Mizuho Dealer's Eye

July 2021

Mizuho Bank, Ltd.

Global Markets Sales Department

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U.S. Dollar – July 2021

Expected Ranges **Against the yen: JPY108.50–112.50**

1. Review of the Previous Month

The dollar/yen pair moved firmly overall in June.

It opened the month trading at the mid-109 yen mark. It was supported at the lower-109 yen mark by expectations about early taping in the US monetary policy. The US released a better-than-expected May ADP National Employment Report on June 3, with the currency pair climbing to the 110 yen range on this and other US bullish economic indicators. The pair was also pushed up by reports that President Biden would review plans to increase corporate tax as part of his infrastructure plan. The May US employment data was released on June 4. The unemployment rate and the average hourly wages data beat expectations, but the nonfarm payrolls figure dipped below expectations. The ADP employment data had roused excessive expectations for tapering and the economic recovery, but the June 4 results poured cold water on these expectations, so the dollar/yen pair dropped back in tandem with sliding US long-term interest rates. The pair moved firmly at its support line at the lower-109 yen level, but its topside was held down as anticipation for early tapering dropped off. It then saw buying and selling around the mid-109 yen mark in the run up to major events like the ECB Governing Council meeting and the release of the US CPI data.

The ECB Governing Council kept policy rates fixed when it met on June 10. In her press conference, ECB president Christine Lagarde said it was too early to discuss tapering the PEPP program. All this was as expected, so the impact on the pair was minimal. The US then released some stronger-than-expected May CPI data, so the greenback was bought for a time and the pair climbed to 109.80 yen. As the details emerged, though, it became clearer that the rise was due in large part to transitory factors. With the FRB also continuing to insist that rising inflation was a temporary phenomenon, the currency pair moved sluggishly as US long-term interest rates fell. With the FOMC meeting looming and several major US economic indicators set to be released, the dollar was not sold further the following week. The yield on 10-year treasuries then recovered to 1.50% after previously falling to the lower-1.40% level, so the dollar/yen pair rallied to the lower-110 yen mark.

The FOMC kept policy rates fixed at its closely-watched meeting. However, the median federal fund rate projection of FOMC members (the dot chart) pointed to a 50bp rate hike by the end of 2023, with the FOMC meeting read as hawkish on the whole. The dollar/yen pair rose to the upper-110 yen mark and it then hit a high of 110.82 yen. Expectations for rate hikes grew at the weekend after several regional FRB governors dropped some hawkish comments about monetary policy, so the dollar was bought. However, the yen was also bought on risk aversion after stocks tumbled, so the currency pair weakened to 109.72 yen. The FRB governor then reiterated that rising inflation was a transitory phenomenon, so the greenback was sold across the board, with the currency pair hitting 110.79 yen on some modest risk appetite. The dollar and yen were both sold on June 23 too, with the pair hitting a high of 111.11 yen. The US released a worse-than-expected May PCE Core Deflator on June 25. As excessive concerns about inflation eased, dollar-selling pressure intensified and the currency pair tumbled to the mid-110 yen level. It then hovered in the mid- to upper-110 yen range in the run up to the release of several US economic indicators at the start of July (as of 17:00 on June 30).

2. Outlook for This Month

The dollar/yen pair is expected to trade firmly in July.

The greenback will be supported once more by the flow of funds into risk assets on expectations for a normalization of economic activity thanks to Covid-19 vaccine roll-outs and so on. There are growing expectations that economic activity will revive in the US and Europe as strict restrictions on movement are lifted. There remain strong concerns about new strains and there are also lingering fears about a new wave of infections in some regions. Despite all this, on a global level there are deep-rooted expectations for a recovery. Japan has also lifted its state of emergency, with hopes for economic normalization likely to grow as the Olympics loom in July. Under these circumstances, risk assets in general and the dollar will probably move firmly. However, economic normalization depends on Covid-19 being kept in check. There is still a risk that new highly-infectious strains could sweep the globe and some people remain pessimistic, so investors should continue to monitor vaccine roll-outs and the spread of new strains.

As for the fundamentals, the US employment data saw a worse-than-expected nonfarm payrolls result. The unemployment rate had improved, but this was due to a rising labor force participation rate. The US economic indicators were not considered as positive results. Though the figures themselves did not meet high prior expectations, the details were not that bad and it seems that the economy essentially remains on the road to recovery. Expectations for tapering also look set to grow steadily on concerns about rising inflation. FRB officials will continue to drop comments aimed at cooling the situation. The FOMC substantially upgraded its inflation outlook for 2021 (PCE core) from 2.0%-2.3% to 2.9%-3.1%. The rate hike projection in the dot chart was also brought forward, with more members expecting a rate hike. As such, the FOMC meeting seemed hawkish on the whole. In his press conference, though, FRB chair Jerome Powell said that "substantial further progress is still a ways off." This was consistent with the FRB's stance that rising inflation is a transitory phenomenon. From here on, the markets will remain in a tug-of-war between rising expectations for early tapering and a commensurate backlash to these excessive expectations.

On the whole, the dollar/yen pair looks set to move firmly this month. The greenback will be susceptible to buying on expectations for FRB tapering and rate hikes. When major countries release their 2Q GDP data, meanwhile, it seems Japan will be the only country to post negative growth, so the yen will continue to be sold too.

Dealers' Market Forecast

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

Bullish on the dollar	15 bulls	112.00 – 109.00	Bearish on the dollar	4 bears	111.25 – 108.00

* Ranges are central values

Tanaka	Bull	112.50 – 109.00	The FRB has shifted in a hawkish direction and it will begin tapering discussions. The market focus will be on the spread of Covid-19 variants and the results of the inflation data and other economic indicators, but the dollar/yen pair will continue to move firmly on the discrepancy in vaccine roll-out rates in the US and Japan and the different directions of each country's monetary policy.
Takeuchi	Bull	112.50 – 108.50	Expectations for tapering and rate hikes will continue to grow on the results of US economic indicators. There are concerns about Covid-19 variants and there will be some correction to excessive expectations regarding monetary policy, but the dollar/yen pair is likely to remain firm. The pair will also be pushed up by the different pace of the economic recoveries in the US and Japan.
Tsutsui	Bear	111.50 – 107.00	Based on what happened in the past, it seems tapering expectations will push the dollar higher. A new quarter has started and investors will be building up new positions at the start of the month with an eye on dollar bullishness, but there will probably be some substantial adjustment mid-July.
Yamagishi	Bull	112.50 – 109.00	As economic activity normalizes, this could lead to soaring asset prices and other problems, so the FRB will probably need to shift away from the easing policies adopted to tackle the Covid-19 crisis. If the markets price in the commencement of tapering at the turn of the year and rate hikes in 2022, the dollar/yen pair will probably continue trading at highs.
Ushijima	Bull	112.00 – 109.00	The FRB has adopted a cautious stance towards rate hikes, but it has also taken a positive stance when it comes to tapering. If the jobs market recovers, the greenback will probably rise in tandem with short-term US interest rates.
Tasaka	Bull	112.50 – 109.00	The FRB began to steer towards an exit in the June FOMC meeting. There remains a dearth of yen-buying factors, while Japanese/US interest-rate differentials have widened. As such, after remaining deadlocked over April–June, the dollar/yen pair's range will probably edge higher this month.
Omi	Bear	111.00 – 108.00	The trend of dollar selling looks set to continue. This is due to ongoing low interest rates, fiscal expansion, and a global appetite for stable currencies. However, this trend will proceed at a gentle pace as the greenback is bought against the yen on risk aversion related to rising US long-term interest rates and falling stocks, for instance.
Ueno	Bear	111.00 – 108.00	The dollar was bought after the June FOMC meeting. However, US interest rates have moved flatly since the meeting as the FRB adopts a cautious stance towards tapering. Under these circumstances, the dollar/yen pair's current level will be ripe for some adjustment.
Yamaguchi	Bull	112.50 – 109.00	The FRB is acting hawkishly compared to other major central banks, so the debate about an exit might be brought forward depending on the results of economic indicators. If US interest rates start rising again, the dollar/yen pair will continue to trend higher.
Onozaki	Bull	112.00 – 109.50	The June FOMC meeting marked the start of the tapering debate. There are also no factors prompting yen bullishness, so the dollar/yen pair will climb as the US economy recovers. The pair's level has edged up since April and it hit 2021 highs in June, with the pair set to rise further from here on.
Tamai	Bull	112.00 – 109.00	Given the focus on the prospect of early tapering by the FRB, it seems the dollar will be bought this month. However, it will probably take some time before the tapering details are ironed out. There are also concerns about the spread of new Covid-19 variants, so the dollar/yen pair's topside will move heavily.
Harada	Bull	112.00 – 109.00	Speculation is growing about early tapering on the strong economy, with the employment data also set to swing upwards as unemployment insurance claims expire. Under these circumstances, the dollar is likely to continue moving bullishly. As such, the dollar/yen pair will remain firm this month.

Oba	Bull	112.00 – 109.75	The FOMC adopted a slightly hawkish approach when it met in June, but the dollar/yen pair has moved cautiously with an eye on economic indicators. The pair will probably edge higher in the trend channel it has moved in since late April. There could be some selling when the pair rises above +2σ of its daily Bollinger Band.
Katoono	Bull	113.00 – 109.00	US interest rates have moved firmly on expectations for FRB monetary policy normalization in the wake of the FOMC meeting, so the dollar/yen pair looks set to continue rising. It will also be boosted by price rises on substantial infrastructure investment and other major economic policies.
Kobayashi	Bull	112.00 – 109.50	The situation will remain unconducive to yen bullishness, even when the dollar moves bearishly. The dollar will appreciate if expectations grow for earlier tapering or rate hikes, so investors will need to watch out for improvements when it comes to economic indicators.
Henmi	Bull	112.00 – 109.00	Though the FOMC made some hawkish interest rate forecasts when it met in June, US rates are moving around 1.5% and they still have room to rise. The FRB is probably laying the ground for some gentle tapering going forward, so the dollar/yen pair will probably move firmly on rising US interest rates.
Otani	Bear	111.50 – 108.50	US interest rates rose after the June FOMC meeting, though this was only transitory. FRB chair Jerome Powell also remains in dovish mode, while concerns are growing about new Covid-19 variants, so the dollar/yen pair's room on the topside will be capped.
Suzuki	Bull	112.00 – 109.50	Stock markets could face some correction on concerns. New Covid-19 variants are also spreading across the US. Nonetheless, it is hard to imagine funds flowing into the yen, so the dollar/yen pair's room on the downside will be capped. There are also deep-rooted expectations for an early start to tapering, so investors will continue to chase the pair's topside.
Okuma	Bull	112.00 – 109.00	FRB members have adopted hawkish stances on the firm US economy, so the dollar is likely to remain firm. There is also speculation that the Japanese economy could stall for a prolonged period as Covid-19 cases surge after the Tokyo Olympics. This situation will also support the dollar/yen pair's movements.

Akihiro Katoono, Forex Sales, Global Markets Sales Department

Euro – July 2021

Expected Ranges	**Against the US$: US$1.1700–1.2000**
	Against the yen: JPY130.50–133.50

1. Review of the Previous Month

The euro/dollar pair weakened on the whole in June.

The greenback was sold against the euro at the start of the month on the results of the May US Manufacturing ISM Report on Business, so the pair climbed to the mid-$1.22 mark. However, the dollar was then bought on June 3 on some bullish US economic indicators, so the pair fell to the lower-$1.21 level before dipping temporarily to $1.2104 on June 4.

With major European stock markets moving firmly the following week, the euro was bought and the pair rallied to $1.22 for a time on June 7. It then moved firmly at the lower-$1.22 level on June 9 as US long-term interest rates dipped below 1.5%. With the ECB Governing Council meeting looming the following day, though, active euro buying was short-lived. At its closely-watched meeting on June 10, the ECB Governing Council decided to maintain the current pace of its purchases under the Pandemic Emergency Purchase Programme (PEPP). The euro was bought directly after. With the dollar/yen pair then rising on the better-than-expected results of the May US CPI data, the euro/yen pair also temporarily hit a weekly high of 133.74 yen. However, in her press conference after the ECB Governing Council meeting, ECB president Christine Lagarde said it was too early to talk about winding down the PEPP, so the euro was then sold. The euro/dollar pair dipped below $1.21 on June 11 as yields on German government bonds fell.

The pair then moved bearishly amid a dearth of new factors on June 14. After hovering right around $1.21, the pair then soared to a weekly high of $1.2147 on June 15 on hopes for a resolution to the trade spat between the US and EU over airplane subsidies. When the FOMC met on June 16, though, it upgraded its economic outlook while also hinting at earlier rate hikes. The greenback moved bullishly on this hawkish stance, so the euro/dollar pair plunged to around the mid-$1.20 level. With US interest rates moving firmly thereafter, the currency pair dropped below $1.20. On June 17, ECB board member Philip Lane said it was too early to talk about ending the PEPP, so the euro was sold further and the pair crashed to $1.1890. The dollar saw more buying on June 18, so the pair's downside hit $1.1848.

With the Nikkei falling sharply, risk aversion prevailed the following week. As the euro/yen pair fell, the euro/dollar pair continued to move bearishly at $1.1848 on June 21. With FRB chair Jerome Powell adopting a dovish stance in his testimony to Congress on June 22, though, the greenback was sold and the pair climbed to the mid-$1.19 level. As risk sentiment's improved on Mr. Powell's dovish comments, the pair moved firmly on June 23. Germany then released a better-than-expected June PMI, so the euro was bought and the pair soared to around $1.1970. After a round of buying, though, the pair fell to the lower-$1.19 mark on rising US interest rates.

The pair hovered around $1.1930 amid a dearth of new factors on June 24. As concerns about inflation in the US eased for a time on June 25, the currency pair rose to the upper-$1.19 level. However, US interest rates then rose again, so the pair dropped below $1.19 on June 29 to end the month trading with a heavy topside.

2. Outlook for This Month

Though investors have reacted well on the whole to the post-pandemic economic recovery, the eurozone authorities looks set to maintain easing for a prolonged period as they focus on a complete recovery. With the FOMC also adopting a hawkish stance in June, the euro/dollar pair looks set to continue trading with a heavy topside on the clear differences in the policies of the ECB and FRB.

There are concerns about the spread of new Covid-19 variants, but there are signs that sentiments are improving on the roll-out of vaccines. The June eurozone business sentiment survey hit its highest level in 21 years on its release on June 29, with the reopening of the economy on vaccine roll-outs helping to prompt a recovery in services and other sectors. When the ECB released its June economic outlook, meanwhile, the data was upgraded (on March’s outlook) when it came to GDP growth (2021: from 4.0% to 4.6%; 2022: 4.1% to 4.7%) and inflation (2021: 1.5% to 1.9%; 2022: 1.2% to 1.5%), with the ECB voicing optimism about the future. However, it did not adjust its monetary policy stance. As well as leaving policy rates fixed, the ECB Governing Council also decided to keep the pace of PEPP purchases unchanged on April–June (and still up on January–March) when it met last month. The ECB indicated it would keep the total scale of the PEPP fixed at 1.85 trillion euros until at least the end of March 2022, with the policy likely to remain in place until the ECB adjudges that the crisis phase is over. In her subsequent press conference, ECB president Christine Lagarde said there had been differing opinions when it comes to the pace of asset purchases, but she also reiterated her commitment to easing on concerns about the uncertainty of the economic outlook. There are also concerns about the recent spread of the delta strain and other Covid-19 variants.

At the moment, expectations for early tapering have sprung up on the steepening of the FOMC’s dot chart in June and on hawkish comments by a series of FRB officials, with the debate about an exit strategy set to flare up again in the US. Last month also reminded investors of the clear differences in the stances of the FRB and ECB. A number of events are looming this month, with a meeting of G20 finance ministers and central bank governors scheduled for July 9 and the ECB and FOMC meeting over July 22 and July 27–28, respectively. However, the ECB is finding it increasingly hard to maintain a balance between the fundamentals and a weak currency, so as many high-ranking figures have stressed, it will probably be too early to start talking about an exit strategy. The focus will also remain fixed on political trends in Germany and France too, so the ECB is unlikely to shift policy, with the euro/dollar pair likely to continue trading with a heavy topside on the divergent monetary policies of the US and Europe.

Dealers' Market Forecast

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

Bullish on the euro	3 bulls	1.2200 – 1.1800	Bearish on the euro	16 bears	1.2000 – 1.1700

* Ranges are central values

Tanaka	Bear	1.2000 – 1.1700	The FRB has shifted in a hawkish direction and it decided to commence tapering discussions. On the other hand, the ECB remains cautious when it comes to an exit strategy. The euro/dollar pair will be weighed down by these divergent policy directions.
Takeuchi	Bear	1.2000 – 1.1750	The euro/dollar pair's movements will be driven by the divergent speculation regarding monetary policy in the US and Europe. There are deep-rooted expectations for tapering and rate hikes in the US, but the ECB remains in cautious mode, so the pair will continue to trade with a heavy topside.
Tsutsui	Bull	1.2250 – 1.1850	The euro/dollar pair will probably move easily by the position inclination. The dollar will probably rise on FRB tapering, but there could be some adjustment to the trend of euro bearishness. If the single currency rises against the pound and the Swiss franc, it will probably do so against the dollar too.
Yamagishi	Bear	1.2100 – 1.1700	The FRB has moved clearly down the path of tapering, but the ECB has kicked discussions about an exit into the long grass, so the euro/dollar pair will move with a heavy topside on these divergent policies. The euro will probably move bearishly if the cross yen's movements are marked by yen bullishness as reflationary trades are unwound on rising US interest rates.
Ushijima	Bear	1.2000 – 1.1700	The dollar was bought back after last month's FOMC meeting, though this trend has taken a breather. Nonetheless, the dollar will probably be bought back again now the FRB has started to discuss tapering. The euro/dollar pair's downside might be tested again in the run up to the FOMC meeting at the month's end.
Tasaka	Bear	1.2000 – 1.1750	The FRB began to steer toward an exit when the FOMC met in June, though the ECB still remains some way from an exit. The euro/dollar pair will move heavily on the topside on these divergent monetary policy stances.
Omi	Bull	1.2200 – 1.1800	The euro/dollar pair will continue to move firmly this month. This will be due to ongoing dollar selling. One potential risk lies in a cut in policy rates. Though several government officials have said there is still room for rate cuts, this seems unlikely right now.
Ueno	Bull	1.2200 – 1.1800	The dollar strengthened after the June FOMC meeting, so the euro/dollar pair moved bearishly last month, though several events now seem to be out of the way. Amid a dearth of new factors, the pair's movements will probably face some adjustment this month.
Yamaguchi	Bear	1.2050 – 1.1750	The ECB is a lot further from an exit than the FRB. The euro/dollar pair will move with a heavy topside on these differing monetary policy stances. The dollar could also be bought on risk aversion due to the spread of Covid-19.
Onozaki	Bear	1.2000 – 1.1600	Though the FRB is likely to start discussing tapering, the ECB remains in cautious mode. The greenback will probably be bought on these divergent stances.
Tamai	Bear	1.2050 – 1.1700	Though the FRB has begun to talk about easing, the ECB remains in dovish mode, so the euro/dollar pair will move with a heavy topside on these different stances.
Harada	Bear	1.2120 – 1.1710	Though economic activity is expected to reopen in Europe, the ECB remains in dovish mode. With the US likely to begin tapering, the euro/dollar pair will move with a heavy topside on these different policy directions.
Oba	Bear	1.1975 – 1.1800	With the US set to start tapering a little earlier than the markets had expected, the euro/dollar pair will probably trade with a heavy topside. However, the FRB's movements could prompt the ECB to lay the groundwork for policy normalization, so investors should be wary of buy-backs.

Katoono	Bear	1.2000 – 1.1700	Though investors have reacted well on the whole to the post-pandemic economic recovery, the eurozone authorities looks set to maintain easing for a prolonged period as they focus on a complete recovery. With the FRB also adopting a hawkish stance, the euro/dollar pair looks set to continue trading with a heavy topside on the divergent policies of the ECB and FRB.
Kobayashi	Bear	1.2100 – 1.1700	The US has begun to talk about tapering, but the ECB remains in easing mode on caution regarding an exit. As such, the euro is likely to remain bearish compared to the dollar.
Henmi	Bear	1.2000 – 1.1700	Though the ECB is set to remain in dovish mode for a while, the FRB began laying the groundwork for tapering at the June FOMC meeting. With the debate about tapering set to begin in earnest from here on, the euro/dollar pair will probably trade with a heavy topside on the divergent monetary policies of the US and Europe.
Otani	Bear	1.2050 – 1.1850	When it met in June, the ECB decided to keep its PEPP purchases at the same accelerated pace in July –September, so excessive expectations for tapering are on the wane. With interest rates within the eurozone held down, the euro/dollar pair will trade with a slightly heavy topside.
Suzuki	Bear	1.2000 – 1.1750	It is growing more likely that the FRB will begin to discuss tapering, but the ECB still seems some way off such a move. The euro will probably be sold against the dollar on the divergent monetary policy stances of the US and Europe.
Okuma	Bear	1.2050 – 1.1700	Though the FRB has shifted in a hawkish direction, the ECB has stressed it is too early to discuss tapering the PEPP, with the ECB some way off monetary policy normalization. There will probably be some verbal interventions to curb euro bullishness too, so the euro/dollar pair will probably trade with a heavy topside.

Joseph McElhill, Europe Treasury Department

British Pound – July 2021

Expected Ranges **Against the US$: US$1.3700–1.4100**
Against the yen: JPY152.00–157.00

1. Review of the Previous Month

The pound moved bearishly at the start of June. It then fell against the dollar and yen from mid-June onwards. However, sterling edged up against the euro before weakening slightly at the month's end. To summarize, from mid-June onwards, the currency markets were swayed by three trends: (1) comprehensive dollar bullishness and euro bearishness, (2) an across-the-board yen rally, and (3) comprehensive pound bearishness. Trend (1) was prompted by rising expectations for an early FRB rate hike in the wake of the June 16 Federal Open Market Committee (FOMC) meeting. The median federal fund rate projection of FOMC members pointed to a 50bp rate hike by the end of 2023 (the projection had previously suggested rates would be left unchanged). With FRB chair Jerome Powell also stating that the debate about tapering (of the FRB's asset purchases) had begun, the FOMC meeting was read as 'more hawkish than expected.' As a result, toward June 18 the pound dropped from just below $1.41 to the $1.38 range against the greenback and it plunged from around 155 yen to the 152 yen range against its Japanese counterpart.

Amid a dearth of new factors, trading was relatively thin on the ground for several days. Sterling edged higher on buy-backs and dollar selling to lock in profits, with the pound/dollar pair rallying from just below $1.38 to the mid-$1.39 level. The (preliminary) UK composite PMI data for June was released on June 23. As 61.7, the figure was down on expectations, though the reaction of the markets was muted. The breakdown showed manufacturing and services moving bearishly, but with employment indicators hitting record highs on the phased easing of Covid-19 restrictions, it seemed the economy remained on the road to recovery. The Bank of England (BOE)'s Monetary Policy Committee (MPC) met on June 24. It kept policy rates and the amount of its asset purchases unchanged, as expected, but it did strike a dovish tone and it mentioned the dangers of tightening too early, for example. As such, rate hike expectations (OIS basis) dropped to 12bps by May 2022, down 2bps compared to before the meeting. As market expectations for an early UK rate hike waned, the pound fell from around $1.3980 to break below $1.3900 again. From June 27 to the end of the month, the pound continued to move bearishly across the board, with the pound/dollar pair closing June around $1.38.

2. Outlook for This Month

The pound looks set to trade firmly in July.

As mentioned earlier, the outlook for the UK economy itself is not pessimistic. When it comes to forex options, the one-month 25-delta risk reversal showed pound put-overs expanding on dollar buying in the wake of the FOMC meeting, but things have already returned to previous levels, so it seems the markets are not overly concerned about pound bearishness. Now the FOMC and BOE meetings are over, attention will focus on the ECB Governing Council meeting mid-July and the Jackson Hole symposium in August, but with few events lined up, it seems the pound will move firmly for a time as it searches for a sense of direction.

Turning to other news, and on June 22 the UK chancellor appointed Catherine Mann, former chief economist at the OECD, to replace Gertjan Vlieghe on the BOE's Monetary Policy Committee (MPC). In a speech in May, Mann hinted at rate hikes in 2022, though it remains to be seen how she act from here on. The BOE's hawkish chief economist Andrew Haldane will also be stepping down in June (he was the only member to vote to cut asset purchases at the recent meeting). Investors will be watching to see who BOE governor Andrew Bailey appoints as Haldane's successor.

Shiho Kawaguchi, Sydney Treasury Office, Asia & Oceania Treasury Department

Australian Dollar – July 2021

Expected Ranges **Against the US$: US$0.7350–0.7770**
Against the yen: JPY82.30–85.80

1. Review of the Previous Month

The AUD/USD pair jostled up and down around $0.77 in the first half of June. After dipping to the $0.7475- 0.7500 range on June 18, it then moved around $0.75 in the latter half of the month.

The pair temporarily rose to the upper-$0.77 area in the first week after Australia posted a better-than-expected 1Q current account balance, but it then dipped back and consumed its gain after the RBA hinted that policy rates might remain the same until 2024. The pair climbed to $0.7774 in the latter half of the week on the firm results of Australia's 1Q GDP data. However, after the US released a bullish May ADP National Employment Report and some strong new applications for unemployment insurance data, US interest rates rose at the weekend on growing expectation for the May US employment data. Then AUD/USD pair fell to a weekly low of $0.7646. However, the result of May US employment data fell below the expectation on its release. The greenback was sold sharply and the pair rallied back to the lower-$0.77 level.

Investors remained in wait-and-see mode overall in the second week until the release of the US May CPI data. The pair remained in a tight 50pips range from Monday to Thursday, though it fell sharply from the upper-$0.77 level to the $0.76 level on the Friday. The US May CPI data ended up beating expectations, but the pair continued trading in a range ($0.7650–0.7770) for a week. The cool market reaction was due to that market participants were aware of the base effect that the data was only strong compared to the previous May, when it had slumped on the impact of Covid-19.

The minutes of RBA board meeting was released in the third week. It said that the board sees the conditions for a rate hike are unlikely to be ready "until 2024 at the earliest," monetary policy "seems to need to remain highly accommodative for some time yet." The minutes also said that members thought it was too early to start talking about an end to QE. These dovish contents saw the AUD/USD pair dropping below $0.77 to hit the upper-$0.76 level. The FOMC then made a hawkish forecast at the meeting, yields on 10-year US treasuries soared and the greenback was also bought, with the currency pair plummeting to around $0.7600. The yield on 10-year treasuries then fell back sharply on June 17 and stocks moved bearishly, with a risk-off mood prevailing. As a result, the pair weakened to $0.7540 and it then dipped to $0.7478 as this trend spilled over into June 18.

The pair moved heavily on falling iron ore prices in the fourth week, but with FRB chair Jerome Powell adopting a dovish stance in his testimony to Congress, expectations for early US rate hikes waned slightly and US stocks rose. The pair subsequently climbed to the mid-$0.75 level. The US May PCE Core Deflator dipped below expectations on a monthly basis in the latter half of the week, so excessive concerns about inflation dropped off. The greenback was sold and the currency pair rose to around $0.7616 for a time. Two-week lockdowns were introduced in the final week to deal with the spread of Covid-19 across several Australian regions, so the pair moved heavily and it hit the upper-$0.75 level once again.

2. Outlook for This Month

The AUS/USD pair's room on the downside looks set to widen in July.

There are concerns that the pace of the economic recovery might slow on the two-week lockdowns implemented in Sydney (NSW) and other regions. The pair will also be impacted by the RBA's policy stance. In the US, meanwhile, the FOMC adopted a hawkish stance at its last meeting. Given the US employment data and the Australian lockdowns, it seems that financial conditions in the two countries are starting to diverge.

When the RBA's board meets on July 6, it will discuss whether to extend its three-year yield target (its yield curve control (YCC) buying target) from April 2024 to November 2024. It will also decide whether to implement more quantitative easing (QE). The result of the meeting will therefore be crucial for gauging the timing of the first rate hike. The RBA has recognized that the Australian economy has recovered at a faster pace than expected, but it has also indicated that it will not hike rates until the inflation rate is moving 'sustainably' in the 2–3% target range. Combined with the current lockdowns, it is hard to imagine any hawkish comments emerging at this point in time.

It seems Australia's domestic fundamentals to be released this month will continue to remain firm, but the AUD/USD pair could be weighed down by ongoing lockdowns.

Mizuho Ashizaki, Canada Office, Americas Treasury Department

Canadian Dollar – July 2021

Expected Ranges	**Against the US$: C$1.2200–1.2600**
	Against the yen: JPY88.00–91.00

1. Review of the Previous Month

The USD/CAD pair opened June trading at C$1.2030. The Canadian dollar continued to move bullishly at the start of the month on the strong results of some Canadian economic indicators and rising crude oil prices, but the greenback was then bought on the hawkish results of the FOMC meeting. After hitting C$1.2487, the pair dropped back after a round of US-dollar buying. However, the greenback continued rising toward the month's end on expectations for tapering in the US.

Canada's 1Q 2021 (January–March) real GDP growth rate was released on June 1. The figure was up +5.6% on the same period last year thanks to housing market growth. This represented the third straight quarter of growth. The markets also reacted well when OPEC+ met and decided to scale back production cuts in stages. US/Iran discussions over a nuclear agreement also stalled. There had been concerns about an increased supply of crude oil if sanctions were lifted, but these concerns now eased off. All this news saw crude oil prices rising. Amid buying in the energy sector, stock prices hit highs on successive days, with the Canadian dollar also rising to C$1.2007 against its US counterpart. Canada's employment data was released on June 4, with the unemployment rate rising to 8.2%. However, the economic indicators had been expected to weaken on the lockdowns imposed to deal with a third wave of Covid-19 infections, so the reaction of the markets was muted. However, the US then released some better-than-expected new applications for unemployment insurance data and a Non-manufacturing ISM Report on Business, so the USD/CAD pair rallied slightly to C$1.2130 on rising US long-term interest rates. The much-anticipated US May employment data was then released. Though the unemployment rate had improved to 5.8% and nonfarm payrolls growth had accelerated on the previous month, the data was down on expectations, so the pair dipped to C$1.2071 on these bearish results.

When the Bank of Canada (BOC) Monetary Policy Committee (MPC) met on June 9, it gave an upbeat outlook for the economic recovery, so the Canadian dollar was bought and the currency pair fell to C$1.2059 before moving in a narrow range from the upper-C$1.20 mark to the lower-$1.21 level. The US May CPI data was released on June 10. At 0.6%, CPI growth was up on the market forecast for 0.4%, but the FRB said inflationary pressures were transitory, so the market reaction was muted. However, the pair then edged up to the upper-C$1.21 mark on renewed speculation about early tapering. The FOMC held its closely-watched meeting on June 16. The median federal fund rate projection of FOMC members (the dot chart) pointed to two rate hikes by the end of 2023. This hawkish shift came as a surprise and the currency pair soared to C$1.2284.

News emerged on June 17 that the UK had seen a surge of cases of the delta variant of Covid-19, particularly among the unvaccinated young. Crude oil prices also fell on reports that the US and Iran were close to reaching a deal. The Canadian dollar was sold to C$1.2487 for a time. The USD/CAD pair then fell to the lower-C$1.23 level after FRB chair Jerome Powell struck a dovish tone in his testimony to Congress. The pair then moved in a narrow range without a sense of direction toward the month's end.

2. Outlook for This Month

Canada has been hit by a third wave of Covid-19 infections, with lockdowns imposed once again, though each state began to steadily ease restrictions from mid-June. Vaccination rates are also rising and Canada now tops the US when it comes to the proportion of people who have received the first shot, with Canada leading the way globally. It is also racing ahead with the second shot, with Covid-19 cases on the slide. Canadian economic indicators are also moving bullishly on the whole.

The BOC Monetary Policy Committee (MPC) kept policy rates fixed when it met last month. As with the previous meeting, it stressed that quantitative easing (QE) and low interest rates would be maintained until the second half of 2022. Household saving rates rose from 11.9% in 4Q 2020 to 13.1% this quarter on the economic support extended by the government during the Covid-19 crisis. If things get back to normal, the MPC expects the domestic economy to recover strongly on consumer spending. The inflation rate is expected to top the 2% target to hit 3% toward summer before stalling throughout the rest of the year. The MPC also said core inflation would undergo a short-lived rise. When it comes to crude oil, OPEC+ decided to increase production over May–July. When OPEC+ next meets on July 1, the focus will be on whether it decides to increase output even further from August. Another concerning factor will be the US/Iran nuclear talks. The hardline conservative anti-American Ebrahim Raisi won Iran's presidential election. Reports suggested the nuclear talks would continue, but talks were then suspended for ten days and it is unclear how things will develop from here on. If a deal is reached, the US will lift sanctions on Iran and this will boost crude oil production. Nonetheless, demand for crude oil will be strong for a while ahead of the summer drive season, so the markets are expecting crude oil prices to rise further. This is also likely to see the Canadian dollar moving firmly.

The BOC MPC will be meeting on July 14. With the economy reopening and vaccination rates rising, the MPC will probably reiterate its bullish outlook for the economic recovery. The FOMC will also be meeting over July 27–28. Most market participants think the details about QE tapering will be held back until the Jackson Hole meeting in August. This month's meeting will probably sound a cautious note as it seeks to avoid any turmoil.

In July, investors should continue to monitor economic indicators, official comments, the situation regarding Covid-19 and the delta variant, and the crude oil market. The greenback will be pushed up as US long-term interest rates rise on the strong results of US economic indicators and rising expectations for tapering. However, the FOMC will try to keep a lid on market turmoil. Other factors prompting Canadian-dollar buying include rising crude oil prices and a sense that there is an oversupply of US dollars. As such, the USD/CAD pair's rise will be capped and the pair will probably trade in a range from C$1.22 to C$1.26 in July.

Hirobumi Nakano, Seoul Treasury Office, East Asia Treasury Department

Korean Won – July 2021

Expected Ranges **Against the US$: KRW 1,110–1,150**
Against the yen: JPY 9.615–10.101 (KRW100)
(KRW 9.900–10.400)

1. Review of the Previous Month

The USD/KRW pair rose in June.

On June 1, the dollar was sold against other major currencies (apart from the RMB), with the USD/KRW pair also falling to a monthly low of KRW1105.0. On June 2, though, the Chinese authorities lifted the reserve requirement ratio for foreign currency deposits from 5% to 7% while also warning about speculative moves behind the RMB's recent bullishness, so the RMB then weakened. Concerns about inflation also surged during overseas trading time on June 3 after the price of labor per single unit of output shot up by +1.7% q-o-q in the US. All this saw the currency pair rising to KRW1119.1 on June 4. However, the greenback was sold on June 4 on the worse-than-expected results of the US employment data (up 559,000 against expectations for a 675,000 rise), so the pair opened June 7 trading at KRW1111.2. Amid a dearth of new factors, the pair then made some minor fluctuations.

The US released some stronger-than-expected CPI data on June 10, but this was largely due to air fares and so on recovering from the Covid-19 slump, with rising inflation apparently a transitory phenomenon. South Korean government bond yields then rose when the governor of the Bank of Korea (BOK) said policy would be normalized if the economy recovered, so the currency pair temporarily dropped back to KRW1111, though it then rose again and it began June 14 trading at KRW1116.3.

The pair then moved flatly at the upper-KRW1110 mark amid an absence of noteworthy factors in the run up to the FOMC meeting on June 16. Though the FOMC decided to keep the FF rate fixed, the accompanying statement mentioned how the impact of Covid-19 was waning on the roll-out of vaccines, with the economy further down the path of recovery compared to the last meeting in April. In the dot chart (the FF rate projection), meanwhile, six out of 19 FOMC members predicted two or more rate hikes up until the end of 2023 (up from two members last time). This suggested that rates would be lifted at a faster pace than market participants had expected, so yields on 2-year and 3-year US treasuries soared, with the USD/KRW pair rising to KRW1130 for the first time in a month.

The pair opened June 21 trading at KRW1135.5. Yields on 2-year treasuries rocketed on concerns about early rate hikes in the US, but flattening also occurred as the yield on 10-year treasuries temporarily dropped to 1.36%, for example. With emerging-economy currencies then being sold across the board, the pair hit a monthly high of KRW1138.8. However, the won was then bought on a sense it was now at a good level, so the pair tumbled to KRW1131.1 on June 22. A sense of composure then swept the markets for several days after FRB chair Jerome Powell, the NY FRB governor and several other FRB officials spoke about how rising inflation was a transitory phenomenon and it would take time to hit full employment.

During overseas trading time on June 24, the Biden administration and a nonpartisan Senate grouping reached an agreement on a $1 trillion infrastructure investment bill. With the won also bought on real demand, the currency pair fell to KRW1126.8. The won was bought on real demand in the final week, but the pair moved with a general lack of direction to eventually close the month at KRW1126.1, up 15.2 won compared to the end of May.

2. Outlook for This Month

The USD/KRW pair will move with a lack of direction in July.

The greenback was bought last month after the FRB upgraded its FF rate projection in the dot chart. The USD/KRW pair also rose. The Bank of Korea (BOK) has spoken about the economic recovery in South Korea and it has also hinted that it might hike rates ('normalization' in the BOK's parlance) within the year to give it room to maneuver, but the impact on the currency pair's movements has been muted on the substantial influence of expectations for FRB rate hikes.

There are three factors to watch out for this month:

(1) A potential shift in FRB monetary policy at the July FOMC meeting, (2) the impact of the delta variant of Covid-19, and (3) hints by the BOK about the timing of rate hikes.

As for (1), the June FOMC has broadly factored in a US economic recovery on the vaccine roll-out, so the markets are not expecting the FOMC to make any further signals about monetary policy normalization when it meets in July. There could be some clues (the hitting of inflation or employment targets, etc.) regarding the timing of rate hikes (the first one is expected some time between late 2022 and early 2023), so investors should continue to monitor events. At the start of 2021, the focus turned to how 10-year treasury yields would move on the post-pandemic recovery. However, investors are now focused on the sharp movements of 2-year and 3-year treasury yields as they seek to gauge the timing of rate hikes. Generally speaking, a sense of ease sweeps the markets when short-term interest rates rise sharply, with the greenback then susceptible to buying, so this trend could see the dollar bought against the won.

Turning to (2), and the delta variant is spreading across the UK, Australia and other countries with successful vaccination programs. Reports suggest the Moderna vaccine is effective against the delta variant, while it seems vaccinated people are not becoming very ill even if they contract the variant, so it is not turning into a major problem. Instead, it will probably become a short-term risk-off factor.

With regards to (3), if the BOK brings forward the timing of the next rate hike, it will probably do so in August, though it might drop some hints when it meets this month. The impact of this factor on the currency pair has been muted so far, but it might have a bigger impact going forward, so caution will be needed.

Under these circumstances, the KRW/USD pair will probably stop rising for a time in July. Though factors (1) and (2) might prompt dollar buying, a FRB rate hike seems to have been sufficiently factored into 2-year US treasury yields. Amid the spread of the delta variant, it is hard to imagine the FRB taking more steps towards financial normalization in July, so the pace of dollar buying will probably ease.

Hirochika Shibata, Taipei Treasury Office, East Asia Treasury Department

New Taiwan Dollar – July 2021

Expected Ranges **Against the US$: NT$27.60–28.10**
Against the yen: JPY3.90–4.05

1. Review of the Previous Month

In June, the Taiwan dollar hits its highest level against the greenback for roughly 24 years, though the US dollar was bought back thereafter.

The USD/TWD pair opened the month trading at TWD27.610. Exporters had sold the US dollar at the end of May and this trend spilled over into June, so the Taiwan dollar remained bullish against its US counterpart. The pair temporarily dipped to TWD27.502, with the Taiwan dollar hitting its highest level against the greenback in roughly 24 years. Taiwan-dollar buying then eased and the pair returned to TWD27.60. The RMB and other Asian currencies then fell against the US dollar. With importers also buying the greenback, the currency pair climbed to TWD27.70. With the number of domestic Covid-19 cases not falling, Taiwan stocks moved sluggishly in the first half of the month. With stocks also being sold on balance by overseas investors, the USD/TWD pair moved firmly on the downside around TWD27.70.

Taiwan stocks edged higher mid-June, so the Taiwan dollar was bought and the currency pair dropped below TWD27.60 for a time on June 11. However, the US dollar was bought back on adjustive movements ahead of the FOMC meeting. With the greenback also being bought by foreign firms and life insurance companies, for example, the pair strengthened to around TWD27.70. US interest rates rose after on June 17 after the FOMC meeting, with the currency pair temporarily hitting TWD27.790, though it soon returned to around TWD27.70. With short-term US interest rates then climbing, though, the Taiwan dollar was sold by overseas investors, so the USD/TWD pair edged up to TWD27.80.

The latter half of the month saw Asian stocks crashing on June 21 on concerns about early tapering in the US. Taiwan stocks were also sold, with the currency pair rising to around TWD28.00. Taiwanese stocks were sold sharply on balance by overseas investors, so the Taiwan dollar faced selling pressure. As a result, the currency pair climbed to TWD28 for the first time in around a month on June 23 before hitting TWD28.026 for a time. It then moved around TWD28.00. Taiwan-dollar selling by overseas investors eased off, while exporters sold the greenback ahead of the end of the quarter, so the pair tumbled to TWD27.850. It then moved around TWD27.90 on brisk movements by overseas investors. However, the US dollar was sold by exporters on June 30. With the Taiwan Capitalization Weighted Stock Index also hitting record highs, the Taiwan dollar was bought by overseas investors, so the pair tumbled to TWD27.822 for a time.

2. Outlook for This Month

The USD/TWD pair is expected to trade in a range in July.

The Taiwan dollar has moved bullishly since last year on brisk exports, with exporters remaining in good shape. The May export amount increased by +28.6% year-on-year, with export orders also remaining firm at +34.5% y-o-y, so exports will remain a bullish factor for the Taiwan dollar. However, expectations for an early rate hike by the

FOMC rose in June, with short-term interest rates, etc. rising, so overseas investors stepped into action and Taiwan dollar bullishness was kept in check by funds flowing outside the country.

As mentioned above, though exporters will sell the greenback in July, the USD/TWD will sway to and fro on the movements of US interest rates. In March and June, dollar selling on brisk exports was overshadowed as overseas investors repatriated funds on rising US long-term interest rates, with this trend helping to keep a lid on Taiwan-dollar bullishness. Furthermore, with interest rates rising overseas, the Taiwan dollar will be sold as insurance companies and other domestic investors move to invest outside Taiwan. From here on, the USD/TWD pair will probably move in a range as US interest rates are swayed by the results of US economic indicators.

Ken Cheung, East Asia Treasury Department

Hong Kong Dollar – July2021

Expected Ranges	**Against the US$: HK$ 7.7550–7.7800**
	Against the yen: JPY 14.00–14.45

1. Review of the Previous Month

Hong Kong dollar spot exchange market in June

HKD spot reversed its course and fell to around 7.76 level after hitting its 3-month high of 7.7560 level. The HKD buying flow related to the IPOs and dividend payments from Chinese companies failed to boost the HKD while the hawkish Fed fueled HKD selling pressure. USD rates jumped after Fed's hawkish shift while the HKD-USD rate spread stayed at near par. Stock Connect inflow into HK stock markets held steady, with the year-to-date flow hovering at around HKD 460bn. IPO activities continued to buoy in first half of this year but the inflow was not strong enough to push HKD to 7.75 level. On the macro side, HK consumption recovery was gradual before border re-opening while labour market improved at a quickening pace, with unemployment rate down by 0.4ppt to 6.0%. CPI inflation remained modest at 1.0%YoY in May.

Hong Kong dollar interest rate market in June

Front-end HKD rates tracked on rising USD rates after Fed's hawkish shift at mid-June. 1-month and 3-month HKD HIBOR edged up to 0.09% and 0.17%, respectively, while the HKD-USD rates spread was trading at near par. HKD liquidity condition remained flush, with HKMA aggregate balance hovering at its record high of HKD 457.5bn. Market participants pushed forward Fed's rate hike expectation, and HKD rates were facing with sooner rate hike pressure under the USD-HKD peg. In particular, 3Y HKD IRS rate jumped notably to 0.52% from 0.39% at May-end. The negative HKD IRS carry (customer pays fixed 3Y HKD IRS, receives floating 3-month HKD LIBOR) widened to -35bps from -22bps at May-end, highlighting the firmer hedging interest on HKD interest rates upside.

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2. Outlook for This Month

Hong Kong dollar spot exchange market in July

USD/HKD spot is expected to range between 7.755 and 7.780 in the coming month. The Fed's hawkish shift pointed to a sooner US rate hike cycle and the shot-up in front-end USD rates could drive USD/HKD higher. The FOMC meeting at July-end could send out more hawkish signal. On the contrary, HKD rates are subjected to the downside risk after the half year-end funding squeeze. The resurgent tapering tantrum will also pressure the EM Asian currencies including the HKD, as the Fed is set to drain excessive USD liquidity earlier than expected. Stock Connect inflow to HKD market should remain steady in the summer, but the dividend payment flow and IPO flow related to the Chinese electronic vehicles (EVs) sector will likely keep the HKD supportive.

Hong Kong dollar interest rate market in July

The hawkish shift at the FOMC meeting in June was the turning point of the downtrend for USD and USD rates. Front-end USD rates were bottomed out and are set to rise further amid the tapering discussion. Meanwhile, HKD liquidity condition should stay flush as long as the HKMA aggregate balance was hovering at its record high of HKD 457.5bn. The HKMA should have little intention to drain HKD liquidity via extra Exchange Fund Bills and Notes (EFBNs) issuances, given the active IPO projects in HK exchanges in H2. The HKD IRS curve within 3 year tenors will come under heavier upward pressure as market participants pushed forward the expectation for Fed's rate hike cycle to tame inflation risk.

Sae Sueyoshi, Treasury Department, MHBK (China)

Chinese Yuan – July 2021

Expected Ranges	**Against the US$: CNY 6.3500–6.6500**
	Against the yen: JPY 16.39–17.95
	Against 100 yen: CNY 5.5700–6.1000

1. Review of the Previous Month

The U.S. dollar/Chinese yuan exchange rate rose in June.

On May 31, the U.S. dollar/Chinese yuan exchange rate renewed its lowest point since the beginning of the year, reaching CNY 6.3565. However, media outlets reported immediately thereafter that the reserve requirement ratio on foreign exchange deposits was raised, which dramatically changed the trend of Chinese yuan appreciation, and the U.S. dollar/Chinese yuan exchange rate rose to the lower-CNY 6.37 level. Thereafter, on June 1, the U.S. dollar/Chinese yuan exchange rate continued rising and reached the CNY 6.38 level. On June 3, market participants bought the U.S. dollar, as U.S. economic indices turned out to be strong. As a result, the U.S. dollar/Chinese yuan exchange rate recovered to the CNY 6.40 level. In the evening of June 4, the U.S. employment statistics were released, and the results turned out to be weaker than estimated, which led the U.S. dollar/Chinese yuan exchange rate to fall from the CNY 6.41 level to the CNY 6.39 level.

On June 7, the U.S. dollar/Chinese yuan exchange market started trading at the upper-CNY 6.39 level, immediately after which market participants started buying the U.S. dollar, and the U.S. dollar/Chinese yuan exchange rate rose to the CNY 6.40 level. However, in the evening of the same day, the Chinese yuan appreciated, and the U.S. dollar/Chinese yuan exchange rate reached the CNY 6.39 level. The U.S. dollar/Chinese yuan exchange market was not impacted significantly by domestic economic indices in China, such as the trade balance announced on June 7 or the CPI announced on June 9. Thus, the U.S. dollar/Chinese yuan exchange rate continued fluctuating without moving in any direction at around the CNY 6.39 level. Under such circumstances, the daily high for the U.S. dollar/Chinese yuan exchange rate started to fall gradually from the lower-CNY 6.40 level to the lower-CNY 6.39 level. On June 11, the U.S. dollar/Chinese yuan exchange rate fluctuated at the CNY 6.38 level.

On June 15, the U.S. dollar/Chinese yuan exchange market opened trading at around the CNY 6.40 level. On June 16, major May economic indices for China were released, and the figures were generally weaker than expected. However, the U.S. dollar/Chinese yuan exchange market was impacted only to a limited extent, as a Federal Open Market Committee (FOMC) meeting was approaching. At the FOMC meeting, the median value of the dot plot for 2023 was raised from 0.125% to 0.625% (implying two interest rate hikes), while many committee members anticipated one interest rate hike or more in 2022. Furthermore, the interest rate on excess reserves (IOER rate) and the overnight reverse repo (RRP) rate were both raised by 5 basis points. As the outcome of the FOMC meeting turned out to be more hawkish than expected in the market, U.S. interest rates rose, strengthening the U.S. dollar in the overall foreign exchange market. As a consequence, the offshore U.S. dollar/Chinese yuan exchange rate rose to the CNH 6.44 level. On June 17, the U.S. dollar/Chinese yuan exchange market opened trading at the CNY 6.42 level with a gap from the previous trading day's closing rate. Thereafter, the U.S. dollar/Chinese yuan exchange rate remained stable as the outcome of the FOMC meeting was reflected in the market. On June 18, the

U.S. dollar/Chinese yuan exchange rate recovered to a level near the CNY 6.45 level.

On June 21, the U.S. dollar/Chinese yuan exchange market opened trading at the lower-CNY 6.45 level. The U.S. dollar remained strong as a result of the hawkish outcome of the FOMC meeting, and the U.S. dollar/Chinese yuan exchange rate approached the CNY 6.47 level in the morning. On the same day, the Loan Prime Rate (LPR) was announced, and the rates were maintained at the existing levels for the 14th consecutive month (the one-year rate: 3.85%; five-year rate: 4.65%), thus impacting the market only to a limited extent. The trend of U.S. dollar appreciation persisted until June 23, and the U.S. dollar/Chinese yuan exchange rate once reached the CNY 6.49 level for the first time since April 28. However, the trend was inverted thereafter, and the U.S. dollar started to depreciate. On the previous day, Federal Reserve Board (FRB) Chair Jerome Powell had emphasized during a congressional testimony that the current inflation situation was only temporary, and this also encouraged market participants to sell the U.S. dollar, leading the U.S. dollar/Chinese yuan exchange rate to fall further.

2. Outlook for This Month

The U.S. dollar/Chinese yuan exchange rate is forecast to remain low in July.

The People's Bank of China (PBOC) raised its reserve requirement ratio on foreign exchange deposits while the State Administration of Foreign Exchange (SAFE) expanded the quotas of outbound security investment for qualified domestic institutional investors (QDII), and the China Development Bank procured U.S. dollars in Mainland China for the first time in six years. In the market, these measures were seen as efforts to stop the rapid appreciation of the Chinese yuan. As a result, the Chinese yuan started to depreciate in June.

Even though the hawkish outcome of the FOMC meeting accelerated the appreciation of the U.S. dollar and the depreciation of the Chinese yuan, the depreciation of the Chinese yuan paused temporarily after the congressional testimony of FRB Chair Jerome Powell.

It is possible for the U.S. dollar to appreciate if U.S. economic indices turn out to be strong. However, it is also necessary to assess if the economic recovery is a temporary one. Therefore, the rise of the U.S. dollar/Chinese yuan exchange rate is likely to last only for a limited period of time. Market participants should remain attentive, as there are various factors that would raise U.S. interest rates and strengthen the U.S. dollar, such as the FOMC meeting in July and others beyond, the Jackson Hole Economic Symposium scheduled for August, the advancement of Covid-19 vaccination programs, and the positive evaluation of the economic stimulus measures to be taken by U.S. President Joe Biden.

On the other hand, there has been remarkable capital inflow into the Chinese stock and bond markets, and this has been strengthening the Chinese yuan.

The major statistics in May turned out to be weaker than expected, confirming that the economy had been recovering at a somewhat moderate pace. However, it is clear that economic activities in China have been expanding more significantly compared to other countries, and this has been a factor to strengthen the Chinese yuan. Even though the U.S. dollar could appreciate with mounting expectations for monetary normalization in the U.S., the Chinese yuan is forecast to strengthen from a long-term perspective based on economic strength in China.

Hayaki Narita, Asia & Oceania Treasury Department

Singapore Dollar – July 2021

Expected Ranges **Against the US$: SG$ 1.3200–1.3500**
Against the yen: JPY 81.00–83.00

1. Review of the Previous Month

In June 2021, the Singapore dollar depreciated against the U.S. dollar.

The Singapore dollar remained weak since the beginning of the month. While the U.S. dollar continued appreciating with mounting expectations for the May employment statistics of the U.S., the Singapore dollar continued depreciating. As a consequence, the U.S. dollar/Singapore dollar exchange rate, which was at the SGD 1.32 level at the beginning of the month, reached the mid-SGD 1.33 level toward June 4. Thereafter, the May employment statistics of the U.S. were released, but the figures were weaker than expected in the market, diminishing expectations for early tapering by the Federal Reserve Board (FRB). Also, U.S. interest rates fell, following which the trend was inverted and the Singapore dollar started to appreciate. The U.S. dollar/Singapore dollar exchange rate returned to the lower-SGD 1.32 level.

Thereafter, the Singapore dollar depreciated gradually toward the middle of the month. After employment statistics had impacted the market, there were few factors of market impact, and there was no clear trend in the U.S. dollar/Singapore dollar market. Thus, the U.S. dollar/Singapore dollar exchange rate continued fluctuating within a narrow range at the lower-SGD 1.32 level.

On June 17, U.S. interest rates rose in reaction to the surprising outcome of a Federal Open Market Committee (FOMC) meeting in the U.S. that turned out to be surprisingly hawkish with an upward revision on monetary policy outlook by committee members. In reaction, the U.S. dollar strengthened in the overall foreign exchange market, while the majority of the currencies of emerging countries depreciated. As a consequence, the trend in the U.S. dollar/Singapore dollar exchange market changed significantly, and the Singapore dollar depreciated against the U.S. dollar, leading the U.S. dollar/Singapore dollar exchange rate, which had been fluctuating at the SGD 1.32 level, to reach the upper-SGD 1.33 level.

Thereafter, the U.S. dollar continued appreciating further, while the Singapore dollar remained weak. Toward June 21, the U.S. dollar/Singapore dollar exchange rate reached its monthly high, at the upper-SGD 1.34 level. After the appreciation of the U.S. dollar slowed, the currencies of emerging countries remained generally weak. Market participants did not see any significant change in monetary policy in the U.S. after the congressional testimony by FRB Chair Jerome Powell. Therefore, the U.S. dollar remained strong, even though there were both negative and positive factors in emerging countries. As of the time of writing on June 29, the U.S. dollar/Singapore dollar exchange rate had been fluctuating at the lower-SGD 1.34 level.

2. Outlook for This Month

In July 2021, the Singapore dollar is forecast to appreciate against the U.S. dollar.

In June, the Singapore dollar weakened against the U.S. dollar as a result of the surprisingly hawkish outcome of an FOMC meeting in the U.S. However, as the U.S. dollar/Singapore dollar exchange rate had already been near the upper end of the NEER band, the Singapore dollar was weakened only slightly, balancing the recent appreciation of the Singapore dollar without any severe impact. Therefore, from a medium- to long-term perspective, the Singapore dollar is still expected to appreciate gradually against the U.S. dollar. (According to our data, the Singapore dollar had been higher than the median value of the NEER by approximately 140 to 150 basis points, while the upper end was 200 basis points and while, after the FOMC meeting, the level fell by approximately 50 basis points.)

The Singapore dollar exchange market is likely to follow U.S. interest rates as well as the U.S. dollar exchange market in the immediate future. However, Covid-19 vaccinations have been advancing relatively rapidly in Singapore, and some see that the country will soon attain herd immunity. The Singapore dollar is therefore establishing its status as a safe currency compared to the currencies of neighboring countries. In the times ahead, it is possible for the Singapore dollar to temporarily weaken to the SGD 1.39 level, as the U.S. starts signaling the timing of its monetary tapering. However, along with economic recovery in neighboring countries and changes in the attitude of the Monetary Authority of Singapore (MAS), the U.S. dollar/Singapore dollar is expected to reach the SGD 1.30–1.33 level in the end.

It is also worth noting that this outlook is generally based on the precondition that the U.S. will maintain its intention of monetary tapering and that the People’s Bank of China (PBOC) will promote the stability of the NEER of the Chinese yuan. Even if the U.S. continues to signal monetary tapering, the Chinese yuan is likely to remain relatively stable. As a result, the U.S. dollar and the Chinese yuan will appreciate, and because the two currencies are both likely to occupy a large proportion of the currency basket for the Singapore dollar, the Singapore dollar exchange rate is expected to stabilize as well.

Takeshi Hashi, Bangkok Treasury Office, Asia & Oceania Treasury Department

Thai Baht – July 2021

Expected Ranges | **Against the US$: THB 31.30–32.50**
Against the yen: JPY 3.41–3.53

1. Review of the Previous Month

In June, the U.S. dollar/Thai baht exchange rate renewed its highest-level since the beginning of the year.

At the beginning of the month, the U.S. dollar/Thai baht exchange market opened trading at around the THB 31.20 level. The Thai baht had been appreciating while the U.S. dollar had been weakening since the previous month, and the trend persisted in June, leading the U.S. dollar/Thai baht exchange rate to continue gradually falling. However, the U.S. dollar/Thai baht exchange rate rallied on June 3, as U.S. economic indices turned out to be strong. Then, on June 4, the May CPI of Thailand was announced, and the result turned out to be +2.44% year-on-year, recording a slowdown from April. In the following week, the U.S. dollar/Thai baht exchange rate continued fluctuating within a narrow range at the lower-THB 31 level from June 7 until June 10, as this was a so-called "Blackout Period" before a Federal Open Market Committee (FOMC) meeting in the U.S. However, on June 11, market participants continued selling the U.S. dollar toward market closing, local time, leading the U.S. dollar/Thai baht exchange rate to fall and approach the THB 31.05 level for the first time in approximately one month.

After the weekend, there were few signs of movement in the U.S. dollar/Thai baht exchange market, as the Chinese market was closed on June 14, and the timing was before the FOMC meeting. Thereafter, media outlets reported that there had been radiation leakage at a nuclear power plant in China, and this encouraged market participants to actively sell the Chinese yuan in the offshore market. However, the Thai baht exchange market was impacted only to a limited extent, and the U.S. dollar/Thai baht exchange rate remained stable, at around the THB 31.10 level. On June 15, Thai Prime Minister Prayut Chan-o-cha announced a plan for October to accept entry without quarantine of those that have been vaccinated. However, there was little impact on the Thai baht exchange market. Then, on June 16, an FOMC meeting was held in the U.S., attracting substantial attention in the market, and the outcome was surprisingly hawkish. The dot plot was significantly higher than expected, leading U.S. interest rates to rise. As a result, market participants started to buy the U.S. dollar in an accelerated manner. Following this trend, the U.S. dollar/Thai baht exchange rate also rose to approach the THB 31.35 level.

On June 17, the U.S. dollar/Thai baht started rising. While the U.S. dollar continued strengthening after the FOMC meeting, President of the Federal Reserve Bank of St. Louis James Bullard, who is known to be dovish, made a remark on June 18 such that interest rates should be raised toward the end of 2022, and this comment strengthened the U.S. dollar further. In the following week, the U.S. dollar continued appreciating, and the U.S. dollar/Thai baht exchange rate reached its monthly high on June 21. Then, on June 24, the central bank of Thailand held its Monetary Policy Committee (MPC) meeting, and the policy interest rate was maintained at 0.50% as a unanimous decision. Also, the 2021 GDP outlook for Thailand was revised downward to 1.8%, and this encouraged market participants to continue selling the Thai baht. Under such circumstances, the U.S. dollar/Thai baht exchange rate rose, once approaching the THB 31.90 level. Toward the end of the month, the U.S. dollar/Thai baht exchange rate continued rising, and hospital beds were filled with Covid-19 patients in both public and private hospitals, fueling concerns over the collapse of the medical system, keeping the Thai baht weak. On June 26, the government announced stricter measures on movement in five provinces, including Bangkok. As a consequence, the U.S. dollar/Thai baht reached the THB 32 mark on June 29, and trading closed at the highest level recorded since the beginning of the year.

2. Outlook for This Month

In July, the U.S. dollar/Thai baht exchange rate is forecast to approach its all-time high.

During June, the U.S. dollar/Thai baht exchange rate continued falling gradually, following the trend of the previous month, until the middle of the month. However, having seen the hawkish outcome of the FOMC meeting in the U.S., market sentiment changed significantly. As a result, the U.S. dollar/Thai baht exchange rate was higher at closing than at opening of the same day for nine consecutive days from June 14. Toward the end of the month, the U.S. dollar/Thai baht exchange rate renewed its highest level recorded since the beginning of the year, reaching the THB 32 level, breaking out of the range in which the exchange rate had remained since March.

The U.S. dollar/Thai baht exchange rate rose mainly because the monetary policy of the U.S. turned out to be hawkish while economic recovery in Thailand had been slow, with the number of domestic Covid-19 cases not yet under control. However, it can be said that the U.S. dollar/Thai baht exchange rate has been rising at a surprising rate. Originally, the Thai baht was expected to strengthen in June, as the dividend flow in May had passed while the SET Index had been on a rise, and there had been robust capital inflow from foreign investors. However, the trend did not change after the FOMC meeting, and the exchange rate has still been rising.

The Covid-19 situation in Thailand seems to be at its worst state so far, with domestic hospitals full of Covid-19 patients, while the fiscal measures of the Thai government have been exhausted. In terms of Covid-19 vaccinations as well, it is said that shipments of vaccines have been delayed, with no optimistic news on the horizon. In terms of monetary policy, at the MPC meeting held in June, the central bank of Thailand maintained its attitude to make decisions based on the situation of Covid-19 vaccinations. Thus, it will take a long time for the Thai economy to be normalized with interest rate hikes. Under such circumstances, there are few reasons for market participants to continue buying the Thai baht. Therefore, it is unlikely for the current trend to be inverted in the U.S. dollar/Thai baht exchange market.

In July, the province of Phuket will be open to those that have been vaccinated abroad. However, those that arrive will not be able to move from the province of entry for at least 14 days. Thus, it is not possible for foreign tourists to increase significantly. It is evident that the Thai government wishes to boost the Thai economy by attracting tourists from abroad. However, as it turns out that the positive impact of such a measure on the real economy is limited, it will become more difficult to expect the economy to be normalized. Therefore, the U.S. dollar/Thai baht exchange rate is expected to approach its high in July.

Rui Uchida, Mizuho Bank (Malaysia) Berhad

Malaysian Ringgit – July 2021

Expected Ranges	**Against the US$: MYR 4.10–4.20**
	Against the yen: JPY 26.38–27.10
	Against 100 yen: MYR 3.690–3.790

1. Review of the Previous Month

As was the case in May, the Malaysian ringgit remained weak in June. At the beginning of the month, the U.S. dollar/Malaysian ringgit exchange market opened trading at the MYR 4.12 level. At the end of the month, the U.S. dollar/Malaysian ringgit exchange rate rose and temporarily reached MYR 4.17 for the first time since November last year. Even though the Malaysian ringgit was somewhat stable during the first half of the month thanks to expectations for Covid-19 vaccinations, the Malaysian ringgit started weakening after a Federal Open Market Committee (FOMC) meeting in the U.S.

At the beginning of the month, the Malaysian ringgit remained somewhat stable. On June 1, Malaysia once again announced a full movement control order (FMCO), along with a new economic measure against the Covid-19 pandemic, i.e., the "Pemerkasa Plus" program, which allots MYR 40 billion with a national treasury payment of MYR 5 billion (half of the previous fiscal measure), as a financial support mechanism. However, impact on the market was limited. On the other hand, various media outlets reported on the positive attitude of the government toward Covid-19 vaccinations, as included in Malaysia's economic plans. Under such circumstances, it has been confirmed that an increasing number of people were vaccinated in June, and this stabilized the Malaysian ringgit exchange market. Furthermore, the May CPI of the U.S. was announced on June 10, and the result turned out to be higher than expected. However, U.S. interest rates fell after this announcement, encouraging market participants to sell the U.S. dollar, and this also supported the Malaysian ringgit.

Toward the middle of the month, the U.S. dollar appreciated, and the Malaysian ringgit depreciated sharply, as market participants understood that the outcome of the FOMC meeting held in the U.S. on June 16 was signaling to imply an early interest rate hike. Furthermore, in Malaysia on June 15, Prime Minister of Malaysia Muhyiddin Yassin announced a national recovery plan. The government strengthened its program for Covid-19 vaccinations toward increasing the number of people vaccinated in one day to 200,000, fueling expectations for the further advancement of the vaccination program. On the other hand, there have been some political moves, as King of Malaysia Abdullah of Pahang called for the reopening of the Parliament of Malaysia despite being under a state of emergency, as a result of which the Malaysian ringgit market remained unstable.

Toward the end of the month, there were negative media reports about Malaysia, and the U.S. dollar/Malaysian ringgit exchange rate weakened, temporarily reaching the MYR 4.17 level on June 24 for the first time in approximately seven months. First of all, ratings agency S&P maintained its sovereign rating outlook for Malaysia at "negative," while revising Malaysia's GDP outlook for 2021 downward from 6.2% to 4.1%. S&P pointed out that overall economic growth has supported the Malaysian ringgit, as exports continued under the movement control order (MCO). S&P also pointed out that, however, tight government finances might lead to a slowdown in the domestic economic recovery along with a delay in the Covid-19 vaccination program and in the lifting of lockdown measures, fueling concern over the further deterioration of fiscal conditions. Furthermore, on June 23, the World Bank also revised the growth outlook for Malaysia downward from 6.0% to 4.5%. Then, on June 25, the May CPI of Malaysia was announced, and the result turned out to be 4.4%—the market estimate was 4.7%. While crude oil prices continue rising, the CPI did not exceed the 5% mark expected in the annual report announced by the central bank of Malaysia in March this year, thus not evoking concerns over inflation.

2. Outlook for This Month

In July, market participants should pay attention to the advancement of Covid-19 measures in Malaysia included in the national recovery plan announced by Prime Minister of Malaysia Muhyiddin Yassin on June 15. The Malaysian government has been working on the promotion of Covid-19 vaccinations in cooperation with both public and private institutions by allocating an additional budget. In addition to the rise of the vaccination rate in Malaysia as a result of an increase in the number of vaccination centers being operated, market participants should also pay attention to the Public-Private Partnership Covid-19 Industry Immunisation Programme (PIKAS), which started on June 16. If the program develops steadily enough to control clusters at work, which has been one of the main factors for the increase in Covid-19 cases, the vaccination rate would rise, reducing the number of infection cases and solving the problem of high ICU occupancy. Furthermore, Malaysian Senior Minister for Finance and Economics and Minister of International Trade and Industry Mohamed Azmin bin Ali shared an outlook that the administration of two million vaccination doses, necessary for the manufacturing industry, would be complete by the end of September thanks to the PIKAS program.

In terms of factors related to external markets, the key event is an FOMC meeting to be held on July 29, which would determine the trend of U.S. interest rates. At the previous FOMC meeting held on June 16, Federal Reserve Board (FRB) Chair Jerome Powell made a remark that the FOMC would start discussing the timing of monetary tapering. Thus, it is most likely that the FOMC will imply the timing of monetary tapering after summer, i.e., after the Jackson Hole Economic Symposium. However, market participants should be reminded that it is also possible for the FOMC to imply the timing of monetary tapering at the FOMC meeting on July 29, depending on the strength of the June employment statistics of the U.S. to be announced on July 2, as well as the CPI of the U.S. to be announced on July 13.

In terms of domestic factors other than the Covid-19 pandemic, S&P and Moody's both made announcements on the sovereign rating of Malaysia in June. S&P revised its estimated growth rate for 2021 from 6.2% to 4.1% with the expected impact of the FMCO introduced on June 1, while maintaining the outlook as "negative," pointing to persisting concerns over the government's debt balance. On the other hand, S&P expressed its intention to wait & see regarding the impact of the pandemic, although it commented about the maintained economic growth that would support the Malaysian economy. Therefore, it is unlikely for this to impact the market immediately. In terms of the political situation, a state of emergency was declared in January this year under the FMCO for the first time in approximately 52 years, and it is scheduled to end on August 1. Under the state of emergency, Parliament of Malaysia sessions were paused, but on June 16, King of Malaysia Abdullah of Pahang called for the reopening of Malaysia's parliament proceedings, and this triggered the government to immediately prepare for the reopening of parliamentary sessions. If the Parliament of Malaysia is reopened, it is easy to expect that opposition parties will severely criticize the measures taken for the Covid-19 pandemic under Prime Minister Muhyiddin Yassin, thus causing long-lasting impact on the Malaysian economy. In such a scenario, participants could expect a change of government, fueling concerns over the depreciation of the Malaysian ringgit based on instability in domestic politics.

Yu Tasai, Asia & Oceania Treasury Department

Indonesian Rupiah – July 2021

Expected Ranges	**Against the US$: IDR 14,200–14,800**
	Against 100 rupiah: JPY 0.75–0.79
	Against the yen: IDR 126.58–133.33

1. Review of the Previous Month

In June, the Indonesian rupiah remained stable at first and weakened thereafter.

On June 2, the U.S. dollar/Indonesian rupiah exchange market opened trading at around the IDR 14,300 level. On the same day, the May Consumer Price Index (CPI) of Indonesia was announced, and the result turned out to be +1.67% year-on-year, as had been estimated in the market. Thus, there was only minor market impact. While there were few important factors in the market, the U.S. dollar/Indonesian rupiah exchange rate continued fluctuating within a narrow range at around the IDR 14,300 level, partly because the announcement of the May employment statistics of the U.S. were scheduled for the end of the week, on June 5. However, the figures in the May employment statistics of the U.S. were not as strong as expected in the market, and this led U.S. interest rates to fall. As a consequence, the Indonesian rupiah remained strong on June 7 in the following week. Thereafter, the Indonesian rupiah remained strong. Then, on June 10, the May CPI of the U.S. was announced, in reaction to which market participants expected price inflation in the U.S. to be temporary, diminishing expectation for an early interest rate hike in U.S. monetary policy. On June 11, at the end of the week, the U.S. dollar/Indonesian rupiah exchange rate thus fell below the IDR 14,200 mark and reached its monthly high at the upper-IDR 14,100 level. In the following week commencing on June 14, the U.S. dollar/Indonesian rupiah exchange rate remained stable at the IDR 14,200 level.

However, in the second half of the month, on June 16, the outcome of a Federal Open Market Committee (FOMC) meeting was released in the U.S., fueling market attention to an early interest rate hike in the U.S. In reaction, the Indonesian rupiah depreciated against the U.S. dollar on June 17 from the IDR 14,300 level to approach the IDR 14,400 level. Under such circumstances, the central bank of Indonesia announced the outcome of its monetary policy committee meeting, as part of which the policy interest rate, the seven-day reverse repo rate, was maintained at the existing level. As this was already been anticipated in the market, there was only minor impact from this announcement on the Indonesian rupiah exchange market. On June 18, the following day, the Indonesian rupiah continued depreciating further against the U.S. dollar, and the U.S. dollar/Indonesian rupiah exchange rate reached the lower-IDR 14,400 level. In the following week commencing on June 21, the Indonesian rupiah continued gradually depreciating against the U.S. dollar, as Covid-19 cases increased significantly in Indonesia, while market participants continued expecting an early interest rate hike in the U.S. Then, on June 23, the Indonesian rupiah further weakened against the U.S. dollar, and the U.S. dollar/Indonesian rupiah exchange rate approached the IDR 14,500. Toward the end of the month, some market participants bought the U.S. dollar based on actual demand, keeping the Indonesian rupiah weak, and the U.S. dollar/Indonesian rupiah exchange rate remained at the IDR 14,400 level (based on the closing rate of June 29).

2. Outlook for This Month

The U.S. dollar/Indonesian rupiah exchange rate is forecast to weaken in July.

In June, in terms of U.S. monetary policy, market participants expected monetary tapering and an interest rate hike to occur earlier than previously expected, and this caused the persistent depreciation of the Indonesian rupiah. While Covid-19 vaccination advances steadily in the U.S. and its effect is becoming visible, economic recovery is likely to continue steadily. Market participants are thus aware of the normalization of monetary policy in the U.S., which would put downward pressure on the Indonesian rupiah. If the U.S. economic indices are announced with strong figures this month, the Indonesian rupiah is expected to depreciate further against the U.S. dollar. Market participants thus need to remain cautious about U.S. economic indices and remarks by important officials in the U.S. On the other hand, there is another worrying factor—the increase of Covid-19 cases in Indonesia. This has the potential to weaken the Indonesian rupiah while also delaying the country's economic recovery, and it could lead to the depreciation of the Indonesian rupiah from a long-term perspective, as it would create an imbalance between normalized monetary policy in the U.S. and the situation in Indonesia. In 2018, the Indonesian rupiah depreciated significantly, while the policy interest rate was repeatedly raised in the U.S. Market participants can be reminded that, at that time, the central bank of Indonesia followed the Federal Reserve Board (FRB) by also repeatedly raising interest rates even faster than the FRB. However, it was not possible to stop the Indonesia rupiah from depreciating. Back then, the domestic economic situation was not preventing interest rate hikes. However, this time, the situation is dramatically different. The Covid-19 vaccination program in Indonesia has been advancing at a much-slower rate than in the U.S., which makes it likely to slow down the recovery of economic activities in Indonesia. Under such circumstances, the central bank could be obliged to raise interest rates to protect the Indonesian rupiah. There are therefore concerns for the depreciation of the Indonesian rupiah to persist for a long time due to limited options for the central bank of Indonesia.

The Indonesian rupiah has been supported by the trade balance of Indonesia, which recorded a significant surplus again in May. While imports have been dramatically recovering, the increasing cases of Covid-19 in Indonesia could support a trade surplus. The trade balance is likely to continue supporting the Indonesian rupiah for a while. However, the key factor in the U.S. dollar/Indonesian rupiah exchange market has been shifting from the trade balance to economic recovery and monetary policy in the U.S. Thus, market participants need to remain cautious about the depreciation of the Indonesia rupiah for an extend period of time.

Yuichiro Sakaki, Manila Treasury Office, Asia & Oceania Treasury Department

Philippine Peso – July 2021

Expected Ranges	**Against the US$: PHP 48.00–49.50**
	Against the yen: PHP 2.20–2.32

1. Review of the Previous Month

In June, the Philippine peso recorded its highest rate in approximately five years, after which it depreciated significantly against the U.S.

At the beginning of the month, the Philippine peso appreciated sharply against the U.S. dollar, and the U.S. dollar/Philippine peso exchange rate once reached PHP 47.610 for the first time in approximately five years, as a result of the improving figure of the manufacturing PMI of the Philippines, as well as the sharp rise of Philippine stock prices that started at the end of May. However, the trend became inverted thereafter, and the Philippine peso started to depreciate against the U.S. dollar, as the Philippine government decided to maintain lockdown measures in metropolitan Manilla and its surrounding provinces, while the Brent crude oil price exceeded USD 70. After the Philippine peso reached its highest rate in five years, there were few market participants that bought the Philippine peso due to feeling cautious. As overall Asian currencies were being sold, the Philippine peso weakened, following the trend. Yet, when the employment statistics of the U.S. were released thereafter, the results turned out to be weaker than estimated, and U.S. interest rates fell significantly, leading to the overall depreciation of the U.S. dollar. As a result, the Philippine peso appreciated against the U.S. dollar again, and the U.S. dollar/Philippine peso exchange rate reached PHP 47.650, approaching the PHP 47.610 mark—the highest rate for the Philippine peso in approximately five years.

After seeing the impact of the employment statistics of the U.S., market participants were waiting for the announcement of the CPI of the U.S. that was to be announced on June 10. Under such circumstances, U.S. dollar-selling, which continued since the announcement of the employment statistics of the U.S., slowed down, encouraging market participants to buy back the U.S. dollar—a trend that dominated the market. At the same time, it turned out that the unemployment rate of the Philippines deteriorated, and the trade deficit was larger than expected in the country's trade balance. In negatively reacting to such headlines, the Philippine peso gradually depreciated against the U.S. dollar. Then, on June 10, the CPI of the U.S. was announced, and the result exceeded the market estimate. However, as market participants saw price inflation as a temporary phenomenon, U.S. interest rates fell, weakening the U.S. dollar in the overall foreign exchange market, which kept the Philippine peso strong.

However, on June 14, U.S. economic indices turned out to be strong, leading the U.S. dollar index to rise significantly. As a result, the U.S. dollar strengthened against overall Asian currencies. Also, foreign currency reserves in the Philippines decreased in May and this also pushed the Philippine peso to weaken against the U.S. dollar, and the U.S. dollar/Philippine peso exchange rate exceeded the PHP 47.80 mark, which had acted as a resistance line. U.S. interest rates continued rising, while the U.S. dollar also continued appreciating thereafter due to a cautious feeling in the market after a Federal Open Market Committee (FOMC) meeting in the U.S., the outcome of which was hawkish. Furthermore, the Philippine government announced its decision to extend the restrictions on movement and gatherings placed in metropolitan Manila and its surrounding four provinces until the end of the month. In negatively reacting to this news, the Philippine peso continued depreciating against the U.S. dollar, and the U.S. dollar/Philippine peso exceeded the PHP 48.00 mark. Then, the U.S. dollar continued to appreciate in the overall foreign exchange market after the surprisingly hawkish outcome of the FOMC meeting. Thus, on June 17, the Philippine dollar weakened significantly against the U.S. dollar, and the U.S. dollar/Philippine peso exchange rate reached PHP 48.380.

After the FOMC meeting, the outcome of which turned out to be hawkish, as mentioned above, the U.S. dollar continued to appreciate, and overall Asian currencies depreciated as a result. Following the trend, the Philippine peso also weakened, even though the Philippine stock market remained robust. On June 24, the Philippine peso weakened to its lowest level in approximately 10 months.

2. Outlook for This Month

The Philippine peso is likely to weaken in July.

As the policy interest rate outlook revealed at the previous FOMC meeting turned out to be more hawkish than expected in the market, U.S. interest rates rose while stock prices fell. Therefore, risk assets, which had been supported by excess liquidity, are likely to weaken in response to such circumstances. Market participants are thus expected to continue selling the currencies of emerging countries, leading the U.S. dollar to appreciate for a while.

While it is possible for risk assets to depreciate temporarily, it is not very likely for risk-averse sentiment to grow in panic, as the outcome about the tapering turned out to be rather dovish, offsetting the hawkish interest rate outlook. Thus far, there has been no specific plan for monetary tapering, and the start of the discussion was postponed, even though FOMC members expected an early interest rate hike. Therefore, the U.S. dollar/Philippine peso exchange rate is forecast to fluctuate mainly within a range between PHP 48.50 and PHP 49.00, hovering at around the PHP 48.80 level.

It is also worth noting that the central bank of the Philippines has maintained a moderate stance in order to prioritize constant economic recovery, even though the latest inflation rate has been above the target range, which is between 2% and 4%. On June 24, at its monetary policy committee meeting, the central bank decided to maintain the policy interest rate at the existing level. Thus, the Philippine peso is likely to depreciate against the U.S. dollar from a medium- to long-term perspective due to the differences in monetary policy between the U.S. and the Philippines.

Junya Tagawa, India Treasury Office, Asia & Oceania Treasury Department

Indian Rupee – July 2021

Expected Ranges	**Against the US$: INR 72.00–75.50**
	Against the yen: JPY 1.46–1.53

1. Review of the Previous Month

The U.S. dollar/Indian rupee exchange rate rose in June.

The U.S. dollar/Indian rupee exchange market opened trading at INR 72.555 in June. The exchange rate was low upon market opening, and this turned out to be the monthly low. While the number of Covid-19 cases started to decrease, the Indian stock price index renewed its all-time high. The net buy from foreign investors reached USD 198 million only within two business days at the beginning of the month. Market participants were expected to sell the U.S. dollar and buy the Indian rupee; however, at the same time, the central bank of India intervened in the market by buying the U.S. dollar and selling the Indian rupee, allegedly offsetting the transactions by foreign investors. Thus, the Indian rupee did not appreciate. On the contrary, there was downward pressure on the Indian rupee, as the foreign exchange market was impacted by rising crude oil prices. The U.S. dollar/Indian rupee exchange rate therefore continued fluctuating within a narrow range between INR 72.90 and INR 73.20 during the first and second weeks of the month.

In the third week of the month, it was confirmed that foreign currency reserves of India had renewed all-time highs, and this fueled speculation about U.S. dollar-buying and Indian rupee-selling interventions by the Indian monetary authorities. Furthermore, crude oil prices remained high, as the negotiation to revive the Iran nuclear deal had been prolonged, encouraging market participants to buy the U.S. dollar and sell the Indian rupee. The market was significantly impacted by the outcome of the Federal Open Market Committee (FOMC) meeting held in the U.S. on June 16, as the meeting turned out to be unexpectedly hawkish. In reaction, the U.S. dollar/Indian rupee exchange market opened trading on June 17 at INR 73.70, with the Indian rupee weaker by 30 paise against the U.S. dollar, compared to the previous day. On the same day, the U.S. dollar index reached its highest level in two months, leading the U.S. dollar/Indian rupee exchange rate to exceed the INR 74.00 mark.

In the fourth week of the month, the Federal Reserve Board (FRB) official mentioned the risk of inflation, which confirmed the content of the economic outlook released by the FOMC, leading the U.S. dollar to strengthen. Every day, the U.S. dollar slowly continued renewing its high, and the U.S. dollar/Indian rupee exchange rate reached its monthly high at INR 74.405 on June 22. Toward the end of the month, there were no more factors to impact the market, but the U.S. dollar/Indian rupee exchange rate remained high, with trading closing at INR 74.26 on June 29.

2. Outlook for This Month

The U.S. dollar/Indian rupee exchange rate is expected to remain high in July.

On May 28, the U.S. dollar/Indian rupee exchange rate was at INR 72.32, whereas it was at INR 74.405 on June 22, recording an increase of almost 2.9% within less than a month, which was a remarkable move that had not been seen for a while. One Asian currency index, which is an index for overall Asian currencies, declined by 1.9% in the same period, confirming that market participants sold not only the Indian rupee but also many Asian currencies. This is due to the fact that market participants preferred to buy the U.S. dollar, based on growing expectations for interest rate hikes in the U.S., as was discussed above. Indeed, the two-year U.S. government bond yield fell significantly, having seen the policy interest rate cut to near zero after the Covid-19 crisis last year. In February this year, the yield fell further to approach the 0.10% level. However, the yield rose sharply to temporarily reach 0.268% after the FOMC meeting held in June. It is understandable that some investment funds flew out from emerging countries, leading the currencies of emerging countries to depreciate.

It is also important to mention that the Indian rupee has depreciated by 2.9% while the Asian currency index mentioned above fell by 1.9%, making us wonder why the Indian rupee depreciated more than the Asian currencies of neighboring countries. This can be explained by the rise of crude oil prices, which rose by 50% compared to the beginning of this year, and even in June alone, the price rose by almost 10%. Also, 85% of the domestic demand of India depends on imports, and therefore the rise of crude oil prices leads directly to U.S. dollar-buying and Indian rupee-selling. Furthermore, the current account deficit of India has grown due to the expanding trade deficit, which has occasionally been encouraging foreign investors to sell the Indian rupee. Thus, the rise of crude oil prices is a negative factor for the Indian rupee for several reasons. From this standpoint, market participants can be reminded of the U.S. dollar/Indian rupee exchange market in 2018, when crude oil prices also rose sharply.

It is necessary to carefully observe the impact of the July employment statistics and the price indices of the U.S. on U.S. monetary policy outlook. However, the dot plot was modified at the FOMC meeting in June, making it difficult for expectations for an interest rate hike to diminish, as they did in May. If crude oil prices remain high, as currently, the U.S. dollar/Indian rupee exchange rate is expected to also remain high.

This report was prepared based on economic data as of July 1, 2021.