# Schroders
# Quarterly Markets Review

## Overview of markets in Q2 2009

### Highlights:

- Global equity markets rallied during the quarter as investors focused on optimism that the worst of the global economic downturn may be over. Both the IMF and G7 released more optimistic assessments of the worldwide economic outlook and macro economic data surprised to the upside.
- Data released during the period generally indicated that the global economy is stabilising. For example, consumer and business confidence, retail sales and housing data all showed some improvement at various stages during the quarter. Although global unemployment is still rising at an alarming rate, there were some positive surprises towards the end of the period, particularly in the US.
- Corporate bonds outperformed government bonds as risk appetite increased and investors took advantage of attractively priced credit.
- The oil price rose significantly, on account of signs that the global economic downturn is bottoming out.

### US

US markets rallied significantly since 9 March to 12 June 2009, the announcement of the US Treasury Public Private Investment Program. Positive signs of stabilisation in the economy, including a rise in ISM manufacturing and new orders as well as better-than-expected housing data and durables goods, boosted the equity markets further. In addition, while the unemployment rate continued to rise, recent data was actually better than expected. After 12 June however, concerns over higher mortgage rates and a drop in industrial production and in retail sales all combined to stall the rally. Nevertheless, the S&P 500 still registered its best performance since the fourth quarter of 1998. The Federal Reserve kept interest rates on hold during the quarter.

### Eurozone

European equity markets rallied strongly in the second quarter, with the most beaten down cyclical sectors staging the strongest recovery. Financials in particular outperformed, leaving the traditionally defensive sectors trailing at the end of the quarter. Despite the optimism in equity markets, the economy continued to contract, albeit at a slower pace than anticipated. To help boost economic growth, the European Central Bank (ECB) urged banks to start lending again, citing the record low interest rates (which are expected to remain at current levels for a protracted period) as an incentive for banks to loosen the reins. The request follows continued efforts by the ECB to provide support for the banking system, primarily through unlimited one-year liquidity loans.

### UK

UK equities began the second quarter on very strong form as the view that Armageddon would be avoided increasingly gained traction amongst investors. This extraordinary relief rally only began to fade in early May, at which point the market moved into a more even-handed range-trading pattern that persisted throughout the rest of the period. The overall economic outlook remains bleak, and S&P revised down the UK's outlook to negative from stable during May. On a more positive note, better-than-expected economic news was released, including retail sales, housing and consumer confidence data, which showed signs of significant improvement towards the end of the period. The Bank of England expanded its quantitative easing programme and kept interest rates on hold at 0.5%.

## Japan

The tentative rally that began in March continued strongly throughout most of the quarter as investors focused less on negative data (such as an unprecedented GDP contraction in Q1) and more on indications of the economic downturn easing. The second half of June saw a slight retreat due to concerns that gains may have outpaced the economic recovery. However, the TOPIX still performed very well during the quarter. The oil price rose around 40% over the quarter, boosted by signs of the global economy not worsening and in particular by recovering demand from China. Outperforming sectors were mostly cyclicals and those benefiting from stronger commodity prices. Defensives tended to be left behind amid market optimism.

## Asia (ex Japan)

Rising hopes for an economic recovery drove Asian equities significantly higher in the second quarter as investors returned to risk assets, shrugging off negatives including nuclear tests by North Korea and renewed fears of swine flu. Cyclicals led the rebound, powered by the bottoming out of global lead indicators of activity and strong liquidity conditions created by unprecedented effort government efforts to reflate the economies in the West and closer to home, massive fiscal stimulus measures initiated by Beijing. The more defensive utilities and telecom sectors lagged.

## Emerging Markets

Emerging markets delivered strong returns during the quarter against a background of improving risk appetite and confidence that the worst of the global economic downturn may be over. Other positives included the announcement from the G20 summit of an increase in the IMF’s resources. During the quarter, the Indian market posted strong returns, rising sharply on news of the Congress party’s unexpectedly decisive victory in the country’s parliamentary elections in May, which is set to give the party a freer hand in pursuing its pro-growth/pro-reform policies. The Indonesian market also performed strongly, benefiting from the central bank continuing to cut interest rates and a relatively benign political outlook following parliamentary elections. Hungary delivered very strong returns, gaining from the strengthening of risk appetite. Although the Korea market delivered a strong absolute return, it underperformed with concerns over tensions with North Korea weighing on sentiment.

## Global Bonds

Although the second quarter has witnessed a tentative pick up in global economic data, the overall macroeconomic situation remained weak. While consumer confidence has improved, many leading indicators have just deteriorated less rather than registering any meaningful improvement. Meanwhile, worldwide unemployment is rising at an alarming rate, and the US housing market continues to contract. Global government bonds fell due to fears over increasing levels of supply. Credit outperformed government bonds as risk appetite increased and investors took advantage of very attractive yield spreads as they started to believe that the current downturn is unlikely to deepen into a 1930s style depression.

## Overview – Total Returns (%) – to end of June 2009

| | 3 months | | | YTD | | |
|---|---|---|---|---|---|---|
| **Equities (MSCI)** | **EUR** | **USD** | **GBP** | **EUR** | **USD** | **GBP** |
| World Index | 14.58 | 21.05 | 5.36 | 5.83 | 6.79 | -6.77 |
| World Value Index | 16.99 | 23.59 | 7.57 | 3.20 | 4.13 | -9.09 |
| World Growth Index | 12.45 | 18.79 | 3.39 | 8.46 | 9.44 | -4.46 |
| World Smaller Companies Index | 21.44 | 28.30 | 11.66 | 13.98 | 15.00 | 0.40 |
| US | 9.70 | 15.89 | 0.87 | 2.80 | 3.73 | -9.44 |
| Eurozone | 19.97 | 26.74 | 10.31 | 3.71 | 4.64 | -8.64 |
| UK | 19.83 | 26.60 | 10.18 | 12.07 | 13.08 | -1.28 |
| Japan | 16.48 | 23.05 | 7.10 | 1.75 | 2.67 | -10.37 |
| Emerging Markets | 27.64 | 34.84 | 17.36 | 35.01 | 36.22 | 18.93 |
| Asia ex Japan | 27.77 | 34.98 | 17.48 | 34.65 | 35.87 | 18.62 |

| | 3 months | | | YTD | | |
|---|---|---|---|---|---|---|
| **Government bonds (JP Morgan)** | **EUR** | **USD** | **GBP** | **EUR** | **USD** | **GBP** |
| US | -8.36 | -3.19 | -15.74 | -5.43 | -4.58 | -16.70 |
| UK | 7.33 | 13.39 | -1.31 | 11.18 | 12.18 | -2.06 |
| Japan | -2.75 | 2.74 | -10.58 | -7.20 | -6.36 | -18.25 |
| Germany | -0.80 | 4.80 | -8.79 | -0.26 | 0.64 | -12.14 |
| **Corporate bonds (Merrill Lynch)** | 4.90 | 10.82 | -3.55 | 8.25 | 9.23 | -4.64 |

Source: Datastream to 30 June 2009

### Important Information:

**For professional investors and advisers only. This document is not suitable for retail clients.**