

Japan Is Ready for Trump

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The initial risk-off shock reaction in Japanese markets notwithstanding, I think Japan is actually well prepared for a Trump presidency. In my view, Team Abe will surprise us with a speedy and constructive counter policy—a sizable fiscal “war chest” has been put aside already, de facto monetized by the Bank of Japan’s (BOJ) commitment to cap borrowing costs at 0%.

Moreover, once the dust settles and the White House top-down economic policy leadership is re-established in Washington, corporate Japan could well benefit—approximately 14% of the profits that Japan Inc. makes comes from North America-based production, so Trump’s promise of a sizable cut in corporate taxes could well add at least a couple of percentage points to Japanese earnings next year.

Be Prepared...

Team Abe has been in power for almost four years, is well-coordinated and has a two-thirds supermajority in parliament. Arguably, it is the most stable and coordinated policy regime in the world. And as an added bonus: unlike Europe, Abe’s financial regulators preside over a stable and well-capitalized banking system.

....and Act

The ability and willingness to act are based on Team Abe’s commitment to massive fiscal countermeasures—¥28 trillion, or 5.5% of GDP, were ratified by Abe’s cabinet in early August. In short: the war chest has been put together ahead of time. No question that “Trump risk” was a key motivator. Now, should deflation risks rise due to Trump, an added fiscal boost can come quickly and is likely to be monetized by the BOJ.

What about the Yen?

Yesterday’s risk-off reaction—yen strength, Nikkei crash—is a standard-procedure market reaction. Whether it turns into a genuine crash depends on Trump’s ability to demonstrate policy leadership. If, as I suspect, he presents a policy team with credible professionals over the next four to six weeks, risks of a sustained rot should recede. The sooner the deal maker and pragmatic capitalist replaces the divisive campaigner, the better.

For currencies, a key force should be U.S. trade policy. If America turns protectionist by imposing tariffs on imports, a structural downshift in the dollar is likely. Here, in my personal view, the hope is that President Trump turns out to be a pragmatist and deal maker. U.S. industry, which relies on the rest of the world for almost half its sales, is poised to work overtime to prevent a Washington-led global trade war.

Note here that not proceeding with the Trans-Pacific Partnership (TPP) is not the start of a trade war. It merely retains the status quo—no added benefits but also, on its own, no added damage. As discussed, tariffs or no tariffs are the litmus test.

Meanwhile, Trump’s election promise of ending tax inversions and incentivizing repatriation of overseas earnings should, at the margin, add to the demand for dollars.

Domestic Agenda

In Japan, the TPP legislation is poised to pass parliament regardless. This is because the added support for farmers and regional economies is an integral part of Team Abe's domestic policies, with or without the potential trade liberalization.

Meanwhile, Abe's personal ambition of rewriting Japan's constitution to allow greater self-dependency and independence may be turbo-charged by a Trump presidency. Ditto for chances of a successful Abe–Putin meeting later this year.

For next year, Team Abe will have to find a new way to engage with China more constructively. However, here Japan is likely to wait and see how President Trump will deal with China. In my personal view, the more hardline Trump is, the more likely a Japan–China rapprochement becomes.

Important Risks Related to this Article

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