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DEBT MARKETS:
Favor treasuries on the sideways to long side as the global economic climate remains unchanged. Domestically, though the ISM manufacturing index was stronger-than-expected, the bottom up data continues to be poor and US car sales posted their worst month since 1981. On the labour front, job loss has been prolific and will be reflected in Friday's Non-Farm Payrolls number. MFGR is expecting a drop of greater than -500K. Additionally, the once organic stimulus of lower mortgage rates is disappearing and refinancing activity is again falling. Internationally, the data is also troublesome. Chinese PMI shrunk for the 4th month in a row, Aussie Building Approvals are down -32.9% Y/Y, and the European PMI figures remain depressed.

Monetary policy and fiscal stimulus will continue to be a global theme. The Fed will remain in ZIRP while other central banks continue to ease policy. The RBA just cut rates 100bps and the BOE and ECB are slated to meet this week. Expect 50bps out of the BOE and a hold from the ECB. On the fiscal front, it feels like political momentum is working toward downsizing the size of government spending in the stimulus package. The Obama Administration's position on the bank bailout is uncertain with a plan coming, but the details unknown. The populist bias of the Administration creates uncertainty over the usefulness and success of the bailout. The uptick in the LIBOR fixing is consistent with worries that the banking sector will remain broken. The market is exhausted and requires a plan that will target sectors capable of rejuvenating economic activity not improving social welfare. Additionally, the market requires a conclusion on the possibility of creating a bank to buy troubles assets. As Congress revisits the original recipe TARP, the market becomes more impatient and the concerns over the stability of the financial sector intensify.

While the aforementioned factors support the market, supply and valuation make the bear case. On the supply front, the Treasury announced it would likely borrow $493B in Q1 with a huge amount of borrowing in the 5 yr space. Funding fears are also a global theme but judging from the most recent US auctions demand for treasuries is still fairly robust. Buyers who fear the risks in the global economy are still parking money in the US. It was noted that low yields in Asia coupled with rising currency fears are making Asian bonds unattractive. Capital evacuation out of such debt will lead to treasury interest. The opening of the corporate market is another bearish factor for treasuries. Supply over the past few weeks has been enormous and the yields offered are significantly more attractive than what is currently associated with the treasuries. The Federal Reserve's creativity also assists in making the bear case. Though the Fed's purchases of MBS and agency paper have not had the desired effect on mortgages, it does reflect their commitment to improving economic conditions.

Looking at the curve, the spread between the 2 year and 5 year treasury is expected to widen on ultra easy monetary policy and aggressive issuance. The spread, near 95 bps, traded to 160 bps in the wake of the '90/91 and '00 recessions. A repeat is expected.

~Kalivas/Hoversen

EQUITY MARKETS:

Equity prices are expected to trade sideways with price action reactionary to the details of the government's stimulus package and plan to aid the banking system. At this juncture, the market has grown tired of politics and confidence in Washington has eroded investor confidence. Profit growth in the financial sector has been bearish with results falling short of expectations. The outlook for profit growth in the financial sector has been revised down for Q1. A rising unemployment rate is expected to spark further credit deterioration in the consumer sector, and commercial real estate delinquency rates are poised to rise on soft consumer demand, reduced demand for office space, and corporate restructuring. Profits in the non-financial sector have been slightly better than expected, but the outlook for growth is cautious going into Q1. A few companies have discussed a bottom in activity, but the economy shows limited signs of accelerating with a January ISM at only 35.6. The main positive for the market rests in an open corporate bond market. $9.85 bln in high yield debt was solid in January. Sales reached their highest total since June of 2008. Investment grade issuance has also been strong. The spread between a corporate B credit and 10 year treasury has fallen about 150 bps since mid January. Credit stress was the genesis of the bear market, and credit shows stability despite poor performance in the financial sector opening up the chance for improved economic conditions.

~Nick Kalivas

CURRENCIES:

The global economy continues to dramatically deteriorate. Capacity and production cuts seem common hat and layoffs in all industries are prolific. The growing economic problems are all laid on the back-drop of a shaky financial system that is in desperate need of rescue. The widespread contraction is weighing heavily on sentiment and keeps risk aversion prevalent. Additionally, it keeps the trade focused on the efforts of governing bodies to backstop the system and prevent a deeper, longer and more damaging recession.

On the Monetary policy front, The RBA just cut their benchmark rate to 3.25%, the bank's lowest target since 1964. Despite already passing two stimulus packages, the bank is likely to continue to cut rates as Australia's main trading partners, US, Japan and South Korea are already in recession. The Aussie economy is dependant on exports and the trade balance has gone from AUD 2.582B in October to AUD .589M in December. Furthermore, the negative economic outlook for China creates further problems for the Aussie macro system. The IMF noted that 8% growth in China is still challenging and moreover that the economy may be in need of additional stimulus. The BOE and the ECB will also make major monetary policy decisions. Their meetings are on 2/5. The BOE is moving toward ZIRP and though they have recently stated that the QE is not on the agenda, MFGR would not rule it out. Though the BOE has been exceptionally proactive in employing alternative policies, the British banks are still reluctant to lend and may require more aggressive measures to generate activity. The ECB also be on the way to significantly lower rates, albeit at a slower pace. Though Euro-Zone PPI and German CPI data clearly showed that inflation has dramatically subsided and German Retail sales and labour figures exhibited a pronounced slow down in conditions, ECB rhetoric, which normally acts as a very trustworthy barometer of policy, suggests that the central bank will remain on hold through March. MFGR agrees with this sentiment and would thus look for the ECB to employ more alternative measures heading into the March meeting.

Bailout and stimulus will remain global theme. The economic community is waiting on the US Senate's revised stimulus plan and continues to hope for some rescue for the

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banking sector. The market is revisiting TARP 1.0 as the bad bank plan is back on the table. The Fed is not impotent at this point, but as far as monetary policy goes, they are nearing the end of their rope. The US is operating in what Chariman Bernanke refers to as "Credit Easing" but it doesn't seem to be keeping mortgage rates down as desired. The option of buying treasuries has been proposed but not yet enabled. If the US government does decide to monetize the debt, expect questions to arise over the integrity of the dollar. On a global scale, the Aussies have pushed through their second package, as mentioned above, and the UK is working on one of their own. Outside of the numerous individual sovereign stimulus packages in Europe, there are rumors that the ECB is also considering the creation of a bad bank. Japan is devising a plan to help recapitalize their banking sector. The plan, as detailed thus far, will buy Y1 trillion in shares held by Japanese banks. The EM space is not to be forgotten as they are working on strategies to backstop their own economies. Brazil has already cut rates 75bps, Mexico is looking into a stimulus package and China is seeking a stimulus for its refiners, just to cite a few examples.

MFGR expects to see the FX markers move in a holding pattern until fiscal stimulus is solidified. Remember that fiscal stimulus needs to be concise, direct and accurate to be effective. The package needs to target areas that are essential to economic recovery, not sectors that simply improve social welfare. If the Senate's revised addition does not encompass these concepts, the market is bound to be thoroughly disappointed. The market also awaits further details from Treasury Secretary Geithner who, next week, will lay out the plans for the Obama administration's bank rescue. MFGR's long term biases still argue for euro, sterling and pound weakness but would not be surprised to see a mild correction in these crosses. The yen will continue to trade in tandem with risk, though intervention is still a possibility considering the conditions of the Japanese trade balance. Such an action would dramatically skew yen-based crosses' correlation with equities and risk.

~Jessica Hoversen

PRECIOUS METALS:

Gold prices are expected to advance in Feb, with prices likely to reach $938.20. The rally should be made in a gradual fashion, with strength coming from Congress's $890B stimulus package and investment inflows created by fear that the stimulus creates inflation. Investment has been strong in gold recently, with 75 tonnes added to the two U.S. ETFs so far this year. We view investment demand that's tied to inflation as premature, as attention in most other markets is still on the potential for economic slowdown. Investment will have to be maintained in order to keep prices buoyant, as fundamentals don't support the strength. The WGC will report Q4 fundamentals in mid-Feb, but anecdotal reports from the Bombay Bullion Association have shown sharp y/y declines in imports to India, especially in Dec and Jan. Imports are likely to remain at low levels despite the spring wedding season, as high prices and excess bank inventories will not create much fresh demand.

~Tom Pawlicki

ENERGIES:

Crude oil prices are expected to reside in a sideways-to-higher trend in Feb. Prices should advance toward the 50-day MA, which is currently near $46.70. Crude has had difficulty in breaking out from the new sideways trend, which we believe has formed as a result of prices having reached a new equilibrium. With selling exhausted, this potential new bottom will be boosted fundamentally by signs of increasing demand in the U.S. and indications that OPEC has reached above-expected compliance with its production

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cutbacks. Recent price cuts by India and China should help to boost demand there as well. Prices could also be supported by the refill of the SPR, which kicks into gear in Mar. Pressure on oil could come from the inability of large funds to create a rebound in prices despite adding 104,636 contracts to their net position since bottoming on Nov 11th. Pressure could also continue to come from disappointing economic data.

~Tom Pawlicki

GRAINS:

Grain prices are expected to work lower. Prices will be pressured by an improved outlook for supply and on going weakness in demand. The recent rains in South America (Argentina) have eased concerns over production loss and crop stress linked to the dry weather which was present in the spring and early summer. High prices have also built expectations for increased plantings in North America this spring, and stock levels are likely to be revised upward in North America. Demand is weak. Ethanol demand is soft and energy prices have been trading flat, while livestock herds have shrunk and livestock producers are reportedly losing money. In the developing world, the global recession and rising unemployment are reducing the move of consumers up the food chain. Technically, the soybean and corn markets are flirting with the 50 day moving average and could turn systems short.

Livestock prices are expected to trade mixed to lower. Supplies are cattle and hogs are tightening, but demand is questionable, especially in the export sector. Cattle inventory numbers show shrinking supply and poor cattle feeding margins are keeping numbers trending downward. Hog supplies are expected to diminish relative to last year, but remain large historically with the industry geared up for robust exports. Poultry numbers are expected to be down 6% to 8% from a year ago and further highlight shrinking supply. Rising unemployment, globally, argues for weaker demand and will work to cap prices. Prices will get some help going into the summer grilling season as weather warms.

~ Feltes / Kalivas

CRB:

The CRB will face nearly equal influences in Feb, as weak demand for grains and livestock will be offset by increasing demand and higher prices in precious metals. Energy markets are thought to be near a bottom. We anticipate soft demand for grains based on weak ethanol production and a shrinking livestock herd. Better moisture in Argentina and increased plantings in North America could boost supply. Cattle inventories will shrink due to poor feeding margins. Gold and silver prices will counter the pressure from ags, as their appeal is increased by investment inflows and inflation hedging. Weak supply/demand fundamentals in gold have been countered by investment that has flocked to gold in anticipation that the stimulus plan and increased Fed balance sheet creates inflation. Perhaps energy markets will be the deciding factor this month, as oil has traded steady for the past six weeks. A breakout above the six week trend is suggested by increasing U.S. demand and narrowing in the contango price structure, however, the market will have to overcome its ongoing focus on weak economic data first. CRB support will be at 349.00 while resistance is 383.00.

~Feltes/Kalivas/Pawlicki

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TRADE RECCOMENDATIONS:

Debt Markets: Buy TUH9 and sell FVH9 at a ratio of 100 TUH9 to 83 FVH9. Basis the on the run issues, risk 82 bps and target 160 bps over time.

Equity Markets: Favor buying 1 March 1200 e-mini NASDAQ call and selling 2 March 1250 e-mini NASDAQ calls for a credit of 10 or better. Risk -10 and hold to exploration.

Currencies: Sell EUR/CHF at 1.5091. Target: 1.4545. Risk: 1.5260.

Energies: Buy CLJ9 at $40.00, target $50.00, risk $38.00

Precious Metals: Buy GCJ9 at $875.00, target $938.00, risk $850.00.

Grains: Favor being short corn calls and long soybean puts.

CRB: n/a

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