

# Forex Market Weekly

## USD/JPY is likely to decline after the FOMC meeting

- Yen strengthens on concerns about a US economic slowdown and US administrative personnel issues
- US and China's moves regarding trade imbalance warrant attention
- USD/JPY is likely to decline after the FOMC meeting

### This week's USD/JPY forecast range

**19-23 Mar: Y105.1-107.1/\$ (Y106.0 at end-previous week)**

Forex Market View DSFE131

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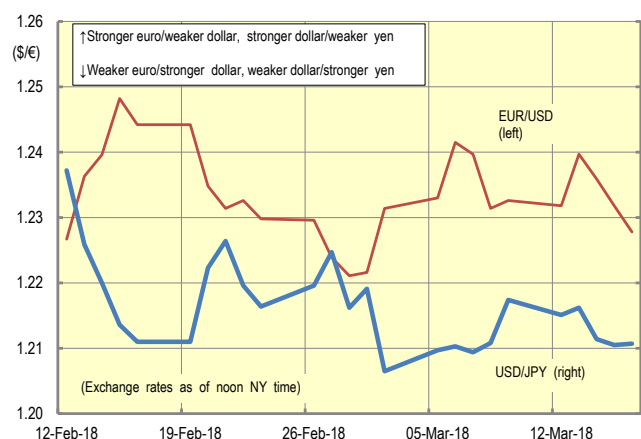


### Overview of last week's forex market

### Yen strengthens on concerns about a US economic slowdown and US administrative personnel issues

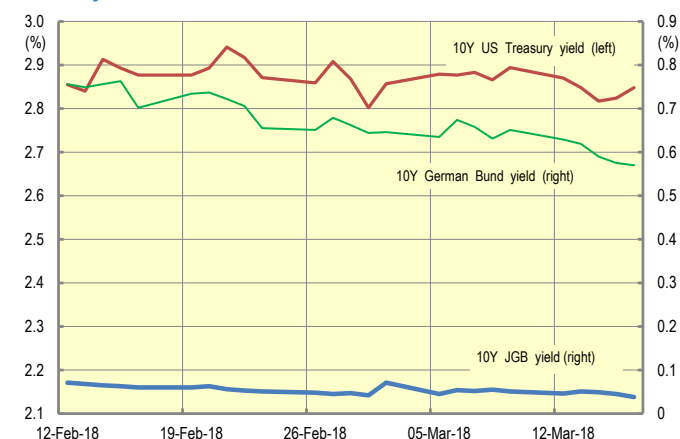
Reflecting the substantial increase in US employment numbers announced on 9 March, stock prices and long-term interest rates rose, pushing up the USD/JPY rate to nearly 107. After Japan's Ministry of Finance reported to the Diet that it had altered Moritomo school-related documents, the yen strengthened as the details were disclosed. Meanwhile, Minister of Finance Taro Aso stated that "I am not thinking about resigning." In the afternoon on the following day (13 March), the market leaned toward higher stock prices/weaker yen, raising the USD/JPY to around 107.30. However, stable conditions were confirmed as the February CPI was in line with the market consensus, while elsewhere US Secretary of State Rex Tillerson was fired, both of which led to dollar depreciation/yen appreciation alongside lower US long-term interest rates/stock prices. Moreover, due to the lower-than-expected February US retail sales, US stock prices and long-term interest rates continued to decline, which led to further yen appreciation. The USD/JPY declined to 105.60, partly reflecting US media reports that President Trump has decided to remove national security advisor H.R. McMaster. However, February US manufacturing production increased 1.2%, the biggest gain since October 2017, exceeding the market consensus of +0.5%. This pushed up US interest rates and helped the dollar recover to slightly above 106. Last week, the leader of Italy's League party implied that a coalition government with the Five Star Movement is possible, which led to euro depreciation.

Chart: Forex Market: USD/JPY, EUR/USD



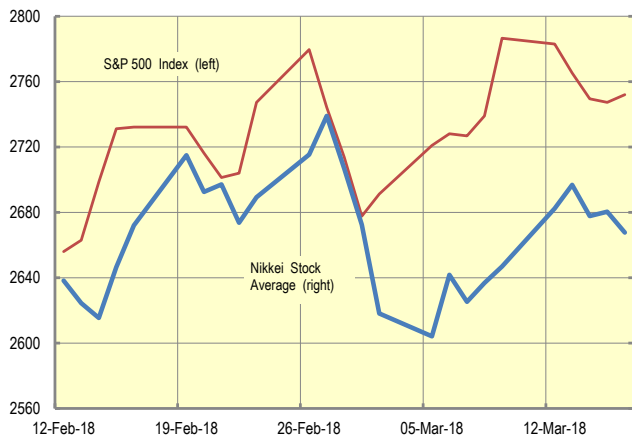
Source: Thomson Reuters; compiled by Daiwa Securities.

Chart: Bond Market: 10Y Sovereign Bond Yields in Japan, US, and Germany



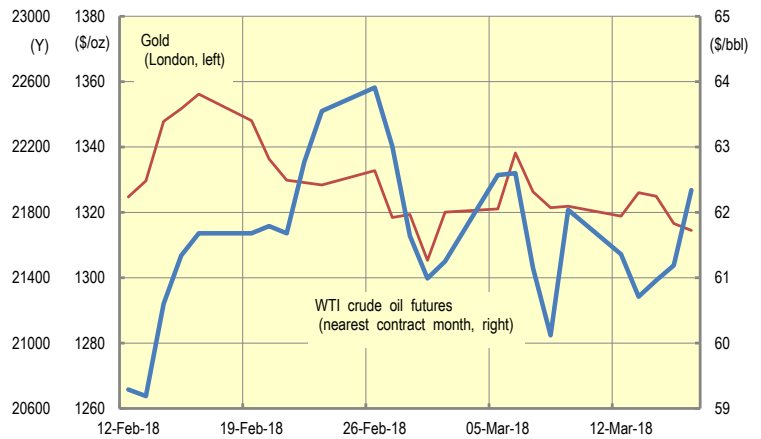
Source: Thomson Reuters; compiled by Daiwa Securities.

Chart: Stock Market: US S&amp;P 500, Nikkei Stock Average



Source: Thomson Reuters; compiled by Daiwa Securities.

Chart: Commodity Market: Crude Oil Futures, Gold



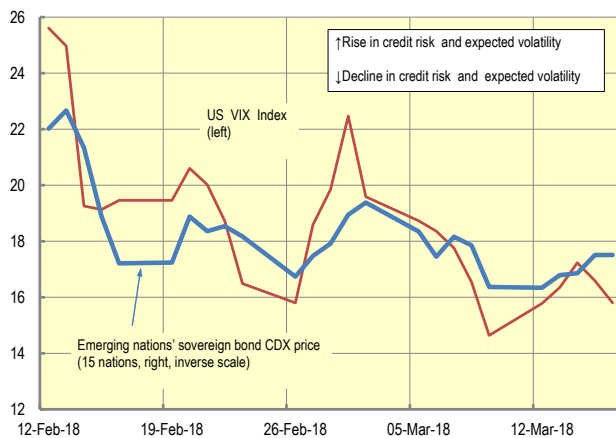
Source: Thomson Reuters; compiled by Daiwa Securities.

### US and China's moves regarding trade imbalance warrant attention

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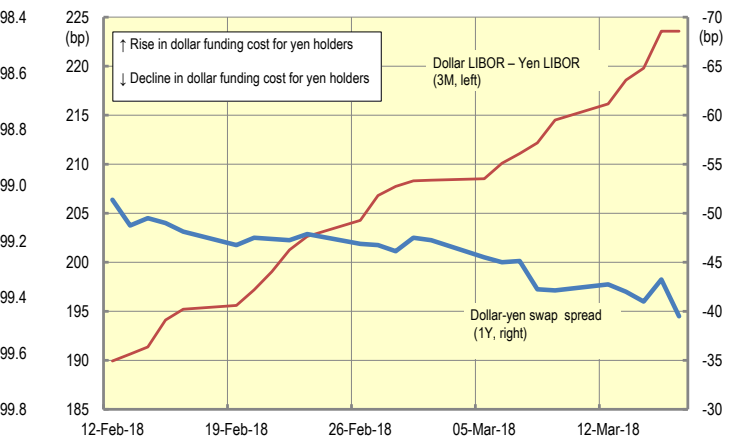
The US administration disclosed that it asked China to cut its annual trade surplus with the US by \$100bn. It has also been reported that the US plans to impose tariffs on up to \$60bn of Chinese imports. Larry Kudlow, who accepted an offer to be Director of the National Economic Council (NEC) following Gary Cohn's departure, is considered to be an aggressive proponent of introducing high tariffs focusing on Chinese products. The Trump administration's economic policy team now consists of hard-liners on China—Commerce Secretary Wilbur Ross, Office of Trade and Manufacturing Policy head Peter Navarro, and NEC Director Larry Kudlow. If the administration decides to impose tariffs on China, the scale may be greater than the recently announced steel/aluminum tariffs. The market would thus lean toward risk-off driven yen appreciation due to concerns about the negative impact on the global economy. China is demanding discipline regarding US protectionist measures, saying that "a trade war would only bring disaster to China, the US, and the global economy."

Chart: US VIX index and Emerging Market CDS



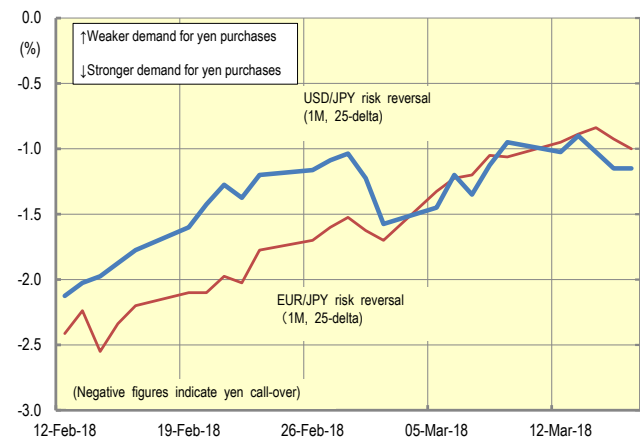
Source: Thomson Reuters; compiled by Daiwa Securities.

Chart: LIBOR Gap and Currency Swap Spread



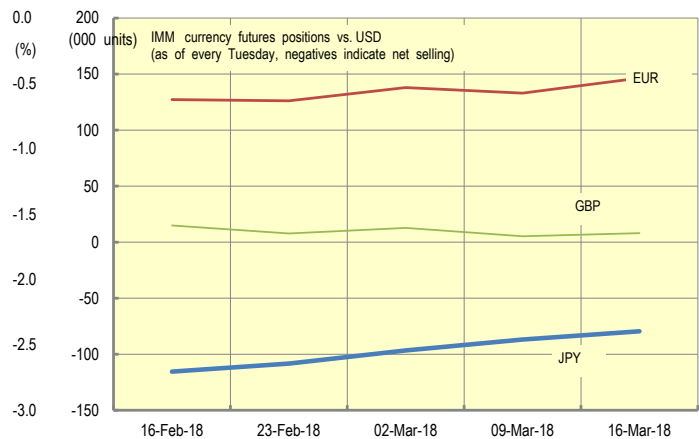
Source: Thomson Reuters; compiled by Daiwa Securities.

Chart: Risk Reversal on Currency Options



Source: Thomson Reuters; compiled by Daiwa Securities.

Chart: Net Position of Currency Futures



Source: Thomson Reuters; compiled by Daiwa Securities.

### USD/JPY is likely to decline after the FOMC meeting

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A decision to implement a 0.25% rate hike (FF rate of 1.50–1.75%) is anticipated at the FOMC meeting on 20–21 March, but members' projections for the economy and interest rates are also being closely watched. In the December FOMC meeting, growth forecasts were revised up in anticipation of tax cut benefits. However, a further upward revision is unlikely because retail sales continued to decline (down 0.1% for three consecutive months during December–February) probably due to constraints on personal consumption reflecting bad weather and lower saving rates/stock prices. An upward revision to the core PCE inflation rate is also not expected, as the rate has been stable at 1.8% for three months in a row. Although import tariffs serve as a factor to raise inflation and push down growth, the impact is uncertain as such tariffs have not yet been imposed. We thus think this factor will not be reflected in the latest economic projections. The median FF rate projection for end-2019 is 2.7%, with the median longer-run projection at 2.8%. Although these figures may be revised up slightly, there is also a risk of lower stock prices due to a rise in US long-term interest rates. The USD/JPY is likely to decline after the FOMC meeting.

### If European economic indicators worsen, the EUR/JPY is likely to decline

The US is considering imposing tariffs on up to \$60bn of Chinese imports. Meanwhile, US Secretary of State Rex Tillerson will be replaced by CIA Director Mike Pompeo. US core CPI for February came in at 1.8%, in line with the market consensus and the same as the January level. Contrary to the market consensus, US retail sales continued to fall in February for a third consecutive month. "Concerns about US protectionism and a hard-line stance," "fading concerns about US inflation," and "worries about a US economic slowdown" are causing not only lower US long-term interest rates/stock prices but also declines in global interest rates/stock prices and cross-yen pairs. The March German ZEW Indicator of Economic Sentiment, the German IFO business climate index, and the Eurozone PMI are scheduled to be announced this week. If these readings continue to worsen following February's numbers, the EUR/JPY is likely to decline further.

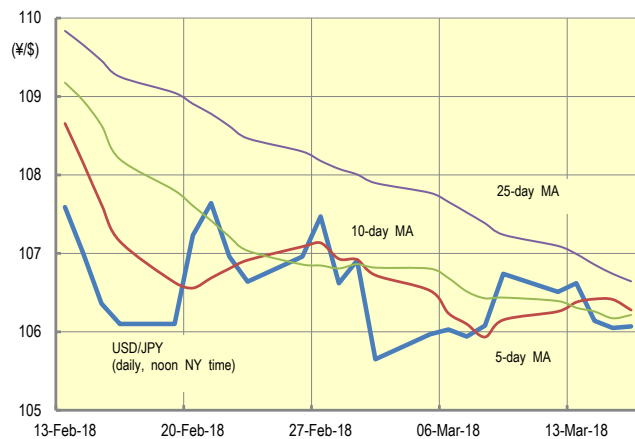
### Noteworthy currency: GBP

The Bank of England (BOE) is to hold a Monetary Policy Committee meeting on 22 March. In the February meeting, the bank indicated a need to raise interest rates at an earlier stage than the market consensus. Market forecasts for the rate-hike timing are thus currently divided, with some favoring May and others looking to August this year. If any committee member votes for a rate hike and/or if a May rate hike is implied, the pound would likely strengthen.

### Noteworthy currency: ZAR

On 23 March, Moody's is scheduled to review its rating on South Africa. If a downgrade can be avoided in line with expectations, the news would serve as a tailwind for the South African rand.

Chart: USD/JPY and Moving Average



Source: Thomson Reuters; compiled by Daiwa Securities.

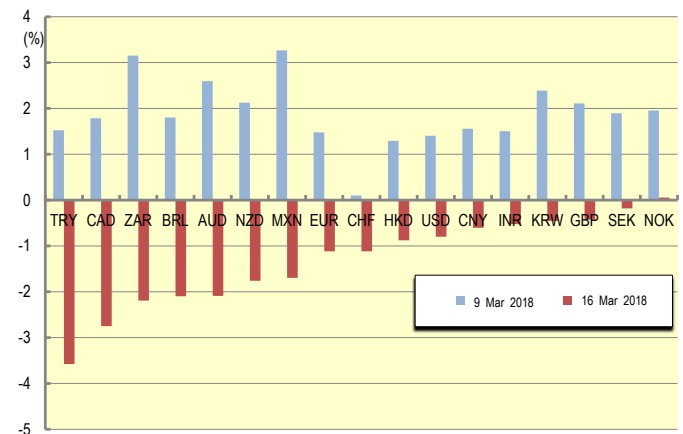
Chart: Weekly Schedule for Major Economic Indicators/events

- 19-Mar ● **G20 Finance Ministers and Central Bank Governors meeting (until 20th)**
  - Summary of Opinions at BOJ MPM (8-9 Mar)
- 20-Mar ○ Minutes of RBA MPM (6 Mar)
  - Feb UK CPI
  - Mar German ZEW Indicator of Economic Sentiment
- 21-Mar Oct-Dec US current-account balance
  - Feb US existing home sales
- 22-Mar ○ **FOMC statement**
  - **Press conference by Fed Chairman Jerome Powell**
  - MPM at Brazilian central bank
  - Mar eurozone PMI (Markit), Mar German IFO business climate index
  - BOE MPC meeting, minutes
  - EU summit meeting (until 23rd)
- 23-Mar Feb Japan nationwide CPI (Statistics Bureau)
  - Feb US durable goods orders
  - Feb US new home sales
  - **Expiration of stopgap budget at US federal government**

Source: Compiled by Daiwa Securities.

Notes: Dates based on JST. ○ indicates monetary policy-related and ● denotes political events.

Chart: Weekly Currency Performance (vs. yen)



Source: Thomson Reuters; compiled by Daiwa Securities.

Chart: Weekly Forex Forecasts

	12-16 Mar 2018 (actual)		19-23 Mar 2018 (forecasts)	
	Range	Weekend	Range	Weekend
USD/JPY	105.6-107.3	106.0	105.1-107.1	105.8
EUR/JPY	130.0-132.5	130.2	129.0-132.0	129.6
EUR/USD	1.226-1.242	1.229	1.219-1.239	1.225

## Noteworthy currencies and factors

GBP	GBP would strengthen if any committee member advocates rate hike and/or May rate hike is implied
ZAR	If downgrade can be avoided, the news would serve as tailwind for ZAR
EUR	Deterioration of economic indicators in eurozone and Germany would lead to euro depreciation

Source: Compiled by Daiwa Securities.

**IMPORTANT**

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**Notification items pursuant to Article 37 of the Financial Instruments and Exchange Law**

If you decide to enter into a business arrangement with our company based on the information described in this report, we ask you to pay close attention to the following items.

- In addition to the purchase price of a financial instrument, our company will collect a trading commission\* for each transaction as agreed beforehand with you. Since commissions may be included in the purchase price or may not be charged for certain transactions, we recommend that you confirm the commission for each transaction. In some cases, our company also may charge a maximum of ¥ 2 million (including tax) per year as a standing proxy fee for our deposit of your securities, if you are a non-resident.
- For derivative and margin transactions etc., our company may require collateral or margin requirements in accordance with an agreement made beforehand with you. Ordinarily in such cases, the amount of the transaction will be in excess of the required collateral or margin requirements\*\*.
- There is a risk that you will incur losses on your transactions due to changes in the market price of financial instruments based on fluctuations in interest rates, exchange rates, stock prices, real estate prices, commodity prices, and others. In addition, depending on the content of the transaction, the loss could exceed the amount of the collateral or margin requirements.
- There may be a difference between bid price etc. and ask price etc. of OTC derivatives handled by our company.
- Before engaging in any trading, please thoroughly confirm accounting and tax treatments regarding your trading in financial instruments with such experts as certified public accountants.

\* The amount of the trading commission cannot be stated here in advance because it will be determined between our company and you based on current market conditions and the content of each transaction etc.

\*\* The ratio of margin requirements etc. to the amount of the transaction cannot be stated here in advance because it will be determined between our company and you based on current market conditions and the content of each transaction etc.

When making an actual transaction, please be sure to carefully read the materials presented to you prior to the execution of agreement, and to take responsibility for your own decisions regarding the signing of the agreement with our company.

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