

## MARKET ANALYSIS

### March 2010

During the past 18 months investors have become all too aware of the effects of a company going bust – Lehman Brothers, AIG, Woolworths...the list is long and varied. Previous decades have also witnessed countries defaulting on debt, though these were largely countries with small economies and corrupt political systems. February 2010 posed a new question to investors: what would happen if a developed economy went bust?

The Greek debt ‘problem’ weighed heavily on stock performance in Europe throughout February. Having used currency swaps with artificially low exchange rates to join the Euro in 2001, Greece did not take advantage of the subsequent economic benefits to reduce her debt. Now the intense pressures in servicing this borrowing, has led to fears that the larger European economies, notably France and Germany, would be forced to bail out the Greek economy, and were met with anger by the man in the street in Paris and Berlin. Political and economic leaders worried that the problem could be contagious and fears resurfaced regarding the debt situation in other Eurozone members, especially Italy, Portugal and Spain.

The impact of the Greek tragedy was felt across the globe in early February, as most equity markets suffered sharp falls. However, markets in the US and UK recovered well in the latter half of the month to record gains of 2.5% and 3.1% respectively, despite disappointing job data from the US.

A positive sign for investors came as Prudential announced a massive rights issue in order to purchase AIG’s Asian business, with the bulls taking this as a signal of a return to ‘business as usual’.

Key Data			
	28-Feb	31-Jan	+/(-)%
<b>FTSE 100</b>	5354.52	5188.52	3.1%
<b>Dow Jones</b>	10325.26	10067.33	2.5%
<b>EuroStoxx50</b>	2728.47	2776.83	-1.8%
<b>Nikkei 225</b>	10126.03	10198.04	- 0.7%
<b>Hang Seng</b>	20608.70	20121.99	2.4%
<b>MSCI EM</b>	935.93	933.59	0.3%
<b>Crude Oil</b>	\$79.61	\$72.64	9.6%
<b>£ = \$</b>	1.5248		
<b>€ = \$</b>	1.3621		
<b>£ = €</b>	1.1195		

Interest Rates	
<b>Bank of England</b>	0.5%
<b>European Central Bank</b>	1.0%
<b>US Treasury Reserve</b>	0.25%

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The foreign currency exchange required to fund Prudential's purchase of AIG's Asian business was one of the factors weighing heavily on Pound Sterling, which dropped to a 2010 low against the US Dollar at the month end. With opinion polls pointing towards a possible hung parliament following the general election due in May, and renewed fears that any UK government will need to resume the quantitative easing programme to inflate away its debt, the long term outlook for Sterling appears negative. Some commentators even envisaged the Sterling/US Dollar exchange rate to test \$1.20 in the summer and autumn.

Increased consumer demand supported a rally in the price of Oil which returned to near the \$80 per barrel mark last seen at the end of 2009.

With most of the major economies, with the exception of Australia, indicating that they are unlikely to raise interest rates in the short term, economists remain focused on macro-economic data such as investor sentiment and US job data in March. Particular attention will also be on Greece as it attempts to cut its national debt and any package that is needed to help the country recover.

## UK

Despite record high inflation Mervyn King, the Governor of the Bank of England, failed to rule out further quantitative easing stating that any recovery in the UK was dependant on the global recovery. The GDP estimate for the 4<sup>th</sup> quarter of 2009 was revised upwards to 0.3%, providing some relief to those who had predicted that the UK was technically still in recession.

## EUROPE

Perhaps unsurprisingly, investor sentiment in Europe overall was down in February, the first negative month since April 2009. Drops in sentiment in France, Greece and many of the smaller nations that now make up the European political union were of enough significance to counter the improved sentiment in Germany, the Netherlands and Sweden, and the non-movement of the UK and Belgium.

## US

Investors in the US were listening carefully as Ben Bernanke, the Chairman of the Federal Reserve, gave his testimony to congressional committees at the end of February. He was gloomy about the prospects of the economy in the short term and confirmed that monetary policy would remain 'ultra-loose' for the foreseeable future.

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## ASIA/PACIFIC

Japan was particularly badly hit as equities suffered at the beginning of the month, following revelations that Toyota will need to recall upward of 8.5 million cars. The scandal has severely shaken national confidence in Japan, which prides itself on its excellent track record in manufacturing. Other exporters in Japan also suffered as a result of the temporary drop in confidence in the Japanese brand.

## EMERGING MARKETS

Emerging Markets in Eastern Europe were badly hit as the fall-out from the Greek debt crisis affected investor sentiment, with investors also increasingly wary of potential losses in property ventures in the region. Equities in Russia were particularly badly hit, down over 6%, whilst other emerging markets recorded sluggish growth as investors remained focused on events in developed markets.

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