

## Introduction

The MPM of the BOJ made a moderate upward revision of their economic outlook. Not surprisingly, however, another round of downward revision of their inflation outlook coupled with the sixth postponement of expected time of achieving 2% target attracted attentions by press reporters. It is also interesting to note that none of them required an additional monetary stimulus.

## Revised outlook

The MPM indicated stronger confidence of economic activities. In the summary of the renewed outlook, they referred to gaining momentum of private consumption after a temporary slow down, and better signs of business investment plans by firms. In addition, they expressed improved prospects of external demand thanks to stabilization of the global economy.

Accordingly, the MPM made an upward revision of their outlook of real GDP growth rates. New outlook for years from FY2017 to FY2019 is +1.8%→+1.4%→+0.7%, in comparison with their previous outlook (+1.6%→+1.3%→+0.7%). While these rates appear to be somewhat higher than market consensus, expected rates of growth for FY2017 and FY2018 would be substantially higher than our potential rate of growth.

In contrast, the MPM downgraded their outlook of inflation. In the summary, they claimed that delayed reactions of firms and households on the behaviors of wage/price setting would be a key factor to prevent acceleration in inflation in spite of continuous reduction in the aggregate demand/supply gap.

Readers may like to note that it is the first time in years that both the cabinet office and the BOJ estimate that the aggregate demand/supply gap may have disappeared. As a result, we need to seek a hypothesis to explain the reasons why it is hard to observe the signs of inflation.

In fact, the MPM pointed out that firms typically have reacted to labor shortages by adjusting their business models and investing in machinery to reduce the needs of hiring workers. Moreover, Governor Kuroda explained that such practices could be found among range of service sectors.

While the managers of firms would admit it has been the case in general, it could have some mixed implications for inflation outlook and monetary policy. The MPM insisted that such practices would be diminished in the end when labor conditions become much tighter in coming years. It could survive, however, if it has been driven by longer-term concerns about our rapid aging society.

Looking from broader perspectives, persistently cautious behavior of wage/price settings could reflect our low prospects of long-term economic growth, rather than our backward-looking formation of inflation expectations as the MPM claimed in the summary of the outlook. In any case, according to the new outlook of the MPM, we need to be more patient before achieving 2% inflation target.

## Policy strategy

Number of press reporters raised the issue of the sixth postponement of expected time of achieving the target since the introduction of the QQE. Interestingly, however, none requested an additional stimulus by the BOJ. On the one hand, they might be satisfied with the current improved outlook of

economic activities. Along this line of thought, some reporters asked Governor Kuroda whether the MPM should review the idea of 2% inflation target itself. Governor Kuroda reiterated the significance of maintaining the target by referring to some upward biases of indicators of inflation, difficulties of monetary policy under nominal zero boundary, and status of “global standards” of the target.

On the other hands, some press reporters suspected that the MPM could run out of effective policy tools under the QQE. Governor Kuroda strongly argued against such concerns and confirmed the MPM's view that current stance of monetary policy has been effective in stimulating economic activities. Moreover, Governor Kuroda expressed the view that it would be more effective as expected rate of inflation as well as natural rate of economic growth improves in coming years.

Along this line of thought, other press reporter asked if the BOJ would not do any additional stimulus in the future, even if outlook of inflation deteriorates further. Governor Kuroda rejected such speculation, and said that the BOJ is ready to conduct an additional monetary stimulus if it is necessary.

At the time of its comprehensive review of the QQE, the MPM might already have thought that moderate growth of economy with the lack of inflation could be probable in coming years. If this might have been the reason for shifting gyration of monetary policy from “quantity” to “interest rate” in order for the sustainability of the QQE, the current framework of monetary policy would rather fit the conditions of our economy and inflation as suggested by their outlook.

Nevertheless, as pointed out by press reporters today, continuous downgrades of inflation outlook by the BOJ could further prevent the improvement of inflation expectations by firms and households. It would be true, if our economic agents have further concerns about monetary policy tools that would be effective to stimulate our inflation.

All in all, confidence in monetary policy and viability of the QQE still depends on the timeframe of higher rate of inflation.

## Long-term rates

In comparison with previous round of press conferences, discussion on policy normalization diminished today due to the obvious reason. Nevertheless, a senior reporter of Nikkei raised the issue of long-term rates in coming years. Specifically, he asked a prospective level of JGB rate when and if the rate of our economic growth accelerate as the outlook by our government forecasts.

While Governor Kuroda avoided to answer the question, he admitted that future rates of JGB yields would depend on the BOJ's monetary policy as well as economic and fiscal conditions. It could have non-negligible implications when we need long years before the normalization of BOJ's assets.

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