Weekly Update
26 May 2009

Market Intelligence Straight to your Business

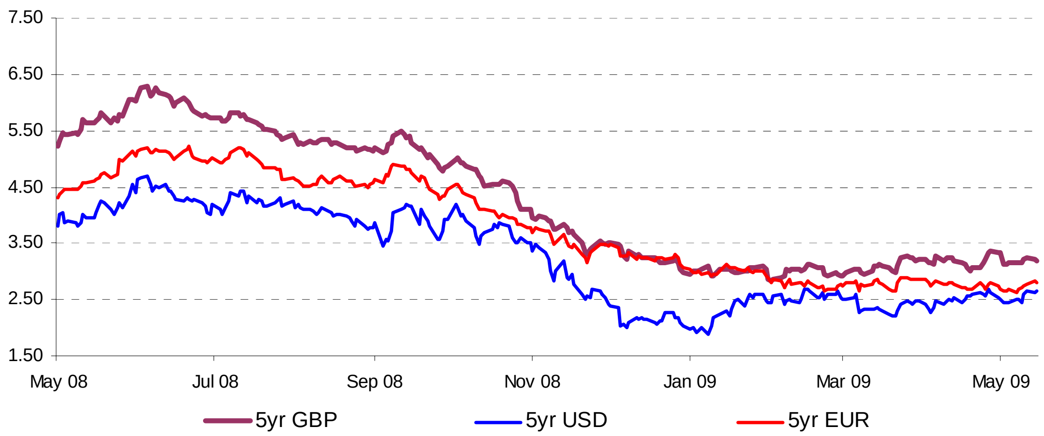
LOOK AT THINGS DIFFERENTLY

BANK OF SCOTLAND
TREASURY

Indicative Swap Rates

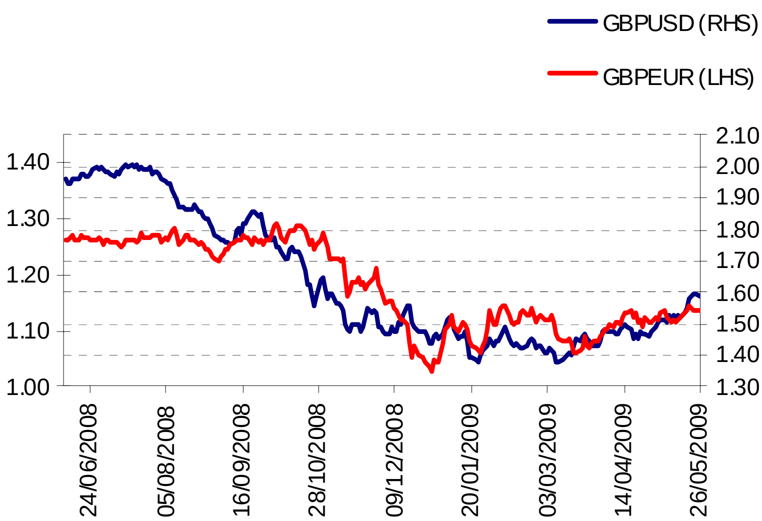
	£ Today	£ 1 week ago	€ Today	€ 1 week ago	$ Today	$ 1 week ago
OFFICIAL RATE	0.50%	0.50%	1.00%	1.00%	0.25%	0.25%
3 MONTH LIBOR	1.29%	1.36%	1.27%	1.24%	0.66%	0.83%
6 MONTH LIBOR	1.51%	1.57%	1.47%	1.45%	1.20%	1.36%
12 MONTH LIBOR	1.77%	1.84%	1.64%	1.61%	1.53%	1.66%
2 YEAR	1.84%	1.87%	1.76%	1.68%	1.26%	1.24%
3 YEAR	2.44%	2.46%	2.17%	2.06%	1.81%	1.76%
5 YEAR	3.18%	3.15%	2.80%	2.69%	2.65%	2.50%
7 YEAR	3.57%	3.48%	3.24%	3.12%	3.15%	2.95%
10 YEAR	3.90%	3.78%	3.64%	3.52%	3.57%	3.33%
20 YEAR	4.23%	4.11%	4.12%	4.02%	3.99%	3.74%
30 YEAR	4.10%	3.96%	3.99%	3.90%	4.06%	3.80%

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



Market Levels

	Today	1 week ago
GBP/USD	1.5849	1.5478
GBP/EUR	1.1369	1.1354
EUR/USD	1.3941	1.3630
GBP/JPY	150.03	148.52
FTSE 100	4336.2	4446.5
Euro Stoxx 50	2411.4	2459.6
*S&P 500	887.0	882.9
**Nikkei 225	9310.8	9290.3
Gold ($/oz)	952.0	925.1
Brent Crude ($/barrel)	58.7	57.8
Gilt Future	118.9	120.8
T-Bond	129.8	131.0
Bund	119.9	120.5



* Friday's closing rate
** Monday's closing rate

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Commentary

Economics & Interest Rates: The potential vulnerability of sovereign credit ratings was the dominant market theme last week. This followed S&P's lowering of the medium-term outlook on the UK's triple-A rating to "negative" from "stable" on Thursday. This was essentially based on the UK's poor outlook for its debt/GDP ratio, which S&P noted was potentially inconsistent with a triple-A rating. While the immediate reaction was a sharp back up in gilt yields (later reversed on a well-covered 5-year auction), it has been the US government bond market which has suffered most this past week. Specifically, financial markets have considered the possibility of ratings downgrades in other major countries laden with debt, notably the US. Indeed, US Treasuries underperformed other government bond markets last week, with yields in the 10-year to 30-year area rising by around 30bp on average.

The knock-on effect of the UK outlook downgrade was sufficient to change the usual market dynamic in times of economic uncertainty. The US S&P500 fell by 1.7% last Thursday, while Treasuries (and the US dollar) sold off. A sovereign ratings downgrade potentially raises the servicing cost of government borrowing. It may also increase the urgency for government efforts to boost the supply-side of the economy, to raise the trend GDP growth rate and put the public finances on a (sustainably) firmer footing through a wider tax base. But the latter clearly takes time to implement.

This week sees a quiet UK economic data calendar with just Nationwide house prices and May's CBI Distributive Trades Survey scheduled for release. In the US, highlights include consumer confidence today and Friday (Conference Board and Michigan), new and existing home sales along with durable goods orders and on Friday, the second estimate of Q1 US GDP. Here, the market looks a modest upward revision to -5.5% annualised from -6.1% in the advance estimate.

In the euro-zone, meanwhile, yesterday's German Ifo business climate index registered a second consecutive monthly improvement, although May's outturn of 84.2 was weaker than the 85.0 consensus. The expectations component, however, was stronger-than-anticipated at 85.9. This continues the recent trend, as the pace of de-stocking by firms starts to slow. Beyond this, April M3 money supply data are published on Friday with a further slowdown in the growth of lending to the private sector expected (from 3.2% in the year to March). May's estimate of the euro-zone CPI inflation rate is also due on Friday, with negative base effects likely to drag CPI further towards zero (consensus: +0.2%Yr).

Currencies: GBP/USD has moved towards $1.60 over the past week as the USD has faced broad based selling pressure. A rise in inflation expectations (derived from US TIPS, inflation expectations are at their highest for 8 months) alongside a risk of a US sovereign downgrade has weighed heavily on the USD.

From a technical perspective GBP/USD has become over-bought and is vulnerable to a correction lower. News of the North Korea nuclear test and weaker German data (Ifo survey) have triggered some risk aversion, leading to the USD opening stronger this week. The key US leading indicator this week is the Chicago PMI – a stronger report is required if the USD sell-off is to regain traction, otherwise the risk of a correction higher will dominate.

EUR/GBP remains range-bound despite a sharp move higher in Euro-zone/UK interest rate spreads. In the absence of major UK data this week, the currency pair should continue to find strong support around £0.8750, leaving risk/reward favouring a small move higher on the week.

Key Economic Releases This Week

Date	Time	Cntry	Release/Event	Period	Forecast	Consensus	Previous
26-May	**15.00**	**US**	**Consumer Confidence**	**May**	**41.0**	**42.0**	**39.2**
27-May	**15.00**	**US**	**Existing Home Sales**	**Apr**	**4.60mn**	**4.65mn**	**4.57mn**
28-May	**08.55**	**GER**	**Unemployment – Change (000s)**	**May**	**+60k**	**+63k**	**+58k**
28-May	**11.00**	**UK**	**CBI Distributive Trades Survey**	**May**	**-10**	**-**	**+3**
28-May	**13.30**	**US**	**Durable Goods Orders (Ex-Transpt.)**	**Apr**	**-0.3**	**-0.3**	**-0.6**
28-May	**15.00**	**US**	**New Home Sales**	**Apr**	**360k**	**364k**	**356k**
29-May	**09.00**	**EUR**	**M3 Money Supply**	**Apr**	**(4.6)**	**(4.6)**	**(5.1)**
29-May	**10.00**	**EUR**	**CPI Estimate**	**May**	**(0.2)**	**(0.2)**	**(0.6)**
29-May	**13.30**	**US**	**GDP - Annualised**	**pQ1**	**(-5.5)**	**(-5.5)**	**(-6.1)**

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

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