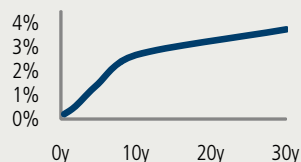


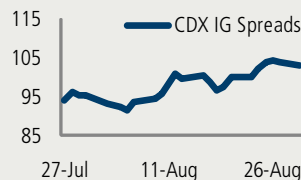
### Market Close

Treas.	Yld	Prev.	Chg.
2yr	0.51	0.48	+0.03
5yr	1.45	1.40	+0.06
10yr	2.66	2.60	+0.06
30yr	3.73	3.66	+0.07



MBS	Price	Chg
FN 4.5%	104-22	-08
GN 4.5%	105-26	-10

Credit	Close	Chg
CDX IG	105.1bp	-2.1bp
CDX HY	\$97.6	\$0.4



Muni	Yld	% Tsy	Chg.
2yr	0.50	97%	-4%
10yr	2.64	99%	-2%
30yr	4.17	112%	-2%

Source: MMA

### Day Ahead:

- Rates: Volatile rates markets reflect heavy issuance, incl. \$13bln of thirty year bonds to be auctioned today
- Credit: Wednesday issuance topped \$22bln, with no signs of letting up on Thursday
- Munis: Higher yielding IG revenue bonds are in vogue, even as AAA's follow Treasury performance

### Market Review:

Traders' screens were filled with red on Wednesday, as the second day of the holiday-shortened week featured heavy two-directional flows, and bonds ultimately proved surprisingly immune to economic pressures. Rate lock selling was one culprit for the downside action, as corporations with planned debt issuance looked to lock-in current funding costs by shorting the Treasury or swaps markets. While the scheduled ten year Treasury sale fared quite well, (3.21x bid/cover for \$21 billion being sold, leading to a yield at auction of 2.67%, 1.5 basis points though 1PM trading levels), it wasn't enough to pull rates out of their funk, and by the New York close, the ten year Treasury was trading at a 2.66% yield after a 6 basis point loss on the day, while the two year Treasury traded higher in yield by 3 basis points to 0.51%. Today's long bond reopening auction should receive a warm reception given the concessions built-in with a morning sell off and the steepness of the 10s/30s spread.

The Fed's Beige Book of economic conditions noted "continued growth...but with widespread signs of deceleration" at the majority of the twelve Federal Reserve districts in July through August. While the report comes as no surprise, it confirms a darkening outlook shared by policymakers across the country. From a consumer perspective, spending was mixed nationwide, with most districts pointing out improved demand for lower-priced items with weakening spending on big ticket items. Businesses experienced slightly better performance, though for manufacturing, a major leading indicator, "the pace of growth appeared to be slower than earlier in the year." One of the most significant problems in stimulating spending is encouraging cautious consumers to borrow, but the July consumer credit release provides little evidence of improving credit demand. Consumer credit declined by \$3.6 billion, primarily from pay downs on revolving lines of credit such as credit cards.

Concerns over European sovereign and private sector credit quality are re-emerging with a vengeance this week after a rough August for credit spreads on the continent. On Wednesday, Ireland (Aa2/AA-) announced that it would be splitting the state-acquired Anglo Irish Bank (A3/BBB) into two components, a "funding bank" and a "bad asset bank." The fact that this split comes less than six weeks after the release of European bank stress test results is once again calling into question the validity of those tests, which we view as far less stringent than the Fed's 2009 SCAP stress tests for US banks. Overall, we anticipate that Eurozone credit quality, both sovereign and corporate, will persist on a downward leg well into 2011. —Guy LeBas

The municipal market followed Treasuries lower Wednesday with benchmark yields moving higher across the curve. Even high grade Minnesota (Aa1/AAA/AAA) had to adjust yields one to two basis points higher to get the \$900 million GO bonds, originally priced yesterday, placed. On the other hand a North Carolina Eastern Municipal Power Auth issue (Baa1/A-/A-) had a seven basis point drop in yields compared to Monday's pricing indicating the strong demand for higher yielding municipals.

In local credit news, S&P bumped the rating of Byram, NJ two notches AA- based on the area's (Sussex County) continued economic strength and the township's strong financial position. Elsewhere in NJ, the rating for Rochelle Park GOs was raised by S&P from A to A+. Moving north, S&P raised the rating for Barnstable MA Fire District three steps from A+ to AA+ based on a stable property tax base. Harris County-Houston Sports Authority, which financed Minute Maid Park, Reliant Stadium and The Toyota Center (Astros, Texans and Rockets) was downgraded by S&P. Last month Moody's dropped senior, junior and third lien bonds to junk. S&P affirmed its BBB rating on the senior lien, about 40% the debt, but dropped the junior and third to B. S&P noted good debt service coverage for senior lien despite declines in hotel occupancy and vehicle tax revenues.

As reported by Bloomberg, California property owners will see some tax cuts according to the CA Board of Equalization based on falling property values across the state (1.8% following a 2.4% decline last year). The Santa Clara assessor, with a keen grasp of the obvious was quoted as saying "This is not your normal downturn." In Florida, a legislative report projected that the FY2012 deficit will be half of previous projections at around \$2.5 billion. The Ohio auditor declared three municipalities to be in fiscal emergency according to the Bond Buyer, illustrating the process many states use to help communities in fiscal distress. In Ohio, the state appoints a commission to help local officials stabilize their financial situation by developing a deficit elimination plan, balancing the budget and identifying strategies to avoid future deficits. —Alan Schankel

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