

BLACKROCK

Week in View - 13 February 2012

Latest market views from the BlackRock Multi-Asset Client Solutions Group

Market Movements

Over the past few days we have seen slight risk-off behaviour in financial markets. In particular, European equities are down by around 3% from their peak, given renewed concerns about Greek financing. Nevertheless, the main contours of market trends so far this year remain intact and overall we remain in a partial risk-on environment.

Since January risk-on behaviour has been very obvious in equity markets; developed market indices are typically up by between 5% and 10% and there have been strong returns in many emerging market indices. It has also been evident in currency markets where a number of emerging market currencies have appreciated, notably the Brazilian real and Indian rupee. Commodity markets have exhibited the trend to some extent, but industrial metals and gold which rose quite strongly in January have flattened out recently and the oil price has been broadly flat since the end of 2011. We have also seen risk-on behaviour in some peripheral European bond markets where there have been material declines in Italy and Spanish bond yields. Also, over the past week the Portuguese ten-year bond yield has fallen from 17% to 12%, which is a helpful development, although 12% is still unsustainable over the long term.

However, high quality government bonds have bucked the risk-on trend. In the UK and Germany ten-year yields have remained very close to the low points reached last autumn. This is an interesting feature, as over the past few years when risk assets have been rising strongly, typically bond yields have climbed. In the current period, risk assets have enjoyed reasonable returns but bonds have not sold off.

The rally so far

However, an important driver of the risk asset rally has been the behaviour of central banks: a generous liquidity provision from the European Central Bank, additional quantitative easing in the UK, the Federal Reserve extending the period in which very low interest rates are likely to remain and the first signs of easing in a number of larger emerging markets. This central bank activity has helped to lower bond yields directly but also has reduced some of the downside risk to economies and markets as well as modestly enhanced growth expectations. We think the fundamental correlation between bond and equity returns is likely to remain negative in the medium term, but while central banks are pivotal in supporting risk assets we may see that correlation weaken in the short term.

Better macro numbers worldwide have also supported the recent strength in risk assets. Nonetheless, it is only really in the US that we have seen a discernable acceleration in growth from a low point in the middle of last year. Elsewhere we have seen some moderation in declines, but these are yet to be replaced by clear re-accelerations. This is particularly evident in Europe where there have been better numbers from Italy and Spain, but they have not been strong enough to suggest the economies have turned a corner.

In emerging economies the overall picture is one in which a sharp slowdown has given way to a flatter period, but there has not been hard evidence to suggest the recovery in the US is broadening out into the rest of the world. Overall, the macro background is not great, but in aggregate there has been some more forward momentum coming through which contrasts very strongly with the concerns of global recession so prevalent last summer. Technical factors have also played their part in the recent rally. We believe investor positioning last autumn became very conservative and

investors had high cash ratios. Some of this cash has been dribbling back into markets, largely because risk premia have been fairly high. In many markets the rally has been pretty low volume, so our feeling is that there is still some cash on the sidelines which could yet start to come through and be invested.

What's next?

Looking ahead, we have a pretty high conviction that loose monetary stances will persist worldwide. There may not be much additional activity in developed economies but we could see much broader easing coming through in some of the larger emerging economies. We expect headline inflation will fall quite sharply in both the developed and emerging worlds as the impact of previous high commodity prices falls away.

We still have concerns about the European economy which is struggling to keep its head above water and faces the challenges of tight fiscal policy and a banking system which is under considerable pressure. It is hard to see a great deal of momentum from Europe over the next few months and some form of mild recession remains the most likely outcome. However, we think the reacceleration in the US economy looks sustainable and we expect to see better growth numbers from the larger emerging economies over the course of the year. Overall, the global macro environment is unlikely to be great, but there is scope at the margin for it to get slightly better from where we are now.

Conservative positioning and the low volume of the rally so far may support more money coming into the markets. However, it is worth emphasising some of the low valuations and high risk premia which were around last autumn have been eroded. Equities are closer to fair value, but remain better value than bonds as yields are low. Bond yields are likely to remain low while central banks persist in such a permissive mode. There is also a large amount of event risk around, such as the current situation in Greece. Elsewhere over the

course of the year, Middle East, US and European politics have potential to generate some pretty big market moves. Overall we still view this as a patchy risk-on environment but given recent moves, the coming weeks and months may feel more patchy than the strong risk on behaviour of the start of 2012.

Highlights for the Week Ahead: 13-17 Feb Economic Diary:

Monday: Japan GDP

Tuesday: US retail sales; Euro area industrial production; Brazil retail sales.

Wednesday: US industrial production; Euro area industrial production; Germany ZEW business survey; Germany, France, Italy, Belgium, Netherlands GDP.

Thursday: US FOMC minutes.

Friday: US leading indicators; US CPI; Canada leading indicators.

Corporate Diary:

Companies releasing earnings reports this week include: platinum producer, Anglo American Platinum, steel manufacturer, ThyssenKrupp and gold miner, African Barrick Gold; cosmetics and beauty company, L'Oreal; financials, Banco do Brasil, BNP Paribas and Societe Generale; food companies, Nestle and Danone; autos, General Motors and Renault; beverage firms, Heineken, Pernod Ricard and Molson Coors Brewing; and, defence and aerospace company, BAE systems.

Market Movements*

| Equity Markets* | 10 Feb 2012 | % Change |
|-----------------|-------------|----------|
| S&P 500 | 1342.64 | -0.17 |
| NASDAQ | 2903.88 | -0.06 |
| TSE 1st Section | 779.07 | 2.42 |
| FTSE S&P World | | |
| Europe | 307.51 | -0.96 |
| FTSE All-Share | 3024.62 | -0.75 |
| DAX | 6692.96 | -1.09 |
| Hang Seng | 20783.86 | 0.13 |

| | | |
|---|--------------------|-------------------|
| Eurostoxx 50 | 2480.755 | -1.37 |
| Bonds | 10 Feb 2012 | % Change |
| Citi World Govt Bond Index All Maturities | 611.7134 | -0.08 |
| Bond yields ** | 10 Feb 2012 | 3 Feb 2012 |
| US | 1.929 | 1.949 |
| Japan | 0.98 | 0.95 |
| Germany | 1.939 | 1.892 |
| UK | 2.134 | 2.18 |
| Currencies | 10 Feb 2012 | 3 Feb 2012 |
| USD/EUR | 1.3189 | 1.3122 |
| GBP/EUR | 0.8373 | 0.8305 |

| | | |
|-------------------------------|--------------------|-----------------|
| JPY/USD | 77.64 | 76.585 |
| USD/GBP | 1.5752 | 1.58 |
| JPY/GBP | 122.2986 | 121.0043 |
| Commodities | 10 Feb 2012 | % Change |
| Oil (Brent Crude) | 118.01 | 4.89 |
| Commodity Futures (CRB) Index | 585.6 | -1.43 |
| Gold | 1722.2 | -1.19 |

*Equity, currency and bond markets measured over seven days, from previous Friday's close to Friday's close. All index returns in local currency terms. All equity index returns are price only. **Bonds: 10-year yield. Past performance is not a guide to future performance. The value of investments and the income from them can fall as well as rise and is not guaranteed. You may not get back the amount originally invested. Changes in the rates of exchange between currencies may cause the value of investments to diminish or increase. Levels and bases of taxation may change from time to time. Issued by BlackRock Investment Management (UK) Limited (authorised and regulated by the Financial Services Authority). Registered office: 12 Throgmorton Avenue, London, EC2N 2DL. Registered in England No. 2020394. Tel: 020 7743 3000. For your protection, telephone calls are usually recorded. BlackRock is a trading name of BlackRock Investment Management (UK) Limited. Issued in Switzerland by the representative office, BlackRock Investment Management (UK) Limited (London), Zurich Branch, Claridenstrasse 25, Postfach 2118 CH-8022 Zurich. Issued in Singapore by BlackRock (Singapore) Limited. For further information, the prospectus, simplified prospectuses, annual report and semi-annual report can be obtained free of charge in hardcopy form from the Austrian paying agent: Raiffeisen Zentralbank Osterreich AG, A-1030 Vienna, Am Stadtpark 9. Issued in Hong Kong by BlackRock (Hong Kong) Limited. This material has not been approved by the Hong Kong Securities and Futures Commission for public circulation and can only be provided to "professional investors" (as defined in the Securities and Futures Ordinance (Cap. 571 of the laws of Hong Kong) in Hong Kong. Issued in Singapore by BlackRock (Singapore) Limited. The Fund is only available to "institutional investors" (as defined in section 4A of the Securities and Futures Act, Chapter 289 of Singapore) in Singapore. The Fund has not been and will not be registered with the Securities and Futures Bureau of the Financial Supervisory Commission in Taiwan and any offering of the Fund in the territory of Taiwan or to Taiwanese investors must be subject to the selling restrictions under applicable law and regulation. This material may only be distributed to Professional Intermediaries. The views expressed herein are as of 16.05.11, and do not constitute investment or any other advice; the views are subject to change and do not necessarily reflect the views of BlackRock as a whole or any part thereof.