MURRAY
INVESTMENT MANAGEMENT

2nd Quarter 2012 Update

Economic Review

U.S. GDP in the 1st quarter was revised down to 1.9% which was weaker than expected, and 2nd quarter economic data was mixed with the net result pointing to continued modest growth. Other parts of the world (China and Europe) are also slowing and renewing concerns for a potential global slowdown.

The European debt crisis (Greece and Spain in particular) and weak U.S. employment growth were two of the more significant stories during the 2nd quarter. The potential exit of Greece from the European Union and a likely European recession caused significant market volatility, but the crisis seemed to be temporarily averted as European leaders agreed on additional stimulus at the end of the quarter.

The unemployment rate remained at 8.2%, but April and May U.S. employment numbers were weaker than expected and averaged 73,000 per month compared to 225,000 per month during the 1st quarter. Given the impact that consumer spending has on the economy, employment weakness is a significant concern for long term, sustainable growth.

In an attempt to drive down long-term interest rates and stimulate economic growth, the U.S. Federal Reserve extended its "Operation Twist" strategy until the end of the year and kept short term interest rates near 0%. There is growing concern that the Fed is losing its ability to stimulate growth as the impact of these accommodative measures is becoming questionable.

Equity Market Performance

	QTD	YTD
S&P 500	-2.75%	9.49%
MSCI EAFE (International index net return)	-7.13%	2.96%

Broad U.S. equity markets were volatile and ended the quarter down but have posted strong results for the first half of the year. Concerns about Europe and a synchronized global slowdown weighed on markets during the quarter, but a potential short term resolution out of Europe led to a very strong rally on the last day of the quarter.

Large cap securities generally outperformed Small and Mid caps while the Financial, Technology and Energy sectors were the weaker sectors during the quarter. Oil prices retreated in the face of reduced global demand and increased U.S. supply, which drove the Energy sector down.

Europe has weighed on equity markets for the last year and led the broad International markets to underperform U.S. markets. The broad International markets have, however, posted positive results year to date.

Bond Market Performance

	QTD	YTD
Barclays US Aggregate Bond (Broad Bond Market)	2.06%	2.37%
Barclays Municipal	1.88%	3.66%
Barclays US Treasury Long	10.57%	4.16%
Barclays US Corporate	2.52%	4.65%
Barclays US Corporate High Yield	1.83%	7.27%

The broad bond market was up during the quarter, and U.S. Treasuries were particularly strong as investors flocked to the safety of these securities. This flight to safety caused the 10 year Treasury to trade below the historically low 1.5% level before closing the quarter at 1.67%.

Economic Outlook

U.S. economic growth has slowed but should continue to grow modestly through the end of the year. Other global economies are also slowing with particular concerns in Europe and China. Given the global nature of our economic system, a slowdown in any major country has the potential to impact other parts of the world.

The largest concern for the U.S. is the impending year-end "fiscal cliff" which includes mandatory spending cuts, tax increases and reduced jobless benefits. If not addressed by Congress, these three issues will clearly slow the economy, but it would not be surprising to see decisions on these issues temporarily extended so that the new Congress can address them early next year.

In addition, U.S. businesses seem to be reluctant to hire and spend given the potential "fiscal cliff" and other uncertainties related to the tax code, health care and regulatory environment. The Supreme Court affirming President Obama's health care plan would seem to provide some clarity but continues to cloud the outlook given the potential for its repeal. The November elections should help clarify the health care debate and these other issues.

The more positive elements of the U.S. economy include cheaper gas prices, a modestly improving employment situation, a housing market that appears to be getting better and a generally strong corporate sector. All of these areas are positive for consumer spending and economic growth, and continued improvement could lead to a more robust economic environment.

Source: standardandpoors.com, bls.gov, Morningstar, bea.gov, cnbc.com, wsj.com, federalreserve.gov and treasury.gov
The performance data shown represents past performance, which is not a guarantee of future results.
Return data is as of 06/30/2012. Except as noted, index returns are Total Returns.

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Market Outlook

Equity markets will likely continue through the end of the year with increased volatility primarily due to the following uncertainties:

1. U.S. Presidential and Congressional elections
2. Potential slowing of corporate earnings
3. European debt crisis
4. U.S. fiscal cliff

Even with all of this uncertainty, equity markets appear to be reasonably valued but are being driven by the latest news headlines. Corporations are generally doing well, and continued earnings growth could lead equity markets higher, but the political stalemate in Washington is giving corporate leaders pause. When some of the above mentioned issues are resolved, corporations may be more inclined to spend and hire which would be very favorable for the economy and markets.

With interest rates at historically low levels, the fixed income space is generally less attractive than equity markets. U.S. Treasury securities should remain in a trading range in the short term, but longer term, they do not look to be attractively priced. Treasury securities have generally rallied when investors are fearful and pulled back when equity bulls prevail. Shorter term fixed income and cash seem to be reasonable fixed investments in this environment.

Murray Investment Management

If you would like help with establishing an investment plan or would like to schedule a portfolio review, please give us a call. Also, please pass along our name to anyone that may be in need of investment advice.

Source: standardandpoors.com, bls.gov, Morningstar, bea.gov, cnbc.com, wsj.com, federalreserve.gov and treasury.gov
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