Morning Wakeup Call European Session

Macro Strategy

Wednesday, January 11, 2012

Time (GMT)	Country	Event	Month	Exp/Actual	Prior
08:00	DE	Full-year GDP	2011	3.00%	3.60%
09:30	GB	Trade	Nov	-8.40bn	-7.56bn
	EZ	German Chanc. Merkel and Italian PM Monti hold talks on eurozone crisis			
	EZ	World Economic Forum launches Global Risks 2012 report			
13:40	US	Fed member Evans speaks on "Perspectives of current economy"			
17:30	US	Fed member Plosser speaks on economic outlook			
	US	Fed Beige book of economic conditions released			

Factors to Watch

Factor	*What's up?*	*Relevance?*	*Importance*	*Outlook & Mkt impact*
Chinese surplus	Trade surplus fell to $155bn in 2011 from $183bn in 2010	Slight reduction in Chinese imbalance implies less savings to drive growth	Mod-High: Global imbalance still exists	*Likely: Imbalance between Asian savings and Western debt will take a number of years to rectify.* **Timeframe: Longer term**
Hedge fund – IMF conflict	Hedge funds exposed to Greeks bonds oppose planned bond swap	Number of hedge funds prefer that Greece nation defaults and CDS' triggered	Mod-High: May generate further Euro pessimism	*Likely: Banks have strong relationship with CBs and global monetary institutions which should see a deal reached.* **Timeframe: Q1 2012**
EU leaders meet	Merkel is set to meet with Italian PM Monti today	Planning to discuss Eurozone crisis	Mod-High: Investors hoping for direction	*Likely: Germany appears to be getting periphery nations to contract fiscal budgets however it is time consuming.* **Timeframe: On-going**

Newswires

Bloomberg www.bloomberg.com	**S. Korea May Join Indonesia Holding Rates** South Korea and Indonesia will probably keep interest rates unchanged this week as a drop in their currencies risks heightening inflationary pressures even as the faltering global economy undermines growth prospects. All 14 economists surveyed by Bloomberg News expect the Bank of Korea to keep the benchmark seven-day repurchase rate unchanged at 3.25 percent on Jan. 13 for a seventh straight month, the longest pause since tightening began in July 2010. Bank Indonesia will keep the reference rate at 6 percent tomorrow, 13 of 18 economists surveyed predict, while the rest see a quarter-percentage-point cut.
New York Times www.nytimes.com	**Fed Turns Over $77 Billion in Profits to the Treasury** WASHINGTON — The Federal Reserve said on Tuesday that it contributed $76.9 billion in profits to the Treasury Department last year, slightly less than its record 2010 transfer but much more than in any other previous year. The Fed is required by law to turn over its profits to the Treasury each year, a highly lucrative byproduct of the central bank's continuing campaign to stimulate economic growth. Almost 97 percent of the Fed's income was generated by interest payments on its investment portfolio, including $2.5 trillion in Treasury securities and mortgage-backed securities, which it has amassed in an effort to decrease borrowing costs for businesses and consumers by reducing long-term interest rates.
Financial Times www.ft.com	**Europe set to block DB-NYSE tie-up** European competition officials have recommended blocking the tie-up between Deutsche Börse and NYSE Euronext, the German and US exchange operators, setting in motion what could be weeks of frantic lobbying to salvage the deal. Joaquín Almunia, the European competition commissioner, has told the merger parties that he plans to prohibit the bid to create the world's biggest exchange group by listings unless they are willing to sell one of the groups' main derivatives businesses – a step executives refuse to take. The antitrust decision is a serious blow to the chances of the German and US groups being able to complete the deal, and highlights how competition concerns have helped scupper a year-long wave…

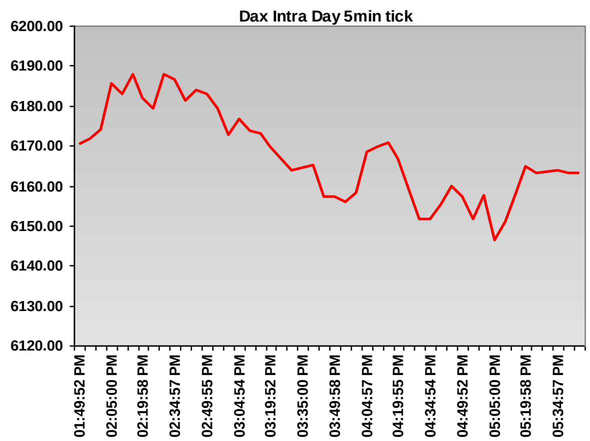
Summary of Asian and US Session and Market Outlook:

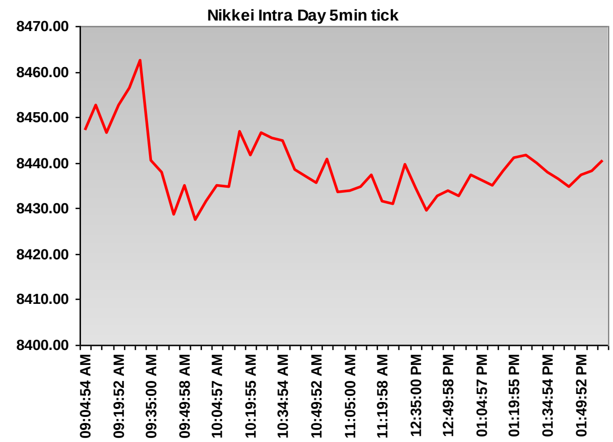
- *Company/sector related news drives EU stocks higher, not significant rise in risk sentiment; Asia stocks thus mixed o/n*
- *US 3yr Treasury draws record demand at auction, US forcing itself ever closer to debt ceiling again*
- *Debt accumulation combined with stronger US growth, rising inflation risks to pressure Treasuries through 2012*
- *EUR-USD fails to hold break above 1.2800, next move seen to the downside; risk/carry trade keeps AUD, NZD buoyant*
- *Corporate credit risk continues to gradually decline; funds flow to EMs on record start in issuance this year*
- *Oil prices range-bound given opposing impact from Iran risks, Europe worries; bias stronger to the upside*

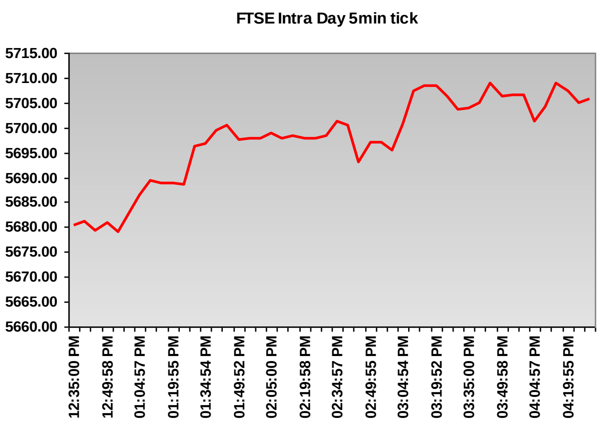
Market Colour and guidance	Bias	Risk to Bias
Equities: EU stocks surprised somewhat in the extent of their gains yesterday. The gains were not necessarily a function of a substantial rise in risk sentiment but more so positive factors noted for each sector. Commerzbank stated that its 2012 funding needs had fallen as low as EUR 6bn, while auto makers Daimler, BMW and VW rallied amid the current reveal at the Detroit auto show. Indeed corporates are looking in somewhat of a healthier position into the start of 2012 with the availability of cheap funding, both in Europe and the US, providing a backstop. The fundamental difference in the US is that corporates are using higher cash levels to leverage themselves and invest again in a growth environment that promises to outperform the EU for some quarters to come. There was very little key data on tap yesterday worth noting. US wholesale inventories data surprised to the downside in its m/m growth in Nov. We had warned of a soft number for Nov after a strong inventory build in Oct and this does not allude to a significant contraction in expected sales activity going forward. With not much key data again today, focus will remain on the meetings between EU leaders and upcoming debt issuance from Germany.	Major mkts retain slightly positive footing; Rallies on confidence in corporate financial positions	Not much in the way of key data today, focus will be on EU news flow and German debt auction
Bonds: The US Treasury drew record demand at its $32bn 3yr note auction last night. The bond generated a bid-to-cover ratio of 3.73 against the previous level of 3.62 and a 12-auction average of 3.31, despite the yield drawn of 0.37% still very subdued. The bulk of the demand came from primary dealers with an uptake of 56.1%. The US Treasury is still due to sell another $34bn this week by way of $21bn in 10yr bonds today and $13bn in 30yr bonds tomorrow. Despite the fact that net issuance is somewhat neutral given a fairly proportional total of securities maturing this week, the US is again testing the limits of its debt ceiling and will need to raise it should it continue to auction off debt of this magnitude. Persistent debt accumulation combined with stronger US growth and rising inflation prospects all add up to a more and more attractive strategic short Treasury trade as we head further into 2012. Meanwhile in Europe, talk is that banks are still hoarding cash to meet refinancing needs for this year. Economic growth in the region is due to remain soft in H1, but this cash will ultimately seep into the economy and generate new credit growth down the line, especially as borrowing costs remain so suppressed.	US Treasuries remain steady as record auction demand entices investors to hang onto long positions	US debt accumulation, stronger growth, rising inflation risks add attractiveness to sell Treasuries on any upticks
Currencies: Yesterday the EUR-USD ended marginally higher but again failed to hold its break above the 1.2800 level as was seen at the end of last week. The pair is still recovering from its earlier oversold status but patterns of consolidation appear all too familiar, suggesting the next break-away could again be to the downside. A recession in Europe should already be priced in for the EUR as it is not something the region as a whole can avoid. The tight monetary conditions through prior years brought about tighter economic conditions and only marginal relief will be found from the latest QE measures taken by the ECB. However it is the debt auctions that are perhaps being priced too negatively as demand continues to be found. Resilient demand at the auctions could spur a short term recovery for the EUR, particularly against the USD and JPY. The USD index weekly chart remains firmly bullish, with long lower shadows showing persistent buying on the dips. The USD index is expected to remain supported on the back of EUR pessimism but the risk/carry trade is also gaining some traction given the trend of improving US data in particular, allowing for a better performance on high yield and commodity currencies such as the NZD and AUD.	EUR-USD consolidating, failure to hold break above 1.2800 suggests next move lower; USD index supported by gains to be capped by risk trade traction	Mkts pricing overly cautiously ahead of various EU debt auctions
Credit Markets: Corporate credit risk is on the decline in US and Europe. The US Markit investment-grade CDX index dropped to 116.3bps yesterday, its lowest levels since late Oct. Substantial money pumping from the Fed in prior years has propped up the money base off which corporates have been able to extend credit and reduce existing debt. A similar monetary propping is expected to filter through to EU corporates through 2012 on the back of the latest ECB efforts. As liquidity levels are raised globally, investors will become more confident in taking on risk once more. One area this is likely to gain traction is in the EM bond markets, with average EM bond yields some 379bps above Treasuries compared to 248bps the same time last year. IMF estimates EM economies will grow 6.1% this year against 1.9% growth in DMs. Interestingly, Bloomberg reports a record start to the year in terms of EM bond issuance since data began in 1999, reflecting the probability of increased fund flow to these markets. Bond issuance has totalled $30.6bn this year.	Monetary stimulus promotes risk taking; Strong EM bond issuance finds equally strong demand given yield on offer	Risk environment still highly dependent on sentiment in EU given debt levels
Energy Markets: As has been the case since the start of the year, movements in the oil markets have been largely driven by a play-off between pricing in a risk premium linked to tension in Iran on the one side, whilst considering the implications that the Europe crisis will have on demand for oil products. Consequently, Brent has been range-bound between $111.27/bl and $114.64/bl since 4 January. Yesterday Brent gained around $0.80/bl to close at $113.28/bl and edged lower overnight to $112.92/bl at the time of writing. The decline came on the back of increased concerns over Europe, coupled with rising US crude stockpiles, as reflected in yesterday's preliminary API data. Today investors will look to German GDP data as well as the Fed's beige book on the US economic conditions for some trading direction. Also keep an eye out for the weekly EIA inventory data.	Iran factor coupled with Europe jitters keep oil range-bound, but bias favours topside	Fed Beige book release, EIA inventory data to generate short term direction

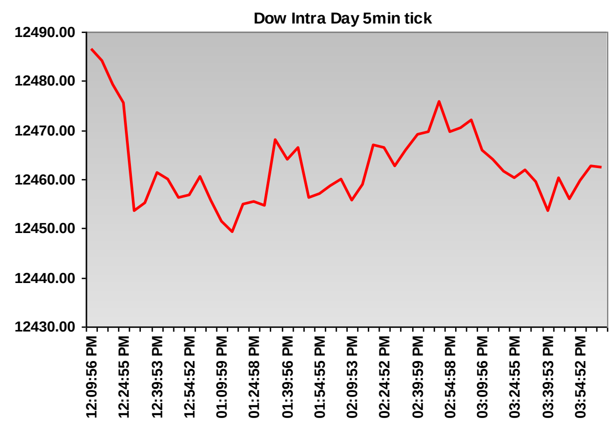
Economic Data Preview	Outlook	Risk
DE Full-year GDP (2011)	Germany saw its fastest expansion in two decades in 2010 after a rotten year in 2009. While growth remained resilient through the first half of 2011 it came under severe pressure in H2 2011 as periphery growth crumbled and demand for German goods faltered. Thus growth is expected to have slowed from 2010. A survey of economists puts growth at 3.0% y/y, if anything there is a possibility of a surprise to the downside.	Slower growth remains entrenched on weak EZ demand, softer China imports

Global Equities









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Please note that the following are indicative pricing and do not constitute tradable levels

World Indices		%Change
Dax	6162.98	2.42
Nikkei	8440.43	0.22
Dow	12462.47	0.56
S&P	1292.08	0.89
FTSE	5696.7	1.50

Commodities and FX		%Change
Brent Oil	112.95	-0.29
Baltic Dry	1258	-3.82
CRB Inde	359.43	1.60
Gold	1635.84	0.30
USD Inde	81.051	0.08
VIX	20.69	-1.80

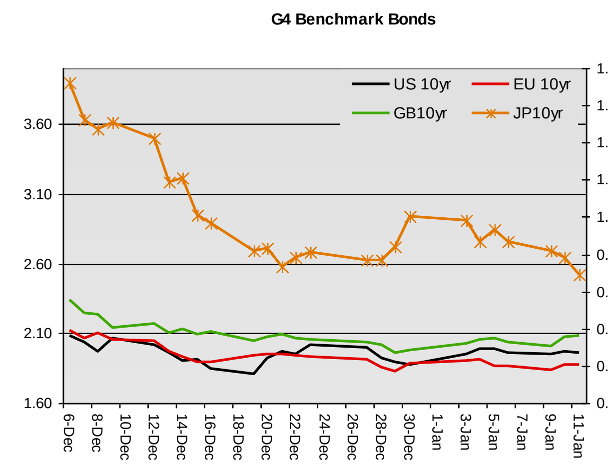
Fixed Income		%Change
US 10YR	1.9613	-0.27
EU 10 YR	1.871	-0.37
GB 10 YR	2.084	0.48
JP 10 YR	0.969	-0.92

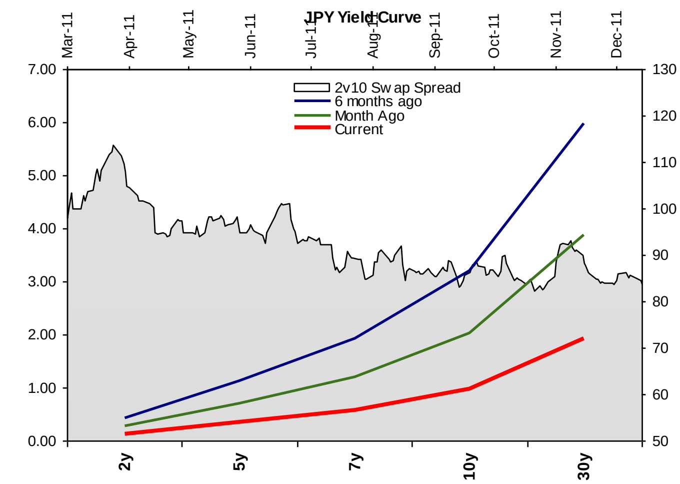
Correlation Matrix 365 Day

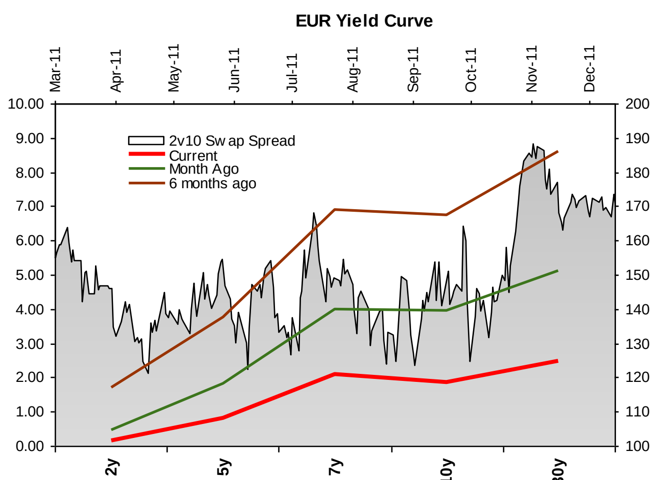
	Gold	Baltic Dry	Brent Oil	USD	CRB	MCSI	Nikkei	FTSE	DJI	DAX	US 10YR	EU 10YR	GB 10YR	JP 10YR
Gold	1.00	0.60	0.09	-0.07	-0.49	-0.66	-0.77	-0.81	-0.54	-0.79	-0.86	-0.83	-0.84	-0.84
Baltic Dry	0.60	1.00	-0.10	0.37	-0.67	-0.78	-0.76	-0.66	-0.49	-0.76	-0.75	-0.75	-0.72	-0.67
Brent Oil	0.09	-0.10	1.00	-0.60	0.61	0.40	-0.02	0.25	0.46	0.28	0.20	0.24	0.15	0.13
USD Index	-0.07	0.37	-0.60	1.00	-0.66	-0.58	-0.24	-0.21	-0.20	-0.39	-0.35	-0.41	-0.36	-0.20
CRB Index	-0.49	-0.67	0.61	-0.66	1.00	0.90	0.69	0.72	0.53	0.75	0.82	0.83	0.81	0.77
MCSI Worl	-0.66	-0.78	0.40	-0.58	0.90	1.00	0.82	0.87	0.67	0.92	0.91	0.91	0.88	0.81
Nikkei	-0.77	-0.76	-0.02	-0.24	0.69	0.82	1.00	0.83	0.51	0.86	0.89	0.84	0.89	0.84
FTSE	-0.81	-0.66	0.25	-0.21	0.72	0.87	0.83	1.00	0.85	0.95	0.89	0.87	0.85	0.82
DJI	-0.54	-0.49	0.46	-0.20	0.53	0.67	0.51	0.85	1.00	0.79	0.60	0.61	0.51	0.51
DAX	-0.79	-0.76	0.28	-0.39	0.75	0.92	0.86	0.95	0.79	1.00	0.92	0.92	0.88	0.80
US 10YR	-0.86	-0.75	0.20	-0.35	0.82	0.91	0.89	0.89	0.60	0.92	1.00	0.98	0.99	0.94
EU 10YR	-0.83	-0.75	0.24	-0.41	0.83	0.91	0.84	0.87	0.61	0.92	0.98	1.00	0.97	0.93
GB 10YR	-0.84	-0.72	0.15	-0.36	0.81	0.88	0.89	0.85	0.51	0.88	0.99	0.97	1.00	0.95
JP 10YR	-0.84	-0.67	0.13	-0.20	0.77	0.81	0.84	0.82	0.51	0.80	0.94	0.93	0.95	1.00

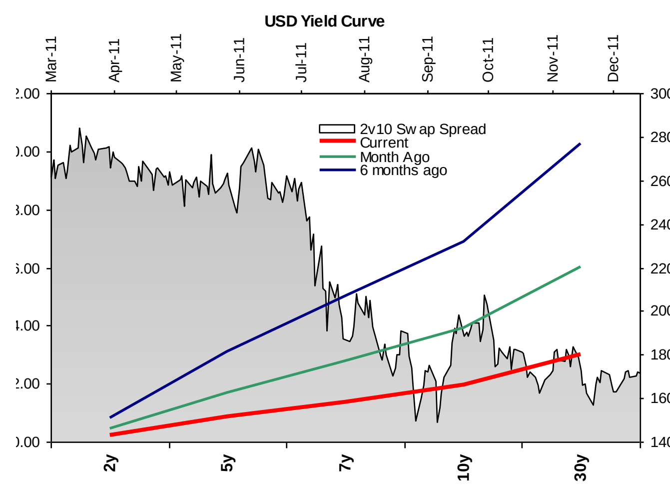
Weak Correlation Blue
High Negative Red
High Positive Green

Currencies		% Change			% Change			% Change
USD Ind	81.05	0.079	JPY	76.91	0.1041	CHF	0.9514	0.22122
EUR	1.274	-0.23	GBP	1.546	-0.155			









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