

ARTICLE FOR THE HERALD FUNDAMENTALS

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Turning points in the stockmarket are never easy. Only with hindsight can we see clearly that the last bull market began in March 2003. March 9th 2009 may come to be seen as a similar turning point. History has shown that few investors have perfect timing. Indeed, 2008 saw several false dawns – bear market rallies that even deceived some high profile investors who called the turn too soon. Investors should not try to make an all-or-nothing bet on timing. Leaving funds invested or continuing with monthly savings is the surest way to participate in a rebound.

Some key economic indicators now point to a more powerful and sustainable rally than those of 2008. Stock-building of metals and other commodities by China has lifted mining shares from extremely oversold levels. The key Baltic Dry Index, which tracks international shipping prices of bulk cargoes, has also shown a sharp recovery. Prices of copper, iron ore and oil are all recovering, and well up from lows. While there is, as yet, a lack of clear confirmation from US housing and employment of a new bull market, there are other favourable signals.

The huge scale of US and European bail-outs of industries such as banking and autos, has provided unprecedented stimulation to Western economies. And, while the recovery in bank profitability falls well short of what is needed to repair damaged balance sheets, the problems may not be revealed till 2010. There is a willingness by governments and regulators to put off the day of reckoning for banks, in terms of reflecting the true value of loan impairments. Stockmarkets and consumers have been primed to receive just good news. This has undoubtedly improved confidence, even if it is not the stuff of a multi-year bull market.

At the same time, many industrial companies have already completed significant cost cutting. Restocking will quickly feed through into recovering profits. And, quantitative

easing by the Bank of England has supported insurers and investment banks via bond purchases, helping them to finance new capital raising by distressed companies.

Not all business problems are easily resolved. Some challenges – for example, in media – are not just cyclical, but reflect broken business models. Consumers are moving more activity online, impacting print media and the high street. Many consumer businesses are in competitive areas and are less attractive opportunities for refinancing than industrial businesses with global leadership in their niches.

The recent refinancing of some industrial businesses has put them in good shape for recovery. The financing window may not remain open long enough, however, to benefit all small and medium size companies or those with deeper rooted problems. Pension fund deficits are one of these challenges which could have serious implications for future dividend payouts in companies like BT. Even in a stockmarket rally, investors should recognise that some sectors have continuing problems.

Stockmarket signals are mixed. Some point to a much briefer bull run than 2003 – 2007, and lower global growth in future. There will be more government intervention and less bank finance for companies. Although confidence has improved, consumer sectors still face the challenges of rising unemployment and a need to increase savings rates. Investors should focus on larger and medium sized businesses in the sectors that will benefit from stimulation and bail-outs.

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