

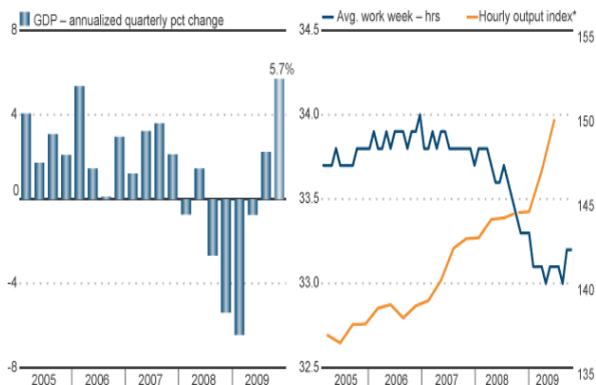
INSIDE DEBT

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Friday, January 29, 2010

CHART OF THE DAY

U.S. GDP and productivity



The U.S. economy grew at a faster-than-expected 5.7 percent pace in the fourth quarter, the quickest pace in more than six years as businesses reduced inventories less aggressively.

TODAY'S TOP NEWS

- U.S. economy up 5.7 pct in Q4, fastest in 6 years
- Obama unveils \$33 billion tax credit to boost jobs
- Fed's Kohn warns on interest rate risk
- FDIC's Bair says proprietary trading ban positive
- Greece and EU close ranks, say no bailout
- U.S. may exempt Treasuries from new bank tax-sources
- Ebbing U.S. home sales hint prices may fall again

ECON WATCH

FOR MONDAY FEBRUARY 1

ET	Indicators	Unit	Reuters	Prior
02:45	FR Producer prices mm	ind	0.1	0.2
03:43	IT Markit/ADACI Mfg PMI	ind	51.2	50.8
03:48	FR Markit/CDAF Mfg PMI	ind	54.7	54.7
03:53	DE Markit/BME Mfg PMI	ind	53.4	52.7
03:58	EZ Markit Mfg PMI	ind	52.0	51.6
04:28	GB CIPS/Markit Mfg PMI	ind	54.0	54.1
04:30	GB BoE consumer Credit	bln	-0.40	-0.376
04:30	GB Mortgage Lending	bln	1.55	1.459
04:30	GB Mortgage Approvals	k	62.0	60.518
08:30	US Personal income	%	0.3	0.4
08:30	US Personal Construct	%	0.3	0.5
08:30	US PCE price index	%	-	0.2
08:30	US Core PCE price index	%	0.1	0.0
08:30	US Real Pers spending	%	-	0.2
10:00	US Construction spending	%	-0.5	-0.6
10:00	US ISM	ind	55.2	54.9
10:00	US ISM Prices paid	ind	62.7	61.5

MARKETS TODAY

TODAY'S TOP STORY: The U.S. economy grew at a faster-than-expected 5.7 percent pace in the fourth quarter, the quickest in more than six years, as businesses made less-aggressive cuts to inventories and stepped up spending. **For more please click here**

TREASURIES: U.S. Treasuries rose on month-end position-squaring, nervousness about the fiscal health of some European nations and expectations the U.S. economy's growth pace in the fourth quarter was unsustainable.

- 30-yr bond prices rose 24/32 to yield 4.50 pct down from 4.55 pct.
- 10-yr Treasury prices were up 10/32 yielding 3.60 pct, rebounding from an earlier 13/32 decline.
- 5-yr notes jumped 8/32 to yield 2.34 pct.
- 2-yr Treasury prices rose 2/32 yielding 0.83 pct.

FOREX: The dollar rose against major currencies after a slew of stronger-than-expected data boosted the view the U.S. economy was recovering faster than other developed countries.

- Dollar index was up 0.73 pct at 79.481 after hitting a high of 79.444, the strongest level since mid-August.
- Dollar rose 0.47 pct to 90.29 yen, after climbing to 90.92 yen.
- The euro fell 0.77 pct to \$1.3864. Earlier it fell to \$1.3863, the lowest since July 9. It rose against the Swiss francs to 1.4706 francs.

CORPORATES: U.S. corporate bond spreads were slightly tighter after strong GDP data from the United States.

- The CDX.IG-13 index tightened by 1 bps to 96 bps.
- U.S. 5-yr CDS rose to 45.25 bps late on Thursday, the widest since June 2009, and were last at 42.5 bps.
- The cost of insuring Greek government bonds fell to 399,500 euros per 10 million of exposure from a record 422,500 euros at the New York close on Thursday.

STOCKS: U.S. stocks fell, erasing an earlier advance, as worries about fiscal turmoil in Europe and a drop in technology stocks offset positive reports on the U.S. economy.

- Dow was down 0.54 pct to 10,065.97, S&P fell 0.98 pct to 1,073.90 and Nasdaq shed 1.45 pct to 2,147.35.
- Shares of Apple lost 3.6 pct to \$192.12 and ranked as the heaviest weight on the Nasdaq, while Microsoft Corp was down 3.36 pct to \$28.18.
- The semiconductor index fell 3.42 pct, while SanDisk Corp tumbled 11.67 pct to \$25.42.
- S&P financial index fell 0.67 pct, S&P technology shed 2.05 pct.
- KBW bank index fell 0.60 pct.

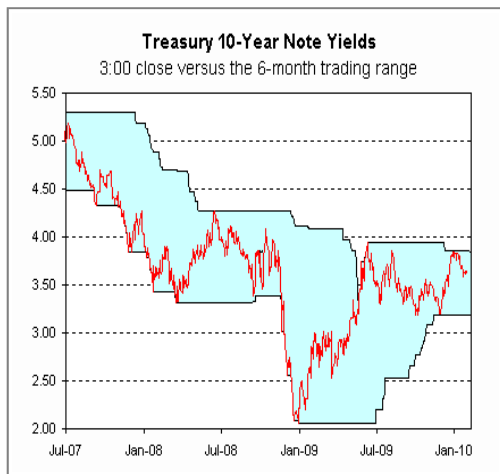
C & E: Oil prices fell 1 percent, marking a more than 8 percent loss for the month, as lagging energy demand outweighed stronger-than-expected U.S. economic data.

- U.S. crude prices fell 1.26 pct to \$72.71 per barrel.
- Gold was down 0.53 pct to \$1,081 an ounce.
- Reuters-Jefferies index fell 0.74 pct to 265.59.

- 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	0.015	-0.015	0.015	0.001
3-Mo Bill	0.080	0.070	0.081	-0.001
6-Mo Bill	0.145	0.135	0.147	-0.002
1-Year	0.285	0.275	0.290	0.001
2-Year	100.055	100.086	0.848	0.043
3-Year	99.977	100.016	1.384	0.074
5-Year	99.477	99.523	2.362	0.156
7-Year	100.172	100.219	3.097	0.172
10-Year	97.984	98.047	3.621	0.172
30-Year	97.625	97.703	4.521	0.516

EQUITIES

	INDEX	CHANGE
DJIA	10097.33	-23.13
NASDAQ	2147.04	-31.96
S&P 500	1077.89	-6.64

OIL

	PRICE	CHANGE
NYMEX	72.7	-1.0
BRENT	73.2	1.1

EURODOLLAR FUTURES

	CLOSE	CHANGE
Feb-10	99.735	-0.003
Mar-10	99.710	0.000
Jun-10	99.590	-0.005
Sep-10	99.350	0.010

FUTURES

	PRICE	CHANGE
CBOT 5 yr	116.01	0.27
CBOT 10 yr	117.52	-0.19
CBOT 30 yr	117.97	-0.19

CURRENCIES

	BID	ASK
Euro	1.3871	1.3874
Sterling	1.5993	1.5998
JP Yen	90.29	90.32
Swiss Franc	1.0601	1.0604
Can Dollar	1.0680	1.0684
Mexico	13.0542	13.0598

FED FUNDS

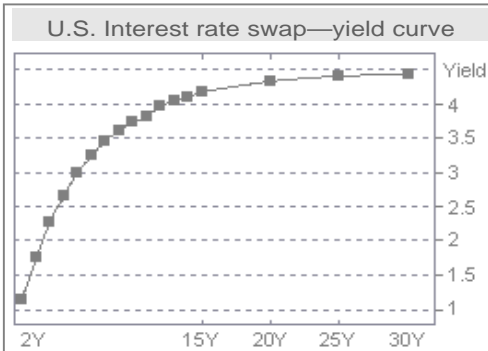
	NYFR SM - 10AM
Open	0.1300 1m 0.2037
High	0.1600 3m 0.2381
Low	0.1000

REPURCHASE AGREEMENTS

G/C		MORTGAGE REPOS	
O/N	0.180	O/N	0.210
2-Week	0.200	2-Week	0.200
1-Month	0.210	1-Month	0.210
3-Month	0.210	3-Month	0.240
AGENCY REPOS		i-REPO SM INDEX	
O/N	0.180	10:00 AM	0.120
2-Week	0.200	3:00 PM	0.116
1-Month	0.210		
3-Month	0.220		

IR SWAPS <19901>

	SPREAD		RATE	
2-Year	26.25	30.25	1.10	1.13
3-Year	34.25	38.25	1.72	1.73
5-Year	29.00	33.00	2.65	2.65
7-Year	13.50	17.50	3.23	3.22
10-Year	10.75	14.75	3.72	3.71
30-Year	-12.00	-8.00	4.40	4.38



EURODOLLAR DEPOSITS & OIS STRIPS (ASKED)

	BID	ASK	BID	ASK
O/N	0.120	0.150	-	-
1-Month	0.180	0.280	0.125	0.135
3-Month	0.240	0.400	0.140	0.150
6-Month	0.250	0.450	0.169	0.179
12-Month	0.700	1.000	0.323	0.333

ACTIVE FANNIE MAE AGENCIES

TERM	COUPN	MATURITY	YIELD-SPREAD		YIELD
2-Year	0.875	12/01/2012	11.5	10	1.01
3-Year	1.375	09/01/2013	23.5	21.5	1.61
5-Year	2.875	09/02/2015	32	31	2.68
7-Year	5.125	18/10/2016	23	20	3.32
10-Year	-	-	-	-	-
30-Year	6.625	15/11/2030	38.25	37.75	4.9

ACTIVE FREDDIE MAC AGENCIES

TERM	COUPN	MATURITY	YIELD-SPREAD		YIELD
2-Year	1.125	15/12/2011	9	0	0.96
3-Year	1.75	22/02/2013	30	29	1.68
5-Year	2.625	20/11/2014	18.5	17.5	2.54
7-Year	5.25	15/09/2016	16.75	16.25	3.26
10-Year	3.75	27/03/2019	25	24	3.87
30-Year	6.25	15/07/2032	41.25	40.75	4.93

Active MBS 15YR

	CPN	BID	ASK	YIELD
FNMA	5.0	105.1820	105.2020	2.562
FHLMC	5.0	105.1720	105.1920	2.575

Active MBS 30YR

	CPN	BID	ASK	YIELD
FNMA	5.5	105.2610	105.2810	2.851
FHLMC	5.5	105.2910	105.3110	2.754
GNMA	5.5	105.2400	105.2600	3.537

Wrightson ICAPSM Chart of the Day

Real GDP: Year-over-Year Growth Rate



TODAY'S TOP NEWS

U.S. economy up 5.7 pct in Q4, fastest in 6 years

The U.S. economy grew at a faster-than-expected 5.7 percent pace in the fourth quarter, the quickest in more than six years, as businesses made less-aggressive cuts to inventories and stepped up spending.

The robust performance closed out a year in which the economy contracted 2.4 percent, the biggest decline since 1946.

In a further boost to recovery hopes, the ISM-Chicago said its business barometer rose to 61.5 in January, the highest in four years, from 58.7 in December.

Consumers grew more confident this month, another survey showed, which should support spending in the months ahead. The Reuters/University of Michigan Surveys of Consumers' January consumer sentiment rose to 74.4 from 72.5 in December. Consumer spending increased at a 2 percent annual rate in the fourth quarter, contributing 1.44 percentage points to GDP. Business investment grew at a 2.9 percent rate, the first increase since the second quarter of 2008, as the drag from the troubled commercial real estate sector was offset by robust spending on equipment and software.

A separate report from the Labor Department showed employment costs rose 0.5 percent in the fourth quarter, just a touch higher than analysts had expected.

Fed's Kohn warns on interest rate risk

A senior U.S. Federal Reserve official warned that the uncertain path of interest rates poses risks for banks inattentive to the match of durations among their assets and liabilities.

Federal Reserve Vice Chairman Donald Kohn told a conference sponsored by the FDIC that the usual uncertainty about interest rates in coming months is compounded in the current situation by the fact that rates are near zero and the Fed has massively expanded the amount of reserves in the banking system.

Kohn said the Fed would stick to that commitment if the economy follows the trajectory expected by the Fed.

When and how fast rates rise depends on the outlook for growth and inflation, Kohn said.

Economists expect only modest growth accompanied by a slow decline in the unemployment rate over the next few years, he said.

The Fed vice chairman suggested that longer-term interest rates may well rise as the Fed raises borrowing costs.

Greece and EU close ranks, say no bailout

Greek and European Union officials closed ranks, insisting there was no chance of a Greek default or an EU bailout and that Athens would do whatever it takes to cut its burgeoning deficit.

"Solidarity is possible, will exist. A bailout is not possible and will not exist," EU Monetary Affairs Commissioner Joaquin Almunia told Reuters Insider TV.

Greek Prime Minister George Papandreou, also at the World Economic Forum in Davos, promised to do all that was required to cut the deficit and restoring confidence.

The euro zone has pledged to cut its budget deficit this year to 8.7 percent of GDP from over 12 percent and return to the EU's 3 percent cap by 2012.

But fears that Athens will not be able to rein in spending have continued to haunt markets and put pressure on the euro, fueling speculation the euro zone would eventually step in.

A senior euro zone official said that there were no formal talks or preparations in any European institutions to help Greece financially and that the EU strategy towards Greece was to continue pressing hard for budget cuts.

Obama unveils \$33 billion tax credit to boost jobs

President Barack Obama proposed \$33 billion in tax credits to coax small businesses into hiring workers as he underscored his commitment to pushing job creation to the top of his agenda. With public frustration over double-digit unemployment eroding his popularity, Obama has begun rolling out initiatives aimed at backing up his jobs pledge made in his economy-focused State of the Union Address earlier this week.

The latest proposal calls for a \$5,000 tax credit for every net new worker hired in 2010. The amount would be capped at \$500,000 per firm to make sure that the bulk of the benefits go to small businesses. He insisted that more work was needed to spur employment and urged the U.S. Senate to push ahead with jobs legislation. The House of Representatives approved a \$155 billion jobs bill in December.

Obama said his tax credit proposal could help small businesses to hire workers while lowering their taxes. He estimated that more than 1 million small businesses could benefit.

Small businesses are the biggest source of job creation and hold the key to reducing unemployment, so funneling money their way is a smart approach. The problem is, even though the economy has resumed growing, confidence is in short supply, leaving these companies reluctant to hire, economists say.

FDIC's Bair says proprietary trading ban positive

Top U.S. bank regulator Sheila Bair said that proposed proprietary trading limits are "very positive," but said they would not have necessarily reined in risk-taking at the institutions that required massive bailouts.

The proposal is designed to prevent banks from using insured deposits to bankroll their own risky bets.

Bair, chairman of the FDIC, said the proposal is helpful, but said major commercial banks were not at the heart of the financial crisis that brought international markets to the brink of collapse.

Treasury Secretary Timothy Geithner has said that risky lending practices, not necessarily risky trading practices such as proprietary trading, were at the root of the crisis.

U.S. regulators must get a better handle on interest rate risks at banks "before it's too late," Bair said.

She added that a thorough evaluation must be done at all institutions to protect them against increases in rates, which could threaten the easy earnings that have helped heal the banking system during the credit crunch.

U.S. may exempt Treasuries from new bank tax -sources

The Obama administration is considering exempting U.S. Treasuries from its proposed new tax on banks in order to prevent disruption in the world's most important funding market, market sources said.

Wall Street fears President Barack Obama's proposed tax to recover bailout funds could deter banks from tapping short-term loans in the repurchase market ultimately making borrowing more expensive.

Bankers have taken their concerns to the Treasury Department, which says it is aware of the potential pitfalls and is weighing ways to side-step them.

Sources familiar with the discussions said the suggestions included a carve-out for Treasury securities in the assessment of the new tax -- which the White House wants to levy on non-deposit liabilities of banks with assets over \$50 billion -- or a method of risk-weighting assets so that riskier instruments would be taxed at a higher rate than safer, more liquid securities such as Treasuries.



TODAY'S TOP NEWS

Ebbing U.S. home sales hint prices may fall again-S&P

A recent decline of U.S. home sales is swelling the supply of houses and may push prices down, adding to losses from an earlier three-year slide, said rating agency S&P's in a statement. "While home prices have been trending up since spring 2009, existing, new and pending home sales are waning, which suggests that lower prices are on the horizon," said the statement. Market analysts and policymakers at the Federal Reserve are closely watching the battered housing sector and the weak jobs market to gauge whether the U.S. economy can go on growing and to determine when the central bank may start raising interest rates. The recent fall in home sales is boosting the number of existing homes on the market, which grew to a 7.2 months supply in December from 6.5 months in November, S&P said. In coming months, "an expanding default and foreclosure pipeline of 2005-2007 vintage mortgage loans may push the 'shadow' inventory of distressed U.S. housing even higher," which could impede the market's stability, S&P added.

Banks expect to toughen lending rules further-ECB

Banks in the euro zone expect to continue toughening their credit rules for firms and households in the first part of 2010, despite hopes the tightening cycle had peaked, the ECB said. A net 4 percent of banks said they saw themselves tightening credit standards to firms in the first quarter, compared with the net 3 percent that toughened lending requirements in Q4 of 2009. House buyers and consumers also face a tougher time getting credit over the next few months, the survey indicated, despite previous hopes that the worst of the lending clampdown may have passed. On firms' prospects, the report said: "Looking forward, euro area banks expect some further tightening of credit standards on loans to non-financial corporations in the first quarter of 2010, with net tightening potentially worsening slightly." Consumers face a similar story. A net 10 percent of banks tightened rules on consumer lending in Q4, while there was disappointing news regarding Q1.

Japan's finmin presses BOJ for deflation response

Japan's finance minister urged the Bank of Japan to align policy with the deeply indebted government's efforts to fight deflation, maintaining pressure for possible monetary easing or even government bond purchases. BOJ Governor Masaaki Shirakawa did not rule out any policy options but reiterated that the central bank's current level of bond buying was appropriate for now. Some policymakers have called on the BOJ to step up purchases to tame rising bond yields, which threaten an economic recovery. Prime Minister Yukio Hatoyama echoed his finance chief, Naoto Kan, in calling for BOJ cooperation, telling parliament that the government will work with the central bank to overcome falls in prices. The BOJ has been hesitant to increase its bond buying further, arguing that doing so would give markets the impression the bank is underwriting public debt. The central bank, under pressure from the government, has toughened its stance on deflation and on Dec. 1 decided to offer commercial banks more short-term funds.

Euro zone inflation below consensus, seen staying low

Euro zone inflation rose much less than expected in January, data showed, a sign that price pressures remain muted despite the nascent recovery and there was no urgency in tightening ECB monetary policy. The Eurostat estimated that consumer prices in the euro zone rose 1.0 percent year-on-year, less than market expectations of a 1.2 percent annual increase, and up from 0.9 percent in December. Economists said inflation in the euro zone could hover around 1 percent this year as rising energy and food prices will push inflation up, but declining core inflation will push it down. Separately, Eurostat said the unemployment rate in the euro zone rose to 10.0 percent of the workforce in December from a downwardly revised 9.9 percent in November -- the highest jobless rate since August 1998. But the figure was still lower than the 10.1 percent forecast by analysts polled by Reuters.

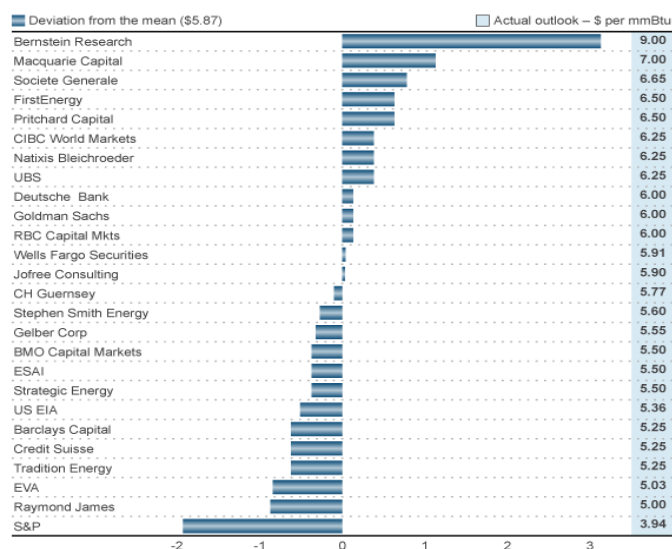
NEXT UP

U.S. natgas 2010 price forecasts hold, cold trims stocks

Energy analysts kept their forecasts for U.S. natural gas prices this year nearly steady from last quarter after a six-week cold snap this winter lifted demand and sharply cut inventories from the record highs seen at the start of the heating season. After steadily trimming their forward price outlooks last year when a deep recession and strong domestic production kept the market oversupplied, most analysts see a slightly tighter balance in 2010 as the economy improves. The Reuters quarterly poll put the consensus forecast for spot prices this year at Henry Hub, the benchmark U.S. supply point in Louisiana, at an average \$5.87 per million British thermal units, little changed from last quarter's estimate but up nearly 50 percent from 2009's average of \$3.99. Of the 26 industry participants, nine revised upward their forecasts from early October, while nine cut them. The rest were unchanged or did not participate in the previous poll. Prices are expected to climb 9 percent in 2011 to \$6.40 as demand, particularly from industrial users, picks up with the economy, but estimates for next year were scaled down by more than 6 percent from the previous quarterly poll.

But many also note that there are several factors that could limit price gains this year and in 2011.

Energy analysts maintain their outlook for 2010 U.S. natural gas prices at \$5.87 per mmBtu



DEEP DIVE Commentary and Analysis

COLUMN-Fed redux: making policy behind the curve

By John Kemp

With clear signs the U.S. and world economies have returned to growth, investors are trying to guess when the Federal Reserve will begin to raise interest rates again.

Voting to maintain the federal funds target at 0.00-0.25 percent at this week's meeting, the rate-setting Federal Open Market Committee reiterated that low rates of capacity utilization, subdued inflation trends and stable inflation expectations were "likely to warrant exceptionally low levels of the federal funds rates for an extended period".

The language echoes almost exactly the phrasing the FOMC used throughout H2 2003, when it repeatedly noted that "the Committee believes that policy accommodation can be maintained for a considerable period" (Aug, Sep, Oct and Dec meetings). The formula was altered in January 2004 ("the Committee believes it can be patient") (January and March meetings) but interest rates were not in fact raised until the end of June 2004.

Even then the Committee continued to damp down expectations of a sharp rise, employing the formula "policy accommodation can be removed at a pace that is likely to be measured". The phrase was repeated throughout the remainder of 2004 (Jun, Aug, Sep, Nov and Dec meetings) and almost to the end of 2005 (Feb, Mar, May, Jun, Aug, Sep and Oct meetings) before the Fed switched to a full inflation alert at the end of the year (Dec 2005).

Federal Reserve Chairman Ben Bernanke was a member of the rate-setting Committee throughout almost all this period. He has passionately defended the Fed's conduct of monetary policy throughout this period, most recently at the American Economic Association (AEA) conference earlier this month, where he rejected criticism it left rates too low too long, and was then too slow to increase them.

LESSONS FROM 2003-2006

Given the Fed believes it did nothing wrong, its conduct of monetary policy in the wake of the 1990-1991 and 2000-2001 recessions is likely to be a template for the months ahead.

Past experience suggests the first increase is at least six months away, but could be much further. It took the Fed another six months to begin raising interest rates after dropping the "considerable period" commitment in 2004. With the Committee still maintaining its "extended period" equivalent, the first rise is unlikely until H2 2010, and perhaps not into 2011.

But this time around the debate is likely to be much more rancorous and the course of policy attended by much greater uncertainty:

(1) While Bernanke refuses to admit the Fed make mistakes in monetary policy (as opposed to banking supervision), he has not convinced many economists, politicians or investors to accept the narrative. The Fed's credibility has been badly dented. Moreover, confidence in its commitment to low inflation, and among foreign investors, has been weakened leaving the central bank less scope to chart a steady course and dismiss deviations in inflation as "temporary".

(2) Federal Reserve Bank of Kansas City President Thomas Hoenig, a respected veteran, has already cast the first, rare dissenting vote, urging the Committee to drop its extended period language because economic and financial conditions had changed sufficiently that it was no longer warranted.

Hoenig's dissent should be interpreted with care. It is unlikely he wants an imminent rate rise. Rather he probably wanted to give the Committee more flexibility and avoid becoming boxed in by a rhetorical promise to keep rates for much of the rest of the year. One criticism of the Fed's approach in 2003-2006 was that

it encouraged excessive risk-taking by inoculating investors against policy risks. Less certainty and predictability might have encouraged more caution.

POLICY BEHIND THE CURVE

The gradual pick up in manufacturing output and shipments around the globe is evident in a variety of real-world indicators. The number of containers handled at the West Coast ports of Los Angeles and Long Beach, as well as Asian trading hubs at Singapore and Hong Kong, has risen consistently in recent months from depressed levels in late 2008 and early 2009.

There has been a similar pick up in air freight, which is one proxy for higher-value added items.

Policymakers nonetheless remain cautious about whether the recovery has enough momentum to be self-sustaining. Much of the rebound has been driven by inventory-related changes along the supply chain. It could falter once production-consumption levels are rebalanced. The Fed will therefore remain inclined to keep rates low until the recovery has proven much more durable.

Past experience suggests monetary policy responds to the cycle with a much longer lag than most analysts assume. The attached chart shows changes in the Fed's policy rate since 1972 and its estimate for capacity utilization in the manufacturing sector.

Rates track capacity use but with a lag. After the last four recessions, capacity use began to rise in June 1975, Feb 1983, Apr 1991 and December 2001; but rates did not rise until Aug 1977, Jan 1987, Feb 1994 and Jul 2004, a lag of 27 months, 46 months, 34 months and 32 months respectively. A large overhang of excess capacity inherited from the previous downturn eased fears about inflation, allowing policymakers to focus on entrenching the recovery.

The average lag between growth resuming and the first rate increase has been 35 months. If the current recovery is dated back to July 2009, rates might not rise until end-2011.

A SUI GENERIS RECOVERY?

While there is a pronounced rhythm to the business cycle, every recovery is in some sense sui generis. There are reasons to think the present one and associated rate changes will differ even more than usual from the "norm":

(1) Policymakers have produced a huge distortion in financial markets, with the lowest rates since World War Two coupled with massive liquidity injections, and an ultra-loose fiscal policy. While the distortion may have been justified, it leaves officials with a lot of heavy lifting to do in order to "normalize" conditions by the time the expansion becomes mature.

The longer the adjustments are postponed, the more abrupt and disruptive they will become, and the greater the risk of inflating another even bigger asset bubble.

In the early stages, the Fed may reduce liquidity rather than raise rates; the Committee has already voted to allow some extraordinary programs to expire. But in the end the cost of borrowing must rise; whether the Committee focuses on reserve volumes, the discount rate or the fed funds target makes little practical difference.

Leaving rate rises until the end of 2011 would represent an enormous gamble. The Fed may start to guide rates to more normal levels before then. Early moves (starting in H2 2010) would enable it to maintain a relatively gentle trajectory.

(2) Epidemic default has only been averted by cutting borrowing costs sharply, enabling over-borrowed households and companies to cut their servicing costs and refinance, while allowing

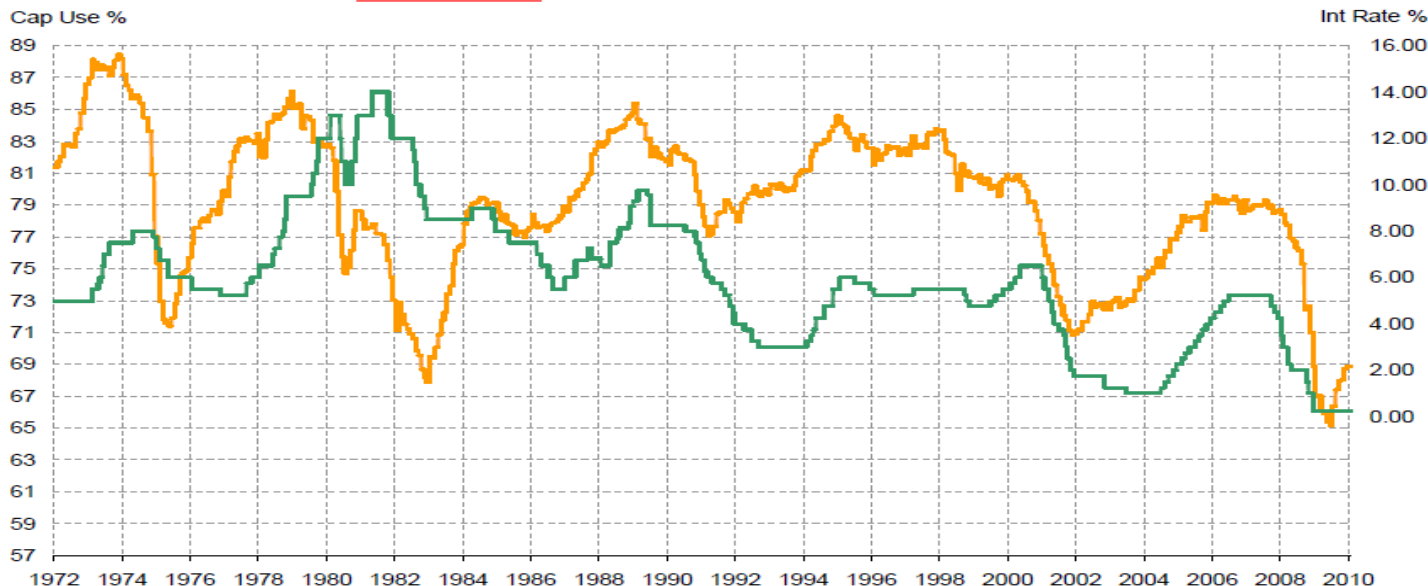
DEEP DIVE Commentary and Analysis

banks to fatten gross interest margins. Given the underlying fragility of the loan book and household finances, raising rates too early would carry a significant risk. With the degree of overleveraging preceding the crisis, it could take several years to repair balance sheets to the point where they could withstand a significant tightening of conditions. Even assuming the economy manages a sustained recovery in

2010, which seems likely, any changes this year are likely to be minor, and monetary conditions are unlikely to normalize significantly until well into 2011.

-- John Kemp is a Reuters columnist. The views expressed are his own --

UNITED STATES: CAPACITY UTILISATION AND INTEREST RATES



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