

October 2009

## Month-end Exchange Rates

|         | September 30, 2009 | October 30, 2009 |
|---------|--------------------|------------------|
| EUR/USD | 1.46170            | 1.47545          |
| USD/JPY | 89.535             | 90.52            |
| GBP/USD | 1.59935            | 1.64835          |
| EUR/JPY | 130.8733           | 133.55775        |
| EUR/GBP | 0.91395            | 0.8951           |
| USD/CHF | 1.03765            | 1.02425          |
| USD/CAD | 1.0733             | 1.0772           |
| AUD/USD | 0.88255            | 0.9036           |
| NZD/USD | 0.72340            | 0.7229           |

## Market Commentary – October 2009

USD moved modestly lower vs. EUR during October, continuing the trend established in Q3 where the US currency had already fallen over 4% during the quarter. Generally speaking, risk appetites and global bourses improved throughout the month, although at times this pattern seemed to falter with subsequent strong USD rallies following. With Eurozone showing increasing signs that economic recovery is becoming entrenched and a surprise positive start to the US corporate reporting season from Alcoa; USD negative sentiment gathered pace. There was a brief short lived rally towards month end as risk appetites and global stock markets came under a degree of pressure with the pace of global recovery coming under scrutiny by market participants and analysts. In contrast to the upward trend for EUR vs. USD, however, JPY moved lower against the greenback during October as Japanese domestic economic conditions appear to be stalling with retail sales and consumer demand remaining weak. Intervention is also a stark possibility as the newly appointed government attempts to stamp its authority on maintaining its election pledge to reignite the economic recovery. For the month, USD fell 0.9% vs. EUR, but was up by 1.1% vs. JPY.

Sterling also had a better month against the back-drop of a weaker US currency, moving ahead by over 3%, whilst it was also able to recover modestly from the recent heavy falls vs. EUR, ending the month 2% higher. Partly as a result of a short squeeze, but also on the back of Bank of England MPC meeting minutes suggesting that a consensus had been formed at the last meeting not to increase further the QE measures already weighing heavily on GBP; but instead to hold off for further signs of economic recovery gaining momentum.

Commodity linked currencies, such as CAD and AUD also made strong head way against an ailing USD, as commodity prices rallied on higher risk appetites and general positive outlook for expansionary global demand. AUD was particularly strong during the month as the RBA became the first G20 economy to raise rates, lifting them 25bps to 3.25%. Subsequent minutes showed the central bank is ready to raise rates further, seemingly accepting the consequent AUD strength (*RBA raised rates a further 25bps to 3.5% on November 3<sup>rd</sup>*). Although often showing signs of strength on the back of higher commodity prices, the CAD came under pressure towards the end of the month as the Bank of Canada, in contrast to the RBA, proved more dovish with regards interest rate policy citing concerns about their currency's strength as an overriding factor that could stifle the economic recovery underway, as well as having a negative impact on the current account position. For the month, AUD ended 2.4% higher vs. USD, whilst CAD was approximately 0.3% lower vs. USD.

The month started stronger for the USD as economic data was mixed leading to falling stock markets and lower risk appetites. Manufacturing ISMA and initial claims data proved weaker than forecast, although this was somewhat offset by positive news on the housing front with pending home sales surging ahead 6.4% mom exceeding a 1% forecast.

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Wall Street and other global bourses once more rallied as they digested the economic data coming out of America, concluding that the longer term effects of weaker numbers on the global recovery should be discounted, and thus sending the US currency and JPY lower once more as risk appetites improved. More downward pressure followed the decision by the RBA to raise rates as investors started to question whether the Fed would follow suit in raising rates and tightening policy, although Bernanke was quick to give guidance by stating the Fed would raise rates only once the recovery had gained a firm hold. This left the USD slightly stronger for a time. As stocks continued to move higher in anticipation of healthy banking sector results, USD came under renewed selling. Indeed, Wall St surged and USD fell heavily following better than anticipated numbers from J P Morgan (as well as Intel), amplified by the release of a less than feared fall in retail sales. Towards month end a familiar story emerged that China would further diversify its foreign currency reserves into EUR, GBP and JPY. Downward pressure on USD was somewhat contained by the fact that many market participants are short the US currency and therefore there remains a risk of a short squeeze. In addition, US data was not giving much in the way of direction, leaving the USD treading water. The last day of October did see a surge higher for both USD and JPY as bourses fell sharply following the release of much softer consumer spending data from both US and Germany.

EUR came under pressure at the start of the month with Trichet commenting that disorderly movements in fx markets can have an adverse impact on the economy. Economic data from the Eurozone was also not as encouraging as it had been in Q3 with German retail sales falling 1.5% mom (estimated at +0.1%) and EZ unemployment rate rising 0.1% to 9.6%. The single currency continued to react to mixed economic data and the dwindling fortunes of USD throughout the remainder of October, eventually breaking EURUSD 1.50 towards month end – the first time in 14 months – as Wall St surged higher on strong earnings and USD moved sharply lower. The last week of the month saw a series of more positive economic data releases which in turn helped EUR solidify its gains against USD. In particular, German unemployment fell 26k vs. an estimate of +20K which pushed the unemployment rate down 0.1% to 8.1%; and EZ sentiment reports showed positive signs across the board from consumers to businesses. Only the small USD rally on the last day of October saw a modest pull back, but not enough to leave EUR 0.9% higher vs. USD for the period.

Looking towards the end of the year, several banks are already beginning to square positions leading up to what is traditionally a lower liquidity period due to year end and Christmas holidays. The lower liquidity could lead to more volatile conditions and some unusual price action in certain crosses. Retail sales and consumer demand leading into the last quarter will also play an important part in determining the strength of the economic recovery, although much of the associated data will not be fully disclosed until Q1 2010.

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