

Introduction

Interestingly, some of the press reporters raised the issue of normalization of QQE, in spite of the fact that we are still distant from 2% inflation. It would imply that the core policy idea of QQE have not been shared well between the BOJ and its observers even at this stage of policy implementation.

Economic and inflation outlook

Before discussing the issues regarding the normalization of QQE, I briefly cover the quarterly revision of outlook by the members of the MPM.

As was emphasized by Governor Kuroda at the press conference, the MPM largely maintained its outlook at the time of January meeting. In fact, they made a few minor revisions of inflation outlook for FY2017 (from +1.5% to +1.4%), and of economic outlook for FY 2017 and FY2018 (from +1.5%→+1.1% to +1.6%→+1.3%).

In spite of the cautious comments above, tone of summary text of the outlook appear to be somewhat bullish, especially in near-term perspectives. The MPM in fact upgraded the current assessment of economic activities by firms with virtuous circle from export to business investment. Moreover, they confirmed that tightening labor markets may have started creeping pressures on nominal wages.

Members of the MPM maintained the view that risks of economic growth and inflation are still tilted downward. Moreover, their most likely sources still remain in overseas economies. Nevertheless, they downgraded the riskiness of some scenarios including downside shocks from Chinese economy.

Normalization of QQE

At the press conference today, some reporters requested to show the strategy of normalization of QQE. Readers may remember that Governor Kuroda's only reply to such requests was "it is too early" in previous cases. Governor Kuroda, however, gave a longer accounts today in comparison to this simplest answer.

Governor Kuroda mentioned that the concrete strategy of policy normalization should be organized depending on the conditions of economy, inflation and financial function just before the BOJ start the process of normalization. In fact, Governor Kuroda told a reporter that achieving the inflation target would be the appropriate time to discuss the strategy in detail. His idea would probably reflect the idea of the current forward guidance by the BOJ.

According to the comments by Governor Kuroda, this is the reason why the BOJ would not explain in detail the strategy of policy normalization. Governor Kuroda claimed that it could mislead the market to disclose the strategy at this stage, because it could be totally different from the actual strategy affected by economic environments in the future.

Press reporters may have been affected too much by the signs of policy normalization by major overseas central banks. Furthermore, in light of the longer distant to inflation target in Japan, the line of thoughts expressed by Governor Kuroda seems to be reasonable. At the same time, however, reporters may have good reasons to refer to the possibility of policy normalization at this stage.

Mechanism of faster inflation

Potential reason for the debate above would be skepticism about achieving the inflation target. Ironically, bullish view of economic activities coupled with somewhat cautious view of inflation included in the revised outlook could have aggravated the skepticism.

As the summary text of the outlook imply, the BOJ has relied on 1) reducing the GDP gap and 2) stimulating the inflation expectations for achieving the inflation target. And the BOJ confirmed at the time of its comprehensive review in September 2016 that transmission of 2) above would take time because the formation of expectation is adaptive (or backward). Moreover, inflation outlook released today suggests that reducing the GDP gap by higher rate of economic growth could have moderate positive effects on actual inflation. This could further lead to a vicious circle on inflation expectation by way of the mechanism of 2) above.

Against the line of argument, the summary text of economic outlook would claim that faster rate of economic growth in consecutive years that estimated potential rate of growth as is expected by the economic outlook would in the end lead to higher rate of inflation, which could trigger a virtuous circle of inflation expectation.

Series of questions raised by press reporters today may reflect that they are not persuaded by the above scenario of achieving the inflation target.

Moreover, it could become probable that the BOJ would still maintain QQE in FY2019, because members of the MPM expect weaker rate of economic growth. While a part of bearish view reflects the potential negative impacts of the next round of consumption tax hike, it also reflects a cyclical weakness of business activities. It would become challenging for the BOJ to proceed its normalization process of QQE when and if momentum of economic activities would lose.

Then from the viewpoint of some press reporters, a fine balance between the benefits of QQE and the costs and risks would have changed. Readers could agree that non-negligible portion of the market would share the skepticism.

Geopolitical risk

With regard to the press conference today, it should be noted that some other reporters raised the issue of this kind of risk emerging in our region. While Governor Kuroda avoided mentioning in detail the potential policy measures to maintain stabilization of the financial system, geopolitical risk could remain for the months ahead. In addition to the normalization of QQE, this may have become the topic that staff of the BOJ would silently discuss at their internal meetings.

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