

Japan's 10-Year Bonds May Rise on Worsening Economic Sentiment

August 2, 2008

Aug. 4 (Bloomberg) -- Japanese bonds may rise for a second day after a report last week showed U.S. payrolls declined for a seventh straight month, increasing concern that exports to Japan's largest export market will wane.

Nikkei 225 Stock Average futures traded lower in Chicago, boosting the appeal of fixed-income securities. Demand for bonds may also increase as traders pared bets the Bank of Japan will boost interest rates this year amid signs of a global economic slowdown. The Ministry of Finance will sell 1.9 trillion yen (\$17.7 billion) in 10-year bonds tomorrow.

"Bonds will try a higher price," said Akihiko Inoue, an analyst at Mizuho Investors Securities Co. in Tokyo. "Concerns about economic deterioration make selling bonds very hard."

Ten-year bond futures for September delivery traded at 136.66 in London from 136.72 at the 3 p.m. close in Tokyo on Aug. 1. The contract will open for trading at 9 a.m. Tokyo time.

The benchmark 10-year bond hasn't traded yet today at Japan Bond Trading Co., the nation's largest interdealer debt broker. The yield on the 1.7 percent bond due June 2018 lost 2 basis points to 1.51 percent on Aug. 1 after touching 1.505 percent, the lowest since April 24.

Nikkei 225 futures traded at 13,105 in Chicago from 13,110 in Osaka on Aug. 1 after U.S. payrolls dropped by 51,000 in July, the Labor Department said on Aug. 1 in Washington. The jobless rate rose to 5.7 percent, the highest since March 2004, from 5.5 percent the prior month.

Japan's bonds often move in the opposite direction to stocks. Benchmark 10-year yields had a correlation of 0.75 with the Nikkei 225 in the past month, according to Bloomberg data. A value of 1 means the two moved in lockstep.

BOJ Odds

There is a 9 percent chance the central bank will raise interest rates to 0.75 percent, from 0.5 percent by Dec. 31, according to calculations by JPMorgan Chase & Co. using overnight interest-rate swaps. The odds were 10 percent on Aug. 1 and as high as 92 percent on June 11.

Demand for bonds may be limited on speculation primary dealers, obliged to bid at debt auctions, may reduce holdings of bonds in case prices decline before they can pass on the new securities to investors.

The prior sale on July 3 drew bids worth 3.09 times the amount on offer, compared with a so-called bid-to-cover ratio of 2.09 at the June sale.

HEALY CONSULTANTS

The 1.7 percent bond due in June 2018 closed at 101.63 to yield 1.51 percent on Aug. 1, according to the Bloomberg Yen Bond Fixing Price. The level is an average rate set at 6:30 p.m. in Tokyo by Daiwa Securities SMBC Co., Nikko Citigroup Ltd., Mizuho Securities Co. and Mitsubishi UFJ Securities Co. A basis point is 0.01 percentage point.

Source: Theresa Barraclough