Zurich Life
Weekly Investment News

10th October 2011

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Global Overview

Most markets gain

Most equity markets ended the week higher, as markets shrugged off bank and sovereign downgrades, instead focusing on better than expected economic data releases along with optimism that the eurozone debt crisis will be resolved within weeks.

US data

Non-farm payrolls rose by a better than expected 103,000 in September (following an upwardly revised 57,000 in August), while the unemployment rate held steady at 9.1%.

Bank of England

The Bank of England left interest rates unchanged at 0.5% as expected, and announced a further £75 billion of asset purchase over the next four months.

Moody's rating agency

Ratings agency, Moody's, downgraded the credit rating of twelve UK banks, noting that the downgrade did not reflect a deterioration in the financial strength of the banking system.

ECB

The European Central Bank left interest rates unchanged at 1.5% on Thursday. Jean Claude Trichet announced further measures in the form of a new €40 billion covered bond purchase plan to support the banking sector.

Italian and Spanish sovereign rating

Credit rating agency Fitch cut Italy's credit rating by one notch from AA- to A+, with a negative outlook. Spain's sovereign credit rating was also cut by two notches from AA+ to AA-, also accompanied with a negative outlook.

Currencies & oil

In currency markets, the safe haven status of the dollar came under pressure at times as investors gained confidence in riskier assets. The €/$ rate ended the week at 1.34. The positive US jobs data boosted demand for oil and the West Texas oil price ended the week almost 5% higher, at $83 a barrel.

	Index	Year to Date Return 31.12.10 to 07.10.11		1 Week Return 30.09.11 to 07.10.11	
		Local Currency %	Euro %	Local Currency %	Euro %
Global	FTSE World	-10.9	-11.7	1.6	1.5
US	S&P 500	-8.1	-8.3	2.1	2.6
US	NASDAQ	-6.5	-6.7	2.6	3.1
Europe	FT/S&P Europe Ex. U.K.	-18.7	-18.7	2.3	2.3
Ireland	ISEQ	-11.2	-11.2	2.4	2.4
UK	FTSE 100	-10.1	-10.5	3.4	3.3
Japan	Topix	-17.5	-12.9	-2.6	-1.7
Hong Kong	Hang Seng	-23.1	-23.4	0.7	1.1
Australia	S&P/ASX 200	-12.3	-16.5	3.8	4.6
Bonds	Merrill Lynch Euro over 5 year Govt.	4.5	4.5	-0.7	-0.7

Global Equities

United States

Overview

US equities registered strong gains last week, buoyed by optimism that eurozone policymakers are finally moving to take decisive action over the region's sovereign debt crisis.

Financial stocks – The financial sector was one of the weakest performers last week, with investors remaining concerned that any recapitalisation of European banks will take time to implement. The main fallers included Bank of America, Goldman Sachs and Citigroup.

Europe

Overview

European markets ended the week in positive territory, boosted by the ECB's moves to shore up the financial sector with additional funding measures. Over the weekend, the leaders of France and Germany announced plans to recapitalise European banks over the next three weeks.

Dexia – On early Monday, a rescue plan for Dexia Bank was announced which includes the sale of the Belgian unit for €4 billion to the Belgian state and a €90 billion guarantee of its funding for the next ten years.

Ireland

Overview

The Irish market tracked global markets, gaining 2% over the week.

CRH – The construction company, which accounts for a large constituent of the ISEQ, rose almost 10% over the week on better US macro data.

Asia Pacific

Overview

Despite experiencing choppy trading, most Asian markets gained as speculation increased that the eurozone will be able to solve its debt crisis, along with encouraging economic data releases.

Bonds

Eurozone bond markets fell on the back of improving economic data figures and speculation that European leaders may be moving closer to a resolution on the debt crisis. As a result, investors moved away from safer assets towards risky equity markets. The Merrill Lynch over 5 year government bond index ended the week 0.7% lower.

Global Outlook

- Indicators of economic activity suggest that global growth rates have peaked for now. Investors are concerned that this is more than a mid-cycle pause and is, perhaps, something more significant. Inflation has been more of a regional or country-specific concern for investors, particularly in some Asian countries, but there have been some shared global concerns, such as energy and food prices; however, some of these should dissipate if growth moderates further. Additionally, there are no major countries actively seeking currency strength – the opposite is the case, if anything - a key indicator that policymakers are not concerned about inflation.
- Short-term interest rates remain at emergency levels in the US and the Fed has recently committed to these levels for another two years. Rates will likely be cut soon in the eurozone, validating the view that this year's hikes were premature - and more easing should be expected globally in the midst of the growth slowdown and financial market stresses. The Bank of England extended its quantitative easing from £200 billion to £275 billion as the crisis threatens the recovery of the US economy.
- The ECB buying of Italian and Spanish bonds had some initial positive impact but stresses re-emerged quickly due to worries over the ECB's commitment to the programme, worries validated by the recent resignation of its (German) chief economist. A sense of extreme nervousness pervades the eurozone bond markets at the moment. The situation is very fluid with the prospect of a Greek default being a major concern. European leaders are currently drafting plans to recapitalise the region's banks to insulate them from solvency concerns stemming from their sovereign bond holdings. To date all of the various measures announced have not solved the problem, and it remains to be seen how politically feasible some of the proposed "solutions" are. German and US bond yields have bounced from extremely low levels as politicians have made efforts to convince investors that they will tackle the eurozone debt crisis in a meaningful manner. While yields could rise in the near term if equities recover some of their losses, long-term interest rates could stay very low for a further considerable period of time.
- In what has been a volatile year, global equities are down around 12% in euro terms, the vast bulk of that fall happening since July. Valuations may be reasonable but investors are now questioning the path of future corporate profits, given renewed economic growth worries; worries over bank funding costs and banks' exposures to peripheral government debt also loom large. Investors are also incorporating risks with regard to fiscal sustainability, default in the eurozone and even the future of the euro itself. We remain concerned that further slow-down concerns have yet to be fully discounted by investors despite recent negative price action. In the immediate term, there is a sense that investors have lost faith in the ability of policymakers in the US and Europe to control events; further falls are quite possible if investors remain in this mindset. Currently, the only offset to this is that sentiment is very negative, often a time at which markets temporarily bottom, and some further policy action could assuage near-term nervousness.
- Currently, the funds are closer to neutral in equities and bonds versus the manager average. Within equity sectors the funds remain underweight financials and overweight technology. Geographically, the funds are underweight in Ireland, the UK, neutral in Japan, Europe and the Pacific Basin and overweight in the US.

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