# Eagle Star Investments

## Weekly News 7th December 2009

# Global Overview

### Equities rebound after Dubai concerns

Equity markets worldwide gained strongly as investors speculated that the panic that surrounded the potential impact of Dubai's debt problems was probably overdone. Instead, investors focussed on the improving economic data worldwide, most notably in the US and China.

### European Central Bank

The ECB left rates unchanged, at 1%, when it met during the week, but announced plans to start withdrawing stimulus measures earlier than most anticipated. This is being signalled as the start of a tightening process in order to avoid any asset-price bubbles stoking inflation.

### US unemployment

The US unemployment rate for November unexpectedly improved to 10%, from 10.2% the previous month. Payrolls fell by 11k over the month, significantly better than the 125k economists had anticipated.

### Chinese data

One of the first lead indicators to improve early this year was Chinese manufacturing data. This improvement has continued since then, and last week saw the index show that manufacturing activity is now growing at the fastest pace in five years.

### Currencies

The dollar rallied against the euro on Friday following the improvement in the unemployment rate and economic data. Having hit almost 1.51 during the week, the €/$ finished just below 1.49.

### Oil & gold

Oil prices declined by 1% last week, but the main story centred on gold. With a strengthening dollar, investors moved away from gold, resulting in a fall of over 4% in its price. This was the biggest one-day fall of a traded commodity in over a year. However, it was still up 2.4% for the week.

| | Index | Year to Date Return 31.12.08 to 04.12.09 | | 1 Week Return 27.11.09 to 04.12.09 | |
|---|---|---|---|---|---|
| | | Local Currency % | Euro % | Local Currency % | Euro % |
| US | S&P 500 | 22.4 | 14.7 | 1.3 | 1.8 |
| US | NASDAQ | 39.1 | 30.4 | 2.6 | 3.1 |
| Europe | FT/S&P Europe Ex. U.K. | 23.8 | 23.8 | 2.8 | 2.8 |
| Ireland | ISEQ | 27.5 | 27.5 | 5.0 | 5.0 |
| UK | FTSE 100 | 20.0 | 27.3 | 1.5 | 2.0 |
| Japan | Topix | 3.5 | -2.2 | 9.7 | 6.2 |
| Hong Kong | Hang Seng | 56.4 | 46.6 | 6.5 | 7.0 |
| Australia | S&P/ASX 200 | 26.3 | 53.8 | 2.8 | 4.4 |
| Bonds | Merrill Lynch Euro over 5 year Govt. | 5.0 | 5.0 | 0.0 | 0.0 |

# Global Equities

## United States

### Overview

US markets gained last week, with some hitting an intra-day high for the year on Friday, as sentiment towards equities improved. The big gains were prompted by the improving unemployment rate and rise in factory order data.

**Bank of America –** BoA rebounded from the previous week's fall, after it raised $19.3bn selling securities in order to help repay the government bailout funds it had received from the Troubled Asset Relief Program. It finished the week over 5% higher.

## Europe

### Overview

European stocks gained for the first time in two weeks. This followed the ECB's upward revision of 2010 and 2011 GDP, while elsewhere, the manufacturing data in China and unemployment data in the US also supported gains.

**Adecco –** The personnel and temporary employment company gained almost 12% over the week. The majority of the move followed the better-than-expected payroll data in the US.

## Ireland

### Overview

The Irish market gained 5% over the week, as CRH performed strongly (+7%). AIB and Bank of Ireland fell slightly, late in the week, as investors await this week's budget before deciding the outlook for the banks.

**Ryanair –** The low-cost airline jumped almost 5% after it announced an increase in the numbers it carried over the past month. Spain's Iberia Airlines and Britain's British Airways also gained as the outlook for both rose.

## Asia Pacific

### Overview

Asian markets were the best performing markets last week, as most recovered strongly from the previous week's concerns surrounding Dubai. Japan's Topix surged 9.7%, which is its biggest monthly gain since August 1992. The Bank of Japan increased fund injections into the money market and boosted its purchase of government bonds. The Japanese government last month said that Japan's economy is suffering from deflation.

# Bonds

Eurozone bonds remained broadly unchanged on a week that the ECB signalled its plans to start withdrawing stimulus measures. This is seen as being the start of monetary tightening over the coming year. The better-than-expected US employment data caused bonds to end the week on a weak note, as global growth prospects improve. The Merrill Lynch over 5 year government bond index is still up 5% this year.

# Global Outlook

- Forecasters expect the global economy to return to positive growth next year following a further contraction of 1% this year. Inevitably, unemployment will lag any recovery in the economy, meaning that economic conditions will continue to "feel" weaker than the statistics suggest. Strains within the financial system have eased considerably but bank lending is still impaired. Partly for this reason, policymakers remain somewhat cautious on the economic outlook. Trade tensions are not yet a major issue but bear watching for any economic or market impact.
- Much of the economic improvement is attributed to the scale and scope of policy initiatives to rescue the banking system and offset the collapse in private sector demand. As we have said before, the ultimate success of these initiatives (or what unintended consequences may arise) remains an open question.
- Short rates continue to hover in a range between 0% and 1% in the major economies, presenting central banks with a tough challenge. They want to keep rates sufficiently low to foster recovery but also want to exit from emergency policy settings as quickly as conditions permit. Recent rate increases in economies like Australia have made investors slightly more nervous, although it's notable that future rate expectations in the US and eurozone are less than 0.25% above their lows. On balance, therefore, investors expect that low rates will persist for some considerable time, notwithstanding that central banks will continue to speak about their exit strategies.
- For bond markets, inflation data is still generally supportive, as is the general liquidity backdrop that has helped other assets. However, 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 have kept bond markets in a trading range, in the past few months. In the eurozone, peripheral bond markets have been slightly more volatile of late as investors become more sensitive to the fiscal positions of individual countries, such as Ireland and Greece.
- In terms of valuations, global equity markets remain rich rather than cheap. To date, markets have been able to grind out recoveries from any dips, with sentiment remaining positive on balance, which is still probably the case today. The structure of the rally remains less convincing at this stage, as volume remains light and momentum indicators diverge. The reaction to last weeks US payroll news is another indication of that pattern.
- Currently, the funds are closer to neutral equities and overweight bonds, versus the manager average. Within equity sectors, the funds are overweight technology and underweight utilities. Geographically, the funds have an underweight position in Ireland and Japan, are closer to neutral in the UK, the US and Europe and are overweight in the Pacific Basin.



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**Zurich Life Assurance plc**
Eagle Star House, Frascati Road, Blackrock, Co. Dublin, Ireland.
Telephone: 01 283 1301 Fax: 01 283 1578 Website: www.zurichlife.ie


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