Japan's Monetary Easing: Fighting Deflation and Stimulating Economic Growth?

By Stephen Lendman
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On April 4, the Financial Times headlined "Bank of Japan follows the Fed, on steroids." Pedal-to-the-metal reflects new governor Haruhiko Kuroda's policy.

At a news conference he said:

> "This is an entirely new dimension of monetary easing, both in terms of quantity and quality."

Except for emergency late 2008 easing, its the largest ever BOJ monetary madness. It's not "short-term emergency" driven. It's a "deliberate change in philosophy."

It abandons everything BOJ said about monetary policy before. It's high risk. The fullness of time will have final say. It may hit home like a hammer.

Plans are to double BOJ's monetary base. Kuroda wants it done in less than two years. The Fed doubled its balance sheet more slowly. Any significant rise in JGBs (Japanese government bonds) means Kuroda's strategy failed.

Until now, BOJ spent 21% of Japan's GDP on QE. It mostly bought short duration bonds. It hoped doing so would "leak out of the banks into the rest of the economy." It never happened.

Plan B is high-risk. Kuroda's doubling down on Plan A. He'll buy longer duration bonds. He'll spend 40% of Japan's GDP on QE. FT calls doing so an "unprecedented monetary 'big bang.' "

Japan's government bond market stands at 240% of GDP. It's the highest debt burden among developed countries. Overall inflation hasn't followed. Nothing's guaranteed it won't.

Kuroda plans to buy around 70% of JGBs. He'll keep doing it for two years. If inflation begins rising, purchases will slow. Instability may follow. Bond prices may fall sharply. Yields will rise. Losses could damage BOJ's balance sheet and credibility.

PNB Paribas Tokyo economist Ryutaro Kono believes "(i)f you pursue a radical policy, asset prices may change greatly, but if you set off a bubble and make the overall economy unstable, then you end up getting your priorities wrong."

Sumitomo Mitsui Asset Management economist Hiroaki Muto said ("t)argeting the monetary base will lead to a huge increase in current account balances that commercial banks keep at the BOJ, but I'm still not sure if this money will move through the economy."

Principalis Asset Management's Pippa Malmgren said "(w)e've never seen such unconventional methods used to create as much inflation as possible."

Monetary and economics Professor Lex Hoogduin called the effects Kuroda's easing "very difficult to control. At the same time, it will be politically very difficult to put a brake on this process. The policy can derail and can lead to distortions in the Japanese economy."

PIMCO's Bill Gross believes BOJ easing risks creating a rout in the yen. G-7 countries may not tolerate it. Much more depreciation is needed "to get even close to 2% inflation," he added.

It hasn't before so why now. At risk is heading it higher, not lower.

Kuroda says now's not the time to worry. "I'm not concerned that longterm interest rates could spike or asset market bubbles will emerge. I don't have any intention of financing government spending."

How many times before have we heard grand plans? How many rosy scenarios turned sour? How many bad endings followed? In the late 1980s, BOJ policy escalated asset and property prices. It did so to unprecedented levels.

Market crashes, rolling recessions, weak recoveries, malaise, deflation, and dangerous deficits followed. Kuroda's heading into unchartered waters. Hindsight may make him wish he never tried.

Market analyst Graham Summers calls Japan the ultimate monetization failure. For two decades, BOJ measures failed. Stagnation characterizes Japan's economy.

Economic activity and employment haven't improved. No matter. Kuroda wants to do more of what hasn't worked. He'll spend 7 trillion yen monthly buying bonds.

Doing so is "complete and utter insanity, especially since there is literally not one single instance in history in which debt monetization has produced economic growth."

At risk is eventual inflation. Kuroda's plan to fight deflation and stimulate growth may backfire. Rising costs already affect food, fuel and other necessities.

Multiple Fed QE rounds failed. Phantom data conceal dire conditions. Economic growth is weak. It's faltering. Real unemployment's 23%.

Nearly 25 million Americans remain jobless. Low-pay/poor benefit part-time or temp ones replaced full-time ones. Inflation's around 9% based on how calculated decades earlier. Poverty or close to it affects half of US households. Record numbers need food stamps.

Kuroda thinks like Bernanke. "We all know how this will end," says Summers. He expects disaster. Every inflated bubble pops. "This time will be no different."

"The lessons from Cyprus are obvious." Warning signs appear early. Cyprus first requested bailout help last June. Months later, it's entire banking system shut down. Unsecured depositors stand to lose most of their wealth. Some may lose everything.

Eurozone economies and America are troubled. So is Japan. Doubling down on what failed for two decades won't work. Expecting different results from doing the same thing repeatedly reflects insanity.

In 1988, Bernanke knew QE didn't work. Two Fed economists explained. Seth Carpenter and Selva Demiralp headlined "Money, Reserves, and the Transmission of Monetary Policy: Does the Money Multiplier Exist?"

Their conclusion:

> "In the absence of a multiplier, open market operations, which simply change reserve balances, do not directly affect lending behavior at the aggregate level."
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> "Put differently, if the quantity of reserves is relevant for the transmission of monetary policy, a different mechanism must be found."
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> "The argument against the textbook money multiplier is not new. For example, Bernanke and Blinder (1988) and Kashyap and Stein (1995) note that the bank lending channel is not operative if banks have access to external sources of funding."
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> "The appendix illustrates these relationships with a simple model. This paper provides institutional and empirical evidence that the money multiplier and the associated narrow bank lending channel are not relevant for analyzing the United States."

QE doesn't work. It could if properly used. It hasn't been. It's improperly used now. Boosting aggregate demand is needed. Doing so requires putting money in consumers' pockets.

Fed-style money printing madness doesn't stimulate growth and create jobs. It flows to bank balance sheets. It's used for speculation, high salaries, big bonus, buying competitors, and consolidating to greater size.

Helicopter Ben dropped lots of money on Wall Street. Doing so sent financial asset prices soaring. None went to Main Street where it belongs. Dire economic conditions there matter. Things head from bad to worse. Nothing ahead looks promising.

Wall Street Journal editors say Japan's economy recovery depends "more on structural reform than monetary policy." Prime Minister Shintaro Abe's Liberal Democratic Party (PDP) resists doing it. He prefers letting Kuroda do most heavy lifting.

Pedal-to-the-metal easing will adversely affect Japan's neighbors. South Korea expressed alarm. A depreciating yen harms its exports. Indonesia, Taiwan, Thailand and Malaysia are concerned. They'll also lose out.

Dropping money on bank balance sheets doesn't work. Bernanke's done it since 2008. According to Paul Craig Roberts:

If QE stops, "confidence in the US dollar would rise. Money would flow into US investments, both supporting the US stock market and helping to finance the large US budget deficit."

"Gold and silver prices would decline. Negative dollar expectations would be squeezed out of oil and grain prices, although drought, flood and supply factors would continue to impact grain prices, and the administration's wars can impact oil prices."

Economist David Rosenberg calls excessive monetary easing "no panacea." It's "self-defeating." America's seeing diminishing returns.

What's needed is "a coherent fiscal policy and the reality that a record 90 million Americans left the labor market entirely, and that 40% of the unemployed ranks have been out of work for over six months."

It's more than double the historic norm. It makes affected workers "increasingly unemployable." Inactivity "impedes their future productivity potential."

Tripling the Fed's balance sheet to $3.2 trillion did little to stimulate growth and create jobs. It hasn't prevented the ratio of new hires to job openings from returning to early onset fall 2007 recessionary times.

Crediting the Fed with housing's modest rebound doesn't wash. Institutional investor all-cash deals get full credit.

From a supply-side perspective, America's economy is moribund. It's dead. Soft demand checks inflation. When it's stronger, Rosenberg expects it to "return with much greater vengeance than has been."

It's because of the "increasingly inelastic shape to the US aggregate supply curve." It's early. In 2005, two years before America's housing bubble burst, Rosenberg warned it was coming.

In the late 1960s, inflation was 2%. Unemployment was 4%. Who could have imagined what lay ahead? It followe failed Fed policy. Real short rates remained negative far too long.

A flawed Phillips Curve policy was pursued. Conventional wisdom believed higher inflation would stimulate growth and decrease unemployment.

Be careful for what you wish for? It may not turn out like you expect. For 12 years, America got four recessions. No one, including the Fed, saw it coming. It missed the last one in late 2007.

In summer 2008, it suggested raising rates. So did the ECB. Its easing policy is more aggressive now than at the depths of the early 2009 crisis.

Fed policies assure missteps. Historical evidence shows increasing inflation produces adverse macro results. This time's no different. It's true for America, Europe and Japan. Bad endings look certain. They'll arrive in the fullness of time.

How long can QE and ZIRP (zero interest rate policy) continue while budget deficits add over $1 trillion to the national debt annually?

Fed policy can't stop now. Eventually, what can't go on forever, won't. It's not hard imagining how things will end. It'll be with a bang, not a whimper.

Global economies everywhere will be impacted. They may be like never before. Recovery will be slow and painful. People who know best say so.

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