Daiwa Securities

Daiwa's View

Will USD/JPY rate exceeding Y150 spur currency intervention?

- War of nerves between market and government/BOJ

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Will USD/JPY rate exceeding Y150 spur currency intervention?

War of nerves between market and government/BOJ

◆ USD/JPY rate reached Y150 amid caution about intervention

Yesterday, the USD/JPY rate finally crossed the Y150 mark. In the forex market, the sense of caution about intervention (incl. the possibility of stealth intervention) was strong. Before the announcement of the middle rate in the Tokyo market, the rate rose to the Y149.9 level. Thereafter, the rate traded in a very narrow range for several hours. Then, when the rate temporarily rose to Y150.08 at around 16:40, it stayed at the Y150 level for a short span of time before returning to the Y149 level. However, the USD/JPY rate tested higher levels once again during New York trading hours in line with rising US yields, rising to Y150.29. Since last week's release of hotter-than-expected US September CPI on 13 October, the market has increasingly factored in a 75bp rate hike at the December FOMC meeting, which is raising market projections for the terminal rate to 5%.

With regard to the USD/JPY rate exceeding Y150, Minister of Finance Shunichi Suzuki said that he would decline to comment on the level, but did state that the authorities could not tolerate excessive and rapid changes by speculators. He also said that there was no change to the authorities' stance of taking resolute measures when there were excessive fluctuations, including those by speculators, emphasizing that the authorities would continue to closely monitor trends with a sense of urgency. Later, Deputy Finance Minister Masato Kanda commented that the authorities were always ready to take necessary action in situations in which excessive fluctuations are not to be tolerated. He also stated that there were unlimited resources for conducting yen-buying intervention.

Although the USD/JPY rate topped Y150 at one point, it has no further upward momentum. This could be interpreted as meaning that smoothing intervention is having an effect. Looking back on the intervention on 22 September, it was conducted after the USD/JPY rate was fixed at the Y145 level and rose to slightly below Y146, not immediately after exceeding Y145. This time, as well, it is possible that intervention will be conducted after the rate has become fixed at the Y150 level. Market participants who are aware of this possibility may not be able to test higher levels carelessly. In any case, given the current US yield levels, we think that the USD/JPY rate will naturally begin to move towards the Y150-155 range. Accordingly, the rate is likely to test higher levels amid caution about monetary intervention.

◆ Yen selling caused by real demand to continue for the time being

According to the September trade statistics released yesterday by the MOF, the trade balance came in at -Y2,094.0bn, the 14th consecutive monthly deficit. In 1H FY22 (Apr-Sep), the trade deficit reached Y11,007.4bn, the largest half-term deficit since FY1973. Many believe that the USD/JPY rate was pushed to a 32-year high due to yen selling caused by real demand in light of the trade deficit (Chart 1). It is said that importers have been buying the dollar (incl. knock-out currency options) in October also, amid dollar buying that has seen the USD/JPY rate rise from the Y145 level to the Y150 level.

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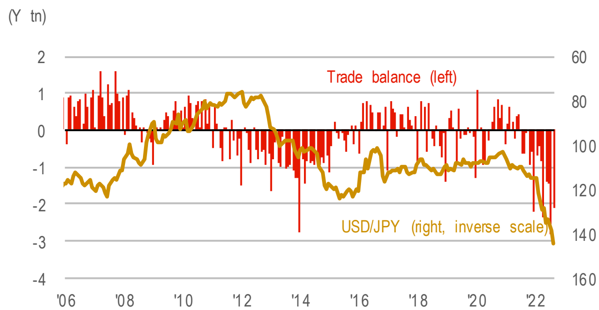
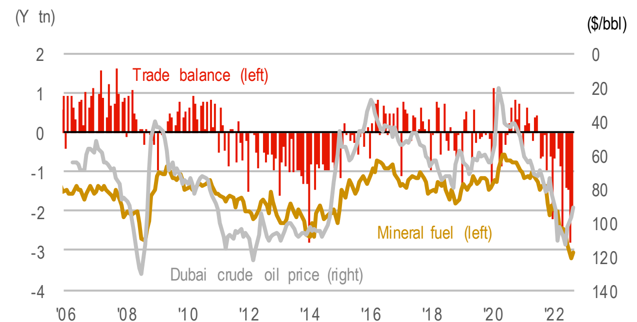
Chart 1: Trade Balance, USD/JPY Rate



Source: MOF, Bloomberg; compiled by Daiwa Securities.

Chart 2: Trade Balance, Crude Oil Prices



Source: MOF, Bloomberg; compiled by Daiwa Securities.

Meanwhile, on a seasonally adjusted basis, the September trade deficit, although large at Y2,009.8bn, was smaller than that in July and August. While exports were given a boost because of higher costs (caused by the weaker yen and higher commodity prices) being passed onto export prices, imports are showing signs of hitting a ceiling. The price of Dubai crude oil, which had risen to nearly $100 in June 2022, has already peaked out. It has now dropped to around $90. With the drop in crude oil prices lowering the price of imported mineral fuel, after a time lag, this is expected to lead to improvement in the trade balance (Chart 2).

That said, it is highly likely that a large trade deficit will continue to be booked for the time being. Dubai crude oil prices had dropped to the $80 level at one point because of caution about weaker demand due to a slowdown in the global economy. However, oil prices are rising once again, reflecting the decision by OPEC+ to make a substantial cut in output. In addition, if we see drastic economic deterioration mainly in Europe and the US, exports are likely to face downward pressure. Even if the trade deficit peaks out, in terms of supply/demand conditions, we are unlikely to see a change in the current situation with a lot of yen selling taking place.

In terms of supply/demand conditions, the Japanese government substantially eased border control measures on 11 October. Specifically, the ban on individual tourists was removed, short-term visitors are no longer required to obtain visas, and the upper limit on the number of people allowed to enter Japan in one day was lifted. These measures are expected to give a strong boost to the recovery of inbound demand. The Japanese government appears to have now implemented most of the measures for recovering inbound demand, but the recovery may be moderate due to prolonged overseas COVID-19-related restrictions, particularly China's Zero-COVID policy.

Regarding this point, Bloomberg reported yesterday that Chinese officials were debating whether to reduce the mandatory quarantine period for people entering China. If China eases border control measures, this will likely serve as a tailwind for the recovery of inbound demand. A turnaround in China's Zero-COVID policy is anticipated around March 2023, when the National People's Congress is to be held. Therefore, there could be a full-scale recovery of inbound demand in the latter half of 2023 or in 2024. It will take some time before the resumption of inbound demand substantially improves supply/demand conditions in the yen market. However, this is important in the sense that Japan's economy will benefit from the weaker yen, so we should keep an eye on this.

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