Weekly investment news

17th July 2006

EAGLE STAR

Global Overview

Equity markets tumble

Global equity markets fell sharply on the week in the face of a wave of bad news, much of it geopolitical. The escalating tensions in the Middle East, a series of bombs on commuter trains in Mumbai and ongoing worries about North Korea and Iran drove prices lower and undermined sentiment.

Oil price hike

Oil prices spiked to new all-time highs of nearly $80 per barrel, driven by the rapidly deteriorating situation between Israel and Lebanon, leading to fears that major oil-producing nations such as Iran could become involved. Other commodity prices also rose.

US results season

The second-quarter earnings reporting season got off to an uninspiring start with disappointing numbers from market heavyweights Alcoa and Lucent.

Japanese interest rates

The Bank of Japan raised its benchmark interest rate on Friday for the first time in six years, from 0% to 0.25%, in a move the Governor of the Bank of Japan described as "delightful".

Currency markets

The US dollar rose on the week, to finish at $1.2640 against the euro. It also rose against sterling and the yen. Gains were largely attributed to the repatriation of funds to the "safe haven" dollar, in the face of global uncertainty.

Market	Index	Year to Date Return 31.12.05 to 14.07.06		1 Week Return 07.07.06 to 14.07.06	
		Local Currency %	Euro %	Local Currency %	Euro %
US	S&P 500	-1.0	-7.3	-2.3	-0.9
US	NASDAQ	-7.6	-13.5	-4.4	-3.0
Europe	FT/S&P Europe Ex. U.K.	0.0	0.0	-3.2	-3.2
Ireland	ISEQ	-0.9	-0.9	-3.9	-3.9
UK	FTSE 100	1.6	1.6	-3.1	-2.5
Japan	Topix	-7.8	-12.5	-3.3	-3.9
Hong Kong	Hang Seng	8.5	1.2	-2.0	-0.7
Australia	S&P/ASX 200	4.3	0.2	-3.3	-1.7
Bonds	Merrill Lynch Euro over 5 year Govt.	-4.2	-4.2	0.7	0.7

Equities

USA

Overview

The US market fell in response to increasing worries about the situation in the Middle East and its effect on oil prices, together with a slightly shaky start to the results season.

Key Movers

Alcoa - The aluminium maker fell nearly 9% on the week, even after reporting record second-quarter earnings. The market took fright at lower-than-expected revenue figures.

Tech stocks – The NASDAQ Index under-performed the broader market, led lower by Lucent Technologies which forecast lower third-quarter earnings, and Microsoft, after it received a $280m fine from European regulators for failure to comply with a 2004 anti-trust finding.

General Motors – The car maker fell over 7% as the CEO said he remained open to a partnership between GM and Renault/Nissan, but played down the possibility of the Nissan CEO taking the helm at GM.

Europe

Overview

European markets did not escape the general malaise last week, falling across the board.

Key Movers

Bright spots – Volvo rose over 8% on the week as speculation mounted that a buyer was amassing the stock. Carrefour impressed with its second-quarter trading update and rose more than 1%. L'Oreal also bucked the trend, rising nearly 2%.

Alcatel – Shares in Lucent's French merger partner fell by nearly 11%, even though its preliminary quarterly figures were in line with expectations.

SAP – Second-quarter figures from the German software group disappointed the market, sending the stock down over 11% on the week.

Ireland

Abbey – The house builder fell nearly 10% on the week following the announcement of an earnings decline, reflecting margin pressure.

Grafton – DIY group Grafton issues a positive trading statement, with good news on deal flow and property disposals.

Asia Pacific

Technology – Tech stocks across the region were undermined by weakness in the sector in the US, where the earnings reporting season has started, with a couple of disappointing numbers from market leaders.

Hong Kong – Hong Kong suffered its biggest one-day percentage drop for a month on Thursday as investors grew nervous about the possibility of a Chinese rate rise.

Bonds

Government bonds made gains in the major markets as investors sought the relative safety of fixed interest investments. Japanese bonds also got a boost from the interest rate rise announced on Friday. In Europe, there were slightly softer inflation numbers in both Germany and France. The Merrill Lynch over 5 year index was up 0.7% on the week.

Global Outlook

- Growth expectations remain at high levels with global GDP forecast to expand by 3.7% in 2006, slightly above last year's figure of 3.6%. The major central banks are focused on cyclical inflation pressures and strong commodity prices.
- The Fed recently raised rates to 5.25%. The probabilities assigned to a further hike or a pause in rate moves have jumped around over the past few weeks, as markets try to gauge the impact of new economic data on the debate within the Fed. Currently, investors expect rates to peak close to 5.5% by year end.
- Despite moderate inflation in the eurozone, rising short rates and less than expected demand from pension funds have kept bond prices under pressure so far this year. The ECB raised rates as forecast to 2.75% recently and markets expect at least two more 0.25% hikes by year end, with a higher probability now given to three such rate hikes following recent ECB commentary.
- Equity markets still remain reasonably supported by a strong earnings' background and favourable valuations relative to bonds; high oil prices and tighter liquidity conditions from higher interest rates remain a concern and periods of volatility are likely. The gradual ending of super-easy money policies in Japan continues to deserve attention because of its potential negative impact on various asset classes.
- Currently, the funds are close to neutral in bonds and slightly overweight equities versus the manager average. Sectorwise, positions are currently pretty balanced as well. Geographically the funds remain underweight Ireland and more neutral in the other regions.

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