mni

All Signal, No Noise

MARKET ANALYSIS

MNI BoJ Preview – July 2020

Meeting Date: Tuesday July 14 – Wednesday July 15 2020

Statement Release Time: N/a

Link To Statement: http://www.BoJ.or.jp/en/mopo/mpmsche_minu/index.htm/

Contents

mni Central Bank Watch - Bank of Japan

MNI Bank of Japan Data Watch List

Inflation		Current	3m ago	3m Chg	6m ago	6m Chg	2Y History	Hit / Miss	Vs Trend	Surprise Index	Z-Score
Tokyo CPI	% y/y	0.3	0.4	↓	1.0	↓					-1.23
Tokyo CPI - Ex Fresh Food	% y/y	0.2	0.4	↓	0.8	↓					-0.71
PPI	% y/y	-1.6	-0.5	↓	0.9	↓					-0.68
Inflation Swap 5y5y	%	-0.20	-0.23	↑	0.15	↓					-0.70
Economic Activity		**Current**	**3m ago**	**3m Chg**	**6m ago**	**6m Chg**	**2Y History**	**Hit / Miss**	**Vs Trend**	**Surprise Index**	**Z-Score**
Industrial Production	% m/m	-8.9	-0.3	↓	-0.6	↓					-2.59
Tertiary Industry Index	% m/m	-2.1	-0.7	↓	1.0	↓					0.07
Core Machinery Oders	% m/m	1.7	2.3	↓	11.9	↓					0.35
Exports	% y/y	-28.3	-1.0	↓	-7.9	↓					-1.82
Monetary Analysis		**Current**	**3m ago**	**3m Chg**	**6m ago**	**6m Chg**	**2Y History**	**Hit / Miss**	**Vs Trend**	**Surprise Index**	**Z-Score**
M2 Money Supply	% y/y	7.2	3.2	↑	2.7	↑					3.91
Bank Lending	% y/y	6.2	2.0	↑	1.8	↑					1.97
Loans Outstanding (Bus)	% y/y	8.31	2.36	↑	2.02	↑					2.20
Housing Starts	% y/y	-12.3	-12.3	→	-12.7	↑					-0.78
Consumer / Labour Market		**Current**	**3m ago**	**3m Chg**	**6m ago**	**6m Chg**	**2Y History**	**Hit / Miss**	**Vs Trend**	**Surprise Index**	**Z-Score**
Retail Sales	% y/y	-12.3	1.6	↓	-2.1	↓					-2.40
Household Spending	% y/y	-16.2	-0.3	↓	-2.0	↓					-1.95
Unemployment Rate	%	2.9	2.4	↑	2.2	↑					1.98
Ave Monthly Cash Earnings	% y/y	-2.1	0.7	↓	0.1	↓					-2.07
Markets		**Current**	**3m ago**	**3m Chg**	**6m ago**	**6m Chg**	**2Y History**	**Hit / Miss**	**Vs Trend**	**Surprise Index**	**Z-Score**
Nikkei 225	Index	22288	18917	↑	23657	↓					0.40
Japanese 10-Year Yield	%	0.03	0.02	↑	-0.01	↑					1.03
Japan Yield Curve (2s-10s)	bps	15.9	15.7	↑	12.0	↑					1.01
JPY TWI	Index	117.00	119.01	↓	115.59	↑					-0.32

Source: MNI, Bloomberg

Business Address – MNI Market News, 5th Floor, 69 Leadenhall Street, London, EC3M 2DB

MNI POV (Point Of View): All Quiet On The Eastern Front

The upcoming Bank of Japan (BoJ) meeting should come and go without much of a fuss. Broad expectations look for the Bank to leave its policy settings unchanged, as it remains alert to the “severe” downside risks surrounding the economy, but still expects a pickup in activity as we move through the remainder of the year.

Recent rhetoric, both from Governor Kuroda and from the summary of opinions of June’s monetary policy decision, point to the Bank adopting a wait and see approach, with the methods deployed in recent months expected to do the heavy lifting.

On forward guidance, the Bank should reiterate that “for the time being, the Bank will closely monitor the impact of COVID-19 and will not hesitate to take additional easing measures if necessary, and also it expects short- and long-term policy interest rates to remain at their present or lower levels.”

The Bank will release its latest round of economic projections, and should revert to the typical point-based estimates this time out, as opposed to the estimate bands that were introduced in April’s Outlook for Economic Activity and Prices, which were a product of the uncertainty surrounding the outbreak and spread of COVID-19.

The GDP growth outlook will probably be based around the lower end of the ranges outlined in April, given the lengthening of the domestic COVID-19 restrictions vs. that which was outlined at the time of the April decision, and the knock on impact of the virus, both at home and abroad, in the time since. That is without factoring in the most recent uptick in Tokyo’s virus cases, which could further hamper sentiment.

A reminder that the Bank’s recently released quarterly regional report noted that “according to assessments from regions across Japan, all nine regions revised down their assessments from the previous ones, as was the case in April 2020, due to the impact of the novel coronavirus (COVID-19), and reported that their economy had deteriorated or had been in a severe situation.”

The Bank’s active Rinban approach (which is aiming to manage yields against a backdrop of increased JGB issuance owing to a greater fiscal burden in the wake of COVID-19, while looking to foster a steeper yield curve), presents the most dynamic part of the Bank’s monetary policy arsenal at present, but hasn’t yielded much in the way of notable surprises, yet, scaling up (for JGBs with up to 10 Years until maturity) to manage yields amid the uptick in supply.

As a side note, Toyoaki Nakamura will cast his vote for the first time at the upcoming meeting. He isn’t expected to break from the majority. As such, expect Kataoka to be the lone dissenter on the board. Kataoka’s dissent will almost certainly take two forms, as per the June meeting:

- “Considering that it was desirable to further strengthen monetary easing by lowering short- and long-term interest rates, in response to a possible increase in downward pressure on prices and with the aim of alleviating firms' and households' interest burden.”
- “Given the severe impact of COVID-19, further coordination of fiscal and monetary policy was necessary and it was appropriate for the Bank to revise the forward guidance for the policy rates to relate it to the price stability target.”

Base Case: No change to the Bank’s monetary policy settings and forward guidance, with ’20 GDP expectations pegged towards the lower end of the range that the Bank outlined in April.

Dovish Case: Little scope for an outright dovish surprise, given the recent Bank communique. Perhaps a dovish tweak to the forward guidance or a GDP outlook that is towards the bottom of the outlined range for the current year, coupled with a softer than expected GDP projection for the following year.

Hawkish Case: Once again, it really is all about the forecasts, given Governor Kuroda’s recent run of rhetoric. No real space for an outright hawkish surprise, with any hint of a glass half-full approach/greater focus on the recovery providing the only realistic sources of a hawkish tinge.

MNI PREVIEW: BoJ Set For July Hold; Still See H2 Recovery

--To Eye Transmission Effects Of Latest Policy Moves

By Hiroshi Inoue

TOKYO (MNI) - The Bank of Japan will stand pat on monetary policy at the July meeting, taking stock of recent decisions that has facilitated funding for companies of all sizes impacted by the spread of the Covid-19 virus.

Policymakers believe the enhanced lending schemes are having the desired transmission effect and will use the two-day meeting to review the medium-term growth and inflation outlooks.

Bank economists still sees the economy in a 'severe' situation after the sharp Q2 slowdown, but believe Q2 saw the low point, with the recovery underway in H2, albeit at a slower pace than initially expected as lingering health concerns and social distance restrictions keep some consumers home.

The high uncertainty as to how the virus will play out and impact the global economy, with downside risks for Japan's exports and corporate capital investment plans, stopped the BoJ agreeing on a single forecast back in April, offering a forecast range instead.

--RISKS

Although many of those risks remain, the BoJ could follow the Federal Reserve's lead and reintroduce and single median forecast in July. However, it will be a matter of communication for the BoJ board - using a single point to highlight an improved outlook or a forecast range to underline the risks remaining.

Certainly the BoJ's medium- to long-term growth expectations are unchanged, underpinned by solid capital investment in software, automation and research and development. The bank also expects the policy measures put in place by the government and the BoJ will help protect jobs and support smaller companies through Japan's summer months.

But there is still a concern that the slower pace of recovery in the service sector, particularly across the hospitality industries, will manifest in a renewed cash crunch around the time of the BoJ's October meeting and Outlook report.

Business Address – MNI Market News, 5th Floor, 69 Leadenhall Street, London, EC3M 2DB

MNI INSIGHT: BoJ Doesn't See JGB Yield Spike, Eyeing Auctions

--BoJ Sees Investor Demand Smoothing any Future Spike in Yields

By Hiroshi Inoue

TOKYO (MNI) - The Bank of Japan believes its own front-loaded buying and attractive investment rates for life and pension funds will prevent a sharp rise in JGB yields over coming months, even as government issuance increases, MNI understands.

With the increased auctions just getting underway, policymakers are aware that markets may have misunderstood the bank's actions over the last month or so, with some investors of the view the BoJ is falling short in its promise to match issuance with purchases.

But the BoJ points to the fact it has increased its bond buying since April, paving the way for the flood of bonds coming from Japan's Ministry of Finance.

MOF has increased its bond issuance for the current fiscal year by JPY59.5 trillion following a second supplementary budget, with an increase in auction sizes across the maturity spectrum. The BoJ has, by-and-large, increased the size, if not frequencies, of its bond-buying operations to match the new sale schedule.

The one bucket of operations that didn't see an increase announced for July was the longer-end of the curve, with BoJ officials noting that the size of issuance was little changed in that sector if the curve. This in part reflects the fact the bank would tolerate modestly higher yields at the longer-end of the curve, but it certainly isn't trying to engineer such a move.

--FOREIGNERS NET SELLERS

BoJ officials are also watching foreign investors, who have been net sellers of JGBs over recent weeks, and what impact that has had on yields. There has been anecdotal evidence of offshore accounts switching out of JGBs into U.S. Treasuries - partly for a yield pick up and partly to ensure dollar liquidity in their portfolios.

The MOF is expected to further increase its bond issuance later in the fiscal year, as it looks to to cover the drop in tax revenues, with a third and possibly even a fourth supplementary budget needed.

BoJ Outlook for Economic Activity and Prices - April 2020

Forecasts of the Majority of the Policy Board Members

y/y % chg.

	Real GDP	CPI (all items less fresh food)	(Reference) Excluding the effects of the consumption tax hike and policies concerning the provision of free education
Fiscal 2019	-0.4 to -0.1	+0.6	+0.4
Forecasts made in January 2020	+0.8 to +0.9	+0.6 to +0.7	+0.4 to +0.5
Fiscal 2020	-5.0 to -3.0	-0.7 to -0.3	-0.8 to -0.4
Forecasts made in January 2020	+0.8 to +1.1	+1.0 to +1.1	+0.9 to +1.0
Fiscal 2021	+2.8 to +3.9	0.0 to +0.7	
Forecasts made in January 2020	+1.0 to +1.3	+1.2 to +1.6	
Fiscal 2022	+0.8 to +1.6	+0.4 to +1.0	

Notes: 1. Given that there are higher uncertainties regarding the outlook, in the April Outlook Report, each Policy Board member made their forecasts as a range and submitted two figures (i.e., the highest and lowest figures) within the range of 1.0 percentage point at most. The forecasts of the majority of the Policy Board members are shown as a range excluding four figures -- namely, the two highest figures and two lowest figures among the forecasts of the nine members. (If a member submits the same forecast figure for the highest and lowest figures, it is counted as two separate figures.) In the January Outlook Report, the forecasts of the majority of the Policy Board members also were shown as a range, excluding the highest and lowest figures, but each member's forecasts took the form of point estimates. Thus, it should be noted that the definition of the forecasts of the majority of the Policy Board members in the January Outlook Report is different from that in the April Outlook Report.

2. Each Policy Board member makes their forecasts taking into account the effects of past policy decisions and with reference to views incorporated in financial markets regarding the future conduct of policy.

3. The direct effects of the October 2019 consumption tax hike on the CPI for fiscal 2019 and 2020 are estimated to be 0.5 percentage point for each fiscal year. In addition, based on a specific assumption using information available at this point, the direct effects of policies concerning the provision of free education on the CPI for fiscal 2019 and 2020 are estimated to be around minus 0.3 percentage point and around minus 0.4 percentage point, respectively.

4. The CPI (all items less fresh food) for fiscal 2019 is an actual figure.

Analysts' Key Comments

Bank of America Securities:

- The BoJ wraps up another two-day monetary policy meeting (MPM) on 15 July. Having already moved aggressively with its COVID-19 response over Mar-Jun, we expect the board to leave all key policy targets unchanged.
- The summary of opinions for the June MPM also suggest the majority of board members believe the central bank has done enough for now to cushion the blow from COVID-19: one member noted that it was "desirable to carefully confirm and examine" the effects of the BoJ's COVID-19 response measures "for the time being."
- The results of the June Tankan should bolster the central bank's confidence that its various liquidity and credit support measures-together with government actions-have so far stemmed a destructive tightening in corporate financing conditions. For example, bank lending conditions remain accommodative, in stark contrast to the situation during the '97-'98 domestic banking crisis and '08-'09 Global Financial Crisis.

Barclays:

- We expect the BoJ to retain current policies, opting in the near term to confirm the effects of the various easing measures taken since March, led by the JPY110tn Special Funds-Supplying Operations to Facilitate Financing in Response to the Novel Coronavirus (COVID-19).
- In the quarterly Outlook report, to be released at the end of the meeting, we expect the BoJ to lower its FY20 GDP growth forecast to reflect the government's extension of the emergency declaration (from 7 April-6 May to 7 April-25 May) after the forecasts were last updated in April, which likely led to a steeper contraction in Q2. Although the BoJ will likely retain its baseline outlook for the economy to return to a recovery path in H2, with business sentiment showing signs of bottoming in the June BoJ Tankan, it will likely also emphasize the uncertain outlook with new COVID-19 infections rising again, especially in Tokyo.

Goldman Sachs:

- We expect the status quo across all monetary policy parameters, including short- and long-term policy rates (yield curve control), asset purchase programs (JGBs, ETFs, etc.), and corporate finance support programs introduced and enhanced between March and June in response to COVID-19.
- Considering that the Summary of Opinions from the June MPM included comments by some policy board members that COVID-19 response measures are largely in place, we believe the BoJ will be content to monitor the effectiveness of these measures for the time being.
- The BoJ is due to release its quarterly Outlook Report. We expect the BoJ to revise down its real GDP growth outlook for FY2020, broadly in line with the downward revision by the IMF and other organizations, while it is likely to maintain the baseline scenario calling for modest recovery from the second half of 2020, with the emphasis on downside risk going forward. The BoJ already cut its outlook for FY2020 sharply to a range between -5.0% and -3.0%, from +0.9% as of January (no median projection was disclosed in April because of the high level of uncertainty). A number of economic data have already been announced for April-May, when the state of emergency was in effect, and thus uncertainty regarding FY2020 growth has likely declined to some extent. We therefore think the BoJ will include a median projection in the July Outlook Report, and we expect it to be around -5%, which corresponds to the lower end of the projection range as of April, but is still slightly more bullish than the consensus estimate.
- Other than this, we basically expect the status quo, with each abound the midway of the projection range as of April.

Business Address – MNI Market News, 5th Floor, 69 Leadenhall Street, London, EC3M 2DB

HSBC:

- We expect the BoJ to leave its policy settings unchanged.
- The Bank's broad-based monetary easing options are limited, and as such, while the economy is hard hit by the COVID-19 outbreak both domestically and externally, the central bank is likely to remain on hold. The focus is on the Bank's open market operations, with the BoJ's assets expanding at an annualised JPY192.1tn pace in March-June. This is much faster than JPY21.0tn in 2019. While the USD operations drove the accelerated expansion in March, the central bank became more active in loan provisions and T-bill purchases more recently.
- Meanwhile, the BoJ will also release its new set of economic forecasts, which is unlikely to show any meaningful revision to both growth and inflation. The Bank's current forecast is roughly in line with our forecasts that imply a gradual recovery in H2 2020. Indeed, retail sales posted a partial recovery in May, while employment stopped falling. On the external front, early data from June suggests a mild recovery on a m-o-m basis.

J.P.Morgan

- The BoJ will stay on hold but start the discussion of how to revive economic growth and avoid deflation. We think this autumn the BoJ likely will strengthen its forward guidance which is now linked to only COVID-19. The June MPM was the starting point of discussion as to how it should promote the economic recovery, and the July MPM likely will start the discussion of concrete steps.
- First of all, by the June MPM the BoJ had completed preparing the credit easing of a total of JPY110tn (20% of GDP), the unlimited provision of JPY and USD with aggressive purchase of JGBs without any guidance and the dollar-funds supplying operations, and expansion of the purchase amount of ETFs (JPY12tn) and J-REITs (JPY180bn) for the COVID-19 crisis. At the July MPM the BoJ is likely to check the effects of those policies especially through the credit easing policy.
- The BoJ will publish the new Outlook Report which covers the period until FY2022. In April the Bank disclosed its forecast only as a range, but as the uncertainty about growth and inflation is reduced, it likely will disclose the point predictions again. We expect the BoJ to forecast a deep recession this fiscal year and a partial recovery for FY2020 and FY2021 with downside risks. Although this growth outlook ensures the negative output gap continues, its forecast for the CPI will turn positive for FY2021 after negative growth in FY2020 while emphasizing the downside risks for these forecasts. Even with such an optimistic scenario for the price outlook, we do not expect the BoJ to draw a picture that has CPI growth coming close to the 2% target by the end of 2022.

Mizuho:

- We think the Bank has broadly finished rolling out new policies aimed at supporting corporate financing and stabilizing the markets, and expect a majority of board members will vote to keep policy on hold.
- The Bank will publish its quarterly Outlook report (the Bank's view) at this meeting. Reuters reported on July 6 that the Bank is likely to maintain its baseline scenario that the domestic economy will recover toward the end of the year. The April Outlook report noted that "Given that there are higher uncertainties regarding the outlook, each Policy Board member made their forecasts as a range and submitted two figures (i.e., the highest and lowest figures) within the range of 1.0 percentage point at most." In addition, the forecasts of the majority of board members were presented as a range that excluded the two highest and lowest figures, rather than the usual practice of showing a median. Bloomberg reported on
- July 7 that BOJ officials say opinion within the Bank is divided about whether it should continue to present forecasts using this new method. Some believe the environment is too uncertain for normal pinpoint forecasts, while others argue that the outlook has cleared enough to warrant a return to announcing the median of the forecasts of the nine board members. In addition, the forecasts of the majority of policy board members for real economic growth could be revised down.
- We expect the Bank to return to its usual method of presenting the median forecast of the majority of policy board members given that some economic data is starting to reflect the calmer, post-corona environment. We present our expectations for the median forecasts of real GDP and core CPI on the following page.
- We expect Governor Kuroda to reiterate at his press conference that the outlook is extremely unclear and that the Bank is focused on responding to the crisis.

NatWest:

- As noted below, we expect the BoJ will once again downwardly revise the outlook for the growth rate at this meeting. However, we do not expect this downward revision will lead to a change in monetary policy. It is not only that financial markets remain stable; Japan is confronting the least deflationary pressures attributed to the novel coronavirus (COVID-19) of all major developed countries. In addition, the allocation for "the Special Program to Support Financing in Response to the Novel Coronavirus (COVID-19) (Special Program)", which was introduced to support corporate financing, was increased from 75 trillion yen to 110 trillion yen at the June meeting. The second supplementary budget for FY2020 incorporated an increase in the effective interest-free and unsecured loans, so the increase in the size of the allocation in June can be seen as an automatic response to the government's budgetary provisions. The BoJ did not see any need for additional measures at the June Policy Board meeting. Even so, the allocation itself was still increased.
- Furthermore, in the June Tankan survey, released last week, the business conditions DI dropped substantially for both manufacturing and nonmanufacturing, yet the deterioration in corporate financial positions was limited. This suggests that fiscal and monetary policies are having a certain impact. The financial position DI ("easy" – "tight") of large enterprises deteriorated 8 points from the March survey to +10%pts. Similarly, the DI for small enterprises deteriorated 9 points to -1%pt. In addition, the lending attitude of financial institutions DI ("accommodative" – "severe") to large enterprises deteriorated 6 points from the March survey to +16%pts, while the same DI for small enterprises improved 1 point to +19%pts. Even when compared to the past, the deterioration in the lending attitude of financial institutions DI was limited, and there is clearly a stance towards limiting the deterioration of corporate financial positions. Consequently, we expect there will be no change in monetary policy at the July Policy Board meeting.
- The Outlook Report will be released at the same time as the forthcoming Policy Board meeting. The IMF released its global economic outlook in late June. This included a downward revision for Japan's 2020 growth rate to -5.8% from -5.2% in April and for 2021 from +3.0% to +2.4%. In the April Outlook Report, the BoJ forecasted a growth rate for FY2020 of between -5.0% and -3.0% and for FY2021 of between +2.8% and +3.9%. However, the spread of COVID-19 is unabated in some developing and emerging countries while a second wave is also evident in some developed countries such as the US. It is highly likely that concerns about a protracted global spread and a second wave were not considered as the main scenario in the April Outlook Report. Consequently, we anticipate the forecast range of growth rates for FY2020 and FY2021 will be downwardly revised by about 0.5% points.
- On the other hand, we anticipate a slight upward revision in the price outlook, reflecting the recent strength in the core inflation rate even as the growth rate has slumped. In the April Outlook Report, the BoJ forecasted core CPI to be in a range of -0.7% to -0.3% in FY2020 and in a range of 0% to +0.7% in FY2021. However, Japan is confronting extremely limited deflationary pressures on its core inflation rate attributed to COVID-19 compared to other major developed countries. Although the contribution to the core core CPI (YoY) of goods and services (eating out, clothes and footwear, transportation, motor vehicles, recreational services) negatively affected by COVID-19 fell by 0.13% points in April, this rose by 0.10% points in May returning to February levels. In addition, considering the results of the June Tokyo metropolitan area CPI, this contribution is likely to once again fall in the June nationwide CPI but it is highly likely that the fall will be only slight. Consequently, we anticipate the ranges for the price outlooks for FY2020 and FY2021 will be upwardly revised by about 0.1% point.

Societe Generale

- We expect no change in monetary policy, with the negative interest rate on part of the current account balance remaining at -0.1% and the long-term (10yr) JGB yield target kept at around 0.0%. However, to further reduce the likelihood of any credit or liquidity deterioration and any decaying of structural elements of the economy, then the bank could move forward with an enhancement of the current support measures, increasing the funds provided under the new programme it announced in May. Rate guidance The BoJ is unlikely to make any policy adjustments until sometime in 2022. We expect the first step to be the raising of the long-term yield target from the current 0.0%. The BoJ will likely not change its negative interest policy until sometime in 2023. Economic assessment A new outlook report reflecting developments since April will be released at the July meeting. We expect the BoJ will maintain the view that "Japan's economy is likely to remain in a severe situation for the time being due to the impact of the spread of the novel coronavirus (COVID-19) at home and abroad." With economic data continuing to show some weakness and inflation remaining muted, we expect the GDP and CPI outlook to be further revised downward.

TD Securities

- With global central banking taking a breather, the BoJ will be content to make no policy changes or signal one is in the offing. We think this will be the status quo for the foreseeable future. This meeting will be accompanied by a downgraded growth estimate in its Outlook Report. This should surprise no one however.