

## Media Release

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# Global View from Sarasin Research: “We are on the brink of an upswing”

**In its latest “Global View” report for Q3 2009, Bank Sarasin concludes that the global economy is set to recover in the second half of 2009. As financial markets stabilised in the second quarter, investors’ risk aversion has been significantly reduced. The reversal of sentiment indicators should start to be felt in the real economy as well. As the recovery kicks in, the Bank advises investors to take a cyclical stance in their portfolios. After the corporate bond rally in the first half of the year, attention will switch to equities in the second half. In its regional selection, Bank Sarasin is focusing on emerging markets. The rotation away from defensive to cyclical sectors is likely to continue.**

One of the recurring themes of every economic cycle is that collective corporate production tends to be cut back excessively during difficult economic conditions, resulting in the sort of bottlenecks we are now experiencing. There are already isolated reports that inventories in several industries are running low. If this trend continues, we can expect a cyclical upswing in the second half of 2009 – as long as states continue to compensate consumers’ reluctance to spend – as well as the return of positive growth rates in most regions of the world.

### **Equity markets benefit – convertible bonds attractive**

The cyclical upturn is likely to put government bonds under pressure in the second half of the year and lead to higher interest rates. But the prospect of a low inflation period in 2010 and the continuation of a zero-interest-rate policy by most central banks will keep a cap on interest rates. Following the strong rally in corporate bonds in the first half of the year, the potential evident back in January is almost exhausted. Bank Sarasin is therefore focusing increasingly on equities, which are likely to benefit most from the upturn. Convertible bonds are also attractive, partly because they stand to benefit from the continuing narrowing of risk premiums, and also since they would profit from the expected stock market rally. Inflation-protected bonds should produce slightly lower returns than normal bonds, but at the same time offer investors the opportunity to protect themselves from a spike in inflation.

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

“We are fairly confident on balance that we are on the brink of a cyclical upswing which should boost the global economy through to 2010. Whether this will develop into a self-sustaining recovery will only become clear in 2010. The return to positive growth from the second half of 2009 onwards should not, however, be misinterpreted as a sign that the worst economic crisis in 80 years is finally over. For the inventory cycle to revive, end-consumer demand must stabilise first.”

### **Philipp E. Baertschi, Chief Strategist at Bank Sarasin**

“We are now overweight in equities, despite the risk of a setback in the short term. We have already significantly reduced the bond holdings in our portfolios. In the third quarter we will use the cash proceeds to further increase our weighting of equities and commodity investments, depending on the market environment.”

### **Economic risks are mid-term in nature**

Bank Sarasin highlights three structural limiting factors that could dampen the mid-term economic recovery: The biggest brake is the low level of lending activity on the part of commercial banks, which is normally an important driver

of economic growth. Consolidating public finances represents the second structural brake. The fiscal stimuli are bound to peter out, so some spending will have to be reined in again, and a mountain of debt (especially with respect to state pension systems) will be increasingly repaid in a bid to put public finances back on a sustainable footing. The third brake is the need to return to balanced international trade relations. Although these factors will all act as a brake on economic growth, they do not necessarily have to lead to another dip in the economy.

#### **Emerging economies could drive growth**

The main barometers of sentiment are already pointing upwards in the emerging economies. Evidently, they respond better to government fiscal programmes and find it easier to stimulate domestic demand. Most of them also have more favourable demographics, which provide a platform of future growth. Bank Sarasin's strategy of increasing portfolio's equities quota of emerging market investments (especially Asia since March 2009) has paid off. The economic situation has improved, especially in China but also in India, much quicker than in industrialised countries. Bank Sarasin's Research team believes that there is still some upside potential over the next 12 months.

#### **Increase exposure to cyclical markets and sectors – Focus on shares with operating leverage**

The turnaround in global sentiment indicators is starting to make not just emerging markets, but also Japan look increasingly attractive. Stock selection is at least as important as regional positioning, however. The best strategy here is to focus on export-oriented companies that generate the bulk of their sales in growth markets. Companies with a high operating leverage, i.e. those whose profits respond most to sales growth, should be favoured during this upturn. The sector allocation is concentrated on the cyclical sectors of Industrials and Materials. Rising demand for steel from China during the first half of the year shows that industrial activity is picking up. There is also strong demand from China for industrial metals. The Financial Services sector has been the top performer in the second quarter. Although the risks in this sector are still high because of the rising numbers of loan defaults and tougher regulatory requirements, the situation seems to be developing in a positive direction. A further increase in exposure to cyclical sectors is likely during the course of the third quarter. Bank Sarasin thinks that defensive sectors such as Healthcare and Telecommunications will continue to underperform for the time being.

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