



Media release

Hong Kong, 11 January 2010

Bank Sarasin's Global View: 2010 will determine whether or not recovery is sustainable

The powerful cyclical recovery triggered in H2 2009 by unconventional monetary policies and fiscal policy stimuli should continue into Q1 2010. Nonetheless, this economic recovery will peter out in H2 2010. The recovery will only turn into a sustained upswing in 2011, with the support of further fiscal stimulus. This is the conclusion of the latest report on the economic outlook, *Global View*, published by Bank Sarasin's Research team for Q1 2010. Given this economic backdrop, Bank Sarasin expects equities, commodities and corporate bonds to post a positive performance in Q1 2010. However, the risk of setbacks will increase as the year progresses. Bank Sarasin therefore does not predict a significant rally in equity markets over the full year and anticipates marked regional differences, particularly in Europe. With companies facing economic uncertainty, skilful stock picking will be crucial for investment success in 2010.

Various structural hurdles are blocking a sustainable growth cycle. The reduction of debt in the banking system, a process known as deleveraging, will rein in lending volumes. The mid-term economic outlook is also overshadowed by the need to manage public deficits and restore the trade balances. The pattern of various leading indicators, including the German ZEW Economic Expectations Index, as well as the Consumer Sentiment and Economy Watchers Index in Japan, indicate with a usual six-month lead time the possibility of slowing growth and a cyclical relapse as early as H2 2010. This slowdown, which is expected to occur by the end of 2010, will need to be cushioned by further fiscal stimuli to lay the foundations for a sustainable upswing from 2011 onwards.

Jan Amrit Poser, Head of Research and Chief Economist at Bank Sarasin

"2010 will determine whether or not the recovery is sustainable. Even though Sarasin confidently expects a positive answer, we are still a long way from seeing a positive economic trend with the power to sustain itself without external assistance. We are convinced that the economy will therefore still need support in the form of monetary and fiscal policy measures. With capacity utilisation so low, deflationary risks will prevail over the next two years."

Philipp E. Baertschi, Chief Strategist at Bank Sarasin

"We expect a good first quarter, so are starting 2010 overweight in equities. But the stock market rally is likely to run out of steam quite quickly. We prefer shares in companies from industrialised nations which have a strong presence in emerging markets. In our stock selection we focus on well-capitalised blue chips that offer a high dividend yield and higher than average growth. Bonds offer only limited opportunities for returns because of low interest rates, although they will become more attractive over the course of the year."

Consistently low interest rate policies and positive company results

With the economy likely to slow in Q2 2010, central banks should maintain expansionary monetary policies through existing interest rates. The rise in long-term interest rates will only be temporary



and rates should fall back below the current annualised level by the end of the year. This suggests a switch from short- to long-duration bonds. In 2009 the correction of the credit market anomalies caused by the collapse of Lehman Brothers was the main driver for the corporate bond market. Now that the credit market is stabilising, the focus is shifting back to fundamental data such as expected default rates. As the economy recovers, credit conditions become less restrictive, and corporate earnings improve, Bank Sarasin expects the default rate to ease slightly. This decline promises some upside potential for corporate bonds in the first half of the year. Based on positive corporate profits and generous liquidity combined with lower interest rates, stock markets should also rally in the short term. This is likely to tail off again from the second quarter onwards. There will be no dominant trend during 2010. It is therefore important to review asset allocation continuously in a critical light. In their regional and sector allocation, equity investors should take a defensive stance and avoid high individual risks.

Europe has the most surprise potential – Caution advised for emerging markets

Given the likelihood of a mixed and by and large not particularly dynamic share performance, Bank Sarasin believes that regional differences will become more important in 2010. Average earnings growth in excess of 30% seems possible for the overall market in Europe. Sarasin's forecast here is significantly higher than the market consensus. European shares are looking increasingly attractive to international investors because the euro is expected to depreciate. In the US market, Sarasin favours export-driven companies who generate a large portion of their sales in emerging markets. Although global investors are still enthusiastic about emerging markets – despite or perhaps because of their strong performance in 2009 – they have the biggest potential for a setback according to Sarasin. There are already signs that the upturn in the manufacturing industry is gradually fizzling out in China and India. The relative performance of emerging markets is therefore likely to falter significantly. At the same time, however, a significant setback could present the ideal opportunity for re-entering emerging markets. Sarasin favours markets with a significant exposure to commodities – especially Brazil. Demand for energy sources will continue to drive earnings forecasts upwards. Sarasin is taking a cautious stance towards Asian emerging markets in 2010.

Investors favour blue chips

2010 will be a difficult year for companies. They will need to find further cost savings. Bank Sarasin sees very little evidence to suggest that repeating the cyclical sector allocation would be a promising bet. Skilful stock picking will therefore be crucial for investment success in 2010. The bank identifies the following criteria for success: large cap companies with attractive returns in the form of dividends and/or share buy-back programmes, companies with attractive valuation ratios and realistic earnings forecasts, and firms focusing on products and services in sectors that are currently prospering. Infrastructure projects, energy efficiency and ecology, meeting new safety requirements, efficiency improvements through technology, and service and maintenance will be the prominent themes of 2010. This means that companies in cyclical sectors, where caution is advised from the macroeconomic perspective, should outperform the market.

Investment implications: Focus on skilful stock picking

In its global sector allocation, Bank Sarasin's favourites include the Consumer Staples sector, where demand is very steady, Industrials, where specific thematic drivers are creating demand for new products, and Energy and Technology. The Bank has a neutral weighting in Healthcare, Commodities and Basic Materials, Telecoms and Utilities. Bank Sarasin thinks that Consumer Discretionary will be one of the losers in 2010. Equally unattractive is the Financial Industry which, as highlighted by recent events in Dubai, suffers from persisting uncertainties and is likely to underperform. While Bank Sarasin advises underweighting banks in a global portfolio, the climate for insurance companies looks more positive and they should therefore be given a neutral positioning versus the benchmark.



Sarasin's favourite stocks for 2010 are:

Arbonia-Forster (AFG), Chevron, Danone, Holcim, Microsoft, Roche, Volkswagen, and Zurich Financial services.

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