

Weekly Trading Desk Update

December 19, 2011

	Current Wk	Prior Wk
Weekly Municipal		
(\$ Bln)		
Negotiated	\$0.37	\$3.79
Competitive	\$0.54	\$1.57
TOTAL	\$0.90	\$5.36
Municipal 30 Day Visible Supply (\$ Bln)	\$4.23	\$8.94
Bloomberg Municipal PICK Offerings Par (\$ Bln)	\$9.15	\$10.70
Municipal Placement Ratio (New Issues)	95.40%	89.50%
Bond Buyer 20 Municipal G.O. Index	3.92%	3.93%

Freasury Supply		Current Auction	Prior Auction	
Day	Maturity	Amount (\$ Bln)	Amount (\$Bln)	
Mon	2 Year	35	35	
Tues	5 Year	35	35	
Wed	7 Year	29	29	
	TOTAL	99	99	

Select F	Conomic Releases			
Date	Event	Period	Survey	Prior
12/20	Housing Starts	NOV	635K	628K
12/20	Building Permits	NOV	635K	653K
12/21	MBA Mortgage Applications	16-Dec		4.10%
12/21	Existing Home Sales	NOV	5.09M	4.97M
12/22	GDP QoQ (Annualized)	3Q T	2.00%	2.00%
12/22	Initial Jobless Claims	17-Dec	378K	
12/22	Continuing Claims	10-Dec	3600K	
12/22	U. of Michigan Confidence	DEC F	68.00	67.70
12/22	Leading Indicators	NOV	0.30%	0.90%
12/23	Durable Goods Orders	NOV	2.00%	-0.70%
12/23	Personal Income	NOV	0.20%	0.40%
12/23	Personal Spending	NOV	0.30%	0.10%
12/23	PCE Core (YoY)	NOV	1.70%	1.70%
12/23	New Home Sales	NOV	315K	307K

Trading Desk Commentary

In 2011's final Federal Open Market Committee session last Tuesday, the Fed kept its target borrowing rate unchanged (O to 0.25%), which came as a surprise to exactly no one. Last Friday marked the 3-year anniversary since the Fed set the target rate at the near-zero mark as the economy and credit conditions had entered a tailspin. Though the Fed's most recent press release emitted a slightly more optimistic tone in regards to domestic growth prospects, the "significant downside risks" were enough to warrant further extension of the accommodative monetary policy.

Less than \$7bln in new issuance was added to the Muni market last week, still well below the current demand driven by attractive Muni-to-TSY ratios and December reinvestment activity. December's Muni supply has been lighter than anticipated and now that we have reached the two-week period surrounding the Christmas holiday, issuers have effectively shut down until after the New Year. This week, supply will be virtually non-existent and activity should be extremely slow (increasingly so as the week progresses) and in to the following holiday-shortened week that will close out the year. Furthermore, a lighter January supply picture has been evolving over the past few weeks. January is yet another month that must typically contend with lively reinvestment activity, suggesting the supply-demand imbalance could continue in to 2012. Strong tax-exempt demand has placed Munis in the midst of a 9-week rally, 63 basis points (0.63%) lower at the 10-yr AAA spot than the mid-October highs, a new record low for the 10-yr Muni scale (MMD).

The uncertainty surrounding the timing of more supply coming to market makes today feel very reminiscent of late September. Muni yields had been pushed sharply higher at the start of this year in response to claims that potential systemic risks were lurking just below that surface of the asset class and widespread defaults were developing in to a real threat. After these claims were labeled unfounded and worries began to dissipate, money returned to the Muni market in droves as investors recognized the value that had been created by the recent sell-off. Furthermore, belt-tightening by municipalities had shelved a large amount of the issuance typically seen in a given year. Yields moved ever-lower and participants began to focus on when supply would grow; predicting that the low yields could not withstand more historically normal supply - whenever it finally arrived. Once issuers reentered the market to seize all-time low borrowing costs, yields buckled and Munis weakened quickly. Today, as we approach year-end, we acknowledge some similarities. We are now at all-time lows that make the yield environment at the beginning of the 2011 look positively cheap. Munis have strengthened for the better part of two months and a lack of planned issuance in the coming weeks is keeping buyers engaged. This has put us back into familiar territory as we enter 2012 - looking for a sign of oncoming tax-exempt issuance with a sneaking suspicion that yields will not be sustainable if and when it finally arrives.

Rates	Current Wk	Yld Change	Prior Wk	Muni to Treasury Ratio
Muni's		-		· ·
2 Year	0.36	0.00	0.36	164%
5 Year	0.93	-0.02	0.95	118%
10 Year	1.93	-0.04	1.97	104%
30 Year	3.62	-0.07	3.69	127%
UST				
2 Year	0.22	0.00	0.22	
5 Year	0.79	-0.10	0.89	
10 Year	1.85	-0.21	2.06	
30 Year	2.85	-0.25	3.10	

Explanation of Key Measures:

Weekly Municipal Supply - The total dollar volume of municipal securities expected to be offered during the upcoming week, broken down by deal type. This helps gauge near term supply and momentum along with the 30 day visible figure.

30 Day Visible Supply - The total dollar volume of municipal securities expected to be offered over the next 30 days. The visible supply, which is compiled and published by The Bond Buyer, indicates the near-term activity in the municipal market.

Bloomberg PICK Offerings - The total dollar amount of offerings listed on Bloomberg's dealer offerings system. The figure helps gauge secondary supply in the market.

Placement Ratio - The amount of bonds sold by underwriting syndicates each week as a percentage of the amount issued that week by issuers selling \$1,000,000 par value or more of securities. The ratio published by The Bond Buyer , helps gauge the demand for municipal bonds in the marketplace.

Bond Buyer 20 G.O. Index - Index published weekly representing the average yield of 20 G.O. bonds with 20 year maturities, rated AA2 by Moody's

Sources: Weekly municipal supply figures, and municipal rates are produced by Thompson Reuter (Municipal Market Data), 30 day visible figures, and the placement ratio are obtained through The Muni Center, and produced by The Bond Buyer. The 20 G.O. index yield is obtained through Bloomberg, and produced by The Bond Buyer. Pick offerings par value, UST supply, economic releases, and UST rates are obtained through Bloomberg Professional Service. Information obtained from these sources is believed to be reliable but is not guaranteed.

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