

February 3, 2010

The main points at a glance

Bonds	→
Equities	↗
Hedge funds	→

Projections at 6 months

The economic recovery is continuing to varying degrees. While good news is at last emerging from the principal developed countries, Asia is confirming its role as the engine of the global economy. In this respect investors' reaction to the prospect of monetary tightening in China says a lot about the role that this Asian giant now plays for the global economic and financial system. The mere thought of an interest-rate hike in China (which is in fact desirable) has rendered the markets more nervous.

The discussions about the need for regulation of the banking sector and the revival of concern about the explosion of public debt did the rest, engendering a significant return of risk aversion. After a good start to the year, the stock markets thus fell back during the second half of the month of January. Fixed-income securities, in contrast, managed to perform well, particularly in the corporate bonds segment, as the yields on certain "bad" sovereign issuers had soared. In the foreign-exchange market, the dollar and the Swiss franc have regained their safe-haven status, while the euro has suffered from the situation in some peripheral countries.

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A publication of the *Research & Analysis* team
Banque SYZ & CO SA
 Tel. +41 (0)22 819 09 09
 info@syzbank.ch

Authors:
 Yasmina Barin
 Enrico Bolzani
 Fabrizio Quirighetti

Economy

United States	2
Increase in GDP: it's not just artificial!	
Europe	3
The recovery continues but not everywhere	
Japan	4
Strong growth at the end of 2009	
Emerging economies	4
China: a first step in the right direction	

Markets

Equities	5
An air pocket but fundamentals are intact!	
Bonds	5
PIGS under scrutiny	
Exchange rates	6
The euro under pressure	

Asset allocation

Allocation grid	7
The proportion of equities has been raised	

Economy

The economic recovery continues. In the advanced countries, the indicators published at the beginning of this year point to a marked rebound in the United States and the main countries of the euro zone. Among the emerging countries, Asia clearly stands out as the leading engine of the global economy. In this respect investors' reaction to the prospect of monetary tightening in China says a lot about the role that the Asian giant now plays for the global economic and financial system.

The recovery of activity, which is materializing earlier than expected, has, moreover, prompted the IMF to raise its growth forecasts. Global GDP should grow by 3.9% in 2010 (+0.8 points compared with the forecasts made in October 2009), owing in particular to the strong rebound of the emerging countries (+6%), including Asia, which is playing a predominant role (+8.4%).

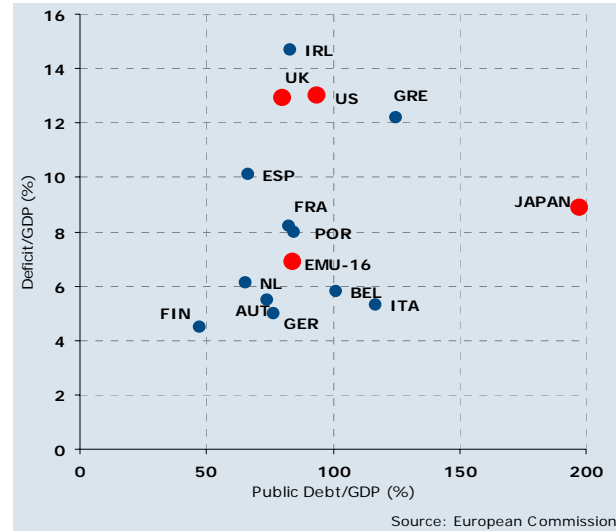
THE IMF'S NEW GDP GROWTH FORECASTS

	2009	2010	2011
WORLD	-0.8	3.9	4.3
ADV ECO	-3.2	2.1	2.4
United States	-2.5	2.7	2.4
Euro area	-3.9	1.0	1.6
Japan	-5.3	1.7	1.2
EM	2.1	6.0	6.3
Africa	1.9	4.3	5.3
CEE	-4.3	2.0	3.7
CIS	-7.5	3.8	4.0
Developing Asia	6.5	8.4	8.4
Middle-East	2.2	4.5	4.8
LATAM	-2.3	3.7	3.8

Source: IMF, WEO update January 2010

At the same time the first month of the year has also been characterized by a revival of fears over sovereign risk. Whereas in the past the explosion of public debt was a phenomenon confined to the emerging countries, it is currently indebtedness in the developed countries that is causing concern. In spite of an aggregate situation better than that of the United States, the United Kingdom or Japan, the euro zone is being particularly weakened owing to the worries over the peripheral countries, such as Portugal, Spain, Ireland or, above all, Greece, which has come under particular scrutiny from investors. This bad press is resulting in particular in a weakening of the single currency.

FORECASTS FOR DEBT AND PUBLIC DEFICITS IN 2010



In spite of a situation that is generally better than that of the other main economic areas, the situation of some peripheral European countries is weakening the euro zone and the single currency.

United States

The economic activity indicators published at the beginning of the year were a pleasant surprise and point to a swifter recovery of economic activity than that expected a few months ago.

First of all, the GDP figures for Q4 2009 suggest that the recovery is no longer being boosted by artificial factors. While more than half of the leap in activity of +5.7% (annualized quarter-on-quarter change) is attributable to the reversal of the inventory cycle, some encouraging signs are also coming from domestic demand. Household consumption is holding up (+2%) despite the discontinuation of specific measures designed to support private spending (such as the car-scrapping bonus). Moreover, residential investments increased for the second consecutive quarter, while investments in capital goods increased significantly (+13.3%). As for foreign demand, it also supported growth to the tune of 0.5%. In total, while the stimulus policies obviously continue to stimulate growth, the GDP details published at the end of last week are fairly encouraging. The inventory cycle is far from over, companies are beginning to invest again and households are regaining some confidence.

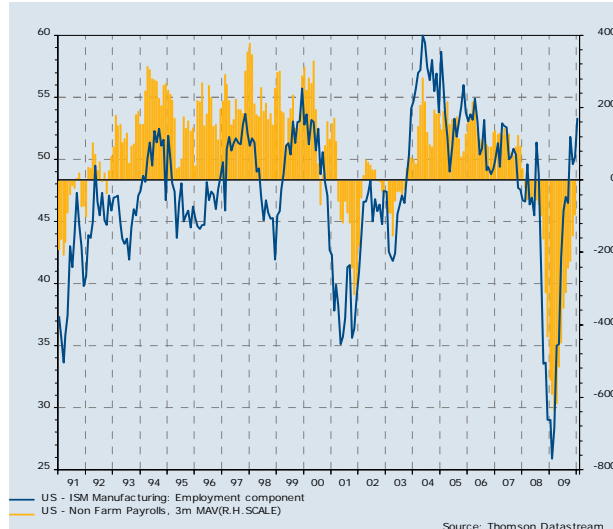
BREAKDOWN OF GDP GROWTH IN Q4

US GDP	Q4 2009		Q3 2009	
	Q/Q% ann.	Contrib	Q/Q% ann.	Contrib
Pers. consumption	2.0%	1.44%	2.8%	1.96%
Durable goods	-0.9%	-0.06%	20.4%	1.36%
Nondurable goods	4.3%	0.67%	1.5%	0.23%
Services	1.7%	0.83%	0.8%	0.37%
Priv Investments	39.3%	3.82%	5.0%	0.54%
Fixed investments	3.5%	0.43%	-1.3%	-0.15%
Non-residential	2.9%	0.29%	-5.9%	-0.59%
Structures	-15.4%	-0.52%	-18.4%	-0.68%
Equip & Softw	13.3%	0.81%	1.5%	0.15%
Residential	5.7%	0.14%	18.9%	0.43%
Chge in inventories		3.39%		0.69%
Net exports		0.50%		-0.81%
Exports	18.1%	1.90%	17.8%	1.78%
Imports	10.5%	-1.41%	21.3%	-2.59%
Government	-0.2%	-0.02%	2.6%	0.63%
TOTAL		5.7%		2.2%

Source: US Department of Commerce

It only remains to be hoped that the fleeting return of job creations observed in November will become sustainable over the next few months. Judging by the leading indicators published recently, the "employment" components of which posted significant gains, this should soon be the case with beneficial effects for the soundness of the economic cycle, even though it remains very difficult to accurately foresee the timing and intensity of the labour market recovery.

"EMPLOYMENT" COMPONENT OF THE ISM MANUFACTURING INDEX AND NON-FARM PAYROLLS



According to the leading indicators and in particular the "employment" component of the ISM manufacturing index, the US labor market is close to a turnaround.

Furthermore, the leading indicators published recently have all signalled a firming of the economy. Among them, the 3.5-point increase in the ISM manufacturing index (to 58.4) is particularly significant, because it is supported by the increase

in its "new orders", "production" and, as already mentioned, "employment" components.

The strength of the recovery does not appear at the moment to be altering the attitude of the Federal Reserve, which has emphasized once again its determination to keep interest rates sustainably low in an environment that is not conducive to a return of inflation. Despite the recent rebound in the consumer price index (to 2.7%), the exceptionally high level of the unemployment rate (10%) and blatant under-use of production capacity are acting as brakes to prevent inflation from getting out of control.

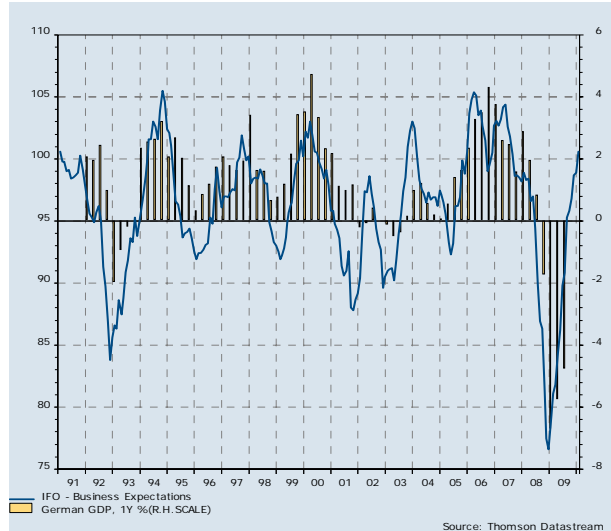
Europe

The recovery of the European economy is continuing at two speeds. On the one hand, the peripheral countries which are having difficulty in pulling out of recession, weighed down as they are by enormous budgetary imbalances and a glaring lack of competitiveness (Greece) or by considerable cyclical adjustments following the bursting of the real-estate bubble (Spain or Ireland). They contrast with Germany and France, which are benefiting from a much more favourable situation, thanks to the reversal of the global cycle (which is beneficial for German industry) or to automatic stabilizers that guarantee a degree of soundness (which is the case for France) in difficult times.

The recently-published sentiment indicators reflect this divergence, as is borne out by the German IFO business climate index, which has leaped up. This increase is particularly welcome since it helps to dispel fears of an imminent dip in the growth of Europe's largest economy. The "expectations for the next six months" component is particularly well-oriented and gives reason to hope that the growth rate will be fairly high over the first half-year. The European Commission's economic sentiment indicator (ESI) also mentions a gradual and swift return to normal for Germany and France, but at the same time reveals a much less flattering situation for Greece, Spain, Ireland or Portugal.

In the meantime the ECB has reiterated its determination to leave low interest rates in place. In this respect we do not see how the European monetary authorities could take a different line. First of all, the recovery remains generally fairly fragile. Then the recent increase in the inflation rate (to 1% in January) is a phenomenon set to be inverted as of this spring when the base effects due to energy prices will disappear. Finally, an interest-rate hike would be disastrous for the peripheral European countries.

GERMAN GDP GROWTH AND THE IFO'S "EXPECTATIONS FOR THE NEXT SIX MONTHS" COMPONENT



The recent leap in the IFO's business climate index for Germany and in particular in its "expectations for the next six months" component points to a continuation of the economic improvement in Europe's largest economy.

The last G7 country to move out of recession, the United Kingdom has at last posted some positive growth figures. It is, however, a very hesitant climb, as GDP increased by only +0.1% in Q4. Activity is likely to speed up in the course of this year, even though the road to recovery might be rather tortuous: a stricken financial sector, heavily indebted households and sharply rising public debt (which might encourage the authorities to raise taxes soon) will further undermine the British economy's growth in 2010. In this environment the Bank of England will leave its interest rates pegged at 0.50% and might even opt for an extension of the total amount of assets repurchased in the context of its quantitative easing.

The two principal leading indicators of the Swiss economy suggest an acceleration of activity in the course of the first half of this year. Both the KOF's economic barometer and the PMI index have turned out to be up, thus pointing to a rather marked recovery of the cycle, like that of Germany. As for the inhibiting effects of the strengthening Swiss franc, they will be more than offset by the recovery of the global economy, which is beneficial for Swiss exporters.

Japan

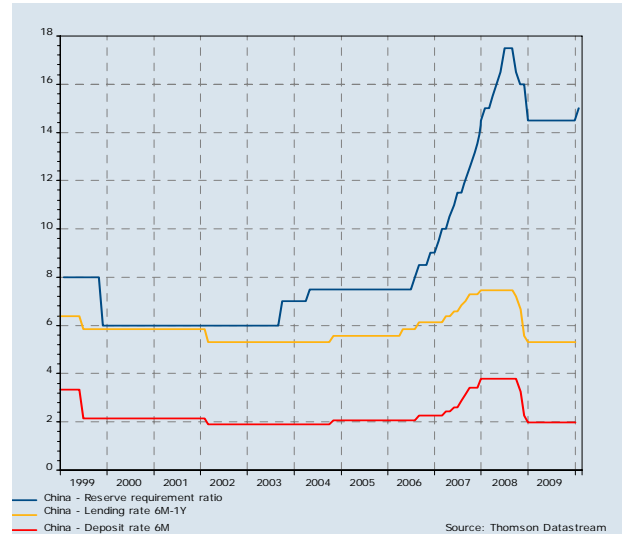
The economic statistics published in Japan reveal a high growth rate at the end of last year. The world's second-largest economy has come close to the brink. Despite the 10th consecutive monthly increase (+2.2% in December), industrial production

has recovered only half of the ground lost during the crisis. As for exports they increased by +2.5% in December but, here again, the drop they sustained last year was severe. The trade surplus that appeared to be earned in Q4 (exports increased by +10.1%, and imports by "only" 6.8%) should nevertheless significantly support GDP.

Emerging economies

The authorities might soon begin to turn the monetary tap by acting on two other fronts: a gradual interest-rate hike and resumption of the guided appreciation of the yuan against the dollar. The 0.5% increase in the ratio of compulsory reserves for Chinese banks (raised to 16.5%) is a first step in the right direction. But this decision is above all symbolic in nature and its consequences are emblematic. It sends a clear signal about the intentions of China's central bank, which appears to be determined to prevent any overheating of an economy that grew at an annual rate of +10.7% in Q4 2009. But the - fairly nervous - reaction from international investors to this decision says a lot about the role that China now plays in the global economic and financial system. It remains that, in our opinion, a monetary tightening in China is more than desirable at a time when the inflation rate is increasing and the money supply is growing ever more quickly.

COMPULSORY RESERVES RATIO AND INTEREST RATES IN CHINA

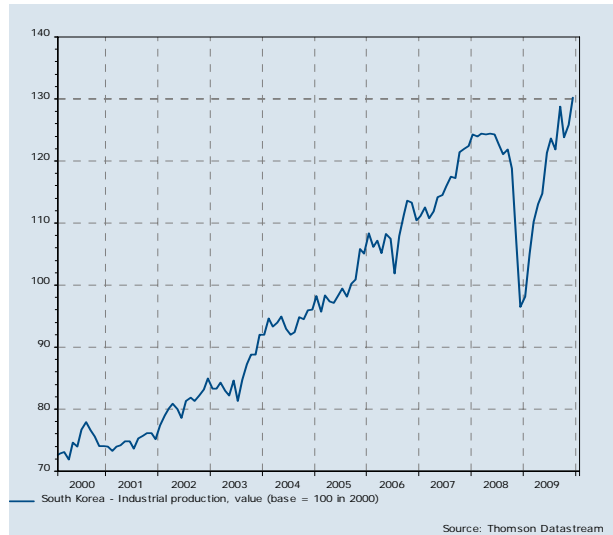


The decision to raise the ratio of compulsory reserves foreshadows a desirable tightening of monetary conditions in China

There is no need to stress that China's dynamism is beneficial for the whole of the Asian region. In this respect the weak GDP increase in South Korea (+0.2% in Q4) is only a temporary break following two quarters of very strong expansion. In this regard, the figures for industrial activity are impressive: it turned out to stand at +3.5% over the

month of December, taking to +33.9% the year-on-year gain. Thus the economic crisis will in the end only have been a passing blip for Korean industry, whose activity has rebounded strongly, attaining – in value terms – a level much higher than that of summer 2008... Benefiting from a strategic geographical and sectoral positioning (among the leaders for electronic products), Korean industry also benefits from an undervalued currency.

INDUSTRIAL PRODUCTION GROWTH IN SOUTH KOREA (IN VALUE, BASE = 100 IN 2000)



A passing blip, nothing more. That is the impact of the financial and economic crisis, even though it hit Korean industry hard. The latter's rebound over the last 12 months has been spectacular.

Markets

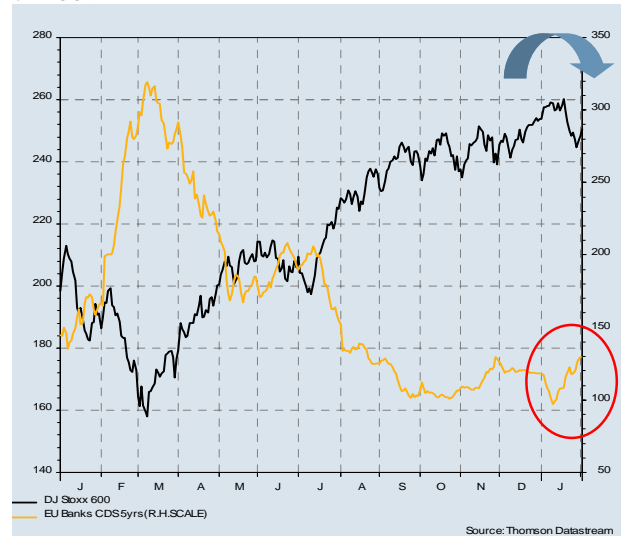
Equities

The month of January featured two stages. The first two weeks extended the positive momentum of 2009, given timely economic statistics. The next two weeks were weighed down by the prospect of monetary tightening in China, a new act in the tragedy of Greece's public finances and by the possible tightening of banking regulations in the United States. This caused a trend reversal, taking the international stock markets into negative figures since the beginning of the year.

In terms of sectors, we observed a better performance of defensive stocks over the period.

The food and pharmaceutical sectors stood out in view of a return of risk aversion. On the other hand, the stocks that were winners in 2009, that is banking and mining shares, were left in a vacuum. President Obama's speeches about an in-depth revamping of the regulation system governing US investment banks weighed heavily on their prices. As for the mining sector, it suffered from the fears over the possibility of monetary tightening in China and the impact this might have on the region's growth.

TREND IN THE EUROPEAN STOCK MARKETS AND THE COST OF PROTECTING EUROPEAN BANK DEBT SINCE THE BEGINNING OF 2009



The revival of fears about the European banking sector, as borne out by the increase in the cost of protecting debt (CDS) and the mistrust of Greek sovereign debt, weighed on the trend in European equities.

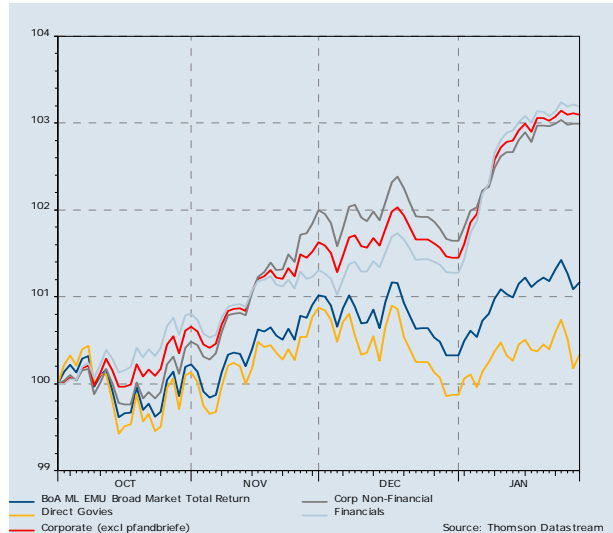
Our scenario has not been altered by the recent events. The general environment remains favourable. A large majority of the corporate earnings results published turned out to be above the market expectations, confirming the improvement in the trends. The economic news is pointing in the right direction. All this is taking place in a context of interest rates that should remain sustainably low both in Europe and in the United States. Finally, we think that a solution to the Greek debt problem will inevitably be found within the European Union. The next few weeks will be driven by the continuation of the corporate earnings season, the economic figures (mainly those on employment) and by the measures linked to the Greek "bail-out".

Bonds

The return of risk aversion, coupled with generally accommodative messages from the principal central banks, has benefited fixed-income securities, as is logical. Bonds denominated in pounds sterling or US dollars posted some very good performances, also owing to the once-again attractive yields offered after a difficult phase at the end of last year. Sovereign bonds in euros, for their part, have taken a slightly more tortuous route, harmed by the fears over the peripheral countries' debt. The cumulative debt of Greece, Portugal, Spain, Ireland and Italy accounts for just over 40% of public issues in the euro zone, which is well above these countries' share of GDP.

Worries about governments' indebtedness are in turn benefiting corporate bonds. Following a lacklustre end to the year, the month of January was very favourable for this asset class. The average performance of European investment grade (financial or non-financial) companies' debt was 1.6% over the first month of the year.

TREND IN THE PERFORMANCE OF BONDS IN EUROS



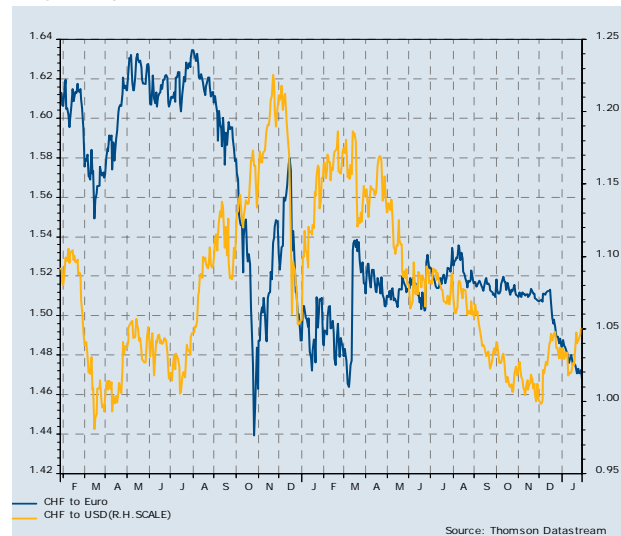
Corporate bonds have, paradoxically, benefited from the return of risk aversion, generated in particular by the worries over sovereign debt.

Exchange rates

The environment has been very favourable for the dollar at the beginning of this year. From an economic point of view, the economic statistics from the world's largest economy have substantiated the theory of a marked rebound of activity. The return of risk aversion has also driven the greenback, in particular against the euro, a victim of the public finances situation in certain European countries. Thus the single currency fell below 1.40 against the dollar. Furthermore until the problems of peripheral Europe are resolved (or as long as a viable solution does not emerge) the euro will remain vulnerable.

In this respect the appreciation of the Swiss franc against the euro is attributable more to the weakness of the single currency than to the strength of the Swiss currency. It is true that the Swiss National Bank has clearly decided to intervene at around 1.50 to support the Swiss franc, which is now trading at 1.47 against the euro.

EUR/CHF AND USD/CHF EXCHANGE RATES OVER THE LAST TWO YEARS



The strengthening of the Swiss franc against the euro is attributable mainly to the weakness of the single currency. The CHF has actually lost ground against the greenback in recent weeks.

Asset allocation

Given the factors described above, we have altered slightly our asset allocation.

On January 18 we had raised the percentage allocated to equities, to reflect the positive sentiment that we had (and still have) about this asset class. On the same date we moderately increased the dollar exposure for the portfolios denominated in euros or Swiss francs.

For a medium risk profile we thus raised to 34% (+6%) the percentage of equities (+2% for the European market, +1% for the US market, +1% for Japanese equities and +2% for emerging country shares). Symmetrically, we reduced the proportion of cash by -4% (now at 3% and by -2% the portion invested in short-term bonds (currently at 38%). Apart from this, the allocation grid remains unchanged. As for the US dollar exposure, it has been raised from 10% to 12%.

Allocation grid for a “medium” risk profile in euros

Bonds		38%
	Short-term bonds	38%
	Long-term bonds	0%
Equities		34%
	Europe	14%
	United States	11%
	Japan	4%
	Emerging countries	5%
Alternative investments		20%
Gold		3%
Structured products		2%
Cash		3%
TOTAL		100%

For the other risk profiles we made the following changes:

LOW-RISK PROFILE:

We have raised the proportion of equities by +4% (to 10%), reducing the share of cash by the same percentage (-4% to 14%). The remainder of the grid remains unchanged (short-term bonds = 61%; long-term bonds = 0%; alternative investments = 11%; structured products = 2% and gold = 2%). The US dollar exposure has risen from 6% to 8%.

MODERATE RISK PROFILE:

The exposure to equities has been raised from 18% to 23%, that of short-term bonds reduced from 51% to 50% and that of cash from 12% to 8%. The percentage of long-term bonds (0%), alternative investments (15%), structured products (2%) and gold (2%) has not been altered. The dollar exposure has been raised from 8% to 10%.

AGGRESSIVE RISK PROFILE:

The proportion of shares has increased from 50% to 56%, at the expense of that of short-term bonds (-2%, to 9%) and that of cash (-4%, to 2%). The weight of long-term bonds (0%), alternative investments (27%) and structured products (3%) and gold (2%) remains constant. The US dollar exposure has risen from 10% to 13%.