Eagle Star Investments

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ZURICH

Global Overview

Equities start 2011 strongly
Equity markets continued their 2010 rally as economic data in the US and eurozone pointed to a strengthening of the economic recovery.

US jobs report
In December, US employers added a total of 103,000 jobs. This was less than expected and re-emphasised the Federal Reserve's view that it could take four to five years for the labour market to 'normalize fully'. The unemployment rate showed an improvement as it fell to 9.4%, from 9.8%. This fall was mainly attributed to people leaving the workforce.

UK inflation
Inflation in the UK remained above the 3% upper limit for the ninth month in December. This is causing analysts to anticipate that the Bank of England will raise rates sooner than anticipated.

Eurozone data
Survey data from the eurozone was better-than-expected albeit with strength at the core going hand-in-hand with peripheral weakness.

Currencies
The dollar rose against all major currencies as stronger survey data offset slightly disappointing monthly payroll data. This, along with funding worries in the eurozone, caused the €/$ rate to end the week at 1.29. This represents the euro weakening by 3.3% over the week.

Oil
Oil prices fell late in the week after data showed that employers added fewer jobs than expected in December. Oil finished the week at $88 a barrel, a fall of 3.7%.

	Index	1 Week Return 31.12.10 to 07.01.11	
		Local Currency %	Euro %
Global	FTSE World	1.0	3.4
US	S&P 500	1.1	4.6
US	NASDAQ	1.9	5.4
Europe	FT/S&P Europe Ex. U.K.	0.8	0.8
Ireland	ISEQ	-0.5	-0.5
UK	FTSE 100	1.4	4.6
Japan	Topix	3.1	4.3
Hong Kong	Hang Seng	2.8	6.3
Australia	S&P/ASX 200	-0.8	-0.4
Bonds	Merrill Lynch Euro over 5 year Govt.	0.1	0.1

Global Equities

United States

Overview
US stocks continued their rally into 2011 after jobs, auto sales and service sector data boosted sentiment. In December, the Institute for Supply Management's non-manufacturing index rose to its highest level since May 2006. The S&P 500 index finished the week at highs not seen since September 2008.

Boeing – The aircraft manufacturer announced better-than-expected deliveries in 2010. This helped push shares over 6% higher on the week.

Europe

Overview

European markets started 2011 in positive territory as Europe's service and manufacturing industries expanded in December and US data pointed to a strengthening of the economic recovery.

Daimler – The carmaker said that December sales at its US Mercedes-Benz unit rose, when compared to a year earlier, and that sales in the US jumped 18% in 2010 overall. Shares in the company were 7% higher on the week.

Ireland

Overview

The Irish market started 2011 in the red as the largest stock, CRH, and banking stocks, fell.

Grafton Group – In a trading statement, Grafton Group said overall sales in 2010 rose 1% and that in the second half of the year they were up 3%. These figures were broadly in line with analysts' expectations. Shares were marginally lower over the week.

Asia Pacific

Overview

Asian stocks were the best-performing markets last week as export-reliant stocks got a significant boost from the improving economic conditions in the US. This, along with a weakening of local currencies against the dollar, helped markets continue their 2010 rally. Australia was the exception, though, as flooding in Queensland continues to affect mining, hurting shares in the sector.

Bonds

Overall, bond markets were relatively flat over the week, but this hides the fact that peripheral countries remain under continued pressure. Portuguese and Spanish bond prices fell, pushing the yield spread versus German bonds wider, as investors fear demand at the first auctions of 2011 will be weak.

Global Outlook

- Global growth forecasts for 2011 remain fairly healthy, albeit lower than last year. A strong Asia, with some spreading inflation concerns, is a familiar theme, as is a two-tier European economy. The US economy ended last year reasonably strongly and overall growth is set to be steady this year after a good 2010. Inflation is forecast to remain a regional or country-specific concern for investors, rather than a global problem; meanwhile, currency tensions are spreading more widely as more countries seek to resist currency strength.
- Developed country central banks continue to set interest rates at emergency levels, although they have risen in some of the stronger economies such as Canada, India and China. In the US, UK and eurozone, 2011 rate expectations have risen by 0.3% to 0.5% above their cycle lows. The ECB wants to normalise monetary policy as quickly as possible and that is part of the reason for internal tension over its buying of peripheral bonds. However, given the precarious state of some of the peripheral economies, higher interest rates are not sustainable and we would expect the ECB to stay on hold for some time to come. The same conclusion applies to the Fed, although market sentiment is less convinced about that than heretofore.
- German and US long-term interest rates have risen by around 0.9% from the cyclical lows, in line with higher short rate expectations and better growth numbers. We would expect that bonds in these markets should at least stabilise in the short-term; if nothing else, rising yields are clearly counter to existing Fed policy, although the ECB's reaction to rising yields is more a concern about the periphery than Germany. However, the general consensus is that German and US yields will rise further over the course of 2011. Spreads in peripheral eurozone markets continue to be another major focus of investors who are concerned that they are being softened up for sovereign default, despite rhetoric to the contrary. It remains unlikely that we will get through this peripheral debt crisis without a full scale, long-dated, ECB-funded mechanism.
- Global equities have started the year positively and the general market expectation is for further gains during 2011, on the basis of reasonable valuations and mid-teens earnings' growth. The eurozone debt crisis continues to dominate country performance within Europe and this trend is likely to persist for some time. In the short-term, overall market sentiment measures are high, although not extreme, suggesting that the fuel for near-term price gains may be limited. We can expect gains during the year to be accompanied by volatility and we can anticipate unspecified "surprises" over the next 12 months, as experienced last year. Investors will need to be vigilant and active once again during 2011.
- Currently, the funds are neutral equities and overweight bonds, versus the manager average. Within equity sectors, the funds are overweight technology and still a little light in the financial stocks with other positions reasonably balanced. Geographically, the funds are underweight in Ireland and Europe, neutral in the UK and Japan and remain overweight in Pacific Basin and the US.

This outlook does not constitute an offer and should not be taken as a recommendation from Zurich Life.
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