Payden&Rygel Weekly Market Update

For the Week Ending September 17, 2010

MARKET LEVELS

	Friday*	Last week	Dec. 31, 2009	One year ago
Dow Jones Industrial Avg	10,601	10,463	10,428	9,784
S&P 500	1,126	1,110	1,115	1,065
NASDAQ	2,314	2,242	2,269	2,127
Russell 2000	652	636	625	615
DJ STOXX Europe 600 (€)	263	265	254	246
Nikkei Index (¥)	9,626	9,239	10,546	10,444
Fed Funds Target	0%-0.25%	0%-0.25%	0%-0.25%	0%-0.25%
2-Year Treasury Yield	0.47%	0.57%	1.14%	0.94%
10-Year Treasury Yield	2.74%	2.79%	3.84%	3.39%
U.S. $ / Euro	1.31	1.27	1.43	1.47
U.S. $ / British Pound	1.56	1.54	1.62	1.65
Yen / U.S. $	85.78	84.15	93.02	91.08
Gold ($/oz)	$1,276.80	$1,246.25	$1,096.95	$1,013.60
Oil	$73.44	$76.45	$79.36	$72.47

Levels reported as of 9:15 a.m. Pacific Standard Time

MARKET RETURNS

Year-to-date (1/1/10-9/17/10)*		Year-to-date (1/1/10-9/16/10)	
Dow Jones Indus Avg.	1.66%	**90 Day T-Bill**	0.08%
S&P 500	0.96%	**2-Year Treasury**	2.26%
NASDAQ	1.98%	**10-Year Treasury**	11.83%
Russell 2000	4.19%	**ML High Yield Index**	10.81%
MSCI World Index	-0.98%	**JPM EMBI Global Diversified**	12.67%
DJ STOXX Europe 600	3.53%	**JP Morgan Global Hedged**	5.57%

Returns reported as of 9:15 a.m. Pacific Standard Time

RECAP OF THE WEEK'S ECONOMIC RELEASES

September 14

Retail Sales – Retail sales grew by 0.4% in August, more than expected and up from July's 0.3% reading. Excluding autos, sales rose 0.6%.

Business Inventories – Business inventories rose by 1% in July, twice as much as expected and the largest increase in two years. However, sales rose as well, holding the I/S ratio steady at 1.26.

September 15

Industrial Production – As expected, industrial production rose by 0.2% in August, down from 0.6% in July. Excluding autos, the increase was 0.5%.

	Capacity Utilization – Capacity utilization crawled up from 74.6% to 74.7% in August. The figure has now recovered half of the ground it lost during the recession.
September 16	**Initial Jobless Claims** – Jobless claims fell for the third straight week, dropping to 450,000 from 453,000 the week before.
	Producer Price Index – The PPI rose by 0.4% in August, led by a rise in energy prices. Excluding food and energy, core PPI rose 0.1% over the month.
September 17	**Consumer Prices** – The CPI rose 0.3% in August, but core CPI, which excludes food and energy, was unchanged from last month. On a year-over-year basis, core inflation remained at 0.9%.
	Michigan Sentiment Preliminary – The index of consumer sentiment unexpectedly fell to 66.6 from 68.9. Unusually, opinion of upper-income households diverged from the rest by being more pessimistic, perhaps in anticipation of tax increases.

OVERVIEW

Headline inflation rose by 0.3% in August, but much of the increase was due to a 2.2% rise in energy prices. Core consumer prices (which exclude food and energy) were unchanged. On a year-over-year basis, core prices were up just 0.95%, the lowest reading since February 1961. In his speech at Jackson Hole last month, Fed Chairman Ben Bernanke pointed to inflation as the one area where FOMC members would likely find agreement and that “the FOMC will strongly resist deviations from price stability in the downward direction.” While the risk of outright deflation remains low and there are signs (including the general stabilization of shelter costs) that CPI may be bottoming, inflation is unlikely to break out above its current range without a significant improvement in the labor market.

The labor market, unfortunately, continues to show sluggish growth. Though initial jobless claims fell for the third straight week to 450,000, claims remain at elevated levels. Similarly, the increases in industrial production and capacity utilization indicate that manufacturing is not slowing as quickly as some feared. Of the data released this week, retail sales were the most encouraging with sales excluding autos growing at 0.6% in August. In general, the data suggest an economy that is improving, but too slowly.

US MARKETS:

TREASURIES

- Surprising news emerged from Japan as the Bank of Japan repurchased $17.5 billion JGB's in an attempt to drive JGB yields lower and weaken the yen relative to other G7 currencies. Because the yen recently strengthened to 15-year highs versus the US dollar, policymakers felt it necessary to intervene and support the export-driven nature of the Japanese economy.

- The bear-steepening trend continued this week in the Treasury market, as yields inside of 5 years ground lower, while 10-year and 30-year yields moved higher. The Fed purchased $1.4 billion of Treasuries in the 2-3 year maturity range, while complex derivative structures caused long-maturity duration paying/rate selling with a weaker Yen. Specifically, 2's/10's and 10's/30's were both higher on the week by 9 basis points. Volume remained above average in the Treasury market, as domestic economic data has been muddy and talk of another round of quantitative easing has persisted.

- Swap spreads moved tighter this week, amidst another round of heavy corporate issuance. No Treasury auctions are scheduled this week, and supply will remain light until 2's, 5's, and 7's are auctioned in the week of September 27th.

- It was a quiet week in the agency market as spreads remained unchanged versus Treasuries. In addition, prices of Treasury Inflation Protected Securities moved in tandem with nominal Treasuries as CPI data released Friday morning was uneventful.

LARGE-CAP EQUITIES

- The stock market rallied for the third consecutive week on positive corporate headlines. Several merger and acquisition deals, as well as an influx of corporate announcements to return capital to shareholders helped lift equity markets. The S&P 500 and Dow Jones Industrial Average indexes both finished the week approximately 1.5% higher, while the NASDAQ index rallied about 3%. Small-cap stocks outperformed large-cap stocks. In terms of style, large-cap growth stocks outperformed large-cap value stocks. The best performing sector was information technology and the worst performing sector was utilities. In earnings news this week, Oracle reported 42 cents per share, beating analysts' estimates of 37 cents per share. The company attributed the strong quarter to better software sales and their acquisition of Sun Microsystems. Shares of ORCL jumped over 7% on the positive news. In other news, Cisco initiated their first-ever dividend. Shares of CSCO rose approximately 6% for the week.

CORPORATE BONDS

- Investment grade primary activity has been on a tear since the unofficial end of summer. The new issue frenzy was somewhat expected; however, the lack of new issue concession was not. It has been estimated that more than a third of deals that have come lately have had either zero or negative concession, signifying strong demand for risk product. Notable deals this week included General Electric ($4 billion) and the Royal Bank of Scotland ($2 billion).

- Investment grade corporates tightened again in the face of an inundation of issuance. Investors have been sitting idly on the sidelines waiting for this time to come. Then again, most investors were also hoping for more of a new issue concession which has been absent recently. The Barclays Credit Index Option-Adjusted Spread (OAS) finished the week at +160, three basis points tighter. Financials tightened seven basis point (banks -6, insurance -8); industrials tightened by three, (basic materials -3, capital goods -1, telecom -3, consumer cyclical -3, consumer non-cyclical -2, energy -5); and utilities tightened by three basis points.

MORTGAGE-BACKED SECURITIES

- The mortgage market closed the week largely unchanged from last week. Thirty-year current coupon mortgage spreads versus the 10-year Treasury closed at 80 basis points to yield 3.52%. Premium mortgage backed coupons, which have been under scrutiny due to concerns about increasing prepayments, were stable with little price volatility. GNMA mortgages were slight underperformers versus conventional mortgages, continuing a trend from the past two weeks. In the private mortgage-backed securities market, secondary activity was robust with many bid lists. Prices continued to edge higher as investor's desire for higher yielding assets remains strong.

MUNICIPAL BONDS

- Relative stability in the US Treasury market provided a backdrop for muni yields to "normalize" this week. With a substantial new issue calendar over $11 billion, there was plenty of activity to facilitate price discovery. Yields were mostly unchanged, especially in maturities shorter than 5 years. Yields on 10-year AAA-rated State General Obligation bonds were 2 basis points lower by Friday, and 30-year bonds saw yields increase by 4 basis points.

- The State of Washington (Aa1/AA+) sold nearly $800 million in tax-exempt General bonds this week in two series on Wednesday. The 2027 maturity in the series C bonds were priced to yield 3.54%, 50 basis points more than a comparable AAA-rated bond.

- Build America Bonds continued to take up a significant portion of issuance, as $3.6 billion of taxable bonds priced this week, according to Bloomberg. Among the largest deals was the City of New York Municipal Water Finance Authority (Aa2/AA+), that issued $750 million of taxable bonds in 2043 and 2041, approximately +50 basis points to Treasuries.

HIGH-YIELD BONDS

- The high yield market is operating at full speed, with over $7.5 billion of bonds pricing this week and a similar or even greater amount expected next week. The new deals have been warmly received, with most of the deals trading up 2% or more in the aftermarket. There is clearly a significant amount of cash in the market and more continues to flow in, attracted by strong relative yields and improving fundamentals. High yield mutual funds reported inflows of $1.2 billion this week and this will add to already higher-than-normal cash levels. Part of the very strong new issue demand is being driven by the relative lack of new issuance over the last few weeks of August and early September. New deals have included refinancings from existing high yield issuers, such as Intelsat and Visant (the former Jostens), and deals such as the $1.8 billion high yield financing for first time issuer Energy Transfer Equity (ETE), a major actor in the gas and related pipeline industries. ETE issued their BB-rated deal with a coupon of 7.5%, and demand was so strong that the deal was up over 3% at break. Month-to-date, the Merrill Lynch BB/B index is up a solid 1.6% and up 10.4% year-to-date.

INTERNATIONAL MARKETS:

EASTERN EUROPEAN EQUITIES

- The CECE index of equities traded in Central Europe (Czech Republic, Hungary, and Poland) gained 2.7% over the past week, while the Russian stock index RTS went down by 1.5%.

- Eastern European growth rates will remain subdued in coming quarters as the recovery in the US and euro region, emerging Europe's largest export market, loses steam, said European Bank for Reconstruction and Development (EBRD) President Thomas Mirow. The London-based lender does not see a need to revise its forecast for economic growth of 3.5% for this year and 3.9% for 2011 for the 30 east European and central Asian countries it invests in, as estimates "have been rather modest." The former communist countries that the EBRD lends to are rebounding from the deepest recession since switching to a free-market policy two decades ago.

GLOBAL BONDS AND CURRENCIES

- Major non-US sovereign bond markets had a relatively quiet week as confidence in the global economic outlook continued to build and stock markets rise. Core European bond yields remained within recent ranges, as did spreads on Spanish and Greece government bonds. Sentiment on Spanish debt was bolstered following strong demand at this week's Bono auctions. However, spreads on 10-year Irish government bonds widened further to historic highs close to 400 basis points over Bunds on speculation that Ireland's deficit reduction plans may be jeopardized by bank losses and that the IMF may have to intervene to provide support. UK Gilt yields closed a few basis points lower across the curve as the Bank of England Governor endorsed the new government's fiscal austerity plans and UK retail sales fell unexpectedly in August – the first decline since January. In Japan, bond investors were relieved that the ruling DJP's leadership ballot which took place in the past week confirmed incumbent Prime Minister Kan. Investors were fearful that a victory for his challenger, Ichiro Ozawa, would see the government adopt a more aggressive fiscal stance, so Kan's win saw 10-year JGB yields end the week 8 basis points lower despite significant outperformance by Japanese stocks on the week.

- In currency markets, improvement in investor confidence saw the US dollar weaken against the Euro, sterling and high-yielding currencies such as the Australian dollar. However the greenback gained against the Japanese yen as intervention and more tough talk from the Bank of Japan appears to have halted the yen's recent steady appreciation. The Swiss franc declined in response to unexpectedly downbeat comments on Switzerland's growth and inflation prospects by the Swiss National Bank, which served to quash expectations of an imminent rate rise.

EMERGING-MARKET BONDS

- Emerging market dollar-pay debt spreads tightened marginally this week as positive risk sentiment continued from the previous week.
- In Turkey, the central bank left its benchmark interest rate unchanged, in line with expectations. The CBRT did indicate that the disinflation process continues and as a result is committed to keeping the policy rate unchanged.
- In a week when currency intervention grabbed the headlines, in particular following the move by the Bank of Japan on the yen, the Colombian Central Bank announced that it will resume daily purchases of $20 million USD to build reserves and stem the recent appreciation of the Colombian peso. The currency saw a modest weakening following the announcement.

NEXT WEEK'S ECONOMIC RELEASES

September 20	*NAHB Housing Market Index*
September 21	*Housing Starts, Building Permits*
September 23	*Initial Jobless Claims, Existing Home Sales*
September 24	*Durable Orders, New Home Sales*