Daily Market Strategy

Monday, 30th November 2009

Market Strategy

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	Close	Daily Change
FX		**%**
EUR/GBP	0.9083	-0.08%
GBP/USD	1.6501	-0.19%
EUR/USD	1.4988	-0.21%
USD/JPY	86.533	-0.07%
AUD/USD	0.9063	-0.80%
Bonds %		**bp**
US 10Yr	3.205	-6.4
EUR 10Yr	3.168	0.2
UK10 Yr	3.530	-10.4
UK 5yr Swap	3.029	0.9
Equities		**%**
S&P500	1091.49	-1.72%
FTSE100	5245.73	0.99%
Eurostoxx50	2831.14	1.13%
Shanghai Composite	3195.30	3.20%
Commodities		**%**
Crude Oil $/bl	76.05	-2.45%
Gold $/oz	1177.6	-0.91%
Copper	312.6	-2.24%
Baltic Dry	3974	-3.52%
Other		
VIX	24.74	20.80%
iTraxx XOVER	543.91	13.8

- **Markets still cautious despite Shanghai rebound**
- **UK consumer confidence records biggest drop in 13 months**

Market Outlook

Kenneth Broux

Opening levels (7.15am)

£/$: 1.6570	€/$: 1.5054	$/Y: 86.16
UK 5y sw: 3.04%	US 5y sw: 2.38%	EU 5y sw: 2.69%

Overnight:
- UK Nov consumer confidence drops to -17 vs -13
- UAE central bank offers special liquidity facility
- EU/China summit offers little hope of immediate yuan shift
- Japanese manufacturing PMI falls for 2nd successive month, Oct IP disappoints

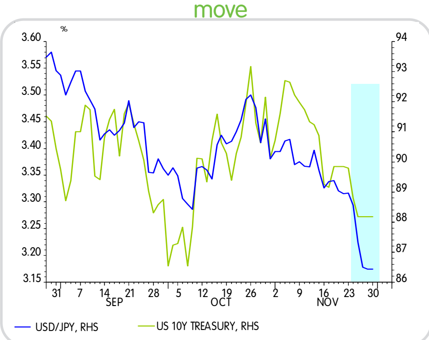
'De-levering' vs 'delivering'. The two opposite market concepts are set to keep tension elevated across asset classes over the coming days as we await the denouement of Dubai's debt problems and the 'Black Friday' trading updates from US retailers plus US November non-farm payrolls. Led by a 3.5% bounce in the Shanghai composite back over 3,155 technical resistance, equity markets made a bullish start to the week (re-leveraging) with the return of risk bringing out sellers of the USD and of short-dated government paper (bearish curve flatteners). We think this set-up has further mileage and dealers will take a 25bps rate hike by the RBA in their stride in the early hours of tomorrow. A more bullish ECB on Thursday could also play a key role in supporting the pro-risk trade, though weak US data could force dealers to take money off the table and square up their portfolios into year-end.

Ahead today: risk of stronger UK October consumer credit figures could bolster GBP crosses and put upward pressure on short-dated yields/swaps. Positive UK retail anecdotes for November and into December suggest households are boosting spending into year-end. Mortgage approvals and lending data and final M4 data are also due. The Chicago PMI is forecast to come in a touch lower at 53.0 vs 54.2.

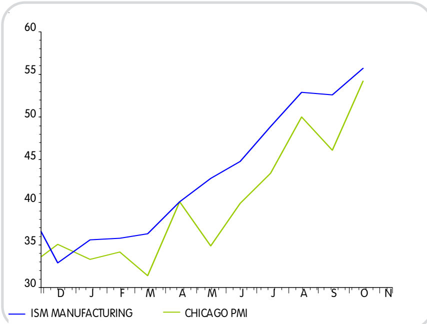
FX: A bounce in Asian equities lifted the mood in high yield and commodity currencies and we look to the RBA (25bps hike expected) to inject additional momentum. AUD/USD bounced over 0.9138 trendline support and from here should target 0.9207 resistance if US equities bounce this afternoon. S&P futures are up 6.90. GBP/USD initially took the weak confidence data in its stride but has just slipped back below 1.65 support. Key support runs at 1.6461. EUR/GBP could be set to make good progress depending on the ECB on Thursday. We look for a rally to 92.0.

Rates: UK 5y swaps dropped 3bps to 3.01% and threaten to re-test 3% support despite the friendlier pro-risk environment. The 2y/10y swaps curve extends its flattening move for a 3rd straight session to 196bps. Key support runs at 194-195bps, an area the curve previously failed to break in early October and again November. UK 5y5y breakevens are steady at 3.78%. The BoE will purchase £1.7bn of long and ultra-long paper.

US 10Y yield: tracking USD/JPY for the next move



Chicago PMI: downside risk for November?



Today's Data	Time	Consensus	Previous
UK Consumer Confidence, Nov	00:01	-17A	-13
UK Hometrack House Prices, Nov	00:01	0.2%A	0.2%
UK Net Consumer Credit, Oct	09:30	-£0.2bn	-£0.3bn
UK Mortgage Approvals, Oct	09:30	57.3k	56.2k
UK M4 Money Supply, Oct final	09:30	n/a	1.8%
EU-16 CPI, Nov flash, %y/y	10:00	0.4%	-0.1%
Canada Monthly GDP, Q3 annualised	13:30	1.0%	-3.4%
Chicago PMI, Nov	14:45	53.0	54.2

Events

BoE reverse auction, £1.7bn: UKT_4.25_070336, UKT_4.75_071238, UKT_4.5_071242, UKT_4.25_071246 UKT_4.25_071249, UKT_4.25_071255, UKT_4_220160

Trend following model signals

Trend Following Model Positions			
	Signal	Date	Entry Level
AUDUSD	short	19-Nov-09	0.9296
NZDUSD	short	20-Nov-09	0.7312
EURUSD	long	26-Nov-09	1.5138
GBPUSD	long	26-Nov-09	1.6705
USDCHF	short	26-Nov-09	0.9964
USDCAD	long	27-Nov-09	1.0619
USDSEK	long	27-Nov-09	6.9712
USDNOK	long	19-Nov-09	5.5908
USDJPY	short	02-Nov-09	90.10
Net-USD portfolio position			11%

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	long	11-Nov-09	1.4769
USDZAR	short	30-Nov-09	7.4041
Net-USD portfolio position			-60%

The current trading environment - a weak trend with low conviction outcomes - has the left the trend following model extremely prone to whipsaw. The model has left its G-10 currency portfolio unchanged this morning, holding a very small (11%) net long USD position. Given the weak trend environment, the model's small position is sensible. Across emerging market currencies, short positions have been triggered in USD/CZK and USD/ZAR this morning. The model's portfolio is now 60% short USD versus emerging market currencies.

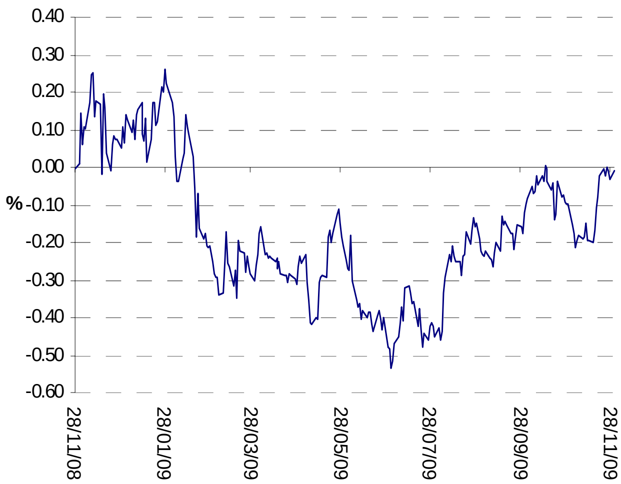


Chart 1: Spread in EZ/UK 2-year interest rate swaps

The chart across shows the spread between 2-year EZ and UK interest rate swaps. The spread is now close to the high observed last month. A close above last month's high would open the way for a move higher in EUR/GBP, eyeing initial resistance at €0.9350. The chart below shows the high level of correlation between EUR/GBP and the interest rate spread.

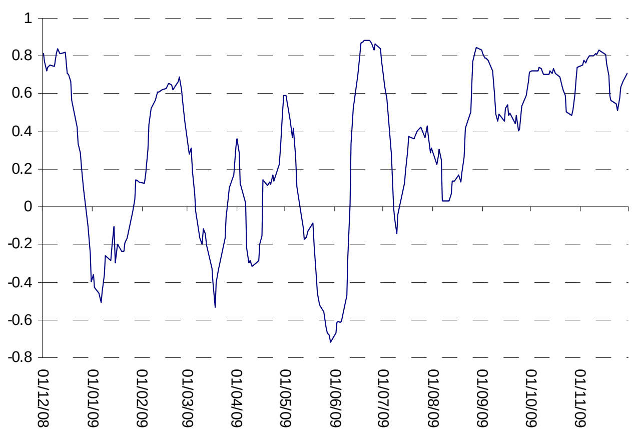


Chart 2: 1-month correlation between EUR/GBP and interest rate swap

Market Summary

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AUD/USD	0.9063	-0.80%
EUR/GBP	0.9083	-0.08%
GBP/EUR	1.1009	0.02%
GBP/USD	1.6501	-0.19%
GBP/JPY	142.78	-0.25%
GBP/CHF	1.6597	0.12%
GBP/AUD	1.8207	0.61%
GBP/CAD	1.7517	0.05%
GBP/NZD	2.3207	0.41%
GBP/NOK	9.3544	0.02%
GBP/ZAR	12.2179	-1.52%
GBP/CNY	11.2622	-0.19%

Bonds %		bp
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DJ Agriculture Index	64.30	0.12%

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*latest price

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Silver $/oz	18.30	-1.96%
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Swaps %		bp
US 5yr	2.348	-11.2
EUR 5yr	2.668	0.3
UK 5yr	3.029	0.9

Official Rates %	
UK	0.50
US	0.25
EU	1.00
Japan	0.10