

# Eagle Star Investments

## Weekly News

28th October 2008

### Global Overview

#### Most equity markets finish lower

Recessionary fears returned to equity markets following the release of poor economic data, overshadowing the previous week's positive performance.

#### US economic data

New jobless claim figures reported an increase in the number of individuals filing for unemployment insurance, confirming further deterioration in the labour market. The Chicago Fed National Activity Index in September fell to its lowest level since 1982, mostly driven by the steep drop in industrial production.

#### UK economic data

Minutes from the Bank of England's October 8th meeting reflected that all nine committee members voted for this month's globally co-ordinated 50bps emergency cut in interest rates. Official figures showed that the economy contracted by more than expected between July and September, leading to fears that a recession will be deeper than previously expected. This release confirmed earlier warnings from Bank of England Governor, Mervyn King, that Britain is entering a recession.

#### Commodities

Several commodities suffered steep declines amid worries that a recession will result in a fall in demand. Despite OPEC's decision to cut oil production by 4.5%, crude oil fell to below \$63 a barrel, the lowest level in 16 months. Gold dipped below \$700 an ounce during the week, whilst copper fell to below \$4,000 a tonne for the first time in nearly three years. Elsewhere, the dollar continued to strengthen, €/£ ending the week at 1.27, whilst £/\$ touched a six-year low at 1.527 as news filtered through that the UK economy had contracted in the third quarter.

Index		Year to Date Return 31.12.07 to 24.10.08		1 Week Return 17.10.08 to 24.10.08	
		Local Currency %	Euro %	Local Currency %	Euro %
US	S&P 500	-40.3	-31.3	-6.8	-1.1
US	NASDAQ	-41.5	-32.7	-9.3	-3.8
Europe	FT/S&P Europe Ex. U.K.	-45.5	-45.5	-7.1	-7.1
Ireland	ISEQ	-61.8	-61.8	-2.6	-2.6
UK	FTSE 100	-39.9	-44.7	-4.4	-7.1
Japan	Topix	-45.4	-25.5	-9.9	3.0
Hong Kong	Hang Seng	-54.6	-47.5	-13.3	-8.0
Australia	S&P/ASX 200	-39.0	-49.9	-2.6	-6.9
Bonds	Merrill Lynch Euro over 5 year Govt.	5.5	5.5	1.8	1.8

### Global Equities



#### United States

##### Overview

Concerns over deteriorating economic data and gloomy earnings results led US markets lower.

**Chrysler** – The Detroit-based car manufacturer revealed last week that it is cutting 25% of its white-collar workforce at the plant, equal to almost 5,000 jobs. The company cited the sharp contraction in sales as the underlying factor.



## Europe

### Overview

Amid financial uncertainty worldwide, European equity markets finished the week sharply lower.

**Royal Bank of Scotland** – Analysts are expecting that RBS may have to make further write-downs of between £4-5 billion Stg in the second half of 2008. The write-downs are likely to be focused on its structured credit portfolio, where values of securities within US sub-prime assets have fallen further in value.

**Auto Manufacturers** – Europe's largest car manufacturer, Volkswagen, has confirmed that it plans to cut the number of contract workers in its German factories by about 20% by the end of the year. Elsewhere, Peugeot Citroen announced last week that it is planning large production cuts of at least 20%, in response to tumbling sales figures. The company has also slashed its 2008 operating margin forecasts from 3.5% to 1.3%. Meanwhile, orders at Volvo, the world's largest truck-maker, have fallen by 55% for the third quarter with European truck orders close to zero due to order cancellations.



## Ireland

### Overview

It was another volatile week on the ISEQ as banking stocks in particular continued to suffer steep declines, and the index ended the week over 2% lower.

**Banking stocks** – Irish Life & Permanent and Bank of Ireland experienced the largest declines, falling by almost 38% and 17% respectively. However, AIB bucked the trend, gaining just over 1%.



## Asia Pacific

### Overview

Asian stocks finished the week mostly in negative territory as fears of a global recession persist. The turmoil experienced in the US was echoed across Asian markets and the Nikkei ended the week at a five-and-a-half year low as export stocks were hurt by the strength of the yen. The yen hit a 13-year high against the dollar and British pound and jumped to a six-year peak against the euro, as investors abandoned riskier positions. In Hong Kong, the Hang Seng Index shed over 13%.

**Samsung Electronics** – The world's largest chipmaker reported its biggest fall in third-quarter profits in more than three years as oversupply led to a reduction in the price of computer chips and flat panel displays. The South Korean company's net profit plunged 44% to \$856m.

## Bonds

Bond prices soared over the week as investors, becoming more risk averse, flocked to the safety of government bonds. The Merrill Lynch >5 year government bond index rose 1.8% on the week.

## Global Outlook

- Policymakers have begun to grasp the incredible risks facing the global economy and have taken a series of measures aimed at preventing a complete implosion of the global banking and economic system. It's now a given that US and European growth rates will be severely curtailed in the next year or so and that a global recession will have to be worked through. Policy action is intended to put a floor under economies and prevent a prolonged slump.
- Policymakers have committed to taking all measures necessary to kick-start the money markets - the lifeblood of the banking system and the real economy. Progress in that regard remains very slow, however, and there are very worrying real economy impacts being notified even now. In the next few weeks and months there will be further sharp falls in official short-term interest rates. A further reduction of at least 0.75% is seen from ECB by the end of the year, with an unquantified cut already pre-announced for early November. US rates are seen falling by 0.5% to 1% tomorrow (Wednesday 29th) and UK rates by at least that amount next week.
- With some markets priced for the deepest slump since the Great Depression, government bonds have received strong safe-haven flows. These may unwind somewhat over the next while as governments step-up their borrowings substantially and if investors' fear of equities and corporate bonds recedes somewhat. Overall however, bonds should be supported by falling short rates and large drops in inflation rates.
- The shattering loss of confidence in corporate bond markets is also manifest in equity markets, where investors are almost inured to the huge volatility, the seemingly random price action and continuing large price falls. Co-ordinated policy action is intended to arrest that fear and set the stage for the return of some semblance of confidence into the banking system, the real economy and equity markets. While history suggests that powerful rallies can occur in the midst of severe bear markets such as we are experiencing now, this notion still appears a distant possibility; sentiment is totally shattered. The unfreezing of the money markets and the banking system is seen by equity investors as the acid test of whether policy action is working or not. Huge uncertainty will persist until those markets begin to return to normality.
- At this stage the funds are currently close to neutral in equities and bonds, versus the manager average. Within equity sectors, the funds are overweight healthcare and underweight basic materials and financials. Geographically, the funds have an underweight position in Ireland, Japan and the Pacific Basin, are neutral in the UK, and are overweight in the US and Europe.

This outlook does not constitute an offer and should not be taken as a recommendation from Eagle Star/Zurich. Advice should always be sought from an appropriately qualified professional.

