

U.S. Daily Directions: December 13, 2007, NY Edition

Today: **Retail sales, PPI, jobless claims, business inventories.** Retail sales for Nov are expected to have risen 0.6%/m/m, both overall and ex-autos, suggesting that they troughed in August. PPI for Nov is expected to have risen 1.5%/m/m overall (tied for the 5th highest increase since 1980) and an above-average 0.2% ex-F&E. Jobless claims (w/e Dec 8) are expected to have remained at a benign 335K. Business inventories for Oct are expected to have risen 0.3%, maintaining a moderating trend since mid-year.

Overnight: **Market stable, but not fixed.** Despite yesterday's liquidity announcement, LIBOR rates remain high. 3-mo euro LIBOR fixed at 4.95%, a high since Dec'00. The US 3-mo LIBOR fixed lower at 4.99%, but its spread over the Fed Funds rate remains extremely elevated at 74bp. S&P futures are down 8.8pt to 1480.60. Treasuries are up slightly 0.5-1.7bp along the curve. The fundamental headlines in the developed world remain ugly. A UK housing survey showed the worst sentiment among real estate professionals since 1998. HBOS, a UK mortgage lender, wrote down earnings \$368mm. Canada's CIBC is facing increasing market suspicion that it is highly vulnerable to the credit rating of a shaky US financial guarantor.

Asset Commentary/Assessment:

Eurodollars: **Not much confidence in liquidity provisions,** the Dec'07 and early-'08 contract yields collapsed on the news of the liquidity provision but then traded partially rebounded as the market reconsidered the massive issues confronting the financial system. The strip suggests a trough in the Fed Funds rate below 3.50% by Dec'08 – Mar'09.

Treasuries: **Yields choppy.** Yields chopped overnight but are headed lower as US accounts start their day. Our trading desk expects solid participation in today's 10yr re-opening to cap the yield at 4.125%. Our 2s30s position slipped another 0.9bp to 142bp (target 175bp, trailing stop 132bp, entry 121bp).

Swaps: **Spreads mixed.** The 2yr tightened 2.1bp overnight, but at 90.75, remains above the Aug/Sep peak. The 10yr tightened 0.2bp to 69.38bp, around the middle of the range since October.

MBS: **Yesterday, whipsaw.** Information the previous evening that the FED failed to disclose liquidity plans during Tuesday's trading hours, brought spreads back to their pre-fed tights. The MBS market opened very volatile as the street digested the news regarding the new liquidity facility plan by the FED. One thing was certain was spreads would get a boost from the added liquidity and MBS was off to the races. Asia came in a buyer on the lows in dollars and mortgages tightened anywhere from 15/32nd to 9/32nds (5.5's and 6's) tighter to the treasury curve from Tuesday's end of day wides. By the end of the afternoon mortgage prices became sticky and were widening and tightening on rallies and sell-offs in the treasury market. The mortgages current coupon closed the session ~7bps tighter to treasuries and ~1.5bps tighter to the swap curve. We continue to favor up in coupon, gold/fns and 10/20 IOs, but are going to stay neutral on the basis as volatility is tremendous.