

TAM INVESTMENT NOTE

February 2009

Obama; No Quick Fixes



Many had hoped that the inauguration of President Barak Obama would ignite investor optimism and kick-start both the US economy and global stock markets. However during his inauguration week we witnessed one of the most serious losses of confidence in the global banking system which left many financial companies teetering on collapse. So will there be any “Obama-effect” and how will the new democratic government cope with the worsening economic situation.

No one can predict the future but there are some very consistent statistics about presidential terms and economic growth; statistically, over many administrations first year of a president's term is a bad one with the lowest stock market return (with the FSTE 100 already down over five percent it's not hard to imagine), the second year is a little better, the third the best year of all. So from historical point of view 2009 may not be year of recovery that many are hoping for with 2010 looking more likely to be pivotal. But, such statistical analysis aside, how will the democratic election promises (should they actually be implemented) effect the stock market?

Tax cuts for the middle class should be a positive for the stock market as consumers (who account for 70% of GDP) will have more money to spend potentially increasing corporate profits and corporate returns. **Healthcare reform** is a mixed bag as it could reduce profits for many insurance companies and some healthcare providers. Equally, however, it may also leave more money in consumers' pockets, which should stimulate the economy. **Raising the capital gains tax** would most likely have a dampening effect on the stock market. Taking away the benefit of a lower long-term capital gains tax removes the incentive for many investors to hold onto their investments for the long-term, and an increase in short-term trading has proven in the past to be detrimental to the value of the stock market.

Given all of the above we at TAM are taking a more pragmatic view; we need change, some tough choices to be made and a wiliness to shake the established order before we climb out of the current downturn; and change is what Obama promises. But more importantly the new government's hands are not as bound as the out-going with any about-face in policy potentially

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applauded rather than ridiculed; we therefore expect stimulus and bail-out packages extensions followed by penalties for those who do not help facilitate a more democratic distribution of wealth. Any such change takes time causing us to anticipate a volatile but moderately flat year ahead for stock markets before the start of a more promising 2010.

Disappointingly the first announcement outlining the Obama stimulus plan was very short on detail as to how the current financial crisis will actually be tackled and side stepped the important questions of addressing how to rid banks of the toxic mortgage assets clogging their balance sheets, or set out the scale and terms of further government cash infusions for the most troubled banks. Following statements from the US Treasury Secretary that this was only "the broad architecture" of the stimulus package, with details to be fleshed out in the coming weeks downgraded the "plan" to simply a "plan of the plan"! Are discontent with the lack of clarity was clearly shared with investors who demonstrated their dissatisfaction though the sharp falls in global equity markets that accompanied the plan's announcement.

The speed at which such negative sentiment can flood back into the financial markets further supports the current positioning within our portfolios. We are maintaining a lower-than-normal exposure to the equity markets through both reduced outright exposure and through the use of absolute-return focused funds. Additionally we are complimenting these long-term core holdings with more opportunistic short-term direction positions. Similarly we have increased our exposure to the Sovereign debt markets (core holdings that have resulted in significant out-performance) anticipating short-term strength in these markets even in the face of historically low interest rates. We do however expect this market to capitulate once some stability returns and any risk premium diminishes.

In summary we have adopted a pro-active approach to building our core exposure to the equity markets during times of market weakness, whilst consolidating short-term gains generated as a result of the high levels of volatility still being exhibited. We therefore expect our portfolios to continue their performance trend and be appropriately positioned when prolonged strength returns to the market.

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