

Weekly Trading Desk Update

January 9, 2012

	Current Wk	Prior Wk
Weekly Municipal (\$ Bln)		
Negotiated	\$2.15	\$0.38
Competitive	\$1.82	\$0.18
TOTAL	\$3.97	\$0.56

Municipal 30 Day Visible Supply (\$ Bln)	\$7.38	\$4.25
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Bloomberg Municipal PICK Offerings Par (\$ Bln)	\$10.44	\$9.61
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Municipal Placement Ratio (New Issues)	89.80%	n/a
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Bond Buyer 20 Municipal G.O. Index	3.83%	3.88%
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Treasury Supply		Current Auction	Prior Auction
Day	Maturity	Amount (\$ Bln)	Amount (\$Bln)
Tues	3 Year	32	32
Wed	10 Year	21	21
Thurs	30 Year	13	13
TOTAL		66	66

Select Economic Releases				
Date	Event	Period	Survey	Prior
1/11	MBA Mortgage Applications	6-Jan	--	-4.10%
1/11	Fed's Beige Book			
1/12	Advance Retail Sales	DEC	0.30%	0.20%
1/12	Retail Sales Ex Auto & Gas	DEC	0.30%	0.20%
1/12	Initial Jobless Claims	7-Jan	375K	372K
1/12	Continuing Claims	31-Dec	3575K	3595K
1/12	Business Inventories	NOV	0.40%	0.01
1/13	Import Price Index (MoM)	DEC	-0.10%	0.70%
1/13	Import Price Index (YoY)	DEC	8.30%	9.90%
1/13	Trade Balance	NOV	-\$45.0B	-\$43.5B
1/13	U. of Michigan Confidence	JAN P	71.50	69.90

Trading Desk Commentary

The first trading week of 2012 showed that the weak supply/strong demand dynamic established in 2011 would continue to drive tax-exempt performance despite the start of a new calendar year. At the end of December, AAA Muni yields tested their resistance levels from the 5-30 year maturity range (set in August of last year) and then finally broke through those levels to set new records. Though we have since weakened (very slightly) since year end, we are still bouncing around the lowest yields ever posted. Thus far, however, investors remain undeterred.

As mentioned last week, roughly \$20bln of reinvestment activity is expected in January, not including the billions of dollars that did not get invested in December due the previous month's scant issuance. As of Friday, planned Muni issuance for the next 30 days was in the \$6bln range, which would not come close to satisfying investor demand should this number not grow. As a result, those looking for an avenue to participate in tax-exempts are being forced to search out other channels.

For the week ending January 4, according to Lipper U.S. Fund Flows data, Municipal bond mutual funds saw \$1.9bln inflows, the second highest weekly total in a year. The famous outflows from Muni bond funds in late 2010-early 2011 have become a very distant memory. Concurrently, the three intermediate duration National Muni ETF's that we closely track (MUB, ITM, TFI) are all currently trading at all-time highs since their respective inceptions.

What does this all mean? For one, the Muni supply picture is going to require close surveillance. At some point, issuers will likely return to the debt markets to take advantage of historically attractive borrowing rates. If supply begins to creep up closer to current demand, we could see a sharp move to higher rates à la September-October of last year. It is also concerning that the first 5 years (approx.) of the Muni curve have not traded through their August 2011 yield lows, suggesting that Muni yields may soon run out of room to tighten any further. However, at this point it is too early to become overly defensive. There is still plenty of money waiting to gain access to the Muni market and Europe's struggles continue to create a need for safer assets. Furthermore, ratios in the longer and shorter parts of the yield curve are still attractive (the 7-10 year range has lost most of its earlier value relative to UST's). For these reasons and the weak forward supply, Munis appear to have a fairly stable short-term outlook. The uncertainties lie a little further in the future. Needless to say, the year is off to an interesting start.

Rates	Current	Yld	Prior	Muni to Treasury Ratio
	Wk	Change	Wk	
Muni's				
2 Year	0.42	0.06	0.36	162%
5 Year	0.87	0.02	0.85	102%
10 Year	1.85	-0.01	1.86	94%
30 Year	3.50	-0.06	3.56	116%
UST				
2 Year	0.26	0.00	0.26	
5 Year	0.85	0.00	0.85	
10 Year	1.96	0.10	1.86	
30 Year	3.01	0.14	2.87	

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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