

DOLMEN WEEKLY TRADER



Weekly Market Commentary July 26th 2010

Second quarter earnings from the majority of US corporates have been reasonably positive however we have seen little in the way of earnings upgrades for 2011. With economic forecasts being reduced, market commentators have been focused on the difference between bottom up (positive) and top down (more negative) forecast of earnings. Markets do not look very expensive and the removal of some risks including; BP, stress tests etc. combined with the lowering of the risk free rate of return creates an improved fundamental outlook. Nonetheless there is a buyer strike with cash levels at institutions reaching recent highs and this leaves the technicians using technical analysis remaining bearish until we take out previous highs such as 5320 on the FTSE. In times of lower turnover, M&A resumes as companies achieve scale through acquisition of market share. We think markets will most likely remain range bound near term before heading higher in Q4. On the economic front growth forecasts in Germany may see some upward bias. The US will take some comfort from Bernanke not in terms of growth but likely policy support if growth slows. The lower interest rate outlook for longer remains. We are seeing an end to some of the Chinese tightening measures allowing a bounce in commodities. Stress tests may result in concerns over sovereign peripheral debt and/or growth rates if bank lending does not resume. Any weaker led Euro increases in growth forecasts may be offset by concerns over fiscal austerity measures in other European economies. Supply of bonds in Europe and the US generally got away last week except at the very long end of the German curve but it is difficult to see excessive demand for 30 year bonds. Key economic releases for the week ahead will come from the US with New Home sales on Monday, Consumer confidence on Tuesday, Durable goods on Wednesday and second quarter GDP on Friday all due for release.

Trading Recommendations

Earnings Season Update

Analyst: Stephen Taylor

Overall earnings in general from the US over the past two weeks have been relatively strong with a few disappointments on the revenue side in particular for financials. We saw numerous companies increase earnings guidance last week including cyclical names such as Caterpillar, 3M, UPS and Honeywell. This has led to estimates increase for the S&P 500 for 2010. Company CEO's have been reasonably upbeat in relation to the outlook for the global economy, however the usual concerns remain in relation to US housing and lower demand from Europe. While earnings have been upgraded for 2010, we have not seen many moves higher for 2011 which is where the market is beginning to focus. With lower GDP forecasts currently expected for 2011 we are unlikely to see any major positive moves on earnings for 2011. For the week ahead the focus will shift to Europe where the majority of companies will be reporting from. Key releases include; BP, Deutsche Bank, SAP, Daimler, Telefonica, Travis Perkins, Lafarge and Siemens.

Vodafone - Buy

Previous Close (150p)

Target (155p)

Analyst: Stephen Taylor

Last Friday Vodafone issued a positive trading statement for its fiscal first quarter of 2011. The results highlight the return to organic service revenue growth & improved outlook in emerging markets in particular India and Turkey. In addition, data revenue growth due to increased smart phone usage in particular with Apple's iPhone is strong and will be a major driver of earnings growth into the future. As a result of its strong update, Vodafone was able to reiterate earnings guidance and its expectation to increase its dividend by 7% a year over the next three years. Vodafone signalled that it will review its business strategy and range of units. This could potentially lead to asset sales and would be taken as a significant positive by the market. We would use any weakness as a buying opportunity.

Oil Major Results Preview

Analyst: Brian Gallagher

The next two weeks sees all the oil majors on both sides of the Atlantic report results for the second quarter. We expect that earnings have improved reflecting higher than forecasted oil prices and further evidence of a recovery in refining margins. Without any doubt the marquee event of the week will be BP's results. The market is expecting the oil major to outline its post Macondo strategy by announcing how it intends to protect itself from the fallout from the recent disaster. We expect the event to be a positive catalyst for the stock as it will mark the beginning of the end of the oil spill. Key oil companies reporting next week include: **BP** (Tuesday/EPS: 26c), **Royal Dutch Shell** (Wednesday/EPS: 69c), **Exxon Mobil** (Thursday/EPS: 145c) & **Chevron** (Friday/EPS: 234c)

Tullow Oil - Buy

Previous Close (1179p)

Target (1470p)

Analyst: Brian Gallagher

Tullow Oil's positive momentum continued this morning with the announcement that the explorer had encountered oil at its Owo well. This Ghanaian prospect has provided greater clarity on the size of the reserves in the Deepwater Tano licence and significantly derisked a number of surrounding prospects. We continue to rate the stock as a buy and see further upside in the company's exploration portfolio.

EU Wide Stress Tests

Analyst: Oliver Gilvarry

Of the 91 European banks examined, seven failed. Both AIB and BOI passed the stress test with AIB passing on the basis of it raising €7.4bn following Ireland's own stress test on the banking system earlier this year. The number of banks failing the exercise was less than expected, but the CEBS stated that 30 institutions passes were dependent on continued government support. The threshold for a pass was a Tier 1 ratio of 6% with 12 banks just passing with Tier 1 levels of less than 7%. AIB was one of these banks with a Tier 1 under adverse conditions of 6.5%. BOI had a Tier 1 of 7.1% under the adverse scenario. UK banks such as Lloyds and Barclays reported a strong Tier 1 under the adverse scenario of 9.2% and 13.7% respectively. The numbers of fails in the tests are not as high as expected with the total capital requirement also lower. The test also assumed no sovereign default of an Euro-Zone nation which will reduce the creditability of the results. The impact on sovereign holdings is only on trading portfolios with for example an estimated haircut of 23.1% for Greece, 14.1% for Portugal and 12.8% for Ireland. For securitisation holdings a downgrade of 4-notches is modelled, which again will be seen as soft. The one positive from the tests is the detailed disclosure by most banks of their sovereign exposure, held in trading portfolios and banking books (excluding a number of German banks). Increased disclosure is a positive, but we believe the tests will not be a catalyst for a rally in European financials as lower economic growth over the next number of years will impact loan growth and in turn reduce profitability.

This Week's Market Events

MONDAY

Corporate

Reckitt Benckiser Group H1, Pearson PLC H1, WSP H1, National Grid TRADE + AGM, Ovoca Gold AGM + EGM

Economics

Hometrack Housing Survey UK, Chicago Fed US, New Home Sales MoM US

TUESDAY

Corporate

AIR France-KLM Q1, Deutsche Bank AG H1, SAP Q2, DAB Q2, Daimler Q2, Deutsche Boerse AG H1, Mittel Q2, UBS Q2, BP Plc Q2, Vodafone AGM, DuPont Q2,

Economics

S&P/CaseShiller Home Price Ind US, Richmond Fed Index US, Consumer Confidence US, ABC Consumer Confidence US

WEDNESDAY

Corporate

Peugeot H1, ArcelorMittal H1, EasyJet Q3 TRADE, BAT H1, Centrica H1, Invensys Q1 TRADE + AGM, BG Group Q2, Rexam H1, Symantec Q1, ConocoPhillips Q2, Visa Q3

Economics

MBA Mortgage Applications US, Durable Goods Orders US, Durables Ex Transportation US, CPI GE

THURSDAY

Corporate

France Telecom Q2, Volkswagen Q2, Royal Dutch Shell Q2, Statoil Q2, Telefonica H1, Banco Santander Q2, Tyco Q3, BAE Systems PLC H1, Rolls-Royce H1, Travis Perkins H1, BT Group Q1, AstraZeneca H1

Economics

Unemployment Rate GE, Consumer Cred UK, Mort Apps UK, M4 Money UK, Bus Climate Indic EC, eZone Confidence EC, Initial Jobless & Continuing Claims US, Fed's Beige Book US

FRIDAY

Corporate

Lafarge H1, Alcatel Lucent Q2, Total Q2, Anglo American H1, Rentokil H1, British Airways Q1, Chevron Q2, Merck Q2

Economics

eZone Unemployment Rate EC, eZone CPI, GDP US, Personal Consumption US, Core PCE US, Chicago Purchasing Manager US, U. of Michigan Confidence US

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