

Scott pours cold water on fears of a further UK bank collapse



Fears that other UK banks could be on the brink of collapse, forcing the Bank of England to mount a rescue operation akin to Northern Rock are "mis-placed scaremongering", according to Ted Scott, manager of the F&C UK Growth & Income Fund. Scott believes that Northern Rock was an isolated case and its downfall resulted from the riskier way in which the bank conducted business. "Their reliance on the wholesale banking market meant that once the credit crisis took hold that source of funding became, to a large extent, closed. As a consequence, the bank did not have the balance sheet strength to support the enormous growth in mortgage lending, much of it at very thin margins and increasingly high loan to values, that it had financed over recent years whilst the housing market boomed. Indeed, in my view one of the main reasons for the excessive growth in the housing market was the reckless lending by the banks of which Northern Rock was the principal culprit," Scott commented. Over recent months several UK banks, such as Barclays, have also shored up their balance sheets through rights issues, placings and attracting overseas Sovereign Wealth Funds to invest in the shares. "For some banks there remains the question as to whether they have done enough as they write-off assets relating to credit instruments, such as CDOs. At the same time they are being forced to write-off loans as the UK economy appears to be lurching into recession," Scott said. "However most banks have much more diversified business models than Northern Rock that should help in the current crisis. They have now been addressing the situation

for over a year since the credit crunch started, which is why the cost of obtaining a mortgage has risen despite interest rates having fallen over the same period."

According to Scott the lack of confidence in financial markets, as evidenced by the London inter-bank rate (LIBOR) remaining well above base rate, is likely to stay with us until the housing market shows some signs of stabilising and the economy has a firmer footing. "In the meantime the banks will find it tough going and may well have to raise further funds via the equity market or selling assets but another Northern Rock is unlikely," he concluded.

Energy stocks provide spice to Indian market

According to Sam Mahtani, manager of the F&C Indian Investment Company, India is facing a 'seismic shift' in its energy position providing abundant opportunities for investors. "India's need for energy is insatiable and is driven by its rapid expansion combined with the fact that most oil and gas (75%) has to be imported", he commented. "Estimates suggest this will cost \$84bn in 2009". However, Mahtani also points to the success of Cairn India and Reliance Industries in finding oil and gas deposits in India. In addition, both companies still have extensive and promising acreage that remains unexplored. Mahtani has significant positions in both Cairn India and Reliance Industries in his fund. Over the next two years a generational shift in India's macro economic backdrop is expected as the energy discoveries of both Cairn and Reliance come on stream. Over this period both companies are set to increase output by 0.7 million barrels of oil and oil equivalent each day. This will account for approximately 0.5% of global oil production. It is also estimated that this will replace up to 36% percent of imports, the equivalent of \$38bn. "The new supplies of gas will enable a number of manufacturing plants and power stations to operate at optimal capacity thereby aiding India's economic expansion", he continued.

India currently has amongst the most heavily subsidised oil price in the world with the costs borne by the Government and producers and suppliers. So what does the future hold for energy demand in India?

Mahtani concluded: "In my view, the sub-continent is only going to go one way which should be good news for Cairn India and Reliance Industries, which have good records of oil discovery. Overall India has 26 sedimentary basins covering 3.14m sq km, which could contain oil and so far only 20% have been properly explored. This potential is boosted by the fact that in terms of new oil exploration India displays relatively low operational and exploratory risk for countries with deep-sea reserves".

Investors play a waiting game on Russia

The recent deterioration in relations between Russia and the West following the military action in Georgia has unnerved foreign investors, impacting the positive sentiment that has been built up over a number of years. According to fund manager Gareth Morgan, a specialist in the Russian market at F&C, the company has moved from overweight to neutral in its position on Russia and is eyeing developments closely. "For investors, Russia is currently at a cross roads. Many Russian stocks are now at extremely attractive valuations, companies across a variety of sectors including retail, mobile telecommunications, steel and oil are reporting strong numbers and the economy is one of the most resilient in the emerging market universe," said Morgan. "However, these tensions with Russia's neighbours and the West, combined with ongoing investigations by Russian authorities into high profile companies in the metals and mining sectors have significantly raised the risk profile for investors in recent weeks. As investors return from the holiday season, there is real potential for further capital outflows from the Russian market unless relations normalise rapidly. "At this stage it is too early to aggressively buy into the Russian market despite strong attractions at the corporate level" he concluded.

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