

## FX Daily: BoJ delivers last shock of the year

The Bank of Japan announced a surprise change in its yield curve control policy, and will now allow JGBs to trade to an upper bound of 0.50%. While Governor Kuroda has explicitly warned this is not a rate hike, taming speculation of further BoJ normalisation in 2023 won't be easy. USD/JPY may break below 130.00. Elsewhere, expect no fireworks from Hungary



The Bank of Japan in Tokyo

### 📉 USD: BoJ hawkish shift may have broad implications

Markets have been shaken from their pre-festive low volatility torpor this morning, as the Bank of Japan announced a surprising change in its yield curve control (YCC) policy. The target band for the 10-year JGB has been widened to +/- 0.50% from the previous 0.25%, essentially allowing higher interest rates in the current inflationary environment despite still officially targeting 0.00% as the outright target. The move was accompanied by an increase in the amount of JGB purchases, from JPY 7.3tn per month to 9tn.

The immediate impact on the yen has been sizeable, with USD/JPY dropping by around 3.0%, and currently trading around 133.00. The BOJ's role as an ultra-dovish outlier among global central

banks had been a key driver of JPY weakness in 2022, and markets are now assessing whether today's announcement is effectively a first step towards a broader policy normalisation process in Japan, which would quite radically change the outlook for the yen in 2023.

Incidentally, there is a risk that speculation of even higher JGB rates in 2023 could spill over into global bonds and equities (like it did today). Governor Haruhiko Kuroda's press conference has been all about pushing back against such speculation: he explicitly warned markets not to interpret this as a rate hike and said that he doesn't think a further widening of the yield band is needed. Our suspicion is that markets may need more reassurance with this, especially considering that Kuroda is due to be replaced in April 2023 and the timing may suggest the BoJ may be laying the groundwork for normalisation under a new governor.

For now, we think risks remain skewed to the downside for USD/JPY into the festive break, and we cannot exclude a break below 130.00 - also given the generally soft dollar environment. For now, the negative reaction in global equities is capping pro-cyclical currencies, and offering some USD support on balance, but broader dollar weakness is surely a possibility in the near term. DXY could press 103.50 by the end of this week.

In the US, housing data will be in focus today, with housing starts expected to have dropped further in November as high mortgage rates continue to weigh on the property sector.

*Francesco Pesole*

## **EUR: Sidelined, for now**

EUR/USD has been on the sidelines of the post-BoJ market reaction, holding marginally above 1.0600. It's likely that the downward pressure on the dollar from the BoJ's hawkish shift has been fully offset by the deterioration in risk sentiment, which negatively impacts the pro-cyclical euro.

As discussed in the USD section above, there are lingering downside risks to the dollar and we could see EUR/USD test 1.0700 before Christmas. Anyway, volatility should become significantly thinner from Wednesday/Thursday, with today's BoJ announcement having been the last major event in markets.

The eurozone calendar includes consumer confidence data - which is expected to have slightly improved in December - and speeches by ECB's Peter Kazimir and Madis Muller.

*Francesco Pesole*

## **GBP: No domestic drivers**

There is nothing to highlight in the UK calendar today, and the pound should continue to be driven by dollar dynamics. EUR/GBP initially had a positive reaction to the BoJ announcement, likely due to GBP's higher sensitivity to the adverse response in global equities, but is now back at yesterday's close.

Still, GBP downside risks should be larger than for the euro if risk sentiment remains pressured today, and EUR/GBP may move to the upper half of the 0.87-0.88 band.

*Francesco Pesole*

## ➔ CEE: NBH ends a dramatic year with a quiet meeting

The economic calendar for today offers several macro numbers from Poland, led by industrial production. We expect November's output to have slowed significantly in year-on-year terms, from 6.8% to 0.7%, well below market expectations. Also, today we will see data from the labour market and industrial producer prices in Poland.

Then in Hungary, the State Debt Management Agency (AKK) will present its financing strategy for next year. The government is currently in the process of revising the budget, but the main question will be what the government's assumption will be for the absorption of EU money.

Later, we will see a decision by the National Bank of Hungary (NBH) at its last [meeting](#) of the year. The NBH has made it clear on several occasions that the temporary and targeted measures, introduced in mid-October, will remain in place until there is a material and permanent improvement in the general risk sentiment. Although we've seen some progress here, we don't think enough has changed to trigger an adjustment in the monetary policy's hawkish "whatever it takes" setup.

Although the EU story is still not over, tangible progress should keep the forint on the stronger side and limit potential losses. Moreover, the NBH liquidity measures have worked, and implied FX yields once again soared to record highs during December; on average, they are double that of regional peers, protecting the forint from a further sell-off in our view. Overall, we expect the forint to move towards 400 EUR/HUF and below that level next year.

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