Daiwa's Economic View

Emergency measures for US tariffs decided, focus remains on consumption tax cuts

- With government measures against US tariffs fixed, supplementary budget before Upper House election is unlikely
- Attention now shifts to Upper House campaign pledges and post-election negotiations between parties
- The biggest focal point is consumption tax cuts; differences between parties become key to tie-ups with ruling parties
- Government measures likely to push FY25 CPI down about 0.1ppt

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On 25 April, the government decided on measures to respond to higher US tariffs. The size of the measures is kept at a level that does not require a supplementary budget before the Upper House election. Thus, it seems unlikely that an extra budget will be compiled before the election.

Going forward, attention will shift to campaign pledges for the Upper House election and negotiations between the ruling and opposition parties on tax cuts after the election. In particular, consumption tax cuts will be the biggest focal point. While opposition parties are all demanding the implementation of tax cuts, the level of enthusiasm differs party by party, which will become a key to cooperation with the ruling parties.

Subsidies for gasoline and other items as a part of the economic measures are expected to push down FY25 CPI by about 0.1ppt.

Government decided on emergency measures for US tariffs, supplementary budget before Upper House election unlikely

On 25 April, the government decided on an "emergency package" in response to higher US tariffs. This time, the package mainly consists of programs that can be implemented within the FY24 supplementary budget or the initial FY25 budget. Specifically, they include a cut in gasoline prices (Y10/liter) and support for electricity and gas bills limited during Jul–Sep 2025.

The government has announced "immediate measures." The ruling and opposition parties are unlikely to have enough time to coordinate additional measures before the Upper House election. Thus, we can say that the possibility of the government announcing a supplementary budget before the election has virtually disappeared.

Focus will shift to campaign pledges and negotiations on tax cuts between ruling and opposition parties after the election

That said, the package is unlikely to be regarded by the public as sufficient to cope with rising prices. Some forecast that the ruling coalition may lose its majority in the July Upper House election. For this election, the Liberal Democratic Party (LDP) and Komeito already hold 74 uncontested seats (a majority in the Upper House requires 125 seats). The ruling coalition may lose its majority if the ruling parties win fewer than 50 seats (contested seats and currently vacant seats) in the election and the opposition parties win close to 80 seats.

Going forward, attention will be paid to campaign pledges for the Upper House election and negotiations between the ruling and opposition parties on tax cuts after the election. The upcoming pledges will influence not only an FY25 supplementary budget (autumn to winter) but also the FY26 tax reform and the FY26 initial budget (in Dec). This is because opposition parties are requiring tax cuts in areas such as gasoline tax and consumption tax. If the ruling parties are in a minority after the Upper House election, the budget can no longer pass the Diet without approval from some opposition members.

In the JGB market, the sense of caution about the issuance of additional JGBs has recently subsided. However, this could become a topic once again from before the election through the end of the year.

The biggest focal point is consumption tax cuts

Going forward, the biggest focal point remains consumption tax cuts. As the public is increasingly seeking action against inflation, debate on consumption tax cuts is accelerating among the ruling and opposition parties.

Most opposition parties actively support consumption tax cuts. On 25 April, the Constitutional Democratic Party (CDP) decided at its extraordinary executive meeting to include consumption tax cuts in its Upper House election pledge, which has a particularly strong impact. Although President Yoshihiko Noda was initially opposed to cuts, it appears that he was unable to ignore pressure from within the party. As a result, opposition parties are now all calling for consumption tax cuts, and the ruling parties cannot avoid discussions on this topic when negotiating with any opposition party.

- Democratic Party for the People (DPP): Across the board cuts to 5%
- Japan Innovation Party (JIP): Cuts of tax on foodstuffs (which had already been lowered to 8%) to zero for two years
- CDP: Temporary cuts of tax on foodstuffs to zero for a limited period of time (without relying on deficit-financing municipal bonds)

Within the ruling parties as well, calls for consumption tax cuts are growing.

- Komeito: Leader Tetsuo Saito stated on 24 April that "a [further] cut to the lowered tax rate is also an option"
- LDP: On 24 April, Upper House Secretary-general Masaji Matsuyama submitted policy requests for Upper House election to party leaders
  In an LDP Upper House member survey, 80% called for consumption tax cuts, of which 70% requested a cut of the lowered tax rate for foodstuffs.

This is a matter that is still a little ways off for the moment, but if consumption tax cuts are to be implemented, the differences in the approach among parties could be a key when deciding on which opposition parties will cooperate with the ruling parties. This will eventually affect the size of the issuance amount of JGBs.

- Targeted items for tax cuts (across the board or only foodstuffs)
- Extent of rate cuts (to what percent, including zero)
- Duration of tax cuts (limited short period of time or open-ended)
- Resources to cover tax cuts (secured or deficit-financing bonds)

Gasoline subsidies in economic measures to push down FY25 CPI by around 0.1ppt

In the latest emergency package, a fixed reduction is to be implemented for gasoline and diesel prices (Y10/liter) and for heavy oil and kerosene (Y5/liter). These measures are scheduled to take effect on 22 May, after a notification period of about one month, which is expected to push down FY25 core CPI by around 0.1ppt.

Meanwhile, the details of support measures for electricity and gas bills are likely to be decided in May. As the support is to be applied to Jul–Sep bills, the downward effect on CPI is expected to appear in Aug–Oct. This is because Jul–Sep refers to the period when electricity and gas are used, with the bills actually being sent in Aug–Oct.

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