

The FX Trader Can the real JPY please stand up

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Summary: Thursday was somewhat of a watershed day, as risk sentiment stumbled badly amidst higher oil prices, but that fresh surge in oil prices failed to drive weakness in bond markets. Instead, we got quite the opposite, which means a somewhat different reaction pattern across currencies and perhaps a chance for the JPY to rally more persistently. Elsewhere, French sovereign bond yields remain an important focus for the euro.

A different kind of day for global markets yesterday The oil price surge since the outbreak of the Middle East conflict earlier this year has generally been associated with rising global bond yields. The US dollar has loosely tracked that rise in global yields since March, and yields have risen more consistently than oil prices have over the last seven-plus months. But since the beginning of this month, the extension higher in oil prices has failed to drive global bond yields higher. Likewise, the US dollar switched into consolidation mode as yields rolled over, posting a brief peak on the hot US September CPI release last week before a sharp reversal that led to our call for a possible trend reversal. We need a bit more evidence that the US dollar is turning, but that remains our base case as long as we have a cap on US treasury yields. Technically, the USD move looks stretched short-term outside of USDJPY. For the next week to two weeks, the JPY is our chief focus for volatility potential far more than the US dollar.

Yesterday was especially interesting as US treasury yields saw their steepest plunge in months even as oil prices posted a new cycle high. Clearly the inflationary concerns from higher oil prices are being weighed against the risk that the supply-side shock of the higher energy input costs into the economy might trigger a recession. The focus yesterday for treasuries was clearly more on safe haven seeking as the US equity market suffered an ugly sell-off. Specific AI sector concerns may be far more important at the moment for equities than oil prices, but either way, the treasury market is the most important intermarket focus for the US dollar here. That being said, a US AI- and tech stock meltdown may be a US dollar risk if global investors who have poured into these stocks don't rotate into US treasuries in further safe-haven seeking.

For the FX Trader, the most interesting developments have been in CHF and JPY, as the plunging yields yesterday sparked an extension of the CHF strength and saw the JPY finally responding more forcefully to what I have posited should be the most supportive combination: lower yields and weak global risk sentiment. The final ingredient that would add even more support for JPY would likely be lower oil prices.

Takeaway: The US dollar is caught here in the crossfire of its safe haven status (USD positive) versus factors that have been thrown into reverse that were formerly supporting the USD rally (higher treasury yields, which now have just fallen steeply). This could eventually lead to a weaker US dollar if yields continue to retreat, but the USD versus risky currency equation could be choppy going if risk sentiment remains weak. Elsewhere, the potential is far greater for something interesting to develop based on the shift in global bond sentiment in the JPY and perhaps in USDJPY – see chart below.

Chart focus: USDJPY Even as one of the key trend indicators failed recently for the Ichimoku technical overview for USDJPY, the lagging span (green line) crossing back above the price bars, the other key

resistance levels have held, including the 200-day moving average in the 158.50 area and the Ichimoku cloud top near the same area. The big bounce overnight is uncomfortable for bears here, but next week is the critical time frame, given the technical setup here (test of resistance, which survived, while downside potential has yet to prove itself) and the FOMC and BoJ meetings are incoming. To the downside, the cloud level becomes “easier” to break in coming days as its lower bound rises slightly, while the lagging span will dip back through the price bars even if USDJPY stays near current levels. To get some downside momentum going, a breakdown through the 155.25-155.00 area is a next step. And the direction in bond yields may have far more to say than chart dynamics here for whether the downside materializes at all.

Looking ahead Next week we have no fewer than five central bank meetings: FOMC, BoC, ECB, BoJ and RBNZ. And for sterling we have the autumn budget statement on Wednesday after the brutal run lower in EURGBP – is that move getting overdone in the near term?

FOMC (Wednesday). The FOMC meeting is now seen very unlikely to bring a rate hike, while the market will desperately sift through the Warsh rhetoric and the statement for clues on the thinking for December, which is now only priced at 90% likely for a hike (+22.5 bps versus a high of +38 bps for the Oct & Dec meetings combined in late September). This meeting may rate low on market reaction potential.

Bank of Canada (Wednesday): The market is leaning heavily for a rate hike next week from Macklem and company after the Governor seemed to be guiding for one in comments over this last weekend: “The question we are going to be asking ourselves is, ‘Is inflation likely to come back down towards our target on its own, or are we going to have to raise interest rates to influence the path, nudge the path for inflation back towards the target?’” He also noted the risk of persistent inflation from higher oil prices. But with the CAD outperformance already in the price, not sure how much follow-on potential there might be now that the hike is mostly priced and another hike is fully in the price through the Jan 27 meeting.

ECB (Thursday): Some ECB members have been back-pedaling from former hawkishness as the vicious rise in energy prices – remember natural gas – have clouded the economic outlook. Some usual hawkish stuff from Germany's Schnabel, but Olli Rehn has said no second round effects in evidence and President Lagarde has stated that higher yields are already doing some of the ECB's tightening job. The key for the euro is the sovereign yield spread situation more than the ECB here. Market not pricing anything for this meeting and looking for a December hike instead, though now with less conviction – so there is some potential for surprisingly dovish (more likely?) or hawkish guidance to move the euro in either direction.

Bank of Japan (Friday): With the retreat in global bond yields and the rise in the JPY, we see the market marking the odds of a BoJ rate hike lower – that is logical. The market is not looking for a hike at next Friday's meeting, where I suspect intermarket forces (the combination of where US Treasury yields, risk sentiment and oil prices are) will weigh far more heavily than BoJ guidance. That guidance in turn will have a lot to do with where the JPY is as well – so look for hawkish guidance if the JPY is back lower and less hawkish guidance if the JPY is pulling to new local highs. December is still priced at better than even odds for a hike.

RBNZ: The market leaning heavily in favour of a hike after the hawkish shift in September, but watch guidance. Clear line in the sand on AUDNZD just under 1.2300 now.

FX Board of G10 and CNH trend evolution and strength. Note: If unfamiliar with the FX board, please see a video tutorial for understanding and using the FX Board.

Leading the G10 FX pack now we have the NOK, which has ground stronger versus the single currency

all weak as oil and gas prices ratcheted higher – EURNOK hit lowest level since late 2022. The JPY has flashed a very strong 2-day momentum reading after yesterday's action – let's see if it can get a persistent move higher going for the first time in a long time. Elsewhere, the euro continues to suck wind on the sovereign debt yield issue. If French bonds can finally rally, this negative focus might ease for a bit – not sure what fresh information we'll be getting in the nearest term – and lower yields elsewhere provide some relief at the margin.

Table: NEW FX Board Trend Scoreboard for individual pairs. In the new trends department, we have GBPUSD attempting to register an uptrend, but it is precisely mid-range here of the entire 2026 range and if we are lurching into a risk-off environment, do we want to have sterling exposure. Big test for sterling next week is the autumn budget statement on the 28th. Similar comments for USDCAD, which is hitting the key 1.4000 area and the market has already priced next week's BoC hike. The GBPJPY "uptrend" looks a red herring after yesterday's action and could be looking at a flip to negative within a day or two if we get follow-on JPY strength. Finally, the AUDNZD uptrend in focus here – with a move through the sub-1.2300 support needed to suggest a downside breakout is developing.

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