GinsGlobal Index Funds

Investment Outlook – February 2010

Global Equities

Following a volatile period in January which saw the MSCI World Index lose 4.1%, the MSCI EAFE (non US industrialized markets) fall 4.4% and the Eurozone itself fall by 4.7% (in Euros) or 6.7% - February proved to be a largely positive month for equities. This trend has since continued into March.

Leading industrialized country indices have clawed their way back to highs reached prior to the January sell off. In fact the S&P 500 and Dow Jones are approaching 18 month highs at current levels.

With the recent Fed meeting leaving rates unchanged for bank inter-borrowing, it is clear the Fed is keen to provide as much stimulus as necessary to avoid any possible double dip recession.

Hiring and employment data continue to show incredible weakness – despite relative improvement form 2009 levels. Nevertheless the Eurozone and US continue to shed jobs and the unemployment rates remain stubbornly high.

Despite Fed intervention in the economy through massive bond purchases and consequently keeping mortgage rates low – it is clear that the increased stimulus and money supply is not leading to much inflationary pressure at this stage. The velocity of money remains very slow and much of the stimulus from the Fed is not being recycled into economic expansion. Rather much of the fed's intervention is leading to banks parking their excess capital overnight with the Fed, as opposed to lending it out.

Uncertainty in Washington over the Obama administrations new tax and health policies has led to many US companies holding back on capital expenditure and hiring. Over 10 million Americans are now out of work. Unemployment levels of 9.7% rise to almost 18% nationwide when coupled with under employment figures which include part-time workers or those wishing to work more weekly hours.

The lack of a Eurozone solution to Greece's fiscal imbalance and possible contagion to other Eurozone members – notably the PIIGS (Portugal, Italy, Irelands and Spain) – has put the Euro under recent pressure – trading at 1.35 to the US – 10% down from levels seen just 3 months ago. Uncertainty in the UK on the outcome of the forthcoming election and also record budget deficits there – has pushed Sterling to levels of 1.49 to the US$ - some 15% below levels seen late last year.

Although these weaker currencies should help boost UK and Eurozone manufactured exports, no fast turnaround is imminent.

Eurozone economic growth is expected to be far slower now than any US or Asian recovery and structural unemployment is growing across Europe.

Although US companies on the S&P 500 have mostly beaten market expectations regarding their earnings, much of this is on the back of once off expenditure cuts. Top line growth remains anemic at best.

The Pacific region gained 1.7% for the month (US$) – when excluding Japan, the region in fact gained a full 2.7% for the period. The Hang Seng and Nikkei are both trading consistently above the 20,000 and 10,000 levels, respectively.

The MSCI World Index gained 1.2% for the month and is now down 3.0% for the year – up 50.9% over the past 12 months. In US$ terms the EMU is down 3.7% for February or 11.1% for 2010.

The US REIT (listed property) market posted a positive 5.7% return for February and is now up 99.9% over the past year.

It is clear the US financial system will continue to see failed banks and the real estate meltdown (specifically commercial properties) will persist for another 12-18 months – when prices are expected to bottom out. Another looming concern is the refinancing of massive amounts of commercial real estate and private equity transactions over the next 24-36 months which will test the robustness of the recovery.

Global Bond outlook

Although the Fed raised the US discount rate earlier this year – the rate which it lends money to banks by 0.25%, as expected no further rate hikes were announced by mid March.

The lack of inflationary pressure and lack of bank lending seems to have put the threat of inflation to one side for now.

Given the tenuous nature of the residential and commercial real estate markets in the US, the Fed has no desire to make mortgage finance more expensive for prospective borrowers – thus the Fed's support of the mortgage markets through the purchase of mortgage securities while being dramatically reduced will not evaporate as some analysts suggest.

The Fed holds large swathes of US bond market securities to prop up the mortgage and corporate bond markets. Given the weak economic recovery expected and problems in the real estate industry in particularly, the Fed will not likely unload its holdings as fast as some predict. Nevertheless at a minimum the lack of Fed buying power will likely lead to increased US mortgage rates and rates at the long end of the yield curve.

The Federal Reserve remains hawkish on raising interest rates anytime soon – most recent Fed statements indicate that the risk of inflation is viewed as very minor considering that some 10 million Americans are now out of work. The US economy needs to generate 100,000 new jobs a month simply to keep pace with the number of new job seekers.

Higher US bond yields are expected as the Yield curve steepens further by year end. It is possible that the 10 year Treasury rate currently at 3.75% approximately may exceed 5.5% by year end.

February proved a fairly flat month for the global government bond market – with this global bond benchmark gaining just 0.3% although it is up 10.9% over the past 12 months.

By comparison the European government bond market gained 1.2% in Euros for the month and is up 6.5% over 1 year.

In the Eurozone, rate hikes are no longer seen as an option given the fallout over sovereign debt risk. The ECB has continued to push back the target date of any likely hikes until well into the later half of the year.

A 2nd wave of US foreclosures is only now beginning to hit as further layoffs effect the market. Currently 1 in 5 US home owners are behind on their mortgage payments or are affected by negative home equity. Persistent high unemployment rates will continue to dampen any real estate recovery well into late 2010. Unemployment losses are expected to peak by mid 2010.

A sustained global economic recovery remains under threat due to huge structural deficit problems in certain Eurozone countries including the UK, Greece, Spain and Ireland. The US is expected to recover far quicker then the Eurozone. It is hoped that Asia will outdo both these old world economic regions.