

BLACKROCK MERRILL LYNCH INVESTMENT MANAGERS

Week in View

Market Review

Despite **US equities posting modest gains** over the week, June proved a difficult month, with indices recording their worst monthly performance since February. The broad S&P 500 index ended June 1.8% lower, despite setting a record close early in the month, as investors digested concerns ranging from inflation to changing expectations of US Federal Reserve monetary policy and fears that leveraged buy-out activity will dry up. Technology sectors showed a certain amount of resilience last week, helping the Nasdaq index to a gain of 0.6%.

Market Movements

Markets	29 Jun 2007	% Change
S&P 500	1503.35	0.05
NASDAQ	2603.23	0.55
TSE 1 st Section	1774.88	-0.17
FTSE/S&P World Europe	452.75	0.39
FTSE All-Share	3404.14	0.41
DAX	8007.32	0.73
Hang Seng	21772.73	-1.03
Citi World Govt Bond Index		
All Mats	484.61	0.42
Bonds*	29 Jun 2007	22 Jun 2007
US	5.03	5.14
Japan	1.87	1.89
Germany	4.57	4.66
UK	5.46	5.52
Currencies	29 Jun 2007	22 Jun 2007
USD/Euro	1.35	1.34
GBP/Euro	0.67	0.67
JPY/USD	123.50	124.09
USD/GBP	2.01	2.00
JPY/GBP	247.77	247.64
Commodities	29 Jun 2007	% Change
Oil (Brent Crude)	72.67	0.32
Commodity Futures (CRB) Index	410.36	0.48
Gold	650.45	-0.39

Mixed economic data and the failure of export stocks to fully recover from strength shown by the yen at the start of the week saw **Japanese stocks end lower**. The currency found support as Finance Minister Koji Omi highlighted the risk involved in carry trades, where investors sell low-yielding currencies, like the yen, to buy higher-yielding assets.

European bourses saw positive performance as M&A activity continued to distance markets from the uncertainty faced by financial stocks in the US. Germany's Dax ended 0.7% higher, while the French CAC-40 gained by 0.5%. Meanwhile, **UK share prices fought**

back from a difficult start to end the week stronger; the FTSE 100 recording 0.6% gains.

Asia-Pacific share prices ended lower last week, as US and Chinese market themes blended to force markets down. Having traded a narrow range, Hong Kong's Hang Seng ended with declines of 1.0%, falling late on Friday ahead of today's public holiday.

Emerging markets saw mixed performance. In Latin America, Brazil's Bovespa gained by 0.2%, while Mexico's Bolsa fell by 1.6%. In emerging Europe, Russia's RTS index ended up 0.1%; a stronger oil price having limited effect on the energy-dominated market.

The Fed left **US interest rates unchanged** at 5.25%, as expected, maintaining its stance on inflation, though modifying its language to state that a "moderation in inflation pressures has yet to be convincingly demonstrated". The yield curve flattened modestly and **bonds sold off, though performance was later recouped** on slightly weaker-than-expected Personal Income data, released on Friday.

The **yen modestly strengthened** versus the US dollar, but stayed within range with most market participants focusing on the fact that the yen was heading for its largest quarterly loss since 2001. Sterling, however, broke the US\$2 level at market close for the first time since April. The renewed **bout of dollar weakness** has been prompted by indications that inflation is falling, the Fed's statement notwithstanding.

A surprise drop in gasoline inventories had **oil prices on the rise**, with traders concerned about supplies during the summer driving season in the US.

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Comment

US rates on hold, but possibility of reduction remains

The Fed left interest-rate policy on hold last week, as expected by most observers.

The accompanying statement acknowledged that core inflation pressures have eased somewhat and that economic growth has continued to slow, however, as detailed earlier, the language was amended to state that a "moderation in inflation pressures has yet to be convincingly demonstrated".

Looking forward, we continue to believe that the Fed will enact a rate cut before the end of this year or, if not, by early next year, given well behaved inflation and the continued likelihood of below-trend economic growth.

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