

Daiwa's Economic View

What will happen to Takaichi's expansionary fiscal policy?

- Sudden decisions to dissolve Lower House for snap election, cut consumption tax
- Fiscal expansion is just getting started
- How to stop expansionary fiscal policy from becoming source of concern

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Concerns about Prime Minister Sanae Takaichi's expansionary fiscal policy are again growing following her sudden dissolution of the Lower House for a snap election and the promise of consumption tax cuts. Both of these decisions were made by Takaichi, reaffirming the distance between her and the ruling parties/government, as well as her strong commitment to expansionary fiscal policy. It is not easy for those around Takaichi to make course corrections.

The initial budget for FY26 was kept relatively restrained, but fiscal expansion will now begin in earnest with reduced consumption taxes on food items, crisis management investments, and growth investments.

A substantial defeat in the February Lower House election might be the only thing that could put the brakes on expansionary fiscal policy. Any subsequent approval ratings decline would also impact expansionary fiscal policy. A major milestone could be the LDP presidential election in September 2027.

Clear stance that important matters to be decided at PM's office

Concerns over the Takaichi administration's fiscal expansion had temporarily subsided with last December's initial budget compilation for FY26. Cutting spending and limiting the issuance of new financial resource bonds to under Y30tn was a positive surprise. However, concerns have since resurfaced after sudden announcements in early 2026, such as dissolving the Lower House for a snap election and consumption tax cuts.

One concern is that there appears to have been no prior coordination with the ruling parties and the government. Rather, these decisions were all made at the Prime Minister's office. Takaichi explained during the 26 January party leaders' debate that she had consulted with the ruling parties, but the truth of the matter remains unclear. However, this policy-making process, in which the prime minister decides her own policies and announces them without first consulting the ruling parties (government), as well as her strong desire for fiscal stimulus, have caused markets to become increasingly cautious.

The 19 January press conference to announce dissolving the Lower House for a snap election also included the surprise announcement that the consumption tax on food would be lowered to 0% for a period of two years. Since then, both the ruling parties and the government seem to be scrambling to contain the fallout.

◆ Consumption tax cut comments at LDP Secretary-General Suzuki's 20 Jan 2026 press conference

- I think the Prime Minister's remarks, though phrased somewhat differently, were intended to convey what was written in the policy agreement for forming a coalition with the Japan Innovation Party.
- The ruling parties have entrusted the policy agreement entirely to the party president. It's not surprising that this was included in the campaign pledges within that framework, given the change in administration.
- Funding sources will be discussed at a 'national council' to be established going forward. Originally, this was a forum for primarily discussing refundable tax credits. I believe it will be properly funded.

◆ Consumption tax cut comments at Finance Minister Katayama's 23 Jan 2026 press conference

- The Prime Minister stated that the national council to be established going forward will simply accelerate discussions of such matters as funding sources and scheduling. She has clearly stated that funding will not rely on special deficit-financing JGBs.
- The national council to be established going forward will need to examine various items, including funding sources and scheduling. For example, how will the restaurant industry be handled? Nothing has been decided yet.
- Refundable tax credits are also something we will always pursue without fail, so naturally they will come into play.
- As Finance Minister, it would be presumptuous for me to answer whether the national council's deliberations indicate that tax cuts may not be achievable due to a lack of funding. Cabinet ministers should not anticipate outcomes.

Earnest fiscal expansion to begin from mid-FY26, continue through FY27

According to Takaichi's own statements, the initial budget for FY26 was originally being compiled by the Cabinet of former Prime Minister Shigeru Ishiba. Compilation of a full-fledged budget under the Takaichi administration will begin in FY27.

During the 19 January press conference to announce dissolving the Lower House for a snap election, Takaichi cited continued crisis management investment and growth investment as key policies. However, neither of these two investments has been allocated significant funding in either the FY25 supplementary budget ([2 Dec 2025 Daiwa's Economic View: FY25 supplementary budget announcement: Key points for FY26 initial budget, JGB issuance plan](#)) or the FY26 initial budget (29 Dec 2025 [Daiwa's Economic View: FY26 budget and JGB issuance plan: Tempering Takaichi's agenda](#)). In other words, these expenditures will begin in earnest starting in FY27.

Takaichi stated on 25 January that she aims to implement the consumption tax cut starting in FY26. She also stated that if the national council's discussions are finalized during the extraordinary Diet session in autumn 2026, she will submit a tax reform bill at that time. This means fiscal expansion will begin with the FY26 supplementary budget. Of the various taxes, past examples have proven that raising the consumption tax is most strongly rejected by the public and can be postponed depending on the economy and prices.

Instead of concluding the consumption tax cuts at the end of FY28, roughly two years after the introduction, it is possible to design a system that will begin offering refundable tax credits in FY29. The government is making preparations with that intention in mind.

◆ Consumption tax cut comments in materials submitted by expert members of Council on Economic and Fiscal Policy (22 Jan 2026)

- Regarding food/beverage consumption tax cut to 0% for two years:
 - Businesses shoulder burden of system support for registers, accounting, billing systems, etc.
 - Impact on other transactions such as dining outside the home
 - Relationship with the implementation period and system design for refundable tax credits, others
 - Impacts on financial markets (yields, forex) and local government finances
 - Examination of funding sources that do not rely on special deficit-financing JGBs

The funding required for refundable tax credits would range from several hundred billion yen to just over Y2.0tn, depending on the design ([Daiwa Institute of Research \(2 Dec 2025\) "Roadmap for Implementing Refundable Tax Credits"](#)). Nevertheless, depending on economic conditions, an extension of the consumption tax cut remains a possibility.

During the 26 January party leaders' debate, Takaichi was criticized for surging long-term JGB yields due to expansionary fiscal policy. In response, she stressed that sufficient consideration of the JGB market had been given during the formulation of the initial budget for FY26. Just to reiterate, those were past measures and the market is now concerned about future measures. There is also a lack of mutual understanding.

Considering when expansionary fiscal policy will stop causing market anxiety

Finally, when will Takaichi's expansionary fiscal policy take on a more disciplined form?

The initial trigger could be the outcome of the February Lower House election. A majority of seats for the ruling parties is the de facto line determining election victory or defeat, but in reality, an outright LDP majority is probably needed to claim victory. If this outright majority cannot be realized, there could be a failure to understand why the Lower House was dissolved without holding discussions with anyone, with no preparation period, and with passage of the budget delayed during the busy New Year's period. In that case, Takaichi's position within the LDP would likely become more delicate.

Moreover, lacking a strong base within the party, overwhelming public support is essential for Takaichi to wield significant influence. As the cabinet's approval ratings decline, the fact that Takaichi has not established close ties with the ruling parties and the government will come into play.

Furthermore, since Takaichi succeeded former Prime Minister Ishiba's term, the LDP presidential election will be held in September 2027. Whether she can be re-elected will depend on her approval ratings at the time. The true key will be whether she can become the face of the LDP during the July 2028 Upper House election.

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