

"When written in Chinese, the word 'crisis' is composed of two characters -- one represents danger and the other represents opportunity."

*--John F. Kennedy*

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# Negatives Outweighing Positives

MOST SEVERE RECESSION SINCE GREAT DEPRESSION

## Negatives

- Global Recession
- Credit Crisis
- Housing Crisis
- Confidence Crisis
- Deflation
- Deleveraging
- Protectionism

## Positives

- Monetary Stimulus
- Fiscal Stimulus (?)
- Sentiment
- Cash Mountain
- Low Commodity Prices
- Toxic Assets Plan (?)

# An Era of Bubbles

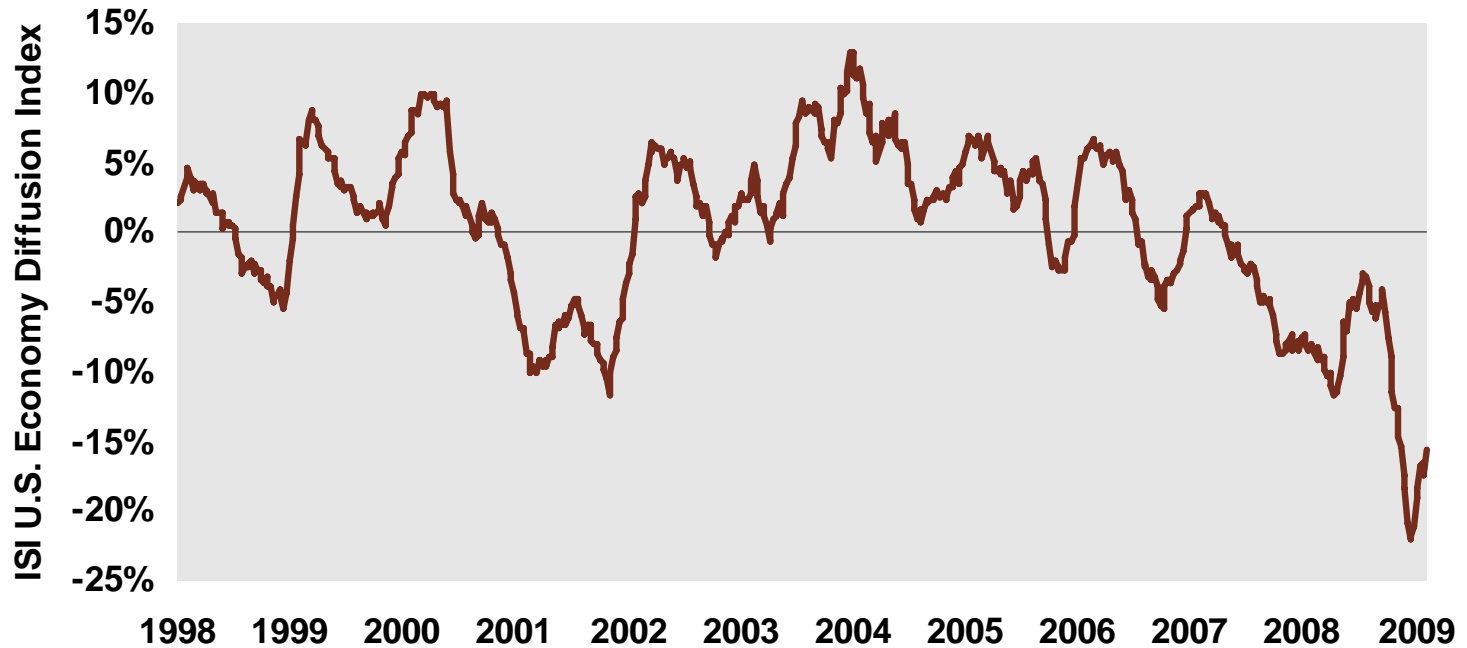
POLICY/OVERSIGHT MORE PROACTIVE IN FUTURE?



# RECESSION/FINANCIAL CRISIS

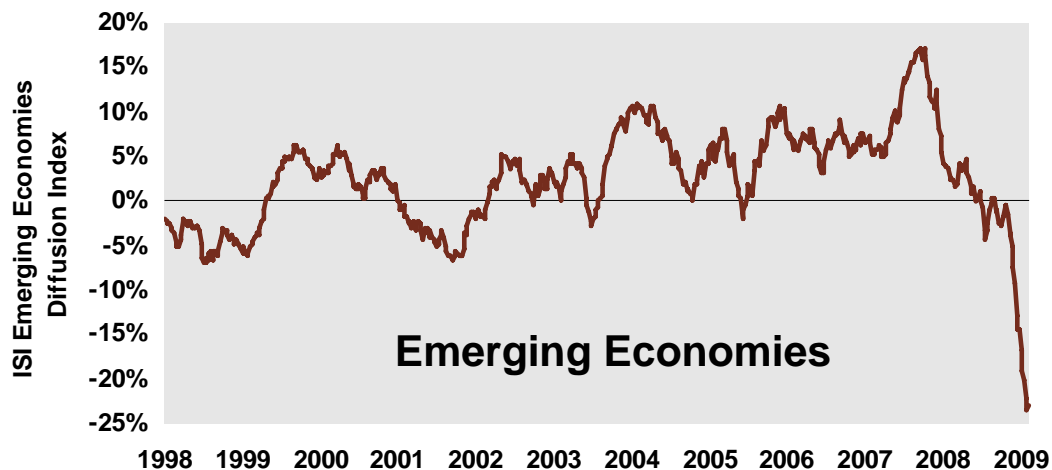
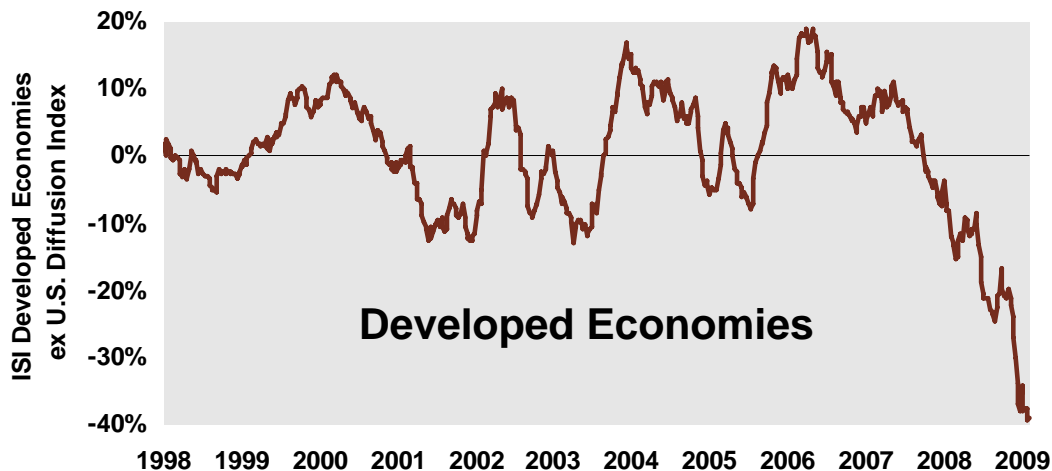
# U.S. Economy Tanked First

COULD LEAD GLOBAL ECONOMY OUT OF RECESSION



# International Economies Imploding

NO ECONOMY IS UNSCATHED ... EVEN CHINA



# U.S. Recession Began Last December

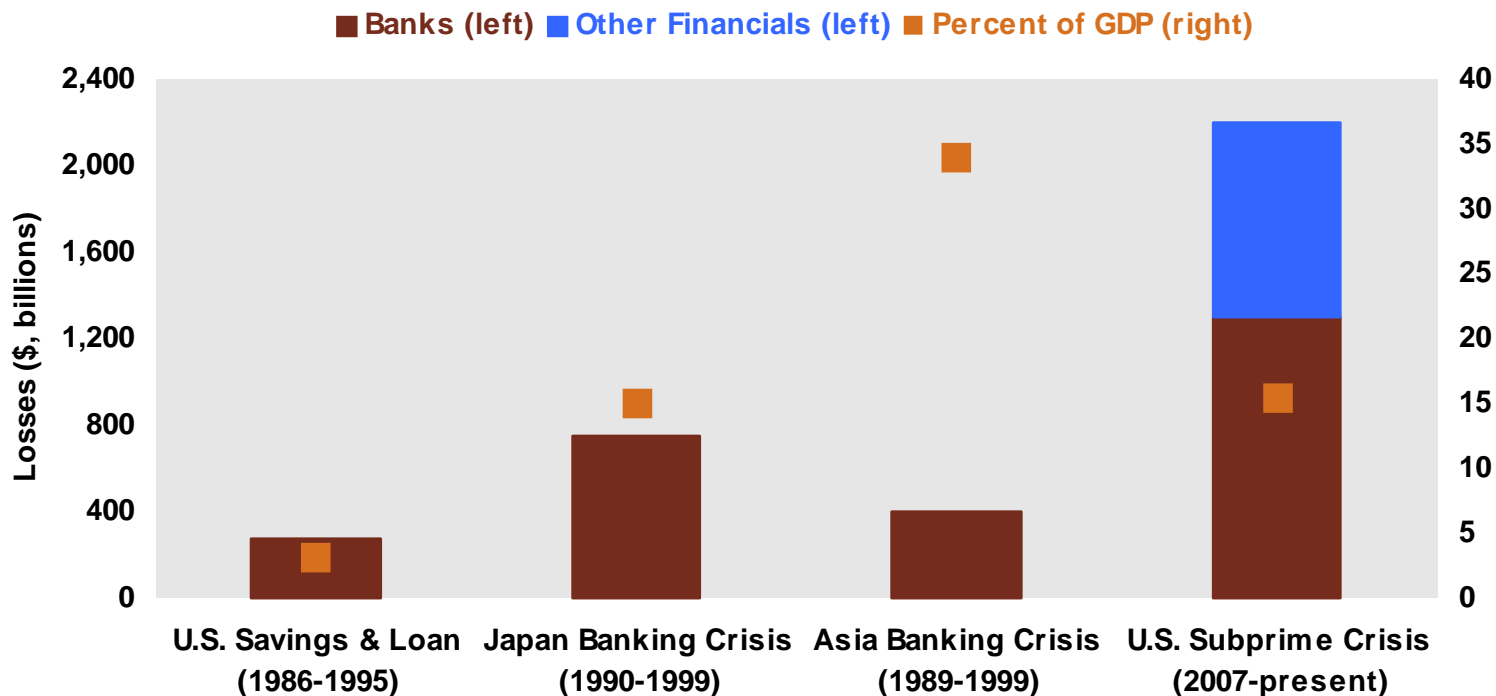
## WHAT IS THE STOCK MARKET TELLING US?

Recession Dates	Bear Market/Correction	Bear Market/Correction Dates	Peak Unemployment Rate (Month/Year)	Months After Recession End
8/29-3/33**	-86%	9/29-6/32	NA	NA
5/37-6/38	-55%	3/37-3/38	NA	NA
2/45-10/45	NA	NA	NA	NA
11/48-10/49	-21%	6/48-6/49	7.9% (10/49)	0
7/53-5/54	-15%	1/53-9/53	6.1% (9/54)	4
8/57-4/58	-22%	8/56-10/57	7.5% (7/58)	3
4/60-2/61	-14%	8/59-10/60	7.1% (5/61)	3
12/69-11/70	-36%	11/68-5/70	6.1% (8/71)	9
11/73-3/75	-48%	1/73-10/74	9.0% (5/75)	2
1/80-7/80	-17%	2/80-3/80	7.8% (7/80)	0
7/81-11/82	-27%	11/80-8/82	10.8% (12/82)	1
7/90-3/91	-20%	7/90-10/90	7.8% (6/92)	15
3/01-11/01**	-49%	3/00-10/02	6.3% (6/03)	19
<b>Average</b>	<b>-34%</b>		<b>7.6%</b>	<b>6</b>
12/07-?	-52%	10/07-11/08*	7.6% (1/09)***	?

\*Thru 11/20/08 low. \*\*Multiple bear markets occurred in date range. \*\*\*Current rate. Bear market (in red) = 20% or more drop in S&P 500. Correction (in blue) = 10%-20% drop in S&P 500. Bear market/correction occurred anytime 1-year prior to recession start through 1-year following recession end. See last slide for description of recession. Source: Bloomberg, National Bureau of Economic Research (NBER), Ned Davis Research, Inc.

# This Financial Crisis is a \$ Doozy

## HITTING NON-BANKS AS WELL



**Other Financials = GSEs, Hedge Funds, Pension Funds/Savings Institutions and Insurance Companies**

7 U.S. subprime costs represent staff estimates of losses on banks and other financial institutions. All costs are in real 2007 dollars. Asia includes Indonesia, Korea, the Philippines, and Thailand. Source: IMF's (International Monetary Fund) Global Financial Stability Reports (April 2008 and January 2009). See [www.imf.org](http://www.imf.org) for more information.

# Policy Actions by Federal Reserve

Action	Funding (\$, billions)	
	Committed to Date	Potential
▪ Reductions in interest rates	NA	NA
▪ Primary and secondary credit programs	94	Unknown
▪ Term Auction Facility	450	600
▪ Takeover of Bear Stearns	29	29
▪ Support for AIG	83	113
▪ Commercial Paper Funding Facility	334	1,800
▪ Money Market Investor Funding Facility	0	540
▪ Asset-Backed Commercial Paper Money Market Mutual Fund Liquidity Facility	24	Unknown
▪ Term Securities Lending Facility and TSLF options	172	200
▪ Primary Dealer Credit Facility	37	Unknown
▪ Purchases of government-sponsored enterprises (GSE) debt	15	100
▪ Purchase of mortgage-backed securities (MBS)	0	500
▪ Term Asset-Backed Securities Loan Facility	0	200
▪ Assistance to Citigroup	0	234
▪ Currency swaps	> 500	Unlimited

# Policy Actions by Treasury

Action	Disbursements (\$, billions)	
	Committed to Date	Potential
▪ Troubled Asset Relief Program (TARP)	247	700
▪ Housing-related tax provisions	0	12
▪ Purchases of obligations and securities issued by Fannie Mae and Freddie Mac	71	Unlimited
▪ Conservatorship for Fannie Mae and Freddie Mac	14	200
▪ Temporary Guarantee Program for Money Market Funds	Unknown	3,000
▪ Supplemental Financing Program	259	Unlimited

# Policy Actions by Other Agencies

Action	Disbursements (\$, billions)	
	Committed to Date	Potential
<b>Federal Deposit Insurance Corporation (FDIC)</b>		
▪ Temporarily raised basic limit on insurance coverage from \$100,000 to \$250,00 per depositor	NA	700
▪ Temporary Liquidity Guarantee Program	NA	1,450
▪ Assistance to Citigroup	0	10
<b>Department of Housing and Urban Development (HUD)</b>		
▪ Redevelopment of abandoned and foreclosed homes	0	4
▪ HOPE for Homeowners Program	0	1
▪ FHA Secure	NA	1
<b>Federal Housing Finance Agency (FHFA)</b>		
▪ Conservatorship for Fannie Mae and Freddie Mac	NA	NA
▪ Streamlined Modification Program	Unknown	Unknown
<b>National Credit Union Administration (NCUA)</b>		
▪ Credit Union Homeowners Affordability Relief Program and Credit Union System Investment Program	0	41
▪ Temporary Corporate Credit Union Liquidity Guarantee Program	1	Unknown

# Fiscal Stimulus Coming (& Growing)

## IS IT ENOUGH / PROPERLY STRUCTURED?

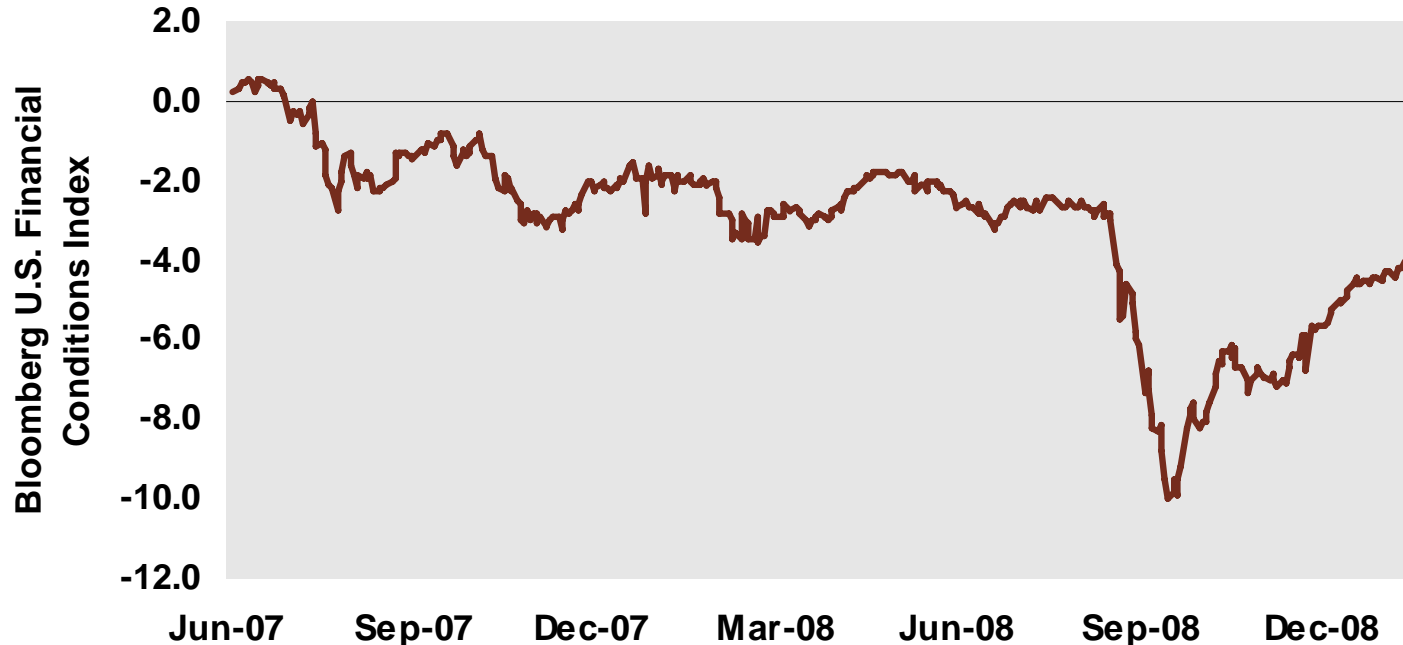
Proposed \$825 Billion** House Stimulus Package	\$, billions*
▪ Tax cuts for individuals and business	275
▪ Aid to states for health care and other essentials	119
▪ Education	117
▪ Aid for unemployed and the needy	106
▪ Infrastructure	90
▪ Energy investments	54
▪ Investments in science and technology	16
▪ Other (may include small-scale investments in categories above)	48

**\* Senate version includes additional \$69b AMT patch**

Estimated Disbursement Schedule of Proposed Stimulus Package
▪ \$170b – end of September (fiscal 2009)
▪ \$356b – fiscal 2010
▪ \$174b – fiscal 2011
▪ \$125b – fiscal 2012 and beyond

# Financial Crisis Index Starting to Recover

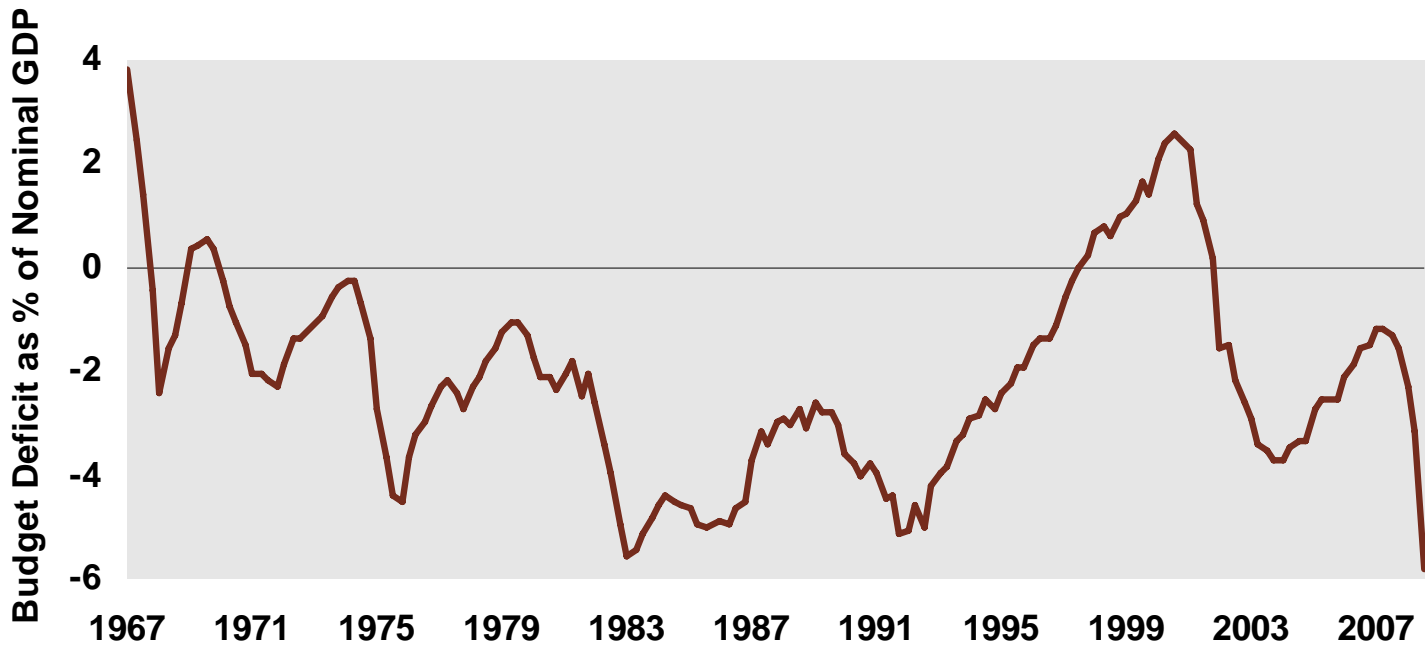
BUT LONGER-TERM SPREADS REMAIN UNCOMFORTABLY ELEVATED



**The BFCI combines yield spreads and indices from the short-term debt markets, equity markets and bond markets into a single normalized index.**

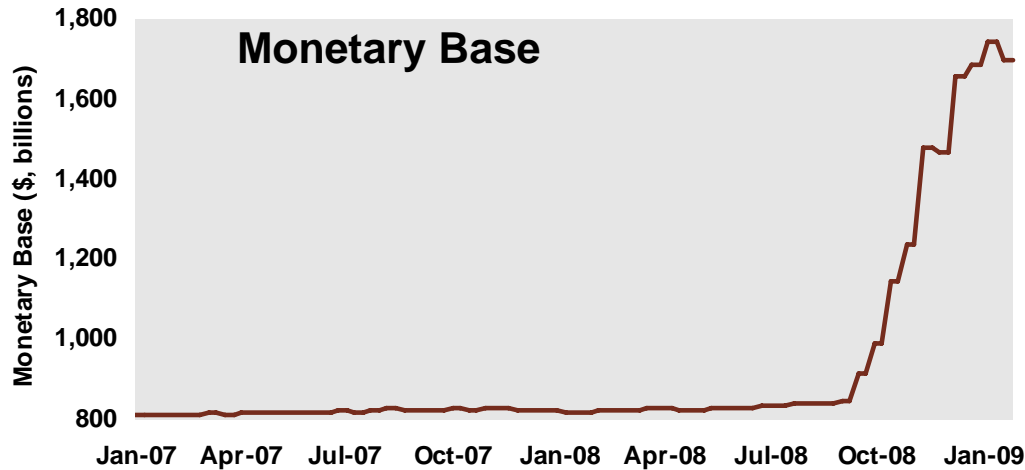
# Budget Deficit To Worsen Significantly

A NECESSARY EVIL TO STABILIZE THE ECONOMY?

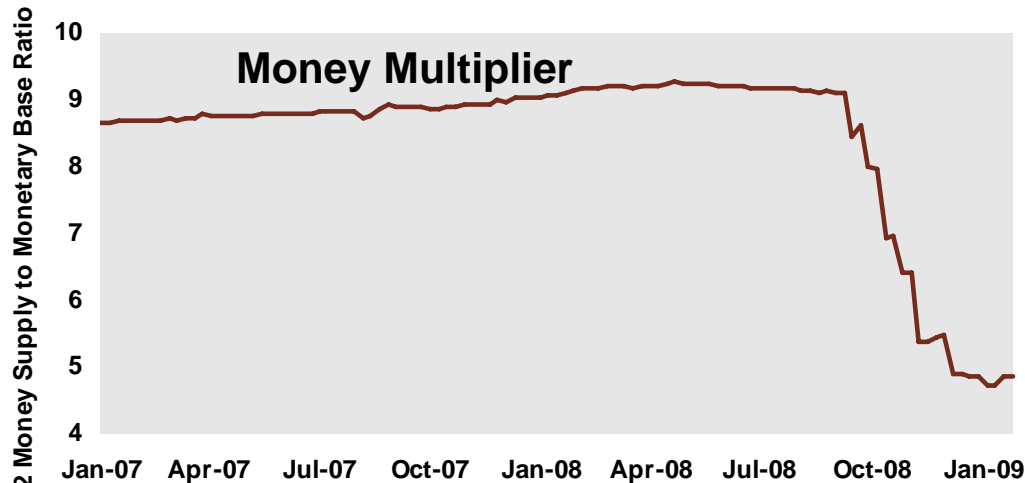


# Monetary Base Explodes

BUT PLUNGING "MONEY MULTIPLIER" IS NOT INFLATIONARY



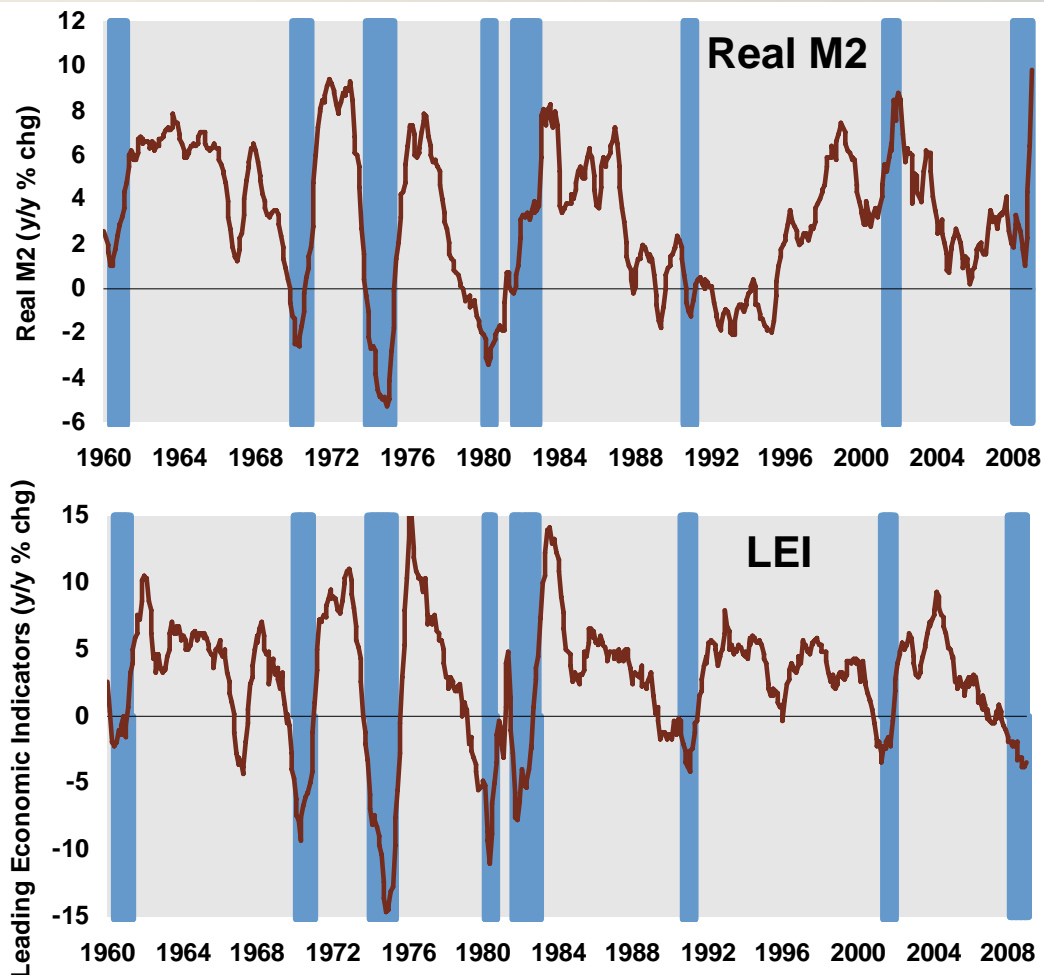
**Fed boosting  
banking reserves**



**But money isn't  
getting into  
economy**

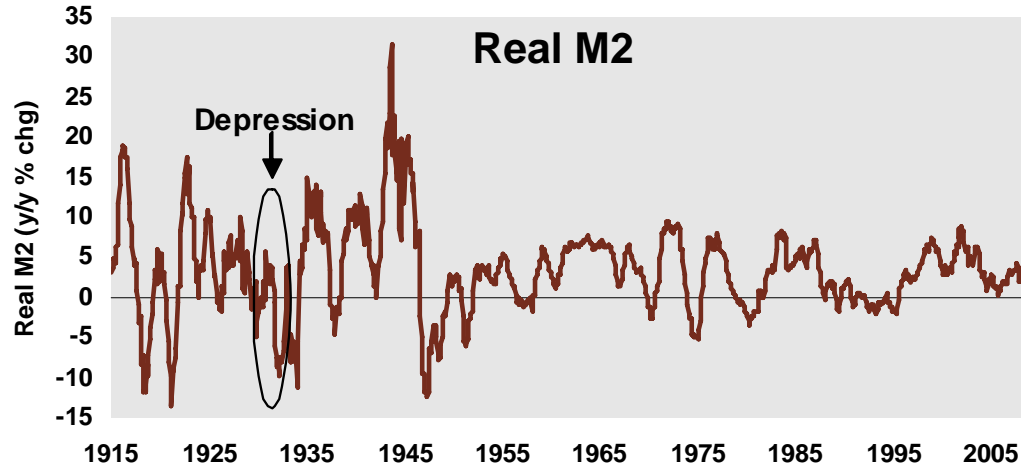
# Money Supply Growth on a Tear

HELPED TURN LEADING INDICATORS UP EVER SO SLIGHTLY

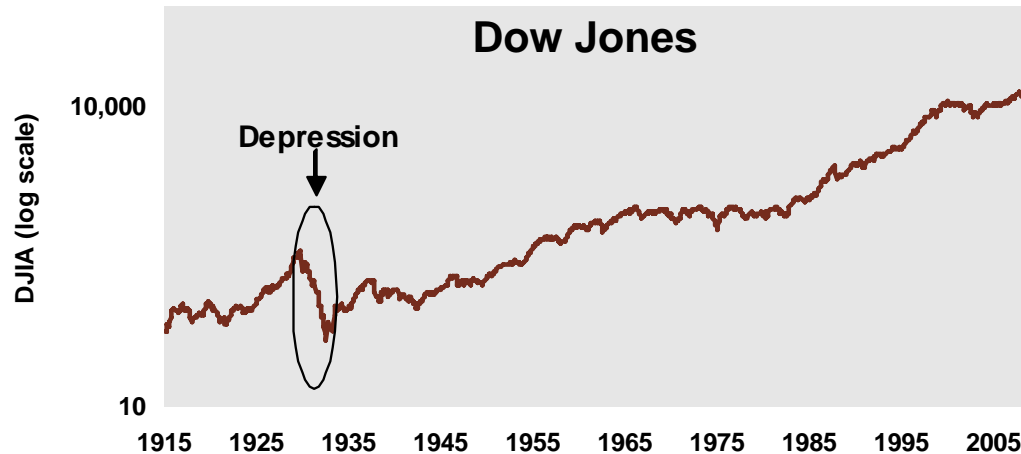


# Tremendous Excess Liquidity in System

SHARP CONTRAST TO DEPRESSION ERA'S CONTRACTING LIQUIDITY

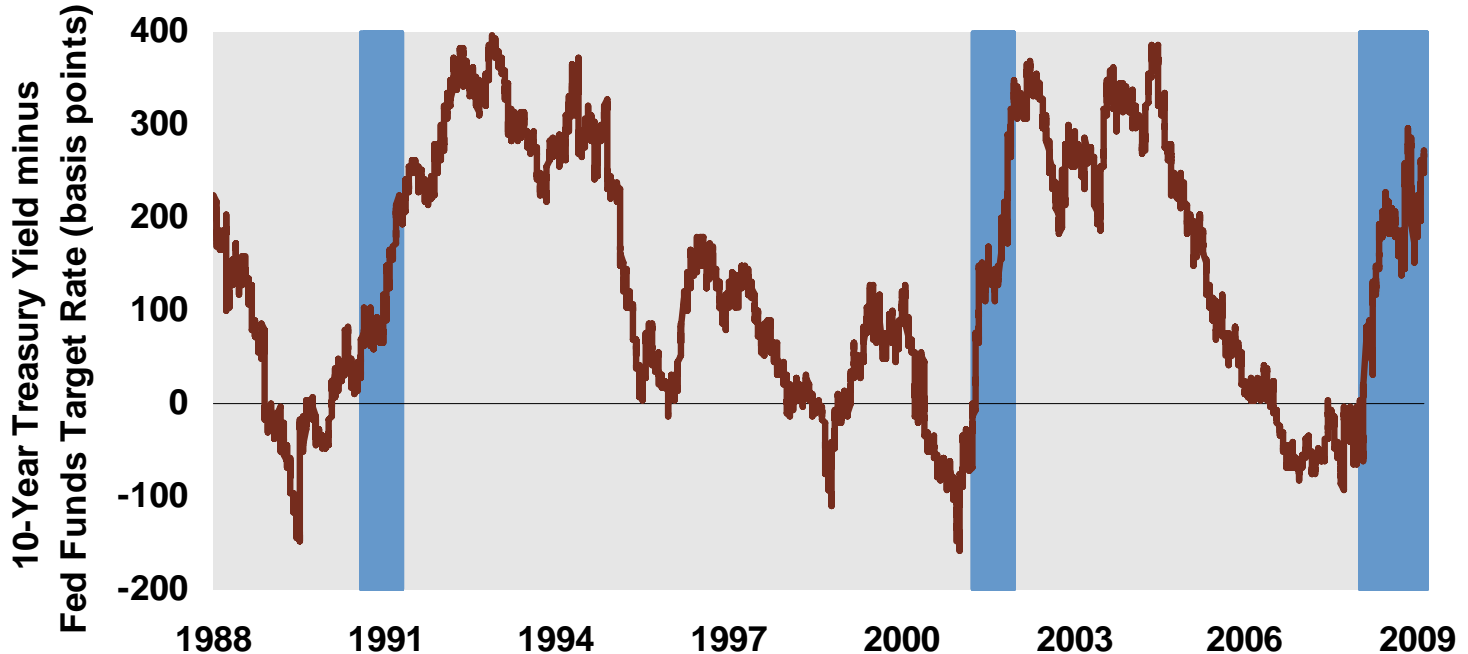


1/31/1915-12/31/2008		
When Real M2 Growth is:	DJIA Gain	% of Time
> 4.76	10.6%	36.3
1.18 – 4.76	6.0%	32.5
< 1.18	-0.6%	31.2



# Yield Curve Now Forecasting Recovery

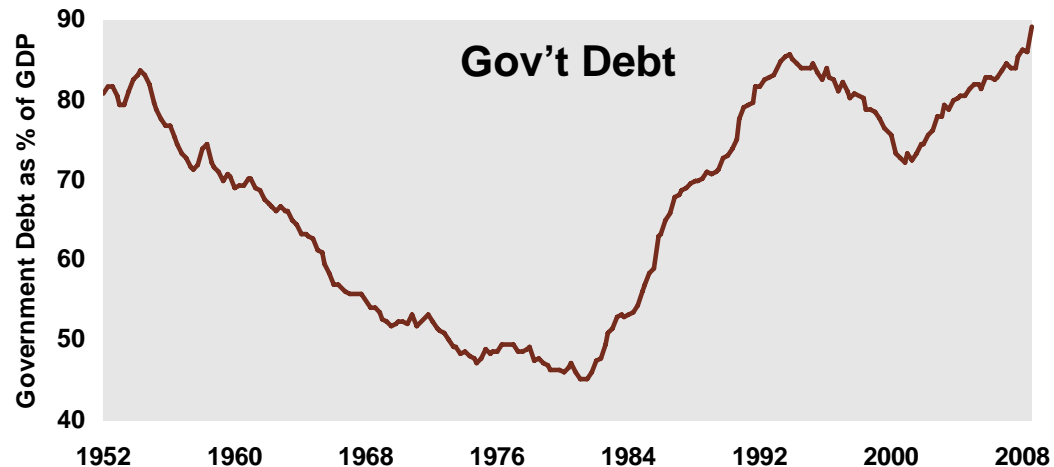
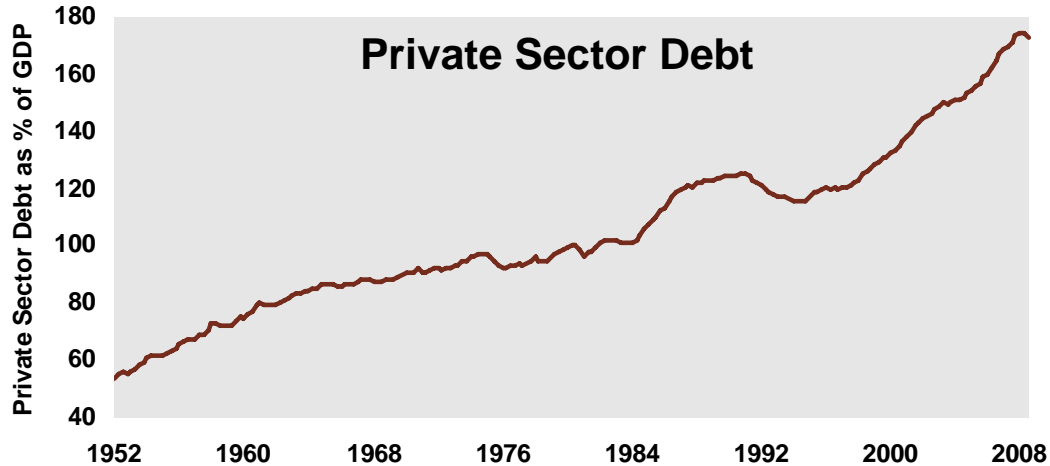
ACCURATELY FORECASTED RECESSION



# HOUSING/CREDIT CRUNCH/CONSUMER

# Private Sector Debt Bubble Bursting

GOVERNMENT TO PICK UP SLACK



# Debt Became a Massive GDP-Driver

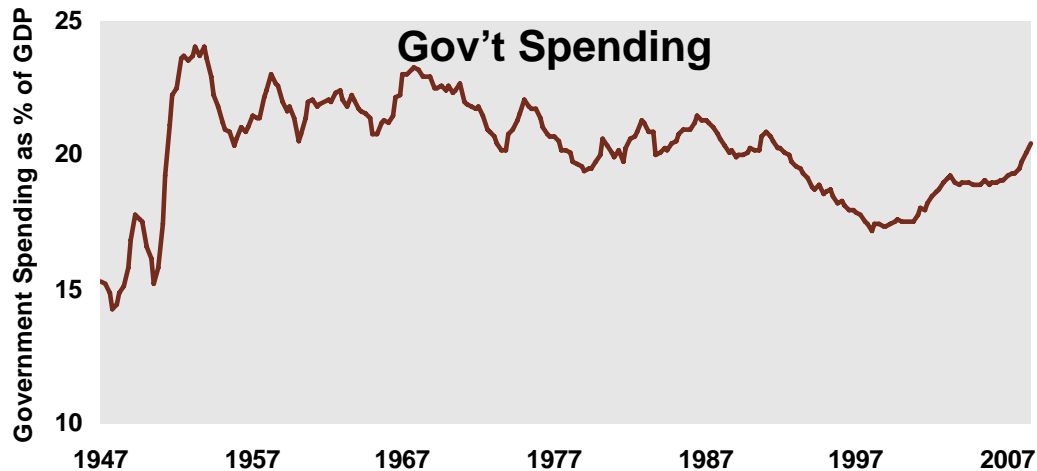
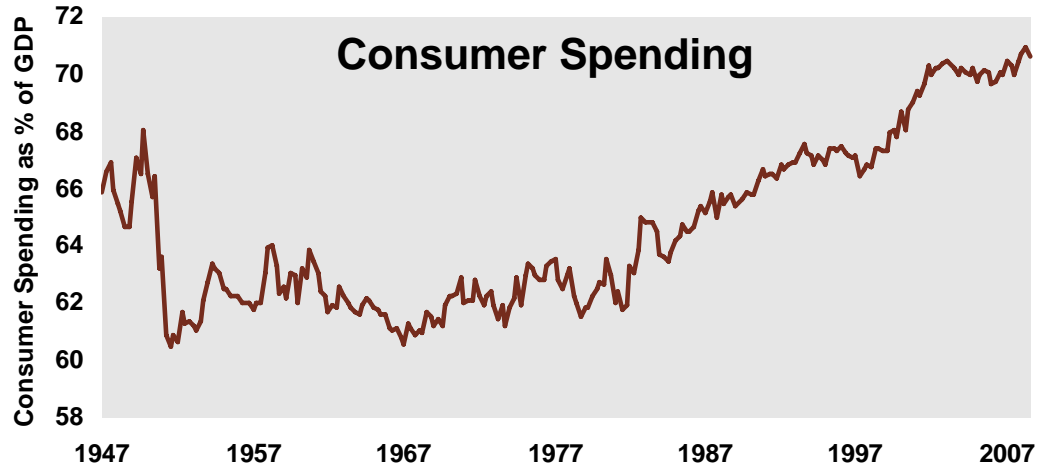
OVER \$5 OF DEBT TO PRODUCE \$1 OF GDP ... NOT SUSTAINABLE

## Diminishing Returns from Debt-Financing by Decade

Date Range	Decade Change in Debt (\$, billions)	Decade Change in GDP (\$, billions)	Debt/GDP
12/31/49-12/31/59	337.6	248.0	1.36
12/31/59-12/31/69	752.1	491.4	1.53
12/31/69-12/31/79	2,785.2	1,655.9	1.68
12/31/79-12/31/89	8,563.7	2,923.8	2.93
12/31/89-12/31/99	12,565.7	3,935.2	3.19
12/31/99-9/30/08*	26,390.5	4,893.3	5.39

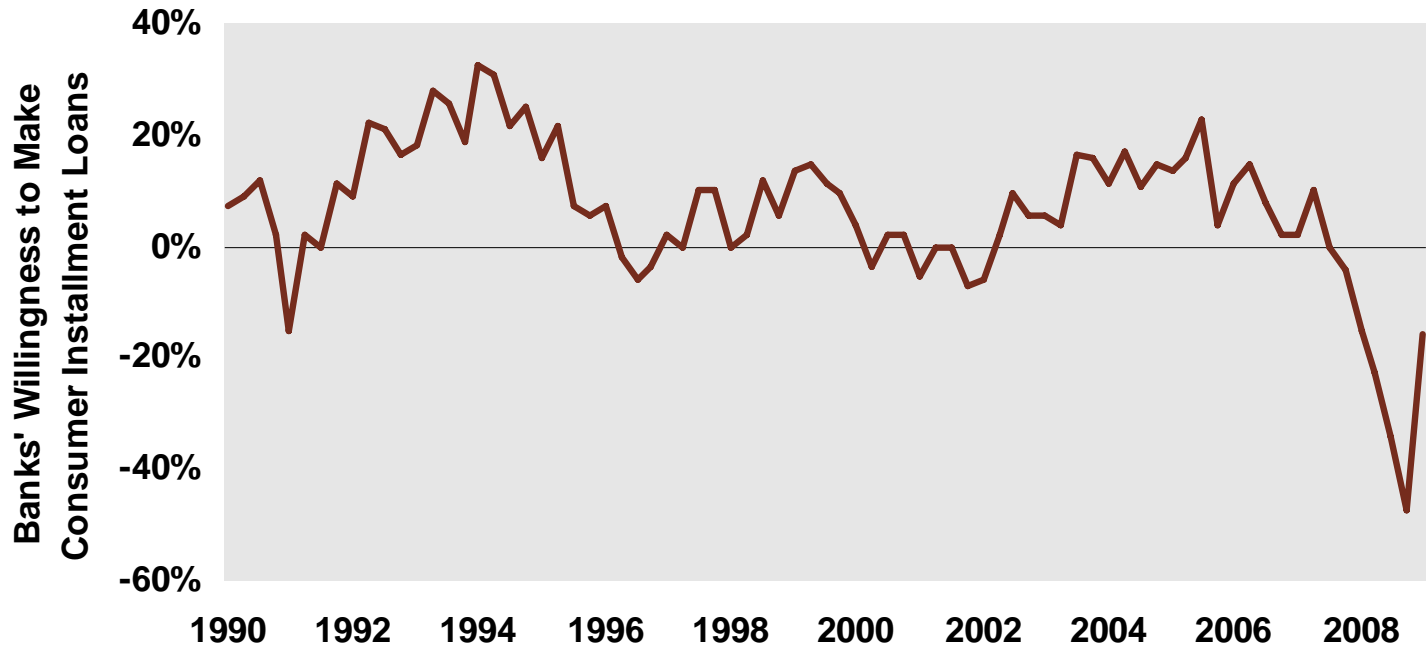
# Consumer Moving to GDP Passenger Seat

GOVERNMENT BECOMING SPENDER OF LAST RESORT



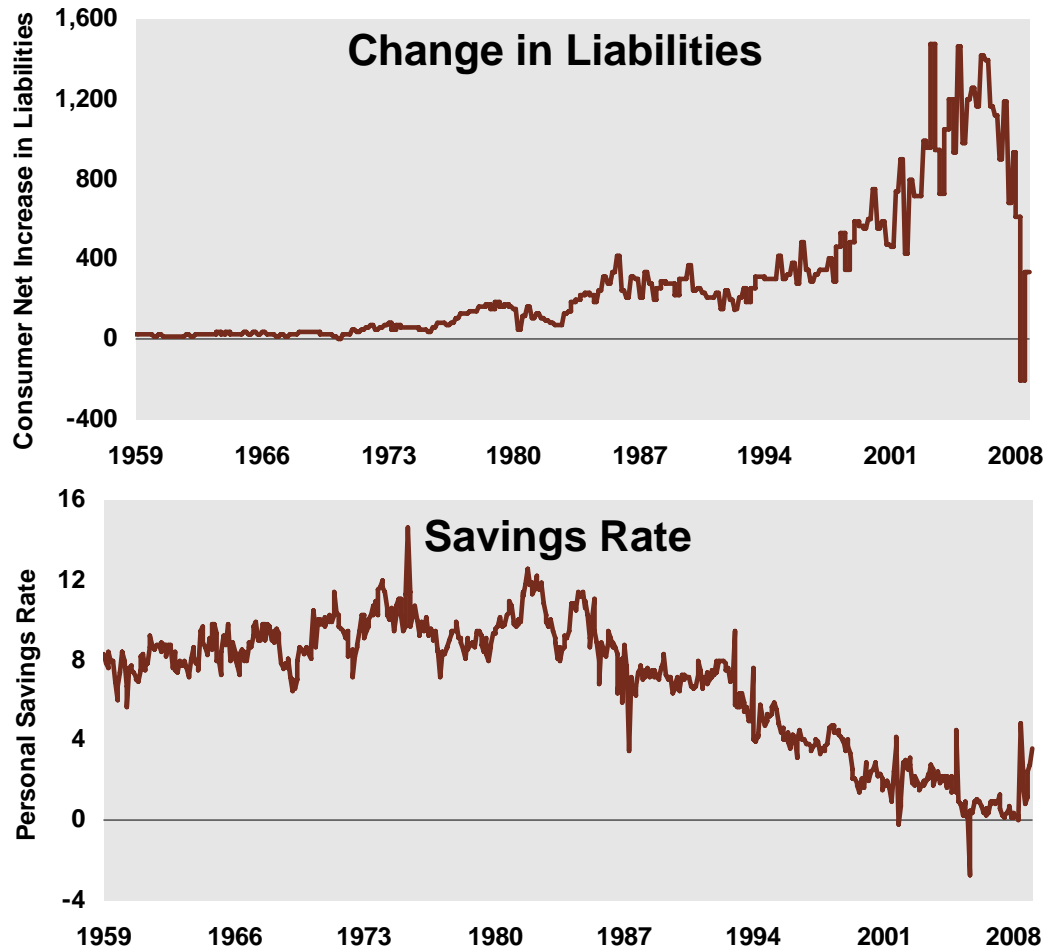
# Banks Finally Loosening Purse Strings

BUT DEMAND REMAINS WEAK



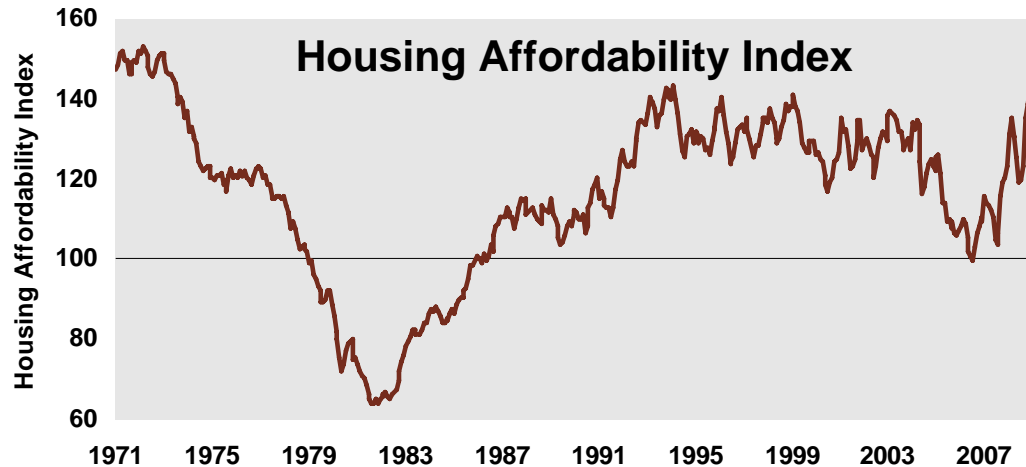
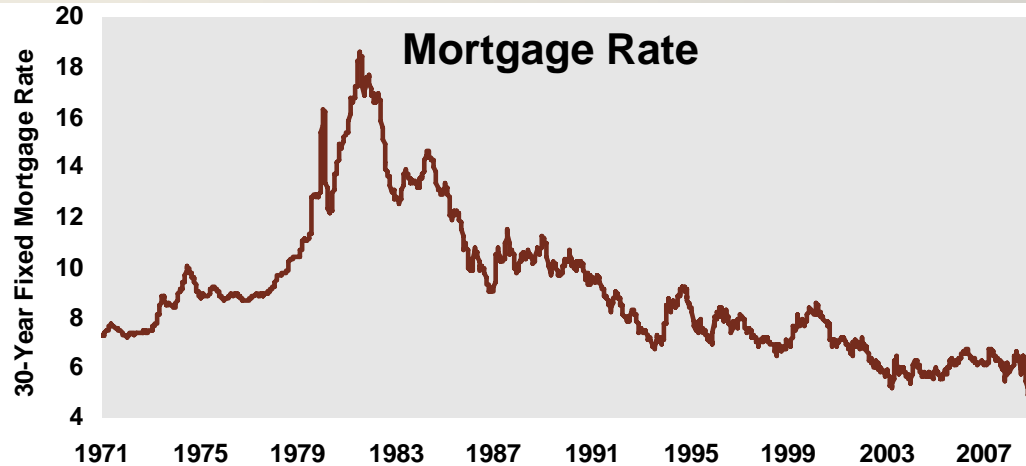
# Consumer Debt Contracts Massively

SAVINGS TO BE BIG BENEFICIARY, BUT NOT GDP



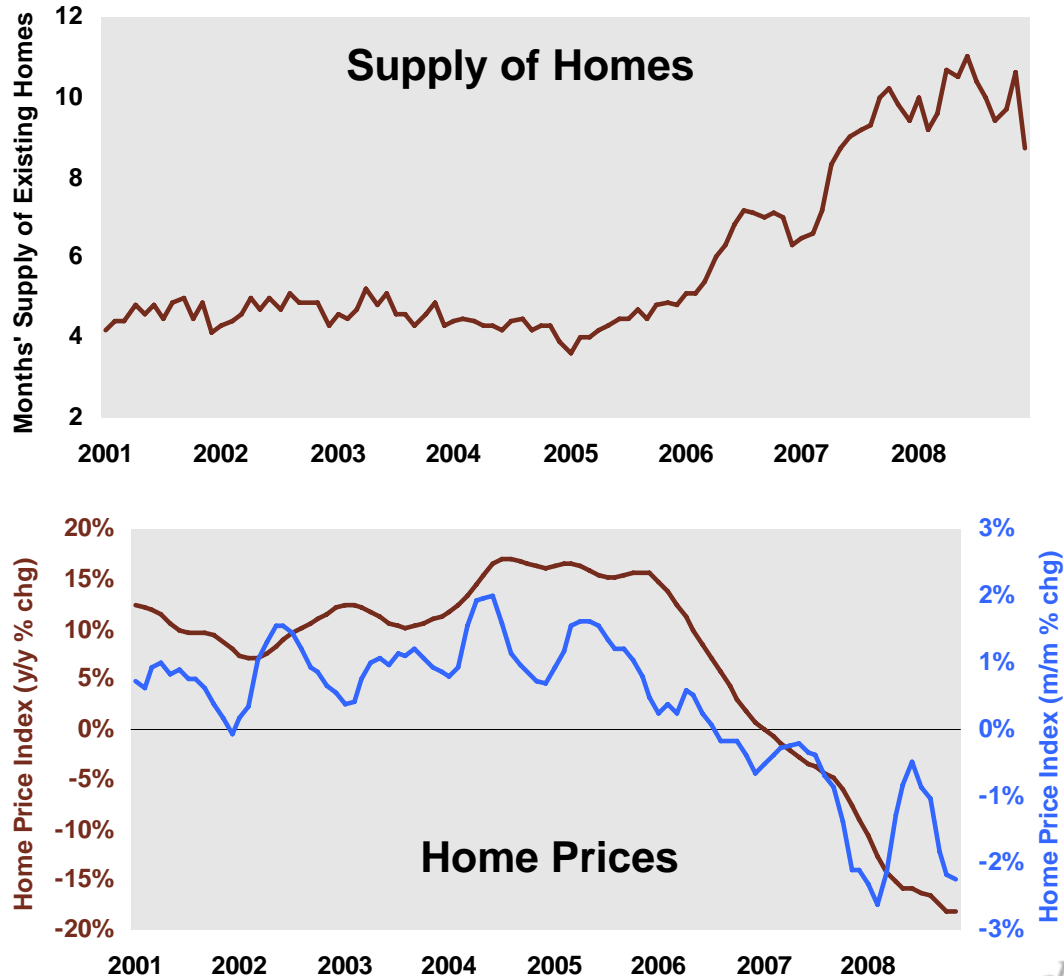
# Mortgage Rates Coming Down

CONTRIBUTING TO RECORD HOUSING AFFORDABILITY



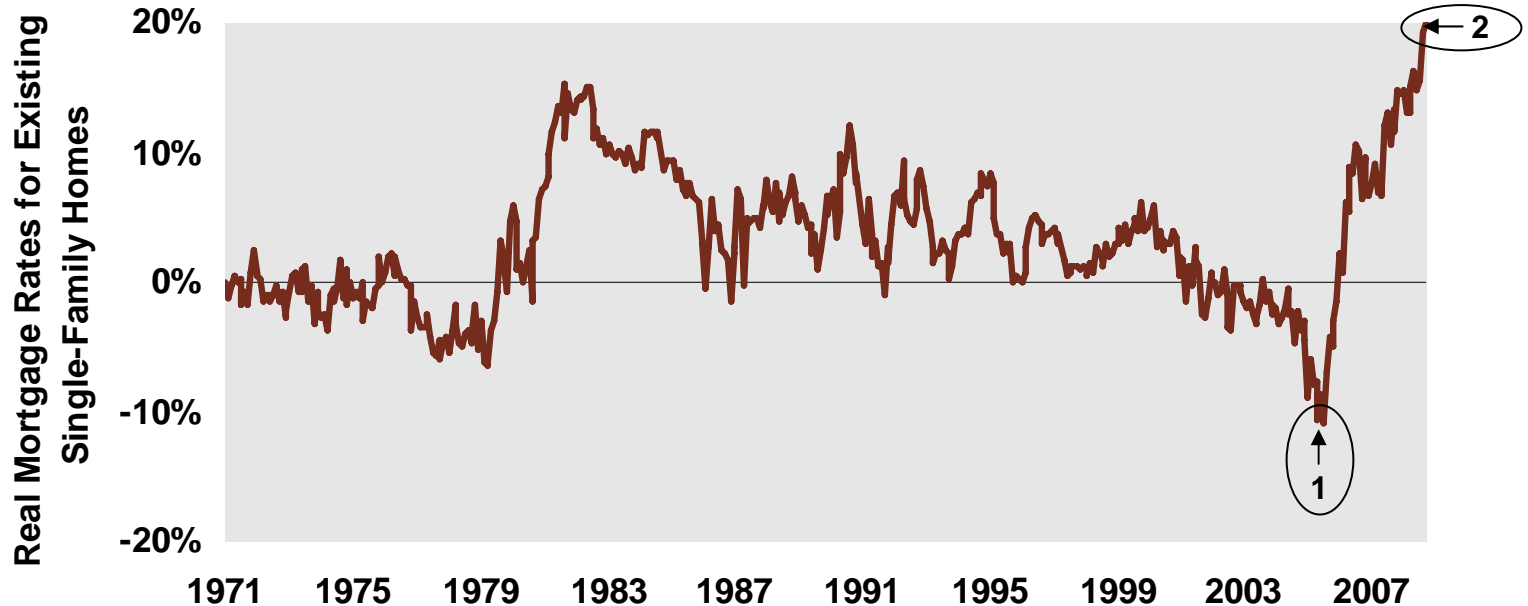
# Housing Inventories Finally Retreating

SUSTAINABLY LOWER INVENTORIES NEEDED FOR FIRMER PRICING



# “Real” Mortgage Rates Stratospheric

WHO WANTS TO BORROW TO BUY A RAPIDLY DEPRECIATING ASSET?

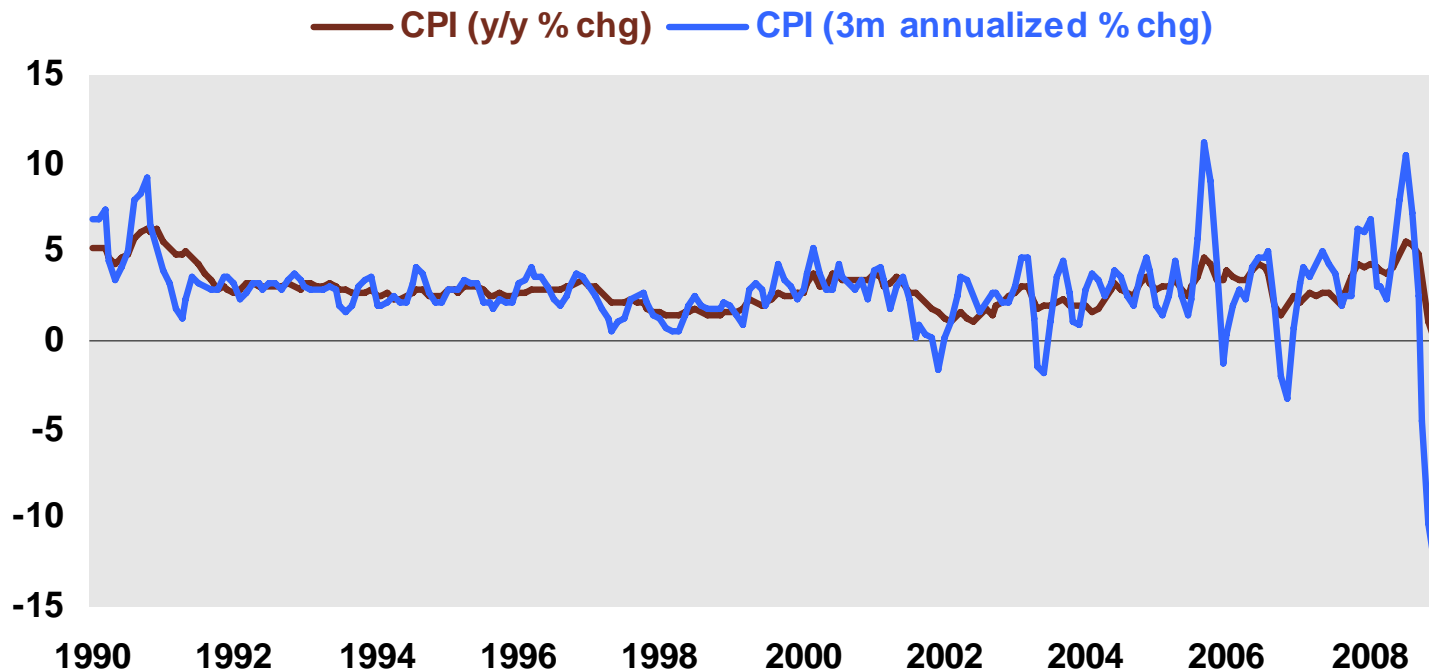


1)  $6.1\% \text{ minus } 16.9\% = (10.8\%)$

2)  $5.3\% \text{ minus } (14.8\%) = 20.1\%$

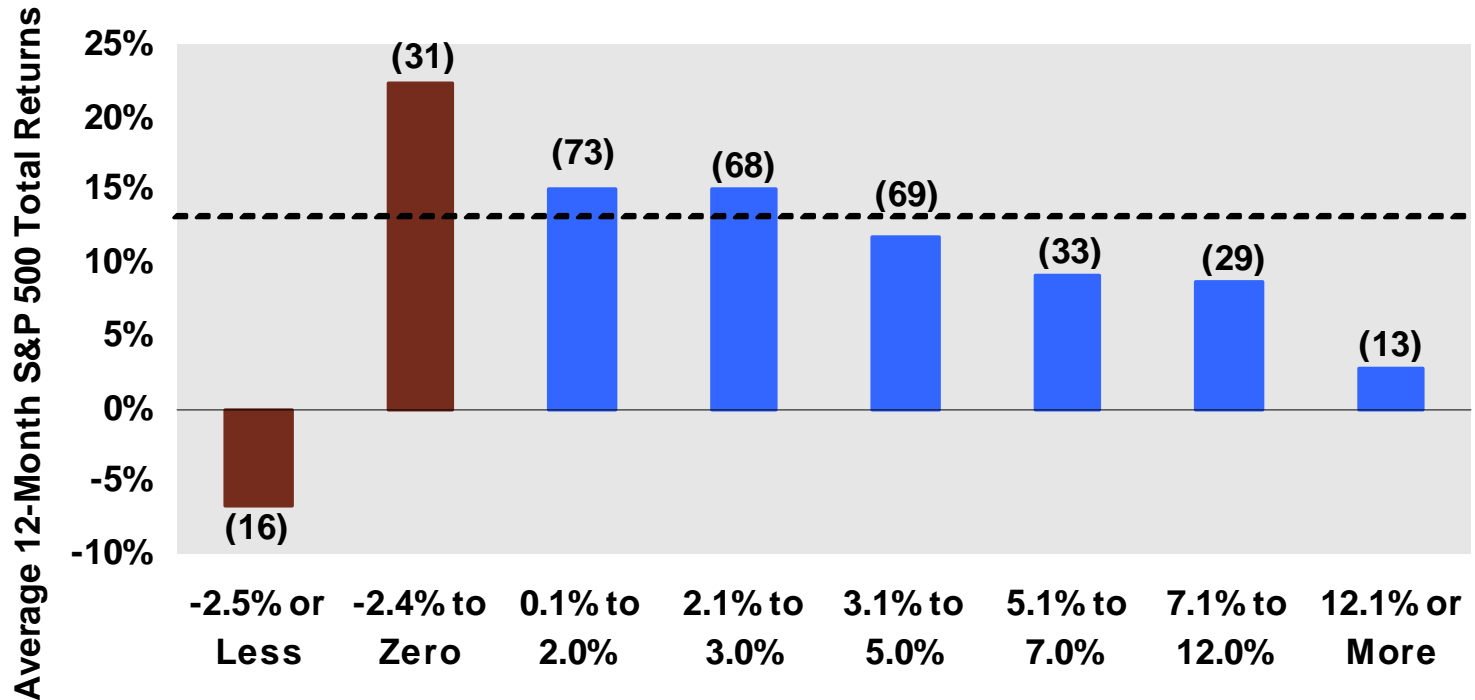
# How Big a Problem is Deflation?

LAST THREE MONTHS' CPI IMPLOSION NOT LIKELY SUSTAINABLE



# What Does Deflation Risk Suggest for Market?

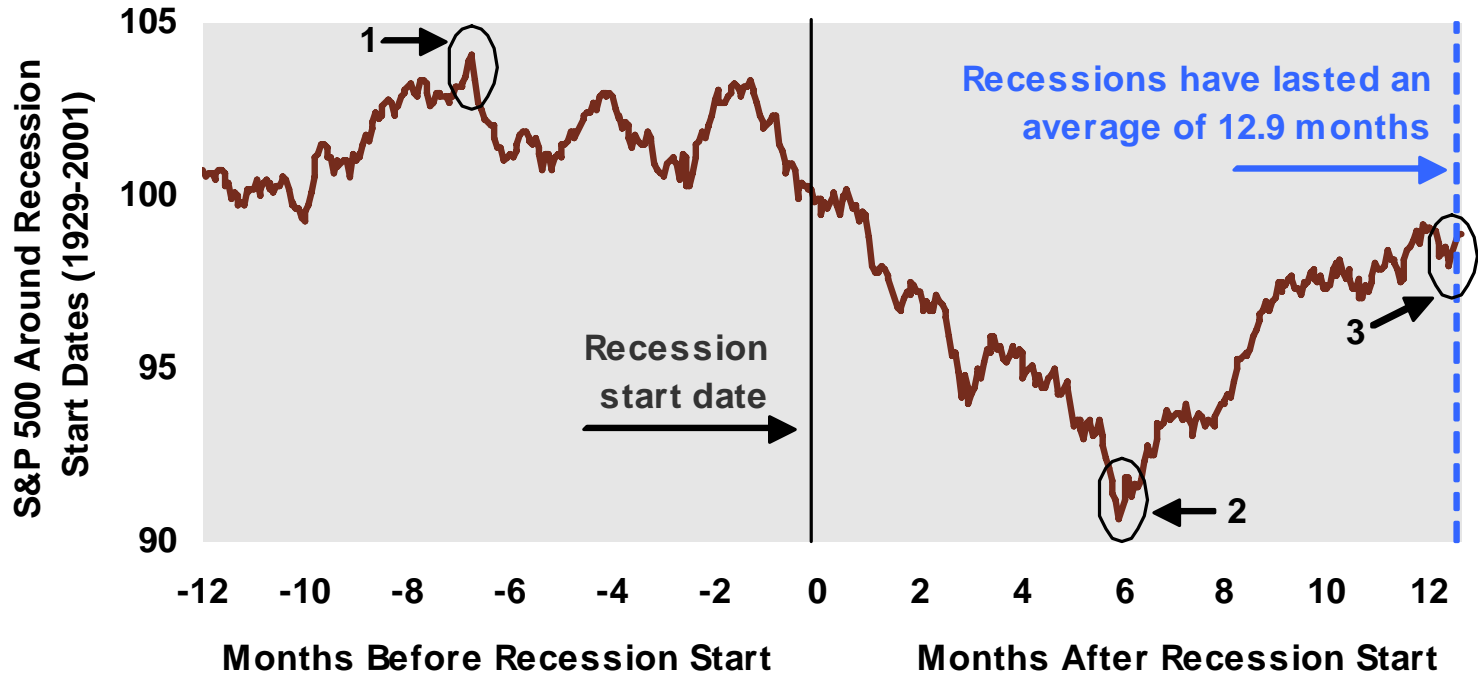
MILD DEFLATION IS LOVED, SEVERE DEFLATION IS HATED



# STOCK MARKET

# Markets Typically Anticipate Recessions

WHILE STARTING TO RECOVER DURING THEM

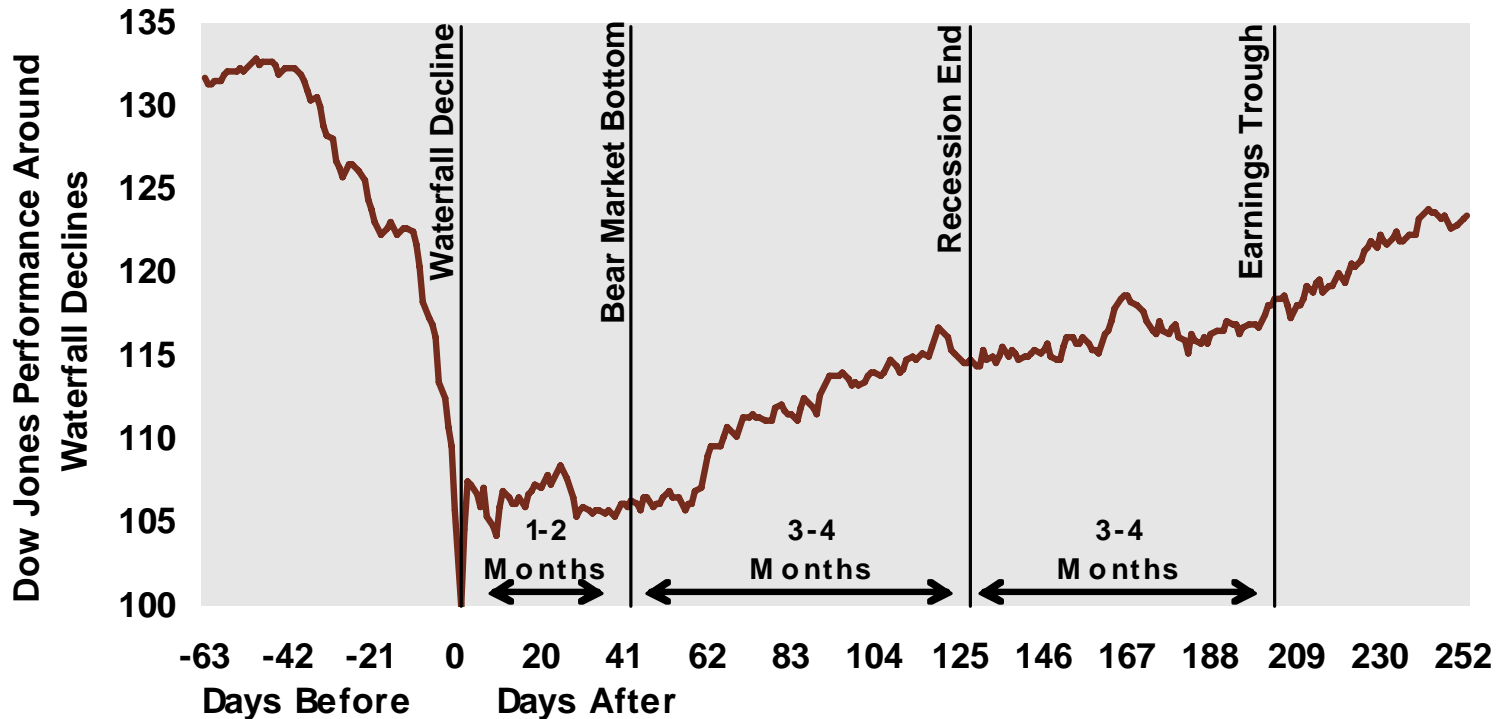


**1-2: Peak-to-trough average decline = 30%**

**2-3: Trough-to-recession end average gain = 25%**

# Post-Waterfall Declines' Phases

WHAT MIGHT HAPPEN FROM HERE?



Waterfall decline defined as a Dow Jones Industrial Average loss of more than 20% in a short period of time; and near the end, the 10-day average of the NYSE total volume rises two times its average seen just a few months earlier. Chart shows performance of the Dow (indexed to 100) as averaged from the 10 waterfall declines between 1929 and 2002. X-axis represents days before and after waterfall decline. Source: Ned Davis Research, Inc.

# Ugly Economy in 2008...Jobs Disappearing

BUT, IS THAT BAD NEWS FOR MARKET?

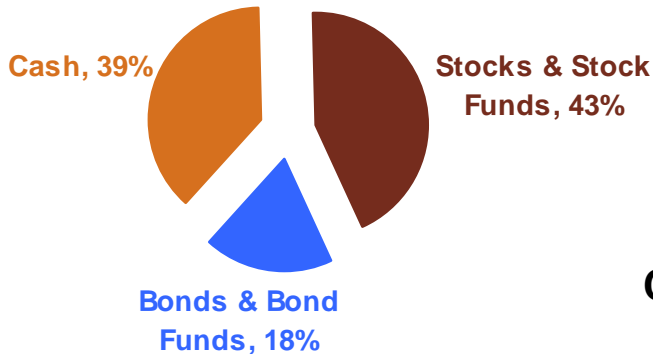
10 Worst GDP Quarters	
Date (of Quarter)	S&P 500 1 Year Later
3/31/58	31.7%
6/30/80	14.9%
3/31/82	36.6%
12/31/53	45.0%
3/31/49	14.8%
12/31/60	23.3%
12/31/81	14.8%
3/31/75	24.4%
12/31/70	10.8%
12/31/57	38.0%
<b>Average</b>	<b>25.4%</b>

10 Worst Jobs Reports	
Date (Month/Year)	S&P 500 1 Year Later
9/45	-6.8%
10/49	21.4%
2/58	36.2%
12/74	31.6%
11/53	38.3%
5/60	19.2%
10/70	13.0%
5/80	20.2%
7/82	50.9%
2/91	12.4%
<b>Average</b>	<b>23.6%</b>

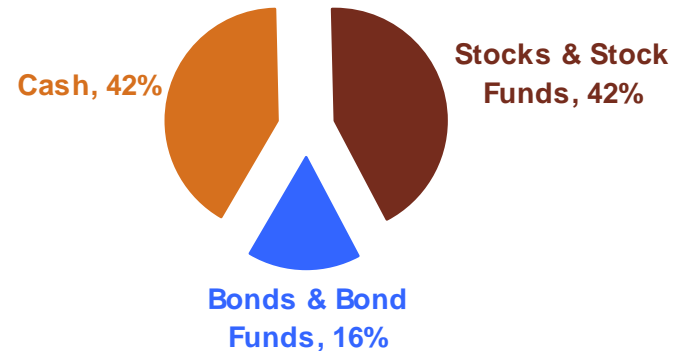
# Cash on Sidelines Surges

TODAY'S CASH LEVELS AT ALL-TIME HIGH

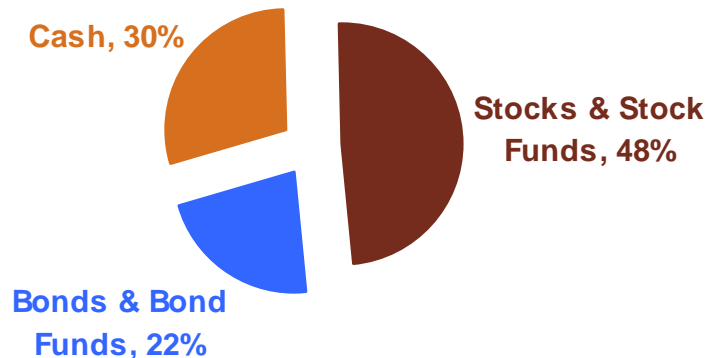
**October 2002**  
**Prior Highest Cash**



**December 2008**  
**Recent Highest Cash**



**January 2009**  
**Current Month**



- **\$9.4T currently held in cash, bank deposits & money market funds = 96% of market value of all U.S. companies**

# Disclosures

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The information provided here is for general informational purposes only and should not be considered an individualized recommendation or personalized investment advice. The investment strategies mentioned here may not be suitable for everyone. Each investor needs to review an investment strategy for his or her own particular situation before making any investment decision.

We believe the information obtained from third-party sources to be reliable, but neither Schwab nor its affiliates guarantee its accuracy, timeliness, or completeness. Opinions and estimates herein are as of the date of the material and are subject to change without notice at any time in reaction to shifting market conditions. Past performance is no guarantee of future results.

Examples provided are for illustrative purposes only and not intended to be reflective of results you should expect to attain.

Slides 8, 9, 10 - On October 3, 2008, FDIC deposit insurance temporarily increased from \$100,000 to \$250,000 per depositor through December 31, 2009. IRAs and certain other retirement accounts for which the deposit insurance limit already was \$250,000 prior to October 3, 2008 will continue to be insured up to \$250,000.

Slides 8, 9, 10 - The U.S. Treasury Temporary Guarantee Program provides a guarantee to participating money market mutual fund shareholders based on the number of shares invested in the fund at the close of business on September 19, 2008. Any increase in shares in the account after the close of business on September 19, 2008, will not be guaranteed. If the value of these shares fluctuate over the period, investors will be covered for either the number of shares held as of the close of business on September 19, 2008, or the current amount, whichever is less. If a client closes his/her account with a fund or broker-dealer, any future investment in the fund will not be guaranteed. The Program has been extended and expires on April 30, 2009. The program will terminate on that date unless extended again by the U.S. Treasury.

# Definitions

## Indexes

Indexes are unmanaged, do not incur management fees, costs and expenses (or "transaction fees or other related expenses"), and cannot be invested in directly.

**The CRB Index** is based on the CRB (Commodity Research Bureau) Futures Index which is a commodity index based on the futures prices of various commodities.

**The Dow Jones Industrial Average** (DJIA, "The Dow") is a price-weighted average of 30 actively traded blue chip stocks, primarily industrials and is the oldest and most widely quoted of all the market indicators.

**The S&P 500 Index** is a capitalization-weighted index of 500 stocks from a broad range of industries. The component stocks are weighted according to the total market value of their outstanding shares.

## Terms

**Asset Allocation** - The strategy of spreading your investment funds across categories of assets such as stocks, bonds and cash equivalents to help offset risks and rewards, based on your goals, time horizon and risk tolerance.

**Housing Affordability Index** – The National Association of Realtors' Housing Affordability Index measures whether or not a typical family could qualify for a mortgage loan on a typical home. A value of 100 means that a family with the median income has exactly enough income to qualify for a mortgage on a median-priced home. An index above 100 signifies that family earning the median income has more than enough income to qualify for a mortgage loan on a median-priced home, assuming a 20 percent down payment.

**Ned Davis Research (NDR) Crowd Sentiment Poll** - Shows perspective on a composite sentiment indicator designed to highlight short- to intermediate-term swings in investor psychology. It's based on seven different individual sentiment indicators in order to represent the psychology of a broad array of investors.

**Recession** - As per National Bureau of Economic Research (NBER), a recession is a significant decline in economic activity spread across the economy, lasting more than a few months, normally visible in real GDP, real income, employment, industrial production, and wholesale-retail sales.