

Macro + FX Strategy

Japan BOJ Apr 2019 MPM: No Change To Policy Rate But Adjusts Forward Guidance & Lowers GDP, CPI Forecasts

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- BOJ tweaked its monetary policy via a clarification of its forward guidance that it “*intends to maintain the current extremely low levels of short- and long-term interest rates for an extended period of time, **at least through around spring 2020...***” while Yield Curve Control and other monetary policy measures remain unchanged.
- BOJ’s projected GDP growth rate in fiscal 2018 was again revised lower to 0.6% (from 0.9% made in Jan 2019), growth forecasts were revised slightly lower for fiscal 2019 and fiscal 2020. Growth for fiscal 2021 is at 1.2%, highest in three years.
- The BOJ CPI inflation point estimates are unchanged in fiscal 2019 while the forecast range was adjusted slightly lower. BOJ trimmed the forecasts for fiscal 2020 lower slightly too. The effects of the consumption tax hike is assumed to be “flushed out” by the subsequent year with CPI inflation that excludes fresh food and CPI that excludes consumption tax hike, both to be at 1.6% in fiscal 2021, still below the 2% target.
- We believe the gap between BOJ’s actual bond buying and the official JPY80trn target presents an opportunity to increase monetary policy easing without changing the policy targets. Assume that the Japan government follows through on its pledge to implement the next consumption tax hike in Oct 2019, that may be enough to “convince” the BOJ that the government is keeping its pledge to fiscal discipline and restore Japan’s fiscal balance at some point in the future. Based on the current projection, the BOJ is buying JGBs at an annual pace of JPY31.1trn (as of 20 Apr 2019) well below the promised pace of JPY80trn. This means that the BOJ may “allow” the Ministry of Finance to issue more debt (JGBs) which the BOJ in turn will buy so as to push the central bank’s JGB buying closer to the JPY80trn annual pace.
- With the dovish overtures dominating, we maintain the view that the path of least resistance is for gradual weakness of the JPY. As such, we reiterate our USD/JPY point forecasts at 111 in 2Q19, 112 in 3Q19 and 113 in 4Q19 and 1Q20.

BOJ Tweaks Forward Guidance To Little Effect, Downgrades GDP & CPI Forecasts Further

On 25 Apr 2019, the Bank of Japan (BOJ) **clarified its forward guidance**, as the central bank announced in its statement that it “*intends to maintain the current extremely low levels of short- and long-term interest rates for an extended period of time, **at least through around spring 2020...***” so as to dispel speculation about BOJ’s commitment to its ultra-easy monetary policy. The BOJ also pledged to implement “*measures contributing to the continuation of powerful monetary easing, including the expansion of eligible collateral for the Bank’s provision of credit.*” It was not a unanimous decision (7-2 vote) as BOJ policy board members, Goshi Kataoka and Yutaka Harada dissented for their respective reasons.

As for BOJ’s decision to maintain Yield Curve Control and other monetary policy measures unchanged from its previous decision on 15 Mar 2019, it was again not a unanimous decision (7-2 vote) with the usual suspects dissenting for the 6th consecutive meeting.

The BOJ also extended the deadline for the fund provisioning to stimulate bank lending to 30 June 2021.

The BOJ is still upbeat about economic outlook for FY 2019 through **FY2021** as the *“economy is likely to continue on an expanding trend throughout the projection period...- despite being affected by the slowdown in overseas economies for the time being” (i.e. blame is put on external factors but is seen as temporary)*. It also noted that *“Domestic demand also is likely to follow an uptrend, mainly against the background of highly accommodative financial conditions and the underpinnings through government spending, despite being affected by such factors as the scheduled consumption tax hike”* [from current 8% to 10% in Oct 2019]. Nevertheless, the BOJ’s projected GDP growth rate in fiscal 2018 was again visibly revised lower to 0.6% (from 0.9% made in Jan 2019) and growth forecasts were revised slightly lower for fiscal 2019 and fiscal 2020. Growth for fiscal 2021 is at 1.2%, highest in three years. (See table on page 4)

The BOJ was again less optimistic about prices even though it still held on to the belief that Japan’s inflation *“will likely to increase gradually toward 2 percent.”* Even as CPI inflation *“has been positive”*, the BOJ reiterated that inflation *“has continued to show relatively weak developments compared to the economic expansion and the labor market tightening.”* The BOJ blamed the weak inflation trends on *“firms’ cautious wage- and price-setting stance...firms’ moves toward raising productivity as well as the technological progress in recent years”* but it is still hopeful that eventually, companies will shift towards rising wages and prices while households will increase their tolerance for higher inflation, and *“further price rises are likely to be observed widely and then medium- to long-term inflation expectations are projected to rise gradually”*. Importantly, the BOJ again noted that risks to both economic activity and prices remains skewed to the downside, and it again highlighted that *“developments in prices continue to warrant careful attention.”* (No material change from the Jan 2019 Outlook)

The BOJ’s CPI inflation point estimates are unchanged in fiscal 2019 while the forecast range was adjusted slightly lower. BOJ trimmed the forecasts for fiscal 2020 lower slightly too. The effects of the consumption tax hike is assumed to be “flushed out” by the subsequent year with CPI inflation that excludes fresh food and CPI that excludes consumption tax hike, both to be at 1.6% in fiscal 2021, still below the 2% target.

In his post-MPM press conference, BOJ Governor Kuroda again reiterated BOJ’s commitment to achieve the 2% inflation target and it will adjust policy quickly if necessary. He explained that the reason to clarify its monetary policy stance in April MPM was to improve BOJ’s credibility, and he noted that it is fully possible that the timeframe under the BOJ forward guidance could exceed spring 2020. He added that the clarification was aimed at dismissing speculation that BOJ will hike rates after the Oct 2019 sales tax hike. And while he said that the latest BOJ FY2021/2022 CPI projections do not mean that inflation will not hit 2% during that fiscal year, Kuroda admitted that there is a low chance of inflation reaching target in FY2021. Kuroda said that the BOJ is not thinking of reviewing interest rates in spring 2020 “no matter what”.

BOJ Outlook: Is More JGB Buying Possible To Push The Pace Closer To JPY80 Trillion?

Among the G10 central banks, BOJ continues to be the least likely to normalize its easy monetary policy anytime soon, and it remains premature for the BOJ to talk about normalizing/tapering its quantitative easing program too, because Japan is still far away from its 2% inflation target (as BOJ evidently expects inflation to be at 1.6% in Fiscal 2021). The projected weaker growth environment and likelihood of downside price pressures in 2019 adds further challenges to BOJ’s monetary policy. Another nagging point of contention which has been unhelpful to BOJ’s “fight” is the fact that the projected annual pace of JGB buying has continued to be well below its official target of JPY80trn.

That said, we think the gap between BOJ’s actual bond buying and the official JPY80trn target presents an opportunity to increase monetary policy easing without changing the policy targets. Assume that the Japan government follows through on its pledge to implement the next

consumption tax hike in Oct 2019, that may be enough to “convince” the BOJ that the government is keeping its pledge to fiscal discipline and restore Japan’s fiscal balance at some point in the future. Based on the current projection, the BOJ is buying JGBs at an annual pace of JPY31.1trn (as of 20 Apr 2019) well below the promised pace of JPY80trn. This means that the BOJ may “allow” the Ministry of Finance to issue more debt (JGBs) which the BOJ in turn will buy so as to push the central bank’s JGB buying closer to the JPY80trn annual pace.

Please click on the following links to access the [24/25 April 2019 BOJ MPM statement](#) and the [BOJ April 2019 Outlook Report \(The Bank’s View\)](#).

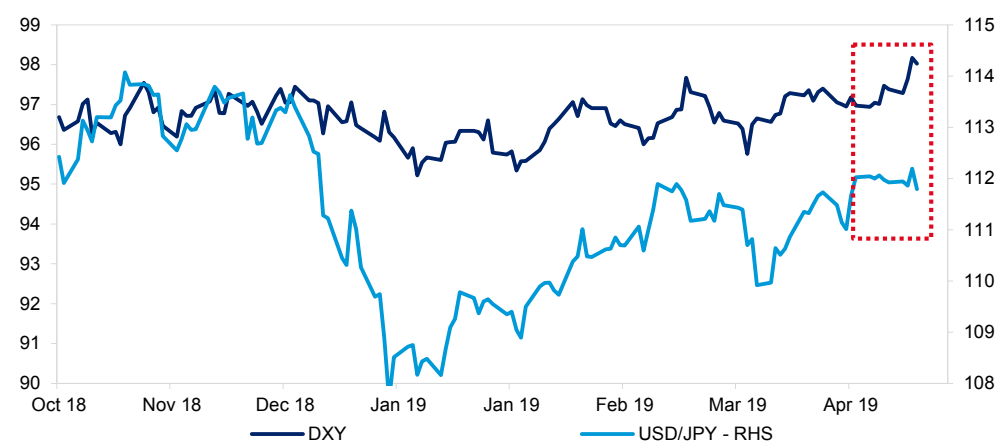
JPY Outlook: Capped At 112/USD Ahead Of Japan Holiday But On Track For Further JPY Weakness Further Out

The USD/JPY remains steady just under 112 despite a tweak in BOJ’s forward guidance earlier. Of late, the USD/JPY has been surprisingly muted given that the US dollar index DXY has rallied strongly. Since 12-Apr, USD/JPY traded only about 40 pips on either side of the 112 handle. In the same period, DXY gained from 97 to 98, near the highest level since May 2017. Concerns of a repeat of the USD/JPY’s flash crash earlier this year (3-Jan) amid thin market conditions in the upcoming 10-day Japan holiday capped the pair at 112.

Further out, we reiterate our view for gradual JPY weakness going forth as the BOJ pledged to continue with its “powerful monetary easing”. There is also a growing consensus amongst analysts (UOB included) for more monetary easing by the end of the year to maintain momentum towards BOJ’s 2% inflation target. With the dovish overtures dominating, we maintain the view that the path of least resistance is for gradual weakness of the JPY. As such, we reiterate our USD/JPY point forecasts at 111 in 2Q19, 112 in 3Q19 and 113 in 4Q19 and 1Q20.

USD/JPY Was Stable Around 112 In The Past Weeks While The DXY Soared

Source: Bloomberg, UOB Global Economics & Markets Research



Forecasts of the Majority of the BOJ Policy Board Members, April 2019								
Variable (Range)	Variable (Range)				Variable (Median, point est)			
	FY 2018	FY 2019	FY 2020	FY 2021	FY 2018	FY 2019	FY 2020	FY 2021
Change in Real GDP	0.6 - 0.6 (↓)	0.7 - 0.9 (↓)	0.8 - 1.1 (↑)	0.9 - 1.2	0.6 (↓)	0.8 (↓)	0.9 (↓)	1.2
Jan 2019 review	0.9 - 1.0 (↓)	0.7 - 1.0 (↑)	0.7 - 1.0 (↑)		0.9 (↓)	0.9 (↑)	1.0 (↑)	
October 2018 review	1.3 - 1.5 (-)	0.8 - 0.9 (↑)	0.6 - 0.9 (-)		1.4 (↓)	0.8 (-)	0.8 (-)	
July 2018 review	1.3 - 1.5 (↓)	0.7 - 0.9 (-)	0.6 - 0.9 (↓)		1.5 (↓)	0.8 (-)	0.8 (-)	
April 2018 review	1.4 - 1.7 (↑)	0.7 - 0.9 (-)	0.6 - 1.0		1.6 (↑)	0.8 (↑)	0.8	
CPI inflation (ex fresh food)	0.8	0.9 - 1.2 (↓)	1.2 - 1.5 (↓)	1.4 - 1.7	0.8 (-)	1.1 (-)	1.4 (↓)	1.6
Jan 2019 review	0.8 - 0.9 (↓)	1.0 - 1.3 (↓)	1.3 - 1.5 (↓)		0.8 (↓)	1.1 (↓)	1.5 (↓)	
October 2018 review	0.9 - 1.0 (↓)	1.5 - 1.7 (↓)	1.5 - 1.7 (↓)		0.9 (↓)	1.6 (↓)	1.6 (↓)	
July 2018 review	1.0 - 1.2 (↓)	1.8 - 2.1 (↓)	1.9 - 2.1 (↓)		1.1 (↓)	2.0 (↓)	2.1 (↓)	
April 2018 review	1.2 - 1.3 (↓)	2.0 - 2.3 (↓)	2.0 - 2.3		1.3 (↓)	2.3 (-)	2.3	
CPI (ex consumption tax hike)	0.8	0.7 - 1.0 (↓)	1.1 - 1.4 (↓)	1.4 - 1.7	0.8 (-)	0.9 (-)	1.3 (↓)	1.6
Jan 2019 review	0.8 - 0.9 (↓)	0.8 - 1.1 (↓)	1.2 - 1.4 (↓)		0.8 (↓)	0.9 (↓)	1.4 (↓)	
October 2018 review	0.9 - 1.0 (↓)	1.3 - 1.5 (↓)	1.4 - 1.6 (-)		0.9 (↓)	1.4 (↓)	1.5 (↓)	
July 2018 review	1.0 - 1.2 (↓)	1.3 - 1.6 (↓)	1.4 - 1.6 (↓)		1.1 (↓)	1.5 (↓)	1.6 (↓)	
April 2018 review	1.2 - 1.3 (↓)	1.5 - 1.8 (↓)	1.5 - 1.8		1.3 (↓)	1.8 (-)	1.8	
Source: Bank of Japan, UOB Global Economics & Markets Research (as of 25 Apr 2019)								

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