

Forex Market Weekly

US-China summit holds key to forex market direction

- Risk-off appreciation of yen, dollar late last week
- US-China summit holds key to forex market direction
- USD/JPY may fall on concerns about slowing US economy

This week's USD/JPY forecast range

26 – 30 Nov: Y111.8 – 113.8/\$ (Y112.9 at end-previous week)

Forex Market View DSFE195
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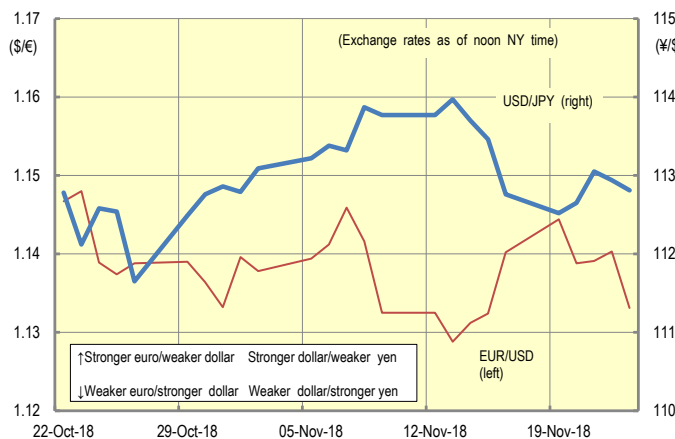


Overview of last week's forex market

Risk-off appreciation of yen, dollar late last week

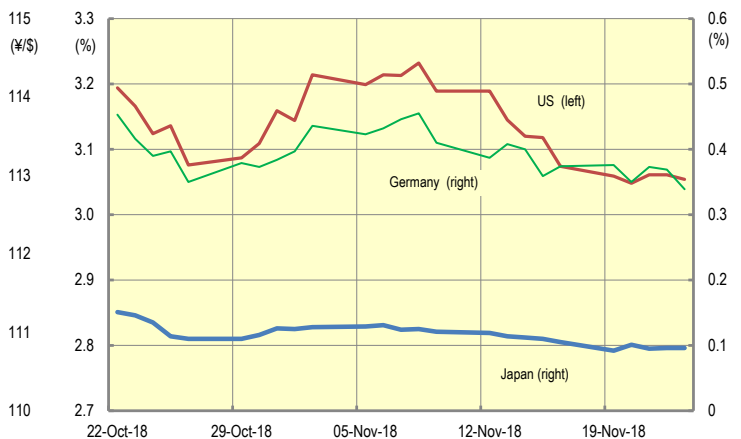
The USD/JPY traded in a narrow range at the start of last week, but then fell as US interest rates were pulled lower by a drubbing for US equities, especially high-tech stocks, following a Wall Street Journal report that Apple was cutting production orders for its new iPhone3 models. A significant deterioration for November US home builder sentiment also played a role. US interest rates continued declining on November 20 as US/European equities and the crude oil price pulled back sharply. The currencies of European, resource-rich, and emerging-market countries were hit by risk-off selling, while the yen and US dollar were bought. The USD/JPY briefly fell to 112.30, but rallied as US interest rates rebounded on the selling of Treasuries to liquidate long positions before the Thanksgiving holiday. The European Commission rejected Italy's 2019 draft budget and recommended sanctions unless Italy makes changes. However, as these moves were in line with market expectations, they did not lead to euro depreciation or yen appreciation. That said, US interest rates peaked on weak US economic indicators. Risk-off moves then pushed up the yen on November 22. Economic indicators that missed market expectations, including Germany's Manufacturing PMI and services PMI for November, led to selling of the euro. The US dollar's effective exchange rate was solid, due in part to the steep oil price drop.

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



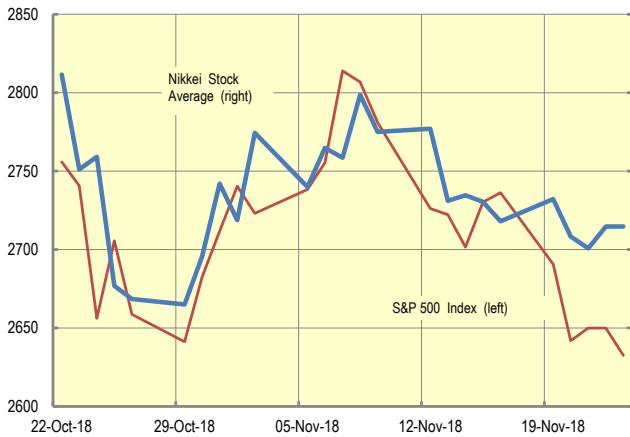
Source: Thomson Reuters; compiled by Daiwa Securities.

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



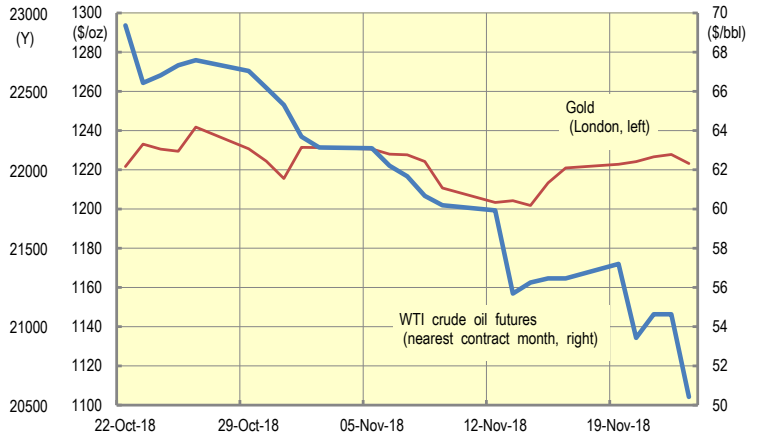
Source: Thomson Reuters; compiled by Daiwa Securities.

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



Source: Thomson Reuters; compiled by Daiwa Securities.

Chart: Commodity Market: Crude Oil Futures, Gold



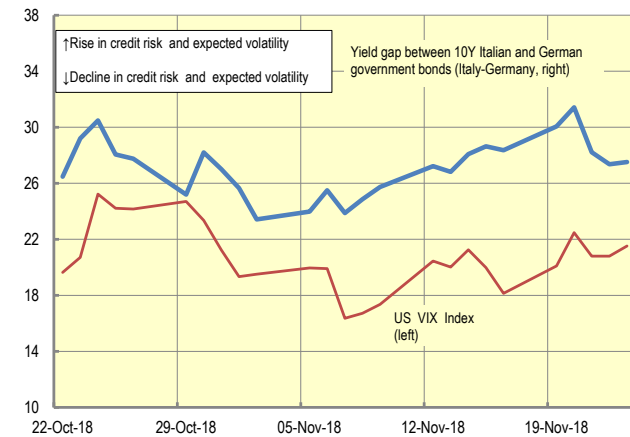
Source: Thomson Reuters; compiled by Daiwa Securities.

Focus on US-China talks during G20 summit

US-China summit holds key to forex market direction

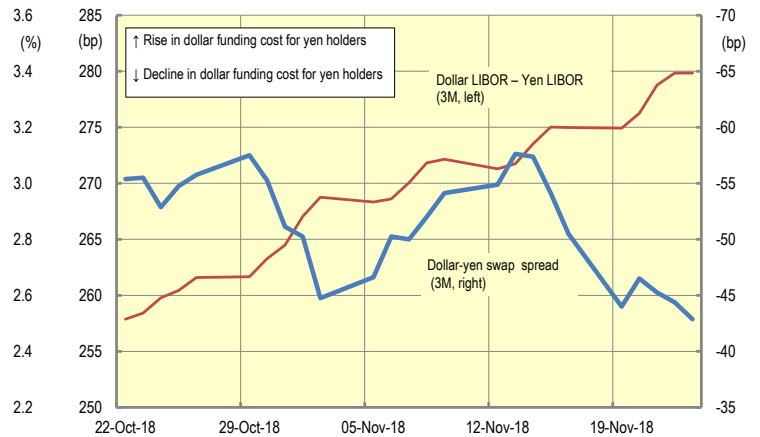
Leaders of the US and China plan to hold separate trade talks during the G20 summit in Argentina (November 30 to December 1). The focus will be on whether the US and China can agree to a trade war “ceasefire.” On November 16, US President Donald Trump praised a list of 142 measures China is willing to take to resolve trade tensions as “pretty complete,” but added that it was still unacceptable as four or five major items were omitted. While hinting that an agreement with China is possible, the US-side is apparently seeking further concessions from China. On November 17, US Vice President Mike Pence said that China has taken advantage of the United States for many years and warned that the US will not end its trade war until China changes its ways. While talks between the US and China could move forward at the G20 summit, Pence indicated that the US will not make any concessions.

Chart: US VIX Index and Gap Between Italian and German Long-term Yields



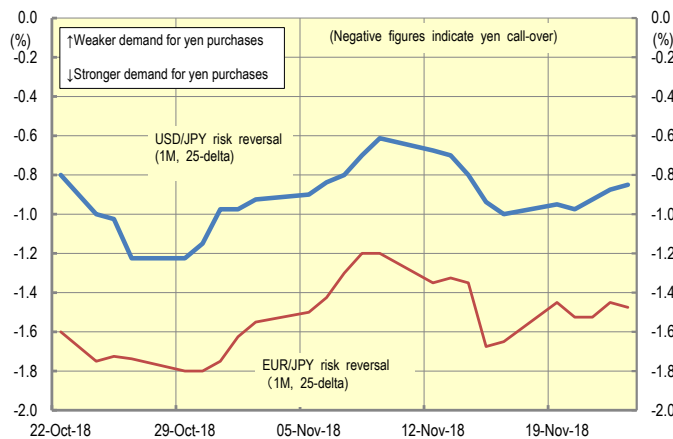
Source: Thomson Reuters; compiled by Daiwa Securities.

Chart: LIBOR Gap and Currency Swap Spread



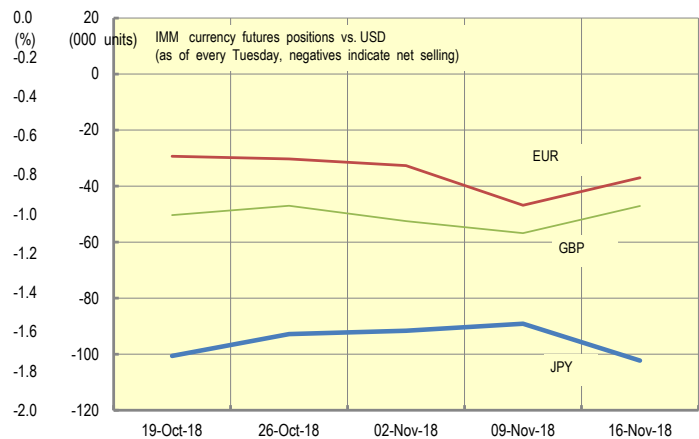
Source: Thomson Reuters; compiled by Daiwa Securities.

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.

US Commerce Secretary Wilbur Ross said on November 15 that “at best” the two sides will only agree to a framework for further talks when meeting during the G20 summit, suggesting the strong possibility that a full agreement will remain out of reach. Ross said that the US is still set to raise tariffs on Chinese goods as planned. On November 20, US Trade Representative Robert Lighthizer presented an updated report on a study into China’s intellectual property right and technology transfer policies. This report clarified that China has not fundamentally altered its unfair, unreasonable, and market-distorting practices that were cited when the investigation was launched in March. Will the US suspend the tariff hike planned for the start of 2019 (from 10% to 25% on \$200 billion in Chinese goods) if China proposes further concessions during talks at the G20 summit? Or will the US will follow through with the planned tariff hike as it still needs to determine whether China is seriously implementing the action plan for resolving trade issues? The latter seems the more likely outcome based on the series of comments from top US government officials. In any event, the outcome of US-China talks in Argentina will probably have some sway on foreign exchange markets.

Indicators point to economic deceleration

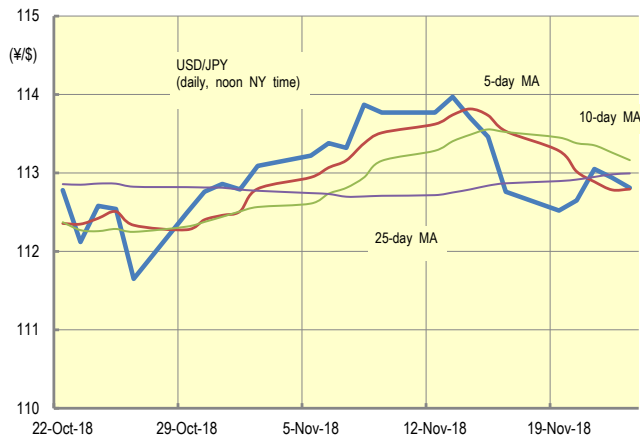
USD/JPY may fall on concerns about slowing US economy

US interest rates and the USD/JPY rebounded modestly, but a sustainable uptrend seems unlikely considering a decelerating trend for the US economy. New home starts and used homes sales grew in October, albeit only modestly, while the number of building permits declined and November home-builder sentiment deteriorated sharply. Furthermore, October durable goods orders declined sharply, indicating that US corporations are losing some desire to invest in equipment. One point of focus is weekly unemployment insurance initial claims. These claims have remained at a high level since June and the four-week moving average has consistently risen since mid-September. US corporations could be losing their willingness to hire new employees. There is the strong possibility that US interest rates and the USD/JPY could again fall as concerns about a slowing US economy mount.

Noteworthy currency: EUR

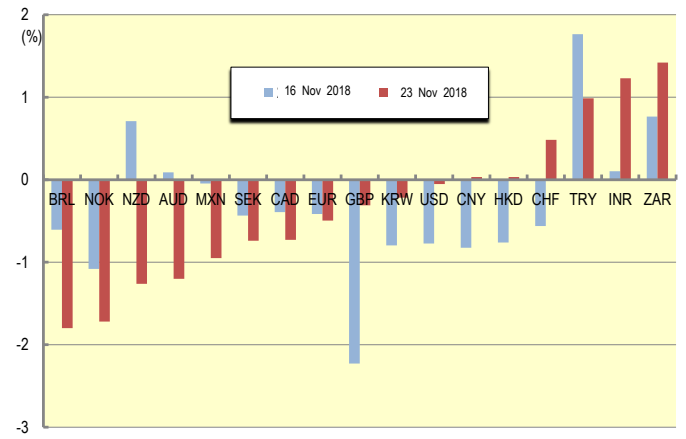
While investors are generally taking a wait-and-see approach to Brexit negotiations and Italy’s financial problems, pessimism about the Eurozone economy has surfaced after Germany’s PMI released last week significantly missed market consensus. Against this backdrop, there are expectations that Germany’s November IFO Business Climate Index, due out on November 29, will include readings somewhat weaker than those in the last survey. The euro will likely weaken if these results miss market expectations. That said, October retail sales (hard data), due out on November 30, are expected to show accelerated growth. The results for these indicators could easily sway the euro.

Chart: USD/JPY and Moving Average



Source: Thomson Reuters; compiled by Daiwa Securities.

Chart: Weekly Currency Performance (vs. yen)



Source: Thomson Reuters; compiled by Daiwa Securities.

Chart: Weekly Schedule for Major Economic Indicators/events

- 26-Nov Nov German IFO business climate index
- 27-Nov Sep US S&P Case-Shiller Home Price Indices
- 28-Nov Nov US Consumer Confidence Index (Conference Board)
Jul-Sep US GDP (revised)
- 29-Nov Oct US new home sales
Nov German jobs report
Nov eurozone Economic Sentiment Indicator (ESI)
Oct US personal income/consumption expenditures
- G20 finance ministers meeting (Buenos Aires)
- 30-Nov ○ FOMC minutes (7-8 Nov)
Oct Japan industrial production, shipments., inventories (preliminary)
Nov China manufacturing PMI (National Bureau of Statistics of China)
Nov eurozone CPI
Oct eurozone unemployment rate
Nov US Chicago Purchasing Manager's Index
- G20 summit meeting (until 1 Dec, Buenos Aires)
- US-China summit meeting (Buenos Aires)

Source: Compiled by Daiwa Securities.

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

Chart: Weekly Forex Forecasts, Noteworthy Currencies/factors

	19 - 23 Nov 2018 (actual)		26 - 30 Nov 2018 (forecasts)	
	Range	Weekend	Range	Weekend
USD/JPY	112.3-113.2	112.9	111.8-113.8	112.7
EUR/JPY	127.8-129.1	128.8	126.9-129.4	127.9
EUR/USD	1.132-1.148	1.135	1.126-1.146	1.135

Noteworthy currencies and factors

EUR	If indicators heighten pessimism about economy, euro would weaken
GBP	Pound would weaken if opposition to Brexit proposal mounts in UK Parliament
SEK	Prime Minister gave up third attempt to form cabinet; expected rate hike would weigh on krone

Source: Compiled by Daiwa Securities.

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[Standard & Poor's]

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[Moody's]

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[Fitch]

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- 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.

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