
Press Release

London, 21 April 2005

ABN AMRO pioneers FX model that predicts price behaviour in EUR-USD spot rate

ABN AMRO today launched a groundbreaking foreign exchange model that indicates whether the EUR-USD exchange rate is likely to trend higher or lower, or instead be subject to movements within a trading range.

The *ABN AMRO FX Regime Prediction Indicator*, the first proven model of its kind, assesses market volatility and positioning to assign a probability factor to likely movements in the EUR-USD spot rate in the coming week.

"This tool provides currency traders and portfolio managers with an extra level of sophistication and choice in managing their currency exposure," said Aziz McMahon, Senior FX Strategist at ABN AMRO.

Typically, currency managers use one of two strategies: 'trend following', which takes positions on long-term trends; and 'volatility capture', which uses option positions to sell volatility between trends.

Adopting a single strategy can cause losses: a market that is range trading undermines maintained long or short positions, while short volatility positions fail to take advantage of trending movements in the spot rate.

This risk has been traditionally hedged by currency managers adopting both strategies side-by-side. There is a limit to the potential losses of a single strategy, but also potential profits are lower.

By following the *ABN AMRO FX Regime Prediction Indicator*, currency managers can now confidently employ a switching strategy, using 'trend following' when the probability is high that EUR-USD is trending up or down, and 'volatility capture' when the probability is high that the EUR-USD exchange rate is simply range trading.

The model has been built from data over the January 2000 to December 2002 period and tested for the period between January 2003 to the end of March 2005. Table 1 overleaf illustrates the superior returns of adopting a strategy of switching between trading styles, following the Regime Prediction Indicator, as compared to a simple strategy of following trend or range trading styles.

In addition, the table illustrates the returns from allocating capital to each trading style according to a probability estimate of whether the trading regime is in 'trending' or 'ranging' mode. This latter probability signal produces lower returns, but has the benefit of less volatile returns than the pure switching indicator and also a higher hit ratio. The two signals may not always coincide, but together they give a better guide to market conditions.

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Table 1: Trading rule comparisons: Regime switching increases returns and information ratio * in our out of sample test. Returns based on period Jan 2003 – March 2005.

Trading Rule	Annualized mean weekly return	Information Ratio	Annualized standard deviation of weekly returns	Biggest 1-week loss	Hit Ratio (% winning trades)
Trend following	3.80%	0.39	9.63%	-3.85%	60.3%
Volatility capture	-2.16%	-0.38	5.70%	-2.78%	51.7%
Static 50:50 style	0.57%	0.09	6.17%	-3.31%	69.8%
Switching style	8.41%	1.08	7.77%	-3.85%	61.2%
Probability weighted	4.13%	0.74	5.59%	-2.94%	68.1%

Source: ABN AMRO

*The ratio of return in relation to risk - the higher the ratio, the greater the return relative to risk

“Our tests show that using our indicators to dynamically switch between, or to adjust the weightings of, different trading styles produces significant improvement on returns compared to a passive approach,” McMahon said.

“The latest model output is a weak signal in favour of EUR-USD trending. The signal is so weak that it is not endorsed by the probability-weighted indicator. This latter indicator is modestly favouring a trading regime.”

“Regime changes have been more frequent than normal in 2005, indicating a very uncertain market. For the coming week our system would recommend investors hold modest short EUR-USD positions,” McMahon added.

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Notes to Editors:

Netherlands-based ABN AMRO is a leading international bank with total assets of EUR 608.6 bln (as at 31 December 2004). It has over 3,000 branches in more than 60 countries and territories, and has a staff of about 100,000 full-time equivalents worldwide. ABN AMRO is listed on the Euronext and New York stock exchanges.

ABN AMRO operates through three Strategic Business Units, each responsible for managing a distinct client segment. Wholesale Clients provides integrated corporate and investment banking services to corporate, institutional and public sector clients worldwide. Consumer & Commercial Clients focuses on retail and SME clients in three home markets – the Netherlands, the US Midwest and Brazil and in a number of selected growth markets. Private Clients & Asset Management provides private banking services to wealthy clients and investment products to financial intermediaries and institutional clients.