

## Group Pension Managed Funds Update to 31<sup>st</sup> July 2006

### Summary

Following on from a disappointing second quarter performance, pension funds experienced small but positive returns during July. On average, pension managed funds rose by 0.8% over the month, with returns ranging from a low of 0.4% (Hibernian and KBC) to a high of 1.3% (Setanta and Standard Life). Over the first seven months of the year, pension funds have returned a modest 1.8%. Over the past twelve months, the average fund return was a healthier 10.2%. Over the three years to 31 July 2006 the average fund return has been strong, at 13.2% per annum. In the five-year period ended 31 July pension managed funds have, on average, returned a less robust 3.9% p.a., reflecting the equity bear market of the early 21<sup>st</sup> century. In contrast, however, the ten year period to the end of July saw an average return of 9.6% per annum. When considering these returns it is important to remember that the investment horizon of most pension schemes is generally over 25 years, and that equities have historically provided significantly higher returns over the long term than bonds, property or cash, although at the cost of greater volatility.

### Market Review

Geopolitical events dominated markets during July. Hostilities between Israel and Lebanon, concerns over the nuclear ambitions of North Korea and Iran, and terrorist attacks in India created a feeling of unease in financial markets. Oil prices rose to historic levels before falling back somewhat towards month end, while commodities also performed strongly. The US dollar strengthened slightly as investors moved into this “safe-haven” currency. Interest rates remained unchanged in Europe and the US, although the Bank of Japan raised rates for the first time in 6 years.

Irish equities were virtually flat during July. Financial stocks underperformed the rest of the market, declining 1.4% amid concerns over rising interest rates in the Eurozone. C&C was a very strong performer. The good weather saw a boost to sales of their Bulmers Cider (Magners in the UK), while the company announced the sale of the Tayto crisp brand for a good price. Ryanair received a boost after months of difficulties due to rising oil prices, with a 23% increase in passenger numbers. Despite rallying strongly towards month end following the successful re-launch of its MS drug Tysabri in the US and Europe, Elan had a poor month overall.

The FT UK index gained 1.5% in sterling terms over the month, rising to 2.7% for Irish investors as sterling strengthened against the euro. The market was supported by oil stocks, which make up 20% of the index, as oil prices reached new record highs. Strong demand for petrol (particularly in the US), escalating conflicts in the Middle East, and concerns over missile tests in North Korea, were the main drivers behind the high oil price. There were two significant IPOs during July. Standard Life listed on the stock exchange, valued at £4.65 billion, while Russian oil company Rosneft also came to market. Merger and acquisition activity continued to make headlines. Insurance company Aviva announced it was in talks to buy US insurer AmerUS. Bid speculation surrounded homes builder McCarthy & Stone, and steelmaker Corus. Boots Chemists completed a £7 billion merger with Alliance Unichem.

US equities gained 0.6% in dollar terms, rising to 0.7% for Irish investors as the dollar gained some ground against the euro over the month. Economic data showed that the US economy is slowing and fewer new jobs are being created, while wages and inflation are rising. Tobacco stocks received a boost after a Florida court overturned an award of \$145bn against them for punitive damages. As elsewhere, oil stocks were strong, supported by rising crude prices and merger speculation in the sector. Microsoft were fined \$280m by European regulators, after they failed to comply with a 2004 anti-trust ruling. Comments from Federal Reserve Chairman Ben Bernanke were interpreted as signalling an imminent end to interest rate increases, and were welcomed by investors. The second quarter earnings season got off to a positive start, although some technology stocks disappointed.

European equity markets were among the strongest performing bourses during July, with the Eurozone region rising 1.2% and the rest of Europe returning a healthy 2.4% over the month. Energy stocks fared well due to the rising oil price. Airline stocks received a boost due to higher passenger numbers. Meanwhile, in the aerospace industry, EADS and Finmeccanica were out of favour due to their association with the troubled aircraft builder Airbus. Car manufacturer Volvo gained on the back of strong earnings and rumours of a takeover. Other auto stocks also reported good results, with the exception of Peugeot which delivered its third profit warning in twelve months. Although the European Central Bank kept interest rates on hold in July, a 0.25% hike in August has been priced into the market.

Last year's star performer Japan has struggled in 2006, and this trend continued into July. The FT Japan index fell 0.4% over the month, bringing the return for the first seven months of the year to -1.6%. Japan is the only major market to be in the red in local currency terms for the year to date. The Bank of Japan raised interest rates for the first time in six years, from 0% to 0.25%. The Tankan survey of business sentiment released at the beginning of the month surprised on the upside; however rising oil prices and missile tests in North Korea created unease among investors. Above expectation earnings announcements from a number of electronics exporters provided the market with a boost towards month end.

Pacific Basin equity markets also declined 0.4% over the month. As with Japan, rising oil prices and missile tests in North Korea created instability in the markets of the region. Rising inflation in Australia has led to increased expectations of an interest rate rise in the near future. Hong Kong was the best performing bourse in the region, as investors reacted positively to the imminent end of interest rate hikes in the US.

Bond yields fell approximately 0.1% over the month, which is not good news for pension funds. The method used to calculate pension fund liabilities means that lower bond yields result in a higher valuation being placed on these liabilities.

## Tables

### 1. Group Pension Managed Fund Returns to 31<sup>st</sup> July 2006

	<b>1 Month</b>	<b>7 Months</b>	<b>1 Year</b>	<b>3 Years</b>	<b>5 Years</b>	<b>10 Years</b>
	<b>%</b>	<b>%</b>	<b>%</b>	<b>% p.a.</b>	<b>% p.a.</b>	<b>% p.a.</b>
AIB Investment Managers	1.0%	2.3%	11.4%	13.3%	2.5%	8.4%
Bank of Ireland Asset Management	0.7%	-0.2%	5.8%	11.2%	4.4%	10.0%
Canada Life/Setanta	1.3%	1.8%	8.9%	13.1%	3.4%	8.5%
Eagle Star	1.0%	2.6%	11.5%	14.3%	5.3%	10.1%
Friends First/F&C	0.6%	1.5%	10.5%	12.9%	4.1%	9.7%
Hibernian Investment Managers	0.4%	3.0%	11.5%	13.4%	4.2%	9.9%
Irish Life Investment Managers	0.6%	1.1%	9.9%	14.3%	4.6%	9.8%
KBC Asset Management	0.4%	1.7%	10.4%	12.1%	1.7%	8.6%
Oppenheim Investment Managers	0.9%	2.3%	10.3%	13.0%	4.3%	12.4%
Standard Life Investments	1.3%	1.9%	12.1%	14.2%	4.1%	8.6%
<b>Average</b>	<b>0.8%</b>	<b>1.8%</b>	<b>10.2%</b>	<b>13.2%</b>	<b>3.9%</b>	<b>9.6%</b>

### 2. Equity Market Index Returns to 31<sup>st</sup> July 2006

<b>Region</b>	<b>1 Month</b>		<b>7 Months</b>	
	<b>Local Ccy</b>	<b>Euro</b>	<b>Local Ccy</b>	<b>Euro</b>
Ireland	-0.1%	-0.1%	3.4%	3.4%
UK	1.5%	2.7%	7.6%	8.1%
North America	0.6%	0.7%	3.4%	-4.3%
Eurozone	1.2%	1.2%	7.8%	7.8%
Rest of Europe	2.4%	2.2%	5.6%	5.5%
Japan	-0.4%	-0.3%	-1.6%	-6.2%
Pacific Basin	-0.4%	0.6%	4.6%	-0.3%