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**From:** Ens, Amanda - [REDACTED]  
**Sent:** Tuesday, July 30, 2013 4:08 PM  
**To:** Epstein, Jeffrey (jeevacation@gmail.com)  
**Cc:** Barrett Team  
**Subject:** Euros in account

Jeffrey,

The euro has had a nice pop recently (~1.3260). You're still long EUR 837,388 in Southern Financial. Would you like to continue holding or convert to USD?

The euro is marginally stronger against the USD this morning ahead of this week's ECB policy meeting. Euro area consumer confidence improved for a third month in July (as expected), reaching the highest in 15 months and adding to indications the 17-nation currency bloc is emerging from a record-long recession. Manufacturing in the euro-zone expanded this month for the first time in two years as economists estimated gross domestic product stopped shrinking in the three months leading up to July. Near term, month-end flows, FOMC, Thursday's ECB meeting and Friday payrolls should drive price action.

Thanks,

Amanda

Amanda Ens | Vice President | Global Investment Opportunities | J.P.Morgan | NMLS ID: 853443



Europe Economic Research

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Euro area economic sentiment improved for the third straight month

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- Economic sentiment improved in line with the PMI

- Quarterly survey shows higher capacity use and better perceptions about the export market

After the large increase in the Euro area composite PMI seen last week, a significant rise in the EC economic sentiment indicator was expected today, which is exactly what happened. The EC sentiment indicator increased 1.2pts to 92.5 in July, and both surveys (the PMI and the EC survey) are now signalling that the Euro area economy is emerging from recession.

The details of the EC survey furthermore showed that the July improvement was broad based, which was another source of content: the manufacturing surveys rose 0.6pts to -10.6; the services component increased 1.8pts to -7.8; the retail sector gained 0.9pts to -13.7; and consumer confidence reached -17.4 after a 1.4pts increase. The only downside in July was the 1.1pts decline in the construction survey. But this discrepancy between the construction sector and the other sectors is not new. Since the beginning of the year, the construction sector only rose 0.4pts while the gain was 3.2pts in the manufacturing sector, 2.0pts in the services sector, and even 8.9pts for consumer confidence.

The European Commission also released the results of its quarterly survey. The 2Q12 level of capacity use in the manufacturing sector rose a fair amount (+0.8pts to 78.1%) but the survey still remains 3.2pts away from its historical average of 81.3%. New orders in the manufacturing sector had a significant swing up of 9.2pts to -5.4, and the export volume expectation indicator rose 2.1pts to 6.8. This was complemented by an improvement in the perception of competitive position of the Euro area manufacturing industry outside the European Union. Thus the tone of the quarterly release was overall positive.

Source: European Commission

Raphael Brun-Aguerre <<http://emaillink.jpmorgan.com/t/AQ/AALqqA/AAXTeg/QZtKRA/CnU/ABP7WQ/AQ/zVlv>>

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Europe Economic Research

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ECB to stick with its guidance

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-- ECB to stay on hold and to stick with its extended period guidance and its easing bias

-- Guidance not yet being challenged by economic or monetary developments, or by markets

-- ECB has not dealt with Eonia normalisation issue and its thinking has become less clear on this

The ECB is likely to stay on hold this week. It is also likely to stick with its "extended period" guidance and its explicit easing bias. This guidance is conditional on a subdued inflation outlook, which in turn is driven by an assessment of the economy and monetary developments. Neither is a big challenge at present, as the economy is only just emerging from recession (broadly in line with the ECB's forecast) and as the money and credit data weakened last week. Repeating the guidance will also help to ensure that money market rates remain low over the intended guidance period.

Even if the guidance is not being challenged by the data in either direction, pressures could emerge over time. For example, a large move up in interest rate expectations, if driven by external factors, could require the ECB to strengthen its guidance by setting calendar dates or thresholds. Similarly, if the Euro area PMI continues to increase as expected, the ECB will need to stick to its new script on inflation. This emphasizes slower-moving "level" variables (e.g. weak demand, weak labor market conditions, and low capacity use) as drivers of inflation. In the past, the ECB has downplayed their significance and focused more on the momentum of growth and factors that tend to push inflation back to target (even when unemployment is high). If core inflation moves lower as we expect, it will be easier for the ECB to maintain its guidance but it may need to clarify its thinking.

There are some other issues. First, the ECB has not dealt with the issue of LTRO repayments and changes in autonomous factors leading to lower levels of excess liquidity. As excess liquidity has now fallen from €800 billion to €230 billion, it is very close to the €100-200 billion range in which Eonia starts to gradually rise back to the middle of the ECB's interest rate corridor. Some view this as equivalent to a 40 basis point stealth rate hike. For a long time, the ECB has rejected this interpretation, arguing instead that LTRO repayments are a sign of banking sector healing and improvements in credit availability in the real economy. More recently, it has been less clear about this. In any case, it could dampen the effect of this Eonia normalization by narrowing its rate corridor or by injecting more liquidity through another LTRO. These options remain on the table, even if they are unlikely to be taken this week.

Second, related to the first issue, it will be important to see what the ECB makes of the large declines in actual bank lending to non financial corporates over the past three months. This may relate to weak loan demand, but may nevertheless lead to some debate about further collateral and liquidity changes. We doubt that actual policy changes are imminent, especially because the joint work with the EIB is progressing slowly and because the ECB tweaked its collateral framework just two weeks ago.

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