

### Additional stimulus

The MPM of BOJ decided the additional stimulus for the first time under the regime of QQE. In addition to its unexpected move, substantial scale of measures surprised our markets in late afternoon.

The policy package consists of two pillars: 1) increase in the scale of JGB purchase (¥50tn → ¥80tn annually) coupled with extending the average maturity (7y → 7 to 10y), and 2) increase in the scale of ETF and J-REIT purchase (¥1tn → ¥3tn and ¥30bn → ¥90bn respectively).

### Backgrounds:

Governor Kuroda explained at the press conference today that the additional stimulus is intended to reduce the risk of losing momentum in improving inflation expectation. He claimed that our inflation expectation would be formed in an adaptive manner, unlike the one in the US where inflation expectation is anchored at around 2%. In light of our experiences of chronic deflation and low inflation for decades, he warns that deflationary minds could easily revive under the recent deceleration of actual rate of inflation.

While the domestic market participants would agree this fundamental idea, they still seem to wonder whether it is an optimal time to conduct the additional stimulus. Many of them in fact claimed that the BOJ should have moved in the spring of this year when there was growing downside risk of inflation. Interestingly, Governor Kuroda also implied that some of the opposing opinions expressed by MPM members against the proposal of the additional stimulus were related to its timing but not to its need itself.

In reply to many questions by the reporters with regard to the timing issue, Governor Kuroda mentioned that it is “critical moment” due to growing number of downside risk of inflation. He highlighted the recent fall in commodity prices as a leading example. According to his view, drops of major commodities due to whatever reasons could affect our inflation expectation. While the policy statement admits some positive impacts on our purchasing power, Governor Kuroda insisted the importance of policy action in a pre-emptive manner.

If you once agree to the appropriateness of the timing, it would not be hard to accept the additional stimulus. In fact, as explained above, the policy package is a simple extension of the original QQE. Moreover, Governor Kuroda gave us the same address of its expected effects. Namely, he argued that the asset purchases would improve our inflation expectation both through affecting our minds directly and through stimulating aggregate demands.

### Benefits and costs:

After the announcement of the additional stimulus today, market players especially on the fixed income front seem to insist the risk of deteriorating market functions. This is not a new issue for QQE. Nevertheless, this issue would require deliberate communication, because depressing the JGB yields is itself the intended effect by the QQE.

As an initial reaction, market department of the BOJ already announced a new set of guideline of JGB purchase operations consistent with the additional stimulus package. Moreover, the BOJ staff was given substantial flexibility in managing the JGB operations in terms of maturities of purchasing assets as explained above.

Similar issue could be found in the foreign exchange market. As I discussed in my recent issue of the Note, there has been a heated discussion in Japan whether the depreciation of our own currency would be beneficial to our economic activities. Today, some of the reporters expressed concerns that the cheap JPY could rather lead to reduction in real purchasing power of households and/or to squeeze the profits of firms. Here again, there is a dilemma for the central bank, because lowering the value of currency as a result of unconventional monetary policy would be one of a few meaningful venue of policy transmission.

In replying to these concerns at the press conference, Governor Kuroda seem to think firmly that the positive effects of QEE is estimated to be much more significant than the costs and side-effects as discussed above. This line of “well anchored” views could also reinforce the BOJ’s commitment to achieve the inflation target, which could help improving our inflation expectation according to the BOJ.

Moreover, some of the side-effects discussed above should rather be treated by micro-economic policy by the government., in my view. For example, labor policy could encourage the firms to increase wages that could prevent negative growth of real purchasing power of households. This is one of the policy focus by the “third arrow” of Abenomics.

### Consumption tax

Our domestic markets seem to pay attention to the relationship between the additional stimulus and the second round hike of consumption tax. In fact, there was the strong view that, if and when the BOJ would decide the additional stimulus, the BOJ would intend to minimize a temporary downward pressure by the second round hike of consumption tax. Moreover, now is the time when Prime Minister Abe will launch the expert panel to discuss the issues in relation to consumption tax hike.

Several press reporters naturally raised this issue. Governor Kuroda strongly denied the relationship between the additional stimulus and the consumption tax hike. Nevertheless, Governor Kuroda added that fiscal consolidation by any means could be beneficial to monetary policy across the world. Furthermore, this style of policy mix - monetary easing and tightening fiscal policy - was included in the joint statement by the BOJ and the government.

If you also take account of the pre-emptive nature of this additional stimulus, the policy action today could effectively send a “message” to the government about pursuing an optimal policy mix, regardless of the BOJ’s intension.

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