

July 2010

Positive lead from better than expected Australia's unemployment data, soaring Chinese exports and retail sales, fresh start-up of rate-hiking cycle in New-Zealand followed by hot talked revaluation of Chinese yuan had added a bit more juice to market sentiments in June, giving a new lease of life to equity markets around the world that had rattled throughout May over a potential slowing down in economic momentum. Risk aversion took a back seat further as steady flow of bad news on sovereign debtors in Euro zone came to a halt led by the optimism that China's move towards greater currency flexibility will reduce probability of China's overheating that would add towards a more balance global economy in terms of the distribution of global demand. In fact, there were a series of bond auctions across the Euro zone region which went largely successful, helping to convince financial markets that buyers aren't on strike, and that even the large debtors are still able to raise funds in the open market. At home, the same celebration was seen wherein the home currency, Indian rupee rose to a one-month high at 45.75 cheering the Chinese move, and mirroring gains in other Asian units.

However, later in the month its rally got ditched as large unwinding bets on higher-yielding assets and global flight to safety began after string of economic data's out of the most major economies particularly in US and China pointed to a notable loss of momentum in the recovery.

KEY PRICING & PERFORMANCE

Curr	Spot	1 Day	5 Day	1 Mon	3 Mon
CHF	1.0774	0.12	2.26	6.86	-1.32
JPY	88.43	-0.05	1.33	2.96	4.65
GBP	1.4945	-0.68	0.05	2.93	-0.7
EUR	1.2238	0.49	-0.51	-0.47	-8.69
NZD	0.6847	-0.49	-3.5	1.19	-3.04
INR	46.45	0.08	-0.57	-0.18	-2.96
AUD	0.8408	-0.09	-2.98	0.24	-7.81
CAD	1.0639	-0.02	-1.56	-1.11	-3.42
KRW	1221.80	-0.41	-2.81	-1.6	-7.51
SGD	1.3994	0.34	-0.74	0.11	0.11
TWD	32.13	0.03	-0.42	-0.51	-1.08
MYR	3.2365	0.37	-0.14	0.77	0.99
CNY	6.7818	0.23	0.47	0.68	0.65

Domestic Events

Fitch Ratings raised India's local currency rating outlook to stable from negative forecasting lower debt ratios on the back of strong economic growth and robust cash flows from telecom auctions.

India's exports rose by 35 % for the seven straight month & has exported \$33 billion worth of goods in the first two months of current fiscal --- April and May, as demand picked up for iron ore, oil and leather goods.

EGoM had approved to market link the fuel prices amid allowing an increase of Rs3.50 per litre of petrol, followed by a hike of Rs2 per litre of diesel and Rs35 per cylinder of LGP.

India's monsoon forecast has been revised up at 102 percent of the long-period average for the June-Sept season from an earlier forecast of 98 percent. The higher rainfall forecast is based on developing La Nina conditions.

India's main food price index rising to 16.90 percent in the year to June 12, higher than the previous week's annual reading of 16.12 percent. Meanwhile the fuel price index remained unchanged at 13.18 percent in the year to June 12.

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G-20 puts the focus on fiscal stability:

The G20 statement brought a focus on reducing fiscal deficits, rebalancing the global economy, financial sector reform, providing development aid and supporting free trade and investment, but perhaps the most important issues addressed (from a near term perspective) were the first two. On fiscal policy, the developed economies apart from Japan, which was recognized to be a special case, pledged at least to halve budget deficits by 2013 and "stabilize or reduce" government debt/GDP ratios by 2016. Furthermore, the G20 agreed that advanced economies facing deficits should boost national savings while surplus economies undertake reforms to rebalance their economies towards domestically driven growth. The Chinese won a small battle in that currency valuations were not directly addressed in the statement, likely in part due to the move on the renminbi.

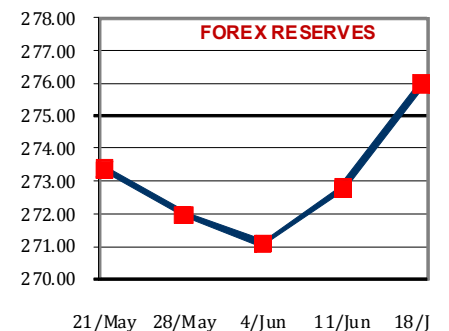
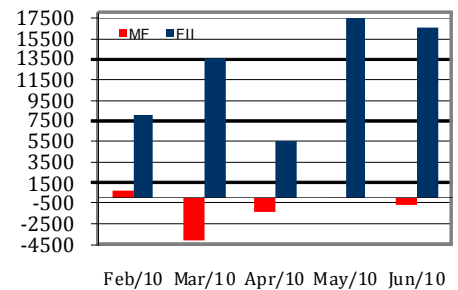
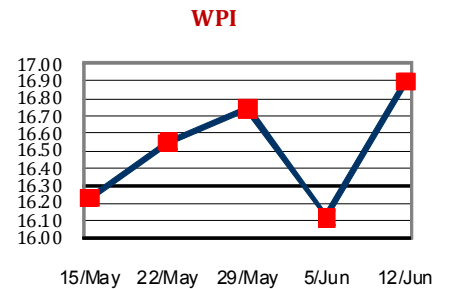
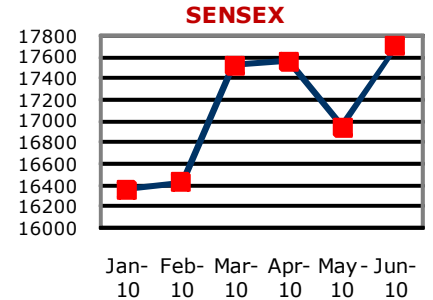
Swiss franc on a big bang:

Swiss franc soared heavily to smack through old records and hit life time highs against the euro after the Swiss National Bank signaled that it will step away from seeking to hold the currency down. Its gains were in line with SNB's recent upbeat assessment on country's economic outlook and revising up Inflation forecast as deflation risk seem to wane. The EUR fell as low as 1.3166 francs, the weakest since its 1999 launch. (See above table)

China not celebrating de-peg after a 23-month halt:

China's announcement that it will allow greater flexibility in its currency's foreign exchange rate breaking its 23-month peg against the dollar was greeted favorably - at least at first. But later disappointment came with investors showing their second thoughts over the pace of the renminbi's rise. It wasn't a free-float or a big revaluation—the yuan can still shift by only 0.5% a day against the dollar. The People's Bank of China has made it clear that it doesn't intend to stomach a rapid rise in the yuan, and indeed it allowed the currency to fall, not rise, against the dollar. Precisely, in broader perspective the step is taken in the right direction as undervaluation of Yuan will help China to provide more jobs to keep its exports going and secondly China, being a major holder of US. Dollars and dollar-denominated debt would help to retain its value of investments.

Domestic Trend



Capital control risk in Asia:

Asian central banks, faced with capital inflows and currency appreciation, have intervened actively to moderate FX appreciation. Unwillingness to allow excessive currency upside is one concern, while policymakers in many countries also are worried over the surge in inflows that now appears susceptible to abrupt reversals. Regulatory measures have already been introduced in Korea and Indonesia, while in other countries tweaks to the system are also said to have been considered though not necessarily implemented at this stage. While these have fallen short of outright capital control, strong inflows indicate tough policy choices ahead. The risks of policy action are highest for KRW and IDR, but measures affecting TWD cannot be ruled out.

Sterling back above \$1.50:

Sterling cherished merrily back over \$1.50 on removal of the dark cloud that had been hanging for months after U.K.'s cost-cutting budget and lack of negative surprises (in the budget) appeared to guarantee the country's top-notch debt rating. The pound has gained nearly seven cents against the dollar since Chancellor George Osborne outlined his fiscal plans, and news that one member of the Bank of England's Monetary Policy Committee had voted to raise interest rates in June has added fuel to the move.

Euro bent on fiscal restraint and banking stress:

Euro came under renewed pressure after its short-lived rally above \$1.24 on rising concern about the health of major European banks. Fitch's surprise decision to downgrade BNP Paribas and Standard & Poor's warning about the health of Spanish lenders helped to focus market attention on the stress tests that central banks are conducting on the region's major banks. The test which is expanded beyond the region's 25 major banks had increased pressure although its carried in an effort to reassure financial markets and ease funding pressures for European financial institutions in general. By the time results are out in July, confidence in European banks had been very low hurting euro's role as a global reserve currency.

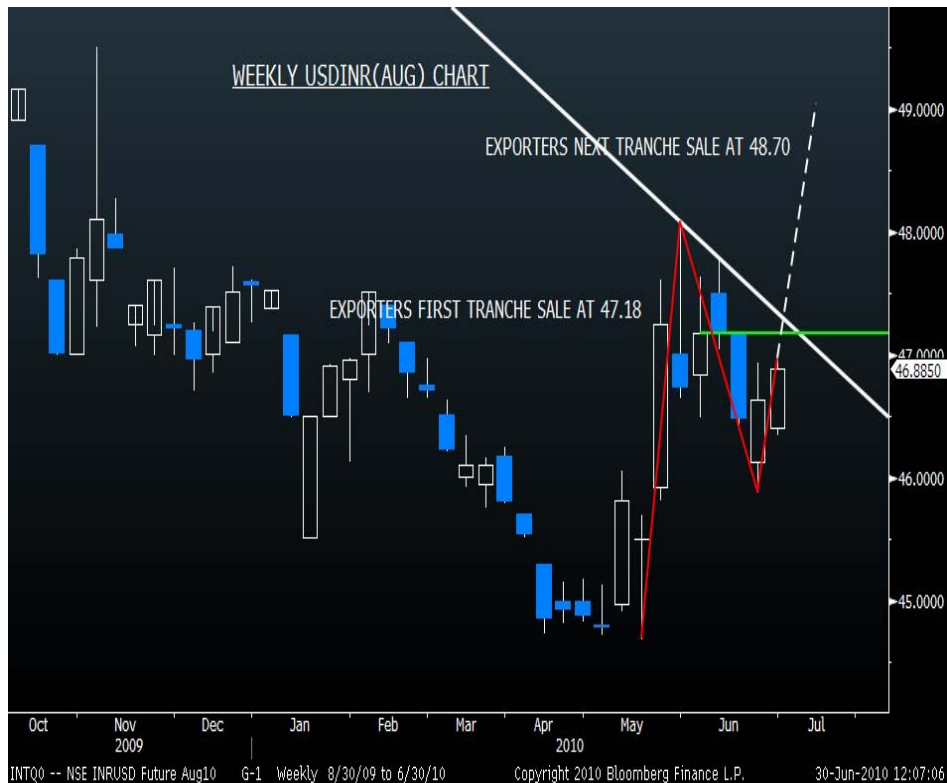
KEY CENTRAL BANK MEETINGS IN JULY

Country	Key Rate	Current Rate	Lst Chng	Chng	Next Meeting
Japan	Overnight Rate	0.10%	12/19/2008	-0.20%	7/15/2010
U.K.	Base Rate	0.50%	3/5/2009	-0.50%	7/8/2010
Canada	Overnight Rate	0.50%	6/1/2010	0.25%	7/20/2010
Euro Region	Refinance Rate	1.00%	5/8/2009	-0.25%	7/8/2010
Australia	Cash Target Rate	4.50%	5/4/2010	0.25%	7/6/2010
China	Lending Rate	5.31%	12/22/2008	-0.27%	n/a
Hong Kong	Base Rate	0.50%	12/16/2008	-1.00%	n/a
India	Repo Rate	5.25%	4/20/2010	0.25%	7/27/2010
Indonesia	Reference Rate	6.50%	8/5/2009	-0.25%	7/5/2010
New Zealand	Cash Rate	2.75%	6/9/2010	0.25%	7/8/2010
Mexico	Overnight Rate	4.50%	7/17/2009	-0.25%	7/16/2010
S. Korea	Call Rate	2.00%	2/11/2009	-0.50%	7/8/2010

Time to lock in Rupee gains:

(SPOT:46.44)

For the month ahead, we continue to hold cautious approach on Indian rupee as investors with rupee income should hedge dollar payables for a month or so. Meanwhile exporters should wait for some time to book for their export orders. This time, rupee is expected to get dumped against dollar as strong gains in EUR & GBP to heavily weigh on rupee.



- Importers can "BUY" USDINR(AUG) dollar at every dips between 46.90-47.15 for target of 47.75-47.90.
- While Exporters should "SELL" USDINR (AUG) at 47.20 and wait for next tranche at 47.75.

Although a global recession is unlikely but series of unenthusiastic data's across the globe is making it obvious for momentum to slow down deeply. Moreover, alarming downgrades by rating agencies on burgeoning debt concerns also gives a leeway for crises to further deteriorate.

Look for positive clues for rupee only if

- ✓ Depreciation in yen against the dollar gives a leeway to widening of carry-trades especially against the growth & commodity linked currencies like AUD, CAD & NZD. There can be potential intervention by the Japanese government as levels below 90 are unjustified. In his latest verbal warning made by the New Japan vice finance minister Ikeda commented in an interview with Dow Jones that he "will try to prevent excessive yen strength" as "a weaker yen is positive for the economy in general.
- ✓ Return of rate hike cycle in Asia with Korea taking a lead. India's policy meet is on 27th July. Rate hike speculation may support rupee on liquidity ground.
- ✓ Local inflationary pressure gets eased to some extent on approach of normal monsoon across the nation.

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