Eagle Star Investments

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ZURICH

Global Overview

Equities rally

Equity markets rose most days last week helping indices worldwide record gains for the week. This rally was mainly stoked by upbeat central bank comments and economic reports.

ECB meeting

The ECB held interest rates at the current low of 1% at its regular meeting last week. It also revised upwards its forecast of economic growth for the region. It expects the region to grow at a rate of between 1.4% and 1.7% for 2010, compared with the previous estimate of 0.7% to 1.3%.

US economic data

Investors got some much-needed economic data to cheer last week after the release of better-than-expected job and manufacturing data reports in the US. Private payrolls grew by 67,000 in August and were revised upwards to 110,000 for July. A separate report showed the service industry expanded in August, after contracting for the previous three months.

Irish credit-spreads

With the uncertainty surrounding the ever-escalating cost of the Anglo Irish Bank bail-out, the spread between Irish and German bonds widened slightly to 3.39% during the week. This happened despite the spreads of most peripheral eurozone bonds narrowing over the week.

Currencies

The euro gained against the dollar as investors looked to higher-yielding currencies following the improved global outlook. The €/$ rate ended the week at 1.29, a rise of 1%. Elsewhere, the Australian dollar rose by 2% versus the dollar for similar reasons.

Oil

Despite an improved outlook on the jobs front, the relatively weak expansion of the service industry caused investors to speculate that the US recovery will be slow and remain weak for some time. Oil prices finished the week slightly above $75 a barrel.

	Index	Year to Date Return 31.12.09 to 03.09.10		1 Week Return 27.08.10 to 03.09.10	
		Local Currency %	Euro %	Local Currency %	Euro %
Global	FTSE World	-1.4	9.2	2.4	1.9
US	S&P 500	-1.1	10.3	3.6	2.7
US	NASDAQ	-1.7	9.5	3.6	2.7
Europe	FT/S&P Europe Ex. U.K.	-0.8	-0.8	3.2	3.2
Ireland	ISEQ	-5.9	-5.9	4.9	4.9
UK	FTSE 100	0.5	7.0	4.5	3.1
Japan	Topix	-9.2	10.9	0.5	0.0
Hong Kong	Hang Seng	-4.1	6.6	1.8	1.0
Australia	S&P/ASX 200	-6.8	6.1	3.9	5.3
Bonds	Merrill Lynch Euro over 5 year Govt.	7.4	7.4	-1.1	-1.1

Global Equities

United States

Overview

US stock markets rebounded for a strong gain over the week, as fears of a double-dip in the economic recovery eased following upbeat economic data and comments from the Federal Reserve that the economy is on a "gradual recovery track".

3Par – The 18-day bidding war between Dell and HP for the virtual storage company, 3Par, ended last week when HP agreed to pay $33 a share. It is now thought that Dell will focus on another company to try to compete further with EMC and IBM. Dell is entitled to receive a break-up fee of $72m from 3Par, as the companies had agreed on a price prior to HP entering the frame.

Europe

Overview

Almost every European markets finished the week higher, as comments from the ECB and economic data in most regions gave investors a boost.

Basic Resources – The sector, which includes iron-ore and coal, was the best performer over the week, rising by almost 7% on upbeat global data. Rio Tinto and Xstrata were two of the biggest gainers.

Ireland

Overview

The Irish market rose by 5% on the week, led by financials and a recovery in CRH's value.

Allied Irish Banks – The bank rallied almost 5% on the week amid reports that it is holding final talks with potential buyers of it stake in Polish bank Zachodni WBK. This is part of its plans to raise €7.4bn in additional capital requested by the Financial Regulator.

Asia Pacific

Overview

Asian markets jumped during the week as investor's sentiment improved after the Japanese government confirmed it was ready to act to rein in the strong yen, and a report that showed China's purchasing managers' index rose, at an expectation-beating rate. The Government's comments helped export-reliant companies, including Canon and Nissan, rally. Australia's market gained momentum as GDP surpassed estimates, driven by the private sector.

Bonds

After three straight weeks of gains, eurozone bonds fell as investors sought to buy risk assets. This followed the upward revision of economic growth for the region, along with the improving data from the US and China. The Merrill Lynch over 5 year government bond index fell by 1.1% 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 there have been some concerns over a double-dip in the US economy. 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 3.5%, 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. Related to this is that investors' convictions are very low and holding periods very short. Low interest rates certainly provide some forward support to risk markets. Additionally, investors seem to believe that the Fed will ride to the rescue with further quantitative easing policy ("QE2"), although the Fed's recent comments don't suggest anything new is imminent. 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; caution is probably warranted still.
- Currently, the funds are neutral equities and slightly overweight bonds versus the manager average. Within equity sectors, the funds are now reasonably balanced. Geographically, the funds are underweight in Ireland and the UK, overweight Europe and closer to neutral in other markets.

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