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# Yen We Have a Problem

- The Japanese Yen is trading at the cheapest level to the U.S. Dollar since 1986 ($1 = ¥160.68).
- The Yen's cheapness compared to the USD is primarily due to the significant difference in interest rates. Japan's policy rate is the lowest among developed economies, at 0.0-0.1%, while the U.S. policy rate is 5.25-5.50%. At the 10-year maturity point, the yield difference between the two countries is more than 325 basis points.
- The large difference between policy rates encourages investment and the flow of funds out of Japan into the higher-yielding U.S., which increases the value of the dollar relative to the Yen.
- A weak Yen helps Japanese companies with global operations by increasing the value of repatriated overseas profits. The weak currency has also helped boost tourism.
- Conversely, it makes the price of imports – such as food and energy – more expensive, which hurts Japanese consumers.
- Japan's finance minister has stated it is ready to intervene in currency markets if necessary.
- The Japanese Minister of Finance has already stepped in to support the Yen this year. In April, Japan spent a record $62 billion to defend the Yen.
- Currency interventions usually provide only short-term support (as shown by the response to April's buying spree). For the Yen to strengthen, either the Bank of Japan (BoJ) has to raise its policy rate, or the Fed has to cut its policy rate (or a combination of both).
- Boosting the Yen significantly would require Japan to raise its policy rate substantially. However, this is unlikely due to low inflation, potential disruptions to the heavily indebted government and economy, and risks to financial stability from losses on the BoJ's large portfolio of Japanese government bonds. Therefore, the fate of the Yen lies with the Federal Reserve.

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