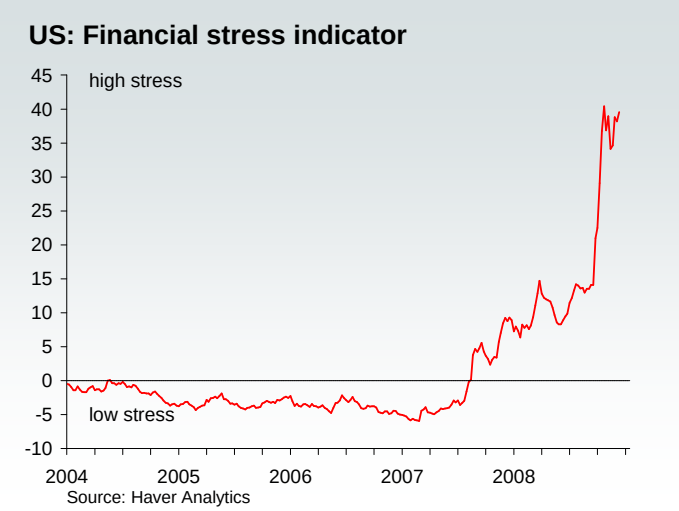
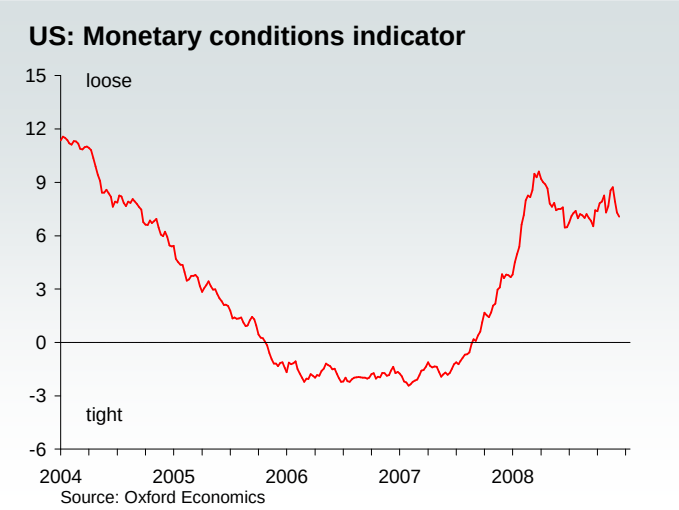
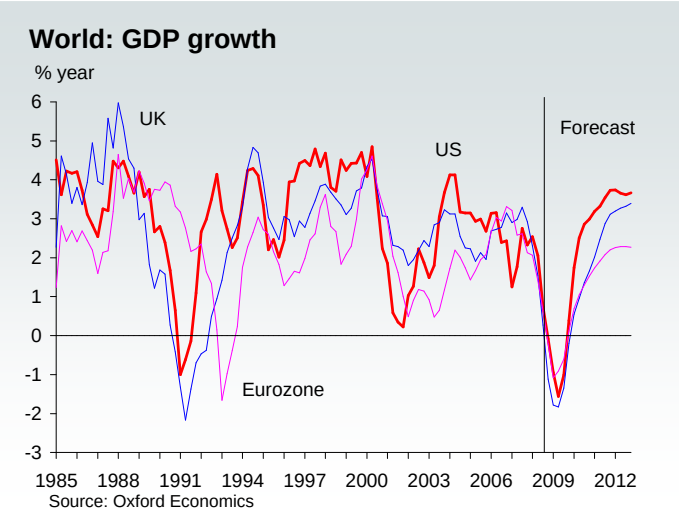
Credit Crunch Watch







Financial stress indicator

- The financial stress indicator is a composite index of a number of indicators including risk spreads, mortgage spreads, equity volatility, commercial paper and commercial loans outstanding and the spread of LIBOR rates over T-bill rates. Financial stress ticked higher over the last week, and remains only marginally below the all-time highs of mid-October. This was despite a large fall in mortgage rates, resulting from Fed moves to buy up mortgage-backed securities. The impact of this was offset by a further widening in credit spreads (partly the result of the sharp drop in long Treasury bond yields) and a renewed rise in equity volatility.

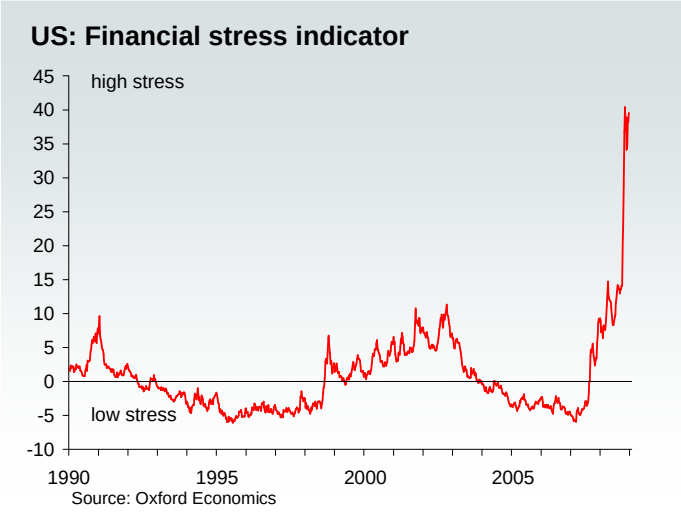
Monetary conditions indicator

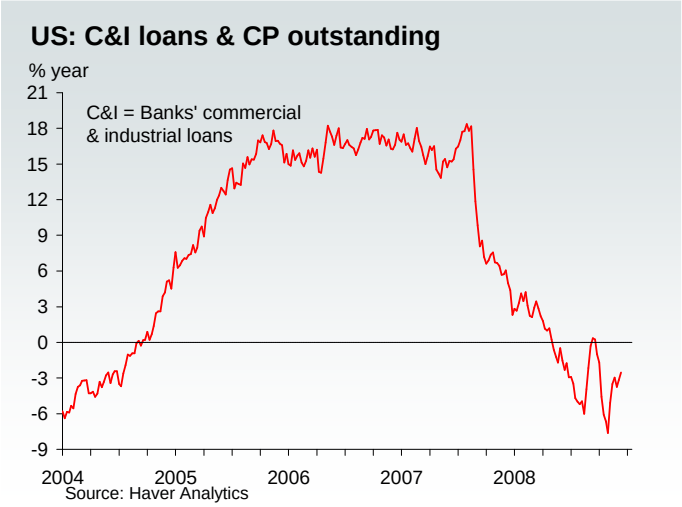
- The monetary conditions indicator is a composite index based on the Fed funds rate, the 10-year bond yield, the yield curve slope and the effective or trade-weighted dollar exchange rate. Monetary conditions tightened again over the last week, led by a flattening of the yield curve and a further strengthening of the trade-weighted dollar. But the Fed is increasingly moving toward loosening monetary conditions using non-standard means, including so-called ‘quantitative easing’. This includes expanding its balance sheet to buy a variety of securities, possibly including treasury bonds. The need for moves of this kind are illustrated by the fact that broad money aggregates are stagnating despite big liquidity injections into the banking sector.

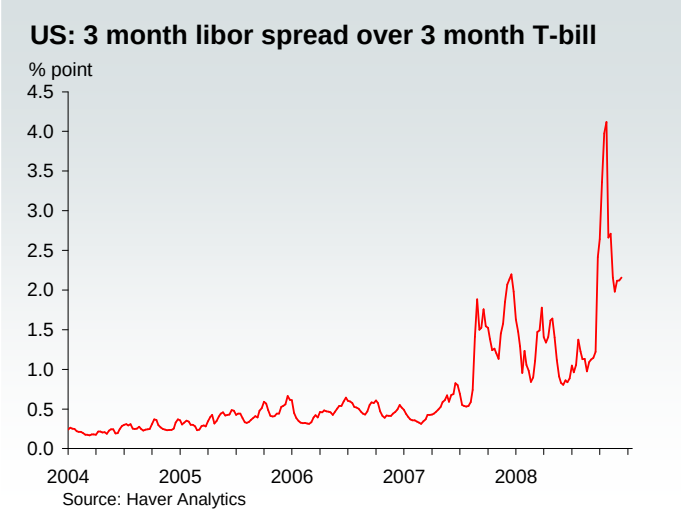
Growth forecasts – US, UK & Eurozone

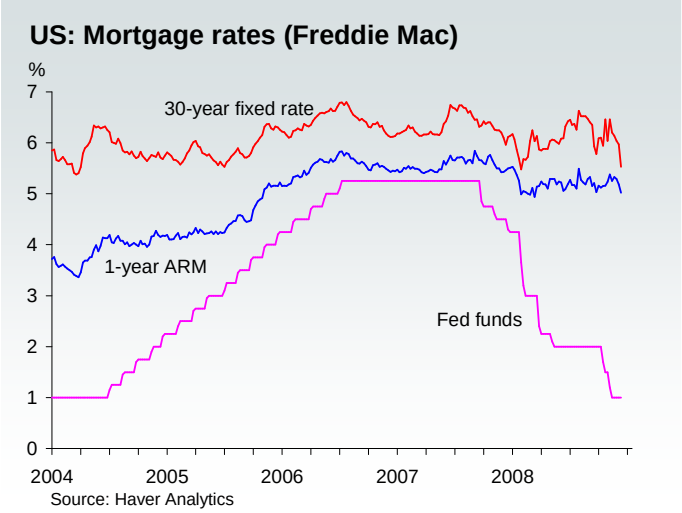
- The downturn in the major economies continues to accelerate. This week’s PMI indices for November for the Eurozone and the UK weakened again from already very depressed levels. Germany factory orders for October dropped steeply, confirming the gloomy recent survey evidence, and Eurozone retail sales data for October also showed a faster than expected contraction. In the US, the non-manufacturing ISM dropped to an all-time low, and most strikingly, the employment report for November was far worse than expected. More than 500,000 jobs were shed in the month and negative revisions to previous data took jobs losses over the last three months to over 1.2 million. Against this background, radical economic policy measures such as ‘quantitative easing’ are rapidly gaining support.

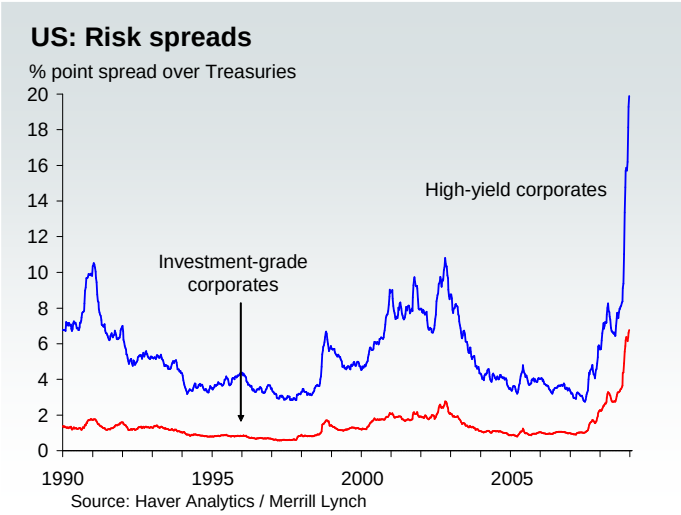
US financial stress measures

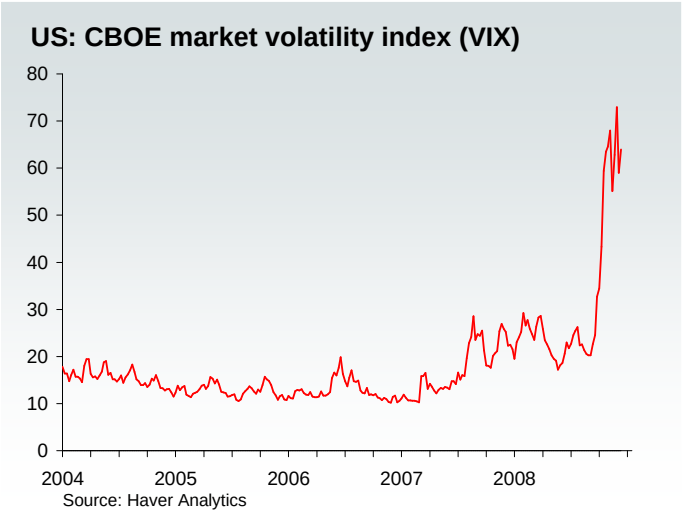




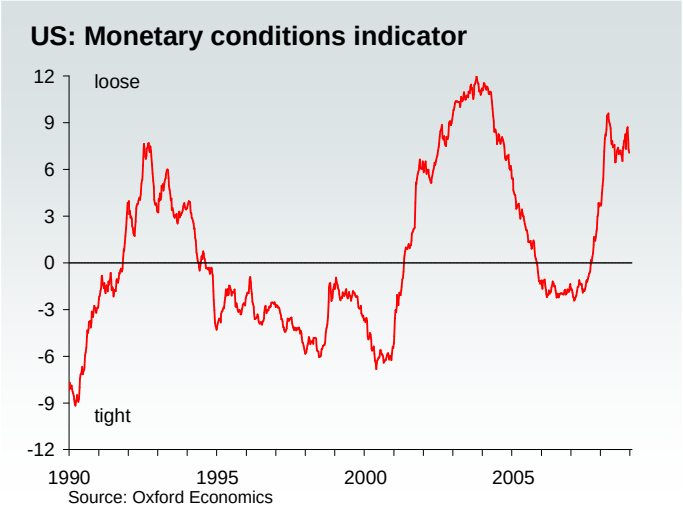


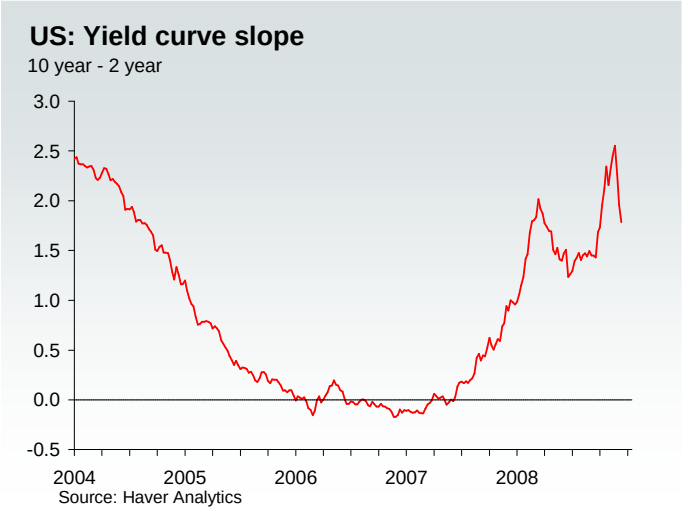


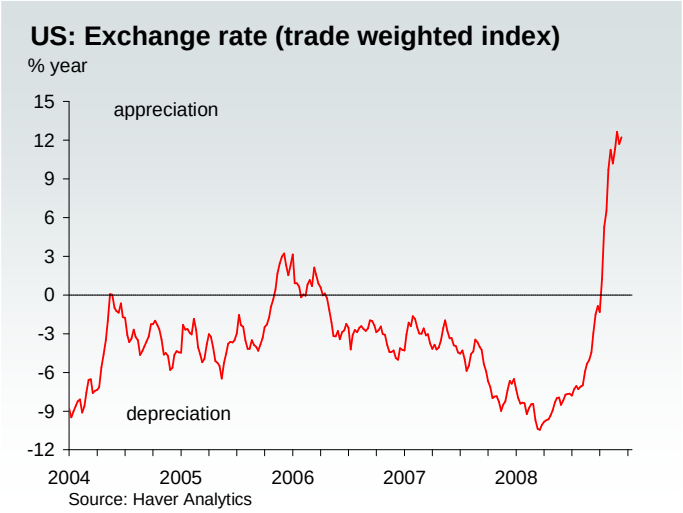


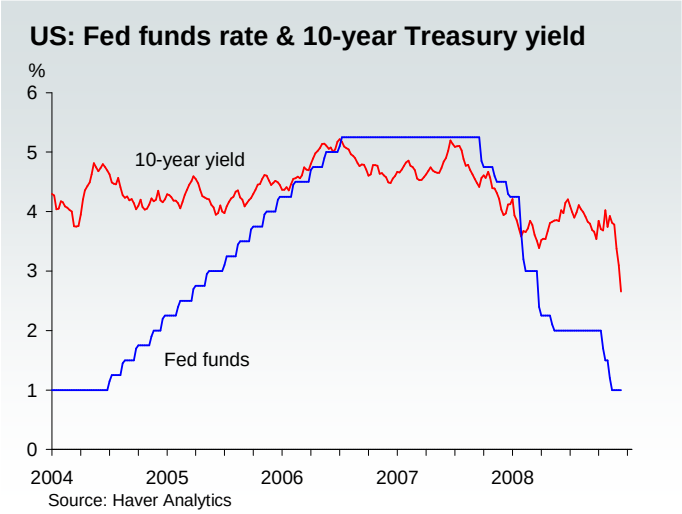


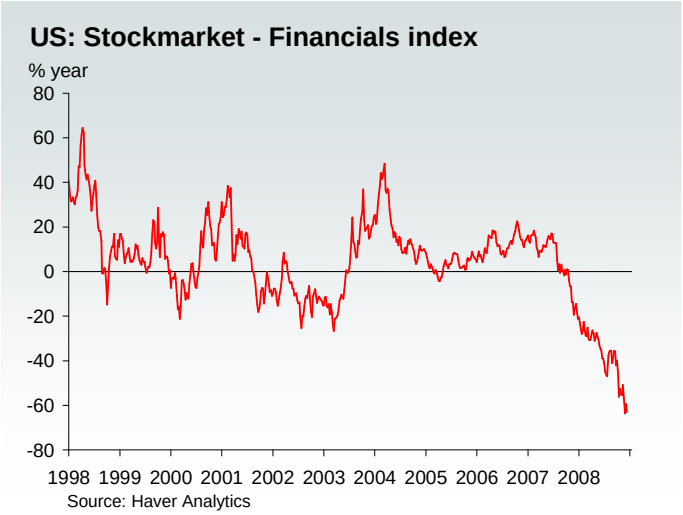
US monetary conditions & other indicators

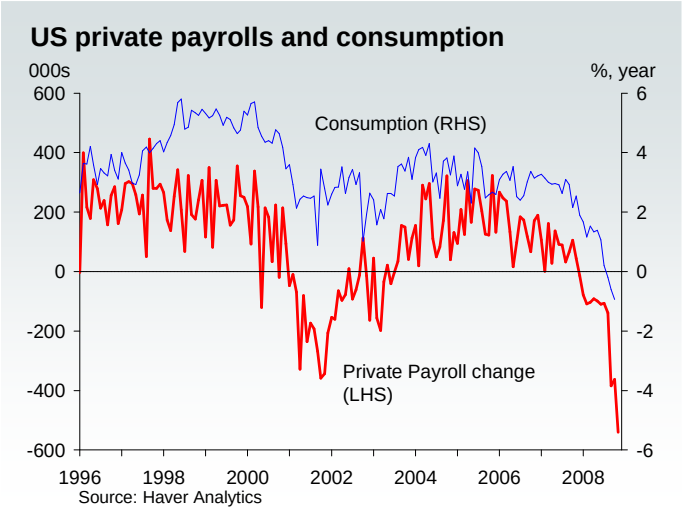












Credit crunch timeline

Apr-07	**New Century Financial, subprime lender, files for bankruptcy**
Jul-07	Credit crunch begins, sharp rise in financial market volatility **Bear Stearns hedge funds collapse** Bernanke warns subprime losses may reach US$100bn
Aug-07	BNP Paribas halts withdrawals from hedge funds due to liquidity problems *Fed cuts discount rate 50bp to 5.75%* **Sachsen Landesbank sold to LBBW due to subprime losses**
Sep-07	Sharp rise in interbank rates Northern Rock seeks emergency support from bank of England *Fed cuts funds rate 50bp to 4.75%*
Oct-07	UBS announces first subprime losses of US$3.4bn Citigroup announces US$9bn of losses, Merril Lynch US$7.9bn *Fed cuts funds rate 25bp to 4.5%*
Dec-07	*Bank of England cuts rates 25bp to 5.5%* *Coordinated central bank liquidity support to cover year-end needs - succeeds in temporarily lowering interbank rates* S&P downgrades several monoline insurers *Fed cuts funds rate 25bp to 4.25%*
Jan-08	Major stock market falls in major economies *Fed cuts funds rate 125bp to 3.0% in two steps* MBIA insurance group announces US$2.3bn losses due to subprime
Feb-08	*Bank of England cuts rate 25bp to 5.25%* G7 estimates subprime losses could reach US$400bn **Northern Rock nationalisation announced**
Mar-08	*Fed offers US$200bn of liquidity support, biggest amount yet, extends to primary dealers* **Bear Stearns collapses and is acquired by JPMorgan** *Fed cuts funds rate a further 75bp to 2.25%*
Apr-08	IMF warns credit crunch losses could reach US$1 trillion *Bank of England cuts rates 25bp to 5%* *Bank of England announces Special Liquidity Scheme offering to swap £50bn of banks' illquid assets for Treasury bills* *Fed cuts Funds rate 25bp to 2%*
May-08	UBS launches US$15.5bn rights issue as losses reach US$37bn
Jun-08	More capital raising efforts - Barclays raises £4.5bn
Jul-08	**US mortgage lender IndyMac collapses** **Authorities announce support for US mortgage lenders Freddie Mac and Fannie Mae** HBOS rights issue in UK flops, leaving shares with underwriters *ECB increases rates 25bp to 4.25%*
Sep-08	**Freddie Mac and Fannie Mae rescued by US government** **Lehman Brothers files for bankruptcy, break up begins** **Merrill Lynch taken over by Bank of America** **Federal Reserve announces US$85bn rescue of AIG, government to take 80% of equity** **UK's HBOS taken over by Lloyds TSB** **Washington Mutual closed down, assets sold to Citigroup** **Belgium's Fortis rescued by Belgian/Dutch/Luxembourg government, Eur 11.2bn cost** Paulson Plan announced to buy bad bank assets worth up to US$700bn **UK mortgage lender Bradford & Bingley nationalised** **Belgian bank Dexia bailed out with Eur6.4bn** Further steep rise in interbank rates, sharp drop in equity markets US House of Representatives rejects Paulson Plan
Oct-08	*Bank deposit guarantees by Ireland, Greece, Germany, Denmark, Spain and Austria* US Senate and House of Representatives pass revised Paulson Plan **Second rescue of Germany's Hypo Real Estate** **Iceland currency collapse and nationalisation of banks** UK announces bank bailout scheme *Coordinated 50bp rate cut by in US, UK, Eurozone, Sweden, Canada and Switzerland* *Rate cuts in China, Korea and Taiwan* *Fed announces direct purchases of commercial paper* US plans US$250bn purchase of stakes in banks Bank bailout plans announced in Holland, Sweden, Korea, Switzerland, Austrai, Belgium, France, Germany, Italy and Greece. Asset purchase plans in Spain and Belgium. *Fed cuts rates further 50bp to 1%* **Merill Lynch, Citigroup and UBS announces further US$18bn writedowns in Q3** *Japan cuts rates to 0.3% from 0.5%, India cuts rates 1%*
Nov-08	IMF bailout packages for Ukraine, Hungary, talks with Pakistan & Iceland China fiscal stimulus package of US$586bn *Bank of England cuts rates 150bp to 3%.* *ECB cuts rates 50bp to 3.25%* Fiscal stimulus packages announced in Germany, Spain and France Eurozone proposes coordinated €200 billion stimulus effort **Rescue package for Citigroup - US$20 billion of equity and US$306 billion of guarantees** *Federal Reserve to purchase up to US$800 billion of asset- and mortgage-backed securities* *Fed Chairman Bernanke discusses possible purchases of Treasury bonds* *Bank of England cuts rates 1% to 2%, ECB cuts 75bp to 2.5%*