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Daiwa's View

Blueprint of assessment stated by Deputy Gov. Amamiya

- Initial thoughts to be revised due to drastic change in global interest rate environment since Jan

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Blueprint of assessment stated by Deputy Gov. Amamiya

Ten days left before BOJ's Mar MPM

Initial thoughts on wider trading band to be revised due to drastic change in global interest rate environment since Jan

Due to difference between Japan and US, upward degree of long-term rates to differ naturally

Ten days are left before the BOJ announces the results of the policy assessment at the Monetary Policy Meeting (MPM) to be held on 18-19 March. Since the central bank announced at the MPM on 18 December 2020 that it would assess monetary easing at the March MPM, we have seen various speculative articles. During this period, the global interest rate environment has drastically changed. As the market and economy are alive, the subsequent rise in yields forced the BOJ to revise its thoughts at that time when the 10-year JGB yield was relatively stable at around 0.02%. BOJ governor Haruhiko Kuroda, responding to a question at the Diet on 5 March about the 10-year JGB yield trading band, clearly stated that he saw no need to widen it. This surprised the market, which had been assuming that a widening of that band was already a done deal ever since Jiji Press reported on 15 January that the BOJ would consider widening it. However, there are clear differences between now and mid-January in terms of both economic conditions and progress administering vaccines in Japan and the US. In addition, a $1.9tn stimulus package is expected to be signed into law soon in the US. It is therefore only natural that the degree of the rise in long-term interest rates would be different in Japan than in the US, reflecting fundamentals.

BOJ's last official communications prior to assessment was speech by Deputy Gov. Amamiya

The BOJ's last official communications prior to the assessment was Deputy Governor Masayoshi Amamiya's online speech at the Yomiuri Economics Forum (anyone can watch/listen to for free) on 8 March. The BOJ has long used this particular forum as a tool for setting its intentions. This speech was announced in the late afternoon on 26 February when the 10-year yield rose to 0.175% at one point in line with US yields. Probably the BOJ felt the need to communicate with the market, and then Mr. Amamiya's appearance at the dais appears to have been decided as the policy assessment is led by him. The contents of the speech entitled "Monetary Policy during and after the COVID-19 Era" were easy to understand. We can say that it is a blueprint of the assessment.

Three points underlie assessment

Framework will not be reviewed; nimble responses with constraints to side effects

In the speech, Mr. Amamiya explained three points that underlie the assessment—(1) it is appropriate for the BOJ to maintain accommodative financial conditions while continuing to pursue QQE with Yield Curve Control, (2) in order to carry this out, the key is to enhance the sustainability of monetary easing by minimizing the policy costs during normal times, and (3) it is important to be prepared to make nimble and effective responses when needed to counter changes in developments in economic activity and prices, as well as in financial conditions. The first point means that the framework will not be reviewed, which has been stated by the BOJ since the beginning. At the time of the announcement of the results, the central bank is likely to add analysis materials that explain that the desired effects are exhibited. In the second point, the words "policy costs" was used, but this means that the side effects will be restrained. To avoid misunderstanding that the assessment is conducted to cope with the side effects, "policy costs" appear to have been used. The third point includes a key word of the assessment—"nimble," and the explanation around the word gets to the point—"when needed" and "to be prepared to make nimble and effective responses." As this means advance preparations, the BOJ will not act soon if there is no need.

We are unlikely to see an immediate change from the next week of the announcement of the assessment results.

Fluctuations within certain range could have positive effect

Gov. Kuroda's remark on 5th caused plunge in yields; acceptable range implied cooling down excessive moves

Regarding the second point of operations to enhance the sustainability of monetary easing, he mentioned the yield curve control. He said that "it is important to strike an appropriate balance between maintaining market function and controlling interest rates. The BOJ believes that it can find more ways to achieve this balance," explaining that "although significant fluctuations in interest rates could lead to undesirable consequences, fluctuations within a certain range could have positive effects on the functioning of JGB markets without losing the effects of monetary easing." The tone is different from that of Gov. Kuroda's remark on 5 March, but we think that "a certain range" at this time is "about double the range of around plus or minus 0.1%." In the Q&A session, asked about Mr. Kuroda's remark on 5 March, Mr. Amamiya replied that it was "a personal thought." However, the governor's personal opinion would be unacceptable. As yields fell at a stroke (10-year yield fell below 0.10% at one point) in the market, he appears to have implied the acceptable range to cool down the market.

No change to recognition as of Jul 2018 and Sep 2016

Making entire yield curve stable and low kept in mind

Mr. Amamiya also said that the BOJ needed to keep three points in mind in conducting yield curve—(i) there is no change in its stance that "interest rates might move upward and downward to some extent, mainly depending on developments in economic activity and prices," which was clarified at the July 2018 MPM, (ii) there is no change in the recognition that "an excessive decline in superlong interest rates could have an impact of lowering the rates of return on insurance and pension products" at the time of Comprehensive Assessment in September 2016, either, and (iii) while the economy has been damaged by the COVID-19 pandemic, what is important now is to maintain the stability in the bond market and stabilize the entire yield curve at a low level.

Cut in short/long-term rates essential option for additional easing

ETF purchases to be revised to flexible ones via analysis of difference in effects according to market conditions

Lastly, he pointed out two examples as measures for the third point of nimble and effective responses—(1) a cut in short- and long-term interest rates and (2) purchases of ETFs and J-REITs. Regarding the first example, he pointed out that "cutting short- and long-term interest rates is one of the essential options for additional easing measures." After the announcement of the assessment, speculative articles said that there is an option to deepen negative rates as a response measure for the next crisis. However, this is the first time that the BOJ's official document clearly stated the option. In his 3 March speech, board member Goushi Kataoka said as his personal opinion that it was appropriate to lower short- and long-term interest rates. While the market views that it is difficult to lower short- and long-term interest rates, Mr. Amamiya showed the stance that such an option will be implemented appropriately when needed. As for the second example, he pointed out that "decisive purchases have had significant positive effects in terms of easing market sentiment, which had deteriorated considerably." It can be said that the BOJ showed a path to conduct flexible purchases in a prioritized manner via analysis of the difference in the effects of purchases according to market conditions.

Concrete examples pointed out by Mr. Amamiya blue print of assessment

US interest rate trends warrant attention for now

At the March assessment meeting, the BOJ is thus likely to consider accepting interest rate fluctuations within a certain range (pointed out by Deputy Gov. Amamiya as second concrete example), the option of cutting short- and long-term interest rates as an additional easing measures (third example), and reviewing ETF/J-REIT purchases to make more flexible in a prioritized manner. It would be meaningless if the BOJ's decision disrupts markets right before the fiscal year-end. The BOJ will probably make sustaining easing its main focus while working hard to create an environment that balances the upside with the downside. Nevertheless, in the near term, the market and the BOJ should monitor US interest rate trends.

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[Standard & Poor's]

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