THE NEW YORK FAMILY OFFICE

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Economic Outlook

Positive Trends in the U.S. Economy: Is America Out of the Woods? (Page 2)

Business & Finance

Are There Signs for Rethinking Production in the U.S.? (Page 2)
Pricing Pressure on Natural Gas (Page 3)
Immense Oil Shale Reserves in the U.S. (Page 4)

Taxes

What is FATCA and What Are the Consequences? (Page 4)
What Can You Learn from Mitt Romney's Tax Return? (Page 5)

Market & Financial Data

Economic Indicators & U.S. Dollar Foreign-Exchange Rates (Page 6)
Interest Rates, Real Estate & Taxes (Page 7)

Positive Trends in the U.S. Economy: Is America Out of the Woods?

The economic data continue to show increasingly positive trends in the U.S. economy, amid weakening global economic activity. In particular the acceleration in employment gains and simultaneous decline in the unemployment rate are key improvements, which lead to increases in personal income, lend support to consumer spending and moderately create new jobs.

There is partially cautious optimism that the recent pace of more than 200,000 payroll gains per month could be sustained through the summer. Compared to the beginning of the year the sentiment has brightened and the increase in personal income will be critical for further development.

Annual growth expectations of 2% on average for 2012 at the beginning of the year have been revised up slightly for the second half of the year, though growth should remain moderate by historic standards at less than 3%.

There remains the risk that a trade-off between more jobs and weaker productivity gains will unfold. Such a trade-off would imply little change to overall GDP growth and explains in large part our continued cautious outlook as we expect real growth to stay at 2-3% on average in 2012. The anticipated slowdown in productivity and pick up in employment costs should underpin just modest corporate profit growth. Also adding to the profit margin squeeze is the inability of firms to fully pass along higher input costs to consumers. The challenging pricing environment for corporations bodes well for overall inflation pressures in the U.S. as excessive slack in the economy keeps a lid on prices.
The U.S. economy still faces headwinds from higher gasoline and oil prices, ongoing consumer caution, the winding down of U.S. fiscal stimulus and slower emerging market growth. In addition, the largest threat to the economic recovery in the U.S. is the European debt crisis and there are fears that an uncontrolled development in Europe could turn the U.S. expansion back into recession. It fits into this big picture that the Federal Reserve Bank announced on January 25, 2012 that the U.S. economy is improving but not enough to warrant higher interest rates for at least two and a half more years. The central bank indicated that it expects to keep the federal funds rate near historic lows until late 2014.

Are There Signs for Rethinking Production in the U.S.?

Over the past several decades the U.S. has experienced a continual deterioration of its manufacturing base and with it a loss of its manufacturing technology and skilled labor.

However, there are signs for rethinking in the U.S. Attitudes are changing toward a healthy recognition of the need to invest in core manufacturing strengths, develop trained skilled labor and put the jobless back to work.

The U.S. economy created 27 million jobs from 1990 through 2008, but 98% were in the service sector of the economy. Over this period of time, the non-service or production sector only created 600,000 new jobs. Part of the slow growth was a result of labor-saving technology advancements, which permanently eliminated jobs. The main reason was, however, that manufacturing jobs held by the middle class moved overseas, offsetting growth in high value-added service jobs in finance, consulting, and computer design. The crucial engine for the service sector was the strong domestic demand with an American consumer who enjoyed spending lots of money.

The financial crisis that began in 2008 curbed U.S. domestic demand almost immediately and it has not come back, making it difficult for continued job growth in the service sector. In contrast to the crisis in Japan in the nineties, where overleveraged corporations caused a "lost decade", in the current crisis corporate America is generally doing very well (except for the financial sector). Instead the U.S. is experiencing overleveraged personal households. In addition, leverage has widened through several "rescue packages" and bail-outs to public households.

Asset values have fallen and have not rebounded. Americans are sidelining their debt-fueled spending and consumption. They use money to repay debt, save more or simply cover living expenses. The government is strapped with its own budget woes due to lower tax revenues and rising expenditures. This situation will only improve gradually.

The slow economic recovery – without creating as many new jobs as experienced after prior recessions – increasingly raises questions on how the vast number of unemployed can secure jobs. Some see the key to preventing a long period of high U.S. unemployment as getting the production sector in a position to make up for the slack in the service sector. Their main focus is on strengthening production in the U.S.

However, there are additional factors and trends, which support the U.S. manufacturing base and create a re-birth of "Made in America". This is largely due to a „leveling of the competitive playing field" primarily associated with labor and transport related costs becoming increasingly more favorable for U.S. manufacturing. When considering the costs and related factors of manufacturing products in a foreign country versus on U.S. soil along with high unemployment plus revitalized federal, state and local incentives and tax breaks, „Made in America" is at least on parity with foreign manufacturing, if not better.

Pricing Pressure on Natural Gas

U.S. energy companies are extracting so much natural gas out of the ground that prices fell in the first quarter to their lowest level in over two years. This situation is not likely to change anytime soon. This is good news for people who use gas to heat homes and for companies that use it to power factories. For U.S. energy companies, however, the domestic natural gas market is looking increasingly out of whack.

Despite a 32% drop in prices last year, onshore production rose 10%, and it is expected to rise another 4% this year, according to Barclays Capital.

Many energy companies have shifted their focus away from natural gas to more profitable oil. Still, natural gas is often a byproduct of oil drilling, and according to some reports some companies are opting to burn off the gas they find because they don't have a way to transport it.

Oil production is not the only factor boosting natural gas supplies. Some gas fields produce so much ethane, a valuable liquid used to make plastics, that companies will drill regardless of gas prices. In addition, some companies need to continue drilling so they do not violate lease terms on millions of acres of land. These deals were struck when gas prices were high.

The growth in energy exploration and production is due to the widespread use of horizontal drilling and hydraulic fracturing, or fracking. Horizontal drilling allows energy companies to extract gas and oil up to a mile away from the actual well. Meanwhile, fracking – which involves pumping millions of gallons of water, sand and chemicals to break open dense rocks and release hydrocarbons – has enabled the industry to tap into energy-rich shale formations once overlooked by petroleum geologists. The exploitation of shale oil and

gas is seeing a boom despite increasing reports about environmental and health issues caused by fracking.

Immense Oil Shale Reserves in the U.S.

One of the largest oil shale reserves world-wide is located in the Green River Formation, which stretches across parts of Colorado, Utah and Wyoming. Estimated oil shale reserves in this region total between 1.2 and 1.8 trillion barrels of oil. Probably not all of this oil can be explored but even conservative estimates of 800 billion barrels of oil are approximately three times as much as the stated reserves of Saudi Arabia.

Who owns the land in the Green River Formation? Interestingly, more than 70% of the land – including the thickest and richest oil shales – are owned by the Federal Government of the U.S. which therefore has direct control over access to the commercially most attractive parts of the reserves.

What is FATCA and What Are the Consequences?

In March of 2010, President Obama signed the Foreign Account Tax Compliance Act (FATCA) into law to prevent tax evasion of U.S. citizens and residents through offshore accounts.

Many U.S. citizens and Green Card holders will run into FATCA for the first time when preparing their 2011 income tax returns. In addition to the Foreign Bank Account Reporting (FBAR) which is reported and filed separately from their income tax return on Form TD F 90.22-1, taxpayers have to attach Form 8938 to their 2011 returns under the FATCA Foreign Financial Assets Reporting rules.

This set of reporting rules sits alongside existing requirements to report foreign bank accounts (FBAR rules). The FATCA rules are tax rules. The FBAR rules are Treasury Department, Bank Secrecy Act rules. Form 8938 is filed to comply with the FATCA rules. Form TD F 90-22.1, which has been in existence since the 1970s, is required under the FBAR rules.

While there is some overlap the scope of FATCA disclosure is clearly broader than FBAR. Therefore, taxpayers who are not required to file FBAR may need to file Form 8938 under FATCA. (Example: Foreign mutual funds, hedge funds, and private equity funds are included under the FATCA reporting, while they are excluded from FBAR.)

Generally, taxpayers must file Form 8938 with their tax returns if the aggregate value of all specified foreign financial assets exceeds $50,000 at the end of the year or $75,000 at any time during the year. There are severe penalties for not filing Form 8938 plus the statute of limitations can be extended.

The new FATCA rules not only affect U.S. citizens and residents but also domestic and foreign financial institutions. The law will require foreign financial institutions (FFIs) to disclose their U.S. account holders' identity and account information by way of entering into an FFI Agreement with the IRS. FFIs who decide not to participate in the program are subject to a 30% withholding tax on all "withholdable payments." Withholdable payments include interest, dividends and other U.S. sourced payments that are already subject to FDAP withholding as well as gross proceeds from the disposition of U.S. securities.

On February 8, 2012 the Treasury and the IRS issued long awaited proposed regulations under FATCA. At the same time, Treasury also released a joint statement from the United States, France, Germany, Italy, Spain and the United Kingdom announcing an agreement to explore an intergovernmental approach to FATCA im-

plementation that would allow FFIs in each country to provide the information required under FATCA to that country's tax authorities rather than to the IRS.

In return the U.S. declared to reciprocate in collecting and exchanging on an automatic basis information on accounts held in U.S. financial institutions for residents of France, Germany, Italy, Spain and the United Kingdom. (Note: The release of the final FATCA regulations is expected for the summer of 2012.)

As a reaction to the FATCA reportings and the increased compliance burden for financial institutions, several foreign banks are currently denying U.S. citizens and residents banking services, closing long-held accounts and refusing to open new accounts. It is expected that other foreign banks will follow. However, a few foreign financial institutions view this situation as an opportunity to comply with the new regulations and gain those U.S. persons as clients if they have certain minimum deposits. If required The New York Family Office can help to make an introduction.

What Can You Learn from Mitt Romney's Tax Return?

2012 is a presidential election year and the couple Mitt and Ann Romney reacted to increasing pressure to disclose their 203 pages long 2010 Federal Tax Return (Form 1040). While the couple paid almost $3 million in taxes, that amounted to less than 14% of their $21.6 million income. Various tax experts analyzed their tax return and the Wall Street Journal published on January 28, 2012 an article with the headline "What You Can Learn From Mitt's Tax Return". The result: The Romneys' tax advisors used many (though not all) perfectly legal opportunities to reduce and defer taxes. Their tax return is a good case study of effective tax planning for other U.S. taxpayers and some of the tips will be discussed below:

1. Avoid salary, wages and tips (to the extent possible)
The Romneys reported no such compensation which is taxable at rates up to 35%. In addition, these types of pay are subject to payroll taxes: a 6.2% Social Security tax (lowered to 4.2% in 2011) and 1.45% in Medicare tax, both of which the employer matches.

2. Strive for "qualified" dividends
Simply speaking "qualified" dividends are dividends from stocks held at least two months and paid by any domestic corporation or most foreign corporations. "Qualified" dividends are taxed at a top rate of 15% and are not subject to the alternative minimum tax (AMT).

3. Generate income from long-term capital gains
The biggest factor in the Romneys' super-low tax rate is their outsize income from long-term capital gains (LTCG). Like "qualified" dividends LTCG are taxed at a top rate of 15% and are not subject to the AMT.
LTCG have additional benefits. While wage earners have almost no flexibility as to timing of their income, the capital gains rules offer unparalleled flexibility. Investors can often time when they take a gain or loss.

4. Realize capital losses
Savvy investors sometimes realize investment losses during market downturns, reacquire the investment after 30 days and use the losses to offset future gains. Please note that there are some restrictions with regards to losses offsetting gains.

5. Beware of small benefits requiring large tax preparation efforts
Avoid small tax benefits that cause large tax preparation efforts for your tax advisors. Often tax preparation fees are disproportionate to the reduction in the overall tax burden.

Economic Indicators & U.S. Dollar Foreign-Exchange Rates

Economic Indicators	Jan. 2011	Nov. 2011	Dec. 2011	Jan. 2012	Feb. 2012
Employment	110,000	157,000	203,000	243,000	227,000
Unemployment Rate	9.1%	8.7%	8.5%	8.3%	8.3%
Avg. Weekly Hours (Manuf.)	40.4	40.4	40.6	40.9	41.0
Avg. Overtime Hours (Manuf.)	3.2	3.3	3.3	3.4	3.4
Building Permits	568,000	680,000	671,000	682,000	717,000
Housing Starts	636,000	685,000	689,000	706,000	698,000
Consumer Confidence Index	60.6	64.1	67.7	61.5	71.6
Purchasing Managers Index	59.9	52.2	53.1	54.1	52,4

Other Indicators	Jan. 30 2009	Jan. 29 2010	Jan. 31 2011	Jan. 31 2012	Feb. 29 2012	Mar. 30 2012
S&P 500 Index	825.88	1,073.87	1,286.12	1,312.41	1,365.68	1,408.47
S&P 500 - Trading Volume (in thousands)	5,350,580	5,412,850	4,167,160	4,235,550	4,482,370	3,676,890
VIX (Volatility Index)	44.84	24.62	19.53	19.44	18.43	15.50

Real GDP	2010	2011	2010 Q4	2011 Q1	2011 Q2	2011 Q3	2011 Q4
Real GDP	3.0%	1.7%	2.3%	0.4%	1.3%	1.8%	3.0%

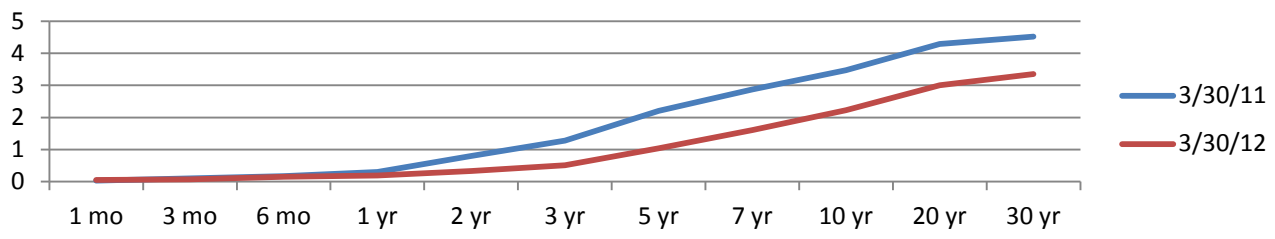
Inflation	2010	2011	Jan. 2012	Feb. 2012
Inflation	1.6%	3.2%	2.9%	2.9%

Currency Exchange Rates	Dec. 31 2009	Dec. 31 2010	Dec. 31 2011	Jan. 31 2012	Feb. 29 2012	Mar. 30 2012
EUR / USD	1.4332	1.3252	1.2949	1.3152	1.3431	1.3301
GBP / USD	1.5926	1.5468	1.5453	1.5694	1.5848	1.5903
CHF / USD	0.9634	1.0629	1.0640	1.0908	1.1144	1.1035
CAD / USD	0.9529	0.9998	0.9804	0.9959	1.0032	1.0011
CNY / USD	0.1463	0.1512	0.1571	0.1586	0.1586	0.1580
JPY / USD	0.0108	0.0123	0.0129	0.0131	0.0124	0.0121

Note: Some Numbers May Be Updated Due to Revisions of Official Statistics.

Interest Rates, Real Estate & Taxes

Treasury Yield Curve (in %)



Base Rates	Apr. 2, 2012	2 Weeks Ago	One Year Ago
30 Day LIBOR	0.24%	0.24%	0.24%
U.S. Treasury			
5 Year	1.03%	1.20%	2.23%
10 Year	2.20%	2.39%	3.47%

Source: Cushman & Wakefield Sonnenblick Goldman

10-Year Fixed Rate Ranges by Asset Class	Max. LTV	Class A	Class B/C
Anchored Retail	70-75%	T + 270	T + 280
Strip Center	65-70%	T + 290	T + 305
Multi Family (Non-Agency)	70-75%	T + 235	T + 240
Multi Family (Agency)	75-80%	T + 190	T + 195
Distribution/Warehouse	65-70%	T + 285	T + 300
R&D/Flex/Industrial	60-65%	T + 295	T + 310
Office	65-70%	T + 270	T + 290
Full Service Hotel	55-65%	T + 325	T + 350

Note: T = Interest Rate for 10-Year U.S. Treasury (2.20%)
Source: Cushman & Wakefield Sonnenblick Goldman (April 2, 2012)

Simplified Presentation of the Most Important U.S. Federal Tax Rates:	
Income Tax	10-35%
Long-Term Capital Gains (LTCG)	15%
"Qualified" Dividends	15%
Corporate Tax	15-35%
Gift and Estate Tax	18-35%

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