

Investment Manager Commentary – Q1, 2008

The first quarter of 2008 was a disaster for equity investors, with markets falling in each consecutive month. The MSCI World Index fell 8.8% in Sterling terms, with UK -10.4% and US -9.2%. Markets which had shown most progress last year were badly hit with Pacific ex Japan -12.6%, and Emerging Markets -10.8%. The idea that these markets could somehow decouple from Western economies has proved to be a false hope; investors in China have lost half their money in six months.

The reason behind these falls was ongoing problems in the banking sector, and continuing stress in credit markets. The UK eased rates by 25bp, the States by 200bp and yet mortgage rates have continued to climb with availability seriously curtailed. House prices in America continued to fall, with the rate of decline accelerating. Similar factors weigh in the UK, Spain and Ireland.

Half way through March, the Fed was forced to rescue Bear Stearns, the first time an investment bank has been bailed out. In truth, there was little option. So intertwined have banking activities become that the failure of one would bring down many.

Investors took heart from this action, and many of the major markets have rallied in the second half of March, and the beginning of April. Amongst others, UBS, Lehman Brothers, RBS and HBOS have announced capital raising issues.

Government Bond investors ignored inflationary concerns and scored major gains, particularly in America.

Outlook

The economic backdrop, both in the UK and US continues to deteriorate, and this is bound to cause further write offs within the banking system. It is not clear that the existing provisions will cover these future losses. We have yet to see significant changes in earnings forecasts to reflect the more difficult outlook, and therefore remain cautious.