

GENERAL INVESTMENT CLIMATE

The Economy

The past months the macro-economic signals were somewhat contradictory.

On the one hand, the American jobless figures deteriorated unexpectedly and confidence indicators declined. On the other hand the housing market in the US seems to be bottoming out and orders for durable goods rose unexpectedly.

In Europe, German producer confidence, as measured by the IFO index, rose to its highest level since June 2007 in September. German unemployment fell to the lowest level since 1992.

The general expectations are that, although we will most probably escape the feared double dip (back fall into recession), a long period of low economic growth has set in.

The American economy cooled down stronger than expected the past months. Economic growth in the second quarter slowed down to 1.6% on an annual basis. For the third quarter economists don't expect any improvements. For the full year 2010 the economy would only grow 1.6%. The weak labour market, with unemployment at 10%, remains the Achilles heel of the American economy.

The hesitant recovery in the US contrasts sharply with Europe, where Germany keeps the engine running. Growth expectations for the European Union were reviewed upwards, from 1% growth in 2010 to 1.8%, notably thanks to Germany, where an economic growth of 3.4% is expected for 2010, compared to only 1.2% previously expected.

There is a striking difference between the core countries of the European Union, which came through the crisis relatively well, and the peripheral member states, such as Greece, Portugal, Ireland and even Spain, that recently saw its credit rating lowered.

Notably Ireland is facing huge problems. The fairy tale of the Celtic Tiger is over. The country now has to pay the price for an overproportional financial sector (the assets of the Irish banks are seven times as big as the Irish GDP) and the associated property bubble. With billions of euros being injected in its zombie banks, the Irish budget deficit will rise to an astonishing 32% of GDP this year.

Mid September, central bankers and supervisors of the western countries finally reached an agreement over new and more severe banking rules, in order to prevent a new credit crisis. Three European watch dogs will be created, for banks, insurance companies and financial markets respectively. However, we are still far away from a true European financial supervisor.

As these so-called Basel III standards are less severe than expected, and the banks have ample time (until January 1, 2018 at the latest) to strengthen their capital reserves, mounting concerns over the financial sector ebbed away again (bar some specific cases such as the Anglo Irish Bank).

Core inflation in the US stabilized at 1.4% in August, quite some way below the "optimal" inflation level of 1.7-2%. In the Eurozone, inflation is currently no reason for concern. In September, inflation is expected to be 1.8%.

Continuous uncertainty at the financial markets and the weak dollar have caused the gold price to reach a new all-time high; for the first time in history, the level of 1,300 dollar was broken. The silver price is at its highest level since thirty years (\$21.38 per ounce).

The oil price keeps fluctuating around \$75 the past months. Both producers and consumers seem to be happy with an oil price between \$70 and \$80.

Money markets and exchange rates

The major central banks left their interest rates unchanged. For nearly one and a half years now, interest rates are at exceptionally low levels.

The American central bank has meanwhile announced a new round of quantitative easing. As inflation and economic growth are low, the Federal Reserve deems it necessary to pour money into the economy by purchasing treasury bonds. Amounts of 500 to 1,000 billion dollar are circulating.

The European Central Bank has excluded a new easing of its monetary policy.

These opposite developments obviously have their repercussions on the exchange rates. In September, the euro broke through the 1.35 dollar barrier for the first time since April. On a quarterly basis, the euro rose over 11% against the dollar. However, this tells more about the weakness of the dollar than about the strength of the euro.

The continued uncertainty has caused investors to run to save currencies, notably the Swiss franc and the Japanese yen. The latter reached its highest level against the dollar since 1995 in September. The Swiss franc is at record highs, both against the dollar as against the euro.

The German long-term interest rate declined further, to the historically low level of 2.25%.

Stock Markets

Table 1.1 - General

	30/sep/10	30/jun/10 - 3 mth	31/mrt/10 - 6 mth	31/dec/09 - 9 mth	30/sep/09 - 12 mth
AEX	334,39	5,55%	-2,86%	-0,28%	7,40%
BEL20	2589,73	8,51%	-2,22%	3,11%	4,19%
DAX	6229,02	4,42%	1,23%	4,56%	9,76%
EU50	2747,90	6,78%	-6,25%	-7,32%	-4,34%
DJ	10788,00	10,37%	-0,63%	3,45%	11,08%
SP500	1141,20	10,72%	-2,41%	2,34%	7,96%
Nasdaq	2368,62	12,30%	-1,22%	4,38%	11,60%
EUR/USD	1,3633	11,41%	0,92%	-4,84%	-6,87%
EUR 3 months	0,8920	0,1250	0,2580	0,1920	0,1390
EUR 10 year	2,5100	-0,2980	-0,8170	-1,0450	-1,0010

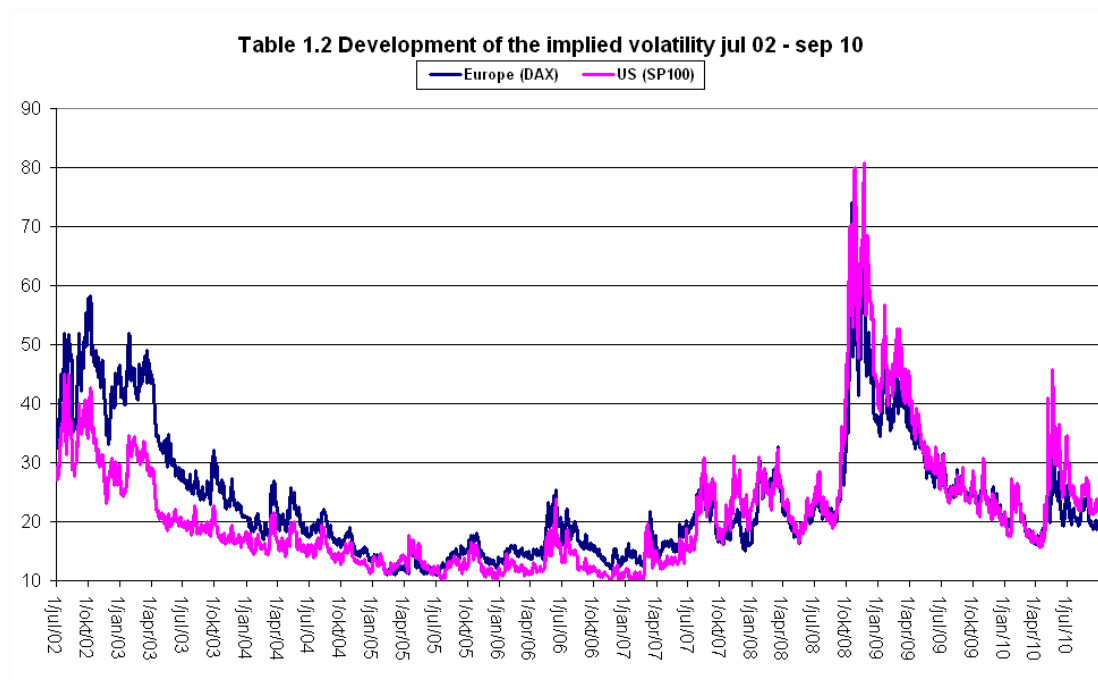
The stock markets showed a versatile pattern over the past months. The gains of July were wiped out again in August, but a very strong month of September resulted in nice quarterly gains. This partly compensated for the very weak second quarter, with most markets now back at the levels of the beginning of the year.

The European stock markets gained around 5% over the past quarter. Their American counterparts performed noticeably better, with gains of 10% and more, benefiting from the weakness of the dollar. September 2010 was even the strongest September month for Wall Street since 1939.

With the exception of the ASCX, which gained 4%, the small- and mid-cap indices performed better than the main indices over the past quarter, with gains of around 10% for the MDAX and the AMX and up to 12% for the SDAX.

Implied volatility

The volatility at the stock markets slowly ebbed away again over the past quarter, dropping back to around 20%.



Long-term development

For about a year now the AEX is moving horizontally, within the range of 300 to 360 points. It remains to be seen when (and in which direction) the index will break out of this range. An upward break-out seems more likely.

