

# Daiwa's View

## PM Takaichi's press conference: Glimpsing future through midwinter election

- Outright LDP majority seen as de facto line determining victory or defeat?
- Higher hurdles to dispelling fiscal concerns as consumption tax cut debate ramps up
- Rising price spiral driven by fiscal stimulus, yen depreciation

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### Outright LDP majority seen as de facto line determining victory or defeat?

Prime Minister Sanae Takaichi announced at a press conference on 19 January that the Lower House would be dissolved on 23 January with the election officially announced on 27 January and voting/ballot counting taking place on 8 February. In explaining the reason for this move, Takaichi stressed that the objective is to again seek renewed public trust for important policy shifts, including a new ruling party structure, a shift to proactive fiscal policy, and enhancing Japan's security policy. She positioned this as "election to create our own future."

Also, Takaichi defined the line demarcating victory or defeat as a "ruling coalition, including the Japan Innovation Party (JIP), securing a majority of seats." She also clearly stated that she was staking her own political future as prime minister on this election. However, dissolving the Lower House this time could risk the creation of a political vacuum at a time of heightened geopolitical risks stemming from deteriorating Japan-China relations. This also carries significant costs such as potential delays in passing the budget. In fact, Takaichi stated that while thorough preparations had been made to ensure no disruption for managing the economy through measures like the FY25 supplementary budget, she also suggested that a provisional budget proposal might be formulated.

Even so, if the election merely results in the ruling party maintaining its majority as before the dissolution, dissatisfaction labeled as "results that did not justify the risks" could emerge within the party. On the surface, a ruling party majority may be the benchmark for the LDP's future, but in reality, Takaichi's clout within the LDP could wane. As such, for Takaichi, the de facto line between victory and defeat will likely be whether the LDP secures an outright majority.

### Even higher hurdle for dispelling fiscal concerns surrounding consumption tax cut

Takaichi announced during her press conference that she intends to set the consumption tax on food and beverages to 0% for a period of two years. This policy is included in the agreement between the LDP and coalition partner JIP. The prime minister herself has expressed strong enthusiasm for tax cuts, stating that this was "a long-cherished aspiration." Following this press conference, JIP co-leader Fumitake Fujita also expressed his "strong support" for reducing the consumption tax on food and beverages.

Meanwhile, reducing the consumption tax on food and beverages is expected to require approximately Y5tn in funding. Takaichi explicitly stated that the government would "not rely on special deficit-financing JGBs" for such funding. She stated that a national council to be held will examine the sources of funding and the schedule. During the press conference she touched on reviewing overall expenditures and revenues, including subsidies, to secure funding sources, but specific measures remain unclear.

The policy of “not relying on special deficit-financing JGBs” itself appears to have been a statement by the Takaichi administration that took the market into consideration to the greatest extent possible. The decision to make the consumption tax cut a temporary measure lasting two years is likely based on that same rationale. If it is a temporary measure, there is no absolute need to make the funding source permanent, while the risk of making the fiscal burden permanent could be mitigated.

The most notable aspect of this press conference was that Takaichi reversed her cautious stance on consumption tax cuts since taking office and shifted to a proactive policy. Since she took office, the market has continued to express caution regarding proactive fiscal policy. A policy shift under such circumstances would further raise the hurdle for dispelling fiscal concerns.

For policymakers, including those in the Prime Minister’s Office, the hurdle to “stop” economic stimulus measures is higher than that to “continue” them. As such, the possibility that the consumption tax cut may not be limited to the initial “two-year temporary measure” will likely remain a concern. Even if a temporary funding plan is presented, concerns about financial deterioration are likely to continue to smolder.

If the ruling party wins the Lower House election, it has been suggested that the government could submit a tax reform bill incorporating a consumption tax cut at the earliest opportunity during the extraordinary Diet session slated for after the election. However, submitting a bill is merely the beginning of the process. In addition to discussing and enacting the bill, considering the preparation required on the ground (designing systems and modifying business operator systems) it is expected that a considerable amount of time will be needed before actual execution. Kyodo News reports a plan for “as early as January 2027,” but realistically, implementation in April 2027 at the earliest would be more appropriate.

### **Consumption tax cut debate accelerates across ruling/opposition parties; fiscal stimulus regardless of election results**

On 19 January, the new “Centrist Reform Alliance” political party, formed by the Constitutional Democratic Party of Japan and Komeito, announced its “Centrist Reform Alliance Platform.” This party advocates “realizing politics that puts citizens first.” Under the slogan “building a new social security model,” which is one of its pillars, it has promoted measures such as a 0% consumption tax on food items (permanent measure) and reducing the burden of social insurance premiums.

In the 2025 Upper House election, while the opposition parties advocated for a consumption tax cut, the ruling coalition at that time (LDP and Komeito) was reluctant. As such, discussions on a consumption tax cut did not move forward. However, in this Lower House election, discussions surrounding consumption tax cuts are now accelerating among both ruling and opposition parties. In other words, regardless of the outcome of the Lower House election, the weighting of prioritized policies could simply change. It is highly likely that a certain degree of fiscal stimulus will be implemented.

Takaichi also stated at her press conference that real wages are projected to turn positive in 2026, citing the effects of government measures to address rising prices. However, the deflator used to calculate real wages is a comprehensive index that excludes imputed rent, making a higher y/y increase than the headline CPI or core CPI (we forecast +1.8% core CPI for FY26) likely. Also, considering that total cash wages for FY25 remained in the mid-2% range, the positive margin for real wages in FY26 is not significant. In other words, if the yen continues to depreciate, there is a good chance that real wages could turn negative again in FY26.

Takaichi has explicitly stated, “We will break away from the budget formulation method that assumes supplementary budgets will be enacted every fiscal year. Instead, we will allocate necessary funds in the initial budget.” However, the possibility of further fiscal stimulus through a supplementary budget cannot be ruled out if real wages were to fall into negative territory.

Meanwhile, if the consumption tax on food items is set at 0%, it could potentially boost real GDP by approximately 0.15ppt and lower the headline CPI by approximately 1.6ppt. If this effect materializes, the CPI could temporarily drop well below 2%. That said, the progression of yen depreciation stemming from fiscal policy and the output gap improvements will heighten medium/long-term inflationary pressures. We should note that the downward pressure on prices due to fiscal stimulus, when accompanied by yen depreciation, cannot serve as a fundamental solution for high prices.

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