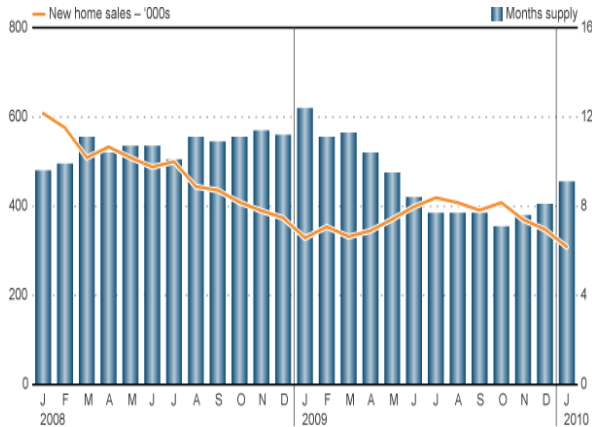


## CHART OF THE DAY

### U.S. new home sales



New home sales fall to a record low in January, with supply edging over nine months.

## TODAY'S TOP NEWS

- Bernanke eases worries about U.S. monetary tightening
- U.S. new home sales hit record low, prices tumble
- Senate passes jobs package, eyes next round
- No change to U.S. housing finance system this year
- Soft demand greets \$42 bln in 5-yr U.S. Treasuries
- U.S. SEC reins in short sellers with new restrictions
- S&P says Greek rating cut possible "within a month"
- ECB to extend unlimited cash steps into Q3-sources

## ECON WATCH

FOR THURSDAY FEBRUARY 25

ET	Indicators	Unit	Reuters	Prior
04:00	DE Unemployment chng	k	19	6.0
04:00	DE Unemployment total	mln	3.70	3.617
04:00	DE Unemployment rate sa	%	8.2	8.2
05:00	EZ Business climate	ind	-1.05	-1.12
05:00	EZ Economic sentiment	ind	96.2	95.7
05:00	EZ Industrial sentiment	ind	-13	-14
05:00	EZ Services sentiment	ind	-1	-1
05:00	EZ Consumer sentiment	ind	-17	-16
08:30	US Durable goods	%	1.5	1.0
08:30	US Ex-transportation	%	1.0	1.4
08:30	US Ex-Defence	%	1.0	0.8
08:30	US Nondefense ex-air	%	0.8	2.2
08:30	US Initial Claims	k	455	473
08:30	US Continuing claims	mln	4.56	4.563
10:00	US FHFA Home price mm	%	-	0.7
18:30	JP CPI, core nationwide	%	-1.4	-1.3
-	US Build permits R numbr	mln	-	0.621

## MARKETS TODAY

**TODAY'S TOP STORY:** U.S. Federal Reserve Chairman Ben Bernanke told Congress a weak job market and tame inflation warrant low interest rates for "an extended period," dampening speculation a policy tightening might be nearing. **For more please click here**

**TREASURIES:** U.S. Treasuries prices traded little changed after some disappointment in the results of a five-year note auction offset bond-positive comments from Federal Reserve Chairman Ben Bernanke.

- 5-yr Treasury prices brought a higher yield than expected, indicating investors were aggressive in trying to push down the price of the notes. The notes yielded 2.395 pct.
- 30-yr bonds were up 8/32 to yield 4.62 pct.
- 10-yr Treasury prices were down 1/32 to yield 3.69 pct.
- 2-yr notes yielded 0.86 pct from a high yield of 0.9 pct in an auction of \$44 billion of the notes on Tuesday.
- 2-10's part of the yield curve flattened by about 3 bps to 282 bps.

**FOREX:** The U.S. dollar fell versus the euro and yen after comments by U.S. Federal Reserve Chairman Ben Bernanke.

- Euro rose 0.18 pct to \$1.3533, earlier rising as high as \$1.3626.
- The dollar fell 0.02 pct to 90.19 yen. Earlier it fell as low as 89.78 yen.
- Euro was up 0.15 pct at 122.04 yen.

**CORPORATES:** U.S. corporate bonds spreads tightened, taking their cue from rising stocks after the Fed's Bernanke reassured investors of his commitment to support the fragile economic recovery.

- The CDX.IG-13 index remained unchanged at 94 bps.
- KFW launched \$3.0 bln of five-year global notes.
- Comcast Corp launched a \$2.4 bln two-part debt sale.
- CDS insuring the debt of BofA have risen to 140 bps from 100 bps in early January, while Citigroup's CDS costs have jumped to 203 bps from 150 bps.

**STOCKS:** U.S. stocks rose after Fed's Bernanke reaffirmed his commitment to keep interest rates low for an extended period to sustain the still-fragile recovery.

- Dow gained 0.89 pct to 10,373.86, S&P rose 0.97 pct to 1,105.2 and Nasdaq was up 1.01 pct to 2,235.90.
- D.R. Horton Inc fell 1.83 pct to \$12.34, pushing down the Dow Jones Home construction index by 0.73 pct.
- IBM gained nearly 0.89 pct to \$127.59.
- Shares of Autodesk Inc jumped 8.69 pct to \$27.89.
- S&P financial index rose 1.73 pct, S&P technology gained 1.05 pct.
- KBW bank index jumped 2.26 pct.

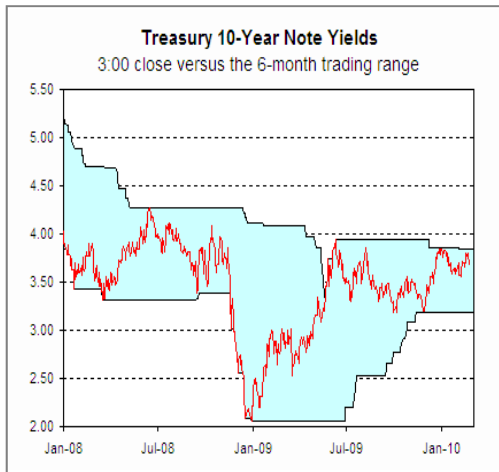
**C & E:** Oil rose despite a big rise in U.S. crude inventories, as Bernanke reaffirmed his commitment to keeping interest rates low.

- U.S. crude prices were up 1.55 pct to \$80.08 per barrel. Earlier, it rose as high as \$80.13.
- Gold fell 0.67 pct to \$1,095.6 an ounce.
- Reuters-Jefferies index gained 0.86 pct at 274.74.

- 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	0.090	0.055	0.091	-0.006
3-Mo Bill	0.115	0.105	0.117	-0.002
6-Mo Bill	0.185	0.180	0.188	-0.004
1-Year	0.310	0.305	0.315	-0.014
2-Year	99.992	100.023	0.880	0.008
3-Year	99.867	99.898	1.421	-0.012
5-Year	99.469	99.516	2.365	-0.063
7-Year	99.984	100.031	3.127	-0.039
10-Year	99.406	99.453	3.697	-0.055
30-Year	99.828	99.891	4.636	-0.031

EQUITIES

	INDEX	CHANGE
DJIA	10344.76	62.35
NASDAQ	2228.37	14.93
S&P 500	1101.37	7.90

OIL

	PRICE	CHANGE
NYMEX	79.8	0.4
BRENT	77.5	0.2

EURODOLLAR FUTURES

	CLOSE	CHANGE
Mar-10	99.733	0.010
Jun-10	99.640	0.025
Sep-10	99.460	0.040
Dec-10	99.150	0.040

REPURCHASE AGREEMENTS

G/C		MORTGAGE REPOS	
O/N	0.150	O/N	0.150
2-Week	0.190	2-Week	0.210
1-Month	0.190	1-Month	0.210
3-Month	0.230	3-Month	0.240
AGENCY REPOS		i-REPO <sup>SM</sup> INDEX	
O/N	0.150	10:00 AM	0.070
2-Week	0.190	3:00 PM	0.065
1-Month	0.200		
3-Month	0.220		

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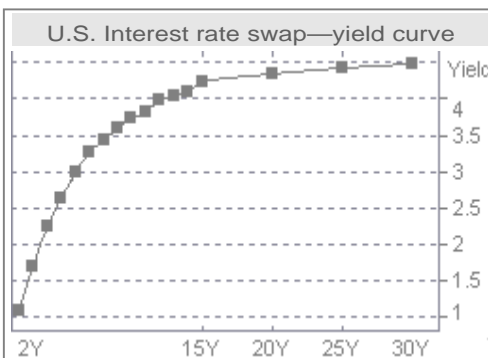
	SPREAD		RATE	
2-Year	21.00	25.00	1.08	1.11
3-Year	29.00	33.00	1.71	1.72
5-Year	30.00	34.00	2.66	2.66
7-Year	13.25	17.25	3.26	3.25
10-Year	6.75	10.75	3.76	3.75
30-Year	-16.00	-12.00	4.47	4.45

FUTURES

	PRICE	CHANGE
CBOT 5 yr	116.48	-0.03
CBOT 10 yr	118.02	-0.03
CBOT 30 yr	117.78	-0.09

EURODOLLAR DEPOSITS & OIS STRIPS (ASKED)

	BID	ASK	BID	ASK
O/N	0.120	0.140	-	-
1-Month	0.200	0.280	0.130	0.140
3-Month	0.220	0.400	0.153	0.163
6-Month	0.250	0.450	0.184	0.194
12-Month	0.600	1.000	0.316	0.326



CURRENCIES

	BID	ASK
Euro	1.3525	1.3528
Sterling	1.5397	1.5402
JP Yen	90.16	90.18
Swiss Franc	1.0817	1.0820
Can Dollar	1.0541	1.0546
Mexico	12.8374	12.8430

FED FUNDS NYFR<sup>SM</sup> - 10AM

Open	0.1300	1m	0.2156
High	0.1400	3m	0.2512
Low	0.0800		

ACTIVE FANNIE MAE AGENCIES

TERM	COUPN	MATURITY	YIELD-SPREAD		YIELD
2-Year	0.875	12/01/2012	1.5	0.5	0.89
3-Year	1.375	09/01/2013	12.5	0	1.53
5-Year	2.875	09/02/2015	29	28	2.63
7-Year	5.125	18/10/2016	19.5	19	3.32
10-Year	-	-	-	-	-
30-Year	6.625	15/11/2030	34.75	34.25	4.98

ACTIVE FREDDIE MAC AGENCIES

TERM	COUPN	MATURITY	YIELD-SPREAD		YIELD
2-Year	1.125	15/12/2011	-2	0	0.87
3-Year	1.75	22/02/2013	19.5	18.5	1.6
5-Year	2.625	20/11/2014	16	15.5	2.52
7-Year	5.25	15/09/2016	16.5	16	3.29
10-Year	3.75	27/03/2019	17.5	16.5	3.85
30-Year	6.25	15/07/2032	35	30.5	4.98

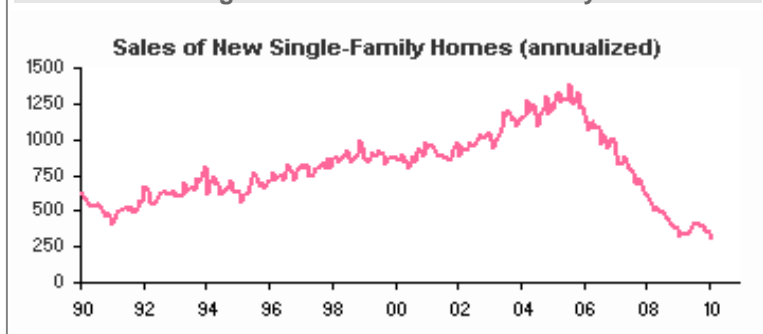
Active MBS 15YR

	CPN	BID	ASK	YIELD
FNMA	5.0	105.0310	105.0510	2.740
FHLMC	5.0	105.0310	105.0510	2.740

Active MBS 30YR

	CPN	BID	ASK	YIELD
FNMA	5.5	105.0510	105.0710	3.101
FHLMC	5.5	105.1510	105.1710	2.923
GNMA	5.5	105.1920	105.2120	3.561

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



## TODAY'S TOP NEWS

**Bernanke eases worries about U.S. monetary tightening**

U.S. Federal Reserve Chairman Ben Bernanke told Congress a weak job market and tame inflation warrant low interest rates for "an extended period," dampening speculation a policy tightening might be nearing.

Bernanke said the U.S. central bank's policy-setting FOMC was prepared to support the economy with extraordinary stimulus for some time.

Fed officials have held the benchmark overnight interbank rate in a zero to 0.25 percent range since December 2008 and have suggested they would likely wait several months after removing the "extended period" phrase from their policy statement before proceeding to raise it.

Republicans wanted Bernanke's view on the long-term implications of the government's funding gap, which he said was not on a sustainable path.

While he said he did not believe the U.S. credit rating would be downgraded, he warned that bond market worries on growing U.S. debt could send interest rates higher and added there was a also some chance, if small, of a sharp dollar drop.

Bernanke said, however, that the time would come for tighter policy and argued the Fed possesses a broad array of tools to remove such accommodation when the time is right.

**Senate passes jobs package, eyes next round**

The Senate passed a modest jobs-creation bill and laid the groundwork for a larger package that would advance Democrats' goal of bringing down the stubbornly high U.S. unemployment rate.

By a 70-28 vote, the Senate approved a \$15 billion package of tax breaks and highway spending and sent it on to the House of Representatives, which could approve the measure quickly for President Barack Obama to sign into law.

Immediately after the vote, Senate Majority Leader Harry Reid said he was readying a package of jobless benefits, state aid and tax breaks that the Senate could take up next week.

Reid plans to pass a series of smaller jobs bills that would avoid the sticker shock of the larger House bill and keep their job-creating efforts in the news.

The bill passed by the Senate includes a \$13 billion payroll tax break for businesses that hire unemployed workers, along with subsidies for state and local construction bonds.

Separately, President Barack Obama launched a vigorous defense of his economic agenda, rejecting critics who call his policies "socialism" and insisting he aims to boost U.S. competitiveness abroad.

**Soft demand greets \$42 bln in 5-yr U.S. Treasuries**

The U.S. government sold \$42 billion worth of five-year debt in a poorly bid auction that showed market fatigue with this week's record slate of bond sales.

Yields at the auction came in above expectations, based on trade in the when-issued market at the deadline for bids.

In another sign of weakness, foreign central bank and large institutional investor demand was low, based on the indirect bidder category, which accounted for 40 percent of the sale.

This was below the average of 51.68 percent in the auctions since June, which has become a benchmark for comparisons due to changes in calculations that have boosted this category.

It attracted bids worth 2.75 times the amount on offer, which was above the average of 2.62 times over the last six months.

The recently growing direct bid accounted for a hefty 13 percent of the sale, well above its 5.6 percent average since June.

**U.S. new home sales hit record low, prices tumble**

Sales of newly built U.S. single-family homes unexpectedly fell to a record low in January, while mortgage demand for purchases hit a 13-year low last week, fanning fears of renewed housing market weakness.

The Commerce Department said sales dropped 11.2 percent to a 309,000 unit annual rate, the lowest level since records started in 1963, from 348,000 units in December.

It was the third straight monthly drop in new home sales and the largest percentage decline in a year. Analysts, who had expected a 360,000 unit pace, said bad weather was partly to blame and warned of more of the same for February.

A separate report from the MBA showed mortgage applications fell for a third straight week, with demand for home purchase loans sinking to the lowest since 1997, hampered by inclement weather. Compared to January last year, new home sales fell 6.1 percent.

The median sales price for a new home fell 5.6 percent last month from December to \$203,500, the lowest since December 2003. That monthly decline reversed December's gain.

**No change to U.S. housing finance system this year**

Changes to the way U.S. homes are financed are not likely to take place until next year at the earliest, U.S. Treasury Secretary Timothy Geithner said.

Geithner told the House of Representatives Budget Committee that the administration would lay out "broad principles" for restructuring mortgage finance companies Fannie Mae and Freddie Mac this year, but he said detailed legislative proposals would not be offered until 2011. Congress would then have to debate and vote on the proposal for any changes to their structure before the president could sign then into law. Geithner also said he opposed a move to put trillions of dollars in obligations of the two government-controlled entities on the federal budget. Separately, Freddie Mac said it lost \$7.8 billion in the fourth quarter and warned it would need to tap more government funds this quarter as the housing market remains fragile.

The government-controlled entity said its loss came as rising defaults kept credit-related expenses elevated at \$7.1 billion and as it wrote down the value of low-income tax credit partnership investments.

The loss was \$6.5 billion before a \$1.3 billion dividend payment on senior preferred stock owned by the U.S. Treasury.

**U.S. SEC reins in short sellers with new restrictions**

U.S. securities regulators adopted a new rule to restrict short selling more than a year after the financial crisis provoked cries to rein in investors who bet on a stock's decline.

The SEC voted 3-2 to approve a rule designed to put the brakes on a stock that is falling precipitously. The new rule attempts to bridge the divide between those who argued a market-wide curb was needed to protect stocks from short sellers and others who said that restrictions would hurt market liquidity.

"The commission was cognizant of the benefits that short selling can provide to the markets," SEC Chairman Mary Schapiro said at a public agency meeting.

The SEC's actions drew a quick rebuke from famed short seller James Chanos, who said the new rule will harm investors' interests through higher transaction costs and missed opportunities.

Under the SEC's rule, if a stock fell by more than 10 percent in a day, a curb would kick in, allowing short selling only above the national best bid. That restriction would last for the day the stock dropped and the day after.



## TODAY'S TOP NEWS

**S&P says Greek rating cut possible "within a month"**

Standard and Poor's may downgrade Greece's BBB+ rating by one or two notches within a month, the agency said, citing downside risks to growth that could hinder the country's deficit-cutting plan.

S&P kept Greece on negative outlook and said it might also cut the rating if the government lost public support for austerity measures aimed at wrenching the country out of a debt crisis that has shaken the euro zone.

"Downside risks for Greece's real and nominal growth are likely to increase the size of needed fiscal consolidation, raising questions about the feasibility of the country's ambitious budgetary goals," S&P said.

Separately, Portugal placed all of the 1 billion euros (\$1.36 billion) in 5-year bonds on offer in an auction, but firm demand failed to prevent a rise in bond spreads on concerns about the fiscal problems in euro zone's most indebted countries.

The average yield climbed to 3.498 percent from 2.759 percent in the latest auction of a similar maturity in November.

**ECB to extend unlimited cash steps into Q3-sources**

The ECB is likely to extend banks' access to unlimited funds at fixed interest rates into the start of the third quarter at its March 4 meeting, as worries about Greece and sluggish growth weigh on financial markets, euro zone monetary sources told Reuters.

Unlimited access to cheap cash has been at the heart of the ECB's efforts to support banks through the financial crisis and analysts expect it to return to pre-crisis mode with liquidity measures before raising interest rates.

Sources said some policymakers would prefer longer-term loans to return to a normal auction procedure as early as the second quarter, although the ECB is aware of the need to smooth the repayment of close to half a trillion euros in 12-month funds on July 1.

Separately, raising inflation targets as part of the monetary policy pursued by central banks would be a "diabolical" error, ECB Executive Board member Lorenzo Bini Smaghi said.

**U.S. junk bonds may post double-digit returns -Pimco**

U.S. high-yield bonds could post investment returns in the high single digits to the low double digits this year after their record 58 percent return in 2009, Pimco said in a new report.

With yields still attractive and the risk of a financial system collapse largely in the past, "we believe investors can capture attractive yields and excess spread in the high-yield market with relatively low default risk," Andrew Jessop, high-yield portfolio manager at Pimco, said in a note on the company's Website.

High-yield bonds also look attractive compared with equities, which typically depend on faster growth to perform well at this point in the economic cycle, Jessop said. However, Pimco's forecast is that slower economic growth will become the "New Normal" amid broad deleveraging trends, increased regulation and de-globalization, he said.

Year to date, junk bonds have returned about 1.4 percent, according to Merrill Lynch indexes. Yields have declined to about 9 percent from over 22 percent during the credit crisis in 2008.

**China tells banks to limit loans to local govts**

China's banking regulator has told commercial lenders to tighten their grip on credit to local governments in an effort to ward off potential risks of default, state media reported.

The move is part of broader efforts, including raising bank reserve requirements, to check explosive lending growth that has set off concerns about asset price bubbles and the potential creation of a fresh crop of bad loans.

In the latest push, the CBRC ordered banks to inspect their existing loans to commercial units used by local governments to raise funds, and to stop lending to those projects that are backed only by expected fiscal revenues, the state-run Shanghai Securities News newspaper said, citing unidentified sources. That follows a decision by the top economic planning agency to tighten control over bond issuance by such investment vehicles, as worries mount over a buildup of local government debt.

About 40 percent of China's 9.6 trillion yuan (\$1.4 trillion) in new loans last year, or 3.8 trillion yuan, went to local governments, state media reported in January.

## NEXT UP

**U.S. Jan durable goods orders seen up 1.5 percent**

The median forecast for new orders for durable goods is for a 1.5 percent rise in January after a 1.0 percent gain in December. Forecasts range from a drop of 0.5 percent to a gain of 5.0 percent.

Stripping out transportation orders - which are heavily skewed by aircraft bookings - the median forecast for new orders for durables is for a 1.0 percent increase in January after a 1.4 percent gain the prior month. Forecasts range from a 1.8 percent drop to a 2.0 percent increase. The median forecast for nondefense capital goods excluding aircraft -- a key component of the monthly report seen as a gauge of business spending -- is for a 0.8 percent rise in January after a 2.2 percent gain in December. Forecasts range from a 1.5 percent drop to a 3.2 percent increase. An increase in civilian aircraft orders likely propelled new orders for U.S.-made durable goods in January. The expected rise in aircraft orders comes as U.S. plane maker Boeing Co reported that it won orders for 10 aircraft during January, building on the 59 orders placed in December. Excluding transportation, orders will likely rise with gains in the two metals categories as well as tech-related equipment.

**ECB to hold rates until late 2010, possibly 2011**

The ECB won't raise interest rates until the fourth quarter and no economist in the latest Reuters poll expected an early withdrawal of ECB liquidity measures as a result of the U.S. discount rate hike last week.

All 87 economists in a poll taken Feb. 22-24 said the central bank would keep rates at their record low of 1.0 percent next week, and gave only a 15 percent chance they would move them up by mid-year.

Median forecasts show interest rates on hold until the final quarter of the year when they will nudge up to 1.25 percent, but 35 of 86 see rates on hold until 2011. Economists gave a median 60 percent chance that rates would rise by the end of the year.

Rates are seen climbing to 1.5 percent by March next year and then rising by 25 basis points each quarter after that.

But it is clear that central banks are eyeing the exits after the worst financial crisis and global recession in nearly 80 years.

All 76 economists who answered the question thought the Fed's move, which caught many in the markets off guard, did not increase the likelihood of the ECB withdrawing liquidity measures any sooner.



## DEEP DIVE Commentary and Analysis

**One-touch with KO way to bet on rising dollar/yen**

By Marco Garavello

Dollar/yen is widely expected to grind higher in 2010 as Japanese government officials make clear their preference for a weaker yen to fight long-standing deflationary pressures in the economy.

Taking a simple long position in the cash market is a risky strategy though, as temporary retracements in the cross in periods of risk aversion may result in investors being stopped out. An option-based strategy allows more flexibility.

One way to bet on a medium-term rise in dollar/yen is to buy a nine-month one-touch option, a structure which pays a fixed payout if a topside strike is hit at any time. Adding a knock-out on the downside - a barrier which kills the option if triggered - makes the structure cheaper.

Japanese Finance Minister Naoto Kan and Prime Minister Yukio Hatoyama on Monday asked Bank of Japan Governor Masaaki Shirakawa to take appropriate steps to defeat deflation, citing difficulties in fixing Japan's finances with deflation.

The BOJ promptly reassured the government it would continue to provide ample funds to the financial markets.

The government fears deflation and a strong yen could hurt Japan's fragile recovery but it is limited in what it can do by the country's massive public debt.

Kan said shortly after his appointment in early January that many Japanese firms are in favor of an exchange rate in dollar/yen at around 95.00

Technical factors could also see dollar/yen rising in the medium term.

First, dollar/yen spot has shown a strong positive correlation in recent months with the spread between 10-year yields in the U.S. and in Japan.

As the spread started widening at the end of November 2009, dollar/yen started trending higher, albeit in a choppy fashion.

This positive spread is expected to stay - if not to widen - as U.S. rates remain supported on expectations of higher inflation, thus inducing some Japanese investors to pile more money into the greenback to benefit from the carry.

Second, launches of large toudains - investment trusts that allow Japanese retail investors to choose funds denominated in currencies other than the yen - like those announced this week, are expected to support dollar/yen and other crosses.

However, any move higher in dollar/yen is likely to remain choppy, as the cross may come under pressure in periods of risk aversion while exporters' hedging activity may also slow any uptrend.

As a result, investors may prefer an option strategy to a simple long position in spot.

A way to bet on a rise in dollar/yen in the medium term is to buy a nine-month one-touch option, which pays a fixed payout should 100.00 be hit at any time during the life of the contract.

As risk reversals still solidly point to the downside, buying topside strikes is relatively cheap. The benchmark 1-year 25 delta risk reversal contract is marked at 2.15/2.65 yen calls over, well above the lows reached at around 1.5 on Dec. 22 when spot was trading around current levels.

Adding a knock-out feature on the downside makes the structure even cheaper.

These are the details of the structure:

Spot reference = 90.50 Maturity = nine Months (Nov. 24, 2010)  
Buy USD/JPY One-touch strike = 100.00, Knock-out = 85.00  
Upfront premium at mid rates = 33 percent dollar notional  
Upfront premium of the equivalent one-touch option at mid rates = 42 percent dollar notional.

The structure offers an attractive risk reward profile of 1:3. The

knock-out level is placed conservatively at 85.00, just above the multi-year lows reached on Nov. 27 before the BOJ signaled its discomfort with the yen's strength by checking exchange rates with Japanese banks.

The knock-out feature makes the structure cheaper by 9 percent of the notional compared to the standard one-touch.

-- Marco Garavello is an FX market analyst for Reuters. The opinions expressed are his own --

**U.S. jobs market to support housing post incentives**

By Lucia Mutikani and Helen Chernikoff

The U.S. government will pull the plug soon on a popular tax credit that has helped prop up the struggling housing sector amid hope that a pickup in hiring will give the market a fresh shot of life.

Housing's fledgling recovery has leaned heavily on a popular tax credit worth up to \$8,000 for first-time buyers and purchases of mortgage-backed securities by the Federal Reserve that have lowered interest rates on home loans.

With the Fed's \$1.4 trillion in mortgage-related debt purchases ending next month and the tax credit expiring in June, there is concern the market might relapse and jeopardize the economy's recovery from its worst downturn in 70 years.

Fears have also been voiced that mortgage rates could rise sharply. Analysts reckon a rush by buyers to beat the June 30 deadline for the tax credit will boost sales in the traditionally busy spring selling period, but they expect a brief lull in the second half of the year.

Sales are then expected to pick up as the economic recovery filters through to the labor market, increasing demand.

"It (recovery) will continue. What I am counting on to bolster demand in the second half of this year is continuing economic expansion," said David Crowe, chief economist at the National Association of Home Builders in Washington.

"Sales will be driven by pent up demand along with low house prices and a return to positive employment growth."

Other economists agree. The labor market, hard hit by the housing-led recession, is expected to start showing job growth as early as March. The jobless rate has dropped from a 26-year high of 10.1 percent in October to 9.7 percent last month.

While mortgage rates are expected to rise by as much as a half-percentage point when the Fed's purchasing program ends, economists expect home loans will remain at affordable levels.

"Home prices are now down almost 30 percent from when they peaked in 2006, so even a 50 or 100 basis points move in the mortgage rates is not going to do substantial damage to the housing recovery," said Torsten Slok, an economist at Deutsche Bank in New York. A basis point is 1/100th of a percentage point.

**HOUSING CANNOT FALTER**

The rate for the 30-year fixed mortgage averaged 4.93 percent in the week ended Feb. 18, according to data from Freddie Mac, and analysts said the rate would have to rise to 6 percent to discourage potential home buyers.

Some analysts expect the Fed to step back into the mortgage market if rates rise too high.

"They can't allow the housing market to falter from here. If you are under 6.0 percent, affordability is still your friend. Sales won't be affected," said Josh Levin, a homebuilder analyst at Citigroup in New York.

Analysts said greater stabilization in the labor market contributed to a decline in mortgage loan delinquencies in the fourth quarter from the July-September period and a fall in the per-



## DEEP DIVE Commentary and Analysis

centage of loans on which foreclosure actions were started. The decline in delinquencies and foreclosures suggests a self-sustaining recovery is building.

Also boding well for a continued market recovery was a steady reduction in the number of homes on the market.

Economists at Deutsche Bank in New York noted that household formation was starting to run above the number of new homes coming on the market -- yet another factor that should support the sector.

Foreclosures remain a problem, however.

"There are currently about 5.5 million mortgages either seriously delinquent or in some stage of foreclosure," said Michelle Meyer, an economist at Barclays Capital in New York.

"We expect the pace at which these foreclosed properties enter the market as re-sales to accelerate in the near term, likely exceeding demand and, therefore, increasing the stock of distressed properties."

According to Meyer, the speed at which the foreclosed proper-

ties enter the market was key to gauging the risk to the housing recovery.

If there are a flood of foreclosed homes, prices will likely take a further tumble and new homebuilding activity would take a hit. Apart from foreclosures, builders are also worried they may not be able to access loans to meet the anticipated rise in demand from the pick up in employment.

"Right now homebuilders are finding it extremely difficult to borrow money to build houses. If that continues ... the builder won't be able to borrow money to build to the demand I expect to see as jobs are created," said the National Association of Home Builders's Crowe.

For some builders the time is just not right to end the incentives.

"I'm not sure this is the time for government to start putting back on their support for housing," Michael Sivage, chief executive officer of Sivage Home, which has operations in Texas and New Mexico.

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(Compiled by Anil Kumar and Pronita Naidu in Bangalore)

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