Eagle Star Investments
Weekly News
19th January 2009

Global Overview

Equity markets trade lower
Equity markets traded lower over the week as sentiment turned sour following disappointing economic data and weak corporate earnings.

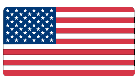
US economic data
US retail sales plunged by 2.7% in December from November, as consumers cut back on spending over the holiday period. Elsewhere, news that US initial claims continue to increase, reinforced recent dire economic releases.

European data
The European Central Bank cut interest rates by 0.5% to 2%, taking it to the lowest level in three years. ECB President Jean-Claude Trichet warned that the eurozone recession could deepen further and the growth forecasts that it published only last month will have to be revised downwards. Elsewhere, growth in the German economy slowed to 1.3% in 2008, the slowest since 2005.

Commodities
Oil prices led the retreat across commodity markets as a rise in weekly crude and refined product inventories heightened fears of a prolonged recession. The oil price finished the week at just under $35 per barrel. The euro dropped to a five-week low against the dollar as fears grew over the health of weaker economies on the periphery of the eurozone, such as Greece who had their sovereign debt rating downgraded by rating agency Standard & Poor's. The €/$ rate finished the week trading at 1.32.

Index		Year to Date Return 31.12.08 to 16.01.09		1 Week Return 09.01.09 to 16.01.09	
		Local Currency %	Euro %	Local Currency %	Euro %
US	S&P 500	-5.9	-0.8	-4.5	-2.8
US	NASDAQ	-3.0	2.2	-2.7	-0.9
Europe	FT/S&P Europe Ex. U.K.	-4.9	-4.9	-7.3	-7.3
Ireland	ISEQ	4.8	4.8	-8.6	-8.6
UK	FTSE 100	-6.5	-0.8	-6.8	-8.2
Japan	Topix	-4.8	0.8	-4.3	-2.8
Hong Kong	Hang Seng	-7.9	-3.0	-7.8	-6.2
Australia	S&P/ASX 200	-4.6	-4.8	-5.0	-8.6
Bonds	Merrill Lynch Euro over 5 year Govt.	-1.6	-1.6	-0.9	-0.9

Global Equities



United States

Overview
Disappointing retail sales, labour market data and corporate earnings, especially among financials, caused further economic concern amongst investors, resulting in markets retreating over the week.

Bank of America – The bank posted a $1.79bn loss for the last three months of 2008 – its first quarterly loss since 1991 and slashed its quarterly dividend to 1 cent. The US bank will also receive an additional $20bn from the Government in return for preferred stock paying a coupon of 8% and a backstop on further losses on some assets.

Citigroup – Struggling US banking giant Citigroup reported a fourth quarter loss of $8.29bn and for 2008 as a whole, the bank made a net loss of $18.7bn. The bank also announced plans to split the firm in two, involving a partial sale of its brokerage business to Morgan Stanley.

Europe

Overview

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

Deutsche Bank – Shares in Germany's biggest bank fell after it announced that it had made a net loss of €4.8bn in the final quarter of 2008. Amid fears that Europe's banks face a renewed crisis, the bank said its full-year loss would be in the order of €3.9bn – its first loss in 50 years.

Royal Bank of Scotland – Over the weekend, RBS announced that it expects to record losses before write-downs of between £7bn and £8bn for 2008. The Treasury has also swapped £5bn of preference shares for ordinary shares, taking its stake in RBS to nearly 70%.

Ireland

Overview

It was another dramatic week on the ISEQ with the fall primarily due to a hugely underperforming banking sector. The announcement on Friday that Anglo Irish Bank had been nationalised caused markets to fall even further and the Irish market finished the week over 8% lower.

Anglo Irish Bank – The share price slumped 23% to 22 cent before trading was suspended on Friday after the Government seized control.

Asia Pacific

Overview

Asian stocks finished the week in the red as fears of a global recession persist. Elsewhere, Japan's core machinery orders in December fell 16.2%, the steepest monthly decline on record. Chinese financial shares were down on the week after UBS and RBS sold stakes in some of the blue chip financials.

Bonds

The announcement by Standard & Poor's that it had cut Greece's sovereign debt rating, increased worries that this downgrade could be replicated across Ireland, Portugal and Spain, resulted in bond markets falling. The Merrill Lynch >5 year Government Bond Index fell 0.9% on the week.

Global Outlook

- The global economic situation remains fragile, with the employment picture likely to remain extremely bad throughout the year. Policymakers have attempted to prevent a deflationary slump through aggressive interest rate reductions and extraordinary interventions in the financial markets. The intention is to get some stability in the forward looking indicators during the next few months.
- The crisis of confidence in the global banking system means that companies, their suppliers and customers continue to be credit-constrained, and at the same time the volume of banks' bad debts has risen appreciably. This is why much of the effort of policymakers has been directed at trying to support the banking system, to reduce the funding costs of banks and to get credit flowing back to the real economy. There has been some partial success in this area - funding costs for example have begun to fall. More initiatives similar to today's UK announcement will be seen in coming weeks by other countries.
- Global short rates will remain low or fall further over the coming weeks and months. The ECB reduced rates last week to 2% but yet again tried to downplay expectations of more rate cuts. Investors remain unconvinced and have continued to price lower rates, expecting the cycle low to be close to 1%. With short rates close to zero in the US the Fed is focused on driving down other interest rates, such as the level of rates that companies have to pay in order to raise debt financing. Further unconventional policy responses will likely be seen there and in other countries over coming months.
- Government bond prices have risen significantly in the last few months due to falling short rates and slumping equity and corporate bond markets. Some commentators have even wondered whether Government bonds have now entered a bubble period. While it's likely that prices may suffer periodically as Governments step-up their borrowings substantially - and profit-taking is always a risk - it remains the case that the economic backdrop should be bond supportive for a while to come. Ultimately the level of short and long term rates may be seen as "emergency" levels and hence not sustainable but that is not within the markets' time horizon yet.
- Since the lows of quarter four last year global equity markets have rallied around 10% and in that time have weathered an onslaught of dreadful economic news and employment data. That gives some support to the idea that markets have discounted a very weak economic picture going forward. There is some optimism surrounding the new unconventional policies of the Fed and further fiscal stimulus measures from the new US administration and other jurisdictions. However as before, the key to any sustainable rally remains the unfreezing of the money markets and the re-opening of the corporate bond markets. Markets will remain volatile and the direction uncertain until those markets begin to return to normality.
- Currently the funds are close to neutral in equities and bonds, versus the manager average. Within equity sectors the funds are overweight healthcare and technology and underweight basic materials and financials. Geographically the funds have an underweight position in Ireland and Japan, and are slightly overweight in the US, the UK, Europe and the Pacific Basin.

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