

IMPACT OF AUGUST 17TH FEDERAL RESERVE BOARD ACTION
ON THE FIXED INCOME ENVIRONMENT

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On the morning of Friday, August 17, 2007, the Federal Reserve Board reduced the discount rate from 6.25% to 5.75% and allowed financing for as long as 30 days, renewable by the borrower, rather than overnight financing. Further, Fed representatives arranged a conference call with leading commercial and investment banks urging them to use the Fed's discount window as a sign of strength rather than the stigma that would normally be associated with such a move. Finally, the Federal Reserve's Open Market Committee, which is responsible for setting the more important federal funds rate, changed its risk assessment from its August 7 meeting stating, in part, that the "Committee is monitoring the situation and is prepared to act as needed to mitigate the adverse effects on the economy arising from the disruptions in financial markets."

We believe that these actions by the Fed are an important first step in the restoration of liquidity to the credit-sensitive fixed income markets. The conditions that we described in our August 6, 2007 update on the fixed income markets continued to deteriorate prompting the Fed action. As an example, the yield on one-month Treasury Bills was 4.83% on August 6 compared to the fed funds rate of 5.25%. Last week, the yield on one-month Treasury Bills declined from 4.62% to 2.96% and it was well below 2% on the morning of August 21st.

Kent and Rick have been in the fixed income markets for 35 years each and have seen conditions like this only a couple of times. However, on each occasion liquidity was restored, and our markets functioned efficiently once again. More action may well be needed, but we believe that the Fed and the federal government will do what is necessary to see that liquidity is in fact restored.

As significant investors, we share your anxiety, but we remind ourselves that the information imparted from market prices in such an extreme environment is limited.



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