Payden&Rygel Weekly Market Update

August 22, 2008

MARKET LEVELS

	Friday*	Last week	Dec. 31, 2007	One year ago
Dow Jones Industrial Avg	11,628	11,660	13,265	13,236
S&P 500	1,292	1,298	1,468	1,463
NASDAQ	2,415	2,453	2,652	2,542
Russell 2000	738	753	766	788
DJ STOXX Europe 600 (€)	284	287	365	369
Nikkei Index (¥)	12,666	13,019	15,308	16,316
Fed Funds Target	2.00%	2.00%	4.25%	4.50%
2-Year Treasury Yield	2.40%	2.38%	3.05%	4.25%
10-Year Treasury Yield	3.87%	3.84%	4.03%	4.65%
U.S. $ / Euro	1.48	1.47	1.46	1.36
U.S. $ / British Pound	1.85	1.87	1.98	2.01
Yen / U.S. $	110.09	110.53	111.71	116.19
Gold ($/oz)	$822.58	$787.70	$833.92	$660.38
Oil	$114.24	$113.77	$95.98	$69.98

Levels reported as of 10.30 am. Pacific Standard Time

MARKET RETURNS

Year-to-date (1/1/08-08/22/08)

Dow Jones Indus Avg.	-12.34%
S&P 500	-12.00%
NASDAQ	-8.96%
Russell 2000	-3.71%
MSCI World Index	-16.44%
DJ STOXX Europe 600	-22.16%

Year-to-date (1/1/08-08/21/08)

90 Day T-Bill	1.61%
2-Year Treasury	3.23%
10-Year Treasury	3.94%
ML High Yield Index	-2.83%
JPM EMBI Global Diversified	1.02%
JP Morgan Global Hedged	2.44%

RECAP OF THE WEEK'S ECONOMIC RELEASES

August 19

Pending Home Sales Index -- The National Association of Homebuilders' housing market index held at its record low of 16 in August.

August 20

Producer Price Index -- The headline producer price index rose 1.2% in July, much more than economists expected. Core PPI, which excludes food and energy, also jumped unexpectedly higher, up 0.7%.

Housing starts – Starts plummeted 11% in July to 965,000 units at an annual rate, the lowest since March 1991. Multi-family starts also fell, dropping 24% after jumping 41% in June. Starts of single-family homes are down 65% from their January 2006 peak.

August 21 *Leading Indicators* -- The index of leading economic indicators plunged 0.7% in July, the biggest one-month drop in about a year. The steep drop in building permits during July explains much of the decline.

OVERVIEW

- Federal Reserve Chairman Ben Bernanke characterized the current period as “one of the most challenging economic and policy environments in memory,” in a speech at the Fed’s annual symposium in Jackson Hole, Wyoming. While this year’s symposium focuses on “Reducing Systemic Risk” – a theme that has pushed to the forefront given the credit problems over the last 12 months – Bernanke kicked-off the event with a keynote address in which he defended the Fed’s actions over the last year. Specifically, Bernanke stated: “In view of the weakening outlook and the downside risks to growth, the Federal Open Market Committee (FOMC) has maintained a relatively low target for the federal funds rate despite an increase in inflationary pressures.” But, probably the most important theme is a more general one: whereas a year ago the Fed Chairman was focused on the housing and mortgage market problems, today the speech and the annual symposium focuses a more looming problem: concerns over the entire financial system. These topics will take several quarters if not years to play out in terms of changes to the regulatory and financial system “infrastructure.” Meanwhile, Fed policy is likely to remain accommodative.

- Data released this week suggest a second-half recovery for the US economy is unlikely, bolstering the case for a low federal funds rate for the foreseeable future. The index of leading indicators posted its largest decline in almost a year, dropping 0.7%. The index is now down 3.3% versus a year ago—its largest one-year decline since the 2001 recession. One of the key components driving the decline in July was building permits. A leading indicator of home construction activity, permits subtracted half a percentage point from the index during the month as permit activity in the US dropped nearly 20% in the month of July.

US MARKETS:

TREASURIES

- Treasury yields continued to consolidate this week as commodities rallied and fears related to financial institutions percolated. Commodities finally found some traction this week after a severe sell-off, providing at least a temporary floor for inflation expectations. However, there was a flight to quality bid in the market stemming from agency and financial institution liquidity strains, resulting in a resiliency in yields. After testing recent wides in yields earlier in the week, agency spreads on senior debt ratcheted back in to end the week.

LARGE-CAP EQUITIES

- Equity markets sold-off this week due to concerns with financial companies and signs of higher inflation. Trading activity continued to be relatively light. The S&P 500 and Russell 1000 indexes both finished down about 1% for the week. Large-cap stocks outperformed small-cap stocks. In terms of style, large-cap growth stocks outperformed large-cap value stocks. The best performing sector was energy and the worst performing sector was financials. Companies in the news this week included mortgage companies Fannie Mae and Freddie Mac. Shares of both sold off over 40% during the week as investors speculated a government bailout will be necessary due to further credit losses. In other news, shares of Lehman Brothers rose 10% after the Korea Development Bank said it was considering a purchase of Lehman Brothers.

CORPORATE BONDS

- Investment grade primary activity (new issuance) was almost non-existent with only few deals pricing early in the week. Issuers are skittish to bring deals in an environment where anxieties surrounding GSE’s and financial credits have kept most investors close to home. Throughout the week there were several earnings downgrades from analysts and suggested write-downs that weighed down on the sector. Late week rumors surrounding Korea Development Bank possibly acquiring Lehman gave some respite to broker spreads, which inturn gave a much needed boost to the overall market.

- Investment grade corporate spreads widened throughout most of the week as the financial sector caused fear amongst market participants. Liquidity continues to be a major obstacle, most likely because most are looking to scale down risk. Until we have more major players adding risk and Wall Street returns from summer vacation, liquidity will remain challenging for the foreseeable future. The Lehman Credit Index Option-Adjusted Spread (OAS) finished the week at +270 basis points, nine basis points wider. Telecom/cable/media widened by seven; utilities tightened by two; industrials widened by four; and financials widened by twenty basis points led by brokers.

MORTGAGE-BACKED SECURITIES

- The agency mortgage market showed slight improvement over the past week. However the focus of the mortgage market was not so much on performance of the sector as much as the probable bailout plans for the thinly-capitalized mortgage institutions (FNMA and FHLMC). The market is coming to terms with the fact that it is increasingly likely that the mortgage agencies will need to call on the support of the Treasury (provide liquidity, purchase debt/equity, inject capital) that was recently granted to them in the just passed housing relief act. The potential for full nationalization of the agencies also received plenty of coverage over the past week. Until there is more clarity as to the role the government might play in supporting the agencies, the mortgage market will waffle around at close to the historical wides in yield spread. With increased clarity and the likelihood of dramatically lower supply of mortgages through the rest of 2008, the prospects for the performance of the sector should brighten. Presently the current coupon mortgage trades at 6.0%--more than 2.0% above Treasury levels.

MUNICIPAL BONDS

- Municipal bonds were thinly traded this week, with slightly lower yields across the yield curve producing gains. Top-rated general obligations maturing in two years yielded 2.03% on Friday's open, lower by one basis point from the start of the week. Ten-year AAA bonds yielded 3.59% lower by 5 basis points, and 30 year AAAs were at 4.70%, higher by 4 from last week.

- The biggest deal this week was the $917 million AA- rated Banner Health issue, with serial maturities from 1 to 30 years. The 30-year maturity bond yielded 5.67% on issue, 101 basis points higher than the 30-year AAA benchmark. Another deal of note was the New York State Thruway Highway and Bridge Trust Fund, which sold $659 million in bonds on Thursday. Rated AA by S&P, the longest maturity of the deal in 2028 priced to yield 4.64%, +25 basis points to the benchmark.

HIGH-YIELD BONDS

- The summer quiet streak continued in the high yield market this week as there was no new issuance and light secondary trading volume. However, the spread of the broad market managed to leak almost 20 basis points wider on equity weakness spawned by reemerging concerns over the GSE's and other financial institutions. For the week the total return on Merrill Lynch US High Yield Constrained Index was -40 basis points going into Friday. Although much economic data will be reported next week, we don't expect activity to pick up significantly until after the Labor Day weekend.

INTERNATIONAL MARKETS:

WESTERN EUROPEAN EQUITIES

- Western Europe Stocks in Western Europe lost ground over the past week. The sectors with the worst performance were travel (-4.4%) and retail (-3.7%). German based tourism company TUI (-5.4%) reported negative Q2 2008 results mostly due to TUI's poorly performing airline business despite the improved sales and earning of subsidiary Hapag-Lloyed. Shares of Arcandor (-17.7%) have reached an all time low. The German retailer issued a profit warning last week and reported poor quarterly results.

Among the sectors that did well were basic resources (+6.7%) and oil & gas (+3.4%). International mining group Rio Tinto signed a pact with India's state-run miner NMDC to establish a 50/50 joint venture in order to secure control of global mineral assets. In addition, Rio Tinto is in process of closing a deal with Indonesia to develop a major nickel concession.

- Among the more notable euro zone macroeconomic news was the decline of French Manufacturing Confidence reaching its lowest level (92) in five years as of July due to a stronger euro and rising oil prices. Europe's manufacturing and service industries contracted for a third month in August as consumers and businesses reeled from July's record oil prices. The German ZEW survey improved to -55.5 points in August from -63.9 points in July. The August current condition index fell to -9.2 points from 17.0 points.

EASTERN EUROPEAN EQUITIES

- The CECE index of equities traded in Central Europe (Czech Republic, Hungary, and Poland) gained 1.0% this week, while the Russian stock index RTS finished the week down by 4.7%. In Central Europe, Czech coal mining company New World Resources gained the most ground (+12.2%), followed by Polish gas company PGN (+4.4%), and Hungarian telecommunications provider Magyar Telekom (+2.9%). Shares of New World Resources increased after the Czech and Polish governments signed a treaty on cross-border mining, which allows companies from both countries to operate in the border area. In addition, China's decision to raise the export tariff on coke from 25% to 40% benefited the Czech mining company. PGN went up after it was announced that the Polish natural gas monopoly will meet with state-run transmission network operator, Gaz-System, to discuss sharing spending on a planned €400 million liquefied natural gas terminal. Among the stocks that did not fare well, Polish biotech company Bioton (-7.1%) led the way, followed by Polish broadcaster TVN (-6.7%), and Hungarian pharmaceutical company Richter Gedeon (-5.3%). Bioton's stock slumped after a brokerage cut its share-price projection by 68%, citing 'poor' second-quarter results. TVN suffered after the shares were downgraded from "buy" to "hold".

- In Russia, coal mining company Raspadskaya (-13.1%) sold off the most, followed by gas company Gazprom (-10.4%), and Novolipetsk Steel (-10.1%). Raspadskaya shares dropped because deadlines for coal exports via Ukrainian ports are threatened by an increase in railcar 'poaching.' Gazprom went down after natural gas prices declined 3.1% at an auction on August 20th. In addition, the company announced that it may raise its investment budget for 2008 by about 25%. Novolipetsk Steel sold off after a competing company announced that domestic steel prices will fall as much as 7% in the next two months after raw material suppliers were ordered to cut prices. Among the leaders of the past week were business management company Sistema (+4.4%), followed by fertilizer manufacturer Silvinit (+3.5%), and Rostelecom (+1.3%). Sistema gained after a Russian investment bank told investors that the shares have 'significant hidden value' because they are trading at less than the price of Sistema's stake in OAO Mobile TeleSystems alone, disregarding the value of the company's other assets. Silvinit's shares got a boost after releasing its first half financials, which showed a 350% rise in net income, far exceeding expectations.

GLOBAL BONDS AND CURRENCIES

- Major government bond markets handed back some of the previous week's gains as a surge in oil prices fed investors' concerns about inflation. In Europe, inflation concerns where amplified by some stronger than expected German wholesale price data and an unanticipated improvement in manufacturing and service sector sentiment data. Two-year Bund yields closed the week about 14 basis points higher, while 10-year yields rose seven basis points. In the UK, although the minutes of the Bank of England's August Monetary Policy Committee meeting echoed the softer tone of last week's *Inflation Report*, and second quarter GDP growth was revised down from 0.1% to 0.0%, Gilts took their main lead from events abroad and yields ended the week several basis points higher across the curve. The Bank of Japan left rates unchanged at its meeting this week as expected and downgraded its assessment of the economy for the second successive month. This, combined with losses on the Nikkei provided relative support for Japanese government bonds, with 10-year yields closing the week two basis points lower.

- In currency markets, the US dollar hit a six-month high against the euro mid-week after US producer price data exceeded expectations, fuelling speculation that the next move in US rates will be up. However, the euro managed to recoup its lost ground to close the week slightly firm after concerns about the financial sector hit the greenback later in the week. The dollar also ended slightly lower against the yen as falling Japanese equity prices increased investors' risk aversion, reducing their appetite for yen carry trades. Against sterling, the dollar was up slightly as the downward revision to second quarter growth and the prospect of eventual UK rate cuts undermined the pound.

EMERGING-MARKET BONDS

- Emerging market dollar-pay debt spreads widened by another four basis points in a fairly directionless week where commodities and stronger equity markets were slightly supportive but didn't really feed through into emerging markets debt. At the beginning of the week, Banco de Mexico announced a 25 basis point increase in its target rate, to 8.25%. Inflation is still well above the 3% medium-term target and the central bank said that the pass-through from commodity prices to final products has yet to be completed, and that the monetary authority would make it a priority to prevent "second-round inflationary effects".

- In Poland, inflation stabilized at 2.2% year-over-year in July, below headline inflation of 4.8% year-on-year. However, net core inflation rose to 3.5% year-on-year from 3.4% in June. The central bank also released the monetary policy committee meeting minutes, showing concerns that further rate hikes could additionally strengthen the zloty and lead to a significant economic slowdown, especially in the face of the global slowdown. Russia's industrial production increased by just 3.2% year-on-year in July 2008 compared to 10.3% year-over-year in July 2007. As a result, growth in Russia's industrial output from January through July 2008 amounted to 5.4%.

FACTORS SHAPING THE MARKET NEXT WEEK

- Next week the US economic data calendar includes the report on gross domestic product (second quarter), the Case-Shiller home price index for June and data on durable goods.

- Next week's calendar for Western Europe includes the release of Spain's Industrial Prices Index and Germany's IFO Business Climate Index on Monday. On Thursday, Germany and France will publish numbers about their employment situation, and France will announce Q2 GDP results. The UK will release Consumer Confidence statistics on Friday and Italy will announce its preliminary Consumer Prices. On Friday, the euro zone unemployment rate will also be published.

- Eastern Europe's week kicks off with the release of Polish July unemployment rates on Tuesday. On Thursday, Hungary is scheduled to publish its unemployment rate for July as well.

NEXT WEEK'S US ECONOMIC RELEASES

August 26 *Case-Shiller Home Prices*

August 27 *Durable Goods*

August 28 *Gross Domestic Product, Second Quarter*

August 29 *Personal Income*