Market Services FX Spotlight

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Where we stand

HEADLINES

- US and Iran halt talks
- Canada US trade talks unravel
- Canada employment rises 75,100
- Canada unemployment falls to 6.4%
- RBA holds rates steady
- US yields soar testing the Treasury

August witnessed sustained USD weakness as deteriorating labour data and recalibrated Fed expectations triggered the selloff. Geopolitical tensions remained firmly at the forefront, with continued headline volatility surrounding US–Iran negotiations over the Strait of Hormuz. Following the large, coordinated US–Japan interventions in late July and early August, markets also remained on edge regarding the timing and magnitude of future yen buying operations.

The first week of August saw Treasury Secretary Scott Bessent announce a potential breakthrough in US–Iran negotiations, suggesting a deal could materialize within 24 hours. This optimism proved premature as the week progressed without any agreement materializing. While Iran signaled a willingness to reopen the Strait of Hormuz, its demands for US military withdrawal, compensation and full sanctions relief were at odds with American negotiators. Separately, Iran and Oman engaged in parallel negotiations for a Strait of Hormuz deal, with both countries indicating they were close to finalizing an agreement. On August 6, Iran announced an arrangement with Oman to establish Hormuz shipping routes valid for two to four months, contingent on maritime service fees rather than passage tolls. But by August 18, Donald Trump claimed naval blockades remained in full effect and stated no active talks with Iran were occurring, contradicting the earlier optimism. As the month continued, both the United States and Iran claimed full control of the strait. Iran threatened renewed military escalation should diplomacy fail, while Trump threatened to bomb Oman if it interfered with US objectives.

The month's second half saw escalation when, on August 20, Trump announced "Economic D-Day," pledging crushing economic sanctions aimed at isolating Iran. US Treasury Secretary Scott Bessent unveiled measures targeting countries providing lifelines to Iran, indicating that China, which purchases approximately 90% of Iran's oil exports, could see its entities cut off from the USD clearing system.

CUSMA negotiations continued in August as Canadian and US trade ministers engaged in discussions surrounding a potential deal, though both sides reportedly remained far apart on key terms as of mid-month. This led Trump to grant a three-day extension beyond the original August 19 deadline. Negotiations ultimately collapsed on August 21, with both sides trading blame. Prime Minster Mark Carney alleged that when a deal appeared near completion, the United States rebutted with new demands, calling the reliability of their commitments into question. Trump countered that Canada had been extorting America for decades, and Commerce Secretary Howard Lutnick also accused Canada of adding last-minute demands. As a result, auto parts, steel, trucks and cars would face 50% tariffs effective January 1, 2027, leading to Canadian retaliation of 50% targeted tariffs on more than 700 US products effective September 8. Despite this, USDCAD traded with minimal reaction, suggesting markets viewed a resolution as eventually forthcoming.

US labour market data deteriorated, with nonfarm payrolls declining 23,000 in July against expectations for positive prints, a sharp reversal from earlier momentum. The weakness was broad-based, appearing in local government education services (–50,000), leisure and hospitality (–40,000), and financial services (–14,000). The bright spot was a 0.1% decrease in the unemployment rate to 4.1%, though labour force participation also declined slightly to 61.4% from 61.5%. This weaker-than-expected data contributed to a sustained USD selloff throughout August as markets revised expectations for Fed rate hikes, with odds of a September increase declining materially. US inflation data came in line with expectations on August 12, with core CPI rising 0.2% month over month and 2.5% year over year.

In contrast, Canadian labour data impressed the market with employment rising 75,100 in July, well above expectations. The unemployment rate declined to 6.4% from 6.5%, while the participation rate increased to 65.1%, suggesting labour market stabilization that supported the CAD rally in August. Canadian manufacturing PMI strengthened to its highest level in four years on August 4, with the composite PMI rising to 49.7 from 47.9. Canadian CPI surprised higher on August 17, printing at 3.0% year over year versus expectations of 2.9% and above the prior month's 2.8%, leaving the Bank of Canada likely on hold in September.

The Reserve Bank of Australia (RBA) held its cash rate steady at 4.35% in a unanimous decision on August 11, maintaining a hawkish hold. While the RBA left rates unchanged, commentary suggested monetary policy remains restrictive and should help cool inflationary pressures over time, leaving open the possibility of future hikes if inflation persistence emerges.

Currency markets saw significant volatility in the yen, with USDJPY falling to 155.23 on the first Monday of August, levels last seen during May interventions. Initial reports suggested a volume of approximately 730 billion yen on Monday, which paled in comparison to the 5.5 trillion yen deployed the prior Friday. It was later reported that the intervention was a joint effort with the US Treasury, while in total Japan spent USD 96 billion intervening between July 30 and August 26. Markets now look to the Bank of Japan to hike in September following hawkish comments from BoJ officials, as intervention only temporarily slows the depreciation in the yen.

On the horizon

The US Treasury announced plans to at least double the size of longer-dated nominal securities buybacks commencing September 9, after yields on US 30Y treasuries hit their highest levels since 2007. Bond markets initially reacted positively, with longer-term yields gapping lower across the board, though this move subsequently retraced. The decision by the Treasury to consider using the Treasury General Account to fund these buybacks was criticized by some market participants who saw the decision as delaying the inevitable. August saw a dramatic repricing of rate expectations, shifting from a September hike assumption at month-start to pricing in a hold, a recalibration that was ultimately tested at Jackson Hole. In his Jackson Hole speech, Chair Kevin Warsh emphasized that inflation was not meaningfully slowing and that the data was not entirely encouraging, resulting in a coin toss between a hold or hike being priced for September. Market participants will still look ahead to labor market data and CPI on September 4 and 11 respectively, before the FOMC meeting.

KEY UPCOMING EVENTS

DATE	EVENT
SEP 2	BoC rate decision
SEP 10	ECB rate decision
SEP 16	Fed rate decision
SEP 17	BoE rate decision
SEP 18	BoJ rate decision

Reform leader Nigel Farage won the Clacton by-election on August 14 with a commanding 62.8% of votes in a contest featuring 34 candidates, the most candidates in British electoral history. Notably, both Labour and the Conservatives declined to participate, underscoring the unique political dynamics of the race. The result demonstrated Reform’s capacity to mobilize core supporters despite losing overall polling position. GBP appreciated throughout the month, reflecting renewed policy clarity under the new government and broader USD weakness.

European energy markets face headwinds heading into winter as escalations between Iran and the US raise concerns about future natural gas prices, with winter contracts already having doubled compared to last year. A severe European heat wave and drought conditions also threatened agricultural output and industrial activity throughout August. Water levels in several German rivers, including the critical Rhine corridor for industrial transport, dropped to record lows, creating concerns about future food price inflation and industrial bottlenecks. These developments will provide additional justification for a second European Central Bank rate hike in September, following the initial tightening to counter second-round effects from the US–Iran conflict.

Regional developments in the Middle East continued with Benjamin Netanyahu rejecting Trump’s Gaza peace plan on August 10, insisting Israeli forces would not withdraw until Hamas fully disarmed. Additionally, Turkey, Saudi Arabia and Pakistan signed a joint defense agreement on August 7, pledging mutual defense commitments with the principle that an attack on one constitutes an attack on all.

Emerging markets

Colombia experienced a significant disruption following a 6.2 magnitude earthquake on August 10, which killed more than 330 people and damaged six critical airports. President-elect Abelardo de la Espriella was sworn in on August 8, with the incoming conservative government facing immediate challenges in managing both disaster recovery and monetary policy calibration. The new government submitted its 2027 budget bill on August 27 and aims to limit borrowing from 2028 onward as a measure of fiscal discipline. Meanwhile, the peso finished close to flat on the month.

Brazil’s political race heated up as Flavio Bolsonaro announced Alfredo Gaspar as his running mate ahead of the October election. Meanwhile, two concurrent developments affected market sentiment: the European Union announced plans to audit Brazil’s food imports following a new free trade agreement, while Brazil’s central bank cut its benchmark lending rate by 25 bps to 14% on August 5. The prospect of a closely contested election with policy uncertainty clouding the outcome weighed on BRL, which underperformed relative to broader EM strength during the month.

The Bank of Korea hiked for the second consecutive meeting on August 27, raising rates by 25 bps to 3% and lifting its 2026 growth forecast. Korean equity markets have exhibited extreme volatility in recent months, with the benchmark index rallying sharply from April lows of 5,170 to June highs of 9,385, only to reverse decisively and plummet to 5,262 in July, a collapse that triggered multiple trading halts and reflected broader Asian equity weakness. August provided respite, with the Kospi stabilizing and KRW appreciating as USD weakness and monetary policy provided tailwinds, delivering a notably less volatile month relative to the preceding period.

The Bangko Sentral ng Pilipinas (BSP) raised its overnight reverse repurchase rate by 25 bps to 5% in its third consecutive hike, adopting a hawkish stance with cautious messaging. While acknowledging H1 growth weakness and reliance on fiscal support for H2 recovery, the BSP signaled limited near-term pause potential due to broadening core inflation and projections showing inflation above target through 2027. BSP Governor Eli Remolona indicated the tightening cycle may have peaked, expressing hope that no further hike is needed and projecting inflation to peak in Q4 with a full recovery by 2027. Yet the statement preserved optionality for additional rate increases if El Nino, wages or oil prices surprise upward. The forward guidance remains open-ended and data-dependent rather than signaling a commitment to pause, reflecting the BSP's focus on anchoring inflation expectations despite the growth-inflation tradeoff.