10/30/2007 5:45

The Morning Email: Treasuries

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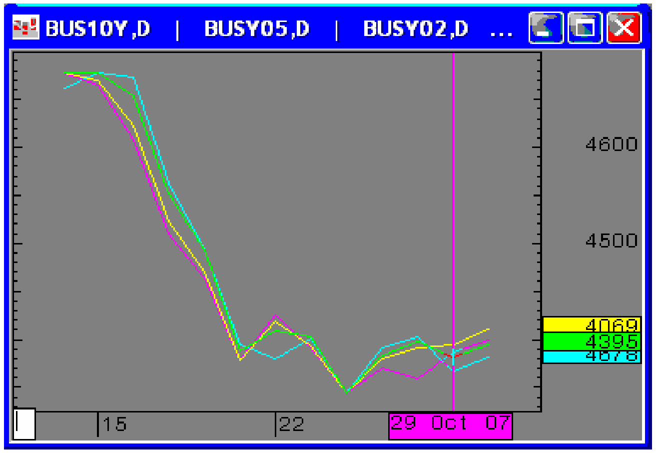
Daily Yield Curve



Source: CQG, Inc. © 2007 Tue Oct 30 2007 05:34:43

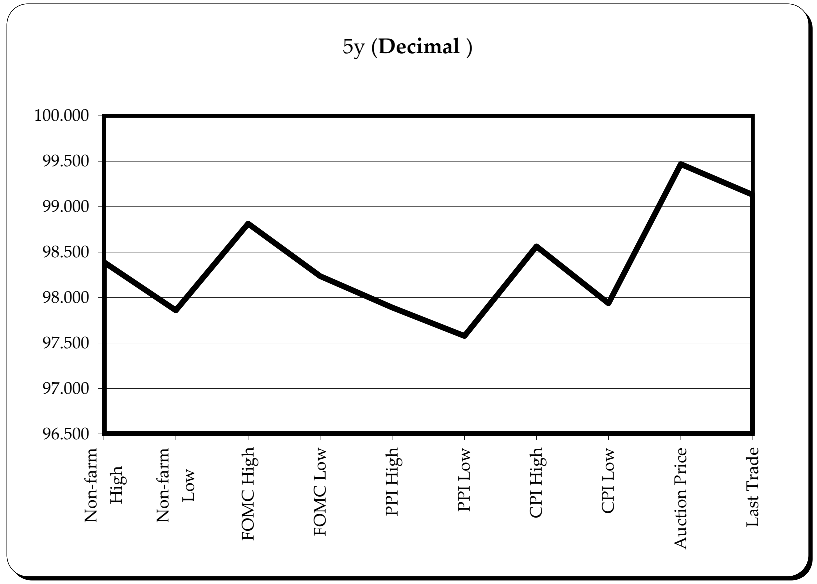
30y **10y** **5y** **2y**

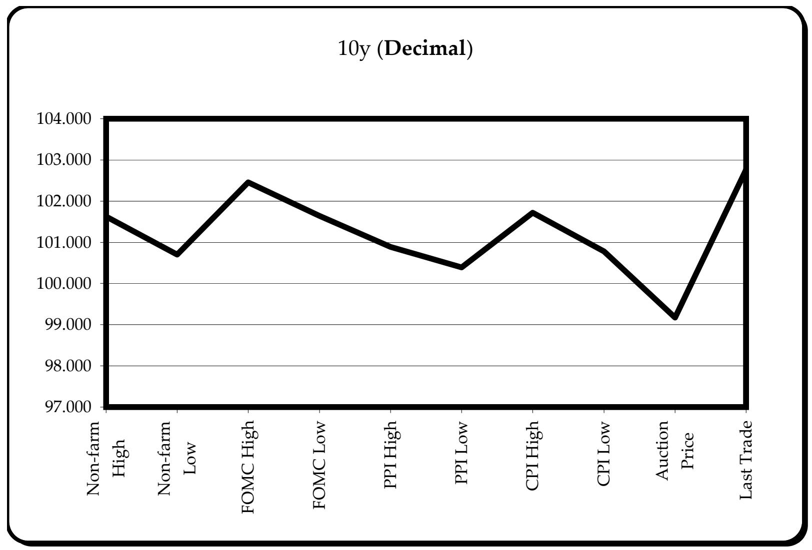
Want something added? Let me know: jgoulding@ghco.com

Important Econ Releases, Highs & Lows

Economic Releases - 32nds	5y	10y	ZNZ7	ZBZ7	Date
Non-farm High	98.1250	101.200	109.160	111.30	10/5/2007
Non-farm Low	97.2750	100.225	108.210	110.15	10/5/2007
FOMC High	98.2600	102.145	110.300	112.30	9/18/2007
FOMC Low	98.0750	101.205	109.115	111.27	9/18/2007
PPI High	97.2850	100.285	108.260	110.31	10/12/2007
PPI Low	97.1850	100.125	108.120	110.05	10/12/2007
CPI High	98.1800	101.230	109.220	111.27	10/17/2007
CPI Low	97.3000	100.250	108.260	110.15	10/17/2007
Auction Price	99.1504	99.056			
Last Trade	99.0420	102.245	110.175	113.15	10/30/2007 5:45

Auctions - 32nds	2 y	5y	10y	30y
Auction Price	99.260	99.150	99.056	99.026
Auction Yield Stop	3.723	3.993	4.855	5.059
Actual Auction Date	10/24/2007	10/25/2007	8/8/2007	8/9/2007



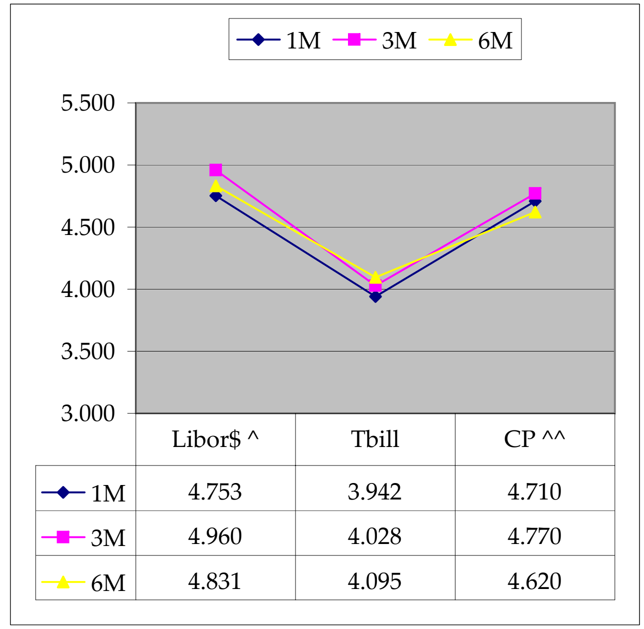


Notes: Cash and futures are adjusted for roll.
Release times are from release to 2pm cdt
(Sep07 to Dec07 Futures roll: ZF = +3; ZN = +9.5; ZB = +5 (tics))
r = reopen

			32 nds				
	Last	Net	High	Low	Open	Volume	SYM NAME
TUAZ7	103.240	(0.0)	103.255	103.232	103.252	18,239	2y Fut
FVAZ7	107.235	(0.0)	107.270	107.225	107.265	34,624	5y Fut
TYAZ7	110.175	(0.0)	110.220	110.165	110.205	61,083	10y Fut
USAZ7	113.150	(0)	113.220	113.140	113.210	12,931	30y Fut
	Last	Net	High	Low	Open	Volume	SYM NAME
BUS02P	99.200	(1.5)	99.212	99.195	99.212	na	2y Cash
BUS05P	99.040	(3.0)	99.065	99.037	99.065	na	5y Cash
BUS10P	102.240	(4.0)	102.290	102.240	102.285	na	10y Cash
BUS30P	105.035	(5)	105.105	105.035	105.095	na	30y Cash
	Last	Net	High	Low	Open	Volume	SYM NAME
BUS02Y	3.818	2.00	3.839	3.785	3.818	na	2y Yield
BUS05Y	4.067	1.90	4.074	4.043	4.06	na	5y Yield
BUS10Y	4.397	1.60	4.404	4.377	4.387	na	10y Yield
BUS30Y	4.677	1.10	4.683	4.658	4.668	na	30y Yield

	Libor$ ^	Tbill	CP ^^
1M	4.753	3.942	4.710
3M	4.960	4.028	4.770
6M	4.831	4.095	4.620
	TSY	Swap	ED Pks ^^^
2y	3.822	64.00	4.397
5y	4.070	65.25	
10y	4.396	62.75	5.301

	Libor$ ^	Repos
0/N	4.808	4.700
1week	4.779	4.550
2week	4.770	4.500



Notes

^Quoted in US Dollars

^^CP = Commercial Paper

^^^ED Pks are colored for pack identifications. Example, the red pack is a 2-yr proxy and is colored red.

Lastly, SYM = Symbol

All times Eastern

15:28 10/29 **US TSYS/RECAP**: US Tsys prices end Mon mixed (10Y, 30Y higher on day, rest lower) amid 1) stocks moved off high earlier but caught late bid, so Tsys gyrate w/ stocks; 2) Tsys bargain-hunting on-and-off; 3) safe-haven bid in T-bills; 4) Street selling in high-grade ABXs; 5) smallish RMBS, ABS bid lists from various types; 6) leveraged accounts, financial institutions, foreign accts sold Tsys intermediates;7)Bargain-hunting in 2Ys near 3.825% in morning, leveraged accts buy 2Ys also; 8) some did 5Y/10Y steepeners or 10Y/30Y flatteners. 9) Corporate rate-lock unwinds. 10) Tsys morning cut losses as US stocks gave up some gains; German Bunds also crept higher amid muted action. 11) Mixed data: weaker Dallas Fed Oct manufacturing index at -6.6 vs. Sept. -4.6) but Oct Mfrg prices paid leapt to 33.6 vs. 17.9 Sept. 12) There was a servicer who had bought up to 25K Mar 10Y 112 calls bought on the day at a 5.64% vol vs. 5.56% settlemt on Fri. 13) Long-end UK Gilt buying as MNI said UK DMO Chief said Gilt issuance likely to fall in FY2008/2009.

15:07 10/29 **US EURODLR FUTURES:** Eurodlr futures finished session lower, near middle of the range while the curve back some of last week's steepneing, the Red/Gold pack spd was 6.25 bps flatter at 89.0 by the bell. In the Fronts (Dec07-Sep08), the Dec07 was in 3.5 bps at 95-32 on combined Globex and pit volume of 163,000, the Mar08 in 3.5 bps at 95-64 on volume of 163,000, the Jun08 in 3.5 at 95-77 on volume of 157,000, while the Sep08 contract was 3.5 bps lower at 95-85 on volume of 152,000. The 2yr proxy Red pack (Dec08-Sep09), settled 3.0 to 3.5 bps lower across the pack with 370,000 contracts traded.

15:07 10/29 **US SWAPS**: Spds ended the session tighter, the 2s/10s spd of spds moving steady to Fri's lvl as long end improved in second half. On heels of decent Asian account receiver-tied support overnight, volume remained tepid at midmorning Monday, with light two- way moves on curve and spread in the fronts to intermediates as accounts positioned for Wednesday's Fed announcement. Spds moved off tights by midsession as Tsy recovered form early lows. According to GovPX:

Time (ET)	2Y Swap/Mid	5Y Swap/Mid	10Y Swap/Mid	30Y Swap/Mid
Mon 3:00	-1.50/64.50	-1.00/65.25	-1.25/62.75	-1.25/59.00
12:45	-1.25/64.75	-0.75/65.50	-0.75/63.25	-0.75/59.50
10:35	-2.00/64.00	-1.50/64.75	-1.00/63.00	-1.00/59.25
9:20	-2.00/64.00	-1.00/65.25	-0.25/63.75	+0.25/60.75
Mon Open	-2.00/64.00	-1.00/65.25	-0.25/63.75	+0.25/60.75
Mon 7:50	-1.75/64.25	-0.25/66.00	+0.00/64.00	+0.25/60.75
Fri 3:00	+0.75/66.00	+1.25/66.25	+1.75/64.00	+2.00/60.50

(cont)

15:15 10/29 **CLOCKS:** For planning purposes, just a reminder that clocks in the U.S. will fall back one hour this coming weekend as Daylight Savings Time ends, restoring time differentials to "normal" with the UK, Europe and the Pacific Rim.

06:16 10/30 **TSYS:** Treasuries are trading modestly lower across the board in London Tuesday, with the curve flattening slightly as the longer-end of the curve outperforms modestly. However, with the Fed beginning a two-day rate setting meeting later today, volumes are light. The market is expecting the Federal Reserve to cut the Fed funds rate by 25bps to 4.50%, amid return of credit crunch jitters. Prices were lower from the getgo in Tokyo, but there was little to attract traders attention. Trader inaction remained into the London session, with the light flows seen as largely interdealer book squaring. The Bund/T-note spread was standing unchanged on Monday's levels, standing at 26 bps. Ahead of the U.S. session, the 2-yr note was trading 1/32 lower at 99 20/32 to yield 3.81%. The 10-yr note was 2/32 lower at 102 26/32 (4.39%), with the Bond 4/32 lower at 105 7/32 (4.67%). The 2-yr/5-yr yield curve was unchanged on Monday's levels, trading at +25 bps, while the 2-yr/30-yr curve was 1 bps flatter, standing at +86 bps.

News: Snapshots throughout the day

MarketNews international

Stone & McCarthy RESEARCH ASSOCIATES

10:06 10/29 **US CMBS**: A string of negative news items, including losses by financial guarantors and Merrill's whopping write-down weight heavily on the CMBS market. Starting off last week on a somewhat more positive tone, by the end of the week, CMBS spreads were 1-25 bpts. wider over the last 5 trading days. In addition to a sell off in the cash market, CMBC indexes were also lower across the board. Further, the funding advantage increased even further for the receiving leg on CMBS swap trades - all further adding pressure on the cash market. According to CMBS strategists at JP Morgan, "We will remain in an environment of heightened spread volatility through at least year end, as each new piece of negative news is met with a disproportionately larger widening than any lack of bad news is greeted with tightening. Given this expectation, we remain underweight CMBS spreads across the capital structure." JP also adds that further declines in the ABX as well as the fear of fire sales in AAA ABS and CDO paper by SIVs, should result in wider cash CMBS spreads.

11:31 10/29 **GLOBAL EARNINGS:** Market sources following earnings season closely and the next two weeks are highlighted by large European names. BAS strategists the recent widening in credit spreads of European financials has been led by some of the largest banks in Europe - UBS, DB and CS - and the scale of the widening has been "unprecedented." BAS says, "given the sheer volume of risk reduction that is implied in the sector, we would expect a relief rally" via spread tightening if no negative surprises come through this week.
Some highlighted dates and names for
Q3 earnings are:
Oct 30 UBS
Oct 31 Deutsche Bank, Generali (Italian Reinsurance Co)
Nov 01 Credit Suisse, ABN Amro
Nov 07 ING, Societe Genrale, Commerzbank. US AIG also out this day
Nov 08 BNP Paribas, Fortis

13:00 10/29 **US OUTLOOK**: Analyst Richard Berner at Morgan Stanley & Co. says "builders may have to slash up to another 40% from 1-family housing starts to balance supply with demand. And real home prices likely will have to decline by 10% to make housing more affordable and boost demand. Neither such a construction decline nor its potential effect on economic activity seems to be in any forecast."

10:52 10/29 **US BONDS**: Bond strategists at Deutsche Bank say 3 factors have been driving the yield curve - risk premia, liquidity and the economy. DB says the importance of the economy has risen even as the liquidity factor has stabilized. But DB is looking for more steepening as the data starts showing the economy is heading into recession and regardless of what action the Fed takes this Wed at its meeting. Commenting on the risk factor, DB says risk premia and the repricing and transfer of assets has been an ongoing factor causing curve steepening since Q3 2006. "The unwind of the conundrum that had caused the unusual flatness of the curve since 2004 has been driven by the reduction in bank demand for mortgages, the reduced growth in overseas demand for dollar assets, and the pressures of mortgage supply have all led to curve steepening," DB says in its weekly piece. "Recently, the subprime crisis and the need to reprice risk assets as they are transferred out of low-capitalized structures such as SIVs and into stronger hands has also boosted the risk premium."

US TSYS: According to Lehman Bros, **the month-end extensions for Nov 1** are:
U.S. Treasury extension at 0.04 years
U.S. Aggregate at 0.05 years
Euro Treasury at 0.11 years
Sterling Gilts at 0.04 years

Duration, DV01s, Curve Spreads, CF

	M Duration	DV01 32	DV01 $	DV01 Box	CF
30y	15.62	5.31	$1,658	10.61	n/a
10y	7.73	2.57	$802	5.13	n/a
5y	4.50	1.43	$446	5.71	n/a
2y	1.92	0.62	$194	2.48	n/a
ZB	9.88	3.64	$114	3.64	1.1103
ZN	5.80	2.07	$65	4.14	0.9069
ZF	3.87	1.35	$42	2.69	0.9119
ZT	1.82	0.61	$19	2.43	0.9593

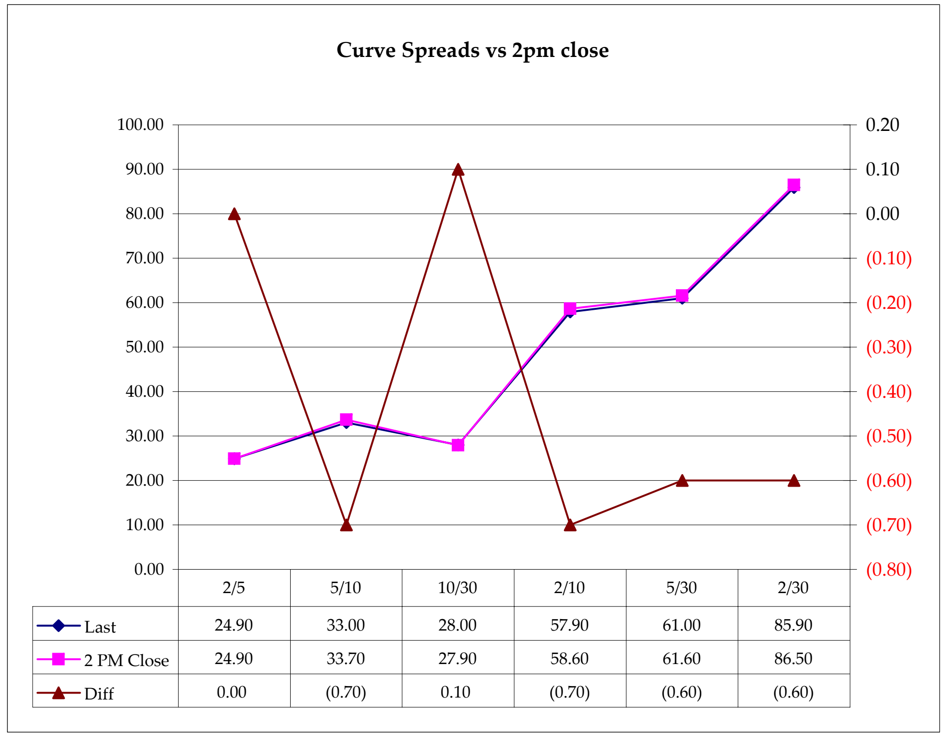
Yield Curve Spreads

	Last	2pm close	Diff
2/5	24.90	24.90	0.00
5/10	33.00	33.70	(0.70)
10/30	28.00	27.90	0.10
2/10	57.90	58.60	(0.70)
5/30	61.00	61.60	(0.60)
2/30	85.90	86.50	(0.60)

DV01 32, said differently, is "how many TICS is in a basis point?".

Example, If **ZN** moves 1~basis point, then, it's moved 2.08 tics (Today, 10/25/07, the value in the box is 2.08).

Since ZN trades in half tics, then, 4.17 boxes = 1 basis point in ZN. (Again, today, 10/25/07, the value in the box is 4.17). Of course the values will be different as you look at this. But, they won't be that much different. So, I think you can get the idea I'm trying to get across.



Notes

CF = Conversion Factor

MDuration = Modified Macaulay Duration

MDuration & DV01s for Futures are based on proxy issue (CTD)

DV01 Box = Dollar Value of 1 basis point move per Box

Hedge Ratio's

US Financial Futures / Eurex Bond

	ZB	ZN	ZF	ZT
Bund (Z)	1.000	1.700	2.700	3.000
Bobl (Z)	0.550	0.970	1.450	1.570
Shatz (Z)	0.230	0.400	0.620	0.680

US Financial Futures

	ZB	ZN	ZF	ZT
ZB		1.758	2.702	5.995
ZN	0.000		1.537	3.411
ZF	0.370	0.651		2.219
ZT	0.167	0.293	0.451	

Eurex Bonds

	Bund (Z)	Bobl (Z)	Shatz (Z)
Bund (Z)	1.0	1.7	4.0
Bobl (Z)	0.6	1.0	2.4
Shatz (Z)	0.2	0.4	1.0

US Treasuries v US Financial Futures

	2y	5y	10y	30y
ZB	1.70	3.92	7.05	14.58
ZN	3.00	6.90	12.39	25.63
ZF	4.61	10.60	19.05	39.40
ZT	5.11	11.76	21.13	43.71

US Treasuries v Eurex Bonds

	2y	5y	10y	30y
Bund (Z)	1.7	3.9	7.1	14.3
Bobl (Z)	3.1	7.1	12.8	25.8
Shatz (Z)	7.8	15.9	28.8	58.1

US Treasuries

	2y	5y	10y	30y
2y		2.301	4.135	8.553
5y	0.435		1.797	3.717
10y	0.242	0.556		2.068
30y	0.117	0.269	0.483	

Note: Any ratio with the Bund, Bobl, or Shatz is from Bloomberg. So, the Bloomberg hedge ratios, in this spreadsheet, are static. Meaning, I only update them once in a while but always on rolls. My hedge ratio's are live, meaning, they're updated in real-time.

Commitment of Traders (COT)

	Current Positions									
	Small Spec			Large Spec			Commercials (Hedgers)			
	Long	Short	Net	Long	Short	Net	Long	Short	Net	
ZF	256,768	226,115	30,653	408,281	257,493	150,788	1,113,600	1,295,041	(181,441)	**ZF**
ZN	366,688	460,597	(93,909)	707,391	299,537	407,854	1,813,525	2,127,470	(313,945)	**ZN**
ZB	158,351	174,964	(16,613)	137,040	157,487	(20,447)	723,267	686,207	37,060	**ZB**

	WoW^ Position Change			
	Sml Spec	Lrg Spec	Comm	
	Net	Net	Net	As of
ZF	**19,688**	**(46,434)**	**26,745**	**10/9/2007**
ZN	**20,311**	**56,768**	**(77,079)**	
ZB	**10,245**	**25,007**	**(35,253)**	

^WoW = Week over week

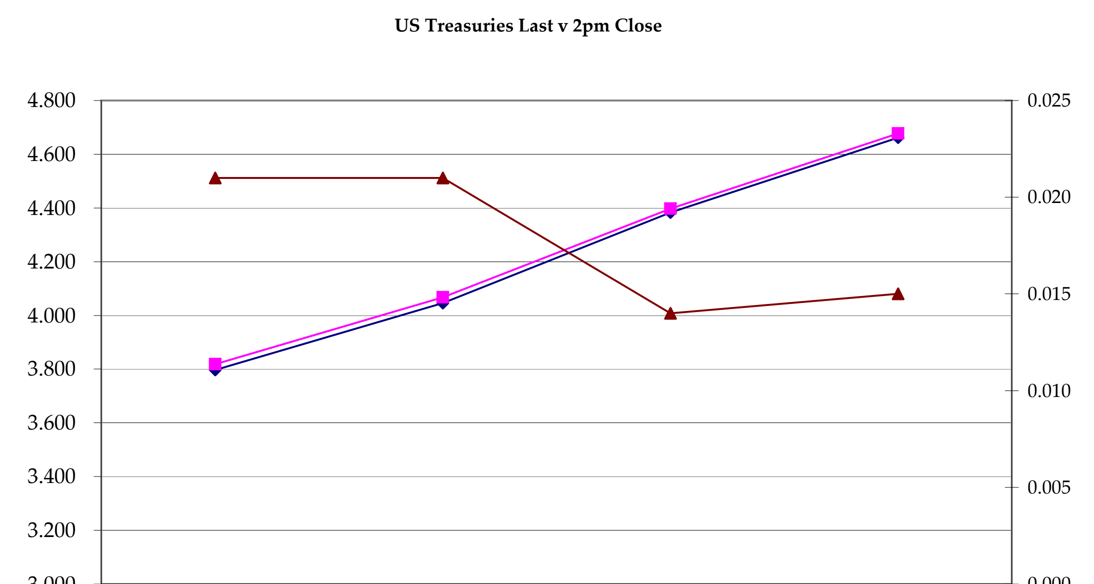
Closes: 2pm CST vs this Morning

	Cpn	Mty	Close 32	Close	Last	Diff	Basis Close	Basis Last	Roll
2y	3.625	10/31/09	99.2150	3.797	3.818	0.021			
5y	3.875	10/30/12	99.0750	4.046	4.067	0.021	28.99	28.42	
10y	4.750	8/15/17	102.285	4.383	4.397	0.014	81.17	80.34	
30y	5.000	5/15/37	105.13	4.662	4.677	0.015	-665.66	-667.00	

	Close 32	Last
ZFZ7	107.265	107.235
ZNZ7	110.210	110.175
ZBZ7	113.21	113.150

Curve Spreads

	Close bps	Last bps
2/5	24.9	24.9
5/10	33.7	33.0
10/30	27.9	28.0
2/10	58.6	57.9
5/30	61.6	61.0
2/30	86.5	85.9



	2y	5y	10y	30y
2pm Cls	3.797	4.046	4.383	4.662
Last	3.818	4.067	4.397	4.677
Diff	0.021	0.021	0.014	0.015

Notes:
Basis = (Cash Decimal - (Futures Decimal * CF))*32
MDuration for Curve Spreads:
Longer duration minus shorter duration
32 = price is quoted in 32nds

Cash Duration Matrix

Cash Duration Matrix				
	2	5	10	30
2	**100%**			
5	43%	~~**100%**~~		
10	25%	58%	**100%**	
30	12%	29%	49%	**133%**

What is this? (1):
2yr cash has X% duration of 5yr cash .

Cash Matrix [DV01 x Duration]				
	2	5	10	30
2	**$194**			
5	$190	~~**$446**~~		
10	$199	$467	**$802**	
30	$204	$478	$821	**$1,658**

What is this? (2):
-2yr cash has DV01 of $202
-Multiply the 2yr DV01 by the percent duration to come up with what the 2yrs DV01 SHOULD be compared to the 5yr.

Cash Matrix [DV01 over / (under) valued]				
	2	5	10	30
2				
5	$4			
10	($5)	($21)		
30	($10)	($32)	($19)	

Cash Matrix [DV01 over / (under) as %]				
	2	5	10	30
2				
5	1.89%			
10	-2.64%	-4.45%		
30	-4.87%	-6.63%	-2.29%	

What is this? (3):
-Now you can see the over/under value, based on the DV01, from contract to contract. In this example we are looking at the 2yr compared to the 5yr.

Or you can look at the over/under value as a percentage instead of dollar terms.

Tic for Tic & Box for Box Matrix

Tic for Tic Matrix

	2y	5y	10y	30y
ZT	1.02	2.35	4.23	8.74
ZF	0.46	1.06	1.90	3.94
ZN	0.30	0.69	1.24	2.56
ZB	0.17	0.39	0.71	1.46

	2y	5y	10y	30y
2y	1.00	2.30	4.14	8.55
5y	0.43	1.00	1.80	3.72
10y	0.24	0.56	1.00	2.07
30y	0.12	0.27	0.48	1.00

	ZT	ZF	ZN	ZB
ZT	1.00	2.22	3.41	6.00
ZF	0.45	1.00	1.54	2.70
ZN	0.29	0.65	1.00	1.76
ZB	0.17	0.37	0.57	1.00

Box for Box Matrix

	2y	5y	10y	30y
ZT	1.02	2.35	8.45	17.48
ZF	0.46	2.12	3.81	7.88
ZN	0.60	1.38	1.24	2.56
ZB	0.68	1.57	1.41	2.92

	2y	5y	10y	30y
2y		2.30	2.07	4.28
5y	0.43		0.45	1.86
10y	0.48	2.23		2.07
30y	0.23	0.54	0.48	

	2y	5y	10y	30y
ZT		2.22	6.82	23.98
ZF	0.45		1.54	5.40
ZN	0.15	0.65		3.52
ZB	0.04	0.19	0.28	

Fed Funds Probability of Tightening or Easing

October	avg target	400	425	450	475	500
10/26/2007	4.5%	0.6%	19.6%	68.7%	10.8%	0.0%
10/29/2007	4.5%	1.9%	10.7%	72.6%	14.5%	0.0%

December	avg target	375	400	425	450	475	500	525
10/26/2007	4.3%	0.0%	20.0%	47.3%	30.7%	1.7%	0.3%	0.0%
10/29/2007	4.3%	0.0%	13.9%	41.3%	44.6%	0.0%	0.0%	0.2%

These probabilities take options into account and are much better at forecasting the FOMC intentions than the 'day-count' equation most analysts on the street use.

Notes:
All probabilities are taken from The Cleveland Federal Reserve

Valuing the Basis

This page is based on the work of Galen Burghardt.

	Basis		Delivery Basket			Futures Price	
	Bullish	**Bearish**	**DC^**	**HDB**	**LDB**	**Up**	**Down**
Repo in GC		x					
Repo on Special	x		Steepen				
Repo Rate Down	x						x
Repo Rate Up		x				x	
Fed buys back issue	x		Flatten	Deliver	Deliver		
Fed stops selling issue	x		Flatten	Deliver	Deliver		
Volitility Up (in general)	x						x
Volitility Down (in general)		x				x	
Volatility Up, PS		x				x	
Volatility Down, NPS	x						x
Volatility Down, PS		x				x	
Volatility Up, NPS	x						x
Fed Raising Rates			Flattens	Deliver	Deliver		
Cost-to-Carry up		x					
Cost-to-Carry down	x						
Market Rallying	x						
Market Breaking		x					
BNOC is Negative		x					
BNOC is Positive	x						
Curve Steepening (in general)	x						
Curve Flattening (in general)		x					
Curve Parallel (in general)		x					

<u>What affects the basis?</u>
changes in rp rates
changes in the slope of the yc and dc
changes in yield spreads
changes in yield volatility
carry convergence

Please see the morning email "US Deliverable Basket" for charts of the Deliverables.

If you're long the basis and the markets going up but the basis is barely going up, then check to see if there's a parallel shift going on in the curve.

Long basis and a parallel shift lowers the value of being long the basis. You won't make as much as you thought. You might even lose

<u>Notes:</u>

^ DC = Delivery Curve. See morning email, US Deliverable Basket for full basket.
PS = Parallel Shift
NPS = Non-Parallel Shift.
BNOC = Basis Net of Change

yc = yield curve
HDB = High Duration Bond/Note
LDB = Low Duration Bond/Note