AMG Market Commentary

April 2011

Earthquake in Japan is not as much a disaster to stock market

On 11 March, the north eastern part of Japan was hit by a magnitude 9.0 earthquake. It was the strongest earthquake in Japan for more than 100 years. Besides, a massive tsunami was triggered. 10-meters tall waves swept away townships, leaving only scrap behind. What added to the plight what the nuclear leakage of the Fukushima nuclear power plant. Japanese stock market plunged some 20% following the disasters, and it brought Asian countries stock markets down with it.

Within days, estimates on the economic impact and loss figures were released. Despite the massive losses, Japanese economy is only expected to decline for 1 quarter and then to recover quickly once the expansion effect of reconstruction kicks in. And the fears of nuclear explosion faded away quickly after rescuers tried to cool the reactors down with seawater. Market sentiment quickly recovered and stock markets started to turn up. By the end of March, nearly every Asian market has regained the lost ground except Japan.

Looking forward, we think that the damage by the disaster is already done and reflected. Barring from a downturn and tragic result for the nuclear crisis, we are expecting no significant downturn in the markets.

Looking forward, all Japan can do is to put themselves up and concentrate on rebuilding the destroyed homes and cities. And undoubtedly, the expenses related to reconstruction shall add to the economy growth in coming years. But, we still do not prefer Japanese stocks related investment as the fundamental problems such as poor investment and consumption demand, heavy debt burden are still there.

While for other Asian countries, the threat of nuclear disaster is fading away. The impact to them should be largely limited to the disruption to component supply for electronics and autos industry, which should be a minor problem for most countries. Thereby, we have decided not to change our views on any markets as a result of the Japanese earthquake and remain positive to Asian emerging markets. While for U.S. and Europe, they are expect to go up with the general market. But, we do not have particular preference for them as their fundamentals are less favourable compare with emerging markets.

US : Positive

In Mar 2011, private sector has added some 240,000 non-farm payrolls and unemployment rate went down to 8.8%. For the 2nd months in a row, U.S. companies have created more than 200,000 jobs. The improvement in job market is a good signs for U.S. economy. Yet, for the stock market, it is now complicated by the possible influence to policy. A major reason for the Fed to launch QE 2.0 was that U.S. was still troubled by high

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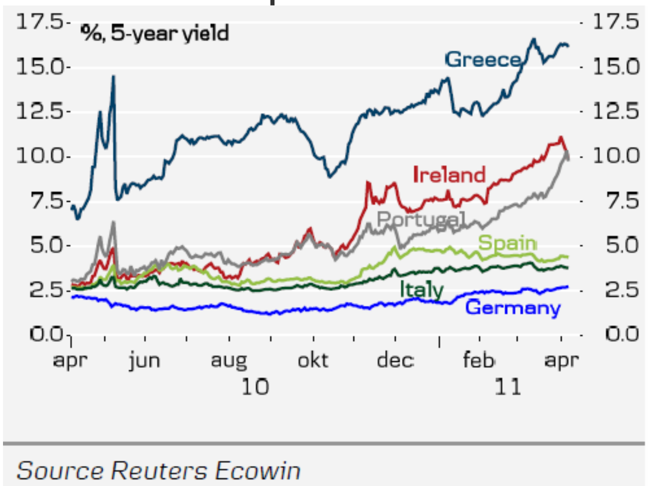
employment. So, an improvement in job market could mean higher chance for policy tightening. And thus, it could bring along more uncertainty to the market.

Europe : Neutral

Monetary policy in Eurozone is another important issue in the market. In the last few months, ECB members especially Chairman Trichet signaled again and again to the market that they are getting more hawkish in policy stance as inflation is. Yet, the worries about weaker members and their debt problem is suggesting

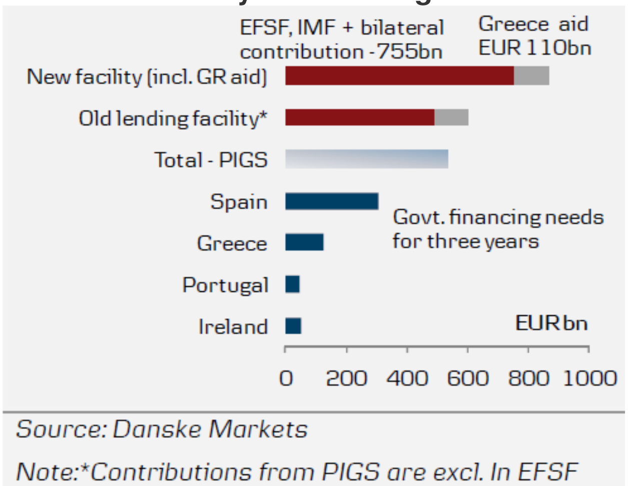
And the debt problem heat up again as Socrates, Portuguese Prime Minister resigned after he failed to push through some austerity measures in the Parliament. The failure for Portugal to agree on deficit cuts stroke the nerve of the market. The bond yield of Portuguese sovereign debt shot up and it brought along Irish and Greek bond yield with it. Luckily, the turmoil did not spread to other asset classes as it was clear that the ESFS has sufficient room to help Portugal and investors' views on Spain did not change, which we can easily tell from the tranquility in its sovereign bonds yield.

5 yield sovereign bond yield for selected European countries



Source: Danske Research

Available capacity for rescue under EFSF and IMF loans facility vs financing needs of PIGS



Source: Danske Research

China : Positive

Chinese CPI went up by 4.90% in Feb 2011, right below the 5% alert level set up the central government. As the threat of inflation persists, the PBOC lifted the required reserve ration of banks by another 0.5% again last month to rein in excess liquidity. And we expect more tightening to come as the monetary tightening has very little success in taming inflation thus far.

Commodities : Positive

Gold price stayed at elevated level for the last month, it had moved in a near range between USD 1,400 and 1,450 for the whole month.

Political turmoil in Middle East provided support to crude oil prices and kept it above USD 100 a barrel. For the war in Libya, it seems like nobody is going to win anytime soon. Neither the rebels nor the government is making progress. So, we do not expect oil productions to recovery anytime soon in Libya. But fortunately, oil production in other major oil producers remains unaffected by the political tension. And we reiterate that WTI crude oil shall stay in the range between USD 95-120.

Hedge Fund : Neutral

Barclay Hedge Fund Index gain 0.35% last month. For the first quarter of the year, Barclay Hedge Fund index reported 1.95% gain. Looking at the strategy sub-indices, Barclay convertible arbitrage index, Barclay distressed securities and Barclay fixed income arbitrage index lead the pack with 4.20%, 3.73% and 3.63% gain for 1Q 2011.

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Government Bonds : Negative
After the disaster, the Japanese government desperately needs to keep interest rate to avoid further damage to the economy and the reconstruction spending shall inevitably add to the debt burden, which is now more than 100% of the GDP. It means zero interest rate policy will be more reluctant and the debt problem will get more severe. So, the Fundamentals are getting weaker for Japanese Yen. Although the Yen jumped after the earthquake, we think it shall just make Japanese Yen and Japanese bonds less favourable to investors.

Things to Look Forward :
For the last 2 years, loose monetary policy from the U.S. and Europe has been an important factor to drive global economy and markets. Still, it seems like the policy turn is about to occur as the ECB is showing more hawkish stance recently and the Fed is about to decide on QE 2.0 which is scheduled to end by June 2011.

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

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