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Press conference by Governor Kuroda—Gap in communication

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Introduction

In spite of the diversified views in the markets, virtually no additional action by the BOJ today faced surprisingly strong negative reactions at least in Tokyo time. While Governor Kuroda showed confidence in the appropriateness of the policy decision today, there still seems to be some risks of miscommunication between the BOJ and the markets. Let me overview the ideas on the monetary policy decision along with the messages of their revised outlook of inflation and economy.

Assessment of economy

Members of the MPM made downward revisions of their outlook as widely expected. Median of expected rate of real GDP growth for FY 2016 has become 1.2% rather than 1.5% as of January this year. That of core CPI inflation drops to 0.5% from 0.8% previously.

Governor Kuroda explained that delayed recovery of the global economy was the important reason for the revision of economic growth. In terms of inflation, he referred to both the prospective low growth of our economy and weaker than expected wage dynamics as the core reason for downgrades.

Nevertheless, Governor Kuroda reiterated the view that virtuous circle of economic expansion would remain intact, largely supported by improving labor conditions and elevated level of corporate profits. In fact, their smaller downward revision of growth rate and inflation rate for FY 2017 suggests that lack luster developments of some major segments of economic activities – that includes consumption, business investment, housing investment and net exports – would be transitory from the viewpoints of members of the MPM.

Rationale for no action and its communication

Their confidence in resilient growth and inflation as an underlying scenario would in turn be the rationale for no action today by the BOJ. From a s different point of view, members of the MPM may think that the policy package introduced in January was powerful enough to take wait-and-see stance for the time being. Also from the technical viewpoint, the BOJ would have good reasons to wait for the FIs and the markets to adjust to the practices and impacts of NIRP

Nevertheless, the markets could still wonder whether NIRP bring about the effects on the economy and inflation that are mighty enough to support achieving the 2% target of inflation. Moreover, if weak dynamics of wage is one of the negative factors, it could continue to have downward pressures on economy and inflation beyond the timeframe of “transitory”. In light of such arguments, the markets also have good reasons to expect the additional stimulus at the April MPM.

In my view, this kind of gap in the idea was the fundamental backgrounds of diversified views concerning appropriateness of the policy action today. It should be noted, however, there may also be some additional factors that resulted in a negative surprise to the markets.

First, gradually growing pessimism about the effectiveness of the QQE may have played a role. Ironically, market’s speculation since last week about an introduction of a fund provisioning operation with negative interest rate may have relieved the exaggerated pessimism about the sustainability of QQE. Of course, such line of thoughts was partly backed by the misunderstanding that the negative rate operations could be substantial enough to become a pillar of QQE.

Second, the markets (including myself) believed that no policy action coupled with downward revision of economy and inflation at non-negligible magnitude could undermine the confidence in the BOJ’s commitment in achieving the 2% inflation target “as soon as possible”. In reply to the question on this issue, Governor Kuroda explained their confidence in underlying strength of our economy and reiterated their commitment in inflation target.

Lastly, the markets may have been impressed by the characteristics of policy actions by the BOJ under Kuroda regime. Like “Super Mario” story in the Euroarea, our markets would always seek some “positive surprise” on the BOJ’s monetary policy front.

As a result, the BOJ could feel at a loss when they are criticized that their no action was the fundamental cause of instabilities of the markets today. Because, from their viewpoints, the BOJ had little to do with speculation about an additional stimulus and its failure. And the markets could claim that they had several plausible reasons to expect some policy actions to enhance QQE.

A possible idea to avoid this kind of gap could be focusing on a medium-target of monetary easing by the BOJ. Like the FRB and ECB, the BOJ implies at times that easing financial conditions from macro-perspective is what the central bank could contribute to. If this is the case, the BOJ and the markets could utilize indicators of financial conditions as effectiveness of monetary policy. Its outstanding benefit over policy dialogue solely on indicators of underlying inflation is easiness of observation by both of the parties.

Outlook of monetary policy

Returning to fundamental aspects of monetary policy by the BOJ, we could still expect another round of additional stimulus not in the distant future. As discussed above, we should note that downward revision of the BOJ’s outlook was at least partly related to “endogenous” reasons rather than solely due to “exogenous” factors such as oil price dynamics. Moreover, risk-balance chart by members of the MPM revised today implies that majority of them are looking at downside risks (possibly generated in overseas economies) of their main scenarios on both growth rate and inflation rate.

This is the reason why Governor Kuroda confirmed his idea that the BOJ is always ready to conduct every option of policy measures without hesitation. Furthermore, Governor Kuroda made substantial efforts to remove pessimism in the market that meaningful measures of QQE are exhausting.

Ironically, large swings of the market prices since last week imply that the markets would still have hope that some policy actions could be effective, although they might be gradually diminishing in the long run.

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