Daily Forex Report

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USD lower, GDP revised higher, existing homes sale drop

- **USD:** Lower, pressured by a recovery in global equity markets, Q4 GDP revised up, existing home sales drop
- **JPY:** Higher, factory output expands and retail sales jump, Yuan revaluation speculation
- **EUR:** Higher, inflation falls, gains in cross to GBP, short covering
- **GBP:** Lower, UK Q4 revised up, Q4 government spending higher than expected
- **CAD and AUD:** AUD & CAD higher, strong Australian credit demand, Canada's C/A deficit narrows

Overview

The USD traded lower Friday pressured by a modest improvement in risk sentiment as equity markets rally in reaction to report of an upward revision in UK and US Q4 GDP, stronger industrial production and retail sales in Japan and strong private sector credit demand from Australia. USD was also pressured by Yuan revaluation speculation. Yuan forwards traded higher in reaction to a newspaper report that the Chinese government is assessing the potential impact of currency gains. US economic data was mixed with Q4 GDP revised higher, Chicago PMI came in higher than expected and Michigan sentiment was revised slightly lower. Existing home sales posted an unexpected sharp decline. Existing home sales are at a seven month low. USD remained on the defensive despite mixed US economic data as US equity markets trade both sides of settlement.

Focus turns to next week's central bank policy meetings in Australia and Canada on Tuesday and the UK and EU on Thursday and Friday's release of US February unemployment. The BOC is expected to maintain steady rate policy, the RBA is expected to hike rates 25 bps, the ECB is expected to remain on hold and there is uncertainty about whether the BOE will maintain its current level of asset purchases. US February unemployment is expected to post a modest rise with nonfarm payrolls unchanged from last month.

Today's US data:
Q4 GDP revised up 0.2% to 5.9%, a reading of 5.7% was expected. February Chicago PMI came in at 62.6, a reading of 60 was expected. February Michigan consumer sentiment was revised to 73.6, a reading of 74 was expected. January existing home sales declined by 7.2% to 505k, a reading a 550k was expected.

Upcoming US data:
Next week's US economic calendar includes March 1st release of January personal income and consumption. Personal income and consumption are expected to rise by 0.4%. January construction spending and the February ISM Index will also be released on March 1st. Construction spending is expected to decline by 0.7% compared to 1.2% decline last month. The ISM Index is expected at 58 compared to 58.4 last month. On March 2nd domestic auto sales will be released. On March 3rd February ADP employment will released expected at 10k compared to -22k last month. February manufacturing ISM Index will also be released on March 3rd expected at 51 compared to 50.5 last month. On March 4th initial jobless claims for week ending 02/27 will be released expected at 490k compared to 496k last month. Q4 productivity, unit labor costs, January pending home sales and factory orders will also be released on March 4th. Q4 productivity is expected unchanged at 6.2%, unit labor costs are expected unchanged at -4.4%, factory orders are expected unchanged at 1% and pending home sales are expected at 98.4 compared to 96.6 last month. On March 5th February unemployment and nonfarm payrolls will be released along

with January consumer credit. The unemployment rate is expected to rise 0.1% to 9.8%, nonfarm payrolls are expected unchanged at -20k and consumer credit is expected at -3.1bln compared to - 1.7bln last month.

JPY

JPY traded higher supported by Yuan revaluation speculation and positive Japanese economic data. A newspaper report suggests that the Chinese government is assessing the potential impact of currency gains and this report fueled Yuan revaluation speculation. JPY sometimes trades as a proxy for Yuan revaluation. Japan reported that January industrial production rose by 2.5% and January retail sales rose by 2.6%. Core CPI declined by 1.3%. Japan's Finance Minister Kan said that Japan still faces deflation but the CPI decline appears to be slowing. The improvement in Japan's industrial production and retail sales and a slowdown in the CPI decline will reduce pressure on the BOE to expand quantitative ease. This marks the fifth day in a row that the JPY traded higher with the JPY supported by safe haven demand sparked by diminished risk appetite as global equity markets struggle due to concern about the outlook for global recovery. JPY also has benefited from this week's Japanese economic data which showed improvement in export sales and stronger retail sales and industrial production. In addition, the JPY has been supported by diminished Fed rate hike fears as Fed Chairman Bernanke says that it is not clear if the US recovery self-sustaining and that interest rates will have to remain low for an extended period. Analysts at J.P. Morgan Chase forecast JPY will trade at 87 next month as traders reduce bets that the Fed will raise interest rates sooner than expected. There was limited reaction to a Bloomberg report which states that the chief global economist for Goldman Sachs O'Neill sees Japan facing the biggest crisis risk in the G-10. According to O'Neill Japan is running out domestic savings and this will make it difficult for Japan to finance its rising budget deficit. O'Neill went on to say that he thinks that the JPY is highly overvalued.

Next week's Japanese economic calendar includes the March 2nd release of January household spending expected at -0.5% compared to 1% last month. The January unemployment rate will also be released on March 2nd expected unchanged at 5.1%.

Key technical levels to watch in USD/JPY include support at 88.55 the February 4th low with resistance at 90.29 the February 25th high.

EUR

EUR traded higher supported by a modest recovery in risk sentiment as global equity markets rallied in Friday's trade and by gains in cross trade to the GBP. An upward revision in UK and US GDP, positive industrial and retail sales data from Japan and strong private sector credit demand from Australia helped to fuel today's improvement in risk sentiment. EUR rallied in cross trade to the GBP with GBP pressured by report of higher than expected UK Q4 government spending. The trade ignored report that EU January inflation declined by 0.8% compared to a 0.3% rise last month. EUR rallied despite ongoing concern about the Greek debt crisis. Greece suspended a bond sale today because of continued market turmoil. There is an interesting report on Bloomberg quoting Goldman Sachs chief economist O'Neill that the Greek debt crisis may make EMU stronger as EU officials seek closer political ties between its members. According to O'Neill, German officials are pressing for greater political union. Focus turns to next Thursday's ECB policy meeting. No policy change is expected as the ECB is restricted by concern that the sovereign debt risk in Europe will be a drag on the EU recovery. Analysts at Deutsche Bank suggest that the EUR could decline to 1.2750 in the months ahead pressured by speculation the Fed will raise rates before the ECB. EUR remains vulnerable to concern about EU sovereign debt risk and ECB policy outlook. EUR downside may be limited because the EUR is oversold.

Next week's EU economic calendar includes the March 1st release of EU February manufacturing PMI expected at 52 compared to 52.4 last month. EU January unemployment will be released on March 1st expected unchanged at 10%. On March 2nd February HICP will be released expected at 1.1% compared to 1% last month. On March 3rd EU February services PMI will be released expected at 52.3 compared with 52.5 last month along with January retail sales. January retail sales are expected at 0.2% compared to flat last month. ECB policy meeting will be held on March 4th, no change is expected.

The technical outlook for the EUR is negative. Expect EUR support at 1.3443 the February 19th low with resistance at 1.3627 the February 24th high.

GBP

GBP traded lower with initial support sparked by a report of an upward revision in UK Q4 GDP giving way to selling pressure sparked by report of higher than expected UK Q4 government spending. UK Q4 GDP was revised up to 0.3% from an original report of 0.1% rise. UK Q4 government spending rose by 1.2%, a 0.2% rise was expected. The improvement in UK GDP will likely encourage the BOE to hold monetary policy steady next week but concern about UK debt trumps the improvement in UK economic growth and the GBP traded lower. There was limited reaction to report that UK February GFK consumer confidence improved to -14 from -17 last month. GBP is trading at a nine-month low versus the USD pressured by concern about UK debt and in reaction to report of a sharp decline in UK business investment. As we approach the May 6th national election in the UK there are two major concerns about how the election may impact the UK deficit. Rating agencies have put the UK on notice that if the government does not take action take credible action to reduce the deficit the UK AAA sovereign debt rating may be cut. The most recent UK election polls suggest that the election may result in a hung parliament. A hung parliament could lead to gridlock and lack of credible effort to reduce the UK deficit. The other concern is that the new UK government will be under intense pressure to take immediate action to reduce the UK deficit. A premature withdrawal of the UK stimulus while the UK economy is still struggling could lead to more significant deterioration not only in the economic but the long-range deficit outlook. Analysts at UBS said that GBP could fall below parity with the EUR and 1.05 versus the USD if the UK government prematurely withdraws stimulus and tightens fiscal policy.

Next week's UK economic calendar includes the March 1st release of February manufacturing PMI expected at 56.4 compared to 56.7 last month. January consumer credit, mortgage applications and mortgage lending will also be released on March 1st. Consumer credit is expected at 0.150 compared 0.052 last month, mortgage applications are expected at 52K compared to 59K last month and mortgage lending is expected at 1.102bln compared to 1.165bln last month. On March 3rd February consumer confidence index will be released expected at 68 compared to 69 last month along with February services PMI expected at 54 compared to 54.5 last month. BOE policy meeting will be held on March 4th, no policy change is expected but there is increased pressure on the BOE to expand quantitative ease.

The technical outlook for GBP is negative as GBP trades below 1.5300. Expect near-term support at 1.5115 the May 18th low with resistance at 1.5327 the February 26th high.

CAD

CAD traded higher supported by a slight improvement in risk sentiment as global equity markets rebound. The rebound in the equity markets is attributed to positive economic data from Japan which reported improvement in retail sales and industrial production, upward revisions in UK and US GDP and strong Australian private sector credit growth. These reports help offset some of this week's concern about the outlook for the global recovery. CAD was also supported by report of a narrowing of Canada's current account deficit. Canada's Q4 current-account came in at -8.75bln compared to a revised -13.8bln deficit last quarter. CAD spent most of the week on the defensive pressured by a spike in risk aversion and weaker commodity and equity markets. Recent action in China to curb lending and concern about sovereign debt risk in Europe are the primary drivers of the uptick in risk aversion. The next major focus for CAD trade will be the BOC policy meeting scheduled for March 2nd. The BOC has pledged to maintain record low yields through June of 2010 provided inflation remains in check. Last week Canada reported above expectation inflation with CPI rising close to the 2% BOC target. Despite the rise in Canada's inflation the BOC is expected to maintain steady rate policy. The BOC's decision to maintain steady rate policy could be a mild negative for CAD.

Next week's Canadian economic calendar includes March 1st release of January IPPI and RMPI along with December GDP. BOC policy meeting will be held on March 2nd, no policy change is expected. On March 4th January building permits will be released.

The technical outlook for CAD is mixed to negative as USD/CAD trades above 1.0600. Look for near-term support at 1.0510 the February 24th low with resistance at 1.0780 the February 5th high.

AUD

AUD traded higher supported by a rebound in risk appetite and in reaction to report of strong Australian private sector credit demand. As noted above, most of today's economic data from Japan. Europe and the US came in above expectation and this helped to fuel a rebound in equities and risk sentiment. Australia's January private sector credit rose by 0.4%. The private sector credit report follows yesterday's report of much stronger than expected Australian Q4 CAPEX spending. The strong private sector credit rise and CAPEX spending revives RBA rate hike speculation and tilts the odds in favor of an RBA rate hike at next Tuesday's policy meeting. This week the AUD has been under significant pressure as investors unwind carry trades because of uncertainty about the global recovery. Tightening in China, Fed rate hike fears, weaker than expected US consumer confidence housing and employment data and sovereign debt risks in Europe fuel concern about the outlook for the global recovery. Concern about the global recovery has overshadowed RBA rate hike speculation and RBA rate hike speculation has been less supportive for the AUD. Focus turns to next Tuesday’s RBA policy meeting. RBA watcher McCrann says there's nothing standing in the way of the RBA from hiking rates 25bps at next Tuesday's policy meeting. In light of this week's US disappointing US economic reports and China's tightening of credit the RBA may be less inclined to hike rates.

Next week's Australian economic calendar includes the March 1st release of Q4 company profits expected 4% compared to -2.1% last month along with Q4 business inventories expected at 0.5% compared to 0.8% last month. Q4 current account will also be released on March 1st expected at -17bln compared to -16.2bln last month. On March 2nd January building approvals will be released expected at -4% compared to 2.2% last month along with January retail sales expected at 1% compared to -0.7% last month. RBA policy meeting will be held on March 2nd. A 25bps rate hike to 4% is expected. On March 3rd Q4 GDP will be released expected at 0.3% compared to 0.2% last quarter. On March 4th January trade balance will be released expected at -2.5bln compared to -2.25bln last month.

The technical outlook for the AUD is negative as the AUD failed to hold above 8900. Expect AUD support at 8750 the February 11th low with resistance at 8953 the February 24th high.

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