

Financial Highlights

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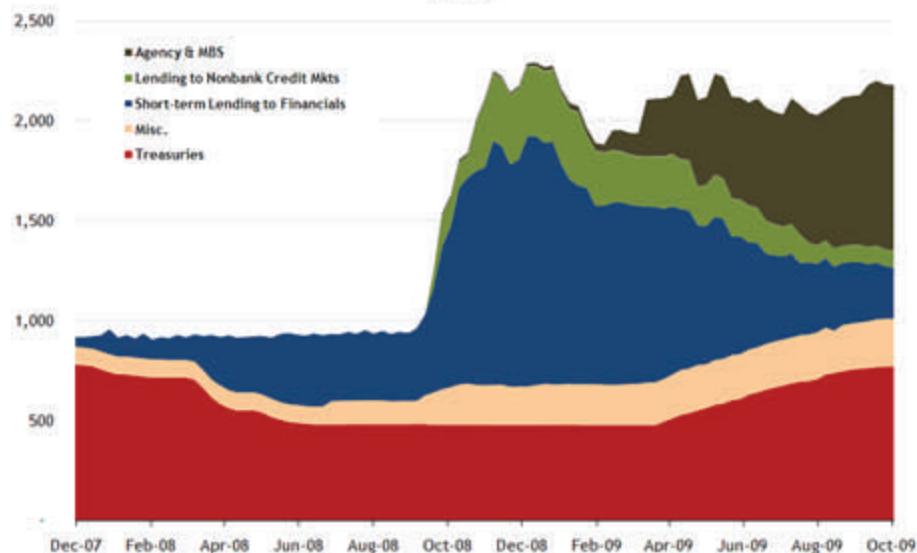
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Federal Reserve

Summary

Federal Reserve Assets (Uses of Funds)
\$ billions

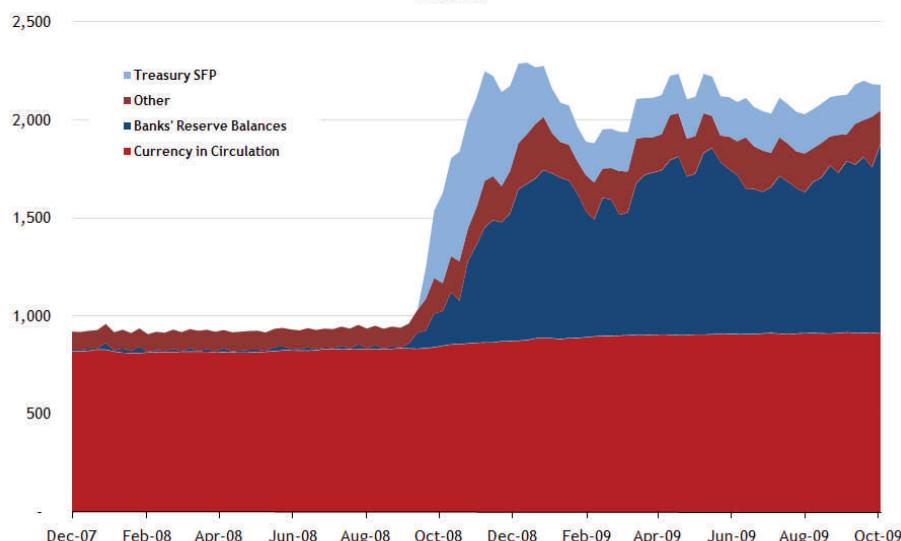


At \$2.18 trillion, the size of the Fed's balance sheet remains close to the upper end of the \$2 trillion to \$2.2 trillion range experienced since March.

Source: Federal Reserve Board

- The Fed's balance sheet from about March to August this year was characterized by sizable declines in short-term lending to financials and nonbank credit markets that were largely offset by holdings of Treasuries, MBS, and agency debt (thus resulting in little change to the total size of the balance sheet). The pace of declines in the Fed's liquidity and credit facilities (excluding TALF) has slowed over August and into September while the increases in Treasury holdings have also slowed. With respect to the direct purchase programs, the Treasury purchases are nearly complete; thus, further increases in directly purchased assets will stem from increases in MBS and agency debt.

Federal Reserve Liabilities (Sources of Funds)
\$ billions



On the liabilities side, bank reserve balances jumped by \$118 billion for the week ended October 7 and now stand at about \$916 billion, or 44% of the balance sheet.

SFP = Supplementary Financing Program

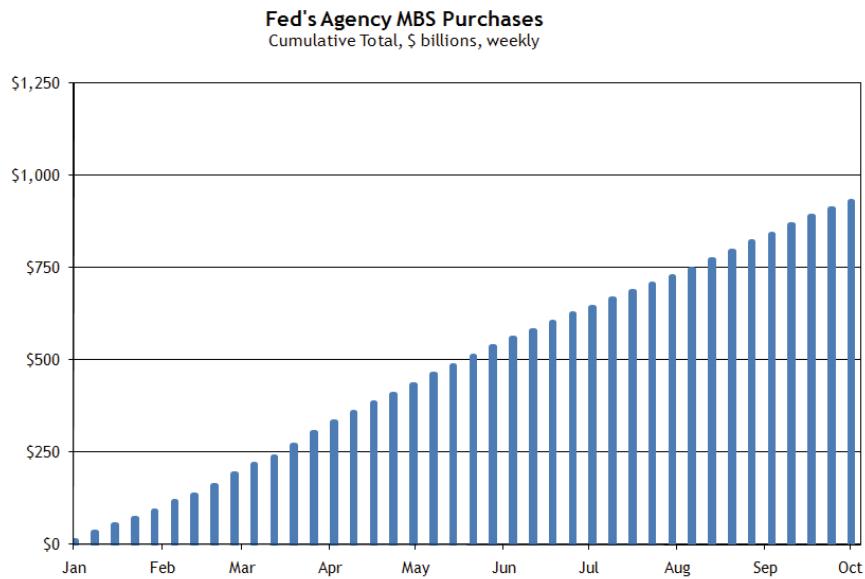
Source: Federal Reserve Board

- On September 16, the Treasury Department announced its intentions to let all but \$15 billion in bills outstanding under the SFP expire "in the coming weeks." The SFP has declined by \$35 billion for two consecutive weeks and stood at about \$130 billion as of the week ended October 7.

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.

Summary

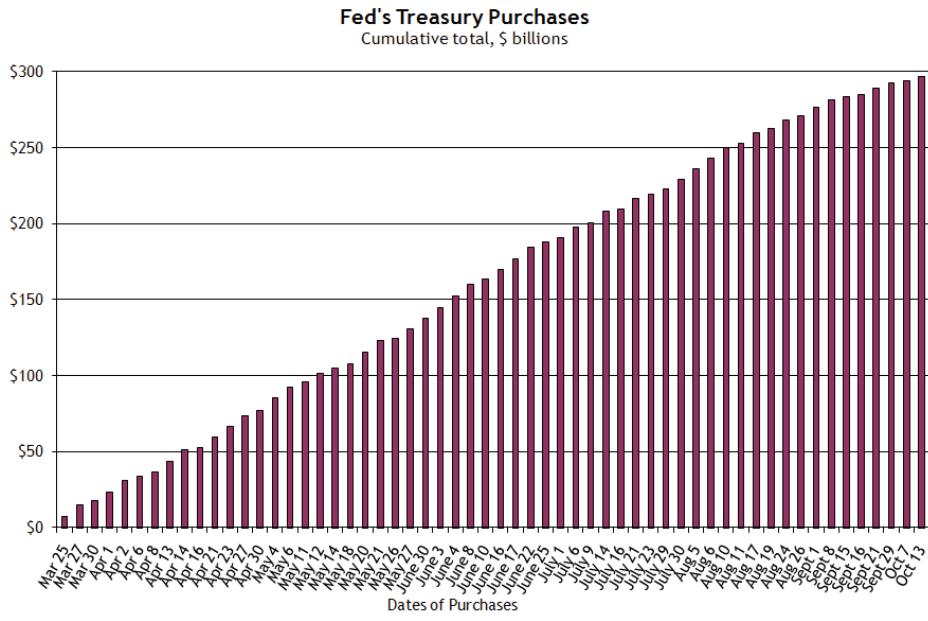
The Fed has now purchased about \$929 billion in agency-backed MBS through the week ended October 7.



Source: NY Fed

- The Fed purchased a net total of \$20 billion of agency-backed MBS between October 1 and 7, bringing its total purchases up to about \$929 billion, and by year-end the Fed will purchase up to \$1.25 trillion.

The Fed now has about \$3 billion remaining to meet its goal of purchasing \$300 billion in Treasury securities by the end of October.

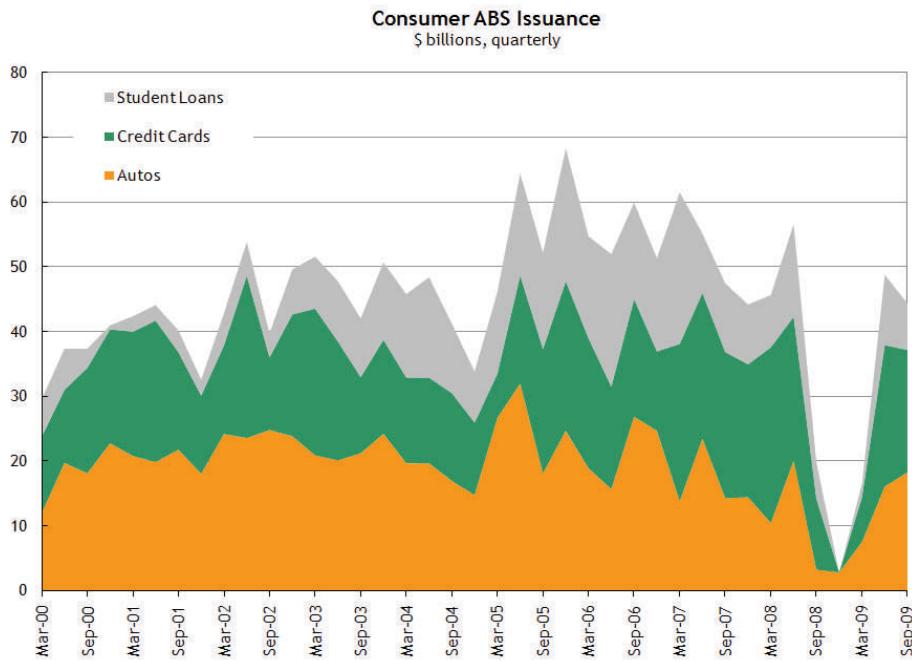


Source: NY Fed

- The Fed has purchased a total of \$297 billion of Treasury securities through October 14, bringing it about 99% toward its goal. Of these, \$4.5 billion have been TIPS purchases.
- In the past week, the Fed made a purchase on October 13 of \$2.949 billion in the seven-to-10-year sector.

Summary

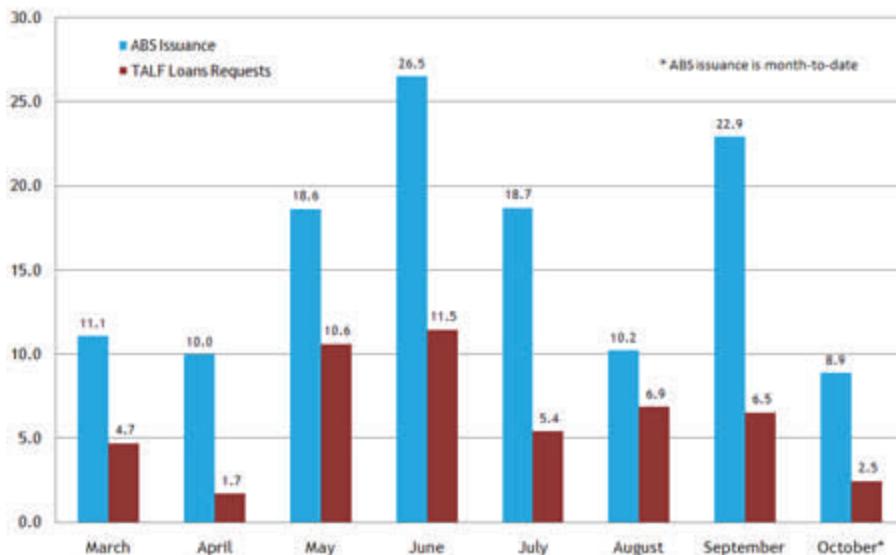
New issuance of consumer ABS has held up through the third quarter after recovering from depressed levels in the fourth quarter of 2008.



Source: J.P. Morgan and Bloomberg

- Consumer ABS issuance was about \$44 billion in Q3, down a marginal \$4.4 billion (or about 9%) from issuance of about \$49 billion in Q2. Issuance in Q2 and Q3 have been just below the pace of average quarterly issuance in 2007 of about \$52 billion.

ABS Issuance and TALF Loan Requests by Monthly Operation
\$ billions



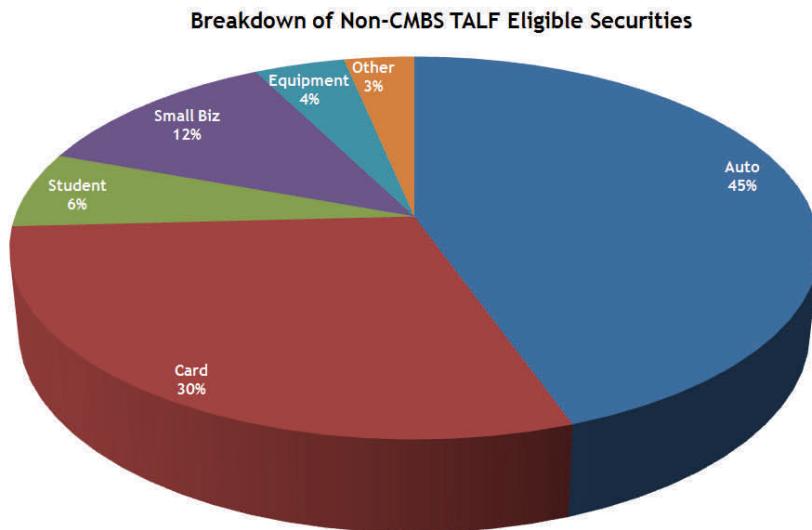
The October TALF operation saw \$2.5 billion in loan requests, the smallest amount since April.

Source: Bloomberg and NY Fed

- So far in October, the ratio of TALF loan requests to new ABS issuance of 0.28 is the smallest since April. The lower ratio may be an indication that the market is better able to absorb the new securities without TALF funding. Note that not all TALF loans are necessarily for securities issued in the most recent month.
- Also note that ABS issuance in the bottom chart includes securities beyond the consumer ABS chart at the top (i.e., the bottom chart includes small business, equipment lease, and other ABS).

Summary

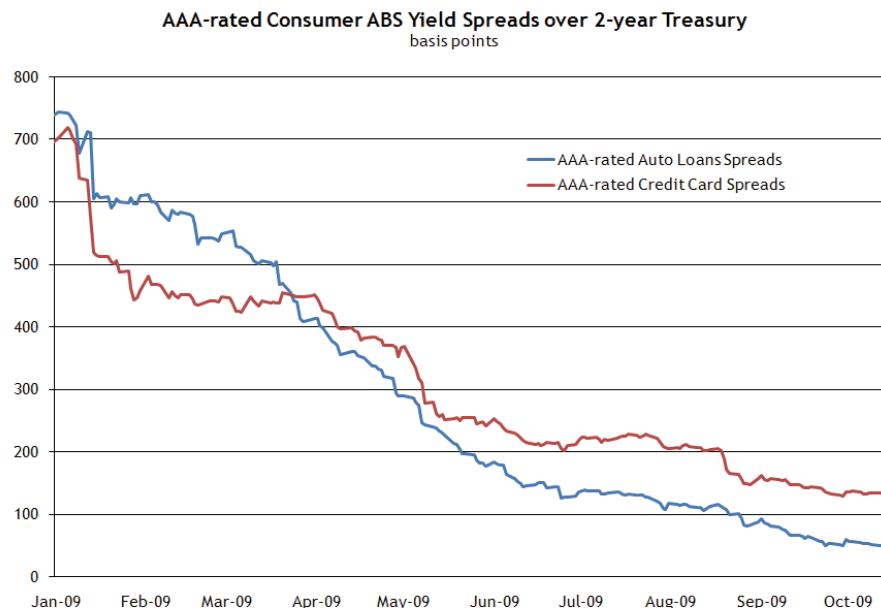
Bloomberg data indicate that about 40% of eligible securities are pledged to the TALF.



Source: Bloomberg

- According to Bloomberg, about \$106 billion in outstanding ABS securities (non-CMBS) is eligible collateral for the TALF; about three-quarters of these securities are backed by auto loans and credit card receivables. As of October 7, the reported size of the TALF on the Fed's balance sheet was approximately \$42 billion, implying that roughly 40% of eligible TALF non-CMBS securities are currently pledged to the facility as collateral.

Risk spreads on consumer ABS have continued to edge lower in recent weeks and months, likely reflecting reduced credit risk premia and improved market liquidity.



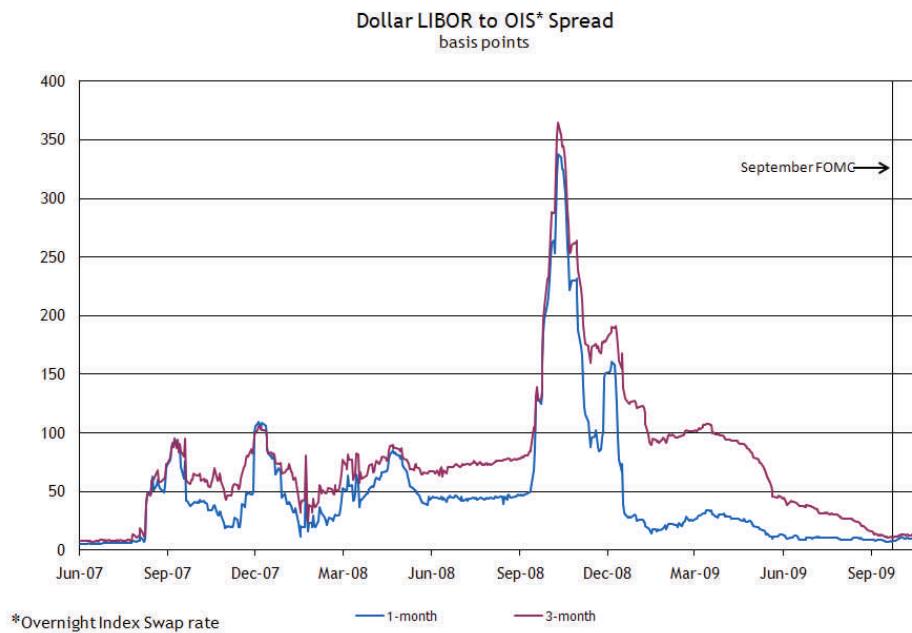
Source: Bloomberg and Merrill Lynch

- Since the first TALF operation in March, yield spreads on securities backed by auto loans and credit card receivables over two-year Treasury rates have declined by about 450 and 305 basis points (bps), respectively. The vast majority of the spread narrowing reflects declines in yields on the ABS (autos down 440 bps and cards down 300 bps since March 17) rather than increases in yields on Treasuries.
- Part of the decline in ABS yields likely reflects improved liquidity conditions (and thus lower liquidity premiums) in the ABS market following implementation of the TALF program.

Broad Financial Market Indicators

Summary

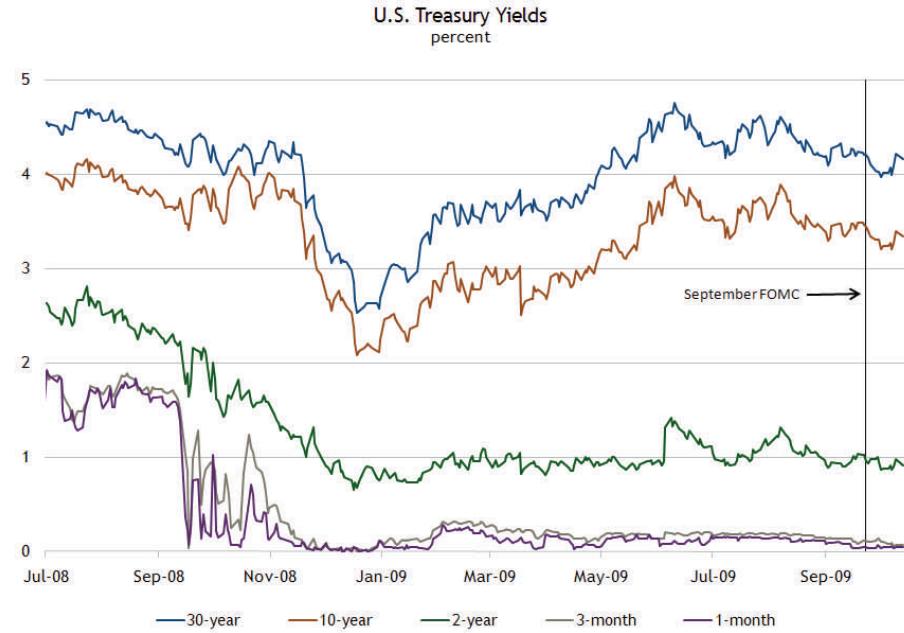
LIBOR-to-OIS spreads have widened slightly since the last Federal Open Market Committee (FOMC) meeting.



Source: Bloomberg and British Bankers' Association

- Since the last FOMC meeting on September 23, the one-month and three-month Dollar LIBOR to OIS spreads have increased 2.1 and 1.8 bps, respectively.

Longer-dated Treasury yields declined over the same period.



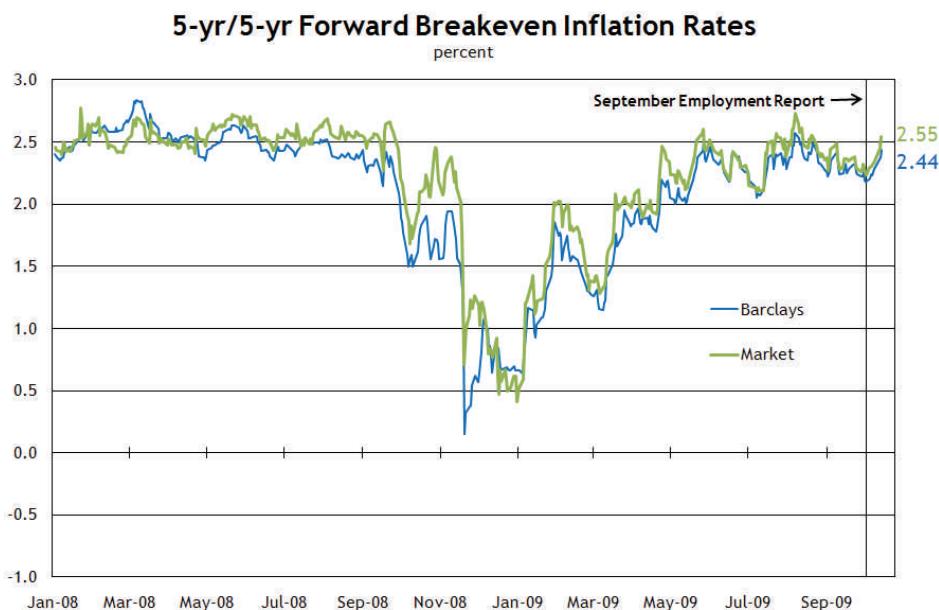
Source: Bloomberg

- Following the last FOMC statement on September 23, longer-dated Treasury yields have fallen: The 30-year bond was down 5 bps to 4.16%, the 10-year note fell 10 bps to 3.34%, and the two-year note was lower by 5 bps to 0.91%, through October 13.

Broad Financial Market Indicators

Summary

Various measures of the break-even inflation rate have increased this month.



Source: Barclays and Bloomberg

- Since the September employment report was released on October 2, the Barclays 5-year/5-year forward breakeven inflation (BEI) rate has risen 26 bps to 2.44% as of October 14. Barclay's 10-year/10-year forward rate (not shown) was 2.54% as of October 13. The Bloomberg measure shows a similar change but at a slightly higher level: The BEI rose 31 bps since October 2 to 2.55%
- The \$7 billion 10-year TIPS auction last week was well received, with a bid-to-cover of 3.12 (the second highest on record) and had a stop-out rate of 1.51%.