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April 2012

Financial Markets Overview
1st Quarter 2012

PIIGS on a Wing

Back in 1977 the rock group Pink Floyd was singing about “Pigs” and “Pigs on a Wing”.

They must have been way ahead of their time although I doubt that they were anticipating the unfolding events in Europe and elsewhere.

- Due to their fiscal and public debt problems **P**ortugal, **I**reland, **I**taly, **G**reece and **S**pain are no often referred to as the PIIGS countries.
- The drama in Europe continues to develop and after the recent debt restructuring for Greece the focus is now squarely on Spain.
- However, the U.S. is now moving in the same direction which is cause for concern.

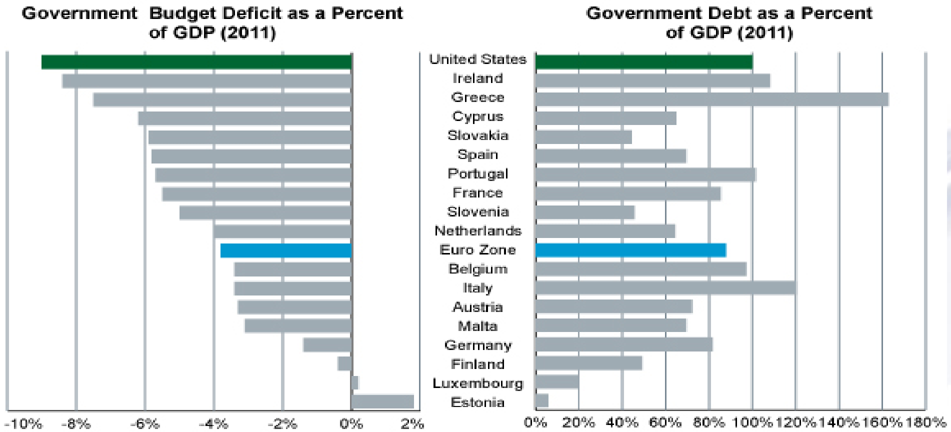
PIIGS on a Wing (cont'd)

The key measurements of the percentage of the budget deficit relative to Gross Domestic Product (GDP) and debt to GDP give a good illustration.

Continuing the budget deficit trend as we have seen in the last few years will put the U.S. on a path towards instability.

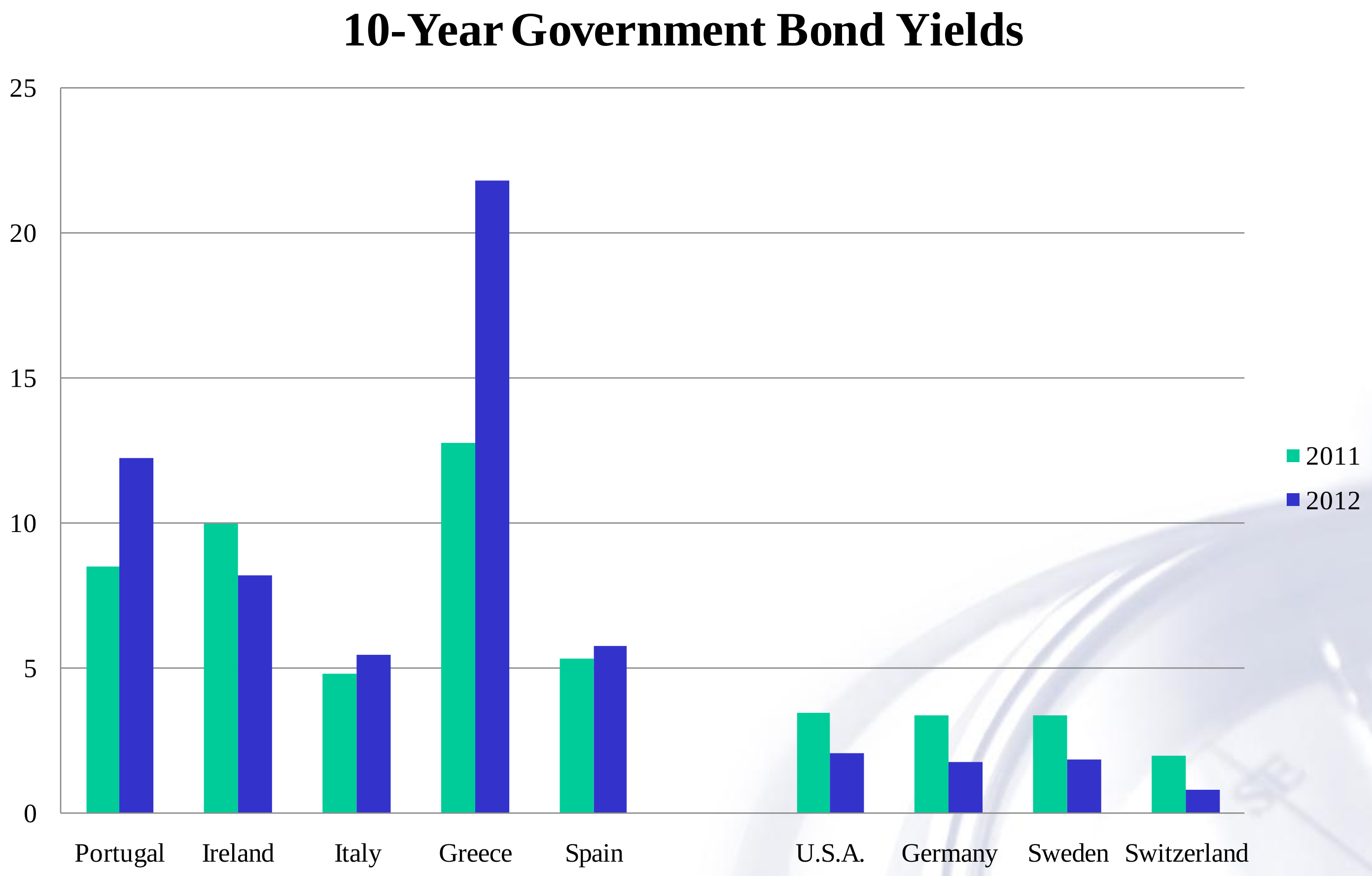
While Europe Receives Much More Attention in the Popular Press, the Levels of Deficits and Debt in the U.S. are Equivalent in Magnitude

2011 National Government Budget Deficits and Indebtedness as a Percent of GDP: Euro Zone and the U.S.



Source: Bloomberg and the Wall Street Journal
Note: U.S. government debt includes securities held by federal agencies, primarily the Social Security Administration

Government Bond Yields



Government Bond Yields (cont'd)

Depending on their fiscal position governments are either being "rewarded" with low and/or sinking yields of their government bonds or "punished" with elevated or rising borrowing costs.

- A comparison of 10-Year government bond yields starkly illustrates what happens when the fiscal situation starts to deteriorate as is the case with Greece, Portugal, Spain and (to a lesser degree) Italy.
- On the other end of the spectrum are the fiscally responsible countries Germany, Sweden and Switzerland.
- The U.S. is currently able to take advantage of its "safe haven" status although it remains to be seen whether that can be maintained.
- The loss of the AAA rating last year has not yet had any measurable impact for the U.S. so far.

Low Interest Rates

U.S. Treasury yields are near historical lows (as of April 17, 2012):

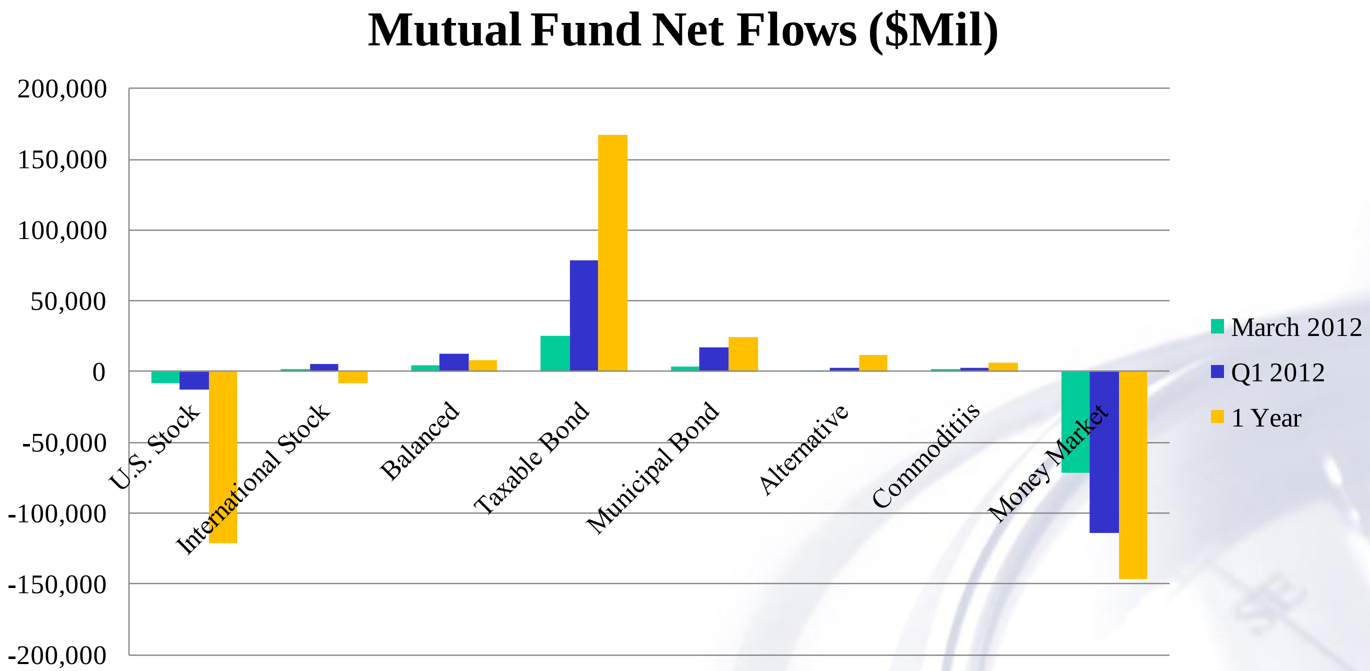
3 months:	0.076% p.a.
2 years:	0.270% p.a.
10 years:	1.998% p.a.

Bill Gross, co-chief investment officer of PIMCO and Warren Buffett, CEO at Berkshire Hathaway have contrasting views on the bond investments.

- Bill Gross sold his entire Treasury holdings in the spring of 2011 only to buy them back recently as he believes that investors will favor U.S. debt over other countries' (primarily troubled European ones).
- Warren Buffett believes that yields have moved so low that bonds are unattractive and even represent a significant risk when interest rates start rising. As a consequence he is favoring stocks.

Fund Flows

- Mutual fund flows still show investors favoring bonds for their perceived lower risk over stocks.
- There were big outflows out of money market funds which are yielding close to zero.



Source: Morningstar

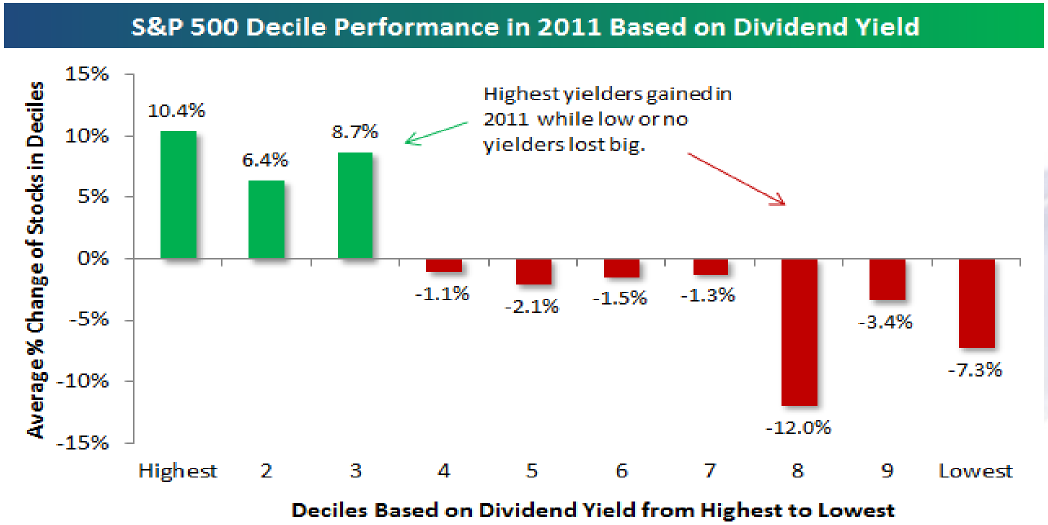
Stock Market Performance

- Stocks had an excellent first quarter 2012 with positive returns across the board.
- The U.S. and Japanese markets fared best during the last 12 months and for the 2 year period the U.S., Germany and the Great Britain showed positive nominal returns.
- Brazil, the former darling of the Emerging Markets now shows a negative return of the past 1 and 2-year periods.

	1st Quarter	1 Year	2 Years
Germany (DAX)	17.78%	-1.34%	12.89%
USA (S&P 500)	12.00%	6.23%	20.44%
Great Britain (FTSE 100)	3.52%	-2.37%	1.57%
France (CAC 40)	8.35%	-14.17%	-13.84%
Japan (Nikkei 225)	19.26%	3.37%	-9.07%
Switzerland (SMI)	5.04%	-1.92%	-9.28%
Hong Kong (Hang Seng)	11.51%	-12.63%	-3.22%
Brazil (Bovespa)	13.67%	-5.94%	-8.33%

Dividends make a Comeback

- With the low yields on bonds stock dividends have all of a sudden become attractive again.
- It is being recognized that companies that are paying regular and/or rising dividends are well established in their markets and may even have pricing power to pass on rising raw material costs.
- As a consequence investor interest for strategies focusing on dividend stocks has been rising a lot during the past 18 months.



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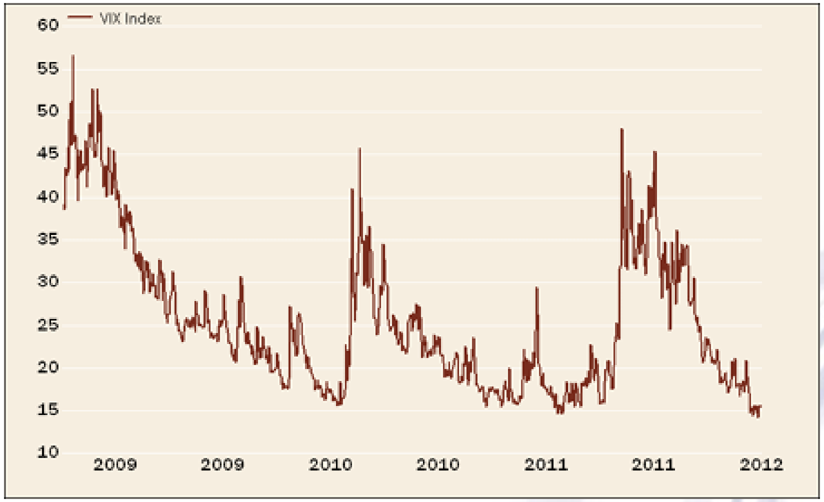
Reduced Volatility in the Markets

- The levels of volatility reached the highest levels in early 2009, 2010 and 2011
- It has now come down significantly since the middle of 2011.



Source: FactSet, as of March 30, 2012

Emerging Markets
(why there can still be substantial risks)

- On April 17 Cristina Fernandez de Kirchner, the president of Argentina, announced the seizure of YPF SA, a local subsidiary of the Spanish oil company Repsol YPF SA.
- This shows that there are elevated levels of risk in emerging markets as their legal systems are not as well established and stable compared to developed countries.
- There have been similar instances in Russia where international joint venture partners were forced to divest after making substantial investments.
- A diversified approach that includes a sufficient number of different countries and regions is highly recommended when considering emerging markets as opposed to single country funds or ETFs.

Conclusions

Some Short/Medium-Term Trends:

- Volatility in the financial markets has come down since the middle of 2011
- There is a continuing risk avoidance by main stream investors (see mutual fund flows)
- Fiscal situation in some developed countries remains an ongoing concern
- Emerging countries could be negatively affected by a continued slowdown in their traditional trading partners.

❖ Caution with long term bond investments

❖ We prefer Value (dividend) stocks

❖ ETFs to cover specific sectors

❖ Treasury Inflation Protected Securities (TIPS)

Contact Information:

Markus Bruderer
Vice President
UNFCU Financial Advisors
24-01 44th Road
Long Island City, NY 11101-4605
Tel.: 212 324 3902
E-Mail: mbruderer@unfcuadvisors.com
Web: www.unfcuadvisors.com

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