

Market Review

The market was strong in the fourth quarter, driven mainly by the performance of underlying equity. Convertibles returned 8.1% for the quarter and 16.8% for the year. They outperformed not only the Standard and Poor's 500 Index, but Treasuries, high yield and investment grade bonds, as well. Investors continued to favor risk in the quarter, as they anticipated the Federal Reserve's (Fed's) second round of quantitative easing.

A solid holiday shopping season resulted in strong performance of the consumer discretionary sector for the quarter. The metals sector also was a top performer, as high demand and a weak dollar drove commodities prices. Building on the previous months' trends, investors continued increasing their allocations to risk assets in the quarter.

Interest rates edged up after a long trend downward. This might be attributed partially to rich pricing and re-allocations to riskier assets. Meanwhile, new issuance continued to be weak; historically low spreads and interest rates offered companies attractive capital alternatives in the straight debt market.

The capital markets remain focused on monetary policy. The Fed's decision to embark on another round of debt purchases drove equities and spreads tighter, as investors searched for returns. This also had a negative effect on the Treasury market.

Outlook and Strategy

We are seeing a rising consensus for growth in 2011, as more sectors price in a sustained economic recovery. We expect continued monetary interventions to distort markets in the short term. We remain somewhat defensive, because of the two main overhangs that remain unresolved in the U.S. economy: Unsustainable leverage at the federal, state, local and personal level; and structurally high underemployment and unemployment.

We will look to job growth as a sign of that a sustainable U.S. recovery is underway. In addition, we'll watch closely for any changes resulting from the execution of monetary policy. We like the defense and health care sectors and are cautious on financials. In general, converts continue to show strength as underlying equities move upward.

Important information

Past performance is not indicative of future results. This commentary contains the current opinions of Aviva Investors and is not intended to be, and should not be interpreted as, a recommendation of any particular security, strategy or investment product. Such opinions are subject to change without notice. This commentary is distributed for informational purposes only and is not a recommendation or investment advice. The information herein is based on sources which Aviva Investors believes to be reliable, but it is not guaranteed to be accurate or complete.

Forward-looking statements, opinions and other information contained in this article are subject to change continually and without notice and may no longer be true after the date of publication. Any such statements speak only to the date they are made and Aviva Investors North America assumes no duty and does not undertake to update forward-looking statements. Such statements are subject to numerous assumptions, risks and uncertainties, which may change over time. Actual results may differ substantially from those anticipated in forward-looking statements. Past performance is not indicative of future results. There is potential for profit or loss with any investment.

No part of this commentary may be reproduced in any form, or referred to in any other publication, without the express written permission of Aviva Investors North America, Inc.

Performance is shown gross of fees and does not include the deduction of management fees and other expenses that may be incurred in managing an investment account. A portfolio's return will be reduced by advisory and other fees.