Market Themes

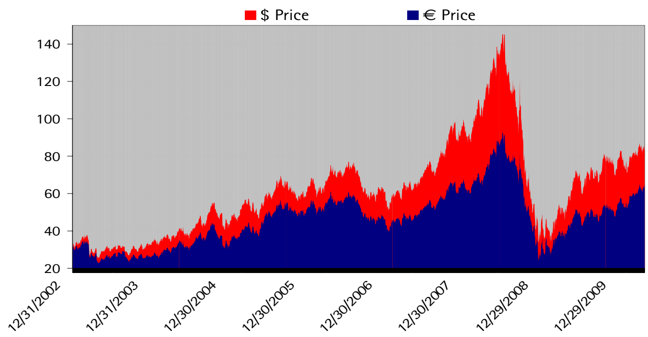
May – 2010

- Sovereign bond markets in the periphery of Europe came under severe pressure during the month as the Greek sovereign debt crisis threatened to spill over into a region-wide problem. This led to pressure on the euro, which fell by 1.6% against the US dollar and Eurozone equity markets which underperformed other equity markets by a significant degree. The global equity market however ended the month in positive territory (+2.3% on the month, +11.6% year-to-date in euro terms).

- At a regional level, the contagion from Greek bond market concerns pushed the DJ Euro Stoxx lower by 2.8% on the month (-2.0% year-to date). Elsewhere, in the UK the FTSE rose by 0.3% on the month (+4.8% year-to-date) and Emerging Markets rose by 1.8% on the month (+9.4% year-to-date), while the S&P 500 (+3.5% on the month, +14.9% year-to-date) and Canada (+3.3% on the month, +15.5% year-to-date) led the way higher.

- At a sector level, Industrials (+4.6% on the month, +18.4% year-to-date), Consumer Cyclicals (+4.3% on the month, +18.3% year-to-date) and Energy (+4.0% on the month, +8.8% year-to-date) led the way, whilst defensive sectors such as Telecoms (+0.2% on the month, +2.8% year-to-date) and Healthcare (-1.3% on the month, +6.8% year-to-date) lagged.

OIL PRICES



- Bond yields in Europe showed a wide divergence during the month, with yields on peripheral government bonds significantly higher, whilst a flight to quality drove yields on "core" Eurozone government bonds lower.

Strategy Changes

- Within our equity portfolios at a sector level we have reduced our underweight position in Consumer Cyclicals (though we remain underweight), further reduced our underweight in Financials and reduced our overweight in Consumer Staples.

- At a regional level, we have increased our exposure to Emerging Markets.

- We remain overweight Energy, Healthcare and Technology and underweight Financials, Telecoms and Utilities.

- We remain underweight bonds in our balanced portfolios.

Market Outlook

- The economic recovery currently underway is real and stronger than is currently priced by financial markets in general and bond markets in particular. From a valuation perspective equities are close to fair value, with significant operational leverage to the economic recovery, while bonds are expensive considering the growth outlook and the level of sovereign indebtedness.

- Concern about sovereign debt in the periphery of Europe has pushed bond yields of those countries higher while bond yields in Germany and the US have fallen. Whilst we believe that this represents a flight-to-quality move rather than a longer term re-pricing of interest rate expectations, if the crisis goes unresolved it will have a negative impact on growth.

- Technical indictors have been suggesting for some time that equity markets were vulnerable to a set-back. Concerns about sovereign debt in the southern part of Europe have come to the fore in recent weeks and have highlighted the risks posed to the financial markets by very high levels of sovereign debt.