

Japan's Notes Decline as U.S. Reports Temper Slowdown Concern

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July 28 (Bloomberg) -- Japanese five-year notes declined after U.S. reports tempered speculation that a slowdown in Japan's largest export market will worsen.

The yield advantage of Treasuries over Japanese bonds widened to the most in seven months after the reports on July 25 showed new-home sales in June fell less than economists forecast and consumer confidence unexpectedly rose. Ten-year yields also climbed from the lowest in a week as stocks extended last week's gains, reducing demand for the security of debt.

"The JGB market is reacting to the U.S. Treasury market," said Keiko Onogi, a debt strategist at Daiwa Securities SMBC Co., one of the 26 primary dealers that are required to bid at auctions, in Tokyo. "The main focus is the U.S. economy, U.S. Treasuries and stocks."

The yield on the 1.3 percent note due June 2013 rose 1 basis point to 1.15 percent as of 12:39 p.m. in Tokyo at Japan Bond Trading Co., the nation's largest interdealer debt broker. The price fell 0.047 yen to 100.694 yen.

Ten-year yields added half a basis point to 1.575 percent, after falling to as low as 1.565 percent on July 25, the least since July 18. A basis point is 0.01 percentage point.

Ten-year bond futures for September delivery were little changed at 135.97 at the Tokyo Stock Exchange and the Nikkei 225 Stock Average advanced 0.4 percent.

U.S. 10-year yields added 10 basis points to 4.1 percent on July 25, after the government said new homes sold at an annualized pace of 530,000, exceeding the median forecast of 503,000 in a Bloomberg News survey. A separate report showed orders for durable goods unexpectedly rose in June.

Consumer sentiment in the U.S. increased to 61.2 last month from 56.6 in June, the Reuters/University of Michigan index showed on July 25. Economists surveyed by Bloomberg News had forecast a sixth consecutive monthly drop, to 56.4.

'Reduced Recession Concerns'

"Last week's economic data has reduced recession concerns," said Eiji Dohke, chief strategist at UBS Securities Japan Ltd. in Tokyo.

The gap in yields between 10-year Treasuries and similar-dated Japanese bonds was about 2.51 percentage points on July 25, the widest since Jan. 1.

Losses in Japanese bonds may be limited on speculation reports this week will back the case for the Bank of Japan to keep interest rates on hold, supporting demand for short-term securities that are sensitive to monetary policy.

A government report on July 30 is estimated by economists to show industrial production declined 1.7 percent in June from a month earlier, after rising 2.8 percent in May.

Rate Outlook

Reports "will continue to show risks that the Japanese economy will slow down," said Tatsuo Ichikawa, a fixed-income strategist at ABN Amro Securities Japan Ltd. in Tokyo. "The BOJ will be stuck between higher inflation and slowing growth."

There is an 18 percent chance the central bank will boost its target rate to 0.75 percent from 0.5 percent by Dec. 31, according to calculations by JPMorgan Chase & Co. using overnight interest-rate swaps.

Demand for bonds may be limited as brokerages prepare for an auction of 1.7 trillion yen (\$15.8 billion) in two-year government notes tomorrow.

Primary dealers that are obliged to bid at the sale may reduce holdings of bonds in case prices decline before they can pass on the new securities to investors.

The prior sale on June 24 drew bids worth 2.47 times the amount on offer, compared with a so-called bid-to-cover ratio of 3.21 at the May sale. The ratio averaged about 3.26 times over the past year.

Source: Theresa Barraclough



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