



From Bailout to Blowout?

If you thought the actions of the G-7 and US Treasury and Federal Reserve to thaw the Global 'credit freeze' was enough, think again. The global economic slowdown will not simply abate as a result of this 'quick fix' measure. Karl Marx would have been smiling at the level of State intervention in the Global financial markets recently.

So the banks are not lending to each other, this was evidenced by a wide 'TED Spread'. This is the difference between the London Inter-Bank Offered Rate (LIBOR) and the three month US Treasury Bill rate. On October 10, this year the TED spread reached an all time high of 465 basis points. This exceeded even the level recorded during the 'Black Monday' market crash in 1987. In short, banks were hoarding funds at an unprecedented rate, with liquidity drying up. But why?

The simple answer is risk. Institutions were eyeing each other with suspicion in height of the credit crisis thinking who would be the next to fail. More than that, the hoarding of cash was a means of keeping themselves (banks) afloat. Much debate has revolved around the failure of Lehman Brothers and the actions of CEO Richard Fuld Jr. Mr. Fuld has testified before a US Congressional Committee on the events leading up to Lehman's filing for Chapter 11 bankruptcy on September 16. In fact, Federal prosecutors have issued subpoenas to several people including Mr. Fuld as a result. An area of focus is whether Fuld or other executives of Lehman misled investors about the condition of the bank in early June 2008. Bravo.

We are not against prosecution if a felony has been committed, in truth, several jail terms should be on offer in this whole scenario. Our problem is that Fuld may become Wall Street's fall guy?

Treasury Secretary Henry Paulson was recently quoted as saying that 'some banks might fail' even with the recent bailout. Critics of the bailout, now tagged, 'Paulson's Plan' point out the unprecedented powers it gives to the Treasury Secretary in terms of the economic and financial landscape. The prospect of all this power residing in the hands of one individual is disconcerting; Mr. Paulson can literally decide who lives, and who dies.

Readers remember that Lehman was rumored to be in merger talks with Bank of America on September 11, 2008. Lo and behold, during that weekend, talks did occur, and Bank of America took over Merrill Lynch, leaving Lehman in the lurch. Research revealed that Merrill CEO, John Thain formerly worked with Henry Paulson at Goldman Sachs. A mere coincidence perhaps? You decide.

The view that Main Street essentially sees Paulson's Plan as a Wall Street bailout seems borne out by a CNN poll conducted on October 17-19 where the Plan received just a 28 per cent approval rating. However, that same poll sample favored government assistance to homeowners who are unable to meet mortgage commitments by 58 per cent. The significance of

the housing crisis cannot be underestimated. If ordinary Americans are having difficulty meeting mortgage payments and have to face gasoline prices around US\$3.00 per gallon at the pump, how can they begin spending to stimulate the economy?

The Gloom, Boom, and Doom publisher, Marc Faber, sees inflationary pressures on global economies that have to print more money. Essentially, increased money supply can lead to increased aggregate demand, but if there is no concurrent increase in the supply of goods, inflation can ensue. Recent economic data released by the US Government during the week October 13-17 showed industrial production falling to its lowest levels in 24 years. Another economic argument is that in spite of the Federal injection of dollars into the financial system, the velocity of money circulation is low, stalling any economic recovery. Incidentally, Mr. Faber correctly advised investors to bail on equities one week before the 1987 Crash.

A large market that existed unregulated by Federal authorities until recent developments caused New York regulators to begin to pay close attention following the subsequent plunging in share prices of Wachovia Corp and Morgan Stanley. This is the Credit Default Swaps or CDS Market. A CDS is simply 'bond insurance' the bondholder can purchase a CDS as protection against the issuer defaulting, which is guaranteed by the seller. The problem here was that the companies that sprang up to write these options were grossly undercapitalized; so much so that they would be unable to pay if a default occurred. Well guess what? Bear Stearns and Lehman have disappeared, and AIG came close the brink. Federal bailouts for bondholders in these institutions did arrive and investigations are continuing as to whether trading in CDS' may have contributed to the capitulation of these institutions. The hard question the Federal Regulators must ask themselves is: "Why little or no attention was paid to these nebulous financial instruments that were allowed to flourish unchecked?"

The Regulators and Monitors of the World Financial Institutions fell asleep at the wheel, and investors have been made and will continue to pay in the short-term.

Current Happenings in Local and International Markets:

- Finance Minister: T&T not immune to recession
 - \$21m in profit for OCM group
 - TTSE makes rule change to prevent small transactions affecting the prices of stocks
 - T&T Economist calls for higher interest rates
 - Sagicor: exposure to the international financial crisis is not significant
 - BICO looking for 50 per cent reduction in energy cost
 - Pan Caribbean sees 13 per cent revenue increase, but trading income falls
 - Prestige Holdings bounces back
 - Stocks, oil, gold tank on growing recession fears
 - OPEC slashes production
 - U.K. GDP Shrinks, First Recession Since 1991 Looms
 - Goldman Sachs May Slash 3,200 Jobs as Turmoil Worsens
 - Foreclosure Filings Rose 71% in Third Quarter as Prices Fell
 - U.S. Initial Jobless Claims Rose to 478,000 Last Week
 - Wachovia Loses \$23.9 Billion on Real-Estate Charges
 - India Lowers Key Rate for the First Time Since 2004
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Table 1: Regional Market Performance (as at 23 October 2008)

Index	Closing Value	Weekly Change (%)	Monthly Change (%)	YTD Change (%)	1 Year Change (%)
TTSE Composite	937.73	-4.69	-13.85	-4.51	-0.72
All Trinidad	1,270.95	-4.43	-13.09	5.85	7.57
JSE Index	94,854.22	-1.06	-9.05	-12.15	-2.59
JSE Select	2,549.27	-0.20	-11.22	-12.96	0.61
All Jamaica	93,547.62	-0.73	-10.86	-12.39	0.31
BSE Composite	1,010.14	-1.54	-3.05	-1.81	-0.86

Table 2: International Market Performance (as at 23 October 2008)

Index	Closing Value	Weekly Change (%)	Monthly Change (%)	YTD Change (%)	1 Year Change (%)
S&P 500	908.11	-4.05	-23.57	-38.15	-40.24
Nasdaq Composite	1,603.91	-6.63	-25.51	-39.53	-42.70
Dow Jones Industrial	8,691.25	-3.21	-19.93	-34.48	-36.45
German Dax	4,519.70	-2.23	-25.52	-43.98	-42.37
FTSE 100	4,087.80	5.86	-20.41	-36.69	-37.25
Nikkei 225	8,460.98	0.03	-30.02	-44.73	-48.57
Hang Seng	13,760.49	-9.65	-27.09	-50.52	-53.16
DJ Eurostoxx	2,452.03	1.16	-21.91	-44.27	-44.00

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