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TEXPERS SUBPRIME CRISIS WORKSHOP

An Overview of:

The Sub-Prime Crisis and U.S. Stock Market

Reality versus Headlines

May 12, 2008

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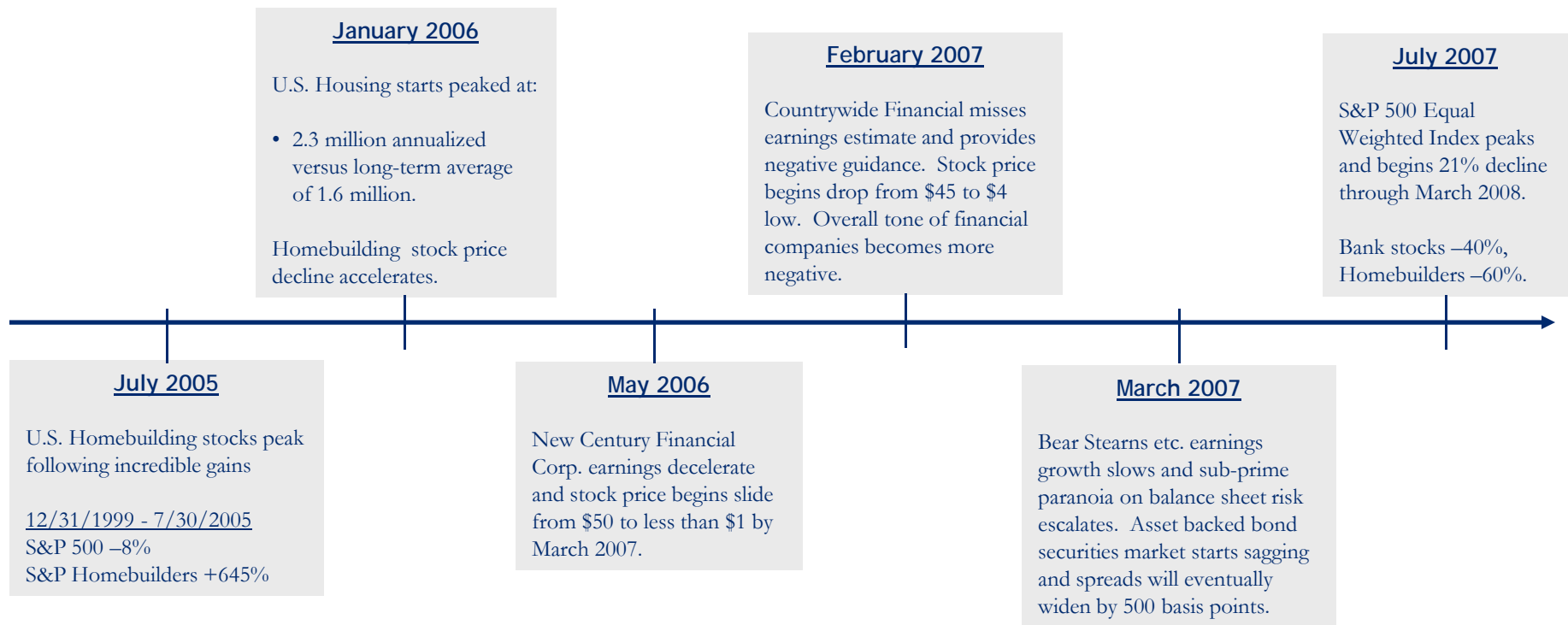
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Major Events in the Sub-Prime Time-Line





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Injured & Casualties of Sub-Prime Crisis

	<u>Peak</u>	<u>Trough</u>
Housing starts	2.2 million	.95 million (-57%)
Home Prices	+17% year over year	-13% year over year
Lennar (LEN)	\$68	\$13 (-81%)
New Century Finance	\$64	\$0
Bear Stearns	\$171	\$5

Index Returns from S&P 500 Peak of 10/9/2007 through Trough of 3/10/2008

S&P 500 Index	-19%
S&P Bank Stocks	-40%
S&P Thrifts & Mortgage Stocks	-67%
S&P Retailing Stocks	-25%
High Yield Bonds	-5%
10-Year U.S. Treasury	+12%
Asset Backed Debt	-8%
CMBS (BBB Rated)	-25%

You cannot invest directly in an index. Indexes are unmanaged and do not incur fees.

Source: Bloomberg



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May 2008

DNA Tests for Traditional Crisis

1. Excess investor speculation and subsequent bubble splattering
2. High inflation followed by restrictive Federal Reserve Policy
3. Intrusive tax or regulatory legislation
4. World political unrest

Sub-Prime Crisis is No Different

1. Excess speculation
2. Fed tightening and flat yield curve
3. Failure of select industries to understand risk
4. Likelihood of greater regulation

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Avoiding High Risk Stocks Has Been Particularly Important Compared To Past Years

	2005	2006	2007	12/31/07 To 4/30/08
S&P 500 total return	+4.9%	+15.8%	+5.5%	-5.0%
Number Stocks with total return worse than -20%	30	16	115	64

Ten Worst Performing S&P 500 Stocks in 2007

Stock	% Change
Office Depot	-64%
MGIC Investment Corp.	-64%
Lennar Corp.	-65%
Pulte Homes	-68%
Washington Mutual	-68%
Ambac Financial Group	-71%
MBIA	-74%
Circuit City Stores	-77%
Countrywide Financial	-78%
E*Trade Financial	-84%

Ten Worst Performing S&P 500 Stocks in 2008

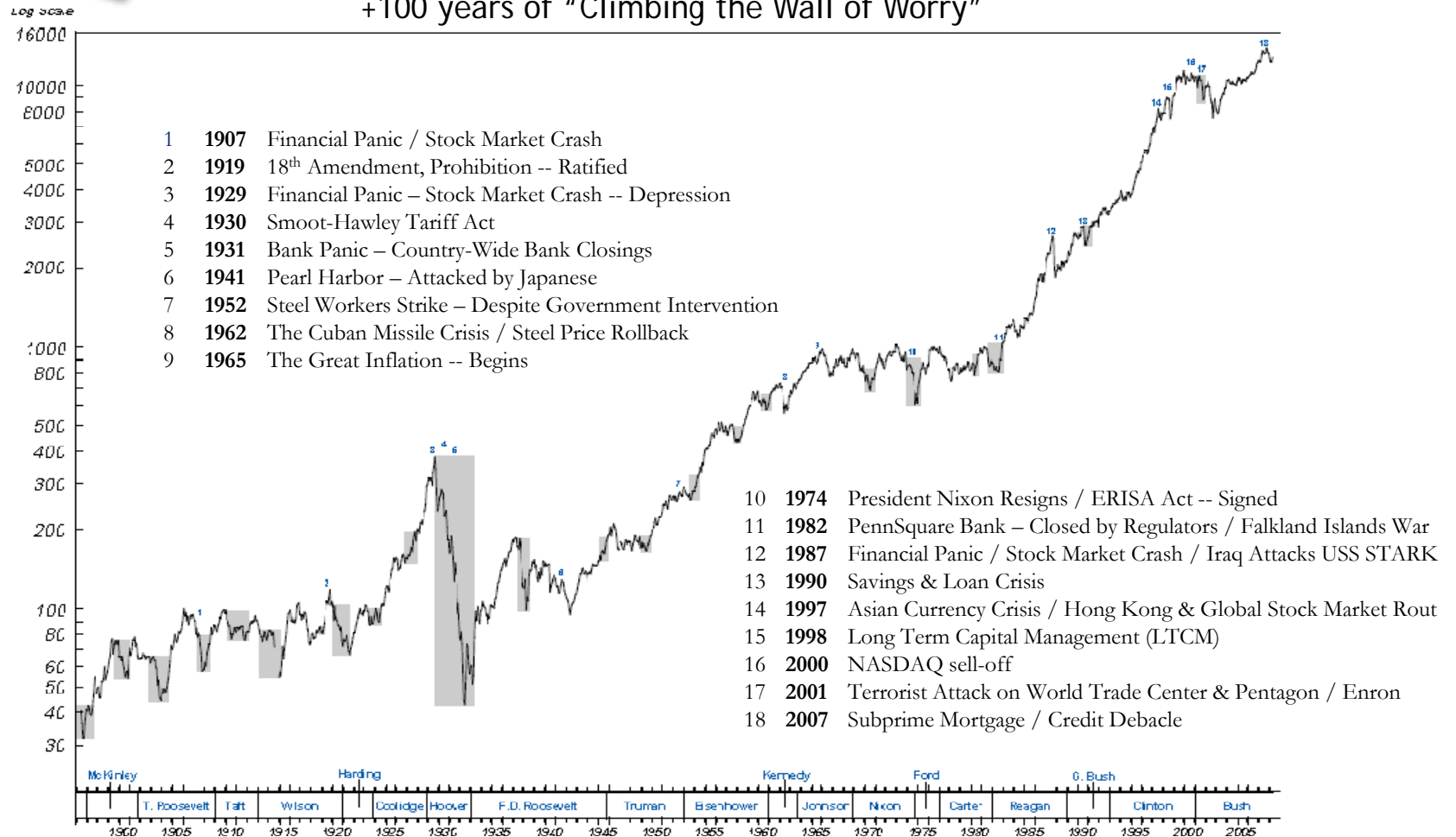
Stock	% Change
Titanium Metals	-42%
WellPoint	-43%
United Health Group	-44%
MBIA	-44%
Harman International Ind.	-45%
Tesoro	-47%
CIT Group	-55%
National City	-62%
Ambac Financial Group	-82%
Bear Stearns	-88%

Past performance is no guarantee of future results. 2008 data is as of 4/30/2008.
 Source: Baseline, Loomis Sayles



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The Dow Jones Industrial Average: 1896-2008 +100 years of "Climbing the Wall of Worry"



Shaded areas represent recessionary periods. 2008 data is preliminary through April.

Data Sources: Dow Jones & Company; The Federal Reserve Board; The National Bureau of Economic Research • Copyright © 2008 Crandall, Pierce & Company • All rights reserved.

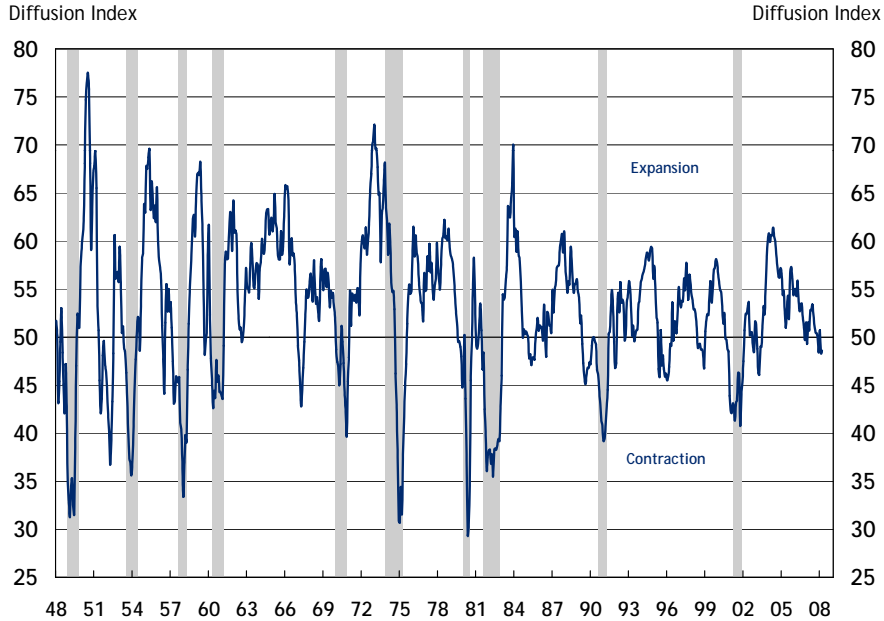
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Still suggests no or mild recession

ISM MANUFACTURING COMPOSITE INDEX

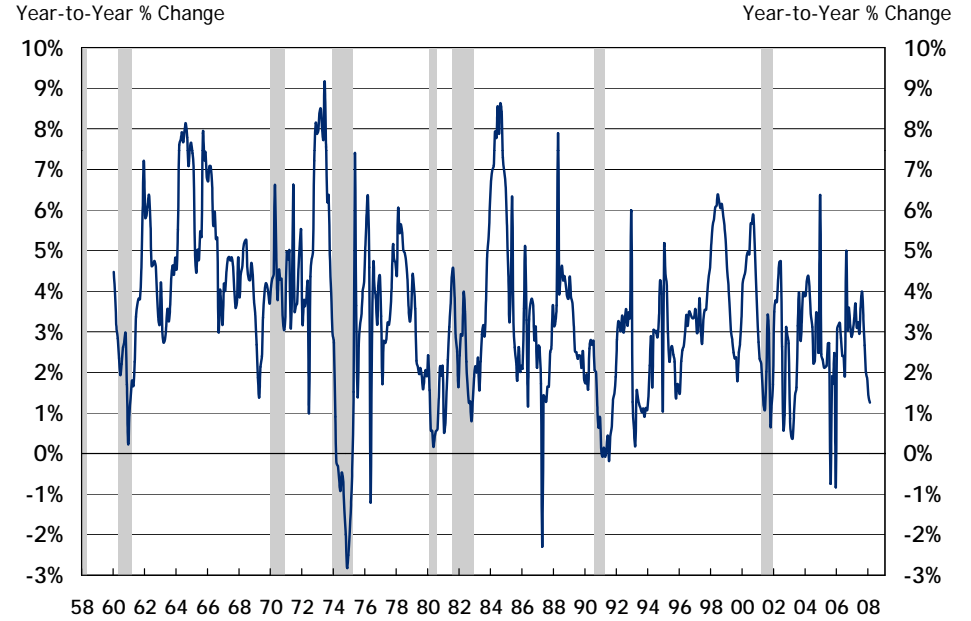


Seasonally Adjusted; Monthly Data; (Shaded Areas Denote NBER-Designated Recessions)
Source: Institute of Supply Management; History Through March 2008

01M-08

Not at recession levels...yet

REAL DISPOSABLE INCOME



Seasonally-Adjusted Annual Rate; Monthly Data; Shaded Areas Denote NBER-Designated Recessions
Source: Commerce Department; History Through February 2008

02M-13



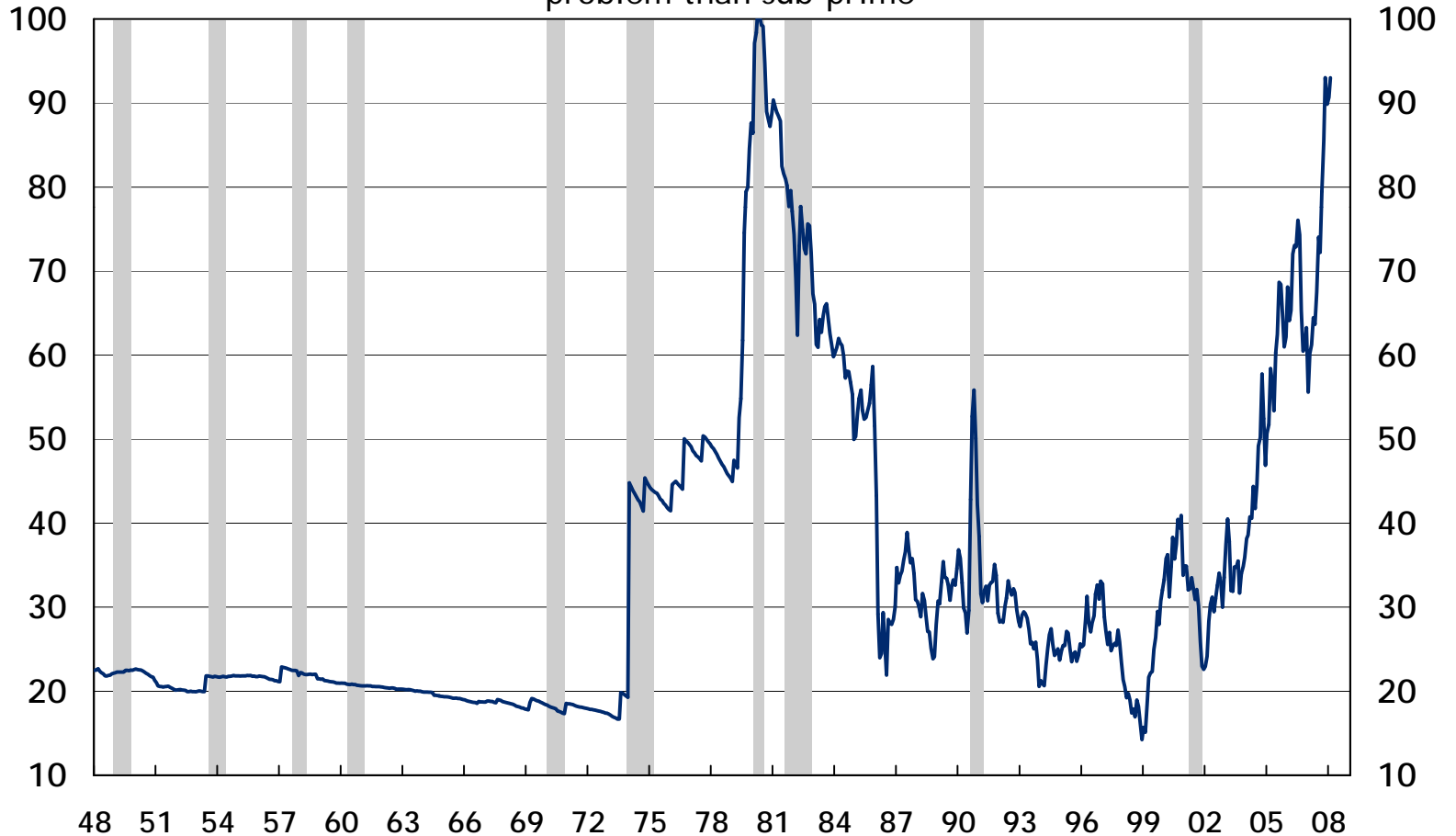
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REAL OIL PRICE

2007 \$/Barrel

Excluding Texas Benefits: Potentially a larger problem than sub-prime

2007 \$/Barrel



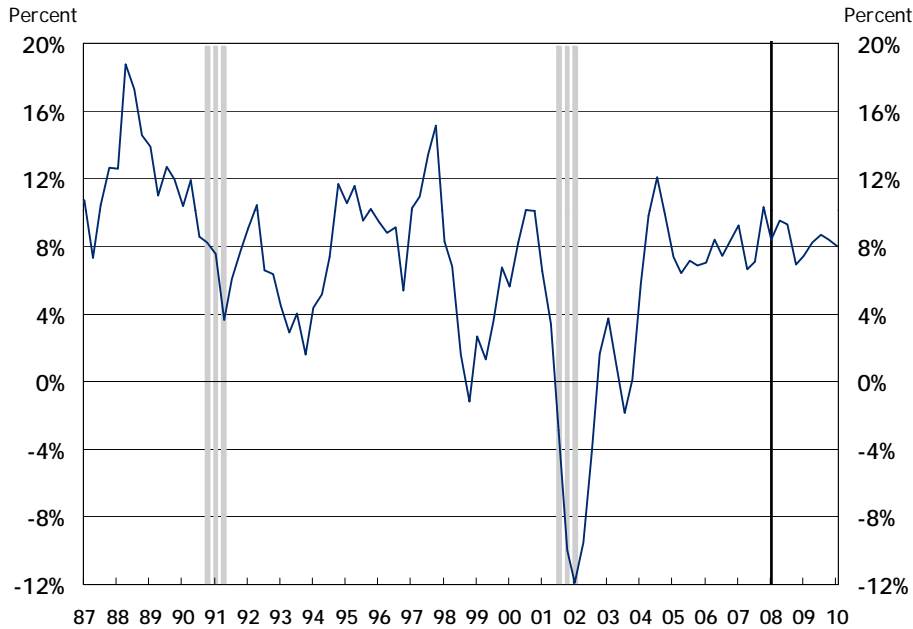
West Texas Intermediate Spot Prices; Uses CPI To Convert To 2007 Dollars; Monthly Data; Shaded Areas Denote NBER-Designated Recessions

Source: U.S. Labor Department; Wall Street Journal; History Through February 2008



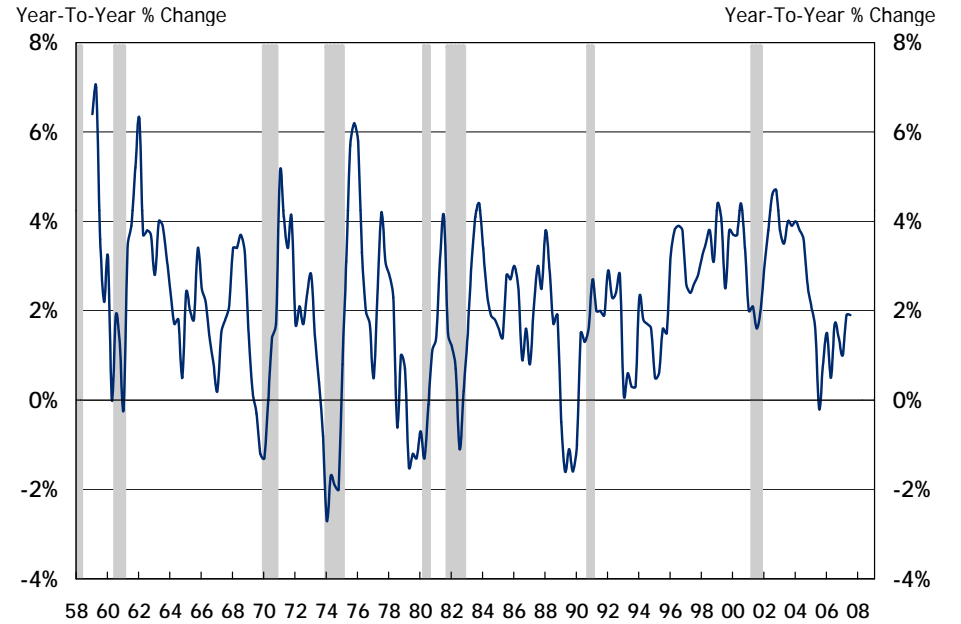
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EXPORTS OF GOODS AND SERVICES



Quarterly Data; Shaded Areas Denote NBER-Designated Recessions
 Source: Commerce Department; Loomis Sayles; History Through Q4:2007; Forecast Through Q4:2009

NONFINANCIAL CORPORATIONS: OUTPUT PER EMPLOYEE-HOUR



Quarterly Data, Seasonally Adjusted, Year-to-Year Percent Change; Shaded Areas Denote NBER-Designated Recessions
 Source: Labor Department; History Through Q3:2007

07Q-02F

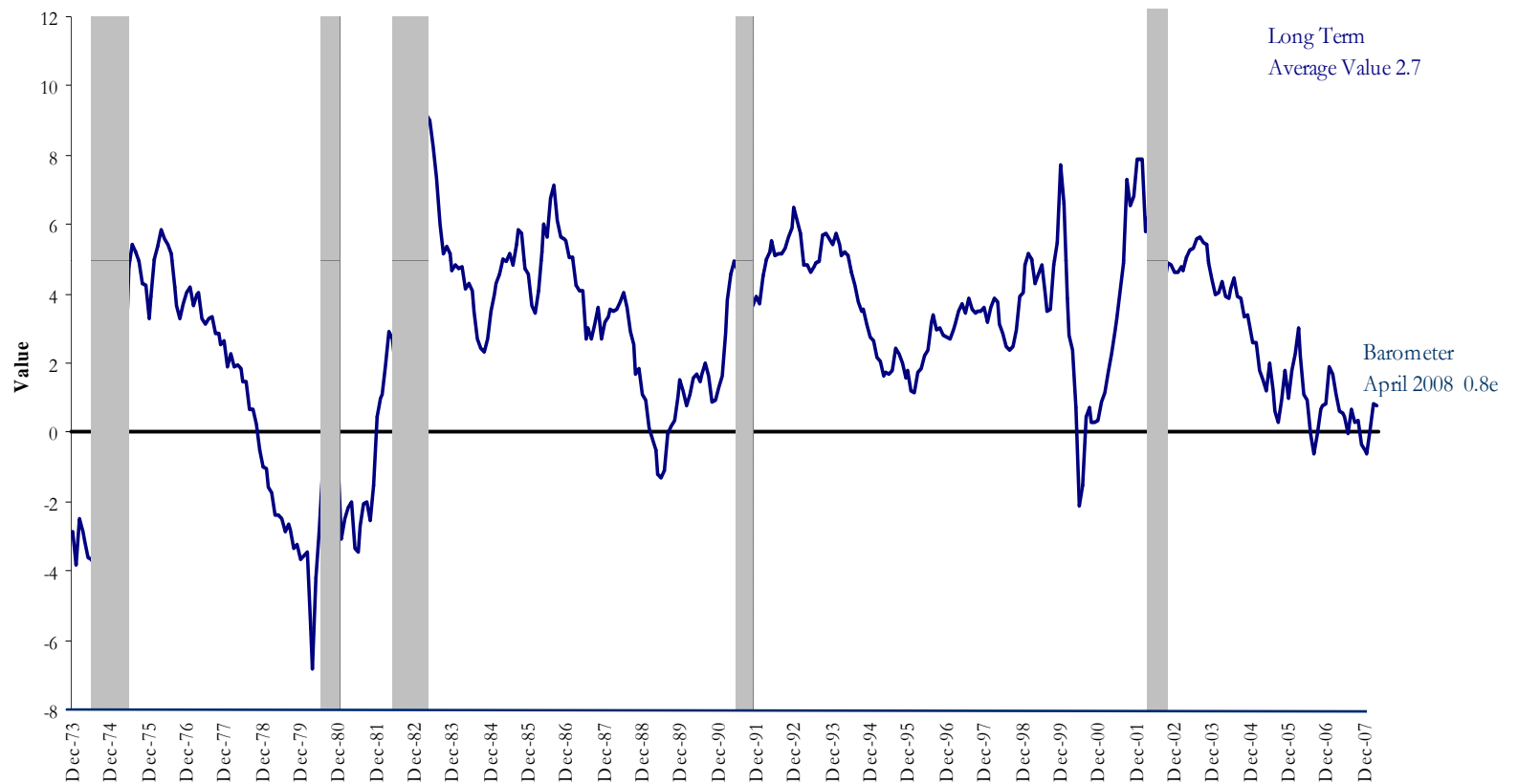
05Q-10



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Advanced Business Barometer

3-4 Quarter Advance View of U.S. Business Conditions



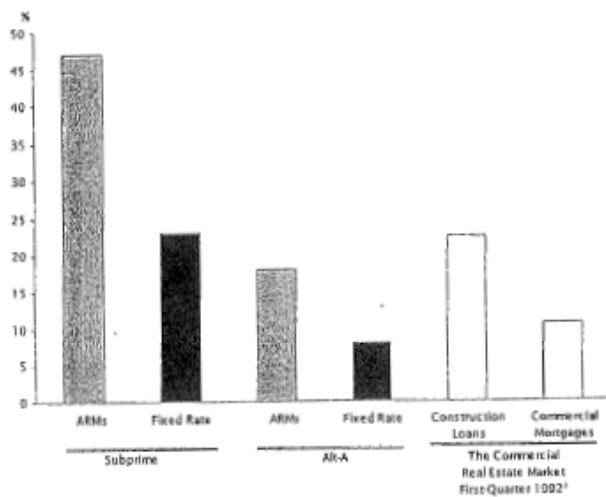
Components:

- Inflation adjusted M2 Money Supply Growth
- Inflation adjusted Monetary Base Money Supply Growth
- Yield Credit Curve Spread (BAA Corps – Fed Funds)
- Index of Leading Economic Indicators



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Share of Subprime and Alt-A Mortgage Loans That are Delinquent on Payments As of February 2008



Source: Federal Reserve Bank of New York, LoanPerformance, FDIC.

¹ Commercial banks with \$10 billion or more in assets.

Estimate of Full-Cycle Losses to U.S. Publicly-Held Financial Institutions As of Mid-April 2008

Category	\$ Billion	
	Total Losses	To U.S. Companies
Subprime and Alt-A Mortgages		
On Balance Sheet	\$75	\$50
Securitized	300	160
Prime Mortgages	40	40
Commercial Real Estate	125	75
Total Real Estate	\$540	\$325
Other Consumer Debt	\$20	\$20
Corporate Loans	50	40
LBO Loans and Securities	70	40
Total All Other	140	100
Grand Total	\$680	\$425

Source: International Monetary Fund, Empirical Research Partners Estimates.



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Commercial Bank Charge-off Rates and Financial Stocks' Performance Relative Growth of a Dollar¹ 1989 Through 1993



Source: Federal Reserve Bank of New York, LoanPerformance, FDIC.

¹ Largest 1,500 stocks; ratio of dollar growth of financials and the market.



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Stock Market Verdict Sub Prime Infected versus Sub Prime Immune Stock Buckets

	Average Stock Price % Change May 07-March 08	Average Stock Price % Change March 08-early May 08	Average Stock Price % Below 52 week high	Average Stock Price % Above 52 week low	Average Latest Quarter Earnings Surprise as a %	Average E.P.S. Estimate Revisions last 3 months	Average P/E next 12 months	Average P/E 5 Year Average	Average Free Cash Flow Yield
Sub Prime Infected 25 stocks	-57%	+14%	-54%	+44%	-25%	-200%	14x	14x	2.7%
Sub Prime Immune 25 stocks	+10%	+17%	-10%	+56%	+13%	+10%	14x	25x	4.3%
S&P 500	-16%	+11%	-11%	+11%	N/A	N/A	15x	17x	4.0%

Sub Prime Infected: GM, KSS, FDO, PHM, LEN, KBH, CCL, WHR, BC, HD, SLM, BAC, C, WB, CMA, MBI, ABK, MS, LEH, NCC, FNM, FRE, WM, CFC, MTG

Sub Prime Immune: BTU, RIG, ESV, SLB, HAL, BHI, DVN, APC, XOM, COP, CAT, DE, UNP, BNI, RIG, MON, DD, FCX, PX, POT, NUE, X, CMI, MTW, GWW



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Estimated Ranking of Stock Market & Economic Crisis

		<u>Peak-to-Trough Market Decline</u>		
1.	Great Depression (1930s)	Dow Jones	-89%	
2.	1980 – 82 Double Dip Recession	S&P 500	-27%	
3.	1965 Onset of Inflation	Stocks Tread Water	15 Years	
4.	Wall Street Financial Panic 1907	Dow Jones	-48%	
5.	1973 – 74 Bear Market	S&P 500	-48%	
Tie for 6 th	6.	Sub Prime Housing	S&P 500	-19%
	6.	Savings & Loan Crisis (1990 – 91 Recession)	S&P 500	-20%
8.	Tech Bubble Implodes 2000	S&P 500	-49%	
9.	1987 Stock Market Crash	S&P 500	-34%	
10.	Long Term Capital Management (1998)	S&P 500	-19%	

Ranking determined by judgment and opinion of portfolio analysts based upon currently available data. Unexpected events may occur. Opinions expressed reflect subjective judgments and will evolve as future events unfold.

Source: Loomis Sayles, Crandall Pierce