MF Global | Strategy

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26/02/10 INSTITUTIONAL USE ONLY March 2010

MONTHLY GLOBAL MARKETS MONITOR

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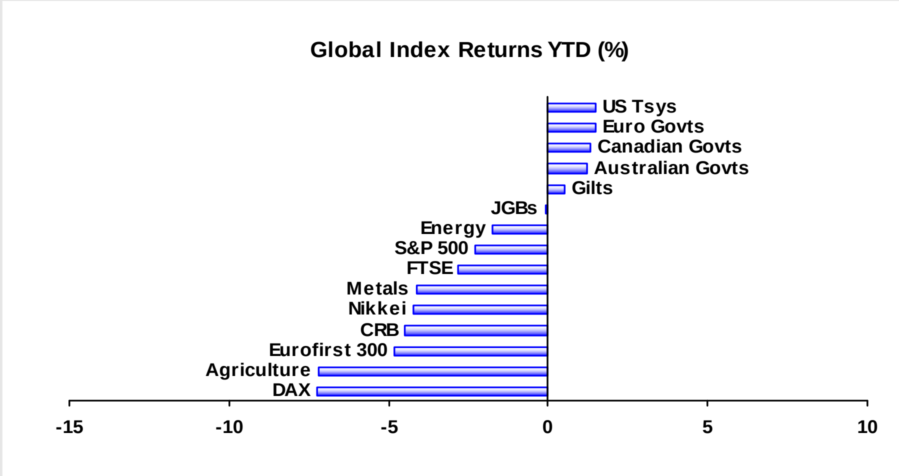

Source: Bloomberg and MF Global UK Limited

CONTENTS

Page

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INTEREST RATE PRODUCTS

Overview | 26-Feb-10

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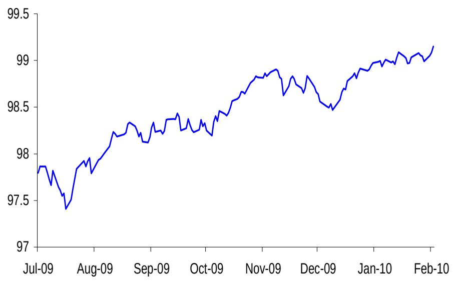
A slow unwinding

FED IN NO RUSH BUT LABOUR MARKET KEY

Despite the earlier than expected tweaking of the Discount Rate, the Fed appears to be in no rush to make an early move in funds rates and interest on excess reserve balances. The health of the recovery will be key to determining the latter, particularly the trends in the labour market.

Although the overall level of employment remains low, the latest decline in the unemployment rate is significant and, if sustained in the coming months, could prove to be a key turning point. The near 6% growth in Q4 annualised GDP and a buoyant manufacturing ISM report are other strong signals that the recovery is well underway. Even some of the weaker numbers, such as non-manufacturing ISM, have shown relative improvement and some encouraging signs within the detail. Developments such as these increase the risk that at one of the next few meetings Fed officials drop the "extended period" language when referring to the duration for keeping rates low, although any tightening could still be quite some time away. We have already seen the Fed's Hoenig, dissenting against the expectation of low rates for an extended period at the last meeting, but not against the actual funds rate decision; hikes may be some way off for now, but they are gradually drawing closer, with the consensus centering on Q3 of this year.

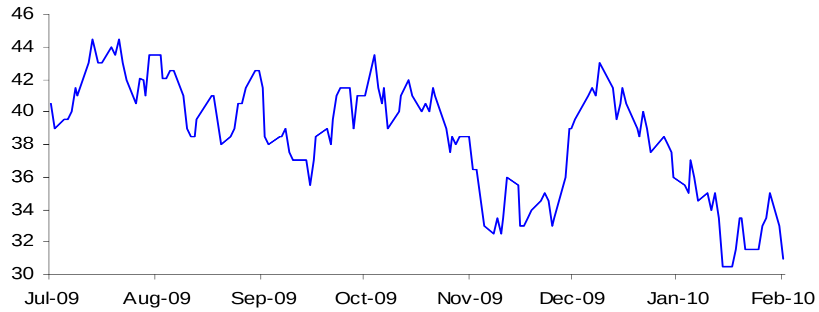
EDZ0



Source: MF Global UK Limited and Bloomberg

Against this backdrop it is difficult to see a differential such as the EDU0/Z0 spread, for example, dropping below 30bp for a sustained period and risks appears skewed to the upside in a zero funds rate regime. Our target is around 40bp with a stop at 26bp (see Trade Alert 10/2/2010 for original recommendation).

EDU0/Z0 SPREAD (BP)



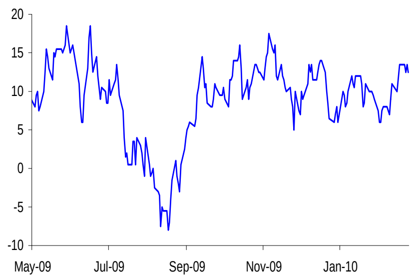
Source: MF Global UK Limited and Bloomberg

Canadian strip too steep

STEEPENING OF THE CANADIAN STRIP OVERDONE

On a related note, we think that the Canadian interest rate strip is looking too steep once more relative to its US counterpart. In particular, the BA/ED M0/U0 box trade (BA flattener, ED steepener) is back to close to the top of its trading range at around 13bp (see chart overleaf). Investors should look to enter this trade close to current levels – ideally scaling in between 13bp and 15bp - and target a return towards parity with a stop at 20bp. Roll is positive; the negative roll on the ED steepener is more than offset by the positive roll on the BA flattener; the BA/ED H0/M0 box is currently trading near to zero.

BA/ED M0/U0 BOX (BP)



Source: MF Global UK Limited and Bloomberg

The BA curve has been steepening as the domestic data has been picking up. Consumer prices rose 1.9% yoy in January, the most since late 2008, while the core rate rose 2% yoy and consumer confidence also jumped to a 23 month high in the same month. The latter partly reflected an improvement in labour market conditions, with the unemployment rate edging down to 8.3% in January from 8.4% in December. Meanwhile, low rates and a greater willingness among Canadian banks to extend new loans have helped to drive a resurgence in the housing market.

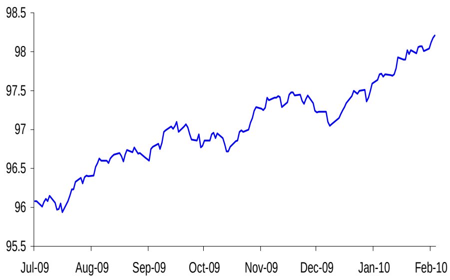
Nevertheless, while GDP grew by 0.4% last November, the Q4 figures are unlikely to reach the near 6% annualized pace seen in the US. At the same time, with the Canadian dollar approaching parity against the dollar, anxiety will remain about the fall out from the buoyant currency on exports. The latter will make the BoC more cautious about tightening policy, especially as the FX move will help to keep a lid on inflation expectations and the central bank has already pledged to leave borrowing costs at 0.25% through June of this year as long as the inflation outlook doesn't shift materially. Indeed, despite edging lower, still high unemployment should also ensure price pressures are contained this year and rates are likely to stay on hold for quite some time yet (see Trade Alert 22/2/2010 for original recommendation).

THE PROSPECT OF MORE UK QE STILL BUBBLING

Short Sterling – ever higher

With the Inflation Report and the minutes of February's MPC meeting suggesting that the pause in the QE programme may only be temporary, there still appears to be a good chance that the Committee may have to give even more support to the UK economy if the recovery disappoints. The latest UK data continues to suggest that the fundamental picture is still weak – inflation pressures are only being temporarily distorted higher by energy base effects - and the prospect of a major fiscal tightening continues to overhang the economy.

L M1

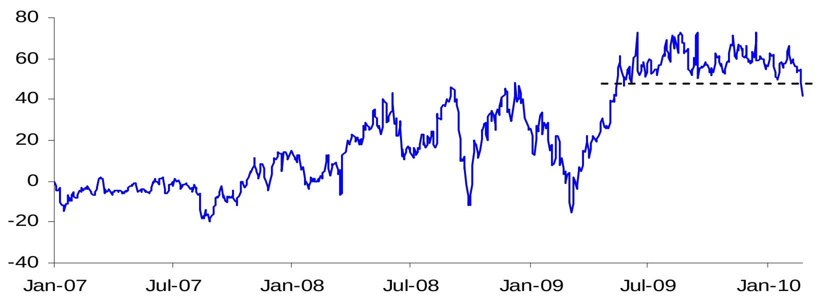


Source: MF Global UK Limited and Bloomberg

Therefore, we are still sticking with the mid-April 0LJ1 98.25/50 call spread (recommended at 6 now 11) and the mid-April 98.375/625 call spread (recommended at 4 and now 7.5), both flagged early in February (see Trade Alert 5/2/2010 for original recommendations) with L M1 having already rallied around 30 ticks to about 98.20 in the intervening period.

We also think that red/green sterling spreads look too high relative to both comparable spreads in euribor and white/red sterling spreads and suggest that investors should consider entering the red/green H1/H2 short sterling/euribor box (sterling flattener, euribor steepener). The rolling generic chart below shows that, at present levels of now under 45bp, this could be starting to make a break much lower. We would initially target a move to back towards its average value of the last 3 years or so of 20bp, but it has the potential to go further, with a stop around 55bp. Roll is negligible (see Trade Alert 25/2/2010 for original recommendation).

GENERIC RED/GREEN L/ER 5/9 BOX (BP): L 5/9-ER5/9 (CURRENTLY L H1/H2-ERH1/H2)



Source: MF Global UK Limited and Bloomberg

INTEREST RATE PRODUCTS

European Volatility | 26-Feb-10

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Euribor Options

A NORMALIZATION OF RISK APPETITE

Euribor implied volatility has fallen to new lows recently, partly as a result of the sustained rally in the underlying but also reflecting the normalization of risk appetite. Paper flows still target 9937 on the upside with continued buying of butterflies and condors in June and September. On the downside we have seen 1x2 put spreads bought aggressively resulting in a weaker put skew and pressure on at-the-money vol.

	Straddle Price	Implied Vol	One day S.D.	50 day Hist Vol
Jun 9925	14	41.75%	2.05 bps	35.00%
Sep 9900	27	46.60%	2.80 bps	35.95%
Dec 9887	41	51.35%	3.70 bps	36.60%

Source: MF Global UK Limited

Short Sterling Options

RATES LOW FOR LONG PERCEPTION STRENGTHENS

The dire economic news and statistics published recently has only added to the perception that rates will remain on hold for a considerable period. As most trade in sterling options has historically occurred in the front months the result has been a temporary dearth of activity. What little trade we have seen has been to the upside, but is dwarfed by the volumes seen in Euribor. Sterling implied volatility has softened recently, but is still stubbornly higher than Euribor.

	Straddle Price	Implied Vol	One day S.D.	50 day Hist Vol
Jun 9925	16	49.05%	2.25 bps	51.85%
Sep 9912	32	62.35%	3.43 bps	55.30%
Dec 9887	50	63.41%	4.45 bps	51.15%

Source: MF Global UK Limited

European Bond Options

SCHATZ ACTIVITY BECOMING MORE BALANCED

Concerns over Greece drove volatility sharply higher at the beginning of the month, with Bund reaching the 5.85-5.90 area for the front month. This vol sentiment was tempered somewhat by a US 10 yr led sell off and the re-emergence of the recent Bobl call spread seller who has shifted attention to the April contract selling 80k 115.75/116.25 call spreads. Put/call skews have returned to more reasonable levels from the extremes we have recently witnessed and as a result, skew plays have been fairly muted. Schatz has still enjoyed a healthy level of activity but with a more balanced directional bias than seen in last month's report.

	Straddle Price	Implied Vol	One day S.D.	50 day Hist. Vol
Apr Bund	159	5.29%	41.0 bps	4.42%
Apr Bobl	93	3.26%	24.1 bps	2.74%
Apr Schatz	35	1.32%	9.1 bps	0.96%

Source: MF Global UK Limited

INTEREST RATE PRODUCTS

US Volatility | 26-Feb-10

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Eurodollar Options

VOLATILITY EASING

After a period of indecision, dollars have squeezed higher, with the inevitable monetary tightening being pushed further into the future. The two standout trades have been the accumulation of a 100k plus position in the Dec10 9800/9700 ps and the purchase of over 50k Sht Dec 90 c @ 2 & 2.5. As would be expected, volatility has eased on the recent rally – bpd values are shown below.

	26/01	25/02
EDH0	1.2	0.5
EDM0	2.5	2.0
EDU0	4.7	3.6
EDZ0	6.3	5.3
EDH1	7.3	6.5

Source: MF Global UK Limited

Bond Options

BONDS STILL RANGE BOUND

With the earlier sell-off being reversed in recent sessions, the bond market still looks range bound. This has been underlined by papers selling of strangles in 10yr, with the 114/119 being the favourite. April has traded 14, May 34 & June from 111 to 60 over the last few days. Volatility has suffered as a consequence.

	26/01	24/02
USJ0	11.08% (7.7 bpd)	9.26% (6.4 bpd)
TYJ0	6.33% (7.5 bpd)	5.83% (7.0 bpd)
FVJ0	4.30% (8.0 bpd)	3.85% (7.2 bpd)

Source: MF Global UK Limited

INTEREST RATE PRODUCTS

Bonds | 26-Feb-10

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US Treasuries

RANGE TRADING

During March, the 10 year treasury yield is expected to range between 3.50% and 3.85%. Factors influencing the market will be mixed.

DATA IMPACT

Economic data is likely to lean friendly, as unusually harsh winter weather adversely affected employment growth, construction, industrial output, and retail sales in February. Although the impact of weather is transitory and the expansion should slowly continue, the market is in the process of questioning the underlying pace of demand given the sharp drop in February Consumer Confidence, the decline in January non-defense capital good orders excluding aircraft, and a record low in January new home sales. No matter the context, weak macro data headlines will cool recovery expectations. Further, lack of confidence in political leadership and the need of state and local governments to cut deficits are creating a headwind to the economic recovery. Globally, the dip in the February German IFO survey, the decline in January French consumer spending, and drop in February Italian Consumer confidence have eased the outlook for growth in Europe. Confirming the slowdown in data, ECB member Draghi recently said the euro area recovery is fragile with weak labor markets and stringent bank lending. Likewise ECB member Quaden called the economic recovery precarious. Looking to Asia, the S&P is forecasting a correction in the Chinese property market, and the PBOC is working to slow lending growth to prevent an asset bubble. Inflationary pressures are limited due to ample slack in the U.S. labor market and low capacity utilization rates in the OECD. A near 10% U.S. unemployment rate and flat to lower trend in the CPI housing component best define deflationary pressures. However, purchasing manager price indices are rising globally and suggest the inventory cycle and increased trade activity are lifting inflationary pressures. There are is also talk of significant labor shortages in Chinese exports areas. The desire to attract rural workers has led to a hike in the minimum wage in certain Chinese exporting states.

CREDIT CONDITIONS

On the surface, credit conditions seem supportive for treasury prices. S&P has warned it may downgrade Greece's credit rating by the end of March. As a result, Portugal, Spain and the European banking system remain under the credit microscope. However, there are signs of stability in the U.S. real estate market. Even though Real Capital Analytics reported a 137% y/y increase in the commercial default rate in Q4 2009, Moody's/REAL Commercial Property Price Index jumped by a sequential record in December suggesting improved conditions. Simon Properties is also looking to take over mall operator General Growth Properties. General Growth is attempting to fend off the takeover believing the offer is too low. Furthermore, high end U.S. homebuilder Toll Brothers reported a normalized cancellation rate of 6.7% in FY Q1 and noted its February sales event produced the highest per community sales deposit for any week in February since 2006. Toll Brothers went on to report that in its best markets deposits were tracking the five and ten year averages.

POOR VALUATION AT THE FRONT END

Technically, the treasury market faces the end of the Fed's MBS purchase program and the removal emergency liquidity measures. At the margin, these measures could leave buyers cautious. Likewise, valuation remains poor at the front end of the curve. Treasury issues with maturity of three years or less are yielding below the year over year core CPI rate of 1.60%.

European Bonds

CROSS CURRENTS

MFGR expects the bund yield to work sideways to lower in March. Yields touched 3.30% in February before sinking back 3.11% due to the high level of risk aversion in the markets. MFGR sees the yield ranging between 2.9% and 3.25%.The market will face cross currents.

POSITIVES FOR BONDS

A number of factors will underpin the bund prices. 1.) The economic data is deteriorating across Europe and eroding confidence. German confidence unexpectedly declined in February. French Consumer Confidence also pulled back. The job situation is worsening in Europe as job focused stimulus wanes. French job seekers hit their highest level since 2009. Finnish unemployment rose to 9.2% from 7.9% German unemployment actually stayed pat in February but remains elevated at 8.2%. From the bottom up, Carrefour announced that they will cut 1672 jobs in Belgium. 2.) There is no resolve over the situation in Greece. Contagion is still a great concern. Moreover, rating agencies are still threatening to downgrade the debt and Moody's just downgraded Greek banks. 3.) Social unrest is increasing as peripheral European countries are forced to face the populous consequences of government retrenchment. Greece has already faced two 24 hour strikes. 4.) There is external risk from the concern over the growth trajectory in China and EM. There are concerns that China and India will reallocate stimulus, focusing it more on domestic consumption rather than infrastructure projects. This will dampen the influence that EM growth packages have had on the macro recovery. There are already concerns that the revival will not have the legs to stay firm in H2. The economic recovery has been fuelled by simulative policy and at this point it does not appear to be self-sustaining. The removal of the potent influence of EM policy will provide insight as to whether or not the recovery in developed economies will be sustainable.

RISKS

Though the factors pressuring the bund yield are compelling, there are tailwinds. For one, from a valuation perspective, bunds are not cheap. Yields are near all time lows. Secondly, policy is still simulative and though the pace of recovery is in question, the recovery itself is not. The Fed is set to keep rates low for an extended period of time and the ECB is likely to engage in the same strategy. Barring a complete, financial meltdown radiating from the Greek debt problems, low rates will encourage risk taking behaviour.

INTEREST RATE PRODUCTS

Foreign Exchange | 26-Feb-10

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Risks to the dollar's rally

AN OVER CROWDED TRADE

MFGR believes that dollar and yen based crosses are likely to trade sideways through March. The fundamentals continue to support dollar strength but the trade is very over crowded. Risk aversion continues to be in focus as credit risk and the situation in Greece and the peripheral European markets remain unresolved. The market will keep a keen focus on the ability of Club Med to issue debt and specifically watch the interest differentials. The current 355bps between the Greek 10-yr and the German 10-yr is disconcerting and to issue debt at that spread foreshadows trouble when Greece is forced to manage colossal interest payments. This threat is the same for all of the PIIGS. Risk aversion is also catalyzed by the removal of liquidity in EM. China has continued to impose stricter lending standards and increased reserve ratios for banks to try and prevent a bubble from occurring. There is now a concern that China and India will relocate stimulus to focus more on domestic consumption rather than infrastructure. This will cause the markets to re-price the trajectory of global growth as the very potent influence of EM stimulus would be reduced.

THE FUNDAMENTAL BACKDROP

Fundamentally, there is still much to focus on. The dollar, in addition to being underpinned by safe haven is supported by the actions of the central bank. Though Chairman Bernanke reiterated that the 25bps hike in the discount rate did not signal policy shift, it did suggest a.) that the Fed is in a position to proceed with unwinding emergency liquidity facilities and b.) the central bank is confident in the US's recovery. However, there are risks to the dollar's rally. For one, while comparably the US looks better than Europe, UK and Japan, the recent round of data has been disappointing. From CAPEX spending to consumer confidence to housing, there are some that are questioning the economy's ability to make this recovery self-sustaining. Moreover, US labour data has been deteriorating. While weather has been an issue, there is a concern that once the winter storms ease, hiring may continue to remain anemic. Secondly, the U.S. political environment is ambiguous and the changes in the tax structure proposed by the Obama administration are anti-growth and will not be conducive to attractive capital.

EUR/USD RANGE TRADING FOR NOW

Outside the US, while we do believe EUR/USD should range in March, the medium-term bear trend will likely remain intact. The data has been unfavorable and the ECB will not be able to raise rates with the active volcano that is Club Med churning in the backdrop. Sterling continues to fall v. the greenback. The pressure comes from the political environment, Darling's continued pledge to keep stimulus high when fiscal sustainability is in question and the possibility of more QE. However, top to bottom GBP/USD has fallen almost 6% in February and some consolidation and correction are likely. Finally, looking at the commodity currencies, MFGR believes that the RBA will hike at their next meeting. This will underpin AUD in the near-term but if China does decide to reallocate stimulus more domestically, it will cause a re-pricing of AUD valuation. MFGR continues to like CAD as the growth momentum seems solid. MFGR would look to sell AUD/CAD post the RBA meeting.

INTEREST RATE PRODUCTS

Money Markets | 26-Feb-10

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Money Market conditions & LIBORs

FOCUS TURNING TO FSA LIQUIDITY RULES

Market liquidity remains thin with activity concentrated on short dates. Attention is beginning to focus on the FSA liquidity rules which begin to bite in the summer which will place emphasis on longer funding putting pressure on 6M and 1Y rates – some are already anticipating this. These liquidity rules and capital requirements will, of course, increase the cost of running a banking business. LIBOR settlement rates are said to continue to have no precise relationship with market rates which are still quite heavily tiered.

UPWARD PRESSURE ON LIBORS

Although, as we say below, the Bank Rate will remain unchanged until the end of the year, upward pressure on LIBORs and longer period rates are likely as liquidity rules are anticipated and banks refinance maturing liabilities. This, and the state of banks in the euro zone which may not yet be fully acknowledged, is expected to continue to widen credit spreads in various instruments which at one time had narrowed to pre-crisis levels.

FX MOVES & IMPLICATIONS FOR MORE QE

On monetary policy, the MPC look comfortable with a weakening exchange rate. Should the euro/sterling rate weaken, i.e. weaker euro, that could be one of the factors prompting more QE eventually – likely to be via gilts and, if necessary, I don't think they will mess around but whack in another £100bn. Gilts look OK despite the doomsters. The maturing SLS will not be replaced (state aid under EU rules) – but private paper, haircut accordingly, could go into a revamped LTR. With the domestic and global outlook so uncertain it is unwise to anticipate a tightening of monetary policy via the Bank Rate until the tail end of the year but remember that a lower remuneration rate for reserves has been kicked into the long grass.

US EQUITIES

TJX ($1 BLN), JUNIPER ($1 BLN), LOWE'S ($5 BLN), AND TRANSOCEAN ($3.2 BLN) HAVE RECENTLY COMMITTED TO BUYING SHARES.

THE SCHLUMBERGER BUY OF SMITH INTERNATIONAL, THE COKE PURCHASE OF NORTH AMERICAN BOTTLING, RR DONNELLY'S BID FOR BOWNE, AND RUMORS THAT MILLIPORE WILL BE BOUGHT HIGHLIGHT VIBRANT M&A ACTIVITY.

US Equities | 26-Feb-10

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Pricing risks

S&P 500 futures are expected to range between 1050 and 1120. The market will continue to price the impact of the Greek fiscal crisis, and signs of stalling economic growth on the direction of corporate profits. There is fear that Greece will be the start a sovereign debt crisis similar to Thailand, which signaled the beginning of the Asian financial crisis in the late 1990's. Credit uncertainty has stalled risk taking in equities despite lack of competition from low treasury and cash yields. Earnings estimates have notched down over the last four weeks, but remain elevated. Share-weighted year over year profit growth for the S&P 500 has been cut from 26.4% to 25.8%. Corporate event flow has been bullish. There have been a number of large buyback announcements and a pick up in M&A activity. Improved business conditions, the need for growth, and a healing of the corporate debt market have benefited M&A. Lack of confidence in political leadership and the need for a painful government sector retrenchment have prevented the market from fully embracing the bullish M&A trend. Looking at sectors, there is no clear catalyst. News from the technology sector has been supportive. Inventories are lean, Ingram Micro noted strong demand for product, and DELL was optimistic about a pick up in enterprise spending. Furthermore, memory prices are firm, the North American semiconductor book to bill ratio has risen sharply, and there is talk of technology product shortage due to labor constraint in China. A seasonal lull in IT demand post Christmas and the Lunar New Year appears to be weighing on the technology sector. On the retail front, the S&P 500 Retailing index is flirting with the late December high helped by increased same store sale growth and tight cost management. Consumer spending has held better than expected given a handful of earnings surprises in the restaurant sector, and Carnival reporting record wave of cruise bookings. Still high unemployment, sluggish income growth, and a consumer which is unwilling to leverage are restraining the sector. Retailers are planning to lift capital spending from 2009 consistent with an improved profit outlook. Financials continue to struggle with limited loan demand and still high credit loss. Credit card and real estate portfolios are mending slowly. Commercial real estate defaults are still rising, although there was some firming of commercial real estate prices in December. The residential market continues to chew threw excessive existing supply. On the plus side, there has been a pick up in short sales and Toll Brothers reported some of its markets were seeing normalized demand. At an investor conference, JP Morgan cut its outlook for return on equity for its investment banking, credit card, commercial banking and retail finance sectors, while reiterating expectations for high loss on its home equity and residential mortgage business. A reduction in loan loss will open up a surge in profits, but a major decline in loss provision is still quarters away.

Material shares are being hurt by concerns over tighter fiscal and monetary policy in China and India, and questions over the strength of housing and auto demand in the OECD. Fading clunker incentives, depressed home sales in the U.S., and talk of excessive building in China have hurt the sector. Rio Tinto recently showed concern that second half 2010 growth would stall as stimulus affects faded. The results of the National People's Congress meeting in early March will influence the material sector. The Chinese government will layout its stimulus plans for infrastructure. There is a feeling that infrastructure project incentives may slow and stimulus will be shifted toward consumption and direct improvement on standards of living. In a recent conference, Dow Chemical indicated that EM continued to lead the economic rebound. Year over year and sequential volume growth was said to be occurring across geographical region except North America.

EUROPEAN EQUITIES

European Equities | 26-Feb-10

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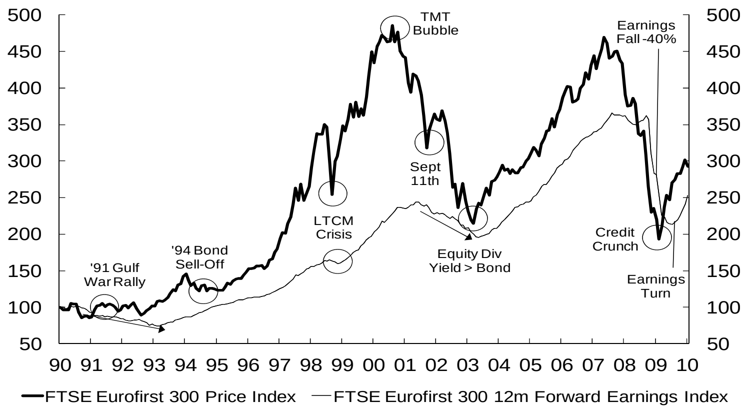
Rising earnings phase

A NEW RISING EARNINGS PHASE

Earnings in Pan-Europe are now turning positive - we are in a new rising earnings phase that we believe is good news for equity prices. From October 2008 to August 2009 12m forward earnings fell -40% peak-to-trough. Since August 2009, Pan-European 12m forward earnings have moved decisively higher as month by month we moved closer to Dec 2010's EPS estimates that are forecast to be more than 20% higher than 2009.

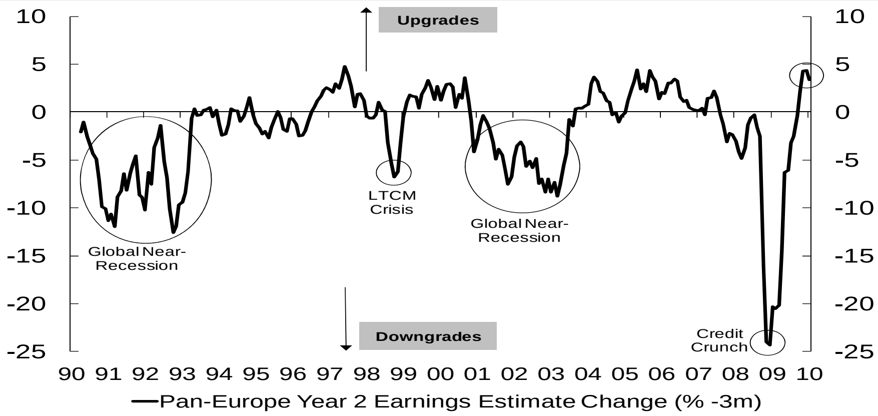
FTSE EUROFIRST 300 PRICE AND EARNINGS INDICES (FEB '90 – FEB '10)



Source: IBES Consensus, Thomson Financial and MF Global UK Limited

If we strip out the growth element of using 12m forward earnings, the chart below shows that year 2 earnings have also moved decisively into upgrade mode. Over the past three months year 2 earnings have been upgraded by over 3%.

PAN-EUROPE YEAR 2 CONSENSUS EARNINGS ESTIMATE CHANGE (% -3M)



Source: Consensus, Thomson Financial and MF Global UK Limited

A SHORT DOWNGRADE CYCLE

What is interesting is how short the downgrade cycle has been during the recent recession. In the early 1990's and early 2000's the downgrade cycle lasted 18 months to 2 years — this time round it has been half that time. We suspect that this is a reflection of better management information systems or one could say that it's been an "SAP recession". That is to say that managements using SAP (or similar) software were able to identify falling demand much earlier than in the early 1990's recession. Consequently, managements were able to shut down plants much earlier; the flipside of this is that as demand improved they have been able to reopen plants much more quickly than in prior recessions. This bodes well for the global economic recovery and consequently supportive of further earnings increases, in our view.

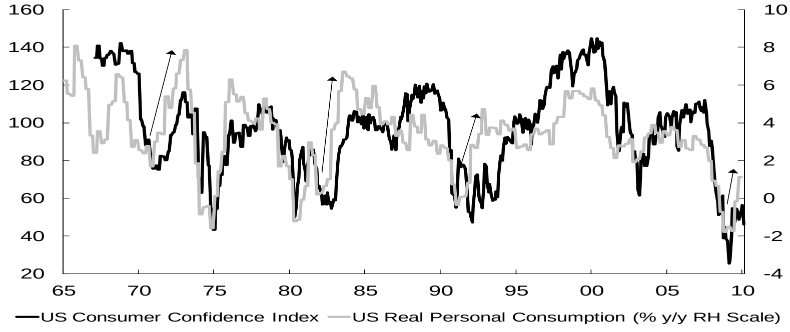
The top-line will grow

ROBUST GDP GROWTH OVER NEXT TWO YEARS SHOULD BE A KEY DRIVER

Much has been written by market commentators that recent earnings upgrades are unsustainable as they are the result of cost-cutting measures and that there will be no top-line sales growth in the coming years. We don't believe that this is true; we agree that at the bottom of a recession, cost-cutting is a key driver of earnings upgrades. However, we believe that robust GDP growth over the next two years will be enough to deliver reasonable top-line sales growth. Low US consumer confidence is often cited as a potential drag on the US recovery. We agree that US consumer confidence is bouncing back from record lows but remains at very subdued levels. With consumer spending representing 70% of US real GDP it is certainly key to the US and Global recovery that US consumers return to the malls and start spending again.

A HIGH CORRELATION BETWEEN CONFIDENCE AND CONSUMPTION

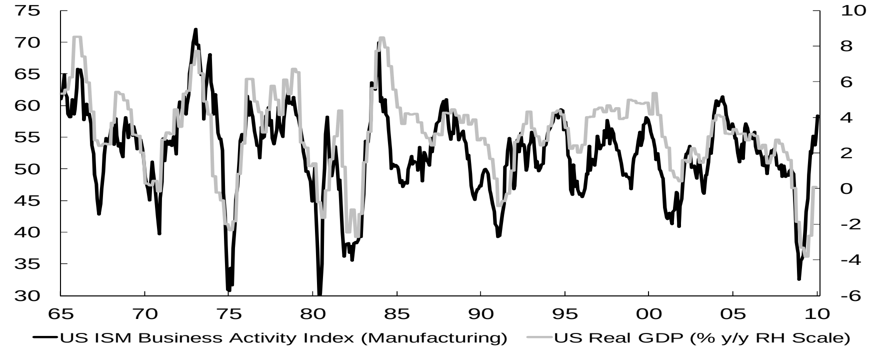
US CONSUMER CONFIDENCE AND US REAL PERSONAL CONSUMPTION %



Source: Thomson Financial and MF Global UK Limited

The chart above shows that there is a very tight relationship between US consumer confidence and US real personal consumption. However, we have highlighted those post-recession periods when US consumer confidence remained low but that did not inhibit US personal consumption. At the start of a recession with unemployment rising and consumer confidence low the US public tends rightly to hold back on spending. However, we suspect that as the recession improves, unemployment starts falling yet consumers' confidence remains cautious but those in employment feel positive enough to start spending again.

US ISM MANUFACTURING SURVEY AND US REAL GDP %

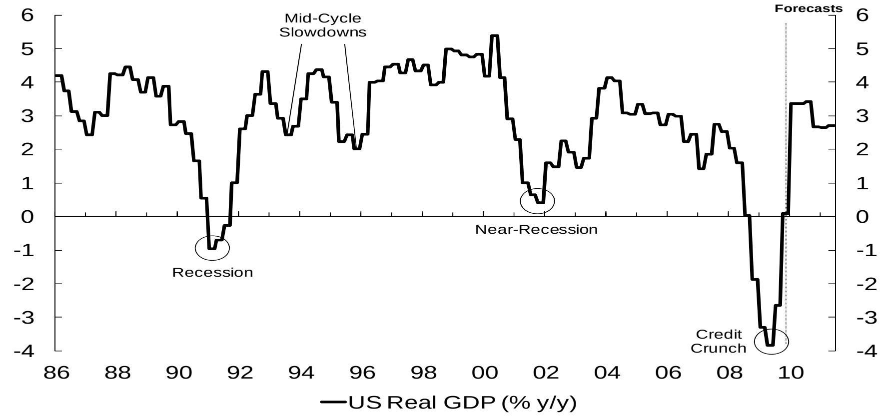


Source: Thomson Financial and MF Global UK Limited

CORPORATE TOP LINE SALES TO DRIVE EARNINGS AHEAD

The US ISM Manufacturing survey has bounced sharply since the start of the year and was one of our key recovery indicators that we highlighted at the start of 2009 to lead the S&P 500 higher. Current readings are consistent with around 3% to 4% US real GDP growth. This ties in well with current consensus forecasts for US real GDP growth of the same 2.5% to 3.0% in 2010 and 2011. At this level we believe that corporate top line sales will grow and will be able to drive the market's earnings ahead.

US REAL GDP %

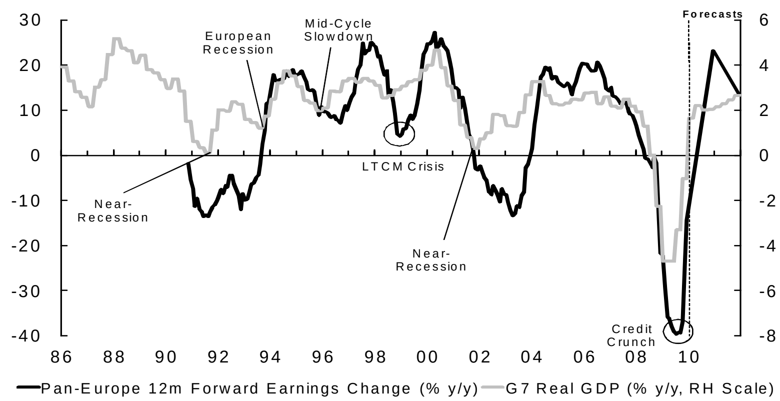


Source: Thomson Financial, Reuters Consensus and MF Global UK Limited

TOP-OF-THE-RANGE FORECASTS

Pan-European earnings tend to have a reasonable but geared relationship with G7 real GDP. If G7 real GDP is healthy at say 2% to 4%, Pan-European earnings tend to grow at 10% to 20%. However, as the global economy falls into recession or close to recession Pan-European earnings turn sharply negative. OECD forecasts expect G7 real GDP to recover to 2.0% to 2.5% in 2010 and 2011. We expect Pan-European 12m forward earnings to rebound 23% in 2010 and continue to rise by 13% in 2011. Our expectations for strong earnings growth is the key driver to our top-of-the-range FTSE Eurofirst 300 2010 year-end target of 1290 (+23%) and 2011 year-end target of 1465 (+14%).

G7 REAL GDP % AND PAN-EUROPE 12M FORWARD EARNINGS CHANGE %



Source: IBES Consensus, OECD Forecasts, Thomson Financial and MF Global UK Limited

If you would like to see the full publication please contact Stewart Breed or your sales representative.

COMMODITIES

Commodities | 26-Feb-10

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CRB

DOWNSIDE RISKS

Investors are unlikely to funnel more capital into commodities during the next 60 days. China continues to rein in credit ahead of an early March National Party Meeting which is likely to shift spending emphasis from infrastructure to consumer goods. Additionally, 2010 global growth estimates are being pared back amid EU issues with sovereign debt, a slow US recovery and downward revisions in Asian growth. Thus individual commodities are more likely to trade on their stand-alone fundamentals than in recent months when large capital inflows "lifted all boats" in the CRB. From a CRB component standpoint, Brazil is poised to harvest a large sugar crop while coffee supplies are fully adequate. Crude oil is range bound in $74-$84 band with inflationary/recovery expectations undermined by ongoing adequacy of supply, doggy demand and no catalyst to propel market above January $85 high driven by early year commodity buying euphoria. Meanwhile gold bulls are humbled by sidelining of investor and physical buying as charts suggest technical erosion to $1018/oz. The livestock price outlook is mixed with expectations for additional upside seasonal strength in hogs (although extended PRC/Russia bans on US poultry bans would pressure entire US meat complex) while cattle highs may be in as warming southern plains temps improve feedlot gains. And finally, grain/oilseed upside is limited by record S. American crops, corn importer shunning of low quality '09 US corn, ample US/world wheat supplies and fear that USDA may be understating total 2010 US corn/soybean planted area. The February CRB rally, which managed to regain about ½ of Jan/early Feb price plunge, was unable to stage a breakout above its 50 DMA suggesting continued erosion to low 440 area. The CRB is currently near high end of expected 441-480 trading range.

SELL CRB 475 OR BETTER

Energy

OIL PRICES SHOULD RANGE BETWEEN $74.00-$84.00/BBL

The oil market is expected to trade in a mixed direction in March, as the energy markets sort out the tugs-of-war between whether the economy is strengthening or weakening, and whether the U.S. or the Eurozone deserves the stronger currency.

Energy prices have been determined mainly by technical factors in the second half of Feb. COT data showed that between Jan 12th & Feb 9th, non-commercials liquidated 93,600 contracts, or 69% of their net long position, causing oil prices to fall roughly $15.00/bbl in that time. Since that decline, we've gotten one week's data so far which has shown that 26,400 contracts were added back to the long side, helping prices advance $3.22/bbl in that time. The buying sent prices above the 50-day moving average and the Feb 3rd high at $78.04. The washout of those long positions in Jan-Feb occurred at a time just before a positive seasonal pattern began on Feb 19th. The positive seasonal lasts until May in gasoline and until Sep in crude oil.

It's not quite a certainty, however, that the oil market will be able to react to the positive seasonal pattern. Ongoing struggles in Europe to deal with Greece's debt situation will have the potential to boost the dollar, and thus make energy less attractive to non-dollar based consumers. The state of the economy is not a certainty, however, after weakness in home sales and consumer confidence in late-Feb increased the chances of a double-dip recession. Prospects for the economy don't appear likely to get much help from Washington either, where focus shifted from healthcare to jobs in late-Jan and back to healthcare by early-Feb. Commodity investors have shown some migration away from commodities, as investment fell in Jan by $12B to $245B, marking the first decline since Nov '08. Investors cited tightening of lending in China as a reason for liquidation.

TRADE THE $74.00-$84.00/BBL RANGE

WE ANTICIPATE GOLD PRICES TO RANGE BETWEEN $1,060-$1,130 THIS MONTH, WITH SILVER RANGING FROM $14.65-$17.00. PLATINUM STILL APPEARS STRONG, AND SHOULD MAINTAIN ITS UPWARD DIRECTION, WITH A RANGE FROM $1,500-$1,600

Precious metals

Precious metals are expected to trade in a mixed direction in March, as they sort out the tugs-of-war between whether the economy is strengthening or weakening, and whether the U.S. or the Eurozone deserves the stronger currency. Precious metals have been jostled by technical factors in the second half of Feb. Open interest in gold, for instance, fell 92,590 contracts from a Nov 23rd high to a Feb 12th low, or 16.8%. The COT data recently showed a 30.8% decrease in the non-commercial net long in a similar period. Both indicators suggested that a major liquidation of longs had taken place and that the market was free to resume buying. A bullish wedge pattern in gold and a developing head & shoulders bottom in gold and silver bolster that argument. The latest COT data showed that a large short also existed in the euro and sterling. Combining that with a 7,400 contract build to gold's non-commercial holdings in the w/e Feb 16th, suggests that metals can benefit from even minor weakness in the dollar. Benefit can also come from a picture of slow economic growth in the U.S., where weakness in home sales and consumer confidence in late-Feb increased the chances of a double-dip recession. Such a condition can increase pressure on the dollar and stock market, and boost the favorability of precious metals as an alternative investment. Prospects for the economy don't appear likely to get much help from Washington, where focus shifted from healthcare to jobs in late-Jan and back to healthcare by early-Feb.

WE'RE LOWERING THE UPPER BOUNDARY OF THE PRICE RANGE GIVEN IN OUR DEC 22ND 2010 OUTLOOK TO $1,225 FROM $1,350 AND THE LOWER BOUNDARY TO $1,018 FROM $1,033 ORIGINALLY. OUR FORECAST FOR AVERAGE AND YEAR-END PRICES IS UNCHANGED AT $1,150.

TRADE THE $1,060-$1,130 RANGE
BUY: PLJ0 AT $1,500, TARGET $1,700, RISK $1,450

While the COT data showed a build in non-commercials' net longs, open interest data has yet to reverse higher, and represents a negative influence. Ongoing problems in Greece won't find a quick solution and could weigh on the euro. The Fed's unwinding of emergency stimulus should also boost the dollar. Pressuring gold will also be the Feb 17th Gold Demand Trends report which showed a surplus of 504 tonnes in 2009 vs. a 293 deficit in 2008. The rally in gold prices in Sep-Nov helped create a 119.7 tonne surplus in Q4, with key physical buyers shut out from the market during key holiday and festival seasons. On Feb 19th, we learned from VM Group that a key spark for the Sep-Nov rally was a sharp 34% reduction in the hedge book. These factors should keep metals prices from getting out of hand on the upside this year.

CK/SK/WK UNLIKELY TO PENETRATE $4.00/$9.80/$5.20 RESPECTIVELY.

Grains

Anticipate range bound trade for the next several weeks. SX 2010 has the best shot of taking out early Feb lows of all three markets as record S. American soybean harvest advances and prospects for a late US spring spawns ideas of higher 2010 US soybean acres. Advise selling out of the money May soybean calls even through wheat, which is linked to corn, has the most negative seasonal tendency during next 60 days. Corn stands the best chance of staging a spring rally amid critical need for higher 2010 acres and a trend or better 2010 US corn yield but price gains will be contained by above average US soil moisture reserves and poor quality 2009 crop corn (that is turning off importers and poised to overwhelm late winter US cash pipeline). Additionally, large S. Hemisphere corn production promises to constrain J/J/A US corn exports even more. Wheat will erode vs. corn as the US growing season gets underway as continuation of prevailing cool/wet Midwest weather pattern into spring is a far greater threat to 2010 US corn production than US wheat production. Upside price breakouts will be constrained further by slower capital flow into commodities that investors view more cautiously amid prospects for a prolonged recession. Our decidedly guarded March price outlook will acquiesce to a broader range of price possibilities mid April onward but for the moment we think burden of proof is on shoulders of bulls in wake of largely technically driven February rallies in corn, soybeans and wheat. Row crop bulls should not look for much relief in USDA's March 10th revision of 2009 production. A far more substantive report will occur on March 31 when USDA updates not only 2010 US row crop acreage but March 1 stocks as well. The trade typically overestimates corn area and underestimates soybean area on the March Intentions report.

SELL WN RALLIES ABOVE $5.30

SELL SX $9.40 OR BETTER

BUYING OIL SHARE BELOW 40.75%

BULL SPREADING SN/SX AT 20 CENTS OR BETTER.

BUY CZ/SELL WZ AT $1.60 OR BETTER

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