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| | **Pension Fund Sub Committee**<br>28TH September 2010<br><br>**Report from the Director of Finance and Corporate Resources** |
| For Action | Wards Affected: ALL |
| **Report Title:** | **Monitoring report on fund activity for the quarter ended 30th June 2010** |

## 1. SUMMARY

This report provides a summary of fund activity during the quarter ended 30th June 2010. It examines the actions taken, the economic and market background, and investment performance, as well as commenting on events in the quarter. The main points arising are:

a) Equity markets fell sharply during the quarter, but other markets were fairly stable. Economic growth is improving.

b) The Fund has fallen in value from £455m to £424.6m, and has underperformed its benchmark over the quarter (-2.1%) as a result of asset allocation (-0.4% - overweight equities, underweight hedge funds and property) and stock selection (-1.7% - underperformance in global equities, bonds and hedge funds). The Fund underperformed the average local authority fund (-0.4%), as a result of underperformance in bonds and global equities, offset in part by gains through asset allocation (higher exposure to alternatives / lower exposure to equities). Over one year, the Fund has underperformed its benchmark (-0.2%) as a result of poor returns from asset allocation (-1.3 – higher exposure to cash and bonds / lower exposure to equities, property and GTAA) offset by good stock selection (+1.2% - UK equities, bonds, hedge funds, private equity and GTAA). Over one year, the Fund has also underperformed the average fund (-4.7%) as a result of lower exposure to equities / higher exposure to alternative assets and poor performance in global equities.

## 2. RECOMMENDATIONS

Members are asked to note this report.

## 3 DETAIL

### ECONOMIC AND MARKET BACKGROUND - QUARTER ENDED 31ST MARCH 2010

3.1 All equity markets fell during the quarter on worries about European banking, economic growth and fiscal tightening by governments. The UK fell by 13%, USA 11%, Germany 1%, HongKong 5% and Japan by 15%. The UK economic background was:

- UK base rates remained at 0.5%. Medium and long-term interest rates fell during the quarter. Concerns about the European banking system and various eurozone countries (Greece, Portugal and Spain) have affected these markets, but UK has benefited from a safe haven status.The Quantitative Easing programme in UK has been suspended at present.
- Headline inflation (RPI) rose by 4.7% in the year to August (5.1% May), and the Index of Consumer Prices (CPI) rose by 3.1% (3.2% May). It is expected that inflation will fall in the second half of 2010 as spare capacity and low pay increases bear down on prices, but there are concerns about inflationary pressures arising from food, raw materials and VAT.
- Average earnings growth (including bonuses) was 1.8% p.a. in July (2.7% May), below the Bank of England's 'danger level' (4.5%). Unemployment has fallen to 1.46m, but may rise as public expenditure is reduced and taxes raised following the recent budget.
- The UK economy grew by 1.2% in Q2 2010 (1.7% over a year). GDP is expected to grow by 1.5% / 2% in 2010 (and 1.5% / 2% in 2011).
- It has been anticipated that consumer spending will fall, though retail sales were up 1.3% in the year to June. The squeeze on incomes, and the decline in equity withdrawal from the housing market following price falls, may depress demand. Although, house prices have risen by 3.9% over one year to August (Nationwide), recent figures have shown falling prices. Mortgage approvals are only 60% of their level two years ago, but have risen since 2009. Capital Economics still expects further house price falls (15%/20%).

In summary,the recession has ended but interest rates are expected to remain low. The government was using both fiscal and monetary policy to combat the downturn, but fiscal policy will be tightened over the next five years. The recovery is expected to be slow with occasional setbacks, but sentiment has improved considerably.

3.2 Central banks have co-ordinated activity to supply liquidity to markets so that credit is available to support economic activity. It is expected that the USA economy may grow by 3% in 2010 (but only 1.5% in 2011) following tax cuts, interest rate cuts, and quantitative easing programmes. Improved payroll data, strong retail sales and a rebound in home construction had indicated that a recovery was underway, but recent figures have shown the recovery to be faltering. It is anticipated that company earnings will also improve. It is expected that Eurozone GDP will grow by 1.5% in 2010, supported by strong growth in Germany. Growth in China and India will be around 12% and 9% respectively in 2010 – emerging market growth is strong and providing export growth to developed economes – and China has raised interest rates and tightened banks' reserve requirements. The world economy is expected to grow by 4.6% in 2010, but only 2% in 2011.

3.3 A paper on market events and future prospects, written by the Independent Adviser, is attached.

3.4 Table 1 below shows the changes in asset allocation, how asset allocation compares with the benchmark and with the average fund (WM Local Authority average), and how the change in the market value during the quarter is allocated across asset classes. Items marked (*) in columns 4 and 8 cannot be separately analysed, but are included elsewhere. The WM Local Authority average asset allocation indicates little change apart from market movements in equities.

**Table 1: Asset Allocation as at 31st March 2010 compared to the Benchmark**

| Market (1) | Market Value 31.03.10 £M (2) | Market Value 31.03.10 % (3) | WM LA Average 31.03.10 % (4) | Fund Benchmark 31.03.10 % (5) | Market Value 30.06.10 £M (6) | Market Value 30.06.10 % (7) | WM LA Average 30.06.10 % (8) |
|---|---|---|---|---|---|---|---|
| **Fixed Interest** | | | | | | | |
| UK Gilts | 14.9 | 3.3 | 10.1 | 4.5 | 17.1 | 4.0 | 11.0 |
| Corp.Bonds | 22.3 | 4.9 | * | 4.5 | 24.4 | 5.8 | * |
| IL Gilts | - | - | 4.4 | - | - | - | 4.8 |
| Overseas | 0.5 | 0.1 | 2.0 | - | - | - | 1.9 |
| Emerg. Market | 8.3 | 1.8 | - | 2.0 | 8.3 | 2.0 | - |
| Infrastructure | 0.8 | 0.2 | - | - | 0.8 | 0.2 | - |
| Secured loans | 8.6 | 1.9 | - | 2.0 | 8.5 | 2.0 | - |
| Credit Opps. | 11.5 | 2.5 | - | 2.5 | 11.6 | 2.7 | - |
| Credit Alpha | 11.1 | 2.4 | - | 2.5 | 10.9 | 2.6 | - |
| Currency Fund | 1.3 | 0.3 | | | 1.1 | 0.3 | |
| **Equities** | | | | | | | |
| UK FTSE350 | 117.2 | 25.8 | 30.0 | 18.5 | 101.1 | 23.8 | 28.8 |
| UK Smaller co's | 15.4 | 3.4 | * | 4.0 | 14.5 | 3.4 | * |
| Overseas | 111.4 | 24.5 | 35.9 | 26.5 | 98.5 | 23.2 | 34.3 |
| USA | 55.9 | 12.3 | 10.8 | - | 51.8 | 12.2 | 11.6 |
| Europe | 22.1 | 4.9 | 9.3 | - | 17.6 | 4.2 | 9.5 |
| Japan | 7.7 | 1.7 | 3.8 | - | 6.9 | 1.6 | 4.2 |
| Pacific | 9.9 | 2.2 | 3.8 | - | 8.6 | 2.0 | 4.3 |
| Other | 15.8 | 3.4 | 6.1 | - | 13.6 | 3.2 | 6.0 |
| **Other** | | | | | | | |
| Property – UK | 20.5 | 4.5 | 6.1 | 8.0 | 22.5 | 5.3 | 6.8 |
| Property – Eu. | 6.8 | 1.5 | * | * | 6.1 | 1.4 | * |
| Hedge funds | 41.9 | 9.2 | 2.3 | 10.0 | 40.7 | 9.6 | 2.6 |
| Private Equity | 38.1 | 8.4 | 3.1 | 8.0 | 38.2 | 9.0 | 3.4 |
| GTAA | 11.5 | 2.5 | 1.2 | 4.0 | 9.9 | 2.3 | 1.2 |
| Infrastructure | 5.0 | 1.1 | * | 2.0 | 5.1 | 1.2 | * |
| Cash | 7.7 | 1.7 | 4.0 | 1.0 | 5.3 | 1.2 | 4.0 |
| **Total** | **454.8** | **100.0** | **100.0** | **100.0** | **424.6** | **100.0** | **100.0** |

3.5 The main changes to the Brent Fund have occurred as a result of market movements, agreed rebalancing and increased exposure to private equity. During the quarter, £1.1m was invested in private equity and £1m in UK property. It has been agreed that £1.25m per month should be invested in global equities (until May 2010). Since the end of the quarter there has also been further investment in UK property (£1m) and private equity (£2.4m).

**Performance of the Fund**

3.6 The independent WM Company measures the returns on the Brent Pension Fund. Table 2 sets out returns for the quarter to 31st March 2010.

**Table 2: Investment Returns in Individual Markets**

| Investment Category | RETURNS | | | | | | Benchmark/ Index Description |
|---|---|---|---|---|---|---|---|
| | Quarter Ending 30.06.10 | | | Year Ended 31.03.10 | | | |
| | Fund % | Benchmark % | WM Local Auth % | Fund % | Benchmark % | WM Local Auth % | |
| **UK Equities** | | | -11.5 | | | 21.2 | |
| UK Equities | -11.5 | -11.9 | | 22.3 | 21.1 | | FTSE 350 |
| UK Small Caps | -6.0 | -5.3 | | 16.0 | 20.3 | | FTSE Smallcap ex IT |
| **Global Equities** | -13.6 | -10.7 | -11.3 | 13.7 | 15.7 | | FTSE World 75% Hedge |
| North America | -11.5 | -10.3 | -10.4 | 36.7 | 26.1 | 25.8 | FTSE USA |
| Europe | -17.6 | -14.4 | -13.6 | 57.4 | 15.9 | 17.3 | FTSE Eu Ex UK |
| UK | | -11.8 | -11.5 | | 21.1 | 21.2 | FTSE All Share |
| Japan | -11.7 | -8.7 | -8.9 | 45.7 | 10.5 | 12.8 | FTSE Japan |
| Pacific (ex Jap) | -12.4 | -10.0 | -8.4 | 67.8 | 32.5 | 31.3 | FTSE Pac. Ex Jap |
| Emerging | -16.3 | -11.1 | -6.9 | 76.8 | 23.2 | 34.1 | FTSE World (Other) |
| **Fixed Interest** | | | | | | | |
| Total Bonds | 0.8 | 2.1 | 2.0 | 14.9 | 7.3 | 13.9 | Brent benchmark |
| UK Bonds | 4.9 | 4.5 | 2.6 | 6.7 | 6.0 | 14.7 | FTSE UK over 15 years |
| Index Linked UK | - | - | 1.4 | - | - | 9.6 | - |
| Corp Bonds | 1.5 | 1.9 | - | 14.4 | 15.9 | - | iBoxx Sterling Non-gilt |
| Secured Loans | 6.3 | 0.9 | - | 52.9 | 4.0 | - | 3 month LIBOR +3% |
| Credit Opportunities fund | 8.3 | 1.4 | - | 8.3 | 5.0 | - | 3 month LIBOR+5% |
| **Other** | | | | | | | |
| UK Property FOF | 5.6 | 3.6 | 2.8 | 25.4 | 23.9 | 17.9 | IPD Pooled index |
| Eu Property FOF | -8.9 | 1.9 | - | -38.5 | 8.0 | - | IPD All properties |
| Hedge Funds | -2.8 | 1.1 | -0.6 | 5.1 | 4.5 | 8.9 | 3 month LIBID+4% |
| Private equity | -2.3 | 0.1 | -0.3 | 7.4 | 0.4 | 9.4 | LIBID 7 Day |
| Infrastructure | 4.1 | 1.1 | - | - | - | - | 3 Month LIBID +4% |
| GTAA | -13.1 | -12.6 | - | 47.7 | 19.8 | - | FTSE 100 |
| Cash | -0.5 | 0.1 | 0.7 | n/a | 2.4 | 1.7 | GPB 7 DAY LIBID |
| **Total** | **-7.1** | **-5.0** | **-6.7** | **14.0** | **14.2** | **18.7** | |

3.7 Details of individual managers' performance tables are attached in Table 3, which shows three month, one year and longer-term information. Returns for the quarter underperformed the benchmark by 2.1%. Part of the underperformance arose as a result of asset allocation (overweight equites, underweight hedge funds and property). The main stock selection factors were:-

a) Fixed interest. The core portfolio underperformed as long dated government bonds rose in the general 'flight to safety'. The manager had overweighted shorter dated bonds, expecting rising yields, and corporate bonds. The satellite fund fell in value as markets became nervous about credit worthiness.

b) Hedge fund of funds underperformed as equity related, macro, event driven and multiple strategies, those that had previously added value in rising markets, suffered in the equity market sell-off. The manager reports that various hedges did not work because many managers were trying to use the same protection – and prices moved accordingly. It appears that markets were highly correlated.

c) GTAA. The manager marginally underperformed as the overweight to global equities (against bonds) was unsuccessful as markets fell. However, two strategies (bond v bond and currency) added value. In particular, the overweight in USA bonds and Japanses yen, and the underweight in the euro, added value equities.

d) Global equities underperformed the benchmark as both value and growth stock selections were unsuccessful. In particular, both financial and materials stocks lost relative value in the market sell-off.

e) Property. The manager outperformed the benchmark, mainly as a result of a distribution from the Protego fund whose value had previously been reduced to nil but also as a result of overweighting the London property market. The European market is bottoming out, and the manager is looking for new funds to commit cash. Most of the underperformance arose as a result of currency (the falling euro).

3.8 Over one year, the Fund underperformed the benchmark by 0.2%. Asset allocation – lower exposure to UK Small companies and overseas equities, higher exposure to bonds and cash (held to fund the Infrastructure mandate) - has been negative. Stock selection added value - private equity, global equities and UK small companies underperformed, but other stock selection was positive – UK equities, bonds, GTAA and hedge funds added value.

3.9 The relative underperformance of the Brent fund against the WM Local Authority average in Q4 (0.4%) arises as a result of poor stock selection in global equities and hedge funds. This is disappointing as asset allocation added value through low exposure to equities / high exposure to alternative investments.

3.10 The Brent fund has underperformed the average local authority fund by 4.7% over one year, mainly because it has had a lower exposure to equities (higher exposure to alternatives – mainly hedge funds and private equity) in a period when equities have performed very strongly. Relative performance has also suffered as a result of reduced returns in global equities.

**Actions taken by the Brent In-House UK Equity Manager during the Quarter**

3.11 There has been some purchases and sales during this quarter to invest dividends (£0.9m) improve tracking error, rebalance the Fund towards global equities, and invest in private equity.

Purchases
a) Took up rights issues.

Sales
a) Sold stocks to ensure more accurate index tracking or as they left the index (such as Edinburgh Dragon Trust).
b) Sold stocks to fund investment elsewhere (£0.8m).

**Future Strategy for the UK FTSE350 Index tracking fund**

3.12 The strategy is that of tracking the FTSE 350 within 0.5% over the year. Activity during July and August included selling stocks to fund increased exposure to property and private equity.

**NEW DEVELOPMENTS AND FUTURE INVESTMENT OUTLOOK FOR THE BRENT FUND**

3.13 Equity markets have risen sharply during July as worries about banking markets recede and investors focus on earnings growth. A number of managers (AllianceBernstein, Henderson, Fauchier and Mellon) report that strategies that lost value in the previous quarter have added value in July. August and early September have proved to be more volatile, but equity markets remain well above the levels of the end of June.

3.14 The 75% currency hedge on the global equity portfolio managed by AllianceBernstein was reintroduced on August 2nd following consultation with the Chair, the Independent Adviser and the manager. The hedge was removed amid fears that sterling may collapse in value. However, although the currency initially fell from 1.51 dollars to 1.43 to the £, the emergency budget and good Q2 GDP figues boosted the value of sterling. The hedge was reintroduced at around 1.57 dollars to the £.

3.15 Gervais Williams, the head of the small companies team at Gartmore and manager of the UK and Irish Small Companies Fund, has resigned. He has been replaced by Adam McConkey, his deputy and a long time member of the small companies team. Processes and procedures will remain the same. I am meeting Adam McConkey and will update members on the outcome of that meeting and other actions taken.

3.16 Members will be aware that the value of the investment in the Henderson PFI Secondary II Fund (Infrastructure Fund) has fallen sharply. It appears that a number of investors in the Fund are threatening Henderson with legal action on the grounds on negligence. I will investigate the options for Brent.

3.17 The Local Government Pension Scheme (LGPS) is currently under review following a long period of rising costs and negative publicity. Two recent announcements have helped funding levels – the switch from RPI to CPI will reduce inflation related payments to pensioners, and the two year pay freeze will reduce the rise in the value of benefits. John Hutton, the former Labour Cabinet minister is currently reviwing public sector pension provision, and will announce his proposals in early

October. It is expected that he may consider such cost reducing measures as a career average scheme (rather than final salary related), higher employee contributions and a higher retirement age.

## 4. FINANCIAL IMPLICATIONS

These are contained within the body of the report.

## 5. STAFFING IMPLICATIONS

None directly.

## 6 DIVERSITY IMPLICATIONS

The proposals in this report have been subject to screening and officers believe that there are no diversity implications arising from it.

## 7 LEGAL IMPLICATIONS

There are no legal implications arising from the report.

## 8. BACKGROUND INFORMATION

AllianceBernstein – June 2010 quarter report.

Henderson Investors – June 2010 quarter report
Persons wishing to discuss the above should contact the Exchequer and Investment Section, Finance and Corporate Resources, 020 8937 1472/1473 at Brent Town Hall.

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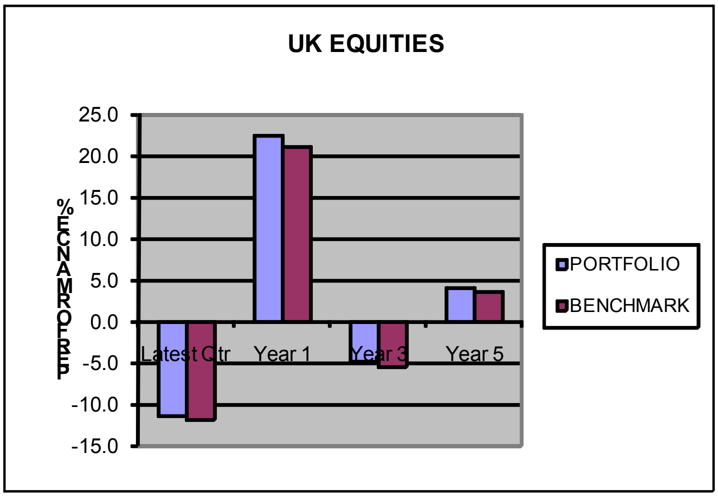
|---|---|
| **DUNCAN McLEOD** | **MARTIN SPRIGGS** |
| **Director of Finance & CR** | **Head of Exchequer and Investment** |

**PERFORMANCE FOR INDIVIDUAL PORTFOLIOS 30th June 2010**

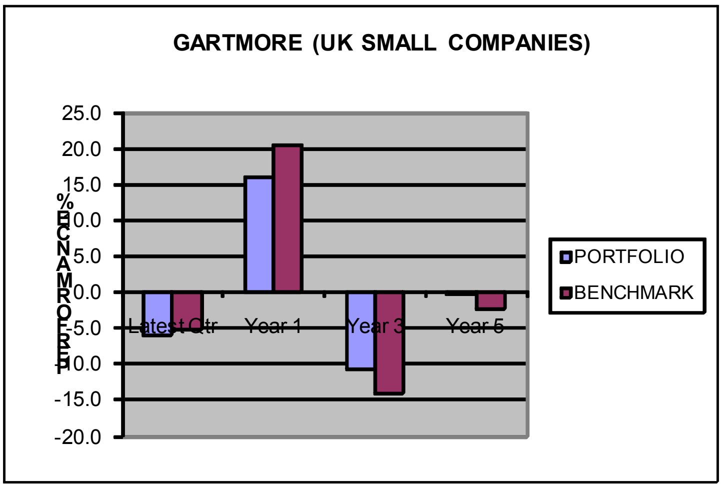
**UK EQUITIES**

| | PORTFOLIO | BENCHMARK |
|---|---|---|
| Latest Qtr | -11.5 | -11.9 |
| Year 1 | 22.3 | 21.1 |
| Year 3 | -4.9 | -5.6 |
| Year 5 | 4.0 | 3.6 |



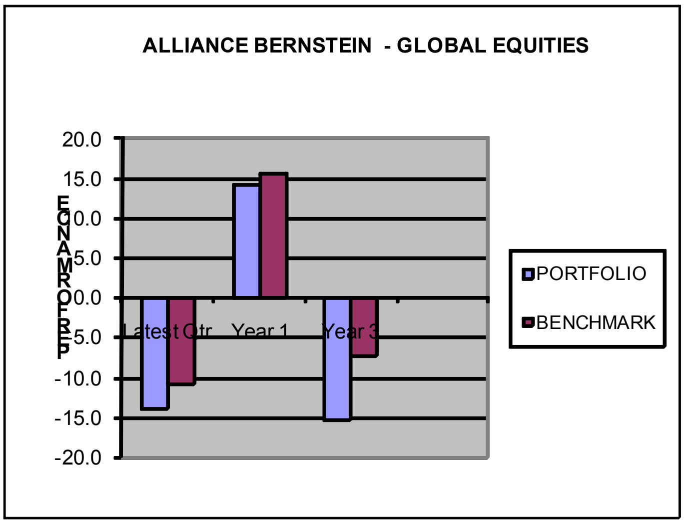

**GARTMORE (UK SMALL COMPANIES)**

| | PORTFOLIO | BENCHMARK |
|---|---|---|
| Latest Qtr | -6.0 | -5.3 |
| Year 1 | 16.0 | 20.3 |
| Year 3 | -10.7 | -14.2 |
| Year 5 | -0.1 | -2.3 |



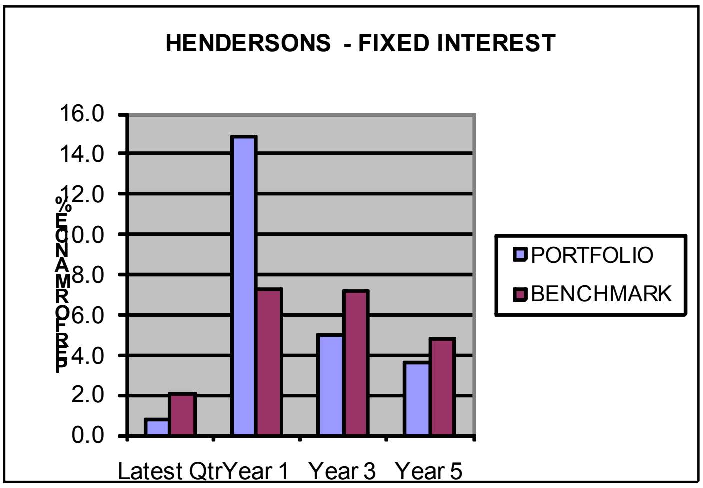

**ALLIANCE BERNSTEIN - GLOBAL EQUITIES**

| | PORTFOLIO | BENCHMARK |
|---|---|---|
| Latest Qtr | -13.8 | -10.7 |
| Year 1 | 14.2 | 15.7 |
| Year 3 | -15.2 | -7.2 |



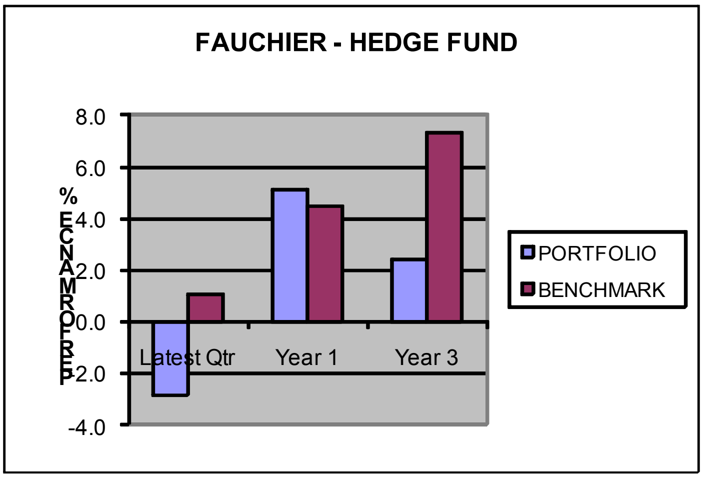
**HENDERSONS - FIXED INTEREST**

| | PORTFOLIO | BENCHMARK |
|---|---|---|
| Latest Qtr | 0.8 | 2.1 |
| Year 1 | 14.9 | 7.3 |
| Year 3 | 5.0 | 7.2 |
| Year 5 | 3.6 | 4.8 |



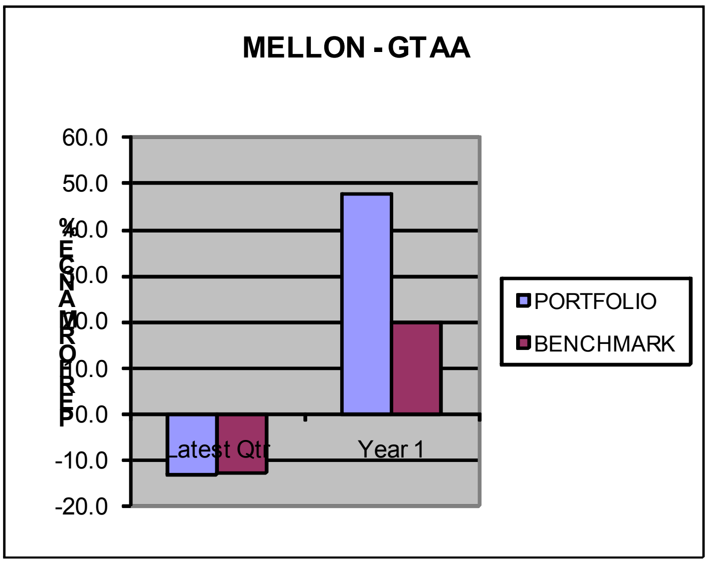

**FAUCHIER - HEDGE FUND**

| | PORTFOLIO | BENCHMARK |
|---|---|---|
| Latest Qtr | -2.8 | 1.1 |
| Year 1 | 5.1 | 4.5 |
| Year 3 | 2.4 | 7.3 |




**MELLON - GTAA**

| | PORTFOLIO | BENCHMARK |
|---|---|---|
| Latest Qtr | -13.1 | -12.8 |
| Year 1 | 47.7 | 19.8 |



## Report from the Independent Adviser

## Investment Report for the Quarter ended 30th June 2010

### Market Commentary

The course of equities during the quarter proved to be highly volatile as markets both in the UK and globally were affected by a combination of rapidly moving and conflicting influences. By the end of the quarter the adverse factors overwhelmed the positive and, as the return table below shows, all the principal equity markets fell. By contrast, it was heartening that fixed interest returns were broadly positive as investors sought the haven of less risky assets.

### Index returns expressed in sterling

| | Indices | Quarter ended 30th June 2010 |
|---|---|---|
| | | % |
| **Equities** | | |
| Emerging Markets | MSCI Emerging Markets Free | -7.0 |
| Japan | FTSE Developed Japan | -8.7 |
| North America | FTSE North America | -10.3 |
| Asia/Pacific | FTSE Developed Asia Pacific (ex Japan) | -10.4 |
| UK | FTSE All Share | -11.8 |
| Europe | FTSE Developed Europe (ex UK) | -14.3 |
| **Fixed Interest** | | |
| UK Gilts | FTSE British Government All Stocks | 4.5 |
| Corporate Bonds | Merrill Lynch Sterling – Non Gilts All Stocks | 2.0 |
| UK ILGs | FTSE British Government IL Over 5 years | 1.6 |
| **Property** | IPD | 4.8* |
| **Cash** | Merrill Lynch LIBOR 3 Month | 0.1 |

* Return for 3 months to 31st May 2010 (latest available)

### Currency Movements for quarter ended 30th June 2010

| Currency | 31st March 2010 | 30th June 2010 | Change % |
|---|---|---|---|
| USD/GBP | 1.517 | 1.496 | -1.4 |
| EUR/GBP | 1.121 | 1.221 | 9.0 |
| USD/EUR | 1.353 | 1.225 | -9.5 |
| Yen/USD | 93.440 | 88.490 | -5.3 |

Within the return table it is scarcely surprising that Europe (-14.3%) was the obvious laggard, principally due to concerns over the very future of the Eurozone and the much publicised fiscal deficits of some of the smaller European countries, especially Greece. UK (-11.8%) continued to be bedevilled by debt problems at all levels. Political worries also abounded in the run up to the General Election. Asia/Pacific (-10.4%) was troubled by the possibility that the pivotal economy of China might be slowing down at last. Japan (-8.7%) continued to be worried about the ability of its new Democratic Party to take sufficiently imaginative steps to begin to solve the long term deflation situation which has almost become an endemic condition in Japan. Even the return for Emerging

Markets fell 7.0%, but that was because they fear that their growing economies will be affected by a lower global demand for their exports on which they are still reliant.

Overall returns in the Fixed Interest sub sectors were helped by their presumed attraction as a form of insurance in the volatile background that affected other asset classes. Property continued to recover from its pronounced down cycle, especially in the UK. Advantage began to be taken of increasingly attractive prime quality valuations. Within the currency world it was the strength of sterling and the recovery of the US dollar (+9.5%) against the Euro were marked in response to the Eurozone's well publicised fiscal deficit and economic woes.

This was a particularly eventful quarter when equities and other asset classes had to contend with a combination of especially adverse factors. The principal negative factors which continued to inflict damage on the markets were those that have existed for some time namely:-

- Adverse comment regarding the fiscal indebtedness of the Eurozone nations together with their respective financial structures. The worst situations were clearly in the south (Greece, Portugal and Spain), who all suffered from weak GDP growth and high rates of unemployment. The better placed Eurozone members continued to be France, Germany and the Nordic region.
- Within the UK, the event of greatest influence was the General Election and the run up period to that day. The return of a coalition government has proved to be a calming influence. So far, the early honeymoon period of the coalition has gone surprisingly well with no apparent major disagreements.
- In the period leading up the UK's general election it was well known that the country's fiscal deficit was proportionally the second highest (£168b) in the European Union. All parties acknowledged that, post the election, the deficit could only be reduced by a programme of tax increases and severe cutbacks in public expenditure. The new government has unveiled its plans in that regard. It will take at least a three year grind to meaningfully reduce the deficit.
- The apprehension that the weaker economies with high fiscal deficits would suffer a double dip recession.
- External market influences included the intransigent situation in Afghanistan, the seemingly never ending Israeli/Palestinian deadlock and the worrisome regime in Iran with its nuclear threat. Although most of these confrontational factors have become discounted in the market place, they are capable of flaring up at any time and therefore have to be carefully watched.
- Governments and central bankers of the most indebted nations, particularly in the Western Hemisphere, are constantly wrestling with their respective debt problems. However, the proverbial silver cloud against this background has undoubtedly been the continuing low level of interest rates which are vital to maintain fragile rates of economic growth as nations struggle to recover from the effect of the sub prime crisis of 2007/2008 . It is worth recording just how low interest rate levels still are:-

| | % |
|---|---|
| Bank of England | 0.5 |
| European Central Bank | 1.0 |
| Switzerland | 0 - 0.75 |
| Federal Reserve Board | 0 - 0.25 |
| Japan | 0.10 |

The maintenance of low interest rates should help consumers and corporations.

- The BP oil spill saga will most likely run and run just as the Exxon Valdez incident did back in 1989. Certainly the aggressive rhetoric of President Obama and Congress has not helped. It seems clear that they are both politicking ahead of the mid term elections in November. Of immediate impact is the suspension by BP of its dividend for 2010 and the $20b subscription to a fund specifically to pay for the spillage and other claims. The dividend suspension will have a marked effect as it is generally estimated that the BP dividend accounts for some one sixth of the UK's total dividend income. It therefore follows that both private and institutional investors will be severely disadvantaged.
- The Organisation for Economic Co-operation and Development (OECD) has lifted its estimate of global growth for 2010 to 4.6% from 3.4% and for 2011 to 4.5% from 3.7%. A major contribution to this comes from the growing economies of the Eastern Hemisphere. The OECD warns that deflation is a risk.
- Stock markets are waiting to see how the world banking system is to be reorganised in order to protect nations from the upheavals of the last three years. Apart from special taxes on banks it does seem likely that banking activities may be split between investment banking and retail banking, similar to the laws that used to prevail in the USA under the Glass Stiegel Act. Certainly the activities of banks are going to be stringently monitored and regulated. Stress testing is just a start. Within the UK, responsibility for the banking system is now entirely that of the Bank of England, avoiding the tripartite system (Treasury, Government and Bank of England) that proved slow and inept at the time of the financial crisis. The changes will take time to unfold, but the result should be a more highly regulated, transparent and safer financial system with much lower levels of leverage and also improved liquidity.

**<u>UK</u>**

**<u>Positive Influences</u>**

- There is to be a new budgeting watchdog called the Office for Budget Responsibility "to provide independent economic and borrowing forecasts for the Government".
- On 19th May the Bank of England held interest rates.
- In the quarter to 30th April 2010, 31,038 new houses were registered, a substantial 74.0% increase on a year ago. New car registrations were 11.5% p.a. higher in April.
- Unemployment fell by 34,000 to 2.47M people in the quarter to 31st May. For May the unemployment rate inched lower to 7.8% from 7.9% in April.
- There is no shortage of international companies wishing to get close to the embattled BP, including Petro China, that country's largest oil and gas producer.
- Within the Emergency Budget of 22nd June, the Office for Budget Responsibility forecast that GDP would grow 1.2% in 2010, 2.3% in 2011, 2.8% in 2012 and 2.9% in 2013. The Budget also estimated that CPI would fall to 2.7% by the end of 2010. Additionally, it forecast that the percentage of unemployed people would fall from 8.0% in 2010 to 6.1% in 2015/16. It was also announced that there would be a levy on bank balance sheets by January 2011, that corporation tax would be cut by 1% over the next 4 years taking it down to 24% by 2014/15, that

VAT would increase to 20% from the current 17 ½% from 4th January 2011 and that the rate of CGT would rise from 18% to 28%.
- The Office for National Savings reported that public sector net borrowing was £16.0B in May versus consensus estimates of £18B.
- The Chancellor George Osborne announced that the FSA would be abolished with a commensurable increase in the powers of the Bank of England. The principal new remit for the Bank of England is to prevent a build up of risk in the financial system in addition to the Bank's monetary policy roll.
- Retail sales in June advanced by a resilient 1.0%, the strongest increase for a year.

**Negative Influences**

- The British Bankers' Association said that lending to financial companies in April fell by £1.1B.
- The fiscal budget now stands at a mammoth £156B.
- On 1st June such was the concern over the leakage from BP's Macendo deep water oil well in the Gulf of Mexico and its damage to the eco system that the company's shares traded 13% lower on the day. It was feared that BP might default on its debts. Additionally, the Obama administration was pressurising BP not to pay shareholders a dividend before the total cost of the oil spill clean up could be estimated.
- On 10th June the Bank of England left interest rates unchanged.
- Whilst the purchasing managers index increased fractionally in May to 55.4 from the 55.3 level of April, this was a lesser figure than the market had been expecting.
- In the first quarter of 2010 the deficit in goods and services reached £9.7B from the £8.7B in the previous quarter. The principal excuse for this deterioration was the weakness in demand from the Eurozone, the UK's biggest trading partner.
- CPI inflation in June was 3.2%. This compares with the government's target of 2.0%. Inflation was affected both by the high price of oil and also January's VAT rise from 15% to 17.5%. A year ago Mervyn King (the Governor of the Bank of England) had been forecasting inflation of only +0.7%!
- In the first quarter of 2010 there were a record 35,680 insolvencies.
- The overly aggressive rhetoric being used against BP by President Obama is no doubt spurred by November's mid term elections. His recent hostile attitude is scarcely likely to improve Anglo American relationships at this critical time. Perhaps Obama should recall that the sub prime and consequent financial banking disaster was spawned in the USA. Two can play the international blame game!
- The International Monetary Fund estimates that the UK GDP growth rate will be 1.2% in 2010 and 2.1% in 2011 versus the government's estimate of 2.3%.
- The National Institute of Economic and Social Research estimates that GDP grew by 0.7% in the second quarter of the year.
- The new Office for Budget Responsibility (OBR) forecasts that the overall fiscal deficit for 2010/11 will be £155B down from original estimates of £163B.
- The Fitch rating authority reduced its BP credit rating from AA to BBB.

- BP announced, in the aftermath of the oil spill and pressure from the US government, that it would suspend its dividend this year and pay $20B into a ring fenced account to be phased over 4 years specifically to clean up the damage as a result of the spill.
- Industrial production receded 0.4% in May against estimates of +0.4%.
- The Government decision to switch from using RPI to CPI when updating the value of private pension payments has caused a stir in the fixed interest markets where the prices of index linked bonds fell.

**North America**

**Positive Influences**

- Construction spending grew by 2.7% in April.
- On 1st June the Bank of Canada raised interest rates by a ¼% to ½%, the first rate increase since July 2007.
- The Commerce Department reported that retail sales advanced by 0.4% in April. This was twice the economists' consensus estimate.
- The unemployment rate for June eased back to 9.5% from May's 9.7%.
- Headline inflation decreased to 3.2% p.a. in June (May 3.4%).
- On 23rd June the Federal Reserve Board (FED) kept interest rates unchanged.

**Negative Influences**

- The trade deficit in May was $40B, little changed from April and March.
- President Obama ordered all 33 deep water oil rigs in the Gulf of Mexico to halt drilling. Indeed, he proposed a 6 month moratorium on offshore drilling. This will certainly impact both economic growth and also job creation. Ready access to energy has always been so vital to the US economy and has been considered somewhat of a divine right by the population.
- The Commerce Department revised the first quarter 2010 GDP growth rate from 3.2% to 3.0%. This compares with economists' estimates of 3.4%.
- Existing home sales dropped by 2.2% in May whilst new home sales fell by 32.7%, the lowest level since records started in 1963.
- The FED reduced its estimate of GDP growth in 2010 to 3.0 – 3.5% from its previous April estimate of 3.2 – 3.7%.
- June retail sales fell a further 0.5% from May's slide of 1.1%. This was worse than forecast.
- The Institute of Supply Management's index of non manufacturing business decreased to 53.8 in June (May 55.4).
- The Conference Board's confidence index fell dramatically to 52.9 in June from 62.7 in May. This was a much steeper fall than expected due to the state of the economy and the labour market.
- The National Association of Realtors announced that pending house sales collapsed by 30.0% in May against economists' estimates of a 12.5% fall.
- The Institute of Supply Management's manufacturing index declined to 56.2 in June against May's 59.7, a much larger drop than expected.
- The US labour force shrank by 652,000 in June, the second largest monthly fall since 1995.

- Durable goods sales fell by 1.1% in May.
- Housing starts fell by 5.0% in June.

## **Europe**

### **Positive Influences**

- On 10th May the European Union and the International Monetary Fund announced a €750B rescue plan to help the most indebted nations within the Eurozone.
- On 13th May Portugal introduced an emergency tax on wages and profits to help tackle the nation's budget problem.
- On 27th May the Spanish parliament passed an austerity package. Not before time.
- On 10th June the European Central Bank (ECB) left interest rates unchanged. The ECB's governor announced unlimited 3 month loans to last to the end of 2010 in an attempt to encourage banks to meet their customer financing needs.
- On the whole, corporations in Sweden, Finland and Norway have exhibited robust earnings growth, outperforming most other European countries.
- Several Eurozone countries have now imposed a ban on short selling programmes. These bans were initiated by Germany, especially in regard to Eurozone government bonds.
- There are now, at last, some signs that Portugal and Spain are introducing emergency measures to improve their finances.
- In a great austerity drive Spain cut civil service pay by 5% to help reduce the country's budget deficit.
- China's State Administration for Foreign Exchange, which manages the country's currency reserves, stated "Europe has been, and will be, one of the major markets for investing China's exchange reserves". Similar backing for the Euro was also stated by the Kuwait Investment Authority and South Korea.
- The Eurozone is conducting stringent stress tests on 91 banks focusing upon balance sheet strength.
- Trichet, head of the ECB, stated "a double dip recession is not at all what we are observing".
- Angela Merkel, the German Chancellor, announced an additional €80B of public spending cuts.
- German industrial production increased by 2.6% in May in part due to strong demand from China.
- German exports expanded by a marked 9.2% in May.
- German engineering orders in May advanced by a prodigious 61.0%.
- At the EU Summit meeting on 17th June there was a call to impose a general levy on European banks to ensure that they contribute to the cost of overcoming the financial crisis.
- Spain is to reform its rigid labour market and is to publish stress test results on its banks. At last a step in the right direction.
- France is to increase its retirement age from 60 to 62.

### **Negative Influences**

- Hungary's economic condition became increasingly weak with the previous government having manipulated the official macro economic data. Rather like the Greek government.
- The Cajasur savings bank failed and its control was passed to the Bank of Spain. There are 45 such banks most of which are involved in Spain's ailing property market.
- Eurozone banks have become increasingly reluctant to lend to each other for fear of the counter party risk. As a result there has been a relentless rise in 3 month EURIBOR, the rate at which European banks charge each other for lending in Euros.
- France's purchasing managers' index for May eased back to 55.8 against 56.6 for April.
- On 31st May the ECB stated the Eurozone financial sector and economy are facing "hazardous contagion" from the region's debt crisis and forecast €195B in bank write downs this year and next.
- The Fitch rating agency down graded Spanish debt from AAA to AA+.
- Germany's ZEW index of investor confidence slumped to 45.8 in May (April 53.0).
- To underline the seriousness of the Eurozone situation the German Chancellor, Angela Merkel, said "what is at stake is no more and no less than the future of Europe, and with it the future of Germany in Europe". This statement was made in the Bundestag regarding support for Greece's drastic 3 year austerity programme.
- There are clear signs that the German Chancellor Angela Merkel's coalition government is showing further weakness.
- On 26th May a German 5 year bond auction failed, clearly demonstrating investor apprehension.
- German industrial orders in May fell by 0.5%, in marked contrast to the rise of 3.2% in April.
- German unemployment rose to 7.7% in June from 7.5% a year earlier.
- Eurozone unemployment fell by 6,000 in April, the first drop for 2 years.
- Angela Merkel, Nicolas Sarkozy and Silvio Berlusconi find themselves in an increasingly parlous state with their respective electorates. This is partly due to the harsh measures they have been enacting to bolster their economies.

**Japan**

**Positive Influences**

- The annualised rate of GDP growth for the first quarter of 2010 was revised up to 5.0% p.a. from 4.9% p.a.
- On 4th June Naoto Kan was elected the new leader of the Democratic Party after the resignation of Yukio Hatoyama as prime minister who had failed to live up to the electorate's high hopes for him. Mr Kan's leadership style is allegedly more dynamic than his predecessor. It is to be hoped that he and his party will be able to enact the essential strong measures which are so urgently needed to address Japan's economic woes.
- On 16th July the Yen surged to its highest level of the year against the US dollar.
- Exports fell by 1.2% in May (April +2.3%)

## Asia/Pacific

### Positive Influences

- The Chinese government hinted that, through its State council, property taxes would be reformed in order to cool down the developing property bubble.
- China has agreed to spend £16B building oil refineries and other petroleum related infra structure in Nigeria in order to boost its reserves of crude oil.
- China's exports at +48.5% in May were much higher than estimated.
- China's trade surplus in May was $19.5B compared with only $1.7B in April
- On 19th June China announced it planned to introduce more flexibility into its exchange rate. It therefore seems likely that the currency peg between the renminbi and the US dollar will be broken. This announcement was cleverly timed, a week ahead of the G20 summit meeting.
- Singapore's first half 2010 GDP growth rate was a stupendous 18.1% p.a.
- The Australian economy added 45,900 jobs in June well ahead of estimates of 15,000.
- On 11th June the New Zealand central bank raised interest rates by ¼% to 2 ¾%.
- On 27th June the Reserve Bank of India raised interest rates by ¼% to counter rising inflation (10.2% in May).
- In the first quarter of 2010 India's GDP grew by 8.6%.

### Negative Influences

- Australia announced plans to impose a 40% tax on the profits of resource companies. Subsequently this proved to be a contributing factor in the replacement of the hitherto popular prime minister, Mr. Rudd.
- In China the purchasing managers' index of the Chinese Federation of Logistics and Purchasing fell to 53.9 in May from 55.7 in April, reflecting lacklustre demand from domestic and foreign markets.
- China's rate of GDP for the second quarter of 2010 fell to +10.3% (first quarter +11.9%).
- China's industrial production in June was 13.7% p.a. down from 16.5% p.a. in May.
- The purchasing managers' index in Korea for June decreased to 53.3 (May 54.6) whilst that of India receded to 57.3 in June from 59.0 in May. China's purchasing managers' index for June fell to 52.1, down from 53.9 in May.
- India's industrial output in May increased by 11.5% p.a. compared with the April rise of 16.5% p.a.
- Tensions between North and South Korea were further inflamed when the North Korean navy torpedoed a South Korean ship.

### Conclusion

To an extent the dismal returns of the reported quarter to 30th June 2010 go some way to discounting all the many uncertainties which currently prevail in the market place, and it goes without saying that it is investor uncertainty, both institutional and private, that is continuing to negatively influence most asset classes. So when will the clouds of gloom part to produce a better market background in which equities, in particular, can recover their losses and once again make worthwhile advances? The answer appears relatively simple. That is to say the following will need to happen:-

- Banks to be restored to a measure of health with genuine stress tested stronger balance sheets. No more debt ridden skeletons should fall out of financial cupboards. This will be especially pertinent within the weaker Eurozone countries like Greece, Spain, Portugal and Ireland.
- Corporate earnings statements will need to reassure shareholders that their respective dividend streams will be maintained and preferably increased. They will also need to reassure that earnings will not be too badly impacted by the current recessionary background and that dividend levels can be maintained or even increased.
- It will be important for governments and central banks to demonstrate that they are enacting the remedial medicine so badly needed, in the Western Hemisphere especially, to resuscitate economic growth and to thereby improve the morale of banks, industrial companies and consumers. Most vitally, it will be essential for banks to be more prepared to lend to those companies and individuals whose spending is an essential stimulus to national economic growth.
- That governments are seen to take proactive measures both to stimulate current levels of economic growth and, at the same time, to ensure that inflation rates will be kept under control. This will be a difficult tight rope walking test which will probably result in pre-emptive increases in interest rates from the present record low historic levels. Such interest rate increases are likely to be incremental and modest.
- The most critical ingredient of all will be that it can be clearly seen that at last the current horrendous levels of fiscal deficits are being meaningfully reduced by timely actions by respective governments and central banks.
- It will be necessary for sufficient liquidity to continue to be injected into the financial system to provide the essential life blood on which consumers, economies, corporations and most asset classes are so reliant.
- And finally, that the threat of a double dip recession in the principal industrial economies can be removed to the relief and comfort of all investors. Rather than a double dip, it seems more likely that economic growth in the Western Hemisphere will be positive, but somewhat anaemic. On the other hand the economies of the Eastern Hemisphere should continue to demonstrate strong growth, but at a lesser pace than in 2009.

If sufficient progress can be made to achieve the above supportive conditions then, and only then, will equity markets breathe a collective sigh of relief and start to make up for so much lost ground. Fixed Interest markets will, as they usually do, continue to focus manically on the rates of national inflation, central bank action and other macro economic data. For this reason, fixed interest returns between now and the year end could be somewhat lacklustre, despite the attraction of this investment class as a safe haven. In general, central bank interest rates are likely to remain very low especially in the UK and USA. Only in the Asia/Pacific region could they increase to any extent. It therefore follows that returns on deposit cash will likely continue to be miserably low.

With regard to other asset classes; Hedge Fund of Funds, Global Tactical Asset Allocation and Currencies are likely to continue to struggle due to the common problem that there is still too much correlation amongst most asset classes. Therefore there are less anomalies of which to take advantage. However, opportunities exist within private equities as liquidity improves and the secondary markets appear increasingly attractive. Infrastructure also benefits from better liquidity and growing demand for its wide spread of underlying sectors such as:- road and bridge tolls, airports, utilities (especially water management), airports, prisons, hospitals and oil terminals. Opportunities also exist within commodities, but because this is a relatively volatile asset class a longer term view is necessary. It is worth re-emphasising that, in the longer term, alternative asset classes have a real role to play in a pension fund and an amalgam of these classes should serve to reduce the portfolio's long term risk. The caveat is that their performance attribution has to be most carefully monitored. Certainly to a much greater degree than the classic asset classes of equities, fixed interest and property.

In sum, despite the current collective gloom, it seems reasonable to suggest that for 2010 as a whole equity returns could be in the high single digit area. If that is achieved it would come as a relief to many and a distinct surprise to some of the current doomsayers and overly pessimistic media and financial journalists.

Valentine Furniss
25th July 2010

## Investment Report for the Month of July 2010

## Index returns expressed in sterling for the month of July 2010

| | **Indices** | **M/E 31.07.10** |
|---|---|---|
| | | % |
| **Equities** | | |
| UK | FTSE All Share | 9.4 |
| Europe | FTSE Developed Europe (ex UK) | 8.4 |
| Asia/Pacific | FTSE Developed Asia Pacific (ex Japan) | 7.1 |
| Emerging Markets | MSCI Emerging Markets Free | 5.6 |
| North America | FTSE North America | 3.5 |
| Japan | FTSE Developed Japan | -0.2 |
| **Fixed Interest** | | |
| Corporate Bonds | Merrill Lynch Sterling – Non Gilts All Stocks | 0.6 |
| UK Gilts | FTSE British Government All Stocks | -0.7 |
| UK ILGs | FTSE British Government IL Over 5 years | -2.7 |
| **Property** | IPD | N/a |
| **Cash** | Merrill Lynch LIBOR 3 Month | 0.1 |

## Currency movements for month ended 31st July 2010

| Currency | 1st July 2010 | 31st July 2010 | Change % |
|---|---|---|---|
| USD/GBP | 1.512 | 1.566 | 3.6 |
| EUR/GBP | 1.214 | 1.202 | -0.9 |
| USD/EUR | 1.246 | 1.303 | 4.6 |
| Yen/USD | 87.060 | 86.660 | -0.5 |

The above return table shows that for the month of July all equity markets flourished (with the exception of Japan -0.2%) and produced robust performances in contrast to the negative equity returns for the quarter ended 30th June 2010. It is heartening that the UK (+9.4%) topped the leader board. By comparison with other regions it is surprising that the USA (+3.5%) was back marker apart from the laggardly Japan (-0.2%). The main reason for these welcome positive returns was the perception that market returns for the second quarter had over discounted the gloom (fuelled by double dip recession fears) and under-estimated both the ability of economies to recover and the level of corporate earnings and dividends to be expected.

The returns from Fixed Interest provided little succour and, apart from corporate bonds (+0.6%), returns were negative with index linked stocks recording a negative 2.7% return, mostly due to contradictory estimates of national rates of inflation with the general consensus of opinion appearing to suggest that inflation increases, after the current recession, would be at a lesser pace than in the past. What will have to be carefully monitored is the food constituent of inflation. Right now drought conditions in many countries and the damaging fires in Russia have caused the cost of certain crops like barley and wheat to double in a matter of weeks.

During July the main factors to affect stock markets were as shown below:-

In the UK

- It is early days, but the coalition government is operating surprisingly well with no apparent major rifts between its constituent parties.

In USA

- President Obama continues to struggle with his popularity ratings as the mid term elections loom even closer (November in fact). There is a view that the BP disaster helped Obama as he was able to take a strong nationalist stand.
- The Chairman of the Federal Reserve Board, Mr Bernanke, in his address to Congress, spooked stock markets by saying that the US economy faced "unusually uncertain" prospects.

In Europe

- There has been a veritable blitzkrieg on the banks to ensure that they now have sufficient balance sheet strength to cope with the types of financial pressures experienced during 2007 - 2009.
- A measure of calm is becoming apparent within the sovereign debt arena particularly in regard to the weaker members of the Eurozone, vide Portugal, Ireland, Greece and Spain.

In Japan

- The nation and its economy seems mired in its old fashioned and outdated policies and culture. Until this demonstrably changes it is as if the nation is destined for ever to malinger in the sloughs of deflation. Japan can derive some comfort from its large international companies together with a strong currency. But this in itself can work against the country's export trade.

In Asia

- The principal talking point has been China's currency the renminbi. In that regard the Chinese government and central bank does not wish to be seen to bow to international pressure to revalue its currency, but at the same time the Chinese regime wishes to increase its status and become a far more influential force on the world stage. It therefore seems likely that the renminbi will be gradually revalued and will ultimately become unpegged from the US dollar.
- Asia is fast becoming the prime catalyst for the growth of world trade. Asian rates of GDP growth remain considerably stronger than their Western Hemisphere counterparts.

During July the principal events and macro economic data within the regions were as follows:-

**UK**

- The Office for National Statistics (ONS) reported that GDP growth in the second quarter of 2010 rose by 1.2% which was double consensus estimates and represented the fastest pace of growth for 4 years. The ONS also reported that, in quarter 2, manufacturing grew by 1.6%, the service sector by 0.9% and business and financial services by 1.3%.
- The Bank of England stated that mortgage approvals were down 3.7% in June.
- The Purchasing Managers' Index receded to 53.1 in July from 54.4 in June.
- British factory purchases increased by 4.1% p.a. in June.
- July retail sales expanded by 2.6% p.a.

**USA**

- On 21st July President Obama signed a bill representing the most sweeping overhaul of Wall Street's regulation since the 1930s.
- On 23rd July the fiscal deficit was estimated at $1,471B, the largest on record, representing 10.0% of the national GDP.
- The White House estimates that the rate of unemployment will average 9.7% in 2010.
- June new home sales advanced by a substantial 23.6%, the largest increase since May 1980. To an extent this was a rebound from the 36.7% collapse in May.
- Second quarter GDP increased by 2.4% p.a. versus estimates of 2.6% p.a. (quarter one grew by 3.7% p.a.).
- Second quarter business investment was up 17% p.a. whilst consumer spending (70.0% of US activity) rose 1.6% (quarter one +1.9%).
- Durable goods orders in June fell 1.0% (May -0.8%), considerably worse than expected.
- The Federal Reserve Board's Beige Book adopted a cautious outlook warning that there were signs of a slow down.
- The Institute of supply Management's index of factory activity in July reduced to 55.5 (June 56.2) whilst its index of non manufacturing activity increased to 54.3 in July (June 53.8).
- Non farm payrolls in July contracted by 131,000 compared with an estimated fall of 65,000.

**Europe**

- Only 7 out of 91 banks that were stress tested failed the test, the implication being that these tests may have been too leniently applied.
- German retail sales fell 0.9% in June compared with a generally estimated 0.2% drop.
- German industrial orders advanced by 3.2% in June which was stronger than expected.
- German industrial production in June decreased by 0.6%.
- German exports in June grew by 1.9%.
- Italy's second quarter GDP rose 0.4%.
- The Eurozone's Purchasing Managers' index for July inched up to 55.8 from 55.5 in June.

**Japan**

- The main feature was the continuing strength of the Yen against the US $.

**Asia/Pacific**

- On 9th July, in order to cool inflationary pressures, the Bank of Korea increased interest rates by ¼ % on the back of estimates of GDP growth in 2010 of 5.8%. The country's exports continued to boom.
- China's Federation of Logistics and Purchasing reported that the Purchasing Managers' index slowed a marginal contraction in July to 51.2 from June's 52.1.
- Indonesia's GDP growth for the second quarter of 2010 was a robust 6.2% p.a. This was better than forecast.

**Conclusion**

The dichotomy for the course of equity markets, in the medium term, was always going to be the extent and speed with which it would be possible to reduce the respective ballooning fiscal deficits of the principal industrialised nations, particularly those in the Western Hemisphere. To do this requires a most delicate balancing act between central bank action on the level of interest rates, and governmental policies to increase taxes and reduce public spending. If the correct balance can be achieved then conditions can be created in which rates of GDP can recover and grow whilst inflation rates are simultaneously contained. This exercise is of course particularly applicable to those economies that suffered most in the toxic conditions resulting from the sub prime furore spanning 2007 - 2009. Those economies most affected have been the USA, Southern Europe (especially Portugal, Greece and Spain), Ireland and the UK. As widely publicised, such countries are continuing to wrestle with increased rates of taxation and deep public cost cutting exercises. Now at last, to the relief of those investors consumed with the paranoia of double dip recession, tentative signs are appearing in the aforementioned countries that the harsh remedial medicine and rigorous disciplines are beginning to work, albeit at a relatively slow pace. Should further progress be made by governments and central banks then the principal conclusions reached in the investment report for the second quarter of 2010 should hold firm. That is to say, it seems reasonable to suggest that equity returns for 2010 as a whole, could be in the high single digit area.

Valentine Furniss