



# *capital eyes*

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In this edition we focus on some larger geopolitical issues, we look at the still evolving story of General Motors and we canvass some views about the future for investment markets.

**Geo-political Issues**

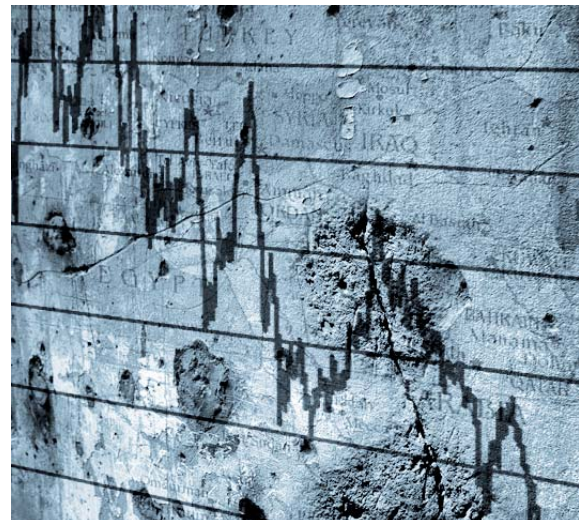
**The General Motors Story**

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## [ **Geo-political Issues**

Since geo-political stability is one of the major factors in market stability and also performance, it is interesting to observe some recent events. There are some encouraging signs of progress here and there. Two of the worst bear markets in the last one hundred years have occurred in the last decade. The latest one has wiped out more than fifteen trillion dollars (US) of asset values affecting every asset class, every market and every investor in some way. Amidst all the upheaval, signs of stability in some regions are indeed welcome.



Problems in the Middle East caused major market disruption in the early 1990s so it is gratifying to observe recent initiatives by US President Obama to find long term solutions. He has made an impressive start demonstrating an ability to bridge divides and open channels for relationship-building with conciliatory language. This is providing an opportunity for politicians and ordinary people alike to look for common ground rather than stirring up the conflicts of the past. Israel has also agreed to come to the table in terms of recognising a Palestinian state and while there is a long way to go, there are encouraging signs.

Strategically important for Israel is Lebanon. Elections there surprised many by illustrating less support for the Iranian-backed Hezbollah. A desire for a more moderate political leadership by that country is a determining factor for the region.

In Iraq, US troops have pulled out of the cities in their staged exit from the country. Iraqi security forces now face the inevitable test of their resolve from the insurgents, and it's anticipated that they will be successful in holding the line. The successful withdrawal of US troops will remove the antagonism and noise from the region and allow the local security forces to address the issues in terms of criminal acts and sectarian violence instead of the elevated rhetoric of fighting the imperialist forces of the US.

Iran has seen unprecedented violence and challenge to the status quo. Some in the West have seen this as a challenge to the Theocracy. It's more complex than that and the Opposition is not calling for a dismantling of the system. At the very least it's encouraging to see an emphasis on the desire of the population to have their votes counted and achieve a type of modern democracy. Ultimately this would bring more accountability in terms of Iran's activities in the region and a softening of the rhetoric towards Israel and a more stable Middle East.

The Pakistani Government's willingness to engage the Taliban militarily has eased some concerns about the Taliban gaining control of a nuclear arsenal. Government forces

are experiencing some success in routing the Taliban. This complements a renewed effort by the US led coalition over the border in Afghanistan which will gain momentum as forces are released from Iraq. This won't have escaped the insurgents, which is why security forces in Iraq will be sorely tested.

All of this is important in terms of the general level of oil prices, its supply and the volatility of prices. If the region keeps moving toward greater political stability and is able to deal with the security issues (insurgents), it may become far more settled. The result of this would be a more stable environment for oil production and lower price volatility from geo-political issues. That could be critical as the global economy pulls out of recession.

## The General Motors Story

General Motors Corporation was once the largest company in the world. What followed was twenty years of producing cars that consumers either didn't want to buy or, in hindsight, shouldn't have bought. All the while, costs spiralled.



After September 11th 2001, GM and other car manufacturers in the US were encouraged to build huge numbers of Sports Utility Vehicles (SUVs). They were purchased either with no interest loans or "cash outs" from home loan re-financing as a stimulus to the economy suffering the after shocks of the "terror attacks" and earlier "tech wreck".

The SUV boom certainly helped as, like the other auto-makers, GM simply used the small truck chassis they already had and fed the SUVs into the market. This was highly profitable for the whole industry until oil spiked and, along with concerns about the environment and the safety of these vehicles (1,000 deaths a year from rollovers), sales fell away. It was never going to be enough for GM anyway.

With plummeting sales over the last year as a result of the credit crunch, the tortured decline was finally over. Despite bailout money from the Government GM, once the largest company in the world, went into Chapter 11 bankruptcy.

They were in bankruptcy for 39 days and have now emerged as the General Motors Company. Some brands have been dropped, twenty-two thousand employees have been fired and fourteen hundred dealers have shut their doors. They have closed some plants and are re-tooling others.

Will this be enough? Will they survive? The jury is definitely out on this one, despite all the rhetoric. What we do know is that this event and period going forward is quite different and we can't use the old rules to give us a view of the future – maybe we never could anyway.

This credit crunch and subsequent recession is exposing any weakness in strategy, management and products and services. The need to survive is forcing new thinking, re-tooling, re-assessment and, above all, change. Failure is a catalyst for change but only time will tell whether the changes GM is making will be enough.

# Investment Markets

Earlier this year the global markets asked: “Are we there yet?” The answer came back that “green-shoots” had been spotted and markets rallied. There were signs that the developed world, especially the US, was “turning the corner”. Have those green shoots withered and died or will they flourish yet?

It was February this year when Bernanke first talked about green-shoots. At the time, markets had been heading south for some time but the rate of decline was easing. An absolute melt down in the banking system had been averted and relief in a range of areas had begun to occur. Businesses have had to restructure to survive this recession so a major casualty has been employment. The US lost 2.1 million jobs in the first quarter this year and 1.3 million jobs in the second quarter. Similar trends are occurring here and in most other economies on a global basis.

## Initial and Continued Unemployment Claims



In Europe, green shoots have been much more elusive and there are large discrepancies in the health of the various EU members. We have the “power-houses” of Germany and France and the now basket-case Ireland. And in Spain for example, there is massive unemployment running into numbers in the mid-teens in some regions. This is disturbing for such a developed economy.

Japan is also experiencing problems. Toyota, a paragon of commercial prowess, is closing plants and not just those in Japan. Japan’s exports have fallen sharply and this had created a predictably negative impact in the region. Australia is approaching recession for the first time in this cycle. Amazingly the “lucky country” has been travelling quite nicely through the turmoil.

Low interest rates remain. That stimulus to growth is still very much needed and rates are unlikely to move up for a while. Our Reserve Bank has stated interest rates will remain low

for the rest of this year and into 2010. Low mortgage interest rates and other incentive packages are assisting house prices. Construction of homes in the US rose in May and June and prices in US large cities are moving up again for the first time in three years. We have some upward movement going on in our local property market and, in Australia, there is already concern being voiced about the next housing-related binge. Buyers are getting “drunk” on the low interest rates.

The recovery in markets is occurring more quickly than it would have done without the bailouts but a very deep hole has been burnt in the overall position of most investors.

At the time of writing, the Standard & Poor’s 500 Index was at its highest level in more than eight months and the MSCI World Index was at its highest level since November 4th 2008. The MSCI Asia Pacific Index was higher than it had been since October 2nd last year.



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But are we there yet? Resoundingly, the answer is probably “no” and, more to the point, what “there” means is open to debate. If it’s true that humans learn far more from failure than success, then there will be some dominant themes the past has taught us about what is required for the future. **Transparency and simplicity** will be key. The convoluted, securitised products of the past failed so perfectly that the memory will endure long after any recovery. **Liquidity** will be another major driver. Being locked in is as painful as loss, perhaps more so. Assets that can be easily

liquidated, even at the expense of lower return, will be the order of the day. Core assets have those attributes. They are simple, transparent and liquid. There will be opportunities for what one writer calls “Core and Explore”, holding simple, transparent and liquid assets with some exploration into **some targeted active management** around the fringes. Lastly, **reducing costs** and getting **tax efficiency** will be needed. Clients of Capital Investment Planning Limited will be aware of the changes being made to achieve these key features at present.

## Annual Volunteering Day 2009

On 17th June, the Team at Capital closed the office for its annual volunteering day. Trees for Canterbury was our chosen organisation this year. We weeded and repotted seedlings as well as undertaking some planting in a nearby local reserve. It was an enjoyable day doing something quite different. We learnt about the organisation which makes such a positive contribution to our community.

Trees for Canterbury is run by the Green Effect Trust. Its objectives are to

- **Employ.** They involve disadvantaged people (physically, intellectually, socially and long term unemployed), providing an environment of acceptance as well as support and training for self development, installing self esteem and good work habits.
- **Educate.** The Trust educates people about environmental awareness.
- **Regenerate.** They cultivate native plants for sale and community planting.



Trees for Canterbury operates from 1.5 hectares of land situated at 42 Charlesworth Street, Ferrymead. They have approximately 150,000 plants at various stages of growth within the nursery. Two-thirds of the output is utilised in community and revegetation projects whilst the remainder is sold at the nursery to provide some self-funding. The nursery is open 7 days a week and is definitely worth a visit if you are looking for native plants.

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