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Press conference by Governor Kuroda – Calm down

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Introduction

From the fundamental viewpoint, it should apparently be a good news for the BOJ to make upward revisions on their quarterly outlook of the economy (even if they were modest). It is interesting, however, Governor Kuroda tried to avoid highlighting its constructive messages and to emphasize that we are still distant from 2% inflation.

Outlook of economy

According to its summary text, members of the policy board made a moderate upward revision on the momentum of business investment. Moreover, they appreciated the sustainability of expansion of private consumption. All in all, they expected the domestic economic activity would go along the path of gradual expansion, although the effects of fiscal policy measures would diminish.

In fact, the ranges of their forecast of real GDP growth rates from FY 2017 to FY 2019 were revised up. New ranges for these three years are: +1.8% to +2.0%, +1.3% to +1.5% and +0.7% to +0.9% respectively. Their new forecast implied that we could enjoy a faster economic growth rate than our potential in FY 2019 in spite of cyclical slowdown of our economy (coupled with some negative impacts of consumption tax hike).

Nevertheless, the summary text insisted that their current forecast was largely in line with their previous one (as of October 2017). While members of the policy board could claim that most of these positive developments had been expected as of October 2017, we could still suspect that their cautious tone of voices could be somewhat intentional.

Outlook of inflation

Members of the policy board also made modestly upward revisions on their inflation outlook. In fact, the summary text suggested that long-term expectation of inflation may have stopped falling further, and aggregate demand/supply gap may have improved further. As a result, they revised up their forecast range of CPI core inflation rate for FY2018 (+1.3% to +1.6%) with the median rate unchanged (at +1.4%).

Nevertheless, the summary text insisted again that their current forecast remained unchanged and evaluated balance of risks were still tilted downward. At the press conference today, Governor Kuroda confirmed several times that we are still distant from 2% inflation target.

Management of the QQE

As expected, a number of press reporters raised the issue of possible modification of target rates under the yield curve control (YCC). In fact, some of them asked about a set of potential conditions. Readers may remember that it has been a focus of attention by the markets and the press since later months of 2017.

With the backgrounds of cautious lines of thoughts on economy and inflation as reviewed above, however, it was consistent for Governor Kuroda to reiterate his idea that the BOJ should maintain the QQE until the achievement of inflation target. Moreover, Governor Kuroda claimed that any discussion on policy normalization at too early stage could reduce the effectiveness of monetary easing, by undermining the strength of policy commitment.

Domestic participants of the markets would not be surprised at all, because they have already noticed the modification of communication since around the time of December MPM meeting. Retrospectively, however, the fundamental reason for the BOJ to highlight the side-effects of the YCC in earlier months is still somewhat unclear.

Some in the markets seem to understand that earlier discussion by Governor Kuroda may have been intended to argue against an idea of additional stimulus within the MPM. Other seem to suspect that they might have been intended to test the reactions of the market under longer-term strategy of policy communication.

In my view, minimizing the side-effects could rather enhance sustainability of the YCC, especially when it would take lengthy period of time before achieving 2% inflation target. Some studies in Europe suggest that cost of negative interest rate on financial intermediation could become cumulative.

It would of course require articulate skill of communication, in order to avoid considerable reactions of the markets. With this respect, the timing of raising the side–effects would not have been favorable at best.

Looking from the global perspectives, the long-term yields of both US treasury notes and major European government notes has risen in a non-negligible manner. Moreover, depreciation of USD has become evident across the board. In such circumstances, it would be rational for global investors to direct their attention to a scenario of policy normalization by the BOJ.

Comprehensive review

Interestingly, some press reporters asked whether the BOJ would conduct the overall review of monetary policy framework. Governor Kuroda denied such cases, claiming that they are comfortable with the YCC introduced as a result of the comprehensive review of the QQE in September 2016.

While the markets would agree with the overall line of thought by Govenor Kuroda, they could still argue, for example, that co-existence of policy targets both in terms of quantity and interest rate could become a source of mis-communication at some stage. Regardless Governor Kuroda would renew his term or not, the MPM would have some task to enhance the efficacy of the QQE.

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