

**July 2010**

## Month-end Exchange Rates

	June 30, 2010	July 30, 2010
EUR/USD	1.22490	1.30280
USD/JPY	88.490	86.660
GBP/USD	1.49610	1.56610
EUR/JPY	108.39140	112.90065
EUR/GBP	0.81875	0.83185
USD/CHF	1.07835	1.04625
USD/CAD	1.06265	1.02995
AUD/USD	0.84465	0.90525
NZD/USD	0.68765	0.72435

## Market Commentary – July 2010

USD weakness that started in June gathered pace in July, albeit exasperated by thin holiday affected market conditions. The US currency ended the month weaker against most major crosses with a fall of 6.4%, 2.1% and 4.7% against EUR, JPY and GBP respectively. The month was marked by signs of a slowdown in economic activity in US and improving confidence and sentiment in EZ. The first trading day in July saw EUR appreciate by more than 2% vs. USD as a slew of weaker US economic data was announced – with disappointing data from US pending home sales, manufacturing ISM and initial jobless claims. Indeed, the month continued along similar lines with the end of the month seeing a weaker than forecast US Q2 GDP release, adding to the negative USD tone. In contrast, and further supporting a resurgent EUR were reports that all German banks had performed well in a series of recent stress tests. This was repeated later in the month, as it became clear that the vast majority of banks across the region (and all the major banks that took part) had successfully passed their own stress tests, leading to improved sentiment in the financial system. In addition, and following the recent turmoil in the debt markets following Greece and other peripheral EU countries' fiscal debt problems, debt sales and auctions appeared to be well received by investors and thus repairing confidence once more as well as allaying fears of rating downgrades. EUR could possibly have traded higher; however, upside was limited by growing expectations that austerity measures being introduced by many countries within the European region could curtail economic growth going forward. As well, the Hungarian government continued to resist EU / IMF conditions placed on their austerity measures and Ireland received a rating downgrade despite the improving regional outlook and debt issuance situation described above.

Japanese Yen was also stronger against the USD during July despite S & P rating agency suggesting a possible rating downgrade, which followed the recent election where the ruling government lost its Upper House majority, thereby weakening its powers to pass certain measures aimed at stimulating economic growth, and which the opposition have so far argued against. The usual positive currency effects for JPY from falling global bourses were also present throughout the majority of the month, especially the US markets, where poor economic data also had the effect of putting downward pressure on USD. Towards the end of July, it was evident that the threat (fear) of BoJ / MoF intervention was becoming more prevalent, and that the possibility of quantitative easing measures being introduced was more likely (aimed at both weakening the currency as well as countering deflation). This also coincided with a bout of improving risk appetites, which in turn led to stronger bourses and subsequent JPY weakness. The month ended, however, on a slightly more positive note for JPY as the BoJ stated that it had no "line in the sand" for when it would likely intervene to weaken the currency. This news upstaged some relatively mixed economic data. JPY ended the month on an 8 month high vs. USD as the US Q2 GDP data fell well short of analysts' expectations.

Sterling had another positive month against USD, following its 3% move higher in Q2, whilst it was not as strong as it had been in Q2 vs. EUR, with a modest 1.6% fall against the later during July, having been up 3% the previous quarter.

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Like EUR, GBP started the month on a positive tone as the softer US data took centre stage with USD under pressure rather than GBP exhibiting signs of strength. Sterling then succumbed to its own weaker domestic data as the trade deficit deteriorated unexpectedly with the anticipated rise in exports failing to materialise and imports up solidly. Further GBP pressure followed the release of Q1 current account data which indicated the UK economy had deteriorated more than suggested in earlier preliminary releases. S & P also retained its negative outlook noting that the economic outlook was more pessimistic than previously suggested or that the emergency budget speech had indicated. GDP data showed that the recession had in fact been much deeper than previously held, and the recovery was now much more dependent on Government spending; leading to fears that the planned government fiscal contraction policy would possibly lead to a “double-dip” recession. Better news for GBP emerged from inflation data which showed it was slowing less than anticipated due to higher food and energy prices, and again the currency gained further from stronger fall in UK unemployment than expected. With further weakness in US data, analysts are beginning to suggest this could lead to global slowdown which would be especially bad for the UK’s budget deficit cutting plans recently announced – GBP sold off temporarily vs. USD and EUR as this analysis emerged and Ireland’s recent rapid decline in GDP was cited as a relevant example of how things could evolve for the UK. However, with the release of Q2 UK GDP data towards month end, showing the economy had grown almost twice as fast as had been forecast (+1.1%), and that the UK banks had passed recent stress tests, GBP regained some of the earlier losses, ending July at a 5 month high vs. USD, but succumbed to EUR strength by month end.

Elsewhere, AUD, NZD and CAD all moved higher, building on recent positive momentum. Generally speaking, these currencies have been closely moving in tandem with commodity prices, which in turn have taken their lead from the relative strength of global growth and the associated level of investor risk appetites. As economic data has emerged (especially in US) indicating a positive outlook for the pace of global demand, risk appetites have increased and been translated into higher equity valuations and stronger commodity prices. For AUD in particular which is closely associated with both raw commodity prices such as gold and coal, but equally affected by risk appetite levels (via the carry trade position), July has been a very positive month with AUD appreciating 7.2% vs. USD. Also helping the Australian currency this month has been the resolution by the new PM of the ongoing issue of the proposed mining industry “super tax”. With this now behind them, and interest rates higher in Australia than any other G10 economy, AUD has benefitted from any periods of rising risk appetites. CAD has also benefitted from the improved commodity and risk appetite conditions in July, but has also seen stronger domestic economic data in the first half of the month – strong employment data pushed down unemployment rate, raising expectations for BoC to hike rates. Therefore it came as no real surprise that BoC raised rates by 25bps to 0.75% towards month end accompanied by further signs of underlying strength emerging from commodity exports.

Markets have been very thin in terms of volume throughout July, and we would anticipate this continuing for much of August. Currencies will continue to take direction from the relative strength of underlying economies, with the recent fragility of the US economy especially noteworthy. With expectations for further monetary easing by the US Federal Reserve intensifying, which in turn continues to weigh on US Treasury yields, the recent USD weakness vs. G10 could well continue over this period, with GBP and EUR benefitting the most.

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