

February 6, 2008

## Downunder Daily

### Taking Credit

**Having briefly – but violently – reconnected, asset markets again disconnected in response to looser fiscal and monetary policy in the US.** Wall Street bounced almost 10% from its intra-day January lows, led by sharp rallies in some cyclical sectors. Credit markets, by contrast, barely responded. (Exhibit 1 shows a selection of credit indicators.)

A few thoughts on this:

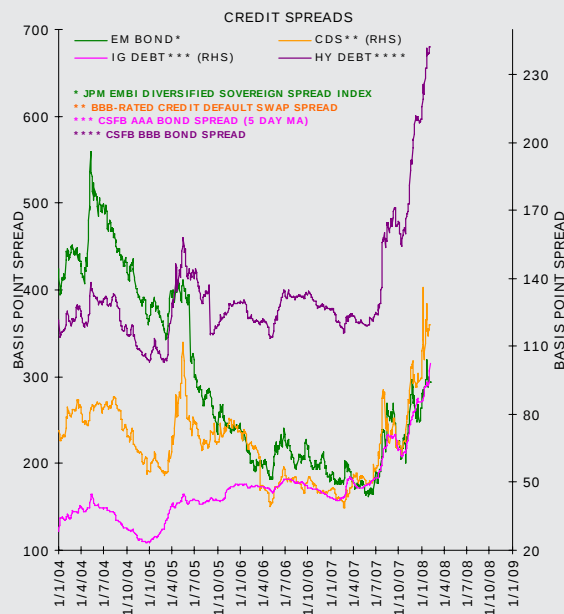
First, equity-credit market disconnect is not unusual at turning points. Our credit team refers to the 'equity-credit' clock, showing how credit and equity markets can move out of synch (see Neil McLeish, *Bear Market Update*, 23 January). Exhibit 2 shows a long-term series of US corporate bond spreads (using the Moody's seasoned BAA series). Spreads typically peak late in a recession, or even after the recession has ended. Equities, meanwhile, usually rally before a recession has ended. Hence, the general rule: Credit is quicker to price recession than equity, while equity is quicker to price recovery than credit.

Second, the current disconnect between equities and long-end Treasuries is more unusual. Long-end Treasury yields usually start to rise before the Fed finishes easing, in anticipation of recovery. In other words, if the equity market rally really reflects investors anticipating recovery – rather than, say, a short-covering rally – it would be usual for Treasury yields to be rising, not falling.

Third, the disconnect between Treasuries and equities is maintaining the apparent relative value of equities versus debt. The well-know Fed model – which compares the yield on equities and Treasuries – continues to signal that equities are at almost unprecedented levels of relative attractiveness, despite the bounce from the lows.

Exhibit 1

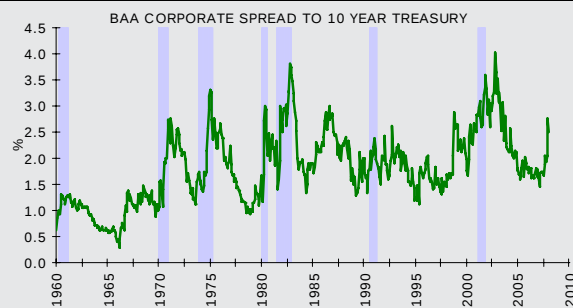
### No Relief in Credit



Source: Bloomberg; Morgan Stanley Research

Exhibit 2

### Credit Recovers Late



Source: Moody's, BEA; Morgan Stanley Research

Morgan Stanley does and seeks to do business with companies covered in Morgan Stanley Research. As a result, investors should be aware that the firm may have a conflict of interest that could affect the objectivity of Morgan Stanley Research. Investors should consider Morgan Stanley Research as only a single factor in making their investment decision.

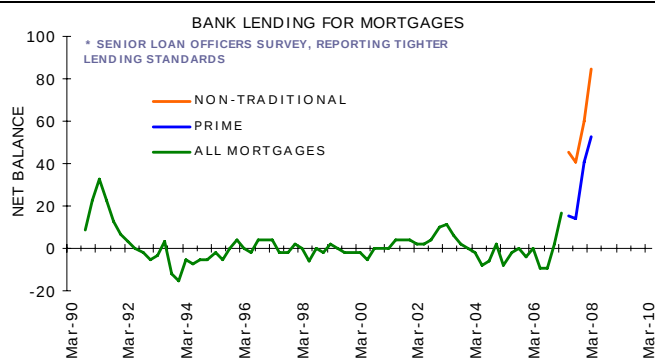
**For analyst certification and other important disclosures, refer to the Disclosure Section, located at the end of this report.**

+ = Analysts employed by non-US affiliates are not registered pursuant to NASD/NYSE rules

February 6, 2008  
Strategy and Economics

Whether the usual lead-lag disconnects between credit and equity hold true in this cycle is a moot point, in my view. It's moot because the credit boom – centered on the consumer – was a key driver of growth (and hence earnings) through the expansion phase. The fact that credit remains in a funk therefore will have particularly important economic implications in this cycle – and that, in turn, will likely affect how policy works (or doesn't), as well as corporate earnings and equity performance.

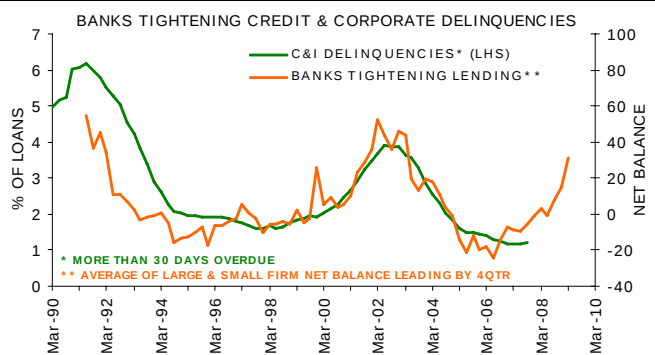
Exhibit 3  
**Tighter Still**



Source: Federal Reserve; Morgan Stanley

In this context, it's critical to remember that we are still very early in the recession cycle. I think it's almost inconceivable that credit providers will loosen lending standards in the midst of the downturn. (That's not to say that market pricing of credit products will remain in a bear market – our credit team thinks that spreads will widen before narrowing by year-end. See Greg Peters, *Credit Strategy Conference Call* presentation, 4 February.)

Exhibit 4  
**Bankers Tighten Ahead of Bad Debt Rise**



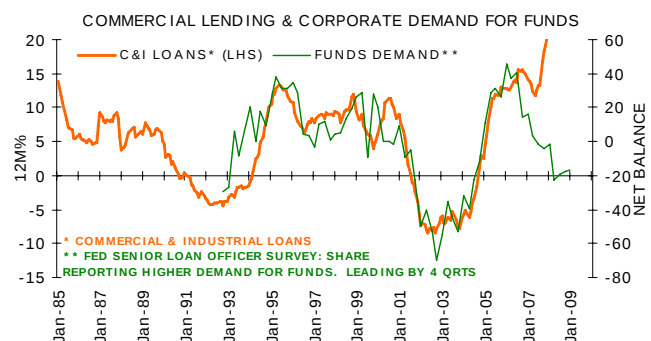
Source: Federal Reserve; Morgan Stanley Research

The Fed's survey of senior loan officers, released yesterday, showed another material tightening in lending standards. Exhibit 3 shows the net balance of respondents tightening mortgage lending standards. (The Fed has only recently asked for separate responses on different mortgage types, but the balance tightening on prime mortgages is now higher than any previous measure for the overall mortgage market.)

Lenders are also tightening standards for commercial borrowers. While it is true that the household sector is the epicenter of credit risk in this cycle, the change in bankers' lending standards has historically provided a good lead on commercial loan delinquencies (Exhibit 4).

Bankers are also reporting reduced fund demand from the corporate sector. This demand indicator typically leads commercial and industrial loan volumes – the recent divergence (Exhibit 5) presumably reflects in part the re-intermediation of previously off-balance-sheet lending vehicles.

Exhibit 5  
**Corporate Credit Demand Easing**



Source: Federal Reserve; Morgan Stanley Research

The important economic point is that tighter lending standards will reduce the effectiveness of monetary policy. Yes, lending standards usually get tightened in a downturn, but this time the tightening seems extraordinary for households – the most restrictive in the history of the Fed survey – which contrasts with the prior recession, which saw little or no lift in lending standards. This supply-side restraint will compound likely lackluster demand for credit, as households focus on reducing debt burdens and leverage rates. The serious economic effects of the ongoing credit malaise suggest that equity markets will struggle to see a sustained rally much ahead of a sustained improvement in credit conditions – and that seems some way off.



## Disclosure Section

The information and opinions in Morgan Stanley Research were prepared or are disseminated by Morgan Stanley Asia Limited (which accepts the responsibility for its contents) and/or Morgan Stanley Asia (Singapore) Pte. (Registration number 199206298Z, regulated by the Monetary Authority of Singapore, which accepts the responsibility for its contents), and/or Morgan Stanley Asia (Singapore) Securities Pte Ltd (Registration number 200008434H, regulated by the Monetary Authority of Singapore, which accepts the responsibility for its contents), and/or Morgan Stanley Taiwan Limited and/or Morgan Stanley & Co International plc, Seoul Branch, and/or Morgan Stanley Australia Limited (A.B.N. 67 003 734 576, holder of Australian financial services license No. 233742, which accepts responsibility for its contents), and/or Morgan Stanley India Company Private Limited and their affiliates (collectively, "Morgan Stanley"). For important disclosures, stock price charts and rating histories regarding companies that are the subject of this report, please see the Morgan Stanley Research Disclosure Website at [www.morganstanley.com/researchdisclosures](http://www.morganstanley.com/researchdisclosures), or contact your investment representative or Morgan Stanley Research at 1585 Broadway, (Attention: Equity Research Management), New York, NY, 10036 USA.

### Analyst Certification

The following analysts hereby certify that their views about the companies and their securities discussed in this report are accurately expressed and that they have not received and will not receive direct or indirect compensation in exchange for expressing specific recommendations or views in this report: Gerard Minack. Unless otherwise stated, the individuals listed on the cover page of this report are research analysts.

### Global Research Conflict Management Policy

Morgan Stanley Research has been published in accordance with our conflict management policy, which is available at [www.morganstanley.com/institutional/research/conflict/policies](http://www.morganstanley.com/institutional/research/conflict/policies).

### Important US Regulatory Disclosures on Subject Companies

The research analysts, strategists, or research associates principally responsible for the preparation of Morgan Stanley Research have received compensation based upon various factors, including quality of research, investor client feedback, stock picking, competitive factors, firm revenues and overall investment banking revenues.

Certain disclosures listed above are also for compliance with applicable regulations in non-US jurisdictions.

### STOCK RATINGS

Morgan Stanley uses a relative rating system using terms such as Overweight, Equal-weight or Underweight (see definitions below). Morgan Stanley does not assign ratings of Buy, Hold or Sell to the stocks we cover. Overweight, Equal-weight and Underweight are not the equivalent of Buy, Hold and Sell. Investors should carefully read the definitions of all ratings used in Morgan Stanley Research. In addition, since Morgan Stanley Research contains more complete information concerning the analyst's views, investors should carefully read Morgan Stanley Research, in its entirety, and not infer the contents from the rating alone. In any case, ratings (or research) should not be used or relied upon as investment advice. An investor's decision to buy or sell a stock should depend on individual circumstances (such as the investor's existing holdings) and other considerations.

### Global Stock Ratings Distribution

(as of January 31, 2008)

For disclosure purposes only (in accordance with NASD and NYSE requirements), we include the category headings of Buy, Hold, and Sell alongside our ratings of Overweight, Equal-weight and Underweight. Morgan Stanley does not assign ratings of Buy, Hold or Sell to the stocks we cover. Overweight, Equal-weight, and Underweight are not the equivalent of buy, hold, and sell but represent recommended relative weightings (see definitions below). To satisfy regulatory requirements, we correspond Overweight, our most positive stock rating, with a buy recommendation; we correspond Equal-weight to hold and Underweight to sell recommendations, respectively.

| Stock Rating Category    | Coverage Universe |            | Investment Banking Clients (IBC) |                |                      |
|--------------------------|-------------------|------------|----------------------------------|----------------|----------------------|
|                          | Count             | % of Total | Count                            | % of Total IBC | % of Rating Category |
| <b>Overweight/Buy</b>    | <b>1048</b>       | <b>44%</b> | <b>333</b>                       | <b>45%</b>     | <b>32%</b>           |
| <b>Equal-weight/Hold</b> | <b>986</b>        | <b>41%</b> | <b>308</b>                       | <b>42%</b>     | <b>31%</b>           |
| <b>Underweight/Sell</b>  | <b>346</b>        | <b>15%</b> | <b>98</b>                        | <b>13%</b>     | <b>28%</b>           |
| <b>Total</b>             | <b>2,380</b>      |            | <b>739</b>                       |                |                      |

Data include common stock and ADRs currently assigned ratings. An investor's decision to buy or sell a stock should depend on individual circumstances (such as the investor's existing holdings) and other considerations. Investment Banking Clients are companies from whom Morgan Stanley or an affiliate received investment banking compensation in the last 12 months.

### Analyst Stock Ratings

Overweight (O or Over) - The stock's total return is expected to exceed the total return of the relevant country MSCI Index, on a risk-adjusted basis over the next 12-18 months.

Equal-weight (E or Equal) - The stock's total return is expected to be in line with the total return of the relevant country MSCI Index, on a risk-adjusted basis over the next 12-18 months.

Underweight (U or Under) - The stock's total return is expected to be below the total return of the relevant country MSCI Index, on a risk-adjusted basis, over the next 12-18 months.

More volatile (V) - We estimate that this stock has more than a 25% chance of a price move (up or down) of more than 25% in a month, based on a quantitative assessment of historical data, or in the analyst's view, it is likely to become materially more volatile over the next 1-12 months compared

with the past three years. Stocks with less than one year of trading history are automatically rated as more volatile (unless otherwise noted). We note that securities that we do not currently consider "more volatile" can still perform in that manner. Unless otherwise specified, the time frame for price targets included in Morgan Stanley Research is 12 to 18 months.

## Analyst Industry Views

Attractive (A): The analyst expects the performance of his or her industry coverage universe over the next 12-18 months to be attractive vs. the relevant broad market benchmark, as indicated below.  
 In-Line (I): The analyst expects the performance of his or her industry coverage universe over the next 12-18 months to be in line with the relevant broad market benchmark, as indicated below.  
 Cautious (C): The analyst views the performance of his or her industry coverage universe over the next 12-18 months with caution vs. the relevant broad market benchmark, as indicated below.  
 Benchmarks for each region are as follows: North America - S&P 500; Latin America - relevant MSCI country index or MSCI Latin America Index; Europe - MSCI Europe; Japan - TOPIX; Asia - relevant MSCI country index.

## Other Important Disclosures

Morgan Stanley produces a research product called a "Tactical Idea." Views contained in a "Tactical Idea" on a particular stock may be contrary to the recommendations or views expressed in this or other research on the same stock. This may be the result of differing time horizons, methodologies, market events, or other factors. For all research available on a particular stock, please contact your sales representative or go to Client Link at [www.morganstanley.com](http://www.morganstanley.com).

For a discussion, if applicable, of the valuation methods used to determine the price targets included in this summary and the risks related to achieving these targets, please refer to the latest relevant published research on these stocks.

Morgan Stanley Research does not provide individually tailored investment advice. Morgan Stanley Research has been prepared without regard to the individual financial circumstances and objectives of persons who receive it. The securities/instruments discussed in Morgan Stanley Research may not be suitable for all investors. Morgan Stanley recommends that investors independently evaluate particular investments and strategies, and encourages investors to seek the advice of a financial adviser. The appropriateness of a particular investment or strategy will depend on an investor's individual circumstances and objectives. The securities, instruments, or strategies discussed in Morgan Stanley Research may not be suitable for all investors, and certain investors may not be eligible to purchase or participate in some or all of them.

Morgan Stanley Research is not an offer to buy or sell or the solicitation of an offer to buy or sell any security/instrument or to participate in any particular trading strategy. The "Important US Regulatory Disclosures on Subject Companies" section in Morgan Stanley Research lists all companies mentioned where Morgan Stanley owns 1% or more of a class of common securities of the companies. For all other companies mentioned in Morgan Stanley Research, Morgan Stanley may have an investment of less than 1% in securities or derivatives of securities of companies and may trade them in ways different from those discussed in Morgan Stanley Research. Employees of Morgan Stanley not involved in the preparation of Morgan Stanley Research may have investments in securities or derivatives of securities of companies mentioned and may trade them in ways different from those discussed in Morgan Stanley Research. Derivatives may be issued by Morgan Stanley or associated persons.

Morgan Stanley and its affiliate companies do business that relates to companies/instruments covered in Morgan Stanley Research, including market making and specialized trading, risk arbitrage and other proprietary trading, fund management, commercial banking, extension of credit, investment services and investment banking. Morgan Stanley sells to and buys from customers the securities/instruments of companies covered in Morgan Stanley Research on a principal basis.

With the exception of information regarding Morgan Stanley, research prepared by Morgan Stanley Research personnel are based on public information. Morgan Stanley makes every effort to use reliable, comprehensive information, but we make no representation that it is accurate or complete. We have no obligation to tell you when opinions or information in Morgan Stanley Research change apart from when we intend to discontinue research coverage of a subject company. Facts and views presented in Morgan Stanley Research have not been reviewed by, and may not reflect information known to, professionals in other Morgan Stanley business areas, including investment banking personnel.

Morgan Stanley Research personnel conduct site visits from time to time but are prohibited from accepting payment or reimbursement by the company of travel expenses for such visits.

The value of and income from your investments may vary because of changes in interest rates or foreign exchange rates, securities prices or market indexes, operational or financial conditions of companies or other factors. There may be time limitations on the exercise of options or other rights in your securities transactions. Past performance is not necessarily a guide to future performance. Estimates of future performance are based on assumptions that may not be realized. Unless otherwise stated, the cover page provides the closing price on the primary exchange for the subject company's securities/instruments.

To our readers in Taiwan: Information on securities/instruments that trade in Taiwan is distributed by Morgan Stanley Taiwan Limited ("MSTL"). Such information is for your reference only. The reader should independently evaluate the investment risks and is solely responsible for their investment decisions. Morgan Stanley Research may not be distributed to the public media or quoted or used by the public media without the express written consent of Morgan Stanley. Information on securities/instruments that do not trade in Taiwan is for informational purposes only and is not to be construed as a recommendation or a solicitation to trade in such securities/instruments. MSTL may not execute transactions for clients in these securities/instruments.

To our readers in Hong Kong: Information is distributed in Hong Kong by and on behalf of, and is attributable to, Morgan Stanley Asia Limited as part of its regulated activities in Hong Kong. If you have any queries concerning Morgan Stanley Research, please contact our Hong Kong sales representatives.

Certain information in Morgan Stanley Research was sourced by employees of the Shanghai Representative Office of Morgan Stanley Asia Limited for the use of Morgan Stanley Asia Limited.

Morgan Stanley Research is disseminated in Japan by Morgan Stanley Japan Securities Co., Ltd.; in Hong Kong by Morgan Stanley Asia Limited (which accepts responsibility for its contents); in Singapore by Morgan Stanley Asia (Singapore) Pte. (Registration number 199206298Z) and/or Morgan Stanley Asia (Singapore) Securities Pte Ltd (Registration number 200008434H), regulated by the Monetary Authority of Singapore, which accepts responsibility for its contents; in Australia by Morgan Stanley Australia Limited A.B.N. 67 003 734 576, holder of Australian financial services licence No. 233742, which accepts responsibility for its contents; in Korea by Morgan Stanley & Co International plc, Seoul Branch; in India by Morgan Stanley India Company Private Limited; in Canada by Morgan Stanley Canada Limited, which has approved of, and has agreed to take responsibility for, the contents of Morgan Stanley Research in Canada; in Germany by Morgan Stanley Bank AG, Frankfurt am Main, regulated by Bundesanstalt fuer Finanzdienstleistungsaufsicht (BaFin); in Spain by Morgan Stanley, S.V., S.A., a Morgan Stanley group company, which is supervised by the Spanish Securities Markets Commission (CNMV) and states that Morgan Stanley Research has been written and distributed in accordance with the rules of conduct applicable to financial research as established under Spanish regulations; in the United States by Morgan Stanley & Co. Incorporated, which accepts responsibility for its contents. Morgan Stanley & Co. International plc, authorized and regulated by Financial Services Authority, disseminates in the UK research that it has prepared, and approves solely for the purposes of section 21 of the Financial Services and Markets Act 2000, research which has been prepared by any of its affiliates. Private U.K. investors should obtain the advice of their Morgan Stanley & Co. International plc representative about the investments concerned. In Australia, Morgan Stanley Research, and any access to it, is intended only for "wholesale clients" within the meaning of the Australian Corporations Act. RMB Morgan Stanley (Proprietary) Limited is a member of the JSE Limited and regulated by the Financial Services Board in South Africa. RMB Morgan Stanley (Proprietary) Limited is a joint venture owned equally by Morgan Stanley International Holdings Inc. and FirstRand Investment Holdings Limited, which is wholly owned by FirstRand Limited.

The information in Morgan Stanley Research is being communicated by Morgan Stanley & Co. International plc (DIFC Branch), regulated by the Dubai Financial Services Authority (the DFSA), and is directed at wholesale customers only, as defined by the DFSA. This research will only be made available to a wholesale customer who we are satisfied meets the regulatory criteria to be a client.

The information in Morgan Stanley Research is being communicated by Morgan Stanley & Co. International plc (QFC Branch), regulated by the Qatar Financial Centre Regulatory Authority (the QFCRA), and is directed at business customers and market counterparties only and is not intended for Retail Customers as defined by the QFCRA.

The trademarks and service marks contained in Morgan Stanley Research are the property of their respective owners. Third-party data providers make no warranties or representations of any kind relating to the accuracy, completeness, or timeliness of the data they provide and shall not have liability for any damages of any kind relating to such data. The Global Industry Classification Standard ("GICS") was developed by and is the exclusive property of MSCI and S&P.

Morgan Stanley has based its projections, opinions, forecasts and trading strategies regarding the MSCI Country Index Series solely on publicly available information. MSCI has not reviewed, approved or endorsed the projections, opinions, forecasts and trading strategies contained herein. Morgan Stanley has no influence on or control over MSCI's index compilation decisions.

Morgan Stanley Research, or any portion hereof may not be reprinted, sold or redistributed without the written consent of Morgan Stanley.

Morgan Stanley Research is disseminated and available primarily electronically, and, in some cases, in printed form.

**Additional information on recommended securities/instruments is available on request.**

**The Americas**

1585 Broadway  
New York, NY 10036-8293

**United States**

Tel: +1 (1) 212 761 4000

**Europe**

25 Cabot Square, Canary Wharf  
London E14 4QA

**United Kingdom**

Tel: +44 (0) 20 7 425 8000

**Japan**

4-20-3 Ebisu, Shibuya-ku  
Tokyo 150-6008

**Japan**

Tel: +81 (0) 3 5424 5000

**Asia/Pacific**

Three Exchange Square  
Central

**Hong Kong**

Tel: +852 2848 5200