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Article

Japan: Some policy tweaks but not a lot

Has the Bank of Japan strengthened its commitment to reaching the 2% inflation target or conceded defeat in getting there anytime soon? Absent a departure from an ultra-easier monetary policy stance, the 10-year JGB yield should retrace its recent spike

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-0.1%

BoJ policy rate
No change

BoJ maintains ultra-easier monetary policy stance

As widely expected, there was no change to the Bank of Japan's ultra-easier monetary policy stance, though today's policy meeting wasn't a complete non-event. There were some policy alterations aimed at enhancing the sustainability of its monetary policy, with more flexible market operations towards the price stability target of 2%. But the changes were subtle.

As we expected, the BoJ didn't abandon its inflation target nor was there any reduction in the asset purchases pace, both having grossly underperformed the 2% and JPY80 trillion targets, respectively.

So what's changed today?

1. **Inflation:** the downgrade of its inflation forecast for FY2018 to 1.1% from 1.3%, and that for FY2019 and FY2020 to 1.5% and 1.6% respectively, from an earlier 1.8% forecast for both years. The statement noted that "it is likely to take more time than expected to achieve the price stability target of 2%".
2. **Forward guidance (introduced for the first time):** the persistently low level of short- and long-term interest rates for an extended period of time, depending on uncertainty regarding economic activity and prices.
3. **JGB purchases:** some flexibility in the 10-year JGB yields around the 0% target, depending on economic activity and prices. A gradual reduction in the current account balances of financial institutions at the BoJ with the negative rate of 0.1%, from the current JPY 10 trillion.
4. **Asset purchases:** adjustment in the asset purchase amount depending on market conditions, and a shift in ETFs allocation towards Topix from Nikkei.

All boils down to inflation

However, everything boils down to achieving the price stability target. And after downgrading its inflation forecast for this and the next two years, the key question is: has the central bank conceded defeat on the objective of raising inflation to the 2% target level? Or just as today's statement notes at the outset, is the Bank actually strengthening its commitment to achieving this target? Only time will tell.

Even with the planned consumption tax in 2019, meeting the inflation target by next year remains a far cry, not only from the BoJ forecast but also from the consensus view. So is the unwinding of stimulus. While inflation so far this year is on track to meet our 0.9% annual forecast, we are reviewing our 1.8% inflation forecast for 2019 as well as the forecast timing of the start of tapering by the end of next year. But for now, absent a significant departure from an ultra-easy monetary policy stance, the 10-year JGB yield giving back its recent spike seems to be a reasonable expectation.

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