MEMORANDUM

To: All Clients

From: Meketa Investment Group

Date: April 2012

Re: First Quarter 2012 Economic & Market Review

Global equity markets soared for a second consecutive quarter, capping the best first quarter for US stocks since 1998. Additionally, foreign stocks performed similarly well as investors embraced riskier asset classes. This was largely due to investor optimism over the near-term future of the Eurozone, improving economic data in the US, and hopes for a "soft landing" in China.

While some near-term issues (e.g., the default of Greek debt) were addressed, a number of concerns remain unresolved. These include sovereign debt issues in Europe, the potential for a "hard landing" in China, and a stalled recovery in the US economy.

Economic Review

First quarter 2012 U.S. GDP is estimated to come in at between 1.5% and 2.0%, below the 3.0% experienced in the fourth quarter. The employment picture continued to show improvement with the unemployment rate declining to 8.2%. Although the unemployment rate has sunk, the labor force participation rate (the percentage of the population that is employed or looking for employment) has sunk to levels not seen since the early 1980s as many have stopped looking for work. As a result, further reductions in unemployment may be unlikely, even if the economic recovery gains momentum. Further, corporate profitability in the U.S. remains at close to record highs mainly due to cost cutting by companies. Going forward, little room remains for companies to further reduce costs, suggesting that continued profitability will need to come from other sources (e.g., capital investment).

In February, European banks took advantage of the second round of cheap three-year loans offered by the European Central Bank (ECB) as part of their long-term refinancing operation (LTRO) program, bringing the total to date to over €1 trillion (approx. $1.3 trillion). This helped to ease fears over a bank liquidity crisis in Europe, but did not address the underlying solvency issues in the region. In March, Greek's second bailout was approved totaling €130 billion (approx. $172 billion) to be paid in installments conditional on the Greek government implementing additional austerity measures. In the short-term, such austerity measures may further restrict economic growth as public sector jobs and wages, as well as social welfare programs, are cut.

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Growth in the emerging economies has slowed recently, but remains well above that of the developed world. Tight monetary policy and decreased demand for exports from the developed world have been the main drivers of the recent slowdown. In China, inflation has declined recently from over 6.0% to close to 3.0% as the government has increased bank reserve requirements and interest rates in part to cool off the real estate market. China's apparent ability to harness inflationary pressures has increased hopes for a "soft landing" and shifted the focus instead to the possibility of a transition in government policy to a more stimulative regime. However, monetary policy is by no means an exact science, particularly in a large and complex economy like China. Loosening monetary policy preemptively could refuel the residential real estate bubble.

Market Review

Market confidence carried over from the prior quarter, as global equity markets continued to rebound from their September lows. After posting the weakest returns in 2011, emerging market equities were the top performers during the first quarter, advancing 14.1%. The U.S. equity market, as proxied by the Russell 3000, returned 12.9% and developed market foreign equities recouped the majority of their 2011 losses, with the MSCI EAFE gaining 10.9%. Although these results are a welcome development for investors, we should note that 2011 also started off strongly (world markets gained +8.7% through April[1]) but ended the year down over 7%.

The yield on the 10-year Treasury bond increased to 2.2%, as investors shifted into riskier investments. Elsewhere in fixed income markets, spread sectors outpaced government bonds during the period. Emerging markets debt led all fixed income markets, returning 8.3%, followed by high yield bonds, which returned 5.3%. The Barclays Aggregate index, a proxy for the broad U.S. investment grade bond market, and the Barclays TIPS index, posted modest gains, up 0.3% and 0.9%, respectively.

Closing Thoughts

Although recent market performance has been strong, there still remain many unresolved, significant issues for the global economy, each of which has the potential to cause disruptions in 2012. In light of these uncertainties, we continue to recommend clients position their portfolios defensively by avoiding "overweights" to riskier asset classes through regular rebalancing.

We look forward to meeting with you to discuss in more detail the markets, the economic environment and most importantly your portfolio(s). At your meeting, or beforehand, when appropriate, we will be sure to share any applicable recommendations for your portfolio(s). In the interim, please do not hesitate to contact us with questions.

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[1] As proxied by the MSCI ACWI index.