

August 22, 2007

## Financial Market Turmoil and Fed Market Action

### NABE Conference Call

August 22, 2007

Research  
North America

Morgan Stanley & Co. Incorporated

**Richard Berner**

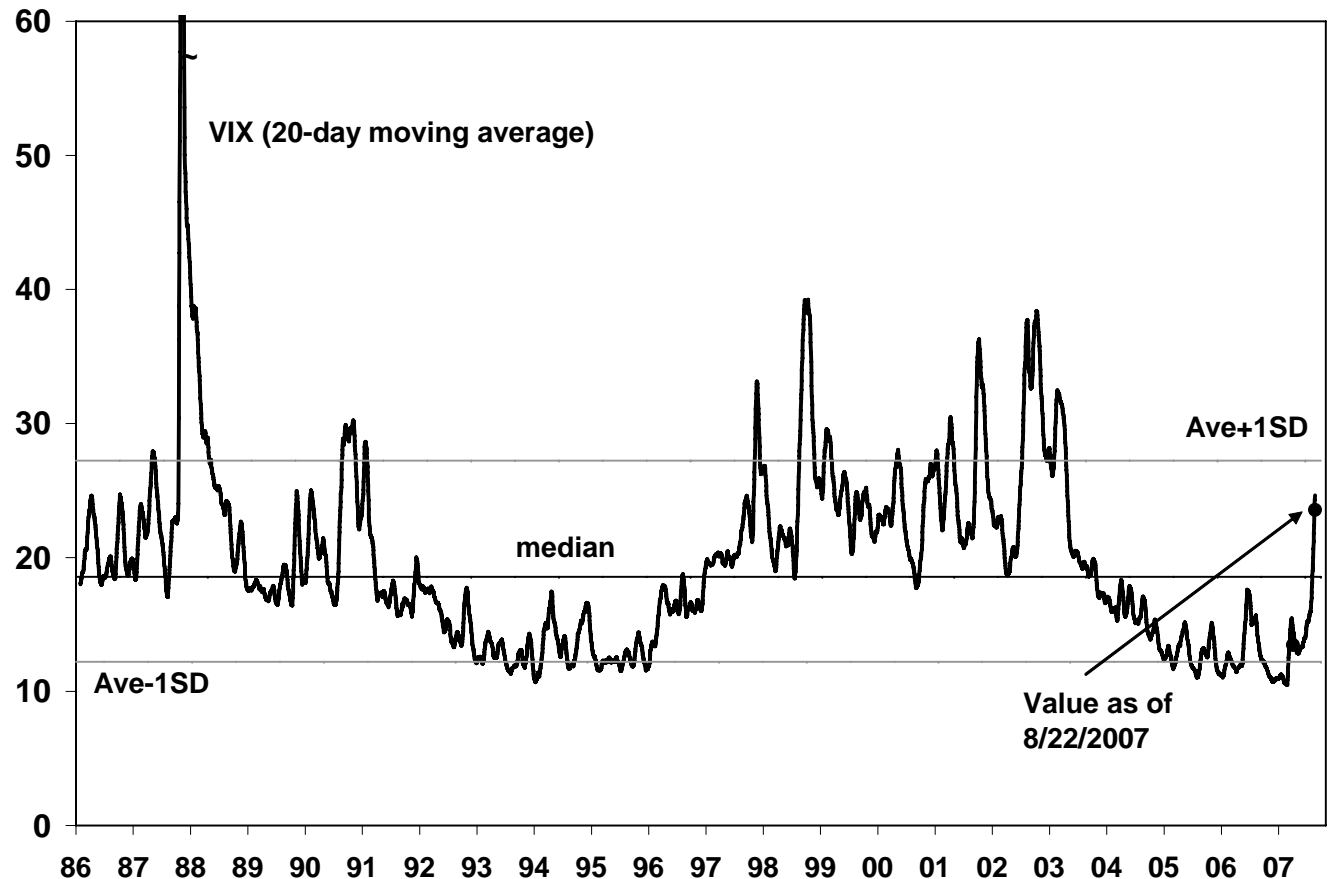
Chief US Economist

richard.berner@morganstanley.com

+1 (1)212 761 3398

## Asset-Market Volatility: Following Fundamentals?

- Secular forces, including Great Moderation, financial innovation
- High “transactional liquidity” – boosted by financial innovation – suppressing volatility
- Low volatility also fueled by cyclical tide of “funding liquidity”
- Selling options to enhance yield the hallmark strategy of the past five years

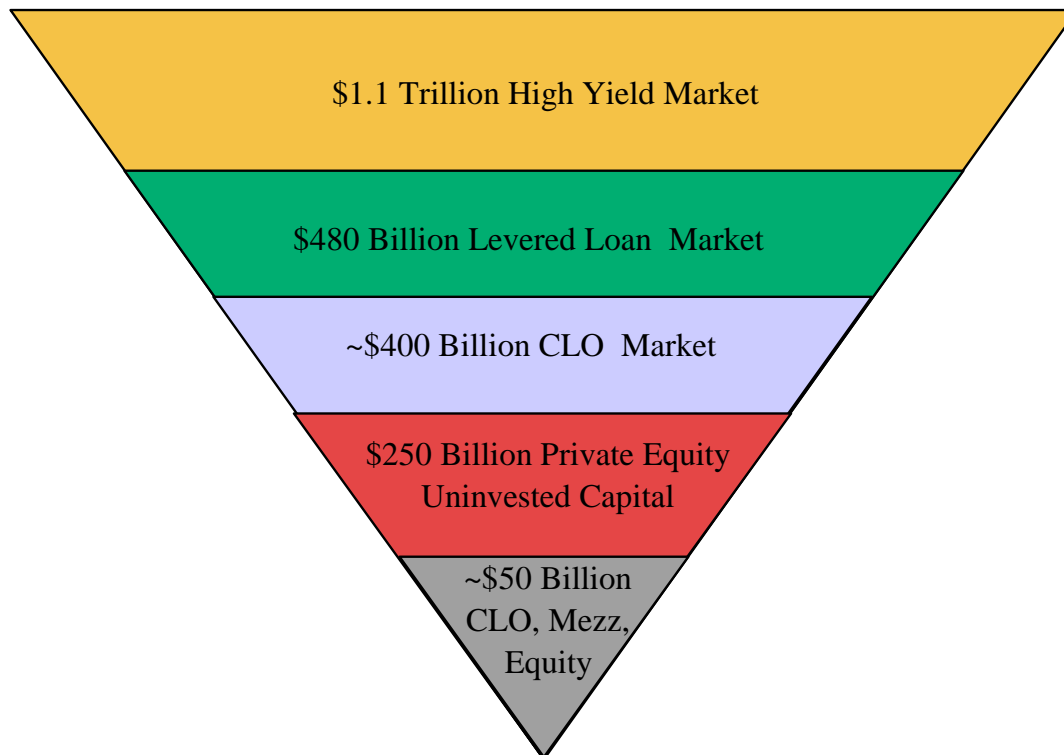


Source: CBOE

Who Puts the “L” in LBO?

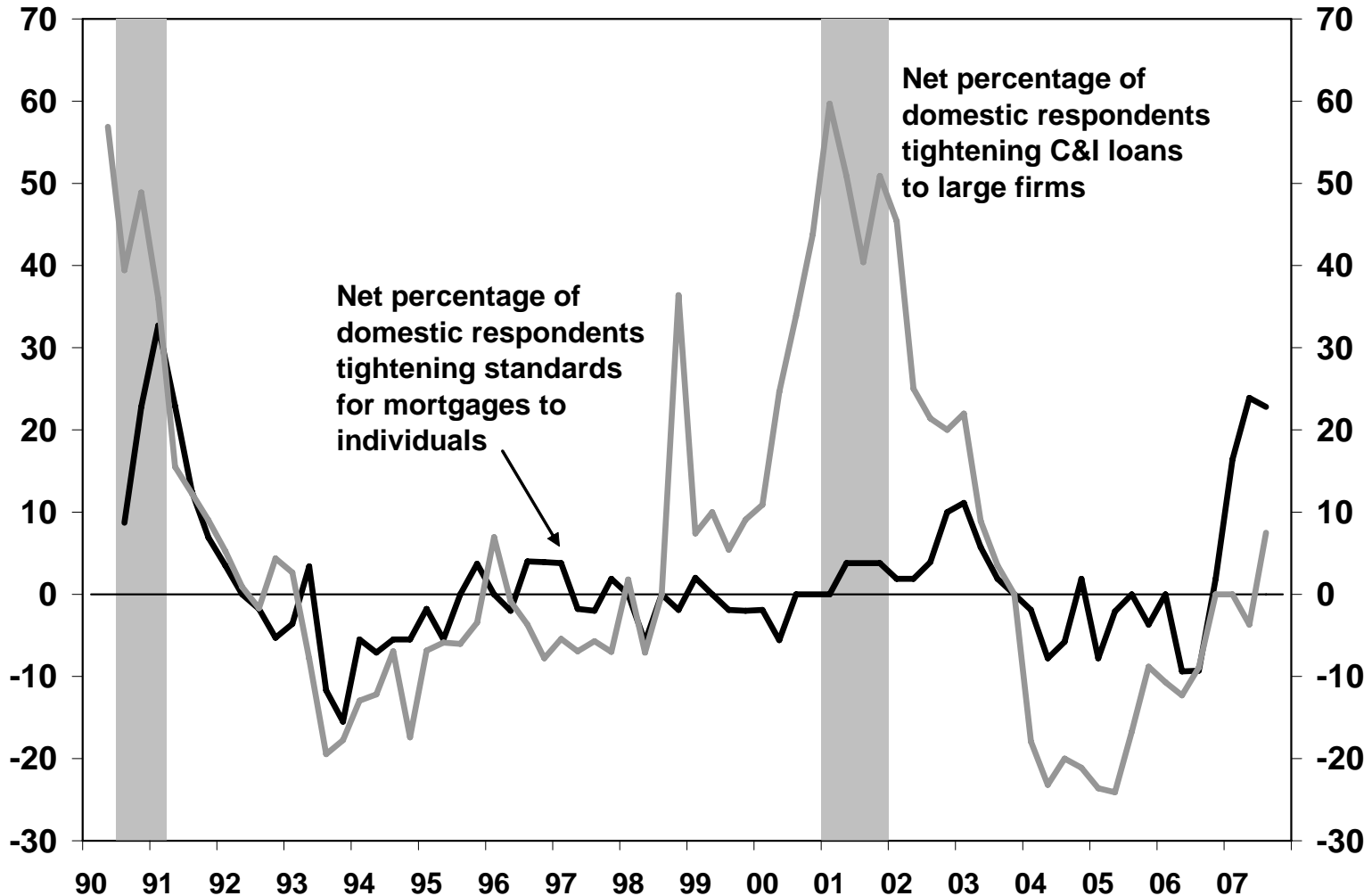
- Much of the “L” in LBOs furnished by leveraged loan market
- CLO market became the primary support mechanism for leveraged loans
- Both US and European CLO portfolios have significant exposure to LBOs
- Risk implications of LBO exposure vary greatly across CLO tranches

Inverted Investment Pyramid



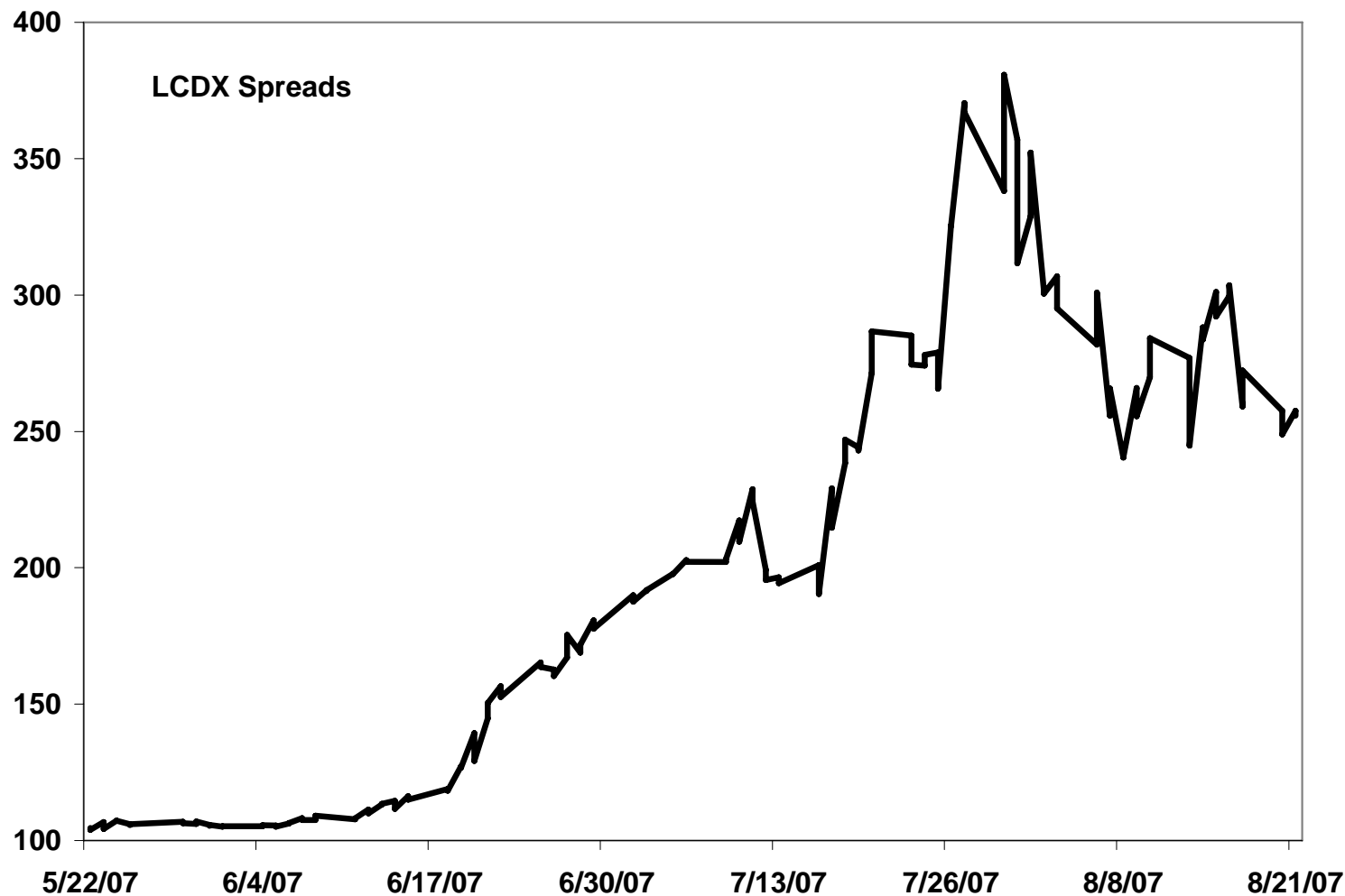
Source: Morgan Stanley

Senior Loan Officers Tightening Standards



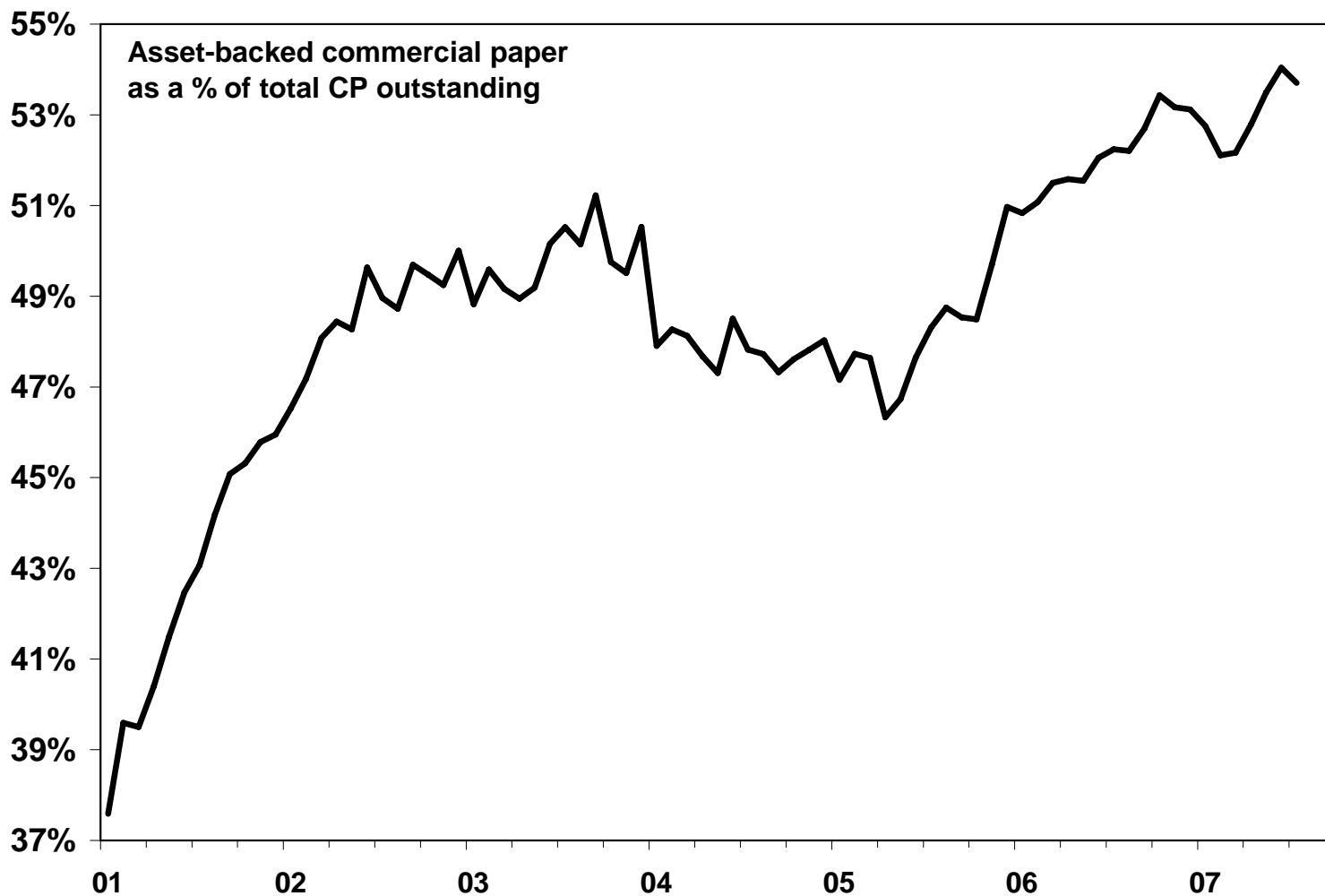
**Note:** 2Q07-3Q07 values for mortgage lending standards are Morgan Stanley estimates.  
**Sources:** Federal Reserve Senior Loan Officer Survey, Morgan Stanley Research

## Risk Spreads Have Widened Considerably



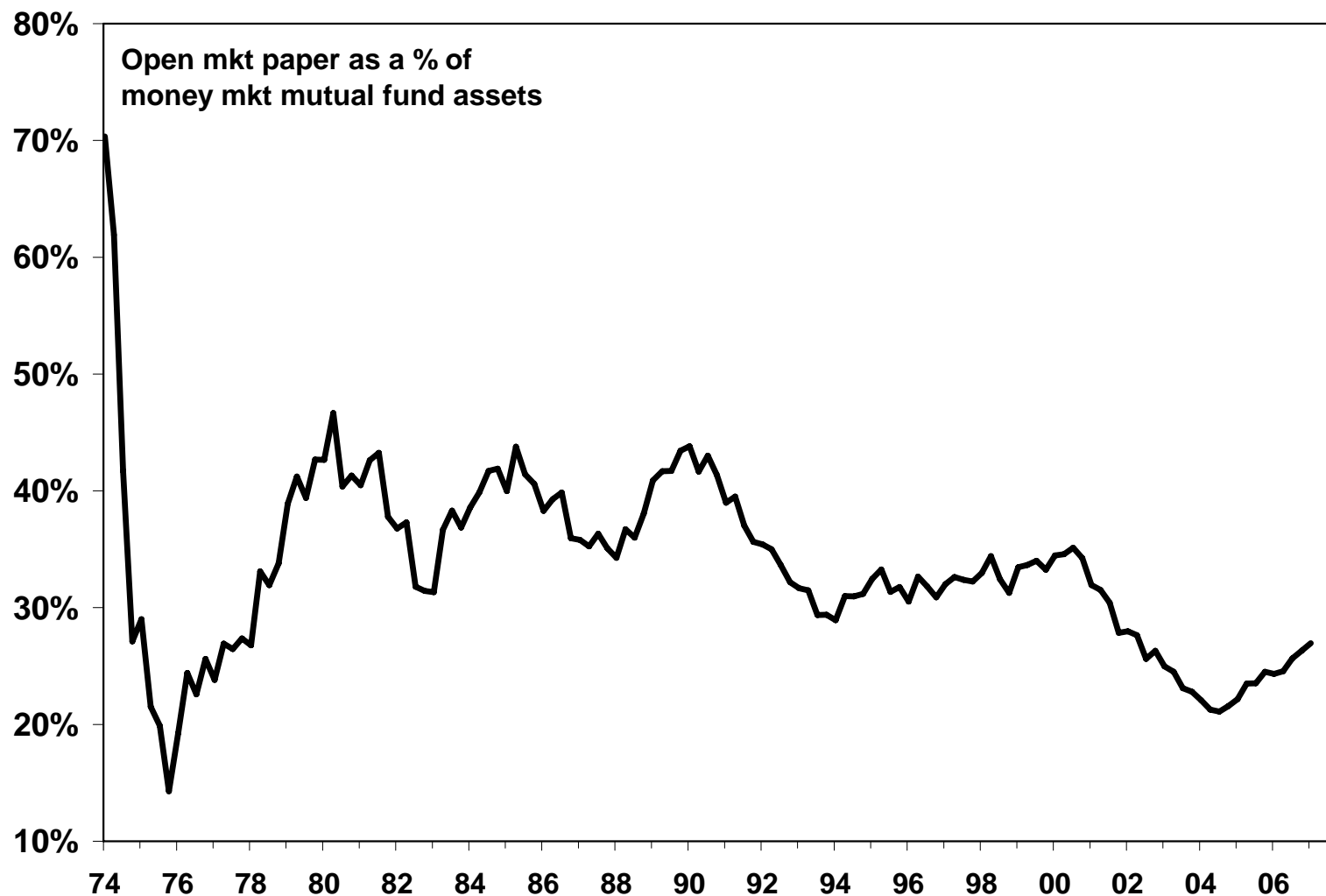
Source: Markit

## ABCP as a % of the Total CP Market Has Grown Dramatically



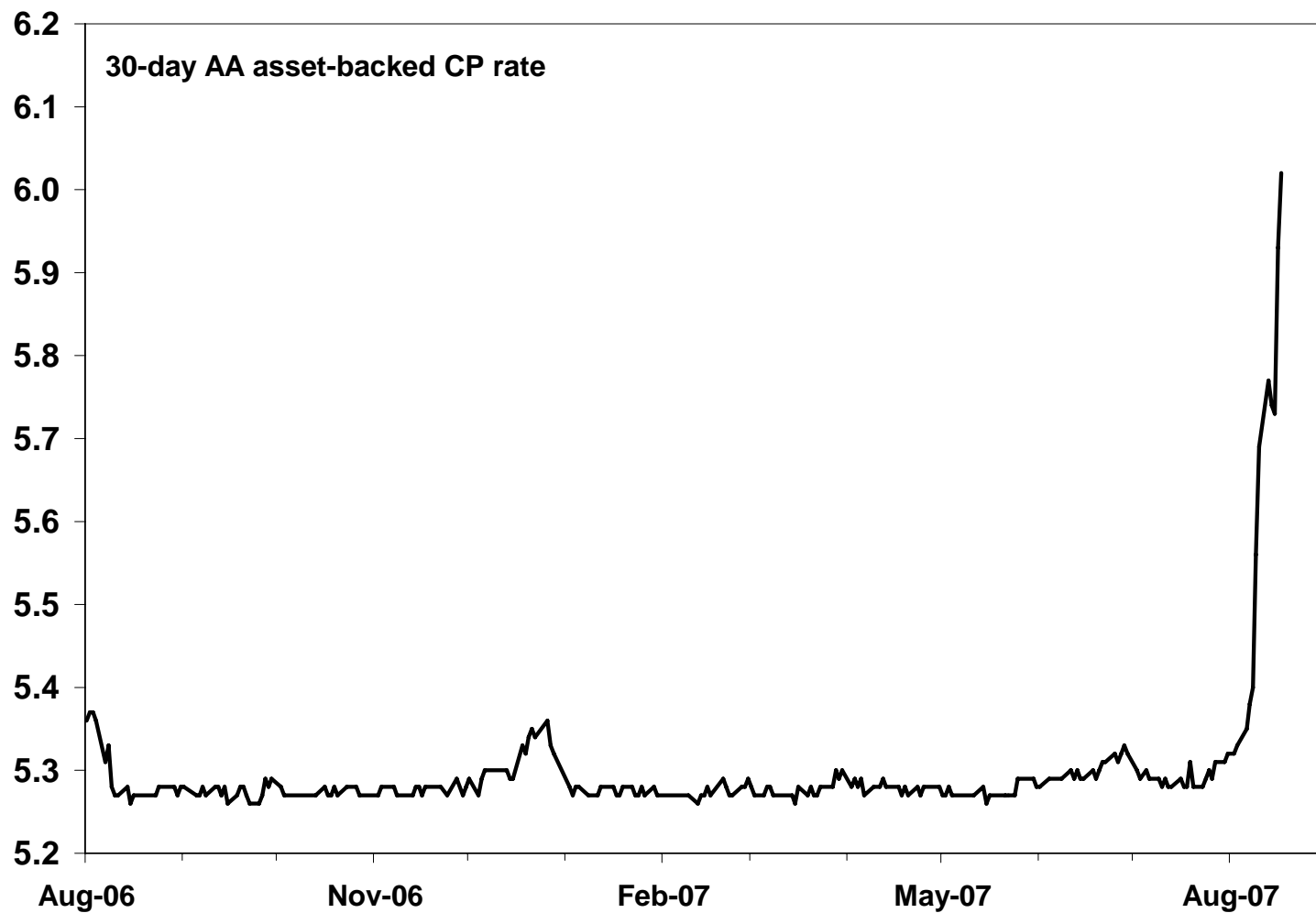
Source: Federal Reserve

## Open Market Paper as a % of Money Market Mutual Fund Assets



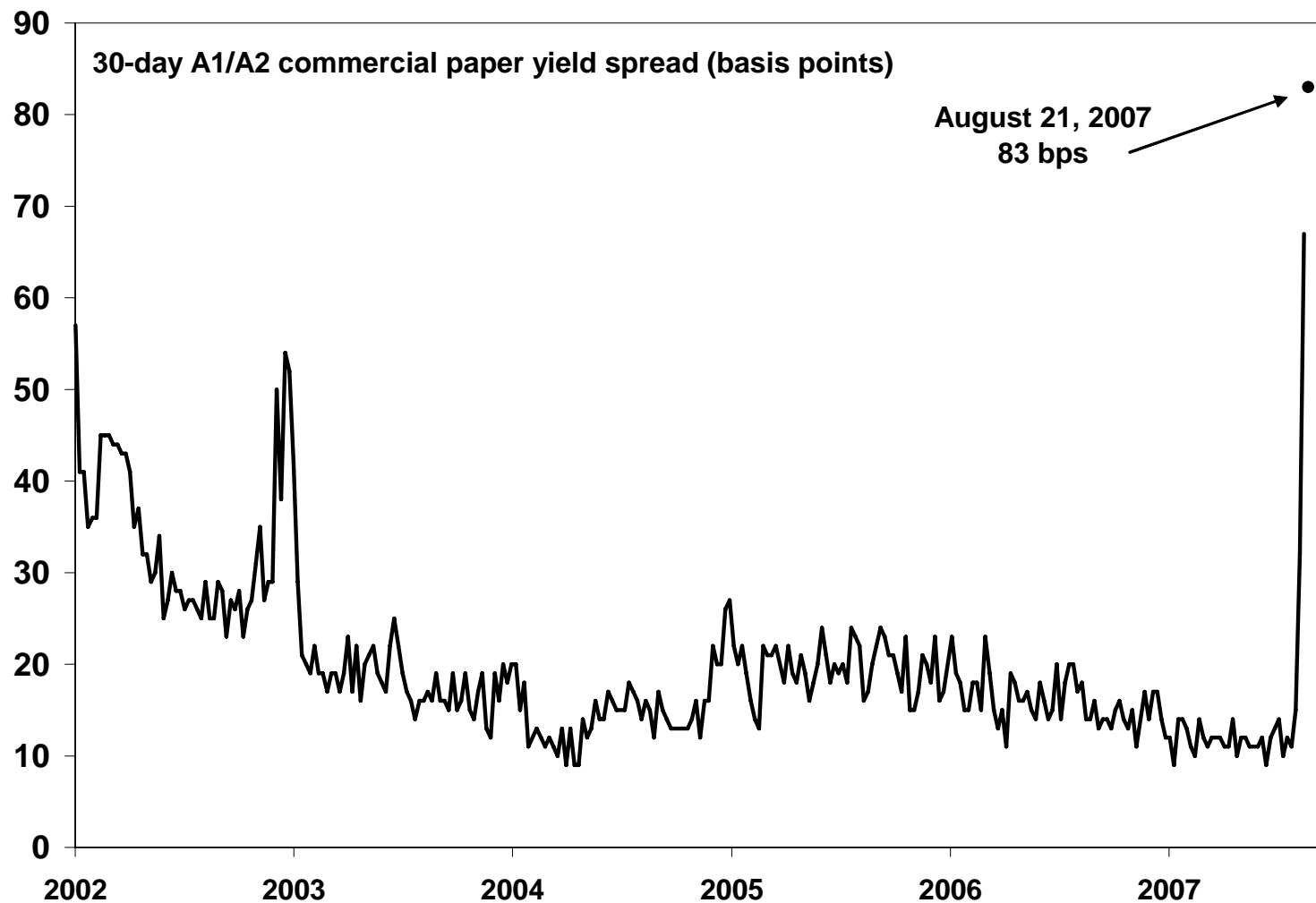
Source: Federal Reserve

## Scramble for Liquidity Pressures Money-Market Rates



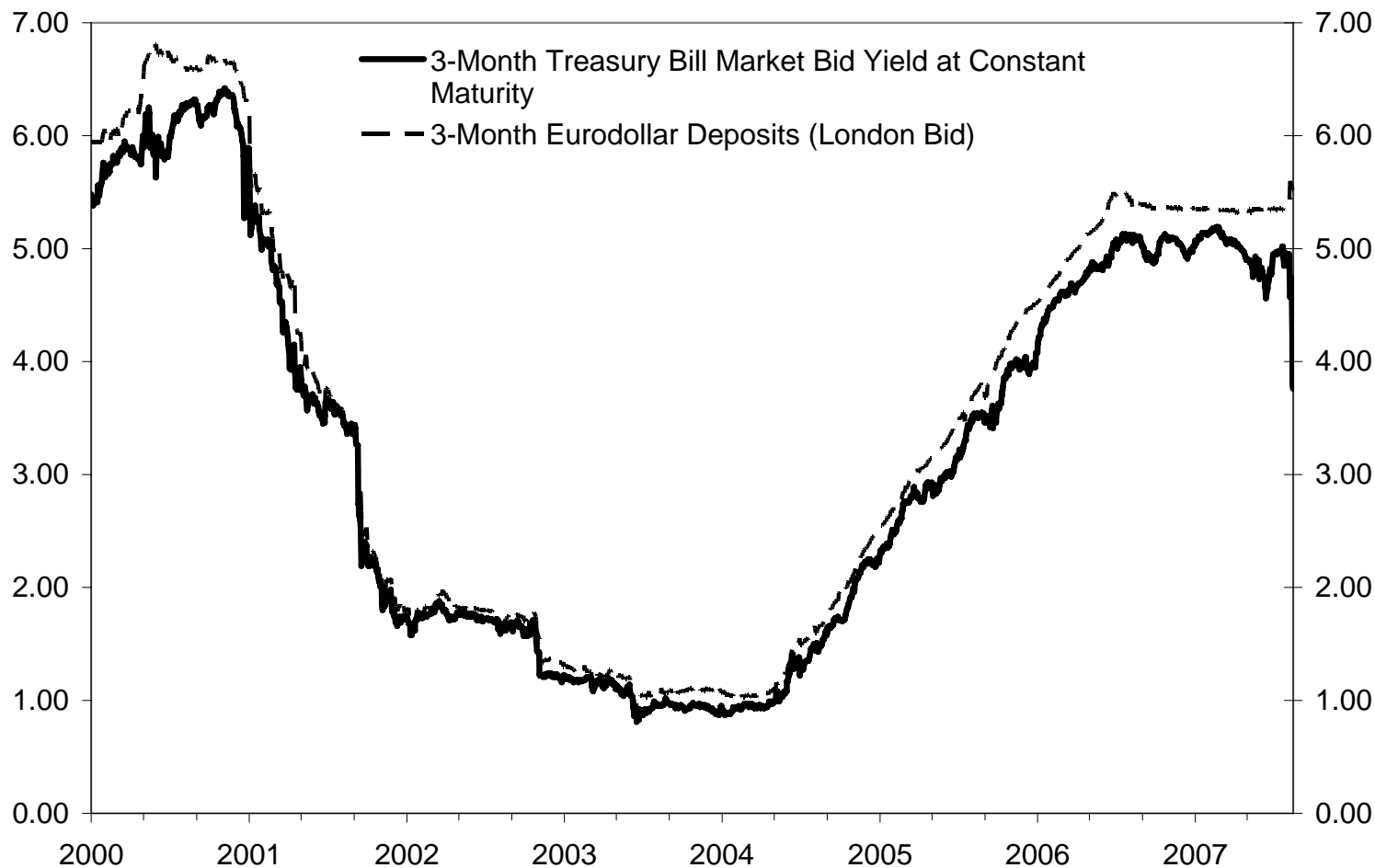
Source: Federal Reserve

## 30-day A1/A2 Commercial Paper Yield Spread



Source: Federal Reserve

### 3-Month Treasury Bill Market Bid Yield / 3-Month Eurodollar Deposits (London Bid)



Source: Federal Reserve; Haver

## Disclosures

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