BNP PARIBAS FX daily strategist

US Edition

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8 March 2004

Market Strategy

The German weekly magazine '**Der Spiegel' is running a report that the FinMin is working on a strategy to allow the issuance of foreign currency denominated bonds,** and to shift the bulk of new euro issuance to the front end of the curve. In addition, swaps are being considered to take advantage of lower interest rates on the front end of the euro curve, in an attempt to reduce the budget deficit in the short-term. 'Spiegel' insists that this operation increases long-term funding risks for Germany, especially at times of rising short-term interest rates.

The US February labour market report was weak. Not only did payrolls increased by only 21k, the household sector reported a decline of 265k in employment in February, suggesting that underlying labour market conditions are weaker than originally assumed. So far, strong household employment data allowed the market to believe that payrolls would increase just after a short delay. Over the past three months the household survey showed an increase of 59k jobs per month, while the payroll survey averaged 42k.

Cost differentials and undervalued Asian currencies force US companies to adjust cost structures further delaying employment, keeping deflationary pressure intact and suggesting the FED will keep monetary policy accommodative beyond summer.

US yields have entered a new trading range and the 10-year Treasury yield is expected to decline to 3.6%. Lower interest rates and yields put the USD under renewed pressure.

EURUSD should test 1.2490/1.2590, but a break of the latter is required to resume the medium term uptrend.

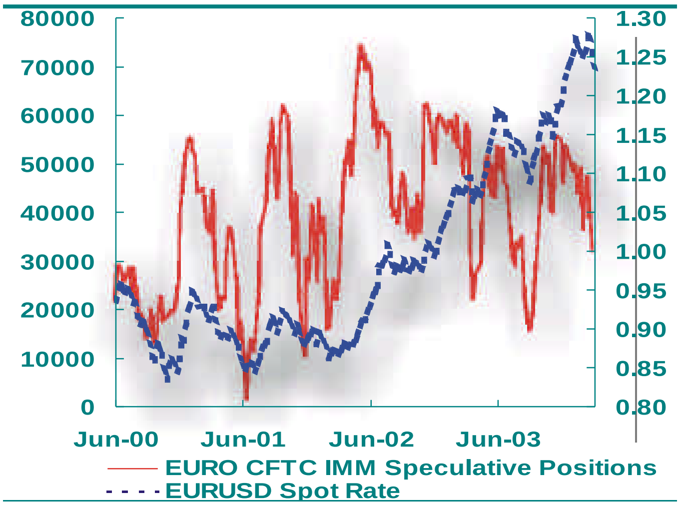
Meanwhile, Japanese monetary authorities continue to intervene. **Friday's intervention might have reached USD20bln** providing support for US asset markets, explaining the supportive US equity market reaction after the release of the weak payroll data.

Japanese monetary authorities are trying to keep USDYEN supported ahead of the fiscal year end. Most Japanese companies are now using 'mark to market' valuation principles. A weak yen not only pushes up Japanese equity prices, it increases the valuation of foreign held assets in yen terms. Accordingly, current yen weakening intervention is seen as a measure to ensure companies are not required to write down asset values by using the new accounting system. The BOJ is likely to protect Friday's interim 111.40 high, which has become support.

Major Data Releases and Events

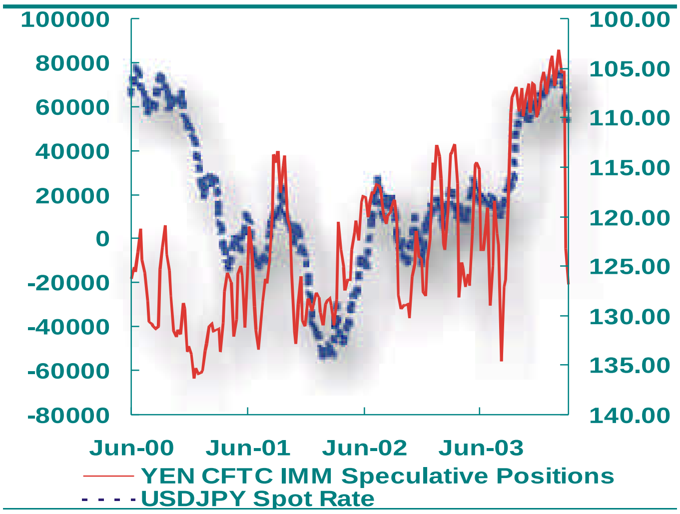
GMT	Country	Data release	Market	Last
13:15	CA (Feb)	Housing Starts	215K	195.5
18:00	UK (Feb)	UK BRC Retail Survey y/y		
	EU	Ecofin meeting		
		Tuesday 9th		
05:00	JP (Jan)	Mach Orders m/m	-2.0%	8.1%
		Mach Orders y/y		18.4%

Chart 1: Euro position adjustment has made little progress



Source: IMM/BNPP Note: Despite the substantial EURUSD decline witnessed from mid February until last week the market has made little progress in adjusting euro long positions. In the absence of real money buying the euro again, EURUSD will remain heavy despite the weak February US labour market report released on Friday. We expect EURUSD to move to 1.2490/1.2590 early this week, but given current market positioning it would take weak US retail and consumer confidence numbers, due on Thursday/Friday to push EURUSD above that significant resistance.

Chart 2: USD: Yen position adjustment complete



Source: IMM/BNPP Note: Short-term yen positions have reversed from long to shorts. Friday's perceived yen-weakening intervention is estimated to have reached USD20bln. Asian currency reserve data have been released this morning indicating that Asian reserves increased by USD165bn in January/February. USD103bln of this reserve increase is due to the very aggressive Japanese intervention activity.

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8 March 2004

Market Focus

CAD fundamentals still supportive

USD/CAD's surge to 1.3580 on Wednesday proved to be short-lived, with the currency pair subsequently plunging over four cents by the end of the week. The Bank of Canada's 25 bp rate cut Tuesday was well anticipated and as such did not result in sustained downward pressure on the CAD. Expectations of future BoC policy fluctuated in the following days, with the fall in June and Sep BA futures significantly reducing the perceived chance for another 25 bp rate cut by Wednesday. However, BA's rallied again on Friday, not due to specific Canadian developments but rather to those in the US, as weakness in the February employment report sent US interest rates plunging, with spillover effects on Canadian yields.

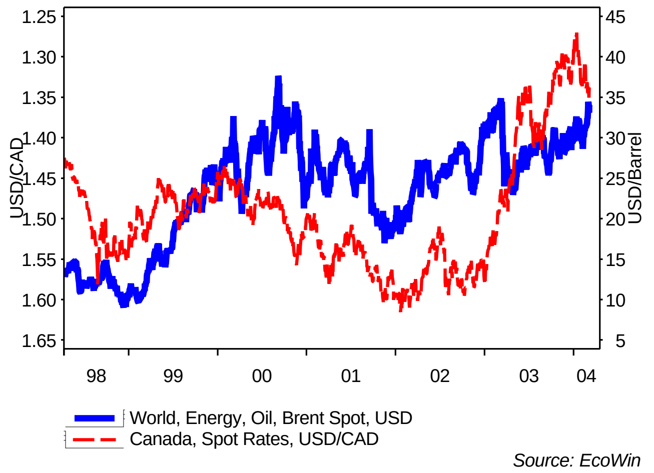
And that highlights one of the problems and uncertainties facing both the BoC and the CAD. Domestic conditions in Canada remain relatively good, but continued sluggishness in the US remains a threat to Canada's growth, especially with the CAD trading at its highest levels since the early-to-mid 1990's. In its statement Tuesday, the BoC noted that external demand has been slightly stronger than expected, but given the continued sluggishness in US labor markets, and the level of the CAD, they must still perceive risks on that front. That said, we also observe the continued rise in oil and gas prices as a potential positive for Canada's trade accounts, as energy counts for roughly 15% of Canada's total exports. The January trade data is due March 10 and will be a focus for the market.

Domestically, conditions in Canada remain fairly sound. Although the BoC noted that final domestic demand has been slightly weaker than expected, most indicators are still pointing to continued recovery this year. Indeed, the Ivey PMI index rose to 59.6 in February, the highest in eight months and reflecting strong output in the economy. Moreover, the employment index also rose to 54.9 from 50.4, suggesting continued hiring. Continued improvement in the labor market implies better consumption going forward, adding to the cycle of improvement in the broader economy. More specific news on the labor market will come with the February employment report, due March 12.

In terms of market developments, some observers have pointed to sizeable pullbacks in the AUD and NZD, and suggesting this implies downside risk for the CAD. However, recall that USD/CAD bottomed below 1.2600 back in January, suggesting that it has already sustained the bulk of its "corrective" phase, something the AUD and NZD have yet to fully experience.

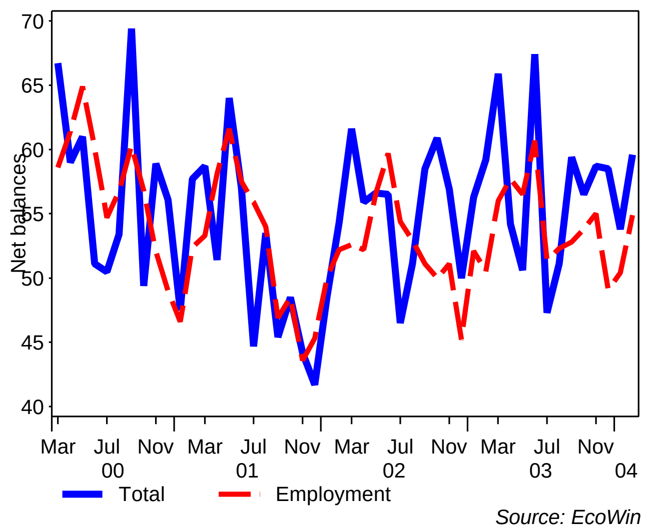
On balance, we maintain our positive outlook on the CAD. The decisive break of the January uptrend Friday adds the case for further near-term USD/CAD declines. Some support is likely at 1.3135, the 50% retracement of the 1.2685-1.3585 rally but on balance, we continue to favor further declines in the coming weeks.

Chart 1: Oil Prices and USD/CAD



Source: EcoWin. Note: Strength in the Canadian dollar has started to weigh modestly on Canada's trade surplus, a factor behind the BoC's 75 bp of easing since last summer. However, one potential support for Canadian trade has been the rise in oil and gas prices, given that energy accounts for roughly 15% of total Canadian exports.

Chart 2: Overall PMI and Employment Component



Source: EcoWin. Note: The Ivey PMI jumped to 59.6 in February, much better than expected and consistent with strong output in the economy. Moreover, the employment term rose to 54.9 from 50.4, suggesting continued hiring which in term implies scope for better consumption going forward.

08 March 2004, London: 12:00 GMT

EURUSD Outlook

EURUSD rallied to 1.2430 on Friday, but has stayed within a consolidative range in Asian and European trading. The 1.2430 resistance is defined by upper trend line resistance intervening on daily charts and while we expect the euro to overcome this level a re-test of 1.2310/1.2270 should be seen first before moving higher to 1.2590. German research institutes have revised their growth outlook lower, using the current euro valuation as an excuse. The weak US labour market report is likely to impact the currency market in the medium–term, especially if weak labour market data spills over into weaker consumer demand. There are some worrying signs: The household survey weakened and is now in line with the weak reading of the payroll survey and wages paid have come down. In fact, US wage growth has slowed to the weakest reading in 18-years only showing a 1.6% yoy growth rate. US February retail sales on Thursday and the consumer sentiment index release on Friday will be key. The weakness of the US job market is due to cost differentials between Asia and the US forcing US companies to dampen costs and to increase productivity. Undervalued Asian currencies increase the competitive disadvantage of US producers.

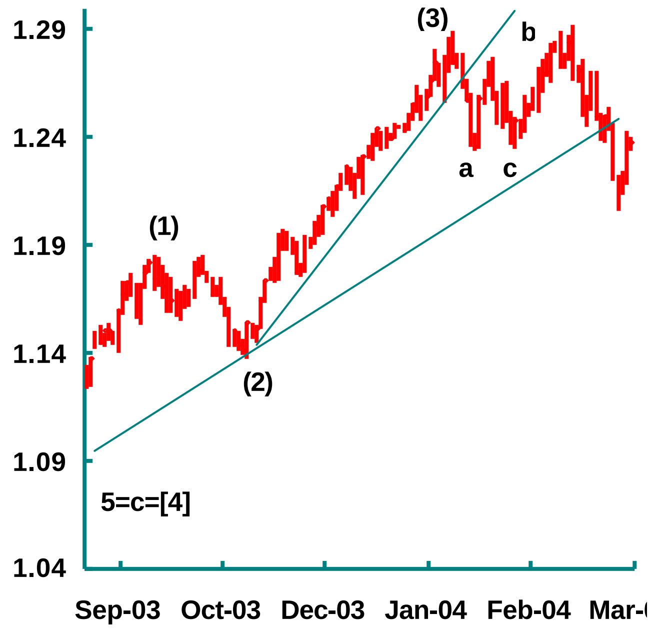
EURUSD Short Term Trading Strategy

Buy 1.2310, 1.2270, stop 1.2540

Technical Trading Model

Short at 1.2560, lower stop to 1.2495

EURUSD Daily



Resistance:	1.2390	**1.2425**	**1.2470**	**1.2490**
Support:	1.2335	**1.2310**	**1.2250**	**1.2060**

USDJPY Outlook

Rumoured official bids kept USDJPY on the uptrend on Friday despite US Feb payrolls underperforming ambitious expectations of 125-130k by over 100k jobs. Yet Japanese fundamentals still bode well for the JPY longer-term. Current conditions in the BOJ Economy Watchers survey increasing back into positive territory for the first time since October (the same month CPI also temporarily turned positive) and a slightly larger-than-expected growth in M2 plus CD's. Additionally, Japan's first 20 days' trade surplus for February leapt 27% y/y, despite the substantial y/y fall in USDJPY. Meanwhile, the lack of widespread international criticism over Japan's apparently more aggressive tactics has elicited curiosity among market players – most likely however the likelihood that Japan's official efforts in boosting the pair come in the interest of window-dressing ahead of financial year end book-closings. MoF officials have said as much, signalling that they expect the USD correction to continue a bit longer, not that they expect an indefinite USD rise. Speculative positioning has also claimed its part in upward pressure for USDJPY; IMM data showed that JPY shorts grew threefold. Medium-term JPY players will likely start getting back into USDJPY shorts as fiscal year end approaches.

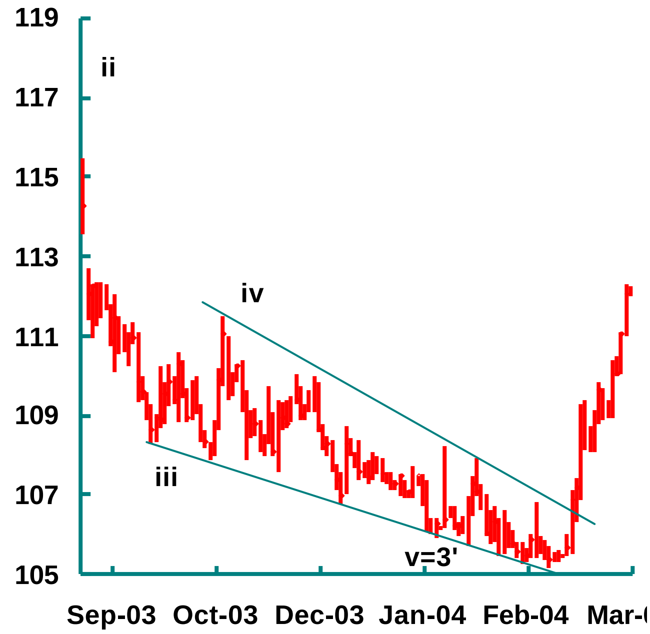
USDJPY: Trading Strategy

Remain neutral

Technical Trading Model

Long from 106.10, increase stop 108.25

USDJPY Daily



Resistance:	112.30	**112.70**	**115.10**	**115.70**
Support:	111.50	**110.10**	**109.90**	**107.00**

8 March London: 12:00 GMT

USDCHF & EURCHF Outlook

Another weak US employment report put the USD back on its heels, with USD/CHF retracing a sizeable portion of its gains since mid-February. The 21K rise in nonfarm payrolls was much weaker than expected, and suggests that despite the improvement in the broader economy, continued sluggishness and over capacity in the labour market will keep the Fed on hold for an extended period. That was reflected in the sizeable decline in the yield curve, with the 10-year yield falling to 3.8% (a 9-month low) and Fed Funds futures implying that tightening expectations have been pushed from August to November. That curbs what had been a bullish near-term bias in USD/CHF, although note that the February 18 uptrend was not breached on a sustained basis, and remains intact, providing support at 1.2710. Typically, we would expect that trendline to give way in the coming days and there is a reasonable chance of that happening. But note that apparent BoJ intervention in USD/JPY helped the USD recover off its lows against all the other majors. And while such actions persist, the downside in USD/CHF may be less of a risk, despite the disappointing developments in the US labour market.

USDCHF Trading Strategy

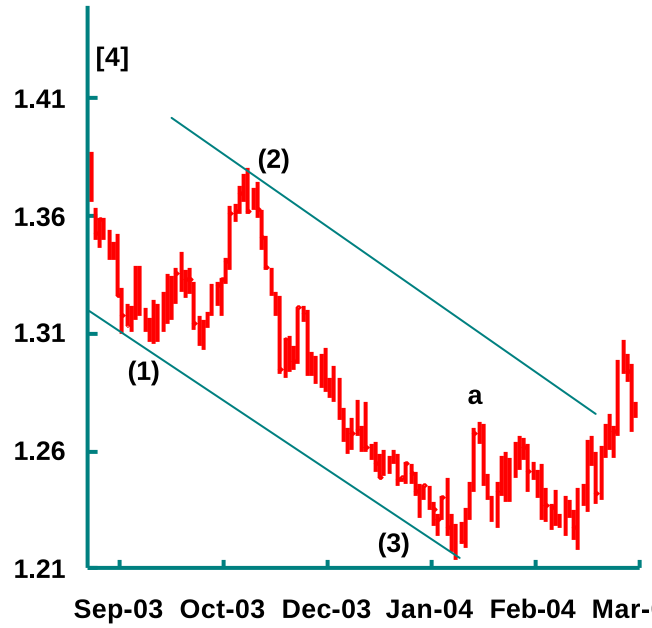
Remain neutral

EURCHF long at 1.5780, stop 1.5750, target 1.6200

Technical Trading Models:

Longs re-established at 1.2515, stop at 1.2620

USDCHF Daily



Resistance:	1.2800	1.2860	1.3075	1.3430
Support:	1.2680	**1.2725**	**1.2575**	**1.2390**

GBPUSD Outlook

Cable exceeded Friday's highs reaching 1.8550 this morning. Trendline resistance intervenes at 1.8575 and a daily closing price above this level is required to open upside potential to 1.8660. This move has been inspired by weak US labour market data reported on Friday and this morning's UK data showing output producer prices in line with expectations, but input producers prices dropping sharply (-1.8% yoy). The decline in input prices is welcome since the MPC is in a tightening mood. Besides the price data, domestic demand indications have come in strong. House prices are rising fast and this evening release of the BRC retail sales monitor (GMT:18.00) should show consumer demand remaining buoyant. However, we do not expect sterling to break significantly higher at this stage. The recent rally in bond markets has come as a surprise to many investors. While the January/ early February sterling rally was due to UK based fund managers liquidating foreign bond holdings, the recent bond market rally may force fund managers to re-establish positions again. Accordingly, we expect the current cable rally to run out of steam at levels near 1.86. A break of 1.8390 signals that a corrective top has been traded.

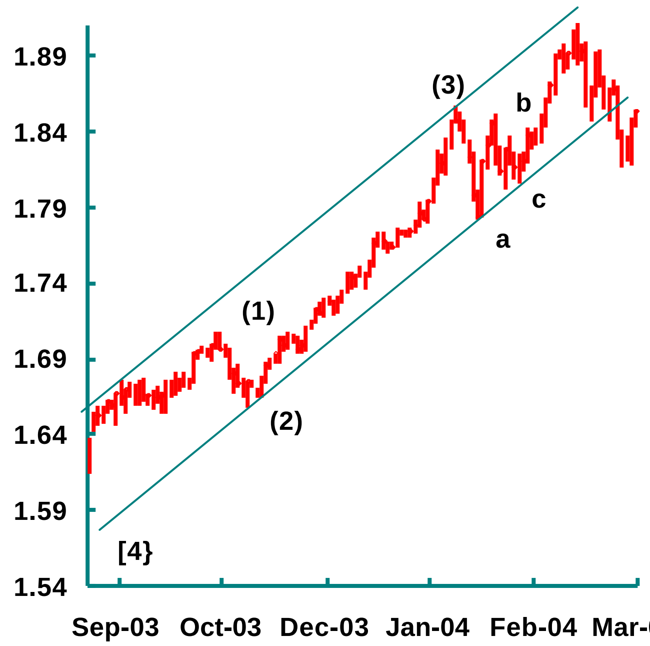
GBPUSD Trading Strategy

Remain neutral

Technical Trading Models:

Short from 1.8590, stop at 1.8580

GBPUSD Daily



Resistance:	1.8575	**1.8650**	**1.8750**	**1.9135**
Support:	**1.8420**	**1.8380**	1.8150	**1.8070**

08 March 2004, London: 12:00 GMT

EURJPY Outlook

EURJPY has staged a rebound above 138.0 however we suspect this may be temporary. Although ECB officials soothed market worries over potential Eurozone easing or intervention, fundamentals remain biased in favour of Asian currencies longer-term. Current conditions in the BOJ Economy Watchers survey increasing back into positive territory for the first time since October (the same month CPI also temporarily turned positive) and a slightly larger-than-expected growth in M2 plus CD's. Additionally, Japan's first 20 days' trade surplus for February leapt 27% y/y, despite the substantial y/y fall in USDJPY. The lack of widespread international criticism over Japan's apparently more aggressive tactics has puzzled many market players – most likely however the likelihood that Japan's official efforts in boosting the pair come in the interest of window-dressing ahead of financial year end book-closings. MoF officials have said as much, signalling that they expect the USD correction to continue a bit longer, not that they expect an indefinite USD rise. Current levels may be conducive to near-term EURJPY shorts, targeting a return to below 135.0

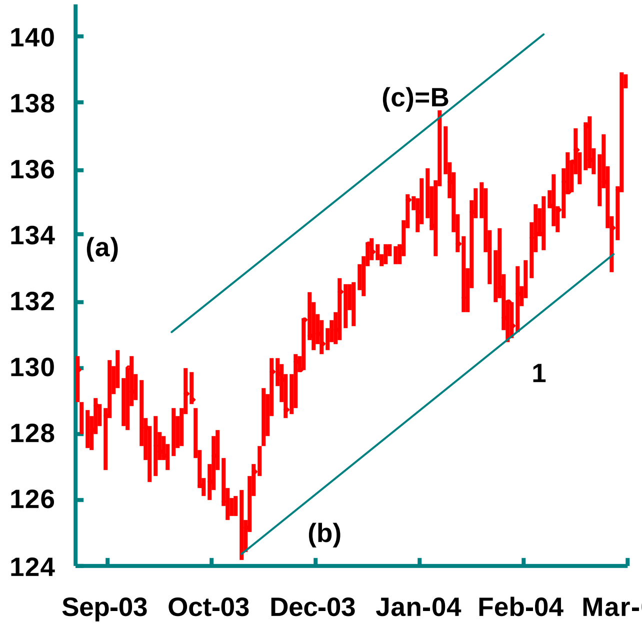
EURJPY Trading Strategy

Remain neutral

Technical Trading Models

Long at 135.95, stop at 136.20.

EURJPY Daily



Resistance	**137.15**	**137.55**	**138.15**	**139.00**
Support	133.90	133.60	132.60	131.85

EURGBP Outlook

The euro's rebound against sterling has been limited by the upper boundary of the major descending channel, now intervening at 0.6725. The failure to overcome this channel resistance keeps the bearish EUR/GBP outlook intact. Indeed, it is interesting to note that during the recent round of position adjustment witnessed over the past few weeks sterling's corrective pullback lagged moves elsewhere. Indeed, our interest rate model for EURGBP shows that market interest rate expectations are still working in favour of sterling which should also keep sterling well supported. We also note that strong repatriation flows by UK fund managers moving out of foreign bonds have provided a strong supportive flow for sterling. However, the rebound in bond markets following the much weaker than expected US non-farm payroll data for February, published on Friday, has triggered a sharp rebound in US bonds. This is likely to bring to a halt the recent repatriation flows especially as US interest rate hike expectations are now being pushed back. But, a break through initial support at the 0.6670 level is likely to trigger another move lower targeting 0.6615 and 0.6590, before a rebound develops.

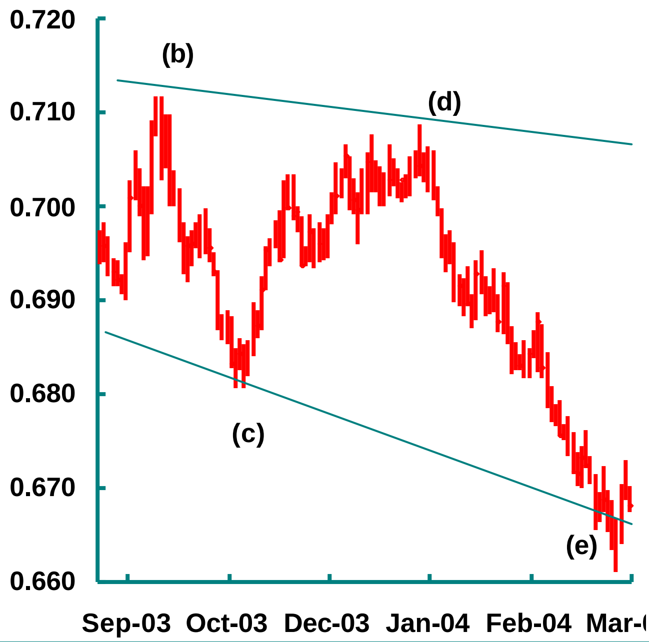
Trading Strategy

Short at 0.6710, stop 0.6735, target 0.6600

Technical Trading Models

Shorts re-established at 0.6705, stop at 0.6750

EURGBP Daily



Resistance:	0.6725	**0.6730**	**0.6760**	**0.6608**
Support:	0.6670	0.6615	**0.6550**	**0.6520**

08 Mar. 2004, TOKYO: 03:00 GMT

AUDUSD Outlook

The downside surprise on US job data and the across-the-board decline in yields have not proven conclusive motivators to build longs again in European and commodity currencies. IMM positioning showed that despite the continued covering in speculative USD shorts, AUD spec players were still net long. That gold has not managed to stay supported above 400 signals that the USD may not yet be ready to return to its longer-term bearish trend. The flurry of AUD Eurobond issues however shows that interest continues in higher-yielding Aussie products, M&A driven outflows, e.g. Macquarie's announcement to buy ING Asian Equties and Telstra's A$636mn acquisition of Dutch firm Trading Post). The prospects of a Fed hike in the future however could limit appreciation longer-term, especially if the US employment picture finally starts picking up in Q2. Near-term indicators could help shape RBA policy. The first wave of February indicators - ANZ job ads (Tue), and employment (Thu) is due this week, along with Consumer and business sentiment, plus January home loans.

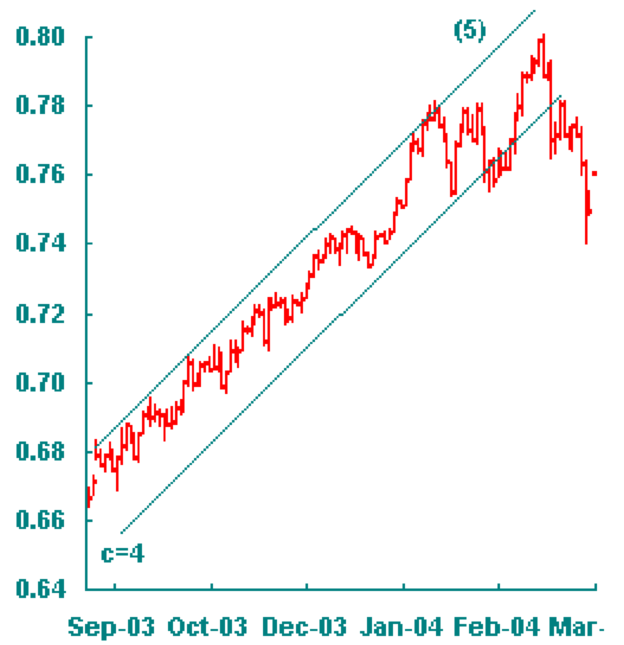
AUDUSD Short Term Trading Strategy

Neutral

Technical Trading Model

Short at 0.7731, stop at 0.7715

AUDUSD Daily



Resistance:	**0.7670**	**0.7700**	**0.7755**	0.7810
Support:	0.7450	0.7410	**0.7365**	**0.7330**

NZDUSD Outlook

The revised Kiwi trade balance is first on the agenda, ahead of retail sales, the final fundamental releases before the Thursday (late Wed GMT) RBNZ rate decision. Market consensus is leaning toward a 25bp rate hike and 90-day bills have accordingly seen yields creep upward. 10y NZ government bonds' spreads against US Treasuries have also widened on the overnight drop in Treasury yields. Considering recent mixed fundamentals, the RBA's decision to stay on hold and Fin Min Cullen's complaints about the currency's strength, the risks are probably to the downside here. We expect that a decision for the RBNZ to remain on hold will aid AUDNZD, currently supported above the 1.1200 level. The pair may also be helped by the NZ Treasury's forecast for Q4 economic growth in New Zealand to have continued at a slower (albeit "robust) pace than the September quarter's 1.5% and nearer 0.9%, compared to Australia's 1.4% expansion over the same period. Although the data will not be available until the last week in March, the forecast gives one more argument for the RBNZ to remain on hold this week, providing a downside NZD surprise.

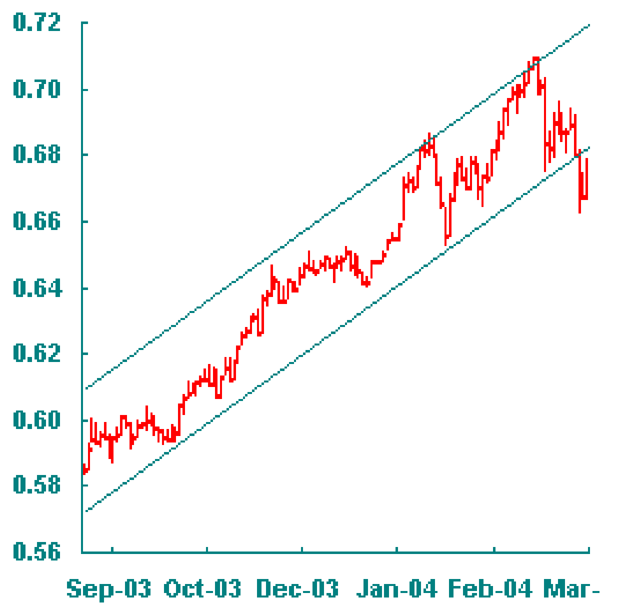
NZDUSD: Trading Strategy

Long AUDNZD at 1.120, stop 1.1150, target 1.1500

Technical Trading Model

Short at 0.6885, stop at 0.6868

NZDUSD Daily



Resistance:	**0.6790**	**0.6860**	**0.6940**	0.6990
Support:	**0.6640**	**0.6540**	**0.6465**	**0.6360**

Long Term FX forecasts

USD Bloc	Q1 '04	Q2 '04	Q3'04	Q4'04
EUR/USD	1.25	1.30	1.28	1.35
USD/JPY	110	102	95	90
USD/CHF	1.27	1.19	1.27	1.22
GBP/USD	1.85	1.88	1.86	1.85
USD/CAD	1.32	1.22	1.24	1.18
AUD/USD	0.77	0.82	0.75	0.76
NZD/USD	0.68	0.70	0.65	0.65
USD/SEK	7.36	6.52	6.80	6.37
USD/NOK	6.96	6.59	6.56	6.15
EUR Bloc				
EUR/JPY	137	133	122	122
EUR/GBP	0.68	0.72	0.69	0.73
EUR/CHF	1.59	1.60	1.62	1.64
EUR/SEK	9.20	8.80	8.70	8.60
EUR/NOK	8.70	8.70	8.40	8.30
EUR/DKK	7.46	7.46	7.46	7.46
Central Europe				
EUR/PLN	4.90	4.75	4.65	4.70
EUR/CZK	32.50	32.00	31.50	32.00
EUR/HUF	265	260	255	260
EUR/SKK	40.00	40.50	40.00	41.00
USD/ZAR	5.90	5.55	6.60	6.45
USD/TRL	1200	1300	1550	1300
Asia Bloc				
USD/SGD	1.68	1.65	1.63	1.60
USD/MYR	3.80	3.80	3.80	3.80
USD/IDR	8500	8200	7900	7700
USD/THB	39.00	37.50	36.00	35.00
USD/PHP	56.00	55.00	54.00	53.00
USD/HKD	7.80	7.80	7.80	7.80
USD/RMB	8.28	8.28	8.28	8.28
USD/TWD	33.00	32.50	32.20	32.00
USD/KRW	1160	1150	1140	1130
USD/INR	45.00	44.50	44.00	43.50
LATAM Bloc				
USD/ARS	2.91	2.97	3.02	3.08
USD/BRL	2.88	2.90	2.93	2.95
USD/CLP	607	604	607	610
USD/MXN	10.80	11.23	11.50	11.78
USD/COP	2893	2929	2965	3001
USD/VEB	1920	1920	2300	3300

*End Quarter

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RECOMMENDATION SYSTEM

Type	Terminology	Horizon
Credit Trend (1)	Positive/ Neutral/ Negative	6 months
Relative Value (2)	Outperform/ Market Perform/ Underperform	1 month
Investment Recommendation (3)	Buy/ Hold/ Reduce/ Sell	Up to 6 months

(1) Credit trend is based on underlying Credit fundamentals, business environment and industry trends;
(2) Relative Value is based on expected market performance relative to sector;
(3) Investment Recommendation is based on BNPP Credit Trend and Relative Value opinions.