

FX Briefing

23 October 2009

Highlights

- EUR-USD climbs over 1.50
- Pound plunges on disappointing Q3 growth
- Intervention pushes up Asian currency reserves

Dollar weakness persists

Towards the middle of the week, EUR-USD breached the 1.50 level for the first time since August 2008. The final push came from US equity markets, which reacted very positively to Morgan Stanley's quarterly earnings in particular. All in all, however, the euro only made moderate gains: towards the end of the week, the common European currency was around 1.5040, about 1½ US cents higher than a week ago.

On the macroeconomic side, there was little impetus. Most of the few US data released did not fully come up to expectations. Housing starts and building permits did not improve markedly in September, and the number of initial jobless claims rose slightly in the middle of October. The European indicators were more upbeat. Most surveys for the euro area went up somewhat. According to preliminary figures, the eurozone purchasing managers' index for the manufacturing sector rose over the expansion threshold of 50 again for the first time. The ifo business climate index also improved further in October, from 91.3 to 91.9. The French figures were even better. General business confidence increased from 86 to 89. It is striking that companies are now seeing the outlook for production in their own companies as almost neutral again. Furthermore, consumer spending rose by over 2% in September; the third quarter therefore remained more or less stable.

Sterling's antics

The pound sterling cavorted around again this week. The pound's recovery, which had begun

last week after remarks made by BoE deputy governor Paul Fisher, received additional support from the Bank of England's minutes. The minutes of the meeting at the beginning of October revealed no intention of extending the asset purchase programme on the one hand, and on the other, buoyed expectations that the UK economy could revert to positive growth rates in the third quarter. Against this backdrop, the euro dropped to about 90 pence.

The forex market's reaction to the release of the preliminary UK GDP data for the third quarter was correspondingly harsh. The figures published on Friday show a further contraction in real GDP of 0.4% compared to the previous quarter, only marginally better than the -0.6% in Q2. The estimate shows that growth remained negative in nearly all sectors, including the financial services sector. After these figures, EUR-GBP rose to almost 0.92. Cable fell by around 3 cents to below 1.64.

Political resistance to appreciation

The downside to dollar weakness is the appreciation of most major currencies with the exception of the yuan and a few other currencies which are pegged to the dollar. Growth prospects in the Asian growth regions and also in commodity countries are much better than in most industrialised countries. The Asian countries are benefiting from robust growth in China; other countries such as Brazil, South Africa, Australia, Norway and Canada, are relying on commodity prices recovering. This, coupled with international in-

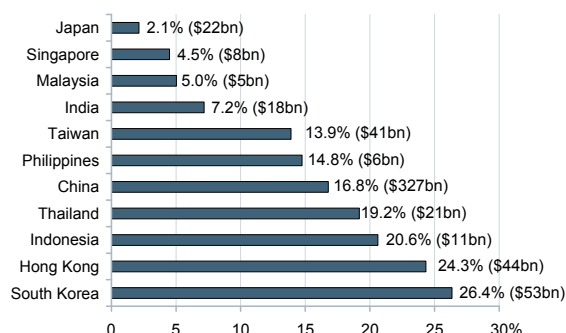
vestors' growing risk appetite, is leading to high capital inflows into these regions and to a significant appreciation of their currencies. Thus the euro has risen by almost 8% since the beginning of this year; but the real has appreciated by 35%, the Australian dollar by 32%, the South African rand by 27% and the Norwegian krone by 26%. Even the Canadian dollar has gained about 16% against the US currency.

Meanwhile, however, there is increasing resistance to appreciation pressure. This week, the Brazilian government introduced a transaction tax on foreign equity purchases, which could put pressure on the real, at least in the short term. The Canadian central bank president hinted at possible measures to weaken the Canadian dollar. And many Asian monetary authorities are resorting to direct intervention to slow down the appreciation of their currencies.

The chart below, which shows the development of foreign currency reserves in leading Asian countries since the end of 2008, gives some insight into these activities. It is clear that the reserves in most of the countries have soared.

South Korea posted the biggest increase – 26%, followed by Hong Kong (24%) and Thailand and Indonesia (about 20% respectively). And China and Taiwan also gained 17 and 14% respectively. In absolute terms, China is the winner with an increase of \$327bn; but Korea is doing very well too with over \$50bn.

Rise in foreign currency reserves in selected Asian countries since end of 2008



Source: Bloomberg, own calculations

Stephan Rieke +49 69 718-4114

Key indicators and important events

Country	Indicator / Event	Release date	Forecast (in % mom/yoy)	Prev. period (in % mom/yoy)	Comments
GE	GfK consumer confid. / Nov	26/10	4.3	4.3	
EMU	Money supply M3 / Sep	27/10	1.9	2.5	yoy
US	Consumer confidence / Oct	27/10	53.1	53.1	
GE	CPI / Okt	28/10	0.0 / -0.1	-0.4 / -0.3	
GE	Labour market / Oct	29/10			
	>absol. change unempl. sa		+15k	-12k	
	>unemployment rate sa		8.3	8.2	
EMU	Economic sentiment / Oct	29/10	85.5	82.8	
US	GDP / Q3	29/10	3.5	-0.7	annualised qoq
EMU	HICP flash estimate / Oct	30/10	-0.2	-0.3	yoy
US	PCE core deflator / Sep	30/10	0.2 / 1.3	0.1 / 1.3	
US	Chicago PMI / Oct	30/10	49.0	46.1	
JP	BoJ interest rate decision	30/10	0.10	0.10	+ Outlook Report

Money and foreign exchange market quotations

	Spot vs. EUR	Change vs. EUR	Interbank offered rates		
	23/10/09	in % week-on-week	1 month	3 months	6 months
EUR	–	–	0.39	0.69	1.01
USD	1.5040	-0.9	0.24	0.28	0.58
JPY	137.86	-1.6	0.16	0.33	0.53
GBP	0.9170	-0.1	0.51	0.60	0.81
CHF	1.5133	0.4	0.10	0.27	0.39
SEK	10.2495	1.3	0.35	0.50	0.78
PLN	4.1813	0.7	3.50	4.18	4.31
CZK	25.946	-0.8	1.55	1.86	2.12
CAD	1.5837	-2.8	0.30	0.50	0.88
AUD	1.6275	-0.6	3.61	3.93	4.50
NZD	1.9907	0.7	2.97	3.10	3.49
SGD	2.0954	-0.8	0.73	0.55	0.63
ZAR	11.2154	-2.2	7.50	7.60	7.65

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