MNI BOJ Preview - October 2020

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Central Bank Watch - Bank of Japan

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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	0.2	0.3	↓	0.4	↓					-1.28
Tokyo CPI - Ex Fresh Food	% y/y	-0.2	0.2	↓	0.4	↓					-1.12
PPI	% y/y	-0.8	-1.6	↑	-0.5	↓					0.29
Inflation Swap 5y5y	%	-0.04	-0.20	↑	-0.23	↑					0.32
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	1.0	-8.9	↑	-0.3	↑					0.44
Tertiary Industry Index	% m/m	0.8	-3.5	↑	-0.7	↑					0.31
Core Machinery Oders	% m/m	0.2	1.7	↓	2.3	↓					0.17
Exports	% y/y	-4.9	-26.2	↑	-11.7	↑					1.14
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	9.0	7.2	↑	3.2	↑					2.46
Bank Lending	% y/y	6.4	6.2	↑	2.0	↑					0.84
Loans Outstanding (Bus)	% y/y	8.50	8.29	↑	2.38	↑					0.90
Housing Starts	% y/y	-9.1	-12.3	↑	-12.3	↑					1.01
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	-1.9	-12.5	↑	1.6	↓					-0.17
Household Spending	% y/y	-6.9	-16.2	↑	-0.3	↓					-0.05
Unemployment Rate	%	3.0	2.9	↑	2.4	↑					1.29
Ave Monthly Cash Earnings	% y/y	-1.3	-2.3	↑	0.7	↓					-0.44
Markets		**Current**	**3m ago**	**3m Chg**	**6m ago**	**6m Chg**	**2Y History**	**Hit / Miss**	**Vs Trend**	**Surprise Index**	**Z-Score**
Nikkei 225	Index	23419	22288	↑	18917	↑					1.23
Japanese 10-Year Yield	%	0.03	0.03	↓	0.02	↑					0.33
Japan Yield Curve (2s-10s)	bps	15.0	15.9	↓	15.7	↓					-0.06
JPY TWI	Index	118.22	117.00	↑	119.01	↓					-0.32

Source: MNI, Bloomberg

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MNI POV (Point Of View): Moving Along

The Bank of Japan's November monetary policy decision should be a relatively straight forward affair, with the Bank set to leave it monetary policy settings unchanged, as the government has set itself up to deploy another (relatively modest) round of fiscal support.

The BOJ is more than happy to let the government take up the slack, given years of ultra-easy monetary policy settings and the well-trodden questions surrounding the Bank reaching the practical limitations of loose policy. While Governor Kuroda and co. have stressed that they are not out of ammunition, the market doubts whether any further loosening would have the desired impact i.e. firing up inflation.

As such, the Bank is set to deem the COVID-19 fighting measures that it has deployed to date as ample, for now, and will leave the door open to doing more, if required, re-deploying its own brand of forward guidance:

"For the time being, the Bank will closely monitor the impact of the novel coronavirus (COVID19) 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."

We should also expect the traditional dovish dissent from Kataoka, who favours an even more aggressive brand of easing.

The Bank's corporate liquidity provisions, that are due to expire in March 2021, will likely be extended at some point, although the Bank will probably wait for the government to outline its next round of fiscal support (some, including MNI, have suggested the government could reveal its hand in November), meaning that the move is unlikely to come at the Bank's October meeting.

The update to the Bank's economic projections should ultimately be inconsequential for monetary policy, although the near-term CPI projections will probably be nudged lower.

Looking ahead, the Bank will likely look to deepen its credit easing methods as the next step along the path of further easing, if required. Although an extension of the existing facilities is much more likely, as outlined earlier. Its active approach surrounding its JGB/Bill purchases will remain in place, with a focus on the shorter end of the curve. A deeper move into negative rate territory would likely only be forthcoming if there is a structural shift in real rate spreads with the U.S. or in the case of notable, sustained JPY strength.

BOJ's July Economic Forecasts

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 2020	-5.7 to -4.5 [-4.7]	-0.6 to -0.4 [-0.5]	-0.7 to -0.5 [-0.6]
Forecasts made in April 2020	-5.0 to -3.0	-0.7 to -0.3	-0.8 to -0.4
Fiscal 2021	+3.0 to +4.0 [+3.3]	+0.2 to +0.5 [+0.3]	
Forecasts made in April 2020	+2.8 to +3.9	0.0 to +0.7	
Fiscal 2022	+1.3 to +1.6 [+1.5]	+0.5 to +0.8 [+0.7]	
Forecasts made in April 2020	+0.8 to +1.6	+0.4 to +1.0	

Notes: 1. Figures in brackets indicate the medians of the Policy Board members' forecasts (point estimates).

2. The forecasts of the majority of the Policy Board members are constructed as follows: each Policy Board member's forecast takes the form of a point estimate -- namely, the figure to which he or she attaches the highest probability of realization. These forecasts are then shown as a range, with the highest figure and the lowest figure excluded. The range does not indicate the forecast errors.

3. 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 were shown as a range excluding four figures -- namely, the two highest figures and two lowest figures among the forecasts of the nine members. Thus, it should be noted that the definition of the forecasts of the majority of the Policy Board members in the April Outlook Report is different from that in the July Outlook Report.

4. 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.

5. The direct effects of the October 2019 consumption tax hike on the CPI for fiscal 2020 are estimated to be 0.5 percentage point. In addition, based on a specific assumption, the direct effects of policies concerning the provision of free education on the CPI for fiscal 2020 are estimated to be around minus 0.4 percentage point.

Source: Bank of Japan

MNI Preview: BoJ To Hold; May Cut GDP View On Weaker Spending

By Hiroshi Inoue

TOKYO (MNI) - The Bank of Japan is expected to stand pat on monetary policy at its two-day policy meeting ending Oct. 29 since the economy is recovering gradually as it expected but the bank may lower its median growth forecast for this fiscal year as private spending and capital investment remain weak.

In July, the bank forecast the economy to contract 4.7% this fiscal year.

Subsequent data showed Japan's economy shrank an annualised 28.1% in the April-June period as businesses scaled back investment in the face of uncertainty and personal consumption declined due to covid-19 restrictions.

Board members are mostly of the view that the economy bottomed out in the second quarter but BOJ economists are watching activity in the non-manufacturing sector, mainly in the hospitality industry, which has taken the hardest hit from the coronavirus, for its impact on the broader economy.

LOWER PRICES

A weaker growth forecast would allow the board to consider lowering the median inflation forecast from July's -0.4%. The bank already expects the key inflation rate to be negative for the time being.

The nationwide core CPI, excluding perishables, fell 0.4% y/y in August for the first drop in three months after being unchanged in July and June. August's decline was the lowest since May 2013 when it also fell 0.4%.

The board largely judges that lending facilities are producing the intended effect, but policymakers are keeping a close eye on financing developments among non-manufacturing companies.

Businesses seem to have ensured enough liquidity beyond this year although bank officials are vigilant about solvency issues amid poor profits and sales at some businesses.

The BOJ has prioritised facilitating corporate financing and maintaining the stability of financial markets to avoid a negative feedback loop.

The bank's focus has shifted to the pace of recovery in 2021 as economic activity, including private spending, will continue to be strongly influenced by developments related to the Covid-19 pandemic.

Analysts' Key Comments

Barclays:

We expect the BoJ to reach a majority decision to retain current monetary policy, as at the last meeting. As monetary policy becomes increasingly subordinate to fiscal policy through the effective monetization of government debt amid large-scale fiscal expansion, we look for the BoJ to monitor the cumulative effects of easing measures taken to date and maintain a wait-and-see stance in the near term, albeit with a bias toward easing.

- Separately, we believe the BoJ is likely to extend its Special Funds Supplying Operations to Facilitate Financing in Response to the Novel Coronavirus (scheduled to end in March 2021) at its December MPM.
- In the quarterly Outlook Report, we expect the Policy Board to lower its FY20 core CPI inflation forecasts to reflect the downward impact of the government's Go to Travel campaign (-0.3pp, in our estimates), but believe it will likely keep its basic assessment of the economy and prices unchanged.

BNP Paribas

We expect the Bank of Japan to extend the pandemic relief currently due to expire on 31 March 2021, with an announcement possible at its October meeting.

- We do not expect the committee to discuss further easing, despite inflation continuing to miss the 2% inflation target.
- We expect the BOJ to continue to conduct policy with an eye on the exchange rate, but do not expect any move to a deeper sub-zero interest rate unless the yen strengthens to around Y95 in USD terms.

Goldman Sachs:

We expect the BOJ to maintain 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 in response to COVID-19.

- In the US, the Fed revised its forward guidance at the September FOMC meeting, bringing it in line with its newly-adopted average inflation target (introduced in late August). The ECB is also working on a "strategy review" of its monetary policy. However, Governor Kuroda reportedly mentioned recently that the BOJ has no intention of revising its inflation target and forward guidance at this juncture.
- The BOJ's Quarterly Outlook Report is due to be released at the October MPM. We expect the BOJ to lower its growth and inflation outlooks for FY2020 by around 0.2 pp each, likely citing sluggish consumption in the summer months due to the COVID-19 resurgence for the growth downgrade, and the Go To Travel campaign (government program subsidizing travel costs) for the inflation downgrade. That said, we expect the BOJ to maintain its baseline scenario of recovery from 2H2020 onward, while emphasizing downside risk, as it has done to date. We also expect the BOJ to broadly maintain its FY2021/2022 outlooks for both growth and inflation..

ING:

No change is expected in the BoJ's policy settings, with the BoJ like many concerned that the recovery will be very weak and pledging to keep financial conditions very accommodative.

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J.P.Morgan:

We expect the BoJ to stay on hold. The BoJ still seems to be concentrating on helping firms to overcome funding difficulties and stabilizing the markets to avoid crisis situations. Having said that, the funding difficulties of firms under COVID-19 have almost peaked out, although conditions have not turned to normalization yet.

- The BoJ's special funding operations and purchases of CPs and CBs will expire at the end of next March, but the discussion of whether the expiration date should be extended seems unlikely to be the topic of this MPM. The timing of this discussion likely will be either the December MPM or the January MPM because the BoJ probably wants to know in advance about the additional economic package which we expect the government will announce to compile at the end of October and the December BoJ Tankan survey in the middle of December.
- The BoJ is closely paying attention to the output gap and inflation expectations to avoid further declines in them in order to achieve the inflation target in the future.
- The BoJ may revise down slightly the growth outlook for FY2020 by taking into account the slower recovery of consumption in the summer than in its original projection; on the other hand, we revised up our own outlook today. However, this potential revision by the BoJ would have no implication for its policy. Since the Japanese economy has already strengthened its pace of recovery despite lagging other DMs, and the BoJ likely will project economic growth to attain a relatively high positive number in FY2021, we don't expect the BoJ to judge further easing necessary to support the growth further at this MPM.
- On the other hand, the BoJ likely will revise down slightly the inflation outlook for FY2020 by taking into account the unexpectedly large impact of the government's subsidy to travel expenses, but likely will judge that there is no change in firms' pricing behavior, differing from the past deflation period, and that the core CPI (ex. fresh food) will return to positive growth in FY2021. The background behind this optimistic view is that the BoJ's output gap is shallower in the negative area than the government's estimation, and the BoJ likely will think it will be easier for the gap to return to a positive level than we do. Furthermore, the BoJ also said officially that its inflation overshooting commitment adopted in 2016 is in the same spirit as the Fed adopting flexible average inflation targeting and strengthening the rate-path forward guidance, so it has little incentive to change its strategy based on inspiration from the other central banks' new policy frameworks for the time being.
- When the impact of COVID-19 subsides, the BoJ will need to change its yield-path forward guidance which is currently linked just to COVID-19 conditions. However, this MPM seems unlikely to be the time to discuss this issue.

Scotiabank:

The policy balance rate is expected to hold at -0.1%, the 10 year JGB target is likely to remain 'around' 0% defined roughly as +/-20bps around this target and purchase programs are expected to remain unchanged. Fresh forecasts will be offered and might face downside risk as global COVID-19 cases trend higher again. Jawboning policy options is expected to accompany the forecasts.

Societe Generale:

We expect the BoJ policy board to maintain the current easing framework.

- With economic activity within Japan remaining resilient and signs of an economic crisis remaining low, we also do not expect any changes to the bank's special programmes implemented in response to COVID-19. With no major change on the economic front, we expect the BoJ to maintain its easing bias and continue to emphasise its stance that "the Bank will closely monitor the impact of COVID-19 for the time being and will not hesitate to take additional easing measures if necessary."
- Economic fundamentals have remained resilient despite the COVID-19 impact lasting longer than we had anticipated at the onset of the pandemic. At the September policy meeting, the bank revised up its overall economic assessment, from the economy being in an "extremely severe situation" to the economy "has started to pick up with economic activity resuming gradually". It also revised up its export and industrial production assessment, and simultaneously revised up its assessment of overseas economies as having "started to pick up from a state of significant depression". With the patient count not increasing significantly, the need for the government to reintroduce draconian containment measures continues to remain low. At the same time, the government's programmes to stimulate economic activity, including subsidies for tourism and eating out, seem to be having their intended effects. The economic data continues to point to an improvement in the economy, with further signs of strength since the September meeting. As a result, the downside risk to economic activity further weakening under the current state of COVID has likely decreased further.
- We expect no major changes to the economic and risk assessment nor the outlook in light of the continuing strengthen in the economic data. The GDP and CPI forecasts could be slightly revised down given the continuing delay in the rebound in public investment and the technical headwinds to prices coming from government policies to stimulate economic activity. However, the underlying belief among the BoJ policy board members regarding the direction of the economy has likely not changed. The consensus view is that the economy has avoided a L-shaped recovery and that fiscal policy holds the key to whether a V-shape recovery will materialise.
- More than a month has passed since PM Suga came to power, succeeding the seven-year administration under PM Abe. The new government's message continues to be that it supports the Abenomics framework of easy fiscal and monetary policy to revive inflation and sustainable reaccelerate growth. Meanwhile, since PM Abe's resignation, Governor Kuroda has continued to emphasise that the BoJ is committed to keeping its side of the joint commitment to achieve the 2% inflation target, as stated in the joint policy statement in 2013. With Governor Kuroda's term lasting until April 2023, and all members of the policy board supporting the current policy objective and direction, the hurdle to change the composition of the policy board to create a new majority to alter the current policy framework remains very high. Thus, we continue to believe the likelihood that the current policy direction will change anytime soon remains low.
- However, with central banks around the world continuing to indicate they will remain accommodative for longer, the hurdle for the BoJ to adjust its easing policies has likely risen.

TD Securities:

The BOJ should be keep its main policy tools unchanged and downgrade its inflation forecast. With another wave of COVID cases surging across the world, the BOJ is likely to express a more cautious tone since its last meeting. The build in corporate profits prior to the pandemic is now eroding rather precipitously, which could prompt new avenues of BOJ support down the line.