

Schroders

Monthly Markets Review

Overview of markets in November 2009

Highlights:

- Most global equity markets rose in November as economic news continued to support the recovery theme. US third quarter GDP growth, however, was revised down from 3.5% to a still strong 2.8% on an annualised basis. The main cause of the revision was less robust gains in consumer spending, although news from other sectors of the economy was quite encouraging. Economic data from China confirmed that their recovery continued apace.
- The US market outperformed on a global basis, although emerging markets were also strong. Japanese share prices fell as analysts priced in reduced export competitiveness due to ongoing currency strength. At the end of the month, however, global markets were volatile as the Dubai government announced a debt restructuring of Dubai World, one of its holding companies, and there were fears that Dubai would default on billions of dollars of debt from banks around the world.
- The US dollar continued to weaken, nudging up commodity prices and driving a rush to gold, which hit new highs during the month.
- Investors continued to be lured back into the credit market with the opportunity to buy high quality bonds very cheaply and corporate bonds outperformed government bonds and cash.

US

US equity markets put in a strong showing in November, despite the headwind of a depreciating currency. Investors were cheered by the G20's commitment to ongoing policy stimulus as well as economic news, which continued to provide impetus to the recovery theme. This included a much better-than-expected rise in the ISM manufacturing index and growing confirmation of a recovery in the housing market with new homes sale picking up. Evidence of a rebound in retail sales provided an additional boost. However, questions about the true strength of the recovery persisted with October's employment report proving, on balance, disappointing, and consumer sentiment falling for a second month on job concerns. News that state-owned Dubai World was seeking to delay repayment on much of its \$59 billion worth of debt took the shine off the gains at the end of the month; however, stocks recovered quickly and the market ended the month significantly higher.

Eurozone

The positive trend in earnings and economic data, particularly the reduction in US jobless claims and better-than-expected worker productivity, helped to improve sentiment at the beginning of November and the re-emerging risk appetite fuelled a rally in eurozone equity markets. However, before the month drew to a close, growing uncertainty about the prospects for global economic growth unsettled markets. The impact of the Dubai debt situation further weighed on eurozone equities in the final days of the month. Banks in particular suffered some of the biggest losses as the market contemplated the potential debt exposure of the region's banks. Miners were the stand out performers, along with industrial stocks and the more defensive sectors such as healthcare, consumer staples and telecom services.



UK

UK equities had a positive month in November, continuing the relatively straight-line increase seen since early March. The FTSE 100 pushed through the 5,300 level, before dropping back towards the end of the month on concerns about Dubai's credit status. Mining companies, in particular, performed well, continuing to benefit from significant emerging markets demand. We believe aftershocks like these are to be expected, however, and serve to reinforce our belief that policymakers will keep interest rates low for some time to come. In terms of economic news, third quarter GDP was revised upward to -0.3% quarter-on-quarter, from -0.4% on the preliminary estimate, as the market expected. Industrial production was revised downwards and services output was revised upwards. CPI inflation accelerated to 1.5% year-on-year (yoy) in October, which was mainly due to higher petrol prices. The Bank of England (BoE) left policy rates at 0.5% and extended quantitative easing by £25 billion to £200 billion, which was less than forecast. The BoE's most recent statement was more upbeat, noting the continuing improvement in the economy.

Japan

The Japanese market lagged global equity markets and finished down in yen terms. Sentiment in Japan remained downbeat, dominated by two concerns. The yen appreciated further, hitting a 14-year high against the dollar as investors moved to diversify out of the US currency. Dilution worries also continued as several companies announced equity offerings (including Mitsubishi UFJ, Hitachi and T&D Holdings) and many more are expected to do so. The Japanese economy saw its highest GDP growth in two years in the third quarter. However, concerns about deflation were intensified by falls in demand indices and a negative reading for core CPI for the eighth consecutive month. Against the background of mounting risk aversion, defensives tended to do well (including land transport, telecoms, foods and pharmaceuticals). Electric power & gas was also boosted by some strong profit reports from companies within the sector. Encouraging earnings and merger talk helped the insurance sector outperform, while speculation around the new government reversing tight regulations boosted consumer finance firms. Export-oriented sectors were hit by the stronger yen, including electric appliances and rubber products. In addition, the oil & coal sector suffered from profit-taking and a string of analyst downgrades.

Asia (ex Japan)

Asian markets eked out modest gains in November, following slight losses in the previous month. Equities were helped by the G20's commitment to the ongoing policy stimulus and a decline in the trade-weighted US dollar, although some gains were erased in late November, when stocks fell on concerns of a possible default by Dubai World's property development subsidiary Nakheel. However, the shock to the markets was quickly stemmed and investors' fears eased as the United Arab Emirates central bank moved to provide emergency liquidity to its banking system. Over the month, the Indian, Philippines and Singapore markets delivered the best relative performance in US dollar terms. Conversely, Hong Kong, Thailand and Korea saw the worst relative performance. Across sectors, materials, consumer staples and technology stocks led the rally while telecommunication services, utilities and industrials trailed.

Emerging Markets

Emerging market equities marginally outperformed global equity markets during the month, with stronger commodity prices proving beneficial. Peru and Mexico were the best performing emerging markets in November. The commodity-driven Peruvian market benefited from an increase in copper prices. Mexico outperformed, despite rating agency Fitch downgrading its sovereign debt rating to BBB. The Mexican market was buoyed by evidence of domestic economic recovery, with the release of third quarter GDP data that was better than consensus expectations. Poland, India and Brazil also

outperformed. In Poland, data was released showing GDP growth accelerating to 1.7% yoy in the third quarter, which was above consensus expectations. The Indian market benefited from further evidence of strong domestic growth momentum, with industrial production growth in September coming in well ahead of consensus expectations at 9.1% yoy. Brazil benefited from higher commodity prices and the strong performance of banking and telecoms stocks. Egypt was the weakest performing emerging market by a wide margin, with Dubai-related concerns having a large negative impact at the end of the month. Turkey also underperformed despite the country's central bank continuing to ease monetary policy (it reduced interest rates by 25 basis points).

Global Bonds

The global economy continued its recovery, although there was a mixed set of economic reports from the US. Positive surprises were seen in home sales and the purchasing managers' index, but data on bank lending and consumer confidence highlighted weakness in the recovery. Unemployment rose above 10% for the first time in over 25 years, but high frequency data suggested that the rate of job losses was slowing.

Corporate bonds outperformed government bonds and cash, as investors continued to purchase high quality bonds at very cheap prices. Furthermore, the continuation of broadly positive economic data continued to fuel investor risk appetite, although this was dampened during the second half of the month primarily due to the threat of default in Dubai World, the Middle Eastern state's flagship holding company. Global government bond performance was supported by lingering concerns over the strength and pace of the worldwide economic recovery.

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

| | 1 month | | | YTD | | |
|--|---------|-------|-------|-------|-------|--------|
| | EUR | USD | GBP | EUR | USD | GBP |
| Equities (MSCI) | | | | | | |
| World Index | 2.35 | 4.14 | 4.60 | 18.93 | 28.45 | 12.53 |
| World Value Index | 2.23 | 4.02 | 4.48 | 17.02 | 26.38 | 10.72 |
| World Growth Index | 2.47 | 4.26 | 4.72 | 20.78 | 30.44 | 14.27 |
| World Smaller Companies Index | 0.63 | 2.39 | 2.84 | 28.12 | 38.37 | 21.23 |
| US | 4.13 | 5.95 | 6.42 | 15.35 | 24.58 | 9.14 |
| Eurozone | 1.64 | 3.42 | 3.88 | 21.71 | 31.45 | 15.16 |
| UK | 1.14 | 2.91 | 3.36 | 29.36 | 39.70 | 22.39 |
| Japan | -2.73 | -1.03 | -0.59 | -2.25 | 5.57 | -7.51 |
| Emerging Markets | 2.51 | 4.30 | 4.76 | 59.45 | 72.20 | 50.86 |
| Asia ex Japan | 0.93 | 2.69 | 3.15 | 53.10 | 65.34 | 44.86 |
| | | | | | | |
| | 1 month | | | YTD | | |
| Government bonds (JP Morgan) | EUR | USD | GBP | EUR | USD | GBP |
| US | -0.30 | 1.45 | 1.90 | -8.45 | -1.12 | -13.38 |
| UK | -1.22 | 0.51 | 0.95 | 7.52 | 16.12 | 1.73 |
| Japan | 4.15 | 5.97 | 6.44 | -1.79 | 6.07 | -7.08 |
| Germany | 1.02 | 2.79 | 3.25 | 2.85 | 11.08 | -2.69 |
| Corporate bonds (Merrill Lynch) | -0.33 | 1.42 | 1.87 | 12.01 | 20.97 | 5.98 |

Source: Datastream to 30 November 2009

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