Bank of Ireland
Asset Management

June 2009

Market Review & Outlook

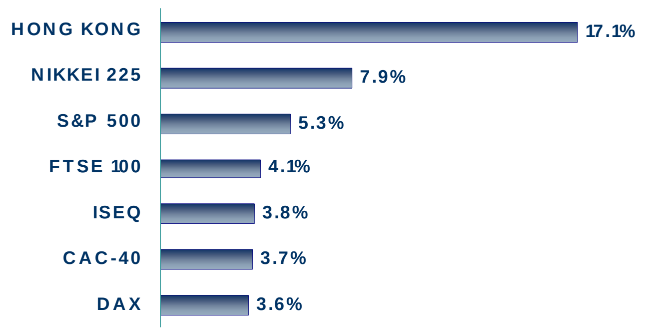
Global stock markets maintained the momentum that has gathered since early March, as investor sentiment was bolstered by increasing evidence that the macro-economic backdrop may be past the worst. The improving outlook for China and other emerging markets underpinned the significant pick-up in commodity prices in May. Although global demand remains relatively weak, crude oil rose by nearly 30% to over US$65 per barrel amid expectations that the turn in the economic cycle will drive future demand. Metal commodities also advanced, arousing inflation concerns, which in turn took the gold price higher and contributed to bond market weakness.

Unsurprisingly perhaps, the chief beneficiaries of improving economic confidence indicators in the past month have been the producers of commodities (energy and mining stocks) and providers of finance (bank stocks). Developing economies' stock markets also surged on the wave of optimism, with Hong Kong's market gaining 17% while India's Sensex Index leapt 28.3% following an election outcome that favoured continued economic reform.

BIAM Strategy and Outlook

- While economic data in the US signal a possible stabilisation at weak levels, the upturn in leading indicators, such as factory orders and confidence measures, has become more pronounced in recent weeks. Leading indicators have also improved in Europe, with the IFO survey pointing to an improved outlook among German businesses, a pattern that is emerging in a number of European purchasing manager indices. In the UK, retail sales expectations have shown some improvement, while mortgage approvals are not declining at the same sharp pace seen just a few months ago.
- There is mounting evidence to suggest that China has effectively decoupled from the 'developed' world economy and GDP is now expected to grow by 8% in 2009. While international trade has suffered, domestic demand appears strong (i.e. robust auto sales, supported by wage growth) and electricity output has rebounded from its recent plunge.
- The recent rally has brought the S&P 500 Index close to 'fair value' relative to its long-term history, according to one Price/Earnings measure. However, a number of other valuation metrics based on asset value multiples indicate that equities are still cheap, while the scale of recent moves are likely to have thrown up relative and absolute valuation opportunities. Markets have not priced in the potential for corporate earnings reverting to trend levels over the next 18 months, something that would be a positive surprise for stocks should this occur.
- US inflation expectations, as implied by the difference between nominal and real (inflation protected or index linked) yields, have risen sharply from particularly low levels and are now getting close to the 2% level. The recent sell off in bond markets is largely due to rising inflation concerns as opposed to a change in real yields. This normalisation is welcome, as yields had reached overextended levels on the downside and now give a fairer reflection of inflation and growth expectations. Overall, we are now modestly more bearish on the outlook for bonds.

Equity market returns - May 2009



Source: Bloomberg. Capital returns in local currency.

Movement in 10-year bond yields

	31-Dec-08	30-Apr-09	31-May-09
US	2.22%	3.12%	3.46%
UK	3.02%	3.50%	3.75%
Germany	2.95%	3.17%	3.58%
Japan	1.17%	1.43%	1.49%
Ireland	4.27%	5.20%	5.45%

Source: Bloomberg.