

# Traders Update

MONDAY 4TH FEBRUARY 2008

## Market Comment

Financial markets remain under considerable stress, and credit has tightened further for some businesses and households. These words used by the Fed, as it delivered its second rate cut in nine days, pretty much sum up the current situation in financial markets. The reassuring words out of monoline insurer MBIA also helped ease nerves somewhat as did the hostile approach by Microsoft to Yahoo!, which demonstrated that M&A was not extinct. What still lurks in the background for the markets is the uncertainty about the broader economy. The Non-Farm Payroll data on Friday showed a decline in jobs of 17,000, but in all likelihood this number will probably be as irrelevant as previous weak readings, when we get a major revision upwards next month. Equally, the stronger than expected Manufacturing ISM reading, when a sub-50 number was expected also served to confuse the market. This pattern of unpredictable readings only serves to extend the period of volatility we have seen so far this year. While the rate cuts will help in the medium-term to bring in more consistent data, in the short-term, uneven economic releases and further fears about monoline insurers will dominate. The latter point could well be key, since while monetary easing is welcome, no-one, not even the Fed can force banks to borrow or lend, and this, along with a deteriorating housing market will do little to ease credit conditions for businesses and households.

## TRADING IDEAS, EARNINGS & PREVIEWS

**Economic view** : Focus returns to Europe this week with the ECB and Bank of England due to decide on interest rates following the US Federal Reserves' decision to lower its Fed Funds rate by a further 50 basis points. We expect that the ECB to remain on hold at 4.00% and Jean Claude Trichet to reiterate his hawkish stance on inflation given that last week data showed that Euro-Zone inflation is currently running at 3.2% well above the ECB's targeted range of 1%-2%. With growth in the UK slowing we expect the Bank of England to reduce rate buy 25 basis points to 5.25%.

### RBS

**Price:** 396p  
**P/E:** 5.57x  
**Div:** 8.56%  
**Target:** £5.75  
**Buy**

**Fundamental view** : A major international investment bank has published a SELL recommendation on **Royal Bank of Scotland (RBS)** at current levels, with a price target of £3.50. We expect the same investment bank to be upgrading this price target and recommendation on RBS within the next 12 months as its core assumption that RBS' bad debts charge deteriorates to the same level that it reached at the end of the last major UK recession in 1992 proves wrong. The other area of scare mongering in the commentary was in relation to the need for a rights issue. By focussing on the capital ratios of "tangible equity : assets" and "equity Tier 1", it is highlighted that RBS' tangible equity : assets ratio was 5.2% in 1989, versus 1.2% forecast for 2008, and that its equity Tier 1 ratio is forecast to be 4.1% in 2008, versus a current sector average of 6.5%. However, "tangible equity : risk weighted assets (RWA's)" and the overall "Tier 1 ratio" are much more relevant ratios in determining the need for a rights issue, and these ratios show that assuming no further major write-downs, that RBS does not currently need a rights issue.

**Next catalyst** : Last December's trading statement confirmed that the bank's Tier 1 ratio as at 31/12/07 will be comfortably within its targeted range of 7% and 8%, and so as a result we are comfortable with our current 2007 and 2008 dividend per share forecasts of 33p and 37p respectively. As a result, we expect a 2007 final dividend per share of 22p net to go ex on c.7th March. As this final dividend alone represents a yield of 5.7% on the current share price, it may generate some buying interest ahead of the early March ex date. In conjunction with RBS' full year results' release on 28th February, we also expect the bank to issue specific 2008 earnings guidance, which could act as a positive catalyst for major share price upside from current levels. Another potential positive catalyst between now and then could be a 0.25% cut in the UK base rate this Thursday, 7th February.

**Chart view**: Recent price action has been positive and a close above the 400 area would break the short term negative outlook.

### Anglo

**Price:** €9.99  
**P/E:** 6.66x  
**Div:** 2.35%  
**Target:** €15.00  
**Buy**

**Fundamental view** : **Anglo Irish Bank's** AGM statement on Friday contained some important reassurance with regard to the bank's 2008 earnings prospects by re-affirming guidance in line with current market consensus of 15% growth in earnings per share. Current consensus forecasts already factor in a slight increase in the bad debts charge from 0.16% of risk weighted assets last year to 0.25%, very slight net interest margin erosion from 1.93% last year to 1.9%, and slightly lower loan growth from 36% last year to 18%. Reassurance was also provided by the statements that the bank's "liquid position is as strong as at 30th September 2007", and that it has "limited exposure to assets impacted by the current credit markets uncertainty."

**Next Catalyst** : Similar such reassurance could be provided by the several full year results' announcements from the UK bank sector this month, with Bradford & Bingley, Barclays, Alliance & Leicester, Lloyds TSB, Standard & Chartered, HBOS and Royal Bank of Scotland all announcing full year results on 13th, 19th, 20th, 22nd, 26th, 27th and 28th February respectively. In Ireland, AIB will announce its full year results on 20th February. These results' releases in eliminating some of the uncertainty and scare

### Ryanair

**Price:** €3.15  
**P/E:** 11.48x  
**Div:** €6.20  
**Buy**

**Fundamental view** : Even though **Ryanair** re-iterated its current year earnings guidance for 17.5% net profit and eps growth to €470m and 31.5c respectively, rather than another "bloodbath" in relation to yields (average fares), it talked this time about a potential "perfect storm" that could lie ahead for the European airline industry. It issued a massive net profit range of between €500m (c.35c per share) and €235m (c.16c per share) for the year ending 31/03/09. Our view is that forward net profit of €445m, 5% lower year on year, will be generated, representing a largely flat year on year eps of 31c, post the new buyback.

**Next catalyst** : Coincidentally, the airline will commence another €200m share buyback after Wednesday of this week, 6th February, which if completed for cancellation at an average price of €3.60 would reduce the number of shares in issue by 3%. The buyback is expected to be completed between now and the airline's full year results' announcement on 3rd June, so don't be surprised if the yield outlook becomes a little more robust at that stage. Our view is that the current share price level of c.€3.15 will once again over time prove to be an attractive entry level for medium term investors.

### Tesco

**Price:** 420p  
**P/E:** 16.75x  
**Div** : 2.6%  
**Target:** 500p  
**Buy**

**Fundamental view** : **Tesco** recently issued its interim management statement encompassing the Christmas trading period. Total UK like-for-like sales increased by 3.1% which was slightly below expectations of 3.5%-4.0%. While the UK performance was slightly disappointing, Tesco's international division saw revenue rise by 26.9%, beating consensus estimates of 22%-25%. International sales now represent 26% of total group sales for Tesco. Central Europe showed particularly strong growth of 30% and in some of its newest countries such as Turkey and Malaysia growth was exceptionally strong with sales rising by 80% and 60% respectively.

**Next catalyst** : The next catalyst for Tesco will be on April 15<sup>th</sup> when the group is due to reports its full-year results. While the UK consumer is clearly under pressure it is Tesco's significant overseas exposure that will help drive profit growth.

### Microsoft

**Price:** \$30.42  
**P/E:** 16.26x  
**Div:** 1.445  
**Target:** \$41  
**Buy**

Last Friday, **Microsoft** made an unsolicited \$44.6bn offer in cash and stock to buy Yahoo in an attempt to challenge Google's dominance in the Internet search services and advertising market. This is the largest transaction that Microsoft has entered into since it purchased online advertising provider aQuantive for \$6bn last year. While the deal is expected to be slightly dilutive to EPS by \$0.05 in 2009, we believe that Microsoft management has the ability to turn Yahoo around and achieve the \$1bn synergies that it predicts. While Microsoft's offer for Yahoo is expensive at 68x earnings, we are of the opinion that the company will be able to turn around the fortunes of Yahoo and pose a serious threat to Google that currently has a 56% share in the US internet search market compared to 31% from a combined Microsoft and Yahoo. The internet and advertising market is expected to double to over \$80bn by 2010. While we do acknowledge that reaction in the investor community has been mixed and some short-term concerns do remain i.e. the possibility of a competing bid we still believe that at 16x 2008 EPS, shares in Microsoft represent excellent value.

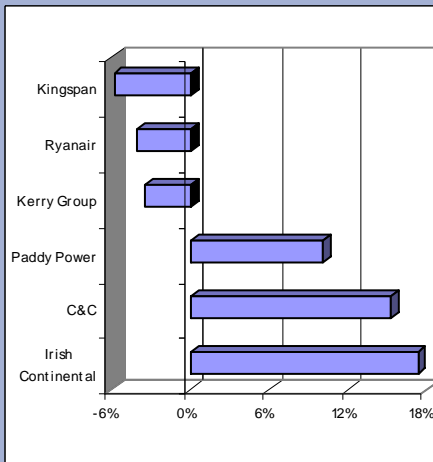
**EARNINGS:** **MON** (Ryanair , Q3) **TUES** (Vallourec , TS) (BP , TS) (B.A , Traffic) (Heidelberg , Q3) **WED** (Aviva , NB) (BHP , H1) (BSKYB , TS) (Electrolux , TS) **THURS** (Deutsche Bank, Prelim) (BT , Q3) (Easyjet , Q1) (Pepsico,Q4) (British Land , Q3) (GlaxoSmithKline , Prelim) (Unilever , TS)

**ECONOMIC:** Monday (Euro-Zone PPI, US Factory Orders), Tuesday (Euro-Zone Retail Sales, US Non-Manufacturing), Wednesday (US Nonfarm Productivity, Unit Labor Costs), Thursday (UK Industrial Production, ECB and BoE interest rate decisions, US Jobless Claims, Pending Home Sales, Friday)

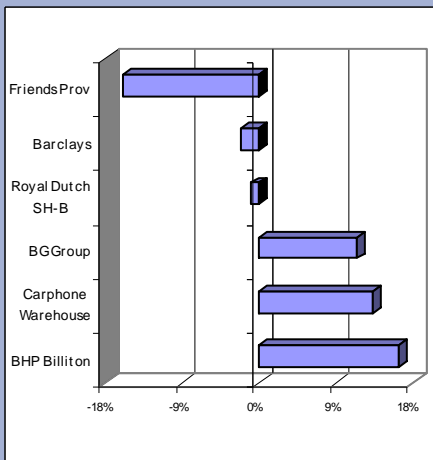
# DOLMEN STOCKBROKERS Traders Update

Last Weeks Best/  
Worst Performers  
25/01/08-01/02/08

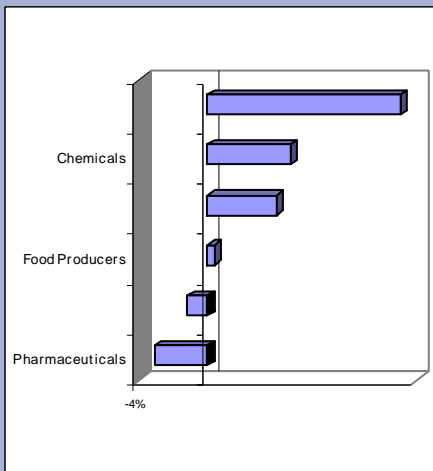
## ISEQ



## FTSE



## Sector changes WTD



# Dolmen Dozen

## WEEKLY UPDATE

Company	WTD	Relevant news
AIB	-4.0%	The US Fed reduces interest rates by another 50bps.
Aviva	-0.5%	An Aviva led consortium acquires a 91.65% stake in S.Korean life insurer LIG Life Insurance.
BP	0.7%	BP wins \$10B deal from Jurong Aromatics to supply Feedstock.
Coca Cola	0.1%	PepsiAmericas Q4 profit up but shares sink on weak FY08 view.
CRH	1.9%	CRH has announced major expansion plans for its Polish and Ukraine cement operations.
Hewlett Packard	-0.2%	HP announces strategy to bridge gap between content creation and publishing.
IAWS	-0.7%	Flowers Food's, a large US bakery concern, earnings growth in 20078 was 16.7%.
IL&P	4.5%	Standard Life's new business sales figures for '07 show a 22% growth in Irish life sales to £56m.
Microsoft	-9.3%	Microsoft makes \$44.6B offer for Yahoo.
Paddy Power	5.3%	Peer Partygaming Q4 revenue reached \$120m. A 52% increase on the 2006 Q2 revenues.
Ryanair	-6.9%	Ahead of Q3 results out on Feb 4th.
Vodafone	3.3%	Q3 Revenues up 15.8% to £9.2B. Organic growth was 4.4%.

DD Unrealised gain YTD	-6.43%	ISEQ YTD	-1.36%
DD Realised gain YTD	-10.55%	FTSE YTD	-6.62%
DD Total YTD	<u>-7.47%</u>	Average performance	<u>-3.99%</u>
Relative Performance		<u>-3.47%</u>	

\* DD Return (Includes dividends & FX changes since stocks inclusion)

## What it says in the 'Sundays'

Company	Paper	Headline
IL&P	S. Independent	"Falling shares boosting yields"
Microsoft	S. Tribune	"Bringing in bad debt specialists"
Paddy Power	S. Tribune	"Microsoft and Yahoo- signals revival of M&A"
McInerney	S. Times	"Worth more than an each way bet"
CREO	S. Business Post	"McInerney ripe for break up"
	S. Business Post	"CREO - an attractive investment"

## Recent Corporate Visits

Company	Change on year	Meeting date	Relevant news
Upcoming Corporate visits : Over the next few months we will have a number of Irish and International companies presenting to US. Paddy Power have confirmed that they will present to US in May, while IAWs have said they will present to us after their results in March. We also expect to have the Irish management of Intel, Microsoft and Hewlett-Packard in to speak with us.			
Anglo Irish Bank	-11.62%	29/11/07	Group CEO David Drumm explained that the bank business model remains protected from the current banking crisis

# Last Weeks Moves

## Equities

	Level	Change WTD	Change YTD	Div Yield	P/E
ISEQ	6840	-1.9%	-8.7%	2.8%	9.9
FTSE 100	6029	-4.8%	-10.7%	4.0%	11.3
DAX	6969	-5.2%	-11.9%	2.8%	11.0
Dow Jones	12473	-4.0%	-8.8%	2.3%	14.3
S&P 500	1395	-5.4%	-9.8%	2.0%	18.9
Nasdaq	2413	-4.1%	-11.8%	0.8%	23.8
EuroStoxx 50	3301	-5.3%	-11.0%	4.0%	10.6
Nikkei 225	13497	-1.8%	-12.9%	1.5%	16.4

## Sector

	Weekly move%	YTD move %
Mining	11.05	0.18
Chemicals	4.73	-7.36
Media	3.92	-6.82
Leisure Goods	3.64	-9.38
General Retailers	3.30	-12.51
Software & Computer	2.88	-6.19
Telecommunications	2.25	-6.68
General Industrials	2.14	2.75
Construction & Materials	2.10	-12.73
Tobacco	2.06	-8.60
Oil & Gas Producers	1.36	-11.28
Personal Goods	1.33	-14.38
Technology Hardware	1.26	-9.56
Beverages	0.98	-5.79
Banks	0.90	-7.38
Gas, Water & Multiutilities	0.62	-7.63
Insurance	0.57	-10.55
Food Producers	0.38	-5.25
Automobiles & Parts	-1.15	-21.08
Pharmaceuticals	-3.03	-10.79

## Commodities

	Current	Change YTD
Crude Oil	\$88.96	-7.1%
Gold spot	\$905.48	+8.6%

## Exchange Rates

	Current	YTD Change	Year End (est)
EUR-USD	1.482	+1.6%	1.55
EUR-GBP	0.753	+2.5%	0.75
EUR-JPY	157.7	-3.2%	165.0

## GDP Growth

	Current	Year End (est)
Ireland	5.00%	3.00%
Euro Zone	2.50%	2.00%
UK	3.10%	2.00%

## Central Bank Interest Rates

	Current	3 month	Year End (est)
Euro Zone	4.00%	4.37%	3.75%
UK	5.50%	5.56%	5.00%
US	3.00%	3.10%	3.00%

## Credit Market Summary

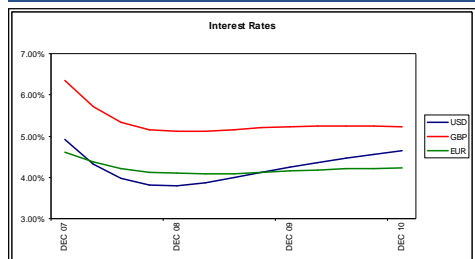
This week started with spreads trading comfortably at 440bps; there was little or no reaction in the credit markets to the Fed 50bps rate cut (reaction would have been very negative if the Fed had not delivered that cut) however by the end of the week the ugly reality of the problems with the Monoline insurers hit the credit markets as analysts began predicting the size of potential write-downs for banks and reports that preliminary bailout discussions between banks and regulators in the US were struggling to agree on bailout solutions. High yield spreads ended the week 5% wider at 464bps.

## Credit Sector Movements

**Building materials:** Wider in the sector – La Farge was this weeks biggest mover, widening 9% after two equity rating downgrades from Credit Suisse and BNP citing the possibility of a slowdown in emerging markets and declining pricing power. Heidelberg was 4.7% wider this week while Saint Gobain was unchanged after a weak week last week, and CRH was unchanged.

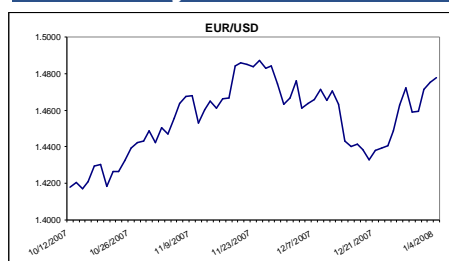
**Retail:** Mixed in the sector – biggest mover was Sainsbury, which widened 11% after announcing that Qatar Investment Authority now owns 25% of the company. Other food retailers were mixed, Morrisons 4.4% tighter while Tesco was unchanged. Non-food continues to under-perform; Dixons moved 4.5% wider to 217bps; while Kingfisher was 1.3% wider at 230bps. MKS was unchanged.

## Interest Rate Outlook

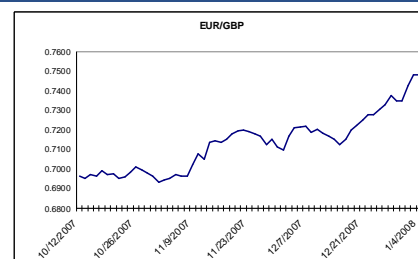


Short-term US Treasuries declined last week after the Fed lowered rates and indicated that further rate cuts could be on the way. The yield on the two-year US treasury fell by 14 basis points to 2.07% while in Europe, the two-year Bund yield fell by 7 basis points to 3.37%.

## Currency Comment



The € strengthened against the \$ last week as the US Federal Reserve lowered its interest rate by a further 50 basis points to 3.00% and indicated that further downside risks to growth remain indicating that further rate cuts could be in line. Focus returns to Europe this week when the ECB is expected to keep its benchmark interest rate on hold at 4.00% and we also expect Trichet to reiterate his hawkish inflationary



The € gained ground against £ last week as expectations increase that the Bank of England will lower its base interest rate by 25 basis point on Thursday to 5.25% without ruling out the possibility of a 50 basis point cut. Economic data from the UK has been weak over the last number of months as the consumer has tightened its belt.



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