



بنك الإمارات دبي الوطني
Emirates NBD

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FX Week

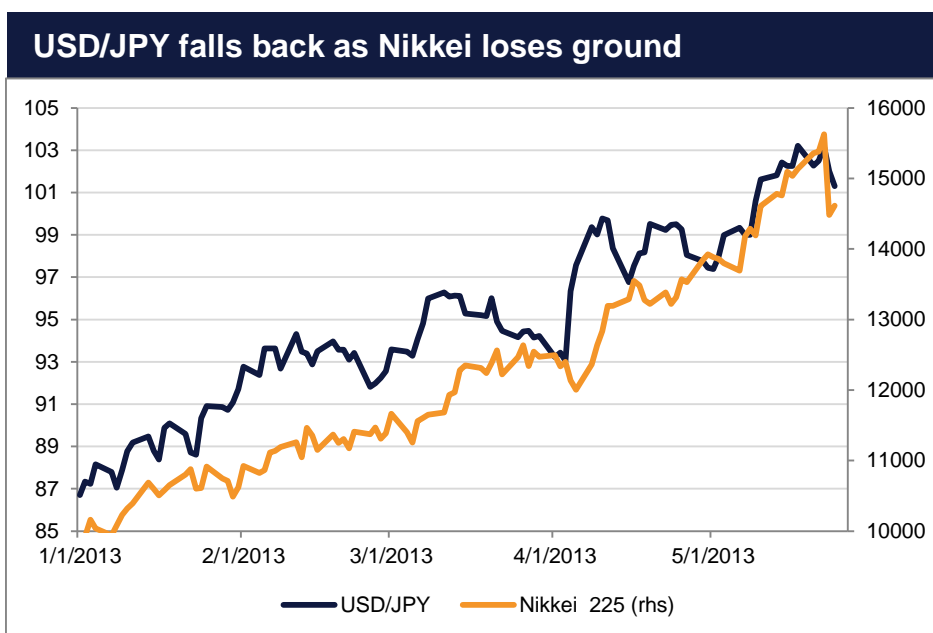
Focus returns onto the JPY

FX markets have rotated their focus on to the JPY over the past few days, as extreme volatility in Japanese asset markets has raised questions about the future of 'Abenomics'; prompting liquidation of some short JPY positions. USD/JPY ended the week at 101.30, down from the highs of 103.70 reached on Wednesday morning. In the coming week, the JPY is likely to remain the centre of attention as the BOJ seeks to reassert itself over the JGB bond markets and thereby restore stability to the Nikkei as well as to the JPY.

The Nikkei plunged by 7.8% on Thursday, and although it recovered modestly on Friday, markets will be looking for more direction from the BOJ Governor Kuroda after he downplayed market movements in his press conference last week. On Friday Kuroda said that he wants to avoid volatility in bond markets and that the BOJ has announced sufficient monetary easing, also saying that he does not have targets for stocks or for the Nikkei. His comments came as the BOJ stepped into the market to buy government bonds for a second consecutive day. Earlier today Kuroda went further by saying that increases in bond yields should reflect economic expectations, saying that rising yields would be negative if they are not based on genuine economic hopes.

With global factors partially responsible

Putting the recent volatility into some context, last Thursday's moves came against a backdrop of renewed uncertainty over US monetary policy, as well as signs that the Chinese recovery was losing steam. In particular Fed Chairman Bernanke appeared on Wednesday to be hinting at the possibility of some reduction in QE being announced 'in the next few meetings'. Fed minutes released the same day also failed to dispel the notion that asset purchases could begin to be 'tapered' over coming months. Global equity markets reacted negatively to these messages, however, and it is perhaps not surprising that Japanese markets, which have risen by the most in recent months (up around 50% since the start of the year), reacted the most negatively. Even after the 7.8% sell-off the Nikkei is still up 67% since last November, suggesting that the adjustment should still be seen as more of a correction than a change of trend.



Source: Bloomberg, Emirates NBD Research

...As well as concerns about JGBs

At the same time the BOJ, after its monetary meeting on Wednesday, also gave the impression of being relatively sanguine about the recent rise of JGB bond yields, which have shot up from 0.4% to almost 1.0% since the BOJ announced its monetary policy revolution on April 4th. While rising bond yields might be the natural consequence of a successful QE program, if it results in higher growth and rising inflation, it appears that markets might have gotten ahead of themselves in Japan's case, as deflation remains very much entrenched despite some promising signs of growth in Q1. This is presumably what Kuroda was alluding to in his comments today, also stating that the intention of Japanese monetary policy is to lower the yield curve and risk premiums. In the short term it would be more natural in our view for long-term interest rates to remain anchored at lower levels as a result of the BOJ's commitment to double the purchases of JGBs each month, with any sustainable rise in yields having to await signs of a genuine turn in inflationary trends. As this might not happen for some time, we think that the rise in yields is vulnerable to a correction. Likewise, the sell-off in the Nikkei probably also looks a little overdone, especially as the global markets may have misinterpreted the speed with which the Fed might begin to wind-down QE.

Upcoming Japanese inflation data will be important

April inflation data will be released for Japan in the coming week and another disappointing outcome (last month deflation was running at -0.5%) could see Japanese markets bounce higher if further QE steps from the BOJ begin to be anticipated. The JPY is likely to react negatively, spurring Nikkei gains, while the prospect of more BOJ bond buying should halt the uptrend at least in yields. Of course if there is a surprise easing of deflationary pressures, then the likelihood is that the uptrend in yields could continue, further undermining stocks and causing the JPY to strengthen.

Fed's QE withdrawal in play in H2

As touched upon above, the markets may also have misinterpreted the Fed's intentions with regard to QE, although after the mixed messages from the Fed's minutes it is easy to understand why. Certainly the Fed did not completely dispel the notion that QE 'tapering' could begin soon, although the greater likelihood is that such a process will have to wait until much later in the year. The minutes of the last FOMC meeting showed that a 'number of participants' could support adjusting asset purchases downward as early as June, provided data showed 'sufficiently strong and sustained growth'. This was the first time that June has been specifically mentioned. However, 'many' wanted to see more evidence that the economy really is strengthening sustainably before tapering the rate of purchases, and 'views differed' about what evidence would be necessary.

EUR – awaiting policy clues

On the US data front, it will be a relatively quiet week, with consumer confidence, personal income, the Chicago PMI index and a Q1 GDP growth revision the main events. The week will also begin slowly with a Memorial Day bank holiday on Monday in the US and a bank holiday in the UK on the same day as well. The USD may remain on the defensive during the early part of the week as markets continue to mull the various messages from policymakers over the past week, and perhaps adjust their outlook for the Fed a little. While the focus on the JPY will remain intense, the EUR appears to be drifting as markets await more data and perhaps more clues about what the ECB can and will do next. Data released last week showed a slight uptick in activity in the Eurozone during May, but not enough to counter the likelihood of another overall contraction in Q2. The survey data in the coming week should reinforce this probability, but for the time being the ECB still seems unlikely to ease

policy again next month.

GBP continues to struggle

GBP meanwhile is struggling, with UK data released last week dispelling hopes that the rebound of Q1 will continue into Q2. Softer than expected inflation, along with very weak retail sales and poor public finance data in April have renewed the focus on the UK's underlying weak fundamentals. Although the minutes of the last MPC meeting were unchanged at 6:3 against expanding asset purchases, the odds are improving that by the time the next Governor Mark Carney arrives in July, the case for easing again will be much more clear. GBP/USD traded close to our 1-month forecast of 1.50 last week, and although it rebounded on Friday as the USD lost ground, its underlying direction remains biased downwards.

AUD weakness pronounced, and welcome

The AUD was the other big casualty of last week, losing out as Chinese manufacturing activity data worsened, and reflecting the possibility that the RBA could cut interest rates further. Chinese data will therefore be watched again closely this week when the official manufacturing PMI reading will be released. Should this also drop into contraction territory in May, as the HSBC/Markit version did last week, then the AUD will continue to soften. Markets will also be on the lookout for signs of weakness in Australia's quarterly capital spending report, as this could renew concerns that the country's mining investment boom could be coming to an end. With commodity prices remaining vulnerable and RBA monetary policy risks tilted towards further easing, the AUD has a number of pressures to contend with. A weaker exchange rate is probably even preferred by the Australian government, which has been protesting about its overvaluation for some time. In an environment in which payroll costs have been rising, a weaker AUD is a relatively painless way of improving competitiveness, as other governments have recently found.

CHF – not to be left behind

Final mention this week should be made of the CHF, following comments from SNB President Jordan last week that the EUR/CHF 1.20 cap could be adjusted if necessary. He also seemed to allude to the possibility of introducing negative deposit rates, as recommended by the IMF last week, and as deployed by other countries previously. The motivation behind such remarks might be related to the fear of being left behind in a devaluation race with the Bank of Japan, although the CHF actually ended the week stronger, at EUR/CHF1.24, as safe haven flows overrode all other concerns on Friday. Over time, however, as markets stabilize again, the CHF should be vulnerable to such rhetoric. Furthermore, the comments reinforce the prevailing bias towards easier monetary policy in Europe, and to that extent should further serve to bolster the USD at its and other currencies' expense

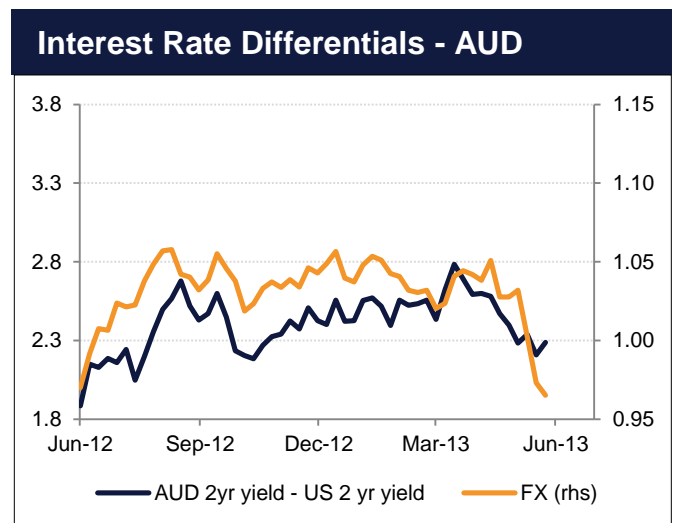
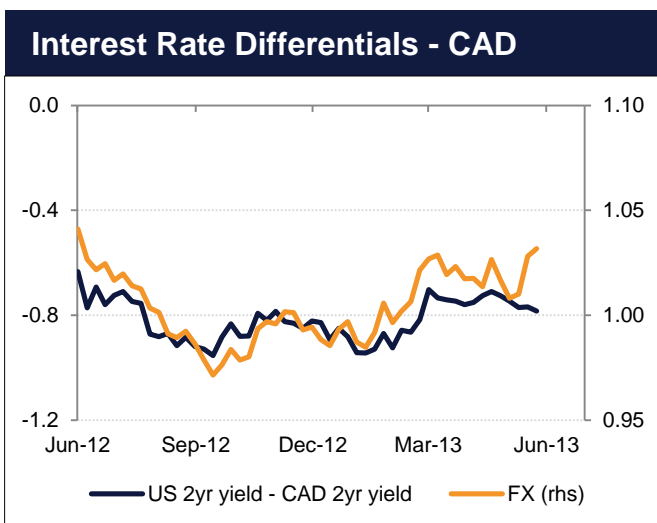
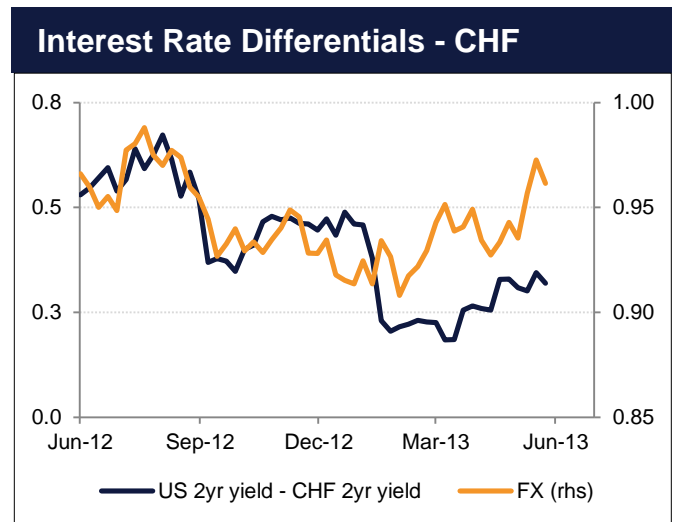
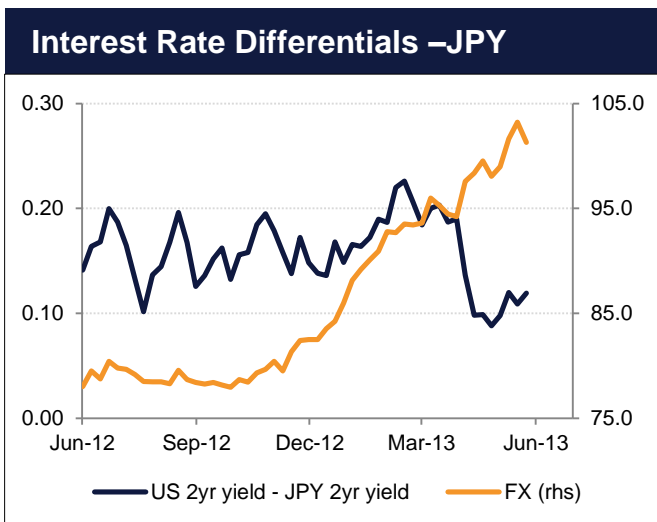
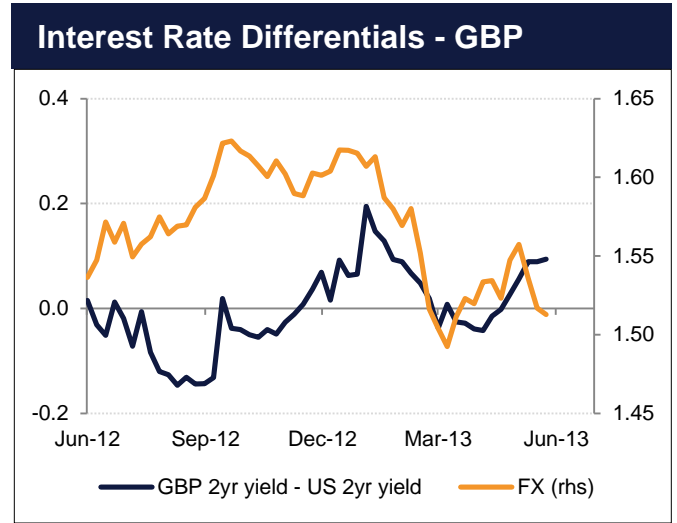
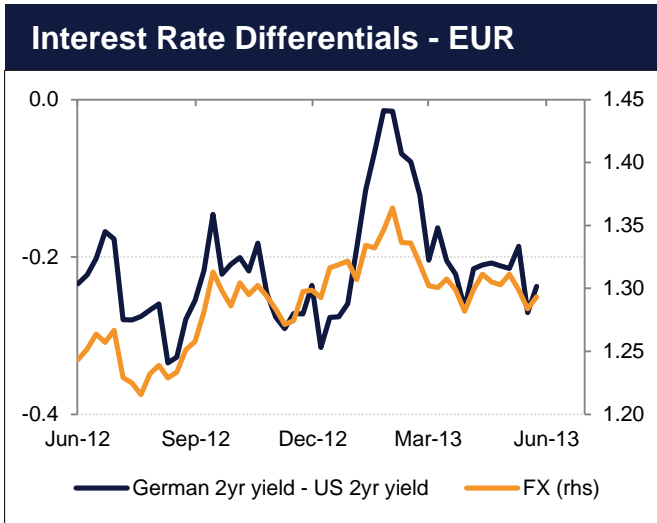
FX Forecasts - Major						Forwards		
	Spot 24.05	1M	3M	6M	12M	3M	6M	12M
EUR / USD	1.2932	1.27	1.25	1.20	1.15	1.2939	1.2949	1.2972
USD / JPY	101.31	103.0	105.0	107.0	110.0	101.26	101.19	100.97
USD / CHF	0.9615	0.98	1.00	1.04	1.08	0.9606	0.9595	0.9568
GBP / USD	1.5127	1.50	1.48	1.45	1.45	1.5118	1.5112	1.5105
AUD / USD	0.9652	0.98	0.97	0.94	0.90	0.9590	0.9531	0.9420
USD / CAD	1.0318	1.03	1.05	1.07	1.10	1.0341	1.0363	1.0407
EUR / GBP	0.8551	0.85	0.84	0.83	0.79	0.8561	0.8571	0.8590
EUR / JPY	131.01	131.0	131.0	128.4	126.5	131.01	131.01	131.01
EUR / CHF	1.2433	1.24	1.25	1.25	1.24	1.2428	1.2423	1.2410

FX Forecasts - Emerging						Forwards		
	Spot 24.05	1M	3M	6M	12M	3M	6M	12M
USD / SAR*	3.7503	3.75	3.75	3.75	3.75	3.7504	3.7503	3.7503
USD / AED*	3.6730	3.67	3.67	3.67	3.67	3.6730	3.6730	3.6728
USD / KWD	0.2861	0.282	0.285	0.282	0.28	0.2870	0.2880	0.2887
USD / OMR*	0.3850	0.38	0.38	0.38	0.38	0.3848	0.3845	0.3845
USD / BHD*	0.3770	0.376	0.376	0.376	0.376	0.3774	0.3780	0.3785
USD / QAR*	3.6409	3.64	3.64	3.64	3.64	3.6429	3.6447	3.6484
USD / INR	55.6450	53.50	53.00	52.00	51.00	55.6536	55.6619	55.6781
USD / CNY	6.1328	6.23	6.22	6.20	6.25	6.1867	6.1968	6.2287

*Denotes USD peg

Source: Bloomberg, Emirates NBD Research

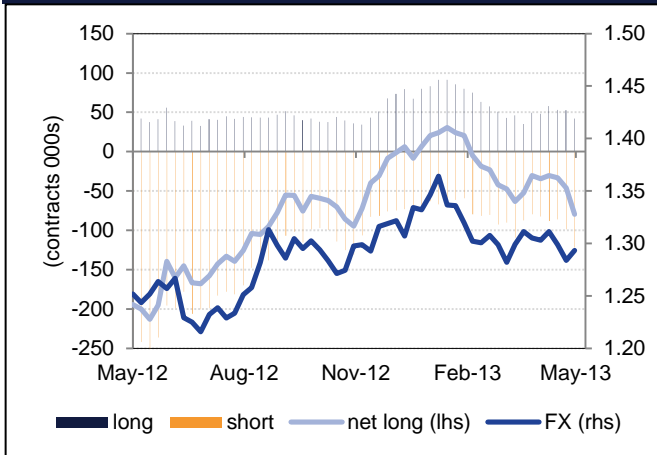
Major Currency Pairs and Interest Rates



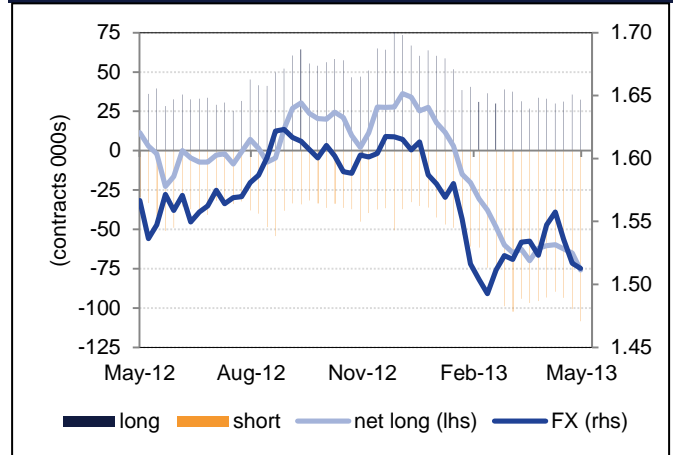
Source: Bloomberg, Emirates NBD Research

Major Currency Positions

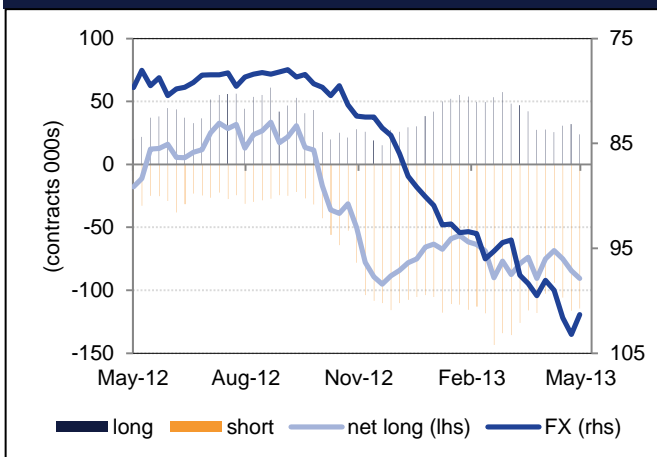
CFTC – Speculative Positions - EUR



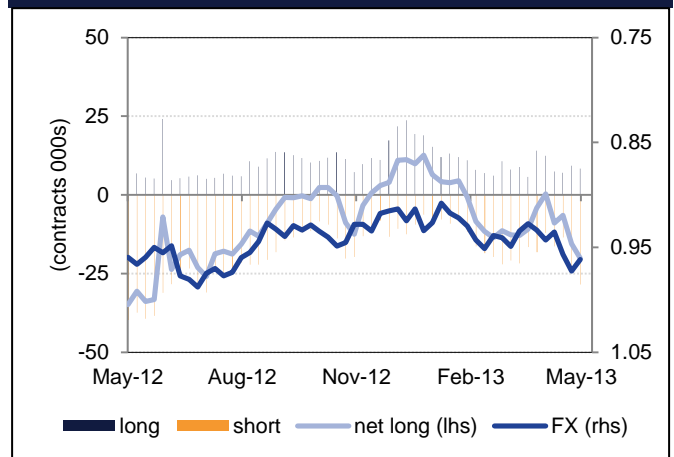
CFTC – Speculative Positions - GBP



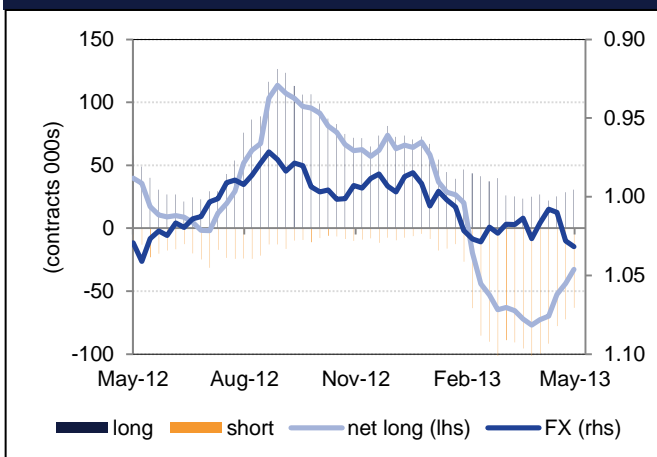
CFTC – Speculative Positions - JPY



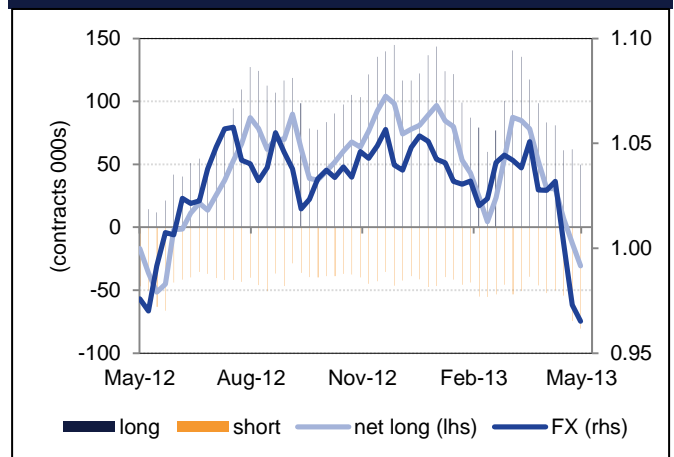
CFTC – Speculative Positions - CHF



CFTC – Speculative Positions - CAD



CFTC – Speculative Positions - AUD



Source: Bloomberg, Emirates NBD Research

Economic Calendar

Date	Country	Event	
28-May	Switzerland	Trade Balance	
	France	Consumer Confidence Indices	
	US	S&P/CaseShiller Home Price Index	
	US	Richmond Fed Manufacturing Index	
	US	Dallas Fed Manufacturing Index	
29-May	Japan	Retail Trade	
	Germany	CPI	
	Germany	Unemployment Rate	
	Italy	Business Confidence	
	UK	CBI Reported Sales	
	Brazil	GDP	
	Canada	Bank of Canada Rate	
	Brazil	SELIC Target - Central Bank	
	30-May	Switzerland	GDP
UK		Nationwide House Prices	
Eurozone		Economic Confidence	
US		GDP	
US		Personal Consumption	
Canada		Industrial Production	
US		Initial Jobless Claims	
US		Pending Home Sales	
31-May		UK	GfK Consumer Confidence Survey
		Japan	Jobless Rate
	Japan	CPI	
	Japan	Industrial Production	
	India	GDP	
	Germany	Retail Sales	
	France	Consumer Spending	
	UK	Mortgage Approvals	
	Eurozone	CPI	
	India	Fiscal Deficit	
	Canada	GDP	
	US	Personal Income/Spending	
	31-May	US	PCE Core
US		U of Michigan Confidence	

Source: Bloomberg

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