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# Mizuho Dealer's Eye

## September 2018

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Mizuho Bank, Ltd.

Forex Department

Yuta Kikuchi, Forex Sales, Forex Department

# U.S. Dollar – September 2018

**Expected Ranges Against the yen: JPY109.00–113.00**

## 1. Review of the Previous Month

The dollar/yen pair's slide eased off over the latter half of August.

The pair hit a monthly high of 112.15 yen on August 1, but it then dropped back to the mid-111 yen mark on news that the Trump administration was considering placing further tariffs on Chinese products. As expected, the FOMC kept monetary policy unchanged, while its statement was also much the same as the previous month. The US employment data for July was released on August 3. Nonfarm payrolls had not grown as fast as the markets had expected, for example, so the pair fell to the lower-111 yen level.

The pair moved with a heavy topside at the lower-111 yen mark on August 6 as the benchmark 10-year treasury yield dipped below 2.93% for the first time in around two weeks. It then tumbled to the upper-110 range on August 8 on reports that China would hit US products with retaliatory tariffs. It bounced back to the lower-111 yen mark on August 9 as emerging-economy currencies weakened across the board, with the pair also supported when the greenback was bought against the euro. The pair dropped to 110.51 yen on August 10 as risk aversion increased on concerns about worsening relations between the US and Turkey.

With tensions rising between the US and Turkey on August 13, the pair fell to 110.11 yen, though it rallied slightly after the Central Bank of Turkey indicated it would 'take all necessary measures' to deal with a fall in the value of the Turkish lira. The pair then rose to a weekly high of 111.43 yen on August 15 as the markets focused on real-demand dollar buying. However, it then tumbled to the mid-110 yen level on concerns of a crisis in Turkey. The pair climbed to the upper-110 yen mark on August 16 on hopes for progress in trade talks between the US and China. Its topside then edged up to the lower-111 yen level after President Trump made some comments that appeared to signal a tolerance for dollar appreciation. The pair fell to the lower-110 yen level on August 17 after a Turkish court dismissed an appeal to free a US pastor.

The pair then weakened to around 110 yen on August 20 on news that President Trump was unhappy about the FRB chair Jerome Powell's predilection for rate hikes. This flow spilled over into August 21, with the pair tumbling to a monthly low of 109.78 yen. On August 23, Kansas City FRB president Esther L. George commented that President Trump's critical comments about rate hikes would not affect the FRB's policy assessment. This led to dollar buying, with the pair subsequently climbing above 111 yen. The pair then rose to 111.49 yen on August 24. As expected, FRB chair Jerome Powell indicated that rates would be lifted at a gradual pace during a speech at the Jackson Hole symposium on the same day.

With US/China trade talks making no concrete progress, the pair dipped below 111 yen at the start of the next week, on August 27. However, it then rose again on August 28 as concerns about trade frictions eased off. On August 29, the EU's chief Brexit negotiator Michel Barnier said the EU was "prepared to offer Britain a partnership such as there never has been with any other third country." The euro and pound were bought as a result. With the cross yen also rising, the dollar/yen pair hit 111.83 yen. The pair crashed to around 111 yen on August 30 as risk aversion grew on concerns about US/China trade relations. The pair moved around 111 yen on August 31.

## 2. Outlook for This Month:

The dollar/yen pair is expected to trade with a heavy topside in September.

Sentiments currently seem to be improving on bullish US stock markets and so on, but a flurry of events is lined up this month (the FOMC meeting, the US midterm elections, emerging-economy concerns, and European political risk), so it is hard to imagine the pair rising.

The FOMC will be meeting over September 25–26. At the meeting over July 31–August 1, the FOMC left the target range for the FF rate at 1.75–2.00%. In the accompanying statement, the FOMC upgraded its view of the economy to 'strong' on the back of the bullish real GDP growth over April–June, for instance, with the FOMC also indicating it would continue to lift rates at a gradual pace as the economy continued to grow at a healthy pace. As such, rate hikes look set to continue from here on, with the FOMC likely to make such a move when it meets this month. However, there is a danger that the FRB could retreat from its hawkish stance on pressure from President Trump, so caution will be needed. The global economy will also require monitoring in the medium to long term. US long-term interest rates are moving sluggishly right now. It is hard to fathom the reason for this given that US indicators are moving firmly on the whole and the FRB has indicated it will continue to lift rates. The gap between long- and short-term US treasuries has shrunken close to breaking below 20bp. Concerns are steadily growing about yield-curve inversion (an event signaling the approach of an economic recession).

The US will also be holding midterm elections on November 6. Seats are up for grabs in both houses of Congress, while 36 out of 50 states will also be holding gubernatorial elections. The Republicans currently hold a majority in both houses, but with President Trump's approval ratings on the slide, the stage is set for a fierce battle. It seems likely the Democrats will regain a majority in the lower house. As such, there is a real political risk that President Trump might swing further toward protectionism as he seeks to garner support by tackling the US's huge trade deficit.

Attention should also be paid to the potential for risk aversion on political risk in Europe. With the real deadline for the Brexit negotiations looming in October, on August 23 the UK published the first in a series of papers advising people and businesses about what to do in the event of a no-deal Brexit. On August 29, though, the EU's chief Brexit negotiator Michel Barnier said the EU was "prepared to offer Britain a partnership such as there never has been with any other third country," so events will require monitoring from here on.

With long- and short-term interest rates flattening out in the US, the greenback will not get much support on the interest-rate front. Furthermore, news about trade tensions will probably increase in the run up to the US midterms. As such, there will probably be limits to how high the dollar can rise.

## Dealers' Market Forecast

(Note: These opinions do not necessarily agree with the other contents of this report.)

### Bullish on the dollar (3 bulls: 109.00–114.00, Core: 109.00–114.00)

| | | |
|---|---|---|
| Fujimaki | 109.00 – 114.00 | Funds are fleeing from China, Turkey and other emerging markets, but concerns about political risk are making the euro a hard currency to buy, so in the end these funds are likely to converge on the dollar. At the same time, bullish economic conditions will probably lead to yen selling, so the dollar/yen pair will probably rise this month. |
| Okamoto | 109.00 – 114.00 | There has been a round of yen buying on risk aversion after the currencies of Turkey, Argentina and other emerging economies tumbled, but this trend has eased off. The dollar/yen pair is also likely to move firmly on expectations for progress in the NAFTA negotiations and other US trade talks. With the US expected to impose tariffs on $200 billion worth of Chinese goods, the pair could swing lower again if events in the emerging economies lead to risk aversion, so caution will be needed. |
| Okuma | 109.00 – 114.00 | The US economy is still moving firmly, despite ongoing concerns about trade frictions, with US stocks continuing to outperform other equities in the stock markets. The dollar will probably be bought during phases of risk aversion. With consumer-related indicators also moving bullishly, it seems almost certain that the FRB will implement another rate hike in September. As a result, the dollar/yen pair is expected to move firmly this month. |

### Bearish on the dollar (8 bears: 107.00–113.00, Core: 108.00–112.25)

| | | |
|---|---|---|
| Tauchi | 108.00 – 113.00 | The dollar/yen pair continues to be weighed down by the US/China trade war. With President Trump also accusing China of currency manipulation, negotiations look set to be stormy from here on. There are even suggestions that the US might set off a currency war by intervening to sell the greenback. Under these circumstances, the dollar/yen pair will probably be held down by deep-rooted cautiousness. |
| Kato | 108.00 – 113.00 | President Trump has accused China and Europe of currency manipulation, but he has not mentioned Japan, which suggests Japanese moves in this area have proved successful. The dollar/yen pair is moving heavily, but providing the Bank of Japan treads carefully and does not explicitly bring easing to an end, the pair is unlikely to slide further. |
| Yamashita | 107.00 – 112.00 | The FOMC looks set to lift rates when it meets in September. However, more members have started to talk about yield-curve inversion, so it is hard to imagine the FOMC releasing a hawkish statement. Emerging-economy currencies look set to continue moving erratically, so the yen will be susceptible to buying. This is a further reason why the dollar/yen pair will probably move with a heavy topside. |
| Seki | 108.00 – 112.00 | The situation in Turkey has not completely calmed down. If emerging-economy currencies are sold again, this could lead to risk aversion, so caution will be needed. US interest rates continue to flatten out too, so if it seems the US will stop lifting rates, the dollar/yen pair will probably grow heavier on the topside. |
| Mitsuishi | 108.00 – 113.00 | The dollar/yen pair is expected to trade in a range overall, but there remain several factors capable of dampening market sentiments, such as fears of a trade war and concerns about the Turkish lira and other emerging-market currencies. As such, market participants should be on guard against downside risk. |
| Ueno | 108.00 – 112.00 | A number of risk factors remain, such as the situation in Turkey and US/China trade frictions. These factors are unlikely to be resolved any time soon and this will probably lead to risk aversion. Under these circumstances, the dollar and yen will both be susceptible to buying and the dollar/yen pair will probably trade within a narrow range, though if anything yen bullishness looks more likely. |
| Moriya | 107.00 – 111.00 | The markets have factored in a September FOMC rate hike, so such a move is unlikely to lead to dollar buying. Of course, dollar selling could also be prompted if the markets focus on a slower pace of US rate hikes from 2019 onwards. The dollar/yen pair's topside could also be weighed down again by risk aversion related to emerging-market currencies. |
| Tsuruta | 108.50 – 112.50 | There are fears that the Turkish lira and other emerging-market currencies could nosedive. Risk aversion could also be fanned by concerns of intensified US/China trade frictions or uncertainty about US/Japan trade talks. Under these circumstances, it is hard to imagine US long-term interest rates climbing further, with the dollar/yen pair unlikely to rise. As such, the yen is likely to face buying pressure this month too. |

Ryutaro Fujimaki, Forex Sales, Forex Department

# Euro – September 2018

**Expected Ranges** **Against the US$: US$1.1300–1.1800**
**Against the yen: JPY125.00–132.00**

## 1. Review of the Previous Month

In August, the euro/dollar pair moved in a range from the $1.13 mark to the lower-$1.17 level.

The pair weakened to the mid-$1.16 mark on August 1 before the release of the FOMC statement. The statement turned out to be much as expected, so the impact on the currency pair was muted. It then fell to the upper-$1.15 level on August 2 on news that the Italian government was divided on the issue of the budget for fiscal 2019. The US released some mixed employment data for July on August 3, so the pair closed the day trading at the mid-$1.15 mark.

Concerns about the German economy intensified on August 6 on the release of a worse-than-expected manufacturing orders indicator for June. The pair tumbled to the lower-$1.15 range, though it then bounced back to the upper-$1.15 mark. It climbed to the $1.16 range on August 7 on rising German interest rates. The trend spilled over into August 8, with the pair temporarily hitting $1.1628. However, the pound then fell after an official from the Bank of England (BOE) said it was hard to imagine the UK's situation improving when it came to the trade issue. The single currency was also pulled lower, though the euro/dollar pair then bounced back to the lower-$1.16 level. With emerging-economy currencies sliding across the board on August 9, the pair dropped to the lower-$1.15 mark on rising risk aversion. The euro-selling trend continued on August 10, with the pair closing the day at the lower-$1.14 level.

With the markets focusing on political uncertainty in Turkey and Italy on August 13, the pair dipped to the upper-$1.13 mark. It moved in the $1.14 range for a time on August 14 before sliding back to the lower-$1.13 level. Market sentiments improved on August 15 on news that Qatar had pledged to provide Turkey with direct investment, so the pair rallied to the mid-$1.13 range. The pair moved more-or-less flatly on August 16.

It moved firmly on August 17 to close at $1.1438. Reports emerged on August 20 that President Trump was unhappy with FRB chair Jerome Powell's predilection for rate hikes. As the greenback weakened across the board, the euro/dollar pair climbed to $1.1485. It edged above the key $1.15 mark on August 21 and then climbed to the upper-$1.15 level while activating stop losses. The dollar fell further on August 22 on uncertainty about the Trump administration, with the pair temporarily hitting $1.1623. Euro selling intensified again on August 23, with the pair dropping back below $1.1550. FRB chair Jerome Powell adopted a cautious attitude towards rate hikes during a speech at the Jackson Hole symposium on August 24. The greenback was subsequently sold, with the euro/dollar pair rising to $1.1639.

The pair strengthened to the upper-$1.16 level on August 27 on the bullish result of the German IFO Business Climate Index for August. The dollar was bought on August 28 on the bullish results of several US economic indicators, with the pair dropping to the upper-$1.16 level. Concerns that the UK would leave the EU without a deal eased off on August 29 following comments by the EU's chief Brexit negotiator Michel Barnier, so the euro was bought and the currency pair bounced back to the lower-$1.17 level. It then tumbled to the lower-$1.16 range on August 30 after Mr. Barnier said a no-deal Brexit was still a possibility.

## 2. Outlook for This Month:

The euro/dollar pair is expected to move with a heavy topside in September.

When it met in June, the ECB Governing Council said it would keep policy rates fixed until summer 2019, thus confirming that negative interest rates will remain in place for the time being. The existence of negative interest rates is a crucial factor for a currency like the euro, so with the situation likely to remain unchanged, the euro's topside will probably grow heavier. Furthermore, yields on Italian government bonds continue to move erratically, with concerns about Italy's creditworthiness still lingering. Populism is rearing its head in several other countries too, with uncertainty also likely to continue when it comes to the Brexit issue. Concerns are also growing about Turkey, a country with a deep geographical connection to Europe. If these concerns intensify, this could lead to growing nervousness in Europe.

Concerns about a trade war with the US continue to smolder away too. With the US midterm elections looming, President Trump may make some inflammatory comments as he seeks to grab the attention of US voters. Last month saw the release of a bullish German IFO Business Climate Index for August. The euro has weakened these past few months on a sell-off and it is possible that the European economy is starting to recover on the back of the weak euro. To gauge whether this is indeed the case, market participants will need to keep a close watch on the economic indicators released from here on.

The euro is moving bearishly, as mentioned above, while the prices of crude oil and other commodities are also moving steadily, so inflation could pick up going forward. When it comes to euro positioning, speculators have built up net shorts. Until now, the euro has been pulled lower by speculators unwinding their long positions, but there is also a risk that speculators may unwind their short positions from here on. In this sense, the situation will be ripe for some position adjustments if the euro/dollar pair rises. Looking at the charts, the key factor this month will be whether the pair drops clearly below $1.15 or whether it continues to move firmly at this level.

## Dealers' Market Forecast

(Note: These opinions do not necessarily agree with the other contents of this report.)

### Bullish on the euro (1 bull: 1.1400–1.2000, Core: 1.1400–1.2000)

| | | |
|---|---|---|
| Okamoto | 1.1400 – 1.2000 | The euro plunged on the Turkey crisis, but its losses are being pared back as sentiments improve. The impact on the eurozone's real economy will probably be limited given the size of Turkey's economy. The situation in Italy is also unlikely to lead to an exit from the EU, so it will probably not prove much of a risk. The euro/dollar pair will be supported by buying when it weakens, so it is expected to move firmly this month. |

### Bearish on the euro (10 bears: 1.1100–1.1800, Core: 1.1300–1.1800)

| | | |
|---|---|---|
| Tauchi | 1.1300 – 1.1800 | Italy's budget proposal for the next fiscal year suggests the country is likely to move down the path of fiscal expansion in blithe disregard for the EU's rules on balanced budgets. Some reports also say Italy has asked the ECB to buy its sovereign debt, so there is likely to be deep-rooted cautiousness when it comes to Italy. With the Turkish currency crisis also continuing to smolder away, the euro/dollar pair looks set to move heavily this month. |
| Kato | 1.1100 – 1.1800 | Events in Turkey have led to a flare-up of risk in other emerging nations like Argentina and Brazil. Market participants will need to watch to see whether this risk spreads to Spain and so on. As such, the euro/dollar pair looks set to continue trading with downside risk for a time in September. |
| Yamashita | 1.1300 – 1.1800 | The deadline for the Brexit talks is looming next month, but no agreement has been reached yet and the possibility of a no-deal Brexit is rising. With Europe also facing an Italian-led crisis about accepting refugees, an early ECB rate hike looks very unlikely. There will probably be more moves away from the euro this month. |
| Seki | 1.1300 – 1.1800 | Europe faces several negative issues, such as Italian political instability and the crisis in Turkey. There are also concerns about the direction of the Brexit talks. As such, there are not many factors conducive to euro buying, with the euro/dollar pair set to move bearishly this month. |
| Mitsuishi | 1.1200 – 1.1800 | The euro faces a number of internal and external risks, including: the divergence in the monetary policies of Europe and the US; concerns about the crisis in Turkey; the Brexit issue; and concerns about the fiscal situation in some EU nations. As such, the euro/dollar pair will probably move with a heavy topside this month. |
| Fujimaki | 1.1300 – 1.1800 | The ECB is likely to stick to its policy of negative interest rates, while market participants are concerned about the situation in Turkey and Italy, so there are no reasons to actively buy the single currency. As such, the euro/dollar pair looks set to move bearishly on the whole. However, euro bearishness could also start to have a positive impact on the economy and inflation. |
| Ueno | 1.1200 – 1.1800 | The euro/dollar pair will probably be swayed by risk factors in the short term. Europe faces several risk factors, such as the situation in Turkey and the Italian budget issue. These are unlikely to be resolved any time soon. The bearishness of emerging-market currencies is also likely to make the greenback a comparatively attractive currency, so the euro/dollar pair looks set to move with a heavy topside this month. |
| Moriya | 1.1300 – 1.1800 | Hopes for an early ECB rate hike are unlikely to flare up. The markets were also roiled by the crisis in Turkey last month and the situation remains up in the air. As market participants continue to focus on European political risk, the euro will be susceptible to selling. |
| Tsuruta | 1.1300 – 1.1800 | The euro/dollar pair renewed a yearly low last month, mainly as a result of the crisis in Turkey. With Turkey showing no signs of releasing the US pastor, market participants will continue to focus on the risk of a slide in the value of emerging-market currencies. In Europe, meanwhile, the Italian government will be submitting its budget proposal to parliament. This could lead to an intensification of fiscal concerns. As such, the euro/dollar pair looks set to move bearishly this month. |
| Okuma | 1.1300 – 1.1800 | Though the crisis in Turkey has cooled off for now, the euro will still be susceptible to downswings on the bearishness of emerging-market currencies. The euro also faces a number of downside risks, including uncertainty about the fiscal and political situation in Italy and concerns about a 'no-deal Brexit.' As such, the euro/dollar pair looks set to move bearishly this month. |

Taihei Yamamoto, Europe Treasury Department

# British Pound – September 2018

| Expected Ranges | Against the US$: | US$1.2650–1.3100 |
|---|---|---|
| | Against the yen: | JPY140.00–147.00 |

## 1. Review of the Previous Month

In August, the GBP/USD pair moved bearishly after opening the month at the $1.31 mark. The EU's chief Brexit negotiator Michel Barnier commented that a Brexit treaty was 80% agreed, with a satisfactory conclusion in sight. UK Prime Minister Theresa May also cut short her summer vacation to return to the business of Brexit from August 6, but the reaction of the markets was frosty and the currency pair traded with a black candlestick for seven days in a row. There was a noticeable slump in UK business confidence. The UK July Services Purchasing Managers Index (PMI) hit 53.5, its lowest level in three months, while the July Manufacturing PMI dipped to 54.0. New orders growth had been particularly sluggish since June. This suggested new business ventures were being kept in check by uncertainty about the Brexit issue.

The closely-watched Bank of England (BOE) policy rate statement saw all nine members of the Monetary Policy Committee (MPC) voting to lift the rate to 0.75%. In his press conference, though, BOE governor Mark Carney said corporate sentiments were moving bearishly on the Brexit issue, with the BOE in no rush to lift the policy rate again. The markets had essentially factored in the rate hike, so the move was actually met with pound selling. The GBP/USD pair then broke below $1.30 the following day when Mr. Carney told the media that a no-deal Brexit was a distinct possibility and that a rate cut might be needed in future.

An opinion poll released on August 6 revealed that a record 76% of respondents had voiced no confidence in the May administration, with sterling falling lower as a result. The UK's international trade secretary then told a UK newspaper there was a 60% chance of a no-deal Brexit. The pound was also sold when BOE MPC member Ian McCafferty suggested that the housing market in London could be hit by European bankers pulling out substantial funds. News emerged on August 9 that the ECB was concerned that Turkish borrowers might not be hedged against a fall in the value of the Turkish lira and might start defaulting on foreign-currency loans. The UK is also heavily exposed to Turkish assets, so this news dragged sterling lower, with the GBP/USD pair renewing a 14-month low. In response, the prime minister's press secretary said the pound's value would be decided by the markets, thus signaling a tolerance for pound depreciation.

The UK July CPI data was released on August 15. Prices were up 2.5% y-o-y, the fastest pace of growth since November 2017. With wages only growing by 2.4% (data released August 14), this meant real wages had actually fallen, so the markets reacted by selling the pound. The currency pair weakened to a monthly low of $1.2662. The UK's Brexit secretary Dominic Raab began negotiations

with the EU's chief Brexit negotiator Michel Barnier from August 21. The UK government also released some no-deal warnings on August 23. As a result, market participants held off from testing the pair's downside. The dollar was also sold when President Trump expressed his dislike for FRB rate hikes, with the pair subsequently shooting up to $1.2936.

## 2. Outlook for This Month:

There are still no signs of a compromise when it comes to the Brexit negotiations. Opinion polls show support for a new Brexit referendum rising to 42%, above the 40% who oppose such a move. Support for the Liberal Democrats has also risen to the 10% mark after the party pledged to hold a second referendum. However, hard-Brexiteers in the Conservative Party will be releasing their own policy document in September. This document will probably be supported by 60 to 80 MPs, more than the 48 MPs needed to trigger a confidence vote in the prime minister, so there is likely to be renewed debate about a change of leadership. With the UK's international trade secretary Liam Fox saying Theresa May's proposal to prolong negotiations would be a 'complete betrayal,' for example, concerns are growing about more cabinet resignations, so caution will be needed. In August, the UK government published the first in a series of papers advising people and businesses what to do in the event of a no-deal Brexit, but these were just the first in a series of reports set for release over the next few weeks, so there will probably be a growing fear that time is running out.

With UK households now spending more than they are earning for the first time in 30 years, the BOE will be keeping a close eye on borrowing costs and it will have a hard time steering toward an exit. With the UK yet to formulate a clear Brexit policy, the BOE has indicated it is in no rush to lift rates again. Market attention was also drawn to the fact that some investors took out options betting on a BOE rate cut just one week after the bank had announced a rate hike. Based on these impending risks, it seems very unlikely that the BOE will lift rates again over the next few months. As such, there is a severe shortage of factors capable of shifting the GBP/USD pair's direction within the year. As for external factors, the US is stepping up its trade wars and there is no sign of things calming down. US opinion polls show more people saying President Trump is doing a bad rather than a good job (58% to 41%), though Mr. Trump does not seem particularly bothered. The friction between the US and Turkey has led to a sharp fall in the value of the Turkish lira and there is a danger this risk could spread over into Europe. Based on all of this, there do not seem to be any factors capable of supporting pound buying, apart from a sense that sterling might be at a good level.

A glance at the political and economic schedule for September reveals that the UK parliament will be debating Brexit again over September 4–13. Reports say the UK prime minister will propose that the UK sticks to EU rules for a longer period, but this is likely to lead to opposition from eurosceptics in her own party. Hard Brexiteers will be releasing their own Brexit plan and they are likely to take exception to Mrs. May's plans. The next key event will be the EU heads of state meeting on September 20. This will probably discuss Brexit in an informal capacity. UK cabinet members have been visiting several EU nations to conduct behind-the-scenes talks, so this meeting will provide clues

as to whether these moves have been successful and whether the two sides are likely to reach an agreement. The opposition Labour Party will be holding its annual conference over September 23–26. Given the UK's hung parliament, the Tories may end up asking Labour for support. The Conservative Party conference will also take place from September 30. The Tories will be announcing some medium- to long-term policies, but last year's conference was a farce, with the prime minister losing her voice and an intruder also handing Mrs. May a certificate of separation from employment.

Kanako Imamura, Sydney Office, Asia & Oceania Treasury Department

# Australian Dollar – September 2018

| Expected Ranges | Against the US$: | US$0.7050–0.7350 |
|---|---|---|
| | Against the yen: | JPY78.50–82.50 |

## 1. Review of the Previous Month

The AUD/USD pair dropped to $0.7177 in August as risk aversion increased on an intensification of trade frictions and financial market turmoil after the Turkish lira fell sharply.

After opening the month at the lower-$0.74 mark, the pair then fell to the mid-$0.73 level after the markets reacted badly to news that the Trump administration was planning to raise tariffs on $200 billion worth of Chinese goods from the initially-planned 10%. It then continued to trade between the mid-$0.73 mark and the lower-$0.74 level. As expected, the board of the Reserve Bank of Australia (RBA) kept the cash rate fixed at 1.50% when it met on August 7, so the impact on the currency pair was limited. The pair hit a monthly high of $0.7453 on September 9, though it then slipped to $0.73 on concerns about global trade frictions. The RBA then released its Quarterly Statement on Monetary Policy, but this contained nothing new, so the pair traded at the upper-$0.73 level amid a dearth of incentives.

Market fears were roused mid-August when the Turkish lira fell sharply. Amid concerns that this trend might ripple across to other emerging-market currencies, bonds were bought and major stocks suffered conspicuous falls. As investors steered clear of risk assets, the currency pair dipped below $0.7300 on August 13 to hit the mid-$0.72 mark. The Central Bank of Turkey then announced it would provide the markets with liquidity, but concerns about the situation in Turkey led to attempts on the Australian unit's downside, with the AUD/USD pair tumbling to $0.7203 on August 15. The Turkish lira rallied on August 16. With China's Ministry of Commerce then announcing it would send a delegation to the US late August for trade talks, hopes grew for an easing of trade tensions, so the currency pair bounced back to the lower-$0.73 level.

The Australian political world was rocked late August when storm clouds gathered around prime minister Malcolm Turnbull's leadership. Mr. Turnbull won a Liberal Party leadership vote on August 21, but with several cabinet members then resigning, Mr. Turnbull said he would not stand again if there was another leadership vote. The markets reacted badly to this political turmoil, with the AUS/USD pair falling to the mid-$0.72 mark. With US/China trade talks failing to produce any significant results, the pair fell to $0.7238 in advance of the next Liberal Party leadership vote on August 24. Finance minister Scott Morrison won the vote and became the next prime minister, but he said he would not shift policy significantly, so political turmoil was reined in and the pair rallied to the lower-$0.73 mark. Australia released its private-sector capital investment data on August 30. At -2.5%, the figure was weaker than expected, so the currency pair fell to the mid-$0.72 level. On August 31,

the markets reacted badly to news that Canada and the US had not reached an agreement during the North America Free Trade Agreement (NAFTA) negotiations, so the AUS/USD pair renewed a 2018 low of $0.7177.

## 2. Outlook for This Month:

The AUS/USD pair will face a number of uncertainties in September too, including global trade frictions, Iranian sanctions and the situation in Turkey, so the pair is expected to continue trading with a heavy topside.

In August, New Zealand's central bank said it expected to keep long-term policy rates fixed through to 2020. The RBA has reiterated that it will continue to keep policy rates at record-low levels for the time being, but with more Australian economists predicting that Australian policy rates will be also kept at current levels through to 2020, the Australian dollar will be a hard currency to buy. On the other hand, the markets have essentially priced in a rate hike when the FOMC meets on September 26, so even if the FOMC does make such a move, the impact on the markets is likely to be negligible. The FOMC will also be releasing its projections for the economy and the federal funds rate (the dot chart), but if the latter projection diverges from the one released at the previous meeting, this could lead to US-dollar selling or buying, with the AUS/USD pair moving accordingly.

The markets are monitoring the direction of the NAFTA renegotiations with Canada, the US/China trade talks, the US sanctions on Iran, and the situation in Turkey (a new factor that emerged last month). US stocks fell in the first half of 2018, but they have bounced back over the last two months. However, the Shanghai Composite Index continues to move bearishly and the Australian dollar could be sold on risk aversion if major stocks tumble across the world, so caution will be needed.

The pair continued to move in a range between $0.73–0.74 for around two months, but its downside was tested last month and it has fallen to a new range between $0.72–0.73, with bearish sentiments growing. The pair's downside will be supported at $0.7160, its low from December 2016, while it will meet upper resistance at $0.7400 and $0.7495.

Several Australian economic indicators will be released in the first week of September. The release of the 2Q Australian GDP data on September 5 will draw the most attention, with the RBA predicting that GDP will hit 3.25% in 2018.

Hiroko Nasu, Canada Office, Global Markets Coordination Department

# Canadian Dollar – September 2018

| Expected Ranges | Against the US$: | C$1.2730–1.3175 |
|---|---|---|
| | Against the yen: | JPY84.55–87.11 |

## 1. Review of the Previous Month

The Canadian dollar was bought at the end of July and this trend spilled over into August, with the USD/CAD pair opening the month at C$1.3027.

The Canadian trade balance for June was released on August 3. At -C$630 million, the scale of the deficit was down sharply on the forecast for -C$2.3 billion. This was the lowest deficit since January 2017. This was probably due in large part to the +2.1% upswing in exports in June. The result was significantly better than expected, so the Canadian dollar was bought directly after, with the USD/CAD pair falling from C$1.3020 to C$1.2981 on the same day.

After a three-day weekend, the pair began trading again at C$1.2970. On June 6, Canada criticized Saudi Arabia's arrest of a human rights activist and called for his release. The Saudi Arabian government called this 'blatant interference' and it said it would cease any new trade or investment with Canada. The currency pair subsequently rose to C$1.3075 on August 7, but it then fell back to the lower-C$1.30 mark on a growing sense that the Saudi Arabian sanctions would only have a minimal impact on the Canadian economy.

August 10 saw tensions between the US and Turkey worsening after the US doubled the tariff rate on Turkish goods. This came after Turkey had turned down a US request to release an American pastor who had been placed under house arrest after being accused of participating in an unsuccessful coup d'etat in 2016. The Turkish lira crashed and this led to market turbulence. Risk aversion saw commodity currencies like the Canadian and Australian dollars being sold against refuge currencies like the greenback and the yen, with the USD/CAD pair rising to C$1.3177 on August 12.

The Canadian CPI data for July was released on August 17. At +3.0% y-o-y and +0.5% m-o-m, the data was up sharply on prior forecasts (+2.5% y-o-y and +0.1% m-o-m). The Canadian unit soared as a result, with the pair dropping from C$1.3150 before the announcement to C$1.3081.

In his closely-watched speech at the Jackson Hole symposium late August, Bank of Canada (BOC) governor Stephen Poloz stuck to the script and failed to make any noteworthy comments. He did express the opinion that the bullish CPI data in July was just a transitory factor. As such, expectations for a rate hike at the September 5 BOC meeting fell, with bets on such a move dipping to 19.5% as of August 27.

News also emerged on Monday, August 27 that the US and Mexico had reached an agreement in the NAFTA renegotiations. As hopes grew that Canada would also join the talks again, the Canadian dollar soared and the USD/CAD pair dropped 0.85% after opening in NY to plunge to C$1.2956.

## 2. Outlook for This Month:

Canada might see a rate hike in September depending on the results of Canada's 2Q GDP data or on whether an early agreement is reached in the NAFTA talks.

Canada has released several better-than-expected indicators, including the May GDP data (released at the end of July), the June trade balance and the July CPI data. At the Jackson Hole symposium on August 24, though, BOC governor Stephen Poloz said it would be wise to take a 'gradual approach' to monetary policy, thus sticking to the tone of the statement released after the July BOC meeting. As such, at this moment in time it seems very unlikely that the BOC will lift rates in September. Most observers believe the next rate hike will take place in October. However, August 27 saw an announcement that the US and Mexico had reached an agreement in the NAFTA renegotiations. Renegotiations between Canada and the US are also kicking off, so if the two sides reach an early agreement before the BOC meeting on September 5, the meeting could spring a surprise. Indeed, a surprise could also be in store depending on the GDP results for June and 2Q (released August 30). In a press conference on August 29, Canadian prime minister Justin Trudeau said a deal could be made by August 31, provided it was a good deal for Canada.

There is a growing sense of optimism in the markets when it comes to trade. Furthermore, crude oil prices (WTI) have a strong correlation to the Canadian dollar's movements, and though they dipped temporarily to $64/barrel on the crisis in Turkey, they then bounced back to $69/barrel and they are now trading stably at highs. This will also support the Canadian unit.

If the NAFTA negotiations drag on longer than expected or become deadlocked, this will probably lead to some Canadian-dollar selling.

The Canadian 2Q GDP was a key indicator attracting a lot of attention before the September 5 BOC meeting. At +2.9%, though, it ended up dipping slightly below the forecast of +3.1%. The probability of a September rate hike dipped further on the result and the Canadian dollar saw more selling. However, the data was slightly above the BOC's projection for +2.8%, so with exports also starting to increase, it seems the Canadian economy is enjoying firm growth.

Yasunori Shimoyama, Seoul Treasury Office

# Korean Won – September 2018

| Expected Ranges | Against the US$: | KRW1,090–1,130 |
|---|---|---|
| | Against the yen: | JPY9.800–10.200 (KRW100) |
| | | (KRW9.804–10.204) |

## 1. Review of the Previous Month

The USD/KRW pair jostled in a range between KRW1105–1140 in August.

The pair opened the month trading at KRW1114.50. It then hit the KRW1130 range on August 3 on news that the US was planning to raise tariffs on $200 billion worth of Chinese goods from the initially-planned 10%. With the markets then entering into summer dry season, the Korean unit was bought and the pair fell to the KRW1116 mark. However, it then hit a monthly high of KRW1136.70 on August 14 as risk aversion intensified on the crisis in Turkey. Turkey then hinted it might hold talks with the US, though, while Qatar announced it would invest in Turkey. With news also suddenly emerging on August 16 that some top Chinese officials would be visiting the US for trade talks, the won was gradually bought back. The US/China talks seemed to produce no newsworthy factors overall, but on August 24 the Chinese authorities said the negotiations had been constructive and the two sides would continue working toward a mutual understanding. The RMB was subsequently bought and the Korean won also followed suit.

The People's Bank of China (PBC) then announced it would reintroduce a counter-cyclical factor in the RMB's reference rate fixing mechanism. This was probably aimed at curbing RMB depreciation. The reference rate was set at a slightly higher level on August 27, with the won also moving firmly as a result. The pair hit a monthly low of KRW1106.90 on August 28 to close at KRW1112.90.

Incidentally, FRB chair Jerome Powell's speech at the Jackson Hole symposium on August 24 was adjudged to be comparatively dovish, but it contained nothing new overall and it seems it was ignored by the markets as a factor.

The final point to touch on is the closely-watched meeting of the Bank of Korea's Monetary Policy Committee (MPC). In the run up to the meeting, the markets found it hard to reach a consensus on what would happen. As broadly expected, though, the MPC left policy rates unchanged (with only one person expressing opposition to such a move). The BOK governor's subsequent press conference contained a number of comparatively dovish replies in response to questions about trade frictions and so on. However, he did hint at a rate hike within the year or at the start of 2019, so it was a difficult to interpret what the press conference actually signified.

## 2. Outlook for This Month:

In September, the USD/KRW pair will probably jostle up and down in a comparatively wide range.

US/China trade frictions will remain a key factor. News emerged at the end of last month that the US would introduce punitive tariffs on $200 billion worth on Chinese goods in the first week of September too (directly after the deadline for public comments ends on September 6). For a time, the movements of the currency pair will be determined by whether or not these tariffs are implemented. If it seems this scenario will be avoided, the Korean won will probably rise at a gentle pace, though it will probably plummet for a time if it seems the tariffs will indeed be implemented.

Under these circumstances, the basic stance of the Trump administration seems to be one of negotiating while trying to wring concessions from China. It seems likely the issue will cool off once the negotiations produce some kind of result. With the US also holding midterm elections in November, President Trump has criticized FRB monetary policy for promoting dollar bullishness. However, if the US does slap further tariffs on $200 billion worth of Chinese goods, this will probably push the dollar higher and the RMB lower, so there are doubts about hard the US will push when it comes to the tariffs. It seems likely the US will throw some bargaining chips on the table to reach a deal with China. In the meantime, the markets will probably jostle up and down on news headlines, with the USD/KRW pair moving within a comparatively wide range. The PBC has introduced a counter-cyclical factor in the RMB's reference rate fixing mechanism, so this mechanism will probably work to curb excessive RMB or won depreciation.

Furthermore, even if the US does invoke the tariffs, the impact on the pair might only last for a few days, depending on China's response. This is because there is nothing for China to gain by stirring up trouble with the US, while President Trump will also want to avoid any dollar appreciation, as mentioned above, so the two sides will probably propose fresh talks or make some other moves aimed at defusing the situation.

As for BOK monetary policy, a rate hike could still happen. On the technical front, the won will probably be bought at the KRW1130 level, provided risk aversion does not flare up excessively.

Nonetheless, there are still several concerning factors, such as the possibility of a fully-fledged trade war between the US and China. Some recent reports have also hinted that the North Korean situation could deteriorate. If any of these scenarios comes to pass, the won will inevitably suffer a sharp, wide-ranging fall. On the whole, the pair will probably jostle up and down in a comparatively wide range while keeping an eye on US/China trends, though market participants should be on guard against a sharp slide in the won's value.

Yuji Miura, Taipei Treasury Office

# New Taiwan Dollar – September 2018

| Expected Ranges | Against the US$: | NT$30.50–31.00 |
|---|---|---|
| | Against the yen: | JPY3.55–3.70 |

## 1. Review of the Previous Month

The USD/TWD pair strengthened in August.

After opening the month at TWD30.619, the pair then moved in a narrow range around TWD30.6 as investors slipped into wait-and-see mode in advance of the FOMC meeting during overseas trading time. As expected, the FOMC kept the target range for the federal funds rate at 1.75–2.00%. The statement released after the meeting contained no major surprises, but news emerged around this time that the Trump administration would be hiking the tariffs imposed on Chinese imports. As concerns about a US/China trade war intensified, US stocks dipped. Stocks also fell sharply in Taiwanese markets on August 2, with the currency pair rising as more overseas funds flowed out of Taiwan. The pair hit the TWD30.7 mark on August 3. However, the RMB then strengthened against the greenback after the People's Bank of China (PBC) introduced a measure to restrain RMB depreciation. The USD/TWD pair also began sliding to hit a monthly low of TWD30.560 on August 8.

It continued to trade in a range around TWD30.6 thereafter, but risk aversion then intensified after the Turkish lira fell sharply on August 10, so the greenback was bought and the USD/TWD pair rose to the TWD30.8 range on August 13 for the first time since March 2017.

As excessive risk aversion eased off in the latter half of the month, the Turkish lira stopped sliding, but concerns about a Chinese economic slowdown then increased on the release of some bearish economic indicators, so Chinese stocks and the RMB fell. The Taiwan unit also weakened, with the currency pair rising to TWD30.875 toward August 16.

However, a US newspaper then reported that the Chinese vice-minister of commerce Wang Shouwen would visit the US to hold talks with David Malpass, the US undersecretary of the treasury for international affairs. The mood in the stock markets changed as hopes grew for progress in the US/China trade talks. With overseas funds also flooding into Taiwan, the Taiwan dollar faced appreciatory pressure, so the USD/TWD pair moved with a heavy topside.

## 2. Outlook for This Month:

The USD/TWD pair is expected to move with a heavy topside in September.

A glance at the indicators released in August shows July's export amount rising for the fifth straight month to hit +4.7% y-o-y (the data temporarily dipped into negative territories in February on the impact of the Spring Festival holidays, but when this month is removed from the equation, growth has been positive for 21 months in a row). There are concerns of a Chinese economic slowdown on the

intensified trade frictions between the US and China, but exports to China still grew by an impressive +9.9% y-o-y. Exports of electronic parts (a key Taiwanese export item) moved firmly at +8.8% y-o-y, with the data confirming that exports remain bullish. However, the import amount also grew sharply on an increase in crude oil imports (+46.8% y-o-y) and so on, so Taiwan's trade surplus fell sharply from $5.21 billion to $2.24 billion. July's CPI figure hit +1.75% y-o-y. This was due in pair to a rise in tourism costs as Taiwan entered into summer holiday mode. The core CPI data (excluding volatile fresh food prices) hit +1.50 y-o-y, up slightly on June's figure of +1.41% y-o-y.

Investors will continue to watch the RMB's movements in September. Attention will also focus on the results of the Bank of Taiwan's Monetary Policy Committee (MPC) meeting.

The Taiwan unit's correlation with its Chinese counterpart has risen sharply since the RMB started falling at a faster pace from June. As with last month, the Taiwan dollar will remain susceptible to the movements of the RMB in September, so market participants will need to keep an eye on headlines related to US/China trade policy (where there are signs of progress) and PBC policy trends.

The Bank of Taiwan's MPC will also be holding its quarterly meeting in September. According to the minutes from the last meeting in June, there will be no need to adjust policy rates as long as the economic situation remains unchanged. There have been no significant shifts in the economic indicators and business results released after the last meeting, so a rate hike looks unlikely this month and the discount rate will probably be kept at 1.375%.

Ken Cheung, Hong Kong Treasury Department

# Hong Kong Dollar – September 2018

| **Expected Ranges** | **Against the US$:** | **HK$ 7.8400–7.8500** |
|---|---|---|
| | **Against the yen:** | **JPY 13.75–14.30** |

## 1. Review of the Previous Month

**Hong Kong dollar spot exchange market in August**

In August, the Hong Kong dollar depreciated against the U.S. dollar to HKD 7.85—the upper end of the fluctuation band in the U.S. dollar peg system. As a result, the Hong Kong Monetary Authority (HKMA) carried out Hong Kong dollar-buying intervention for the first time since May. While Hong Kong stock prices were falling, capital outflow from Hong Kong started to become visible again. In the second quarter, the GDP growth rate of Hong Kong recorded a slowdown from the annual rate of 4.6% observed in the previous year to 3.5% (the estimate was 3.9%). On a quarterly basis, the growth rate turned out to be 0.2%—the lowest rate since the first quarter in 2016. In addition to the risks caused by trade frictions between the U.S. and China, the weakening Hong Kong economy has also accelerated the depreciation of asset prices while strengthening pressure for capital outflow. Furthermore, the capital outflow (via the Shanghai-Hong Kong *Stock Connect* system) that started from the beginning of the year accelerated from the CNY 679 billion observed at the end of July to CNY 800 billion. The further depreciation of the Chinese yuan and the depreciation of Chinese A-Shares happened at the same time, resulting in the acceleration of capital outflow to the Chinese onshore market. While the U.S. dollar peg system is being maintained, there were opportunities for carry trades as a result of the widening interest rate differentials between the Hong Kong dollar and the U.S. dollar caused by the interest rate hike by the Federal Reserve Board (FRB), which kept the Hong Kong dollar from appreciating. After the market intervention by the HKMA, the one-year Hong Kong dollar forward point rose sharply from –535 points, the lowest in three months, to –350 points.

**Hong Kong dollar interest rate market in August**

As the Hong Kong dollar continued to depreciate to HKD 7.85—the upper end of the fluctuation range—the HKMA carried out market interventions. In order to protect the Hong Kong dollar, the HKMA started to reduce Hong Kong dollar liquidity. The aggregate balance of the HKMA, which is the index for the liquidity level of the Hong Kong dollar, fell below HKD 100 billion for the first time in 10 years. After the market intervention by the HKMA, the one-month HKD HIBOR rallied sharply from 1.29%—the lowest level in two months—to 1.4%. Then, the yield difference between the one-month

HKD HIBOR and the one-month USD LIBOR narrowed in the middle of August from –70 basis points to –60 basis points. However, it was –40 basis points at the end of July. On the other hand, the three-month HKD HIBOR remained within a narrow range between 2.0–2.1%, which kept the interest rate differential between the U.S. and Hong Kong unchanged at around –40 basis points. Furthermore, for medium-term periods as well, the three-year and five-year Hong Kong dollar interest rates did not change at 2.6% and 2.7%, respectively. However, in August, most banks in Hong Kong raised interest rates for real estate following the hike of the Hong Kong dollar deposit interest rates.

**Hong Kong stock market in August**

The benchmark Hang Seng Index fell to 26,871—the lowest level in a year—as the Hong Kong stock market suffered from downward pressure caused by the trade frictions between the U.S. and China, as well as due to the depreciation of the Chinese yuan. However, market sentiment improved thereafter, as the sell-off of technology stocks had ended while the trend in the Chinese stock market and the Chinese yuan exchange market was reversed. As a result, the Hang Seng Index rallied as well.

## 2. Outlook for This Month:

**Hong Kong dollar spot exchange market in September**

In September, the U.S. dollar/Hong Kong dollar exchange rate is expected to fluctuate between HKD 7.84 and HKD 7.85. In September, the FRB is expected to raise the interest rate by 25 basis points, which makes it likely for the U.S. dollar/Hong Kong dollar exchange rate to approach the HKD 7.85 level several times. In the U.S. dollar peg system, growing interest rate differentials between the U.S. and Hong Kong would continue putting downward pressure on the Hong Kong dollar until the Hong Kong dollar interest rates catch up with the U.S. dollar interest rates. While concerns over the trade frictions between the U.S. and China and the weakness in the Hong Kong stock market persist, growing uncertainty regarding the Hong Kong economy is a factor that could accelerate capital outflow from Hong Kong and cause the depreciation of the Hong Kong dollar. The one-year Hong Kong dollar forward point is likely to rise as a result of the liquidity absorption by the HKMA.

**Hong Kong dollar interest rate market in September**

As the HKMA resumed its foreign exchange market interventions by absorbing Hong Kong dollar liquidity, the Hong Kong dollar interest rates are expected to rise. As short-term interest rates are sensitive to the liquidity level, the Hong Kong dollar is likely to start flattening gradually. Furthermore, as it has become unlikely for the Chinese yuan to continue depreciating against the U.S. dollar to reach

the CNY 7 level, a large amount of capital outflow from the Hong Kong dollar market is unlikely within a short term. On the other hand, as the HKMA has been absorbing a large volume of liquidity this year, banks in Hong Kong are likely to raise their prime rates—the base interest rates—for the first time in 2006 following the interest rate hike by the FRB. In other words, this suggests that interest rates will start appreciating in Hong Kong this year, exposing Hong Kong assets to downward risks.

Kei Yano, Treasury Division, MHBK (China)

# Chinese Yuan – September 2018

| Expected Ranges | Against the US$: | CNY 6.4500–6.9500 |
| --- | --- | --- |
| | Against the yen: | JPY 15.54–17.52 |
| | Against 100 yen: | CNY 5.7100–6.4400 |

## 1. Review of the Previous Month

**Foreign exchange market**

In August, the Chinese yuan continued depreciating against the U.S. dollar due to concerns over the trade frictions between the U.S. and China, as was the case in the previous month. However, in the second half of the month, the Chinese yuan started to appreciate again as a result of the measures taken by the Chinese monetary authorities to control the depreciation of the Chinese yuan.

In the first half of the month, the media reported that the U.S. was considering raising customs duty worth USD 200 billion against China (from 15% to 25%), in reaction to which the Chinese yuan depreciated significantly, also causing stock prices to depreciate. Furthermore, at the Federal Open Market Committee (FOMC) meeting in the U.S., a decision was made to gradually raise the interest rate, which led the Chinese yuan to depreciate significantly against the U.S. dollar, leading the U.S. dollar/Chinese yuan exchange rate to exceed CNY 6.89 from around the CNY 6.80 observed at the beginning of the month.

On August 3, the People's Bank of China (PBOC) announced that it would resume the foreign currency risk reserve system, which led the trend to reverse, and the Chinese yuan started to rally. Thereafter, the Shanghai Stock Exchange Composite Index reached its highest level in two years, thanks to expectations for new policy measures, which accelerated Chinese yuan-buying. Furthermore, in order to stabilize the Chinese yuan market, the PBOC instructed private banks to avoid "crowd behavior" in which Chinese yuan-selling leads to further Chinese yuan-selling. As a consequence, the U.S. dollar/Chinese yuan exchange rate fell below the CNY 6.80 level.

On August 10, the Turkish lira depreciated sharply after the announcement made by the U.S. to introduce customs duties against Turkey, as a form of sanctions. The media reported that the European Central Bank (ECB) was concerned about Turkey's large debts to financial institutions in the euro zone, which also encouraged market participants to sell the euro. As a result, the Chinese yuan depreciated as well. The Chinese yuan weakened further thereafter due to the fact that a large Chinese IT company

released its financial results, showing a weak balance sheet. Thus, the U.S. dollar/Chinese yuan exchange rate temporarily exceeded CNY 6.93.

Thereafter, some market participants bought back the Chinese yuan, as the media reported that trade negotiations between the U.S. and China had resumed. On August 20, U.S. President Donald Trump made a remark to give warning regarding interest rate hikes in the U.S. while criticizing China and Europe for manipulating the exchange market. In reaction to this, the U.S. dollar weakened and the U.S. dollar/Chinese yuan exchange rate fell to approach CNY 6.84 again.

There was no progress in the trade negotiations between the U.S. and China thereafter, which led the U.S. dollar/Chinese yuan exchange rate to approach CNY 6.89 again. However, on August 24, the PBOC announced its decision to re-introduce counter-cyclical factors, which led the Chinese yuan to appreciate against the U.S. dollar to the lower-CNY 6.8 level.

**Interest rate market**

In the first half of the month, interest rates depreciated. As market participants expect the interest rates to be higher in the times ahead with measures of monetary easing, the underlying interest rate overnight SHIBOR temporarily reached 1.422%, falling significantly below the deposit reserve rate. For other terms as well, interest rates remained low. However, once the overnight rate rallied, interest rates for other terms started rising as well. Toward the end of the month, liquidity was provided through open-market operations and new medium-term lending facilities (MLFs), which led the overnight interest rate to start falling while the appreciation of interest rates for other terms also slowed down.

## 2. Outlook for This Month:

**Foreign exchange market**

In September, the depreciation of the Chinese yuan is forecast to slow down as a result of a series of measures to control the depreciation of the Chinese yuan.

Since August, the Chinese monetary authorities have carried out a measure to control the depreciation of the Chinese yuan three times. First of all, on August 3, the foreign currency risk reserve system was re-introduced. On August 16, banks in the free trade zone in Shanghai were advised to control capital supply in the Chinese yuan toward foreign financial institutions. Furthermore, counter-cyclical factors were re-introduced on August 24. With this series of measures to control the depreciation of the Chinese yuan, the U.S. dollar/Chinese yuan exchange rate, which had exceeded CNY 6.93 at the peak time,

returned to the lower-CNY 6.8 level. Thus, now that trade negotiations between the U.S. and China have resumed, the sharp depreciation of the Chinese yuan against the U.S. dollar is unlikely, as the Chinese monetary authorities would not let the U.S. dollar/Chinese yuan exchange rate exceed CNY 7.0.

On the other hand, it is also unlikely for the Chinese yuan to start appreciating against the U.S. dollar. The Chinese yuan would only start appreciating if there is practical progress in trade negotiations between the U.S. and China, which saw no progress as of August 22 and 23, or if the recently weakening fundamentals start improving. The monetary policy is clearly driven toward easing, with expectations for further cuts of the deposit reserve ratio, which would put downward pressure on the Chinese yuan. As the U.S. has indicated its plan to gradually raise the interest rate, the Chinese yuan is forecast to continue depreciating, albeit slowly.

Risks in the times ahead include Brexit negotiations and persisting political problems in Europe as exemplified by the issue of Italy opposing the European Commission regarding the acceptance of refugees. Therefore, if market participants continue selling the euro and buying the U.S. dollar rapidly, this may also encourage market participants to sell the Chinese yuan, regarding which we need to be cautious.

**Interest rate market**

In September, interest rates are forecast to remain low, with measures of monetary easing. Since the beginning of July, the PBOC has been supplying a large amount of one-year funds to the short-term monetary market through MLFs. Even though interest rates appreciated temporarily in August, the liquidity level has been kept high. It is possible for the Chinese monetary authorities to continue taking measures of monetary easing, such as a deposit requirement ratio cut, in order to support the economy and maintain the liquidity level. The downward pressure on interest rates is therefore expected to persist.

On the other hand, if the actual economy grows thanks to the fiscal policy, and thus if this leads to the appreciation of stock prices, bond prices may depreciate, raising long- and medium-term interest rates. While the trade frictions between the U.S. and China persist, market participants should remain cautious about the attitude of the Chinese monetary authorities, along with the related impact on the actual economy.

Shinya Maegawa, Asia & Oceania Treasury Department

# Singapore Dollar – September 2018

| Expected Ranges | Against the US$: | SG$ 1.3550–1.3800 |
|---|---|---|
| | Against the yen: | JPY 79.50–82.50 |

## 1. Review of the Previous Month

In August, the U.S. dollar/Singapore dollar exchange rate fluctuated violently within a wide range between the lower-SGD 1.36 level and the lower-SGD 1.38 level, as a result of the media report on the trade frictions between the U.S. and China, the sharp depreciation of the Turkish lira, and the third remark this year by U.S. President Donald Trump to give warning to interest rate hikes.

In the first week of the month, the media reported that U.S. President Donald Trump was planning to introduce a customs duty of 25% on imports from China worth USD 200 billion, which fueled concerned over the trade frictions between the U.S. and China. Under such circumstances, risk-averse sentiment strengthened in the market and the Singapore dollar weakened against the U.S. dollar from the lower-SGD 1.36 level to the upper-SGD 1.36 level. On August 3, the U.S. dollar remained strong, and market participants sold the Singapore dollar as a result of which the U.S. dollar/Singapore dollar exchange rate reached the lower-SGD 1.37 level.

In the second week of the month, the June manufacturing order index of Germany was released on August 6, recording a result that was significantly weaker than the market estimate. As a result, the euro weakened and the U.S. dollar strengthened. As a result, the Singapore dollar remained robust against the U.S. dollar at the upper-SGD 1.36 level. On August 7, the Chinese yuan exchange market was stable, leading the U.S. dollar to depreciate against other major currencies. While market participants were selling the U.S. dollar and buying the Singapore dollar, the U.S. dollar/Singapore dollar exchange rate fell from the upper-SGD 1.36 level to the lower-SGD 1.36 level. On August 9 and 10, market participants reacted negatively to the sanctions against Turkey and Russia by the U.S. under the Trump administration. Under such circumstances, the Turkish lira and the Russian ruble reached their low, while the Singapore dollar was sold to the lower-SGD 1.37 level.

In the third week of the month, the Turkish lira depreciated even further on August 13, which affected other currencies of emerging countries. Following this trend, market participants also sold the Singapore dollar to the upper-SGD 1.37 level to the U.S. dollar. Thereafter, the Banking Regulation and Supervision Agency of Turkey announced its decision to control swap transactions to 50% or less of bank assets, slowing down the sharp depreciation of the Turkish lira. Under such circumstances, other

currencies of emerging countries all depreciated. As a result, market participants sold the Singapore dollar, and the U.S. dollar/Singapore dollar exchange rate once reached the lower-SGD 1.38 level. On August 16, the media reported that the trade negotiations between the U.S. and China would be resumed in late August, in reaction to which market participants bought back the overall Asian currencies. Market participants thus also bought the Singapore dollar, and the U.S. dollar/Singapore dollar exchange rate reached the mid-1.37 level. Then, on August 17, the media reported that a Turkish court had rejected an appeal to release a U.S. pastor, encouraging market participants to sell the U.S. dollar.

In the fourth week of the month, the media reported on August 20 that trade negotiations between the U.S. and China would resume before the end of the month, in reaction to which the majority of Asian currencies appreciated. Furthermore, it was reported that U.S. President Donald Trump was not satisfied with the interest rate hikes carried out by the FRB, which encouraged market participants to sell the U.S. dollar more actively. As a consequence, the Singapore dollar was bought and the U.S. dollar/Singapore dollar exchange rate reached the mid-SGD 1.36 level. On August 21, market participants continued selling the U.S. dollar. On August 22, the market was closed in Singapore. Then, on August 23, the U.S. dollar strengthened, as FRB Chair Jerome Powell was expected to maintain his hawkish attitude at his speech scheduled at the *Jackson Hole* Economic Symposium. As a result, the U.S. dollar/Singapore dollar exchange rate reached the mid-SGD 1.37 level.

In the fifth week of the month, a former lawyer of U.S. President Donald Trump accepted plea-bargaining on August 27, while the President made a decision to cancel the visit of the Secretary of State Pompeo to North Korea. In reaction to such news, the U.S. dollar/Singapore dollar exchange rate remained at the mid-SGD 1.36 level.

## 2. Outlook for This Month:

In September, the U.S. dollar is likely to remain strong, and therefore the Singapore dollar is forecast to weaken. The Singapore dollar market is expected to be affected by the risk sentiment surrounding the trade frictions between the U.S. and China, as well as the currency crisis in Turkey and the risks in emerging countries.

In the middle of the previous month, the second-quarter GDP of Singapore was released and the result turned out to be +3.9%, falling below the market estimate, which was +4.1%. However, the growth rate remained high. The June retail sales and the July non-petroleum oil exports of Singapore both exceeded the market estimate, demonstrating the strength of the Singapore economy.

Furthermore, at the end of the previous month, U.S. President Donald Trump made a comment to give

warning to interest rate hikes for the third time this year, which impacted the exchange market by encouraging market participants to sell the U.S. dollar. Thereafter, FRB Chair Jerome Powell made a speech at the *Jackson Hole* Economic Symposium without any change in attitude from previous speeches. However, given that the U.S. dollar was sold against other currencies, it seems that the market has already reflected the interest rate hike in September to a great degree. Since the beginning of the second quarter, the economic expansion has been accelerating in the U.S. and prices are appreciating, which makes it unlikely for the FRB to slow down the pace of interest rate hikes.

With regard to the trade frictions between the U.S. and China, during the vice-ministerial level trade negotiations between the U.S. and China held at the end of August, there was no settlement seen that could be said to mitigate the situation. As the meeting was only a vice-ministerial level meeting, the sense of distance between the two countries is still significant and the possibility of an agreement is unlikely, and thus the trade frictions between the U.S. and China may last for a longer term. For this reason, market participants are expected to continue buying the U.S. dollar for a while, weakening the currencies of emerging countries, including the Singapore dollar.

Hiroyuki Yamazaki, Bangkok Treasury Office

# Thai Baht – September 2018

| Expected Ranges | Against the US$: | THB 32.20–33.35 |
|---|---|---|
| | Against the yen: | JPY 3.33–3.45 |

## 1. Review of the Previous Month

In August, the U.S. dollar/Thai baht exchange market opened trading at around THB 33.20. The July Consumer Price Index of Thailand turned out to be 1.46%, almost at the same level as the estimated level, at 1.49%. As the Federal Open Market Committee (FOMC) meeting concluded without any surprise, the market remained static. On the following day, the Thai baht depreciated following the depreciation of the Chinese yuan, in reaction to which the U.S. dollar/Thai baht exchange rate rose to approach THB 33.30. On August 3, the People's Bank of China (PBOC) announced a measure to control the depreciation of the Chinese yuan, leading the U.S. dollar/Chinese yuan exchange rate to fall sharply. Following this trend, the U.S. dollar/Thai baht exchange rate also depreciated rapidly to the upper-THB 33.10 level. The July employment statistics of the U.S. were also announced, but there was no particular surprise, confirming the expectation of two interest rate hikes by the FOMC. From August 6, the following day, to August 8, there was no particular movement in the market. On August 8, the central bank of Thailand held its monetary policy committee meeting, and it was announced that the policy interest rate was going to be maintained at the existing level of 1.5%. This announcement impacted the exchange market only to a minimal degree. On August 9, the following day, market participants bought the Chinese yuan, following which the U.S. dollar/Thai baht exchange rate also fell to the THB 33.10 level. Thereafter, sanctions against Turkey and Russia by U.S. President Donald Trump caused a negative reaction in the market and the U.S. dollar/Thai baht exchange rate rallied to the THB 33.20 level. On August 10, the following day, the Turkish lira continued depreciating, while the euro also depreciated sharply. Furthermore, stock prices weakened worldwide. Under such circumstances, market participants sold the currencies of emerging countries in an accelerated manner, and the U.S. dollar/Thai baht exchange rate once rose to approach THB 33.35.

After the weekend, the market was closed in Thailand on August 13, and while pressure to sell the Thai baht was strengthening in the offshore market, the U.S. dollar/Thai baht exchange rate once rose to approach THB 33.40. On the following day, the big concerns in the market over Turkey started to calm down. As a result, the U.S. dollar/Thai baht exchange rate fell to approach THB 33.25. On August 15, as the economic indices of China turned out to be weak on the previous day and while downward pressure was growing on the euro due to fiscal issues in Italy, market participants bought the U.S. dollar, leading the U.S. dollar/Thai baht exchange rate to rise to approach THB 33.35. Thereafter, the Turkish monetary

authorities announced a decision to cut the upper limit of bank swap transactions from 50% to 25%, leading the Turkish lira to appreciate sharply. Following this trend, the U.S. dollar/Thai baht exchange rate also fell to approach THB 33.30. Then, on August 16, the offshore Chinese yuan interest rates appreciated sharply, increasing rapidly the cost of transactions that expect the depreciation of the Chinese yuan. As a result, market participants bought the Chinese yuan, following which the U.S. dollar/Thai baht exchange rate also fell.

On August 20 after the weekend, the second-quarter GDP of Thailand turned out to be +4.6% year-on-year, exceeding the estimated level. As a result, the U.S. dollar/Thai baht exchange rate fell below the recent low recorded on August 1. While the depreciation of the U.S. dollar was accelerating, the exchange rate continued to fall further, falling below the THB 33.00 mark, and trading closed at around THB 32.95. On August 21, market participants continued selling the U.S. dollar, leading the overall currencies of emerging countries to strengthen. As a consequence, the U.S. dollar/Thai baht exchange rate once fell to approach THB 32.65. On August 22, the following day, the exchange rate rallied after hitting bottom. Furthermore, on August 23, the next day, there was no particular progress in trade negotiations between the U.S. and China, leading the U.S. dollar/Thai baht exchange rate to rise and approach THB 32.90. Then, on August 24, China introduced counter-cyclical factors in order to control the depreciation of the Chinese yuan, which led to the appreciation of the Chinese yuan. Following this trend, the U.S. dollar/Thai baht exchange rate also fell to approach THB 32.60. Toward the end of the month, the governor of the central bank of Thailand, Veerathai Santiprabhob, made a dovish comment emphasizing that there is no urgent pressure to raise the interest rate, weakening the Thai baht, and the U.S. dollar/Thai baht exchange rate returned to approach THB 32.80.

## 2. Outlook for This Month:

In September, the U.S. dollar/Thai baht exchange rate is forecast to remain low. In the second half of April, the U.S. dollar/Thai baht exchange rate started rising. Along with the appreciation of the U.S. dollar, the exchange rate rose to approach the mid-THB 33 level, after which the appreciation slowed down before the exchange rate eventually started to fall. This was due to the fact that the second-quarter GDP of Thailand turned out to be stronger than expected, after which expectations grew over an interest rate hike by the central bank of Thailand, resulting in the appreciation of the Thai baht. However, toward the end of the month, the governor of the central bank of Thailand, Veerathai Santiprabhob, made a remark that there was no urgent need to raise the interest rate, which swept away any existing expectations for an interest rate hike. As a result, the U.S. dollar/Thai baht exchange rate rose again toward THB 32.80. Under such circumstances, the Thai baht is still expected to remain strong in the times ahead. This is based on the fact that the Thai economy remains strong and the current account balance has remained positive despite figures that are weaker than expected. Thus, it can be said that the

fundamentals continue to suggest the appreciation of the Thai baht. On the other hand, it had been expected that the U.S. dollar would be sold due to risk-averse sentiment in the market caused by the trade frictions between the U.S. and China. However, until now, market participants have rather been buying the U.S. dollar. This may not be a question of risk-averse sentiment or risk-taking sentiment but the fact that the U.S. dollar was sold throughout the year in 2017, which simply led to buybacks. If this is the case, from the point of view of the U.S. dollar/Thai baht exchange market, the exchange rate has already returned halfway at the mid-THB 33 level after falling from THB 36 to THB 31. Thus, the depreciation of the Thai baht is likely to slow down for the moment. On the other hand, thanks to the strong economy, interest rate hikes are likely in the future. It is thus possible for the Thai baht to slowly appreciate against the U.S. dollar toward the THB 32 level.

Shinichi Sekigami, Mizuho Bank (Malaysia) Berhad

# Malaysian Ringgit – September 2018

| Expected Ranges | Against the US$: | MYR 3.9500–4.1500 |
| --- | --- | --- |
| | Against the yen: | JPY 26.60–28.00 |
| | Against 100 yen: | MYR 3.5700–3.7600 |

## 1. Review of the Previous Month

In August, the Malaysian ringgit depreciated against the U.S. dollar from the MYR 4.06 level to the MYR 4.11 level, with the impact of the trade frictions between the U.S. and China, along with the depreciation of the Chinese yuan.

At the beginning of the month, the U.S. dollar/Malaysian ringgit exchange market opened at the MYR 4.06 level. On August 1, the Federal Open Market Committee (FOMC) in the U.S. made a change in its statement regarding economic growth in the U.S. (from "solid" to "strong"), while market participants remained cautious about the stagnant situation involving the customs duties between the U.S. and China. As a result, the Malaysian ringgit depreciated against the U.S. dollar to MYR 4.0820 on Friday, August 3. On the same day, the July number of non-agricultural employees of the U.S. was announced, which recorded a positive growth of 157,000. Even though this result was weaker than expected (+190,000), the result of June was revised upward. On August 7, the Malaysian ringgit renewed its low against the U.S. dollar at MYR 4.0870, as China announced its decision to introduce an additional customs duty on imports from the U.S. worth USD 60 billion, such as natural gas and semiconductors. On the other hand, the offshore Chinese yuan renewed its low, and the People's Bank of China (PBOC) raised the margin requirement rate from 0% to 20% for domestic banks selling the Chinese yuan in exchange contracts, in order to control speculative actions. The PBOC thus sent the message that it does not welcome the sharp depreciation of the Chinese yuan, which led the offshore Chinese yuan to appreciate. As a consequence, the U.S. dollar/Malaysian ringgit exchange rate returned to MYR 4.0670 on August 9.

However, the U.S. re-imposed sanctions against Iran, Turkey, and Russia, which fueled concerns about geopolitical risks once again. In particular, the Turkish lira sharply depreciated on August 10 because of Turkey's decision to introduce an additional customs duty on iron and aluminum imported from the U.S., which impacted not only emerging countries but also the European continent via the concerns of European banks, which are largely exposed to the Turkish market. On the other hand, the July core CPI of the U.S. recorded its highest figure in the past 10 years, which led market participants to expect the

Federal Reserve Board (FRB) to accelerate the pace of its interest rate hikes. Under such circumstances, the market sentiment continued to lead the Malaysian ringgit to depreciate. As a result, the U.S. dollar/Malaysian ringgit exchange rate exceeded the MYR 4.10 mark on August 15.

On August 17, the second-quarter GDP of Malaysia was released, and the result turned out to be +4.5% year-on-year, which is significantly weaker than the estimate (+5.2% year-on-year) because of the weakness of the agricultural and mining industries, reaching the lowest level since the fourth quarter in 2016. However, there was no significant impact on the Malaysian ringgit exchange market. Also, once the media reported on the visit of the undersecretary of the Ministry of Commerce of China to the U.S., tension regarding trade issues was mitigated. In reaction to this, market participants bought back the Malaysian ringgit as well. While the media reported on the criticism by U.S. President Donald Trump regarding the induced depreciation of the Chinese and European currencies, the U.S. dollar depreciated, leading the Malaysian ringgit to strengthen. As a result, the U.S. dollar/Malaysian ringgit exchange rate returned to MYR 4.0910 on August 21. However, on August 22, the minutes of the FOMC meeting turned out to be hawkish, and on August 23, the U.S. announced the second round of additional customs duties against China worth USD 16 billion. As a consequence, the Chinese yuan depreciated significantly. Furthermore, on August 24, the July core CPI of Malaysia was announced and the result turned out to be –0.2% year-on-year—indicating disinflation for the first time. Following this trend, the Malaysian ringgit also renewed its lowest rate for this year against the U.S. dollar at MYR 4.1110, on the same day.

## 2. Outlook for This Month:

In September, the U.S. dollar/Malaysian ringgit exchange rate is expected to fluctuate within the range between MYR 3.95 and MYR 4.15. The weakening factors for the Malaysian ringgit include the persisting trade war between the U.S. and China as well as the downward risks on the Chinese yuan, as has been the case so far. However, the assets of foreign investors are starting to come back to Malaysia, and expectations are growing for policy measures under the new government.

In August, the Malaysian ringgit renewed its lowest rate against the U.S. dollar, as it also did in the previous month. This is considered to be the result of trade frictions and the resulting depreciation of the Chinese yuan, while the slowdown in exports also contributed to this as a domestic factor. However, assets of foreign investors worth MYR 4 billion flew into the Malaysian bond market in July, while assets of foreign investors were flowing out from April to June—the period surrounding the national election. On August 22, the new government under Prime Minister Mahathir Mohamad celebrated its 100$^{th}$-day anniversary after its establishment on May 14. Prior to that, the Prime Minister visited China and suggested a revision of the mega projects that Chinese companies are being entrusted with, such as

the discontinuation of the East Coast Rail Link project. At the same time, the media also announced that the government advisory body, a member of which is former governor of the central bank Tan Sri Zeti Akhtar Aziz, was preparing a report for this 100th day, which would be the center of attention in terms of the primary balance. Furthermore, in September, Malaysian government bonds will see their maturity dates. A ratings company, Fitch, maintained the Malaysian sovereign rating (A–) on August 14, while announcing the outlook as "stable." However, as September will be the last month of the third quarter, market participants should be carefully observing rebalancing flows by foreign investors.

It should also be mentioned that the central bank of Malaysia announced its decision to partially change the foreign exchange regulations on August 17 in order to enhance business efficiency. Major changes include (1) reduction of the administrative duty regarding the forced conversion of export bills into the Malaysian ringgit, (2) introduction of the central bank approval system for foreign currency contracts for more than six months for the purpose of the repayment of foreign currency borrowings or imported debt payment, and (3) removal of the ban for non-residents on interest rate derivatives transactions in the Malaysian ringgit through designated overseas bases. However, these did not impact the Malaysian ringgit market as had been expected, perhaps because they only regarded the external environment, such as the tensions related to trade issues and the depreciation of the Chinese yuan. However, these changes generally consist of measures of monetary easing, showing the attitude of the new governor to prioritize the domestic industry, including foreign companies. It is considered that the sales and service tax (SST), the re-introduction of which was approved at Parliament, would theoretically impose smaller burden on final consumers compared to the previous GST. Yet, market participants should remain cautious about the impact of this on consumer sentiment at the time of introduction.

Ryosuke Kawai, Asia & Oceania Treasury Department

# Indonesian Rupiah – September 2018

| **Expected Ranges** | **Against the US$:** | **IDR 14,300–14,900** |
|---|---|---|
| | **Against 100 rupiah:** | **JPY 0.74–0.78** |
| | **Against the yen:** | **IDR 127.50–135.00** |

## 1. Review of the Previous Month

In August, the U.S. dollar/Indonesian rupiah exchange rate fluctuated within the range between IDR 14,390 and IDR 14,660. The exchange rate remained generally high, and it once reached IDR 14,660 for the first time since October 2015.

At the beginning of the month, the U.S. dollar/Indonesian rupiah exchange market opened at around IDR 14,425. On August 1, the July Consumer Price Index of Indonesia was announced, and the result turned out to be within the range of the market estimate. Thus, this impacted the exchange market only to a limited degree. On August 6, the second-quarter GDP of Indonesia was announced, and the result turned out to be +5.27% year-on-year, exceeding the market estimate (the estimate was +5.12% year-on-year). In addition, the Chinese yuan appreciated and market participants bought back overall Asian currencies against the U.S. dollar. As a result, the U.S. dollar/Indonesian rupiah exchange rate fell to approach IDR 14,390—the monthly low. In the meantime, the July amount of foreign currency reserves in Indonesia was announced on August 7, recording negative growth for the sixth consecutive month, at USD 119.8 billion (negative growth of USD 1.5 billion from the previous month).

In the middle of the month, the second-quarter current account balance was announced after the closure of the foreign exchange market on August 10. As had been anticipated, the deficit expanded significantly compared to the previous figure (first quarter: –USD 5.7 billion, second quarter: –USD 8 billion). In reaction to this, the U.S. dollar/Indonesian rupiah exchange rate rapidly rose to approach IDR 14,630 on August 13 in the following week, as there were also growing concerns regarding Turkey. Then, on August 15, the July trade balance was announced, recording the largest deficit this year at USD 2 billion, which led the U.S. dollar/Indonesian rupiah exchange rate to rise further.

Thereafter, the U.S. dollar/Indonesian rupiah pair continued trading at around IDR 14,600. However, in the second half of the month, importing companies needed to buy the U.S. dollar, strengthening the upward pressure on the U.S. dollar/Indonesian rupiah exchange rate. As a result, on August 24, the U.S. dollar/Indonesian rupiah exchange rate once reached IDR 14,660 for the first time since October 2015,

after which the exchange rate has been moving at around IDR 14,650 (as of the closing of August 29, 2018).

On August 14 and 15, the central bank of Indonesia held its regular meeting and unexpectedly raised the interest rate by +0.25% to 5.5%, for the first time in 27 months since May 2016. However, the impact of this on the market was limited.

## 2. Outlook for This Month:

In September, the Indonesian rupiah is forecast to remain weak due to the pressure to sell the Indonesian rupiah and buy the U.S. dollar, based on actual demand (in terms of the current balance) as well as on transactions related to quarterly hedge restrictions.

Since the end of April, the outflow of funds of foreign investors led to the sharp appreciation of the U.S. dollar/Indonesian rupiah exchange rate. However, the capital outflow is currently slowing down, partially thanks to the interest rate hike carried out by the central bank of Indonesia (the holding balance of Indonesian government bonds by foreign investors was up to IDR 839 trillion as of the end of July, while it is IDR 847 trillion as of August 28).

Yet, the U.S. dollar/Indonesian rupiah exchange rate is expected to remain high, as there is strong pressure to sell the Indonesian rupiah based on actual demand (due to deficits in terms of the currency account balance).

On August 10, the second-quarter current account balance of Indonesia was announced, and as had been expected, the deficit expanded. Furthermore, the July trade balance of Indonesia was announced on August 15, recording the largest deficit this year. Even though high political officials, including President Joko Widodo, made comments regarding the reinforcement of measures to reduce the current account deficit, the level of efficiency that can be achieved remains unclear. The downward pressure on the Indonesian rupiah is therefore forecast to persist in terms of the current account balance.

It should also be mentioned that it is likely for the Indonesian rupiah to be sold in September in order to comply with quarterly hedge regulations. If risk-averse sentiment grows in the market due to situations outside of Indonesia, such as the trade frictions between the U.S. and China, the U.S. dollar/Indonesian rupiah exchange rate may well finally exceed IDR 14,700 for the first time since September 2015.

Yoichi Hinoue, Manila Office, Asia & Oceania Treasury Department

# Philippine Peso – September 2018

| **Expected Ranges** | **Against the US$:** | **PHP 52.80–54.00** |
|---|---|---|
| | **Against the yen:** | **JPY 2.06–2.12** |

## 1. Review of the Previous Month

In august, the U.S. dollar/Philippine peso exchange market opened trading at PHP 53.05.

Market participants continued selling the U.S. dollar since the end of the previous month after the announcement of the second-quarter GDP.

Furthermore, at the beginning of the month, market participants mainly adjusted positions before important events (i.e., the Federal Open Market Committee [FOMC] meeting on August 1, the release of the July employment statistics of the U.S. on August 3, the announcement of the July Consumer Price Index of the Philippines on August 7, the announcement of the second-quarter GDP growth rate of the Philippines on August 9, and the monetary policy committee meeting at the central bank of the Philippines [BSP]).

At the FOMC meeting, the outcome held no surprises, and market participants continued buying back the Philippine peso. The July employment statistics of the U.S. showed the number of non-agricultural employees falling below the market estimate. In reaction to this, market participants sold the U.S. dollar in the foreign exchange market. Furthermore, the Chinese yuan appreciated as a result of strengthened foreign exchange restrictions in China. Following this trend, the overall Asian currencies strengthened against the U.S. dollar. The U.S. dollar/Philippine peso exchange rate fell below PHP 53 on August 6, temporarily reaching PHP 52.84—the highest rate for the Philippine peso against the U.S. dollar since June 8 this year.

On August 7, the July Consumer Price Index of the Philippines was announced, and the result turned out to be +5.7% (the previous result was +5.2%, and the market estimate was +5.5%). This made it clear that the interest rate would be raised by 50 basis points (0.5%) at the monetary policy committee meeting of the BSP, held on August 9. It should also be mentioned that the June trade balance of the Philippines was announced on August 8, recording a deficit of USD 3.35 billion—achieving a slight reduction of the deficit from the previous month's result (a deficit of USD 3.69 billion).

The above events were both positive factors for the Philippine peso. However, the position adjustment carried out actively at the beginning of the week (a buyback of the Philippine peso) has slowed down, and the U.S. dollar/Philippine peso exchange rate was pushed to the PHP 53 level by August 9.

In addition, the second-quarter GDP growth rate of the Philippines turned out to be +6.0% year-on-year, recording a slowdown from the result of the first quarter, which was 6.6% year-on-year (revised downward from +6.8%). Thereafter, the BSP raised the overnight loan interest rate—the policy interest rate of the Philippines—by 0.50%, to 4%. However, this had already been reflected in the market, and thus it did not cause any particular action in the market. The U.S. dollar/Philippine peso exchange rate hovered at around the lower-PHP 53 level.

Thereafter, risk-averse sentiment dominated the market with growing geopolitical risks related to Turkey and the U.S. The sharp depreciation of the Turkish lira impacted Asian currencies. As a result, the U.S. dollar/Philippine peso exchange rate approached the PHP 53.55 level—the latest high for the U.S. dollar. On August 15, the U.S. dollar/Philippine peso once reached PHP 53.535. However, the appreciation of the U.S. dollar remained slow, and market participants were highly cautious of market intervention by the BSP when the U.S. dollar/Philippine peso exchange rate was at the PHP 53.50 level.

After the release of the minutes of the FOMC meeting, market participants bought the U.S. dollar. However, this was not enough to move the exchange rate from the level that would fuel caution about market interventions. Once the economic symposium at Jackson Hole was over, the downward pressure on the Philippine peso was slightly weakened. The U.S. dollar/Philippine peso exchange rate thus continues to fluctuate at the lower-PHP 53 level without moving in any direction (as of 10 a.m. on August 28).

## 2. Outlook for This Month:

The second-quarter GDP growth rate of the Philippines was released last month, recording a slowdown mainly due to the fact that expanding imports pushed downed the growth rate. On the other hand, fixed-asset formation has been significantly increasing, such as in investment in infrastructure carried out by the government, while personal consumption has been confirmed to be robust. Therefore, it is generally considered that it is not necessary to worry too much about a slowdown in the growth rate.

However, it is important to continue observing how much inflation will impact personal consumption in the times ahead, keeping in mind the possibility for figures in the third quarter to be negatively affected.

The BSP emphasized that there are persistent upward risks in its price outlook during the press

conference after the monetary policy committee meeting, revising the latest inflation rate outlook upward (from 3.3% to 3.7% for 2018 and from 4.5% to 4.9% for 2019). The BSP expressed its view that a strong monetary policy is essential to control inflation, while seeing almost no negative impact of the interest rate hike on the economy. It can be seen as a hawkish statement (meaning, being assertive about interest rate hikes in the times ahead). As the actual policy interest rate is still negative based on the inflation outlook for 2019, an additional interest rate hike before the end of the year is possible.

In addition to what was discussed above, it should also be mentioned that the June amount of remittances from Overseas Filipino Workers (OFWs) was announced to be USD 2.36 billion on August 15, recording negative growth of –4.5% year-on-year, showing a slowdown from USD 2.47 billion—the figure from the previous month. However, based on the sum with the June trade balance (a trade deficit of USD 3.35 billion), the figure for this month turned out to be a deficit of USD 990 million, cutting the deficit from the USD 1.22 billion recorded in the previous month, which can be a factor to weaken the downward pressure on the Philippine peso.

The U.S. dollar/Philippine peso exchange rate had been kept from rising further above PHP 53.50 through cautious market interventions by the BSP over the past two months. It seems that there are not many market participants that are continuing to buy the U.S. dollar when there is a possibility of market intervention. The BSP is concerned with the possible acceleration of inflation based on the depreciation of the currency. Market participants are thus likely to remain sensitive about actions taken by the Philippine monetary authorities.

Under such circumstances, it is also possible for market participants to buy back the Philippine peso. However, from a medium-term perspective, market participants are expected to buy the U.S. dollar as a safe asset based on the appreciation of the U.S. interest rates and on concerns over the trade frictions between the U.S. and China, all the while selling the Philippine peso with the twin deficits of the Philippines.

It also seems that the U.S. dollar/Philippine peso exchange rate will not exceed the PHP 53.50 level, with a lack of influential factors. If risk-averse sentiment grows in the market, the Philippine peso can start depreciating against the U.S. dollar again (as of 10 a.m. on August 28).

Junya Tagawa, India Office, Asia & Oceania Treasury Department

# Indian Rupee – September 2018

| Expected Ranges | Against the US$: | INR 67.90–71.30 |
|---|---|---|
| | Against the yen: | JPY 1.56–1.63 |

## 1. Review of the Previous Month

In August, the U.S. dollar/Indian rupee exchange rate renewed its all-time high.

In August, the U.S. dollar/Indian rupee exchange market opened trading at INR 68.59. On August 1, the Reserve Bank of India (the central bank of India, also referred to as the "RBI") announced its decision to raise the policy interest rate in the same way as was done in June. Furthermore, the price outlook for the second half of this fiscal year was revised upward, which encouraged market participants to buy the Indian rupee in anticipation of price appreciation. Thus, on September 2, the U.S. dollar/Indian rupee exchange rate fell to its monthly low at PHP 68.26. However the exchange rate did not continue falling thereafter, and the U.S. dollar/Indian rupee exchange rate continued fluctuating at the upper-INR 68 level without moving in any direction.

However, toward the end of the second week of the month, Turkey refused the release of a U.S. pastor, in reaction to which U.S. President Donald Trump imposed sanctions by doubling customs duties on steel and aluminum imported from Turkey. As a result, the Turkish lira depreciated by more than 30% within two days, which encouraged market participants to sell the currencies of emerging countries. Following this trend, the U.S. dollar/Indian rupee exchange market also opened on Monday, August 13, with a gap from the closing rate of the previous trading day. Thereafter, the exchange rate rapidly exceeded its all-time high observed on July 20 (INR 69.13 against the U.S. dollar). Then, on August 16, the U.S. dollar/Indian rupee exchange rate rose further to reach INR 70.395—the monthly high.

In the fourth week of the month, market participants were aware of the possibility of rupee-buying market interventions by the RBI, while concerns were mitigated regarding trade negotiations between the U.S. and China. As U.S. President Donald Trump also made a comment to confirm that he would not support policy interest hikes, the U.S. dollar/Indian rupee exchange rate returned to the mid-INR 69 level. However, thereafter, the crude oil price appreciated, encouraging market participants to sell the Indian rupee. As a consequence, the U.S. dollar/Indian rupee exchange rate reached the INR 70 level again. As of August 28, when this article is being written, the U.S. dollar/India rupee pair has been trading at around INR 70.10.

In August, the Indian rupee/Japanese yen exchange rate fell to a lower level.

The Indian rupee/Japanese yen exchange market opened trading at the JPY 1.632 level, after which it reached it monthly high at around JPY 1.636. At the beginning of the month, the U.S. dollar/Indian rupee exchange rate continued fluctuating within a narrow range, while the U.S. dollar/Japanese yen exchange rate fell from the upper-JPY 111 level to the mid-JPY 110 level. Following this trend, the Indian rupee also weakened against the Japanese yen. As was discussed above, the media reported actively on Turkey, and the order of currency strength was the Japanese yen, the U.S. dollar, and the Indian rupee, leading market participants to select the Japanese yen. On the other hand, market participants tended to sell the Indian rupee, as a result of which the Indian rupee/Japanese yen exchange rate fell below the JPY 1.60 mark. Thereafter, the Indian rupee/Japanese yen exchange rate continued fluctuating within a narrow range at around JPY 1.58. However, on August 21, the U.S. dollar/Japanese yen exchange rate fell below JPY 110. Following this trend, the Indian rupee/Japanese yen exchange rate also fell to approach JPY 1.572—the monthly low.

However the exchange rate did not continue falling after a while. When the U.S. dollar/Japanese yen exchange rate recovered to the JPY 111 level, the Indian rupee/Japanese yen exchange rate also recovered to the JPY 1.59 level. As of August 28 when this article is being written, the Indian rupee/Japanese yen pair has been trading at the JPY 1.585 level.

## 2. Outlook for This Month:

In September, the U.S dollar/Indian rupee exchange rate is expected to remain low.

With regard to the trade negotiations between the U.S. and China, which were a major preoccupation for market participants until August, there has still been no remarkable progress. However, there has been no intensification of the trade frictions either, maintaining a lull. The depreciation of the Chinese yuan, which continued for a while, has also slowed down, as the Chinese monetary authorities took a measure to control violent fluctuation by changing the calculation method of the underlying exchange rate. With regard to Turkey as well, there has been no specific solution, but stock and bond prices, as well as the exchange rate in Turkey, have all hit bottom, and it seems that the confusion in the market has calmed down as time went by.

When it comes to the U.S., the media repeatedly reported that FRB Chair Jerome Powell emphasized once more the continuation of interest rate hikes at the economic symposium held at Jackson Hole. However, after the speech, market participants did not buy the U.S. dollar, and on the contrary, the U.S.

dollar depreciated. This shows that market participants judged the speech more calmly than the mass media.

With regard to Indian economic indices (as a new tax system was introduced in July 2017, indices calculated based on year-on-year comparison may have some data noise), the June industrial production recorded positive growth of +7.0%, the July Consumer Price Index recorded positive growth of +4.17%, and the July service PMI recorded 54.2 for the first time since October 2016, demonstrating the maintained strength of the Indian economy. In the minutes of the Monetary Policy Committee meeting of the RBI held in August, it was made clear that committee members see the two consecutive interest rate hikes as a pre-emptive action. Thus, it has become less likely for the interest rate to be raised again in the times ahead. However, the price outlook was revised upward while the economic outlook is also marked as positive, while there is some uncertainty regarding external factors.

In addition, the depreciation of the Turkish lira and the Chinese yuan has reached a lull, after encouraging market participants to sell overall Asian currencies and the currencies of emerging countries. The interest rate hike in the U.S. in September has already been reflected in the market, and therefore the U.S. dollar is not likely to appreciate based on this. As economic conditions in India remain strong, the U.S. dollar/Indian rupee exchange rate, which has been at its all-time high, is not likely to rise further but is expected hit a ceiling.

One risk factor that could lead the Indian rupee to depreciate further is the crude oil price. The target rate for the production cut set out by *Organization of the Petroleum Exporting Countries* (OPEC) members and non-members in July was 109%, and thus market participants should remain cautious about a situation in which the WTI price approaches USD 75 (Brent USD 80) again.

This report was prepared based on economic data as of September 3, 2018.
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