

BANK OF JAPAN'S MONETARY POLICY AND IMPLICATIONS FROM FED'S POLICY

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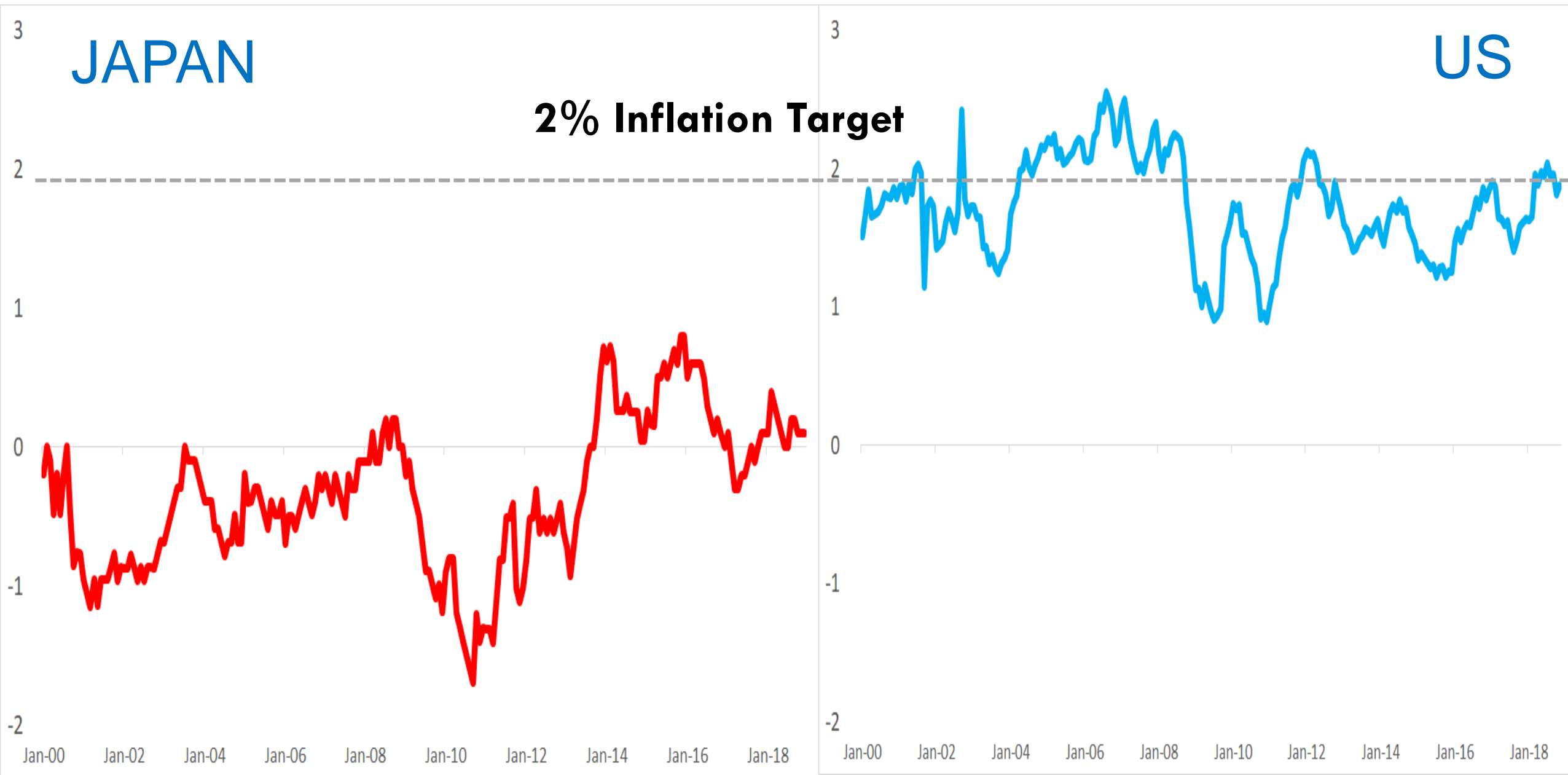
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**1. INFLATION & INFLATION
EXPECTATIONS
~ JAPAN AND THE US ~**

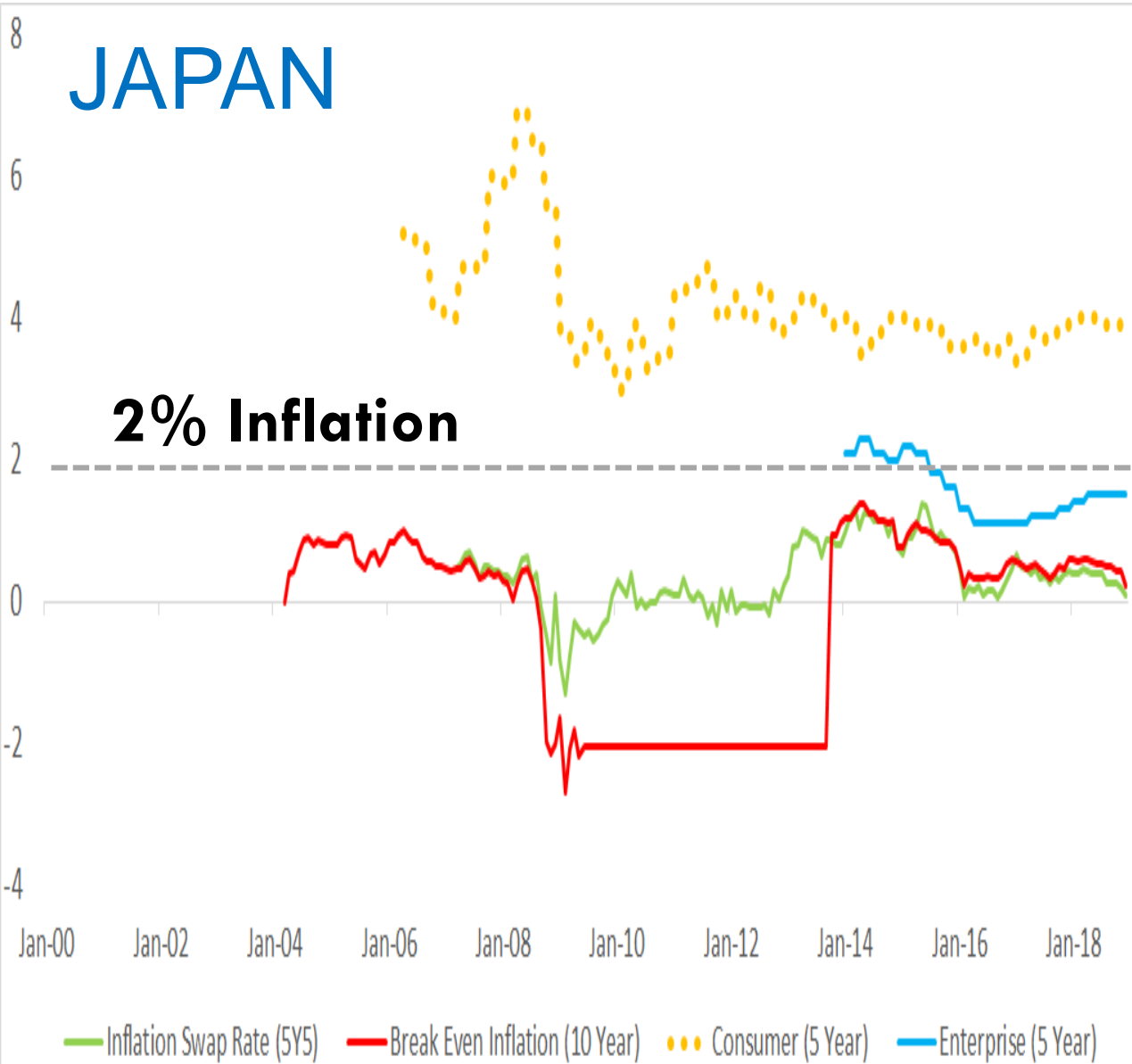
UNDERLYING INFLATION



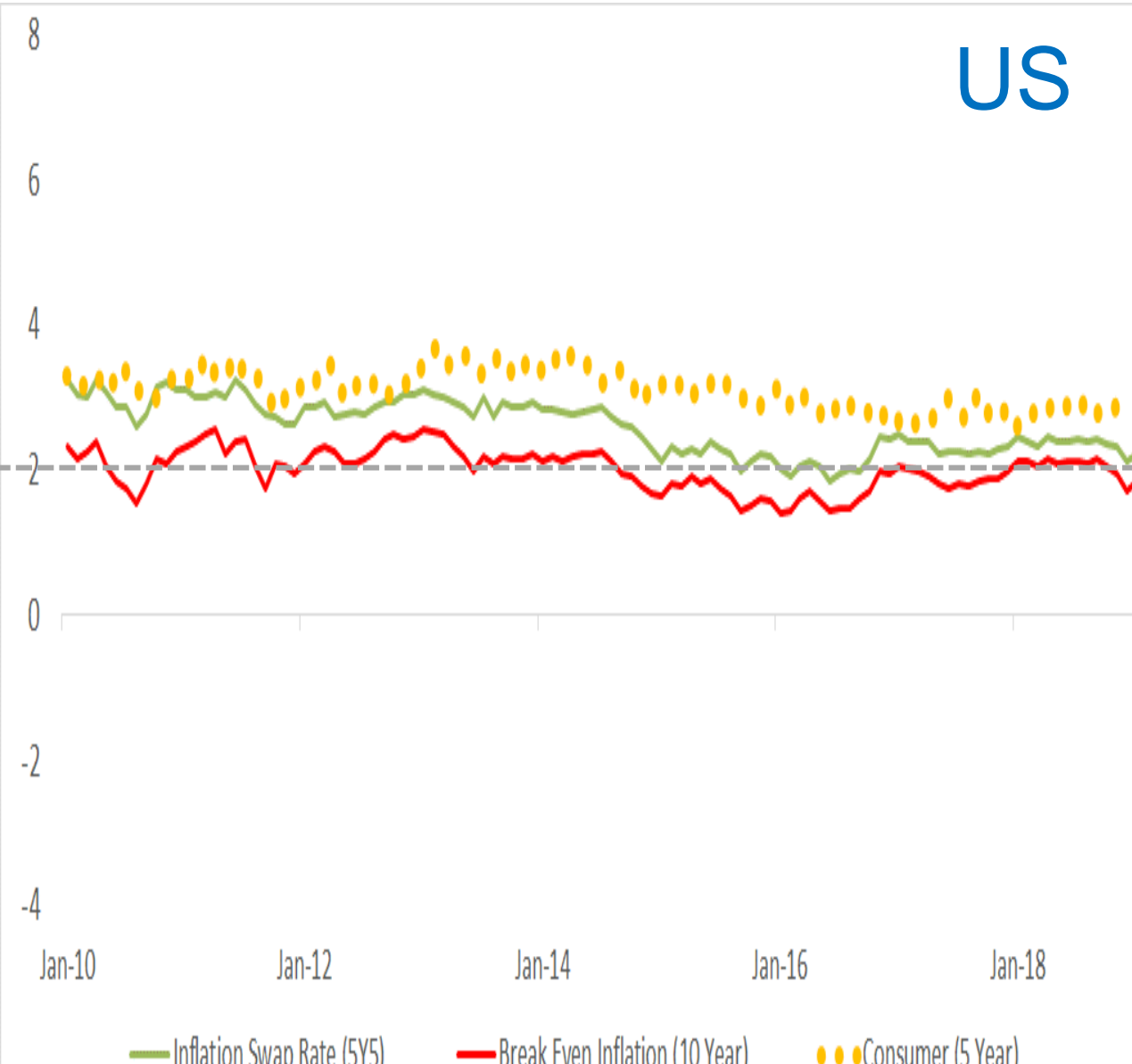
INFLATION EXPECTATION

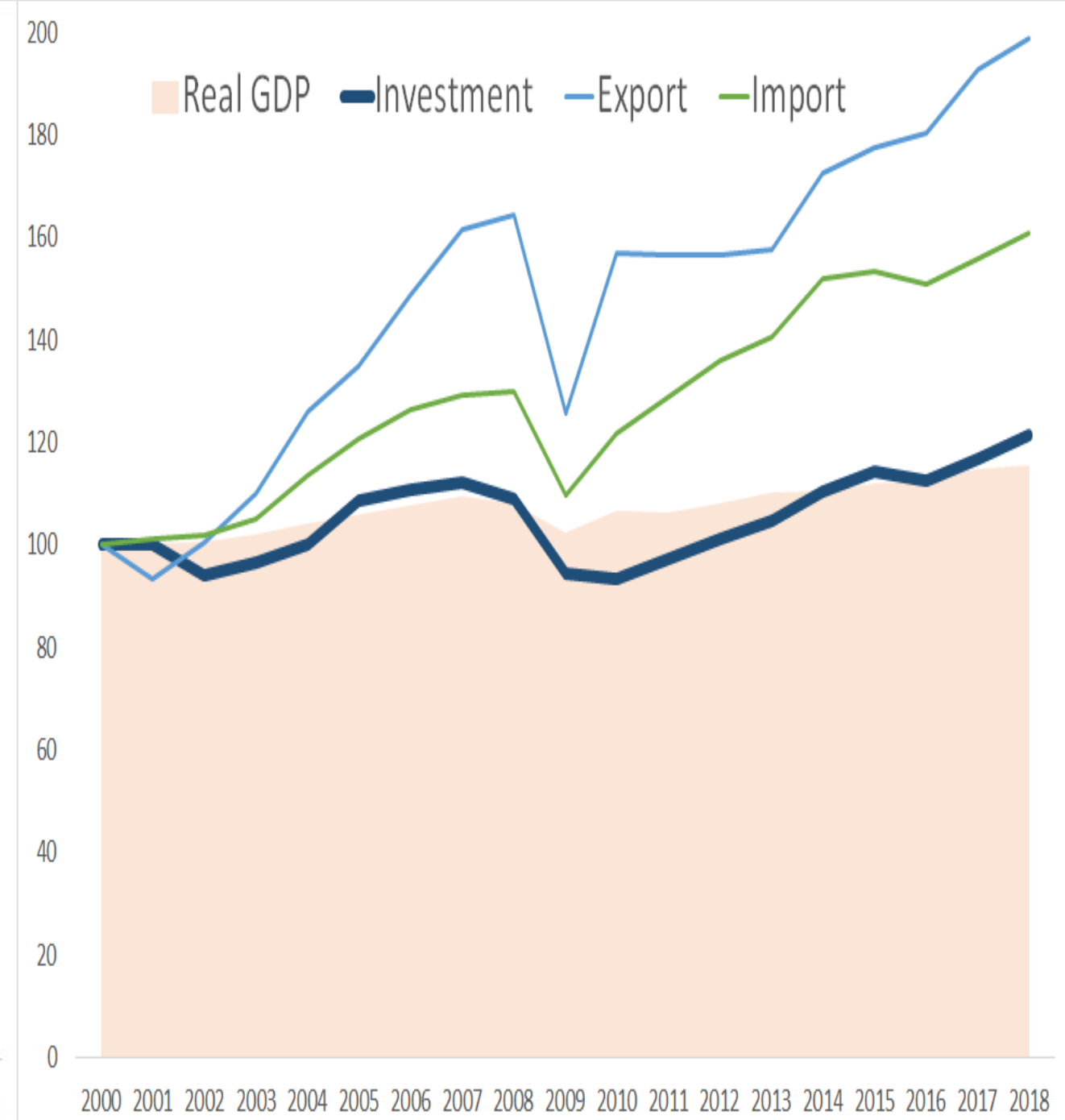
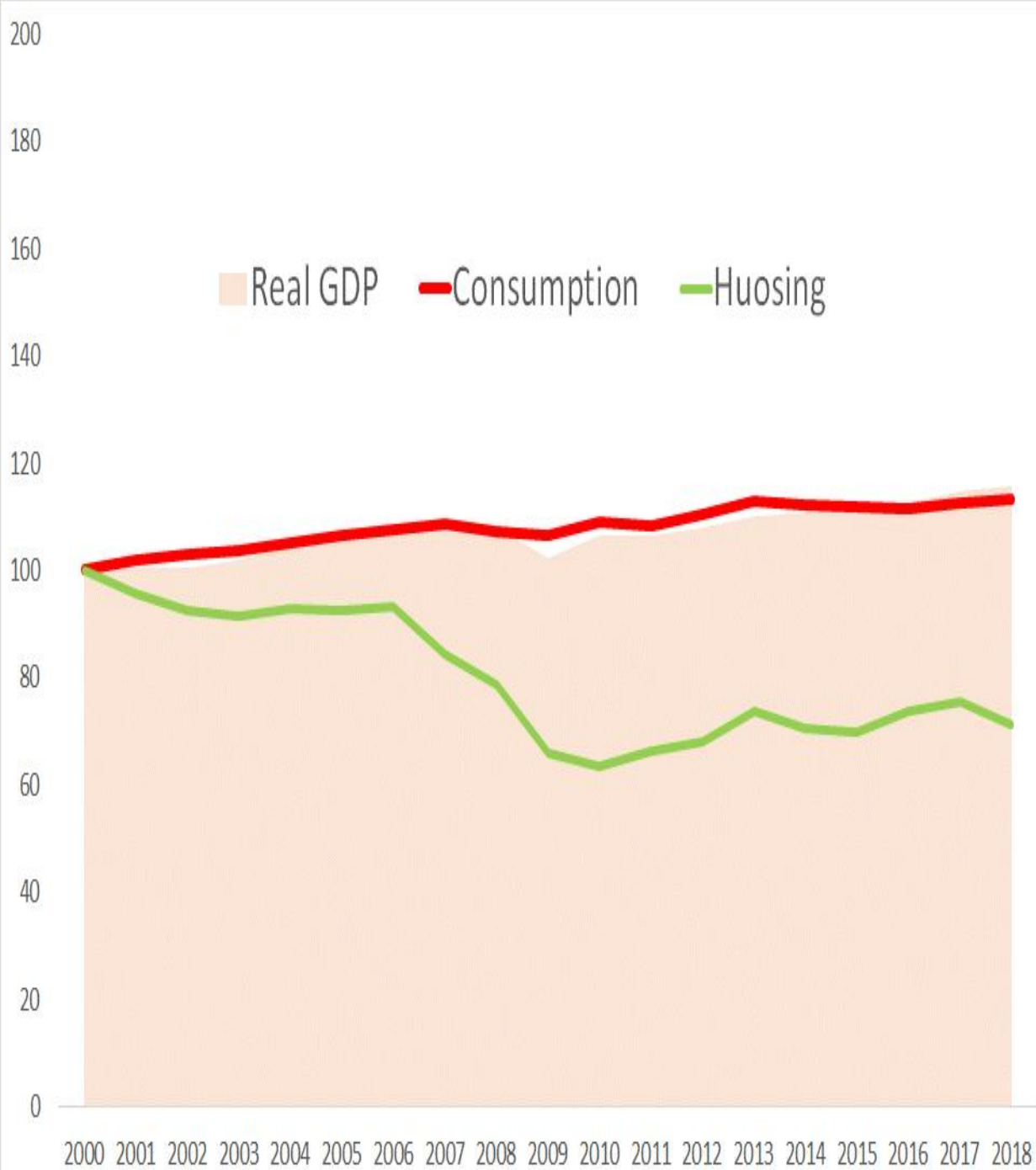
JAPAN

2% Inflation



US





BOJ

ALMOST GIVING UP
THE 2% TARGET



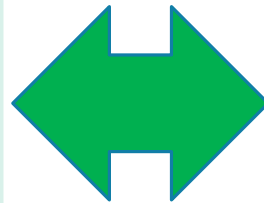
Flexible Interpretation
of the 2% Target
($\pm 1\%$)?

THE FED

ENSURING
SYMMETRIC 2%
INFLATION TARGET



The Price-Level
Targeting?



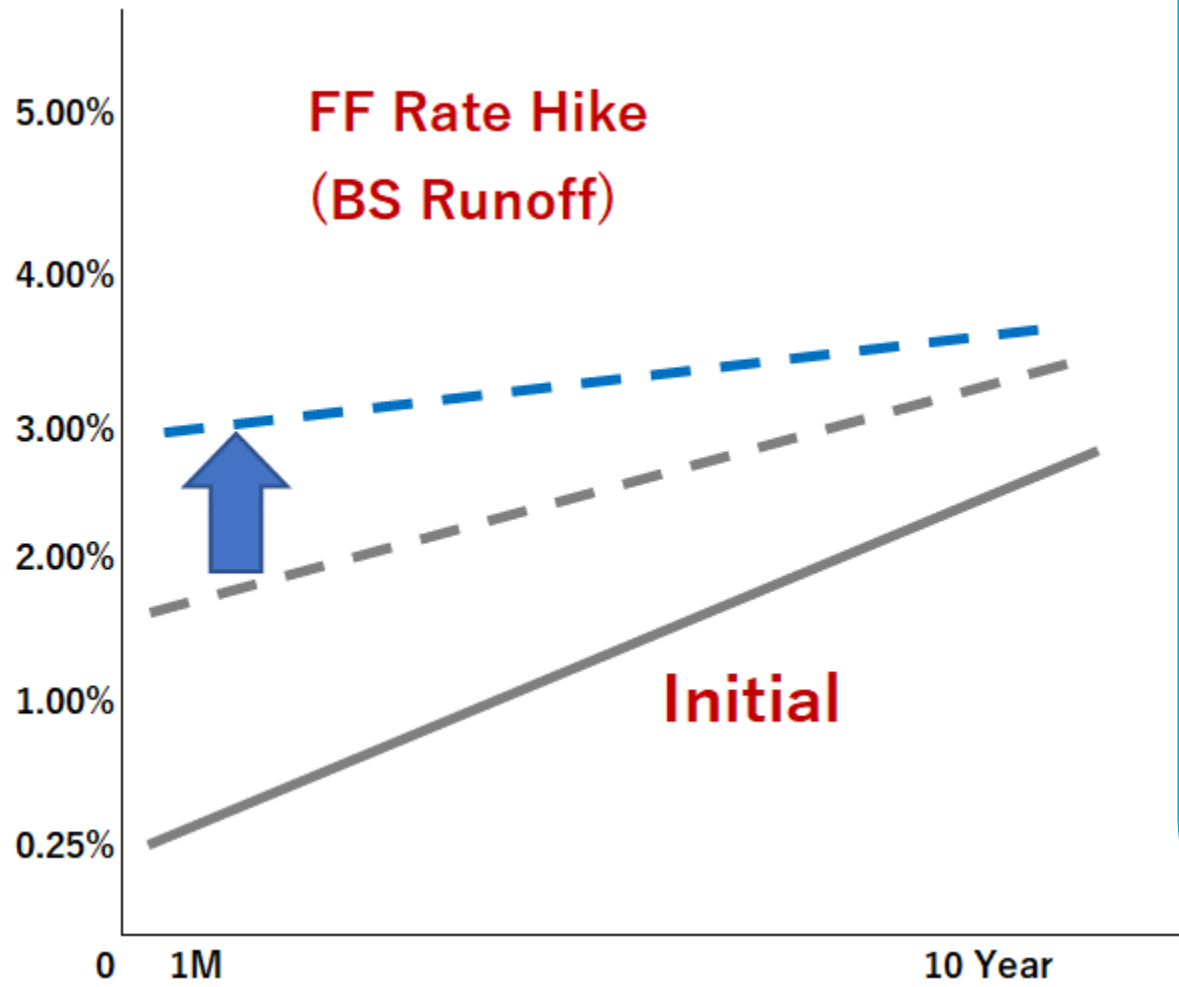
2. ACTIONS FOR 2019

~JAPAN AND THE US~

BOJ: UNANTICIPATED DEVELOPMENTS SINCE THE 4TH QUARTER 2018

- **Underperformance** of Japan's **stock prices** and downward-revision of **corporate profits**
- **Downward pressures** on the **10-year yield**
- **Renewed pressures** on **yen' appreciation**
- **Change** in **Fed's Monetary Policy Stance**

ACTUAL YIELD CURVE



FED & BOJ

- Uncertainty because of the faster-than-expected flattened yield curve
 - One more hike only?
- May be good for US stock prices but bad for the \$/¥ yen rate
- Japanese stock prices may be volatile due to conflicting forces (favorable US stock prices but potentially-greater appreciation pressures)

FED: GREATER MARKET DEMAND FOR (LONG-RUN) RESERVE BALANCES

July 2017

SOMA Holdings \$3.2
trillion

Reserve Balances:
\$613 billion

June 2018

SOMA Holdings \$3.7
trillion

Reserve Balances:
\$880 billion

Dec. 2018

SOMA Holdings \$4.0
trillion

Reserve Balances:
\$1.2 trillion

- FED's balance sheet runoff may **end up earlier** than initially projected
- FED's more dovish done since Jan. 2019 have amplified markets' expectations
- May be good for US stock prices but **bad for the \$/¥ rate**

Growing Dilemma

Growing Stress
in the Financial
Sector

Need to Keep
roughly over
105 yen

BOJ

- Likely to maintain the 0% 10-year yield target and $\pm 0.2\%$ range ($\pm 0.3\%$ if possible)
- Need to find a right amount of **JGB** purchases in the substantially-low 10-year yield environment
- Continue **ETF** purchases of around 6 trillion yen

3.OPTIONS FOR THE BANK OF JAPAN AND NORMALIZATION

Forward Guidance

Limited impact when **neutral rates** are **low**

Less credible due to **limited** impacts on inflation

QE

Potentially-**large** balance sheet damage

Distortion in asset markets and Inequality

Negative Rate

Stress on the financial sector

Cash substitution

BOJ'S FORWARD GUIDANCE

Original

- will continue with **QQE with YCC**, aiming to achieve 2%, **as long as necessary for maintaining 2% in a stable manner**

Over-Shooting

- will continue **expanding the monetary base until the core inflation exceeds 2% and stays above 2% in a stable manner**

YCC

- **maintain the current low levels of short- and long-term interest rates** for an extended period of time, taking into account uncertainties including the effects of the **consumption tax hike**

UNWINDING PROCESS

- **Widen** the 10-Year Target Rang ⇒ Raise Target
- Continue to **Taper** JGB Purchases

Need to Modify Forward Guidance

- **Complete** the Tapering of JGB Purchases
- **Eliminate** the 10-Year Target and Range

The First Short-Term Rate Hike

Cut in ETF Purchase