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All Signal, No Noise

MARKET ANALYSIS

MNI BOJ Preview - September 2020

Meeting Date: Wednesday September 16 - Thursday September 17 2020

Statement Release Time: N/a

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

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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	↓	0.4	↓					-1.11
Tokyo CPI - Ex Fresh Food	% y/y	-0.3	0.2	↓	0.5	↓					-1.69
PPI	% y/y	-0.5	-2.8	↑	0.7	↓					0.22
Inflation Swap 5y5y	%	-0.19	-0.23	↑	-0.10	↓					-0.26
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	8.7	-9.8	↑	1.9	↑					2.57
Tertiary Industry Index	% m/m	-0.5	-8.0	↑	0.3	↓					0.08
Core Machinery Oders	% m/m	6.3	-12.0	↑	2.9	↑					1.21
Exports	% y/y	-19.2	-21.9	↑	-2.6	↓					-0.42
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	8.6	5.1	↑	3.0	↑					2.81
Bank Lending	% y/y	6.7	4.8	↑	2.1	↑					1.21
Loans Outstanding (Bus)	% y/y	8.70	5.08	↑	2.21	↑					1.21
Housing Starts	% y/y	-11.4	-12.9	↑	-10.1	↓					-0.23
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	-2.9	-13.9	↑	-0.4	↓					-0.41
Household Spending	% y/y	-7.6	-11.1	↑	-3.9	↓					-0.23
Unemployment Rate	%	2.9	2.6	↑	2.4	↑					1.21
Ave Monthly Cash Earnings	% y/y	-1.3	-0.7	↓	1.0	↓					-0.59
Markets		**Current**	**3m ago**	**3m Chg**	**6m ago**	**6m Chg**	**2Y History**	**Hit / Miss**	**Vs Trend**	**Surprise Index**	**Z-Score**
Nikkei 225	Index	23140	21878	↑	21143	↑					1.10
Japanese 10-Year Yield	%	0.05	0.01	↑	-0.15	↑					1.00
Japan Yield Curve (2s-10s)	bps	15.9	15.6	↑	9.5	↑					0.71
JPY TWI	Index	115.41	117.94	↓	118.02	↓					-1.57

Source: MNI, Bloomberg

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MNI POV (Point Of View): That'll Do, For Now

With Japanese Chief Cabinet Secretary Suga's role as outgoing Japanese Prime Minister Abe's successor confirmed this should be a fairly straight forward Bank of Japan (BOJ) decision. Suga is the definition of a continuation candidate and has already confirmed that he will not be pulling back on the arrows fired under the Abenomics program.

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."

It should also leave its broader monetary policy settings unchanged.

Still, expect the traditional dovish dissent from Kataoka, who favours more aggressive easing.

The economic assessment that the Bank provides should be a little more upbeat, given that the worst-case scenario has seemingly been averted, at least for now. However, the coming months will be the real test for the strength of the economic rebound, with particular focus set to fall on the Bank's quarterly Tankan survey.

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. 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 JPY strength.

MNI PREVIEW: BOJ Set To Hold; Pace Of Recovery A Concern

By Hiroshi Inoue

TOKYO (MNI) - The Bank of Japan is set to stand pat on monetary policy at the September meeting, as the domestic economy is seen recovering moderately after the record contraction in Q2, although policymakers will highlight downside risks amid signs the bounce back may be slower than expected.

The BOJ will use the 2-day meeting, which ends Sept 17, to examine the transmission of current policy and how its impacting both the pace of the recovery and the outlook amid lingering concerns over the Covid-19 pandemic.

Policymakers will likely underline their view that exports and industrial production are on the comeback and will likely remain solid in Q3. They will also point to the strength of private spending in recent months, underpinned by pent-up demand and the government's cash distribution, although they could warn that spending is seen losing momentum.

The board will look at whether there will be a need to lower its forecasts for full-year growth in the October outlook update on the back of the risks it sees, lowering it from the 4.7% contraction it forecast in the July report.

--TANKAN SURVEY

There is a slew of data that the Bank will have at its disposal between now and the October meeting, including the September Tankan business survey and the outcome of the quarterly BOJ branch managers' meeting.

Although much economic activity has resumed for both firms and households, the overhanging Covid concerns and self-imposed social distancing are still acting as a drag on the recovery, but the BOJ is still basing assumptions on the basis of no full-scale return of the virus and the impact on the economy.

The BOJ decision comes the day after the Federal Reserve policy decision. Although officials at the BOJ expect the Fed to move to strengthen forward guidance in coming months, they don't expect the move to come at the September meeting, as they see the current 'lower for longer' message as well understood by financial markets.

BOJ officials don't expect the Fed's policy decisions this month to fuel a rapid rise for the yen over coming weeks.

Analysts' Key Comments

Barclays:

We see the BoJ sticking to QE and YCC amid fiscal expansion and continuing to support corporate finance through measures that offset the side effects of NIRP (effectively subsidizing the banks by increasing the basic balance of their BoJ current accounts, which pays positive interest, in accordance with new lending).

Daiwa:

We expect the central bank to maintain the status quo for its monetary policy as data for Jun-Aug released since the last meeting confirmed recovery trends after reopening the economy, which has provided some stability for financial markets.

- In its statement, we expect the central bank will upgrade its economic assessments for overall conditions, overseas economies, exports, and production by adding the expression "picking up". Data for Jul-Aug showed a lull for momentum compared to the data for June. However, recoveries will likely continue from September provided progress toward containing the virus is sustained. As such, the BOJ can retain its economic recovery scenario for the second half of the year. The period from Jul-Sep to Oct-Dec will likely remain a key period for ascertaining the degree to which economic activity is recovering.

Goldman Sachs:

We expect the BOJ to maintain the status quo across all monetary policy parameters, including short- and long-term policy rates, asset purchase programs (JGBs, ETFs, etc.), and corporate finance support programs introduced in March and subsequently enhanced in response to COVID-19.

- Corporate borrowing is still heightened, which has been filled especially by the government's financial support program. Under this program, the government provides companies with not only the interest payable on loans but also assurances from credit guarantee associations, while the BOJ provides free liquidity to financial institutions, which actually extend loans to companies. In order to prevent corporate failures as much as possible, we think that the BOJ will focus on keeping implementing this finance support as smoothly as possible, while scrutinizing the effect.
- Meanwhile, market interest is likely to focus on monetary policy under a new administration after Prime Minister Shinzo Abe steps down. Mr. Suga has said that he will basically maintain the course of Abenomics, centered on the combination of active deployment of fiscal stimulus and large-scale monetary easing (September 3, Nikkei). Mr. Suga also reportedly has confidence in BOJ Governor Haruhiko Kuroda's policy moves (September 6, Nikkei). The current monetary policy framework will thus likely be maintained, in ongoing efforts to achieve the 2% inflation target.
- At the same time, Mr. Suga has stated that he would want to see monetary easing expanded if it is deemed necessary to maintain jobs and ensure the continuity of companies (September 3, Nikkei). Mr. Suga is known for his strong awareness of the forex rate, having in the past said that forex is an important subject for him in terms of crisis management, and aims to create an environment in which Japanese exporters can continue to operate in Japan (December 27, 2016, Nikkei). Therefore, we cannot rule out the possibility that Mr. Suga could encourage the BOJ to ease further, if the yen appreciates significantly.

HSBC:

We expect the Bank of Japan (BoJ) to leave its policy setting unchanged, with its policy balance rate at -0.10% and 10y Japanese Government Bond (JGB) yield target at "around" 0.00% +/- 20bps. The Bank's broad-based monetary easing options are limited as the current negative rate regime is non-binding constraints for many commercial banks and limits the pass- through effect of a rate cut. As such, the focus is on the Bank's open market operations to support financial markets, with the Bank's balance sheet continuing to expand. Indeed, the BoJ's assets were up JPY110.2trn y-o-y in August, at a much faster rate than an average JPY70.8trn in Q2 20 and JPY30.6trn in Q1 20. This is mainly driven by short-tenor operations of T-bill purchases and loan provisions, while the JGB purchase pace remains largely unchanged.

ING:

For the central bank with the longest history of unorthodox policies, doing yet more of the same seems a particularly pointless exercise, even if other central banks (Federal Reserve, European Central Bank) seem determined to do so with tweaks to their inflation targets under the guise of strategic reviews. Japan has already raised its inflation target once before, in 2013 (up from 1% to 2%). The result of which was that the BoJ simply missed its target by an even wider margin each month.

J.P.Morgan:

We expect the BoJ will continue the wait-and-see stance. The amount of special operations to facilitate the COVID-19 financing jumped at the end of August, which exceeded the amounts for special operations in June and July, suggesting that the funding needs of firms remain under the slow recovery from the COVID-19 crisis. This strong demand for the funding still warrants monitoring, and at this MPM, the BoJ likely will stay in emergency mode.

- Beyond such lingering conditions of funding, the Japanese economy is on a recovery trend, and the BoJ likely will revise up its current assessment of the Japanese economy. But the Bank likely will not change its overall outlook, and see both upside risk for manufacturing and downside risk for services. On the other hand, inflation is subdued and the August BoJ core CPI (ex. fresh food & energy, consumption tax hike & free education), to be published after this MPM, likely will become negative on a year-on-year basis, for the first time since March 2017. But the BoJ expects the current weak CPI growth to continue only within this year, and likely will continue to think it is hard to push inflation from the monetary policy side as long as social distancing continues, so that the current weakness of CPI growth would not directly induce the heated discussion of BoJ action this time.
- Rather, when the BoJ projects growth and inflation until 2022 in the Outlook Report, we expect it will seriously discuss the economic and inflation outlook and its appropriate policy response by checking the strength of capex of firms, their pricing behavior, and their inflation expectations from the BoJ Tankan survey (the next one will be published on October 1). Under the limited room for further easing, we maintain our view that the BoJ eventually will be forced to strengthen its rate-path forward guidance, which is currently linked only to the COVID-19 situation, by linking to the inflation outcome in October at the earliest, or next January. We can guess the BoJ, before taking actions, wants to see the impact of the Fed's new action of adopting flexible average inflation targeting and expected related action. Only if the yen appreciates rapidly and persistently reflecting the expected reduction of the real yield differential, could the BoJ think of cutting the short-term policy rate, which should be a risk scenario, not a main scenario, after this MPM.
- Suga already said he will maintain the current relationship with the BoJ.
- In the future, the BoJ may start the review of monetary policy during the COVID-19 era, possibly in 2021. Deputy Governor Wakatabe said that although the BoJ had already made a comprehensive assessment in September 2016 (and adopted an inflation makeup policy with an inflation overshooting commitment like the Fed's current policy framework and the yield curve control), the BoJ deems it necessary to give further consideration to what kind of monetary policy should be applied in the COVID-19 era while referring to the discussions of other central banks.

Mizuho:

There are reports the Bank may upgrade its economic forecast, probably because economic activity is gradually pulling out of its pandemic-triggered contraction. Meanwhile, the Bank's coronavirus funding operations and the higher ceiling on its purchases of corporate bonds and commercial paper are set to continue until March 2021, and we expect it will remain in "crisis mode" at least until next spring. We project policy will be left on hold at the upcoming meeting. We do not expect Board members to begin seriously discussing an early exit from crisis mode, and at the same time we see little reason for the BOJ to extend these programs or increase their size so soon. Governor Kuroda's press conference is therefore unlikely to contain any market-moving information.

Scotiabank:

The BoJ's monetary policy stance will stay highly growth-supportive for an extended period of time, yet we do not expect any changes to be announced at the policy meeting. The BoJ maintains a dovish bias and stands ready to support the economy further if needed; it has pointed out that it expects short- and long-term policy interest rates to remain at their present or lower level for the time being.

Societe Generale:

We expect the BoJ policy board to maintain the current easing framework. The board will likely decide to continue to apply a negative interest rate of -0.1% to part of the current account balance and to maintain the long-term (10yr) JGB yield target at around 0.0%. We also expect the asset purchase programme framework to remain unchanged, with the BoJ ready to buy an unlimited amount of JGBs if necessary. The BoJ will likely maintain its easing bias and continue to emphasise the 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."

- PM Abe's resignation has kindled speculation about whether the current easing framework will change under the new prime minister. However, we think that the BoJ and government's commitment to achieve the 2% inflation target, as stated in the joint policy statement in 2013, has not changed. Governor Kuroda's term lasts until April 2023. Thus, PM Abe's successor will not be able to change the leadership of the BoJ for some time. Furthermore, all the current policy board members have indicated their support for the current easing framework. The next government would therefore face a considerable hurdle if it wanted to change the composition of the policy board to create the majority needed to alter the current policy framework. Thus, we think that PM Abe's resignation will not have any material impact on the BoJ's commitment or on the direction of its easing policies over the near term.
- The positive effects of the series of economic support programmes implemented by the government and BoJ to cushion the effects of COVID-19 remain strong. Japan's credit cycle is still on an upswing, as confirmed by the July BoJ Tankan survey. The capex cycle likewise, with private non-residential investment as a percentage of GDP remaining above 16% in the latest GDP reading. The labour market also remains resilient with the unemployment rate still below 3% and signs emerging of job seekers returning to the labour force. Thus, for the moment, an L-shaped recovery appears to have been avoided. In light of such evidence, we think the BoJ policy board will maintain the view that policymakers have done enough for now and that it should monitor the effects of the policies implemented so far before taking any further action. We expect no major change to the BoJ's economic assessment or outlook at the September policy meeting.
- It is also still our view that the economic fundamentals remain resilient despite the impact of COVID19 lasting longer than we had anticipated at the onset of the pandemic. The BoJ is likely to consider that the need for additional easing or support has not risen over the past few months. However, the BoJ policy statement and subsequent statements by policy board members are likely to underline that the bank is carefully monitoring the situation and ready to act with further easing if deemed necessary to dispel any fears that could form in market. With data continuing to indicate that an L-shaped recovery has been avoided, the likelihood remains strong that a U- or V-shaped recovery will materialise rapidly once the COVID-19 situation calms down.

TD Securities:

BoJ continues to implement its current array of policy measures but is unlikely to add to them. Pressure has arguably lessened, with Q3 activity picking up and a second wave of virus cases receding. As such, BoJ is likely to upgrade its economic assessment, albeit modestly, while continuing to highlight downside risks.