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Market Review

January 2011

U.S. Economic Data

The U.S. economy picked up steam towards the end of 2010 as U.S. consumers increased spending and U.S. companies increased their net exports. The real gross domestic product of the U.S. grew at an annual pace of 3.2% during the fourth quarter, according to the initial estimate. U.S. consumer spending (red bar in figure 1), which accounts for about 70% of GDP, grew at 4.4%, the biggest increase since the beginning of 2006. This contributed 3% to GDP. A sharp decrease in imports and an increase in exports resulted in net exports (green bar) contributing 3.4% to real GDP.

It is worth noting that the growth in GDP during the recent few quarters came from businesses building their inventories (blue bars). However, shrinking inventories during fourth quarter subtracted 3.7% to the GDP.

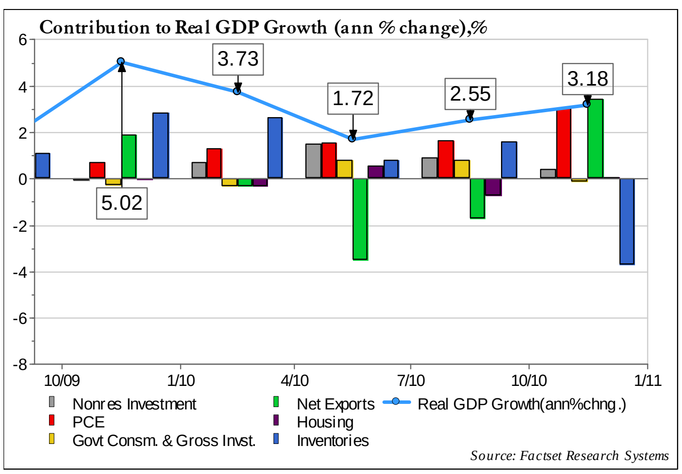

Figure 1

Consumers had to dip into their savings to fund part of the spending as income growth remained weak. The saving rate has been steadily declining during the last six months and stood at 5.3% (figure 2) at the end of December after reaching a peak 6.3% in June this year.

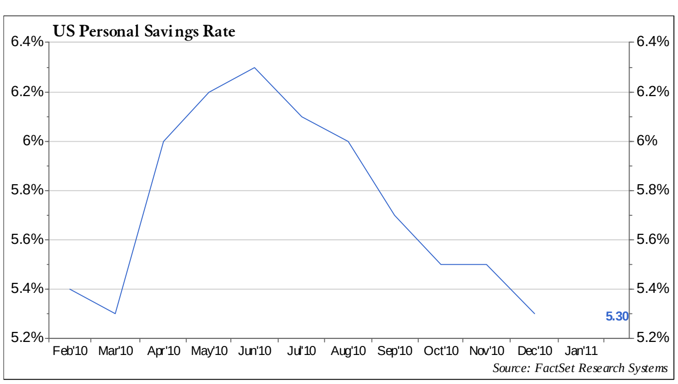

Figure 2

Real GDP increased 2.9% during 2010 versus a decrease of 2.6% in 2009. The real GDP totaled $13.38 trillion (2005 chained dollars), rising above the $13.36 trillion peak set in fourth quarter of 2007 before the recession. As the next chart shows, U.S. real GDP output levels have now slightly exceeded the pre-recession levels (0.14%) but with nearly 5% fewer workers (figure 3). This shows the extent to which companies have embraced leaner and more efficient processes resulting in an increase in the U.S. employee productivity.

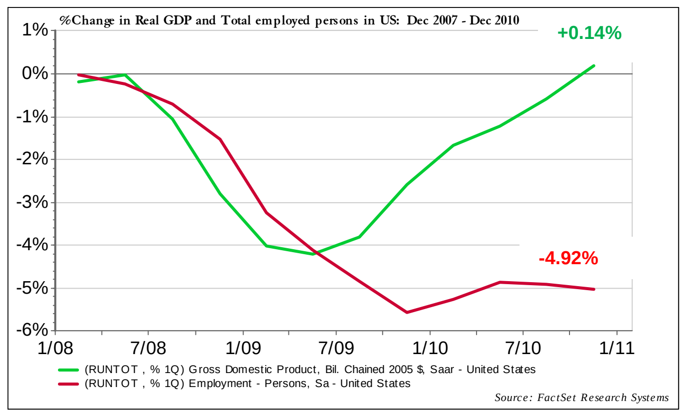

Figure 3

The Unemployment rate fell from 9.8% in November to 9.4% in December and 9% (figure 4) in January 2011. This is the lowest since April 2009. However, the January non-farm payrolls were just above flat, increasing by 36K vs. a consensus of 140K. The U.S. Government attributed the subpar labor market performance on the snow storms. The mixed January numbers are further obscured by the Labor Department's annual benchmark revisions. The civilian labor force was reduced by 504,000, which contributed to most of the 622,000 decline in unemployed last month.

Figure 4

Both manufacturing and non-manufacturing sectors continued their expansion in January with both reporting numbers above their respective consensus estimates. The

ISM Purchasing Managers Index reported 60.8, up from 58.5 in December (figure 5). The ISM Non-Manufacturing Index rose to 59.4 from 57.1 in December. The ISM Non-Manufacturing Index (or the service industries), which is far larger than the manufacturing side, expanded at the fastest pace since August 2005 and is now in fifth straight month of expansion and 14th straight month above 50.

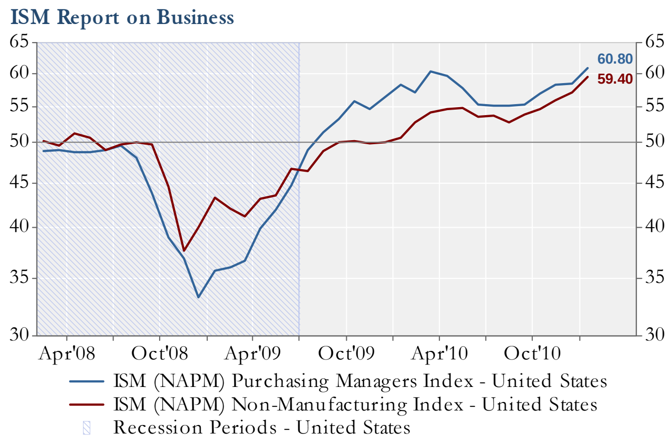

Figure 5

Equity Markets

The stock markets had a good January despite some volatility (figure 6) during the end of the month as the situation in Egypt unfolded. Large and mid-cap stocks outperformed small cap stocks in the U.S. The S&P 500 and S&P Mid-Cap gained 2.37% and 2% respectively, while the Russell 2000 lost 0.26% in January.

The MSCI World index and MSCI EAFE returned 1.96% and 1.6% last month, respectively. The FTSE 100 was down 0.55% and the STOXX 600 recorded returns of 1.63% during the same period. The MSCI Emerging Markets index was down 2.10% in January. India had the worst monthly decline in more than two years with the BSE SENSEX index down -10.64%.

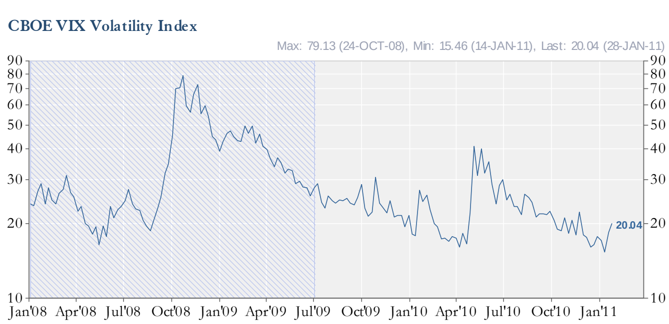

Figure 6

Bond Markets

The U.S. Benchmark 10 year yields were nearly flat in January closing at 3.378%. The 10 year yields were at 3.371% the prior month end. They have since surged and are currently at 3.65%, the highest levels since May 2010. The bond market appears to believe that most of the recent economic data (including today's unemployment rate report) likely indicates an increasing momentum in economic recovery. There is also speculation that even the developed economies may need to start raising interest rates to counter the surge in global food and energy prices. The U.S. Benchmark 30 year treasury yields have also increased during the last few days and are currently at 4.73%.

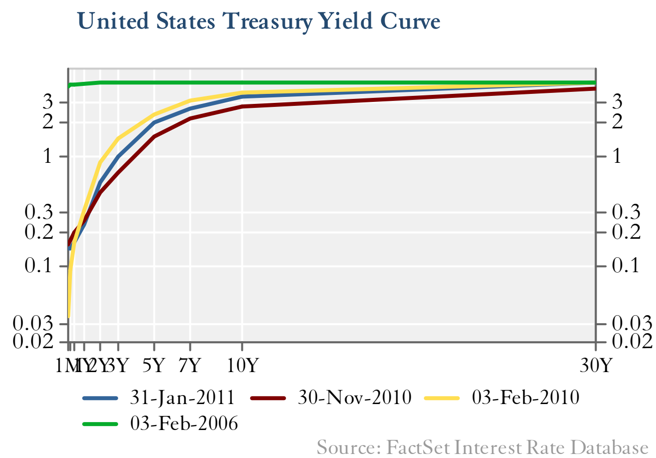

Figure 7

The German 10 Year Bund yield rose by nearly 18 bps to close at 3.15% (figure 8) for January. The UK 10 Year GILT yield increased 25 bps, closing at 3.64%. The 30 year UK treasury came down 5 bps to close the month and year at 4.19%. The U.S. bond market (as represented by the Barclays Capital U.S. Aggregate Index) was nearly flat, returning 0.12% last month.

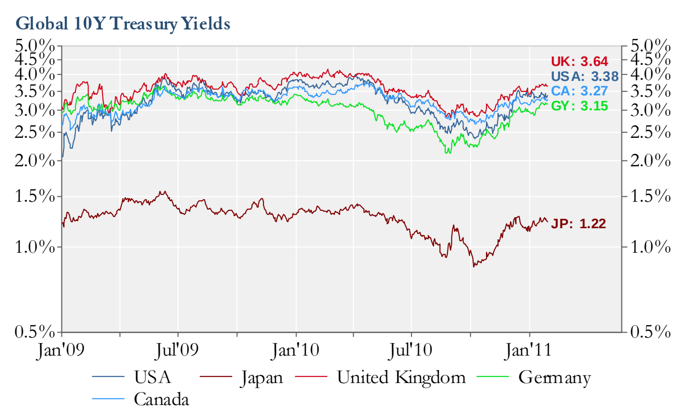

Figure 8

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Currency

The US Dollar Index fell 1.6% in January. The Swedish Krona gained 4.1% against the dollar making it one of the best performing currencies in January. The South African Rand was amongst the worst performers, losing nearly 8%.

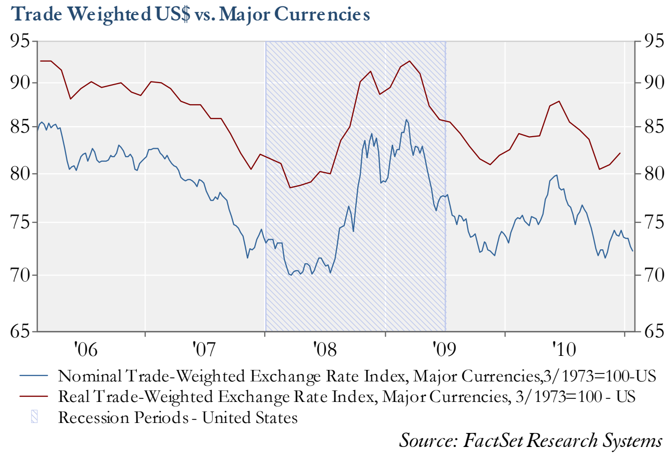

Figure 9

Euro closed at 1.37 USD gaining 2.44% against the US Dollar. The British Pound closed at 1.60 USD appreciating 2.65% against the green back.

Commodity Markets

The commodity markets had a mixed month in January. Precious metals like Gold and Silver gave back some of the gains made during the recent months while Energy and Food rallied after the Egyptian riots.

The Dow Jones UBS Commodity Index was up 1% during January. S&P GSCI Index was up 3.05% during the same period. Gold futures closed at $1,334.5 per ounce, down nearly 6.11% for January. Gold did rally nearly 1.7% on 28th January as investors took off risky assets and embraced safer havens amidst the Middle East turmoil. Silver lost nearly 9% to close at $28.17 per troy ounce.

Copper set record highs in January (figure 10) and crossed US$10,000 a metric ton on 3rd February on tight fundamentals. Robust demand, tight inventories, production problems and fear of supply disruptions due to a cyclone in Queensland are reasons behind the spike in Copper prices.

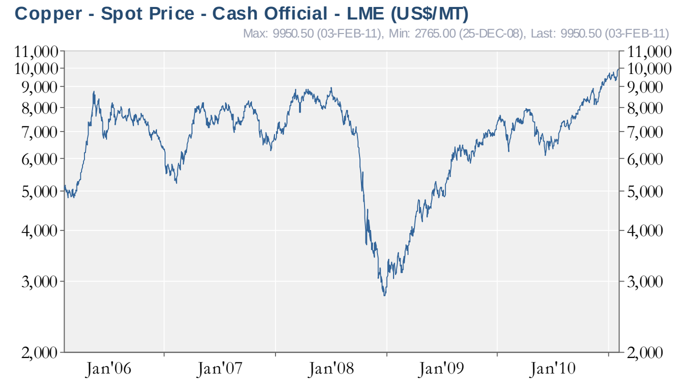

Figure 10

Crude oil prices closed at $92.19 a barrel, gaining about 1% during January after rising nearly 8% during the last few days of the month amid fears that crude shipments through Suez Canal would be interrupted.

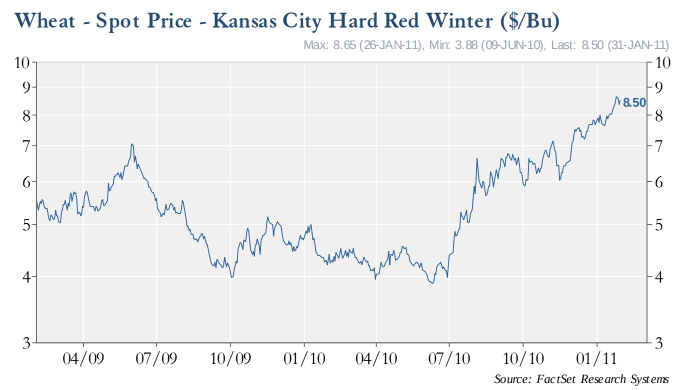

Figure 11

Soaring food prices and chronic unemployment spurred protests in Egypt, Yemen, Algeria and Tunisia. This led to speculation that governments from emerging economies would increase their imports of food crops. Rice, Corn and Wheat futures gained 11%, 5% and 6% respectively in January. Cotton jumped more than 16% in January, posting the biggest monthly rise since 1960 as farmers struggled to meet the strong demand in China.