FX

Global

FX Note

How High Will USDJPY Go?

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USDJPY Climbing Back Up

In the last couple of weeks, the USDJPY has been moving up after having recently experienced a period of quite heavy decline. After having briefly just broken below the 140.00 level around mid Sep, the pair has climbed back up and look to be testing the 150.00 level. The question now is whether the pair can on a sustained move upwards.

Bullish Positioning was Too Stretched but Currently Looks More In Line

As a start, we need to first understand what has actually driven the fall in the pair before this rebound occurred. The fall in USDJPY since Jul had been due in essence to a macro shift of which the Fed has now pivoted to embark on a rate easing cycle with the first cut of 50bps coming in Sep. At the same time, the BOJ has also been engaging on a tightening cycle as they exited negative interest rates and scaled down their bond purchase programs. US – JP yield differentials therefore were turning increasingly more favorable to the JPY. Back in Jul, speculative positioning for JPY was extremely stretched on the bearish side as the CFTC net short positioning was at its most extreme levels in years. When macro conditions turned, we saw a very rapid unwind of these short positions. Positioning would then turn to be very bullish.

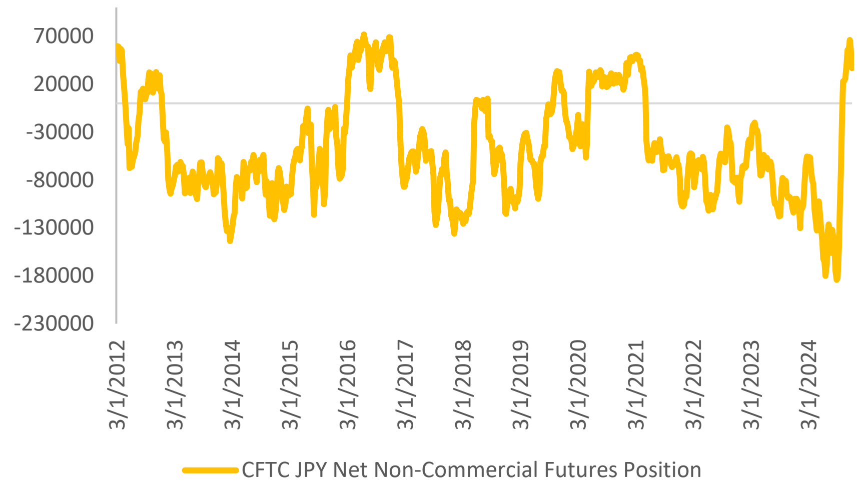
This bullish positioning data can be important somewhat in helping to imply the extent to which USDJPY can still climb further. By end Sep, the net CFTC positioning had shown that bullishness had climb to a level not seen since 2016. Whilst we do believe that conditions are favorable in the medium term for USDJPY to head lower, there is little reasonable justification for fast money to be this bullish given short term conditions. In the near term, there are few developments just yet that can actually support further moves downwards in USDJPY and such strong JPY bullishness. The Fed may have already embarked on an easing cycle but for now the pace of it is still very uncertain pending how US data evolves. Also, new PM Ishiba himself had stated support for an accommodative BOJ monetary policy whilst Ueda has recently sounded somewhat less hawkish. US – JP yield differentials may not turn sufficiently favorable fast enough to allow for substantial JPY gains so soon.

Some of the bullish positioning has already come off during the first week of Oct and there is reason for us to believe that it has fallen further in the second week given the climb in USDJPY. In some sense, bullish positioning now looks more in line with macro conditions. Even so, we would be wary as speculative positioning can have a tendency to overshoot. Regardless, positioning at this point implies that upside for USDJPY is more likely limited. As a note, 1M risk reversals at the same time are indicating bullishness.

How would the Near Term Macro Background Fare for the JPY?

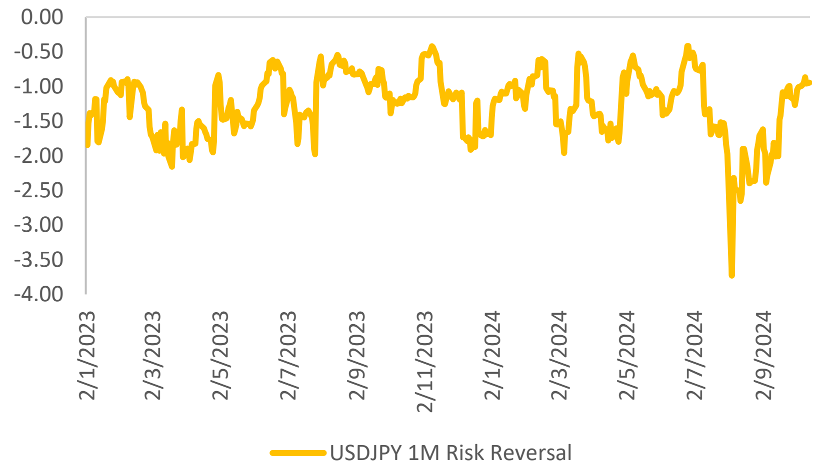
In the near term, it is difficult to expect the macro environment to turn significantly favorable for the JPY so soon and in some sense risks instead tilt to some further upside for USDJPY. The possibility of only a slow softening in US data is likely to keep market anxious whilst Fed officials may likely be supportive of a gradual pace of easing. Fed Fund Futures and OIS still imply a good probability of a 25bps cut but the possibility of market overshooting on the hawkish side can see the probabilities

Chart 1: The Highly Bullish Positioning Has Recently Come Off



Source: Bloomberg, Maybank FX Research & Strategy

Chart 2: Risk-Reversals Imply Higher Expectations for the Pair to Climb Higher



Source: Bloomberg, Maybank FX Research & Strategy

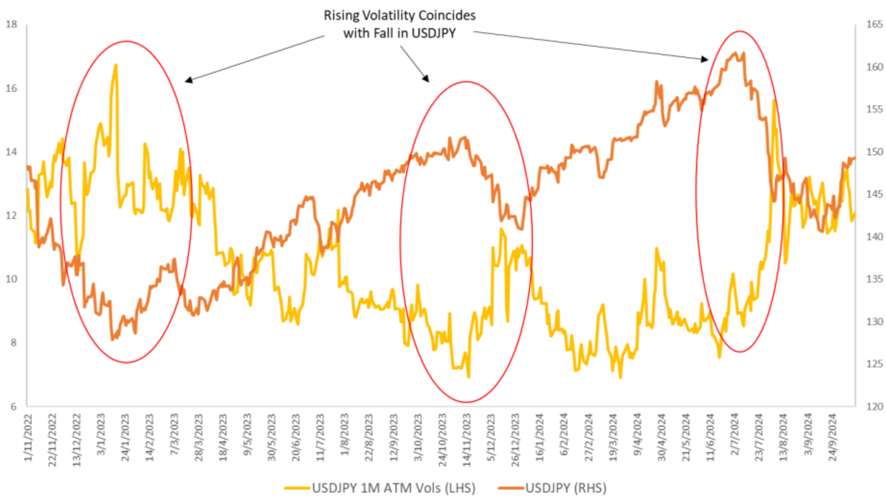
pare back further. Any hike by the BOJ also looks less likely this month given that the central bank may continue to await further data before making any additional moves. Real wage growth had recently again turned negative whilst there is a risk for CPI readings to slow near term (even if we expect it to pick-up again towards year-end). The BOJ would also likely want more time still to assess the impact of the monetary adjustments made so far.

We would do like to mention that there are other domestic factors that would limit the USDJPY upside. This includes that the government may become uncomfortable with the JPY depreciating too quickly. From the recent low on 16 Sep 2024 until 11 Oct 2024, USDJPY itself had climbed by about 6.05%. In comparison, before the suspected intervention on the 22 Sep 2022, the USDJPY had risen by about 8.10% from the start of Aug until then. Before another potential intervention on 29 Apr 2024, the USDJPY had risen by about 7.74% from its then recent low on 11 Mar 2024. So far though, we can say that there has not really been much strong jawboning from the Japanese government officials. Finance Minister Katsunobu Kato has recently expressed concerns about the sharp JPY movements as he pointed out that it can have a negative impact on business activity and citizens' lives. We do note that the current environment does differ quite significantly from other intervention episodes in the last three years given that we are now in a rate easing environment compared to being in a tightening cycle previously.

Can the Carry Trade Build Up Significantly Again?

We think there is a lower possibility of this happening for a few reasons. The first reason is that the macro environment over the medium term is much less supportive of this given that the policy divergence is more in favor of the JPY given the Fed is on an easing cycle whilst the BOJ is tightening. More importantly though, periods of heightened volatility in JPY actually deters investors from engaging in the carry trade. Historically, in the last few years we have notice that the higher volatility in USDJPY has coincided with a decline in the pair. At this point, USDJPY volatility can be considered at being at a more elevated level compared to the past.

Chart 3: Rising Volatility Coincides with Declines with USDJPY and can Deter the Carry Trade



Source: Bloomberg, Maybank FX Research & Strategy

Cautious on the Technicals

The possibility of breaking above the 150.00 resistance cannot necessarily be ruled out. The RSI at this point is not quite at overbought conditions yet and does highlight the possibility of further upside. However, the MACD and the stochastic do look like it is stretched on the upside. A break of the 150.00 resistance level would open the way for the pair to test the 152.00 mark (key psychological level that USDJPY failed to break on multiple occasions except in Apr 2024). Support is around 145.20 (200-dma) and 140.00. Pattern wise, an inverted head and shoulders looks to have formed with a neckline at around the level of 149.00 and a break of that level may imply a further climb higher. Even so, we are not inclined to believe that this technical charting pattern can necessarily play out given that bullish positioning has already come off quite a bit and the possibility of Japanese government concern on currency weakness. Overall, we stay cautious regarding the technicals.

Chart 4: Cautious on the Technicals

Source: Bloomberg, Maybank FX Research & Strategy

Conclusion: Near Term, Upside Risks but Downward Medium Term Trend Intact

In the near term, we are cautious on both the macro environment and the technicals being more supportive of further upside for the USDJPY. However, we are also aware that speculative bullish positioning may have already come off a lot and that would limit the upside gain for USDJPY. Concerns expressed by the Japanese government on any rapid rise in the USDJPY can also keep markets at bay.

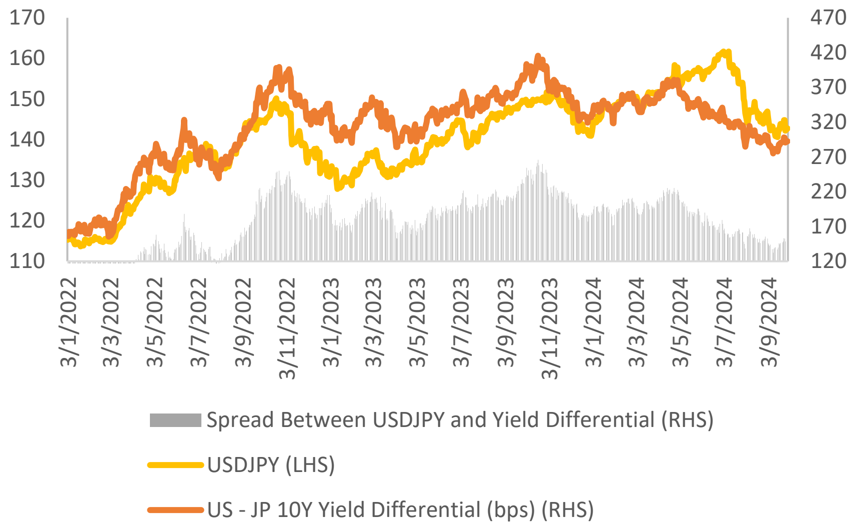
In the medium term, we continue to stick to our forecast seeing that the USDJPY would head lower over time. We expect that the USDJPY can likely encounter some turning point towards year end with the Japanese elections completed and US data continuing to soften. Japanese PM Ishiba (likely to retain his position) can potentially sound less dovish after the elections are done given that he could have been trying to avoid market volatility during the campaign. Ueda may also lean more supportive of tightening towards year-end especially as inflation data could again pick-up more by then after the utility subsidies period is over. Wages we believe would also continue to grow at a robust pace, feeding into more demand driven price pressures. Therefore, we see that the BOJ would hike by 25bps in Dec 2024. Into 2025, the possibility of continuing growth in corporate profits and wages in addition to inflation edging higher can allow for the BOJ to hike further. We see the central bank moving by 25bps possibly in Jun 2025 and another time by the same amount in Dec 2025, which would bring the rate to 1.00%. Most importantly, we think market would grow more confident of a Fed easing cycle becoming more entrenched in time especially as US data continues to soften allowing for a Fed cut of 25bps each in Nov 2024 and Dec 2024 (as forecasted by our economist). This can help guide UST yields lower from current levels, which in our view is already starting to factor too dovish an expectation of the Fed. Our economist sees 125bps of Fed cuts next year and that should help continue to guide USDJPY lower.

Table 1: USDJPY Forecasts

Forecast	4Q 2024	1Q 2025	2Q 2025	3Q 2025
USDJPY	138.00	136.00	134.00	132.00

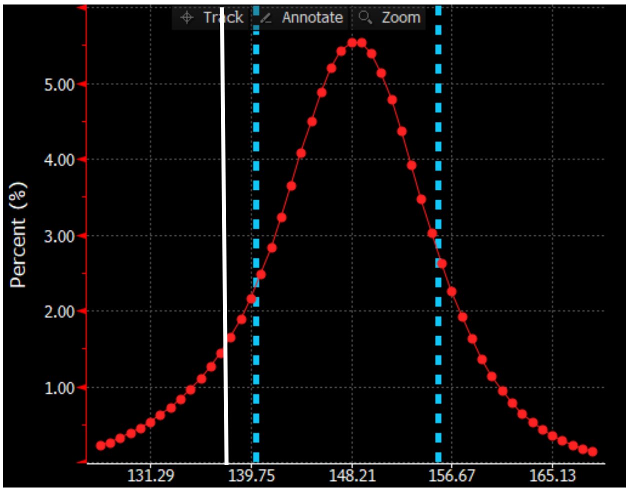
Source: Bloomberg, Maybank FX Research & Strategy

Chart 5: USDJPY Would Edge Lower Over Time as Together with Narrowing US - JP Yield Differentials



Source: Bloomberg, Maybank FX Research & Strategy

Chart 6: Options Implied Market Expectations of the USDJPY for 4Q 2024



Source: Bloomberg, Maybank FX Research & Strategy
Note: White line indicates our 4Q 2024 forecast at 138.00

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