

BLACKROCK

Week in View - 23 August 2010

Despite a generally quiet week, the pressure remained on risky assets, as important economic data increased the probability of some of the downside scenarios for the US economy.

Equity movements were fairly muted, with the S&P500 down around 70bps, the UK's FTSE down around 1.3%, and Europe a bit weaker. Asian markets fared a little better, with Hong Kong off 0.4%, Japan off around 0.2% and China A-shares rising.

Government bonds were generally the week's winners, with 10-year Treasury yields down 14bps at one point before finishing the week down only bps. 30-year issues dropped more than 20bps, to levels last seen in March of last year. 10-year Gilts saw no real pullback on the week and saw yields drop by 14bps; similar moves were seen in the German bund market.

Market Movements

Markets	20 Aug 2010	% Change
S&P 500	1071.69	-0.70
NASDAQ	2179.76	0.29
TSE 1st Section	829.59	-0.20
FTSE S&P World		
Europe	300.16	-1.74
FTSE All-Share	2681.12	-1.32
DAX	6005.16	-1.72
Hang Seng	20981.82	-0.43
Citi World Govt Bond Index All Maturities	589.39	0.63
Bonds**	20 Aug 2010	13 Aug 2010
US	2.61	2.67
Japan	0.93	0.98
Germany	2.25	2.39
UK	3.07	3.21
Currencies	20 Aug 2010	13 Aug 2010
USD/Euro	1.27	1.28
GBP/Euro	0.82	0.82
JPY/USD	85.74	86.35
USD/GBP	1.55	1.56
JPY/GBP	132.97	134.58
Commodities	20 Aug 2010	% Change
Oil (Brent Crude)	73.70	-2.02
Commodity Futures (CRB) Index	492.43	-0.59
Gold	1226.70	1.09

The economic news last week was certainly supportive of such moves. While it was probably no surprise to see weak housing activity data in

the US, as the industry struggles with the expiry of tax credits, the signs of slippage were more widespread. Two data points in particular triggered alarm bells: initial weekly claims for unemployment insurance; and the manufacturing survey from the Philadelphia Federal Reserve, known affectionately as the Philly Fed Survey.

Initial claims provide a useful high-frequency indicator of layoff activity, showing the number of new benefit claimants each week. This number has spent most of the last three months in a range between 450,000 and 470,000. This is hardly a strong number, but even an economy with falling unemployment usually posts numbers of around 350,000. Also, this range represents a material improvement on the 650,000 peak seen in early 2009. So it was an unwelcome surprise to see claims above the 470,000 mark for a third-successive week, as the latest print took us back to 500,000.

Every commentator began the year emphasising the importance of the job market to the sustainability of the recovery, and it follows that a labour market moving in the wrong direction is a serious challenge to the health of the recovery.

Looking beyond the labour market, one could say that the underlying driver of hiring is how companies are feeling about the world. Service industries have generally remained rather cautious, but manufacturers globally have been a bright spot since the start of the year. So it was a worry to see the Philly Fed Survey, which is perhaps the largest of the regional US surveys, reporting a sharp downturn in business conditions for manufacturers.

In one sense, this was not surprising - the rapid manufacturing recovery was always going to moderate. But the latest data indicate there is a risk of manufacturing downshifting before the service sector is ready to resume its growth.

How does this news affect our broad survey of the economic outlook? Well, it's important to register that these developments raise the risk of economic disappointments to come: even if the US avoids recession, it needs growth of 2% or more to bring the unemployment rate down and that is now open to dispute.

It seems likely that the doubts in investors' minds will now continue to linger after summer is past. As such, we have been making moderate reductions in risk positions by adding put option

protection, and by reducing some holdings in European and Japanese equities.

But at this point it's also important to add some longer-term context. Corporate spending has been improving through much of the year, and offers enough firepower to limit the effect of government belt tightening. Households have repaired balance sheets quicker than most thought possible, even in problem countries like the US and the UK.

And, perhaps most interestingly, the gradual normalisation of bank lending markets seems to be ongoing. There are some anecdotal signs of bank lending starting to increase, while aggregate surveys of loan demand and lending standards are pointing to an easing in both.

These create the potential for significant support for the economy in 2011, and leave us still positioned with a small overweight in equities and additional investments in areas such as EM debt and High Yield.

The latter is particularly interesting in the current environment, as our work suggests that High Yield returns hold up particularly well in weak growth environments. That enthusiasm doesn't stretch to governments, despite the renewed buying frenzy, with European yields in particular looking stretched as they return to late 2008 levels.

*Equity, currency and bond markets measured over seven days, from previous Friday's close to Friday's close. All index returns in local currency terms. All equity index returns are price only. **Bonds: 10-year yield. This material is for distribution to professional intermediary clients only and should not be relied upon by any other persons. Past performance is not a guide to future performance. The value of investments and the income from them can fall as well as rise and is not guaranteed. You may not get back the amount originally invested. Changes in the rates of exchange between currencies may cause the value of investments to diminish or increase. Levels and bases of taxation may change from time to time. Issued by BlackRock Investment Management (UK) Limited (authorised and regulated by the Financial Services Authority). Registered office: 33 King William Street, London, EC4R 9AS. Registered in England No. 2020394. Tel: 020 7743 3000. For your protection, telephone calls are usually recorded. BlackRock is a trading name of BlackRock Investment Management (UK) Limited. Issued in Switzerland by the representative office, BlackRock Investment Management (UK) Limited (London), Zurich Branch, Claridenstrasse 25, Postfach 2118 CH-8022 Zürich from where the Company's Prospectus, Simplified Prospectus, Articles of Association, Annual Report and Interim Report are available free of charge. Paying Agent in Switzerland is JPMorgan Chase Bank, National Association, Columbus, Zurich Branch Switzerland, Dreikönigstrasse 21, CH-8002 Zurich. In Singapore, this information is issued by BlackRock Investment Management (Singapore) Limited. The offer which is the subject of this information memorandum is not allowed to be made to the retail public. This information memorandum is not a prospectus as defined in the Securities and Futures Act. Accordingly statutory liability under that Act in relation to the content of prospectuses would not apply. You should consider carefully whether the investment is suitable for you. The views expressed herein are as of 23.08.10, and do not constitute investment or any other advice; the views are subject to change and do not necessarily reflect the views of BlackRock as a whole or any part thereof.