

# MARKET UPDATE

MARCH 18, 2011

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## UPDATE ON JAPAN IMPACT

Japan is the world's third largest economy and an important center of production for electronic components, computers, and cars. The US and China are its most important trade partners, followed by South Korea, Taiwan, Hong Kong, Singapore, Thailand and Germany. The OECD reports that the four prefectures most affected by the earthquake account for 6% to 7% of Japan's population and economic output. This disaster will reduce Japanese economic activity until electricity and manufacturing can be restored, and reconstruction efforts add to output. DBS Bank of Singapore estimates that the disaster will cost the Japanese economy about \$100 billion or 2% of GDP, twice the impact of the Kobe earthquake, which cost 1.0% of 1995 GDP.

In the US, we anticipate slower price declines or even price increases for computers, smartphones, and televisions. Lumber and other materials prices could increase during the year as reconstruction begins. Auto prices may increase slightly as US imports of Japanese cars fall until manufacturing capacity is restored. Japan does not export commodities to any significant extent, but Bank of Japan monetary easing could result in higher prices globally of metals, foods and other goods. US exporters of food and heavy machinery could benefit from reconstruction efforts.

We have been in contact with many of your managers to learn about the potential impact on their portfolios, their views and prospective portfolio changes. The international equity managers are re-assessing their positions, particularly Japanese stock holdings. Most of the managers have been underweight Japan because of concerns over the country's slow growth, aging population and large fiscal deficit. For the time being, most long only managers are making modest portfolio changes. Some value oriented managers, however, are evaluating new opportunities given the stock market decline. Many hedge fund managers have reduced both long and short positions in Japan, with some benefitting from yen currency positions. The majority of managers expect volatility to remain high during this period of uncertainty.

Stratford will continue to monitor your portfolios closely, but recommend taking no action at this time.

Our sympathies go out to all of the individuals affected by this tragedy.