

Daily Market Strategy

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Market Strategy

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- Gold extends slide; upside risk for yields ahead of Bernanke; US auctions
- Yen off lows on talk of repatriation flows; Nikkei extends rally

Market Outlook

Kenneth Broux

Opening levels (7.15am)

£/\$: 1.6447

€/£: 1.4876

\$/¥: 89.75

UK 5y sw: 3.13%

US 5y sw: 2.61%

EU 5y sw: 2.73%

It may be too early to call a turning point for the USD and bond yields/swaps after Friday's stronger US employment report, but the rally in USD crosses and spike in yields are a taster of what 2010 may look like if the US economy starts showing more tangible evidence that economic conditions are normalising. With expectations now rising for a return to positive jobs growth as soon as next month for the first time since December 2007, we see a danger that markets get carried away in pricing in full recovery and earlier exit/policy tightening. With liquidity inevitably set to deteriorate over the holiday period, the USD could be set for a strong finish into year-end as higher Treasury yields compress G10/US spreads. Some unwinding of Friday's price action could take place today if Fed chairman Bernanke urges caution in his remarks and paves the way for a status quo at the last FOMC meeting of the year next week. Indeed, we have already seen some modest profit-taking in the US dollar this morning with the DXY index down around 0.4% this morning.

Ahead today: German factory orders are forecast to post an increase of 0.8%, similar to the gain in September. In the US, focus will be on Bernanke speaking at 17:00 and consumer credit numbers - the market expects a ninth consecutive contraction. ECB President Trichet speaks before the European Parliament while the BoE is set to purchase £1.7bn in 2020 to 2034 gilts.

FX: for USD/JPY, the post NFP rally faded above 90.0 overnight with talk of repatriation flows squeezing the cross to 89.83. Key support comes in around 89.2. Japanese firms Mitsubishi and Hitachi are reported to be preparing capital increases, with proceeds of overseas share offerings likely to be repatriated. EUR has also sold-off sharply this morning following a break of its upward trend line from the March lows (see chart) to below 1.48. This opens the way to possible move down to 1.4626.

Rates: UK 5y swaps opened at 3.13% this morning and we look for rates to settle at the upper end of the range ahead of the PBR and MPC meeting. The 2y/10y swaps curve has continued to flatten this morning to 196bps, led by the short-end, where it finds strong support. For US 10y yields, a break of 3.50% brings 3.57% resistance into play. We expect to see pressure for higher yields going into the auctions starting with 3y notes tomorrow, with 2y/10y curve flatteners favoured.

	Close	Daily Change %
FX		
EUR/GBP	0.9018	-0.91%
GBP/USD	1.6474	-0.40%
EUR/USD	1.4858	-1.29%
USD/JPY	90.560	2.60%
AUD/USD	0.9147	-1.00%
Bonds %		bp
US 10Yr	3.472	8.8
EUR 10Yr	3.238	6.1
UK10 Yr	3.627	3.6
UK 5yr Swap	3.123	8.7
Equities		%
S&P500	1105.98	0.55%
FTSE100	5322.36	0.18%
Eurostoxx50	2910.33	1.19%
Shanghai Composite	3331.90	0.45%
Commodities		%
Crude Oil \$/bl	75.47	-1.29%
Gold \$/oz	1161.4	-3.83%
Copper	323.8	-0.23%
Baltic Dry	4107	1.11%
Other		
VIX	21.25	-5.39%
iTraxx XOVER	499.45	-6.8

EUR/USD breaks upward trend line



Today's Data	Time	Consensus	Previous	Events
German Factory Orders, Oct	11:00	0.5%	0.9%	ECB speaker: president Trichet (08:00), Honohan (08:30), Quaden (10:45)
Canada Building Permits, Oct	13:30	n/a	1.6%	Fed speaker: chairman Bernanke (17:00), Dudley (22:45)
US Consumer Credit, Oct	20:00	-\$9.7bn	-\$14.8bn	BoE reverse auction (£1.7bn): 4.75_070320, 4_070322, 5_070325, 4.25_071227, 6_071228, 4.75_071230, 4.25_070632, 4.5_070934

*All charts are sourced to Lloyds TSB Corporate Markets Economic Research, Bloomberg & DataStream

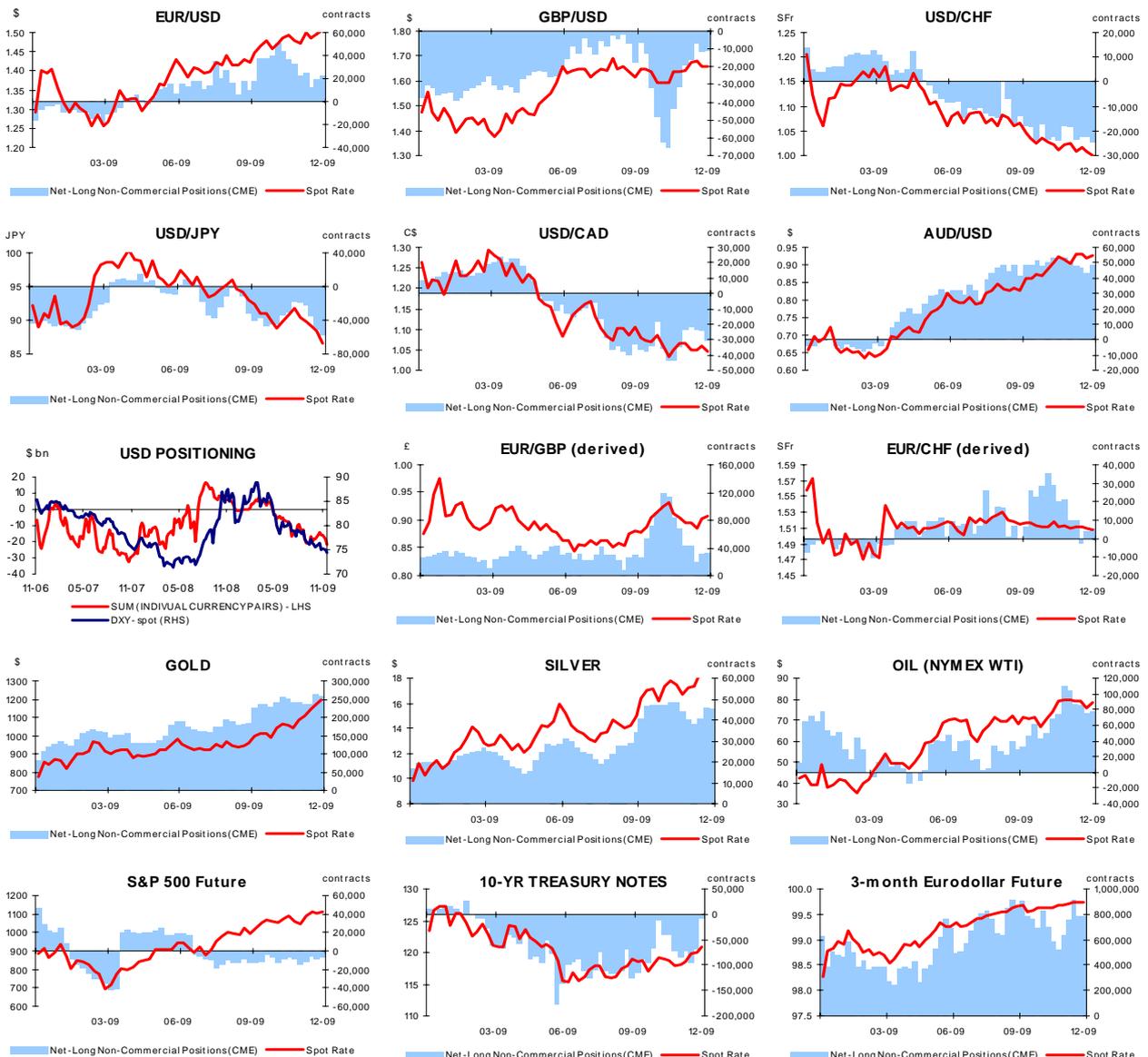
Trend following model signals

Trend Following Model Positions			
	Signal	Date	Entry Level
AUDUSD	short	19-Nov-09	0.9296
NZDUSD	long	04-Dec-09	0.7217
EURUSD	long	26-Nov-09	1.5138
GBPUSD	long	26-Nov-09	1.6705
USDCHF	short	26-Nov-09	0.9964
USDCAD	long	04-Dec-09	1.0571
USDSEK	short	02-Dec-09	6.9044
USDNOK	short	02-Dec-09	5.6195
USDJPY	long	07-Dec-09	90.56
Net-USD portfolio position			-33%

Trend Following Model Positions			
	Signal	Date	Entry Level
USDCZK	short	30-Nov-09	17.428
USDPLN	short	05-Nov-09	2.8609
USDSGD	short	10-Nov-09	1.3863
USDTRY	short	02-Dec-09	1.5025
USDZAR	short	30-Nov-09	7.4041
Net-USD portfolio position			-100%

The trend following model has reduced its short USD position this morning, selling JPY and purchasing USD. The previous short USD position versus the JPY has been closed for a loss of 0.50%. Overall, the model has reduced its short USD portfolio versus developed market currencies to just 33% and is currently long US dollars against AUD, CAD and JPY. Against developed market currencies, the model remains short USD versus all the currencies in the portfolio.

FX & Commodity Futures Positioning



Market Summary

	Close	Daily Change %		Close	Daily Change %
FX			Equities		
EUR/USD	1.4858	-1.29%	S&P500	1105.98	0.55%
USD/JPY	90.56	2.60%	DJIA	10388.90	0.22%
AUD/USD	0.9147	-1.00%	FTSE100	5322.36	0.18%
EUR/GBP	0.9018	-0.91%	Eurostoxx50	2910.33	1.19%
GBP/EUR	1.1089	0.92%	Shanghai Composite*	3331.90	0.45%
GBP/USD	1.6474	-0.40%	*latest price		
GBP/JPY	149.20	2.20%	Commodities		
GBP/CHF	1.6750	1.16%			%
GBP/AUD	1.8011	0.61%	Crude Oil \$/bl	75.47	-1.29%
GBP/CAD	1.7428	-0.34%	Gold \$/oz	1161.4	-3.83%
GBP/NZD	2.2998	0.34%	Copper c/lb	323.8	-0.23%
GBP/NOK	9.3710	0.83%	Silver \$/oz	18.52	-1.65%
GBP/ZAR	12.2309	-0.14%	Baltic Dry	4107	1.11%
GBP/CNY	11.2475	-0.39%			
Bonds %			Swaps %		
		bp			bp
US 10Yr	3.472	8.8	US 5yr	2.618	13.5
EUR 10Yr	3.238	6.1	EUR 5yr	2.728	5.6
UK10 Yr	3.627	3.6	UK 5yr	3.123	8.7
Other			Official Rates %		
VIX	21.25	-5.39%	UK	0.50	
iTraxx XOVER	499.45	-6.8	US	0.25	
DJ Agriculture Index	63.31	-1.63%	EU	1.00	
			Japan	0.10	

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