

“Most generations, it might be said, walk in a path which they neither make, nor discover, but accept; the main thing is that they should march .... The practical thing for a traveler who is uncertain of his path is not to proceed with the utmost rapidity in the wrong direction” - The Acquisitive Society by R. H. Tawney

## A Transformative moment for the BOJ: a catalyst to keep rates low and equity/bond prices high

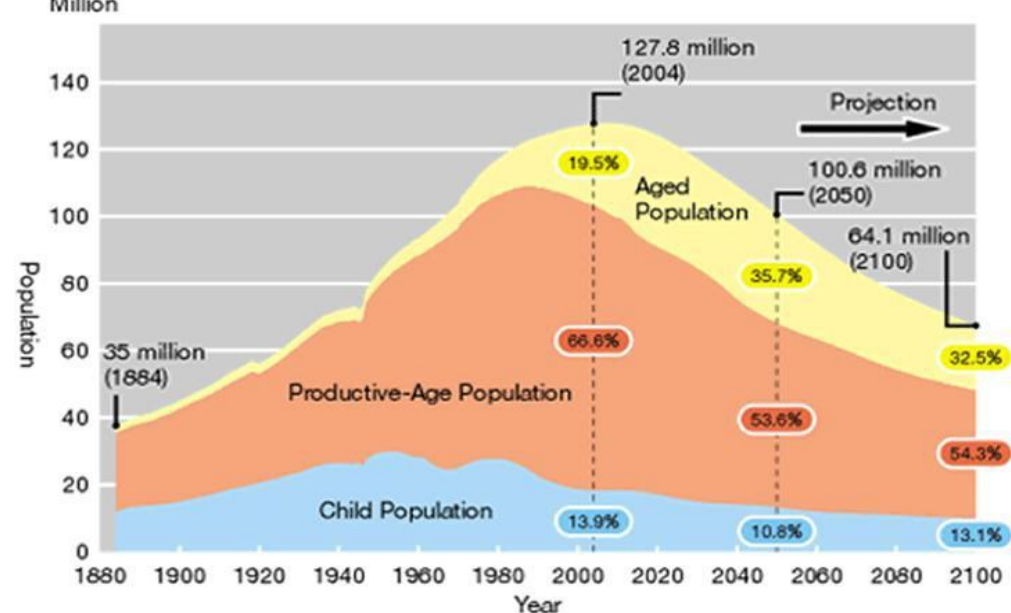
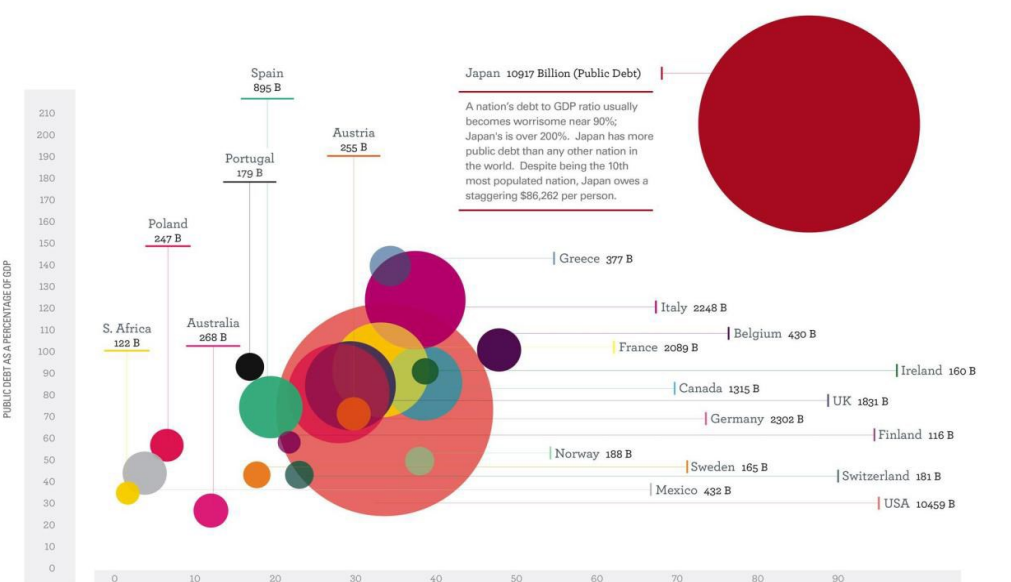
The BOJ has been embarking on a rapid US styled easing program since 2012. They spend nearly 30% of their central government tax revenues financing their own debt and have a debt to GDP ratio that surpasses anything seen in the OECD (or really elsewhere for that matter). On Friday, Bank of Japan Governor Haruhiko Kuroda announced new stimulus measures that would rival anything we have seen so far. The central bank and government pension fund will pump trillions more yen into the economy to attempt to jolt markets into action and thwart the decades old deflation problem that the country faces. The Bank of Japan will expand its asset buying program by as much as 33%, but more interesting is the mix of new purchases which include equities and real-estate.

Bank of Japan's current balance sheet is about 50% of GDP. This compares to 20-30% for the US and Europe. John Hermann from Mitsubishi UFJ Securities believes that it will reach about 75% of nominal GDP within 15 months. This is effectively a triple of the US Federal Reserve program. The BOJ's purchases beyond JGBs is the most significant and surprising measure. This is unprecedented action taken by the central bank which should put enormous pressure on Mario Draghi at the ECB to expand his program. What this may do is double back to the US and disallow the US to hike rates as easily as they thought.

The BOJ is extending out the yield curve taking on more duration in their bond portfolio. They currently buy up a great majority of the JGBs in auction, so what's next? Likely, we will see more money coming into US treasuries. Not just does the US have higher yields, but the market is more liquid and the credit is good. New volume will come in and keep US yields down for longer, notably at the longer end of the curve. I'm worried that we may see continued flat or falling rates. Despite the rally in the Nikkei over the last year or so, I would look for continued gains as people try to ride a 2013 styled US stimulus fueled equity market to double digit annual returns—the actively managed hedge funds are still trailing their benchmarks.

## DEBT CRISIS: JAPAN

Forget Greece, when you look at the numbers Japan poses the greatest worry.



Source: National Institute of Population