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TOUCHSTONES

INVESTMENT CONSULTING • FIDUCIARY AND SRI COUNSEL • VIAGEM FOUNDATION PROGRAM

This newsletter, for faith and mission-based organizations, presents pertinent information relating to our work, industry best practices, and real life experiences.

Summary and Initial Impact of the Sub-Prime Financing Crisis

The past few months have been interesting seeing how the sub-prime lending crisis has played out in the marketplace, and the impact it has had on investors.

The likelihood of faith-based investors being directly affected by Sub-Prime issues is very low. However, indirectly they have been affected by increased uncertainty and volatility in the broader investment markets.

Sub-prime concerns were a by product of the recent U.S. housing boom, which lasted well beyond the average length of previous expansions. During this time, housing prices rose as the demand for real estate increased and supply became somewhat restricted, especially in the more popular, high-growth areas of the country.

Many investors increased their exposure to real estate and related securities when rates were low, from earlier in the decade.

As lenders and investors attempted to expand their services, products, and portfolios to capitalize on the trend, some of them got involved in non-conforming, adjustable rate loans to borrowers, who otherwise may not have been able to qualify for a loan.

As the economic recovery and expansion took hold and the Federal Reserve raised rates, the cost of adjustable rate loans continued to rise as did the risk of defaults.

Some of those homeowners who found it easy to get (adjustable rate) loans to purchase their homes, were finding it difficult to make payments on their mortgages.

Defaults led to foreclosures, which led eventually to more supply than demand for residential homes, which led to concerns about valuations, which led to bankers being concerned about collateral, which led to some investors having trouble selling assets in their portfolios without taking losses, which led to lack of liquidity to fulfill some redemption requests, which led to the U.S. Federal Reserve lowering the discount and target Fed Funds rates to enable easier access to credit for banks, consumers, and investors; which puts us where we are today.

The short-term result from this situation on the markets has been increased uncertainty and volatility. Additional fall-out is expected from the sub-prime crisis over the next several months, however, the proactive response from the Fed and other central banks has encouraged investors to not panic and stay the course. We'll stay tuned.

Finally, a couple of key ways to reduce the impact of negative economic situations on your portfolio are to: proactively maintain a broad diversification of different asset classes and an ongoing understanding of the individual securities in your portfolio. Please let us know if you would like any help.

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