

Markets rattled by growing magnitude of fiscal challenges

15 February 2010*

NEWS

- Confidence remained fragile throughout the week as investors waited for news of a specific and co-ordinated plan from the Eurozone to address Greece's fiscal problems. What actually resulted from a meeting of European leaders on Thursday was a broad pledge of support for Greece, but investors were disappointed by the lack of any specific bail-out plan.
- The Governor of the Bank of England (BoE), Mervyn King, presented a report that downgraded medium-term growth and inflation forecasts from the last report in November. This, combined with references to the fragile UK recovery, gave the strong impression that the BoE is currently in no rush to raise rates, despite having paused its quantitative easing programme last week.
- Ben Bernanke laid out the Federal Reserve's (Fed) future vision for unwinding the extraordinary support for the US financial system. The timing of the policy shift was not confirmed by the Fed Chairman on Wednesday.
- China raised its banks' reserve ratio requirement by one percentage point for the second time in a month. Such a move signals that the Chinese authorities are intent on a further tightening in policy in order to avoid an overheating of its economy.

VIEWS

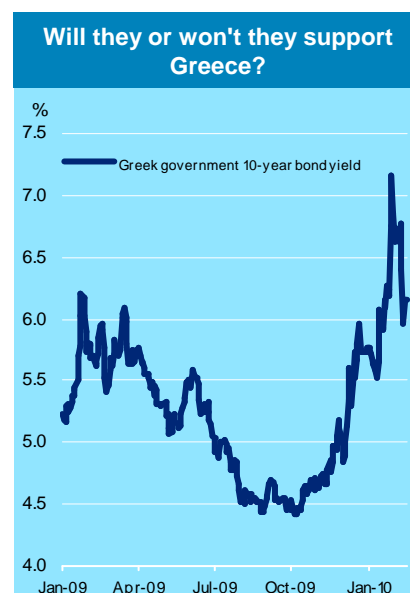
- Low interest rates, government spending, falling inflation and a stabilising labour market should allow growth to continue to improve until mid-2010.
- Improving economic growth, rising inflation, normalising interest rates and heavy issuance will likely send government bond yields higher in 2010.
- The dollar could continue to appreciate on the back of solid US data during the first half of 2010, but the path of least resistance for the dollar remains down in the longer term.
- Despite an attractive valuation, sterling will struggle against most G10 and emerging market currencies until there is more clarity on the UK government's fiscal position.
- We believe the equity market rally will continue during the first half of 2010 on the back of positive earnings growth and continued positive surprises in both industrial production and household consumption data.

THIS WEEK

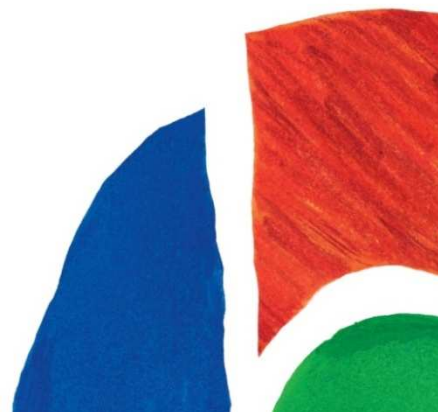
- Economic attention in the UK will focus on the monthly inflation numbers. UK CPI is expected to reach 3.5% in January, up from 2.9% in December. At this level, the Governor of the BoE will be forced to write a letter to the Chancellor to explain the inflation overshoot.
- Focus this week will be on the nature of planned financial support for the Eurozone peripheries. The 16 finance ministers of the Euro area meet on Monday and all 27 European Union (EU) finance ministers meet on Tuesday (EcoFin).
- In the UK, the equity market reporting season will be gaining momentum this week. Beginning with Intercontinental on Tuesday, attention will move onto Rexam, Ladbrokes, Kingfisher, and Rentokil as the week progresses.

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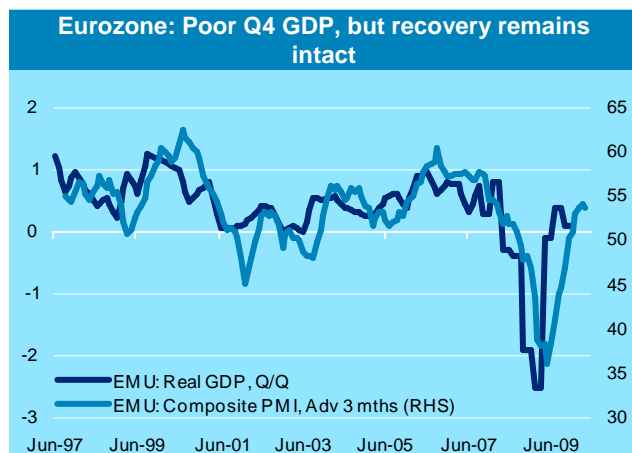
*All data to week ending 12 February 2010
unless otherwise stated



Source: Bloomberg, as at 12 February 2010



ECONOMIC DATA



Source: Datastream, Henderson Global Investors, as at 12 February 2010

GDP Growth %	2009	2010*	2011*
US	-2.5	2.9	3.1
Japan	-5.4	1.3	1.5
Eurozone	-3.9	1.3	1.6
UK	-4.7	1.5	2.2
G7	-3.6	2.0	2.2
Asia ex Japan	5.2	7.8	7.4
World	-2.2	3.0	N/A

Inflation %	2009	2010*	2011*
US	-0.3	2.2	1.9
Japan	-1.3	-1.0	-0.3
Eurozone	0.3	1.2	1.5
UK	2.1	2.4	1.7
G7	0.0	1.4	1.5
Asia ex Japan	1.8	3.6	3.7
World	1.4	2.6	N/A

Bond Indices	5 Feb	12 Feb	% cge
FTA Government Stocks	2308	2282	-1.1
FTA Index-Linked	2481	2413	-2.7
JP Morgan Global Govt Bond Index	551	548	-0.5

10-year Bond Yield (%)	5 Feb	12 Feb	Dec 2010*
UK	3.98	4.14	↑↑↑
US	3.57	3.69	↑↑↑
Eurozone	3.11	3.19	↑
Japan	1.36	1.33	↑

Other	5 Feb	12 Feb	June 2010**
Interest Rates (%)			
UK	0.50	0.50	0.50
US	0.25	0.25	0.25
Eurozone	1.00	1.00	1.00
Japan	0.10	0.10	0.10

Currencies & Commodities	5 Feb	12 Feb	Dec 2010**
£/€	0.87	0.87	↑
\$/£	1.56	1.56	→
\$/€	1.37	1.36	↓
¥/\$	89.4	90.0	↑
Oil (Brent crude \$/barrel)	70.3	71.3	↑
Gold (\$/Troy oz)	1057	1087	↑

↑↑	Strong upward trend
↑	upward trend
→	Little change
↓	downward trend
↓↓	Strong downward trend

Source: Datastream, Henderson Global Investors, as at 12 February 2010
 * Consensus economics, as at 11 January 2010
 ** Henderson Interest Rate Team forecast

MACRO

Following four consecutive weekly declines, risk assets staged a rebound last week. Equities, commodities, emerging market currencies, and external debt all bounced on the back of initial rumours, and then the 'pseudo' confirmation of EU fiscal support for Greece. G7 government bonds sold off, with the UK continuing its underperformance, whilst the euro remained under pressure despite the EU's confirmation of implicit support for Greece.

Following high level meetings last week, the EU released a brief statement regarding its position on Greece's fiscal situation. In the statement, the EU indicated that it would "take determined and coordinated action, if needed, to safeguard financial stability in the euro area as a whole". Following an initially positive reaction, market participants began to question the vague nature of the statement and concerns grew about the lack of any concrete measures to solve Greece's fiscal crisis. In our view, it seems unlikely, given the EU's assertion that it will "safeguard financial stability", that it would choose not to assist Greece with its substantial refinancing requirements this year should it encounter difficulties as they arise.

In its quarterly inflation report, released last week, the BoE erred on the side of 'too much' rather than 'too little' policy stimulus as it maintained its forecast for a fall in the inflation rate to below its target during the BoE's forecast horizon. UK gilts reacted positively immediately following the release of the report, but gave back all the gains, and then some, to finish lower on the week.

Initial estimates from Eurostat showed that the European economy grew a disappointing 0.1% in the fourth quarter, versus analysts expectation of 0.3%. Although the initial estimate does not provide a detailed breakdown of GDP contribution, commentary on member states' statistics websites indicated that net trade contributed most of the growth, whilst other sectors of the economy contracted. Further signs of the ongoing US economic recovery were evident last week as retail sales showed a strong rebound in January as job shedding slowed and labour income growth continued to rebound, whilst US small business optimism ticked up slightly.

BONDS & CURRENCIES

The currency market consolidated following previous weeks of strong US dollar outperformance. The dollar continued to benefit from its status as a safe-haven and the euro came under pressure due to fears that Greece's woes would trigger contagion to other Eurozone countries. As a result, the euro touched an eight-month low, falling below \$1.36 and ended the week down 0.4%. The spread of peripheral Eurozone government bond yields narrowed, but remained high, with the 10-year Greek/German spread standing at 293 basis points (bp), an increase from 273bp on Thursday. Government bonds largely gave back some of the price rises they had seen in previous weeks as risk assets proved more stable and the safe haven flows into bonds were reversed somewhat. The gilt market also struggled with increased supply as the BoE has now put its purchases of gilts on hold.

COMMODITIES

Oil generally followed the upward progress of equity markets, highlighting the high level of correlation amongst risk assets. It managed to rally moderately during the week (Nymex oil +4.1%) following a number of weeks of sustained underperformance. Base metals performed well with copper rising 8.5%, whilst gold also rallied, clawing back some of its losses since the early December peak in prices.

UK EQUITIES: The FTSE 100 made its first weekly advance (+1.6%) in five weeks, despite volatile behaviour in the banking sector influenced by concerns surrounding Chinese policy and Greek budget problems. Banks remained under pressure as traders took their lead from the ever-widening sovereign debt insurance prices, most notably for Dubai. Lloyds Banking Group was down 3.3% at 46.6p on Friday, down 3.6% on the week, and Barclays lost 2.6% over the five-day period, ahead of its results announcement next week.

In the telecoms sector, BT shares dropped almost 9% on Thursday (-5.4% for the week) after the company announced a £9bn pension fund deficit and highlighted regulator concerns about the existing agreement between the company and the fund's trustees. The deficit compares unfavourably to the company's current market capitalisation of £9.3bn and highlights the competing claims on the company between shareholders and pension scheme members.

Fashion retailer New Look became the third UK company of the week to blame unfavourable market conditions for postponing its plans for an IPO. It was hoped that the flotation would result in an enterprise value of between £1.7bn-1.8bn. The retailer's decision came after Travelport, the US travel group, struggled to win the support of investors and cancelled its £1.2bn IPO on Wednesday. In addition, theme park operator Merlin Entertainment similarly postponed its £2bn flotation, leading to a big blow for bankers who had hoped the IPO market would receive a 'kickstart' and see an influx of advising fees for new issues.

Mid and small Caps: Desire Petroleum was in focus last week, with its shares falling 3.3% to 103p after news that, in January, the Argentine government had detained a British oil industry vessel because of it operating in waters close to the Falkland Islands. Argentina has before now complained about the imminent advent of drilling for oil in the Falklands; despite this, Desire is due to start drilling in the North Falkland basin next week.

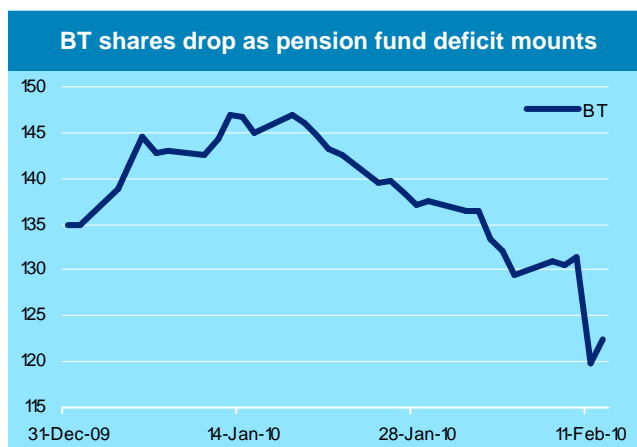
Elsewhere, Diamondcorp (unch) announced progress on its mines located in Botswana and South Africa, with plans to raise £4m to further develop its South African mine. The company is confident that the diamond price outlook has been improving; however, shares in the company fell back on the news.

OVERSEAS EQUITIES

European markets: The FTSE Eurofirst 300 index rose 1.6% over the five-day period, with four consecutive days of gains being broken over worries about China. Banking stocks were volatile over the week as the fiscal outlook for peripheral eurozone nations dominated sentiment. A macro release indicated that Greece saw its economy contract by 0.8% in the fourth quarter of 2009. Other countries that still remain in recession include, Spain, Latvia, and Romania.

Alcatel-Lucent, the largest fixed-line phone networks group in the world, announced net profits of €46m in the fourth quarter of 2009, compared with a €3.89bn net in the same period of 2008. However, shares of the Paris-based company slumped (-15.4%) as it cut its profitability guidance for 2010. Elsewhere, Italian oil giant Eni (+4.0%), outperformed market expectations with fourth quarter underlying net income of €1.39bn, compared with estimates of €1.22bn.

MARKET DATA



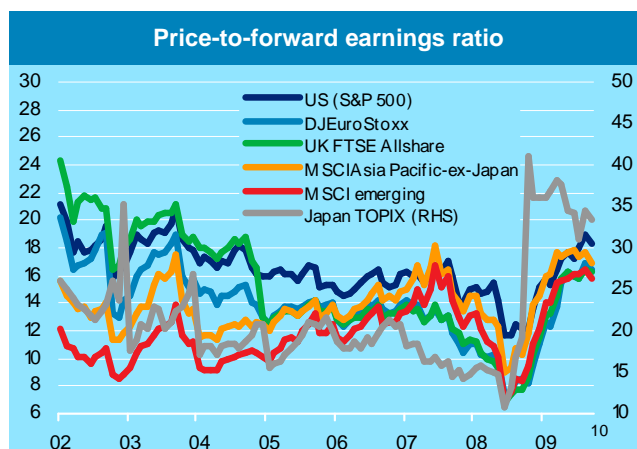
Source: Datastream, as at 12 February 2010

Equities	5 Feb	12 Feb	% cge
UK - FTSE All-Share	2597	2633	1.4
UK - FTSE 100	5061	5142	1.6
UK - FTSE 250	9036	9053	0.2
UK - FTSE Small Cap	2774	2759	-0.5
Eurozone - DJ Euro Stoxx	249	252	1.1
US - S&P 500	1066	1076	0.9
US - Nasdaq	2141	2184	2.0
Japan - Topix	892	892	0.0
Hong Kong - Hang Seng	19665	20269	3.1
MSCI Emerging Markets (US\$)	898	922	2.7

Source: Datastream, as at 12 February 2010

Consensus EPS Growth %	2009* (yoy)	2010* (yoy)	2011* (yoy)
US	3.2	29.6	20.8
Japan	N/A	88.1	25.5
Eurozone	-27.5	33.7	23.1
UK	-33.3	31.2	24.7
Asia ex Japan	4.1	24.2	16.8
MSCI Emerging Markets US\$	3.4	29.6	19.7

Source: Datastream, Henderson Global Investors, as at 31 January 2010
* Consensus forecast

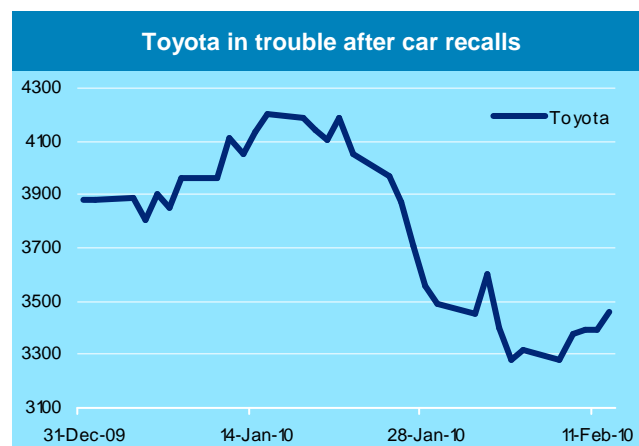


Source: Datastream, Henderson Global Investors, as at 31 January 2010

US markets: The S&P 500 broke free of its four-week losing streak to end the week in positive territory (+0.9%) and the Nasdaq also finished up at 2.0%. The Dow Jones closed below 10,000 on Monday for the first time since November, but regained some of its losses to finish up 0.9%. News flow was mixed over the week; the December trade balance widened to \$40.2bn as detailed in a report on Wednesday, with exports seeing a rise of \$4.6bn to \$142.7bn, whilst imports increased \$8.4bn to \$182.9bn. But market sentiment was lifted on Friday, with news that US retail sales outperformed economists' expectations, rising 0.5% in January.

At the stock level, PepsiCo was notable among those firms releasing results. Over the week, the firm gained 2.4%, its share price rising to \$60.92, after doubling its quarterly profits due to rising international sales. At the sector level, industrial and energy stocks, which had initially shown strength, underperformed at the end of the week as investors' concern turned to the effect of China's tightening announcement on commodities demand. Metal-related stocks largely sold-off, paring gains. Alcoa only managed a 0.8% rise.

Asian markets: With discussion of a bailout for Greece, the Nikkei 225 managed to edge 0.3% higher over the five-day period. The Hang Seng index and Shanghai composite jumped 3.1% and 2.7%, respectively. After faltering earlier in the week, risk appetite recovered mid-week as China's consumer prices index rose less than forecast in January, at 1.5% from a year earlier, indicating perhaps that China's desire to control growth may not be impossible.



Source: Datastream, as at 12 February 2010

Following hot on the heels of one of the biggest recalls in auto history, Toyota's credibility suffered another blow, with the announcement of a 300,000 recall of its Prius hybrid model because of concerns over their brakes. Although the stock added 4.4% over the five-day period, it has fallen over 17% since late January, when the news broke about faulty accelerator pedals on other late model cars.

Unfortunately, Toyota wasn't the only Japanese carmaker to experience negative press during the week: Honda wobbled (-2.4%) after it unsettled investors with an announced recall of 438,000 vehicles, mostly in the US, to fix airbags. Japan's second-largest carmaker is fixing the problem, which has been linked to at least one death and 11 injuries in the US. There was also bad news for Panasonic, as it reported a loss for the last nine months; its share price dipped on the announcement and ended down 6.2%.

Week ahead		Consensus
Monday 15 February	FINALS: Fidessa ECONOMICS: Australia: Reserve Bank of Australia meeting minutes released	More detail regarding the decision not to increase rates
Tuesday 16 February	QUARTERLIES: Turbotec Products INTERIMS: Monitise FINALS: Axis Shield, Barclays, Devro, Domino's Pizza UK & IRL, InterContinental Hotels Group, Premier Foods ECONOMICS: UK: CPI (Jan, mom, yoy) UK: RPI (Jan, mom, yoy) Germany: ZEW survey - economic sentiment (Feb)	Stronger petrol price inflation and VAT rise. Consensus: 0.1%; 3.5% Effects of large mortgage rate cuts in 2009. Consensus: 0.0%; 3.8% Uncertainty in the air
Wednesday 17 February	TRADING ANNOUNCEMENTS: Assura Group, Umeco INTERIMS: Thorntons FINALS: Cyprotex, Rexam ECONOMICS: Eurozone: Trade balance (Dec, €, sa) UK: Jobless claims change (Jan) Spain: GDP (Q4, qoq, yoy, F)	Small monthly fall for three consecutive months Expected to be unchanged from preliminary estimate
Thursday 18 February	INTERIMS: Reed Elsevier FINALS: BAE Systems, Biocompatibles, Ladbrokes, Morgan Crucible, ProStrakan ECONOMICS: Eurozone: Consumer confidence (Feb, A) US: Initial jobless claims (13-Feb) Japan: BOJ rates decision 0.1% 0.1% 0.1%	Element of stability expected, but still below its long-term average Consensus: 450,000 Yen's strength to determine whether BoJ will strengthen QE
Friday 19 February	QUARTERLIES: Shire Plc INTERIMS: BlueBay Asset Management FINALS: Anglo American, Millennium & Copthorne Hotels, Rentokil Initial, Shire Plc ECONOMICS: Eurozone: PMI composite (Feb, A) US: Consumer price index (Jan, mom)	Increase in food and energy prices to cause rise in aggregate

Markets returns source Datastream price index for equities, total return for bonds, local market terms. This document has been produced based on Henderson Global Investors' research and analysis and represents our house view. The information is made available to clients only incidentally. Unless otherwise indicated, the source for all data is Henderson Global Investors. Any reference to individual companies is purely for the purpose of illustration and should not be construed as a recommendation to buy or sell or advice in relation to investment, legal or tax matters. Please remember that past performance is not a guide to future performance. The value of an investment and the income from it can fall as well as rise as a result of market and currency fluctuations and you may not get back the amount originally invested. Tax assumptions may change if the law changes, and the value of tax relief will depend upon individual circumstances.

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