



Quarterly Economic Report – 3rd Quarter 2008

Outlook and Strategy

The third quarter of 2008 saw an upheaval to the global economic system that is unprecedented in scope and size. Some of the oldest, most storied names in financial services have either been acquired or failed and these problems have spread to Europe and Asia.

Any thoughts of the Federal Reserve Bank tightening monetary policy have disappeared as emergency plans have been implemented by both the US Treasury and the Federal Reserve to inject liquidity into the global banking systems. Failure to do so could have left the banking system damaged beyond repair.

At the core of this problem is a “distrust” of the intrinsic value of many types of financial assets. These assets had been used to collateralize loans and when there was no longer an active mechanism to provide a market value for these assets; borrowers could not obtain funding for the loans. The failure of several issuers of financial debt, especially Lehman Brothers and Bear Stearns, has now effectively shut down the credit markets and borrowers ranging in size from multi-billion dollar customers to one man businesses are finding it impossible to obtain loans at almost any price.

Consumer lending has suffered as well and this darkens the picture for auto dealers and other sellers of big ticket items. It has been observed that under current lending standards a FICO score of 720 or higher is required to get a car loan at standard interest rates. This credit rating is only achieved by less than 10 percent of all Americans.

Job losses are another result of the credit tightening. The monthly Non-Farm Payrolls report has been negative for nine consecutive months and on a year to date basis, we have seen a net job loss of almost 600,000 jobs. The Unemployment Rate has moved above 6% and is expected to rise significantly over the next few months. Currently, we are at a multi-year high on the number of people who are collecting unemployment benefits.

Congress has enacted an emergency spending plan which allocates over \$700 Billion dollars for the US Treasury to acquire non-performing assets from domestic financial institutions. It is hoped this measure may improve liquidity and, if not stimulate growth; at least provide some measure of stability to stop the economic downturn.

The Federal Reserve Bank has shifted into crisis mode as well. They have created several new and unusual processes to add funds to a banking system that has become frozen in place. The longer term outlook is clouded as the extent this will spread beyond the US markets is yet to be seen. It may ultimately take a multi-national approach by all the G-8 members to end the crisis. To this end, interest rates will probably decline over the next several quarters, a dramatic change to the outlook just a few weeks ago.