

The Next BOJ Governor – The Agenda

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Japanese prime minister Shinzo Abe is about to appoint the next Bank of Japan (BOJ) governor. More than anything, the appointment will define the future of Japanese finance and markets. There is little doubt that for most investors at home and around the globe, much of the success of Abenomics is primarily due to Kurodanomics. In my view, BOJ governor Haruhiko Kuroda deserves a second term, if he wants it. Current market volatility has probably increased Kuroda's chances of becoming the first BOJ governor since 1960 to get a second term.

Let's keep aside the “who” for now and focus on the “what.” Yes, there is much to do for the next BOJ leader.

- The current global market rout will have to be addressed sooner or later, putting to the test not just soft communication skills but the next governor's willingness to use hard-currency power: Will the BOJ's ¥6 trillion ETF “war chest” be used more aggressively? So far in the downdraft, the BOJ has been notably silent.
- Structurally, the BOJ's pro-growth credentials will need to be asserted against mounting fears of a 2019/20 Japan recession. Recession? Yes, markets will not deny the combined negativity of the next consumption tax hike (October 2019) and the pre-Olympic construction boom-turning-bust (typically, activity peaks about 12–18 months before the start of the games, i.e., next spring). Those two negatives will start to dominate Japan's 2019/20 forecasts before long.
- An added challenge for the next governor: The current BOJ board expects the 2% inflation target to come into sight at just about the same time when fears of the combined negativity from tax hikes and pre-Olympic bust combine. The new governor will have to manage this conflict, and the earlier he starts doing so, the better. Waiting until next year is not an option, in my view.
- On the domestic side, Japan's regional banks are undercapitalized, fragmented and without viable franchise models. Managing the consolidation of the secondary banking system is an urgent task for the next BOJ governor. He'll need lots of political capital as well as strong respect from the private banks to create a better foundation for regional—and thus domestic—growth. This is why an academic without real-world experience or leverage with the technocracy would be unsuited for the BOJ top job, in my view.

- The next governor can either create the future of finance or be forced to play catch-up to China or South Korea. Technological progress in general, and fintech and blockchain in particular, demand regulatory leadership from central banks. The BOJ cannot afford to merely sit on the sidelines anymore. Yes, Tokyo wants to be Asia's leading financial center, and it needs strong BOJ leadership on progressive rules and regulations for that.
- Central banks in general, and the BOJ in particular, will have to redefine their policy goals and targets. While the simplicity of an inflation target makes it attractive, the growing complexity forced by relentless technological innovation, entrepreneurial drive and globalization may demand a more complex target for central banks. Here, Prime Minister Abe launched a campaign for a nominal GDP level target about two years ago. It will be interesting to see whether Abe's next governor will follow his lead.

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