

**UBS Investment Research**  
**The Morning Adviser**
**RBA To Cut Next Week**

31 May 2012

[www.ubs.com/fx](http://www.ubs.com/fx)

- The latest batch of Australian economic data overnight confirmed that non-mining sectors of the economy continue to lose momentum. As a result, our Australia economics team now thinks the RBA will lower the cash rate by 25 bp on Tuesday, and are still looking for a total of 50 bp of easing by August. The euro meanwhile managed to stabilize – it seems investors are now questioning the merits of holding on to a bearish directional view over the next 48 hours in the face of unpredictable month-end flows today and the payrolls report on Friday. The remote possibility of ECB President Draghi hinting at a future policy response in today's parliamentary testimony may also have helped arrest the euro's descent for now. EURUSD risks would still appear to be skewed to the downside in our view given the concept of Eurozone bonds is still facing stiff resistance from Germany and the Netherlands; and the political and practical hurdles to any euro-wide bank recapitalisation scheme are significant. Indeed no material policy decisions seem likely ahead of the Greek election on June 17, portending more nervous trading in the interim. The Greek election itself is still too close to call, but the resilient public support for SYRIZA should continue to weigh on the euro. Of the three polls released on Wednesday, one showed SYRIZA in the lead over the New Democracy (30.0% vs 26.5%), another showed a dead heat (at 24.5%), and the third put the New Democracy on top, albeit by a slim margin (23.4% vs 22.1%). GBPUSD remains under pressure, as BoE data confirmed another month of net outflows from overseas gilt investors and the Bank's Chief Economist Dale highlighted the risks to the UK economy from the Eurozone crisis. The yen continues to sport a firm profile, with Deputy Governor Yamaguchi's claim that the domestic economy is in better shape than expected further dampening expectations of bolder BoJ action. Japan's Vice Finance Minister Nakao served reminder of the intervention threat, reinforcing our view that yen bulls will still have more room to run on the crosses than USDJPY.

**Key Events**

31 May 2012			Source: UBS Global Economics				
Country	GMT	Release/Event	Frequency	UBS	Prev/Revised	Consensus	Actual
<i>Euro Area</i>	<i>07:00</i>	<i>ECB's Draghi Speaks</i>					
<i>Germany</i>	<i>07:55</i>	<i>Unemployment Rate sa (May)</i>	<i>%</i>	<i>6.80%</i>	<i>6.80%</i>	<i>6.80%</i>	
<i>Norway</i>	<i>08:00</i>	<i>Unemployment Rate (May)</i>	<i>%</i>	<i>2.60%</i>	<i>2.60%</i>	<i>2.40%</i>	
<i>Euro Area</i>	<i>09:00</i>	<i>Euro-Zone CPI Estimate (May)</i>	<i>y-o-y</i>	<i>2.50%</i>	<i>2.60%</i>	<i>2.50%</i>	
<i>United States</i>	<i>12:30</i>	<i>GDP (Annualised) (Q1 S)</i>	<i>q-o-q</i>	<i>1.90%</i>	<i>2.20%</i>	<i>1.90%</i>	
<i>United States</i>	<i>12:30</i>	<i>Initial Jobless Claims (May-26)</i>	<i>lvl</i>	<i>370K</i>	<i>370K</i>	<i>370K</i>	

**Research Spotlight**
**Cash Is King In Europe**
**UBS Global Economics**

- The internal deconstruction of the euro is accelerating. We believe that the Eurozone has the tools to fill the hole the private market is creating - and that this process will leave northern Eurozone countries with such large receivables from the south, in excess of EUR1 trn, that Eurobonds will become necessary. Eurozone bank deposit guarantees and bank recapitalization schemes would be powerful if they proved durable, and to be durable they must be domestically driven and financed. Please see <http://www.ubs.com/fx> for details.

## EUR

Targets: EURUSD 3m 1.25, 12m 1.15

- Ireland holds a referendum on whether to adopt the EU's Fiscal Compact today. Exit polls released after polling booths close at 21:00 GMT on Thursday will likely provide the first indication of the outcome, although final official results are not expected until Friday afternoon. The latest opinion polls suggest the 'yes' camp is in the lead with 49% of those surveyed saying they will vote yes, 35% backing a 'no' vote, and 16% undecided.
- Italian sovereign 10-year yields rose by 16bp to a four-month high of 5.9% as the government fell short of its target at yesterday's bond auction. It sold EUR5.73 bn against a maximum target of EUR6.25 bn. Meanwhile Spanish 10y yields are now perched just 13 bps shy of a new euro-lifetime high.
- EU Commissioner Rehn said he is "ready to propose" giving Spain an extra year to take its fiscal deficit back below 3% of GDP. The EU Commission also said it is willing to "envisage" direct ESM bank recapitalisations and the establishment of a "banking union" that would allow Eurozone countries to share the burden of bank failures. We note however that the Commission often champions pro-integration policies which are ultimately dismissed by the governments of EU states.
- The Eurozone economic confidence index dropped to 90.6 in May from 92.8 in April against the consensus of 91.9. Loans to the private sector in the Eurozone grew 0.3% y/y, the slowest pace in two years, while Eurozone M3 grew by 2.5% y/y in April (prior: 3.2%, consensus: 3.4%).

## GBP

Targets: GBPUSD 3m 1.62, 12m 1.44

- UK April mortgage approvals came in at 51.8k, a little better than the 50.1k expected by markets. The March figure was revised up to 51.1k from 49.9k. M4 growth came in at +0.7% m/m and 3.8% y/y. This is the measure of money that is watched by the MPC. It is expanding at its fastest pace since Q1 2009. All told, the data have been a little better than expected and, at the margin, supports our call of no QE expansion at the June meeting.

## AUD

Targets: AUDUSD 1m 1.00, 3m 0.97

- Actual capex spending in Q1 was stronger than expected at +6.1% (cons. 4.0%), and capex spending intentions were also firm. However, our Australia economics team note that this was largely due to a buoyant mining sector and that the rest of the economy continues to lose momentum. The sharp fall in residential building approvals (-24.1% y/y vs. cons. -13.8%), confirms this. They now expect the RBA to cut 25 bp off the cash rate at the upcoming meeting on Tuesday.

## FX Technicals

### USDJPY clears 79.00

EURUSD	BEARISH	Downtrend extends; a clearance of 1.2368 has opened up the way towards 1.2152. Resistance is at 1.2506.
USDJPY	BEARISH	Yesterday's sell-off took out support at 79.00 exposing 78.36 next. Resistance is at 79.82.
GBPUSD	BEARISH	Abrupt sell-off through 1.5517 has exposed 1.5328. Resistance is at 1.5603.
USDCHE	BULLISH	The pair rallied yesterday; the focus is now on 0.9776. Support lies at 0.9529.
AUDUSD	BEARISH	The pair pressures 0.9690/64 support area; a confirmed break here would trigger further weakness towards 0.9600. Resistance is at 0.9898.
USDCAD	BULLISH	The focus is on 1.0319; a break here would signal further strength towards 1.0389. Near-term support is at 1.0204.
EURCHF	NEUTRAL	Resistance is at 1.2076, while support lies at 1.2000.
EURGBP	BEARISH	Momentum is negative; a break below 0.7950 would expose 0.7850. Resistance is at 0.8046.
EURJPY	BEARISH	Support at 97.69 has also given way opening 97.05. Resistance is at 99.45.

\*NOTE: The trend for each currency pair as defined in the table is determined by our proprietary model and is independent of our discretionary interpretation of price action

Source: FX Strategy