

Corporate Trust Connection

Spring 2002

Welcome to U.S. Bank Corporate Trust Services

All of us at U.S. Bank Corporate Trust Services would like to welcome former Firststar Corporate Trust customers to the U.S. Bancorp family. We're thrilled to have you on board and to offer you an expanded array of products and services. And, you can expect the same level of outstanding service from the same great people you've come to know.

Five Star Service Guaranteed

As part of our integration, we've incorporated the Five Star Service Guarantee philosophy you're already familiar with. The U.S. Bank Corporate Trust Services Five Star Service Guarantee states:

- Your primary contact will be knowledgeable and



take responsibility for your relationship.

- We will respond to inquiries by the end of the next business day.
- We will provide timely and accurate statements and bills.
- We will process payments in a timely and accurate manner.
- We will process routine security transfers within 72 hours of receipt.

If U.S. Bank Corporate Trust Services fails to meet the required level of service in any of our five service

guarantee categories, we will pay you a minimum of \$25.

Coming Up

Because of the unique nature of the corporate trust business, the Corporate Trust Services integration was completed as of Jan. 1, 2002. Other Firststar offices will assume the U.S. Bank name throughout 2002, so you may notice the change gradually over the next several months.

Be sure to visit usbank.com/corporatetrust for more information. If you have questions about any of our products and services, please contact your Account Manager. He or she will be available at the same phone number as always.

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Did You Know...

During 2001, U.S. Bank Corporate Trust Services continued its mission to provide you with the best selection of products and services available in the most convenient and effective method possible. Some of these accomplishments include:

- Adding three new locations (Cincinnati, Milwaukee and St. Louis) to our roster of offices, providing you with easy, local access to your Account Manager.
- Providing Stock Transfer Services and expanded Escrow Services to our product offerings.
- Introducing U.S. Bank SPANS Online, our state-of-the-art Internet reporting and processing system for commercial paper and medium-term issuing and paying agency clients.

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Five Star Service Guaranteed

2001 *Looking Back*

Reflecting on the past is normally an opportunity to celebrate our successes and resolve to learn from our mistakes. Of course, 2001 was not just any year. It will be remembered primarily as the year the United States was struck by the most devastating terrorist attack in history.

Although the economy was sluggish prior to the attacks, the downturn may not have been severe enough to qualify as a recession. However, the aftermath of Sept. 11 – including the pummeling of the travel industry and increased layoffs – helped push the economy into recession. Tracing back to the beginnings of the downturn, the National Bureau of Economic Research declared that the recession had begun in March, ending the country's longest economic expansion ever.¹

The positive news is that the work of the country

continues and there are signs that a recovery is in progress.

Interest Rates: How Low Can They Go?

In an effort to stimulate the faltering economy, the Federal Reserve Board lowered short-term interest rates an unprecedented 11 times

yields temporarily as prices rose (see chart).

Lower consumer loan rates, coupled with 0% financing promotions by car companies, helped fuel consumer spending and limited the depths of the recession. In October, retail sales surged 7.1%.² However, the

longest stretch since the Great Depression. Inflation remains benign, with the Consumer Price Index rising just 1.6% for the 12-month period ending in December.³

Closer to Home...

Throughout the year, U.S. Bank Corporate Trust Services worked diligently on its integration with the former Firststar Corporation into U.S. Bancorp. In the fall, we unveiled our Five Star Service Guarantee. The past year brought many challenges and opportunities, and we held steadfast in our commitment to bring you the best possible service and solutions to your financing needs. We would like to take this opportunity to thank you for your past business and support.

The following lists the 52-week highs and lows, as of Dec. 31, 2001, based on Merrill Lynch Bond indexes published in The Wall Street Journal:

	High	Low
Treasury 10+ year	5.94%	4.83%
Corporate 10+ year High Quality	7.31%	6.27%
Tax-Exempt 12-22 year (AA)	5.32%	4.67%

in 2001. The federal funds rate – the rate banks charge each other for overnight loans – dropped from 6.0% on Jan. 3 to 1.75% by Dec. 11, the lowest since 1961.

In addition, the Treasury Department's announcement that it was discontinuing the issuance of 30-year bonds helped push down bond

Conference Board's Consumer Confidence Index fell in November, reflecting consumers' unease about rising unemployment and layoffs (unemployment rose to 5.8% in December; its highest level since Aug. 1995³).

Industrial output fell for the 13th month in a row by 1.1% in October; the

¹ Source: National Bureau of Economic Research, in a statement released Nov. 26, 2001; www.nber.org.

² Source: *Business Week*, Dec. 3, 2001.

³ Source: U.S. Department of Labor, Bureau of Labor Statistics, www.bls.gov.

Fallout for the Bond Market

The Demise of the 30-Year Treasury

The bond market got a Halloween surprise from the U.S. Treasury Department. On Oct. 31, 2001, the agency announced it would no longer sell 30-year Treasury bonds. Whether the maneuver was a treat or a prank depends upon your perspective, but it sparked the largest price change for the bonds in over a decade. The long bond ended the day up 5½ points, or

\$52.81 for a bond with a \$1,000 face value, to close at 107½. Yields plummeted to a three-year low, 4.88%.*

"When the Treasury Department made its announcement, the 30-year bond had its biggest one-day price gain ever, and the entire bond market rallied for about two weeks," says Keith Hembre, U.S. Bank director, economic research and fixed income risk management. Around the middle of November, though, releases of new economic data sent the market back in the other direction. "We saw a

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Looking Forward 2002

Predicting what will happen to the economy is a lot like forecasting the weather. You can make an educated guess based on prevailing conditions, but you never know when the winds will change.

Nonetheless, there are positive signs. The Asset Management group of U.S. Bank is anticipating a positive economic environment in 2002. The Bond Market Association, in its annual forecast, is calling for the economy to contract in the first quarter, begin recovery in the second and accelerate in the third and fourth quarters.¹

What Could Help

Positive indicators for recovery include:

Continued low inflation. As of December 2001, inflation as measured by the Consumer Price Index had risen at just 1.6% on an annualized basis.² Forecasts call for an increase of 2.0% in 2002.¹

Interest rates. The Fed's aggressive action in lowering short-term interest rates may begin to have an effect on businesses, encouraging borrowing and expanding.

Federal spending. The government has approved additional federal spending on defense and security, as well as aid to industries adversely affected by the terrorist attacks.

Low energy prices. A drop in the price of oil due to lower demand has resulted in lower gas and oil prices. It's been estimated that consumers may save nearly \$50 billion in heating costs this winter over last year.³

Tax cuts. Although the rebate checks distributed last year had a smaller impact on consumer spending than anticipated, lower tax brackets may leave more discretionary money in consumers' pockets and have a greater impact this year.

Reduced inventory. The large-scale decline in inventories that occurred in 2001 should help stimulate production.

What Could Hurt

Some of these factors are double-edged swords. If low interest rates begin working too well, for example, it could trigger inflation. Other areas that potentially could limit the intensity of the recovery include:

Oil supply. If conflict escalates in the Middle East, oil supplies could be curtailed, causing price spikes at home.

Consumer confidence. Another terrorist strike could undermine any gains made in consumer confidence. It could also contract business travel even more, further damaging an already troubled travel industry.

Unemployment and layoffs. More news like the Enron bankruptcy can keep worried workers from spending cash. In addition, the unemployment rate rose to 5.8% in December² and is expected to reach 6.1% in 2002.¹

Global economics. Since global economic activity remains weak, export activity may be challenged. Negative growth is forecast for Japan and weak growth as well as a depressed value for the euro in Europe for 2002.

What About Bonds?

Flight to quality in the bond market pushed rates lower temporarily, but by mid-December, yields were up significantly from their lows. Any inflationary pressures that may be felt in 2002 could cause rates to drift higher.⁴ The federal budget deficit, which will cause the government to borrow more, will also have an impact. The Bond Market Association expects issuance in the Treasury market to rise, particularly on the short end, in 2002. It also expects issuance in the municipal market to remain strong – totaling about \$250 billion – largely as a result of



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declining revenues.⁵ Corporate issuance, however, is expected to decrease, while asset-backed issuance increases.

Regardless of what 2002 brings, you can be assured that U.S. Bank Corporate Trust Services stands ready to help you find solutions to your financing concerns. Visit us at usbank.com/corporatetrust, or call your Account Manager.

¹ Source: "The Economic Outlook: Economic Recovery Expected to Begin in Second Quarter 2002," The Bond Market Association, www.bondmarkets.com.

² Source: U.S. Department of Labor, Bureau of Labor Statistics, www.bls.gov.

³ Source: *Business Week*, Dec. 3, 2001.

⁴ Source: *Institutional Investor*, November 2001.

⁵ Source: *The Bond Buyer*, Dec. 26, 2001.



The Demise of the 30-Year Treasury... *continued from page 2*

reversal of the entire gain caused by the Treasury announcement," Hembre says.

Reasons for the Decision

Treasury officials maintain that they suspended issuance of 30-year bonds simply because they're no longer needed to pay off the national debt. Analysts note, however, that the move has the direct effect of cutting long-term interest rates – a goal that has eluded Alan Greenspan and the Federal Reserve Board.

Eliminating sales of the long bond should increase demand for 10-year Treasury notes, which help

determine mortgage rates. The resulting lower yields on 10-year notes and lower mortgage interest rates will help stimulate economic activity. Many homeowners will refinance their mortgages and end up with more cash in their pockets rather than locked up in home equity.

At the same time, the government lowers its borrowing costs. To entice investors, long bonds had to carry a higher interest rate than shorter-term bonds. The federal budget is swinging from a surplus back into a deficit, so there will be an increase in federal borrowing. Uncle Sam just won't have to pay as much per dollar borrowed.

Impact on the Bond Market

Hembre believes the Treasury's move will not affect the bond market in the coming year. "Ultimately, bonds are going to reflect fundamental values," he says. "The supply and demand for money plus interest rate expectations are the factors that influence bond yields and prices.

"There are sometimes temporary distortions in the market as a result of announcements like the one on October 31, but then yields and prices move back to their fundamental values.

"At any particular maturity for a bond – two-year, five-year or 10-year – the yield reflects the fact that there are an equal number

of people on each side of the deal who think that rates will either go up or go down. The current yield is the balance that equates buyers and sellers," Hembre explains.

The Fallout

The 30-year Treasury was considered an important benchmark for the bond market. Corporate bond issuers often considered the long-bond yield when making decisions about their bond issues. Hembre notes that, "It may take some time for the market to sort out what it will use as a benchmark for 30-year maturities."

* Source: *The Wall Street Journal*, Nov. 1, 2001.

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Some banks promise great service, but U.S. Bancorp will guarantee it. Our exclusive Five Star Service Guarantee incorporates the performance standards that reflect our customers' expectations for quality, responsiveness, accuracy and availability. If we fail, we make good on our commitment by crediting the customer's account a set amount – proof positive that we mean what we say.

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Comments and suggestions for the newsletter are welcome and should be forwarded to Kathleen Engesser, Marketing Manager, U.S. Bank Corporate Trust Services, (651) 244-8440 (phone) or kathleen.engesser@usbank.com (e-mail).

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