MARKET UPDATE

Equity Review Outlook

- June was relatively a quiet month as it coincided with the 2006 FIFA World Cup that kicked off in the second week. Volume traded fell 35% from a 3 month average of RM1.2 bn. During the month, the KLCI index fell by 1.41% along with the MSCI Asia Ex Japan index that fell by 0.61%. The newly launched FTSE Emas index fell by 1% on the first week of its debut to close at 5994.29 points. Overall, market sentiment remained sombre as investors were concerned over rising prices and slowing global economy that may curtail corporate profit growth going forward. Meanwhile, the lifting of the designation of Iris Corp has helped to re ignite some interests in the second and third liner stocks.

- We saw the tail end of the first quarter result announcements. Astro surprised the market with better than expected first quarter earnings. Stronger performance was attributed to lower losses in Celestial Pictures, tighter cost control as well as higher than expected advertising and subscription revenue growth. Meanwhile, Tanjong Plc's 1st quarter earnings were in line with street estimates. Although the group's gaming division reported higher than expected price payout, it was mitigated by narrower losses from Tropical Island, lower effective tax and investment gains from the disposal of its LPG division.

- M&A talks once again stole the limelight in the corporate scene with the resignation of Sulaiman Abdul Rahman Taib as chairman of RHB. It was subsequently reported that EPF had offered to buy Utama Banking Group's 32% stake in the company but the purchase price was not disclosed. This move could be a precursor to another round of merger and acquisition in the domestic banking industry. In a nutshell, investors were generally positive on this development, as it would pave a way for the long awaited group-wide restructuring and re-rating of the stock.

- On a separate note, Transmile Group entered into a strategic alliance with DHL International to tap on the fast growing overnight air express business in Asia Pacific. The move was seen as a "win-win" situation with Transmile being able to leverage on the DHL international brand name and extensive network while DHL would be able to grow their Asian operations through Transmile's traffic rights and low operating costs.

- On the economic front, the second quarter GDP grew at 5.3% y-o-y up 0.1% from the preceding quarter while inflation rose 3.9% in May from 4.6% in April. For the whole of 2006, we expect GDP to grow by 5.4% and inflation to peak at 4% due to higher energy costs following the 12% tariff hike imposed by Tenaga.

- In the US FOMC meeting on 29th June, FED announced the widely anticipated 25 bps hike. During the meeting, FED also indicated that it did not have a clear idea as to what the next policy move would be because the central bank was not certain whether the weakness in the economy would continue or if inflation would continue to drift upwards. While the marketplace has priced in another 25 bps rate hike in the August meeting, FED's less hawkish statement could signal an end to its policy tightening cycle.

- In terms of investment strategy, we had decided to raise cash levels to try preserve the capital of the Funds. We are adopting a more defensive approach either through holding more cash or in more dividend yielding stocks.

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MARKET UPDATE

Fixed Income Review Outlook

- In US, the FOMC raised its target fed funds rate by 25bps for the seventeenth consecutive time to 5.25% on 29 June 2006. From the FOMC statement issued, investors raised the odds that the Fed may be prepared to pause soon, although things remain data-dependent as ever. On the economic front, the May CPI came in as expected at 0.4% mom, which is lower than 0.6% mom registered in April. Sales of existing homes fell 1.2% mom in May to the slowest pace in four months as higher interest rates dampened buying activity. 1Q GDP reading came in largely within expectations at 5.6%. This is supportive for a halt in the monetary tightening regime, yet the stubbornly high oil prices remain a major threat to inflationary risks. International crude oil prices were hovering at USD70/barrel for most of the month and rose up to USD73/barrel towards month end due to escalating risks in Iran. The US Treasuries yield curve flattened during the month where the short end went up in tandem with the Fed Fund Rate hike. The 2, 5 and 10-year UST ended at 5.15% (+12bps), 5.09% (+6bps) and 5.14% (+2bps) respectively.

- The RM bond market was relatively quiet as there was no Bank Negara Monetary Policy meeting in June and the kick off in World Cup 2006 in Germany. May CPI came in favorably at 3.9% yoy (4.6% in April) due to softer transport costs and lower telecommunication charges. However, the June CPI is expected to back up to the region of 4% due to the flow through effect of the electricity tariff hike in June. Economic growth was resilient with 2nd quarter GDP at 5.30%yoy.

- During the month, Ringgit continued its depreciating trend against the US Dollar since the emerging market sell off in May. The Ringgit was traded at a low of 3.687 in June compared to 3.576 in May. The Ringgit strengthened slightly towards the end of month after the FFR hike in US, as the market is expecting Bank Negara to follow Fed's footstep in their next MPR meeting in July 29. The 3, 5 and 10-year MGS ended at 4.48% (+12bps), 4.57% (+7bps) and 5.08% (+19bps).

- Bank Negara has announced a re-opening of a RM3 billion 10-year MGS, where the size of issuance is at the high end of the market expected range. The 10-year MGS was issued at 5.108% and drew a strong bid-to-cover of 2.69 times. On the PDS side, there were a few primary issuances namely the Sabah Development Bank, Tabreed US Dollar denominated bonds and UEM Builder. Independent Power Producer (IPP) bonds were in the limelight during the month as a result of the possible re-negotiation of a new IPP pact, which could involve the postponement of the start-up of future completed power plant projects. During the month, RAM has revised Lingui's outlook from A2 stable to negative due to its poor financial performance while the long-term ratings of Ambang Sentosa was also downgraded from BBB to C by MARC.

- In July, the RM bond market will continue to take the lead from the US treasuries and Fed outlook. We expect the market to be more active after the World Cup finals. We believe Bank Negara is likely to raise the OPR in the July monetary policy meeting to close the gap with US rates and tame medium term inflation outlook. There will be two new government issues namely a 5-year GII and 3-year MGS reopening in July which could put some pressure on MGS yields. In terms of strategy, we would remain cautious with short duration. However, we are seeing some value emerging as bond yields are re-priced higher.

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