MORTGAGES/AGENCIES-Sectors cheapen as Treasuries decline
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NEW YORK, Aug 18 (Reuters) - Yield spreads on Fannie Mae and Freddie Mac U.S. mortgage-backed securities and "federal agency" debt widened against Treasuries on Tuesday as Treasuries lost their safe-haven appeal.

U.S. Treasury debt prices dipped, surrendering some of Monday's sharp gains as stocks rose, sapping the safe-haven allure of government debt. For details, double-click on [ID:nN18432636]

While the regular and robust buying by the U.S. government has been the biggest positive for agency MBS and agency debt securities, it leaves them vulnerable to cheapening when the central bank eventually pulls back. It has also inflated prices to levels that have made many investors cautious about securities from government-sponsored enterprises.

"U.S. agency MBS are a decent midterm holding," said Pamela **Turner**, director of research at **Xavier Capital** Management in Largo, Maryland.

"Yes, U.S. agency MBS are very expensive," she said.

Turner, who also teaches finance at Howard University, said option adjusted spreads to Treasuries were at 173 basis points at the end of October 2008, which was the height of the financial crisis, and now option adjusted spreads are less than 25 basis points.

U.S. agency MBS have posted gains for eight consecutive months, she said.

"We believe that spreads in the sector will widen out before year-end because of the rich valuations and the uncertainty about the future of the GSEs," she said.

Xavier Capital Management, which has $95 million in assets under management, continues to be about 15 percent underweighted in U.S. agency MBS relative to its weighting in the Barclays Capital U.S. Aggregate benchmark, she said.

Turner said originations from 2009 are at a premium, unlike the 2006-2007 vintages.

"Uncertainty about the future structure of the GSEs keeps a cloud over U.S. agency MBS, especially for foreign investors," she said.

The yield premium on Fannie Mae MBS paying 4.50 percent interest compared with the 10-year Treasury note widened to 0.973 percentage points on Tuesday from 0.950 percentage points on Monday, according to Reuters data.

That is sharply narrower than the end of last year when the yield premium was around 1.863 percentage point.

The Federal Reserve has set a goal to buy up to $1.25 trillion of agency MBS, $300 billion of Treasuries and $200 billion of agency debt in 2009. The purchases are part of its effort to lower borrowing costs.

The Fed purchases of agency MBS and agency debt total $741.608 billion and $111.037 billion so far in 2009, respectively.

Active 15- and 30-year mortgage securities were 2/32 to 11/32 lower. Prices on 30-year 4.50 percent coupons were 11/32 lower. Bond equivalent yields on 30-year 4.50 percent coupon MBS ranged from 4.415 percent to 4.548 percent.

Prices on 30-year 5.00 percent coupons were 6/32 to 7/32 lower. Bond equivalent yields on 30-year 5.00 percent coupon MBS ranged from 4.188 percent to 4.226 percent.

Yield spreads on agency debt securities were 3 to 4 basis points wider against Treasuries as supply weighed.

The Federal Farm Credit Banks Funding Corp said on Tuesday it sold $1.1 billion in new five-year designated bonds due Sept. 22, 2014 through the Federal Farm Credit Banks Consolidated System Bond Program. For details, double-click on [ID:nN18424764]

The 3.00 percent bonds were priced at 99.847 to yield 3.033 percent or 60 basis points over comparable U.S. Treasuries.

The Federal Home Loan Bank System will announce its August debt funding plans on Wednesday.

U.S. 10-year Treasury notes <US10YT=RR> were 11/32 lower at 100-28/32 to yield 3.520 percent. Yields, which move inversely to price, were up from Monday's 3.481 percent. (Additional Reporting by Chris Reese, John Parry and Caryn Trokie; Editing by James Dalgleish)

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