



## BOND MARKET WEEKLY

WEEK OF NOVEMBER 16, 2009

### MARKET OVERVIEW

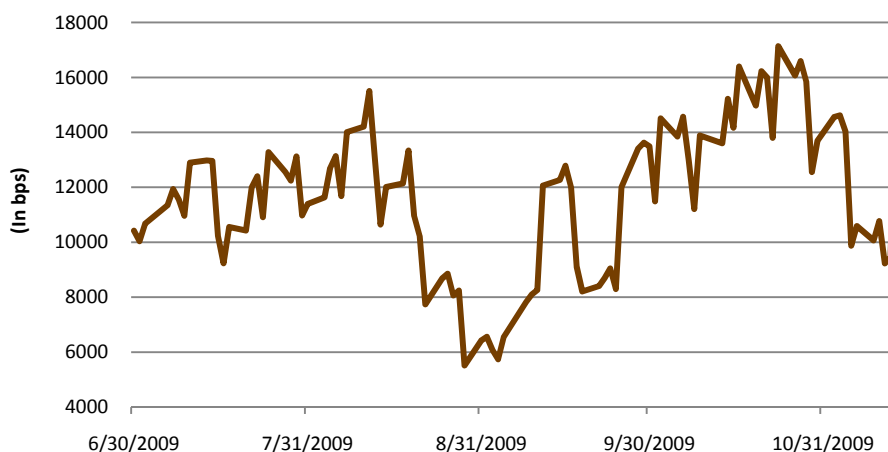
- Last week the market was atypical with the Veteran's Day holiday on Wednesday and little in the way of economic data on the calendar. However, solid 3- and 10-year Treasury auctions provided a measurable catalyst for the bond market. The benchmark 10-year yield dropped 7 bps to 3.43% as of Friday afternoon on the early week auction momentum. Thursday's 30-year auction was a bit weaker, but any market hangover that resulted was erased by late Friday.
- The yield curve flattened slightly on the week as the inflation trade paused a bit. The spread between 2- and 10-year notes fell 4 bps to +261 while 2- to 30-year spread fell just 1 bp to +354.
- The inflation breakeven measure in the TIPS market fell by 1 bp to 1.78% across the immediate 5-year horizon while the longer 5-year, 5-year forward horizon fell 4 bps to 2.71%.
- While the economic data was light on the week, initial jobless claims readings did further confirm a downward trend with 502,000 filings last week and 5.631 million continuing claims.
- Trade balance data released for September showed a surprise jump in the current account deficit and in combination with other revisions points to a lower Q3 GDP revision ahead (currently +3.5%).
- This week's calendar ramps up substantially with Retail Sales, CPI, Empire Manufacturing and Philly Fed data. Plenty of catalyst for the bond market which is coming off another impressive digestion of massive supply.

### TAX EXEMPT MARKETS

- Municipal bonds rallied slightly this week with 10-year yields falling 2 bps to 3.15% and 30-year bonds falling 1 bp to 5.02%.
- Demand continues to be strong despite a heavy calendar over the past month and looking forward. The Bond Buyer Visible Supply Index is a heavy \$15.6 billion as issuers are looking to get a number of deals sold before year-end.
- New deals this week include Charlotte Water/Sewer, NC (\$367 million), Los Angeles Airport (\$662 million) and the New Hampshire Turnpike (\$218 million).
- Investor demand continues unabated with tax exempt mutual fund inflows of \$899 million for the week ending November 4th. We expect that demand could taper off through year-end due to cash needs but should strengthen in 2010.
- Assured Guaranty was downgraded last week to Aa3 with a negative outlook, Moody's also affirmed Assured Guaranty Municipal (the former FSA) at Aa3. Losses from structured products continue to be higher than expected, although claims paying resources remain strong. While Assured has rebranded FSA into a municipal only bond insurer, it will be interesting to see if the market and the ratings companies differentiate the two.
- With a holiday shortened week our trading was somewhat muted as there seemed to be little secondary flow in the market. Most of our inquiries focused upon filling holes in specific portfolios as opposed to broad based buying.

#### Bond Buyer 30-Day Visible Supply

6/30/09-11/16/09; Source: Bloomberg





### **TAX EXEMPT MARKETS (CONT.)**

- We expect that, with the upcoming holidays, liquidity could weaken somewhat through year-end. Therefore, for accounts requiring cash, the sooner we are notified, the better execution we can achieve for our accounts. Please let us know if you would like to discuss upcoming client liquidity needs.

### **TAXABLE MARKETS**

- New issuance was pretty strong with \$20.6 billion of investment-grade corporates being priced despite a holiday shortened week. The biggest issuer was Cisco Systems (A2/A+) for a total of \$5 billion priced via a 5-year at +67 to Treasuries, a 10-year at +100, and a 30-year at +130. One has to wonder what Cisco intends to do with the funds considering that as of 10/24/09 they had \$4.8 billion of cash and short-term investments of \$30.6 billion which together exceeded total debt outstanding by \$25 billion. Given the pickup in merger activity within the tech hardware space recently, perhaps they are positioning for an acquisition.
- The Barclays US Corporate Investment Grade Index continued to tighten, ending the week at +201 OAS (option-adjusted spread), 3 bps better than the previous week. Other than new issues, the market had little data to digest. The tail end of Q3 2009 earnings announcements from companies consistently showed lower revenues but successful cost-cutting measures.
- Home mortgage rates fell to their lowest level in five weeks according to the Freddie Mac survey. Their national survey of the average 30-year mortgage rate came in this week at 4.91%, 7 bps better than the prior week. MBS volatility moved to their lowest levels since last spring and mortgage applications filed to purchase homes hit their lowest level in over eight years which helped push MBS spreads to very tight levels. The Barclays US MBS Index was 14 bps tighter to end the week at +4 OAS.
- The Fed bought \$13.5 billion of agency MBS and \$1.845 billion of agency debt last week. This brings the program purchase totals to \$1.005 trillion and \$152 billion to date for MBS and agency debt, respectively.

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