

# Flash Comment

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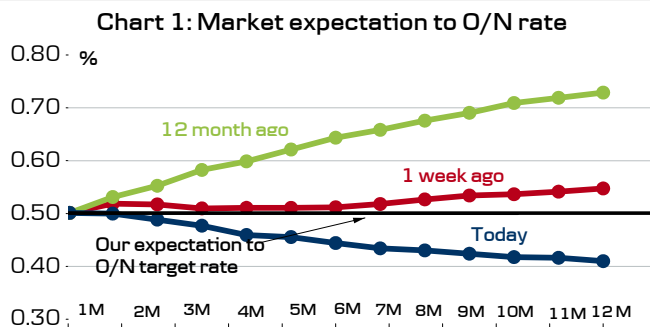
## Japan: BoJ leaves interest rates unchanged as expected

The Bank of Japan (BoJ) as expected left its leading O/N target rate unchanged at 0.5% in a unanimous decision. The statement on monetary policy was broadly unchanged compared to its September statement. BoJ believes growth will remain sluggish for the time being but will eventually recover as the impact from higher commodity prices abates and the global economy moves out of its current deceleration phase. Not surprisingly, it continues to see considerable downside risk to the economy from the current financial crisis. BoJ still believes it has to be aware of upside risk inflation due to changes in inflation expectations. It also still believes that monetary policy is very accommodative and will eventually have to be tightened if the downside risk to the economy decreases substantially. However, that is certainly not the case at the moment. Hence, the main message continues to be unchanged interest rates for the foreseeable future.

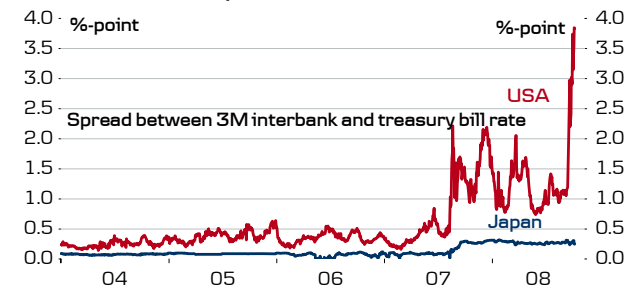
If anything we believe BoJ could soften its view on growth and inflation in the coming months – possibly at the October 31 monetary policy meeting, when BoJ will release revised GDP forecasts. The August numbers were overall very poor and industrial activity seems to be declining and not flat as BoJ currently believes.

Although BoJ like most other central banks is flooding the money market with liquidity, the Japanese money market is still doing much better than the US and European money markets (see chart 2) partly due to the significant deposit surplus in most Japanese banks. Hence, we do not believe that there is the need for extraordinary measures to stabilise domestic money markets like in Europe and the US besides increasing the liquidity in the USD market.

There has been no market reaction to BoJ's interest rate decision. However, during the past week, money markets have started pricing the possibility of a rate cut. The 12M forward O/N rate in the past week has declined to 0.40% currently from 0.54% (see chart 1). We still believe BoJ will be on hold for the next year, but we are certainly not ruling out anything given the current state of the financial markets. From a macroeconomic perspective, the impact of a rate cut will probably be limited. If BoJ is going to cut rates, we believe it is most likely to happen in a co-ordinated international effort to stabilise financial markets.



**Chart 2: Direct impact from credit crisis still modest**



# BoJ View of the Economy

## October 2008

“Economic growth has been sluggish due to the effects of earlier increases in energy and materials prices and weaker growth in exports and will likely remain sluggish for the time being as a slowdown in overseas economies becomes more evident. Although there are substantial uncertainties, the economy, in the longer run, is expected to return gradually onto a moderate growth path as the effects of earlier increases in commodity prices abate and overseas economies move out of their deceleration phase.”

“With regard to risks factors, strains in global financial markets have intensified in the wake of failures and rescues of U.S. and European financial institutions and there are downside risks to the world economy.”

[Complete October Statement of Monetary policy](#)

## September 2008

“Economic growth has been sluggish against the backdrop of high energy and materials prices and weaker export growth. While growth will likely remain sluggish for the time being, it is expected to return to a moderate growth path as commodity prices level out and overseas economies move out of their deceleration phase.”

“With regard to risks factors, tensions in global financial markets have increased and there are downside risks to the global economy.”

## Forecast of policy board members, July 2008

% y/y		GDP	DB	CGPI	CPI	DB
Fiscal 2008	Median	1.2 (1.5)	<b>0.4</b>	4.8	1.8 (1.1%)	<b>1.8</b>
	Range	1.2-1.4 (1.4-1.6)		4.7-5.0 (2.4 2.8)	1.7-1.9 (0.9 to 1.1)	
Fiscal 2009	Median	1.5 (1.7)	<b>1.6</b>	1.8 (1.5)	1.1 (1.0)	<b>0.6</b>
	Range	1.4-1.6 (1.6-1.8)		1.8 - 2.0 (1.3-1.8)	1.0-1.2 (0.8-1.0)	

**Note:** CGPI= domestic corporate goods prices, CPI= consumer prices excluding fresh food, fiscal year = April-March. Numbers in parentheses are previous BoJ forecast. Bold numbers are current Danske Bank Forecast

**Source:** Bank of Japan, Outlook for Economic Activity and Prices and July policy statement.

Name	Position	Policy stance	Appointed
Masaaki Shirakawa	Governor	Neutral	Apr. 2008
Kiyohiko Nishimura	Deputy Governor	Dove	Mar. 2008
Vacant	Deputy Governor	-	-
Miyako Suda	Board member	Hawk	Apr. 2006
Atsushi Mizuno	Board member	Hawk	Dec. 2004
Tadao Noda	Board member	Hawk	Jun. 2006
Seiji Nakamura	Board member	Neutral	Apr. 2007
Hidetoshi Kamezaki	Board member	Dove	Apr. 2007

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