# MainStreet Advisors
# Financial Market Update

June 10, 2011

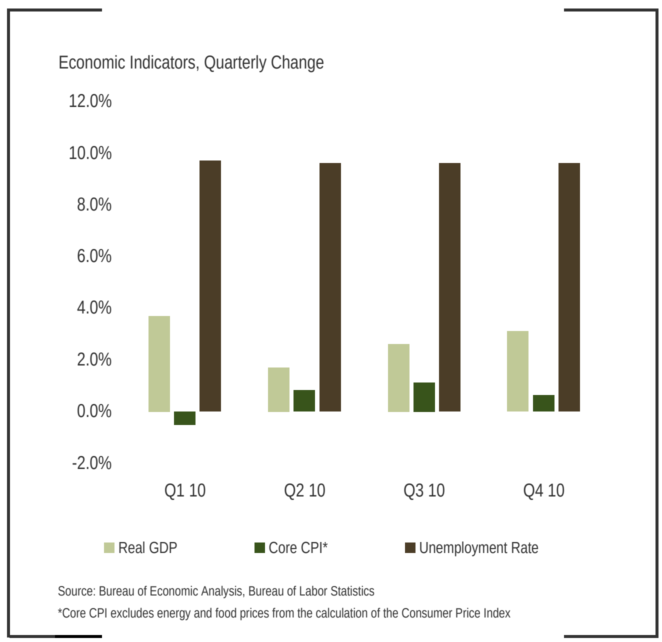

## Economic Update

Fed Chairman Ben Bernanke gave a gloomy speech this week regarding the outlook for the U.S. economy. He said the economy "is still producing at levels well below its potential" and called the uneven economic recovery "frustratingly slow." He blamed the weak first quarter on supply chain disruptions in Japan and also said the depressed housing market has been a big factor in the weakness of the recovery. The market was looking for hints of the possibility of a third round of quantitative easing, and while, he did indicate monetary policy will remain accommodative for an extended period, it seems QE3 is unlikely.

The U.S. trade deficit narrowed slightly in April, falling to $43.7 billion from a revised $46.8 billion gap in March as exports increased and imports declined, according to a report from the Commerce Department. This is likely a temporary improvement, as the decline in imports of automobiles, parts, and engines as a result of the supply problems in Japan accounted for 90% of the change. Meanwhile, higher oil prices seem to have curbed consumption and driven a $2.4 billion cutback in oil imports. This was in contrast to March, when high oil prices were blamed for a widening of the trade deficit.

The price of goods imported into the U.S. rose for the eighth consecutive month, according to a report from the Labor Department. Despite a drop in fuel prices, the import price index rose 0.2% in May driven by higher costs for auto parts and cotton apparel. Prices are now 12.5% higher than a year ago. Export prices were also up 0.2% last month and up 9.0% for the past 12 months.

Initial jobless claims edged up 1,000 to 427,000 for the week ended June 4, according to the Labor Department. This was higher than most economists expected and the ninth straight week that claims came in above the 400,000 mark. Ben Bernanke remarked that the "jobs situation is far from normal" and noted his concern over the high level of long-term unemployment in his speech, pointing out that nearly half of the unemployed have been jobless for more than six months.




Source: Bureau of Economic Analysis, Bureau of Labor Statistics
*Core CPI excludes energy and food prices from the calculation of the Consumer Price Index

| | | |
|---|---|---|
| June 7th | ICSC-Goldman Same Store Sales, Wkly. Chg. | 0.4% |
| June 7th | Consumer Credit, April Monthly Change | 6.3B |
| June 8th | MBA Purchase Applications Index, Wkly. Chg. | -4.4% |
| June 8th | EIA Petroleum Status Report, Wkly. Chg. | -4.8M Barrels |
| June 9th | International Trade Balance Level, April | -43.7B |
| June 9th | Initial Jobless Claims (Week ending 6/4) | 427,000 |
| June 9th | EIA Natural Gas Report, Wkly. Chg. | 80 bcf |
| June 10th | Import Prices, May Monthly Chg. | 0.2% |
| June 10th | Export Prices, May Monthly Chg. | 0.2% |

Source: Bureau of Economic Analysis, U.S. Department of Commerce, Federal Reserve Banks, U.S. Department of Labor, U.S. Department of Commerce, The Conference Board, the National Association of Realtors, the National Association of Home Builders, the European Central Bank.

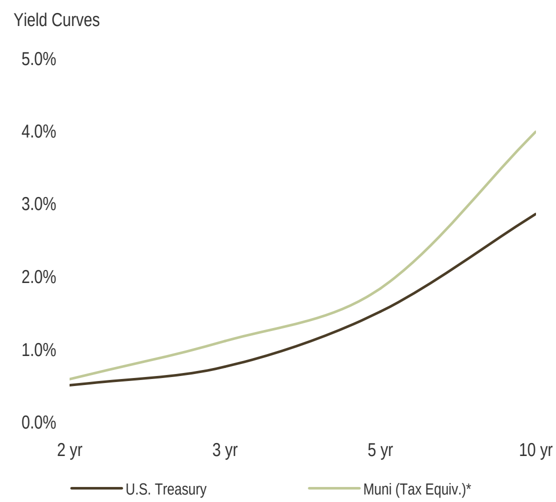
## Bond Market Update

Demand for bonds remained robust as U.S. Treasuries rallied on speculation the U.S. economic recovery may lose momentum as the government and central bank curtail stimulus measures. The strong wave of buying pushed trading volume in Treasuries to their highest level since February 2008. The Federal Reserve released its final schedule of operations under its $600 billion bond purchase program, saying it will purchase $50 billion of securities through the end of June. In an effort to maintain accommodating monetary policy, the central bank will continue to reinvest proceeds from maturities in its agency and mortgage-backed holdings into Treasuries.

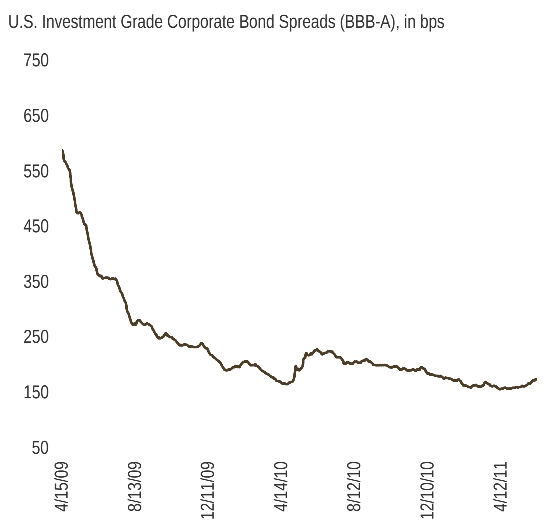
Meanwhile, a rally in corporate bonds has pushed the Barclay's U.S. Corporate Investment Grade Index higher by 9.11% over the last 12 months. A driver of strong demand in this sector has been a focus on deleveraging in the private sector, with investors redeeming collateralized mortgage-backed securities (CMBS) and other structured asset classes for corporate bonds. Fundamentals for investment grade companies increased incrementally during the first quarter of this year on the back of strong earnings. Median net leverage ratios declined significantly to levels not seen since 1994, spurred by the high post-crisis cash positions high grade companies continue to maintain. For comparison, the median level of cash as a percentage of assets has increased to 4.56%, well above the pre-crisis high of 2.85% set in 2004.

| Issue | 6.3.11 | 6.10.11 | Change |
|---|---|---|---|
| 3 month T-Bill | 0.04% | 0.05% | 0.01% |
| 2-Year Treasury | 0.45% | 0.41% | -0.04% |
| 5-Year Treasury | 1.65% | 1.58% | -0.07% |
| 10-Year Treasury | 3.04% | 2.99% | -0.05% |
| 30-Year Treasury | 4.25% | 4.18% | -0.07% |

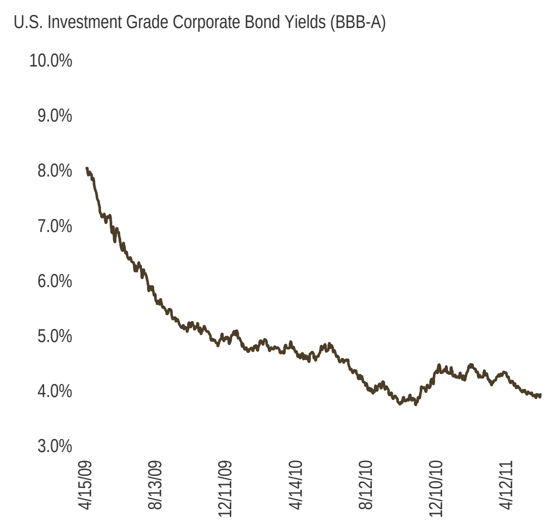
Source: Bloomberg, FTN Financial, The Wall Street Journal, U.S. Department of Treasury.




Source: U.S. Department of Treasury, Standard & Poor's, FTN Financial
*Taxable Equivalent rate is calculated by using a 35% tax margin




Source: Merrill Lynch




Source: Merrill Lynch

## Stock Market Update

The market selloff continued this week as Thursday was the only day with positive returns. The Dow closed up 75 points on Thursday while all but one of the S&P sectors advanced on positive trade deficit news. The relief rally fizzled in the last half-hour of trading and investors unloaded stocks on Friday due to continued worries about the recent slowdown in economic growth. The Dow fell below 12,000 on Friday to close down for the sixth straight week, the longest weekly losing streak for stocks since the fall of 2002.

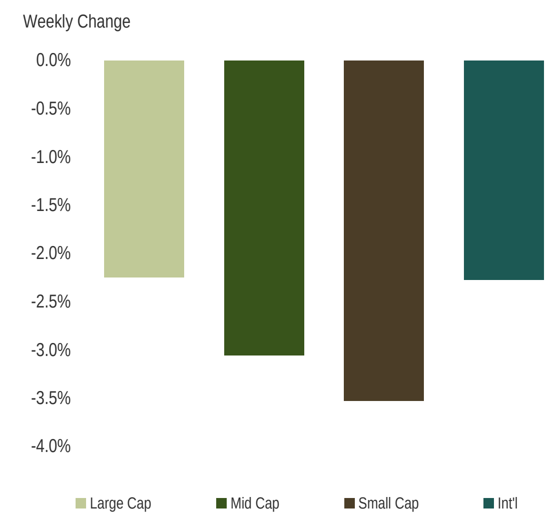
Financial stocks were especially weak on Friday. Travelers fell 2.7% after the company said that natural disasters in April and May cost the insurance company close to $1 billion. Energy stocks were also weak amid reports that Saudi Arabia would unilaterally increase oil output driving crude oil prices lower, to near $99 a barrel. An OPEC meeting earlier in the week failed to reach an agreement to increase oil production. Also affecting the energy sector on Friday was news that China's oil imports in May rose 21% over last year, demonstrating that higher oil prices are not dampening China's demand for oil.

For the week, The Dow Jones Industrial Average closed at 11951.91 down 1.64%. The broader S&P Index ended the week at 1270.98, a decline of 2.24%. The NASDAQ closed at 2643.73, down 3.26%. Overseas developed markets as measured by the MSCI EAFE Index fell 2.27% for the week. Defensive sectors such as health care, utilities, and consumer staples outperformed once again. Domestic small cap stocks were especially weak as the Russell 2000 Index declined 3.53%.

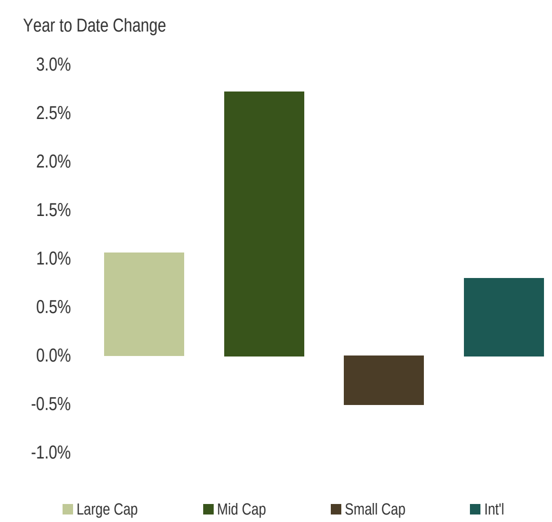
Stocks of note this week include McDonald's (MCD) whose same store sales increased below expectations. Exxon Mobil (XOM) reported three major oil discoveries in the Gulf of Mexico.

| Issue | 6.3.11 | 6.10.11 | Change |
|---|---|---|---|
| Dow Jones | 12,151.26 | 11,951.91 | -1.64% |
| S&P 500 | 1,300.16 | 1,270.98 | -2.24% |
| NASDAQ | 2,732.78 | 2,643.73 | -3.26% |
| Russell 1000 Growth | 605.29 | 583.43 | -3.61% |
| S&P MidCap 400 | 961.26 | 931.94 | -3.05% |
| Russell 2000 | 808.17 | 779.68 | -3.53% |
| MSCI EAFE | 1,701.51 | 1,662.91 | -2.27% |
| MSCI Small Cap | 1,158.96 | 1,142.25 | -1.44% |

Prices reflect most recent data available at the time of publication
Source: Bloomberg, Russell Investment Company, Standard & Poor's, Morgan Stanley Capital International, The Wall Street Journal, MarketWatch.



Source: Standard & Poor's, Russell Investment Company, MSCI



Source: Standard & Poor's, Russell Investment Company, MSCI

## Alternative Investments Market Update

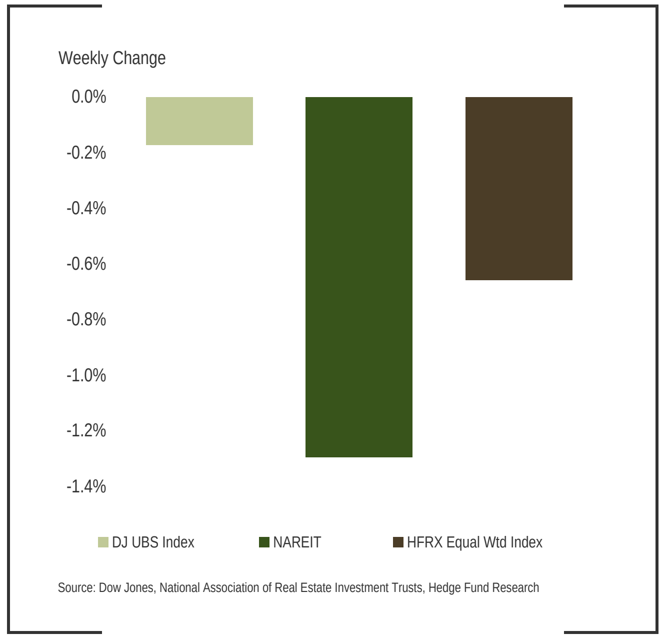
Crude oil dropped 1.45%, or $10.20, this week, settling at $99.01 a barrel, thanks in large part to Saudi Arabia announcing an increase of 10 million barrels a day in oil production over the next month. With the dollar on the rise, gold ended the week down 0.66%, closing at $1,532.20 an ounce. One of the lone bright spots in commodities was sugar, which gained 2.46%, settling at 24.54 cents a pound, as production continues to fall short of expectations in Brazil.

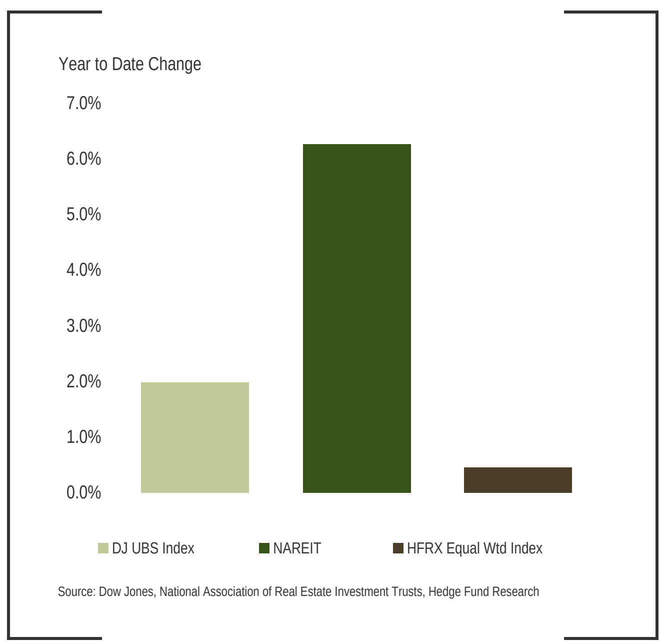
Federal Reserve Chairman Ben Bernanke stated this week that commodity prices are being driven primarily by global supply and demand and aren't a threat to major acceleration of inflation. He noted that as long as inflation expectations remain stable and well anchored, and commodity-price increases eventually stabilize, then this will not be reflected in a standard increase in inflation. "I think the increase will be transitory, that it will pass, and we will go back to a level of inflation that is consistent with our price stability mandate," stated Bernanke. Even with his inflation outlook, "sustained rises in the prices of oil or other commodities would represent a threat both to economic growth and to overall price stability, particularly if they were to cause inflation expectations to become less well anchored. We will continue monitoring these developments closely and are prepared to respond as necessary to best support the ongoing recovery in a context of price stability."

According to a report from the Economic Times, hedge fund managers are beginning to take on another title, that of a local banker. With traditional lenders continuing to avoid risky borrowers, hedge funds are stepping in to fill this void. However, the lending force also poses a significant risk to these companies, given the unregulated nature of this relatively "new" banking system. Being a last resort lender, these funds typically charge interest rates that are several percentage points higher than banks. Loaded up with high-cost loans, borrowers may find themselves falling deeper into debt, or even bankruptcy. To put this into perspective, over the last year, Rentech, an energy business based in Los Angeles, has been borrowing from a group of funds at an interest rate of 12.5%.

| Issue | Previous Week | Current[1] | Change |
|---|---|---|---|
| Gold | 1,542.40 | 1,532.20 | -0.66% |
| Crude Oil Futures | 100.47 | 99.01 | -1.45% |
| Copper | 412.10 | 404.25 | -1.90% |
| Sugar | 23.95 | 24.54 | 2.46% |
| HFRX Equal Wtd. Strat. Index | 1,180.25 | 1,172.50 | -0.66% |
| HFRX Equity Hedge Index | 1,152.36 | 1,136.04 | -1.42% |
| HFRX Equity Market Neutral | 1,031.65 | 1,022.14 | -0.92% |
| HFRX Event Driven | 1,412.41 | 1,401.52 | -0.77% |
| HFRX Merger Arbitrage | 1,544.31 | 1,536.91 | -0.48% |
| Dow Jones UBS Commodity Index | 165.89 | 165.60 | -0.17% |
| FTSE/NAREIT All REIT | 144.67 | 142.80 | -1.29% |

1 Prices reflect most recent data available at the time of publication
Source: Dow Jones, National Association of Real Estate Investment Trusts, Hedge Fund Research, Bloomberg, The Wall Street Journal, The International Monetary Fund.



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