
# Citizens Bank & Trust Market Review

## March 2012

[In This Issue]



Citizens Bank & Trust

# U.S. Economy Improving as Europe Teeters on Recession.

## Recent Economic Indicators

| | |
|---|---|
| Thomson Reuters/Univ. of Michigan Consumer Sentiment | 75.3 |
| Consumer Confidence | 70.8 |
| Existing Home Sales, Monthly Change | 4.30% |
| New Home Sales, SAAR* | 321,000 |
| Personal Income, Monthly Change | 0.30% |
| Personal Consumption Expenditures, Monthly Change | 0.30% |
| Non-farm Payroll Increase/Decrease | 227,000 |
| Unemployment Rate | 8.3% |
| ISM Non-Manufacturing Index | 57.3% |
| ISM Manufacturing Index (PMI) | 52.4% |
| New Durable Good Orders, Monthly Change | -4.0% |
| Industrial Production, Monthly Change | 0.0% |
| Capacity Utilization | 78.5% |
| Retail Sales, Monthly Change | 0.4% |
| CPI, Monthly Change | 0.4% |
| CPI Core, Monthly Change | 0.2% |
| PPI, Monthly Change | 0.1% |
| PPI Core, Monthly Change | 0.4% |
| U.S. Trade Deficit | $48.8 billion |
| 3Q11 Non-farm Productivity, Quarterly Change, SAAR* | 0.9% |
| 3Q11 Real GDP, Quarterly Change, SAAR* | 3.0% |

*Seasonally Adjusted Annual Rate
Bureau of Economic Analysis of the U.S. Department of Commerce, U.S. Department of Labor, the Federal Reserve, Thompson/Reuters/University of Michigan, Institute for Supply Management, National Association of Realtors, The Conference Board. Values reflect most recent data available at time of publication.

## Overview

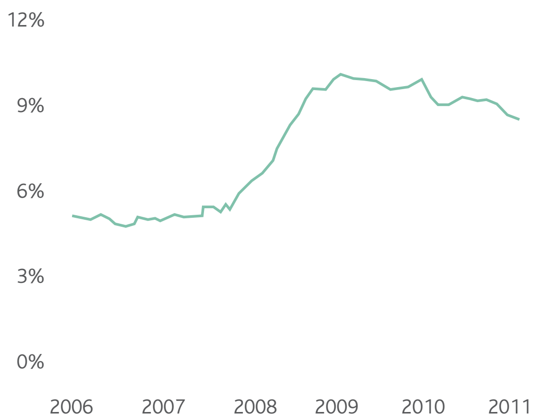
The likelihood of the eurozone economy falling into a recession increased as the 17 nation economy shrank for the first time since the second quarter of 2009. GDP for the eurozone contracted 0.3% for the fourth quarter after anemic growth of 0.1% the previous quarter, according to Eurostat. The Italian and Dutch economies both fell into recession after shrinking 0.7%. Portugal contracted another 1.3% and GDP in Greece fell a staggering 7.0%. The overall number was supported by better than expected numbers out of France and Germany. High unemployment and austere fiscal policies will continue to weigh on the eurozone economy in the near- and intermediate-terms.

Things on this side of the pond look much better. U.S. economic growth in the last quarter was stronger than originally thought. The Commerce Department revised fourth quarter GDP growth up to 3.0% from the initial 2.8% estimate released in January. The improvement was largely attributed to an upward revision in nonresidential fixed investment, a downward revision to imports, and an upward revision to personal consumption expenditures. Things on the forefront still look good with the Conference Board's Leading Economic Index showed a 0.4% increase in January following an upwardly revised 0.5% gain the previous month. The fourth consecutive gain in the index reflected broad based strength among its components and points to a stronger U.S. economy in the coming months.

## Employment

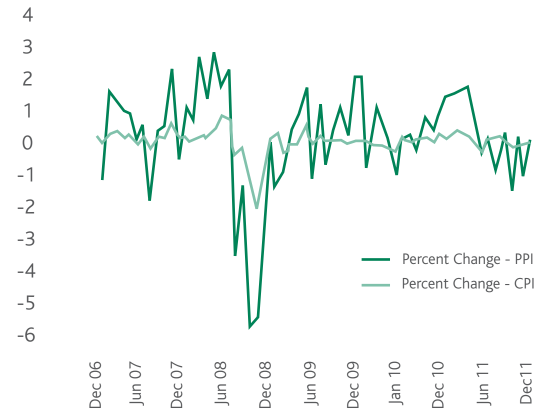
Initial jobless claims hit a recovery low of 351,000 during the February 11 week, but rose moderately to 362,000 by the week ended March 3. The increase caused the four-week average to edge up slightly to 355,000 snapping a seven-week streak of improvements. Despite the recent leveling off of the downward trend, we are now at levels that can be considered average for a normal labor market.

Unemployment Rate
January 2006 through February 2012




Source: FactSet, U.S. Department of Labor

Change in PPI and CPI, monthly
December 2006 - January 2012




Source: Federal Reserve Bank of St. Louis

Employment gains maintained a healthy pace in February as 227,000 jobs were added in the U.S., according to the Labor Department. The report also showed sizeable upward revisions to the past two months of data, with 284,000 jobs added in January (originally 243,000) and 223,000 in December (originally 204,000). The private sector once again outstripped the total with 233,000 jobs added during the month with significant gains seen again in the manufacturing space, while 6,000 jobs were shed from the government payrolls. The household survey showed gains in both employment and the labor force, keeping the unemployment rate at 8.3% as expected. Overall the data still indicates improvement in the labor market, but perhaps at a slightly slower pace than we have seen in recent months.

## Consumer Confidence and Spending

Consumer confidence continued its strong upward trend in February after taking a breather in January. The Conference Board's index surged more than nine points during the month to 70.8. Lynn Franco, Director of The Conference Board Consumer Research Center, said "despite further increases in gas prices, [consumers] are more optimistic about the short-term outlook for the economy, job prospects, and their financial situation."

Personal income growth decelerated but remained healthy while income gains seen in recent months are starting to give spending a boost. Income rose 0.3% following a 0.5% burst in January and spending rose 0.2% after being flat the previous month, according to the Commerce Department. Retail sales also grew in January, but at a rate less than markets were expecting. Retail sales were up 0.4% after being flat the previous month. There was surprising weakness in the auto component which fell 1.1% in conflict with a motor vehicle sales report released earlier in the month that showed unit sales jumped to a 14.2 million annual rate in January. Excluding this oddity, the numbers looked healthy across most other components.

## Inflation

After three months without rising prices, inflation started to pick up again at the consumer level. A report from the Labor Department showed headline inflation was up 0.2% in January. Year-over-year CPI inflation decelerated, though, to 2.9% from 3.0% in December. Inflation at the producer level rebounded 0.1% during January after slipping 0.1% the previous month. The increase was all at the core level as both the energy and food components declined. Overall the numbers look to be within a margin of safety between fears of deflation and worries of excessive inflation.

## Business Activity

The momentum we have seen recently in manufacturing hit a slight speed bump in January. Durable goods orders slipped 4.0% during the month following a revised 3.2% jump in December, according to data from the Commerce Department. Weakness was led by the volatile aircraft subcomponents, but most other components were down as well.

A separate report from the Institute for Supply Management (ISM) showed manufacturing in the U.S. expanded at a decelerating rate. The PMI registered 52.4 in February, down 1.7 from January's reading of 54.1. New orders, backlogs, production and employment components all slowed but are still growing at a respectable pace. One surprising positive in the report, given the economic contraction in Europe, was a jump in new export orders from 55.0 to 59.5. Despite the reports the overall picture for manufacturing still looks strong and comments from respondents to the ISM survey indicated a pick-up in demand. The non-manufacturing sector expanded at a slightly faster rate up one half-point to 57.3, led by a 2 point increase in the new orders component.

ISM Report on Business Activity
Index Levels from January 2006 through February 2012


Source: Institute for Supply Management, FactSet

S&P/Case-Shiller Home Price Index
20 City Composite Index Levels January 2001 through December 2011


Source: Standard & Poor's

## Housing

Record low mortgage rates and sharp price declines spurred sales activity of existing homes in January. The median existing home price fell 4.6%, according to the National Association of Realtors (NAR). That price weakness was confirmed by S&P Case Shiller data that showed the 20-city index fell 0.5% in December. This closed out the 2011 year with a 4.0% annual drop in prices, the worst reading since the housing crisis was in its infancy in mid-2006. The lower prices helped drive sales up 4.3% during January, reducing supply to an economic recovery low of 6.1 months. In addition to low prices and mortgage rates NAR chief economist Lawrence Yun identified pent-up household formation and rising rents as contributors to the uptrend. Contract signings for existing home purchases were also up, rising 2.0%.

Meanwhile new home sales failed to muster much strength in January, according to a report from the Commerce Department. Sales of new homes came in at a 321,000 annual rate, down 0.9% from the upwardly revised December number. Overall the housing market is still very depressed and there doesn't seem to be any indication that things will improve much in the near-term.

## World Economy

We had been enjoying a pleasant few months without Greece dominating the financial headlines, but all good things come to an end. European finance ministers backed a second bailout package for Greece on February 21 valued at €130 billion that will allow the country to make good on a €14.5 billion bond payment next month. For its part the Greek government agreed to more oversight by the EU, IMF and ECB and was required to pass an enormously unpopular package of austerity reforms. Greece was also required to amend its constitution to give priority to debt service payments over other obligations, a move viewed by some as compromising national sovereignty. The program still requires the approval of private sector investors who are being asked to take 75% losses on their Greek debt holdings. The goal is to get Greece's debt-to-GDP down to 120%, but that may be difficult to sustain as the focus on austerity creates further downward pressure on an economy already in its fifth year of recession.

Chinese Premier Wen Jiabao set a lower target for China's economic growth in his speech to open the annual legislative meeting of the country. The government is now targeting economic growth of 7.5% in 2012, lower than the 8.0% goal for last year. The Chinese economy often exceeds the official objective, however, which was the case last year when growth was 9.2%. Wen said "There is downward pressure on economic growth. Prices remain high." He also mentioned other challenges the country is facing in real estate, agriculture, land rights and food and drug safety. Meanwhile manufacturing in China showed a small sign of improvement as the government's purchasing manager's index rose by a half point to 51 and a separate report from bank company HSBC showed modest contraction but at a slower rate.

# Most fixed income markets rally again.

| Fixed Income Current Yields | | 2/29/12 |
|---|---|---|
| 3 Month U.S. T-bill | | 0.08% |
| 2 Year U.S. Treasury | | 0.30% |
| 5 Year U.S. Treasury | | 0.87% |
| 10 Year U.S. Treasury | | 1.98% |
| 30 Year U.S. Treasury | | 3.08% |

| Total Returns[1] | 1 Month | YTD |
|---|---|---|
| Barclays U.S. Aggregate | -0.02% | 0.85% |
| Barclays U.S. Govt./Credit | -0.11% | 0.95% |
| Barclays U.S. Municipal Bond | 0.10% | 2.41% |
| Barclays U.S. Corp. High Yield | 2.37% | 5.48% |
| Barclays U.S. Long Credit A | 0.96% | 3.30% |
| Barclays U.S. Treasury 20+ Year | -2.34% | -2.62% |
| Barclays Global Aggregate | -0.07% | 1.60% |
| Barclays Emerging Markets | 2.73% | 5.14% |

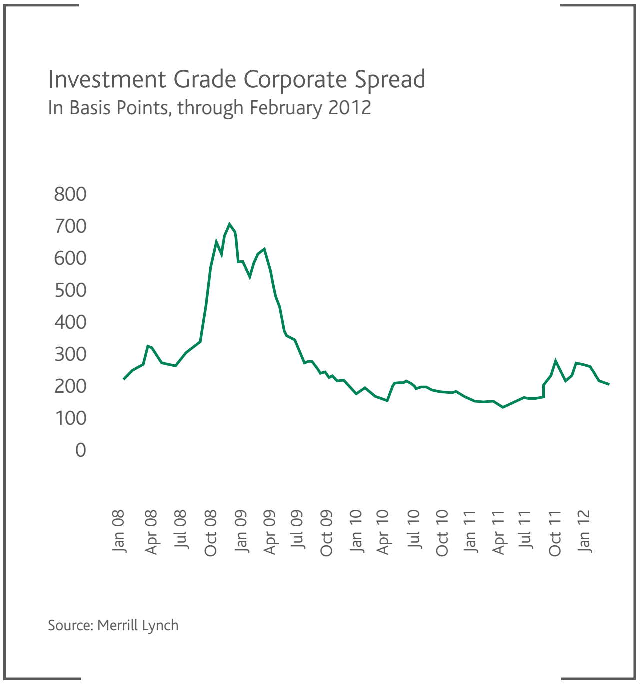
1 Month and 12 Month ending 2/29/12.
Source: U.S. Department of the Treasury, Barclays Capital
Values reflect most recent data available at time of publication.

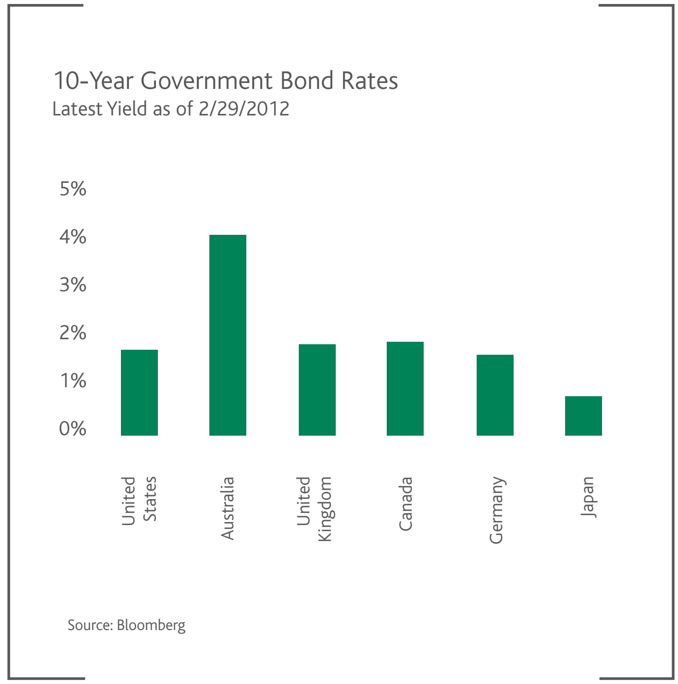
## Overview

Similar to last month, most bond market asset classes rallied with the exception of long-term U.S. Treasuries and TIPS. Investment grade corporate, high yield, municipal, emerging market and global treasury ex-U.S. indices all posted gains, while the Barclays U.S. Treasury 20+ Year index returned -2.34% for the month and TIPS lost 0.33%. Separately, the outlook for Europe improved modestly, with yields on Italian and Spanish 10-year government debt dropping below the 5.0% level, down from 6.0% last month.

Reduced expectations for more short-term monetary stimulus from the Federal Reserve drove U.S. Treasury demand lower, amid an unmistakable lack of mention of the possibility of another round of quantitative easing by Chairman Bernanke in his testimony before Congress. Without the impetus of QE3, worried investors sold government debt concerned prices could fall without the Fed as a major buyer. However, many strategists continue to anticipate the Fed will adopt additional easing measures later this year if economic growth disappoints, as Bernanke characterized the recovery as "uneven and modest." The Fed Chairman also repeated his broadly dovish assessment of the economy citing the soft backdrop of "restrained growth, persistent downside risks and moderating inflation. " Finally, because some market participants earlier had interpreted post-FOMC comments about the distribution of the first rate hikes in 2014 as implying "exceptionally low" meant anything below 1%, Bernanke clarified that forward guidance refers to the commitment to the 0% to 0.25% range on the federal funds rate.

Meanwhile, analysts at Goldman Sachs, long known as bond market bears, acknowledged that yields have remained lower than they anticipated due to the combined effect of continued uncertainty in the euro-zone area and the Federal Reserve's easy monetary policy keeping short-term interest rates near zero. Although they expect bond yields to tick higher in coming months, they feel "some of the euro-area risk needs to be removed before we can recommend taking short positions" on Treasuries.



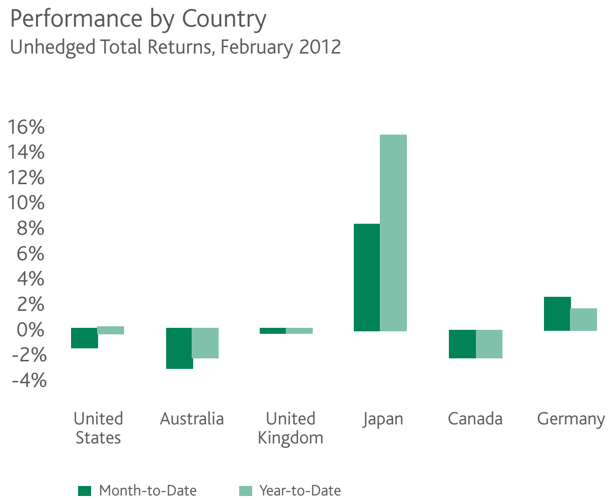

## Corporate

The investment grade corporate sector finished sharply higher yet again increasing by 0.84% for the month, bringing year-to-date gains to 3.07%. Many strategists feel the Federal Reserve's pledge to keep short-term rates low encourages investors to focus on the extra yield, or spread, offered by high-grade bonds. As such, mutual funds and ETFs focused on this sector of the market have experienced robust inflows over the past several months. This demand has driven investment grade yields to their lowest levels in more than two decades, according to Merrill Lynch. The yield on the firm's U.S. Corporate Master index fell to 3.44%, down from 4.00% a year ago and 9.30% reached in October 2008. While yields remain near record lows, relative spreads above Treasuries have not tightened to levels consistent with weakening buyer interest, suggesting continued strength looking forward. While, most eurozone financial sector bonds should still be avoided given the high degree of risk associated with this region, attractive opportunities exist for selective banks in Canada and Australia, as they are likely to benefit from still wide spreads and solid balance sheets.

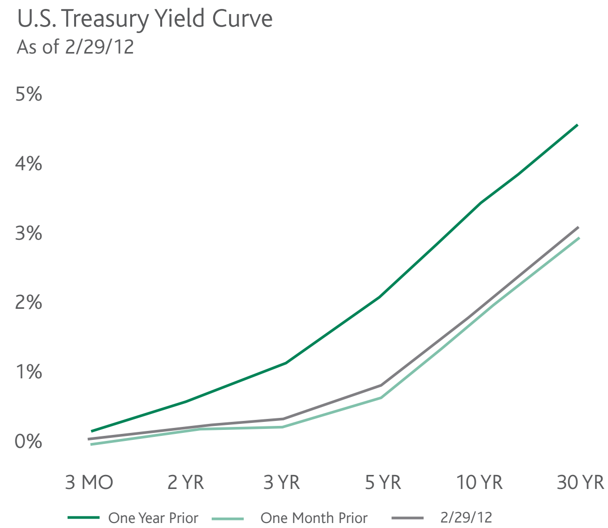
High yield bonds rose considerably gaining 2.37% for the month, brining year-to-date gains to 5.48% as investors continued to seek higher yields in the current low interest rate environment. "Falling yields and declining market volatility have brought a flood of new high yield bond issuance to market this year. This issuance rush completes a virtuous circle where improved liquidity and rising bond prices enhance the longer-term outlook for high yield debt," said Ben Garber, analyst at Moody's. Against this backdrop, investors should maintain a market-weight exposure to this asset class via mutual funds or ETFs.

## Municipals

Following the lead of most other fixed income sectors for the month, the Barclays Municipal Bond index increased by 0.10%, posting gains in ten of the last eleven months. A seasonal decline in new-issue supply coupled with considerable redemptions, historically high relative value levels as expressed by tax-exempt yields as a percentage of corresponding U.S. Treasury note yields and a range-bound U.S. Treasury market remain the primary drivers of demand. Meanwhile, sensitivity to bankruptcy issues intensified given concerns about a Detroit Michigan Chapter 9 filing and persistent structural challenges facing state and local general obligation credits. For states, tax revenue growth is unlikely to be enough to overcome the costs associated with long-term liabilities. Local municipalities face continued state aid cuts along with declining tax bases from lower home values. Despite these concerns, many strategists feel federal policymakers will continue to aid municipalities, which will likely prevent widespread default risk and diminish the potential for negative market shocks. Without the fear of a meaningful default spike in the general obligation markets, market participants anticipate little risk of a slowdown in demand in the overall muni market, particularly given the fundamental stability in the essential services revenue sector. Although default risks remain low, we advocate a focus away from lower-rated state and local G.O.s, favoring essential service revenue bonds as an alternative. At the same time, investors should pursue selective selling on the long end of the yield curve and among weaker credits rated BBB and below, given excessively robust demand in these areas. Finally, we continue to recommend high quality municipal bonds in the five- to 10-year maturity range for moderate to aggressive investors, and a one- to five-year focus for conservative investors.




Source: Barclays Capital




Source: U.S. Department of Treasury

## International

The Barclay's Global Treasury ex-US index gained 0.45% on an unhedged basis, but lost 1.05% on a local currency basis, consistent with a weaker U.S. dollar against the euro and other major currencies. Many of the safe-haven countries gave back gains from last month, with Canada, the United Kingdom, Australia and Sweden posting losses. For the third straight month, treasury securities from several over-sold eurozone peripheral countries increased with Italy (5.20%), Ireland (1.78%) and Spain (0.66%) leading the pack as borrowing costs in these countries decreased considerably. Despite another ECB bailout package for Greece, Standard & Poor's downgraded the country's long-term debt rating from CC to "Selective Default." The move was expected as S&P said it would consider Greece in selective default if it retroactively added collective-action clauses to its sovereign debt as part of an effort to force creditors to participate in a bond-swap offering. Greece's parliament approved this measure in mid-February, sparking concerns these clauses would trigger payments on credit-default swap contracts. Eurozone officials have long worried that widespread CDS payments could ripple through the region, deepening the debt crisis.

Risks to the Bond Market RallyAn unraveling of the second Greek bailout package and a spike in oil prices are the biggest risks to the bond market rally in riskier asset classes. The markets reacted favorably to a recent bailout agreement in Greece, as it appeared sufficient to avoid a disorderly default. However, the country still faces the challenge of cutting its debt burden while imposing significant austerity measures. Specifically, broad-based wage cuts will likely add to the strains of an economy near depression levels. An important implication is that a disorderly default in Greece may spillover to other euorzone countries also facing the challenge of sustaining economic growth with growing fiscal constraints.

A spike in oil prices resulting from an escalation of tensions between Iran and Israel would also likely disrupt the recent rally. Although highly unlikely, a complete shutdown in exports from Iran could increase oil prices by as much as $40 per barrel. However, most strategists agree that other OPEC nations could increase production targets by as much as necessary to provide a cushion against what would likely be a short-term loss in output from Iran.

# The 2012 rally continues into February.

| Total Return | Month | YTD |
|---|---|---|
| Dow Jones Industrial Average | 2.89% | 6.55% |
| S&P 500 | 4.32% | 9.00% |
| NASDAQ Composite | 5.59% | 14.09% |
| S&P 100 | 4.62% | 9.01% |
| S&P 400 MidCap | 4.50% | 11.40% |
| S&P 600 SmallCap | 2.12% | 8.83% |
| Russell 2000 | 2.39% | 9.63% |
| MSCI EAFE | 5.63% | 9.49% |

1 Month and YTD total return ending of of 02/29/2012.

Values reflect most recent data available at the time of publication.
Source: FactSet

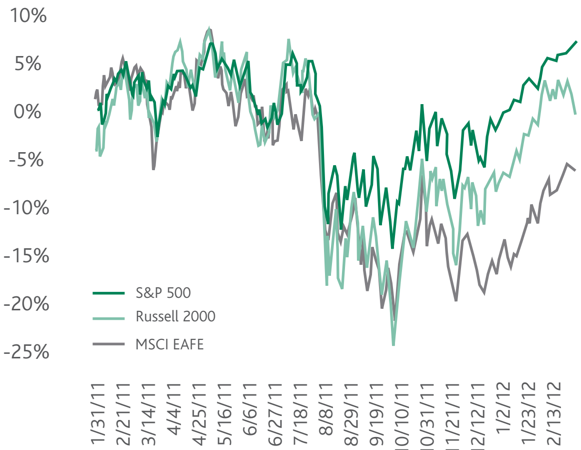
## Overview

Continued positive economic data and solid corporate earnings results led stocks higher worldwide again in the month of February, despite rising oil prices and mixed news out of Europe regarding the ongoing debt crisis. According to Marketwatch.com, a Bank of America Merrill Lynch survey of fund managers showed increased confidence towards stocks as 26% of respondents are now overweight equities, compared to only 12% in January.

The Dow Jones Industrial Average broke through the 13,000 level in the last week of the month for the first time since 2008. The index had a total return of 2.9%, its fifth consecutive month of gains. The broader S&P 500 Index returned 4.3%, while the technology heavy NASDAQ Composite Index rallied 5.6%. Year-to-date the NASDAQ (+14.1%) continues to outpace the S&P 500 (+9%) and the Dow (+6.55%) on a total return basis through the end of February.

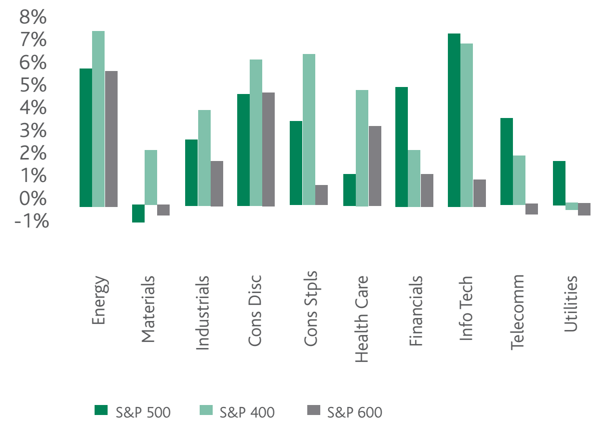
Corporate earnings were mixed again last month as fourth quarter earnings season wound down. Home Depot & Lowe's both surpassed expectations and raised guidance. General Motors reported record profits. Wal-Mart's earnings declined as the company was forced to lower prices to boost sales during a highly competitive holiday season. With 94% of S&P 500 companies reporting as of March 2nd, earnings positively surprised by 3% on average, the lowest level in several years. Information Technology companies surprised the most of all sectors, by 11%, while Telecommunications firms missed expectations by about 6% on average. In total, fourth quarter 2011 S&P corporate earnings grew only 5% as growth ranged from -24% for the Telecomm sector to +15% for IT stocks.

Equity Performance
Trailing one Year Cumulative Price Return, as of 2/29/12




Source: Yahoo! Finance

S&P Sector Performance by Market Capitalization
2/29/12




Source: Standard & Poor's

## Domestic Equity

Information Technology (+7.4%), Energy (+5.9%) and Financials, (+5.0%) had the highest total returns of the S&P large cap sectors in February. Investors continued to search for beta in stocks like Jabil Circuit (+15.2%) and Ebay (+13.1%). Devon Energy (+13.5%) and National Oilwell Varco outperformed their Energy sector peers. Returns were slightly negative for Materials (-0.4%), while Utilities (+0.7%) and Health Care (+1.3%) were also among the weakest sectors. Freeport McMoran sold off nearly 8% after a 26% return last month. Earnings for materials companies in the fourth quarter declined 18% on average.

According to Russell Indices large cap stocks out-performed mid cap and small cap stocks in February, a reversal of the prior month. The Russell 1000 Index returned 4.4% compared to 4.2% for the Russell Midcap Index and 2.4% for the Russell 2000 Index of small cap companies. Growth out-performed value across all market caps for the month. Large cap growth (+4.8%) returns were higher than large cap value (+4.0%). Mid cap growth stocks also outperformed mid cap value stocks (+4.5% vs. +3.9%). For small cap stocks the outperformance was most pronounced with growth outperforming value (+3.3% vs. +1.5%).

In other corporate news, Johnson & Johnson announced its next chief executive, a long-time JNJ veteran, while Berkshire Hathaway announced that a successor to Warren Buffet had been chosen, just not yet disclosed. Regulators on both sides of the Atlantic approved Google's acquisition of Motorola Mobility and its 17,000 patents. Apple's stock price closed over $500 early in the month, finishing February at $542, up 19.7%, and now represents over 17% of the NASDAQ 100 Index.

## International Equity

International equities continued to rebound from last year's declines. The broad MSCI EAFE Index of developed markets had a total return of 5.8% in U.S. dollar terms for the month of February with nearly all markets positive except for Greece (-8%). The Nordic countries of Norway (+15.5%), Denmark (+14.4%), and Sweden (+10.7%) were particularly strong. Germany (+8.4%), France (+7%), the UK (+5.2%) and Japan (+5.1%) also had solid returns. The European Central Bank conducted its second long-term refinancing operation (LTRO) in which 800 banks participated in the three-year loan program. The Bank of Japan expanded its asset purchasing program mid-month, indicating monetary easing, in an effort to put an end to the deflation that has weighed heavily on the Japanese economy for years. Year-to-date the MSCI EAFE Index had a total return of 11.4% through the end of February.

The total return for the MSCI Emerging Markets Index was 6.0% for the month. Egypt (+14.9%) and Thailand (+12.3%) led all countries with China (+6.5%), Brazil (+5.5%) and India (+4.8%) also strong. China's leading human resource services provider 51Job, Inc. reported earnings well ahead of expectations leading to a stock increase of 14% for the month. IShares reported fund flows into emerging market exchange traded products were positive every week in 2012 through March 2nd. The total return or the MSCI EAFE Emerging Markets Index year-to-date was 18.1% through the end of February.

# Commodities continue to surge.

| Price Change | Month | YTD |
|---|---|---|
| Dow Jones UBS Commodity Index | 2.70% | 5.24% |
| Oil | 8.12% | 7.55% |
| Copper | 2.17% | 12.70% |
| Gold | -1.67% | 9.04% |
| NAREIT- All REITS | -0.66% | 5.76% |
| NAREIT-Industrial/Office | 1.06% | -9.82% |
| NAREIT- Residential | -3.77% | 0.12% |
| S&P Global Property Ex-U.S. | 9.00% | 9.00% |
| HFRI Emerging Markets Index | 4.28% | 9.31% |
| HFRI Fund Wtd Comp. Index | 2.14% | 4.95% |
| HFRI Equity Market Neutral | 1.12% | 2.54% |
| HFRI Event Driven | 1.89% | 4.56% |
| HFRI Market Defensive | 0.36% | 0.78% |
| HFRI Merger Arbitrage | 0.91% | 1.61% |
| HFRI Short Bias | -7.61% | -12.32% |

1 Month and YTD total return as of 2/29/12
Values reflect most recent data available at the time of publication.
Source: Dow Jones, National Association of Real Estate Investment Trusts, Hedge Fund Research, Standard and Poor's, wsj.com - Market Data Center, Private Equity Online, FINalternatives.

## Overview

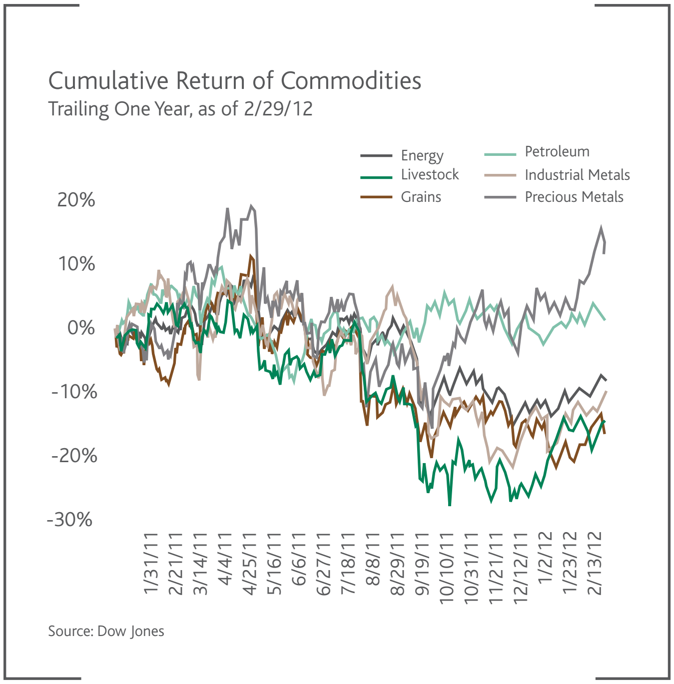
Commodities continued right where they left off in January, as the Dow Jones Commodity Index gained 2.70% last month, bringing it up 5.24% on the year. Hedge funds and real estate investment trusts took a step back in February, as the HFRI Fund Weighted Composite Index and the FTSE NARIET All REITs Index dropped 2.14% and 0.66%, respectively. Alternatives kicked off 2012 on the right foot, as commodities, hedge funds and real estate investment trusts (REITs) all posted positive returns for January. The Dow Jones UBS Commodity Index rose 2.47%, the HFRI Fund Weighted Composite Index gained 2.63% and the FTSE NAREIT All REITs was up 6.47% last month.

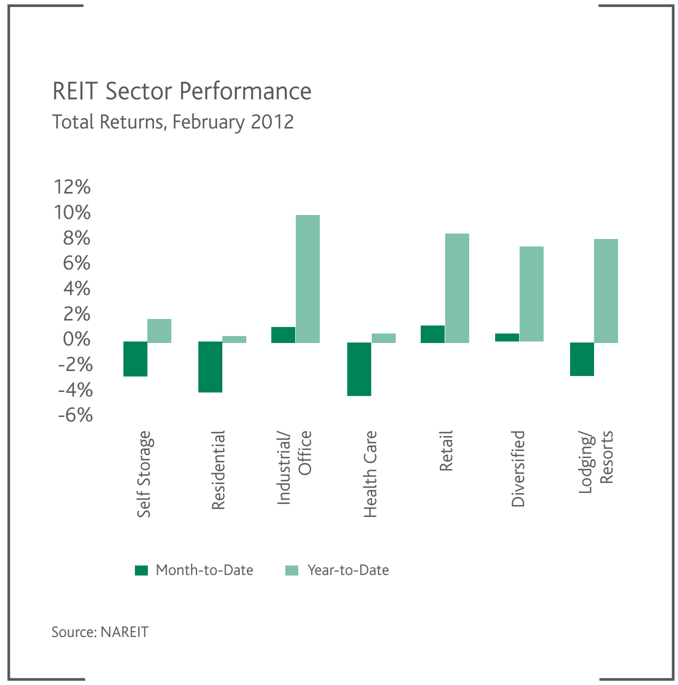
## Commodities

The Dow Jones Commodity Index was up 2.70% in February after a 2.47% gain in January. Natural Gas prices slipped once again, now down over 19% for the year, while future indices for silver, tin, and platinum are all up over 20% year-to-date. Global turmoil in the Middle East continues to keep hedge funds and other investors quite bullish on commodities, as they have been since September 2011.

Gold fell nearly $100 an ounce from a three-month high last week after Fed Chairman Bernanke's statements regarding the possibility of maintaining a low-rate environment until late 2014, but Gold prices were still up 2.76% in February and Silver was up nearly 12%. The price volatility of precious metals is lower so far in 2012 from the swings of 2011. Precious metals still tend to move significantly on any currency-related news, especially stemming from Europe and that would affect the Euro/U.S. Dollar relationship. Gold now sits at just over $1,700 an ounce.

Finally, crude oil (WTI) was up nearly 8% in February, its largest monthly gain since October, 2011. Geopolitical factors seem to have a strong grip on crude prices in this market environment as seen by volatile price swings in reaction to headline news. We saw an example of this last week as Brent Crude rose $2/barrel in just 5 minutes, finishing up over $3/barrel for the day, on a false news report of a




pipeline explosion in Iran. Some analysts are expecting a correction as the recent high prices seem to be driven mostly by nervous speculation about Iran and other issues. Bloomberg analyst Caroline Baum suggests that higher oil prices may not be a bad thing; massive hiring in the oil industry has given tens of thousands of Americans well-paying jobs and reduced unemployment in several areas of the country. North Dakota, for instance, where the booming Bakken oil formation sits, boasts an unemployment rate of just over 3% compared to the national rate of 8.3%.

## Real Estate

Real estate investment trusts (REITs) were lower last month after a strong start to the year. After posting gains of roughly 6.50% in January, the FTSE NAREIT All REIT index was down 0.66% last month, lowering year-to-date gains to 5.86%. The FTSE NAREIT All Equity REITs also fell in February, slipping 0.91%, significantly lagging the S&P 500 during this same period, which was up 4.32%. The index composed of all equity REITs is now up 5.39% for the year. This trend was similar when you dove deeper into sector specific REITs. Residential was down 3.77% in February, bringing year-to-date gains just above flat at 0.12%. Health care was also hit hard, down 4.17% last month and barely in the green at 0.23% on the year. Self-storage and lodging/resorts also suffered losses, down 2.58% and 2.65%, respectively, last month. It wasn't all bad news though, as industrial/office gained 1.06% in February and is now up 9.82% on the year. Retail had a strong month as well, up 1.10% and 8.21% year-to-date. The Vanguard REIT ETF (VNQ), which tracks an index that measures the performance of publicly traded equity REITs, underperformed the DJIA in February as well. The latest under-performance problem stems from mortgage REITs, as the possible implementation of government-backed refinancing programs for underwater homeowners gains traction.

## Hedge Funds

Hedge funds added 2.14% in February, bringing their year-to-date gains to 4.95%, their strongest start to a calendar year since 2000, according to Hedge Fund Research (HFR). One of the industry's most closely watched indicators, the HFRI index indicates that most strategies are higher this year due to the rally in equity markets "fueled by hopes for stronger growth and a solution to Europe's debt problems." The HFRI Equity Hedge Index climbed 6.9% in the first two months of the year and despite trailing the S&P 500 in both January and February, this has been one of the better starts to the year for the industry in over a decade.

The strong 2012 start, is in large part due to strategies that underperformed in 2011, according to HFR. Equity hedge funds added 2.99% in February, up 6.9% year-to-date, while event driven funds added 1.89%, 4.56% year-to-date, with significant positive contributions from activist and special situation funds. Fixed income-based relative value arbitrage funds gained 1.7% in February thanks to spread tightening and strong liquidity. Emerging markets funds posted strong gains of 4.3% in February, for a year-to-date gain of 9.3%. Analysts note that performance was strong across all emerging markets, with Russian and Eastern Europe strategies faring particularly well, up 12.7% so far this year. Kenneth Heinz, president of HFR, attributed hedge funds early success as benefiting from "improvement or total reversal of the trends, sentiment and volatility which contributed to the challenging environment in 2011. While equity market volatility may rise from early 2012 subdued levels, hedge funds are well positioned in the current environment to opportunistically adjust exposures and generate gains across multiple asset classes globally in 2012." Only short-bias funds had a disappointing showing last month, declining 7.61%, and now down 12.32% for the year.

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