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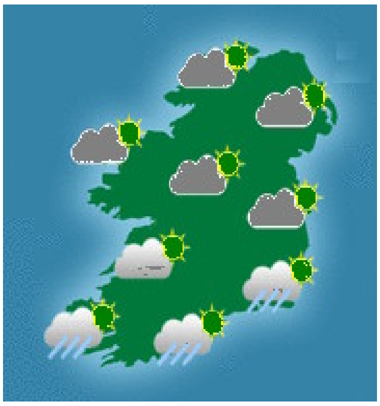
The Angle

Issue 5 – June 10 2008

Rainy Season



It's been a fairly rough year to date for economies, housing markets, investors, banks, businesses and governments across most of the globe. There are signs that perhaps the worst of the credit crunch is over, but with continuing sub-prime write offs and record high interbank lending rates, there would appear to be some more time left to run on this rainy season.

In parallel to a world wide credit shortage, the Irish housing market continues to stall. Unfortunately for those looking to buy, lending institutions continue to charge every increasing mortgage rates and are applying stronger underwriting criteria, making it more difficult to get mortgage approval. This lack of credit is also impacting some commercial activities, where companies are trying to fund growth.

On a global scale, commodity prices have raised based on rising demand and speculation. Both food prices and energy prices are on the rise. Herein lays the primary concern for central banks. If they lower interest rates, this may have the effect of increasing commodity prices even further. This inflationary impact would be counterproductive to any interest rate decreases. The term "stagflation" is now being coined to explain this potential economic state. A stagnation in economic growth coupled with a growing rate of inflation.

The ECB has always held the view that they would weather the storm and that knee jerk rate cuts would be counterproductive in the longer term. The US Federal reserve lowered its base rate in response to fears that the US financial market could implode if they did not take emergency actions. The Bank of England appears to have taken a middle of the road approach, trying to balance housing market concerns, inflationary fears and a slowing UK economy.

They say time heals all wounds. One would hope that credit markets return to a more normal state in the second half of this year. If equity markets show some sustained growth, speculators may cross over from commodities and release some of the current price pressures.

Unfortunately, central bank lending rates are not likely to lower anytime soon. There is now the potential (65% chance) of a 0.25% ECB rate increase as early as next month, as announced by the king of "Medium term price stability" - ECB president Jean-Claude Trichet on June 5th. This is not a welcome development for those looking for an economic stimulus; with inter bank lending rates already at record highs.

For those investors looking at long term investment planning, global equity markets may appear to offer value at present, however it will probably be 2009 before sustained growth in markets can be expected. The expectation still remains that emerging economies will continue to grow and may still offer the best medium term outlook. Those economies exporting Oil (Russia and Middle East countries) will continue to reap the benefits of current record prices, albeit based on a weakening dollar.

Equities –

If you consider all that has occurred in 2008 and all of the recent economic turmoil, it could be argued that most primary markets are holding up reasonably well.

When one considers the virtual collapse of the US investment bank, Bear Stearns in March and the continued troubles for both the US economy and US housing sector, a local currency decline of just -6.2% for the S&P 500 year to date is not as bad as one might expect. Assuming of course we are at the bottom of the cycle. I would see the S&P 500 offering a recovery potential in 2nd half of the year.

Japanese returns are also just under a 6% decline year to date. But many of the credit issues effecting US and European markets have not had much impact on the Japanese economy, which still remains in a dormant phase. The Bank of Japan key interest rate remains at 0.5%, imagine the run on investments and lending if that was the ECB base rate! There have been high levels of foreign capital inflows into the Japanese economy over the last number of months and the Nikeii may now finally be showing signs that it has the potential to outperform western markets.

2008 YTD Equity Market Performance

(June 4th)

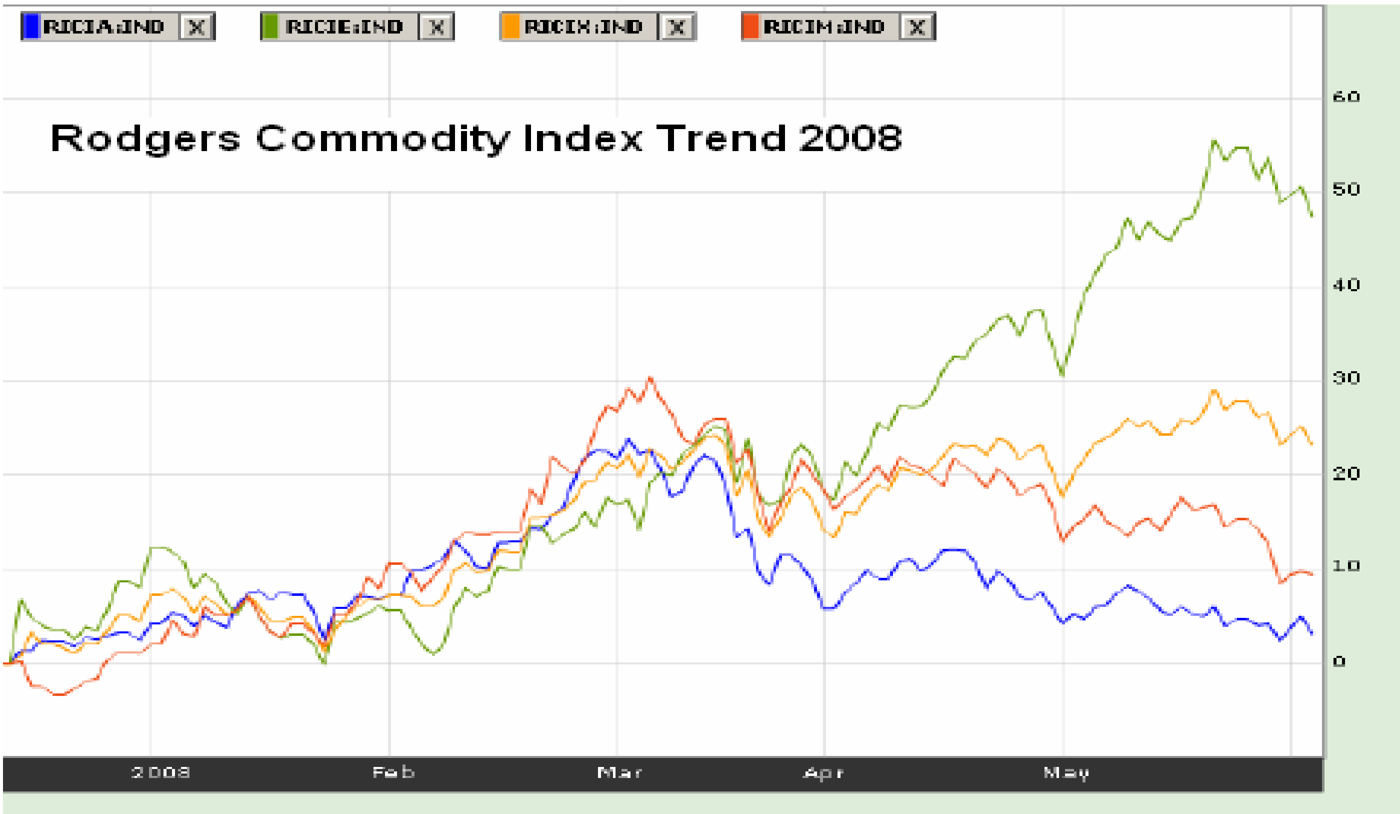
Market	Index	LC return %	Euro return %
Latin America	S&P Lac 40	11.5%	6.3%
Russia	RTSI	2.5%	-2.7%
Japan	Nikeii	-5.7%	-6.1%
US	S&P 500	-6.2%	-11.4%
UK	FTSE 100	-7.5%	-14.5%
Asia	MSCI Asia Ex Japan	-8.4%	-13.7%
Australia	S&P/ ASX 200	-11.9%	-9.1%
Hong Kong	Hang Seng	-12.7%	-18.0%
Europe	FTSE Euro Plus	-13.3%	-13.3%
Germany	DAX	-13.4%	-13.4%
Ireland	ISEQ	-14.6%	-14.6%
India	Sensex	-21.5%	-34.5%
China	Shanghai Composite	-34.8%	-35.1%
Global	S&P 1200	-4.7%	-9.9%

It is interesting to note that the markets which showed the highest gains over the last couple of years are now demonstrating the highest year to date falls. Relative volatility measured against more established markets, is one of the main characteristics of emerging markets. Both Chinese and Indian markets have showed large year to date price declines. But if one expects a global equities bounce back, here is where the greatest bounce could be achieved. Chinese GDP is still expected to hit 9.6% for 2008 and India's GDP to grow by about 8% in 2008.

I also feel that US markets may end the year higher than European markets as the US Federal reserve are demonstrating a far more aggressive approach in stimulating economic activity that the ECB. The USD will continue to weaken against the Euro, but should not weaken too much further this year.

Commodities –

The growth trend in commodities continues upwards as expected, however the increase in the price of crude oil and oil derivatives, has taken many by surprise. Energy commodity prices are up almost 40% year to date, with both agricultural commodities (+2%) and metals (+9%) showing more moderate levels of price inflation.



The price of oil has a direct impact on the global economy, as it directly impacts general price inflation and in turn the decisions taken by central banks when setting interest rates. There are many commentators holding the view that the natural price of oil should be around $110 a barrel. On the other hand, global demand is on an upward trend and the market has seen speculators buying oil in the belief that prices will continue to increase short term. I would hold the former view that prices will lower in the second half of the year lowering to between $100 and $110 a barrel, which should in turn feed positively into markets, particularly airline stocks.

Property –

Ireland –

Residential – According to the May PTSB/ESRI index house prices declined by an average of -2.2% over the 1st quarter of 2008. Although the index indicates a continuing softening in prices, there is a slowdown in the rate of decline. In quarter 4 2007 the decline was -3.9%. Given the time lag of at least 3 months on this index, the index will continue to report price declines through quarter 2. The index is down -9.5% since Jan 2007, which would indicate that the index has still some catch up to get to the widely accepted house price decline of approx 15% over the last 18months. The index should start bottoming out over the summer months and we may even see some price increases in the autumn buying season.

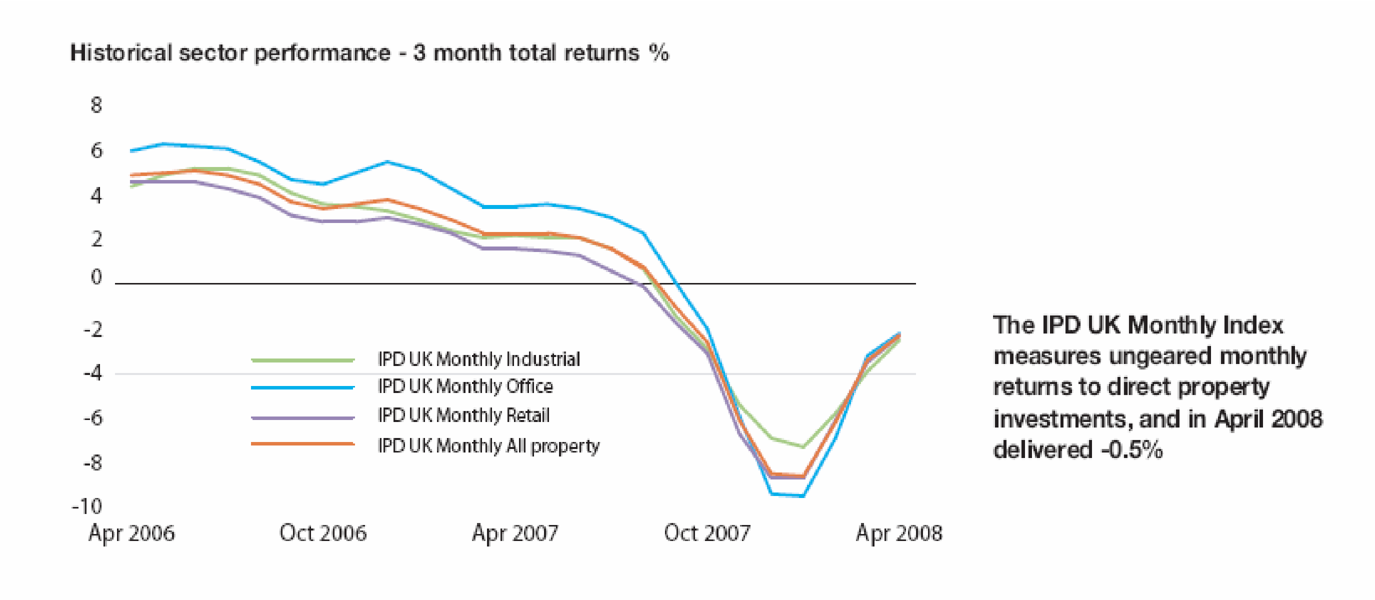
Regardless of residential prices, the level of activity in the residential market remains very low. With ECB rates now stuck or potentially going higher and a lack of cheap credit for those seeking mortgages, I can not see any pick up in activity levels in 2008.

Commercial – According to the SCS / IPD property index; the quarter 1 2008 total return for Irish commercial property was -2.3%. Capital values reduced by -3.3%. I see this price decline likely to continue with further weakening in rental growth, as the slowdown in the Irish economy impacts the level of achievable rents. 2008 is likely to see a total negative return on Irish commercial property.

UK –

Residential – The May Halifax House Price Index showed UK house prices fell by -2.5% in March, by -1.3% in April and -2.4% in May. These are significant price declines, with prices now approaching September 2006 levels. The Bank Of England seems to be focused on the inflationary pressures in the UK economy, with no sign of an immediate rate reduction at present. Retail Banks are not lending as much and have pulled many mortgage products from the market. Many first time buyers just cannot get a mortgage at present. The fundamentals for the UK housing market remain strong in the medium to long term, however fears over the UK economy sliping into a recesssion and a lack of available credit will see prices remain under pressure through 2008.

UK – Commercial – The most recently published IPD UK commercial property index shows the monthly April total return for all commercial property was down -0.5% (capital growth down -1.0%). Quarter 1 returns were down -3.3% (capital growth down -4.6%). There has been an approving price trend since the index bottomed out in December 2007. I would rate UK primary commercial property, which has strong lease terms, strong tenants and a good location as a **BUY** at present. We still have some availability in the **Santander House** property located in the city of London, which will close in a couple of week's time. We have a brochure of this product on the website, on the commercial property page.



My **"Angle" portfolio** is **down -8.4%** year to date in Euro terms. Although the mid year return is in negative territory, it is still ahead of the **S&P Global index** which is **down -9.9%** in Euro terms.

My Irish stocks pick performance is as follows; IAWS +8.17% CRH -5.8% and Anglo -30.65%. I will still keep these stocks in the portfolio, Anglo is being battered like most financials, but I still feel it has potential to regain lost ground in the 2nd half.

Here is how each asset class returned within the portfolio

Equities	-13.3%
Property	-10.3%
Commodities	+13.1%
Total	-8.4%

2008 starting base portfolio value was €50,150 all bought in Jan 1. Value June 5th €45,926.

My reset "Angle" investment portfolio (*__not__ necessarily yours)*

Equities – **65%** **5% Ire** (Stocks IAWS, Anglo, CRH) **| 5% Germany** (Dax) **10% Europe ex UK** (FTSE Euro+) **| 10% Asia Pacific** (MSCI Asia ex Japan) **| 5% Japan Nikeii | 10% India** (Sensex) **10% Latin America** (S&P LAC40) **| 10% US** S&P 500

Property – **25%** **15% UK Commercial** (IPD) **| 5% Euro Property** (*EPRA Index) **5% Asian property** (*TSE REIT Index)

Commodities - 10% **5% Uranium** (Cameco) **| 5% Commodity Index** (RICIX)

Note: I have reset investment split on percentages outlined above. I have brought Japan and US equities into portfolio for first time this year. I have increased weightings in India and Latin America, with reducing holdings in Germany and Asia. I have increased exposure to UK commercial property index by reducing holdings in Asia and Europe REIT indices. I have reduced holdings in Commodity index, with my belief that the oil run is over for 2008.

**** Both the EPRA and TSE REIT indices are based on companies exposed to property assets. Direct property investment should be viewed as long term and will differ from the indices used in this portfolio.***

By Morton Rennick – ACMA QFA
