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Flash Note
10/07/2018

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Japan's monetary stimulus. A never-ending story?

BOJ's Kuroda says current easing policy to continue

- In an opening address to the BOJ branch managers meeting, Governor Haruhiko Kuroda says the current monetary policy will continue, aiming to achieve the price stability target of 2%, as long as it is necessary for maintaining that target in a stable manner.
- The governor explained with great detail objectives, which make me think that the program of stimuli will be longer than what the consensus had been estimating: "The central bank will continue expanding the monetary base until the year-on-year rate of increase in the core CPI exceeds 2% **and stays above the target in a stable manner**".
- Nevertheless the Nikkei discussed indications of a fissure among BOJ board members on the side effects of the current ultra-loose monetary policy. While some members (Kuroda among them) are increasingly concerned about adverse impacts on the banking sector, others such as Yutaka Harada or Takako Masai said that "it is appropriate to continue with strong monetary easing in a persistent and sustainable manner, while being more careful than ever when examining developments in economic activity and prices".
- Tapering not before 2H2019: The government forecasts overall consumer price growth of 1.5% in FY19. This compares to market consensus of 1.0% CPI in 2019.

Macro update: Wages accelerate but consumption struggles.

- May nominal average wages +2.1% y/y vs consensus +0.9% and revised +0.6% in prior month. Real wages +1.3% y/y vs consensus 0.0% and revised (0.2%) in prior month.
- The Sankei reported that 82.2% of companies will implement wage hikes from the spring. The report noted that the majority of firms are increasing pay to retain employees amid the tightness in the labor market, particularly among small businesses.
- On the negative side, May household spending was -3.9% y/y vs -1.3% in prior month

Fiscal: Positive dynamics, but not enough

- Ministry of Finance reported Japan's FY17 revenues rose 6.0% y/y to ¥58.788T. This marks the third highest on record and the largest in 26 years on the back of corporate earnings strength.
- Corporate tax revenues expanded 16.1% to ¥11.995T as external demand was a tailwind, boosting exporter earnings.
- Income tax revenue rose 7.2% to ¥18.882T with growth in investment income from higher dividends cited as a main driver alongside wage growth.
- Japan needs revenue increase to meet FY25 fiscal target. Cabinet Office estimates that Japan would need an extra ¥2.4T ($21.6B) in revenue to achieve a primary fiscal surplus in FY25, even under an optimistic scenario of more than 3% nominal GDP growth. The objective is to fill revenue shortfalls with taxes rather than debt issuance.

Economic Outlook: Government sees growth despite tax hike.

- The Cabinet Office estimates 1.5% GDP growth in FY19 despite an upcoming tax hike, counting on wage hikes spurred by labor shortages to drive the recovery.
- A credible projection? The forecast is faster than potential (structural) growth of 1%, and markedly more bullish than the 0.8% predicted by the Bank of Japan and private-sector think tanks.

Financial Market Outlook

- Japan's Government Pension Investment Fund's (GPIF) has exceeded its 25% allocation target for domestic stocks for the first time at the end of March, which means that GPIFs portfolio is now less likely to be a force that elevates the market as it did in the past.
- We maintain our FY2018 fundamental target price for the Nikkei225 at 23.100 (vs currently at 22.410)
- We keep stable our Dec 18 target for the 10 year government bond yield at 0%
- Target for the JPY-USD at 111.20 (vs current 110.85)

One question that I ask myself constantly is whether in Europe, once we have reached a point of extension in stimulus such that the prices of debt assets have gone beyond all manipulation -making it increasingly difficult to see a normalization-, we will continue the same monetary strategy as in Japan

Best