Euro Falls Most Since May Amid ECB Rate-Cut Bets; Krona Drops

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By Joseph Ciolli

Oct. 31 (Bloomberg) -- The euro dropped the most in more than five months versus the dollar after the inflation rate in the region unexpectedly cooled, fueling speculation the European Central Bank will cut interest rates to spur the recovery.

The shared currency fell against most of its 16 major peers as separate data showed unemployment in the euro area climbed to a record 12.2 percent. The yen pared its first gain in five days versus the dollar as a U.S. business barometer unexpectedly jumped. Sweden's krona sank for a fourth day before a report tomorrow forecast to show manufacturing slowed.

"There was a big downward surprise for inflation numbers in the euro zone," Vassili Serebriakov, a foreign-exchange strategist at BNP Paribas SA in New York, said in a phone interview. "It was a very dovish signal for the European Central Bank. Markets built up long positions in the euro too quickly." A long position is a bet an asset will rise in value.

Europe's 17-nation currency slid 1.1 percent to $1.3591 at

11:56 a.m. New York time and touched $1.3587 in the biggest intraday drop since May 2. The euro dropped 1.3 percent to

133.57 yen. Japan's currency rose 0.3 percent to 98.20 per dollar after depreciating to 98.68 yesterday, the weakest level since Oct. 17.

The euro has gained 0.5 percent this month versus the dollar and has advanced 3.1 percent this year. The U.S. currency was little changed versus the yen in October and has climbed 13 percent since the start of the year.

Volatility Rises

A measure of price swings among the currencies of Group of Seven nations increased to the highest in almost two weeks. The JPMorgan G7 Volatility Index rose to 7.86 percent, the most since Oct. 18, after sliding to 7.48 percent Oct. 28, the lowest since Dec. 21. The 2013 average is 9.37 percent.

The Canadian dollar rose versus all of its 16 most-traded counterparts after the government reported the nation's economy expanded 0.3 percent in August, topping forecasts for a 0.1 percent gain. The currency, nicknamed the loonie, gained 0.3 percent to C$1.0446 per dollar.

Sweden's krona dropped against the dollar and euro. It slid

1.1 percent to 6.4604 per greenback, fell 0.1 percent to 8.7857 to the common currency and declined 0.4 percent to 1.0875 per Norwegian krone.

An index of Swedish manufacturing based on a survey of purchasing managers declined to 54.5 in October from 56 the previous month, economists in a Bloomberg survey forecast before a report from Swedbank Markets tomorrow.

'Catching Up'

"The latest underperformance of krona versus euro, dollar and especially against the Norwegian krone is fundamentals catching up with the otherwise fairly resilient krona," said Valentin Marinov, head of European Group-of-10 foreign-exchange strategy at Citigroup Inc. in London.

The euro area's annual consumer-price index declined to 0.7 percent in October, the least since November 2009, from 1.1 percent last month, the European Union's statistics office said.

A Bloomberg News survey estimated it would stay at 1.1 percent.

The central bank has said there's a "subdued outlook" for price growth in the region, and the October data mark the ninth month the rate has been less than its 2 percent ceiling. While the economy has exited a recession, the ECB predicts only a "gradual" recovery. Policy makers next meet Nov. 7.

The ECB will cut its refinancing rate to 0.25 percent from

0.5 percent at its meeting in December, according to new forecasts published in a client note by Greg Fuzesi, an economist at JPMorgan Chase & Co. in London. The weaker-than- forecast CPI numbers raise "very big" questions about the outlook for inflation and the ECB's response, Fuzesi said.

Best Performer

The euro has gained 6.3 percent this year, the best performer of 10 developed-nation currencies tracked by Bloomberg Correlation-Weighted Indexes. The dollar has advanced 2.6 percent, and the yen, the biggest loser, has slumped 11 percent.

Japan's currency strengthened against most major peers after the policy-setting U.S. Federal Open Market Committee said yesterday following a meeting that policy makers see improvement in economic activity while maintaining monthly bond purchases.

The Federal Reserve buys $85 billion of bonds a month to push down long-term yields and spur growth. A Bloomberg survey taken Oct. 17-18 forecast it would slow purchases in March.

“The FOMC statement has challenged the market belief that the Fed would wait until 2014 before tapering,” said Daragh Maher, a currency strategist at HSBC Holdings Plc based in London. “This is bad for the risk-on mood that had been prevailing and has lent consequent support to the traditionally safe-haven yen.”

BOJ Stimulus

The Bank of Japan said after a policy meeting today it will maintain its pledge to expand the monetary base by as much as 70 trillion yen ($713 billion) a year, a decision forecast by all 34 economists in a Bloomberg survey.

The dollar pared its loss versus the yen as the MNI Chicago Report’s business gauge rose to 65.9 in October, the fastest pace since 2011, from 55.7 a month earlier. Readings above 50 signal expansion. A Bloomberg survey of economists forecast 55.

Trading in over-the-counter foreign-exchange options totaled $23 billion, from $38 billion yesterday, according to data reported by U.S. banks to the Depository Trust Clearing Corp. and tracked by Bloomberg. Volume in options on the euro- dollar exchange rate amounted to $5 billion, the largest share of trades at 22 percent. Options on the dollar-yen rate totaled $3.2 billion, or 14 percent.

Euro-dollar options trading was 6 percent less than the average for the past five Thursdays at a similar time in the day, according to Bloomberg analysis. Greenback-yen options trading was 53 percent below average.

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