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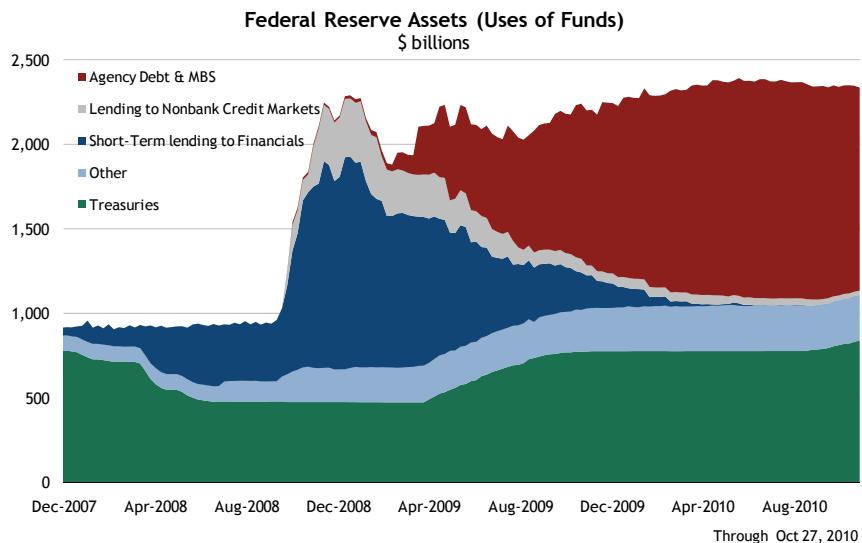
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Federal Reserve

Summary

The balance sheet contracted \$9.9 billion for the week ended October 20.

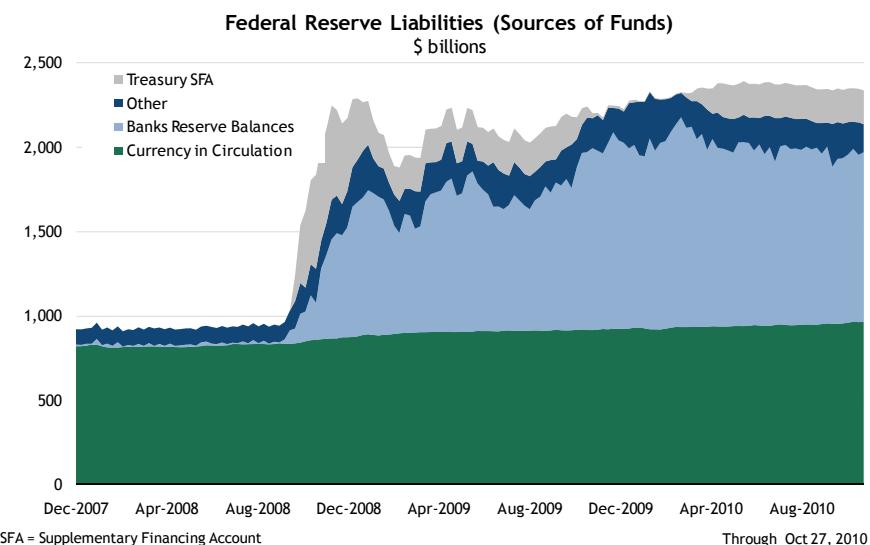


Source: Federal Reserve Board

- Treasuries continued to replace MBS on the balance sheet, growing by \$5.7 billion. Agency debt and MBS together declined \$15.7 billion.

On the liabilities side of the balance sheet, bank reserve balances grew by \$15.5 billion.

The decrease was more than offset by a \$25 billion decrease in Treasury deposits with Federal Reserve banks.



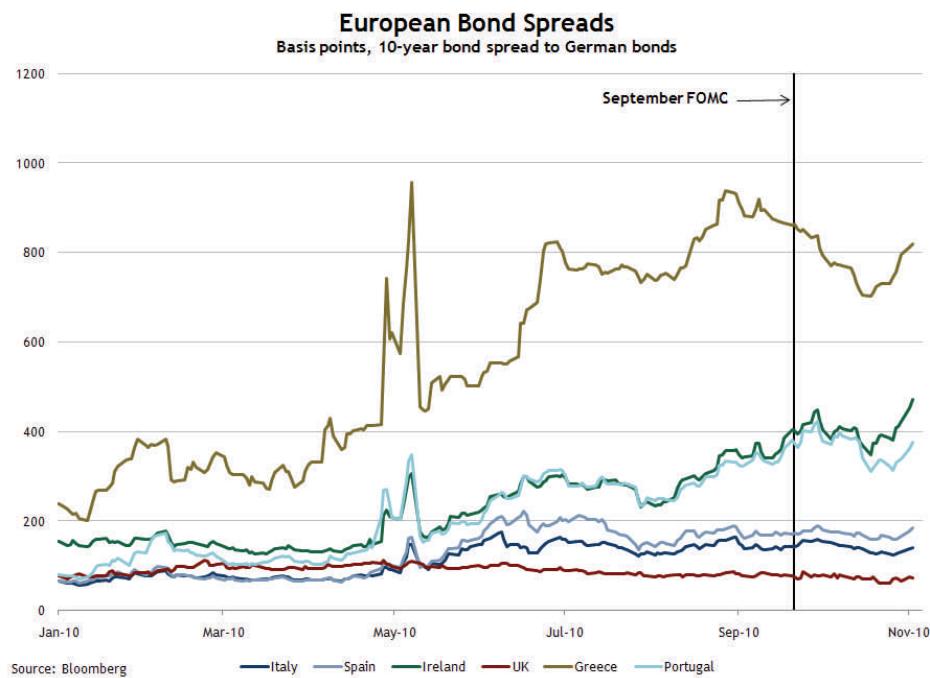
Source: Federal Reserve Board

Assets: Lending to nonbanks—TALF, CPFF, AMLF, and MMIF; Short-term lending to financials—discount window, TAF, currency swaps, PDCF, and repos; Misc.—Maiden Lanes I, II, and III, credit to AIG, and other Fed assets. **Liabilities:** Other—Reverse repos, Treasury cash holdings, and deposits with Federal Reserve Banks other than reserve balances and excluding the Supplementary Financing Program.

European Debt

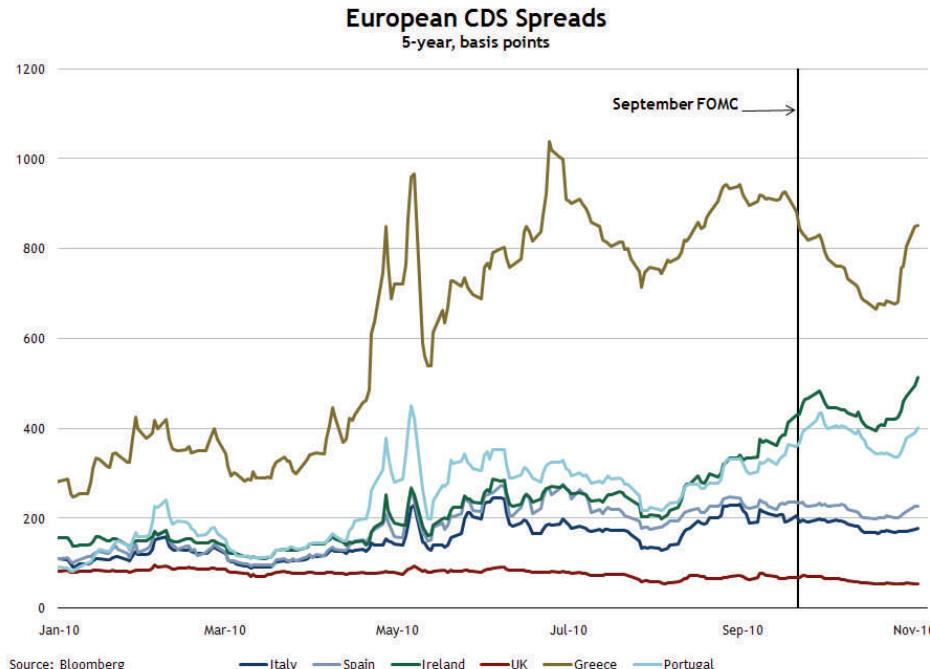
Summary

Some peripheral European bond spreads (over German bonds) continue to be elevated, particularly those of Greece, Ireland, and Portugal.



- Since the September FOMC meeting, the 10-year Greece-to-German bond spread has narrowed by 45 basis points (bps), from 8.62% to 8.17%, though the spread has risen by 110 bps in the past two weeks.
- Similarly, with other European peripherals' spreads, Portugal's is essentially unchanged over the intermeeting period but is 56 bps higher than two weeks prior, and Ireland's spread is actually 70 bps higher since the last FOMC meeting and 100 bps higher since October 19.

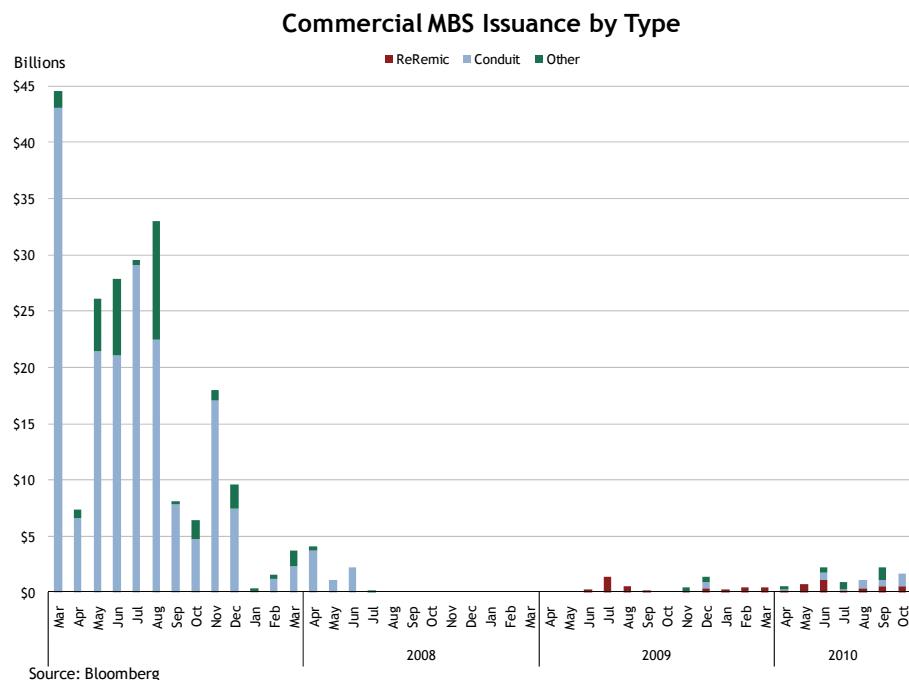
Similarly, CDS spreads have widened recently after several weeks of stabilization.



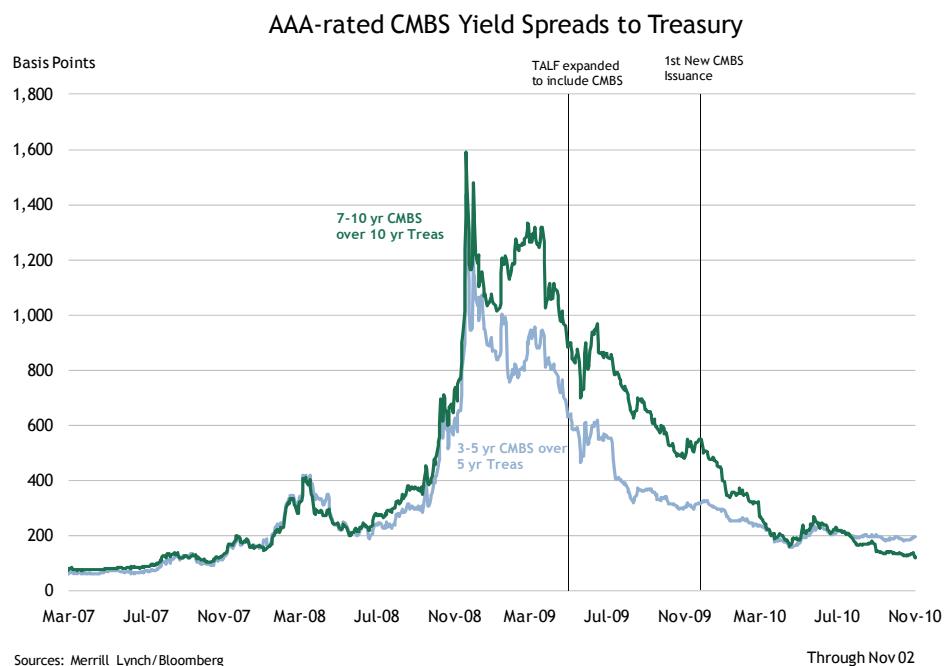
Securitization Markets

Summary

Issuance of commercial MBS remains very low; however, there was a large conduit deal in October and several in the pipeline for November.



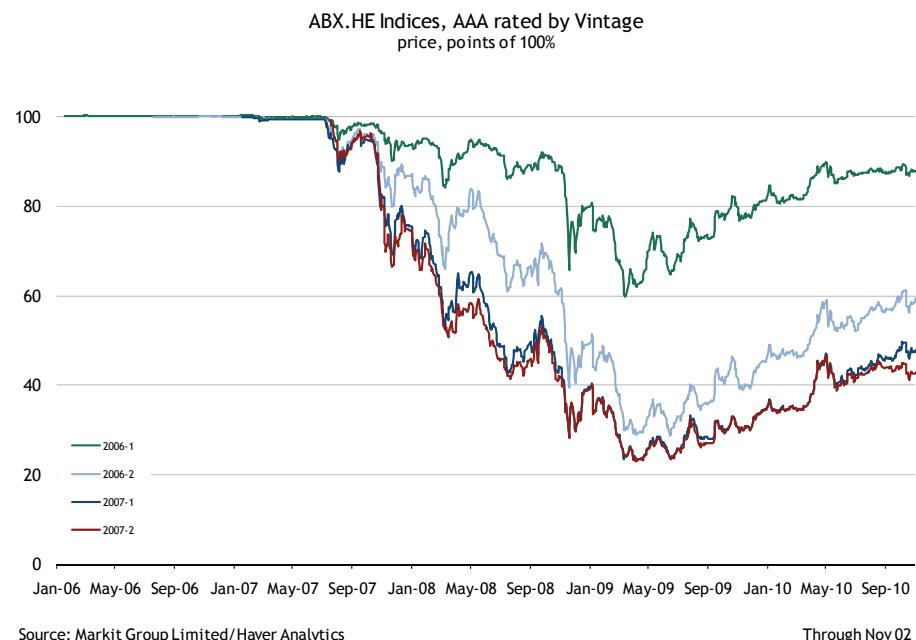
Top rated three-to-five-year CMBS yield spreads over five-year Treasuries have been stable since June. Yield spreads on seven-to-10-year CMBS over 10-year Treasuries have declined in recent months.



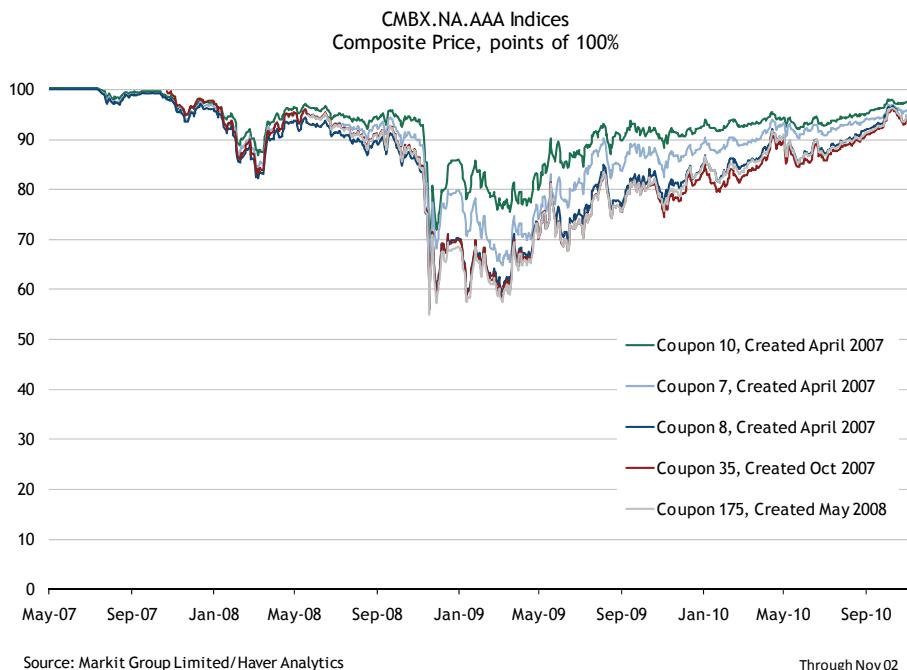
Securitization Markets

Summary

The ABX continues to rise across all vintages, indicating a decline in the cost to insure against default on the underlying home equity loans.



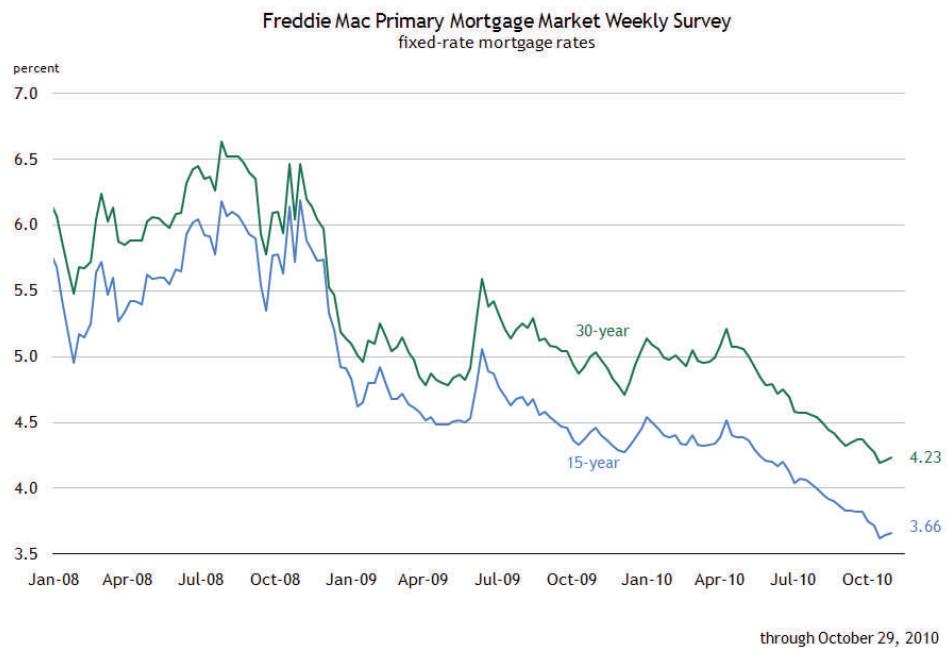
The same is true for the index value of commercial MBS credit default swaps. All vintages of the CMBX.NA.AAA continue to rise, indicating a lower cost to insure against default of commercial MBS.



Mortgage Rates

Summary

The 30- and 15-year fixed mortgage rates edged up slightly for the second consecutive week; both are up from the record lows set for the week ended October 15.



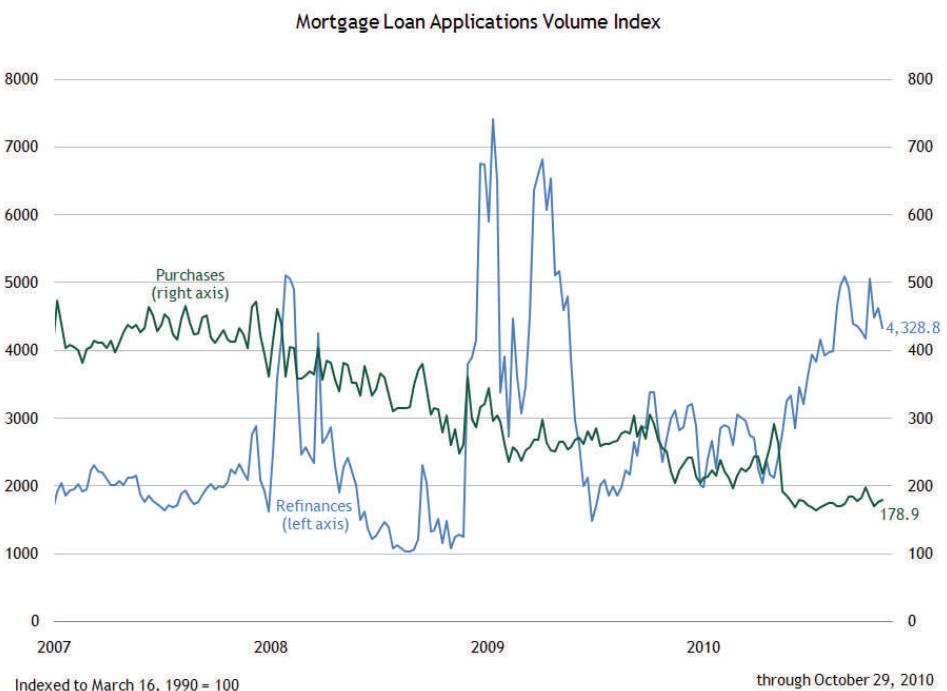
Source: Federal Home Loan Mortgage Corporation/Haver Analytics

- The 30-year fixed rate averaged 4.23%, up slightly from 4.21% a week ago. At this time last year the 30-year fixed rate averaged 5.03%.
- The 15-year fixed rate averaged 3.66%, up slightly from 3.64% a week ago. At this time last year the 15-year fixed rate mortgage averaged 4.46%.

Mortgage purchase applications increased last week, and the purchase index rose 1.4% from the week earlier.

The refinance index decreased 6.4% from the previous week, marking the third straight weekly decline.

The purchase index and refinance index are measures of loan application volume reported in the MBA's Weekly Application Survey. The survey has been conducted weekly since 1990 and covers more than 50 percent of all U.S. retail residential mortgage applications.



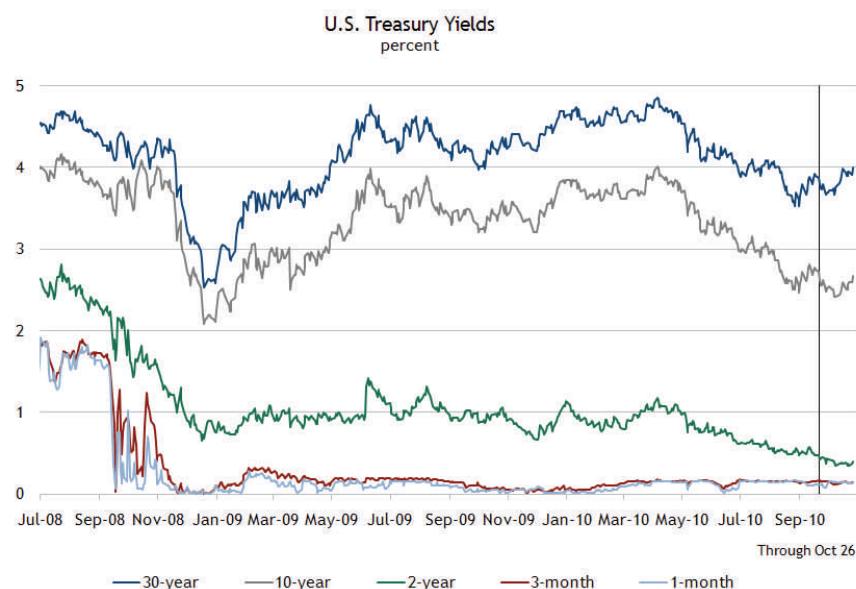
Source: Mortgage Bankers Association/Haver Analytics

- The refinance share of mortgage activity decreased slightly to 81.3% from 82.3% the previous week.

Broad Financial Market Indicators

Summary

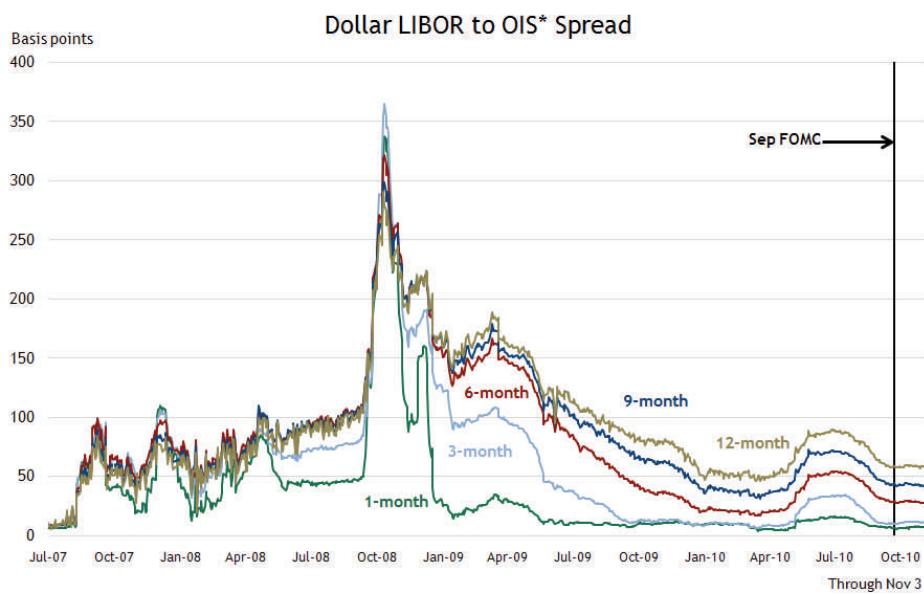
The two-to-30 year part of the yield curve has steepened further since the September FOMC meeting, with the two-year hitting an all-time series low.



Source: Federal Reserve Board/Haver Analytics

- Thirty-year Treasury bonds have risen 22 bps to 4.01% since the September FOMC meeting, while the 10-year notes are up only 5 bps to 2.66%, and the 2-year declined 9 bps to 0.34%, an all-time low going back to 1976.

LIBOR to OIS spreads are relatively unchanged since the September FOMC meeting, as all tenors have changed less than 2 basis points in either direction.



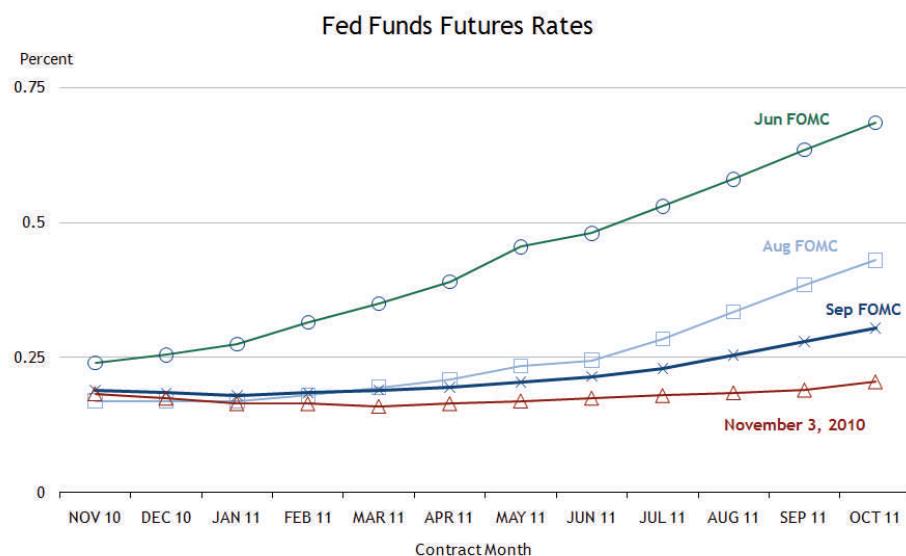
Source: British Bankers Association/Bloomberg

*Overnight Index Swap rate

Broad Financial Market Indicators

Summary

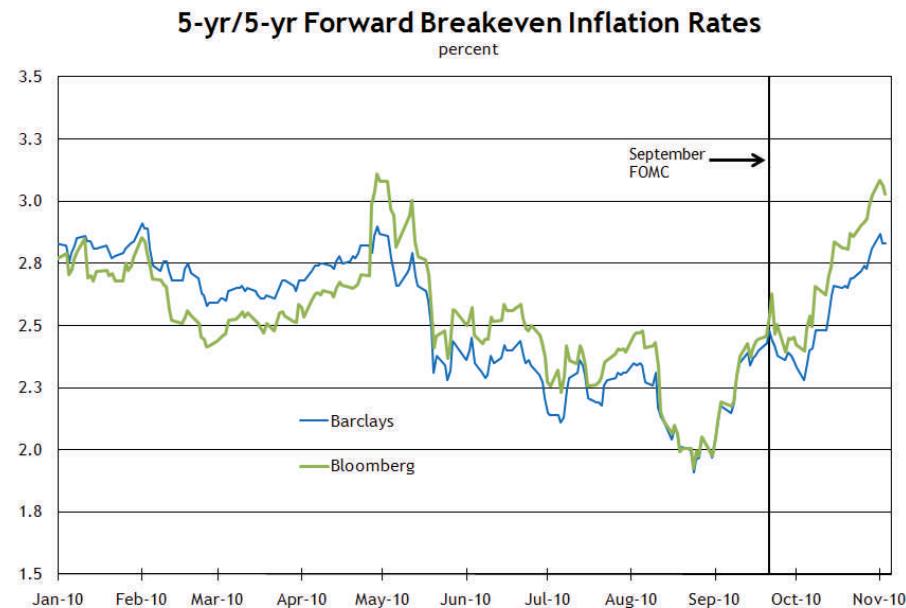
The curve of expected rates from the fed funds futures market has moved even lower in the intermeeting period.



Source: Bloomberg

- The fed funds futures markets currently does not expect a rate increase in 2011.
- As of November 3, the futures market for fed funds indicates an implied rate of about 21 bps for the October 2011 contract, nearly 50 bps lower than what was expected around the time of the June 2010 FOMC meeting.

Break-even inflation rates have risen about a third of a percentage point since the last FOMC meeting.



Source: Bloomberg/Barclays

- One measure calculated by Barclays suggests investors see CPI inflation five to 10 years out as averaging about 2.83%, which is up 35 bps from the last FOMC meeting.