

# Forex Market View

## Factors affecting dollar and yen appreciation

- The dollar has risen more against developed market currencies than against emerging market currencies
- There has been no risk-off yen strengthening despite the euro weakening on EU economic slowdown
- Will worsening of US economic data shift the market from dollar strengthening to yen strengthening?

### USD/JPY forecast range (latest: noon New York time)

14 Feb- 13 Mar: Y107.0-112.0/\$ (Y110.84/\$ as of 13 Feb)

Forex Market View DSFE214

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Daiwa Securities Co. Ltd.

**From risk-on yen weakening to dollar strengthening driven by improving US economic data**

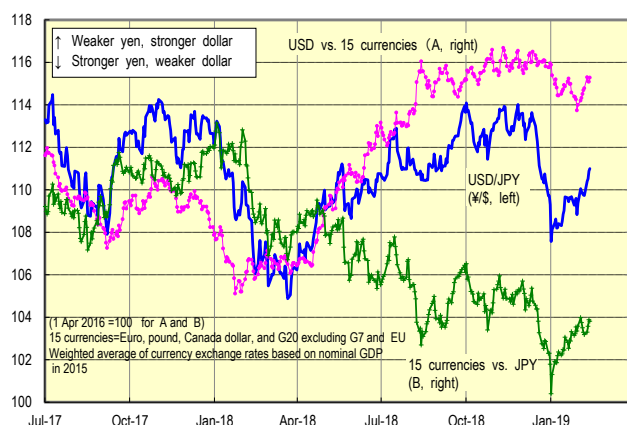
### The dollar has risen more against developed market currencies than against emerging market currencies

The USD/JPY rose above 110, but there was a shift in the driving factor from yen weakening to dollar strengthening. The value in yen terms of a basket of 15 major currencies excluding the yen and the dollar (the cross-yen) rose from its bottom in early January until 4 February (the next trading day after US jobs data were announced) but has weakened since then. In contrast, the exchange rate of the dollar vs. that same basket declined until 31 January, but has risen since February 1, following announcement of unexpectedly strong US employment data and the ISM manufacturing PMI. Thus, yen depreciation has faded while the dollar has shifted from a weakening to a strengthening trend. When the market moves from a risk-on weakening of the yen and dollar to a risk-off strengthening of the yen and dollar, the yen tends to strengthen more than the dollar does. Since that is not happening now, it may be the case that risk-on yen depreciation is losing momentum while the improvement of US economic data is strengthening the dollar.

**The dollar has risen more against developed market currencies than against emerging market currencies**

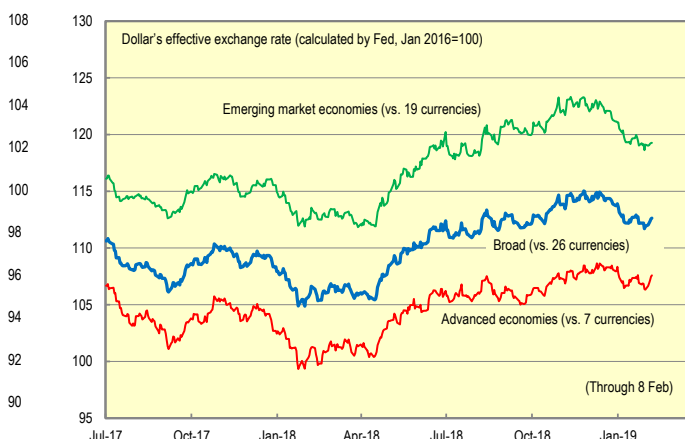
The dollar's effective exchange rate index announced by the Fed shows a clear rebound in the dollar index vs. seven developed market currencies but not much of a rebound vs. 19 emerging market currencies. If it was US economic data improvement and risk-off moves that triggered dollar appreciation, either both dollar indices should have risen similarly or the dollar index vs. emerging market currencies should have risen by more, because the high yielding currencies of emerging markets tend to decline more than developed market currencies do during risk-off markets. That is not what happened, however. The weakness of the dollar's appreciation vs. emerging market currencies indicates that there has not been much dollar appreciation driven by risk-off sentiment. Furthermore, the dollar's relatively greater appreciation vs. developed market currencies can be attributed not only to the dollar's strength but also to the weakness of those currencies.

Chart: Exchange Rates of USD, JPY, and Other Currencies



Source: Thomson Reuters; compiled by Daiwa Securities.

Chart: Dollar's Effective Exchange Rate



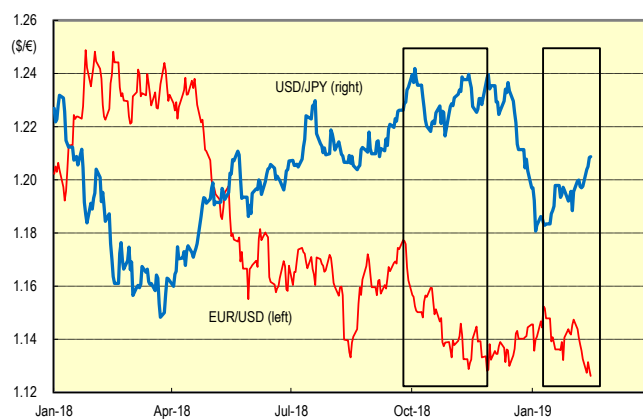
Source: Thomson Reuters; compiled by Daiwa Securities.

### There has been no risk-off yen strengthening despite the euro weakening on EU economic slowdown

**There has been no risk-off yen strengthening despite the euro weakening on EU economic slowdown**

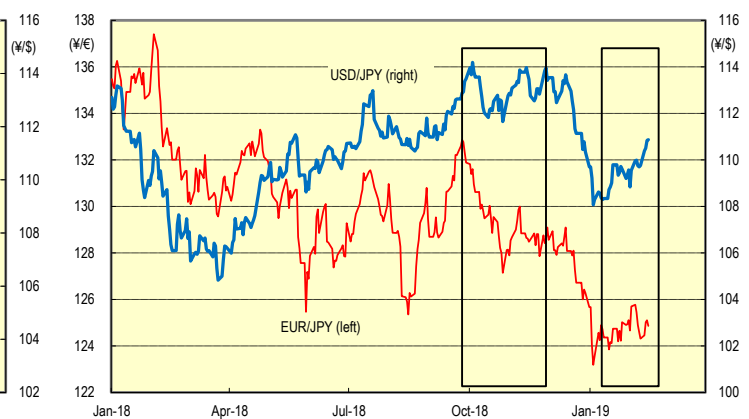
The developed market currencies that have declined the most vs. the dollar since the start of February are the euro, pound, and yen. The euro has been declining because the economic data for EU countries has continued falling short of market expectations. The pound has also been declining on rising concerns over a no-deal Brexit, brought by the lack of progress toward renegotiating an orderly deal with the EU as the March 29 deadline draws near. When the euro and pound were weakening against the dollar in Oct-Dec 2018 there were risk-off pressures strengthening the yen and keeping a lid on the USD/JPY. The USD/JPY started rising in January 2019, however. Although the EUR/JPY dropped sharply in Oct-Dec 2018, it rose in January 2019 and its decline in February was small. Concerns over an economic slowdown in Europe and a no-deal Brexit have put downward pressure on the euro and pound, but they led to dollar buying based on relatively stronger US economic data without clearly triggering risk-off purchases of the yen.

Chart: USD/JPY and EUR/USD



Source: Thomson Reuters; compiled by Daiwa Securities.

Chart: USD/JPY and EUR/JPY



Source: Thomson Reuters; compiled by Daiwa Securities.

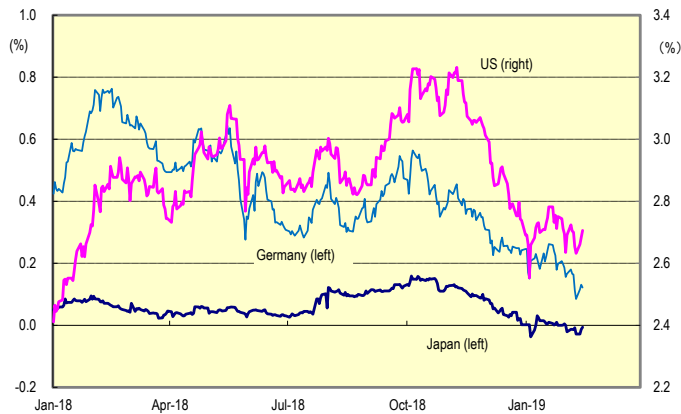
### Will worsening of US economic data shift the market from dollar strengthening to yen strengthening?

**The decline in long-term rates is constraining risk-off yen appreciation**

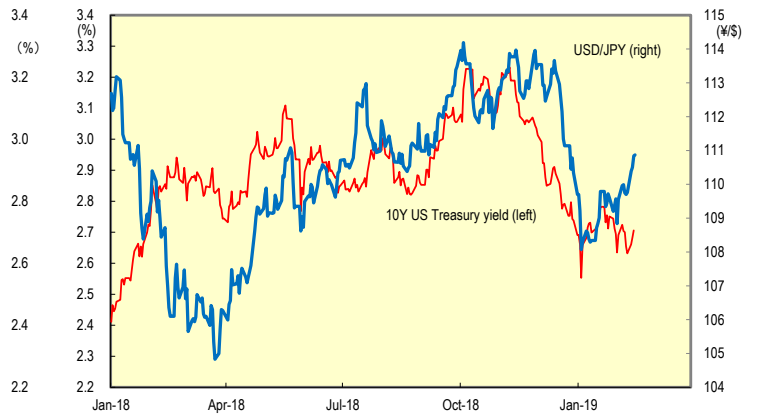
In the US, unlike in Oct-Dec 2018 when rate hike expectations kept long-term rates high, slight expectations of rate cuts put long-term rates in a declining trend, as in Germany. The interest rate environment is conducive to declines in both the USD/JPY and cross-yen rates. The likely reason that the USD/JPY has risen and cross-yen rates have been firm despite that is that interest rate declines have constrained both share price weakening and risk-off yen appreciation. In Europe, although long-term rates and currency values have declined on deterioration in the economic data, expectations that such declines will be a positive for the economy have kept share prices firm. In the US, share prices are being supported by strong economic data and declines in long-term rates brought by the fading of rate hike expectations. Additionally, share prices in both China and US are apparently being supported by expectations that additional tariffs can be avoided with the US and China signing a trade deal.

**Will worsening of US economic data shift the market from dollar strengthening to yen strengthening?**

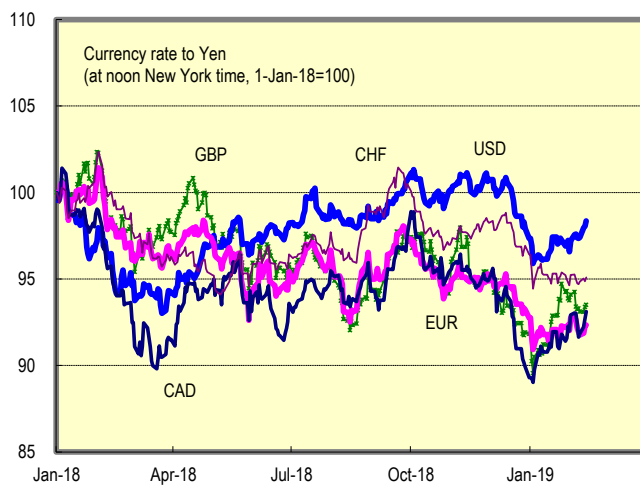
In other words, we think the existence of expectations that the global economy will not only worsen is constraining risk-off driven share price declines and yen appreciation. Even if the US and China strike a trade deal and additional tariffs can be avoided for the time being, however, it would probably not create any new positive effects on the global economy, while any risk-on effects from expectations of a trade agreement are time-limited and unlikely to last after the agreement. If previously strong US economic data were to start showing weakness or EU economic data continue to weaken, it may create concerns that an economic slowdown could not be contained even if long-term rates decline (and even if currencies declined) and thereby make the emergence of risk-off pressures more likely. US economic data can have a particularly strong impact on the global economic outlook and the market trend, and a worsening of that data would likely amplify risk-off moves and cause the FX market to shift from dollar appreciation to yen appreciation.

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


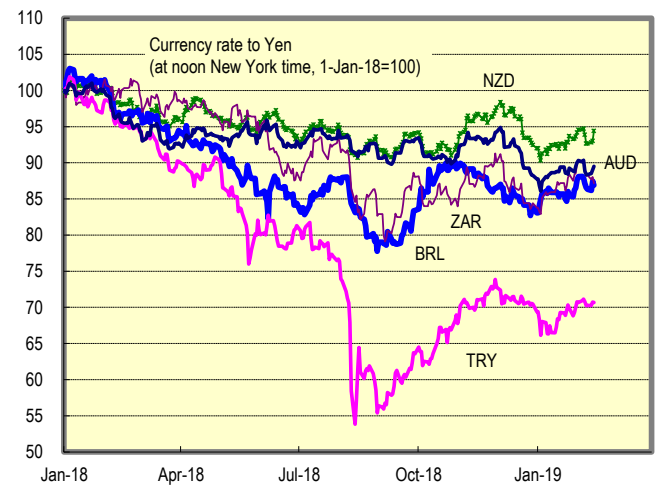
Source: Thomson Reuters; compiled by Daiwa Securities.

**Chart: USD/JPY and 10Y US Treasury Yield**


Source: Thomson Reuters; compiled by Daiwa Securities.

**Chart: Major Currencies/JPY FX Index**


Source: Fed, Thomson Reuters; compiled by Daiwa Securities.

**Chart: EM Currencies/JPY FX Index**


Source: Fed, Thomson Reuters; compiled by Daiwa Securities.

Chart: Currency Exchange Rate Forecasts

	Actual		Forecast				
	28 Sep	31 Dec	Jan-Mar	Apr-Jun	Jul-Sep	Oct-Dec	Jan-Mar
	2018	2018	2019	2019	2019	2019	2020
USD-JPY	113.7	110.3	109.0	110.0	107.0	105.0	105.0
			104-112	104-112	104-112	101-110	101-110
EUR-JPY	131.9	126.3	122.0	125.5	122.0	119.0	119.0
			118-128	118-130	118-130	115-127	115-127
AUD-JPY	82.1	77.7	76.5	79.5	76.0	73.5	73.5
			73-81	73-82	73-82	70-79	70-79
CAD-JPY	88.0	81.0	80.5	82.0	79.5	77.5	77.5
			77-85	76-85	76-85	74-83	74-83
NZD-JPY	75.2	74.0	73.0	75.0	72.0	69.5	69.5
			70-78	69-78	69-78	66-75	66-75
TRY-JPY	18.8	20.9	19.5	20.8	19.5	18.5	18.5
			17-22	17-22	17-22	16-21	16-21
ZAR-JPY	8.0	7.7	7.6	7.9	7.5	7.2	7.2
			7.2-8.3	7.0-8.3	7.0-8.3	6.7-8.0	6.7-8.0
BRL-JPY	28.1	28.5	28.0	29.8	28.2	27.0	27.0
			26-31	26-31	26-31	25-30	25-30
KRW-JPY	10.2	9.9	9.5	9.8	9.4	9.1	9.1
(100 KRW)			9.1-10.0	9.1-10.1	9.1-10.1	8.8-9.8	8.8-9.8
CNY-JPY	16.5	16.1	15.6	16.2	15.5	15.0	15.0
			15.2-16.5	15.0-16.5	15.0-16.5	14.5-16.0	14.5-16.0

Source: BIS, Fed, Thomson Reuters; compiled by Daiwa Securities.

Notes: 1) Actual shows market rates at noon NY time.

2) Forecast upper row; as of quarter end, lower row; range during quarter.

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In order to ensure the fairness and transparency in the markets, Credit Rating Agencies became subject to the Credit Rating Agencies' registration system based on the Financial Instruments and Exchange Act. In accordance with this Act, in soliciting customers, Financial Instruments Business Operators, etc. shall not use the credit ratings provided by unregistered Credit Rating Agencies without informing customers of the fact that those Credit Rating Agencies are not registered, and shall also inform customers of the significance and limitations of credit ratings, etc.

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- 3) Prohibition of the ratings in cases where Credit Rating Agencies have a close relationship with the issuers of the financial instruments to be rated, etc.
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### ■ Credit Rating Agencies

#### [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.
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- 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.

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Corporate Name: Daiwa Securities Co. Ltd.

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Chief of Kanto Local Finance Bureau (Kin-sho) No.108

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The Financial Futures Association of Japan  
Japan Investment Advisers Association  
Type II Financial Instruments Firms Association