

Weekly Economic Update

25th April 2010

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Summary

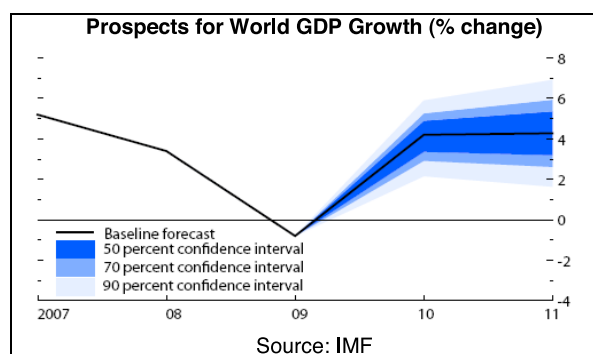
The UK economy continued to grow in the first quarter of this year. However, the pace of the recovery has slowed, which will give the political parties further debating ground ahead of the general election on 6 May. Against the backdrop of rising raw material and commodity prices, a weaker currency, somewhat stronger economic activity and loose monetary policy, the rise in inflation is starting to create some unease.

Statistics

Economy

World Economic Outlook

The IMF revised up its forecasts for global growth, now predicting 4.2% in 2010 and 4.3% in 2011, noting that recovery, though unsynchronised, has been faster and stronger than expected. The advanced economies will underperform, with growth to remain sluggish, but emerging and developing economies, outside of emerging Europe and the CIS, are recovering more strongly. Many emerging countries are again growing rapidly and some have begun to slow their accommodative economic policies in the face of high capital inflows. The IMF projects 2010 growth of 3.1% for the US, 1% for the Eurozone, 1.9% for Japan, 10% for China, 8.8% for India and 5.5% for Brazil. Global restocking will account for a significant portion of growth, which may prove temporary. Also, activity remains dependent on highly accommodative macroeconomic policies. According to the IMF, fiscal stimulus planned for 2010 should be implemented to give the economy momentum, apart from countries where the need to restore confidence by reducing large deficits are paramount.

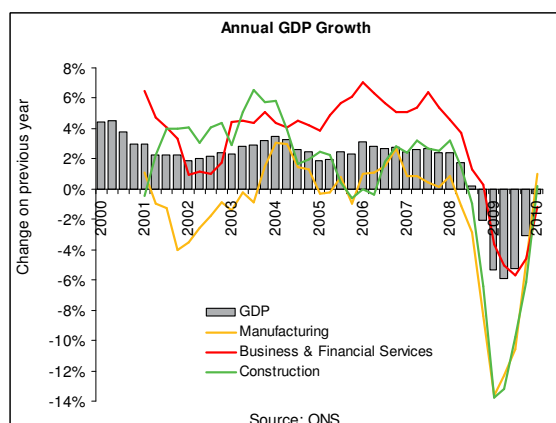


Global financial stability

Risks to global financial stability have eased as the economic recovery has gained steam, according to the IMF's latest Global Financial Stability report. However, concerns about advanced country sovereign risks threaten stability and could prolong credit constraints. In addition, in some emerging market countries the surge in capital inflows has led to fears of inflation and asset price bubbles. The IMF reduced the estimated bank write-downs and loan provisions during the financial crisis to date (2007-2010) to \$2.3 trillion from \$2.8 trillion in October 2009, due to improving economic conditions. Two-thirds or \$1.5 trillion of the expected losses had been realised by the end of 2009. Banking system health is generally improving, due to economic recovery, continued de-leveraging and normalising markets. Bank capital needs have declined substantially, but segments of banking systems in some countries remain capital deficient, mainly due to losses related to commercial real estate. Financial sector repair and reform remain high-priority requirements. Banks face considerable challenges: a large amount of short-term funding will need to be refinanced this year and next; more and higher-quality capital will likely be needed to satisfy investors in anticipation of future more stringent regulation; and not all losses have been written down to date.

UK growth

The pace of the UK economic recovery slowed in the 1st quarter of 2010, with activity dragged down by the harsh winter. According to a preliminary estimate, UK GDP expanded by only 0.2% during the quarter and was down 0.3% year-on-year. The services sector rose 0.2% quarter-on-quarter, but was down 0.2% compared to a year ago. Within this, the business and financial services sector was up 0.6% during the quarter, but 1.2% down year-on-year. Manufacturing production increased 0.7% in the 1st quarter of 2010 and up 1% year-on-year. The sector is benefiting from re-stocking, improved competitiveness due to the weaker pound, and a pick-up in domestic and export demand. Construction output contracted by 0.7% quarter-on-quarter, as it was hit particularly by the bad weather. Construction output was up 0.2% year-on-year. Overall, the UK economic recovery is still being supported by low interest rates and quantitative easing, a weaker currency and stronger global trade. Growth is expected to strengthen over the course of 2010. However, the upside for UK growth in the years ahead could be limited by a substantial tightening of fiscal policy needed to restore public finances.



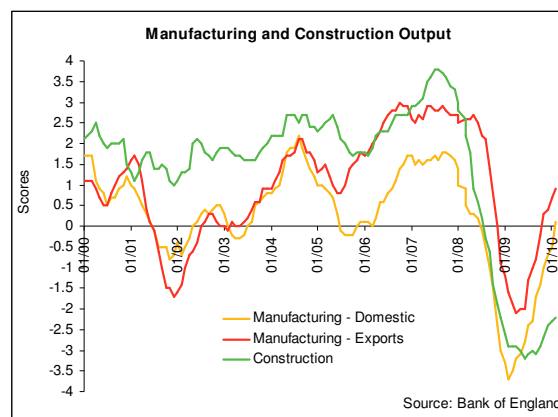
Bank of England minutes

The Monetary Policy Committee's decision in April to leave the bank base rate on hold at 0.5% and maintain its Asset Purchase Facility at £200bn was made unanimously. The minutes of the meeting reveal that the MPC was relatively optimistic about the prospects for growth, but it voiced increased concern over the strength of inflation, which jumped to 3.4% despite weak activity.

Business Condition survey

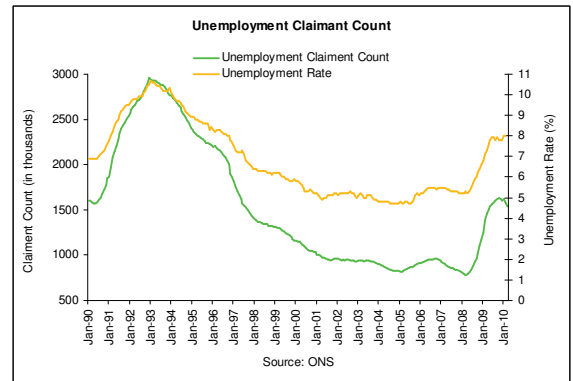
The Bank of England's survey of Business Conditions in March reveals that:

- Consumer spending and retail sales growth has softened slightly.
- Housing demand and supply appears to be balancing and house prices, which had been rising for a number of months, are stabilising.
- Investment intentions picked up a little, but remain subdued. The main constraints are the wide margin of spare capacity, tight credit conditions and uncertainty about future demand and plans for public spending.
- Business services output picked up, due to stronger. Manufacturing output continues to recover gradually.
- Construction activity is still low, although there are some signs that activity has stabilised in recent months. New homebuilding has picked up slightly. However commercial property construction remains particularly weak. Looking ahead, anticipated public spending cuts are likely to undermine future workload.
- The availability of bank lending has improved modestly in March. At the same time, demand for bank finance remains weak, with companies continuing to repay debt, and large businesses resorting to the capital markets for their financing needs.
- Pay pressures remain muted. In contrast, non-labour costs continue to rise, reflecting increases in metals prices and transport costs. Prices of steel and fuel have risen further in March, in part due to higher demand from emerging economies. Transport and freight costs picked up sharply, reflecting earlier reductions in global capacity as ships and container vessels were temporarily taken out of service
- Manufacturing output prices rose slightly in March. Consumer price inflation stabilised.



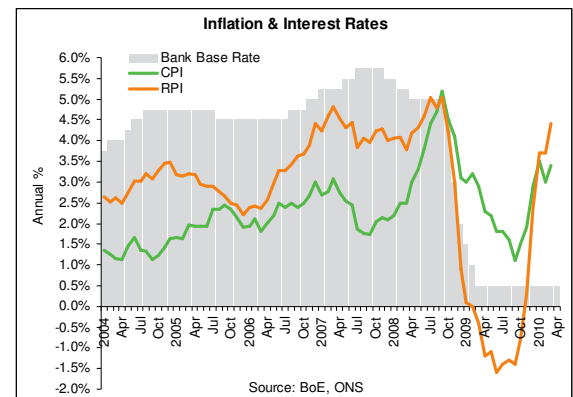
Labour market

The latest UK labour market data reveal a mixed picture. Unemployment rose 43,000 in the three months to February to 2.5 million, the highest for 16 years. The unemployment rate rose to 8%. The number of people employed fell to the lowest level since 2005. However, the number of people seeking benefits fell by 32,900 in March, the fourth decline in five months. Average weekly earnings, including bonuses, rose 2.3% on a year earlier, up from 0.8% in the three months to January, largely driven by the financial sector bonuses.



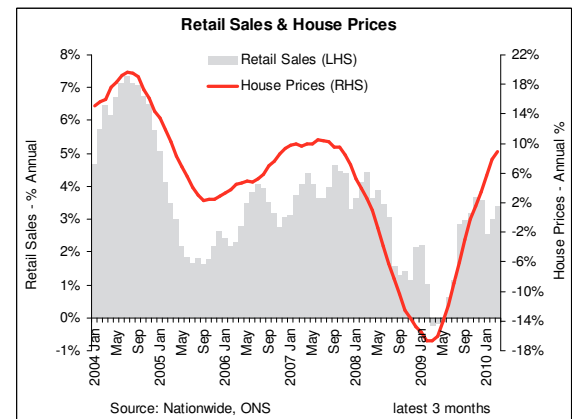
Consumer price inflation

CPI inflation rose by more than expected in March, jumping to 3.4%, up from 3% in February. The retail price index rose 4.4% year-on-year in March, the fastest pace of price increases since September 2008. The largest upward contribution in CPI came from housing and household services. A further increase came from fuel prices. Despite the sharp increase, the Bank of England believes that inflation will come down appreciably by the end of the second quarter 2010.



Retail Sales

The seasonally adjusted value of retail sales excluding fuel rose by 4.5% in March compared to a year ago. Retail sales volumes were up 4% over the same period. Whilst retail sales have been firm in recent months, consumers continue to face challenging conditions, including higher unemployment and low earnings growth. This together with a still uncertain UK economic outlook will make consumers cautious about their spending.



Retailer survey

UK retail sales values in March rose by 4.4% on a like-for-like, buoyed by Easter sales, according to the British Retail Consortium. On a total basis, sales rose 6.6% year-on-year. Food sales continue to outpace non-food sales, as consumers remain cautious in the face of economic and political uncertainty.

Industrial trends

The CBI's industrial trends survey shows that UK manufacturing activity is strengthening. A majority of manufacturers' surveyed report that total order volumes rose in April, due to an improvement in both export and domestic demand. However, orders and output are recovering from thirty-year lows, and the level of order books remains below normal for the vast majority of manufacturers. Sentiment about the overall business situation is improving. Looking ahead, much stronger growth in orders is expected in the three months ahead. However, cost pressures appear to be intensifying due to rising raw material prices. Output price inflation is increasing and profit margins are coming under renewed pressure. Investment intentions for the year ahead remain subdued. In particular, the majority of firms report that they planned to reduce capital expenditure on buildings. 62% of firms say they are working below capacity.

Public finances

Total public sector net borrowing in the 2009/10 financial year was £152.8bn, up by £65.9bn from 2008/09. The public sector had a budget deficit of £14.8bn in March compared with a deficit of £12bn a year ago. Public sector net debt reached £890bn at the end of March,

equivalent to 62% of GDP. The UK entered the 2008/09 recession with one of the biggest structural budget deficits in the advanced economies. The crisis has led to an increase in expenditure, such as unemployment benefits, and a fall in tax revenues, in particular from the financial and real estate sector. This, together with banking sector support and the £20bn fiscal stimulus led to a sharp increase in public sector debt over the last financial year.

Housing market activity

The pace of UK housing market recovery appears to be slowing. According to the RICS's latest housing market survey, house prices continued to rise in March, but at a slower rate than in preceding months. Seller activity increased. The average stock of property on surveyors' books also rose, as the number of completed sales fell during the month. Buyer interest stabilised following 14 months of consecutive increases. Against this background, prices are expected to stabilise. However, there are significant differences among the regions. London, the South East and Scotland saw house prices rise firmly in March. In contrast, prices fell in East Anglia, Yorkshire and Humberside, the North and the West Midlands.

Exchange Rates

The Sterling continued to strengthen against the Euro last week, with one Pound buying €1.156. The Euro lost ground against other major currencies, as Greek bonds slumped and the cost of insurance against Greek default surged to a new record high. Against the Dollar, the Sterling held relatively stable last week at \$1.546.

Commodities

Oil prices rose last week to \$86.6 a barrel of Brent crude. Oil prices are now 70% higher than last year. In contrast, metals prices fell back, with copper and nickel down 3% and aluminium 7% lower. The iron ore index rose to \$178.48/tonne last week, up 3% on a week earlier and 23% higher than last month. The global steel price index held stable, but is up more than 50% compared to this time last year. Corus last week said it had raised its offers for reversing mill plate by £80/mt on all orders from April 23, due to rises in raw material costs and increasing demand. Corus previously raised reversing mill plate prices by £60/mt on February 7 and by another £60/mt on March 22.

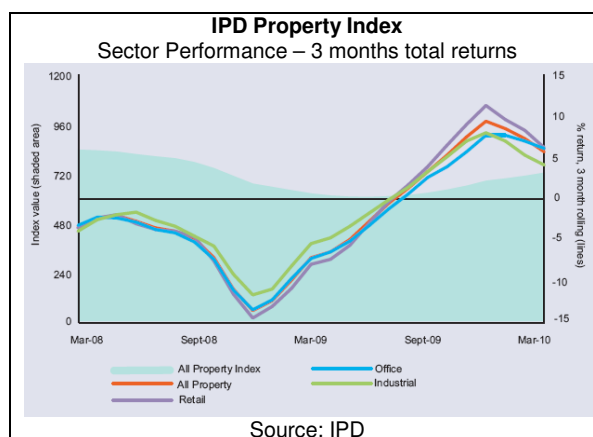
Commodity Prices (23rd April 2010)				
	Price	Weekly change	Monthly change	Annual change
"Brent" Oil (\$/barrel)	86.6	3%	7%	70%
Copper (\$/tonne)	7,660	-3%	3%	69%
Aluminium (\$/tonne)	2,265	-7%	2%	59%
Nickel (\$/tonne)	26,800	-3%	20%	135%
Global Steel Price (Index 04/1994=100)	195.96	0%	12%	51%

Source: FT, LME, Cruspi

Construction

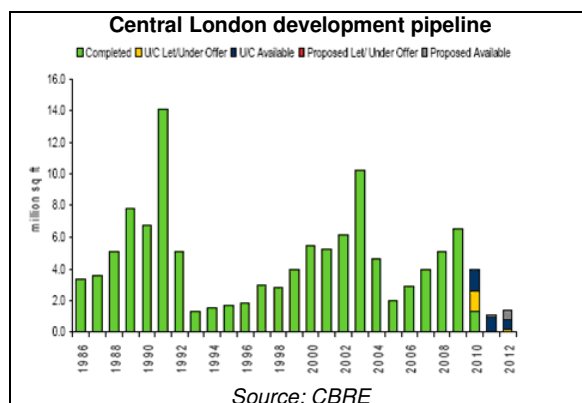
Commercial Property Returns

UK commercial property capital values rose further in March, up 1.6% compared to 1.3% growth seen in February. Offices capital growth was 1.8% in March, while retail values rose by 1.6% and industrial by 0.9%. Overall, commercial capital values rose by 3.9% in the 1st quarter of this year, compared to 7.4% growth recorded in the final quarter of 2009. The 12-month capital growth rate is now 7.6%. In March, the main drivers of capital growth were rental and yield movements. The office sector saw rents improve for the first time in two years. Overall average rents still declined by 0.1%. All property initial yields fell by 10 bps in March, to 6.7%. Over the last nine months yields have come down by 120 bps. Office yields fell by 120 bps, to 6.9% over the past eight months. Retail yields now stand at 6.4%, while industrial yields are 7.3%.



Central London offices market

According to the CBRE's monthly update on the Central London offices market, demand for space strengthened during the 1st quarter of 2010 to 4.4m sq ft, due to a number of large deals made. Occupancy rates in key buildings increased as take-ups improved. Availability in Central London fell by 16.7m sq ft at the end of the 1st quarter, down 22% from the June 2009 peak. Availability now stands at 7.7%. Supply in the City and West End declined to 6.6m sq ft and 6.2m sq ft respectively.



Looking ahead

The Nationwide is expected to report that house prices rose in April, but the pace may have slowed. The CBI Distributive Trades Survey for April is likely to show that a majority of retailers saw sales increase, as consumer spending remains more resilient than expected. The consumer confidence index is likely to show that confidence weakened further in April after suffering a slight relapse in March, due to persisting economic and political uncertainty.

Market Watch

The FTSE 100 ended last week slightly below the previous week's close, with equities under pressure from more negative updates from Greece, volatile commodity markets and mixed UK economic data.

Last week the US Securities and Exchange Commission (SEC) charged investment bank Goldman Sachs with fraud. It sued Goldman for having allowed hedge fund client John Paulson to select some of the underlying subprime credits in a portfolio, which he then shorted by buying insurance from Goldman, while not disclosing this to investors on the other side of the trade. Paulson earned \$1bn, while losing parties including RBS (\$840m) and IKB (\$150m) had to be bailed out by the UK and German governments. Goldman denies the charges.

Shares were also hit by the European no-flight ban due to a volcanic eruption in Iceland. The six day stop inflicted huge losses on the airline industry.

The biggest hit to the markets was once again due to Greece. The EU revealed that Greece's 2009 budget deficit was revised up to 13.6% of GDP from 12.9%. Moody's then cut Greece's sovereign rating and left the door open for further cuts. The yields on Greek 10-year bonds soared to nearly 9%, making it more expensive to raise funds. Greece had little choice than to trigger the EU/IMF support mechanism in the form of a €45bn loan facility agreed earlier in April.

Property companies had a mixed week. Quintain Estates and Developments and Derwent London performed well, with shares up 3.2% and 2.2%

respectively in the week to Friday. Shaftesbury and Hammerson also gained. All others saw their share price falling, with the Unite Group the biggest loser, down 3.2%.

Building contractor Morgan Sindall fell by 4.7%, while Balfour Beatty shed 1.4%. Other contractors, including Carillion, Kier and Lend Lease had a better week.

Among **building material suppliers**, SIG and Wolseley were up last week, gaining 10.2% and 6% respectively. In contrast, Marshalls and Kingspan share prices fell 5.3% and 2.8% respectively.

House builders performed strongly last week, with Taylor Wimpey and Persimmon seeing double digit share price growth.

Share Prices	Friday 22 nd April 2010			
	Index	Week	Month	Year
FTSE100	5,724	-0.4%	0.9%	42.4%
	Market Cap, £m	Week	Month	Year
Real Estate				
British Land	4,150	-0.7%	3.9%	13.1%
Hammerson	2,770	1.7%	2.7%	30.3%
Land Securities	5,110	-0.7%	-0.9%	28.6%
Liberty Intl.	3,160	-1.3%	3.8%	23.5%
Shaftesbury	896.8	2.0%	6.3%	44.8%
Great Portland Est.	1,020	-1.0%	8.7%	57.2%
Derwent London	1,480	2.2%	11.5%	75.9%
Segro	2,340	-0.8%	0.5%	36.7%
Quintain Estates & Development	290.2	3.2%	-0.9%	203.3%
St. Modwen Properties	379.3	-2.3%	2.3%	26.2%
Unite Group	374.1	-3.8%	-9.3%	143.2%
Workspace Group	275.9	-2.0%	6.7%	60.0%
Minerva	188.2	-0.4%	39.8%	749.1%
Average**		-0.3%	3.1%	41.7%
Building Contractors				
Balfour Beatty	2,010	-1.4%	2.8%	0.0%
Carillion	1,420	1.4%	11.5%	47.5%
Morgan Sindall	248.0	-4.7%	4.6%	-5.9%
Kier Group	422.5	3.2%	7.1%	24.5%
Lend Lease Corp*	2,840	2.9%	-0.1%	28.1%
Average		1.1%	3.7%	22.5%
Building material suppliers				
Wolseley	4,710	6.0%	4.0%	44.7%
SIG	814.9	10.2%	14.9%	4.6%
Marshalls	194.0	-5.3%	6.5%	1.2%
Kingspan	1,036	-2.8%	12.5%	102.3%
BSS	378.0	1.8%	14.1%	0.1%
Average		4.7%	7.1%	44.9%
Housebuilders				
Persimmon	1,500	10.7%	11.7%	27.1%
Taylor Wimpey	1,410	14.8%	14.9%	24.0%
Barratt	1,270	9.0%	5.9%	28.3%
Bovis Homes	586.2	6.8%	11.1%	-3.0%
Bellway	967.1	6.0%	11.3%	6.2%
Berkeley	1,190	6.4%	6.7%	-11.6%
Average		9.5%	10.3%	14.6%

*Lend Lease Corporation Limited is listed on the Australian and NZ stock exchange

**Sector averages are weighted according to current market capitalisations