

Currencies leap as grip on yen eased

Cathy Holcombe

Japan briefly took its finger off the yen-intervention button yesterday, leading to a stunning shift in global asset values.

The country's finance ministry, which had spent more than US\$80 billion (HK\$624 billion) this year to keep its currency from rising too high, pulled official bids from the foreign exchange market after the Group of Seven industrialised nations issued a communique calling for more "flexibility in exchange rates".

With the government's hand removed, the yen bounced. Within hours it climbed 2 per cent to a three-year high of 111.14 against the US dollar, a seismic shift for a major currency.

Despite continued defences by central banks in South Korea and Taiwan, their units were also pulled north. The Australian dollar leapt to within a hair's breadth of the five-year high hit in July, while in Hong Kong the yuan hit a new record on the offshore non-deliverable market.

Asian shares tumbled, led by exporters whose products would get more expensive in US dollar terms. Benchmarks in Japan and South Korea fell more than 4 per cent.

Bonds were also hit, with US treasuries falling amid expectations Asian central banks would curtail purchases if they were buying fewer US dollars to weaken currencies.

"After reading the communique three times, I have to come to the conclusion that the [US Treasury] is more and more concerned with the exchange rates of the world," said Chris Melendez, whose Tempest Asset Management hedge fund specialises in foreign exchange trades.

"I think the dollar will continue to decline this week, and perhaps for the rest of the year," he said.

An end to Japan's intervention regime would have serious effects for regional economies, heavily dependent on exports. So serious that few expected Japan's Ministry of Finance to get out of the game; indeed, by afternoon, after the yen hit a three-year high, traders were already spotting what appeared to be dollar-buying.

Top Japanese officials also tried to talk down the yen yesterday, but their words were made hollow by the obvious retreat from the forex market. The key question now is how far Japan will allow the yen to rise. Some say another 6 per cent rise is not unlikely.

"If history is any guide, the next line in the sand may be 104. That is where the Ministry of Finance previously did most of its intervention once the [yen] went below the teens," Deutsche Bank strategist Marshall Gittler said.

Such a move could prove detrimental to the ongoing recovery in Japan's economy that has attracted billions of dollars to its stock market this year from overseas investors.

Based on estimates by brokerage analysts, Bloomberg said operating profit at Toyota would be reduced by about 23 billion yen (HK\$1.58 billion) for each one-yen gain by the Japanese currency.

In smaller versions, that story would be reflected in the profit and loss accounts of companies across Asia, from chipmakers in Taiwan to mobile phone firms in South Korea.

One obvious exception would be China, whose yuan is effectively pegged at 8.27 to the US dollar.

This year China surpassed Japan for the first time to become the biggest Asian exporter to the United States. A rise in the yen would, on the surface, appear to lay out the red carpet for further competitive gains.

That angle was taken up in the stock markets yesterday. China shares listed in Hong Kong fell, and perhaps with good reason.

"There would be a lot of noise if the yen and the Taiwan dollar and the won are going

to move up but China isn't going to move up. No one expects China to get away with this scot-free," said Kim Eng Securities head of Hong Kong research Stephen Brown.

While he does not think China will prematurely adjust its own currency policy in light of a rise in regional pressure, he expect offsetting handicaps on China's exports.

Brown also points out that 60 per cent of China's exports are from overseas-managed companies. They essentially operate on a US dollar basis anyway; they will benefit from a weaker greenback but not from an artificially weak yuan as few inputs or materials are sourced on the mainland.

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