



Terry O'Brien
Head of Equity Trading, EMEA
Securities Finance
Global Transaction Services
Citi's Institutional Clients Group

Welcome

Markets are showing signs of confidence and with additional lending supply we are witnessing the first signs of stability in over a year. This reverses the year to date trend where nearly all sectors within the major indexes experienced significant downturns. Although this has been a very challenging environment to deliver revenue, our clients have benefited from the knowledge and experience of the global trading strategies executed by Citi in accordance with our clients' investment guidelines.

The International Securities Lending Association (ISLA) and Risk Management Association (RMA) recently held their annual conference in Barcelona. It was pleasing to see a strong turnout from the Securities Finance industry with a significant focus on regulation, re-education & risk mitigation of lending. Collateral flexibility was in great demand from the broker community; as the cost for OECD bonds increases they are forced to turn to less expensive, more flexible options, such as Euros & US Dollars or Equities as a preferable collateral alternative.

As part of our ongoing efforts to maximise opportunities for our lenders, we have increased our usage of the Equilend trading system. This trading platform can help to deliver additional revenue opportunities for clients through higher utilisation of portfolios via the 'AutoBorrow' functionality; this in turn has increased operational productivity by automating low-margin transactions, allowing traders to focus on achieving ever-higher rewards from special situation trading. Plans to further automate the servicing of loans by utilizing Mark to Market, Dividend, Billing and Contract comparison services will add system efficiencies which reduce costs and increase productivity as volumes continue to grow.

US equities¹

News

Securities lending spreads across 10 of 12 analysed indices increased during the week ending 28 August. Loan balances across 8 of 12 analysed indices increased during the week ending 28 August. Loan volume in CAC40 increased the most (6.9%) compared to the prior week, while Russell 2000's loan balances decreased the most (-1.2%) during the last week in August. The Standard & Poor's (S&P) 500 added

3.4% in August and the Dow climbed 3.5% as reports from consumer confidence to home sales topped economists' forecasts. Financial stocks had the biggest gains this month, with the S&P 500's second-largest industry-rising 13%. That's three times the August advance for industrial shares, which had the month's second-steepest gain. The S&P 500 has advanced for the past six months, the longest stretch of gains since January 2007.

Active stocks

- American International Group Inc (AIG)
- Sequenom Inc. (SQNM)
- First Solar Inc. (FSLR)
- Alliance Data System Corp. (ADS)
- Energy Conversion Devices Inc. (ENER)
- Validus Holding (VR)

¹ www.bloomberg.com accessed on 31 July and 3 August 2009; SunGard Financial System.

US cash and money markets²

Interest rates across the money-market yield curve continued their historic decline unabated during the month. The three-month Libor benchmark, which had dropped below 0.50% last month for the first time since inception of the index, declined another 15 basis points (bps) during August (see graph). The widely viewed Libor/OIS spread, which ballooned to over 400 bps last September has fallen to below 25 bps, a level that had been targeted by FRB Chairman Bernanke.

Economic data continued to indicate a move towards growth from recession. While an additional 247,000 jobs were lost in July, the number was stronger than had been anticipated by the market, as was some of the data associated with both the manufacturing and service components of the US economy.

The FOMC statement, following the committee's meeting on 12 August, included language that indicated a recovery, while modest, was taking hold and that

the Fed would start to consider actions to remove some of the non-traditional policy accommodation, while at the same time stating that it continues to maintain very low short-term interest rates for an extended period.

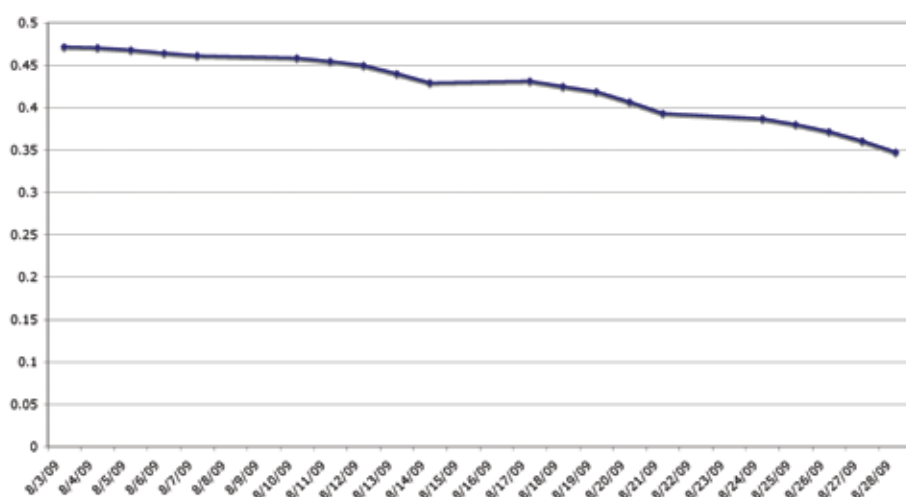
In the statement, the FOMC re-affirmed the plan to purchase Treasury, Agency and Agency MBS. However, it announced that the pace of the purchase of USD300 billion of US Treasury securities would be slowed in order to promote a smooth transition in the market away from the QE programme.

There is speculation that the FOMC may vote to reduce the size of the USD1.25 trillion MBS purchase programme at the next meeting.

On 25 August, President Obama nominated Ben Bernanke for a second term as Chairman of the Board of Governors of the Federal Reserve. In his acceptance statement, Mr Bernanke vowed to "help provide a solid foundation for growth and prosperity in an environment of price stability. Mr Bernanke now needs to be confirmed by the US Senate, and while his confirmation seems to be a sure thing, it is likely that his reconfirmation hearing will be a bit more challenging than his first.

² www.bloomberg.com accessed on 3 September 2009

3 Month Libor



US corporate bonds³

Current news

The cost to protect US corporate bonds from default rose to the highest level in more than a week as stocks worldwide slumped on speculation that the six-month rally had outpaced prospects for earnings growth.

Credit swaps on the Markit CDX North America Investment-Grade Index, used to speculate on the creditworthiness of 125 companies in the US and Canada or to protect against losses on their debt,

climbed 4 bps to a mid-price of 119 bps as of 11.33 on 31 August in New York. That's the highest since 20 August, according to CMA DataVision. An increase typically signals deterioration in the perception of credit quality.

Credit swaps on both investment-grade and high-yield, high-risk companies have plunged as investors encouraged rising economic indicators to seek higher-yielding assets. They've also dropped as company defaults continued to rise. This year, 211

corporate issuers have defaulted, almost four times the 55 defaults at this time in 2008, S&P's said in its August report.

Issues in demand

- Arvinmeritor (CUSIP 043353AC5)
- Blockbuster Inc (CUSIP 093679AC2)
- Jarden Corp (CUSIP 471109AB4)
- MGM Mirage (CUSIP552953BB6)
- Wise Metals Group (CUSIP977255AC2)

³ www.bloomberg.com, accessed on 28 and 31 August 2009.

US Treasury and agency

The specials market was relatively quiet in August. The summer doldrums seemed to take hold of the repo market. Other than the current two-year note, the open roll rate on all of the on-the-runs averaged above 0% throughout the month. This is a break from what has become the new "norm" since the inception of the TMPG fails charge.

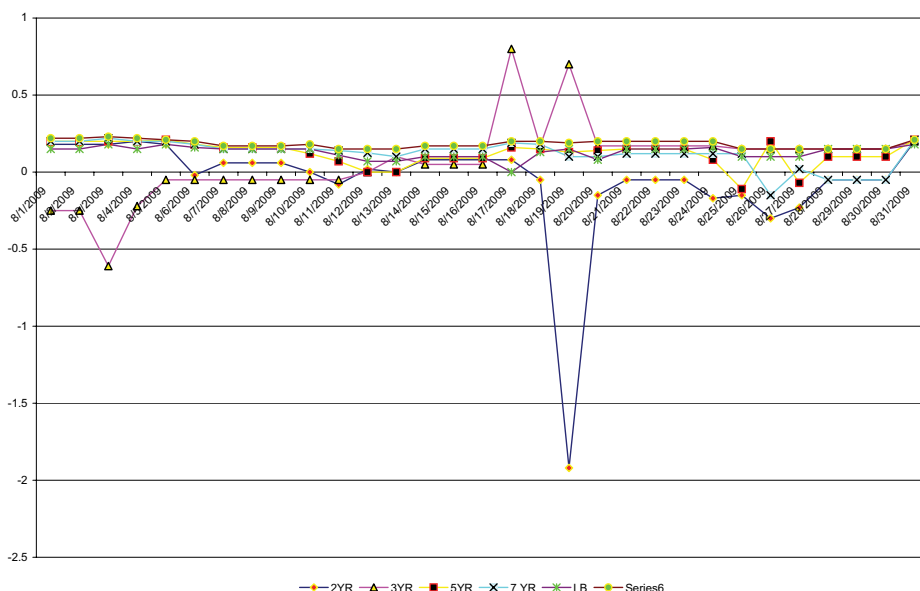
However, the term markets for some of the current issues were active. For instance, the open roll for the current ten-year note averaged 13.5 bps since its issuance on 17 August.

Despite the fact the paper didn't trade special on open, the term market was immediately active seeing the issue trade at -30 to -40 bps to mid September. There was a similar situation for the current three-year, the paper averaged 24 bps on open but traded at -13 to mid September. These term rates imply the overnight rates should begin to trade deeply negative in September.

Fed funds were relatively soft again during August, mirroring July's average of 17 bps. Treasury GC averaged 20 bps and agency GC averaged 22 bps. The phenomenon of treasury GC trading higher than Fed Funds

continued as issuance size continued to increase. The FOMC announcement was on 12 August. The Fed unanimously agreed to keep the nominal fed funds rate between 0 and 0.25%.

Current Treasury Issues - Open Roll Rates Aug 09



European money markets

The European Central Bank (ECB), as expected, left interest rates at a record low at its August meeting. The ECB also refrained from further policy stimulus while it assessed the impact of its bond purchases and 12-month repos.

Economists are now expecting the eurozone economy to expand at 0.3% in the third

quarter, bringing to an end Europe's worst recession since World War II.

However with unemployment rising and consumer prices falling at the fastest pace on record, the road to recovery will not be smooth.

Data releases tended to support the idea that the eurozone economy has bottomed

out, with Germany and France unexpectedly returning to growth in the second quarter.

Demand for European exports is also improving just as government rescue packages and lower interest rates begin to support spending at home.

European government bonds

European government GC balances climbed for the fifth consecutive month in August, with sub-10 year German and French government bonds attracting particular demand against lower-rated European government debt. Greek government debt continues to yield well above other European countries, the spread in yield between ten-year Greek bonds (GGB 6 07/19/19 GR0124031650) and the ten-year European Benchmark Bund (DBR3 1/2 07/04/19 DE0001135382) remained over

120 bps ending August 4 bps wider.

Last month's gilt specials fell back to GC. The Bank of England announced an extension of the Asset Purchase Facility (APF) by a further GBP50 billion over the next three months to GBP175 billion, while also expanding the programme to include secured commercial paper.

The restriction of supply caused by the APF has until now helped generate genuine market shortage's of certain issues,

creating specials in this market. Concerned with the negative impact to regular market functions the Bank also announced that gilts purchased through the APF would be made available through the Debt Management Office's Standing Repo Facility on a one-week term basis, effectively mitigating future gilt specials.

European equities

Balances

Balances in August were slightly down compared to July, despite the rally in the markets. This was due to the quieter holiday period.

News

As the economies of various countries maintain their recovery momentum, we are beginning to see a rethink on short-selling restrictions. In August, the Italian Securities and Exchange Commission announced its decision to revoke the restrictions on short sales on the Italian regulated markets. However, some countries have maintained their short-selling restrictions and there are some calls for a permanent regime in Europe.

Europe's Dow Jones Stoxx 600 fell 0.6% on the last day of the month, reducing its

monthly advance to 4.9%. The rally has driven the price-earnings ratio for the index up to 48.6, the highest level since June 2003.

The index has rallied 49% since 9 March as the German and French economies unexpectedly expanded and earnings at companies from Goldman Sachs Group Inc. to Roche Holdings AG spurred speculation that the worst of the global recession was over.⁴

European consumer prices dropped less than economists forecast in August as the economy recovered from the deepest slump in six decades. Prices in the 16-member euro region fell 0.2% from the year-earlier month after declining a record 0.7% in July, the European Union statistics office in Luxembourg announced. Economists predicted a 0.3%

decrease, according to the median of 36 estimates in a Bloomberg survey.⁵

Active stocks

- Immofinanz (IIA AV)
- Sacyr Vallehermoso (SYV SM)
- Banco De Sabadell (SAB SM)
- Swedbank (SWEDA SS)
- Amer Sports (AMEAS FH)
- AIG (AIG US)
- Heritage Oil (HOIL LN)
- British Airways (BAY LN)
- National Express (NEX LN)
- Stagecoach (SGC LN)
- Thomas Cook (TCG LN)

⁴ www.bloomberg.com, accessed on 31 August 2009.

⁵ www.bloomberg.com, accessed on 31 August 2009.

Asia-Pacific equities

The overall balance is up over 25% as Australian dividend season arrived. New Zealand balance jumped over 600% and Australia balance increased over 100%.

Japanese balance dropped slightly over 4% as rebalance before the September dividend season. The IMF approved a General Special Drawing Rights (SDR) allocation and separately approved a special one-time allocation of SDRs, which together would supplement central banks' FX reserves. In Asia, the biggest beneficiaries will be countries whose FX reserves will be supplemented the most: Fiji, Sri Lanka, Pakistan and Mongolia.

China/Hong Kong

The external environment is becoming friendlier to rebound in trade. Property investment is gaining footing, while housing supply remains relatively low. Liquidity remains abundant and unemployment worries are easing. In July, China's total trade volume expanded by 22%, much more than the typical summer. China is geared to benefit from a fast recovery in the US. The Hong Kong government announced a tentative schedule of government bond issuance for 9 September to 10 February 2009. The first issuance will kick-start the HKD100 billion government bond

programme planned over the next 5 to 10 years.

Korea

Consumer confidence rose to an almost seven-year high in July, likely helped by the accommodative monetary and fiscal policy and strong rally in the financial markets. Ample liquidity and low interest rates have supported the revival of mortgage lending and housing prices. Service-industry production rose 1.7%, with impressive gains in real-estate services.

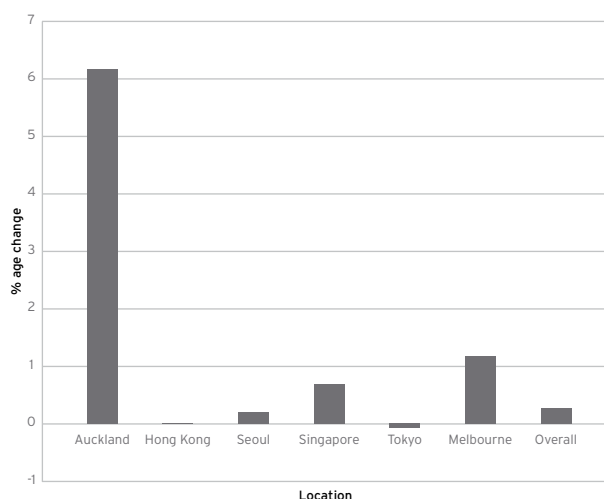
Taiwan

Typhoon Morakot caused heavy rains and mudslides in the mountains and heavy casualties in southern Taiwan. This is likely the most severe damage since the 921 earthquake a decade ago. But the damage to nominal GDP ratio is likely less than 0.1%. Both M1A and M1B continued to accelerate on a booming equity rally and larger capital inflow. But M1B growth is peaking as the CBC strengthened its open market operation to absorb more liquidity from banks in August.

Tight stocks across the region

- B28Q941: ALIBABA.COM
- 6617794: AXA ASIA PACIFIC
- B018L76: China Shipping
- 6215035: COMMONWEALTH BANK
- B1VNYN6: COUNTRY GARDEN
- 6211679: Doosan Heavy
- 6497071: Hanjin Shipping
- 6450267: HYNIX SEMICONDUCTOR
- 6450267: HYNIX SEMICONDUCTOR
- 6490928: KIA MOTORS
- 6600879: MAANSHAN IRON&STEEL
- 6628859: NEPTUNE ORIENT
- 6715740: QBE INS
- B1VT035: YANGZIJANG SHIPPING

On-loan balances from July to August 2009



For further information, please contact your Citi representative.

Contacts



USA, New York

Laurie Zeppieri

Tel: +1 212 657 1075

Email: laurie.zeppieri@citi.com



Europe, London

Brian Staunton

Tel: +44 (0) 20 7500 5411

Email: brian.staunton@citi.com



Asia, Hong Kong

Larry Komo

Tel: +65 6328 5377

Email: lawrence.komo@citi.com

Global Transaction Services
www.transactionservices.citi.com

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