

INSIDE DEBT

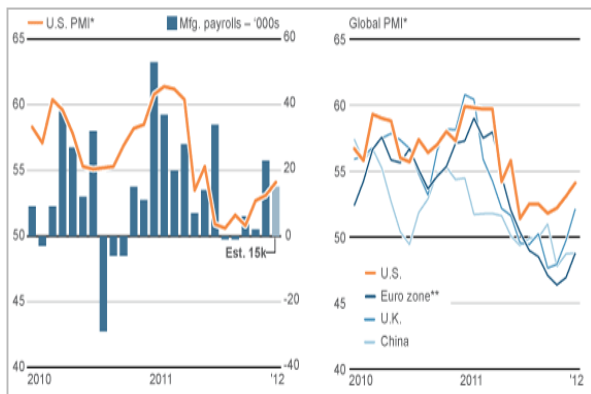
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Wednesday, February 1, 2012

CHART OF THE DAY

U.S. and global manufacturing

Click on the chart for full-size image



U.S. manufacturing continued its expansion in January, and analysts expect 15,000 jobs were added to the sector. Globally, manufacturing activity expanded in the U.K., but contracted in the euro zone and China (HSBC PMI).

TODAY'S TOP NEWS

- U.S. manufacturing picks up, but private job gains slow
- World factory output curbed by troubled Europe
- Euro zone inflation stable, bets still on for ECB rate cut
- Markets warm to European debt, Portugal pressure eases
- Obama presses Congress to step up aid for homeowners
- Belgium slides into recession
- U.S. Treasury studies negative-yield debt auctions

ECON WATCH

FOR THURSDAY FEBRUARY 2

ET	Indicators	Unit	Reuters	Prior
05:00	EZ Producer Prices mm	%	-0.2	0.2
05:00	EZ Producer Prices yy	%	4.3	5.3
07:30	US Challenger Layoffs	k	--	41,785
08:30	US Initial Claims	k	375	377
08:30	US Continuing Claims	mln	3.55	3.554
08:30	US Productivity	%	0.8	2.3
08:30	US Unit Labor Costs	%	0.8	-2.5
09:45	US ISM New York	ind	--	534

- For EYE ON ASIA click here
- For MARKET SNAPSHOT on Asia click here
- For EYE ON LATAM click here

U.S. MARKETS TODAY

TODAY'S TOP STORY: U.S. manufacturing growth accelerated in January to its highest level in seven months, though a measure of employment faded and private-sector employers added fewer jobs than expected, data showed. **For more please click here**

TREASURIES: Treasury prices fell as investors, encouraged by improving manufacturing data and hopes of an orderly debt restructuring by Greece, snapped up riskier assets such as stocks and corporate bonds.

- Traders said much of the price action was likely related to technical factors, such as position squaring, and said most investors were set for further yield gains.
- 10-yr notes dropped 11/32, yielding 1.83 pct from 1.80 pct and 30-yr bonds slumped more than a point to yield 3 pct from 2.94 pct.

FOREX: The euro rose amid renewed optimism that Greece will reach a deal with its creditors while the yen hit a three-month high versus the U.S. dollar for a third day, increasing speculation that Japan may step in to halt its rise.

- The euro was up 0.54 pct at \$1.3153, off an earlier low of \$1.3023 and closer to the session peak of \$1.3218. Analysts said the euro would need to breach technical resistance at the 38.2 pct retracement of its October-January decline, around \$1.3235.
- The dollar fell to 76.00 yen and was last at 76.21, down 0.03 pct from the prior close and the fifth straight day of declines.
- The euro was up 0.51 pct at 100.24 yen, having dropped to 99.22.
- The euro was last up 0.07 pct at 1.20 francs with the session low at 1.2028 francs.

CORPORATES: Corporate bond spreads tightened on upbeat global PMI data and Greece neared a long-delayed deal on its debt swap.

- The CDX.IG-17 index tightened by 1 bps to 100 bps.
- New issuers included, Aurora Oil & Gas Limited, Energy Future Intermediate Holding and Codere Finance.

STOCKS: Stocks extended January's rally after upbeat global manufacturing data boosted sentiment and as Greece neared a long-delayed deal with private creditors.

- Dow gained 83.55 points or 0.66 pct to 12,716.46, S&P rose 11.67 points or 0.89 pct to 1,324.08 and Nasdaq climbed 34.43 points or 1.22 pct to 2,848.27.
- Caterpillar rose 1.28 pct, Bank of America gained 3.22 pct Citigroup rose 2.86 pct, while Amazon slid 7.7 pct.
- Index of housing stocks rose 1.84 pct.

C & E: Crude futures ended lower on pressure from a government report showing crude and gasoline stockpiles rose sharply last week in the United States.

- Oil lost 1.04 pct to \$97.46 per barrel.
- Gold added 0.35 pct to \$1,743.2 an ounce.
- Reuters-Jefferies index slipped 0.25 pct to 311.53.

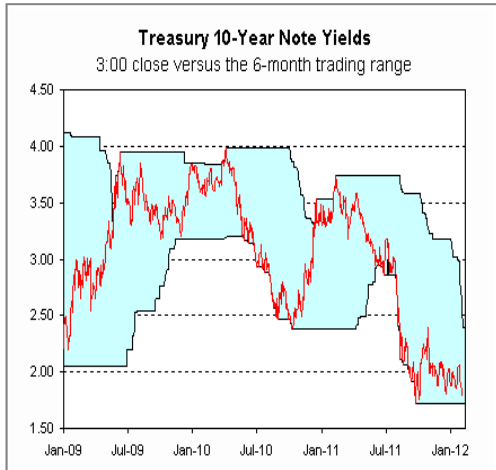
For a video preview of next week's economic events, [click here](#)

REUTERS INSIDER

- 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	0.065	0.035	0.066	0.013
3-Mo Bill	0.065	0.050	0.066	0.004
6-Mo Bill	0.090	0.080	0.091	0.008
1-Year	0.125	0.100	0.127	0.006
2-Year	100.039	100.070	0.231	-0.016
3-Year	99.844	99.875	0.304	-0.016
5-Year	100.711	100.750	0.730	-0.098
7-Year	99.953	100.000	1.257	-0.086
10-Year	101.656	101.719	1.814	-0.125
30-Year	102.078	102.141	3.019	-1.563

EQUITIES

	INDEX	CHANGE
DJIA	12761.00	127.11
NASDAQ	2851.18	37.23
S&P 500	1328.30	15.81

COMMODITIES

	PRICE	CHANGE
NYMEX	97.6	-0.8
BRENT	111.7	0.7
SPOT GOLD	1744.4	7.2
PALLADIUM	692.2	11.4
SILVER	33.8	0.6

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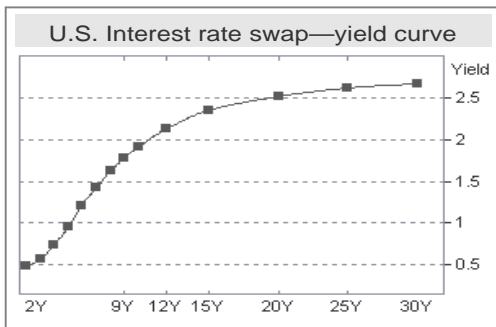
	SPREAD		RATE	
2-Year	26.25	30.25	0.49	0.52
3-Year	25.75	29.75	0.56	0.59
5-Year	23.75	27.75	0.96	0.99
7-Year	16.50	20.50	1.44	1.46
10-Year	8.00	12.00	1.93	1.94
30-Year	-32.75	-28.75	2.69	2.69

EURODOLLAR FUTURES

	CLOSE	CHANGE
Feb-12	99.51	0.01
Mar-12	99.57	0.03
Jun-12	99.57	0.03
Sep-12	99.55	0.03

REPURCHASE AGREEMENTS

G/C		MORTGAGE REPOS	
O/N	0.250	O/N	0.290
2-Week	0.220	2-Week	0.250
1-Month	0.210	1-Month	0.240
3-Month	0.200	3-Month	0.250
AGENCY REPOS		i-REPO SM INDEX	
O/N	0.260	10:00 AM	0.200
2-Week	0.220	3:00 PM	0.197
1-Month	0.220		
3-Month	0.220		



FUTURES

	PRICE	CHANGE
CBOT 5 yr	123.99	-0.05
CBOT 10 yr	131.97	-0.28
CBOT 30 yr	144.38	-1.06

EURODOLLAR DEPOSITS & OIS STRIPS (ASKED)

	BID	ASK	BID	ASK
O/N	0.090	0.120		
1-Month	0.240	0.350	0.093	0.103
3-Month	0.340	0.490	0.098	0.108
6-Month	0.540	0.690	0.104	0.114
12-Month	0.820	1.030	0.112	0.122

NYFRSM - 10AM

1m	0.2495
3m	0.5222

FED FUNDS

Open	0.1000
High	0.2200
Low	0.1000

CURRENCIES

	BID	ASK
Euro	1.3161	1.3162
Sterling	1.5834	1.5838
JP Yen	76.24	76.26
Swiss Franc	0.9151	0.9154
Can Dollar	0.9982	0.9984
Mexico	12.8880	12.8960

ACTIVE FANNIE MAE AGENCIES

TERM	COUPON	MATURITY	YIELD-SPREAD	YIELD
2-Year	0.5	8/9/2013	1 -2	0.233
3-Year	0.75	12/19/2014	12.5 9.5	0.423
5-Year	1.25	1/30/2017	25.5 22.5	0.981
7-Year		-		
10-Year				
30-Year	6.625	11/15/2030	22.5 19.5	3.242

ACTIVE FREDDIE MAC AGENCIES

TERM	COUPON	MATURITY	YIELD-SPREAD	YIELD
2-Year	0.375	11/27/2013	5.5 2.5	0.278
3-Year	0.625	12/29/2014	13 10	0.428
5-Year	1	3/8/2017	28.5 25.5	1.011
7-Year		-		
10-Year	2.375	1/13/2022	46.5 43.5	2.313
30-Year	6.25	7/15/2032	24.5 21.5	3.262

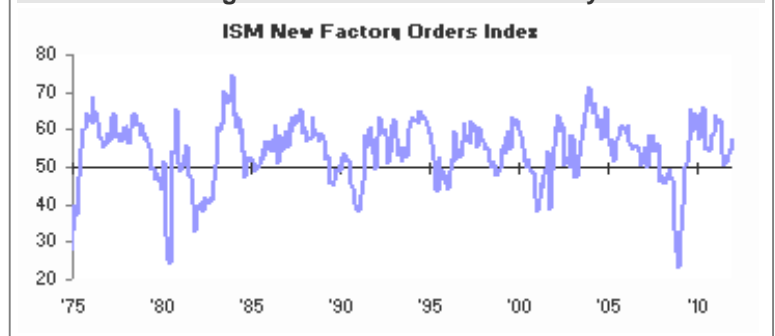
Active MBS 15YR

	CPN	BID	ASK	YIELD
FNMA	3.5	105.0450	105.0510	2.391
FHLMC	3.5	105.0500	105.0500	2.235

Active MBS 30YR

	CPN	BID	ASK	YIELD
FNMA	4.0	105.1860	105.1920	1.970
FHLMC	4.0	105.1120	105.1160	2.079
GNMA	4.0	107.2460	107.2520	2.020

Wrightson ICAPSM Chart of the Day



TODAY'S TOP NEWS

U.S. manufacturing picks up, but private job gains slow

U.S. manufacturing growth accelerated in January to its highest level in seven months, though a measure of employment faded and private-sector employers added fewer jobs than expected, data showed.

The Institute for Supply Management said its index of national factory activity rose to 54.1, from a revised 53.1 the month before, and was the highest level since June 2011. It fell just short of expectations for 54.5. The private sector added 170,000 jobs last month, the ADP National Employment Report showed, shy of economists' expectations for a gain of 185,000 jobs.

Uncertainty over the outlook for the U.S. economic recovery also prompted the central bank to signal it will keep interest rates at ultra-low levels for nearly three years.

But top central bank official Charles Plosser criticized the Fed for that move, saying it undermined confidence and caused confusion. The ISM new orders gauge for manufacturers gained to 57.6 from 54.8, while the employment index slipped to 54.3 from 54.8.

Separate data from the Commerce Department showed construction spending jumped in December to its highest level in more than 1-1/2 years, breezing past expectations.

Separate data showed borrowing by small businesses rose in December to the highest level in more than four years, suggesting underlying strength for an important part of the economy.

Euro zone inflation stable, bets still on for ECB rate cut

Consumer price inflation in the euro zone remained at 2.7 percent for the second straight month in January, data showed, off last year's peak and supporting bets that the European Central Bank will cut rates to help revive the economy.

Inflation in the 17 countries sharing the euro was in line with expectations of economists polled by Reuters and unchanged from December, as rising unemployment cuts into household spending and pushes businesses to freeze or reduce prices.

Although the January reading was only a first estimate by the European Union's statistics office Eurostat, economists see inflation slowing over the next few months as many of the euro zone's nations slip into a brief recession in 2012.

Obama presses Congress to step up aid for homeowners

President Barack Obama called on Congress to approve a \$5 billion to \$10 billion effort to help U.S. homeowners refinance as part of a wider package of proposals to shore up the depressed housing market.

Obama had sketched out the proposals in his State of the Union address last week, including a tax on banks to pay for the plan that Republicans quickly rejected.

The White House offered more details ahead of a speech by Obama to expand on his initiative, which some Republicans have derided as an election-year ploy.

Nearly 11 million Americans are underwater on their mortgages, meaning they owe more than their homes are worth. Millions more have lost homes to repossession in states that will be up for grabs in 2012.

Meanwhile, the regulator for mortgage finance companies Fannie Mae and Freddie Mac said investors could now sign up to pre-qualify to bid on foreclosed properties held by the government-controlled firms.

Separately, a proposed settlement to resolve mortgage abuses by top U.S. banks will give states broad authority to punish firms that mistreat borrowers in the future, according to documents seen by Reuters.

World factory output curbed by troubled Europe

Crumbling global demand restrained factory output in Asia and most of Europe in January, business surveys showed, putting pressure on policymakers to shore up growth and counter a spreading malaise.

The Eurozone Manufacturing Purchasing Managers' Index, compiled by Markit, rose to 48.8 last month from 46.9, revised up from a flash reading but recording its sixth month below the 50 mark that divides growth from contraction. French manufacturing contracted again in January, as did major economies Spain and Italy, as well as Greece and Ireland. Data from Britain was decidedly more upbeat than the figures from continental Europe, showing its manufacturing sector unexpectedly grew in January. The PMI rose to 52.1 from 49.6, easily beating expectations for 50.0.

The official China PMI inched up to 50.5 in January from 50.3, which was welcome news. But new export orders fell sharply, again underscoring the troubles in Europe. The HSBC Markit PMI for China told the same if slightly more negative tale, holding at 48.8 in January. Comparable figures due later from the United States, the world's biggest economy, are expected to show an uptick in activity as well. India bucked the gloomy trend, with factory activity growing at its fastest pace in eight months. Unlike most of its Asian peers, India's economy is far less exposed to export demand. The PMI reading of 57.5 in January marked almost three years of expansion in the manufacturing sector.

Markets warm to European debt, Portugal pressure eases

Cautious optimism that the euro zone crisis may be turning a corner fuelled demand for European government debt, easing pressure on Portugal, seen as the most vulnerable country after Greece.

Portuguese bonds led a rally in debt issued by the euro zone's lower-rated states, capitalising on a successful treasury bill auction and on increased confidence a deal to reduce Greece's debts to private bondholders will be clinched this week.

Ambitious economic reform programs announced by the new governments of Italy and Spain have helped improve market sentiment around the euro's future, although there are concerns that a deep recession in southern Europe may yet derail debt reduction efforts. In Greece, Prime Minister Lucas Papademos sought backing from political leaders for more austerity measures, with the International Monetary Fund warning that long-term, cross-party commitment to reforms is key to securing a new bailout. With a long-delayed agreement with private sector creditors to cut the country's debt by 100 billion euros nearly wrapped up, the EU, the IMF and Greece are racing to complete talks on a 130-billion-euro bailout by the end of this week.

Belgium slides into recession

Belgium fell back into recession in the second half of last year, data showed, the first euro zone member not subject to a bailout program to do so. It paved the way for what is expected to be a very difficult 2012 for the 17-member bloc, both core economies and those in the debt-ridden periphery.

Gross domestic product in Belgium shrank by 0.2 percent in the fourth quarter, following a quarterly contraction of 0.1 percent in the July-Sept period. Final quarter figures for the euro zone, which grew by 0.2 percent in the third quarter, will be published on Feb. 15. Greece and Portugal, which with Ireland are being bailed out by the European Union and others, are both struggling in recession.

TODAY'S TOP NEWS

U.S. Treasury studies negative-yield debt auctions

The U.S. Treasury Department is studying the possibility of holding auctions that would allow for a negative yield after Wall Street advisers unanimously recommended it do so as soon as possible, a Treasury official said.

The Treasury announced a \$72 billion quarterly refunding of three-year, 10-year and 30-year debt securities to take place next week and said the sales will raise \$22.4 billion of new cash. "Treasury believes that the current issuance schedule and offering size for notes and bonds are adequate to address forecasted borrowing needs over the near term," Treasury Assistant Secretary Mary Miller said in a statement.

Separately, financial firms that deal directly with the Federal Reserve told the Treasury Department they believe it would not take much to trigger another round of central bank bond buying, the Treasury said.

"For now, it would appear the Fed has exhausted their options for easing policy through communications," the primary dealers said at quarterly meetings with Treasury officials to discuss the government's borrowing plans.

Central Europe rides German wave in Jan, led by Poland

Manufacturing jumped to its highest level in six months in Poland in January, while contractions in Hungary and the Czech Republic revealed improvements in exports reflecting a better than expected start to the year in main market Germany.

Poland's Purchasing Managers Index, a survey of factory activity, jumped to its highest level in six months in January to 52.15 points, well above the 48.8 sounding that signalled a contraction in December and also above analysts' forecast of 49.4.

In the Czech Republic and Hungary, where exports account for two thirds to three quarters of output, manufacturing was below the 50 point line that marks the boundary between expansion and contraction.

The Czech Purchasing Managers' Index shrank to 48.8 in January from 49.2 in December. Hungary's PMI, compiled under different methodology than the Czech and Polish figures, increased to 49.8, from a revised 48.6 in December.

China economy faces downward risks in 2012 -FinMin

China's economy faces downward risks in 2012, as weakening external demand cuts into growth of the country's export sector, the Finance Minister Xie Xuren said in remarks published.

He also said inflationary pressures in China remain strong as international markets are awash with cash, which has helped push up global commodity prices.

"There exists some downward pressure for the economic growth. As the external demand is now fading clearly, Chinese exporters are facing increasing difficulties," Xie said in an article published in the ruling Communist Party's mouthpiece magazine, Seeking Truth, which was posted on the central government website.

Xie also emphasized the important role of fiscal policy in maintaining China's steady and relatively fast economic growth and said Beijing would continue to implement a proactive fiscal policy this year.

S&P: Japan sales tax plan relief only temporary

The Japanese government's plan to double the 5 percent sales tax will slow growth in public debt only temporarily as the government needs to raise taxes further and cut spending to improve its finances, Standard & Poor's said.

Decisions on the sales tax alone are unlikely to be a trigger for a ratings or outlook change as Japan's rating also depends on its long-term economic growth, the credit ratings agency said. The appropriate level for the sales tax depends in part on the state of the economy, and the government needs to time tax hikes to ensure they lead to an overall increase in revenue, according to the ratings agency.

"Even if the sales tax plan is approved, the horizon for implementation is long," Takahira Ogawa, director of sovereign ratings at S&P, told Reuters in an interview.

"When we look at the sovereign rating, we have to look at economic growth conditions in the long term." S&P's rating on Japan is AA-, three notches below the highest rating. The outlook is negative, meaning there is a chance of a downgrade.

NEXT UP

POLL-BoE to ramp up QE in Feb, ECB to cut rates in Mar

The Bank of England will announce next week that it will pump an extra 50 billion pounds of money into the UK economy, just as the chances of the European Central Bank starting its own money printing scheme fade, a Reuters poll showed.

Despite signs from business surveys that Europe's economy might be perking up, economists say both Britain and the euro zone are afflicted by profound economic weakness that will require further central bank action.

The ECB looks likely to cut interest rates in March from their record low 1.0 percent down to 0.75 percent, almost in line with its British peer that has left rates on hold at 0.5 percent for almost three years. Next to act to provide further monetary stimulus will be the BoE. Forty-nine of 56 economists thought the central bank will announce a new round of asset purchases next week worth a median 50 billion pounds (\$79 billion), which would take the total spent since March 2009 to 325 billion pounds.

The poll suggested there was just a median 20 percent chance the ECB will start making unsterilized bond purchases, down from 30 percent in January and 40 percent in December.

Only 13 out of 71 economists thought the ECB will cut interest rates to 0.75 next week, although 41 thought they would do by the March meeting.

PREVIEW-Spain tries again to clean up troubled banks

Spain's government will force its banks to recognize some 50 billion euros (\$65.5 billion) in losses on bad loans to builders in a fresh financial sector reform on Friday, but doubts will still linger over the worthless property on the banks' books.

The aim is to trigger a fresh wave of mergers to create stronger new banks four years after a property boom went bust and restore confidence to Spain, which has yet to shake off the euro zone debt crisis.

The new centre-right government has pledged to straighten out the banks once and for all, but officials are worried the reform will put great strain on Bankia, Spain's fourth-biggest bank by market value, which is particularly exposed to real estate.

The reform will give newly merged banks up to two years to write down toxic assets by setting aside provisions on their books, other banks will get one year, said several sources close to the negotiations on the new rules.

EYE ON ASIA

POLL & PREVIEW

China banks, brokerages see PBOC cutting RRR once in Feb

Chinese banks, brokerages and other financial institutions expect the country's central bank to cut banks' reserve requirement ratios once by 50 basis points in February, meaning the market is moderately optimistic about returns on fixed-income products, a Reuters poll showed.

More than 70 percent of the 24 domestic banks, brokerages and other financial institutions participating in the monthly Reuters fixed income poll believe the People's Bank of China will cut the RRR once this month.

Roughly the same proportion of institutions expect the central bank to cut required reserves twice over the next three months in all, for a total cut in the ratio of 1 percentage point.

Most expect China's government bond market will be mildly bullish in February as a result, with yields on 10-year treasury bonds expected to fall around 6 basis points to around 3.35 percent on average by the end of the month, the poll showed.

None of the participants expected the PBOC to cut benchmark interest rates in February, citing still high inflation, although nearly 30 percent of them said the central bank might cut rates once in the next three months, with the one-year deposit rate being cut by 25 bps to 3.25 percent.

EVENTS

For Feb 2

AUSTRALIA

- Building approvals final for December: Expected 2.0 pct Prior 8.4 pct
- Private house approvals final: Prior 4.8 pct
- Trade balance G&S in A\$ final: Expected 1200 mln Prior 1380 mln

CHINA

- German Chancellor Angela Merkel will start a two-day visit to China.
- People's Bank of China is expected to sell 3-month bills and might conduct 91-day repos.

INDONESIA

- Indonesia's finance ministry is expected to announce an indicative target for a debt auction on Feb. 7. The ministry's debt office is supposed to sell three-month and one-year T-bills, as well as 15-year and 20-year bonds.

JAPAN

- Bank of Japan Deputy Governor Hirohide Yamaguchi is expected to speak at Takamatsu, he could take this opportunity to shed some insight on the BOJ's next move, its take on recent developments in Europe.

MARKET SNAPSHOT as of 3:00 pm EST

GOVERNMENT BOND BENCHMARKS					EQUITIES			FORWARDS 3 months <FORWARDS>		
	5-Year		10-Year			Close	Change		Bid	Ask
	Bid	Yield	Bid	Yield						
Australia	112.203	3.340	116.182	3.852	S&P/ASX200	-	-	JPY	-6.85	-6.35
Japan	99.832	0.335	100.315	0.965	NIKKEI 225	8809.79	7.28	AUD	-102.34	-101.75
China	102.329	3.010	101.336	3.400	HKSE	20333.37	-57.12	NZD	-49.6	-48.6
Hong Kong	101.200	0.572	99.050	1.298	SHANGHAI	2268.08	-24.53	HKD	-6	-3
Singapore	102.600	0.493	106.450	1.506	STRAITS TIMES	2904.76	-1.93	SGD	-3.8	-3.3
					SENSEX	17300.58	107.03	THB	18	18.4
INTEREST RATE SWAPS <SWAPS>					DEPOSITS 3 months <DEPOS>			NDF's 3 months <NDFS>		
	5-Year		10-Year			Bid			Bid	Ask
	Bid	Ask	Bid	Ask						
AUD	4.1625	4.2225	4.55	4.605	JPY	0.18		CNY	-0.018	-0.013
JPY	0.4275	0.4875	0.9325	0.9925	CNY	5.2		TWD	-0.075	-0.055
CNY	3.92	4.02	3.92	4.12	AUD	4.6		KRW	1133	1134
HKD	0.87	0.95	1.62	1.7	NZD	2.95		INR	50.53	50.63
TWD	1.02	1.04	1.27	1.31	HKD	0.3		MYR	3.057	3.061
INR	5.85	6.05	5.8	6.2	SGD	0.25		PHP	42.98	43.08
KRW	3.3925	3.4325	3.545	3.585				IDR	9010	9110
SGD	1.04	1.07	1.87	1.91						

EYE ON LATAM

LATAM TOP STORIES

Brazil trade hit by global slowdown, tough 2012 eyed

Brazil posted its first trade deficit in two years in January as the global economic slowdown curbed demand for commodities, official data showed, raising pressure on President Dilma Rousseff to come up with measures to aid exporters. Brazil posted a trade gap of \$1.29 billion in January, the worst ever on record for that month, down sharply from the \$398 million surplus in January 2011, the Trade Ministry said. In December, Brazil posted a trade surplus of \$3.8 billion. Exports in January plummeted 27 percent from December, mostly due to a drop in exports of iron ore. Brazil is the world's No. 2 exporter of the raw material used to make steel.

Mexico 2012 inflation forecast rises-cenbank poll

Mexican inflation expectations for 2012 rose for the fourth month in a row, but policymakers see temporary factors behind the spike and will likely keep interest rates steady this year. Analysts polled by the central bank now see a 3.79 percent rise in consumer prices this year after inflation rose to a one-year high just under 4 percent in early January. Analysts saw a 3.69 percent annual rate for 2012 in the last monthly poll. Mexico's central bank said on Tuesday the recent spike in inflation was due to high food prices that should not stoke wider pressures, while the impact of weakness in the peso would be temporary.

Growth estimates also ticked up, the central bank said, as analysts factored in improving economic prospects in the United States, Mexico's top trading partner.

Analysts forecast 3.33 percent for economic growth in 2012, higher than the 3.23 percent expected in the last poll but slower than the 4 percent rate that the finance ministry said the economy grew last year.

According to Mexican interest rate swaps, investors see the country's central bank holding its benchmark rate at 4.50 percent through 2013.

Colombia registers lower deficits in 2011-sources

Colombia registered lower than expected fiscal deficits in 2011 thanks to strong tax collections in Latin America's fourth-largest economy, market sources told Reuters.

The market sources, who had just emerged from a meeting with the finance ministry, said that the consolidated deficit for last year was 2.2 percent of gross domestic product, down from the previous estimate of 2.9 percent.

The central government deficit was 2.9 percent of GDP from a previous estimate of 3.2 percent, they said.

In December, Colombia announced it expected to issue up to 24.7 trillion pesos in TES bonds in 2012 of which 18 trillion pesos would be sold at auction.

Peru CPI surprises with first fall since May

Consumer prices in metropolitan Lima fell 0.10 percent in January, the first time prices have fallen in eight months, Peru's government said. Economists polled by Reuters had expected the index to rise 0.15 percent, but analysts said the surprise fall in inflation is not likely to prompt the central bank to cut the benchmark interest rate when it meets on Feb. 9.

Peru's national statistics agency, which released the Lima inflation data, also said national consumer prices fell 0.03 percent countrywide in January, the first time it had included a national

LATAM MARKETS TODAY

TREASURIES:

- Mexican 10-yr notes were down, yielding 5.95 pct and 30-yr bonds fell yielding 7.34 pct.

FOREX:

- Brazilian real was down 0.86 pct to 1.7339 per dollar.
- Mexico's peso lost 1.14 pct to 12.8925.
- Chile peso slumped 0.91 pct to 486.95 per dollar.
- Colombia's peso slipped 0.55 pct to 1,799.6 to the dollar and Peru sol was unchanged at 2.688 to the dollar.

STOCKS:

- MSCI Latin American stock index added 2.23 pct to 4,141.59.
- Oil producers, mining companies and homebuilders drove gains in Brazil's benchmark Bovespa index. The index gained for a tenth session in twelve, rising 2.37 pct to 64567.18.
- OGX surged 5.68 pct, Vale rose 2.01 pct. Homebuilder Gafisa added to Tuesday's 6 pct rally, gaining 5.87 pct. Limiting gains, Banco Bradesco fell for a second day, and it was down 0.22 pct.
- Mexico's IPC index rose for a third straight day, gaining 0.77 pct to 37,709.65, America Movil led the index higher, gaining 0.92 pct and Femsa rose 2.42 pct.
- Chile's IPSA index rose for a second straight day, adding 1.31 pct to 4,316.37.
- Cencosud added 3.53 pct and Endesa Chile rose 2.28 pct.

LATAM TOP STORIES

(continued)

calculation in its monthly report. The Lima inflation data has long served, for analysts, as the yardstick for national inflation. Transportation costs measured in the Peruvian capital rose sharply in December due to holiday travel, but fell 0.94 percent in January, according to INEI. Consumer prices in metropolitan Lima rose 0.27 percent in December. January was the first drop in prices the since May 2011, when prices dropped by 0.02 percent. Even with the January fall, inflation in the past 12 months was 4.23 percent, much higher than 3 percent, the upper edge of the central bank's target range.

Brazil mulls commodity derivatives bourse-report

The Brazilian government is considering the creation of a bourse focused on trading of derivatives contracts on agricultural commodities to help protect farmers against unwanted price swings, a local newspaper said.

One alternative under review would put futures contracts on some commodities on the BM&FBovespa's BM&F commodities trading platform, Valor Economico said, citing an unnamed source familiar with the situation.

Another alternative could be creating a shadow bourse in which only derivatives contracts on some agricultural commodities would be traded, the newspaper said. Brazil President Dilma Rousseff ordered the studies, which are in a preliminary stage, Valor noted. A spokeswoman for the Brasilia-based presidential palace did not have an immediate comment. The country is one of the world's largest producers of poultry, beef, orange juice, grains, coffee and other foodstuffs.



DEEP DIVE Commentary and Analysis

ANALYSIS - Why ECB liquidity is not reaching Portugal

By Swaha Pattanaik

A slump in Portuguese bond prices in the past month shows there are parts of the euro zone government debt market that massive shots of cheap money from the European Central Bank cannot reach.

Italian, Spanish and Irish bonds have all rallied as banks used some of the 489 billion euros they borrowed from the ECB in December to buy such debt, a profitable trade because the special three-year loans were so cheap.

But this cash has not helped Portugal, whose borrowing costs recently rose to levels that could eventually force it to seek a second international bailout or even a debt restructuring.

"It doesn't work for Portugal because, for it to work, people need to be persuaded that the economy and the debt (situation) are sustainable," said Bill Blain, senior director at Newedge.

"Investors are being pragmatic. They are looking at the sustainability of Portuguese debt and saying there will have to be a restructuring. They are more confident about buying Spain and Italy because these are big bond markets where banks are piling in surplus liquidity."

LOOKING AFTER NUMBER ONE

The conditions of the bailout Portugal received from the International Monetary Fund and European Union last year also help explain why the country's own banks aren't ploughing ECB loans into the government bond market.

The lenders said Portugal must ensure its banks increased the capital they set aside in case loans they had made turned sour. The banks are therefore putting aside more cash and cutting lending.

"The Portuguese banks have to reduce their loan to deposit ratio and while the IMF's fear is that it might happen too fast, it would be a contradiction to ask Portuguese banks to make full use of the LTRO (the ECB's three-year loans) to buy sovereign debt," said Gilles Moec, co-head of European economic research at Deutsche Bank.

Given this backdrop, and a need for all European banks to build up a bigger capital buffer against exposure to government debt, Portuguese banks have not been among the biggest borrowers from the ECB.

A Credit Agricole CIB analysis of central bank data estimated they borrowed far less than banks from many other countries -- including Italy, Spain, France, Greece, Netherlands, Ireland and Germany.

There was very little net increase in Portuguese banks' ECB borrowing once Credit Agricole analysts had taken into account the value of their maturing ECB loans.

By contrast, they estimate Italian, Spanish, French, Greek and Italian banks borrowed twice as much from the ECB as they needed to roll over maturing loans, leaving them spare cash to buy government bonds.

AVOIDING JUNK

Of course, those foreign banks who borrowed more ECB money than they needed could have bought Portuguese bonds.

But Portugal is traditionally more dependent than Spain or Italy on overseas investors buying its bonds and this is working against it as foreigners stay away.

They are concerned about Portugal's deteriorating economic outlook, its lack of competitiveness, and the scale of the fiscal problems the government has to fix.

And those financial institutions and investors still holding Portugal's debt started to think again after Standard & Poors cut its credit rating to junk on Jan. 13.

"There is clear evidence from flows that there has been a steady loss of confidence in Portugal since the summer of last year," said Simon Derrick at Bank of New York Mellon.

"What is noticeable is that in mid-January you see a pick up in these outflows which coincides with the credit downgrade."

Portuguese 10-year bond yields soared above 17 percent this week, prompting the ECB to buy Portuguese debt in the secondary market to bring them down again.

While the central bank's intervention is helping in the short term, analysts say trading conditions in the Portuguese bond market may have deteriorated beyond the point of no return.

One of the most worrying developments has been the widening gap between the prices that banks quote to buy Portuguese bonds and those they quote to sell them.

The wider this gap, known as the bid/offer spread, the harder it is to make money by buying and selling a financial asset.

"You can drive a truck through the bid/offer spread and so no-one is buying Portuguese bonds in any significant amount, apart from the ECB," said Frederik Ducrozet, euro zone economist at Credit Agricole CIB in Paris.

"Restructuring makes no sense on fundamental grounds but this is not about fundamental reasons or rational behaviour because we are well beyond that point and this is a broken market."

ANALYSIS - Europe in the 99-cent bin

By Chris Taylor

With the Standard & Poor's 500 Index off to its best January in 15 years, it's getting tougher to find cheap stocks in the United States. But it's not much of a problem in Europe.

Sovereign default worries have made the region's shares the cheapest they've been to American investors since 2004.

Companies in the S&P Europe 350 are trading at around 10 times earnings for 2012, compared to 12.2 for the S&P 500. That means investors are getting a 20 percent-plus discount for looking across the pond.

For good reason, of course. Investors are still nervous about the future for European equities, since no one yet knows how the debt crisis is going to play out. On any given day, fresh rumors abound regarding the dismal outlook of nations like Greece, Spain, or Italy.

For speculators with nerves of steel, the point of maximum fear is when you can often make your most lucrative bets. And big, blue-chip European companies - the powerful multinationals that aren't going to disappear, no matter what happens to Portuguese bond yields - look to be on sale. With their U.S.-listed ADRs (American Depositary Receipts), buying shares is a snap.

"There are a lot of European companies that look attractive right now," says Stan Pearson, head of European equities for Standard Life Investments. "Focus on world-class companies with geographic diversification and strong balance sheets. Then you won't even have to make a judgment about the Euro, because those companies will be able to weather whatever happens."

Some of Pearson's favorites: Danish drugmaker Novo Nordisk, with its strong diabetes franchise, and Belgium's Anheuser-Busch InBev, the brewer behind Budweiser and Beck's. Both happen to be headquartered in Europe, but are worldwide cash machines that aren't about to be felled by any sovereign debt troubles. For 2010 InBev threw off the equivalent of \$7.5 billion in free cash flow, and Novo Nordisk \$2.8 billion.

As always with deep-value investing, you'll have to be prepared to sidestep falling knives. And in Europe, the sky seems to be full of them. As a result, it's probably wise to stay away from European financials for the time being, which are particularly exposed to the region's economic woes. Utilities should also



DEEP DIVE Commentary and Analysis

give you pause - they're highly regulated and tied to particular regions.

Instead, hunt for names with a healthy portion of their operations and profits overseas, and that boast manageable debt, solid earnings and decent yield. That's the kind of profile that attracts Robert Quinn, chief European equity strategist for S&P Capital IQ. One top pick: Telecom goliath Vodafone for its international breadth and reasonable forward P/E of 10.2 paired with a juicy 5.4 percent yield. Among sectors, Quinn likes consumer staples, energy, insurance and telecoms but is shying away from consumer discretionary and diversified financials.

An added bonus of investing in Europe: The average yield on equities is much higher than in the U.S. market - almost double, in fact. That should provide downside support, and appeal to income-hungry baby boomers as well. France Telecom currently yields almost 13 percent, for instance, while oil giant Total offers 5.6 percent.

If you're willing to take a risk on our beleaguered friends across the Atlantic, here's what investors should keep in mind:

Look for stocks that have taken an unfair beating. Limit your shopping to robust franchises where potential bad news is already baked into the numbers. German industrial giant Siemens has tanked 35 percent from last spring -- from \$145 to under \$95 -- making it low-hanging fruit for U.S. investors, according to

Joe Tatusko, chief investment officer of wealth managers Westport Resources. It boasts low debt, lofty return-on-equity, and nearly half its sales are outside of Europe.

Despite the currency ties, countries within Europe all have very different economic outlooks, though. Germany, for instance, is no Italy when it comes to its finances. As a result, stocks focused on Northern Europe will generally be less risky than those operating in the Mediterranean region.

Currency issues will play a role. If the Euro is in for a rough ride, as many analysts predict, it could actually provide an earnings jolt for European megacaps. "By year-end we expect the Euro to trade closer to \$1.10," says Christopher Vecchio, a currency analyst for foreign-exchange site DailyFX. "A weaker currency is generally supportive of European multinationals, because it lowers production costs and helps exports."

Saddle up for a bumpy ride. If you do buy into Europe, don't expect volatility to decrease anytime soon. Ratings agencies are on the warpath, with Fitch recently downgrading the debt of five euro zone countries including Spain, Italy and Belgium. Until visibility becomes clearer, it will take time for your bargain shopping to pay off. "Go in with a two-year time horizon," says Standard Life's Pearson. "The backdrop is still very uncertain, and you're going to be bounced around by the headlines for a while yet."

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