

Daily Foreign Exchange Update

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USD UP ON CHINA AND COMMODITY/EQUITY WEAKNESS

- China's SAFE says it is still buying Treasuries; sees gold as an unlikely reserve vehicle.
- CAD weaker today but still outperforming helped by surging short term yields.
- EUR still trading within one month 1.3436 - 1.3839 range; which we expect to hold.
- Fears over downgrading of UK bank debt & negative sentiment weighing on GBP.

FX Market Update

European equities are under pressure following a mixed day in Asia, while US equity futures are losing ground and pointing to a negative open. These factors are contributing to the tone of risk aversion in the FX market today. The USD is well supported against most majors while the Japanese yen is the best performing currency by a wide margin. US government bond yields are ticking lower and away from two week highs, with Treasuries likely seeing some support from comments from the director of China's State Administration of Foreign Exchange (SAFE) **that US Treasury purchases are ongoing each day**. Gold is also moving sharply lower, also on comments from SAFE which suggested that **the metal would be unlikely to be China's primary investment used to diversify its reserve holdings** due to the risks posed by volatile price swings and the impact that a player the size of China would have on the market.

• AUD and CAD are outperforming (but lagging JPY and the USD), despite some weakness in the commodity complex as oil and copper are both down over 1%. Apart from the scandies, GBP is one of the most prominent laggards and has trended lower intraday to below the 1.50 level as weak housing and trade data, as well as the **threat of financial sector downgrades from Moody's** weighs on the currency. EUR is holding its ground reasonably well as currencies feel the pressure against the USD today, with the Eurozone fiscal credibility gap seeing some minor mending with stories circulating regarding the potential for the creation of a **European Monetary Fund (EMF)** to backstop countries under crisis pressure. Though this notion (a proposal of the German Finance Minister Wolfgang Schauble) is now making the rounds, there also seems to be a realization that the creation of an EMF would face significant legislative hurdles.

• The dollar index has continued to generally hold in a stable range between 79.80 and 81.30 for nearly three weeks, with only slight signs of easing. The comments from SAFE's director Yi Gang should provide the USD with an added tone of support in the near term. **Data from the US Treasury (see graphic) has suggested that China was perhaps making accelerated efforts to diversify out of US Treasury securities** in recent months, with a particularly large drop in Treasury holdings in December. The fear of reserve diversification out of the USD has for the time being moderated, helped by the sharp slide in EUR which used to be seen as an obvious and desirable choice for an alternative reserve vehicle currency. S.T.

Americas

USDCAD (1.0300) • CAD is outperforming despite the fact that it has lost 0.4% to the USD in early trading. Without any economic data today, CAD is at the mercy of financial market conditions and expectations regarding Friday's employment data. The first factor is unresponsive today as commodities are under pressure and the USD is generally well supported against the majors, boosted by the comments from China's SAFE and today's weaker equity environment. Expectations for a positive employment print have helped shorter term Canadian government bonds move lower, **sending the 2-year to its highest yield level in months yesterday at 1.54%**. It hasn't been since the September employment data (released on October 9th) that yields have moved so Canadian dollar supportive, which has helped to nullify the short term upside in US government rates (see graphic). USDCAD continues to be pressured towards its 2010 low at 1.0207, though relenting somewhat today which has brought **the first day in eight without a concurrent lower intraday high and intraday low**. Look for support in USDCAD at 1.0250 and resistance at 1.0340. S.T.

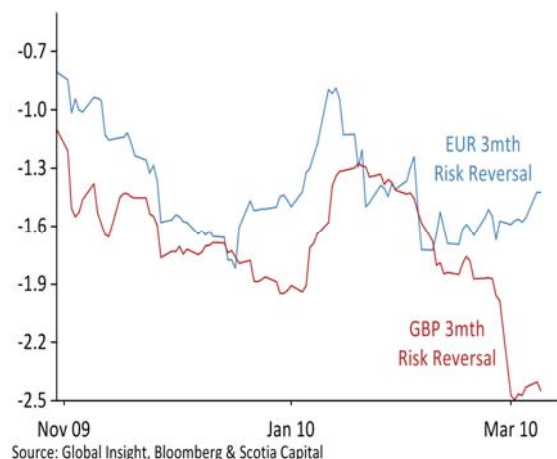
CHINA'S SAFE SAYS TREASURY BUYING IS ONGOING



CANADA SHORT TERM YIELD SURGE HELPING CAD



INVESTORS PROTECTING AGAINST GBP DOWNSIDE



Europe

EURUSD (1.3560) • EUR is a mid-performer today, having lost 0.6% against the USD and trading almost at the mid-point of its recent 1.3436 to 1.3839 range. This range has held since February 5th and as signs of EUR stabilization have increased, we expect this 400 point range to hold over the near term. • **Mixed comments from Fitch and weaker than expected earnings have put some downside pressure on EUR** as we move into the North American open. Fitch’s comments included: 1) that several of the weaker EU members have put in place sensible policies; 2) that it is unlikely that any country will withdraw from Euro Area; and 3) that German aid for Greece would likely be overturned by the courts. Still most indicators point to stabilization in EUR. • Today’s pivots (see table) point to the potential for buying pressure at 1.3514 and selling pressure to emerge at 1.3652. C.S.

GBPUSD (1.4950) • GBP is underperforming today, having lost 0.8% against the USD. Negative comments from **Fitch**, including that the UK’s fiscal adjustment is too slow, are weighing on the currency. Also impacting the currency are worries over the **potential for downgrades on the UK banking sector and today’s wider than expected trade balance**, which included a month-over-month drop in both exports and imports. • **Negative sentiment has stabilized towards euro, but has yet to do so towards sterling.** Until we see some signs of a shift in sentiment, GBP is most likely to face ongoing pressure. **Speculators** (as reported by the CFTC) have increased their short GBP position to a new record high of \$6bn. Risk reversals continue to portray a market that is eager to protect against further GBP downside. The

bottom chart on page 1, graphically shows that since February, EUR risk reversals have stabilized, while **GBP risk reversals have accelerated their drop.** Finally, news and **media coverage** remains negative GBP. Accordingly, there could still be more downside pressure on GBP before it too is able to stabilize. • **Technically, there are no warning signs on the charts that hint of a sudden reversal and instead most studies are firmly in sell GBPUSD territory.** A close below 1.50 would be bearish. Support lies at 1.4900 followed by last week’s low of 1.4784, Resistance comes in at the psychological 1.5000 followed by the 9-day moving average of 1.5083. Today’s pivots (see table) suggest that buying pressure will emerge at 1.4861, while selling pressure will be at 1.5118. C.S.

Asia / Oceania

USDJPY (89.75) • USDJPY was unable to break above its 50-day moving average of 90.60 yesterday and has drifted lower. The combination of today’s risk averse trading and repatriation of yen have been the key drivers over the last 12-hours. Interest rate differentials continue to be the most important driver of USDJPY. C.S.

USDCNY (6.8263) • In the Asian session, **SAFE has made significant comments with regards to their FX policies. In summary, many of the comments are not new, but together they point towards an intentional move to make some adjustments to currency policy in China.** This will be a slow but a much needed process. Today’s comments included: 1) China is trying to **open its capital accounts**; 2) an attempt is being made to develop **cross-border yuan** products to expand outbound investment channels; 3) **FX reserves** are already appropriately diversified; 4) The **US market** is very important to them; 5) China will try to keep **yuan stable**; 6) There is a desire to let market decide on **currency used to settle commerce.** • We expect that China is approaching the time when policy makers will once again allow a measured pace of yuan appreciation. We do not expect a sudden revaluation. Tomorrow’s **exports release, expected to climb 38.3% y/y, is an important hurdle for policy makers.** A strong release would bring the likelihood of yuan appreciation one step closer. C.S.

Key Pricing & Levels

	30 Day Hist Vol	Spot	1 Day Change	1 Week Change	100 Day MA	200 Day MA	Pivot 1st Support	Pivot 1st Resistance
USDCAD	9.9	1.0311	0.0039	-0.0054	1.0528	1.0752	1.0272	1.0330
EURUSD	10.0	1.3557	-0.0077	-0.0041	1.4362	1.4335	1.3514	1.3652
GBPUSD	9.9	1.4951	-0.0115	-0.0022	1.6106	1.6228	1.4861	1.5118
USDCHF	9.2	1.0790	0.0058	0.0028	1.0376	1.0494	1.0717	1.0821
USDJPY	11.2	89.78	-0.53	0.88	90.17	91.92	89.38	90.43
AUDUSD	13.6	0.9059	-0.0033	0.0030	0.9060	0.8714	0.9037	0.9108
USDMXN	12.2	12.70	0.02	0.04	12.93	13.11	12.63	12.73
DXY (USD index)	7.0	80.77	0.34	0.20	77.51	78.00	80.32	80.98
CRB Commodity		276.71	-0.22	4.00	275.85	265.17	N/A	N/A
Gold		1,116.30	-7.25	-17.40	1,113.70	1,041.19	1,108.43	1,130.96
WT Crude (Nymex)		80.23	-1.64	1.09	77.36	72.99	79.79	81.54
Nat Gas (Nymex)		4.53	0.01	-0.18	5.10	4.39	4.47	4.59
BoC Noon Rate		1.0286	CAD (close from Bloomberg not BoC):					1.0272

Pricing Source: Bloomberg

3/9/2010

Today's Releases & Speakers

	Period	Cons	Last	Significance	
9:30 AM	US Fed's Evans Speaks to Economists in Arlington, Virginia			Medium	
10:00 AM	US IBD/TIPP Economic Optimism	MAR	47	46.8	Low
10:00 AM	MX Trade Balance	JAN F	--	-332.6M	Medium
10:00 AM	MX Consumer Prices (MoM)	FEB	0.5%	1.1%	High
5:00 PM	AU RBA Deputy Bank Governor Lowe speaks in Sydney			Medium	
6:30 PM	AU Westpac Consumer Confidence	MAR	--	-2.6%	Medium
6:50 PM	JN Machine Orders (MoM)	JAN	-3.5%	20.1%	Medium
6:50 PM	JN Domestic CGPI (MoM)	FEB	0.1%	0.3%	Medium
7:30 PM	AU Investment Lending	JAN	--	1.9%	Medium
12:00 AM	CH Trade Balance (USD)	FEB	\$7.15B	\$14.17B	Medium
12:00 AM	CH Exports YoY%	FEB	38.3%	21.0%	Medium
2:00 AM	GE Trade Balance	JAN	14.5B	13.5B	Medium
2:45 AM	FR Industrial Production (MoM)	JAN	0.1%	-0.1%	Medium
2:45 AM	FR Manufacturing Production (MoM)	JAN	0.2%	-0.8%	Medium
4:30 AM	UK Industrial Production (MoM)	JAN	0.3%	0.5%	Medium
4:30 AM	UK Manufacturing Production (MoM)	JAN	0.2%	0.9%	Medium

Suggested Reading

- [European Monetary Fund Q&A](#), Ralph Atkins, **FT** (March 9, 2010)
- [Moody's Says UK Banks' Rating Lose Their Crutch](#), David Enrich, **WSJ** (March 9, 2010)
- [Spring Oil Rally Seems Less Likely This Year](#), Brian Baskin, **WSJ** (March 9, 2010)
- [Japan edges from America towards China](#), Gideon Rachman, **FT** (March 8, 2010)

Our Monthly FX Strategy Call is now available, please dial in at your convenience.

On this month's 20 minute call we discuss:

- 1) Has the EUR stabilized - the key signals
- 2) USDCAD outlook into year-end 2010

To dial into the call (the replay is available for 30 days)

Dial: 416-695-5800

Passcode: 16272369#

For more information please go to:

<http://www.scotiafx.com/conference/index.htm>

Conference call commands

Press 1 – Skip backward 5 seconds

Press 3 – Skip forward 5

Press 4 – Skip backward 5 minutes

Press 6 – Skip forward 5 minutes

Press 5 – Pause the playback

If you have any questions, please contact:

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The next call will be held on Wednesday March 10th, 2010.

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