

FX Viewpoint

Currencies
Global

AUD and JPY: Central banks' policies vs risk appetite

- ◆ The RBA delivered a hawkish hold on 6 August, and the BoJ unexpectedly hiked rates to 0.25% on 31 July
- ◆ While yields are likely to remain important for FX, risk appetite is becoming a more dominant force
- ◆ Over the near term, if risk sentiment worsens, the AUD is likely to take a hit, but the JPY could strengthen further, in our view

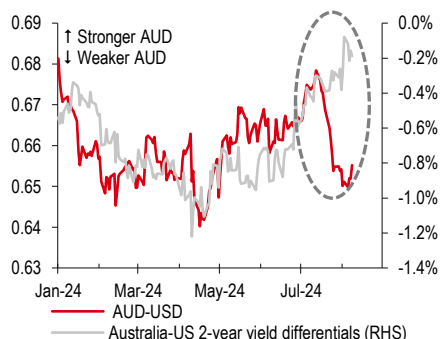
Over the past 30 days (ended 8 August), the AUD was the second worst performing currency in the G10 space, losing 2.2% against the USD (and only outperforming the NOK, which lost 2.4% against the USD), while the JPY's performance topped the list, gaining almost 10% against the USD (*Bloomberg*, 8 August 2024).

The JPY has benefited from global risk aversion and the recent stock market selloff, given its "safe haven" status. Domestic developments, like FX intervention in July by the Ministry of Finance and **an unexpectedly hawkish Bank of Japan (BoJ), which hiked rates to around 0.25% on 31 July**, also helped boost the JPY.

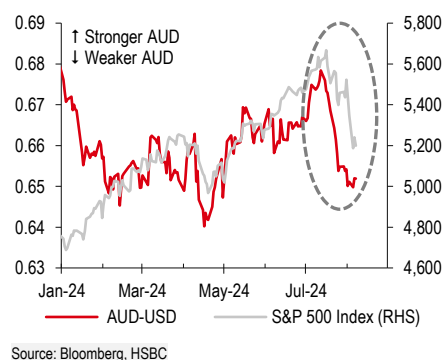
Over the near term, **if risk sentiment deteriorates, the JPY could strengthen further**. Conversely, **should markets become less pessimistic on the US economy, the JPY is likely to weaken** amid the wide yield differential between Japan and the US. Looking beyond the near-term volatility, we still expect the JPY to have a modest recovery against the USD, as the yield differential between Japan and the US will be closing gradually.

As for the AUD, we expect the currency to have a bumpier upward path against the USD in the months ahead. Domestically, the Reserve Bank of Australia (RBA) kept its policy rate unchanged at 4.35% on 6 August, although a hike was considered. The RBA remains more concerned about still too high inflation than weak growth. **Our economists still expect the RBA to remain on hold through 2024, with rate cuts beginning only from 2Q25**. Charts 1 and 2 show that AUD-USD seems to open up the gap with its yield differential, but to take cues from risk appetite (with the S&P 500 Index as a proxy).

1. AUD-USD and its yield differential



2. AUD-USD and risk appetite



US data releases will remain essential going into September. **Any notable deterioration in US data** will raise concerns of a synchronised global slowdown and fears of a US recession, **likely weighing on the AUD**. However, **if data suggest disinflation and resilient growth from the US**, AUD-USD could rise amid monetary policy divergence and risk appetite.

Recent JPY strength was triggered by global risk aversion and domestic developments

We still see the JPY recovering modestly against the USD over the medium term

AUD-USD seems to be taking cues from risk sentiment, rather than its yield differential as of late

US data releases will be key for AUD-USD over the near term

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