

Japan fiscal boost coming?

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The damage done by Typhoon Hagibis, the tropical cyclone that hit Japan this month, to Japanese private residences and public infrastructure raises the likelihood of sizable fiscal stimulus coming within the next three-to-five weeks. At the same time, Japanese insurance companies are poised to prepare for rising cash claims and begin raising liquid balances; and banks are poised to see a pick-up in home construction and business loan demand. For Yen public markets, the net effect in our view will be a steepening of the Japanese yield curve, which in turn should be positive news for banks and other “value stocks” in the equity market.

A 2-3 trillion-yen stimulus package

Prime Minister Shinzo Abe and his team are extremely “trigger happy” for added fiscal spending, with the potential negative from the 1 October consumption tax hike already threatening the sound economic policy management credentials of the cabinet. Now the need for fast and decisive government action has become obvious and urgent. Countermeasures and extra fiscal spending of around 2-3 trillion yen, about half-a-percent of Gross Domestic Product (GDP), are likely to be announced before end-October/early-November.

Importantly, the expected added fiscal stimulus will raise the effectiveness of Bank of Japan (BoJ) policy: a new direct transmissions channel will be opened-up for BoJ liquidity to actually reach the real economy. Make no mistake, in Japan fiscal dominance is a reality; and “New Monetarism” is not a theory but concrete policy practice.

All said, Japanese equities are moving towards a potentially very powerful sweetspot: the US-China trade war resolution should boost the fortunes of exporters; and the new fiscal stimulus could boost domestic demand in general, banks and value stocks in particular.

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