

Lazard Insights

Conference Call Series

15 December 2011

Opportunity, Austerity, Growth, and Inflation: The Road Ahead

Featured Speaker: **Ronald Temple**, CFA, Managing Director, Portfolio Manager/Analyst

2011 was a year largely marked by macro uncertainty. As we look ahead to 2012, we believe that much of this uncertainty will continue, as developed markets remain largely focused on balancing austerity measures with the need for growth. However, emerging markets appear to be at a turning point with regard to inflation. Against this backdrop, we believe fundamental research and security selection will be pivotal for investors in the new year.

If we think about 2011, it has been somewhat of an overwhelming year, yet again, of macro uncertainty. Sadly, we think we can say quite safely that 2012 will offer more of the same. At a high level, one could describe the developed world as facing the challenge of sustaining economic growth, even while governments cut spending and raise taxes (quite aggressively in some cases). In the developing markets, the challenge lies on the opposite end of the spectrum, in trying to control inflation without greatly decelerating economic growth from levels that have been quite high. In discussing the likelihood of continued macro volatility, the following three points should be noted: first, that the Eurozone issues have not been solved, and we believe that severe strains in the months ahead may increase volatility yet again; second, that U.S. politicians have little incentive to compromise as we near the 2012 elections, as both parties try to highlight their major philosophical differences to voters; and third, that we have increasing confidence that after a bleak year of relative performance in emerging markets, the battle against inflation, and seeking to achieve a soft economic landing, increasingly appears to have been won. However, in order to understand the current economic environment, we believe one needs a foundation of how to think about debt and leverage.

Exhibit 1 Balancing Debt and Growth

	Income (\$)		Debt (\$)		Debt/Income (%)
Year 1	100,000		60,000		60.0
Year 2	105,000	➤ 5%	66,000	➤ 10%	62.9
Year 3	110,250	➤ 5%	72,600	➤ 10%	65.9

	Income (\$)		Debt (\$)		Debt/Income (%)
Year 1	100,000		100,000		100.0
Year 2	105,000	➤ 5%	110,000	➤ 10%	104.8
Year 3	110,250	➤ 5%	121,000	➤ 10%	109.8

For illustrative purposes only.

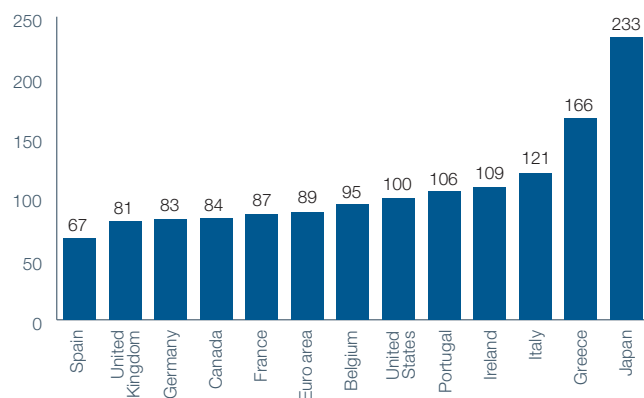
In Exhibit 1, we highlight a simplistic approach to debt and income. Although this is on an individual level, it could be translated to a national level by thinking of income as GDP, and debt on a national/regional scale. There are three key elements to any evaluation of how much debt a borrower can handle. One is how much debt the borrower has relative to his or her income (e.g., debt/GDP). The second is the interest rate on that debt (e.g., government bond yields), and the third is how quickly one can grow his or her income (e.g., GDP). The first bracket portrays a hypothetical case where income of an individual in year one is \$100,000, and the debt is \$60,000, so there is a debt/income ratio of 60%. If that person had a 10% interest rate, and a 5% growth in income, in year number two the debt/income ratio would grow from 60% to 62.9%, and so on to year number three with a debt/income ratio of 65.9%. It is important to note how potentially dangerous it is when the interest rate on debt is higher than the gross income. Looking at the bottom bracket, one can see a case in which the starting point is 100% debt/income. One realizes that the percentage change is about the same as in the previous example, but the magnitude of the number is

Exhibit 2

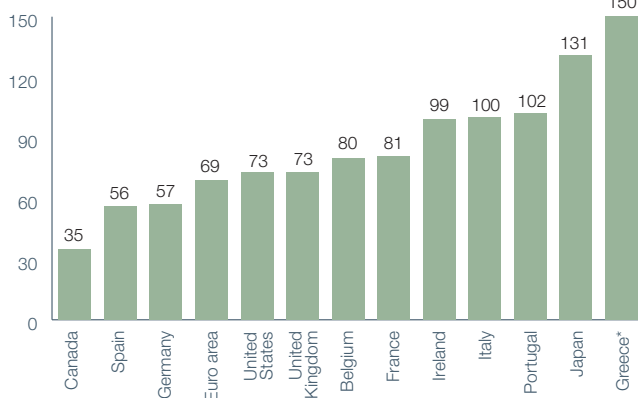
Government Debt is One Indicator of Risk

Government Gross Debt 2011¹

(% of GDP)

Government Net Debt 2011^{1,2}

(% of GDP)



As of September 2011

1 Most recent data divided by annual GDP (projected for 2011). World Economic Outlook projections for 2011.

2 Net general government debt is calculated as gross debt minus financial assets corresponding to debt instruments.

* Lazard estimate. Estimated data is not a promise or guarantee of future results and is subject to change.

Source: IMF, Global Financial Stability Report

larger. The 100% debt/income grows to 104.8% in the second year, and then on to 109.8% in the third year. As one analyzes countries, it is important to assess where they are starting, how fast their economies are growing, and what interest rates they are paying.

However, government debt is just one indicator of risk; there are multiple layers of risk one must consider when thinking about how much debt is sustainable. In Exhibit 2, on the left-hand side we show government gross debt outstanding, while on the right-hand side we portray government net debt outstanding. The difference between the two charts is that government net debt excludes government bonds that are owned by government entities. For example in the United States, the Social Security Trust Fund, which owns \$2.5 trillion in Treasuries, would be excluded as that is effectively money the government owes itself. In other cases, such as Japan, the figure excludes its sovereign wealth fund (or foreign exchange reserves) and gold assets. The government net debt calculation is an attempt to figure out if a government's material assets can offset part of the debt on its balance sheet. One can see that Greece is the outlier in terms of government net debt. As previously discussed, when the growth rate of an economy is lower than its interest rate (in Greece, growth is now negative), it will likely result in a vicious downward spiral in terms of the amount of debt relative to income.

A second piece of the analysis is government borrowing from non-residents. Just because a country has a high level of debt does not mean default is inevitable. If the country funds most of its own

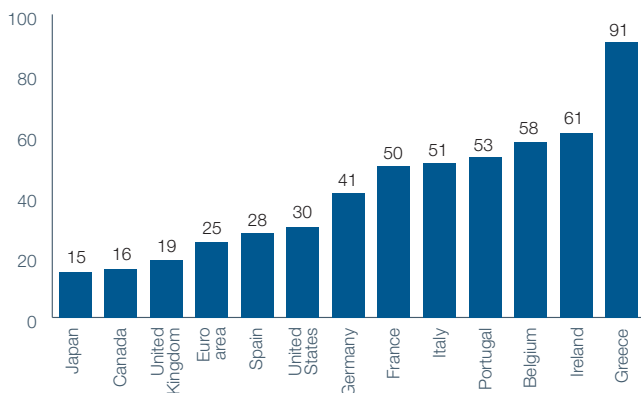
borrowing, it may be at low risk of default. As illustrated in Exhibit 3, the outlier to the good side on the left is Japan, where only 15% of government bonds are held by foreigners. Additionally, most Americans are surprised to learn that only 30% of American debt is

Exhibit 3

Government Borrowing from Non-residents also Matters

Government Debt Held Abroad¹

(% of GDP)



As of September 2011

1 Most recent data for externally-held general government debt (from Joint External Debt Hub) divided by 2011 GDP from WEO. Note that debt data from JEDH when they are at market value are not comparable to WEO debt data when they are at market value.

Source: IMF, Global Financial Stability Report

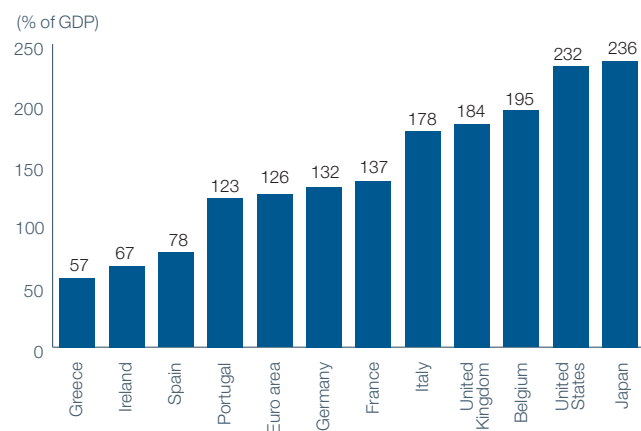
held by foreigners, implying, conversely, that 70% of Treasuries are owned by Americans. To the right end of the spectrum, you can see Greece is very dependent on foreigners, as are Ireland, Portugal, and Italy. It is important to note that in the Eurozone you would expect foreigners to own more debt, as anyone across the border, but within Europe, is considered foreign.

From another angle, assume a country has a government with too much debt outstanding and is overly reliant on foreigners, and hence needs to fund itself in a different way. In this case, one would want to assess how wealthy the households are in that country. In other words, how much tax you can take from the citizens to address the deficit issue. Exhibit 4 portrays household net financial assets as a percentage of GDP by country. What is important to recognize is that net financial assets includes checking accounts, life insurance, equities, bonds, or any other financial assets an individual may own, but not the person's house, because it is a physical, not a financial, asset. However, net financial assets subtracts financial liabilities from financial assets. This means that the net financial asset calculation takes into account the debt used to buy a house, but not the house itself, when considering the financial position of a country's household sector. As a result, we consider net financial assets as a conservative measure.

Exhibit 4 shows that the United States and Japan are very wealthy countries. In particular, it is worth considering that U.S. GDP is

Exhibit 4 The Next Level of Assessment Is the Household

Households' Net Financial Assets¹



As of September 2011

1 Most recent data divided by annual GDP (projected for 2011). Nonfinancial corporates' gross debt includes intercompany loans and trade credits, and these can differ significantly across countries.

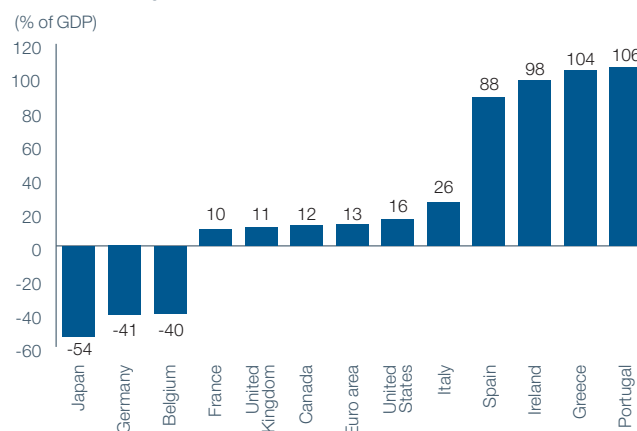
Source: IMF, Global Financial Stability Report

about \$15 trillion. Even excluding housing, which is the single-largest asset for most Americans, there is a very large amount of wealth – around \$35 trillion of net financial worth. In contrast, when you move to the other end of the spectrum, with Portugal, Ireland, Greece, and Spain, one sees very low levels of household wealth relative to much smaller GDP figures (particularly in Greece, Ireland, and Spain), even while their governments have quite a bit of debt outstanding.

In Exhibit 5, an illustration we call the Acid Test, we look at how much money a country is owed by all of the residents, companies, banks, and government (i.e. the entire economy in each country) to foreigners, versus what foreigners owe to the people in that country. The idea in this example is to find the net debtor or creditor position of each country, in aggregate, as a percentage of its GDP. On the far right-hand side of the chart, one can see that the PIIGS (or Portugal, Ireland, Italy, Greece, and Spain) all have very high levels of debt relative to what they are owed by foreigners. One thing that is important to note which is not represented on this chart is any consideration of the deadlines, or the maturity dates, of debt. A country could be on the left-hand side of this chart (in aggregate, owe a small amount to foreigners) and seemingly in a very good position. However, if the country owes its foreign lenders a great deal of money in the near-term, but they in turn owe the country money in ten years, there may be a liquidity problem. However, the key point of this chart is that,

Exhibit 5 Acid Test: External Debt Across All Sectors

Total Economy Net External Liabilities^{1,2}



As of September 2011

1 Most recent data divided by annual GDP (projected for 2011). Nonfinancial corporates' gross debt includes intercompany loans and trade credits, and these can differ significantly across countries.

2 Calculated from assets and liabilities reported in a country's international investment position.

Source: IMF, Global Financial Stability Report

looking at the overall stock of debt, Portugal, Ireland, Greece, and Spain have problems. One should recognize, however, that Italy is very different from the rest of the PIIGS (i.e. the real question in Italy is of its willingness to pay). If you refer back to Exhibit 4, you will see that Italian households are very wealthy, and are actually quite a bit wealthier than German households relative to GDP. The PIIGS, excluding Italy, on the other hand, don't have a lot of household wealth, and owe foreigners a lot of money. This is a divergence in the Eurozone crisis between those countries that might not be able to pay (Portugal, Ireland, Greece, and Spain), and the one country that might not be willing to pay (Italy), is an interesting point to consider.

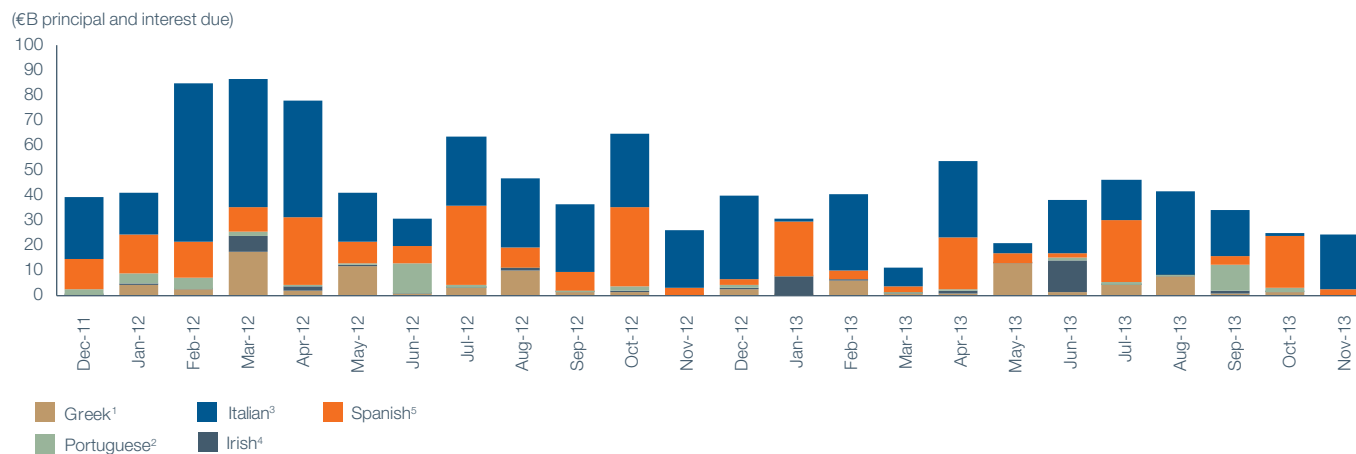
In Europe, we do not believe the situation has been solved, but do believe that it can be solved. One should remember that over time there can be solutions to problems, but the key is that the European Union (EU) needs time, and they need quite a bit of it. In our view, the way to decrease tension in the Eurozone, and ultimately solve this issue, is comprised of a number of measures. First, the EU needs to agree, develop, and implement rules around fiscal union. While policymakers did agree on certain rules twenty years ago in the Maastricht Treaty, and later with the Growth and Stability Pact, they did not figure out how to implement them effectively to ensure that countries within the euro abided by them, particularly rules concerning their deficits and total debt outstanding. Second, the EU needs to recapitalize their banking systems sufficiently, so that if things were to go wrong, in Greece or even Portugal, the banks would not automatically be in a situation where they are no longer solvent. Unfortunately, for over a year and a half (since May 2010), Greece has contaminated France because of the French banks' ownership stakes and exposure to the region, and likewise Portugal has caused issues for the Spanish banks because of their exposure, and so on through the Eurozone (including Germany). The European banking system, in our view, is still too leveraged, and needs to raise more capital over time. Third, we believe that the fiscal situations in Italy and Spain need to be stabilized. This is not to say that Italy and Spain must reduce their debt immediately, but is largely a case of developing confidence among investors, in our view. This could be accomplished by showing that there is a credible plan in place to decrease current year deficits, and ultimately decrease the total debt outstanding. Unfortunately, we are still not there. Finally, the Greek debt restructuring needs to be finalized. Greece has reached a point where it cannot sustain its debt and will have to restructure, but we have yet to establish the necessary details, much less implement them. If all of the measures described above are carried through, then the European Central Bank (ECB) can more openly provide time to accomplish these objectives by providing financing, purchasing government bonds, or financing banks to purchase those bonds.

On 26 October 2011, the EU made a major announcement that encompassed what we believe were the right agenda items, such as bank recapitalization, insurance on government bonds through the European Financial Stability Facility (EFSF), and the Greek restructuring. Unfortunately, there was not enough detail or substance to these ideas, in our opinion. The 9 December 2011 agreement was much the same; there was some new content, and the governments agreed to accelerate the creation of the European Stability Mechanism (ESM) to July of 2012 from 2013. We believe that the ESM will be a much more robust facility than the EFSF, which, in our view, is largely a dead-on-arrival vehicle at this point. The EU agreed to lend up to €200 billion to the International Monetary Fund (IMF), with the intention that the IMF could use that money to support bond markets and assist European governments that are in trouble. The governments also agreed to continue planning for fiscal union. However, they left us with some lingering uncertainties, such as how a fiscal union might work, how long it might take for 17 countries to modify their constitutions, and why the rules would work this time, when they did not work before. We believe these are important points to keep in mind, but that the problems can be solved, given enough time. Changing constitutions, adopting treaties, and getting voters involved is a process that may well take years. Unfortunately, markets are not likely to give them years to do so.

As previously mentioned, we believe 2012 will be a volatile year. In our opinion, there are six different flash points that could potentially cause market volatility as we move into the new year. The first flash point, in particular, is one of the most worrisome topics right now. It is starting to gain recognition among investors, but not enough in our view. Exhibit 6 displays the amount of government debt and interest that are due on maturities from December 2011 in the PIIGS. If one looks at Italy, one can see that, between February and April of 2012, the country has €150 billion to refinance in a three-month period. To put it in a starker perspective, on 29 February 2012 and 1 March 2012, €45 billion of debt will reach maturity, and Italy will have two days alone to repay it.

In addition, as mentioned before, we do not believe the EFSF will be effective, the ESM will not be in place until July, and the ECB is insisting that they will not buy bonds for these governments. This could put Italy in a difficult position over the next few months. The next flashpoint could be the dissolution of the EFSF if a number of nations, perhaps just one (which would pivotally be France), lose their AAA credit rating from the key credit-rating agencies. We believe this is highly probable given that Standard & Poor's, Moody's, and Fitch all warned of downgrades in the Eurozone. The third flashpoint is a disorderly Greek debt restructuring. We tend to think of it as being off the

Exhibit 6 Debt Refinancing Requirements



- 1 As of 8 December 2011; National Statistical Service, Bloomberg
- 2 As of 8 December 2011; Central Statistics Office, Bloomberg
- 3 As of 8 December 2011; Source: Instituto Nacional de Estadística, Bloomberg
- 4 As of 8 December 2011; INE, Bloomberg
- 5 As of 8 December 2011; ISTAT, Bloomberg

radar, but as previously mentioned the details of a restructuring have not been agreed. Several months ago there was a 21% haircut that bondholders had to agree to voluntarily. The key point is that it had to be voluntary because the EU and the ECB did not want to have Greece declared to be in default. The entities were concerned for two reasons: the first is that it may trigger credit default swaps (CDS), and the potential waterfall effects of that CDS trigger; the second, which we believe to be equally important, is that the ECB cannot accept any security that is technically in default as collateral. They can accept a government bond that is rated 'junk', but not defaulted. The 26 October agreement calls for those bondholders to take not a 21% loss, but a 50% loss. However, we are concerned that if the bondholders do not agree, then it could lead to a disorderly restructuring.

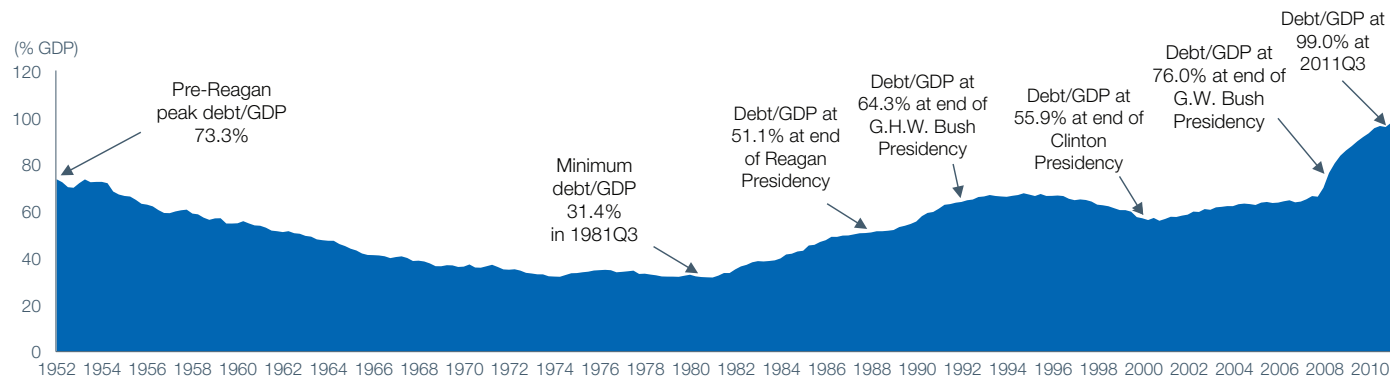
Flashpoints four and five are that domestic elections derail the already agreed upon fiscal union plans, and that voters reject Treaty changes. At this point we are at the ultimate intersection of economics and politics, and the dynamic is much like the task of trying to thread five to ten different needles in exactly the right sequence, all while the needles are moving. Flashpoint number six addresses the aforementioned balancing act between austerity and the need for growth. The primary concern on the economic front in Europe right now is that the countries might have engaged austerity with a little too much vigor, particularly in the peripheral nations, where major benefit cuts for citizens and public sector employees are coming in Portugal and Spain. In addition, although we're seeing a Eurozone consensus GDP of just above 0% for the

fourth quarter this year and the first quarter 2012, that number may become negative and Europe might enter a bigger, or deeper, recession. The key thing to note, as was discussed around Exhibit 1, is that if one's income is shrinking, it is harder to manage debt; therefore, a double-dip recession would be highly negative for the Eurozone.

In contrast, the United States is starting from a very different position. First, as shown in Exhibits 2 through 4, government net debt to GDP outstanding for the U.S. is 73%, 70% of the debt is domestically funded, and the households are very wealthy. The net worth of financial assets for American households, including homes, is \$57 trillion. The total amount of debt outstanding is \$15 trillion, which includes the debt the government owes itself. The U.S. is an example of a very wealthy country with a lot of debt, but debt that can be paid four times over. The second thing to consider is that the United States, like many other countries, still prints its own currency, whereas the individual member nations of the Eurozone gave up their ability to print currency as it is done collectively. Moreover, the dollar is the reserve currency of the world, and U.S. monetary and fiscal authorities are aligned. Therefore, there are positive features of the United States that are important to recognize. However, even with those positive features and a better starting point, we cannot sustain the current trajectory of our deficits.

Exhibit 7

U.S. Debt has Tripled Since 1981



As of 30 November 2011

Debt represented as gross debt and displayed as a percentage of GDP in the period being measured.

Source: Haver Analytics, U.S. Treasury Department, Bureau of Economic Analysis

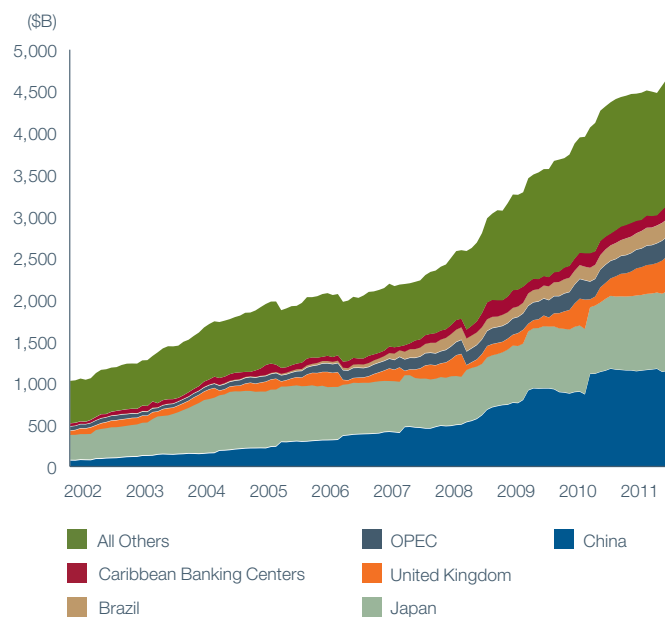
There are a number of ways to look at debt: nominal terms (which is \$15 trillion), inflation-adjusted terms, and relative to the income of the country at hand, which we believe is the best view. In Exhibit 7, one can see that from 1952 to 1981 the debt to GDP ratio in the United States declined from 73% to 31%. It is interesting that some wish to 'return to the Reagan era' to solve

the deficit issue, but under Ronald Reagan's presidency the deficit (or debt to GDP ratio) grew from 31% to 51%. The main reason for this, in our view, was that there were tax cuts that were supposed to be followed by spending cuts, but the spending cuts never happened. Unfortunately, in our view, there has been bipartisan irresponsibility in Washington for the last thirty years, which has taken us to the point where gross deficit is at 99% at the third quarter of 2011. We cannot sustain this trajectory over time.

Exhibit 8

Foreign Investors Still Own less than 1/3 of U.S. Treasuries

Foreign Ownership of U.S. Treasuries



As of 30 November 2011

Debt displayed as a percentage of GDP in the period being measured.

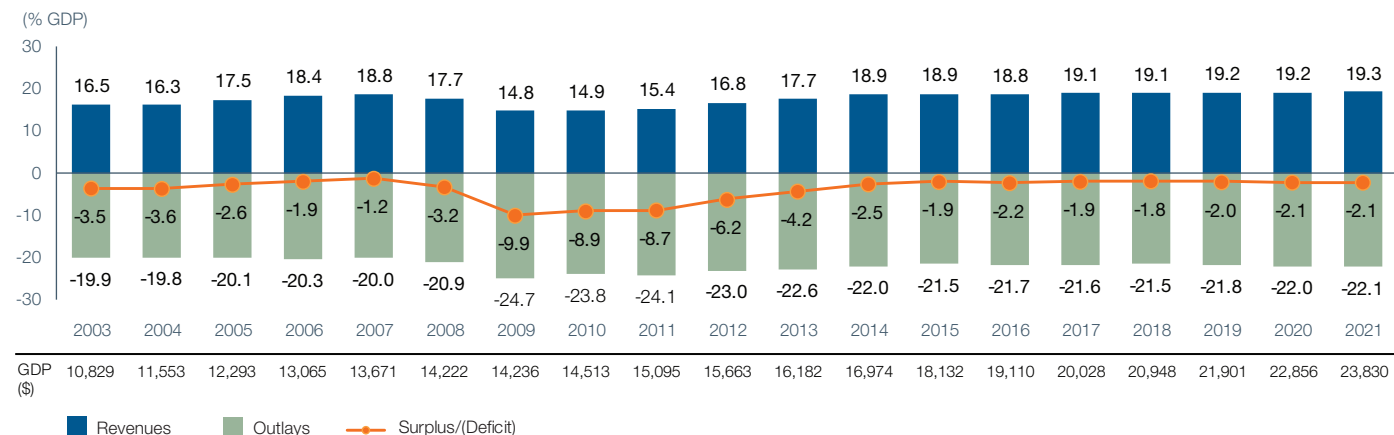
Source: Haver Analytics, U.S. Treasury Department

However, we believe people have been unnecessarily alarmed by the amount of debt owned by foreign investors. As shown in Exhibit 8, since 2002 the amount of debt owned by foreigners increased from \$1 trillion to over \$4 trillion. It should be noted that China, which is the single largest foreign owner, only owns 8% of U.S. Treasuries. Japan owns 7%, and all foreign investors combined own 31% of the debt outstanding. It is also interesting that the U.S. Federal Reserve and the Government Retirement Fund combined own another 42% of the debt. Fifteen years ago, those two numbers combined added up to 45% versus 73% today. In effect, private investors have been largely squeezed out of owning Treasuries over the last few decades.

In terms of moving from the stock of debt to the flow of debt, Exhibit 9 shows the base case according to the Congressional Budget Office (CBO) in terms of where U.S. fiscal deficits are likely headed over the years ahead. However, we adjusted for a few factors. First, we assume that tax cuts for all of the households under \$250,000 of income will become permanent at the end of 2012. It is important to note that these tax cuts cost \$2.5 trillion through 2021. The second adjustment is due to the CBO's requirement to only assess costs that have been legislated, so given that we have no legislated departure date from Afghanistan and Iraq, they must assume that U.S. troops will stay there forever. If

Exhibit 9

The U.S. Fiscal Situation Has Started to Improve



As of December 2011

All fiscal years ending 30 September (e.g., fiscal year 2009 ended 30 September 2009)

Congressional Budget Office August baseline projections. Projections and estimated data are not a promise or guarantee of future results and are subject to change.

Source: The Budget and Economic Outlook: An Update, Table 1-2, August 2011, Congressional Budget Office, Center on Budget and Policy Priorities, Bureau of Economic Analysis, Treasury Department, Lazard estimates

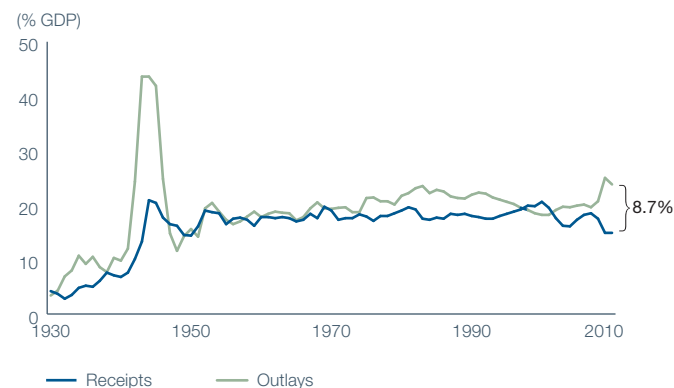
one instead believes that there will be a gradual withdrawal, it will save \$1.3 trillion in expenditures. The CBO also assumes that the Medicare fix to lower payments to doctors will be implemented, although each year Congress postpones the fix to the following January. The CBO must nonetheless assume that Congress will cut these costs every year but, based on history, we assume that those costs will not be cut. In the most recent fiscal year that ended on 30 September 2011, the deficit totaled 8.7% of GDP. Given the assumptions laid out, and supposing moderate real GDP growth, we believe the deficit could be cut by more than half by 2013. As with Italy and Spain, it is not that we have to cut the debt outstanding tomorrow, but we have to prove to the market that we are on the right trajectory. We believe the United States can deliver on that in the next few years.

Exhibit 10 shows another part of the equation, demonstrating that there needs to be compromise. Federal tax receipts, or the federal government's income, are at a 60-year low. At the same time, the government's spending is nearly at a 60-year high, and the gap between the two (8.7%) is the federal budget deficit this year. If you review the numbers in detail, we believe the reality of the situation is that spending needs to be cut, and taxes need to increase. The key challenge we face in the United States, in our view, is getting past the 2012 election, as both parties are trying to paint it as a philosophical test, and also because the looming election is lessening the incentive to compromise. Unfortunately, in order to lower the federal deficit, we believe that compromise is necessary.

Exhibit 10

Federal Tax Receipts Are Near a 60-year Low, and Outlays Are at a 60-year High

Summary of Receipts and Outlays



Data presented through FY2011E

Forecasted or estimated results do not represent a promise or guarantee of future results and are subject to change.

Source: Fiscal Year 2012 Historical Tables—Budget of the U.S. Government, Congressional Budget Office, Bureau of Economic Analysis, Treasury Department

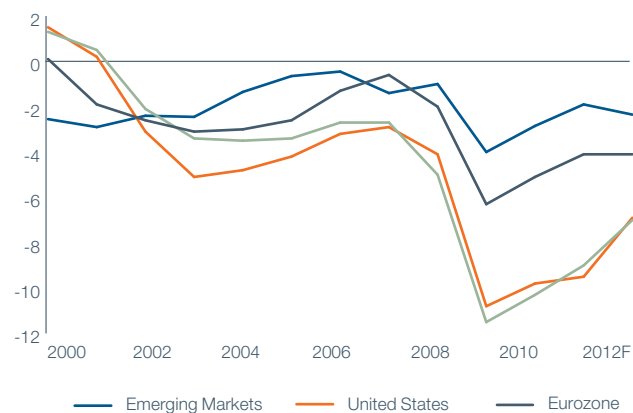
Relative to Europe and the United States, the emerging markets are the ultimate contrast. They are in a much better position fiscally, as is shown in Exhibit 11. The chart on the right displays the total amount of debt outstanding in the emerging markets, United States, United Kingdom, and Eurozone as a percentage of GDP. One can see that the number for the emerging markets is much lower than for the developed markets. The chart on the

Exhibit 11

The Emerging Markets' Fiscal Position is Better than That in the Developed World

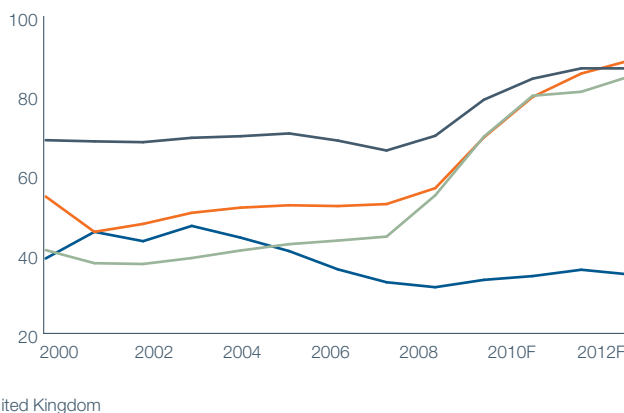
Strong Fiscal Indicators in EM

(Fiscal Deficit as % GDP)



Lower Debt/GDP Ratios in EM

(Debt as % GDP)



As of November 2011

Includes 20 emerging market countries

Source: Moody's, Lazard

Forecasted or estimated results do not represent a promise or guarantee of future results and are subject to change.

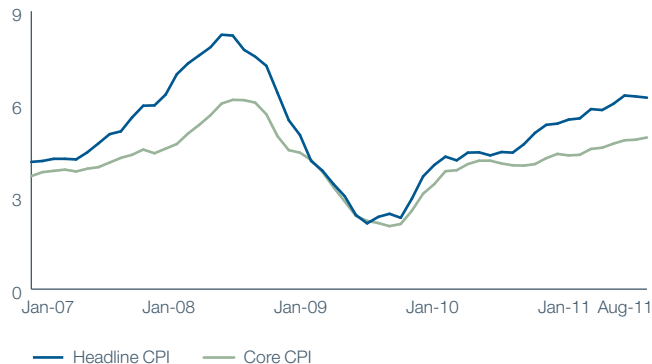
left side shows the annual deficits for emerging markets relative to the same regions, and again the emerging markets are in a much stronger position. Although developed markets affect the emerging markets, emerging market countries have more effectively controlled their fiscal situation through the downturn, and over time have reduced their debt outstanding and their vulnerability to the Western credit crisis, in our opinion.

Exhibit 12

Emerging Market Inflation Appears to be Stabilizing, but Vigilance is Required

Emerging Markets Inflation*

(%)



* Calculated as the sum of individual country year-over-year inflation rates, each weighted by each country's share in total emerging market GDP measured in U.S. dollars.

As of 31 August 2011

Source: IMF World Economic Outlook, Haver Analytics, Lazard

The bigger issue in emerging markets is the balancing act of how to decrease inflation without substantially slowing economic growth. Exhibit 12 shows headline and core inflation data through August 2011. The numbers seem to plateau in August. If the numbers were aggregated since that time, it would show positive signs of inflation declining faster than expected. For example, the latest Chinese inflation figures from November were 4.2% versus 5.5% in October, versus 6.5% in July. This appears to suggest a fairly strong deceleration of inflation. Over the last two years emerging market central banks have been tightening monetary policy to try to slow inflation rates, but we believe they have shifted to an easing mode. This appears to be definitive in some countries, in our view, as evidenced by reserve requirement decreases in China in the last two weeks, and interest rate decreases in Brazil.

In summation, we believe developed markets will face challenges in the years ahead. In particular, Europe may encounter flash points that could cause volatility. The United States and Europe have many common issues, as both have too much debt and need austerity, but also need to maintain GDP growth. We are less concerned about the United States, as the debt issues do not appear to be as pressing. However, the country should not be complacent about this topic, in our view. We believe the emerging markets have controlled inflation well, at least for the present. Their central banks seem to be moving toward easing monetary policy, which in our opinion could be beneficial for those markets.

As we look to 2012 and beyond, we believe that an important lesson of 2011 is that companies are able to grow even if real GDP is sluggish. Consider the hypothetical situation shown in Exhibit 13. The exhibit demonstrates that company revenue growth expectations should take into account real GDP, inflation, market share gains, and international growth. Given these factors, the implied potential corporate revenue growth is 5%–11%, even in a weak economic environment. If we also account for operating leverage and capital management, we can arrive at high single-digit to low double-digit earnings growth per share for listed companies.

Exhibit 13 Even in a Slow Growth Economy, Equities can be Attractive

Real GDP	1–3%
Inflation	+2–3%
Market Share	+0–2%
International Growth	+2–3%
Total	5–10%

For illustrative purposes only.

Considering the macro uncertainty, many investors likely feel the temptation to respond by investing in risk-off investments in order to avoid the volatility of equities. However, we believe that one should consider the opportunity of equities versus debt. One needs to think about risk-reward, as it is currently quite asymmetric. There is not a lot more money to be made by owning a ten-year Treasury if yields go to 1%. On the other hand, if yields go to 5%, you can actually lose quite a bit of money. To the extent one wants fixed income, we find corporate and high yield debt in developed markets, as well as global fixed income strategies and emerging markets debt, interesting. We believe that just as one should understand the companies in an equity portfolio, he or she should do the same in a fixed income portfolio. Understanding where a company gets its revenue, who its competitors are, who its clients are, what its regulators are doing, and having a very forward-looking view of what the company can earn in this economic environment is paramount.

If you look at the third-quarter earnings season for the United States, revenue for the S&P 500, excluding financials, rose over 11% from a year ago, and earnings per share and net income rose 17.5%. Meanwhile, equity markets declined from twelve months ago. We believe it is very important to recognize that despite market volatility, U.S. companies exceeded the hypothetical example from Exhibit 13 last year. However, the market has not recognized it because of elevated macro uncertainty.

We believe there are very good opportunities for investments in the long term, if security selection is well managed. The economic environment we anticipate over the next several years is not going to be the economic environment we saw in the last twenty or thirty years, in our opinion. Recognizing this, we believe bottom-up security selection, as well as having a forward-looking view and fundamental research to support it, is pivotally important.



Important Information

Published on 1 February 2012.

This summary is for informational purposes only. The information and opinions presented does not constitute investment advice and has been obtained or derived from sources believed by Lazard to be reliable. Lazard makes no representation as to their accuracy or completeness. All opinions and estimates expressed herein are as of the date published and are subject to change. This summary is not intended to, and does not constitute, an offer to enter into any contract or investment agreement in respect of any product offered by Lazard Asset Management and shall not be considered as an offer or solicitation with respect to any product, security, or service in any jurisdiction or in any circumstances in which such offer or solicitation is unlawful or unauthorized or otherwise restricted or prohibited.

Equity securities will fluctuate in price; the value of your investment will thus fluctuate, and this may result in a loss.

This summary and all research and materials enclosed are the property of Lazard Asset Management LLC.

© 2012 Lazard Asset Management LLC. **Australia:** Issued by Lazard Asset Management Pacific Co., Level 39 Gateway, 1 Macquarie Place, Sydney NSW 2000. **Germany:** Issued by Lazard Asset Management (Deutschland) GmbH, Neue Mainzer Strasse 75, D-60311 Frankfurt am Main. **Japan:** Issued by Lazard Japan Asset Management K.K., ATT Annex, 7th Floor, 2-11-7 Akasaka, Minato-ku, Tokyo 107-0052. **Korea:** Issued by Lazard Korea Asset Management Co. Ltd., 10F Seoul Finance Center, Taepyeongno-1ga, Jung-gu, Seoul, 100-768. **United Kingdom:** For Professional Investors Only. Issued by Lazard Asset Management Ltd., 50 Stratton Street, London W1J 8LL. Registered in England Number 525667. Authorised and regulated by the Financial Services Authority (FSA). **United States:** Issued by Lazard Asset Management LLC, 30 Rockefeller Plaza, New York, NY 10112.