

# Daiwa's View

## IMF official also touched on deepening of negative rates by BOJ

- International understanding secured?

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### International understanding secured?

In his 19 October interview with the media<sup>1</sup>, BOJ governor Haruhiko Kuroda said that “If we need further easing of monetary conditions, we would certainly reduce short- to medium-term interest rates. But we do not want to reduce super-long interest rates,” which has come to be an issue.

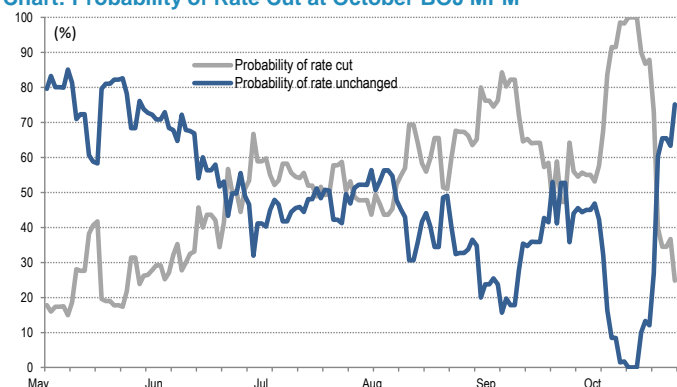
Of course, this remark is not advance notice of additional easing. He just indicated a policy option in the case that additional easing is necessary, and reconfirmed his previous remarks—he clearly stated in his interview with *Nikkei* dated on 5 September and [his 24 September speech in Osaka](#) that an additional easing option was deepening of negative rates and at the same time the BOJ did not want an excessive decline in superlong yields.

### ◆ Press Conference by BOJ governor Kuroda (24 Sep 2019)

• The conclusion of the Comprehensive Assessment in 2016 is unchanged. If we conduct additional easing, we need to lower short- and medium-term interest rates further. However, there is no need to cut superlong yields. On the contrary, we will not be surprised even if they rise.... If we cut short- and medium-term interest rates, we would adjust the JGB purchase program as needed to avoid an excessive decline in superlong yields.

That said, the BOJ reminded us of the fact that the first option for additional easing is deepening of negative interest rates in a situation where expectations for a rate cut at the October Monetary Policy Meeting (MPM) have declined to around 20%. We think that this fact is important. In this respect, Reuters interviewed an IMF official on 18 October<sup>2</sup>, who endorsed Mr. Kuroda's remarks, although the news did not attract market attention under screen of Mr. Kuroda's interview.

Chart: Probability of Rate Cut at October BOJ MPM



Source: Bloomberg; compiled by Daiwa Securities

<sup>1</sup> Reuters News: Kuroda says BOJ can 'certainly' cut short-term rates if it were to ease (19 Oct 2019).

<sup>2</sup> Reuters News: IMF says deepening negative interest rates an option for Bank of Japan (20 Oct 2019).

Concretely, Odd Per Brekk, deputy director of the IMF's Asia and Pacific department as well as a mission chief of Japan, stated that "We think that lowering the negative interest rate remains an option." In addition to monetary easing, he talked about the need of a package with fiscal policy and structural reform, saying that "Of course, given stubbornly anchored inflation expectations, a whole package (of steps) is needed, especially structural reforms."

However, Mr. Brekk opined in his April 2019 interview that "the first line of defense should be fiscal policy rather than conducting further monetary easing, if the risks turn out to materialize on the downside." Compared to six months ago, he has leaned toward further monetary easing and pointed out deepening of negative rates as a concrete tool. We think this fact is also important.

Every year, the IMF conducts a comprehensive discussion on the economic policy at member nations. Regarding Japan as well, the content is announced as "Staff Concluding Statement of the Article IV Mission." In the past, the content had a major impact on the subsequent fiscal and monetary policies also in Japan<sup>3</sup>. In fact, after the announcement of the Article IV Mission in June 2016, the BOJ conducted its "Comprehensive Assessment" and shifted to yield curve control (YCC) policy at the September 2016 MPM.

◆ **Japan: Staff Concluding Statement of the 2016 Article IV Mission (20 Jun 2016)**

• Monetary policy would have to be reset for the long haul and carefully balance the benefits of providing further easing with the potential risks to medium-term financial stability, including JGB market liquidity, the profitability of financial institutions, disintermediation, and reduced market functioning, and limits to JGB purchases and negative interest rates.

Given the latest remark by Mr. Brekk, we think that deepening of negative rates by the BOJ (if needed) has already gained international understanding. That said, the IMF is reiterating the side effects of monetary easing in the statement of the Article IV Mission—"the low interest rate environment exacerbates ongoing challenges for the financial system."

During his business trip to Washington, Mr. Kuroda clearly stated that "we are carefully watching the impact on financial institutions" and "we would address the side effects if we conduct additional easing." If the central bank chooses to deepen negative interest rates, it would announce a package to offset the adverse impact via measures to support bank earnings in the name of "measures to cope with side effects," in addition to induction of long-term/superlong yields to a somewhat higher level. Specifically, possible measures include (1) a revision to the three-tier structure of current account deposits at the BOJ (transfer to basic balance), (2) utilization of current account deposits at the BOJ as collateral, and (3) support for banks' foreign currency procurement.

<sup>3</sup> Mr. Brekk has been Article IV mission chief of Japan since previously.

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