

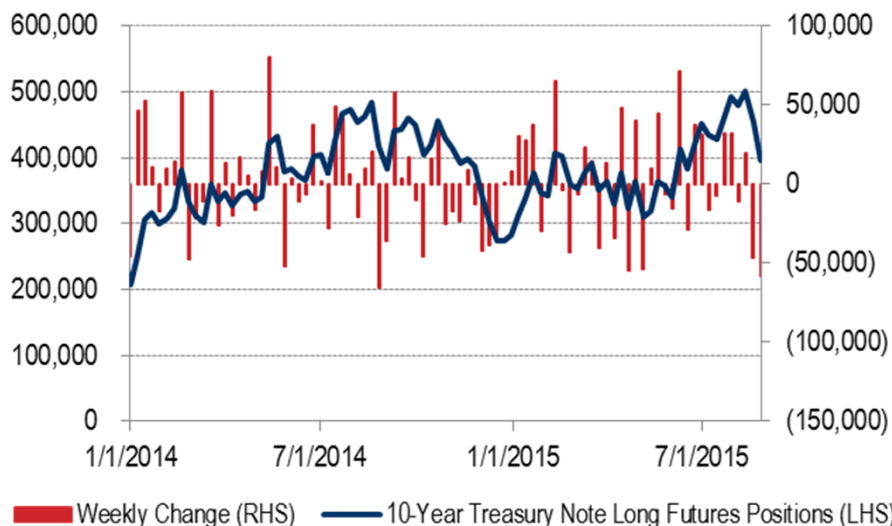
Current Rate Environment

Short Term Rates	Thursday	Prior Week	Change
1-Month LIBOR	0.20%	0.20%	0.00%
3-Month LIBOR	0.33%	0.33%	0.00%
Fed Funds	0.25%	0.25%	0.00%
Fed Discount	0.75%	0.75%	0.00%
Prime	3.25%	3.25%	0.00%
US Treasury Yields			
2-year Treasury	0.72%	0.62%	0.10%
5-year Treasury	1.51%	1.43%	0.08%
10-year Treasury	2.18%	2.04%	0.14%
Swaps vs. 3M LIBOR			
2-year	0.92%	0.90%	0.02%
5-year	1.67%	1.60%	0.07%
10-year	2.29%	2.16%	0.13%

Fedspeak & Economic News:

- The US Treasury market experienced one of the most volatile weeks in recent memory. The 10-year Treasury yield hit a weekly low of 1.90 percent on Monday – after panic seized global markets when China failed to unveil further stimulus over the weekend – and then hit a high of 2.19 percent during the close on Friday. There is a lot of speculation as to what the driving force behind yields is.
- Market participants threw a temper tantrum on Monday, after the People's Bank of China failed to announce a stimulus expansion, causing a sharp rally in US Treasuries and selloff in global equities. It is important to take into consideration that the market had been building a concentrated long position after the 10-year Treasury yield found a new home above 2.45 percent in July. If we take a look at the CFTC's 10-Year Treasury futures data, we see that the market was heavily long on August 11: Investors held about 500,000 contracts, which was the highest level since March 2008. From August 11-18, ~46,000 contracts were liquidated and then by the week after, another ~58,000 contracts were exited (after Monday's rally). The two-week liquidation was the third largest in five years and suggests that investors sold into the rally. But it is the dramatic selloff that perplexed participants.
- A number of reports have tied the pronounced selloff to China selling US Treasuries in an effort to stem the decline in the value of the yuan. This is reasonable: China is one of the largest holders of US Treasuries, so if the 800-pound gorilla comes to the playground looking to sell, then markets are going to move. However, we do not have the reserve data to verify this because it is not out yet; the most recent Treasury International Capital data (TIC) are available only through June and China's reserve figures are available only through July. Instead, we can look to US economic data to explain part of the move. For the time being, data show that the United States has been well insulated from economic woes in China: Second quarter economic growth handily beat expectations (+3.7% vs. +3.2% expected), while consumption and business investment have picked up as well.
- Despite improving economic data, the implied probability via fed futures suggests that a hike in September is unlikely. In addition, during the Fed's Jackson Hole Summit in Wyoming, Vice Chairman Fischer, along with other officials, acknowledged that the global equities selloff last week would influence the timing of the rate hike. The next two weeks will be critical to the Fed's decision.

Liquidation of 10-Year Treasury Note Futures Long Positions



The chart shows that long positions in 10-year Treasury Note futures reached their highest level in recent memory at 500,000 contracts on August 11, which was the same day that the Chinese central bank announced the devaluation of the yuan. During the following two weeks, positions would be liquidated while the market was rallying sharply. The liquidation helped provide a ceiling during the rally.

The Week Ahead

- We will have an abundance of top tier economic data this week, with the most prominent release being the August jobs report (Friday). Expectations call for an addition of 200,000 workers in August and the jobless rate ticking lower to 5.2 percent.
- The jobs report will be the last before the Fed meets again in two weeks (Sep 16-17) so its importance cannot be emphasized enough.

Date	Indicator	For	Forecast	Last
31-Aug	Chicago Purchasing Manager	Aug	54.4 (A)	54.7
1-Sep	ISM Manufacturing	Aug	52.5	52.7
1-Sep	Markit US Manufacturing PMI	Aug F	52.9	52.9
2-Sep	Factory Orders	Jul	0.9%	1.8%
2-Sep	ADP Employment Change	Aug	200k	285k
3-Sep	Trade Balance	Jul	-\$42.55B	-\$43.84B
4-Sep	Change in Nonfarm Payrolls	Aug	217k	215k
4-Sep	Unemployment Rate	Aug	5.2%	5.3%

Sources: Bloomberg; Treasury futures positions per CFTC

Cleveland, OH

David Bowen 216-689-3925 Mary Coe 216-689-4606 Dusko Djukic 216-689-4224 Sam Donzelli 216-689-3635 Anand Gomes 216-689-4932 Frank Kuriakuz 216-689-4071

Seattle, WA

Greg Dawli 206-689-2971 Wil Spink 206-689-2972

Documentation

Ramona Berce 413-567-6758 Linda Maraldo 216-689-0516 Marybeth Simon 216-689-0897



Disclaimer

This communication is generated by the derivatives sales & trading unit of KeyBank and conveyed as commentary on economic, political and/or market conditions or, in some cases, may be considered to be a general solicitation for entering into derivatives transactions, as contemplated under Commodity Futures Trading Commission (“CFTC”) Regulation 23.605, and is not a “research report” as defined therein. This communication is not to be construed as a recommendation or opinion with respect to any derivative or trading strategy involving a derivative for purposes of CFTC Part 23 Regulations. This communication does not take into account the investment objectives, financial conditions, or needs of individual parties and is not intended to serve as a basis for entering into a derivatives transaction or to suggest, in any manner, that a party should enter into a particular derivatives transaction or trading strategy involving a derivative. Parties should consult their own advisors for opinions and advice on whether to enter into any derivatives transaction or trading strategy involving a derivative. The information contained herein has been obtained from sources deemed to be reliable but it is not represented to be accurate, complete or objective. In providing this information, neither KeyBank nor any affiliate of KeyBank is acting as your agent, broker, advisor, or fiduciary, or is offering any tax, accounting, or legal advice regarding these instruments or transactions. KeyBank may have current positions or strategies that may be inconsistent with any views expressed herein.

Cleveland, OH

David Bowen	Mary Coe	Dusko Djukic	Sam Donzelli	Anand Gomes	Frank Kuriakuz
216-689-3925	216-689-4606	216-689-4224	216-689-3635	216-689-4932	216-689-4071

Seattle, WA

Greg Dawli	Wil Spink
206-689-2971	206-689-2972

Documentation

Ramona Berce	Linda Maraldo	Marybeth Simon
413-567-6758	216-689-0516	216-689-0897

