

JPY: Why the yen has lost that safe haven feeling

With USD/JPY now above 140, we have been asked several times whether the yen has lost its safe haven status. We think two factors are important drivers here: the nature of this year's shock which has seen Japan's trade surplus wiped out, and the extreme juxtaposition of Fed and Bank of Japan policy. Don't bet on a USD/JPY turn this year



Yen loses its safe haven shine

With USD/JPY trading above 140 and financial assets under pressure, one could think that the yen is losing its status as a safe haven currency. The data support that idea. In 2020, when the world was rocked by the pandemic, USD/JPY had a 0.35 positive correlation with the MSCI World equity benchmark. That meant that when equities fell, the JPY typically outperformed against the dollar – i.e. JPY as a perceived safe haven. This year the USD/JPY correlation with equities is now zero – suggesting the JPY has lost some safe haven properties. Why?

I'd say it's down to two main factors – a) the nature of the crisis and b) the juxtaposition of the US and Japanese macro-financial policies.

On the former, the war in Ukraine has seen energy prices surge. Given that Japan imports all its

fossil fuel energy, Japan's terms of trade have collapsed – that is the price Japan receives for its exports versus what it pays for its imports. That is a large negative income shock. That has been most visible in Japan's trade account. Last summer Japan was earning JPY6trn a year on trade. Over the last 12 months, that trade surplus has swung to a JPY6trn deficit on higher energy bills. A safe haven currency typically needs to be backed by a strong trade surplus – such that there is a natural demand for a currency in a crisis. The JPY has lost that backing from trade.

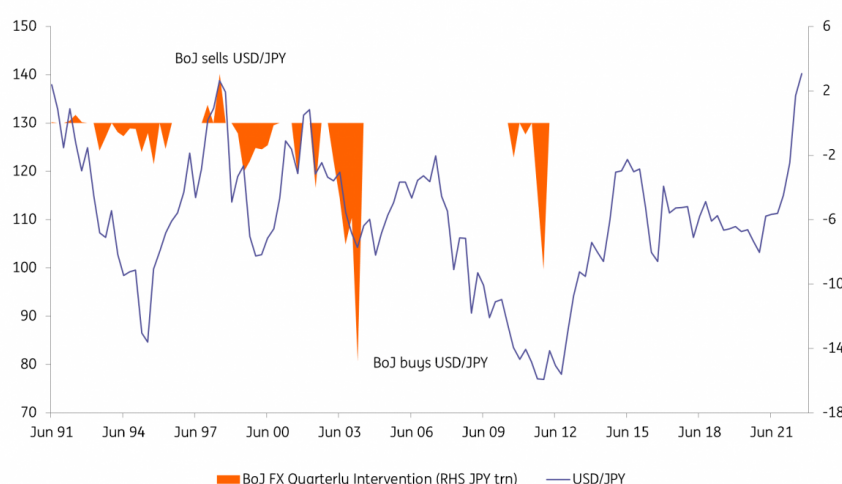
On the US-Japan story, the US Federal Reserve and the Bank of Japan (BoJ) are just about as far apart as you can get. The hawkish Fed has raised rates aggressively this year and promises to do more. The BoJ is one of the very few dovish central banks in the work (joined recently by the People's Bank of China). It is still engaging in quantitative easing. In practice, this now means that holding a 3m USD deposit pays 3% per annum. Hold a 3m JPY deposit and you will still be charged 0.10% for the pleasure. This 3%+ spread in rates really raises the bar for the JPY to outperform as a safe haven currency.

JPY would rally if equities fell hard enough...

Two final points – I suspect that if US equities fell hard enough that the Fed tightening cycle was substantially re-priced lower (and we haven't seen too much of that this year), the JPY would outperform again and USD/JPY would drop. I also suspect USD/JPY is moving into a zone where Japanese policymakers will show more overt concern – they intervened to sell USD/JPY back at these levels in the late 1990s.

But equally, we are a long way from a 1980s Plaza-type accord to weaken the dollar in general. That would require the Fed needing to cut rates (highly unlikely this year) or the BoJ to hike rates (again unlikely). So given the way things are going this year, a move to 150 certainly can't be ruled out.

USD/JPY and BoJ intervention levels. BoJ sold USD/JPY above 140 in the late 90s



Source: Japanese Ministry of Finance, ING

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