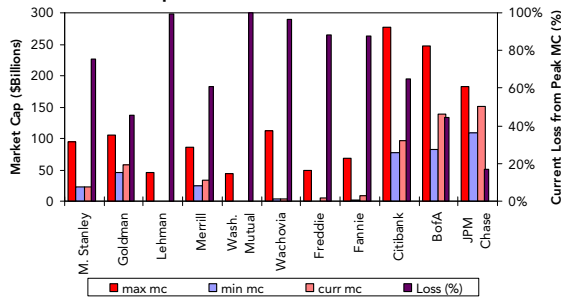


# Economic Review

The U.S. financial landscape changed dramatically in September as several venerable firms declared bankruptcy or were taken over as the wave of financial troubles expanded. The Treasury provided additional funds to the Federal Reserve to provide liquidity to banks as bank-to-bank lending remained stalled. The first attempt at a government buyout of tarnished mortgage debt from financial institutions failed after the U.S. House rejected a \$700 billion plan. The stock market reacted by losing \$1 trillion in value following the vote. As long as banks continue to hold undetermined amounts of bad debt on their books, lending activity around the world will remain constrained, and have long lasting effects on economic growth. The bailout plan attempted to remove bad debt and uncertain mortgage cashflows from banks' balance sheets so that a stable base of collateral at banks would allow interbank, consumer, and business lending to resume and limit economic pains.

## Bank Market Cap Losses

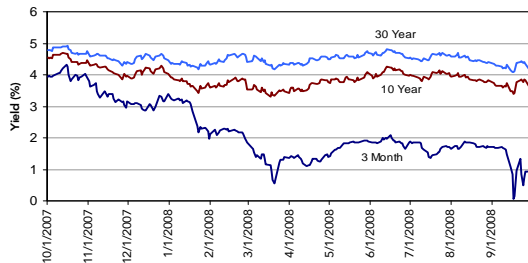


Source: Bloomberg Sept 1, 2006, Through Sept. 30, 2008

A highly volatile month in the stock markets unfolded when Fannie Mae and Freddie Mac were brought under the control of government agencies. As a dramatic reaction to worries about the companies' abilities to cover expected defaults on mortgages owned unfolded, the Treasury formally assumed responsibility for their obligations, keeping the companies from default and bankruptcy.

Lehman Brothers declared bankruptcy after it was unable to find emergency funding to cover impending obligations. Lehman's default was far reaching, resulting in several money-market funds falling below \$1/share. Many Lehman investors, bondholders, and counterparties lost billions of dollars in the aftermath. The same weekend, Merrill Lynch was bought by Bank of America for \$50 billion in stock. Merrill Lynch teetered on the edge of bankruptcy before B of A stepped in to add the investment bank to its expanding portfolio of financial services. The Treasury provided \$50 billion to backup non-Treasury and non-muni based money market funds and keep shares from falling below \$1.

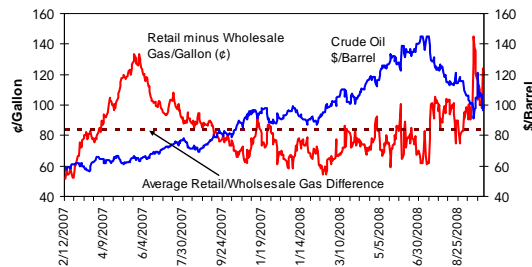
## Flight to Safety Lifts Treasury Prices; Yields Fall



Source: Lehman Brothers/Barclays

Following the Lehman and Merrill events, the two remaining large investment banks, Goldman Sachs and Morgan Stanley, raised additional capital and changed their official status to bank holding companies, a status that organizes the companies into deposit-based banks, in the format of Citigroup, B of A, etc.

## Retail Gasoline Lags Crude Oil's Plunge



Source: Bloomberg

Washington Mutual declared bankruptcy, marking the largest financial institution to become insolvent. The remains of the company were purchased by JPMorgan Chase. Wachovia Bank also declared bankruptcy, and was acquired by Citigroup for \$2 billion, with substantial guarantees from the federal government. The purchase gives Citigroup the third largest retail banking presence in the U.S.

The government took an 80% controlling interest in insurance giant AIG after the parent company became short on cash to pay upcoming obligations. The move allowed the company time to organize the sale of its underlying and highly profitable insurance businesses.

The SEC implemented a short term ban on short selling for 799 financial institutions. The move was mirrored in several European markets, as governments attempted to save banks that were not in imminent danger of collapse and protect the worldwide financial system.

Crude oil fell to a low of \$90.51 on forecasts of diminishing demand worldwide. Consumers have benefitted little from crude's 30% drop from its July peak, only seeing gasoline fall 11% over the same period. Refineries have been running below 80% capacity after damages from hurricanes Gustav and Ike, while demand continues to drop.

Unemployment rose to 6.1% in August, with high weekly jobless claims foretelling a higher September value. GM, Chrysler, and Ford were given \$25 billion in loan guarantees from the federal government, which are intended to further alternative fuel research and development.

### As of September 30, 2008

	September	3 Months	YTD
S&P 500	-8.9%	-8.4%	-19.3%
Russell 1000 Value	-7.4%	-6.1%	-18.9%
Russell 1000 Growth	-11.6%	-12.3%	-20.3%
Russell 2000	-8.0%	-1.1%	-10.4%
MSCI EAFE	-14.5%	-20.6%	-29.3%
LB Agg	-1.3%	-0.5%	0.6%
3-Month T-Bills	0.3%	0.6%	1.8%