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Bank of Ireland: Half year results

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Market Movers

IRISH PAPERS TODAY

Total State funding provided to Anglo now poised to top €24bn (*The Irish Times*)

Pretax loss of €341m for NIB after impairment charges (*The Irish Times*)

Billions more "will go into Anglo black hole" (*Irish Independent*)

INTERNATIONAL PAPERS TODAY

Fed downgrades outlook (*Financial Times*)

BP oil spill lawsuits to be heard in New Orleans (*Financial Times*)

Fed takes gloomier growth view (*Wall Street Journal*)

Market View

Analyst: Stephen Taylor

European equity markets have opened lower this morning following declines in the US and Asia overnight. The Federal Reserve's more negative outlook on the US economy is pressuring markets with the resumption of its quantitative easing program only slightly negating the cautious assessment of the economy. The Fed acknowledged in its statement that 'the pace of economic recovery is likely to be more modest in the near term than had been anticipated'. While the outlook is cautious it does not indicate that officials are overly worried about the potential for a double dip recession. However as a result of its concerns the Fed has decided to start reinvesting the proceeds from its maturing agency and mortgage-backed securities (MBS) holdings into Treasury securities. While the move is not aggressive, it sends a clear signal that the Fed is ready to act if required to do so. According to Capital Economics, this may amount to \$150b a year, which will have little impact on the Fed's balance sheet, which currently stands at \$2.3trn. We take it as a positive that the Fed is ready to act when required and take a more proactive approach to the crisis than its European counterparts. That being said we are clearly entering a lower growth phase than had been anticipated, however given the solid position that corporates are in both financially and operationally we maintain our positive outlook for equity markets. As for today the main focus will be in the UK with the Bank of England's inflation report due for release, while unemployment data will also be closely watched.

BoI: Buy **Previous Close** €0.85 **Target** €1.20 **Analyst** Oliver Gilvarry

Bank of Ireland (BOI) reported first half results this morning with focus on impairment charges, declines in net interest income and operating profits. Non-NAMA impairment charges were €893m down 4% yoy, with management continuing to reiterate guidance on non-NAMA loan losses. Net interest income (NII) declined by 29% yoy to €1.11bn, in line with expectations and operating profit fell 32% to €553m. Profitability is being impacted due to competition on deposits, higher term funding costs, the government guarantee and reduced business activity. Net Interest Margins (NIM) declines highlight these pressures falling from 1.59% at year end to 1.41% at the half year. On NAMA impairments, the group has taken another €466m, leaving the group with €2.9bn of provisions against NAMA loans. The coverage ratio in non-NAMA declined slightly to 42% from 44% as the end of December, with residential mortgages the main reason for the decline. Impaired loans in residential have increased by 58.5%, with large increases in property and construction and SME impaired loans. Customer deposits remained flat from the full year at €84bn with the loan to deposit ratio increasing to 1.43x from 1.41x at the full year. The results this morning have a number of positives including the fall in non-NAMA impairment charges for the first half of the year along with management re-iterating guidance on the impairment charge over the cycle. The decline in NII and operating profits highlight the difficulties for the Irish banks with funding expensive and little demand domestically for debt. We still believe BOI is best placed of the Irish banks to take advantage of the current difficulties and after its recapitalisation, management can now focus on achieving their 2013 targets.

Smurfit Kappa: Buy **Previous Close** €7.85 **Target** €9.50 **Analyst** Edward Keeling

Smurfit Kappa released its Q2 results this morning and the group has posted a result ahead of consensus expectations. EBITDA for the period came in at €221m, ahead of analysts forecasts of €200m, but probably broadly in line with a whisper number of c. €220m. EBITDA margins were 13.0%, higher than 12.3% in 2009, primarily reflecting the progress in its European packaging business. This segment was supported by increasing demand growth and further advances in corrugated price recovery. Revenue for the period was €1,696m, which is compared with estimates of €1,614 and €1,498 from the same period last year. The group's performance continues to highlight the significant contribution of its Latin American operations which is supported by sustained strong volume and pricing momentum in the region. After a 7% year on year demand growth in Q1, it's Latin American corrugated deliveries were 11% higher year on year in Q2. In Europe, the group's corrugated volumes were on average 5% higher than in Q1. In addition, for the beginning of Q3, demand for the group's corrugated products has remained firm. Net debt increased by €239m in the first half of the year, as a result of cyclical working capital outflows, combined with negative currency impacts and the cash flow linked to the asset swap with Mondi. Nonetheless, Smurfit still expects strong cash flow in the second half of the year, which will lead to a positive free cash flow for 2010 in total and to a meaningful reduction in its net debt to EBITDA ratio. In terms of outlook, Smurfit has not seen any signs of a slowdown across its businesses to date and now expects to deliver EBITDA growth in the region of 20% for the full year.

Aviva

BUY

Current Price: £3.84

Price Target: £5.00

11th August 2010

Analyst: **Oliver Gilvarry**



- Aviva's recent full year results beat estimates in a number of areas. Operating profit increased by 21% yoy with EPS increasing by 55.8%. Sales increased by 4% in the period to €20.2bn.
- New business margins improved by 30bps to 2.40% driven mainly by the UK, with margins at 3.4% due to better cost control.
- Cost control continues with a reduction of 4% yoy and on a constant currency basis, costs were flat despite higher sales.
- Capital within the group remains strong with IGD solvency at £3.8bn, a decline of £700m due to a once off pension provision, dividend payment and FX moves. The group retains hedges to protect the capital position for volatility in the market along with currency hedges.
- Shareholders funds is invested mainly in debt securities and mortgages at 85%. The majority of the debt securities portfolio in investment grade with only £538m exposure to Greece, Spain and Portugal.
- The loan to value (LTV) of the UK Commercial mortgage book has increased to 99%, but the rental cover remains at 1.3x with arrears of less than 1%. The group maintains its £1.1bn provision against the UK annuity book and during the conference call, there was no indication any of this will be reversed in the foreseeable future.
- The strong operating profits along with the balance sheet strength allowed the board to increase the interim dividend by 6% to 9.5p, which is well covered. The group has continued to grow capital organically delivering £900m in the first half of the year and has increased guidance for the full year to £1.5bn from £1.3bn. This provides further stability to the current payout and allowing further increases in dividend.
- On individual businesses, the UK Life and Pensions performed very well with sales increasing along with higher margins. General insurance also performed well helped by higher premiums, resulting in a combined ratio of 98%.
- Aviva Europe increased sales and operating profit in the period, but new business margins fell by 2bps to 3.6%. The group has performed well in Europe due to a large number of bancassurance agreements along with an increase in retail sales.
- In the US, sales fell but this was offset by higher margins increasing operating profit by 258%. Aviva's CEO stated they will see how the division performs over the next number of quarters and the group is not looking for any acquisitions in America.
- The embedded value (EV) for the half year was £4.61, but we expect this to move towards £5.00 for the full year. With further cost savings, increasing sales and an attractive ROE, we value the group conservatively at 1x EV. The group will also pay a dividend yield of 6.60% that is well covered and will increase further in coming years.

Descriptive Stats		Shareholders	
Year to date	-3.19%	Blackrock	4.94%
52 Week High	474p	Legal & General	3.93%
52 Week Low	290p	Axa	3.81%
Reuters	AV.L	Franklin Resources	3.21%
Bloomberg	AV/ LN	M&G Inv. Mgt.	2.52%

	FY09	FY10e	FY11e
Revenue £m	31,821	39,846	41,896
Operating Profit	2,786	2,420	2,615
Net profit	1,627	1,741	1,878
EPS p	56.9	56.6	61.2
DPS p	24	25	27
P/E	6.77	6.81	6.29
Div Yield	6.31%	6.56%	6.88%

Peer Analysis	P/E 10	P/E 11	Div Yield
Prudential	21.1	16.7	3.41%
AXA	8.6	8.65	3.86%

2009 Revenue Breakdown



UK	31%
Europe	52%
North America	14%
Asia Pacific	2%
Aviva Investors	1%



International Equity Markets

Index	Value	1-Day	YTD
ISEQ	2,959	-0.8%	-0.9%
FTSE	5,376	-0.6%	-1.7%
Dow Jones	10,644	0.4%	2.1%
S&P	1,121	0.5%	0.5%
Nikkei	9,551	-0.2%	-11.9%
Stoxx 50	2,800	-1.0%	-6.5%

Sector Performances

Sector	Index	1-Day	YTD
Construction	253	-1.7%	-9.3%
Technology	193	-1.1%	3.3%
Oil & Gas	305	-1.5%	-8.6%
Financials	226	-1.2%	1.0%
Retail	264	-0.3%	8.1%
Food & Drink	324	0.3%	7.0%

Commodity Prices

Commodity	Index	1-Day	YTD
Crude Oil	80.25	-1.5%	-4.1%
Copper	331.25	-1.2%	-2.7%
Gold	1,204.25	0.2%	9.3%
Silver	18.16	-0.5%	7.5%
Wheat	726.75	-2.3%	21.0%
Cattle	95.33	-0.2%	6.1%

Currency Exchange Rates

Currency	Index	1-Day	YTD
€/\$	1.318	-0.3%	-8.8%
€/£	0.831	-0.1%	-6.8%
£/\$	1.585	-0.2%	-2.3%
\$/JPY	85.440	-0.6%	9.2%
€/JPY	112.580	-0.9%	-16.5%
€/SFR	1.382	-0.4%	7.9%

5Yr Credit Spreads

Product	Index	1-Day	YTD
Invest Grade	119.7	1.6%	49.9%
High Yield	513.3	2.3%	-0.5%
Financials	143.6	4.8%	67.0%
BoI	325.2	2.3%	15.9%
AIB	438.8	3.3%	43.2%
RBS	201.6	1.5%	26.5%

Money Market Rates

Rate	EUR	UK	US
Overnight	0.8%	0.5%	0.2%
3-Month	0.9%	0.7%	0.4%
1-Year	1.2%	1.1%	0.5%
2-Year	1.4%	1.4%	0.7%
5-Year	2.0%	2.3%	1.7%
10-Year	0.028	3.3%	2.8%

Date	Company	Region	Event
11/08/2010	E.ON AG	DE	Q2
11/08/2010	SolarWorld AG	DE	Q2
11/08/2010	Bank of Ireland	IE	INTERIM
11/08/2010	Smurfit Kappa Group Plc	IE	Q2
11/08/2010	Nestle SA	CH	INTERIM
11/08/2010	Adecco SA	CH	Q2
11/08/2010	Balfour Beatty PLC	GB	H1
11/08/2010	Standard Life Plc	GB	Q2
11/08/2010	Cisco Systems	US	Q4
11/08/2010	Macys	US	Q2
12/08/2010	Conergy AG	DE	Q2
12/08/2010	Greencore Group PLC	IE	TRADE
12/08/2010	Prudential Plc	GB	INTERIM
12/08/2010	Psion Plc	GB	INTERIM
12/08/2010	The Estée Lauder Co.	US	Q4
13/08/2010	Bauer AG	DE	Q2
13/08/2010	Fresenius SE	DE	Q2
13/08/2010	Hypo Real Estate Holding	DE	Q2
13/08/2010	ThyssenKrupp AG	DE	Q3
13/08/2010	JCPenney	US	Q2
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Date	Event	Region	Estimate
11/08/2010	Claimant Count Rate	UK	--
11/08/2010	Jobless Claims Change	UK	--
11/08/2010	Average Weekly Earnings	UK	--
11/08/2010	ILO Unemployment Rate	UK	--
11/08/2010	BoE Quarterly Inflation Report	UK	--
11/08/2010	MBA Mortgage Applications	US	--
11/08/2010	Trade Balance	US	--
11/08/2010	Monthly Budget Statement	US	--
12/08/2010	ECB Publishes Aug. Report	EC	--
12/08/2010	Euro-Zone Ind. Prod.	EC	--
12/08/2010	Import Price Index (MoM)	US	--
12/08/2010	Initial Jobless Claims	US	--
12/08/2010	Continuing Claims	US	--
13/08/2010	GDP s.a. (QOQ)	GE	--
13/08/2010	Euro-Zone GDP s.a. (YoY)	EC	--
13/08/2010	Euro-Zone GDP s.a. (YoY)	EC	--
13/08/2010	Advance Retail Sales	US	--
13/08/2010	Retail Sales Less Autos	US	--
13/08/2010	CPI Ex Food & Energy (YoY)	US	--
13/08/2010	Retail Sales Ex Auto & Gas	US	--
13/08/2010	U. of Michigan Confidence	US	--
13/08/2010	Business Inventories	US	--

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