Eagle Star Investments

Weekly News 15th June 2009

Global Overview

Equity markets continue to make gains

Most equity markets traded in a tight range for the week, but still managed to record modest gains. This followed further signs that the recession is easing, most notably the strong Chinese industrial output data and news that the US banks are to begin paying back the bail-out funds.

US economic data

Investors got a boost from further upbeat economic data, as jobless claims, retail sales and consumer sentiment all showed continued signs of improvement. On top of these, a robust sale of 30-year Treasury bonds helped sentiment in the US equity markets, after it attracted solid demand, despite a weak 10-year bond sale on Wednesday.

Chinese economy improves sentiment worldwide

Further signs of a recovery in economic growth came from a Chinese government report showing China's retail sales jumped over 15% in May, the most in four months. Investments in factories, property and roads also surged by a better-than-estimated 33% in the first five months of 2009, compared with a year earlier.

Currencies & Commodities

In currency markets, the €/$ rate finished the week unchanged at 1.40, as gains experienced early in the week were erased. On commodity markets, the oil price advanced further after data from both the US and Europe showed a drop in stockpiles and output respectively. The oil price finished the week up, at just over $72 a barrel.

	Index	Year to Date Return 31.12.08 to 12.06.09		1 Week Return 05.06.09 to 12.06.09	
		Local Currency %	Euro %	Local Currency %	Euro %
US	S&P 500	4.8	4.2	0.7	0.6
US	NASDAQ	17.9	17.3	0.5	0.5
Europe	FT/S&P Europe Ex. U.K.	5.5	5.5	1.0	1.0
Ireland	ISEQ	26.8	26.8	1.3	1.3
UK	FTSE 100	0.2	12.7	0.1	2.9
Japan	Topix	10.6	1.7	3.7	3.6
Hong Kong	Hang Seng	31.3	30.7	1.1	1.1
Australia	S&P/ASX 200	9.1	25.2	2.3	3.6
Bonds	Merrill Lynch Euro over 5 year Govt.	-1.8	-1.8	0.7	0.7

Global Equities

United States

Overview

US equity markets added to their 2009 gains, as economic data once again surprised to the up-side, giving further indications of stabilisation.

Bank of America – Shares in Bank of America rallied by over 16%, after stockbrokers raised their price targets for the company, based on expectations that the bank will have paid back all of its TARP loan by early 2010. Most financial stocks saw shares rise over the week for the same reason.

BlackRock – Investment management company, BlackRock, became the world's biggest asset manager after Barclays confirmed it would sell its Global Investors division to it for $13.5bn.

Europe

Overview

European markets rose to seven-month highs following improving US retail sales and Chinese investment, as both signalled the worst may now be over.

Healthcare stocks – GlaxoSmithKline and Sanofi Aventis, who are both developing swine flu vaccines, saw their shares jump following the WHO's move to raise the alert for swine flu to the top of the agency's six-stage pandemic scale. Shares rose by 8% and 3% respectively.

Ireland

Overview

The Irish market finished the week marginally higher, despite names like Aer Lingus, Ryanair and C&C bucking the trend.

Aer Lingus – The airline confirmed the extremely difficult market conditions it faces, particularly for Winter, after it announced a reduction in its Winter seat capacity on the long-haul network, by 25% for this year. Its shares fell by 10% on the week.

Asia Pacific

Overview

Asian markets gained strongly, following rising Chinese investment and retail sales and an improvement in Australian consumer sentiment.

China's investment – China's central bank said new lending doubled to 664bn yuan in May, from 318.5bn yuan a year earlier, adding to a credit boom that is supporting the government's 4 trillion yuan stimulus plan. The Industrial Commercial Bank of China, the world's largest by market value, China Construction Bank and Bank of China all saw their shares rise over the week.

Bonds

Bonds gained over the week, following the successful 30-year bond auction in the US and the biggest fall in German wholesale prices in 22 years, signalling that inflationary impulses remain very weak. The Merrill Lynch over 5 year government bond index rose by 0.7%.

Global Outlook

- The general feeling amongst investors is that economic data has stabilised after being in freefall earlier this year. The hope is that an inventory rebound will help growth in the short term, and that policy action will put a more lasting floor under activity in the medium term. Signs of less stress in the financial system have bolstered these hopes. However, a lot of the 'green shoots' sentiment has its origin in China and Asia. This is a concern, given that the region is export-oriented and highly dependent on the US consumer.
- The scale and scope of policy initiatives to save the banking system and offset the collapse in private sector demand have been unprecedented. The ultimate success of these efforts – or their unintended consequences – is still far from certain, however, given the depth of the crisis faced by the global economic system.
- Short rates have likely reached their cyclical lows in the major economies – at somewhere between 0% and 1% – and the question is how short rates can be maintained at these levels. The success of the quantitative easing (QE) programs around the globe has been mixed. The way in which US mortgage rates have been "allowed" to rise in recent weeks is a concern. In any event, the major central banks are already talking about exit strategies from these initiatives.
- Bonds performed quite badly, while investors re-embraced risk assets and authorities disappointed with their QE policies; many commentators have also speculated on the long-term inflation risks from the current policy mix. Peripheral bond markets, such as Spain and Ireland, have been helped by "solidarity" expressions from the EU and ECB and a more positive attitude towards risk assets. Periodic concerns about the budgetary positions could easily impact on these spreads again, although it seems that the political commitment to containing this issue has strengthened in recent weeks. At least in the short term, bond markets in general have probably reached support levels and a more constructive period may lie ahead.
- Economic green shoots, oversold markets, large short positions and pessimistic sentiment combined to produce a powerful bear market rally in equity markets over the past three months. The stress test of the US banks was choreographed very well, and corporate debt markets have also been more supportive. While the general feeling in the equity markets is that we get a period of consolidation followed by further gains, at this stage the burden of proof may be moving more towards the bulls; there could easily be some disappointment with policy initiatives or the pace of improvement in real economic data.
- Currently, the funds are close to neutral in equities and overweight bonds, versus the manager average. Within equity sectors, the funds are overweight technology & financials and underweight healthcare & utilities. Geographically, the funds have an underweight position in Ireland and the US, are closer to neutral in Japan, the UK and Europe, and are overweight in the Pacific Basin.

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