



I N V E S T M E N T V I E W S

No. 11 of 2007

NOVEMBER 2007

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Investment

- * Currencies The dollar stays under pressure. Up again for the Loonie and the Aussie dollar.
- * Bonds Yields fall, but not a lot.
- * Equities Surprising strength, especially for the BRICs.
- * Oil/Commodities A surge in oil and gold, partly thanks to dollar weakness.

News/Views

- * Bentley Reid Group acquired.
- * UK Inheritance Tax and Domicile.
- * HMRC's attack on undeclared interest from offshore accounts.

GENERAL COMMENT

SOMETHING NASTY IN THE WOODSHED

The events of the last few weeks suggest that those banks who are forced to report quarterly (i.e. in the US), having initially under-estimated the scale of their losses from sub-prime mortgage related securities, are now coming back with second, much more gruesome estimates. Citigroup and Merrill Lynch are the two most notable of these and have both lost their Chief Execs in the wake of their confessions, which added \$1bn and \$4bn to their original estimates of \$3bn and \$4bn respectively. Now it may be that prices of these instruments are falling so rapidly that such incremental losses just represent market movements. Or it may be that they cannot price them and this represents more up to date assessments. It may, of course, mean that they haven't really got a clue.

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5TH FLOOR, 21 DARTMOUTH STREET • LONDON SW1H 9BP • ENGLAND • TELEPHONE 020-7222-5888 • FAX 020-7222-6880
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Whichever is the true reason, this begs a number of questions. Firstly, if the potential for error is so great can we have any confidence that this represents the true state of affairs? Secondly, why should such egregious adjustments be restricted to just two banks and are we in for a wave of them? Thirdly, what about those banks, such as in the UK, which only have to report bi-annually? Fourthly, only about 25% of this stuff is held by banks so what about insurers and pension funds, whose liabilities are much more long term and who may be hoping that this will go away in time? And what is the potential for banks to have to take back poor credit on their books, thereby eating possibly dramatically into their capital base. Estimates of the potential size of sub-prime losses have risen sharply. A few months ago, this was said to amount to possibly \$100 billion. In September's IV we guessed at a number of \$200 bn on the basis of roughly a quarter going bad. Current expectations are now up to this level and rising. Yet the declared provisioning is only a small fraction of this. More worrying, there are worries that the sub-prime problems are spreading up the credit chain.

The immediate impact on the stock market has been to increase volatility. An observer returning from a five month vacation would notice no difference to speak of in price levels in the developed markets although financials have been hit quite hard. The US financial sector is down about 12% since the end of May, while the overall market is down about 3%. Extract the financial sector and the market has actually risen by about 3% over this period. The emerging markets, where liquidity is known to be plentiful, have soared during this period. Taking the BRIC markets (Brazil, Russia, India and China) the rises have been between a quarter and a half since the end of May (in BRIC order) much of this after the first Fed discount rate cut on August 18th. Resources have performed in a similar manner.

The general lack of concern shown by the developed economy markets in the face of a credit problem that appears to be getting more serious by the day suggests that this is perceived to be a liquidity issue rather than a solvency issue. The sanguinity of the emerging and resource markets supports this thesis. While in previous crises these have led the way down their resilience this time illustrates well that they are the sources of excess global liquidity rather than dependent on it; the external deficits of the late 1990s have long gone and in their place are huge and rising surpluses.

This indifference is also being applied to valuations. While EM PE ratios are somewhat haphazardly calculated and generally unreliable, they are nevertheless in the mid to high teens in emerging Europe, rather higher in Latin America, higher still in India and stratospheric in China. Such ratings do not suggest that value is the driving force behind the gains in these markets.

We have noted a number of times that valuations in the developed markets are undemanding provided this is not the end of the cycle; that is to say, so long as profits are rising. However, this happy state of affairs has ground to a halt in the latest quarter in the US. Initial expectations were that the record run of double-digit earnings growth would indeed be broken but that profits would still grow by about 6%; however, the out-turn after 80% of constituents have reported is a decline of almost

2%. This is not that surprising because bank profits have been badly damaged by provisioning, but what if such provisioning continues into the next quarter at the same or at higher levels, a rather likely prospect? Furthermore, the earnings falls have not been confined to banks - consumer discretionary stocks have also begun to feel the cold winds. It may be that the market will continue to be two-tier, with financials falling and the rest continuing to rise. However, even if non financials merely rise in line with earnings this could still amount to a re-rating of the overall market. Not a problem, the bulls would say, noting that markets usually do re-rate at this point because interest rates are falling. While it is true that short rates have been cut by the Fed, there are still inflation concerns around, not least at the Federal Reserve itself. China is no longer exporting deflation as wages rip and the continuing ascent in the oil price must at some point find its way into the inflation numbers. True, slower activity, will be a counter-inflationary force, but it will also be a force against domestic profitability. This is probably less of a problem than it seems because US majors now achieve half their sales overseas but, as we have recounted before, the US consumer remains the most important driver of world growth and a domestic slowdown will reverberate elsewhere. If inflation becomes an issue the Fed will stop cutting rates and bond yields will rise. Were this to happen the re-rating argument will be hard to justify.

For the moment, markets appear unconcerned about profitability issues outside the banking sector and are being driven by continuing high levels of surplus liquidity. However, little consideration seems to have been given to the risk that the liquidity crisis in the credit markets could turn into a solvency crisis. The sharp decline in the price of Citicorp was prompted by an analyst's suggestion that the sub-prime losses were sufficiently large to require a re-build of its capital base either by cutting the dividend, raising new capital or both. The \$100bn US Treasury backed "super fund", established to take up the best of the liquidity strapped CDOs has been met with considerable cynicism. There has been some media comment that the sponsoring banks are trying to shift the problem off their balance sheets and that this will merely allow the lack of valuation transparency to prevail for longer. Memories have been rekindled of the refusal to face up to similar issues by the authorities in Japan throughout the 1990s and the ensuing extended impact on that economy. There is also more than a whiff of suspicion that these banks might know of "something nasty in the woodshed", misgivings which have been heightened by the recent revelations from Merrills and Citigroup. Should the banks have to take back on to their balance sheets significant tranches of low grade debt the regulatory weighting that such debt will attract, which grows as the rating agencies slash credit ratings, will have a considerably larger negative impact on capital and reserves than the nominal value of such loans. This in turn will constrain lending ability without capital injections. The prospect of a credit crunch is still growing.

Such a prospect would exacerbate the problems in the housing market, not just by making new mortgages more difficult to obtain but also by constraining credit more generally, such as on credit cards. This has become evident in the last few months in the UK, both in card issuance and also in increased charges and borrower scrutiny. It would be surprising if the US was any different in this regard. The risk of a sharp economic slowdown in the US, led by consumer retrenchment, has not gone away. It's just that the markets don't ascribe a very high probability to it. Not yet, anyway.

THEY SAID IT THIS MONTH

We are now the proud possessors of 'Business Miscellany' published by the Economist. From this we discovered that the oldest company in the world was Kongo Gumi of Japan described as a construction company but actually a high quality temple builder founded in 578. Further investigation revealed that Kongo Gumi went bankrupt earlier this year. Does this mean that the rise of Mammon has destroyed the temple building market in Japan? Well partly, but the real reason for the collapse was different but still Mammon related in the form of huge debts incurred to finance real estate speculation. A business lesson there for us all.

For those who really want to know the new oldest company in the world is Stora Enso founded in 1288, a thriving listed paper company in Finland.

We have also been privileged this month to see extracts from a new book called 'Potty, Fartwell and Knob: Extraordinary but True Names of British People'. Even leaving out all those not suitable for publication in Investment Views there are still some splendid examples including Anna Rack, Barb Dwyer, Pete Sake, Constant Pain, Luke Warm, Minnie Cooper, Jim Shoe, Hazel Nutt, Evans Gates, Sue Permann as well as the remarkable Gertrude Obedience Goose, Wonderful Ramsbottom and Very Horsey Troth.

And finally, how sad is this?

In 1998 the New Republic published an article called "Praised Be Greenspan" that described a bond-trading firm that had turned its offices into a shrine to Greenspan, complete with a glass case containing "two Bic pens Greenspan supposedly used in 1993." Traders, reported the magazine, would come in to gaze at his photograph and meditate throughout the day. Much later, readers learned that this detail had been invented by one of the writers of the piece, the infamous fabulist and liar Stephen Glass, but at the time nobody in Washington seemed to think it outlandish...

At the risk of overkill we have two golfing jokes this month. One follows the usual theme of wives and golf, and the other is entirely different.

"A man and his wife walked into a dentist's office.

The man said to the dentist, "Doc, I'm in one hell of a hurry! I have two buddies sitting out in my car waiting for us to go play golf. So forget about the anaesthetic and just pull the tooth and be done with it. We have a 10:00 AM tee time at the best golf course in town and it's 9:30 already. I don't have time to wait for the anaesthetic to work!"

The dentist thought to himself, "My goodness, this is surely a very brave man asking to have his tooth pulled without using anything to kill the pain."

So the dentist asks him, "Which tooth is it sir?"

The man turned to his wife and said, "Open your mouth, Honey, and show him."

"A priest, a doctor, and an engineer were waiting one morning for a particularly slow group of golfers.

The engineer fumed, "What's with those guys? We must have been waiting for fifteen minutes!"

The doctor chimed in, "I don't know, but I've never seen such inept golf!"

The priest said, "Here comes the green-keeper. Let's have a word with him."

He said, "Hello George, what's wrong with that group ahead of us? They're rather slow, aren't they?"

The green-keeper replied, "Oh, yes. That's a group of blind firemen. They lost their sight saving our clubhouse from a fire last year, so we always let them play for free anytime."

The group fell silent for a moment.

Then the priest said, "That's so sad. I think I will say a special prayer for them tonight."

The doctor said, "Good idea. I'm going to contact my ophthalmologist colleague and see if there's anything he can do for them."

The engineer said, "Why can't they play at night?"

MARKET COMMENT



CURRENCIES

There are months when writing something new and interesting about currency markets is extremely difficult and October 2007 has turned out to be one of them. Having looked back to see what we wrote in September, we found that in direction if not in the precise degree, history had effectively repeated itself. The dollar weakened overall, the star currencies were again the Australian and Canadian dollars both with gains of over 4%, the European currencies were stronger than the yen which actually fell marginally against the dollar, and the renminbi did not show any real sign of acceleration in its rate of appreciation although it did do a little better than in the previous month. All these were pretty exact replicas of September's movements and, not surprisingly the reasons for the moves seem to have been very similar as well.

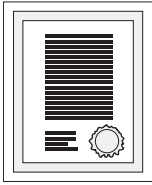
In the US, although the third quarter GDP numbers at 3.9% were comfortably ahead of expectations, this is now regarded as history with forecasts for the fourth quarter centering on not much more than zero. The news on the housing market seems to go from bad to worse to even worse, and the latest revelations from Merrill Lynch and Citigroup on their subprime loan exposures are hardly conducive to confidence. Where these two eminent names have trodden it must surely be reasonable to expect others to have followed although the silence in some quarters is becoming deafening. The Fed has reiterated its view that it is not in business to bail out imprudent bankers but it still cut rates by 0.25% during October suggesting that it is rather concerned with the slowdown becoming apparent in the real economy. The fact that it seemed to have boxed itself into a position, where to cut was what the markets were demanding

and not to cut could have led to a massive sell-off, is beside the point. It will not make the same mistake again, hence the accompanying statement which was quite hawkish in tone, but there will surely be further rate cuts to come in the next few months at a time when some other central banks (Australia and Europe?) may be raising rates, and others (UK?) will be standing pat. Hardly a background against which the dollar should be expected to rebound sharply despite its apparent cheapness on a purchasing power parity basis.

Elsewhere, the ECB has left rates unchanged despite both money supply growth and headline inflation, now up to 2.6%, being above target levels. This is probably just as well given the incipient signs of slowdown in the Euroland economy, but the anti-inflationary zeal of the ECB is such that another rate rise in due course looks likely even if this comes at the expense of growth. One should not forget that a rising currency by itself creates tighter financial conditions and that it may not take too much more strength in the euro to make the pips really begin to squeak. Similarly, in the case of sterling, currency strength is beginning to cause problems although less than it would have done in the past because of the hollowing out of the UK manufacturing sector. The economy, where third quarter GDP reached a respectable 3.3%, remains strong so far and this, along with another upward push in inflation, argues for a further rate increase which would be the sixth in the current cycle. However on the other side of the coin UK growth could be quite hard hit by the problems in the financial sector (given the importance of financial services to the UK economy) and, at the same time, there are worries that tighter credit could adversely impact both the residential and commercial property markets. On balance another rise looks unlikely but, as in Europe, rates are likely to fall less fast than those in the US.

Japan is finding growth hard to come by, although the startling collapse in housing starts is due to technical changes in the implementation of earthquake-proofing standards rather than to a genuine decline in activity. This means that the Bank of Japan has not been able to implement the rate increases that it is so keen to put in place and there is little sign that this will change in the near future. So again we have another major currency where rates will be stable or maybe rising compared with the falls expected in the US. Australia too, even after a tenth successive rise in early November to 6.75%, is still more likely to see rates rise further rather than fall thanks to the strong economy and vibrant credit growth.

Overall, then, the picture is of internal and external factors combining to put pressure on the dollar, so the supposition must be that the weakness of the last two months will continue. But we should remember that, for the health of the global economy, the surplus currencies such as the yen and the renminbi need to rise and take some of the pressure off the European currencies which have already risen far enough.



BONDS

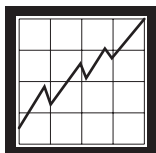
Bonds made steady progress over the month, especially after data released mid-month underlined just how dire the US housing market is becoming. Housing starts tumbled some 10% during September alone and now stand at a fourteen-year low. While these are not yet at the same levels as at the trough of the 1991 recession, it should not be forgotten that the US population has grown the best part of 20% since then and that we are still not anywhere near the bottom in this market. It seems to us that the impact on the consumers' balances sheets must have a follow-through effect on consumption patterns, especially when coupled with the severe credit squeeze, regardless of the continued resilience of the labour market. However towards the end of the month, the third quarter GDP release revealed that the US consumer is still very much alive and kicking, and growth over the period at 3.9% on an annualised basis was far stronger than the market had been expecting. This wiped out the best of the gains made over the month, leaving the major bond market yields with the exception of Australia trading between 4 and 8 basis points lower. The strong GDP report did not prevent another widely anticipated quarter point cut in the Fed's funds rate, though the muted nature of the Fed's accompanying press release went some way to temper expectations of further cuts.

Bond yields continue to offer little in the way of real yield for investors. While the widely watched US core CPI rate has slipped back to 2.1% over recent months, this figure ignores more 'volatile' items, such as food and energy. Of course, it is in these volatile items where we are seeing the strongest pricing pressures and it is difficult to argue that the move in the oil price has been somehow merely cyclical in nature.

There are now signs that food prices may be embarking on a similar structural boom following a 30 year bear market, which has driven so many marginal producers to the wall and starved the industry of capital. One of the market saws has it that we should be less worried about oil prices today rather than in yesteryear because the western economies have become more 'efficient' in their use of oil. While it has been true that over many years growth in oil consumption on a volume basis has lagged economic growth, what matters in inflationary terms is how much is actually spent on oil as a proportion of income. Over the last five years the increase in spending on oil has been far in excess of the incremental gain in nominal GDP. Expenditure on oil as a proportion of personal income is still shy of the peaks seen in the late 70s but it is far higher than it was during the 90s and the trend is clearly upwards. Oil is playing an increasingly important part in our economies again and it would be foolish to disregard its potential impact on inflation. Pressures on the US core CPI rate may be waning as the impact of the growing troubles in the housing market start to reverberate through the system. However, the headline rate looks certain to remain under stress with the oil price approaching \$100 a barrel. The headline US CPI of 2.8% (likely to rise to 4% or above) compares with the 10 year US bond yield of 4.5%, and such a real interest rate does little to whet our appetite for the asset class.

The Australian bond market continues to move in an opposite direction to the global trend and yields here rose a further 0.08% over the month. The economy continues

to grow at a blistering rate and the labour market is getting increasingly tight. The Reserve Bank of Australia, having passed the opportunity to move in October, lifted rates by 0.25% in early November as widely expected. Inflation remains at a reasonably low 1.9% though the RBA is closely following the trimmed mean rate which is running at a more worrying 2.9%. At the moment there are few signs of any easing in the pressures within the system and the tax cutting pledges made in the election campaign by Howard and Costello will only exacerbate things further if they to be put in place. Further interest rate rises next year are not out of the question.



EQUITIES

Markets continued to recover in October, but have suffered setbacks during the first few days of November. This is despite what in our view is a deteriorating situation in Western financial systems. The initial provisioning announced by some banks in September and October has proved to be inadequate as far as Merrill Lynch, Citigroup and now Morgan Stanley are concerned. We shall be surprised if these turn out to be the only banks which have to do this. There has been some provisioning from banks in Europe but, apart from HSBC's earlier in the year, there has been no mention yet from any of the UK banks. We are nervous that the true scale of problems will turn out to be considerably larger than has so far been admitted.

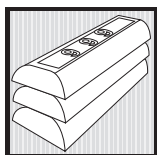
While the credit problems originate from the sharp deterioration in the US housing market, the ownership of these loans is much more widespread. Furthermore, house price growth in parts of Europe is also beginning to slow or even reverse. In the UK, prices are still said to be rising but activity is reported to be slowing. We cannot be certain, therefore, that the American experience will not eventually be reflected elsewhere although the magnitude will probably be less.

For us, a particular concern is the degree of uncertainty that still prevails. It is not at all obvious that banks are actually aware of the scale of potential write-downs that will be necessary and their share of exposure to these instruments is only about a quarter.

We are also worried about the acceleration in the fall of the US dollar. Should this become a rout it may be necessary for the US authorities to take action. The growing doubts about the potential inflationary consequences of the sharp rise in the oil price also imply that market expectations of more rate cuts in America may be misplaced.

In this environment we do not feel that valuation, which continues to favour equities, is necessarily going to be the principal driving force for stock markets in the near future, particularly as the prospect for short term earnings growth has been damaged by write downs in the financial sector. The potential for sharp moves up in equities seems rather less than the risk of either stagnation or falls in the near term. Since

markets have recovered a good part of their summer losses, even allowing for the falls of the last few days, we consider that the prudent course is to take risk off the table until the dust settles.



GOLD/COMMODITIES

It was a case of onwards and upwards in commodity markets during October as the CRB Raw Industrials Index reached a new peak, oil raced towards \$100 per barrel and the gold price hovered around levels not seen for over twenty five years.

The price of WTI oil appreciated by a staggering 15.8% last month and closed at a nominal high of \$95, just shy of the International Energy Agency's estimated inflation-adjusted high of \$102/barrel, achieved in April 1980. The main catalyst was geopolitical tension as Turkey prepared its troops for an incursion into oil-rich northern Iraq and the United States imposed further economic sanctions on Iran. There is mounting speculation that, as a final swan-song, President Bush will authorise a military attack on the Persian state and with it being OPEC's second largest producer, the implications would be profound.

In the closing stages of the month, the price was boosted by the announcement that US crude stockpiles were at a two-year low, although refiners have little incentive to hoard at current spot prices. Furthermore, whilst demand continues to outstrip supply by a small margin, there is no shortage of oil underground. The existing shortfall has developed because of a lack of investment in additional capacity, but this trend may begin to reverse as revenue projections are upgraded in response to recent market moves.

With the fundamental situation appearing tight, but not irreversible, common sense would suggest that the oil price should let off a little steam, particularly as OPEC's production increase of 500,000 barrels per day comes into effect this month. That said momentum and a weakening dollar are working in its favour, meaning that consolidation could commence from above the \$100/barrel mark.

The plunge in the US dollar triggered another stellar month for gold. It rose by 6.2% to \$797/oz and is fast approaching the nominal record of \$850/oz set in January 1980. It has gained 18% since the end of August, but with activity in the gold futures market at record levels one must be cognisant of the increased likelihood of sharper drawdowns.

According to the World Gold Council, fundamentals improved earlier this year as jewellery consumption, which dominates overall demand, rose by 22% in tonnage terms in the twelve months to the end of June. Growing affluence in India, where demand rose by 71%, has had a palpable effect, but these figures relate to a period where trading occurred below \$700/oz and there is growing evidence that demand may now be waning in response to the latest price surge. Like oil, gold has had a

remarkable run in the past three months and a correction looks probable. However, its returns are highly correlated to the plight of the US dollar and should the global reserve currency continue to weaken, there is likely to be further upside for the yellow metal.

Soft commodities have been found wanting over the past few weeks, but remain the star performers this year. The wheat price has appreciated by 59% so far, a meteoric rise that is forcing food manufacturers to pass on costs to the end user. Whilst this can be more easily absorbed by spenders in developed nations, governments of countries where food expenditure constitutes a larger proportion of disposable income are growing increasingly nervous. In an attempt to quell social unrest, both Russia and China have recently returned to policies of controlling prices of basic foodstuffs. Whilst this practice is eerily reminiscent of the dark days of communism, one cannot rule out the same measures being introduced elsewhere.

POLICY SUMMARY MATRIX

The matrix set out below is a summary of our current policy stance on the various equity and bond markets which we monitor. It is not intended as anything other than a guide on where we stand and we will change the content as our views alter. Cash exposure is a residual and will tend to be high when negatives outweigh positives and vice versa.

In the light of international financial developments we have drawn in our horns further in equities reducing all areas to negative with the exception of resources (energy) where we continue to be overweight.

6-12 Month View	Strongly Negative	Negative	Neutral	Positive	Strongly Positive
EQUITIES					
US		■			
UK		■			
EUROPEAN		■			
JAPANESE		■			
AUSTRALIAN		■			
ASIAN		■			
RESOURCES		□		■	
BONDS					
US		■			
UK		■			
EUROPEAN		■			
JAPANESE		■			
AUSTRALIAN		■			
OTHER		□		■	

Written and edited by:
Gavin Roberts and Martin Paling

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Bentley Capital (Pacific) Limited is registered by the Securities and Futures Commission in Hong Kong.

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In addition, we must emphasise that such other advice given and views expressed in this publication are our personal views based upon our understanding of relevant legislation and related authorities. No reader should take any action based upon the content of this publication without first seeking further and more detailed advice from Bentley Reid & Co or their own financial advisers.

MARKET PERFORMANCE

31st October 2007

All performance numbers show % changes except for bond yields which show yield changes.

	Now	1 mth	3 mth	12 mth
CURRENCIES (VS USD)				
GBP	2.0774	+2.0	+2.2	+8.9
CHF	1.1591	+0.8	+3.8	+7.3
AUD	0.9270	+4.7	+8.2	+19.8
JPY	115.29	-0.2	+3.3	+1.6
EUR	1.4468	+1.7	+5.7	+13.4
BOND YIELDS (10 yr)				
US	4.46	-0.1	-0.3	-0.2
UK	5.00	-0.0	-0.3	+0.5
Germany	4.29	-0.1	-0.0	+0.6
Australia	6.24	+0.1	+0.2	+0.6
Japan	1.61	-0.1	-0.2	-0.1
EQUITIES				
UK. FTSE 100 (GBP)	6721.60	+3.9	+5.7	+9.7
US. Dow Jones (USD)	13930.01	+0.2	+5.4	+15.3
Japan. Nikkei Dow (JPY)	16737.63	-0.3	-3.0	+2.1
Australia. All Ords (AUD)	6779.10	+3.0	+9.6	+26.6
MSCI Pacific ex Japan (USD)	1635.89	+7.7	+20.2	+52.1
MSCI Europe ex UK (Local Currencies)	1410.77	+2.3	+2.8	+13.2
MSCI Latin America (Free) (USD)	4616.41	+11.5	+21.3	+73.3
MSCI World Index (USD)	1682.35	+3.0	+7.4	+18.2
MSCI World Index (GBP)	809.83	+1.5	+5.1	+8.6
MSCI World Index (AUD)	1814.83	-1.4	-1.3	-1.3
COMMODITIES				
Oil (WTI)	US\$ 94.55	+15.8	+20.9	+61.0
Gold	US\$789.50	+6.2	+18.6	+30.4

BC FUND PRICES**31st October 2007**

	Bid	1 mth	3 mth	12 mth
Friends Provident				
£ Balanced Mirror Fund	£ 1.221	+2.3	+1.9	+6.5
CF Bentley Capital Investment Funds				
£ Balanced	£ 1.3593	+2.2	+2.2	+7.6
US\$ Balanced	US\$ 1.1412	+1.0	+3.2	+10.1
£ Income	£ 0.9953	+0.3	+1.0	N/A
Royal Skandia				
A\$ Balanced	A\$ 1.599	+1.1	+5.8	+13.0
£ Balanced	£ 1.385	+2.4	+2.6	+6.8
US\$ Growth	US\$ 1.174	+1.4	+2.4	+10.4
EUR Balanced	€ 0.995	+0.8	+0.1	+5.0

All performance numbers show % changes.

If you would like us to email you the BC Fund Prices each month please email us a request to administrator@bentleyreid.co.uk

NEWS / VIEWS

BENTLEY REID GROUP ACQUIRED

We are pleased to announce that Bentley Reid Group has been acquired by The Bank of N T Butterfield & Son Limited. Nic, Rupert and the Bentley Reid team will continue to provide the same tax, Trust and investment services but clients will benefit from the greater financial depth, security and backing of Butterfield Bank. Attached below is the text of a press release for your information. Should you have any questions, please do not hesitate to contact us.

With best wishes

Nic & Rupert Bentley

NEWS RELEASE

Butterfield Bank Makes Key Strategic Acquisition of Wealth Management Group

Hong Kong - 29th October 2007: The Bank of N.T. Butterfield & Son Limited ("Butterfield Bank") is pleased to announce that it has acquired the entire share capital of Bentley Reid Group, a privately-held, international wealth management company with offices in Hong Kong, London and Malta.

Established in 1979, Bentley Reid Group provides financial and tax advisory and investment management services to private clients and charities from offices in Hong Kong and London. Through its Malta-based subsidiary, Bentley Trust, the Group provides trust and company formation and administration on an international, multi-jurisdictional basis. Bentley Reid Group has close to half a billion dollars (US\$) in assets under discretionary management and approximately US\$2 billion in assets under advice and administration.

In announcing the acquisition, Alan Thompson, Butterfield Bank's President and Chief Executive Officer, said, "This transaction represents an important strategic milestone, as wealth management is a core business for Butterfield Bank. Expanding our private client services to new international markets and acquiring wealth management clientele is central to our growth strategy." Earlier this month, the Bank announced the expansion of its Swiss operations with the establishment of a trust company in Geneva, following the establishment of a subsidiary in Zurich in late 2006.

Graham Brooks, Executive Vice President, International, Butterfield Bank said, "In

Bentley Reid, we have acquired a well-established, prestigious group whose operations and personnel are an excellent fit with those of the Bank. The deal increases our existing private client business and allows us to extend our relationship-focused service model to new markets." He added, "The Hong Kong presence will provide us with the ability to attract new clients in the dynamic Far East market. The office in Malta gives us a foothold in one of Europe's newer financial centres, providing us with another jurisdiction through which we can administer clients' assets. Very importantly, Bentley Reid's London operations complement our sophisticated and increasingly successful UK Private Bank and will enhance our investment management capabilities in that jurisdiction. I look forward to working with the Bentley Reid team."

Bentley Reid Group principals Nic Bentley, Chairman, who is based in Hong Kong, and Rupert Bentley, Chief Executive, who is based in London, along with the existing Bentley Reid management team will continue to manage their client relationships as executives of Butterfield Bank Group.

Rupert Bentley commented on the transaction, "This is good news for Bentley Reid's clients and staff. Butterfield Bank shares our philosophy of relationship-led services and has an excellent reputation in the fields of private banking, asset management and trusts. Our clients will continue to deal with the Bentley Reid executives who currently advise them, but will now have access to a broader range of services in many more jurisdictions as a consequence of our joining the Butterfield Bank family."

Note to Editors:

Butterfield Bank is Bermuda's first and largest independent bank, and a specialist provider of offshore financial services. The Butterfield Bank Group offers a full range of community banking services in Bermuda, Barbados and the Cayman Islands, encompassing retail and corporate banking and treasury activities. In the wealth management area, the Group provides private banking, asset management and personal trust services from its headquarters in Bermuda and subsidiary offices in The Bahamas, the Cayman Islands, Guernsey, Switzerland and the United Kingdom. The Group provides services to corporate and institutional clients from offices in Bermuda, The Bahamas, Canada, the Cayman Islands and Guernsey, which include investment and pension fund administration, asset management and corporate trust services. Butterfield Bank is a publicly traded corporation with shares listed on the Bermuda and Cayman Islands stock exchanges. Further details on Butterfield Bank can be obtained from our website at: www.butterfieldbank.com.

UK INHERITANCE TAX AND DOMICILE

There have been two recent events concerning UK domicile, residence and Inheritance Tax.

1. the statements made by George Osborne, the shadow Chancellor at the Tory Party conference
2. the statement made by the Chancellor in his Autumn Statement in the Houses of Parliament.

Let me take these in order.

1. George Osborne's Statement

What Mr Osborne proposed is that the zero rate limit for IHT be increased to £1 million for each individual. This means that, if the Tory Party come to power and if they legislate as they have proposed, nobody (UK non-domiciled or domiciled), will pay IHT on their UK estate (in the case of a non UK domiciliary) or their worldwide estate (if UK domiciled) unless the value exceeds £1 million (in the case of a single person) or £2 million (in the case of a couple).

This was a political masterstroke. It is designed to exempt from IHT nearly 9 million individuals in the UK who, over the last 5-10 years, had become potentially liable to IHT because of the rapid rise in the value of their homes. That this was a political masterstroke is beyond doubt as the opinion polls bear witness.

Mr Osborne went on to state that there are 150,000 non-domiciliaries in the UK (Labour say that there are 115,000). I suspect that the figure will be much higher than both suggest as there are hundreds of thousands of individuals who are temporarily in the UK (Australian, South Africans etc) who will not be making their tax returns on a non-domiciled basis.

He went on to propose that the non-domiciliaries should pay £25,000 p.a. for the privilege that their non-domicile status gives them. This done, Mr Osborne's profit and loss account was

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| i) loss of IHT revenue because of new
£1 million threshold | £3.5 billion p.a. |
| ii) new income 150,000 x 25,000 | £3.7 billion p.a. |

and this simple mathematics in the eyes of the electorate looks prudent and sensible, while taking 9 million out of the IHT tax net, IHT being the second most hated tax in the UK.

The problem is that Mr Osborne's assumptions are wildly inaccurate.

- a) There must at least 250,000 temporary resident non UK domiciled workers in the UK, who save no tax. All their UK income is taxable and they have very few assets or income anywhere else. They could not afford the £25,000 p.a.
- b) Whatever the total is of wealthy non-domiciliaries, there is probably no more than 20,000 seriously wealthy non-domiciliaries who will be happy to pay the £25,000 p.a. and not notice this. So, while Mr Osborne thinks he will lose £3.5 billion p.a. (which is probably correct) and get back £3.75 billion p.a., the reality is that the receipt side will probably yield only 20,000 x £25,000 = £500 million p.a. from the £25,000 p.a. levy. The Chancellor has pointed this out, but neither the Tory Party nor the country appear willing to listen.
- c) This leaves us with the non-domiciliaries who are not poor but have wealth which is insufficient to simply cough up the £25,000 p.a. and not notice its absence. What will they do? Provided that these individuals have planned properly under good advice, they could simply concede that they no longer wish to use the remittance basis of taxation, in which event the £25,000 p.a. will no longer be payable. Correct planning before entering the UK, should mean that these individuals will suffer little negative tax consequence.

2. The Chancellor

There can be no doubt whatsoever that Brown and his Chancellor have been caught on the wrong foot by George Osborne and the Tory proposals.

It is equally clear that what the Chancellor proposed re IHT, residence and domicile in his Autumn Statement, had not been in the original speech prepared by the Chancellor before the Tory proposals were announced. They have been prepared with considerable haste and without any real thought.

What the Chancellor proposed was

- i) after a non UK domiciled individual has been resident for tax in the UK for 7 years, that individual will have two options
 - a) pay £30,000 p.a. and continue to enjoy the remittance basis for taxation, or
 - b) abandon the remittance basis of taxation, from which point they will be assessed in the UK on their worldwide income and capital gains regardless of whether or not they are remitted to the UK.
- ii) when deciding an individual's UK tax residence, days of arrival in the UK and days of departure will be considered as resident days, when by extra statutory concession, they had been regarded as non-resident days.
- iii) if an individual continues to use the remittance basis of taxation as in i) above,

the taxpayer will not be entitled to claim personal allowances against their tax in the UK

- iv) certain anti tax avoidance measures are to be introduced under the following headings
 - * the source of funds exemption is to be abolished
 - * alienation of income and gains through the use of offshore structures such as companies and trusts which convert taxable income and gains into non-taxable payments will be abolished
 - * extension of the definition of remittance in connection with foreign income
- v) the zero rate threshold for IHT for married couples and civil partners was increased to £600,000.

Once again and as with Osborne and the Tory proposals what is proposed does not appear to stand up to detailed consideration.

- a) The circa 20,000 very rich will be happy to pay the £30,000 and forego their personal allowances. For the rest of the non-domiciliaries, if they have done their non-domicile planning properly, they can forego the remittance basis and mitigate the negative consequences. The revenue gained from this will be as small as for the Tories.
- b) It is the case that HMRC have already attacked successfully those who make very regular visits to the UK, with the Commissioners agreeing that the days of arrival and days of departure may be considered as resident days. There is nothing new in this, and it has already affected those who make regular visits.

For those who make infrequent visits the consequences are insignificant.

- c) For non-domiciliaries who use the remittance basis, they are normally wealthy. The loss of personal allowances will not concern them.
- d) We cannot comment on the anti-avoidance rules proposed as the detail of these is yet to be disclosed. From the headings however, for those who have done their wealth planning effectively, there does not appear to be any grounds for concern.
- e) While the increase in the IHT threshold to £600,000 was an attempt to compete with the Tory proposals, this is not a concession or increased allowance. For those who plan properly they will already get a £600,000 allowance if they are a couple. For single people the threshold remains at £300,000.

There is one feature which is common to both proposals. Both have "tinkered" with both IHT thresholds, residence rules, domicile and related issues. Neither the Tories nor the Labour Party have attacked the fundamental concept of UK domicile. That's important.

Finally, I must stress that we have yet to see the details of both proposals. We will have detail on the Labour proposals later in the year and will comment then if they are relevant. We will have to wait longer for Mr Osborne and the Tory proposals to be spelt out in detail, as this will not be available until the Tories come to power.

The above comment is based therefore on the detail and facts that have been published thus far. No actions should be taken by any reader of this note except under appropriate professional advice.

N.B. Bentley FCA

11.10.2007

HMRC's attack on undeclared interest from offshore accounts

You will be aware of the ongoing "attack" on offshore bank accounts by Her Majesty's Revenue and Customs (HMRC) in relation to possible undeclared interest (Tax Evasion).

Background

HMRC suspected that there were a significant number of "offshore" accounts held by UK Tax resident individuals where the interest on those accounts was not being declared for Tax in the UK.

Accordingly HMRC approached the major high street banks with offshore banking units (Jersey, Guernsey, IOM etc) and asked them to disclose details of all accounts held offshore which were owned by UK resident individuals. On the grounds that to provide this information would be a breach of client confidentiality, most banks refused to provide the information requested. HMRC took the matter to court and the courts ruled that HMRC were entitled to receive the information they had requested.

Amnesty offered

Faced with the prospect of having to consider a substantial number of cases that they did not have the human resource to handle, HMRC offered a short window of opportunity to Taxpayers who had not declared income arising on their offshore accounts. Taxpayers could come clean and suffer only the arrears of tax due with interest and a penalty of just 10%. The initial phase of this amnesty, required offending taxpayers to register with HMRC by 22 June 2007 stating their intention to make full disclosure.

The second stage gave Taxpayers until 26 November 2007 to provide full details and pay the arrears of tax due together with the appropriate interest and penalty.

Where are we now?

1. We are told that HMRC have identified 400,000 names from their trawl of

information provided by the major banks with offshore facilities. We are told that only 60,000 people took the initial step required by 22 June. This leaves a large number of taxpayers who have not made disclosure.

2. Although the initial stage has passed for the reduced "10%" penalty, it is not too late for taxpayers to make full disclosure to their tax office and remain in a position to mitigate the potential penalties.
3. How will HMRC approach to the remaining names they are interested in?
 - i) HMRC may identify the larger tax liabilities first
 - ii) They may undertake a matching procedure, comparing information they have on file with the information supplied by the taxpayer
 - iii) They may identify Taxpayers against whom they may wish to take criminal proceedings

It will depend largely upon the manpower available to them and the detail of each case

4. We understand that HMRC are currently sending out request letters for information to individuals who they suspect may not have made full disclosures in the past.
5. We are told that, flushed with the success of the initial exercise, HMRC have sent out requests for information to an additional 170 institutions such as building societies, small banks and financial advisers.

It is clear that the momentum of this exercise is increasing.

What should you do if you receive such a letter?

You should not panic. If you receive a letter this does not mean that HMRC believe you are involved in Tax evasion. It means only that some institution has disclosed that they hold offshore an account which bears your name and address. I must stress that there is nothing to prevent a UK resident individual having an offshore bank account, and in some cases it can be advantageous to do so.

However, you will be wise to seek professional advice on how to respond to the letter you receive. Advice which we can provide.

Stuart Hambling
2.11.2007

THE BENTLEY REID GROUP

www.bentleyreidgroup.com

The Bentley Reid Group was founded in 1978. The Group seeks to provide contemporary wealth management advice and solutions, while emphasising the more traditional values of efficiency, discretion and personal service. The Group has four main activities that can be accessed individually or that can come together to provide you and your family with an integrated personal wealth management service.

TAX & GENERAL FINANCIAL ADVICE - www.Bentley-Reid.com

Our professional staff can help you to resolve an isolated problem or advise you on how best to structure the whole of your financial affairs. Bentley Reid seeks to ensure the tax efficient security and growth of your wealth and offers continuity of advice during your lifetime and for your family and heirs thereafter. Advice is offered on a multi-jurisdictional basis from our offices in London and Hong Kong.

INVESTMENT MANAGEMENT & ADVICE - www.Bentley-Capital.com

Bentley Capital offers a comprehensive range of investment services, satisfying the requirements of regular savers and those with substantial capital. We have extensive experience managing individual portfolios, Trust and Charity monies and personal pension funds, focusing on achieving the clients stated aims with the agreed level of risk and volatility. Some of our more popular mandates have been replicated as larger pooled funds: for further details please see www.bc-funds.com.

TRUST & COMPANY MANAGEMENT - www.Bentley-Trust.com

Bentley Trust is a fully authorised Trust company, focusing on efficient, flexible, compliant service provision. If required in the overall structure of your financial affairs, our Executives can set up and administer trusts and companies, working with your chosen advisers to provide a robust, legitimate, enduring solution.

UK PROPERTY SERVICES - www.BRProperty-Services.com

In conjunction with trusted third parties, we have extensive experience managing all aspects of private client residential and commercial property ownership. We can administer every aspect of physical property ownership including the initial search, purchase negotiations, renovations, sourcing a tenant and on-going rental management. In addition we can provide advice on both quoted and unquoted property investments and the most tax efficient way to hold any property interest.

CONTACT DETAILS - For further information, please contact:

UK:	Ralph Davis	rdavis@bentleyreid.co.uk
	Tel 020 7222 5888	Fax 020 7222 6880
HK:	Melody Rooke	mrooke@bentleyreid.com.hk
	Tel 2810 1233	Fax 2810 0849