

March 4, 2010

Updated MSCI All Country World Index Rankings (1-45)

The following report is Bretton Woods Research's quarterly ranking of the 45 countries that comprise the MSCI All Country World Index.

Improvements in the European variable along with the unrest in the Middle East and North Africa led to a reversal of fortunes for our last ranking as the developed world outperformed our favorite emerging markets. Between our last MSCI update on December 1 and this week, the top 20% and bottom 20% of the ranking delivered an average return of negative 2.6% and positive 16.1%, respectively. Not surprisingly, eight out of the top nine countries for the period were European. The exception was Russia, which is nominally European.

The key shift in the investment outlook for Europe began in late December when Brussels backed away from its shock therapy plans to reduce debt in the highly indebted PIIGS countries. The shift specifically occurred when Ireland was not required by Brussels to raise its 12.5% corporate tax rate as a condition of its bailout and was given 7.5 years to repay its lifeline. This was in stark contrast to the 3-year window afforded to Greece that was also attached to significant increases in personal, corporate, capital gains and dividend tax rates. Of course, it was critical that despite the raft of tax increases imposed on Ireland, the country was allowed to maintain its 12.5% corporate tax rate, which will keep significant amounts of "corporate production" within its borders.

There is now serious discussion within the EU to extend Greece's repayment schedule to 30 years. Should such an arrangement emerge, it would likely serve as a template solution for the rest of the PIIGS, which would stall shock therapy austerian policies, improve the growth outlook and thus the continent's various sovereign credit worries.

Despite the positive evolution of the European debt situation and the subsequent rebound in most European capital markets during the last three months, we do not think the region will necessarily outperform the rest of the world. For the most part, we see fiscal policy hemmed in by the fiscal conservatives that dominate policy in the European core, such as Germany, France and the Netherlands. And 'fiscal consolidation' will remain a headwind for the region.

The best fiscal policymaking on earth continues to come out of Asia where governments, including Japan's, are in strong competition for capital and talent. As a result, they are looking to enhance their attractiveness by reducing tax rates. Positive

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fiscal discussions in Indonesia, China and Japan are likely to help that region power-through the negatives of a weak-dollar, buoyant commodity environment. The improving fiscal discussion in Japan could even encourage Republicans and Democrats in Washington to enact corporate tax reform this year, which would be very bullish. As we have said before, though, we do not expect tax reform negotiations to start this month. Perhaps we will hear proposals beginning in April.

Aside from the select countries that are reducing tax rates and incentivizing risk-taking and production, it is also important to note that in a stagflation environment where high unemployment and rising prices continue to test governments in the third world, commodity-based economies in the developed world, especially those that are cutting taxes too, have an economic advantage and should outperform the rest of the world.

We fear that many emerging markets facing incipient inflationary pressures are on the brink of a major interest-rate hiking cycle. This is a misguided policy tactic in our view, and represents significant risk for economies such as Brazil and India. In the long-term, continued dollar weakness could put all major central banks on course for simultaneous interest rate increases, which would be similar to the period between 2007 and 2008 when all major central banks, i.e. the Fed, BoJ, PBoC, ECB, and BoE, were either raising rates or keeping rates elevated in an effort to *slow* their economies to keep general prices down. We believe that this was one important factor contributing to the financial crisis.

In the following ranking, we continue to highlight important developments and continuing trends around the world since our December 1 ranking. We remain bullish on those countries reducing tax rates and appreciating their currencies, such as in Asia. Tax increases or hawkish, anti-growth interest rate policies continue to factor strongly in our determination of the worst countries. Some European countries appear to be positioned for more austere pain and so their rankings have been downgraded accordingly.

Of course, as we noted in our recent assessment of the Libyan situation, there is a high probability that more civil unrest will emerge in other Muslim countries where there is a dearth of economic opportunity, including Iran, Pakistan and Oman. Consequently, investors must be on guard. Consistent with history, monetary extremes such as we have today are breeding vast economic and geopolitical crises. So our rankings should be considered as a guide under conditions where geopolitical tensions are at current levels.

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1	INDONESIA	10	JAPAN	19	NORWAY	28	SOUTH AFRICA	37	CZECH REPUBLIC
2	PERU	11	NEW ZEALAND	20	INDIA	29	TAIWAN	38	AUSTRIA
3	CHINA	12	COLOMBIA	21	BRAZIL	30	SWITZERLAND	39	NETHERLANDS
4	RUSSIA	13	HONG KONG	22	CHILE	31	TURKEY	40	ITALY
5	HUNGARY	14	KOREA	23	POLAND	32	FINLAND	41	SPAIN
6	CANADA	15	US	24	BELGIUM	33	IRELAND	42	PORTUGAL
7	PHILIPPINES	16	SINGAPORE	25	DENMARK	34	UNITED KINGDOM	43	FRANCE
8	MALAYSIA	17	ISRAEL	26	MEXICO	35	SWEDEN	44	GREECE
9	THAILAND	18	GERMANY	27	AUSTRALIA	36	MOROCCO	45	EGYPT

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1. INDONESIA (December rank: 1): Asia continues to be the one region on earth where enlightened tax policy holds sway, and Indonesia is a key example. Recently, Chief Economic Minister Rajasa cited the low corporate tax rates throughout Asia -- e.g. Singapore and Thailand's plans to respectively cut to 15% from 18% and 20% from 23% -- as a rallying cry to cut Indonesia's 25% corporate tax rate. We expect Indonesia will seek a 20% rate for 2012. This is clearly positive. Additionally, on monetary policy, rupiah strength is still considered an ally in the fight against inflation. Deputy Central Bank Governor Sarwono continues to argue that rupiah appreciation will help to keep 'imported inflation' in check. He also suggested recently that there will be a respite to the steady increases in the central bank's short-rates. He said, "If inflation behaves as I mentioned, I don't think we need to raise [rates] again." [Key Stats: Annualized CPI: 6.84% in January 2011; Benchmark rate: 6.75%, 25 basis points higher YTD; Forex: 2.45% appreciation versus USD in past 12 months.]

2. PERU (December rank: 4): We like the pro-growth pronouncements coming from the Peruvian government. While Chile responds to global inflationary pressures with higher interest rates, Peru's government is advertising that it would like to grow its way out of inflation. As a result, it has cut its VAT to 18% from 19%, as well as its financial transaction tax to 0.005% from 0.05%, and it has standardized capital gains tax rates at 5% versus rates that previously varied between 5% and 30%. Meanwhile, Peru's central banker Velarde has lately thrown cold water on the idea of rate hikes in the near future, acknowledging that higher fuel prices could slow the global economy. Peru's outlook is improving. [Key Stats: Annualized CPI: 2.17% in January 2011; Benchmark rate: 3.5%, 50 basis points higher YTD; Forex: 2.7% appreciation versus USD in past 12 months.]

3. CHINA (December rank: 20): The expected improvements in fiscal policy that we suspected would ensue following the June revaluation of the yuan now appear to be in play. Specifically, income tax thresholds will be raised and debated at the National People's Congress, which concludes on March 15. The details are not yet clear, but we

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expect the increases to be across-the-board, as they were in 2008. Additionally, researchers in the Ministry of Finance have recently recommended a reduction in China's top marginal income tax rate to 35% from 45% and some plan to automatically increase income tax thresholds for inflation. PBOC deputies suggest that boosting imports instead of suppressing exports would help redress imbalances in external accounts. While we don't believe 'balanced' trade accounts are the aim of a well functioning global economy, the formulation is part of the justification for further yuan appreciation, which we view as a positive. And discussion of yuan convertibility is being framed with respect to facilitating Chinese trade and investment due to high demand. This is the right way for China to proceed with internationalizing the yuan. Of course, we respect and hope that the Chinese continue to pressure the West toward monetary reform and a price rule before they commit to full-fledged convertibility. We remain bullish on China. We are moving China up in our ranking given the improving fiscal policy discussions in Beijing. [Key Stats: Annualized CPI: 4.4% October 2010; Benchmark rate: 5.56%, up 25 bps YTD; Forex: 2.5% appreciation vs. USD in past 12 months.]

4. RUSSIA (December rank: 23): The ruble has appreciated nearly 4% against the dollar during the last 12 months. To its credit, Russia's Bank Rossii continues to refuse stemming those gains. According to Finance Minister Kudrin, the central bank will favor a "very flexible" exchange-rate policy in an effort to contain inflation. CPI is rising nearly 10% year-over-year. Economic Development Minister Nabiullina recently affirmed that Russia was not going to move away from its flat tax makeup to a more progressive system and that raising taxes to plug the budget deficit was "a dead end." Note that hints from Prime Minister Putin last year that Russia was moving in this direction prompted our move out of our long Russia recommendation. In addition to the positive news from Nabiullina, Kudrin stated recently that Russia cannot raise taxes for two or three years for fear of slowing its economy. Good news. We are bullish on Russia. [Key Stats: Annualized CPI: 9.6% January 2010; Benchmark rate: 8.00%, up 25 bps YTD; Forex: 4.2% appreciation vs. USD in past 12 months.]

5. HUNGARY (December rank: 14): We are still bullish on Hungary. Prime Minister Orban remains committed to the tax reforms enacted in January including a 16% income tax rate, a 10% corporate tax rate and the abolition of the estate tax. He is also opposed to any EU corporate tax harmonization, which Germany continues to press for. In our last MSCI quarterly report, we were concerned with central bank policy given how the monetary policy committee (MPC) was top-heavy with anti-growth technocrats who equate growth with inflation. Indeed, they were threatening to raise interest rates so long as pro-growth tax changes were being implemented. New legislation passed by

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Orban's parliament will allow for the selection of new MPC members by Orban's government. This will change the composition of the committee and lead to interest rate policy more in line with Orban's growth objectives. We think Orban's people understand monetary policy very well given their emphasis last year that all the Hungarian economy needed from a central bank was "currency stability." Along those lines, we are encouraged to hear that a plan may be in the works to help Hungarian holders of Swiss-franc mortgages by fixing the Hungarian forint to the Swiss Franc at 190 for several years. Note, the forint has appreciated more than 15% against the dollar since the Greek debt crisis in May 2010. [Key Stats: Annualized CPI: 4.0% in January 2011; Benchmark rate: 6.0%, 25 basis points higher YTD; Forex: 0.27% appreciation versus USD in past 12 months.]

6. CANADA (December rank: 8): In a stagflationary world where high unemployment and rising prices may continue to test governments in the third world, we think there is a good chance that commodity-based economies in the developed world can outperform their peers. Canada is a standout in this respect. Tax policy continues to work in Canada's favor, with the government under Conservative Steven Harper likely to follow through with plans to cut the nation's corporate tax rate to 15% from 16.5% for 2012. The central bank targets a 2% inflation rate. While the January headline rate was 2.3%, core inflation was just 1.4%. Importantly, we think the loon's 7.4% appreciation against the dollar during the last year is positive and will likely help to keep headline CPI restrained. Overall, we are bullish on Canada. [Key Stats: Annualized CPI: 2.3% in January 2011; Benchmark rate: 1.0%, no change YTD; Forex: 7.47% appreciation versus USD in past 12 months.]

7. PHILIPPINES (December rank: 19): Austerian policymaking continues to find little purchase in the Aquino administration, in contrast to the previous one. This should help the Philippine economy. Budget Secretary Abad recently emphasized that only plans to close loopholes and 'leaks' will be implemented to increase tax revenues. There is actually a proposal to cut taxes on credit card companies. Tax hikes would only be considered if revenue projections fall significantly short. And according to Abad, "so far they are not." Additionally, interest rate policy looks dovish with Finance Secretary Purisma saying that there is no reason to expect rate increases. Meanwhile, the central bank has avoided heavy handed actions to limit capital inflows, with Deputy Reserve Bank Governor Guinigundo saying that the Bank can't "join the herd on policy action...There's hardly any evidence of asset price inflation." So long as global GDP remains positive, the Philippines should continue to do well. Continued appreciation of the peso against the dollar will help offset inflationary pressures. [Key Stats: Annualized

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CPI: 3.5% in January 2011; Benchmark rate: 4.0%, no change YTD; Forex: 5.85% appreciation versus USD in past 12 months.]

8. MALAYSIA (December rank: 6): The best thing going for Malaysia is the ringgit's 10+% appreciation against the dollar during the last twelve months, and the government's follow-through last year in reducing its corporate tax rate to 25%. But it did raise the sales tax to 6% from 5% as part of its effort to reduce the government's deficit to 5.4% of GDP. It was 5.6% in 2010. If fuel subsidies are cut under the duress of \$100+ oil, there could be a political backlash which would lead to redistributive fiscal policies. For now, we are optimistic on Malaysia. [Key Stats: Annualized CPI: 2.4% in January 2011; Benchmark rate: 2.75%, no change YTD; Forex: 10.78% appreciation versus USD in past 12 months.]

9. THAILAND (December rank: 5): Thailand seems to be benefitting from the rise in food prices -- especially rice, a major export crop. And food subsidies from the government are apparently helping to keep CPI below 3%. Another positive is that Finance Minister Chatikavanij has dismissed calls to match recent Vietnamese dong devaluations. He has, however, suggested that interest rate policy this year is likely to 'err on the hawkish side'. While the government's growth forecasts include a \$90/bbl oil price, \$110 oil will prove to be a headwind for Thailand and other Asian countries. So long as baht strength continues, we are bullish on Thailand. [Key Stats: Annualized CPI: 2.87% in February 2011; Benchmark rate: 2.25%, 25 basis points higher YTD; Forex: 7.10% appreciation versus USD in past 12 months.]

10. JAPAN (December rank: 36): Prime Minister Kan has changed his talking points on the consumption tax, and it could prove to be the critical shift necessary to reduce Japan's 41% effective corporate tax rate by five percentage points. Kan has specifically adopted the stance of Japan's most popular Prime Minister of the last 20 years, Junichiro Koizumi, who would always agree to the idea of a consumption tax increase, with the proviso that the next administration should raise the rate. In other words, Koizumi was always seemingly agreeable to the idea but kicked the can down the road. Similarly, Kan is saying that the consumption tax needs to be doubled to 10% from 5%, but that an election should take place before any legislation takes place on the issue. Meanwhile, Kan is pushing for a reduction in the corporate tax rate for 2012. Factions within Kan's DPJ party would like the corporate tax rate lowered to 25% by 2014. In fact, Japanese corporate lobbyists are pushing for a 17% increase in the consumption tax hike in the hopes that it will allow bigger cuts in the corporate tax rate. A 25% rate would be on par with China's corporate rate. This is the most promising development out of Japan in a decade, in our opinion, and could allow Japan's economy to emerge from its torpor. This could be bad news for Japanese bonds, however, as we expect any

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improvement in growth expectations to ultimately lead to higher interest rates from the Bank of Japan. Passage of corporate tax cut legislation this year could push the Japanese 10-year yield above 1.7% by year-end. We think that the improving fiscal discussion in Japan is part of the reason behind the yen's strength against the dollar. We do not expect material weakness in the yen. Japanese official inflation remains very weak, with yen strength vis-a-vis the dollar as a counter-weight to higher commodity prices. We do not expect CPI to threaten significantly higher this year, although it has clearly improved from the negative 2.5% rate of early 2009. Still, CPI need not even be positive for the BoJ to raise rates. During the most recent rate increase in February 2007, annualized inflation was running about negative 0.2% at the time, and real GDP was 2.1% in Q4 2006. All the BoJ needs is to sense that a real economic expansion is building for it to begin raising interest rates, which could happen by the second or third quarter of this year if Kan's corporate tax cuts pass. Japan rises in our ranking. [Key Stats: Annualized CPI: 0.0% in January 2011; Benchmark rate: 0.1%, no change YTD; Forex: 7.80% appreciation versus USD in past 12 months.]

11. NEW ZEALAND (December: 16): The government may levy a reconstruction tax to help with the cleanup and rebuilding following the Christchurch earthquake. Like the reconstruction taxes levied in Chile following its own earthquake, we do not think it will derail the growth outlook or overwhelm the recent positives on tax policy. Last year, we highlighted New Zealand's income and corporate tax cuts that went into effect this year. The top personal rate was reduced from 38% to 33%, and the corporate rate from 30% to 28%. The tax reductions are being financed by an increase in the VAT from 12.5% to 15%. We still expect the central bank to be dovish on rates. Markets are even suggesting the possibility of a 25 basis point cut at the March 10 meeting due to the earthquake. Given generally improving tax policy, we think that the kiwi will continue to strengthen against the dollar. We are bullish on New Zealand. [Key Stats: Annualized CPI: 4.0% in December 2010; Benchmark rate: 3.0%, no change YTD; Forex: 7.91% appreciation versus USD in past 12 months.]

12. COLOMBIA (December rank: 9): While Colombia will continue to benefit from rising commodity prices, such as in coffee, the internal policy-mix is likely to become a net drag on the country's economic performance. We remain concerned with President Echeverry's commitment to produce a balanced budget by 2014. It would be better for the government to focus on incentivizing production and risk-taking by halving Colombia's 33% corporate tax rate. Instead, the administration seems focused on austere measures to lower Colombia's 3.1% budget deficit. Last year, Echeverry lowered the threshold on the wealth tax and decreed that the financial transaction tax remain in place at least until 2014. The negative tilt on fiscal policy should limit the

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upside for Colombia. It moves down in rank. [Key Stats: Annualized CPI: 3.4% in January 2011; Benchmark rate: 3.25%, 25 basis points higher YTD; Forex: 0.08% appreciation versus USD in past 12 months.]

13. HONG KONG (December rank: 10): With Hong Kong's Financial Secretary announcing recently that the territory has 'fully recovered' from the 2008-2009 crisis, it is possible that authorities may become more aggressive in dealing with burgeoning inflation pressures, as the CPI is set to rise to 4%-4.5% by year-end from 3.6% currently. The government may continue to raise the sales tax on property and further tighten mortgage requirements following such moves late last year. But for now, we are pleased that Chief Executive Tsang is looking to address the 'supply' end of the real estate equation by considering an increase in the amount of land that can be developed. Additionally, Tsang recently unveiled a budget addendum which offered residents cash handouts and income tax exemptions up to HK\$6,000 (\$700). The move, aimed at helping citizens deal with rising prices, may benefit nearly 6 million people. The overall outlook for Hong Kong is positive due to its smart capital tax structure, but CPI is likely to rise toward 4-4.5% this year. It falls a bit in rank. [Key Stats: Annualized CPI: 3.6% in January 2011 (NSA); Benchmark rate: 0.50%, no change YTD; Forex: Pegged to USD.]

14. KOREA (December rank: 7): The administration of President Lee Myung Bak seeks to achieve a GDP growth rate of 5% amidst an inflation rate of 3%. Unfortunately, monetary policy is a bit negative, insofar that the won's small appreciation against the dollar during the last year has allowed the CPI to rise in January to a 4.1% annualized rate. The won has appreciated just 3.12% during the past twelve months, substantially less than the Thai baht or Malaysian ringgit during the same period. Not coincidentally, CPI in Thailand and Malaysia remains below 3%. President Lee remains supportive of plans to reduce, by 2012, the corporate income tax to 20% from 22% and to reduce the top marginal personal income tax rate to 33% from 35%. This is positive of course. Our overall outlook on Korea is positive, although geopolitical considerations with the North will linger and central bank policy is a concern. Korea moves out of our top nine. [Key Stats: Annualized CPI: 4.1 in January 2011 (NSA); Benchmark rate: 2.75%, 25 basis points higher YTD; Forex: 3.12% appreciation versus USD in past 12 months.]

15. USA (December rank: 27): We continue to believe that dollar weakness will persist in 2011, leading to higher commodity prices and more cost-push inflation. This may set us up for a stagflation market in 2011. But the prospects for smart compromises on tax policy have improved since President Obama's speech calling for a corporate tax cut, and Treasury Secretary Geithner's follow up that such legislation should be dealt with immediately. In late January, FASB decided to nix plans to reintroduce mark-to-market

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accounting, which is a positive for markets and the economy. As our clients know, we called the bottom in financials in March 2009, following hearings on Capitol Hill that suggested FASB would adjust mark-to-market accounting rules. According the [Brian Wesbury](#) in January, "FASB surrendered on fair value accounting for loans. In the face of overwhelming opposition, banks will be allowed to carry loans on their books at amortized cost, reflecting cash flow (payments), as well as reasonable estimates of likely loan losses." The U.S. moves up substantially in rank. [Key Stats: Annualized CPI: 1.6% in January 2011; Benchmark rate: 0.25%, no change YTD; Forex: 27.73% depreciation versus gold in past 12 months.]

16. SINGAPORE (August rank: 13): Singapore appears to be in good hands. Finance Minister Shanmugaratnam views rising food and fuel prices and Middle East unrest as offering little relief from inflationary pressures. Currency appreciation remains the primary mechanism for limiting inflation in the Singapore economy. Tharman has correctly acknowledged, though, that a "sharp appreciation" of the Singapore dollar to offset the inflation of the last six months would be undesirable. As a result, the government will try to offset some of the price increases through rebates and other types of subsidies, while continuing a sub-10% annual rate of currency appreciation against the dollar. We expect the Singapore dollar to continue its gradual appreciation against the US dollar, which should help the inflation outlook. Government revenues have come in better than expected as GDP hit a record 14.5% growth rate last year. The government forecasts at least 4-6% GDP growth in 2011. The government's deficit is about 0.1% of GDP, and its forecast for a balanced budget by 2012 seems very plausible given the country's economic growth. Minor, positive tax changes this year include the exempting of bank interest from withholding tax. Importantly, we do not foresee any negative tax moves during the next year. The city's tax structure is the second most attractive in Asia, behind Hong Kong. Overall, we remain bullish on Singapore, but it falls in rank given improvements in other countries and the positive momentum that could bring. [Key Stats: Annualized CPI: 3.6% in January 2011 (NSA); Benchmark rate: 0.50%, no change YTD; Forex: Pegged to USD.]

17. ISRAEL (December rank: 24): Property tax exemption levels have been raised, and there is now no capital gains tax on properties valued less than 2,200,000 shekels (US\$607.7K). Also, a tax hike on gasoline has been rescinded, and taxes on water and bus and rail fares have been lowered. But in order to pay for that, Prime Minister Netanyahu's cabinet has frozen by one year (pushing it to 2013) a proposed 1 percentage point cut in the top two income tax brackets. Also, there was a 1% budget cut across all government departments. We expect that the cut in the corporate tax rate to 23% will be delayed by one year. The government's deficit is only 3.7% of 2010 GDP,

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but it is committed to reducing it to 3% by the end of 2011. Central banker Stanley Fischer, who raised the benchmark rate by 25 basis points last month to 2.5%, says that Israel has almost closed its output gap given the fact that labor participation is very high. This is unmistakable hawkishness. Despite the likelihood of continued Mideast unrest, we see Israel continuing to move down the Laffer Curve, which helps its outlook. We are slightly bullish on Israel, although interest rate policy now appears to be a risk. [Key Stats: Annualized CPI: 3.6% in December 2010 (NSA); Benchmark rate: 2.50%, 50 basis points higher YTD; Forex: 3.92% appreciation versus USD in past 12 months.]

18. GERMANY (December rank: 26): The Merkel government does not plan any tax hikes in the near-term, including a financial transactions tax. Unfortunately, a source from the Finance Minister's office recently indicated that there is no room for tax cuts until at least 2015. Also, Bundesbank President Weber correctly stated that the continent's debt crisis is not a currency crisis, which could alleviate worries that the euro currency union is on the brink of dissolution. Notwithstanding that positive, there are growing indications that the European Central Bank will raise interest rates soon and fast to head off mounting inflation risks. With the benchmark rate at 1% currently, we think that it could end the year at 1.75% or 2%. January CPI was revised lower to 2.3%, but it is still above the target of 2%. We expect CPI to persist above 2% in 2011. Euribor rates continue to suggest that the ECB is very likely to raise rates this year to about 1.75%. On the political front, we suspect Angela Merkel's CDU party will continue to lose political clout, which could usher in a change from Merkel on such issues as Germany's approach to the euro and sovereign debt issues, or lead to a challenge of Merkel's leadership and possibly new elections. The Social Democratic Party (SPD) has begun to make political gains by recently winning the Hamburg elections in a landslide victory. In that election, SPD local leaders such as Olaf Scholz (a rising star in our opinion) campaigned as pro-business centrists, while remaining pro-euro and pro-Eurobonds on the issue of the European sovereign debt. If Merkel loses the upcoming Baden-württemberg elections later this month to the SPD, it could signal the beginning of the end for Merkel. Reports that Merkel is insistent on prescribing fiscal discipline for the rest of the continent with sanctions and upward corporate tax harmonization schemes continues to underscore her station as Europe's most dangerous politician. Ultimately, however, we think Germany will go along with a moderation in its anti-growth, pro-austrian stance, to the benefit of Europe. We are slightly bullish on Germany, which moves up in rank. [Key Stats: Annualized HICP: 2.0% in January 2011; Benchmark rate: 1.0%, no change YTD; Forex: 1.74% appreciation versus USD in past 12 months.]

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19. NORWAY (December rank: 34): We are optimistic that overall fiscal policy will remain in neutral. During the last quarter, the government increased "sin taxes" on alcohol and tobacco, but avoided any major tax increases. Despite a general strengthening of the krone -- likely tied to a continued weak-dollar environment and higher oil prices, which benefits Norway -- interest rate increases are a threat. The central bank, Norges Bank, has signaled that rate hikes will likely begin by mid-2011. The benchmark rate stands at 2.0%. Note that it was reduced to 1.5% in 2009; its pre-Lehman peak was 5.75% in June 2008. Given our expectations for higher oil prices, the outlook for Norway is somewhat positive. [Key Stats: Annualized CPI: 2.0% in January 2011; Benchmark rate: 2.0%, no change YTD; Forex: 5.52% appreciation versus USD in past 12 months.]

20. INDIA (December rank: 17): There are mixed signals coming out of India. Tax policy is improving, albeit slowly. Income tax thresholds are set to rise. With the threshold on the top marginal rate of 30% rising to INR800,000 (\$16,783) from INR500,000 (\$10,823). But plans to cut the corporate tax have been shelved this year. And the eventual unification of the goods and services tax continues to be delayed. April 2012 may be the earliest implementation date at this point. India's fiscal deficit is expected to be 5.2% of GDP this year and is forecast to decline to 4.6% next year. This is something to monitor, as it could furnish reasons for the Reserve Bank of India's hawks to go into action. For us, the weakest link in the Indian policy-mix has been monetary policy, as the central bank typically views higher interest rates as the proper, primary response to rising prices. One member on the monetary policy committee even sought a 50 basis point increase in the reverse repo rate. There have been seven rate increases since March 2010, when the rate stood at 3.25%. The rate is now 5.50%. At its pre-Lehman peak the rate was 6%. Meanwhile, wholesale price inflation reached 8.2% in January. RBI Governor Subbarao recently mentioned that the food inflation in India, which is filtering into wholesale prices, is a derivative of 'supply constraints'. This is at least a helpful, implicitly dovish characterization. Still, the RBI is worlds away from directly dealing with inflation by appreciating the rupee. Late last month, Subbarao affirmed the doctrine of floating rates, saying that the rupee exchange rate 'should be determined by the market.' Such a stance does not help the RBI's fight against inflation, so hawkish interest rate policy remains a risk for India. Still, we expect the rupee to continue strengthening in a gradual manner along a band of INR48-44/USD on the back of expected tax cuts and continued economic growth. We are neutral on India. [Key Stats: Annualized CPI: 8.8% October 2010; Benchmark rate: 6.25%, up 200 bps YTD; Forex: 4.6% appreciation vs. USD in past 12 months.]

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21. BRAZIL (December rank: 21): President Rousseff appears to be focusing on the bottom rungs of society as she looks to raise the income tax exemption threshold. But a curious warning from former central banker Fraga over the potential for too much leverage in the Brazilian economy does raise red flags for us. Fraga believes that the economy is 'overheating' and that the SELIC, Brazil's benchmark rate, ought to be raised by as much as 75 basis points in a single meeting. We certainly think that Brazil's central bank will raise rates this year. If Fraga's suggestions are taken up, we would stay on the sidelines of Brazil. We are neutral on Brazil given the potential for hawkish-rate interest policy, and the central bank's soft peg to the weak-dollar around BRL1.65/USD. [Key Stats: Annualized IPCA CPI: 5.99% in January 2011; Benchmark rate: 11.17%, 50 basis points higher YTD; Forex: 8.1% appreciation versus USD in past 12 months.]

22. CHILE (December rank: 3): Chile's peso has appreciated nearly 10% against the U.S. dollar during the past twelve months. This is a positive forex dynamic that should mitigate inflationary pressures spawned by the weak dollar. CPI was 2.7% in January 2011, which is positive because the central bank is targeting inflation around 3% (+/- 1%). But the fear of capital inflows runs strong in Chile. The announcement in early January that the central bank would purchase \$12 billion in a bid to weaken the peso amounted to the largest single day drop in the peso in the last twenty years. We suspect that the peso-dollar rate found a floor in January and that the peso will gradually weaken from here, which would worsen the Chilean inflation outlook. Another potential negative is that the central bank has been citing rising food prices as one the reason for its hawkishness on interest rates. It has raised short-term rates eight times during the past nine months and may continue. Given our belief that dollar weakness will continue into 2012 as well as the erroneous policy remedies by Chile's central bank, we are lowering Chile in our rankings. We are doing this despite the fact that we believe the Chilean mining taxes tied to post-earthquake reconstruction have been fully priced into Chile's stock market. [Key Stats: Annualized CPI: 2.7% in January 2011; Benchmark rate: 3.5%, 25 basis points higher YTD; Forex: 9.29% appreciation versus USD in past 12 months.]

23. POLAND (December rank: 30): Unable to reach agreement with Brussels on how Poland's pension system is scored in government accounting terms, Poland has opted to make some important changes to its pension system. The government intends to cut transfers to private pension funds to 2.3% of employees' salaries from 7.3%. The rest of those transfers would go to the state-run pension system. The change is being characterized as a softer form of what Hungary did late last year, which we saw as a net positive. According to Finance Minister Rostowski, Poland's total debt obligations would

amount to 40 percent of GDP if the government can implement the proposal. No tax increases are planned. Already the recent VAT increase, to 23% from 22%, is being blamed for the slowdown in January's retail sales. Without the pension reforms, we feared that Poland's debt-to-GDP ratio could have breached 55%, which would have produced an automatic increase in the VAT to 25%. That risk has now diminished. We also think that it is helpful that Prime Minister Tusk is no longer pushing for fast adoption of the euro, which could have invited more severe austerity for Poland. He rarely discusses the prospect of joining the euro these days, with his most recent pronouncements acknowledging that the EU must resolve some of its internal issues first. The country's deficit is expected to be 6.6% of GDP by year-end. We are slightly bullish on Poland. [Key Stats: Annualized CPI: 3.8% in January 2011; Benchmark rate: 3.75%, 25 basis points higher YTD; Forex: 0.62% appreciation versus USD in past 12 months.]

24. BELGIUM (December rank: 35): Finance Minister Reynders may make the first E1,700 in interest on Belgian sovereign bonds exempt from withholding and interest taxes. This is a slightly positive development. Generally, fiscal policy is neutral with the caretaker government of Belgium showing no bold strokes. Prime Minister Leterme said no welfare cuts or tax increases were being considered for 2011. Given that Belgium's 2011 debt obligations will be more than 50% of expected government revenue, any positive development in EU debt negotiations, i.e. an agreement on Eurobonds and the lengthening of debt repayment schedules, should have a positive impact on Belgian debt. The overall outlook for the country is slightly positive so long as European sovereign credit risk remains stable or improves. [Key Stats: Annualized HICP: 2.5% in January 2011; Benchmark rate: 1.0%, no change YTD; Forex: 1.74% appreciation versus USD in past 12 months.]

25. DENMARK (December rank: 39): Prime Minister Rasmussen's coalition consensus on austerity -- spending cuts and keeping tax rates the same -- is beginning to break down. New conservative leader Lars Barfoed is seeking to lower personal and corporate taxes on the back of spending cuts. This is smart, refreshing thinking on tax policy -- especially coming from Denmark, the stereotype for modern socialism. The next general election is scheduled no later than November 2011. Fiscal consolidation in Denmark will mean more budget cuts, but no major negatives on fiscal policy. The central bank is keeping the krone loosely pegged to the euro at +/- 2.25% on either side of DKK7.46/E. It is currently at DKK7.45. We believe the krone will likely trend higher. Denmark's policy-mix is neutral for now, but its prospects are improving given Barfoed's political campaign and our optimism that European bureaucrats are shying away from shock-

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therapy austerity. [Key Stats: Annualized CPI: 2.7% in January 2011; Benchmark rate: 0.75%, no change YTD; Forex: 1.14% appreciation versus USD in past 12 months.]

26. MEXICO (December rank: 11): We are not seeing a great turnaround for fiscal policy in Mexico. Interestingly it is the old PRI that is campaigning for VAT cuts, and President Calderon's PAN is resisting the idea. The PAN seems committed to austerity. Despite a slight negative policy tilt, Mexico may benefit from continued dollar weakness and a buoyant commodity outlook. With the peso having appreciated 5% against the dollar year-to-date, at least the Bank of Mexico is not using heavy handed, anti-growth approaches to weaken the peso. We are neutral on Mexico and have lowered its rank. [Key Stats: Annualized CPI: 3.78% in January 2011; Benchmark rate: 4.5%, no change YTD; Forex: 5.0% appreciation versus USD in past 12 months.]

27. AUSTRALIA (December rank: 15): Plans for a carbon tax by 2012 are being hit with ferocious attacks by opposition party leader Tony Abbott. Given how Prime Minister Gillard softened her stance on the mining tax last year, we think that she will backpedal from the unpopular tax plan. The Reserve Bank of Australia targets a 2-3% inflation band. Inflation was 2.7% in December, down a tenth of a percent from September's quarterly figure. Reserve Bank board member Warwick McKibben warned last week that Australia could be trapped in a liquidity bubble, saying, "This is shaping up to be much bigger than 2004 to 2007. This cycle is even bigger." What's interesting is that McKibben sees today's U.S.-led liquidity expansion similar to the 1970s when there was a surge in food, mining and energy prices that led to global stagflation. To be sure, McKibben is a rate hawk. But he correctly sees quantitative easing as contributing to the inflation problem, and as the world moves further into a stagflationary environment, McKibben's views may win more allies in the coming months, which could lead to higher rates in Australia. For now, futures suggest the benchmark rate might only rise 25 basis points to 5% by year end. In general, we think the Australian outlook, which is positive, is tied to China's growth outlook. We are neutral on Australia given the threat of a carbon tax and the potential for hawkish rate policy. [Key Stats: Annualized CPI: 2.7% in December 2010; Benchmark rate: 4.75%, no change YTD; Forex: 13.73% appreciation versus USD in past 12 months.]

28. SOUTH AFRICA (December rank: 22): Finance Minister Gordhan says that the government's deficit of 5.3% of GDP is very manageable and, therefore, does not require austere tax hikes. But policymakers are pursuing a socialist model in South Africa, which will limit the upsides of any commodity-led expansion. The government may, however, raise the VAT and impose a payroll tax to pay for healthcare spending and fulfill its promise to extend 'quality care' for all South Africans during the next 14 years. The rand has weakened approximately 7% against the U.S. dollar since January

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1. Fortunately, the South African Reserve Bank understands that rand strength is positive for fighting inflation. Additionally, the CPI is rising 3.7% year-over-year, which is at the lower limit of the Bank's 3-6% target range. Despite the government's redistributionist tendencies, we think South Africa will benefit from a weak-dollar environment. We are neutral on South Africa. [Key Stats: Annualized CPI: 3.7% January 2011; Benchmark rate: 5.5%, no change YTD; Forex: 0.77% appreciation vs. USD in past 12 months.]

29. TAIWAN (December rank: 18): Taiwan is reacting to rising property prices with fiscal proposals, such as a tax on unoccupied dwellings of up to 15%, a 10% tax on luxury goods and an increase in the tax on retained earnings to 15% from 10%. The government has also allowed local governments to reimpose an idle land tax that was suspended in 1985. As a result, the city of Taipei is set to raise the tax on luxury homes in July. These are slight negatives at the margin, which will diminish the upside for Taiwan. Monetary policy is neutral, with continued currency appreciation helping to mitigate inflationary pressures, even as short-term interest rates creep higher. As the economy continues to expand, the central bank will likely continue to incrementally increase the discount rate, which now stands at 1.625%. For context, in August 2008, the rate stood at 3.625%. Despite the steady increase, we expect the Taiwan dollar to continue strengthening against the U.S. dollar. Closer integration with China following its free trade agreement last summer should continue to help economic conditions. Despite our optimism on Mainland China's growth prospects and the potential positives that holds for Taiwan, we are staying neutral given recent negatives at the margin. [Key Stats: Annualized CPI: 1.11% in January 2011; Benchmark rate: 1.625%, no change YTD; Forex: 7.73% appreciation versus USD in past 12 months.]

30. SWITZERLAND (December rank: 25): The Swiss government recently signed double taxation agreements with Romania, Slovakia and Singapore. Swiss National Bank President Hildebrand recently stated that he expects short-term price stability to persist and that economic growth could surprise to the upside in upcoming quarters. CPI grew only 0.3% year-over-year in January, while the franc has appreciated 12% against the euro and 11% against the dollar during the last year. We view the stability in the price indices and forex appreciation as positive developments. We are neutral on Switzerland. [Key Stats: Annualized CPI: 0.3% in January 2011; Benchmark rate: 0.54%, 4 basis points lower YTD; Forex: 13.57% appreciation versus USD in past 12 months.]

31. TURKEY (December rank: 2): Turkey's capital markets are getting buffeted by continuing turmoil in the Middle East and North Africa. Unfortunately, we do not expect that phenomenon to subside anytime soon, especially with the Fed's weak dollar policy

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continuing to push food and fuel prices higher around the world. Turkey has made some moves to mitigate this inflationary surge, for example, by cutting the import tax on wheat to 0% until May 1. It has also offered to ease tax payments for companies hit by Libyan unrest. Interest-rate policy is dovish with the benchmark interbank rate at 7%. It is unlikely to rise during the next six months. Lira strength against the dollar is likely to continue, and in so doing, it will work to mitigate inflationary pressures. This may help with the rising cost of gas, which already at 1.90 euros per gallon and is the most expensive in Europe. The government must do more, such as reducing the near 68% share of taxes that make up gas prices. Otherwise, the price squeeze on the Turkish public and economy will continue to worsen. We are neutral on Turkey given our concerns with continued MENA unrest. [Key Stats: Annualized CPI: 4.9% in January 2011; Benchmark rate: 6.25%, 25 basis points lower YTD; Forex: 3.86% depreciation versus USD in past 12 months.]

32. FINLAND (December rank: 28): The Finnish government is seeking to raise taxes on nuclear fuel, which will impact the country's energy industry. Given strong demand this may be positive for government tax revenues. While an improvement to the European debt situation could be positive for Finland, we remain neutral on the country. [Key Stats: Annualized HICP: 1.9% October 2010; Benchmark rate: 1.0%, no change YTD; Forex: 8.47% appreciation vs. USD in past 12 months.]

33. IRELAND (August rank: 41): The electoral victory of Fine Gael, which seeks to lower the VAT and other austerian tax increases, suggests that Ireland's new government will likely resist further attempts at anti-growth, austerity measures. At the least, Fine Gael is committed to keeping Ireland's 12.5% corporate tax rate. In fact, there is a broad consensus on retaining that low-tax feature of Ireland's economy. The outlook is improving for Ireland. It should benefit from Brussels continued move away from a shock therapy approach. It moves up from our bottom nine. [Key Stats: Annualized HICP: 0.2% in January 2011; Benchmark rate: 1.0%, no change YTD; Forex: 1.74% appreciation versus USD in past 12 months.]

34. UK (December rank: 33): The UK economy is still dealing with the headwinds of rising capital gains taxes and a bank tax. But tax increases from last year are largely priced into the FTSE. Unfortunately, it seems that the Tories are more committed to austerian policies in the short-term, than trying to accelerate UK's economic growth rate. For example, Finance Minister Osborne recently said in response to the unpopularity of Prime Minister Cameron's tax policies, "No politician likes cutting spending and increasing people's taxes, but I was delivered a mess by the previous Government and I am trying to clear it up." This is blinkered rhetoric, which shows just how far Britain's Tories have strayed from the days of Thatcher. Interest rate hikes are likely this year.

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The Bank of England's inflation target of 3% has been repeatedly breached, and Mervyn King continues to point the finger toward rising commodity prices. Futures suggest the benchmark rate, now at 0.5%, will rise to 1.5% by year-end. We think that is a fair prediction. We are neutral on the UK. [Key Stats: Annualized HICP: 4.0% in January 2011; Benchmark rate: 0.50%, no change YTD; Forex: 8.0% appreciation versus USD in past 12 months.]

35. SWEDEN (December rank: 32): During the last four years, Sweden's borders have been opened for more labor migration into the country, and state-owned companies have been sold. Stockholm has also cut property taxes and abolished the wealth tax. Today, the state's total tax take comes to 45% of GDP, compared to 56% ten years ago. Finance Minister Borg recently stated that Sweden is pretty much out of its fiscal crisis. Given concerns with faster economic growth and rising food, raw material and fuel prices, we expect the country's central bank to raise rates quickly throughout 2011. This will be a negative drag on Swedish equities. Sweden falls in rank. [Key Stats: Annualized HICP: 1.4% in January 2011; Benchmark rate: 1.50%, 25 basis points higher YTD; Forex: 11.33% appreciation versus USD in past 12 months.]

36. MOROCCO (December rank: 37): The government is aiming to sell off state assets and keep spending down to achieve a deficit of 3.5% of GDP by year-end. But subsidies on energy and food have increased as a result of the unrest in North Africa. While no major tax increases are being discussed, the strengthening dirham in recent months, should the trend continue, would help the overall outlook for Morocco. The government expects 5% GDP growth this year, which it sees as possible if commodity prices cool. We are neutral on Morocco, but it moves up slightly in rank due to the strengthening dirham. [Key Stats: Annualized CPI: 2.2% in January 2011; Benchmark rate: 3.25%, no change YTD; Forex: 0.91% appreciation versus USD in past 12 months.]

37. AUSTRIA (December rank: 29): A capital gains tax that was hastily passed in late December is being challenged by the banking industry due to excessive compliance costs. The law went into effect January 1, two days after it was published. The new law eliminates the capital gains tax exemption for assets held longer than one year and introduces a 25% rate. Austria's coalition government is divided over the issue even as banks are railing against it. The move stems from the government's desire to reduce its deficit to 3.2% of GDP this year, versus 4.1% in 2010. This is a negative development for Austria and reduces its relative attractiveness. We are neutral on Austria, but it falls in rank. [Key Stats: Annualized HICP: 2.5% in January 2011; Benchmark rate: 1.0%, no change YTD; Forex: 1.74% appreciation versus USD in past 12 months.]

38. CZECH REPUBLIC (December rank: 31): Our concerns with Czech fiscal policy continue. This year, the center-right commitment to fiscal discipline will lead to a VAT increase in the fourth quarter of 2011 and any hiccup in growth could lead to more austerity down the road. Still, some proposed changes to the pension system, which will reduce contributions in the public system, may improve the overall public finance outlook in the years ahead. Nonetheless, we think the government's goal of achieving a balanced budget by 2016 -- the government's deficit is currently about 4.8% of GDP -- is misguided. The greater fear is that self-imposed demands of fiscal austerity will eventually lead the Czech Republic to abandon its 15% flat tax on personal income in favor of a progressive system. The idea was raised in political circles last year. Continued appreciation of the Czech koruna -- it has appreciated more than 7% in the past twelve months -- is positive and should mitigate inflationary pressures. While the Czech Republic may benefit from Europe moving toward a more reasonable sovereign debt fix, our concerns with fiscal policy in the country persist. We remain neutral on Czech Republic. [Key Stats: Annualized CPI: 3.4% in January 2011; Benchmark rate: 0.75%, no change YTD; Forex: 7.42% appreciation versus USD in past 12 months.]

39. NETHERLANDS (December rank: 40): Fiscal consolidation in the Netherlands will mean more budget cuts, but we do not expect any major tax increases. Only some small austrian measures should be implemented this year. Some longer-term government proposals are to raise the retirement age to 66 from 65, and to increase health insurance premiums. The policymix is generally neutral. The country's outlook is slightly positive so long as the European variable remains stable. We are neutral on the Netherlands. [Key Stats: Annualized HICP: 2.0% in January 2011; Benchmark rate: 1.0%, no change YTD; Forex: 1.74% appreciation versus USD in past 12 months.]

40. ITALY (December rank: 42): The fate of Prime Minister Berlusconi this year could decide whether or not Europe suffers another credit crisis similar to May-June 2010, which could be even larger in magnitude. Because the principal and interest on Italy's outstanding debt amounts to more than 60% of government revenues, we believe that any push for anti-growth, austrian tax hikes could send Italy headlong into a sovereign debt crisis. Fortunately, Berlusconi has refused to raise taxes in recent years, despite Italy's deficit, which stands at 4.6% of GDP. For now, Italy's policy-mix is generally neutral, but we are worried that it could worsen significantly if Berlusconi were to fall from power and his successor government raised taxes. We will be monitoring his trial which is set to begin April 6. [Key Stats: Annualized HICP: 1.9% in January 2011; Benchmark rate: 1.0%, no change YTD; Forex: 1.74% appreciation versus USD in past 12 months.]

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41. SPAIN (December rank: 43): Spain has been coping with the bust of its real estate sector since 2009. The government has given regional savings banks, or *cajas*, until September to recapitalize themselves or face takeover. In the meantime, the government is under pressure from Brussels to reduce its deficit, somewhere close to 9% of GDP, down to 3%. Austerity measures last year included increasing the VAT to 18% from 16%, tax increases on upper incomes, and raising the tax on savings to 19% from 18%. On the back of a 34.2% increase in revenue last year, Spain's Finance Minister recently announced that Spain cut its deficit in 2010 to 9.2% from 11.2% in 2009. Still, unemployment stands at nearly 20% for the general population and nearly 43% for those 25 and younger. To address the problem, the Labor Minister has offered a one-year holiday on social security taxes (100-75% reduction) for those 30 and younger or for the long-term unemployed hired on a part-time basis. This is far from pro-growth policymaking. But in terms of near-term sovereign debt concerns, we view Spain's total debt obligations on par with those of Finland, totaling about 25% of government revenue for the year. Spain should benefit from Brussels' continued move away from a shock therapy approach, but it is among our least favorite investment destinations. [Key Stats: Annualized HICP: 1.9% October 2010; Benchmark rate: 1.0%, no change YTD; Forex: 8.47% appreciation vs. USD in past 12 months.]

42. PORTUGAL (December rank: 38): The loose 'austrian consensus' between the Socialist Party and the Social Democratic Party continues in Portugal with January's presidential election result reinforcing the policy tilt. Social Democrat Cavaco Silva was handily re-elected as president with 53% of the vote, versus the 20% garnered by his nearest challenger, leftist candidate and anti-austerity figure Manuel Alegre. Portugal, like Greece, Italy and Belgium, has debt and interest obligations this year that will surely total more than 50% of government revenues, which is one reason why sovereign yields and CDS prices are so high. At 475, the price on 5-year CDS contracts for Portuguese debt are trading about 175 points above comparable Hungarian CDS prices. In Portugal's case, the impact of the European debt crisis and its own austerity measures since last year-- which included increases in income and VAT taxes -- caused GDP in Q4 2010 to contract 0.3%. The Bank of Portugal expects a contraction of 1.3% of GDP for 2011 with more austerity likely. Still, the sovereign debt outlook for Portugal could improve substantially if the EU discussions on sovereign debt mechanisms continue moving away from austrian cram-downs. For instance, if the terms of the Greek debt repayment are extended to 30 years -- as recently suggested by Eurogroup chief Juncker -- it would set a precedent for a similar workout should Portugal need assistance. This could stall plans for further austerity measures and provide substantial relief to Portugal's bond and equity markets. For now, however, we are negative on

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Portugal. [Key Stats: Annualized HICP: 3.6% in January 2011; Benchmark rate: 1.0%, no change YTD; Forex: 1.74% appreciation versus USD in past 12 months.]

43. FRANCE (December rank: 41): Prime Minister Sarkozy has been a disappointment, more so than Merkel, when it comes to internal fiscal policy. Sarkozy oversaw an increase in the top marginal income tax rate to 41% from 40%, a 1% increase in capital gains and dividend taxes, and an increase in social security contributions last year. And this week, Sarkozy abandoned the so-called wealth tax cap, which ensures that the wealthy never pay more than 50% of their income in taxes. Sarkozy's government would like the tax load on the wealthy to rise to roughly 60%. We remain negative on France in a relative sense, though France may be able to recover, albeit slightly in absolute terms on the back of improvements in European debt talks. [Key Stats: Annualized HICP: 1.9% in January 2011; Benchmark rate: 1.0%, no change YTD; Forex: 1.74% appreciation versus USD in past 12 months.]

44. GREECE (December rank: 45): The news that Greece could win a 30-year extension on its EU debt repayment schedule could make Greek sovereign debt one of the most speculative, but possibly most rewarding rebound plays of the year. If the repayment schedule is not extended beyond the 2014 deadline, we think that more austerity is in store for Greece. Finance Minister Papaconstantinou wants to reduce Greece's budget to 1% of GDP by 2015 and will likely find more taxes to raise in that misguided effort. He instead should be seeking ways to grow Greece's economy, which contracted 4.5% last year and is expected to shrink another 3% this year. The country's sovereign debt obligations are set to increase to more than \$34 billion annually between 2011 and 2014. This is why any improvement in the debt repayment terms could allow austere demands to cool, reducing the threat of negative fiscal policy in the next few years and thus reducing Greece's near-term default risks. The outlook for Greece remains negative, but an extension on the debt repayment schedule could lead to a significant improvement for Greek debt. [Key Stats: Annualized HICP: 4.9% in January 2011; Benchmark rate: 1.0%, no change YTD; Forex: 1.74% appreciation versus USD in past 12 months.]

45. EGYPT (December rank: 12): While some see an opportunity to play a rebound in a post-Mubarak Egypt, we fear that a new Egyptian government will focus on income redistribution, and if the IMF is allowed to advise on policy, then Egypt may move away from its flat tax system to a more progressive one. As we have mentioned before, the IMF is licking its chops at the prospect of dictating an austerity package for Cairo, given Egypt's deficit of 8.1% of GDP. [Key Stats: Annualized CPI: 11.7% in January 2011; Benchmark rate: 8.25%/9.75%, no change YTD; Forex: 7.7% depreciation versus USD in past 12 months.]

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