

## FX Briefing

19 June 2009

### Highlights

- SNB wants to prevent appreciation of franc, confirms willingness to intervene
- FOMC will try to dampen interest rate hike expectations

### US dollar: changing patterns

In the course of the last two weeks, the US currency has firmed somewhat. EUR-USD was still around 1.42 in the first week in June. After having fallen below 1.38 for a time, the euro is now back at around 1.39 again. Like the euro, most major currencies lost ground against the dollar, particularly the Swedish krona, the zloty and the Canadian dollar. USD-JPY climbed over 98 temporarily, but relinquished its gains at the beginning of the week. It is currently around 96, as it was in the first week in June.

At its bi-annual media conference, the Swiss National Bank confirmed that it would maintain its very expansive monetary policy stance and that it was willing to prevent the appreciation of the Swiss franc against the euro. However, the remark that there was no clearly defined intervention level seems to have prompted the markets to test EUR-CHF below the 1.50 level. Reportedly, this led to intervention later that day in support of the euro. At any rate, it recovered to around 1.51 again towards the end of the week. The Canadian central bank has also intervened during the last few days – albeit only verbally – to prevent the Canadian dollar from strengthening. Moreover, the BoC governor confirmed the bank's intention to keep interest rates at 0.25% until the middle of 2010, and even hinted at the possibility of additional quantitative easing measures.

#### USD: Between interest rate rise expectations and crisis fears

Market reactions in the forex market are not following a set pattern at the moment. On the release of the US labour market report for May,

which indicated that the pace of job losses was slowing significantly, the US currency firmed. This is a sign that things are getting back to normal: the slight improvement in the labour market figures fuelled speculation that the Fed could start to raise interest rates sooner than expected – possibly even as early as 2009. The yield on 2-year T-notes shot up from below 1.00% to over 1.30%, even rising over 1.40% for a short time. Furthermore, the interest rate disadvantage to equivalent euro papers narrowed by about 25 points, which would normally serve to strengthen the dollar.

At the beginning of this week, however, economic optimism began to wane. After having risen the previous two months, the New York Empire Manufacturing Index dropped from -4.5 to -9.4 in June; US industrial production fell again in May, by 1.1%, and is thus heading for a contraction of 3% or more in the current quarter; moreover, weak housing starts and building permits show that residential construction, unlike existing homes transactions, has not yet bottomed out. In this environment, equity markets, which had not gone up since the beginning of June as it is, began to tumble. The bond markets regained lost ground. And how did the dollar react? The greenback continued to strengthen. The movement here was clearly following the “safe haven” pattern again: when the crisis seems to be escalating, market participants become risk-averse and flock into the dollar.

The anxious mood lifted somewhat after it was reported on Thursday that the Philly Fed Index had surged to just below zero (-2.2 from -22.6).

Some market participants also saw the decline in continuing claims as a good sign, even though it is not clear whether it signified an increase in employment or merely that less people had a right to claim unemployment benefit.

Uncertainty is still rife, however; within the space of a few days, the markets alternate between diametrically opposed scenarios. The Federal Open Market Committee's regular meeting is scheduled for next Wednesday. There are not expected to be any announcements on monetary policy measures. The Fed will leave interest rates on hold and continue with its quantitative measures. Markets will be focusing more on the statement, particularly with regard to the longer-term interest rate outlook. We are expecting the Fed to confirm the signs that the economic downturn is slowing and to state that things are also improving in financial markets. However, the emphasis will probably be on allaying fears of inflation rising and interest rates being raised accordingly in the near future, in particular by pointing out the extremely low level of capacity utilisation. The gist of the last statement is likely to be reiterated, i.e. that given the economic situation,

exceptionally low interest rates are justified for some time to come.

It is very hard to predict how forex market players will react to this message. In normal circumstances, a downward correction of interest rate expectations would have a negative impact on the dollar. The reaction will largely depend on whether a mood of economic scepticism or optimism predominates in the markets.

The US economic indicators at the beginning next week are not likely to shed much light on the way things are going. Durable goods orders will probably have declined in May, whereas home sales are expected to have increased, partly as a result of tax incentives. In Europe, the monthly series of sentiment indicators will be published, including the ifo business climate index for June, French and Italian national business climate indices, and the preliminary purchasing manager indices. They will probably have improved, but are not likely to raise any great hopes of an upswing.

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## Key indicators and important events

Country	Indicator / Event	Release date	Forecast (in % mom/yoy)	Prev. period (in % mom/yoy)	Comments
GE	Ifo business climate / Jun	22/6	85.0	84.2	
GE	GfK consumer confid. / Jul	23/6	2.5	2.5	
GE	PMI manufacturing/ Jun	23/6	41.6	39.6	
FR	Business confidence / Jun	23/6	74	72	
US	FOMC monetary policy	24/6	0.0-0.25	0.0-0.25	
US	Durable goods orders / May	24/6	-1.3	1.7	mom
IT	Business confidence / Jun	25/6	70.4	68.7	
EMU	Industrial new orders / Apr	25/6	0.0 / -31.9	-0.6 / -31.3	
GE	Consumer price index / Jun	26/6	0.3 / 0.1	-0.1 / 0.0	
US	PCE core deflator / May	26/6	0.1 / 1.8	0.3 / 1.9	

## Money and foreign exchange market quotations

	Spot vs. EUR	Change vs. EUR	Interbank offered rates		
	19/06/09	in % week-on-week	1 month	3 months	6 months
EUR	-	-	0.93	1.27	1.48
USD	1.3938	0.7	0.32	0.63	1.20
JPY	135.02	2.1	0.24	0.51	0.71
GBP	0.8478	0.5	0.67	1.26	1.47
CHF	1.5116	-0.1	0.20	0.40	0.54
SEK	10.9444	-1.9	0.76	0.99	1.32
PLN	4.5149	-0.9	3.95	4.64	4.79
CZK	26.400	1.1	1.85	2.22	2.41
CAD	1.5703	-0.1	0.33	0.63	1.06
AUD	1.7295	-0.3	3.26	3.50	3.79
NZD	2.1737	0.7	2.89	3.14	3.31
SGD	2.0280	0.5	0.34	0.44	0.56
ZAR	11.3100	-0.6	8.25	8.00	8.25

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