

### Interest rates/Bond markets

#### Waiting for labour market data

##### USA

- Macroeconomic figures continue to improve and we now expect a shift towards a more hawkish language by the Fed
- Should labour data in particular improve further, the first rate hike will likely be done at the start of the last quarter 2010
- 10-year treasury yields are expected to move gradually higher over the month - a firm payroll report on Good Friday has the potential to cause a severe market reaction

##### Euro Area

- German bund yields are significantly below levels seen at the start of the year, but this is not true for Euroland on aggregate as fears surrounding the Greek fiscal crisis continue to dominate the market
- A rate hike by the European Central Bank is likely delayed until worries about sovereign debt abate in a convincing manner
- Corporate credits benefit from these uncertainties and spreads are set to tighten further next month

##### Japan

- Bank of Japan is the only major central bank which continues to extend its liquidity program
- Like elsewhere, we see room for gradually higher bond yields as deflation fears seem overdone

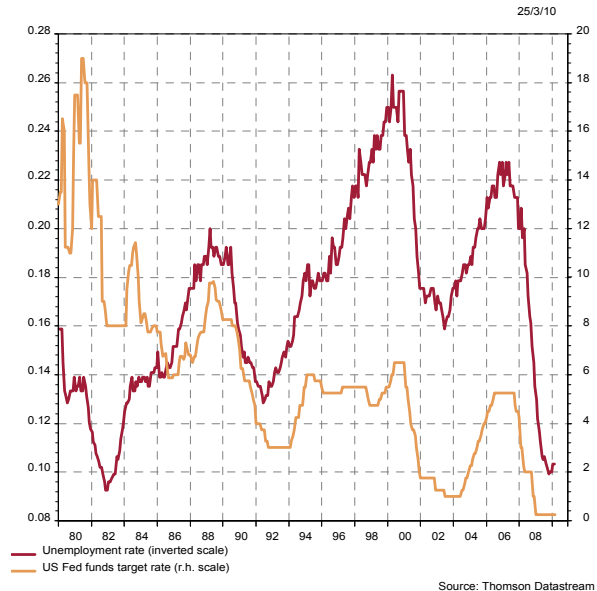
##### United Kingdom

- Public borrowing needs for fiscal year 2009/10 and for the period until 2015 are revised markedly lower by the Chancellor
- February inflation data came in below market's expectations, meaning that the central bank missed its inflation target only temporarily

##### Switzerland

- Fiscal situation should deteriorate in coming two years, but looks very healthy in international context
- Comparably limited borrowing needs are already priced into current yield spreads in our view

### How long will the Fed wait this time?



It is consensus view that yields should move higher until the end of the year. Yet, there is disagreement over the reasons for such a move. Incoming news on the fiscal situation in the US and the UK suggest that the worst projections on rising deficits made last year should not materialise. If true, bond markets should not be more worried about future public borrowing needs today than they were at the end of last year. Secondly, inflation expectations too should not be a source for higher nominal yields for the time being as we do not believe that inflation will rise significantly until next year. Inflation expectations would only shift markedly to the upside once market participants start to believe that central banks are too complacent in their monetary generosity. Judging by the reaction of key central bank representatives on a proposal to set higher inflation targets, we are not concerned that central banks will wait too long before starting to normalise monetary policy. In the case of the Federal Reserve System in the US, we think that the incoming labour market data over the second quarter will be the key to reassess their position. Should the US labour market recover – as we expect – in a convincing manner, representatives of the Fed will start to hint at an approaching end of the near zero interest rate policy. Markets will adjust accordingly, which means that yields at the long end of the curve should move slightly higher in response to higher future money market rates.

### Stock markets

The revival of risk appetite

#### USA

- The FOMC sent a signal to the market that it would not take steps closer to raising rates yet
- The market environment should thus be favorable once again for risk assets and carry trades
- We expect higher stock prices over one month as the signs of a sustainable, broad-based economic recovery are increasing

#### Euro Area

- As expected, European equities recovered notably over the past month, generating a full year's performance in only four weeks
- Despite a notable Euro depreciation and widening spreads of Greek debt, investors moved into stocks and caused the market to actually look overbought
- We expect the positive momentum to continue underpinned by favourable macro data

#### Japan

- Exports continue to expand due to the robust global recovery and strong demand out of China
- Over the past month, Japanese equities had a fairly strong run closing somewhat the relative performance gap to other markets

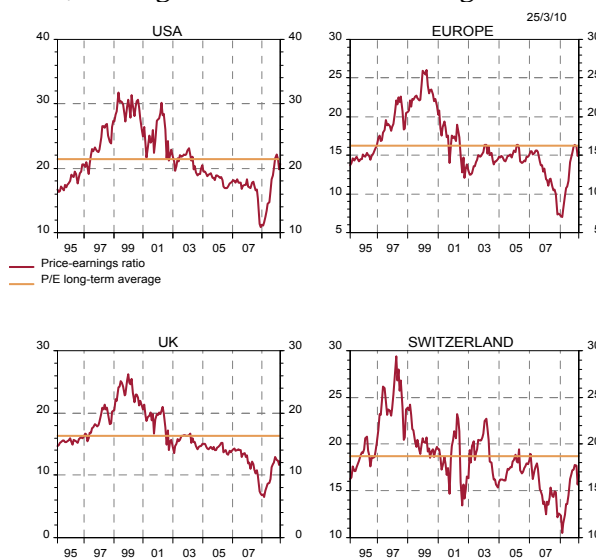
#### United Kingdom

- As regards the upcoming general election, the best outcome for UK stocks would be a clear and decisive victory for either of the two main parties
- Over the past two months, the public finances have already improved notably

#### Switzerland

- Strong fundamental data support equities and brighten the outlook for top-line growth
- Our regional allocation model suggests an overweight position in Swiss equities

### Price/earnings ratios still below average



Source: Thomson Datastream

The major drivers, such as the global economic recovery, the earnings rebound and loose financial conditions around the globe are still intact and underpin the current bull market in equities as well as credits. Namely so purchasing managers' indices and business surveys around the globe continue to climb to rather lofty levels in the meantime. After the biggest worries surrounding the Greece debt crisis and its potential contagion into other European countries has calmed down somewhat, investors' risk appetite staged a strong comeback. The first set of earnings reports for the first quarter 2010 will be published over the coming weeks and should underline the notion that earnings are increasingly driven by revenues rather than cost cutting initiatives. At the same time however, the surprise potential is diminishing as expectations of analysts and investors have adapted to a brighter outlook for revenue growth as well. Investors who have only limited risk-taking capabilities have reduced their equity exposure last year and need to enter the market in earnest. Money market allocations have not yet dropped to normalised levels which means that there is enough cash potential to provide tailwind for the ongoing rally in risky asset classes.

### Currencies

#### Notable Swiss Franc appreciation

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#### USA

- USD has lost some ground again against CHF which is a sign of strong Swiss economic data rather than USD weakness
- Economic outperformance does support the view of a stronger USD vs Euro in the longer run

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#### Euro Area

- Due to the Greek crisis, the Euro weakened against 13 of the 16 major currencies and fell to a record low level against the CHF
- We believe that EUR/USD has undershot fair levels due to Greece related concerns and we see the potential of a counter move in the short term

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#### Japan

- JPY should trade higher based on long-term drivers like the 2-year carry
- In the longer term, main drivers point to JPY weakness, reflecting a Fed exiting quantitative easing and a BoJ fighting deflation more vigorously and for longer

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#### United Kingdom

- Dovish comments by the Bank of England initiated the ongoing depreciation trend of GBP
- We remain constructive for the GBP, as low valuation, good surveys and relatively high inflation will eventually have the expected impact

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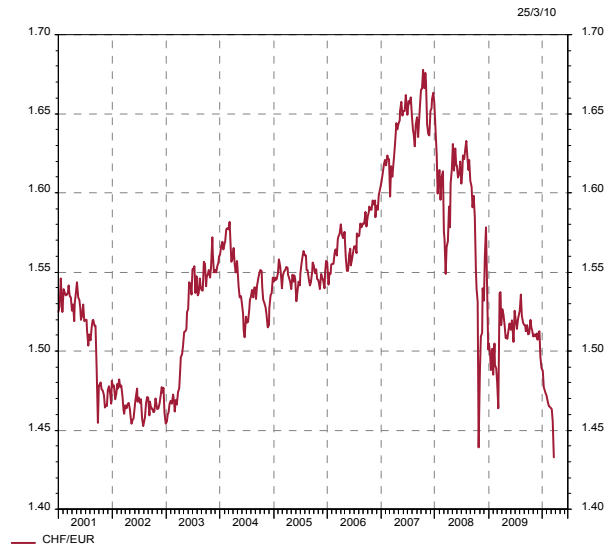
#### Switzerland

- A series of stronger than expected macro data cause a sharp appreciation of the Swiss Franc
- Unlike in the past, the Swiss National Bank has abstained from FX intervention thus far
- We expect the CHF to depreciate versus EUR in the mid-term even without support from the SNB

#### Released and approved by the Economics Department

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#### Euro on lowest level since inception



The Greek tragedy continues to be the dominant factor in determining currency movements. Europe's single currency weakened to a 10-month low versus the Greenback after French and German political leaders said any bailout package for Greece would require IMF help. Against the Swiss Franc, the Euro even fell to the lowest level since its inception. Yet, the latest macro and survey data out of the Euro core countries underline that the recovery phase is still gaining strength and should thus calm fears as regards growth dynamics going forward. We think the Euro has thus undershot fair levels and see the potential of a counter move of the Euro versus USD to fundamentally more consistent levels as qualms surrounding Greece should settle. In the longer term, however, the US economy's expected economic outperformance relative to the Euro Area and resulting implications as regards central bank action should add tailwind to a USD appreciation. A stronger USD forecast is substantiated by our 2-year carry regression model, which we enriched by a risk sentiment factor in the meantime. Indeed, quality and extent of the US recovery in particular and central bank parlance are key to FX crosses going forward.