

## Financial Highlights

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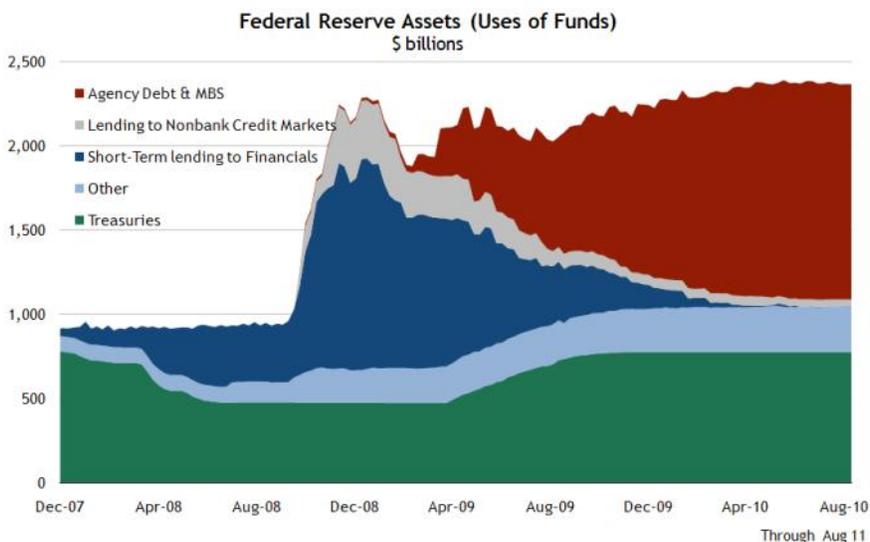
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# Federal Reserve

## Summary

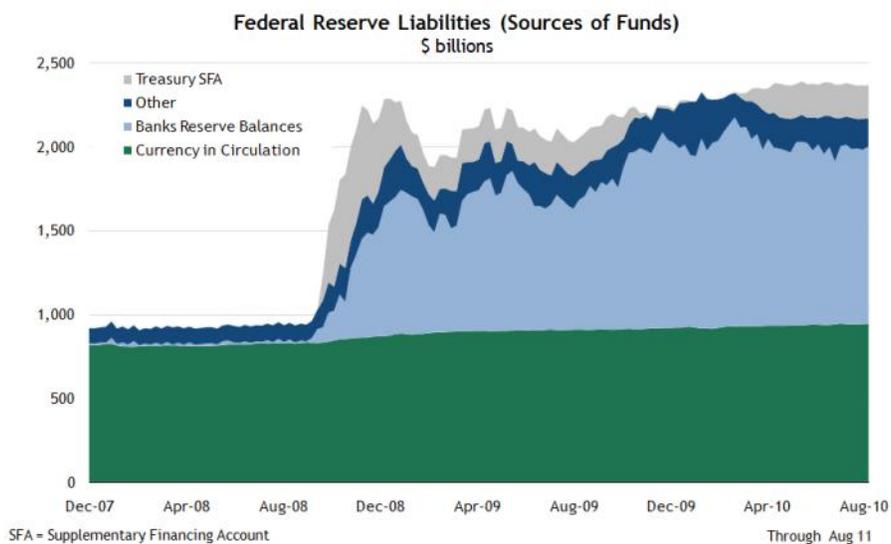
The balance sheet remained essentially unchanged, increasing by \$1.1 billion for the week ending August 11.



Source: Federal Reserve Board

- MBS on the balance sheet increased by \$1.7 billion.

Bank reserve balances increased by \$18 billion, offsetting a \$17 billion decline in Treasury deposits at Federal Reserve banks.



Source: Federal Reserve Board

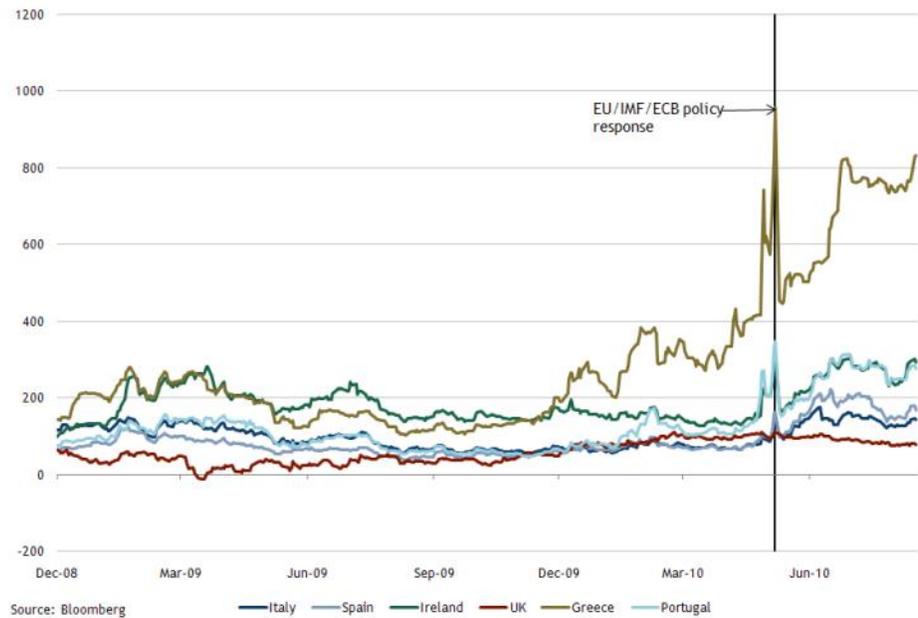
**Assets:** Lending to nonbanks—TALF, CPFF, AMLF, and MUIFF; Short-term lending to financials—discount window, TAF, currency swaps, PDCF, and repos; Misc.—Maiden Lanes I, II, and III, credit to AIG, and other Fed assets. **Liabilities:** Other—Reverse repos, Treasury cash holdings, and deposits with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

# European Debt

## Summary

Peripheral European bond spreads over German bonds remain volatile and elevated.

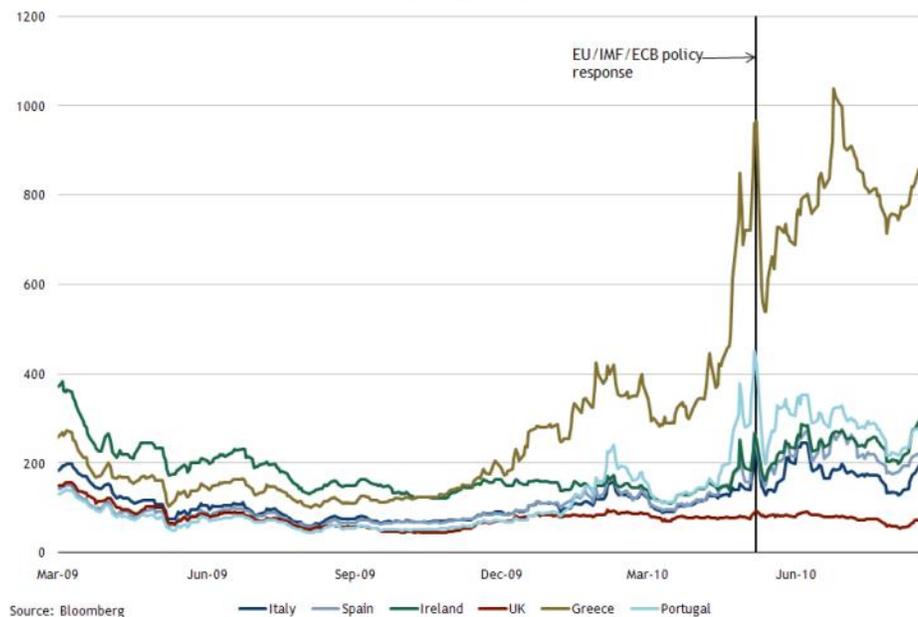
**European Bond Spreads**  
Basis points, 10-year bond spread to German bonds



- Since August 9, the 10-year Greece-to-German bond spread has risen 93 basis points (bps) through August 17. Likewise, Portugal's bond spreads rose 32 bps, Italy's rose 16 bps, Spain's rose 21 bps, and Ireland's rose 42 bps during the same period.

Similarly, CDS spreads have widened.

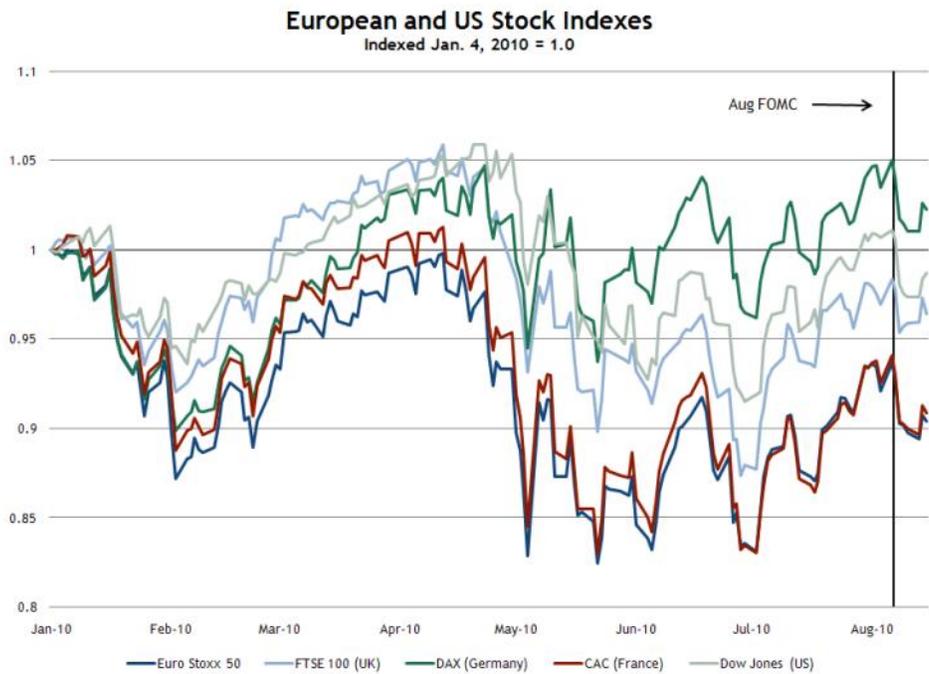
**European CDS Spreads**  
5-year, basis points



# Bond and Equity Markets

## Summary

Equity markets in Europe and the United States remain volatile and are, except for the DAX (Germany), lower year to date.



Source: Bloomberg



Source: Merrill Lynch, Wall Street Journal

# Bond and Equity Markets

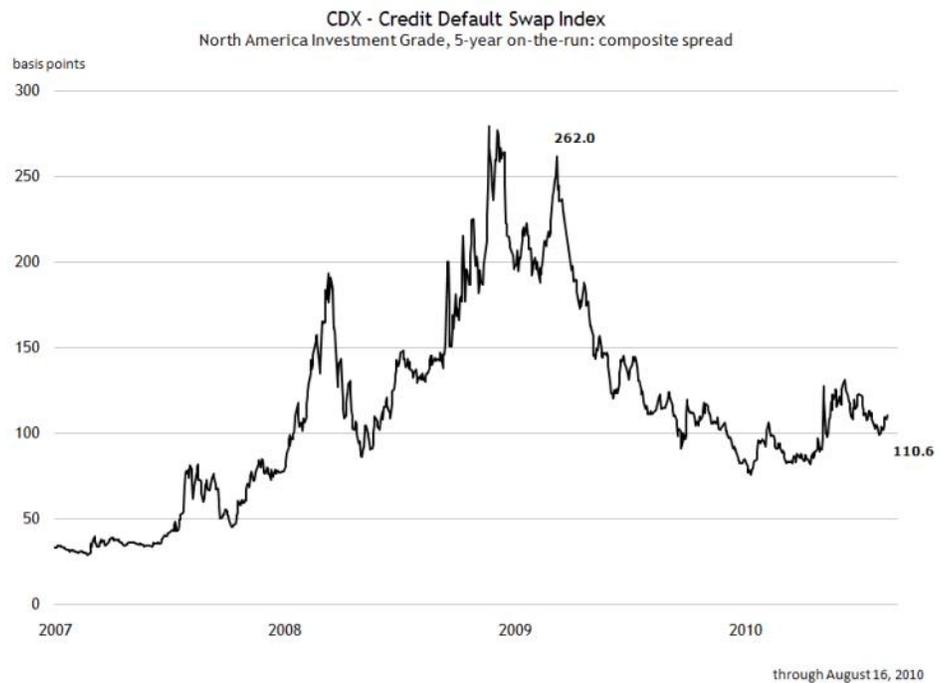
## Summary

The cost of insuring losses on corporate bonds rose to its highest level in more than three weeks.

The CDX climbed to 110.6 basis points on August 16, reaching its highest level since July 21.

Investors use the CDX to hedge against losses on corporate debt or to speculate on creditworthiness. An increase in the CDX generally signals a deterioration in the perception of credit quality.

One basis point equates to \$1,000 annually on a contract protecting \$10 million in debt.

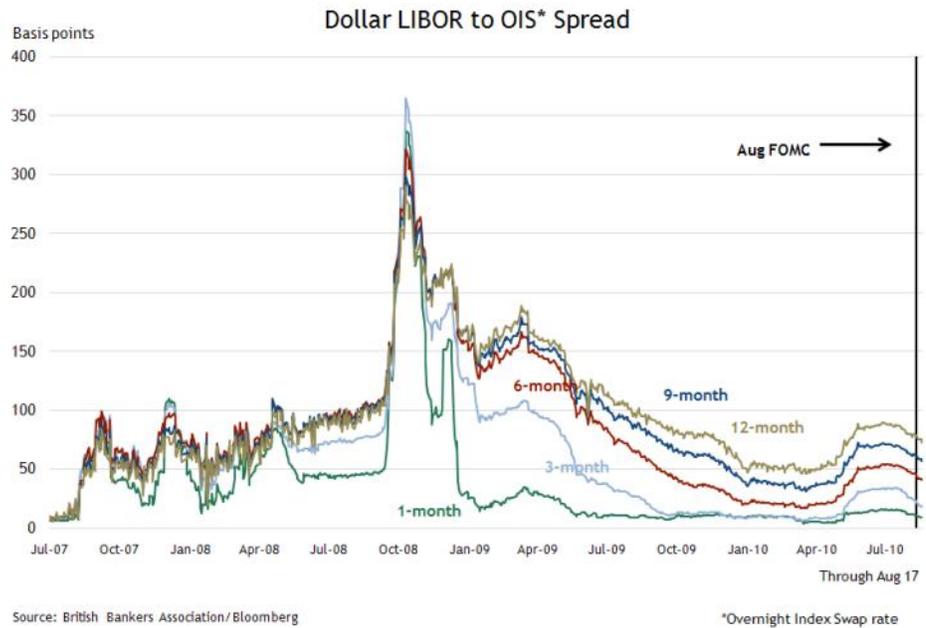


Source: Markit Group Limited/Haver Analytics

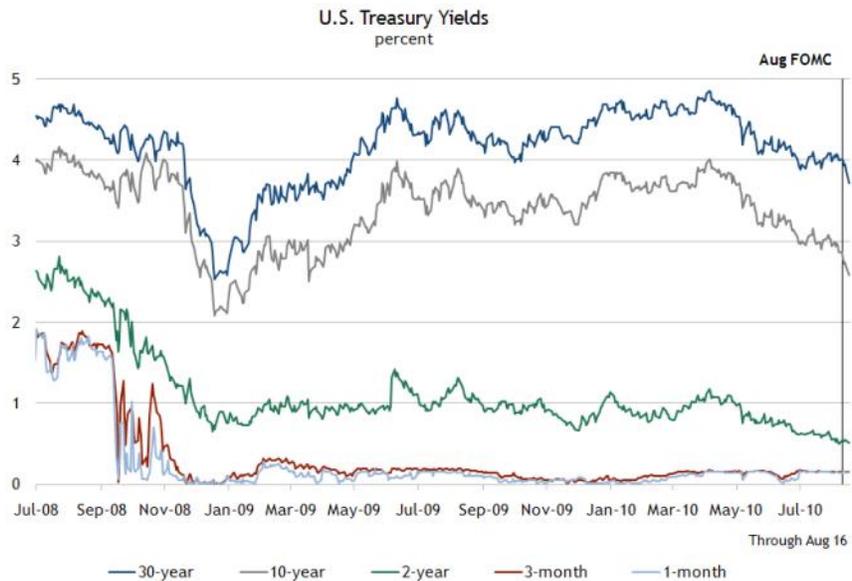
# Broad Financial Market Indicators

## Summary

LIBOR to OIS spreads have narrowed slightly since the August FOMC meeting but remain elevated relative to levels seen earlier this year.



Longer-dated Treasury yields have declined since the August FOMC meeting.



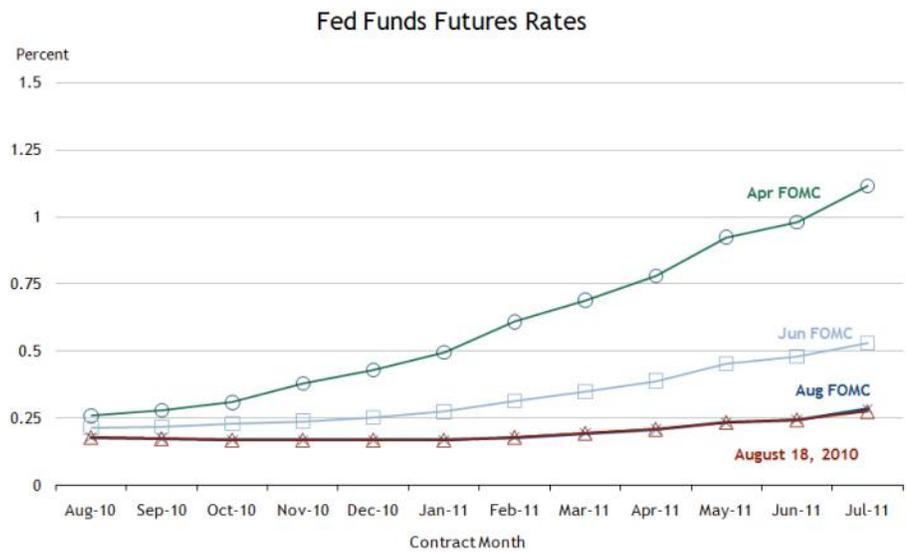
Source: Federal Reserve Board/Haver Analytics

- Since the August FOMC meeting, 30-year Treasury bonds have declined 28 bps to 3.7%, and 10-year Treasury bonds have declined 21 bps to 2.6%.

# Broad Financial Market Indicators

## Summary

The curve of expected rates from the fed funds futures market flattened further over the intermeeting period but has not changed during the past week.



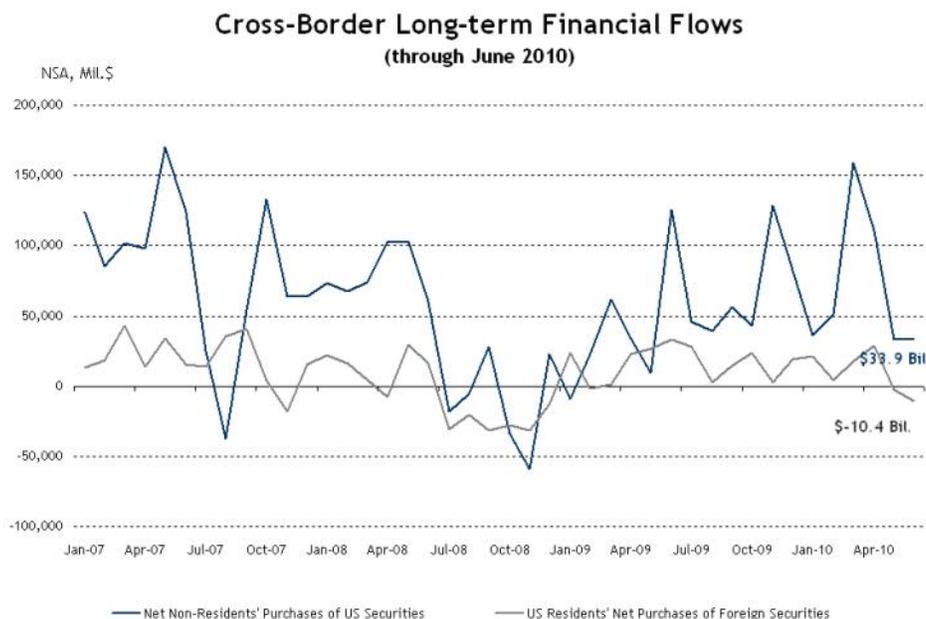
Source: Bloomberg

- The fed funds futures markets expect a rate increase around late 2011 or early 2012.

## Broad Financial Market Indicators

### Summary

On net, nonresidents bought \$33.9 billion in long-term U.S. securities in June. U.S. residents continued to repatriate funds, on net selling a total of \$10.4 billion in foreign bonds and equities.



Source: U.S. Treasury/Haver Analytics

- On net, nonresidents bought \$33.9 billion in long-term U.S. securities in June. Nonresident investors remained net buyers of U.S. Treasuries and federal agency securities, but on net sold U.S. equities and corporate bonds.
- On net, U.S. residents repatriated capital for the second consecutive month in June, consistent with increased risk aversion in financial markets. U.S. investors sold a net \$6 billion in foreign bonds and \$4.4 billion in foreign equities. Sales of foreign assets imply higher supply of capital for the U.S. economy.
- China reduced its holdings of U.S. Treasury securities for the second consecutive month in June to \$848 billion. China still accounts for about a third of all U.S. Treasury securities holdings by foreign official institutions and about a fifth of total foreign holdings. At the end of the first quarter, nonresidents held 50% of marketable U.S. government debt.