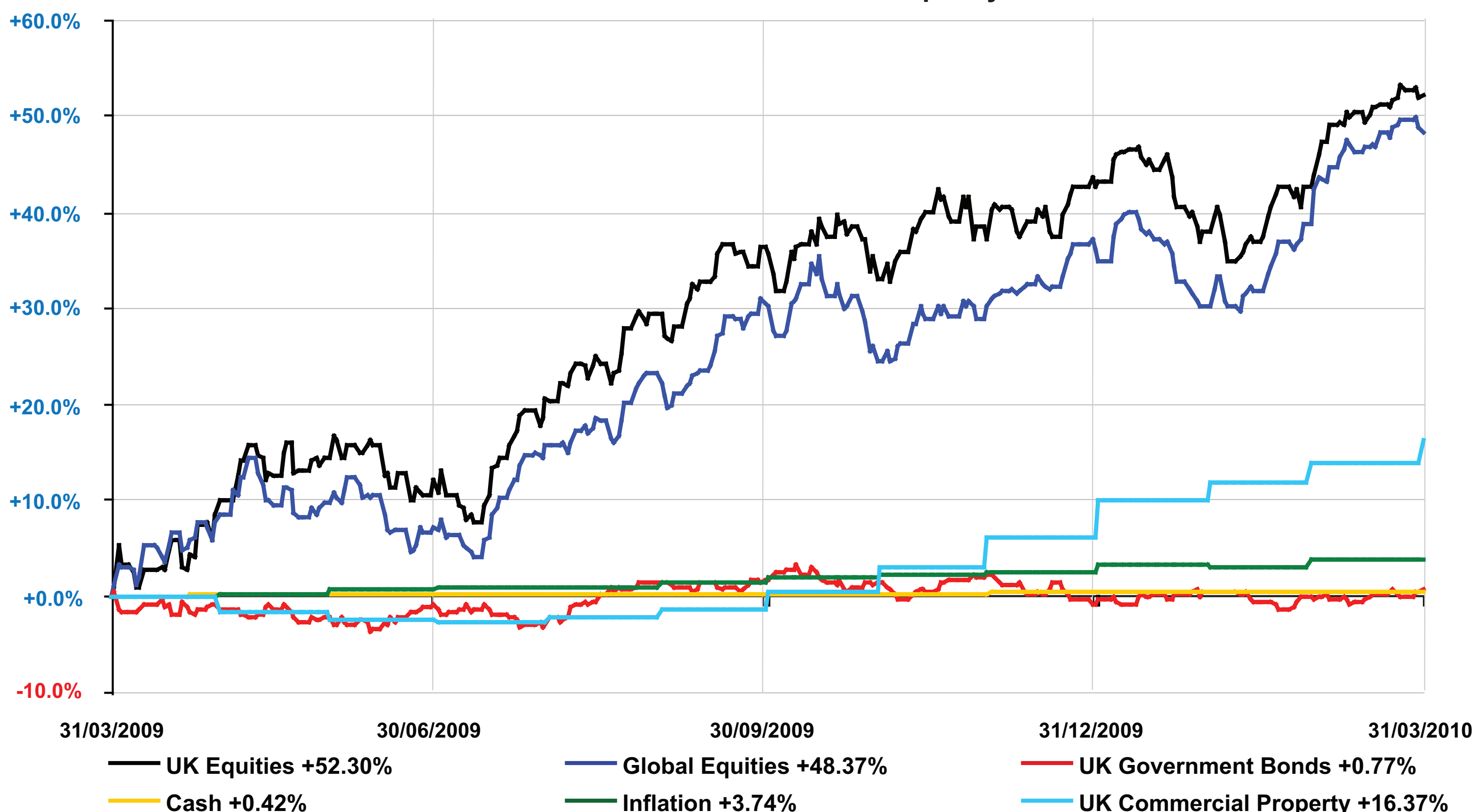
CCLA INVESTMENT MANAGEMENT LTD
MARKET REPORT MARCH 2010

Summary

- International equity markets had another positive month.
- Bond returns also were positive, corporate bonds performed better than government stocks, with longer dated and lower quality issues the preferred areas.
- Property values advanced again, bringing a positive quarter to a close.
- Sterling was mixed, losing ground against the US dollar but improving against the euro and yen.



Sources: Bloomberg, IPD: FTSE All-Share Total Return Index, FTSE All-World Total Return Index, FTSE UK Govt All-Stocks Total Return Index, IPD Monthly Total Return Index*, 7 Day LIBID, Retail Price Index* (*lagged a month to give a contemporaneous picture).

Review

Global equity markets produced positive returns in March. The FTSE All World Index enjoyed a total return over the month of +6.95%, bringing the return over the past 12 months to +48.27% to a sterling based investor. This performance was matched by that of the domestic market. The FTSE All-Share Index returned +6.76%, boosted by the return on medium sized companies (+9.59%) but held back by smaller companies which, with a gain of just +1.10%, continued to lag. Within the market, investors favoured ‘growth’ companies in the tug-of-war with the ‘value’ alternatives.

The range of performances across the regions was narrow. Asia had the best gain, with a return of +7.98% but no market was too far behind. The return from Europe was +7.32%, from the USA +6.37% and from Japan +5.53% - although this comparison suffered from currency factors, as sterling showed sudden strength relative to the yen. Of the various individual countries, Europe’s best performance came from Finland (+13.28%), the worst from Belgium (+3.27%). In Asia, Thailand gained most (+14.14%) and New Zealand was the laggard (+4.31%).

In fixed income markets gilts gave a slightly positive return (+0.80%) but corporate bonds were stronger, with longer dated and lower rated issues most sought after. The iBoxx Non-Gilt BBB Index returned +2.69%, the Over 10 year Index +2.59%.

Values advanced again in the property market, the estimated total return over the month was +2% (it will be some weeks before the actual indices are published). This would mean gains of c.+ 5.5% over the first quarter, suggesting that the long bear phase suffered by the sector is now firmly in the past.

Sterling had a mixed performance. It fell slightly against the US dollar (-0.35%) and moved higher against both euro (+0.57%) and yen (+4.69%). Over the past year sterling has been relatively stable but overall has improved against all three major comparators, gaining +6.01% relative to the dollar, +3.97% relative to the euro and +0.13% relative to the yen.

Domestic economic news has continued to illustrate a frail and uncertain recovery. Although activity levels seem to be edging higher, data lacks consistency and is more reflective of a change in trend than an established move back to sustained expansion. One piece of unequivocal disappointing news was on the balance of trade which deteriorated, despite the sharp falls in sterling in 2008 and early 2009.

Little serious attention was paid to the Budget, with most commentators regarding it more as political theatre than a serious economic event, an opportunity to announce the availability of £100m to remedy potholes but not to disclose how the budget shortfall will be closed. In the support documentation there was some interesting if troubling statistics on the projected growth in public debt levels. These have doubled to £857 billion over the past five years and are expected to rise to £1,400 billion by 2014. On current interest rate assumptions this will create an annual interest bill of £1,000 per annum for everyone in the UK.

The picture of a slow improvement in activity levels been mirrored in Europe and the United States and the authorities in both areas have signalled an intention to keep interest rates at low levels for the foreseeable future. Despite reluctance from some participants, a consortium was cobbled together to support Greece and with a safety net in place, it was possible to press ahead with the debt issuance programme – but at a price. The latest bonds were sold at an interest rate of 5.9%, far too high to be affordable over the medium term given the financing obligations which lie ahead. The support programme for Greece should be viewed as a victory, but in a battle, not a war. Over the past year governments have effectively solved the credit crisis but not the debt crisis and the problems of excess debt will continue to pose very significant challenges for some years to come.

Outlook

With an election in the UK only weeks away economic policy announcements are likely to be sparse. International news should be supportive but not dramatically so, this recovery will be slow to ignite relative to past upturns. Equity markets are likely to remain volatile but we expect the underlying uptrend to remain in place. Property also should continue to improve as valuations normalise after the sharp markdowns of 2008 and early 2009. We remain cautious of bonds. This sector has underperformed equities very substantially over the past year and could stabilise near term. Our concerns however look beyond this and so we would be sellers of any rally. Sterling is reasonable value on purchasing power parity valuations but is vulnerable to political developments and disappointing economic news.

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