



## Bond Market Weekly

Week of March 30, 2009 | Municipal and Corporate Review

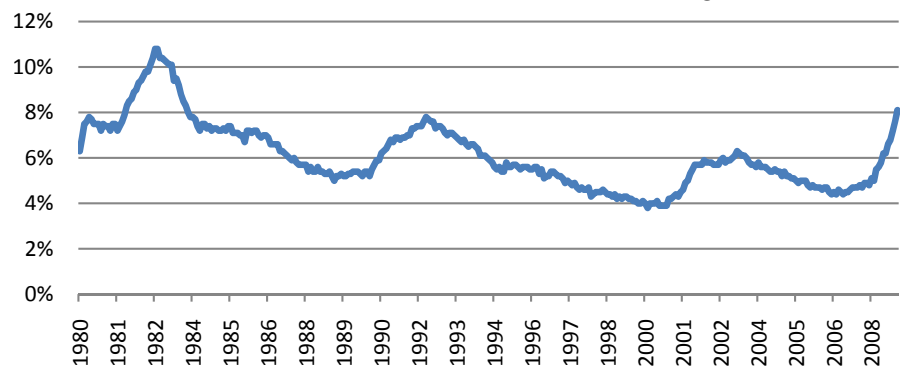
Page 1 of 2

### Market Overview

- ❑ Treasury gains on news of Fed purchases retraced slightly last week as the benchmark 10-year note rose 12 bps to 2.76%. An announcement last week of the Fed's intent to also purchase long maturities surprised the market and helped 30-year Treasuries to outperform. 2- to 10-year Treasury spreads rose 8 bps to +185, while 2-to 30-year spreads fell 9 bps to +270 on the news.
- ❑ The Fed's actual Treasury purchases totaled \$15 billion during the week and represented a small offset to the \$98 billion in new supply of 2, 5 and 7-year maturities.
- ❑ Treasury announced a Public-Private Partnership Investment Program (PPIP) to rid bank balance sheets of "legacy assets". While not much impact was seen in the Treasury market, risky assets including equity, corporate and mortgage assets did see widespread gains.
- ❑ TIPS continue to perform well and, as a result, moved the current 5-year horizon breakeven 31 bps higher to 0.98%. The 5-year, 5-year forward measure rose just 7 bps to 2.02%. We should note that the indicative nature of investor sentiment extracted from Treasury and TIPS markets has now been compromised by the Fed purchase program. While relative value extraction remains possible, using the yield data as indicator will be challenging given the Fed's manipulation.
- ❑ A steady flow of better than expected economic data continued last week, albeit at depressed levels. Existing and new home sales (+5.1% and +4.7% MoM Feb, respectively) along with durables goods orders (+3.4% mom Feb) were much better than expected. Many economists suggests that an unsustainable collapse in activity post-Lehman's collapse is now giving way to inevitable rebound. How long activity can continue to improve in the face of 8%+ unemployment will be telling. That rate is estimated to rise to 8.5% in the March survey due out Friday. Nonfarm payrolls are expected to record a loss of 660,000 jobs in March.

### US Unemployment Rate Total (MoM)

3/30/1980-3/30/2009; Source: Bloomberg



### Tax Exempt Markets

- ❑ Municipal bonds performed well in a week of massive issuance with yields on 10-year municipals falling 2 bps.
- ❑ The name of the game last week was new issues beginning with the much anticipated California GO deal. What began as a \$4 billion issue was quickly upsized to \$6.54 billion on the back of strong demand from both retail and institutional investors as yields on the long end were over 6% and enticed many from the sidelines.
- ❑ New issues totaled \$12 billion last week. Most were well received by investors with many deals being tightened by the time they were priced. Total visible supply has now fallen to roughly \$12 billion according to the Bond Buyer 30-Day Visible Supply Index.



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Page 2 of 2

### Tax Exempt Markets

- ❑ This week the wave of new deals will continue with \$352 million from Energy Northwest in Washington and \$375 million from Cornell University. With strong retail demand the deals should do reasonably well despite the continued large amount of supply in the market.
- ❑ Individuals continued to put money into the municipal bond market with \$887 million inflows for the week ending March 18<sup>th</sup>, according to the Investment Company Institute. So far in 2009 roughly 65% of the outflows at the end of the last year have been replaced, according to Municipal Market Advisors.
- ❑ In budget news, the New York MTA approved rate increases last week on subways and buses in order to plug a \$1.2 billion deficit. Rates will increase as high as 30% in some cases and many positions will be cut in order to bring revenues in line with expenses.
- ❑ Berkshire Hathaway Assurance Corp. (BHAC), the only remaining AAA bond insurer by all ratings companies, was put on negative watch last week by S&P due to the weakened financial profile of the parent company. This notice supports the idea of many in the market is that bond insurance may never be AAA. This supports that credits that will be enhanced in the future will tend to be BBB and A rated credits in riskier sectors, potentially weakening the financial profiles of the bond insurers in the long run.
- ❑ Like most market participants last week our focus was mainly on new issues. We purchased new deals for the DC Airport Authority, Peoria, IL, Maricopa County, AZ and the Oregon Lottery deal.

### Taxable Markets

- ❑ Last Monday's announcement by the Treasury to initiate the PPIP and expand the Term Asset-Backed Securities Facility (TALF) gave a boost to the mortgage securities market as it seeks to draw new capital into the markets. One aim of these programs is to provide massive support for mortgages which resulted in MBS outperforming Treasuries. The option-adjusted spread of the Barclays Capital U.S. MBS Index tightened 6 bps to +102 OAS. This market was also lifted by diminishing momentum in the Senate for a cram-down provision of the HR 1106 bill and an unexpected rise in January housing prices. The total return for the MBS Index is up 2.08% YTD.
- ❑ Corporates were up on the week, lifted by the news of the PPIP's benefit to the financial sector. It remains to be seen if the price at which banks are willing to sell assets will align with the price at which buyers are willing to pay, but the incentives placed by the Treasury to facilitate the two were viewed positively by the market. Spreads improved in the financial sector by 9 bps to +760 OAS and overall brought the Barclays Capital U.S. Corporate Investment Grade Index 6 bps tighter to +540 OAS. The total return for this Index is down 1.86% YTD.
- ❑ Corporate new issuance continued to be strong with \$34.6 billion of new debt priced including \$14 billion backed by the FDIC.
- ❑ Agencies were unchanged on the week with the spread of the Barclays Capital U.S. Aggregate Agencies Index at +78 OAS. The total return for this Index is down 0.46% YTD.