Research

Middle Market Bond Dealer Report

The Securities Industry and Financial Markets Association[1] is pleased to report the results of its quarterly *Middle Market Bond Dealer Report*. Based on publicly available information, the report analyzes and presents aggregate information and trends related to bond issuance in which one or more regional securities firms—non-primary dealers—are the lead underwriter or "book runner" on the deal. The report's coverage focuses on long-term transactions—those in which the stated original maturity at issuance is greater than thirteen months—and covers the range of fixed-income market sectors, including municipal bonds, corporate bonds, federal agency securities and asset-backed and private-label mortgage-backed securities.

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Regional Firm-Led Underwriting Surges in 2006 Led by Corporate and Securitized Sectors; Municipal and Agency Volume Lower

Regional firm-managed issuance in the municipal, corporate, federal agency, and structured finance market sectors surged to $520.1 billion in 2006, 61.7 percent above the $321.6 billion a year ago. The year-over-year increase was led by the securitized finance sector with 2006 volume nearly triple that of 2005 and the corporate bond sector in which volume also increased substantially. The regional dealer underwriting share increased to more than 9.7 percent of total U.S. issuance volume, compared to 6.5 percent in 2005.

Issuance growth has been supported by beneficial financial market conditions. Strong credit quality, historically low default rates, investor demand for credit products, and ample liquidity have combined to create the favorable conditions and tight credit spreads, a trend that persisted throughout 2006. The Federal Reserve's completion of its monetary tightening phase in August further spurred the credit markets in the fourth quarter. Recent economic data suggest GDP growth surpassing the earlier consensus below-trend growth expectations for 2007, which bodes well for continued elevated issuance levels in the credit markets over the next year.

Strong liquidity and investor demand are keeping market conditions at a cyclical peak. Later in the year, credit and pricing conditions are likely to fall back, perhaps leading to reduced investor risk tolerance should liquidity conditions moderate. Rating agencies are projecting gradually rising default rates, which should still remain well below long-term averages. In addition, shareholder-favoring strategies, increased leverage and the pace of LBO activity could pose event and single name risk that would affect pricing. The effect of the recently reported increase in subprime mortgage default and delinquency rates appears to be contained within that sector as sustained economic and employment growth underpins a continued positive operating environment.

Regional firm-led issuance for full-year 2007 should approach 2006 levels depending on the direction of benchmark yields, credit quality trends and economic growth. The consensus view is that the housing sector correction will conclude this year, stabilizing the mortgage-affected sectors. The municipal bond sector should continue to see refunding levels below the peak year of 2005 absent a reduction in interest rate levels, but new municipal bond issuance is expected to continue to grow. Corporate issuance should remain at historically high levels, driven by M&A and LBO deal volume.

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1 The Securities Industry and Financial Markets Association brings together the shared interests of more than 650 securities firms, banks and asset managers. SIFMA's mission is to promote policies and practices that work to expand and perfect markets, foster the development of new products and services and create efficiencies for member firms, while preserving and enhancing the public's trust and confidence in the markets and the industry. SIFMA works to represent its members' interests locally and globally. It has offices in New York, Washington D.C., and London and its associated firm, the Asia Securities Industry and Financial Market Association, is based in Hong Kong.

Regional Municipal Underwriting Volume Slows in 2006 Due to Decline in Refunding Volume

Despite a strong fourth quarter, regional firm-led municipal volume declined in 2006 to $126.5 billion, 7.2 percent less than 2005 volume. On a linked quarter basis, issuance increased in the fourth quarter to $37.7 billion, 24.4 percent higher than the third quarter and 19.7 percent higher than the same period a year ago. The fourth quarter was also the only quarter in 2006 in which the volume exceeded that of the same quarter in 2005. The lower full-year issuance level is attributable to reduced refunding volumes, which were partially offset by growth in new money municipal bond issuance.

Both competitive and negotiated municipal underwriting volumes were lower in 2006 than in the previous year. Regional firm-led negotiated issuance declined 5.5 percent, to $106.2 billion, down from $112.4 billion in 2005. Year over year, competitive sales volume in 2006 also declined, reaching $18.7 billion, down 17.6 percent from $22.7 billion in 2005.

The Midwest ranked first among geographic regions and accounted for more than 26.8 percent of regional firm-led underwriting volume, with the Southwest ranking second and the Southeast a close third. The top issuing states were Texas and California, accounting for 20.7 percent of regional firm-led underwriting through the fourth quarter.

In general, municipal market conditions benefited from historically low benchmark yields and tight tax-adjusted credit spreads Nearly sixty percent of issuance volume had the highest Moody's rating, Aaa, with 14.5 percent by volume rated Aa or below, and 26.2 percent unrated. Credit enhancement provided support for 67.4 percent of total issuance by dollar volume. Education continues to be the largest use-of-proceeds sector, accounting for 37.2 percent of regional firm-led municipal volume in 2006.

Corporate Bond Underwriting More than Doubles in 2006

Regional firm-led corporate underwriting volume totaled $69.1 billion in 2006, more than double the $28.3 billion in 2005. Fourth quarter issuance was $21.9 billion, and more than triple the volume in the fourth quarter of 2005, 68.5 percent higher than the third quarter. Regional-led corporate issuance accounted for 6.6 percent of total U.S. corporate issuance in the first nine months of the year, a increase from 3.8 percent in the first nine months in 2005.

Shareholder friendly strategies, balance sheet releveraging, and business capital spending growth continued to be the drivers of corporate issuance growth. Issuance is likely to remain strong during 2007 with debt financed corporate acquisition activity, including M&A and LBO's, likely affecting corporate issuance volume.

U.S.-based corporations accounted for 65.9 percent of regional-led corporate issuance in 2006. Among states, North Carolina-based corporations continued to rank first by a wide margin with 35.9 percent of issuance volume during the year followed by Texas-based corporations at 6.7 percent market share. Financial services remain the dominant regional-led issuance sector in 2006, accounting for 75.4 percent of total issuance.

Securitized Underwriting Strong Despite Housing Slowdown; Agency Issuance Declines

Regional firm underwriting of securitized debt increased to $188.6 billion in the 2006, nearly triple the $74.4 billion in 2005. The pace, though, moderated in the fourth quarter to $45.0 billion, an 8.2 percent decline from the third quarter but more than 70.4 percent higher than in the fourth quarter in 2005. Despite the housing market slowdown, regional firm-led residential mortgage-backed securities (RMBS) issuance reached $71.0 billion, slightly less than a third of all regional-led securitized issuance. Strengthened underwriting standards following recent credit quality weaknesses and rising delinquency levels found in the subprime sector are likely to affect subprime mortgage-backed securitization volume. Commercial mortgage-backed securities (CMBS) issuance was the second largest issuing sector and totaled $34.5 billion in 2006, nearly three times the volume in 2005, as commercial real estate market conditions remained strong.

Federal agency issuance managed by regional firms rose to $74.9 billion in 2006, a 2.7 percent increase over 2005. Year-over-year growth in agency issuance volume can be attributed to the housing government sponsored entities near completion of capital management and portfolio restructuring initiatives and conforming mortgage origination growth. SIFMA's primary dealer survey projects total agency issuance growth in the first quarter in 2007, undoubtedly influenced by mortgage originations picking up as the housing correction progresses and conditions stabilize.

The Middle Market Report is based on new issue data provided by Thomson Financial, a part of Thomson Corporation (www.thomson.com) and a leading provider of information and technology solutions to the financial industry.

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2006:Q4 Long-Term Muncipal Issuance
By Geographic Region

Southeast	$ Bil	# Issues	% of Tot. Vol.*
Southeast	**25,852.4**	**1,283**	**20.4%**
Florida	6,054.6	221	23.4%
North Carolina	2,957.9	76	11.4%
Alabama	2,721.3	158	10.5%
Louisiana	2,441.7	123	9.4%
Georgia	2,352.3	121	9.1%
Tennessee	2,207.9	121	8.5%
South Carolina	2,058.8	83	8.0%
Virginia	1,878.3	65	7.3%
Kentucky	1,190.2	186	4.6%
Mississippi	930.6	93	3.6%
Puerto Rico	656.4	4	2.5%
West Virginia	402.4	32	1.6%

Southwest	$ Bil	# Issues	% of Tot. Vol.*
Southwest	**28,551.6**	**2,005**	**22.6%**
Texas	13,068.2	780	45.8%
Colorado	5,092.8	258	17.8%
Arizona	3,148.3	154	11.0%
Kansas	2,004.6	266	7.0%
Arkansas	1,577.6	172	5.5%
New Mexico	1,513.3	72	5.3%
Oklahoma	1,494.5	247	5.2%
Utah	652.3	56	2.3%

Mid West	$ Bil	# Issues	% of Tot. Vol.*
Mid West	**33,900.5**	**3,870**	**26.8%**
Illinois	6,573.7	672	19.4%
Ohio	6,167.0	435	18.2%
Michigan	4,547.2	348	13.4%
Indiana	4,042.9	280	11.9%
Missouri	3,512.4	343	10.4%
Minnesota	3,234.6	621	9.5%
Wisconsin	2,425.9	492	7.2%
Iowa	1,713.1	323	5.1%
Nebraska	1,131.1	255	3.3%
North Dakota	347.3	73	1.0%
South Dakota	205.3	28	0.6%

Far West	$ Bil	# Issues	% of Tot. Vol.*
Far West	**18,422.6**	**911**	**14.6%**
California	13,067.1	588	70.9%
Washington	2,332.7	147	12.7%
Oregon	815.0	58	4.4%
Nevada	622.1	28	3.4%
Idaho	440.5	29	2.4%
Montana	400.6	43	2.2%
Alaska	340.1	10	1.8%
Wyoming	244.7	6	1.3%
Hawaii	96.6	1	0.5%
Guam	63.2	1	0.3%

Northeast	$ Bil	# Issues	% of Tot. Vol.*
Northeast	**19,760.4**	**1,473**	**15.6%**
Pennsylvania	6,950.0	442	35.2%
New York	4,541.3	501	23.0%
New Jersey	2,519.4	209	12.7%
Maryland	1,472.9	40	7.5%
Massachusetts	1,419.0	140	7.2%
Connecticut	1,160.8	55	5.9%
Delaware	569.1	13	2.9%
D. of Columbia	420.3	9	2.1%
New Hampshire	403.7	28	2.0%
Maine	131.0	15	0.7%
Rhode Island	105.5	15	0.5%
Vermont	67.4	6	0.3%

Total: $88,091.8 Million **Total Number of Issues 6,763**

* Regional percentages represent the portion of total U.S. regional dealers accounted for by that region. State percentages represent the portion of total issuance in the region.

Source: Thomson Financial

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2006:Q4 Long-Term Municipal Top 25 Issuers

	Issuer	$ Mil	# Issues
1	Detroit City-Michigan	1,168.8	4
2	Illinois Finance Authority	878.5	53
3	Ohio	845.7	11
4	New Mexico Mortgage Fin Auth	721.5	12
5	South Carolina Student Loan Corp	682.0	2
6	Massachusetts Dev Finance Agcy	651.2	25
7	NYC Municipal Water Finance Auth	650.4	2
8	Indianapolis Loc Pub Imp Bond Bk	590.1	7
9	North Carolina St Ed Assist Auth	570.0	2
10	Wisconsin Health and Ed Fin Auth	546.1	26
11	Connecticut	523.0	4
12	California Statewide Comm Dev Au	508.1	34
13	Washington State Hsg Fin Comm	505.5	26
14	Hamilton Co (Cincinnati) SD	501.3	2
15	Pennsylvania St Pub Sch Bldg Au	492.9	12
16	Louisiana Housing Finance Agcy	480.2	13
17	Denton Co (Lewisville) ISD	478.6	3
18	NYS Dorm Authority	473.6	10
19	North Carolina Med Care Commiss	472.0	7
20	Louisiana Public Facilities Auth	451.5	12
21	Los Angeles Municipal Imp Corp	448.6	1
22	Chicago City-Illinois	439.1	13
23	Illinois	425.0	2
24	Puerto Rico Hsg Finance Auth	411.6	2
25	Greater Chicago Metro Wtr Rec Dt	397.4	1
	Total Top 25	**14,312.7**	**286**
	Industry Total	**126,487.5**	**9,546**

Source: Thomson Financial

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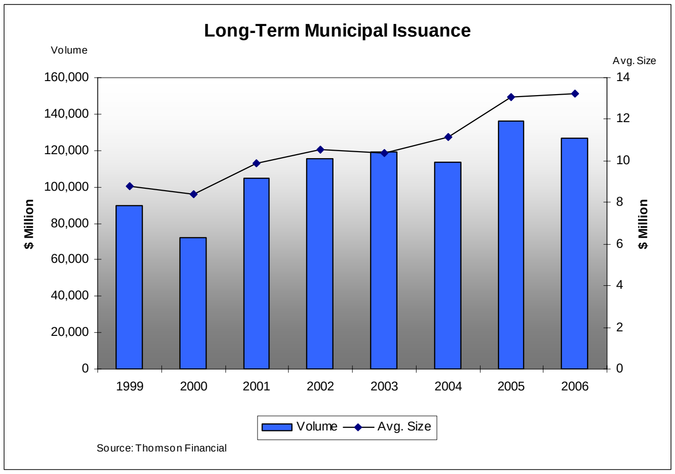

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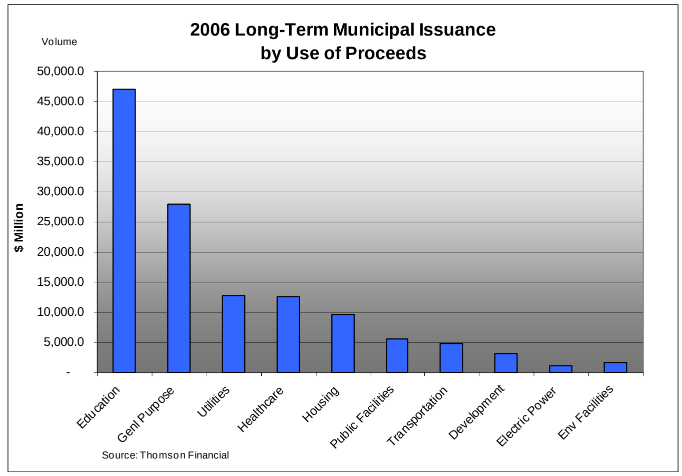

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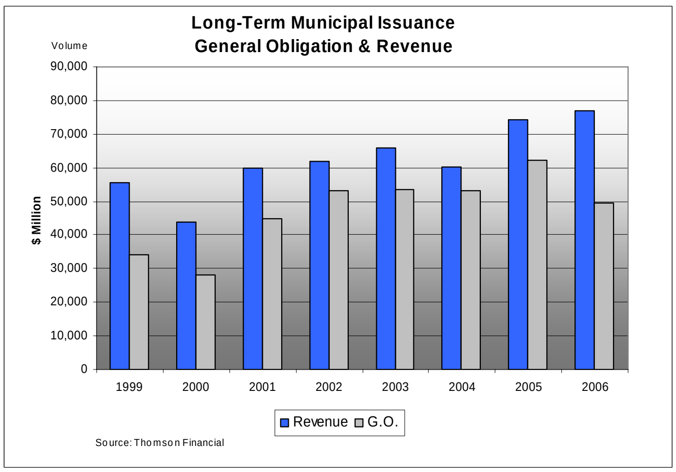

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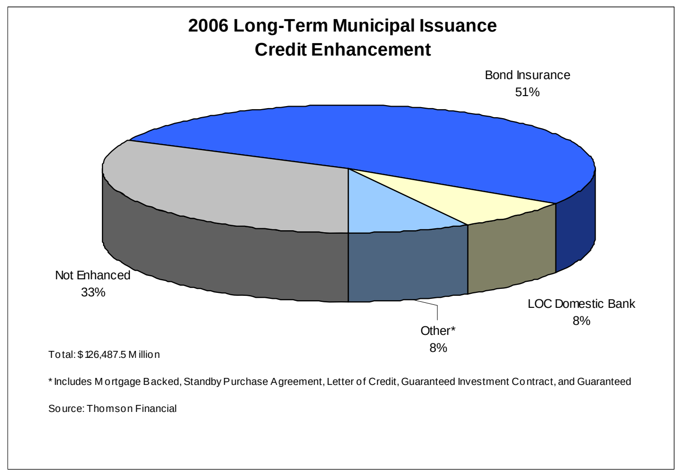

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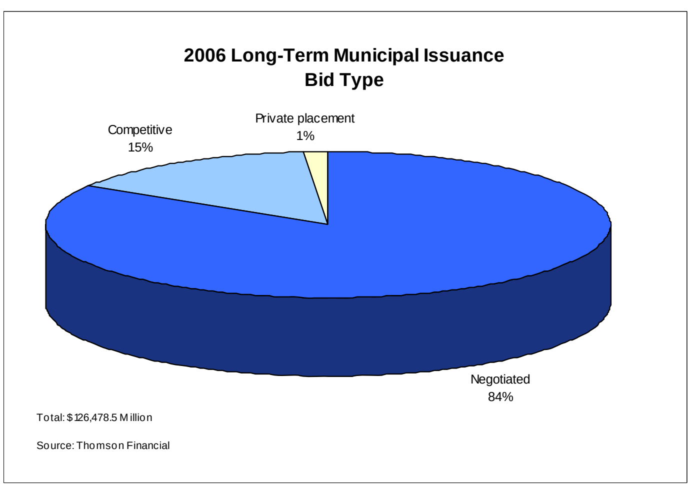

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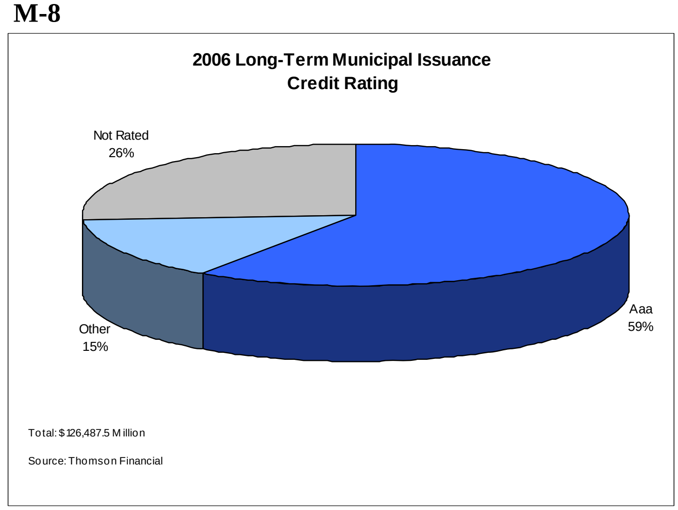

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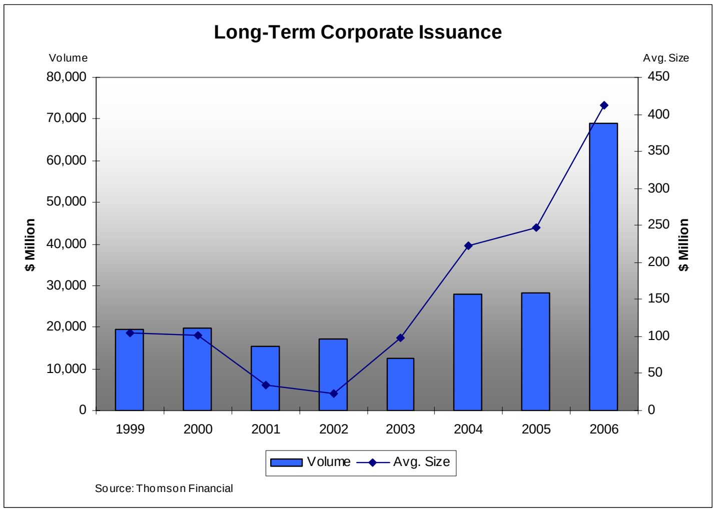

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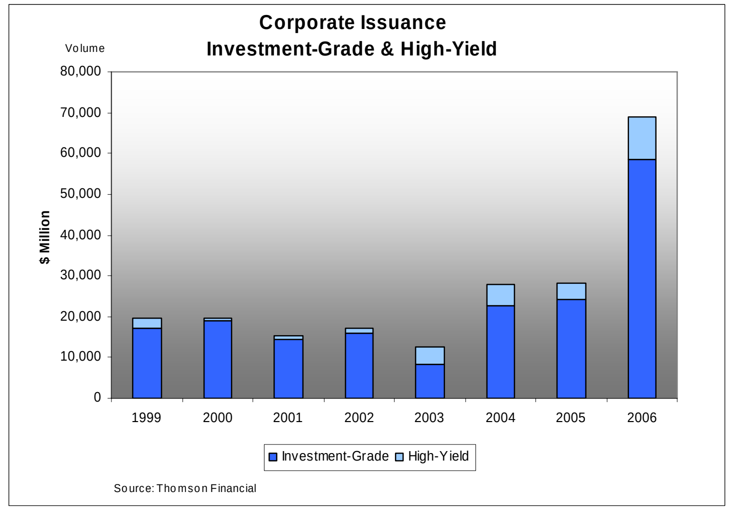

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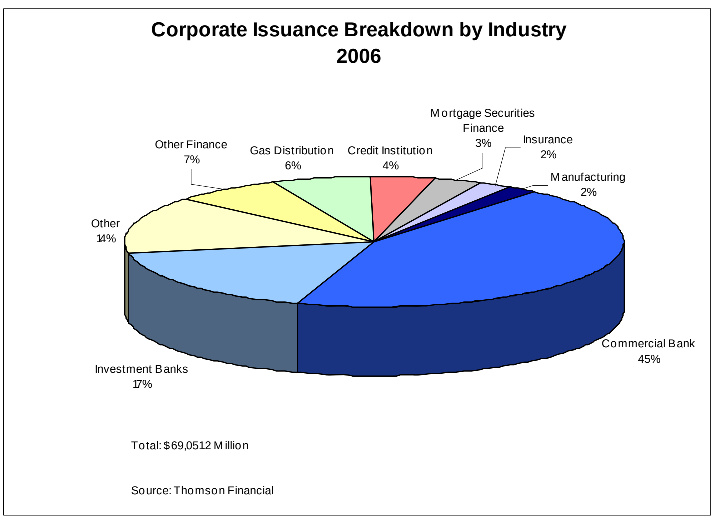

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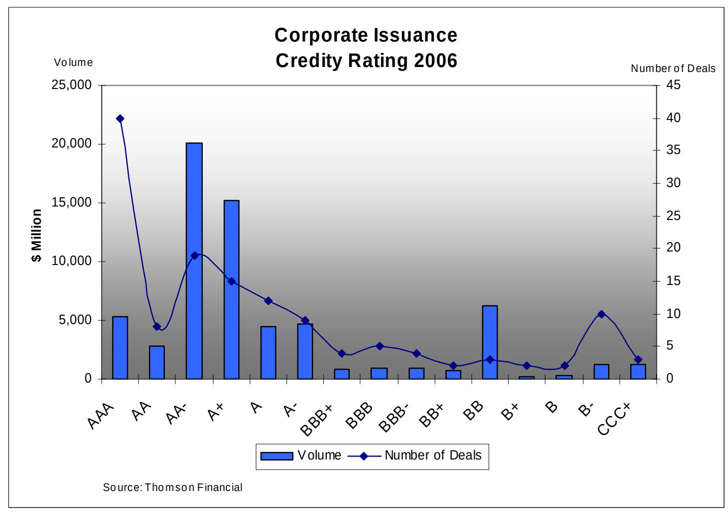
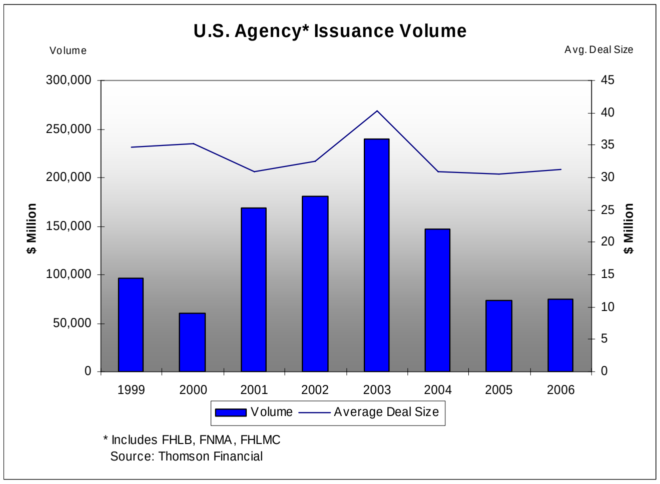


C-5 Issuance by State 2006:Q4

	State	$ Mil	# Issues		State	$ Mil	# Issues
1	North Carolina	24,820.0	16	15	Georgia	680.0	5
2	Foreign	23,556.0	58	16	New York	515.8	8
3	Texas	4,634.0	4	17	Massachusetts	500.0	2
4	Ohio	2,115.0	7	18	Illinois	340.0	3
5	Virginia	1,612.5	5	19	Delaware	310.0	4
6	Connecticut	1,510.0	5	20	Maryland	275.0	3
7	Minnesota	1,048.0	2	21	Rhode Island	193.9	1
8	Nevada	960.0	1	22	Michigan	150.0	2
9	Unknown	925.0	3	23	Utah	145.0	1
10	Tennessee	875.0	5	24	West Virginia	125.0	1
11	Idaho	850.0	3	24	Washington	125.0	1
12	Wisconsin	755.0	4				
13	New Jersey	725.0	2		Total Top 25	68,455.2	151
14	Pennsylvania	710.0	5		Industry Total	69,051.2	160

Source: Thomson Financial

A-1



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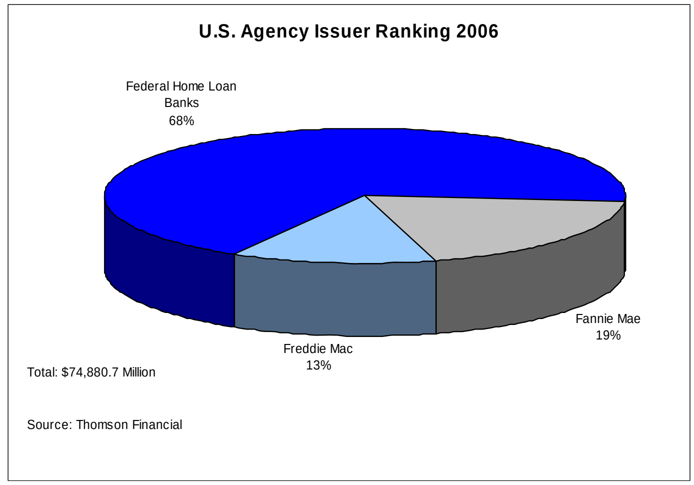

Regional Report –Securitized Markets

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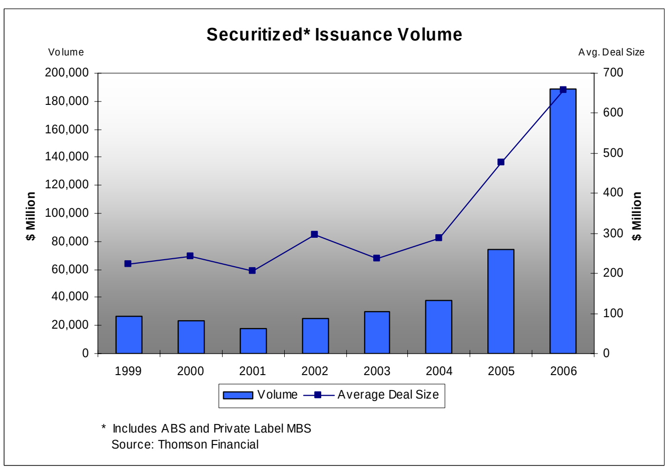

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