

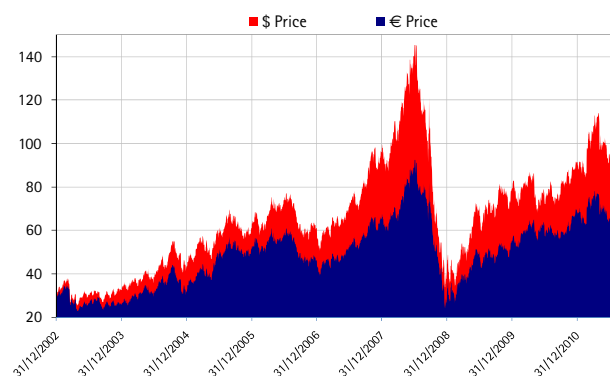
Market Themes

September–2011

- August saw an aggressive sell off in equity markets: the global equity market fell by 7.9% over the month in euro terms (-12.9% year-to-date).
- The sell off was driven by; (i) concerns about global growth in general and US growth in particular, (ii) European sovereign debt concerns, (iii) European bank funding concerns and (iv) a downgrade of US sovereign debt by one of the main rating agencies.
- Bond yields saw significant contraction to the extent that investors are prepared to buy US 10yr bonds offering a negative real yield.
- The macro data confirms that growth has been and is likely to be more anaemic than previously thought by market participants
- The emergence of sovereign debt issues in the Eurozone has forced ECB buying of Italian, Spanish and Irish bonds, leading to a significant yield retrenchment, particularly in Irish bonds where the 10 year yield has fallen from a peak of 14% to less than 9%.
- The slower pace of recovery in the US encouraged the Federal Reserve to loosen policy a little further by putting a time frame on the "extended period" language regarding "exceptionally low levels" of interest rates, committing to keep rates low until "at least though mid-2013".
- The earnings season was generally disappointing relative to expectations and this coupled with the weaker growth outlook means that we are beginning to see downgrades of earnings forecasts.
- Concerns about sovereign debt in Europe inevitably lead to concerns about the debt exposure of European banks, which in turn leads to increased funding stress. The sector fell by 19.9% over the month (-28.7% ytd).

At a broad sector level, energy (-10.7% on the month, -11.3% ytd), financials (-9.9% on the month, -18.8% ytd) and industrials (-9.6% on the month, -15.5% ytd) were the worst performers. Defensive sectors such as utilities (-4.0% on the month, -12.2% ytd), telecoms (-4.5% on the month, -7.7% ytd), and healthcare (-4.6% on the month, -3.3% ytd) outperformed, but nevertheless were in negative territory.

OIL PRICES



European markets were again the worst performers over the month, the EuroStoxx falling by 12.9% (-16.6% ytd). Emerging markets (ex-Japan) were also weak, falling by 9.4% on the month (-15.9% ytd). Canada (-3.6% on the month, -10.3% ytd), Australia (-5.5% on the month, -12.1% ytd), and the US S&P (-5.9% on the month, -10.1% ytd) were the regional outperformers.

Strategy Changes

- All of the above highlight the significant increase in risk aversion by markets. In this regard we have a similar aversion and have adopted a defensive strategy.
- At a sector level we continue to be overweight healthcare and underweight financials. Regionally we have reduced our European exposure and maintain an overweight within Japan.
- Within bonds we maintain an overweight in Irish bonds relative to other peripheral markets, where we remain underweight. We have further increased our exposure to Norwegian government bonds and reduced our exposure to German government bonds.

Market Outlook

- The macro economic data has deteriorated faster than we or the market had expected. Whilst we don't believe that a renewed recession will occur, anaemic growth combined with fiscal constraints in the US and Europe and monetary constraints in China due to high inflation rates mean that the balance of risks to global growth are clearly to the downside.
- We anticipate periods of significant risk aversion and relief over the coming months but think that, until the Eurozone sovereign debt crisis is dealt with in a comprehensive manner and the outlook for US growth improves, risk aversion will prevail notwithstanding the apparent cheapness of equities in general and European equities in particular.
- The sovereign debt crisis in Europe lingers on, with political indecision and an apparent absence of political will to resolve the situation. This uncertainty will continue to cloud the outlook for markets.