JANUS

Investment **Insights**

April 2009

Market Perspectives from Janus' Seven Global Sector Teams

The market environment has been extremely challenging over the past 18 months, and it may take some time for the market and economy to stabilise. Despite the generally bearish sentiment, however, we think there are many individual investment opportunities in the market today that offer compelling valuations and risk/reward profiles. In this paper, Janus' seven global sector teams provide their bottom-up views on a range of topics impacting the companies they cover, from short-term cyclical developments and the new US administration's policies, to secular themes that they believe will drive long-term performance.

Acknowledgements

This paper is the result of a collaborative effort among members of Janus' investment team and investment writers, and represents the collective expertise of the firm's portfolio managers and research analysts. The opinions expressed herein should not be construed as investment advice.

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Executive Summary

The market environment has been difficult over the past 18 months. No region or sector has been immune to the negative sentiment and sell-off plaguing world equity markets. Governments around the world have attempted to restore confidence, but markets have continued to struggle as investors remain concerned with the potential depth and length of the current economic downturn. While we do not know how long this downturn could persist, we think the recent volatility and weakness have provided opportunities for long-term investors.

Recent market performance has demonstrated to us that investors have been fearful and afraid to invest in business opportunities, or take advantage of the relatively low valuations across many sectors and regions of the world. Europe and Asia are suffering through recessions along with the Americas, but we are finding individual opportunities in each of these areas where we believe investors have overreacted. Emerging markets, which collapsed even more than developed markets during the worst of the sell-off, now offer favourable risk/reward opportunities for certain investors in our view.

As we look at the macro picture, it is clear the global economy faces many challenges and that it would be easy to remain bearish on the overall market in the near term. However, we think there are a number of positive developments to keep in mind. These include the potentially favourable impact of the fiscal stimulus, the significant decline in energy prices and lower mortgage rates. Finally, we have begun to witness markets functioning normally again. In September and October 2008, markets traded down on fear and a crisis of confidence – not because of the particular prospects of individual companies. Since the beginning of 2009, however, company fundamentals have begun to matter again to investors – an environment that we believe is well-suited to our investment approach.

At Janus, we pride ourselves on our in-depth fundamental research, which gives us conviction in our beliefs during a difficult – or any – market environment. It may take some time for the economy and the market to emerge from the current malaise, but once they finally stabilise, we believe the intrinsic values of the companies we own could be realised, potentially in a way that could prove beneficial to our investors.

The following discussion provides the opinions of Janus' seven global sector teams, listed below. These sectors are defined by Janus, based upon how Janus aligns research teams. Therefore, Janus may place a small number of industries in different sectors than MSCI or Barclays assigns them (i.e. Janus moved drug retailers from the consumer sector to the healthcare sector).

- Communications
- Consumer
- Energy
- Financials
- Healthcare
- Industrials
- Technology

These opinions cover topics ranging from short-term cyclical developments and the new US administration's policies and approach to handling the financials crisis along with their respective impacts on various sectors, to secular themes that we think will drive long-term global sector performance. These global assessments play a role in how we evaluate individual companies – consistent with our bottom-up research effort – the core of the Janus investment process for nearly 40 years. Our fixed income and equity teams continue to work closely together, modelling businesses in an effort to determine if they can service their debt and improve their competitive position, thus increasing their chances, in our view, of emerging from the recession in a stronger position. We believe our research has uncovered many individual companies trading at attractive valuations relative to our estimate of their future cash flows.

While this discussion provides the teams' thoughts and positioning within each global sector through the end of March 2009, it is important to note that these views could change without notice, particularly in today's volatile environment. In addition, these opinions were not necessarily shared by the portfolio managers at Janus. Nevertheless, there was some consensus among the sector teams that valuations in many segments of the equity and bond markets were very attractive, along with many risk/reward profiles. Through our fundamental research, we believe we can uncover these opportunities in an effort to benefit our clients and shareholders long term.

We believe staying true to sound, time-tested investment principles will help increase investors' chances for long-term success. Historically, when the environment has seemed to be at its worst, it has often been a good time to invest. We think there are many individual opportunities in the market today that offer favourable risk/reward profiles. While the road to recovery could be lengthy, we continue to believe that the Janus research process, which combines the views of our fixed income and equity market teams, will help lead us to these opportunities.

Communications Sector

"In general, we're looking for the secular growth opportunities that we think have become inexpensive because of the cyclical impact the current environment has had on their revenue streams."

Summary

Consumers and businesses worldwide have been pulling back, and economic activity across the globe has suffered greatly. This proved to be a challenge for the communications sector in 2008. The sector's 38% decline, according to the MSCI World Index, was slightly better than the 40% drop posted by the overall index in 2008. The sector was down more than 10% through March 2009 compared to a nearly 12% drop for the overall index. Companies that fit within the Janus communications sector are summarised in Exhibit 1.

Exhibit 1
Sub-Industry Classifications of the Communications Sector

Advertising	Internet Software & Service
Alternative Carriers	Movies & Entertainment
Broadcasting & Cable TV	Photographic Products
Catalog Retail	Publishing
Integrated Telecomm Services	Wireless Telecomm Services
Internet Retail	

Source: Janus

Outlook

Similar to the second half of last year, 2009 is likely to be a difficult year for this sector because of the continuing credit crisis and the significant impact it has had on consumer and business spending (Exhibit 2). We are hopeful the US government's stimulation measures, as well as the coordinated efforts of other governments around the world, will begin to stabilise consumer spending by the second half of the year and perhaps lead to a rebound in consumer activity and, ultimately, communications stocks in 2010.

The most cyclical companies within the sector are typically those exposed to advertising revenue, such as advertisers, broadcasting and cable TV companies, catalog retailers, publishers and, to a certain extent, Internet software and services providers. We think advertising revenue will continue to decline over the short term and eventually rebase at a lower long-term rate of growth for all major world economies. We expect to experience a trough in advertising earnings and consumer pressure during the first half of 2009, but believe signs of improving conditions will begin to emerge by the second half of 2009 as a result of the massive global monetary stimulus currently being implemented. In our opinion, advertising will continue to be under pressure in the near term with the weakness spreading to all advertisers, even the leaders, and across all media.

Investors have been very focused on short-term cash flow and leverage profiles, and have been unwilling to take the risk on growth businesses that might develop over the next two to three years. This fearful mind-set has created opportunities for us to invest in strong franchises that we believe will survive and are themselves investing in opportunities that could develop over the next three to five years, thus potentially positioning themselves to emerge from the current malaise in a much stronger position.

Exhibit 2

Issues Facing the Communications Sector

Negatives	Positives
Debt levels and access to capital	Valuations
Weak consumer trends	Favourable secular growth trends in select industries
Sharp slowdown in business spending	

Source: Janus

Positioning

Despite our bearish outlook for advertising, we have identified a select global advertising agency that we feel is seeing more manageable revenue declines than the overall measured media market due to its globally diverse business and fee-based revenue structure. In addition, we believe its highly variable cost structure will help its margins remain fairly stable, potentially helping the company weather the current environment.

We are also using the current market environment as an opportunity to invest incrementally in other businesses that have already been hit hard by fear and where we believe the market is placing too great an emphasis on the short-term risks. Examples include select Internet companies, global media giants and wireless tower infrastructure names that fit our criterion of possessing strong, defensible franchises that are highly cash generative and are producing strong returns on investment. These companies also have the potential to benefit from secular growth drivers and management teams that can capitalise on those opportunities. In particular, market fears have weighed heavily on a select wireless tower company with a relatively high degree of debt on its balance sheet. We think the company has a strong franchise that is growing and is supported by very stable cash flows. While we have been cognisant of the company's debt levels, we have taken a different view than the market because we think these attributes will allow it to service its debt and continue its growth. After running aggressive downside scenarios in our financial models, we feel that recent valuations more than compensate for the risks associated with holding this or any similar name over the short term.

Among other areas of interest are telecommunications companies in developing markets. We are bringing our experience in analysing mature telecommunications companies and applying them to emerging markets, such as assessing the impact that growing data usage in the markets will have on such companies going forward. We are weighing long-term trends, such as increased use of data plans and lower capital expenditure needs, against the stressed economic environments and positioning ourselves accordingly. In addition, we are doing detailed studies on established cable companies to gain a deep understanding of their financing needs and risks to the leverage they have employed.

Long term, we see opportunities in the sector arising in two particular areas: Internet and mobile communications. These areas have been driving winners and losers in not only content, but distribution strategies. The growth in demand for data services via the Internet and via mobile communications globally has been increasing at a significant rate, and we are focusing on the secondary impacts this trend could continue to have on everything in the communications sector, including media. While we have been positioned somewhat defensively in recent months, we think there are many long-term secular growth opportunities to exploit.

Consumer Sector

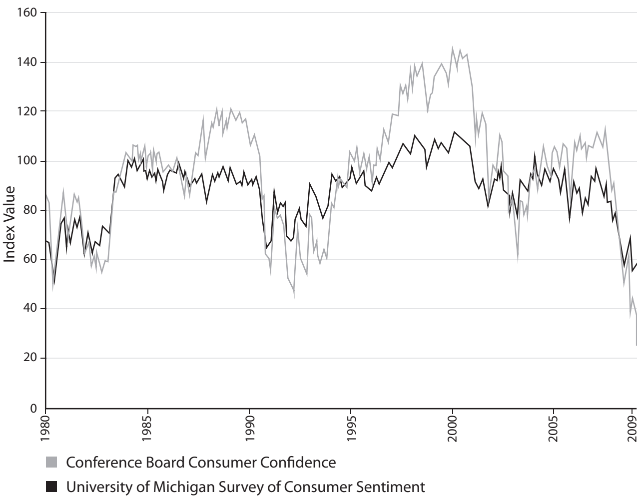
"In any environment, there are going to be winners and losers, so we have tried to focus on companies in the consumer space that are focused on selling necessities – companies that are focused on and successful at providing exceptional value to consumers."

Summary

The rapid deceleration in the global economy negatively impacted the consumer sector going into the 2008 holiday season and continued to do so through January 2009. The Conference Board's Consumer Confidence Index in the United States touched an all-time low in late February, indicating the extent of the consumer fallout (Exhibit 3).

Exhibit 3

Consumer Confidence and Sentiment



As of March 31, 2009
Source: Bloomberg, Conference Board, University of Michigan

Increasing unemployment, falling home values and investment portfolios as well as widespread uncertainty have weighed significantly on the consumer. Despite the dramatic decline in confidence, the consumer sector (summarised in Exhibit 4) was one of the best performing groups on a relative basis during 2008, although its roughly 26% decline, according to the MSCI World Index, was of little consolation.

Strong growth in necessity spending (staples) helped partially offset the declines in discretionary spending. To date, the sector has outperformed the overall market, declining 10% through March 2009.

Exhibit 4

Sub-Industry Classifications of the Consumer Sector

Agricultural Products	Home Improvement Retail
Apparel & Luxury Goods	Hotels, Resorts & Cruise
Apparel Retail	Household Products
Automotive Retail	Hypermarkets & Super Centers
Brewers	Leisure Facilities
Casinos & Gaming	Leisure Products
Computer & Electronic Retail	Meat, Poultry & Fish
Department Stores	Packaged Foods & Meats
Distillers & Vintners	Personal Products
Distributors	Restaurants
Education Services	Soft Drinks
Food Distributors	Specialised Consumer Services
Food Retail	Specialty Stores
Footwear	Textiles
General Merchandise Store	Tobacco
Home Furnishing Retail	

Source: Janus

Outlook

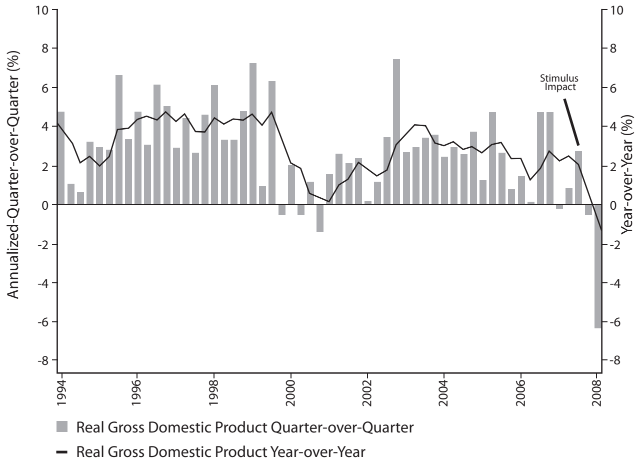
Consumer spending worldwide is likely to remain weak over the short term because of less credit availability, rising savings rates, accelerating unemployment and consumers' generally cautious outlook. While this may support taking a bearish stance on the consumer over the near term – which was the case for us heading into the 2008 holiday season – we are encouraged by some signs of stabilisation that emerged in March. For instance, February same-store sales among some generally discretionary retailers improved from prior months. In addition, other retailers indicated sales trends that were less negative than in late 2008. This suggests to us that the rate of decline in consumer spending may not be getting worse. As a result, we have recently become more constructive on discretionary-related companies.

The retail area is a business model that has historically been predicated on two main components: adding new stores (increasing square footage) and generating positive same-store sales growth. Our concern is that many retail business models could be irreparably damaged as a result of the credit crisis and subsequent economic downturn. A sudden and sharp slowdown in sales per square foot and very slow foot traffic have resulted in negative operating leverage for many of these retailers, which has compounded their decline. As a result, we are attempting to avoid companies in this sector that we believe have "broken" business models.

The recently passed $787 billion US stimulus package should be beneficial for consumers, but we expect the impact on overall spending to be temporary at best (a few months). The $350 billion US fiscal stimulus passed in March 2008 helped boost second quarter US gross domestic product, of which roughly 67% is consumer spending. But this was short-lived as subsequent quarters showed continued deterioration in economic activity (Exhibit 5).

Exhibit 5

US Gross Domestic Product



As of March 31, 2009
Source: Bureau of Economic Analysis, Bloomberg

We think the more progressive tax code in the United States, which seems to be the approach that President Barack Obama's administration is taking with its recent budget plan, is likely to have an impact on the sector. This would likely be a negative for higher-income consumers and better for low- and middle-income consumers, which could be beneficial for lower-end retailers that tend to have more staple products.

Finding the right companies in which to invest is a continuous, bottom-up process at Janus. We talk with suppliers, competitors and distributors to verify which companies are doing well so we can confirm our investment thesis and determine whether the growth prospects of a company are sustainable.

Our research efforts also include taking surveys with, for example, cosmetics salespeople and retail shoppers to obtain a better sense of current consumer trends and current sentiment. The analysts will also routinely visit stores to assess customer traffic as well as stores' discounting techniques, which can have a profound impact on profitability. Visits ahead of the holiday season showed that outlet or discount malls in the United States

Exhibit 6

Issues Facing the Consumer Sector

Negatives	Positives
Weak housing market	Stimulus package
Rising unemployment	Valuations for select groups
Negative sentiment and rising savings rate	Improving same-store sales trends

Source: Janus

were displaying similar merchandise to the main stores, suggesting downward margin pressure as companies tried to move inventory off their shelves any way they could. More recently we have seen a reduction in retail inventories, suggesting to us that the risk of markdowns is now much lower than it was in late 2008.

Exhibit 6 summarises the issues we believe will affect the consumer sector.

Positioning

In the current environment, we are favouring consumer companies that we think offer value to consumers, can potentially generate significant cash flows and have conservative balance sheets. We also favour those with strong, leading brands that are less likely to lose (and potentially more likely to gain) market share in a challenging environment. Finally, we seek quality companies with valuations that we think imply severely bearish outlooks.

Currently, our highest conviction holdings include well-managed discount stores and consumer products companies. Our holdings have become balanced between discretionary and staples holdings as compared to last year when we were more tilted toward staples. While we have remained cautious on high-end retailers worldwide, we have been making incremental investments in select names due to what we think were significantly depressed valuations. We don't believe these names have been as severely impacted as the market thinks. These are premiere retailers that we feel will come out of the current environment stronger.

We have also invested in stores that have benefited from the closing of competitors, which we were able to anticipate by monitoring suppliers at the height of the credit squeeze. Other investments have been in retailers that we felt will benefit from company-specific factors, such as organic growth and market share gains, which could help them overcome the difficult macroeconomic environment, or in stores that have demonstrated stability and were benefiting from the trading-down trend we have seen in the sector.

Finally, we are focused on companies that have non-US growth exposure while being cautious of currency exposures and how they impact their business models. Overall, we have been very sensitive about the type of retailers that we have been aligned with and are looking for companies that we believe continue to have the ability to address the value proposition with consumers, who, in our view, want high quality at a reasonable price (not necessarily the cheapest price). We believe our long-term, grass-roots approach; focus on conservative balance sheets and cash flow generation potential; and attention to valuations can help us identify consumer sector names that are likely to emerge from the current downturn in strong positions.

Energy Sector

"While we acknowledge the pressure from a slowing economy, we think the energy sector is an attractive area to invest because of long-term supply and demand dynamics."

Summary

The energy sector saw a strong reversal of fortune during the second half of 2008 as oil, natural gas and other energy prices retreated from record levels. Crude oil fell from its peak of near $150 per barrel in July to the $40 per barrel level as the year came to an end. Concern over a sharp drop in demand given the weakening economic environment has been a strong crosscurrent for oil prices and the rest of the energy sector in recent months. In 2008, the energy sector within the MSCI World Index declined more than 35% and was down a more modest 11% through the end of March 2009.

Exhibit 7 summarises the companies we consider to be a part of the energy sector.

Outlook

Broadly speaking, oil and natural gas prices have been under pressure, but we do not think the demand destruction that has occurred as a result of the global economic slowdown will last. As a result, we think oil and natural gas prices are more likely to head higher than lower.

Because oil and natural gas prices have such a big influence on the performance of many of the companies in this sector, we spend a lot of time combing through and analysing production and consumption data to forecast future supply and demand for oil and natural gas prices. In the case of oil, the data we have gathered and maintained on various oil fields and regions worldwide suggest supply conditions are likely to remain relatively tight over the long term, partly because the bulk of new supply is coming from harsher environments and deeper waters, which are technically challenging and higher cost areas. Part of our research process is to understand the geology of the fields and location of the natural resources within the field. We speak with seismic engineers, geologists and other industry experts to gain greater insight into the potential and likely amount of oil produced from a given field, including the duration, peak production levels and potential costs.

Based on our research, we have found that most new supply requires oil prices above $40 per barrel in order for an oil company to earn more than its cost of capital. For instance, some of the discoveries in the deep waters off the coast of Brazil are roughly 5,200 meters below the ocean floor, which not only requires specialised technology to extract, but will likely take years before maximum sustainable production rates are reached. In addition, numerous wells may be required to extract the oil. All of this raises the overall cost of production and the price of oil required for a company to develop oil in this region. As a result, we believe the price of oil is likely to move higher rather than remain at current levels.

Long term, there are many other reasons we have found to support our view that the supply of oil could be less than the market expects and that oil prices could move higher.

Exhibit 7
Sub-Industry Classifications of the Energy Sector

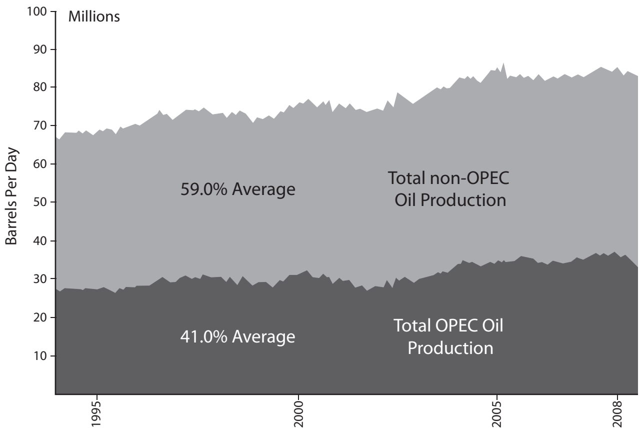
Coal & Consumable Fuels	Oil & Gas Drilling
Electric Utilities	Oil & Gas Equipment & Services
Gas Utilities	Oil & Gas Exploration & Production
Independent Power Producers & Energy Traders	Oil & Gas Refining & Marketing
Integrated Oil & Gas	Oil & Gas Storage & Transportation
Multi Utilities	Water Utilities

Source: Janus

First, we estimate that at peak production, recent large discoveries will represent less than 2% of the amount of oil currently being produced in a day. Second, countries that belong to the Organisation of Petroleum Exporting Countries have a larger influence on incremental supply hitting the market than non-OPEC nations. Over the past 15 years, OPEC has accounted for roughly 41% of the world's total daily oil production (Exhibit 8).

Exhibit 8

World Oil Production (OPEC vs. Non-OPEC)



As of February 28, 2009
Source: Bloomberg, Energy Intelligence Group

As a result, cuts in OPEC production can greatly influence the supply and price of oil. Many OPEC nations do not have a big incentive to produce more oil at $40 per barrel given the demands on their fiscal budgets. Countries like Saudi Arabia need to generate substantial oil royalties to help sustain their national budgets, which include significant social benefits for their citizens, and likely need oil prices to rise to $60 or higher. Lastly, we think decline rates, a key barometer used to estimate a field's production life, will likely be higher than the 6% the market was estimating through the end of March 2009 because at lower oil prices, much of the discretionary investment needed to offset these declines does not make economic sense since the costs would likely exceed the returns on the investment.

On the demand side, we look at aggregate demand figures country by country, product by product. Economic activity is important on a short-term basis, but so are the secular trends within a country or region. While a prolonged global economic slowdown or even a depression could exacerbate the demand destruction that has occurred, many developing countries, particularly in Asia, have seen large increases in the demand for energy over the last decade. China has played a big part in the developing world's hunger for oil in recent years because of the industrialisation occurring there. As a result, we think demand for oil will resume its long-term uptrend once global economic activity normalises.

Renewable or alternative energy was a big topic of discussion as more traditional sources of energy had their historic rise. Despite the Obama administration's support for spending in this area, we think the world is still a number of years away from finding a more economical replacement for oil as any shift would require a great deal of infrastructure development. Even more traditional energy sources, like natural gas, would require a large investment in infrastructure and development before they could become a viable alternative to oil-based products used in automobiles. That is why we think there will be less of a negative impact on demand and thus on some of the traditional oil and gas players than the market thinks, which we believe creates an opportunity for us to purchase some strong companies at attractive valuations.

In Exhibit 9, we present additional factors that will impact the energy sector.

Exhibit 9

Issues Facing the Energy Sector

Negatives	Positives
Recession and slowing global growth	Reserves and valuations
Increased emphasis on alternative energy	Stimulus package – increased infrastructure spending
Access to capital	Industrialisation of emerging countries

Source: Janus

Positioning

The precipitous decline in energy prices has been a result of weakening demand, something that we have not seen for several years. In our view, this has provided much relief to what remains a supply-constrained market. We do not think the current situation is sustainable, however. Many companies we have evaluated were trading on proven reserves based on a sustained low price of oil and no growth prospects. It has been cheaper to buy oil already discovered than to go out and drill for it. Therefore, we like companies that would likely benefit the most from higher oil prices and where their stock prices do not fully give credit to the size of their potential reserves. In our opinion Exploration and production companies such as select US and Brazilian producers fall into this category.

Our research not only helps us get a feel for the possible direction of oil prices, but it also helps reveal the types of companies that could benefit the most. As a result of our findings, we have been led to some select U.K. oil-field machine and equipment makers and Swiss rig operators that specialise in niche markets like deep waters. We think these companies will benefit over the long term as the "easy-to-get" oil has already been exploited. We have been less interested in oil services and well maintenance companies that may be called to service these fields, largely because the sharp slowdown has hurt their order book and pricing. Long term, they have had difficulty adjusting overhead quickly to changing demand conditions.

Overall, we think the long-term uptrend in oil prices will resume, providing support for the sector.

Financials Sector

"We view this market to be a stock picker's market in which differentiated research based on fundamental analysis and grass-roots contacts can be more profitable."

Summary

The financial crisis that began in July 2007 has reshaped the financials sector. The crisis originated with the subprime mortgage market and the extensive use of leverage, and then ended in a global recession. Not surprisingly, the financials sector was the worst-performing group in 2008, falling about 53%, according to the MSCI World Index. It has continued that pace through March 2009, returning roughly -21% on a year-to-date basis. Exhibit 10 lists the industry groups in this business sector.

Outlook

Several industries within the financials sector underwent major changes as a result of the credit crisis. Perhaps the largest impact has been on US and European investment banks and government-sponsored entities in the United States, two of the most significantly leveraged areas within the sector. As a result of the credit crisis, large investment banks have gone bankrupt, been acquired or been converted to bank holdings companies while deleveraging their balance sheets. Meanwhile, GSEs like Fannie Mae and Freddie Mac were under US government control at period end. Some banks in the United Kingdom and Ireland were also taken over by their respective governments.

Government participation has increased across the financial services sector. Aside from taking control of the GSEs, the US government invested directly in private institutions such as Citigroup and American International Group (AIG). In most cases, the government's terms were dilutive to equity holders. Uncertainty about which bank was going to survive and which bank would need capital remained a problem for the sector through the end of March. We believe one of the challenges facing the sector is the restoration of confidence that banks have adequate capital. As a result,

Exhibit 10

Sub-Industry Classifications of the Financials Sector

Asset Management & Custody Bank	Office REITs
Consumer Finance	Other Diversified Financial Services
Diversified Banks	Property & Casualty Insurance
Diversified Capital Markets	REITs
Diversified Real Estate Investment Trusts	Real Estate Management & Development
Industrial REITs	Regional Banks
Insurance Brokers	Reinsurance
Investment Banking & Brokerage	Residential REITs
Life & Health Insurance	Retail REITs
Mortgage REITs	Specialised Finance
Multi-Line Insurance	Specialised REITs
Multi-Sector Holdings	Thrifts & Mortgage Finance

Source: Janus

Exhibit 11
Issues Facing the Financials Sector

Negatives	Positives
Rising costs and lower profitability	Unprecedented government efforts worldwide to support the global financial system
Continued weakness in housing	Potential for more government stimulus, particularly in housing
Credit cycle that is highly correlated with the economy and employment, both of which have been worsening	30-year mortgage rates in the United States near 40-year lows
Continued pressure on capital and financials balance sheets and the deleveraging process limiting lending activity	Potential slowing or even an end to the massive deleveraging taking place
Increased regulation, particularly in the United States	Valuations in many cases

Source: Janus

we think the current environment warrants continued focus on the quality of balance sheets and overall capital requirements. We are favoring financials that we believe are well-capitalised.

Part of the balance sheet analysis depends on asset markets. Institutions are hurt by mark-to-market accounting in illiquid markets. Reforms may go a long way toward restoring confidence in the US and global financial system. We believe the new US administration has indicated a clear direction toward increased regulation for the financial services sector overall. President Obama has been clear that he thinks one of the causes of the current crisis was the gradual deregulation of the sector over the last decade.

We have not only focused on balance sheet analysis in identifying quality investment opportunities, but we have also dedicated much of our bottom-up research efforts to assessing trends in loan activity. We use a vast group of contacts, including those within government and throughout the private sector, in addition to talking with competitors and customers. For instance, we speak with bank loan officers to try to determine the availability of loans. Our data so far suggest banks are reluctant to approve new loans and that the overall mood remains weak. We are looking for signs of loan growth and normalisation of credit markets.

Lastly, we would like to see housing stabilise. It is critically important to the economy overall, in our view. Ultimately, renewed economic activity drives the success of the banks that survive or even thrive beyond the crisis. In our opinion it is critical that the major government programs target the housing market and loan growth.

A number of risks and opportunities exist within the beaten-down financials sectors. Exhibit 11 summarises some of the more pertinent issues.

Positioning

Despite the risks and challenges, we expect some areas will benefit when the environment normalises, whether in the next several months or years, and this is where we are actively seeking investment opportunities. Well-capitalised banks that can take market share both organically and through acquisitions are also attractive to us. We believe financials that don't rely on leverage, such as asset managers and exchange operators, remain appealing in this environment. A third area is in insurers. We were starting to see some early signs of firmer pricing among property and casualty insurers, which is generally a good time to invest in that group. We also like companies we think could benefit from disruptions within the industry. AIG's struggles and uncertainty surrounding its future could give other insurance companies a chance to win customers and take market share.

Bottom line, we are not only favouring companies we believe are appropriately capitalised, but companies that also have a record of good risk management and are likely to benefit as we emerge from the recession. We believe the opportunities are significant, and the value of fundamental research is as important now as it has ever been.

Healthcare Sector

"When you have a company that's really addressing an unmet medical need with a product that has no alternatives, that's the kind of company we think can still thrive – even in a very difficult economic and political environment."

Summary

The healthcare sector may have been one of the better-performing sectors during the recent bear market, but its 21% decline within the MSCI World Index in 2008 was of little consolation. The Obama administration's new budget proposal, which could fundamentally change the US healthcare sector, has also hurt the group through March 2009 as the sector has fallen nearly 10%. Prior to 2008, the sector had underperformed the broader market for five years, which gives us confidence that the sector's relative underperformance could reverse. The significantly lower valuations with which it began the period and the challenges facing the rest of the economy could make this group more attractive, despite the uncertainty associated with the new administration's potential to enact major changes. Our definition of the sector's makeup is summarised in Exhibit 12.

Exhibit 12
Sub-Industry Classifications of the Healthcare Sector

Biotechnology	Healthcare Supplies
Drug Retail	Healthcare Technology
Healthcare Equipment	Life Sciences Tools & Services
Healthcare Facilities	Managed Healthcare
Healthcare Services	Pharmaceuticals
Healthcare Distributors	

Source: Janus

Outlook

We believe the long-term drivers of healthcare spending remain intact, including aging populations, rising life expectancies (driven by the adoption of medical technology) and higher standards of living globally. We think all of these factors should continue to support higher healthcare spending than gross domestic product growth in most of the world's economies.

While we believe the long-term prospects remain favourable, the short-term outlook for the healthcare sector is clouded by two key factors: the economy and healthcare reform. Although healthcare has long been considered "defensive," we do not think the sector will be immune to economic forces, given increasing patient share of costs and the rising number of workers who could lose their medical insurance from layoffs. Select areas within healthcare (for example, capital equipment for hospitals) could also be negatively impacted by the ongoing credit crunch.

The Obama administration's proposals for healthcare reform have weighed on the sector since they were announced in late February. However, while the debate in Washington over the coming months could lead to increased volatility and headline risk, in our view the administration's proposals so far look manageable for most healthcare companies. The largest impact might be felt in the US managed care sector, where a proposed change in the Medicare Advantage program, which is a health maintenance organisation for seniors, could negatively impact the largest providers in that marketplace. We believe these concerns are priced into many managed care stocks, which were trading below historic trough multiples as March came to an end.

The pharmaceutical industry should be less impacted by the changes proposed by the Obama administration. The biggest effect in our view comes from an increase in rebates in the US Medicaid program, which should have a relatively modest impact on revenues of most companies. Questions remain about whether the US Medicare Part D program (the pharmaceutical plan for seniors) will be changed, but this program has been functioning quite well (coming in below cost and with high customer satisfaction in the 85% to 90%+ range), which suggests to us that there is little reason or political pressure to change it.

Pharmaceutical companies were also proactively addressing the challenging environment through increased merger and acquisition activity, which should allow for substantial cost savings and reduce excess industry capacity going forward. Near-term challenges have created attractive valuations in pharmaceuticals. Select pharmaceutical companies that we think have strong balance sheets and generate significant cash flow are trading at significant free-cash-flow yields. These companies are still growing and buying back stock, but their stock prices were trading at low historical multiples through March, which implied considerable pricing of potentially bad news.

For biotechnology companies, a key concern is the prospect of generic biologic drugs, or so called "biosimilars." We think US legislation on biosimilars has a good chance of passing this year or next, but the impact will not be felt for years (because of high regulatory hurdles), and competition will ultimately be much more limited than for standard pharmaceuticals in our opinion. For example, biosimilars currently available in Europe represented only a small share of the market through the end of March because of ongoing safety concerns.

In addition to monitoring political and regulatory events, we have spent a significant amount of time on the road attending medical conferences, meeting with doctors, talking to industry consultants and conducting surveys of potential customers to assess possible scenarios for the companies we follow. We have also maintained an in-house database to cross-check prescription trends with current pricing data to gain insights into which generic drugs are taking market share and to increase our understanding of falling demand versus distribution changes. For example, earlier this year we were able to determine from our internal calculations based on the database that a select biotechnology company's decline in sales for a particular drug was actually an indication of the distributors working down inventory rather than an actual reduction in demand for the drug. This revelation increased our conviction in the holding.

Lastly, the medical technology industry should be less impacted by the changes proposed by the current US administration. A key concern is whether reimbursement to hospitals will ultimately be changed in such a way as to drive down prices for medical devices. So far, these concerns appear to be theoretical in our view, and may be captured in valuations, which were approaching historical troughs through the end of March.

Positioning

We seek a balanced approach with exposure across the different subsectors within healthcare and across geographies and market capitalisations. This includes biotechnology companies, pharmaceuticals, medical device makers and healthcare services firms. In terms of current strategy, we remain focused on companies that are addressing unmet medical needs (such as cancer and AIDS) where there are few or no alternative treatment options. We think these companies can do well even in a difficult economic environment.

Companies that can control costs and help others control costs are compelling opportunities to us. This includes generic drug makers and pharmacy benefit management firms, which actually earn higher profits when they save money for the healthcare system by using lower cost generics and private label products. We believe political uncertainty and five years of underperformance during the global economic boom have created many attractive valuations within the healthcare sector. We seek to use our proprietary research to identify high-quality or improving businesses within the sector that are trading at a significant discount to our estimate of intrinsic value.

Exhibit 13
Issues Facing the Healthcare Sector

Negatives	Positives
Political uncertainty	Aging population and rising life expectancies worldwide
Rising unemployment and uninsured	Rising income and standard of living worldwide

Source: Janus

We are less constructive on hospitals, which could be vulnerable to declining utilisation rates, Medicaid funding cuts in the United States, reduced support from endowments (due to investment performance) and the likelihood for rising bad debts. Consequently, hospitals will likely cut spending, which could impact medical equipment makers and suppliers, although medical devices generally fall low on the spectrum of cost-savings opportunities in the eyes of hospital administrators. We believe the weak performance of many medical device makers since the beginning of the year has made valuations relatively attractive in this area and that there will not likely be much pressure on these names from healthcare reform. We favour medical equipment makers and suppliers that generate a larger portion of revenues and cash flows from recurring services and supplies versus those with revenues that are largely driven by new sales. We are also mindful of those life science companies that could be negatively impacted by the credit environment, as small- and medium-size biotechnology laboratories struggle with funding shortfalls. Finally, we are assessing the impact a strengthening dollar can have on overseas earnings of US-based companies in medical technology and pharmaceuticals.

Industrials Sector

"One of the things we at Janus really pride ourselves on is finding names and opportunities that we believe will do well once the market rebounds. Once the market finally does stabilise, the intrinsic value of the companies we own could be realised in a way that has significant upside."

Summary

The recession that became evident during the latter months of 2008 took a significant toll on the industrials sector, which was the second worst performing behind financials for the year, losing more than 45%, according to the MSCI World Index. Information gathered through March suggests that trend has continued into 2009 as the typically cyclical industrials sector has fallen nearly 12%. While we think earnings estimates for 2009 could be too optimistic, valuations for industrials through the end of March 2009 were below previous trough levels, suggesting the market was pricing in the worst recession in 30 years. Prices may fall even further as a result of potential earnings disappointments, which we think could add to the volatility within the sector over the near term. Exhibit 14 summarises how we view the industrials sector.

Outlook

One area that we are paying close attention to is higher financing costs, which have raised the "hurdle rate," or required rate of return that makes a new project worth pursuing. Other areas are US residential and non-residential construction spending levels, and public policy and investor perceptions regarding defense spending. Overall, capex budgets were being slashed, providing a negative backdrop for the sector.

Exhibit 14
Sub-Industry Classifications of the Industrials Sector

Aerospace & Defense	Diversified Metals & Mining	Industrial Machinery
Air Freight & Logistics	Electrical Components & Equipment	Marine
Airlines	Environmental & Facilities Services	Marine Ports & Services
Airport Services	Fertilizer & Agricultural Chemicals	Metal & Glass Containers
Aluminum	Forest Products	Motorcycle Manufacturers
Auto Parts & Equipment	Gold	Office Services & Supplies
Automobile Manufacturers	Heavy Electrical Equipment	Paper Packaging
Building Products	Highways & Rail Tracks	Paper Products
Commercial Printing	Home Furnishings	Precious Metals & Minerals
Commodity Chemicals	Homebuilding	Railroads
Construction Engineering	Household Appliances	Specialty Chemicals
Construction & Farm Machinery	Housewares & Specialties	Steel
Construction Materials	Human Resources & Employment Services	Tires & Rubber
Diversified Chemicals	Industrial Conglomerates	Trading Companies & Distributors
Diversified Commercial & Professional Services	Industrial Gases	Trucking

Source: Janus

Financing challenges have led to fewer projects being funded and reduced capital budgets. Within the industrials sector, companies like airlines are directly impacted since they are typically dependent upon outside financing to acquire airplanes. Other companies, such as component manufacturers, are hit more indirectly, as their customers are challenged to secure credit. In terms of capital spending cuts, the mining industry will likely suffer the greatest impact; we estimate reductions of 40% to 50% from the $90 billion spent industrywide in 2008.

Residential construction in the United States appears to be approaching a bottom in our view with housing starts at post-World War II lows (Exhibit 15), while Europe appears to be further from a bottom as evidenced by recent steep declines in housing permits in Spain, France and the U.K. We expect US non-residential construction, which impacts industries like steel producers among many others, to weaken significantly during 2009 based on falling manufacturing metrics, capacity utilisation rates and architectural billings. Our analysis suggests that a negative scenario could reduce spending in this sector by $150 billion from a peak of $400 billion as of January 2008. We expect project starts this year in the United States to account for about 500 million square feet of commercial space, about half of the annual average in the last 13 years. In 2010, construction activity could be lower still. Also, disconcertingly, REIT indices have been touching all-time lows. We believe Europe is being similarly impacted in non-residential construction, as indicated by declining cement consumption and truck production numbers, among other measures.

Exhibit 15

US Housing Starts

As of March 31, 2009
Source: Bloomberg, US Department of Commerce

US housing has been in a downturn for three years, so it may be one of the industries that could rebound sooner than later cycle groups, which are now starting to go through significant downturns with customers pulling orders or who are unable to secure credit to make orders.

We do not expect that the Obama administration will make many changes regarding defense spending over the short to medium term, given that it has been supportive of national defense and given the slowly evolving nature of defense and government spending in general. As a result, we think the US defense budget is relatively safe from cuts over the near term and that these stocks could still benefit. In addition, valuations were attractive to us through the end of March, despite the potential political uncertainty during the later years of President Obama's current term.

Exhibit 16 summarises the issues we believe will affect the industrials sector.

Exhibit 16
Issues Facing the Industrials Sector

Negatives	Positives
Slowing global growth and recession	Stimulus package – increased infrastructure spending
Weak commodity prices	Valuations at historically low levels
Weak housing market	
Access to capital	

Source: Janus

Positioning

While we focus our research on finding individual companies through a bottom-up approach, we cannot ignore the macroeconomic picture. Along with an evaluation of the macro environment and assessing the growth potential of companies relative to their current valuations, we pay special attention to management as well. We favour companies whose management teams understand what they can and cannot control in their business. A select plastics and glass packaging manufacturer falls into this category because its management has been aggressive in cutting costs and improving profitability without sacrificing growth. Flexible capital needs and strong businesses with competitive moats that do not require a lot of capital on a short-term basis are other traits we find appealing.

We cannot exactly pinpoint the bottom, but we have been moving into some early cycle names that we believe act as leading indicators and should outperform over the short term should signs of economic improvement become evident. In addition, we think there are companies that are likely to benefit from increased infrastructure spending, such as suppliers of construction aggregates (such as gravel, sand and stone) and cement makers. As part of our research, we made direct contacts with quarry owners to assess current pricing trends as well as to gauge the impact the stimulus package could have on it. Our findings increased our conviction in select names within this space. Conversely, our surveys of heavy equipment dealers and distributors helped us to avoid certain manufacturers that were facing significant downturns in their businesses.

One of our highest conviction names is a select conglomerate that generates 40% of revenues and 60% of profits from after-market services and spare parts. The company has a diversified business portfolio, what we think is a strong balance sheet, was trading at attractive value (as of the end of March) in our view and significantly raised its dividend recently.

The deep sell-off within the sector has been indiscriminate based on valuations that we think project little or negative growth long term for some companies. We believe this has created opportunities in many companies that fit our ideal profile, which includes strong franchises with predictable, recurring revenue streams (those with service components and/or long-lived, stable order flow) and high free-cash-flow yields trading at attractive valuations. This kind of profile helps give us conviction, even when we see sharp declines in a company's stock price.

Technology Sector

"Companies where we hear good things from the key players in the market are the kinds we get excited about buying and we're looking to own. "

Summary

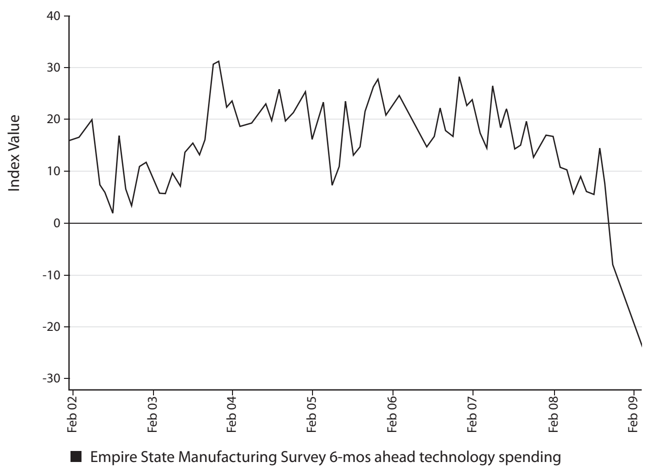
Historically, the technology sector has been impacted by business information technology spending and to a certain extent consumer activity. This sector has been hurt by the credit crisis and the subsequent global economic downturn. The sector, as represented by the MSCI World Index, declined nearly 44% in 2008, but has fared better through the end of March, posting a year-to-date fractional gain. The industry groups within this sector are summarised in Exhibit 17.

Outlook

The current environment has been challenging for investors. The credit crisis, a weak economy, high-risk aversion, and forced selling or liquidation by some in the investment community have weighed on the market and technology stocks worldwide. The credit crisis' impact on technology stocks has been both indirect (through a slowdown in spending and activity) and direct (through frozen capital markets). Many sectors, particularly financial services, have cut back their IT spending. Weak retailers, struggling industrial firms and energy companies with slowing businesses are also cutting back on IT spending. Companies are doing more with less in the corporate IT space, which has been a multi-year trend. We think this could continue, particularly with the weak economic environment (Exhibit 18). Overall, we expect a downshift in global growth in 2009 – one that will likely lead to a below-trend growth rate of the global economy.

Exhibit 18

IT Spending Trends in New York Federal Reserve District



As of March 31, 2009
Source: Bloomberg, Federal Reserve

Exhibit 17

Sub-Industry Classifications of the Technology Sector

Application Software	Home Entertainment Software
Communications Equipment	IT Consulting & Other Services
Computer Hardware	Networking Equipment
Computer Storage & Peripherals	Office Electronics
Consumer Electronics	Semiconductor Equipment
Data Processing & Outsourced Services	Semiconductors
Electronic Equipment Manufacturing	Systems Software
Electronic Manufacturing Services	Technology Distributors

Source: Janus

Exhibit 19

Issues Facing the Technology Sector

Negatives	Positives
Weak consumer and business IT spending	Stimulus package – increased spending on alternative energy
Access to capital	Valuations in some segments

Source: Janus

As the technology sector has matured, we have seen more companies use debt financing as part of their capital structures, whereas six or seven years ago the vast majority of "good" technology companies had no debt. We think this shift has made it more important for us to understand the characteristics of a company's debt in great detail. Frozen credit markets have added to the complexity of this analysis. For instance, little or no access to capital could mean important projects get put on hold or canceled, potentially hurting future growth.

We take a longer term focus in our investment approach, looking beyond the cyclical challenges currently facing the sector and immersing ourselves in what is going on secularly from both the industry participant's and customer's perspectives. Our in-depth research includes speaking with "people on the ground." For example, in the semiconductor space, we spend a lot of time interviewing application engineers, who are the ones evaluating and buying semiconductor products on a day-to-day basis. We are able to get a feel for which products these engineers are buying and why. Corporate IT, whether it is spending on software, hardware, storage or networking gear, is a big driver of performance within the sector. So, we also spend a lot of time speaking with chief technology officers and chief information officers at a number of companies across various industries, asking them which technology firms are gaining "mind" share and which are likely to gain "wallet" share a year from now. From there, we assess whether we think any market share gains are durable on a multi-year basis. If customers, competitors or suppliers tell us that a company is doing well, it becomes a more compelling investment, in our view.

Exhibit 19 summarises the key issues affecting the technology sector.

Positioning

In an environment where there is an economic headwind, we place more emphasis on companies that have high, defensible margins. We also look to areas where competition is less intense. Specifically, we are particularly interested in companies we believe are, or have historically been, able to maintain or increase their margins, even in a recession. This means we are focused on companies that we feel have a very strong product and competitive position with consistent sales execution and the potential to generate high returns on invested capital. In our opinion, some select computer product manufacturers fall into this category given the premium price they have historically been able to capture.

We are attracted to companies that develop and provide enterprise software as a service. These are typically young companies that deliver software to their customers via the Internet. The client does not run the software from its own servers; rather it accesses the software remotely with the provider "hosting" the software. We think these companies have good multi-year growth prospects because they deliver a high return on investment to their customers. Select human resource management and public relations management companies are examples that fit into this category.

Mobile and handheld technology developers in the United States and Canada are appealing to us. In particular, we think the smart phone segment of the market will grow at a much faster pace than the overall handset industry over the next few years, though overall handset growth could slow. Smart phones allow users to not only make phone calls, but also browse the Internet and manage their data (such as their calendar, contacts, files and so on). Given this fundamental view, we attempt to find investment ideas we think will benefit from this growth, in addition to select device makers themselves. We have been attracted to some infrastructure providers that we think could benefit from an increased amount of data flowing over their wireless networks as a result of the growth in smart phone usage.

Whether it is semiconductor stocks, alternative energy, or hardware and software makers, one thing that remains consistent in our approach is our obsession with understanding how things could change in a big way over the next few years, and which vendors and which companies could be the beneficiaries of that meaningful change. While we try to be cognisant of the macroeconomic picture, we feel that the way we add the most value is through anticipating meaningful fundamental change and investing in those technology companies on that basis.

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