

\$700 Billion Finally Approved

Sarah Lloyd

After a week of held breath, the \$700bn bailout fund was finally approved by the House of Representatives on Friday by 263 to 171. The legislation was passed by the Senate on Wednesday (24/09), but the House of Representatives was warier due to the impending elections and resultant increased interest in the economy by voters.

The bill will allow the Treasury Department to purchase up to \$700bn of troubled mortgage-related assets from financial institutions. The requirements of the bill are that the Treasury Secretary aims to maximize returns for taxpayers, prevent further market disruptions and strive to ensure stability

in local communities.

Furthermore, the \$700bn rescue fund was accompanied by \$152bn in tax breaks and other tools to enable the federal regulators to deal with the growing economic crisis. Fears of a recession may have pushed the bill through the second time. The current situation also provided an opportunity for the tax breaks to be introduced as the pressure has been on for quick action.

Governor A. Schwarzenegger warned that the state of California may need an emergency federal loan of \$7bn within weeks as it is one of the states frozen out of the bond

market by the credit crunch. With states struggling to fund day-to-day government operations the rescue fund has become increasingly important.

The bill left many unhappy - some complained the tax breaks weren't offset, and others questioned the increased federal intervention in private markets. The split vote clearly demonstrated uncertainty on how best to proceed although the consensus was that something had to be done.



Investment banking may have finished on Wall Street but it has just received its biggest lifeline ever

B & B in National Hands

Bhavin Dhanani

The eighth biggest bank in the UK, Bradford and Bingley (B&B), has been taken over by the public sector. It is the second bank this year to be nationalised after Northern Rock suffered the same fate in February.

Under the deal, the Government will take control of the bank's loan portfolio which is currently valued at £50bn. The savings have been bought by Banco Santander. The Spanish bank's presence in the UK is strengthening. It already owns Abbey and recently agreed a deal to take over Alliance & Leicester.

B&B's business model has been under increased scrutiny by ana-

lysts. It specialises in buy-to-let mortgages which have seen an increased number of defaults recently. There was reassurance from the Treasury that savings were safe. However it looks as if shareholders will be the real losers of the deal. They are set to receive minimal compensation from the sale. Bond holders are also set to lose out.

The nationalisation marks the end of an era in the UK. Every building society that de-mutualised into a bank has either been taken over or failed. The UK banking market is now becoming more concentrated which many fear may lead to decreased competition.

Markets

- Thompson this week announced it was "recession proof" as people see holidays as a necessity now
- Supermarkets have increased marketing and product range in their own budget products amid the current turmoil
- Consumer luxury companies' share prices have started to tumble as investors feel there will be a spending cut-back. Apple's share price fell 18% despite favorable reviews regarding its new phone and i-pods
- CAI led by 16 Italian entrepreneurs will acquire Alitalia after the unions agreed to the deal

Winners, Losers

Company	Price	Change
HBOS (banking)	200.5p	18.7%
Lloyds TSB (banking)	290.25p	15.7%
Tesco (supermarket)	415.70p	12.1%
Morrison (supermarket)	269.00p	9.4%
Fresnillo (mining)	280.75p	-17.0%
Cairn Energy (fossil fuels)	1854p	-17.6%
Vedanta (mining)	1019p	-21.3%
Lonmin (mining)	1701p	-31.1%

Banking Models

Hype in the current market, when not focussed on the cost of MBSs, has been focussed on the various banking models.

Investment banking has apparently had its day (20 years) in the sun and it is time for another model to have a go. While both Goldman Sachs' CEO Lloyd Blankfein and Morgan Stanley's John Mack are adamant the model works if used responsibly, both banks changed their status last week. With higher margins, less regulation and reward for more risk, it is easy to see why the two banks wanted to retain their 'IB' status for as long as possible. The fact that both applied for holding bank status over the same weekend demonstrates that maybe they were pushed into their decision.

Morgan and Goldman, along with others, enjoyed public status over the good years as their share price soared and record dividends were paid by all. However, it was this same "Plc" status that triggered the banks' abandonment of their once cherished model of high leverage and returns. Market faith fled the industry after the high profile demise of first Bear Stearns, then Lehman Brothers and finally the fire sale of Merrill Lynch to Bank of America. With their share price tumbling and rumours abound of fundamental liquidity problems, both sought the shelter of commercial bank status and the deposits associated.

In 1929 after the Wall Street crash, the Glass-Steagall act was passed after the authorities concluded commercial banks engaging in stock market "activities" were risking depositors money. The act meant commercial banks could take deposits but not underwrite securities. Investment banks could underwrite but could not take deposits. The funding commercial banks thus signed up for came with the added supervision of the authorities. The Federal Reserve are allowed to, and do, place permanent personnel on banks' premises to supervise first-hand their operations.

Whether one system is better than the other remains to be seen. One given is that the large investment bank is 'dead' for now. If pressure on the 'universal' commercial banks resurfaces though they may be forced to spin-off their investment banking operations which may see IB as we knew it resurrected.

Were the House of Representatives and the Senate right to pass the new \$700billion bill?

What does the bill that has just been passed actually achieve? It gives banks that have caused the world economy to come to a near standstill large sums of money for what is in effect 'worthless assets'. No doubt something had to be done, but other options exist. An alternative and less risky method suggested was for the Federal Reserve to buy shares in any struggling banks both to bail them out and then reap the rewards when the crisis ended.

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mail@strictlyBIF.com

US Acquisitions Sky-Rocket

Sarah Lloyd

Wells Fargo, the San Francisco lender, announced on Monday that it plans to buy Wachovia for circa \$15.1 billion, in an all-stock deal, outbidding Citigroup. However, the Citigroup has demanded that Wachovia honour the alleged exclusive acquisition agreement, prohibiting Wachovia from entering into any negotiations other than with Citi.

Wachovia shareholders stand to receive 0.1991 shares of Wells Fargo per Wachovia share, thus

valuing Wachovia shares at \$7 each compared to their Thursday close of \$3.91. Wachovia shares stood at \$10 each on Friday 26 September before the Citigroup deal was announced.

The Wells Fargo offer was approved by the board Thursday but is still subject to Wachovia shareholder and regulatory approval.

JPM's government-backed bid for Washington Mutual, worth \$1.9 billion, went through this week.

Strictly Bites

Switzerland's largest bank, UBS, has cut 2000 jobs in its investment banking arm as part of a major restructuring programme. It will also end trading in commodities other than precious metals.

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The Financial Services Authority (FSA) has raised the savings guarantee from £35,000 to £50,000 per financial institution.

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The move by the FSA follows on from Ireland's decision to provide a 100% guarantee on all savings. This saw many transferring their balances to Irish institutions.

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German mortgage bank, Hypo Real Estate, is on the verge of failure. A planned €35bn government bailout collapsed after negotiations with financial institutions ended.

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Dexia received a major cash injection of €9.2bn from shareholders and the governments of France, Belgium and Luxembourg to restore confidence in the bank.

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Data shows that US banks borrowed a record \$367.8bn per day in the week ending October 1st.

The Belgian and Luxembourg governments, alongside the Dutch government, stepped in to throw a €11.2bn lifeline to Fortis after investor confidence dwindled.

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The European Central Bank decided to hold euro zone interest rates at 4.25% despite pressure for a cut to kick start the ailing euro zone economy.

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Data from the Office of National Statistics showed that the UK experienced no growth in the second quarter of 2008 fuelling rumours of a Bank of England interest rate cut next week.

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The collapse of Lehman Brothers was ultimately down to JP Morgan's decision to freeze \$17 bn of the Lehman's assets on the Friday before its collapse, according to Lehman's creditors. They say JP Morgan's actions sparked the liquidity crisis at Lehman that led to their eventual demise.

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Mitsubishi Bank is in talks with Morgan Stanley to take its Japanese prime brokerage arm. The Japanese bank already had a 21% stake in the Wall Street giant at close on Friday.

