SIFMA®
Securities Industry and
Financial Markets Association

RESEARCH REPORT

AUGUST 2009

RESEARCH QUARTERLY

Volume IV
No. 8

New York ▪ Washington ▪ London ▪ Hong Kong

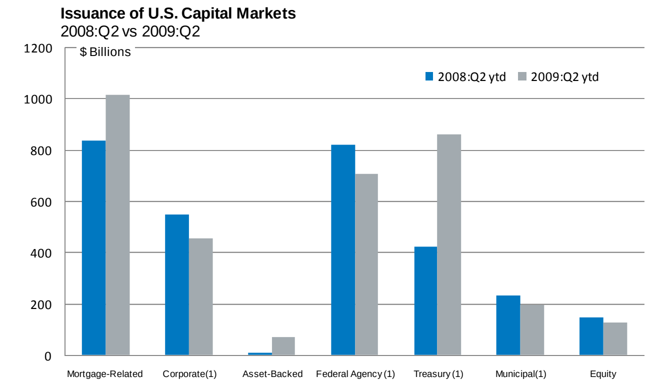
Table of Contents

Capital Market Issuance Reached $3.31 Trillion in Second Quarter 2009

Securities issuance totaled $3.42 trillion in the first half of 2009, a 13.5 percent increase over the $3.01 trillion issued in the first half of 2008. Equity underwriting grew as the secondary market rebounded in the second quarter, though initial public offerings remained anemic. Issuance of asset-backed securities increased over the previous quarter, but was lower then levels in the same year-earlier period. The market for mortgage-backed securities continued to be dominated by agency MBS as rising delinquencies, increasing foreclosure rates, declining home prices and tighter mortgage underwriting guidelines continued to depressed the sector and are expected to persist for some time.

Federal agency debt issuance decreased in the second quarter from the first quarter and was slightly less than the $820.3 billion issued in the second half of 2008. Treasury issuance fell modestly as the federal government sought to meet the expected budget shortfall. Municipal fund raising was up from the previous quarter, aided in part the introduction of Build America Bonds, which were launched in the market in April as part of the federal government's stimulus plan.

Most economists agree that a U.S economic recovery is expected to emerge later this year, although the strength of that recovery is not expected to be robust. Though still tight, credit conditions have eased during the second quarter, the housing market data suggest a bottom may be near. Despite some positive signs, there are reasons to be cautious. The number of home foreclosures continues to increase, the national unemployment rate has risen to a post-1983 high 9.5 percent and is still rising, and the expanding federal deficit may pose serious problems in future.



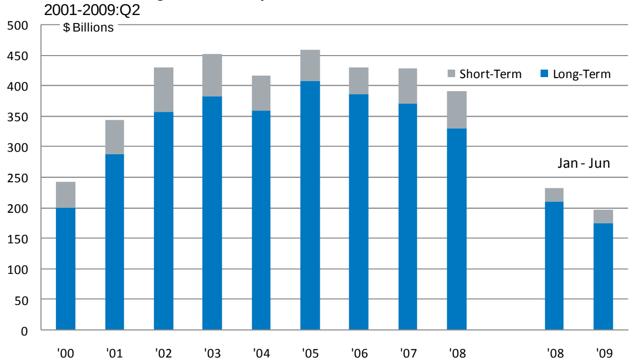
(1)Includes long-term issuance only
Source: Thomson Reuters, U.S. Treasury, U.S. Federal Agencies

Issuance Highlights

$ Billions	2009:Q2 only	2008:Q2 ytd	2009:Q2 ytd	% Change
Municipal (1)	111.2	231.5	196.6	-15.1%
Treasury (1)	533.5	423.6	860.3	103.1%
Federal Agency (1)	290.8	820.3	704.5	-14.1%
Mortgage-Related	648.1	836.7	1,013.3	21.1%
Asset-Backed	49.6	114.4	67.4	-41.1%
Global CDO	1.8	41.9	2.6	-93.8%
Corporate (1)	237.5	334.8	454.6	35.8%
Equity	111.6	147.4	124.3	-15.7%

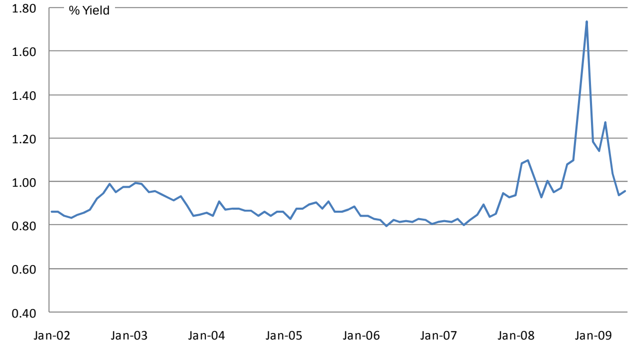
* Percent change between 2009:Q2 and 2008:Q2
(1) Includes long-term issuance only

Short-[1] and Long-Term Municipal Issuance
2001-2009:Q2



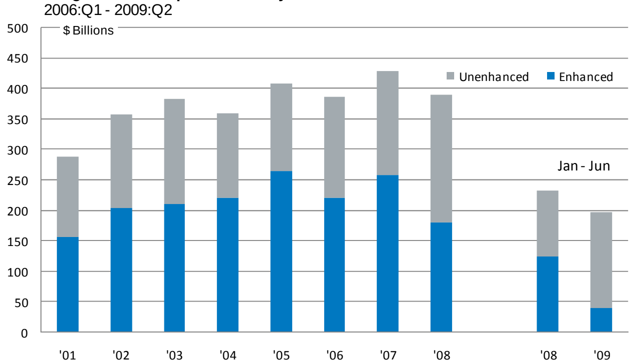
[1]Includes maturities of 13 months or less
Source: Thomson Reuters

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



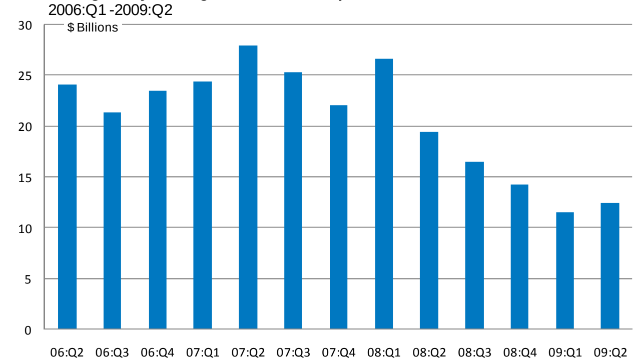
Source: Bloomberg Finance L.P.

Long-Term Municipal Issuance by Enhancement Status[1]
2006:Q1 - 2009:Q2



[1]Includes maturities of 13 months or more
Source: Thomson Reuters

Average Daily Trading Volume of Municipal Securities[1]
2006:Q1 -2009:Q2



[1]Includes both dealer-to-dealer and customer-to-dealer transactions.
Source: Municipal Securities Rulemaking Board

Municipal Issuance Volume Rose

Short- and long-term municipal issuance totaled $111.2 billion in the second quarter of 2009, up 30.2 percent from the $85.4 billion issued in the first quarter of 2009, but still less than the $146.1 billion issued in the same year-earlier period. Issuance totaled $196.6 billion in the first half of 2009, down 15.1 percent from the $231.5 billion issued in the same period last year.

The lengthy recession and declining home prices has caused tax collections to decline in virtually every state. Personal income tax (PIT) revenues, which on average account for 36 percent of a state's revenues, have declined so dramatically that many states are facing the most severe financial crisis in many years. A June 2009 report released by the Rockefeller Institute of Government showed that state income tax revenues declined by 26 percent, or $28.8 billion, in the first four months of 2009, compared to the same year-earlier period.

The municipal bond market has been hit especially hard in the second quarter; for the first time Moody's placed all municipal bonds on negative credit watch, foretelling potentially widespread downgrades. The impact of fiscal distress on cities and states across the nation has been profound, most notably in California. Unable to reach a budget deal, California began issuing IOUs, a maneuver not utilized since the Great Depression. Both Moody's and Fitch recently downgraded California's debt ratings; Moody's and Fitch affects approximately $72 billion and $79 billion, respectively, of general obligation and lease supported bonds.

Long-term municipal issuance volume was $95.2 billion in the second quarter of 2009, up from $79.9 billion issued in the first quarter but down from $128.9 billion issued in 2Q'08. Short-term issuance in the second quarter of 2009 was $16.1 billion, nearly three times the $5.4 billion issued in the first quarter, but slightly below the $16.9 billion issued in the same year-earlier period. The second quarter issuance surge was due in part to the introduction of Build America Bonds (BABs) in April as part of President Obama's stimulus package. BABs are taxable municipal bonds that provide either (1) a payment to the issuer equal 35 percent rebate on the interest paid on the bonds or (2) a tax credit to the bond holders of up to 35 percent of the interest they receive, although few of this second type have been issued. Second quarter 2009 BAB issuance amounted to $15.4 billion, with California being the largest BAB issuer at $6.0 billion.

Issuers' use of bond insurance, which has been declining over the past couple of years, continued to drop in the first half of 2009. Only 11.0 percent of all new issues carried bond insurance in the first six months compared to 24.0 percent in the first half of 2008. Letters of credit from domestic banks also decreased over the same time period, to 5.1 percent of issuance from 12.6 percent.

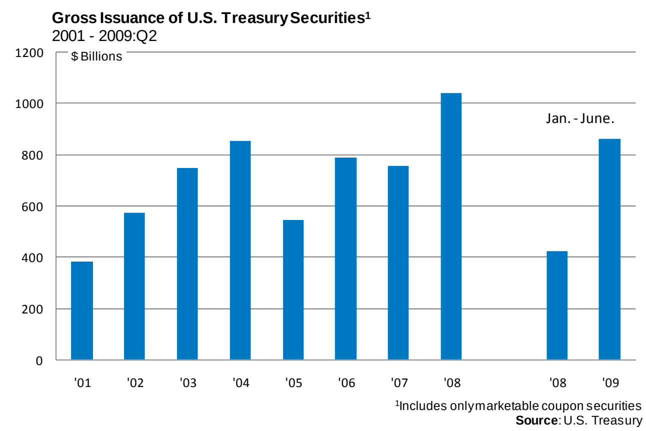
Issuance of variable rate demand obligations (VRDOs) accounted for 8.7 percent of total municipal issuance in the second quarter of 2009, down from 8.8 percent in the previous quarter, while fixed-rate issuance decreased to 86.7 percent from 89.2 percent. Unenhanced new issues on a dollar volume basis rated AAA by Moody's Investors Services declined to 7.6 percent in the first half of 2009 from 14.9 percent in the same year-earlier period, and those rated AAA by Standard & Poor's rose to 22.8 percent from 16.3 percent.

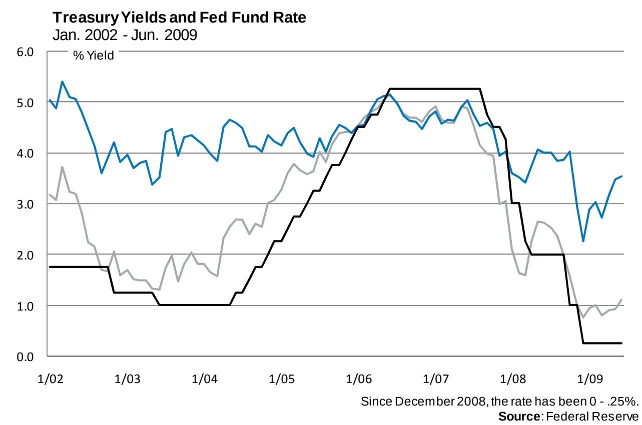
The yield ratio of AAA-rated 10-year municipals to that of comparable 10-year Treasury securities ended the second quarter of 2009 at 95 percent, still above the pre-crisis average of 85 percent in 2007, but well below the level of 174 percent recorded at the end of 2008. AAA-rated municipal bond yields ended 2Q'09 at 3.37 percent, down from 3.45 percent at the end of the first quarter and 4.00 percent at the end of the same year-earlier period. The SIFMA Municipal Swap Index yield declined to 0.30 percent at end-June compared to 0.54 percent on March 25. As of the end of the second quarter, the 52-week average was 1.40 percent.

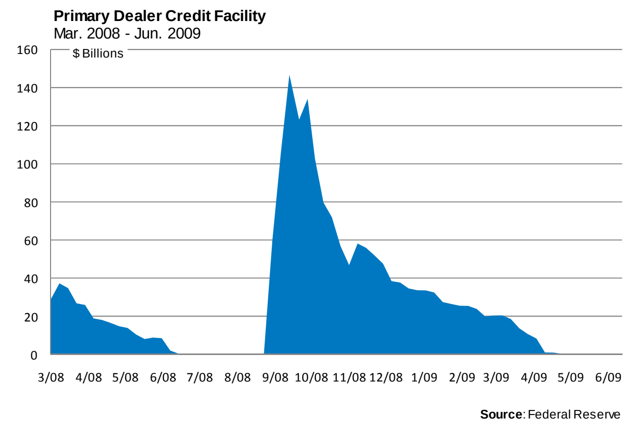
New Money Volume Rises, Refundings Fall in First Half

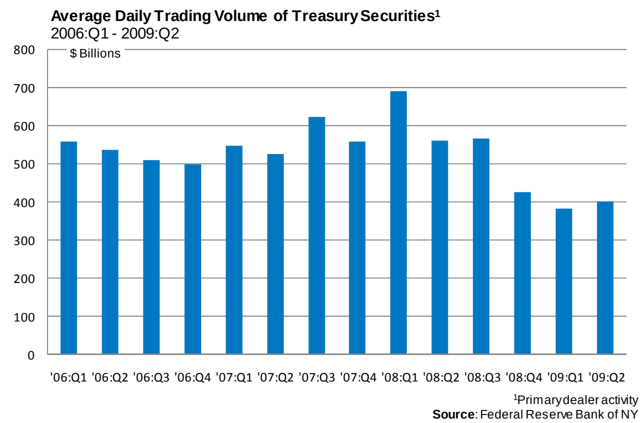
New capital issuance totaled $122.8 billion in the first half of 2009, 2.9 percent greater than that in the first half of 2008. The larger use-of-proceeds sectors also saw an issuance increase in the first half of the year compared to the same period in 2008; general government sector issuance grew 32.5 percent to $41.2 billion; education-related issuance rose X percent to $31.6 while transportation sector issuance increased 11.7 percent to $16.4 billion.

Refunding activity totaled $73.8 billion in the first half of 2009, dropping 33.8 percent from the $111.5 billion issued in the first half of 2008. Issuance volume fell in most sectors, with eight sectors falling and only two sectors rising. Transportation-related issuance took the largest percentage hit, falling 79.5 percent to $3.3 billion while education-related issuance fell 21.6 percent to $18.4 billion . In contrast, the general government sector saw an increase of 32.4 percent to $23.3 billion.









Net Treasury Redemptions Decline, Fed Rates Remained Unchanged

Total second quarter net issuance of U.S. Treasury securities, including bills and coupons but not including cash management bills, was negative for the third consecutive quarter, with a net redemption of $16.6 billion, compared to a net redemption of $51.9 billion in the first quarter and $45.6 billion in the second quarter of 2008. Net coupon issuance was $370.4 billion, more than double the $165.6 billion issued in the first quarter and seven times the $52.3 billion issued in the same year-earlier period. Consistent with the results of SIFMA's recent Government Forecast,[1] 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 budget deficit of $455 billion for fiscal year (FY) 2008, which was less than the forecast of $482 billion. The budget deficit in fiscal year 2009 is expected to rise to $1.8 trillion, according to a recent survey of the SIFMA Economic Advisory Roundtable.[2]

Gross coupon issuance volume increased 142.7 percent during the second quarter of 2009 to $533.4 billion from $219.8 billion in the second quarter of 2008, while retirements were flat. Gross issuance of bills was flat, while retirements rose. 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 $400.5 billion in the second quarter, 4.7 percent higher then the $382.4 billion in the first quarter but 28.5 percent below $560.5 billion average recorded in the second quarter of 2008.

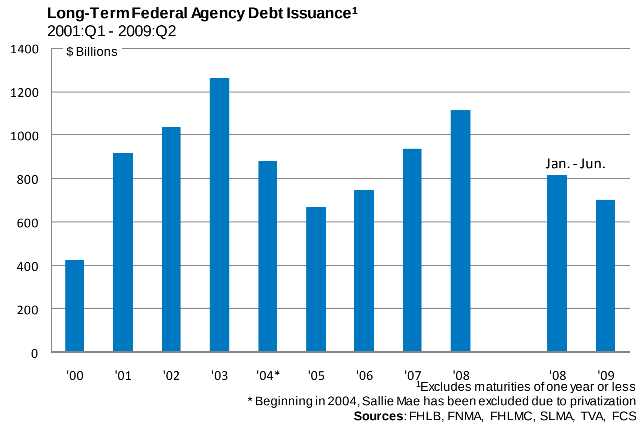
The number of primary dealers closed at the end of the second quarter at a low of 16 with the consolidation of Merrill Lynch in February and withdrawal of Dresdner Kleinwort; however, the addition of Jefferies and RBC, as well as the return of Nomura, increased the number of primary dealers to 18.

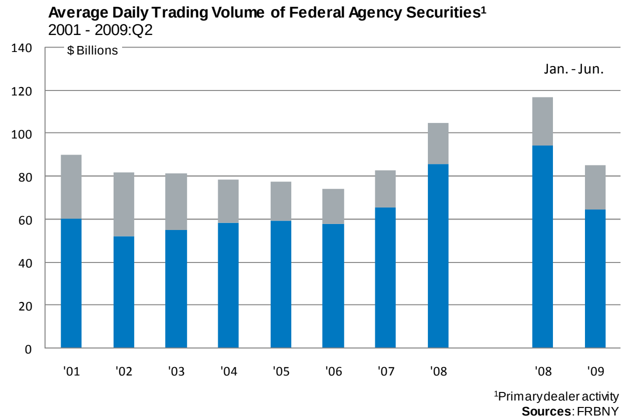
Second quarter news was dominated by the debate over signs of economic stabilization and concerns over the potential inflationary impact of both expansionary monetary and fiscal policies, unlike the first quarter, which had been dominated by efforts to stabilize financial markets and industry. Inflationary

[1] The most recent SIFMA Government Forecast can be found at: www.sifma.org/research/pdf/GovForecast0709.pdf
[2] The most recent SIFMA Economic Advisory Roundtable forecast can be found at: www.sifma.org/research/pdf/EconOutlook0609.pdf

concerns are driven mainly by worries over size of the existing fiscal stimulus package and other contemplated programs, such as health care reform currently under debate, as well as the dramatic expansion of the Federal Reserve's balance sheet in programs such as TALF and the agency and federal securities purchase program, even as usage of the Federal Reserve's other liquidity facilities has receded. On the other side of the debate are those more concerned about deflation who point out that without fiscal spending there would be no signs of economic stabilization and that the expansion of the Fed's balance sheet is no imminent danger because the banks are not using those reserves and therefore cannot transmit any increase to the economy.

The 2-year Treasury yield was 1.11 percent at the end of the second quarter, up from 0.81 percent at the end of the first quarter and 0.76 percent at end-December 2008. The 10-year Treasury yield rose more steeply, increasing to 3.53 percent at the end of the second quarter from 2.71 at the end of the first quarter and 2.25 percent at the end the previous quarter. The 2-year to 10-year yield spread increased to 242 basis points (bps) at the end of the second quarter from 190 bps at the end of the first quarter and 149 bps at the end of December 2008. Traders track this *spread*, or difference, in yield between the 2–year U.S. Treasury note and the 10–year Treasury note because it represents expectations about the direction of Fed monetary policy, as well as inflationary expectations in the economy.





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 second quarter of 2009, federal agency long-term debt issuance totaled $290.8 billion, a decrease of 29.7 percent from the $413.7 billion issued in the first quarter 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 totaled $97.2 billion in the second quarter, 12.2 percent below that in the first quarter and 42.7 percent below the $169.6 billion issued in the same year-earlier period. Year-to-date, FHLB issuance was $207.9 billion, over 45 percent below that in the first half of 2008.

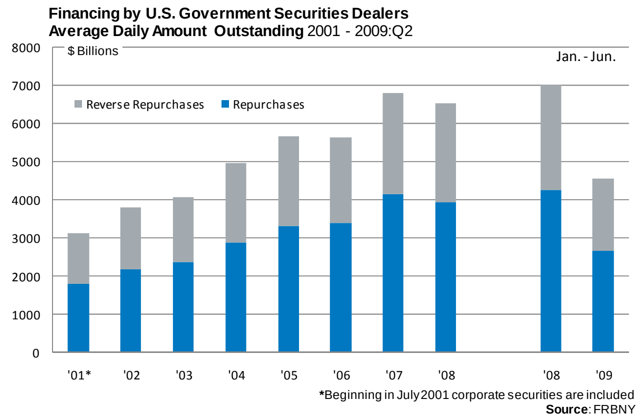
Late in the third quarter of 2008, the U.S. government put Fannie Mae and Freddie Mac into conservatorship. The two agencies issued $84.0 and $105.3 billion of long-term debt, respectively, in the second quarter of 2009, a slight decline from the first quarter.

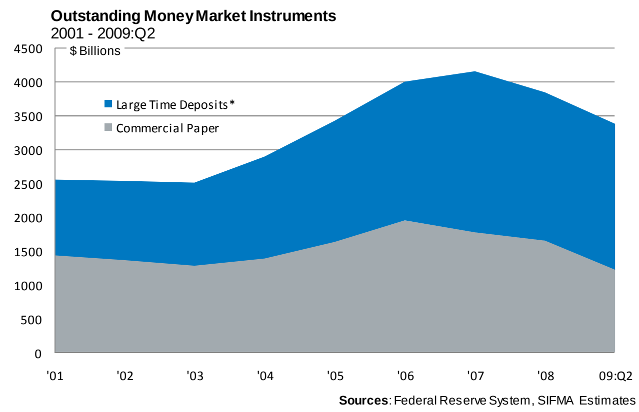
Long-term issuance by the Farm Credit System was $22.6 billion in the second quarter, 11 percent below that in the first quarter 2009 and 28 percent below that in the same year-earlier period. The Tennessee Valley Authority had no issuance of long-term debt for the fourth consecutive quarter.

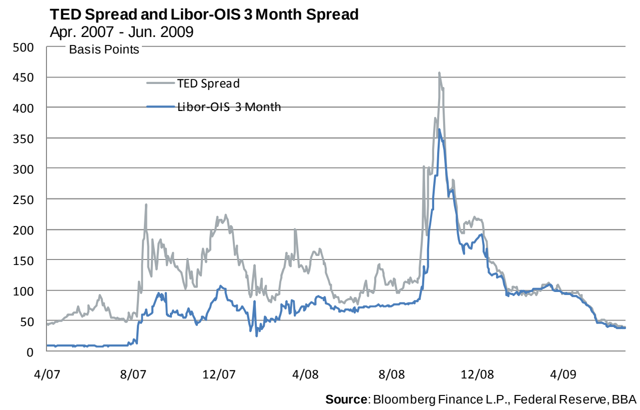
SIFMA's recent Government Forecast[3] projects federal agency debt issuance will increase to $333 billion in 3Q'09 compared to the $120 billion issued in 2Q'09.

[3] SIFMA Government Forecast can be found at: http://www.sifma.org/research/pdf/GovForecast0709.pdf

Funding and Money Market Instruments







Repo Average Daily Amount Outstanding Down 1.8 Percent in the Second Quarter

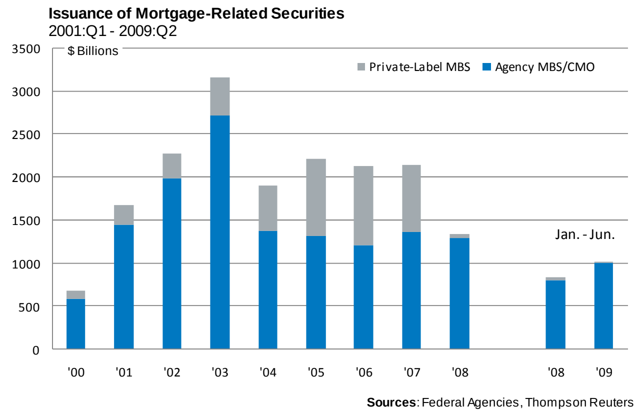
The average daily volume of total outstanding repurchase (repo) and reverse repo agreement contracts totaled $4.6 trillion in the second quarter of 2009, a 1.8 percent decrease from the average in the prior quarter. Daily average outstanding repo totaled to $2.0 trillion, a 2.7 percent decrease from the prior quarter, while reverse repo agreements averaged $2.7 trillion, unchanged from the prior quarter's average. These data represent 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.

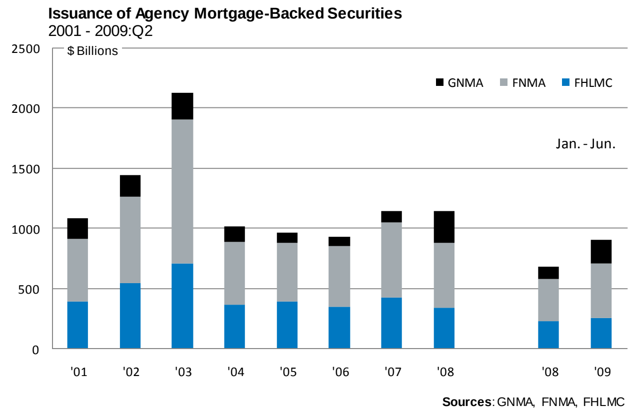
CP Outstanding Continued to Decline in the First Quarter

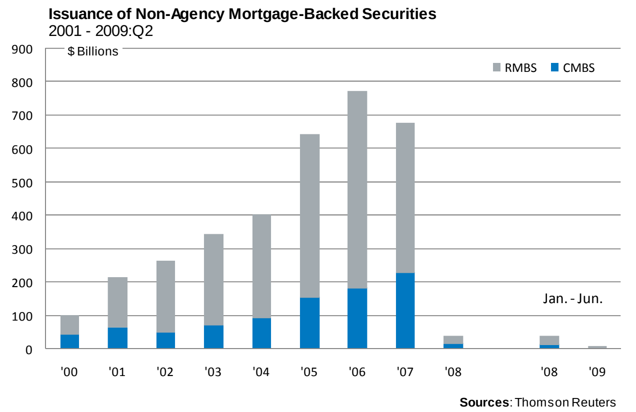
The outstanding volume of total money market instruments, including commercial paper (CP) and large time deposits, totaled $3.4 trillion at the end of the second quarter of 2009, a 6.4 percent decrease from the $3.6 trillion outstanding at the end of the first quarter 2009.

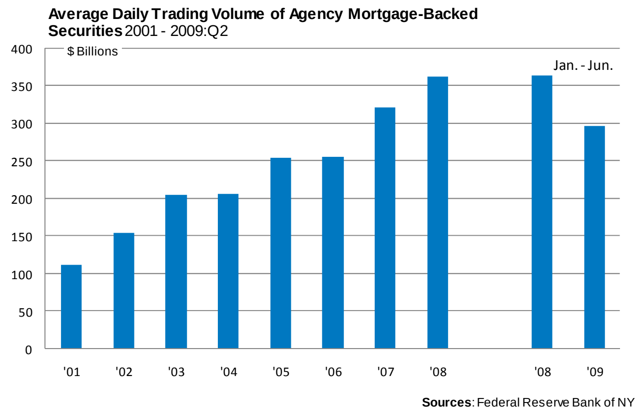
CP outstanding totaled $1.3 trillion at the end of second quarter, down 10.2 percent from the the end of the first quarter. Financial CP outstanding decreased 10.0 percent to $575.6 billion at the end of the second quarter, from $639.0 billion totaled at the end of first quarter. Non-financial CP outstanding reached $130.5 billion, a 12.8 percent decline from the $149.7 billion at the end of the first quarter 2009.

Mortgage-Related Securities









Mortgage-Related Market

Issuance of mortgage-related securities, including agency and non-agency pass-throughs and collateralized mortgage obligations (CMO), totaled $648.1 billion, an increase of 77.2 and 45.2 percent from the $365.8 billion and $446.2 billion issued in the prior quarter and second quarter of 2008 respectively.

Agency and Non-Agency Issuance

As in prior recent quarters, issuance was largely driven by the agency market. The two GSEs (Fannie Mae and Freddie Mac) were allowed to expand their portfolios to $900 billion, and issuance of MBS increased compared to 2008, although on par with levels seen in 2006 and 2007. Fannie Mae issuance in particular jumped in May and June due to the securitization of $61.4 and $33.2 billion, respectively, of seasoned loans held in their portfolio. However, Ginnie Mae issuance has increased substantially: issuance in the second quarter 2009 reached $117.0 billion, up 72.3 percent from the second quarter of 2008 and, more notably, up 20.7% from 2007 full-year issuance. The growth is due to the sharp rise in FHA originations, particularly in the refinancing subcategory of prior FHA loans as well as existing non-FHA conventional mortgages refinanced into FHA loans. Ginnie Mae MBS outstanding is on track to reach one trillion by 2010.

In the non-agency, or private-label, sector, $6.6 billion residential mortgage-backed securities (RMBS) were issued according to Thomson Reuters, six times the revised first quarter 2009 issuance of $1.1 billion. Of the second quarter total, 38.4% were in the form of re-securitizations (or re-REMICs), with the remainder of issuance primarily stemming from a passthrough securitization of seasoned loans benefiting from a GSE wrap. The private label market remains dormant due to reduced lending, lack of investor demand, low liquidity, and continued deterioration of the sector. The pace of decline in housing prices has moderated; notably, S&P’s 20-City Case-Shiller HPI increased month-to-month in May for the first time since 2006.

While the Term Asset-Backed Securities Lending Facility (TALF) officially expanded into new commercial mortgage-backed securities (CMBS) in June (followed by legacy CMBS shortly after at the end of second quarter), no bids were submitted in the first CMBS auction held on June 16. The private-label CMBS primary market remains closed, with only $262.5 million of re-securitizations issued in the second quarter of 2009. Reduced consumer spending, rising vacancies, refinancing uncertainty, and the bankruptcy and/or consolidation of both small and large business companies will continue to unfavorably impact both the CMBS and larger commercial real estate (CRE) market; according to the Federal Reserve Beige Book, the commercial real estate outlook is "mixed," even as the sector remains "weak" and "slow" in all districts.

Government Assistance Strong; Effect Still Uncertain

The Federal Reserve began purchasing agency MBS and debt and longer-dated Treasuries in December 2008, committing to buy up to $1.25 trillion in agency MBS, $200 billion in agency debt and $300 billion in Treasuries before the end of 2009. In the second quarter 2009, the Federal Reserve purchased net $328.6 billion of agency MBS, predominantly 30-year fixed rate securities within the 4.0 to 5.5 coupon range; $44.1 billion in agency debt; and $183.2 billion in Treasury securities.

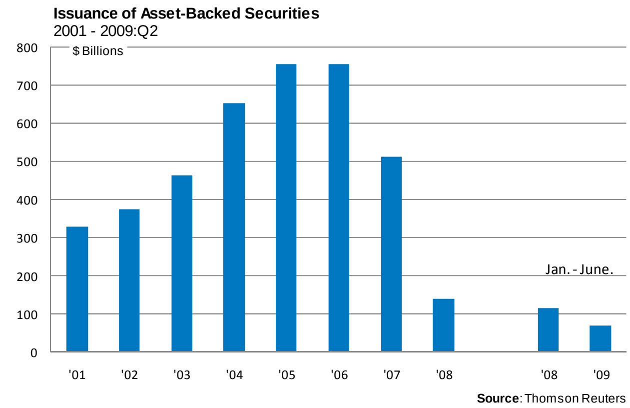
The Federal Reserve purchases of agency MBS have helped to lower primary mortgage rates. Low mortgage rates in the second quarter encouraged the refinancing of existing loans. According to the US Treasury, from the launch of the Making Home Affordable Plan in February 2009 through mid-May, over one million Americans took advantage of these low rates to refinance and continue to do so, albeit at lower volumes due to the rise in mortgage rates by the end of May.

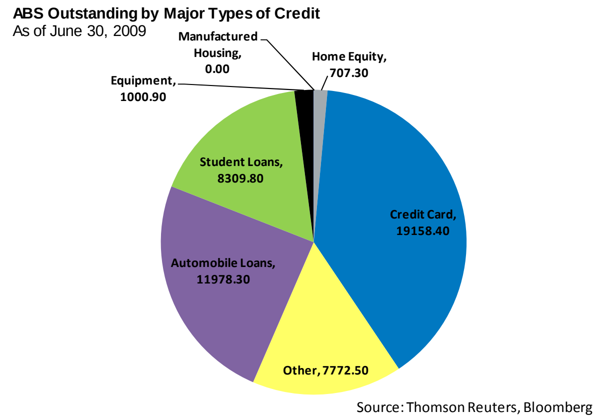
The Obama Administration's Making Home Affordable Plan, introduced in late first quarter 2009, allows mortgage borrowers with a loan owned by a GSE to refinance, including underwater borrowers traditionally locked out of the refinancing market (with a LTV ratio up to 105 percent). The plan was modified at the end of second quarter 2009 to include underwater borrowers with an LTV of up to 125 percent and has recently been extended in a substantially similar form to FHA borrowers.

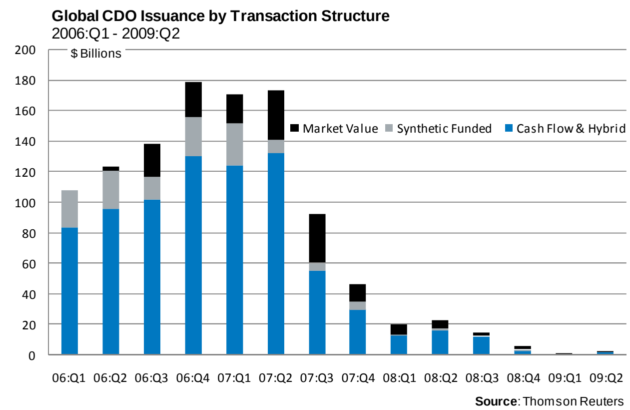
Home sales, of both new and existing homes, rose in second quarter 2009 from the prior quarter, aided in part by homebuyer tax credits on the state and federal levels, low mortgage rates, and some demand, particularly in lower-cost housing.

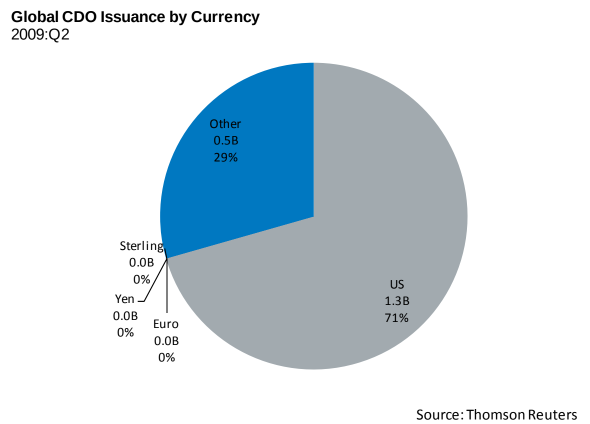
However, legislative changes continue to impact the market: H.R. 1728, the Mortgage Reform and Anti-Predatory Lending Act, passed the House of Representatives on May 7; this bill includes a number of mortgage lending-related provisions as well as risk retention requirements for securitization. It is unclear if and when the Senate will take action. Furthermore, after the second quarter, the Obama administration released a number of pieces of proposed legislation, including some that will directly impact lending and securitization markets. While loan modifications are still ongoing, the high re-default rate and relatively low number of modifications has been seen as unsatisfactory, suggesting the return of certain legislative provisions such as bankruptcy cram down for primary-residence mortgage debt.

Asset-Backed Securities and CDO Market









Asset-Backed Market

Asset-backed securities issuance in the second quarter of 2009 reached $48.6 billion, an increase of 199.8 percent from the first quarter of 2009 and a decrease of 22.9 percent from the second quarter 2008. With the exception of housing-linked ABS sectors (e.g., home equity and manufactured housing), asset-backed securities issuance has returned to the levels seen prior to 2006. The Term Asset-Backed Securities Lending Facility (TALF) played a significant role in the return of issuance; according to Bloomberg, $34.2 billion of TALF-eligible securities were issued in the second quarter of 2009, comprising 70.4 percent of all ABS issuance in second quarter 2009. However, $14.4 billion of non-TALF-eligible securities were also issued and spreads in all ABS categories have significantly tightened.

Three TALF auctions for financing were held during the second quarter 2009 for a total of $23.8 billion, resulting in 69.6 percent of all TALF-eligible issuance being financed by TALF and the remainder cash-financed. Bids for TALF financing through the second quarter expanded from the auto and credit card class to include equipment, small business, student loan, insurance premiums, and servicing advances. However, credit card and auto securitization transactions continue to dominate TALF auctions, accounting for 79.7 percent of all TALF financing in the second quarter 2009.

However, credit quality continues to deteriorate in all asset classes. Unemployment reached 9.5 percent in June 2009, and while consumers continue to pay down both revolving and non-revolving consumer debt at a rapid clip, delinquencies and charge-offs in all ABS categories continued to rise Small business in particular has been impacted with the shutdown or potential bankruptcy of small business-oriented credit card issuers and banks. In secondary markets, a number of credit card ABS issuers stepped in to support their transactions with added credit support.

Auto Loan and Credit Card ABS Lead Issuance Totals

Issuance continues to remain strong in the auto ($12.0 billion) and credit card ($19.2 billion) sectors. The expansion of TALF to other ABS asset classes aided issuance in other sectors: student loans ($7.6 billion), equipment ($2.6 billion), and "other" issuance ($6.4 billion), which contains certain TALF-eligible ABS such as insurance premiums and mortgage servicing rights.

The two housing-related sectors, home equity and manufactured housing, continue to remain weak. Home equity issuance totaled $707.4 million in the second quarter, a moderate decline of 9.6 percent from the prior quarter. Manufactured housing remained nonexistent with zero issuance and will continue remain so as a glut of housing supply from foreclosures continue to saturate the housing market.

Global CDOs

Global collateralized debt obligation (CDO) issuance rose modestly in second quarter 2009, with $1.8 billion issued, an increase of 142.9 percent from the $757.2 million issued in first quarter 2009, but 91.6 percent below the $22.0 billion issued in second quarter 2008.

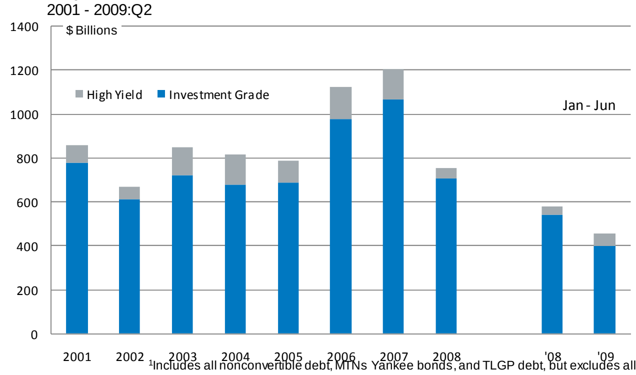
Cash flow and hybrid issuance totaled $1.3 billion in second quarter 2009, a substantial jump of 559.6 percent from the prior quarter, while market issuance rose modestly to $540.9 million, up 17.1 percent from the prior quarter. Funded synthetic issuance disappeared, with no issuance in second quarter 2009 compared to $98.5 million in the first quarter. The future of synthetic issuance, both funded and unfunded, is expected to remain uncertain as the credit default swap (CDS) market transitions to new trading and settlement conventions in both the US and Europe. Legislative and regulatory proposals in both regions additionally contribute uncertainty to this particular market segment, as measures to reduce speculation in this market gain legislative traction.

Based on CDO purpose segmentation, issuance for arbitrage purposes accounted for all CDO issuance in the second quarter 2009.

High yield loans and investment grade bonds were again the only two collateral classes comprising CDO issuance, with 1.3 billion and 540.9 million issued, respectively, in second quarter 2009. By denomination, issuance has been largely denominated in USD or "Other." As in the prior quarter, there were no new EUR- and GBP-denominated issuances.

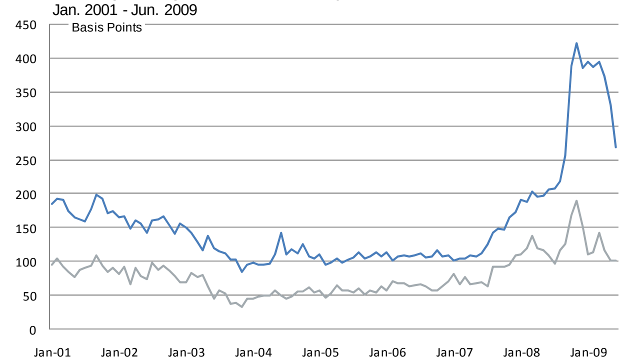
Corporate Bond Market

Corporate Bond Issuance[1]
2001 - 2009:Q2



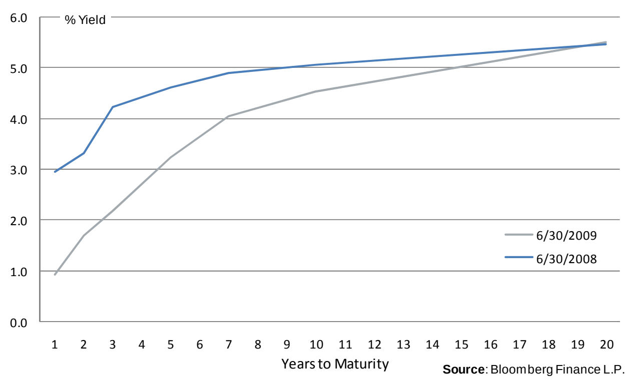
[1]Includes all nonconvertible debt, MTNs Yankee bonds, and TLGP debt, but excludes all issues with maturities of one year or less, CDs, and federal agency debt
Source: Thomson Reuters

U.S. Corporate Spreads to U.S. Treasury - 10 Year
Jan. 2001 - Jun. 2009



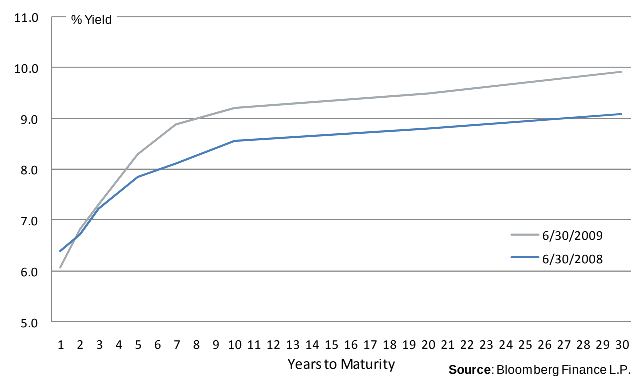
Source: Bloomberg Finance L.P.

U.S. Corporate: AAA Industrial - Yield Curves



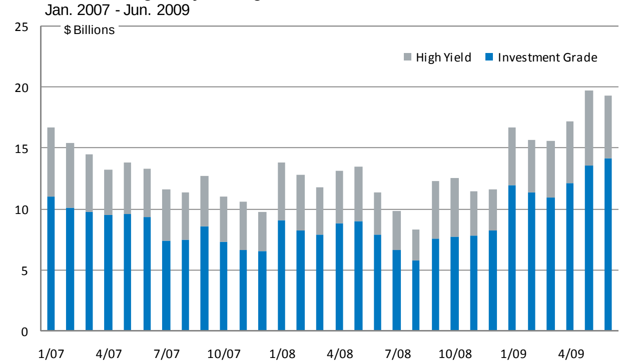
Source: Bloomberg Finance L.P.

U.S. Corporate: BB Industrial - Yield Curves



Source: Bloomberg Finance L.P.

TRACE Average Daily Trading Volume
Jan. 2007 - Jun. 2009



Source: FINRA

Corporate Bond Issuance Remains High Despite Decline from First Quarter

Total corporate bond issuance rose to $237.5 billion in the second quarter of 2009, a 9.4 percent increase from $217.1 billion in the previous quarter. In total, the first half of 2009 saw corporate bond issuance fall 17.0 percent to $454.6 billion from the same year-earlier period. In addition, $172.4 billion was issued under FDIC's Temporary Liquidity Guarantee Program (TLGP).

U.S. high-yield debt issuance was $48.3 billion in the second quarter of 2009, up nearly four and a half times from $10.8 billion in the first quarter, while investment grade issuance, including TLGP debt, totaled 189.2 billion, a decrease of 8.5 percent from the prior quarter.

Credit Quality Remains Weak; Speculative-Grade Widening

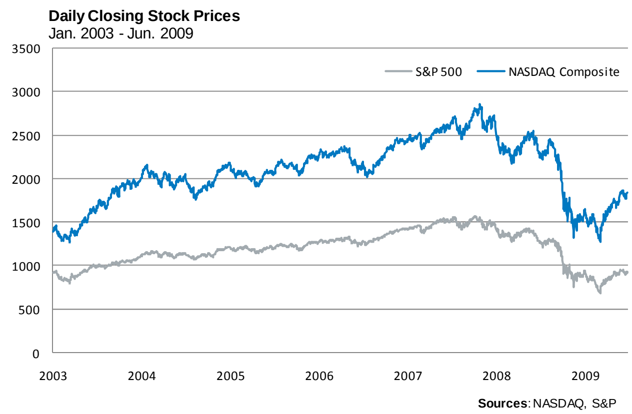
Corporate credit quality has been declining in aggregate over the past year and is expected to continue to remain poor. With speculative-grade defaults accelerating, the number of credit downgrades rising, and general uncertainty about the future of the economy persisting, S&P expects spreads to remain at their current elevated levels for some time. S&P reported that investment grade bond spreads contracted to 305 basis points (bps) at the end of the second quarter of 2009 from 493 bps at the end of the first quarter, yet remained above the five-year moving average of 219 bps. Speculative-grade spreads also contracted considerably in the second quarter, falling from 1428 bps at the beginning of the quarter to 976 bps by the end of the second quarter, well above the same year-earlier period spread of 250 bps and the five-year moving average of 618 bps. As of June 30, 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.

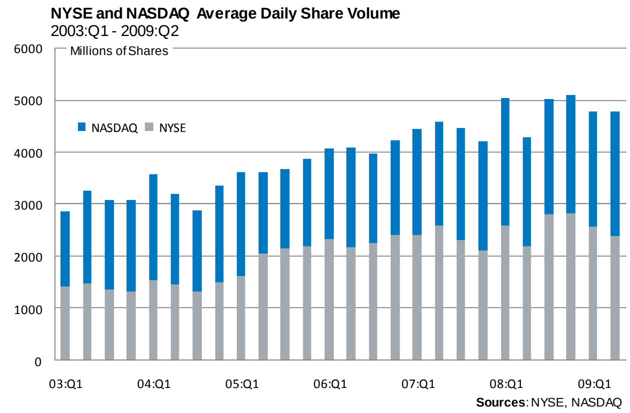
According to S&P's Global Fixed Income Research, the large number of downgrades, especially in the stressed sectors, is likely to stay elevated through most of 2009. The U.S. continued to experience the highest number of defaults compared to the rest of the world, contributing 128 so far this year out of 178 globally. The increase in defaults reflects a deep decline in economic fundamentals and earnings prospects of companies. Other contributing factors to the expected rise in defaults are the tight credit conditions, which have 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 that were 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 14.3 percent by the end of first quarter 2010.

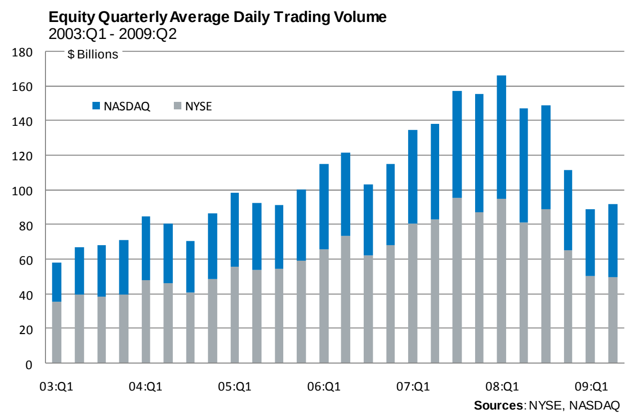
Corporate spreads remained at elevated levels in the second quarter but have declined throughout the first half of 2009. As of June 30, the JP Morgan U.S. Liquid Index spread, or JULI, was 258 bps, compared to 492 bps in the immediately preceding quarter and 169 bps in the same year-earlier period. The Merrill Lynch high-yield index spread tightened 648 bps to 1,055 bps at the end of June from 1,703 bps in March, still well above the 735 bps seen at the end of the second quarter 2008.

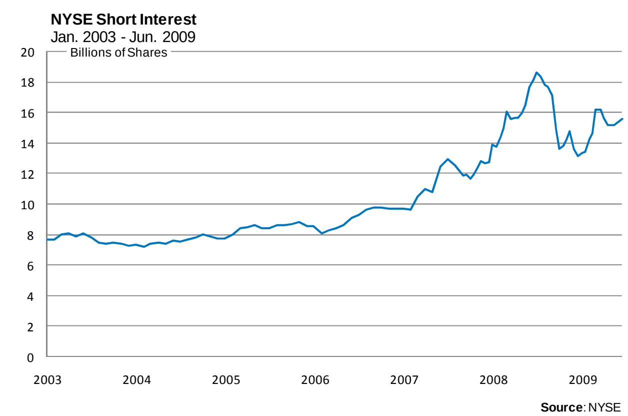
Dollar Trading Volume

According to FINRA'S TRACE system, estimated investment-grade bond average daily dollar trading volume was $14.1 billion in the second quarter, up 29.4 percent from the $10.9 billion average traded in the first quarter and 78.7 percent above the second quarter 2008 average. The second quarter high-yield bond average daily dollar trading volume of $5.2 billion marked an 13.0 percent increase from the previous quarter's $4.6 billion and was 49.8 percent higher than the average in the same year-earlier period.









The equity markets rose in the second quarter: the NASDAQ increased by 20.6 percent; the S&P 500 increased by 15.2 percent; and the Dow Jones Industrial Average (DJIA) increased by 7.7 percent.

Share Trading Volume Trading

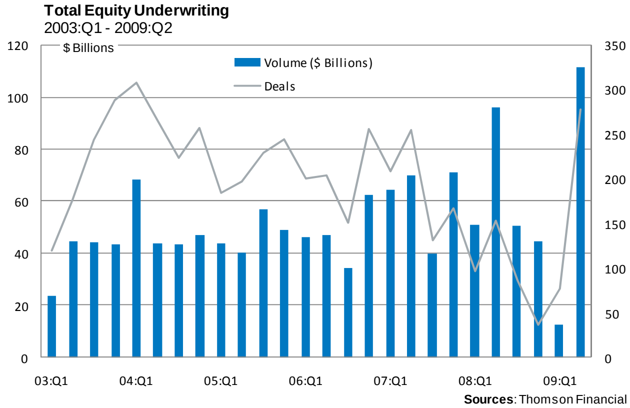
The New York Stock Exchange's (NYSE) second quarter daily average share trading volume decreased to 2.4 billion from last quarter's 2.6 billion shares, but was 8.7 percent above that in the second quarter of last year. The NYSE's average daily dollar trading volume fell slightly to $50.0 billion from previous quarter's $50.3.

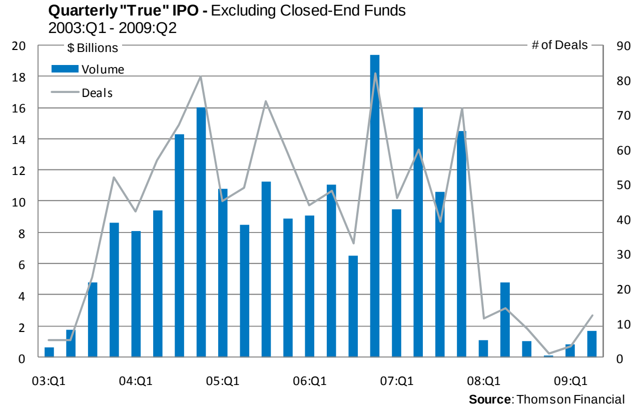
The NASDAQ's daily average share trading volume rose 7.9 percent to 2.4 billion shares from last quarter's average, but grew X percent compared to 2Q'08. NASDAQ's average daily dollar trading volume increased to $42.2 billion from previous quarter's $38.9 billion.

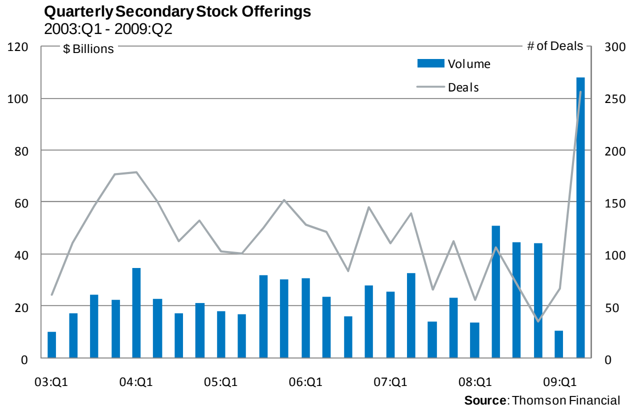
AMEX/ACRA's daily average share trading volume decreased by 11.9 percent from the previous quarter's daily average of 603.1 million shares to 531.0 million shares, but year-over-year was an increase of 72.3 percent.

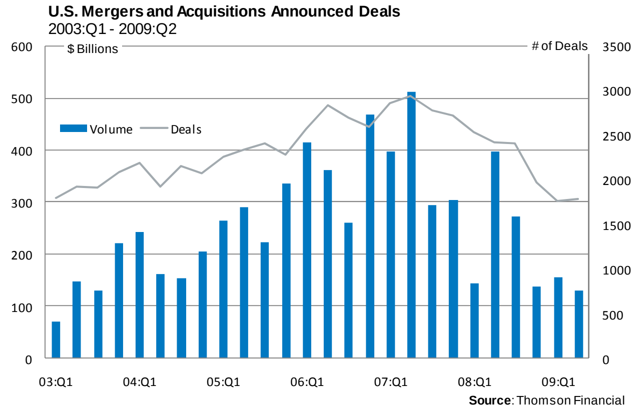
Short Interest

NYSE short interest was 15.6 billion shares at the end of the second quarter, a decrease of 3.6 percent from the previous quarter-end and was 16.2 percent below the record high 18.6 billion shares set on July 15, 2008.









Equity Underwriting

Equity underwriting increased substantially this quarter from the prior quarter, a 777.8 percent increase to $111.6 billion from 12.7 billion.

Second Quarter "True IPOs" Double

U.S. initial public offerings (IPOs) nearly doubled in the second quarter to $2.3 billion from $1.2 billion in the first quarter. "True" IPOs (which exclude closed-end fund IPOs) more than doubled to $1.7 billion, up from $0.8 billion in the first quarter of 2009.

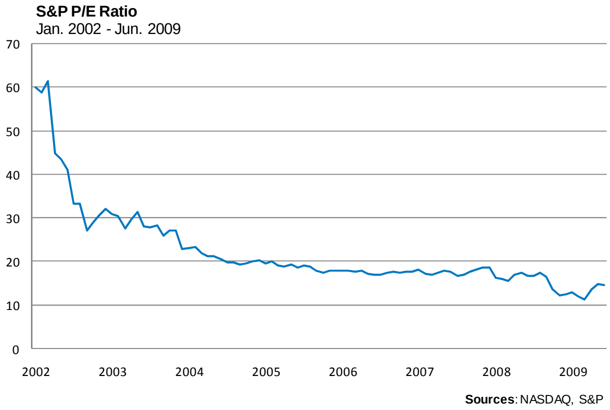
Secondary Offerings At All Time High

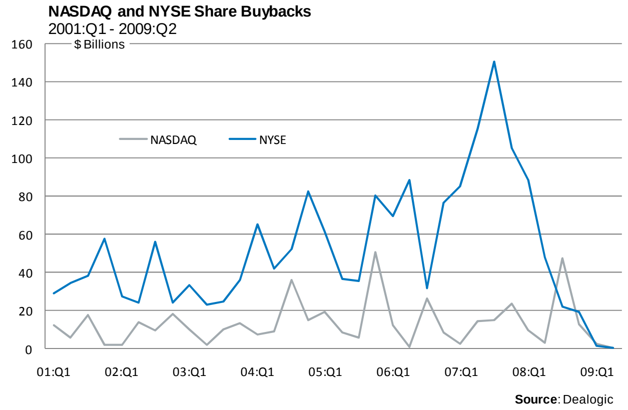
Second quarter secondary market issuance totaled at an all time high $107.9 billion, a ten fold increase from the previous quarter of $10.8 billion and nearly twice the amount of the previous record, set in 2008.

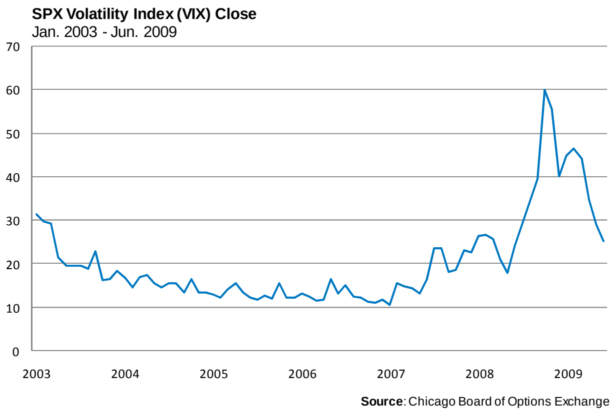
U.S. M&A Slows

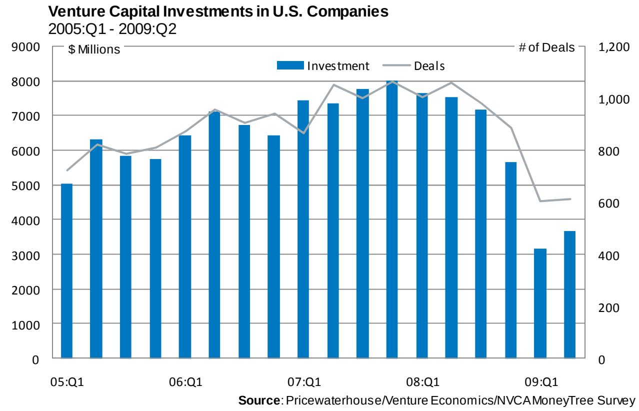
Announced U.S. mergers and acquisition (M&A) deal volume decreased in the second quarter to $130.0 billion, 17.4 percent below the first quarter level of $157.4 billion while the number of deals increased slightly to 1,785.

The dollar and deal volume of completed M&A fell in the second quarter compared the first quarter, down 74 percent in value to $59.2 billion and 1,354 deals.









P/E Ratio Steady

The P/E ratio of the S&P 500 averaged 14.68 in the second quarter, compared to the preceding quarter's average of 14.74.

Share Buy Back Volume Declined

Corporate share repurchases declined for the seventh consecutive quarter. There was no buy back volume on the NYSE after volume of $1.34 billion in 1Q'09. Buy backs on NASDAQ totaled only $72.42 million compared to 1.3 billion in the first quarter.

CBOE VIX edges Down

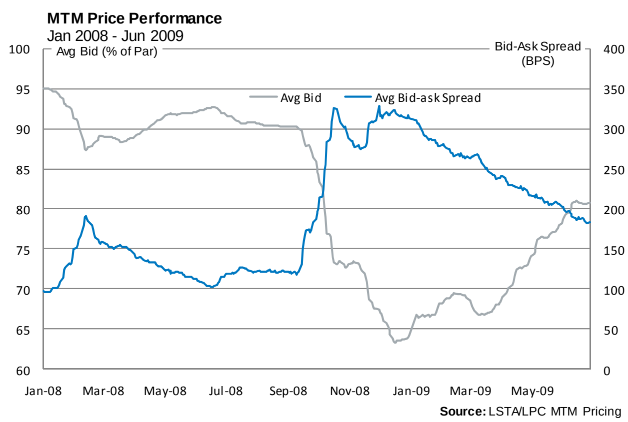
The Chicago Board Options Exchange Index (VIX) closed at 25.0 at the end of the second quarter, a 13.3 percent decrease from the previous record high quarter end of 28.9 set in the first quarter.

Venture Capital/Private Equity Rebounds

Venture capital increased by $483 million from the prior quarter, for a total investment value $3.7 billion on 612 deals. The two strongest sectors in the second quarter were software and biotechnology, with investment totals of $664.1 million (135 deals) and $888 million (85 deals), respectively. Private equity investments rose in the second quarter, ending a run of five consecutive quarters of decline.

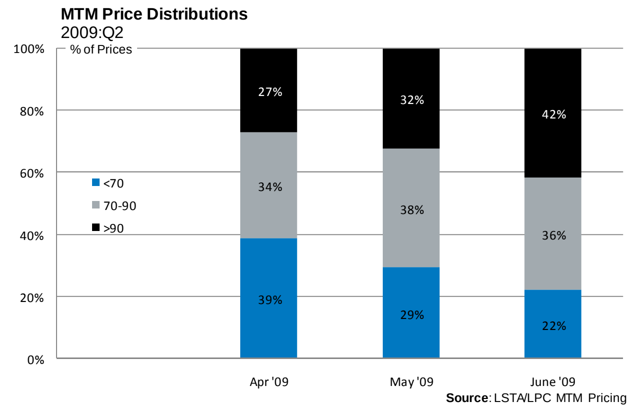
LSTA Secondary Loan Market Review: June 2009[4]

Mark-to-Market (MTM) prices climbed by 300 bps or 3.9 percent during June, boosting 2Q'09's MTM gains to 12.7 points or 18.6 percent. As bids strengthened and trading increased, bid-ask spreads tightened. Over the past three months spreads have contracted by 25 percent to 180 bps. That said, June's performance was a tale of two halves. The average bid on the LSTA MTM dataset reached an 8-month high of 80.9 by mid-month but profit taking and negative macroeconomic sentiments began to slow the market's rally through month-end. Year-to-date, MTM prices have rallied 16.8 pts, or 26 percent, as bid-ask spreads have tightened by more than 135 bps or 43 percent.

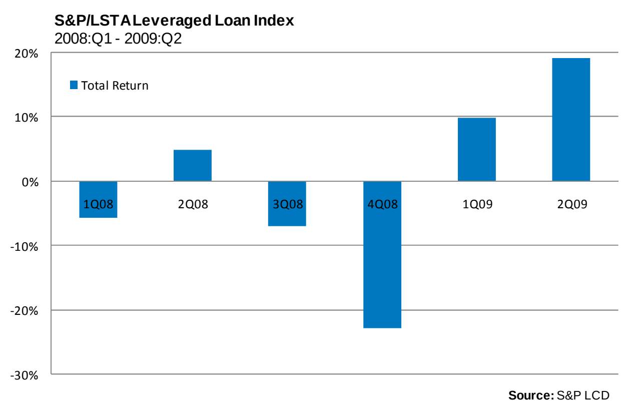


After falling to an all-time low of 8 percent at year-end, the share of loans priced above 90 edged up to 14 percent in 1Q09 and then exploded to 42 percent in June. On the other end of the price spectrum, the percentage of loans priced below 70 has fallen from nearly 50 percent of the market in 1Q'09 to just 22 percent by month-end June.

With higher prices comes a stronger return, and strong they were this quarter. Following its then record high 9.8 percent 1Q'09 return, the S&P/LSTA Leveraged Loan Index continued to surge forward by registering a 19.18 percent return during 2Q'09.



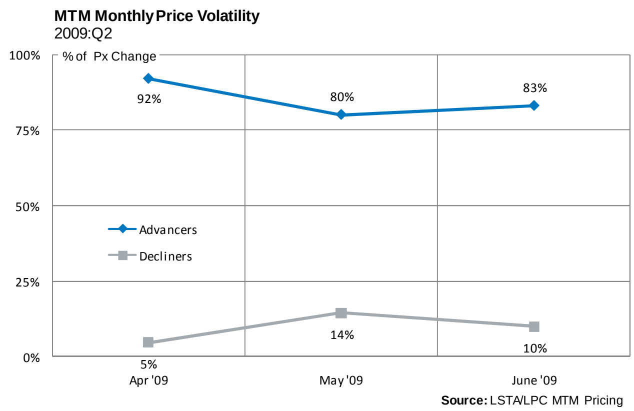
Though the Great Loan Rally of '09 has lost some momentum in recent weeks, the market managed to deliver another solid gain in June, with the S&P/LSTA Leveraged Loan Index up 4.38 percent. The index has now posted positive returns in each of the past six months, and has delivered a staggering 32.2 percent YTD return which has completely erased last year's record loss of 29.1 percent.

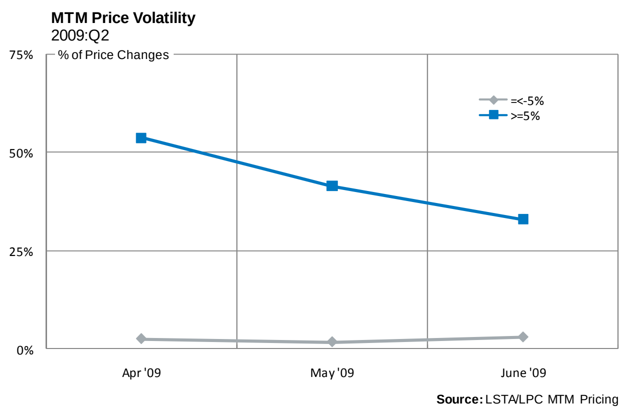


Market breadth was positive for the fifth consecutive month; 83 percent of loans recorded MTM gains during June while only 10 percent reported losses. Even as the market gave back some of its gains by June's end, 33 percent of loans still reported MTM gains of 5 percent or better with only 3 percent recording losses of 5 percent or worse .

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

While most of 1Q'09's gains were attributed to a market that bifurcated on credit where lenders favored loans with higher credit quality and better structures, 2Q'09's historic rally was widespread and has since pushed the returns on lower rated credits and 2nd liens past that of their less riskier counterparts. Exemplifying the depth of the second quarter rally, an average of 85 percent of prices advanced each month while only 10 percent declined. Last quarter those figures were 65 percent and 31 percent, respectively.





SIFMA RESEARCH QUARTERLY

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

SUMMER INTERNS

David Beard
Elizabeth Hom
Stephanie Yu

SURVEYS

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

SIFMA® www.sifma.org

Securities Industry and Financial Markets Association