# Eagle Star Investments

## Weekly News 29th June 2009

# Global Overview

### Equity markets retreat as fear returns

After three months of mostly steady gains on equity markets, investor sentiment turned sour as poor economic data resurrected fears over the strength of the global recovery. Despite a late rally on Thursday, announcements from the World Bank on its downward revision to growth forecasts and the Federal Reserve noting that interest rates will remain low for some time, resulted in most equity markets ending the week lower.

### US economic data

The Federal Reserve left interest rates unchanged, as expected, reiterating that borrowing costs should remain exceptionally low for some time. The Federal Bank did not make any change to its asset purchase plans. The US economy contracted by 5.5% in the first three months of the year, slightly less than estimated. However, investors chose to focus on disappointing jobless claims.

### European economic data

In a bid to unlock credit markets and kickstart a recovery, the European Central Bank pumped a massive €442bn of one-year loans into the eurozone banking system. Meanwhile, whilst the eurozone manufacturing purchasing managers' index rose from 40.7 to 42.4, the services index disappointed, declining from 44.8 to 44.5.

### Oil & Currencies

On commodity markets, the oil price edged lower as weekly US data showed a drop in crude stockpiles but a surprisingly large increase in US reserves of gasoline. The oil price finished the week at just over $69 a barrel. In currency markets, the US dollar weakened against the euro after the Fed indicated that interest rates would remain at low levels. The dollar also came under renewed pressure on discussions that China could diversify its reserves away from the US currency. The €/$ rate finished the week at 1.40.

| | Index | Year to Date Return 31.12.08 to 26.06.09 | | 1 Week Return 19.06.09 to 26.06.09 | |
|---|---|---|---|---|---|
| | | Local Currency % | Euro % | Local Currency % | Euro % |
| US | S&P 500 | 1.7 | 0.7 | -0.3 | -1.2 |
| US | NASDAQ | 16.6 | 15.4 | 0.6 | -0.3 |
| Europe | FT/S&P Europe Ex. U.K. | 0.4 | 0.4 | -1.5 | -1.5 |
| Ireland | ISEQ | 14.9 | 14.9 | -4.4 | -4.4 |
| UK | FTSE 100 | -4.4 | 7.4 | -2.4 | -2.9 |
| Japan | Topix | 7.9 | 1.9 | 0.9 | 1.0 |
| Hong Kong | Hang Seng | 29.3 | 28.0 | 3.8 | 2.8 |
| Australia | S&P/ASX 200 | 4.9 | 19.0 | 0.1 | -0.6 |
| Bonds | Merrill Lynch Euro over 5 year Govt. | -0.2 | -0.2 | 1.0 | 1.0 |

# Global Equities

## United States

### Overview

Disappointing labour market statistics and housing data undermined recent optimism about the economy, resulting in equity markets retreating over the week.

**Oracle** – The software giant beat Wall Street's estimates for its fourth fiscal quarter, and issued a better-than-expected forecast for the current period. The company reported a 7% decline in earnings for the quarter ended May 31st, but these results still came in ahead of estimates from analysts.

## Europe

### Overview

Weak eurozone economic data, combined with poor performance from financial stocks, resulted in European markets finishing 1.5% lower.

**Vodafone** – The world's largest mobile phone company is speculated to be considering a bid for T-Mobile UK Limited, the British wireless unit of Deutsche Telekom AG. This deal could potentially create an entity with about 35 million subscribers, or 40% of the UK mobile market.

## Ireland

### Overview

The ISEQ followed the rest of the world lower, ending the week over 4% down.

## Asia Pacific

### Overview

Despite some intra-week volatility, Asian markets ended the week in positive territory. Both the Topix and Hang Seng indices gained by almost 1% and 4% respectively, as investors shrugged off disappointing economic data.

# Bonds

Eurozone bonds made healthy gains last week, as equity markets fell and investors focused on increased expectations that interest rates will remain low for the foreseeable future. This provided a positive backdrop for government bonds, and the Merrill Lynch over 5 year government bond index rose by 1.0%.

# Global Outlook

- The general feeling amongst investors is that economic data has stabilised after being in freefall earlier this year. The hope is that an inventory rebound will help growth in the short-term and that policy action will put a more lasting floor under activity in the medium-term. Signs of less stress in the financial system have bolstered these hopes. However, a lot of the 'green shoots' sentiment has its origin in China and Asia. This is a concern, given that the region is export-oriented and highly dependent on the US consumer.
- The scale and scope of policy initiatives to save the banking system and offset the collapse in private sector demand have 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 is for how long short rates can stay at these levels. The success of the quantitative easing (QE) programs around the globe has been mixed. The way in which US mortgage rates have been "allowed" to rise in recent weeks is a concern. In any event, the major central banks are already talking about exit strategies from these initiatives.
- Bonds performed quite badly as investors re-embraced risk assets and authorities disappointed with their QE policies. Many commentators have also speculated on the long-term inflation risks from the current policy mix. Peripheral bond markets, such 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. At least in the short-term, bond markets in general have rallied from support levels and have entered a more constructive phase.
- Economic green shoots, oversold markets, large short positions and pessimistic sentiment combined to produce a powerful bear market rally in equity markets over the past three months. The stress test of the US banks was choreographed very well, and corporate debt markets have also been more supportive. While the general feeling in the equity markets is that we may get a period of consolidation followed by further gains, at this stage the burden of proof may be moving more towards the bulls; there could easily be some disappointment with policy initiatives or the pace of improvement in real economic data.
- Currently, the funds are close to neutral in equities and overweight bonds, versus the manager average. Within equity sectors, the funds are overweight technology, more neutral financials and underweight healthcare & industrials. 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.



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