

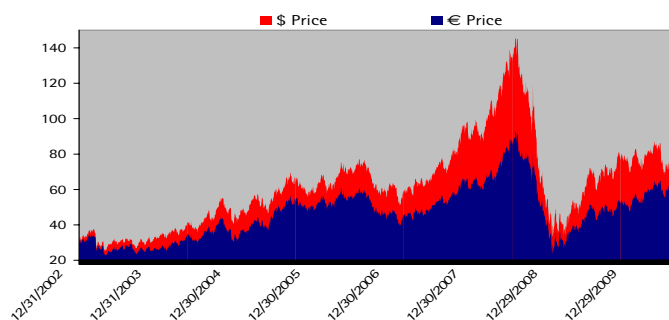
Market Themes

August – 2010

- An element of calm returned to financial markets during the month as bond spreads for peripheral eurozone governments began to tighten steadily. Poor economic data in the US merely encouraged speculation of further help from the monetary authorities, whilst the weakness of the euro has clearly helped the eurozone, where economic indicators showed a dramatic improvement over the course of the month. Global equities had a positive return in July returning 1.9% in Euro terms, (+7.8% year-to-date). The Euro had a strong recovery in July returning 6.7% versus the US dollar as sovereign debt concerns receded.
- Economic data over the month showed a swing in favour of the eurozone, where growth indicators picked up dramatically, particularly for the "core" countries; helped in no small part by the weakness of the euro. Data from the US continued to disappoint, although the data late in the month indicated that the economy, while not as strong as it has been, continues to expand.
- European financials outperformed in July after the Basel Committee announced a relaxation of proposals surrounding capital and liquidity rules. The fact that the majority of European Banks passed the EU stress tests also provided comfort for investors although questions remained over how stringent these tests were.
- At a sector level, the defensive sectors of Healthcare (-5.1% mtd, +1% ytd) and Staples (-0.2% mtd, +11.2% ytd) posted negative returns for the month, while Financials (+4.1% mtd, 7.4% ytd), Telecoms (+2.6% mtd, +6.1% ytd) and Basic Materials (+2.4% mtd, +5.3% ytd) were the better performers.

At a regional level, European markets reversed recent trends and were the best performers in July with a return of +6.2%, (-4.8% ytd), followed by the UK (+5.4% mtd, +3.7% ytd) and Australia (+4.8% mtd, +2.0% ytd). Japan (-2.8% mtd, +11.7% ytd), Hong Kong (-1.6% mtd, +5.4% ytd) and the US (+0.4% mtd, +8.5% ytd) were the laggards in July.

OIL PRICES



- Bond yields in peripheral European bond markets moved lower over the month, helped in part by a number of successful auctions of peripheral government bonds, particularly in Spain. The ECB has slowed its purchases of bonds significantly, making it clear that these purchases will be used to support peripheral markets in times of stress rather than when sentiment is reasonably good.
- Bond yields in the US were little changed on the month while yields in Germany moved marginally higher in July. While spreads in peripheral markets have tightened considerably they remain elevated relative to more normal levels.

Strategy Changes

- Within our equity portfolio we remain overweight Healthcare, Technology and Consumer Staples and underweight Financials, Telecoms and Utilities.
- We remain underweight bonds in our balanced portfolios. Within our bond portfolios, we remain overweight core bond markets and underweight peripheral bond markets.
- Portfolios remain overweight cash.

Market Outlook

- Economic data from the US continued to be softer than expected. European data has been stronger in a large part due to the benefit to European exporters of a lower Euro. The debate will continue on whether the softness in US data indicates a double dip or is in line with a normal slowdown post the initial stages of recovery. For now the data while slower still indicates economic expansion and double dips are a rare phenomenon.
- Equity valuations are attractive for the long-term investor however the volatility witnessed in Q2 is indicative of the risks posed to equity markets from the re-pricing of sovereign risk. While these tensions have eased somewhat in recent weeks they have not gone away and as a result we remain tactically cautious within our asset allocation.