

World Follows UK Initiative

Bhavin Dhanani

Banks in the UK and the US have received substantial funding from the governments of their home countries, in effect part nationalising them. In exchange the governments will receive perpetual preference shares in these banks.

On Monday, the UK Government announced that three banks, the Royal Bank of Scotland (RBS), Lloyds TSB and Halifax Bank of Scotland (HBOS), will be injected with a total of £37 billion. Of this, RBS will receive £20 billion giving the public a 60% stake in the battered bank. The public will also own 40% of the combined Lloyds TSB and HBOS. A key part of the plan is that directors will not receive

cash bonuses this year while future bonuses are to be paid in shares, aligning the interests of shareholders and managers.

The US government's \$700 billion plan has been reconfigured to involve, somewhat reluctantly, purchasing shares in nine major financial institutions and hundreds of community banks in a deal totalling \$250 billion. The banks that have signed up so far include Goldman Sachs, Morgan Stanley, Citigroup, JP Morgan and Bank of America. The US government will not take majority stakes in these banks with each bank eligible to receive a maximum of \$25 billion.

The Swiss government has injected SwFr6 billion

into UBS, the nation's largest bank. It has also allowed UBS to transfer \$60 billion worth of risky assets into a state controlled fund. Credit Suisse was also offered a similar plan but has raised SwFr10 billion from private sources.

This is another unprecedented move from global governments to control the financial crisis. Experts feel more is still to come before the situation gets brighter. Bank's shares rallied over the week despite increasing fears of a global recession.



RBS, HBOS and Lloyds TSB are all set to receive government funding

Credit Crunch Still Biting

Sarah Lloyd

Citigroup reported third quarter losses of \$2.8 billion with quarterly revenues of \$16.7 billion, down 23 per cent on the quarter. The US bank wrote-off \$4 billion in toxic assets associated with subprime related mortgages and structured investment vehicle assets. This is the fourth consecutive quarter that write-downs have inhibited the bank's profits.

Having agreed to be taken over by Bank of America, Merrill Lynch reported a third quarter net loss of \$5.2 billion due largely to write-downs and credit losses on complex debt securities. Total write-downs amounted to \$9.5 billion, but were mitigated by the \$4.4 billion sale of Merrill's stake in Bloomberg.

State Street saw its net profit rise by a third to \$477

million in the latest quarter as volatile markets resulted in higher trading fees. However, its shares dropped by more than 12 per cent after a press release announced it might help some "under pressure portfolios managed by State Street Global advisors". The US custody bank's revenue rose by 24 per cent to \$2.8 billion and costs rose by 14 per cent to \$1.9 billion.

JP Morgan Chase, one of the banks due to receive \$25 billion in government funds, recorded earnings of \$527 million during the third quarter. JP Morgan's profits were down 84 per cent from \$3.4 billion when compared to the same quarter of last year. Wells Fargo is said to have made \$1.64 billion during the period, a fall of 24 percent compared to the same quarter of last year.

Markets

- OPEC, the oil cartel, are set to meet this week and in response to the falling oil may announce a cut in supply. This speculation led oil to rally near the end of the week falling below £70 per barrel at one point. Brent Crude closed at \$70.95 on Friday.
- The impending global recession has meant the "safe-haven" of commodities has been hit of late as demand is expected to fall. China's demand alone will not be enough to sustain the industry. Commodities companies were hit. Xstrata, Rio Tinto and Kazakmys all had shares trading down 20% during the week.

Winners, Losers

Company	Price	Change
Severn Trent (utilities)	1335p	26.42%
Schroders (banking)	855p	25.74%
UTD Utilities (utilities)	661p	20.73%
Inmarsat (telecoms)	397.25p	20.29%
Xstrata (commodities)	950p	-22.32%
Aviva (insurance)	308.25p	-25.18%
Prudential (insurance)	270p	-28.62%
HBOS (banking)	80p	-35.59%

Too Big to Fail or Too Big to Prop-Up?

The recent turmoil in the markets has led to central banks in Europe and around the world declaring their largest financial institutions are safe. The great and the good have declared the countries flagship banks will not be left to fall. If one needed supporting various governments have announced they will support them.

The Suisse government has made a rather large oversight in its recent declaration though. Pledging to support both UBS and Credit Suisse would be a hard promise to keep judging by the country's economic figures. UBS, the largest of the two, has assets worth four times that of Switzerland's economy and Credit Suisse measures in at over two times the GDP of the economy. With combined assets of over 6 times what Switzerland would be able to support their promise of total safety, to increase consumer confidence, is likely to have been a hollow one.

Switzerland is not the only country over committing itself. RBS' assets amount to almost twice the UK's GDP as do ING's when compared to the Dutch economy. The recent bailouts of RBC Dexia and Fortis required multiple government actions. The size of these banks is nothing compared to the might of Deutsche bank, BNP Paribas or even the "world's largest bank" HSBC. Cumulative assets reach into the tens of Trillions and thus not the home country nor the world combined would be able to save these banks. This is without mentioning any bank in the US, where average bank assets dwarf their European counterparts. Ireland, the smallest economy so far, has underwritten €400bn in deposits, a figure this economy could not meet if there were a run on its banks.

While these banks may be hard to keep afloat if they fall, the promise of total safety may not be as optimistic as the figures suggest. Acting promptly and ensuring no more runs on banks could just save each country's economies. The various preference share schemes offered in the recent government backed initiatives will make sure the situation of a major banking failure should not ensue. Prevention is better than cure in the banking world.

The UK or the US way?

Two controversial plans developed this week but is one more so than the other? The UK plan encourages banks who need help to re-capitalise with government help. However the US is forcing all banks to use tax-payers money. Is this damaging to US banks or ensuring a healthier financial market?

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Please contact us at,

mail@strictlyBIF.com

Economies Contract

Sarah Lloyd

Figures show the UK faces a slowing economy and rising consumer price inflation, which stood at a 16-year high of 5.2 percent - far above the Bank of England's target of 2 percent. The price of oil has halved to \$75 per barrel in recent weeks and food inflation has also eased leading Prime Minister Brown to predict that inflation is soon to fall.

Unemployment on the other hand has shot up at its fastest pace since the early 90's, the jobless rate now stands at 5.7 per cent. A Reuters poll of UK economists suggests that

unemployment can be expected to keep rising - possibly to 6.6 per cent.

The Reuters poll also found that the UK economy is already in a recession and is expected to see a 0.2 per cent contraction at the tail-end of 2008. The UK is also expected to shrink by 1 per cent in 2009, the first full year economic contraction since 1991.

UK recession is just part of the impending global crisis. President Bush met with European leaders this week as the economic gloom has hit US consumer confidence and new-home construction has plummeted.

Strictly Bites

French bank, **Caisse d'Epargne**, has announced a **loss of €600 million** in a **rogue trading** incident. The loss has sparked an audit into all French banks ordered by Christine Lagarde, the French Finance Minister.

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Twelve executives from collapsed investment bank **Lehman Brothers** have received **subpoenas** - an order to testify in court - over allegations that they **misled** the public about their **financial health**.

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Lloyds TSB has issued **debt** in the value of **£400 million**, the first debt sale by any financial institution since the collapse of Lehman Brothers.

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The price war on **petrol** amongst the big supermarkets has heated up after all cut petrol prices **below £1** on the back of the recent slump in oil prices.

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Iceland will decide whether to take a **loan** from the **International Monetary Fund** within a week as the economic crisis strangles the country.

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Shares in Italian bank **UniCredit** **surged** after the **sovereign wealth fund of Libya** became the second largest shareholder in the company. The North African nation will take a **4.23%** stake in the bank.

The chief executive of Deutsche Bank, **Josef Ackermann**, will **forgo his bonus this year**. Instead he will give it to colleagues who he said "deserve the money more than I do".

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Consumer confidence in the US suffered its **largest monthly loss** in October with the Michigan sentiment index plunging from **70.3 to 57.5**.

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The **trade deficit** in the eurozone **rose** sharply in August due to a surge in **imports**. The deficit stood at **€9.3 billion**. Analysts had expected a deficit of €5.5 billion for August.

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The **Bank of England** has announced new rules for money markets in an attempt to provide stability in them. They will **no longer disclose** how much **money** it has **lent** to banks overnight and have also set up a **new discount window** where **asset back securities** can be swapped for **government securities**

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Merrill Lynch CEO, **John Thain**, has announced **savings of \$7 billion** need to be made when the Investment bank's merger with Bank of America goes ahead. He expects most of the savings to result in **job losses especially in Operations, Finance and technology**. No job losses will occur in Fixed Income or commodities though.