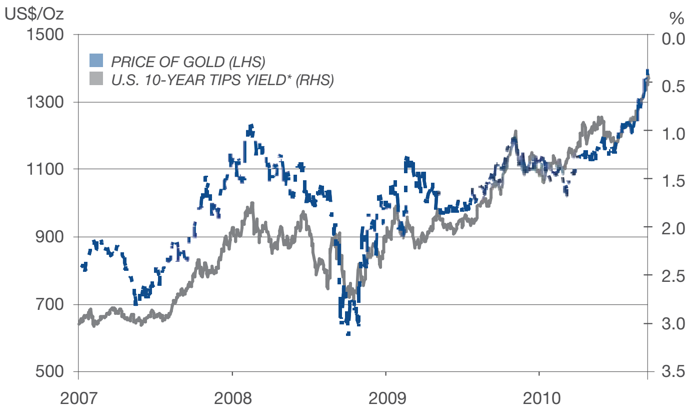
Weekly Review

Week ending 15th October 2010

Global equity markets rose for a seventh consecutive week as measured by the MSCI World Index on the back of better than expected earnings reports and the enduring prospect of further monetary stimulus in the US. Since Federal Reserve Chairman Ben Bernanke first hinted at a second round of quantitative easing on August 27th the S&P 500 Index has rallied by over 12%. In a speech on Friday Bernanke further cemented expectations of more asset purchases by reiterating that additional action may be required to address low inflation and high unemployment, although no firm details of any new stimulus were provided. It is increasingly evident that US monetary policy is more geared towards avoiding deflation than inflation, suggesting that real interest rates are likely to remain low for some time yet. Inflation expectations have increased accordingly in recent weeks to reflect this asymmetric policy approach.

Gold vs. U.S. real interest rates



With this in mind the above chart shows the relationship between the gold price and real interest rates: gold has rallied as real interest rates have declined with the two appearing to track each other closely. Despite having already reached the lower bound for nominal policy rates the Fed managed to further decrease real interest rates in the economy via quantitative easing. With real yields now below 1% on a 10 year basis there is little room for further decreases, so if this relationship persists the upside for gold appears to be limited. Indeed gold continued to hit new record highs last week and has tripled in just five years, but sentiment remains positive nonetheless with the futures market suggesting that there is a high degree of interest backing further gains. Although there are measures that make the yellow metal appear undervalued – for example when adjusted for inflation gold remains well below its all-time high – there remains plenty of downside potential. Indeed one should also remember that the annualised volatility of the gold price is only marginally lower than that of global equities.

The US dollar continued its recent weakness versus most major currencies over the past five days as it sank to its lowest level of the year on a trade-weighted basis and to a nine month low versus the euro. The Monetary Authority of Singapore played a part in the former by widening the trading band of the Singapore dollar against the US dollar, thus inviting a stronger local currency so as to reduce the risk of inflation in a country that was able to boast 10.3% year-on-year GDP growth as of the end of Q2. On the other hand, in a move echoing that made by Brazil recently, Thailand last week introduced a tax on foreign holdings of bonds in order to rein in currency appreciation, with the Thai Baht having risen by almost 12% versus the greenback year to date.

With the exception of Japan all regional equity markets posted positive returns over the week resulting in the MSCI World Index adding 1.2%, a slight underperformance compared to the 1.9% return of emerging markets. Most commodities also strengthened on the back of a weaker US dollar, as the RICI Agriculture Index and gold gained 2.0% and 1.9% respectively. Within the fixed income space convertible bonds added 1.1% over the period to more or less keep up with equity markets and outperform other credit indices. Investment grade credit posted negative returns across most regions on the back of rising government bond yields – 10 year US Treasury and German Bund yields rose by 17 and 12 basis points respectively – although global government bond indices only delivered small declines due to US dollar weakness. High yield indices made modest gains in the US and Europe, returning 0.4% and 0.5% in local currency terms.

Source: RMB Asset Management / Bloomberg / Lipper Hindsight. October 2010.

Returns to 15 October 2010

Asset Class/Region	Index	Currency	Week	Month to date	Year to date
Equities					
United States	S&P 500 NR	**USD**	1.0	3.1	6.7
United Kingdom	FTSE All Share TR	**GBP**	0.9	2.9	9.7
Continental Europe	MSCI Europe ex UK NR	**EUR**	1.7	2.7	5.6
Japan	Topix TR	**JPY**	-1.6	-0.4	-7.3
Australia	S&P/ASX 300 TR	**AUD**	0.2	2.4	-0.3
Global	MSCI World NR	**USD**	1.2	3.8	6.5
Global emerging markets	MSCI World Emerging markets TR	**USD**	1.9	4.3	15.6
Bonds					
US Treasuries	JP Morgan United States Government Bond Index TR	**USD**	-0.8	-0.3	8.7
US Treasuries (inflation protected)	Barclays Capital U.S. Government Inflation Linked TR	**USD**	-0.2	2.4	9.6
US Corporate (investment grade)	Barclays Capital U.S. Corporate Investment Grade TR	**USD**	-1.3	-0.5	10.3
US High yield	Barclays Capital U.S. High Yield 2% Issuer Cap TR	**USD**	0.4	1.7	13.2
UK Gilts	JP Morgan United Kingdom Government Bond Index TR	**GBP**	-1.0	-0.7	9.1
UK Corporate (investment grade)	Merrill Lynch Sterling Non Gilts TR	**GBP**	-0.4	0.0	11.2
Euro Government Bonds	Citigroup EMU GBI TR	**EUR**	-0.2	0.4	5.0
Euro Corporate (investment grade)	Barclays Capital Euro Aggregate Corporate TR	**EUR**	-0.1	0.4	6.9
Euro High yield	Merrill Lynch Euro High Yield 3% constrained TR	**EUR**	0.5	1.8	17.0
Japanese Government	JP Morgan Japan Government Bond Index TR	**JPY**	-0.2	-0.1	3.3
Australian Government	JP Morgan Australia GBI TR	**AUD**	-0.1	-0.3	6.0
Global Government bonds	JP Morgan Global GBI	**USD**	-0.1	1.6	10.1
Global Bonds	Citigroup World Broad Investment Grade (WBIG) TR	**USD**	-0.1	1.5	7.7
Global Convertible bonds	UBS Global Convertible Bond	**USD**	1.1	3.1	9.0
Emerging Market Bonds	JP Morgan EMBI +	**USD**	0.2	1.6	16.2

Source: RMB Asset Management / Bloomberg / Lipper Hindsight. October 2010.

Returns to 15 October 2010

Asset Class/Region	Index	Currency	Week	Month to date	Year to date
Property					
US Property securities	MSCI US REIT TR	**USD**	1.4	4.4	23.8
UK Property securities	FTSE EPRA/NAREIT United Kingdom TR	**GBP**	0.8	6.3	3.7
Europe ex UK Property securities	FTSE EPRA/NAREIT Developed Europe ex UK TR	**EUR**	2.5	3.9	22.5
Australian property securities	FTSE EPRA/NAREIT Australia TR	**AUD**	0.4	1.4	2.9
Asia Property securities	FTSE EPRA/NAREIT Developed Asia TR	**USD**	1.5	6.0	17.1
Global Property securities	FTSE EPRA/NAREIT Developed CR	**USD**	1.5	5.3	15.9
Currencies					
Euro		**USD**	0.6	2.6	-2.3
Sterling		**USD**	0.5	1.6	-0.8
Yen		**USD**	0.6	2.7	14.4
Australian Dollar		**USD**	0.6	2.2	10.0
Rand		**USD**	0.6	2.4	8.2
Commodities					
Commodities	RICI TR	**USD**	0.1	3.4	6.1
Agricultural Commodities	RICI Agriculture TR	**USD**	2.0	6.4	18.5
Oil	Brent Crude Index (ICE) CR	**USD**	-1.2	8.0	8.6
Gold	Gold index	**USD**	1.9	4.6	21.5

Source: RMB Asset Management / Bloomberg / Lipper Hindsight. October 2010.

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