

# Schroders

## Quarterly Markets Review

### Overview of markets in Q3 2009

#### Highlights:

- Global equity markets continued to generate very strong returns during the third quarter of 2009 due to a combination of improving economic data, increased risk appetite and continued investor inflows into equities.
- There were further indications of a global economic recovery, with many major countries likely to return to positive growth in Q3 2009. The principal engine of this recovery is industry, where output is ramping up quickly in response to the restocking of rapidly depleted inventories. GDP data released in mid-August showed that both the French and German economies had already officially emerged from recession in Q2 2009, with both economies reporting growth of 0.3% for the period. Stronger exports and consumer spending – helped by government stimulus measures – led this rebound in Europe.
- Corporate bonds generated positive returns, due to better-than-expected economic data, outperforming government bonds and cash.
- The oil price traded sideways during the quarter, rising and then falling towards the end of the period due to concerns over demand from China.

#### US

The US equity market, as measured by the S&P 500 Index, had its strongest quarter for over a decade. Economic data turned positive, with lead indicators continuing to rebound from the very low levels seen earlier in the year. There were improvements in ISM manufacturing, GDP estimates and housing. However, unemployment and consumer spending still remain concerns, even though the US government has taken initiatives such as the 'cash for clunkers' scheme. Positive earnings revisions have helped support share price gains, as a number of companies have reported the beneficial impact of earlier cost cuts and generally better operating environments. Several US banks announced moves to leave behind government support in one way or another – repaying TARP funds, reducing a government ownership stake or exiting the asset guarantee program.

#### Eurozone

Improved sentiment and increased risk appetite continued to support European equity market gains during the quarter. Cyclical names within the financials, industrials and materials sectors led the charge, once again - those companies that were the most operationally geared into the economic recovery - along with companies in industries that have been supported by short-term government initiatives (e.g. autos). The European Central Bank is expected to keep interest rates on hold at a record low of 1.0%. The central bank also launched its second-round offer of unlimited one-year liquidity to eurozone banks, although future demand for credit is likely to remain muted as banks continue to improve their capital ratios.



## UK

UK equities rallied strongly during the third quarter as a variety of factors underpinned a continued improvement in risk appetite. Corporate news in the US and UK provided one element of support, as the evasive cost cutting action taken in previous quarters fed through to a generally better-than-expected earnings season. In addition, there was evidence of an improvement in economic conditions, hopes of a resumption in M&A and, all the while, high demand for placings, which highlighted a growing appetite for shares and proved to be self-reinforcing. The Bank of England left interest rates on hold at 0.5% during the quarter, and in August, it decided to extend its quantitative easing programme by a further £50 billion.

## Japan

Despite a renewed rally from mid-July to mid-August, the prevailing mood over the quarter was one of retrenchment, and the TOPIX finished down in yen terms. Investors became concerned that stock markets may have outpaced what is proving to be a tentative economic recovery. Further uncertainty was introduced by the general election, which ended the long period of rule by the Liberal Democratic Party, and the policies of the new government. Against this background, defensives performed well (foods, pharmaceuticals and telecoms), as did some cyclical sectors benefiting from global restocking demand (electric appliances, rubber products). Financials suffered amid further regulatory and political noise.

## Asia (ex Japan)

Investors' confidence of a global economic recovery continued to strengthen in the third quarter, lifting Asian equities higher. This was despite ongoing speculation that Beijing would adjust its easy monetary policy stance, which caused regional markets to pull back during August amid fears that this would derail the recovery in China and abroad. As a result of this, China and Hong Kong markets were the key laggards over the quarter while Indonesia and Korea were the best performers. Across sectors, cyclicals within the technology, consumer discretionary and material sectors continued to lead the gains. The defensive healthcare and consumer staples sectors also put in a strong showing, though telecoms and utilities lagged.

## Emerging Markets

Emerging markets generated impressive returns during the quarter, outperforming global equity markets, as they benefited from investors' increasing appetite for risk assets. In Latin America, Peru, Colombia and Brazil delivered the best returns, with the central banks in each country reducing interest rates. In other developments, rating agency Moody's upgraded Brazil's sovereign debt rating to investment grade. In Asia, Indonesia and Korea were among the strongest performers. In Indonesia, positives included confirmation that President Yudhoyono won re-election in the first round of voting, while the country's central bank cut interest rates. Korea is seen as a likely beneficiary of an expected recovery in global activity. In Europe, Hungary and Poland posted the best performance. Hungarian equities benefited from its central bank cutting interest rates while in Poland, better-than-expected data was released for second-quarter GDP.

## Global Bonds

The global economy showed signs of recovery during the third quarter of 2009. For example, global business and consumer confidence generally improved. In addition, US industrial production was stronger than expected in August, and the US also saw an encouraging decrease in the rate of job losses.

Due to this better-than-expected economic data, credit performed particularly well in September following more muted returns in August, and outperformed government bonds and cash over the quarter. Global government bonds also generated positive returns, despite continuing concerns over increasing levels of supply. Government bonds were supported by fears over the strength and sustainability of the global recovery.

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

	3 months			YTD		
	EUR	USD	GBP	EUR	USD	GBP
<b>Equities (MSCI)</b>						
World Index	12.81	17.57	21.06	19.40	25.55	12.86
World Value Index	14.96	19.81	23.36	18.64	24.76	12.15
World Growth Index	10.66	15.33	18.75	20.03	26.21	13.46
World Smaller Companies Index	17.37	22.31	25.95	33.77	40.66	26.45
US	10.92	15.59	19.03	14.03	19.91	7.79
Eurozone	20.76	25.85	29.59	25.24	31.69	18.39
UK	13.74	18.53	22.05	27.46	34.03	20.49
Japan	2.26	6.57	9.73	4.05	9.41	-1.64
Emerging Markets	16.14	21.04	24.63	56.80	64.88	48.22
Asia ex Japan	14.32	19.13	22.67	53.93	61.86	45.51
	3 months			YTD		
<b>Government bonds (JP Morgan)</b>	EUR	USD	GBP	EUR	USD	GBP
US	-1.94	2.19	5.22	-7.27	-2.49	-12.34
UK	-3.83	0.22	3.20	6.92	12.43	1.07
Japan	4.18	8.57	11.79	-3.32	1.66	-8.61
Germany	2.11	6.41	9.57	1.85	7.10	-3.72
<b>Corporate bonds (Merrill Lynch)</b>	3.94	8.32	11.54	12.52	18.32	6.36

Source: Datastream to 30 September 2009

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