

Introduction

As a simultaneous commentator of Nikkei CNBC TV program, I was surprised to find the press conference by Governor Kuroda was crowded with so many reporters today when the BOJ did not change their policy or their assessment of economy. Almost all the issues raised were related to the implications of crude oil price that has been falling by 30% additionally since the policy decision of the additional stimulus. Let me discuss several interesting points related to this specific topic.

Benefits and costs

In reply to a number of questions, Governor Kuroda explained that significant drop of crude oil price would have positive effects on our economy. Like Chairperson Yellen the other day, he insisted that household could increase real income, and the Japanese economy could benefit from improved terms of trade.

It may have caused some confusion among the observers of the press conference, although the Governor's line of argument is straightforward from the viewpoint of our fundamental economy. Series of questions by reporters suggest that many of them may understand that the BOJ's decision of the additional stimulus was simply due to the view that cheaper crude oil would rather harm our economy through dis-inflationary expectations.

The BOJ in fact implemented the additional stimulus, because the lower price of crude oil and its spillover effects on broader goods and services could delay improvements of inflation expectation. Nevertheless, Governor Kuroda insisted that such developments were problematic to the BOJ, because they observed some weakness of our economic recovery at the time of the additional stimulus.

This may be the most tough part of communication policy by the BOJ, however. At the end of October, the BOJ appeared to maintain their relatively bullish view. Moreover, they only released their outlook that had already taken account of the positive effects of the policy decision. Although Governor Kuroda suggested that we should pay attention to a counterfactual path of economy without economic stimulus, we would not have any clues at all.

Further additional stimulus

If you believe that the BOJ introduced the additional stimulus simply because of a negative impacts of lower oil prices on inflation expectation (without paying attention to conditions and outlook of aggregate demands), you could have an interesting expectation. Namely, you could argue that the BOJ should conduct further additional stimulus in the near future, because the crude oil prices have already dropped by over 30% since the end of October.

In reaction to such cynical proposals by the reporters, Governor Kuroda explained that underlying strength of our economic recovery has been improved partly because of the additional stimulus itself, and this is why the BOJ is less concerned about a potential negative effects of lower oil prices on our inflation expectation.

From longer-term points of view, some other reporters further asked Governor Kuroda if the BOJ is ready conduct another round of stimulus in coming months when our rate of headline inflation would be depressed further, even if the crude oil prices would stabilize around the current level.

Governor Kuroda, in reply to these questions, reiterated his strong intension to achieve the inflation target in two years time and expressed his commitment in doing anything without hesitations when the prospects of the achievement becomes vulnerable. Nevertheless, he also implied that such a contingent scenario seems to him less likely.

According to his accounts, rate of inflation in FY2015 is still expected to accelerate in later months, even if it could decelerate further in earlier months as the reporters speculates. This is because the level effects of crude oil prices could diminish at last if they would not fall further, and the aggregate supply and demand gap could become smaller with small magnitude of improvements of economic activities, in light of our extremely low potential growth rate.

Unfortunately, however, this inflation scenario may appear difficult to understand or simply strange to our markets.

Implications

One important implication from the discussion at the press conference today would be the significance of aggregate demand and supply conditions in the context of inflation targeting by the BOJ. It might be "technically" necessary for the BOJ to take account of such conditions, in order to differentiate two case of oil price drop in terms of policy formation.

It might be, however, a small but important step by the BOJ if this implies some signs of changing policy idea. We all remember that Governor Kuroda explained to us that a downward pressure on inflation for whatever reasons should be taken care of by the BOJ, since our inflation expectation would not be anchored firmly at this stage.

If the weight of aggregate demand and supply conditions in the policy thoughts by the BOJ becomes somewhat heavier, the idea of QQE could approach to a traditional macro-economic discretionary policy in spite of its unconventional scale. Moreover, features of a termination condition and normalization thereafter of the QQE could become different from what we currently expect.

Conclusion

In light of further downward pressure on inflation in coming months and of difficulties in communicating their inflation scenario through FY2015 as discussed above, midterm review of the outlook of economy and prices by the BOJ at the next MPM on January 21 would not be an easy task and could attract further attention by the press and the markets.

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