بنك الإمارات دبي الوطني
Emirates NBD

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FX Week

USD holding up surprisingly well, considering

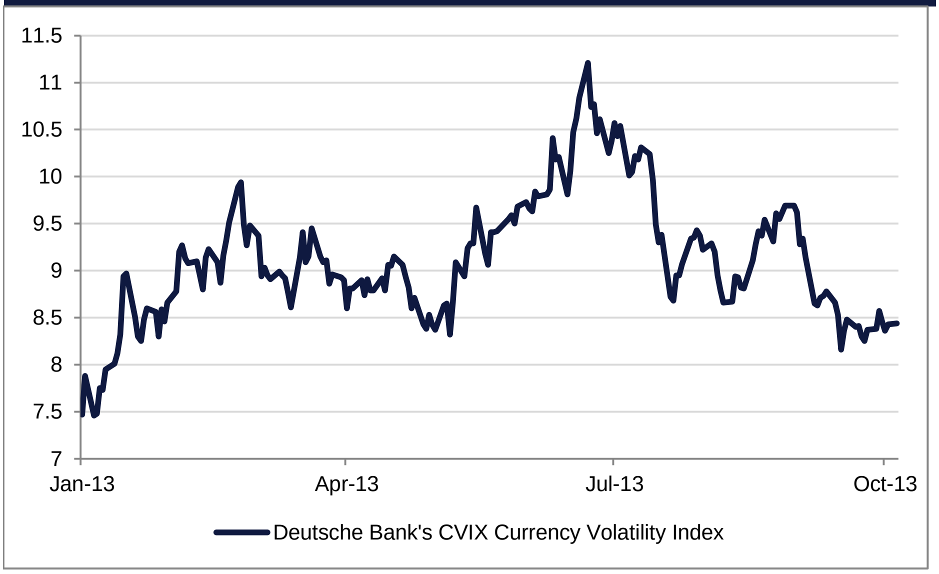
Considering the events of the last fortnight, with the US government shutting down, Fed tapering on hold and the ECB signaling a more relaxed stance over its monetary policy, we are a little surprised that the USD is not already much weaker. EUR/USD barely pushed above 1.36 last week before falling back again, while GBP/USD could not sustain gains above 1.62. There is as yet no end in sight to the shutdown, however, and if it persists through this week without resolution the situation will become more complicated by the proximity to the debt ceiling deadline on or around October 17th. This would certainly place more pressure on risky asset markets and presumably push the USD down as well as that date approaches.

However, for the moment the markets appear to be of the belief that an agreement will be found, avoiding a debt default by the US government and seeing civilian government employees return to work. This after all has been the pattern of previous US government shutdowns. News over the weekend that Congress has voted to allow furloughed government workers to receive back pay may also lend support to such sentiment, suggesting that politicians are well aware of the limits to which they can go. The coming week will remain tense, therefore, but for the time being the pressure appears contained. Given this picture, we remain relatively comfortable with our view that USD weakness will be temporary, and that resolution of these big fiscal and monetary policy questions will eventually see it start to recover.

Beyond Washington the FOMC minutes will be the main focal point this week

Apart from the news out of Washington this week the FOMC minutes will be the main focal point for financial markets. These are the minutes of the September meeting at which the decision was taken not to begin tapering the Fed's USD85bn of monthly asset purchases. Thus any light the minutes can shed on that decision will be welcome, perhaps providing clues about any new timeline the Fed is working towards in terms of bringing QE to an end. Somewhat surprisingly last week SF Fed President Williams suggested that the FOMC is still working towards the timetable Ben Bernanke highlighted in June, of reducing QE later this year and ending it by the middle of 2014.

FX volatility may be set to rise



Source: Deutsche Bank Bloomberg, Emirates NBD Research

Any confirmation of that in the minutes would likely give the USD renewed support. With official economic data releases now being affected by the shutdown the markets will have little else to go on, apart from a number of data releases from private sector sources, such as the University of Michigan consumer sentiment index. Reassuringly, however, the activity data that has been released over the last week is still consistent with recovering momentum in the economy.

EUR trades firmer but downside risks remain

The EUR benefited from the easing of Italian political tensions last week, and with the ECB also adopting a less dovish tone than the markets had expected, following its monthly council meeting, the combined effect was to push EUR/USD above 1.36 briefly. Although the ECB left its easing bias and its forward guidance unchanged, President Draghi did not sound in any urgency to utilize the policy instruments the ECB has at its disposal, even though the Eurozone's CPI fell further to 1.1% in September.

Although we raised our one-month forecast for EUR/USD to 1.38 last month, this was largely because of the US Fed's failure to start tapering QE in September. With the ECB also now showing less disposition to ease monetary policy further (and with the US government shutting down), it may have been expected that this level would already have been tested. That it has not demonstrates that the EUR's rally is unlikely to last. Firstly, the Fed's decision only represents a delay to QE tapering, while in the Eurozone we would not be surprised if the ECB does start to ease monetary policy again probably close to the end of the year. Interest rate differentials (see page 5) already suggest that the EUR/USD has rallied beyond near-term estimates of fair value, while the prospect of further monetary policy divergence between the Fed and the ECB would only add to the EUR's downside risks. We would also warn that FX markets may become inherently more volatile, as the outlook for monetary and fiscal policy becomes harder to read.

GBP vulnerability also returns

GBP/USD's recent rally also looks as if it is vulnerable to being unwound, with Cable ending the week just above 1.60, having failed to sustain highs of 1.6260. One factor behind the drop could be that rhetoric from the Bank of England continues to suggest that any unwinding of its QE is still some way behind that of the Fed. Data released last week also gave the impression that the momentum in the UK recovery may already be slowing, with PMI data for manufacturing, construction and services, all coming off their recent highs. The Bank of England's MPC meets in the coming week but no change in monetary policy is expected. UK Industrial production and trade figures will also be released this week, with both presenting risks to the pound's continued firmness.

JPY and CHF supported for the moment by shutdown fears

USD/JPY and USD/CHF losses last week were the clearest reflection of uncertainty over the US fiscal situation, but even here the moves have been relatively contained, with both pairs pulling back from their week's lows below 97.0 and 0.90 respectively at the end of the week. In both cases an agreement to end the US government shutdown would be greeted positively seeing them return to 99.00 and 0.92 respectively in the first instance. Over time we see both rallying further still as the Bank of Japan continues its aggressive monetary policy stimulus, while the CHF should also be weighed on by the SNB's ongoing protection of the EUR/CHF1.20 level.

But risk aversion appears to lack conviction as shown by AUD and NZD

On the opposite end of the risk scale the AUD and the NZD have also been surprisingly firm considering the overall pressure on risk loving markets. Again this speaks of the lack of conviction in current risk aversion based around expectations of a US government bond default. This has allowed both the AUD and the NZD to benefit from the messages from their respective central banks, with the RBA dropping its easing bias, and the RBNZ warning of sustained interest rate rises to come, by as much as 200 basis points over the next two years if property prices there continue to rise. Of the two the RBNZ is clearly the most hawkish and we would not discount the possibility of the RBA easing policy again further in the months to come, especially if unemployment data (to be released in the coming week) remains challenging.

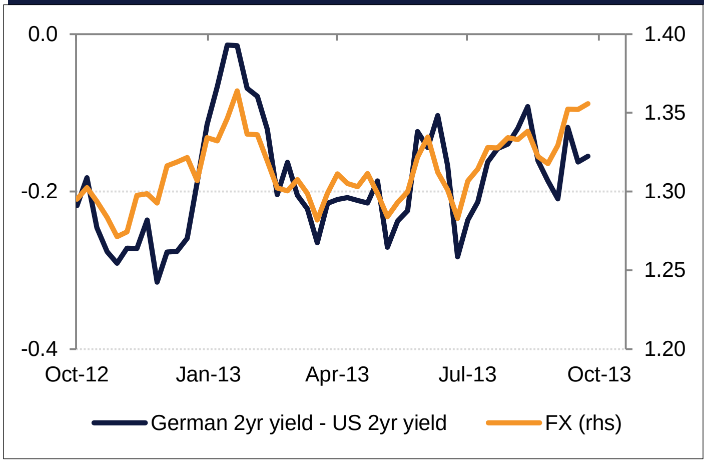
FX Forecasts - Major						Forwards		
	Spot 04.10	**1M**	**3M**	**6M**	**12M**	**3M**	**6M**	**12M**
EUR / USD	1.3558	1.38	1.34	1.28	1.20	1.3561	1.3564	1.3573
USD /JPY	97.48	100.0	103.0	107.0	110.0	97.42	97.35	97.14
USD / CHF	0.9072	0.90	0.93	0.98	1.04	0.9065	0.9056	0.9035
GBP / USD	1.6010	1.64	1.60	1.58	1.55	1.5998	1.5988	1.5965
AUD / USD	0.9435	0.95	0.90	0.88	0.85	0.9378	0.9324	0.9213
USD / CAD	1.0294	1.03	1.05	1.07	1.10	1.0318	1.0341	1.0389
EUR / GBP	0.8468	0.84	0.84	0.81	0.78	0.8476	0.8484	0.8501
EUR / JPY	132.14	138.0	138.0	137.0	132.0	132.14	132.14	132.14
EUR / CHF	1.2298	1.24	1.25	1.25	1.26	1.2290	1.2282	1.2260

FX Forecasts - Emerging						Forwards		
	Spot 04.10	**1M**	**3M**	**6M**	**12M**	**3M**	**6M**	**12M**
USD / SAR*	3.7502	3.75	3.75	3.75	3.75	3.7504	3.7508	3.7521
USD / AED*	3.6730	3.67	3.67	3.67	3.67	3.6728	3.6728	3.6728
USD / KWD	0.2827	0.282	0.285	0.282	0.28	0.2872	0.2892	0.2972
USD / OMR*	0.3850	0.38	0.38	0.38	0.38	0.3845	0.3842	0.3835
USD / BHD*	0.3768	0.376	0.376	0.376	0.376	0.3785	0.3790	0.3814
USD / QAR*	3.6411	3.64	3.64	3.64	3.64	3.6432	3.6458	3.6501
USD / INR	61.4400	64.00	62.00	59.00	57.00	61.4559	61.4686	61.4905
USD / CNY	6.1240	6.15	6.15	6.20	6.20	6.1539	6.1659	6.1974

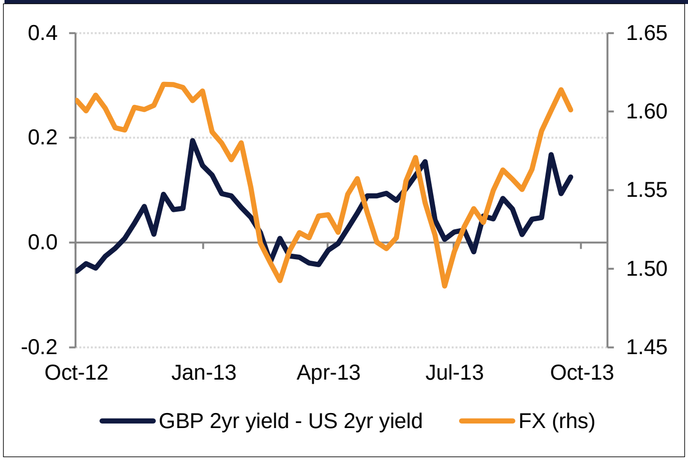
**Denotes USD peg*
Source: Bloomberg, Emirates NBD Research

Major Currency Pairs and Interest Rates

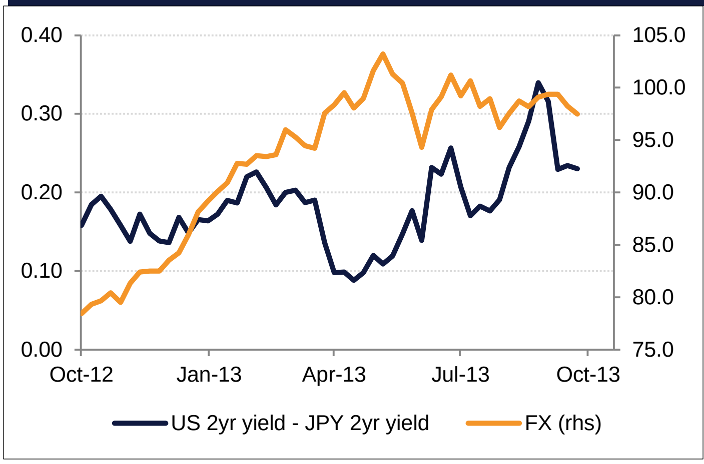
Interest Rate Differentials - EUR



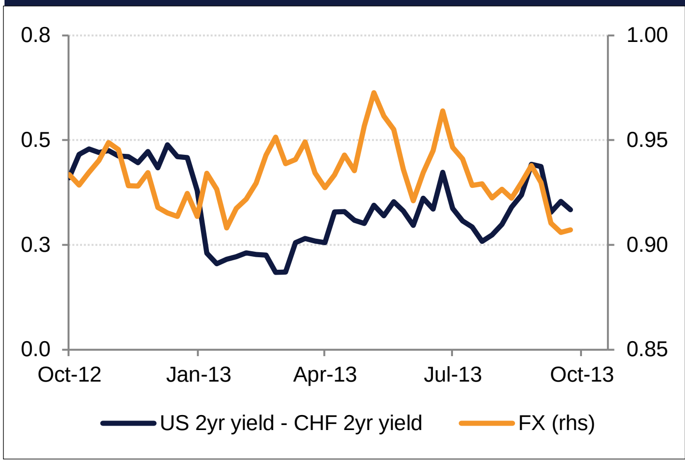
Interest Rate Differentials - GBP



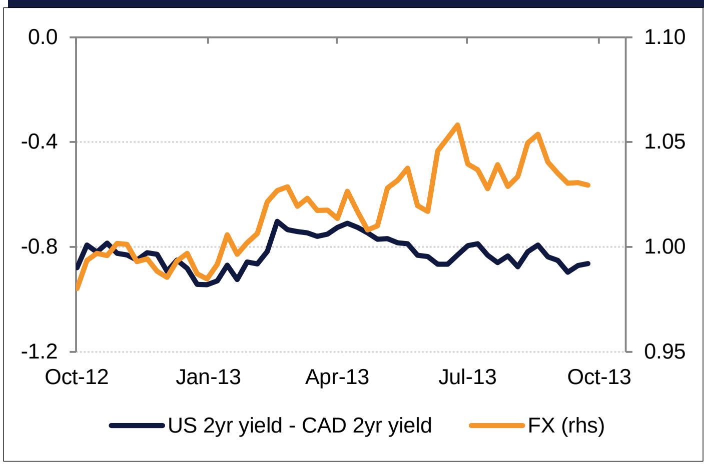
Interest Rate Differentials –JPY



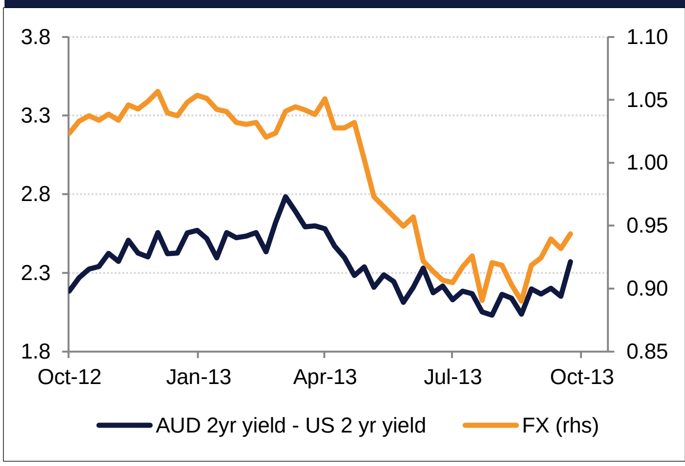
Interest Rate Differentials - CHF



Interest Rate Differentials - CAD



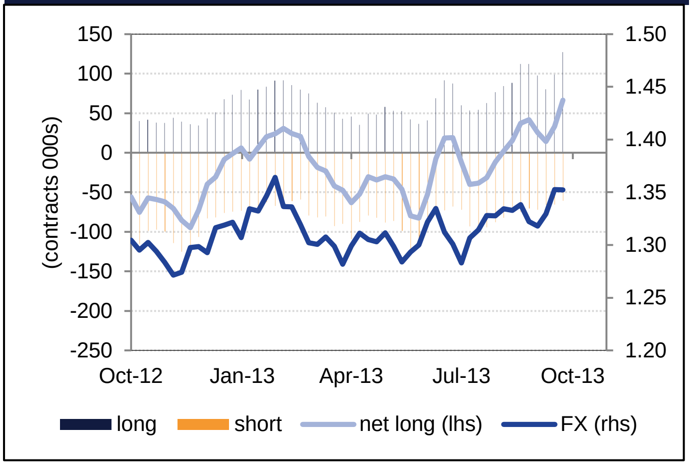
Interest Rate Differentials - AUD



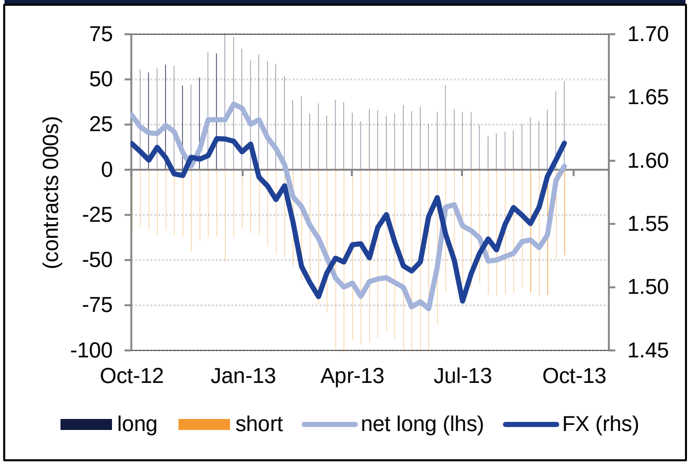
Source: Bloomberg, Emirates NBD Research

Major Currency Positions*

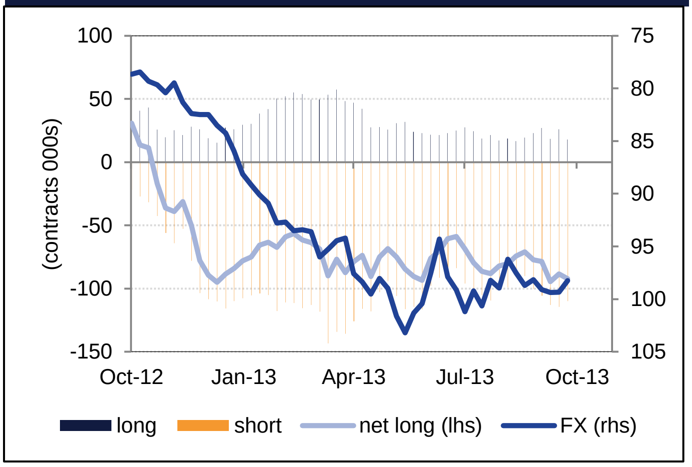
CFTC – Speculative Positions - EUR



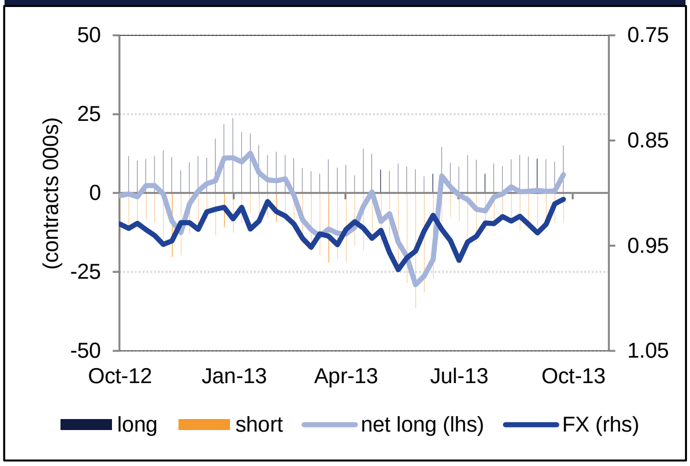
CFTC – Speculative Positions - GBP



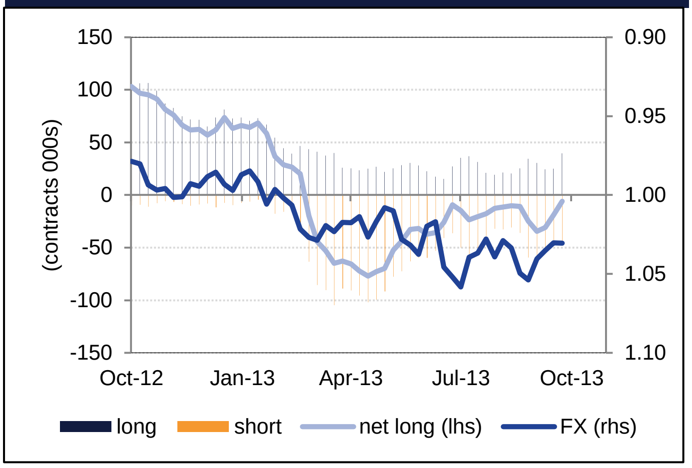
CFTC – Speculative Positions - JPY



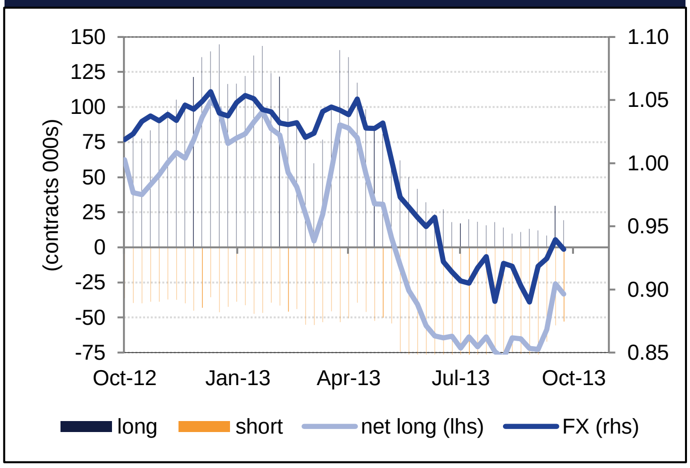
CFTC – Speculative Positions - CHF



CFTC – Speculative Positions - CAD



CFTC – Speculative Positions - AUD



Source: Bloomberg, Emirates NBD Research
**Data as of 13th September, 2013*

Economic Calendar

Date	Country	Event
7-Oct	Japan	Bank of Japan’s Monthly Economic Report
	Eurozone	Sentix Investor Confidence
	US	Consumer Credit
8-Oct	UK	RICS House Price Balance
	Japan	Trade Balance
	Switzerland	Unemployment Rate
	Germany	Trade Balance
	France	Bank of France Business Sentiment
	Switzerland	CPI
	Switzerland	Retail Sales
	Germany	Factory Orders
	Canada	Housing Starts
	US	Trade Balance
9-Oct	UK	Industrial Production
	UK	Trade Balance
	Germany	Industrial Production
	US	MBA Mortgage Applications
	Russia	CPI
	US	Fed releases minutes of its meeting
	Brazil	Selic Rate
10-Oct	Japan	Tertiary Industry Index
	Australia	Unemployment Rate
	France	Industrial Production
	Italy	Industrial Production
	UK	Bank of England Rate Decision
	US	Initial Jobless Claims
	Egypt	CPI
11-Oct	Germany	CPI
	Italy	CPI
	India	Industrial Production
	US	PPI
	Canada	Unemployment Rate
	US	Retail Sales
	US	U of Michigan Confidence
12-Oct	China	Trade Balance

Source: Bloomberg

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