

These commentaries and indicators represent the views from a sample of bespoke Fund Managers for Quarter 4, 2010 (period Oct-Dec)

For financial advisers only

United Kingdom

UK Overall Rating: 3.78

Company	Rating	Company	Rating
Allianz Global Investors	3	Invesco Perpetual	4
Barings Asset Management	4	Rathbones	4
BlackRock	4	Royal London Asset Management	3
BNY Mellon	4	SWIP	4
Henderson	4		

BlackRock - 4

- The UK economy is pulling out of recession more slowly than other major economies but recent data points to the upturn continuing at a slightly more rapid pace.
- The headwinds for the UK economy are well understood with balance sheet repair likely to limit consumption growth and current austerity plans looking to cut spending by 10-11% of GDP over the next 5 years.
- Recent earnings growth has been more positive than expected. Sterling weakness has been a tailwind and is likely to remain a supportive tailwind into the rest of the year.
- Equity risk premium is high given the strong earnings yield of UK market despite valuations looking attractive in a historic context.

Allianz Global Investors - 3

To those who have followed the UK's recent fiscal history, the surprising feature of the last quarter has been the extent to which gilts and sterling have become a safe haven. This is largely a relative assessment of course, but concerns over the potential instability of the Eurozone have caused a recovery in sterling to its highest level against the euro for 18 months, while the 10 year gilt yield has fallen below 3.5%, almost back to the low point in early 2009, and new gilt issues remain well covered.

On the basis of growth expectations therefore, we see little pressure in the direction of rising interest rates.

Indeed, we think that there is at least a 50% chance that during the next twelve months we will see a further round of quantitative easing beyond the present £200 billion, especially if the US leads the way. There is some sign that inflation expectations are rising, and the OECD, now supported by one member of the MPC, believes that "the process of normalisation of interest rates needs to start soon". However, the current inflation numbers are elevated and the fundamental evidence points strongly towards declining inflation. The monetary aggregates are weak and getting weaker; real wages growth is negative, while, as the Bank of England puts it, "the persistent margin of spare capacity is likely to drag inflation below the target" of 2%. Should sterling continue to strengthen, this could occur sooner than anyone expects. In conclusion, it is hard to see how economic recovery for the UK will remain, at best, anything other than tentative and vulnerable to shocks.

Royal London Asset Management - 3

While corporate earnings news has been good and the recent weakness in share prices offers some upside, we feel that the UK equity market has now discounted much of the improvement in economic prospects which we expect to occur this year. As such, there is no longer such a clear call to be so bullish on markets, although we do not expect a dramatic reversal in the near term. Our central scenario is for reasonably robust global economic growth this year, before a slowdown in 2011. There are, however, major risks either side of this view, towards higher inflation and policy tightening, or renewed deflation concerns.

Key:

1 Snarling Bear 2 Bearish 3 Neutral 4 Bullish 5 Raging Bull

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Allianz - 3

A series of disappointing data releases late in Q2 2010, including flagging consumer confidence and private-sector job growth that has barely reduced the unemployment rate, is leading more and more investors to wonder whether a double-dip scenario is likely in the US and beyond.

Yet many fail to recognise that fiscal deficits are also the result of actions taken by corporations and households, mostly when they both try to increase their net savings out of private-income flows. Indeed, the private sector cannot net save more money unless some other sector is willing to deficit spend. Strictly speaking, simple algebra shows that domestic households and firms can only run a financial surplus when the current account balance is greater than the government financial balance. In the extreme, when both domestic households and the corporate sector try to achieve a very large positive financial balance or net saving position, at the same time, say after an asset bubble has burst, then you need to have a very large trade surplus, a very large government deficit, or some combination of the two (such that, again, the current account balance is much larger than the fiscal balance). There is no other way to square this circle - this is not high theory - it is simply accounting realities revealed at the macro level.

BNY Mellon - 4

From a starting point of above-trend growth, US economic activity is expected to slow during H2 2010 as the engines of recovery - fiscal stimulus, exports and inventories - all begin to fade. We still believe underlying conditions will remain sufficiently strong to ensure the economy does not slip back into recession thanks to a continuation of easy monetary conditions and a financially sound corporate sector. Looking further ahead, we envisage a prolonged period of moderate growth as the stance of fiscal policy shifts from stimulative to restrictive and private sector demand, subdued by structural factors, grows at a modest pace only. Against this backdrop, economic output is set to remain below potential, exerting continued downward pressure on inflation. Core inflation could be at zero by mid-2011. Consequently, we foresee no material change to US monetary policy in the near term. Expectations as implied by Fed Fund futures suggest no change in Fed policy until mid-2011.

Jupiter - no rating supplied

We expect the quality of companies to become increasingly important as the economy moderates. While last year's rally was led by financials, consumer cyclicals and other higher risk stocks, many large-cap companies with strong balance sheets stayed relatively undervalued. With recent market weakness, some of these quality companies have seen their valuations fall to the lowest levels in years. Having rigorously reduced costs during the recession, they are expected to benefit from a strong expansion in profit margins as revenues recover. We continue to focus on blue-chip multinationals, especially in the areas such as industrials, consumer staples and healthcare, which should benefit from the market's rotation into "quality".

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Barings - 2

For us, Japan remains something of a trading market as we find little or no reason to be strategically invested in this market. It was noticeable that as we entered 2010, too many investors had thought they had a non-consensus overweight to the region. The strength of the Yen has served them well but the performance of the equity market has been lacklustre throughout. So when we think of the equity market, and not the Yen, we are firmly in the 2 camp.

Invesco - 4

We believe that the moderation in the pace of growth in China is a positive development, given the threat of overheating, and that authorities there will be successful in creating the conditions for a shift towards greater domestic consumption. This would improve Japanese companies' competitiveness in China, a market which accounts for around 25% of Japanese exports. In terms of sectors, we prefer financials, including banks, stockbrokers and real estate companies. These stocks are trading on cheap valuations, should benefit from further improvement in the economy and, in our analysis, have stronger earnings prospects than the market anticipates. Large, globally orientated exporters are also preferred. Many of them trade below their break-up values and this, in our view, undervalues their long-term earnings power, as they are well placed to exploit growing demand in Asia and recovery in developed markets.

Jupiter - no rating supplied

Yet again, politics is impacting Japanese equities. Prime Minister Kan seems to understand the key issues such as the ineffectual tax system and the horrendous overhang of government debt in Japan. It is too early to know, however, whether understanding them actually leads to addressing them. He plans to cut corporation tax but this is likely to be implemented in conjunction with a reduction of loopholes which raises the percentage of companies that pay tax from the current 28%. The beneficiaries should be companies that make the majority of profits domestically. The recent pullback in equities, together with recovering corporate earnings, has made Japanese equities looking undervalued even on an earnings basis. However, we expect the value trap to remain in place if Japan fails to sort out the political issues.

Rathbones - 3

Japan's recovery slowing but is continuing, with unemployment falling.

SWIP - 3

Our outlook over the medium-to-long term remains cautiously positive. This is supported by strong external demand and a vigorous rebound in the industrial sector. We believe that banking and other financial stocks are in a strong position to take advantage of Japan's continued economic recovery. Last year, performance was held back by equity issuance as the big banks strove to improve their balance sheets. This process is now almost complete and falling credit costs should help their earnings to beat expectations.

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BNY Mellon - 4

Macroeconomic factors continue to dominate the outlook for investment as we move into the second half of the year. Last quarter, we described the ‘tug of war’ between the significant structural headwinds facing the global economy and the unprecedented stimulus put in place by the authorities that had encouraged belief in a strong cyclical rebound. At that time, the cyclical bulls were firmly in the driving seat, with risk-asset markets, such as equities, continuing their run from the lows of March 2009. In the last quarter, investor sentiment increasingly focused on the downside risks for growth and the consequential possibility of deflation. Already-low government bond yields have slumped even lower and, in the case of German bunds (which have benefited from the flight out of peripheral European bond markets), yields have dropped below the levels seen in the 2008 credit crisis. We will continue to invest cautiously in terms of exposure both to the economic cycle and to the world’s financial sectors. However, we will also continue to identify appealing areas for investment, not least among the more stable areas of equity markets, where valuations are attractive.

Henderson - 4

There have been signs of encouragement in European economic data, where industrial production in France and Germany suggest that the outlook for growth in the region is not as anaemic as widely thought. All things considered, Europe could yet benefit from a sharp improvement in sentiment.

Rathbones - 2

Five years ago, Europe was a convergence traded; now it is very much a divergence trade. A combination of strong economic management of the economy and quality manufacturing companies gaining a competitive stronghold from sustained euro weakness make for a compelling argument for German equities. It is also fair to say the euro is unlikely to replace the dollar as the world’s reserve currency any time soon. Indeed, we believe the euro should devalue further to bolster exports. Sovereign debt problems in the peripheral countries will continue as the limitations of the bank stress-tests are exposed.

SWIP - 4

This is a testing period for European equities. The recent austerity measures are a step in the right direction, but markets are likely to remain cautious until concrete evidence emerges that the measures are working. What’s more, spending cuts and tax hikes alone will not be enough to wrest the eurozone out of the crisis: structural changes are also needed. The peripheral countries of the 16-nation region have become markedly less competitive since joining the single currency; this will need to be addressed if long-lasting growth is to take hold. It is no surprise that many are looking to Germany to boost domestic demand and help lift Europe from its economic malaise, but this is likely to be more hope than reality.

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Barings - 4

We have been overweight technology, recognising that while corporate balance sheets were strong there is a big incentive to invest in productivity-enhancing technology. The sector has performed well year to date, and we have recently downgraded from a 5 to a 4 in recognition of this outperformance. Concerns about a double dip recession might just mean that both corporates and consumers are a bit hesitant about the spending on technology hardware and/or software.

BlackRock - 4

- The sector is expected to remain volatile but with an upward trend into the latter part of the year.
- Inventories remain controlled and capacity generally remains tight, so a recovery in corporate IT spending should lead to renewed improvement in newsflow and sentiment, as long as consumer spending holds up.

Henderson - 4

Companies have not only cut costs through 2009, they have built up cash on their balance sheets. As confidence returns to the corporate sector, we may see this cash being spent. While some will go on rebuilding inventories from the current low levels, some may be used on Capex.

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