



## Newsflash

A new month and the 66<sup>th</sup> issue of Viewpoint from FP.

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## Table of Contents

- |                      |       |
|----------------------|-------|
| 1. March 2012 Review | 1 – 5 |
| 2. Important Notice  | 7     |

**momentum**



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Asset allocators continue to debate the merits of equities versus fixed income securities. Whilst core developed market government bonds have enjoyed a multi decade bull run, which has greatly enhanced their risk-return profile, equities have appeared to lurch from boom to bust. In 2011, global equities declined by 5.5%, with monthly returns ranging between -8.6% and +10.3%, whilst bonds smoothly earned a return of 7.2% for the year. To date in 2012, however, equities are in the ascendance, whilst bonds have lost ground. Global equities rose by 1.3% in March, buoyed by strong positive returns in the second week of the month. Within this headline return, shares in the US and Japan rallied by over 3% in local currency terms, whilst the UK and mainland Asia recorded losses. Global government bonds mirrored their return in February with falls of 1.1%, to leave investors in negative territory for the year. In January global developed equities outperformed global government debt by 3.7%, with this performance differential widening to 6.0% in February, before narrowing last month to 2.4%.

Beginning on the 19th of December, global equities have moved steadily higher over the course of the first quarter of 2012. This momentum appeared to slow last month, however. Indeed, since closing above 1,400 points on 15 March, the S&P 500 has traded within a narrow band of between 1,417 and 1,393 points, as if investors have become anchored to this symbolic threshold.

Stock markets incorporate far more information than simple threshold levels, however, and the underlying data has equally slowed to arrest the progress of equity markets, at least in the short term.

The US has been the focus of the recent improvement in economic data. Positive sentiment was enforced by the final reading of US fourth quarter GDP, which left output growth unchanged at 3.0% (annualised) quarter-on-quarter, the strongest rate of output growth since June 2010. Commentators have highlighted a number of data disappointments in March, namely with regards to regional manufacturing surveys in the US. Regional surveys of announced activity levels by companies fell below economists' forecasts in March, having roundly trumped expectations the previous month. Post the quarter end, however, the ISM Manufacturing index, the largest forward-looking survey of activity, beat expectations, rising to 53.4 from 52.4 the previous month. Indeed, the balance of positive surprises to negative ones, as aggregated by Citigroup's Economic Surprise index, remains positive, despite trending downwards in 2012. By the end of the month, the index stood a little above zero, indicating that either expectations are now appropriately set or a portion of the data has indeed softened.

Confidence is a key determinant of final demand, and hence the improvement in US sentiment may support output growth going forwards. Whilst still some way below its pre-crisis norm, confidence has nonetheless shown a significant improvement since October last year. The US Conference Board's Consumer Confidence index exceeded expectations for the second month in a row in March at 70.2, with consumers' assessment of current conditions at its highest level in three and a half years. The University of Michigan's survey has equally consistently ticked upwards since August 2011, reaching a 13 month high in March. Confidence has also shown signs of improvement in Europe. German business confidence rose to an eight month high in March, according to the Ifo Institute's Business Climate index. Italian consumer confidence similarly exceeded economists' forecasts in March, at 96.8 versus 93.5 expected, whilst French consumer confidence rose by the most in almost five years. Sentiment

was given a timely boost on the last business day of the month, as EU finance ministers added EUR 200 billion to the region's existing bailout facilities.

Greece's debt restructuring in March marked the first such event in an advanced economy in over 60 years. The exchange, and subsequent arbitration process involving credit derivatives was completed without major incident. Sellers of Credit Default Swaps (derivatives contracts designed to protect against the risk of default by bond issuers) face a bill of around USD 2.5 billion on Greek government bonds, after the final price of the nation's outstanding obligations was agreed at 21.5% of face value. Banks that have sold CDS contracts are obliged to redeem the bonds at face value from current holders, thereby covering the 78.5% shortfall. Both the International Monetary Fund (IMF) and ratings agency Standard & Poor's have questioned the viability of Greece's restructuring, raising the prospect of further intervention in the future. Data from purchasing managers in both Europe's services and manufacturing sectors disappointed economists' forecasts in March, with Germany's Manufacturing index dipping below par at 50, indicating a drop in announced activity levels by survey respondents. To put this latest reading into context, the series fell as low as 32 in January 2009.

Credit followed government bonds down over the month, whilst a degree of spread compression helped insulate returns for corporate bond holders. The Citigroup World Broad Investment Grade index fell by 0.6% in March in US dollar terms, compared to returns of -1.1% for government bonds. In Europe, corporate debt added 0.9% in euro terms, whilst high yield rallied by 1.3%. Both corporations and governments have taken the opportunity provided by current low interest rates to increase their issuance of debt. The UK treasury announced plans during the quarter to consider issuing bonds with a tenor of 100 years, or even in perpetuity, in order to add a low interest rate component into their debt capital structure.

Against this background of moderating economic data balanced against improved confidence, there are several key issues for investors to focus on. In Europe, investors' attention has shifted away from Greece towards Iberian neighbours Portugal and Spain. Portuguese 10 year government bond yields have been above 10% for the past nine months, implying a lack of faith in Lisbon's creditworthiness, even though the country has sufficient funds to meet its obligations until 2013 (by virtue of its bailout from the EU and the IMF). In Spain, banks' 'bad loans' as a proportion of total lending have reached their highest level since 1994, according to the central bank, as record unemployment pushes borrowers into arrears. Central bank officials dealt a blow to the government by confirming that the economy is likely to have entered a new recessionary phase in the first quarter of 2012, with the government already committing to swingeing spending cuts in order to meet its deficit targets.

Authorities in China have cut the country's growth target to 7.5%, down from 8% between 2005 and 2011. China's official Purchasing Managers' index registered 53.1 in March, versus 50.8 expected; HSBC's index, which, amongst other differences from the official series, takes into account seasonal variations in activity, fell to 48.3 in March from 49.6

in February. Beijing acted to ease lending conditions in rural areas during March, by reducing the reserve requirement ratio for specific branches of the Agricultural Bank of China Ltd. Moderating inflation may leave authorities with room to loosen monetary policy.

Global property securities added 1.2% in March. Real estate is one of the main components of household and corporate balance sheets and the weakness of this area of the market has acted as a meaningful headwind to the global recovery post 2008. As such, the outlook for property markets in major regions remains of keen interest to investors. Confidence amongst US homebuilders remained steady in March at its highest level since June 2007, whilst sales expectations climbed for the sixth consecutive month. The mood was tempered as month-on-month new home sales growth disappointed forecasters.

Commodities fell by 2.6% in March according to the Roger's International Commodity index. Beijing increased fuel prices towards the end of the month, with prices for petrol and diesel rising by 7% and 7.8% respectively. The news depressed investors' outlook for Chinese growth, in turn putting pressure on some commodities markets.

## Asset Class Performances

Asset Class/Region	Index	To 30 March 2012		
		Currency	Month	Year to date
<b>Developed Markets Equities</b>				
United States	S&P 500 NR	USD	3.2	12.4
United Kingdom	FTSE All Share TR	GBP	-0.9	6.1
Continental Europe	MSCI Europe ex UK NR	EUR	0.2	9.5
Japan	Topix TR	JPY	3.3	18.5
Asia Pacific (ex Japan)	MSCI AC Asia Pacific (ex Japan) TR	USD	-2.8	11.3
Global	MSCI World NR	USD	1.3	11.6
<b>Emerging Market Equities</b>				
Emerging Europe	MSCI EM Europe NR	USD	-4.3	19.3
Emerging Asia	MSCI EM Asia NR	USD	-3.2	13.3
Emerging Latin America	MSCI EM Latin America NR	USD	-3.2	14.6
BRICs	MSCI BRIC NR	USD	-6.3	13.8
Global Emerging Market	MSCI EM (Emerging Markets) NR	USD	-3.3	14.1
<b>Bonds</b>				
US Treasuries	JP Morgan United States Government Bond Index TR	USD	-1.0	-1.3
US Treasuries (inflation protected)	Barclays Capital U.S. Government Inflation Linked TR	USD	-1.1	0.8
US Corporate (investment grade)	Barclays Capital U.S. Corporate Investment Grade TR	USD	-1.0	2.1
US High Yield	Barclays Capital U.S. High Yield 2% Issuer Cap TR	USD	-0.1	5.3
UK Gilts	JP Morgan United Kingdom Government Bond Index TR	GBP	-0.8	-2.0
UK Corporate (Investment grade)	BofA Merrill Lynch Sterling Non Gilts TR	GBP	0.0	2.8
Euro Government Bonds	Citigroup EMU GBI TR	EUR	0.2	3.5
Euro Corporate (investment grade)	Barclays Capital Euro Aggregate Corporate TR	EUR	0.9	5.7
Euro High Yield	BofA Merrill Lynch Euro High Yield Constrained TR	EUR	1.3	12.7
Japanese Government	JP Morgan Japan Government Bond Index TR	JPY	0.1	0.3
Australian Government	JP Morgan Australia GBI TR	AUD	0.5	-0.5
Global Government Bonds	JP Morgan Global GBI	USD	-1.1	-0.9
Global Bonds	Citigroup World Broad Investment Grade (WBIG) TR	USD	-0.6	0.9
Global Convertible Bonds	UBS Global Convertible Bond	USD	0.2	8.7
Emerging Market Bonds	JP Morgan EMBI +	USD	-0.2	4.0

Asset Class/Region	Index	To 30 March 2012		
		Currency	Month	Year to date
<b>Property</b>				
US Property Securities	MSCI US REIT TR	USD	5.0	10.4
UK Property Securities	FTSE EPRA/NAREIT United Kingdom TR	GBP	3.5	10.5
Europe ex UK Property Securities	FTSE EPRA/NAREIT Developed Europe ex UK TR	EUR	4.9	9.5
Australian Property Securities	FTSE EPRA/NAREIT Australia TR	AUD	-0.6	7.3
Asia Property Securities	FTSE EPRA/NAREIT Developed Asia TR	USD	-4.7	16.5
Global Property Securities	FTSE EPRA/NAREIT Developed TR	USD	1.2	12.9
<b>Currencies</b>				
Euro		USD	-0.5	2.6
UK Pound Sterling		USD	0.0	2.8
Japanese Yen		USD	-1.6	-6.5
Australian Dollar		USD	-4.1	1.0
South African Rand		USD	-2.9	5.2
<b>Commodities</b>				
Commodities	RICI TR	USD	-2.6	5.2
Agricultural Commodities	RICI Agriculture TR	USD	-0.8	1.9
Oil	ICE Crude Oil CR	USD	0.4	14.9
Gold	Gold index	USD	-6.1	8.6
Hedge Funds	HFRX Global Hedge Fund	USD	0.0	3.1
<b>Interest Rates</b>			<b>Current rate</b>	<b>Change at meeting</b>
United States	13 March 2012	USD	0.25%	-
United Kingdom	5 April 2012	GBP	0.50%	-
Eurozone	4 April 2012	EUR	1.00%	-
Japan	9 April 2012	JPY	0.10%	-
Australia	3 April 2012	AUD	4.25%	-
South Africa	29 March 2012	ZAR	5.50%	-

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