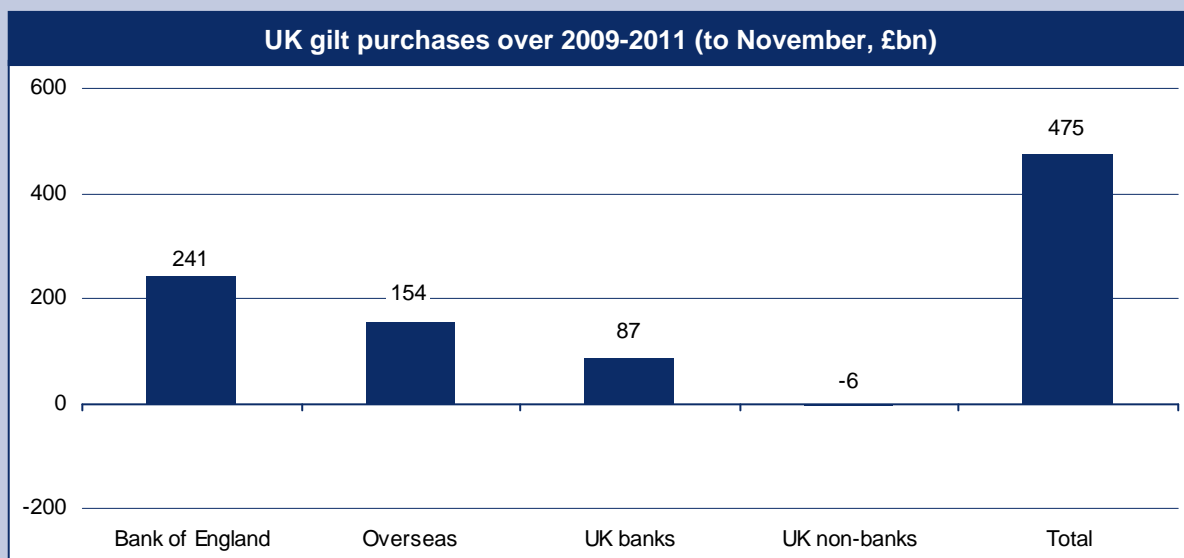


Global Snapshot

January 2012

UK non-banks dump gilts as official / foreign buying soars

- Bank of England figures on gilt purchases cast doubt on Chancellor George Osborne's claim that low yields represent a vote of confidence in the UK's economic and fiscal fundamentals. Yields, instead, have been suppressed by a combination of QE, regulatory-driven bank buying and capital flight from the Eurozone (i.e. a loss of confidence in competing markets).
- In November alone, the Bank bought £23.9 billion while overseas investors ploughed £16.3 billion into gilts – just below a record £16.6 billion in September 2008, when Lehman failed. With the Debt Management Office (DMO) issuing “only” £11.9 billion, official and foreign demand was sated by UK non-bank investors and banks selling on a large scale – reflecting, presumably, a judgement that yields were unsustainably low. UK non-banks reduced their holdings by a record £23.1 billion in November following £16.7 billion in October.
- The dominant role of policy-related and foreign buying is not new. The DMO has issued £475.1 billion of gilts since the start of 2009 – equivalent to a third of annual GDP. The Bank has hoovered up £240.9 billion of this flow leaving £234.2 billion – less than half – to be absorbed by “the market”. Capital flight from the Eurozone contributed to foreigners buying £153.8 billion with the remainder taken up by UK banks, largely reflecting regulatory pressure to increase holdings of “high-quality” liquid assets. Despite the supply avalanche, therefore, UK non-bank investors – the traditional buyers – have actually reduced their holdings, by £6.1 billion, since the start of 2009.
- Current yields are likely to be sustainable only if the Bank buys even more gilts or forces banks to do so, while Eurozone stabilisation efforts prove fruitless, resulting in a further capital inflow.



Source: Bank of England and Henderson calculations, Jan 2009 to Nov 2011

Simon Ward, Chief Economist

Simon Ward's latest online updates can be found at www.moneymovesmarkets.com

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Henderson
GLOBAL INVESTORS

Global growth expectations for 2012 have been lowered



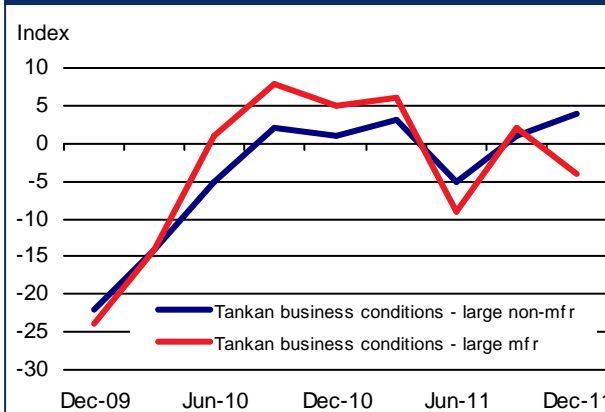
Source: Bloomberg, world gross domestic product growth forecast, daily data, 22 Jul 2011 to 3 Jan 2012

Consensus GDP growth estimates (%)

	2010	2011*	2012*
US	3.0	1.7	2.1
Japan	4.5	-0.6	2.0
Eurozone	1.8	1.6	-0.1
UK	1.8	0.9	0.7
G7	2.6	1.3	1.1
Asia ex Japan	9.0	7.2	6.7
World	4.3	2.9	2.7

Source: Consensus Economics, as at 12 December 2011. * Forecast GDP – gross domestic product

Japanese non-manufacturing enterprises report stronger business conditions than manufacturers



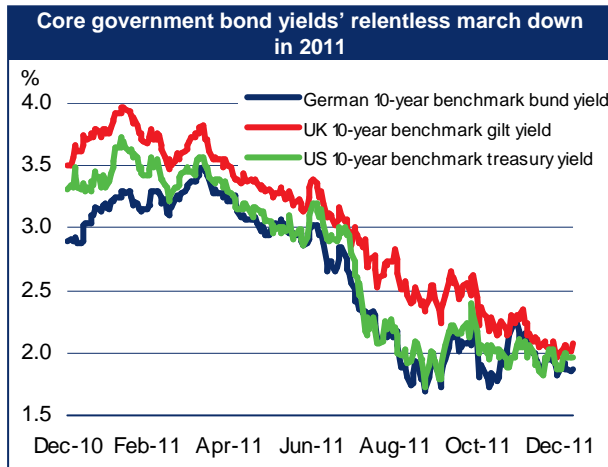
Source: Datastream, Tankan business conditions, quarterly data, Dec 2009 to Dec 2011

Consensus inflation (CPI %)

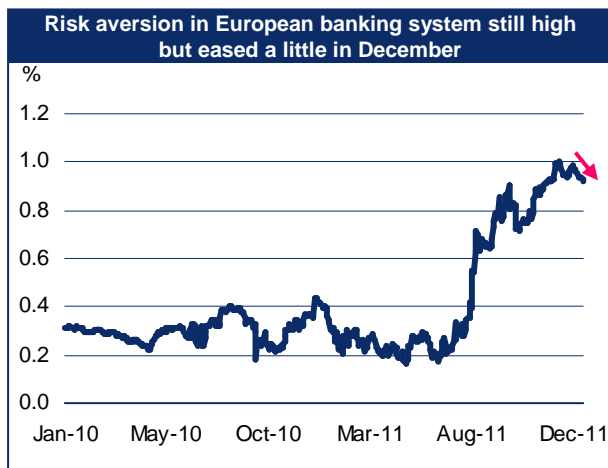
	2010	2011*	2012*
US	1.6	3.2	2.1
Japan	-0.7	-0.2	-0.2
Eurozone	1.6	2.7	1.8
UK	3.3	4.5	2.7
G7	1.4	2.7	1.7
Asia ex Japan	4.2	5.4	4.0
World	2.8	3.7	2.9

Source: Consensus Economics, as at 12 December 2011. * Forecast CPI – consumer price index

- European Union leaders, with the exception of UK Prime Minister David Cameron, agreed in principle on a new 'fiscal compact' of stricter tax and budget rules for member states at the Brussels summit. The European Central Bank continued to cut interest rates by 0.25% to 1.0% and, in an attempt to support the region's fragile banking sector, also announced a longer-term refinancing operation (LTRO) for banks, which it supplied with €489 billion of 3-year loans at an interest rate of just 1%. Preliminary figures show that annual inflation across the Eurozone fell in December to 2.8% from 3% in November.
- The Bank of England, which suggested that weak bank lending would continue to hold back the UK economy, left its monetary policy unchanged as the latest year-on-year consumer price inflation (CPI) data moderated down to 4.8%. Surprisingly, activity in the UK service sector, which accounts for around 70% of the UK's economic output, accelerated in December according to the PMI survey. Data out of the US continued, in the main, to surprise on the upside. 200,000 new jobs were created in the US during December, beating consensus forecasts by a significant amount, with around 1.6 million new jobs created in 2011 as a whole. Further good news included a rise in the ISM Manufacturing survey to 53.9% in December, as factories in the US expanded at their fastest monthly rate since June 2011. However, US retail sales over December disappointed, rising by an estimated 0.1% on the previous month.
- Japan's quarterly Tankan survey showed a slowdown in production by large manufacturers. Elsewhere, imports into China rose by 11.8% in December, year-on-year, the weakest pace in more than two years. China also saw its first year-on-year drop (-10%) in foreign direct investment in 28 months, but, on the positive side, its purchasing managers index showed factory activity expanded slightly in December. Annual CPI inflation marginally fell for the month to 4.1% providing further room for the People's Bank of China to loosen monetary policy. Meanwhile, the Reserve Bank of Australia took the country's benchmark interest rate down to 4.25% in an attempt to stimulate the economy.



Source: Datastream, 10-year benchmark government bond yields, daily data at 10 January 2012



Source: Datastream, Euribor 3-month rate minus EONIA 3-month swap index rate, daily data at 10 January 2012.

10-year bond yields (%)	31 December 2011	2012*	2013*
US	1.88	→	↑
Japan	0.99	→	↑
Eurozone	1.83	→	↑
UK	1.98	→	↑

Currencies	31 December 2011	2012*	2013*
Yen/\$	76.96	→	↑
\$/Euro	1.29	→	↓
Euro/£	1.20	↑	↑
\$/£	1.55	↓	↑

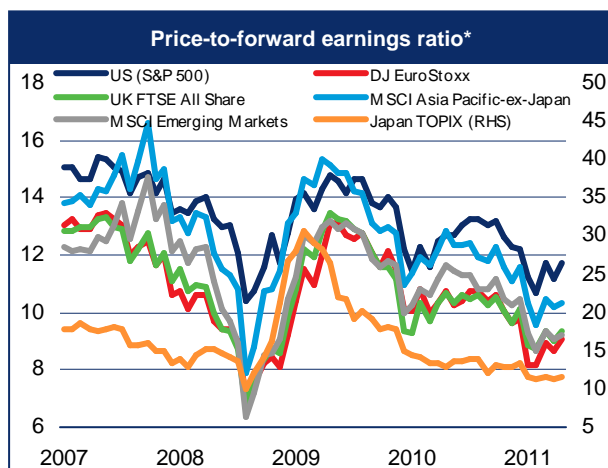
Note: Down arrow indicates a strengthening in the currency in the numerator, and vice versa

Emerging markets and commodities	2012*	2013*
G4/EMFX	↓	↓
Emerging market interest rates	↓	→
Oil	↑	→
Base metals	→	↑
Precious metals	↓	↑
Agriculture	→	↑

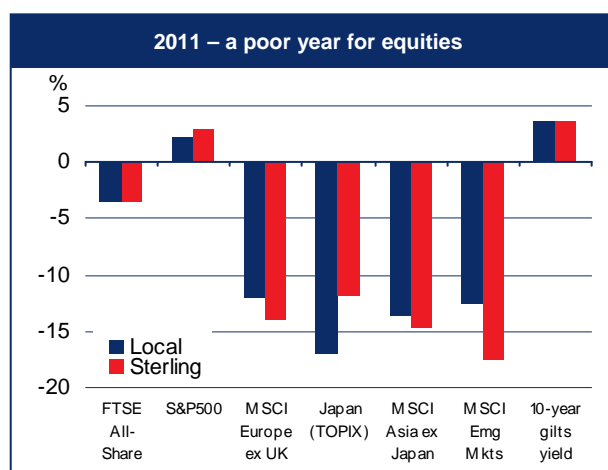
Source: Datastream, Bloomberg, Henderson Global Investors, as at 31 December 2011. *Henderson Interest Rate Team view. EMFX – Emerging Markets Foreign Currency. G4/EMFX – ratio, up arrow indicates a strengthening in the EM currencies and vice versa.

- The European sovereign debt crisis was as resilient in December as in the preceding months, keeping core government bond markets volatile. The eighth euro crisis summit of the year was held in December and resulted in the passing of new austerity measures and proposals for greater fiscal coordination in the region. Despite lacking sufficient detail, the outcome seems to have helped the government bonds of Italy and Spain as their yields fell (prices rose).
- However, the Standard & Poor's rating agency placed the majority of European sovereign ratings on review for downgrades. As a further sign of risk aversion and growing stress in the Eurozone, short-term German government bills sold at a regular auction in early January were priced with a negative yield - for the first time investors are paying Germany for the privilege of lending it money.
- Following a poor performance in November credit markets rallied in December with junior banking bonds and high yield outperforming investment grade bonds. Financials were helped by the actions of the European Central Bank (ECB) extending further liquidity measures to European banks, which although somewhat assuaged liquidity concerns at the banks, has not resulted in fresh money pouring back into peripheral government bonds as hoped. The ECB also delivered a quarter point (0.25%) rate cut on 14 December.
- The US dollar was the best performing currency in December as possible downgrades in Europe made it an even more attractive destination for safe haven flows, while the euro continued to suffer from the ongoing debt crisis. Commodity currencies traded with the general tone of risk assets and ended somewhat weaker.

↑↑ Strong upward trend, ↑ Upward trend, → Little change, ↓ Downward trend, ↓↓ Strong downward trend



Source: Datastream, Henderson Global Investors, monthly data as at 1 January 2012. * 12-month forward price-to-forward earnings ratio.



Source: Datastream, Bloomberg. One-year total returns to 31 December 2011.

Equity market levels	2011	2012*	2013*
US	↑	↑	↑
Japan	↓	↑	↑
Euro-area	↓	↑	↑
UK	↓	↑	↑
Asia ex Japan	↓	↑	↑
MSCI Emerging Markets US\$	↓	↑	↑

Source: Henderson Global Investors, as at January 2012. * Forecast.

Equity market returns for December 2011 (%)	Local	Sterling	Dollar
US: S&P 500	0.9	2.1	0.9
Japan: Topix	0.0	1.8	0.7
Euro-area: Euro Stoxx	-0.4	-3.1	-4.1
UK: FTSE All-Share	0.8	0.8	-0.4
MSCI Far East ex Japan (US\$)		2.4	1.2
MSCI Emerging Markets US\$		-0.1	-1.3

Source: Datastream, Henderson Global Investors, index price returns, at 31 December 2011.

- Global equities ended the final month of 2011 in mixed territory. The month started with continued concerns over the future of the euro but rallied on thin volumes into year-end. Government easing in China restored some confidence in Asian equity markets, while in the US stronger figures on trade and consumer spending aided investor sentiment. In local currency terms, US and UK equities outperformed Europe, emerging markets, Asia ex Japan and Japan.
- 2011 was a disappointing year for risk assets as investors fled to the safe havens of German bunds, gold, the Swiss franc and the yen. The MSCI World Total Return US\$ Index ended 2011 down 5%. The main drags on equity performance were the intensification of the euro debt crisis, waning economic momentum in the US and slowing growth concerns for emerging markets. Towards the end of the year the US economy provided some cheer, with a pick-up in consumer spending and an improvement in manufacturing activity. Given the region's escalating sovereign debt crisis, European stocks, somewhat surprisingly, somewhat held up relatively well, outperforming emerging markets and Japan.
- In the main, companies enjoyed a further year of balance sheet strengthening in 2011 and dividend payments are set to be higher in 2012. Indeed, on most valuation measures, equity markets have started the year cheaper than they began in 2011, and look particularly attractive relative to the low bond yields currently on offer. However, political and central bank responses to the ongoing difficulties facing the global economy are expected to continue to dictate the direction of markets in the short term.

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