SPDR UNIVERSITY

2011 MID YEAR SPDR® ETF OUTLOOK

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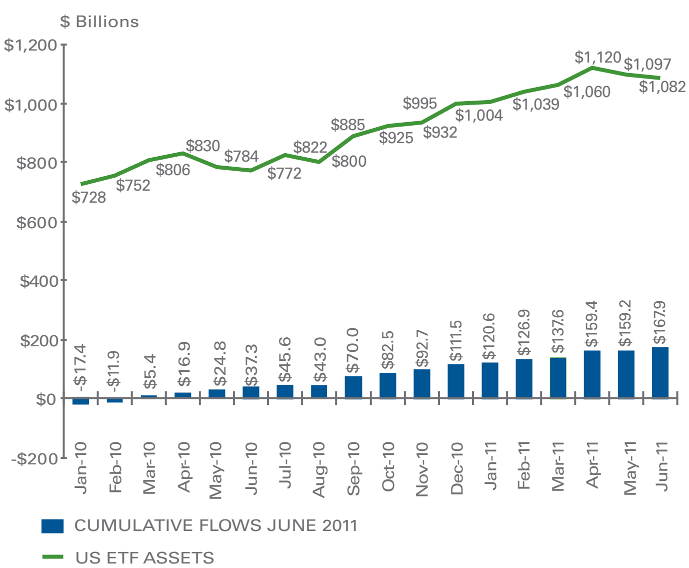
The first half of 2011 had no shortage of unique events which have helped to drive market returns. Unrest in the Middle East, the earthquake and subsequent tsunami in Japan, uncertainty surrounding the municipal bond markets, inflationary pressures in the emerging markets and continued concerns of sovereign risk in Europe to name a few. Place these against a backdrop of historically low interest rates and continued high unemployment in the US, as well as a global economy still feeling the effects of the credit crisis and what would one have? You might expect a seemingly precarious market environment. However, US companies have seen revenues rise, profit margins swell and, along with many developed international companies, are now trading at relatively attractive prices. This dichotomy of market forces has made for a very interesting start to the year.

Not surprisingly, this market unrest has been reflected in Exchange Traded Fund (ETF) flows. During the first six months of the year, US ETFs took in an impressive $56.3 billion, an increase of over 50.9% in comparison to the first half of 2010 when net new inflows totaled $37.3 billion. At this pace, 2011 inflows are poised to surpass last year's total of $111.5 billion.

FIGURE 1: ETF CASH FLOW AND ASSET GROWTH



Source: Bloomberg, SSgA Global ETF Strategy & Research, as of 6/30/2011.

The fixed income, developed international and dividend/fundamental categories lead inflows with gains of $16.3 billion, $12.6 billion and $6.4 billion, respectively. Whereas the emerging markets, US small cap and commodity sectors lead outflows with $3.7 billion, $2.2 billion and $2.1 billion, respectively.[1]

2011 INVESTMENT RESULTS

REITs rewarded investors in the first half of 2011, returning 10.9%. US mid cap equities also provided strong returns of 8.6%, while small caps returned 7.5% and large caps added 6.0%. Investors in gold were also rewarded with solid performance of 7.1%, as this asset class continues to be in favor.

Emerging market stocks were the laggards during the first six months of the year, returning only 0.9%. In contrast, the MSCI EAFE Index returned almost 5.0%. This was a marked change from the prior two years during which emerging markets significantly outperformed their developed counterparts.

Bonds also fared well, given the prevailing low interest rate environment. Bonds linked to inflation, international in particular, benefitted from increased consumer prices both here in the US and around the world. International inflation linked bonds managed to achieve an 8.1% return. International bonds returned nearly 6%, helped by the relative weakness in the US dollar in the first half of 2011. Risk was also rewarded in the bond market, as high yield bonds were up 4.8%.

The strong performance in commodities that has been enjoyed over the past two years was tempered during the first six months of 2011. While the return for gold was greater than 7%, the broader asset class, as measured by the Dow Jones UBS Commodities Index, returned -2.6% during the first half of the year.

FIGURE 2: 2011 YTD PERFORMANCE BY ASSET CLASS

ASSET CLASS	INDEX	2011 YTD TOTAL RETURN (USD)
US REITS	Dow Jones US Select REIT Index	10.93%
US MID CAP EQUITIES	S&P MidCap 400® Index	8.56%
NON-US TIPS	DB Global Government ex-US Inflation Linked Bond Capped Index	8.06%
US SMALL CAP EQUITIES	S&P SmallCap 600® Index	7.54%
GOLD	London PM Fixing (Spot Price)	7.11%
US LARGE CAP EQUITIES	S&P 500® Index	6.02%
INTERNATIONAL BONDS	Barclays Capital Global Treasury ex-US Capped Index	5.97%
US TIPS	Barclays Capital US Government Inflation-Linked Bond Index	5.84%
INTERNATIONAL EQUITIES	MSCI EAFE Index	4.98%
US HIGH YIELD BONDS	Barclays Capital Very Liquid High Yield Index	4.83%
US FIXED INCOME	Barclays Capital U.S. Aggregate Index	2.72%
INTERNATIONAL SMALL CAP EQUITIES	S&P Developed Ex–U.S. Under USD2 Billion Index	2.47%
EMERGING MARKET EQUITIES	MSCI Emerging Markets Index	0.88%
COMMODITIES	Dow Jones UBS Commodities Index	-2.58%
EMERGING MARKET SMALL CAP EQUITIES	S&P Emerging Under USD2 Billion Index	-4.13%

Source: FactSet, SSgA Global ETF Strategy & Research, as of 6/30/2011.

So what did this mean for investors? In general, for investors who were not invested in all cash, returns have been modestly favorable. A blend of 60% of the S&P 500 Index and 40% of the Barclays Capital Aggregate Bond Index would have provided a return of 4.70%,[2] a relatively decent figure, but a far cry from the double digit performance achieved in 2009 and 2010.

Based on the year-to-date returns in Figure 2, an investor would have been better served with a more diversified portfolio by adding US small and mid cap stocks, developed international stocks, REITs, inflation protected bonds, high yield bonds and gold to a simple blend of large cap stocks and bonds.

STRONG ETF FLOWS PROPEL INDUSTRY'S GROWTH IN 2011

Through June 2011, ETF assets increased by $87.2 billion—a gain of almost 9%. With a positive cash flow of $56.3 billion, this growth was driven by more than just market appreciation. At this pace, 2011 will mark the fifth straight year that ETF inflows have exceeded $100 billion.

FIGURE 3: ETF NET FLOWS

2007 ETF FLOWS	$149,027
2008 ETF FLOWS	$178,395
2009 ETF FLOWS	$116,010
2010 ETF FLOWS	$111,447
2011 YTD FLOWS	$56,318

Source: Bloomberg, NSX, SSgA Global ETF Strategy & Research, as of 6/30/2011.

Investors concentrated their investments in several asset classes, most notably fixed income, developed international and dividend strategies. With inflationary pressures possibly causing concern for investors, international flows have come into developed markets at the expense of emerging markets.

FIGURE 4: ETF CATEGORIES WITH HIGHEST INFLOWS YTD 2011

ETF CATEGORY	2011 NET FLOWS ($ MILLIONS)
FIXED INCOME	16,251.32
INTERNATIONAL—DEVELOPED	12,613.09
DIVIDEND/FUNDAMENTAL	6,398.31
INVERSE/LEVERAGED	5,389.80
SPECIALTY—DOMESTIC	3,606.50

Source: Bloomberg, SSgA Global ETF Strategy & Research as of 6/30/2011.

In addition to the emerging markets, investors mostly pulled money from US small cap stocks, commodities, US small cap value stocks and financials. Interestingly, the commodities, financials and small cap categories had net positive flows through April. In May and June, fixed income ETFs garnered the greatest flows. This was reflective of investors paring back risk and turning more defensive as default concerns in Greece heightened.

FIGURE 5: ETF CATEGORIES WITH HIGHEST OUTFLOWS YTD 2011

ETF CATEGORY	2011 NET FLOWS ($ MILLIONS)
INTERNATIONAL—EMERGING	-3,722.65
SIZE—SMALL CAP	-2,215.11
COMMODITY	-2,109.95
STYLE—SMALL VALUE	-332.69
SECTOR—FINANCIALS	-253.08

Source: Bloomberg, SSgA Global ETF Strategy & Research, as of 6/30/2011.

While the first half of 2011 has presented investors with a host of significant market events and diverging trends, some investment themes have managed to stay consistent.

INCOME GENERATION

Another multi-year trend that has continued into 2011 is the increased investment in ETFs that provide exposure to high dividend paying stocks. With government bond interest rates near historic lows and cash rates virtually at zero, investors have been starved for income in their portfolios. Investors have embraced the notion of "getting paid while they wait," rather than counting on capital appreciation. Dividend-oriented ETFs offer the potential for capturing much of the upside of traditional equities while providing higher yields. Historically, dividend income has contributed approximately one third of total equity returns to the S&P 500 Index. This percentage has historically been even greater in the international markets.[3]

With US government securities offering historically low yields and significant price risk in the event of rising interest rates, ETF investors may begin to look for other bond (or hybrid) investment opportunities in the second half of 2011. Three intriguing options that offer attractive yields and decreased interest rate sensitivity are convertible bonds, preferred stocks and high yield bonds. Because they are convertible to equity shares, convertible bonds are true hybrid securities. In addition, they tend to offer a greater upside potential than traditional bonds, but with more downside protection than stocks.

RETHINKING ASSET ALLOCATION WITH REAL ASSETS

In an effort to enhance returns and lower their risk profile, many sophisticated investors continue to look to improve the diversification of their portfolios. Decreased risk can often be achieved by adding investments with low or negative correlations. This means that the investments do not move in synch with other asset classes. In other words, one asset may have positive returns, while the other is negative.

Equity markets tend to be highly correlated. For example, over the past fifteen years ending June 2011, the S&P 500 Index has experienced a 0.90 correlation to the S&P 400 Index, suggesting that US large cap stocks and US mid cap stocks have a high tendency to move in the same direction. In contrast, the S&P 500 Index and the MSCI EAFE Index have a correlation of 0.84.[4] This implies that international stocks are slightly less correlated to US large cap stocks.

On the other hand, stocks and bonds tend to have low correlations. Over the same time period, the correlation between the S&P 500 Index and the Barclays Capital Aggregate Index was 0.01.[5] From a diversification standpoint, the most desirable investments tend to have positive returns and low or negative correlations with other assets.

As ETF investors expand their search for non-correlated returns in 2011, one investment area poised for significant growth is the real assets category, which includes inflation-linked bonds, real estate investment trusts, natural resources stocks and commodities. In addition to their correlation benefits, real assets can also help protect portfolios against inflation, which could resurface in earnest as economic conditions continue to improve.

FIGURE 6: CORRELATIONS TO TRADITIONAL ASSET CLASSES

	CORRELATION TO S&P 500 INDEX	CORRELATION TO BARCLAYS CAPITAL AGGREGATE INDEX
BARCLAYS CAPITAL US GOV'T INFLATION LINKED BOND INDEX	0.28	0.74
DEUTSCHE BANK INTERNATIONAL INFLATION PROTECTED INDEX	0.70	0.53
DOW JONES GLOBAL SELECT REAL ESTATE INDEX	0.90	0.27
S&P GLOBAL NATURAL RESOURCES INDEX	0.77	0.13
GOLD	0.02	0.42

Source: SSgA Global ETF Strategy & Research, Zephyr StyleADVISOR, as of 6/30/2011.

BROADENING PORTFOLIOS WITH NON-US EXPOSURE

Around the world, most investors exhibit a significant home country bias in their portfolios. According to the 2010 World Wealth Report, high net worth investors in North America, Europe and Asia-Pacific held between 59% and 76% of their portfolios in their local regions. North American investors demonstrated the most home bias, holding only 24% of assets outside North America. Similar data can be found from an analysis by Cerulli Associates of mutual fund and separate account wrap programs at brokerage firms. In the second quarter of 2010, they found that only 15-16% of those accounts were invested in international equities.[6]

From an asset allocation standpoint, US investors remain underinvested in non-US investments. Consider that:

- Non-US equities represent approximately 58% of total world equity market capitalization.[7]
- Non-US bonds represent approximately 65% of total world bond issuance.[8]

We expect to see ETF investors continue to expand allocations to markets outside their home country. One critique of international diversification has been the increase in correlations among US, European, Asian and emerging market equities. However, untapped opportunities such as small cap equities remain in different regions. In addition, even as we have seen increased correlations across countries, sectors remain less correlated globally.

CONCLUSION

While the first half of 2011 has been fairly fruitful for investors, it has been marked with uncertainty and a growing consensus of slower economic growth for the remainder of the year. With inflows totaling more than $56 billion, ETF assets climbed almost 9% through June 30, 2011, with a wide range of asset classes providing positive total returns. In general, risk was rewarded in the US with small cap stocks outperforming large caps, and riskier junk bonds outperforming the broad bond market. This was not the case for international equities, where emerging markets and international small caps struggled. Unlike 2010, developed market stocks have outperformed the emerging markets, with small cap international stocks underperforming larger cap names.

Looking ahead to the remainder of 2011 and into 2012, one may reasonably forecast the following for the ETF industry:

1. ETFs that track the non-US equity and fixed income markets will continue to be areas of future growth.
2. Investors will continue to seek income-oriented investments, whether it is with dividend-oriented ETFs or fixed income ETFs with higher yields, such as high yield bonds, convertible bonds or preferred stocks.
3. There will be a greater emphasis on inflation protected and lower duration bonds, as investors become increasingly wary of increased inflationary pressures and potential rate hikes both in the US and around the world.
4. The search for diversification will continue, as investors try to add investments with low or negative correlations to stock and bonds, which typically can be found in commodities, natural resource stocks, inflation linked bonds and REITs.
5. With a recent increase in Active ETF filings and after relatively incremental growth to date, actively managed ETFs will begin to gain traction.

DIVIDEND ORIENTED SPDR ETFS
– SPDR S&P Dividend ETF (SDY)
– SPDR S&P International Dividend ETF (DWX)
– SPDR S&P Emerging Markets Dividend ETF (EDIV)

INCOME ORIENTED BOND SPDR ETFS
– SPDR Barclays Capital Convertible Bond ETF (CWB)
– SPDR Wells Fargo Preferred Stock ETF (PSK)
– SPDR Barclays Capital High Yield Bond ETF (JNK)

REAL ASSET-ORIENTED SPDR ETFS
– SPDR Barclays Capital TIPS ETF (IPE)
– SPDR DB International Inflation Protected Securities ETF (WIP)
– SPDR Dow Jones Global Real Estate ETF (RWO)
– SPDR S&P Global Natural Resources ETF (GNR)
– SPDR Gold Shares (GLD)

INTERNATIONAL SMALL CAP SPDR ETFS
– SPDR S&P International Small Cap ETF (GWX)
– SPDR S&P Emerging Markets Small Cap ETF (EWX)
– SPDR Russell/Nomura Small Cap Japan ETF (JSC)

ABOUT SPDR® ETFS
SPDR ETFs are a comprehensive fund family of over 100 ETFs, spanning an array of international and domestic asset classes. Offered by State Street Global Advisors, SPDR ETFs provide investors with the flexibility to select investments that are precisely aligned to their investment strategy. Recognized as the industry pioneer, State Street created the first ETF in 1993 (SPDR S&P 500® – Ticker SPY). Since then, we've sustained our place as an industry innovator through the introduction of many ground-breaking products, including first-to-market launches with gold, international real estate, international fixed income and sector ETFs.

For information about our ETF family, visit www.spdrs.com

INDEX DEFINITIONS

BARCLAYS CAPITAL AGGREGATE INDEX

The Barclays Capital U.S. Aggregate Index represents the securities of the US dollar-denominated, investment grade bond market. The Index provides a measure of the performance of the US dollar-denominated, investment grade, bond market, which includes investment grade (must be Baa3/BBB- or higher using the middle rating of Moody's Investor Service, Inc., Standard & Poor's, and Fitch Rating) government bonds, investment grade corporate bonds, mortgage pass through securities, commercial mortgage backed securities and asset backed securities that are publicly offered for sale in the United States.

BARCLAYS CAPITAL US GOVERNMENT INFLATION-LINKED BOND INDEX

The Barclays U.S. Government Inflation-linked Bond Index measures the performance of the inflation-protected public obligations of the US Treasury. Inflation-protected public obligations of the US Treasury, commonly known as "TIPS," are securities issued by the US Treasury that are designed to provide inflation protection to investors. The Index includes publicly-issued, US Treasury inflation-protected securities that have at least 1 year remaining to maturity on index rebalancing date, with an issue size equal to or in excess of $500 million.

BARCLAYS CAPITAL VERY LIQUID HIGH YIELD INDEX

he Barclays Capital High Yield Very Liquid Index includes publicly-issued, US dollar-denominated, non-investment grade, fixed-rate, taxable corporate bonds that have a remaining maturity of at least one year, regardless of optionality, are high-yield using the middle rating of Moody's, S&P, and Fitch, respectively, and have $600 million or more outstanding face value.

BARCLAYS CAPITAL GLOBAL TREASURY EX-US CAPPED INDEX

The Barclays Capital Global Treasury Ex-US Capped Index tracks fixed-rate, local currency sovereign debt of investment-grade countries outside the United States.

DB GLOBAL GOVERNMENT EX-US INFLATION-LINKED BOND INDEX

The DB Global Government ex-US Inflation-Linked Bond Index measures the total return performance of inflation-linked government bonds from developed and emerging market countries outside of the United States. The Index includes government debt (direct obligations of the issuer country) but does not include quasi-government debt or corporate debt. The securities are denominated in and pay coupon and principal in the domestic currency of the issuer country. The following countries are included: Australia, Brazil, Canada, Chile, France, Germany, Greece, Israel, Italy, Japan, Mexico, Poland, South Africa, South Korea, Sweden, Turkey, Uruguay and the United Kingdom. In addition, the securities in the Index must be inflation-linked and have certain minimum amounts outstanding, depending upon the currency in which the bonds are denominated. To be included in the Index, bonds must: (i) be capital-indexed and linked to an eligible inflation index; (ii) have at least one year remaining to maturity at the Index rebalancing date; (iii) have a fixed, step-up or zero notional coupon; and (iv) settle on or before the Index rebalancing date.

DOW JONES EX-US SELECT REAL ESTATE SECURITIES INDEX

The Dow Jones Ex-US Select Real Estate Securities Index is a float-adjusted, market capitalization-weighted index that defines and measures the investable universe of publicly-traded, real estate securities in countries outside of the US.

DOW JONES-UBS COMMODITY INDEX

The Dow Jones-UBS Commodity Index aims to provide broadly diversified representation of commodity markets as an asset class. The index is made up of exchange-traded futures on physical commodities. The index represents 19 commodities, which are weighted to account for economic significance and market liquidity.

MSCI EAFE INDEX

The MSCI EAFE Index (Europe, Australasia, Far East) is a free float-adjusted market capitalization index that is designed to measure the equity market performance of developed markets, excluding the US & Canada. As of June 2007 the MSCI EAFE Index consisted of the following 21 developed market country indices: Australia, Austria, Belgium, Denmark, Finland, France, Germany, Greece, Hong Kong, Ireland, Italy, Japan, the Netherlands, New Zealand, Norway, Portugal, Singapore, Spain, Sweden, Switzerland, and the United Kingdom.

MSCI EMERGING MARKETS (EM) INDEX

MSCI Emerging Markets Index: An index created by Morgan Stanley Capital International (MSCI) that is designed to measure equity market performance in global emerging markets. The MSCI Emerging Markets Index is a float-adjusted market capitalization index.

S&P 500® INDEX

The S&P 500® Index is composed of five hundred (500) selected stocks, all of which are listed on the Exchange, the NYSE or NASDAQ®, and spans over 24 separate industry groups.

S&P MIDCAP 400 INDEX

The S&P MidCap 400 covers over 7% of the US equities market, and is part of a series of S&P US indices. Included in the index are companies with market cap in the range of US $1 billion to US $4.5 billion. This range is reviewed from time to time to ensure consistency with market conditions. The index also includes companies that should have four consecutive quarters of positive as-reported earnings, where as-reported earnings are defined as GAAP Net Income excluding discontinued operations and extraordinary items.

S&P SMALLCAP 600 INDEX

The S&P SmallCap 600 Index measures the performance of the small-capitalization sector in the US equity market. The selection universe for the Index includes all US common equities listed on the NYSE, NASDAQ Global Select Market, NASDAQ Select Market and NASDAQ Capital Market with market capitalizations between $250 million and $1.2 billion. The Index is float-adjusted and market capitalization weighted.

DOW JONES-UBS COMMODITY INDEX

The Dow Jones-UBS Commodity Index aims to provide broadly diversified representation of commodity markets as an asset class. The index is made up of exchange-traded futures on physical commodities.The Index represents 19 commodities, which are weighted to account for economic significance and market liquidity.

GOLD LONDON PM FIXING (SPOT PRICE)

The London fix is a method of determining the price of gold. It is carried out twice a day (10:30AM and 3:00PM, London time) by the 5 members via a dedicated conference call facility.

S&P EMERGING SMALL CAP INDEX

The S&P® Emerging Markets Under USD2 Billion Index is a float adjusted market cap weighted index that represents the small capitalization segment of emerging countries included in the S&P Global BMI Index. The Global BMI Index captures the full universe of institutionally investable stocks in developed and emerging markets with float-adjusted market capitalizations of at least $100 million.

S&P INTERNATIONAL SMALL CAP INDEX

The S&P® Developed Ex–U.S. Under USD2 Billion is a market capitalization weighted index that defines and measures the investable universe of publicly traded companies domiciled in developed countries outside the U.S. The Developed Small Cap Index is "float adjusted," meaning that only those shares publicly available to investors are included in the Developed Small Cap Index calculation.

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1 Bloomberg, SSgA Global ETF Strategy & Research, as of 6/30/2011.

2 FactSet, SSgA Global ETF Strategy & Research, as of 6/30/2011.

3 Standard & Poor's.

4 Zephyr StyleADVISOR, SSgA Global ETF Strategy & Research.

5 Zephyr StyleADVISOR, SSgA Global ETF Strategy & Research.

6 Cerulli Associates, eVestment Alliance.

7 S&P BMI Global Index, as of 6/30/2011.

8 Barclays Capital Global Aggregate Index.

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