

Daiwa's Economic View

Potential risk of Komeito leaving coalition deserves more attention than DPP leader Tamaki's political future

- Following Takaichi's victory in LDP presidential election, market is focused on potential coalition with DPP and future of its leader Tamaki, but likelihood of Tamaki becoming Finance Minister or Prime Minister is small
- The more pressing issue warranting attention is potential risk of Komeito leaving coalition due to serious conflict with LDP
- There are already emerging concerns about schedule for formulating budget and other matters being delayed; there would be sudden rise in political uncertainty if Komeito actually left coalition

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With Sanae Takaichi having become the president of the Liberal Democratic Party (LDP), the market is focused on her party potentially forming a coalition with the Democratic Party for the People (DPP). However, there is currently little chance of DPP leader Yuichiro Tamaki becoming Finance Minister or Prime Minister.

The more pressing issue warranting attention is the potential risk of Komeito leaving the coalition due to a serious conflict with the LDP. This conflict is already raising concerns about the schedule for formulating the budget and other matters being delayed. If Komeito were to actually leave the coalition, there would be a sudden rise in political uncertainty.

Concerns about Tamaki becoming Finance Minister or Prime Minister have receded substantially

With the new LDP President Takaichi taking office and the LDP and DPP growing closer, the JGB market is sensing that there is a risk that Yuichiro Tamaki could become Finance Minister or Prime Minister. However, it is currently unlikely that Tamaki would be appointed to either position.

Firstly, with regard to the possibility of Tamaki becoming Finance Minister, it would be difficult for the DPP to join the LDP-Komeito coalition after Takaichi had been appointed Prime Minister. The Japanese Trade Union Confederation (Rengo), the DPP's largest supporting organization, has clearly stated that the DPP's participation in the ruling coalition would be unacceptable. With many core members of the DPP being lawmakers from labor unions, the party cannot ignore the views of Rengo on this issue.

Tamaki himself has cited the abolition of the provisional gasoline tax rate—an issue already agreed upon by the LDP, Komeito, and DPP—as a prerequisite for joining the coalition. This provisional gasoline tax rate will very likely be abolished as part of the Takaichi administration's economic measures. In other words, this would mean that the DPP would not be a part of the coalition at the time of the start of the Takaichi administration.

And, regarding the possibility of Tamaki becoming Prime Minister, we think it is even less likely that Tamaki could become a candidate for Prime Minister who would be able to create unity among opposition parties. Tamaki himself has indicated that he is opposed to the idea, stating that he could not partner with parties that have different fundamental policies. The Constitutional Democratic Party of Japan (CDP) is pushing for a candidate for Prime Minister who could create unity among opposition parties, but the gaps between the CDP and the DPP are significant, particularly on energy and national security policies.

Deepening LDP-Komeito conflict; Komeito seriously considering leaving coalition

The potential risk of the LDP-Komeito coalition dissolving is the political event that the market should be focused on at the moment, rather than what is happening with Tamaki and the DPP. The conflict between the two parties has become more serious since Takaichi won the leadership election. However, the true point of contention is the LDP's handling of political funding scandals, not the conservative stance taken by Takaichi.

On 7 October, the LDP leader Takaichi and Komeito leader Tetsuo Saito held their initial meeting, but, unusually, the agreement to continue the coalition was postponed. Komeito itself is not involved in the political funding scandals. However, its coalition with the LDP causes it to be viewed in a similar light by the public, which has become one of the reasons it has lost seats. In the wake of their failure to secure a majority in the Upper House election in July, Komeito is making forceful demands that the LDP tighten regulations on corporate donations and fully disclose the details of the slush fund scandal.

The LDP and Komeito have been in a coalition for nearly 30 years, and this is not their first conflict. However, the current confrontation appears to be very serious. It has been reported that Komeito held a party meeting on the 9th in which opinions were split roughly fifty-fifty regarding whether the party should stay in the coalition.

However, the LDP's position is that it is opposed to stricter regulations on corporate donations, and that the slush fund issue has been settled through internal party discipline and the public's verdict in the election. The fact that President Takaichi and Vice President Taro Aso have almost no ties with Komeito is exacerbating the situation. On the 9th, President Takaichi met with former Prime Minister Yoshihide Suga, who has strong ties with Komeito, suggesting that she is desperately searching for a solution.

Komeito plans to decide the direction of the coalition at a party leaders' meeting on the 10th. The LDP-Komeito coalition is truly at a critical juncture.

LDP-Komeito conflict is delaying nomination of prime minister, and also affecting the timing of budget formulation

The conflict between the LDP and Komeito is also affecting the timing of the formulation of the budget. The election to nominate the prime minister to be held in the extraordinary Diet session, initially scheduled for 15 October, is now expected to be postponed to the 20th or 21st. Following that, a series of diplomatic events are scheduled, making a short-term resolution necessary.

If the launch of the Takaichi administration were delayed, the entire schedule for formulating economic measures and other tasks would also be pushed back. The cabinet's decision on the FY25 supplementary budget and the revisions to the JGB issuance plan are likely to be delayed until December. Passage of the budget within the calendar year is now at risk. According to the usual schedule, the FY26 initial budget would be decided by the cabinet in late December, along with the JGB issuance plan, but this could also be affected.

Political situation would suddenly become highly uncertain if coalition collapsed

Should the LDP-Komeito coalition actually collapse, the political outlook would become completely unpredictable.

To begin with, it would be unclear whether the election to nominate the prime minister in the Diet would result in Takaichi becoming Prime Minister. Even if a Takaichi administration were formed, it would be an even smaller minority ruling party than the LDP-Komeito coalition, making it extremely difficult to pass budgets and bills in the Diet.

If she were to call a snap general election, the LDP would lose Komeito's powerful electoral support, likely making a further reduction in the number of seats unavoidable.

The Takaichi administration's cabinet appointments and fiscal policy will become matters of interest once the LDP-Komeito coalition is safely secured. The issue could be resolved if the LDP were to compromise on the political funding issues. However, not all LDP lawmakers believe a coalition with Komeito is indispensable, so there is a risk that we will not be able to rest assured of a positive outcome to the situation. For now, the focus of attention should be on the fate of the LDP-Komeito coalition.

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