



Key News

- [U.K. Economy Shrank 0.2% in Third Quarter, Less Than Previously Estimated](#)
(Bloomberg)
- [Brazil Has No Reason to Keep Increasing Currency Reserves, Freitas Says](#)
(Bloomberg)

Quotable

“Investment in fixed assets such as factories and the rail network accounted for more than 95 percent of China’s 7.7 percent growth in the first three quarters of 2009 and made up 45 percent of gross domestic product, which is higher than any major economy in history, according to Morgan Stanley Asia Chairman Stephen Roach.”

[Bloomberg](#)

FX Trading – Europe Baking its Own Cake

Will the world economy be able to continue its recovery process as global monetary stimulus measures are phased out?

That’s a good question; and I doubt I can sufficiently answer it ... except to say that it’s probably a lot easier said than done.

But as far as how currencies might be affected by the withdrawal from stimulus, here’s how Joachim Fels, Manoj Pradhan and Spyros Andreopoulos of Morgan Stanley seem to think the major central banks will fall in line with interest rate moves:

“We expect the beginning of the exit from super-expansionary monetary policies and its implications to be the dominant global macro theme in 2010. We will discuss details of the likely monetary exit strategies across countries in next week’s year-end *Global Monetary Analyst*. Here, it suffices to say that we expect the Fed, the ECB and the PBoC to move roughly in tandem and raise interest rates from 3Q10, with the Bank of England following in 4Q. Some, like the central banks of India, Korea and Canada, are likely to move earlier, while others, such as Japan, will lag behind.”

Yesterday we sent around a news piece to our paying members that talked about how maybe the excessive stimulus and bailout mentality is returning to the financial system the abnormal risk taking and irresponsible practices that sparked market failure, especially in Europe.

That makes us wonder whether the Morgan Stanley trio’s forecast for the ECB and Fed to move in tandem upon exit is a low probability bet. Based on hundreds of billions of euros in writedowns expected in 2010 and the fact that European banks dominate (as a

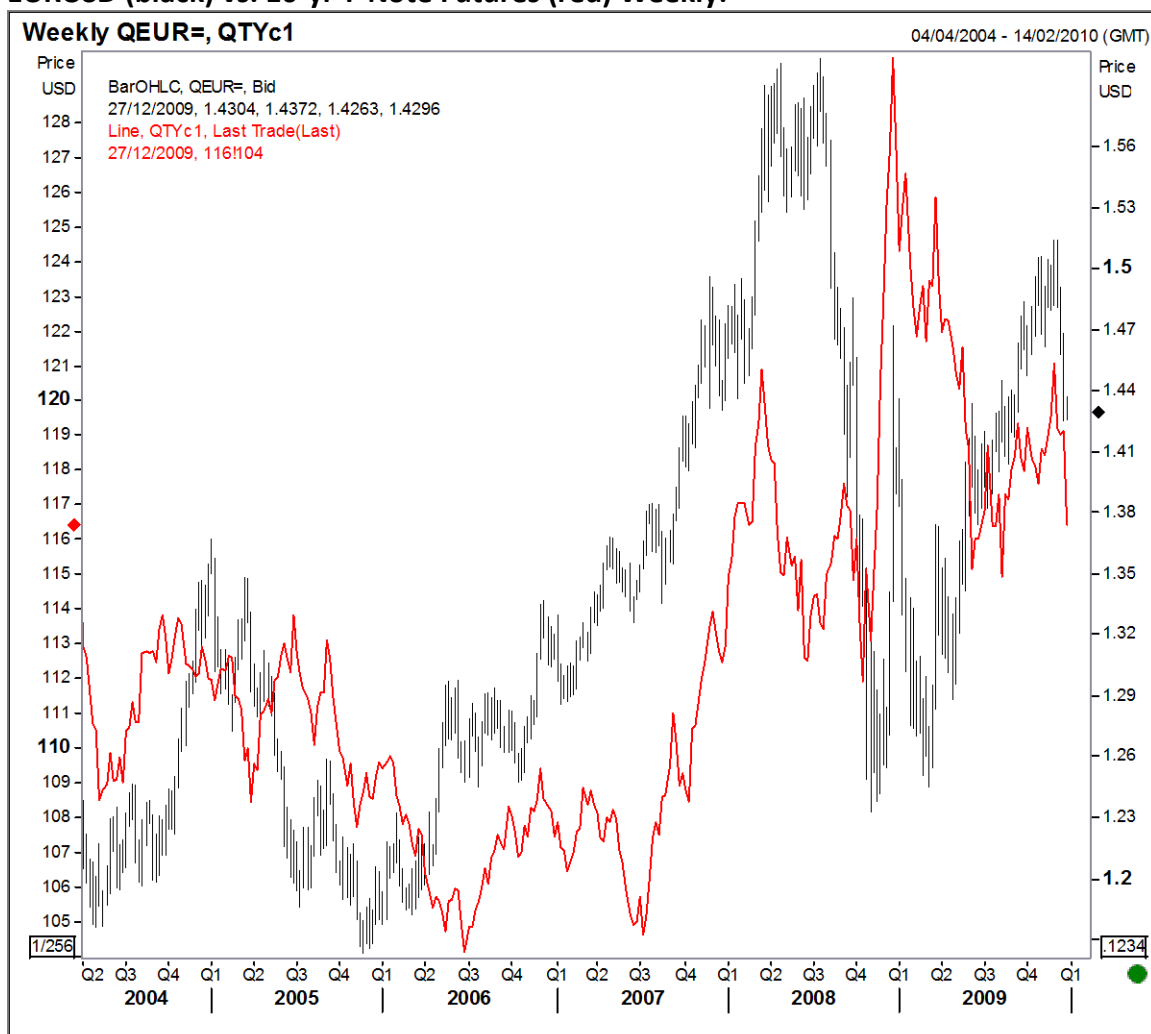
percentage of assets) the global financial system, we seem to think the ECB may be a bit slower to its six-shooter than the Fed.

But when we make a statement like that – anything that attempts to play up the US as being in a less unfavorable position than one of its counterparts – we’re almost certainly reminded by our readers that the US owes a lot of money to China ... and China is going to stop buying US treasuries ... Zhou said such and such ... or whatever.

Ok, fine – I concede. The US is no model of fiscal discipline. Not by a long shot. But much of that is baked into the cake. And that in and of itself is part of the reason that the items we expect will impact Europe are not already baked into the cake.

Assuming we’re not cutting off our nose to spite our face, then the ECB will lag ... and so will the euro as we push through 2010.

EURUSD (black) vs. 10-yr T-Note Futures (red) Weekly:



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