Forex Focus: Euro's Not Going To Stay Over $1.30

By Nicholas Hastings

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LONDON (Dow Jones)--The euro's ability to make a sustained rally over $1.30 is even weaker now than it was before.

Last Friday's stress test results for European banks have failed to boost faith in the European financial system as they were designed to do.

At the same time, evidence that the U.S. recovery is stalling is now well-discounted in the same way that recent signs of strength in the euro-zone economy are unlikely to last.

Optimists may still be hoping the euro will make a technical break up to $1.3125 in order to meet a significant Fibonacci replacement level.

But a move down to the single currency's next support level at $1.2735 now looks more likely.

See the euro's latest attempt to rally over $1.30:

http://www.dowjoneswebservices.com/chart/view/4309

Let's face it, plans to boost investor confidence in European banks, by proving that they can withstand the upcoming economic slowdown, just haven't worked.

Yes, the tests may have increased transparency to a certain extent but they have patently failed to remove the threat of difficulties further down the road.

Yield spreads on euro-zone sovereign debt have hardly moved since the results were announced and the euro itself quickly reversed its small initial gains.

The impression is that little has changed and worries about sovereign risks will remain a drag on the single currency.

Economic data will also provide little support for the euro, certainly against the dollar, just now.

On the U.S. side, a steady deterioration in the data over the last few weeks has raised fears of a double-dip recession and reduced speculation that monetary policy would be tightened.

However, that is all over now. The Fed has reassured markets it is on standby to add even more liquidity if needed. Also, Treasury Secretary Geithner has dismissed suggestions that the economy will shrink again.

If anything, some economists say that U.S. second-quarter GDP Friday will surprise on the upside.

By contrast, the positive economic news that has come out of the euro zone over the last few weeks isn't expected to last. The improvement in economic data has been associated largely with the euro's slide earlier in the year--from over $1.50 towards the end of 2009 to under $1.20 in June. The euro's rebound since then is likely to unravel all the economic benefits that have been produced by higher exports.

It certainly looks as if speculators were already anticipating this, with the latest data on futures positioning from the Chicago Mercantile Exchange showing that long euro positions continued to decline quite sharply last week.

So while there could still be some residual upward pressure on the euro as the single currency bounces around just under $1.30, there appears to be little reason to expect any real momentum to keep it rising above that level.

Early Tuesday, the euro was making another attempt to climb over $1.30 as global risk sentiment improved in the wake of stronger-than-expected U.S. new home sales Monday and a general rally in global equities. Optimism over the global economic recovery also received a boost from news that both Israel and India raised their interest rates this week.

By 0645 GMT, the single currency had risen to $1.3006 from $1.2997 late Monday in New York, according to EBS. It was also up at Y113.13 from Y112.91.

The dollar was also up at Y86.97 from Y86.89.

Bloomberg TNI FRX POV

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 Reuters   USD/DJ
   Thomson   P/1066 or P/1074
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(Nick Hastings has covered the foreign exchange markets and industry for over 20 years. Apart from his written commentary and analysis, he also appears on Fox Business News and CNBC television in Europe, Asia and the U. S. He can be contacted on +44-20-7842-9493 or by email: nick.hastings@dowjones.com)

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