Market Comment_30Nov2022

Protests against Covid controls erupt across China. The yen has been strong recently.

1.Fed minutes are "dovish", and the US dollar and US stocks are "rangebound" sideways.

The minutes of the Federal Reserve's November Federal Open Market Committee (FOMC) meeting, released in the early hours of last Thursday (24 November), show that "slowing the pace of interest rate hikes" has basically been the consensus among officials with the overall bias being "dovish". At the moment, the biggest conflict plaguing the market is the Fed's policy of "slowing the pace of rate hikes but keeping rates high for a longer period" and what the terminal rate will be. The current "range-bound" pattern in most financial markets may indicate that investors' expectations that the Federal Reserve may raise interest rates to 5% have been fully absorbed by the market. And what impact could a real rise from the current 4% benchmark rate to 5% (or 6%) have? Over the past six months, the risk aversion brought about by the Fed's "aggressive rate hikes" may have ended, with more and more "USD-longs" taking profits and exiting the market. This is the reason for the softness of the US dollar over the past two months. The US Dollar Index has been oscillating in a narrow range between 105.00-106.00 on the low side after the release of the minutes. Technically, a subsequent drop below 105 could trigger a more significant decline. If it holds steady at 105.00, it could restart a rally. Highlights of the Fed's November meeting minutes are as follows.

1) *At the November monetary policy meeting, a substantial majority of participants judged that a slowing in the pace of increase would soon be appropriate. Some Fed officials would like to see more data before the pace of rate hikes slows. Given the lag in the impact of monetary policy, a "slower pace of rate hikes" would better allow the Fed to assess progress towards its goals. A slower pace of rate hikes would reduce risks to the financial system, and a slowdown in the economy should await more progress in cooling inflation.*
2) *As monetary policy approached a sufficiently restrictive level, participants stressed that the federal funds terminal rate became more important than the pace. A more restrictive policy is consistent with risk management, and the risk of excessive tightening rises.*
3) *Participants agreed that there were fewer signs of upward inflationary pressures. Participants generally noted that risks to the inflation outlook remained tilted to the upside.*

4) *All participants agreed that November's 75 basis point rate hike would be appropriate.*
5) *There is significant uncertainty about the terminal rate needed to curb inflation, with the terminal rate seen as higher than previously expected.*
6) *Labour markets remain tight, with initial indications that the economy may slowly move towards a better balance between supply and demand.*
7) *Despite signs of tight liquidity conditions and increased interest rate volatility, the US Treasury market continues to function in an orderly manner.*

Investor confidence in the Fed's overall monetary policy shift has increased significantly. If inflation continues to fall, the terminal rate could be lower than previously expected, and interest rate markets are revising the "terminal rate" for the Fed's rate hike path significantly. The Fed's policy rate is expected to reach 4.875% by May 2023, down from the 5.135% forecast following the November Fed meeting. On Monday (28 November), a number of Federal Reserve heavyweights made "hawkish" remarks, "Fed needs to reach at least the bottom of the 5% to 7% range ", giving the dollar a small boost.

1) *St. Louis Fed President Bullard: "An inverted yield curve is not necessarily signaling a recession; the Fed needs to raise rates to the bottom of the 5%-7% range and will continue to raise rates through 2023, to reach deflation in 2023; the market slightly underestimates the possibility of more aggressive rate hikes by the FOMC to curb very high inflation. "*
2) *Fed Vice Chairman Brainard: "In the context of increased uncertainty about global inflation, the Fed must guard against the risk of inflation expectations remaining above its 2% target; in the context of a series of prolonged supply shocks and high inflation, it is essential that monetary policy should take a risk management stance to avoid the risk of upside inflation expectations. "*
3) *New York Fed President Williams: "Inflation is too high, and Further tightening of monetary policy should help restore the balance between demand and supply and bring inflation back to 2 percent over the next few years, " "tighter monetary policy has begun to reduce inflationary pressures, which will take some time, but expects core goods prices to come down going forward; it is expected that restrictive policy will need to be maintained until 2023 and Interest rates will not be cut until at least 2024, and the underlying expectation is that there will be no recession."*
4) *Cleveland Fed President Loretta Mester: " The costs of stopping tightening too early are high; I need to see more data are showing a further slowdown in price pressures or even lower core service sector prices."*

Source: Tradingview

Technical analysis shows that the monthly K-line chart and RSI oscillator of the DXY Index are currently in a classic "regular bearish divergence" pattern, signaling a reversal opportunity if the RSI oscillator fails to exceed the previous high after the DXY Index has made the next high. If this happens, the first target may be towards the Fibonacci 61.8% retracement, probably at around 105.30 (which has already been hit at about 25 November), and the second target may be towards the Fibonacci 50% retracement, probably at about 102.30 or thereabouts. DXY is currently quoted at 106.30.

The US dollar peaked, with US equity indices and non-US currencies bottomed. The US 10-year Treasury yield revised sharply lower (3.85%-3.62%), with the US dollar consolidating at lower levels. The USDJPY surged 470 pips, corresponding to the recent decline in oil prices, the Canadian dollar depreciated more significantly, and non-US currencies "rallied weakly" as well as "range-bound". Gold, the three major indices rose weakly and remained "range bound” overall. Below is a record of the past week's gains and losses.

- *DXY Index oscillated between 105.00 - 107.50, now at 106.50*
- *The Dow Jones is range-bound between 33400-34350 and is now at 33750*
- *The S&P 500 Index is range-bound between 3900-4040 and is now at 3951*
- *The Nasdaq is currently trading at 11470 in a range of 10600-11900*

- *XAUUSD oscillated in a range of 1720.70-1763.50, now at 1749.50*
- *EURUSD oscillated between 1.02250-1.0495, now at 1.03370*
- *GBPUSD oscillated between 1.1750-1.2150, now at 1.1950*
- *AUDUSD oscillated between 0.6590-0.6790, now at 0.6680*
- *NZDUSD oscillated in a range between 0.6080-0.6280, now at 0.6200*
- *USDJPY down 470 pips (142.20-137.50) or JPYUSD up 3.31%*
- *USDCHF oscillated between 0.9600-0.9385*
- *USDCAD up 350 pips (1.3300-1.3650), or CAD down 2.63%*
- *USDCNH range-bound between 7.1150-7.2550*
- *USDSGD range-bound between 1.3850- 1.3700*

Global stock markets have "bottomed out", with Asia-Pacific and European equities, following the lead of US equities, also opening up to varying degrees of range-bound consolidation over the past week. The Nikkei 225 was particularly notable for its fall of around 680 pips. This corresponds to the recent 470pips surge in the JPYUSD, confirming the long-standing traditional view that the yen is negatively correlated with Japanese stock indices such as the Nikkei 225 Index.

- *SING30 oscillated in a range of 290.50-296.50*
- *JP225 down 680 pips (28500-27820), or 2.39%*
- *AUS200 up 140 pips (7100-7240), or 1.97%*
- *GER30 in a range of 14300-14580*
- *EU50 oscillated in a range of 3900-3975*
- *UK100 up 140 pips (7390-7530) or 1.89%*
- *NL25 rangebound between 712.20-726.20*
- *FRA40 range-bound between 6620-6735*
- *CH20 oscillated in a range of 11000-11200*
- *ES35 up 330 pips (8100-8430), or 4.07%*
- *TWIX oscillated between 550-580*

2. China's central bank announced a 25 basis point interest rate cut, USDCHN reacted flatly.

The People's Bank of China (PBOC) announced on Friday (25 November) its decision to cut the reserve requirement ratio for banks by 25 basis points (bps), effective from 5 December, lowering the weighted average ratio for financial institutions to 7.8% and releasing about 500 billion yuan in long-term liquidity to prop up the faltering economy. China's central bank had already initiated the first 25 basis point reduction in that rate in April this year, this is the second cut. The USDCNH reacted flatly after the decision to lower the rate was announced. Over the past week, the overall range has oscillated sharply between 7.1200 and 7.2550. Chinese central bank officials said the purposes of this ratio cut: are: 1) to maintain a reasonable abundance of liquidity, maintain reasonable growth in total monetary credit, implement a package of policy measures to stabilize the economy, increase support for the real economy, and support the effective improvement of the quality of the economy and reasonable growth in quantity. 2) It is to optimize the funding structure of financial institutions, increase their sources of long-term stable funding, enhance their ability to allocate funds and support industries severely affected by the pandemic as well as small, medium and micro enterprises. 3) The reduction in funding costs for financial institutions will be approximately 5.6 billion RMB per year, which can contribute to lowering the overall financing costs of the real economy through the transmission from financial institutions.

At the same time, in response to the various property crises that have emerged in the real estate sector over the past year or so, there have been "debt defaults by real estate companies", "mortgage suspensions leading to unfinished buildings", and "real estate-related non-performing loan crises". The Chinese government, in relation to the financing of China's real estate, has issued a new "China’s 16-Point Plan" (also known as the "Notice on the Current Work of Financial Support for the Stable and Healthy Development of the Real Estate Market" policy) requires to treat state-owned and private enterprises consistently and equally when granting loans, and to promote the stable and healthy development of China's real estate market, promoting the continued promotion of credit lines and credit bond support from a number of large state-owned banks to high-quality real estate enterprises, etc.

Source: Tradingview

From a technical analysis: The USDCNH's daily K-line chart and RSI oscillator have come out of a classic "regular bearish divergence" pattern, signaling a reversal opportunity if the RSI oscillator fails to exceed the previous high after the USDCNH's price refreshes to the next high. In other words, the CHNUSD may start a wave of upward movement. Meanwhile, the USDCNH may have formed a "head-and-shoulders tops" technical pattern between September and November. If the USDCNH fails to break above the recent high of 7.2750, it may continue to brew the "right shoulder" of the "head-and-shoulders tops" pattern down to the 7.0000 level. If it breaks below 7.0000, a sharp downward retracement could be initiated.

3. The yen has been strong recently, generally rising against non-US currencies.

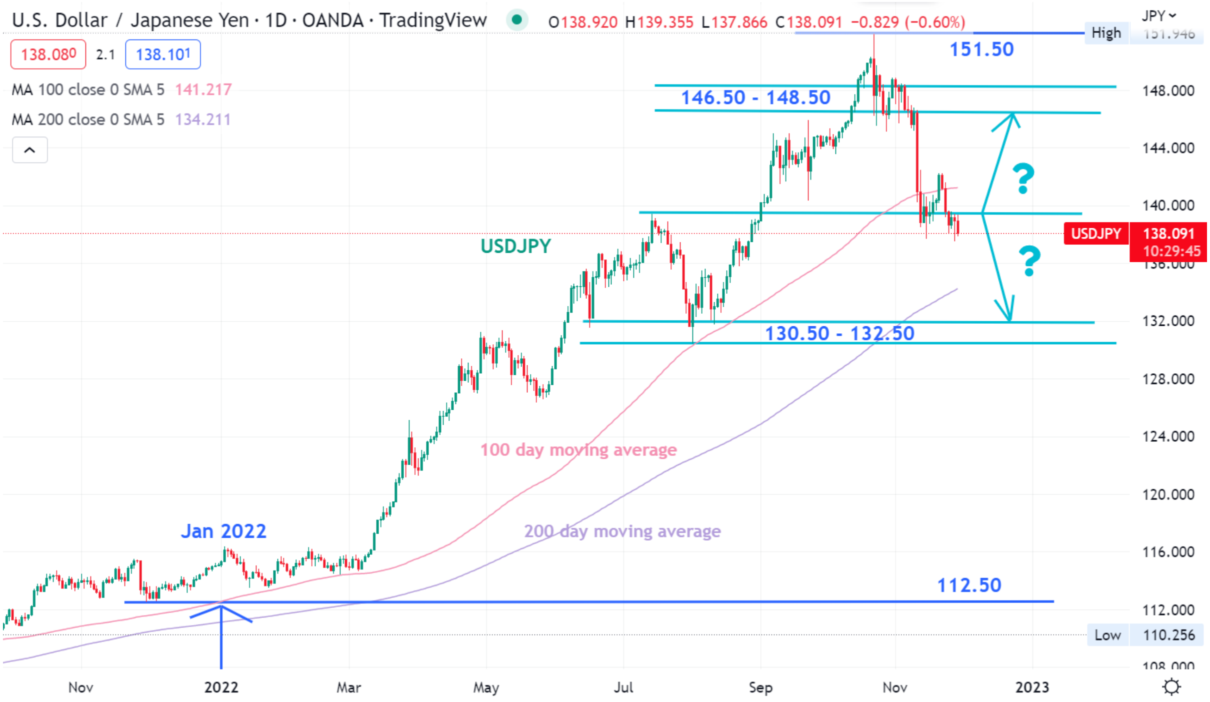
1) How long can the yen remain strong? USDJPY may continue to be "range-bound".

Over the past week, the USDJPY has continued to weaken, partly due to the fall in the yield on the US 10-year Treasury bond and partly due to the outbreak of "blank paper protests" in many parts of China, which has triggered a rise in risk aversion in the market, driving demand for the safe-haven yen. Although the Bank of Japan has maintained an accommodative monetary policy, departing from the Fed's "tightening monetary policy", the Fed's "slowdown in tightening monetary policy" has limited further gains in USD/JPY since November. USDJPY, which has been on an uptrend since early 2022, may have recently "peaked" in the 150.00-151.90 range. Technically, as the USDJPY has followed the US 10-year Treasury yield so far this year, during October-November, the US 10-year Treasury yield has formed a "double top" in terms of technical patterns. This may signal that the current market "bets" on higher interest rates from the Federal Reserve have cooled significantly. It also signals that the USDJPY may have "peaked".

The Bank of Japan's leading candidate for governor, former BOJ deputy governor Hiroshi Nakaso, said at a recent meeting last Thursday (17 November), “once the financial crisis is over, the central bank must cancel emergency support to avoid causing a moral hazard in the market. While the policies of Abenomics are appropriate, this monetary policy has also carried too much of a burden." His statement was interpreted to mean that he would not support a shift to a more accommodative monetary policy if he became governor of the Bank of Japan. That means there is a possibility of a major policy shift at the BoJ next April when current BoJ Governor Haruhiko Kuroda leaves office.

Japan Tokyo CPI rose by 3.8% year-on-year in November, up from 3.5% in October and the 3.6% expected. Japan Tokyo CPI (excluding fresh food and energy) rose by 2.5% year-on-year in November, up from 2.2% in October and 2.3% expected. Japan's manufacturing PMI fell to 49.4 in November, the worst in two years, with both new export orders and overall new orders declining and falling below 50 for the fifth consecutive month, in line with the unexpected 0.3% fall in Japanese GDP in the third quarter. Japan department store sales rose 11.4% year-on-year in October, down from 20.2% in September. The poor PMI data and retail sales data may have reinforced the BOJ's view that domestic demand is weak and CPI inflation is largely input and cost driven and, therefore, unsustainable. The central bank will continue to pursue an accommodative monetary policy, especially in light of the current poor global economic outlook.

There is still a long way to go if the JPY is to return to the price levels seen earlier this year. The 8.58% fall in USDJPY in October-November (151.50-138.50) has taken USDJPY back below the important psychological level of 140.00, which is currently quoted at around 138.65. If it continues to move lower, it may look towards the 132.50-130.50 range around August this year. If it rebounds, it could go back to the 146.50-148.50 range set in September this year.



Source: tradingview, USDJPY will need to break out of the 146.50-148.50 range if it is to return to the highs of around 150-151 set in October. I expect this to be less likely. USDJPY may remain range-bound within the 132.50-146.50 range in the coming months.

2) The Yen returned strongly last week, while non-US currencies were generally weak against the Yen.

USDJPY's recent decline and the yen's strength, on the one hand, was due to the release of relatively dovish minutes from the Federal Reserve, which further boosted the yen's appreciation. On the other hand, the protests across China against the "zero-Covid policy" also stimulated the market's "risk aversion" to heat up. Last week, the Japanese yen was the strongest performing currency, showing its "safe-haven" properties. With the "USDJPY" leading the decline, and against the backdrop of a "generally weak rebound in non-US currencies against the USD", non-US currencies tended to fall collectively against the JPY. Since China's "blank paper protest" against the "zero-Covid policy" erupted last Saturday, risk aversion has been on the rise. GBPJPY, EURJPY, AUDJPY and NZDJPY each fell by around 200 to 350 pips, with USDJPY having the most significant drop and the Japanese yen having the biggest gain against the US dollar, up around 470 pips. The following are the record gains and losses for the past week.

- *USDJPY down 470 pips (142.20-137.50), or 3.31%*
- *GBPJPY down 350 pips (169.00-165.50), or 2.07%*
- *EURJP down 300 pips (146.00-143.00), or 2.06%*
- *NZDJPY down 200 pips (87.50-85.50), or 2.29%*
- *AUDJPY down 200 pips (94.20-92.20), or 2.12%*
- *CADJPY down 360 pips (105.80-102.20), or 3.40%*
- *CHFJPY down 380 pips (148.80-145.00), or 2.55%*
- *SGDJPY down 280 pips (102.80-100.00), or 2.72%*

4. Protests against China's covid lockdowns erupt across China, and solidarity with China protesters is seen worldwide.

China's strict "Dynamic zero-COVID" strategy is an essential deterrent to economic growth not only in China but also in some of the countries around the world that depend on China's economic growth. Over the past week, the desire for an end to the "zero-Covid policy" has turned into a "blank paper protest" by the people and university students in their quest for "freedom and democracy". Protests against the "zero-Covid policy" and "blank paper protests" have been taking place across China since last Saturday night (26 November). This round of protests was sparked by the death of 10 victims of a fire in Urumqi, Xinjiang, on 24 November, suspected to have been caused by "pandemic restrictions" and unable to escape, with rumors on the internet that as many as 44 people may have been killed. The "Wulumuqi Middle Road" has become a gathering place for people in Shanghai to pay tribute. People in major cities in China, such as Beijing, Chongqing, Guangzhou, Chengdu, Zhengzhou and Wuhan, and students from universities, have participated in different ways in the "Blank Paper Protest" to express their dissatisfaction with the "zero-Covid policy". Chinese students studying abroad have also held various protests and tributes to the victims of the Xinjiang fire in front of Chinese embassies in the US, UK and Australia. Chinese officials have deployed additional police forces to maintain order.

China's current "zero-Covid" measures remain an important determinant of market risk sentiment and future growth prospects. Strict restrictions are not only holding back China's economic recovery but also creating a certain degree of an impediment to the growth of the global economy. Reflecting on the financial markets, the event saw the 'yen' safe-haven currency rise and the yuan fall to a new low in almost three weeks. Mainland China and Hong Kong stocks fell sharply on Monday (28 November) but rallied sharply after 29 November and have now recovered all their losses. The following are the record gains and losses for the past week.

- *USDCNH oscillated between 7.1150-7.2550*
- *CHINA50 up 850 pips (11800-12650) or 7.20% after falling to a low of 11800*
- *CHINAH up 620 pips (5680-6300), or 10.92%, after falling to a low of 5680*
- *HK50 up 1580 pips (16820-18400), or 9.39%, after falling to a low of 16820*

5. WTI oil price falls below 75. The oil price outlook is still unclear.

On Monday (28 November), WTI crude oil fell below the crucial psychological level of US$75/barrel and once touched a low of US$74.00 before starting a sharp rebound up and is currently quoted at US$79.30/barrel. This is the first time since the "Russia-Ukraine war" that the price has fallen below this level, returning to the level of around 4 January earlier this year. Subsequently, market news indicated that OPEC might seriously consider the possibility of introducing new production cuts at its proposed ministerial meeting this Sunday (4 December). Last week, Minister of Energy of Saudi Arabia Abdulaziz bin Salman Al Saud dismissed market speculation that OPEC might increase production by 500,000 BPD. Salman said the 2 million barrel reduction would last until the end of 2023 and that OPEC was "ready to intervene" if there was a need to "balance supply and demand".
The market is currently expecting the G7 price cap for Russian oil to be in the previously set range of US$65-70. With high inflation in countries worldwide, the G7 countries also want Russia to keep oil flowing to avoid a spike in global prices. Helima Croft, Global Head of Commodity Strategy, Global Research, RBC Capital Markets, said, "The oil price cap is not designed to reduce Russian revenues, but to keep Russian oil on the market. Predictably, a higher oil price cap will not lead Russia to take production cuts, while OPEC is likely to take further action in this case."
The US replenished the SPR, defending oil prices at US$70/bbl. The current worse pandemic situation and "blank paper protests" in China may make the outlook for China's economic recovery even more uncertain. They may also be a drag on oil prices.
Technically, crude oil has generally maintained a downtrend since the beginning of November, with WTI Oil oscillating in a range of 74.00-82.80 and Brent Oil oscillating in a range of 82.00-90.50 over the past week.

Short-term risks:

Please focus on Fed Chairman Powell's speech this Thursday (1 Dec) at 2.30 am if he makes "hawkish remarks." It may halt the dollar's recent retreat. In terms of economic data, focus on the US core PCE price index for October, one of the inflation indicators the Fed is also concerned about, released this Thursday (1 Dec). Also, please focus on the upcoming US non-farm payroll data this Friday (2 Dec) at 9.30 pm. If the non-farm payroll data shows that the labour market remains strong, the Fed may slow the pace of interest rate hikes sooner; the data may also provide new clues to the overall direction of the market next. Also, please focus on the release of the ISM Non-Manufacturing Index for November next Monday (5 December) and the University of Michigan Consumer Confidence Index (preliminary) for December next Friday (9 December).

The author believes that the probability of a small rebound upward for the dollar in the future is high. On the one hand, the US dollar has recently retraced by 9.09% (115.50-105.00). On the other hand, US inflation remains high, with the US CPI recording an annual rate of 7.7% in October, but this is still a long way from the Fed's inflation target of 2.0%. The Fed's "tight monetary policy" will continue to "curb inflation", and the Fed is not currently in a position to initiate a significant "monetary policy" shift. The policy of "slowing the pace of interest rate increases but maintaining high-interest rates for a longer period" remains unchanged.

By Sandy Wang,

12:10 pm SGT time, 30 Nov 2022