Central bank chief Haruhiko Kuroda wanted unanimous support from his board for a radical monetary plan to pull Japan out of the economic doldrums.

**Kuroda’s calculus: How the Bank of Japan staged its big bang**

**BY LEIKA KIHARA**
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**DEFLATIONARY DARK DAYS:** Japan’s new central bank governor Haruhiko Kuroda hopes his radical easing plan will lead Japan out of two decades of economic stagnation.

*REUTERS / ISSEI KATO*
From the moment he assumed the job in March, Bank of Japan Governor Haruhiko Kuroda had a number in mind: 9. The number had nothing to do with the scale of the bank’s stimulus plan, which the market had been buzzing about. It was a vote target.

The central bank’s policies are determined in votes by its nine-member board, chaired by the governor. And Kuroda wanted all eight of his colleagues to back his controversial plan to jolt Japan out of its long slump by flooding markets with cheap money. Only weeks before Kuroda joined, the board had voted 8 to 1 against a plan for bold monetary easing. Now, vocally backed by a new prime minister, Kuroda knew the arithmetic had moved in his favor. He was joining the board with two new deputies. They plus two sympathetic veterans on the board gave the new governor a 5-4 edge. But Kuroda wanted unanimous support.

His recipe was radical: double Japan’s money supply in two years, and promise to ignite 2 percent inflation in two years, reversing nearly two decades of falling prices. Investors doubted the cautious BOJ had the stomach; Kuroda calculated that a 9-0 victory would show the BOJ now meant business.

In a two-week whirlwind of meetings, according to people with knowledge of those deliberations, Kuroda won over the four holdouts on the policy board for the biggest attack on stagnation by any central bank in recent years. The campaign kicked off at a secret weekend retreat in downtown Tokyo, inside a former BOJ dormitory.

On April 4, the board gave him his 9-0 win. The degree to which Kuroda delivered on his promise, and the extent of his support, stunned financial markets. The impact was exactly according to script: The yen went into a precipitous slide, Tokyo stocks extended a five-month rally, and government-bond yields fell to record lows.

The dramatic vote swing highlighted both the power of Kuroda’s nerdy charisma and the influence of a group of senior BOJ officials who had agitated behind the scenes for a more aggressive policy for months. It is far too early to know whether Kuroda will conquer deflation, but the story of how he won his first battle suggests the new governor has galvanized internal support for the long fight ahead. This account is based on interviews with more than a dozen central bank insiders before, during and after Kuroda’s first days at the central bank.

“MR. SPOCK”

Kuroda’s central idea is a more determined version of the U.S. Federal Reserve’s “quantitative easing,” which involved pumping vast amounts of money into the American financial system. His plan calls for the BOJ to roughly double annual purchases of Japanese government bonds to a half-trillion dollars and double its purchase of riskier assets in two years.

The aim is to push down long-term interest rates, encourage companies and individuals to borrow, and induce investors to seek higher returns, in the equity markets for instance.

The 68-year-old Kuroda seems an unlikely change agent. A cerebral retired...
Easy money

Haruhiko Kuroda, tasked with a “regime change” at the Bank of Japan by Prime Minister Shinzo Abe, stunned markets on April 4 when the BOJ announced it would pump $1.4 trillion into the economy to end two decades of stagnation. It sent the yen to its lowest in almost 4 years.

Ministry of Finance bureaucrat with a master’s degree in economics from Oxford, he doesn’t pound tables or raise his voice, say people who have worked with him. His analytical bent reminds one former associate of “a Japanese version of the Mr. Spock character” from Star Trek.

But Kuroda has been a relentless critic for 15 years or more of what he saw as the BOJ’s lack of decisive action in the face of a stalled economy. That stance was what prompted the new prime minister, Shinzo Abe, to whisk him away from the top job at the Asian Development Bank.

Career BOJ officials got an inkling of what Kuroda had in mind on March 4, when he appeared at his first confirmation hearing in a cramped committee room at the lower house of parliament. Members of the BOJ’s elite Monetary Affairs Department watched a closed-circuit video feed from the seventh floor of the central bank’s headquarters to take stock of their incoming boss.

It was a month before the new BOJ board’s first policy meeting. The bureaucrats had drawn up three scenarios, knowing time would be tight. The first was a relatively tame increase in asset purchases; the second was a bolder proposal to extend the duration of bonds the central bank would buy to five years or longer, up from three years.

By the time Kuroda finished his nearly three-hour session, it was clear both of those proposals were effectively dead. Wearing a dark suit and a black tie with silver stripes, Kuroda appeared subdued. But his tone was authoritative, and confirmed much of what the watching bureaucrats had suspected: Kuroda would come out swinging.

They realized he wanted the bank, over the next few weeks, to come around to the most radical of the set of options they had imagined: to buy bonds of all maturities and boost purchases of riskier assets, such as exchange-traded funds and real-estate investment trusts. The only question was whether the rest of the board would follow the incoming BOJ chief.
Three days later, the BOJ board met for its last policy review under the retiring governor, Masaaki Shirakawa. It stood pat on policy. Overnight interest rates – the bank’s primary tool – were already essentially at zero. Shirakawa had been openly skeptical about how much more the central bank could do, especially if the government didn’t match fresh monetary easing with structural reforms of the economy, such as cutting red tape and freeing up the labor market.

It was a stance that frustrated some senior BOJ officials, who like Kuroda, wanted a more radical approach. “What we had to change was the incremental approach to monetary policy,” one said.

Shirakawa had been under intense pressure the past year to give ground. Abe rode to power in December’s election on a campaign that focused on ending Japan’s debilitating price declines and bashing the central bank. The vote turned into an unexpected referendum on the BOJ, and the BOJ lost.

In January, Shirakawa was dragged into accepting Abe’s call to double the bank’s inflation target to 2 percent - even though prices were still falling, and the BOJ’s own forecasts showed inflation wouldn’t exceed even 1 percent for the next two years. Central bankers hate setting difficult goals: Failure can undermine their credibility with the public. Credibility, in turn, is everything. If a central bank can make people believe inflation is coming, for instance, that very expectation might spur people to buy things before they grow expensive – a self-fulfilling prophecy.

Shirakawa reluctantly engineered an enhanced, “opened-ended” round of quantitative easing, though he set it on timed release. The additional asset purchases would begin more than half a year after he left office.

At Shirakawa’s last board meeting, on March 6 and 7, Sayuri Shirai, who had previously shared his caution, proposed starting the open-ended bond-buying immediately. Board member Ryuzo Miyao proposed committing the BOJ to maintaining zero interest rates until the 2 percent inflation target was “in sight.”

But without a leader willing to catalyze the growing readiness for change, both dovish proposals were voted down 8-1.

**PUSHING ON AN OPEN DOOR**

More signs of movement came on March 12. The more conservative of the two nominees to be Kuroda’s deputy governors, career BOJ civil servant Hiroshi Nakaso, said in his confirmation hearing the bank “shouldn’t be bound to precedents and must think with a new mindset.” Nakaso had always warned of the dangers of loading the BOJ’s balance sheet with too much long-term debt. Now, he acknowledged the bank could have done more to beat deflation.
Nakaso was cast in the Shirakawa mold but he was a realist. He would accept the tide’s turn toward “Abenomics,” but would fight for the things the central bank most wanted to preserve. The first was the BOJ’s statutory independence, granted in a 1998 law that critics — including, for a time, Abe himself — were threatening to rewrite. Also vital for Nakaso, who as a BOJ bureaucrat had engineered the end to a previous spell of quantitative easing in 2006, was the need to work on an exit strategy for Kuroda’s reflation program.

Kuroda’s other nominee for deputy, Kikuo Iwata, was, if anything, more committed than his new boss to radical reflationary tactics. The academic economist had branded the BOJ as “‘The Guardians of Deflation’” in a book last year. He now was pushing for the unorthodox idea of targeting not just the size of the BOJ’s balance sheet for expansion, but also a measure of Japan’s entire money supply.

Kuroda would make no formal contact with the protocol-sensitive BOJ before his March 20 inauguration. But staffers were already hard at work anticipating policies he might want.

Again there were three scenarios. But in a sign of how rapidly the game was changing, even the most modest plan — increasing annual Japanese government bond purchases by 30 trillion yen ($300 billion) — was far more radical than the Shirakawa era, when a big increase was 10 trillion yen. Even that wouldn’t be enough for Kuroda, who would also reject a 40-trillion yen plan. He insisted on the biggest option — boosting debt purchases by 50 trillion yen ($500 billion) a year.

Kuroda now had on his side his two deputies and willing accomplices in board members Miyao and Shirai, the former academics who had proposed policy tweaks at the previous meeting. That gave him a 5-4 majority for his big-bang plan.

At that point, Kuroda decided to gather the new board for the first time at a weekend retreat at Hikawa-ryo, a former BOJ residence near the Syrian embassy, people familiar with the deliberations told Reuters about this previously undisclosed meeting. The getaway is the central bank’s place of choice when privacy is paramount.

Obscured behind earthen walls, Hikawa-ryo appears to be an oasis of solitude from outside its wooden gate. Inside, Kuroda’s focus that weekend was to hear out the doubts of the four BOJ board members who were not yet in the reflationist camp.

One of them was former Nomura Securities economist Takahide Kiuchi, who worried about the risks of giving the government a blank check to issue new debt. During its long slump, Japan has run up the largest ratio of debt to economic output of any advanced economy, some 200 percent — double the ratio of the United States and exceeding even the 170 percent of Greece.

In the discussions, Kuroda took care not to appear to be imposing his will in steering the debate, listening carefully and with a reassuring smile to what everyone had to say. “He’s a good listener,” one BOJ official said.

Moreover, a consensus was beginning to form, and bucking a consensus in Japan takes guts, said Miyako Suda, a former BOJ board member who sometimes voted against boosting bond purchases in the past. “It’s tough, particularly if you’re voting against monetary easing. People like it when central banks ease policy, so you need courage to vote against it,” she told Reuters.

Two of the four unconvinced board members — former market economist Takehiro Sato and banker-turned-policy-maker Koji Ishida — to some extent had already supported Kuroda’s calls for radical monetary expansion and a departure from Shirakawa’s incremental approach.

But Sato was deeply suspicious about incoming Deputy Governor Iwata’s calls to target the monetary base — the sum of Japan’s cash in circulation plus deposits that commercial banks hold with the BOJ. Sato argued this would essentially be a reversion to Shirakawa’s incremental approach.

As he used the retreat to launch his push for a unanimous vote, Kuroda also let it be known he was unwilling to delay the big decision, even if that meant splitting the board vote, according to officials with knowledge of the deliberations.

The board was largely agreed on the need for bolder action — even if they were divided on how to do it, the officials said. Kuroda was helped by the fact that board members were under extraordinary pressure not to appear to be resisting the will of the Japanese people, who had given Abe a strong electoral mandate. Lawmakers had repeatedly warned they would overhaul the bank’s legal charter if it didn’t wage all-out war on deflation.

“The board members may have thought they should vote as one to show their determination to achieve 2 percent inflation, or face threats of a revision to the BOJ Law,” said prominent BOJ watcher Izuru Kato, chief economist at Totan Research.

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The other doubter, Ishida, thought more time was needed to deliberate on the potential consequences of such a momentous overhaul of BOJ policy.

A third board member, Yoshihisa Morimoto, a former electric-power
executive, wasn’t opposed to further easing, but he balked at the sheer size of the package. He questioned whether the BOJ really needed to do so much in a single go.

Kiuchi, the former Nomura economist and debt hawk, worried that loading up the BOJ’s balance sheet with so much long-term debt would complicate an eventual exit from an ultra-easy policy. He wanted the BOJ to issue guidance to the market that its massive bond-buying would not mean the bank was monetizing government debt – printing money to repay it.

The retreat ended without the unanimous endorsement of his plan that Kuroda was seeking.

In the two days leading up to the landmark April 3-4 policy meeting, Kuroda began working the library-quiet eighth floor of the BOJ headquarters, where board members have their offices.

A habitual organization man from his decades at the Finance Ministry and his eight years heading the Asian Development Bank, Kuroda met each board member in his or her office. He sought to allay their remaining concerns, while insisting the bank needed to send a “simple, clear” message with its decision, according to the officials with knowledge of those talks.

He knew the importance of presentation. Shirakawa had tended to diminish the impact of his 14 easing decisions by talking down their significance in professorial tones. Kuroda had long experience influencing financial markets from his days leading Japan’s currency policy at the Finance Ministry, where he was regularly ambushed by reporters for comment on possible yen-selling interventions.

Presented with carefully calibrated proposals on how much the BOJ would need to boost money supply to achieve the desired level of inflation, Kuroda asked his staff to go big on the numbers. “Can we make it double for everything?” he asked.

By the time he faced the media to announce the policy, he had a simple chart with four bullet points, each with the number 2 highlighted in red: 2 percent inflation in two years; a doubling of the monetary base; and at least a two-fold increase in the BOJ’s bond holdings and average maturity.

He later said nothing was “magical” about the number 2, but repeatedly said at his news conference he wanted the new policy to be “easy to understand”.

Kuroda got almost everything he wanted. The only hint of dissent was board member Kiuchi’s lone - and unsuccessful - plea to water down the BOJ’s commitment to hitting its inflation target in two years.

“All the board members talked about this and came to the conclusion that instead of taking incremental steps, the BOJ would decide on all the necessary steps this time,” Kuroda told a news conference. Sporting a red tie, he was animated, accenting his points with frequent smiles and hand gestures. “We had that kind of discussion, and I was able to garner everyone’s support.”

But there wasn’t time to forge agreement on everything. The bank failed to set a new measure to show it wasn’t simply printing money to repay the national debt. It could agree only to suspend the previous limit, which the new policies broke. And the policy board left operational details undecided - to the consternation of the banks that would be on the receiving end of the BOJ’s fire hose of liquidity.

**BANKS BLINDSIDED**

The BOJ’s decision to deluge financial markets with cash sent the benchmark Nikkei Stock Average to a near five-year high. The yen went to a four-year low to around 100 to the dollar. The 10-year bond yield hit a record low 0.315 percent before rebounding.

Major banks were blindsided, in part because they hadn’t been consulted on the market implications of the central bank’s massive asset purchases. In the past, the BOJ had worked out details of its asset-buying operations after sounding out the banks in detail to cushion the potential market impact. The central bank skipped that process this time because of Kuroda’s urgency in getting his big bang plan approved at his first board meeting.

When the BOJ summoned executives of major banks for a meeting on April 11, the bond market was in gyrations. Some bankers complained the BOJ was on the verge of crowding them out of the 900-trillion-yen JGB market, making it harder for banks to buy the bonds they have relied on during a decade of slow growth as a safe-haven substitute for loans.

“It’s actually scorched-earth tactics,” said Hideo Kumano, a former BOJ official who is now chief economist at Dai-Ichi Life Research Institute in Tokyo. “They are burning markets to the ground, reducing them to ashes.”

BOJ officials were shaken by the financial industry’s criticism, acknowledging that the rush to get the plan out had left the market in the dark about the operational details of the $500 billion in annual bond purchases. But there is no going back.

“Basically, we’re coming up with the specifics as we go along,” one senior central bank official said.

Additional reporting by Sumio Ito, Yoshifumi Takemoto and Stanley White; writing by William Mallard, Editing by Bill Tarrant and Michael Williams
Bank of Japan under new management

The Bank of Japan unleashed the world's most intense burst of monetary stimulus on April 4, promising to inject about $1.4 trillion into the economy in less than two years. Here are short profiles of the Bank of Japan's board that took the decision:

**HARUHIKO KURODA, 68, GOVERNOR** – He was plucked from the Asian Development Bank by Prime Minister Shinzo Abe to deliver radical reflationary policies at the Bank of Japan. Took office in March. Kuroda had long criticised the BOJ for doing too little, too late to end deflation and boost the Japanese economy. A voracious reader of books ranging from philosophy to detective novels.

**KIKUO IWATA, 70, DEPUTY GOVERNOR** – He was among the most firmly established critics of the BOJ, arguing the central bank could have ended deflation sooner with more aggressive action. Took office in March. He had advocated the BOJ target base money – cash and deposits at the central bank – in guiding policy. That was one of the steps the BOJ took on April 4.

**HIROSHI NAKASO, 59, DEPUTY GOVERNOR** – He was in charge of the central bank’s international affairs before being named to Kuroda’s team in March. With his fluent English and deep overseas contacts, Nakaso played a key role in trying to contain the damage to global banks from the collapse of Lehman Brothers in 2008.

**KOJI ISHIDA, 65** – The veteran banker voiced caution over shifting the BOJ’s policy framework too quickly, even as governor-nominee Kuroda was advocating aggressive action. Ishida feared that overloading the bank’s balance sheet with long-term debt could bind its hands on future decisions.

**RYUZO MIYAO, 48** – A soft-spoken former academic known for his research on inflation-targeting, he is considered among the board’s keenest proponents of unorthodox easing. Miyao has proposed several policy changes in the past, including raising the BOJ's inflation target to 2 percent. He has been willing to cut interest rates, proposing in December cutting the 0.1 percent floor on money-market rates. His proposal was rejected 8-1.

**TAKEHIRO SATO, 51** – The former economist at Morgan Stanley MUFG Securities had argued for buying foreign bonds as a future option for the BOJ. He backed down after the idea drew heat from other G7 nations that consider it tantamount to currency intervention. Initially regarded as a policy dove, the amateur violinist was one of two members who dissented to the BOJ’s January decision to double its inflation target to 2 percent.

**TAKAHIDE KIUCHI, 49** – The former Nomura Securities chief economist was one of the two board members voting against raising the BOJ’s inflation target to 2 percent in January. He said this was far above a sustainable level for Japan, which has seldom had inflation that high, even during asset bubbles. Kiuchi, despite earlier warning against loading up on longer-dated debt, joined the rest of the board in voting for most of Kuroda’s reflationary policies in April. But he proposed watering down the BOJ’s commitment to hitting its inflation target in two years. His proposal was rejected 8-1.

**SAYURI SHIRAI, 50** – The former International Monetary Fund economist often sided with ex-governor Masaaki Shirakawa, who argued the BOJ had already offered enough stimulus. The board’s only woman, while mostly voting with the majority, surprised markets in March by proposing, shortly before Kuroda joined, that the BOJ combine its two bond-buying schemes to make it easier to buy longer-dated debt – an idea the incoming governor was floating. The proposal was rejected 8-1 before being adopted at Kuroda’s first meeting in April.

**YOSHIHISA MORIMOTO, 68** – The former utility executive has always voted with the majority since joining the board in 2010. He has also warned the government must play its role in beating deflation by pursuing structural reform and deregulations to make Japan an easier place to do business.

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