Economics & Strategy

DBS Flash

Japan: BOJ expands risky asset purchases

Economics/growth/monetary/fiscal

Group Research

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- *The Bank of Japan announced to expand the purchases of risky assets at today's meeting, including ETFs, REITs, CPs and corporate bonds.*
- *The BOJ will also establish a new lending program to help corporate financing*
- *Given the high degree of economic and financial market uncertainties, further easing remains likely*
- ***Implication for our forecasts**: We maintain the forecast of a 10bps cut in the short-term policy rate in 1H20. Additional fiscal stimulus is also expected ahead*

Following the US Fed's emergency policy move overnight, the Bank of Japan (BOJ) brought forward its regular meeting by two days and announced a set of measures to support the economy hit by COVID-19. These include:

1) Double the pace of ETF and REIT purchases to JPY 12tn and JPY 180bn per annum, respectively
2) Raise the upper limit of CP and corporate bond purchases by JPY1tn each, to JPY3.2tn and JPY4.2tn respectively
3) Introduce a new lending program, providing commercial banks with one-year, zero interest rate loans using corporate debt as collateral (JPY8tn)

The short-term and long-term interest rate targets, however, were left unchanged at -0.1% and 0% respectively. The quantitative target of JGB purchases was also kept unchanged, at "around JPY80tn" per annum.

An initial response to recession and deflation risks

From the macro perspective, the BOJ is responding to the risks of economic recession and deflation caused by the COVID-19 outbreak. GDP growth already fell sharply by -7.1% QoQ saar in 4Q19, dragged by the consumption tax hike and typhoon. Growth looks set to contract further in 1Q20, as the COVID-19 epidemic hurts both overseas and domestic demand. Exports to major markets are likely to decline on a broad basis in 1Q20, as the COVID-19 related disruptions spread from China/Asia to Europe and the US. Domestic consumption would also be hit badly, given the steady rise in infection cases in Japan, the sharp decline in the Nikkei, as well as the news about a possible delay/cancelation of Tokyo Olympics.

The BOJ's monetary policy framework

	Quantitative and Qualitative Easing					Yield Curve Control	
	JGBs	ETFs	REITs	CPs	Corporate bonds	Short-term	Long-term
	(JPYtn, per annum)	(JPYtn, per annum)	(JPYbn, per annum)	(JPYtn, outstanding)	(JPYtn, outstanding)	(%)	(%)
2013/04	60-70	1	30	2.2	3.2		
2014/10	80	3	90				
2015/12		3.3					
2016/01						-0.1	
2016/07		6					
2016/09	About 80						Around 0 (±10bps)
2018/07							Around 0 (±20bps)
2020/03		12	180	3.2	4.2		

Sources: BOJ, DBS

On the prices front, Core CPI in Tokyo already dropped notably to 0.5% YoY in Feb20, down from 0.8% in Dec19. The ongoing deterioration in the output gap and the collapse in oil prices will likely bring deflation/deflation expectations in the months ahead. Meanwhile, the Fed slashed rates to zero and restarted QE at its emergency meeting overnight. Aggressive easing by the Fed could induce appreciation pressure on the yen versus the dollar, which in turn, compounds deflation pressures in Japan.

What's the next?

Still, the BOJ's policy decision failed to impress investors today. The Nikkei closed 2.5% lower. And the USD/JPY dropped by 1.4% to 106.4 as of the time of writing. For now, the BOJ remains cautious about pursuing more radical easing measures – deepening the negative interest rate policy (NIRP), probably due to concerns about the adverse impact on banks' earnings.

Given the high degree of economic and financial market uncertainties, we think further easing remains likely in the months ahead. We continue to expect a 10bps cut in the short-term policy rate in 2Q20, which would be accompanied by counteracting measures to mitigate the side-effects on the banking sector.

Fiscal stimulus is also on the cards. The cabinet has approved a sizeable supplementary budget worth JPY4.5tn (0.8% of GDP) in Dec19, to cushion the impact of the earlier consumption tax hike and typhoon disaster. With Abe's government vowing to take bold steps to beat the COVID-19 fallout, extra spending of JPY5-10tn could be expected ahead.

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Sources: Data for all charts and tables are from CEIC, Bloomberg and DBS Group Research (forecasts and transformations).