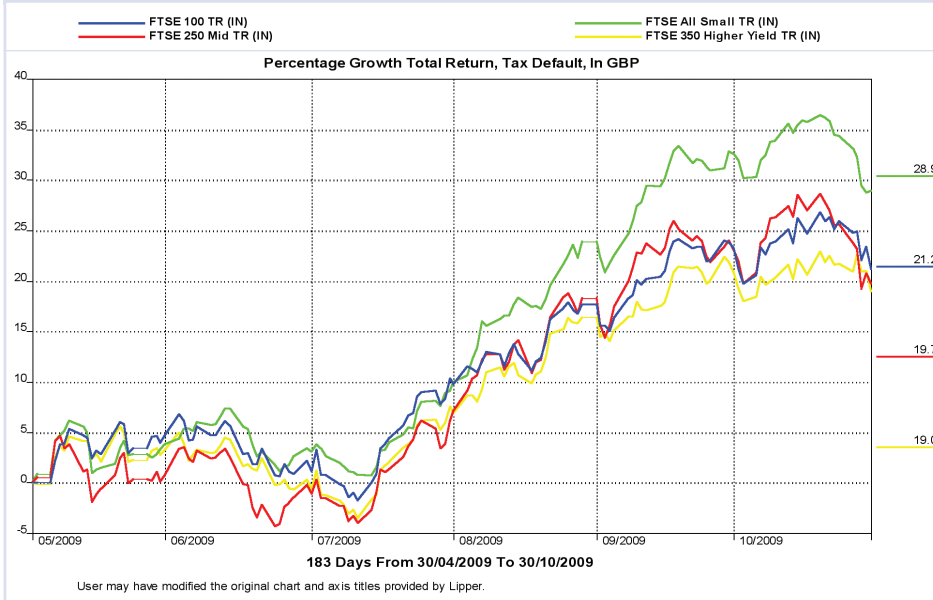


## NOVEMBER 2009

### UK EQUITIES

Contrary to expectations, output in the third quarter of 2009 contracted for the sixth consecutive period, making this the longest recession since records began in 1955. The declines were broad-based – including construction, manufacturing, mining, water, and electricity. GDP is now 5.2% lower than it was at the same time last year, slightly better than the 5.5% year-on-year loss in the second quarter. Although disappointing, these latest figures do see a welcome return to growth in the shorter term – particularly when set beside the 1.5% decline in the second quarter.

The package (most notably the car scrappage scheme and the business tax deferral scheme) and the aggressive monetary actions by the Bank of England have impacted positively on the UK economy. After all, similar actions in the US, Germany and France have encouraged some expansion. Disaster may have been averted but the recovery remains fragile. We may well see some growth imminently as businesses re-stock their inventories – a mirror image of the inventory run-down that saw economic growth contract so sharply. But it begs the question where will sustainable growth come from? With high unemployment, house prices still not stable, tight credit conditions and a high household savings ratio the consumer looks an unlikely source. The necessary regulatory reforms which will almost certainly involve tighter oversight and harsher capital reserve requirements. The government has only a limited arsenal and may, in the worst case, be forced to raise taxes sooner than it would like to. This leaves the Bank of England with a heavy burden.



### US EQUITIES

Following surprisingly strong growth in the third quarter of 2009 it seems likely that the US economy will continue to show signs of recovery in the fourth quarter.

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### EUROPEAN EQUITIES

The Monetary Policy committee at the European Central Bank (ECB) is likely to maintain interest rates at 1% for the foreseeable future. At the press conference in October, Jean Claude Trichet explained that "the latest information further supports our view that the euro area economy is stabilising and is expected to recover at a gradual pace". He cautioned that "the euro area economy is stabilising and is expected to recover at a gradual pace". Little has changed since then and the ECB will continue to support the credit markets by selected purchases of covered corporate debt and providing unlimited liquidity. So far the ECB has been remarkably successful, even though on the face of it, they have been less aggressive than the Bank of England and Federal Reserve. Evidence for this can be seen in the euribor (Euro Interbank Offered Rate) rate which stood at 5.4% this time last year and which now stands at 0.72%.

Loans to households and companies in the euro zone grew at the slowest rate on record in September. Unprecedented levels of liquidity provided by the ECB have led to a surge in real estate and commodities, in the shorter term. In the medium term rising asset prices should encourage risk averse investors away from safer, less productive investment – then a more sustainable recovery may take place, allowing governments in turn to rebuild their own balance sheets.

### JAPANESE EQUITIES

Japanese equities remain in pessimistic territory even after nine consecutive months of improvement – the recovery remains fragile. It is likely that Japanese equities will continue to be in decline.

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