

Eagle Star Investments

Weekly News

25th May 2009

Global Overview

Equity markets make modest gains

Most global equity markets made modest gains last week against a backdrop of more mixed economic data. Some concerns were aired with respect to rising bond yields and the AAA rating of the US being under pressure.

US economic data

Minutes from the last Fed meeting revealed that it has reduced its growth forecasts for the US economy over the next few years. Elsewhere, latest jobless claims numbers revealed another high figure of 631,000 jobs lost.

Other lead economic indicators improve

Inter-bank lending rates and risk spreads continue to fall to their lowest levels for more than a year. Elsewhere, the VIX volatility-index, the gauge of stock-market volatility, has declined to levels not seen since the collapse of Lehman Brothers.

UK economic data

The credit rating agency, Standard & Poor's, revised its outlook on the UK's sovereign credit ratings, to negative from stable, because it fears a surge in government debt over the coming years. The UK has had an AAA rating since 1978.

Currencies & Oil

In currency markets, the dollar fell to its lowest level so far this year, as optimism that the worst of the financial crisis may be over and investor concerns over high levels of US debt weakened the safe-haven demand for the currency. The €/£ rate rose 3.5% on the week, ending at over 1.40. The oil price climbed to over \$62 a barrel, as data showing a large increase in Chinese demand and weakness of the US dollar attracted investors to commodities. The oil price finished the week at just over \$61 a barrel.

Index		Year to Date Return 31.12.08 to 22.05.09		1 Week Return 15.05.09 to 22.05.09	
		Local Currency %	Euro %	Local Currency %	Euro %
US	S&P 500	-1.8	-2.3	0.5	-3.0
US	NASDAQ	7.3	6.8	0.7	-2.7
Europe	FT/S&P Europe Ex. U.K.	2.7	2.7	2.3	2.3
Ireland	ISEQ	15.1	15.1	2.5	2.5
UK	FTSE 100	-1.6	7.0	0.4	1.6
Japan	Topix	1.9	-2.5	-0.7	-3.6
Hong Kong	Hang Seng	18.6	18.0	1.6	-1.9
Australia	S&P/ASX 200	1.1	12.0	-0.3	0.4
Bonds	Merrill Lynch Euro over 5 year Govt.	-1.0	-1.0	-0.7	-0.7

Global Equities



United States

Overview

Despite concerns about the implications of rising US government debt levels, reassuring comments from Moody's about the credit-rating outlook for the US, along with better-than-expected retail earnings reports, supported investors' optimism.

Sears – The largest US department store chain reported a surprise profit of \$26m in the first-quarter of 2009, far exceeding analysts' expectations. This is a marked improvement from the same period a year earlier, when the retailer posted a \$56m loss.



Europe

Overview

European stocks ended the week over 2% higher amid renewed optimism about improving financial and economic conditions.

British Airways – The airline reported a loss before tax of £401m, for the year ending 31st March, citing the weak pound and higher fuel costs as reasons for its largest loss since the company was privatised in 1987.



Ireland

Overview

The Irish market followed the rest of the world higher, finishing the week up 2%.

National Asset Management Agency (NAMA) – Today marks the deadline for banks and building societies covered by the State guarantee, to provide the breakdown of their property and development loans to NAMA officials. These loans cannot be transferred to NAMA until the legislation is ratified. The government has signalled its willingness for the Oireachtas to be recalled over the summer months, to ensure NAMA legislation is endorsed.



Asia Pacific

Overview

Asian stock markets weakened across the region as investors reacted to the Federal Reserve's outlook for the US economy. Japan's Topix fell by 0.7%, as Japanese GDP data for the first quarter of 2009, showed that the economy shrank at its fastest pace on record, as exports plunged. Elsewhere, India's market recorded its best week since 1992, on hopes that the victory by the Congress party would bring about much-needed reform.

Bonds

Bond markets fell back last week, in response to the possibility of sovereign downgrades and investors remaining concerned about high levels of bond issuance to finance the recession. The Merrill Lynch over 5 year Government Bond Index fell by 0.7%.

Global Outlook

- Amidst the deepest global recession in decades, the recent focus has been on some green shoots in the global economic data. The hope is that the worst of the negative data is behind us, that an inventory rebound will help growth in the short term and policy action will put a more lasting floor under activity in the medium term.
- From fiscal expansion to rate cuts, to quantitative easing (QE) programs, to measures aimed at removing assets from the banking system, the scale of the initiatives to save the banking system and offset the collapse in private sector demand has 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 now is, how long will these rates be maintained. The success of the US and UK QE programs has been quite mixed so far, and it remains to be seen how the ECB will deploy its corporate bond-buying program. In any event, the major central banks are already talking about exit strategies from these initiatives, suggesting a tepid level of commitment to their implementation.
- Bonds have performed poorly, as investors have re-embraced risk assets and authorities have disappointed with their QE policies, with many commentators also speculating on the long-term inflation risks from the current policy mix. Peripheral bond markets such as, 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.
- Economic green shoots, combined with large short positions and pessimistic sentiment, produced a powerful bear market rally in equity markets over the past few weeks. The stress test of the US banks was choreographed very well, allowing a number of banks to raise new capital or announce their expectation of doing so; corporate debt markets have also been more supportive to equity markets. However, market sentiment seems to have swung from one extreme to another in this large rally, creating room for disappointment with policy initiatives and the possibility of setbacks in risk markets.
- Currently, the funds are close to neutral in equities and overweight bonds, versus the manager average. Within equity sectors, the funds are overweight technology and underweight healthcare and 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.

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.