
The dance of the headless chickens

In the second week of September, a news search engine picked up a story from the archive of the South Florida Sun Sentinel about United Airlines filing for bankruptcy protection. The United Airlines share price dropped 75% to \$3, even recording a trade at a single cent, before the airline put out a statement pointing out what nobody had bothered to check, that the story dated back to 2002, and that UA had emerged from Chapter 11 in 2006.

In the current febrile atmosphere, facts and fundamentals are cast aside by markets obsessed by rumour and momentum. For those prepared to look beyond the panic of the day to the long term opportunity, current markets present the sort of opportunity for contrarian investors that comes along once or twice a decade. At these rare times, market sentiment and momentum are negative, but some of the fundamental indicators are improving. This state of affairs rarely lasts long.

Research by Morgan Stanley shows that a 100 basis point fall in inflation adds 1.6 to the price-earnings ratio of the market.

The list of improving fundamentals starts with the \$50 a barrel drop in the oil price, which reduces the transfer of spending power from consumers to producers by \$1.5 trillion per annum, before adding in the benefit of the drop in gas and coal prices. This has led to a sharp decline in inflation expectations, not just as shown in economists' forecasts but also in market prices. Yields on government bonds have fallen and the inflation-protected corner of the market shows this to be the result of lower inflation rather than lower real yields. Research by Morgan Stanley shows that a 100 basis point fall in inflation adds 1.6 to the price-earnings ratio of the market.

The nationalisation of Fannie Mae and Freddie Mac in the US turns an implicit government guarantee of its credit into an explicit one. What is important is its effect, a sharp drop in US mortgage rates. This is likely to underpin the US housing market, which is showing signs of bottoming out, and improve consumer confidence, thereby stimulating the US economy. Thanks to booming exports, the US economy has continued to grow, activity indicators there and in Japan are steadily picking up, in contrast to the UK and Europe.

The ECB and the Bank of England have yet to decisively cut interest rates, but it is inevitable that markets will force their hand over the next few months. The longer the delay, the greater will be the effect on long term inflation expectations. Nobody should expect a return to the easy credit conditions of two years ago with limitless low cost loans available regardless of credit risk, but

lower rates will make it profitable to lend to quality customers again and restart the process of credit expansion. This will underpin slow but sustainable growth and improving business conditions.

In the short term, markets are obsessed with the collapse or forced rescue of former financial giants such as Lehman, HBOS and AIG. This has led to extreme volatility, risk aversion and disruption to money markets, forcing the Central Banks to inject liquidity. The US authorities propose to go much further with a broad-ranging plan to restore confidence in credit markets. At present, the herd is inclined to believe that this is doomed to failure and that chaos will be permanent, but this is far too pessimistic. Confidence should, before long, be restored and markets should recover rapidly.

The biggest negative for equity markets has largely been forgotten, the continuing decline in earnings forecasts. Earnings trends appeared to be improving in the second quarter but turned down sharply in the third, with August the worst month in the cycle by some margin and September also poor. However, an excess of bad news is discounted in current valuations, with the global market on a 2008 p/e ratio of just 12.2 and a 2009 one of 10.4. For the global market to be on a fair value p/e ratio for 2009 of 16, 2009 earnings would have to fall 35% below current forecasts and see no more than trend growth of 6%-7% thereafter.

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Markets usually turn around six months before earnings trends, and the first place for that to happen could be the UK. Sterling's 10% decline against the Dollar is very good news for the UK market, over 60% of whose earnings derive from overseas. Despite this, only 45% of changes to the estimates for UK companies are currently upgrades, and aggregate growth is forecast at only 6.8% in 2008 and 6.4% in 2009, leaving the UK market on a 2009 p/e ratio of just 8.5. Nowhere is the contrast between struggling markets but outstanding value and reducing risks clearer than at home. Investors who miss the current opportunity to buy, risk a long period of regret. However, whilst we see opportunities emerging, the economy still faces large systemic risks, especially in the banking sector. Investors should seek advice before making investment decisions as perceived opportunities may be unsuitable.

FirstGroup (FGP)

Transport

Buy

Medium Risk	Year End March	2008A	2009E	2010E
Price: 550p	EPS (p)	46.3	51.1	55.2
Market Cap: £2.65bn	PER (x)	11.9	10.8	10.0
12 mth high/low: 824/487p	Net Dividend (p)	17.05	19.00	20.75
Next results: November 08	Net Yield (%)	3.1	3.5	3.8



Source: Consensus Forecast, Reuters, October 2008. Chart: Yahoo Finance, September 2008.

High fuel prices, congestion charges and parking restrictions are likely to encourage people to switch from cars to buses and trains. The companies that operate these services offer steady, long-term growth at reasonable valuations. FirstGroup is our favourite in the sector.

FirstGroup was formed in Aberdeen in 1995 but the acquisition of Laidlaw for \$3.5bn last October made it also the market leader in North America. The UK Bus division (32% of profits) is the largest in the UK, running more than one in five of all local services. Nearly 9,000 buses carry three million passengers a day in more than 40 towns. UK Rail (32% of profits) runs a quarter of the network with 275 million passengers a year, operating Capital Connect, Great Western, ScotRail and TransPennine Express. In North America (36% of profits), First Student is the largest provider of student transportation with 60,000 yellow school buses carrying 4 million every day. First Transit is one of the largest managers of city public transport systems and First Services provides fleet maintenance services. Greyhound is the only continental provider of intercity coach services, serving 3,100 destinations and carrying over 25 million passengers annually.

Effectively, First Group operates regulated local monopolies. Performance and customer service are the key to good relationships with passengers, regulators and government. Bus contracts are generally stable but rail franchises are short-term nowadays, though this could change with the next government. Safety is a key issue, but the operators have little control over investment in either the rail or road networks.

In the past seven years, EPS have risen 98%. First quarter trading was in line, with like-for-like passenger revenue ahead 6.4% in the UK Bus division and 10.7% in UK Rail. In North America, \$150m per annum of cost synergies are anticipated, while school buses achieved strong contract retention and new business. At Greyhound, a declining revenue trend was reversed. FirstGroup is hedged 100% for fuel this year, but only 30% for 2009/10. As a result, analysts' EPS expectation has declined 4.9% in the last six months even though fuel is only some 10% of total costs in buses, and less than 5% in rail. The peak of this cost pressure may now be past and operators should be allowed to raise prices to compensate. Despite a share issue in May, net debt is still some £1928m, but interest cover of 4.1x is satisfactory for such a stable business.

Cookson (CKSN)

Industrial (Ceramics)

Buy

Medium Risk	Year End Dec	2007A	2008E	2009E
Price: 458p	EPS (p)	54.4	68.4	80.2
Market Cap: £978m	PER (x)	8.4	6.7	5.7
12 mth high/low: 874/426p	Net Dividend (p)	13.0	17.0	20.0
Next results: March 09	Net Yield (%)	2.8	3.7	4.4



Source: Consensus Forecast, Reuters, October 2008. Chart: Yahoo Finance, September 2008.

Once a humble paint manufacturer known as Lead Industries, Cookson's main focus is now its ceramics division (48% of turnover and 62% of profits last year). Trading as Vesuvius, its main market is steel makers, for which it is the world leading manufacturer of furnace lining products and systems for controlling the flow of molten metal. It is also a leading supplier of specialist ceramics to control molten materials in the glass, solar panel and foundry industries.

Foseco, acquired in April for just over £600m, is a worldwide business supplying specialist chemicals to foundries. Vesuvius and Foseco both provide consumable products to handle molten metal. Their products are vital for customers' plants but only a small part of costs. Both are global market leaders with high market shares and have been able to grow faster than their markets. The wide-ranging Electronics division (33% of profits): manufactures items such as lead-free solder and solder paste, surface finish products for printed circuit boards, corrosion-proof coatings, and semi-conductor packaging materials. Precious Metals division (5% of profits) is a leading supplier of alloy materials, semi-finished and finished jewellery in the US, UK, France and Spain. Europe accounted for 34% of total revenues in 2007, the North America 31%, Asia-Pacific 27% and the rest of the world 8%.

Whilst the past is somewhat chequered, margins have steadily improved since 2003 and EPS have increased from just 1.1p to 54.4p. Recent interims beat expectations, with revenues up 10% (excluding Foseco and currency movements). Pre-tax profits and EPS rose 45% and 32% respectively. Consensus EPS expectations have risen over the past six months, by 14% for this year and 21% for 2009. Foseco's annualised contribution to operating profits is already over £80m, compared with £50m before its acquisition in 2007. Global steel production has grown by 7-8% annually over the last five years, driven primarily by demand in India and China. Growth has now slowed but was still 5.7% in the first half. Vesuvius is also benefiting from the growth of continuous casting which now accounts for well over 90% of steel in developed markets.

Last year, the margin on sales and return on capital were 8.2% and 42.7% respectively. Net debt was £721m following the Foseco acquisition, but interest cover remains comfortable at some 7.9x. Cookson's prospective 2009 P/E ratio is at a 25% discount to the UK Capital Goods sector.

May Gurney (MAYG)

Construction Services

Buy

High Risk	Year End March	2008A	2009E	2010E
Price: 205p	EPS (p)	18.5	21.5	23.5
Market Cap: £143m	PER (x)	11.1	9.5	8.7
12 mth high/low: 345p/195p	Net Dividend (p)	4.6	5.0	5.5
Next results: Dec 08	Net Yield (%)	2.2	2.4	2.7

Source: Consensus Forecast, Reuters, October 2008. Chart: Yahoo Finance, September 2008.



Some of the least exciting businesses prove to be the most successful and May Gurney is a classic example of this. It came to the market in June 2006 at 186p and its share price nearly doubled in just over a year. Since then, and despite continuing its excellent growth record of nine years of unbroken growth under the current management, the shares have fallen back with the market. This provides an excellent buying opportunity.

The company describes itself as a “dynamic, integrated, support and construction services company providing maintenance and enhancement services to the highways, rail, utilities, municipal waste and general infrastructure markets particularly within the public and regulated sectors with a national customer base.” The recently appointed Chairman, David Sterry, was previously the Chief Executive and led a successful management buy-out in 2001. Under this management, May Gurney has grown both organically and by acquisition.

The maintenance services business represents 67% of the business although this will rise to around 80% following the recent acquisition of ECT Recycling. There are three main services: Highway Maintenance, which includes surface dressing, gully clearing and street lighting; Municipal Waste Services, where they run a number of household waste recycling centres and undertake waste and recycling collection;

and Utility Services, which include waste water improvements, electrical, gas and mobile telecom maintenance and inspection.

The remaining third of the business is Engineering and Project Services. This includes environmental engineering, flood defence and coastal management (May Gurney is a preferred contractor for the Environment Agency) and public building enhancement. In the rail sector, they undertake structural work such as embankments, bridges, signal boxes and stations on behalf of Network Rail.

Apart from Network Rail, which represents around 15% of the business, their other significant customers include Southwest Water, Norfolk County Council and National Grid, all of which represent around 10% of their business. A recent AGM statement indicated that the order book had continued to increase to in excess of £1 billion and they had managed to extend their Norfolk County Council contract to 2012. They also have other long term contracts with Essex, East Sussex, West Sussex and Northamptonshire councils.

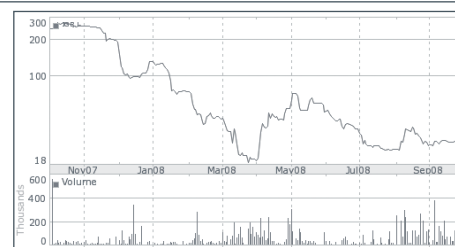
Recent figures to March 2008 showed revenue up 8% at £437 million, underlying profits up 15% to £18.7 million and earnings per share up 9% to 18.5p. The business is highly cash generative and has no debt. The shares are highly attractive in these uncertain markets.

International Greetings (IGR) Gift Wrap/Cards

Buy

High Risk	Year End March	2008A	2009E	2010E
Price: 29p	EPS (p)	29.5p	-	-
Market Cap: £14m	PER (x)	1.0	0	0
12 mth high/low: 282p/17p	Net Dividend (p)	10.0p	2.0p	2.0p
Next results: Feb 09	Net Yield (%)	34.4	6.9	6.9

Source: Consensus Forecast, Reuters, October 2008. Chart: Yahoo Finance, September 2008.



International Greetings is one of the world's leading designers, innovators and manufacturers of gift wrap, crackers, cards, stationery and other accessories. It was established in 1979 by Anders Hedlund, has grown both organically and by acquisition, and floated on AIM at 50p per share in 1995. In ten years, the shares rose by more than eight times as the company became the largest player in the UK market with around a 40% market share. It had a turnover of £197 million producing pre tax profits of £18.1 million and earnings per share of 29.5p.

Unfortunately, last July, when the share price stood at 417p, it produced its first profit warning, indicating a slow-down in the UK retail climate. This proved to be just the start of International Greetings' problems. Despite the Directors buying shares at 255p in September 2007, the company issued another profit warning in December 2007 in which it indicated that results would be materially below expectations. This led to the founder standing down and Paul Fineman, whose own Anker business had been acquired in 2006, became Managing Director alongside Nick Fisher, the Chief Executive.

In February, following a review of the business, the company said that it had seen a further significant slow down in the business not helped by

manufacturing inefficiencies, additional freight costs, higher than anticipated bad debts and increasing stock provisions. The company's share price fell to around the current level, more than 90% below its peak. In April, the company announced a reorganisation, rationalising its UK manufacturing facilities, closing its Latvian factory and moving manufacturing operations to China. The full year figures announced in August showed a loss before tax of £3.1 million, a loss per share of 3.2p and no final dividend.

Clearly, the story has been a disaster but the company still has a turnover of nearly £200 million and appears to have lost very few customers. Under the direction of Paul Fineman, the company has started to get back on track and should produce a small profit in the current year. It has debts of £64.8 million but an overdraft of £90 million has been renewed for a further twelve months. 40% of the workforce has been made redundant enabling the sale of a number of sites to reduce debt in due course. The shares are high risk but we believe they have a very significant recovery potential.

Review of Past Recommendations

COMPANY	DATE	RECOMMENDATION	RECOMMENDED PRICE (p)	CURRENT PRICE (p)	CHANGE (%)	RELATIVE TO ALL SHARE INDEX (%)	CURRENT RECOMMENDATION
Smith & Nephew	Sept	Buy	636	573	-10	+3	Buy
Bunzl	Sept	Buy	662	673	+2	+15	Buy
Rotork	Sept	Buy	1074	921	-14	-1	Buy
Dignity	Sept	Buy	730	690	-5	+8	Buy
Cadbury	Aug	Buy	604	558	-8	+1	Buy
Marks & Spencer	Aug	Buy	239	225	-5	+4	Buy
Spice	Aug	Buy	101	110	+9	+18	Buy
MDM Engineering	Aug	Buy	188	145	-23	-14	Buy
Reckitt Benkiser	July	Buy	2605	2785	+7	+18	Buy
Mothercare	July	Buy	328	343	+5	+16	Buy
ACM Shipping	July	Buy	242	200	-18	-7	Buy
Begbies Traynor	July	Buy	163	171	+5	+15	Buy

Prices as at 2 October 2008

Banks: there has been a fundamental shift in the structure and outlook of the global banking sector in recent months. Consolidation has created some clear winners in the UK sector. We view the Barclays deal to buy Lehman Brothers' US trading assets and the Lloyds TSB takeover of HBOS as beneficial to both sets of shareholders. Barclays has, in effect, bought itself a very large stake in the US investment banking for as little as \$250m whilst the enlarged Lloyds TSB will have almost a one third of the UK mortgage and retails savings market. Once the dust settles on the sector, we see both Barclays and Lloyds TSB outperforming. We already have Lloyds TSB on our buy list and we now have added Barclays. We are also positive on HSBC (strong balance sheet and global reach) and Standard Chartered (Asia exposure) but suggest switching out of RBS due to its stretched balance sheet and the poor outlook for the ABN AMRO business.

BG (1009p) Buy: BG pulled out of its £6bn bid for Origin Energy after the Australian management sealed a deal to sell 50% of its coal-seam gas business to ConocoPhillips for £4bn. Although this was a strategic blow for BG, it was encouraging that they did not overpay for assets. BG has strong growth in its LNG and Oil & Gas production business which should generate excellent returns for shareholders over the medium and long term. The potential of its stake in the giant Brazilian Santos field is not fully reflected in the share price. In time, we see BG as being a takeover target but in the meantime the shares are supported by fundamentals. BG remains our top pick in the sector.

Cape (225p) Buy: The half year results showed growth in turnover of 58% although this was helped by acquisitions, a 103% rise in adjusted operating profit to £29.9 million and an increase in adjusted earnings per share of 28% to 13.1p. Cape also generated £26.1 million of cash from operating activities which helps to reduce net debt. The management announced that the 2008 full year results will be ahead of market expectations, helped by strong progress in both the energy and natural resource sectors. Cape also announced that it will join the main market in the second quarter of 2009.

Aero Inventory (358p) Buy: The full year results were at the top end of expectations with revenue up 78% to \$440 million, pre tax profits up 60% to \$73.1 million and earnings per share up 65% to 108.7 cents. The dividend was increased by 20% to 12p giving a total for the year of 18p per share. The company continues to benefit from airlines needing to outsource as many of their services as possible in order to cope with fuel costs and recession pressures and this has led to Aero Inventory receiving a record number of enquiries. We continue to regard the shares as a strong long term investment.

Clapham House (90p) Buy: The recent AGM statement indicated that trading continued to be satisfactory. The company now operates from 82 locations including 53 Gourmet Burger, 23 Tootsies and 6 Real Greek restaurants. Gourmet Burger continues to be one of the fastest growing restaurant chains in the UK despite the difficult conditions the sector is experiencing. The sale of the Bombay Bicycle Club reduced the company's debt substantially and the shares remain a buy particularly with Capricorn Ventures owning 25% of the company.

CVS Group (212p) Buy: CVS produced its first full year figures following flotation last year and these showed revenue up 59% to £62.15 million, like-for-like cash-flow growth up 12% at £6.3 million and strong cash generation from operations of £8.27 million. The company continues to have first mover advantage with a 7% market share on a national basis operating from 151 surgeries. We believe this company to be relatively recession resistant with a strong management and the shares remain a buy.

Plant Health Care (315p) Buy: The latest interim figures showed revenue down slightly to \$7.9 million but this was due to the discontinuance of one product in the US. The loss before tax at \$3.335 million was inline with expectations and the company announced a multi year supply agreement with Scotts in the US. Since the results the company has announced a further deal with Bayer Crop Science and we expect other significant deals to be signed within the next few months.

Collectives & Managed Investments

Equity markets continue to be under pressure from the uncertain state of the global economy. One week there is the threat of a banking meltdown the next, an economic crisis characterized by huge trade deficits and the excessive increase in money supply. We do not know how severe the current problems will be or how long they will last. We believe that when the outlook is at its gloomiest, investors should start to increase their exposure to equities.

Warren Buffet's recent investment in Goldman Sachs may be an example of this, as may Anthony Bolton's comment that equity prices were near their low. Following their example is surely tempting, but the question is in which specific area to invest. We think the US authorities have been the most proactive in their handling of the recent economic issues and are likely to cause the US economy to enjoy modest but sustainable growth. In turn, this should be positive for the US Dollar as US interest rates rise from emergency levels and rates elsewhere fall. For these reasons we would suggest investors consider an exposure to **North American smaller companies**, a sector of the market which offers good growth prospects and should be a part of a well diversified equity portfolio.

Smaller companies are now under-valued relative to larger companies the world over, have better growth prospects and managers have more opportunity to add value over the indices.

Fixed Income Research

All eyes have been on the massive problems in the banking and insurance sectors over the past month, causing substantial moves in both the currency and bond markets. The trend is towards risk aversion, benefiting government and supranational bonds at the expense of corporates and major currencies at the expense of smaller, higher yielding ones.

There are increasing signs of a slowdown in Europe with the European Central Bank cutting their 2008 growth forecast from 1.8% to 1.4% and their 2009 one to 1.2%. Germany is expected to achieve 1.8% this year but Italy has no growth at all. In Spain, house prices are expected to fall a further 20% this year. Additionally the European purchasing managers index (PMI) has fallen to a six year low. The ECB is maintaining rates at 4.25% but is likely to reduce them as soon as inflation is past its peak.

In the UK, the CPI rose once again to 4.7% but we are near the peak and inflation should move back down towards 2% over the next year. This is likely to give the Bank of England the opportunity to cut rates to 3.5% before long. There are signs of inflationary pressure easing as factory output prices fell 0.6% in August. The softer currency led to a 3.1% pick up in exports although overall manufacturing activity fell 0.2%. The economy will probably shrink by 0.3% to 0.4% over the second half of 2008 before turning up some time next year.

Over the past 5 years, the average UK smaller companies fund has outperformed the FT Small Cap index by over 5% a year. Since there are few banks in the small cap sector, it has been relatively unaffected by the banking disasters. We think that investors, where suitable, should now add to their holdings in smaller companies before the news flow improves and the herd piles in.

The volatility and risk of individual smaller companies, despite the better average performance, is a good reason for investors to opt for a diversified portfolio with funds managed by specialists who devote their whole time to the sector, especially those who have expertise in overseas markets. For these reasons, we recommend the **Findlay Park North American Smaller Companies Fund**.

The **Findlay Park North American Smaller Companies Fund** was launched in 1998. In the past 12 months to August 31st it has returned -2.18% versus -6.73% and -12.97% for the Russell 2000 small cap index and S&P 500 respectively. In the past 10 years, it has achieved an annualized return of 18.2% versus growth of 9.3% and 4.5% achieved by the above indices. The fund is currently £3.4 billion in size. Approximately 66% is invested in the US, 9% in Canada and 8% in Latin America. 16% is currently invested in cash or fixed interest, a tactical move by the managers whilst they look for attractive buying opportunities.

Unemployment in the US rose to a five year high of 6.1% while the recovery in retail sales fizzled out, dropping 0.3% in August. The root cause of this problem, the housing market, is down 5.3% over the past year – not as bad as many expected but foreclosures are at a 29 year high. The bold action by the US Treasury regarding Fannie Mae, Freddie Mac, AIG and the toxic loan fund will hopefully start to draw a line under all the mortgage problems and enable the economy to start recovering. There has been concern regarding the amount of government debt after these actions but it is still significantly lower in percentage terms than the debts of Germany, Japan and Italy.

While we worry about our economy shrinking by 0.4%, spare a thought for Japan – whose economy shrank by 3% annualised in the second quarter.

The currency markets have been volatile though the US Dollar has strengthened. During the past two months, the Euro has moved between 1.59 and 1.40 – a 13% range while Sterling has bounced around between 2.00 and 1.76. This turbulence has caused a flight to quality with higher yielding and emerging market currencies being particularly hard hit. The Turkish Lira and the South African Rand are down around 8% but hardest hit are the Australian Dollar and the Brazilian Real which are down 18%. Volatility is set to continue but if the US Treasury plans go ahead and are to largely successful, we anticipate a further

strengthening of the Dollar. In due course, once the current panic has subsided, currencies like the Australian Dollar will offer good value again.

The flight to safety has benefited government bonds and Treasury Bills. At one point, 3 month US Bills were yielding nothing at all. Two year US, German and UK yields fell to 1.6%, 3.6% and 4.0% respectively and 10 year yields to 3.4%, 4.0% and 4.4%. There have been large inflows into these bonds.

The desire for safety has pushed most corporate yields up, especially those of banks and insurance companies. The selling

of perpetual bonds and preference shares of these issuers has caused yields to rise three to four per cent. Even GE, which is AAA rated, has lost ground with the 6.75% June 2018 bond yield rising from 6.6% to 7.1%. The best performance has come from companies who are perceived as 'bomb-proof', like the Cadbury 7.25% 2018 which has rallied around 50 basis points in price to yield 7.0%. Although bank issues are very volatile at present, we believe that carefully chosen corporate names in solid business areas like mining and oil industries offer good yields to lock in for the medium term.

Sterling Bond Investment Opportunities

The recent turbulence in the bond markets has caused some enormous movements in corporate bond prices and yields. Most affected have been the non-bullet bank name issues where fears that perpetual and preference share issues may not be repaid if the turmoil continues have led to a massive sell-off. Although this may be justified in more exposed bank names, we believe that the more solid institutions like Lloyds TSB and Standard Chartered, will ride out the storm and therefore this spike-down in prices offers an opportunity for the more aggressive investor.

Elsewhere yields have also continued to rise but, if the borrowing company is sound and with reasonable prospects, these higher yields also offer an investment opportunity. Many of these yield rises are caused by a combination of panic selling and mark downs by banks and brokers who do not wish to take stock on to their books, whatever the quality of the issuer.

Below we list a few issues that we believe are attractive at current levels. There may be further weakness in the short term but these companies are expected to be able to finance their liabilities.

All of these issues, apart from British Airways, are investment grade. Imperial Tobacco, Cadbury and Lloyds are all very solid companies. Next and Kingfisher, although suffering from the downturn in consumer spending, are weathering the storm and the Daily Mail's circulation is holding up despite advertising revenues slipping. We have recommended British Airways before, at a higher yield. HBOS*, assuming the takeover by Lloyds TSB goes through, should be substantially re-rated, but you may wish to wait for the takeover to be completed. These opportunities are there at present, but may not be for long.

BOND	RATING	PRICE	YIELD TO REDEMPTION
Imperial Tobacco 6.875% 2012	BBB	98.80	7.23%
Next PLC 5.25% 2013	BBB	85.50	8.98%
Kingfisher 5.625% 2014	BBB-	83.50	9.22%
*HBOS 6.0884% 2015 ¹	AA	60.80	15.80%
British Airways 7.25% 2016	BB+	93.25	10.00%
Cadbury Schweppes 7.25% 2018	BBB	101.10	7.02%
Daily Mail 5.75% 2018	BBB	76.50	9.43%
BUPA 6.125% 2020 ²	A-	76.00	9.58%
Lloyds TSB 8% 2023 ³	AA	105.00	7.42%

¹callable 2015 ²callable 2020 ³callable 2023

Mid market indications taken as of 2 October 2008

SIPPS, ISAs, IHT - changes afoot

David Goodfellow of our affiliated company, Eden Financial Advisers Limited, highlights a few financial issues for consideration.

SERPS, S2P and SIPPs

In the last Eden View we highlighted that a large number of people had contracted out of the State Earnings Related Pension Scheme (SERPs, more recently becoming the State Second Pension, S2P), through insurance companies' 'contracted out' policies, predominately in their Managed funds. Many have subsequently contracted back in, but still have the insurance company scheme, with no additional funds being paid, often forgotten but still in some poorly performing funds. We urged clients to review these policies as these policies can now be transferred to a SIPP structure, allowing the underlying investments to be more actively managed.

The SIPP structure may not be suitable for everyone, but a simple review of the performance of those funds may reveal some relatively poor performance as an August survey identifying 92 'dog funds' suggests. The SIPP structure that Eden Financial Advisers utilises will allow these contracted out policies to be transferred with effect from the beginning of December, providing a little time for a review of the policies.

Pensions still represent a tax efficient method of saving for retirement with up to 40% income tax relief on contributions up to 100% of earned income.

Pension investments

With the worldwide investment markets suffering, now may be a good time to make pension contributions, for those in a position to do so. Pensions still represent a tax efficient method of saving for retirement with up to 40% income tax relief on contributions up to 100% of earned income (to a maximum of £235,000 during the 2008/09 tax year), funds growing in a tax efficient manner and on retirement 25% of the fund being able to be withdrawn tax free. However, investors should also remember that to obtain the relief certain restrictions apply such as that access is only allowable from age 55 and that 75% of the fund must provide a pension income, which is taxable.

By making a pension contribution prior to the end of January rather than in the first few days of April it may be possible, in some circumstances, to reduce tax payments on account. As ever, professional advice should be sought in relation to the amount of the contribution, the tax implications and the pension structure used.

PEPs and ISAs are amalgamating

In May, we reminded clients that from 6 April 2008 all Personal Equity Plans (PEPs) would become 'stock and shares' Individual Savings Accounts (ISAs) and that clients should review the performance of the array of sundry PEPs and ISAs collected over the years. Eden Financial Advisers Limited can assist with any review and analysis.

Clients should also be aware that Eden Financial Limited will be amalgamating all clients' PEP and ISA accounts in November which should reduce paperwork and future administration.

Inheritance tax planning

With asset values falling over the last 12 months and Messrs Osborne and Cameron announcing proposals that they will increase the nil rate band to £1 million per person (ie £2 million per couple) upon change of Government, many clients have become more nervous about committing to long term IHT solutions. However, doing nothing on the basis that a Conservative government will immediately change this IHT 'allowance', may not necessarily be sensible as future events may not necessarily pan out as expected. Not all IHT planning needs to be irreversible.

Many clients will still have an IHT liability even if the Conservative proposals become reality, but those who may fall out of the IHT net in the future should still ensure that they have considered the options in the short term.

Clients wishing to consider any of the above proposals should contact David Goodfellow on 020 7509 7475 or by email on david.goodfellow@edenfinancial.com.

Our advice is based on our current understanding of the law and practice of taxation, pensions and investments.

Where any reference in this communication is made to tax, it should be noted that tax reliefs or rates assumed are those currently applying, whereas their value will depend on the individual circumstances of the investor. Levels and bases of, and reliefs from taxation, are subject to change.

The Financial Services Authority does not regulate taxation and trust advice, the Alternative Investment Market and some aspects of offshore investments. Our advice is intended to be used as a basis for further discussion and transactions should not be implemented before that takes place.

The past performance is not a guide to future performance and should not be used to assess the risks associated with the investment.

Eden Asset Allocation Framework

EQUITIES unchanged after intra month increase

Equity weighting maintained at 50% of portfolio, despite short-term uncertainty. Value is excellent, bond yields are supportive and sentiment is reassuringly very negative, though earnings downgrades continue.

US Equities

Neutral (mixed) . Economy and earnings growth likely to recover 6m before elsewhere but valuations are lower elsewhere.

UK Equities

Focus on overseas earners and mid sized companies. Buy selected banks, resource stocks, consumer staples and quality industrials. Neutral on aerospace, negative on telecoms and utilities, buy pharma and tech elsewhere.

Europe ex-UK

Neutral. Low valuation compensates for poor earnings growth. Small & mid cap attractive.

Japan

Neutral. Disappointing at present, earnings trends are dire but long-term potential is great.

Asia Pacific ex-Japan

Positive. Value has improved to excellent.

Emerging Markets

Positive. Value is now excellent and earnings growth is good.

FIXED INCOME

Maintain exposure at 25% of portfolio.

Developed Markets

10 year Gilts & German Bunds neutral, US Treasuries expensive.

Corporate bonds

Positive. Higher grade bonds and high yield are attractive relative to government bonds, but the recent treatment of bond and preferred holders of financials means that investors need to be highly selective.

Emerging Markets

Good opportunities in local currencies, avoid "hard" currency debt.

ALTERNATIVE INVESTMENTS

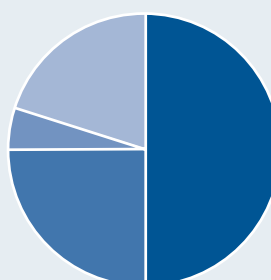
Maintain exposure at 20% of portfolio.

Private equity funds are on very attractive discounts. Listed property funds are cheap but fundamentals are negative. Gold equities are cheap relative to the gold price. Need to be very selective in hedge funds for now but opportunities will return.

CASH AND CURRENCIES

Maintain the cash exposure to 5% of portfolio

Those with cash shouldn't invest down to 5% just yet. The \$ is good value again.



Model Weights for Moderate Global Multi-Asset Portfolios

- 50% Equities
- 25% Fixed Income
- 5% Cash
- 20% Alternative Investments

Recommendation Guide

Buy +20% expected absolute price performance over next 12 months

Hold +10% to -10% expected absolute price performance over next 12 months

Sell -20% expected absolute price performance over next 12 months

Eden^{Financial}

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