

Weekly Update

20 April 2009



Market Intelligence Straight to your Business

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LOOK AT THINGS DIFFERENTLY

 **BANK OF SCOTLAND**
TREASURY

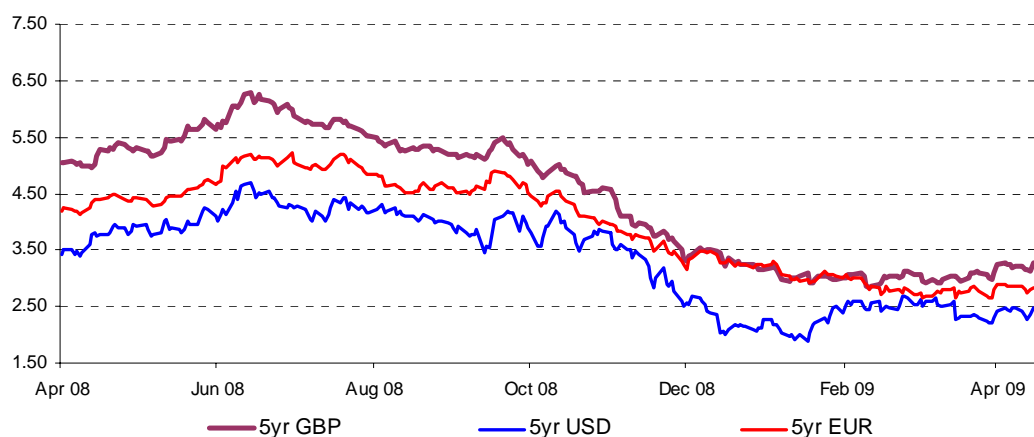
Indicative Swap Rates

	£		€		\$	
	Today	1 week ago	Today	1 week ago	Today	1 week ago
OFFICIAL RATE	0.50%	0.50%	1.25%	1.25%	0.25%	0.25%
3 MONTH LIBOR	1.52%*	1.57%	1.41%*	1.44%	1.10%*	1.14%
6 MONTH LIBOR	1.75%*	1.80%	1.60%*	1.63%	1.64%*	1.69%
12 MONTH LIBOR	1.98%*	2.01%	1.77%*	1.78%	1.92%*	1.96%
2 YEAR	2.30%	2.19%	1.99%	1.94%	1.55%	1.46%
3 YEAR	2.74%	2.64%	2.33%	2.32%	1.91%	1.82%
5 YEAR	3.29%	3.20%	2.84%	2.87%	2.45%	2.40%
7 YEAR	3.58%	3.49%	3.20%	3.25%	2.79%	2.76%
10 YEAR	3.83%	3.74%	3.55%	3.60%	3.08%	3.06%
20 YEAR	4.15%	4.01%	4.04%	4.08%	3.41%	3.41%
30 YEAR	4.03%	3.86%	3.93%	3.89%	3.42%	3.43%

Rate quotes taken from the inter-bank mid-market.

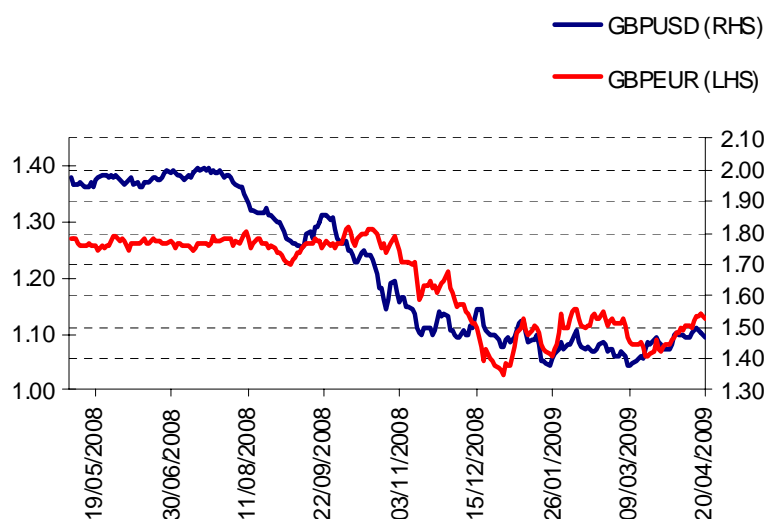
Swap rate quote conventions - UK: Semi, Actual/365 vs. 6M Libor Euro: Annually, 30/360 vs. 6M Libor US: Annually, Actual/360 vs. 3M Libor

*Friday's close



Market Levels

	Today	1 week ago
GBP/USD	1.4650	1.4854
GBP/EUR	1.1265	1.1113
EUR/USD	1.3004	1.3368
GBP/JPY	145.10	148.70
FTSE 100	4104.8	3983.7
Euro Stoxx 50	2338.8	2247.9
*S&P 500	869.6	856.6
**Nikkei 225	8924.8	8924.4
Gold (\$/oz)	870.5	893.9
Brent Crude (\$/barrel)	52.0	53.9
Gilt Future	122.1	122.3
T-Bond	129.8	131.0
Bund	122.0	121.8



* Friday's closing rate

** Monday's closing rate

Commentary

Economics & Interest Rates: Equity markets have broadly continued their six-week upswing. The US S&P500 rose by around 1% during the week (FTSE Eurofirst 300: +4.2%, FTSE-100: +2.6%, Nikkei: -0.6%). Banking stocks performed well on the back of better-than-expected Q1 results from Goldman Sachs, JPMorgan and Citigroup. This further increase in risk aversion kept government bond markets on the back foot, with gilts underperforming both the euro-zone and US Treasuries in the run-up to Wednesday's UK Budget.

There is little doubt that Chancellor Alastair Darling will publish significant downgrades to his GDP projections for 2009/10 and 2010/11. We look for the mid-point of Mr. Darling's GDP forecast range to be around -3.5% for this fiscal year and +0.5%, next. Compared with November's Pre-Budget Report (PBR), these represent downward revisions of 2.5 and 1.25 percentage points, respectively. A sharply weaker economic outlook clearly implies public sector net borrowing (PSNB) numbers even bigger than those published in last year's PBR. Market estimates centre on an average £175bn shortfall in 2009/10 and 2010/11, some £60bn higher in each fiscal year.

The DMO's gross gilt issuance number will be crucial for the outlook for the UK government bond curve. In mid-March, the DMO reported a gilt funding requirement of £147.9bn for 2009/10, around 65% of which is to be met from the short and medium-dated sector. But this was based on a central government net cash requirement (CGNCR) forecast from the PBR. A more up-to-date figure for gilt funding might be in the order of £180-200bn – a big commitment by any standards. A flatter gilt curve seems possible given the area of issuance. In broad terms, we look for a fairly neutral Budget, with the Chancellor's hands tied in terms of affordability of 'giveaways' alongside the risk of choking off recovery in an effort to improve the public finances via the tax system.

This week's economic data calendar features UK March CPI, April MPC minutes and latest labour market data. The level of claimant

count unemployment could well breach 1.5 million this week. In the euro-zone, ECB President Jean-Claude Trichet has repeated his preference for tackling the region's economic problems through the banking system, rather than implementing fully-fledged quantitative easing (QE). Economic data this week include various business surveys, including Germany's ZEW / Ifo reports and Thursday's preliminary PMI manufacturing and services surveys. It will be interesting to see if the expectations components of the Ifo survey, along with the "headline" ZEW survey, continue to show signs of improvement. But weak external demand remains the main drag on euro area activity at present.

Currencies: On the whole the rally in equities appears mostly isolated. Commodity prices have been relative stable - the CRB (our favoured broad commodity index) has exhibited a huge reduction in volatility as the index has flattened out. In terms of FX, the follow through has not been as expected - usually growth sensitive currencies would rally alongside equities - with NZD/USD drifting lower last week and the AUD/USD stalling at its 200 moving average.

Whilst economic data are showing a slight up tick (last week both the empire and Philly Fed surveys showed marked improvements), the data continue to signal contraction. In such an environment the rally in equities, which are moving from an extremely oversold state, is unlikely to be sustained much longer. At that point we would look for another move higher in the USD. In fact the USD DXY index has broken through key resistance (at 86.125) this morning.

The focus this week is firmly on the UK budget. Concerns over the amount of public borrowing will dominate the FX market reaction. With the Chancellor set to announce a significant budget deficit, the downside risks to sterling are clear if the public sector net borrowing numbers come in larger than consensus. As well as the budget announcement, downside risk to sterling this week arises from interest rate spreads. GBP/USD has failed to sustain a foothold above \$1.50 and a break through the 100-day MA (\$1.4531) would open the way for a move down towards \$1.40.

Key Economic Releases This Week

Date	Time	Cntry	Release/Event	Period	Forecast	Consensus	Previous
21-Apr	09.30	UK	CPI	Mar	-0.4 (-0.1)	-0.3 (0.0)	-0.5 (0.9)
21-Apr	10.00	GER	ZEW – Economic Sentiment	Apr	-1.0	2.0	-3.5
22-Apr	09.30	UK	Claimant Count Change	Mar	110.0k	100.0k	138.4k
22-Apr	12.30	UK	Budget 2009	-	-	-	-
23-Apr	09.00	EUR	"Flash" PMI Services	pApr	41.2	41.5	40.9
23-Apr	09.00	EUR	"Flash" PMI Manufacturing	pApr	34.5	35.4	33.9
24-Apr	09.00	GER	IFO Survey – Expectations	Apr	82.3	82.6	81.6
24-Apr	09.30	UK	GDP	aQ1	-1.5 (-3.8)	-1.5 (-3.8)	-1.6 (-2.0)
24-Apr	09.30	UK	Retail Sales	Mar	-0.7 (1.1)	-0.5 (1.3)	-1.9 (0.4)

Annual rates shown in brackets. Consensus figures taken from Bloomberg poll

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