



PORTFOLIO MANAGER'S REPORT



Thursday June 03, 2010 9:05 AM

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CURRENT OFFERING YIELDS - Thursday: 06/03/2010 9:05 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	0.130%	-1.00 bp's	0.188%	0.359%			3-Jun	ADP Employment Change Prior: 32K Actual: 55K
6 mo	0.216%	UNCH	0.288%	0.435%			3-Jun	Nonfarm Productivity Prior: 3.6% Actual: 2.8%
12 mo	0.370%	-0.2 32'ds	0.542%	0.647%			3-Jun	Unit Labor Costs Prior: -1.6% Actual: -1.3%
2 yr	0.829%	-1.5 32'ds	1.038%	1.147%	1.729%	1.779%		
3 yr	1.279%		1.471%	1.748%	2.279%	2.379%		
5 yr	2.178%	-3.5 32'ds	2.336%	2.950%	3.028%	3.328%	DJIA	10,287.63 38.09
10 yr	3.394%	-3.5 32'ds	3.584%	4.980%	4.344%	4.394%	NASDAQ	2,292.73 11.66
30 yr	4.289%	-14.5 32'ds	4.797%	6.920%			S & P 500	1,102.87 4.49

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

Treasuries Fall on Bets Payrolls Will Show Evidence of Economic Recovery

June 3 (Bloomberg) -- Treasuries fell for a second day on speculation tomorrow's U.S. employment report will show the economic recovery is gaining momentum, reducing demand for relative safety. The drop in bonds pushed the yield on the 10-year note to the highest level in two weeks before the Labor Department's figures, which are forecast by economists to show payrolls grew last month by the most since 1983. Global stocks rose on the prospects for the world's largest economy.

Today's Topic: Putting Your Excess Funds to Work

It's been discussed almost to the point of absurdity, but why sell overnight funds at .25% (or less) when you have no loan demand to fund? There may be some valid reasons related to regulatory issues or an erratic deposit base with large balance swings, but for most institutions it usually comes down to a rate call or fear of structuring a mismatch of longer assets supported by much shorter liabilities. Actually, the key word is most likely fear. Caution is a good thing. But, a rational plan to put your excess funds to work is still possible within the perspective of conservative balance sheet management.

First, at the expense of sounding like a broken record (a scratched CD for the younger set) critically analyze why you have excess funds. The funds may be seasonal or part of the natural ebb and flow of the balance sheet, but it might be related to the dreaded "over payment" on the liability side. Have you rationally determined a pricing strategy that fits today's low rate and weak loan demand environment? Does it still make sense to maintain your position in the "rate hierarchy" of your local community at the expense of your spread and margin? Specifically, are you paying too much for public funds when you have no loan demand to offset them? The Fed is practically giving banks free money and bids for public money (which require pledging thereby decreasing your liquidity) should be in line with other sources of available funds.

Let's assume you have excess funds because you have done all you can do to discourage the shopper's of the world, what do you do? It depends on the structure of the existing investment portfolio to some extent. If you have maturities or calls coming due in the next 12 to 24 months, why not invest now, in accordance with your normal portfolio strategy, and determine what to do with the maturities when they come due. Yes, this assumes the spread over your cost of funds today is acceptable, and that you may have to decrease that spread if rates shoot up, but it appears to be a minimal risk, depending on your structure.

A recent example is illustrative of this strategy. A "throw-away" bid of 80 basis points for six month public money turned out to be the winning bid. The next day 5.8mm dollars came in the door, resulting in an overnight position in the 6mm range. Fortunately, about 24mm is coming due in the next 24 months (approximately 37% of the entire investment portfolio). Loan funding is not an issue, so the 5.8mm is now invested in accordance with the investment strategy already in place. This includes about half in agencies in the three to five year range and about half in the five to eight year range in tax exempt municipal bonds. The maturing securities may or may not be reinvested, depending on the situation at the time. This strategy is preventing a negative arbitrage (80bps -25 bps, or -55bps) and is producing a positive spread approaching 200 basis points.

Take a look to determine if this strategy will work for you.