

North Atlantic Asset Mgt Ltd. Weekly Newsletter

October 8th, 2008

"Fear is a much stronger motivational force. The loss of \$1,000 has a much bigger impact than the gain of \$1,000." – Andrew Lo, Professor in Behavioral Science at the MIT

INDEX / CURRENCY	Week*	YTD
S&P 500	(14.61%)	(31.17%)
Dow Jones Industrial Average	(13.29%)	(29.07%)
Nasdaq	(15.58%)	(33.42%)
Toronto Stock Exchange	(21.32%)	(37.30%)
Brazil Bovespa	(36.20%)	(53.76%)
DJ Europe 50	(13.45%)	(40.19%)
UK FTSE 100	(13.71%)	(41.23%)
Japan Nikkei 225	(13.20%)	(32.75%)
Hong Kong Hang Seng	(14.39%)	(44.30%)
Australia S&P/ASX 200	(19.35%)	(47.01%)
Euro	(2.97%)	(6.29%)
Pound	(2.80%)	(12.83%)
Yen	6.03%	11.67%
CRB Commodity Index	(10.39%)	(13.69%)

*Over a week, from Sept 30th to midday Wednesday Oct. 8th

Past performance is not an indicator of future returns.

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NEGATIVE FEEDBACK LOOP

Will Logic Prevail?

This week given the actions of the U.S. Federal Reserve and the coordinated global central bank effort to revive the markets (details given below), it is particularly difficult to explain another decline in the markets. There is the overarching problem of the crisis of confidence in the global economy, yet it is hard to find anything logical in the daily gyrations of the market. At the moment fear seems to be the only way to describe the situation. Fear can be seen everywhere; headlines raising questions about depression, crowds gathering around office televisions at the hint of any news, and the average person on the street suddenly deeply concerned about their savings. Behavioral scientists call this situation "negative feedback loop" where one piece of bad information feeds on another and another etc. At this point, an emotional desire to preserve wealth can override the need to consider longer-term strategies. However signs of "capitulation", where investors throw in the towel, may signal a possible market rebound.

Where is the Opportunity?

To many, signs of capitulation can be read as an indicator that the market may be approaching a bottom. It represents the most opportune time to invest in the markets. This is not to guarantee the market will continue to rise from that point onwards, as the financial markets tend to be extremely volatile in these conditions. There is probably still some downside left in the market but history suggests the recovery will be quick. So, the need to stay invested and not liquidate positions is key. (See NAAM's special piece at www.bfm.bm for information on recoveries.)

Review of the Week's Events

The U.S. Federal reserve took several major steps this week to try to shore up U.S. market and in particular free up the credit markets. Wednesday morning, the U.S. Federal Reserve coordinated with the central banks of Europe, the U.K., Canada, Sweden and Switzerland to cut interest rates, in an effort to revive the global economy.

This came along side separate rate cuts from China, Hong Kong and Australia on Tuesday. Also on Tuesday, the U.S. Fed announced it will lend directly to corporations, bypassing ailing U.S. banks through issuance of short term loans know as commercial paper. In addition, the U.K. government unveiled one of the broadest bailouts of this crisis investing close to \$87 billion in the country's largest financial institutions.

Last Friday, the House of Representatives in the U.S. passed the Troubled Asset Repurchase Program (TARP). This provides over \$750bn for the U.S. Treasury to purchase poor performing securities from various institutions, in an effort to stabilize financial institutions' balance sheets and encourage lending. The U.S. Treasury plans to start buying up these troubled assets soon.