

## Global Markets Weekly

**Falling volatility, narrowing spreads and new highs for equities.**

**Markets remained in optimistic mood this past week**, with the VIX Index of expected volatility falling further, the spread between corporate and government bond yields narrowing and the S&P reaching an 18-month high. The benchmark US equity index has now rebounded 10% from its early February low, led by financials, real estate and basic materials. Sterling also regained some ground against the dollar and euro.

**Policy support continues to underpin growth.**

In a further indication that policy-makers in advanced economies are willing to underpin growth, **the US Federal Reserve (Fed) kept interest rates at emergency lows and repeated the phrase in its policy statement that rates were expected to stay there 'for an extended period.'** The Bank of Japan (BoJ) also doubled a short-term lending facility to banks. However, tensions over Greece re-emerged, with Prime Minister George Papandreou threatening to turn to the IMF for emergency funding unless the European Union (EU) comes up with firm proposals of its own by the time of the EU summit on 25-26 March.

**The UK government borrowed 'only' £12.4 bn in February (still a whopping deficit).**

**There was some good news in the UK, with the public-sector borrowing requirement coming in lower than expected** at 'only' £12.4 bn in February and the unemployment rate falling slightly. Sterling strengthened on the back of the data, climbing to just shy of \$1.54. Speculative short positions against sterling have come off a bit in a possible sign that some investors are already anticipating a further rebound in the currency. For the fiscal year 2009/10 as a whole, the public sector borrowing requirement may come in at £5-10 bn less than the £178 bn the government had predicted in December. We will know more after the Budget on 24th March. However, this would still be a whopping annual deficit, on a par with Greece, at around 12% of GDP.

**BoJ boost to banks is no "miracle cure" for deflation.**

**The Japanese central bank decided to double a programme of three-month 0.1% loans to banks** from 10 to 20 trn yen (\$220 bn). The BoJ measures were largely symbolic, however, with Japanese banks already having enough liquidity. The problem is their reluctance to lend. Indeed, BoJ Governor Shirakawa claimed that there was no "miracle" cure for deflation.

**US inflation data supported the Fed decision to keep rates low.**

The Fed's decision to continue with its pledge to keep rates near zero for an extended period led investors to pare back their expectations for early rate increases. Indeed, **the latest US inflation data also suggested that there is no need for early policy tightening.** Headline inflation came in slightly lower than expected at 2.1% in February, down from 2.6% in January. Core inflation was only 1.3%. Despite this, one member of the Fed's rate-setting committee did dissent. Thomas Hoenig warned that the continued pledge to keep rates at emergency lows could lead to financial imbalances and put the long-term stability of the economy and financial markets at risk.

**Emerging countries are facing rising inflation pressures.**

**Inflation figures in the developed world contrast sharply with inflation developments in emerging markets**, where commodities such as food are a more important component of the total consumption basket. For example, Indian consumer price inflation is currently running at 16% and wholesale price inflation rose to 10% in February. In response, India's central bank unexpectedly raised interest rates on Friday, a month before its scheduled monetary policy meeting.

**Carl Astorri**  
+ 44 20 7753 1612

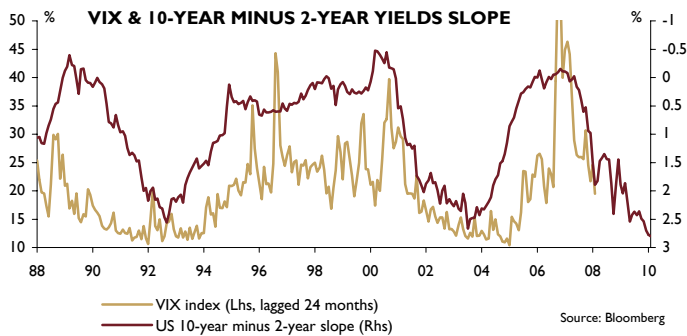
**Jean-Maurice Ladure**  
+44 20 7753 1469

**Henry Lancaster**  
+44 20 7957 2426

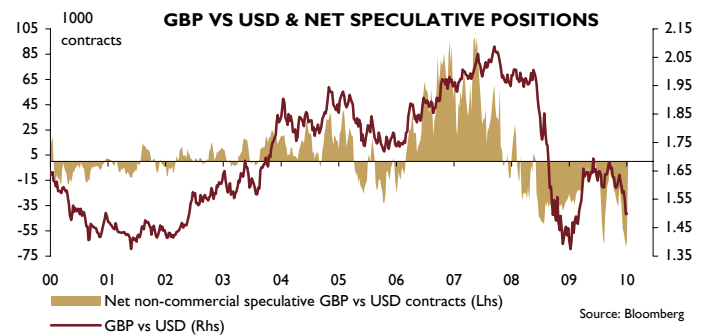
**Georgios Tsapouris**  
+44 20 7753 1888

# Charts of the Week

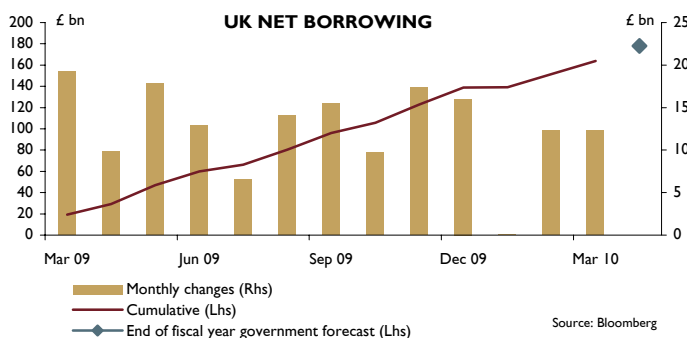
The slope of the US yield curve suggests that volatility could fall further



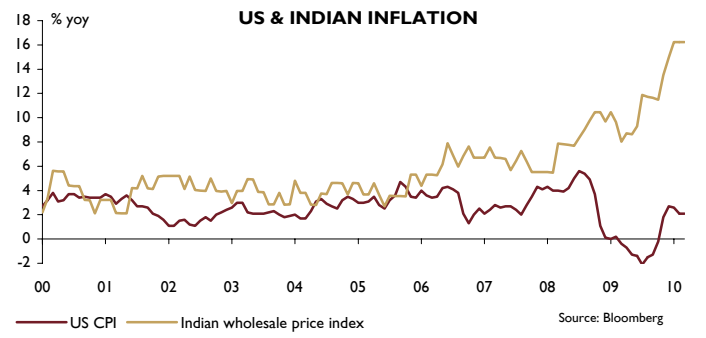
Significant accumulation of negative sterling positions leaves room for short covering



UK deficits undershoot in March, and may come in below target for the full fiscal year, although still substantial



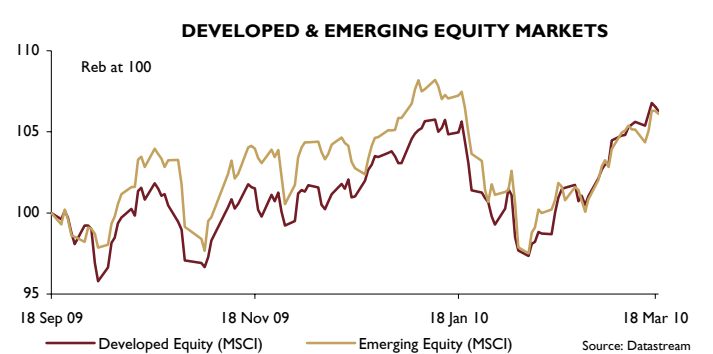
Divergence in inflation means emerging-market interest rates are set to rise further while US rates remain on hold



# Market Performance

Equity Markets As of: 19-Mar-10	Performance (% local)					
	Current	-1W	-1M	-3M	YTD	09
<b>Developed Equity (MSCI)</b>	<b>858</b>	<b>0.6</b>	<b>4.7</b>	<b>5.2</b>	<b>3.1</b>	<b>22.8</b>
FTSE All Share	2,892	0.5	5.5	9.0	4.8	25.0
FTSE 100	5,650	0.4	5.5	8.7	4.4	22.1
S&P 500	1,160	0.9	4.6	5.2	4.0	23.5
Nasdaq Composite	2,374	0.3	5.8	7.4	4.6	43.9
DJ EuroStoxx	274	0.1	4.3	2.4	-0.5	23.4
Nikkei 225	10,825	0.7	6.9	6.7	2.6	19.0
Hang Seng	21,371	0.8	7.4	0.9	-2.3	52.0
<b>Emerging Equity (MSCI)</b>	<b>43,235</b>	<b>0.9</b>	<b>5.3</b>	<b>3.2</b>	<b>0.2</b>	<b>58.6</b>
BRIC (MSCI)	533	0.2	5.5	2.9	-0.2	68.0

Source: Datastream



10-Year Bond Yields As of: 19-Mar-10	Change (basis points)					
	Current	-1W	-1M	-3M	YTD	09
US Treasuries	3.7	-1	-9	15	-14	158
UK Gilts	4.0	-15	-32	7	-16	102
Euro Bonds	3.1	-6	-17	-3	-28	44
Japanese Bonds	1.4	2	3	13	8	11

Source: Datastream

Commodity Markets As of: 19-Mar-10	Performance (%)					
	Current	-1W	-1M	-3M	YTD	09
Commodities (TR)	266	0.0	-1.8	-2.3	-4.9	18.9
WTI Oil Price (Spot)	81	-0.7	1.0	10.7	1.7	102.4
Gold Bullion (Spot)	1103	-0.5	-1.4	-0.1	0.7	27.1
Industrial Metals (TR)	353	0.0	2.1	5.7	0.9	80.0

Source: Datastream

# Interest Rates & Inflation

Inflation & Interest Rates		Current Inflation (%)	RBS Interest Rates Forecast (%)			Rate Announcement Next Date
			Current	Jun '10	Sep '10	
United States	(Fed Funds)	2.1	0.25	0.25	0.75	28-Apr
United Kingdom	(Base Rate)	3.5	0.50	0.50	0.50	08-Apr
Eurozone	(Repo Rate)	0.9	1.00	1.00	1.00	08-Apr
Japan	(Call Rate)	-1.3	0.10	0.10	0.10	07-Apr

Source: Coutts, RBS, Datastream

Issued by Coutts & Co, which is authorised and regulated by the Financial Services Authority. Coutts & Co is registered in England No. 36695. Registered office: 440 Strand, London WC2R 0QS.

The value of investments, and the income from them, can go down as well as up, and you may not recover the amount of your original investment. Past performance should not be taken as a guide to future performance. Where an investment involves exposure to a foreign currency, changes in rates of exchange may cause the value of the investment, and the income from it, to go up or down.

The information in this document is not intended as an offer or solicitation to buy or sell securities or any other investment or banking product, nor does it constitute a personal recommendation. The information is believed to be correct but cannot be guaranteed. Any opinion or forecast constitutes our judgement as at the date of issue and is subject to change without notice. Any Coutts company, or a connected company, its clients and officers may have a position or engage in transactions in any of the securities mentioned.

The analysis contained in this document has been procured, and may have been acted upon, by Coutts & Co and connected companies for their own purposes, and the results are being made available to you on this understanding. To the extent permitted by law and without being inconsistent with any applicable regulation, neither Coutts & Co nor any connected company accepts responsibility for any direct or indirect or consequential loss suffered by you or any other person as a result of your acting, or deciding not to act, in reliance upon such analysis.

Not all products and services offered by the individual Coutts companies are available in all jurisdictions, and some products and services may be available only through particular Coutts companies.

None of the overseas Coutts companies or offices is an Authorised Person subject to the rules and regulations made under the Financial Services and Markets Act 2000 for the protection of investors and depositors, and compensation under the Financial Services Compensation Scheme will not be available in respect of business transacted with them.