

# Weekly Review

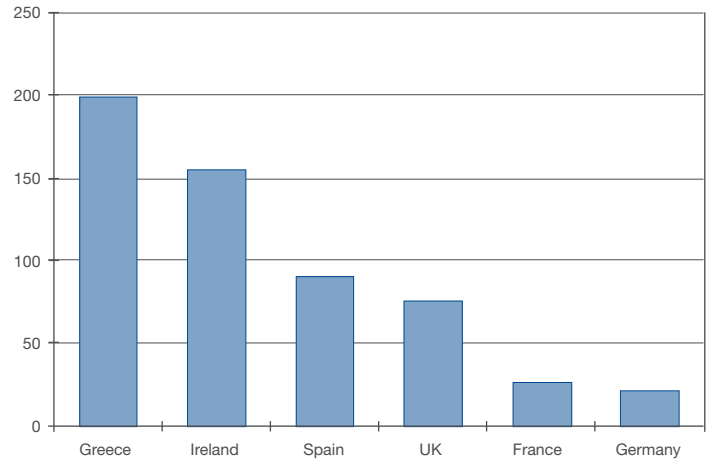
Week ending 11<sup>th</sup> December 2009

Positive investment returns proved elusive last week as most asset classes posted flat to negative returns, with the only notable exception being US investment grade and high yield bonds. With the corporate earnings season finished news flow was mostly focused on sovereign risk issues, particularly those of Dubai and Greece. Following unprecedented levels of stimulus, and with fiscal deficits now bulging, markets are becoming increasingly concerned about the possibility of a sovereign default. Elsewhere, the UK pre-budget speech commanded some attention although little came of it, whilst Ireland announced an austere budget that gives an indication of the pain that many Western countries will have to experience in years to come.

It is widely accepted that fiscal tightening must commence well ahead of any tightening of monetary policies. Indeed with fiscal deficits sitting at extremely high levels in most western countries authorities have few options but to tighten soon, with a large amount of this likely to come via higher taxation. With markets scrutinizing public accounts there is a real need for authorities to announce budgets that can return their finances to a level and sustainable footing.

In the UK last week, Chancellor of the Exchequer Alastair Darling delivered the pre-budget report which was an opportunity to begin addressing the country's huge deficit. However, no meaningful tightening of fiscal policy was undertaken and the announcement that commanded the most attention was a punitive 50% tax on bankers' bonuses over £25,000. With a general election due by May 2010 it looks as though the bulk of the fiscal tightening will not take place until 2011. Monetary conditions also remained unchanged in the UK with interest rates left at 0.5% and the quantitative easing budget at £200bn. As mentioned previously, Ireland announced major public sector cuts during the week including a 5% pay cut for public sector workers earning below €0,000 a year. Ireland is clearly further down the road towards fiscal reform, but nonetheless a budget deficit of 11.6% of GDP is still expected for 2010.

5 Year Credit Default Swap Spreads (11<sup>th</sup> December 2009)



However, the main source of concern for markets remains Greece where the risk of default is deemed to be highest due to an unsustainable budget deficit of over 12% of GDP. The cost of insuring against a default on their debt has more than doubled over the past three months according to credit default swap (CDS) spreads. This is a measure of the cost of insuring against a default on sovereign debt. The chart above shows the spread compared to other countries deemed to be in a stressed position, and also compared to what are perceived to be their much safer peers of France and Germany (see chart).

This backdrop of news produced generally negative returns for equities and fixed income securities. In local currency terms most regional equity markets declined by over 1%, although the S&P 500 managed a gain of 0.1%. All regions remain in positive territory for the month following the strong gains of the week before. Within fixed income, government bonds also produced mostly negative returns with the JP Morgan Global Government Bond Index posting a return of -0.7%. Credit indices produced more of a mixed bag but investment grade and high yield bonds achieved positive returns of as much as 0.8% in the US and Continental Europe. Broad commodities posted a decline of -2.9%, with oil and gold falling -2.1% and -5.6% respectively. The US Dollar weakened against most major currencies with the exception of the Japanese Yen.

**Returns to 11 December 2009**

| Asset Class/Region                  | Index  | Currency | Week | MTD  | YTD  |
|-------------------------------------|--|----------|------|------|------|
| <b>Equities</b>                     |  |          |      |      |      |
| United States                       | S&P 500 NR   | USD      | 0.1  | 1.0  | 24.5 |
| United Kingdom                      | FTSE All Share TR                                    | GBP      | -1.2 | 1.4  | 26.4 |
| Continental Europe                  | MSCI Europe ex UK NR                                 | EUR      | -1.7 | 2.3  | 24.3 |
| Japan                               | Topix TR   | JPY      | -0.2 | 5.7  | 5.3  |
| Global                              | MSCI World NR  | USD      | -1.1 | 0.6  | 28.5 |
| Global emerging markets             | MSCI World Emerging markets TR                       | USD      | -1.0 | 2.1  | 75.4 |
| <b>Bonds</b>                        |  |          |      |      |      |
| US Treasuries                       | JP Morgan United States Government Bond Index TR     | USD      | -0.1 | -1.4 | -2.5 |
| US Treasuries (inflation protected) | Barclays Capital U.S. Government Inflation Linked TR | USD      | -0.6 | -2.1 | 10.6 |
| US Corporate (investment grade)     | Barclays Capital U.S. Corporate Investment Grade TR  | USD      | 0.4  | -0.5 | 19.0 |
| US High yield                       | Barclays Capital U.S. High Yield 2% Issuer Cap TR    | USD      | 0.8  | 1.5  | 56.1 |
| UK Gilts                            | JP Morgan United Kingdom Government Bond Index TR    | GBP      | -1.1 | -2.3 | -0.7 |
| UK Corporate (investment grade)     | Merrill Lynch Sterling Non Gilts TR                  | GBP      | -0.5 | -1.3 | 11.1 |
| Euro Government Bonds               | Citigroup EMU GBI TR                                 | EUR      | -0.1 | -0.4 | 4.7  |
| Euro Corporate (investment grade)   | Barclays Capital Euro Aggregate Corporate TR         | EUR      | 0.3  | 0.1  | 15.8 |
| Euro High yield                     | Merrill Lynch Euro High Yield 3% constrained TR      | EUR      | 0.2  | 1.0  | 74.0 |
| Japanese Government                 | JP Morgan Japan Government Bond Index TR             | JPY      | 0.0  | 0.0  | 0.8  |
| Global Government bonds             | JP Morgan Global GBI                                 | USD      | -0.7 | -2.7 | 4.3  |
| Global Bonds                        | Citigroup World Broad Investment Grade (WBIG) TR     | USD      | -0.7 | -2.1 | 7.8  |
| Global Convertible bonds            | UBS Global Convertible Bond                          | USD      | -0.2 | 0.5  | 40.0 |

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| Asset Class/Region               | Index                                      | Currency | Week | MTD  | YTD  |
|----------------------------------|--|----------|------|------|------|
| <b>Property</b>                  |  |          |      |      |      |
| US Property securities           | MSCI US REIT TR                            | USD      | -1.7 | 3.1  | 21.7 |
| UK Property securities           | FTSE EPRA/NAREIT United Kingdom TR         | GBP      | -4.1 | -1.9 | 7.0  |
| Europe ex UK Property securities | FTSE EPRA/NAREIT Developed Europe ex UK TR | EUR      | -3.6 | 0.1  | 35.2 |
| Asia Property securities         | FTSE EPRA/NAREIT Developed Asia TR         | USD      | -0.6 | 1.6  | 43.5 |
| Global Property securities       | FTSE EPRA/NAREIT Developed CR              | USD      | -1.9 | 1.3  | 29.3 |
| <b>Currencies</b>                |  |          |      |      |      |
| Euro                             |  | USD      | -1.8 | -2.6 | 5.2  |
| Sterling                         |  | USD      | -1.8 | -1.1 | 12.9 |
| Yen                              |  | USD      | 0.4  | -3.8 | 1.2  |
| Australian Dollar                |  | USD      | -0.4 | -0.4 | 30.7 |
| Rand                             |  | USD      | -1.3 | -1.3 | 22.8 |
| <b>Commodities</b>               |  |          |      |      |      |
| Commodities                      | RICI TR                                    | USD      | -2.9 | -4.3 | 20.1 |
| Agricultural Commodities         | RICI Agriculture TR                        | USD      | 0.0  | -2.8 | 4.8  |
| Oil                              | Brent Crude Index (ICE) CR                 | USD      | -2.1 | 1.1  | 94.2 |
| Gold                             | Gold index                                 | USD      | -5.6 | -4.4 | 30.5 |

### Important notes

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