Japan: Just spend it

In what looks like an admission that monetary policy is out of ammunition, Japan's government is now turning back to fiscal stimulus to give the economy a boost. The size of the package, however, provides no excuse for raising our GDP forecasts, just an excuse not to slash them

Japan has smoothed the impact of the consumption tax hike

The last time the Japanese government attempted to expand the tax revenue base by increasing the consumption tax, it delivered a fiscal drag[1] to the economy of 1.9% of GDP. Japan's annual GDP in fiscal year 2014 fell to -2.6% from 2.8% the previous year.

This time, the government has put in place considerable offsetting measures to the latest consumption tax hike - cuts to pre-school education fees, free higher education, and benefits for low income pensioners for example, to soften the blow.

[1] Fiscal drag is defined as the change in the cyclically-adjusted primary balance.

Not much of a "boom" before the "bust"

Notwithstanding this, the economy is slowing. 3Q19 GDP managed 0.4% quarter-on-quarter growth – hugely disappointing given the expectation for some front-loading of expenditure. And despite the limitations of the front-loading, the decline in retail activity that has followed it suggests that a post-tax slump may be developing.

The government may in the past have turned to the Bank of Japan (BoJ) for some assistance. But with negative policy rates, zero-yield targeted 10Y Japanese government bonds, and a faltering quantitative easing programme, a generous viewpoint is that the BoJ has maxed out its policy options.

The size of the package has been exaggerated

Now, despite the persistent deficit, and the huge stock of government debt, Japan is about to unleash another fiscal stimulus programme. For those who believe that this is the global answer to weak growth (some European Central Bank members, for example), Japan is an instructive lesson in how not to do it, and the limitations of fiscal policy.

> *Any inclination to utter phrases like "kick-starting the economy", should be rapidly expunged from your thoughts.*

The headline of the package has also swelled with repeated speeches, to stand at a chunky sounding JPY26 trillion (USD239 billion). Though as far as we can see from the Ministry of Finance, this refers to total spending on the boosted areas, not the actual additional (incremental) spending.

Selected fiscal stimulus measures and their cost

Stimulus measures	Supplementary budget	Initial budget for FY20 (increase from FY19)
Natural disaster recovery and protection	JPY2.4tr	JPY1.1tr
Boosts to SME productivity, overseas operations agriculture and forestry	JPY0.8tr	n/a
Support for child rearing, private consumption (points system for cashless payments) and society (child care, higher education)	JPY1.0tr	JPY0.6tr
Total	**JPY4.3tr**	**JPY1.8tr**

Source: Ministry of Finance, ING

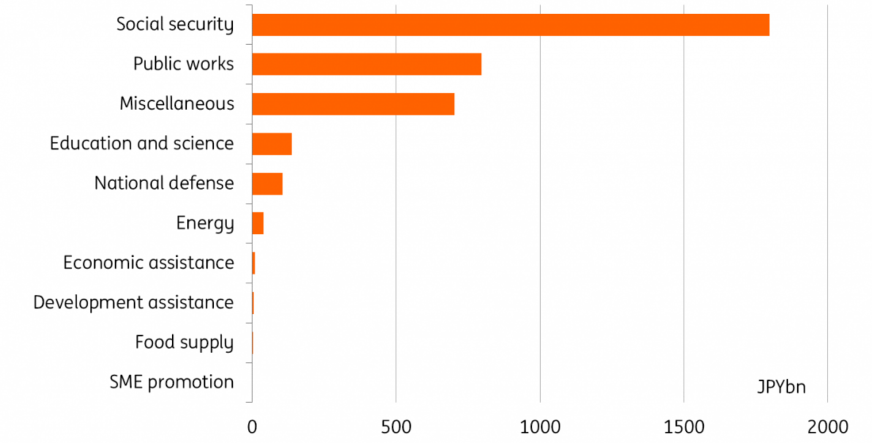
This is "slump avoidance" not "stimulus"

The measures so far outlined provide an offset to the construction spending slowdown anticipated at the end of the 2020 Tokyo Olympics preparation, and include plans to provide a tablet for every school desk to the end of junior school. It is also suggested that cashless payment will be encouraged by providing cash equivalent points to accounts that load up in excess of 20,000 yen onto smart phone payments systems.

There is without doubt a considerable amount of double-counting relating to these headlines. But as far as we can tell from the published documents, the combined size of supplementary budget measures and "stimulus" within the initial FY2020 budget sum to a much smaller JPY6.1 trillion (JPY4.8 trillion from the supplementary budget and JPY1.8 trillion from the initial budget). Perhaps the most telling figure is the FY2020 primary budget deficit which stands at an estimated JPY9.2

trillion, exactly the same as FY2019 – in short, the "fiscal thrust" is zero.

Incremental fiscal support measures (Supplementary 2019 and FY2020 initial budgets)



Source: Ministry of Finance, ING

Kick that can

In contrast, the government is claiming the package will have a net stimulatory impact on the economy of around 1.4 percentage points of GDP.

You can go round and round in circles with Japanese public finances and get nowhere fast. Whatever form of reality you accept with these numbers, the short story of this fiscal package is that far from providing a reason for upgrading our GDP forecasts for 2020, this latest stimulus merely provides an excuse not to slash them, and raises questions about how to avoid a slump in 2021.

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