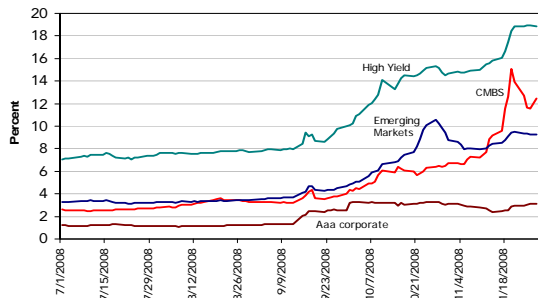


# Economic Review

History was made in November as Barack Obama won the Presidential election. Upon taking office, he will face tremendous financial upheaval in the markets, a slowing economy, and global adversaries challenging his resolve. Obama spent the month building his cabinet and crafting plans for a massive spending bill he will introduce in January, which is expected to include infrastructure investments, and may forego an income tax increase in the near-term. Europe and Japan marked a second quarter of negative growth, while China proposed a \$600 billion infrastructure plan to boost economic activity. Bond markets sent yields on non-Treasury bonds soaring, reflecting the continued fall of asset prices and collateral values, as well as an expected upturn in corporate defaults. The 10-Year Treasury yield briefly fell below 3%, as demand rose to record levels for secure debt issues.

## Bond Yields Reflect Market Unease

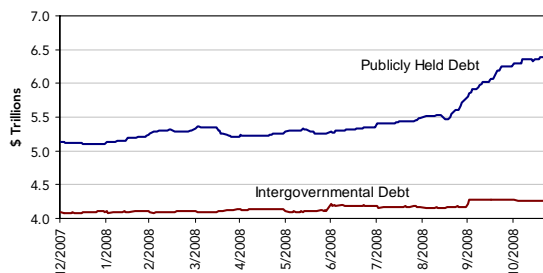


Yield minus 10-Year Treasury Bond Yield  
Source: Barclays

The stock market remained decidedly negative through most of November. Citibank's stock declined from \$13.65 on October 31, to just over \$3 mid-month. Lingering concerns over non-performing assets, management's ability to set a path for recovery, and coordinated selling efforts forced the bank to seek a second government bailout. The new deal gives \$20 billion in additional capital, and puts the government on the hook for 90% of its bad debt, which is around \$300 billion.

Investors were stunned as Treasury Secretary Paulson scrapped plans to purchase bad debt from financial institutions, changing the original mandate of the Troubled Assets Relief Program (TARP). Instead, his new focus would be to directly inject capital into the companies. The original plan was rejected because of the time needed to implement purchases, and the resulting loss in bank capital that would have resulted if assets were sold at fire-sale prices.

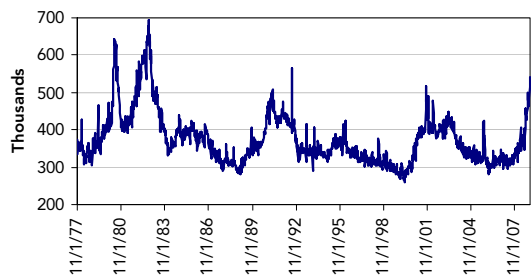
## U.S. Federal Debt Soars Ever Higher



Source: U.S. Treasury

GM, Ford, and privately-held Chrysler appealed to the federal government for financial assistance. As the companies spent down billions from their cash reserves to fund ongoing operations, they were brought to within months of bankruptcy. Weak auto sales and high labor costs led to the financial squeeze. The companies asked to use the \$25 billion that Congress pledged for research and development to fund day-to-day operations. The companies, when asked for plans detailing their paths to recovery, were unprepared and their appeal was summarily rejected by Congress, pending a second hearing in early December. The three automakers will likely be able to restructure labor agreements only through bankruptcy proceedings. The possibility of a quick turnaround in a dismal sales market is negligible. The companies face a tough hurdle to increase market share at a time when the largest segment of buyers shun the companies' offerings. New designs typically take three years to reach the market, and convincing skeptical buyers about quality advancements and long-term viability in the interim is a difficult obstacle to overcome.

## Initial Weekly Jobless Claims



Source: Bloomberg

The cost to taxpayers for the numerous bailouts has both short and long-term consequences. The federal debt owed to the public (excluding social security and other similar lending) has risen \$1.2 trillion since Bear Stearns was sold in February 2008. Every U.S. citizen now owes nearly \$21,000 on this debt, and pays \$800/year in interest. The long term effects of bailouts for companies that ultimately fail or destroy large amounts of capital are felt in the lost opportunities for other companies to receive investments and develop new products. It is akin to investors trying to save vacuum tube manufacturers at the expense of investing in fledgling transistor companies. Misallocations and losses of capital stunt growth and prevent new technologies from being developed, and ultimately lead to a higher rate of unemployment.

The unemployment rate rose in October to 6.5%. Mass layoffs in most industries are expected to continue as the economy contracts. Consumer spending slowed, and is expected to remain subdued. State and local governments, which budgeted for best-possible situations, now face layoffs and cutbacks as their revenues fall sharply lower and the consequences of unchecked spending growth rise.

### As of November 30, 2008

	November	3 Months	YTD
S&P 500	-7.2%	-29.7%	-37.7%
Russell 1000 Value	-7.2%	-28.9%	-37.7%
Russell 1000 Growth	-8.0%	-32.9%	-39.5%
Russell 2000	-11.8%	-35.7%	-37.4%
MSCI EAFE	-5.4%	-35.4%	-46.6%
Barclays Agg	3.3%	-0.5%	1.5%
3-Month T-Bills	0.1%	0.5%	2.1%