

PORTFOLIO INTERIM SUMMARY

May 2008

I have delayed creating Portfolio Interim Reports when they will predominately just restate the continuation of the predictions made in recent issues. However just recently a number of important events have occurred, which I believe are significant. Last week the Swiss Bank UBS sold a mixed bundle of their "USA Loan Debt" portfolio with a face value of around \$23billion USD for \$15billion USD...A circa 34% discount. This does have an effect. For sometime the international Political and Banking powers have been encouraging the Directors of their large nationally based banks to open their books and bring some transparency to the extent of their Bank's liabilities re the sub prime and associated financial debacle.

It is only when someone is willing to buy an asset that a general market value of securities can be properly assessed. I anticipate that other banks will gradually be forced to attempt similar sales and although we have no way to accurately assess whether the sale was of mainly quality grade "Prime" loans and indeed what UBS may still hold in less attractive "Sub prime" paper, I believe it will herald the beginning of a process which eventually will provide the desired transparency which markets must have to function effectively. I further believe that it will cause another round of trauma and uncertainty to markets. Financial stocks took a further hit last Wednesday after Moody's Investors Service said it is "conducting a thorough review" regarding the possibility that computer errors incorrectly gave high quality ratings to certain debt securities that later sank in value. This can only add further problems in an industry that doesn't need it and perhaps time will prove that the UBS deal was the best one made.

This will add to the existing vulnerability caused by the recent surge in oil, gasoline and commodity prices and extend through the third quarter 08. We have written for years regarding the demographically driven need for oil, however I would still assess the 130+USD prices we see today are unrealistic and unsustainable. I know this is a contrarian view, however, one of the fundamental basics of supply and demand economics is that when prices rise to a level which changes consumer's lifestyles that the fall off in demand when it finally impacts is considerable. OPEC especially, have always been concerned to avoid these boom and bust cycles and although a considerable part of the problem is in the bottleneck of the refinery process, that has never previously stopped them ensuring that supply and demand was generally so balanced whereby increase demand would ensure that higher prices prevailed without killing the



market.

This usually entailed putting more oil into the market, however there is a perception that the speculators...as evidenced by 21 large 1 million ton tankers anchored in Iranian waters, fully laden and going nowhere are part of a concentrated programme to manipulate the marketplace. It has been done before and generally ends in tears. The forward contracts are being bought by speculators to trade, not for delivery and as such, I predict that governments and authorities will come under greater pressure, to either ease their high tax levels on fuel or enact oversight controls and restrictions to limit the possibilities for speculative trading in both oil and basic foodstuffs.

I still believe that oil is more likely to find a value at \$85USD before moving back to \$100+USD, however present geopolitical conditions may continue to prop speculatively raised values for quite some time to come. However, the impact oil has on all other commodities and services are such that Central Banks are more likely to begin measures to apply brakes on what will inevitably be higher overall inflation risks. As inflation seeps into the overall economic mix Central banks will be require to raise interest rates, which will strengthen their currencies, which, in normal scenarios, would also assist in reducing prices. However, let me reiterate that it is the speculators which are firmly in the driving seat and as such can still manipulate the markets for the foreseeable future.

The above, combined with slowing global economic predictions will I believe cause the markets to return to the volatile ways experienced in the first quarter even although I am confident that growth figures expected over the next few weeks, will actually show a slight increase rather than dip into negative territory. This should allow us, once more, to enhance the average unit cost within our portfolios, as well as providing some secondary level investment opportunities

(I shall provide in next months report a list of possible opportunities).

Our viewpoint has always been to select/recommend those investments which are valued much below their current “Fair value price” When commonsense mid to long term opportunities exist, they are selected and where possible (depending on Portfolio size) we attempt to buy our long term position at two or three “multi low” opportunities. This enables us to achieve our holdings at low average values.

We saw some short positive rallies in April across a wide spread of our selected investments, which gives, I believe a perfect example of what the future holds, once this volatile phase passes. April’s rally was predicated on the onerous viewpoint that things were about to get better and that the USA had not slipped into a technical recession. Ergo the rally. We have always held the view point that it wouldn’t be until the second half of the year that we would begin to see which areas remain reasonably buoyant and those which were about to experience contracting conditions.

I neither hold a greatly pessimistic or optimistic view of present fundamental market conditions. I do expect to see volatility once again becoming prevalent however as investor sentiment is swayed by whatever news is current on the day. Short term traders, fuelled by sector speculators hold the fort at the present moment and many ancillary events, such as the USA Democratic presidential race, which usually would begin to impact certain investment sectors, as the final winner is I believe the likely next President, would begin to influence sentiment. Perhaps it is the perception that once the Bush presidency is over, no matter what taxes and cost may be applied by the new incumbent, that an overall improvement in conditions are expected. In any event the outcome is presently taking second stage to more current events.

The high oil prices and the dour views expressed in the minutes of the US FED have shaved more than five percent, in a few days last week, from the main US and international markets. In addition although jitters over the housing-driven credit crisis have calmed since March, they are far from over. The higher prices are beginning to impact consumers globally as evidenced by Mastercard and Visa reporting their clients cutting back spending. It was expected that only around \$20billion of the US government’s “Stimulation package” cheques would be spent within the general economy, but even that figure may prove optimistic as consumers use their “windfall” to pay off debt and buy basics. In my experience these “bubble” scenarios generally lose steam. Markets today cannot be paying the price of a demographic scenario expected to occur in eight to ten years. This is especially true regarding oil and basic commodities. The long term fundamentals have not changed since last year, or indeed for many years and no new information regarding supply has been presented recently when oil was at \$50,\$60,\$70USD. The world has known about diminishing stock levels and increasing demand matrixes for decades.

Food on the other hand has experienced recent drought and supply disruptions, which with the higher cost of fertilizers and transport etc., have added expenses throughout the whole process. The world has the technology, available land and expertise to ensure supply demands are met, although I fear that price inflation in food is likely to generally rise. Therefore I expect the next two or three months could provide some rapid changes in sectors and regions, especially as all governments will come under greater pressure from their citizens to find long term global solutions to these problems. Simply put, all governments through years of broken and unworkable Common Agricultural Policies and farm subsidies; regulatory failures in financial oversight responsibilities etc., have put themselves in the position whereby their citizens will increase pressuring them to find workable solutions. I personally have little confidence that governments will combine and apply the logical solutions to correct the obvious deficiencies in the near future. However, I do believe that sufficient pressure will be brought to bear on fundamental speculation. In any event last week’s losses have been somewhat reversed.

Finally, in January it was still very difficult to accurately assess the actual “downside” risks to the markets of the various scenarios they faced. As time passes and more information becomes available and we shall begin to understand the extent of the difficulties, however, there exists a palpable nervousness which is more likely to cause negative reactions before a relative normalcy can be expected to return. As always we shall be monitoring the markets and take advantage as circumstance develop.

Regards

Alan Lamb