

Global Markets Weekly

Equity markets were less volatile, but still falling. Greece's fiscal woes continued to weigh on the euro.

US growth bounced back in Q4, helped by lower inventory reduction and solid investment. Other US data was mixed.

The Fed pledged to keep US rates at extremely low levels.

The UK economy emerged from recession, but at a snail's pace. Reaction was muted, as investors focused on the eurozone's problems.

Greek bond yields spiked to their highest since joining the euro.

India continued the trend of policy tightening in emerging Asia.

Equity market volatility declined last week, but the trend for stocks was still down. The euro continued to weaken on the back of concerns over Greece's fiscal problems, breaking the 1.40 mark against the dollar for the first time since July last year and falling against the yen too. Commodities were also weaker, and for January as a whole they posted their worst month since December 2008.

US GDP growth accelerated to 5.7% quarter-on-quarter annualised (q/qa) in the fourth quarter (Q4), up from 2.2% q/qa in Q3, the biggest gain in six years. **A large part of the strong growth was due to lower inventory reductions, though investment was also strong.** Final consumer demand was relatively soft at 2.0% q/qa. Between 1992 and 2007 US consumer spending grew at an annual average of 3.5%. Overall this was good news, if not good enough to change the subdued mood in the market. Either way, investors may soon regard this as 'rear-view mirror' data, and are probably focusing more on indicators of the strength of the recovery. Other US data out during the week were mixed. Weekly initial jobless claims were still some way off the level that would be consistent with meaningful job creation and home sales came in below expectations, suggesting the stimulus effect from the homebuyer tax credit may already be fading.

At its regular rate-setting meeting, the **US Federal Reserve (Fed) said interest rates would remain 'exceptionally low' for an 'extended period'**. However, **one member of the committee dissented** in favour of removing the 'extended period' language. The **Fed also confirmed that asset purchases would end in Q1**, though this policy remained open to economic and financial market developments.

The **UK economy also grew in Q4, but at a snail's pace** of 0.1% q/q, ending six quarters of contraction. The **detail of the report showed stagnation in key areas** of the private sector, such as business services. Growth was below expectations and highlights the headwinds facing the UK economy. In the full year 2009, the economy contracted by 4.8%, the largest slump in output in the post World War II period. However, the immediate market reaction was relatively muted, with sterling only down by around 1 cent against both the dollar and the euro. For now, it appears that investors are still giving the UK the benefit of the doubt and problems in the Eurozone are arguably more pressing.

Indeed, **Greece's deficit problems continue to weigh on the single currency. Greek ten-year government bond yields spiked above 7%** this week, to their highest level since it joined the single currency. There were rumours mid-week that China would be buying Greek bonds. This was later denied by Greek officials, leading to a sell-off in the bond market.

Finally, **policy tightening continues in emerging Asia.** The Reserve Bank of India raised its cash reserve ratio by 75 basis points (bp) to 5.75%, citing concerns over rising asset prices, and exceeded expectations for a 50 bp increase. However, the Bank of Japan reiterated its commitment to 'extremely loose' policy at its rate-setting meeting, though it did not increase its emergency liquidity program as some had expected.

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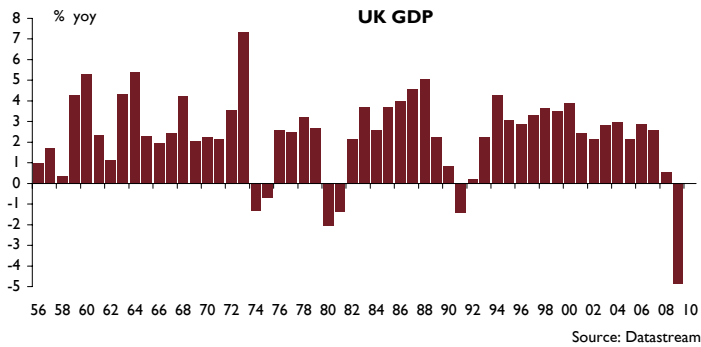
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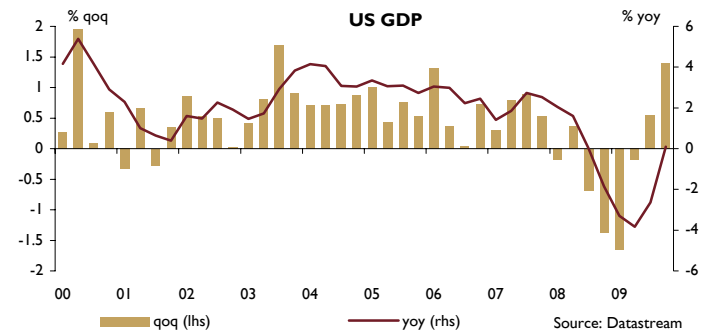
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Charts of the Week

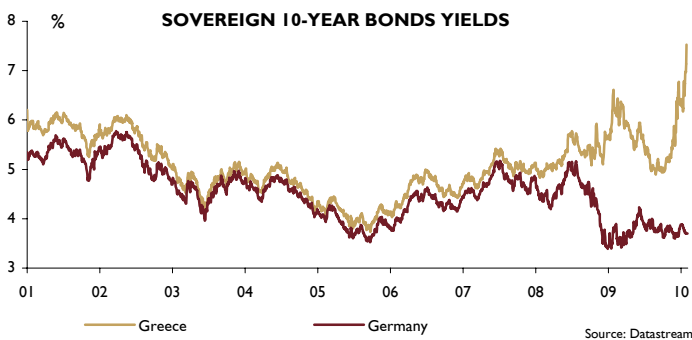
UK economy emerges from recession (just), but 2009 saw the worst annual contraction since World War II



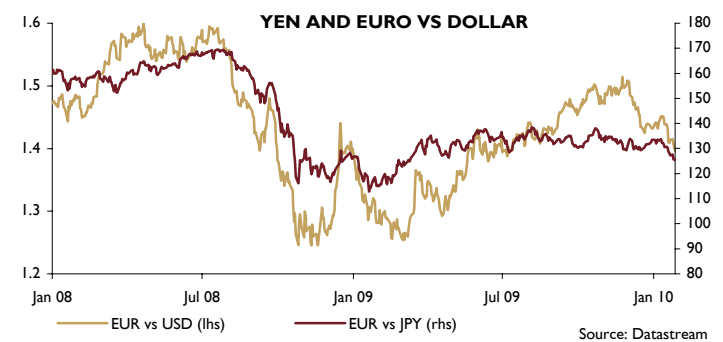
US economy bounces back in Q4, helped by lower inventory reduction and strong investment



Greek government bond yields at their highest levels since joining the single currency



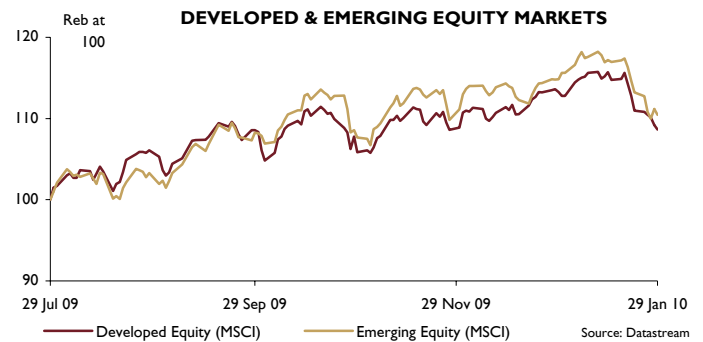
Euro weakens against dollar and yen, as Greek debt problems cast a shadow on the eurozone



Market Performance

| Equity Markets As of: 29-Jan-10 | Performance (% local) | | | | | |
|------------------------------------|-----------------------|-------------|-------------|------------|-------------|-------------|
| | Current | -1W | -1M | -3M | YTD | 09 |
| Developed Equity (MSCI) | 802 | -2.1 | -4.4 | 0.8 | -3.7 | 22.8 |
| FTSE All Share | 2,660 | -2.0 | -4.0 | 1.2 | -3.6 | 25.0 |
| FTSE 100 | 5,189 | -2.2 | -4.6 | 1.0 | -4.1 | 22.1 |
| S&P 500 | 1,074 | -1.6 | -4.7 | 0.7 | -3.7 | 23.5 |
| Nasdaq Composite | 2,147 | -2.6 | -6.2 | 2.4 | -5.4 | 43.9 |
| DJ EuroStoxx | 262 | -1.7 | -5.3 | -0.6 | -4.7 | 23.4 |
| Nikkei 225 | 10,198 | -3.7 | -4.1 | 3.1 | -3.3 | 19.0 |
| Hang Seng | 20,122 | -2.9 | -6.4 | -5.4 | -8.0 | 52.0 |
| Emerging Equity (MSCI) | 41,204 | -2.4 | -3.8 | 1.8 | -4.5 | 58.6 |
| BRIC (MSCI) | 506 | -2.5 | -4.5 | 0.4 | -5.3 | 68.0 |

Source: Datastream



| 10-Year Bond Yields As of: 29-Jan-10 | Change (basis points) | | | | | |
|-----------------------------------------|-----------------------|-----|-----|-----|-----|-----|
| | Current | -1W | -1M | -3M | YTD | 09 |
| US Treasuries | 3.6 | -2 | -21 | 9 | -25 | 158 |
| UK Gilts | 4.0 | -1 | -18 | 24 | -11 | 102 |
| Euro Bonds | 3.2 | -1 | -17 | -10 | -19 | 44 |
| Japanese Bonds | 1.4 | 0 | 2 | -8 | 3 | 11 |

Source: Datastream

| Commodity Markets As of: 29-Jan-10 | Performance (%) | | | | | |
|---------------------------------------|-----------------|-------------|-------------|-------------|-------------|-------------|
| | Current | -1W | -1M | -3M | YTD | 09 |
| Commodities (TR) | 259 | -4.3 | -7.6 | -4.2 | -7.3 | 18.9 |
| WTI Oil Price (Spot) | 73 | -1.5 | -7.6 | -9.0 | -8.2 | 102.4 |
| Gold Bullion (Spot) | 1078 | -1.3 | -2.6 | 3.1 | -1.7 | 27.1 |
| Industrial Metals (TR) | 319 | -7.2 | -9.2 | -0.2 | -8.8 | 80.0 |

Source: Datastream

Interest Rates & Inflation

| Inflation & Interest Rates | | Current Inflation (%) | RBS Interest Rates Forecast (%) | | | Rate Announcement Next Date |
|----------------------------|-------------|-----------------------|---------------------------------|--------|--------|-----------------------------|
| | | | Current | Mar'10 | Jun'10 | |
| United States | (Fed Funds) | 2.7 | 0.25 | 0.25 | 1.00 | 16-Mar |
| United Kingdom | (Base Rate) | 2.9 | 0.50 | 0.50 | 0.50 | 04-Feb |
| Eurozone | (Repo Rate) | 0.9 | 1.00 | 1.00 | 1.00 | 04-Feb |
| Japan | (Call Rate) | -1.7 | 0.10 | 0.10 | 0.10 | 18-Feb |

Source: Coutts, RBS, Datastream

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