

- FINANCIAL ARMAGEDDON
- QUANTITATIVE EASING
- PORTFOLIOS
- THE BUDGET
- LETTER TO THE EDITOR

	1/1/04	1/1/05	1/1/06	1/1/07	1/1/08	5/4/08	1/7/08	5/10/08	1/1/09	5/4/09	1/7/09
<b>FTSE 100</b>	4477	4814	5618	6220	6457	5947	5625	4980	4434	4030	4249
<b>FTSE All Share</b>	2207	2411	2847	3221	3287	3039	2856	2522	2209	2051	2172
<b>Dow Jones (US)</b>	10454	10783	10717	12463	13265	12609	11345	10325	8776	8018	8447
<b>S&amp;P 500 (US)</b>	1112	1212	1248	1418	1468	1370	1277	1099	903	843	919
<b>Nikkei 225 (Japan)</b>	10677	11489	16111	17225	15308	13293	13514	10938	8860	8750	9958

#### Leading Growth Equities

Balfour Beatty  
BHP Billiton  
BG Group  
Compass Group  
G4S  
Prudential  
Reed Elsevier  
Tesco  
W M Morrison

#### Higher Yielding Equities

BP  
Centrica  
GlaxoSmithKline  
HSBC  
National Grid  
Rexam  
Scottish & Southern Energy  
Smiths Group  
Vodafone

#### Smaller Companies

Croda  
De La Rue  
Hunting  
Inmarsat  
Morgan Sindall  
Petrofac  
Premier Oil  
VT Group  
Weir Group

#### Overseas Companies

Nestlé  
Roche  
Suez  
Woodside

#### Investment Trusts/ Unit Trusts & Overseas Funds

Bankers Inv Trust  
Edinburgh Inv Trust  
M&G Corp Bond Fund  
Monks Inv Trust  
Murray Income Trust  
Templeton Emerging

## THE GREEN SHOOTS OF YOUTH BUDDING FROM EXPERIENCED BRANCHES

### STOCKMARKETS

I am sure the whole nation is feeling somewhat embarrassed, saddened and subconsciously ashamed by the appalling political and financial mess we find ourselves in, early in the 21st century. And yet, as I compose this chronicle in the heart of the Norfolk countryside, I hear a tiny skylark and in the immortal words of Shelley:

"That from Heaven or near it  
Pourest thy full heart  
In profuse strain of unpremeditated art"

That skylark brings back the reality of eternity and though we are probably in the worst political and financial mess for 50 years, and one day things will get better.

As my readers will know, Stockmarkets have been very disappointing over the last year due to the unprecedented banking crisis (which has been so well documented that I do not need to expand upon it here):

FTSE 100	01/07/2008	5625
	05/10/2008	4980
	01/01/2009	4434
	09/03/2009	3460 low
	05/04/2009	4030
	01/07/2009	4249

and though there has been little news since the last chronicle (except the political mess on which more later), there have been 5 major financial factors that I discuss below.

Financial Armageddon/Quantitative Easing/Currency/Rights Issues and Open Offers (all of which are inter-related) and the Budget (which was a 'shocker' and purely political).

## FINANCIAL ARMAGEDDON

Following the collapse of Lehman Brothers and the Government rescue of Royal Bank of Scotland and HBOS (now Lloyds Banking Group) from near certain bankruptcy, the FTSE 100 fell to 3460 on 9th March 2009.

Such events had not been seen since the Wall Street Crash of 1929 and one felt closer to 'Financial Armageddon' than ever before in one's lifetime.

But, helped by Government intervention, this was not 'Financial Armageddon' and so far 'we have been saved'.

The 'relief factor' now comes into play and like that Skylark, reality and sustainability returns.

I discuss Equities later in this chronicle, but this 'relief factor' and the 'realisation of reality' has begun to help Equities recover to more realistic historical values.

Make no mistake, we are still in a very serious financial mess and this will take a long time to pull out of. But the artificial financial techniques are working and equilibrium and normality will return one day.

Indeed we highlighted the first 'green shoot' in our last chronicle when Barclays received a clean bill of health from the FSA.

Like dormant bulbs in the Winter, commerce has gone into hibernation as it retrenches, but just as Spring follows Winter, the efficient will survive and green shoots will grow.

I have no doubt that we have averted 'Financial Armageddon' and patiently await the arrival of the green shoots of Spring.

## QUANTITATIVE EASING

Government debt, due to Quantitative Easing, is now incomprehensible, but where has all the money gone? - I haven't seen it, and even "cleaning your moat" does not cost this much!

The only plausible explanation I have had so far was from a banker friend of mine and I quote:

*"The Government has agreed to lend billions to the major clearing banks. This will stop them going bust.*

*However, they must conserve cash to build up balance sheets so that they do not have to force vulnerable customers into bankruptcy.*

*This will take at least 3 years, by which time these vulnerable customers will have sorted themselves out.*

*The 'easing' will then recover, the Government will be repaid and the cycle starts again, after a long cold shower, but not Armageddon.*

*This is why banks are not lending to Real Estate Property Companies at the moment. There is no desperate economic need to lend on property ventures, therefore don't, and conserve cash."*

This might sound too simplistic, but it is a very complicated subject. This explanation makes sense and I am a very simple man.

## CURRENCY

At the peak of the financial crisis, sterling was thrown away and at one stage fell:

	01/07/2008	Low	01/07/2009
US/£1	1.99	1.35 (Jan 2009)	1.65
Euro/£1	1.26	1.02 (Dec 2008)	1.17
£1/Euro	0.79	0.98	0.85

But it is worth remembering that currencies usually go the opposite way to 'expert predictions'.

It was not long ago that teenage scribblers were predicting:

Eur/£1 = parity (100p)

Since then the rate has recovered from 1.02 to 1.17 (in other words 98p to 85p).

And 35 years ago I remember dealing in US\$ at 1.63.

To make life very simple I always say:

US/£1 = should be around 1.63  
Eur/£1 = should be around 80p

and using this 'CWL B formula' puts currencies into perspective.

But, weaker Sterling has made imports more expensive and exports cheaper.

## RIGHTS ISSUES AND OPEN OFFERS

We now live in extraordinary financial markets where:

- 1) Base rate has fallen to  $\frac{1}{2}\%$  to get the economy going.
- 2) However, banks will not lend to customers as banks build up their own liquidity (least of all lending to the property or building industry).

This means that 'over borrowed' corporate Britain, desperate for cash, must resort to raising this from shareholders (via Rights Issues) and not via their banks (bank borrowing).

We have seen many Rights Issues and Open Offers from:

The Property sector	Land Securities, Hammerson, British Land
The Building sector	Travis Perkins, Taylor Wimpey
The Banking sector	Royal Bank of Scotland, Lloyds Banking Group
Over borrowed companies	Rio Tinto, Greene King, Marston's

How different this is from the Harvard educated genius, who discovered:

'share buy back schemes'

to enhance earnings per share, at the expense of long term liquidity for survival and growth.

Thank goodness Barratt & Cooke have built up liquidity in most portfolios to be able to take up Rights where applicable.

## FIXED INTEREST

Base rate at ½% is artificial and unsustainable.

As explained, this is a temporary measure for banks to build up their own liquidity and when achieved in a few years time, base rates will return to normality.

(Base rates have averaged 5% for 315 years and have never been below 2% before).

We therefore believe:

- 1) Conventional Gilts are much too high, with 5 year gross redemption yields at 2.9%.  
(Source: Bloomberg).
- 2) Index Linked are more attractive, where we believe inflation will rise significantly after 2011. We therefore suggest purchasing Index Linked Gilts 2013/2016.
- 3) Eurobonds reflect commercial rates of interest between 5% - 6.5%, though 'the market' is difficult under £50,000 nominal of stock.

## EQUITIES

Taking all the above points into consideration:

- 1) We have weathered the storm of the threat of 'Financial Armageddon' and are now experiencing the 'relief factor'.
- 2) Quantitative Easing has given the Banks and over geared companies the time to recover.
- 3) While 'Rights Issues' are giving companies the access to capital to refinance.
- 4) A weak currency should help exports and hinder imports (though this is likely to lead to greater inflation).
- 5) High commodity prices will help:  
Oil companies  
Mining companies  
(but again will lead to higher inflation).
- 6) And consistent spending must continue in sectors such as:  
Household, Supermarkets, Pharmaceuticals and Utilities
- 7) And it is a fact that last year the majority of FTSE 100 companies increased their dividends by at least 10%. This year will not be so good with cut or reduced dividends from several Bank/Insurance/Property/Building and Telecom companies, although I note approximately half of the FTSE 100 companies reporting results in Spring 2009 increased dividends by more than 10%.  
(Source: Telegraph).

We therefore believe that, overall, dividends from FTSE companies will continue to rise in the long term.

It is now easy to create a portfolio of high yielding Equities to produce a net yield of 4.5% plus, so much higher than Gilts or Deposits (but remember the higher the yield the lower the prospects for growth).

On historical:

	Now	Long Term Average
P/E's	9.9 x	15 x
Yields	4.7%	3.0%
Dividend cover	2.1 x	2.0 x

Equities look good value, but profits are likely to stagnate or even fall before moving forward again, affecting today's ratings.

## THE BARRATT & COOKE PORTFOLIO

Taking all these points into consideration, our advice is consistent.

Clients come to Barratt & Cooke to invest surplus capital:

- 1) Having purchased property.
- 2) Having built up liquidity.
- 3) With income from work or pensions
- 4) And having provided for future pensions.

Barratt & Cooke advise clients how to invest this surplus cash in Stockmarkets and we still believe in:

1) **A proportion in cash deposit:**

Building this up on recoveries in the Stockmarket.

Investing this on falls in the Stockmarket.

Taking opportunities on Rights Issues, individual shares, FTSE 100 iShares etc.

2) **Retaining a good proportion in Fixed Interest:**

Gilts (Index Linked)  
Eurobonds (gross income)

for liquidity and income.

3) **A good proportion in leading Equities, with:**

- a) A spread geographically (a large proportion of FTSE earnings are derived overseas).
- b) A spread of sectors.
- c) A spread of leading stocks within these sectors.

We have all learnt that even the most respected companies can go wrong and therefore diversification is essential.

However bleak the future may look, we do believe in 'the Equity culture'. We do believe 'Equities look good value'. We do believe in 'long term investment' and we do believe in the old saying 'it is very easy to sell, but much more difficult to get back in'.

## OVERSEAS MARKETS (JOHN EVERALL)

Global Stockmarkets have just enjoyed their best quarterly performance in recent years, with emerging markets particularly strong:

	Rise Since 5th April 2009
Dow Jones (US)	+ 5.4%
Nikkei (Japan)	+13.8%
FTSE Eurofirst 300	+10.1%
FTSE All-World Emerging Market Index	+24.4%

However, it should be remembered that Emerging Markets were hit hardest by the turmoils of 2008.

Much of this improvement can be attributed to the relief that the second Great Depression appears to have been averted.

## US

The dollar has weakened against sterling since 5th April 2009 (\$1.48 to \$1.65) which has cancelled out the gains made on the US market to sterling investors. Looking forward, there are mixed signals with:

- Consumer confidence dropping in June
- The unemployment rate still high at 9.4%
- US industrial production still declining

We remain cautious on US stocks and would only invest in high quality brand names such as Procter & Gamble.

## Europe

Europe remains in a precarious position with inflation turning negative (-0.1%) in June for the first time ever. There are worries that European Governments have been slower than the UK and US to deal with the banking problems and that the Eastern European economies (eg Latvia) remain in serious trouble.

We still like 'specialist' European stocks such as Syngenta and Roche Holdings, which should be less affected due to their global exposure.

## Japan

Despite the Nikkei's rally, Japan remains unattractive, with its export led economy continuing to suffer from the fall in demand for goods worldwide.

## China/India

We continue to favour these growing economies, which do not have the high debt problems associated with the UK/US economies where we like Henderson TR Pacific.

## Australia/Brazil

Both of these resource rich economies look attractive with commodity prices likely to remain strong. For exposure to Brazil, we like Templeton Emerging Markets (22% in Brazil).

## CORPORATE ACTIONS (SINCE 5<sup>TH</sup> APRIL 2009)

As companies need to 'refinance', they are finding it difficult to borrow from the banks and they are therefore going to shareholders, hence the flood of Rights Issues and Open Offer Share Placings:

### Rights Issues

Wolseley	11 for 5 at 400p
Inchcape	9 for 1 at 6p and share consolidation
Premier Oil	4 for 9 at 485p
Greene King	3 for 5 at 270p
Marston's	11 for 10 at 59p
DSG International	5 for 7 at 14p
Lonmin	2 for 9 at 900p
Travis Perkins	7 for 10 at 365p
Rio Tinto	21 for 40 at 1400p

### Open Offers

Lloyds Banking Group	0.6213 shares for every share held at 38.43p
Liberty International	2.60198 shares for every 10 shares held at 310p
Taylor Wimpey	1 for 1 at 25p

### Redemptions

2½% Treasury Index Linked Stock 2009

### Capitalisation Issues

Lloyds Banking Group (1 for 40)

Barratt & Cooke study each individual issue.  
We study each individual client.  
We give individual advice to suit that client.

We do not expect clients to appreciate the work that goes on behind the scenes, but some of the paperwork being produced exemplifies this advice, especially where many of our clients hold in their portfolios:

Rio Tinto  
Lloyds Banking Group  
Index Linked Gilts  
and others

In view of the number of issues now taking place and the speed that they have to be processed (often within 10 days of an issue), Nominees are becoming essential and are now the norm amongst private client stockbrokers, making life easier for clients.

We have almost reached the stage requiring 'all Advisory/Discretionary portfolios to be in Nominees', as stockmarket and settlement systems have changed to become more efficient.

There will be certain exceptions which are understandable.

We are reviewing the whole position for non-Nominee clients and will be in touch in due course.

## THE BUDGET

This Budget really brings us back to the bad old days of 'old Labour', with the policies of:

'soak the rich and con the poor'

Income Tax is to be raised sharply:

- 1) Above £150,000 from 40% to 50% (the highest for 20 years)
- 2) But even meaner:

Above £100,000 the withdrawal of personal allowances  
Above £150,000 the loss of tax relief on pensions

Public spending and public borrowing will increase sharply with:

- a) The economy due to shrink by 3.5% in 2009
  - b) Public borrowing to rise to £175bn this year
  - c) National debt to reach £1.4 trillion in 2013/2014 which is equal to about 80% of the economy
- and:
- d) It has now been announced that Welfare payouts are greater than income tax receipts!

This is if you believe a word that Mr Darling or Mr Brown say.

In last year's budget Darling predicted:

	Prediction	Reality
Gross Domestic Product (GDP)	+2.5%	-3.5%
Net Borrowing	£38bn	£175bn
Income Tax Receipts	£171bn	£141bn
Inflation (RPI)	2.25%	-3%
Exports	+5.25%	-8.75%
Household Consumption	2.25%	-3.0%

Has any Chancellor ever got it so wrong? No wonder Sir Mervyn King, Governor of the Bank of England, is becoming seriously worried about Government economic policy.

However, there are a few bright spots for clients:

- 1) ISA allowances will increase to £10,200 per annum next year and this increase will take place from 6th October 2009 for investors who will be 50 before 5th April 2010.

*From 6th October 2009, the ISA subscription limit will increase to £10,200 for anyone eligible to invest in an ISA who was born on or before 5th April 1960 (ie who will be aged 50 or over during the current tax year). Up to £5,100 of the new ISA allowance can be saved in a cash ISA with one provider. The remainder of the £10,200 can be invested in a stocks and shares ISA with either the same or another provider. Alternatively, the full £10,200 can be invested in a stocks and shares ISA with one provider. (Source: HM Revenue & Customs)*

These higher limits will apply to all eligible ISA investors with effect from 6th April 2010, but an increase to £10,200 for people over 50 in October 2009 (don't ask me why - perhaps Darling will be 50 in October).

- 2) Capital Gains Tax stays at 18% which makes capital gain so much more attractive than taxable income.
- 3) Some AIM/PLUS stock remain free of inheritance tax if held for 2 years, as does some agricultural land.
- 4) Sadly: after 225,000 miles and 14 years, M94 KBO has been scrapped, but it is the most satisfying £2,000 I shall ever receive!

The moral is:

- a) Add maximum to ISA, particularly for income, where higher rates of tax do not apply.
- b) Try to establish capital gain rather than very high income, where capital gains tax is free up to £10,100 and then taxed at only 18%.

We shall be advising clients throughout the year.

### **CWLB'S PERSONAL CONCLUSION**

Jensen Button still leads the Formula 1 championship; Yeats won his 4th Ascot Gold Cup; Kinda Ready won the Dog Derby; the garden is looking marvellous and that tiny skylark is still pouring his heart out.

We have survived Financial Armageddon; the economy is still going round, albeit rather weakly; and one day the fruits of the green shoots of recovery will arrive (but not quite yet).

And therefore life is not so bad.

I am thrilled that Barratt & Cooke continues to grow in both size and reputation.

I am thrilled that Sam Barratt has joined his brother William in the firm.

I am thrilled with the whole staff, both the 'front office' and 'support team'.

I am thrilled that the younger members of staff wish to continue the traditional ethos of Barratt & Cooke.

I now feel justified in lining up all my personal clients with the most appropriate colleagues to help me in my absence when I shall be totally involved in my 'shrieval year', from April 2010. This will be with total confidence in the knowledge that Barratt & Cooke is in as good a shape as it ever has been. The green shoots of youth are budding out from the experience and wisdom of the older (but still very strong) branches.

I shall continue to concentrate on the major issues of 'overall portfolio management' and 'Barratt & Cooke strategy', but my colleagues will be helping me on a day to day basis. I shall continue to stay in touch with clients through these chronicles, which will hopefully continue to be full of words of wisdom and some well chosen wit!

C W L Barratt  
1st July 2009

P.S. Sadly in this issue there is no riddle, but you may enjoy reading my letter to 'The Editor' overleaf.

## LETTER TO THE EDITOR

Many of my readers enjoy my 'musing', rather than the sophisticated financial jargon.

I thought some of you would enjoy reading my recent 'Letter to the Editor', which was never published thank goodness.

With apologies to Mr Brown, it is not all his fault, and to be totally unbiased I do not know that any political party is better than the other.

Dear Sir

Following Sir Alan Sugar's elevation to the House of Lords (to join other notorious members such as the twice disgraced Lord Mandelson and Baroness Uddin who is alleged to have claimed a £100,000 mortgage on an empty property), how long will it take before we hear those rottweiler words:

"Your political life has been a complete shambles.

You robbed tax credits from pension funds and destroyed final pension schemes for millions of workers.

You sold the country's gold supplies close to the very bottom of the market, at US \$275 an ounce (now \$928).

You have endorsed bringing interest rates down to a 315 year low of ½%, destroying income for savers.

You have not eradicated 'boom and bust'.

You have led us into deflation using 'RPI' (real price inflation).

You transferred responsibility for Banking supervision from the Bank of England to the FSA. Lord Turner, the Chairman of the FSA is now calling for tri-party talks between the Government, the FSA and the Bank of England.

You have been Prime Minister during the worst financial crisis the UK has seen for 30 years.

You have seen unemployment rise to 2,260,000, which could reach 3,000,000. (Source: HRM Guide)

You are proposing the highest rates of income tax for 20 years.

Your borrowing requirement will soar to £175bn this year and public debt will rise to £1.4 trillion in 2013/2014, equalling 80% of the economy.

You have presided over a shameful House of Commons, many of whom are on the fiddle with expenses.

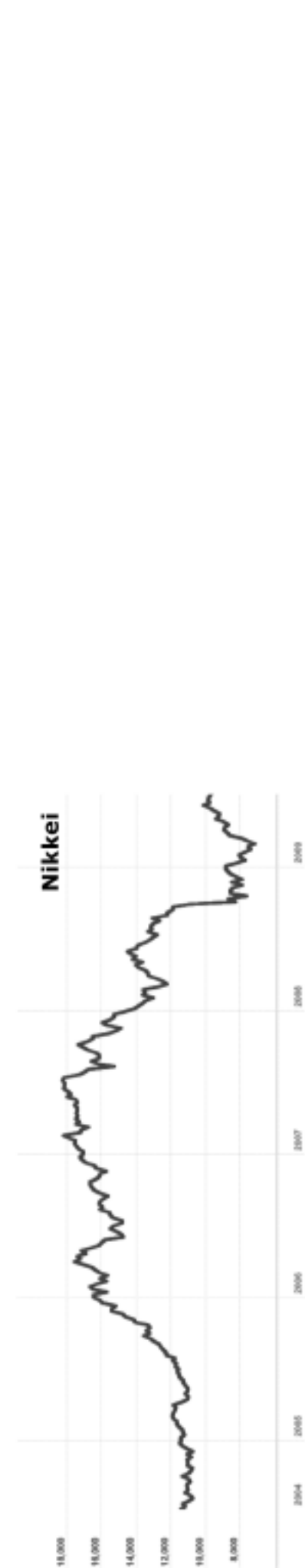
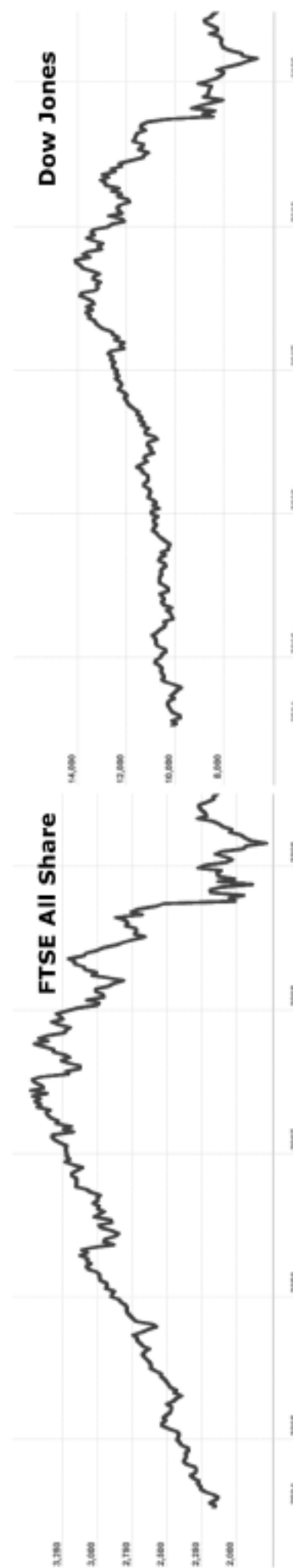
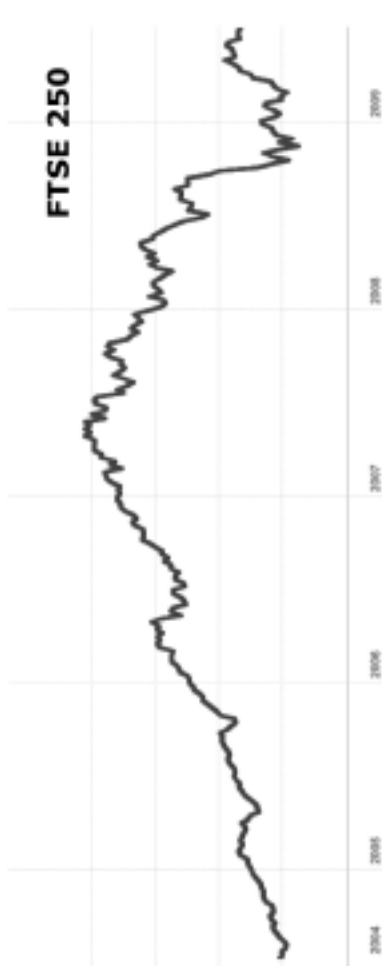
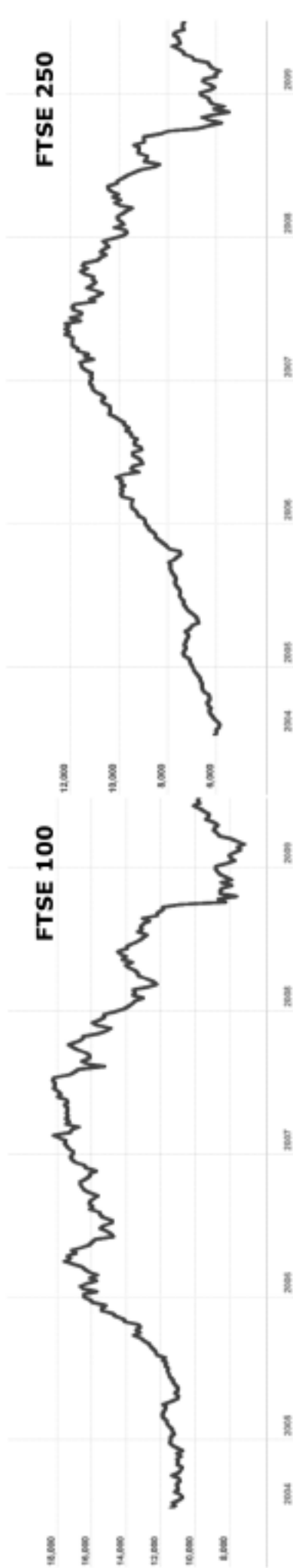
The Speaker of The House has had to resign.

And now, Mr Brown, the Governor of the Bank of England, Mervyn King, is in open warfare with your Chancellor's economic policies."

I am sorry Mr Brown, I like you, the world banking crisis is not just your fault and you might have saved the world with Quantitative Easing. I do not think any of the other politicians are much better, but as Prime Minister, you must take the responsibility.

For this Mr Brown, you're fired.

C W L Barratt



Source: [www.ft.com](http://www.ft.com)