Fixed Income Weekly

Fixed Income Market Comments

Three items drove interest rates down last week. The first was the dramatic changes that the Federal made last week to include the onset of inflation targeting, interest rate forecasting by its 17 members and further hinting by Chairman Bernanke that there will be additional quantitative easing this year. The second and third items were not as influential as the first but did have some impact. The second was the government released the advance Gross Domestic Product (GDP) report for the last quarter of 2012 and it came in at 2.8% growth which was slightly below street estimates of 3.0%. Third, the problems in Europe continue with Greek debt negotiations not going well and similar concerns causing interest rates to spike in Portugal. We will go into further details on each of the three items below.

Treasury debt rallied last week as the FOMC announcement that it will likely keep interest rates low for the foreseeable future and slightly weaker than expected fourth-quarter GDP causing the yield on the benchmark 10-year Treasury to fall 13 basis points (bps) to 1.89% while the 2-year note yield fell three bps to 0.21%, creating a 2s/10s spread of 168 bps. The yield curve flattened as the 2s/10s fell by 11 bps. The yield on the 30-year bond fell by four bps to 3.06%.

Spreads tighten and yields fell on credit issues as continued Fed activism in the markets sent money into risk asset classes. High yield corporate bond debt tightened 15 bps to +632 bps over comparable maturity Treasury debt (yield fell to 7.50% from 7.78%) and investment grade corporate bond debt tightened 11 bps to +206 bps over (yield fell to 3.46% from 3.66%)

Federal Open Market Committee (FOMC) Meeting

It was an eventful week for the Federal Reserve as the Fed announced that it would begin inflation targeting. The FOMC committed to holding inflation at 2.0%, concluding years of debate that Bernanke advanced after becoming Fed chief in 2006. Starting with his confirmation hearing in 2005, Bernanke said an inflation goal would reduce “public uncertainty” while anchoring long-run expectations about policy making. The Fed joins at least 12 other central banks such as the Reserve Bank of New Zealand, the central bank of Sweden and the Bank of Mexico in specifying its inflation target. Unlike many of its counterparts, the U.S. central bank must also follow a congressional mandate to promote full employment as well as fight inflation.

FOMC members, for the first time last week, published their forecasts for the federal funds rate. The projections show a majority of policy makers expect the benchmark lending rate to remain below 1.0% for the next three years. However, the forecasts showed three of the 17 members said the Fed should raise rates in 2012 and three said raise them in 2013. The Fed extended the horizon on its pledge (broad definition of the word as the statement reads “likely warrant exceptionally low levels) made August 9 to keep its benchmark interest rate at a record low level at least through mid-2013 to at least through late 2014. The FOMC has left its target for overnight loans between banks in a range of zero to 0.25% since December 2008.

Fed Chairman Bernanke, speaking at a news conference after the statements, said that the option of further large-scale bond purchases is still “on the table.” Minutes of last week’s meeting, to be released in three weeks, will include “qualitative information” regarding FOMC participants’ expectations for the central bank’s $2.92 trillion balance sheet for the first time. The Fed’s obligation to ensure full employment “stands on an equal footing” with the price goal, Bernanke said, adding that the central bank will be flexible in pursuing both congressionally mandated objectives.

Many believe that Bernanke is setting the table for another quantitative easing (this one would be QEIII for those keeping score) that will more than likely be announced in late spring this year. Bets are that QEIII would be in the form of MBS purchases of approximately $500 billion. In August, the Fed pledged to keep its benchmark rate “exceptionally low” until mid-2013, and in September it decided to replace $400 billion of short-term debt in its portfolio with longer-term Treasuries in an effort to lower borrowing costs even more. The moves followed two rounds of large-scale asset purchases totaling $2.3 trillion that ended last June.

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The Fed also announced last week new forecasts for inflation, gross domestic product and unemployment for the next three years. The economic forecasts show officials expect little improvement in the unemployment rate by the fourth quarter of this year compared with the 8.5% last month.

The personal consumption expenditures price index (the price measure Fed officials chose for their inflation target) is expected to be below the 2.0% goal at the end of this year. Inflation will range from 1.4% to 1.8% this year and 1.4% to 2.0% in 2013, Fed officials forecast. In November, they projected inflation of 1.4% to 2.0% in 2012, and 1.5% to 2.0% next year.

Federal Reserve analysts lowered their forecast for GDP growth this year to 2.2% to 2.7%, down from a projection of 2.5% to 2.9% in November. They predicted the economy next year will expand 2.8% to 3.2%, compared with a previous forecast of 3.0% to 3.5%.

Richmond Fed Bank President Jeff Lacker dissented from the decision because he "preferred to omit the description of the time period over which economic conditions are likely to warrant exceptionally low levels of the federal funds rate," according to the FOMC statement.

Other attempts at transparency include the Fed chairman holding press conferences for the first time last year as part of a broader effort to reveal more to the public about central bank operations and the FOMC now publishing policy makers' forecasts four times a year, up from two during the era of Fed Chairman Alan Greenspan. In November the committee released new data that reveals its changing views on risk and uncertainty.

Fourth-Quarter GDP

Consumer spending restraint held growth in the U.S. economy to a 2.8% annual pace in the fourth quarter, slower than economists forecast; however, it was the fastest pace in more than a year. GDP (the value of all goods and services produced) climbed at a 2.8% annual pace following a 1.8% gain in the third quarter, according to data from the Commerce Department. The median forecast of 79 economists surveyed by Bloomberg News called for a 3.0% increase. Projections in the Bloomberg survey ranged from 2.4% to 4.5%. However, growth excluding a jump in inventories was just 0.8%.

For 2011, the U.S. economy grew 1.7%, less than 3.0% a year earlier. However, the U.S. is likely to outperform Europe and Japan this year, according to the International Monetary Fund (IMF). The IMF this week kept its U.S. forecast for 2012 unchanged at 1.8 %. It predicted a 0.5% contraction in the 17-nation euro area and a 1.7% growth in Japan.

Problems in Europe

European leaders continued to spar with Greece over a second rescue program, clouding progress toward a permanent aid fund and tougher budget rules designed to stabilize the euro. Greece faced criticism that its economic makeover is faltering; however, it fended off German-led calls for a European overseer to take command of its budget after its deficits surpassed targets for two years. Bargaining with Greece over a debt write-down and its economic management threatened to overshadow a summit meant to point the way out of the financial crisis by speeding the setup of a full-time €500 billion ($654 billion) rescue fund and signing off on a German-inspired deficit-control treaty.

Greece is making progress on one component of the package, nearing an agreement for bondholders to accept deeper losses on a 50% cut in the face value of more than €200 billion of debt. Creditors are reportedly willing to take an average coupon of as low as 3.6% on new 30-year bonds. As recently as January 23, creditors wanted an average coupon of about 4.25%, two people familiar with the talks said then. That offer equated to a loss of about 69% on the net present value of Greek debt.

European concerns that Greece can deliver budget cuts and economic reforms are holding up other parts of the package, which Greece needs to meet a €14.5 billion bond payment due on March 20. German Chancellor Merkel said that they won't have a thorough discussion of Greece because the troika is in Greece and they don't have a result of the talks with the banks.

The troika -- the European Commission, European Central Bank and International Monetary Fund -- oversees the €110 billion program awarded to Greece in 2010 and conducts talks on an additional €130 billion pledged in October. Germany's call for an EU-appointed overseer of Greece's budget prompted consternation in Athens and led other European governments to warn against treating Greece differently than other countries.

Holders of Portuguese bondholders are fearful that they are headed down the same path as that of Greece bondholders, with the yield on the nation's 10-year bonds rising today to a euro-era record of 16.45%. Portugal's debt and lack of growth is very similar to Greece. Its bonds are falling because it's very obvious to everyone that if there's a haircut for Greece, there might well be a haircut for Portugal too.

EU chiefs arrive in Brussels today to put the finishing touches on a German-led deficit-control treaty and to endorse the statutes of a €500 billion ($656 billion) rescue fund to be set up this year. Efforts to hold the 17-nation euro area together with bolstered fiscal rules and a stronger firewall are colliding with stalled progress in Greece. The increase in borrowing costs is dimming prospects in Portugal's ability to sell longer-term bonds in the public markets by the end of next year, as investors may be forced to endure writedowns before rescue funds from the EU run out in June 2014. Portugal GDP will contract 3.0% in 2012, the International Monetary Fund said in a December review of the Portuguese bailout plan.

Prime Minister Pedro Passos Coelho has said Portugal will adhere to targets set in the €78 billion bailout agreed to last year. Should Portugal's fiscal discipline fail to result in lower borrowing costs, international lenders may have to offer more support, he said at a January 24 press conference in Lisbon after meeting Spanish Prime Minister Mariano Rajoy. "If for external reasons that don't have to do with the fulfillment of the program, Portugal or Ireland aren't in a condition to return to market on the scheduled date, the IMF and the EU will maintain aid," Passos Coelho said.

Treasury Auction Highlights

In the new issue Treasury market, the U.S. Treasury Department auctioned $99 billion consisting of $35 billion in 2-year and 5-year notes on Tuesday and Wednesday, respectively and then $29 billion of 7-year notes on Thursday.

The U.S. Treasury Department sold $35 billion of 2-year notes at a yield of 0.25%, the highest since November. The yield on the 2-year notes was the highest since 0.28% November 21. At the December auction, the notes yielded 0.24%. The bid/cover ratio (which gauges demand by comparing the number of bids to the amount of securities sold) rose to 3.75 from 3.45 at the last 2-year note sale, indicating stronger demand. The bid/cover ratio was the highest since 4.07 at the November 21 auction. At the past six auctions of 2-year notes, bids were received for 3.69 times the amount of notes being sold, on average. Indirect bidders (a group that includes foreign central banks) bought 32.9% of the amount sold, compared with 21.6% in the prior auction.

The Treasury sold $35 billion in 5-year notes that was met with stronger-than-forecast demand ahead of the Federal Open Market Committee statement on the direction of U.S. monetary policy. The notes drew a yield of 0.899% with a bid-to-cover ratio of 3.17, the highest since May, versus an average of 2.863 for the previous 10 sales. Indirect bidders purchased 43.4% of the notes, compared with an average of 43.7% for the past 10 sales.

The Treasury sold $29 billion of 7-year notes at a record low yield of 1.359%, as demand rose relative to the last auction of securities with the same maturity. At the previous auction, the notes yielded 1.43%. The bid/cover ratio rose to 2.73 from 2.68 at the last 7-year note sale, indicating stronger demand. The bid/cover ratio was the highest since 3.20 at the November auction. Indirect bidders bought 31.8% of the amount sold, compared with 42.0% in the prior auction.

Fixed Income Sector Spreads

Sector	1/2/02	1/2/03	1/2/04	1/3/05	1/6/06	1/2/07	1/2/08	1/2/09	1/4/10	1/3/11	1/3/12	1/26/12
Agencies	n/a	36*	28*	41	36	25	47	103	34	27	52	46
Mortgages	71	37	31	26	52	37	87	147	17	42	75	71
Corporates	170	182	94	80	91	88	198	555	170	154	234	208
BABs***	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	201	218	230	202
High Yield	716	829	381	284	356	277	569	1,641	612	515	699	636

Fixed Income Sector Yields

Sector	1/2/02	1/2/03	1/2/04	1/3/05	1/6/06	1/2/07	1/2/08	1/2/09	1/4/10	1/3/11	1/3/12	1/26/12
Treasuries	4.52%	3.19%	3.36%	3.75%	4.40%	4.77%	3.59%	1.72%	2.46%	1.92%	1.03%	1.00%
Agencies	n/a	4.89%*	5.03%*	3.85%	4.77%	5.09%	4.15%	2.52%	2.27%	1.68%	1.22%	1.13%
Mortgages	6.41%	4.91%	5.02%	4.92%	5.46%	5.61%	5.36%	3.96%	4.14%	3.70%	2.68%	2.61%
Municipals	4.49%	3.73%	3.61%	3.63%	3.93%	3.94%	4.00%	4.52%	3.63%	3.80%	2.82%	2.56%
Municipals**	6.91%	5.74%	5.55%	5.59%	6.05%	6.06%	6.15%	6.95%	5.59%	5.85%	4.34%	3.94%
BABs***	n/a	n/a	n/a	n/a	n/a	n/a	n/a	n/a	6.59%	6.37%	5.00%	4.81%
Corporates	6.49%	5.25%	6.01%	4.69%	5.33%	5.65%	5.79%	7.67%	4.73%	4.04%	3.74%	3.49%
High Yield	12.48%	12.08%	7.37%	6.74%	8.21%	7.70%	9.64%	19.40%	9.00%	7.38%	8.36%	7.52%

*Fannie Mae Only
** Based on 35* Federal Income Tax Bracket
***Build America Bonds (Taxable Municipal Bonds)

Sources:
Barclay's Indices
Bloomberg News Service,

Economic Calendar

DATE	TIME	INDICATOR	CONSENSUS	PREV. REPORT
1/30	08:30	Personal Income	0.4%	0.1%
1/30	08:30	Personal Spending	0.1%	0.1%
1/30	08:30	PCE Deflator (YoY)	--	2.5%
1/30	08:30	PCE Core (MoM)	0.1%	0.1%
1/30	08:30	PCE Core (YoY)	1.7%	1.7%
1/31	08:30	Employment Cost Index 4Q	0.4%	0.3%
1/31	09:45	Chicago Purchasing Manager	63.0	62.2
1/31	10:00	Consumer Confidence	68.0	64.5
2/1	08:15	ADP Employment Change	185K	325K
2/1	10:00	Construction Spending (MoM)	0.7%	1.2%
2/1	10:00	ISM Mfg	54.5	53.9
2/1	10:00	ISM Prices Paid	49.8	47.5
2/1	--	Domestic Vehicle Sales	10.50M	10.45M
2/1	--	Total Vehicle Sales	13.55M	13.52M
2/2	08:30	Nonfarm Productivity 4Q P	1.0%	2.3%

2/2	08:30	Unit Labor Costs 4Q P	0.8%	-2.5%
2/2	08;30	Initial Jobless Claims	375K	377K
2/2	08:30	Continuing Claims	--	3554K
2/3	08:30	Change in Nonfarm Payrolls	150K	200K
2/3	08:30	Change in Private Payrolls	168K	212K
2/3	08:30	Change in Mfg Payrolls	10K	23K
2/3	08:30	Unemployment Rate	8.5%	8.5%
2/3	08:30	Avg Hourly Earning (MoM) All Emp	0.2%	0.2%
2/3	08:30	Avg Hourly Earning (YoY) All Amp	2.0%	2.1%
2/3	08;30	Avg Weekly Hours All Emp	34.4	34.4

Sources: Bloomberg

Financing Calendar

DATE	TERM	APPROX. YIELD	AMOUNT
1/30/12	3-Month	0.05	$31 bln
1/30/12	6-Month	0.08	$29 bln

Sources: Bloomberg

Bond Rating Changes

Upgrades	Rating Type	Agency	Current Rating	Last Rating
AmerCable Inc/AR	LT Local Issuer Credit	S&P	B- *-	B-
Electrical Components International Inc	LT Local Issuer Credit	S&P	B *-	B
Republic Mortgage Insurance Co	LT Local Issuer Credit	S&P	Ru	CCu
Mohegan Tribal Gaming Authority	LT Local Issuer Credit	S&P	CC *-	CCC *-
Trailer Bridge Inc	LT Local Issuer Credit	S&P	NR	D
Amerco Inc	LT Local Issuer Credit	S&P	NR	BB+
Natixis Financial Products LLC	LT Local Issuer Credit	S&P	A	A+ *-
Patriot Coal Corp	LT Local Issuer Credit	S&P	B+ *-	B+
SG Americas Securities LLC	LT Local Issuer Credit	S&P	A	A+ *-
Societe Generale Bank & Trust	LT Local Issuer Credit	S&P	A	A+ *-
Eastman Kodak Co	LT Local Issuer Credit	S&P	D	CCC- *-
River Rock Entertainment Authority/The	LT Local Issuer Credit	S&P	NR	D

Downgrades	Rating Type	Agency	Current Rating	Last Rating
AmerCable Inc/AR	LT Local Issuer Credit	S&P	B- *-	B-
Electrical Components International Inc	LT Local Issuer Credit	S&P	B *-	B
Republic Mortgage Insurance Co	LT Local Issuer Credit	S&P	Ru	CCu
Trailer Bridge Inc	LT Local Issuer Credit	S&P	NR	D
Amerco Inc	LT Local Issuer Credit	S&P	NR	BB+
Natixis Financial Products LLC	LT Local Issuer Credit	S&P	A	A+ *-
Patriot Coal Corp	LT Local Issuer Credit	S&P	B+ *-	B+
SG Americas Securities LLC	LT Local Issuer Credit	S&P	A	A+ *-
Societe Generale Bank & Trust	LT Local Issuer Credit	S&P	A	A+ *-
Eastman Kodak Co	LT Local Issuer Credit	S&P	D	CCC- *-
River Rock Entertainment Authority/The	LT Local Issuer Credit	S&P	NR	D
US AgBank FCB	LT Local Issuer Credit	S&P	NR	AA-

Sources: Bloomberg

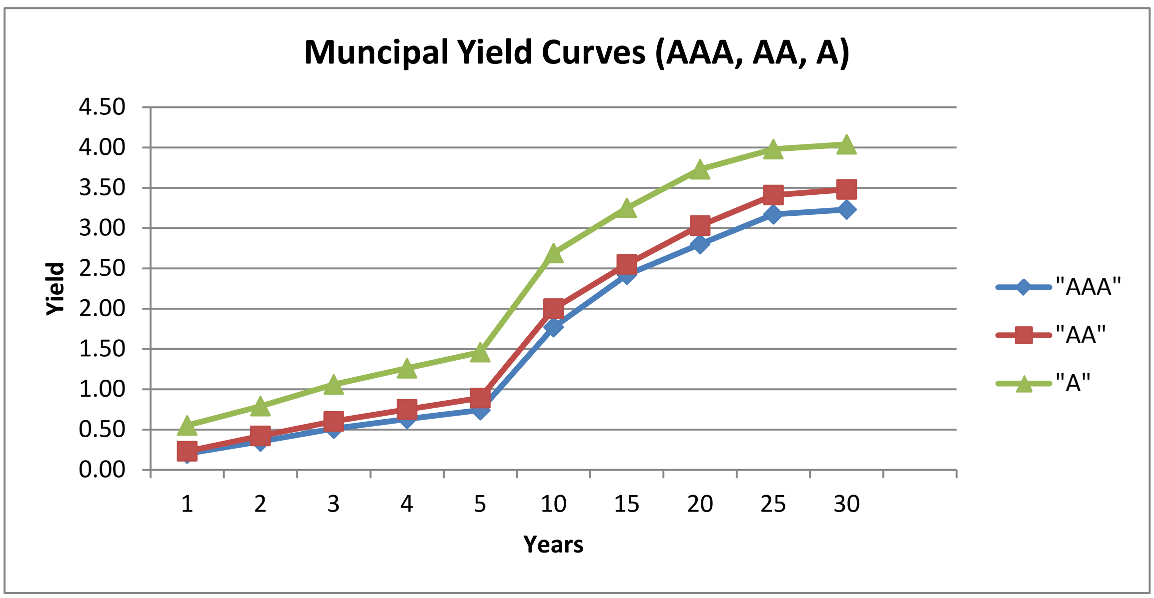
Treasury Yield

Sources: Bloomberg

For more information please contact your Financial Advisor.

Municipal Yield Curve

General Obligations - Yields as of 01/27/12							
Time (Yrs)	**Year**	**"AAA"**	**Pre-re**	**Insured**	**"AA"**	**"A"**	**"BAA"**
1	**2013**	0.20	0.20	0.39	0.23	0.55	1.40
2	**2014**	0.35	0.35	0.74	0.42	0.79	1.81
3	**2015**	0.51	0.51	1.01	0.60	1.06	2.11
4	**2016**	0.63	0.63	1.21	0.75	1.26	2.36
5	**2017**	0.74	0.73	1.39	0.89	1.46	2.57
10	**2022**	1.77		2.57	2.00	2.69	3.77
15	**2027**	2.42		3.13	2.55	3.25	4.20
20	**2032**	2.80		3.61	3.03	3.73	4.55
25	**2037**	3.17		3.86	3.41	3.98	4.75
30	**2042**	3.23		3.92	3.48	4.04	4.82



Please note that these levels are representative of institutional net levels, and do not reflect retail sales credit.
These yields should be used as general market indicators only.

Source: **Municipal Market Data**

SUMMARY OF KEY FIXED INCOME MARKET INFORMATION

WEEK ENDING : 1/27/2012

		TODAY	WEEK AGO	MONTH AGO	YEAR AGO
BOND BUYER REVENUE INDEX		4.71%	4.77%	na	5.61%
BOND BUYER 20-BOND INDEX		3.68%	3.60%	na	5.25%
BOND BUYER 11-BOND INDEX		3.42%	3.34%	na	5.00%
REPRESENTATIVE MUNICIPAL BOND YIELDS					
(Source: Bloomberg)					
'AAA' RATED G.O.s	2 Year	0.34%	0.34%	na	0.74%
	5 Year	0.87%	0.84%	na	1.91%
	10 Year	2.00%	1.91%	na	3.58%
	15 Year	3.09%	3.08%	na	4.32%
	30 Year	3.59%	3.55%	na	4.98%
PRIME RATE (Source: Bloomberg)		3.25%	3.25%	na	3.25%
DISCOUNT RATE (Source: Bloomberg)		0.75%	0.75%	na	0.75%
FEDERAL FDS AVG (Source: Bloomberg)		0.25%	0.25%	na	0.25%
COMMERCIAL PAPER	30 Day	0.07%	0.09%	na	0.19%
{PRIME ISSUERS}	60 Day	0.10%	0.13%	na	0.22%
Bond Equivalent Yield	90 Day	0.11%	0.14%	na	0.24%
(Source: Bloomberg)					
AGENCY DISCOUNT NOTES *	30 Day	0.03%	0.02%	na	0.13%
Bond Equivalent Yield	60 Day	0.04%	0.04%	na	0.14%
	90 Day	0.05%	0.05%	na	0.16%
TAXABLE 7-DAY FLOATER		0.32%	0.33%	na	0.94%
(Source: Robert W. Baird & Co.)					
TAX FREE 7-DAY FLOATER	Non-AMT	0.08%	0.07%	na	0.29%
(Source: Robert W. Baird & Co.)	AMT	0.18%	0.17%	na	0.71%
U.S. TREASURY BILLS	3 Month	0.05%	0.05%	na	0.14%
Bond Equivalent Yield	6 Month	0.07%	0.07%	na	0.16%
(Source: Bloomberg)					
GOVERNMENTS	2 Year	0.21%	0.24%	na	0.59%
(Source: Bloomberg)	5 Year	0.76%	0.88%	na	1.98%
	10 Year	1.92%	2.02%	na	3.37%
	30 Year	3.09%	3.08%	na	4.56%
CORPORATE 'A' FINANCE YIELDS					
(Source: Bloomberg)	2 Year	1.68%	1.66%	na	1.73%
	5 Year	2.53%	2.61%	na	3.47%
	10 Year	4.08%	4.11%	na	4.83%
	30 Year	5.41%	5.34%	na	5.91%
CORPORATE 'A' UTILITY YIELDS					
(Source: Bloomberg)	2 Year	1.33%	1.34%	na	1.76%
	5 Year	2.05%	2.17%	na	3.12%
	10 Year	3.48%	3.58%	na	4.59%
	30 Year	4.41%	4.43%	na	5.78%
CORPORATE 'A' INDUSTRIAL YIELDS					
(Source: Bloomberg)	2 Year	0.61%	0.68%	na	0.99%
	5 Year	1.57%	1.74%	na	2.60%
	10 Year	3.10%	3.22%	na	4.36%
	30 Year	4.31%	4.36%	na	5.60%
CDs	1 Year	0.40%	0.40%	na	0.35%
(Source: Robert W. Baird & Co.)	2 Year	0.85%	0.95%	na	0.80%
	5 Year	1.75%	1.90%	na	2.00%
	10 Year	3.00%	2.90%	na	3.00%

* Yields presented represent the prevailing market price as of 1/26/2012 and are not representative of a specific issue.

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