



## Bond Market Weekly

Week of October 19, 2009 | Municipal and Corporate Review

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### Market Overview

- ❑ A late week rally in long US Treasuries pushed the yields on the 10-year note to 3.40% after worse than expected earnings for Bank of America and General Electric weakened the equity market. However, 10-year yields did finish the week 2 bps higher.
- ❑ September's advance retail sales estimate came in better than expected at -1.5%. This was somewhat offset by downward revisions to prior releases. The better economic numbers are consistent with the overall recent trend of stronger numbers.
- ❑ The Consumer Price Index came right in-line with expectations however the year-over-year numbers remained negative.
- ❑ Empire Manufacturing, more of a leading indicator, was very strong and came in considerably better than expectations. Nearly all sectors of the survey were stronger, including employment. This led to a midweek spike in equities and a decline in US Treasury prices.
- ❑ Initial Jobless Claims fell by 7,000 from 521,000 to 514,000 while Continuing Claims fell by 48,000 jobs on the week. Both numbers beat expectations.
- ❑ The US Dollar continued to slide against most major currencies and remains a serious concern for market participants.
- ❑ Next week's calendar includes the September Producer Price Index, Housing Starts and Existing Home Sales, all of which will shed light on the veracity of the economic rebound currently underway.

### Tax Exempt Markets

- ❑ Municipal bonds had a difficult start last week, but firmed considerably on Thursday and Friday. 10-year bond yields rose 11 bps to 3.21% and 30-year bonds rose 10 bps to 5.01%.
- ❑ With continued fears of large supply and dealers scrambling to lighten their inventories, municipal bonds were in free fall at the beginning of the week. By the end of the week, as the Treasury market firmed, better ratios and higher absolute yields pushed buyers to emerge in force.
- ❑ Forward supply continues to rise with the Bond Buyer 30-Day Visible Supply Index at \$16.4 billion. While seemingly a large amount of supply that could weigh down the market, this is somewhat misleading. Many of the new issues on the calendar are refundings and when yields rise significantly, these issues tend to get pulled from the market. We observed this with the State of Hawaii, Houston School District and a portion of the Washington State GO deal. This supply overhang combined with strong demand may leave municipal bonds range bound for some time.
- ❑ Investor demand remains high with tax exempt mutual fund inflows of \$2.7 billion for the week ending October 7. Until demand wanes considerably it will be difficult for municipal prices to fall too far.
- ❑ In positive ratings news, the State of Louisiana was upgraded to AA- from A+ by Standard and Poor's citing the continued rebound from Hurricane Katrina. In addition, the State was not impacted by the boom that most of the country experienced, and therefore was not affected greatly by the bust.
- ❑ With the continued sell-off and the highest yields available in months, we aggressively bought bonds across the curve but focused mostly in the 10- to 15-year area of the curve. Many of our purchases focused upon AA rated bonds where we found the most relative value due to a large amount of primary and secondary supply. We purchased a Hawaii COP deal this week as well as a zero coupon new issue for the Baldwin County, GA school district.



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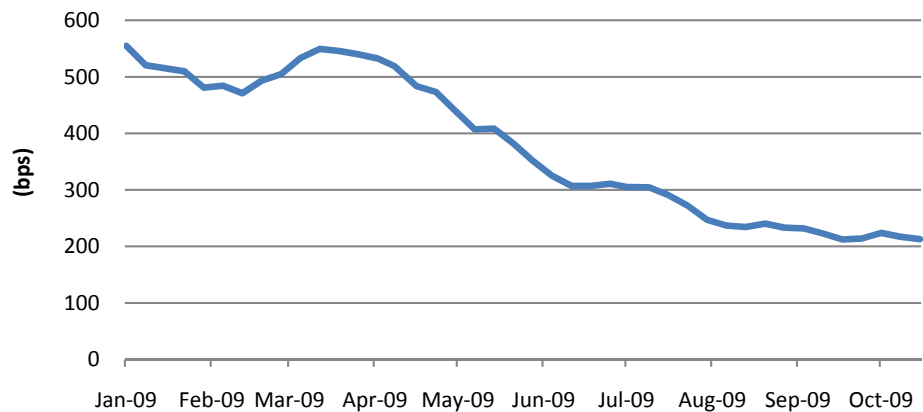
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### Taxable Markets

#### US Corporate Investment Grade Index

12/31/08-10/16/09; Source: Barclays Capital



- ❑ Even with a Columbus Day holiday-shortened week, corporate new issuance surged 82% from the prior week to \$22.7 billion. Deals were highlighted by Anheuser-Busch InBev NV and Deere & Co. Anheuser-Busch (Baa2/BBB+) matched the largest non-financial issuer of the year with a \$5.5 billion 4-part issue under the 144a private-placement registration. They priced a 3-year, 5-year, 10-year, and 30-year at spreads of +160, +185, +210, and +220, respectively. Deere (A2/A) did a 2-part deal with the 10-year priced at +110 and the 20-year priced at +120 for a total of \$1.25 billion.
- ❑ Earnings season forged onward with bellwether names like Goldman Sachs, JPMorgan, and Intel providing confidence to the markets. The tone changed a bit Friday as disappointing announcements from GE and Bank of America tempered previous enthusiasm. The Barclays U.S. Corporate Investment Grade Index ended the week 4 bps tighter to +213 OAS (option-adjusted spread).
- ❑ The MBS market ended the week unchanged in spreads with a +26 OAS reading in the Barclays U.S. MBS Index. Within the sector, higher coupons outperformed because of slower than expected prepayments reported in higher coupon conventional collateral for the month of September. Also, the Fed purchased \$16.1 billion of agency MBS for the week bringing their total purchases up to \$941.0 billion. The national survey of 30-year conforming mortgages by FHLMC showed an average of 4.92%, 5 bps higher than the previous week.
- ❑ In agencies, U.S. Central Federal Credit Union issued the first debt under the Temporary Corporate Credit Union Liquidity Guarantee Program (TCCULGP). The program is offered to member credit unions and guarantees principal and interest payments by the full faith and credit of the US Government, similar to the FDIC's backup of the TLGP program for banks.