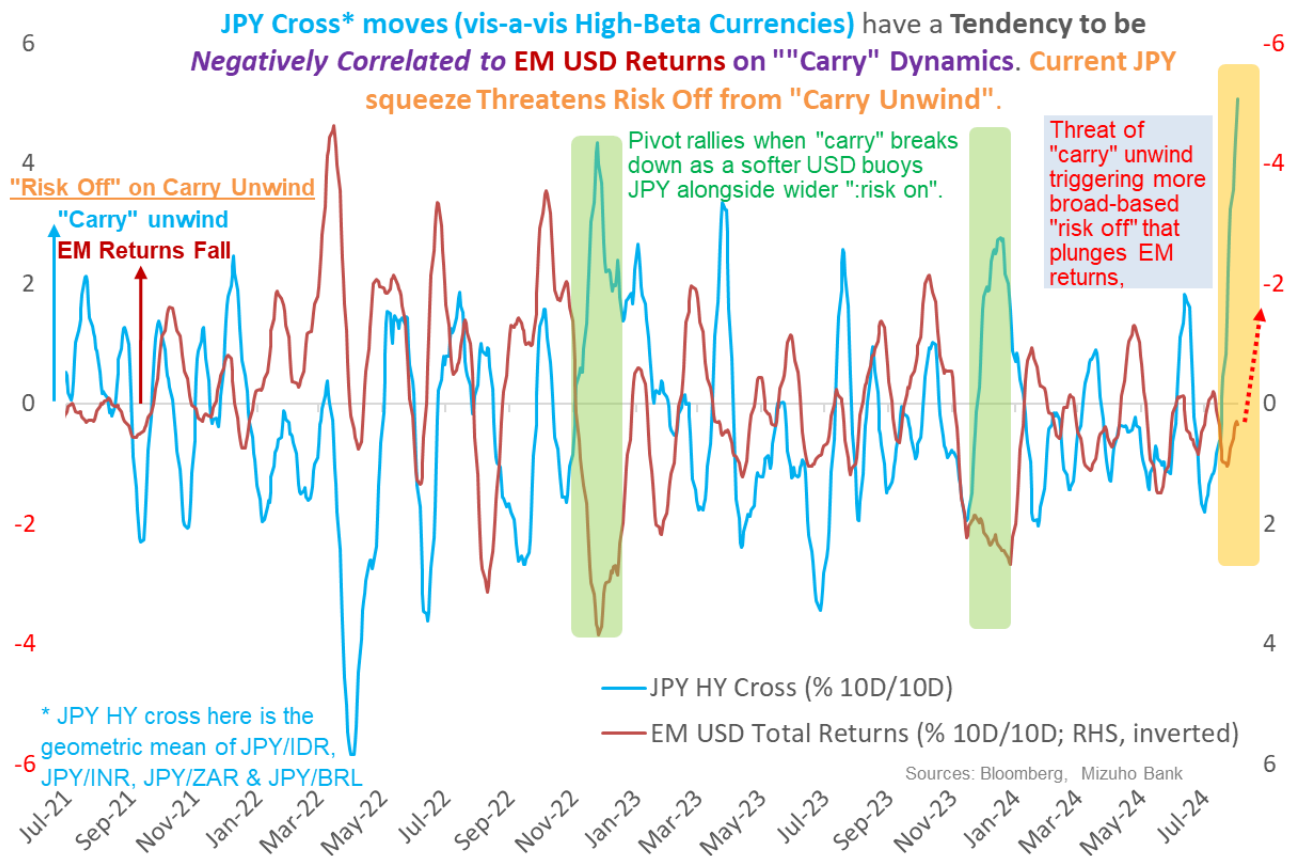


Carry Unwind – Neither “Carry Nor Calm



“A man that flies from his fear may find that he has only taken a short cut to meet it.” – J.R.R Tolkien

- The **JPY squeeze** since 10th July* has been **particularly acute**, with the JPY *surging some 8-9% in just over 3weeks*.
- This has inevitably resulted in **some degree of unwind in JPY-funded “carry trades”**.
- Specifically, as the sharp JPY surge imposes **exchange-rate losses that overwhelm “carry” returns** (from JPY-funded investments in high-yielding assets), ultimately forcing liquidation.
- The silver lining is that **a wider contagion that triggers a sustained meltdown in EM/risk assets** have been *averted thus far*.
- Partly because the **JPY squeeze**, and **resultant “carry unwind”**, has been *due to a build-up of events***, *not an uncontrolled blowout of risk aversion*.
- But the **dark clouds of adverse feedback loop** between **“carry” liquidation and “risk off” contagion** cannot be ignored.
- Point being, the sheer magnitude of JPY squeeze warns of a more emphatic “carry” liquidation with knock-on impact on risk assets.

- Especially if **JPY-equities** and **JPY-EM FX correlations** turn *profoundly and pervasively negative*.
- *Counsel to “keep calm and carry on” will get no love.*
- But to avoid self-reinforcing panic, is perhaps the more critical thing for markets to avert a deeper sell-down.
- That said, **caution rules the roost** as sustained JPY/CNY wedge favours keeping away from HY Cross/JPY.

*Corresponding to a plunge in USD/JPY from 162 to sub=150

** From Trump’s rant on exchange rate/mercantilism to opportunistic intervention on the “Trump trigger” to BoJ rate hike.

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