# FOREX FOCUS: Frost Bites The Pound

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A DOW JONES NEWSWIRES COLUMN

LONDON (Dow Jones)--A frosty time is being had by all round here, and that includes the pound.

As sub-zero temperatures sweep across Britain, sterling is finding itself caught up in a web of concerns over the impact the snow will have on an already faltering U.K. economy and over the increasing threat that the euro zone's crisis is posing to U.K. banks.

For the last few months, sterling had done rather well.

Indeed, it has even held up against a strengthening dollar:

http://www.dowjoneswebservices.com/chart/view/5159

Approval for the Conservative-led coalition government's fiscal tightening, signs that the U.K. economy was more robust than expected and the U.K.'s exclusion from the problems of peripheral Europe all helped to make the pound a good bet.

Now, this picture of success is falling apart.

Not only is the U.K. economy swiftly losing traction, well in advance of an increase in value-added tax that kicks in at the start of the new year, but the country is now being dogged by persistently high inflation pressures.

Hopes of a last-minute shopping spree over Christmas have now been dashed as snow-bound Britain keeps many consumers away from their desks as well as away from the shops. With delivery systems also affected, there is little chance that online shopping will take up the slack and the losses to the economy from the weather will probably amount to many billions.

Another fall in mortgage lending last month, with new figures from the Council of Mortgage Lenders showing a 4.6% drop Monday, means house prices and consumer confidence will also remain soft.

The next major focus for sterling investors is the release Wednesday of the minutes of the Bank of England's last policy meeting. Any hawkish response by the bank's monetary policy committee members to recent stubborn consumer price numbers would, under normal circumstances, be seen as positive.

The Confederation of British Industry is already suggesting that interest rates will have to be hiked within six months.

But, if investors reckon that the central bank can't tighten policy because of weak growth projections, the impact on the pound is more likely to be negative.

The deterioration in the U.K. picture has coincided with rising evidence that the U.K. isn't as immune to the euro-zone debt crisis as initially thought.

The most obvious link remains high U.K. bank exposure to debtors such as Ireland, with Lloyds Bank admitting that up to 54% of its loans to that country are impaired.

Investors are now waiting to see what HSBC Holdings PLC and Royal bank of Scotland Group PLC, the other two major U.K. lenders to Ireland, have to say about their Irish exposure.

The fact that there is no early end to the debt crisis is adding to sterling's woes.

With Irish debt now rated just above junk level and with the International Monetary Fund warning that more austerity will be needed, chances are that Dublin will be returning cap in hand for another bail out, even though the European Central Bank is already questioning the legality of the last one.

However, it is probably the failure of European Union leaders to seek a more long-term solution and prevent contagion to other debtors, such as Spain, Portugal and Italy, that is inflicting the most damage, with sterling now finding itself suffering a similar fate to the highly vulnerable euro.

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| Bloomberg | TNI FRX POV |
| Reuters | USD/DJ |
| Thomson | P/1066 or P/1074 |

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