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Global

FX Flash

JPY Climb - Will it Continue?

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JPY Sees Sharp July Climb

Since the 11 Jul 2024 when an intervention was suspected to have occurred, we have seen the USDJPY fall by about 5.89% at time of writing, which is roughly equal to the amount of 8 – 9 big figures. The steep fall has caught market attention and not surprisingly given how stretched JPY short positions, the moves for the currency can be violent and aggressive once strengthening momentum starts to take hold. The question at this point though is what actually caused this strengthening to take place. Although there are various factors being speculated upon, it is very possible that an unwind in the JPY funding carry trade has driven this rally somewhat. There are a few reasons that could be driving this JPY carry unwind which includes:

1. **Global central banks tilting dovish amid expectations of BOJ turning more hawkish:** In the last few weeks, we have already started to see a number of central banks start to ease. The BoC has already cut by 50bps so far amid concerns of downside risks ECB has already done so by 25bps and actually has tilted more dovish. Lagarde herself has also warned of downside risks and another 25bps cut in Sep is looking more likely. The RBA similarly too looks more dovish. More Fed officials are hinting at the possibility of a cut coming in Sep. Meanwhile, markets are also cautious of the possibility of the BOJ tilting more hawkish at next week's Jul meeting and undertaking a rate cut. Therefore, under these circumstances, the JPY funding carry trade would start to look less attractive.

2. **Rising risk - off sentiment going into Aug month:** Across various asset classes, we are seeing investors turning cautious and beginning to sell off as we build up to a period of lower liquidity in Aug. Particularly in equity markets, tech stocks have been taking quite a bit of a hit recently as investors close off positions. Currencies similarly look to be facing the same situation as investors sell off in high yielders and close off their funding positions with the JPY or CHF. We do note that sharp falls in JPY in Jul has not just happened in 2024 but also in 2023 and 2022.

3. **Supportive JPY comments from politicians:** We do note that comments from both Japanese political figures and US Presidential candidate Trump may have helped to sustain a strengthening momentum and support more unwinding of the carry trade. Digital Minister Taro Kono had mentioned that the "yen is too cheap and we need to bring it back up" whilst LDP Secretary General Motegi said, "excessive yen declines are clearly negative for Japan's economy". Donald Trump himself meanwhile said that the US has a "big currency problem" because of the weakness of yen and yuan. Such words make it appear like a future potential US administration and Japanese government may only be more comfortable with seeing that the JPY weakness is stemmed.

4. **Intervention timing was quite apt:** The suspected intervention on 11Jul 2024 looks to have been quite well timed as it acted as a start for the strengthening momentum just ahead of the favorable developments. The action had occurred just as US CPI had come out softer than expected, which raised the likelihood of a Fed cut coming in Sep 2024. The intervention move had also

occurred ahead of the developments that we have mentioned in the earlier points.

5. **Higher Volatility Supports Carry Unwind:** The increase in the volatility of the JPY is also possibly deterring parties from continuing to sell the currency. Investors are also therefore choosing to unwind their carry trade JPY funded positions consequently. If we look within Asia, from a carry return sharpe ratio perspective, we see that the THB, TWD and KRW are the three hardest hit. We also take note that the unwind of the JPY funded carry trade could be leading to widespread cross-asset liquidation (amid massive deleveraging) causing a rise in volatility globally.

Can the JPY Strengthening Momentum Persist?

Our own forecast sees the USDJPY higher from current levels in 3Q 2024 before coming off in 4Q 2024. We are sticking to our forecast at this point although we do note it also depends how the BOJ meeting pans out next week. We are of the view that BOJ is unlikely to hike at the Jul meeting given they would want to see a few more months how data pans out, especially regarding the extent the strong Spring wage negotiations results feed into higher wages and consequently into consumption and inflation. As it is, economic conditions still look fragile and core core inflation has actually been softening towards the 2.0% target making a BOJ hike decision more complex. We do though think that economic data should improve building up to the Oct 2024 meeting allowing for a 15bps hike then. The BOJ holding back in the near term on a hike as we see it would instead lead to some pullback in the JPY recent strength. Furthermore, as we head deeper into 3Q 2024, we are inclined to believe that central banks other than the BOJ that are leaning dovish (such as the ECB) may want to play down market expectations of them aggressively easing. Inflation is still only gradually softening and global central banks may not be keen to quickly allow financial conditions to ease too quickly. The Fed we think for one is unlikely to express too dovish a tone even if they cut in Sep given they may not wish for financial conditions to loosen too much. This can have its own effect on the pace to which EM central banks (Note: high-yielding EM currencies are major part of the JPY funding carry trade) would ease this year.

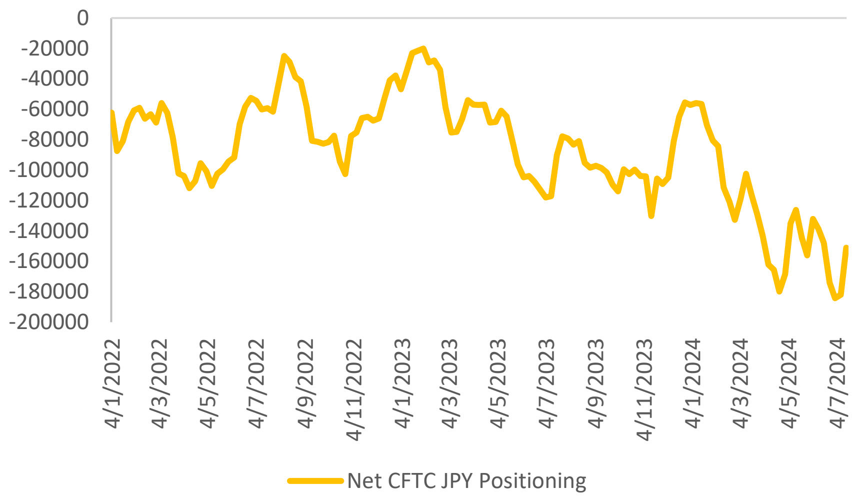
However, as we move into year-end, we actually expect that the USDJPY should come off on the basis that the easing cycle of global central banks would become more entrenched. The Fed would likely be more clear on its easing cycle by then and this would induce EM central banks to cut too. Other DMs such as the ECB would possibly too. We also note of economic risks to Europe in the case of a Trump victory given his talk of 10% tariffs on imports from the rest of the world other than China. This can place more pressure on the ECB to cut rates. JPY funded carry trade could therefore become less attractive over time.

Near term, we do not rule out the possibility of further USDJPY downside. We are now closely watching the 152.00 support level which it is currently testing. Next level of supports after that is at 151.54 and 150.00. We remain cautious on the JPY going into next week. There could be more downside in the run up to the BOJ meeting next week as the short squeeze could persist. Rick events in the next few days include the release of the US Jun PCE core index tomorrow where it is expected to soften on a yearly basis. That data point itself also builds up to the FOMC next week, where markets would be keeping a close eye on what the Fed tone would be amid other recent softening data points. Markets could keep staying on the edge building to these events, which can support more JPY funded carry unwind.

Table 1: USDJPY Forecast

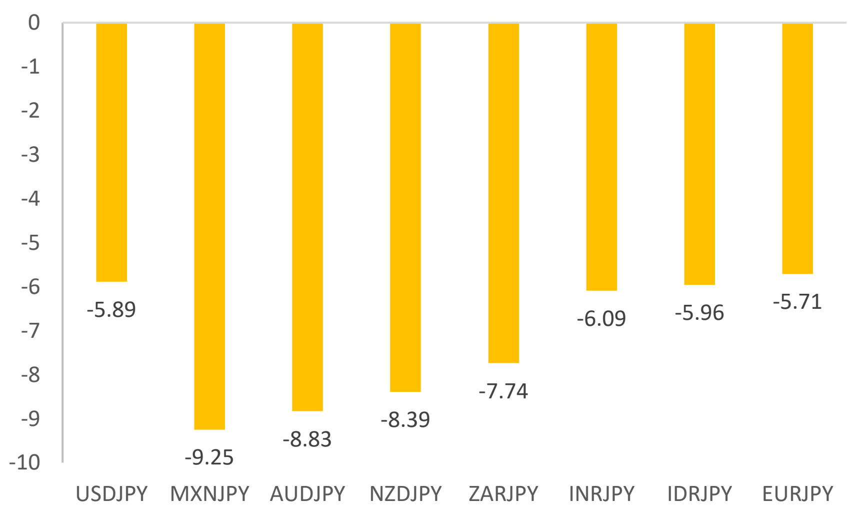
Forecast	3Q 2024	4Q 2024	1Q 2025	2Q 2025
USDJPY	165.00	160.00	152.00	150.00
JPYSGD	0.82	0.83	0.88	0.89
JPYMYR	2.82	2.88	2.99	3.00

Chart 1: Stretched Short JPY Positions have Made JPY Moves More Violent



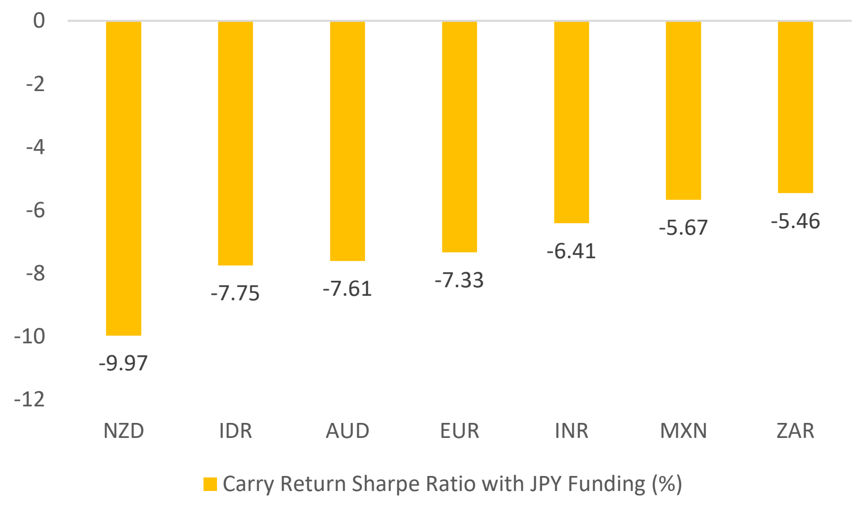
Source: Bloomberg, Maybank FX Research & Strategy

Chart 2: USDJPY Falls in Line with a Decline in Other Higher Yielding Crosses with JPY since 10 Jul



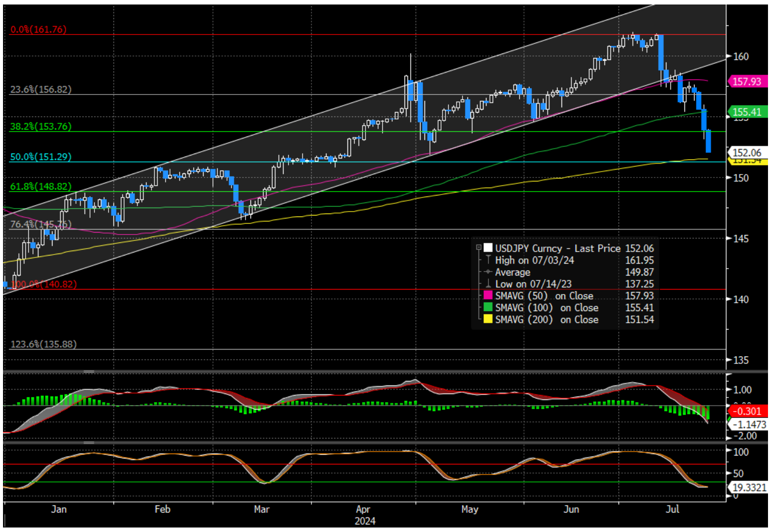
Source: Bloomberg, Maybank FX Research & Strategy
Note: Spot returns calculated from the dates of 10 Jul 2024 to 25 Jul 2024

Chart 3: Carry Return Sharpe Ratios Stand Strongly Negative over the Last Month for a Number of High Yielders with JPY Funding



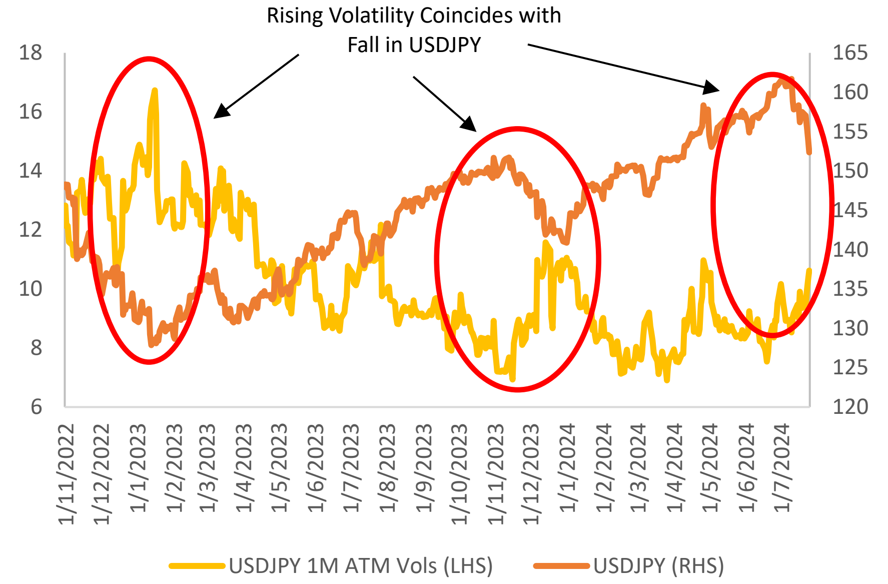
Source: Bloomberg, Maybank FX Research & Strategy
Note: Carry Return is calculated from 10 Jul 2024 - 25 Jul 2024

Chart 4: Key Support Levels at 152.00, 151.54 (200-dma) and 150.00



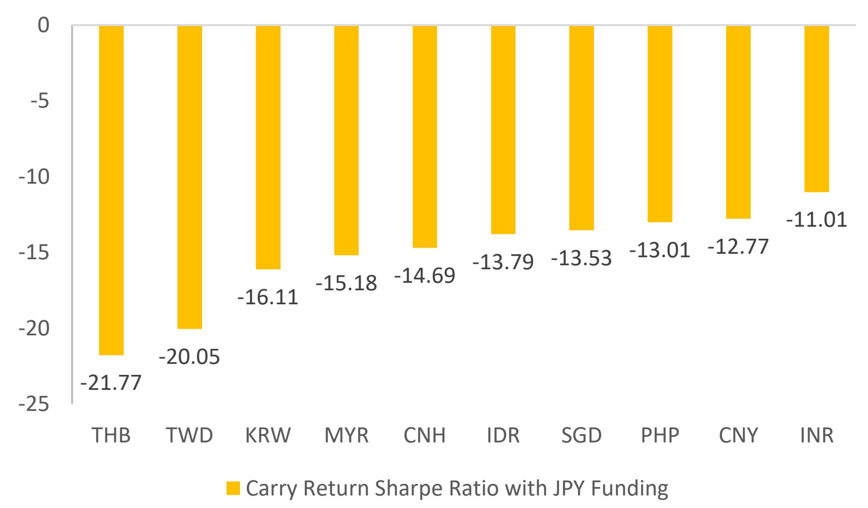
Source: Bloomberg, Maybank FX Research & Strategy

Chart 5: Rising Volatility Deters People from Selling the JPY, Supporting JPY Funded Carry Trade Unwinds



Source: Bloomberg, Maybank FX Research & Strategy

Chart 6: Carry Return Sharpe Ratios for Asia in the Last Five Days



Source: Bloomberg, Maybank FX Research & Strategy
Note: Carry Return is calculated from 18 Jul 2024 - 25 Jul 2024

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