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Japanese yen plummets to 32-year low against the U.S. dollar

The exchange rate of Japanese yen against the US dollar recently plummeted to its lowest rate in 32 years – JPY 147.66 per dollar. The yen's latest decline occurred less than a month ago, with the September slide prompting authorities to intervene in the currency market for the first time since 1998.

Increased spreads between US treasuries and Japanese government bonds

The Japanese yen fell to a rate of 147.66 per dollar, its lowest exchange rate against the U.S. dollar in 32 years, a report said. The yen's latest record drop came after official U.S. figures showed prices rose faster than expected. The U.S. Federal Reserve has resorted to rate hikes to curb inflation, but these hikes have in turn led to a strengthening of the Dollar against other world currencies.

However, unlike other central banks that followed in the footsteps of the U.S. Federal Reserve and raised interest rates, the Bank of Japan (BOJ) reportedly maintained a "ultra-light monetary policy". Investors in turn reacted to the resulting spread between U.S. Treasuries and Japanese government bonds by selling the yen.

In September, when the rising dollar drove the yen to a 24-year low against the greenback, the BOJ responded by intervening in the foreign exchange markets for the first time since 1998. According to a BBC article, the Japanese authorities are again likely to respond to the yen's latest plunge with further intervention.

The report quotes Japanese Finance Minister Shunichi Suzuki as suggesting that "appropriate measures"will be taken to prevent the yen from continuing to slide.

“We cannot tolerate excessive volatility in the currency market due to speculative movements. We monitor currency movements with a strong sense of urgency”, Shunichi Suzuki was quoted as saying.

Prevent “negative financial amplification”

In late September 2022, when the Japanese currency fell by more than two yen in one day against the dollar, the Japanese authorities responded by spending nearly $20 billion. While the intervention helped stabilize the yen, some analysts question the sustainability of such a solution.

However, in a new blog post, the International Monetary Fund (IMF) suggested that a temporary intervention in the foreign exchange market might be the most appropriate solution. As the blog explains, such an exchange rate intervention can *“help prevent negative financial amplification if a sharp depreciation increases risks to financial stability, such as corporate failures, due to currency mismatches.”*

The IMF notes that in addition to helping reduce threats to financial stability, intervention in foreign exchange markets has the potential to help a country’s monetary policy.

“Finally, temporary intervention can also support monetary policy in rare circumstances where a sharp depreciation of the exchange rate could unanchor inflation expectations, and where monetary policy alone cannot restore price stability“, explains the IMF blog.