

BLACKROCK

Week in View

It was another difficult week for financial markets, with signs of trouble particularly evident in Europe where, on average, the major equity indices were down by some 6%.

We have seen risk aversion in other asset classes: the oil price has fallen back to near US\$70 a barrel; industrial metals have been weak, with copper down almost 20%; and the euro has continued to weaken quite sharply against the US dollar.

Interestingly signs of stress are less visible in the bond markets, with downward moves in yields not particularly significant given the heavy weakness in equity markets. Credit spreads have widened out, but the widening has been relatively slight and spreads have not clearly broken out of the ranges of the past six or nine months.

Market Movements

Markets	05 Feb 2010	% Change
S&P 500	1066.19	-0.72
NASDAQ	2141.12	-0.29
TSE 1st Section	891.78	-1.04
FTSE S&P World Europe	294.12	-3.70
FTSE All-Share	2596.72	-2.40
DAX	5434.34	-3.11
Hang Seng	19665.08	-2.27
Citi World Govt Bond Index All Mats	561.83	0.18
Bonds*	05 Feb 2010	29 Jan 2010
US	3.57	3.59
Japan	1.36	1.31
Germany	3.11	3.20
UK	3.98	4.00
Currencies	05 Feb 2010	29 Jan 2010
USD/Euro	1.37	1.39
GBP/Euro	0.87	0.87
JPY/USD	89.36	90.66
USD/GBP	1.56	1.60
JPY/GBP	139.80	145.27
Commodities	05 Feb 2010	% Change
Oil (Brent Crude)	69.79	-2.45
Commodity Futures (CRB) Index	453.7	-2.49
Gold	1056.8	-1.95

The focus for attention has been events in Greece, where political resistance to fiscal tightening has become somewhat more apparent with the threat of a general strike later this month. Greek spreads over German bunds have now widened out to about 3.5% and we have seen increasing signs of contagion to other troubled European markets, although, it has to be said the fundamentals in many of these markets are not as poor as in Greece.

How does the Greek case finish up? There are several possibilities, the first of which sees Greece actually managing to push through material fiscal tightening sufficient to convince investors that its fiscal position is sustainable. There has been some progress over the past few weeks in this context, and the Greek government is trying to pledge itself to get the deficit down from 12% now to 3% 2012.

Clearly, if this is achieved, the world would start to look very different, as was the case with Ireland last year. There is some possibility that Greece could move in the right direction

relative to these targets, but the problem at the moment is two-fold. Firstly, the Greek government has been much better at indicating targets rather than how they are going to be reached, and, secondly, the political backlash against these potential cuts has become more extreme.

The second possibility is that the strains on Greece force the country's departure from the EMU. This still looks very far fetched, as it is not clear how Greece would actually leave the European Monetary Union or, more particularly, what the benefits would be.

Short term interest rates in Europe are already very close to zero so there is little to be gained in terms of a looser monetary stance if Greece were to go it alone, but the major challenge would be that Greek debt is in euros and leaving the euro would leave all of the country's debt in what would then be deemed a foreign currency, causing a major concern to investors. As such, Greece leaving the EMU, either voluntarily or because it is kicked out, looks to be the least likely of all potential solutions.

The third possibility is that Greece defaults, and it should be remembered that a default is not about not paying any of the debt off ever, rather than about missing a relevant interest payment. It is probably too early to be talking about this, as if there is going to be a default then it is improbable that it would happen this year. In the longer term, politically, a lot of emphasis will be put on the avoidance of this outcome.

Moving to a fourth possibility, there could be room for some sort of EU bail out, and while it is highly unlikely the European Central Bank would act alone, the EU can do one of two things.

Firstly, a €50 billion facility was established last year, which at the time was meant to help East European countries outside of the euro area. This could probably be redirected to help the Greeks if necessary.

Secondly, under Article 122 of the Lisbon Treaty, it is possible for EU governments to bail out member states, providing the difficulties faced by said governments are beyond their control. However, there is a very strong line coming from German politicians, in particular, arguing that the difficulties in Greece were actually self-inflicted wounds.

The problem here is that if there were to be no bail out, and if Greece was to default, then one can see the process unravelling to a greater extent in Europe, with increasing pressure placed on countries like Spain and Portugal, and, in a broader context, on the fiscal problems of the US, the UK, and Japan, whereby any Greek default might lead to investors taking a much closer look at sovereign debt in a global context. When a push comes to a shove, it may well be the case that we will see some sort of assistance from the EU.

So how does all of this end? We are anticipating an immediate resolution whatever happens, and the Greek issue is likely to be with us over the next few months at least.

Ultimately, the "muddle-through" scenario - whether the Greeks sort things out, or they do receive the EU assistance - looks to be the most likely, but this is far from guaranteed and this element of uncertainty is what has eroded investor confidence in financial markets more generally.

Against this, spreads in Greek bonds over German bunds are already high, but the issue has already been well identified by investors, and we shouldn't forget some of the more positive fundamental factors that are still evident in the global economy.

Notwithstanding this, the past week is probably indicative of the year that we have ahead of us. We know there are debt issues looming on the sidelines, and there will be periods when

they become centre stage. But there will also be periods when they are pushed aside by what is still a broadly improving macro background.

As such, it is inappropriate to take a highly negative view on risk assets, even if we have a bumpy road ahead of us over the next few weeks and months.

*Bonds: 10-year yield. Equity, currency and bond markets measured from previous Monday's close to Monday's close. All index returns in local currency terms. All equity index returns are price only. 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 08.02.10, 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.