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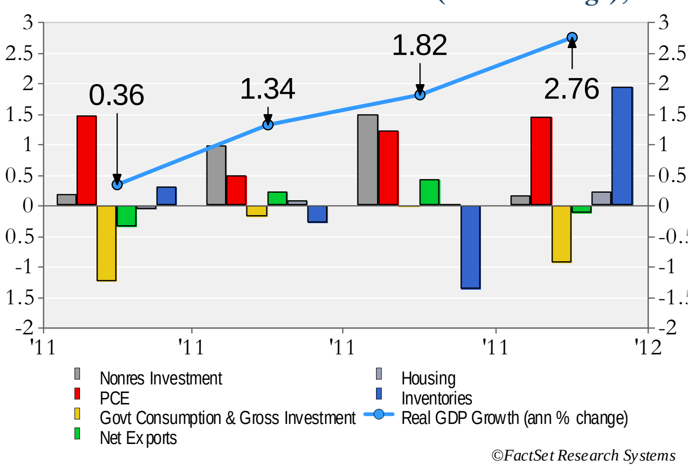
Market Review

January 2012

Economic Review

U.S. real GDP grew at an annual rate of 2.8% in the final quarter of 2011, according to the advance estimate released by the Bureau of Economic Analysis. This was the fastest pace in the last five quarters although it was slightly lower than the consensus estimate of 3%. The acceleration in GDP was primarily boosted by the rebuilding of business inventories (blue bar in the chart below) and growth in personal consumption expenditure (red bar), contributing 1.94 and 1.45 percentage points respectively. The growth was partially offset by a decrease in federal and state government spending and on acceleration in imports. Real final sales (GDP less inventories) rose 0.8%, the slowest pace since the first quarter and significantly below the consensus of 2.5%, indicating poor demand during the holiday quarter.

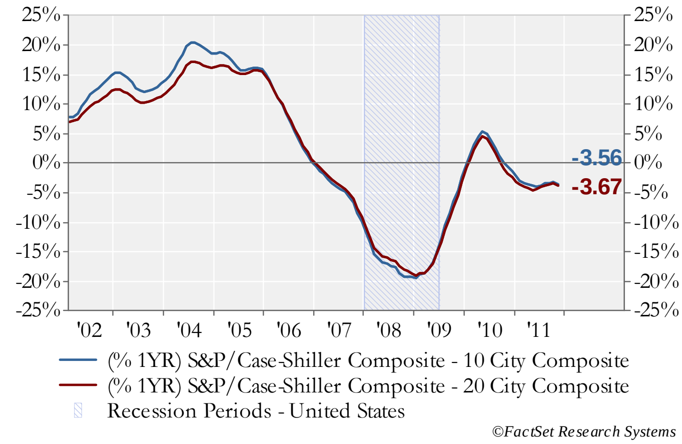
Contribution to Real GDP Growth (ann % change),%



The economy added 243,000 jobs in January (on a seasonally adjusted basis) according to the Bureau of Labor Statistics (BLS). Total jobs before seasonal adjustment fell by 2,689,000. BLS had estimated the seasonal decline to be 2,932,000. The difference between the two numbers was reported as an increase in employment. The unemployment rate beat expectations and fell for the fifth straight month, down to 8.3%. This is the lowest rate in nearly three years. The labor participation rate fell to 63.7%, the weakest reading since May 1983, while the employment/population ratio remained subdued at 58.5%.

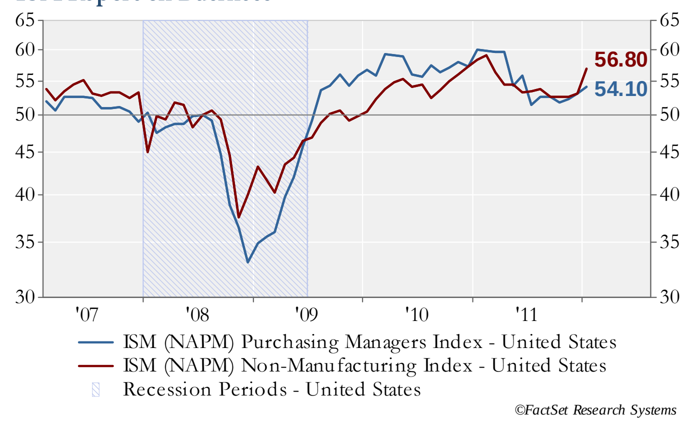
Home prices continue to drop according to the S&P Case Shiller Index data through November, in spite of record low mortgage interest rates. The Case-Shiller 10 and 20 City Indices dropped 3.6% and 3.7% respectively from a year ago. U.S. housing starts dropped 4.1% from November to December primarily due to a 20.4% drop in the volatile multifamily sector. However, single family starts increased 4.4% in that month. December existing home sales rose 5%, a third consecutive monthly increase. New home sales dipped 2.2%, making 2011 the worst on record since 1963.

S&P/Case-Shiller Home Price Indices



The Institute of Supply Management (ISM) Non-Manufacturing Index climbed to an eleven month high of 56.8 in January, up from a revised 53 in December. The ISM Manufacturing Index rose to 54.1, the fastest pace in seven month as new orders, production and employment improved. A value above 50 indicates an expansion.

ISM Report on Business



Retail sales increased 0.1% in December and are up 6.5% versus a year ago. Consumer spending was flat, while personal income increased by 0.5%. Personal savings came in at 4% in December, up from 3.5% in November. The December headline CPI remained unchanged while the core CPI increased 0.1% month over month. The headline CPI is up 3% year over year, while the core CPI held steady at 2.2%.

The Federal Reserve Open Market Committee extended their current zero interest rate policy through late 2014, citing a weak outlook. Chairman Bernanke also signaled a possible QE3, if the economy does not continue to improve.

The imminent credit crunch in the Eurozone has seemingly been put off for a little while as investors realized the European Central Bank's long term refinancing operation (LTRO) as essentially a backdoor Quantitative Easing. Fitch downgraded the debt of six Eurozone countries, while S&P downgraded European Financial Stability Fund and the debt of nine Eurozone sovereign countries including France, Austria, Italy and Spain. The downgrades seem to have had little impact, as subsequent Italian, Spanish and French debt issues were well received indicating that the market may already have priced a wide round of rating cuts. The markets remain focused on Greek debt negotiations with bondholders, but no agreement had been reached by the month end. The 10-year Portuguese yields crossed 16%, the highest since the Euro was formed. The International Monetary Fund announced plans to bolster its lending resources by $500 billion as it prepared to cut its forecast of global growth.

The UK & Germany economies contracted by 0.2% and 0.25% respectively during the final quarter of 2011. The unemployment level in the Euro area remained steady at a high 10.4%.

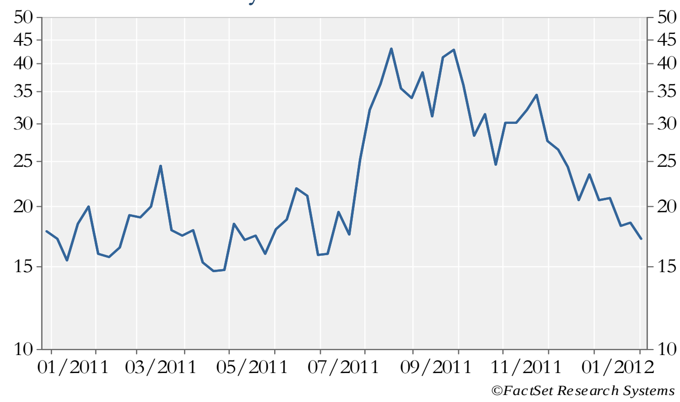
Global manufacturing activity picked up in January. Chinese PMI increased to 50.3, defying expectations that its output would contract. German manufacturing expanded for the first time in four months, growing to 51 in January. Chinese real GDP beat expectations coming in at 8.9% during the fourth quarter of 2011.

Equity Markets

Global equity markets got off to a flying start in 2012, posting strong gains as Eurozone fears abated due to an infusion of liquidity by the ECB, the Fed's announcement of a prolonged period of low interest rates and better than expected economic data. The S&P 500 returned 4.5%, the best January returns since 1997. Reflecting the increased risk appetite, cyclical stocks significantly outperformed the more defensive sectors that led in 2011. The month's best performing stocks were among the worst performing stocks during 2011. The technology-oriented Nasdaq Composite Index gained 8.06%. International markets, especially emerging markets, made a strong come back. Market volatility, as measured by VIX Index, stayed well under the 2011 average of 24 closing at 19.44.

U.S. markets advanced during the first week of January reflecting the upbeat U.S. labor data. The equity markets marginally extended their gains during the second week on mixed economic data and renewed concerns about European Debt Crisis. However, lowered borrowing costs in Europe, satisfactory early fourth quarter earnings and a rise in home builder confidence helped boost equity returns during the third week. Risk appetite abated slightly towards the end of the month as the Feds announcement of low rates through 2014 was countered by lower than expected GDP growth and weak new home sales.

CBOE VIX Volatility Index



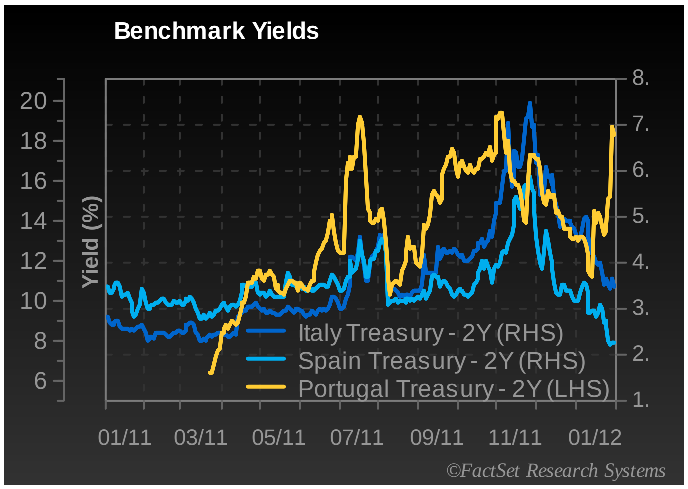
Measured in US Dollars, the MSCI World Index gained 5.05% in January, erasing its loss for 2011. The MSCI EAFE Index climbed 5.35%. The MSCI Emerging Markets recorded 11.36% gains. Measured in their local currencies, the FTSE 100 and STOXX 600 indices gained 2.05% and 4.16% respectively in January.

Bond Markets

The U.S. bond market, as measured by the Barclays Capital U.S. Aggregate Index, added 0.88% in January. Corporate Credit and High Yield outperformed Treasury as investor appetite increased primarily due to improved liquidity in the European banking market. The BofA Merrill Lynch US High Yield gained 2.9%, while Barclays Capital U.S. Aggregate Government Treasury Index returned 0.42% in January.

For the month, 10-year Treasury yields declined 8 basis points and the 2-10 year Treasury curve flattened 5 bps as the Fed committed to keep the front end rates anchored. The 30-year Treasury yield widened 5 basis points. The 10-year and 30-year Treasury yields closed at 1.8% and 2.94% for the month. Corporate and high yield debt spreads narrowed 19 and 113 bps during January, according to Markit CDX indices.

The ECB's liquidity injections seems to have reduced the short term risk in Europe as evident by significant improvement in Italian and Spanish short term yields since the inception of LTRO. However, the two year Portuguese debt widened 510 bps in January, as investors worried if it could be the next Greece.



The UK 10 Year GILT yield was flat and closed at 1.97% in January. The German 10 Year Bunds decreased 5 bps to close at 1.79%.

Currency

The US Dollar Index, used to track the US Dollar against a basket of six currencies, decreased 1.11% last month. The weakness in the US Dollar was the result of the Federal Reserve's commitment to keeps the rates low through 2014. The Euro continued to depreciate during early January, reaching $1.27 by mid-January before rebounding to end the month at 1.309 USD/EUR. The British Pound closed at 1.5780 USD/GBP in January.

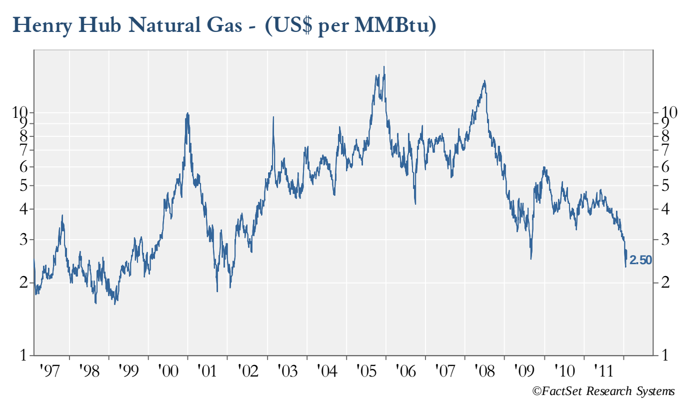
Commodity Markets

The Dow Jones UBS Commodity Index and the S&P GSCI Index gained 2.47% and 2.23% respectively for the month of January, as commodity prices surged on waning concerns of European debt crisis and as investors expected the FOMC's low interest rate policy through 2014 could weaken the US Dollar and increase demand for commodities.

All the S&P GSCI sub indices had positive returns in January, led by precious metals with a gain of 11.98%. Gold ended up 10.89% on the back of a weakening US Dollar, closing at $1740.40/oz. Silver followed Gold higher, returning 19.16%.

Industrial metals including Copper and Aluminum also had double digit returns in January. Tin had the strongest gains amongst all the commodities tracked by S&P GSCI index, returning 26.75%.

Natural Gas and Coffee prices declined the most in January. Natural Gas continued its downtrend in 2012, losing 17.32% by the month end on record storage and mild winter. Coffee declined 5.2% on expectations of a bumper crop in Brazil, the world's largest coffee producer.



The Baltic Dry Index, a composite of global freight costs for dry bulk commodities such as coal, iron ore and grains, collapsed to a 25 year low of 647 (as of Feb 3rd 2012). This likely reflects a weak global demand and an increase in shipping capacity.