

Bearish Times for Stearns

Bhavin Dhanani

The fifth largest American investment bank, Bear Stearns, has received a bailout package from the Federal Reserve and JP Morgan. It has recently been speculated that the bank has been in trouble and this revelation has confirmed that the worst of the credit crunch is not over.

Bear Stearns has appointed JP Morgan and Lazard as advisors for long-term funding. The financing being provided by JP Morgan is only for 28 days. Most of the bank's revenues derive from their fixed income business thus it had a wide exposure to

the sub-prime mortgage crisis. In a statement Bear Stearns said, "Our liquidity position in the last 24 hours has significantly deteriorated".

Bear Stearns was heavily involved in lending to hedge funds. Last year it bailed out two of its own funds. The collapse of Carlyle Capital Corporation provided the bank with undervalued mortgage backed securities which had been used as collateral. This fuelled rumours that the bank was facing a liquidity crisis.

Many in the UK are labelling the bank as the American Northern

Rock. Although Bear Stearns is massive by comparison, the situation is fairly similar. It has been suggested that a takeover of the bank could be possible. Given the current climate it may be difficult to find a bidder. Another possibility is a split, but this may not be feasible given that Bear Stearns' business is mainly in fixed income.

Shares in Bear Stearns dropped massively, closing the week on \$30.85, a fall of 56%.



Problems at Bear Stearns suggest that one of America's biggest banks will become a takeover target

Fed Increases Cheap Lending

Phillip Butler

The Federal Reserve continued its drastic action in the US economy in an attempt to stave off an ever looming US recession.

Days after guaranteeing to provide temporary loans to banks and bond dealers, it unveiled a new arrangement, the Term Securities Lending Facility (TSLF). The TSLF allows primary dealers to borrow up to \$200bn of treasury securities for 28 days, by offering less credit worthy bonds as collateral.

The arrangement works in two ways. As the TSLF is a bond for bond agree-

ment, its immediate impact will be to provide liquidity. It will take illiquid bonds from the market and issue treasury securities in their place.

Additionally, by issuing treasury securities they are satisfying the huge demand for treasury securities. Although this is on a temporary basis it should ease market conditions where buyers are increasingly tentative.

The Fed is offering around a quarter of its asset base in the TSLF scheme, which raises concerns over credit risk. The lowest collateral accepted is AAA.

Markets

Winners, Losers

- The Dow Jones this week closed roughly on par, up a little at 11,951.09. The FTSE was not as good down, 1.20% to 5,631.70.
- Retail figures will be released this Thursday and are expected to show current market conditions reflected in a decrease in high street activity. The activity is thought to have decreased by around 0.5% compared to January.
- Gold and Oil both rallied this week amid concerns over exchange rates. Oil increased \$5.17 to \$107.54 and Gold increased \$31.00 to break \$1000 reaching \$1,007.10.

Company	Price	Change
Standard Life (insurance)	234.50p	13.0%
Kazakhmys (commodities)	1790p	7.9%
Aggreko (hiring)	627p	7.6%
Intertek (testing)	963p	7.5%
HBOS (banking)	110p	-9.4%
Br Airways (aviation)	226.50p	-10.7%
Mitchells (comms)	377p	-10.9%
Yell (directory)	167.33p	-14.2%

Company Profile

Name: Bear Stearns Company

Share price: \$30.85

Business sectors:

Retail Banking, combines equities fixed income and investment banking to offer sales, trading and financial advisory

Global Clearing, offers financing, clearing services and securities lending. Services are provided to hedge funds, brokers and high net worth individuals

Wealth Management, asset management is combined with private client services

Employees: 14,000

Recent M&A:

November 2007, the company brought Williams Power company, involved in the energy sector

Sales Revenue: Capital Markets, 80% Wealth Management 8% and Global Clearing 12%

Total Revenue: Net income for fiscal year ending November 2007, \$233 million

Hair Cut

Haircuts refer to the "trimming" of value off assets used as collateral. The haircut value is a percentage taken off the par value of the asset. This value is stated by the receiver before the transaction can be finalised.

The recent problems in the markets have caused the value of the haircut to increase. Since it reflects the risk associated with the asset, haircuts are increasing as markets begin to suffer.

Recently, for the first time in almost two decades, government bonds have been required to provide a haircut when used as collateral.

The Federal Reserve's recent scheme to help out the markets (see story two) utilises this haircut process. The Fed will only accept AAA rated securities that are not up for downgrading. Despite this all bonds offered will suffer a haircut before they will be taken in exchange for government bonds.

The ECB requires all securities to sustain a haircut before they accept them as capital. In 2003 the ECB required all asset backed securities that offered no coupon and with maturities greater than 10 years to incur an 18% haircut to the par value of the asset.

Any queries, comments or requests?
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Gold Reaches New Heights

Bhavin Dhanani

The price of gold has soared to new extraordinary highs. On Thursday the price of one ounce broke the \$1000 barrier for the first time in history. On Friday the rise continued with prices peaking at \$1007.10 before closing at \$999.15.

In recent weeks the price of the precious metal has gone up and up. As investors seek a safe haven and protection from the ever weakening dollar, the demand for gold has increased, pushing

prices up. As gold is dollar denominated it becomes comparatively cheaper for holders of other currencies as the dollar falls in value. This again causes greater demand, meaning that the price pushed higher.

Already this year gold has risen by 20% and it is set to rise further. In 2007 the price increased by 32%. With the Federal Reserve likely to cut rates in the United States again on Tuesday, the price of gold is set to continue on its upward trend.

Strictly Bites

Dresdner Kleinwort's owner may be about to sell. Insurance group **Allianz** is ready to offload the underperforming unit.

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Citigroup has pledged \$1 billion to rescue six of its hedge funds. The plan renewed fears that many funds are close to collapse.

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Prudential, the insurance group, has denied it will float its **Asian arm**. The arm is valued at £16 billion, around the same as the whole group's stock market value.

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Lehman Brothers has started to cut its workforce. It plans to shed 5% overall, with many of the redundancies coming in the UK.

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Eurozone inflation hit 3.3% last month as a result of high energy and food prices.

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The **Chinese economy** grew by an annualised 15.4% in the first two months of 2008. The same figure was 18.5% in 2007.

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Inflation in China hit a 12 year high. In February the rate reached 8.7% from 7.1% in January.

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The Bank of England has revealed that the average household inflation expectation is 3.3%, up from 3% in November.

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Private equity group **JC Flowers** could be about to make a bid for **Friends Provident**, the insurance group. The insurer announced a 97% fall in profits to £16 million.

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JP Morgan has downgraded forecasts for the economic growth of **India** to 7%. The latest figures show that in January the Indian economy grew by 5.8%.

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Consumer confidence in America hit a 30 month low according to the **IBD/TIPP** economic optimism index. The index stood at 42.5. A figure of below 50 is pessimistic.

Google completed its merger with **DoubleClick** this week, almost a year after the deal was announced.