

Eagle Star Investments

Weekly News

10th November 2008

Global Overview

Most equity markets end in the red

It was a mixed week on equity markets as the pre-election rally came to an abrupt end on Wednesday, as sentiment turned sour following disappointing economic data and weak corporate earnings in the US.

US economic data

There was further grim economic data in the US which shows the scale of what new President, Barack Obama, will inherit. Employment figures showed the steepest monthly drop in non-farm payrolls for over seven years, resulting in the unemployment rate hitting 6.5%. This came on the back of disappointing housing and service sector data.

Interest rate cuts

Following recent cuts in the US, Australia and Japan, to name but a few, the Bank of England and European Central Bank both continued the trend in an attempt to avoid a global recession by reducing key interest rates last week. The ECB reduced the rate by the expected 0.5%, to 3.25%. However, the BoE surprised markets by cutting its rate by a massive 1.5%, to 3%. This move by the BoE caused sterling to weaken significantly against most major currencies.

Further stimulus package

Over the weekend, finance ministers and central bank governors representing the G20 said they would take "all necessary measures" to get financial markets back to normal and counter the backlash of the credit crisis. This, along with China's unveiling of a nearly \$600bn economic stimulus plan to boost domestic demand, has resulted in a strong opening to the week for markets.

Commodities

Oil retreated last week, to finish at \$61 per barrel, as recessionary fears persist worldwide. Most of last week's falls were erased though, following the stimulus package announced by China, the largest contributor to last year's global economic growth.

Index	Year to Date Return 31.12.07 to 07.11.08		1 Week Return 31.10.08 to 07.11.08		
	Local Currency %	Euro %	Local Currency %	Euro %	
US	S&P 500	-36.6	-27.6	-3.9	-4.2
US	NASDAQ	-37.9	-29.0	-4.3	-4.5
Europe	FT/S&P Europe Ex. U.K.	-40.2	-40.2	-0.5	-0.5
Ireland	ISEQ	-59.2	-59.2	-6.7	-6.7
UK	FTSE 100	-32.4	-38.7	-0.3	-3.1
Japan	Topix	-40.4	-22.4	1.4	1.3
Hong Kong	Hang Seng	-48.8	-41.1	2.0	1.7
Australia	S&P/ASX 200	-36.1	-44.0	0.8	1.7
Bonds	Merrill Lynch Euro over 5 year Govt.	5.7	5.7	2.8	2.8

Global Equities



United States

Overview

On the week that the US voted in a new president, disappointing housing, jobs and corporate earnings caused further economic concern amongst investors, resulting in markets retreating over the week.

General Motors – One of the bellwether stocks in the US, General Motors, announced Q3 losses which were double what analysts had been expecting and said it faced a liquidity crunch, hitting sentiment towards the auto sector. GM finished the week almost 25% lower.

News Corp – The media group controlled by Rupert Murdoch saw shares sink by 20% over the week, following a profit warning from the group due to the worsening advertising market. Google has also been hit by a similar slowdown in online advertising.



Europe

Overview

Most markets finished the week slightly lower as the global sell-off of equities midweek negated the effect of the interest rate cut by the ECB. Investors took hope from the fact that the ECB is ready to move lower again, most likely in December.

ArcelorMittal – The world's largest steelmaker cut production, put growth plans on hold and warned of a fall in Q4 profits as the economic slowdown impacts on business. It finished the week over 14% lower. The announcement of the Chinese stimulus package, however, saw it recoup most of last week's losses in Monday's early trade.



Ireland

Overview

Banking stocks led the ISEQ lower last week. It finished almost 7% lower, bringing losses in 2008 to 60%.

Allied Irish Banks

AIB issued a profit warning last week after a sharp deterioration in the quality of its loan book over the past few months. The bank stated that it would target to increase its tier 1 capital ratio, to around 7%, over time and that it has several options available to increase its capital ratio, including asset sales.



Asia Pacific

Overview

Asian markets finished the week in positive territory despite the immediate fears of a global economic slowdown. Recent interest rate cuts across the region, along with the expectation of more to come, have boosted investor appetite for risk assets.

Bonds

Eurozone bonds gained strongly as eurozone interest rates were cut and Jean-Claude Trichet, President of the ECB, gave an indication the ECB would cut further, most likely in December. The Merrill Lynch over 5 year government bond index rose 2.8% on the week.

Global Outlook

- Policymakers have taken a series of measures to counter the incredible risks facing the global economy and to prevent a complete implosion of the global banking and economic system. It is now a given that US and European growth rates will be severely curtailed in the next year or so and that a global recession will have to be worked through. Policy action is intended to put a floor under economies and prevent a prolonged slump.
- Policymakers have committed to taking all measures necessary to kick-start the money markets - the lifeblood of the banking system and the real economy. While there have been some positive developments in that regard, there are abundant signs of how the banking crisis has rapidly spread into the real economy; a more rapid improvement in the money markets is vital if further deterioration in economic activity is to be forestalled.
- The shocking deterioration in economic indicators in the past two months means that further sharp falls in official short-term interest rates will be seen in a host of countries over the coming weeks and months. The ECB has practically pre-announced another cut for December, with investors seeing an additional 0.50% cut at that stage and more cuts in the new year. Similarly, UK rates will likely be reduced further to new multi-decade lows; markets see rates falling to 2% in coming months. Meanwhile in the US, even with rates now at 1%, investors expect an additional 0.25% reduction next month. With rates at these levels, the Fed is likely to be studying more unconventional interest rate policies - such as trying to actively lower longer-term interest rates.
- With some markets priced for the deepest slump since the Great Depression, government bonds have received strong safe haven flows. These may unwind periodically as governments step-up their borrowings substantially and if investors' fear of equities and corporate bonds recedes somewhat. Overall, however, bonds should be supported by central bank policies and large drops in inflation rates.
- The shattering loss of confidence in corporate bond markets is also manifest in equity markets, where investors have become almost inured to the huge volatility, the seemingly random price action and large price falls. Co-ordinated policy action is intended to arrest that fear and set the stage for the return of some confidence into the banking system, the real economy and equity markets. History suggests that powerful rallies can occur in the midst of severe bear markets such as we have experienced this year - especially when sentiment is totally shattered, as it had become in the past few weeks. The decisive US election result could be a positive for investor confidence and statements by the President-elect will be closely scrutinised for policy clues. However, it is the unfreezing of the money markets and the banking system that is seen by equity investors as the acid test of whether policy action is working or not. Expect volatility and uncertainty to persist until those markets begin to return to normality.
- Currently the funds are slightly overweight equities and slightly underweight in bonds, versus the manager average. Within equity sectors, the funds are overweight healthcare and underweight basic materials. Geographically, the funds have an underweight position in Ireland and Japan, are neutral in the Pacific Basin, and are overweight in the UK, US and Europe.

This outlook does not constitute an offer and should not be taken as a recommendation from Eagle Star/Zurich. Advice should always be sought from an appropriately qualified professional.