

FX Briefing

15 May 2009

Highlights

- Euro area GDP plummets in the first quarter
- Chinese exports indicate ongoing weakness in world trade
- Q1 GDP data makes further downward revisions to growth forecasts necessary

Euro rally stopped by growth fears

This week, stock markets once again proved to be a reliable risk barometer. At the beginning of the week, risk appetite was still high, but this changed in the second half of the week when stock prices turned, showing that market participants had become more cautious again. Accordingly, higher yielding currencies were sold, and financing currencies benefited: The yen rose not only against the dollar but also against most other currencies. EUR-USD dropped from a peak of 1.3722 in the middle of the week (close to its 3-month high) to 1.3550, and most emerging market currencies also suffered losses.

Risk aversion rose again because after a number of favourable results, several economic indicators came in worse than expected. This started on Tuesday with Chinese export figures – the first to be released for April. After the relatively favourable results in March, markets had expected the drop to be less pronounced again in April, indicating a stabilization in world trade. But then the figures showed that total Chinese exports had fallen faster again – by almost 23 % year-on-year.

This does not bode well for the April figures of other major export countries. Therefore, foreign demand could remain a drag on growth in the second quarter. The figures for German steel production are pointing in the same direction: Output fell to fresh record lows in April. This dampened rising hopes of a recovery which had been supporting stock markets for weeks.

Moreover, production figures in the other major European countries were much worse than in Germany. As a result, total production in the eurozone was lower than market participants had expected. So it looks as though the second quarter is off to a bad start, which means that GDP will very probably shrink further.

First quarter GDP figures for the EMU have confirmed the expected decline in the first quarter. Germany was hit particularly hard with –3.8 % qoq. Even if the German economy stagnated in the remaining three quarters, the minus for 2009 would be close to 6 %. Bundesbank president Axel Weber is not expecting GDP growth rates to turn positive this year. We are forecasting a further decline.

In the euro area, the extent of the decline in GDP was less pronounced, but even so the drop in the first quarter would mean a minus of almost 4% for the entire year if GDP was to stagnate from now on. In the latest ECB Monthly Bulletin, the professional forecasters have assumed a decline of 3.4% for the euro area in 2009, but given the result for the first quarter, this appears too “optimistic”. Therefore, the ECB forecasts will probably have to be revised down further. On the bond markets this led to a lot of speculation in the past few days that interest rates would fall, which helped to weaken the euro in the second half of the week.

The US figures on the other hand were mixed. Given the trade and inventory data, first quarter

growth looks set for a significant upward revision. However, retail sales were on the weak side and initial jobless claims indicated an ongoing deterioration in the jobs market.

Next week, markets are going to focus on the sentiment indicators for May: Will the upward

trend of the past two months have continued? If it has not, growth fears will increase again. In this case, EUR-USD is likely to trade at the lower end of the 1.37 to 1.29 range that has been intact since the middle of March.

Uwe Angenendt +49 69 718-3648

Key indicators and important events

Country	Indicator / Event	Release date	Forecast (in % mom/yoy)	Prev. period (in % mom/yoy)	Comments
GE	ZEW economic sent. / May	19/5	33.0	13.0	
UK	BoE minutes of 6-7 May	20/5			
US	FOMC minutes of 29 Apr	20/5			
JP	GDP / Q1	20/5	-18.0	-12.7	annualised qoq
GE	PMI manufacturing / May	21/5	40.4	35.4	
EMU	PMI manufacturing / May	21/5	40.8	36.7	
US	Leading indicators / Apr	21/5	0.8	-0.3	mom
US	Philadelphia Fed index / May	21/5	-17.0	-24.4	
JP	BoJ monetary policy meeting	22/5	0.10	0.10	

Money and foreign exchange market quotations

	Spot vs. EUR	Change vs. EUR	Interbank offered rates		
	15/05/09	in % week-on-week	1 month	3 months	6 months
EUR	-	-	0.82	1.25	1.45
USD	1.3553	-1.1	0.33	0.83	1.36
JPY	128.79	3.4	0.26	0.53	0.72
GBP	0.8933	-0.3	0.74	1.36	1.57
CHF	1.5029	0.7	0.20	0.40	0.54
SEK	10.6718	-1.3	0.75	0.96	1.28
PLN	4.4946	-3.1	3.94	4.52	4.63
CZK	26.994	-1.0	2.05	2.50	2.60
CAD	1.5923	-2.3	0.40	0.80	1.20
AUD	1.7961	-1.6	3.34	3.53	3.78
NZD	2.2983	-2.1	2.96	3.20	3.51
SGD	1.9885	-1.2	0.80	0.47	0.56
ZAR	11.6657	-3.9	9.00	8.50	8.50

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