Daiwa's View

Intervention, rate check, then intervention again?

- It is highly likely that currency intervention was conducted on the 11th, but determining whether it occurred on the 12th is difficult

FICC Research Dept

Kenta Tadaide
81-3-5555-8466
kenta.tadaide@daiwa.co.jp

Kenji Yamamoto
81-3-5555-8784
kenji.yamamoto@daiwa.co.jp

Daiwa Securities Co. Ltd

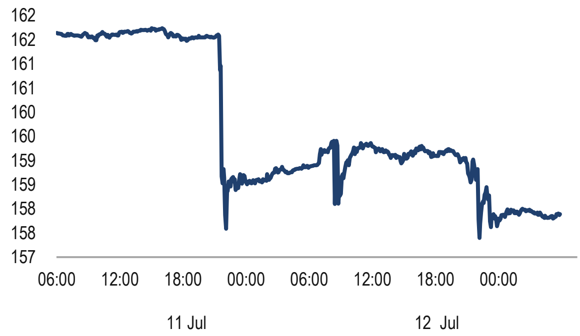
Intervention, rate check, then intervention again?

During New York trading hours on 11 July, the USD/JPY rate plunged (Chart 1). Since the beginning of July, the USD/JPY rate has been testing Y162, and, on the 11th, it seemed likely that the rate had become fixed in the upper range of Y161. However, in response to the US CPI report for June, the rate fell below Y161, and then rebounded to around Y161. From that point, yen-buying suddenly intensified, leading to a decline to the Y157 level at one point. The initial reaction was selling of the dollar triggered by US CPI readings that were much weaker than market estimates. However, Japanese monetary authorities appear to have implemented currency intervention on top of such selling.

The latest currency intervention was not implemented immediately after the yen renewed its recent low, which probably surprised the market. Also, in terms of the timing, the authorities may have intended to reproduce the "reverse CPI shock" that occurred on 10 November 2022. Looking back at the currency intervention in 2022, the authorities implemented yen-buying/dollar-selling intervention on 22 September for the first time in about 24 years as the USD/JPY rate substantially exceeded Y145. After that, the rate topped Y150 on 21 October, and then intervention was repeated on the 21st and the 24th in the following week. Eventually, the USD/JPY rate posted a downtrend after reaching its peak on 21 October. From then on into January 2023, the yen strengthened to the Y127 level, partly due to the boost from the "reverse CPI shock."

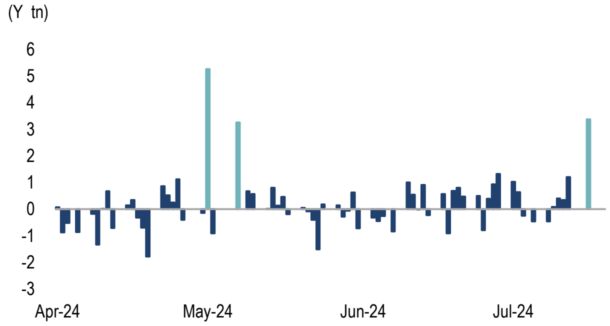
On the night of 11 July 2024, Vice Minister of Finance Masato Kanda stated that the authorities were not in a position to comment whether or not intervention had been conducted. However, TV Asahi reported that Government sources said that the government/BOJ had implemented currency intervention. Mainichi Newspapers also reported that Government sources disclosed that the Japanese government/BOJ had implemented yen-buying/dollar-selling currency intervention.

Chart 1: USD/JPY Rate on 11 and 12 Jul



Source: Bloomberg; compiled by Daiwa.

Chart 2: Divergence from Projections for Treasury Fund and Other Sources of Changes in Current Account Balances at BOJ Since Beginning of Month



Source: BOJ, Ueda Yagi Tanshi; compiled by Daiwa.

On the morning of the 12th, Mr. Kanda made a comment regarding the fact that some news stories had reported that government officials had admitted that currency intervention had been implemented, stating that it was hard to imagine government officials making such comments, even if intervention had taken place, and that the number of parties concerned was limited considering the absolute need to avoid insider transactions, and that those in the know might be limited to as few as a handful of people.

We are not sure if what the leaked articles claim is true. However, it is highly likely that intervention was indeed implemented based on projections for changes in current account balances at the BOJ, as already reported. The BOJ announced that the projection for Treasury Fund and other sources of changes in current account balances at the BOJ on the 12th and the 16th was minus Y3,170bn. The projection announced at the beginning of the month was plus Y200bn. Therefore, we estimate that the difference, Y3,370bn, indicates the scale of yen-buying intervention (Chart 2). In the movements, which appear to have been caused by intervention, the yen strengthened by around Y3.5 vs. the dollar from around Y161 to about Y157.5. Therefore, the difference is consistent with estimated price movements in which intervention changes on a scale of Y1tn were roughly equivalent to a Y1 change in the USD/JPY rate.

Also, on the 12th, there was nervousness in USD/JPY trading due to speculation about foreign exchange intervention. On the morning of the 12th, there were news reports that the BOJ had implemented a "rate check" against the euro. The check against the euro is new. According to MOF data since April 1991, the dollar is the only counterparty currency for yen-buying intervention. From 1999 to 2003, euro-buying/yen-selling intervention was conducted every year. However, if euro-selling/yen-buying intervention were implemented, this would be the first case. In fact, the EUR/JPY rate hit Y175.42 on the 11th, which is a record level (hitting a record high) since the start of the euro in 1999.

In response to the rate check by the BOJ, the yen strengthened with the EUR/JPY rate falling from the lower half of the Y173 range to around Y171.5, and the USD/JPY rate declining from the lower half of the Y159 range to the upper half of the Y157 range. However, within two hours, the yen had been roughly restored to the level it was at before the rate check. Nevertheless, the yen suddenly strengthened during New York trading hours, with the USD/JPY rate falling to the lower half of the Y157 range and the EUR/JPY rate declining to around Y171.5, both of which were strong levels on the 11th. Regarding these movements, a view is emerging in the market that currency intervention was also conducted on the 12th for the second consecutive day.

That said, if we assume that intervention was actually implemented on the night of the 12th, the scale of the intervention would be smaller than that on the 11th. The USD/JPY rate declined by around Y1.5. If we assume that intervention changes on a scale of Y1tn were roughly equivalent to a Y1 change in the USD/JPY rate, we estimate that the amount of actual intervention was limited to Y1.5tn. We should confirm the projections for changes in current account balances at the BOJ that are to be announced tonight, but it may be difficult to determine whether intervention of this scale definitely occurred.

Projections for Treasury Fund and other sources of changes in current account balances at the BOJ fluctuate by several hundred billion yen. When large fluctuations occur, the difference exceeds Y1tn. Therefore, when intervention on a scale of around Y1.5tn occurs, it is difficult to determine whether the divergence from the amount projected in advance was the result of intervention or fluctuations in treasury funds and others sources.

Either way, in the near term, the market is likely to become more concerned about currency intervention if the USD/JPY rate reaches around Y162. Meanwhile, the USD/JPY rate has not yet posted a clear downside breakout vs. the 50-day moving average line. The focus of attention will be whether the Dollar Index and/or the USD/JPY rate will decline further amid the downtrend in the US long-term rate. If a correction in the USD/JPY rate were to continue, Y155 would be regarded as a point of reference for the lower limit for now.

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