

Trading Desk Commentary

US Treasuries closed out the week with a roller coaster finish which saw the 10-year spot jump 13 basis points higher on Thursday only to retrace the majority of those losses on Friday. The two-day period illustrates the current mindset in fixed income – it's all about the Fed. And the Fed has painted itself into a corner, or maybe it has the market right where it wants it. As we have mentioned, market participants have become extremely data dependent, especially towards the housing and labor sectors. Inflation is so low right now that the market is, for the most part, ignoring inflation indicators until the data starts showing more signs of upward pressure. For now, all eyes are watching jobs numbers given the Fed's explicit emphasis on supporting better employment data. Concurrently, further recovery in housing remains critical to the restoration of wealth in this country, so the significant growth in home prices since the beginning of the year has been a bright spot in 2013. However, participants are rightfully concerned that as the likelihood of the tapering grows (or at least in the market's best estimation), so too will mortgage rates as a function of their strong correlation with the 30-year US Treasury bond. This puts the Fed atop a very narrow tightrope. Bernanke and his predecessor will be forced to balance the Fed's reduction in asset purchasing with the resulting increase in interest rates that could choke off one of the keystones to the ongoing recovery. Some bothersome housing data that has hit the tape in recent weeks likely factored into the Fed's decision to avoid the dreaded "taper" talk. The Fed showed no signs of slowing its stimulus in the very near future. If anything, the Fed tweaked its language to intonate that downside risks to the economy may have actually gathered a bit of momentum and are a greater concern today than six weeks ago. But through its communications with the public, the Fed has shown it can steer markets or at the very least "test the waters" before unveiling major shifts in Fed policy. This is a powerful tool in its own right and one that the Fed is not afraid to use. The Fed is more transparent under Bernanke versus the Greenspan days – a positive development. But this has also effectively provided the Fed with another arrow in its quiver. Given the weight that economic data and the Fed's words currently carry, one simply cannot afford to ignore them.

A manageable supply week and the reality of a summer Muni market allowed tax-exempts a more peaceful week than experienced by its taxable counterparts. Activity still feels light in both the primary and secondary markets, though new issuance continues to find an audience each week. Munis are offering significant value relative to US Treasuries, likely supporting crossover activity. However, the major concern for the Municipal space remains the weekly divestments in Municipal bond mutual funds. Since the beginning of the year, Muni funds have now lost over \$18bn (in excess of \$2bn over just the last week). The risk of higher interest rates and splashy credit headlines specific to Muniland have outflows snowballing which introduces increased selling pressure into the system. A wide array of deal sizes and types comprise next week's expected \$7.3bn in new supply, but general rate volatility should continue to dictate interest in debt markets. A firm US Treasury backdrop remains the primary driver of better interest in Muni debt. We remain defensive against the risks posed by potential rate volatility but continue to selectively purchase Munis within this framework when we pinpoint opportunity.

Muni Rates	Current Wk	Yld Change	Prior Wk	Muni to UST
2 Year	0.43	0.00	0.43	145%
5 Year	1.31	0.04	1.27	96%
10 Year	2.71	0.01	2.70	104%
30 Year	4.22	0.01	4.21	114%
UST Rates				
2 Year	0.30	-0.01	0.31	
5 Year	1.36	-0.01	1.37	
10 Year	2.61	0.05	2.56	
30 Year	3.69	0.07	3.62	

	Current Wk	Prior Wk
Weekly Municipal Supply (\$ Bln)		
Negotiated	\$4.18	\$3.39
Competitive	\$2.42	\$1.30
TOTAL	\$6.60	\$4.69

Municipal 30 Day Visible Supply (\$ Bln)	\$11.14	\$9.56
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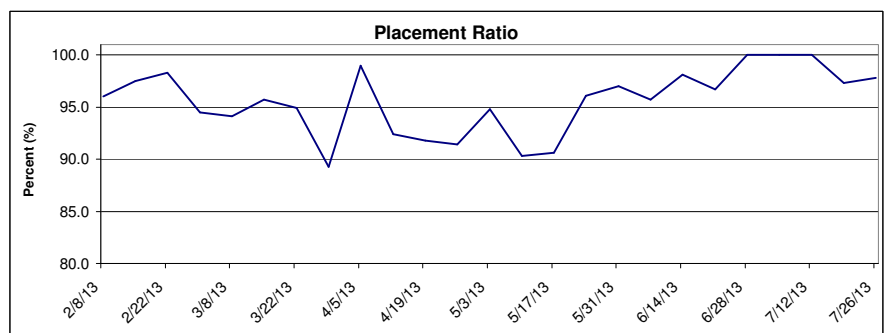
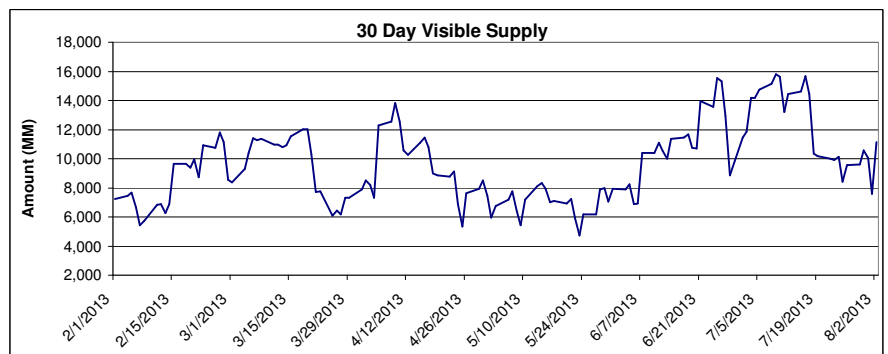
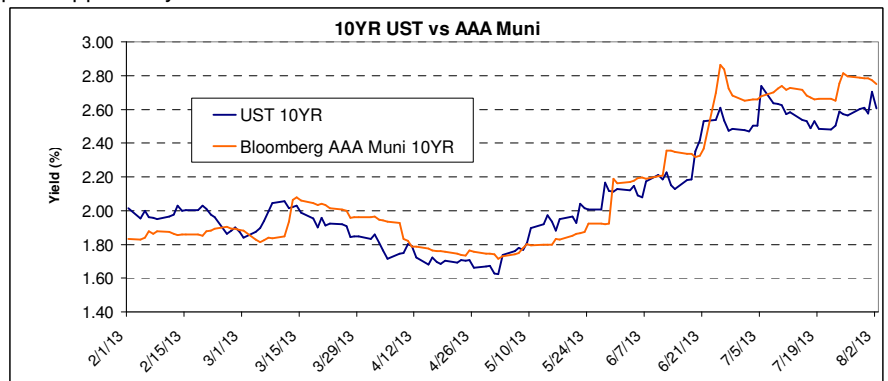
Bloomberg Muni PICK Offerings (\$ Bln)	\$15.32	\$17.13
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Muni Placement Ratio (New Issues)	n/a	97.8%
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Bond Buyer 20 Municipal G.O. Index	4.70%	4.77%
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Select Economic Releases

Date	Event	Period	Survey	Prior
8/6	Trade Balance	Jun	-\$43.3B	-\$45.0B
8/7	MBA Mortgage Applications	2-Aug	--	-3.7%
8/8	Initial Jobless Claims	3-Aug	336K	326K
8/8	Continuing Claims	27-Jul	2945K	2951K
8/9	Wholesale Inventories MoM	Jun	0.40%	-0.50%



Caprin Strategy Summary

Name	Target Duration Position	Target Maturity Range	Highlights
Short Maturity Muni	Min  Max	0 YRS  5 YRS	Prefer Hlth, Hsg, Pwr to G.O.'s for Yield
Low Duration Taxable	Min  Max	0 YRS  5 YRS	Prefer Corporates and Taxable Munis
Intermediate Muni	Min  Max	0 YRS  17 YRS	Prefer Hlth, Hsg, Pwr to G.O.'s for Yield
Intermediate Taxable	Min  Max	0 YRS  12 YRS	Prefer Corporates and Taxable Munis
Tactical Muni ETF	Min  Max		Slight Overweight to CA and NY
Core Plus ETF	Min  Max		Slight Overweight to Corporates and BABs
Tactical Opportunity ETF	Min  Max		Slight Overweight Munis, Underweight Taxables

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 MuniCenter, 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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