



December Bond Bulletin

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December saw global bond markets marginally weaken on signs of stronger global economic growth. In the UK, government bonds returned -0.1% whilst credit spreads were marginally tighter on the month. The best area was index-linked bonds where breakeven implied inflation rates widened i.e. investors wanted more inflation protection.

The main focus in December continued to be sovereign risk in the Eurozone with increased focus on Spain and Portugal. Bank debt remained under pressure, with lower tier 2 bonds being impacted by a "liability management" exercise at Bank of Ireland. Conversely, corporate credit performed reasonably as evidenced by positive absolute returns from the consumer and industrial sectors in the sterling credit market.

Activity in credit funds was relatively subdued as new issue activity declined and secondary market liquidity deteriorated. We participated in a new issue from Central Networks (electricity distribution) and selectively took advantage of weakness in Spanish telecoms and Italian banks to increase exposures.

Our economic view for 2011 remains unchanged – growth will be sluggish and inflation will not be a problem. We, therefore, used the weakness in government bonds markets in the early part of December to increase duration and we ended the year with funds broadly in line with their benchmarks.

RLAM funds are generally positioned for an improvement in credit markets. We expect that the UK yield curve will flatten in 2011 and still prefer longer dated bonds.

Source: rlam as at 5 January 2011 unless otherwise stated.

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