

New Year Same Story

Bhavin Dhanani

2008 has arrived but financial institutions have nothing much to celebrate. Three of the big American banks announced profit figures last week which, as many expected, were very disappointing.

Citigroup reported a massive \$9.83 billion loss for the final quarter of 2007 on Tuesday. Revenues had dropped by 70% from the previous year and a sub-prime write-off of \$18.1 billion pushed fourth quarter earnings into the red. In addition to this dividends will also be cut by 41%. The bank was able to secure a hefty cash injection

of \$13.5 billion, half of which came from the Singapore government.

JP Morgan was able to outperform its rival as it announced a \$2.97 billion fourth quarter profit, a decrease of 34%. A write-down of \$1.3 billion relating to sub-prime mortgages was revealed but revenues in the period did rise by 7%. A cautious approach has been adopted by the bank as it has put \$1.1 billion aside to cover any further bad debts in 2008.

Merrill Lynch wrote down a mammoth \$16 billion, resulting in a \$9.8 billion loss for the

period, the largest quarterly loss in its entire history. For the year ending 2007 Merrill reported a \$7.8 billion loss, their first since 1989. An injection of \$6.6 billion was received from a group of investors which will strengthen the bank's balance sheet.

Last week's figures took the losses past the \$100 billion mark since last May. Total exposure is expected to reach \$380 billion and last into 2009.



Citibank is currently suffering the most during the credit crisis, they have lost market value equivalent to the GDP of Nigeria in the last year.

Northern Rock Talks Coming

Bhavin Dhanani

Commodities and Exchanges

- The price of oil reached the fabled \$100 per barrel mark for the first time. One transaction was carried out on January 2nd. The particular trader lost around \$600 because he traded above the market price in order to break the limit. Oil is almost five times more expensive than it was in 2002.
- Gold traded at a record high recently reaching \$917.90 and forecasts suggest it could breach \$1000 per troy ounce as gold is seen as a haven for investment in volatile times. The average gold price for the first half of 2008 is expected to be 30% higher than it was in 2007 before the current market volatility struck.
- Platinum has set records for some time, driven by the weakening US dollar. Platinum closed at \$1581 on 15th December setting another record high for the commodity. Coffee has reached a ten year high, along with cocoa topping its highest value for four and a half years. The optimal portfolio allocation of commodities has risen from almost zero percent to 20% in some situations.
- The FTSE 100 closed at a five month low on January 18th down to 5901.7. Since the 31st December the index has fallen 8.5%, its worst ever start to a year. It reached a low of 5856.80 during trading on the same day.

Gordon Brown has revealed that talks are now underway to sell Northern Rock to the private sector after it received suitable bids for the bank. However he has refused to rule out the possibility of nationalisation but this is felt to be an option that should be avoided. Chancellor Alistair Darling branded this option as "undesirable".

Goldman Sachs, who have been appointed by the Government, have formatted a proposal that has received the backing of the Government. The loans handed to the troubled bank by the Bank of England will be packaged up and sold as gilts, which would be collateral-

ised against mortgage assets, a big risk given the current climate. This proposal will come as music to the ears of the Virgin Group led consortium and Olivant as it provides another finance option.

The Northern rock board have now thrown their weight behind the Virgin Group bid. Virgin owner Sir Richard Branson is optimistic their offer will succeed. "I'm still confident that our bid is good. And I personally believe it's the best bid on the table, it's the best option for Northern Rock."

Northern Rock's share price closed this week at 64.5p.

Interest Rates

The new year has seen another interest rate decision from the Bank of England. This one, unlike the last left interest rates the same at 5.5%.

Many pressured for another cut, the credit crunch caused tightening on the availability of credit and has cut activity in the financial sector to levels not seen since the recession in the 1990s. The number of mortgage approvals fell by around 25% in November and the retail sector posted their poorest Christmas since 2005.

This poor growth should lead to a rate cut but inflation prospects are on the up. The cost of energy combined with current consumer-price growth means there could be higher inflation into the year above the government demanded level. The current poor pound could also push inflation and the bank needed to make sure it kept inflation under control in the near future.

Fund Injection

The holiday saw a fund injection by five central banks to ease current liquidity problems. The Bank of England, US Federal Reserve, European Central Bank and the Canadian and Swiss Central banks will offer \$110bn in cash loans. The loans were intended to increase confidence and ward-off recession.

Central banks lending to the markets instead of financial institutions asking for help removes the stigma attached to a loan. This reduces the impact on the share price of a company.

With problems rooted in the US sub-prime market the loans were not expected to be fully beneficial. However, the repackaging of debt and worldwide sales mean the credit crisis is global. The massive write-downs incurred by banks meant they were reluctant to lend to each other and thus the loans were intended to correct this.

The recent increase in inter-bank lending enabled the Bank of England to defer a rate cut and focus on inflationary pressures, proving the injection has had a positive impact.

Strictly Bites

Activist investor **Nelson Peltz** has told confectionary group **Cadbury's** to sell businesses and appoint new executives after a year of poor performance.

DSG, the electrical retailer who recently left the **FTSE 100**, is close to being removed from the **FTSE 250** after announcing year profits could be down **£40-50million**.

Following **Alliance & Leicester's** drop in share price due to recent troubles in the **Banking sector**, its price is now attracting interest from former suitor **Santander**.

The big four **Supermarkets** had positive Christmas' with increases in **like for like sales**, showing higher food prices did not deter **consumers**.

Brewers have been hit hard following a series of disappointing last **quarter results**. Most have been regarded as **short term** problems following the **smoking ban** earlier in the year.

Merrill Lynch announced it is receiving an extra **\$6.6bn** from **Asian and Middle Eastern Investments**.

Countrywide Financial has had to reject market rumours that it is **bankrupt**. This also follows speculation it could be bought by **Bank**

Citigroup has announced it is raising **\$14.5bn** from the governments of **Singapore** and **Kuwait** through their **Sovereign Wealth Funds**.

India's biggest **IPO** of **\$3bn** was achieved when **Reliance Power**, now valued at **\$30bn**, floated this week, selling **228million shares** in under a minute.

America's big bond insurers have underwritten **\$2.4trillion** of **private** and **public sector bonds**. A bankruptcy would severely worsen the credit crunch due to the number of **banks** and **financial institutions** that rely on their guarantees.

LSE has opened an office in **Beijing** following the US markets to try and attract **Chinese** firms to list on the **London based exchange**.

UBS plans to shrink its **investment banking business** after writing off **\$14bn** of **sub-prime** linked loans and warning of more write-downs to follow.

India's Central Bank has been accused of **protectionism** following its refusal of **UK banks'** plans to open **rural branch networks**.

Oracle has purchased **BEA systems** for **\$8.5bn**, **\$2bn** more than its first approach suggested. **Carl Ichan**, an **activist shareholder** in **BEA**, persuaded **BEA** to sell.