



بنك الإمارات دبي الوطني
Emirates NBD

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FX Week

Focus is on the Fed in the week ahead

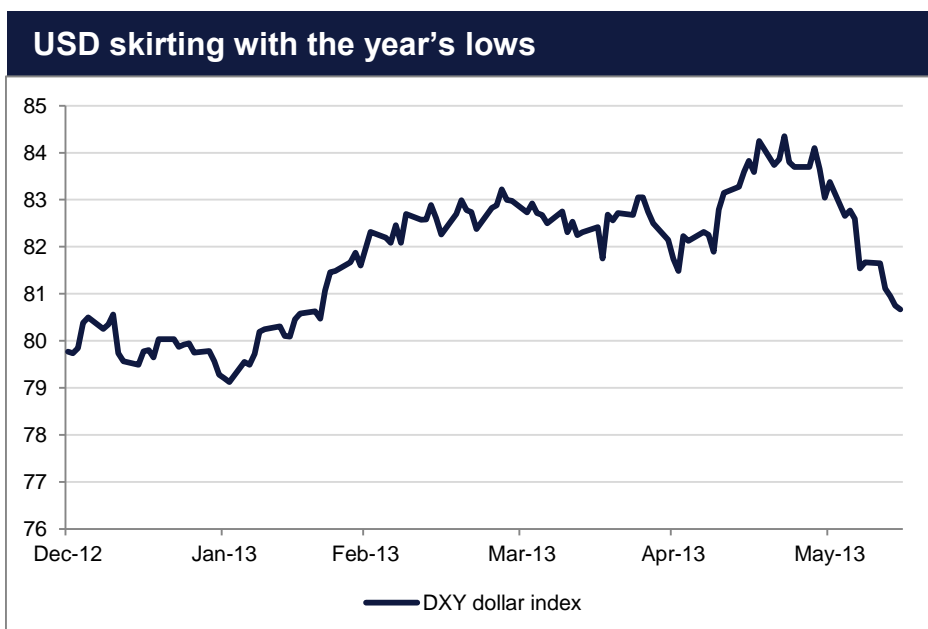
Currency markets, and indeed most financial markets around the world, will be firmly focused on the US Federal Reserve's FOMC meeting this week. As one of only a few meetings a year at which new economic forecasts are released and a press conference held, there will be more than just the usual focus on whether Quantitative Easing is maintained. Even if there is no change to the current USD85bn of asset purchases conducted by the Fed every month (which is our base case), the opportunity will exist to present a timeframe in which a 'tapering' of QE purchases might be expected.

The immediate run-up to the meeting has been characterized by pronounced volatility in financial markets, but also by a continued steady firming in US economic data. US retail sales in May rose by 0.6%, weekly jobless claims fell by 12,000 and house price data has also been firm. However, uncertainty still exists over the manufacturing sector which remains weak, and inflation which at 1.1% is a long way below the Fed's 2.0% target. Jobs are being created, but not necessarily fast enough to weigh on the unemployment rate. In addition, the fiscal tightening currently underway due to the sequester is drawing more criticism, with the IMF denouncing US fiscal policy as 'excessively rapid and ill-designed' over the weekend, claiming that it will knock 1.75% off growth this year and will further weaken it in 2014.

For these reasons it seems unlikely that the Fed will announce any change in the amount of assets being purchased just yet. This should serve to calm some of the fears in financial markets, although it will be in the detail of the economic forecasts that the real reaction will be generated. Greater optimism about growth, the labour market and inflation will increase the likelihood that 'tapering' will begin later this year, which we expect to begin in Q4.

Relief rallies to be limited

The extent of any relief rally by equity and fixed income markets will be limited, therefore, and the USD may not sell-off much further either. Long USD positions against major currencies have been trimmed in recent weeks (see page 5), creating the potential for renewed buying interest to emerge as the markets continue to countdown to the beginning of the end for QE. Emerging markets and high-yielding currencies are already exhibiting renewed vulnerability to the USD, and this can be expected to spread to major currencies as the US' superior economic performance wins out.



Source: Bloomberg, Emirates NBD Research

USD/JPY positioning more balanced

In this context USD/JPY probably remains the main currency pair in focus, given the volatility of Japanese markets over the past fortnight driven by a combination of US and Japan related concerns. Although US issues are dominant, Japan's are not insignificant either, as question-marks remain about its strategy for promoting growth and escaping from deflation. Last week's announcements from the government and from the Bank of Japan did little to quell these concerns, with no new initiatives forthcoming to reverse downward pressure on the Nikkei or upward pressure on the JPY.

However, with USD/JPY having crossed forcefully below 95.0 last week, the market is probably now at least more balanced than it has been from a positional perspective. For instance, USD/JPY is now close to where it was before the BOJ announced its 'monetary revolution' in early April. This suggests that we might be close to reaching a natural near-term limit to further JPY gains, although further disappointments in terms of economic data or from a policy point of view could still see it strengthen a bit more. Going forward, this week sees Japanese external trade for May, with its deficit expected to have widened from April. Probably more significant will be the weekly portfolio data from the Ministry of Finance, which for a month now has been showing portfolio inflows rather than the reverse. To the extent that this continues, it will be perceived as disappointing and as a failure of the policies enacted earlier this year, contributing to further pressure on Japanese markets as well as to further upward pressure under the JPY. Likewise if inflation fails to take-off then this would also be perceived as a failure of policy to date, requiring more measures to be taken to stimulate price rises.

EUR & GBP susceptible to a USD rebound

The EUR and GBP have also both benefited from the general drift lower in USD/JPY, as long USD positions have been squared ahead of the Fed's announcement this week. To some extent local factors have also contributed to their rallies as well, as economic data in both areas have shown a modest improvement over the last month, dampening expectations about the need for further monetary stimulus. However, as we see both of these recoveries as vulnerable to ongoing austerity policies, we suspect that the pressure for more monetary easing will return, probably later this year. And as this will probably coincide with the US Fed finally embarking on its 'tapering' of QE, the risks are still tilted towards monetary policy divergence between the US and Europe in 2013, which should support the USD at the expense of both these currencies.

In the coming week, data in the Eurozone includes the German ZEW index as well as the flash PMI surveys for June. In the UK, attention will be on inflation for May, retail sales and public finance figures, as well as on the minutes of the last Bank of England monetary policy meeting. It may be too soon to expect the data to deteriorate, but even in the absence of this, both the GBP and the EUR could be susceptible to a Bernanke induced USD recovery.

High yield FX pulls back from extremes

The AUD was finally able to recover a little ground in the last few days of last week, after its momentous decline over the past month, from 1.03 to almost 0.93 in the space of five weeks. However, the restoration of rough stability does not equate to a return of confidence in the battered currency. Indeed, it probably exemplifies the risks faced by a number of high yielding and/or emerging market currencies in the face of a changing monetary policy environment in the US. The INR also managed to rebound slightly from its INR59.0USD lows, but it also still remains vulnerable as US policy begins to normalize. Indian WPI inflation fell slightly in May to 4.7%, but with currency weakness maintaining price risks going forward the RBI will probably remain cautious when it meets this week, and leave its interest rates unchanged.

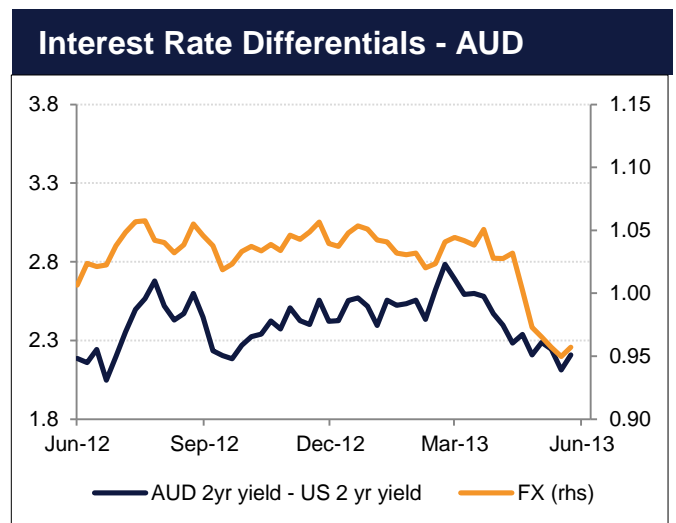
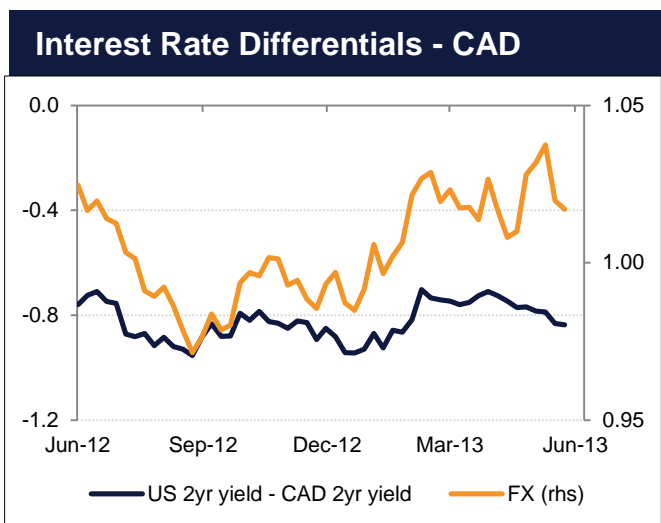
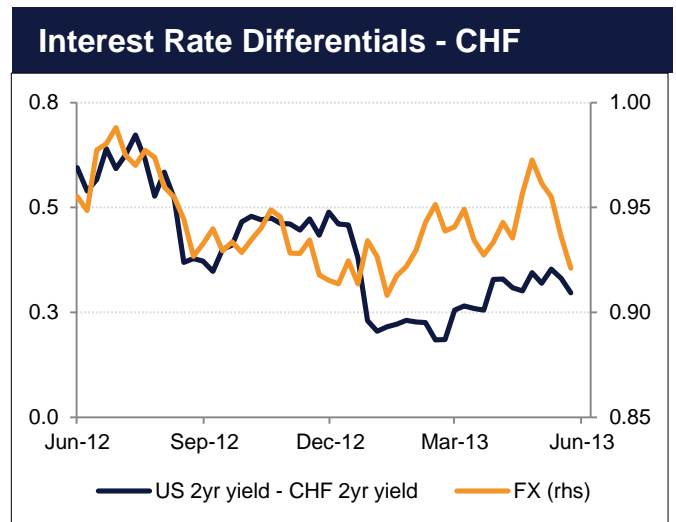
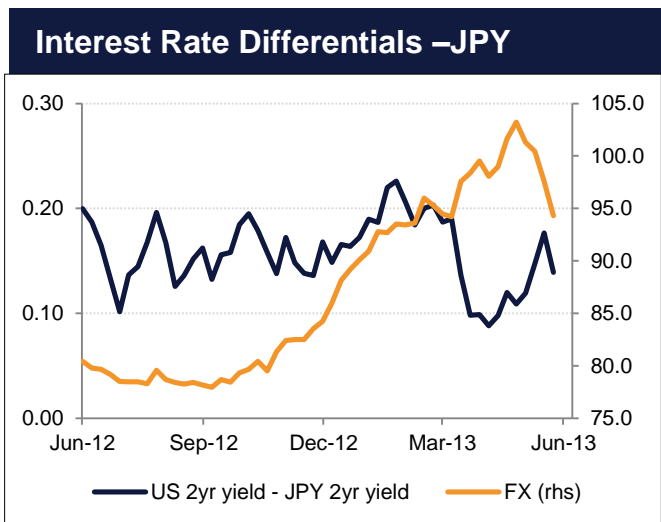
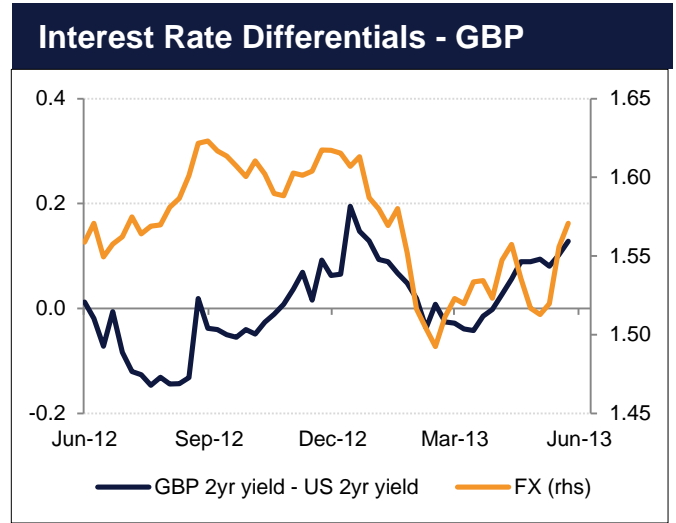
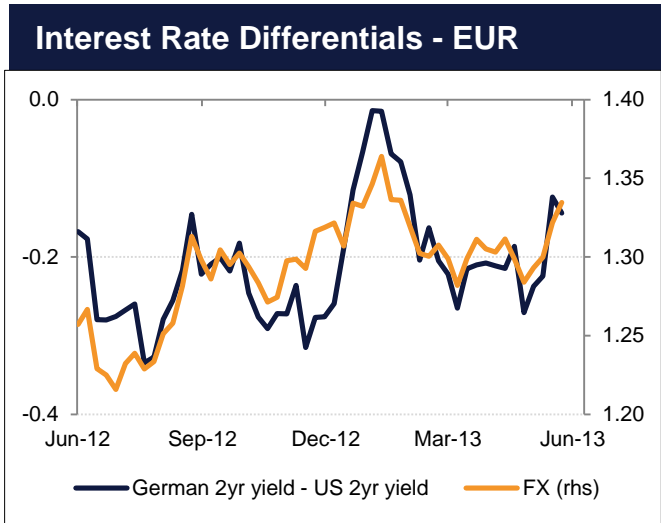
FX Forecasts - Major						Forwards		
	Spot 14.06	1M	3M	6M	12M	3M	6M	12M
EUR / USD	1.3347	1.28	1.25	1.20	1.15	1.3353	1.3361	1.3379
USD / JPY	94.31	100.0	105.0	107.0	110.0	94.26	94.19	93.98
USD / CHF	0.9211	0.96	1.00	1.04	1.08	0.9203	0.9192	0.9166
GBP / USD	1.5707	1.51	1.48	1.45	1.45	1.5698	1.5690	1.5678
AUD / USD	0.9570	0.98	0.97	0.94	0.90	0.9507	0.9451	0.9343
USD / CAD	1.0170	1.03	1.05	1.07	1.10	1.0193	1.0215	1.0262
EUR / GBP	0.8497	0.85	0.84	0.83	0.79	0.8506	0.8515	0.8533
EUR / JPY	125.60	128.0	131.0	128.4	126.5	125.60	125.60	125.60
EUR / CHF	1.2293	1.23	1.25	1.25	1.24	1.2287	1.2280	1.2261

FX Forecasts - Emerging						Forwards		
	Spot 14.06	1M	3M	6M	12M	3M	6M	12M
USD / SAR*	3.7501	3.75	3.75	3.75	3.75	3.7502	3.7508	3.7519
USD / AED*	3.6729	3.67	3.67	3.67	3.67	3.6728	3.6727	3.6727
USD / KWD	0.2833	0.282	0.285	0.282	0.28	0.2847	0.2853	0.2874
USD / OMR*	0.3850	0.38	0.38	0.38	0.38	0.3846	0.3845	0.3837
USD / BHD*	0.3770	0.376	0.376	0.376	0.376	0.3776	0.3780	0.3785
USD / QAR*	3.6416	3.64	3.64	3.64	3.64	3.6425	3.6438	3.6468
USD / INR	57.5287	56.75	55.50	55.00	53.75	57.5383	57.5464	57.5623
USD / CNY	6.1309	6.23	6.22	6.20	6.25	6.1950	6.2225	6.2692

*Denotes USD peg

Source: Bloomberg, Emirates NBD Research

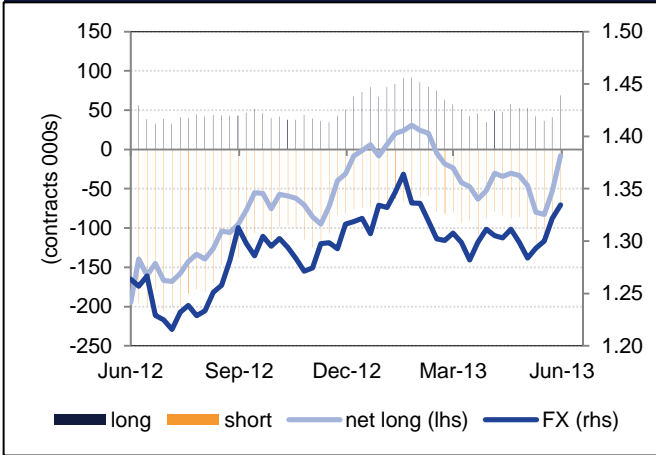
Major Currency Pairs and Interest Rates



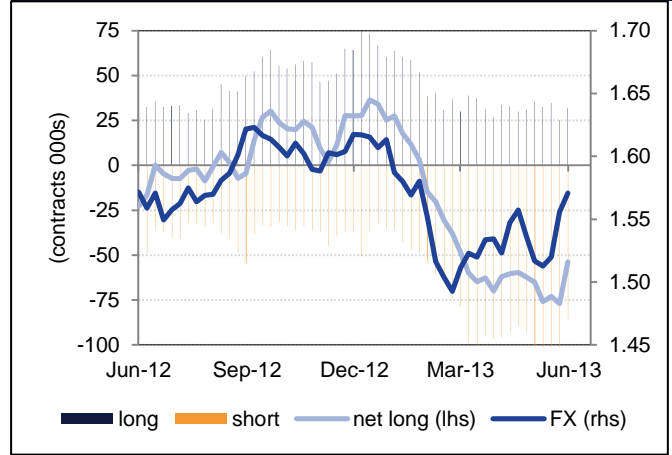
Source: Bloomberg, Emirates NBD Research

Major Currency Positions

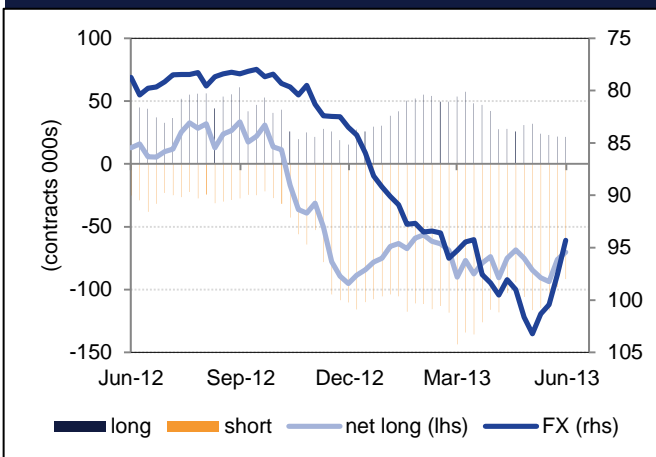
CFTC – Speculative Positions - EUR



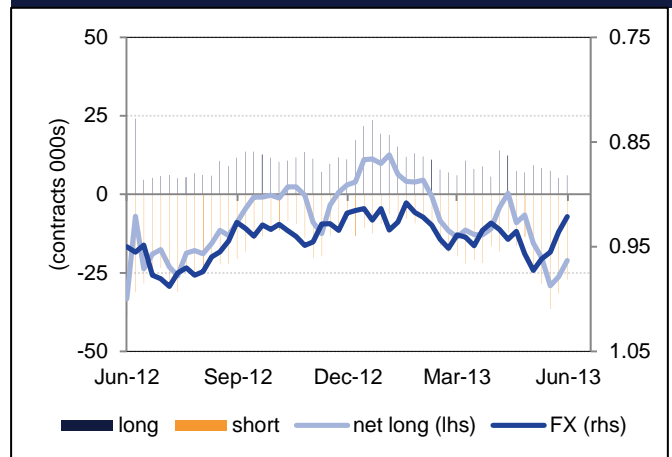
CFTC – Speculative Positions - GBP



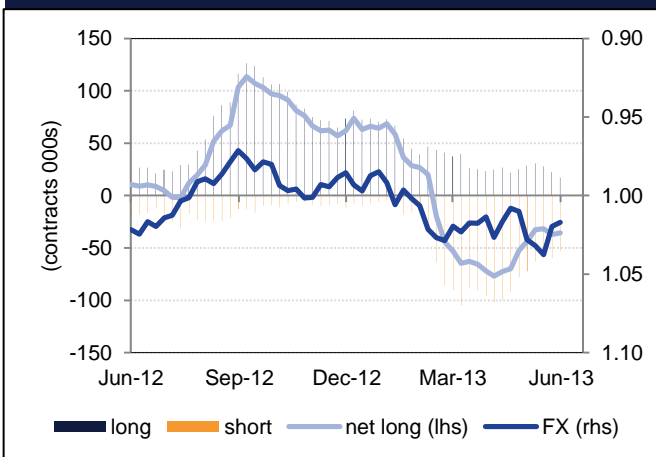
CFTC – Speculative Positions - JPY



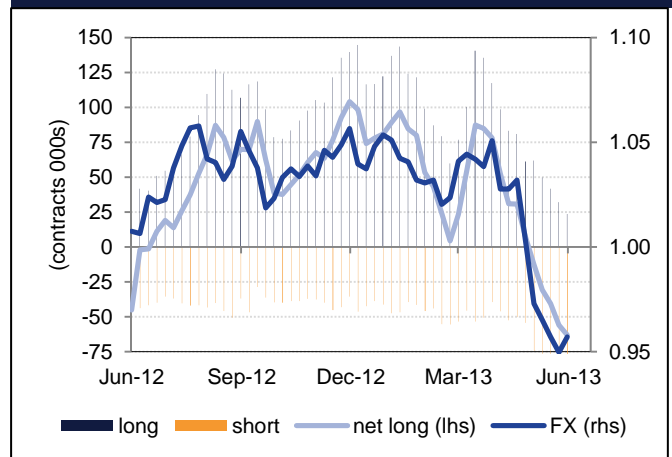
CFTC – Speculative Positions - CHF



CFTC – Speculative Positions - CAD



CFTC – Speculative Positions - AUD



Source: Bloomberg, Emirates NBD Research

Economic Calendar

Date	Country	Event	
17-June	Japan	Tertiary Industry Index	
	India	RBI rate decision	
	Italy	Trade Balance	
	Eurozone	Trade Balance	
	US	Empire Manufacturing	
	US	NAHB Housing Market Index	
18-June	Australia	RBA Policy Meeting – June Minutes	
	Japan	Industrial Production	
	UK	CPI	
	UK	Retail Price Index	
	Germany	ZEW Survey	
	US	CPI	
	US	Housing Starts	
	Morocco	Interest rate decision	
	19-June	UK	Bank of England Minutes
		US	MBA Mortgage Applications
US		FOMC rate decision	
20-June	Switzerland	Trade Balance	
	France	PMI Manufacturing / Services	
	Germany	PMI Manufacturing / Services	
	Eurozone	PMI Manufacturing / Services	
	UK	Retail Sales	
	UK	CBI Trends Total Order	
	Brazil	Unemployment Rate	
	US	Initial Jobless Claims	
	Eurozone	Consumer Confidence	
	US	Philadelphia Fed	
	US	Existing Home Sales	
	Egypt	Rate decision	
	21-June	UK	Public Finances
		Canada	CPI
Canada		Retail Sales	

Source: Bloomberg

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