

# Abenomics Approaching Its One-Year Mark

## Implementation and Progress



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# Abenomics: what should we expect?

The ex ante view

## Fiscal policy

(Stimulus, consumption tax)

## Monetary policy

(2 percent inflation, QQME)

## Growth reforms

(TPP, Diet session)

*Initiates recovery,  
growth becomes self-sustained.  
Over time, deficit and debt ratio  
decline*

*Inflation expectations rise, portfolio  
rebalancing picks up, core inflation  
starts rising*

*Investment recovery,  
employment and wages rise,  
labor supply and productivity  
increase*

Where are we? What's next?

Recovery, Fiscal  
sustainability



Inflation



Higher growth

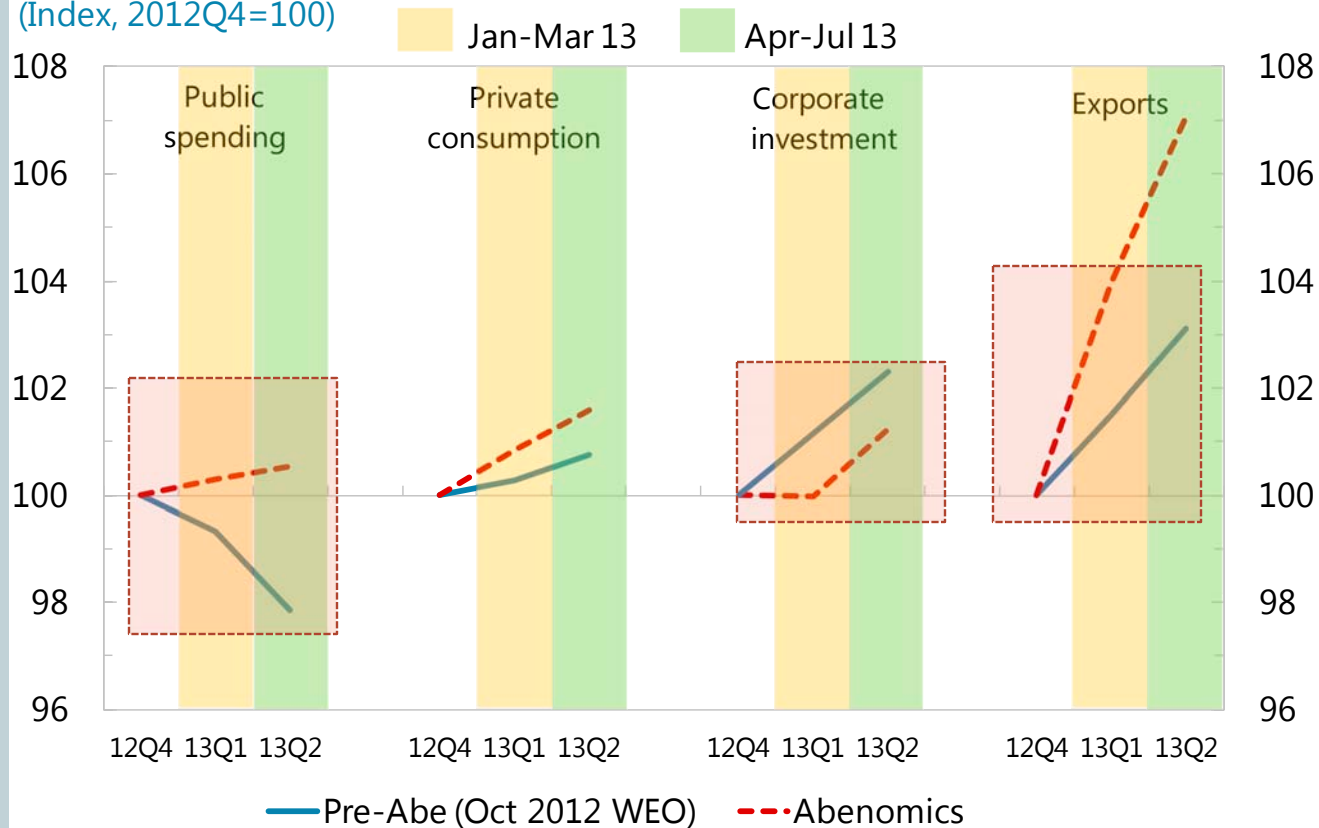


**Recovery  
on track?**

# Growth accelerated and mainly reflects monetary and fiscal stimulus

## Components of Real GDP

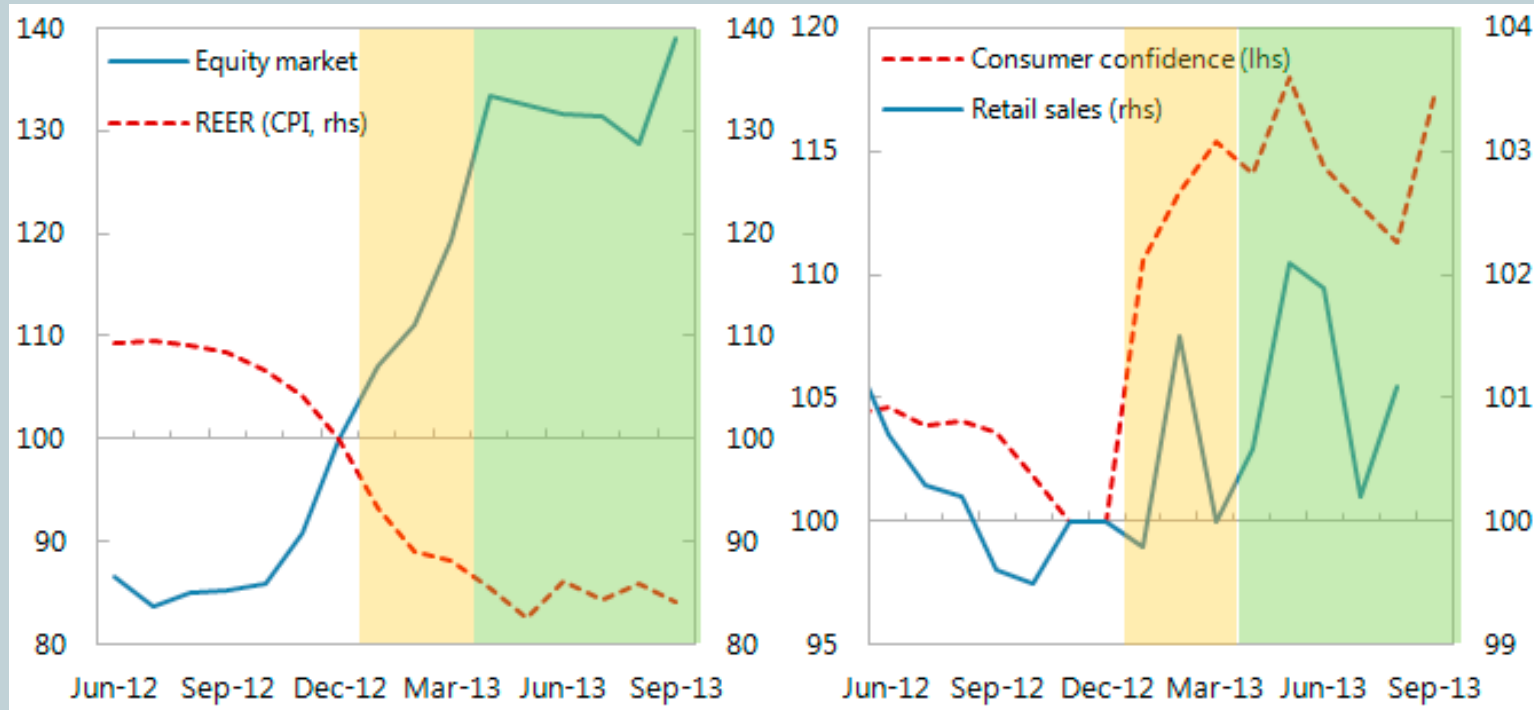
(Index, 2012Q4=100)



**Recovery  
on track?**



# Exchange rate and equity market steady and consumption has remained strong

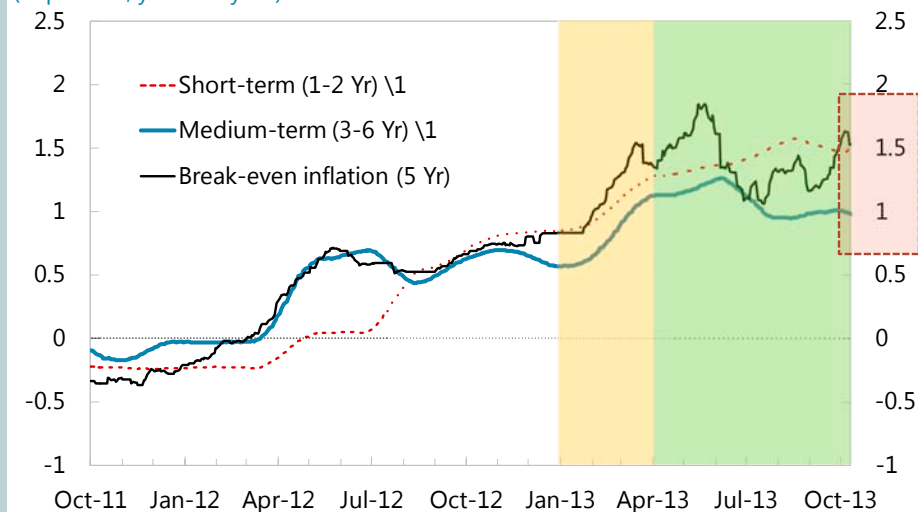


## Progress on Inflation?

# Inflation expectations have risen but are below the BoJ's 2 percent target

### Inflation Expectations

(In percent, year-on-year)

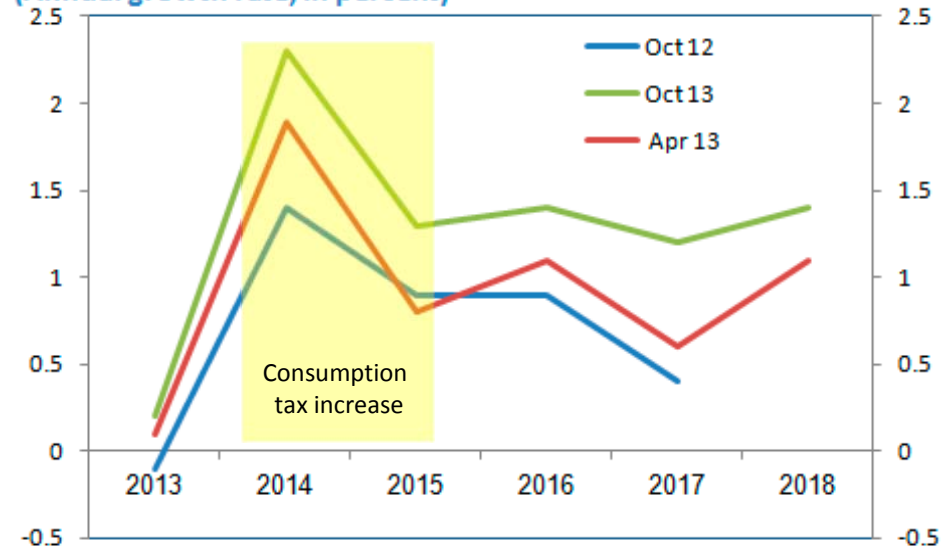


Source: Bloomberg.

1/ Expectations based on inflation swaps bid and ask prices.

### Consensus forecast

(Annual growth rate; in percent)



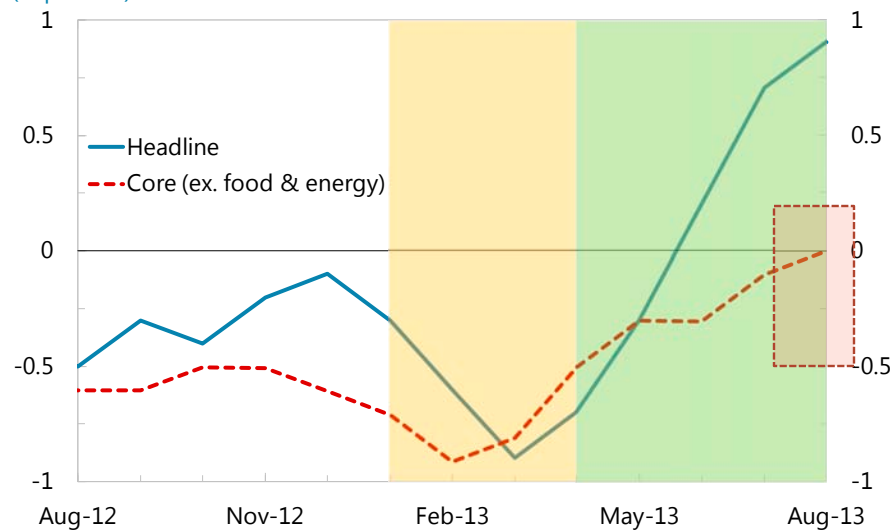
## Progress on Inflation?

# Inflation is up and mainly the result of higher import costs



### Year-on-Year Inflation

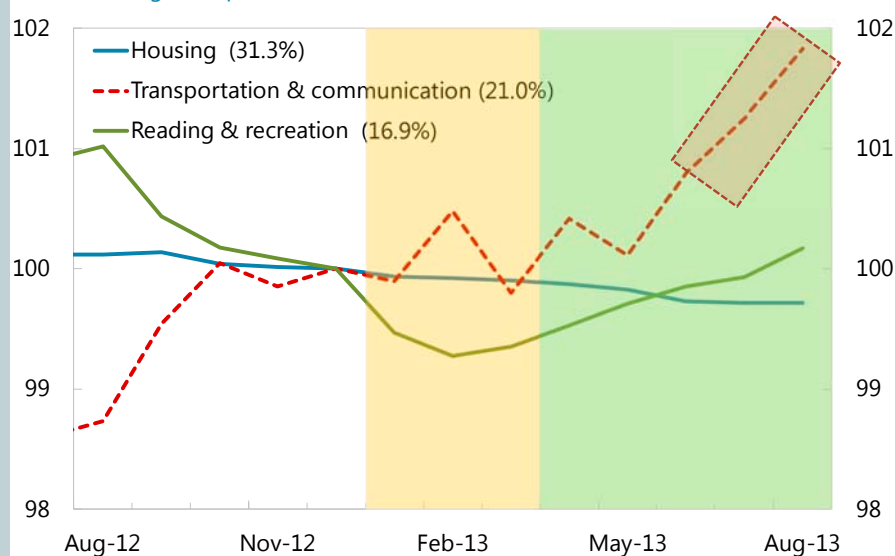
(In percent)



Sources: CEIC database; and IMF staff estimates.

### Core Core-CPI Index (SA): Key Inputs

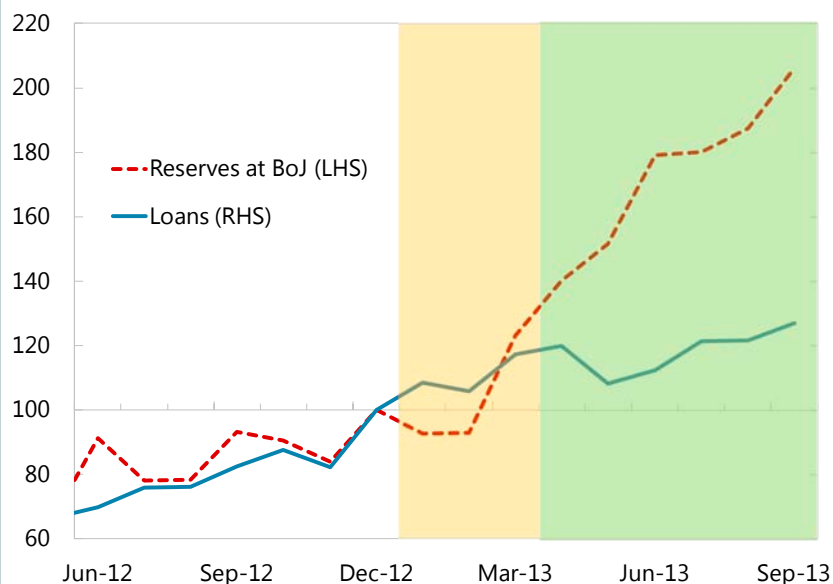
(Relative weights in parenthesis)



## Transition to sustained recovery?

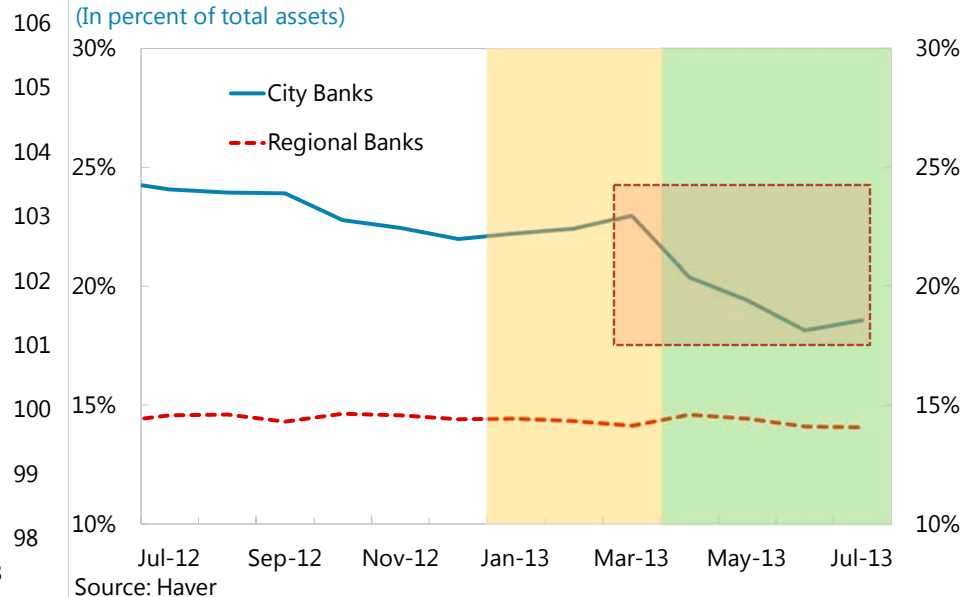
# Portfolio rebalancing has been gradual

### Banks Assets



### JGB Holdings of Japanese Banks

(In percent of total assets)

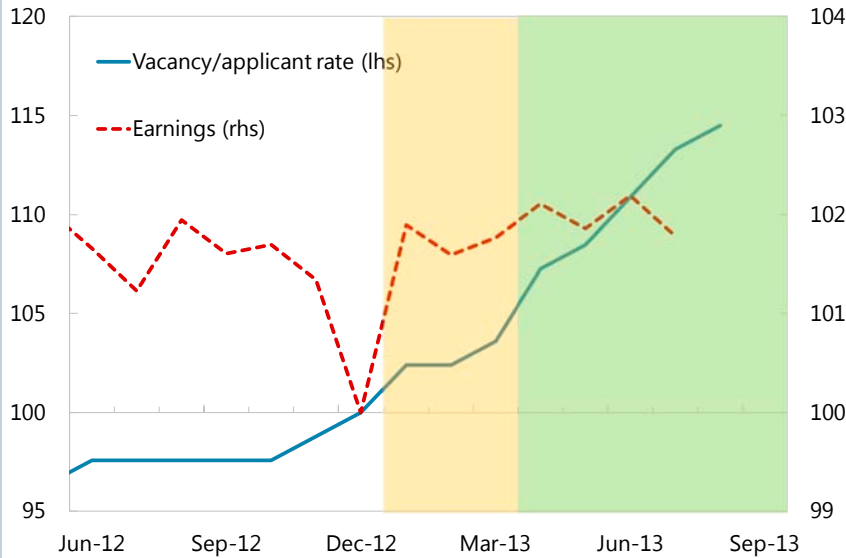


**Transition  
to sustained  
recovery?**

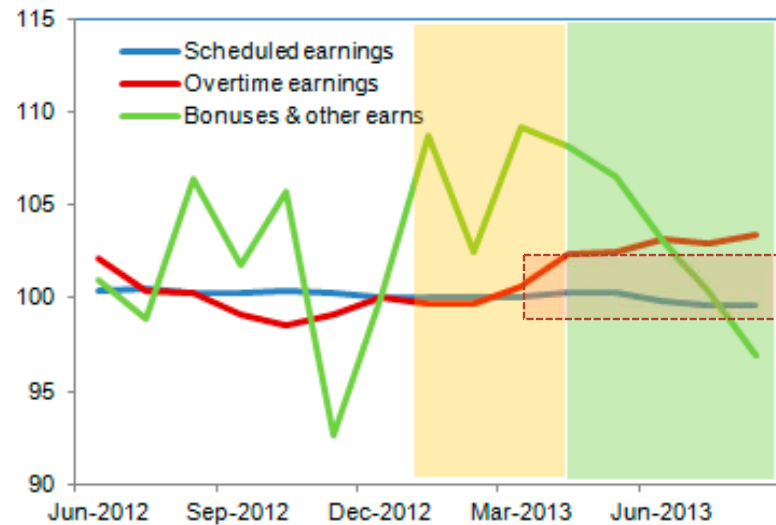
# Labor markets are tighter, but basic wages have not risen



**Labor Market**



**Cash earnings (all industry, sa)**





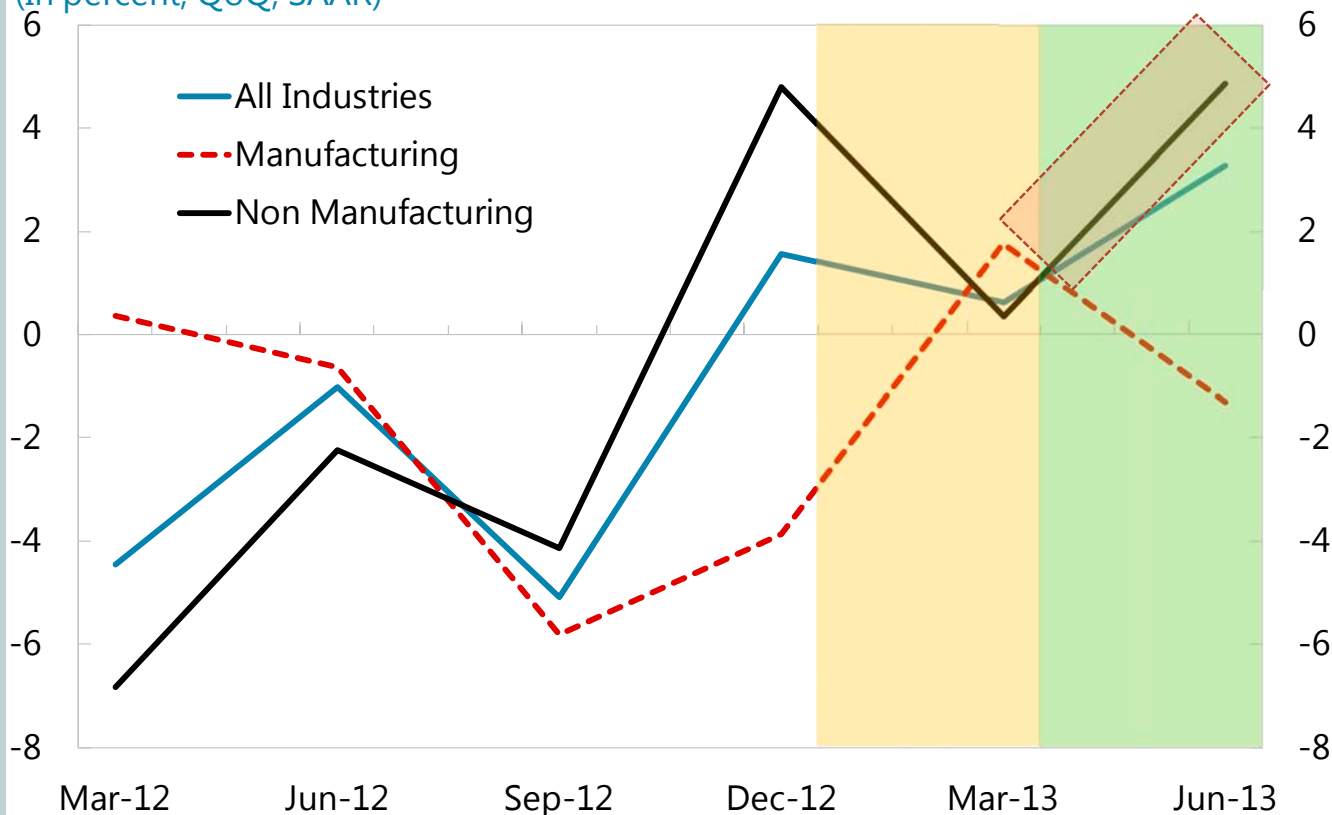
**Transition  
to sustained  
recovery?**

# Investment has picked up but needs to be sustained and broadened



## Private Investment in Plant and Equipment

(In percent, QoQ, SAAR)



Sources: MoF via CEIC

# Abenomics: comparing developments and expectations

## Fiscal policy

✓✓

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*Initiates recovery,  
growth becomes self-sustained.  
Over time, deficit and debt ratio  
decline*

## Monetary policy

✓

~

*Inflation expectations rise, portfolio  
rebalancing picks up, core inflation  
starts rising*

## Growth reforms

~

~

*Investment recovery,  
employment and wages rise,  
labor supply and productivity  
increase*

Where are we? What's next?

**Recovery, Fiscal  
sustainability**



**Inflation**



**Higher growth**



**Where are  
we?**



# Abenomics so far successful but now entering critical phase



## Growth needs to become self sustained

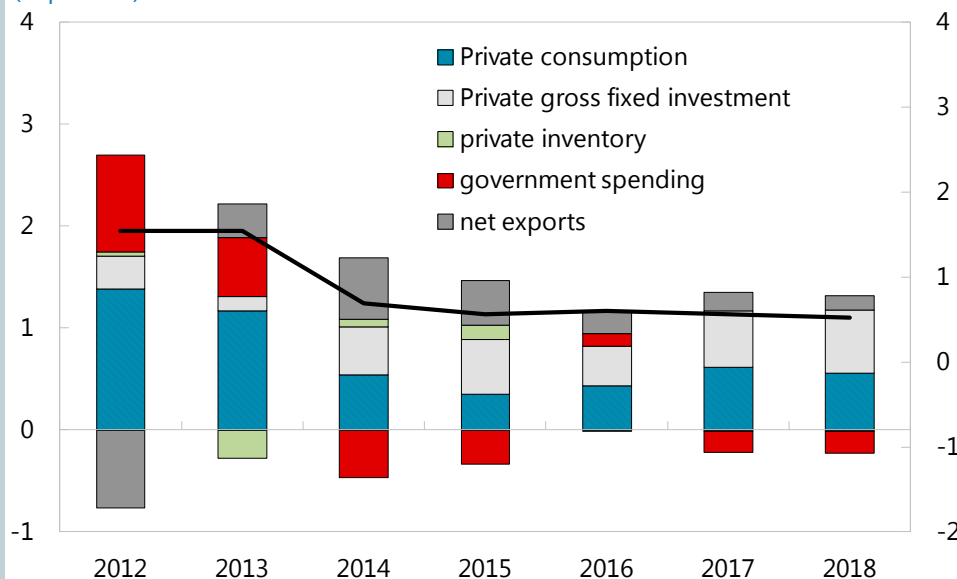
- necessary to meet inflation target and support fiscal reform over long-haul

## Challenges ahead

- *Structural reforms take time*  
**What can be done in short term?**
- *Fiscal reforms need to proceed*  
**How to minimize growth effects?**
- *Inflation/expectations need to rise*  
**How can monetary policy become more effective?**

### Components of GDP growth

(In percent)



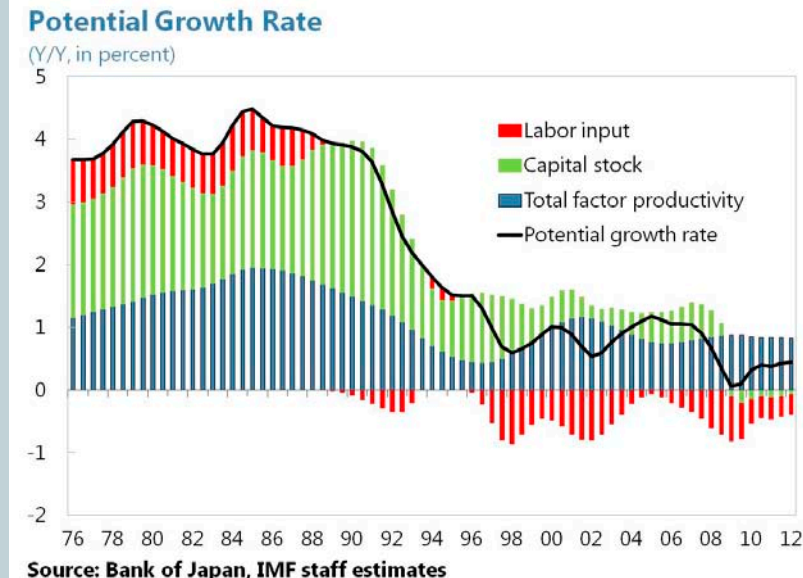
Source: IMF staff estimates

# What needs to happen?

## Broad-based growth reforms

### Adopt comprehensive growth reforms to raise potential growth

- Increase labor force participation and reducing labor market duality (IMF WP13/202)
- Deregulate agriculture and services
- Enhance role of the financial sector in generating growth (IMF WP 12/291)



### What can be done in the short term?

- **Immediate action** (signature initiative) to boost growth expectations: open up a specific sector, region, market
- **Consider measures** to encourage wage and investment growth. Options?

## What needs to happen?

# Proceed with fiscal reform, and adopt concrete long-term plan

## Rising public debt requires sustained attention

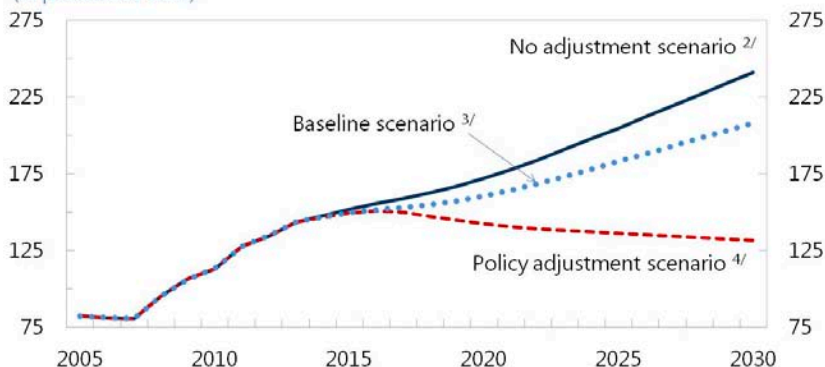
- Without further action, debt-to GDP ratio will increase further after 2015

## What can be done in the short term?

- Stimulus can be made effective
  - Temporary - no permanent commitment
  - Timely - fast acting
  - Targeted - effective in raising demand
- Clarity on corporate tax reform
- Outline fiscal measures beyond 2015 (e.g., increase of pension age to 70) to maintain confidence in public finances and create fiscal space

Japan: Net Public Debt <sup>1/</sup>

(In percent of GDP)



Sources: Cabinet Office; and staff estimates and projections.

1/ Net debt of the general government including the social security fund.

2/ No consumption tax increases but automatic withdrawal of fiscal stimulus.

3/ Consumption tax increases to 8 percent in 2014 and 10 percent in 2015.

4/ Policy adjustment scenario assumes a 11 percentage points of GDP improvement (baseline scenario +5½ points) in the structural primary balance between 2011 and 2020.

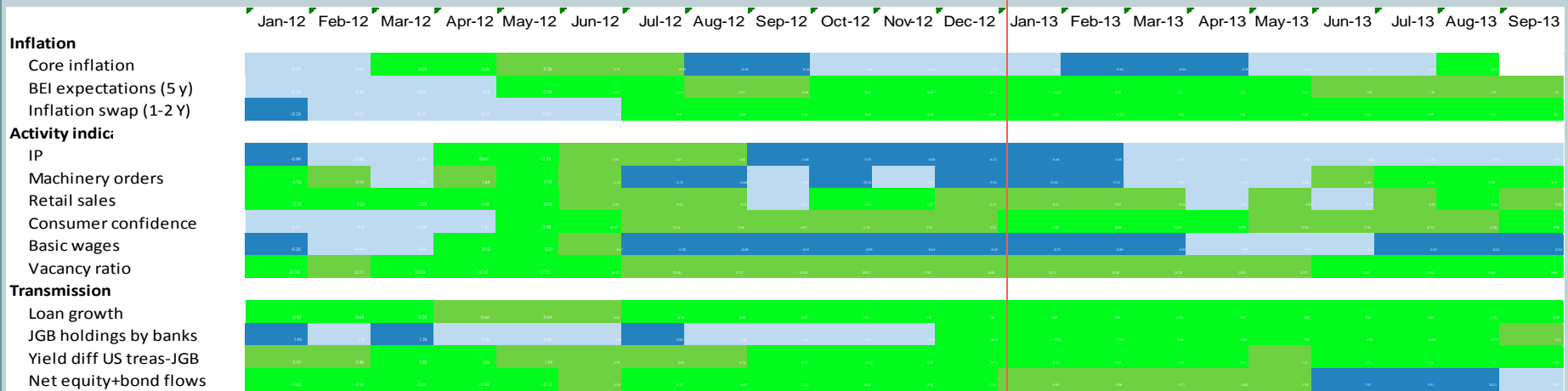
## What needs to happen?

# Maintain supportive monetary policy stance

## Difficult to track progress of QQME

- No historical benchmark for re-anchoring inflation
- Varied signals from tracking different indicators

Abenomics →



Note: Heatmap: blue-deflationary green-inflationary effect

## What can be done in the short term?

- Continued clear communication on commitment to achieve 2 percent inflation
- Prepare for the eventuality of more easing including through more forward guidance.



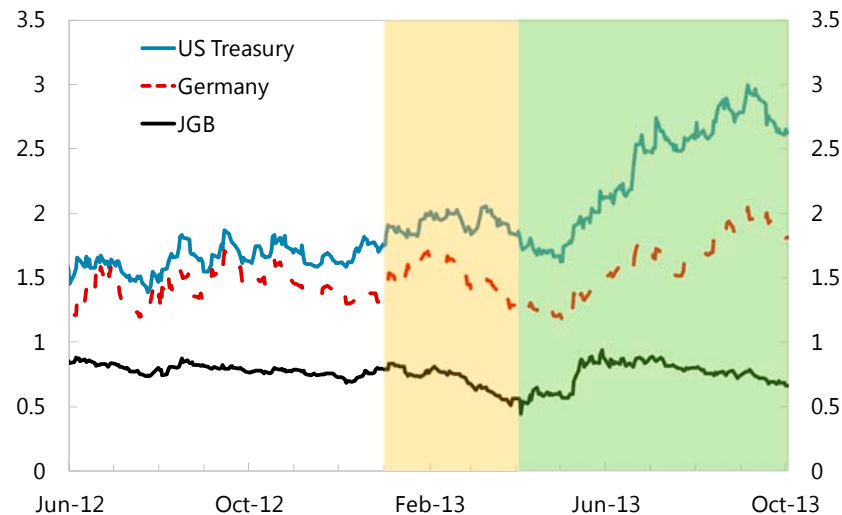
**THANK YOU**

# Bond yields have remained low and volatility has declined



## 10-Year Sovereign Bond Yields

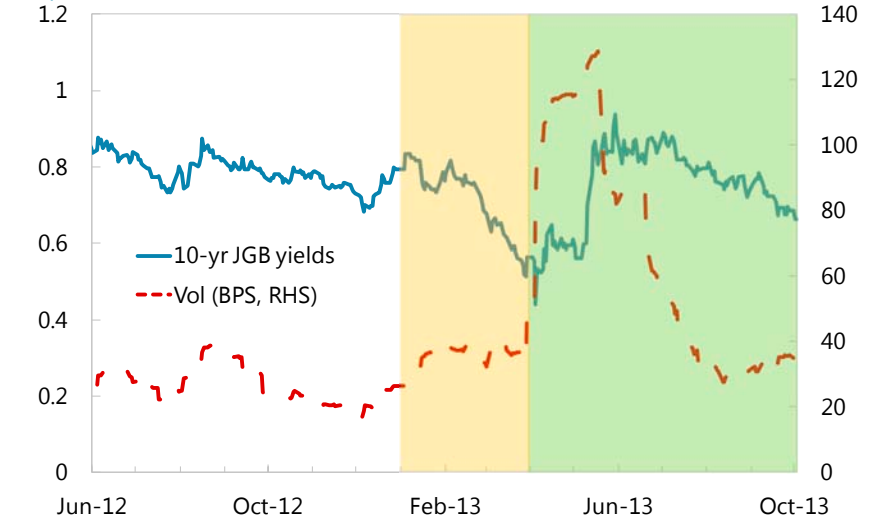
(In Percent)



Source: Bloomberg.

## Japan: JGB 10-Year Yields and Volatility

(In percent)



Source: Bloomberg.

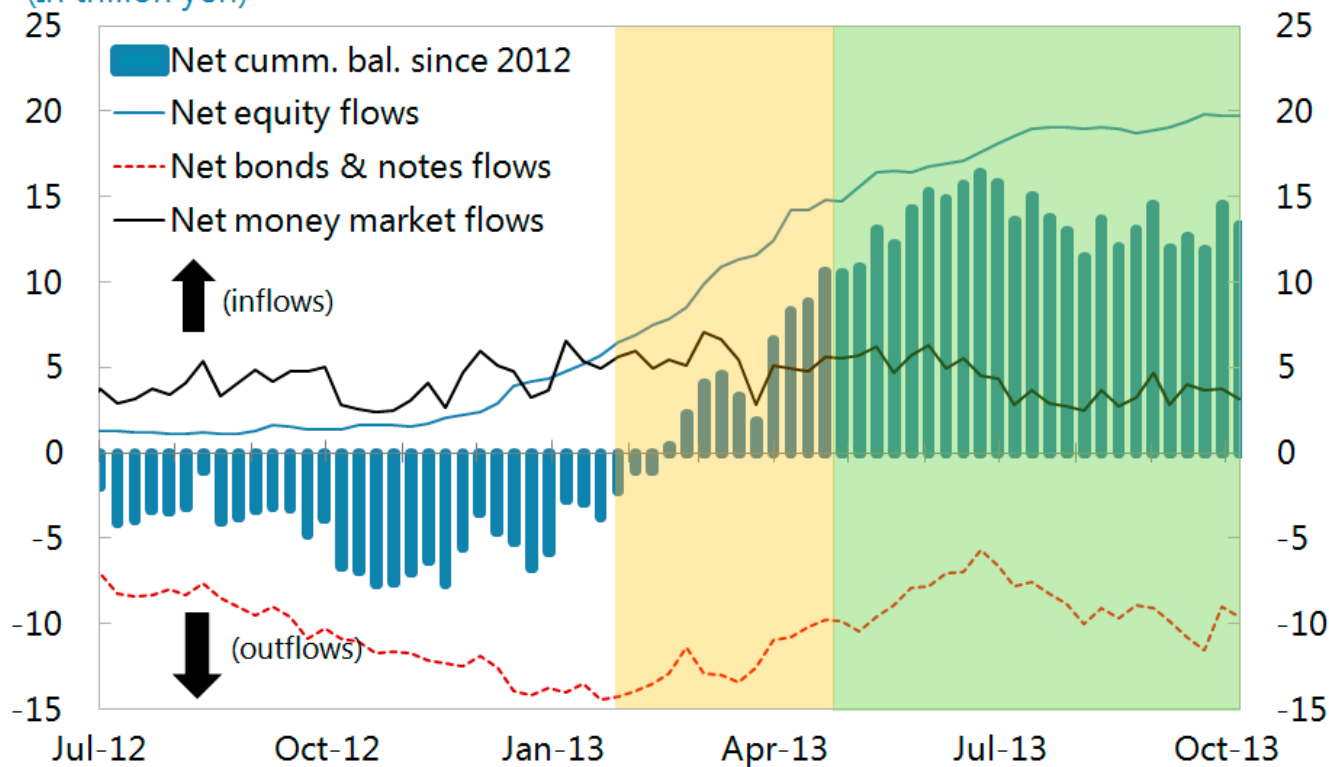


# Capital flows into bond and equity markets



## International Transaction in Securities <sup>1/</sup>

(In trillion yen)



Source: Japan Ministry of Finance.

<sup>1/</sup> Cumulative positions since January 2012.