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## Erik Ristuben, CIO for client investment strategies at Russell Investments comments on:

- The current US economic situation
- US corporate earnings

Erik Ristuben, Chief Investment Office (CIO) for client investment strategies at Russell Investments, provides his latest market outlook:

### The current US economic situation

**Q: The US is in a fourth quarter scenario. Congress and the White House are still in talks about raising the debt ceiling and a resolution does not appear to be imminent. What would be the most favourable outcome from a market standpoint?**

**A:** “A resolution is needed prior to August 2<sup>nd</sup>. Congress has already raised the debt ceiling 70 times over the last couple of decades, so this issue is not extraordinary. What has made this a big issue now is that politicians have noted that their fiscal house is not in order, and the Republican Party has taken this opportunity to point out that there is some real fiscal work to do in the United States.

“The challenge is not raising the debt ceiling in itself, but rather other problems that could potentially happen, such as an actual (but more likely technical) default on US debt. This has technically happened a couple of times in the past and there wasn’t much of a market reaction, but it has been 15 years or so since this occurred. The US is not as good a credit risk as it was– it has a lot more debt – and the fiscal situation is much worse than back then.

“The suspicion that a lot of people have is that even if the US was to technically default on its debt, the rest of the world would view it as a less worthy credit risk, and in line with this uncertainty would demand a higher interest rate from them. The US would be paying a higher interest rate as a country, and subsequently as individuals. That’s the big worry. There are a lot of knock on worries about the

impact of a default on the banking system and potential downgrades on US debt, all of which have very significant, potentially dire consequences. Both political parties know this, and we think that this will end up providing the motivation to solve this issue, before real problems are injected into the system.

**Q. There has been talk of a US credit rating downgrade - how likely is this to happen?**

A: "It's hard to say. Firstly, it's hard to say how much people listen to the credit rating agencies anymore. There has been a fair amount of criticism, much of it valid, at how the agencies handled the mortgage back debt problems that the US had a few years back. I think at some point if the US doesn't get its fiscal house in order they will adjust the credit rating. The US needs to figure out how to spend within its own needs and avoid that outcome. I don't think a ratings downgrade is imminent, but if the US does go beyond technically defaulting, which is incredibly unlikely, then it will be sooner rather than later.

**US Corporate Earnings**

**Q: Corporate earnings in the US have been good and you expect them to continue to be good. Google was a bright spot – so could good corporate earnings provide a much needed market distraction right now?**

A: "Macro events will play out as they will. They may be resolved painfully, politically, and grindingly, but we think they will get resolved. If this is the case it's very likely that earnings will be positive. Remember the market is up on a half year basis more than its average return. It has not been a bad year for equities, and I think that's because earnings have been good and people believe that earnings might matter. Google had a great number, JP Morgan had a good number and these are the two most significant names that have reported so far. These good strong earnings are a good sign for the quarter, probably not as strong as we've seen the last two years but still very good."

*For the full interview, please visit: <http://conversation.russell.com/2011/07/15/lowering-the-boom-on-raising-the-debt-ceiling/>*

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