



بنك الإمارات دبي الوطني
Emirates NBD

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FX Week

EUR/USD faces 'twin' tests at the start of the month

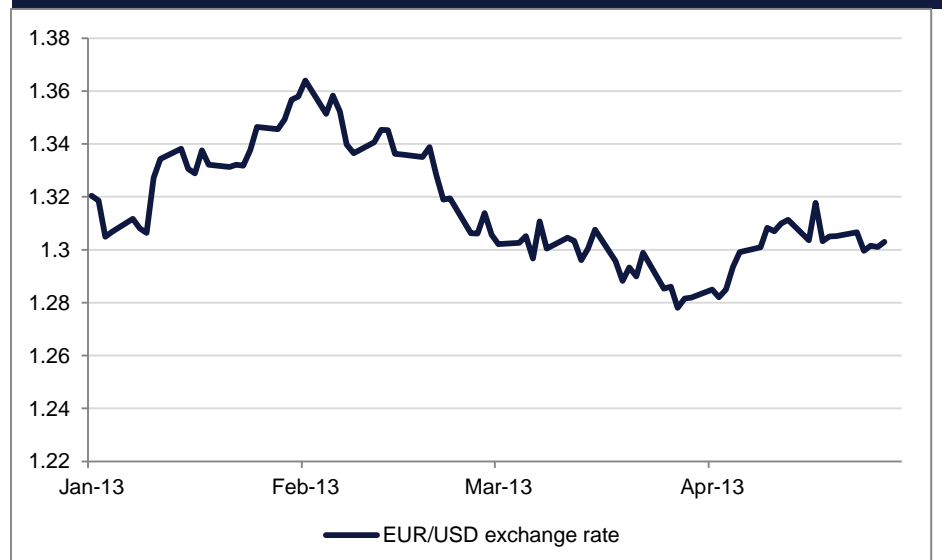
Markets will begin the new month with more than the usual degree of focus on the two key events at the start of any month; namely the ECB meeting on Thursday followed on Friday by the latest US employment data. EUR/USD has fallen into a trading range since early April roughly between 1.30-1.32 as doubts about the US recovery have begun to grow. However, as well as these concerns, the Eurozone's outlook has also darkened, to such an extent that an ECB rate cut now looks almost inevitable in the coming week. Consequently the EUR's bias still appears to be downwards with the greater risk being that it breaks the bottom of its existing trading band in the context of easier ECB monetary policy and amidst new structural risks.

An ECB rate cut appears likely

We have long maintained that the ECB will eventually bow to economic pressures by easing monetary policy further, regardless of the limited benefits this might bestow on a relatively stagnant Eurozone economy. Our forecast since the start of the year has been that the refinancing rate will be cut to 0.50% by the middle of it, premised on the realization that a H2 13 economic recovery will fail to materialize. Now it seems that that moment is approaching, with ECB officials increasingly appearing to acknowledge in recent weeks that more can be done via monetary policy to assist ailing growth. Even the hawkish Bundesbank President Weidmann has intimated as much by saying that interest rates can be reassessed if the economic data changes.

The data does appear to have changed, with slower growth not just afflicting the peripheral nations of the Eurozone but increasingly the core of Germany and France as well. Last week the PMI index for the whole Eurozone fell to 46.5 while Germany's PMI's also fell into contraction territory, matched by weakness of its own IFO index. For the periphery the pain is only getting worse, with unemployment topping 6 million and 3 million respectively in Spain and France. So much so that political voices are increasingly being heard casting doubt on the efficacy of further austerity measures, including from the EU President Manuel Barroso. As such a 25bps interest rate cut is the least that might be expected from the ECB this week, while other steps might also be announced to help unfreeze credit, such as easier collateral requirements at the level of national central banks.

EUR/USD becalmed in April



Source: Bloomberg, Emirates NBD Research

Other cross currents

EUR/USD will not only be influenced by ECB monetary policy, however. Some comfort might be drawn from the restoration of tentative stability in Italy following the appointment of a new Prime Minister, Enrico Letta, at the end of last week, and his formation of a new government over the weekend. Against this, however, has been the news that German Bundesbank is seeking a judicial judgment on the legality of the ECB's Outright Monetary Transactions. These have been widely acclaimed to have helped alleviate pressure on regional bond markets, allowing long term interest rates to decline from last year's highs, even without them having had to be used. While it seems unlikely that this case will succeed in derailing their implementation, the mere uncertainty could be enough to ruffle financial markets ahead of the verdict due in June.

US jobs data also pivotal

Of course, the other factor that arguably matters almost as much to EUR/USD is the outlook for the US economy, with next Friday's jobs data for April providing a critical litmus test of its fortunes. We already know that Q1 GDP, which rose by 2.5% (annualized), was negatively affected by public sector spending cuts in March as a result of the 'sequestration' program. Should the early April data also show the US economy being held back by these USD85bn of monthly spending cuts, then the markets are likely to postpone further their expectations for the ending of the Federal Reserve's Quantitative Easing program, which could further hamper the USD. For the time being the USD index (Bloomberg's DXY index) is holding in around 82.5, but this could be tested if non-farm payrolls disappoint again, as they did in March. It could also extend the period in which the EUR/USD occupies its current trading range.

However, we think that the US economy has more resilience than is currently factored into most estimates, which should see payrolls and growth recover in coming months, restoring the likelihood of a reduction to QE in late 2013, and an end in 2014. The Federal Reserve's FOMC will also meet in the week ahead and it will be interesting to see its take on the current 'soft-patch' being seen. On balance, taking all of the above factors into account we still see the risk being greater of Eurozone disappointment than US, leading us to stick with our 3-month forecast looking for EUR/USD to reach 1.25.

GBP buoyed by GDP

GBP recovered strongly late last week, benefiting from stronger than expected UK Q1 GDP data which rose by 0.3% q/q. As the markets were fearful of a 'triple-dip' recession in Q1, forcing the Bank of England to buy more QE assets, the data provided at least temporary reassurance that this will not happen anytime soon, possibly not until the new Governor Mark Carney takes office in the middle of the year. As demonstrated by the charts on page 6, the speculative FX market is still heavily short of GBP, leaving more scope for the pound to rally if the upcoming PMI activity data for April out this week prove better than expected.

USD/JPY100 still in sight

USD/JPY has again backed off from the 100 level, following gains seen on the back of the G20's failure to criticize Japan for currency manipulation at its summit a week ago. The latest Bank of Japan meeting made no further changes to monetary policy at its latest meeting, after its 'monetary policy revolution' announced at the beginning of the month. However, with the BOJ now forecasting inflation of 1.9% in two years' time, the scale of the challenge it faces remains enormous given that the latest deflation reading of -0.5% y/y. The BOJ also raised its growth forecast to 2.9% this year (March 2013-March 2014), up from 2.3% previously. A heavy Japanese data calendar lies ahead this week although a long weekend will keep things quiet until Tuesday, with holidays again on Friday. PMI activity data, retail sales, unemployment and industrial production will be the highlights, although these may not have much

bearing directly on the JPY, which is probably more dependent on investment flows at the beginning of the new financial year.

CHF softness

The CHF weakened last week towards 1.23 versus the EUR, as the news of the appointment of a new Italian prime minister took some of the upward pressure off the safe-haven franc. In coming days domestic data out of Switzerland may add to the downward pressure on the CHF if it confirms that the Swiss economy remained in contraction territory during April. The latest Swiss KOF leading indicator reading was at least slightly better than expected at 1.02 in April, but the overall outlook depends largely on the Eurozone economy which remains largely stagnant. Worth keeping an eye on is USD/CHF which is moving closer to 0.95, our 1-month forecast. As there is likely to be some renewed downward pressure on the EUR ahead of the ECB meeting on Thursday, keeping EUR/CHF steady, USD/CHF may show more sensitivity to Switzerland's own fundamentals revealing the CHF's true directional trend.

An RBI rate cut awaited

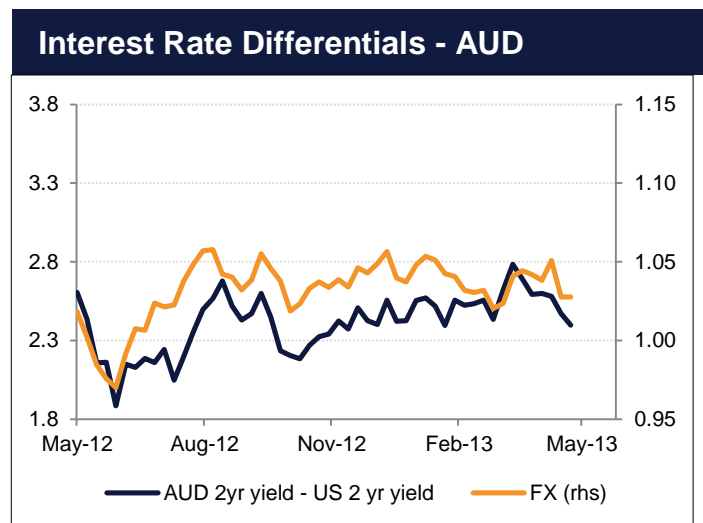
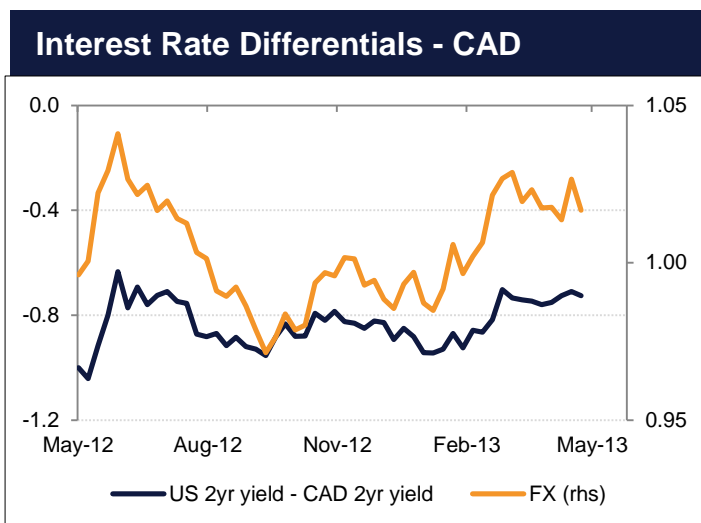
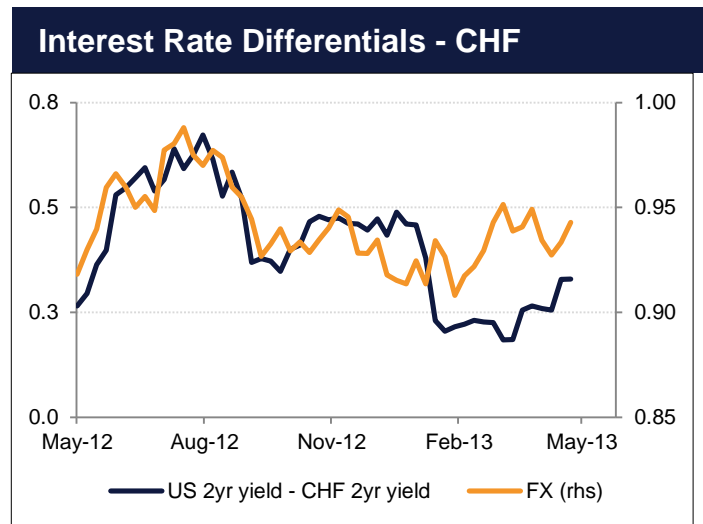
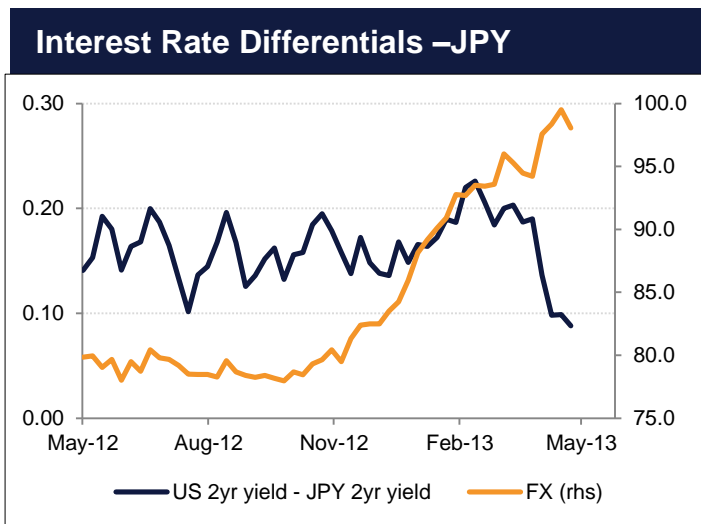
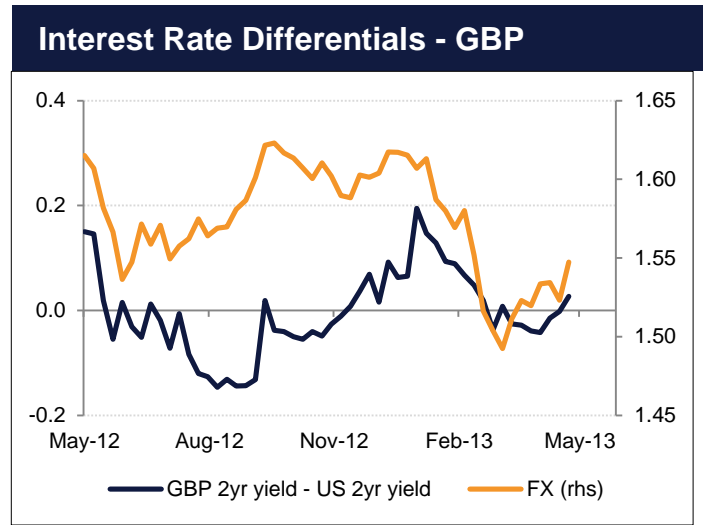
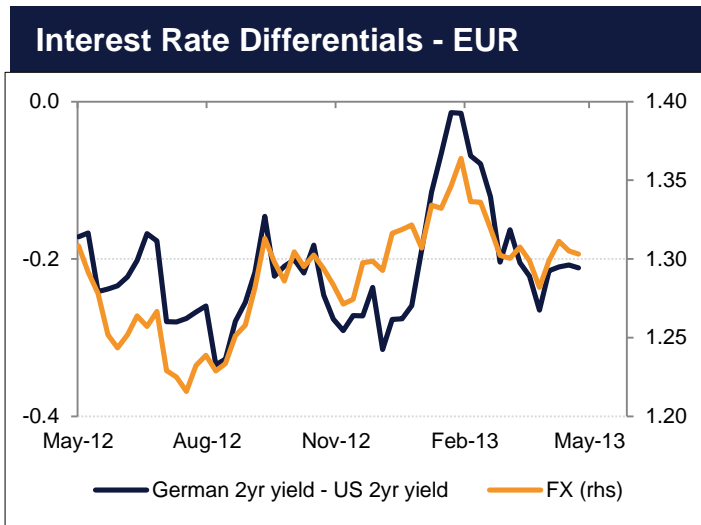
A sharp correction in global commodity prices along with decline in domestic inflationary pressure is believed to have provided enough room for the Reserve Bank of India to reduce repo rate by 25 bps when it meets later this week. Additionally, the Government of India is also considering a move in which its cash holdings with the RBI may be deposited with commercial banks, thereby adding close to INR 1tn liquidity to the system. The INR movements have been range bound in the last month despite expectations of a rate cut being priced in, with the USD's movements weigh on the INR.

FX Forecasts - Major						Forwards		
	Spot 26.04	1M	3M	6M	12M	3M	6M	12M
EUR / USD	1.3030	1.28	1.25	1.20	1.15	1.3038	1.3049	1.3073
USD / JPY	98.05	100.0	103.0	105.0	110.0	98.00	97.92	97.70
USD / CHF	0.9429	0.95	0.98	1.02	1.08	0.9420	0.9408	0.9378
GBP / USD	1.5473	1.48	1.45	1.42	1.45	1.5465	1.5459	1.5454
AUD / USD	1.0276	1.01	0.97	0.94	0.90	1.0207	1.0143	1.0021
USD / CAD	1.0167	1.03	1.05	1.07	1.10	1.0188	1.0209	1.0249
EUR / GBP	0.8419	0.86	0.86	0.85	0.79	0.8429	0.8438	0.8457
EUR / JPY	127.73	128.0	129.0	126.0	126.5	127.73	127.73	127.73
EUR / CHF	1.2276	1.22	1.22	1.22	1.24	1.2272	1.2266	1.2250
FX Forecasts - Emerging						Forwards		
	Spot 26.04	1M	3M	6M	12M	3M	6M	12M
USD / SAR*	3.7502	3.75	3.75	3.75	3.75	3.7504	3.7507	3.7514
USD / AED*	3.6730	3.67	3.67	3.67	3.67	3.6729	3.6730	3.6731
USD / KWD	0.2851	0.282	0.285	0.282	0.28	0.2856	0.2858	0.2864
USD / OMR*	0.3852	0.38	0.38	0.38	0.38	0.3850	0.3849	0.3849
USD / BHD*	0.3770	0.376	0.376	0.376	0.376	0.3774	0.3778	0.3785
USD / QAR*	3.6393	3.64	3.64	3.64	3.64	3.6417	3.6436	3.6481
USD / INR	54.3750	53.50	53.00	52.00	51.00	54.3831	54.3919	54.4095
USD / CNY	6.1651	6.23	6.22	6.20	6.25	6.2206	6.2251	6.2361

*Denotes USD peg

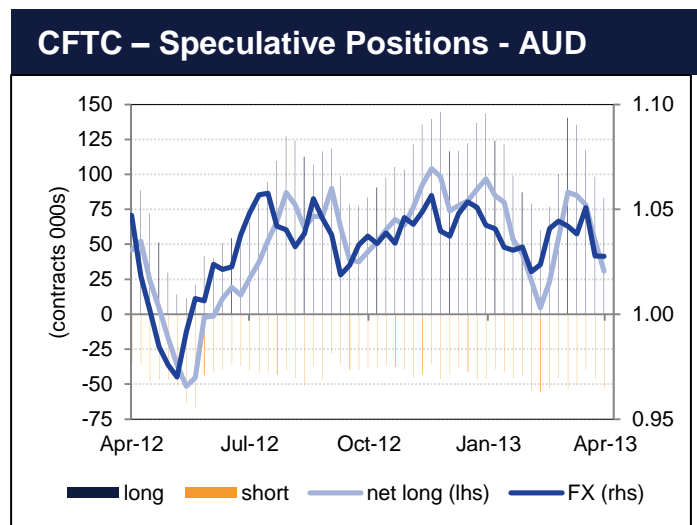
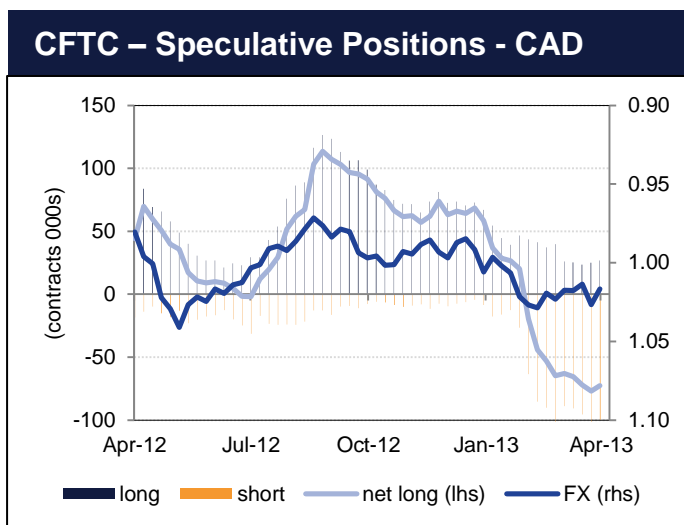
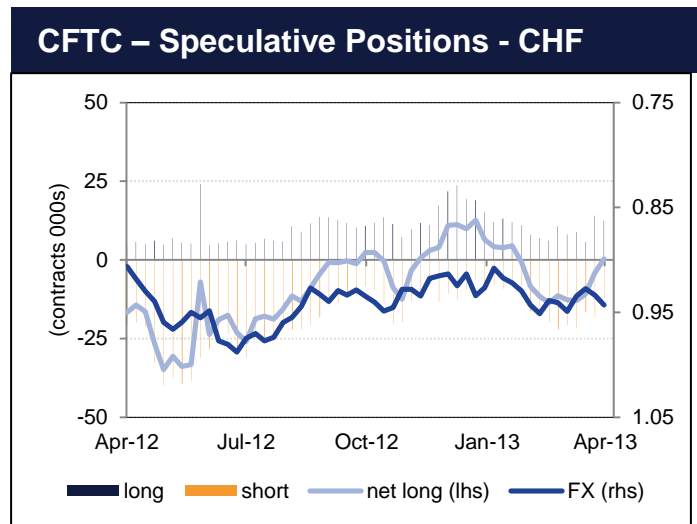
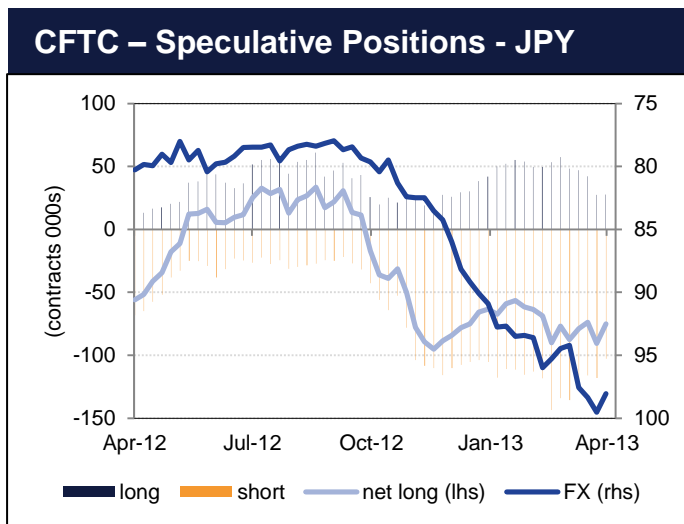
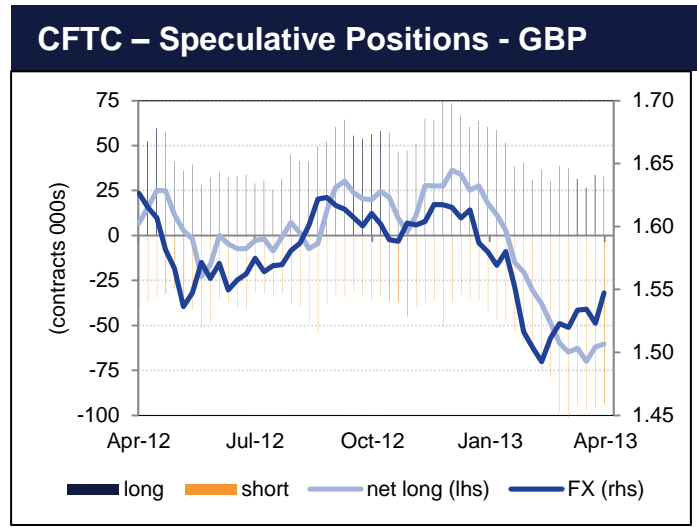
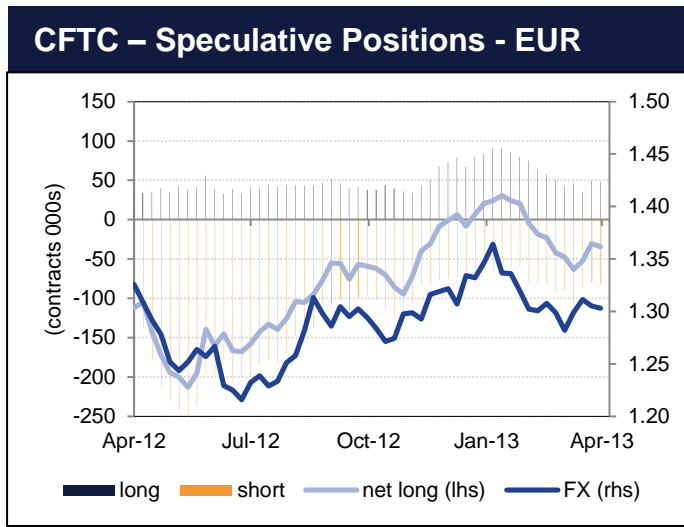
Source: Bloomberg, Emirates NBD Research

Major Currency Pairs and Interest Rates



Source: Bloomberg, Emirates NBD Research

Major Currency Positions



Source: Bloomberg, Emirates NBD Research

Economic Calendar

Date	Country	Event	
29-Apr	Germany	CPI	
	Italy	Business Confidence	
	Eurozone	Consumer Confidence	
	US	Personal Income / Spending	
	US	PCE Core	
	US	Pending Home Sales	
	US	Dallas Fed Mfg Activity	
	30-Apr	UK	GfK Consumer Confidence Survey
Japan		Jobless Rate	
Japan		Industrial Production	
Japan		Retail Trade	
Japan		Housing Starts	
Germany		Retail Sales	
Germany		GfK Consumer Confidence Survey	
Germany		Unemployment Rate	
UK		Mortgage Approvals	
UK		Money Supply	
Eurozone		CPI	
Eurozone		Unemployment Rate	
Italy		CPI	
Canada		GDP	
US		S&P/CaseShiller Home Price Index	
1-May		China	Manufacturing PMI
		UK	Nationwide House Prices
	UK	PMI Manufacturing	
	US	MBA Mortgage Applications	
	US	ADP Employment Change	
	US	ISM Manufacturing	
	US	FOMC Rate Decision	
	2-May	Switzerland	Manufacturing PMI
Italy		Manufacturing PMI	
France		Manufacturing PMI	
Germany		Manufacturing PMI	
Eurozone		Manufacturing PMI	
Eurozone		ECB Rate Decision	

2-May	US	Trade Balance
	US	Initial Jobless Claims
	Brazil	PMI Manufacturing
	Brazil	Trade Balance
3-May	India	RBI Rate Decision
	UK	PMI Services
	Brazil	Industrial Production
	US	Change in Non-Farm Payrolls
	US	Unemployment Rate
	US	Factory Orders
	US	ISM Non-Mfg Composite

Source: Bloomberg

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