

Weekly Review

Week ending 20th November 2009

Equity markets mostly consolidated their recent gains last week with many regional indices posting small declines. The S&P 500 index lost -0.1% for the week, whilst UK and European indices declined -1.0% and -1.7% respectively. Japan continued its notable recent slide with a -3.2% return for the week, bringing month to date performance to -6.3% and marking significant underperformance versus developed market equities which have thus far gained 3.8% in USD terms for November. Fixed income securities provided positive returns on the whole, with UK government and investment grade debt leading the pack with gains of 1.6% and 1.3% respectively. Commodities also performed well with broad indices gaining in excess of 2%. Amongst currencies, the US Dollar continued to exhibit negative correlation with equity markets by strengthening versus most major currencies with the exception of the Japanese Yen.

Over in the US, various dovish comments coming out of the Fed last week gave renewed confidence to market participants that rates will indeed remain low for an “extended period”. The Fed chairman Ben Bernanke justified this on the basis that economic activity continues to be constrained by reduced levels of bank lending and high unemployment. On this point it is interesting to consider the length of time between rate cuts and hikes for previous recessions in the US. The first rate hike following the downturn in the early 90’s came almost five years after the first cut, and for the recession in the early part of this decade it came three and a half years after the first cut. If these were to be viewed as comparable scenarios then we would expect rate hikes to begin in 2011 or 2012 this time around, but of course there is a possibility that things may be different this time.

Anyway, comments made by Bernanke and others over the course of last week led to a rally in the front end of the Treasury yield curve with 2 year notes breaking through 0.7%. This has increased steepness of the yield curve to near record levels (see chart bottom left of page), something that has historically been an indicator of good future investment returns. However, there is a risk that the long end of the curve may become unstable due to concerns over inflation and / or supply issues and authorities therefore lose control of monetary conditions. This increased risk potentially explains some of the recent strength in the gold price.

Gold price \$/oz



The chart above shows the gold price. The eternal debate as to whether gold is a valid investment continues to rumble on, whilst meanwhile its price continues to grind higher. Sceptics argue that gold has no utility and that it should be viewed as a speculative interest because it does not generate returns that can be analysed and valued; it is instead influenced mostly by demand from investors. On the other hand, those who are currently bullish on gold largely view it as a hedge against today’s unprecedented economic conditions and the risks posed by inflation or US Dollar devaluation. For now, the bulls are enjoying strong returns and gold is outperforming even equities in November with a return of 9.5% for the month to date.

US Treasury Yield Curve Steepness (30 yr yield - 2 year yield)



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Asset Class/Region	Index	Currency	Week	MTD	YTD
Equities					
United States	S&P 500 NR	USD	-0.1	5.5	22.7
United Kingdom	FTSE All Share TR	GBP	-0.8	4.4	26.4
Continental Europe	MSCI Europe ex UK NR	EUR	-1.7	2.5	23.2
Japan	Topix TR	JPY	-3.2	-6.3	-0.5
Global	MSCI World NR	USD	-1.0	3.8	27.3
Global emerging markets	MSCI World Emerging markets TR	USD	0.3	5.6	73.9
Bonds					
US Treasuries	JP Morgan United States Government Bond Index TR	USD	0.5	0.5	-2.0
US Treasuries (inflation protected)	Barclays Capital U.S. Government Inflation Linked TR	USD	1.0	1.9	12.0
US Corporate (investment grade)	Barclays Capital U.S. Corporate Investment Grade TR	USD	0.4	0.6	18.7
US High yield	Barclays Capital U.S. High Yield 2% Issuer Cap TR	USD	0.2	0.9	53.5
UK Gilts	JP Morgan United Kingdom Government Bond Index TR	GBP	1.6	0.4	1.2
UK Corporate (investment grade)	Merrill Lynch Sterling Non Gilts TR	GBP	1.3	0.6	11.9
Euro Government Bonds	Citigroup EMU GBI TR	EUR	0.4	0.2	4.7
Euro Corporate (investment grade)	Barclays Capital Euro Aggregate Corporate TR	EUR	0.4	0.6	15.4
Euro High yield	Merrill Lynch Euro High Yield 3% constrained TR	EUR	0.3	0.6	73.7
Japanese Government	JP Morgan Japan Government Bond Index TR	JPY	0.3	0.6	0.6
Global Government bonds	JP Morgan Global GBI	USD	0.5	1.3	5.2
Global Bonds	Citigroup World Broad Investment Grade (WBIG) TR	USD	0.3	1.1	8.5
Global Convertible bonds	UBS Global Convertible Bond	USD	0.0	2.8	38.7

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Asset Class/Region	Index	Currency	Week	MTD	YTD
Property					
US Property securities	MSCI US REIT TR	USD	-5.0	5.7	17.0
UK Property securities	FTSE EPRA/NAREIT United Kingdom TR	GBP	-5.1	2.5	14.0
Europe ex UK Property securities	FTSE EPRA/NAREIT Developed Europe ex UK TR	EUR	-2.7	-0.4	38.7
Asia Property securities	FTSE EPRA/NAREIT Developed Asia TR	USD	-2.3	-2.5	39.0
Global Property securities	FTSE EPRA/NAREIT Developed CR	USD	-1.9	1.2	27.2
Currencies					
Euro		USD	-0.3	0.6	6.8
Sterling		USD	-1.0	0.2	14.9
Yen		USD	0.8	1.7	1.9
Australian Dollar		USD	-1.9	1.1	31.0
Rand		USD	-2.1	3.0	21.7
Commodities					
Commodities	RICI TR	USD	2.2	3.1	24.0
Agricultural Commodities	RICI Agriculture TR	USD	2.6	5.7	5.7
Oil	Brent Crude Index (ICE) CR	USD	2.2	1.7	98.5
Gold	Gold index	USD	3.3	9.5	32.4

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