Fundamental Analaysis for 15 March 2009

Contributed by Administrator
Monday, 15 March 2010

* Greek debt crisis continues to hang over the euro…

* Moody’s says the UK and US debt ratings are secure, for now…

* Swiss National Bank lets the franc appreciate…

* Lots of data on tap in the US this week…

And Now… Today’s Analysis!

Greek debt is the euro’s Sword of Damocles….

But the dollar got a chance to shine a bit this morning in early European trading, snapping three days of gains for the Euro. European finance ministers begin a two day meeting in Brussels this afternoon, but the German and French finance ministers damped speculation of a bailout for Greece. German Finance Minister Wolfgang Schaeuble continues to insist Greece must ‘go it alone’ and he was joined by French Finance Minister Christine Lagarde over the weekend. Both feel that 4.8 billion euros in budget cuts will put Greece back on track.

But the markets don’t agree, and the euro got hit; dropping almost a full cent from its highs on Friday. The euro had rallied back to within a smidge of $1.38, matching the 30 day highs for the common currency. The Greek debt crisis will continue to hang over the euro like the Sword of Damocles. Analyst has told the Greek story of Damocles to everyone on the desk, but its been a while since he wrote about it in the Pfennig, so here is a brief explanation of the ancient Greek story:

Dionysius (II) was a fourth century B.C. tyrant of Syracuse, a city in Magna Graecia, the Greek area of southern Italy. To all appearances Dionysius was very rich and comfortable, with all the luxuries money could buy, tasteful clothing and jewelry, and delectable food. He even had court flatterers to inflate his ego. One of these was the court sycophant, Damocles. Damocles used to make comments to the king about his wealth and luxurious life. One day when Damocles complimented the tyrant on his abundance and power, Dionysius turned to Damocles and said, “If you think I’m so lucky, how would you like to try out my life?”

Damocles readily agreed, and so Dionysius ordered everything to be prepared for Damocles to experience what life as Dionysius was like. Damocles was enjoying himself immensely… until he noticed a sharp sword hovering over his head, that was suspended from the ceiling by a horse hair. This, the tyrant explained to Damocles, was what life as ruler was really like.

Damocles, alarmed, quickly revised his idea of what made up a good life, and asked to be excused. He then eagerly returned to his poorer, but safer life.

So today’s Greek debt crisis is the euro’s Sword of Damocles, threatening to fall and slice through the common currency. Only time will tell if the Greeks will be successful in their efforts to refinance their debts. For now, the focus of international currency speculators is locked on this story, and until some other event or crisis draws their attention, the euro will continue to be fairly volatile.

One thing which could shift the focus of the currency markets is a story which appeared in today’s WSJ. Moody’s released their quarterly Aaa Sovereign Monitor report this morning, confirming the triple-A ratings of the US, UK, and Spain. But the report said these countries have moved ’substantially’ closer to losing their Aaa ratings as the cost of servicing their debt continues to rise. “At the current elevated levels of debt, rising interest rates could quickly compound an already complicated debt equation, with more abrupt rating consequences a possibility,” said Pierre Cailleteau, Managing Director of Moody’s Sovereign Risk Group. The US will spend more on debt service as a percentage of revenue this year than any other top rated country except the UK. According to the report, the US and UK are maintaining their Aaa rating because of their ability to raise taxes and force spending cuts on discretionary programs.

The pound continued to fall over the weekend, holding just above $1.50 as a poll showed the elections to be held shortly may end in a ‘hung’ parliament. A YouGov Plc poll published in yesterday’s Sunday Times showed Labour at 33 percent, the opposition Conservatives at 37 percent, and the Liberal Democrats with 17 percent. UK Prime Minister Gordon Brown stepped up his attacks on the conservatives, saying the Conservatives would ‘wreck the recovery’ with their planned budget cuts. A hung parliament would make it more difficult to tackle the budget problems in the UK, adding to the problems pushing the pound sterling lower.

Another report showed there are currently more wager on the pound weakening against the dollar than when George Soros made his fortune betting against the pound in 1992. Futures traders have over 8 times more wagers on the pound weakening vs. the US$ than when Soros forced the pound from the European Exchange Rate Mechanism. Seems like everyone is starting to climb aboard the bandwagon, a little late to the party, but still not good news for the sterling.

The Swiss franc rose to its strongest level in nearly 1 1/2 years against the euro this morning. A Swiss government report showed annual producer and import prices declined at the slowest pace in more than a year, dampening fears of deflation. Economic growth seems to be taking hold, and the Swiss National Bank has been quite in the currency markets, letting the franc appreciate. The SNB sold francs last year in order to hold down its appreciation vs. the euro, but they seem to be willing to accept a higher franc given the recent economic data. With the Greek debt problems continuing to keep the euro volatile, investors may be wise to look at the Swiss franc as an alternative.

The one currency which rallied vs. the US$ over the past trading day was the Canadian dollar, which was up slightly. Investors moved toward the Canadian dollar as they bet the Canadian central bank will move to raise rates earlier than their US counterparts. Recent data released over the past month show the Canadian economy is recovering a bit more quickly than here in the US. Interest rate markets are pricing in a 22 percent chance of a quarter point raise by the BOC at their June meeting, and a 100 percent chance of an increase at the July meeting. If the BOC moves prior to the FOMC, the Canadian dollar would likely move through parity; a level we haven’t seen since July of 2008.

The other commodity currencies of AUD and NZD pared their recent gains as risk returned to trader’s screens. The Moody’s report, and continued worry over the Greek debts has moved investors away from riskier assets, causing a pullback by both the Aussie $ and kiwi. These currencies will benefit whenever there is positive news regarding global growth, and get sold off on any news calling the global recovery into question. These currencies are momentum trades, and will continue to rise and fall with global economic predictions.

We have a pretty big week of economic data here in the US, and start the week off with the volatile Empire Manufacturing number, followed by the net TIC flows, industrial production, and capacity utilization all scheduled to be released today. Tomorrow will give us a picture of the US housing market, with Housing starts and building permits along with the Import Price Index. We will also get the FOMC rate decision, which is pretty much of a foregone conclusion with rates remaining at their current .25% level. Wednesday will bring us the PPI numbers along with mortgage application data. Finally, Thursday will be a busy data day with the weekly jobs data along with CPI, the Current Account Balance, and leading indicators for February.

Like I said, we have a full slate of economic data this week; so strap yourselves in, as this get a bit volatile. Running a bit behind this morning, so I will get right to the currency wrap-up:

Currencies today 3/15/10: American Style: A$ .9133, kiwi .7011, C$ .9818, euro 1.3727, sterling 1.5053, Swiss .9446, European Style: rand 7.400, krone 5.8426, SEK 7.0811, forint 193.55, zloty 2.8401, koruna 18.6025, RUB 29.3425, yen 90.71, sing 1.3968, HKD 7.7586, INR 45.618, China 6.8262, pesos 12.579, BRL 1.7624, dollar index 80.112, Oil $80.75, 10-year 3.69%, Silver $17.07, and Gold… $1,107.10