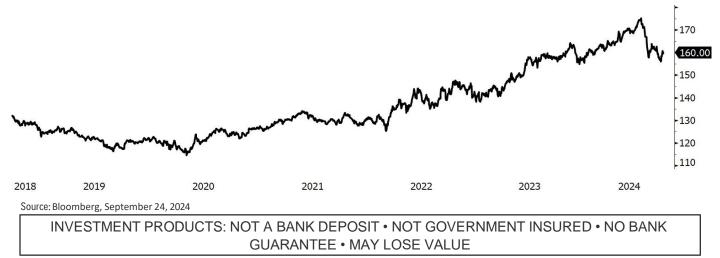
# EURJPY – Positioning For Yen Strength Via The Euro

3 October 2024					
Forecast (Sep 2024)	Spot	0-3m	6-12m	LT	
EURJPY	160.00	154.00	144.00	143.00	

- EUR is under the spotlight once again following the release of euro area September PMIs that point to a deepening manufacturing recession led by Germany while resilience of services seems to be fading too. Possibly of more concern to the ECB is a sustained reduction in new orders at their sharpest pace since January, alongside a new 10-month low in business confidence, making companies scale back their workforce for the 2nd successive month. The press release accompanying the data also adds that "demand weakness has resulted in slower inflation of input costs and output prices" with the former easing to their lowest since Nov'20.
- The PMI data ought to evoke a dovish response from the ECB but not so with Governing Council member Kazaks speaking after the PMI release saying that "the risk of service price inflation is still more significant at the moment" even as the data points to euro area manufacturing in contraction with rising concerns about sub-indices such as employment in particular which have also been weak lately.
- With ECB's "hawkish" inflation projections presented at the September meeting already dated as oil prices have dropped more than 10% since mid-August and with euro area growth fundamentals weakening further, the forces that apply pressure on inflation are mostly to the downside, as illustrated by the ECB's own assessment of moderation of wage pressure and weak domestic demand. This could see ECB terminal rate pricing shift substantially lower and weaken EUR as the Bank potentially finds itself behind the curve.
- Political risk also seem to be increasingly weighing on EUR as the new government appointed by French President Macron and led by Prime Minister Barnier has a very limited margin of maneuver, given the lack of a genuine power base in parliament. This raises the risk of continuing political instability and policy opacity in France beyond next year while the shift to the far right in regional elections in Germany, if seen, would potentially risk adding a further political risk premium to EUR.
- Meanwhile in Japan, BoJ Governor Ueda may have signaled a delay in further tightening by raising concerns about the US outlook at the BoJ's September meeting, but any weakness in Yen as a result is likely to be capped as Japan rates markets were not positioned for a BoJ October hike anyway and even if BoJ delays further tightening, USD-JPY rate compression at the short end will likely continue as the Fed embarks on further rate cuts. But the big difference for Yen from pre- August (before speculative accounts undertook to disorderly exit the yen-carry trade) and now is all the key domestic private players (Japanese funds, retail accounts, exporters) are aligned the same way looking to buy Yen on dips. This should cap JPY weakness and ultimately culminate in a more sustained decline in the EURJPY cross as the ECB moves deeper into its rate cut cycle.

# EURJPY has seen a one-way directional trajectory since 2020 but tide seems to be turning



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Highest quality	Aaa	AAA	AAA
High quality (very strong)	Aa	AA	AA
Upper medium grade (Strong)	Α	А	А
Medium grade	Baa	BBB	BBB
Not Investment Grade			
Lower medium grade (somewhat speculative)	Ba	BB	BB
Low grade (speculative)	В	В	В
Poor quality (may default)	Caa	CCC	CCC
Most speculative	Ca	CC	CC
No interest being paid or bankruptcy petition filed	С	D	С
In default	С	D	D

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