

KING & SHAXSON

UK Break-Evens look a tempting buy.

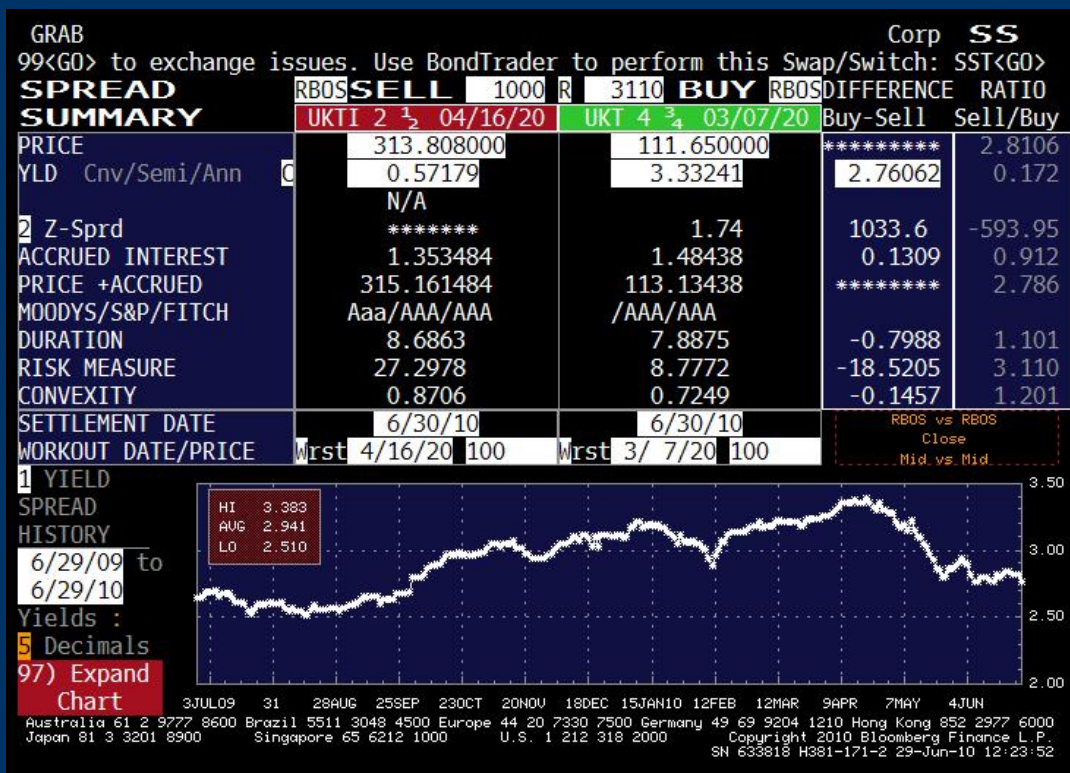
The latest UK RPI figure was rather disconcerting at 5.1%. In addition, we had the expected rise in VAT to 20% in the Budget. Is Mervyn King being a little too relaxed?

As we can see from the break-even graph below, the market is not reflecting any major inflationary pressure. On the other hand, break-evens may well be where they are due to factors other than anything to do with inflation. We have been going through some jittery times and the outperformance by conventional gilts may just reflect the flight to quality. Those seeking safe havens would not necessarily choose index linked bonds for that purpose. Recent data from the US has meant worries for continued global growth and there are continuing concerns in Europe. There have also been increasing calls of deflation. Should we be buying UK break-evens at these levels?

With equity markets continuing to move south and with investors creeping back into their safe haven, risk aversion shells, we feel that a better opportunity awaits us. We would suggest that a return to a break-even of 2.5%, as seen in the graph below of the UK 10 year would be the level to target. We feel that with RPI at 5.1% we would need to see an extended period close to 2% or below in order to bring the average over the next 10 years down to 2.50% . That will take some doing.

US 10-year BEIRs at 1.6% and particularly the French 10-year at 1.77% are also looking very cheap. We again suggest that these levels be watched carefully to give us the opportunity of exploiting any spike down.

UK 10 Year Break-Even



Source: Bloomberg

	UK		US		FR		FR <i>e</i>	IT		SWE		CAN	AUS	NZ
	10Y	30Y	10Y	30Y	10Y	30Y	10Y	10Y	30Y	5Y	30Y	30Y	5Y	7Y
IL BOND	2.5%20	2%35	2.125%19	3.375%32	1.0%17	3.15%32	1.6%15	2.1%17	2.35%35	3.5%15	3.5%28	3%36	4%15	4.5%16
REAL YIELD	0.57	0.86	0.99	1.70	0.67	1.49	0.56	2.26	2.46	0.74	1.32	1.41	2.23	2.53
RPV/CPI	5.10	5.10	2.00	2.00	1.60	1.60	1.50	1.50	1.50	1.20	1.20	1.40	2.90	0.00
TOTAL RETURN	5.67	5.96	2.99	3.70	2.27	3.09	2.06	3.76	3.96	1.94	2.52	2.81	5.13	2.53
12MTH HEDGE			0.00	0.00	0.28	0.28	0.28	0.28	0.28	-0.20	-0.20	-0.47	-4.28	-3.18
TOT.RET. £	5.67	5.96	2.99	3.70	2.55	3.37	2.34	4.04	4.24	1.74	2.32	2.34	0.85	-0.65
CONV BOND	4T20	4.25%36	2.75%19	5.375%31	3.75%17	5.75%32	5%16	5.25%17	5%34	3.75%17		5%37	6.25%15	6%17
YIELD	3.38	4.24	2.84	3.83	2.44	3.65	2.29	3.64	5.03	2.38		3.70	4.78	5.22
SIMPLE BEIR	2.81	3.38	1.85	2.13	1.77	2.16	1.73	1.38	2.57	1.65		2.30	2.55	2.69

Note : All yields have been annualised.

The information used here is obtained from sources that we consider to be reliable but its accuracy and completeness cannot be guaranteed. The opinions and conclusions contained are those of King & Shaxson Limited. ("K&S"), and are subject to change without notice. No responsibility is taken for any losses, including any consequential loss, which may be incurred by acting upon such recommendations or information.

Whilst all reasonable care has been taken to ensure that the facts stated herein are accurate and that the forecasts opinions and expectations contained herein are fair and reasonable, neither the author nor K&S has verified the information contained herein and accordingly none of the author, K&S nor any of their respective directors, officers or employees makes any representation or warranty, express or implied as to the accuracy or completeness of the information or opinions contained herein and shall not be in any way responsible or liable for the contents hereof and no reliance should be placed on the accuracy, fairness or completeness of the information contained in this document. No person accepts any liability whatsoever for any loss howsoever arising from any use of this document or its contents or otherwise arising in connection therewith. Nothing in this paragraph shall exclude liability for any representations or warranties made fraudulently. The material does not attempt to describe all the economic, political, competitive and other factors that underlie any estimates, forecasts, or opinions, or potential changes that could affect the assumptions on which these estimates, forecasts and opinions are based. K&S makes no representation that the information is current. In particular, but without limiting the preceding sentence, statements of fact or opinion regarding securities, investments, financial products, companies, markets, territories or particular circumstances may not be up-to-date or may not represent the current opinion of K&S.

Any opinions, forecasts or estimates herein constitute a judgment as at the date of this report. There can be no assurance that future results or events will be consistent with any such opinions, forecasts or estimates. This information is subject to change without notice. It may be incomplete or condensed and it may not contain all material information concerning the Company.

This document does not constitute or form part of and should not be construed as any offer for sale or purchase of (or solicitation of or invitation to make any offer to buy or sell) any securities nor shall it or any part of it form the basis of or be relied on in connection with any contract or commitment whatsoever.

The information contained in this transmission is legally privileged and confidential information intended only for the use of the individual or entity named above. If the reader of this message is not the intended recipient you are hereby notified that any dissemination, distribution or copy of this facsimile or any parts of it is strictly prohibited. If you have received this facsimile in error, please notify us immediately by telephone +44 (0)20 7426 5950 and speak to Compliance).

King & Shaxson Capital Limited Reg. No. 2863591 and King & Shaxson Limited Reg. No. 869780, members of the London Stock Exchange, and King & Shaxson Asset Management Limited Reg. No. 3870667. The Registered Office for all companies is 6th Floor, Candlewick House, 120 Cannon Street, London, EC4N 6AS. All companies are registered in England and are part of the PhillipCapital Group.

King & Shaxson Capital Limited (FSA Reg. No. 169760), King & Shaxson Limited (FSA Reg. No. 179213), and King & Shaxson Asset Management Limited (FSA Reg. No. 193698) are Authorised and Regulated by the Financial Services Authority, 25 The North Colonnade, Canary Wharf, London E14 5HS.