

Schroders

Monthly Markets Review

Overview of markets in July 2009

Highlights:

- Global equity markets rallied in July, buoyed by optimism about the potential for global recovery and US second quarter earnings results that were generally better than expected. Although the weakness seen in late June persisted through the first week or so of July, global markets then resumed their upward trajectory and many indices hit new highs for the year.
- US economic data was mixed, although hopes that the global economy might have turned the corner were restored by a better-than-expected corporate earnings season, in which many companies announced bullish outlooks. Economic data also improved later in the month and President Obama, among others in the administration, made cautiously optimistic comments about a recovery.
- Corporate bonds outperformed government bonds as risk appetite remained resilient and investors took advantage of attractively priced credit.

US

US equities regained their strength after a brief lull in late June amid further signs of stabilisation in the economy. Initially, investor concerns about the strength of the recovery clouded sentiment, as US economic data was mixed, with house sales and manufacturing output showing moderate improvement, but weak prints coming from the labour market, retail sales and consumer confidence. For example, the number of job losses accelerated, and was worse than most analysts expected, with the unemployment rate rising 0.1% to 9.5%. However, hopes of an economic recovery were evident, following better-than-expected earnings results. Risk appetite increased and cyclicals led the equity market higher, with defensives lagging but still generating positive returns.

Eurozone

Eurozone equity markets lost momentum at the beginning of July before bottoming out and staging another strong rally to reach an eight month high. Sentiment was buoyed by mainly positive corporate earnings reports and some encouraging economic data. For example, the eurozone manufacturing PMI index rose more than expected, although it is still contracting, albeit at a less severe pace. In addition, industrial production, consumer confidence and German unemployment and business confidence data surprised to the upside. The European Central Bank left interest rates on hold at 1.0% as expected in July, but indicated that they would lower borrowing costs further if there was renewed economic weakness and/or signs of deflation.

UK

Equity markets picked up once again in July, helped by renewed growth in China, encouraging signs on the US housing market and positive corporate earnings news from the US and UK. In fact, with UK companies, in the main, proving able to surprise on the upside (given some fairly low expectations amongst analysts), the UK market embarked on another significant rally and



consequently broke out of its trading range. The Bank of England kept interest rates on hold in July, as the market expected. There were a number of positive data releases. Halifax and Nationwide reported better-than-expected housing data and consumer spending and retail sales remained resilient. On a more negative note, second quarter GDP was disappointing, contracting 0.8% quarter-on-quarter.

Japan

The Japanese market delivered a positive return in July against a background of a continuing global equity market rally. US economic data was mixed, although it improved towards the end of the month. A similar story played out in Japan. Macro data was mostly quite weak although bright spots included a fourth consecutive month-on-month improvement in industrial production and a further upgrade of the government's official economic outlook. Later in the month, strong performance from US indices boosted the Japanese market and the earnings season in Japan also lifted sentiment. Positive surprises outnumbered negative by some margin, as the effects of many companies' cost-cutting efforts started to show through.

Asia (ex Japan)

After a weak start to the month, Asian equities regained their strength following largely positive economic data and earnings results. This included word that the South Korean economy had accelerated to the fastest pace in six years on higher exports and household spending and that China was on track to reach its 8% growth target this year following increased government spending and a surge in bank lending in the second quarter. The rally was further sustained in the wake of better-than-expected earnings numbers, which triggered a number of broker upgrades. As with previous months, cyclicals continued to lead the gains, particularly oil and metals related companies, as commodity prices rose over the month while the more traditionally defensive sectors trailed but still generated positive returns. It was the fifth straight month of gains for the region.

Emerging Markets

Emerging markets delivered strong returns during the month and outperformed global equities, gaining from investors' improved appetite for risk. Poland and Indonesia were the best performing emerging markets over the month. The Polish market was boosted by strong returns from banking stocks. In Indonesia, positives included confirmation that President Yudhoyono won re-election in the first round of voting while the country's central bank continued to cut interest rates. Turkey and Korea were also among the strongest performing emerging markets. The Turkish central bank continued to cut interest rates and suggested that there may be room for further easing. Korea is a likely beneficiary of an expected recovery in global activity - over the month data was released showing GDP growing by 2.3% quarter-on-quarter in the second quarter and industrial production increasing by 5.7% month-on-month in June (the latter was ahead of consensus expectations).

Global Bonds

Early in the month, economic reports showed little more than a slowing in the rate of decline and there were fears that the production boost from restocking and the massive global stimulus could not be sustainable in the long term. Furthermore, structural concerns over the global economy remained. For example, high and rising unemployment rates in the US and eurozone continued to weigh on consumer confidence and demand. However, economic data improved later in the month, fuelling hopes that the economy was on the mend. Against this background, global government bonds rose, despite persistent concerns over increasing levels of supply. Nevertheless corporate

bonds continued to outperform government bonds as risk appetite remained strong, with investors taking advantage of attractive yield spreads.

Overview – Total Returns (%) – to end of July 2009

| | 1 month | | | YTD | | |
|--|---------|-------|-------|-------|-------|--------|
| | EUR | USD | GBP | EUR | USD | GBP |
| Equities (MSCI) | | | | | | |
| World Index | 7.34 | 8.50 | 7.78 | 13.60 | 15.87 | 0.48 |
| World Value Index | 8.00 | 9.17 | 8.44 | 11.46 | 13.68 | -1.42 |
| World Growth Index | 6.68 | 7.83 | 7.12 | 15.70 | 18.01 | 2.34 |
| World Smaller Companies Index | 7.65 | 8.81 | 8.09 | 22.69 | 25.13 | 8.52 |
| US | 6.39 | 7.54 | 6.82 | 9.37 | 11.55 | -3.26 |
| Eurozone | 9.56 | 10.75 | 10.02 | 13.63 | 15.89 | 0.51 |
| UK | 8.10 | 9.27 | 8.54 | 21.14 | 23.56 | 7.15 |
| Japan | 3.16 | 4.28 | 3.59 | 4.97 | 7.06 | -7.15 |
| Emerging Markets | 10.13 | 11.32 | 10.58 | 48.68 | 51.64 | 31.51 |
| Asia ex Japan | 11.89 | 13.10 | 12.35 | 50.66 | 53.66 | 33.26 |
| | | | | | | |
| | 1 month | | | YTD | | |
| Government bonds (JP Morgan) | EUR | USD | GBP | EUR | USD | GBP |
| US | -0.66 | 0.42 | -0.25 | -6.05 | -4.18 | -16.90 |
| UK | -1.21 | -0.14 | -0.80 | 9.84 | 12.03 | -2.85 |
| Japan | 0.08 | 1.16 | 0.49 | -7.13 | -5.28 | -17.85 |
| Germany | 1.17 | 2.26 | 1.58 | 0.91 | 2.92 | -10.74 |
| Corporate bonds (Merrill Lynch) | 2.84 | 3.95 | 3.26 | 11.32 | 13.54 | -1.53 |

Source: Datastream to 31 July 2009

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