Investment Consequences of Fiscal Austerity and Aggressive Fed Policy

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Consequences of Extreme Policies

IMF Comments:

The U.S. economy would likely grow as much as 2% higher this year if the government were not tightening fiscal policy*

Loosening monetary policy in the United States…could trigger another recession or even deflation**

*Reuters, April 16, 2013

**International Business Times, April 17, 2013

Opposing Extremes

Fiscal Austerity vs. Aggressive Monetary Ease

Or Larger Deficits, Future Crisis

Or Recession, Higher Rates

Slow Growth

Determinants of Policy and Growth

Past Recessions		Recent Recession
Small stimulus →large response	**DEMOGRAPHICS**	Less risk taking, consumption, borrowing
Postponable	**ENTITLEMENTS**	Imminent
Stable, rising value	**HOUSING**	Negative equity, mobility bank costs, jobs
Conventional mortgage Conservative balance sheet	**LEVERAGE**	HEL, LTV, Teaser ARMS, NINJA 30:1, variable financing, structured products
Selective	**BANK CRISIS**	Widespread (leverage, bad loans)
Painful	**STOCK MARKET**	Devastating, changed investment behavior
Cyclical recovery	**JOBS**	Outsourcing, more with less

Policy Standoff

Fiscal Austerity vs. Monetary Ease

Slow Growth

Fear of Rising Rates

Fear of Inflation

What if: Washington Gets Worse?

Fiscal Policy:

Complete Gridlock

Increased Austerity

No Balanced Budget

Recession

Monetary Policy:

Increased QE

Large Balance Sheet

Slow Growth,
with consequences

Investor Consequences:

Equity Rout

High Yield Deteriorates

Safe Havens Perform

Fear of Rising Rates, Inflation

What if: Continued Policy Stalemate

Other Determinants of Growth Prevail

DEMOGRAPHICS

ENTITLEMENTS

HOUSING

LEVERAGE

BANK CRISIS

STOCK MARKET

JOBS

What if: Policy Status Quo with Other Growth Factors

Investing Consequences

Expectations for: Improving Growth	Fear of: QE Reduction, Inflation
Improving Equity Market	Steeper Yield Curve
Sustained Credit Market	Weaker High Quality Bonds
	Safe Haven Demise

What if: Washington Gets Responsible?

If:
Fiscal Policy Initiative

Leadership

Budget Resolution

Tax Reform

Regulatory Clarity

Then:
Monetary Policy Adjustment

Reduce QE

End QE

Raise Short Rates

Sell Portfolio

Stronger Economic Growth

Equities Improve

Credit Markets Perform

Safe Havens Capitulate

Fear of Rising Rates, Inflation

Definitive Risk: Fed Policy

$85 b in perspective

Consequences of QE

Investment Implications

2013: Shifting Investment Rationale

Less Risk:	Europe Asia U.S.
Confidence in U.S. Growth:	Housing Jobs Lending
Avoiding Investment Pain:	Cash Reserves Higher Interest Rates Inflation

Risks to Current Investment Behavior

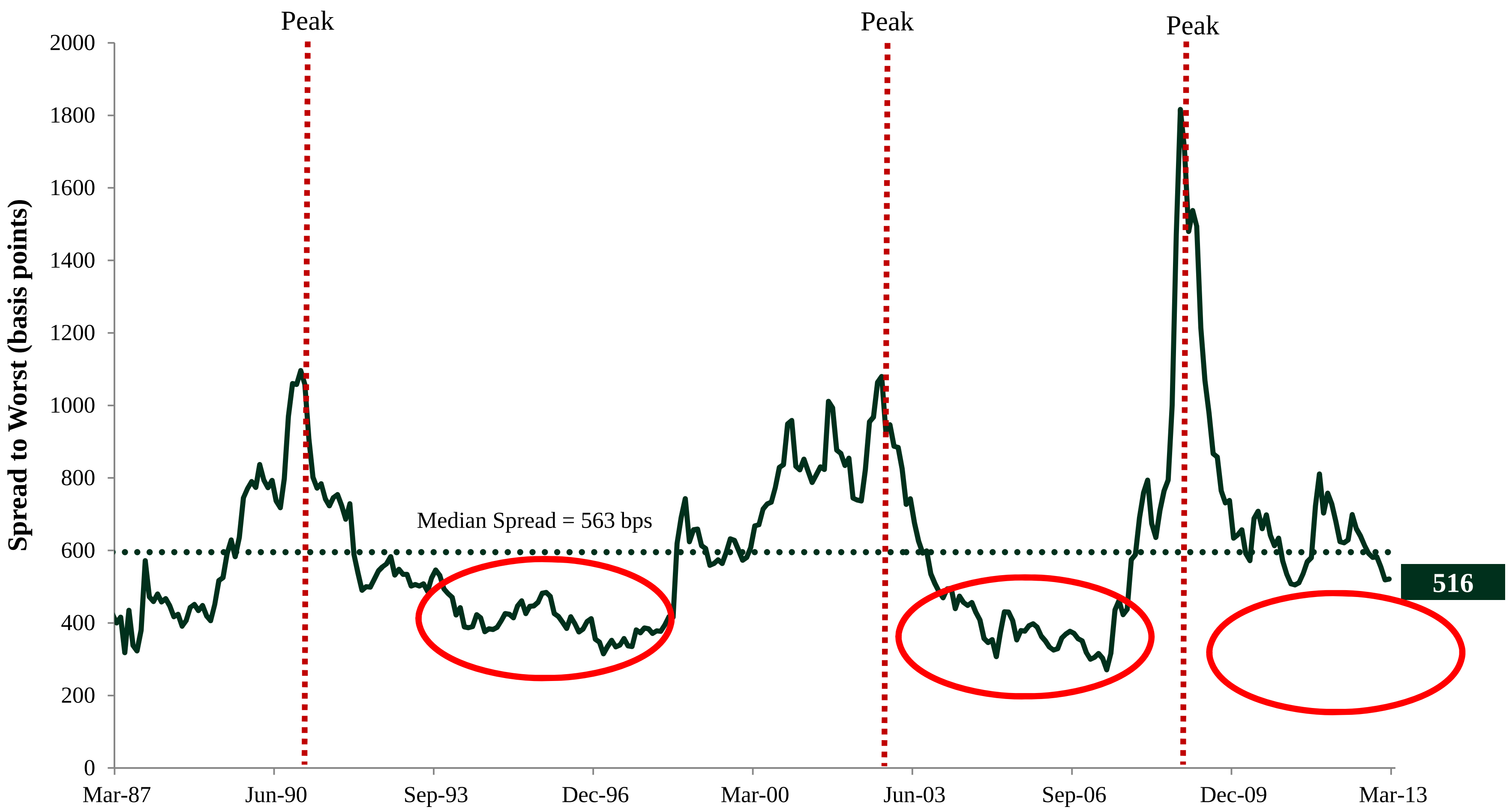
Europe: Recession
Cyprus
Bank Crisis

China: Export dependent
Empty infrastructure
Bad debts

U.S.: Fiscal inaction/action
Inflation
Monetary Policy

High Yield Corporate Bond Spreads

(as of 03/31/2013)



Source: Credit Suisse.

For illustrative purposes only and does not represent any specific Lord Abbett product or any particular investment.

Investment Grade Corporate Bond Spreads

Source: Barclays, *Represented by Barclays Corporate Baa-Rated Bond Index.
Past performance is no guarantee of future results.
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Other Asset Classes During Rising Rates*

Performance in Varying Sectors of the Bond Market

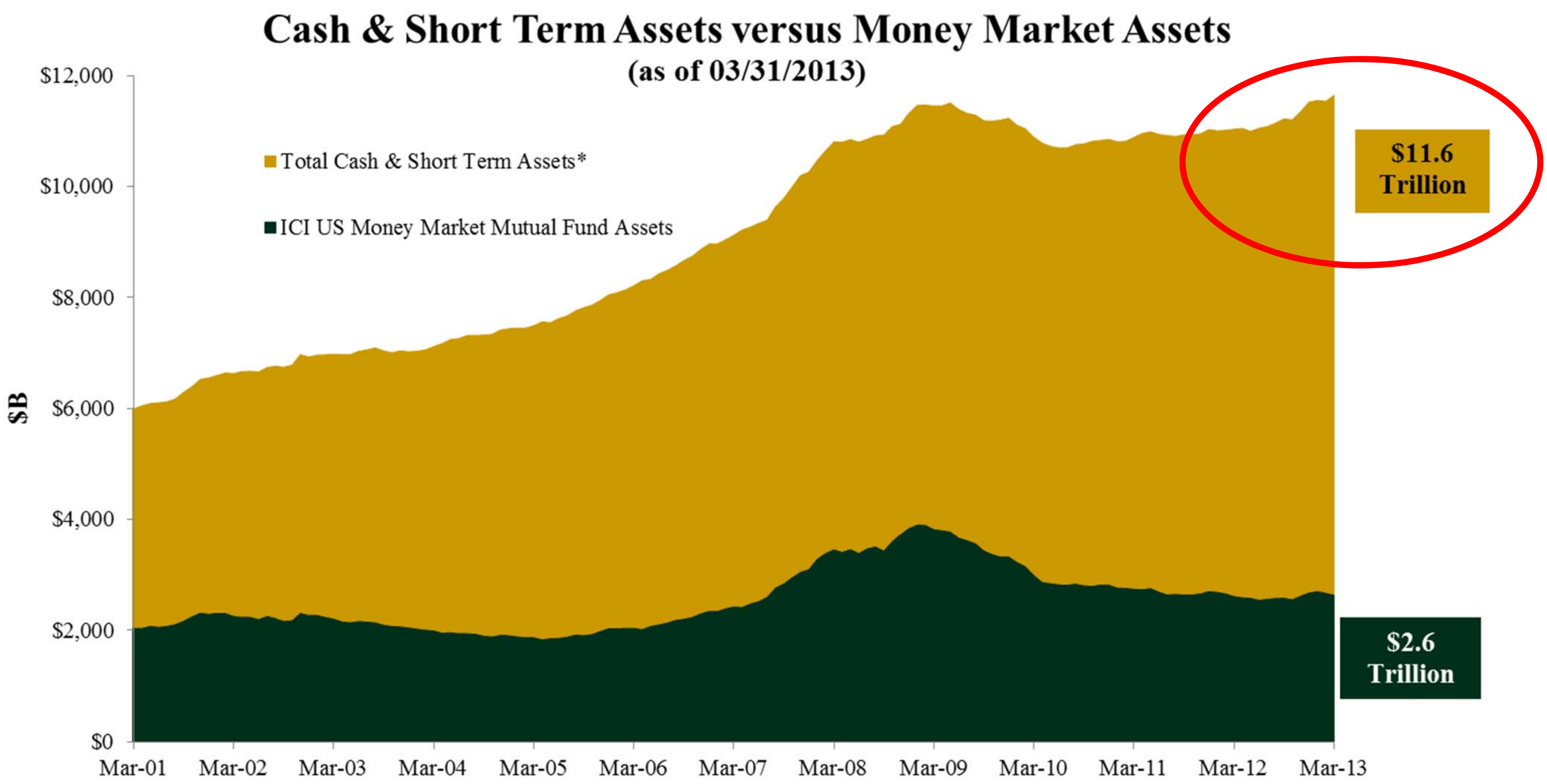
Index	1994	1999	2004 – 2006**
10-Year Treasury	-8.3%	-8.3%	+2.7%
Corporate Bonds[1]	-3.3	-1.9	+3.9
BBB Corporates[2]	-2.6	-0.8	+3.9
High Yield Corporates[3]	-1.0	+2.5	+8.4
1 – 3 Year Corporates[4]	+1.2	+3.9	+2.8
1 – 3 Year BBB Corps[5]	+1.6	+4.7	+3.0
Senior Loans[6]	+10.3	+4.7	+6.2

[1] The BofA Merrill Lynch Corporate Master Index
[2] The BofA Merrill Lynch U.S. Corporates BBB Rated Index
[3] The BofA Merrill Lynch U.S. Corporate High Yield Master II Index
[4] The BofA Merrill Lynch U.S. Coporates 1-3 Yrs Index
[5] The BofA Merrill Lynch U.S. Corporates BBB Rated 1-3 Yrs Index
[6] The Credit Suisse Leveraged Loan Index

Source: Bloomberg, BofA Merrill Lynch, Credit Suisse, and Morningstar.
Past performance is no guarantee of future results.
*Represented as when the Fed Funds rate was rising.
**2004 – 2006 indicates three-year average annual returns.

For illustrative purposes only and does not represent any Lord Abbett product or any particular investment. Indexes are unmanaged and are not available for direct investment.

Cash Balances Remain High



Source: Investment Company Institute data, Federal Reserve, and Bloomberg.
For illustrative purposes only and does not represent any specific Lord Abbett product or any particular investment.
*Total cash and short-term assets include money market assets (ICI), large time deposits, all commercial banks, NSA (not seasonally adjusted), savings deposits, and small time deposits.

Favor: Equity, Credit At Risk: Safe Havens

Investor Perceptions

US Growth Factors

Fed Policy Risk

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