# Eagle Star Investments

## Weekly News 21st December 2009

ZURICH

# Global Overview

### Mixed week for equities

It was a mixed week for equities as uncertainty still hangs over a number of countries' credit ratings, negating the improved growth prospects in many regions.

### Federal Reserve

The Fed left interest rates unchanged when it met last week. It did, however, start preparing investors for next year by announcing the ending of the emergency lending programs from 1st February, citing the "improvements in the functioning of financial markets".

### US data

There was further good economic data for investors to cheer last week. Industrial production, housing starts and the lead economic indicators all showed further improvement last month, with all three beating analysts' expectations. Jobless claims, however, continued to show volatility and disappoint.

### Eurozone data

German business confidence reached its highest level since before the crisis took hold in July 2008. The revival in exports and manufacturing growth has helped this recovery.

### Strengthening dollar

The dollar touched a three-month high against a number of major currencies, following the Federal Reserve's comments on the economy. After strengthening by almost 2% the previous week, the dollar added another 1.9% against the euro, leaving the €/$ rate currently sitting just above 1.43.

### Oil

Oil recorded its biggest weekly gain in two months, due to weather-related factors in the US. Oil finished the week slightly above €73 a barrel, a gain of 5% for the week.

| | Index | Year to Date Return 31.12.08 to 18.12.09 | | 1 Week Return 11.12.09 to 18.12.09 | |
|---|---|---|---|---|---|
| | | Local Currency % | Euro % | Local Currency % | Euro % |
| US | S&P 500 | 22.1 | 19.0 | -0.4 | 1.8 |
| US | NASDAQ | 40.2 | 36.7 | 1.0 | 3.2 |
| Europe | FT/S&P Europe Ex. U.K. | 22.1 | 22.1 | 0.4 | 0.4 |
| Ireland | ISEQ | 24.9 | 24.9 | 0.0 | 0.0 |
| UK | FTSE 100 | 17.2 | 26.2 | -1.2 | 0.1 |
| Japan | Topix | 4.0 | 1.6 | 0.6 | 1.3 |
| Hong Kong | Hang Seng | 47.2 | 43.4 | -3.3 | -1.3 |
| Australia | S&P/ASX 200 | 24.9 | 53.5 | 0.3 | -0.2 |
| Bonds | Merrill Lynch Euro over 5 year Govt. | 5.6 | 5.6 | 0.8 | 0.8 |

# Global Equities

## United States

### Overview

Despite the Federal Reserve pointing to further improvements in the economy and the financial markets, US stocks finished the week mixed due to worries surrounding corporate profits and stock sales by Citigroup and Wells Fargo.

**Citigroup –** One of the last US banks to repay taxpayers' bailout funds sold 5.4bn shares last week. These were at a discount to what the government paid when it purchased its one-third stake in the bank earlier this year. Citigroup said the Treasury would not sell any of its holdings for at least 90 days. However, the issuance caused its shares to fall by 14%, although it finished well off its lows for the week.

**FedEx –** FedEx fell by over 3% after it reduced its profit forecast for Q3. The new earnings-per-share forecast is less than analysts had expected. However, its full year guidance was in line with expectations.

## Europe

### Overview

Most European markets inched higher after business sentiment in the region increased to a 17-month high, while the Fed's more upbeat outlook also helped sentiment.

**Pharmaceuticals –** Roche and Nobel Biocare both gained strongly last week due to the continued strengthening of the dollar. Both companies generate over 30% of their profits in North America and, therefore, have seen their profit outlook improving. Roche gained 4%, while Nobel Biocare gained just over 8%.

## Ireland

### Overview

The Irish market finished the week flat, with banks once again the worst performing stocks.

**Banking sector –** Bank of Ireland and AIB both dropped by 17% due to further concerns about the amount of new capital that each bank will need following the purchase of their loans by NAMA. The Governor of the Central Bank said that it is quite possible the government will end up with as much as a 50% stake in the banks.

## Asia Pacific

### Overview

Most Asian stocks declined for another week as investors fear that markets are getting ahead of themselves and possibly into overshoot territory. Markets in the region are trading at a valuation premium to the rest of the world, bolstered by low interest rates and increased government spending. Property and banking stocks were the hardest hit.

# Bonds

Bonds benefited from the mixed week for equity markets, despite the further improvement in economic data worldwide. Greece came under further pressure following its latest credit-rating downgrade, this time by S&P. The Merrill Lynch over 5 year government bond index rose by 0.8% on the week.

# Global Outlook

- Forecasters expect the global economy to return to positive growth next year following a further contraction of 1% this year. It is inevitable that unemployment will lag any recovery in the economy, meaning that economic conditions will continue to feel weaker than the statistics suggest. Strains within the financial system have eased considerably but bank lending is still impaired. It is partly for this reason that policymakers remain somewhat cautious on the economic outlook. Trade tensions are not yet a major issue but bear watching for any economic or market impact.
- Much of the economic improvement is attributed to the scale and scope of policy initiatives to rescue the banking system and offset the collapse in private sector demand. As we have said before, the ultimate success of these initiatives – or what unintended consequences may arise – remains an open question.
- Short rates continue to hover in a range between 0% and 1% in the major economies. Central banks want to keep rates sufficiently low to foster recovery but also want to exit from emergency policy settings as quickly as conditions permit, a tricky balancing act which causes difficulties in communicating with investors. While recent rate increases in economies like Australia have made investors slightly more nervous, it's notable that future rate expectations in the US are less than 0.25% above their lows and hit new cycle lows in the eurozone last week. On balance, therefore, investors expect that low rates will persist for some considerable time.
- For bond markets, inflation data has been generally supportive, as is the general liquidity backdrop that has helped other assets. However, the 'elephant in the room' remains the exit from emergency policy settings – which is bound to have some impact on bond markets – and these concerns have kept bond markets in a trading range in the past few months. In the eurozone, peripheral bond markets have been more volatile of late as investors become more sensitive to the fiscal positions of individual countries, such as Ireland and Greece.
- In terms of valuations, global equity markets remain rich rather than cheap. To date, markets have been able to recover from any dips with sentiment remaining positive, which is still the case on balance today. However, for some time now, the structure of the rally has been less convincing than the pure market levels suggest, with volumes lighter and momentum indicators diverging somewhat.
- Currently, the funds are closer to neutral in equities and overweight bonds, versus the manager average. Within equity sectors, the funds are overweight technology and underweight utilities. Geographically, the funds have an underweight position in Ireland and Japan, are closer to neutral in the UK, the US and Europe and are overweight in the Pacific Basin.



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