

Morning Commentary

GBP Desk London

11 January 2012

Time (GMT)	Country	Event	Month	Expect	Previous
ON	UK	BRC Shop Price Index y/y	Dec		2.00%
09:30	UK	Visible Trade Balance GBP/Mn	Nov	-8400	-7557
09:30	UK	Trade Balance Non EU GBP/Mn	Nov	-5000	-4554
09:30	UK	Total Trade Balance (GBP/Mln)	Nov	-2400	-1552
10:30	UK	U.K. to Sell GBP3 Bln 3.75% 2021 Bonds			
12:00	UK	Prime Minister's Question Time in House of Commons			

UK Today

- The UK Transport Minister told MPs y/day that the govt will press ahead with the building of HS2, a high speed railway between London and Birmingham, and thereafter through to Manchester, Leeds and onto Scotland. There are doubts over the value of this project with even its own estimates revising down the economic value of the project in the past year. This is a good example of the problems inherent with the political and economic order. Politicians desire to be seen to do something and thus will push through with infrastructure projects in order to advance their political ends. And while infrastructure spending is the better of a number of evils, it can still be severely misguided. The private sector should be driving these projects as it is private individuals and businesses that will make use of them.
- Cable has entered a range between 1.5400 and 1.5700 in recent weeks as news out of Europe and the US drives direction. The techs indicate that there is the risk of further downside on a break lower, but fundamentally upside is favoured for the pair. We have noted before that the short EUR trade may be one that is overdone. If this trade unravels Cable could be a significant beneficiary. The UK monetary environment remains tight with money supply growth contracting, whereas in the US money growth is rampant. Thus the relative new supply of Dollars vs. Sterling is differing and if demand for USDs wavers somewhat in the coming months, whether this is driven by confidence in the EZ or renewed concerns about the US debt limit, then Cable could push back towards the 1.6000 mark in the months ahead. Intraday one should follow the techs and be weary of the potential bear-flag.
- The Libor OIS spread has recently retraced off the highest level seen in recent months at 60bp to 59bp at present. However this level of banking liquidity tension remains concerning. However the UK gilt-swap spread has moderated quite significantly in recent weeks indicating that credit risk is moderating despite elevated liquidity tension. Value could be found in swaps over gilts as this gilt-swap spread moderates further in the months ahead as the level of credit risk subsides.
- **GBP-USD techs:** The stochastic has generated a crossover buy signal but the losses in early trade so far suggest that a bear flag could be evolving. A break above 1.5490 will confirm the buy signal in which event 1.5559 can be targeted. A break below 1.5445 will confirm that the flag is evolving - then target 1.5374. *Strategy: Break above 1.5490 targets 1.5559. Break below 1.5445 targets 1.5374*

Global Fixed Income

- The US Treasury drew record demand at its \$32 billion 3yr note auction last night. The auction's bid-to-cover ratio came in at 3.73, the highest since at least 1993. The bond priced at 0.37%, yields flat on the day. The bulk of demand came from dealers who took 56.1% of the offer, while indirects accounted for 38%. Direct bidders came in at a 2-year low of 5.3%.
- The US Treasury will still sell another \$34 billion worth of debt securities this week, including \$21 billion worth of 10yr bonds today and \$13 billion of 30yr bonds on Thursday, for a total of \$66 billion this week. \$30.5 billion will be raised at the auctions, as \$35.5 billion worth of securities mature, according to Bloomberg.
- Turning then to Europe, where reports are still coming out that banks are parking record amounts with the ECB, the mood is still gloomy with market talk remaining decidedly bearish of the outlook. Talk is that banks are hoarding cash in order to satisfy refinancing needs this year, and that as a result, it won't generate an economic turnaround. However, once banks tap this money in refinancing activity, it will begin to seep into the economy and in turn start to generate new credit growth.
- The bund asset swap spread remains in a general downtrend, down from peaks of 80bps in November to 53.8bps by yesterday's close. That said, credit risk for peripheries remains elevated, with the Italian 5yr CDS spread at 518bps, only down marginally from peaks of 600bps reached late last year. Today, Germany will sell EUR4 billion worth of 5yr bonds at 10:15 GMT, while the UK comes to market with GBP3 billion worth of 2021 bonds.

Please note the following at mid points and do not constitute tradable levels.

04:52:57 AM GMT

Swaps	Bonds	Spreads	Yield Curve
1YR	1.346		1Y GILT 0.4175
2YR	1.305	4H 13 104.68 86.5	2Y GILT 0.421
3YR	1.348	2Q 14 103.91 91.5	3Y GILT 0.55
4YR	1.448	2T 15 106.57 88.5	4Y GILT 0.8035
5YR	1.584	4 16 113.92 64.5	5Y GILT 1.075
6YR	1.736	4 16 113.92 79.5	6Y GILT 1.2855
7YR	1.898	5 18 121.87 60.5	8Y GILT 1.7525
8YR	2.064	3T 19 114.90 39.5	10Y GILT 2.064
9YR	2.21	3T 20 114.88 33.5	15Y GILT 2.6035
10YR	2.331	3T 21 114.58 25.5	20Y GILT 2.8735
12YR	2.511	3T 21 114.58 44	25Y GILT 2.992
15YR	2.69	5 25 129.04 15	30Y GILT 3.0965
20YR	2.861	4T30 128.44 6	40Y GILT 3.158
25YR	2.953	4T38 131.32 -8	50Y GILT 3.119
30YR	2.989	4Q40 121.72 -12	Yield Curve Shape
40YR	3.031	4Q49 124.40 -11	2v10 164.3
50YR	3.054		10v30 103.25
60YR	3.071		

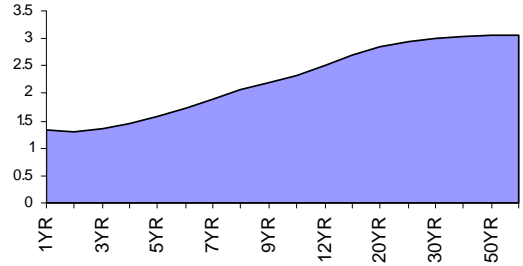
Swap Curve Shape	BBA
2v5	27.9 1m 0.77756
2v10	102.6 2m 0.88744
10v30	65.8 3m 1.08863
2v5v10	-46.8 6m 1.38681

MPCS	SONIAS	FRAs
DEC	0.52 1W	0.515 1X4 1.11
JAN	0.513 2W	0.514 2X5 1.12
FEB	0.498 3W	0.513 3X6 1.11
MAR	0.494 1M	0.513 4X7 1.08
APR	0.487 2M	0.505 1X7 1.39
MAY	0.482 3M	0.501 2X8 1.38
	4M	0.5 3X9 1.35
	5M	0.495 6X12 1.31

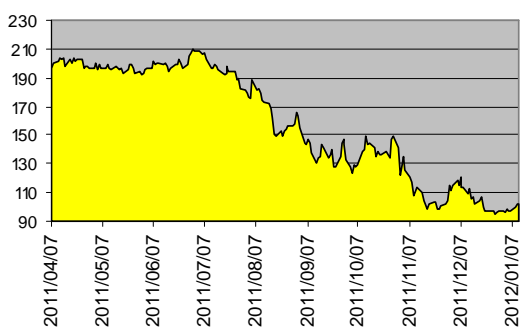
FRA v SONIA SPD	Forwards	
JUN	62.4 6M	0.495 SW -0.82
SEP	59.12 7M	0.49 2W -1.76
DEC	57 8M	0.485 1M -4.065
MAR	56.5 9M	0.48 2M -8.37
JUN	57 10M	0.48 3M -12.96
SEP	56 11M	0.48 6M -28.33
DEC	55.5 1YR	0.475 9M -43.44
MAR	55 18M	0.465 1Y -58.23
	2YR	0.475 1Y -58.23

Indices and FX Rates					
GBPUSD	1.5453	Gold	1635.89	DJI	12462.47
EURGBP	0.8242	Platinum	1477.74	FTSE	5696.7 CLS
GBPJPY	118.85	Silver	29.91	NIKKEI	8438.71
GBPCHF	1.4704	Palladium	638.47	S&P	1292.08

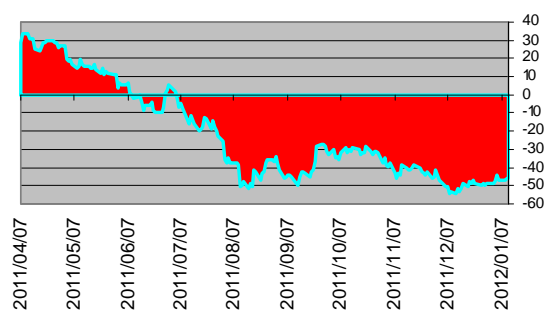
Swap curve



2v10 Swap Spread



2v5v10 Fly



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