

Flash Note:
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Japan - A quick x-ray of the situation in the the economy & financial market.

Economy: Pressure on policymakers to do more amid slowing economy.

- The government and the BOJ will need to devise fresh ways to boost flagging economic growth. There are suggestions that policymakers may have overestimated the strength of consumer demand after department store sales and new car sales fell sharply (in part due to the recent consumption tax hike).
- No fiscal stimulus in our view: The scope for meaningful fiscal stimulus remains stymied by a large debt load and tax revenue undershooting official estimates. Although Japan's budget next fiscal year will top ¥100T (\$914B) for a second straight year, highlighting the struggle to curb government spending, expenditures will rise only about 1.2% to ¥102.7T.
- Data has been weak recently:
 - November household spending growth was -2.0%/y/y (although improved vs the -5.1% y/y seen in prior month, it is still in negative territory, and we believe it will continue so, as nominal growth in average wages grew at -0.2% y/y and real wages expanded at a negative rate of -0.9% y/y (worse than the revised -0.4% in prior month).
 - December composite PMI remained weak at 48.6 (deteriorating from the 49.8 seen in November). The fall was mainly due to the decline seen in the services PMI, which was cut from 50.3 to 49.4, **while the manufactured PMI deteriorated marginally (from 48.9 to 48.4).**

Despite weakness, the BOJ leaves policy unchanged and we have reasons to believe it will not ease further

- The BOJ voted 7-2 to leaving short term rates at -0.1% and long term rates at around 0%.
- The Bank reiterated the idea that “the Japan's economy is moderately expanding”, though exports, production and business sentiment have shown some weakness, mainly affected by the slowdown in overseas economies and natural disasters.
- Meanwhile, the Boj decided to introduce the ETF lending facility, through which it can temporarily lend its ETFs holdings to market participants, with the aim of improving the liquidity in ETF markets. The duration of the

lending will be within one year, with lending rates determined by multiple-competitive auctions or by the BoJ in advance.

- We still think that the bank will not ease further in 2020 for the following reasons:
 1. Japan's Government Pension Investment Fund, which has total assets of around ¥160trn, has been green-lighted to buy more foreign debt on an unhedged basis. This followed a rule change that reclassified foreign debt holdings that were currency-hedged as being "domestic". The effect will be to create more selling pressure on the yen, and thus, no need to ease policy to compensate for the effects of a rise in Fx.
 2. Global risk-on shift points to continued capital flows out of Japan. On balance, meaning that JPY could remain subdued (with no need for the BoJ to act and keep it low). The yen is likely to stay in the ¥105-¥115 range.
 3. While recent data has been soft; that was to be expected ahead of a recent 2pp hike in the consumption tax.
 4. Japan is set to raise GDP outlook to 1.4% growth for next fiscal year. The combination of investment spending associated with next year's summer Olympics, and some offsetting fiscal supports, suggests that Japan can weather a soft patch without suffering a fully-fledged downturn.

Finance: Stricken local banks in Japan turn to riskier credit to survive.

- 20 out of 29 Japanese regional banks said they've reduced JGB holdings. Five said they've bought foreign notes with ratings at the triple B level. This foray into riskier investments marks a dramatic shift from the past.

Foreign transactions: Japanese investors remain buyers of foreign assets during 1H December:

- Net buyers of ¥440B in foreign equities during the first half of December.
- Net buyers of ¥747B in foreign bonds during the first half of December

Andbank's Financial market outlook

- Japanese Equities – N225: UNDERWEIGHT. Target 23,732 (Exit 24,919). Currently at 23,851.
- Japanese Bonds – Govies: UNDERWEIGHT. Target yield 0.00%
- Forex – USD-JPY: MARKETWEIGHT. Mid-term target 110. Currently at 109.89

Best regards