• With everyone worried about Halloween costumes and parties, and waiting for this week's market excitement, it comes as no surprise that markets drifted listlessly as October came to a close. Equities finished generally flat and the Treasury yield curve steepened by 7 bps with the two-year yield settling at 0.34%. However, for the month, equities outperformed bonds handily despite the growing suspicion of Fed Treasury purchases on the horizon. The data was mixed, with new and existing home sales beating expectations in sign of stabilization in that market and durable goods orders ex-transportation showing some weakness. The preliminary GDP report for the third quarter came in at 2%, in line with expectations and up from the final Q2 growth rate of 1.6%. Chicago PMI showed strong growth in new orders and employment, while consumer sentiment was weaker than expected. The uptrend has certainly plateaued in recent weeks, making week's new information all the more pivotal to the market's next move.

• It is rare to see such a confluence of events that can so precipitously move a market, but the week ahead provides just such an occasion. The Fed, an election, and a jobs report in the same week--this is certainly a time to pay attention to the action. Most players are looking for a market response and direction that will carry us through the end of the year and provide greater medium-term clarity. The week starts out gradually with income and spending data for the consumer, along with the ISM Manufacturing report and Constructions Spending. The two-day FOMC meeting begins on Tuesday, sandwiching itself around the mid-term elections, where Republicans are slated to reclaim a majority in the House and potentially even out the Senate. Many governor races are also close at this point, as joblessness and sluggish growth leave most voters fatigued with Washington and state capitols. Wednesday afternoon brings the FOMC policy statement, where the board is expected to release guidance on a second quantitative easing. The expectation is for an initial Treasury purchase schedule of $500-750 billion, a strategy that accelerates the flow and bolsters the supply of money for the economy to utilize. We also see initial job data from ADP and Challenger, along with the ISM services report to gauge the state of this majority sector. Friday morning we have the nonfarm payrolls report, where economists expect a 60k bump in jobs for October and an unemployment rate of 9.6%. The last two weekly joblessness reports have shown fewer jobs lost than expected, so many will expect an upside surprise on the order of 100k jobs. If we were to see the modest quantitative easing, a Republican majority take the House, and a strong jobs report, look for stocks and rates to take off higher. If the Fed QE2 package is bigger than expected, rates could fall as the market will jump into Treasuries before the Fed starts buying. If the Fed decides not to initiate QE2, rates across the curve would likely skyrocket on the order of 25-50 bps.

Index Rates	Last	Week Ago	Month Ago	Year Ago
1-mo LIBOR	0.25%	0.26%	0.26%	0.24%
3-mo LIBOR	0.29%	0.29%	0.29%	0.28%
6-mo LIBOR	0.45%	0.45%	0.46%	0.56%
12-mo LIBOR	0.76%	0.77%	0.78%	1.20%
Fed Funds Target	0.25%	0.25%	0.25%	0.25%
Prime Rate	3.25%	3.25%	3.25%	3.25%
SIFMA Muni Swap Index	Call	0.30%	0.27%	0.26%

Treasury Rates	Last	Week Ago	Month Ago	Year Ago
2-yr Treasury	0.34%	0.36%	0.43%	0.89%
3-yr Treasury	0.50%	0.53%	0.65%	1.39%
5-yr Treasury	1.17%	1.15%	1.28%	2.31%
7-yr Treasury	1.89%	1.86%	1.88%	2.97%
10-yr Treasury	2.60%	2.56%	2.51%	3.39%
30-yr Treasury	3.98%	3.93%	3.69%	4.23%

Taxable Swap Rates	Last	Week Ago	Month Ago	Year Ago
2-yr LIBOR	0.43%	0.45%	0.51%	1.15%
3-yr LIBOR	0.65%	0.67%	0.76%	1.73%
5-yr LIBOR	1.33%	1.31%	1.39%	2.54%
7-yr LIBOR	1.97%	1.92%	1.93%	3.03%
10-yr LIBOR	2.58%	2.51%	2.44%	3.44%

Tax-Exempt Swap Rates	Last	Week Ago	Month Ago	Year Ago
2-yr SIFMA	0.47%	0.50%	0.56%	1.07%
3-yr SIFMA	0.65%	0.68%	0.77%	1.54%
5-yr SIFMA	1.22%	1.23%	1.31%	2.16%
7-yr SIFMA	1.74%	1.75%	1.77%	2.54%
10-yr SIFMA	2.28%	2.26%	2.22%	2.89%

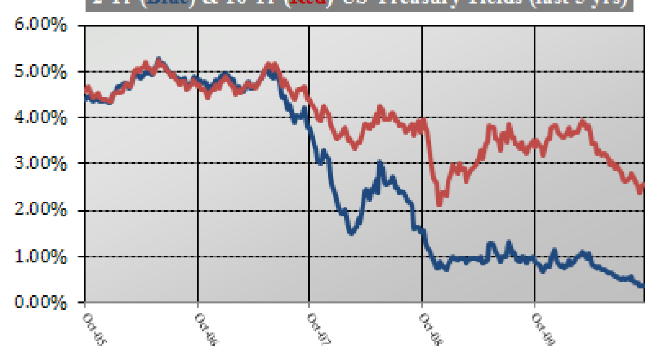
Rate Caps (cost in bps)	Strike = 4.00%	Strike = 5.00%
3-yr LIBOR Cap	23	21
5-yr LIBOR Cap	92	66
7-yr LIBOR Cap	250	171
10-yr LIBOR Cap	568	391

Fwd Implied 3mL Rate	Last
Dec. 10	0.33%
Dec. 11	0.53%
Dec. 12	1.01%
Dec. 13	1.86%

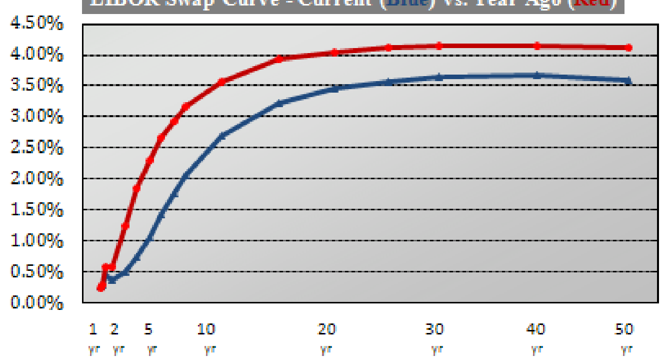
Conventions

LIBOR swaps use 1-month LIBOR, monthly payments, act/360 day count. SIFMA swaps reset weekly and pay monthly, act/act day count. All else equal, amortizing swaps will have lower rates. For % of LIBOR swaps, multiply the % used by the taxable swap rate.

2 Yr (Blue) & 10 Yr (Red) US Treasury Yields (last 5 yrs)



LIBOR Swap Curve - Current (Blue) vs. Year Ago (Red)



Cardea Partners is a firm of seasoned professionals dedicated to bringing transparency of execution and education to end-users in the derivatives marketplace. Specializing in interest rate risk management and strategy and debt portfolio analysis, we are pleased to provide our weekly commentary on the US rates market and an economic perspective for the benefit of our client organizations. We love to discuss the markets and keep our clients ahead of the (really steep) curve--please let us know how we can help your organization identify and manage its financial risks.

CARDEA PARTNERS

Warm regards,

Ryan Kozak, Christopher Hunt,
Joseph Momich, and Rex Evans

Derivative and Debt Advisory Services

Cleveland, OH (440-892-8000)
San Francisco, CA (925-988-0703)
Miami, FL (954-642-1270)

cardeapartners.com