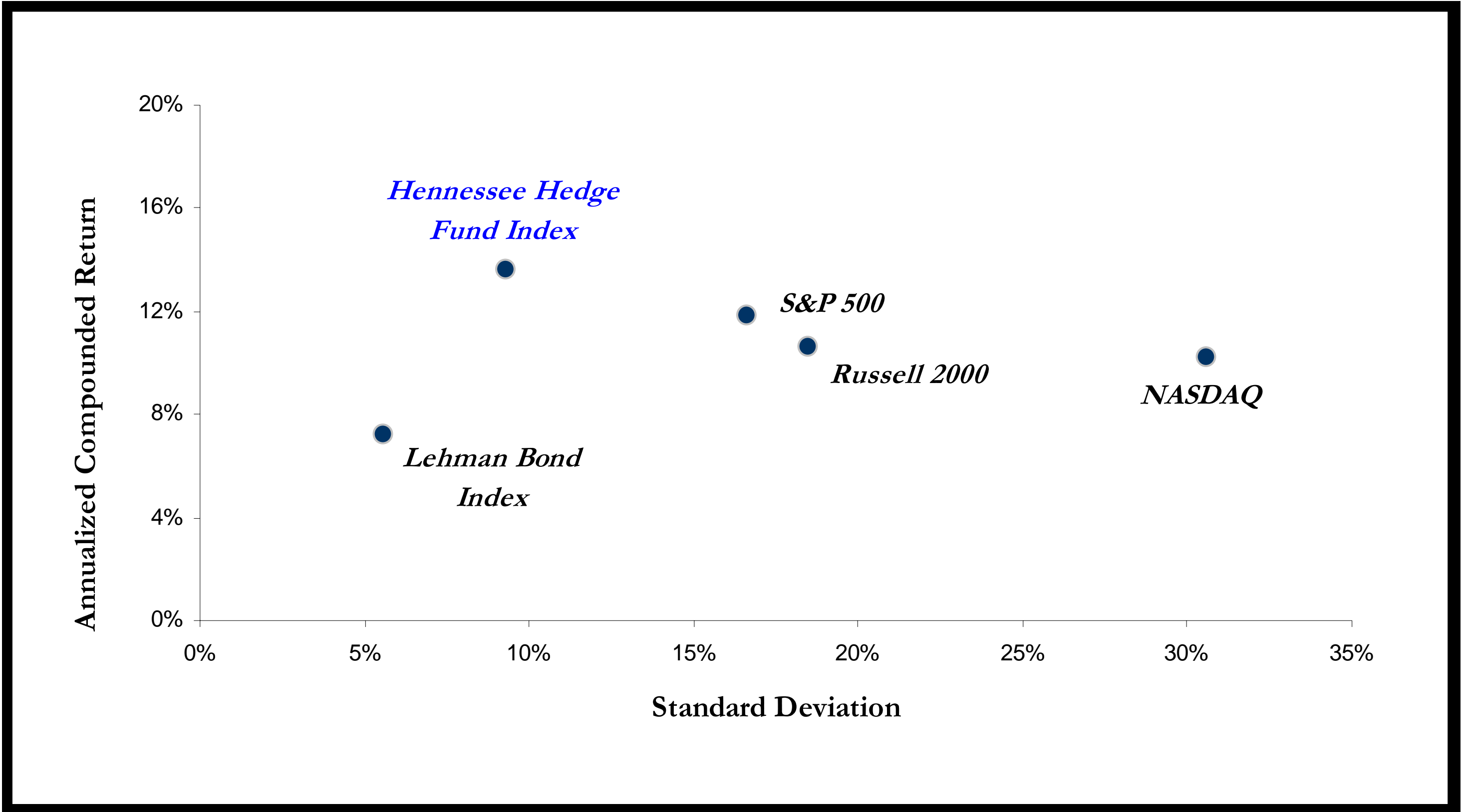
The Institute for Supply Management's manufacturing index (ISM Index), a diffusion index measuring national manufacturing conditions by surveying 300 firms on employment, production, new orders, supplier deliveries and inventories, continued its downward decline in December. **The final 2008 reading for the ISM Index came in at 32.4 (readings below 50 indicate a contracting factory sector), down from 36.2 in November and the lowest index reading in 28 years.** The New Orders Index, a key indicator for ongoing demand, plunged to 22.7, the 13th consecutive decline for the index and its lowest level since January 1948.

The Standard & Poor's/Case-Shiller U.S. National Home Price Index, which tracks changes in the value of the residential real estate market in 20 metropolitan regions across the United States, dropped a record rate in October. **The index fell -18.0% on a year-over-year basis, making for the 22nd consecutive monthly decline for the index and reaching a level not seen since March of 2004.**

The Labor Department reported consumer prices experienced the biggest one-month decline in November, the second consecutive record decline dating back to February 1947. The Consumer Price Index (CPI) fell -1.7% in November, down from -1.0% in October. The energy index fell -17.0% in November, almost twice the October decline. Energy prices are now -32.4% below the July peak earlier this year. The gasoline index fell -29.5% in November and is now -47.0% below its July peak. **The core rate, which excludes food and energy, was flat and remains at its lowest point since September of 2005.** The year-over-year CPI fell to +1.1% in November, substantially below the 17 year high set this past July at +5.6%. **In the near term, economists anticipate inflation to remain in check. However, they believe the unprecedented actions taken by the government in the past year to stimulate the economy could lead to inflationary pressures over the longer term.**

Due in large part to accelerating layoffs and deteriorating markets for housing, stocks and other investments, the consumer confidence hit an all-time low in December. The Consumer Confidence Index fell to 38.0 in December, down from 44.7 in November and below its prior low of 38.8 in October. **The index finished the year well off its high set in July of last year at 112.0.**





The Hennessee Hedge Fund Indices® are calculated from performance data supplied by a diversified group of hedge funds monitored by the Hennessee Hedge Fund Advisory Group. The Hennessee Hedge Fund Index is an equally- weighted average of the funds in the Hennessee Hedge Fund Indices®. The funds in the Hennessee Hedge Fund Index is net of fees and unaudited. The hedge fund performance data has been obtained from sources believed to be reliable, but no guarantee is made with respect to accuracy. Past performance is no guarantee of future returns. This material is for general information only and is not an offer or

You Wouldn't Use a Stock Index to Benchmark Your Bond Portfolio

So Why Use One to Benchmark Your Hedge Funds?

Hennessee Hedge Fund Indices®

Hennessee Group recognized the need for the creation of specific 'benchmarks' to measure a hedge fund manager's success. From this original concept, the blueprints of the Hennessee Hedge Fund Indices® evolved into what we know today.

The Hennessee Hedge Fund Indices® have been used as a hedge fund benchmark since 1987. Created real-time, the Hennessee Hedge Fund Indices® are an equally weighted average of a diversified group of hedge funds consisting of 23 different investment styles.

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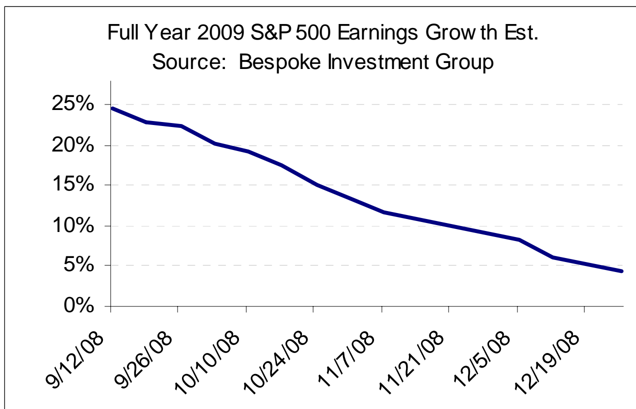
Your Strategic Partner In Hedge Fund Investing

As sentiment among consumers has deteriorated in recent months, they have significantly shifted their spending habits, opting to save money and pay down debt. The US Commerce Department announced retail sales in the U.S. fell -1.9% in November and is now off -7.4% from a year ago. While retail sales have fallen, personal savings for U.S. households has increased dramatically. Savings rose to +2.8% in November. That is +0.4% higher than the +2.4% in October and much greater than the +0.1% rise economists expected. **In addition, the Federal Reserve reported that household debt fell for the first time ever in the third quarter.**

In light of the slowing economy and shift in consumer spending habits, corporate earnings have come down significantly in recent months. **Third quarter 2008 operating earnings for the S&P 500 Index declined from $184 billion in the third quarter of 2007 to $143 billion in the third quarter of 2008, representing a -22% drop on a year-over-year basis.** Energy continued to be the primary contributor, with an earnings increase of +89% from a year earlier. Conversely, financials experienced a -193% decline in earnings from a year earlier and consumer discretionary companies experienced a -42% drop. **Current estimates call for a -12% decline in fourth quarter 2008 operating earnings on a year-over-year basis and a +4.5% gain in operating earnings for the full year 2009.** That said, it is widely believed these estimates are still too optimistic and likely to be further reduced in the coming months. Most experts believe 2009 operating earnings are likely to experience negative growth.



In light of the tumbling financial markets and weakening economy, the U.S. government has become increasingly aggressive with its fiscal and monetary policies. **In addition to aggressively reducing its target for the federal funds rate to a range of 0% to .25%, the Fed has created a variety of lending facilities in an attempt to stabilize troubled financial companies and increase liquidity for the credit markets.** As a result, the Fed has greatly expanded the size of its balance sheet with notable programs such as the Troubled Asset Relief Program (TARP). And with inflation in check, at least in the near future, expectations are for the Federal Reserve to keep interest rates low for the duration of 2009 as well as further expand the balance sheet well beyond the $2 trillion it has grown to in the past year.

President-elect Obama recently announced the new administration will embark on an economic stimulus package designed to create millions of jobs by making "the single largest new investment in our national infrastructure since the creation of the federal highway system in the 1950s." In addition, the Federal Reserve has plans to reliquify the mortgage market with a $600 billion purchase of housing-related GSE's and mortgage-backed securities. The Fed will also lend up to $200 billion against the issuance of asset-backed securities collateralized by student loans, auto loans, credit card loans, and loans guaranteed by the Small Business Administration. **While these actions are considered necessary by many to stabilize the economy and restore confidence in the financial markets, there is increasing concern that we are setting the stage for future problems, particularly inflation.**

There is belief the worst of the credit crisis could be behind us, however most hedge funds remain very cautious as the global economy appears to be in the midst of a deep recession, and is showing no signs of a turnaround anytime soon. While investors are pleased with many of the actions taken by the government and Federal Reserve, they believe it will take time to take effect.

Heading into 2009, hedge funds believe improvements in the credit markets, unemployment and consumer and corporate spending will be critical for the economic recovery to take hold. **That said, many managers are seeing compelling opportunities from a valuation perspective in the market place and plan to opportunistically increase their exposures in the coming months.** In addition, many funds believe they will see the return of differentiation among stocks and sectors in 2009 and will also benefit from less competition chasing the same alpha generating trades.

Long/Short Equity
(YTD: -18.34% / DEC: +0.31%)

Long/short equity funds struggled in 2008 as stocks experienced one of their worst sell-offs in recent history; no sector, style or market capitalization was spared. While the majority of hedge funds were able to generate profits on the short side of their books, these gains were more than offset by losses incurred on their long positions. To illustrate the breadth of the sell-off, only 29 stocks in the S&P 500 Index experienced gains in 2008. **The Hennessee Long/Short Equity Index gained +0.31% in December, however finished 2008 down –18.34%. While on an absolute basis long/short equity funds disappointed, they still managed to outperform on a relative basis as the S&P 500 Index closed 2008 down –38.49%.** Conversely, the Hennessee Short Biased Index generated a +26.31% gain for the year, and was the best performing strategy by a significant margin.

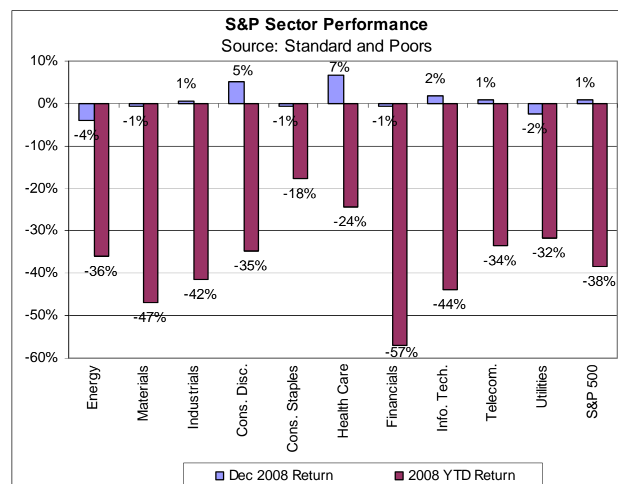
Over the longer term, long/short equity funds have drastically outperformed their traditional counterparts. **The Hennessee Long/Short Equity Index has generated an annualized return of +7.06% over the 10 year period while the S&P 500 Index has lost -3.03%.**

Hennessee Long/Short Equity Index vs. S&P 500
Source: Hennessee Group; Standard & Poor's

	Long/Short Equity Index	S&P 500	Difference
1998	7.3%	26.7%	-19.4%
1999	33.9%	19.5%	+14.4%
2000	10.2%	-10.1%	+20.3%
2001	2.9%	-13.0%	+15.9%
2002	-6.4%	-23.4%	+17.0%
2003	19.4%	26.4%	-7.0%
2004	7.8%	9.0%	-1.2%
2005	6.8%	3.0%	+3.8%
2006	11.1%	13.6%	-2.5%
2007	12.1%	3.6%	+8.5%
2008	**-18.3%**	**-38.5%**	**+20.2%**
Annualized (1998-2008)	**+7.06**	**-3.03**	**+10.3**

While the sub-par performance in 2008 of long/short equity funds was largely attributable to the broad based sell-off in equities, further complicating the ability of managers to generate alpha were the extreme levels of volatility coupled with the disconnect between company fundamentals and share price movements. The VIX hit an all time high in 2008 as dramatic news pertaining to the declining economic conditions, disappointing corporate earnings and ongoing financial crisis led to wild intra-month swings. In addition, the ongoing global deleveraging process caused by rising levels of redemptions and fund liquidations resulted in forced selling and short covering, particularly in many of the names widely held by hedge funds. Lastly, the unprecedented actions taken by the government in 2008, particularly with regards to the bailout of select companies and short sale ban of over 950 stocks further exacerbated already irrational stock price movements.

In 2007, long/short equity funds benefited from a wide dispersion in returns among sectors and stocks as managers were able to identify profitable positions on both the long and short side of their books. While this strategy held up in the early part of 2008 with the long energy, short financial trade; the second half of the year brought a strong sell-off across all sectors. As the year progressed and the sell-off deepened well beyond expectations, hedge funds became increasingly defensive. By year end, the turmoil in the financial markets had reached a crisis level and the correlation between individual stock price movements rose to extremely high levels. **The extreme sell-off coupled with the lack of differentiation among sectors and stocks left little options for managers other than to focus on capital preservation. In short, the primary contributor to relative out performance for long/short equity funds in 2008 was the defensive posture of one's portfolio.**



The financial sector was the worst performing sector in the S&P 500 Index for the year. The financial crisis, which began in 2007, continued to deepen in 2008 and led to a sharp sell-off across the entire sector. The failure and subsequent takeover of Bear Stearns, the failure of Lehman Brothers, the bailout of AIG, the takeover of Merrill Lynch and the transformation of Goldman Sachs and Morgan Stanley into commercial holding companies were just

some of the major story lines of 2008. Despite such troubles, the sector proved to be an alpha generator for many funds in the early part of the year as many funds anticipated the difficulties well ahead of time and maintained shorts on the sector.

However, this trade became increasingly difficult during the second half of the year. In addition to valuations getting low, the government intervened on many levels, particularly by bailing out troubled financial companies. In addition, the SEC placed a ban on the shorting of over 950 companies, primarily in the financial industry. The ban not only limited their ability to short troubled companies but also led to short squeezes, whereby companies with weak fundamentals experienced strong gains. That said, the short profits generated in the first half of the year led to the Hennessee Financial Equities Index strongly outperforming on a relative basis. **The Hennessee Financial Equities Index declined -14.99% while financials within the S&P 500 Index finished the year down -57.0%.** With financials trading at increasingly attractive levels and interest rates at historical lows, hedge funds are stating they will look to cautiously increase their long exposure to the sector in 2009. A particular emphasis will likely be in the equity securities of recovering financials that experienced extreme sell-offs as a result of the credit crisis.

The energy and materials sectors – popular themes for hedge funds in recent years - started 2008 strong, but sold off strongly in the second half of the year due in large part to slumping revenues and concerns regarding the slowing economy. The energy sector within the S&P 500 Index finished the year down -35.9%, while materials were off -47.1%. Notable decliners included Schlumberger, Halliburton, Chesapeake Energy, Massey Energy and Transocean. **In light of the dramatic sell-off in commodity related names, many hedge funds are finding these sectors once again attractive and will look to cautiously increase their exposures heading into 2009 as they still believe the longer term supply/demand story remains intact.**

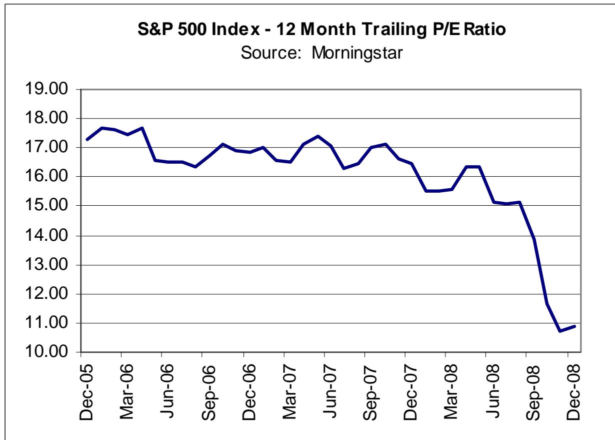
As the long energy, short financial trade came to an end in July and the markets commenced a broad sell-off, many managers sought the safety of defensive sectors such as consumer staples and healthcare. Both sectors generate steadier earnings streams, as they are necessities for consumers and are therefore considered more resistant to recessionary headwinds. **For the year, consumer staples and health care were the two top performing sectors on a relative basis within the S&P 500 Index, declining -17.7% and -24.5%, respectively.** Hedge funds benefited late in 2008 with holdings in several blue chip consumer staple companies, such as Hershey, Kellogg, Campbell Soup, Anheuser-Busch and Colgate-Palmolive. In addition to overweighting blue chip consumer staples, many funds benefited from holdings in discount retailers. As recessionary worries grew, cautious consumers looking for bargains turned to discount retailers which led to earnings surprises and positive revisions for Wal-Mart, Target, BJ's Wholesale Club and other discount retailers. That said, most hedge funds are likely to reduce exposure to consumer staples in the coming months as valuations look expensive on a relative basis. In addition, there are expectations the aggressive actions taken by the government in recent months will begin to alleviate recessionary pressures and result in consumer staples lagging the broad equity markets.

As for healthcare, accelerating M&A activity in the biotech sector during the year, most notably the bid for Genentech by Roche and the bid for Imclone by Bristol-Myers Squibb, served as support for the sector. The share prices of several other large and mid cap biotech stocks also considered acquisition targets benefited from the uptick in M&A activity during the year. Hedge funds continue to favor this sector due in large part to the predictable earnings streams and compelling valuations; most healthcare sectors are currently trading at 10-year low multiples on forward 12-month P/E's. **That said, one particular headwind for the healthcare sector in the short term is the Obama presidency and uncertainty surrounding policy initiatives.**

Along with traditional long/short equity managers, activist investors experienced significant declines in 2008. **While the long bias nature of activist funds certainly hurt performance in the past year, many managers also struggled due to the freezing-up of the credit markets.** Managers were less successful employing typical activist strategies such as encouraging companies to utilize debt to fund stock-buyback plans or increase dividends. The headlines in 2008 were dominated by activist investors struggles to squeeze out value in their companies, most notably Yahoo. While 2008 was a difficult year, the outlook for activist investing looks promising or at least improved. **There are expectations that new rules related to executive-pay and corporate-governance will emerge from Washington in 2009 which will favor activist strategies. In addition, managers will likely look to work with sovereign wealth funds that are now heavily invested in U.S. companies which could provide funds additional leverage when employing certain activist strategies. Lastly, activists will likely look to increase their exposure to distressed assets in 2009 as the opportunity set continues to increase.**

While the monetary and fiscal policies in recent months are expected to bring some stability to the markets over the next six to twelve months, most hedge funds plan to remain cautious given the uncertain times, particularly with regards to

earnings prospects. That said, as they continue to position their portfolios to protect capital, they are also preparing to exploit the opportunity set presented. From a valuation perspective, hedge funds believe the equity markets are looking increasingly attractive with the S&P 500 Index trading at a trailing P/E ratio of 10.7x, down from 15.5x at the beginning of 2008 and below its historical average of 16.0x.



In addition, hedge funds believe that 2009 will present compelling opportunities in individual names for both the long and short sides of their books which could lead to double digit unlevered returns for the year

Arbitrage/Event Driven

(YTD: -18.57% / DEC: +1.00%)

The Hennessee Arbitrage/Event Driven Index finished the year by advancing +1.00% in December, bringing 2008 year-to-date performance to -18.57%, the worst year in history for the index. 2008 was a year of tremendous challenges as the subprime credit collapse quickly spread into a full blown crisis of confidence. A flight to quality and massive deleveraging led to forced selling and liquidations. **In September 2008, fears of a global systemic meltdown caused massive, fevered unwinding of positions, resulting in a spectacular and unprecedented market crash.**

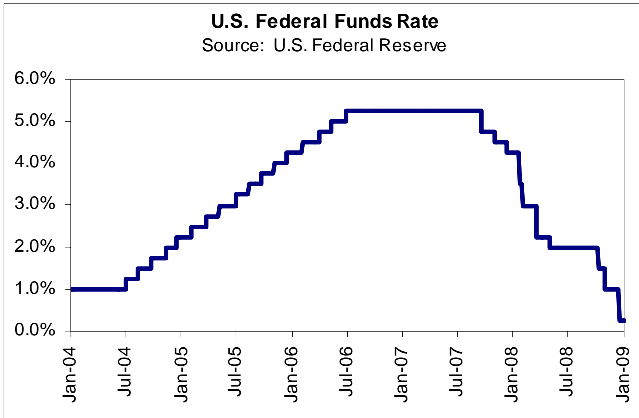
Almost every asset class, with the exception of Treasuries, experienced unprecedented declines in 2008. Crowded trades and investor redemptions further exacerbated risk reduction and forced selling, causing losses for almost all hedge fund strategies. Credit-related, distressed and convertible strategies suffered significant losses as high yield credit spreads exploded, while merger arbitrage funds were able to outperform on a relative basis.

In addition to the typical investment challenges, hedge funds faced several external challenges in 2008, such as the removal of ability to short stocks, utilize normal leverage and operate in the face of mass redemptions. Managers also faced counterparties issues, such as the failure of Bear Stearns and Lehman Brothers, which called into question the security of assets.

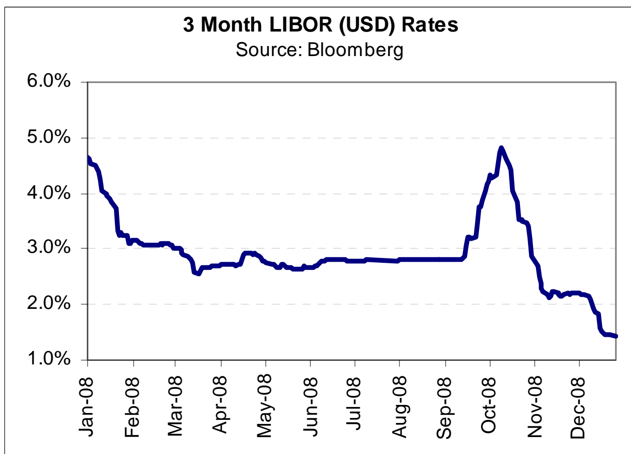
The combination of these factors resulted in a "perfect storm", causing double digit declines for hedge fund strategies, resulting in the industry's worst performance ever. Multiple arbitrage funds declined –16.35% in 2008 (-0.12% in Dec), according to the Hennessee Multiple Arbitrage Index. The second worst performing year would be 1994, when the index was up +3.58%. **However, the carnage of 2008 should create incredible opportunity for surviving hedge fund managers with capital to invest in 2009 and beyond.** Given the severe dislocations in many asset classes, there are many attractive opportunities for hedge fund managers with long-term time horizons. **Hedge fund investors should focus on quality managers who can generate real returns without the use of excessive leverage.** Investors should also focus on less crowded trades and more innovative strategies. Hedge funds will have to adapt to much less availability of leverage, as less is available to market participants. **However, we expect that this will lead to less capital invested and less crowded trades, leading to greater potential rates of return.**

While we maintain an optimistic outlook, it should be noted that there have been a significant amount of hedge funds that have opted to freeze redemption, create sidepockets or further limit the selling of illiquid assets. **This redemption overhang will be worked through in the first half of 2009, and may potentially provide negative pressure on prices. In addition, the discovery of the $50 billion Bernie Madoff fraud may also affect redemptions in the first half of 2009. In addition, these issues have given the hedge fund industry a "black eye" and 2009 will likely bring greater scrutiny by investors and more regulation by the government.**

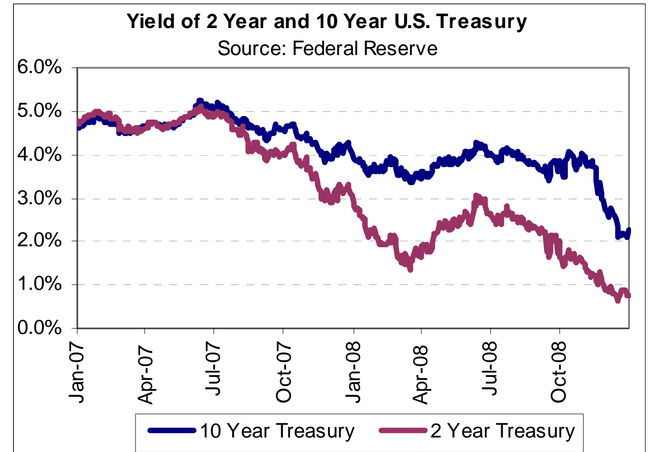
The credit markets experienced dramatic changes in 2008 as a full blown crisis resulted in markets completely freezing. The Federal Reserve and central banks across the globe made concerted efforts to increase lending and thaw credit markets. **The Federal Reserve lowered the Fed Funds rate 10 times since September 2007 by 5.25% to the current range of 0 to 25 basis points.**



The Fed and Treasury committed billions of dollars in attempts to restore order. The government effectively backstopped parts of the short-term markets, increased lending to financial institutions, provided guarantees on bank and finance-company debt, took steps to bring down home mortgage rates and tried to ensure that consumers and lenders have access to capital. Three Month Libor rates skyrocketed in September and October, as banks refused to lend. **Efforts appear to have helped, as the 3 Month Libor Rate has declined; however, credit markets remain impaired and more improvement is needed.**

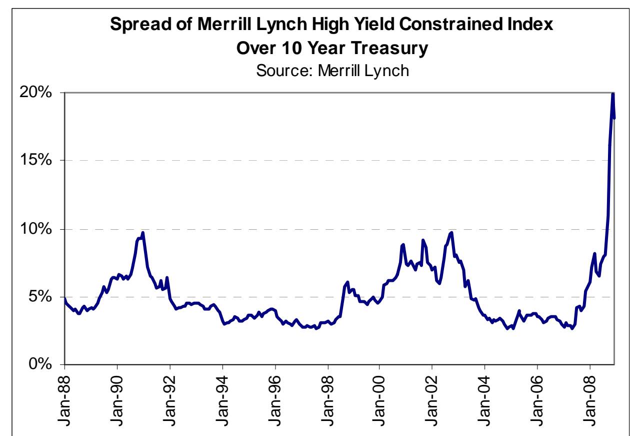


In 2008, investors poured into Treasuries, causing prices to skyrocket and yields to plummet, making these securities by far the best-performing asset class, returning +14% for the year. Yield on the 2 Year Treasury declined from 2.88% to 0.76%, while yield on the 10 Year Treasury declined from 3.91% to 2.25%. Yields on some short term Treasuries actually became negative at one point. **Most investors believe that yields are likely to rise, as current yields are too likely too low to compensate investors, and they will likely move to riskier assets.** In addition, there may be reduced foreign demand as the outlook for long term inflation has increased, which would lead to a weaker dollar.



Outside of Treasuries, all credit securities experienced significant losses. **Investment-grade corporate bonds declined -7% and spreads tripled to 6.00% from the start of the year, according to Merrill Lynch.** Tax-exempt municipal bonds also lost investors -4% in 2008, a historically safe asset class.

The spread on the Merrill Lynch High Yield Index widened by an incredible 1220 basis points during 2008 (the spread on the Merrill Lynch High Yield Index tightened from 1988ps to 1812bps in December, after hitting a new record high of 2182bps mid-month.). The widening of spreads drove declines as junk bonds fell -26% in 2008. Managers state that the price of the average junk bond declined to 61 cents on the dollar from 93 cents.



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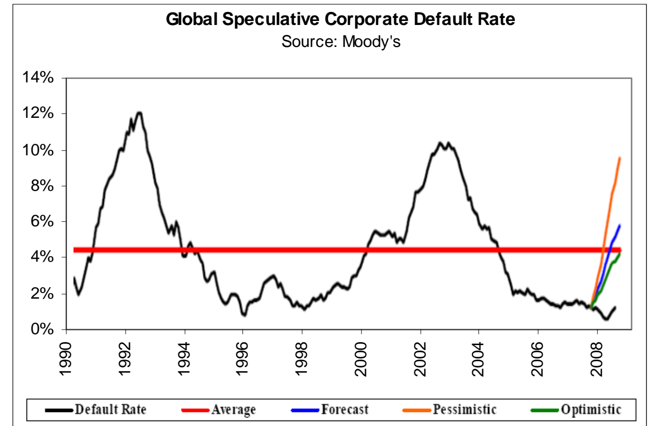
The Hennessee Distressed Index increased +1.27% in December as spreads tightened from extreme levels, but fell -26.30% for the year. In 2008, some managers benefited somewhat from a generally negative view on credit, relatively high cash positions and low exposures. However, the average manager was unable to avoid heavy losses as credit spreads rose sharply and investors were forced to delever.

The current distressed cycle is attributable to lax underwriting standards for many years, leading to an overextension of borrowing. While this applies to the overall credit markets, this was specifically seen in subprime mortgages in 2006, leveraged buyouts in 2007, and in overleveraged financial institutions like Lehman Brothers and Bear Stearns in 2008. In corporate credit, managers report that covenant-lite bank loans and pay-in-kind toggle notes disguised the true health of companies and allowed for the extension of liquidity. **In addition, a huge growth in demand for high-yield products by CDOs, CLOs and other structured products supported huge new issuance.** Leverage continued to build into the system, until it was unsustainable, and conditions dramatically reversed in 2008, resulting in a crash. Current conditions are extremely challenging for leveraged companies. **Demand for credit has essentially disappeared as funds have deleveraged and in some cases liquidated.** Investors with capital remain on the sidelines. In addition, the cost of financing has increased dramatically as spreads have increased. The consumer led recession and tight credit conditions will lead to significant difficulty for companies in need of capital. With funding markets under pressure, bankruptcy protection becomes the most viable option for many companies in 2008.

There were 231 "major" (firms with assets greater than $50 million) bankruptcy filings in 2008, including Lehman Brothers, which filed for bankruptcy in September, becoming the largest bankruptcy in history. There were several bankruptcies by airlines, retailers, financial institutions, casinos, homebuilders, and other economically sensitive companies.

The default rate among speculative-grade bond issuers world-wide, as tracked by Moody's Investors Service, currently remains low at 3.1%; however has tripled since the beginning of the year. **The general consensus is for a sharp rise in default rates. While forecasts range in optimism, most expect for global speculative-grade default rates to reach 4.5% in 2008 and 8% to 10% at the end of 2009.**



Managers are optimistic on the outlook for distressed, however, point out that we are currently in the beginning stage of what may be an unprecedented distressed cycle. **While managers are developing traditional long term distressed strategies, managers state that there are already technical short term investment opportunities due to extreme levels of market volatility, risk aversion, and forced selling of assets creating a significant dislocation.** In the short term (6-12 months), managers report utilizing the following strategies:

Short Credit: Several managers are still short corporate credit via CDS in economically sensitive sectors, expecting companies to face significant distress and possibly bankruptcy.

Long Credit: Several managers have purchased attractive corporate debt which is offering 15% to 20% unlevered returns. Managers are focusing on high quality companies with short duration (1 to 2 years) and expect bonds to realize returns at maturity.

CDS-Bond Basis Trade: Managers report an attractive investment opportunity in historically wide CDS-bond basis – the spread between a cash bond and its matched maturity equivalent CDS. (There is now an estimated $60 trillion in notional CDS outstanding, 20 times the amount at the end of 2002, and 4 times the market cap for the entire U.S. stock market.)

Leveraged Loans: Managers have built positions in leveraged loans, which are often secured by assets of companies. Prices tumbled to less than 70 cents on the dollar, while in normal times they trade close to par, and actually fell below the levels of unsecured bonds at one point.

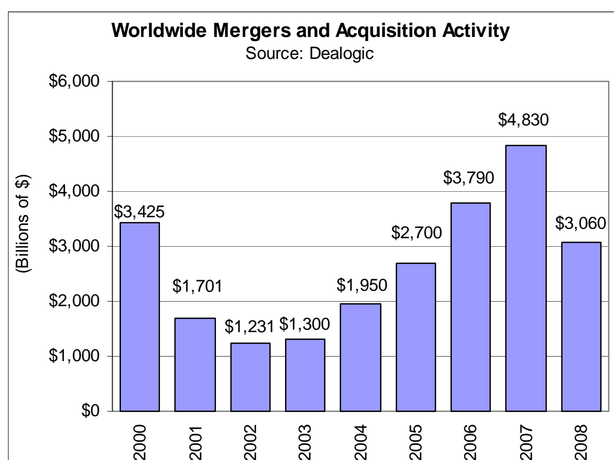
Bank Debt: Managers are buying first lien bank debt as leveraged owners are being forced to sell at discounted levels. Late in the year, first lien bank debt was trading at 40 to 70 cents on the dollar and offering mid- to high-teen unlevered returns, with potential for higher returns.

Subprime and RMBS: Managers believe there are opportunities in subprime loans and residential mortgage backed securities. Mortgage markets imploded in 2006, 2007 and 2008, and are now in a restructuring phase. Managers believe that high quality Triple A subprime and Alt-A RMBS prices are trading at reasonable levels with returns in the low to mid-teens.

Managers are also extremely optimistic on the fundamental outlook for long term distressed opportunities over the next couple years and believe we are on the cusp of an incredible opportunity on the long side. As previously noted, managers expect the number and amount of defaults to accelerate quickly over the next 12 to 18 months. Debtor-in-possession and exit financing will present significant opportunities due to benefits of seniority, downside protection and attractive yields. However, managers remain cautious and selective realizing that assets may get even cheaper.

The Hennessee Merger Arbitrage Index advanced +1.93% in December, bringing year to date returns to -0.87%. Merger arbitrage was one of the best performing strategies for the year, only underperforming Short-Biased and Macro funds. Merger arbitrage managers benefited from a conservative approach, high levels of cash and a focus on strategic deals.

In 2008, global merger and acquisition volume fell -29% to $3.06 trillion, which is a robust year relative to historical averages, but a sharp slowdown versus 2007. Private equity-led buyouts, which accounted for about 15% of 2007 activity, fell to 6% in 2008.



National governments accounted for a big portion of M&A activity, especially in the U.S. The U.S. government rescued Fannie Mae and Freddie Mac in September, as well as AIG later in the year. The Troubled Assets Relief Program (TARP) accounted for $258 billion in deals in the fourth quarter. In addition, the financial services industry was extremely active as several firms were forced into deals in order to stave off bankruptcy, including Bear Stearns, Merrill Lynch, and several others.

Managers generated significant profits in strategic deals, believing that companies would take advantage of depressed valuations to make beneficial acquisitions. There were several key strategic deals and profitable positions completed in 2008, **including the $23 billion acquisition of Wrigley's by Mars, the $52 billion acquisition of Anheuser-Busch by InBev, and the $13 billion acquisition of EDS by Hewlett Packard.**

However, deals were extremely vulnerable as the economy slowed sharply and the credit crunch made borrowing extremely difficult. BHP Billiton's bid for Rio Tinto would have been the largest acquisition ever, but collapsed in 2008. In October, United Technologies dropped its $2.6 billion bid for Diebold and Waste Management dropped its offer for Republic Services. Apollo Management, a private equity firm, paid $1 billion to Huntsman to terminate an acquisition. In recent weeks, several managers took losses as spreads widened on Dow Chemical's acquisition of Rohm & Hass. In the wake of Kuwait's cancellation of a $17.4 billion joint venture with Dow, several questioned the ability of Dow to finance its acquisition of Rohm and Hass at $78-a-share.

Managers remain very concerned that the negative headwinds of 2008 – tight credit conditions, volatile equity markets and deepening global recession – may continue into 2009. Thus, managers are maintaining a cautious position, such as low exposures and significant cash balances. Managers continue to focus on strategic deals as there are well-capitalized companies that can pay cash to acquire assets at a deep discount.

Managers state that it is possible we may see a robust "corporate control" market in 2009 and 2010, similar to 1988, when many companies went on buying sprees with U.S. stock valuations at depressed levels. In addition, most expect the majority of deals in 2009 to be smaller ($500 to $1 billion) and completed out of necessity. Companies will need to merge to remain viable, increase cash flow and pay down debt.

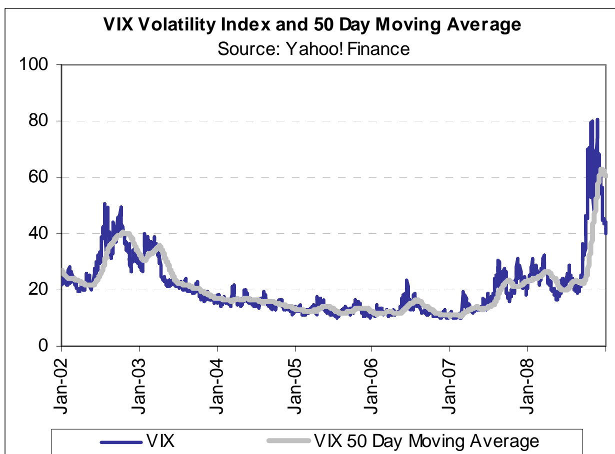
The Hennessee Convertible Arbitrage Index advanced +3.90% (-20.87% YTD) in December, its first monthly advance since May. In December, credit spread tightening, secondary market richening, and declining interest rates made positive contributions to performance. However, **for 2008, convertible arbitrage funds struggled significantly, experiencing their largest annual decline by a wide margin.** For the year, convertible arbitrage funds were negatively affected by:

- Widening of credit spreads (increased +1200 basis points in 2008)
- Decline of stock prices (S&P 500 declined -38.5%)
- Higher cost and availability of leverage

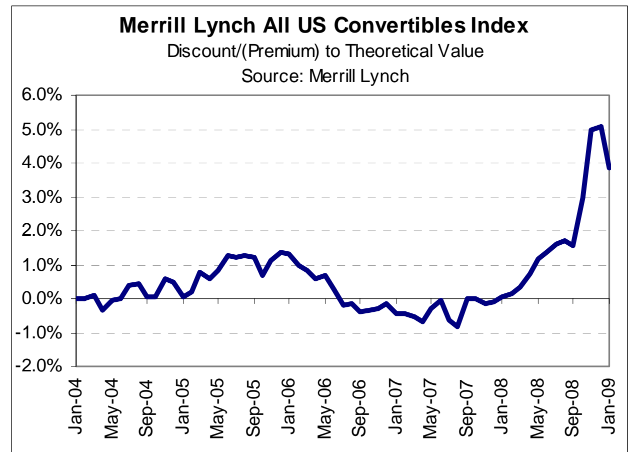
- Deleveraging due to higher borrowing costs and counterparty concerns
- Temporary ban on short selling in September
- Weakness in the financial sector (combined with increased representation by financials)
- A broad-based flight to quality
- Forced selling due to margin calls and mass redemptions
- Illiquid and frozen markets where selling significantly outweighed buying

A tightening of credit spreads made a positive contribution to performance in December. The spread on the Merrill Lynch High Yield Index tightened from 1988 bps to 1812 bps during the month, after hitting a new record high of 2182 bps mid-month. **However, for 2008, the spread on the Merrill Lynch High Yield Index widened by 1220bps, significantly detracting from performance.**

For the year, 90-day average equity volatility spiked from 38.6% to 113.2%, and average call-implied volatility jumped from 47.3% to 77.8%. In 2008, the VIX increased from 22.50 to 40.00, and hit a new record high of 80 in November. While volatility is a positive for the convertible arbitrage strategy, convertible implied volatility lagged listed and realized volatility, reducing its positive effect in 2008. **Managers expect markets to remain volatile for the immediate future, but expect to see a peak in volatility by mid-2009, if not already.**



Average theoretical discount of the All US Convertible VXA0 Index dropped from 5.07% cheap to 3.85% cheap during the month, after hitting a low of 3.28% cheap mid-month. **For the full 2008, the average theoretical discount of the All US Convertible VXA0 Index increased dramatically from 0.07% cheap to 3.85% cheap, after hitting a high of 6.4% in October**.



Interest rates also made a positive contribution to performance. In 2008, the 2-year Treasury yield dropped by 231bps, while the 10-year yield declined by 178bps. However, the positive effect was largely overwhelmed by the many negative factors of 2008.

Convertible arbitrage hedge funds typically utilize leverage to deliver performance. As Lehman Brothers and Bear Stearns failed, the cost of borrowing sharply increased. When combined with poor performance, many funds were not able to maintain leverage, faced margin calls and were forced to liquidate portfolios. In addition to hedge funds, many market makers and proprietary trading desks were forced to deleverage, further exacerbating selling pressure.

Given the significant dislocation of 2008, managers are optimistic on convertibles for 2009. Managers are presently seeing tremendous opportunity in convertible bonds. Managers believe that once selling pressures subside, convertibles could outperform over the next 1 to 2 years. While most managers are bias towards U.S. convertibles, some are also optimistic on Asian convertibles, as they have shorter put dates (1-3 years) and higher yields (20-50%).

Managers report that technicals of the convertible market started to improve in December, for the first time since mid 2007, as the convertible space had more buyers than sellers. This is largely due to the emergence of new, large buyers who are non-traditional. In addition, there were companies buying back convertible issues and incenting holders to convert early. Several firms have announced plans to launch dedicated convert funds in recent weeks, some in a long only format. **However, managers remained concerned about redemptions given several funds freezing redemptions and imposing gates. Once selling pressure subsides, managers can stop worrying about liquidity and can refocus on identifying arbitrage opportunities.**

While 2008 has been traumatic for investors across the globe, the resulting environment is likely to produce "once in a lifetime" opportunities for investors who remain committed and who have capital to invest. The combination of forced sellers, risk aversion, and limited access to leverage has led to a significant supply and demand imbalance.

While significant headwinds remain, such as a global economic slowdown, impaired credit markets, and changes to the hedge fund industry, hedge funds should continue to outperform on a risk-adjusted basis and should generate strong returns in 2009.

Global/Macro

(YTD: -20.72% / DEC: +0.61%)

The Hennessee Global/Macro Index increased +0.61% in December (-20.72% YTD). The index finished the year down significantly, amid a turbulent trading environment and an aversion to risk depicted by an investor flight to quality. Risk aversion showed peaks in 2008, with the TED spread and the Libor-OIS spread reaching all-time highs in September, two key measurements of risk sentiment. **Managers were left with little place to hide as US Treasuries and gold were the two of the few profitable asset classes in 2008.**

Global Interest Rates 2007 to Current (As of 12/31/08)

	Rate Cuts (bps)	2007 Year End Rate	2008 Year End Rate
G7 Average	-245	3.70%	1.25%
US	-400	4.25%	0.25%
ECB	-150	4.00%	2.50%
BOE	-350	5.50%	2.00%
China	-275	4.25%	1.50%
Japan	-40	0.50%	0.10%
Australia	-250	6.75%	4.25%
Canada	-275	4.25%	1.50%
Switzerland	-225	2.75%	0.50%
Russia	+300	10.00%	13.00%
Brazil	+250	11.25%	13.75%

The global equities market finished the year substantially down, with the MSCI EAFE declining -45.09%, but ending the year with a December rally of +5.92%. **Despite the large global coordinated effort to increase liquidity, including worldwide rate cuts and large stimulus packages, every major equity market finished the year with negative returns.** The December rally implies that investors have better hopes for the new year, as valuations are considered extremely low and government policies have injected massive amounts of money into the markets.

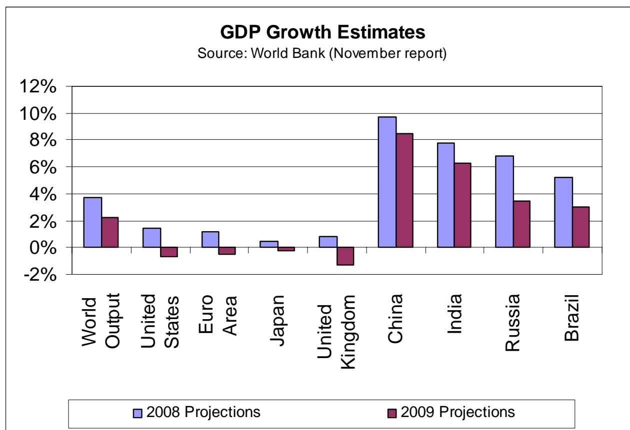
For the first three quarters, investors were focused on a global spike in inflation, due to rising commodity prices. As the credit crisis spread from the US to global economies, inflation fears switched to concerns of a global financial system meltdown and declining global growth. Global growth is expected to be 1% in 2009, down from 3% in 2008 and 4.1% in 2007. Inflation data estimates show an expected decrease from 4.8% in 2008 to 2.0% in 2009, according to Barclays Capital. Unemployment hit new highs in many regions. **In the new year, managers believe that the international economies are still risky investments considering the end of year drop in commodity prices and continued flight to quality. They do, however, see long-term opportunities for future gain and growth, as valuations are at extreme lows.**

Managers in Europe saw increases in December, with the Hennessee Europe Index finishing the month -1.05% but finished the year down -18.95%. European countries saw positive returns in December, with the MSCI Europe Index finishing up +5.18% for the month, but lost -48.20 for 2008%. **A general consensus among managers shows that many believe the European governments took too long in initiating rate cuts, spurring further downturns.** In addition, the short ban initiated in many countries, and active until January 16 in England, had a negative impact on many investors, as it hampered the ability of hedge funds to function normally. Managers believe that the removal of the short ban will cause a further decrease in European equities.

To spur growth in Europe, the government has been forced to enact rapid rate cuts (cutting 175bps from October to December) and large stimulus packages. Inflation estimates have plummeted from 3.3% at 2008 year end to 1.1% in 2009. The EU approved a rescue plan that makes cash injections and loan guarantees available to lenders and a $672 billion bank stimulus package approved in Germany in December. Despite stimulus, GDP estimates have been decreased from .9% in 2008 to -1.3% in 2009. **While valuations are at new lows, investors will be weary to jump back into the market too early, despite the optimistic view over recent government stimulus packages.** In the long term, managers are seeing very attractive opportunities in Europe, with P/E ratios now at 7x, close to historical lows.

The failure of developed countries to avoid recession has taken a toll on Asian nations, proving that they are not de-coupled from U.S. and other developed countries. The MSCI Asia Pacific ex Japan Index finished the year down -53.30%. A reduction in exports caused equity markets to plummet, hurting managers throughout the region. With developing nations experiencing declines in unemployment and investor confidence, demand for goods declined and Chinese economy was dramatically hurt. The Baltic Dry Index reached all time lows in 2008, implying

that trade across the globe had dramatically declined. Without the benefit of fast growing China, other Asian nations were not far behind in the decline. Equity markets experienced declines in China as growth estimates were revised down to 9.7% for 2008 and 8.5% for 2009 (as of November 31), and Asian countries as a whole expect growth rates in 2008 and 2009 of 5.4% and 3.6%, respectively. **While growth is set to slow, many managers are still optimistic towards Asia as a whole, particularly China, as growth is still positive.**



Also hurt by decreased trade and slowing growth was Japan, with the Nikkei tumbling -42% in 2008. The decline of the auto industry in 2008 was detrimental to Japan, as auto exports are one of the primary economic drivers. Furthermore, an increase in the strength of the yen caused a decrease in world trade. Japan reduced its already low rate of .5% down to .1%. These already very low interest rates and high levels of public debt will make it hard for Japan to further increase liquidity, which may prove necessary, in 2009. Economists are expecting a sharp decline in inflation, and expect growth to decline for the next four quarters.

Emerging markets were hit hard by the decrease in demand for commodities, and slowing exports to developed countries. The MSCI EM finished the year down -54.48%, despite a return of +7.60% in December. Hedge funds also saw decreases, with the Hennessee Emerging Markets Index dropping -30.01% in 2008 and seeing minimal gains of +0.05% in December. There was a large sell off in emerging market equities, as investors became more risk averse. Due to both geopolitical tensions with Georgia and their heavy reliance on energy exports, Russia finished December down -7.83% (-74.16% YTD), one of the worst performing countries. Managers remain cautious on Emerging Markets, but also see opportunities in 2009. **From a long-term standpoint, P/Es are at 7.0x trailing earnings, which is valued at 40% of average. With developed countries in a recession, Emerging Markets may account for a substantial amount of growth in the future.** Furthermore, managers believe that exports are becoming less important, as domestic demand is on the rise.

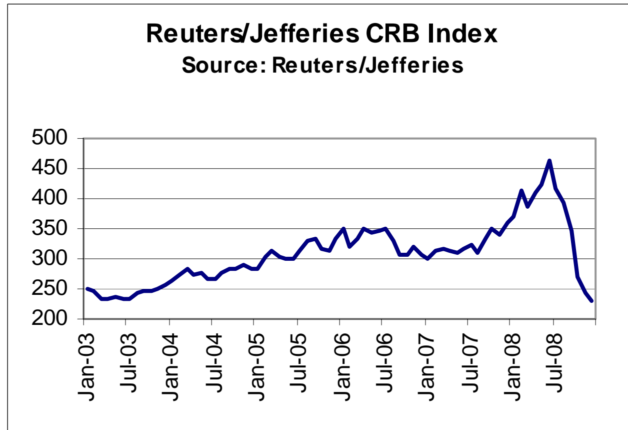
Latin American markets were some of the worst performers of 2009 with the Hennessee Latin American Index down -27.48% for the year, but showing returns of +2.76% in December. After several years of strong performance and a source of major growth throughout the world, Latin America was among the worst of the Hennessee Indices, only behind Emerging Markets. The deterioration of developed nations crippled these nations this year, due to decreased trade and currency volatility. Managers are predicting severely slowed growth in Latin America. The GDP is forecasted to be 0.9%, down from 5.8% in 2008. **The investor flight to quality drew substantial capital from Latin America, which leaves the country with little monetary backing for government stimulus.** The financial systems here are underdeveloped, and therefore monetary easing will be overshadowed by the dysfunctional financial markets. **In the short term, managers believe that returns are likely to be bleak and recovery is dependent upon the effect of stimulus packages in the US and other developed countries.** Like other Emerging Markets, managers see low valuations and are optimistic that profits are possible when the economy returns to more normal conditions.

Macro managers saw profitable returns with the Hennessee Macro Index returning +2.06% in December, and (+3.37% YTD). **The most profitable trades for managers, over the year, came from currency trades, commodities and yields.**

Commodities in 2008 showed a dramatic boom-to-bust cycle, with prices soaring to start the year, and seemingly having no floor towards year-end. With the epic failure of Bear Stearns, commodities, (especially gold) gained favor among investors, seen as an asset that could help portfolios weather the financial storm. With fears of an energy crisis at hand, oil prices soared to new highs in July, reaching $145.29 a barrel. As the economy deteriorated, unemployment rose and consumer spending declined, oil plummeted, hitting a low of $33.87 a barrel in mid December.

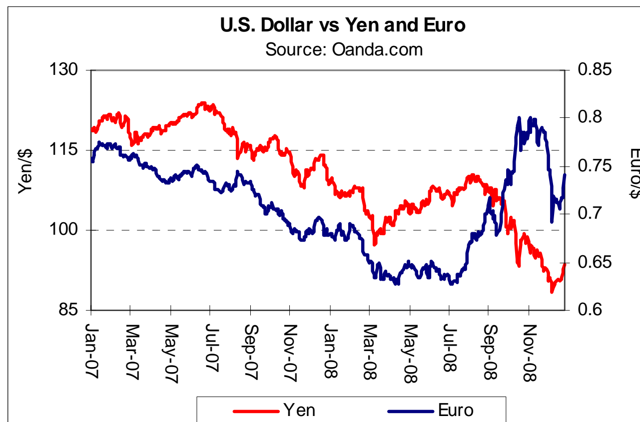
Coal started off the year with dramatic increases, peaking at $132 in July, but with the energy sectors in decline, they finished the year slightly above $62. **With the tightening credit markets and investor risk aversion, managers began to liquidate positions in commodities, as traders became scarce, deleveraging became popular and capital became king.** Managers are maintaining share positions in coal, with reduced exposures, and anticipate an increase in

energy over the next year. For 2009, managers have a bleak outlook, based upon fears of fewer traders, continued tighter markets and the headwind of global recession.



Managers who invested in gold generated gains, as gold finished 5.8% higher in 2008, showing an increase for the 5th year in a row. Investors flocked to gold, which is considered a safe haven among investments. Most financial institutions predict that gold will continue to rise, as demand is fairly inelastic, but production is decreasing. Furthermore, as gold is tied to currency, the volatility in the currency market leaves gold as an attractive alternative.

Currency markets saw an active year, characterized by the falling pound and raising yen. Managers early in the year saw profits from the yen carry-trade, where investors sold the yen at low interest rates in order to fund riskier high-yield assets. **The yen saw a surge late in the year, as managers opted away from risky assets, and bought back the yen. Over the year, the yen surged by 19% over the dollar, 22% against the euro 40% over the pound.**



The pound did not fare so well over the year, with investors worried about ailing financial markets, rising unemployment in Britain and late year interest rate cuts. Managers remain skeptical on the strength of the pound, and some are even going so far as to predict that the euro will surpass the pound by the end of 2009.

The dollar had a turbulent year, with a decrease against the euro in the first two quarters, then a surge beginning in July. **The dollar benefited amid a flight to safety and global deleveraging.** Managers saw gains as many predicted this shift mid year. December showed a decline in the dollar, falling 12% against the euro, as the Fed cut interest rates to between 0.00% and 0.25%. Over the year, however, the dollar has seen a 3.7% gain against the euro, 34% against the South Korean won, and a 37% climb against the South African rand. In addition, the Russian rouble dropped 25% against the dollar, the Brazilian real lost 31% and the Indian rupee fell 23%.

Investors, in 2008, saw treasury yields decrease substantial amounts, due to a massive flight to quality. The benchmark 10-year yield ended at 2.22% after beginning 2008 at 3.91%. More over, the 30-year bond yield ended at 2.67%, just above the 10-year, but opened 2008 at 4.35%. Most telling, however is the 3-month yield, which ended 2009 at 0.12%, down from 3.26% at the end of 2007. Considered a gauge of investor confidence, yields dipped below zero twice in 2008.

These historically low three month yields indicate that investors preferred a safe haven for their money, and were not looking to preserve cash, not seek alphas. There was an increase in the 3 month yield at the end of December, showing that some investor confidence is returning. Managers feel that Treasuries are over bought, and will decrease in value in the new year, leaving room for more risky investment. For 2009, many managers are predicting that yield curves will steepen. **The treasury yields are too low, according to investors and an expected common theme for 2009 will be the shorting of US treasuries.**

Managers remain cautious as we start 2009. Macro managers had a successful 2008, generating modest profits. Managers key themes for 2009 include a increase in Treasury yields, a tightening of high yield credit spreads, and a long-term bullish outlook on gold and inflation.

HENNESSEE HEDGE HOG CORNER

The following are extracts from research related to hedge fund managers we monitor and do not necessarily represent the views of the Hennessee Group LLC:

We believe the markets are forward looking and may start to discount an economic recovery in 2010 even if analyst estimates continue to be ratcheted down.

We think the odds of a depression, with prolonged deflation similar at worst to the 1930s, are low. There is a good chance that the November lows were the bottom of this bear market in stocks.

We feel that the best returns in 2009 will be credit strategies, as high yield credit spreads are likely to tighten from historical highs.

We expect to slowly build up exposures over the next couple months as the markets continue to respond to fundamentals and as there are no more financial disasters that are announced.

Oil is oversold in our view. Excellent long term opportunities also exist in the Material, Industrial, and Healthcare. We are not particularly excited about consumer staple stocks.

We plan on looking more at corporate debt securities especially in cases where there is a solid underlying business worth more than the underlying debt and corporate management is intent on reducing overall leverage which should benefit the debt holders.

Busted convertibles have become absolutely and incredibly attractive as the magnitude of the cheapness is so great that neither lack of leverage nor cost of leverage has a material impact on the expected returns.

With the direction of equities and the availability of credit uncertain, **any security that is vulnerable to stock exposure or to a dependency on refinancing debt is extraordinarily risky** and, in our view, largely fairly priced.

We believe that the real economic impact of such fiscal policies will be muted, much the same as the monetary stimulus of the past four months, as the velocity of money has slowed substantially and banks continue to be extremely stubborn in their lending practices.

We remain extremely focused on the health of corporate and sovereign credit, which will continue to have a dramatic impact on equity values.

In just a few short months we had gone from worrying about whether there was enough of any of these commodities to whether there would be enough demand to use the existing supply.

We see lots of opportunities in the corporate and high yield market to make equity type returns and we have been focusing a lot of our attention here.

We are short Treasuries. I think that is probably the most common trade out there right now.

We are reducing merger arbitrage exposure as it is really difficult to get deals done. We expect for some activity in 2009 as companies with cash by discounted assets, but we don't expect premiums to be high.

We are looking at financials, as they will need to rebound in order for the overall market to rebound. We are actually looking at buying some banks as the interest rate environment looks attractive once lending resumes.

We have increased convertible arbitrage exposure. We feel there should be a retrace of some losses simply due to any liquidity reentering the market. We saw this a little bit in December but expect it to continue.

We think one of the major challenges in 2008 was the U.S. government's unpredictable policies. We think that the government has learned from its mistakes and expect less radical changes in 2009.

We are long energy independence/alternatives, such as nuclear and wind. The new administration will make investments in this sector.

We are concerned that the Madoff related losses may lead to another round of heavy hedge fund redemptions in the first quarter of 2009.

We expect to see a push for greater hedge fund regulation and transparency in 2009.

We are very happy that 2008 is over.

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HENNESSEE HEDGE FUND RANKINGS

MONTHLY RANK 2007 (Net)	YTD	JAN	FEB	MAR	APRIL	MAY	JUNE	JULY	AUG	SEPT	OCT	NOV	DEC
ASIA - PACIFIC INDEX	19	22	9	20	9	21	22	17	21	8	12	10	18
CONVERTIBLE ARBITRAGE INDEX	15	3	20	14	18	18	9	13	10	21	21	18	1
DISTRESSED INDEX	21	13	18	7	14	11	14	21	13	17	19	23	8
EMERGING MARKETS INDEX	23	15	3	18	16	13	17	22	23	18	22	20	15
EUROPE INDEX	13	17	4	10	11	6	12	19	11	13	16	9	23
EVENT DRIVEN INDEX	18	14	15	13	13	10	16	16	2	22	17	14	21
FINANCIAL EQUITIES INDEX	8	5	11	23	22	22	23	2	5	16	3	3	5
FIXED INCOME INDEX	6	4	23	6	5	9	8	4	3	4	6	5	10
GROWTH INDEX	16	21	17	17	4	1	10	20	18	15	13	16	14
HEALTHCARE AND BIOTECH INDEX	9	20	19	22	7	7	6	1	15	12	9	8	20
HIGH YIELD INDEX	12	7	21	4	10	14	7	7	12	14	18	13	9
INTERNATIONAL INDEX	17	18	6	21	6	16	19	23	16	20	15	11	3
LATIN AMERICA INDEX	22	11	1	19	3	3	15	6	22	23	23	15	11
MACRO INDEX	2	2	5	12	12	15	3	11	20	2	2	2	4
MARKET NEUTRAL INDEX	5	9	8	8	21	19	2	14	14	10	5	7	6
MERGER ARBITRAGE INDEX	3	8	10	3	15	17	13	3	1	3	4	4	7
MULTIPLE ARBITRAGE INDEX	11	6	13	11	19	8	5	10	7	11	14	12	17
OPPORTUNISTIC INDEX	7	12	7	9	17	2	4	18	17	7	11	17	12
PIPES/PRIVATE FINANCING INDEX	10	10	12	5	20	20	11	12	9	5	8	21	16
SHORT BIASED INDEX	1	1	2	1	23	23	1	5	19	1	1	1	22
TECHNOLOGY INDEX	14	23	22	2	2	12	18	9	8	9	10	19	19
TELECOM AND MEDIA INDEX	4	19	14	16	1	5	20	8	4	6	7	6	2
VALUE INDEX	20	16	16	15	8	4	21	15	6	19	20	22	13

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HENNESSEE GROUP LLC
HEDGE FUND ADVISORY

HENNESSEE HEDGE FUND INDICES®

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2007 (Net)	YTD	YTD RANK	% of mgrs. >S&P, ytd	JAN	FEB	MAR	APRIL	MAY	JUNE	JULY	AUG	SEPT	OCT	NOV	DEC
ASIA - PACIFIC INDEX	**-24.54%**	**19**		-5.00%	1.11%	-3.30%	1.78%	0.51%	-4.03%	-2.30%	-2.79%	-5.34%	-5.77%	-2.14%	-0.17%
CONVERTIBLE ARBITRAGE INDEX	**-20.87%**	**15**		0.21%	-0.25%	-2.36%	1.16%	1.32%	-0.54%	-1.68%	-0.53%	-8.78%	-10.58%	-4.03%	3.90%
DISTRESSED INDEX	**-26.30%**	**21**		-2.77%	0.06%	-1.30%	1.38%	1.72%	-1.69%	-2.65%	-0.87%	-7.79%	-9.47%	-7.19%	1.27%
EMERGING MARKETS INDEX	**-30.01%**	**23**		-3.35%	2.70%	-2.78%	1.31%	1.59%	-2.68%	-3.17%	-3.47%	-7.91%	-11.87%	-4.60%	0.05%
EUROPE INDEX	**-18.95%**	**13**		-3.67%	2.68%	-1.74%	1.68%	2.22%	-0.91%	-2.48%	-0.54%	-6.97%	-7.62%	-1.82%	-1.05%
EVENT DRIVEN INDEX	**-24.29%**	**18**		-3.11%	0.58%	-2.11%	1.41%	1.74%	-2.40%	-2.23%	0.90%	-8.99%	-8.32%	-3.68%	-0.60%
FINANCIAL EQUITIES INDEX	**-14.99%**	**8**		-0.84%	1.02%	-5.14%	-1.19%	0.50%	-4.51%	0.42%	0.42%	-7.42%	-1.71%	0.80%	2.00%
FIXED INCOME INDEX	**-9.72%**	**6**		-0.83%	-5.63%	-1.15%	2.81%	1.84%	-0.49%	-0.12%	0.57%	-4.11%	-3.02%	-0.28%	0.56%
GROWTH INDEX	**-20.89%**	**16**		-4.92%	0.39%	-2.71%	2.87%	3.78%	-0.59%	-2.58%	-1.42%	-7.33%	-6.36%	-3.85%	0.18%
HEALTHCARE AND BIOTECH IN-	**-15.38%**	**9**		-4.53%	-0.12%	-3.56%	2.61%	1.90%	0.01%	2.56%	-1.17%	-6.89%	-4.66%	-1.76%	-0.46%
HIGH YIELD INDEX	**-18.82%**	**12**		-1.49%	-0.35%	-0.88%	1.77%	1.51%	-0.40%	-1.19%	-0.60%	-6.98%	-8.99%	-3.45%	1.01%
INTERNATIONAL INDEX	**-21.78%**	**17**		-4.00%	2.42%	-3.32%	2.65%	1.48%	-3.00%	-3.39%	-1.17%	-8.32%	-7.37%	-2.25%	2.76%
LATIN AMERICA INDEX	**-27.48%**	**22**		-1.98%	3.51%	-2.82%	3.52%	2.88%	-1.70%	-1.09%	-3.33%	-11.34%	-14.35%	-3.72%	0.49%
MACRO INDEX	**3.37%**	**2**		1.21%	2.43%	-2.07%	1.55%	1.49%	1.00%	-1.42%	-2.55%	-2.16%	-0.21%	2.20%	2.06%
MARKET NEUTRAL INDEX	**-8.53%**	**5**		-1.83%	1.28%	-1.38%	-0.37%	1.06%	2.53%	-1.83%	-0.95%	-6.44%	-1.83%	-0.75%	1.95%
MERGER ARBITRAGE INDEX	**-0.87%**	**3**		-1.60%	1.04%	-0.79%	1.34%	1.47%	-1.21%	0.20%	1.20%	-3.08%	-1.80%	0.56%	1.93%
MULTIPLE ARBITRAGE INDEX	**-16.35%**	**11**		-1.32%	0.88%	-1.98%	0.73%	1.89%	0.01%	-1.42%	0.03%	-6.84%	-6.50%	-2.66%	-0.12%
OPPORTUNISTIC INDEX	**-14.67%**	**7**		-2.58%	1.69%	-1.40%	1.27%	3.27%	0.14%	-2.35%	-1.23%	-5.28%	-5.37%	-3.95%	0.48%
PIPES/PRIVATE FINANCING INDEX	**-15.85%**	**10**		-1.94%	0.95%	-1.01%	0.49%	0.83%	-0.85%	-1.59%	-0.10%	-4.64%	-4.18%	-4.84%	0.00%
SHORT BIASED INDEX	**26.31%**	**1**		4.71%	3.13%	1.27%	-3.20%	-1.47%	7.13%	-0.39%	-1.79%	3.05%	9.21%	3.64%	-0.93%
TECHNOLOGY INDEX	**-19.68%**	**14**		-6.64%	-0.63%	0.32%	3.92%	1.70%	-2.92%	-1.32%	0.00%	-6.00%	-4.87%	-4.37%	-0.33%
TELECOM AND MEDIA INDEX	**-7.77%**	**4**		-4.42%	0.76%	-2.41%	5.48%	2.40%	-3.61%	-1.30%	0.52%	-4.84%	-3.31%	-0.52%	3.80%
VALUE INDEX	**-26.06%**	**20**		-3.67%	0.44%	-2.38%	2.49%	2.86%	-3.70%	-2.05%	0.24%	-8.20%	-10.23%	-5.06%	0.39%
HENNESSEE HEDGE FUND INDEX	**-19.15%**		**87%**	**-2.92%**	**0.75%**	**-2.11%**	**1.80%**	**1.98%**	**-1.43%**	**-1.81%**	**-0.88%**	**-6.80%**	**-6.67%**	**-3.02%**	**0.51%**
LONG/SHORT EQUITY	**-18.34%**			**-3.61%**	**0.61%**	**-2.15%**	**1.98%**	**2.42%**	**-1.43%**	**-1.48%**	**-0.56%**	**-6.67%**	**-5.81%**	**-3.25%**	**0.31%**
ARBITRAGE/EVENT DRIVEN	**-18.57%**			**-1.67%**	**-0.30%**	**-1.58%**	**1.39%**	**1.60%**	**-1.04%**	**-1.52%**	**0.02%**	**-6.83%**	**-7.33%**	**-3.61%**	**1.00%**
GLOBAL/MACRO	**-20.72%**			**-3.25%**	**2.19%**	**-2.75%**	**1.89%**	**1.44%**	**-2.25%**	**-2.39%**	**-2.37%**	**-6.52%**	**-7.17%**	**-1.90%**	**0.61%**
DJIA	**-33.84%**			-4.63%	-3.04%	-0.03%	4.54%	-1.42%	-10.19%	0.25%	1.45%	-6.00%	-14.06%	-5.32%	-0.60%
LEHMAN AGG. BOND INDEX	**5.24%**			1.68%	0.14%	0.34%	-0.21%	-0.73%	-0.08%	-0.08%	0.95%	-1.34%	-2.36%	3.30%	3.73%
MSCI EAFE (USD) PRICE INDEX	**-45.09%**			-9.29%	1.27%	-1.52%	4.95%	0.28%	-8.31%	-3.28%	-4.29%	-14.71%	-20.24%	-5.70%	5.92%
NASDAQ	**-40.54%**			-9.89%	-4.95%	0.34%	5.87%	4.55%	-9.10%	1.42%	1.80%	-11.64%	-17.73%	-10.77%	-2.70%
RUSSELL 2000	**-33.79%**			-6.88%	-3.80%	0.26%	4.10%	4.48%	-7.83%	3.61%	3.50%	-8.10%	-20.90%	-11.98%	5.80%
S&P 500	**-38.49%**			-6.12%	-3.48%	-0.60%	4.75%	1.07%	-8.60%	-0.99%	1.22%	-9.08%	-16.94%	-7.48%	0.78%

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