

TARP and TALF Changed

Pearl Boateng

US Treasury Secretary Timothy Geithner has announced major changes to the Troubled Asset Relief Plan (TARP) this week. Following criticism from watchdogs of the original allocation of TARP funds, new proposals regarding tax cuts, job opportunities, increased spending on infrastructure and limits on bankers' bonuses have been implemented.

Current changes to TARP (\$787bn/£548bn) propose the following. The creation of a public-private investment fund of between \$500bn and \$1 trillion that will enable retail banks to offload their mortgage backed securities. A \$500,000 (£355,000) cap has been placed on executive bonus pay. Calls for a single

government body e.g. the Federal Deposit Insurance Corporation (FDIC) to regulate the banking sector and prevent further bank collapses and the need for emergency bail-outs such as that of the Lehman Brothers and AIG. An existing scheme, the Term Asset Backed Securities Loan Facility (TALF) will also receive extra funding to help expand the availability of consumer credit. TALF will now employ new standards of loan modification thus making it easier for the public to borrow money, especially for student loans and mortgages. The FED, US central bank as well as the Treasury could potentially chair this scheme. Other TARP changes include

heavy income tax cuts for individuals (approximately 36% of the plan), less funding to states, as well as \$46bn dedicated to boosting spending in the housing and automobile markets.

With US interests rates already approaching zero, the budget deficit reaching record levels and the bulk of the funds scheduled to be spent in 2010, the effectiveness of the new TARP depends greatly on the actions of individuals and government officials within the world's largest economy.



Chief Executives of eight US banks were required to explain their use of bailout cash.

Dark Days for the UK Economy

Bradley Wright

Markets

- This week sees the Bank of England Interest Rate meeting minutes released. An indication of how the board voted will yield answers as to whether they believe the UK economy is approaching equilibrium.
- The state of public sector finances is also released this week.
- Retail, internet and high street sales figures are to be released Friday. Despite the "credit crunch", internet sales are widely expected to rise.

Winners, Losers

Company	Price	Change
Randgold (resources)	3321.0p	9.28%
Lonmin (resources)	1131.0p	8.75%
Smith Nephew (medical)	552.50p	8.12%
Fresnillo (resources)	393.25p	7.96%
Prudential (insurance)	306.00p	-18.24%
Avivia (insurance)	328.25p	-18.80%
Legal & GNRL (insurance)	46.00p	-28.12%
Lloyds (banking)	58.50p	-41.79%

Britain is in a 'deep recession' according to the chairman of the Bank of England. Mervyn King issued some stark warnings on Wednesday, causing the FTSE to enter freefall.

The MPC's quarterly inflation report produced some worrying results. The economy would shrink by at least 3.5 per cent in '09, with only minimal growth (0.9%) forecast for 2010. This is in contrast to the Treasury's own report which predicted a 1.25 per cent fall in the UK's output and a 1.75% forecast for growth in 2010.

The Treasury's report increased market volatility, with the pound dropping and bond yields tumbling. Ten year gilts fell a quarter of a point to 3.4%, their biggest single day fall in over a decade. Unemployment was again up, rising to 1.97 mil-

lion in the three months to December and it is expected the first quarter of 2009 will see this number reach 2.25 million.

King has announced some quite drastic measures to try and combat the downturn. It seems the bank has thrown out its orthodox method - that of J M Keynes (using interest rates to stimulate growth) - and is now adopting a new, and essentially untried, method of stimulating an economy. This method, quantitative easing, involves the central bank 'printing' money to buy assets within the economy. This will not increase the amount of cash in the UK but create much capital, which can be spent by the BoE on government bonds or currency. This should direct cash into the bank accounts of those holding the assets.

The consequences of the current Interest rate lows

The role of a credit rating agency is to rate how credit worthy a company is, i.e. what is the likelihood that a company will default on their debt. There are three big players in this field, Standard and Poor's (S&P), Moody's and Fitch Ratings.

Credit rating agencies use specific company financials and ratios to deduce their ratings. These ratios include profitability ratios, liquidity ratios, leverage ratios and interest rate coverage ratios. Furthermore, it is of great importance to look at the macroeconomic conditions in markets where the company operates as well as the industry.

The big three agencies rate their bonds slightly differently. However, the most creditworthy companies are given an AAA rating and the least creditworthy companies are given a D by Fitch and S&P, and a C by Moody's. A bond rated BBB or Baa and above is classified as investment grade. Anything below these ratings is classified as junk or high yield investments.

The rating which a company receives has a big impact on their bond prices and yields. If a company is downgraded the spread over a risk free government bond increases and due to the inverse relationship between yields and prices, the bond price would decrease. The opposite would apply in the case of an upgrade. The reliance markets offer these ratings stem from the amount of company information these firms have access to.

G7 Commits to Open Markets

During the two day discussions finance ministers met to talk about maintaining financial stability, the US package capping bankers' bonuses to one third of pay and, most importantly, their commitment to retain global market openness to avoid exacerbating the fragile world economy after the US and Chinas' protectionist strategies...

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Swiss Banks Hit Hard

Sunny Shah

Europe's biggest casualty of the credit crisis, UBS, announced last week that it has lost nearly SFr20bn (\$17bn) in 2008. A statement said the bank would axe a further 1,500-2,000 investment banking jobs, bringing its workforce to 15,000, about one third less than a peak of almost 23,000 attained during the credit boom. Switzerland's largest bank still intends to retain its commitment and presence in the investment banking market despite reporting the biggest loss in Swiss corporate history. They hope this arm will still be profitable by the end of the year.

Another Swiss Group, Credit Suisse, declared that it had lost a net SFr8.22bn (\$7.12bn) on write-downs and punishing trading conditions, as well as weakness in its asset management arm. Chief Executive Brady Dougan said the group has had a strong start to 2009 and was profitable across all divisions year to date.

In the UK, investor confidence in Lloyds Banking Group was shaken further last week after it warned that the newly acquired HBOS had suffered a worse-than-expected £10bn loss in 2008, triggering a share price collapse for the combined bank.

Strictly Bites

Eurozone Gross Domestic Product fell 1.5 per cent in the fourth quarter, led by a dramatic deterioration in the German economy. As a result, the Eurozone faces its worst recession in 50 years.

Newly acquired Halifax Bank of Scotland suffered a much worse-than-expected £10 billion loss in 2008. This caused a loss of investor confidence and a share price collapse for the combined bank, Lloyds Banking Group.

Fortis' holding shareholders voted against carving up the company and selling a part to BNP Paribas. As a result, Fortis Bank is now considering a stand-alone option paper to remain as Belgium's largest bank.

The attorney general of North Carolina, the home state of Bank of America, has questioned the payment of 2008 bonuses and asked the bank for justification given that it has received \$45 billion of taxpayer money.

Concerns about the health of the banking sector offset the optimism surrounding Obama's expected economic stimulus package and caused volatile trading in U.S. stock markets on Friday.

UK lawyers have criticised a banking bill aimed at staving off future bank crises. Lawyers claim the bill gives authorities too wide a scope for intervention, dubbing one of the clauses the "Henry VIII clause" due to the power given.

Further policy steps are being taken by the Bank of Japan to ease the corporate financing squeeze. The BoJ may extend its purchasing of corporate debt for a further six months in order to help companies that have had difficulty raising cash.

The prospect of extraordinary measures undertaken by the BoE is placing strain on sterling. Wariness of the Bank's next policy steps—further interest rate cuts and/or quantitative easing—caused the sale of sterling.

France has become the first leading economy to impose bonus limits. Bonuses will be paid over several years and relate to long-term profitability.

Northern Rock shareholders failed in their compensation case to obtain damages for the loss of their holdings. The High Court disagreed with investors' argument that the government compensation scheme was a breach of human rights.