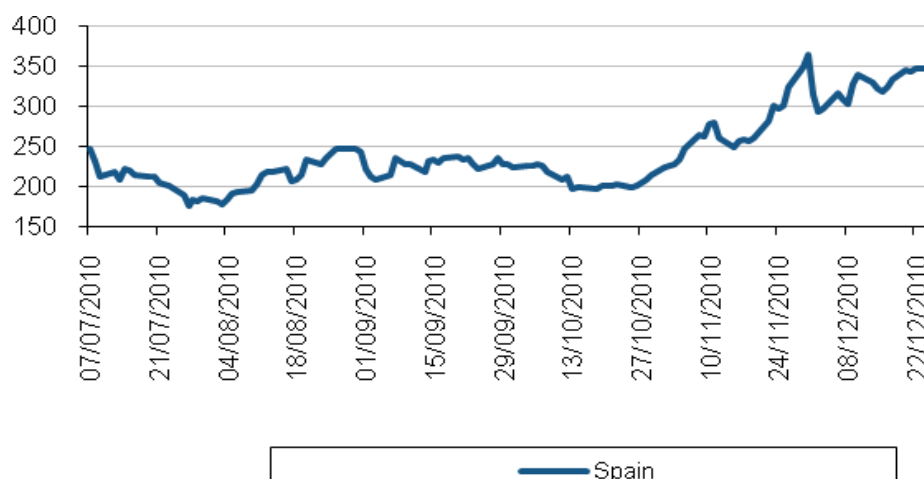


Markit Intraday Alert: A tale of exports and inflation



Source: Markit

The European CDS market opened 2011 on a strong note in response to economic data released yesterday and today. It was the first opportunity for London traders to react to the solid leading indicators published on Monday. Both the Markit Eurozone Manufacturing PMIs and the ISM Manufacturing report came in better than expected, providing ammunition to those predicting an improvement in the global economy this year. Such optimists received further support today in the form of the Markit UK Manufacturing PMI. The index for December came in at 58.3, a sixteen-year high. The high level of export orders will be welcomed by the UK government, which is pinning its hopes on an export-driven recovery.

But fresh evidence of inflationary pressures – input prices rose at the fastest rate in the survey’s nineteen year history – will be less well-received. Hawks in the Bank of England’s MPC will have yet another reason to vote for interest rate rises, and the VAT rise kicking in this month will only increase the pressure. And the evidence of rising prices was not confined to the UK. The eurozone CPI rose by 2.2% in December, the first time it has gone above the ECB’s 2% ceiling since November 2008. Few, however, are predicting a rate rise before the end of this year.

The sovereign market was relatively quiet today ahead of what should be a busy month for government bond issuance. France and Germany are due to tap the market on Thursday and Italy and Spain are scheduled to follow next week. The latter country received a boost today when China asserted that it will continue to buy Spanish government debt. China made a similar statement on Portugal late last year that had only a limited tightening effect on the sovereign’s

spreads. Spain's spreads were just 10bp tighter today, though this marked a slight outperformance in comparison to the other peripherals. News that the government is planning a second round of bank stress tests was also welcomed, though investors will be understandably sceptical given the results of the initial tests.

Gavan Nolan

Credit Analyst

Markit

Tel: +44 20 7260 2232

Email: gavan.nolan@markit.com

For further information, please visit www.markit.com

The intellectual property rights to this report provided herein is owned by Markit Group Limited. Any unauthorised use, including but not limited to copying, distributing, transmitting or otherwise of any data appearing is not permitted without Markit's prior consent. Markit shall not have any liability, duty or obligation for or relating to the content or information ("data") contained herein, any errors, inaccuracies, omissions or delays in the data, or for any actions taken in reliance thereon. In no event shall Markit be liable for any special, incidental, or consequential damages, arising out of the use of the data. Markit is a trademark owned by the Markit group.