



# PORTFOLIO MANAGER'S REPORT



Thursday July 29, 2010 9:02 AM

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## CURRENT OFFERING YIELDS - Thursday: 07/29/2010 9:02 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)	29-Jul	Initial Jobless Claims Prior: 464K Actual: 457K
3 mo	0.145% - 0.10 bp's	0.129%	0.450%			29-Jul	Continuing Claims Prior: 4487K Actual: 4565K
6 mo	0.197% + 0.10 bp's	0.192%	0.465%				
12 mo	0.283% -0.2 32'ds	0.386%	0.571%				
2 yr	0.609% UNCH	0.745%	0.935%	1.409%	1.429%		
3 yr	0.975%	1.128%	1.470%	1.775%	2.325%		
5 yr	1.707% + 1.0 32'ds	1.894%	2.541%	2.557%	3.287%	DJIA	10,542.54 44.66
10 yr	3.021% + 1.0 32'ds	3.232%	4.677%	3.821%	4.021%	NASDAQ	2,267.33 2.77
30 yr	4.129% -10.0 32'ds	4.655%	6.950%			S & P 500	1,110.75 4.62

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

### U.S. 10-Year Yield Increases as Jobless-Claims Decline, Note Auction Looms

July 29 (Bloomberg) -- Treasury 10-year yields approached the highest in two weeks as data showed initial claims for jobless benefits fell last week for the third time this month and the U.S. prepared to sell \$29 billion in seven-year notes. U.S. 30-year bonds dropped, pushing yields to a one-month high, as equities in Europe and U.S. stock futures advanced. The government's note sale today will wrap up three auctions this week totaling \$104 billion. Treasuries gained the most in a week yesterday as a Federal Reserve survey showed U.S. economic growth slowed in some areas.

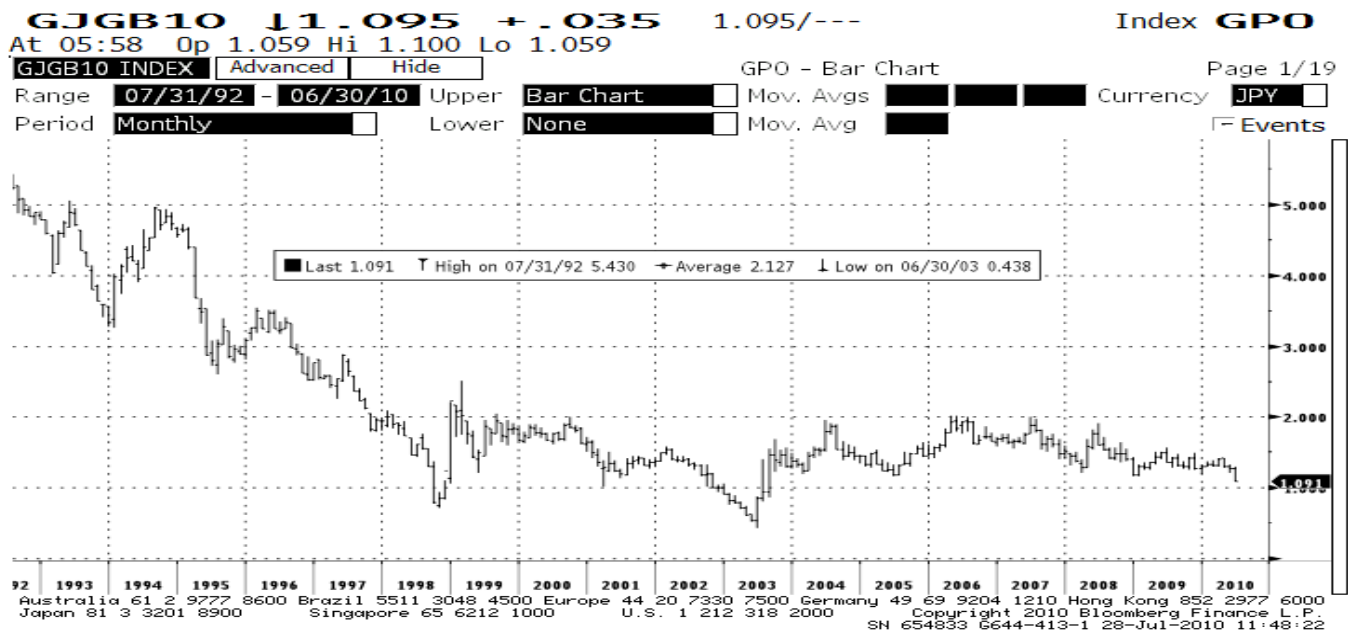
### Today's Topic- Is the Cure Making the Patient Sicker?

Who wants to borrow money to expand their businesses when the Federal Reserve is telling them the economy is bad and not likely to improve soon? NOT VERY MANY PEOPLE. Saying economic conditions are terrible for "an extended period" of time becomes a self fulfilling prophecy. Low interest rates for an extended period stifles economic growth... just ask Japan.

(See below the graph of the Japanese 10 year bond and an article from Tuesday's (7/27) Bloomberg News)

If you have a \$50 million dollar bank in a community paying an average rate on deposits of 4.00%, the town receives \$2 million dollars in interest income yearly to spend. Lower the rate paid by the bank to the community, and economic activity subsides as the direct result of less interest income. People are walking around with heads full of bad economic thoughts and very limited interest income in their pockets. They're worried about larger government intrusion in their lives.

Think interest rates are going up? Probably not until after the fall elections. Even then, it could be a short spurt up and then back down. The moral of this story.... be ready to buy bonds this fall.



## **U.S. Two-Year Yield May Fall to Match Japan's 0.15%, Takei Says** **2010-07-27 03:28:07.701 GMT**

By Wes Goodman

July 27 (Bloomberg) -- Treasury two-year yields may fall to match Japan's, the lowest in the world, because of deflation in America, said Mizuho Asset Management Co. in Tokyo, a unit of Japan's second-largest publicly traded bank.

"Two-year yields are obviously headed south," said Akira Takei, head of non-yen bonds at Mizuho, which has the equivalent of \$21.9 billion in assets. "I wouldn't rule out that they will fall to the same level as the Japanese yield within a year or two. The likelihood is very high."

U.S. two-year rates were 0.60 percent as of 12:25 p.m. today in Tokyo. The figure dropped to a record low of 0.5516 percent on July 23. Japan's yield was 0.151 percent, the least of 29 bond markets tracked by Bloomberg.

Investors snapped up Treasuries this year as slowing U.S. economic growth dropped the inflation rate to the lowest level in 40 years and stocks fell, increasing demand for the relative safety of government debt. Two-year yields, among the most sensitive to what the Federal Reserve does with interest rates, also slid as traders bet the central bank will keep borrowing costs at a record low.

A decline in U.S. two-year yields to 0.151 percent in 12 months would bring a 1 percent gain to an investor who bought today, according to data compiled by Bloomberg. Treasury bulls are in a minority. A Bloomberg survey of banks and securities companies projects the two-year yield will climb to 1 percent by year-end, with the most recent forecasts given the heaviest weightings.

### **Fed Deflation Concerns**

Takei said minutes of the Fed's June meeting released this month show policy makers are becoming more concerned about deflation, a general decline in prices.

"The economic outlook had softened somewhat and a number of members saw the risks to the outlook as having shifted to the downside," the minutes said. "A few participants cited some risk of deflation."

The Fed has pledged to keep borrowing costs low for "an extended period." It may drop this language within six months and say instead that it plans to hold rates down until deflation ends, Takei said. The Bank of Japan did the same thing when it was trying to stem a decline in prices in 2006.

Futures contracts on the CME Group Inc. exchange show a 38 percent chance policy makers will boost the target lending rate for overnight bank loans at least a quarter-percentage point by April, dropping from 55 percent odds a month ago.

U.S. consumer prices excluding energy and food rose 0.9 percent in June from a year earlier, matching the lowest since 1966, according to the Labor Department.

Two-year Treasuries have returned 1.9 percent in 2010, versus 6 percent for the broad market, according to Bank of America Merrill Lynch indexes. MSCI's World Index of shares handed investors a 1.6 percent loss after accounting for reinvested dividends.