

RESEARCH QUARTERLY

Volume I V No.

6

Capital Market Issuance Reached \$1.42 Trillion in First Quarter 2009

Securities issuance totaled \$1.42 trillion in the first quarter of 2009, 70.2 percent above issuance in the fourth quarter of 2008 and a 2.8 percent increase from the \$1.38 trillion issued in the same year-earlier period.

In the mortgage-backed sector, agency MBS volume continued to dominate as several microeconomic drivers negatively influenced private-label and non-agency issuance; double digit delinquency rates, rising foreclosures, declining home prices and tighter mortgage underwriting guidelines will continue to depress this sector in 2009. In the asset-backed sector, issuance increased modestly from the prior quarter as the Term Asset-Backed Securities Loan Facility (TALF) began, but the sector remains impacted by unemployment and rising consumer bankruptcies. In the CDO sector, issuance collapsed, both on a quarterly basis and year-over-year volume.

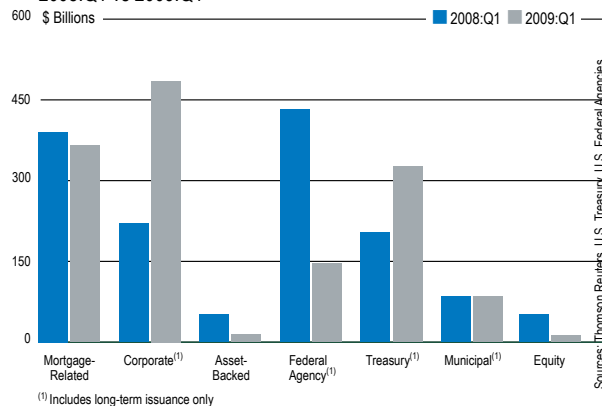
Underwriting in the equity sector declined as the secondary market dried up along with the IPO and preferred markets.

Federal agency debt issuance rose in the first quarter from fourth quarter; however, issuance is substantially down from the same period a year ago. Treasury issuance decreased modestly as the federal government sought to meet its expected budget shortfall. Municipal fund raising in the capital markets was up from the last quarter of 2008, as states and localities looked to meet financing requirements to offset reduced tax revenues amid slower economic growth.

The U.S. government announced the Public-Private Partnership Investment Program (PPIP)¹ at the end of first quarter 2009 with the intent to improve liquidity on legacy real estate assets, whole loans and securities; and to help restore the flow of credit among U.S. financial institutions.

Issuance in the U.S. Capital Markets

2008:Q1 vs 2009:Q1



⁽¹⁾ Includes long-term issuance only

Issuance Highlights

\$ Billions	2009:Q1 only	2008:Q1 ytd	2009:Q1 ytd	% Change
Municipal ¹	85.0	85.4	85.0	-0.5%
Treasury ¹	326.8	203.8	326.8	60.4%
Federal Agency ¹	146.3	432.4	146.3	-295.6%
Mortgage-Related	364.8	390.6	364.8	-6.6%
Asset-Backed	14.7	51.4	14.7	-71.4%
Global CDO	5.0	481.6	5.0	-88.4%
Corporate ¹	485.1	220.9	485.1	119.6%
Equity	12.3	51.2	12.3	-76.0%

* Percent change between 2009:Q1 and 2008:Q1

¹ Includes long-term issuance only

CONTRIBUTORS

Kyle Brandon	kbrandon@sifma.org
Charles Bartlett	cbartlett@sifma.org
Paul Rainy	prainy@sifma.org
Sharon Sung	ssung@sifma.org

¹ For more information on PPIP <http://www.sifma.org/legislative/PPIP.shtml>

Municipal Issuance Volume Rose

Short- and long-term municipal issuance totaled \$85.0 billion at the end of the first quarter 2009, up 21.4 percent above the \$70.0 billion issued in the last quarter of 2008 and virtually unchanged from the \$85.4 billion issued in the first quarter of 2008.

Long-term municipal issuance volume was \$79.7 billion, up from \$51.0 billion issued in the fourth quarter and \$65.8 billion issued in the same period last year. Short-term issuance was \$5.3 billion, 72.1 percent below the \$19.0 billion issued in the fourth quarter 2008, and down 73.5 percent from the \$20 billion issued in the same year-earlier period.

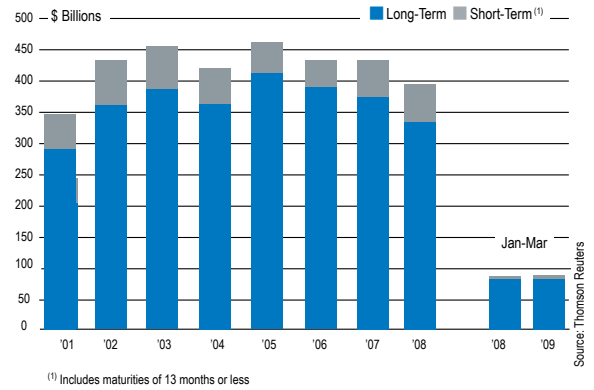
The ratio of the 10-year AAA-rated general obligation (G.O.) municipal yield to that of Treasury securities of similar maturity stood at 1.27 percent at first quarter end, compared to 1.74 percent at the end of December. As of end-March, the yields on 10-year municipal securities were 3.45 percent, compared to 2.71 percent for comparable treasuries.

New Money and Refunding Volume Both Rise

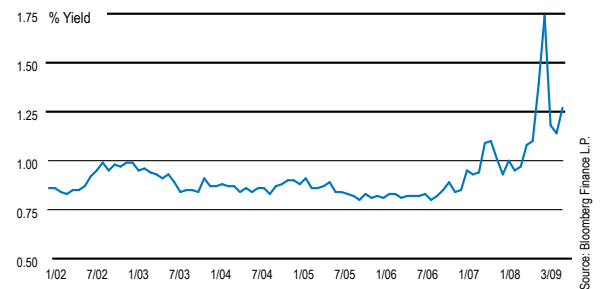
New capital issuance totaled \$54 billion in the first quarter, up 7.5 percent from the fourth quarter of 2008, snapping a streak of three consecutive quarterly declines. The larger use-of-proceeds sectors recorded issuance increases in the first quarter, with the largest, education-related issuance, totaling \$16.1 billion, compared to \$11.4 billion in the previous quarter. The second place general government sector issued \$21.9 billion through March, an 80.5 percent increase, while transportation sector issuance declined by 61.5 percent, with \$3.1 billion in new money issued compared to \$8.1 billion in fourth quarter 2008.

Refunding activity totaled \$31 billion in the first quarter of 2009, 7.3 percent above the \$28.9 billion issued in the fourth quarter of 2008. Issuance volume was mixed, with five major categories rising and five falling. Education-related issuance was up 29.3 percent to \$23.8 billion in 2009 compared to \$18.4 billion in the first quarter of 2008, while general government sector issuance increased to \$28.7 billion from \$17.6 billion. In contrast, transportation-related issuance decreased 67 percent to \$5.4 billion from \$16.3 billion in the prior year's first quarter.

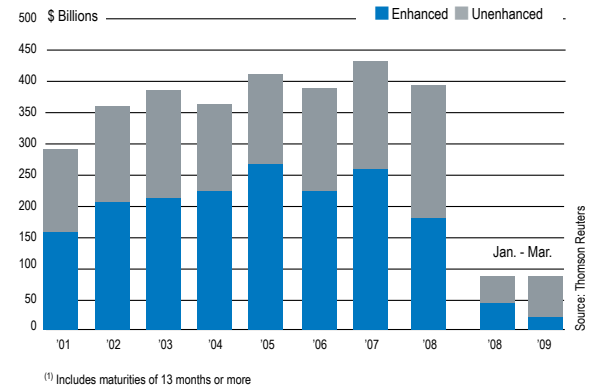
Short- and Long-Term Municipal Issuance
2001–2009:Q1



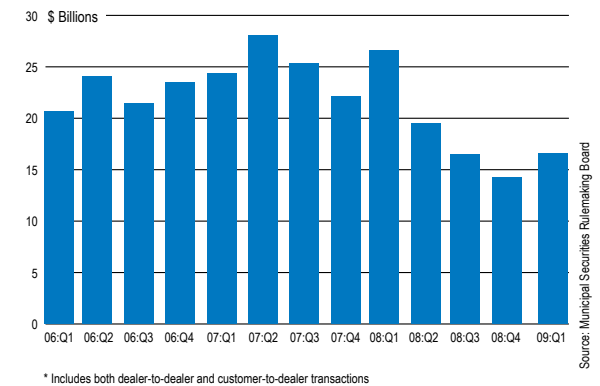
Municipal GO AAA and 10-Yr Treasury Ratio
Jan. 2002–Mar. 2009



Long-Term* Municipal Issuance by Enhancement Status
2001–2009:Q1



Average Daily Trading Volume of Municipal Securities*
2006:Q1–2009:Q1



Net Treasury Redemptions Decline, Fed Rates Remained Unchanged

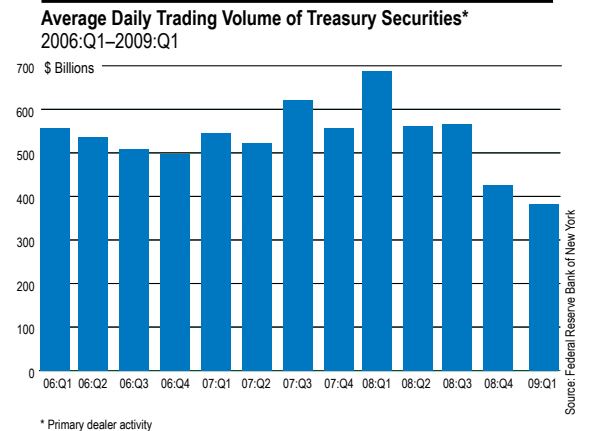
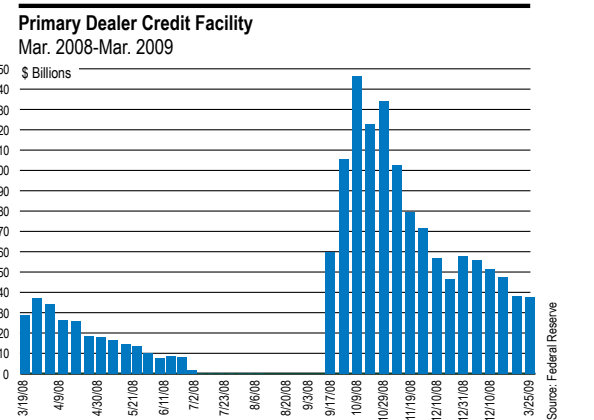
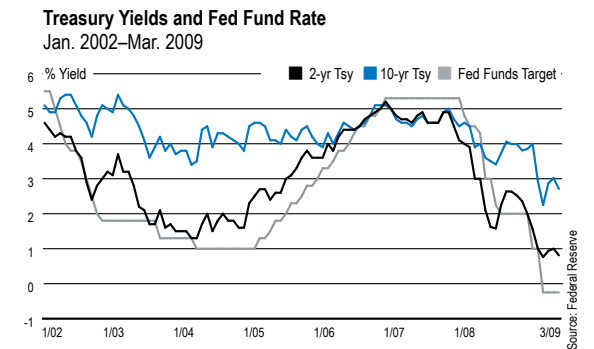
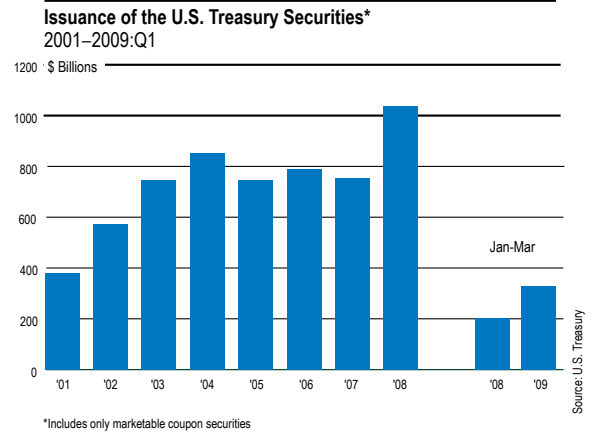
Total net issuance of U.S. Treasury securities, including bills and coupons, was negative in first quarter 2009, with a net redeemed amount of \$51.9 billion, compared to a net redemption of \$264.7 billion in the fourth quarter of 2008 and net issuance of \$190.9 billion in the first quarter of 2008. Net coupon issuance was \$165.6 billion, down 17.3 percent from the \$200.3 billion issued in the fourth quarter of 2008, but up significantly from the \$36.4 billion issued in the same year-earlier period. Consistent with the results of SIFMA's recent Government Forecast², the Treasury announced it expects to borrow \$356 billion of marketable debt in the second quarter of calendar year 2009. The U.S. federal government recorded a total budget deficit of \$455 billion for fiscal year (FY) 2008, which was less than the forecast of \$482 billion. The budget deficit in FY2009 is expected to rise to \$1.75 trillion on the ongoing fiscal support and economic stabilization programs.

Gross coupon issuance volume decreased 11.4 percent during the first quarter of 2009 to \$326.8 billion from \$368.9 billion in the fourth quarter of 2008. Bill redemptions totaled to \$217.5 billion in the first quarter, less than half of the \$465 billion redeemed in the previous quarter. Gross issuance is affected by expected refunding of maturing and callable debt as well as Treasury's new cash needs. Daily trading volume of treasury securities by primary dealers averaged \$382.4 billion in the first quarter, 9.3 percent lower than the \$425.1 billion in the fourth quarter of 2008 and 43 percent below \$671.1 billion average recorded in the first quarter of 2008.

First quarter news was dominated by efforts to stabilize financial markets and industry. In an effort to add liquidity to the financial markets, the Federal Reserve maintained the Fed Funds target rate between zero and 0.25 percent during the first quarter.

On March 18 and 19, the Federal Reserve announced the expansion of its agency and treasury purchase program, with an additional \$750 billion in agency mortgage backed securities, \$100 billion in agency direct obligations, and \$300 billion in long-term Treasury securities in purchases to help improve conditions in private credit markets. On March 23, the Treasury and FDIC announced details of the Public-Private Partnership Investment Program (PPIP), a two-part program designed to provide equity and debt financing for the purchase of whole loans and securities.

The 2-year Treasury yield was 0.81 percent at the end of the first quarter, up from 0.76 percent at end-December 2008. The 10-year Treasury yield rose more steeply, increasing to 2.71 at the end of the first quarter, from 2.25 percent at the end the previous quarter. The 2-year to 10-year yield spread increased to 190 basis points at the end of the first quarter from 149 basis points at the end of December. Bond and stock traders track the spread, or difference, in yield between the 2-year U.S. Treasury note and the 10-year Treasury note because the spread represents fixed-income traders' expectations about the direction of Fed monetary policy, as well as inflationary expectations in the economy.



² The most recent SIFMA Government Forecast can be found at: <http://www.sifma.org/research/pdf/GovForecast0409.pdf>

Agency Issuance

Agency debt issuance started to shift more toward longer-term debt as the credit markets began to unfreeze and very short-dated securities started to mature. In the first quarter of 2009, federal agency long-term debt issuance totaled \$146.3 billion, an increase of more than 52.9% from the \$95.8 billion issued in the fourth quarter of 2008. Fannie Mae and Freddie Mac did not record any issuance in February and March of 2009.

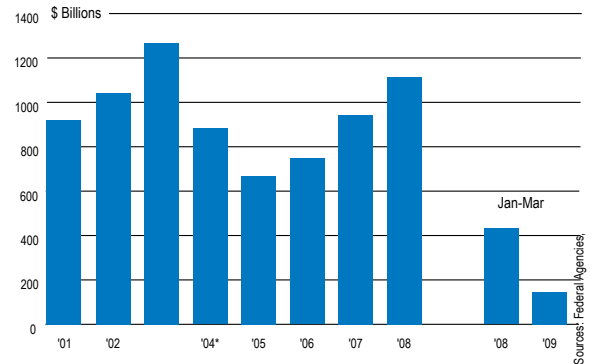
The Federal Home Loan Banks (FHLB) have acted as an important and lower-cost source of liquidity for lending for depository institutions during the prolonged credit crisis. FHLB issuance reached \$110.7 billion in the first quarter of 2009, an increase of nearly fourfold from the \$22.5 billion issued in the fourth quarter of 2008, but 49.1 percent below the \$217.3 billion issued in the same year-earlier period.

Late in the third quarter of 2008, the U.S. government put Fannie Mae and Freddie Mac into conservatorship. Freddie Mac's January debt issuance of \$53.3 billion was 61.5 percent greater than the entire fourth quarter of 2008, when \$33.3 billion was issued, but decreased compared to the \$89.0 billion recorded in the first quarter of 2008. Issuance of debt by Fannie Mae was completely non-existent in the first quarter of 2009, compared to \$26.6 billion and \$88.4 billion issued in the fourth quarter and first quarter of 2008, respectively.

Long-term issuance by the Farm Credit System reached \$25.4 billion in first quarter 2009, compared with \$20.7 in the previous quarter and \$41.5 billion in the first quarter of 2008. The Tennessee Valley Authority had no issuance of long-term debt for the third consecutive quarter.

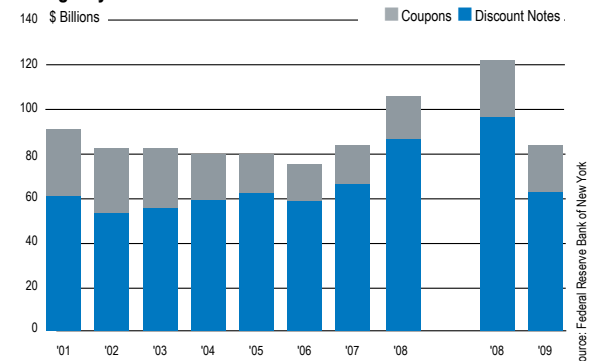
SIFMA's recent Government Forecast³ projected a decrease in federal agency debt issuance in the second quarter of 2009 to \$88 billion compared to \$413.7 billion issued in the first quarter of 2009 and \$387.9 billion issued in the second quarter of 2008.

Long-Term Federal Agency Debt Issuance⁽¹⁾
2001–2009:Q1



⁽¹⁾ Excludes maturities of one year or less
* Beginning with 2004, Sallie Mae has been excluded due to privatization

Average Daily Trading Volume of Federal Agency Securities⁽¹⁾ 2001–2009:Q1



⁽¹⁾ Primary dealer activity

³ SIFMA Government Forecast can be found at: <http://www.sifma.org/research/pdf/GovForecast0409.pdf>

Long-Term Federal Agency Debt Issuance

\$ Billions	2008	2008:Q1	2009:Q1	% Change*	\$ Change*
FHLB ¹	515.1	217.2	110.7	-49.0%	(106.5)
Freddie Mac	253.7	93.6	0.0	-43.1%	(40.3)
Fannie Mae	248.4	93.0	53.3	-100.0%	(93.0)
FCS ²	110.5	40.1	25.4	-36.7%	(14.7)
TVA ³	2.1	1.6	0.0	-100.0%	(1.6)
Totals	1,129.8	445.5	189.4	-57.5%	(256.1)

*Percent and amount change between 2008:Q1 and 2009:Q1

¹Federal Home Loan Bank System

²Farm Credit System

³Tennessee Valley Authority

Sources: Thomson Reuters and Federal Agencies

Mortgage-Related Market

Issuance of mortgage-related securities, including agency and non-agency pass-throughs and collateralized mortgage obligations (CMO), totaled \$364.8 billion, an increase of 68.7 percent from the \$216.3 billion issued in the prior quarter, but a decrease of 6.6 percent from the \$390.5 billion issued in the first quarter of 2008.

As in recent quarters, issuance was largely driven by the agency market. Among the changes introduced by Obama's Making Home Affordable program, the two GSEs (Fannie Mae and Freddie Mac) were allowed to expand their portfolio by \$50 billion, to \$900 billion each.

In the first quarter of 2009 only \$15.2 million in non-agency, or private-label, residential mortgage-backed securities (RMBS) was issued, a decline of 99.7 percent from the \$5.5 billion issued in the previous quarter and a decline of 99.9 percent from the \$11.9 billion issued in the first quarter of 2008. The private label market continues to have little to no activity due to reduced lending, lack of demand, low liquidity, deteriorating loan quality and political uncertainty. Issuers and investors alike continue to wait for additional details concerning PPIP and the potential expansion of TALF, which recently expanded to include newly issued and legacy commercial mortgage-backed securities (CMBS). Legislative uncertainty continues to remain in Congress, with cramdown provisions stripped, 5896 has been passed and sent to the President; HR 1728 has been passed by the House but Senate action is unclear. Other mortgage-related bills continue to circulate and will cloud the markets further.

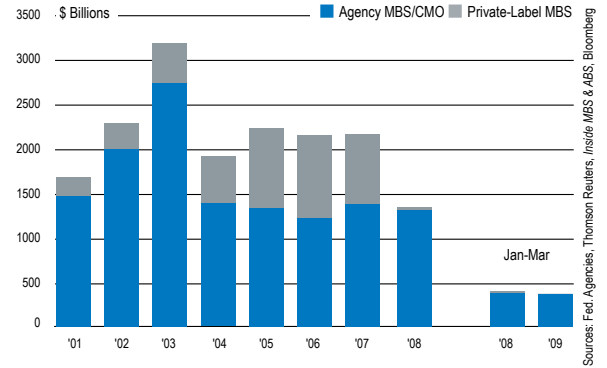
Private-label CMBS issuance market remained closed with no new issuance for the second consecutive quarter. Reduced consumer spending, rising vacancies, refinancing uncertainty, and the bankruptcy and liquidation of large major retailers unfavorably impacted the CMBS and larger commercial real estate market. Shortly after the end of first quarter 2009, General Growth Properties, the second largest commercial real estate investment trust (REIT), filed for Chapter 11 bankruptcy protection, the largest ever U.S. commercial real estate bankruptcy filing.

The Future Remains Uncertain Despite Government Aid

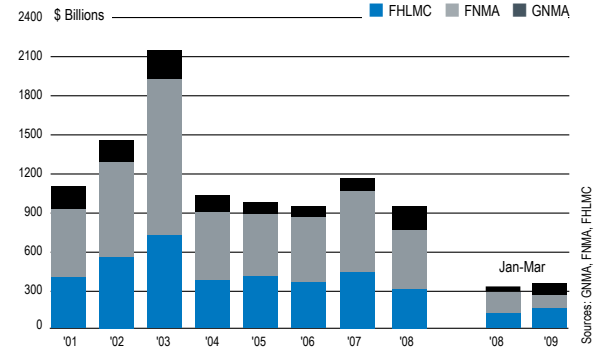
The Federal Reserve began purchasing agency debt and longer-dated Treasuries in December 2008, committing to buy up to \$1.25 trillion in agency MBS, \$300 billion in Treasuries, and \$200 billion in agency debt before the end of 2009. As of the end of the first quarter, the Fed purchased net \$302.2 billion of agency mortgage securities, concentrating the majority of purchases to 30-year fixed-rate securities within the 4.0 to 5.5 percent coupon range; \$52.7 billion in agency debt; and \$20.0 billion in Treasury securities. The purchases helped drive mortgage rates down substantially: according to the Mortgage Bankers Association, contract rates for 30-year fixed-rate mortgages decreased to 4.61 percent at the end of March 2009 from 5.07 percent at the beginning of January.

In addition, the Obama Administration's Making Home Affordable Plan, introduced in early March 2009, allows mortgage borrowers with a loan owned by an agency to refinance, including underwater borrowers traditionally locked out of the refinancing market (with a LTV ratio up to 105 percent). Low mortgage rates, combined with greater eligibility, helped drive refinancing activity. According to MBA, refinancing drove the majority of new mortgage applications in the first quarter of 2009, ranging from 66.7 percent to 79.8 percent of all applications on a weekly basis. The program also provides incentives for servicers to modify loans. Accompanying

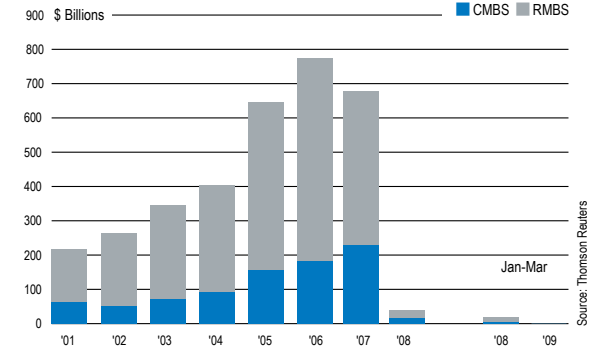
Issuance of Mortgage-Related Securities
2001–2009:Q1



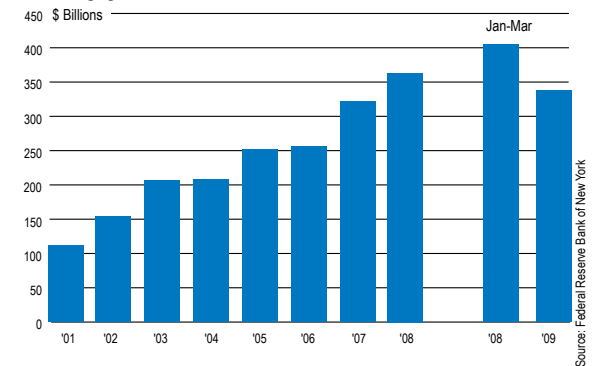
Issuance of Agency Mortgage-Backed Securities
2001–2009:Q1



Issuance of Non-Agency Mortgage-Backed Securities
2001–2009:Q1



Average Daily Trading Volume of Agency Mortgage-Backed Securities⁽¹⁾ 2001–2009:Q1



⁽¹⁾ Primary dealer activity

the modification program the Second Lien program was introduced in late April in order to additionally help homeowners with second mortgages.

However, the real-estate market has continued to weaken and will continue to depress the mortgage-related markets. The S&P/Case-Shiller Home Price 20-City Composite index continued to fall in the first quarter, declining 18.6 percent on a year-over-year basis in February after dropping 19 percent year-over-year in January 2009, for a total decline of 30.7 percent from its peak in July 2006. Declining property values have put a substantial number of borrowers underwater: according to Loan Performance, 1 in 5 properties were underwater at the end of December 2008. Delinquencies continue to rise in all mortgage loan categories as job losses increased; despite foreclosure moratoriums imposed late in fourth quarter 2008 by the GSEs and large banks, foreclosures were up 9 percent in the first quarter of 2009 from the prior quarter, according to Realtytrac, and increased 24 percent from first quarter 2008 pace. Housing inventory continues to remain at elevated levels.

Asset-Backed Market

The asset-backed securities (ABS) market revived in the first quarter of 2009, spurred by the start of the Federal Reserve Board's Term Asset-Backed Loan Facility program. Total ABS issuance was \$14.7 billion in the first quarter, an increase of 326.4 percent from the \$3.5 billion in fourth quarter 2008, but 71.3 percent below the \$51.4 billion issued in the same year-earlier period. The TALF program, although initially greeted with enthusiasm, received lukewarm reception in the first quarter as potential investors and issuers shied away due to potential TARP restrictions and the political backlash exacerbated by AIG bonuses.

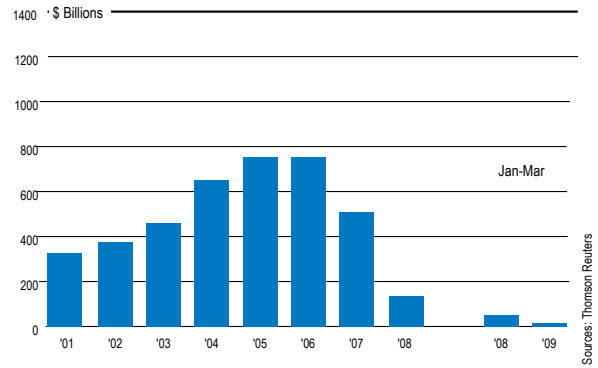
Although the ABS market held up relatively well compared to the mortgage-backed securities market, credit quality continued to deteriorate in all asset classes, with job losses and rising personal bankruptcies continuing to impact the sector. While revolving consumer debt outstanding dropped by an annualized rate of 6.5 percent in the first quarter 2009 as consumers continued to pay down debt, delinquencies and charge offs in credit card, home equity, auto, and student loan categories continued to rise.

Auto Loan and Credit Card ABS Leads Issuance Totals in First Quarter

Issuance was particularly strong in the auto (\$7.6 billion) and credit card ABS (\$3.0 billion) sectors due to their eligibility for TALF financing. The first and only TALF subscription in first quarter 2009 resulted in \$4.71 billion in loans, with \$1.9 billion of auto ABS and \$2.8 billion of credit card ABS financed by TALF. Deals financed by TALF in the beginning of the second quarter have expanded to other sectors eligible for TALF financing, such as student loan, small business, and equipment.

Student loan and other ABS issuance totaled \$2.0 billion and \$1.6 billion, respectively, in first quarter 2009. Both equipment and home equity ABS remained weak, with \$514.7 and \$130.7 million issued. Manufactured housing remained flat with zero issuance as a glut of housing supply continues to saturate the market and housing starts remain at an all time low.

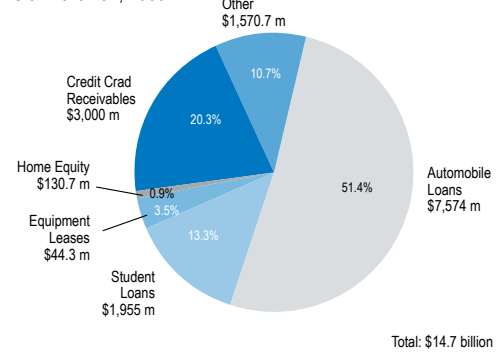
Issuance of Asset-Backed Securities
2001-2009:Q1



Sources: Thomson Reuters

ABS Outstanding by Major Types of Credit*

As of March 31, 2009



Total: \$14.7 billion

*Percentages may not add due to rounding.

Sources: Thomson Financial, Bloomberg

Global CDO Markets

Global collateralized debt obligation (CDO) issuance continued to fall in first quarter 2009 with only \$762.9 million issued. This represents a decrease of 86.6 percent from the \$5.7 billion issued in fourth quarter 2008 and was 96.2 percent below the \$19.9 billion issued in the first quarter of 2008.

Market and Purpose Segmentation

Cash flow and hybrid CDO issuance dropped to \$196.8 million from \$3.1 billion in the fourth quarter of 2008 and \$12.8 billion in first quarter 2008. Since the third quarter of 2007, all issuance within this category has been of the cash flow type. Funded synthetic issuance fell to \$104.2 million, down 30.5 percent from \$150.0 million in fourth quarter 2008, although up 27.6 percent from \$75.4 million a year earlier. Synthetic issuance, both funded and unfunded, is expected to remain uncertain in the future as the credit default swap market transitions to new trading and settlement conventions in the United States and potentially Europe and Asia. Market value CDO issuance also continued to decline in first quarter 2009, with \$461.9 million issued, down from \$2.4 billion in fourth quarter 2008 and \$7.1 billion in first quarter 2008.

Based on CDO purpose segmentation, arbitrage CDOs remained the largest CDO asset class, accounting for \$658.7 million of issuance in first quarter 2009, while balance sheet CDOs took the remaining \$104.2 million of issuance.

Collateral and Currency Segmentation

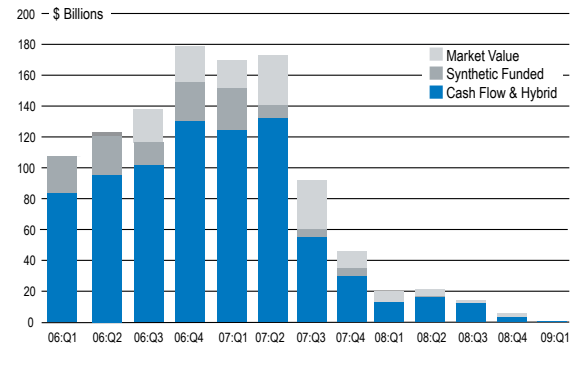
Although the structured finance (SF) collateral group encompasses a wide range of collateral types, it has been historically dominated by mortgage-related and asset-backed collateral. The shutdown of both mortgage- and asset-backed securities markets and reduced investor appetite spilled over into CDO issuance, with no new SF CDO issuance reported for first quarter 2009, compared to \$1.8 billion issued in fourth quarter 2008 and \$6.5 billion a year earlier.

Beginning in late 2008, the percentage of USD-denominated CDO issuance amongst global issuance has steadily declined. As of Q1 2009, USD-denominated CDO issuance makes up 25.8 percent of global funded CDO issuance, up from 20.4 percent in fourth quarter 2008 but down from 47.2 percent in the same period a year ago.

Euro-denominated CDO issuance shut down completely in Q1 2009 with no new issuance, down from \$2.7 billion issued in 4Q 2008. European institutions remained focused on liquidity through central bank repo operations; notably, the European Central Bank discontinued the eligibility of CDOs of ABS (SF CDO) for repo as of March 1, 2009. Other issuance, predominantly comprised of Korean won-denominated issuance, took the balance of total issuance, at \$461.9 million in the first quarter.

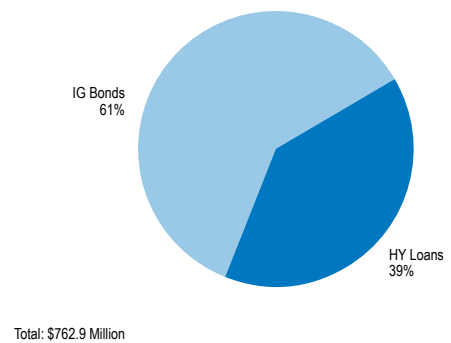
By segmentation, both the high yield loans and investment grade bonds were the only two collateral classes that made up CDO issuance, with \$301.0 million and \$461.9 million issued, respectively, in first quarter 2009, a decline from the \$2.9 billion and \$930.0 million issued, respectively, a year earlier.

Global CDO Issuance by Transaction Structure
2006:Q1–2009:Q1



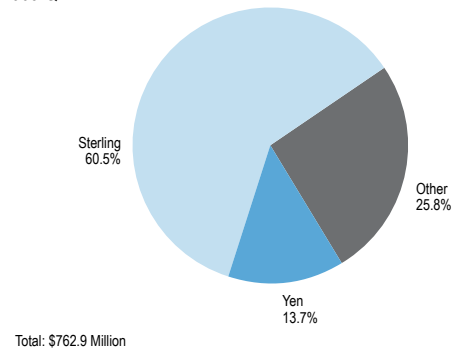
Source: Thomson Reuters

Global CDO Issuance by Underlying Collateral
2009:Q1



Source: Thomson Reuters

Global CDO Issuance by Currency
2009:Q1



Source: Thomson Reuters

Repo Average Daily Amount Outstanding Down 33 Percent in the First Quarter

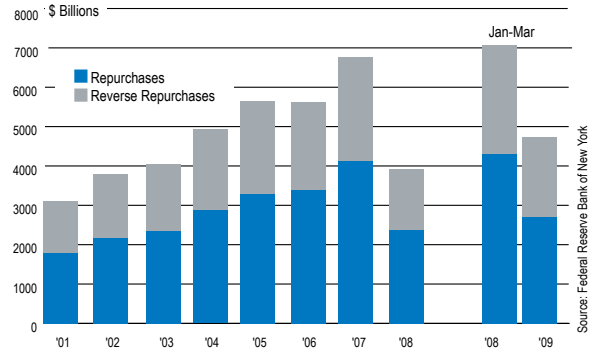
The average daily volume of total outstanding repurchase (repo) and reverse repo agreement contracts totaled \$4.7 trillion in the first quarter of 2009, a 33.2 percent decrease from the \$7.1 trillion average in the first quarter of 2008. Daily average outstanding repo totaled to \$2.7 trillion, a 37.1 percent decrease compared to \$4.3 trillion in the prior year, while reverse repo agreements averaged \$2.0 trillion, down 27.1 percent from the first quarter 2008 average. This data represents financing activities of the primary dealers reporting to the Federal Reserve Bank of New York, which includes repurchase and reverse repurchase agreements involving U.S. government, federal agency, agency mortgage-backed, and corporate securities.

CP Outstanding Continued to Decline in the First Quarter

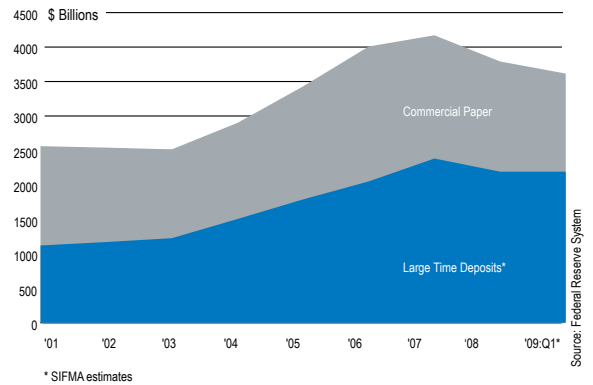
The outstanding volume of total money market instruments, including commercial paper (CP) and large time deposits, totaled \$3.6 trillion at the end of the first quarter of 2009, a 4.6 percent decrease from the \$3.8 trillion outstanding at end-December 2008.

CP outstanding totaled \$1.4 trillion at the end of first quarter, down 11.0 percent from the \$1.6 trillion totaled at the end of the prior year. Financial CP outstanding decreased 10.6 percent to \$638.2 billion at the end of the first quarter of 2009, from \$713.7 billion at the end of fourth quarter 2008. Non-financial CP outstanding reached \$149.7 billion, a 17.3 percent decline from the \$181.1 billion at the end of fourth quarter 2008.

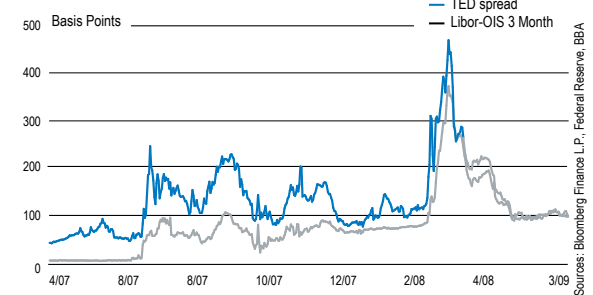
Financing by U.S. Government Securities Dealers
Average Daily Amount Outstanding 2001–2009:Q1



Outstanding Money Market Instruments
2001–2009:Q1*



TED Spread and Libor-OIS 3 Month Spread
Apr. 2007–Mar. 2009



Corporate Bond Issuance Rebounds in First Quarter

Total corporate bond issuance increased in the first quarter, rising 295.6 percent to \$267.3 billion from \$82.6 billion in the fourth quarter and was more than twice the \$220.9 billion issued in the same year-earlier period. In addition, \$267.4 billion was issued under FDIC; Temporary Liquidity Guarantee Program (TLGP).

U.S. high-yield debt issuance was \$10.8 billion in the first quarter of 2009, up 285.7 percent from the level in the fourth quarter of 2008, following two consecutive quarterly declines.

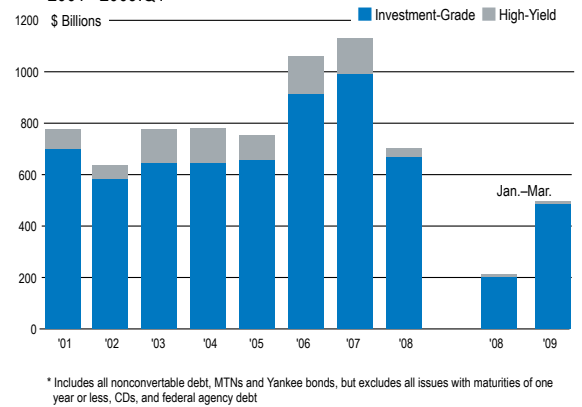
Credit Quality Remains Weak; Speculative-Grade Remains Elevated

Corporate credit quality has been declining in aggregate over the past year and is expected to continue to remain poor. With speculative-grade defaults accelerating, the number of credit downgrades rising and general concern about the future of the economy growing, S&P expects spreads to remain at their current elevated levels for some time. S&P reported that investment grade bond spreads contracted to 493 basis points (bps) at the end of the first quarter of 2009 from 523 bps at the end of 2008, remaining well above the five-year moving average of 185 bps. Speculative-grade spreads fluctuated considerably in the first quarter, falling from 1,628 bps at the beginning of the quarter to 1,399 bps at the end of February before rising to 1,428 bps at the end of the quarter, nearly three times the five-year moving average of 525 bps. As of March 31, 2009, consumer products, media and entertainment, and retail/restaurants continue to be the most affected sectors, unsurprising in light of falling consumer demand against a backdrop of economic and credit-market turbulence. These sectors, according to S&P, consistently have the highest levels of risk among distressed companies.

According to S&P's Global Fixed Income Research, large numbers of downgrades, especially in the stressed sectors, are likely to stay elevated through most of 2009. The U.S. continued to experience the highest number of defaults compared to the rest of the world, contributing 45 issuers this year out of 68 globally. The increase in defaults reflects a deep decline in the economic fundamentals and earnings prospects of companies. Other contributing factors to the expected rise in defaults are the credit freeze, which has effectively halted lending to speculative-grade borrowings, a record-high proportion of issuers with speculative-grade ratings, and the seasoning of much of the debt rated 'B-' or lower issued in the past several years. As a result of these factors, a large number of defaults will probably be concentrated in the first two to three quarters of 2009. The S&P U.S. speculative-grade default forecast is 13.9 percent for the next 12 months.

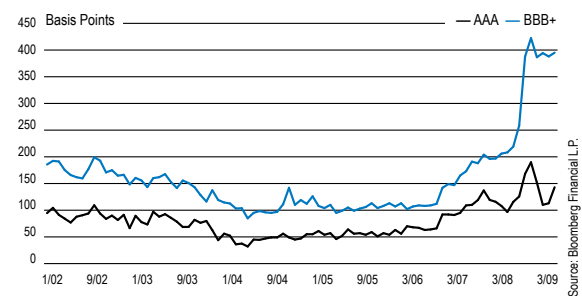
Corporate spreads remained under pressure and at elevated levels in the first quarter. As of March 31, the JP Morgan U.S. Liquid Index spread, or JULI, was 492 bps, compared to 475 bps in the immediately preceding quarter and 208 basis points in the same year-earlier period. The Merrill Lynch high yield index spread tightened 109 bps to 1,703 bps at the end of March from 1,812 bps in December, well above the 821 bps at the end of the first quarter 2008. The credit derivative swap market, as measured by Markit's CDX.NA.HY spread, widened to 1,543 bps, up 400 bps from the end-December 2008 spread of 1,143 bps.

Corporate Bond Issuance*
2001–2009:Q1



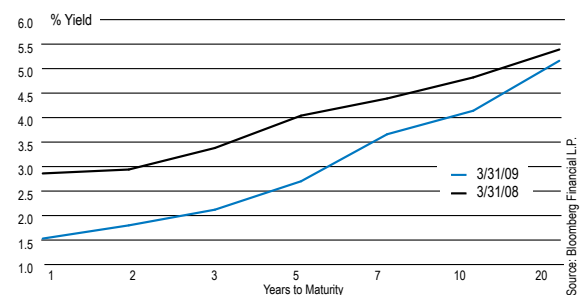
Source: Thomson Reuters

U.S. Corporate Spreads to U.S. Treasury — 10-Year
Jan. 2001–Mar. 2009



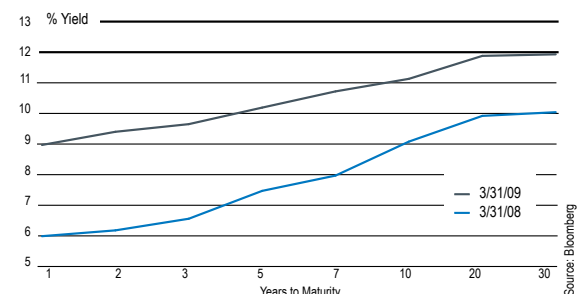
Source: Bloomberg Financial L.P.

U.S. Corporate: AAA Industrial — Yield Curves



Source: Bloomberg Financial L.P.

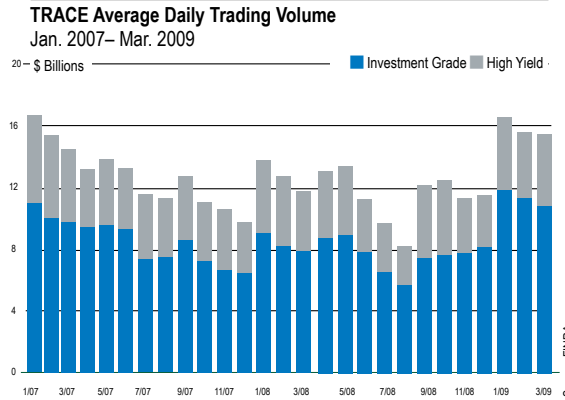
U.S. Corporate: BB Industrial — Yield Curves



Source: Bloomberg

Trading Volume

According to FINRA's TRACE system, estimated investment-grade bond average daily dollar trading volume was \$10.9 billion in the first quarter, up 32.9 percent from the \$8.2 billion average traded in the fourth quarter and 38.5 percent above the first quarter 2008 average. The first quarter high-yield bond average daily trading volume of \$4.6 billion marked a 37.3 percent increase from the previous quarter's \$3.4 billion and was 19 percent higher than the average in the same year-earlier period.



Underwriting and IPOs Dry Up; Trading Volume Declines

The equity markets continued their downward trend in the beginning of the first quarter as governments around the globe steer credit markets away from the edge. The U.S. government programs helped stabilize short-term debt markets, as President Obama's administration kicked off its financial rescue efforts with the February 10 announcement of TALF and the March 23 announcement of PPIP.

The equity markets continued to falter in the first quarter: the Dow Jones Industrial Average (DJIA) declined by 13.3 percent, the S&P 500 by 11.7 percent and the NASDAQ by 3.1 percent from end-fourth quarter levels. Since the close of the first quarter of 2008, the DJIA, S&P 500 and the NASDAQ have declined by 38.0 percent, 39.7 percent and 32.9 percent, respectively.

Share Trading Volume Down

The New York Stock Exchange's (NYSE) average daily share volume was 2.57 billion shares in the first quarter, 9.3 percent below the fourth quarter average, while the NASDAQ average volume decreased 2.0 percent to 2.23 billion shares. Compared to the first quarter a year ago, NYSE and NASDAQ volume declined 1.2 percent and 8.8 percent, respectively. The ARCA/AMEX average trading volume was 603.1 million shares in the first quarter, down 5.3 percent from the previous quarter, but up 49.3 percent from the first quarter of 2008.

The NYSE's average daily dollar trading volume fell to \$50.3 billion in the first quarter, down 22.8 percent from the previous quarter and 46.9 percent below that in the first quarter of 2008. NASDAQ average daily dollar trading volume, which declined for the fourth consecutive quarter, was \$38.9 billion in the first quarter, down 16.3 percent from the previous quarter and 45.7 percent below the same year-earlier period.

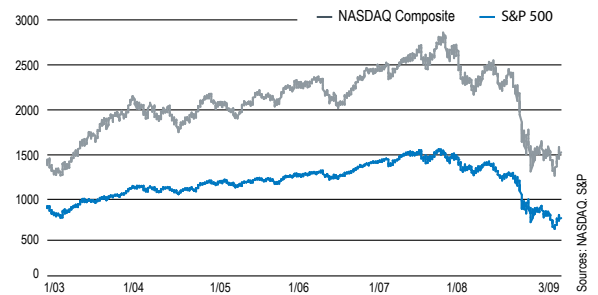
Short Interest Rises in First Quarter

NYSE short interest closed the first quarter at 16.6 billion shares, up 25.3 percent from the end of the fourth quarter, but 13.1 percent below the record high of 18.61 billion shares set on July 15. The 2009 first quarter level of 16.6 billion shares represented 4.2 percent of the total shares outstanding on the NYSE.

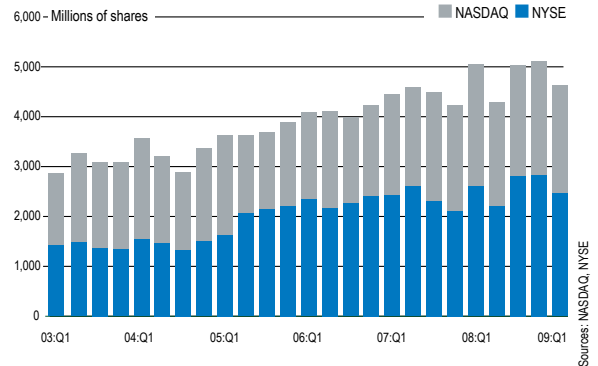
Total Corporate Underwriting Driven By Investment Grade

First quarter total corporate underwriting volume (corporate debt, securitizations, and equity issuance) was \$244.8 billion, up 89.7 percent from the \$129.0 billion in the fourth quarter, but down 28.2 percent from the first quarter of 2008. Equity underwriting declined to \$12.3 billion, down 72.5 percent from the prior quarter and 76.0 percent below that in the same year-earlier period. Initial public offerings (IPOs) and preferred stock offerings all but ceased in the first quarter of 2009.

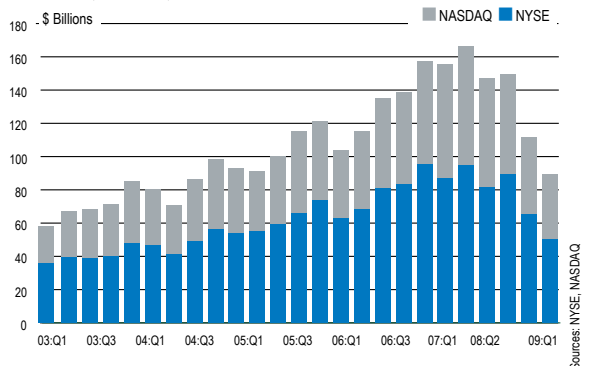
Daily Closing Stock Prices
Jan. 2003–Mar. 2009



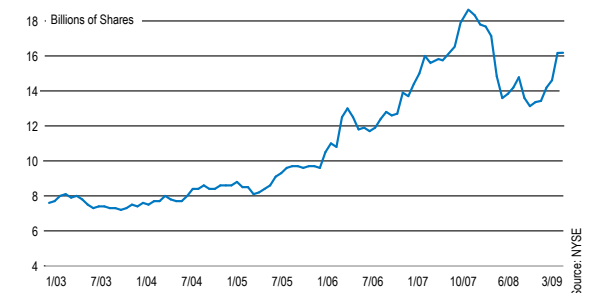
NYSE and NASDAQ Average Daily Share Volume
2003:Q1–2009:Q1



Equity Quarterly Average Daily Trading Volume
2003:Q1–2009:Q1



NYSE Short Interest
Jan. 2003 – Mar. 2009



First Quarter “True IPOs” Fell to 1975 Levels

U.S. IPOs raised \$1.2 billion in the first quarter of 2009, up from the previous quarter’s issuance of \$0.1 billion, but down 72.6 percent from the first quarter of 2008. “True IPO’s,” which exclude closed end fund IPOs, totaled \$0.8 billion, up from the \$0.1 billion issued in the previous quarter, but down 26.4 percent from the level in the first quarter of 2008. “True IPO” issuance was comprised of only 4 deals in the first quarter, compared to the 91-deal quarterly average recorded since 1990. The last time issuance was this low in back-to-back quarters was in the third and fourth quarter of 1975. The IPO backlog declined to \$1.4 billion on 10 deals at the end of the first quarter, from \$27.1 billion on 132 deals at the end of the first quarter in 2008, according to Dealogic.

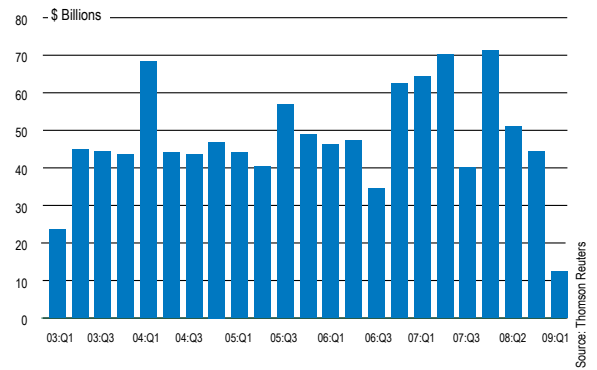
Secondary Offerings Fall to 2003 Level

First quarter secondary market issuance totaled \$10.4 billion, down 76.6 percent from the last quarter of 2008 and 24.4 percent below that in the same year-earlier period. This is the lowest quarterly issuance amount recorded since the first quarter of 2003, and was 59.7 percent below the \$25.8 billion quarterly average over the previous 23 quarters.

U.S. Mergers and Acquisition Shows Modest Increase

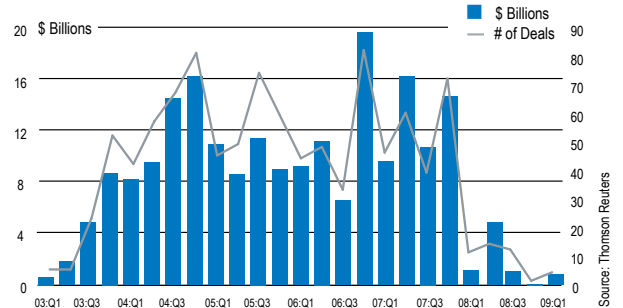
U.S. M&A announced deal volume rose in the first quarter to \$158.5 billion, 14.3 percent above the fourth quarter 2008 level of \$138.7 billion and 10.2 percent above the first quarter of 2008 volume of \$143.6 billion. The number of deals declined to 1,689, down 14.2 percent from the fourth quarter and over 30 percent below that in the same year-earlier period. The dollar volume of completed M&A deals totaled \$227.7 billion in the first quarter, a 12.0 percent decrease from the previous quarter, but 3.1 percent above that in first quarter 2008. The number of completed deals declined by 14.3 percent in the first quarter and was 37.4 percent below the first quarter 2008 level.

Total Equity Underwriting
2003:Q1–2009:Q1



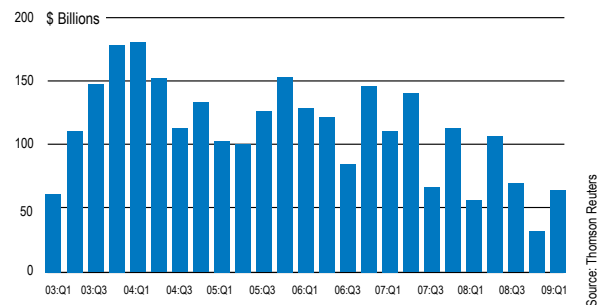
Source: Thomson Reuters

Quarterly “True” IPO - Excluding Closed-End Funds
2003:Q1–2009:Q1



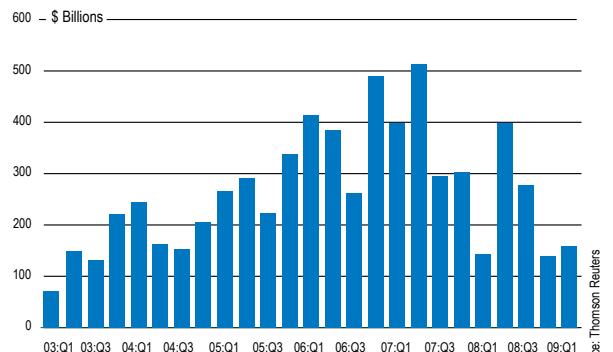
Source: Thomson Reuters

Quarterly Secondary Stock Offerings
2003:Q1–2009:Q1



Source: Thomson Reuters

U.S. Mergers and Acquisitions Announced Deals
2003:Q1–2009:Q1



Source: Thomson Reuters

P/E Declines

The P/E ratio of the S&P 500 stood at 11.30 at the end of first quarter, down 9.2 percent from the end of 2008 and 27.8 percent from the first quarter of 2008. This marked the third consecutive decline in the monthly average as well as the third consecutive quarterly decline.

Share Buyback Volume Down Again

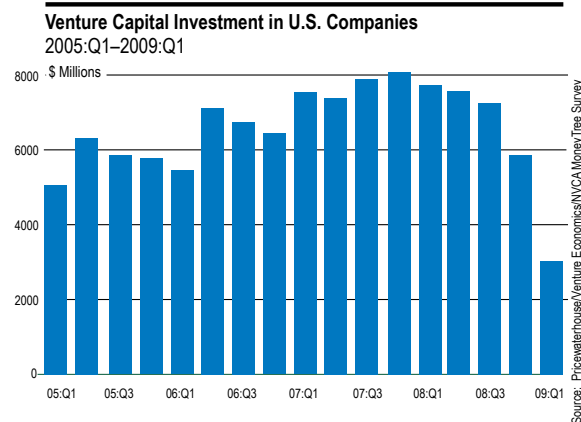
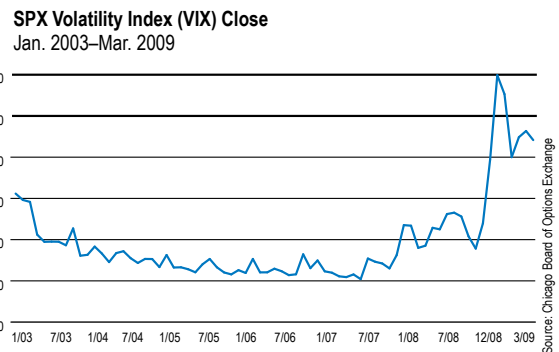
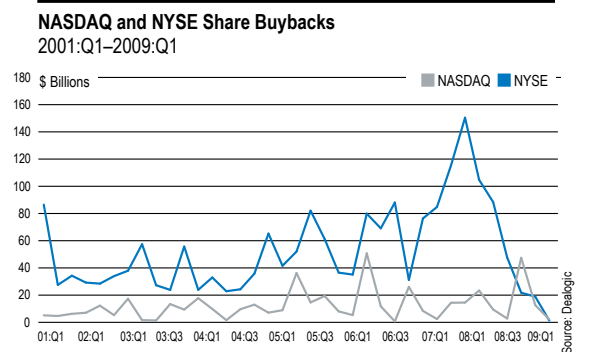
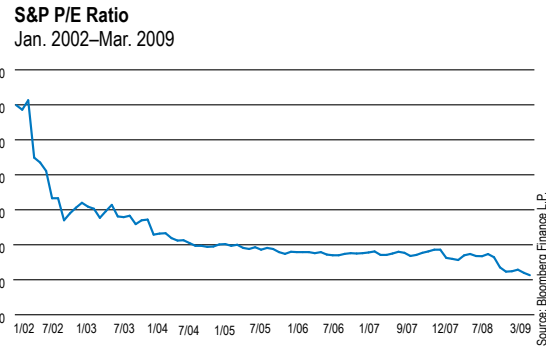
Corporate share repurchases declined for a sixth straight quarter, with first quarter 2009 buyback volume down 92.9 percent on the NYSE and 82.8 percent on the NASDAQ from the previous quarter. Announced buyback volume on the NYSE was \$1.3 billion on six share repurchase programs, while NASDAQ share buyback volume was \$2.2 billion on three programs. The first quarter buyback totals were the least recorded since 2000, for both the NYSE & NASDAQ.

CBOE Volatility Index Closes Quarter at Record High

The Chicago Board Options Exchange Volatility Index (VIX) closed the first quarter of 2009 at a quarter-end record high of 44.14, 10.4 percent above the year-end close of 40.00. The previous quarter-end high was recorded in the third quarter of 1998, when the VIX closed at 40.95. The volatility index never fell below 36 in the first quarter and reached an intra-day high of 57.36 on January 20, well below the record intra-day high of 89.53 set on October 24, 2008.

Venture Capital/Private Equity

Venture capital investments in the U.S. declined for the fifth consecutive quarter, totaling \$3.0 billion on 549 deals, down from \$5.7 billion on 866 deals in the fourth quarter and \$7.3 billion on 970 deals in the first quarter of 2008. The two strongest sectors remained software and biotechnology, with investment totals that reached \$614.2 million (138 deals) and \$576.8 million (81 deals), respectively.



Review of First Quarter Secondary Loan Market

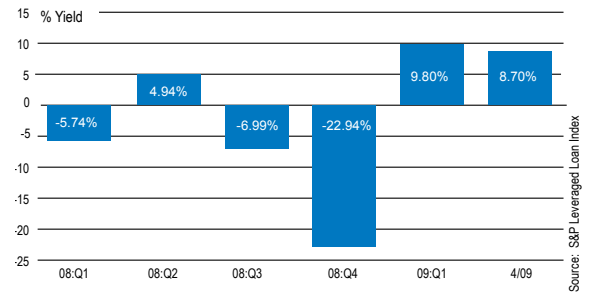
Although new loan supply has been mostly limited to debtor-in-possession (DIP) financing and amendments, the secondary loan market has seemingly found its footing in early 2009. Prices in the secondary market continued to rally higher during April following the best performing quarter in the history of the loan market. On the heels of January's 7.4 percent gain, the S&P/LSTA Leveraged Loan Index (LLI) generated a record 9.8 percent quarterly return during first quarter 2009 as bids in the secondary improved by 500 basis points (bps). Prices were beaten down to such low levels across the board by year-end 2008, that investors began to focus on differentiating credit quality from price; subsequently, the market began to bifurcate on the upswing. Savvy managers went bargain hunting for high quality paper that was oversold, while collateralized loan obligations (CLOs) searched for BB-rated paper priced in the 80s to help repair their dented over collateralization (OC) ratios. As a result, secondary trading increased 6 percent quarter-over-quarter to \$107.9 billion on more than 56,000 trades following three consecutive quarters of decline. Par trading fell by 10 percent to \$81.9 billion while distressed trading increased 164 percent to an all-time high of \$26 billion. Distressed trades accounted for 24 percent of activity by dollar value and 20 percent by trade count.

Price gains in 2009 have been historic even as fundamentals such as earnings and credit quality have weakened – there have been 21 defaults already this year. By month-end April, the default rate (by principal amount) spiked to a record 8 percent, from 3.75 percent at year end. But technicals have improved, most notably the lack of loans available for sale through Bids Wanted in Competition (BWIC) activity – an efficient and effective way to quickly sell-off large sized loan portfolios through an auction-type process. April BWIC activity fell to a miniscule \$240 million, a figure that indicates forced selling has subsided. However, with the average loan price hovering in the 70s, investors could no longer ignore the equity-like returns available across the secondary loan market. After bidding up high yield debt and equities to a point of relative unattractiveness, real money players swooped in to capture the still attractive senior secured yields available in the secondary loan market. As a result, April Mark-to-Market (MTM) price gains totaled 560 bps or 8.2 percent which increased the average secondary price of the LSTA MTM dataset to a 6-month high of 74. As bids strengthened and additional liquidity was available, bid-ask spreads tightened 21 bps to a 6-month low of 217 bps.

Since falling to an all-time low of 8 percent at year-end, the percentage of MTM loans priced above 90 rose to 17 percent during February, only to retract to 15 percent by quarter-end. By the end of April, that percentage hit 27 percent. Just as important, the percentage of loans priced below 70 declined markedly. The below 70 price segment had hovered between 48 percent and 49 percent - a noteworthy improvement from December's record high of 57 percent - but came crashing down to 39 percent by the end of April.

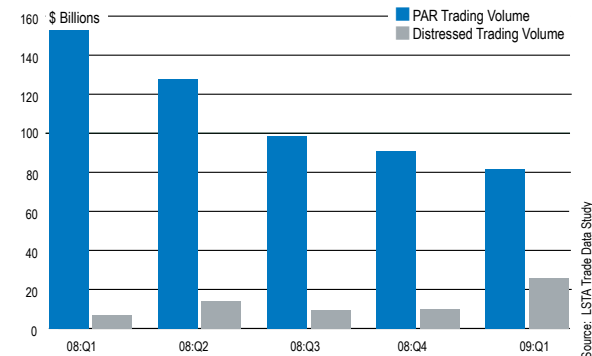
Following the record high 9.8 percent first quarter 2009 return, the S&P/LSTA Leveraged Loan Index powered forward with a 8.7 percent April return, also an all-time high. The index has now posted positive returns in each of the past four months elevating 2009's YTD return to 18.53 percent. Most of this year's gains occurred during two months – January and April. January's gains were a product of a market that bi-furcated on credit with the strong getting stronger and the weak getting weaker; April's gains, on

S&P/LSTA Leveraged Loan Index Returns
2008:Q1–2009:Q1



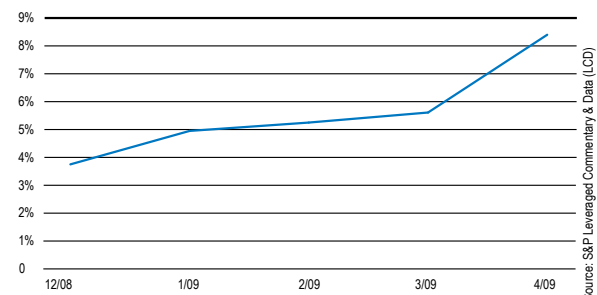
Source: S&P Leveraged Loan Index

Trading Volume
2008:Q1–2009:Q1



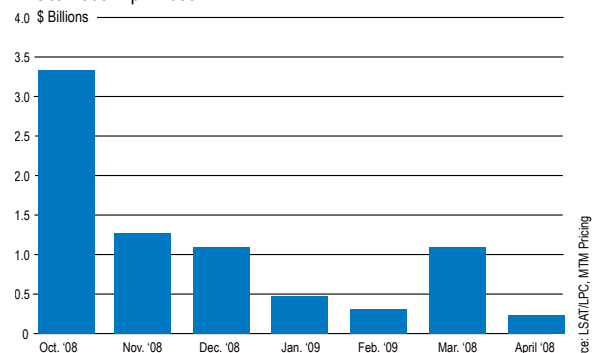
Source: LSTA Trade Data Study

Lagging 12-Months Default Rate by Principal Amount
Dec. 2008–April 2009



Source: S&P Leveraged Commentary & Data (LCD)

Bids Wanted in Competition (BWIC) Volume
Oct. 2008–April 2009

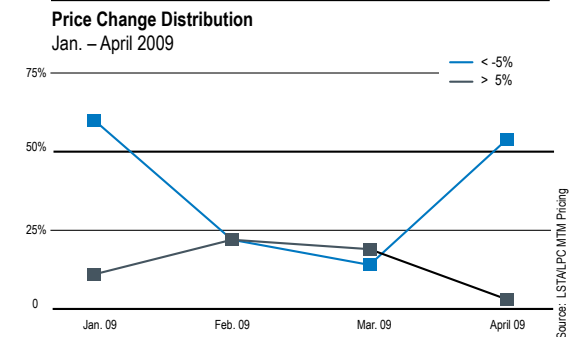
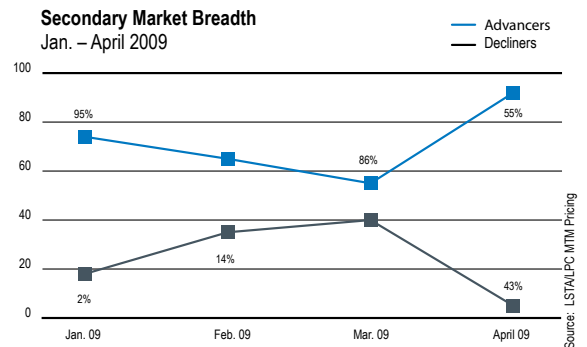
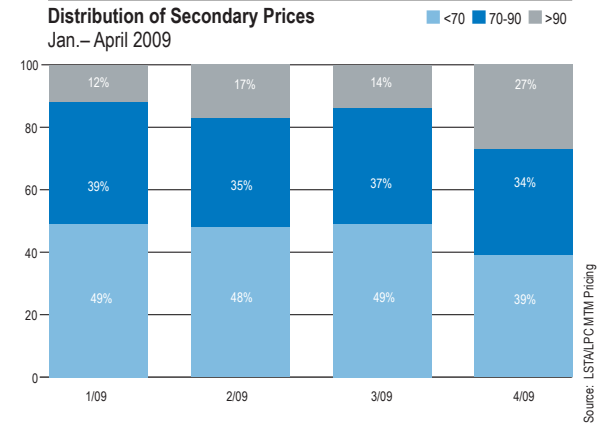
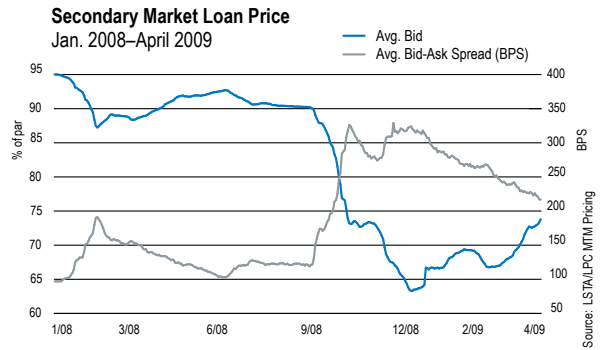


Source: LSTA/LPC, MTM Pricing

The author of the Leveraged Loan discussion is Ted Basta, Loan Syndication and Trading Association (LSTA), Vice President of Market Data & Analysis

the other hand, were substantially wide-spread and even included loans found in the CCC bucket. Supporting this market-wide rally, a whopping 92 percent of loans recorded MTM gains during April while only 5 percent reported losses on an advancer-decliner ratio of 18.4 to 1. Comparatively, during the January rally, 75 percent of loans recorded MTM price gains but 18 percent of loans reported losses. April's gains were not only widespread, but substantial. For example, the percentage of loans recording monthly MTM gains of 5 percent or more reached 54 percent in April. Conversely, the percentage of price drops at 5 percent or worse totaled only 3 percent; In January, 11 percent of MTM losses were in that range.

Year-to-date, loan prices strengthened by more than 1,100 bps, or 17 percent. At the same time, bid-ask spreads have narrowed by 100 bps, or 31 percent, but investors note that further retraction is necessary to bring back higher levels of liquidity and subsequent trading volumes. Whether the rally that pushed the average secondary loan price into the mid-to-high 70s is sustainable, the speed in which default rates are rising and expected recovery rates are falling will continue to pressure loan returns into the foreseeable future. However, April's gains came as a much needed boost to loan investor confidence, although no one has laid the bear to sleep just yet.



SIFMA RESEARCH DEPARTMENT

Kyle Brandon
Managing Director, Research
kbrandon@sifma.org

New York Staff
Switchboard: 212-313-1200

Charles Bartlett: cbartlett@sifma.org
Paul Rainy: prainy@sifma.org
Sharon Sung: ssung@sifma.org

Surveys
Bernard Reichert: breichert@sifma.org
Nancy Cosentino: ncosentino@sifma.org