



# PORTFOLIO MANAGER'S REPORT



Thursday May 20, 2010 8:59 AM

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## CURRENT OFFERING YIELDS - Thursday: 05/20/2010 8:59 AM

## TODAY'S ECONOMIC DATA

	Trsy (Last Price)	Change (From Yest)	Agcy NC (Bullets)	Muni - TEY (A1; GO; BQ)	CMO (Avg Life)	MBS (Avg Life)			
3 mo	0.155%	-0.70 bp's	0.192%	0.405%			20-May	Initial Jobless Claims	
6 mo	0.211%	-0.70 bp's	0.277%	0.511%			20-May	Prior: 444K Actual: 471K	
12 mo	0.308%	-0.7 32'ds	0.524%	0.723%			20-May	Continuing Claims	
2 yr	0.716%	+ 3.5 32'ds	1.013%	1.253%	1.616%	1.666%	20-May	Prior: 4627K Actual: 4652K	
3 yr	1.148%		1.451%	1.859%	2.148%	2.248%		Leading Indicators	
5 yr	2.013%	+ 7.5 32'ds	2.327%	3.071%	2.863%	3.163%		Prior: 1.4% Actual: ---	
10 yr	3.240%	+ 7.5 32'ds	3.594%	5.132%	4.190%	4.240%	DJIA	10,255.96	-188.41
30 yr	4.109%	+ 35.0 32'ds	4.793%	6.950%			NASDAQ	2,246.78	-51.59
							S & P 500	1,092.45	-22.60

Source: Bloomberg Fair Value Curve or Last Price (Treasury only); ALL yields and spreads are "representative", not actual. Spreads change as the market changes, actual offerings may be higher or lower than

## TODAY'S NEWS

### Treasury 10-Year Note Yield Drops to Lowest Level This Year on Euro Crisis

May 20 (Bloomberg) -- Treasuries climbed, pushing the 10- year note's yield to the lowest level this year, as the response of European authorities to the sovereign-debt crisis drove investors to the relative safety of U.S. debt. The extra yield investors demand to hold 10-year U.S. securities instead of German debt narrowed after European Central Bank executive board member Jose Manuel Gonzalez-Paramo said in an interview with Italy's Il Sole 24 Ore newspaper Germany didn't tell the bank of its plan to ban some speculative activities. U.S. yields indicate traders cut bets on inflation to the lowest in six months. U.S. jobless-benefit claims rose.

### How Much Longer Will the Fed Hold Their Outsized MBS/CMO Position?

An interesting story (excerpted below) posted yesterday on Bloomberg News. As we have discussed at great length in this space, the agency MBS/CMO market has benefitted terrifically from the Fed's quantitative easing. As the Fed's market moving acquisition of mass quantities of this paper ceased in March, the investing public's most important question became "When will the liquidation begin?" Obviously, the sale of these securities has the potential to proportionately reverse the positive price action which the purchase of these bonds ignited. Thus portfolios which own these bonds, and have benefitted greatly from their appreciation, are correctly concerned about what the Fed (the 800lb gorilla) will do with their bonds.

If your portfolio is significantly proportioned with agency MBS/CMO, you'll want to be "ahead of the Fed" when it comes to a liquidation (unless you're okay with owning them once the Fed begins selling and prices are most likely to depreciate quickly). We don't know when the "perfect time" to sell is. With the Fed saying they'll be holders (for now) this may not be the last opportunity....but it certainly is an opportune moment if you're feeling particularly uneasy about the future.

Just how many *can* squeeze out that door once the proverbial theatre is on fire?

### **Fed Officials in No Hurry to Sell Mortgage Assets, Minutes Say** 2010-05-19 18:00:00.22 GMT

By Scott Lanman

May 19 (Bloomberg) -- Federal Reserve policy makers last month said they were in no rush to sell \$1.1 trillion of mortgage-backed securities, with a majority preferring to wait until after the central bank starts raising interest rates.

"Most participants favored deferring asset sales for some time," while others wanted to announce a schedule or start sales soon, the Fed said in minutes of its April 27-28 meeting in Washington, released today. Officials lowered their projections for inflation, excluding food and fuel, while keeping forecasts little changed for economic growth and unemployment in 2011 and 2012.

Chairman Ben S. Bernanke and his colleagues are debating when and how fast to shrink the Fed's balance sheet and raise interest rates as the economy recovers. The Fed aimed to lower home-loan costs and boost growth by buying mortgage securities through last March after lowering the benchmark interest rate almost to zero in December 2008.

"Even though the recovery appeared to be continuing and was expected to strengthen gradually over time, most members projected that economic slack would continue to be quite elevated for some time," according to the Federal Open Market Committee report, which doesn't identify the specific governors or regional-bank presidents making comments.

Officials expected inflation to remain "below rates that would be consistent in the longer run with the Federal Reserve's dual objectives" of maximum employment and stable prices, the minutes said.

Some policy makers said at the meeting they were concerned about potential spillover to the U.S. from the Greek debt crisis, more than a week before European officials stepped in with an almost \$1 trillion aid package and the Fed decided to restart emergency currency swaps.

### Fiscal Consolidation

"If other European countries responded by intensifying their fiscal consolidation efforts, the result would likely be slower growth in Europe and potentially a weaker global economic recovery," the minutes said.

At last month's meeting, the FOMC voted 9-1 to retain a pledge to keep the federal funds rate at a record low for an "extended period." While the labor market is "beginning to improve," employers are still reluctant to hire, and inflation will remain "subdued for some time," the April 28 statement said.

Kansas City Fed President Thomas Hoenig dissented for the third straight meeting, saying the "extended period" language limited the central bank's flexibility to raise interest rates. The minutes didn't indicate that other voting officials might join him.