

Forex Focus: Yen Will Hang On To Safe-Haven Status For Now

By Nicholas Hastings

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LONDON (Dow Jones)--Ripping the safe-haven mantle off the yen isn't easy.

In fact, it looks as if the Japanese currency will hang on to its haven status for a little while yet.

Last Sunday's disappointing election results for the ruling DPJ party may not prove quite the political and fiscal disaster that many fear and the Japanese recovery may yet prove more robust than expected.

On top of that, Japanese investors may soon be forced to start bringing money back home under new investment rules coming into force next month.

Indications of the strength of the yen's safe haven came on Tuesday when the yen immediately turned back up against the dollar and the euro after Moody's announced its downgrade of Portuguese debt.

Recent rallies in the dollar and the euro against the Japanese currency had already started to look shaky after China made it clear that it will continue cooling the property boom, despite forecasts that new growth data later this week will confirm that the economy is already slowing.

Both developments sent investors scampering out of risky asset markets and into safe havens such as the dollar.

And, in the event, the yen too.

See how resilient the yen has remained against the dollar in recent weeks:

<http://www.dowjoneswebservices.com/chart/view/4259>

The Japanese currency had been expected to lose its attraction after the DPJ lost its Upper House majority and now faces an uphill struggle to keep Japan's plan to reduce its fiscal deficit on track.

The three major credit agencies--Standard & Poor's, Moody's and Fitch--all warned that the country remains at risk from a debt downgrade as a result of the elections.

However, the ruling DPJ coalition has already ruled out an early election that might have increased political uncertainty, and a senior official from the International Monetary Fund has said he is still optimistic that the country will cut its public deficit, since the main political parties agree on the need for urgency.

The state of the Japanese economy could be another reason for the yen to hang on to its safe-haven status. In a world where the global recovery is far from secure and fears of a double-dip recession in the U.S. remain an issue, Japan is showing some unexpected resilience.

New consumer confidence data have been particularly helpful in boosting optimism.

Here is how Julian Jessop, chief international economist at Capital Economics in London, sees it: "The further improvement in consumer confidence in June supports other survey evidence that Japan's economic recovery still has plenty of momentum, despite the recent uncertainty in the financial markets and signs of weakness in some of the labour and spending data."

Adding to that are new rules that will put a limit on the leverage of margin trading from the start of August.

Tohru Sasaki, a currency strategist with JP Morgan Chase & Co. in Tokyo, said this will mean traders with leverage of more than 50 times will have to unwind those positions before the end of the month.

In a study entitled, "Mr. & Mrs. Watanabe May Need to Buy Back JPY in Coming Weeks," Sasaki noted that a recent survey showed 36% of all margin traders are holding positions with more than 50% leverage.

"Therefore, there should be some yen buying back in coming weeks stemming from the new regulation on leverage."

So instead of counting on a dollar recovery to Y90 or more, the market could well find that the U.S. currency becomes mired in a narrow trading range with the yen, until the Japanese currency starts to seriously lose its haven status.

More relaxed global sentiment, helped by Greece's successful auction of Treasury bills Tuesday as well as positive earnings from Intel, helped to encourage investors back into riskier currencies early Wednesday in Europe.

By 0645 GMT, the euro was up at Y113.05 from Y112.64 late on Tuesday in New York, according to EBS. The dollar was also up at Y88.95 from Y88.58. However, the euro slipped back to \$1.2702 from \$1.2721 as the market waited to see how Portugal's bond offering fares later Wednesday, after its credit rating was downgraded by Moody's Tuesday.

Bloomberg TNI FRX POV

Reuters USD/DJ
Thomson P/1066 or P/1074

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