



# BREWIN DOLPHIN

## MARKET STRATEGY

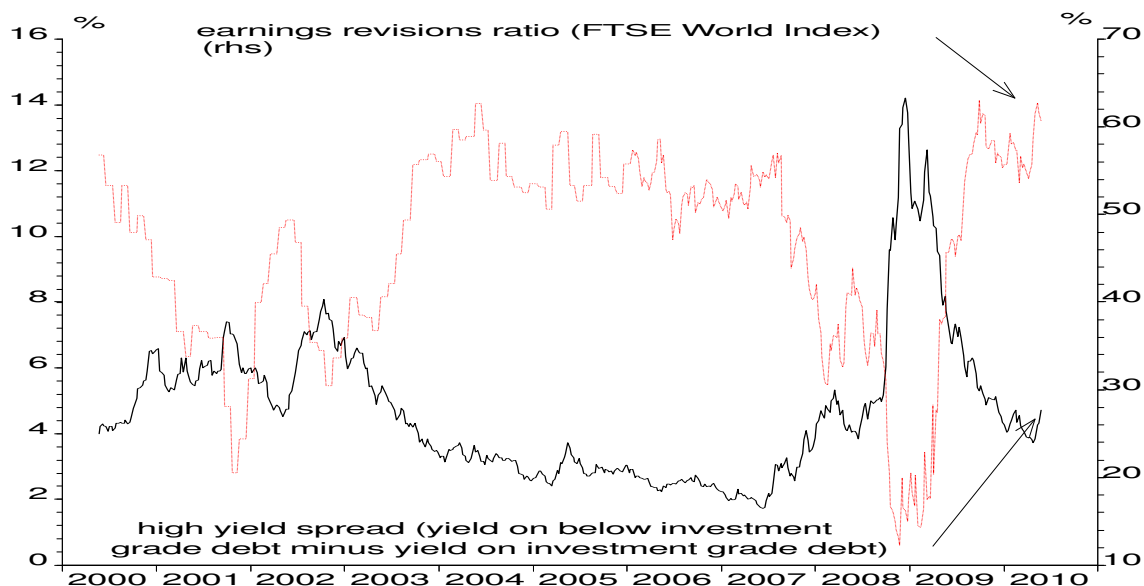
INVESTMENT RESEARCH

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***So, if you've got your gilts, hang on to them!***



Source: DATASTREAM

Credit spreads have been opening up over the past weeks but the feature that is particularly worrying is the widening of the high yield spread. The latter has tended to be a good 'predictor' of earnings news flow. As the chart shows, the earnings revisions ratio – the proportion of companies for which analysts are revising up their earnings estimates – has varied inversely with it.

As outlined in a recent note ([What's really bugging Wall Street, 21 May 20110](#)), there is potentially a strong deflationary impulse associated with the sovereign debt crisis. For a start, the sentiment created by the sovereign debt crisis risks adversely influencing consumer and business confidence. On top of this, the imposition of fiscal austerity risks impeding a recovery in Europe that has barely begun. Meanwhile, the risk of an appreciating dollar is a loss of recovery momentum behind the dollar bloc (notably the US and China), the bloc that has led the upswing in the global economy.

A strong dollar retards economic growth not only by inhibiting exports for dollar priced goods and services but also by encouraging a substitution of imports for domestic output in the dollar bloc.

For equity markets, the risk then is a 'less good' backdrop for earnings news flow. It would not be surprising to see earnings expectations trimmed as the year progresses. Not a cheerful prospect for equity markets!

All of which suggests that the major central banks are likely to keep policy on hold for some while. So, if you've got your gilts hang on to them!

## IMPORTANT NOTES

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