Eagle Star Investments

Weekly News 23rd August 2010

ZURICH

Global Overview

Concern lingers

Most equity markets finished the week in negative territory after another batch of economic data caused investors to question the strength of the economic recovery. Stocks, commodities and high-yielding currencies all suffered as investors became more defensive.

ECB comments

Axel Weber, a council member of the European Central Bank, said that the bank should not withdraw stimulus measures until 2011, causing investors to fear that the eurozone's economy is going to struggle for the rest of the year.

US jobless claims

Initial jobless claims in the US unexpectedly rose by 12,000 last week, to hit 500,000. Elsewhere, the Federal Reserve of Philadelphia announced that its economic conditions index slipped into negative territory this month, pointing to a contraction of manufacturing in the region, suggesting corporate profit momentum will not be sustained.

Currencies

The euro tumbled to a five-week low against the dollar, partly due to Axel Weber's comments which reduced investor appetite for higher-yielding currencies. The €/$ rate ended the week at 1.27, a fall of 0.7%.

Oil

Oil prices fell by over 2% last week, to $73 a barrel, as the US economy continued to struggle, signalled by the jump in jobless claims. Further to this, there was downward pressure on the price of oil due to inventories reaching the highest level in 20 years.

	Index	Year to Date Return 31.12.09 to 20.08.10		1 Week Return 13.08.10 to 20.08.10	
		Local Currency %	Euro %	Local Currency %	Euro %
Global	FTSE World	-3.1	8.0	-0.7	-0.2
US	S&P 500	-3.9	8.4	-0.7	0.0
US	NASDAQ	-3.9	8.3	0.3	1.0
Europe	FT/S&P Europe Ex. U.K.	-3.5	-3.5	-1.4	-1.4
Ireland	ISEQ	-7.4	-7.4	-2.4	-2.4
UK	FTSE 100	-4.0	4.1	-1.5	-1.3
Japan	Topix	-8.6	12.1	-0.2	1.1
Hong Kong	Hang Seng	-4.1	7.9	-0.4	0.2
Australia	S&P/ASX 200	-9.0	1.7	-0.6	-0.7
Bonds	Merrill Lynch Euro over 5 year Govt.	7.9	7.9	1.5	1.5

Global Equities

United States

Overview

US stock markets fell heavily after jobless claims data disappointed investors, causing US markets to finish the week overall relatively flat. The week ahead contains many important economic releases, including new homes sales and Q2 GDP revisions.

Merger & acquisition activity – It was a busy week of M&A activity. McAfee, the maker of security software, saw its shares surge almost 60% following Intel's agreement to buy the company for $48 a share. Intel is proposing an all-cash deal. Also, Potash announced that it rejected a $39bn bid from BHP Billiton. BHP Billiton subsequently went hostile with its bid. Potash was up 34% on the week, well above the bid price.

Europe

Overview

European markets had their biggest drop in seven weeks amid investor concern that economic growth will struggle. Axel Weber's comments added to this concern.

BG Group – The natural gas producer saw shares rise by over 6% as speculation mounted that it may be a takeover target.

Holcim – The cement company announced results that missed expectations, while also deciding not to give guidance on sales or earnings for the remainder of 2010, causing its shares to drop by 5%. These news also dragged construction industry-related stocks lower on the week.

Ireland

Overview

The Irish market fell by over 2% on the week, with CRH, Elan and financials leading the way lower.

CRH – Ahead of its interim results this week, shares in the company lost 6% over the week due to the number of highway contracts awarded in the US falling during July, compared with the previous year, and Holcim's disappointing results, which weighed on the sector.

Asia Pacific

Overview

Markets in the Far East were marginally down due to the weak economic data worldwide. This "loss of momentum" in the global recovery was behind JP Morgan's decision to trim China's growth forecasts for this year and 2011. Also during the week, China's economy surpassed Japan's as the world's second-largest during last quarter. Taiwan's market performed better as GDP was stronger-than-expected due to domestic demand strength.

Bonds

Eurozone bonds surged as investors looked for the relative safety of defensive assets. Axel Weber's comments, which raised expectations that the ECB will continue to support the economy through to the end of the year, along with weak economic releases, contributed to German bond prices hitting record highs. The Merrill Lynch over 5 year government bond index rose by 1.7% over the week.

Global Outlook

- Global growth forecasts are healthy enough for this year and next (3.6% and 3.3%). However, weak bank lending and financial market volatility add to downside risks to both forecasts, and we have begun to see some forecasts being pared back for the US. Inflation pressures globally remain modest, reflecting weaker data in developed economies and stronger readings in emerging economies and Asia. Indeed, further disinflation is a greater near-term concern than inflation. Exports are very strong from some European economies but domestic demand remains subdued and the global economy is still very lopsided. The key concern is whether the private sector in Europe and the US can grow without continued government support.

- Central banks continue to set interest rates at emergency levels in Europe and the US, although they have risen somewhat in some of the stronger economies such as Canada, India and China. By extension, 2011 rate expectations have reached new cycle lows in the US, UK and eurozone, in many ways an extraordinary situation which is at odds with the expectations for recovery.

- These low short-term interest rates, combined with disinflation concerns, continue to support the major bond markets such as Germany, the US and Japan, with long-term interest rates falling to levels that will unnerve many risk investors and policymakers. Bond prices in these markets have risen so quickly that some levelling out or pullback could easily occur in the short-term. Peripheral bond spreads in the eurozone have widened again of late, with Irish yield spreads over Germany trading back over 3%, a new cyclical wide. Some of this is due to illiquid trading conditions, with a sense that Ireland's fiscal measures have been swamped by its banking woes. It is quite possible that the rescue mechanism in place for eurozone countries will be further tested in the months ahead.

- Global equities are only modestly lower this year but this masks very large gyrations: we have had four 7%+ falls, one 9% and one 14% rally. One impact of this is that investors' convictions are very low and holding periods very short. Low interest rates certainly provide some forward support to risk markets and investors seem to believe that the Fed will ride to the rescue with further quantitative easing policy ("QE2"). Sentiment and market action have turned mixed again and bond market developments are a concern for equity markets, as they suggest that the macro environment is deteriorating and caution is warranted still.

- Currently, the funds remain underweight equities and overweight bonds versus the manager average. Within equity sectors, the funds are now reasonably balanced. Geographically, the funds are underweight in Ireland, Europe, the UK and the US, and are neutral in Japan and the Pacific Basin.

Print Ref: CSA63

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