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Market Review






OCTOBER 2008

Bail (out) set at $700bn!!

Financial market panic reached a new crescendo in mid-September typified by US equities which had their largest one-day fall since September 11, 2001. All the major Western market indices including the FTSE hit new lows for the year as a series of (mainly US) developments fanned the flames of the fire. The US Government was forced to intervene and rescue Fannie Mae and Freddie Mac the two institutions guaranteeing half of all US mortgages. Latterly the US Federal Reserve had to take control of AIG Group, one of the largest US insurers, Bank of America took over a weakened Merrill Lynch, investment bank Lehman Brothers was forced into liquidation, and Washington Mutual was rescued by JP Morgan. In the UK rumours swirled about the viability of several banks including HBOS, the largest UK mortgage provider, and 'buy-to-let' specialist Bradford & Bingley. Despite recent reassurances HBOS was forced into a deal with Lloyds TSB, agreeing to be taken over by its larger rival. Bradford & Bingley was effectively nationalised. It is debatable how long either would have been able to survive on their own given their large reliance on wholesale money markets, which to all intents and purposes have dried up. Central banks, including the Bank of England, are now providing the much needed liquidity as banks are too scared to lend to one another.

The Federal Reserve and other Central banks had pumped $180bn into global money markets but it was the announcement of a $700bn bailout plan by the US authorities which finally gave hope that the current crisis may be contained. UK banks may receive some direct benefit from this because of their substantial operations in the US. HSBC has the largest exposure (about $85bn) to the sorts of beleaguered assets that the scheme may rescue. The package was eventually voted through, despite widely held reservations amongst politicians and public alike. In London a ban on naked short selling of certain financial equities contributed to the largest one-day rise ever in the UK market (FTSE100 was up 8½%). It is hoped that UK and European interest rates will start to fall as we move into 2009.

The oil price has fallen from summer highs of over $140 per barrel to around $90 which will feed through to lower inflation figures as we move into the new year. Although not yet confirmed by the official data the UK economy is thought to be in recession and it is widely agreed that an easier monetary policy is required. Looking forward, once a peak in the inflation rate has been confirmed the Bank of England is expected to aggressively reduce interest rates. Stock markets anticipate events therefore an improved outlook is possible for equity markets as we move into 2009.

Three Month Performance

	30/09/08	30/06/08	Change
FTSE 100	4902.45	5572.60	-12.0%
FT All Share	2483.67	2855.69	-13.0%
US Dow Jones	10850.66	11350.01	-4.4%
Nasdaq Comp	2091.61	2292.98	-8.8%
FTSE Eurotop 300	1050.12	1201.36	-12.6%
Japan Nikkei	11259.86	13481.38	-16.5%
APCIMS Growth	2865.67	3109.64	-7.8%
APCIMS Balanced	2553.60	2726.73	-6.3%
APCIMS Income	2016.32	2128.11	-5.3%
£/$	$1.7829	$1.9927	-10.5%
Euro/£	€1.2626	€1.2640	-0.1%
Gold (per ounce)	$871.18	$926.07	-5.9%
Brent Oil	$97.44	$140.24	-30.5%

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A new service launched - see back page

Stock Selections (prices as at 3rd October 2008)

'Defensive' blue-chips

Tesco

Price 406.5p Yield 2.7% PE 15.1

Mkt.Cap. £31951m High/Low 495.7p/337.6p

Good management of costs and product mix has allowed Tesco to maintain food sales during the consumer slowdown, and continued strong growth from its overseas stores has allowed the group to still grow profits. Overseas sales now account for 25% of the group total, but more importantly, 50% of profits growth. Its venture into the US, Fresh & Easy, should become significant over the next 3 to 4 years.

Growth is also being derived from other, increasingly significant parts of the group. Tesco Personal Finance is now contributing strongly – with original partner Royal Bank of Scotland recently bought out. Its on-line and home delivery services show double-digit growth and its smaller format convenience (Express) and urban (Extra) store offerings are expanding steadily, with scope for further growth in the UK. The interim results released 30th September showed group profit up 10% - ahead of expectations.

Compass Group

Price 335.5p Yield 3.2% PE 22.4

Mkt.Cap. £6180m High/Low 396p/272p

Compass is the world's largest contract caterer, with food service businesses in the UK, US and Continental Europe.

The middle part of the decade was a difficult time for the group with profit warnings and a major lawsuit into alleged improper conduct in securing contracts with the UN. Management weathered the storm and at the same time restructured the business, selling non-core units. Now Compass is in a 'golden period' as it has growing success in winning substantial contracts in the government sector, education, healthcare, leisure, sports and vending, at a time when organisations are increasingly looking to out-source catering.

In its 29th September trading update Compass said annual sales growth will "comfortably" top 5%, and sales in its main market, North America, remained strong during the summer.

Whitbread

Price 1073p Yield 3.4% PE 24.1

Mkt.Cap. £1867m High/Low 1811p/924p

Whitbread now concentrates on hotels and restaurants. Its brands include Premier Inns, Brewers Fayre, Beefeater and Costa Coffee.

Premier Inns is the largest hotel chain in the UK and now accounts for 70% of group profit. Premier has out-performed the wider hotel market – like-for-like sales at Premier were up 7% in the 24 weeks to 14th August. The chain is picking-up business from customers who are trading down during the economic slowdown. At the same time the group is adding about 4,000 new rooms this year, and targeting a 50% increase to 55,000 rooms within the next 5 years. Costa Coffee is also expanding at a similar pace into Europe. Its like-for-like sales rose by 3.7% in the 24 week period, whilst pub restaurants grew by 4.4%. The group is ideally placed for further growth in this difficult environment.

More speculative investments

Eaga

Price 138p Yield 2.2% PE 19.2

Mkt.Cap. £346m High/Low 202p/90.5p

Established in 1990, Eaga is the UK's leading provider of residential energy efficiency solutions, providing improvements to over 1,000 UK homes every day, most of the work derived from government grant-funded programmes.

Government initiatives such as the Carbon Reduction Target Scheme (CERT) and the 'Warm Front Scheme' are behind Eaga's contracts with the major UK energy suppliers such as Scottish Power (a £200m contract for the outsourced management and delivery of Scottish Power's entire CERT obligation). A £500m contract with the BBC to assist in the nationwide switchover from analogue to digital TV, proves Eaga can win sizeable contracts outside its core competency of heating and insulation.

The excellent visibility of forward earnings and strong free cash flow justify a higher valuation.

Investec

Price 315p Yield 7.9% PE 5.5

Mkt.Cap. £1336m High/Low 587p/267p

Investec is an international specialist banking group and fund manager operating in three principal markets: South Africa, the UK, and Australia.

The bank has written down the value of its mortgage and structured credit assets, but its exposure is only modest. In comparison to other banks it is in a strong position. This was reflected in its 18th September trading update, in which it said it expected its first half operating profit to match that achieved a year earlier. The group continues to maintain a high level of liquidity and capital well in excess of minimum regulatory requirements. In fact management stated that it was on the look out for assets that have been mispriced because of the market turbulence – a sign of its financial strength.

Rok plc

Price 85.5p Yield 4.0% PE 7.4

Mkt.Cap. £153m High/Low 237p/61p

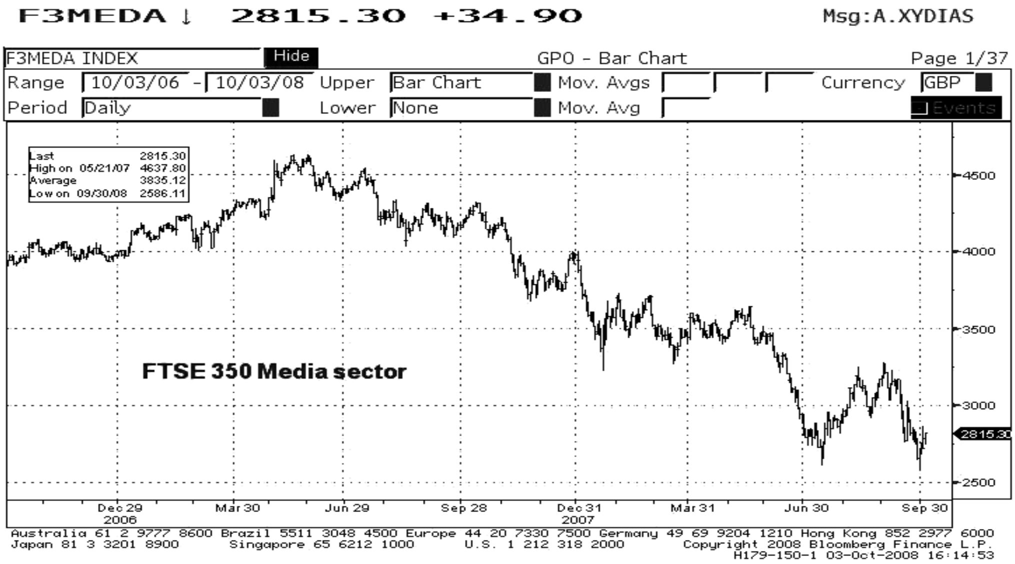
Rok is a building and maintenance company with branches in every major town and city in the UK. Its services are split into 3 sub-categories: New Build – is divided between private and public. Projects are of typical value of about £1.2m and include the likes of health centres, golf clubs, social housing. Planned repairs and refurbishments – nearly all of the work is won through long-term contracts with Britain's social landlords. Response maintenance – the group have a growing number of long-term contracts with major insurers like RSA Insurance and Zurich to provide repair and maintenance work following accidents and insurance claims.

Management has reacted to the changing economic environment by closing its property division, and greatly reducing its resources committed to private new build. Overall the business is benefiting from the trend towards greater outsourcing of repair and maintenance work, and increased spending on public housing.

Media – sector expected to outperform !

It may seem illogical to recommend a sector that traditionally relies on advertising, when advertising budgets are usually reduced during economic downturns. Historically, however, share prices in the sector tend to bottom-out about 9 months before a bottom in GDP growth. With the current projection for UK GDP pointing to a low around the middle of next year, prices may start to pick-up from here. Additionally, the sector displays a seasonal bias. Traditionally the fourth quarter sees prices rise, probably reflecting more buoyant advertising ahead of Christmas.

The FTSE 350 Media sector index has fallen by more than 40% since its peak in the middle of last year. This reflects the downgrades in earnings expectations, compounded by general market weakness due to the 'credit crisis'. Further earnings downgrades are likely, but these may have been priced-in. In the last recession of the early 1990's, the sector index fell 35% peak to trough. In valuation terms, the sector's historic PE is 10.7. The low of the 1990/91 recession was at 10.



Favoured stocks in the sector

Reed Elsevier

Price 579p Yield 3.3% PE 15.8

Mkt.Cap. £6389m High/Low 696p/512p

Reed produce numerous trade publications in the science & medical, legal, education and business-to-business industry sectors. Increasingly it is delivering its publications by electronic means.

Reed's subscription-based products afford a high degree of visibility. The legal and scientific publishing businesses enjoy high renewal rates as customers are often locked-in through multi-year contracts, or its publications are the leading journals in the field and thus enjoy a must-have quality.

Reed announced first half results that exceeded expectations Pre-tax profits from continuing operations rose to £350m from £308m.

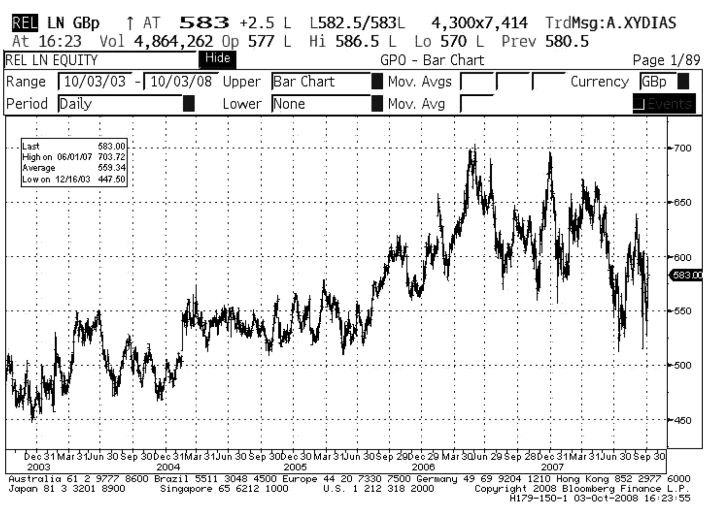
WPP

Price 454p Yield 3.1% PE 11.6

Mkt.Cap. £5345m High/Low 716p/414p

WPP is one of the largest advertising agencies in the world with 1400 offices in 103 countries. Its operations encompass not just advertising but also media investment management, information and consultancy, public relations, and branding and identity services.

Organic growth is expected to fall to 0% in 2009 from 4.5% in 2008, but pick up again in 2010. WPP's valuation is discounting a cyclical worst-case scenario – the 8.5x 2009 forward PE the shares trade on is still well below the 12.5x low achieved in the advertising recession of 2001/02.



Contracts for Difference (CFD)

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What are CFDs?

A Contract for Difference (CFD) is an agreement between you and a provider such as BSCFDs to exchange the difference between the opening and closing values of a particular contract at its close.

CFDs are traded on margin which means that you do not need to provide the full cost of the underlying asset in order to trade in it. Instead, to open a CFD position you only need to provide a fraction of the full value of the underlying asset. CFDs therefore allow you to increase your exposure to a market, and consequently multiply the potential return (or loss) you could make.

Why trade CFDs?

CFDs are a way of trading on the price movements of a wide range of financial markets around the world without buying or selling the underlying asset directly. The global range of markets available include equities, indices, currencies and commodities.

CFDs can also be used to speculate on upward or downward price movements, or alternatively used to hedge an existing portfolio against any price falls. There is no stamp duty payable of UK equity CFDs and with BSCFDs there are no commission charges to pay on index or sector CFDs (although tax laws can change and depend on individual circumstances).

Further information

CFD trading carries a high level of risk to your capital with the possibility of losing more than your initial investment and may not be suitable for all investors. Ensure you fully understand the risks involved and seek independent advice if necessary.

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