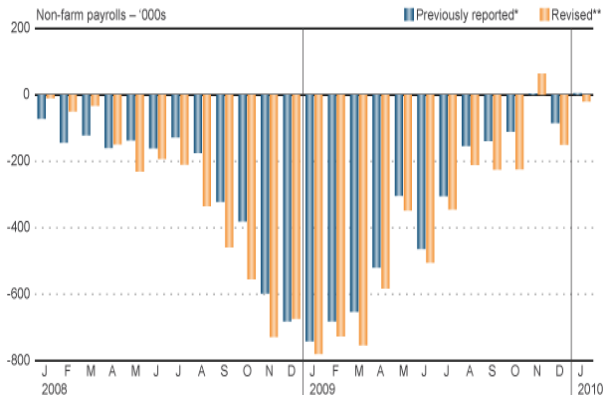


## CHART OF THE DAY

### U.S. non-farm payrolls



The labor department said the U.S. employers unexpectedly cut 20,000 jobs in January which was far smaller than the revised 150,000 drop for the previous month.

## TODAY'S TOP NEWS

- U.S. jobless rate hits 5-month low but payrolls fall
- Obama unveils plan to boost small business credit
- Policymakers try to calm markets after euro sell-off
- Fewer U.S. homeowners see home values falling-survey
- Air Products bids \$5.1 billion for rival Airgas
- OECD December indicators show improved outlook
- UK manufacturers' price pressures up strongly in Jan
- Euro Libor sets new low, euribor rallies
- German industry output slumps in fresh recovery blow

## ECON WATCH

FOR MONDAY FEBRUARY 8

ET	Indicators	Unit	Reuters	Prior
00:00	JP Economy watchers poll	ind	-	35.4
04:30	EZ Sentix Index	ind	-3.2	-3.7
08:15	CA House starts, annualized	k	-	174.5
10:00	US Employment Index	ind	-	91.8

## MARKETS TODAY

**TODAY'S TOP STORY:** The U.S. unemployment rate surprisingly fell to a five-month low in January and factory payrolls grew for the first time since 2007, hinting at a labor market recovery even though the economy lost 20,000 jobs. **For more please click here**

**TREASURIES:** U.S. Treasuries rose with the 30-year bond gaining more than a point, as stocks fell and a weaker-than-expected payrolls report kept inflation concerns at bay.

- 30-yr bond prices rose 16/32 to yield 4.51 pct
- 10-yr Treasury prices rose 12/32 yielding 3.57 pct down from 3.61 pct.
- 2-yr Treasury prices were up 2/32 to yield 0.77 pct.
- The spread between 10-yr Treasury yields and 10-yr TIPS yields narrowed by 7 bps to 225 bps.

**FOREX:** The U.S. dollar and yen gained as persistent worries about the euro zone's fiscal stability pushed investors further away from risky assets and into traditional safe-havens.

- The dollar index was up 0.5 pct at 80.315. Earlier, it rose to 80.683, its strongest since July 2009.
- Euro fell 0.45 pct at \$1.3664, after falling as low as \$1.3586, the lowest since May 2009.
- Dollar was up 0.43 pct at 89.38 yen.
- The euro fell 0.02 pct to 122.14 yen, after falling to 120.72 yen, the lowest since Feb. 24, 2009.
- Sterling shed 0.75 pct to \$1.5635.

**CORPORATES:** U.S. corporate bond spreads were little changed after U.S. jobs data pointed to a slow recovery and investors worried about the health of the euro zone's weakest economies.

- The CDX.IG-13 index widened by 3 bps to 102 bps.
  - Moody's Liquidity-Stress Index fell to 7.7 percent from 8.6 percent in December and is now well below its peak of 20.9 percent reached in March 2009.
- STOCKS:** U.S. stocks erased a midday drop to end flat on Friday, closing out a volatile week punctuated by mixed signals from the labor market and growing anxiety over fiscal problems in Europe.
- Dow rose 0.1 pct to 10,012.23, S&P was up 0.29 pct to 1066.19 and Nasdaq gained 0.74 pct to 2141.12.
  - S&P technology index rose 1.1 pct, S&P financial index rose 1.21 pct and S&P energy index fell 0.11 pct.
  - KBW banks index rose 1.33 pct.
  - Tyson Foods' share rose 4.72 pct to \$14.65.

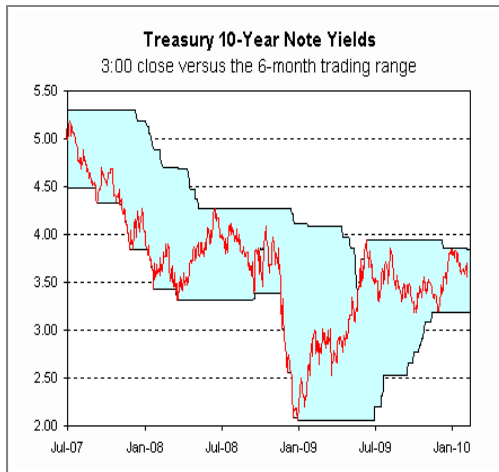
**C & E:** Oil slid as a stronger dollar and data showing additional U.S. job cuts as investors fled from risky assets like commodities.

- It was the second straight session of steep declines, as oil prices on Thursday posted their biggest one-day fall since July.
- U.S. crude prices fell 1.82 pct to \$71.81 per barrel.
- Gold was up 0.35 pct to \$1,066.35 an ounce.
- Reuters-Jefferies index shed 1.94 pct to 258.55.

- 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	0.040	0.005	0.041	-0.004
3-Mo Bill	0.095	0.085	0.096	0.004
6-Mo Bill	0.155	0.145	0.157	-0.004
1-Year	0.275	0.270	0.279	-0.004
2-Year	100.227	100.258	0.760	0.094
3-Year	100.367	100.398	1.248	0.188
5-Year	100.117	100.164	2.225	0.352
7-Year	100.844	100.891	2.990	0.461
10-Year	98.531	98.594	3.554	0.422
30-Year	97.922	97.984	4.502	0.688

EQUITIES

	INDEX	CHANGE
DJIA	9894.87	-107.31
NASDAQ	2114.13	-11.30
S&P 500	1051.86	-11.25

OIL

	PRICE	CHANGE
NYMEX	71.5	-1.7
BRENT	69.8	-2.3

EURODOLLAR FUTURES

	CLOSE	CHANGE
Feb-10	99.738	-0.005
Mar-10	99.700	-0.010
Jun-10	99.595	-0.005
Sep-10	99.395	0.030

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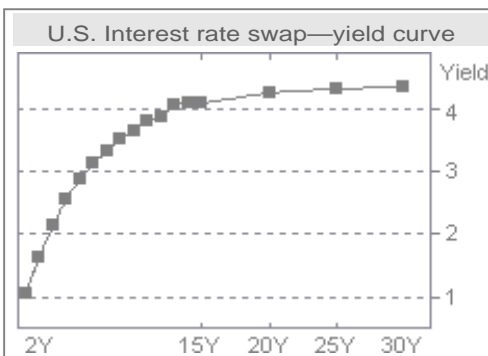
	SPREAD		RATE	
2-Year	28.50	32.50	1.04	1.06
3-Year	38.00	42.00	1.62	1.64
5-Year	32.25	36.25	2.54	2.55
7-Year	13.75	17.75	3.12	3.12
10-Year	7.75	11.75	3.62	3.61
30-Year	-16.50	-12.50	4.34	4.31

FUTURES

	PRICE	CHANGE
CBOT 5 yr	117.07	0.41
CBOT 10 yr	118.84	0.59
CBOT 30 yr	117.22	-0.16

REPURCHASE AGREEMENTS

G/C		MORTGAGE REPOS	
O/N	0.170	O/N	0.170
2-Week	0.200	2-Week	0.210
1-Month	0.200	1-Month	0.220
3-Month	0.240	3-Month	0.250
AGENCY REPOS		i-REPO <sup>SM</sup> INDEX	
O/N	0.160	10:00 AM	0.110
2-Week	0.200	3:00 PM	0.110
1-Month	0.210		
3-Month	0.240		



CURRENCIES

	BID	ASK
Euro	1.3627	1.3630
Sterling	1.5597	1.5602
JP Yen	89.24	89.26
Swiss Franc	1.0752	1.0754
Can Dollar	1.0723	1.0728
Mexico	13.1860	13.1916

EURODOLLAR DEPOSITS & OIS STRIPS (ASKED)

	BID	ASK	BID	ASK
O/N	0.140	0.160	-	-
1-Month	0.180	0.280	0.127	0.137
3-Month	0.240	0.400	0.141	0.151
6-Month	0.250	0.450	0.163	0.173
12-Month	0.650	1.000	0.293	0.303

FED FUNDS

	NYFR <sup>SM</sup> - 10AM
Open	0.1500 1m 0.2133
High	0.1500 3m 0.2461
Low	0.1200

ACTIVE FANNIE MAE AGENCIES

TERM	COUPN	MATURITY	YIELD-SPREAD	YIELD
2-Year	0.875	12/01/2012	17 14	0.97
3-Year	1.375	09/01/2013	25 22	1.56
5-Year	2.875	09/02/2015	36.5 35	2.59
7-Year	5.125	18/10/2016	28 0	3.27
10-Year	-	-	- -	-
30-Year	6.625	15/11/2030	40 39.25	4.9

ACTIVE FREDDIE MAC AGENCIES

TERM	COUPN	MATURITY	YIELD-SPREAD	YIELD
2-Year	1.125	15/12/2011	11.5 10	0.87
3-Year	1.75	22/02/2013	29.5 28.5	1.54
5-Year	2.625	20/11/2014	23.5 22.5	2.45
7-Year	5.25	15/09/2016	23.75 23	3.23
10-Year	3.75	27/03/2019	28 27	3.83
30-Year	6.25	15/07/2032	49 0	5.04

Active MBS 15YR

	CPN	BID	ASK	YIELD
FNMA	5.0	105.2860	105.3060	2.432
FHLMC	5.0	105.2960	105.3160	2.420

Active MBS 30YR

	CPN	BID	ASK	YIELD
FNMA	5.5	106.0970	106.1170	2.650
FHLMC	5.5	106.1070	106.1270	2.575
GNMA	5.5	106.0550	106.0750	3.405

Wrightson ICAP<sup>SM</sup> Chart of the Day



## TODAY'S TOP NEWS

**U.S. jobless rate hits 5-month low but payrolls fall**

The U.S. unemployment rate surprisingly fell to a five-month low in January and factory payrolls grew for the first time since 2007, hinting at a labor market recovery even though the economy lost 20,000 jobs.

The decline in payrolls reported by the Labor Department was far smaller than the 150,000 drop posted in December. November's data from the survey of employers was revised sharply higher to a gain of 64,000, up from 4,000.

The jobless rate fell to 9.7 percent from 10 percent in December. Analysts had expected payrolls to rise by 5,000 and the unemployment rate to edge up to 10.1 percent.

In another sign of labor market improvement, the average work-week unexpectedly edged up to 33.3 hours, the highest in a year, from 33.2 in December, while manufacturing overtime rose to 3.5 hours, the highest since September 2008.

In a separate report, ECRI said its Weekly index fell slightly to 130.9 for the week ended Jan. 29 from 131.4 the prior week. The index's annualized growth rate declined for the eighth straight week to 21.5 percent, from 22.7 percent the previous week.

Separately, U.S. President Barack Obama said new jobs figures showed the United States was climbing out of the "huge hole" created by the recession but cautioned that they were not cause for celebration.

**Policymakers try to calm markets after euro sell-off**

European policymakers scrambled to reassure markets about the stability of the 16-nation currency bloc as investors shed euro assets for a second day and Portugal backed a law that may push its swollen deficit higher.

European Central Bank Governing Council member Ewald Nowotny called talk of a euro zone breakup "absurd" and tried to play down the sharp fall in the euro, which hit its lowest level against the dollar since May 2009.

Greek Prime Minister George Papandreou, on a visit to India, promised to "credibly apply" an austerity program designed to bring his country's yawning debt and deficit under control.

But worries about Portugal mounted after its opposition-led parliament defied the Socialist government and approved a bill on regional finances that could complicate the country's budget consolidation drive.

Greece, Portugal and other bloc members with swollen deficits like Spain face intense pressure to get their public finances in order and calm markets worried about the risks of a sovereign default.

**Air Products bids \$5.1 billion for rival Airgas**

Air Products and Chemicals Inc launched an unsolicited \$60-a-share cash bid for rival Airgas Inc, whose shares rose above that mark, indicating that investors expect a higher bid.

The \$5.1-billion bid represents a 38-percent premium over Airgas's Thursday closing price.

The jump of Airgas shares above the \$60 mark indicated Airgas shareholders view the current offer as too low, and may prompt a higher proposal -- which Air Products said it was willing to consider if Airgas shows "additional value" -- or a bid from a rival. Airgas said its board would review the proposal and advised its shareholders to take no action. A representative was not immediately available for comment.

Air Products said the deal would be financed through a one-year bridge loan from JPMorgan Chase & Co and that it is willing to sell assets to assuage regulatory concerns.

**Obama unveils plan to boost small business credit**

President Barack Obama, looking for ways to drive down high U.S. unemployment in an election year, proposed to expand credit for small businesses and urged Congress pass laws to boost jobs.

Obama proposed Congress temporarily expand credit through two Small Business Administration programs, the latest in a series of White House efforts to improve the flow of credit to small businesses, which are a core source of new U.S. jobs.

Separately, Obama will issue an executive order next week creating a panel to tackle the record U.S. deficit and mounting debt in a step designed to toughen fiscal discipline.

White House spokesman Robert Gibbs also told reporters that Obama would sign a bill on either Tuesday or Wednesday raising the government's borrowing authority to \$14.3 trillion, and reinstalling pay-as-you-go rules to curb spending.

The White House forecasts a record \$1.56 trillion deficit in the fiscal year to Sept. 30, 2010, but then projects this funding gap to more than halve as a share of the economy by the end of Obama's term in January 2013.

**Fewer U.S. homeowners see home values falling-survey**

Fewer U.S. homeowners expect the value of their homes to decline in the year ahead, but they also believe gains are unlikely, according to a Thomson Reuters/University of Michigan survey published.

The proportion of homeowners that expected declines in the value of their homes in the year ahead fell to 15 percent in January, the lowest level since early 2007.

That is down from 16 percent in the fourth quarter, and sentiment has improved over the past year.

The mean anticipated annual gain over the next five years held steady at 2.7 percent in January. Given consumers' long-term inflation expectations, a zero, inflation-adjusted gain was expected.

In the January 2010 survey, three-in-four homeowners viewed current home buying conditions favorably because of very attractive prices and low mortgage rates.

But, when asked about home selling conditions, nine of ten homeowners viewed current market conditions for the sale of their home unfavorably, largely over price declines.

**OECD December indicators show improved outlook**

The outlook for recovery in most of the world's major economies improved in December but the indicator for China dipped slightly, according to an OECD survey released.

The OECD's Composite Leading Indicator for 29 developed countries rose to 103.1 in December from 102.2 the previous month and 10.1 points higher than a year ago.

The CLI for the Group of Seven -- Japan, the United States, Canada, Italy, France, Germany and Britain -- rose to 103.1 from 102.1 in November. That was 10.4 points higher than a year earlier.

The improvement was slightly less marked in four large emerging market countries. They are not members of the OECD and are not covered by the overall OECD indicator.

The CLI for Russia rose to 101.0 from 100.8 in November, for Brazil it rose to 99.1 from 99.0 while the outlook for China eased to 103.1 in December from 103.2.



## TODAY'S TOP NEWS

**UK manufacturers' price pressures up strongly in Jan**

A strong rise in oil prices pushed British manufacturers' raw material costs up more than expected last month and at their sharpest annual rate since October 2008, official data showed. The Office for National Statistics said producer input prices jumped 2.0 percent in January to stand 8.4 percent higher than a year ago, well above expectations for a 6.3 percent annual rise.

Factory gate inflation also rose more than expected. Output prices rose 0.4 percent on the month and 3.8 percent on the year, the highest annual rate since December 2008.

Many economists reckon the central bank may be forced to nudge up its inflation forecasts when it publishes updated quarterly forecasts next week.

Separately, Alistair Darling, Britain's finance minister, voiced concern that the push for financial reform was losing momentum, but he said he saw general agreement on issues like capital requirements.

**Euro Libor sets new low, euribor rallies**

Interest rate-sensitive euribor futures rallied across the 2011 strip, driving their implied rates sharply lower while the benchmark interbank lending rate for euros was set at a record low.

Mounting worries about the fiscal health of heavily indebted euro zone fringe economies have hit risk appetite and prompted market players to push out expectations for the European Central Bank to tighten its ultra-loose monetary policy.

The three-month euro Libor was set at an all-time low of 0.60125 percent and the equivalent rate for dollars was set slightly higher at 0.24969 percent, having retested the record low of 0.24875 percent at Thursday's fixing.

Three-month sterling Libor was a touch higher at 0.61969 percent.

Highlighting that liquidity, latest data showed banks parked 217.7 billion euros at the ECB's overnight vault, up from 210.2 billion euros.

ECB Governing Council member Erkki Liikanen said the central bank will pull back more of its extraordinary liquidity measures at next month's meeting.

**German industry output slumps in fresh recovery blow**

German industrial output fell sharply in December, putting the manufacturing core of Europe's largest economy on a weakened footing going further into 2010 and dealing a fresh setback to recovery hopes.

The Economy Ministry said industrial output fell 2.6 percent on the month in seasonally adjusted terms, below the consensus forecast in a Reuters poll of economists for a rise of 0.5 percent and weaker than even the lowest projection.

Economy Minister Rainer Bruederle has said growth in the first quarter of 2010 could be near zero.

The government expects the economy to grow by 1.4 percent this year, driven by a projected 5.1-percent rise in exports. However, Bruederle said earlier on Friday Germany's economic recovery is not yet self-sustaining.

German business sentiment rose more than expected in January to its highest level in 1-1/2 years, suggesting recovery will gather pace once the economy emerges from a harsh winter.

**Canada's jobless rate unexpectedly drops in January**

Canada's unemployment rate unexpectedly fell in January to its lowest rate since September and the economy added more jobs than expected, suggesting the economy's recovery was gaining momentum.

The unemployment rate dipped to 8.3 percent in January from 8.4 percent in December, and 43,000 jobs were added, Statistics Canada said.

Economists surveyed by Reuters had predicted an unemployment rate of 8.5 percent and a gain of 15,000 jobs.

Almost all of the new jobs were part-time, to some extent reflecting the first notable increase in youth employment since the fall of 2008. The youth jobless rate fell to 15.1 percent from 16.0 percent.

The decline in the unemployment rate from its peak, if it stays on pace, could point to transition from emergency level interest rates, economists said.

## NEXT UP

**POLL-Most primary dealers see Fed rate hike this year**

The U.S. Federal Reserve will start raising interest rates in the fourth quarter of this year as the jobs picture improves gradually, according to the median forecast of big banks that do business directly with the U.S. central bank.

The poll of primary dealers was conducted after government data showed the U.S. economy unexpectedly lost jobs in January even as the unemployment rate dropped to 9.7 percent -- a five-month low.

Six dealers changed their forecasts for the level at which the U.S. jobless rate would peak, compared to a Jan 27 poll.

The poll showed dealers expect the jobless rate to have already peaked at 10.1 percent.

Seventeen of the 18 primary dealers in the Fed's network responded to the Reuters poll.

Nine out of 17 dealers expect the Federal Reserve to start raising rates this year. The Federal Reserve cut its benchmark interest rate to near zero in December 2008 and has pledged to keep rates extraordinarily low for "an extended period."

Dealers expect the Fed to change this pledge one or two quarters before it begins to raise rates.

**PREVIEW-BoE to cut 2010 growth, raise inflation forecasts**

The Bank of England will almost certainly revise down its growth forecasts for this year while ramping up its inflation profile when it unveils its quarterly Inflation Report on Wednesday, a Reuters poll showed.

Fourteen of 19 economists in the poll, taken this week, said the central bank would revise down its growth forecasts from the surprisingly upbeat numbers announced in November, with four saying it would be unchanged and one revised down.

Economists were similarly convinced about inflation, with 18 saying the profile for 2010 would be revised up from November, one saying it would be left unchanged and one that it would be revised down.

Seven of 15 said growth forecasts would be revised down, seven said they would be left alone while one said they would be revised up. For inflation, five said projections would be revised up, seven went for unchanged and four said revised down. The bank said in November that inflation would be below its 2 percent target at around 1.6 percent in two years time but was likely to rise sharply above target in the near term, with risks broadly balanced for the end of 2011.



## DEEP DIVE Commentary and Analysis

**ANALYSIS-European junk bond revival steams into 2010**

By Simon Jessop

European corporates tapped the high-yield bond market in record numbers in January -- a funding play that heralds the revival of regional "junk" bond issuance, even if some remain wary of its sustainability.

Unlike the U.S., the European market is traditionally smaller and shallower, with firms mostly relying on bank loans and only going to the bond market on an opportunistic basis.

While issuance after the telecom junk bond boom of 1999-2000 and in the pre-credit crunch leveraged buyout binge flourished, record January deals of over \$7 billion and 2010 forecasts of \$50 billion-plus, imply a lasting structural shift is afoot.

"What we are seeing now is Version 3.0, with a lot more corporate issuance, much more akin to the way the U.S. market is," said Henrik Johnsson, head of European high-yield capital markets at Deutsche Bank.

In 2009, high-yield issuers accounted for nearly one quarter of the wider non-financial U.S. corporate bond market and just 6.5 percent in Europe, Thomson Reuters data shows.

So far this year, European supply is 28 percent, a faster growth rate than in the United States, the data shows.

Reduced bank lending to leveraged firms has coincided with the exit of institutional investment vehicles such as collateralized loan obligations (CLOs), which accounted for more than half of pre-crisis leveraged loan buying, bankers said.

"It is unlikely that CLOs will come back in any material form, so the issuance that was taken away from the market by the leveraged loan market should now come as high yield bonds," said Martin Reeves, director of global credit research at Alliance Bernstein.

Yield-hungry investors in a low interest rate environment have partially driven the shift, through increased demand, but more cautious investors may take longer to be won over.

"Some hedge fund clients we have spoken to have said they are not convinced about the sustainability of the high-yield market, despite the widespread view that the bank market is not as dependable as it once was," said Larry Wieseneck, head of global finance and risk solution at Barclays Capital.

**NEED INPUT**

For banks and investors to build up their high-yield presence they need deals, which means issuers.

If forthcoming, investors would see "it makes sense to have a high-yield capability", said Wieseneck, adding the market had to consist of "more than just telecom and cable companies".

There is now growing evidence that a broader range of issuers are using the market than before, bankers said.

Johnsson said there are "more diverse types of issuers and investors coming into the market. For the first time we're seeing food processing companies like (Spanish cured meats supplier) Campofrio doing deals in Europe."

Other non-traditional high-yield names include data company Interxion, which is roadshowing a 200 million euros (\$274.3 million) deal, and French pharma Novasep, which secured 270 million euros in December.

"Smaller companies have come to market, many of which haven't (previously) been on the radar screen of investors," said Peter Charles, European head of debt syndicate at Citi.

With deals to be made, banks and others are hiring. Nomura has hired two new high-yield analysts, and plans to "continue growing its high yield platform".

Of the investors, Scottish Widows Investment Partnership (SWIP), whose high-yield bond team manages more than 1.5 billion pounds (\$2.38 billion), has hired more specialist staff.

Steven Logan, SWIP's head of high-yield bonds, said he expected the sector to continue showing "incremental growth", this feeding into profitability and "enabling asset managers to invest in additional resources".

Thomson Reuters data shows that in the next five years more than \$1 trillion of leveraged loans are due to mature in Europe, as well as more than \$125 billion of high-yield corporate bonds.

"The sheer volume of debt maturing, combined with banks' constrained lending capacity, which is unlikely to abate any time soon... tells me this (strength in Europe's high-yield bond market) is set to continue," said Gilbey Strub, executive director at the European High Yield Association.

**ANALYSIS-Disunity, economic woes dog EU image drive**

By Timothy Heritage

The European Union's efforts to improve its global image are looking increasingly unconvincing as it struggles to contain a debt crisis in Greece and put down talk that its 16-nation euro currency bloc could break up.

When the last of the EU's 27 member states finally accepted the Lisbon reform treaty last year after nearly a decade of disputes and hesitation, EU leaders hailed the start of a bright new era for the world's biggest trading bloc.

But two months after the treaty came into force, the EU is dogged by rivalry among member states, differences over economic policy, confusion over who does what and criticism that it has left economic problems to fester for too long.

Policymakers in the 16 countries that use the euro are struggling to convince markets about the stability of their euro zone because of fears that other debt-ridden countries such as Spain and Portugal could follow Greece into severe trouble.

"There has been a lot of rhetoric about the 'European project' (to strengthen the EU) but to a large extent governments have had their heads in the sand and not addressed the tough underlying problems," Simon Tilford, chief economist at the Centre for European Reform think tank in London, said.

"There is an insularity and provincialism which is very worrying." The Lisbon treaty creates a full-time president, enhances the role of EU foreign policy chief and hands the European Parliament more power. It is also meant to ease decision-making and strengthen the bloc's global role.

But battles for influence continue and Spain has upset some states by seeking the lead as holder of the separate, rotating EU presidency, an organizational role that is held for six months by each country but has less visibility under the treaty.

**FEARS OVER EURO AREA**

A perceived lack of unity over how to solve Greece's debt problems and prevent them spreading to other countries in the euro area has contributed to the concerns of investors worried about a sovereign default. The euro has hit its lowest level against the dollar since May 2009.

"Now we are in a (difficult) situation and it is quite clear they don't have a plan for dealing with it," said Juergen Michels, an economist at Citigroup in London.

Analysts no longer discount the possibility that a smaller member of the currency bloc such as Greece could be pushed out, though most believe monetary union will survive.

Such fears prompted Ewald Nowotny, a member of the European Central Bank's Governing Council, on Friday to dismiss suggestions that the euro zone might break up as "absurd".

The stakes are high, not only because the fiscal problems could spread, but because the credibility of European economic policymakers is at stake.

"This is much more than an issue about problems in the periph-



## DEEP DIVE Commentary and Analysis

ery. It is a test case of the ability of the (European) Commission and Eurogroup (of finance ministers) to impose the essential fiscal discipline needed to underpin EMU (European monetary union)," BNP Paribas said in a research note on Friday.

## OBAMA BLOW

The EU's credibility problems stretch far beyond its difficulties convincing markets it can solve its economic woes.

It suffered a deep blow to its prestige this week when Washington announced that President Barack Obama would not attend an EU-U.S. summit in Madrid in May, and indicated that confusion over who represents the EU at meetings under the Lisbon treaty had been a factor in the decision.

This was a bitter disappointment for Spain and the bloc, which represents more than 500 million people, particularly so soon after the EU's pride was hurt at international climate change talks in Copenhagen in December.

Although the final deal in Copenhagen was largely based on ideas promoted by the EU, Washington did not invite it to last-minute talks with other powers that sealed the deal and it was aggrieved that its more radical proposals were ignored.

## LIGHT AT THE END OF THE TUNNEL?

Supporters of the Lisbon treaty say it is just a matter of time before its positive effects are felt.

"If we want to see movement that brings new gravity to EU institutions, it'll be in one, two or three years," said Ulrike Guerot of the European Council on Foreign Relations think tank.

There may be light at the end of the tunnel because the European Parliament is expected next week to approve the new European Commission, the EU executive body that has legislative, regulatory and policy-making powers.

The Commission's ability to launch major initiatives has been frozen since November because of delays in confirming it in office, caused largely by obstacles to securing Czech approval for the Lisbon treaty and a long wait for Ireland to back it.

But new problems are also emerging. The European Parliament has shown it is ready to flex its muscles under the new treaty, which increases its responsibility for shaping legislation, and this could hold up or water down Commission initiatives.

A battle is already looming over plans to create banking watchdogs because some parliamentarians are challenging a deal between Britain and other finance ministers.

Tightening financial regulation after the global economic crisis is an EU priority and any delay or failure to do so would deeply undermine the EU's reputation.

INSIDE DEBT is produced by Reuters in partnership with ICAP.

(Compiled by Anil Kumar and Rahul Karunakar in Bangalore)

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