

Russell Update

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History in the Making: Paulson and Bernanke Show Spectacular Leadership in a Time of Crisis

Erik Ristuben, Russell Investments' Chief Investment Officer, Multi-Strategy Solutions, addresses the historic bail-out by the U.S. central bank today.*

Note the date, note the players. While it is way too early to declare victory, and there are many uncertainties that lie ahead, September 18, 2008 will likely go down as one of the most important dates in financial market history. In our industry, the significance of specific dates is all too often associated with pain and tragedy. Yesterday may also be remembered with such attributes. But I believe that it is more likely that it's historical significance will be as the day that signaled the culmination of a spectacular display of governance and leadership of the two individuals, whom above all others are entrusted with the economic futures of our nation and the world, U.S. Secretary of the Treasury Henry Paulson and the Chairman of the U.S. Federal Reserve Ben Bernanke.

These men have faced the most complex potential financial crisis in history with creativity and bold action. Yesterday's action appears to be the culmination of what I believe will be a successful attempt to address overwhelming market concerns regarding liquidity and solvency that have played havoc with the global financial markets. Given the level of well documented financial dislocation associated with the mortgage market, and the subsequent securitization of that debt and the astounding leverage assumed by financial institutions, the unwinding of those excesses was destined to be painful. The mandate that Paulson and Bernanke have had -- and continue to have -- is to make sure that it is not fatal. As we have been saying many times over this year, the markets' volatility has had much to do with the probability that the financial service sector of the US, and perhaps the world, would fail. The probability of this outcome has not been viewed as likely, but at times, the market considered the probability of its occurrence as greater than zero. And that thought made people scared, causing panic, which was compounded by the screaming headlines these past few days. The panic in money markets began Tuesday, when the Reserve Primary Fund, a money-market mutual fund whose assets under management have tumbled 65 percent in recent weeks, fell below \$1 a share in net asset value, because of its losses on debt issued by Lehman Brothers Holdings Inc.

What has happened beginning Thursday afternoon (September 18), is a concerted global effort to address the fundamental issues facing our markets. In excess of US\$250 Billion dollars in liquidity were pumped into the system and a "Resolution Trust Company" (RTC) like entity has been proposed to remove the corrosive contaminate of "toxic waste" mortgage related debt from the balance sheet of the financial services industry and onto the one entity capable of owning it long enough to realize its likely economic value regardless of current market sentiment, the US government. In addition, both the US and the UK have now banned short selling of financial services companies for at least the next two weeks. Finally, they are directly addressing the money market issues by providing funds to banks to buy commercial paper to allow for early redemptions. In the US, these efforts have broad bi-partisan support, some of the earliest comments supporting the creation of an RTC for this crises were from democratic Congressman Barney Frank and democratic Senator Chuck Schumer, notable for a number of reasons, the most significant of course being that they are the Chairmen of the House and Senate Finance Committees. Such serendipity is rarely coincidental.

Early returns on these moves have been dramatic: since the first RTC whispers late in trading day yesterday, the Dow Jones Index moved over 600 points in roughly an hour and a half, Asia rallied in Friday trading, Europe rallied and emerging markets surged over 8%. The S&P/TSX Composite Index has surged over 500 basis points so far.

The level of pain and stress of the early week, although extremely difficult for all involved, was likely necessary. In order for the markets to view the actions of the last 24 hours so favorably, and without notable dissension, it had to be the case that the urgency of the situation had to be clear to all -- and the danger palpable. This level of understanding likely created the political and economic cover for the authorities to act in ways that would not have been possible earlier.

Again, it is too early for any of us to say definitively that the worst is over; only the passage of time will make that clear. All I am saying is note the date and note the players, because history will.

The U.S. Government's Plan

- [The Treasury said it would use \\$50 billion to back money market mutual funds](#) whose asset values fall below \$1 a share. The intent is to shore up ailing money markets after signs that this long-safe corner of financial markets, home to some \$3.5 trillion of deposits, was at risk of falling victim to the year-old credit crunch. The Treasury said concerns about the net asset value of money market funds falling below \$1 have exacerbated global financial market turmoil and caused severe liquidity strains in world markets. 1
- [The Federal Reserve said it would lend even more money](#) directly to financial institutions so they could purchase certain assets from money market funds. 2
- [The SEC temporarily banned short-selling](#) on 799 financial stocks to boost investor confidence on Friday, one day after the UK Financial Services Authority took a similar step. 3

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