

Industry Group Impact Of The Yen

The breakout of the yen to new highs last week was seen as a negative for Japan's many export-oriented industries. There was a time in the not-too-distant past leaders of various American industries such as automobiles, steel, chemicals and consumer electronics would have been cheering this development from the rooftops; I am not all that certain they would have found the reason for the yen's strength, repatriation of funds following the earthquake and tsunami, unseemly.

Those reactions were muted given two long-term developments, the rise of China as Asia's leading export powerhouse and the weakened state of many of the American industries listed above. However, this is not to say the yen has no impact on the relative performance of many of the industry subgroups within the S&P 1500 Supercomposite. Let's use a methodology last discussed for the [euro](#) during 2010 Greek debt crisis. Standard & Poor's divides the market into ten economic sectors and its S&P 1500 Supercomposite into 154 industry groups, 145 are active at the moment. If we take the relative performance of each group against a series of primal market factors, one of which is the yen, at 90% confidence levels, we can assess which groups are affected positively and negatively. If each of those groups' regression betas, the amount by which we should expect their performance relative to the S&P 1500 to change as a function of the yen, is multiplied by its weight in the index, we can sum the positive and negative changes together and derive a net weighted performance beta.

The table below summarizes the results. The cells on the left contain the groups with negative relative performance betas; these are stocks whose relative performance should rise in response to the falling yen. These are concentrated in the financial, energy and basic materials sectors, highlighted with yellow, mauve and gray backgrounds, respectively. The cells on the right contain the groups with positive relative performance betas; these are concentrated in the healthcare and utility sectors, highlighted with orange and green backgrounds, respectively.

Japanese Yen Beta-Weighted Impact On S&P 1500							
	SPR	JPY	Weighted		SPR	JPY	Weighted
	Weight	Beta	Beta		Weight	Beta	Beta
Other Diversified Financial Services	3.3%	0.895	0.030	Pharmaceuticals	5.5%	0.413	0.023
Investment Banking & Brokerage	127%	0.833	0.011	Soft Drinks	2.30%	0.460	0.011
Diversified Banks	167%	0.591	0.010	Household Products	2.30%	0.457	0.011
Asset Management & Custodial Banks	115%	0.714	0.008	Packaged Foods	166%	0.436	0.007
Regional Banks	146%	0.545	0.008	Tobacco	148%	0.395	0.006
Life & Health Insurers	104%	0.731	0.008	Electric Utilities	196%	0.281	0.006
Consumer Finance	0.80%	0.717	0.006	Integrated Telecommunications	2.45%	0.223	0.005
Oil & Gas Equipment	160%	0.293	0.005	Biotech	142%	0.332	0.005
Retail REITs	0.52%	0.697	0.004	Hypercenters & Superstores	1.19%	0.378	0.004
Specialized REITs	0.71%	0.472	0.003	Multiline Utilities	147%	0.305	0.004
Construction & Farm Machinery	1.14%	0.274	0.003	Restaurants	129%	0.285	0.004
Multiline Insurers	0.40%	0.760	0.003	Aerospace & Defense	2.65%	0.109	0.003
Oil & Gas Exploration	187%	0.154	0.003	Computer Hardware	3.12%	0.082	0.003
Movies & Entertainment	1.40%	0.203	0.003	Managed Health	0.90%	0.267	0.002
Property & Casualty Insurers	2.22%	0.122	0.003	Healthcare Services	0.75%	0.274	0.002
Specialized Finance	0.40%	0.626	0.002	Gold	0.25%	0.834	0.002
Steel	0.38%	0.629	0.002	Air Freight & Logistics	100%	0.181	0.002
Residential REITs	0.36%	0.505	0.002	Healthcare Equipment	0.42%	0.369	0.002
Office REITs	0.31%	0.579	0.002	Life Sciences Tools & Services	0.48%	0.267	0.001
Diversified Metals & Mining	0.33%	0.527	0.002	Drug Retailers	0.59%	0.203	0.001
Automobile Manufacturers	0.39%	0.390	0.002	Healthcare Distributors	0.42%	0.275	0.001
Coal & Cons. Fuels	0.26%	0.564	0.001	Data Processing & Outsourcing	1.27%	0.086	0.001
Construction & Engineering	0.29%	0.487	0.001	Food Retailers	0.31%	0.347	0.001
Hotels	0.33%	0.344	0.001	Environmental Services	0.35%	0.232	0.001
Broadcast & Cable TV	0.22%	0.517	0.001	Insurance Brokers	0.25%	0.262	0.001
Diversified REITs	0.17%	0.627	0.001	General Merchandise Retailers	0.48%	0.113	0.001
Industrial REITs	0.09%	1.191	0.001	Personal Products	0.24%	0.227	0.001
Thriffs & Mortgages	0.23%	0.454	0.001	Specialty Chemicals	0.50%	0.106	0.001
Industrial Machinery	1.10%	0.095	0.001	Food Distributors	0.19%	0.260	0.000
Internet Retailers	0.61%	0.136	0.001	Education Services	0.15%	0.319	0.000
Apparel & Accessories	0.35%	0.239	0.001	Brewers	0.07%	0.574	0.000
Oil & Gas Refining	0.18%	0.462	0.001	Gas Utilities	0.37%	0.109	0.000
Oil & Gas Storage	0.33%	0.238	0.001	Healthcare Suppliers	0.12%	0.311	0.000
Aluminum	0.10%	0.660	0.001	Metal & Glass Containers	0.18%	0.157	0.000
Homebuilding	0.16%	0.423	0.001	Healthcare Facilities	0.16%	0.180	0.000
Specialty Stores	0.30%	0.216	0.001	Distributors	0.09%	0.268	0.000
Department Stores	0.35%	0.183	0.001	Distillers & Vintners	0.09%	0.221	0.000
Electrical Components & Equipment	0.63%	0.098	0.001	Reinsurance	0.10%	0.184	0.000
Home Improvement Retailers	0.67%	0.086	0.001	Healthcare Technology	0.08%	0.120	0.000
Diversified Chemicals	0.84%	0.069	0.001	Water Utilities	0.03%	0.282	0.000
Wireless Services	0.35%	0.158	0.001				
Auto Parts & Equipment	0.25%	0.214	0.001				
Apparel Retailers	0.63%	0.081	0.001				
Oil & Gas Drilling	0.23%	0.221	0.001				
Semiconductor Equipment	0.37%	0.101	0.000				
Paper Products	0.14%	0.207	0.000				
Casinos & Gaming	0.15%	0.189	0.000				
Motorcycle Manufacturers	0.06%	0.354	0.000				
Multisector Holdings	0.04%	0.522	0.000				
Publishing & Printing	0.17%	0.106	0.000				
Tires & Rubber	0.02%	0.787	0.000				
Construction Materials	0.10%	0.179	0.000				
Electrical Manufacturing Services	0.11%	0.135	0.000				
Commercial Printers	0.05%	0.258	0.000				
Forest Products	0.04%	0.277	0.000				
Building Products	0.10%	0.119	0.000				
Photo Products	0.01%	0.246	0.000				
Commodity Chemicals	0.01%	0.308	0.000				
Subtotal:	32.57%		-13.92%	Subtotal:	38.6%		1130%
				Total:	71.18%		-2.62%

The net result is a net weighted beta of -2.62%. We can verbalize this as, "For every 1% increase in the yen we should expect a .0262% decline in the S&P 1500, all else held equal."

We always should take care whether a relationship is causal or spurious. Let's take that large bloc of financials, highlighted in yellow. In general, a stronger yen has been associated with the unwinding of carry trades and a reduction in overall global risk appetite. That should be associated with decreased results for the financial sector. The same logic applies for both energy and basic materials; both of these sectors have been associated with leveraged bets on commodities and emerging markets.

The positive linkage to the healthcare and utility sectors is a little more difficult to explain other than to note both sectors have benefited from declining interest rates and increased leverage. The healthcare sector in particular has been trading as if it depends on Other Peoples' Money, something we might associate more with real estate development. But both sectors are heavily regulated and therefore rely more on yield than on growth for their returns.

The stronger yen, by itself, is a negative for the market by virtue of its presence in carry trades. But it is not by itself; indeed it has been losing its [global funding role](#) to the U.S. dollar for almost two years. Once the initial shock wears off, the stronger yen should not, by itself, be responsible for major stress in the U.S. market.