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# New Age for the monetary Policy

# OUTLINE OF PRESENTATION

## Part 1

- **Exchange-Traded Fund Purchases and Five Related Issues**

## Part 2

- **Feasibility of the 2% Price Stability Target**

## Part 3

- **Searching for a New Monetary Framework**

# **Part 1. BOJ's ETF (Stock) Purchases and 5 Related Issues**

# Central Banks' Stock Purchases for Two Reasons

Monetary Policy  
counter-cyclical  
policy

Reserve Management  
management of  
foreign reserves held  
by central banks

# Gov. Bonds As Main Purchasing Assets

- JGB yields are the **benchmark** for measuring long-term fixed interest rates (mortgages, loans, and corporate bonds).
- The decline in the yields will help to raise risk assets (such as **stocks**) through promoting **search for yield** due to **declined returns on bonds**.
- The decline in the yields will help to raise risk assets through **lowering the discount rate** and thus higher PV of cash flows.

# Why led to BOJ's Decision to Purchase ETFs?

- Exerting downward pressure **directly on the risk premia**, thereby promoting the stock markets and **portfolio rebalancing among individuals**.
- Promoting a **wealth effect** directly.
- Generating momentum to correct **undervaluation** of stock prices speedily.

# What are the ETFs?

 Listed on the stock exchange.

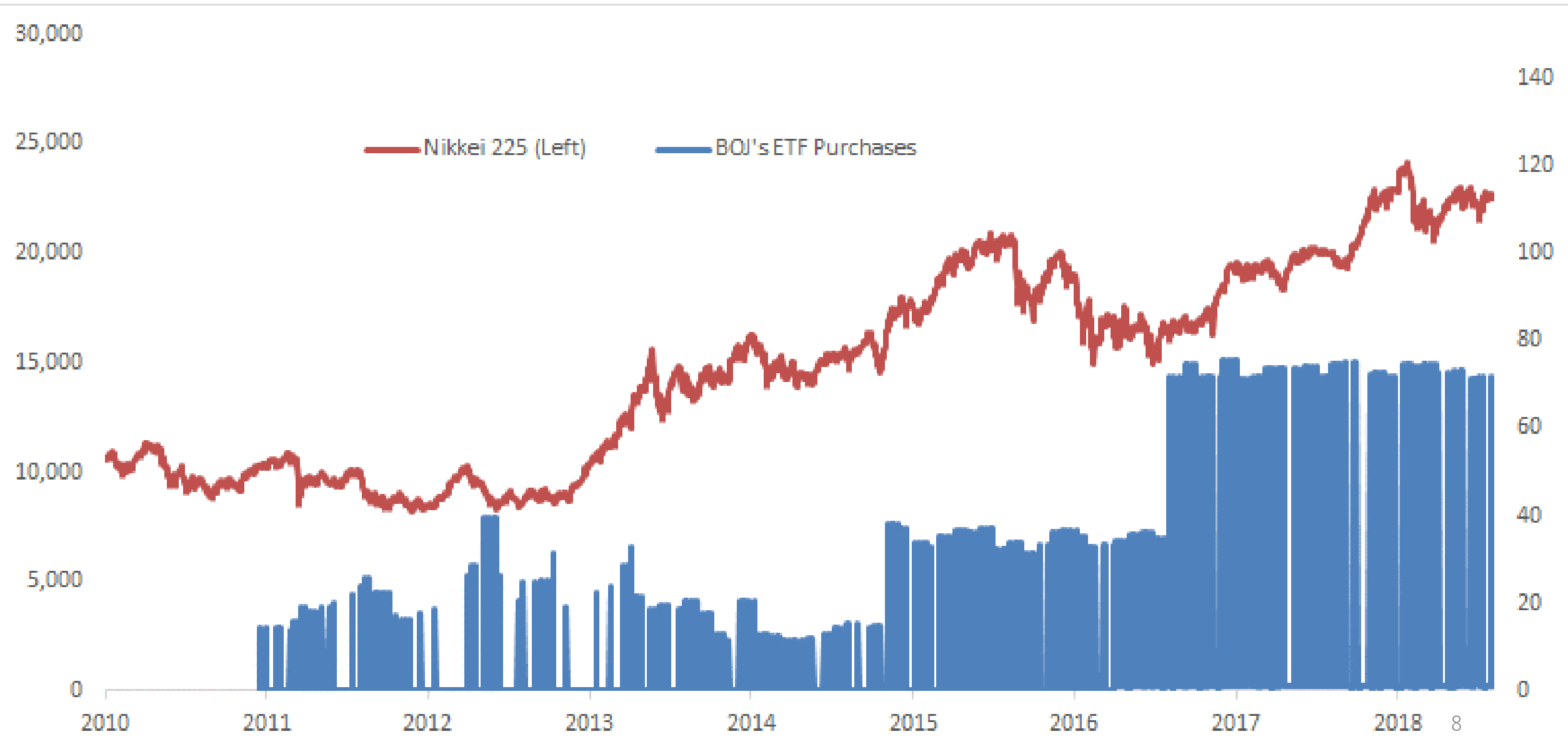
 ETFs Track (1) TOPIX, (2) Nikkei 225, (3) JPX-Nikkei Index 400

 BOJ indirectly purchases stocks through trust banks.

 BOJ DOES NOT exercise voting rights.

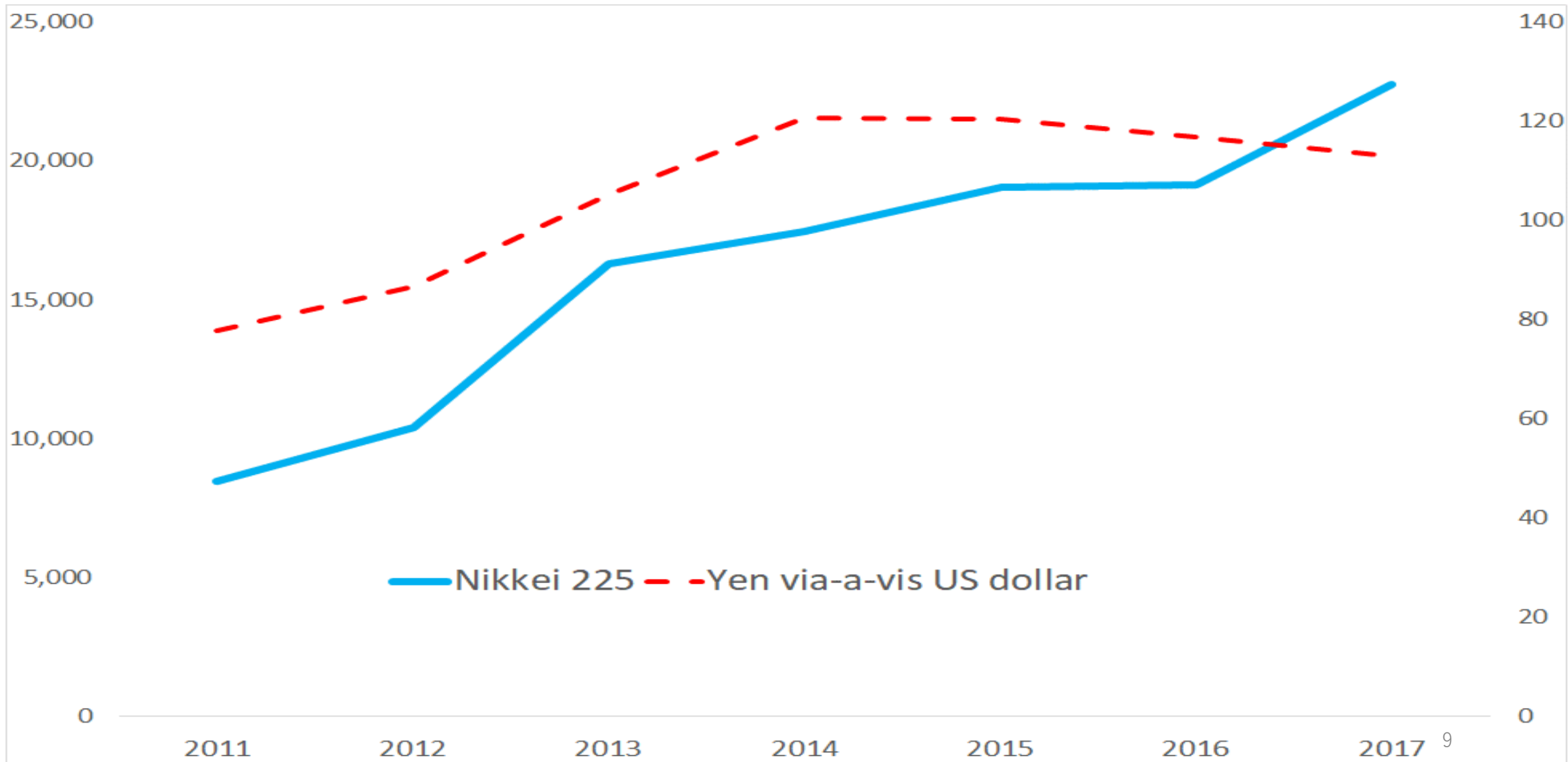
 The BOJ purchases about JPY 6 trillion annually.

# Stock Price and ETF Purchases



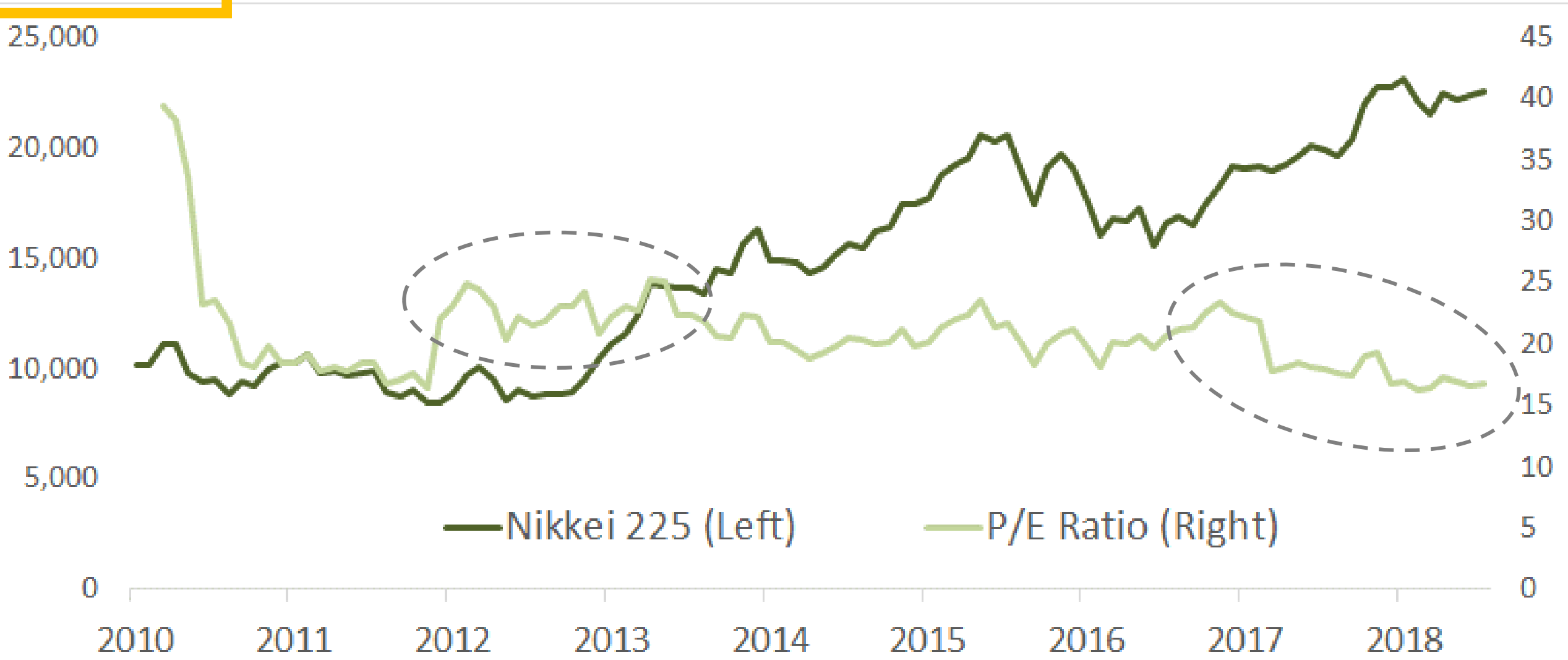


# NIKKEI 225 AND YEN VIS-À-VIS US\$



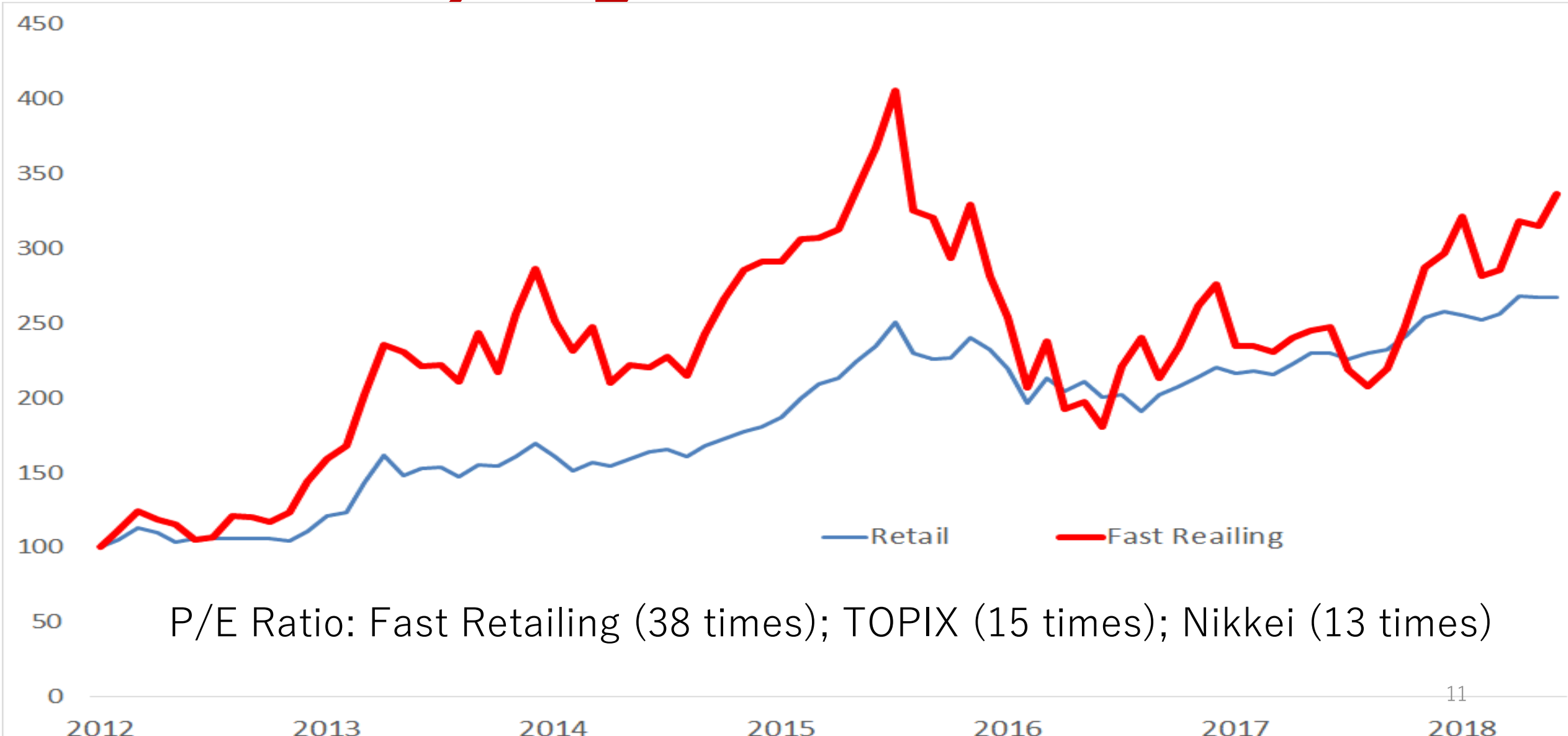
# Issue 1

# Stock Price and P/E Ratio



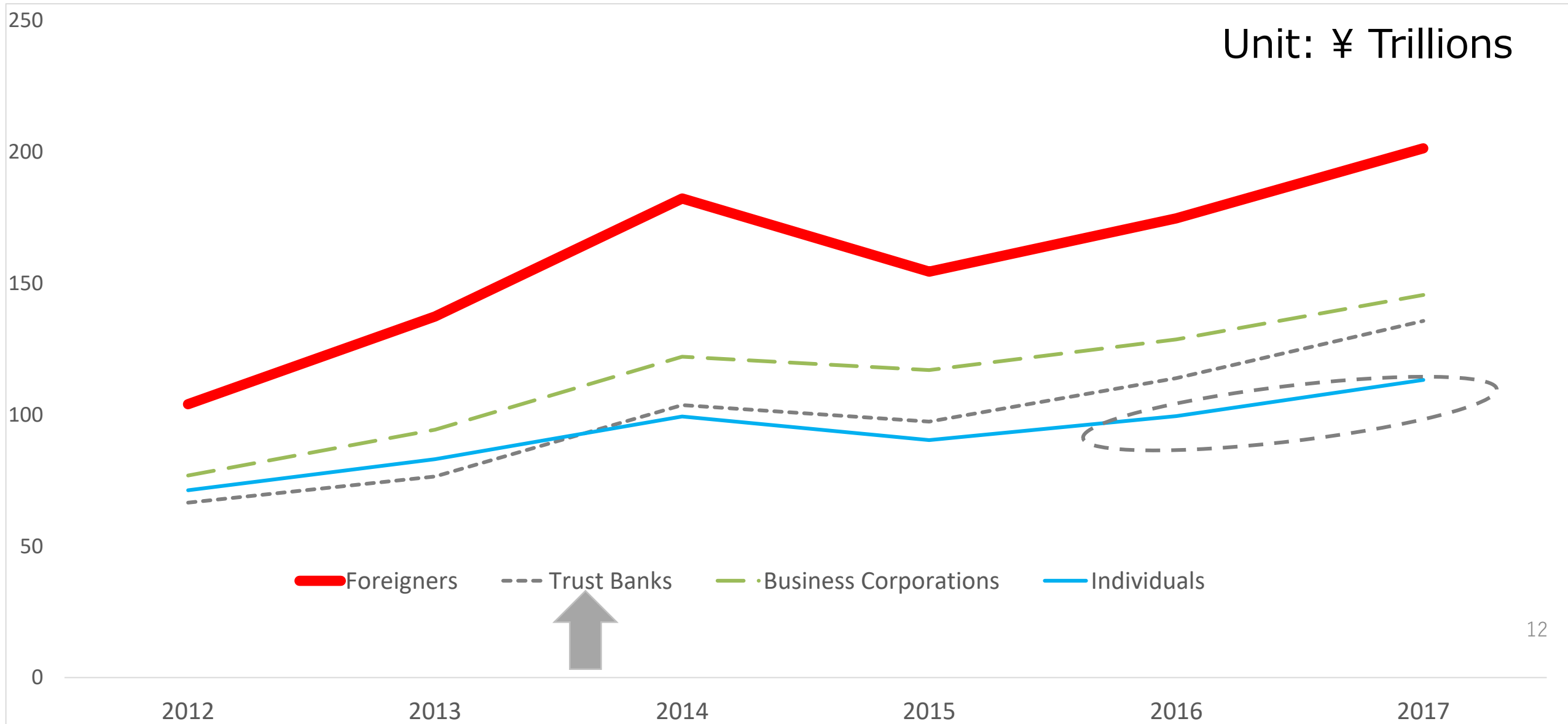
## Issue 2

# Small-Cap Firms' Stocks (Nikkei 225) Might be Overvalued



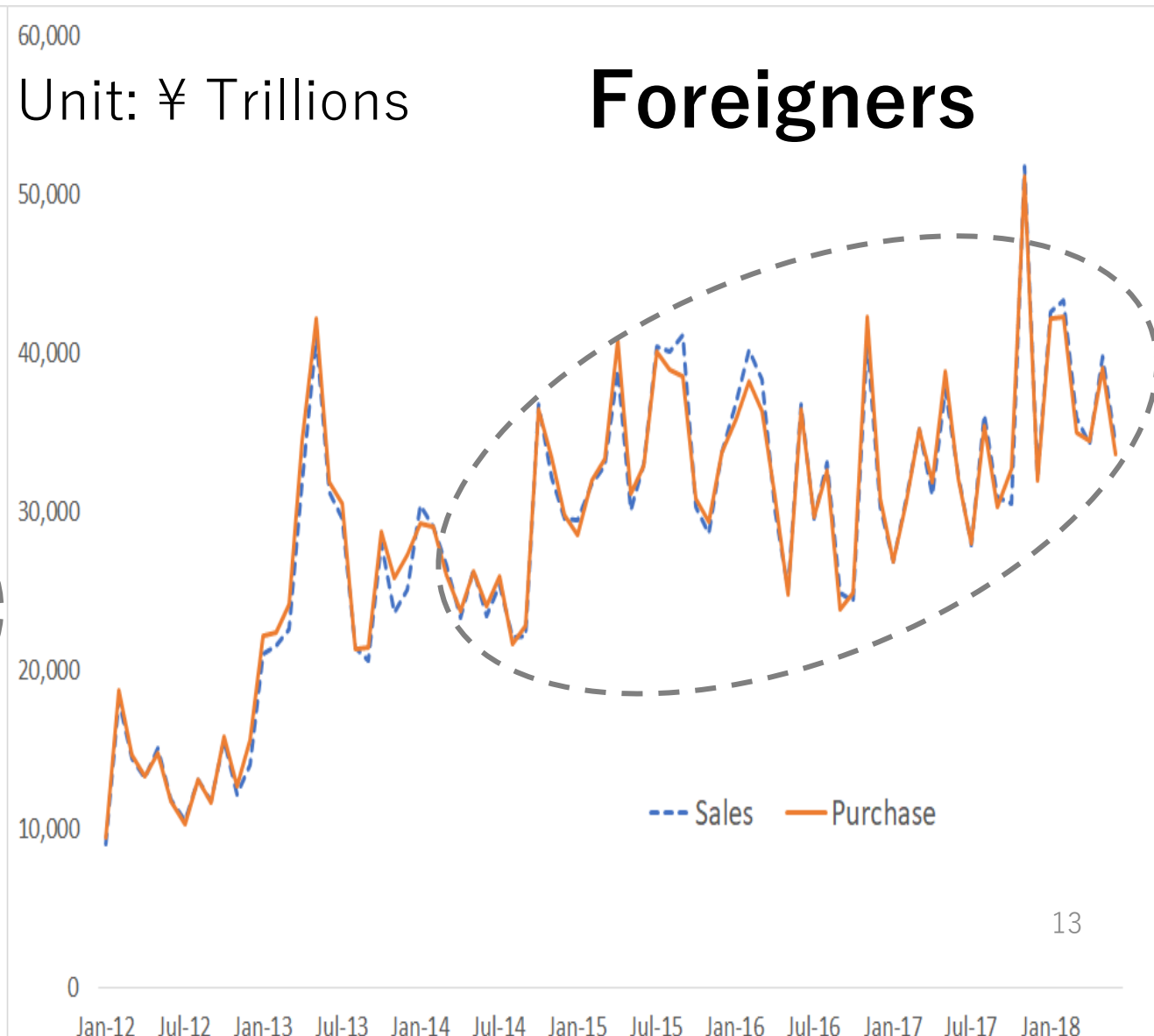
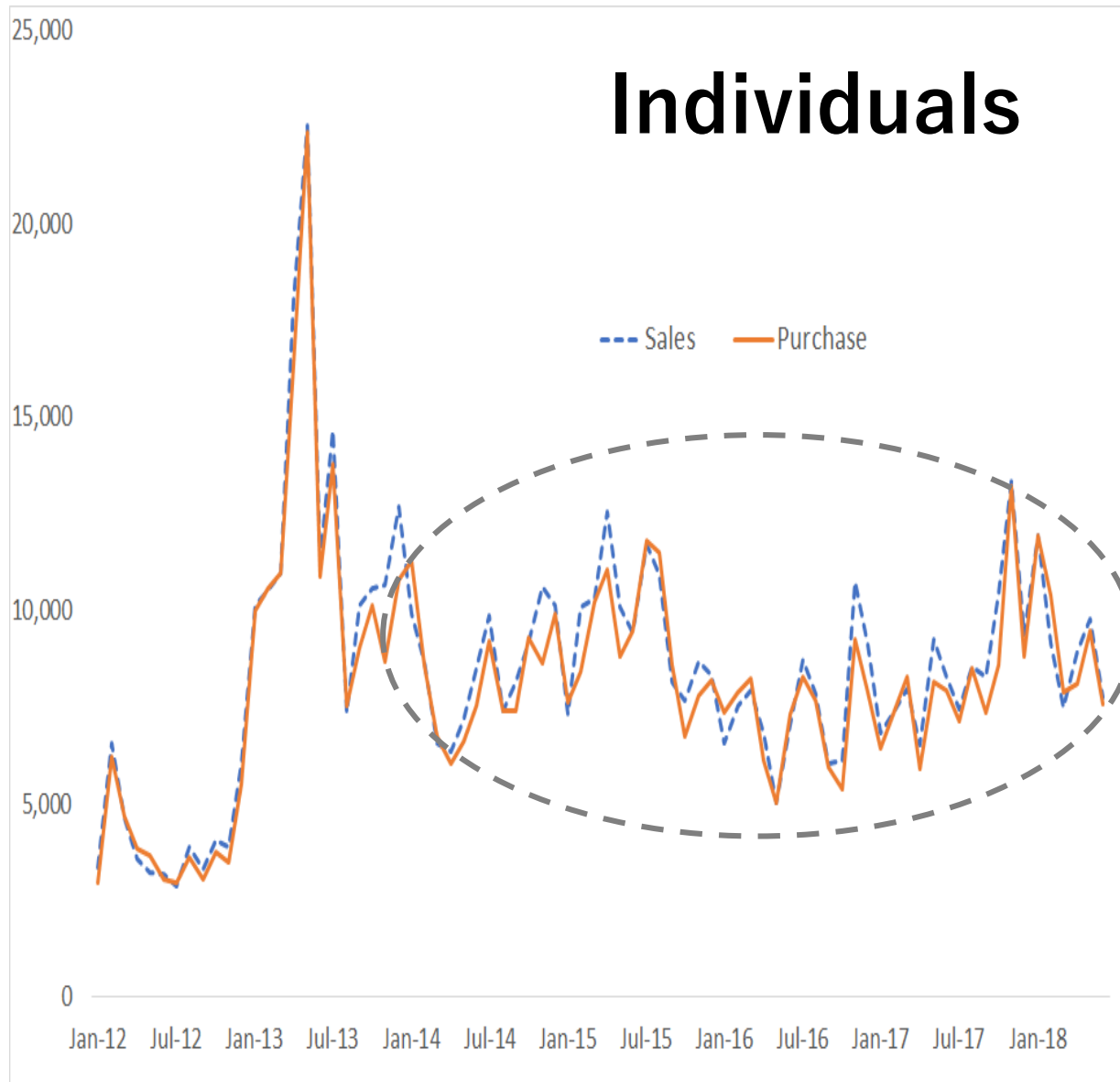
# Issue 3

## Large Stock Holdings by Foreign Investors



# Large Stock Transaction by Foreign Investors

## Individuals



## Issue 4

# BOJ becoming Top Shareholders

Name of Listed Companies	BOJ's Share (% of Total Stocks Issued)	BOJ's Share (% of Floating Stocks)
Advantest	19	43
Fast Retailing	18	70
Taiyo Yuden	17	28
TDK	16	25
Uni • Family Mart HD	15	38
Toho Zinc	15	23
Trend Micro	15	27
Comsys	14	31
Nissan Chemical	14	22
Konami HD	14	31

Source: Nikkei Newspaper (June 27, 2018)

## Issue 5

# Complicated Normalization Process

- Expanding the Target Range & Raising the 10-Year Yield Target
- Reducing JGB Purchases to ¥20 Trillion



- Reducing the JGB and ETF Purchases to ZERO
- Eliminating the 10-year Target



Raising Short-Term Policy Rate

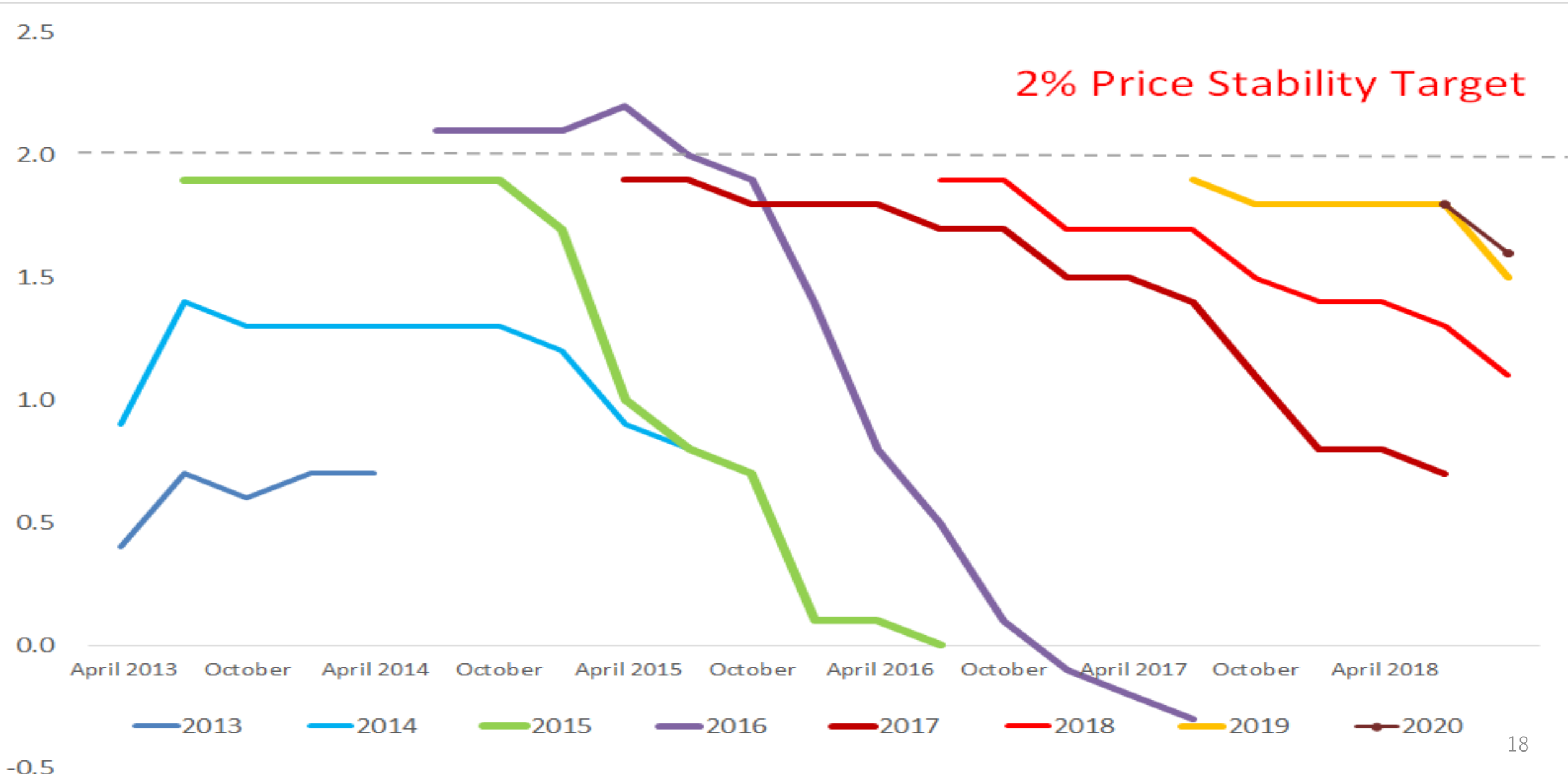
# **Part 2. Feasibility of the 2% Price Stability Target**



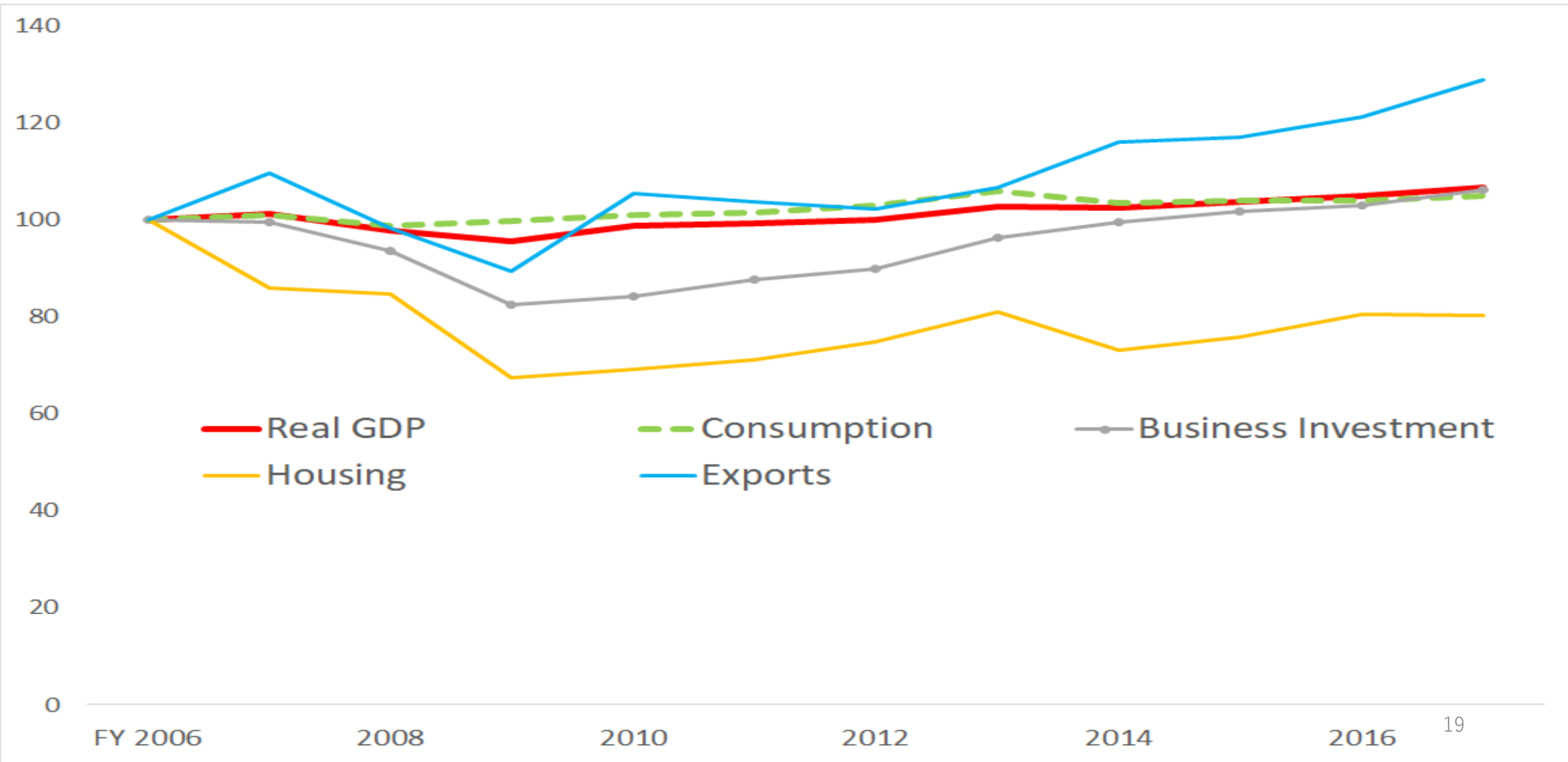
# CPI Inflation (exc. tax effect)

	CPI	Exc. Fresh Food	Exc. Food and Energy
2013	0.9	0.8	0.2
2014	0.8	0.8	0.5
2015	0.2	0.0	0.7
2016	-0.1	-0.2	0.2
2017	0.7	0.7	0.0
<b>AVERAGE</b>	0.5	0.4	0.3

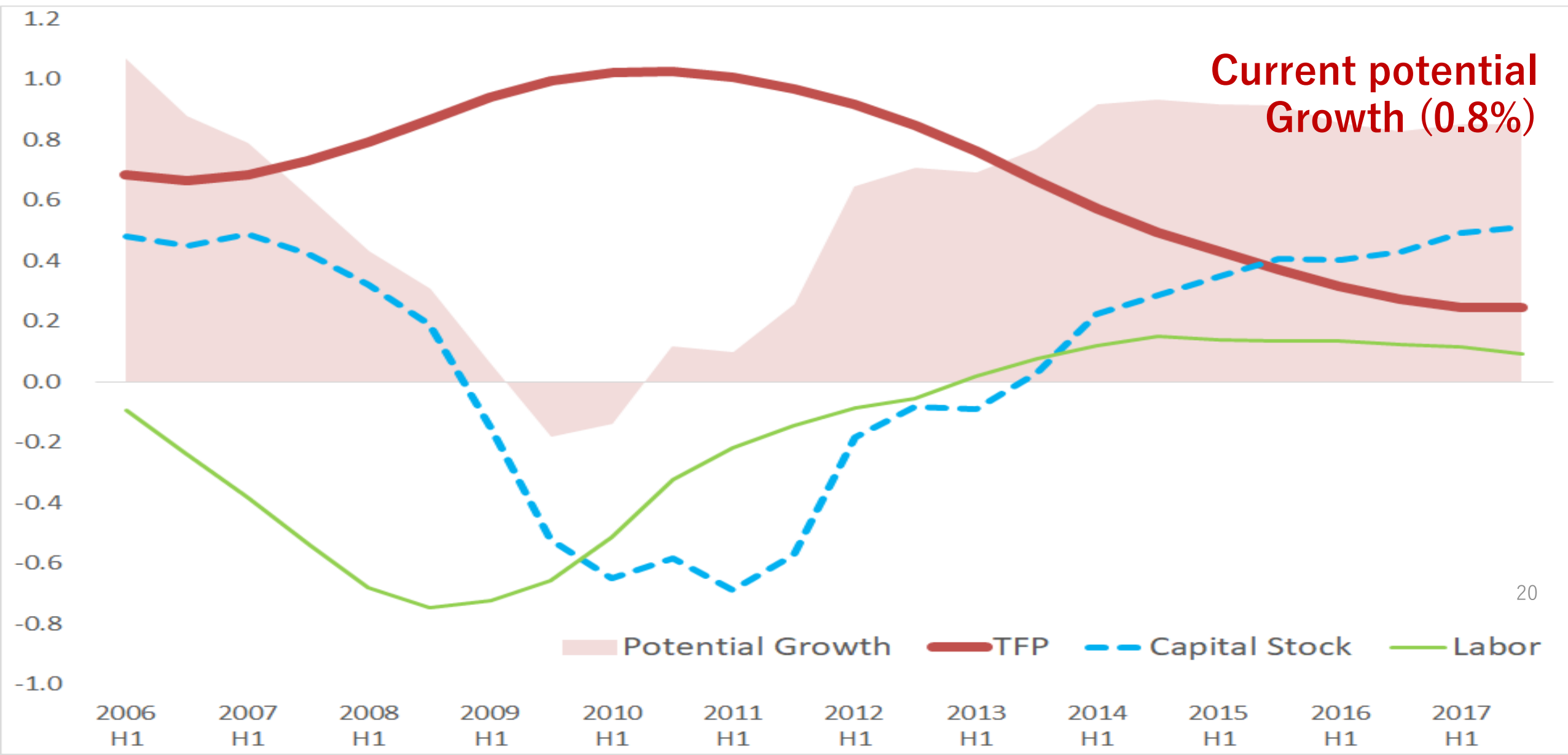
# BOJ's Inflation Outlook (Median)



# Real GDP and Composition (FY 2006=100)



# Potential Growth without TFP Contribution



# Sluggish Consumption

- Households **DO NOT** feel that **income has risen**. They **DO NOT** expect a higher income.
- **A third of population is more than 65 years old.**
- The majority of households **worry about the post-retirement life** (due to insufficient pensions or financial assets)

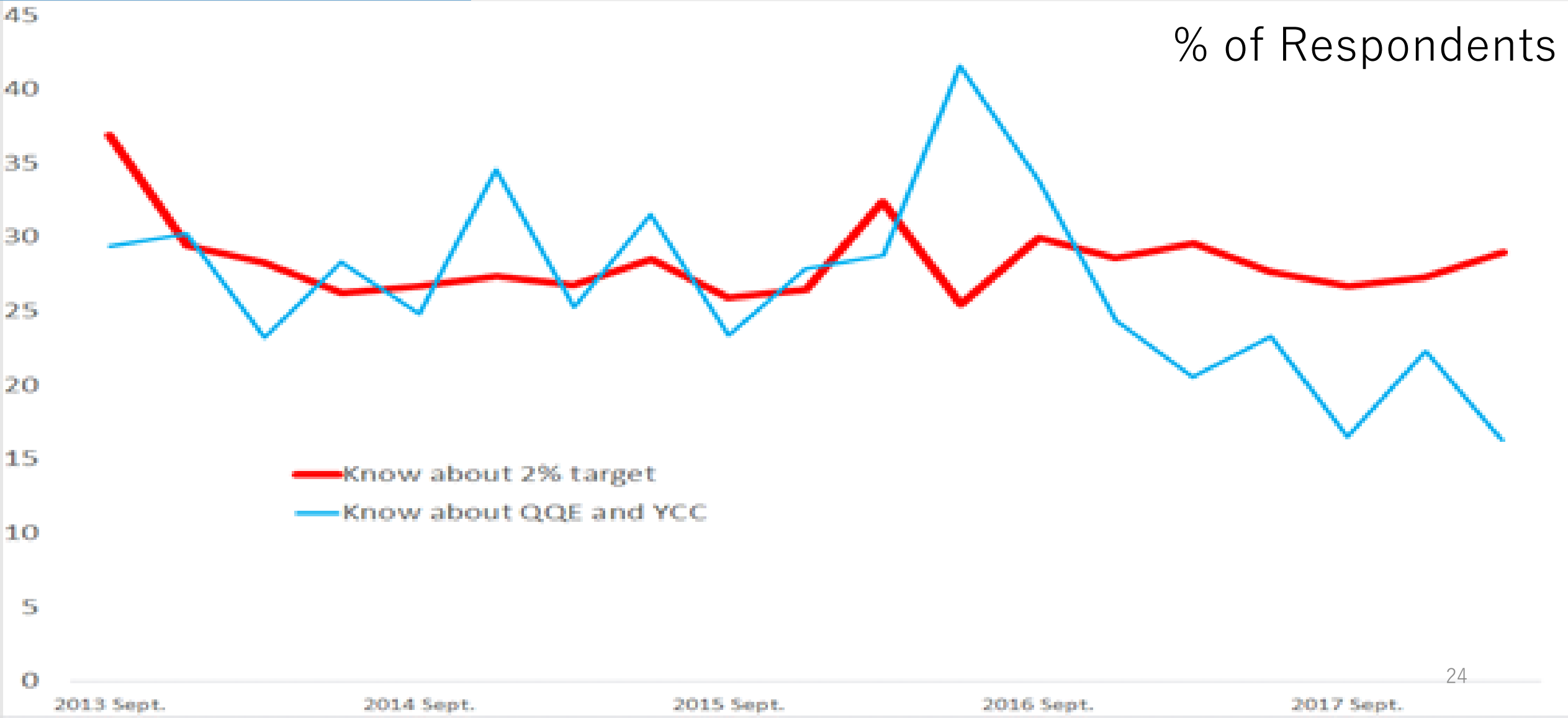
**Part 3. Searching for a New  
Monetary Policy Framework  
-- Case of Japan --**

# New Frameworks Discussed Globally

- Option 1: Raising the Inflation Target
- Option 2: Adopting the Price-level Targeting
- Option 3: Nominal GDP Targeting
- Option 4: Nominal Wage Targeting

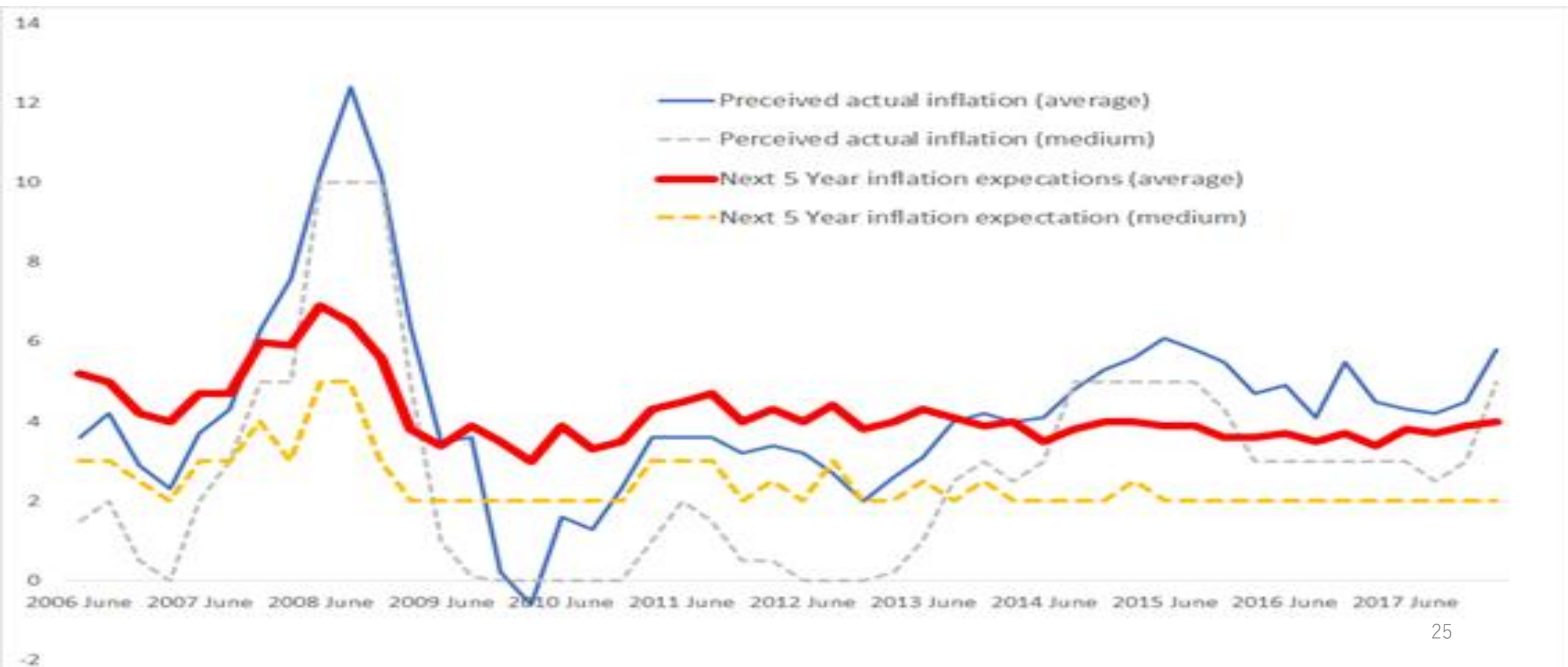
# Opt. 1: Raising Inflation Target

# Awareness of the 2% Target and Monetary Policy



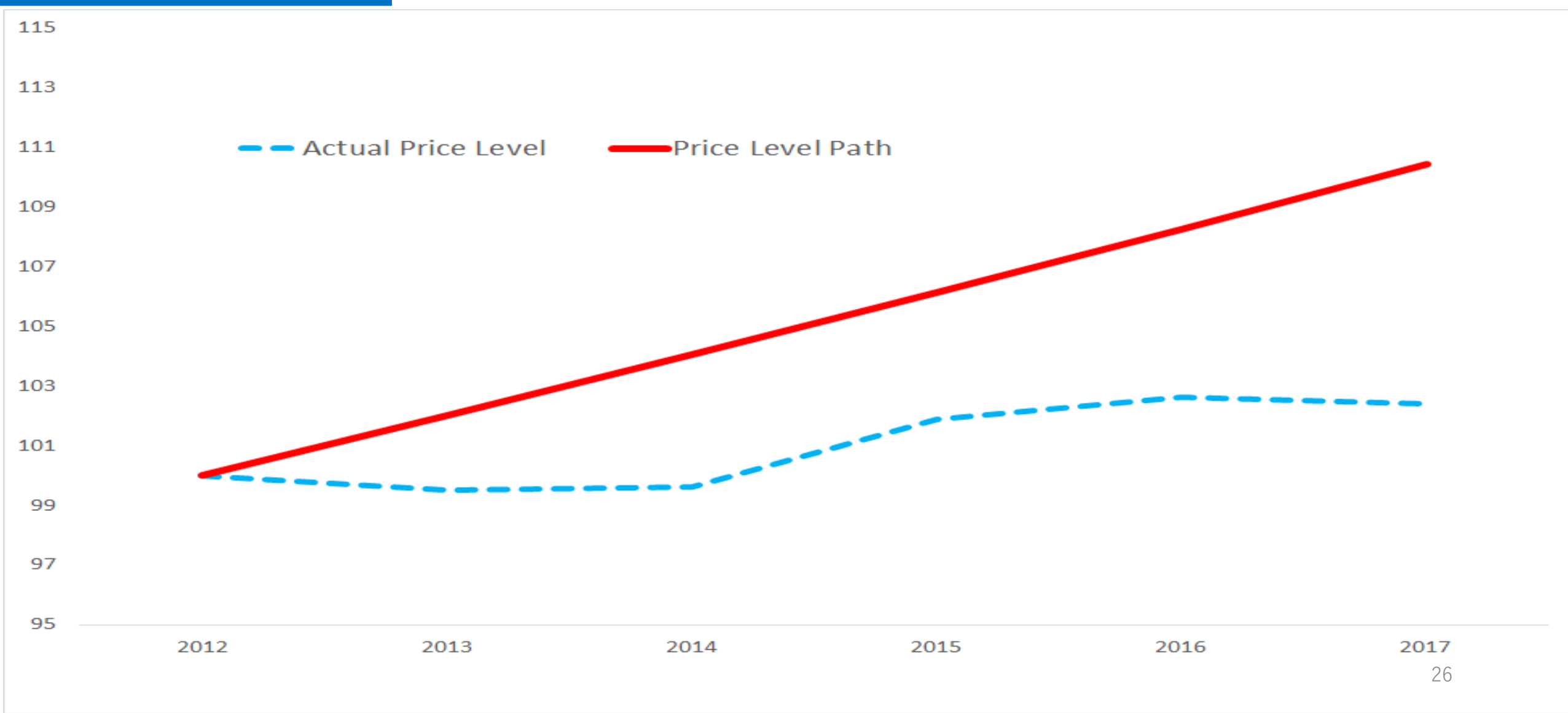


# Households' Perceived Inflation and Inflation Expectation



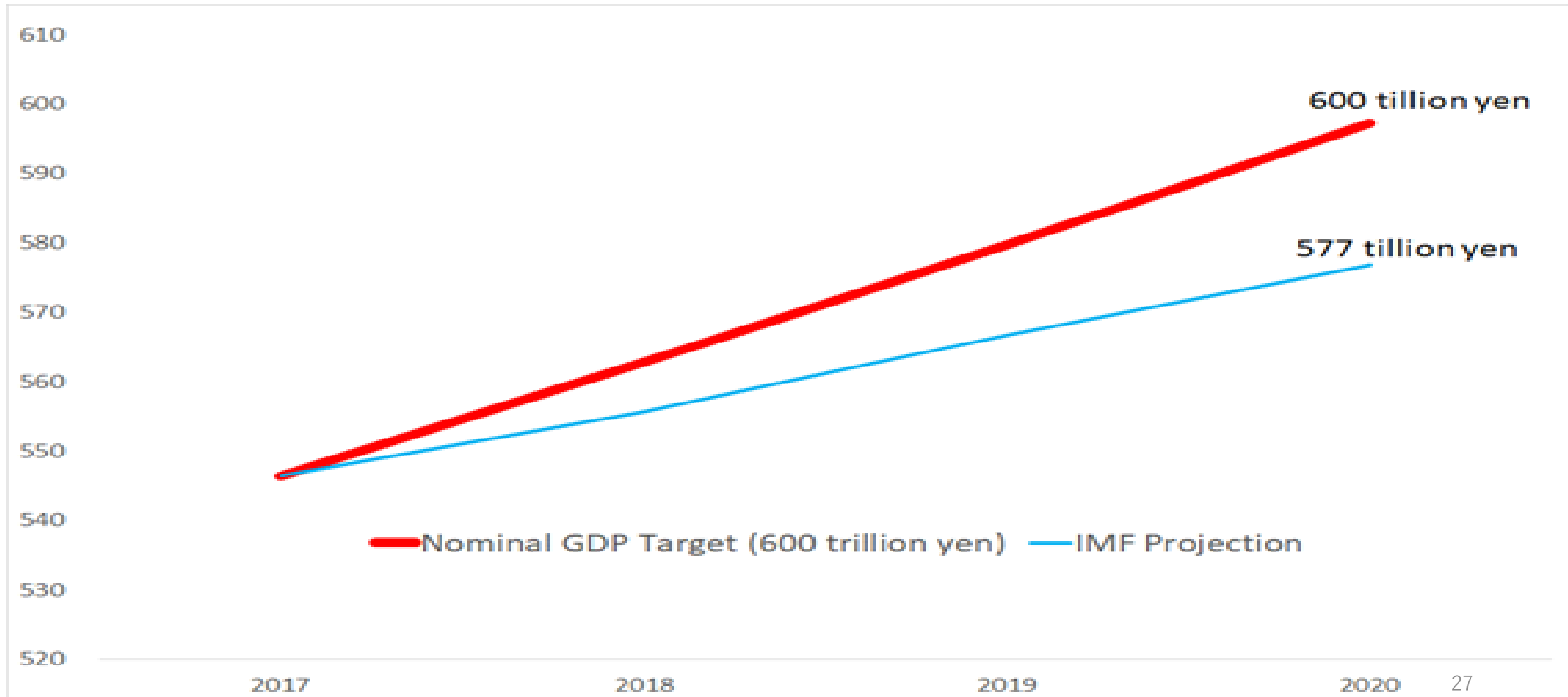
# Opt. 2 Price Level

# Desired and Actual Price Level (2012=100)



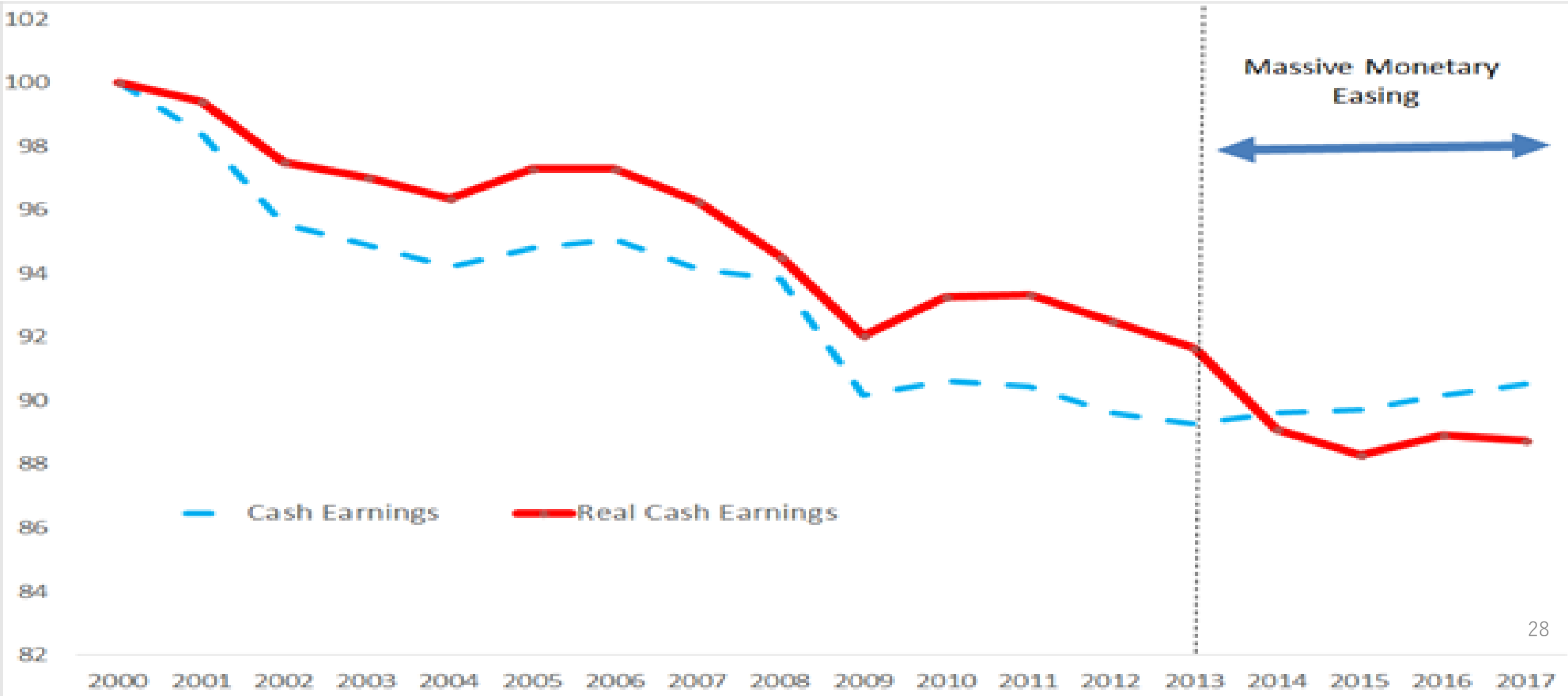
# Opt. 3 Nominal GDP

# Government Adopted Nominal GDP Target in 2015



# Opt. 4 Nominal Wage

# Nominal and Real Wage Levels (2000=100)



# Discussions Japan on the 2% Price Stability Target in Japan

## Three Options:

- Abandon?
- Reducing to 1%?
- Adopting  $\pm 1\%$  to the 2% price stability target (1-3%)

# Conclusions

- **Purchasing stocks as an unconventional monetary easing** has positive impacts on stock prices. At the same time, the effectiveness on inflation and market functioning needs to be carefully examined. **Exit policy** may be challenging.
- The difficulty to achieve the 2% price stability may reflect **structural problems** (e.g., low wage expectation, concerns about social security system)
- Various new monetary policy framework proposals to achieve higher inflation **may not be suitable in the cast of Japan**. Rather, **flexibility on the 2% price stability target may be desirable.**