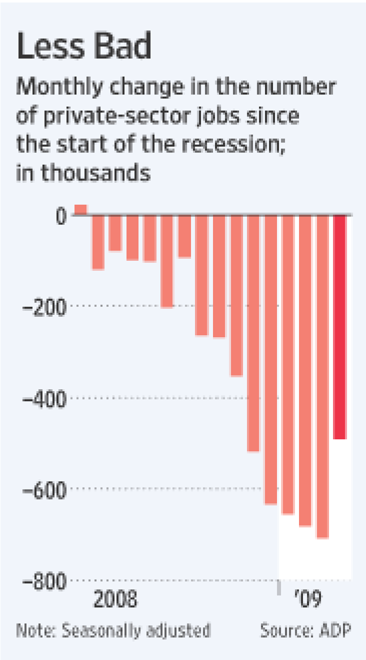
AMG Market Commentary

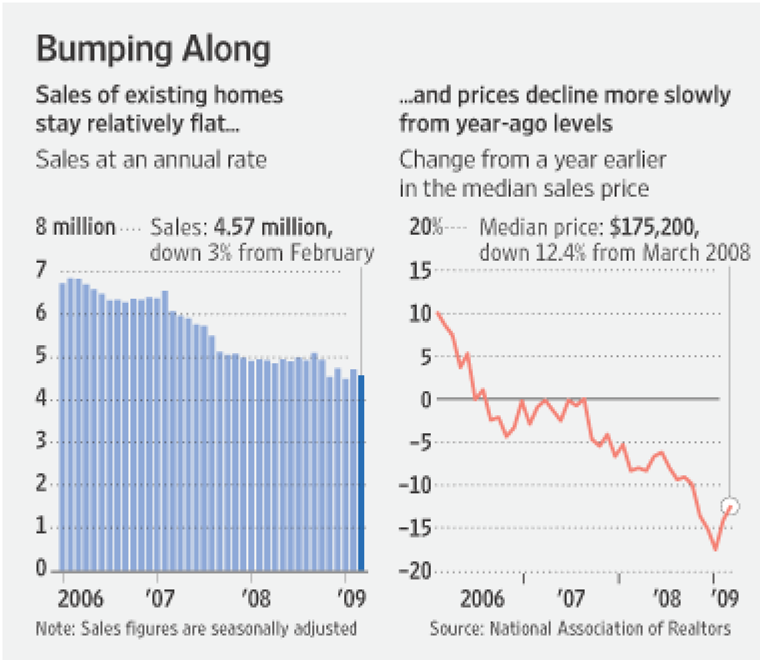
May 2009

LIQUDITY AND CONFIDENCE COME BACK

Recent data showed that the free fall in U.S. economy was slowing down as government rescue action started to take effect and credit market come back to life. Instead of deeper recession, a gradual recovery in late 2009 or early 2010 becomes the market consensus.

The improvement in economic data was broad based. Home sales and prices (depicted below), manufacturing PMI, credit spread and job market all reported slower decline lately. The hope for economy to bottom out was gaining support from facts for the first time in more than a year.





Better than expected data was more than comforting to investors, they fled safe heaven assets and put back money to risk assets. As a result, stocks, commodities and high yield currencies all started a rally. More than 50%

gains were reported for many markets, to name a few, Hong Kong and China, Brazil, Korea, India and Crude oil futures.

But, we must be very careful here. What's we are saying is a slight rebound from historical lows, most of the data told us that the economy is still deep in contraction.

Household is an area of particular concerns. Consumption and job data are slow to show any improvements. After rising in Feb 2009, U.S. consumption figure resumed the trend of decline in March and April. For the job market, over 500K job losses was reported in April. Albeit it was smaller than 700K slashed in last 2 months. It showed that more and more Americans were thrown out of the job market.

All in all, the economy is only showing early signs for stabilizing. It is far too much to look for recovery. Admittedly, investment market has a tendency to front-run the economy on investors' expectation. But, it is difficult to justify the recent rally as we only see twilight for the economy. Rather than chasing in amid the rally, buy into the markets on adjustments would be a more viable strategy.

US : Neutral

The results of the stress test for major financial companies came out finally. It made no surprise to the market. Although 10 of the 19 tested institutions need to raise capital, U.S. Treasury Secretary Geithner reaffirmed the public that no major financial institution was facing a risk of bankruptcy. The stress test ended with no major impact on investment markets.

Economic data generally pointed to smaller contraction. PMI data improved in April compared with March. U.S. ISM non-manufacturing index rose to 43.7 while the manufacturing index went up to 40.1. Besides business activity, liquidity conditions showed improvements also. 1-month LIBOR dropped below 1% for the first time since Lehman Brothers went under. It indicated that market borrowing cost for banks was approaching normal level.

EU : Neutral

Economic conditions in European were poor. 2009Q1 GDP data was the worst even reported. Eurozone GDP fell more than estimates, it contracted 2.5% compared with last quarter. German GDP contracted by 2.5% qoq and French fell 1.2%. The European government also downgraded their full year forecast.

However, recent data also showed some signs of stabilization. Germany reported increase in exports and manufacturing orders in March compared with February. Export was up 0.7% while manufacturing orders added 3.3%.

Japan : Neutral

Twilight was also showed in the economic data for Japan. Declines in Japanese exports eased slightly from -49.4% in February to -46.5% in March.

China : Positive

Government stimulation and loose liquidity conditions propped up Chinese economy and helped to keep up Chinese GDP growth. Still, a struggle between domestic driven growth and external driven contraction continued.

Fixed asset investment went up 30.5% in April as investments in railroad and ports jumped. But, foreign direct investment fell another 9.5% in April. Moreover, external trade continued with the slump, exports declined by 22.6% in April.

Emerging Markets India : Positive

India election was expected to end with no obvious winner and a coalition government was expected to come after that. However, it turned out that the ruling party alliance UPA won a great victory and nearly got sufficient seat to control the Parliament on its own. Election of UPA was taken as a positive result as it is regarded as a supporter for reforms. With UPA firmly in power, investors' found no reason to worry about the political risk for Indian market.

Commodities : Positive

Return of risk appetite was also affecting commodities prices. Crude oil finally broke the USD50 mark amid the return of risk appetite. Gold, a traditional safe heaven asset, fell slightly to USD 880/ounce.

Hedge Fund : Neutral
Strong equities market performance helped hedge fund also. The Barclay Hedge Fund Index jumped by 5.14% in April, it added to the YTD performance and made it 5.57% till end of April.

Government Bonds : Negative
High grade government bonds came under pressure. U.S. treasuries, German Bund, Japanese government bonds all declined in prices. Now, 10 years U.S. Treasuries yields 3.1%, German Bund yields 3.44% while U.K. Gilt yields 3.5%. They are at highest level since November 2008. But, it does not make the high grade government bonds attractive investments. In fact, the yields are just returning to normal levels as investors' need for safe heaven wanes.

Things to Look Forward:
Improvements in economic data stroked optimistic sentiment in investment markets. Here we must stress that recent data only suggests the economy could be reaching the bottom. But, no signs of recovery were seen yet. Continued improvement is needed to support the rally in risky assets prices. So far, housing market and manufacturing activity showed a more obvious trend for stabilizing while consumption and job market still lagged behind.
Although A/H1N1 flu is getting lower attention in investment community than before, the virus is getting more widespread and inflection number is rising every day. The chance for large-scale outbreak and more severe disruption to the economy to occur is getting higher.

* All figures and information are collected from WSJ, Bloomberg.com & Barclay Hedge.

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