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ForexWatch Daily Briefing

G7

Thursday, August 07, 2008

News and data out of Europe

* German June manufacturing orders -2.9% m/m vs -1.4% May, +0.5% exp.

News and data out of North America

* Canada July Ivey Purchasing Managers Index 65.5 v. 66.0 expected
* Nymex crude ends -57 cents at $118.60
* Freddie Mac reports Q2 loss of $821 mln, provision for credit losses of $2.5 Bln
* China forex regulator says scraps requirement for firms to sell forex income; simplifies approval process for direct overseas investment
* US Treasury: China"s forex actions are positive step

Themes

* The US dollar index closed above the 200-day Moving Average (74.21) for the first time since April 3, 2006.

* The move higher in the US dollar was led by the USD/JPY after massive stops were triggered above 108.60 to a high of 109.88.

* The move up in the US dollar was underpinned by another fall in the oil price after US government inventory figures showed a surprise rise in reserves.

* The move higher in the USD/JPY was not sparked by any individual news items or data. Analysts say that the market was very short ahead of rumoured barriers at 108.50 and 109.00 and expectations that Japanese investors would be forced out of long AUD/JPY and NZD/JPY positions.

* The rallies on equity market has improved investor risk appetite and suggests that Japanese investors will not alter their "sell JPY investment strategy.

* The US dollar index closed at 74.27 up from Tuesday's close at 73.90. (More in a closer look at the FX market)

A closer look at the commodity markets

* NYMEX Crude settled at 118.58 down from 119.17 at Tuesday's close. The price popped above 120 after the American Petroleum Institute issued a report saying that stocks fell, but five minutes later the US government {EIA} reported that stocks rose more than the market was expecting. The range for Tuesday's session was 117.11/120.49.

* Gold closed at 879 up from 874 yesterday. Copper closed up 0.15%.

* The CRB index closed at 397.24 down from 398.41 at Tuesday's close.

A closer look at the equity markets

* Wall Street finished in the black after recovering from being down 0.75% in the morning session. The Dow was down around 90 points early in the session after Freddie Mac reported a larger than expected loss. The market rallied in the afternoon due to another fall in the oil price, the perception that the rising US dollar was good for Wall Street and a reassuring outlook from Cisco.

* The Dow rose 40.30 points or 0.35% to 11,656.07; NASDAQ rose 28.54 points or 1.21% to 2,378.37.

* The VIX index fell to 20.23 from 21.14 late Tuesday.

A closer look at the Treasury market

* Treasury yields rose slightly due to the extension of the rally on Wall Street and fall in risk aversion.

* The 2-year Treasury yield rose to 2.58% from 2.55% late Tuesday; the 10-year Treasury yield rose to 4.05% from 4.02% late Tuesday.

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A closer look at the FX market

* The EUR/USD traded up to 1.5516 in early Europe before another extremely disappointing European economic number, this time German IO, sent the EUR/USD lower. A break higher in the USD/JPY and a fall in the oil price sent the USD broadly higher during the US session and the EUR/USD fell to 1.5398 to knock out a 1.5400 barrier. The EUR/USD was offered into the US close and was trading around 1.5410.

* The USD/JPY moved higher in Europe to take out the large 108.50 option barrier, but the turbo move higher came after the US session got underway. Large option as stops were targeted above 109.00 and 109.50 and the market was caught short and had to cover. Many traders were looking for JPY strength to emanate from Japanese unwinding of long AUD/JPY and NZD/JPY strategies, but that never eventuated, as risk appetite is on the rise. The USD/JPY traded up to 109.88 and is closing close to that level ahead of a large 110.00 option barrier.

* The large move higher in the USD/JPY dragged the EUR/JPY higher to 169.32 with the market a bit wary of selling the EUR ahead of the ECB meeting later today. The EUR/JPY is closing close to the highs and is above 169.00.

* The GBP/USD fell below the 1.9500 level due to broad USD strength and is now within sight of the trend low and major short-term support at 1.9409.

* The AUD/USD traded back to the 200-day MA around 0.9200/05 during the early London session where sellers emerged in good numbers. The AUD/USD came under heavy pressure during the US session with real money and spec accounts bailing out of the AUD/USD and NZD/USD as the US dollar continued its rise higher. The AUD/USD traded as low as 0.9065 and is closing around 0.9090.

Looking Ahead

22:45 NZD Employment
23:50 JPY Machinery orders
01:30 AUD Employment

OVERNIGHT RANGES

Currency	High	Low	Close
EUR/USD	1.5516	1.5398	1.5409
USD/JPY	109.88	108.23	109.79
EUR/JPY	169.32	167.21	169.05
GBP/USD	1.9595	1.9467	1.9475
USD/CHF	1.0610	1.0503	1.0603
USD/CAD	1.0496	1.0400	1.0490
AUD/USD	0.9206	0.9065	0.9085
NZD/USD	0.7270	0.7165	0.7175

Wrap-up

Sentiment towards the US dollars has improved dramatically and looks like it will continue to do so. While the US economy is far from being a bright light, the strong evidence that the economic malaise that has seen the US economy slump is now spreading to infect the global economy. Perceptions that the global economy is slowing is underpinning the US dollar in two ways. It is leading to the unwinding of "decoupling" strategies that involved selling US dollars for other currencies and commodities. The slowing global growth scenario is also leading to a significant sell off in oil and other commodities, which is also broadly supporting the USD. If Trichet softens his hawkish rhetoric ever so slightly after the ECB leaves rates on hold as is widely expected, the EUR/USD will head down to the trend low just above 1.5300.

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