

WORLD FOREX: Dollar Mostly Lower As China Boosts Sentiment

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LONDON (Dow Jones)--The dollar fell against the euro and sterling in European trading hours Monday as China's decision to allow greater flexibility in the yuan's exchange rate fuelled a broad-based rally for currencies perceived as risky.

The People's Bank of China said Saturday it would allow the yuan's exchange rate to be more flexible, a move widely seen as signaling it would let the yuan resume a gradual rise against the dollar. Beijing had essentially pegged the yuan to the U.S. currency since July 2008, as an emergency measure to help stabilize the Chinese economy amid the worsening global financial and economic crisis.

In reaction to the weekend news, sterling hit a fresh one-month high against the dollar, at \$1.4937, while the 16-country euro rose 0.3% as the decision by China's central bank over the weekend boosted sentiment in the currency markets across the board.

"The move is likely to support risk to some extent for several reasons," said Paul Robinson, an analyst at Barclays Capital in London, pointing out that trade tensions between the U.S. and China should ease as a result.

A stronger yuan should reduce the probability of China overheating, he said, adding it is also "likely to be an ongoing move towards a more balanced global economy in terms of the distribution of global demand."

Aside from its modest weakness against the euro and sterling, the dollar also weakened against other Asian currencies and commodity-linked currencies. The Australian dollar hit a fresh one-month high at US\$0.8844 from US\$0.8728 late Friday.

That reflects a rise in investor confidence, and in expectations that with a stronger yuan, China will be in a position to import more from Australia and other commodity-producing nations.

The dollar climbed against the safe-haven yen, again in line with more positive sentiment.

View the dollar's performance against the yen here:
<http://www.dowjoneswebsites.com/chart/view/4147>

However, the PBOC has stressed that it will not allow the yuan to rise quickly, limiting the scope of the move. The dollar-yuan exchange rate is still allowed to fluctuate by only 0.5% on either side of the central parity rate. Despite an initial surge in the yuan in over-the-counter trading, the official dollar rate by Monday's close in China was unchanged at CNY6.8275.

That means the run-up in currencies perceived as risky, or with the greatest trade links with China, could evaporate quickly. "From a theoretical point of view, we do not expect much more than an initial reflex move (in) the foreign exchange markets," said analysts at Commerzbank. "It seems that the effects of a possible appreciation of the renminbi on euro-dollar are often over-estimated," the bank's analysts added.

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Elsewhere, the Swiss franc hit a new record high against the euro overnight, jarring with the market's generally more buoyant tone. The safe-haven franc acts as a magnet for investors in times of stress, so it would normally be expected to fall in upbeat market conditions.

Instead, the franc spiked higher in the immediate aftermath of the Chinese move, with the euro sinking to a record low of CHF1.3665, and the Swiss currency remained close to these elevated levels for the rest of the European session, hovering around CHF1.3725.

Lutz Karpowitz, an analyst at Commerzbank said the rise in the Swiss franc is independent of the news from China and does not fit in to the overall asset-market rally. Instead, he said this marks a continuing reaction to the Swiss National Bank's decision to drop its currency-management policy last week.

Elsewhere in Europe, the region's emerging market currencies gained, again helped by the rise in risk sentiment.

At 0900 GMT, the euro was trading at \$1.2404, up from \$1.2370 late in New York Friday, according to trading system EBS. It had earlier climbed as high as \$1.2490.

The dollar was sharply higher against the yen, at Y91.33 from Y90.74, while the euro was at Y113.26 from Y112.26. The pound was stronger at \$1.4870 from \$1.4812.

The ICE Dollar Index, which tracks the dollar against a trade-weighted basket of other major currencies, was a little weaker at 85.48 from 85.699.

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