

## Risk aversion continues as tensions rise in the Eurozone

8 February 2010\*

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\*All data to week ending 5 February 2010  
unless otherwise stated

### NEWS

- Global risk assets suffered for the fourth straight week amidst continuing fears surrounding the potential for sovereign defaults. Equities, commodities, emerging market currencies and external debt were among the asset classes that came under selling pressure despite significant disparities in their underlying fundamentals.
- The Bank of England decided not to increase its quantitative easing (QE) programme past £200bn, preferring a 'wait and see' approach. The Monetary Policy Committee members felt the 0.1% increase in fourth quarter GDP signalled enough of a recovery to temporarily halt QE.
- A commission of experts in Athens told the country's Parliament that it had uncovered €40bn of hidden debts during an investigation into past manipulation by the financial authorities. The ratings agencies consequently downgraded Greek bonds.
- British house prices are set to rise 6% this year according to the Centre for Economics and Business Research. The strength of the upturn has taken many economists by surprise.
- Jean-Claude Trichet, the President of the European Central Bank warned that the world economy could face a catastrophe unless leaders find common ground in their plans to redesign the regulation of the financial sector.
- Food price inflation fell in January for the first time in five months, helping to curb the effect of the increase of VAT, according to the British Retail Consortium. The price of food rose at an annual 2.9% in January, down from 3.7% in December.

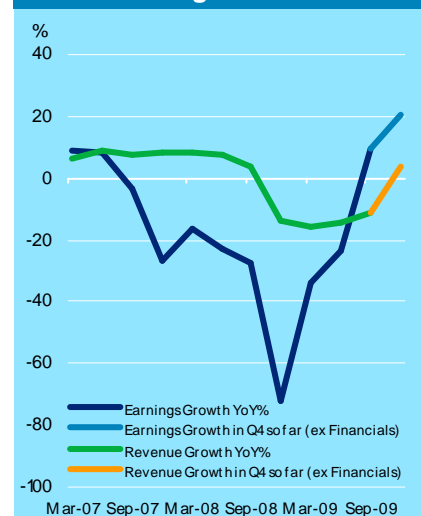
### VIEWS

- Low interest rates, government spending, falling inflation and a stabilising labour market should allow growth to continue to improve until mid-2010.
- Improving economic growth, rising inflation, normalising interest rates and heavy issuance will send government bond yields higher in 2010.
- The dollar could continue to appreciate on the back of solid US data during the first half of 2010, but the path of least resistance for the dollar remains down in the longer term.
- Despite an attractive valuation, sterling will struggle against most G10 and emerging market currencies until there is more clarity on the UK government's fiscal position.
- We believe the equity market rally will continue during the first half of 2010 on the back of positive earnings growth and continued positive surprises in both industrial production and household consumption data.

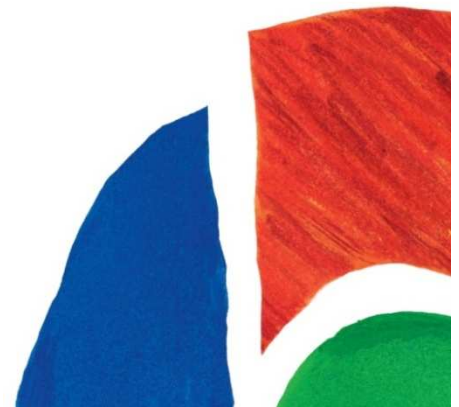
### THIS WEEK

- Focus will lie with the mining sector as Xstrata, BHP Billiton and Rio Tinto announce fourth quarter results.
- The Bank of England will post the keenly awaited inflation report on Wednesday; it may change assumptions about UK interest rates. The majority believe UK rates will remain unchanged for most, if not all of the year, but inflation problem signals could quickly change this view.

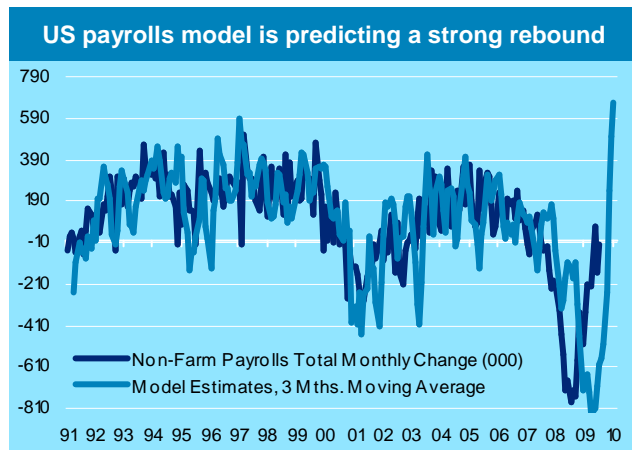
### Are companies seeing top line growth?



Source: Datastream, as at 5 February 2010



## ECONOMIC DATA



Source: Datastream, Henderson Global Investors, as at 5 February 2010

| GDP Growth %  | 2009 | 2010* | 2011* |
|---------------|------|-------|-------|
| US            | -2.5 | 2.9   | 3.1   |
| Japan         | -5.4 | 1.3   | 1.5   |
| Eurozone      | -3.9 | 1.3   | 1.6   |
| UK            | -4.7 | 1.5   | 2.2   |
| G7            | -3.6 | 2.0   | 2.2   |
| Asia ex Japan | 5.2  | 7.8   | 7.4   |
| World         | -2.2 | 3.0   | N/A   |

| Inflation %   | 2009 | 2010* | 2011* |
|---------------|------|-------|-------|
| US            | -0.3 | 2.2   | 1.9   |
| Japan         | -1.3 | -1.0  | -0.3  |
| Eurozone      | 0.3  | 1.2   | 1.5   |
| UK            | 2.1  | 2.4   | 1.7   |
| G7            | 0.0  | 1.4   | 1.5   |
| Asia ex Japan | 1.8  | 3.6   | 3.7   |
| World         | 1.4  | 2.6   | N/A   |

| Bond Indices                     | 29 Jan | 5 Feb | % cge     |
|----------------------------------|--------|-------|-----------|
| FTA Government Stocks            | 2304   | 2308  | 0.2       |
| FTA Index-Linked                 | 2484   | 2481  | -0.1      |
| JP Morgan Global Govt Bond Index | 538    | 551   | 2.4       |
| 10-year Bond Yield (%)           | 29 Jan | 5 Feb | Dec 2010* |
| UK                               | 4.00   | 3.98  | ↑↑↑       |
| US                               | 3.59   | 3.57  | ↑↑↑       |
| Eurozone                         | 3.19   | 3.11  | ↑         |
| Japan                            | 1.31   | 1.36  | ↑         |

| Other                       | 29 Jan | 5 Feb | June 2010** |
|-----------------------------|--------|-------|-------------|
| Interest Rates (%)          |        |       |             |
| UK                          | 0.50   | 0.50  | 0.50        |
| US                          | 0.25   | 0.25  | 0.25        |
| Eurozone                    | 1.00   | 1.00  | 1.00        |
| Japan                       | 0.10   | 0.10  | 0.10        |
| Currencies & Commodities    | 29 Jan | 5 Feb | Dec 2010**  |
| £/€                         | 0.87   | 0.87  | ↑           |
| \$/£                        | 1.60   | 1.56  | →           |
| \$/€                        | 1.39   | 1.37  | ↓           |
| ¥/\$                        | 90.7   | 89.4  | ↑           |
| Oil (Brent crude \$/barrel) | 71.8   | 70.3  | ↑           |
| Gold (\$/Troy oz)           | 1078   | 1057  | ↑           |

|     |                       |
|-----|-----------------------|
| ↑↑↑ | Strong upward trend   |
| ↑   | upward trend          |
| →   | Little change         |
| ↓   | downward trend        |
| ↓↓↓ | Strong downward trend |

Source: Datastream, Henderson Global Investors, as at 5 February 2010  
 \* Consensus economics, as at 11 January 2010  
 \*\* Henderson Interest Rate Team forecast

## MACRO

G7 government bonds, the US dollar and the Japanese yen were amongst the assets that benefited from the flight to quality last week. The euro remained under pressure as sovereign default fears continued to focus on countries within the single currency zone, most notably Greece. Given the vastly different fundamental backdrop of various asset classes, a continuation in the broad-based risk asset sell-off seems unjustified. In equities, three quarters of S&P 500 companies (market cap basis) have reported earnings with 75% beating analysts estimates; those companies have also shown positive top-line revenue growth for the quarter, a sign that the economic recovery is indeed taking hold. With earnings growth consistently beating estimates, it's possible analysts will raise their earnings targets going forward which, when combined with the decline seen in equity prices, should push valuations back into 'cheap' territory. On a cyclically adjusted basis (Graham-Dodd P/E), equities remain good value, which augurs well for the asset class if earnings are, indeed, returning to trend.

Global purchasing managers' indices for January were released last week and increased marginally at the aggregate level (53.2 versus 53.0 previously) which, given the recent gains seen in this metric, was a disappointment to markets. Nonetheless, the number indicated continued growth in the global economy as it came in above the key 50 boom/bust line.

The release of the all-important US non-farm payrolls (employment) data on Friday was of particular interest given the concurrent release of the benchmark revisions to last year's data. As indicated beforehand by the US Bureau of Labour Statistics benchmark revisions showed that the US economy lost 930,000 more jobs than initially reported throughout 2009 due to an overestimation of job creation by the business birth/death model. Otherwise, the data showed that the US economy lost 20,000 jobs in January, which was worse than the 15,000 increase in employment that had been expected by analysts. Notwithstanding the poor headline print, temporary help payrolls - a leading indicator for the overall jobs market - increased for the third straight month, a positive indication for future for total payrolls going forward. The beginning of hiring for the US census, which is expected to add about a million jobs to payrolls in total, will become apparent in the data next month and its effects are expect to peak around April.

## BONDS & CURRENCIES

Bonds rallied as investors shied away from equities due to concerns over sovereign debt and the strength of a global recovery. However, debt spreads widened between 'quality' government bonds and those of Spain, Greece and Portugal as fears remained that a default would be triggered by their debt crisis. The spread between 10-year Greek note yields over the German bund widened to 368 basis points (bp) on Friday. However, Portugal's credit default swap saw a high on Friday as it hit a record 226bp - the cost of insuring €10m of debt over 5 years would be €226,000 per year. As a result the euro faltered as investors reduced exposure to the region; falling 1.5% against the dollar over the week and 2.8% over the yen as investors sought the safe haven of relatively safer currencies; the dollar surged to its highest level in seven months. Sterling was one of the week's worst performers as concerns over Britain's fiscal position mounted, losing 2.3% against the dollar.

## COMMODITIES

Commodities suffered in the light of the sell-off to the relative safe havens of dollar assets and quality government bonds. The rise in sovereign risk weighed heavily on gold and the metal fell 2.3% over the week. Crude oil (ICE March Brent) slumped 2.6% and copper fell by 6.5%.

**UK EQUITIES:** the FTSE 100 index fell for a fourth successive week (-2.4%) as investors sought the safety of 'quality' government bonds, as doubts persisted over the debt positions of many European countries. The index has not fallen for four consecutive weeks since July 2008.

The general financial sector was badly hit this week; interdealer broker ICAP's shares lost almost a fifth of their value, falling 21%, after posting a profit warning. In the same sector, Tullett Prebon lost a tenth of its value as it took collateral damage. Against the market trend, Vodafone increased 3.5% after exceeding revenue expectations in Q4 2009.

Liberty International rose at the end of the week, as it unveiled plans to split out its London property business. Analysts from Societe Generale saw about a 10% upside potential on Liberty shares from the split, with the core retail business being valued at £2.3bn. Basic resource stocks fell 3.9% over the week as the price of copper fell for the fourth consecutive week and on investor concern over the pace of the economic recovery; Xstrata led mining stocks lower, falling 7.9% ahead of full year results today. BP was 0.9% lower as fourth quarter results failed to meet expectations on Tuesday and Cairn Energy 1.8% lower as crude oil prices took a tumble.

**Mid and Small Caps:** shares in vaccines and biopharmaceuticals developer Lipoxen dived by 25% after it announced its 2009 revenues were lower than expected due to a delay to clinical trials. Shares in electronic payments and cash machines operator Payzone have been suspended ahead of its potential acquisition. A significant portion of its debts will have to be written off for the deal to go ahead. Character Group, the toymaker, gained 7.0% on Friday as its share buyback programme continued.

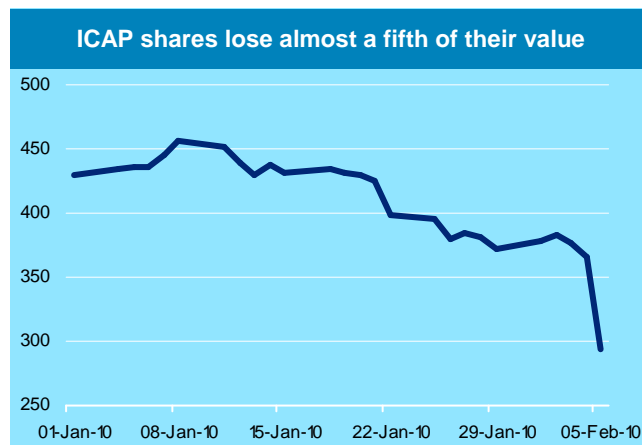
Elsewhere, London-based pub group Fuller, Smith & Turner said it continues to trade strongly and expects full year results to exceed expectations. However, the company said it was cautious about the UK economic outlook and the prospects for its customers for 2010 and beyond.

## OVERSEAS EQUITIES

**European markets:** The FTSE Eurofirst 300 Index fell 3.7% over the week, hitting a three-month trough, due to concerns over the potential exposure to some of the region's frailest economies. The Athens General plunged 8.3% over the week to a nine month low, Lisbon's PSI 20 lost 7.2% and Spain's Ibex 35 lost 7.7% over the week.

European banks were the biggest losers. It was thought the sell-off reflected fears about banks' exposure to assets from the faltering economies and what potential losses could do to inhibit their own capital. The sector lost 6.4% over the week; in 'peripheral' Europe, the largest fallers were the National Bank of Greece (-12%), Banco de Valencia in Spain (-15%) and, in Portugal, Banco Espirito Santo (-11%).

## MARKET DATA



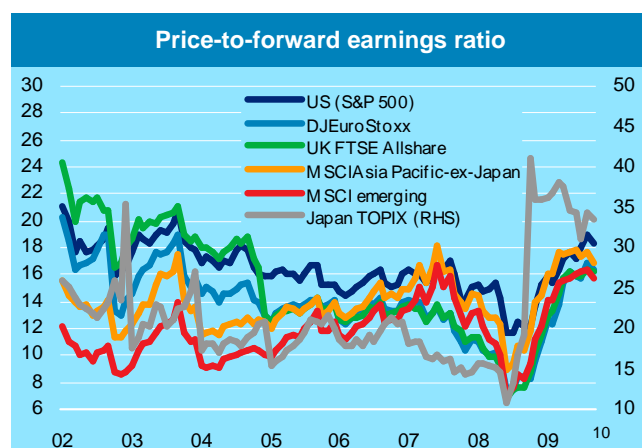
Source: Datastream, as at 5 February 2010

| Equities                     | 29 Jan | 5 Feb | % cge |
|------------------------------|--------|-------|-------|
| UK - FTSE All-Share          | 2660   | 2597  | -2.4  |
| UK - FTSE 100                | 5189   | 5061  | -2.5  |
| UK - FTSE 250                | 9237   | 9036  | -2.2  |
| UK - FTSE Small Cap          | 2807   | 2774  | -1.2  |
| Eurozone - DJ Euro Stoxx     | 262    | 249   | -4.8  |
| US - S&P 500                 | 1074   | 1066  | -0.7  |
| US - Nasdaq                  | 2147   | 2141  | -0.3  |
| Japan - Topix                | 901    | 892   | -1.0  |
| Hong Kong - Hang Seng        | 20122  | 19665 | -2.3  |
| MSCI Emerging Markets (US\$) | 934    | 898   | -3.8  |

Source: Datastream, as at 5 February 2010

| Consensus EPS Growth %     | 2009* (yoy) | 2010* (yoy) | 2011* (yoy) |
|----------------------------|-------------|-------------|-------------|
| US                         | 3.2         | 29.6        | 20.8        |
| Japan                      | N/A         | 88.1        | 25.5        |
| Eurozone                   | -27.5       | 33.7        | 23.1        |
| UK                         | -33.3       | 31.2        | 24.7        |
| Asia ex Japan              | 4.1         | 24.2        | 16.8        |
| MSCI Emerging Markets US\$ | 3.4         | 29.6        | 19.7        |

Source: Datastream, Henderson Global Investors, as at 31 January 2010  
\* Consensus forecast



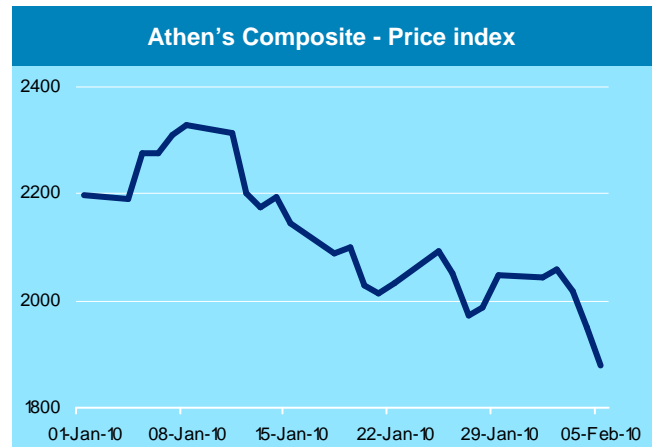
Source: Datastream, Henderson Global Investors, as at 31 January 2010

**US markets:** the S&P 500 index had a mixed week, ending down 0.7%. The index dropped -2.2% on Thursday as it suffered its biggest loss since April 2009, as fears over European sovereign debt and lower-than-expected weekly unemployment data took hold. Shares rallied on Friday as monthly job figures eased some of the concerns over the recovery in the US. Utilities, financial institutions and healthcare companies retreated more than 1.6%, recording the biggest declines among 10 industries.

The Dow Jones Industrial Average fell below 10,000 for the first time in three months and the Vix Index - Wall Street's 'fear' gauge that tracks market volatility - soared 20.0% on Thursday and moved a little higher on Friday. Large caps Merck, Coca-Cola and 3M fell more than 2% to help lead declines in the Dow. MasterCard (-10.8%) and Pfizer (-3.5%) both fell after posting earnings that missed analysts' estimates.

Tyson Foods rose 4.7% after the company posted better than expected first quarter profits. Airgas (37.8%) was the biggest riser on the S&P on Friday after an unsolicited bid was made by Air Products & Chemicals. It has already been rejected twice but said that this time it is prepared to take the offer straight to the shareholders.

**Asian markets:** The Nikkei 225 Average was down 1.4% on the week due to debt concerns. The Shanghai Composite was also down (-1.7%), falling below the 3,000 level.



Source: Datastream, as at 5 February 2010

The Hang Seng index in Hong Kong fell below the 20,000 level for the first time since September 2009 as it mirrored the same sovereign debt concerns of the world equity markets and recent demand for banks waned. Investors were also held back by the prospect of Chinese monetary tightening.

However, after a week of poor publicity for the company, shares in Toyota picked up at the end of the week despite additional concerns about more recalls for brake problems on the 2010 model of its Prius Hybrid. The company instilled confidence as it posted better-than-expected third quarter profit and gave positive guidance for future earnings. Honda Motor announced an increase in its profit forecast, which sent its share price up 2.6% on Thursday.

| Week ahead                   |   | Consensus  |
|------------------------------|---|--|
| <b>Monday 8 February</b>     | <b>INTERIMS:</b> Kofax<br><b>FINALS:</b> Amino Technologies, BATM Advanced, St. Modwen Properties, Xstrata<br><b>ECONOMICS:</b> UK: RICS house price balance (Jan)  | Waning demand and signs of easing supply   |
| <b>Tuesday 9 February</b>    | <b>QUARTERLIES:</b> British Land Co; Prodesse Investment Ltd, Wolfson Microelectronics<br><b>FINALS:</b> Alphameric, Prodesse Investment Ltd., Sarantel Group 'A', Sarantel Group 'B', Sperati (Ca), Wolfson Microelectronics<br><b>ECONOMICS:</b> UK: Trade balance (Dec, £)<br>Germany: CPI (Jan)   |  |
| <b>Wednesday 10 February</b> | <b>INTERIMS:</b> BHP Billiton, Hargreaves Lansdown, Morse, Pan African Resources<br><b>FINALS:</b> CSR, Pacific Assets Trust, Reckitt Benckiser, Smurfit Kappa Group, Teleticity Group<br><b>TRADING ANNOUNCEMENTS:</b><br><b>ECONOMICS:</b> UK: BoE inflation report<br>France: Industrial production (Dec, yoy, mom)<br>Australia: Unemployment rate (Jan)<br>China: Exports (Dec, yoy) | Further gain expected<br>Expected to hover around 5.5% this year<br>Chinese New Year effect will distort the numbers   |
| <b>Thursday 11 February</b>  | <b>INTERIMS:</b> Diageo<br><b>FINALS:</b> Catlin Group, Minorplanet Systems, Rio Tinto, Rolls-Royce Group, Smith & Nephew<br><b>ECONOMICS:</b> US: Advance retail sales (Jan)<br>US Initial jobless claims (6 Feb)  | Increase in petrol prices expected to push sales up<br>Small decline expected  |
| <b>Friday 12 February</b>    | <b>QUARTERLIES:</b> Smith & Nephew<br><b>ECONOMICS:</b> Germany: GDP (Q4, yoy, qoq)<br>France: GDP (Q4, yoy, qoq)<br>Eurozone Industrial production (Dec, mom, sa)<br>Eurozone GDP (Q4, qoq, A)<br>US: U. of Michigan confidence (Feb P)  | Small rise<br>Strong bounce on consumer spending gains<br>Another monthly rise<br>Similar pace of expansion to Q3<br>Decline in confidence due to weaker equity markets and higher initial claims data |

Markets returns source Datastream price index for equities, total return for bonds, local market terms. This document has been produced based on Henderson Global Investors' research and analysis and represents our house view. The information is made available to clients only incidentally. Unless otherwise indicated, the source for all data is Henderson Global Investors. Any reference to individual companies is purely for the purpose of illustration and should not be construed as a recommendation to buy or sell or advice in relation to investment, legal or tax matters. Please remember that past performance is not a guide to future performance. The value of an investment and the income from it can fall as well as rise as a result of market and currency fluctuations and you may not get back the amount originally invested. Tax assumptions may change if the law changes, and the value of tax relief will depend upon individual circumstances.

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