

4 November, 2009

Forex News

USD CHF JPY

Dollar short-term strengthening

Swiss franc stable, thanks to SNB

Yen has rivals for carry trade

US dollar

EURUSD exceeded the 1.5 mark in the past few weeks, but only temporarily – and the development was followed by a significant countermovement as well. Profit-taking played an important part, but the slump on the stock exchanges was the decisive factor. It pushed up uncertainty, which in turn boosted the attractiveness of the US dollar. We cannot make any meaningful estimates as to when the slump on the equity markets will be over. However, we do consider the most recent appreciation of the dollar a temporary one, as the negative factors will prevail for this currency in the medium term.

We therefore stick to our opinion that the dollar will continue to fall in the coming months; however, an increasing number of signals would indicate that this development may be characterised by high levels of volatility. The markets are well aware of the burdening factors for the US dollar, such as the massive expansion of public debt and the extreme course of the central bank. This has led to relatively high positions betting on a weaker dollar. In addition, the low interest rates have boosted the attractiveness of the dollar as financing currency for carry trades. Even if there are no hard facts available that would support this notion, a number of statements are pointing in that direction. This means the market is rife with speculations against the dollar, and consequently with nervousness about any unwanted movement of the currency. The high manoeuvring mass would suggest that the short-term fluctuations of the dollar exchange rate will intensify. However, these movements will take place around the medium-term downward trend of the dollar and are not tantamount to its end.

Swiss franc

The Swiss National Bank is sticking to the counteracting of an excessively strong franc. The intraday movements of the exchange rate often yield the same picture: a recurrent strengthening trend is interrupted by a jump of the franc weakening, pointing to an intervention of the SNB. This speaks in favor of continued strengthening pressure on the franc, which is stabilized via SNB interventions. We expect a similar picture in the future too. When exactly the interest rate differential could support a weakening of the franc again is unclear. This depends both on the timing of future rate hikes abroad and on the availability of credit in francs, as the rate differential cannot be taken advantage of otherwise. The ongoing strengthening pressure does not seem to abate anytime soon, which is why we expect a sideways movement of the franc in the future too.

Japanese yen

The yen has strengthened up to USDJPY 89 once more and quotes currently close to USDJPY 90. Traditionally, the yen has been a popular currency for carry trades, thanks to the low interest rates: a loan in yen would be invested in higher-yielding currencies such as the Australian or New Zealand dollar (or even in the US equity markets). This implied a weakening of the yen: the borrowed yen would be sold against another currency for investing. These carry trades seem to be en vogue again, especially since the RBA hiked rates. The new feature is that the dollar interest rate is currently lower than the yen one, which is why the USD is considered a carry trade funding currency as well. This implies – in addition to the negative interest rate differential – that the weakening pressures on the yen are less strong than in the past (see Currency models USDJPY), which supports the yen.

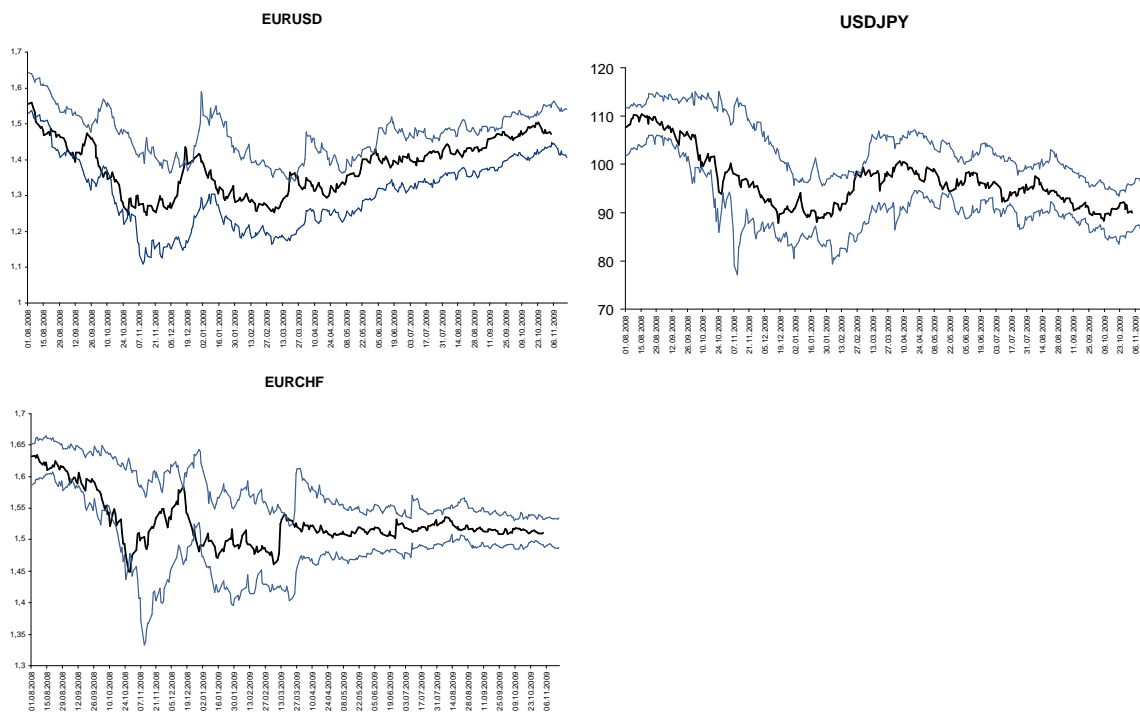
At their last meeting, the BoJ has – like the Fed earlier - decided to withdraw from additional purchase and credit-facility programs. Financing conditions for firms on the financial markets seem to have improved sufficiently to finish the purchase of CP and corporate bonds at the end of 2009. The additional credit facility for firms will be maintained until the end of the fiscal year in March 2010. The deposit facility will be continued as well, in order to maintain sufficient liquidity in the system. Thus, additional measures in Japan are handled simultaneously to the ones in the US. Interest rates should remain low for a longer time, though, as the bank forecasts negative inflation rates for the next three years. Thus, we think that only rate hikes (or withdrawal of liquidity by the Fed) in the US (but not in Japan) will exert weakening pressures on the yen. In the short term, the yen could still strengthen further; we expect quite wide oscillations around USDJPY 90. Together with the EURUSD forecast, this implies a EURJPY exchange rate close to 139.

Bandwidths for next two weeks

The following bandwidths were prepared based on market estimates of future exchange rate risks. Starting with today's exchange rate, an upper and a lower limit can be estimated for the exchange rate two weeks from now. This covers the most likely scenarios.

We have compared the forecasted bandwidth with the actual exchange rate in a chart.

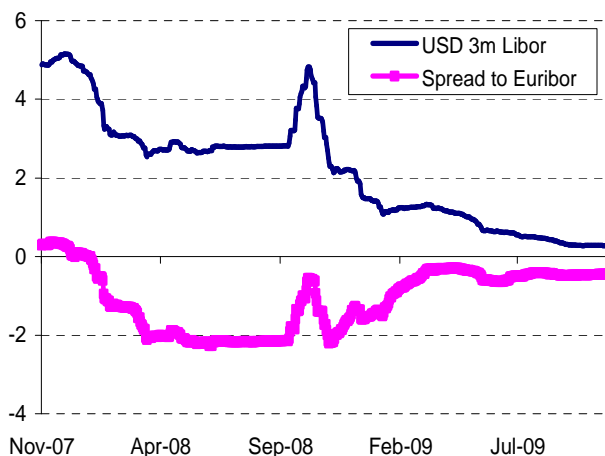
The markets *expect* much wider fluctuations in the future than seen in the past as well, although we have noticed a decline most recently. Thus, the forecasting risk has increased.



EURUSD



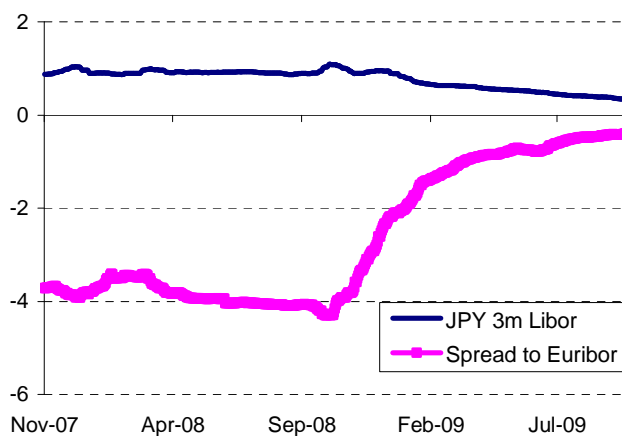
3m US Libor and Spread to Euribor



EURJPY



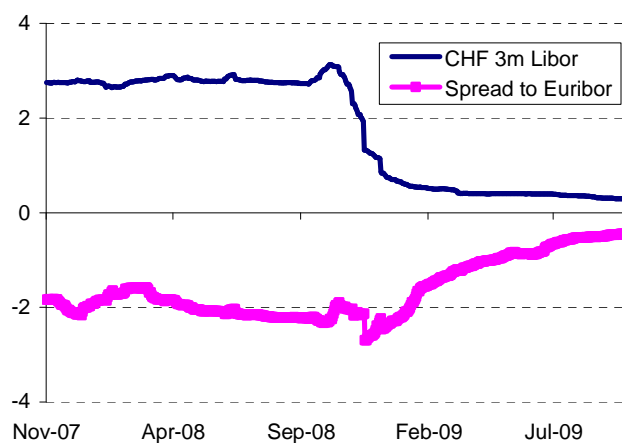
3m JPY Libor and Spread to Euribor



EURCHF



3m CHF Libor and Spread to Euribor



Forecasts: Exchange Rates

End of Month	Current	Dec. 09	Mar. 10	Jun. 10	Sep. 10
EURUSD	1.4761	1.55	1.53	1.55	1.50
EURJPY	133.77	139.5	137.7	142.6	142.5
USDJPY	90.63	90.0	90.0	92.0	95.0
EURCHF	1.51	1.51	1.51	1.51	1.51

Forecasts: 3m interest rates

End of Month	Current	Dec. 09	Mar. 10	Jun. 10	Sep. 10
EURO	0.67	1.00	1.10	1.30	1.60
Japan	0.32	0.30	0.30	0.30	0.30
USA	0.28	0.30	0.40	0.60	0.90
Switzerland	0.26	0.25	0.25	0.25	0.30
Spread vs Euribor	-0.41	-0.75	-0.85	-1.05	-1.30

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Sales	Fixed Income Domestic Sales		+43 (0)5 0100 - 83200
	Treasury Domestic Sales		+43 (0)5 0100 - 84130
	Institutional Sales		+43 (0)5 0100 - 84300
	Corporate Sales		+43 (0)5 0100 - 84100

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