PORTFOLIO MANAGER's REPORT

Wednesday August 18, 2010 8:30 AM

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CURRENT OFFERING YIELDS - Wednesday: 08/18/2010 8:30 AM

	Trsy (Last Price)	Change (From Yest)	Agcy NC (Bullets)	Muni - TEY (A1; GO; BQ)	CMO (Avg Life)	MBS (Avg Life)
3 mo	0.153%	+ 0.50 bp's	0.138%	0.450%		
6 mo	0.179%	- -0.70 bp's	0.173%	0.480%		
12 mo	0.233%	-0.1 32'ds	0.324%	0.586%		
2 yr	0.488%	+ 0.5 32'ds	0.632%	0.905%	1.288%	1.308%
3 yr	0.793%		0.951%	1.389%	1.593%	2.143%
5 yr	1.402%	+ 1.0 32'ds	1.588%	2.359%	2.252%	2.982%
10 yr	2.589%	+ 1.0 32'ds	2.808%	4.511%	3.389%	3.589%
30 yr	3.711%	+ 12.0 32'ds	4.340%	6.920%		

TODAY'S ECONOMIC DATA

18-Aug	MBA Mortgage Applications Prior: 0.6% Actual: 13.0%	
DJIA	10,391.66	-14.19
NASDAQ	2,204.68	-4.76
S & P 500	1,091.57	-0.97

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 Rise as Slowdown Fuels Speculation of Higher Fed Purchases

Aug. 18 (Bloomberg) -- Treasury 10-year notes rose, pushing yields near a 17-month low, as investors speculated whether the weakening U.S. economic recovery will prompt the Federal Reserve to increase purchases of government securities. The Fed plans to acquire Treasuries due from August 2016 to August 2020 tomorrow, after purchasing $2.551 billion of securities yesterday, to hold borrowing costs down. The central bank announced the purchases on Aug. 10, saying it would buy securities for the first time since October using funds from principal payments of its holdings of mortgage-backed debt. A report tomorrow may show weekly unemployment filings rose.

Today's Topic- Top Quality Muni Bonds Are Your Port in a Storm

You know that guy who predicted 12 of the last two economic downfalls? Yeah, that guy…well these days he's busy writing copy for the journal of "Munis are the Next Big Crisis." Yep, everybody loves a train wreck and every financial journalist loves ginning up the crowd, selling programs (aka: cover stories) and then feigning surprise when reality proves to be a mere fraction of the rumor. Most of the muni soothsayers of doom are only partially aware but wholly committed to their premise. Rarely will they allow pertinent details to get in the way of a good story. They cite facts in the same fashion a drunk uses a streetlamp: more for support than illumination.

So let's illuminate. The fact of the matter is this: General Obligation (GO) and essential purpose revenue bonds, historically, have enjoyed a *nearly spotless* record of uninterrupted and timely payments of principal and interest to bondholders. GO bonds are backed by the full "ad valorem" taxing authority of the issuer and essential purpose revenue bonds are paid by users of these vital services (water, heat, etc.) Fitch, Moodys and S&P are all in the business of rating municipal bonds. All three agencies have also published reports studying the matter of municipal defaults. In each report, the bonds least likely to default have been identified as:

- State and local GO bonds
- School district GO bonds
- Power, water and sewer Revenue bonds
- Public higher education GO bonds
- GO and Revenue debt backed by state or local levied taxes and appropriations

The Moodys data, dated Feb 2010, covers 40yrs of issuance and found that investment-grade munis experience lower default rates than similarly rated corporate bonds. For example, the average 5-year historical cumulative default rate for investment-grade municipal debt is 0.03%, compared to 0.97% for corporate issuers, while for speculative-grade debt (Baa and lower) the rates are 3.4% and 21.4% for municipals and corporate issuers respectively. In the Fitch data (compiled from 1987 - 2002) the <u>cumulative</u> default rate in all of these issues was less than one quarter of one percent (0.25%). Comparatively, the simultaneous default rate for AAA corporate debt was nearly twice this pace @ 0.43%. So why isn't this being reported? Perhaps because many writers don't know the difference between general obligation bonds and General Sherman…but they know one of them laid waste to Atlanta, so they must be bad.

Keep in mind that in times like these when home values are sagging and discretionary income is tight, issuers of GO debt backed by ad valorem real estate taxes will counter the depressed values by raising the mill levy. Similarly, utilities will make a case to adjust usage fees north. This is happening right now. Will there be trouble in muni bonds? Yes – within the broad universe of municipal issuers and structures there are bound to be troubles. Particularly with "project bonds" and low use private activity bonds. So avoid those, and similar, "siren songs" and stick to the plain vanilla structures that have a history of performance. Use your noggin, avail yourself to the issuer's debt figures and buy with confidence. You're likely to find some of the highest taxable equivalent yields available in the "top shelf" marketplace.

Please call your CCB Capital Markets representative for further discussion.