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The Yen's divine wind

July's events are likely to leave a lasting and profound impact on the global financial market infrastructure. The developments in question were not directly related to geopolitics, despite the breakdown of the fragile truce in the Middle East, nor were they driven by the unprecedented repricing and sell-off in AI-related equities. Instead, the focus was on the foreign exchange market, where Japanese authorities conducted the largest intervention operations ever seen in an effort to support the Japanese yen.

While Japanese authorities have intervened in currency markets before, what made the events of the final week of July truly exceptional, and arguably once-in-a-generation developments, was the reported participation of US authorities.

The yen entered July close to four-decade lows, with 'fast money' holding most bearish positioning since 2007, amounting to nearly 138,000 net short contracts. Carry trade conditions were described by some of the market's key participants as the most attractive since 2000. On 30 July, the yen surged more than 3.3% intraday against the US dollar, reaching 157.98 and recording its largest single-day gain since December 2023, amid reports of Japanese authorities intervening to purchase yen. Subsequent Bank of Japan data suggested that approximately ¥8.45 trillion (around $53 billion) was spent on 30 July alone, likely representing the largest single-day currency intervention on record.

Reports indicated that Japanese authorities intervened again on 31 July, marking a second consecutive day of market action. Most notably, the US Treasury was reported to have sold euros and purchased yen through the Federal Reserve Bank of New York, representing an unusual degree of bilateral coordination that some market participants described as a potential "new normal" in foreign exchange intervention.

Turning to the US dollar, it entered July following a strong June. The Bloomberg Dollar Spot Index had risen by 2% during June, its strongest monthly performance since the outbreak of the Iran conflict, driven largely by expectations of further Federal Reserve tightening under Chairman Kevin Warsh. However, that momentum faded rapidly as investors reassessed the Federal Reserve's willingness to continue tightening policy.

This reassessment was reinforced at the Federal Open Market Committee meeting, where interest rates were left unchanged at 3.50%-3.75% following a 9-3 vote.

The decision disappointed dollar bulls, with speculative long US dollar positions having reached their highest level since 2014 ahead of the meeting. Consequently, the Bloomberg Dollar Spot Index recorded its worst weekly performance in more than three months, falling 1.3% during the final week of July.

Sterling, by contrast, was one of the month's relative outperformers. The Bloomberg British Pound Index reached a one-year high in the middle of July. Reports that incoming Prime Minister Andy Burnham would appoint a market-friendly Chancellor of the Exchequer were widely cited as a catalyst for the pound's broad-based strength.

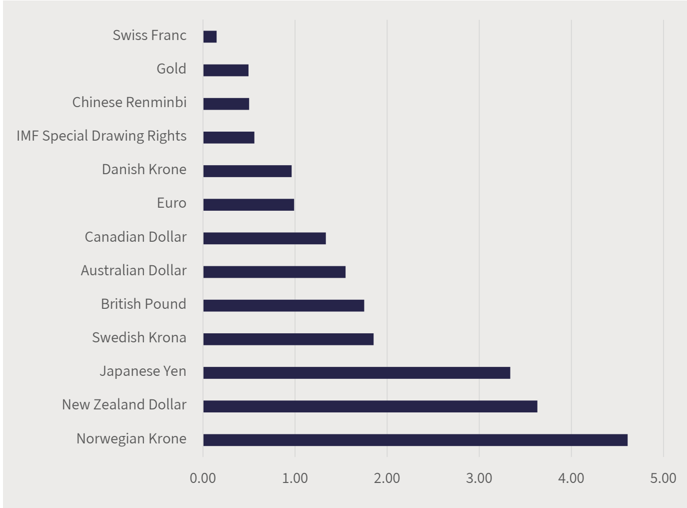
In summary, July was a highly volatile month for foreign exchange markets, characterised by a weakening US dollar, a dramatic intervention-driven recovery in the yen, and persistent inflation-related uncertainty surrounding central bank policy. The UU Dollar Spot Index (DXY) declined 1.26% over the month and closed below the 100.00 level. Among G10 currencies, the Norwegian krone was the top performer, followed by the New Zealand dollar and the Japanese yen. Both major European currencies fared well against the US dollar, with EUR/USD rising 0.99% and GBP/USD advancing 1.75%.

Nevertheless, they finished the month in the middle of the performance rankings (please refer to the accompanying table for details). Meanwhile, the Chinese renminbi recorded another stable and positive month, appreciating to levels (USDCNH closed the month at 6.7500) the level not seen since March 2022!

Looking ahead, it remains extremely difficult to assess the full implications of the recent developments in the yen. For many years, the yen has served as the primary funding currency for a wide range of leveraged investment strategies across asset classes. Given that the credibility of both Japanese and US authorities now appears to be directly linked to the success of these interventions, investors who previously viewed betting against the Bank of Japan as a one-way trade may be forced to reassess their strategies and adjust risk exposures accordingly. Such repositioning would likely add to what is already an elevated level of uncertainty across global financial markets.

The following chart shows the yield on 5-year Japanese Government bonds and the JPY exchange rate.

July performance vs. USD (%)



Source: Bloomberg Finance L.P., 31 July 2026.

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