

Investors Tap Treasuries As Stocks Take Breather

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It was a quiet day on Wall Street yesterday, but these days, quiet is relative.

The stock market was basically flat, but as turmoil in the market for mortgage and other risky assets continued, money gushed into ultra-safe, short-term U.S. government debt, driving down interest rates. The yield on three-month Treasury bills fell to 3.01 percent from 3.76 percent. The decline was its biggest one-day swing since the stock market crash of 1987, according to calculations by Bloomberg News.

That was just one piece of evidence that the financial markets, while apparently calm yesterday, may have only been taking a breather.

"Today was a bit of a pause," said Georges Ugeux, chief executive of the investment bank Galileo Global Advisors. "People reflected on the short-term stability that came about from the Fed's moves and considered what the next move will be."

Ugeux was referring to the Federal Reserve's surprise move Friday to make funds available on more favorable terms to banks, which then drove the market higher. As the markets continued to digest that move yesterday, there was mixed news on what may lie ahead for corporate earnings and the economy.

On the positive side, the home improvement chain Lowe's said its profit rose 9 percent in the second quarter, and while the company cut its forecast for the year ahead, investors had feared an even more negative prognosis. Lowe's closed at \$28.50, up \$1.63, or 6.1 percent.

Investors also seemed to react favorably to news that Treasury Secretary Henry M. Paulson Jr. and Federal Reserve Chairman Ben S. Bernanke would meet privately today with Senate Banking Committee Chairman Christopher J. Dodd (D-Conn.).

"People think the meeting implies there would be some discussion about interest rates, and in this climate, any discussion of interest rates would be about cutting them, not raising them," said David R. Kotok, chairman of the investment advisory firm Cumberland Advisors.

On the negative side, Thornburg Mortgage of Santa Fe, N.M., said it would sell billions of dollars of its most stable mortgages because it cannot raise any of the riskier short-term debt on which it normally relies. Mortgage lender Countrywide Financial of Calabasas, Calif., announced layoffs.

The day's positives and negatives seemed to cancel each other out, leading to a drop in the broad-based Standard & Poor's 500-stock index of 0.39, or 0.03 percent, to 1445.55. The Dow Jones industrial average rose 42.27, or 0.32 percent, to 13,121.35. The technology-heavy Nasdaq composite index rose 3.56, or 0.14 percent, to 2508.59.

The dramatic move in the market for short-term Treasury debt reflected investors' lack of faith in the market for commercial paper, or short-term debt issues by companies. Normally, creditworthy companies can easily take on short-term debt that they use to manage cash needs. Commercial paper is an asset widely held by many money-market mutual funds, for example, which offer stable returns with little risk.

In the past three weeks, however, as part of a broader credit crunch, investors have lost faith in the commercial paper market. They fear that seemingly safe debt issued by stable firms will turn out to have a high risk of

default. Thus, people who would normally buy commercial paper when they want to move money from stocks into an asset that is nearly as safe as cash are instead buying debt issued by the U.S. government.

With more investors demanding the same Treasury bills, the winning bidders are those who will settle for a lower return. The drop yesterday in rates for short-term Treasuries is the latest in a series of declines this month. The yield, or effective interest rate, on three-month Treasury bill was nearly 5 percent at the beginning of August, before falling to its current rate of about 3 percent.