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Upcoming Economic Events (Singapore Local Time):

- 2021-08-16 07:50 Japan GDP (Q2)
- 2021-08-17 17:00 Eurozone GDP (Q2)
- 2021-08-17 20:30 US Retail Sales (July)
- 2021-08-18 10:00 RBNZ Interest Rate Decision
- 2021-08-19 09:30 Australia Unemployment Rate (July)
- 2021-08-20 09:30 PBoC Interest Rate Decision
- 2021-08-25 20:30 US Durable Goods Orders (July)
- 2021-08-26 20:30 US GDP (Q2)
- 2021-08-26 to 2021-08-28 Economic Policy Symposium in Jackson Hole

The annual Jackson Hole Economic Policy Symposium, to be held from 26th to 28th August, is the most anticipated economic event in the next two weeks. Global investors will look for any early signal from the Fed for potential policy changes facing an overheating economy.

Markets in Focus

Figure 1 Bloomberg Dollar Index



The US Dollar has been trading in an increasingly tighter range since the beginning of the year. The latest employment and CPI numbers continue to reflect a heated economic recovery in the US. More Fed officials are turning hawkish. Both are tailwinds for the US Dollar. We are closely watching the 1150 level on the Bloomberg Dollar Index, the breaking of which would suggest a potential reversal in the Dollar.

Figure 2 US 10-Year Treasury Yield



US 10-year treasury yield climbed to the high of 1.8% in March but has retraced 50% of the move since then. The retracement is arguably over after a double bottom in late July. 10-year yield sharply rebounded after the latest Nonfarm Payrolls release on 6th August.

Figure 3 Eurodollar Jun 2023 Future



The June 2023 Eurodollar future suggests that the interest rate market is pricing in fewer than three 25bps rate hikes by the FOMC meeting in June 2023. We could not help but wonder if the Fed will take more aggressive action when more data suggests inflation comes faster, higher, and stronger than expected.

Figure 4 Generic 1st Nikkei USD Future



Japan is still not ready to lift the state of emergency anytime soon because of the surge in Delta variant cases. With the Tokyo 2020 Olympic Games over, Japan's domestic economy will continue to face significant challenges, as seen in the Nikkei index, near completion of a potential descending triangle top.

Figure 5 Soybean Oil Dec 2021 Future



The December 2021 Soybean Oil contract has completed a textbook diamond top formation after a parabolic rally since last year. It is highly probable that Soybean Oil price will pull back a lot more from here.

Market Views

The July CPI number printed 5.4%, the highest since August 2008. The July Nonfarm Payrolls also beat market consensus by 73k more jobs, showing healthy recovery in employment. Facing the overheating economy, the Fed is becoming increasingly hawkish. Dallas Fed President Robert Kaplan was among the latest officials to suggest that the central bank should begin to taper its monthly bond and MBS purchases soon.

The most notable market reactions include a sharp rebound in Treasury yields and a strong bid in the US Dollar. We are paying close attention to the US Dollar near the upper resistance of an 8-month consolidation range. We will likely see the US Dollar breaking out and heading meaningfully higher if the Fed signals to dial back the accommodative monetary policies early via tapering or rate hikes. A strengthening Dollar is a massive headwind for commodities, especially after the parabolic advances enjoyed by most of them in the past 12 months.

As suggested in the [previous issue](#), the US equities are mostly unaffected as both S&P and Dow Jones Industrial Average made new all-time highs in the past week. The situation in Japan, however, is not so rosy. While the whole world has been awed by the Olympians' grits, pursuit of excellence and sportsmanship at the Tokyo 2020 Olympic Games, the absence of tourists and the impact of the pandemics have left Japan with some huge financial losses that cannot be quickly recouped. Given the surge in new COVID cases and an extended state of emergency, we can only expect the Japanese economy to diverge further from other countries such as the US.

How to play the theme out

A hypothetical investor can consider the following three trades¹:

Case Study 1: Short Nikkei USD Future

If the investor were to short the Nikkei USD future (NKDU1) at around 28100 and set the stop at 29500, his maximum loss per contract would be $(29500 - 28100) \times 5 = 7000$ USD. An initial measured target points to 24000, resulting in $(28100 - 24000) \times 5 = 20500$ USD.

Case Study 2: Short Soybean Oil Future

If the investor were to short the Soybean Oil future (ZLZ1) at around 61.4 and set the stop at 65, his maximum loss per contract would be $(65 - 61.4) \times 600 = 2160$ USD. An initial measured target points to 50, resulting in $(61.5 - 50) \times 600 = 6900$ USD.

Case Study 3: Long Eurodollar June 2023 99x98.5 Put Spread

If the investor thinks the Fed will hike rates more and faster than currently being priced in, he could buy the Eurodollar June 2023 99x98.5 vertical put spread (EDM3 9900P – EDM3 9850P) at 0.08. The maximum loss would be the premium of $(0.08 \times 2500) = 200$ USD if EDM3 future settles above 99 by expiry, i.e., the LIBOR rate is still below 1% by then. The maximum potential payoff of this position would be $(99 - 98.5) \times 2500 = 1250$ USD less the premium paid (200 USD) if EDM3 future settles below 98.5 by expiry, indicating the LIBOR rate is higher than 1.5% by then.

¹ Examples cited above are for illustration only and shall not be construed as investment recommendations or advice. They serve as an integral part of a case study to demonstrate fundamental concepts in risk management under given market scenarios.

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The trainers and researchers in ITS have been regularly speaking on various exchange/broker hosted trading seminars and writing for various research publications over the years. Catering to both aspiring and experienced traders, we want to help in bridging the void between the theoretical and practical aspects of derivative trading, with guidance from our team of seasoned and active traders.

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