

Global Overview

Markets fall heavily

Equity markets worldwide finished the week sharply lower as China moved to remove some liquidity from its financial system, while investors also focussed on the potential effect of President Obama's proposals to reduce financial risk.

US financial proposal

Banking stocks had a tough week as Barack Obama asked Congress to approve his proposal to block banks from proprietary trading and sponsoring private equity & hedge funds.

Chinese bank reserves

With new loans continuing to exceed forecasts, the Chinese government moved to rein in lending and remove some liquidity from the system by increasing the bank reserve ratio. This requires Chinese banks to set aside more of their deposits, with the aim of cooling the expansion in the economy.

Dollar strengthens, gold & oil retreat

Tightened lending in China and investors' flight to the safety of the US dollar caused commodities to retreat sharply. The dollar index gained 1.2% against a basket of six major currencies, while the €/€ rate ended the week at just below 1.42. Gold and oil prices both declined as a result, as demand for commodities as an alternative investment was curbed. Oil finished over 4% lower at \$74.50 a barrel, while gold fell by 3%.

	Index	Year to Date Return 31.12.09 to 22.01.10		1 Week Return 15.01.10 to 22.01.10	
		Local Currency %	Euro %	Local Currency %	Euro %
US	S&P 500	-2.1	-0.9	-3.9	-2.4
US	NASDAQ	-2.8	-1.6	-3.6	-2.1
Europe	FT/S&P Europe Ex. U.K.	-2.2	-2.2	-2.9	-2.9
Ireland	ISEQ	2.1	2.1	-2.0	-2.0
UK	FTSE 100	-2.0	-0.9	-2.8	-1.9
Japan	Topix	3.7	8.6	-2.6	-0.2
Hong Kong	Hang Seng	-5.2	-4.3	-4.3	-2.9
Australia	S&P/ASX 200	-2.5	-0.5	-3.0	-3.4
Bonds	Merrill Lynch Euro over 5 year Govt.	0.0	0.0	0.7	0.7

Global Equities



United States

Overview

US markets erased 2010's gains after experiencing their biggest weekly drop since October. Markets were led lower by President Obama's proposal to limit financial risk and China's move to cool economic growth. On the upside, though, of the companies that have reported earnings so far, 79% have beaten analysts' estimates.

Alcoa – After declining by 8% the previous week, the aluminium producer fell by another 14% as investors fear that China's move to withdraw some liquidity from the financial system will cool economic growth and reduce the demand for commodities.

Kraft – Kraft Foods fell by almost 6% after Cadbury accepted its \$19.2bn takeover bid.



Europe

Overview

European stocks fell the most in three months as investors moved away from risk assets. Banking shares were the weakest sector, retreating by over 6%.

Cadbury – Shares in Cadbury rose by 5% after its board approved the takeover bid from Kraft Foods. This ends almost four months of negotiating and results in the creation of the world's largest confectioner.



Ireland

Overview

The Irish market finished the week 2% lower, led by financial and resource stocks.

Elan – The pharmaceutical company got a boost when the European Medicines Agency (EMA) reiterated that the benefits of the Tysabri drug continue to outweigh the risks. It did, however, recommend that a number of measures be put in place to ensure adequate monitoring and vigilance of patients with signs of the PML virus. Elan finished the week 4% higher.



Asia Pacific

Overview

Data released showed that Japanese demand for bank loans dropped the most in more than five years as companies cut spending. This has prompted the Bank of Japan to consider expanding an emergency-loan programme for banks. At the other end of the spectrum, China moved to try and cool the pace of economic growth by increasing its bank reserve ratio.

Bonds

Eurozone bonds overall failed to gain, despite investors' move towards safer assets. However, bonds issued by core countries performed well, whereas peripheral markets such as Greece and Portugal lost ground, as risk spreads widened. The Merrill Lynch over 5 year government bond index finished the week unchanged.

Global Outlook

- As we have been saying for some time, forecasters are positive for global growth during 2010. The key is whether the economies in Europe and the US are strong enough to stand on their own, and whether governments and central banks can withdraw some of the massive stimulus they have been providing. Note that while strains within the financial system have eased considerably, bank lending is still impaired. It is partly for this reason that policy makers remain somewhat cautious on the economic outlook and this remains a key variable to watch during the year.
- The long-term implications of the past two years and the unintended consequences of policy actions are still hot debates in the investment and political worlds. So far, risk assets have responded positively and that remains the immediate focus for most market participants.
- Short rates continue to hover in a range between 0% and 1% in the major economies. Investors keep getting nervous about rate expectations in the US and Europe only for policy makers to make soothing comments. At the same time, the latter want to exit from emergency policy settings as quickly as conditions permit, a tricky balancing act which continues to be difficult to communicate. It is notable that end-2010 rate expectations in the US, UK and eurozone reached new lows last week. On balance, therefore, investors expect that low rates will persist for some considerable time.
- For bond markets, inflation data is still generally supportive, as is the general liquidity backdrop that has helped other assets. As was the case for much of last year, the "elephant in the room" remains the exit from emergency policy settings - which is bound to have some impact on bond markets - and these concerns continue to keep bond markets in a broad trading range. We may be closer to the bottom of that range at the moment. In the eurozone, peripheral bond markets have been more volatile of late, with Greece making a new cyclical high in spread terms last week, but Irish bonds have behaved well in that context.
- Global equity markets remain on the richer side of the neutral valuation line. Markets began the year optimistically but have lost some of that in the past week or so. It is yet another test to see whether the "grinding higher and shallow retracement" pattern evident for the last few months will continue into 2010. Many argue that the structure of the rally has been less convincing than the pure market levels suggest and that significant risks remain. However, the overall positive trend, we think, is still intact.
- Currently, the funds are neutral to closer to neutral in equities and overweight bonds, versus the manager average. Within equity sectors, the funds have gone closer to neutral but are still overweight technology and basic materials and underweight utilities. Geographically, the funds have an underweight position in Ireland, are closer to neutral in the UK, US and Japan, and are overweight in Europe and the Pacific Basin.

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