Our Guides - the **Technical Trader's Guide** and the **Macro Trader's Guide** both deal with these and many other markets in much more detail over multiple time- frames. **Key Trades Bulletins** subscribers receive a detailed report on every trade we enter for our Key Trades Portfolio. More details about all these products: CLICK HERE

Market Update 27th November 2009

The surge of the Yen

The Macro Trader's view:

The Yen is a currency that has recently benefited from periods of risk aversion. When stocks have been sold the Dollar has rallied on safe-haven buying and the Yen has strengthened too. Even though the Japanese economy has suffered its own damaging recession, traders see the Yen as a refuge from periods of great uncertainty.

Recently, the Japanese economy has begun to recover with the recent release of stronger than expected Q3 GDP but weak spots remain: condo sales have been weaker than expected recently and so too have department store sales.

But the historical strength of the Japanese economy has mostly been due to exported manufactured goods and that remains true today. However, even as recession has been declared over, Japan continues to be dogged by deflation with CPI data released last week showing a decline of 2.4% year on year.

So why, when the US economy has also emerged from recession and it has a better debt-to-GDP ratio than Japan, has the Yen begun to show such unequivocal strength against the Dollar and also against the Euro and Sterling?

The answer is that even though Japan continues to suffer from deflation and the country has a debt-to-GDP ratio in excess of 100% it has a large current account surplus and a trade surplus which means they have few concerns about financing a budget deficit.

The US, on the other hand, not only runs a huge budget deficit, projected to be 12% of GDP or in cash terms US$1.8T with a debt to GDP ratio forecast to hit 70%+ of GDP, but also runs a large trade deficit.

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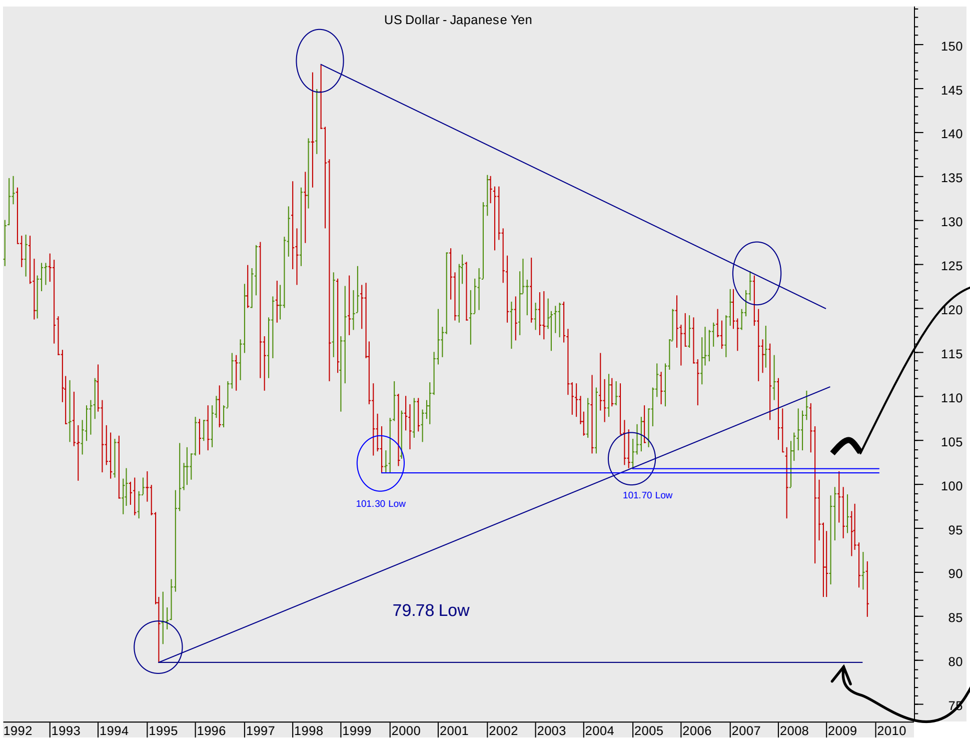
Although this dramatically reduced during the recession, as the US economy has begun to grow again, so too has the trade deficit. For now funding issues are manageable as the outlook for US inflation remains benign and the markets retain confidence in Fed chairman Bernanke.

But China, India and others are not happy. They have massive reserve holdings in US Dollars and Dollar denominated assets, principally US Treasury Bonds. They are unhappy that current US Government economic policies will lead to an erosion of the Dollar's value over time.

The Euro, often touted as an alternative reserve currency, isn't quite up to the role. So the only other currency that offers a safe place to hold reserves is the Yen and this could partly explain the Yen's current strength against the Dollar.

Clearly, the percentage of the world's reserves held in Yen remains small compared to the Dollar, but we are talking about diversification, and Gold has also benefited from this. Looking ahead we see a clear trend establishing and the Yen will be the beneficiary.

The Technical Trader's view:



MONTHLY CHART

The failure of the market to get back up through the powerful resistance from the old lows at 101.30 and 101.70 is clear.

A retest of 79.78 is likely…

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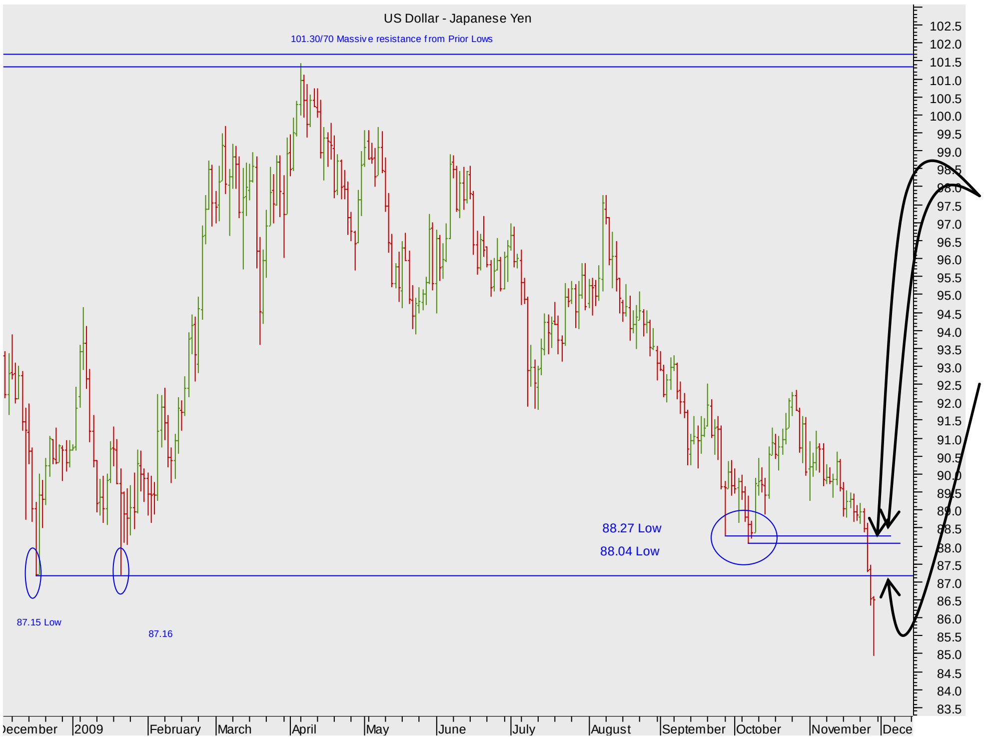

DAILY CHART

Having driven down through both the near old lows at 88.27 and 88.04

and

the pivotal old lows at 87.15 and 87.16, the market has a great deal of resistance above in case of any attempted Dollar rally.

The speed and violence of the move makes it look over-extended.

But the Dollar bears will take great comfort in that overhead resistance.

Mark Sturdy

John Lewis

Seven Days Ahead

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