

# Daily Market Strategy

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## Market Strategy

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- EU/IMF deal for Greece, ECB abandons collateral plan
- FX/risk correlation breaks down

### Market Outlook

Kenneth Broux

Opening levels (7.15am)

£/\$: 1.4868

€/£: 1.3345

\$/¥: 92.51

UK 5y sw: 2.91%

US 5y sw: 2.71%

EU 5y sw: 2.45%

### Overnight

- ECB divided over IMF assistance, external considered detrimental to euro stability; to abandon increase in collateral requirement next year to weigh on the EUR
- bi-lateral loans a difficult sell for Chancellor Merkel ahead of NRW state election
- disappointing US 7y auction; b/c 2.361 indirect bidders get 41.9%, directs take 8.1%, tail 4bp

A mildly positive reaction is observed this morning in currency and bond markets to the 'breaking news' from the EU summit. Though the EUR could build gains through weakness in JPY crosses, the single currencies still languishing near the weekly lows and Greek debt has responded in a rather hesitant fashion (compression in 10y spread/bunds running out of steam at 300bp). We'll see how the day goes, but the Greek PM and debt agency PDMA will be gunning for a further tightening below 300bp to clear the issuance hurdles in April. The announcement by the ECB that it will not raise its minimum collateral requirements early next year as originally planned is quite extraordinary in a way (politicians leaning on central bank), though we understand that haircuts will be phased in (more details at next ECB meet on April 8). The announcement comes only three weeks after ECB president Trichet reaffirmed that collateral changes would take effect in 2011. In addition, the involvement of the IMF, whilst necessary in the short-term as a backstop, has been opposed by Trichet and Weber among others and will only reinforce the view that the ECB's independence this week has been undermined. In this context, it is difficult to see global currency accounts getting too enthusiastic of a EUR bounce considering the options for 'safer' (USD) or higher yield/commodity options (CAD, AUD) in the G10.

### Ahead today

- UK: business investment has disappointed and partially explains why the UK has fallen behind the US in the recovery stakes; final Q4 data this morning are not expected to show a revision from the previous -5.8% q/q estimate, the 6th consecutive drop.
- EU: a slew of ECB speakers is lined up, including ECB president Trichet at 16:00.
- US: final estimates of Q4 GDP and the price deflator are not expected to show major deviations from the 2nd estimate. The 3rd and final release comes with a breakdown of corporate profits. Overall profitability rose 10.8% in Q3-09, with US financial sector profits jumping 31.1%.

**FX:** the breakdown in correlation with pro risk has been evident this week and makes selecting the winners more difficult as equities continue to rally. Whilst we could see some reversal in stocks today on concerns of US supply indigestion, the USD looks well paced to consolidate this week's gains vs the G10, with widening 10y US/G10 rate differentials and domestic troubles in the euro zone and the UK underlining confidence in the EUR and GBP. We think the EUR remains a sell despite the EU agreement on Greece. Rallies in EUR/USD are possible up to descending trendline resistance in the 1.3650 area, but should be sold with a medium term target of 1.3250. For EUR/GBP, failure to make headway below the 100d MA at 0.8916 underlines the lack of conviction post Budget to nudge GBP higher. Election polls this weekend will set the early tone next week, but indications of a further narrowing of the gap between Labour and the conservatives (increased risk of hung parliament) will not do EUR/GBP any good.

**Rates:** Technically UK 5y swaps have been drifting in a range for most of March, but risk of a range break is still validated as rates struggle to bounce off the bottom at 2.90%. Another sloppy US auction overnight does not bode well for government bonds generally, though K 10y paper has managed to hold in below 4.05%, arguably assisted by 'not so great' UK retail sales data yesterday. Business investment and profit taking in stocks may attract some buyers before the weekend, though selling pressure in the US could dictate higher UK yield across the curve.

|                    | Close   | Daily Change % |
|--------------------|---------|----------------|
| <b>FX</b>          |         |                |
| EUR/GBP            | 0.8961  | 0.04%          |
| GBP/USD            | 1.4813  | -0.37%         |
| EUR/USD            | 1.3273  | -0.32%         |
| USD/JPY            | 92.730  | 0.47%          |
| AUD/USD            | 0.9074  | 0.00%          |
| <b>Bonds %</b>     |         | <b>bp</b>      |
| US 10Yr            | 3.878   | 2.5            |
| EUR 10Yr           | 3.152   | 7.3            |
| UK10 Yr            | 3.979   | 6.2            |
| UK 5yr Swap        | 2.915   | 0.2            |
| <b>Equities</b>    |         | <b>%</b>       |
| S&P500             | 1165.73 | -0.17%         |
| FTSE100            | 5727.65 | 0.88%          |
| Eurostoxx50        | 2948.09 | 1.52%          |
| Shanghai Composite | 3059.72 | 1.34%          |
| <b>Commodities</b> |         | <b>%</b>       |
| Crude Oil \$/bl    | 80.53   | -0.10%         |
| Gold \$/oz         | 1090.5  | 0.35%          |
| Copper             | 338.1   | 1.05%          |
| Baltic Dry         | 3177    | -2.04%         |
| <b>Other</b>       |         |                |
| VIX                | 18.40   | 4.84%          |
| iTraxx XOVER       | 431.62  | -8.7           |

### Today's Data

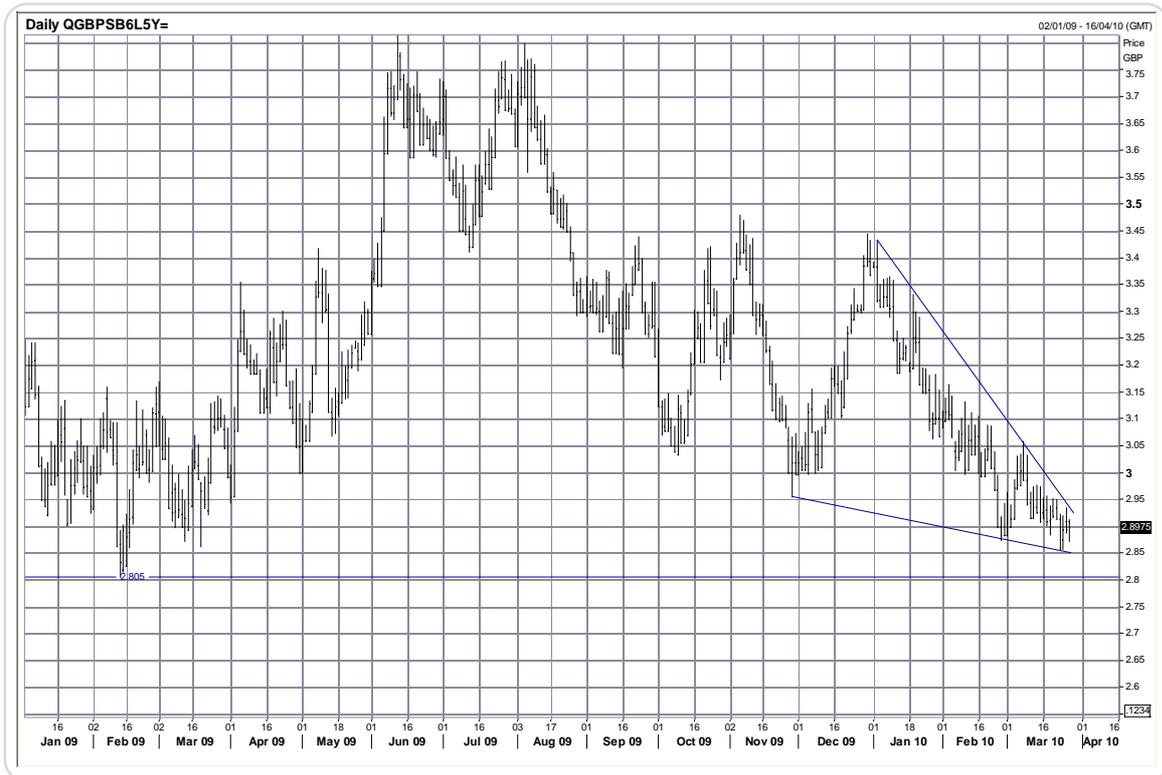
|  | Time  | Consensus | Previous | Events  |
|--|-------|-----------|----------|---|
| UK Business Investment, Q4 final       | 09:30 | -5.8%     | -5.8%    | ECB speakers: Bini Smaghi (07:30), Constancio (11:15),        |
| US -- GDP, Q4 final                    | 12:30 | 5.9%      | 5.9%     | Trichet (16:00), Papademos (20:00)                            |
| -- Core PCE Index, Q4 final            | 12:30 | 1.6%      | 1.6%     |   |
| Uni. Of Michigan Confidence, Mar final | 13:55 | 73.0      | 72.5     | Fed speakers: Warsh (15:30), Bullard (20:00), Tarullo (22:00) |

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

USD/JPY: through 92.50; US/JGB 10y spread near 250bp



UK 5y swaps: waiting for the range to break; support at 2.80%



## Market Summary

| <b>FX</b>            | <b>Close</b> | <b>Daily Change %</b> | <b>Equities</b>         | <b>Close</b> | <b>Daily Change %</b> |
|----------------------|--------------|-----------------------|-------------------------|--------------|-----------------------|
| EUR/USD              | 1.3273       | -0.32%                | S&P500                  | 1165.73      | -0.17%                |
| USD/JPY              | 92.73        | 0.47%                 | DJIA                    | 10841.21     | 0.05%                 |
| AUD/USD              | 0.9074       | 0.00%                 | FTSE100                 | 5727.65      | 0.88%                 |
| EUR/GBP              | 0.8961       | 0.04%                 | Eurostoxx50             | 2948.09      | 1.52%                 |
| GBP/EUR              | 1.1159       | -0.06%                | Shanghai Composite*     | 3059.72      | 1.34%                 |
| GBP/USD              | 1.4813       | -0.37%                | *latest price           |              |                       |
| GBP/JPY              | 137.35       | 0.09%                 | <b>Commodities</b>      |              | <b>%</b>              |
| GBP/CHF              | 1.5913       | -0.23%                | Crude Oil \$/bl         | 80.53        | -0.10%                |
| GBP/AUD              | 1.6324       | -0.36%                | Gold \$/oz              | 1090.5       | 0.35%                 |
| GBP/CAD              | 1.5169       | -0.64%                | Copper c/lb             | 338.1        | 1.05%                 |
| GBP/NZD              | 2.1053       | -0.59%                | Silver \$/oz            | 16.62        | 0.24%                 |
| GBP/NOK              | 9.0345       | 0.58%                 | Baltic Dry              | 3177         | -2.04%                |
| GBP/ZAR              | 11.0824      | 0.82%                 |                         |              |                       |
| GBP/CNY              | 10.1140      | -0.34%                |                         |              |                       |
|                      |              |                       | <b>Swaps %</b>          |              | <b>bp</b>             |
| <b>Bonds %</b>       |              | <b>bp</b>             | US 5yr                  | 2.732        | 3.1                   |
| US 10Yr              | 3.878        | 2.5                   | EUR 5yr                 | 2.449        | 2.0                   |
| EUR 10Yr             | 3.152        | 7.3                   | UK 5yr                  | 2.915        | 0.2                   |
| UK10 Yr              | 3.979        | 6.2                   |                         |              |                       |
|                      |              |                       | <b>Official Rates %</b> |              |                       |
| <b>Other</b>         |              |                       | UK                      | 0.50         |                       |
| VIX                  | 18.40        | 4.84%                 | US                      | 0.25         |                       |
| iTraxx XOVER         | 431.62       | -8.7                  | EU                      | 1.00         |                       |
| DJ Agriculture Index | 57.56        | -1.71%                | Japan                   | 0.10         |                       |

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