

## Group Pension Managed Funds Update to 30<sup>th</sup> September 2006

### Summary

During the third quarter of 2006, pension funds recovered all of the losses incurred during the second quarter, rising 5.4% on average. This brings the average return for the first nine months of the year to 6.5%. Over the past twelve months, the average fund return was a healthy 11.7%. Over the three years to 30 September 2006 the average fund return has been strong, at 14.8% per annum. In the five-year period ended 30 September pension managed funds have, on average, returned a less robust 7.3% 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 September saw an average return of 9.4% 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

Equity markets got off to a poor start in September, due to concerns over the extent of the slowdown in the US economy and fears that this might precipitate further interest rate hikes by the US Federal Reserve. However, as the month progressed, falling oil prices and benign inflation data allayed these worries. Oil prices have fallen over 20% since reaching record highs in early August. Commodity prices also fell back during September. Emerging markets were affected by political instability, but were buoyed by the less negative outlook for the US economy.

Irish equities rose by 2.4% during September, as the ISEQ closed above 8,200 for the first time. This brings the return on domestic equities to 9.9% for the third quarter of 2006, and 13.7% for the first nine months of the year. The Irish economy remains buoyant, with consumer spending up 7%. For the first time ever, the number of people employed breached the 2 million mark, while second quarter GDP grew by 5%. Despite a raft of positive results and changing interest rate expectations, Irish financial shares slightly underperformed the broader market. Technology stocks on the other hand significantly outperformed, rising 3.9% over the month. Lower oil prices boosted Ryanair's share price by 12.5%, while Aer Lingus was floated at the lower end of the expected price range and quickly rose over 12%. The continued success of the Magners brand in the UK helped C&C to gain almost 23% in September.

UK equities were one of the worst performing markets during September, returning just 1.2% in sterling terms and 0.4% in euros. The UK equity market is heavily exposed to oil and mining stocks, and therefore struggled against a backdrop of falling oil and commodity prices over the month. On the plus side, retailers delivered surprisingly strong earnings and takeover rumours boosted estate agents and some life insurers.

Despite a bumpy start to the month, US equities recovered somewhat to deliver a return of 2.3% in dollar terms during September. A strengthening dollar increased this to 3.4% for Irish investors. An unexpectedly large rise in labour costs created uncertainty about the outlook for US interest rates, as investors worried about the inflationary impact of such costs. However, a substantial drop in the price of oil, combined with a slowdown in the housing market, set minds at ease. Indeed, following the Federal Reserves' decision to keep interest rates on hold, sentiment swung in the opposite direction with concerns raised that the economy would slow too quickly. By month end the consensus view was that the economy was in for a soft landing, and markets rallied. Technology stocks outperformed the market overall, rising just under 4% in dollar terms. Intel benefited from the dismissal of a challenge from Adobe, Microsoft jumped on news that its new MP3 player should be released before Christmas, Apple rose amid rumours of a film download service and Ebay was seen as a takeover target. Tobacco stocks received a setback on foot of a ruling regarding low-tar cigarettes.

European markets delivered the strongest performances over the month. Corporate activity dominated investor sentiment, as a number of well-known companies engaged in merger and acquisition discussions. Telecom Italia's parent company was rumoured to have been approached by News Corp, Bank of America was said to be looking to takeover ABN AMRO, German chipmaker Infineon received and rejected a bid from private equity groups, Dutch retailer Ahold was the subject of reports linking it to a merger with Belgian counterpart Delhaize, while Spanish power generator Endesa was the target of a bidding war. Merck unexpectedly announced that it was buying Swiss biotechnology company Sereno for €10.6bn, creating the seventh largest drugs group in Europe. German truckmaker MAN had a €9.6bn bid for Sweden's Scania rejected. Volkswagen, a major shareholder in Scania, apparently favour a three-way merger between the firms.

Having recovered slightly in August, Japanese equities resumed their downward slide in September. The market declined 1.1% in yen terms, bringing the return for the first nine months of the year down to a lacklustre 1.2%. Export stocks were out of favour, due to concerns over a potential fall in demand from the US. Sony announced that their long-awaited new console, the PS3, would be delayed, missing the lucrative Christmas season in several markets. Disappointing economic data also impacted on the equity market.

Equity markets in the Pacific Basin region experience mixed fortunes during September. The overall performance of the region was 2.2% in local currency terms. However, returns ranged from a low of 1.1% in Australia to a high of 4.8% in Taiwan. The Australian market is heavily weighted towards mining stocks, which fell in response to declining commodity responses. A slowdown in economic growth also dampened investor enthusiasm. Taiwan experienced a broad-based rally after a cool-down of political tensions. Meanwhile, technology stocks in particular benefited from optimism in the export sector and hopes of strong demand in the lead up to Christmas.

Pension schemes received some bad news, however, as Eurozone bond yields fell in the wake of lower inflation expectations. As these yields are used to value pension scheme liabilities, lower bond yields will result in higher values being placed on schemes' liabilities.

## Tables

### 1. Group Pension Managed Fund Returns to 30<sup>th</sup> September 2006

	<b>1 Month %</b>	<b>3 Months %</b>	<b>9 Months %</b>	<b>1 Year %</b>	<b>3 Years % p.a.</b>	<b>5 Years % p.a.</b>	<b>10 Years % p.a.</b>
AIB Investment Managers	1.8%	5.9%	7.3%	12.8%	14.9%	6.0%	8.4%
Bank of Ireland Asset Management	1.3%	5.2%	4.3%	9.1%	12.6%	7.6%	9.7%
Canada Life/Setanta	1.5%	4.9%	5.5%	8.7%	14.3%	7.0%	8.2%
Eagle Star	1.9%	5.6%	7.2%	12.3%	16.0%	8.5%	9.9%
Friends First/F&C	2.1%	5.5%	6.5%	12.4%	14.8%	7.6%	9.4%
Hibernian Investment Managers	1.9%	5.0%	7.7%	13.2%	15.1%	7.6%	9.8%
Irish Life Investment Managers	1.8%	5.4%	5.9%	11.5%	15.8%	8.2%	9.6%
KBC Asset Management	2.0%	5.7%	7.1%	13.3%	14.1%	5.6%	8.5%
Oppenheim Investment Managers	1.2%	4.6%	6.1%	10.2%	14.3%	7.1%	12.1%
Standard Life Investments	1.9%	6.5%	7.1%	13.6%	15.8%	7.9%	8.4%
<b>Average</b>	<b>1.8%</b>	<b>5.4%</b>	<b>6.5%</b>	<b>11.7%</b>	<b>14.8%</b>	<b>7.3%</b>	<b>9.4%</b>

### 2. Equity Market Index Returns to 30<sup>th</sup> September 2006

Region	1 Month		3 Months		9 Months	
	<i>Local Ccy</i>	<i>Euro</i>	<i>Local Ccy</i>	<i>Euro</i>	<i>Local Ccy</i>	<i>Euro</i>
Ireland	2.4%	2.4%	9.9%	9.9%	13.7%	13.7%
UK	1.2%	0.4%	3.2%	5.2%	9.3%	10.7%
North America	2.3%	3.4%	5.3%	6.3%	8.3%	1.1%
Eurozone	2.7%	2.7%	7.7%	7.7%	14.7%	14.7%
Rest of Europe	3.3%	2.7%	9.1%	7.7%	12.6%	11.1%
Japan	-1.1%	-0.7%	2.4%	0.1%	1.2%	-5.8%
Pacific Basin	2.2%	2.6%	5.2%	6.1%	10.6%	5.2%