



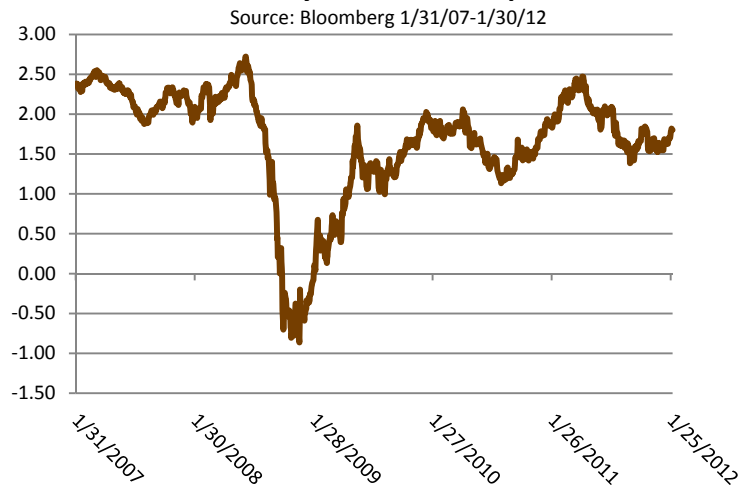
## BOND MARKET WEEKLY

WEEK OF JANUARY 30, 2012

### MARKET OVERVIEW

- The trading week saw the yield on the 10-year US Treasury finish 13 bps lower at 1.90% and the 30-year fell 4 bps to 3.06%. The 2- to 10-year spread narrowed 10 bps to 168 bps, and the 2- to 30- year narrowed 1 bp to 285 bps.
- The 5-year break-even inflation rate widened 10 bps on the week and starts the trading week at 180 bps. The longer term 5-year, 5-year forward, which measures the market's future inflation expectations, widened 1 bp to 239 bps.
- Initial Jobless Claims 377k v. 370k estimate, Leading Economic Indicators 0.4% v. 0.7% estimate, GDP 4Q 2011 2.8% v. 3.0% estimate, GDP price index 0.4% v. 1.9% estimate. This week gives us a look at Case Shiller Home Price Index, Chicago Purchasing Managers report, and ADP Employment data.

### 5-Year History of Inflation Expectations



### TAX EXEMPT MARKETS

- Municipals rallied last week with 10- and 30-year yields falling 3 and 4 bps to 2.17% and 4.06%, respectively.
- Mutual funds saw inflows with Lipper reporting \$513 billion of inflows for the week ending 1/25/12.
- The Bond Buyer 30-day Visible Supply Index is \$6.28 billion. New deals this week include the Massachusetts College Building Authority (\$195 million), Nebraska Public Power (\$235 million), and the Puerto Rico GDB Taxable (\$500 million).
- In ratings news, Moody's Investors Services withdrew Lackawanna County, PA's 'Ba3' GO rating. They cited a lack of available financial information or completed audits which led to the rating withdrawal. This credit has had a history of multi-year fund imbalances and strained finances.

### TAXABLE MARKETS

- There was a big drop in total investment grade issuance. We had averaged about \$27 billion per week of new debt so far this month, but last week it was \$8.9 billion. National Rural Utility Cooperative Finance 'A1/A+' came to market with demand that was, by some reports, more than 7 times oversubscribed. It was a total of \$800 million split equally between 3- and 10-year bonds and priced at +80 and +115, respectively. One name not seen often was an offering by Harley Davidson 'Baa1/BBB+' to borrow \$400 million of a 5-year note at +195.
- Secondary trading, however, was up 10% from the prior week. According to TRACE, \$71 billion bonds traded (the strongest week so far this year) with finance issuers the most active again on strong performance. A couple examples were the 10-year benchmark notes of Morgan Stanley and JPMorgan that tightened 20bps and 15bps, respectively.
- The Barclays U. S. Corporate Investment Grade Index was 10 bps tighter to finish the week at +207 OAS.



## TAXABLE MARKETS (CONT.)

- Agencies traded very well last week, with the belly and long end of the curve keeping pace with the rally in Treasuries and the front-end significantly outperforming them. After the new Fed language, investor demand for spread product in both bullet and callable agencies was insatiable and resulted in a 5 to 7 bps tightening and a considerable drop in volatility. Freddie Mac issued a new 5-year benchmark at +32.5 to the 5-year which drew strong investor demand.
- Like Agencies, the agency MBS market took off after the Fed announcement and the entire coupon stack tightened to their like duration Treasuries, especially current coupons. This was a result of investors demanding more yield and duration which caused current coupons in both 15- and 30-year pools to outperform anywhere from 8 to 14 ticks. Mortgages applications decreased 5% from the previous week.
- New issuance was low again last week in taxable municipals with no new deals of significant size. The only deal we participated in was Tucson Water; however, we were active adding to existing credits in the secondary market. Liquidity remains good and taxable municipals continue to benefit from an overall lack of supply.

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