GinsGlobal Index Funds

Investment Outlook – September 2009

Global Equities

Global Equity markets posted a 4.0% gain in September based on the MSCI World Index return. For the year it is now up 24.9% in 2009, and down -2.3% over the 12 month period. Given the continued nervousness and economic weakness, the rebound since the March 9th lows remains impressive.

Given the major US employment cuts (7 million since the start of the recession) and cost savings amongst the leading publicly listed companies, the 3rd quarter earnings season has resulted in some impressive bottom line improvement; mostly through these cost cutting measures. By mid October it was little surprise that the Dow therefore powered through the 10,000 level which is symbolically important. Still further gains are expected in the US equity market before year end. It is however worth noting that the market is pricing in the end of a recession as of the 3rd quarter in the US. The weaker US$ is also playing a major role in the US market's resurgence –given that more than half of the earnings from US companies in the S%P 500 originate from abroad. Thus a weaker dollar helps US exports and results in currency gains (boosting foreign earnings) - directly affecting the bottom line.

The S&P 500 is expected to exceed the 1200 levels within the next month or two. Other key indices such as the FTSE 100 – above 5100 levels, the Nikkei above the 10,000 level, the Dax at 5600 levels and the Hang Seng recovering to almost 23,000 – show that a worldwide recovery story is in the offing. The US is still expected to exit the recession quicker than most of Western Europe.

US unemployment numbers remain stubbornly high at 9.8% while certain states such as California and Michigan now top 12%. In the US the decline in employment is the worst on record since World War 2. The Obama administration remains under immense pressure to provide stimulus, however in the face of a record deficit no further stimulus is expected.

The Federal reserve remains hawkish on raising interest rates anytime soon – most recent minutes point to rates remaining on hold until mid 2010. Currently the Fed Fund rate is 0.25% which has helped boost bank profits this year. Large banks are still hoarding much of their cash and have dramatically reduced commercial property lending. Any increase in interest rates will have a hugely negative effect on property markets. Fortunately the spectre of inflation remains muted for now.

A continued bullish outlook for the commodity market is expected to boost emerging markets leading indices over the next 6-12 months. During the 3rd quarter the MSCI Emerging Markets Index rose 20.9%, translating into a year to date performance of 64.5%. Oil demand is expected to increase with oil prices trading in a $75-90 band over the next 2 quarters.

For the month of September, the broad US Market (MSCI USA) grew 3.8% and is now up 19.3% for the year. By comparison the MSCI EMU (Eurozone) rose 4.4% in euro terms for the month and is now up 24.0% for the year. In US$ terms this translates into a very impressive 2009 return of 26.6%. The US REIT market posted a 7.0% gain and is up 17.7% for the year.

The global market excluding the US, as measured by the MSCI EAFE rose 3.6% for the month and is now up 25.5% for the year in US$ terms. Pacific markets (MSCI Pacific) gained 1.7% for the month and are up 21.4% for the year in US$.

It is clear the US financial system will continue to see failed banks and the real estate meltdown will persist for another 12-18 months – when prices are expected to bottom out. Over 150 smaller US banks are expected to have been closed by year end. To date the number is 99.

Global Bond outlook

The end of the US recession is officially expected to be at the end of the 3rd quarter 2009. This would make it the longest post war recession with the deepest percentage cuts in employment in over 50 years. The reduction of bank lending and related liquidity (credit cards, mortgages being limited) – will lead to a dramatic reduction in consumer spending – normally accounting for 70% of the US economy. US household debt has stopped rising; a sure sign that consumers are cutting back at a feverish pace. Thus any recovery is expected to be anemic at best, with mostly a jobless recovery envisaged throughout 2010.

Fortunately the threat of inflation is barely visible to the Fed, so this will help low rates to endure until well into 2010 - fueling the nascent economic recovery and assisting that the real estate market regains its footing.

The Fed and ECB are withdrawing their quantitative easing measures as the private sector begins to pick up the slack once more. The US government will no longer guarantee money market funds or other bond purchasers by the end of the year.

The Fed has to still convince the market that it is not going to let inflation loose, so no rate increase is planned for as long as possible – likely mid 2010 at the earliest. Bernanke is likely to simply remove the Fed's own spending and enlarged balance sheet purchases and related interventions by Christmas.

US economic recovery is sluggish at best, and any significant recovery is now being put off until mid 2010, although the longest running recession in 30 years is expected to officially terminate before year end.

Recently US Government bond yields began a pick up – especially the 10yr Treasury Note reflecting possible fears of inflation. The bad news is that the mini mortgage refinancing boom that was kicked off earlier in the year after the Fed's entry into the bond market drove rates downward - has since fizzled out with mortgage rates recently jumping as much as 1% on 30yr fixed loans – to 5% levels. Larger mortgages above the $417,000 threshold of Fannie Mae have moved up beyond 6.2% which is stifling activity at the top end of the market.

Meanwhile a 2nd wave of US foreclosures is only now beginning to hit, as further layoffs affect the market. Rising unemployment will continue to dampen any real estate recovery well into late 2010. Unemployment losses are expected to peak by mid 2010.

Spreads on corporate, high yield and municipal bonds over governments have come down dramatically over the past quarter as well as LIBOR spreads. This new normalcy has led to steady bond returns the past few months.

The European Government Bond Index gained 0.6% for the month and has gained 4.3% for 2009. The index is now up 10.7% for the 12 month period. The World Government Bond gained 2.3% for the month and is now up 4.6% for 2009 and 13.8% over the past 12 months.