

DAILY FX UPDATE

Thursday, January 9, 2014

FED MINUTES ARE MEDIUM TERM USD POSITIVE

- USD is mixed; with European currencies rallying & growth FX weak.
- Fed minute takeaway is a medium-term USD positive—pace of tapering could be increased with 200+ nonfarm prints in Feb & March.
- Fed—Yellen provides first interview to Time magazine.
- CAD trades to 3+ year lows, in tandem with rates; outlook is for further weakness in next 6-months. Today's data: housing starts & prices.
- EUR retraces yesterday's losses; ECB holds rates at 0.25%. Draghi likely to maintain dovish tone—language around inflation will be focus.
- GBP is flat as BoE holds rates at 0.5%; makes no change to asset purchase program or unemployment threshold.
- JPY is weak - BoJ Shirai supports accommodation if risk materialize.
- AUD is weak, ignoring stronger than expected retail sales at 0.7%/m.
- CNY softens from highs as CPI falls to 2.5% below Nov & expectations.

FX Market Update - Markets are mixed leading into today's ECB press conference and tomorrow's nonfarm payrolls report. Soft inflation data from China weighed on growth sensitive currencies (CAD and AUD) in the Asian session; with EUR supported by improving confidence. Global central bank policy has markets in data watching mode, leaving upcoming employment and inflation data as key releases for FX markets. C.S.

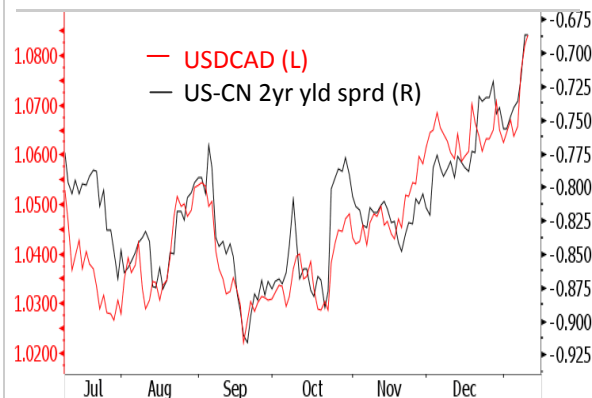
Fed minutes takeaway is a medium-term USD positive as majority of officials saw the marginal efficacy of QE purchases declining. As long as nonfarm payrolls continue close to 200k/mth and inflation does not fall further we would suggest that tapering is more rapid than the \$10bn per meeting priced in. Over time this should be USD positive. C.S.

Fed minute summary:

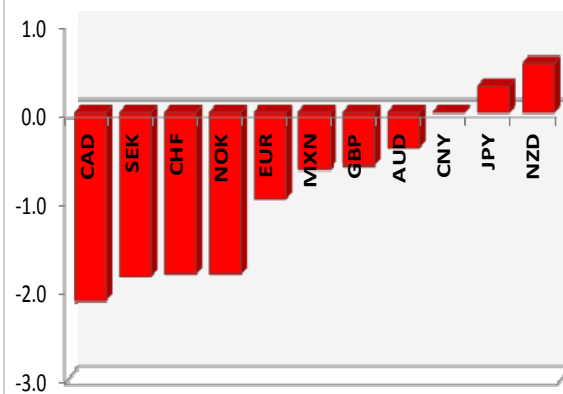
- **Pace of tapering from here** - measured, cautious and not preset.
- **Pace dependent on:** labour, inflation and the cost/benefit of QE.
- **The unemployment threshold:** retain 6.5% but provide qualitative guidance around what to do when crossed—it seems increasingly unlikely this will be lowered with the Fed instead framing how it will balance inflation and unemployment once crossed.
- **The decision to taper was based on:** increased confidence in economic growth, labour, inflation and financial market conditions. Inflation expected to move back towards target but watching carefully.
- **Financial stability risk:** there is some increased focus on financial stability risk, however the Fed judges these risks as moderate.
- **Fixed-rate, overnight reverse repo facility:** the potential importance of this facility once policy begins to be normalized is highlighted again by the extension of the program and ongoing work into how effectively the facility can put a floor on money market rates.

USDCAD (1.0840) • CAD has fallen to a fresh three plus year low, is down 0.2% from yesterday's close and is the worst performing primary currency leading into the open. CAD is trading at multi-year lows against the USD, GBP and EUR. Today's data includes housing starts, home prices and building permits, however these releases are unlikely to have the

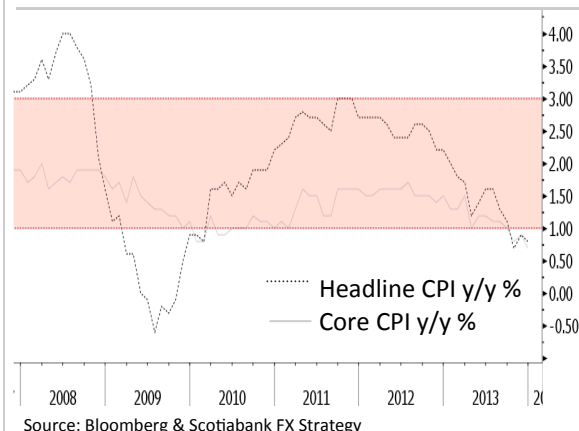
CAD TRADING IN TANDEM WITH RATES



FX RETURNS YEAR-TO-DATE AGAINST USD



EUROZONE DISINFLATIONARY PRESSURES



same CAD negative impact as the dual trade reports did on Tuesday. A weak trade report from Canada juxtaposed against a strong trade balance from the US reminded markets of the uncertainty that overhangs the Canadian export market as exports have so far failed to recover to the extent that many had hoped and as the impact of increased US oil production poses to the Canadian oil sector. Yesterday, the EIA released its short term outlook (see Suggested Readings or [link](#)), forecasting an increase in US daily crude production from 7.5bbl/d to \$85 bbl/day in 2014; as well as stable Brent and WTI prices in 2014, averaging \$105 and \$93, respectively. C.S.

CAD has been the worst performing primary currency year-to-date—see middle chart. With the weakness well correlated with interest rates (see top chart of the US-CN 2yr yield spread versus USDCAD). The key near-term risk is tomorrow's dual Canadian and US employment release. We expect CAD to weaken further in the next six months on the back of relative central bank policy, Canadian domestic economic underperformance, uncertainty over the outlook for the Canadian oil sector and building negative CAD sentiment. C.S.

USDCAD short-term technicals: bullish—all technical studies suggest further upside risk, with the RSI at just 70, leaving plenty of room before USDCAD is vulnerable to overbought levels. Option market pricing (risk reversals) has failed to move in tandem with spot; however this alone is not enough to position against the upward trend. Resistance from here lies the psychological 1.0900. C.S.

EURUSD (1.3605) • After weakening down to the mid 1.35s yesterday, EUR is retracing, trading just above 1.36 into the NA session. As expected the ECB left interest rates on hold at 0.25% as the market turns its attention to President Draghi's press conference. The tone is likely to be similar to December, noting a prolonged period of low inflation (see bottom chart) and anchored inflation expectations. However any shift in the tone around inflation would be an important negative development for EUR. We expect President Draghi to repeat the ECB's forward guidance, maintain a dovish tone, and reiterate that the central bank still has tools within its tool box that it can implement. We hold a year-end 1.25 EUR target. C.S.

Technicals: buy/sell signals and pivot levels

| | 30 Day Hist Vol | Spot | MACD | 9 & 21- day MA | DMI | RSI | Pivot 1st Support | Pivot 1st Resist. |
|-----------------|--------------------|--------|------|-------------------|------|-----|----------------------|----------------------|
| USDCAD | 6.2 | 1.0845 | buy | buy | buy | 70 | 1.0790 | 1.0873 |
| EURUSD | 5.1 | 1.3603 | sell | sell | sell | 45 | 1.3560 | 1.3641 |
| GBPUSD | 4.8 | 1.6455 | sell | buy | buy | 57 | 1.6395 | 1.6497 |
| USDCHF | 7.0 | 0.9095 | buy | buy | buy | 61 | 0.9071 | 0.9123 |
| USDJPY | 8.0 | 104.95 | sell | buy | buy | 63 | 104.65 | 105.18 |
| AUDUSD | 7.9 | 0.8884 | buy | buy | sell | 38 | 0.8849 | 0.8936 |
| USDMXN | 9.4 | 13.12 | buy | buy | buy | 56 | 13.02 | 13.19 |
| DXY (USD index) | 4.5 | 80.97 | buy | na | buy | 60 | 80.81 | 81.15 |
| EURCAD | 6.9 | 1.4753 | sell | buy | buy | 63 | 1.4679 | 1.4794 |
| GBPCAD | 8.9 | 1.7846 | buy | buy | buy | 68 | 1.7715 | 1.7914 |
| AUDCAD | 6.8 | 0.9635 | buy | buy | buy | 59 | 0.9597 | 0.9670 |
| CADMXN | 11.6 | 12.10 | sell | buy | sell | 41 | 12.02 | 12.17 |

BoC Noon Rate 1.0804

Source: Scotiabank & Bloomberg

1/9/2014

Suggested Reading

[Janet Yellen: The sixteen trillion dollar woman](#), Time (January 9, 2014) - In her first as Fed chief, provides thoughts on why the housing market is back on track, companies will invest, and more new jobs are on the way this year. She now has the world's largest economy in her hands.

[FOMC minutes try to reassure; plus an interesting par about financial vulnerabilities](#), C. Garcia, FT Alphaville (January 9, 2014)

[Fed faces bond market showdown over rates](#), M. Mackenzie, FT (January 9, 2014) - with long-dated Treasury yields having risen sharply higher over the past year ahead of the Fed's taper starting, the pressure point in the bond market is the two-year sector.

[Fed eyes bubble risks, minutes show](#), J. Hilsenrath, WSJ (January 9, 2014) - Fed officials turned their attention to the risk of financial bubbles as they scanned a brightening economic outlook and formulated a plan to gradually wind down their bond-buying program this year.

[Short-term energy outlook](#), EIA (January 2014)- expect Brent to decline to \$105/bbl in 2014 and \$102/bbl in 2015; while WTI average \$93/bbl in 2014 and \$90/bbl in 2015; with US domestic production increasing from 7.5 million bbl/d in 2013 to 8.5 bbl/d in 2014 & 9.3 in 2015.

EURUSD short-term technicals: bearish—all studies are in sell territory, a break below the 100-day MA at 1.3546, would accelerate selling pressure. We favour short and medium term short EUR positions. Support lies at the 100-day; while resistance lies at recent congestion at 1.3650. C.S.

GBPUSD (1.6460) • GBP is subdued, entering the NA session flat to yesterday's close. As expected the BoE left interest rates on hold at 0.5%, made no change to its £375b asset purchase program and did not adjust its unemployment threshold of 7.0%. The BoE could lower the level of the unemployment threshold or provide guidance around how the BoE will react once the threshold has been reached at an interest rate meeting or in its February 12th inflation report. Until then unemployment reports will provide a key input to the outlook for GBP. We are bearish, believing it has been priced to perfection. C.S.

GBPUSD short-term technicals: mixed which provides a warning to GBP bulls. Support lies at yesterday's low of 1.6377; with resistance at 1.6500. C.S.

USDJPY (104.95) • USDJPY is relatively quiet, trading within its week long range; with an upward trend still intact. In a speech, BoJ member Shirai suggested that he favours additional easing 'without hesitation' if downside risk materialize. C.S.

USDJPY short-term technicals: mixed as the MACD remains in sell territory even as the upward trend remains in tact. Support lies at 104.00; while resistance is at the January high of 105.44. C.S.

Today's Releases & Speakers

| Time (EST) | Country | Release | Period | Cons | Last | Significance |
|------------|---------|---|--------|--------|--------|--------------|
| 08:15 | CA | Housing Starts | Dec | 190.0K | 192.2K | med-high |
| 08:30 | CA | Building Permits MoM | Nov | -2.70% | 7.40% | med |
| 08:30 | CA | New Housing Price Index MoM | Nov | 0.10% | 0.10% | med |
| 08:30 | EC | ECB President Draghi Holds Press Conference After Rate Decision | | | | HIGH |
| 08:30 | US | Initial Jobless Claims | 4-Jan | 335K | 339K | med-high |
| 10:00 | US | House Monetary Policy Subcommittee Hearing on Fed Bond Buying | | | | low |
| 13:30 | US | Fed's George (non-voting hawk) speaks on economy; Q&A unknown | | | | med |
| 20:00 | US | Fed's Kocherlakota (voting dove) hosts Q&A on policy & outlook | | | | med |
| 21:00 | CH | Exports YoY | Dec | 5.00% | 12.70% | HIGH |
| 04:00 | NO | CPI MoM | Dec | 0.20% | 0.10% | med-high |
| 04:30 | UK | Industrial Production MoM | Nov | 0.40% | 0.40% | med |
| 04:30 | UK | Construction Output SA MoM | Nov | 0.80% | 2.20% | med |