



Market fundamentals went out the window last week as fear and panic gripped investors and market volatility reached extreme levels. The continued lack of a functioning credit and cash market continued to be the dominant theme and concerns about the global banking system saw an unprecedented level of government and central bank intervention with the UK Government launching its own version of a bail-out package and the Federal Reserve moving to service the private sector by accepting commercial paper as collateral for funding. The most significant event however was the co-ordinated move by six central banks to all cut interest rates by 0.50% in an attempt to free up the cash markets. These efforts however all failed to reverse the most severe equity sell-off since 1987 as the problem continues to be not the cost of cash, but the unwillingness of banks to lend to each other. The other issue that remains is concern about the capitalisation of the global banking system and by consequence the ramifications on the global economy. Global growth has slowed dramatically in recent months and nowhere is this more evident than in the fall in oil and other commodities which are now down over 45% since their mid-July peak. The problem for equity markets is that the traditional drivers of performance- earnings and dividends- are under threat, a fact that is decidedly negative. However the other factor that has contributed to the severe sell-off in equities is that with the exception of the government bond markets, equities are the only normal functioning asset class, so as is now the case, when investors require cash they will sell their most liquid risk assets. Until such time as the inter-bank and credit markets free up, the risk to equity markets remains elevated.

## TRADING IDEAS, EARNINGS & PREVIEWS

### Ranking of Irish Banks

Looking at Irish banks and the risk levels of each, we have ranked them based on our perceived level of risk. We have determined ILP has the lowest risk of Irish banks due to 88% of the loan book been residential mortgages in Ireland & the UK with no exposure to residential or commercial development. Capital is not an issue as ILP has circa €1Bn of excess capital in its life book that can be used to support the banking portfolio. On the downside, it is the most heavily reliant on wholesale funding of the Irish banks.

The next favoured Irish bank is AIB due to its ability to realise capital from selling assets such as Poland and M&T in the US and this could conservatively raise €1Bn in extra capital. This would offset dilution for shareholders in the scenario AIB has to raise extra capital due to bad debts. A negative point for AIB is its exposure to Residential and Commercial developers of €23.5Bn with Ireland been the majority of this exposure.

On the remaining two banks, we favour BOI over Anglo due to the more diversified and less loan risky book in BOI. BOI is our third pick due to its lack of disposal options compared to AIB and it has a lower core Tier 1 than ILP and AIB.

### Banking Update

This morning, the UK government outlined further details on its financial support to the banking industry. The government is making capital investments in RBS along with the soon to be merged Lloyds/HBOS to the tune of £37bn. RBS will raise £20bn under the scheme with £15bn coming from the issue of new ordinary shares which will be fully underwritten by the UK Treasury along with £5bn in preference shares. The ordinary shares will be issued at 65.5p while the preference shares (which will not be convertible in to equity) will carry a coupon of 12%. No dividend will be paid until preference shares have been repaid. The government will hold a 60% stake in RBS. The merged Lloyds/HBOS entity will seek £17bn of capital of which £11.5bn will be by HBOS and £5.5bn by Lloyds and it will be 43.5% owned by the UK Treasury. Following completion of these capital infusions, each of the institutions will have Tier 1 capital ratios in excess of 9%. In contrast, Barclays has announced that it plans to sell £6.5bn of shares to private investors without turning to the government for capital support. Barclays will raise £3bn by December 31 and will sell ordinary stock to raise about £600m to fund the purchase of Lehman Brothers' assets. Barclays will also issue a further £3bn in ordinary shares by March 31 2009.

Meanwhile, European leaders yesterday agreed on a concerted action to tackle the current credit crisis. The key measures announced were : a pledge to guarantee, until the end of 2009, bank debt issues with maturities up to five years; permission for governments to buy stakes in banks, and a commitment to recapitalise what they called 'systematically' critical banks in distress. The statement from the group gave no indication of how much governments were willing to spend or the size of the bank assets deemed to be at risk. We expect European governments over the next number of days to announce further details on the measures. The announcement should be taken as a positive and should see some form of liquidity return to interbank markets, although it still may take some time for interbank borrowing rates to return to a normalised levels.

### Microsoft

Price: \$22.70  
P/E: 11x  
Div: 2.1%  
Target: \$35.00

#### Buy

**Fundamental View :** There has been increasing concern that the recent slowdown in global economic activity will have a major negative impact on corporate spending on technology. While there is no doubt that risks exist we believe that large cap diversified technology companies like Microsoft will be well able to whether the current downturn and the recent sell off in its share price in line with the market represents an excellent buying opportunity for a company with strong earnings growth and balance sheet. On 22 September, Microsoft announced that it will buyback as much as \$40bn, raise its dividend and issue its first set of commercial paper. The buyback highlights the company's confidence in its growth prospects going forward a point reiterated by its CEO Steve Ballmer last Friday as he commented that the group aims to maintain its 'strong growth' throughout 2009. At 11x 2009 forecasted earnings, the group is currently trading and the bottom end its historical trading range a multiple we feel is totally unjustified given its growth prospects.

**Next Catalyst :** Microsoft is due to release its fiscal first quarter earnings on 23 October. Given Microsoft's diversity through its product offering and geographic footprint we believe the group is well able to withstand the current economic slowdown.

### Diageo

Price: 827p  
P/E: 12.5x  
Div: 4.2%  
Target: 1150p

#### Buy

**Fundamental View :** In the current climate we are recommending that our clients focus on stocks with strong cash flows, stable balance sheets and defensive qualities. Diageo is just such a company and offers excellent value at current levels. Diageo is well diversified geographically, with significant proportion of revenues from Europe US and emerging markets. Diageo enjoys pricing power with its products as a result of premium level branding. Within the drinks sector, spirits & liquors is more stable than beer in times of economic weakness. This is particularly true for the premium and super-premium brands in Diageo's portfolio.

**Next Catalyst :** Diageo isn't due to release results until mid-February. In the mean time, the main catalyst that will move Diageo is industry data reports as well as a possible re-rating of the stock as a result of its defensive qualities. We also note the positive affect Sterling weakness has on Diageo's profits.

### Kerry Group

Price: €17.15  
P/E: 11.2x  
Div: 1.13%  
Target: €23

#### Buy

**Fundamental View:** Similar to IAWS, Kerry will benefit from the fall in soft commodity prices plus the fall in fuel oil prices. In their interim results Kerry exceeded expectations on operating margins with Consumer Foods increasing margins by 10bps and margins remaining constant in Ingredients & Flavours. Falling input costs due to lower fuel oil and food commodity prices will support margin growth going forward. The strength of the Ingredients & Flavours was also highlighted due to the increase in revenues with Asia Pacific growing by 20%, Americas by 7% and Europe by 5%.

**Next Catalyst :** At the interim results management repeated their guidance for EPS for FY08 between €1.51 and €1.55. Looking out to FY09 management have stated double digit EPS growth is possible if GBP & USD exchange rates remain close to 0.79 and 1.58 respectively. With the recent moves in the dollar looking like it will remain below the 1.55 going forward, the possibility of double digit EPS growth next year is high. That would give a 2009 EPS of €1.68 and using the sector average of 13.5x, would give a 12-month price target

## Earnings Week Ahead

**Mon:** Royal Philips Electronics (Q3).

**Tues:** Investor AB (H1), Burberry Group (H1), Cadbury (H1), Whitbread (H1), SABMiller (Q2), Carphone Warehouse (Q2), Domino's (Q3), Intel Corp (Q3), Johnson & Johnson (Q3), PepsiCo (Q3), Visa (S'Holder Meeting).

**Wed:** Diageo (MS), Abbott (Q3), eBay (Q3), JPMorgan (Q3), Coca-Cola (Q3), Wells Fargo (Q3).

**Thurs:** Britvic (TS), Smith News (FY), Nokia (Q3), BofNY Mellon (Q3), Baxter (Q3), Capital One (Q3), CIT Group (Q3), Citigroup (Q3), Harley Davidson (Q3), IBM (Q3), Merrill Lynch (Q3), United Tech. (Q3), Continental Airlines (Q3)

**Fri:** Rank Group (H1), WPP Group (Q3).

## Economic Week Ahead

**Mon:** UK Producer Price Index (09:30).

**Tues:** UK RICS House Price Balance (00:01), UK CPI (09:30), DCLG UK House-Prices (09:30), EU Industrial Production (10:00), German ZEW Survey (10:00), ECB Trichet Speaking (17:15), Irish Budget (15:45)

**Wed:** German CPI (07:00), UK ILO Unemployment Rate (09:30), EU CPI (10:00), US Producer Price Index(13:30), US Advance Retail Sales (13:30), US Empire Manufacturing Index (13:30), FED's Bernanke Speaking (17:15), Fed Beige Book (19:00).

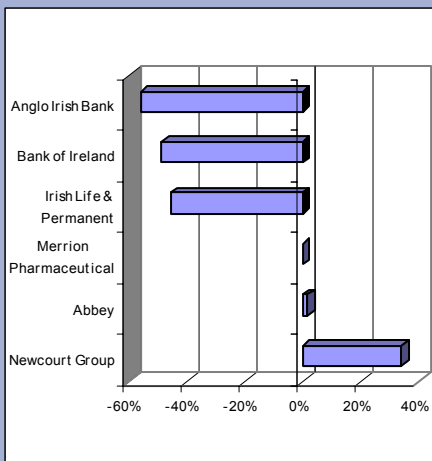
**Thurs:** US CPI (13:30), US Initial Jobless Claims (13:30), US Industrial Production (14:15), US Phil Fed Survey (15:00), US NAHB Housing Index (18:00).

**Fri:** US Housing Starts (13:30), US Michigan Confidence Survey (15:00).

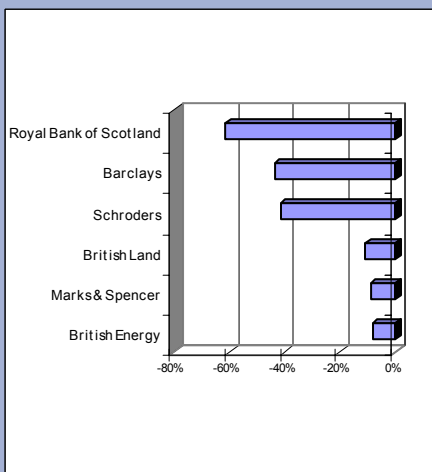
# DOLMEN STOCKBROKERS Traders Update

Last Weeks Best/  
Worst Performers  
06/10/08-10/10/08

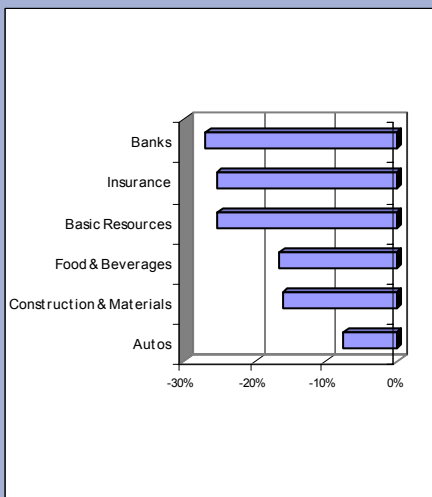
## ISEQ



## FTSE



## Sector changes WTD



# Dolmen Dozen

## WEEKLY UPDATE



Company	WTD	YTD	Relevant news
AIB	-43.5%	-73.0%	EU approves Ireland's €485bn guarantee plan.
Aviva	-13.8%	-38.8%	Aviva assures investors that it has no trouble with its solvency capital.
BP	-19.6%	-38.8%	TNK-BP says it has fully resolved its shareholders dispute.
IN&M	-13.3%	-57.8%	UK Peer Daily Mail & General Trust says full year results will be at lower end of expectations.
E.ON	-28.3%	-47.8%	E.On signs asset swap deal with OAO Gazprom granting it a stake in Yuzhno Russkoye gas project
CRH	-5.0%	-36.8%	US Federal, state and local transportation agencies obligate \$37bn in highway funds.
Hewlett Packard	-13.3%	-26.2%	HP to strengthen presence in China with new PC manufacturing plant.
Aryzta	-13.1%	-3.4%	La Brea's sales are now more than double the level which existed at the time of the IAWS purchase.
IL&P	-45.6%	-70.1%	IL&P pass on the full 50 basis point ECB interest rate cut.
Microsoft	-18.8%	-40.0%	Microsoft adjusts hiring plans, but is not initiating a recruitment freeze.
Paddy Power	-10.5%	-48.5%	Worldspreads reports accelerating activity levels.
Vodafone	-15.3%	-41.7%	Vodafone confirms it has made a non-binding proposal to acquire 15% stake in Vodacom.

## What it says in the 'Sundays'

Company	Paper	Headline
Irish banks	S. Independent	Soden says Bol must unite with its rivals at AIB
IL&P	S.Times	IL&P shuns overture from Anglo
Irish Banks	S.B.Post	Some banks may opt out of state guarantee scheme
IL&P	S.Tribune	Lloyds TSB and HBOS eye IL&P if sale is on
Irish Banks	S.Tribune	Banks call in developers ahead of property write downs

## Corporate Visits

### COMPANY

### PRESENTATION DATE

ThirdForce

19th September



## Last Weeks Moves

Equities	Level	Change WTD	Change YTD	Div Yield	P/E08
ISEQ	2871	-27.2%	-58.6%	6.8%	4.9
FTSE 100	3932	-21%	-39.1%	6.1%	7.8
DAX	4544	-21.6%	-43.7%	5.1%	9.4
Dow Jones	8451	-18.1%	-36.3%	3.8%	10.5
S&P 500	899	-18.2%	-38.7%	3.4%	17.2
Nasdaq	1650	-15.3%	-37.8%	1.3%	27.0
EuroStoxx 50	2095	-23.2%	-43.1%	5.9%	8.7
Nikkei 225	8276	-24.6%	-45.9%	2.6%	10.0

Sector	Weekly move%	YTD move %
Autos	-7.414	-37.796
Construction & Materials	-16.132	-49.512
Food&Bev	-16.555	-31.853
Chemicals	-16.962	-37.575
Travel & Leisure	-18.455	-45.554
Personal & Household Goods	-18.522	-39.046
Industrials	-18.916	-45.785
Healthcare	-19.008	-24.852
Technology	-19.047	-48.332
Retail	-19.144	-43.063
Media	-19.499	-44.765
Telecom	-19.802	-42.848
Financial Services	-21.4	-49.276
Oil & Gas	-22.651	-44.369
Utilities	-25.392	-44.349
Basic Resources	-25.425	-55.496
Insurance	-25.434	-45.379
Banks	-27.098	-50.045

## Commodities

	Current	Change YTD
Crude Oil	\$77.7	-18.9%
Gold spot	\$869.85	4.3%

## Exchange Rates

	Current	YTD Change	Year End (est)
EUR-USD	1.346	-7.7%	1.45-1.50
EUR-GBP	0.793	7.9%	0.74-0.78
EUR-JPY	134.13	-17.7%	165.0

## GDP Growth

	2007	2008 (est)
Ireland	5.00%	1.00%
Euro Zone	2.50%	1.50%
UK	3.10%	1.00%

## Central Bank Interest Rates

	Current	3 month	Year End (est)
Euro Zone	4.25%	5.38%	4.25%
UK	5.00%	6.29%	4.75%
US	2.00%	4.82%	2.00%

## Credit Market Summary

An incredible week for financial markets, credit markets in particular. We have seen an unprecedented level of government intervention, with the aim of stabilizing financial markets. The UK government is injecting capital in to its banking system, Spain has set up a €50bn TARP-like structure, the Fed will buy and hold commercial paper and a coordinated 50 bps cut from the major Western Central Banks. Spreads on financials tightened throughout the week, but non-financials widened, making new highs. A major issue currently facing credit markets is the viability of CDS contracts as bond insurance. The auction to settle Freddie and Fannie CDS contracts yielded some odd results with the recovery rate on sub-ordinates being higher than senior bonds. On October 21st, the cash payments from Fridays Lehman CDS auction are due to settle, and on the 23rd CDS referencing Washington Mutual debt will go into settlement auction. These two events could potentially have huge consequences for credit markets going forward.

## Credit Sector Movements

**Banking sector**—Following on from numerous government interventions, European banks spreads have tightened across the board as the credit risk continues to move into the real economy. The main beneficiaries were the UK banks, Barclays tightened 111bps to 141 and RBS tightened 98 to 195. The Irish banks spreads tightened noticeably also, AIB is now trading at 119bps, compared with levels greater than 300 bps in recent weeks. US banks spreads are wider, Morgan Stanley is now trading at 1240bps, over 250 bps wider on the week.

## Interest Rate Outlook

A co-ordinated move by six Central Banks helped to support the market on Wednesday and estimates for all major economies are now changing downwards after the co-ordinated move. The rate cuts haven't helped improve liquidity in the market and banks are still trying to obtain funds in wholesale markets. The rate cut had no effect on 3-month EURIBOR, which remains at elevated levels at the end of the week with the same been true for USD and GBP interest rates. Further aggressive rate cuts are now certain in the UK and Euro-Zone and the US with targets for Euro-Zone and UK interest rates below 3.00% by the end of 2009.

## Currency Comment

### EUR/GBP

As with all currencies last week saw large volatility in EUR/GBP due to the uncertainty in the market. The week saw bailouts of UK banks plus co-ordinated interest rate cuts from all major Central Banks. UK Economic data is light in numbers, but heavy in importance this week, Monday has PPI figures with a fall off expected as economic activity slows and input prices decrease. Tuesday sees CPI figures for September released and an increase to 4.9% should be the peak for UK inflation and on Wednesday unemployment figures are due for releases and should show the weakening economy translating into job losses. The currency pair will remain volatile with further pressure to come onto GBP as the data continues to disappoint.

### EUR/USD

The dollar rally continued last week with economic fundamentals been ignored as investors seek safe heavens. Key data this week in the US will be Retail sales for September on Wednesday followed by the Fed Beige Book later in the day. The housing market will be in focus on Friday with Housing starts released and consumer confidence numbers are released on the same day by the University of Michigan. The dollar will retain its momentum this week as the uncertainty continues in the world economy.



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## DOLMEN SECURITIES LTD

75 St. Stephen's Green, Dublin 2, Ireland. Tel : +353 1 633 3800/1890 400 300  
45 South Mall, Cork, Ireland Tel : +353 21 422 2122  
Theatre Court, Mallow St, Limerick, Ireland. Tel : +353 61 436 500

E-mail: [info@dsl.ie](mailto:info@dsl.ie)  
E-mail: [cork@dsl.ie](mailto:cork@dsl.ie)  
E-mail: [Limerick@dsl.ie](mailto:Limerick@dsl.ie)