

## Introduction:

In spite of earlier expectations, press conference by Governor Kuroda this time was rather crowded by the reporters. They may have wanted to see whether the BOJ would revise down their economic outlook due to substantial underperformance of our export in 1H of this year as well as growing tensions of geo-political risks. Hear are my impressions of Governor Kuroda's comments.

## Slight revision of statements

In response to the economic indicators recently released, the BOJ actually made the revisions of their policy statement. First, the BOJ described that our export has been actually weak. In fact, many in the markets have some fears that the export would not be easy to be recovered because of important factors including 1) losing competitiveness of our exports and 2) shift in production facilities by Japanese corporations.

Second, the BOJ admitted that our industrial production in recent months was also weak. Because the weakness was largely in relation to transportation machinery and there may be unexpected increase in domestic inventory of their products, we suspect that the weakness in production was largely due to carried-over effect of the consumption tax hike, especially on auto-mobile sales.

All in all, market participants have been concerned that these developments could decelerate our economic recovery this year, which could result in the underperformance of the inflation target by the BOJ in FY2015 in the end.

Interestingly, however, Governor Kuroda reiterated his views on these developments. He insisted that some weakness of industrial production would be limited and temporary. Moreover, he expected our exports would grow gradually in accordance with the recovery of global demands. He explained that lackluster developments of our exports may have been due to cyclical factors including severe weather in the US and slower recovery of south-eastern Asia.

It would be worth thinking about a reason for such divergence of the tones of voices between the statement and the Governor's comments. It could be a sign of possible slight differences of the views among the members of the policy board with regard to the economic outlook. We would look forward to the minutes of the MPM this time, as well as their next semi-annual revision of economic outlook in October.

## Policy transmission

At the press conference, some reporters also raised the implications of higher and spreading risks of geo-politics to our economy. While Governor Kuroda admitted that potential impacts could be complicated and would be hard to explain in detail at this juncture, he said he would not expect that the impacts could affect the BOJ's economic outlook considerably.

There could be some possible reasons for his rather optimistic view. First of all, Japanese economy has less direct economic relations with some areas in concerns. Probably Governor Draghi, for example, has more reasons to think this issue seriously. In addition, Governor Kuroda might be confident about our economic recovery, because the important drivers have been domestically oriented. Both private consumption and fiscal expenditures have contributed to the success of Abenomics so far, in spite of the underperformance of our exports discussed above.

While this line of argument seems to be reasonable, we may need to think another transmission venue of the impacts of geo-political risk. That is the market developments. Whenever risk aversion grows in the markets, JPY rates tend to appreciate and our stock prices tend to drop. When we remember that the developments of these important markets have played significant roles for our economic recovery so far, we may have good reason to be concerned about the transmission of geo-political risks through this channel.

Governor Kuroda reiterated his optimistic views in spite of these possible concerns, possibly because he may believe our economic recovery has already gained self-sustained mechanism depending on domestic factors, although the recovery was initially triggered by the market developments. His understandings of the mechanism of our economic recovery would be tested in the future course of global economic and political developments.

## Answer to criticism

Lastly, a reporter asked what kind of policy action the BOJ should take when there emerges some criticism among general public against the inflation policy. In fact, articles of national newspapers suggest that some people are frustrated by the actual decrease in real wages, due to slower increase in nominal wages than the rate of inflation.

Overseas readers of this Notes may like to note that upward revision of nominal wages, especially in the part of regular wages, may be still on the way. Although large corporations actually agreed to revise the labor conditions, managers of SMEs seem to remain cautious about increase in labor costs.

While Governor Kuroda admitted it would be the case currently even from macro-economic perspectives, he argued that the real wages have been decreased largely by the acceleration in the pace of inflation by the consumption tax hike, whose impacts would be temporary in nature.

Nevertheless, the BOJ seems to pay more attention to this line of criticism recently. In fact, Governor Kuroda discussed this issue in detail in his speech on August 1. He in fact raised two points against the criticism. First, modest 2% inflation would encourage economic agents to make positive consumption and investment. Second, our economy could become vulnerable again to economic shocks, unless modest 2% inflation would be maintained.

Thus, the BOJ could need to deal with some political issues, even if they could successfully achieve the inflation target. This is one of the reasons why Governor Kuroda has been vocally requesting the government to pursue the economic growth strategy by structural reforms. Whether this strategy would be successful is still uncertain, because it would naturally take time to have the fruits of structural reforms.

**Author: Tetsuya Inoue**  
**General Manager and Chief Researcher**  
**Financial Technology and Market Research Department**  
**Nomura Research Institute**

This note is intended solely for informational purposes and should not be construed as investment advice. The author does not guarantee the accuracy or completeness of the information contained. Opinions in this note are those of the author and do not represent the views of Nomura Research Institute or Financial Technology and Market Research Department. This note is exclusively for the personal use of those receiving it directly from the author.