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RESEARCH QUARTERLY

First Quarter 2013

RESEARCH REPORT

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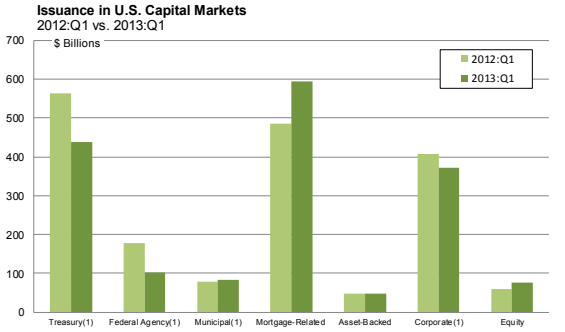
CAPITAL MARKETS OVERVIEW



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

Issuance Highlights - Year-Over-Year

$ Billions	2013:Q1	2012:Q1	Y-o-Y % Change*	2013 YTD
Treasury (1)	439.0	562.9	-22.0%	439.0
Federal Agency (1)	102.7	177.7	-42.2%	677.4
Municipal (1)	82.9	79.1	4.8%	82.9
Mortgage-Related	595.2	485.9	22.5%	595.2
Asset-Backed	48.0	48.2	-0.4%	48.0
Global CDO	23.5	9.4	150.3%	23.5
Corporate (1)	371.7	408.3	-9.0%	371.7
Equity	77.1	60.0	28.4%	77.1

* Percent change between 2013:Q1 and 2012:Q1

Quarter-Over-Quarter

$ Billions	2013:Q1	2012:Q4	Q-o-Q % Change*
Treasury (1)	439.0	638.3	-31.2%
Federal Agency (1)	102.7	139.6	-26.4%
Municipal (1)	82.9	97.5	-15.0%
Mortgage-Related	595.2	565.2	5.3%
Asset-Backed	48.0	44.8	7.1%
Global CDO	23.5	24.1	-2.3%
Corporate (1)	371.7	375.7	-1.1%
Equity	77.1	64.9	18.8%

* Percent change between 2013:Q1 and 2012:Q4
(1) Includes long-term issuance only

Total Issuance Falls in First Quarter 2013

Long-term securities issuance totaled $1.72 trillion in the first quarter of 2013, a 10.9 percent and 5.8 percent decline, respectively, quarter-over-quarter (q-o-q) and year-over-year (y-o-y). Declines in U.S. Treasuries, the federal agencies, municipal debt, and corporate were only partly offset by gains in mortgage-related and asset-backed asset classes.

During the March FOMC meeting, the Fed indicated that economic activity returned to moderate economic growth following a pause late in 2012. The Fed reiterated that the exceptionally low range for the target Fed Funds rate of 0-0.25 percent will remain appropriate at least as long as the unemployment rate remains above 6.5 percent, medium term is projected to be no more than a half percentage point above the long-run goal of 2 percent and longer-term inflation expectations continue to be well anchored.

Total gross issuance of Treasury bills and coupons, including cash management bills, was $1.97 trillion in 1Q'13, a 6.2 percent decrease from $2.10 trillion issued in 4Q'12 and an 1.3 percent decrease from 1Q'12's issuance of $1.99 trillion. Total fourth quarter net issuance of U.S. Treasury securities, including CMBs, increased to $349.9 billion, up 18.4 percent from the previous quarter's $295.4 billion but 12.8 percent below the $401.2 billion issued in 1Q'12.

Federal agency long-term debt (LTD) issuance was $102.7 billion in the first quarter compared to $136.8 billion in the 4Q'12, and fell 41.2 percent y-o-y.

Long-term municipal issuance volume, including taxable and tax-exempt issuance, totaled $82.9 billion in the first quarter of 2013, a decline of 15.0 percent from the prior quarter ($97.5 billion) but an increase of 4.8 percent year-over-year. Volumes were slightly below the 10-year average of $83.0 billion.

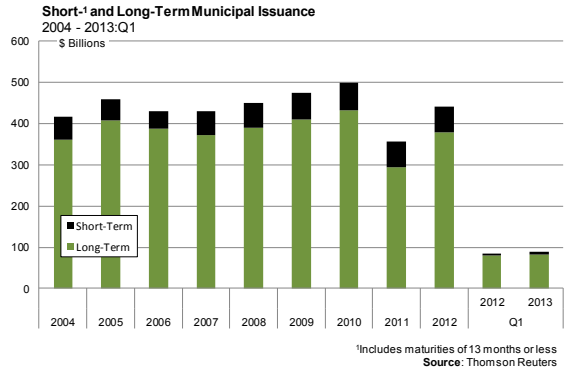
Issuance of mortgage-related securities, including agency and non-agency passthroughs and collateralized mortgage obligations (CMOs), totaled $576.0 billion in the first quarter, a 2.0 percent and 18.6 percent increase, respectively, from 4Q'12 ($564.5 billion) and 1Q'12 ($485.4 billion).

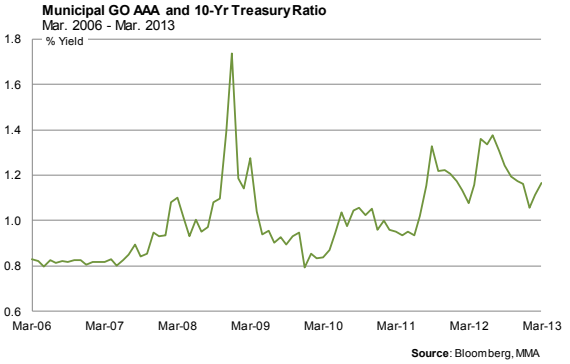
Asset-backed securities (ABS) issuance totaled $48.2 billion in the first quarter, an increase of 7.1 percent from 4Q'12 ($44.8 billion) but unchanged from 1Q'12.

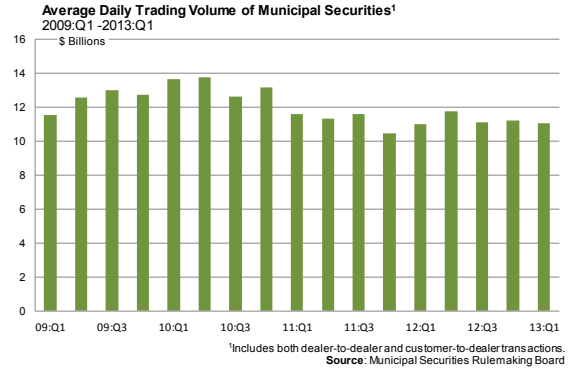
Corporate bond issuance totaled $365.2 billion in 1Q'13, almost unchanged from the $364.6 billion issued last quarter but 9.8 percent below the $404.8 billion issued in 1Q'12. The issuance of high yield bonds was $91.9 billion in 1Q'13, the third largest quarterly issuance on record.

Equity underwriting reached $77.1 billion in the first quarter, 21.1 percent above the $63.6 billion in 4Q'12 and 28.9 percent above the $59.8 billion in 1Q'12. Secondary market issuance increased to $53.5 billion on 227 deals from $41.8 billion on 179 deals in 4Q'12 (an increase of 27.8 percent and 26.8 percent, respectively). "True" initial public offerings decreased in 1Q'13 to $8.5 billion on 41 deals, a 3.9 percent decrease from $8.8 billion and a 10.9 percent decrease from 46 deals in the previous quarter.

MUNICIPAL BOND MARKET







Long-term municipal issuance volume, including taxable and tax-exempt issuance, totaled $82.9 billion in the first quarter of 2013, a decline of 15.0 percent from the prior quarter ($97.5 billion) but an increase of 4.8 percent y-o-y. Volumes were slightly below the 10-year average of $83.0 billion.

By use of proceeds, general purpose led issuance totals in 1Q'13 ($18.7 billion), followed by primary & secondary education ($18.2 billion), and higher education ($7.9 billion).

Refunding volumes stayed elevated in the first quarter but declined slightly as percentage of issuance (62.8 percent) compared to 4Q'12 (66.8 percent), but was still above 1Q'13 (57.2 percent).[1] With refundings still driving most municipal issuance volume, municipal supply, net of redemptions, continues to remain overall negative in the first quarter.

Yields and Total Return; Trading Activity Declines Slightly

Ratios of 10-year tax-exempt AAA GOs and similar-maturity Treasuries moved higher in the first quarter, ending at 106 percent. The municipal market returned 0.8 percent on a total return basis in 1Q'13, compared to 0.6 percent in 4Q'12 and 3.4 percent in 1Q'12.

Tax-exempt money market funds reported a decline in assets in 1Q'13, reporting $274.5 billion in assets under management, a drop of $10.3 billion, or 3.6 percent of assets, from 4Q'12.

Trading activity declined q-o-q to $11.05 billion in 1Q'13, a 1.5 percent decline from 4Q'12 ($11.21 billion) but was an increase of 0.6 percent increase from 1Q'12 ($10.98 billion). By number of trades, however, trading activity picked up by 7.6 percent and 3.0 percent q-o-q and y-o-y., respectively.

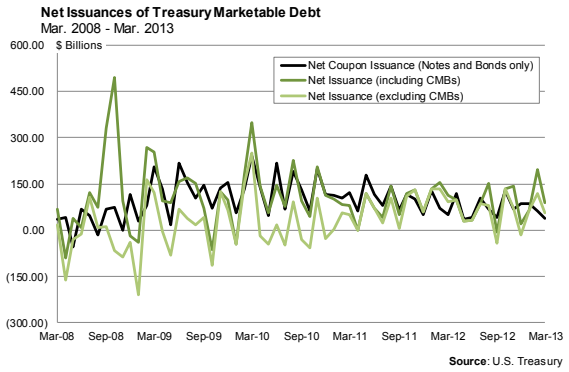
VRDO Issuance Remains Scarce, but Floating Rate Notes Pick Up

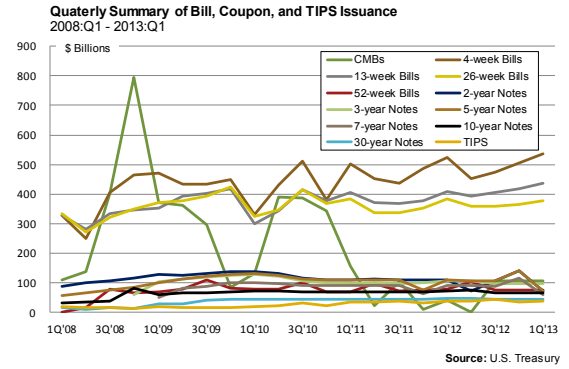
Issuance of variable-rate demand obligations (VRDOs), long-term municipal bonds with floating interest rates that reset periodically and a put feature, declined in the first quarter. According to Thomson Reuters, $1.1 billion were issued in 1Q'13, a decline of 72.7 percent and 37.1 percent, respectively, q-o-q and y-o-y.

In the first quarter of 2013, $3.4 billion of floating rate notes (FRNs), were issued, representing 4.2 percent of all issuance, a new high. FRNs, which have historically been a rare phenonmenon in the municipal market, have increasingly become popular with the demise of the auction rate market and the continued gradual decline in the VRDO market, with volumes picking up beginning in late 2008. Despite concerns over LIBOR, the use of the index remains pervasive; since 2009, approximately three-fifths (59.8 percent) of all FRNs issued have been LIBOR-indexed, while a third (35.3 percent) have been SIFMA-indexed. The balance of FRNs have been linked to rates privately set by banks in direct purchases.

[1] Percentages represent both full refundings and the full dollar amount of deals that contain both refundings and new financing.

TREASURY MARKET





Gross Issuance of U.S. Treasury Securities Decreases

Total gross issuance of Treasury bills and coupons, including cash management bills (CMBs), was $1.97 trillion in 1Q'13, a 6.2 percent decrease from $2.10 trillion issued in 4Q'12 and an 1.3 percent decrease from 1Q'12's issuance of $1.99 trillion. Total first quarter net issuance of U.S. Treasury securities, including CMBs, increased to $349.9 billion, up 18.4 percent from the previous quarter's $295.4 billion but 12.8 percent below the $401.2 billion issued in 1Q'12. The issuance of net marketable debt, excluding CMBs, was $243.9 billion in 1Q'13, 26.3 percent below the U.S. Treasury's February 1Q'13 borrowing estimate of $331 billion.[2]

Excluding cash management bills (CMBs), total net issuance stood at $243.9 billion in 1Q'13, a 28.1 percent increase from $190.4 billion in the prior quarter but 32.5 percent below 1Q'12's issuance of $361.2 billion.

CMBs issuance stood at $106.0 billion in 1Q'13, unchanged from 4Q'12's $105 billion and the highest quarterly CMBs issuance since 1Q'11 ($155.0 billion).

Approximately $435.0 billion in Treasury coupons and Treasury Inflation-Protected Securities (TIPS) were issued in the first quarter, 33.8 percent below the $656.6 billion issued in the prior quarter and 22.8 percent below issuance of $563.7 billion y-o-y. The U.S. Treasury indicated that it remains pleased with the TIPS demand.

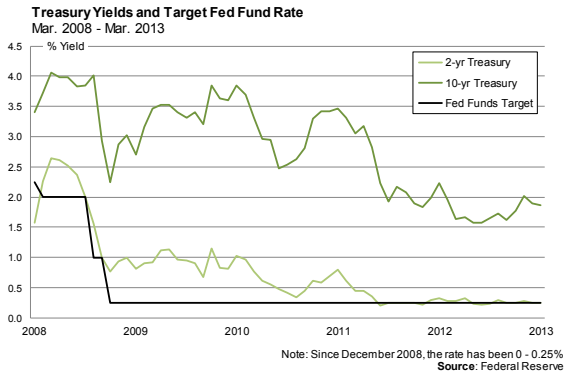
Excluding TIPS, total gross issuance of Treasury marketable coupon securities was $439.0 billion, a 30.8 percent decrease from $634.0 billion issued in 4Q'12 and 22.1 percent below the $563.2 billion issued in 1Q'12. Net coupon issuance for the first quarter of 2013 was $186.9 billion, a 33.8 percent decrease from 4Q'12s $282.4 billion and down 24.4 percent y-o-y. The decrease in issuance of those maturities was mainly due to the timing of the auctions rather than an actual decrease in Treasury borrowing.

As the U.S. Treasury has transitioned from bill to coupon financing, the percentage of nominal coupons in the Treasury's portfolio has been gradually increasing; the average maturity of the portfolio continues to lengthen and is expected to reach the upper end of the historical range by 2016. The average maturity of the portfolio is currently 64.5 months, compared to 64.4 months last quarter and well above the 3 decade average of 58.1 months.[3]

Gross issuance of bills, including CMBs, was $1.53 trillion in 1Q'13, a 4.5 percent increase from previous quarter's $1.46 trillion and a 6.9 percent increase from $1.43 trillion issued during the same year-ago period.

Treasury's most recent Quarterly Refunding Statement provided an update on the Treasury's proposed Floating Rate Note (FRN) Program, which was announced at the August 2012 Quarterly Refunding. Treasury has reviewed the comment letters that were received in response to the Advance Notice of Proposed Rulemaking (ANPR) published on December 5, 2012, and has decided to use the weekly High Rate of 13-week Treasury bill auctions as the index for Treasury FRNs. The Treasury plans to issue a final rule on floating rate notes in the coming months, with the first FRN auction estimated to occur in either 4Q 2013 or 1Q 2014. This timeframe reflects Treasury's best estimate for implementing required auction regulations and IT systems modifications. Treas-

[2] Treasury Announces Marketable Borrowing Estimates, February 4, 2013.
[3] Minutes of the Meeting of the TBAC of SIFMA, February 5, 2013.



ury will provide additional information regarding the timing of the first auction at the August refunding.

The Supplementary Financing Program (SFP) remains suspended. The reintroduction of the SFP remains impossible for the foreseeable future, as future debt limit increases remain uncertain. U.S. federal government debt reached the statutory debt limit of $16.8 trillion dollars on April 3, 2013. The U.S. Treasury noted that it is prepared to use extraordinary measures at the expiry of the debt limit suspension in May, if needed.

Trading Volume Increases

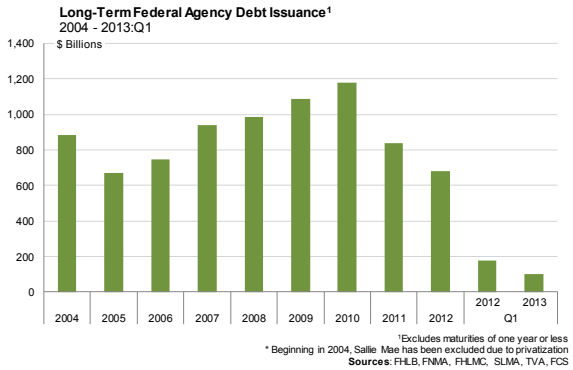
The average daily trading volume increased in the first quarter of 2013, the first increase in trading activity and the highest level since 1Q'12. Daily trading volume of Treasury securities by primary dealers averaged $531.4 billion in 1Q'13, a 4.6 percent increase from $507.9 billion in the previous quarter but 2.4 percent below the $544.3 billion traded daily in 1Q'12. The 5-year average of daily trading volume of Treasuries declined to $510.2 billion from $518.1 billion in the prior quarter.

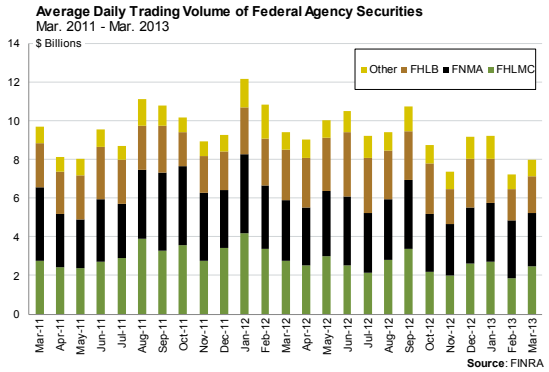
Treasury Yields Increase

In 1Q'13, Treasury yields increased across medium- and long-term maturities while decreasing for short-term maturities. Two-year rates decreased slightly to 0.24 percent at the end of March from 0.25 percent in December 2012, 5-year yields increased to 0.77 percent in March from 0.72 percent, 10-year yields rose from 1.78 percent in December to 1.86 percent in 1Q'13, and the 30-year yields increased in first quarter to 3.11 percent from 2.95 percent. SIFMA's Quarterly Issuance and Rates Forecast Survey[4] respondents forecast benchmark yields to decrease across all maturities in the second quarter of 2012 and rebound in the third quarter. Two-year Treasury yields are expected to decrease to 0.21 percent by June 2013 before rebounding to 0.25 percent in September 2013, five-year yields are projected to decline to 0.70 percent in 2Q'13 before rebounding to 0.80 percent in 3Q'13, ten-year rates are forecasted to drop to 1.75 percent in the end of June 2013 before climbing to 1.95 percent at the end of September, and 30-year yields are expected to finish 2Q'13 at 2.95 percent before climbing to 3.10 percent in 3Q'13.

[4] 2Q'13 SIFMA Quarterly Issuance and Rates Forecast survey can be found here.

FEDERAL AGENCY DEBT MARKET





Federal agency long-term debt (LTD) issuance was $102.7billion in the first quarter compared to $136.8 billion in the 4Q'12, and fell 41.2 percent y-o-y. Overall, average daily trading volume of agency securities in the first quarter was $42.6 billion, in line with $42.3 billion that traded in Q1'12.

The 12 Federal Home Loan Banks (FHLB) issued $46.4 billion in LTD in the first quarter, a decrease of 29.7 percent and 47.4 percent, respectively, from 4Q'12 ($66 billion) and 1Q'12 ($88.2 billion). A little more than $810.5 billion in short-term debt (STD) was issued in 1Q'13, a decrease of 22.1 percent q-o-q and an increase of 11.7 percent y-o-y.

Total FHLB LTD outstanding was $472.9 billion at quarter end, relatively unchanged from $471.5 billion outstanding at the end of the fourth quarter and down 1 percent y-o-y ($476.3 billion). Discount notes decreased slightly to $193 billion at quarter-end 2013 from year-end 2012 ($216.3 billion). However, this was an increase from 1Q'12 ($181.7 billion).

Fannie Mae's 1Q'13's gross debt issuance, both STD and LTD, totaled $146.6 billion, up 13.5 percent from 4Q'12 ($129.1 billion); STD issuance increased to $83.9 billion, a 30.5 percent increase q-o-q while LTD issuance remained unchanged at $62.7 billion. Fannie Mae had $115.3 billion in STD outstanding in 1Q'13, up from $105.2 billion STD outstanding as of 4Q'12, and $520.4 billion LTD outstanding, a slight increase from $516.4 billion in 4Q'12.

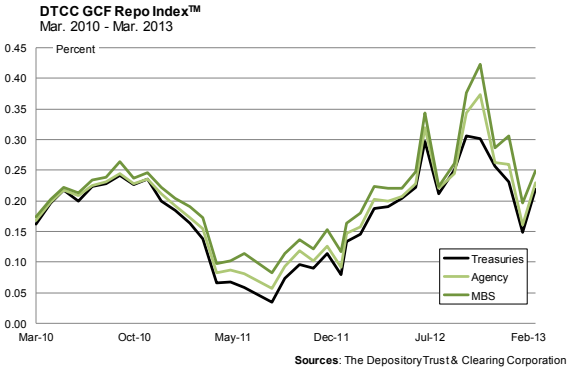
Freddie Mac's first quarter gross debt issuance totaled $103.8 billion, a 5.4 percent decrease from 4Q'12 ($109.7 billion) and a 20.5 percent decrease from 1Q'12 ($130.6 billion). As of quarter-end, Freddie Mac had $124.4 billion STD and $411.1 billion LTD outstanding, an increase of 4.91 percent and a decrease of 5.8 percent, respectively, from the prior quarter.

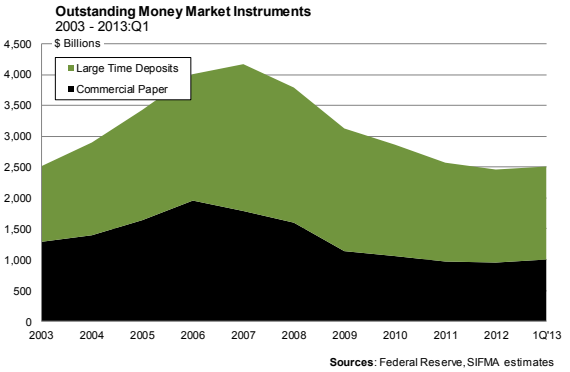
Total Farm Credit System gross debt issuance at year end totaled $107.5 billion. Total debt outstanding ended the first quarter at $197.9 billion, of which $17.1 billion was short-term and $180.8 billion was long-term debt.

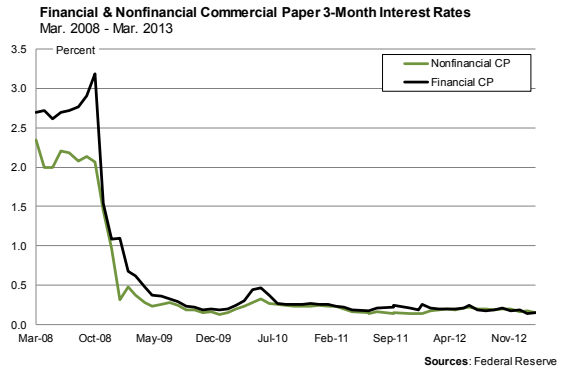
Primary dealers polled by SIFMA in the First Quarter Government Forecast survey expected gross coupon issuance for the four largest Federal agencies (FHLB, Fannie Mae, Freddie Mac, and the Farm Credit Systems) to reach $106.2 billion in the second quarter of 2013.[5] By agency, gross coupon issuance was expected to be $34.1 billion for Fannie Mae, $11.1 billion for Freddie Mac, $44.2 billion for the FHLBs, and $16.8 billion for the Farm Credit System.

[5] See SIFMA's U.S. Government Forecast 1Q'13.

FUNDING AND MONEY MARKET INSTRUMENTS







Total Repurchase Activity Decreases in Fourth Quarter[6]

The average daily amount of total repurchase (repo) and reverse repo agreement contracts outstanding decreased to $3.83 trillion in 1Q'13. This represents a decrease of 21.5 percent from 4Q'12's average of $4.88 trillion, and a 21.0 percent decrease y-o-y.

Daily average outstanding repo transactions totaled $2.38 trillion in 1Q'13, down from 4Q'12's average of $2.73 trillion. Further, reverse repo transactions in 1Q'13 averaged nearly $1.44 trillion, down from 4Q'12's $2.15 trillion.

Treasuries, Agency and MBS Repo Rates Fall

In 1Q'13 the DTCC GCF Repo rates decreased for Treasuries, agency debt, and MBS. Specifically, the repo rate for Treasuries (30-year and less) decreased to 0.219 percent from 4Q'12's 0.257 percent. The agency repo rate fell to 0.229 percent from 0.262 percent, and the MBS repo rate decreased to 0.249 percent from 0.287 percent. More generally, the use of agency MBS as collateral for repo has decreased, with approximately 37.6 percent by dollar amount of tri-party repo collateralized by agency MBS in the first quarter, compared to 38.8 percent in 4Q'12.

Total CP Outstanding Increases

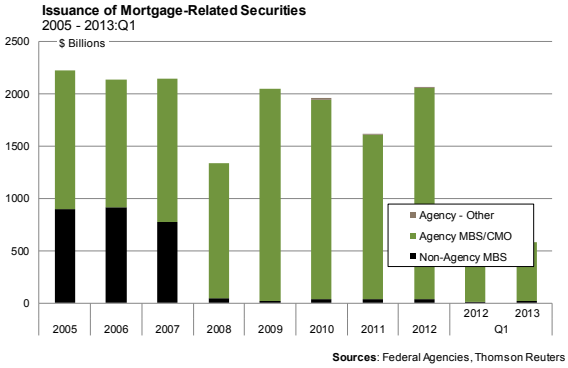
The outstanding volume of total money market instruments (MMI), including commercial paper (CP) and large time deposits, stood at $2.51 trillion at the end of the first quarter, 2.9 percent above the $2.43 trillion in 4Q'12 and a 3.4 percent decrease y-o-y. CP outstanding totaled approximately $1.01 billion, a 5.1 percent increase from the $952 million in 4Q'12 and a 0.6 percent increase y-o-y. Large time deposits totaled $1.5 trillion in 1Q'13, an increase of 1.6 percent from 4Q'12, yet a 5.8 percent decrease y-o-y from $1.6 trillion.

Financial and Nonfinancial 3-Month CP Interest Rates Decrease

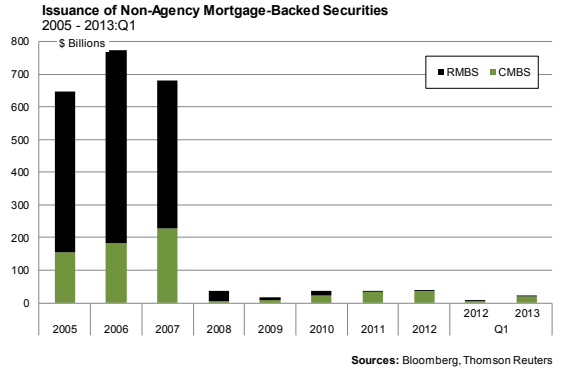
The interest rates for financial and nonfinancial CP decreased in the first quarter of 2013. Financial CP's rate was 0.15 percent at the end of 1Q'13, which represents a decrease of two basis points (bps) from 4Q'12's 0.17 percent, and was five bps lower than 1Q'12's 20 bps. The rate for nonfinancial CP was 0.15 percent in 1Q'13, which represents a five bps decrease from 4Q'12's 0.20 percent, and a three bps decrease from 1Q'12's 0.17 percent.

[6] As a reminder, repo data is provided by the primary dealers only: http://www.newyorkfed.org/markets/gsds/search.cfm. For a breakdown of tri-party repo data, please refer to the Federal Reserve Bank of New York's Tri-party Repo Reform website here: http://www.newyorkfed.org/banking/tpr_infr_reform.html.

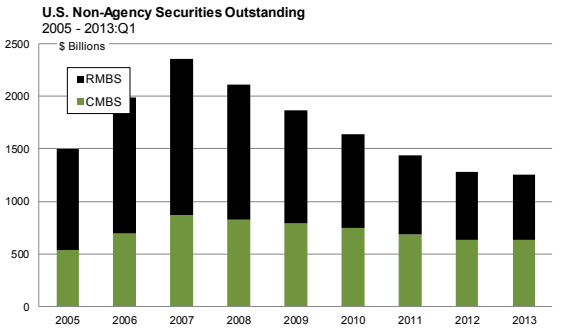
MORTGAGE-RELATED SECURITIES



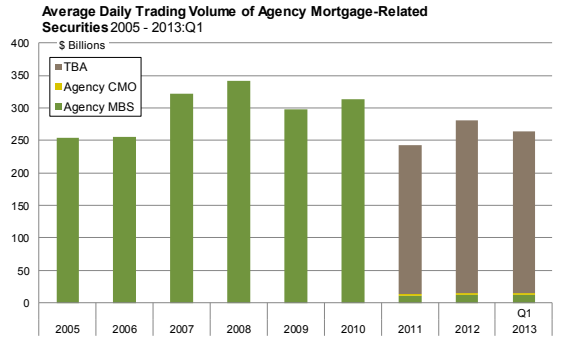
Sources: Federal Agencies, Thomson Reuters



Sources: Bloomberg, Thomson Reuters



Sources: Loan Performance, Fitch Ratings, Moody's, S&P, SIFMA, Thomson Reuters
In 2011Q1, ABS outstandings were revised and certain securities in non-agency were moved to ABS categories. Numbers have been restated to reflect changes.



Sources: Federal Reserve Bank of NY (pre-2011), FINRA Trace (2011 onward); 2011 data is a daily average beginning May 15, 2011 as Trace data starts May 2011.

Mortgage-Related Market Increases

Issuance of mortgage-related securities, including agency and non-agency passthroughs and collateralized mortgage obligations (CMOs), totaled $576.0 billion in the first quarter, a 2.0 percent and 18.6 percent increase, respectively, from 4Q'12 ($564.5 billion) and 1Q'12 ($485.4 billion). The pickup in issuance was almost entirely due to the pickup in the non-agency sector, particularly commercial mortgage-backed securities (CMBS) issuance. Overall, the agency share of issuance declined to 96.5 percent in 1Q'13, down from 98.6 percent in the prior quarter.

The housing market continued to recover during 1Q'13. The Case-Shiller 20-City Composite index rose to 149.8 in February 2013, posting continuous gains monthly since reaching a post-crisis low of 136.86 in January 2012.

According to Freddie Mac, average rates on conventional 30-year mortgages, after moving steadily upward at the beginning of the quarter, reached the 2013 high of 3.63 percent on March 14th before moving back down again, ending the quarter at 3.57 percent.

Agency Issuance and Outstanding

Agency mortgage-related issuance totaled $556.0 billion in 1Q'13, an increase of 0.9 percent and 16.1 percent, respectively, from 4Q'12 and 1Q'12. Activity levels remained similar to the prior quarter. Agency MBS outstandings increased by 0.7 percent in 1Q'13.

Non-Agency Issuance and Outstanding

Non-agency issuance totaled $20.0 billion in 1Q'13, an increase of 49.3 percent from 4Q'12 ($13.4 billion) and a threefold increase from 1Q'12 ($6.4 billion). The rise was primarily due to CMBS issuance, composing the majority of non-agency issuance, reaching $18.4 billion in 1Q'13. Non-agency RMBS issuance was $1.6 billion in 1Q'13, an increase of 421.4 percent and 77.2 percent, respectively, q-o-q and y-o-y.

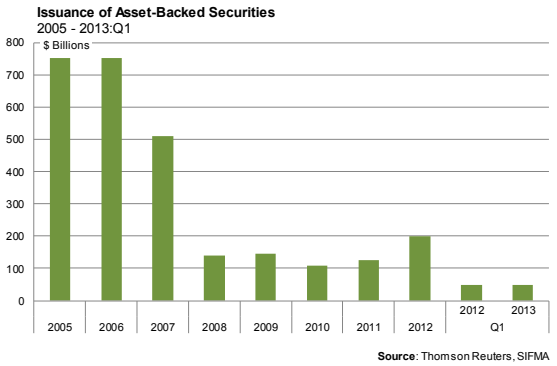
Interest in non-agency RMBS, a sector particularly affected by the crisis, picked up in the first quarter. More notably, two new banks issued jumbo prime deals in the first quarter, a first since the crisis began: a $2.3 billion deal from J.P Morgan Chase and a $307 million deal from Everbank. Previously, the only new jumbo deals in the market had been from the Redwood Trust (Sequoia Mortgage).

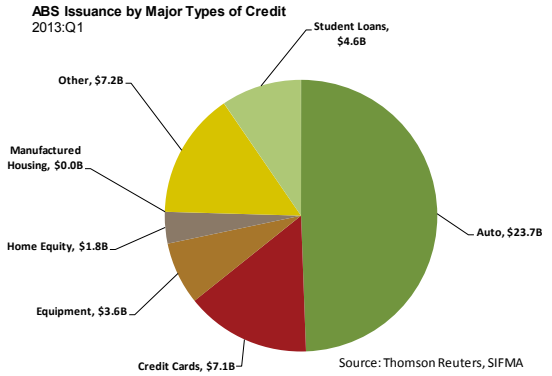
Non-agency outstandings continued to decline, with $1.25 trillion outstanding end-March, down 2.3 percent from the end of 2012, comprising $636.4 billion in non-agency CMBS (unchanged from the prior quarter) and $613.6 billion in non-agency RMBS (a decline of 4.6 percent from the prior quarter).

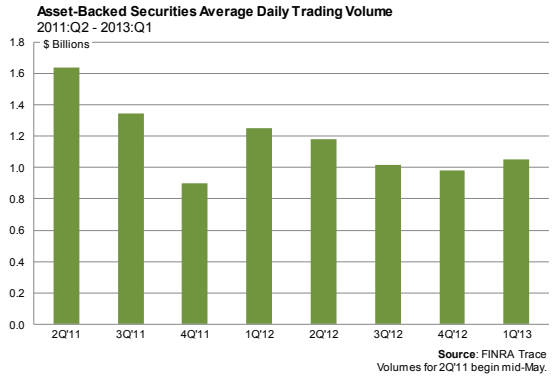
Trading Activity and Rates

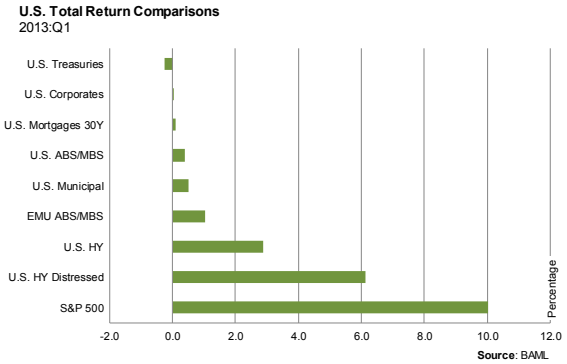
Average daily trading volumes of agency mortgage-related securities, including passthroughs, CMOs, and TBA, were $263.9 billion in 1Q'13, a decline of 5.9 percent from 4Q'12. Average daily trading volumes of non-agency CMBS and RMBS in 1Q'13 were $2.37 billion and $2.32 billion, respectively, an increase of 15.0 percent q-o-q for CMBS but a decline of 5.5 percent q-o-q for RMBS.

ASSET-BACKED SECURITIES









Asset-Backed Market Increases,

Asset-backed securities (ABS) issuance totaled $48.2 billion in the first quarter, an increase of 7.1 percent from 4Q'12 ($44.8 billion) but unchanged from 1Q'12. The auto sector continued to lead issuance totals with $23.7 billion (49.4 percent of total issuance in 1Q'13), followed by other ($7.2 billion, or 15 percent) and credit cards ($7.1 billion, or 14.8 percent). The 'other' category experienced pickup again, with a cell tower lease deal coming to market as well as several new catastrophe bond deals.

Outstandings continue to decline, with $1.69 trillion outstanding at the end of the first quarter, compared to $1.70 trillion in 4Q'12 and $1.79 trillion in 1Q'12. Only auto and equipment outstandings grew in the first quarter, increasing by 4.7 percent and 4.5 percent, respectively, from 4Q'12. In the remainder of the ABS sectors, however, outstandings continued to decline. Declines were most pronounced in manufacturing housing (5.2 percent).

According to the Federal Reserve, consumer credit outstandings continue to climb, increasing by 5.7 percent on an annual basis in 1Q'13, a decline of 6.5 percent in 4Q'12 and 5.4 percent in 1Q'12. Nonrevolving accounts have grown at a faster pace than revolving accounts: in 1Q'12, revolving accounts grew 0.2 percent on an annualized basis while non-revolving accounts grew 8.1 percent.

Trading Activity Increases

Daily average trading activity in ABS increased in the first quarter to $1.05 billion, an increase of 6.6 percent q-o-q but a decline of 16.1 percent y-o-y.

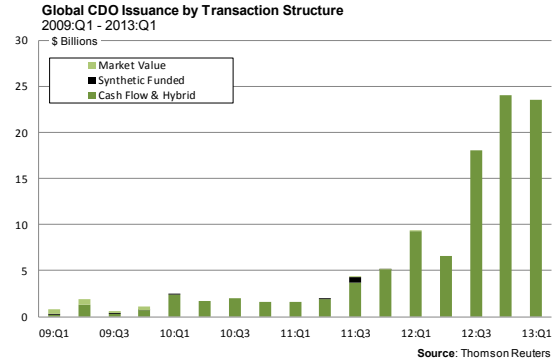
According to the Bank of America-Merrill Lynch indices, the total return for ABS and CMBS was 0.38 percent in 1Q'13, down from the 0.99 percent in 4Q'12.

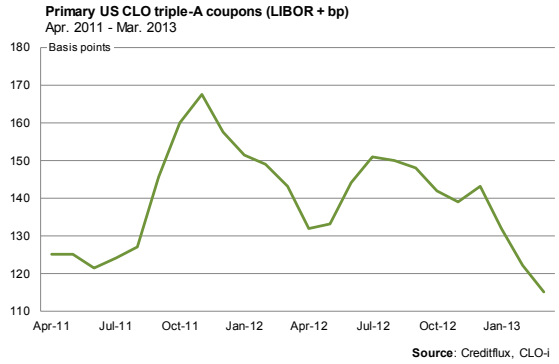
Global Collateralized Debt Obligations Issuance Rises

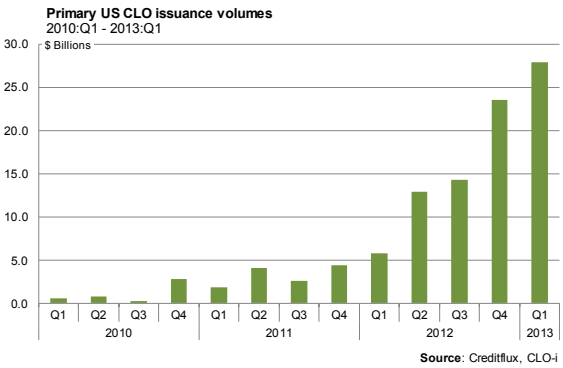
According to Thomson Reuters, global funded CDO issuance totaled $23.5 billion in 1Q'13, a decline of 2.3 percent q-o-q ($24.1 billion) and an increase of 150.3 percent from 1Q'12 ($9.4 billion). U.S. CLO issuance continues to drive most of new global CDO volume in 2013.

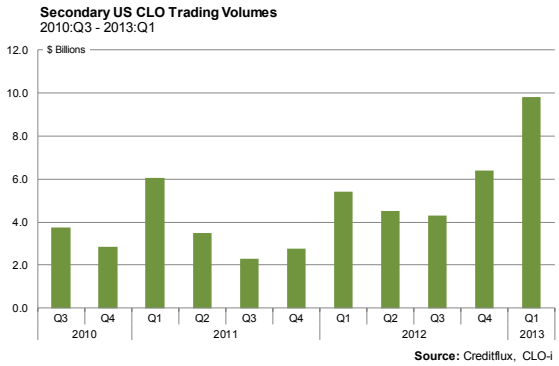
USD-denominated CLO outstandings increased for a fourth quarter in a row, growing by 6.3 percent from 4Q'12, driven by the rise in U.S. CLO issuance. However, outstandings of structured finance CDOs and other CDOs continues to decline.

COLLATERALIZED LOAN OBLIGATIONS[7]









2013 US CLO volumes On Course To Grow Beyond $100 Billion

For the seventh successive quarter, production of new U.S. CLOs increased, with $27.9 billion of issuance. Issuance in 1Q'13 topped the $23.5 billion that was printed in the 4Q'12, which at the time was the prior post-crisis record in issuance volume.

In the first three months of 2013, 55 US CLOs were printed. Issuance of these deals was spread across a large field of managers, with 51 individual managers coming to market. Twelve of these CLO managers (23.5 percent) were pricing deals for the first time since the crisis.

First quarter volumes are equal to just under half of the issuance seen during the whole of 2012 ($56.6 billion). If the current pace of CLO issuance continues to be maintained for the rest of the year, the market is on course to break beyond $100 billion in U.S. CLO volumes this year.

With business in this sector of the market so busy, a central theme during 1Q'13 was for new arrangers to emerge. StormHarbour, BNP Paribas and Cantor Fitzgerald all took on CLO structuring roles for the first time on U.S. post crisis CLO deals (CLO 2.0).

The largest transaction to price was Ares CLO XXVII, which weighed in at $940 million; UBS was responsible for arranging the deal.

CLO triple-A spreads reach post-crisis tights

A key driver behind the large quarterly total was the fall in triple-A rated CLO spreads. With spreads ending 2012 at around 140 bps, Symphony CLO XI, one of the first deals out of the door in 2013, priced its senior liabilities at 130 bps. This, in turn, set the mark for other deals to follow and was the tightest triple-A print in eight months.

Triple-A CLO spreads continued to compress during 1Q'13, hitting a post-crisis tight of 110 bps in February from a Prudential-managed deal. For the remainder of the quarter, spreads began to slowly edge out, settling in the mid-high 110s by the end of March.

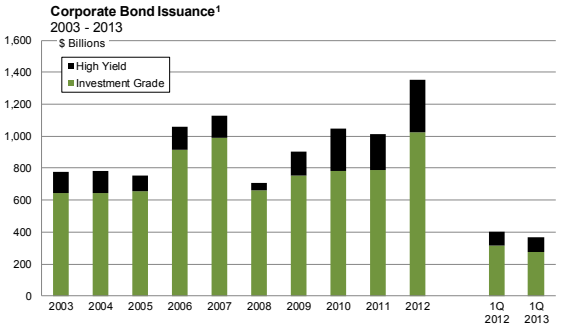
Volumes of Secondary CLO Paper Reach New Highs

Observers expected that when the market for new issue CLOs picked up, trading volumes of secondary CLO paper would fall back. This was not the case in 1Q'13 when $9.8 billion of U.S. CLO paper was put on the auction block, making it one of the most active quarters on record.

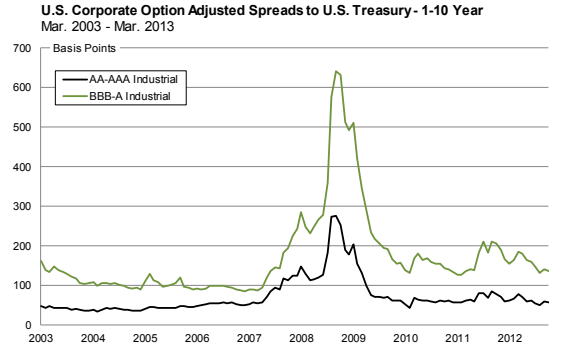
Most of the activity came in a busy February; $1.5 billion of CLO paper was circulating in the first full week of the month, marking it out as one of the busiest since the crisis.

[7] The author of the CLO section is Sayed Kadiri, Creditflux. For any questions, please contact Sayed Kadiri at sayed.kadiri@creditflux.com.

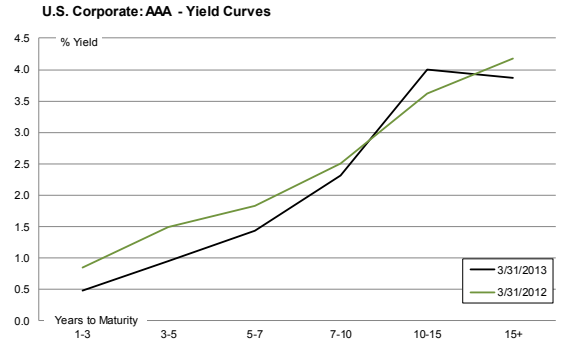
CORPORATE BOND MARKET



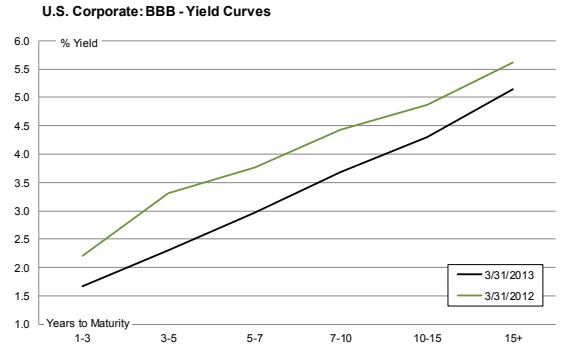
[1]Includes all nonconvertible debt, MTNs Yankee bonds, and TLGP debt, but excludes all issues with maturities of one year or less, CDs, and federal agency debt
Source: Thomson Reuters



Source: Bank of America Merrill Lynch



Source: Bank of America Merrill Lynch



Source: Bank of America Merrill Lynch

Corporate Bond Issuance Stays Flat

Corporate bond issuance totaled $365.2 billion in 1Q'13, almost unchanged from the $364.6 billion issued last quarter but 9.8 percent below the $404.8 billion issued in 1Q'12.

Investment grade (IG) bond issuance increased to $273.4 billion, a 1.5 percent increase from 4Q'12's $269.4 billion but a 12.6 percent decrease from $312.9 billion issued in 1Q'12. Financial companies remained the leading industry in IG debt issuance, representing 52.8 percent of IG issuance (up from 36.7 percent in 4Q'12), followed by energy and power with 11.0 percent (down from 16.3 percent in 4Q'12).

After a quarterly record high of $95.2 billion in 4Q'12, the issuance of high yield (HY) bonds declined slightly to $91.9 billion in 1Q'13, down 3.5 percent from the previous quarter and almost unchanged from $91.8 billion in 1Q'12. Despite the decline, the $91.9 billion issued in the first quarter was the third highest HY debt quarterly issuance volume on record, behind 4Q'12 ($95.2 billion) and 3Q'12 ($93.7 billion). Despite investor concerns regarding the situation in Europe and slow recovery of the U.S. economy, demand for HY corporate debt remained high in 1Q'13. As a result, many firms were able to refinance their maturing debt at the record low yields or explore opportunities financed at relatively low cost.

Speculative-grade Bond Spreads Narrow; U.S. Default Rate Decreases Slightly

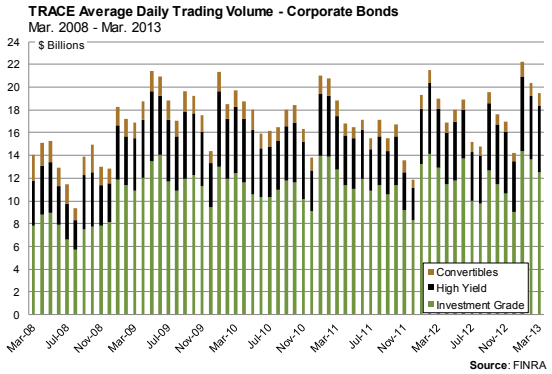
According to the S&P, composite spreads for IG bonds stayed relatively unchanged in the first quarter of 2013, while the spreads for HY bonds narrowed. Spreads of IG bonds increased slightly to 186 bps at the end of March 2013 from 182 bps at the end of 4Q'12 but declined from 205 bps in 1Q'12. Spreads of IG bonds remain 25.4 percent below the 5-year average of 244 bps. HY bond spreads narrowed significantly in the first quarter of 2013, finishing at 514 bps, 7.2 percent below 554 bps at the end of 4Q'12 and 17.4 percent below 622 bps in 1Q'12. Despite the significant decrease in the cost of borrowing over the last year and HY bond spreads remaining 26.1 percent below its 5-year moving average of 750 bps., spreads remain considerably wider than the tightest recorded spread of 265 bps as of May 25, 2007.

The S&P's Global Fixed Income Research reported the global corporate default tally to be 21 issuers in 1Q'13, of which fourteen were based in the U.S., which represents an increase in U.S. defaults from 9 in 4Q'12. The top reasons for defaults remained unchanged as majority of defaults happened due to a missed interest or principal payment (seven defaults in 1Q'13) or bankruptcy filings (six defaults). The trailing 12-month default rate has decreased to 2.4 percent in March 2013 from 2.6 percent in December 2012 and from 2.5 percent in March 2012. Based on the future expectations and the likely path of the U.S. economy and financial markets, the S&P predicts that the default rate will rise to 3.4 percent by year-end 2013, up from 2.6 percent as of December 2012.

S&P US Corporate Rating Actions

	2013:Q1	2012:Q4	2012:Q1
Upgrades	55	46	77
Downgrades	62	88	67

Source: S&P Fixed Income Research



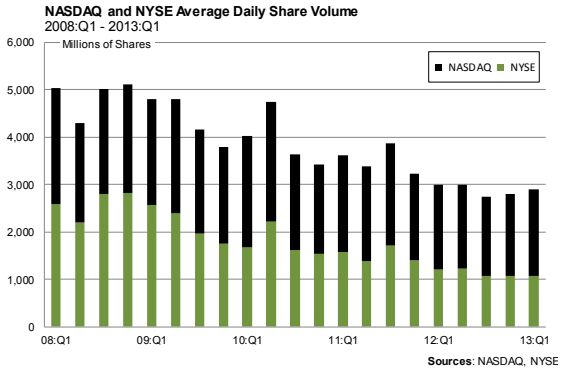
In 1Q'13 S&P Ratings Services downgraded 62 and upgraded 55 U.S. issuers, a better outcome than in previous quarter, when there were 88 downgrades versus 46 upgrades. The ratio of downgrades to upgrades declined from 1.2 for 1Q'13 from 1.9 in 4Q'12 but increased y-o-y from 0.9. (summary of the numbers in the table to the left).

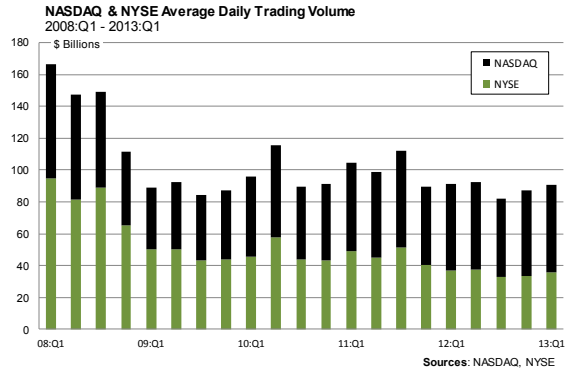
IG Trading Volume Increases

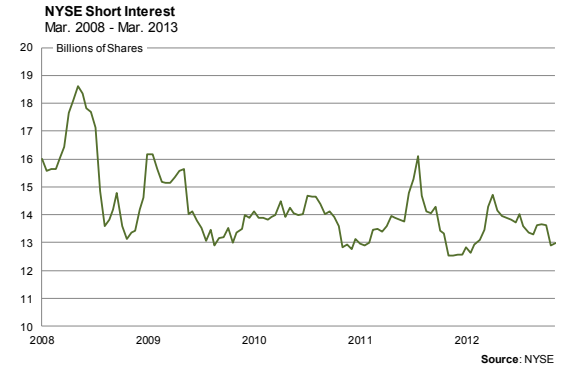
According to the FINRA TRACE data, trading volume for IG, HY, and convertible bonds (CVs) increased in the first quarter of 2013. IG average daily trading volume increased to $13.5 billion, up 30.3 percent from $10.4 billion in 4Q'12 and up 0.9 percent from $13.4 billion in 1Q'12. HY average daily trading volume stood at $6.0 billion in 1Q'13, an 18.8 percent increase from $5.0 billion in the fourth quarter and a 9.7 percent increase from $5.5 billion in the same year-earlier period. The average daily trading volume of CV bonds increased as well. In 1Q'13, CV bonds trading volume stood at $1.2 billion, 38.5 percent above 4Q'12's $0.9 billion and 8.6 percent higher than the average trading volume of $1.1 billion a year ago.

On a monthly basis, after a very slow month of December, corporate bond trading volumes increased significantly in January, which was the month with the highest trading activity in the first quarter. For IG bonds, trading increased to $14.4 billion in January, a 58.9 percent increase from $9.1 billion in December, while for HY bonds, trading increased to $6.5 billion, a 47.9 percent increase from $4.4 billion over the same period.

EQUITY AND OTHER MARKETS







The S&P 500 closed the fourth quarter at 1,569.19, a 10.0 percent increase from the prior quarter and 11.4 percent up y-o-y. The NASDAQ Composite Index finished the first quarter of 2013 at 3,267.52, a 8.2 percent gain from 4Q'12 and a 5.7 percent increase y-o-y. The Dow Jones Industrial Average (DJIA) increased as well, finishing 1Q'13 at 14,578.54[8], an 11.3 percent gain q-o-q and a 10.3 percent increase from 1Q'12. Equity investors recorded quarterly gains as U.S. GDP growth increased at an annual rate of 2.5 percent in 1Q'13 after a very modest 0.4 percent growth in 4Q'12.

NYSE & NASDAQ Daily Share Volume Increases

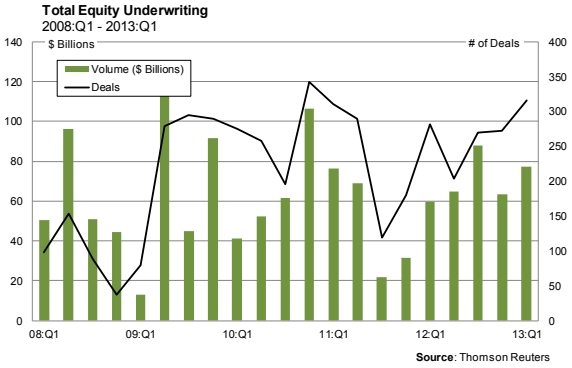
The New York Stock Exchange's (NYSE) 1Q'13 average daily share volume increased to 1.08 billion shares, 0.8 percent above the previous quarter's 1.07 billion but 10.4 percent below 1.2 billion in 1Q'12. The 1.08 billion traded is the third lowest quarterly average daily share volume on NYSE since 0.96 billion shares in 3Q'00 after the 1.07 billion in 4Q'12. The NYSE's average daily dollar volume increased as well. The average dollar volume stood at $35.5 billion in 1Q'13, 7.0 percent above the previous quarter's $33.2 billion but 4.0 percent lower than 1Q'12's $36.9 billion.

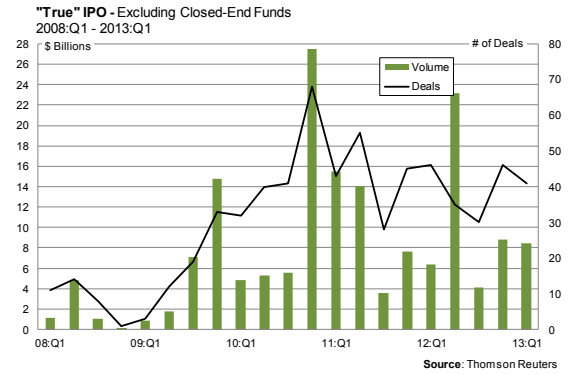
NASDAQ's average daily share volume increased by 5.0 percent to 1.8 billion shares in 1Q'13 and by 1.3 percent y-o-y. The dollar trading volume increased to $55.2 billion in 1Q'13, up 2.4 percent from $53.9 billion in 4Q'12 and 1.2 percent above the 1Q'12's $54.6 billion.

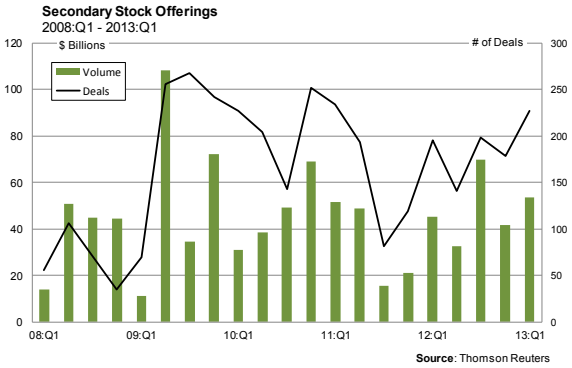
NYSE Short Interest Increases

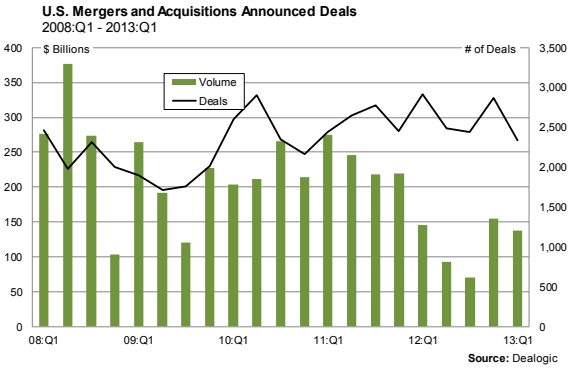
The number of shares sold short on the NYSE Group stood at 13.2 billion shares at the end of 1Q'13, up 2.5 percent from 12.9 billion at the end of previous quarter and 4.7 percent above 12.6 billion in 1Q'12. The short interest increased steadily during the quarter with the highest tally of 13.6 billion in the middle of March but remained 6.5 percent below the 5-year average of 14.2 billion shares.

[8] The Dow Jones Industrial Average passed the 15,000 level for the first time on May 7, 2013.









Equity Underwriting Increases

After a slow fourth quarter of 2012, equity underwriting increased in 1Q'13. Underwriting reached $77.1 billion in the first quarter, 21.1 percent above the $63.6 billion in 4Q'12 and 28.9 percent above the $59.8 billion in 1Q'12. Equity underwriting in 1Q'13 was 23.1 percent higher than the 5-year average of $32.6 billion. The number of equity underwriting deals increased in 1Q'13 to 316 deals, up 16.2 percent q-o-q and 12.1 percent y-o-y. The average deal size increased to $243.9 million in the first quarter, an increase of 4.3 percent and 15.0 percent, respectively, from 4Q'12 and 1Q'12.

IPO Volume Declines

"True" initial public offerings (IPOs), which exclude closed-end mutual funds, decreased in 1Q'13 to $8.5 billion on 41 deals, a 3.9 percent decrease from $8.8 billion and a 10.9 percent decrease from 46 deals in the previous quarter. The $8.5 billion in 1Q'13 was 7.2 percent above the 5-year average of $8.2 billion. According to Dealogic, the leading sector in IPOs in the first quarter was healthcare (32.7 percent of the total), followed by oil and gas (11.7 percent) and real estate and property (10.5 percent) sectors.

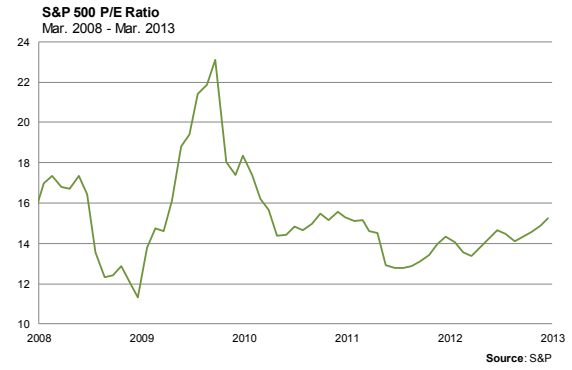
Secondary Offerings Increase

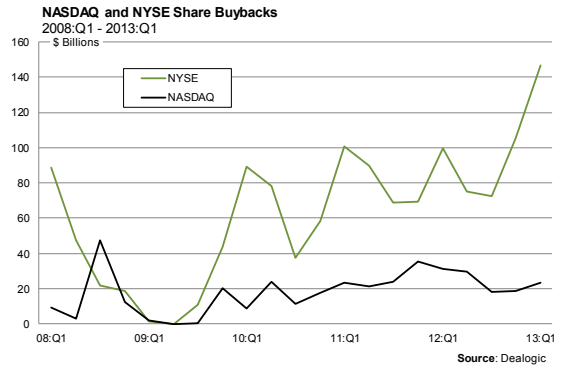
Secondary market issuance increased to $53.5 billion on 227 deals from $41.8 billion on 179 deals in 4Q'12 (an increase of 27.8 percent and 26.8 percent, respectively). The average deal value for the quarter increased by 0.7 percent to $235.5 million from $233.8 million in the previous quarter. Year-over-year, secondary issuance increased by 18.7 percent in dollar volume and by 16.4 percent in number of deals.

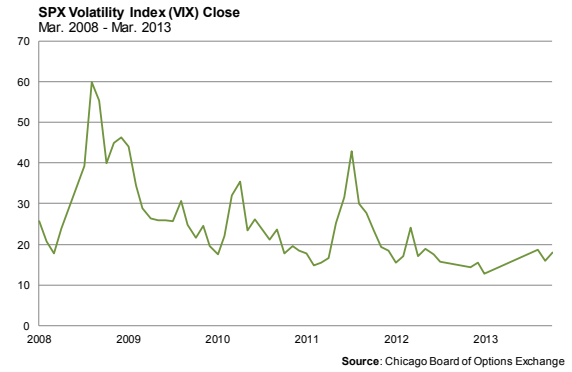
Announced M&A Volume Decreases

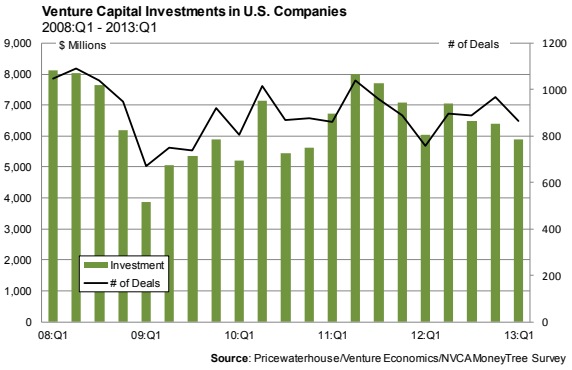
Announced U.S. mergers and acquisitions (M&A) volume in 1Q'13 stood at $137.8 billion, down 11.0 percent from the previous quarter's $154.8 billion and a 5.1 percent decrease y-o-y. The slowdown in M&A activity at the beginning of the year was expected following the year-end rush to close deals prior to the impending tax changes. Some of the bigger deals in 1Q'13 included: the Google acquisition of Channel Intelligence, the Twitter acquisition of Bluefin Labs and the Facebook agreement agreeing to acquire Microsoft's Atlas DMT. M&A volume remains 35.0 percent below the 5-year quarterly average of $211.9 billion. The number of deals decreased by 18.5 percent, falling to 2,336 this quarter from 2,868 in 4Q'12, while the average deal size rose by 9.2 percent to $59.0 million.

According to data from Dealogic, the amount "U.S. Inbound" M&A (money invested in U.S. companies by those outside the U.S. through M&A), decreased by 77.9 percent to $18.0 billion from an exceptionally high volume of $81.5 billion in the previous quarter. On the other hand, the dollar amount U.S. companies invested in other countries increased; American firms invested $61.2 billion in deals outside of the U.S., a 5.9 percent increase from $57.8 billion in 4Q'12.









P/E Ratio Increases, Remains below Five-Year Average

The S&P 500's P/E ratio averaged 14.9 in 1Q'13, up 4.0 percent from the previous quarter's average of 14.3 and 2.3 percent below the 5-year average of 15.4. The P/E ratio increased by 7.1 percent y-o-y and is 32.6 percent below the quarterly high of 22.1 in 4Q'09.

Share Buybacks Increase on NYSE and NASDAQ

The volume of corporate share repurchases on NYSE totaled $146.9 billion on 122 deals in 1Q'13, up 39.2 percent by dollar volume but down 7.6 percent by number of deals, from $105.5 billion on 132 deals in 4Q'12. The average deal size increased by 50.7 percent to $1.2 billion in 1Q'13 from $799.1 million in 4Q'12. Year-over-year, NYSE share buybacks increased by 47.6 percent in dollar volume and by 17.3 percent in number of deals.

NASDAQ's buybacks stood at $23.6 billion in 1Q'13, a 25.5 percent increase from 4Q'13's $18.8 billion while the number of deals decreased by 30.1 percent to 93 from 133 q-o-q. The average deal size increased to $253.4 million from $141.2 million (up 79.5 percent). Year-over-year, NASDAQ share repurchases declined by 24.2 percent in dollar volume but increased by 13.4 percent in number of deals.

CBOE VIX Index Decreases

The Chicago Board Options Exchange Volatility Index (VIX) decreased by 29.5 percent to 14.2 in the first quarter of 2013 from 17.5 in 4Q'12. The index has showed a general downward trend since the beginning of October 2011. During the first quarter, a low of 11.3 was reached in the middle on March right after the high of 19.0 was reached at end-February.

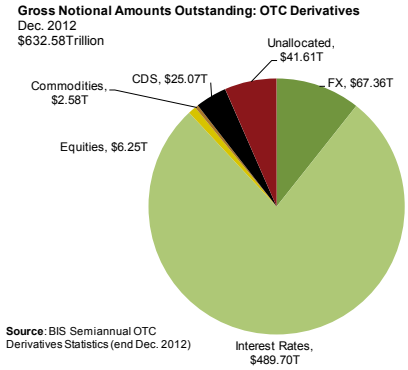
Venture Capital Declines

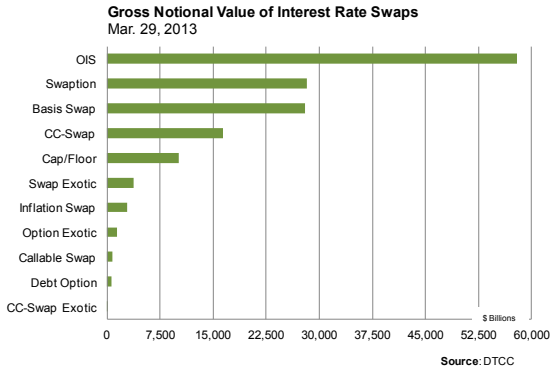
Venture capitalists invested $5.9 billion in 863 deals in the first quarter of 2013, according to the MoneyTree™ Report from PricewaterhouseCoopers LLP (PwC) and the National Venture Capital Association (NVCA), based on data provided by Thomson Reuters. Quarterly venture capital (VC) investment activity fell 11.9 percent in terms of dollars and 14.8 percent in the number of deals compared to the fourth quarter of 2012 when $6.7 billion was invested in 1,013 deals. Compared to the 1Q'12, venture capital investments decreased by 2.4 percent in dollar volume but increased by 13.9 percent in number of deals.

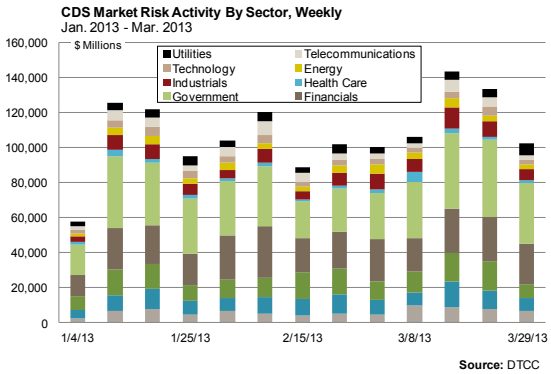
The life sciences (biotechnology and medical device industries combined) and clean technology sectors both saw marked decreases in both dollars and number of deals in the first quarter. However, there was a notable percentage increases in dollars invested in the media & entertainment industry while the software industry accounted for 40 percent of the dollars invested in the quarter.[9]

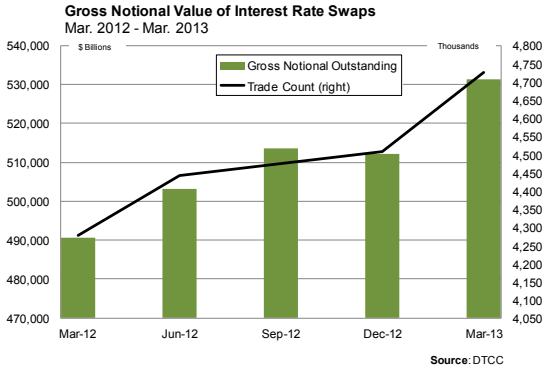
[9] PricewaterhouseCoopers LLP and the National Venture Capital Association, MoneyTree™ Report, Press Release, April 19, 2013.

DERIVATIVES









According to the most recent Bank of International Settlements (BIS) Semiannual Over-the-Counter (OTC) Derivatives Markets Statistics Report (released May 2013), the gross notional amount outstanding of OTC derivatives totaled $632.6 trillion as of end-December 2012 (down 1.2 percent from end-June). Although foreign exchange contracts saw a slight increase from end-June 2012, up 1.2 percent to $67.4 trillion. However, all other risk categories and instruments saw decreases of varying degrees. Commodity contracts saw the largest decrease, dropping 13.6 percent to $2.6 trillion. Credit default swaps (CDS) and other products (unallocated in the BIS report) had the next largest decreases, down 6.9 percent (to $25.1 trillion) and 1.2 percent (to $41.6 trillion), respectively. While the gross notional amount outstanding for all risk categories and instruments aside from foreign exchange contracts decreased, the gross credit exposure of outstanding OTC derivatives remained relatively flat from end-June 2012 to end-December 2012 at $3.7 trillion.

Interest Rate Swaps[10]

According to DTCC data, the gross notional value of outstanding interest rate swaps (IRS) at the end of March 2013 was $531.2 trillion, up 3.7 percent from end December's $512.2 trillion. Decreases in debt options, callable swaps and exotic options were offset by increases in overnight indexed swaps, forward rate agreements and inflation swaps. The number of contracts outstanding increased slightly q-o-q to 4.7 million, with the largest increases in forward rate agreements (up 13.9 percent q-o-q) and swaptions (up 13.2 percent q-o-q). The largest decreases were found in debt options (down 6.3 percent q-o-q), cross-currency exotic swaps (down 4.7 percent q-o-q) and callable swaps (down 4.6 percent q-o-q).

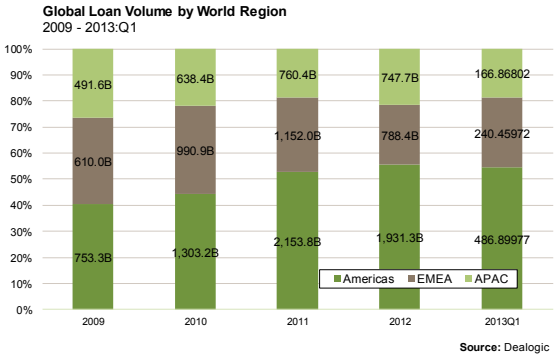
Credit Default Swaps

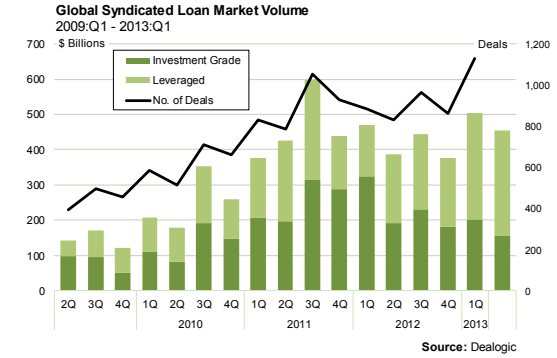
According to DTCC data, the gross notional value outstanding of CDS, including single names, tranches and indices, stayed relatively flat at $23.63 trillion end-March 2013 from $23.19 trillion end-December 2012, but declined 10.4 percent y-o-y. Single name CDS outstanding decreased slightly on a gross notional basis by 3.2 percent q-o-q to $12.9 trillion (from $13.3 trillion), while on a net notional basis, the outstanding value decreased by 4.5 percent q-o-q to $951 billion (from $996 billion).

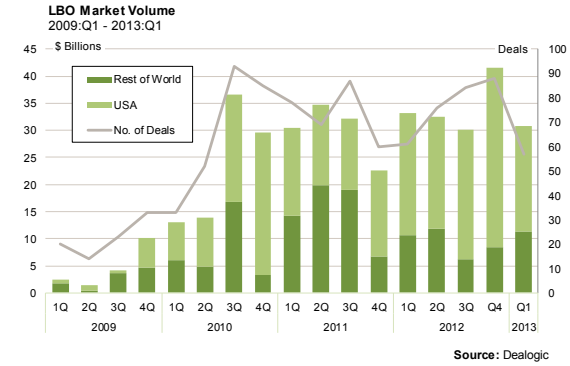
In the first quarter, net notional outstandings were concentrated in government and financial reference entities ($252.0 billion and $221.1 billion, respectively). CDS outstanding increased on a net notional basis q-o-q in certain Eurozone sovereigns, including Germany, France and Spain but decreased in Italy. The most often referenced entities outstanding by gross notional exposure in the first quarter were concentrated in European sovereigns, as was the case in 4Q'12, led by Italy ($333.2 billion), Spain ($172.1 billion) and France ($138.0 billion). Aside from governments and financials, outstandings increased on a net notional basis in both consumer services (up 12.8 percent q-o-q, to $107.2 billion) and consumer goods (up 11.2 percent q-o-q, to $115.0 billion). Some of this activity may be explained by the European ban on "naked" sovereign CDS positions in November 2012, which some experts believe has led to increased trading in financial CDS.

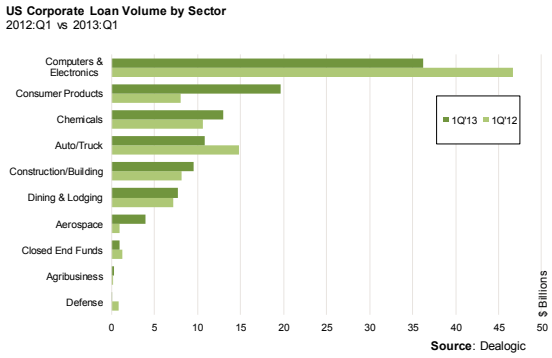
[10] Beginning May 2012, DTCC took over responsibility for collecting/publishing OTC interest rate trades from TriOptima. As such, sizable increases in certain categories may be the result of different reporting and collecting procedures.

PRIMARY LOAN MARKET









U.S. marketed syndicated loan volume totaled $455.3 billion in 1Q'13, down 9.7 percent from the $504.4 billion in 4Q'12 but a 17.5 percent increase y-o-y. The number of deals similarly declined to 743 in 1Q'13, the lowest since 2Q'10 (709 deals).

U.S. market loans accounted for 54.4 percent of the global loan volume in the first quarter of 2013, a slight decline from all of 2012 (55.7 percent) as the European market picked up.

Regional Breakdown

The Americas accounted for 54.4 percent of global loan volume in 1Q'13 with $486.9 billion borrowed, down slightly from its 55.7 percent share in 2012. EMEA lending accounted for a 26.9 percent of global volume, up from 2012 (22.7 percent).

Use of Proceeds

Refinancing volume totaled $175.6 billion in the first quarter of 2013, accounting for 38.5 percent of U.S. syndicated loan volume, up from 25.4 percent in 4Q'12 and 31.7 percent in 1Q'12. General corporate purpose volume declined 23.1 percent to $157.1 billion in 1Q'13 from $204.3 billion in 4Q'12, but was an 18.3 percent increase from the $132.8 billion in 1Q'12.

Deal Types

Investment grade (IG) loans stood at $155.9 billion in 1Q'13, down 23.2 percent and 19.0 percent, respectively, q-o-q ($203.2 billion) and y-o-y ($192.4 billion). Average all-in pricing increased to 182.0 bps in 1Q'13, up from 165 bps in 4Q'12 but a decline from 184.9 bps in 1Q'12.

Leveraged loan volume was $299.3 billion in 1Q'13, a decline of 0.6 percent q-o-q ($301.2 billion) but an increase of 53.4 percent y-o-y ($192.2 billion). Leveraged loan volume accounted for a 65.7 percent share of U.S. marketed loans in 1Q'13, the highest quarterly proportion on record.

Corporate Borrowers

U.S. corporate loan volume fell to $375.4 billion in 1Q'13, a 10.5 percent decline from the $419.4 billion borrowed in 4Q'12 but a 22.5 percent increase from the $306.4 billion borrowed in 1Q'12. The number of deals however, declined to 610, a 36.7 percent decline q-o-q, compared to 668 in 1Q'12, a 8.7 decline. The average tenor in 1Q'13 was 4.8 years, up from 4.6 years in 4Q'12 and 4.3 years in 1Q'12.

Healthcare led all industries in the first quarter, with a total volume of $41.6 billion, followed by utility ($40.7 billion). Mining experienced the largest q-o-q increase to $18.0 billion, up from $3.1 billion, due to a $16.5 billion deal from Freeport-McMoran Copper & Gold Inc. The top 10 industries accounted for 71.3 percent of U.S. corporate lending volume in 1Q'13.

Financial Sponsor & LBO Loan Volume

U.S. sponsor-related loan volume totaled $138.2 billion in 1Q'13, up 7.6 percent from the $128.4 billion in 4Q'12 and a 47.2 percent increase from 1Q'12 ($93.9 billion). Computers & electronics was the largest industry targeted for LBOs at $22.4 billion, followed by retail at $16.8 billion.

Kyle Brandon
Managing Director, Director of Research

SIFMA RESEARCH

Charles Bartlett - Vice President, Director of Statistics
Sharon Sung – Assistant Vice President, Research
Justyna Podziemska – Associate, Research

General Research Contact: research@sifma.org

SIFMA CAPITAL MARKETS

Joseph Cox – Senior Associate, Capital Markets
Timothy Cummings – Senior Associate, Capital Markets
Craig Griffith – Senior Associate, Capital Markets
Ilona Logvinova – Associate, Capital Markets