



PORTFOLIO MANAGER'S REPORT



Wednesday July 28, 2010 8:54 AM

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CURRENT OFFERING YIELDS - Wednesday: 07/28/2010 8:54 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	0.145%	+ 0.30 bp's	0.145%	0.495%		28-Jul	MBA Mortgage Applications	Prior: 7.6% Actual: -4.4%
6 mo	0.196%	- 0.10 bp's	0.207%	0.526%		28-Jul	Durable Goods Orders	Prior: -1.1% Actual: -1.0%
12 mo	0.293%	-0.2 32'ds	0.409%	0.617%		28-Jul	Durables Ex Transportation	Prior: 0.9% Actual: -0.6%
2 yr	0.641%	+ 0.9 32'ds	0.813%	0.980%	1.441%			
3 yr	1.017%		1.209%	1.511%	1.817%			
5 yr	1.768%	+ 2.0 32'ds	2.000%	2.571%	2.618%			
10 yr	3.039%	+ 2.0 32'ds	3.309%	4.708%	3.839%			
30 yr	4.095%	+ 2.5 32'ds	4.685%	6.950%				
							DJIA	10,515.67 -22.02
							NASDAQ	2,284.67 -3.58
							S & P 500	1,110.79 -3.05

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 Yields Are Near Two-Week High Before Fed Report, Auction

July 28 (Bloomberg) -- Treasury 10-year yields traded near the highest level in almost two weeks before a Federal Reserve report that may show the U.S. recovery is slowing and a government auction of \$37 billion of five-year notes. The yield on five-year securities slipped before the sale of the debt today, the second of three note offerings this week totaling \$104 billion. Treasuries earlier gained as data showed durable-goods orders unexpectedly fell in June.

Today's Topic- An Anomaly in Agency Land

As we all know, a portfolio manager is normally rewarded with an enhanced yield in exchange for assuming optionality (call risk) in a bond purchase transaction. These are hardly normal times however. As interest rates continue to decline, the spread advantage of one time callable agencies versus non-callable agencies has all but disappeared.

Consider these two new agency issues priced yesterday:

- 1)FHLB 2.00% due 11-13-15 callable 8-13-12 (1 time call) priced at par
- 2)FHLB 2.00% due 11-3-15 non-callable priced at par

Where's the incentive in buying the callable bond?

For the buyer willing to take on a substantial premium, "off-the-run" bullet agencies can actually out yield callables as shown in the example below:

FHLB 5% due 12-21-15 @ 2.10 % yield non-callable

Granted, one could argue that none of the above bonds are particularly exciting – but it is important in today's interest rate environment to understand and appreciate relative value.

If you think rates can't go lower and today's options won't be exercised, then you had better check your bond call report. Dozens of agencies are being called each day in the 1.00% to 2.00% range.

Stick with bullets over one time callables. It's a better option.