

Base Rate Cut Not Enough?

Bhavin Dhanani

The Bank of England has slashed the UK base rate from 4.5% to 3%. The 150 basis point cut is the biggest the UK central bank has ever made. The last time rates were cut to such an extent was in 1981, prior to the Bank of England receiving its independence.

The interest rate is now at its lowest point since 1955. The bold move is a clear indication that the key problem for the UK economy is recession, rather than inflation. Business bodies welcomed the move but the reaction on the stock market was not as good. The leading index, the FTSE 100, ended Thursday down 255 points or 5.6% despite a brief rally after the

news was made official. There is anxiety amongst investors that the rate cut is simply another indicator of the severity of the impending recession.

Retail banks are now under pressure to cut the interest rate on mortgages. Gordon Brown has requested the cut is reflected in all variable mortgage products.

Homeowners with tracker mortgages automatically benefit from having mortgages linked to the base rate. However those on variable rate mortgages may not experience the full rate cut. Standard variable rate mortgage holders of Halifax Bank of Scotland, Lloyds TSB, Royal Bank of Scotland, Abbey and Nationwide are

all set to benefit after these financial institutions promised to pass on the rate cut. HSBC and Barclays are reviewing whether to pass on the rate cut.

The rate cut spelt bad news for savers. Most fixed rate products have now been either withdrawn or the return has significantly fallen.

The European Central Bank also met this week to discuss interest rates. In a move that was not as bold as the Bank of England's, rates were cut a moderate 0.5% to 3.25%.



News from the Bank of England this week saw the base interest rate for the United Kingdom cut by 1.5%

More RBS Debt and Shares

Sarah Lloyd

Following on from the Government's 400 billion pound bail out plan, the Royal Bank of Scotland has been under pressure to source new capital.

RBS delayed issuance of its prospectus for £20bn of capital in October, allegedly in order to benefit from new accounting standards.

As such, the prospectus was released last Wednesday. It discusses the issue of new ordinary and preference shares. The total amount to be raised is £19.7bn net of expenses.

Analysts believe RBS will have a tough job persuading investors to purchase ordinary shares which may otherwise be purchased by the Government who are acting as underwriter.

RBS isn't the only institution struggling to raise capital. Hedge funds are facing problems as investors demand cash and lenders squeeze funding.

Described as the worst crisis to hit the hedge fund sector in more than a decade, many hedge funds are expected to disappear. Man Group, the world's largest listed hedge fund lost a third of its value this week as shares fell on the announcement of a drop in funds of 1.7 billion pounds.

The Goldman Sachs Investment Partners fund, launched at the beginning of the year, has experienced a 15.5% drop in performance since its launch. Analysts predict the industry will shrink by a third with many fund managers having to provide lenders with significantly higher collateral.

Markets

- The FTSE 100 closed this week up 1.51% at 4449.52. This was despite rate cuts around the world. The UK index is still down over a quarter on the year.
- Wednesday sees the release of both the Bank of England's Inflation index for the Month of October and the release of the latest figures for unemployment in the UK.
- Friday also sees the release of two important indices. The European Gross Domestic product figures are to be released, as are the European figures for the Consumer Price Index.

Winners, Losers

Company	Price	Change
International Power (power)	283.75p	20.49%
M & S (retail)	266.00p	20.09%
Tate & Lyle (commodities)	428.00p	18.81%
Legal & GNRL (insurance)	85.20p	18.33%
Vedanta Res (commodities)	831.50p	-8.83%
Std Chartered (banking)	911.50p	-9.21%
3i Group (insurance)	489.50p	-14.42%
Man Group (hedge fund)	282.50p	-21.69%

Hedge Funds

The Hedge Fund business worldwide is worth an estimated \$1.7 trillion but their business, despite being so profitable, is currently the bane of many blue chip companies.

An industry that profits from shorting stocks in order to buy them back at a lower price in the future is being squeezed itself. As the world's securities fall in value, collateral calls are increasing on assets held by Hedge funds.

To meet the calls, funds are being forced to sell other assets. Funds have also been exposed to poor market perception. As a result, in some cases, up to 25% of various hedge funds' assets have been requested to be liquidated by investors. Redemptions are pushing funds towards more liquid and less profitable securities to meet their obligations to the investor. The recent ban on short selling has meant many funds have found capital hard and expensive to come by.

While many CEOs, including the vocal John Mack of Morgan Stanley, have publically criticized the hedge funds' strategy of short selling, they may yet come to rue their words. Hedge Funds are now selling billions of dollars worth of securities. These fire sales are widely blamed for the decrease in world markets' especially at the tail end of last week.

Last month saw declines in the Hedge fund industry reach 5.4% on top of year losses of over 15%.

Interest rates not cut but slashed by Bank of England!

The BoE is seen to have taken decisive action by not concentrating on the level of rate cuts, but by deciding on a level appropriate for the times. With US rates at 1% and EU rates at 3.75%, has the UK taken the initiative again in world economics?

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Sources: www.theft.com, www.reuters.com, www.economist.com, www.timesonline.com, www.bbc.co.uk, www.yahoofinance.com, www.bloomberg.com

Jobs Tumbling Amid Turmoil

Sarah Lloyd

With the US economy witnessing unemployment rates at a 14-year high, banks such as Goldman Sachs and Citigroup are faced with a weakening economy and mounting potential losses.

Goldman Sachs, the leader on Wall Street and the firm thought most likely to survive the current financial crisis, is cutting 10 per cent of its workforce—or 3200 jobs. Analysts suggest that the fact that Goldman is cutting now, when it did not do so earlier, is an indication that the firm is becoming more pessimistic about

the coming year.

Citigroup has been notifying staff that the bank's plans to discard 9,100 positions over the next 12 months—or 2.6 percent of its headcount.

These job cuts come on top of tens of thousands of jobs already lost at Citi and the rest of Wall Street. The outlook for jobs on Wall Street is grim as Barclays expects to eliminate 3000 as it integrates the U.S. operations of Lehman Brothers and cuts of as much as 10,000 are expected when Merrill Lynch is fully acquired by Bank of America.

Strictly Bites

A sensational attempt by two ex-bank heads to take over the Halifax Bank of Scotland (HBOS) board has been rejected. Sir Peter Burt, former chief executive of Bank of Scotland and Sir George Mathewson, former boss of Royal Bank of Scotland, want to maintain the bank's independence.

The International Monetary Fund (IMF) has revised its growth figures for several of the world's economies. It is now estimating that the developed economies as a whole will contract by 0.3% in 2009. Other predictions include a contraction of 1.3% in the UK, 0.8% in Germany, and 0.7% in the US. However with the help of emerging powerhouses such as China, India and Russia, the world economy is estimated to grow by 2.2%.

The US Treasury has announced plans to sell bonds to finance the \$700 billion bank bailout scheme. By the end of 2008 they expect to raise \$550 billion. This week a \$55 billion debt issue will take place. \$30 billion of this will be through Treasury bonds maturing in 10-30 years. \$25 billion will be raised through a new bond type with three year maturities.

Christmas parties across many top tier financial institutions have been cancelled after the volatility in financial markets.

The IMF has approved a loan to Ukraine. The Eastern European nation has been hurt by a fall in demand for steel, its main export. The loan is worth \$16.4 billion. The IMF anticipates that the Ukrainian economy will shrink by 3% next year.

Official figures from the US show that the official rate of unemployment stood at 6.5% in October, a 14 year peak. 240,000 jobs were lost bringing the number of those who have lost their jobs to 1.2 million in 2008.

A report by the Centre for Economics and Business Research has argued the Chancellor should cut VAT to 12.5% for a short period. This will aid the economy through a recession.

Berkshire Hathaway, the insurance company owned Warren Buffet, has said that its third quarter net earnings plunged 77%. The fall in profit was attributed to a drop in insurance underwriting profits, and heavy losses on the value of investments.

France's largest bank, BNP Paribas, saw third quarter profits fall by 56%. The collapse of Lehman Brothers and the nationalisation of the Icelandic banking sector meant loan loss provisions increased from €462 million to €1.99 billion.

Sources: www.theft.com, www.reuters.com, www.economist.com, www.timesonline.com, www.bbc.co.uk, www.yahoofinance.com, www.bloomberg.com