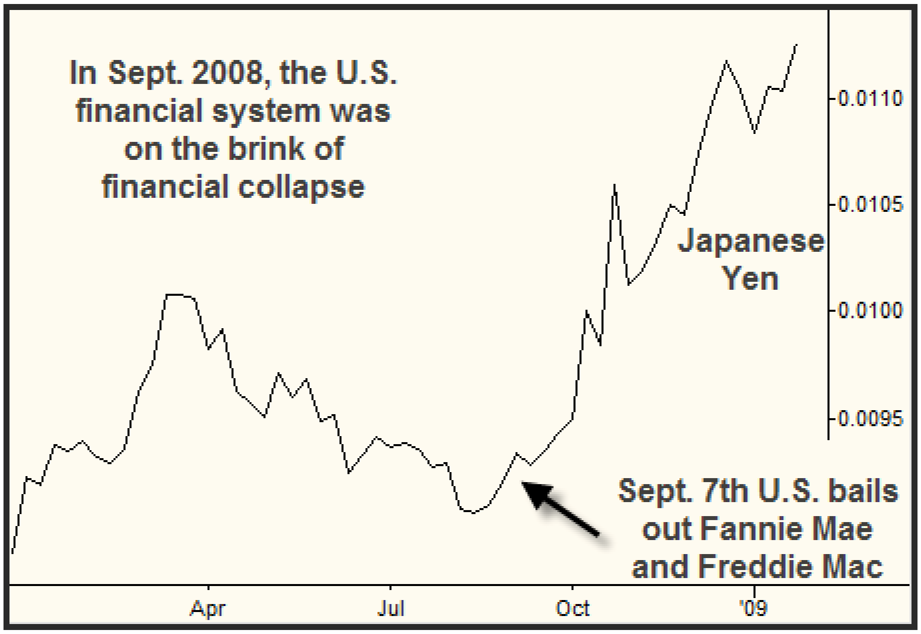
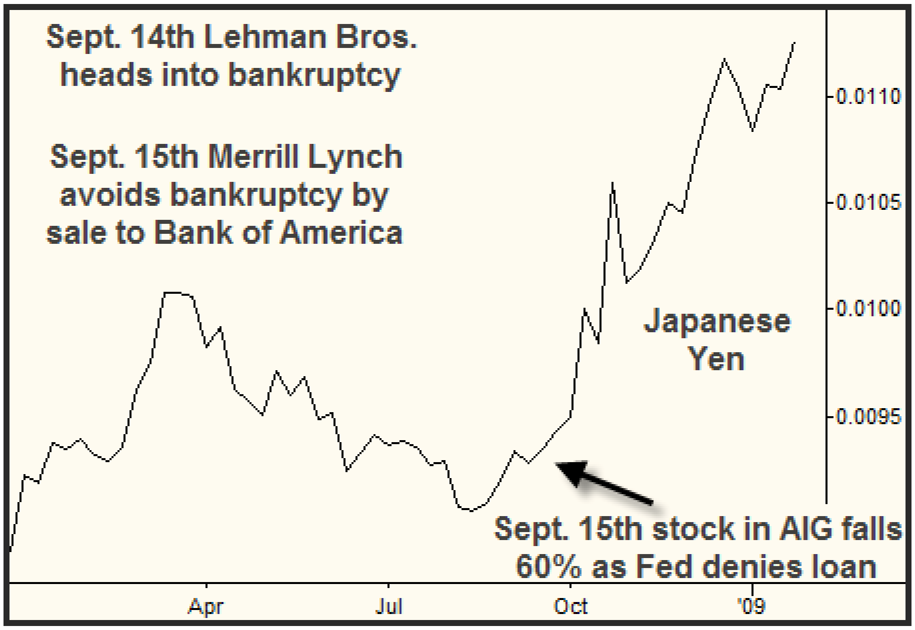
Government's Affect on the Foreign Exchange Market

In the world economy, changes in government policy can have a dramatic affect on one nation's economy vs. another. Especially sensitive are the currency markets. We only have to go back a few years to the summer of 2008 to see an example of how decisions by the U.S. and European governments caused some very large moves in world currencies.

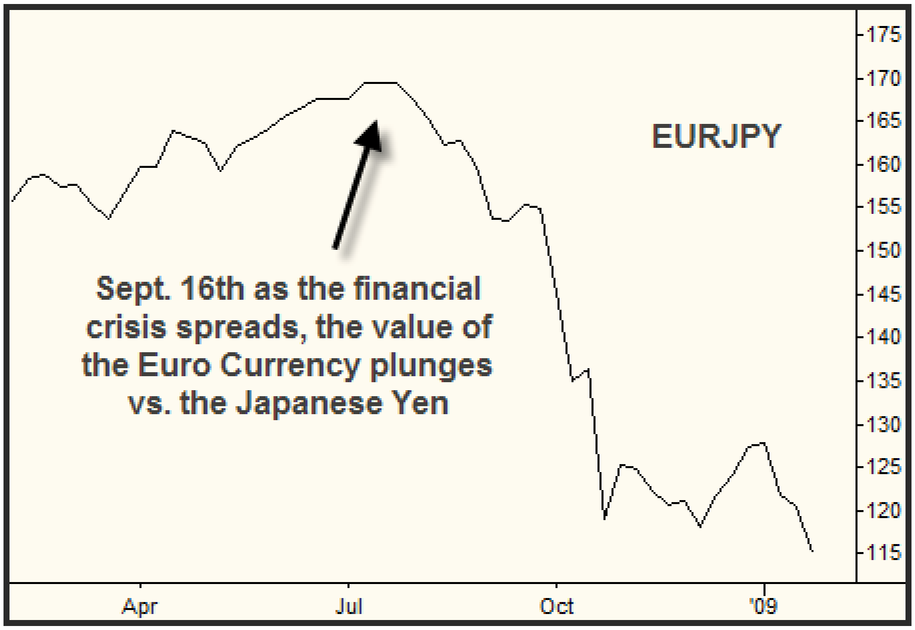


In the chart above of the Japanese Yen, as soon as the decision was made by the White House to come to the aid of the large financial institutions, the Japanese Yen quickly became the favorite of currency traders.



The three weeks following the crisis of September 15th 2008 was devastating for the U.S. economy as the Dow Jones Industrial Average plunged nearly 31% to a low of 7884. As fears of a banking crisis spread to London and Paris, European leaders vowed to work together to stop the growing panic. Of the handful of economies in the world that were less affected by the crisis, the Japanese Yen began to replace the Euro and the US Dollar as the world's favored currency.

When government leaders intervene in the financial markets, prices move quickly to try and adjust, especially in the Foreign Currency Markets (or FOREX). Late in the summer of 2008, while the Japanese Yen was advancing, the values of U.S. and European currencies were declining.



In the chart above of the EURJPY, the decline during the summer of 2008 from 165.00 to 125.00 represents a change of more than $40,000 in the value of a standard Forex contract.

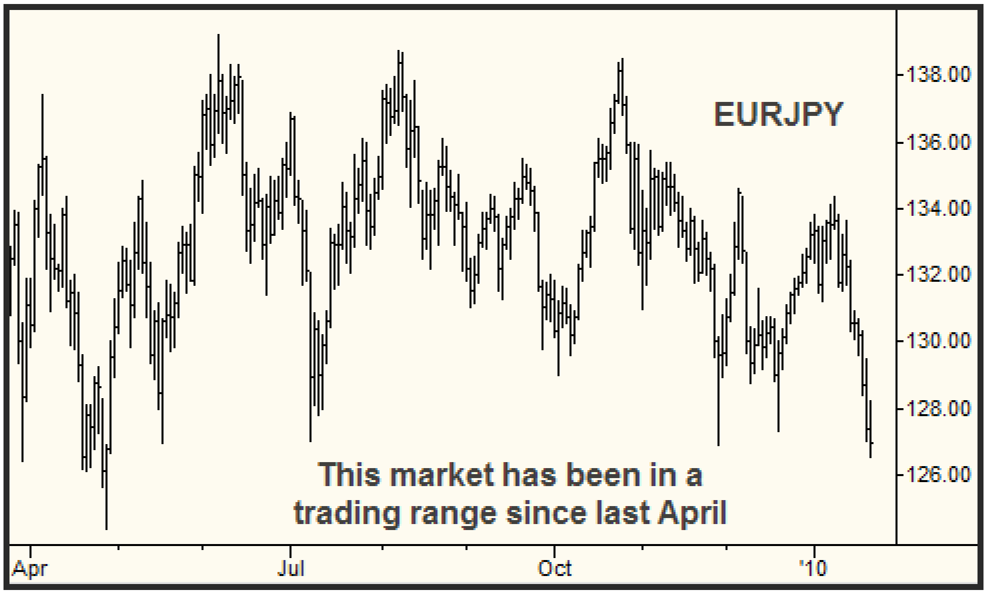
Much has happened since the financial crisis of 2008. The markets have stabilized and the U.S. has a new President. For 2010, will the decisions that are made by this new administration be an aid to the healing process or will they hinder it? Here are a few recent headlines:

"Obama Ready to Fight Banks
Stocks in Free Fall as the Impact of the Obama Crackdown Hits Home"

"Obama Goes 'Toe-to-Toe' with U.S. Banks
Never Again will the American Taxpayer be Held Hostage"

With the new war on banks, the White House seems to be favoring a lower stock market. Historically, a declining stock market has been positive for the U.S. Dollar and the Japanese Yen.

Let's look at a current chart of the Euro vs. the Japanese Yen:



As we can see in the chart above, this market has been in a 9-month trading range between 125 and 139. This trading range won't last forever.