

FX Daily: BoJ lift-off underwhelms the yen

The Bank of Japan has finally ended its eight-year reign of negative interest rates and shifted to a more conventional policy of targeting short-term interest rates. Kudos to BoJ Governor Kazuo Ueda for achieving this without dislocating financial markets. A policy rate near 0.1% still leaves the yen vulnerable in a low-volatility world



The Bank of Japan in Tokyo

➔ USD: Choppy into tomorrow's FOMC meeting

The dollar has shown a little strength over the last 24 hours, reconnecting with the higher short-term interest rate story. We notice as well the turnaround in some of investors' favourite FX trades (e.g., long Mexican peso), which may be profit-taking ahead of tomorrow night's FOMC meeting and Thursday's Banxico meeting, where there is a high chance of the first Banxico cut.

The major story this morning, however, is the Bank of Japan ending its eclectic monetary policy mix. Gone are the negative interest rates, yield curve control and purchases of ETFs and Real Estate Investment Trusts. Instead, excess reserves at the BoJ will now be remunerated at 0.10% and the BoJ will target the overnight call rate (its main policy rate now) in a range of 0.0-0.1%. The yen sold off on the headlines that the BoJ would keep an accommodative policy for a while, but recent headlines are suggesting that further rate hikes may be forthcoming now that the virtuous

link between wages and prices has been confirmed.

The problem for the yen, however, is that volatility remains exceptionally low and the carry trade exceptionally popular. USD/JPY may well trade in a 150-152 range for the time being (locals in Tokyo think the BoJ will not intervene to sell USD/JPY until 155), and a lower USD/JPY will have to be led from the dollar side.

Moving onto today, the US calendar is quiet ahead of [tomorrow's FOMC meeting](#). With the market now just pricing 68bp of Fed cuts this year, the FOMC could prove a mild dollar negative. For the time being, however, the risk of the Fed Dots shifting to just 50bp of cuts this year could continue to prompt some modest dollar short covering. One thing to mention regarding today's data is the housing starts. Democrats are starting to put pressure on the Fed over the locked-up housing market; no one wants to move home and lose a 3% mortgage rate. A lower housing starts figure could prove a mild dollar negative.

DXY may well trade a 103.50-104.00 range today.

Chris Turner

➔ EUR: ZEW in focus

EUR/USD has softened a little, which seems to be more in line with short-term interest rate differentials. At -135bp, two-year EUR:USD swap rate differentials remain at their widest levels for the year. We have already heard today from the European Central Bank's Luis de Guindos, who said the ECB needs to wait for June before deciding on a rate cut. We doubt a marginally better German ZEW number today will move the needle much on ECB rate cut expectations or the euro and it looks like EUR/USD will struggle to get back above 1.0900 short term.

Elsewhere, we note EUR/CHF flying high at 0.9660. Data released today showed that the Swiss National Bank was still selling FX in the fourth quarter of last year. It might have flipped to FX buying this quarter, but confirmation of that will not emerge until late June. In focus, however, is Thursday's Swiss National Bank rate meeting, where some are looking for the first rate cut. That is not our house view, but we do not rule it out given that the SNB only meets four times per year compared to eight times for the ECB. A surprise SNB cut would likely carry EUR/CHF over 0.9700 and potentially USD/CHF sharply higher, since EUR/USD could come lower on a major European central bank cutting rates.

Chris Turner

➔ GBP: Holding pattern into Thursday

EUR/GBP continues to trade above major support at 0.8500 and should continue to trade tight ranges into Thursday's Bank of England meeting. ING's UK economist James Smith looks for [unchanged forward guidance](#), which could prove a mild sterling positive and see EUR/GBP retest 0.8500 – especially if the SNB cuts rates on the same day.

Chris Turner

➔ CEE: The sell-off across EM has shuffled the cards

Today's calendar in the region is essentially empty – however, yesterday's sell-off in the EM

universe shuffled the cards sufficiently. This should keep the markets busy today. PLN, in our view, has shown the biggest anchor from rates. With levels around 4.320 EUR/PLN, this could be an opportunity for some to go long PLN at cheaper levels. However, on the flip side, we may see more noise around the central bank this week (as we mentioned yesterday), which may trigger another EUR/PLN move higher.

EUR/CZK is back above 25.20, in line with our expectations yesterday, and we expect it to stay there until Wednesday's Czech National Bank meeting. The most complicated situation we see now is for the HUF, which on the one hand has returned to 395 EUR/HUF and at the same time rates have been hit by a strong sell-off. This has shot the interest rate differential at the short end of the curve almost to the highest levels since the beginning of the year, which we believe will lead to a stronger HUF in the end. Given the extent of the move, we need more days to determine where the market is. We believe there could be solid potential later on, given the bullish market view on HUF assets.

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