



Bond Market Weekly

Week of April 6, 2009 | Municipal and Corporate Review

Page 1 of 2

Market Overview

- ❑ 10-year treasury yields rose 13 bps last week from 2.76% to 2.89% on expectations of increased supply which offset the prior week's announcement that the Fed would buy long-term Treasuries. The stock market rebounded nearly 8% from Monday's low of 7,437 to close above 8,000 on Friday.
- ❑ The Fed is planning to purchase Treasury notes maturing from 10 to 17 years today as part of the \$300 billion program intended to drive consumer rates lower and stimulate the mortgage and other lending markets. Also, the Treasury will sell \$59 billion in notes this week.
- ❑ Freddie Mac announced that the rate on 30-year fixed-rate mortgages fell to 4.78% last week, lowest since the FHLMC was formed by Congress in 1971. This rate, which does not include up-front points charged to the borrower, is for conforming non-jumbo loans. In the wake of the Fed's announced and actual Treasury purchases, Fed Chairman Bernanke pointed to the lower mortgage rates stating the drop may help improve the housing market.
- ❑ TIPS returned 6.1% in the month of March – best monthly performance since the Treasury began selling the inflation-linked notes in 1997. Demand for TIPS has been strong this year as concerns mount that policy makers will struggle to control inflation once global economies begin growing again. The Treasury plans to sell \$6 billion in 10-year TIPS this week.
- ❑ The U.S. unemployment rate rose to 8.5% in March as 663,000 jobs were reported lost for the month, which was in line with analysts' estimates and not as severe as some economists and traders feared.
- ❑ 1Q09 corporate earnings, the controversial "stress test" of U.S. banks' capital ratios and balance sheet stability announced by Treasury Secretary Tim Geithner will be closely-watched by the markets in April. The stress tests, which are expected to reveal which banks might require additional capital infusions – either via TARP, or private investors, in conjunction with the recently-announced PPIP legacy asset auction plan, have the potential to set the tone for the entire bank and finance sector, if not the capital markets in whole, for the remainder of the year.

Tax Exempt Markets

- ❑ Municipal bonds performed reasonably well last week with yields on 10-year municipals falling 5 bps to 3.44% significantly outperforming 10-year Treasuries whose yields rose 13 bps for the week.
- ❑ New issue supply was steady last week but did not reach the levels of the previous week. The Bond Buyer 30-Day Visible Supply Index stayed steady at around \$12.5 billion. New deals this week include \$550 million for Fairfax County, Virginia, \$433 million in NYC GO's which includes a taxable and tax exempt portion and \$400 million for the state of North Carolina.
- ❑ Selling pressure for taxes has not been evident in any great degree. With only nine days left before taxes are due the selling pressure is much more muted than in previous years. Retail demand remains high with the Investment Company Institute reporting tax exempt mutual fund inflows of \$711 million for the previous week, a 12th consecutive week of inflows into municipal bond funds.



Bond Market Weekly

Week of April 6, 2009 | Municipal and Corporate Review

Page 2 of 2

Tax Exempt Markets

- ❑ The state of Illinois was, unsurprisingly, downgraded last week to A1 stable from Aa3. The downgrade, like S&P's, was due to the continued deficits at the state level. Illinois is one of the few states that is not required to balance its budget. On the positive side the state has a virtually unlimited ability to raise taxes on Illinois residents.
- ❑ We were relatively quiet last week digesting many of the new deals from the previous week. We focused mostly on specialty state items and investing new and existing cash in portfolios.

Taxable Markets

- ❑ The FASB gave a boost to taxable markets with changes to accounting rules regarding fair value of assets and the impairment of securities. While last week's PPIP announcement incorporates leverage in an effort to lift prices for securities and loans on the balance sheet of banks, the easing of mark-to-market accounting gives the financial entities more discretion on realizing losses and their need to sell.
- ❑ Agencies improved again last week as the FASB changes were seen as positive for the housing related government-sponsored agencies. If the fair value of assets can be priced higher and reverse some of the MTM losses, the GSEs stand to see improved capital levels. Another positive for the market stems from technicals. Total net issuance collectively for FNMA, FHLMC, and FHLB has been -\$69 billion YTD. The Barclays Capital U.S. Aggregate Agencies Index tightened 5 bps last week to +73 OAS.
- ❑ The mortgage market outperformed Treasuries last week as measured by the Barclays Capital U.S. MBS Index. Spreads tightened 6 bps to + 96 OAS in part by another \$32.9 billion of Agency MBS purchased by the Fed.
- ❑ The corporate market improved another 8 bps last week to +532 OAS in the Barclays Capital U.S. Corporate Investment Grade Index. The Industrial sector improved 8 bps, while Utilities were unchanged and Financials improved by only 4 bps. It seems that despite the new accounting rule benefit to the Financial sector, confidence has been shaken by fears of nationalization of banks. Fox news reported that a prominent bank has been trying to return their TARP money with interest, but has been denied and threatened by the Administration if it persists in returning the money.

Fed's YTD Purchases of Agency MBS

Source: Federal Reserve

