

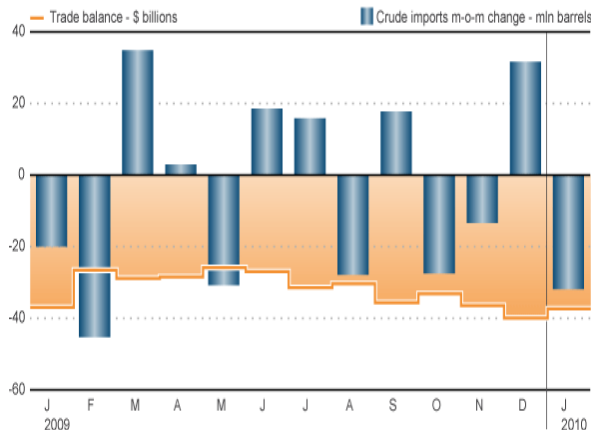
# INSIDE DEBT

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Thursday, March 11, 2010

## CHART OF THE DAY

### U.S. trade balance & oil imports



The U.S. trade deficit narrowed unexpectedly in January as oil imports fell to their lowest since February 1999, a government report showed.

## TODAY'S TOP NEWS

- U.S. jobless claims fall, trade gap narrows on oil
- Obama outlines strategy to boost exports
- China overheating fears grow, spurring tightening talk
- U.S. dollar still rules, but debt level a risk - S&P
- U.S. bank reform talks fail, overhaul hopes dim
- CFTC head scolds Wall Street for resisting reforms
- Four EU states call for inquiry into CDS market
- U.S. \$13 bln of 30-yr bonds draw robust demand
- Canada trade surplus, housing data signal recovery
- Japan growth revised down, adds to pressure on BOJ

## ECON WATCH FOR FRIDAY MARCH 12

ET	Indicators	Unit	Reuters	Prior
02:00	DE Wholesale price ind mm	%	0.3	1.3
02:00	DE Wholesale price index yy	%	2.3	1.9
05:00	EZ Industrial production mm	%	0.7	-1.7
05:00	EZ Industrial production yy	%	-1.9	-5.0
07:00	CA Employment change	k	20.0	43.0
07:00	CA Unemployment rate	%	8.3	8.3
08:30	US Retail sales mm	%	-0.2	0.5
08:30	US Retail sales ex-autos mm	%	0.1	0.6
09:55	US U.Mich sentiment prel	ind	73.6	73.6
09:55	US U.Mich conditions prel	ind	82.0	81.8
09:55	US U.Mich expectations prel	ind	68.0	68.4
10:00	US Business Inventories mm	%	0.2	-0.2

## MARKETS TODAY

**TODAY'S TOP STORY:** The number of U.S. workers filing new claims for unemployment benefits fell only slightly last week, indicating that rapid job growth would probably continue to elude the economy for a while.  
**For more please click here**

**TREASURIES:** Most U.S. Treasuries posted narrow price losses, but the 30-year bond advanced after the Treasury's third auction of the week successfully drew investors to the government's longest-term security.

- The government's sale of \$13 bln worth of 30-yr bonds concluded a series of well-bid auctions totaling \$74 bln.
- Short- and intermediate-term securities posted narrow losses, but the 30-yr bond moved higher after the auction.
- 30-yr bonds rose 14/32 in price, their yields easing to 4.66 pct from 4.69 pct on Wednesday.
- 10-yr notes fell 1/32 yielding 3.72 pct, while the 2-yr notes were down 3/32 to yield 0.95 pct from 0.91 pct.

**FOREX:** The dollar traded little changed versus major currencies after mixed data on U.S. trade and jobless claims failed to give investors direction.

- The euro rose 0.18 pct to \$1.3679. The euro peaked intraday at \$1.3687 with a low of \$1.3620.
- The dollar rose 0.06 pct to 90.54 yen, after touching a two-week high on Wednesday.
- The euro rose to a session high against the Swiss franc of 1.4630 francs, compared with 1.4610 just before SNB's comments on currency intervention. The euro was last at 1.4615 francs.

**CORPORATES:** U.S. corporate bond yield spreads were steady, as strong demand for this week's wave of new debt sales continued to support the market.

- The CDX.IG-13 index remained unchanged at 83 bps.
- Medtronic Inc launched \$3.0 bln of debt in a three-part sale.

**STOCKS:** Rising bank shares led a late-day rally, helping the S&P 500 hit a 17-month closing high and offsetting worries China may move to cool its overheating economy.

- Citigroup shares was up 5.56 pct at \$4.18. The KBW bank index rose 1.72 pct.
- Dow rose 0.42 pct to 10,611.84, S&P was up 0.4 pct to 1,150.23 and Nasdaq gained 0.4 pct to 2,368.46.
- An index of U.S. industrial shares slipped 0.3 pct, with diversified manufacturer 3M fell 0.37 pct at \$81.26.
- S&P financial index rose 0.91 pct, S&P technology rose 0.41 pct.

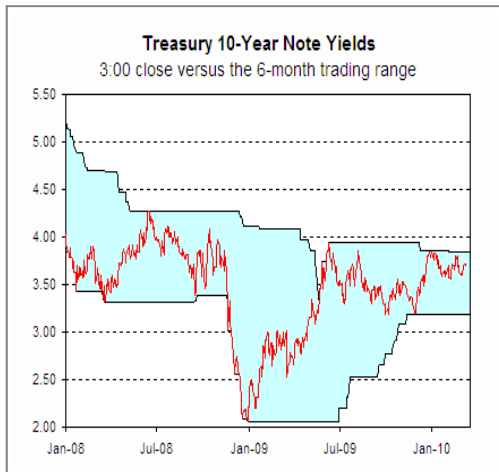
**C & E:** Oil settled nearly unchanged above \$82 a barrel amid uncertainty about whether China will tighten monetary policy, which could dent energy demand in the world's second-largest oil consumer.

- U.S. crude prices rose 0.19 pct to \$82.25 per barrel.
- Gold was little changed at \$1,108.5 an ounce.
- Reuters-Jefferies index was down 0.45 pct at 273.39.

- 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	0.125	0.09	0.127	-0.003
3-Mo Bill	0.150	0.140	0.152	0.003
6-Mo Bill	0.215	0.205	0.218	0.008
1-Year	0.385	0.380	0.391	0.012
2-Year	99.844	99.875	0.956	-0.082
3-Year	99.625	99.656	1.504	-0.102
5-Year	99.813	99.859	2.415	-0.133
7-Year	99.031	99.078	3.156	-0.086
10-Year	99.188	99.234	3.723	0.023
30-Year	99.359	99.438	4.665	0.484

**EQUITIES**

	INDEX	CHANGE
DJIA	10564.76	-2.57
NASDAQ	2357.55	-1.39
S&P 500	1144.47	-1.15

**OIL**

	PRICE	CHANGE
NYMEX	82.1	0.0
BRENT	78.2	-0.3

**EURODOLLAR FUTURES**

	CLOSE	CHANGE
Mar-10	99.738	0.000
Jun-10	99.615	-0.015
Sep-10	99.420	-0.020
Dec-10	99.120	-0.025

**REPURCHASE AGREEMENTS**

G/C		MORTGAGE REPOS	
O/N	0.210	O/N	0.210
2-Week	0.240	2-Week	0.240
1-Month	0.240	1-Month	0.240
3-Month	0.240	3-Month	0.280
AGENCY REPOS		i-REPO <sup>SM</sup> INDEX	
O/N	0.210	10:00 AM	0.150
2-Week	0.240	3:00 PM	0.151
1-Month	0.240		
3-Month	0.250		

**IR SWAPS <19901>**

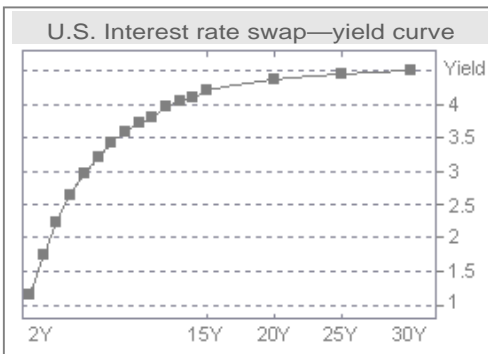
	SPREAD		RATE	
2-Year	19.00	23.00	1.14	1.16
3-Year	23.50	27.50	1.73	1.75
5-Year	23.50	27.50	2.65	2.65
7-Year	8.25	12.25	3.23	3.23
10-Year	1.75	5.75	3.74	3.73
30-Year	-17.75	-13.75	4.48	4.46

**FUTURES**

	PRICE	CHANGE
CBOT 5 yr	116.45	-0.12
CBOT 10 yr	117.88	-0.20
CBOT 30 yr	117.16	-0.41

**EURODOLLAR DEPOSITS & OIS STRIPS (ASKED)**

	BID	ASK	BID	ASK
O/N	0.150	0.170	-	-
1-Month	0.200	0.280	0.159	0.169
3-Month	0.220	0.400	0.177	0.187
6-Month	0.250	0.450	0.217	0.227
12-Month	0.600	1.000	0.381	0.391



**CURRENCIES**

	BID	ASK
Euro	1.3674	1.3676
Sterling	1.5053	1.5058
JP Yen	90.58	90.60
Swiss Franc	1.0689	1.0692
Can Dollar	1.0240	1.0246
Mexico	12.5799	12.5860

**FED FUNDS**

	NYFR <sup>SM</sup> - 10AM
Open	0.1600 1m 0.2175
High	0.1600 3m 0.2575
Low	0.1600

**ACTIVE FANNIE MAE AGENCIES**

TERM	COUPN	MATURITY	YIELD-SPREAD	YIELD
2-Year	1	04/04/2012	16.5 0	1.11
3-Year	1.75	22/02/2013	16.5 0	1.66
5-Year	2.875	09/02/2015	26 0	2.67
7-Year	5.125	18/10/2016	18.5 18	3.34
10-Year	-	-	- -	-
30-Year	6.625	15/11/2030	35.5 35	5.02

**ACTIVE FREDDIE MAC AGENCIES**

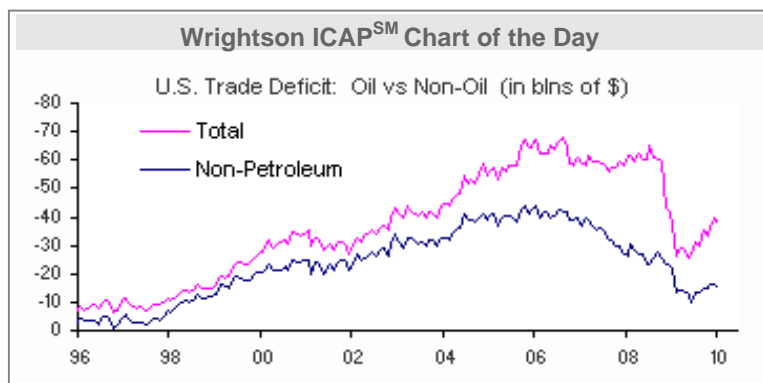
TERM	COUPN	MATURITY	YIELD-SPREAD	YIELD
2-Year	1.125	15/12/2011	-1 -6	0.94
3-Year	1.625	15/04/2013	25 0	1.75
5-Year	2.625	20/11/2014	16 14	2.56
7-Year	5.25	15/09/2016	17.25 16.75	3.33
10-Year	3.75	27/03/2019	21 19	3.96
30-Year	6.25	15/07/2032	36 34	5.04

**Active MBS 15YR**

	CPN	BID	ASK	YIELD
FNMA	5.0	105.2660	105.2720	2.859
FHLMC	5.0	105.2700	105.2700	2.887

**Active MBS 30YR**

	CPN	BID	ASK	YIELD
FNMA	5.5	105.1370	105.1430	3.005
FHLMC	5.5	105.2570	105.2630	2.907
GNMA	5.5	106.1070	106.1130	3.038



## TODAY'S TOP NEWS

**U.S. jobless claims fall, trade gap narrows on oil**

The number of U.S. workers filing new claims for unemployment benefits fell only slightly last week, indicating that rapid job growth would probably continue to elude the economy for a while.

Initial claims for state unemployment benefits slipped 6,000 to 462,000, the Labor Department said, a touch less than market expectations for a drop to 460,000.

Separately, the Commerce Department said the U.S. trade gap shrank 6.6 percent to \$37.3 billion in January as oil imports fell to their lowest since February 1999. Exports declined too. Analysts had expected the deficit to widen to \$41.0 billion.

After falling sharply in the second half of 2009, initial weekly jobless claims have stalled around 470,000 in recent months. Analysts say they need to drop to a 400,000 to 450,000 range to signal sustainable private-sector job growth.

U.S. imports fell 1.7 percent in January, while exports slipped 0.3 percent after rising in the eight prior months. Analysts shrugged off both declines and said they expected a reversal in February.

**China overheating fears grow, spurring tightening talk**

Chinese consumer inflation spurted to a 16-month high in February and a raft of economic data displayed broad-based strength, providing fresh arguments for policy tightening sooner rather than later.

The pace of credit growth halved in February, as expected, but some economists said the central bank would probably not wait long before increasing banks' required reserves for a third time this year and perhaps even raising interest rates or resuming gradual appreciation in the yuan.

CPI quickened to 2.7 percent in the year to February from 1.5 percent in the year to January, handily beating forecasts of 2.3 percent. Annual factory-gate inflation quickened to 5.4 percent in February from 4.3 percent in January. Economists had forecast 5.2 percent.

Factory output exceeded expectations, expanding 20.7 percent in January and February from year-earlier levels, while retail sales growth of 17.9 percent was just a touch lower than forecast. Still, investment growth of 26.6 percent in January and February beat market forecasts of a 26.0 percent rise.

**U.S. bank reform talks fail, overhaul hopes dim**

Chances of a broad overhaul of U.S. financial regulation dimmed after bipartisan Senate talks collapsed, helping boost bank share prices and jeopardizing a top Obama administration priority.

Senate Banking Committee Chairman Christopher Dodd, warning that time was running out to pass legislation this year, said he would unveil his own bill on Monday and aim to get it to the Senate floor by Easter.

Earlier, Senator Bob Corker said a simultaneous White House push to get healthcare reform through Congress had thrown a wrench into their effort. The list of administration priorities that are now in peril is steadily lengthening.

Dodd said he was setting out his own proposals in an effort to keep the process moving in a year cut short by congressional elections in November. He said his committee would begin considering the bill the week of March 22. The bill Dodd will unveil on Monday contains some elements negotiated with Corker, both senators emphasized, but key stumbling blocks, including how much authority to give to a new consumer financial protection agency, remain.

**Obama outlines strategy to boost exports**

President Barack Obama, anxious to spur growth and tackle high unemployment, laid out a plan for tougher enforcement of trade laws, government advocacy and credit assistance to double U.S. exports in five years.

Obama also prodded China to move to a "more market-oriented exchange rate," which he said would make a big contribution to putting the global economy on a healthier path after the worst economic downturn in decades.

That means the United States cannot "stand on the sidelines" as other countries are busy negotiating trade deals, said Obama, who first announced his goal of doubling exports in his State of the Union speech in January.

High U.S. unemployment is fueling anxiety about trade and trade agreements, which many of the president's fellow Democrats blame for million of manufacturing job losses.

But when the United States negotiates trade deals, it must aggressively enforce those agreements to make sure other countries honor the commitments they make, Obama said.

Many believe the biggest trade challenge the United States faces is China, which has kept its currency pegged at 6.83 yuan to the dollar since July 2008.

**U.S. dollar still rules, but debt level a risk - S&P**

The U.S. dollar is still the most important world currency, Standard & Poor's said, but added that rising levels of U.S. debt and dependence on foreigners to finance much of pose risks to the currency's primacy.

Without a credible plan to rein in fiscal spending, the agency said external creditors could reduce dollar holdings, which could put pressure on the United States' 'AAA' credit rating, which keeps government borrowing costs low. For now, the credit ratings agency said the size of the U.S. economy and the depth of its financial markets mean the dollar will continue to dominate global trade and foreign exchange transactions. The agency also said the dollar's role is an important factor supporting the United States' AAA credit rating -- the highest investment-grade rating. The main risk to the dollar's status comes from the growing amount of U.S. government debt, S&P said, particularly the share held by foreign central banks and sovereign wealth funds. Separately, benchmark costs for banks borrowing dollars around the globe rose to a 3-1/2 month high as markets wondered if the U.S. Federal Reserve would signal the end of zero-rate policy next week.

**CFTC head scolds Wall Street for resisting reforms**

The head of the top U.S. futures regulator chided Wall Street for resisting calls to make over-the-counter derivatives markets more transparent, arguing major reforms are required after the recent financial crisis. Laying out his case for more oversight of the unregulated market he estimates is worth \$300 trillion -- arguments he has made repeatedly as lawmakers hash out reforms -- Gary Gensler took financial firms to task for putting their shareholders ahead of the public interest. Gensler's push comes as European regulators are moving forward with their own ideas about how to limit risk in the over-the-counter market and restrictions on the trading of credit default swaps, which some have pointed to as the cause behind the global financial crisis.

Separately, an overwhelming majority of Americans wants Wall Street subjected to tougher regulation in the aftermath of the bank bailout and the bonus scandals that have rocked the U.S. financial sector, according to a Harris poll.



## TODAY'S TOP NEWS

**Four EU states call for inquiry into CDS market**

An inquiry must be opened into the role and impact of speculation linked to credit default swaps trading in EU government bonds as soon as possible to determine any market abuse, the heads of four countries said. The move stops short of repeating recent calls for an immediate ban on selling CDS contracts to 'naked' buyers who have no interest in the underlying asset -- thereby making it easier to find broad backing from the bloc's finance ministers who will discuss CDS markets next Tuesday. The moves would be aimed at preventing undue speculation, enhancing transparency and improving the safety of derivative transactions, according to the letter, which was released by the office of French President Nicolas Sarkozy.

Separately, EU policymakers injected a dose of cold reality into talk of creating a European monetary fund, questioning who would pay for it and stressing the principle of no bailouts for countries in trouble must stay. Eurogroup Chairman Jean-Claude Juncker said such a fund should protect only the interests of the entire euro zone, not any individual member of the currency bloc.

**U.S. \$13 bln of 30-yr bonds draw robust demand**

The U.S. government attracted robust demand at its offering of \$13 billion worth of 30-year bonds, ending a series of well-bid auctions on a resoundingly strong note.

The long-bond sale, a reopening of previously issued debt, was the last of this week's three bond offerings totaling \$74 billion and should tamp down for now any worries over the government's ability to attract investors in numbers. The auction drew bids worth 2.89 times the amount on offer, outperforming the average of 2.58 at the last six reopenings of 30-year bonds.

In one apparent weak note, foreign central bank and large institutional investor demand, gauged by the indirect bidder category, appeared weak, accounting for about 24 percent of the sale. This was well below the average of about 43 percent in the reopenings since June, which has become a benchmark for comparisons due to changes in calculations that had boosted this category.

**Canada trade surplus, housing data signal recovery**

Canada's economy showed more signs of recovery in January as the trade surplus and new home prices continued to climb, adding to strong fourth-quarter data to suggest higher interest rates could be around the corner.

Statistics Canada said the trade surplus grew more than expected in January to C\$799 million (\$776 million) as higher prices for commodities such as gold boosted exports, while imports fell. Markets had expected a C\$100 million surplus.

New home prices climbed 0.4 percent in the month and 0.1 percent from January 2009, the first 12-month increase in over a year. In another report on the fourth quarter, Statscan said industries ramped up their production to 70.9 percent of capacity from 68.7 percent in the previous quarter, the first substantial jump in three years.

Canada's trade surplus with the United States narrowed slightly to C\$4.1 billion from C\$4.2 billion in December due to lower auto sales.

**Japan growth revised down, adds to pressure on BOJ**

Japan's economy grew less than initially estimated in the fourth quarter and a broad gauge of price trends posted the biggest negative reading on record, adding to pressure on the Bank of Japan to ease monetary policy further next week.

The BOJ is leaning towards doing exactly that at its policy meeting on March 16-17, sources familiar with the central bank's thinking said, but there is disagreement among its seven board members on how to justify such a move.

Deputy finance minister Yoshihiko Noda said that he wanted to attend the BOJ's meeting next week and that he believes the BOJ has a sense of crisis -- comments most likely intended to push the central bank further towards easing policy.

The economy grew 0.9 percent in the October-December quarter, slower than the preliminary estimate of 1.1 percent and a median market forecast of 1.0 percent, as capital spending rose less than initially reported and as private inventories subtracted from growth, data by the Cabinet Office showed.

## NEXT UP

**Fed seen keeping "extended period" low rate vow**

Lingering U.S. labor market weakness and nagging doubts about the solidity of the economic recovery are expected to keep the Federal Reserve committed to holding borrowing costs very low for a long time at a monetary policy meeting next week. The Fed is widely expected to hold benchmark U.S. rates near zero and reiterate that conditions warrant keeping them "exceptionally low" for an "extended period."

The Fed may leave open the possibility they could resume if the recovery falters.

Most Fed officials have emphasized that high unemployment and tame inflation warrant a continued promise to hold rates very low for a long time.

The Fed is expected to say that its purchases of around \$1.7 trillion of assets will end as planned March 31. However, in light of the modest pace of recovery, it may well leave the door to further buying unlocked, saying it remains ready to modify plans if necessary to support stability and growth.

Some pressure is building within the committee to temper the extended period language by substituting something vaguer like "some time."

**Snowstorms seen damping U.S. Feb retail sales**

Snowstorms that blanketed parts of the country last month probably dampened U.S. retail sales. Recalls by Toyota Motor Corp likely combined with the bad weather to weigh on auto sales. According to industry data, auto sales fell 3.7 percent to an annualized 10.8 million units in February.

Excluding autos, retail sales probably edged up. Chain store sales rose strongly last month, with some retailers posting their best monthly sales performance since just before the start of the recession in December 2007.

The median forecast for retail sales is for a fall of 0.2 percent after a 0.5 percent rise in January. Forecasts range from a drop of 1.0 percent to an increase of 0.9 percent.

The median forecast for sales excluding autos is for a gain of 0.1 percent after an increase of 0.6 percent in January. Forecasts range from a fall of 0.8 percent to a rise of 0.6 percent.

But a combination of inclement weather and lower gasoline prices is expected to have depressed receipts from gasoline stations, holding back sales excluding autos.

Even if the data comes out somewhat less upbeat, the market would likely discount the weather impact.



## DEEP DIVE Commentary and Analysis

**Boutique boom fading as Wall St banks expand**

By John Parry

The window of opportunity is closing for boutique bond trading firms to make a killing from market turmoil as big Wall Street banks regain their footing and rehire staff.

During the financial crisis and its aftermath, bid/offer spreads, or the gap between the price for selling or buying a bond, widened dramatically, offering opportunities for middlemen.

Small boutique firms reaped much of the profits from these wider spreads. Many bond salesmen, traders and analysts who fell victim to layoffs or jumped ship from the big firms seized a lucrative opportunity at these smaller shops which pay commissions on trading profits.

Now the tables are turning. As the credit crisis has abated, reducing market volatility, bid/offer spreads have slammed shut over the past several months, squeezing profits at smaller brokerages.

Though boutiques are still hiring, the biggest banks and brokerages have returned to profit. They are taking greater risks and taking on staff.

Cheap credit is allowing big firms to trade bonds in volumes that swamp smaller rivals and compensate for lower profit margins.

In their search for new talent, some big banks are rehiring staff who defected to the boutiques.

"The big guys now are pushing the others aside," said John Jay, senior analyst at Aite Group, a Boston-based market research consulting company. "The larger firms have decided that in a more stable environment they are willing to take a little more of an aggressive stance."

**LOWER SPREADS, LOWER PROFIT**

Among the boutique firms that embarked on a hiring drive were Broadpoint Capital, BTIG, Cantor Fitzgerald and Chapdelaine Credit Partners. Several are hiring more staff, including BTIG, an institutional broker dealer, which said this week it has launched a U.S. convertible securities business.

But conditions are becoming more challenging for boutiques. As big Wall Street firms increase hiring, "it's getting more competitive," said Sandy Ewing, a principal and founding partner of Chapdelaine Credit Partners.

When the crisis was at its height, the cost of buying a bond priced at par value, or 100 cents on the dollar could be as much as one cent, an unusually wide spread, said one bond market veteran.

Average bid/ask spreads on the highly liquid 30-year Treasury bond, have narrowed to around 0.03 of a percentage point, the tightest since October 2007. That compares to a wide of around 0.14 of a percentage point in January 2009, the biggest in at least eight years, according to TradeWeb data.

So on a \$100 million trade, the bid/offer difference has narrowed to about \$30,000 now from \$140,000 then.

For less liquid corporate bonds, the widening of bid/offer spreads in the crisis was much bigger, so the subsequent narrowing has been more pronounced, analysts say.

"All that spread to be made probably evaporated inside of nine months or so," said Jay. Last year was especially profitable for firms trading distressed debt in the secondary market, but activity in that sector has dropped off sharply since the start of this year, Jay said.

**GIANT COMEBACK**

The Wall Street behemoths which came close to collapse in the crisis have repaid government bailout funds. Their business has been boosted by a rebound in prices of company bonds and stocks and a surge in government and corporate debt issuance.

Corporate bond yields have fallen since the crisis, enabling companies to borrow more cheaply via new debt sales. A near record volume of corporate bond issues has enabled the behemoths to pick up more fees for underwriting these deals, unlike the boutiques.

"An important factor is that as the new issue market has opened, the bigger banks are well positioned to do new issues and the smaller brokers are not positioned to compete in the same way," said Erlend Lochen, head of U.S. credit and global head of high yield with Standard Life Investments in Boston.

Better functioning lending markets are helping replenish the traditionally deep pockets of the big U.S. investment banks. That helps them borrow heavily to "leverage" their own bets on bonds and magnify potential trading profits.

As they amass more capital, bigger banks and brokerages are stepping up hiring.

Peter Gonye, co-leader in search firm Spencer Stuart's private equity and investment banking practice in North America says over the past six months he has seen some senior staff move from boutiques to sell-side firms. The big Wall Street firms are looking to replace people they are now losing to hedge funds and money management firms, he said.

Job cuts have slowed to a trickle as hiring has started to pick up over about the last year.

The pace of planned U.S. financial sector job cuts decelerated sharply in 2009 to 51,505 according to outplacement firm Challenger, Gray & Christmas Inc., down from 260,110 in 2008, a record high since 1997 when Challenger started compiling financial sector data.

Last month, only 375 planned job cuts were announced in the financial area, the lowest monthly number in a decade.

**ABS supply seen steady as issuers re-assess strategy**

By Nancy Leinfuss

As the U.S. asset-backed market emerges from a crisis period and bids farewell to government assistance, new regulations and lower consumer credit demand are expected to contain issuance.

Consumer ABS issuance is expected to remain close to the \$140 billion of supply sold last year with the help of the Federal Reserve's emergency loan facility as issuers reassess strategy amid a changing securitization landscape.

"The fact of the matter is that TALF, likely the most successful government program in the market to date, is now gone and we believe the consumer ABS market will survive just fine without it," said Ajay Rajadhyaksha, analyst at Barclays Capital, who expects issuance to remain unchanged in 2010.

The Fed's Term Asset-Backed Securities Loan Facility (TALF) has been credited with revitalizing the consumer ABS market that was locked in the grips of a credit crunch in 2008 through early 2009. Through the program, liquidity was pumped back into the market, soaring funding costs fell and issuance resumed.

"The financial crisis and recession has been the most serious test of the non-mortgage ABS market in its 23-year history," said John McElravey, analyst at Wells Fargo Securities. "The market recovered in 2009, and our expectation is for conditions to improve further in 2010."

Under TALF, issuers sold \$105 billion of securities backed by auto loans, credit cards and student loans. The Fed made \$56 billion in loans to investors to purchase securities during a year-long program that expired in March.

Another \$35 billion of non-TALF sales were sold as the market recovered.



## DEEP DIVE Commentary and Analysis

## A CHANGING LANDSCAPE

Still, while issuers are actively selling securities on their own amid markedly improved conditions in the ABS market, a new securitization landscape that includes new accounting rules and regulatory changes has emerged, forcing some to re-assess whether securitization is the right funding tool.

That, and lower credit demand from consumers hurt by high unemployment and a weak economy, is expected to temper volume.

ABS issuance has totaled \$25 billion so far this year and has been largely led by auto issuers. The segment also drove supply in 2009 with \$69 billion of sales.

By contrast, supply from the credit card segment, which led issuance in prior years, has been noticeably absent with just \$1 billion in sales this year following \$46 billion in 2009.

Bank credit card lenders are expected to use ABS to a lesser degree than in the past given recent regulatory changes and the rising costs of securitization through higher credit enhancement. Some are turning to the corporate bond market, or relying on their own deposit base to fund new consumer loans.

"The significant inflow of deposits to commercial banks after the financial crisis and the increase in deposit insurance may make balance sheet funding a better option for credit card ABS issu-

ers," said McElravey.

New accounting changes require off balance sheet credit card securitizations held by banks in separate trusts to be moved back on balance sheet, thereby eliminating capital relief.

"Securitization will lose its capital advantage in many cases now that ABS programs will need to be consolidated on balance sheet," said McElravey.

Mike Kagawa, ABS portfolio manager at Payden & Rygel, expects to see supply fall as credit card issuers look to fund debt elsewhere.

"If you look at the credit card issuers, some are using alternative means of financing like the unsecured market over securitization," said Kagawa.

Another factor that will curb the rise in issuance is falling demand for credit from consumers struggling with loss of jobs during an economic recession. Many have opted to pay down debt and curtailed spending and borrowing.

U.S. consumer revolving debt, which comprises credit and charge cards, has fallen for 16 consecutive months through January 2010.

"There's the issue that people are paying down their credit cards and revolving debt continues to fall. That lessens the need for securitization," said Kagawa.

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(Compiled by Anil Kumar and Pronita Naidu in Bangalore)

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