

DAILY FX UPDATE

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INFLATION IS THE KEY FOR FX AND IT IS RISING

- USD is weak; with no data expected today as market ignores geopolitical risk. Focus to turn increasingly towards July 30th Fed meeting.
- Building inflationary pressures important for central bank policy & FX. Upside or rising inflation surprises from AUD, CAD, UK & US.
- CAD is higher but still in range; retail sales today often volatile but will provide insight into strength of consumer.
- EUR is flat but traded to a fresh ytd low. Limited news flow.
- EUR crosses: EURJPY, EURGBP, EURAUD, EURCAD all dropped to fresh lows highlighting that downside pressure is broadly based.
- GBP is soft after BoE minutes prove less hawkish than expected. Carney speaks at 7:45am EST today.
- JPY is flat on limited news flow. Upcoming risk is trade & CPI.
- AUD rallies as CPI proves stronger than expected limiting the RBA.
- NZD is strong leading into the RBNZ decision (5pm EST today); rates are expected to increase to 3.5% but it will be tone that matters.
- CNY is strong leading into the flash HSBC manu PMI, expected at 51.0.

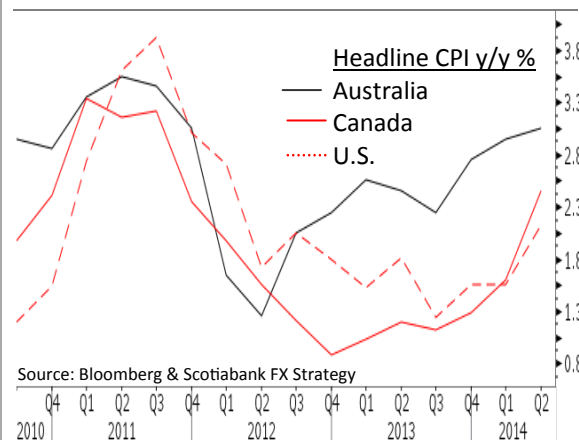
FX Market Update - Into the NA open markets are embracing risk with equities higher and a soft USD; however the US 10-year warns as it falls to 2.45%. Today there is no US data and no Fed speeches; leaving geopolitical risks as the core focus. Yesterday's US inflation data suggest that broadly based pricing pressures continue to build, this is also the case in Australia and Canada (see charts). This shift is likely to be accompanied by a shifting central bank tone and currency reaction. C.S.

USDCAD (1.0725) • CAD is stronger into the open, having gained 0.1% since yesterday's close. USDCAD has traded in a relatively tight 8-session range of 1.0709 to 1.0794; with the last two sessions suggesting there is significant indecision in markets. Rumours on potential M&A trades (see readings) and building inflationary pressures in Australia might have helped to support CAD in the Asian and European sessions. Today retail sales, typically a somewhat volatile release, is expected to rise 0.6% m/m and 0.3% m/m ex auto. The Canadian consumer has been relatively strong in 2014, helping to support an above consensus growth pattern. A string of stronger than expected economic releases has helped to firm the near-term growth outlook and today's release will also feed into this and prove important for USDCAD traders. C.S.

USDCAD short-term technicals: bullish—however as spot fails to make new highs there is building concern that technical signals will begin to fade. Support lies at the psychologically important 1.0700; while resistance comes in at the 50-day at 1.0794. C.S.

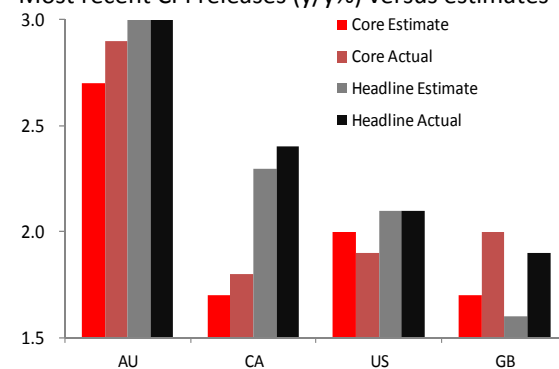
EURUSD (1.6470) • EUR is weak, flat since yesterday's close, but having broken below its recent range and the February lows. Downside pressure has also built on EUR crosses, with EURJPY, EURGBP, EURCAD and EURAUD all having dropped to fresh lows in the last 24 hours. Building on yesterday's comment, we see this build as suggesting there is ongoing downside pressure on EUR, which is likely to pull it lower still. News

INFLATIONARY PRESSURES PICK UP



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Most recent CPI releases (y/y%) versus estimates



INFLATION RELEASES KEY METRIC FOR AUD



flow has been quiet, with no fundamental releases except for mixed second tier data from France. We look for a near-term test of 1.3380. C.S.

GBPUSD (1.7040) • GBP is soft, having broken through support and now trading to a July low. Support from here lies first at the psychological 1.7000 followed by the June 25th low of 1.6953. The BoE minutes were the core focus, interpreted as less hawkish than expected by markets but still supporting our core view that the BoE is eager to enter its hiking cycle but that rate increases will prove gradual. Some of the takeaways include:

- 1) a 9-0 unanimous vote;
- 2) the risk of a Bank Rate hike derailing the economy was receding as the expansion was more established;
- 3) the path of rate hikes is likely to be gradual;
- 4) sustained economic momentum was looking more assured;
- 5) the lack of wage growth remains a core focus of the BoE and adds to uncertainty on the outlook;
- 6) the Bank Rate's path is highly dependent on developing economic conditions;
- 7) given persistent headwinds stemming from the financial crisis, the Bank Rate would ultimately remain below its historical level for some time.

The market reaction (of GBP weakness) highlights how much good news is already priced into GBP and one of the major risk factors for the currency. We hold a Q314 forecast of 1.72 and a Q414 target of 1.70. C.S.

USDJPY (101.40) • JPY is flat, having traded in a relatively tight range during the Asian and European session. News flow was limited as the market looks towards the release of Japanese trade data (7:50pm EST) today and CPI tomorrow. C.S.

AUDUSD (0.9450) • AUD is strong, having rallied 0.6% since yesterday's NA close after the inflation print proved stronger than expected. Headline Q2 CPI increased to 3.0%/y while the trimmed mean increased to 2.9%/y (well above both the Q1 print and the estimate—see inflation charts). The details suggest that the inflationary pressure is relatively broad based with q/q gains in every sub-sector. However, recent fundamental data releases have disappointed—in July alone the data has warned of a soft labour market, a wider than expected trade deficit and weak retail sales. All of which reduces the pressure on the RBA to hike interest rates (currently the market is pricing in no change over the next 12-months). We hold a Q314 AUD target of 0.94 and a year-end target of 0.92, both are above consensus. C.S.

TECHNICALS: BUY/SELL SIGNALS AND PIVOT LEVELS							Jul 23, 2014	
	30 Day Hist Vol	Spot	MACD	9 & 21- day MA	DMI	RSI	Pivot 1st Support	Pivot 1st Resist.
USDCAD	4.5	1.0726	buy	buy	buy	48	1.0707	1.0752
EURUSD	3.3	1.3468	sell	sell	sell	29	1.3439	1.3514
GBPUSD	2.9	1.7046	sell	sell	sell	48	1.7020	1.7084
USDCHF	3.9	0.9023	buy	buy	buy	67	0.8990	0.9044
USDJPY	3.5	101.41	sell	sell	sell	44	101.29	101.57
AUDUSD	6.4	0.9450	sell	sell	buy	59	0.9391	0.9480
USDMXN	5.8	12.94	sell	sell	sell	45	12.91	12.97
DXY (USD index)	2.7	80.75	buy	na	buy	65	80.58	80.88
EURCAD	5.0	1.4447	buy	sell	sell	35	1.4399	1.4514
GBPCAD	5.0	1.8285	buy	buy	sell	46	1.8243	1.8342
AUDCAD	6.6	1.0136	buy	buy	buy	57	1.0083	1.0162
CADMXN	5.4	12.06	sell	sell	sell	46	12.04	12.08
BoC Noon Rate		1.0745	Source: Scotiabank & Bloomberg					

Suggested Reading

[BoE vote 9-0 as some PMC see falling risk from rate increase](#), J. Ryan, **Bloomberg** (July 22, 2014) - The BoE said some members of its MPC have started to argue that the risk of a rate increase undermining the recovery has fallen as growth becomes more entrenched.

[Food fight hidden from view muddies BoE rates debate](#), E. Charlton, **Bloomberg** (July 22, 2014) - U.K. supermarkets may be masking the true scale of price discounting, complicating the task facing policy makers as they debate how long to keep interest rates at a record low.

[Fed worries about effects of its new interest rate tool on markets](#), M. Derby, **WSJ** (July 22, 2014) - Reverse Repos: the Fed thinks the new tool will play no more than a "useful supporting role," largely because of rising concerns about its potential effects on the financial system.

[Jobs are not enough](#), G. Ip, **The Economist** (July 22, 2014) - The economy is closer to full employment than the Fed had expected just a year ago with rate rises still at least a year away; however as Chair Yellen noted, rate hikes will be sooner if unemployment keeps falling.

[Repsol said to explore bid for Canada's Talisman energy](#), M. Baigorri, **Bloomberg** (July 22, 2014) - Repsol SA (REP) is exploring a bid for Talisman Energy Inc. (TLM) as it looks to deploy cash it received as compensation for the loss of its stake in Argentina's YPF SA (YPF).

TODAY'S RELEASES & SPEAKERS

Time (EST)	Country	Release	Period	Consensus	Last	Significance
08:30	CA	Retail Sales MoM	May	0.6%	1.1%	med-high
08:30	CA	Retail Sales Ex Auto MoM	May	0.3%	0.7%	med-high
10:00	EC	Consumer Confidence	Jul A	-7.5	-7.5	low
17:00	NZ	RBNZ Official Cash Rate	24-Jul	3.50%	3.25%	HIGH
18:45	NZ	Trade Balance	Jun	100M	285M	med
19:50	JN	Trade Balance	Jun	-¥642.9B	-¥909.0B	med
21:35	JN	Markit/JMMA Japan Manufacturing PMI	Jul P	--	51.5	med
21:45	CH	HSBC China Manufacturing PMI	Jul P	51.0	50.7	HIGH
03:00	SP	Unemployment Rate	2Q	24.90%	25.93%	med-high
	EU	preliminary PMI's: euro area, GE, FR; mfg, serv, composite				HIGH
03:30	SW	Unemployment Rate	Jun	9.0%	8.0%	med-high
03:30	SW	PPI MoM	Jun	--	1.1%	med
04:30	UK	Retail Sales Ex Auto MoM	Jun	0.3%	-0.5%	med-high

CONFERENCE CALL—USDCAD OUTLOOK

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This presentation is now available at your convenience.

The pre-recorded webcast is available at: <https://cc.callinfo.com/cc/playback/Playback.do?id=d1jkpt>

For just the presentation go to: www.scotiabank.com

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