Forex Focus: Bank Of Japan Will Have To Be Back Soon

By Nicholas Hastings

A DOW JONES NEWSWIRES COLUMN

LONDON (Dow Jones)--The Bank of Japan will be back in the markets sooner than we think.

At the moment, the central bank's massive Y2 trillion intervention exercise week before last certainly appears to have worked in pushing the yen lower.

The dollar is still trading over Y84.00, well above the Y82.97 level at which the central bank entered the market.

See how the how the dollar has performed against the yen since the intervention Sept. 15:

http://www.dowjoneswebservices.com/chart/view/4639

Since then, however, economic data indicate that a weaker yen is becoming even more imperative for Japan.

Also, global risk sentiment is deteriorating again. Doubts over the global recovery are becoming more of an issue and tensions between the U.S. and China are once again on the rise.

This shift in sentiment will accelerate safe-haven flows in the Japanese currency, pushing it higher against other major currencies such as the euro as well as against the dollar.

Pressure on the Japanese authorities to pursue a weaker yen policy have increased over the last week with the economy showing little sign of a bounce and the ministry of finance now resorting to another $55 billion economic stimulus package.

The damage that yen strength is having on Japanese exports was evident in the new trade data Monday showing that export growth slowed in August. The rise of 15.8% on the year was the slowest since the start of 2010.

The latest Bank of Japan Tankan survey Wednesday is likely to only make matters worse. The survey may show an improvement in the third quarter but should indicate that things will turn sour in the fourth.

The increased need for Japan to engineer a weaker yen could well coincide with a period when flows into the currency become even more intense.

More talk of increased quantitative easing from the U.S. is likely to be followed by a similar rise in talk of more monetary easing from the euro zone as confidence in the global recovery continues to deteriorate.

If that is the case, the yen's safe-haven role will only expand as investors move out of the euro as well as the dollar.

Of course, the Bank of Japan will follow the Fed and the ECB with its own plans for increased unconventional measures.

But, this will have little impact on overall yen sentiment, especially now that trade tensions between China and the U.S. are likely to increase.

Despite calls by U.S. President Barak Obama for China to accelerate its appreciation of the yuan against the dollar, the People's Bank of China actually pushed the dollar higher against the yuan at its fixing Monday.

This indicates Beijing has little intention of putting its own economic recovery at risk in order to help U.S. exporters.

For the yen, this could mean even heavier safe-haven flows both because of rising tensions between Washington and Beijing and because of the prospects of an even slower U.S. recovery.

Early Tuesday, the yen was a little higher against the dollar, which came under initial pressure from a report in the Wall Street Journal signaling that the Federal Reserve will adopt a less aggressive and more gradual increase in quantitative easing this time around.

The dollar eased back to Y84.18 by 0645 GMT from Y84.25 late Monday in New York, according to EBS.

The euro, however, fell to $1.3422 from $1.3444 and to Y113.04 from Y113.25.

Although talk of further quanitative easing has often been seen as negative for the |U.S. currency, some analysts are saying that a more gradual increase could be positive.

Certainly, new economic data from the U.S. later in the day, which are expected to show a small fall in house prices and a decline in consumer confidence, will increase speculation that more quantitative easing is needed.

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