

## Introduction

Under a virtuous circle of economic recovery as insisted again by Governor Kuroda, we would not have imminent issues for monetary policy for now. Nevertheless, reporters raised some points of interests that included the developments of inflation expectations and the management of forward guidance for coming months.

## Economic conditions

It would be appropriate to review the BOJ' evaluations of current economic conditions as the major backgrounds for policy debates.

Governor Kuroda reiterated the view that a virtuous circle from production to expenditure via income remains intact. In fact, he did not agree to the concerns expressed by some reporters that private consumption could become stagnant. Rather, Mr. Kuroda pointed out the momentum of consumption by referring to broader based increase in expenditures. Moreover, he mentioned about the signs of recovery of business investments thanks to the increase in corporate profits.

Moreover, Governor Kuroda suggested that the overseas major economies are also on their recovery paths. In the US, he insisted the strength of private economic activities under the high uncertainties of fiscal policy. Regarding the Europe, Governor Kuroda drew the attentions to the bottoming out of real GDP growth rate, while he implied some concerns about the trend of dis-inflation in recent months.

All in all, Governor Kuroda looked more confident about the on-going economic recovery. Nevertheless, divergence of the views on economic conditions . especially on the overseas front . is maintained between the BOJ and the markets. This is indeed not a serious issue for now, but could become an important factor in terms of the policy dialogue between the BOJ and the markets.

## Inflation expectations

Governor Kuroda explained his view of the formation of inflation expectations deliberately as a reply to press reporters.

He mentioned that there are two major ways of encouraging such expectations. First, according to his comments, inflation expectations could be generated by a strong commitment by the central bank to achieve the inflation target. Second, inflation expectations would develop depending on the actual and historical performances of inflation.

In light of the framework of the QQE. Governor Kuroda may have reiterated that the future course of inflation should be sustained by the higher inflation in recent months, even if the effects of the policy commitment in the QQE would gradually diminish regarding inflation expectations. If it would be true, the QQE could be substantially successful not only for removing the deflationary minds but also for providing stronger policy effects through negative real interest rates.

While his line of argument seems to be plausible, we may still have uncertainties about such "adaptive" formation of expectations. For example, as a press reporter suggested, large part of higher inflation in recent months could be attributed to external factors including those by exchange rates. Moreover, inflation minds of our general public would depend on the "second round" effect of consumption tax hike in coming April.

## Forward guidance

There is a discussion in the market about possible modification of the QQE, especially on the front of forward guidance. In particular, private economists may feel the ambiguousness about the current BOJ's commitment, when they think it would be difficult to achieve the 2% inflation target sometime in FY2015. According to their arguments, the BOJ should commit more clearly in the achievement of the target, regardless of the timing.

The BOJ may have noticed this issue, and may rather have maintained it intentionally. On the one hand, they need to mention the absolute timing ("within two years") to enhance the effect of policy announcement on our deflationary minds, as discussed in the previous section. On the other hand, they would like to commit to maintain the QQE to strengthen the effects of forward guidance on long-term interest rates.

As a reply to a press reporter, Governor Kuroda insisted that the BOJ would maintain the QQE until 2% inflation is stably preserved. While this was not a totally new discussion, it should be noted because of the following implications.

First, it could pave the way for the BOJ to modify their inflation outlook, when and if 2% inflation in 2015 would become less plausible from their point of views. This is because the BOJ could argue that additional injection of funds would be necessary to achieve the target. Second, it could also pave the way for the BOJ to maintain the QQE in an "open-ended" manner. With this respect, the BOJ could be in a similar condition as the FRB in terms of management of asset purchase program.

Open-ended operations could indeed have some side-effects. Nevertheless, in comparison with possible enhancements of the QQE as suggested by some market participants, it could become a second-best solution in terms of the choice of instruments as well as the impacts on the markets.

## Conclusions

As a press reporter pointed out, CPI inflation rate in the US and Japan virtually converged in September. Moreover, HICP inflation rate in Euro-area was about the same level. Interestingly, however, the reactions by the policy makers and the markets were totally different.

This contrast would of course reflect the inflation performances in respective economic areas in recent years, and as a result, could have significant clues for understanding the formation of inflation expectations in coming months.

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