Bank of Ireland

Asset Management

January 2008

Month in Review

“Concerns about the US economy and worries of further bank losses put financial markets in turmoil in January and prompted the Fed to take radical action on interest rates – cutting the Feds funds rate from 4.25% to 3%.”

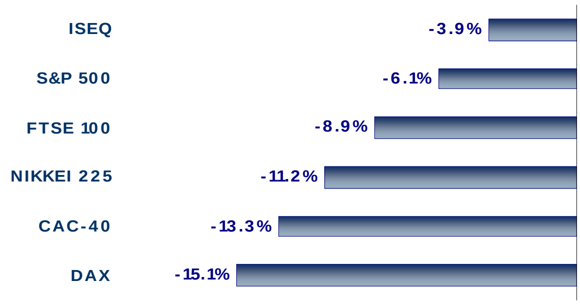
Desmond Lawrence, Senior Portfolio Specialist

Extreme volatility in financial markets…

- The first month of 2008 proved to be particularly turbulent as fears about the potential for a US recession grew. This was further exacerbated by news that a ’rogue’ trader had lost $4.9bn at Société Générale following a series of wrong-way bets on market indices.

- The Federal Reserve (Fed) aggressively reduced interest rates to allay recession fears, reducing the Federal funds rate to 3% from 4.25% in the space of eight days. The US government also moved to provide $150bn of fiscal stimulus to the economy. The Bank of England disappointed markets in leaving interest rates unchanged even as the domestic economic backdrop deteriorated.

Equity market returns - January 2008



Source: Bloomberg. Capital returns in local currency.

Ireland’s stock market outperforms…

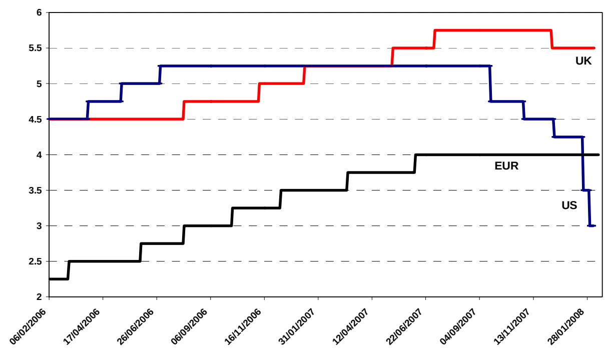
Equity markets experienced significant losses in January as investors reassessed earnings potential in light of a US slowdown. Economic data revealed that the credit crisis was affecting the wider US economy—Wall Street woes spreading to Main Street. Housing data missed already-negative expectations and the labour market showed signs of stress, after remaining largely robust to date.

A key influence on market weakness was the decision of ratings agencies to put monoline insurers (bond insurers) on watch for possible downgrades. Losing AAA ratings would result in the downgrade of many bonds that they insure, potentially forcing another round of bond-related losses for the banking industry.

European markets were weak against this backdrop as the new interest rate differential with the US prompted further euro strengthening. Events at SocGen also rattled investor confidence.

The ISEQ was a strong relative performer, recording superior (if still negative) returns to other European indices. This followed a poor 2007, and building-related stocks were remarkably robust performers in January. Irish banks also outperformed their international peers in the month.

US interest rates now below Eurozone...



Source: Bloomberg.

Continued overleaf

Bank of Ireland
Asset Management

High demand for the relative safety of bonds…

Bond prices rose throughout January as investors rushed into fixed interest assets to escape the turbulence of equity markets. Moves were most marked in the US following the sharp reduction in interest rates. Despite the mantra of the European Central Bank that inflationary pressures could result in a rate hike, bond yields tracked lower.

Inflation worries were a feature throughout January and concerns were voiced about the inflationary implications of such aggressive interest rate cuts by the Fed. The overall US inflation rate has shot up from 2% in August to stand at 4.1% in the latest release.

10-year bond yields

	31-Jan-07	31-Dec-07	31-Jan-08
US	4.81	4.03	3.60
UK	4.98	4.51	4.48
Germany	4.10	4.31	3.93
Japan	1.71	1.51	1.44

Source: Bloomberg.

Looking into the months ahead…

- The consensus is that the United States is now probably in a recession. In our view, this downturn will be neither deep nor prolonged, but there is a risk of continued high volatility on equity markets in the near-term. Although the European Central Bank has dismissed calls for lower interest rates, we expect that due to weakening market conditions interest rate cuts will likely happen later in the year. The Fed is likely to continue cutting rates while the Bank of England will also cut further, probably as early as its February meeting.

- The extreme dislocation in equity valuations during January threw up some compelling investment opportunities and we will continue to seek out and take advantage of such opportunities as they arise. Valuations still appear to be low on any long-term perspective and any action we take will be measured, particularly against a likely background of high volatility.