Japanese Industrialists Judo Yen Speculations

FOREIGN EXCHANGE

Japanese industry conducted a successful "judo operation" this week against speculative pressures which were steadily pushing up the Japanese yen and threatening to destroy the country's exports. The Bank of Japan's sudden and totally unexpected slashing of its discount rate from 6 to 5 percent on April 19 rudely snatched the rug out from under the yen speculators, among them the major New York-based international banks. The yen promptly fell more than 3 percent from last week's three-year high of 270 to the dollar down to 277 as of April 21.

The Japanese central bank's move was forced by industrial interests and sections of Prime Minister Fukuda's own party, the LDP, which are opposed to Fukuda's policies of accomodation with the Carter Administration in the USA. It has been widely reported in the international financial press that during Fukuda's trip to Wahington earlier this month, he agreed to allow the yen to appreciate so as to eliminate Japan's large trade surpluses, which have been endangering the stability of the Eurodollar debt structure. Japan would aid the refinancing of dollar-denominated Third World debt by importing *more* raw materials and semi-finished products from the Third World, while, paradoxically, exporting *less* manufactured goods.

Following his meeting with Carter, Fukuda announced his tacit approval of the revaluation, publicly stating that the Bank of Japan would pursue a "free market" policy and would no longer intervene to keep the yen down. The London financial press reported that Fukuda would allow the yen to go as far as 260 to the dollar.

When the dollar slipped below 270 yen last week, however, Japanese industry revolted. The steel industry complained that it is already slashing prices in order to maintain its competitive position in international markets and actually requires an exchange rate of 290 to make a profit.

The Bank of Japan resumed its heavy intervention to depress the yen and then, on April 19, announced its judo move — the discount rate reduction.

This rate cut was a laudatory move in itself since it removes part of the financial burden on Japanese corporations, thereby helping to sustain the economy without the inflationary effects of big government "pyramid building" programs Keynesian-style.

As a side effect, the large Japanese trading companies took advantage of the fact that yen-sector interest rates had dropped below dollar rates. Instead of borrowing dollars to finance their imports, the trading companies began to borrow yen and then sold the yen for dollars both to cover their imports and to meet their short-term dollar obligations; this exerted strong downward pressure on the yen.

The leading New York international banks were, meanwhile, caught completely off guard by the Japanese maneuver. A Bankers Trust trader complained: "A lot of people had long positions on the yen. They took their profits when the market was very thin (triggering the sharp fall)....The U.S. prefers the yen up rather than having to resort to protectionism against Japanese exports. That's why *we* still see a stronger yen."

The reduced yen exchange rate does not necessarily entail a slowdown in the internationalization of this currency. In fact, international use of the yen for trade financing has steadily increased, since it is seen by many countries as a means to insulate themselves against dollar inflation. According to Japanese bankers, during the last three months, the proportion of Japan's imports which are invoiced in yen has risen from 3-4 percent to 5 percent, while the proportion of exports invoiced in yen has risen from 20-25 to 25-30 percent.

...But Bundesbank Buckles Under

The actions of the Japanese central bank contrast sharply with those of the West German Bundesbank this week, which appears to have acquiesced to the Carter Administration's demand that West Germany eliminate its trade surplus. In its April report, the Bundesbank announced that the country was "aiding the world economy" by slashing its 1977 current account surplus to $1.59 billion, half last year's total. The report stated that during the first two months of this year, West Germany actually ran a current account deficit of $253.9 million, which the Bundesbank traced to the stagnation of exports.

On April 21, Otmar Emminger, who just replaced Karl Klasen as the president of the Bundesbank, announced his support for the $15 billion special bail out facility proposed by IMF managing director Witteveen. Emminger stated he believed the Witteveen plan would be approved at the IMF Interim Committee meeting on April 28 — a move which would prop the Eurodollar market and hence the dollar itself.