Investment Manager Commentary

End 3rd Quarter 2009

Q3 proved to be one of the best for many years, with all risk markets benefiting, following a pause in June. To an extent, markets are recovering from the dramatic falls seen this time last year, and through the Spring of this year.

A policy of zero interest rates combined with quantitative easing have caused investors to increase their appetite for risk; money on deposit earns nothing, and is unlikely to do so for some considerable time. So the hunt has been for assets that produce income, now that the financial system is unlikely to implode.

This remarkable turn in fortune seems to have been encouraged by a string of positive surprises, with companies delivering figures exceeding very low expectations, and background economic data being read as supportive, or at least presented as such. Without doubt, economic activity has picked up, inventories having been reduced to the bare minimum through the end of last year. Stimulus programmes have also helped, such as scrapping old cars, but arguably, this has only brought forward future demand.

Excess capacity and rising unemployment has kept the lid on inflationary pressures, and has thus provided a very supportive background for fixed interest investments. With banks unwilling to lend, companies have bypassed them, and headed straight for the credit markets; bond issuance has surpassed corporate loans, year to date. Importantly, these new issues come with much stronger covenants than previously, to the benefit of investors.

Looking back at the end of Q3, we have reached a point where many, but not all, asset classes have seen a V shaped recovery in value pending confirmation that the underlying data is supportive.

Outlook

The pickup in activity is, of course, very welcome whether it be as a result of restocking, or genuine recovery. Given the huge amounts of cash sitting on the sidelines, asset prices could yet go higher. However, only an increase in top line sales will drive future growth, which is what concerns us.

Consumers are laden with debt, and the prospect of increasing unemployment looms as governments hack back spending. Banks are constrained in lending, and will suffer further losses in property and domestic loans. Against this kind of headwind, there is scope for disappointment and we thus maintain our cautious stance.

CDO

October 16th, 2009