What’s Hot: positioning for a stronger yen

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Key Takeaways

- As the Bank of Japan prepares to raise interest rates, the yen carry trade is entering a critical phase that could trigger widespread cross-asset volatility.
- An abrupt unwind of yen-funded positions could force rapid deleveraging across equities, foreign exchange, credit, and crypto, but a gradual shift would allow investors time to reposition.
- Investors can navigate the volatility through currency-hedged Japanese equity strategies and targeted JPY exchange traded products for hedging or directional positioning.

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At the start of December 2025, Bank of Japan (BoJ) Governor Kazuo Ueda delivered his clearest signal yet that a rate hike may be imminent. Markets reacted instantly and the Japanese yen (JPY) jumped roughly 0.6% against the US dollar (USD) as investors recalibrated expectations for Japan’s policy path.

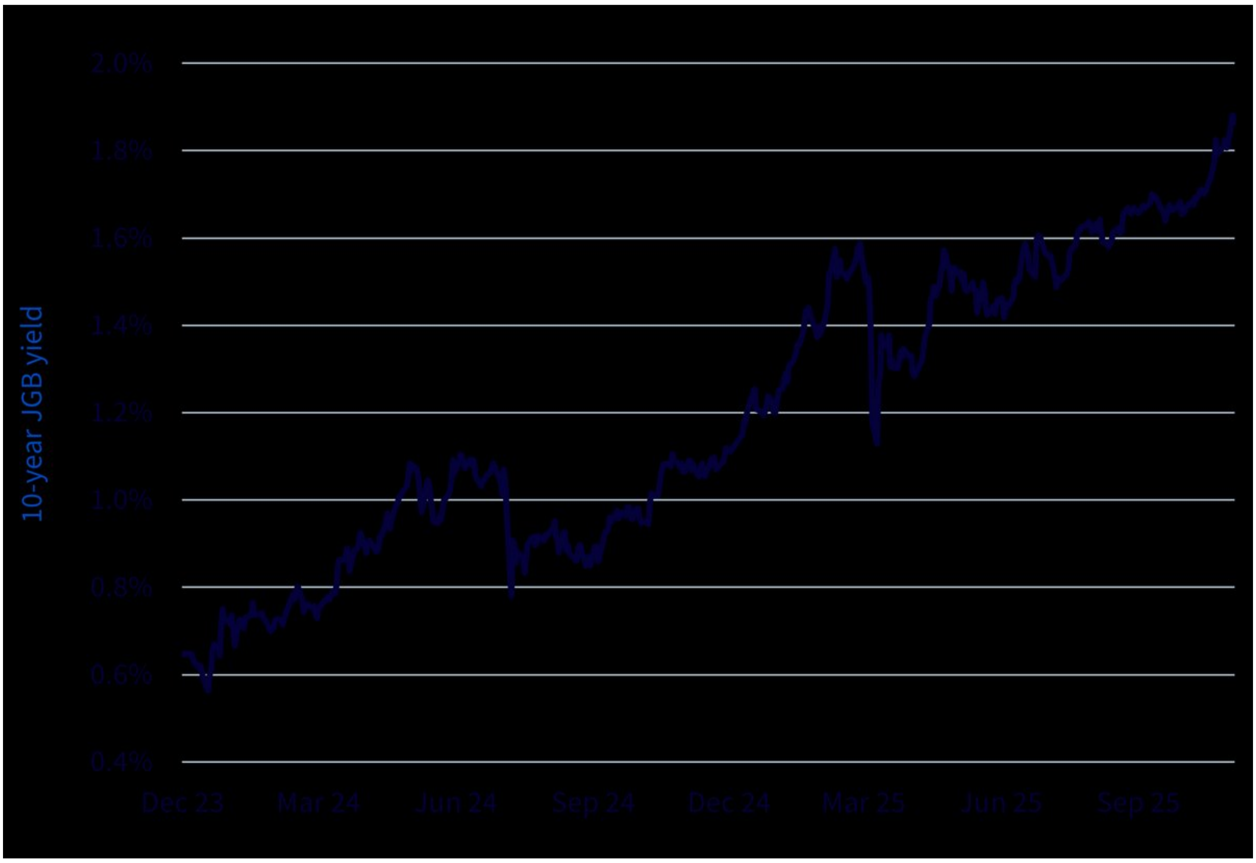
For a currency long used as the world’s cheapest source of funding, even subtle shifts matter. With Japan now deep into its first tightening cycle in decades, those signals point toward one dominant theme: the unwinding of the yen carry trade.

The trade: simple mechanics, high stakes

The yen carry trade is built on a simple idea: borrow in Japan at very low rates and deploy the capital into higher-yielding assets abroad. But that simplicity masks growing vulnerabilities as Japan exits its era of ultra-easy money.

Bank for International Settlements (BIS) data shows yen-denominated credit to non-residents grew 6% year-on-year in Q1 2025, reaching JPY 65.6 trillion1. Growth remains positive, but it has slowed steadily since Q3 2024, right after Japan began tightening and carry exposures began to unwind. This marked a clear downshift from the double-digit annual expansions seen in the years prior.

Figure 1: 10-year Japanese Government Bond (JGB) yield



Source: Interest Rate : Ministry of Finance. 02 December 2025. **Historical performance is not an indication of future performance, and any investment may go down in value.**

As Figure 1 illustrates, the 10-year Japanese Government Bond (JGB) yield climbed from 0.65% at the end of 2023 to 1.86% by early December 20252. The ascent reflects a decisive departure from ultra-accommodative policy. First through adjustments to Yield Curve Control, then its removal, and finally the BoJ's early rate hikes and reduced bond purchases.

The 10-year JGB has become a clean visual proxy for a regime shift as markets are now pricing in sustainably positive inflation and wage growth, after decades where deflation was the norm.

The timing: gradual vs abrupt unwind

With monetary tightening underway and funding costs rising, the debate is no longer if the carry trade unwinds, but how. Markets will price the difference aggressively.

If the unwind remains gradual:

- Funding costs rise in manageable steps, giving leveraged investors time to pare back risk.
- Yen appreciation unfolds over weeks rather than erupting in a single spike.
- Liquidity tightens but avoids sudden gaps.

- Cross-asset volatility firms but remains tradeable.

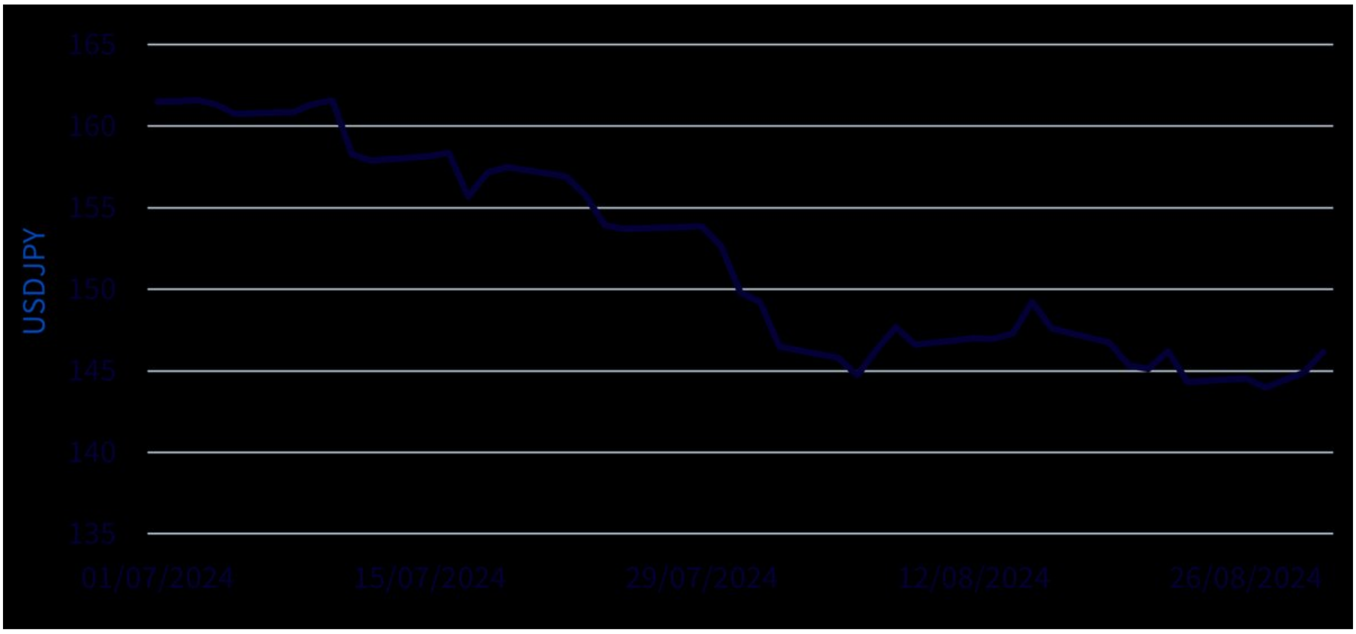
Under this path, capital still rotates back toward Japan, but repositioning can occur over months, not hours.

If the unwind accelerates:

- The yen can reprice sharply as crowded carry positions unwind simultaneously.
- Deleveraging spills into equities, foreign exchange, credit, and crypto.
- Cross-border flows reverse abruptly, particularly where yen funding is vital.
- Offshore funding spreads widen as liquidity thins.

Markets already saw a preview. In August 2024, the yen strengthened roughly 6% within days3, slicing through carry exposures across asset classes. That is a reminder of how quickly positioning can unravel when funding conditions turn.

Figure 2: When yen carry trade unwinds fast



Source: Optuma, WisdomTree. 02 December 2025. **Historical performance is not an indication of future performance, and any investment may go down in value.**

What comes next reflects structural policy realignment, not a transient data point.

Positioning: navigating a more volatile currency landscape

As currency volatility rises and carry trades unwind, the case for currency-hedged exposure to Japan becomes stronger.

WisdomTree Japan Equity UCITS ETF (DXJ) provides targeted access to dividend-paying, export-driven Japanese corporates that tend to benefit from a weaker yen but can see margins compressed when the currency strengthens.

Its currency-hedged share classes help investors stay exposed to corporate fundamentals while reducing the impact of yen volatility on portfolio returns.

For investors seeking directional exposure to the yen, whether defensive or opportunistic, WisdomTree's JPY exchange traded product suite provides tools for:

- Hedging international portfolios against yen strength.
- Trading foreign exchange momentum or mean reversion.
- Positioning around the timing of BoJ rate moves.

These instruments allow investors to navigate currency volatility proactively rather than simply absorb it.

Final thought

For years, the yen carry trade has quietly underpinned global liquidity. As the BoJ prepares to tighten further, that support is fading, and the pace of the fade will set the tone for global markets.

- A gradual unwind means adjustment.
- An abrupt unwind means turbulence.

Either way, investors who recognise the timing dynamics and position early will be better placed to separate signal from noise as global markets transition into a more volatile, opportunity-rich phase.

1 Statistical release: BIS international banking statistics and global liquidity indicators at end-March 2025
2 Interest Rate : Ministry of Finance. 02 December 2025.
3 BIS Bulleting No 90. The market turbulence and carry trade unwind of August 2024.

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