



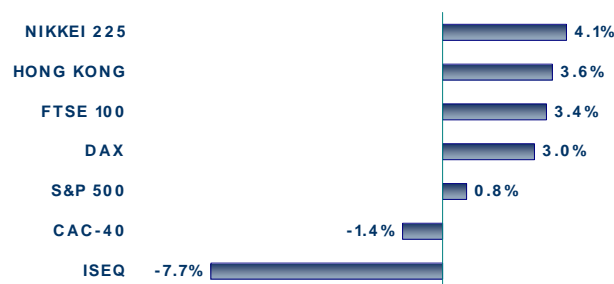
“At the end of a tumultuous year for equity investors, a ‘Santa Claus’ rally provided a positive finish to 2008. While it doesn’t dispel the memory of large negative returns in the year, it does suggest that the actions of policymakers are having some effect on sentiment.”

Leona Nicholson, Head of Irish Equities & Global Equity Product

Central banks slash interest rates...

- Stock markets generally enjoyed positive returns in December, although there were some notable exceptions (including Ireland) and the impact on the full-year outcome was relatively small. 2008 returns were among the worst ever – the US S&P 500 had its biggest loss since the 1930s.
- Financial markets were turbulent in the first half of December as rapidly deteriorating economic data spurred substantial official intervention. Central banks around the world slashed interest rates further, while government stimulus packages were increasingly evident.

Equity market returns – December 2008



Source: Bloomberg. Capital returns in local currency.

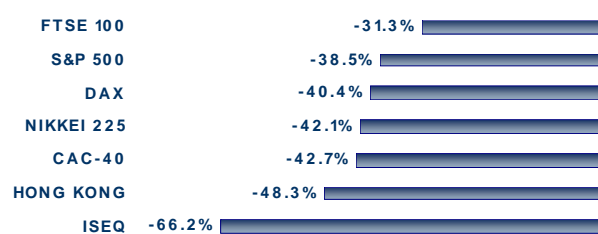
Irish equity return lags peers in December...

The Irish stock market shed a further 7.7% in December, to take its full-year loss to 66.2% – the biggest ever annual loss for the ISEQ Index. As was the case throughout the year, banks led the way down as investors remained on the sidelines while the issue of recapitalisation was ongoing in the background. The departure of Anglo Irish Bank’s Chairman and also its CEO over a director loan issue was swiftly followed by the Irish government announcement that it is to invest €5.5 billion in the three main banks, in return for high-yielding preference shares. This overshadowed strong gains by Aer Lingus as Ryanair launched a second bid for the airline and staff agreed to new terms and conditions. CRH also advanced on the potential of increased US infrastructure spending.

The S&P 500 Index gained 0.8%, even as a number of attempts to salvage the US auto industry made for volatile trading. A deal to lend the carmakers up to US\$17 billion in funding improved sentiment, as did President-elect Obama’s stated plans to spend up to US\$1 trillion on infrastructure projects and tax cuts. Earlier in the month, the Federal Reserve cut interest rates to a target-range of 0-0.25% – effectively as low as it could go. This offset some of the shock surrounding economic data detailing the biggest number of monthly US job losses since 1974, and the worst manufacturing index reading since 1982.

Signals from the Bank of England that it might follow the US towards near-zero interest rates, coupled with news that the UK government would increase the budget deficit to 8% of GDP, contributed to a sharp sell-off in the British pound. Sterling lost 16% against the euro and nearly 20% against the Swiss franc. The US dollar also weakened in response to its monetary and fiscal stimulus plans.

Deep losses for stock markets in 2008...



Source: Bloomberg. Capital returns in local currency.

Euro eyes parity with sterling...



Source: Bloomberg.

Bonds continue to reap gains...

The macro environment continued to be supportive of government bonds. Interest rates in all major and many developing markets were cut further in December as accelerating weakness in the economic outlook drove demand for fixed-interest instruments. The government guarantee element should not be overlooked as risk aversion among investors resulted in three-month US treasury bills yielding a negative return on a few occasions in December. The yield on a UK two-year gilt fell from 2.21% to 1.05% in December.

Bond markets in the US and UK outperformed Eurozone bonds in the month. Even though European Central Bank President Jean-Claude Trichet stated that the economy would contract by up to 1% in 2009, suggestions from the bank that it might pause the trend towards lower interest rates contributed to the relative underperformance.

A tacit acceptance by the US and UK central banks that they may purchase non-government debt and longer-dated sovereign issues also contributed to a sharp fall in their respective currencies.



10-year bond yields

	31-Dec-07	30-Nov-08	31-Dec-08
US	4.03	2.92	2.22
UK	4.51	3.77	3.02
Germany	4.31	3.26	2.95
Japan	1.51	1.40	1.17

Source: Bloomberg.

BIAM Outlook

- From an economic perspective, the immediate outlook is uninviting as data releases over the next few months are likely to detail contracting economic activity, rising unemployment and falling demand for goods and services. Indicative of the deepening nature of the downturn, the International Monetary Fund (IMF) predicted in November that the global economy would grow by 2.2% in 2009, just a month after forecasting growth of 3%.
- However, central banks have cut interest rates significantly, while governments around the world have been putting together stimulus packages in an attempt to prevent the recession from worsening further. The sharp fall in oil prices is also likely to act as a stimulus. Lower fuel costs should boost disposable income and reduce pressures on business margins. The combination of stimuli leads us to believe that the recession will not turn into a prolonged Japanese-style downturn.
- The spread between Libor rates and government borrowing costs narrowed towards the end of 2008. Whether this reflects increased readiness among banks to lend to one another remains to be seen, but if that is the case it should ultimately translate to lower corporate borrowing costs. Business sentiment has hit decades-low levels and a stabilisation of the forces that have ravaged earnings would be a positive.
- Equity market valuations are forward-looking and have acknowledged this recessionary environment for some time. The consensus view of market participants is that stocks are cheap, but a renewal of equity market volatility is possible given the pending weakness in corporate earnings in 2009.