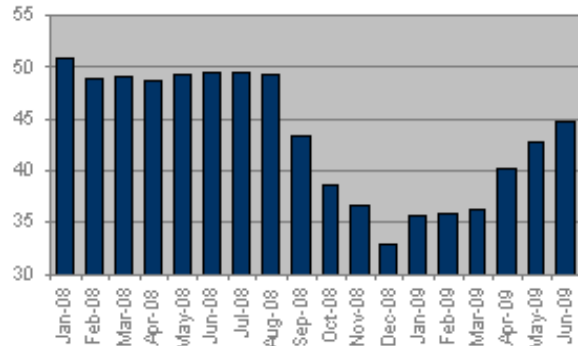


CHART OF THE DAY

U.S. ISM Manufacturing PMI



The U.S. manufacturing sector shrank in June but at a slower pace than during the prior month, the index of national factory activity edged up to 44.8 in June from 42.8 in May according to ISM report.

TODAY'S TOP NEWS

- U.S. jobs gloom overshadows manufacturing glimmers
- China requests reserve currency debate at G8
- U.S. int. rates seen hinging on Fed's exit strategy
- U.S. to pull GM funding if sale not done by July 10
- U.S. SEC proposes say on pay for TARP companies
- M.Stanley, MUFG in loan sharing alliance
- U.S. oil product stocks up sharply, crude down - EIA
- Euro zone factory PMI rises but Germany lags
- Interbank rates at fresh lows as new qtr starts
- UK factory PMI hits 13-mth high as recession eases

ECON WATCH

FOR THURSDAY JULY 2

ET	Indicators	Unit	Reuters	Prior
5:00	EZ Producer prices	mm	% 0.1	-1.0
5:00	EZ Unemployment rate		% 9.4	9.2
7:45	EZ ECB rate decision		% 1.0	1.0
8:30	US Initial claims		k 615	627
8:30	US Jobless contin claims		mln 6.740	6.738
8:30	US Non-farm payrolls		k -363	-345
8:30	US Manufacturing Payroll		k -148	-156
8:30	US Unemployment rate	mm	% 9.6	9.4
8:30	US Average earnings	mm	% 0.1	0.1
10:00	US Factory orders	mm	% 0.8	0.7
10:00	US Durable goods, R	mm	% -	1.8
10:00	US Durable ex-trns R	mm	% -	1.1
10:00	US Durables ex-def, rev	mm	% -	1.4
10:00	US Nondef cap ex-air R	mm	% -	4.8
10:00	US Factory ex-transp	mm	% -	0.1

MARKETS TODAY

TODAY'S TOP STORY: U.S. manufacturing mustered its highest level of activity in nearly a year in June but unexpected weakness in private sector employment signaled how slow an economic recovery might be, reports showed. **For more please click here**

TREASURIES: Longer-dated U.S. Treasuries fell as higher stocks eroded any safe-haven bid, while the start of a new quarter had bond traders refocusing on worries over a deluge of pending government debt supply.

- 10-yr Treasury fell 3/32 in prices for a yield of 3.55 pct from 3.54 on Tuesday.
- 30-yr bond yield was unchanged at 4.34 pct.
- 2-yr Treasury yield fell to 1.05 pct from 1.12 pct.
- 2-10's part of yield curve steepened by about 8 bps to 250 bps.

FOREX: The dollar fell to a three-week low against the euro, pressured by news China has asked to debate proposals for a new global reserve currency at next week's Group of Eight summit.

- The euro rose 0.83 pct against the dollar to \$1.4146, earlier it hit as high as \$1.4201 in the wake of the China news, its highest since June 5.
- The dollar rose 0.31 pct to 96.64 against the yen.
- The dollar index fell 0.6 pct to 79.65.

CORPORATES: U.S. corporate bond spreads tightened, tracking a rise in equity markets and economic data supported the recovery bets.

- The CDX-IG.12 index was unchanged at 131 bps.
- National Australia Bank launched a two-part government-guaranteed debt sale which includes \$1.75 bln 5-yr floating rate notes and \$1 bln in fixed-rate notes.

STOCKS: U.S. stocks rose, as investors took reassuring manufacturing data from China, Europe and the United States as a fresh signal that the world's economy is on the road to recovery.

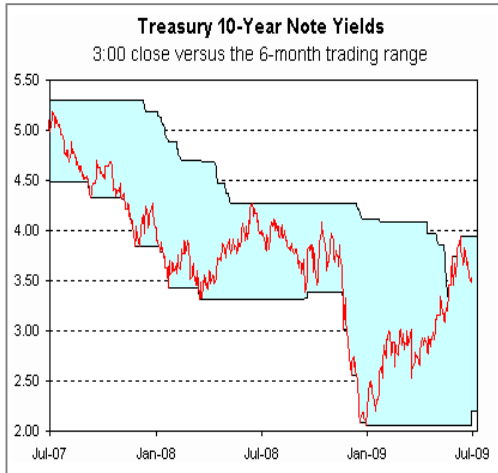
- Dow rose 0.68 pct to 8,504.06, S&P was up 0.44 pct to 923.33 and Nasdaq gained 0.58 pct to 1,845.72.
- S&P technology index rose 0.59 pct, S&P financials index fell 0.5 pct and S&P energy index rose 0.22 pct.
- KBW banks index fell 0.71 pct.
- General Mills shares rose 3.86 pct to \$58.18 after it forecasted a stronger than expected annual profit.

C & E: Oil prices fell after government data showed a build in U.S. gasoline inventories ahead of the Independence Day holiday, traditionally the peak of the summer driving season.

- U.S. crude fell 0.84 pct to \$69.29 a barrel.
- Gold rose 1.57 pct to \$940.35 an ounce.
- The Reuters-Jefferies CRB index was up 0.48 pct to 251.17.

- For MARKET SNAPSHOT click here
- For NEXT UP click here
- For DEEP DIVE click here

MARKET SNAPSHOT as of 3:00 pm EST



TREASURIES <5> <500>

	BID	ASK	YIELD	CHANGE
1-Mo Bill	0.170	0.135	0.172	0.01
3-Mo Bill	0.170	0.160	0.172	-0.015
6-Mo Bill	0.320	0.310	0.325	-0.021
1-Year	0.530	0.523	0.540	-0.015
2-Year	100.141	100.172	1.054	0.133
3-Year	100.930	100.961	1.552	0.211
5-Year	100.523	100.570	2.513	0.219
7-Year	100.281	100.328	3.205	0.055
10-Year	96.531	96.578	3.544	-0.047
30-Year	98.484	98.547	4.341	-0.125

EQUITIES

	INDEX	CHANGE
DJIA	8504.06	57.06
NASDAQ	1845.72	10.68
S&P 500	923.28	3.96

OIL

	PRICE	CHANGE
NYMEX	69.3	-0.6
BRENT	68.8	-0.5

EURODOLLAR FUTURES

	CLOSE	CHANGE
Jul-09	99.403	0.000
Sep-09	99.355	0.000
Dec-09	99.145	0.005
Mar-10	98.890	0.000

FUTURES

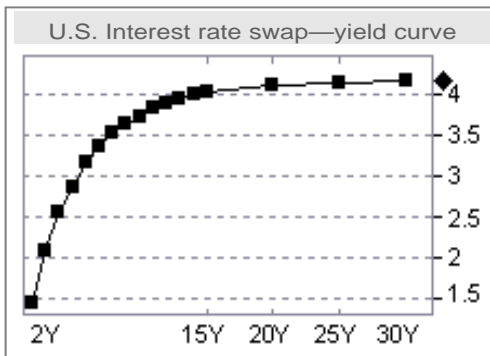
	PRICE	CHANGE
CBOT 5 yr	114.96	0.24
CBOT 10 yr	116.30	0.03
CBOT 30 yr	118.36	0.00

REPURCHASE AGREEMENTS

G/C		MORTGAGE REPOS	
O/N	0.250	O/N	0.300
2-Week	0.250	2-Week	0.300
1-Month	0.300	1-Month	0.300
3-Month	0.300	3-Month	0.350
AGENCY REPOS		i-REPO SM INDEX	
O/N	0.300	10:00 AM	0.190
2-Week	0.300	3:00 PM	0.199
1-Month	0.300		
3-Month	0.350		

IR SWAPS <19901>

	SPREAD		RATE	
2-Year	41.25	45.25	1.46	1.48
3-Year	51.75	55.75	2.07	2.08
5-Year	39.75	43.75	2.91	2.91
7-Year	18.50	22.50	3.39	3.38
10-Year	21.50	25.50	3.75	3.74
30-Year	-16.75	-12.75	4.17	4.15



CURRENCIES

	BID	ASK
Euro	1.4153	1.4156
Sterling	1.6477	1.6482
JP Yen	96.49	96.52
Swiss Franc	1.0744	1.0748
Can Dollar	1.1485	1.1492
Mexico	13.1109	13.1170

FED FUNDS NYFRSM - 10AM

Open	0.2200	1m	0.3225
High	0.3000	3m	0.6137
Low	0.1250		

EURODOLLAR DEPOSITS & OIS STRIPS (ASKED)

	BID	ASK	BID	ASK
O/N	0.200	0.250	-	-
1-Month	0.250	0.650	0.212	0.222
3-Month	0.450	1.050	0.220	0.230
6-Month	0.900	1.400	0.265	0.275
12-Month	1.400	2.050	0.471	0.481

ACTIVE FANNIE MAE AGENCIES

TERM	COUPN	MATURITY	YIELD-SPREAD	YIELD
2-Year	1.375	28/04/2011	14 0	1.24
3-Year	1.875	20/04/2012	20 18	1.8
5-Year	3	28/07/2014	38 36	2.95
7-Year	5	15/03/2016	34.75 34.25	3.55
10-Year	-	-	-	-
30-Year	6.625	15/11/2030	0 53	-

ACTIVE FREDDIE MAC AGENCIES

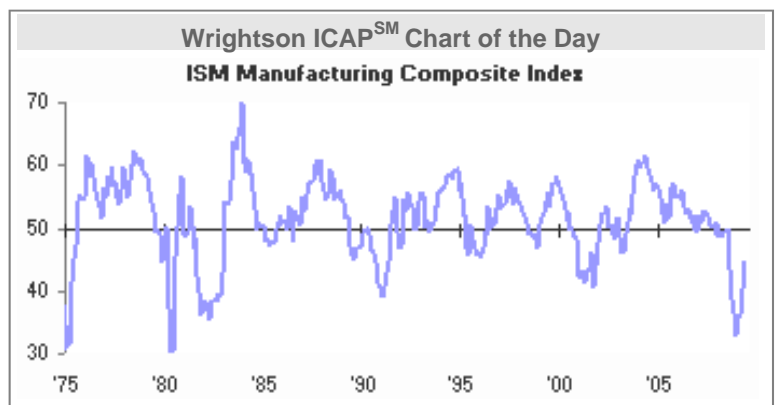
TERM	COUPN	MATURITY	YIELD-SPREAD	YIELD
2-Year	1.625	26/04/2011	13.5 0	1.23
3-Year	1.75	15/06/2012	0 24.5	-
5-Year	2.5	15/05/2014	34 0	2.92
7-Year	4.75	19/01/2016	30 0	3.54
10-Year	3.75	27/03/2019	41.5 40	3.96
30-Year	6.25	15/07/2032	49 48.5	4.83

Active MBS 15YR

	CPN	BID	ASK	YIELD
FNMA	5.0	103.1400	103.1600	3.594
FHLMC	5.0	103.0670	103.0870	3.652
GNMA	5.0	103.1330	103.1530	3.924

Active MBS 30YR

	CPN	BID	ASK	YIELD
FNMA	5.5	103.0410	103.0610	3.839
FHLMC	5.5	103.0310	103.0510	3.853
GNMA	5.5	103.0630	103.0830	4.471



TODAY'S TOP NEWS

U.S. jobs gloom overshadows manufacturing glimmers

U.S. manufacturing mustered its highest level of activity in nearly a year in June but unexpected weakness in private sector employment signaled how slow an economic recovery might be, reports showed.

U.S. private employers slashed a bigger-than-expected 473,000 jobs in June, according to a report from ADP Employer Services.

However, the ADP report showed the pace of private job losses slowed from the 485,000 lost in May.

U.S. manufacturing shrank in June but at a slower pace than in May. The ISM said its index of national factory activity edged up to 44.8 from 42.8 in May and above economists' median forecast for 44.5. A reading below 50 indicates contraction.

Another report said pending U.S. sales of previously owned homes edged up 0.1 percent in May, for the fourth straight monthly gain.

U.S. construction spending fell 0.9 percent in May, however, to the lowest rate in more than five years, showing an economic stimulus plan passed in February had given little relief to public construction.

The Mortgage Bankers Association said its U.S. mortgage applications index fell 18.9 percent in the week to June 26 to its lowest since November, despite slightly lower borrowing costs.

U.S. interest rates seen hinging on Fed's exit strategy

U.S. interest rates in the second half will likely move on perceptions of how the Federal Reserve handles paring its burgeoning balance sheet and ending emergency funding programs, analysts said.

There have been growing concerns over the inflation fallout from the Fed's moves to bail out the economy after the credit crisis last autumn.

The Fed's unconventional funding programs, adoption of a near-zero rate policy and buying of Treasuries have helped to stabilize the economy, analysts say, but it is unclear how the bond market and economy will respond whenever the Fed moves away from the bailout programs.

An end to the Fed's emergency measures poses a "cliff-effect" risk for the bond market, according to Morgan Stanley.

They forecast benchmark 10-year Treasury note yields could push toward 4.25 percent by the end of the year, almost 0.70 percentage point above current levels. Short-term yields on the other hand will likely stay steady.

They also expect increased volatility and higher risk premiums on spread products like mortgage-backed securities.

U.S. SEC proposes say on pay for TARP companies

U.S. securities regulators proposed giving investors a greater say on executive pay at companies that have received taxpayer funds, as requested by Congress.

The SEC voted unanimously to give shareholders an advisory vote on executive pay at more than 500 companies that received funds under the TARP.

IMF staff have recommended the IMF issue no more than \$150 billion in debt as a way to raise funding for the global institution, IMF board sources said.

IMF staff have recommended the IMF issue no more than \$150 billion in debt as a way to raise funding for the global institution, IMF board sources said.

China requests reserve currency debate at G8 -sources

China has asked to debate proposals for a new global reserve currency at next week's Group of Eight summit in Italy and the issue could be referred to briefly in the summit statement, G8 sources said.

One G8 source who was involved in the negotiations said China made the request during preparatory talks about a joint statement to be issued on the second day of the summit in L'Aquila by the G8 plus the G5 and also Egypt.

This forum, meets on July 9 to discuss the financial crisis, trade and climate change and for the first time a G8 summit will also produce a joint G14 statement.

A European source with knowledge of preparations for the summit also said China had raised the subject of a reserve currency debate and that it might be mentioned during the meeting, though the source added: "Any country at the meeting can raise issues they see fit."

The debate centers on proposals by some emerging powers that an alternative should be found to the U.S. dollar as the global reserve currency, to reflect the shifting balance of power in the globalize economy.

U.S. to pull GM funding if sale not done by July 10

The only viable option to save General Motors Corp is a sale of its main assets to a "New GM" backed by the federal government, a U.S. Treasury official told a bankruptcy court as the automaker sought approval for the deal.

The official, Harry Wilson, also said the government would withdraw its portion of the \$33 billion "debtor-in-possession" financing for GM if the sale of the main assets did not close by the government's July 10 deadline.

Wilson estimated that GM has received \$10 billion in funding since its bankruptcy filing. The U.S. government provided the bulk of the funding, with about 15 percent coming from the Canadian government, he said.

Under questioning from a lawyer representing personal injury claimants, Wilson said the government did feel obliged to take on liability claims if they prevented New GM from being viable.

A successful sale of GM's main assets would be the second big victory for the Obama administration's autos task force.

M.Stanley, MUFG in loan sharing alliance

Morgan Stanley and its biggest shareholder, Japan's Mitsubishi UFJ Financial Group, have agreed to pool their lending resources under an agreement designed to help win more investment banking business.

The agreement, which expands an existing relationship between the two banking groups, calls for a joint venture to provide loans to companies across North America. Combined loan commitments to U.S. firms would be more than \$100 billion.

Mitsubishi UFJ said the agreement will help its overseas expansion, which has lagged that of major global players. The alliance also covers operations in Asia, Europe, the Middle East and Africa.

MUFG said the alliance is expected to contribute 30 billion yen in gross profit for the year to March 2012.

In a separate report, Bank of America Corp's primary investment management unit is drawing lower than expected bids after its likeliest suitor, BlackRock Inc, inked a blockbuster deal to buy Barclays Global Investor, the Financial Times reported, citing people close to the matter.



TODAY'S TOP NEWS

U.S. oil product stocks up sharply, crude down - EIA

U.S. gasoline and distillate stocks rose sharply due to weak demand last week, while crude oil inventories fell more than expected, according to data from the U.S. EIA released.

Gasoline inventories rose 2.3 million barrels to 211.2 million barrels ahead of the July 4th holiday weekend, normally a time of increased demand. Analysts polled by Reuters had forecast a 1.9 million barrel build.

Crude oil stockpiles fell 3.7 million barrels to 350.2 million barrels in the week to June 26, compared to an expected draw of 2 million barrels.

Distillate stockpiles, which include diesel and heating oil, rose 2.9 million barrels to 155 million barrels against analyst projections of a 1.5 million barrel build.

Euro zone factory PMI rises but Germany lags

The euro zone manufacturing economy contracted less than initially thought in June but there was a significant difference among countries with Germany lagging behind, a survey showed.

The Markit Eurozone Manufacturing PMI for June rose to 42.6 from 40.7 in May, its highest since last September and above the 42.4 flash estimate.

The PMI rose last month on an improved outlook in the decline of new orders taken on. The new orders index rose to 44.9 from 42.2 in May, its highest level since June last year.

Yet the euro zone economy contracted by 2.5 percent in the first three months of the year, and is not expected to grow until the fourth quarter of this year at the earliest.

German retail sales rose 0.4 percent on a monthly basis in May, the third consecutive monthly increase but the country's leading retail group warned that sales would shrink this year as job losses pile up.

Interbank rates at fresh lows as new qtr starts

The rates banks charge each other for dollars, euros and sterling marked fresh record lows with massive central bank cash injections expected to keep money markets rates depressed into the third quarter.

Interbank borrowing costs continued their grind lower as markets await the outcome of the ECB's policy meeting on Thurs-

day widely expected to keep interest rates on hold at a lifetime lows.

Three-month Libor on euros and dollars declined to all-time lows of 1.07375 pct and 0.58750 percent respectively. The equivalent rate for sterling also plumbed record low of 1.17750 percent.

The spread between three-month Libor and OIS narrowed by five basis points to 48 basis points for euro.

UK factory PMI hits 13-mth high as recession eases

Hopes that Britain's economy is emerging from recession got a boost from data which showed less of a decline in services and manufacturing activity, though doubts remain about the durability of any recovery.

Britain's main manufacturing survey, the CIPS/Markit manufacturing purchasing managers' index, rose to 47.0 last month from 45.4 in May -- the highest since May 2008 and just ahead of analysts' forecasts for smaller improvement to 46.5.

Manufacturing output grew for the first time since last March, with an index reading of 52.1 up from 48.1 in May, though the overall index, which includes hiring intentions and other elements, still shows a modest contraction in overall activity.

The PMI survey showed the new orders index rose to its highest since March 2008 and the export orders index also improved. The employment index also rose to show the slowest pace of job-shedding since last August.

Japan firms' grim mood to put BOJ exit plans on ice

Japanese business morale improved less than expected in June, plagued by doubts about the global economy, giving the central bank little room to retreat from ruptured corporate finance markets.

The survey's main sentiment index for big manufacturers improved to minus 48 in June from a record low of minus 58 in the previous quarterly survey in March, the first rise in two and a half years.

That was still worse than a median forecast in a Reuters poll of minus 43, and pessimists still far outnumbered optimists.

Meanwhile, Japan's public pension fund said it posted a record loss of almost \$100 billion in the last financial year, hit hard by the global financial crisis and a sharp appreciation in the yen.

NEXT UP

POLL-U.S. jobless rate in June seen highest since 1983

The U.S. economy likely shed a further 355,000 jobs in June and the unemployment rate hit a 26-year high, but for a nation mired in its deepest recession since at least World War Two that may be good news.

The U.S. Labor Department's report due on Thursday is expected to depict an economy still wallowing in recession but confirm that the pace of job loss has slowed, which would suggest the 18-month-old recession is easing its grip.

The report, which will be dissected by financial markets for clues on the economy, is expected to show the unemployment rate rose to 9.6 percent -- its highest since June 1983 -- from 9.4 percent in May, according to a Reuters poll of economists.

While still severe, that would be in line with the 345,000 positions eliminated in May and would reflect a sharp slowing in job losses for an economy that shed an average of 691,000 jobs a month in the first quarter.

ECB to hold rates at record low, take stock of actions

The European Central Bank is expected to keep euro zone interest rates unchanged on Thursday, say it sees faint signs of economic recovery and fill in some of the missing details of its unorthodox plan to buy bonds.

Eighty-one of 82 economists polled by Reuters forecast the ECB would leave the refinancing rate at 1.0 percent, and the Governing Council will probably repeat that rates are appropriate at the current record low.

The ECB is likely to refrain from any new policy steps so it can take stock of its unconventional measures to tackle the euro zone recession -- last week's injection of almost half a trillion euros of ultra-cheap funding into money markets, and the soon-to-be-launched program to buy 60 billion euros' worth of mortgage and public debt-backed bonds.



DEEP DIVE Commentary and Analysis

ANALYSIS-Crusading U.S. FTC faces financial reforms set

By Diane Bartz

A White House plan to create a new U.S. agency to enforce consumer protection rules for banks and mortgage lenders is a bitter pill for the Federal Trade Commission, which had sought more power to fight financial fraud, but could now see the proposal taken away altogether.

The FTC, which enforces antitrust and some consumer protection laws, is one of six federal regulators that will be affected by the proposed Consumer Financial Protection Agency. The new agency would fight abusive practices employed during the recent housing and credit boom such as poor mortgage loan disclosures and "fee traps" on credit cards.

"Every power that this (proposed) agency has comes from somebody else and that means turf war," said Scott Talbott, chief lobbyist for the Financial Services Roundtable, which represents 100 major financial services organizations.

"I think that there is a political wind to create this agency," he said, arguing for a bill that would put consumer protection and bank solvency under the same agency.

Created in 1914 as a trust-busting agency to prevent unfair business competition, the FTC also pursues consumer-oriented scams such as hidden fees in prepaid calling cards, credit repair scams and fake foreclosure prevention schemes.

FTC Chairman Jon Leibowitz said that there were details to work out in how the new agency would work, if it is created.

"We applaud the president's efforts," Leibowitz told Reuters. "What he wants to do is far better than the status quo."

The Obama administration's legislative plan, if approved, would mean a loss of prestige for the FTC. Agency chairman Leibowitz went before a congressional panel on March 31 to ask for expanded power to bring civil penalties for deception or other misdeeds in financial services.

"If Congress looks to create one consumer protection entity ... we believe that we are best-suited at the commission to play that role," Leibowitz told Reuters in April.

Under the bill, the agency could lose about 60 of the nearly 200 lawyers in its consumer protection staff, said Joel Winston, associate director of the FTC's financial practices division.

"It's significant, but well less than the majority," said Winston, who said the bill could mean the loss of enforcement authority aimed at preventing deception in mortgage lending, credit reporting, debt collecting and data security for financial institutions.

A DIFFERENT DRUG WAR

The proposal was released as the FTC moved aggressively on another front -- opposing deals between brand name pharmaceutical companies and generic rivals that delay the entry of generic drugs to the marketplace.

The FTC has sued companies that made the deals and recently released a report showing the settlements -- which they say may violate antitrust law -- and cost U.S. consumers \$3.5 billion per year. The campaign has raised eyebrows in the Washington antitrust community.

"I think that the FTC's position that reverse payments ... are almost always anti-competitive, that's mistaken," said Bruce McDonald, a former Justice Department deputy assistant attorney general.

McDonald, now with the law firm Jones Day, said the proposal to create a new agency was, "a setback for the FTC because they've been working hard to pursue their consumer protection agenda."

The FTC has made a big push recently on fraud and misrepresentation in loan modifications, mortgages and foreclosures,

said David Turetsky of Dewey LeBoeuf LLP.

"You always worry a little bit when things get reshuffled because you don't want this kind of work to slow down or be interfered with," said Turetsky.

"In Washington, there's a lot of focus on jurisdiction and who wins and who loses," he added. "The real focus has to be on what's good for consumers."

Small U.S. banks fear new regulations may be costly

By Chavon Sutton

Community banks that avoided the excesses of the lending boom and survived the financial crisis without too much trouble are now increasingly worried that they will get penalized by the U.S. government's regulatory crackdown.

While there was reckless behavior by some of America's smaller banks, and a number are paying the ultimate price through failure and government seizure, there were many who stuck to conservative lending practices and turned away business if it was high risk.

The Obama Administration is proposing a raft of new regulations aimed at preventing banks and other companies from taking on risks that could again threaten the whole global financial system.

The only problem -- the demands of the new regime could hurt smaller banks more than their larger brethren.

"We support the strong systemic risk regulation over too big to fail institutions because it will protect taxpayers and the economy from future economic crises, said Karen Thomas, executive vice president of government relations for the Independent Community Bankers Association (ICBA).

"But we want the reform to be more targeted to those institutions that caused the problems, not community banks."

Community banks say the proposals to create a new Consumer Financial Protection Agency, remove the thrift charter, and require banks to hold a financial interest in loans they originate, are among changes that put an undue burden on some of the institutions that did not engage in abusive practices.

"It seems to me that we already have strong and strict consumer protections," said Frederick Schea, Chief Executive of First Savings Bank of Perkasie, an Upper Bucks County, Pennsylvania bank with \$1.1 billion in assets.

He said the creation of a new agency will likely lead to "additional fees on top of already high fees we pay for FDIC deposit insurance and other regulatory fees."

HITTING EARNINGS

These fees can soon cut into margins.

For example, River Valley Financial Bank, an Indiana-based bank with \$384 million in assets, pays \$80,000 annually in regulatory fees. Last year, it reported \$2.5 million of net income, making regulatory fees equivalent to three percent of its earnings.

"I'm not happy about having a new regulator for compliance because another one could cost up to an additional \$80,000 for us," said Matthew Forrester, the CEO of the bank.

Other related costs include limits on leverage and expenses for compliance and audit staff.

Some of these costs went up after the 2002 Sarbanes-Oxley corporate governance law, passed in response to the Enron and WorldCom scandals. The law was much criticized in corporate circles for increasing the cost of auditing.

"This is one of our fears," said Forrester. "I hope it doesn't go off track like Sarbanes-Oxley did."

Community banks may also face additional costs as proposed changes include the axing of the Office of Thrift Supervision.



DEEP DIVE Commentary and Analysis

There is a possibility that banks now under the OTS umbrella will have to pay charter conversion fees as a result.

But consumers will also feel the pinch in the form of higher loan fees, lower rates for deposits, and less access to financial products, small banks say.

"The strength of our financial system is its diversity," said Thomas of the ICBA. "To overwhelm small banks with regulation will result in limited choices for consumers at a higher price."

SOME DISCOUNT IMPACT

Still some analysts say that while the impact of new regulation will be felt at the margin, it will not be broad enough to be cataclysmic.

"The top 19 banks make up about 90% of the banking system and are the plumbing of our financial system," said Tanya Azarchs, a bank credit analyst for Standard and Poor's. "If there were widespread failures of small banks, it would be disruptive and cause some dislocations to smaller communities, but not to the financial system."

But bank trade organizations say that while the top 19 might be the plumbing, the small banks are the bloodline, providing access to capital for small and niche communities, as well as America's small businesses.

"Small banks provide intangible value to the communities they serve, including volunteer hours and the bulk of small business

loans," said Diane Casey-Landry, Chief Operating Officer of the American Bankers Association. "A failure of a small bank impacts local hospitals, economic boards, and even minority groups."

According to the FDIC, the U.S. had 8,246 financial institutions as of June 2009 and of those, 7,555 had assets of \$1 billion or less.

While federal intervention, through the Troubled Asset Relief Program and other measures, is widely considered positive, small banks are saying that the system is designed to look after the larger banks.

"What we're seeing is that there is not the same access to Capital Purchase Program funds because the solutions were not designed to work for small banks," said Casey-Landry.

According to the ABA's estimates, "it would only take \$550 million to bring all small banks up to well-capitalized and this would be valuable to communities," Casey-Landry said.

RBC Capital Markets analyst Gerard Cassidy expects 1,000 banks to fail as a result of the current economic downturn, but he says the picture isn't entirely dismal, given the sheer number and role of community banks in America.

"We're never going to be a country like Canada with five banks," said Cassidy. "The community bank is woven into the fabric of this country and will always be here."

INSIDE DEBT is produced by Reuters in partnership with ICAP.

(Compiled by Anil Kumar and Lokesh Jain in Bangalore)

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