

1<sup>st</sup> December 2008

# Market Insight

## Sterling takes a tumble

The British Pound continues to look weak despite finding some strong support against the USD, EUR and CHF in the week beginning 23<sup>rd</sup> November 2008. Market participants are looking ahead to the UK interest rate decision on the 4<sup>th</sup> of December with most analysts expecting an interest rate cut of at least 0.75%. So far this year, Sterling has fallen 22% against the USD, 16% against the EUR, a hefty 36% against the JPY and 19% against the CHF. The severe effects of the US housing market collapse that have led to the 'credit crunch' have urged investors to look for low risk, safe haven currencies such as JPY, CHF and to a large extent the USD despite the credit related problems we are seeing today originating in the US.

EUR/GBP has been very bullish since the start of October for several reasons. Since the drastic exacerbation of credit market problems in September, the interest rate outlook for all currencies has changed significantly. Six months ago most central banks were contemplating and even leaning towards raising interest rates in order to combat inflation. Inflation figures and projections in the UK, EU and US were all well above widely accepted targets which gave central banks a problem of having to choose between capping inflation but reducing growth and maintaining growth but allowing inflation to stay elevated. Very high commodity prices were the main factor behind inflationary concerns in the middle of this year; this problem has now abated which has removed the main obstacle for central banks to reduce interest rates.

The interest rate outlook for all G10 currencies is now very dovish. However, as all central banks are now scrambling to ease monetary policy, they are doing so at different levels of magnitude. The ECB has been reducing rates at a more measured pace in comparison to the Bank of England which has given the EUR a strong bid since September. Although EUR interest rates were much lower than GBP in the early part of this year, they are now higher which means that investors holding their funds in EUR will receive a higher level of return compared to those holding their funds in GBP.



### Market Research

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