# Eagle Star Investments

## Weekly News 14th December 2009

ZURICH

# Global Overview

### Equities retreat

Most equity markets finished the week slightly lower, but losses had been pared late in the week however, after encouraging economic data from China and the US. Worries over debt concerns in Greece and Dubai caused nervousness amongst investors.

### Dubai

Abu Dhabi provided $10bn to help Dubai World, the state-owned company, meet its debt obligations. This included $4.1bn needed to repay an Islamic bond maturing for a real-estate unit.

### US data

Data for November confirmed the improved economic conditions in the US. Retail sales rose by 1.3%, while consumer sentiment rebounded from a three-month decline. Both of these well exceeded analysts' expectations.

### Chinese data

China's growth was further demonstrated last week after the releasing of data showing its industrial output surged 19%, from last year's levels, in November. Having fallen for a number of days, copper prices recovered some of their losses following this.

### Currencies

The dollar's rally against the euro continued last week on the back of positive retail and consumer data. Over the week, the dollar strengthened by 1.8% to finish at a two-month high against the euro. The €/$ rate currently sits at 1.46.

### Oil

Oil declined last week, extending its losses to eight straight days, as the dollar gained strongly against the euro, curbing investor demand for commodities. It finished the week just below €70 a barrel, a decline of 7% for the week.

| | Index | Year to Date Return 31.12.08 to 11.12.09 | | 1 Week Return 04.12.09 to 11.12.09 | |
|---|---|---|---|---|---|
| | | Local Currency % | Euro % | Local Currency % | Euro % |
| US | S&P 500 | 22.5 | 16.9 | 0.0 | 1.8 |
| US | NASDAQ | 38.9 | 32.5 | -0.2 | 1.6 |
| Europe | FT/S&P Europe Ex. U.K. | 21.7 | 21.7 | -1.8 | -1.8 |
| Ireland | ISEQ | 24.9 | 24.9 | -2.0 | -2.0 |
| UK | FTSE 100 | 18.7 | 26.1 | -1.1 | -0.9 |
| Japan | Topix | 3.4 | 0.3 | -0.1 | 2.6 |
| Hong Kong | Hang Seng | 52.2 | 45.3 | -2.6 | -0.9 |
| Australia | S&P/ASX 200 | 24.5 | 53.8 | -1.4 | 0.0 |
| Bonds | Merrill Lynch Euro over 5 year Govt. | 4.8 | 4.8 | -0.2 | -0.2 |

# Global Equities

## United States

### Overview

Encouraging data on the economy and improved sentiment towards the dollar helped US markets recover early week losses and finish the week relatively unchanged. However, there was caution after the President of the Federal Reserve, Ben Bernanke, warned the economy faces 'significant headwinds'.

**Airlines –** A reduction in the price of oil and some optimism about travel demand pushed the Amex Airline Index to its highest level since February. Delta led the way with a 13% increase, while US Airways rose 9%.

## Europe

### Overview

European stocks declined last week as Fitch Ratings downgraded Greece's sovereign debt rating, along with five of the nation's lenders. Elsewhere S&P Ratings Services cut their outlook for Spain.

**Banks –** The banking sector was the worst performing sector last week, when it finished the week 4.4% lower. National Bank of Greece plunged 20%, while Banco Santander fell almost by 7% on fears that increasing funding costs for their respective countries could lead to weaker economic growth from fiscal austerity.

## Ireland

### Overview

The Irish market finished the week almost 2% lower, dragged down by further weakness in the banking sector.

**Banking sector –** The three main banks came under pressure last week due to uncertainty surrounding the discounts being applied to loans transferred to NAMA. This, along with weakness in banks worldwide following the downgrading of Greece's rating due to national debt concerns, caused heavy falls in AIB (-16%), Irish Life & Permanent (-14%) and Bank of Ireland (-13%).

## Asia Pacific

### Overview

Asian stocks retreated last week as banks were hit hard following the weaker-than-expected GDP data from Japan and the uncertainty which is still surrounding Dubai's debt restructuring. Economic data out of China on Friday continued to indicate growth intact, with industrial production ahead of analysts' estimates giving Asian markets an end of week boost. Technology stocks bucked the trend though, as investors speculated that the improving conditions in the US will bolster demand for the sector.

# Bonds

Bonds retreated slightly over the week following Germany's announcement that it plans to sell a record amount of bonds next year, as the government faces its bleakest budget since World War II. This, along with better-than-expected US 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 fell by 0.2% on the week.

# Global Outlook

- Forecasters expect the global economy to return to positive growth next year following a further contraction of 1% this year. It is inevitable that 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. It is partly for this reason that 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. Central banks want to keep rates sufficiently low to foster recovery but also want to exit from emergency policy settings as quickly as conditions permit; a tricky balancing act which causes difficulties in communicating with investors. While recent rate increases in economies like Australia have made investors slightly more nervous, it is 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.
- 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 the case today. However for some time now, the structure of the rally has been less convincing than the pure market levels suggest, with volumes lighter and momentum indicators diverging somewhat.
- Currently, the funds are closer to neutral in 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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