Weekly Review

Week ending 5th August 2011

Equity markets suffered large and well-publicised falls last week. In the US, the S&P 500 index fell by 7.2% on a total return basis. In aggregate, global equities fell by 8.5% during an extremely difficult five days for investors. The losses are attributed in part to recent events in the US and Europe and the faltering response of policymakers to concerns over unwieldy public debt piles, but the clearest causal link can be drawn to the deteriorating outlook for global growth. Yields on 10 year US Treasuries fell by over 20 basis points over the course of the week, as investors sought safe haven assets.

The House of Representatives approved a new debt ceiling bill on Monday evening by 269 votes to 161. In spite of the new bill, Standard and Poor's announced on Friday evening that it was downgrading the US' AAA rating to AA+, with a negative long term outlook (Moody's had previously affirmed the highest rating, albeit at negative outlook). Standard and Poor's highlighted the country's deteriorating longer term debt dynamics and the apparent political intransigence as having been behind its decision. Most commentators are not predicting a significant market reaction to the news. Whilst the decision may impact the cost of funding of some financial institutions, any moves are likely to be at the margin. The US Dollar remains the reserve currency of choice and there are few genuine alternatives to the US debt market.

Italian 10 year yields rose above 6.2% intraday on Tuesday, with Spanish yields similarly rising to 6.4%, as investors signalled the urgency of fresh support. The European Financial Stability Facility in its new expanded guise is unlikely to come into effect before September, as the legal documents are drafted, amended and finally signed by the 17 Eurozone governments. The European Central Bank (ECB) announced on Thursday that it would act in the interim by restarting its bond purchase program, which has lain dormant since March. The Bank's decision to exclude Italian and Spanish bonds from its programme of purchases saw yields on the two country's debt reach new highs on Thursday, prompting rapid revisions to the plan. Italy's government will move to make additional reforms under pressure from the ECB, with the inclusion of a balanced-budget amendment into their constitution. The worry is that more and more investors may be leaving Europe's capital markets, which has implications for aggregate borrowing levels in the future.

The contraction in US output in 2008 was larger than previously estimated according to the Bureau of Economic Analysis, whilst growth in the subsequent years has been slower. Latest estimates suggest the US economy grew by 1.6% in the year to the end of June, a rate which has historically precipitated a fall in output due to declining confidence levels. July's purchasing managers' data for manufacturers in the US came in below consensus at 50.9 versus 54.5 expected, down from 55.3 in June. Such a reading continues to imply expansion, albeit at a lower rate than the market expected. Survey data for non-manufacturing companies was also below consensus, at 52.7 versus 53.5 expected, down from 53.3 in June. US nonfarm payrolls data for July came in ahead of market expectations on Friday, whilst June's figure was also revised higher, providing a brief relief rally which reversed towards the close.

Elsewhere, Japan intervened in the foreign exchange market on Thursday in order to weaken the yen, as the currency moved close to 80 JPY per USD intraday. The moves had been undermining the competitiveness of Japanese exports. Switzerland's central bank similarly cut interest rates in response to the rising exchange value of the franc. As at the time of writing, gold has passed through USD 1,700 per troy ounce, benefiting from its safe haven status.

To reiterate the sentiment of our note to clients on Friday, there are currently many risks to the global economy and we anticipate further periods of volatility ahead. However these problems are well recognised and are being rapidly discounted by markets. There remain areas of strength in the global economy such as the rise of the Asian consumer, and monetary policy in the developed world will remain loose for a long time to come. This may prove to be an excellent opportunity to accumulate positions in the equity of high quality companies at historically low valuations levels and at a time when, financially, the corporate sector has rarely been stronger.

Source: Momentum Global Investment Management Limited / Bloomberg. August 2011

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Returns to 5 August 2011

Asset Class/Region	Index	Currency	Currency returns: Week ending 5 August 2011	Currency returns: Month to date	Currency returns: YTD 2011
Equities					
United States	S&P 500 NR	**USD**	-7.2	-7.2	-3.9
United Kingdom	FTSE All Share TR	**GBP**	-9.6	-9.6	-9.0
Continental Europe	MSCI Europe ex UK NR	**EUR**	-10.5	-10.5	-12.0
Japan	Topix TR	**JPY**	-4.8	-4.8	-9.8
Asia Pacific (ex Japan)	MSCI AC Asia Pacific (ex Japan) TR	**USD**	-8.9	-8.9	-5.6
Global	MSCI World NR	**USD**	-8.5	-8.5	-5.4
Global emerging markets	MSCI World Emerging Markets TR	**USD**	-8.4	-8.4	-8.1
Bonds					
US Treasuries	JP Morgan United States Government Bond Index TR	**USD**	1.1	1.1	5.4
US Treasuries (inflation protected)	Barclays Capital U.S. Government Inflation Linked TR	**USD**	0.3	0.3	10.5
US Corporate (investment grade)	Barclays Capital U.S. Corporate Investment Grade TR	**USD**	0.8	0.8	6.7
US High yield	Barclays Capital U.S. High Yield 2% Issuer Cap TR	**USD**	-1.9	-1.9	4.2
UK Gilts	JP Morgan United Kingdom Government Bond Index TR	**GBP**	1.4	1.4	6.7
UK Corporate (investment grade)	Merrill Lynch Sterling Non Gilts TR	**GBP**	0.6	0.6	6.2
Euro Government Bonds	Citigroup EMU GBI TR	**EUR**	0.5	0.5	0.6
Euro Corporate (investment grade)	Barclays Capital Euro Aggregate Corporate TR	**EUR**	-0.3	-0.3	2.4
Euro High yield	Merrill Lynch Euro High Yield 3% constrained TR	**EUR**	-2.9	-2.9	1.3
Japanese Government	JP Morgan Japan Government Bond Index TR	**JPY**	0.5	0.5	1.5
Australian Government	JP Morgan Australia GBI TR	**AUD**	2.3	2.3	9.1
Global Government bonds	JP Morgan Global GBI	**USD**	-0.2	-0.2	6.1
Global Bonds	Citigroup World Broad Investment Grade (WBIG) TR	**USD**	-0.1	-0.1	6.1
Global Convertible bonds	UBS Global Convertible Bond	**USD**	-5.0	-5.0	-2.4
Emerging Market Bonds	JP Morgan EMBI +	**USD**	0.2	0.2	7.4

Source: Momentum Global Investment Management Limited / Bloomberg. August 2011

Returns to 5 August 2011

Asset Class/Region	Index	Currency	Currency returns: Week ending 5 August 2011	Currency returns: Month to date	Currency returns: YTD 2011
Property					
US Property securities	MSCI US REIT TR	**USD**	-12.4	-12.4	-2.4
UK Property securities	FTSE EPRA/NAREIT United Kingdom TR	**GBP**	-10.4	-10.4	1.1
Europe ex UK Property securities	FTSE EPRA/NAREIT Developed Europe ex UK TR	**EUR**	-12.3	-12.3	-8.6
Australian property securities	FTSE EPRA/NAREIT Australia TR	**AUD**	-4.8	-4.8	-8.6
Asia Property securities	FTSE EPRA/NAREIT Developed Asia TR	**USD**	-6.9	-6.9	-8.7
Global Property securities	FTSE EPRA/NAREIT Developed CR	**USD**	-10.3	-10.3	-4.1
Currencies					
Euro		**USD**	-1.2	-1.2	5.8
Sterling		**USD**	-0.2	-0.2	4.7
Yen		**USD**	-1.7	-1.7	3.3
Australian Dollar		**USD**	-5.0	-5.0	1.8
Rand		**USD**	-2.6	-2.6	-4.0
Commodities					
Commodities	RICI TR	**USD**	-5.1	-5.1	-1.8
Agricultural Commodities	RICI Agriculture TR	**USD**	-0.8	-0.8	-5.8
Oil	Brent Crude Index (ICE) CR	**USD**	-5.9	-5.9	18.8
Gold	Gold index	**USD**	1.9	1.9	17.5

Source: Momentum Global Investment Management / Lipper Hindsight. August 2011.

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