

Topic

Concluding Remarks

Date

March 14, 2016 (17:30pm – 18:00pm)

PanelistsMr. Isaya Shimizu, (Nikkei senior staff writer)
Tetsuya Inoue, Mr., General Manager, Nomura Research Institute (Moderator)**Summary****1. What QQE has achieved****Inoue (Moderator):**

• After three years of QQE, and I would like to hear your opinions on what the policy has achieved and what it has not.

Mr. Shimizu:

• Around this time each year we see numerous recaps of QQE. For the first two years the story was clear enough: the policy had had a positive impact on the markets in the form of a cheaper yen and rising stock prices, but the effect on the real economy had been limited. In the first two years, there were three main reasons why QQE did not provide a boost to the real economy. First, the fallout from the consumption tax hike was greater than the BOJ had expected. Second, export volume did not grow and the knock-on effects for production and employment were limited in spite of the weak yen. Third, falling oil prices had a significant impact on general prices, as the BOJ itself acknowledged.

• This year, however, it has been harder to come up with a clear-cut story. It may not be appropriate to discuss negative interest rates policy (NIRP) based on the market's reaction just effective for one month, but there are concerns about whether NIRP will provide the same kind of fillip to the markets that QQE did. One reason for the different impact of the two policies, as noted in the panel discussion, is that globally there are no longer any countries willing to accept a strong currency. In the first two years of QQE, the USD and the CNY, which was effectively pegged to the dollar, were allowed to appreciate, while QQE drove the yen lower. But China is now abandoning its strong-CNY policy and the US is increasingly trying to keep the dollar's strength in check. A key question then becomes how QQE is supposed to function when no major economy is willing to allow its currency to appreciate against the yen. At the same time, it has become clear that monetary accommodation will not work unless the government commits itself to enhancing the growth potential of Japan's economy.

2. Is unconventional monetary policy running out of road?**Inoue (Moderator):**

• The argument that unconventional monetary policy in a broader sense is approaching its limits is being made across the developed world. What is your view on this topic?

Mr. Shimizu:

• The points I made largely apply to the additional easing measures announced by the ECB the other day. Whether quantitative easing or negative interest rates, the main transmission mechanism for these policies was weaker EUR. The market's less-than-favorable reception to the latest measures is probably due to the perception that these policies will not work if no major economy is willing to allow its currency to rise.

• One of the side effects of NIRP is its negative impact on the banking sector. In Japan, the simplified question is whether banks can adapt to NIRP with their current business model. In the Eurozone, meanwhile, banks' fragility in terms of credit risk makes it difficult for the ECB to augment NIRP, as noted by ECB President Draghi at his press conference. On the other hand, the Eurozone has the "fiscal space" needed to carry out fiscal stimulus. In particular, it makes little sense for Germany to pursue a weak-currency policy at a time when it is running a current account surplus.

• From a longer-term perspective, the Eurozone-like Japan—needs to boost its growth potential with economic structural reforms. But to borrow a phrase used by former BOJ Governor Shirakawa, the central bank will be asked to respond to "acute symptoms" in the economy whether or not that is appropriate in theory. In that sense, I do not think that unconventional monetary policy is at an impasse, and I think a variety of new approaches are likely to emerge. However, we are entering a phase in which the limitations of such policies will become increasingly evident.

Inoue (Moderator):

•As the limits to the unconventional monetary policies to overcome the zero constraint become clear, do we need to provide a larger "margin of safety" for the inflation target?

Mr. Shimizu (Moderator):

•The "global standard" for inflation targets is 2%. This number is based on the upward bias of price indices and the asymmetry of deflationary and inflationary risks. As noted in the panel discussion, the yen will come under upward pressure if Japan does not adopt the standard target of 2%. In theory, it may be worthwhile to discuss whether 2% is the most appropriate level given the view that the developed economies have entered a period of long-term stagnation. And with the limitations of unconventional monetary policy growing increasingly evident, I think we need to reconsider whether it makes sense to maintain powerful accommodative monetary policies for achieving an inflation target. However, Japan risks further appreciation of the yen unless this discussion is coordinated at the international level.

3. Dialogue with the market**Inoue (Moderator):**

•What issues have there been over the last few years in terms of central banks' dialogue with the market?

Mr. Shimizu:

•At an earlier Financial Markets Panel conference, Mr. Inaba made a very important point. He said market participants believe—incorrectly—that central banks have information that is not available to them. For example, the market interpreted the FOMC's "dot chart" last December as signaling the FRB's intention to hike rates four times in 2016, but in fact the FRB does not appear to have been that hawkish. I think that interpretation was based on the illusion that FOMC members held information or knowledge regarding the economic and price outlook that market participants did not have.

•Mr. Inaba also touched on the possibility that central banks hold superior information regarding the state of financial institutions obtained via their bank supervision. Having reported on central banks for 20 years, I do get the sense that they bring together some of a nation's most talented economists, and yet their economic forecasts still tend to miss the mark by quite a wide margin. Vague projections by a central bank tend to be criticized in the media for lacking in transparency, but they may just be a reflection of a great deal of uncertainty in the economic and financial environment. In any event, problems related to the central bank's dialogue with the market will not go away unless we begin from the truth pointed out by Mr. Inaba.

Inoue (Moderator):

•In the US as well, a comparison of the FOMC's December growth forecast for the next year with actual recorded growth shows that the FRB has consistently overestimated the strength of the economy since the global financial crisis. Hence the FRB is sometimes criticized for failing to accurately grasp structural changes in the economy and financial sector since the crisis.

4. Future topics for Financial Markets Panel**Inoue (Moderator):**

•At every Financial Markets Panel conferences, I ask what sorts of topics we should discuss in the future.

Mr. Shimizu:

•One panelist said today it would be difficult for Japan to put deflation behind it with monetary policy alone. Even if that is true, I think it has to be presented as a legal argument for it to carry any weight at the central bank. The BOJ Governor Kuroda has taken a different stance from the so-called reflationists; he is not arguing that deflation is always and everywhere a monetary phenomenon. What he is saying is that deflation may have monetary causes and it may have non-monetary causes, but inasmuch as the central bank is legally responsible for assuring price stability, its duty is to fight deflation. To argue that monetary policy alone is not sufficient to overcome deflation seems to be talking at cross-purposes.

•Governor Kuroda has also passed the bar examination, and he often takes a legal approach to issues. I get the impression that this sort of approach is emphasized at the BOJ, perhaps partly because many of the people playing key roles in the policymaking process also have legal backgrounds. The Bank of Japan Act's mandate for the BOJ is to ensure stable prices and a stable financial system. Regarding the former, the BOJ has gradually moved to a numerical target since defining price stability in October 2000 as a state of affairs characterized by neither deflation nor inflation. In January 2013 it defined price stability as an inflation rate of 2%.

•Clearly stipulating the principle in the legislation that deflation - unlike inflation - could not be prevented solely by monetary policy has been criticized for having the potential to lead to dangerous outcomes, even if it captures an important point. In other words, an attempt to revise the Bank of Japan Act could lead discussion in a variety of other directions. In that sense, I think it is important that this discussion be conducted at the international level (much like discussion of the inflation target, as noted earlier). In any event, even if the thesis that deflation cannot be overcome using monetary policy is true, it will ultimately need to be presented as a legal argument.

Inoue (Moderator):

• These are very complex issues. As was suggested in the panel discussion, we may also need to prepare a proper legal argument for the central bank's role in maintaining financial stability from macro perspective. While it is difficult to say when these specific issues might be raised, I think we need to prepare for them. Mr. Shimizu, thank you very much for your time today.
