C Y P R E S S
ASSET MANAGEMENT, INC.

MARKET COMMENTARY **APRIL, 2011**

The S&P 500 enjoyed its best first quarter since 1998, rising 5.4%, led by the energy, materials, and industrial sectors of the market. Investors certainly had a lot to digest, between the unrest in the Middle East and North Africa, the tragic sequence of disasters in Japan, the ongoing worries about the solvency of peripheral Europe (Portugal is the latest to ask the ECB for help) and the showdown over the U.S. federal budget deadline. The latter foreshadows the much larger issue of the unsustainable size of the federal budget deficit and future entitlement spending, which is exerting ongoing pressure on the dollar.

Historic Global Events Dominate 1Q 2011 And Influence Outlook

The biggest story of the quarter was the historic popular uprisings across the Middle East: regime change in Egypt, civil war in Libya, and popular unrest that extended even into Saudi Arabia. The turmoil sent oil prices sharply higher, rising 15% in the quarter to $105 (WTI).

Japan's response to its crisis has been slowed by the nuclear power disaster left in the tsunami aftermath. A significant part of Japan's manufacturing base has been at least partially disrupted and this will negatively impact a number of industries over the next 3 to 6 months, particularly the supply chains supporting the electronics and auto industries. As a result, Japan will be a headwind to global growth in the second quarter, but is unlikely to have a long term impact on the overall global economy. The Japanese will rebuild, the crisis could actually serve to galvanize their economy which has been moribund for two decades, and the rebuilding process should be a boost to growth in the second half of the year. Reconstruction could prove particularly meaningful to the industrial, materials and resource sectors of the market.

All of these concerns, the instability in the Middle East, crisis and economic disruption in Japan, the European debt crisis, and the looming battle over the U.S. budget deficit and debt level, are ongoing and are likely to continue to pressure the market over the next few months. Japan and higher oil prices should both serve to restrain growth in the second quarter. In addition, QE2 (the Feds program to buy $600 billion of treasuries) is concluding at the end of June. The last time the Fed cut back on quantitative easing at the end of March 2010, the economy slowed and the S&P 500 pulled back some 10%. The hope is that this time around the economy is strong enough to grow on its own without monetary stimulus and that a self-sustaining recovery is underway. Given a continuation of economic growth into the second half, the withdrawal of stimulus and declining demand for U.S. debt could cause bond prices to fall and interest rates to rise. Rates are artificially low today and higher rates, if they do not occur too abruptly, would actually be a positive sign of a more normal and healthy economy. All factors considered, the near term upside for stocks would appear limited as these challenges play out in the second quarter and the gains of the prior two quarters are consolidated.

Resilient Global Economy Driven By Emerging Markets

Through it all, the resilient global economy and its corporate beneficiaries have remained healthy. Solid growth in emerging economies and a slowly but steadily improving domestic economy describe the current environment. We hear a lot of talk about the global imbalances (e.g. the U.S. fiscal and trade deficits contrasted with China's trade and fiscal surpluses), and the dichotomy between an aging and debt burdened developed world and a younger, dynamic and cash flow positive emerging world. But there is a more positive side to the oddly balanced modern global economy. Slow growth in Japan, Europe and the U.S. has helped to keep inflation and interest rates low while the emerging economies continue to fuel global growth and trade.

Rise Of Consumer Spending In Emerging Markets

Consumer spending is rising in emerging economies and is now larger than U.S. consumer spending. In just ten years, emerging market consumer spending has risen from 22% of total global consumer spending to 34%. This is supported by faster employment growth and population growth in emerging market countries. While global population growth has slowed, emerging market population continues to grow at more than double the rate in developed countries, and now represents over 85% of the global population (i.e. 6 billion out of 7 billion).

The best illustration of the rise of consumerism in emerging markets is the auto. EM auto sales are now greater than in developed countries. Just ten years ago they were about 25% of total global auto sales, today they are just over half. China is now the biggest auto market in the world by volume, currently running at around 18 million units in annual sales, almost 5 million above current U.S. units.

Shifts In Global Economy Favor Industrials & Resources

In a big picture sense, the global economy was led by U.S. consumption and consumer demand in the 1980s and 1990s. A decade ago, the engine of growth shifted to China and the emerging markets. Phase one has been industrialization and urbanization and rising standards of living. Phase one continues, but phase two has begun which involves greater consumption and rising consumerism (from autos and appliances to personal care and higher protein diets and retail goods). Merrill Lynch notes that today "Asia emerging market" is now bigger than the U.S. and is expected to grow at 7.5% in 2011.

We are ultimately becoming a supplier to the emerging markets: think Germany for manufacturing, Canada and Australia for resources. The result is slower growth in the U.S. and most other developed economies, and growth that is more tied to foreign markets, global trade, and business investment spending. This transition explains part of the reason why the U.S. consumer and U.S. economy "feels so bad" despite the robust global environment and record corporate profits.

In today's emerging market driven global economy, U.S. and international global industrial companies should continue to outgrow the U.S. and other developed nation economies. Your portfolio is positioned to benefit from its exposure to more rapidly growing foreign markets. The global economic environment is particularly favorable for resources, materials, and industrials;

those companies supplying the bricks and mortar and the infrastructure and industrial "know how" to emerging markets. One example is energy, where we should see record demand for oil in 2011. EM demand is likely to keep oil prices in a range of $80 to $110 barring a double dip global recession. American prowess in electronics, computer, and communications technology is well recognized but we are no less a leader in the also vitally important energy field. Most do not realize that today roughly half the rigs that operate in the world operate in the U.S., and if you add Canada, we represent some 65% of the global rig count. Just as significantly, we also possess most of the world's know how in finding and developing oil and gas.

U.S. Debt & Budget Deficit Preview

The federal budget deficit shapes up to be the critical political and market shaping event of the next couple of years. The solution to both the short and long term federal deficit requires serious entitlement reform. **All we really need to know is this: entitlement spending plus interest payments alone should exceed the total revenue of the federal government in 14 years, 2025, per the CBO**. We can't pay for the social security and healthcare benefits currently promised citizens when they retire. There is time and there are straightforward solutions to solving our debt problem, but they require hard and difficult decisions out of Washington. There will be no artificial time clock like with the recent annual budget battle or the debt ceiling, just a global super power reduced to the brink of default and bankruptcy, unable any longer to sell its debt to China or anyone else. Let's hope it does not come to that. In the meantime, we encourage you to visit the following link for a pretty thorough and balanced analysis of the federal debt crisis: http://www.kpcb.com/usainc/USA_Inc.pdf

Conclusion

In a potentially historic shift, the industrial, resource (in the U.S. think oil and gas shale driven energy renaissance, in Australia think iron ore and mining, in Canada think both), and business spending/investment side of the U.S. economy have changed places with the consumer, housing, and construction. Your portfolio reflects these global trends. In particular we have recently been adding to the industrial sector of our portfolios. S&P 500 profits should continue to outpace the U.S. economy based on its strong linkage to the global economy. Stock valuations remain reasonable by historic measures, balance sheets are strong, and cash flow supports dividend growth that should be well in excess of profit growth (consensus forecast is for 10% to 12% growth in S&P 500 operating profits in 2011). Nevertheless, don't expect much from stocks in the second quarter beyond the consolidation of recent gains. The issues and risks highlighted in the beginning of our commentary will take time to clarify and resolve, potentially setting up for a stronger second half of the year.

Cypress Asset Management – April 2011

Good News

China

New highs for Chinese Yuan, up 4% year over year. *ISI 4.6.11*

Yuan currency continues to grow in use as a global currency: Barclays Capital will expand its offshore Yuan foreign exchange product range. Products will include offshore Yuan deliverable spot, forward and swaps against G10 and Asian currencies. *Dow Jones 4.11.11*

Auto sales in China rose 32% in 2010. 46% in 2009 when sales passed the US to become the world's largest.

GM sold more cars in China than in the US for the first time. *AP 1.24.11*

China now the biggest trading partner for Australia, Japan, Korea, India, Russia, and South Africa. China has replaced US as the top export market for Brazil. *WSJ 3.11.11*

India

India now home to 17 percent of the world's population at 1.2 billion in 2011. Could overtake China as most populated country by 2030.

Emerging Market

Emerging Market consumer spending is now larger than US consumer spending. EM consumer spending now same size as all developed economies ex US. *ISI 10.27.10*

Emerging Market employment is now 83% of world employment. *ISI 10.27.10*

Emerging Market Auto Sales now as large as developed world auto sales. *ISI 10.27.10*

"Asia Emerging Market" is now bigger than the US economy and expected to grow at 7.5% in 2011. *BAML 4.1. 11*

Global Finance Gets More Global

- Coach, L'Occitane International and Prada indicate interest in Hong Kong listings. *Fox Business 4.11.11*
- Australia Exchange rejects offer from Singapore Exchange. *WSJ 4-2011*
- Four Japanese companies and two South Korean companies buy a 15% stake in Brazilian minerals company, CBMM. *Reuters 3.2.11*
- NYSE Euronext rejects takeover offer from NASDAQ ICE, favors Deutcshe Boerse offer. *Bloomberg 4.3.11*
- Freeport-McMoran and Xstrata positioning for potential takeovers as Chinese metal demands increases and financing conditions improve *Bloomberg 4.6.11*

Bad News

China

China's central bank lifts base lending rate by 25BPS to 3.25%. One year lending rate 25BPS higher to 6.3%. *Marketwatch 4.11.11*

Higher oil prices and Japanese earthquake impact China vehicle output, limit March sales increase to 5.4%. Chinese auto association said this year's sales growth might fall short of the previous estimate of 10-15%, sales still running at impressive 18 million annual rate.

China posted its first quarterly trade deficit in six years for 1Q 2011. *Financial Times 4.9.11*

Middle Eastern Dominoes Start to Fall

- American ally Mubarak regime falls in Egypt after 30 years in power.
- Libyan revolt outcome still in flux as civil war provokes NATO intervention.
- Tunisia President of 28 years flees to Saudi Arabia.
- Bahrain – Saudi Troops quell violence in this home to the US 5th Fleet.
- Yemen – Leader stands down.
- Syria – Huge popular protests, citizens are repressed by government troops.
- Saudi Arabia – Saudis draft over 10,000 troops to quell "day of rage".

Europe

ECB tightens interest rates for first time since 2008, Euro strengthens.

Euro Debt Crisis continues:
 Portugal government falls.
 Portugal asks European Union for debt bailout.

ECB warns of rising commodity prices. *FT 1.24.11*

Europe's $2 Trillion in Distressed Debt larger than US. *Bloomberg 4.11.11*

Japan

Japanese magnitude 9 earthquake, one of the five most powerful since 1900, devastates northern part of island. Ensuing tsunami levels coastal towns and devastates Fukushima nuclear plant which remains uncontrolled.

Good News (continued)

United States

Dow settles above 12,000 level for first time since June 19, 2008. *Market Watch 2.1.11*

Many US economic indicators showing multi-year growth:

- Rig count continues to surge to new high. *ISI 4.11.11*
- Railcar loadings make new highs. *ISI 4.11.11*
- ISI Trucking Survey hits 5 year high. *ISI 3.29.11*
- S&P Operating EPS are likely to reach a record $95 this year and $103 in 2012. *ISI 3.28.11*
- US initial employment claims decline *ISI 3.19.11*
- Real GDP in 4Q 2010 moves above 2007 peak, economy in expansion. *ISI 1.28.11*
- Chain store sales stronger than expected.
- US Household employment improving off bottom. *ISI 3.11*
- C&I loans plus Commercial Paper made new high. *ISI 4.11.11*

ISI state income tax receipts survey increased to 54.6 in March 2011 from recession low of 7.9.

S&P dividends in 1Q surged 47% annualized rate quarter over quarter. *ISI 4.11.11*

JP Morgan leads $22 billion increase in bank dividend payouts and buybacks. *Bloomberg 3.19.11*

Over $90 billion in M&A deals in the two weeks ended 4.11.11. *ISI 4.11.11*

Energy Renaissance

- US Oil Production revives despite offshore disruption. US oil production rose to its highest level in decade.
- US was largest contributor to the increase in global oil supplies from 2009 to 2010. US is on track to increase domestic production by 25 percent by the second half of the decade due to "unconventional" techniques. *FT 3.3.11*
- Noble Energy wins first post-spill deep-water drilling permit. Deep water activity starts up again in Gulf after almost year long shutdown. *WSJ 2.28.11*
- US accounts for fully one half of total global rig count, US & Canada combined account for 65%. *Baker Rig Count 3-2011*

Bad News (continued)

United States

ISI lowers 2Q 2011 US GDP to +2% from +3%; still forecasts 3.5% for 2nd half of year, but with downside risk.

US Balance Sheet Is Weak

Federal Debt ceiling grows from $3 trillion in 1990 to **$14 trillion**. Treasury officials push lawmakers to raise debt ceiling by next month. *WSJ 4.4.11*

US runs $222.5 billion deficit in February, highest ever for any month. *WSJ 3.10.11*

Budget deficits for 2009-2011 on track to average **-$1.3 trillion** annually, 9% of GDP. *WSJ 3.10.11*

Entitlement spending plus interest payments alone should exceed the total revenue of the federal government in 14 years, 2025, per the CBO. *CBO 2011*

US: 2X more people work for government (22.5 million) vs. manufacturing (11.5 million). *FT 3.25.11*

Half of $2.2 Trillion cost of state and local government is the tab for salary and benefits. *WSJ 4.1.11*

Walmart CEO expects inflation. *USA Today 3.30.11*

Marc Faber says Buying Long Term Treasuries is "suicidal". *Bloomberg 1.3.11*

California faces $28 Billion Budget Gap. *Bloomberg 1.3.11*

Housing to remain depressed in 2011. *ISI 3.3.11*

More people collect food stamps than live in California and Texas combined. *Good Website 2.1.11*

Economy faces test with end of QE2 in June. *Huffington Post 4.12.11*

Pick 'Em – Could be Good, Could be Bad

- **Dollar Down, Commodities UP. The decline in the dollar is one of the factors driving up commodity prices.**
- **Energy and copper prices could be at levels that can impact the economic expansion.** *ISI 4.11.11*

Follow The Money

Mergers and Acquisitions

Biggest Worldwide Announced Deals in the First Quarter, 2011
Ranked by deal value, net of debt as of announced date, in $ billions

Buyer	Seller	Deal Value ($B)
ATT (US)	T-Mobile(US)	39.00
Duke Energy (US)	Progress Energy (US)	13.61
Deutsche Borse	NYSE Euronext	10.48
Blackstone (US)	Centro Property (US)	9.40
Berkshire Hathaway (US)	Lubrizol (US)	9.21
Ensco (US)	Pride Intl (US)	7.49
Alpha Natural Resources (US)	Massey Energy (US)	7.08
Texas Instruments (US)	National Semiconductor (US)	6.50
Trian Fund Mgmt (US)	Family Dollar (92.15%) (US)	6.40
ProLogis (US)	AMB Property (US)	6.15
Ventas (US)	National Health Property (US)	6.12
Danaher (US)	Beckman Coulter (US)	5.78
Valeant Pharma Intl (Canada)	Cephalon (US)	5.70
PPL (US)	E.ON (UK)	5.66
DuPont (US)	Danisco (Denmark)	5.62
Telefonica (Brazil)	Vivo (37.75%) (Brazil)	5.54
PetroChina (China)	Encana (Cutbank Ridge 50/50) (Canada)	5.45
IPIC (UAE)	CEPSA (52.9%) (Spain)	5.36
LVMH (France)	Bulgari (Italy)	5.18
Vodafone (UK)	Vodaphone Essar (33%) (India)	5.00
Equinox (Australia)	Lundin Mining (Canada)	4.82
BHP Billiton (Australia)	Chesapeake shale assets (US)	4.75
Cliffs Natural (US)	Cons. Thompson Iron Mines (Canada)	4.70
Liberty Global (US)	Kabel Baden-Wurttemberg (Germany)	4.48
Emirate of Abu Dhabi (UAE)	Aldar Properties (UAE)	4.46
Daimler, Rolls Royce (Germany, UK)	Tognum (Germany)	4.39
Total		$198.33

Source: WSJ/Dealogic