



## TEMPLE BAR INTERNATIONAL MARKET UPDATE

### Week in View to 7<sup>th</sup> November 2008

#### A volatile week for all asset classes

Another extremely volatile week saw equity markets, on average, finish fairly close to where they were seven days ago, but with substantial volatility in between. A significant midweek rally seemed loosely associated with the result of the US election, in which Barack Obama recorded a victory over John McCain, although this unwound to some extent towards the end of the week.

While the recent bounce from equity market lows may not have signalled any sustained recovery, the extent of the subsequent retracement is negligible in the context of the previous decline, which emerged from the middle of September.

When we look at the dispersion of returns across risk assets, particularly equities, we note that performance is being driven by beta at the moment. As a result, during periods in which markets are rising, emerging markets and more-cyclical sectors are outperforming, while against declining markets, it tends to be the more-defensive sectors that are doing better.

#### Market Movements

Markets	7 Nov 2008	% Change
S&P 500	930.99	-3.90
NASDAQ	1647.40	-4.27
TSE 1st Section	879.00	1.37
FTSE S&P World Europe	266.93	-0.11
FTSE All-Share	2190.61	0.32
DAX	4938.46	-0.99
Hang Seng	14243.43	1.97
Citi World Govt Bond Index All Mats	528.85	0.99
Bonds*	7 Nov 2008	31 Oct 2008
US	3.77	3.98
Japan	1.51	1.47
Germany	3.68	3.91
UK	4.19	4.53
Currencies	7 Nov 2008	31 Oct 2008
USD/Euro	1.28	1.27
GBP/Euro	0.81	0.80
JPY/USD	98.23	98.35
USD/GBP	1.58	1.62
JPY/GBP	154.82	158.91
Commodities	7 Nov 2008	% Change
Oil (Brent Crude)	56.63	-6.21
Commodity Futures (CRB) Index	365.84	-1.01
Gold	742.85	1.96

#### A shift in focus to recessionary pressures

It's important to stress that market attention has shifted significantly over the past few weeks. We saw significant concerns about financial sector solvency in September and October, though aggressive action taken by policy makers to recapitalise the banks put a temporary cap on these concerns.

More recently, concerns have shifted to more conventional issues, and in particular, the much greater evidence of recessionary pressures.

What has happened, in fact, is that global demand has declined rapidly and, having started to slow in the middle of the year, the past few weeks have seen the release of some quite shocking economic numbers, which are being replicated in pretty much all of the major regions, along with evidence of material slowdown in China.

As a result, concerns over the financial system have been usurped by concerns that the global economy is entering a recession, with little sight of any immediate respite. With a high degree of conviction, we suggest that these are going to persist into 2009, although with the current quarter likely to be one of the worst we've seen for some time, it will also potentially be worse than any we're going to see next year.

While we should brace ourselves for some extremely poor economic and corporate newsflow, policy makers have the bit between their teeth, with interest rates being cut around the world and some countries announcing fiscal packages. Very interestingly, last week, we saw an expected cut in rates from the European Central Bank, along with a very aggressive 150 basis points cut in rates from Bank of England, justified by the appalling numbers coming out from both the UK and other countries over the past week or so.

While the 150 basis points exceeded even our expectations, we expect the next cut of around 50 basis points around about February, and we see no reason for European and UK short-term rates to stop falling as low as they need to. Our prediction of two further cuts may be undershot if circumstances dictate, and we are very likely, in Europe, to end up where the US is, with either zero or negative real interest rates.

#### Long-term value in pursuit of a meaningful catalyst

In the face of all this macro easing, it is possible that there can be some stability in the macro cycle in 2009. We would expect the lower oil price to help here, as well as some improvement in capital market liquidity, but it's going to be a long slog and we think that, if we do hit a trough, any recovery is going to be weak, largely as a result of constraints in the financial system. With regards to where we will end up, the environment is likely to remain very volatile for risk assets. Equity and credit prices, we think, are in the process of bottoming, and, while we do not expect the previous lows in equity markets to be broken, they may certainly be re-tested.

Although we see the markets in a bottoming process, this may prove to be extended, and something that may go on well into 2009. What we're really looking for at the moment is some movement towards better conditions in both real economies and in financial markets. We're not seeing this at the moment and therefore we lack a catalyst for a sustained move. The best way to summarise market prospects is by saying that there is a lot of long-term value there, but this long-term value is pursuing a meaningful catalyst.