Forex Focus: Confidence In Risk-Taking On the Rise

By Nicholas Hastings

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LONDON (Dow Jones)--For the first time in months, global investors appear more confident about taking risks.

This doesn't mean that they won't lose their confidence again but it does mean that the dollar might look more attractive.

This more 'risk on' mode has emerged for two reasons: fears of a double-dip recession in the U.S. have largely receded and worries about the European financial system are much reduced now that bank stress-test results have been published.

Of course, disappointing data from the U.S. or signs of some default in Europe could still send investors heading back into safe havens. But, the risks of more wholesale reversal in investment flows, as we have seen in recent months, aren't as high as they were.

Take Wednesday's disappointing 1.0% fall in U.S. durable goods orders and the Beige Book's rather tepid economic assessment. Both failed to knock the dollar sharply lower as they would have done only a week or two before.

See how the euro continues to struggle to establish itself over $1.30:

http://www.dowjoneswebservices.com/chart/view/4323

Evidence that investors aren't as defensive as they were can be seen in the decline of both the yen and the Swiss franc, two of the traditional safe havens that have attracted steady support in recent months, as well as the fall in the price of gold and the decline in bond prices in several key sovereign markets.

Fears of a double-dip recession in the U.S. could well recede further later this week, especially if U.S. GDP data Friday show that the economy continued to grow by a relatively strong 2.5% in the second quarter after expanding by 2.7% in the first.

Recent comments from Federal Reserve officials suggesting that they are less dovish than the market thinks, and that the central bank is prepared to ease monetary policy again if needed, have also helped to persuade many investors that the recovery isn't faltering quite as badly as they had feared.

Although there remain some concerns about the credibility of stress tests conducted on European banks over the last four months, investor support for euro-zone assets has returned and even European banks' share prices have rebounded markedly.

In the esoteric world of credit default swaps, which measure how much investors have to pay to insure debt against default, the gap between European and U.S. benchmark indexes has narrowed to virtually nothing now after hitting a record 23 basis points back in early May when the bank debt crisis was raging.

Of course, one measure of global risk appetite that could continue to steer many leading currencies is the performance of equity markets.

However, this time around, equity strength, indicating continued investor confidence, should play into the dollar's hands.

With the prospects of rate increases remaining very low elsewhere, any suggestion that U.S. yields could start to rise will ensure that the dollar attracts even more support.

Indications of this are not only visible in the euro's recent inability to make a sustained rally over $1.30 but in the dollar's retreat from its recent lows against the yen and calls from some analysts for long dollar positions against the Japanese currency to stay in place for now.

Early Thursday, the euro was being lifted by European buying with the single currency rising to $1.3032 by 0645 GMT from $1.2988 late on Wednesday in New York, according to EBS.

It also rose to Y113.74 from Y113.54 while the dollar slipped to Y87.27 from Y87.44.

Bloomberg TNI FRX POV

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 Reuters   USD/DJ
   Thomson   P/1066 or P/1074
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