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The Market Focus has Shifted to the 'US dollar Depreciation Rate', and the Gold and Crude Oil Rally Looks Promising.

Key Takeaways:

- *The market as a whole may turn to expect the dollar to "depreciate" more than "appreciate";*
- *The Fed's March interest rate meeting to raise interest rates by 25 basis points, and it is difficult to stop the dollar continued to fall;*
- *The US Dollar Index and US Treasury yields are slightly "decoupled";*
- *The expectation of a "hawkish rate hike" by the European Central Bank and the strengthening of the expectation of a "policy shift" by the Federal Reserve may be more favourable for the euro;*
- *The outlook for the interest rate policy of the Federal Reserve may continue to dominate the USDJPY trend;*
- *Crude oil may have already hit bottom and rebounded, with a future target of 100.00.*

1. The whole market may expect the dollar to "depreciate" more than "appreciate".

1) Fed raised interest rates by 25bps at the March rate meeting, unable to stop USD from continuing to fall.

The Federal Open Market Committee (FOMC) March interest rate meeting last Thursday night (23 March) raised the target federal funds rate by 25 basis points to 4.75% to 5.00%, as expected by the market, making it the ninth consecutive rate hike since the Fed started the current round of rate hikes in March last year. After a slight gain of 1.48% (from 101.50 to 103.00), the US Dollar Index continues to trend lower and is currently quoted around 102.20. The market's expectation of the end of the current Federal Reserve rate hike cycle has put pressure on the US dollar, and the US dollar may shift to a "depreciation rate" more significant than an "appreciation rate". The US dollar index, which hit around 105.50 on 8 March, may become a phased "high" for the dollar this year, and the peak range of 113.50-114.50 set in late September last year may be irretrievable.

Key points from the Fed's policy statement: Fed officials unanimously supported a 25 basis point rate hike, highlighted the uncertainty caused by the recent banking turmoil, kept the median interest rate expectation for this year unchanged at 5.1%; did consider a pause in rate hikes in the days running up to the meeting, and rate cuts are not the basic expectation for this year. If necessary, rates will be raised even higher. The recent balance sheet expansion is temporary and does not affect monetary policy. No Federal Reserve official believes there will be a rate cut in 2023. The statement removed the phrase "FOMC members expect continued rate hikes to be appropriate", as repeatedly used in the past eight statements and replaced it with "it is expected that some additional policy tightening may be appropriate". This change in wording has been interpreted as suggesting that the Fed's rate hike cycle is nearing its end.

At a press conference afterwards, the critical points of Fed Chairman Powell's remarks were as follows: severe failures by Silicon Valley Bank management have led to liquidity risks for the bank, SVB is an exception, there are no widespread weaknesses in the banking system, all investigations into this banking failure are welcome, deposit flows in the banking system have stabilised over the past week, the banking system is healthy and resilient, and we are conducting a comprehensive review to determine whether stronger regulation is needed. The higher-than-expected economic data since the beginning of the year and the recent banking crisis roughly offset each other. It is expected that there may be one more rate hike this year, and a rate cut is not our basic expectation for this year. It is crucial to maintain confidence in the Federal Reserve. We are very focused on bringing down inflation. Non-housing service prices have not made progress, and commodity inflation is declining, although the pace is slower than we would like. We are also very aware of the concentration risk in commercial real estate. The policy must be tight enough to lower inflation, and some tightening may come from credit conditions. The tightening of financial conditions may be more severe than indicated by the indicators, and we need to understand the extent and duration of this tightening. In the end, we will take sufficient measures to bring inflation down to 2%. If we need to raise rates higher, we will do so. The banking crisis makes a "soft landing" less likely, but Powell believes there is still a path there.

The policy statement of the March Federal Reserve meeting and Chairman Powell's speech showed some subtle changes compared to February, possibly influenced by the recent bank failures in the US. It should be noted that the US Consumer Price Index (CPI) inflation rate for February fell from 6.4% to 6%, which is still three times the Fed's policy target of 2%. Moreover, inflation tends to rise more easily than it falls, so there may be fluctuations in CPI data in the future (for a more detailed explanation, please refer to the previous article Inflation is Easy to Rise but Hard to Fall, and the "Low-Interest Rate Era" May be Hard to

Return). This is also why the Fed may "continue to raise interest rates". I believe that the probability of another 25 basis points rate hike at the May meeting is still high. In addition, some recently released data suggests that the US economy remains robust. The March Markit Composite PMI (preliminary) for the US recorded 53.3, better than the previous value of 50.1 and the expected 49.5; the March Markit Manufacturing PMI (preliminary) for the US registered 49.3, better than the previous value of 47.3 and the expected 47, and also a new high since October last year; and the March Markit Services PMI (preliminary) for the US recorded 53.8, better than the previous value of 50.6 and the expected 50.5. This may also support the Fed's confidence in another 25 basis points rate hike in May.

Given the pressure on the US banking sector, the Fed may be more cautious about future interest rate hikes. Some recent comments by Fed officials have also signaled a shift in their stance towards "continuing to raise interest rates." Neel Kashkari, president of the Minneapolis Fed, who had previously held a hawkish stance, recently (26 March) stated that recent bank turmoil had increased the risk of a US economic downturn, but it is still too early to judge what this means for the economy and monetary policy. However, St. Louis Fed President Bullard stated that Silicon Valley Bank is an exceptional case, and the US banking system is still very strong and resilient, in a very good position. There is a low probability of recent pressures triggering a global crisis.

According to the CME Fed Watch tool, the probability that the Fed will maintain its interest rate at 4.75%-5.00% in May is 52%, while the probability of raising the interest rate by 25 basis points to the 5.00%-5.25% range is 48%. The probability of a 25 basis point rate cut in September is 42.8%, while the probability of keeping the interest rate unchanged is 24.2%. The interest rate peak for this year is projected to be between 4.25% and 4.50% in December. These data suggest that market expectations for the Fed to continue raising interest rates have further decreased, with bets on at most one more rate hike and a potential rate cut before the end of the year. Bank of America recently lowered its forecast for the Fed's interest rate peak from 5.25%-5.50% to 5.00%-5.25%.

Source: TradingView

The inverted yield curve of US 30-year/2-year Treasury bond yields (US 30-year Treasury bond yield minus US 2-year Treasury bond yield) reached a peak of 119 basis points (-1.19%) around 8 March 2023 and briefly broke out of inversion on 24 March, touching 0.045% before returning to an inversion of 25.3 basis points (-0.253%). The reversal and rise of the US 30-year/2-year Treasury bond yield curve, breaking through the "zero" axis, may also signal that the Federal funds rate or other future interest rates will slowly begin to reverse downward. This is consistent with market expectations that the Federal Reserve may enter a rate-cutting cycle in the coming months. Specifically, we need to closely observe whether other long and short-term yield curve inversions will also break out of inversion in the coming months.

2) The US Dollar Index and US Treasury yields are slightly "decoupled".

Reflected in the financial market, the US dollar index fluctuated between 103.00 and 101.50 last week, with an overall tendency to decline. It is currently quoted at 102.65. Following the failure of major US banks such as Silicon Valley Bank in recent times, the 6-month, 1-year, 2-year, 10-year, and 30-year US Treasury yields "peaked" around 5.30%, 5.27%, 5.07%, 4.08%, and 4.03%, respectively. They have rebounded to 4.85%, 4.53%, 4.04%, 3.56%, and 3.77%, respectively, and are relatively unchanged from a week ago. Non-US currencies, gold, and the three major US stock indices consolidate "narrow-range oscillations". It is worth noting that there has been a slight "decoupling" between the recent decline in the US dollar index and the collective rise in US Treasury yields. Does this suggest that the "market has fully digested and fully priced in the Fed's tightening policy for this year"? Or it indicates that the increase in the US dollar has been fully digested. However, US Treasury yields are still expected to rise slightly under the expectation that the Fed may at least raise interest rates once again. The US dollar may remain in a "sideways consolidation" before the Fed truly begins to tighten its policy and then enter a more obvious decline over the next few months. This may be the beginning of a new round of "market reversal".

Source: TradigView

US 6-Month, 1-Year, 2-Year, 10-Year and 30-Year Treasury yields rose slightly over the past week, while the Dollar Index remained generally lower. The slight "decoupling" of US Treasury yields and the US Dollar Index is worthy of further observation by investors.

3) The expectation of a "hawkish rate hike" by the European Central Bank and the strengthening of the expectation of a "policy shift" by the Federal Reserve may be more favourable for the euro.

Speaking last Wednesday (22 March), ECB President Christine Lagarde said that she maintained her hawkish stance, that inflationary momentum remains strong, and that there is no trade-off between price stability and financial stability while noting that the ECB must bring inflation down to its target level.

The German Council of Economic Experts had recently warned that inflation could rise again if monetary policy is affected by risks in the financial markets. Inflation will come in at 6.6% in 2023 and 3.0% in 2024, the council predicted, indicating an inflation challenge ahead for the euro area. Compared to the Federal Reserve, the ECB's interest rate resolution last week sent a strong message to the market that the banking system is still resilient, and the ECB's committee is still open to further interest rate hikes, despite the fact that the Credit Suisse banking crisis may have passed. A few ECB officials have expressed concern that the current low expectations for policy rates are a deviation from the ECB's original intention to "raise rates to fight inflation" as soon as possible, which may suggest greater upside potential for the euro going forward. The market may have underestimated the ECB's determination to continue to raise interest rates to "fight inflation", and if it is confirmed that the banking sector is sailing through the crisis in the future, the ECB will probably continue to raise interest rates to higher levels to fight inflation, which will provide support to the euro.

2. The outlook for the interest rate policy of the Federal Reserve may continue to dominate the USDJPY trend.

Last week, the rising market risk aversion boosted the Japanese yen. This week, First Citizens Bank has agreed to acquire parts of the bankrupt Silicon Valley Bank (SVB)'s equity and will take on all of SVB's deposits and loans. First Citizens Bank's acquisition of SVB's deposits and loans, as well as some other assets, means that SVB's investors need not worry about the safety of their deposits or loans. This news may help alleviate anxiety about stress in the US banking system and ease some of the risk aversion sentiment, combined with a slight increase in US Treasury yields, causing USDJPY to fluctuate between 129.50 and 131.50.

Japan's latest inflation figures were mixed. According to official data, headline inflation eased last month, with the Consumer Price Index (CPI) registering an annualised rate of 3.3% in February, a full percentage point lower than the 4.3% recorded in January. However, policymakers are dissatisfied with the performance of core inflation, which excludes volatile food and fuel prices. The core CPI recorded 3.5% in February, higher than the 3.2% recorded in January. Inflation remains robust, and one indicator is even at its peak in nearly forty years. Food prices have risen slightly. In February, food prices contributed 0.1% more to the CPI, rising to 2.0%, of which 1.7% came from non-perishables. This mainly reflects higher import costs, as direct imports of food or imported energy and other products have raised domestic production costs. Perishables contributed only 0.3% to the February CPI. CPI, excluding fresh food and energy, continued to climb, rising 0.3% year-on-year to 3.5% in February. Consumer goods prices rose due to higher import costs. Inflation in clothes and footwear accelerated by 0.5% to 3.6 % in February, while inflation in Medical Supplies & Appliances and equipment rose by 1.2% to 2.4%.

The current Governor of the Bank of Japan, Haruhiko Kuroda, will step down on 8 April. The next Governor, Kazuo Ueda, is not expected to make any major policy changes in the short term. Meanwhile, the BoJ's next interest rate meeting (28 April) will be the first meeting by the new Governor, Kazuo Ueda, who has previously stated that he needs to see a change in the inflation trend before he will exit easing. According to reports, the Japanese government has expressed concern over the Bank of Japan's long-standing loose monetary policy. Any slight adjustment in policy by Kazuo Ueda may provide support from the Japanese government for the yen's rise. For now, the "divergence" in monetary policy between Japan and the US will remain the main driver of the USDJPY trend.

Bank of Japan Governor Haruhiko Kuroda recently reiterated his policy view that continued large-scale monetary easing is appropriate, that a sustainable inflation target has not been reached and that it is too early to discuss the specifics of an exit from the policy. In addition, Shigeyuki Goto, Minister of Economic Revitalization of Japan, recently said that they are going to use budget reserves to pay for a stimulus package worth 2.2 trillion yen. This is also a statement in line with Haruhiko Kuroda's easing policy.

3. Singapore’s Central Bank Boosted Gold Reserves 30% in January.

Gold has historically been recognised as the most valuable financial instrument in times of “political and economic crisis” and “geopolitical conflict”. The "safe-haven", "monetary", and "investment" properties of gold were fully demonstrated in 2022. Since the outbreak of the Russia-Ukraine War at the end of February 2022, it has been very logical for central banks worldwide to choose to increase their gold reserves gradually. In 2022, central banks around the world increased their gold purchases by 1,136 tons throughout the year, which is the highest peak of global central bank gold purchases since 1967, the second highest since the record of central banks purchasing gold began in 1950, and also the thirteenth consecutive year of "net purchases of gold" by central banks worldwide. At the same time, the total amount of US Treasury bonds sold by countries around the world in 2022 reached US$246.4 billion. Among them, Japan, as the largest foreign holder of US Treasuries, reduced its holdings by US$69.8 billion in 2022, an important "reference" indicator for observing the future performance of the global financial market. Recently (24 March), the share price of Deutsche Bank, the largest commercial bank in Germany, plummeted on the Frankfurt Stock Exchange, with an intraday decline of over 14%, causing concerns about European bank stocks in the market and igniting safe-haven sentiment, which also supported gold.

Since we headed into 2023, there have been three major buyers who have purchased a large amount of gold. The first is Singapore. According to relevant reports on 9 March, the Singaporean central bank purchased 44.6 tons (1,434,600 ounces) of gold through the Monetary Authority of Singapore (MAS) in January 2023, increasing its gold holdings from 153.8 tons to 198.4 tons, which means that Singapore's gold reserves have grown by 29% in just one month. This is the second-largest single-month purchase of gold in Singapore's history. The first large-scale purchase of gold by Singapore was in 1968, when it purchased 100 tons of gold from South Africa. As a small country and a financial centre in Southeast Asia, Singapore's large-scale increase in gold holdings may be to solidify its "financial centre" status. The second is Turkey, which was also the largest gold buyer among global central banks in 2022. Due to the 30% depreciation of its currency last year, the purpose of purchasing gold is to combat inflation and increase the credibility of its financial system. The third is China. The China central bank had been increasing its gold holdings for four consecutive months since November-December last year, and China's total gold reserves have risen to 2,050 tons.

Currently, the world may be experiencing the initial stage of "economic stagflation," with high inflation in developed countries such as the United States and Europe. The Federal Reserve may soon enter the final stage of raising interest rates, while US Treasury yields and the US dollar index have peaked. In addition, some countries in the "European and US economies" may enter an economic recession, highlighting the value of allocating and investing in gold. The author not only firmly believes in the value of investing in gold but also sees silver, copper, and other precious metals as good investment targets in 2023 and beyond.

Gold is set to rise in 2023 for three reasons, according to Ryan Voon, a commodities trader at Goldman Sachs. First, the trend of gold selling is nearing its end. Second, regardless of when the Fed shifts, it is positive for gold and other safe-haven assets. Third, due to the influence of geopolitical conflicts, central banks worldwide will favour neutral assets like gold. In recent reports, Goldman Sachs also mentioned that if central banks continue to buy gold at a rate of 400 tons per quarter, gold prices could rise by 25% under similar conditions. In a less extreme scenario, if central bank purchases are reduced to 250 tons per quarter in 2023, gold prices could rise by 12.5% under similar conditions.

It is almost a foregone conclusion that gold will have an overall upward trend in 2023. Technically speaking, since December 2022, gold has been fluctuating within a range of 1765.00-1800.50. However, it stabilised around 1800.00 in early March this year and has surpassed the critical psychological level of US$2,000 per ounce after the recent bankruptcies of the three major banks in the United States, reaching a high of US$2010 per ounce. Currently, it is around US$1966.50 per ounce, and it is expected to start a bigger uptrend later this year. In the short term, it is expected to towards a peak range around 2050-2070, which was hit in late February or early March 2022 during the outbreak of the Russia-Ukraine conflict.

Source: TradingView

Gold had its highest test touched the US$2050-US$2070 per ounce range in late February/early March 2022, just after the Russia-Ukraine conflict broke out. This is also, f the target range for gold's rise, which is currently at around US$1,966.50 per ounce at present.

4. Crude oil may have already hit bottom and rebounded, with a future target of 100.00.

The recent simultaneous rise in gold and oil prices is highly correlated, with the potential for even more significant increases in the future, mainly driven by the expected depreciation of the US dollar. Firstly, although the market is still expecting a 25 basis point rate hike from the Federal Reserve in May, the US dollar is still clearly biased towards depreciation, which is beneficial to oil prices. Secondly, the announcement of the acquisition of Silicon Valley Bank by America's First Citizen Bank has further eased concerns about the banking industry, reduced overall market risk aversion sentiment, and increased risk appetite, which is beneficial to oil prices. Thirdly, President Xi’s trip to Russia last week may lead to the possibility of peaceful negotiations to end the "Russia-Ukraine war", which has also boosted market risk appetite. Fourthly, the signal of reduced oil production in Russia, with production being reduced by 500,000 barrels per day (about 5% of its production level) since March, will limit the supply side, which is also one of the factors driving oil price increases. Fifthly, China's demand for oil may continue to rise. Sixthly, WTI crude oil rose sharply in the short term due to news from Turkey, and its subsequent impact is still under observation. Turkey decided to suspend crude oil exports via the Kurdistan region after the international arbitration ruling that the export of crude oil via the Kurdistan region required Iraqi consent. This news triggered a surge in WTI crude oil prices starting this Monday, closing up by as much as 5%.

Technically speaking, the oil price has rebounded to US$70-US$75 per barrel but has repeatedly been oscillating since then. Since 20 March, the oil price may have hit bottom, and it is currently maintaining a rebounding trend. Since Monday (20 March), WTI has rebounded significantly from around US$64.50 to US$73.50, while Brent oil has rebounded dramatically from US$70.50 to US$79.10.

- *WTI oil rose by 900 pips (from US$64.50 to US$73.50), or 14.31%, and is currently trading at US$73.40.*
- *Brent oil rose by 860 pips (from US$70.50 to US$79.10), or 12.20%, and is currently trading at US$78.65.*

Source: TradingView

WTI Oil has rebounded significantly from around US$64.50 to US$73.50 and may reach US$100.00 within the rest of this year.

5. Short-term risks

The Federal Reserve faces the difficult task of balancing "price stability" (i.e., "fighting inflation"), "financial stability," and "economic growth" in its future policymaking. The author believes the Federal Reserve may focus on "financial stability" and "price stability" first. Improving inflation conditions has always been the main focus of the Federal Reserve's policymaking. Please pay attention to the US PCE (Personal Consumption Expenditures) Index data on Thursday (30 March) and the US Core PCE (Personal Consumption Expenditures) Index next Friday (31 March). Pay attention to the release of the minutes of the FOMC Meeting next Thursday(6th Apr) and the US non-farm payroll data on Friday, 7 April. Improving inflation conditions remain the main focus of the Federal Reserve's policymaking.

In addition, it is expected that before the May FOMC meeting, there will be more market volatility, as well as a "depreciation of the dollar before appreciation", and we need to closely examine in terms of the relevant data on the improvement of inflation in the United States, as well as the interest rate policies of the European Central Bank and other developed countries' central banks, which can serve as a "demonstration" reference. The Federal Reserve will not abandon its fight against inflation by raising interest rates, it may support the appreciation of the US dollar. Still, economic development and financial stability require the depreciation of the US dollar. It is also necessary to be vigilant that when the market fully digests and prices in the Fed's tightening policy for this year, the downtrend of the US dollar may become more determined. The US dollar index, around 105.50, may become a phrased high for the dollar this year.

In the Asia-Pacific region, pay attention to the data on China Manufacturing PMI and Non-Manufacturing PMI for March on Friday (31 March), as well as the Caixin PMI for March in China on Monday (3 April). Pay attention to the release of the Tokyo CPI and Japan Core CPI for March and retail-related data next Friday (31 March). Pay attention to the Reserve Bank of Australia's interest rate decision and monetary policy statement on Tuesday (4 April), as well as the Reserve Bank of New Zealand's interest rate decision and statement on Wednesday (5 April).

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