

## MARKET ANALYSIS: What Does Abe's Resignation Mean for Markets?

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Figure 1: 3m Implied JPY Vols Well Contained Despite Political Uncertainty



### Policy continuity not under threat, BoJ to remain supportive

Under Abe's tenure, Japan's economic recovery has been defined by his flagship 'Abenomics' policy, with the mix of monetary easing, government spending and structural reforms generally helping bolster the country's recovery from the Global Financial Crisis. While long-lasting sustainable inflation has remained elusive, the policy has succeeded in keeping the JPY weak, Japanese equity markets bid and government bond yields persistently low.

The (relatively) sanguine response to Abe's resignation so far is an indication that markets expect Abe's successor to retain the key tenets of his economic policies. Another supportive factor for policy continuity is that the most influential 'arrow' of Abenomics will not change: Kuroda's term at the Bank of Japan isn't due to end until April 2023, which should continue to lend support to the JPY remaining weaker for longer.

Market prices corroborate with this theory. JPY implied vols added a very small premium on the news this morning, but all front-end prices remain contained (particularly when compared to the levels seen during the Coronavirus crisis). While Japanese equities did pull lower on the news (the Nikkei 225 shed just over 300 points into the close) a resumption of JPY weakness should prove supportive of the index, with source reports already this morning suggesting there will be no change in BoJ policy as a result of Abe's departure.

This keeps the medium-term outlook for the JPY unchanged. The biggest risks to Japan remain exogenous, with the US Presidential election, global trade tensions and Coronavirus the key factors for Japanese asset prices going forward.

**Candidates for Abe's Succession:**

Name (Age)	Political Positions Held	Notable Policy Stances	Chances Of Becoming PM?
<b>Tarō Asō (79)</b>	Deputy PM & Finance Minister (since 2012), Prime Minister (Sep 2008-Sep 2009), Minister for Foreign Affairs (2005-2007)	Continuity candidate, and likely only a caretaker PM. Seen as an experienced foreign policy operator. Was PM when the LDP was ousted from gov't for the first time in 15 years in 2009.	Moderate. Should Abe's resignation be viewed as a destabilising moment for Japan amidst the COVID-19 pandemic, Asō would be the best placed candidate to act as a caretaker PM until the time allows for a full leadership contest.
<b>Shigeru Ishiba (63)</b>	Minister for Overcoming Population Decline and Vitalizing Local Economy (2014-16), Secretary General of LDP (2012-14)	The most prominent Abe critic in the LDP. Wants an end to ultralow interest rates, combined with significant increases in public spending on infrastructure and public works. Not strongly committed to Abe's proposed constitutional changes. Takes a similar stance to Abe on relations with China.	One of the two frontrunners. In a direct contrast to Kishida, Ishiba is popular publicly, coming first in a Kyodo poll of preferred next prime ministers in late August, but does not carry the support of a large section of LDP lawmakers.
<b>Fumio Kishida (63)</b>	Minister for Foreign Affairs (2012-17)	Seen as a foreign policy dove compared to Abe. Not so supportive of proposed change to Japan's pacifist constitution that would allow the country to go to war (the change was one of Abe's top priorities in office). Has said easy mon pol at BoJ 'cannot go on forever'.	One of the two frontrunners. Seen as Abe's favoured pick and is popular among LDP lawmakers. However, is not popular publicly, coming fifth in a Kyodo opinion poll in late August with just 2.8% support.
<b>Shinjiro Koizumi (39)</b>	Minister of the Environment (since 2019)	Seen as allied with Abe on conservative social views, having paid respect at the controversial Yasukuni Shrine to Japan's war dead earlier in August. Has sought to present a progressive image in his time as Environment minister, encouraging Japan to cut back on its coal use.	Low. While Koizumi is viewed as a rising star within the LDP and publicly (third most popular candidate in August Kyodo poll) and likely to go onto high office, at present he is not believed to have the support level within the party to win the top job this time around.
<b>Tarō Kōno (57)</b>	Minister of Defence (since 2019), Minister of Foreign Affairs (2017-19), Chair of National Public Safety Commission (2015-16)	Supporter of Japan joining 'Five Eyes' intelligence network with US, UK, Canada, Australia and New Zealand, and therefore seen as a strong proponent of united front in putting pressure on China. Has previously urged BoJ to set out plans for end to ultra-east mon pol. Instead, is more supportive of fiscal austerity; earlier in 2020 he cancelled plans for a new missile defence system from the US, saying the cost of implementation was too high. Social conservative who has engaged in spats with South Korean gov't over wartime history.	Low-to-moderate. Relatively popular publicly (4th most preferred candidate in August Kyodo poll), but lacking support within the LDP due to his strongly anti-nuclear power stance and support for allowing sons of female royals, or female royals themselves, to ascend to the Japanese Chrysanthemum Throne.

<p><b>Toshimitsu Motegi (64)</b></p>	<p>Minister for Foreign Affairs (since 2019), Minister of Economy, Trade and Industry (2012-14)</p>	<p>Acting chief of the Takeshita faction within the LDP. The faction has previously sought to back rivals to Abe when he has faced internal party votes. However, Motegi is seen as a strong backer of Abe and a solid foreign policy presence supportive of continued close relations with the US. Is said to have softened his notoriously hard-shelled personality in the run up to a potential bid to be PM.</p>	<p>Low. Does not even have the full backing of his own faction within the LDP so if he were to run, would be seen as a very long shot.</p>
<p><b>Seiko Noda (59)</b></p>	<p>Minister of Internal Affairs and Communications (2017-19)</p>	<p>Critic of Abe within the LDP, Noda publicly spoke out against Abe's defence bills in 2015. Also a strong opponent of Abe's proposed constitutional changes, and would likely chart a less combative foreign policy course with China and could shy away from an ever-closer relationship with the US.</p>	<p>Low. While Noda could make waves in attempting to become Japan's first female PM, she is not viewed as having requisite backing within the LDP to make it far in any contest.</p>
<p><b>Yoshihide Suga (71)</b></p>	<p>Chief Cabinet Secretary (since 2012), Minister for Internal Affairs and Communications (2006-07)</p>	<p>Continuity candidate. Suga has served as one of Abe's closest lieutenants during both of his terms in office. Supportive of devolution of powers to local gov'ts. Damaged by scandals in Oct 2019 that claimed the positions of Justice Min Katsuyuki Kawai and Economy, Trade and Industry Min Isshu Sugawara, both of whom Suga was close to.</p>	<p>Moderate. Suga would be seen as a relatively safe pair of hands, and is seen to have the backing of LDP Secretary-General Toshihiro Nikai who said "He has great capabilities [and] the ability to endure in the post."</p>

### Summary of Analyst Views:

- Most analysts see Abe's resignation as transitory, with his successor likely to retain and continues the key tenets of his Abenomics economic policy.
- A minority of analysts see near-term uncertainty as markets question the longevity of Abe's flagship Abenomics programme under a new PM. However, all of those surveyed see this risk aversion being faded over time.
- As a result, while there will be near-term uncertainty, the trajectory of the Japanese economy should be unaffected by handover, with the Bank of Japan seen supporting throughout.

### Analyst Views

#### Citi FX

- Don't see Abe's resignation as changing fundamentals as the BoJ is the one taking care of monetary policy and we are unlikely to see any immediate changes. As such, they still look for a Y105 - 107 range in USD/JPY.

#### CLSA

- Sees whoever replaces Abe as having very similar policies and strategies. They see markets as likely uncomfortable with the uncertainty, but the succession is likely to allow few tweaks to policy that were probably in the works anyway.

**JP Morgan**

- Ahead of Abe's resignation, JPMorgan wrote that a double-whammy of Abe resigning and US President Trump losing the election in November could be enough to pressure USD/JPY to Y100.
- They add that the broad outlines of Abenomics would be unlikely to change under a successor, meaning a risk-aversion rally could fade.

**Mizuho Securities**

- Sees Abe's resignation as meaning the probability is rising for an end to Abenomics. Abenomics, together with the BoJ's aggressive policy, had kept the JPY weak and as such Abe's resignation has led to JPY buying and some risk aversion.
- Mizuho see the key as whether BoJ policy changes in any material way, but adds that the knee jerk response is likely to be short-lived as other factors including Coronavirus, Sino-US tensions and the Presidential election take precedent.

**MUFG**

- Writes that they see it as difficult to think the BoJ will make a reversal in policy just because Abe steps down, adding that the bigger risk likely comes after BoJ governor Kuroda's term ends in April 2023.

**Nordea**

- They write that Japan likes continuity, which means that whoever replaces him will continue more or less in the same direction. They write there are questions on whether a successor will shake up the status quo to the same extent as Abe, who was quite unique in that respect.
- Sees short-term uncertainty as likely temporary, with the open question on policy choices taken over the coming few months.

**Sumitomo Mitsui**

- Sees JPY gains as limited as markets expect that Japan's current fiscal and monetary stimulus policies will be maintained amid the Coronavirus crisis no matter who is the successor.

**MNI POLICY****BOJ On Watch For Market Reaction To Abe News**

The Bank of Japan will keep a watchful eye on financial markets in coming hours and days, if, as media reports suggest, Japan's Prime Minister Shinzo Abe announces his intended resignation later Friday on health grounds.

The Nikkei stock index fell and the yen strengthened in knee-jerk reactions immediately after the local media reports circulated, before reversing some of the move

Abe will hold a news conference at 1700 JST (0800 GMT) on Friday, with speculation mounting for days that he will resign for health reasons. His resignation could give the impression to markets that Abenomics -- aggressive monetary easing, flexible fiscal policy and growth strategy -- could take a temporary back seat.

One question further for financial markets is whether an Abe resignation results in the resignation of the BOJ Governor Haruhiko Kuroda, as the governor was appointed and reconfirmed by the PM, who has been fully supportive of the central bank's policies.

There are fears inside the BOJ that Kuroda stepping down could trigger market speculation that the central banks will abandon its 2% price target, strengthen the yen and see lower stock prices as growing uncertainties would trigger investors' risk-off attitude temporarily.

Whoever become the prime minister, the government will unlikely change the policy of supporting the economy and employment as the coronavirus hangs around.

The BOJ has said that the momentum toward achieving the 2% price target is lost temporarily due to the coronavirus pandemic but is unlikely to abandon the price target as such a move will strengthen the yen.

The BOJ will continue to make efforts to maintain the stability of financial system in order to avoid Japan from falling into deflation.

BOJ officials are heartened by the lack of the yen's rise following the U.S. Federal Reserve's decision of allowing inflation to overshoot 2% moderately "for some time" to compensate for below-target periods, but they will keep a close eye on a yen.

BOJ Governor Kuroda may make a comment in response to the Abe press conference later Friday.