Regional
Specialists
Review

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# WorldView

**Overview:** *It's remarkable that a rolling series of revolutions across the Middle East and North Africa, a Japanese natural disaster and associated nuclear concerns, and European sovereign default (or "restructuring") risk have appeared to dent financial markets only fleetingly. On the other hand, commodity prices have been quite elevated for some time. This has already led to higher rates of inflation in many emerging economies, and is now appearing in the developed world.*

*Global growth remains robust, with a greater contribution from emerging (e.g., Brazil) and commodity (e.g., Australia) economies. However, as monetary authorities tighten policy, and national treasuries pull back on spending, many expect the global economic pace to moderate. The developed world continues to recover from the excesses of the last decade, but growth remains positive, if subdued. Inflation is the key risk "du jour" and is likely to remain in the headlines for many months to come.*

## North America

Tony Caxide, CFA®
Chief Investment Officer

The U.S. economic recovery appears to have established firmer footing, and investor perceptions are becoming more uniformly positive. New jobs are suddenly near "peak" average levels in the two previous recoveries, the consumer continues to quench strong pent-up demand with robust spending, and manufacturing is re-accelerating. Housing remains weak, but few expect much from this sector for the time being.

The external shocks noted in the Overview weren't enough to shake confidence permanently. Inflation, however, is rising on strong commodity prices and will remain a concern for some time. We expect that underlying inflation will rise but not become a major concern.

# WorldView

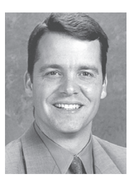
## *Asia*

Jeff Wilkins, MBA
Director, Portfolio Mgmt.

The situation with the Fukushima Daiichi nuclear power plant remains tenuous and it remains difficult to predict how the crisis will be resolved. Based on the extraordinary industriousness and resilience of the Japanese people, we expect this situation will boost GDP in the long term, as the country rebuilds. While the earthquake and tsunami did unite the ever-wrangling divided government for a time (which we viewed as a major positive), many in the minority parties are now calling for the resignation of Prime Minister Kan.

March economic releases, which would reflect some post-quake impacts, are yet to be released. February data was relatively positive across the board. Looking at the 1995 Kobe quake, which did not include a tsunami but did affect a much more industrially significant part of the country, the Japanese were able to overcome great destruction and rebuild in surprising time.

## *Europe*



Eric Shisler, CFA®
VP, Portfolio Management

Economic growth continues to be slow in the Euro-zone, putting pressure on those countries seeking to reduce their deficits. Fourth-quarter GDP was reported at an annualized 1.2%, similar to the previous quarter. Several sectors remain weak (retail sales have been flat for the past year and construction spending is still falling) as austerity measures and 9.9% unemployment take a toll on European consumers.

Portugal has officially requested a bailout from the European Union, joining Greece and Ireland –– a reflection of the ongoing financial weakness in Europe's periphery countries.  On the other hand, core Europe, specifically Germany, is experiencing stronger growth, particularly in its industrial sector thanks to strong export demand.  Finally, the European Central Bank raised its administered rates for the first time in this cycle, by 0 .25% to 1.25%, on recent consumer inflation above the targeted 2%.

## UK

Chris O'Daniel, CTP, CFA®
Director, Portfolio Mgmt.

A weather-induced contraction, coupled with fiscal austerity, has called into question the trajectory of growth in the UK. Housing, job creation, retail sales, wage gains and consumer credit growth are weak. In contrast, manufacturing remains robust. Inflation, owing to an increase in the value-added tax and price increases in raw materials, is running appreciably ahead of the policy goal.

Three members of the Bank of England's policy-making committee voted to increase rates in March. Previously, in December, only one of nine members favored raising rates. It's likely that monetary policy will become more restrictive during 2011.

In summary, given the underlying economic trends, the likelihood of a low-growth/high-inflation scenario cannot be dismissed.

## Emerging Nations

Tony Caxide, CFA®
Chief Investment Officer

China remains a force in the global economy, even as its leadership takes numerous steps to slow economic growth and rapidly rising inflation. Authorities have started to tighten liquidity with higher interest rates and high reserve requirements for banks, among other steps. But credit growth remains too strong, and it's taking longer to turn this ship than the government anticipated. China continues to display many elements of a bubble.

On a longer-term view, China is taking some of the steps that critics have demanded to shift the balance from an excessive reliance on investment (which includes many empty office and apartment buildings) and exports (which can be viewed as harming the growth prospects of its trade partners) toward greater growth of wages for Chinese workers and a greater emphasis on consumer spending. Authorities have initiated a gradual appreciation of its currency, the yuan, which will further help balance trade accounts that currently heavily favor China.

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