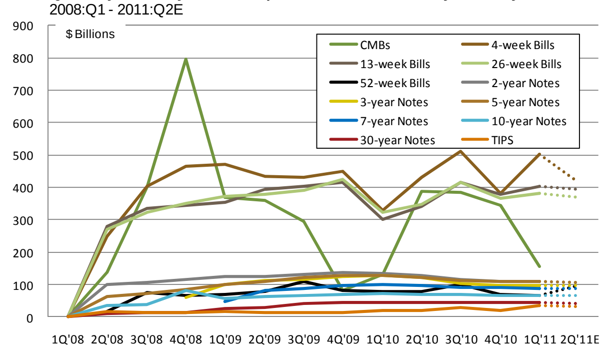
STABILIZING COUPON ISSUANCE; YIELDS TO RISE SLIGHTLY

Quarterly Summary of Bill, Coupon, and TIPS Issuance by Treasury
2008:Q1 - 2011:Q2E



Source: U.S. Treasury, 2Q'11 SIFMA Government Forecast Survey

TOTAL ISSUANCE OUTLOOK The SIFMA Quarterly Issuance Survey[1] forecasts total net Treasury bill, note and bond issuance to be $307.0 billion in the second quarter of 2011, approximately 15.8 percent above the net $265.2 billion issued (but 4.2 percent below the $320.5 billion previously forecast in SIFMA's 1Q'11 issuance survey[2]) in the first quarter of 2011 (actuals include cash management balances). Notably, 4-week bills issuance is expected to drop over 17 percent below 1Q'11 levels.

Excluding cash management bills (CMBs), total net issuance was $110.2 billion in 1Q'11, more than 4.5 times the $19.9 billion in the prior quarter. The use of short-term CMBs dropped significantly from being consistently over $100 billion in previous months to $25 billion and $30 billion in February and March 2011, respectively.

The total first quarter net issuance of $265.2 billion was a little higher than Treasury's February borrowing estimate[3] of $237 billion for the first three months of 2011. However, the $307.0 billion forecast for second quarter by survey participants is slightly above Treasury's February estimate of $299 billion.

The economy saw some signs of recovery during 1Q'11 as unemployment levels dipped slightly, consumer spending and confidence grew, and the housing market showed some stabilization. With the Dodd-Frank Act passed into law over nine months ago, the proposed rulemakings are well underway. The uncertainties remain, however, over just how final rules will be implemented, which may be a partial reason for slower pace of the economic recovery.

In addition, the national deficit currently rests at a little over $14 trillion and has been widely predicted to reach the $14.3 debt ceiling before May of this year. As of March 31, the total debt outstanding that is subject to the limit was $14.2 trillion, leaving approximately $76 billion before the debt limit is reached. With the shifting of political parties in both the House and Senate comes a shift in core interests. As investor confidence grows in a sustained economic recovery, priorities in Congress have swung to controlling the deficit and reducing national spending.

Overall, net issuance of bills and coupons are expected to continue to decline further in 2Q'11. Treasury previously indicated through their November refunding process that they will be stabilizing coupon issuance (with the potential for further reductions) and increasing TIPS auctions.

TREASURY COUPON ISSUANCE The median forecast for net new issuance of Treasury coupon securities (notes and bonds) is $357.0 billion in the second quarter, 5.2 percent above 1Q'11's net issuance of $339.2 billion.[4] Gross coupon issuance is expected to total approximately $533 billion, 3.1 percent below the $550.2 billion issued in the prior quarter. Survey respondents also expect Treasury to finish 2Q'11 with $85 billion in cash,[5] below the $95 billion mark Treasury estimated in February for an end-June cash balance. Part of the difference may be due to some respondents excluding from their forecasts the $5 billion allocated for Treasury's Supplementary Financing Program (SFP). The percentage of nominal coupons in the Treasury's portfolio has risen to 73 percent (from long-term average of 69 percent) and is expected to rise further as the Treasury's goal is to continue to extend the average maturity of outstanding debt.

[1] The survey was conducted beginning on April 6, 2011 and ending on April 19, 2011. Survey results are medians and the dates and numbering of quarters are based on calendar year rather than fiscal year, unless otherwise noted. A description of the participants is provided on page 5. Previous survey reports may be found at http://www.sifma.org (Research Reports).

[2] SIFMA's 1Q'11Government Forecast Survey results can be found here.

[3] See US Treasury's first quarter 2011 marketable borrowing estimates.

[4] Net coupon issuance projections for the second quarter of 2011 ranged from $337 billion to $532 billion.

[5] Net cash position projections for the end of the second quarter of 2011 ranged from $15 billion to $290 billion.

AGENCIES' COUPON ISSUANCE Survey participants forecast total gross coupon issuance by the four largest Federal agencies to be $227.4 billion in the second quarter.[6] Survey respondents indicated that approximately 37 percent of 2Q'11's issuance volume is expected to come from the Federal Home Loan Banks (FHLBs), 25 percent from Fannie Mae, 30 percent from Freddie Mac, and the remaining 8 percent from the Farm Credit System Banks.

The Administration's Housing Finance Reform White Paper [7] has been released in February and specifically addressed the Government Sponsored Enterprises (GSEs). The paper provided an analysis of what led to the current situation and outlined many areas that need to be addressed in the reform.

T-BILL ISSUANCE Survey participants expect to see net bill redemption of $50 billion in the second quarter, slightly smaller than the $74 billion redeemed in the first quarter of 2011. The wide variance in responses received[8] showed there was no consensus on expectations for net bill issuance. The Treasury bills have fallen as a percentage of the portfolio to 20 percent since November 2010. This trend is expected to continue especially as the Treasury announced that it would reduce the size of the Supplementary Financing Program (SFP) from $200 billion to $5 billion. This action was taken to provide flexibility to debt managers, given the proximity to the statutory debt limit.

TIPS Survey respondents forecast that Treasury will issue $32 billion of Treasury Inflation-Protected Securities (TIPS) in the second quarter, 6.4 percent below the $34.2 billion issued in 1Q'11. Treasury announced that it has been pleased by the performance of TIPS auctions over the past year, particularly in light of the increase in issuance. Going forward, Treasury expects to issue over $100 billion in TIPS in 2011. No further changes to the program are expected in the near future.

U.S. TREASURY YIELD OUTLOOK

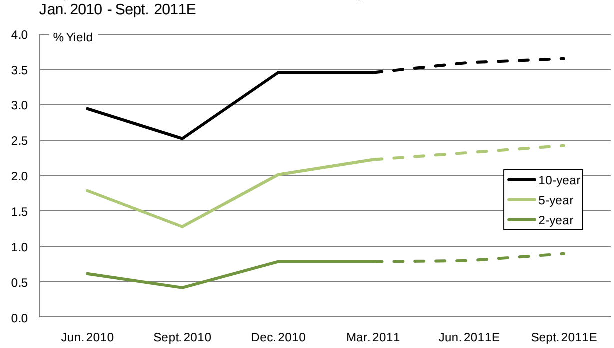
The survey forecasts benchmark Treasury yields will slightly increase going forward through the third quarter of 2011, following a period of significant yield increases since November 2010 (and following the QE2 announcement). Recently, Treasury yields have increased slightly both in the front- and back-end of the curve. 2-year rates increased from 0.59 percent in 4Q'10 to 0.79 percent in 1Q'11 and 10-year rates rose from 4.35 percent to 4.51 percent during the same period. Concerns about inflation and the value of the US Dollar have correspondingly risen as well. Going forward through September of this year, survey respondents do forecast increase in yields (summarized in the table on the left side).

Treasury Yield Projections and Ranges

	Mar. 31, 2011	Jun. 30, 2011 E	Sept. 30, 2011 E
2 year Treasury Note	0.79	**0.8** (0.7 - 1.0)	**0.9** (0.8 - 1.4)
5 year Treasury Note	2.22	**2.3** (2.2 - 2.7)	**2.4** (2.3 - 3.1)
10 year Treasury Note	3.45	**3.6** (3.3 - 3.9)	**3.7** (3.5 - 4.5)
30 year Treasury Bond	4.51	**4.7** (4.5 - 5.0)	**4.7** (4.6 - 5.4)
3 Month LIBOR	0.30	**0.3**	**0.3**

Source: 2Q'11 SIFMA Government Forecast Survey

Projected 2-Year, 5-Year, and 10-Year Treasury Yield Movement
Jan. 2010 - Sept. 2011E



Source: U.S. Treasury, 2Q'11 SIFMA Government Forecast Survey

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[6] Includes Fannie Mae, Freddie Mac, the Federal Home Loan Banks (FHLBs), and the Federal Farm Credit Banks Funding Corporation.
[7] SIFMA Statement on Administration's Housing Finance Reform White Paper can be found here.
[8] Net bill issuance projections for the second quarter of 2011 ranged from a net redemption of $150 billion to a net issuance of $161 billion.

UPSIDE AND DOWNSIDE RISKS TO RATES

The survey also asked participants about risks to their forecasts or events that could cause interest rates to move higher or lower than forecasted (summarized below in Table 4). The dominant risks identified on the upside (higher-than-expected yields) were: faster-than-expected economic recovery, growing inflationary pressures, failure to raise the debt ceiling (and related national budget problems), and earlier Fed tightening actions.

Conversely, the main risks noted on the downside (lower-than-expected yields) were: slowdown in economic progress or growth, weakening economy, spilling over from continued European sovereign debt troubles, collapse of long-term inflation expectations, and another round of bond-buying program.

Summary of Risks to Rate Forecast

	Risks to Upside	Risks to Downside
#1	Debt ceiling impasse lasting longer and turning into fical crisis	European sovereign debt risk flare
#2	Misinterpratation of debt ceiling constraint; upward inflation surprise; upside economic growth surprise	Downside economic growth surprise; collapse of long-term inflation expectations
#3	Fed tightening the policy early	US economy weakening
#4	Continued difficulty for the budget compromise and debt ceiling increase; market concern at the end of QE2 in June	Less than expected job recovery; the Fed cointinuing to discount a recent spike in commodity prices
#5	Stronger than expected growth; the Fed raising rates sooner than Q1 2012	Lowered inflation expectations; renewed global risk contagion that causes flight to Treasuries
#6	Higher than expected inflation	Economic data weaker than expected
#7	End of QE2 having larger impact than expected	QE3

Source: 2Q'11 SIFMA Government Forecast Survey

SPREADS OUTLOOK

Respondents expect agency-to-Treasury yield spreads and swap spreads to widen slightly for the short-term securities through the second and third quarter of 2011 and stay flat for the intermediate- and long-term securities. The 3-month LIBOR rate is expected to stay flat at 0.3 percent through the next two consecutive quarters.

Distribution of Duration Weightings

	Strong Over	Over	Neutral	Under	Strong Under
0-3 yrs	0%	33%	17%	50%	0%
3-7 yrs	0%	17%	50%	17%	17%
7-10 yrs	0%	33%	17%	17%	33%
10-30 yrs	0%	17%	17%	17%	50%

Source: 2Q'11 SIFMA Government Forecast Survey

PORTFOLIO ALLOCATION RECOMMENDATIONS

The survey asked for model portfolio allocation recommendations, compared to the current portfolio weighting, across the maturity spectrum of the U.S. Treasury yield curve. The results generally favor a neutral and underweight recommendation for the shorter time horizons and are mixed when it comes to longer time horizons. What is worth pointing out, none of the survey respondents recommended strongly over-weighting any of the time horizons.

SIFMA'S GOVERNMENT SECURITIES ISSUANCE AND RATES FORECASTS

SIFMA's Government Securities Issuance and Rates Forecast

Forecast numbers appear in bold

Issuance Projections (in $Billions)

U.S. Treasury Borrowing[1]	1Q'11	2Q'11E
Net Coupon Issuance	339.2	**357.0**
Gross Coupon Issuance	*550.2*	***533.0***
Gross Coupon Redemptions	*211.0*	***176.0***
Net Bill Issuance	(74.0)	**(50.0)**
Gross Bill Issuance	*1,510.7*	***1,254.0***
Gross Bill Redemptions	*1,584.8*	***1,300.0***
Quarter end cash balance (expected)	190.6	**85.0**
U.S. Treasury Quarterly Gross New Issuance		
4 week Bill	502.7	**416.0**
13 week Bill	404.0	**394.0**
26 week Bill	382.0	**368.0**
52 week Bill	67.0	**96.0**
2 year Treasury Note	109.2	**105.0**
3 year Treasury Note	97.4	**96.0**
5 year Treasury Note	109.2	**105.0**
7 year Treasury Note	88.9	**87.0**
10 year Treasury Note	67.0	**66.0**
30 year Treasury Bond	42.7	**42.0**
Treasury Inflation-Indexed Securities	34.2	**32.0**

Federal Agency: Projected Total Gross Coupon Debt Issuance[2]	
Fannie Mae	**55.8**
Freddie Mac	**67.8**
Federal Home Loan Bank System - Office of Finance	**83.8**
Federal Farm Credit Banks Funding Corporation	**20.0**

	FY estimates
Federal Budget Deficit Estimate - FY2011	**1,400.0**
Federal Budget Deficit Estimate - FY2012	**1,100.0**

Rates & Spreads Outlook

Interest Rates (End of Quarter in %Yield)	3/31/11	6/30/11E	9/30/11E
2 year Treasury Note	0.79	**0.8**	**0.9**
5 year Treasury Note	2.22	**2.3**	**2.4**
10 year Treasury Note	3.45	**3.6**	**3.7**
30 year Treasury Bond	4.51	**4.7**	**4.7**
3 Month LIBOR	0.30	**0.3**	**0.3**
Spreads to Treasury (End of Quarter in Basis Points)			
2 year Agency Benchmark/Reference Notes[3]	6.5	**6.8**	**7.0**
5 year Agency Benchmark/Reference Notes[3]	20.5	**20.0**	**20.0**
10 year Agency Benchmark/Reference Notes[3]	44.0	**35.0**	**35.0**
2 Year SWAP Spreads	16.9	**20.0**	**20.0**
5 Year SWAP Spreads	20.0	**20.0**	**20.0**
10 Year SWAP Spreads	10.5	**9.0**	**11.0**

[1] *Excluding Federal Reserve's purchase*

[2] *Including all callable coupon issuance and excluding all discount notes*

[3] *Agency spreads to Treasury yield are in basis points.*

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The Securities Industry and Financial Markets Association's Quarterly Government Securities Issuance and Rates Forecast reflects the responses to a survey of members of the Association's Primary Dealers Committee and Government Securities Research and Strategist Committee. The Committee is composed of trading strategists and research analysts at Association member firms who specialize in the U.S. government and agency securities markets. The survey is intended to provide market participants with the current consensus expectations and median forecasts of many of the Primary Dealers and other firms active in the U.S. government and agency securities markets.

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