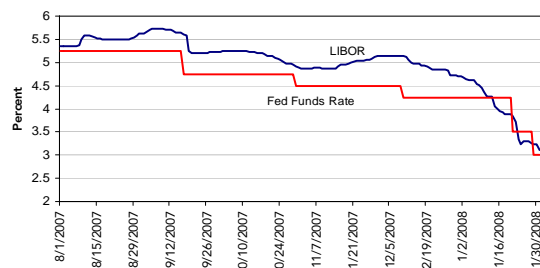


# Economic Review

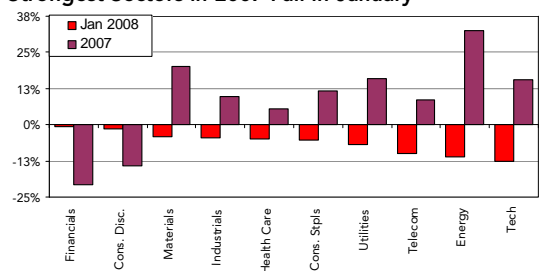
Economic worries sent global equity markets sharply lower in January. California lawmakers struggled with a \$14.5 billion budget deficit, brought on by falling property values and automatic spending increases, while also defeating a planned state-run comprehensive healthcare system. Homeowners in Nevada, California, and Florida experienced the largest drops in home values during 2007. Foreclosure rates rose, with the bulk of subprime loans still facing higher interest rate resets in 2008. The Presidential race narrowed to four strong candidates, with many delegate-rich states set to vote on February 5<sup>th</sup>.

## LIBOR Reconnects with Fed Funds Rate



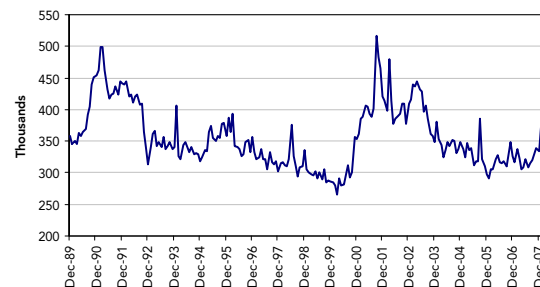
Source: Bloomberg

## Strongest Sectors in 2007 Fall in January



Source: Standard & Poor's  
Performance During Month of January and Year of 2007

## Initial Jobless Claims Rise



Source: Bloomberg

Following a shocking selloff in international stock markets, the Federal Reserve convened an emergency session and lowered interest rates 75bps on January 22<sup>nd</sup>. Eight days later, rates were lowered an additional 50bps, bringing the Fed Funds Rate and Discount Rate to 3.0% and 3.5%, respectively. Evidence of slowing growth, supported by a weakening employment outlook and continued housing turmoil, coupled with a view of inflation moderating later in 2008, provided support for the actions. The cumulative cuts were the largest in one month since October 1984.

U.S. consumer inflation rose 4.1% in 2007, while Eurozone inflation grew 3.2%. The European Central Bank remained reluctant to cut interest rates, reiterating an anti-inflation stance as support for its views. The Bank of England entered 2008 facing possible rate cuts as it deals with the beginning of an expected retraction in real estate markets, similar to that currently experienced by the United States.

Fourth quarter GDP growth slowed to 0.6%, while expanding 2.2% in 2007, well below the 3.3% average since 1983. Two consecutive quarters of negative GDP growth are necessary to define a recession.

President Bush and Congress debated an economic stimulus plan, which would provide one-time tax rebates and accelerate business deductions. The total dollar amount would be roughly equivalent to 1% of GDP. The plan also included addendums to allow Fannie Mae and Freddie Mac to purchase home loans up to a value of \$729,000, up from the current limit of \$417,000. The effectiveness of the plan remains unproven, as calls for permanent tax code changes were voiced.

Subprime loans continued to batter balance sheets, as evidenced by Merrill Lynch and Citibank. Merrill Lynch took losses of \$16.7 billion, and Citibank booked losses of \$18.1 billion on their subprime loan holdings. Citibank continued to hold nearly \$40 billion in subprime-related securities on its books. Large layoff announcements also accompanied Citibank's news of the writedowns.

Crude oil rose to \$100.09/barrel, before retreating to the low \$90s. Gold prices rose above \$942/ounce on fears of rising inflation and weakening growth. The previous nominal high of \$850/ounce was reached in 1980.

Financial stocks benefitted from lower interest rates, which widened the spread between their borrowing costs and the costs they charge businesses and consumers for loans. Bank of America announced plans to purchase troubled mortgage lender Countrywide for \$4 billion, a fraction of its value early in 2007.

### As of January 31, 2008

	January	3 Months	1 Year
<b>S&amp;P 500</b>	-6.0%	-10.6%	-2.3%
<b>Russell 1000 Value</b>	-4.0%	-9.6%	-5.4%
<b>Russell 1000 Growth</b>	-7.8%	-11.5%	0.5%
<b>Russell 2000</b>	-6.8%	-13.6%	-9.8%
<b>MSCI EAFE</b>	-9.2%	-14.2%	0.2%
<b>LB Agg</b>	1.7%	3.8%	8.8%
<b>3-Month T-Bills</b>	0.5%	1.3%	5.1%