



National Investment Fund for Credit Unions



Second Half 2009

Exploring Hope for the Economy

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National Investment Fund for Credit Unions (NIFCU\$)

PRESENTATION OUTLINE

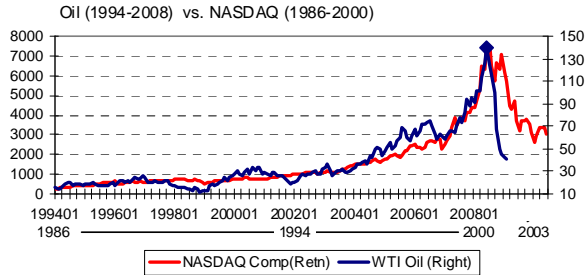
- How did we get here?
- Economic status report
 - consumers
 - investors
 - businesses
 - state & local governments
- Economic growth
- Employment
- Auto industry/ vehicle sales
- Housing market
- Inflation picture
- Federal Reserve policy
- Investment landscape
- Regulatory overview & potential consequences
- Wrap -up



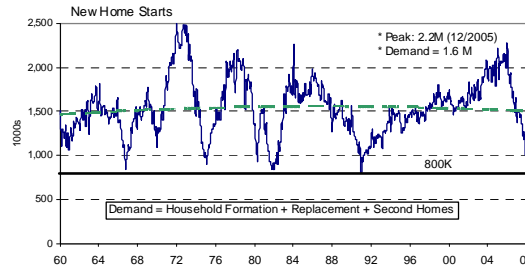
"I'm feeling phantom pain where my 401(k) used to be."

UNCOMMON FORCES CONSPIRED TO GET US HERE

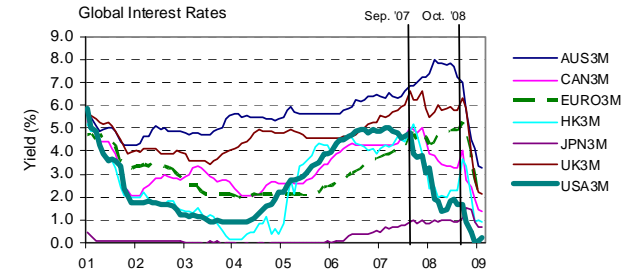
Oil/Commodity Prices



Housing Weakness



Inflation Targeting



Presidential Election
Geopolitical Concerns
Developing Economy Needs

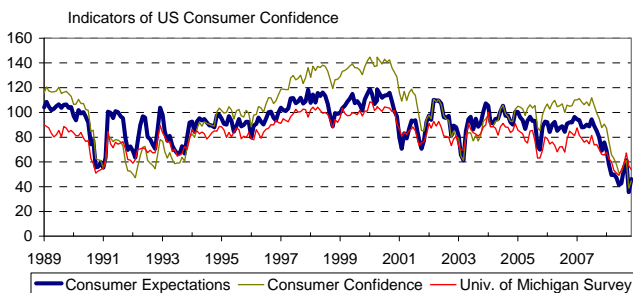
Credit Losses

FAS #157: Fair Value Accounting
Securitization/Leverage
Suspended Uptick Rule

Capital Markets

Market Liquidity
Exotic AB Securities
Hedge Funds
Credit Default Swaps

Confidence Suffering



Credit Crisis
Bank Capital &
Reserve
Requirements

Sequencing of Perfect Storm

1. Housing weakness—beginning 12/05
2. Timing of Fair Value Accounting rules—11/06
3. Suspending Uptick Rule—7/07
4. ABCP meltdown 7/07
5. Super-spike in oil prices to \$147—7/08
6. Lehman failure/Reserve Fund breaking \$
7. Central Banks constrained by inflation targets

ECONOMIC STATUS REPORT

- U.S. economy began contracting late last year, with the Global Financial Crisis accelerating in September 2008. Major impetus came from high oil prices and weakness in housing.
- Declining oil prices in 2H2008 equated to \$350 B tax cut (\$700B vs. \$147 WTI). On the rise once again.
- Consumers de-leveraging; impacted by evaporation of MEW, rising unemployment and modest wage growth. Savings rate now rising rapidly.
- Atypical global slowdown began with lean corporate inventories, low core inflation, stable interest rates, & minimal overcapacity. Industrial activity, investment and trade are key to 2009 growth.

Source: HighMark Capital Management estimates & Thomson Datastream

ECONOMIC STATUS REPORT continued

- Profit margins, productivity remain higher than expected, while inflation pressures are absent.
- Global economic growth being led by emerging economies. Increasing dependence on urbanization & industrialization should support new consumers. Exceptional worldwide monetary stimulus totaling a massive \$10 trillion plus interest rate cuts should reverse effect of credit squeeze.
- Secular disinflationary forces helping maintain operating efficiency, profit margins: hyper-competition, globalization, outsourcing, Internet price transparency, innovation and creativity.

GLOBAL STABILITY MEASURES NOW APPROACHING US\$10.0 TRILLION

Amount	<u>Worldwide Government Fiscal Measures, including U.S. Treasury Programs</u>
\$150 billion	Stimulus package:\$150 billion in rebates and tax incentives, doubled deficit
\$700 billion	TARP: \$700 Billion to recapitalize banks (some overlap with PPIF)
\$787 billion	2009 Economic Recovery Package (inc. \$200B FRE/FNM, \$75B loan mods)
\$600 billion	FHA, Freddie Mac & Fannie Mae increasing lending capacity, restructuring loans
\$586 billion ++plus	China's stimulus, Eurozone/UK stimulus, etc.
Bank Deposits Rising	FDIC Deposit Insurance increased from \$100K to 250K
	<u>Federal Reserve/U.S. Treasury</u>
\$900 billion	Global Interest rate cuts, coordinated policy now beginning October 2008
\$200 billion	Term Auction Facility (TAF) provides funds in exchange for bank assets
No Limit Set	Treasury Security Lending Facility (TSLF) exchanges assets from non-bank firms
\$1,000	Commercial Paper Funding Facilities (CPFF/AMLF) supports liquidity, exchange and new issuance
\$1,000	Term Asset-Backed Securities Loan Facility (TALF) lends for AAA purchases
	Public-Private Investment Program (PPIP)
	<u>Non-U.S. Actions</u>
Global	Coordinated interest rate cuts
\$341billion	European bank equity recapitalization in preferred shares
\$2,000 billion	Additional liquidity facilities, credit lines and asset guarantees
	<u>Other Measures</u>
	FASB clarification on FASB #157: Fair Value Accounting

SIGNIFICANT GLOBAL CUTS IN INTEREST RATES

Flirting with Zero

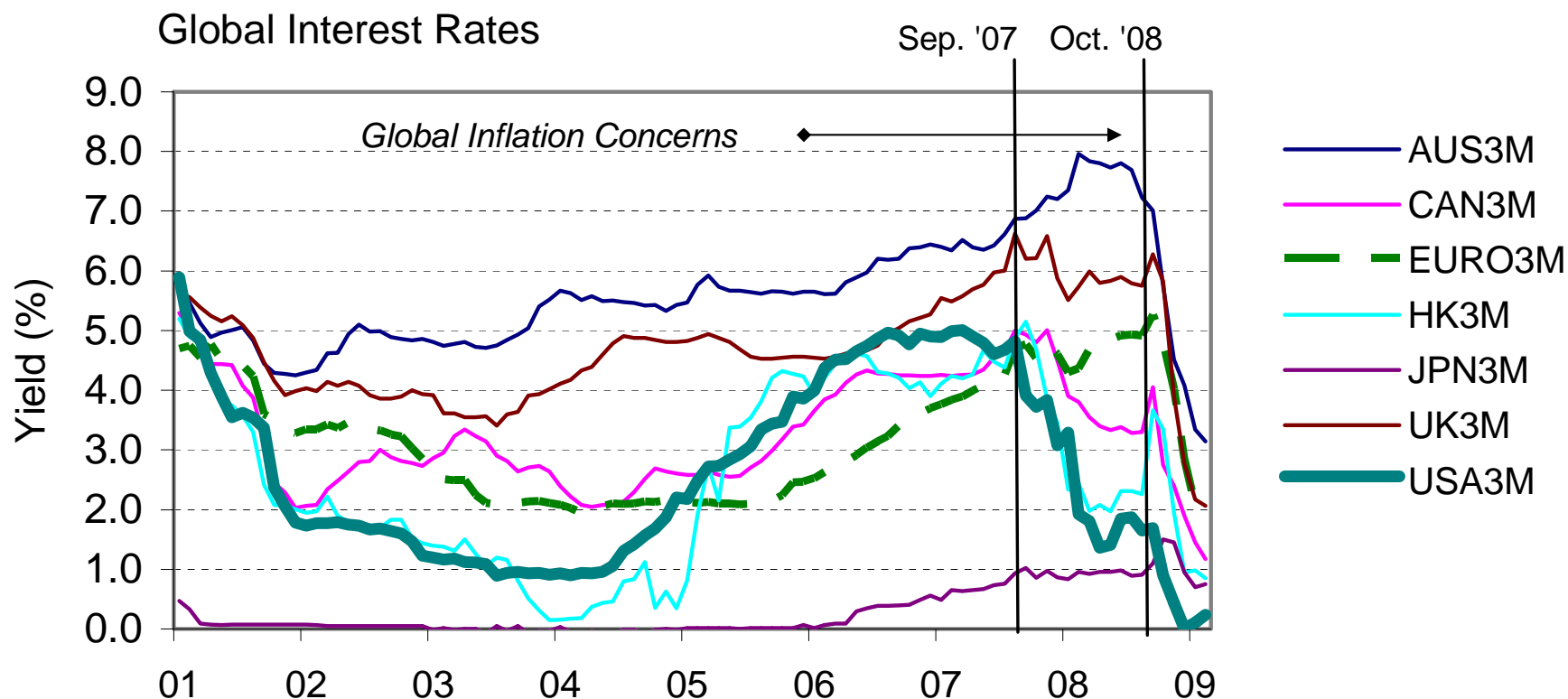
<u>Country</u>	<u>Peak Rate</u>	<u>Last Increase</u>	<u>First Cut</u>	<u>Current Rate</u>	<u>Latest Cut</u>	<u>Total Cut</u>	<u># Cuts</u>
U.S. Federal Reserve	5.25%	Jun-06	Sep-07	0.25%	-0.75%	-5.00%	7
Bank of Canada	4.50%	Jul-07	Oct-08	0.25%	-0.25%	-4.25%	10
Bank of England	5.75%	Jul-07	Dec-07	0.50%	-0.50%	-5.25%	9
European Central Bank	4.25%	Jul-08	Oct-08	1.00%	-0.25%	-3.25%	7
Riksbank (Sweden)	6.75%	Sep-08	Oct-08	0.50%	-0.50%	-6.25%	5
Bank of Switzerland	2.75%	Sep-07	Oct-08	0.25%	-0.25%	-2.50%	5
Bank of Japan	0.50%	Feb-07	Oct-08	0.10%	-0.15%	-0.40%	2
Reserve Bank of New Zealand	8.25%	Jul-07	Jul-08	2.50%	-0.50%	-5.75%	7
Reserve Bank of Australia	7.25%	Mar-08	Oct-08	3.00%	-0.25%	-4.25%	6
Reserve Bank of India	9.00%	Jul-08	Oct-08	4.75%	-0.25%	-4.25%	6
Bank of Korea	5.25%	Aug-08	Oct-08	2.00%	-0.50%	-3.25%	6
Bank of China	7.47%	Dec-07	Oct-08	5.31%	-0.27%	-2.16%	5
Hong Kong	6.75%	Mar-07	Sep-07	0.50%	-1.00%	-6.25%	7

***Bold** indicates tightening policy during financial crisis

Source: Compiled by HighMark Capital Management

GLOBAL INTEREST RATES

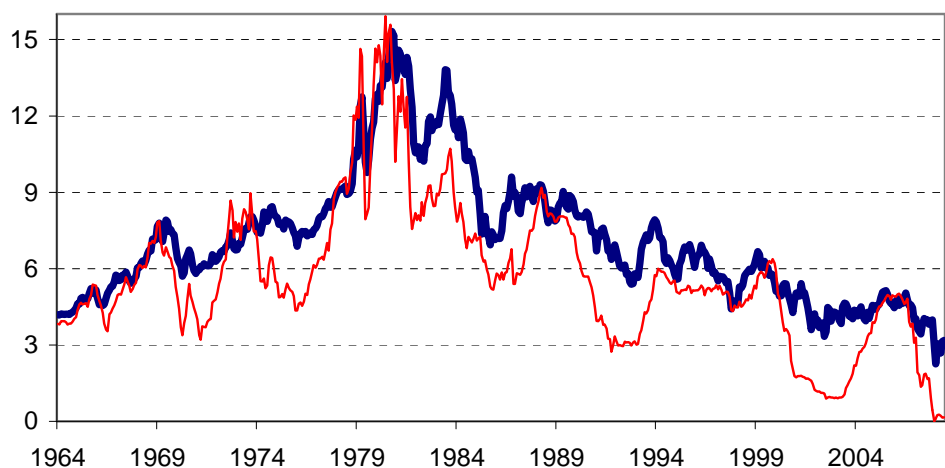
October 2008 was a significant inflection point for global interest rates, monetary stimulus



Source: HighMark Capital & Thomson Datastream

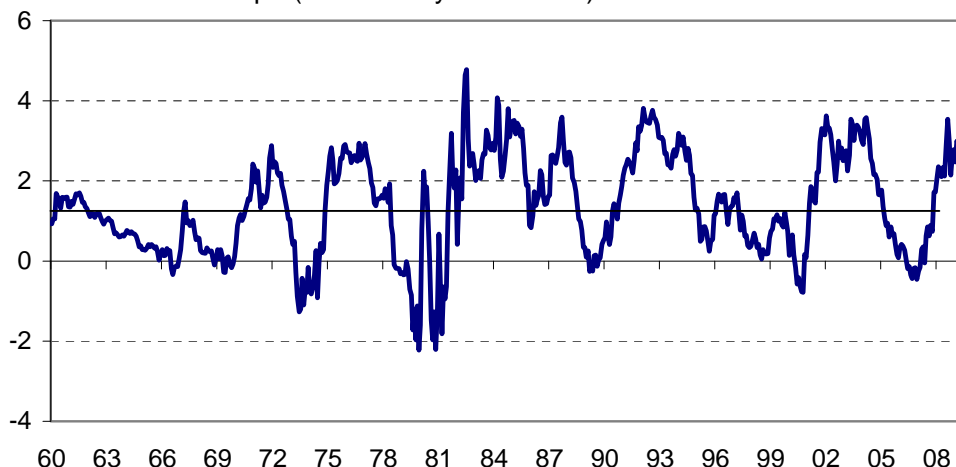
U.S. INTEREST RATES ARE NOW VERY LOW

US Interest Rates

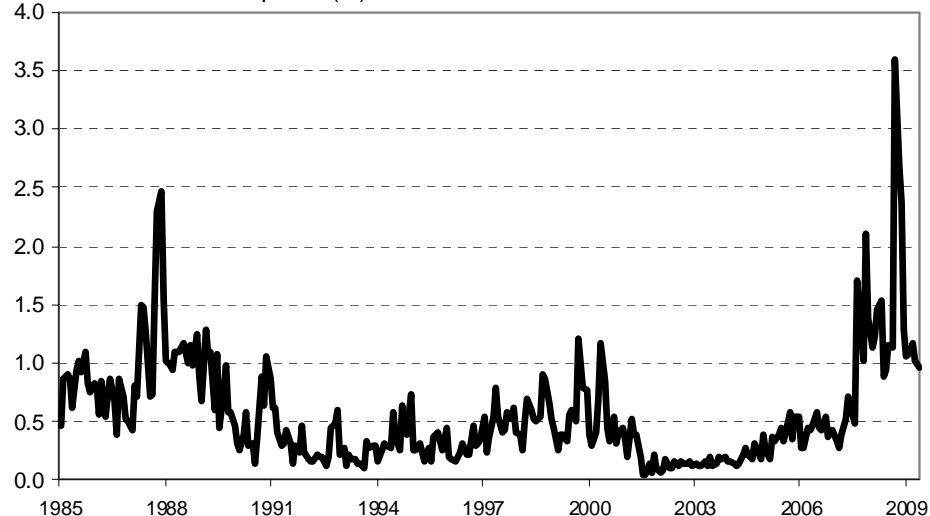


- *The yield curve has steepened which bolsters bank net interest margins*
- *Mortgage rates fell below 5% briefly in early May.*
- *TED spread still elevated, but starting to normalize.*
- *Global interest rates: ECB and BOE finally cut rates significantly.*

Yield Curve Slope (T-Bills - 10y Treasuries)

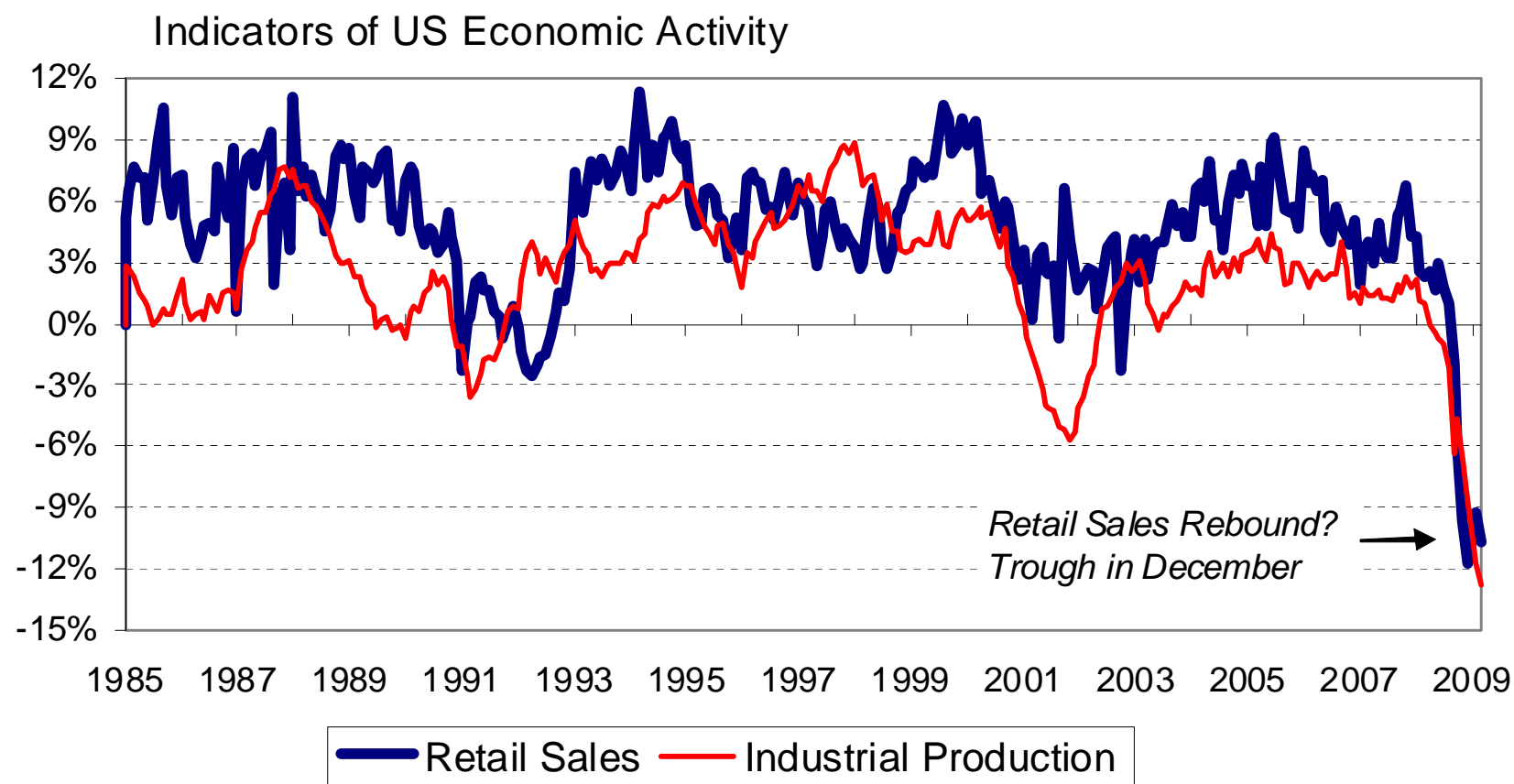


3m Euro - T-Bill Spread (%)



Source: HighMark Capital & Thomson Datastream

CONTRACTION BEGAN IN SEPTEMBER 2008 WITH CREDIT CRISIS



Source: HighMark Capital & Thomson Datastream

Unusual Factors

- Twin Hurricanes in Gulf of Mexico hit production
- Boeing Strike took est. 0.2% off GDP in 3rd Qtr
- Auto Industry shut-down Dec. 23rd – Feb. 2nd.
- Credit crisis seized up all financing

POLLING QUESTION

When do you think the U.S. economy will recover?

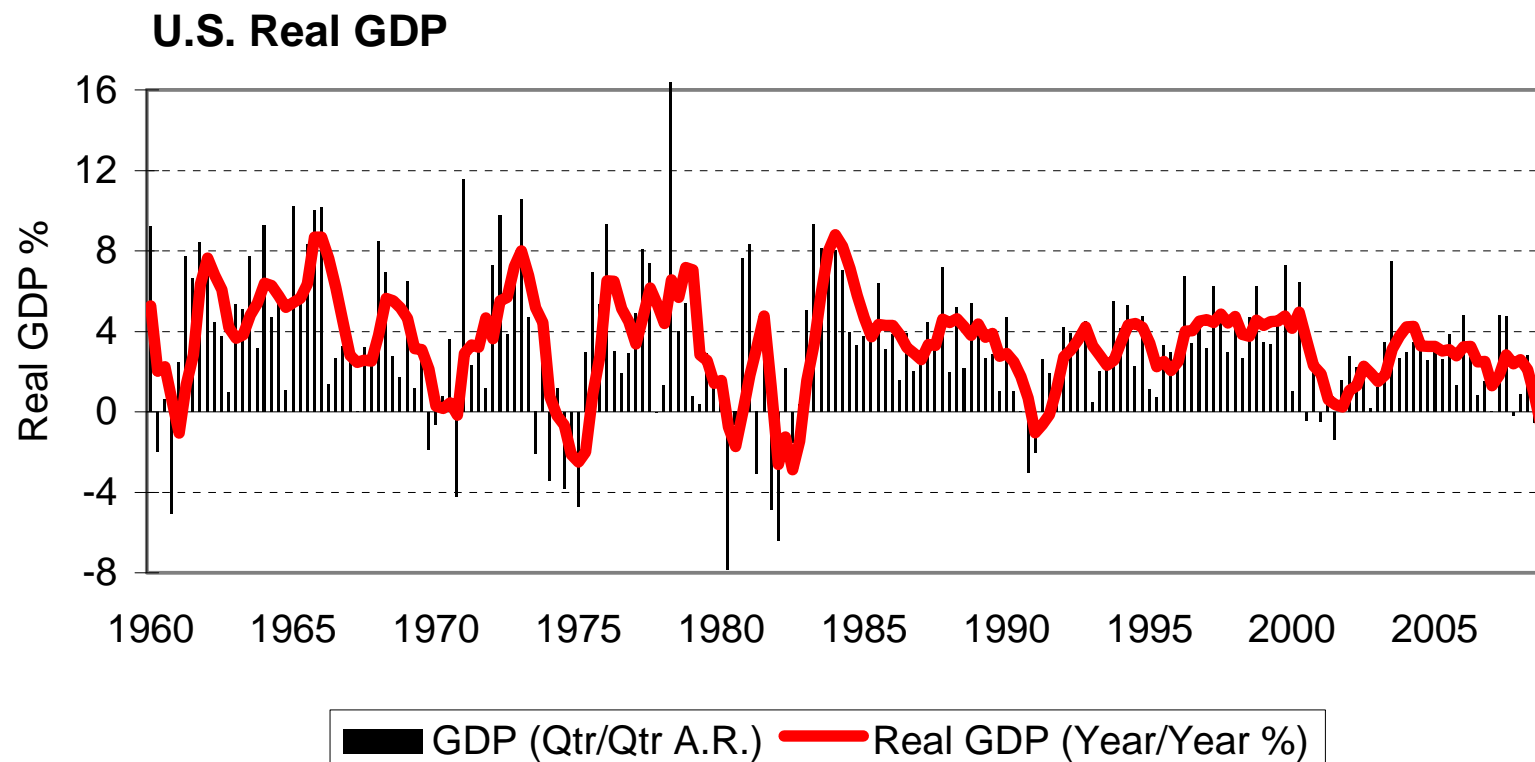
A. Later in 2009

B. First half of 2010

C. At a later date

U.S. GROSS DOMESTIC PRODUCT

Real GDP 1st Quarter: -5.7% A.R. following growth of +1.1% in 2008.



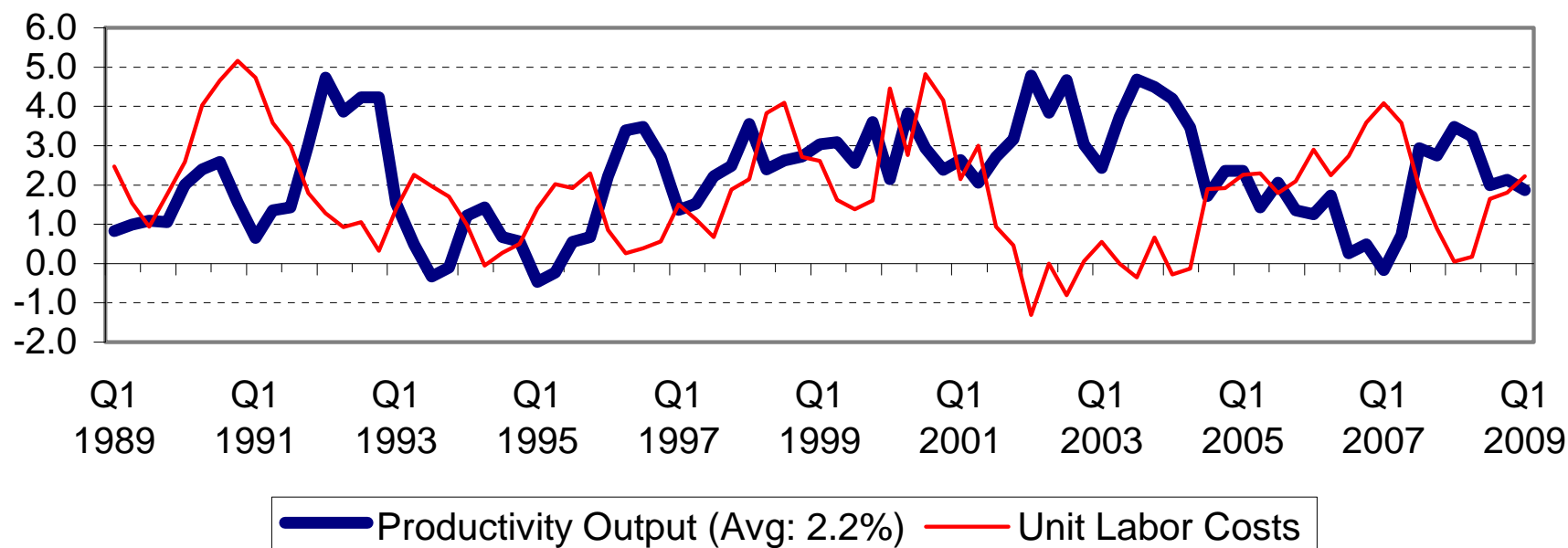
Note: 2001 Recession now revised away

Source: HighMark Capital and Thomson Datastream

PRODUCTIVITY

2008 2.7% Exceeds 2.2% Average. Similar to 2003, Profits Could Rebound Quickly

Productivity and Unit Labor Costs



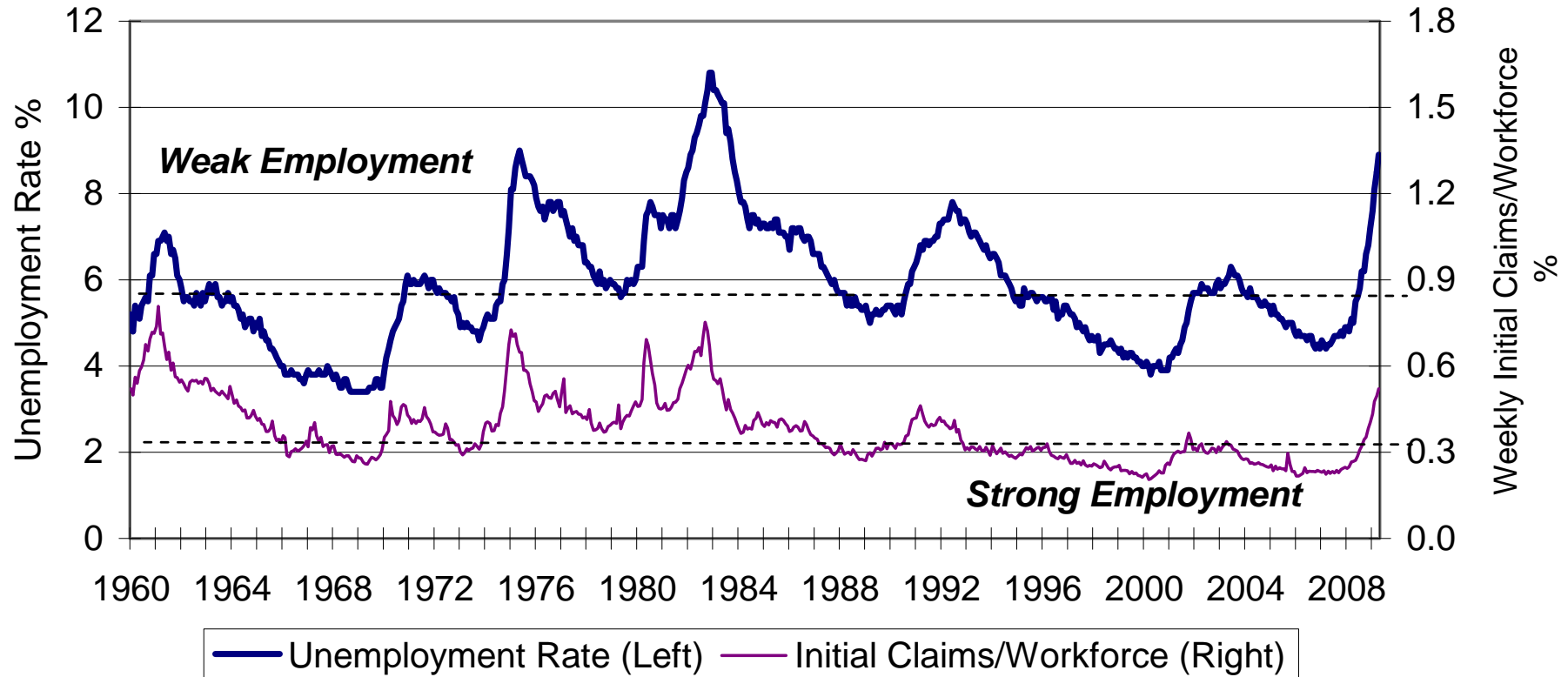
Source: HighMark Capital & Thomson Datastream

US UNEMPLOYMENT RISING

May Non-farm payrolls surprised: -345K vs. -550K expected.

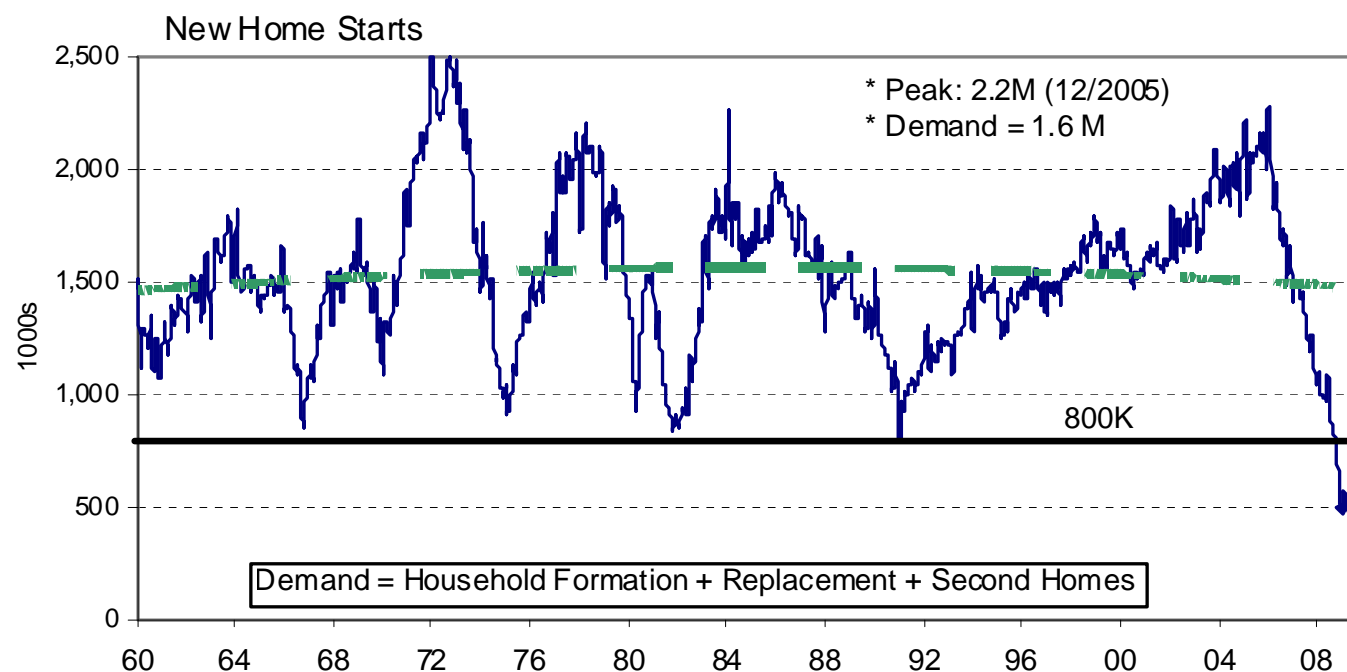
Workforce expansion of 1M in April to May period boosted jobless rate to 9.4%

US Employment



Source: HighMark Capital & Thomson Datastream

HOUSING MARKET AFFORDABILITY: BETTER RATES, PRICES, INVENTORY



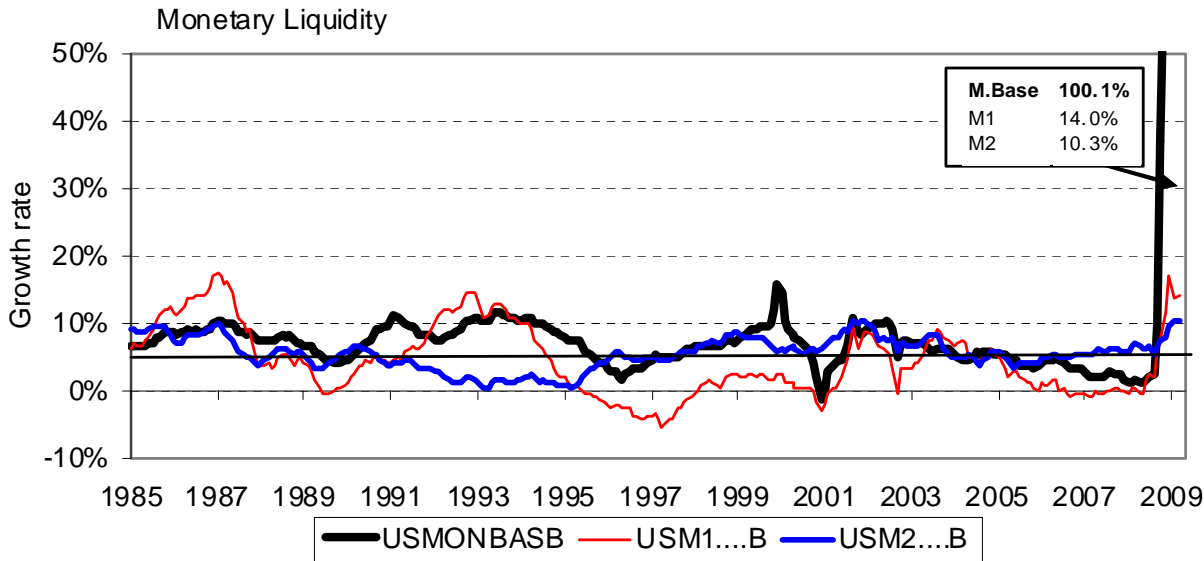
RECENT EVENTS IN PERSPECTIVE

- 90% of homes owned outright or carry a Fixed Rate Mortgage
- Residential construction starts: -77% off peak. Typically bottom ~1 million, not current 500K level (deficit building).
- Adjustable rate benchmarks are much lower. Some resets are driving down payments vs. CMT and other interest rate indices.
- Stability in home sales is a pre-requisite for prices to bottom.
- Prices now -22% off 2006 peak.
- Supply at about 9.6 months versus 9.7 at start of 2009. Average is 5 months.

Source: HighMark Capital, Federal Reserve, NAR & Thomson Datastream

MONETARY POLICY: WATCHING THE MONETARY BASE

Federal Reserve has added a lot of liquidity. Cash on sidelines at record level.



Source: HighMark Capital & Thomson Datastream

**Money Market Mutual Fund Assets
June 17, 2009**

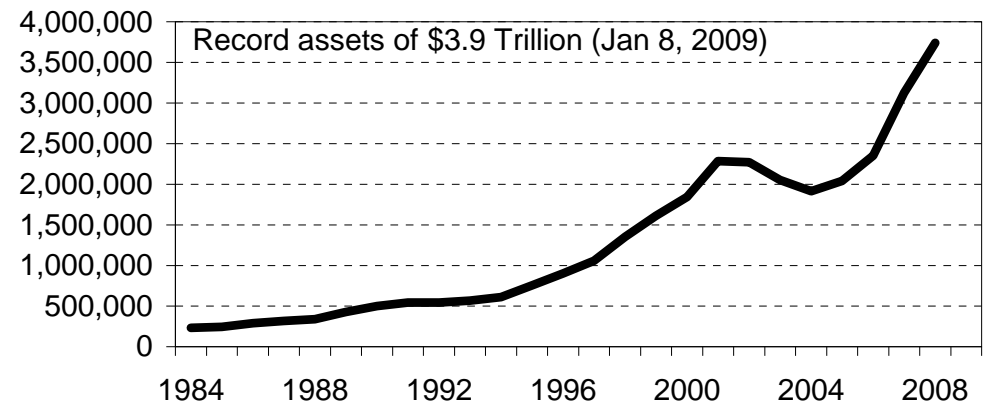
\$3,675,000,000,000

Household Bank Deposits:

\$8,000,000,000,000 (est.)

---ICI, Federal Reserve Flow of Funds

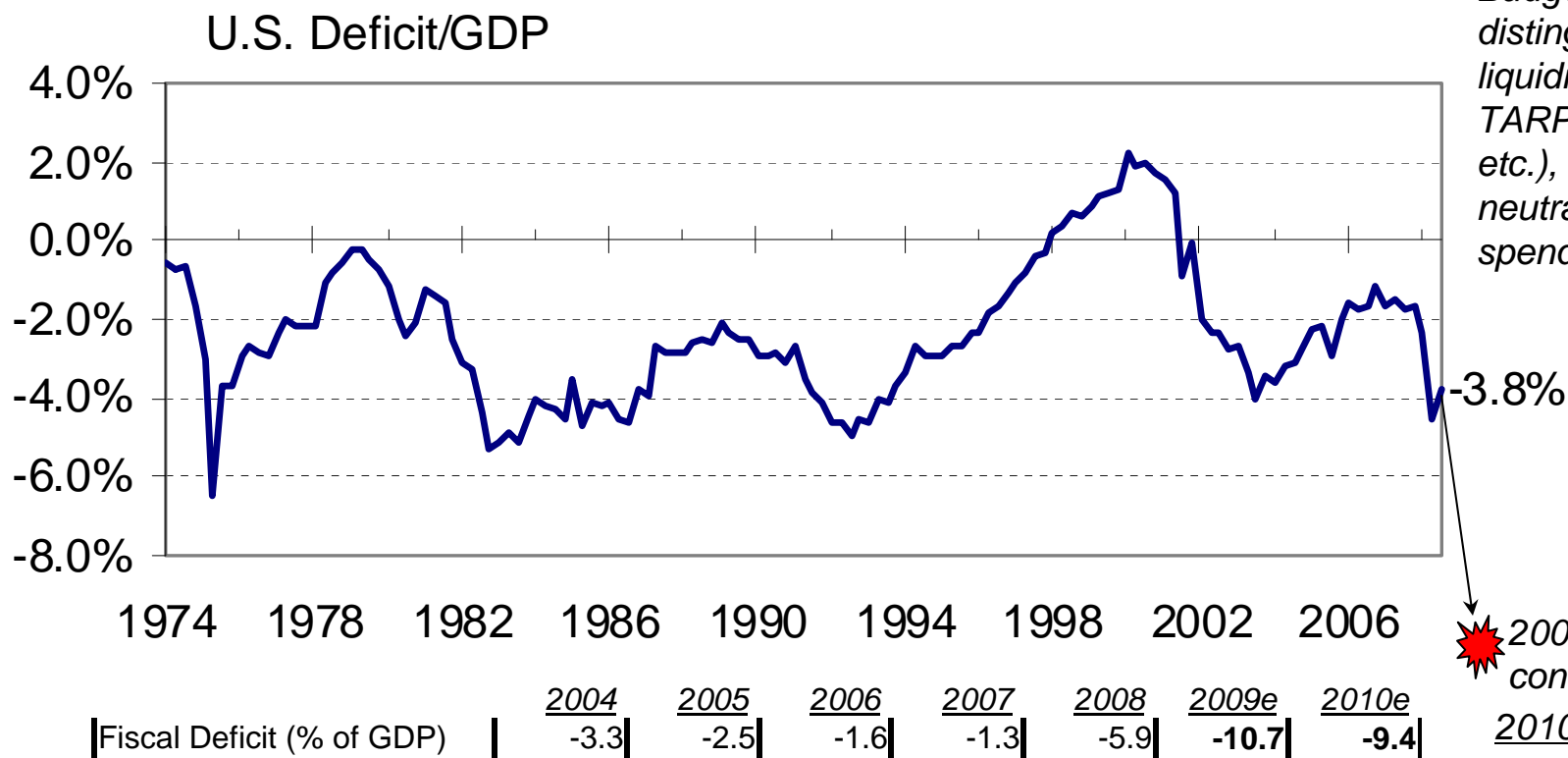
Money Mkt Fund Assets (\$MM)



Source: ICI Databook

AMERICA AT A CROSSROADS: U.S. FEDERAL DEFICIT

Important to differentiate net deficit impact of each of the various programs



Budget deficit tracking distinguishes between liquidity /guarantees (i.e., TARP, TALF, TAF, TSFL, etc.), which are deficit neutral and government spending programs

Source: HighMark Capital, Thomson Datastream and Bloomberg Consensus Estimates

American Recovery and Reinvestment Act of 2009: **\$790 Billion** over 10 years
 \$282 B (36%) in tax relief, \$315 B (40%) spending, plus entitlement benefits

Source: HighMark Capital & Thomson Datastream

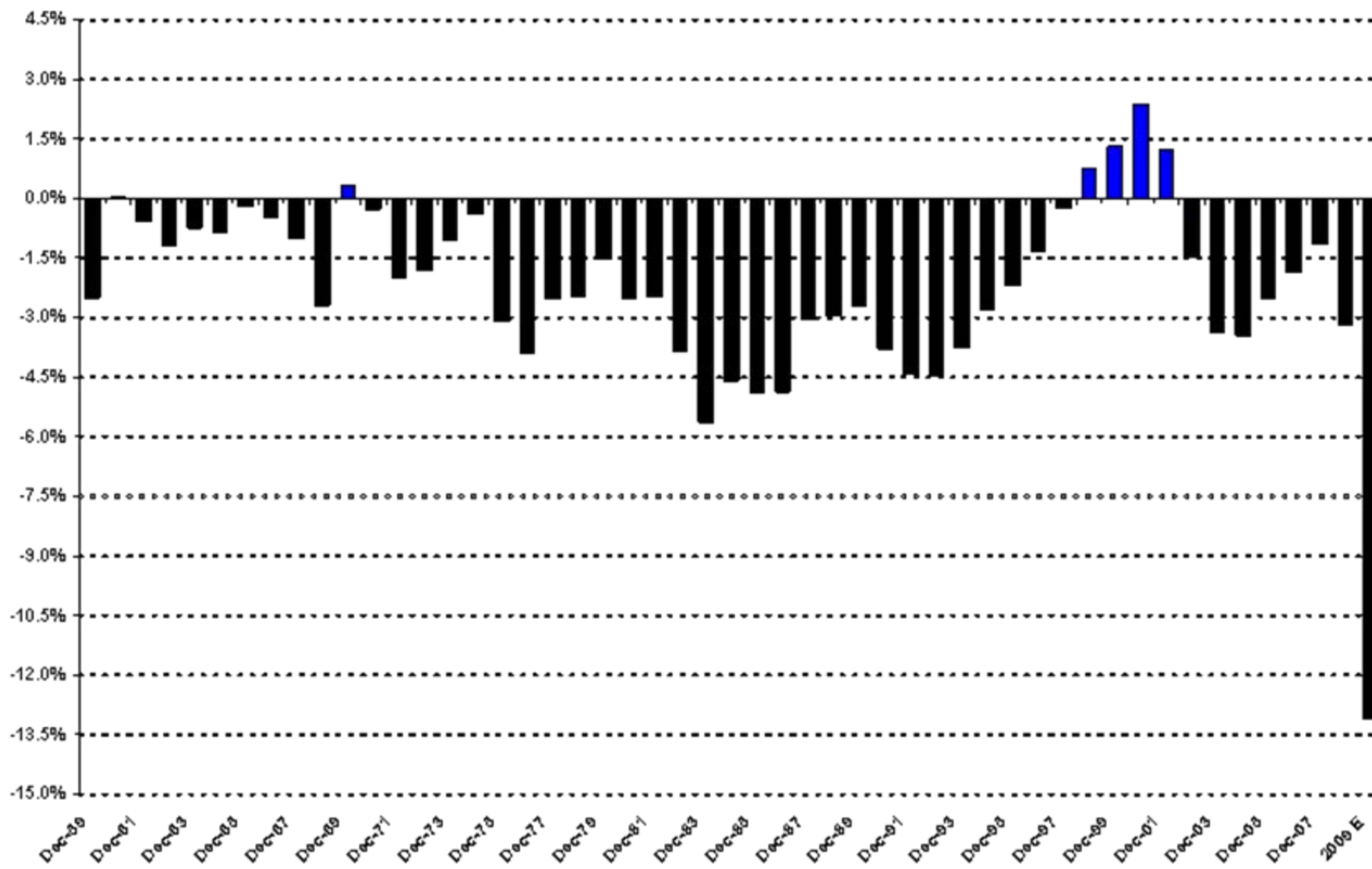
POLLING QUESTION

How concerned are you about the rising national debt & potential for significantly higher tax rates in the next few years?

- A. Very concerned
- B. Somewhat concerned
- C. Not concerned at all

CBO SCORING OF BUDGET SUGGESTS 13.1% DEFICIT

**Federal Budget Deficit
% of GDP**



HIGHMARK'S OUTLOOK

Key Concerns: continued Housing Weakness & rising Oil Prices

Economic Environment

- US\$10 Trillion of global stimulus, plus interest rate cuts
- U.S. real growth should trough later this year.
- Low inflation given commodity price declines.
- Plunge in oil prices in 2H 2008 is now being reversed. Was a \$700 Billion tax cut from high of \$147 WTI to low of \$42 per barrel.
- Housing weakness: Affordability improving with lower rates, inventory declining.
- Commercial real estate, now declining, will act as a drag.
- Business and Consumer: Coiled spring of deferred demand needs trigger/catalyst.
- Developing countries increasingly dependent on infrastructure development.
- Urbanization & Industrialization = jobs + credit access → insatiable consumption.
- Risk that credit crisis persists and confidence is slow to recover.

HIGHMARK'S OUTLOOK continued

Key Concerns: continued Housing Weakness & rising Oil Prices

Interest Rates

- Interest rates low with plenty of monetary stimulus globally.
- Europe and UK following Fed lower: Coordinated moves since October 2008.
- Treasuries expensive, despite huge supply, but credit risk premiums are compelling.
- Yield curves are finally steeper, which will bolster bank profitability.

Market Interrelationships

- US dollar devaluation improved competitiveness.
- Sentiment improving, but volatility still high - market psychology is key.
- Critical consequences of suspending uptick rule, strict interpretation of fair value.

A FEW SUGGESTIONS AFTER MANY LESSONS LEARNED

- Well-regulated markets can improve capital market efficiency and bolster investor confidence.
- Better regulatory enforcement, greater consistency, increased transparency needed most.
- Upgrade training of regulatory staff; require continuing education.
- New complex financial product innovations can spread quickly and slip through the cracks as regulators are often stretched to keep up. Consolidate banking and security regulators to minimize overlap, increase control, and close gaps in oversight.
- Derivatives registry (DTCC Deriv/SERV) can improve monitoring, but centralized clearing of swaps and other OTC derivatives may be needed.
- Expect increasing collateral requirements, and changes to repo clearing.
- Facilitate better access to investment tools, education, advice and guidance for individuals. Many new products can be confusing and have been misused or simply misrepresented.

WHAT YOU SHOULD BE FOCUSED ON

- Credit quality – cannot just rely on the rating agencies.
- Liquidity – this is where markets ran into problems in periods of stress.
- Diversification – not just in your investments, but in sources of liquidity.
- Due diligence – there is no substitute for truly understanding what you are buying. Even if you are using a short term investment vehicle/ sweep to manage your cash you need to know who the manager is, their tenure, philosophy on risk and track record.
- Regulation alone, cannot keep you out of trouble. There will always be gray areas.

- **YOU CANNOT LEGISLATE COMMON SENSE**

BACK TO BASICS



"I don't know if we'll be rich again, but we may be thin again."

CONTACT INFORMATION

I can be reached at 415-705-7580.

As I work on a trading desk, it is possible that I may need to call you back.

I can also be reached via email at hillary.elder@uboc.com or through our client service line at (800) 634-6521.

Additional information regarding the National Investment Fund for Credit Unions (NIFCU\$) can be accessed at www.nifcus.com or through www.nafcu.org/nifcus

