New Albany Investment Management

Market Insight…

… Performance
Economic Update
Charts of Interest

April 18, 2011

Market Performance:

Week ending 4-15-2011

Sector	week	1mo	YTD
S&P 500	-0.6%	3.0%	5.5%
Russell 2000	-0.7%	5.6%	6.9%
MSCI EAFE USD	-1.0%	8.2%	4.7%
MSCI EM	-2.0%	8.0%	2.6%
Bar Cap US Bonds	0.8%	0.1%	0.9%
Gold	0.0%	5.5%	6.6%
Real Estate	2.6%	4.4%	8.3%
Energy	-3.0%	3.6%	14.4%

Economy:

•First quarter, it now appears that U.S. real GDP is closer to 2% in 1Q vs. original forecast of 3.5%

•U.S. industrial production rose +0.8% m/m in March, with upward revisions to prior months, capacity utilization continues to rise, and the headline NY Fed index for April ticked higher to 21.7.

•U.S. retail sales also rose +0.4% m/m in March, and +0.6% ex autos and gas.

•Job Openings and Labor Turnover Survey (JOLTS) done by the Bureau of Labor Statistics showed that the number of people quitting their job continued to show a rebound in February (quitting likely requires a base level of confidence).

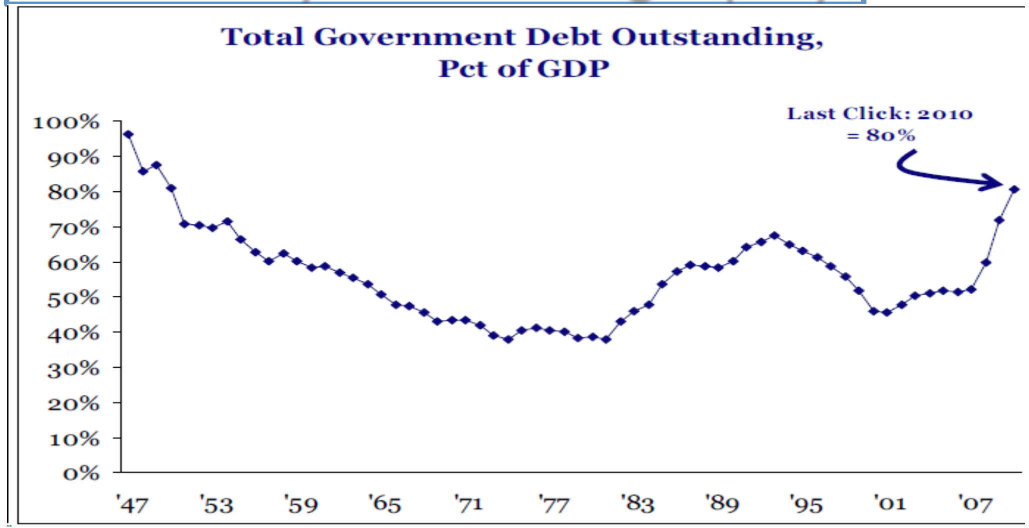
•The biggest divergence during the past several weeks has likely been 1) the ECB's move to raise interest rates verses 2) the Fed has maintained its dovish posture. Different in mandate, with the ECB focused singularly on inflation, while the Fed has responsibility for both U.S. unemployment and the change in the price level.

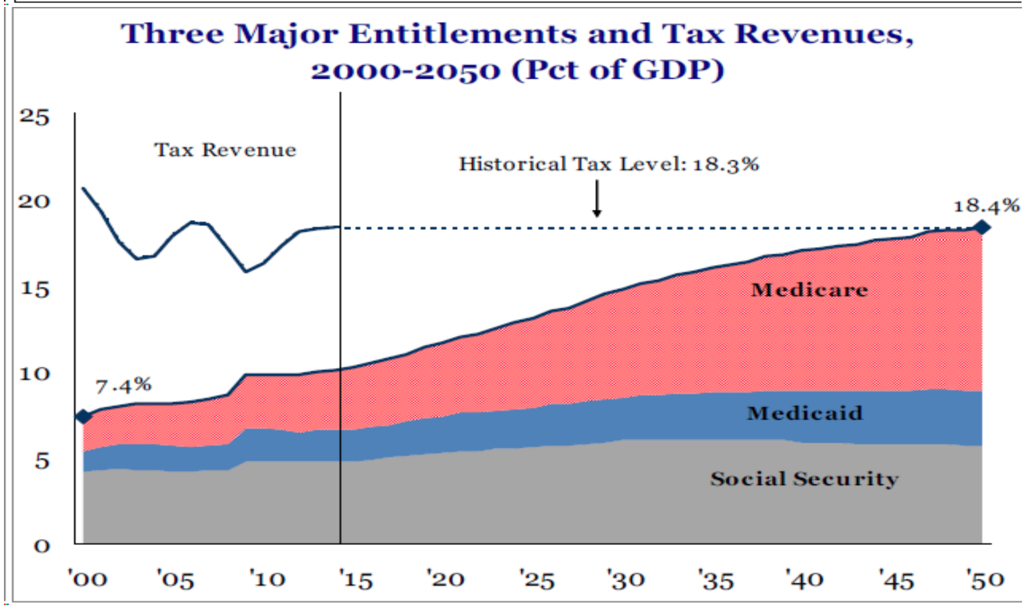
•Inflation in US will not rise significantly until owner's rent (which comprises 40% of CPI) begins to rise. With vacancy rates at 9%, there is still little inflation pressure. However once vacancy rates fall below 7%, inflation can accelerate quickly.

Fiscal Policy

- S&P placed US debt on credit watch arguing that the possibility of a grand political deal on entitlement reforms seems too far off in the future. The issue is not an all-or-nothing proposition but rather a two-step process starting with smaller reforms such as a discretionary spending cap and Medicaid reforms as part of the upcoming debt ceiling increase. Smaller reforms now will buy policymakers time to come up with a solution for the larger reforms on Medicare, Social Security, and taxes, which will likely be the story in 2013.
- Budget Debate: The debt limit has been lifted 10 times in the past decade and, in that time, net debt has more than doubled. The debt limit could serve as a catalyst for a positive reform making the S&P warning ending actually a catalyst for good change.
- Previously, ('95-96) a debt limit debate the S&P 500 declined more than 3 pct as fears about a debt limit increase took hold. But the S&P 500 closed 8 pct higher from its low when the debt limit was increased 6 weeks later. The S&P is currently down a similar 3 pct from its high.
- POLICYMAKERS FACE A CHALLENGE SELLING AUSTERIT. Economic concerns, such as jobs, and gas prices are still paramount to voters. Yet, voters by a roughly 2 to 1 margin oppose cutting entitlements and tax increases.

Fiscal Policy: Debt rising rapidly





Over time, Medicare, Medicaid, and Social Security will consume all US tax revenues.

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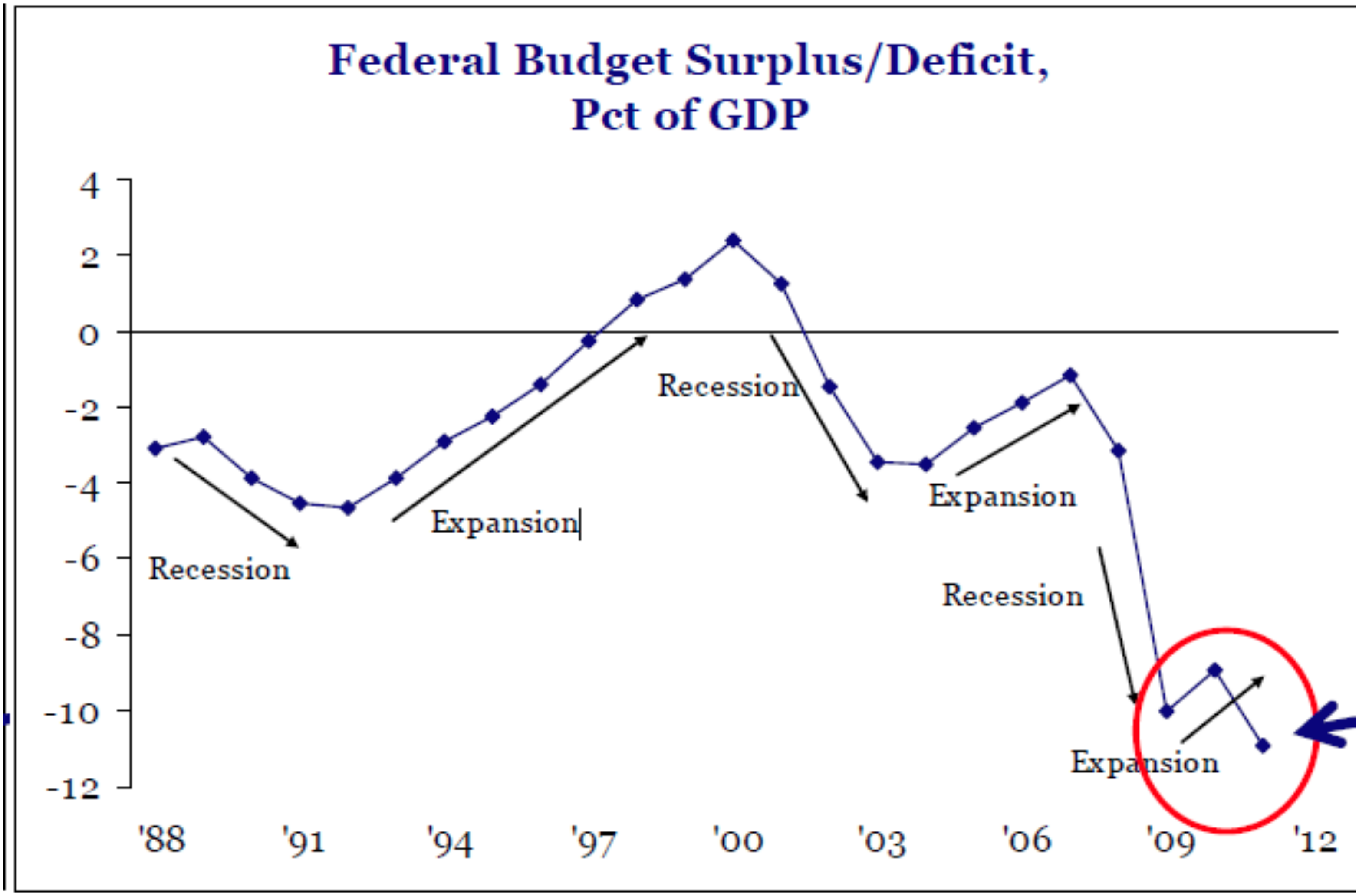
Fiscal Policy: Despite expansion, deficit continues to grow due to rise in debt payment and entitlement programs



Market View: Strategas

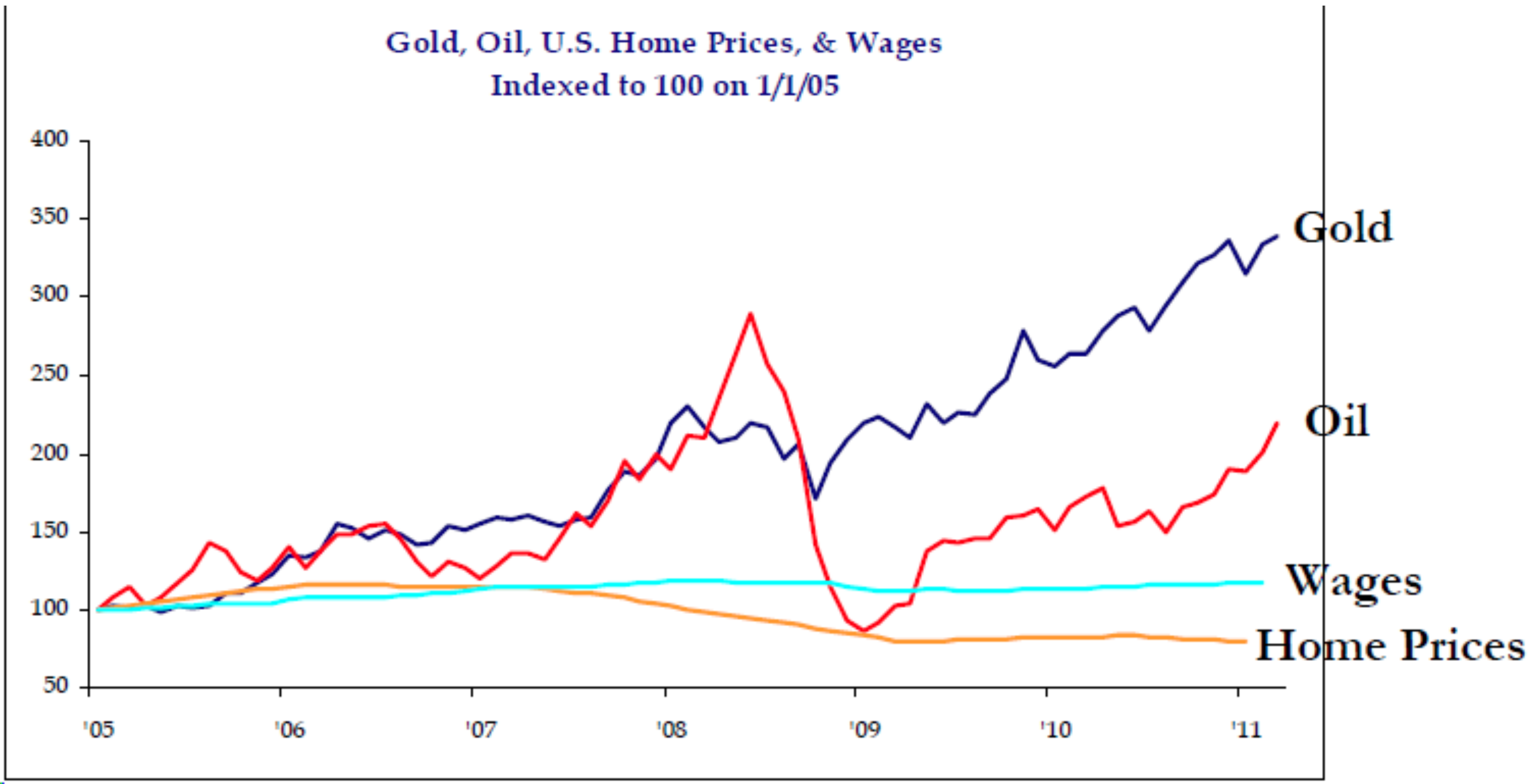
Bullish until these factors change significantly…..

We're Bullish Until…

- **30/10 Spread** *(Watching 10-Year yields alone is unlikely to give the early warning signs of incipient increases in inflationary expectations).* ✓
- **3-Month US$ Libor Flashes Signs of Financial Stress** *(Despite problems in Europe, Libor is actually declining).* ✓
- **Mortgage Rates Push Back Towards 6%** *(All clear here, now roughly 5%).* ✓
- **Commodity Price Inflation Forces China to Meaningfully Slow Economic Growth** *(This has started).* ✘
- **Our Proprietary Bellwether Index of Economically Sensitive Stocks Breaks Down** *(No signs of structural weakness).* ✓
- **Signs of Protectionism Creep into Global Policy** *(Although this remains a concern, there is little evidence of this - yet).* ✓

Inflation in the Modern World:

The concept of "bi-flation" – China will likely continue to inflate the prices of everything that it needs (oil, copper) and leave the prices of everything it doesn't (U.S. homes, American labor) to its own devices.



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Markets:

- Equity Correction still not a major top. Major tops in stocks are, more often than not, accompanied with severe stress in the credit markets – to date, there is no meaningful evidence of this playing out Credit spreads in LIBOR, Investment Grade, and High Yield remain benign.
- Market correcting against the backdrop of rising moving averages. This is healthy

The 50, 100, 150, and 200-day moving averages all remain upward sloping. <u>**Pullbacks, against the backdrop of upward sloping moving averages, tend to remain contained events.**</u>

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Markets: Gold