Notes on Financial Markets Vol.119

# Summary of Opinions at the MPM in January 2016

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## Introduction

It seems that "Summary of Opinions at the MPM" has functioned better than expected by the markets since its introduction in the last month, largely because it has covered a series of important policy decisions without considerable delay.

Let me discuss the points of discussion on the negative rate policy and its implications for the modified QQE evidenced in "Summary" released today.

## Assessment of economy

"Opinions on Economic and Financial Developments", as the first part of "Summary", implies the consensus view that there was a growing concerns about the downside risk of sentiments of firms and households. Its major source, according to the sentences in this part, was increasing uncertainties about the global economic and financial system, which was enhanced by the sharp fall in crude oil price and the instabilities of emerging economic and financial systems.

Moreover, all of the sentences referring to the risks above suggest that such psychological impacts could lead to the risk averse attitude toward economic activities, including increasing in nominal wages, which would undermine the ongoing improvement of underlying inflation.

In the meantime, a couple of sentences imply the confidence in the resiliencies of our domestic economy. While a sentence points out a possibility of deceleration of industrial production in coming quarter, "Summary" shows confidence in modest economic growth for coming years.

Therefore, as a main scenario, several sentences argue that the improvement of underlying inflation would remain intact for the time being. Nevertheless, other sentences imply the growing cautious views on the outlook of inflation, and expect further delay of the expected time to achieve the 2% target.

## Monetary Policy

In light of the introduction of the negative rate policy at January MPM, readers would like to focus on the two issues of discussion in "Opinions on Monetary Policy" part; 1) the rationale for additional stimulus this time and 2) the choice of specific option.

On the issue 1), proponents refer to the needs of pre-emptive action to prevent a suspension of improvements of underlying inflation. This line of thoughts seems to be consistent with the assessment of economy and inflation as discussed above. In contrast, opponents deny the imminent need to take action. According to several sentences, they were confident in underlying improvements of our economy and inflation, although they admitted the balance of risk was tilted to the downside.

Core of the discussion in this part is on the issue 2), however. On the one hand, proponents insist the benefit of increased flexibility from introducing the negative rate policy. In addition, they show the confidence in minimizing the costs to financial institutions by way of the three tier system. It is also interesting to note that a sentence refers to the benefits of learning from the experiences of some European states in dealing with the problems in practice.

On the other hands, opponents highlight the risk of introduction of the negative rate to mislead the market that the asset purchase has already faced its boundary. According to their concerns, it would all the more be true when taking account of the fact the BOJ had introduced a set of "Supplementary" measures in December MPM.

Moreover, they argue that the negative rate policy would not be consistent with the QE in terms of its purpose to increase monetary base, due to potential negative impacts on the incentives of financial institutions to participate in JGB operations. With this respect, a sentence raises the potential case that the BOJ could become a sole buyer of short- and medium-term JGBs when the JGB yield curve drops further.

Furthermore, they question the balance of benefits to our economy and the costs to our financial system, and suggest that the negative rate policy should be limited to such occasions as economic/financial crisis.

It is also interesting to note that opponents refer to its implications in the future. First, a sentence refer to the risk that the markets would request further reduction in policy rate whenever the market conditions lose stability. We could then observe further trouble of financial institutions and households, according to the concerns expressed in the sentence. Second, another sentence points out the risk of global competition of negative rate among central banks.

## Implications

Thanks to the "Summary" this time, we are able to understand that the most important point of divergence of the opinion among the board members was not the imminent need to take action, but the specific choice of policy measure.

In terms of its balance of benefits and costs, it is not surprising to observe the difference of opinion on its side-effects on financial institutions and households. Regardless of this aspect, proponents tend to highlight the enhanced flexibility thanks to this additional measure to the BOJ. In contrast, opponents see the risk in the opposing direction; introduction of negative rate could rather enhance the markets' fear about the limitation of the QQE.

It is also interesting to note that only the opponents refer to the issues relating to the dialogue with the markets and the overseas central banks. If the large part of effects are expected to transmit through domestic and international markets, these are the non-negligible issues.

All in all, readers of "Summary" this time would still feel uncertainty about the priority of policy measures for the management of the QQE when and if there are additional downside risks to our economy and inflation, because it does not include the discussion about the potential boundary of asset purchase in detail.

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