

U.S. Daily Directions: April 14, 2008, NY Edition

Day ahead: **Retail Sales, business inventories, Fed's Warsh.** Retail sales for Mar are expected to have remained unchanged overall but to have risen 0.2% ex-autos. Business inventories for Feb are expected to have risen 0.6% m/m. The Fed's Warsh (voter) speaks regarding the financial markets.

Overnight: **More financial losses.** US equity futures are lower on an unexpected loss reported by a major US bank and below-expectations earnings by an European electronics maker. The US\$ is mixed after the G7 meeting ended with a statement pointing out the negative economic effects of overly volatile FX markets.

Asset Commentary/Assessment:

Eurodollars: **Overnight, yields mixed.** The yield for the Apr'08 contract fell 0.25bp, those for the May-Jul'08 contracts rose 1-1.5bp, and the yields for further out contracts fell - as much as 7bp for the Sep'09 contracts. The odds of a 50bp cut on Apr30 have risen to 50%, up from 46% a week ago. The potential trough for the Fed Funds remains centered on 1.75% during H2'08. This view is less dovish than our base case of 1.50% by mid-year, but reflects our risk scenario of the Fed slowing its easing tempo during Q2.

Treasuries: **Yields lower on earnings.** Treasuries remained range-bound in Asia, but turned lower in Europe and gather steam into the US open on the poor US bank earnings report. Yields for both the 2yr and 10yr Treasuries are breaking below the uptrending support line from the mid-March lows. For the 2yr, this support was at 1.753%, while for the 10yr it was 3.458%. We stated in the weekly that the converging price action indicated the potential for a breakout in either direction, especially in light of earnings and data risk this week. Our futures team has suggested buying strangles to capture the idea that "something's gotta give".

MBS: **Friday,** MBS opened tighter this AM as an increase in servicer buying offset an increase in origination selling. However, the basis began to give up ground after the U. of Michigan Confidence survey released its lowest level since 1982. Despite a steeper curve and an uptick in vol, MBS held up fairly well in the rally with FN 5.5s keeping pace with the 10yr and widening out 3 bps vs the 5yr.

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