

Revitalizing America



Investment insights on the economy,
elections and policy choices

Presented by UBS Wealth Management Americas

Investment Summary

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Rick Rieder, Russ Koesterich, John Savercool and Mike Ryan

What can investors expect in this critical election year?

“While we are in the midst of a continuing, yet fragile recovery, much about the nation and the world remains unsettled.”

- Mike Ryan
Chief Investment Strategist
UBS Wealth Management
Americas

“We are more than three years removed from our country’s deepest recession since the Great Depression,” said Mike Ryan, UBS Wealth Management Americas’ (WMA) Chief Investment Strategist. “And while we are in the midst of a continuing, yet fragile recovery, much about the nation and the world remains unsettled.” The 2012 U.S. presidential elections come at a time of considerable voter concern over a wide range of issues, including the outlook for the U.S. economy, the trajectory of the federal government’s debt burden, the nation’s influence and competitiveness on the world stage and the unsettling fate of a series of entitlement programs for retiring Baby Boomers.

Ryan spoke with a distinguished panel of industry strategists during UBS WMA’s most recent event on Revitalizing America. Russ Koesterich, Global Chief Investment Strategist at BlackRock, Inc., Rick Rieder, Chief Investment Officer of Fixed Income at BlackRock and John Savercool, Senior Lobbyist with the U.S. Office of Public Policy for UBS Americas, shared their critical insights and perspectives about what to expect from the financial markets in this pivotal election year as well as investor portfolios in the coming months.

Market fundamentals and valuation are not enough this year

Historically, strategists have always looked to market fundamentals to guide investors. Given today’s dramatic developments unfolding in Washington and in the economy, this approach may no longer apply.

According to Mike Ryan, getting the fundamentals and valuation are not enough anymore and understanding policy dynamics is really critical. The upcoming elections and Washington policymakers today are influencing the economic issues in a truly unprecedented way.

When asked his views on potential election outcomes for the White House and Congress, Savercool pointed out that while it is still too early

to draw conclusions, at this point he expects President Obama to win re-election and the Republicans to retain the House and possibly even win a small majority in the Senate.

Savercool also believes that we're still months away from the elections and several defining issues for voters have yet to come into play—the most prominent being energy prices and healthcare. As we approach the crucial summer months, people will actually be paying more attention to what they're paying at the pump. This summer Congress will also have the chance to re-litigate the healthcare bill when the Supreme Court reviews its constitutionality.

“From a foreign policy standpoint, Iran may emerge as a major election issue.”

“At that time, both President Obama and the Republicans will make their case on what should happen with healthcare,” Savercool noted. “The unemployment rate at election time could also sway voters since employment is clearly a top of mind issue for Americans. And of course, from a foreign policy standpoint, Iran may emerge as a major election issue.”

- John Savercool
Senior Lobbyist
U.S. Office of Public Policy
UBS Americas Inc.





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- Russ Koesterich

Global Chief Investment Strategist
BlackRock, Inc.

Equity markets: focus on the energy sector, emerging and smaller, developed markets

Given that the post-election period may present several attractive equity opportunities, Russ Koesterich identified some likely “winners and losers.” He also referenced, however, the challenging economic scenario expected to unfold in January 2013, when the Bush tax cuts and unemployment benefits expire and roughly \$100 billion in budget cuts are scheduled to hit. “All told, you’ll have, according to economists, a \$600 billion fiscal drag,” said Koesterich, adding that, “an environment where consumers spend less while trying to pay down debt to sustainable levels relative to their income.”

In light of these events, he expects even slower U.S. economic growth. But he also foresees a “silver lining.” Corporate profitability is close to record highs. U.S. companies have more than \$2 trillion in cash. Rates are low and so is inflation. This has created a somewhat positive environment for the equity market as investors look to stocks for higher returns. Koesterich suggests individuals consider diversifying their equity portfolios outside the U.S. markets.

Emerging markets have improved considerably since last year and smaller developed markets, such as Canada, Australia, Norway, Singapore and Hong Kong, have weathered the financial crisis quite well. Koesterich is optimistic about the energy sector: “We’re seeing that oil prices are remaining high. It’s likely to stay that way for the next 5 or 10 years. The sector is cheap.”



Fixed income markets: rates are historically low—and could stay that way

“Monetary policy will need to transition to fiscal policy that doesn’t fuel inflation... I think we’ll talk more about inflation protection—it’s one of the things that will be top of mind for people, going forward.”

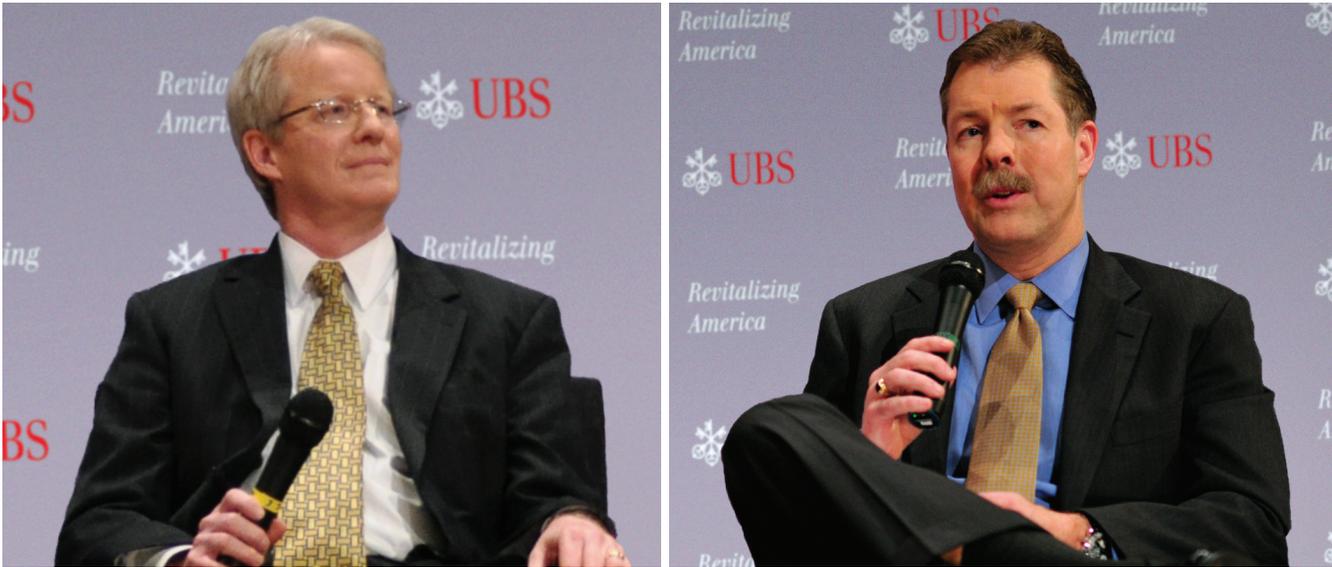
- **Rick Rieder**
Chief Investment Officer
Fixed Income,
BlackRock, Inc.

The fixed income markets ended 2011 as the best-performing asset class, but not without considerable anxiety over the debt ceiling debacle and the downgrade of U.S. sovereign debt. Ironically, U.S. Treasuries benefited the most from these circumstances. Against this backdrop, the compelling issue for the credit markets becomes whether today’s political dynamics might alter either the risk profile or different sectors of the fixed income markets.

Rick Rieder identified several key issues for debate on the campaign trail: the municipal bond deduction; the fate of refinancing; and Fannie Mae and Freddie Mac. “Equally important, is restoring lost income. Short-term yields out five years are trading virtually at zero percent given the Federal Reserve’s efforts to put significant liquidity into the system.”

Rieder went on to say that although everyone has been talking about the current “bond bubble” and how rates are poised to go higher, he has a different point of view based on a supply and demand scenario. The aging population with longer life expectancies will likely demand more fixed income product to meet their income needs—just as the supply is shrinking. Rates may drift a bit higher, but not by much. He recommends staying flexible in terms of the investments you choose in search of incremental yield.

He also noted that monetary policy will need to transition to a fiscal policy that doesn’t fuel inflation. “As you get into this election season, I think we’ll talk more about inflation protection—it’s one of the things that will be top of mind for people, going forward.”



The future political landscape: eventually finding common ground

Looking beyond the investment landscape to the future of the post-election political landscape, Ryan questioned whether or not it was possible for elected officials to come together across the partisan divide. Savercool was optimistic about the possibility of bipartisanship. “It’s generally easier to find agreement after an election—when voters just want results and they’re really tired of the politicking. So there could be a period of greater harmony. But to instill a longer-term bipartisan spirit in Washington, you really need voters to tell Washington what they want—more strongly than they’re hearing today.”

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We believe 2012 is a truly pivotal year politically and economically, with challenges expected to remain. To continue this conversation on the issues, the outlook and the opportunities, and to learn how they may impact your personal investment strategy, we encourage you to speak to your UBS Financial Advisor.

Ask for a copy of the current Wealth Management Research report: *Election Watch 2012, Perspectives on a critical political season*. For additional information on UBS Wealth Management America’s Revitalizing America initiative, visit our dedicated website at ubs.com/revitalizingamerica.

- **John Savercool**
Senior Lobbyist
U.S. Office of Public Policy
UBS Americas Inc.

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