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Changing the GPIF will be easier said than done

Key takeaways

- Finance Minister Katayama Satsuki moved markets when she said that the Takaichi government wants Japanese institutional investors to increase their holdings of domestic assets.
- However, reversing Abe-era reforms could be a complicated process, and without additional details, the finance minister's remarks may be another example of the government's "oral intervention" against rising yields than a fully fledged plan to use demand from pension funds to cap interest rates.

On 10 July, Finance Minister Katayama Satsuki roiled markets when she said in a press conference following Friday's cabinet meeting that the Takaichi government would push the Government Pension Investment Fund (GPIF) and other pension funds to increase their holdings of domestic assets. However, there are several reasons to question the credibility of Katayama's remarks.

First, when evaluating comments by Katayama, Chief Cabinet Secretary Kihara Minoru, Economic Revitalization Minister Kiuchi Minoru, or Prime Minister Takaichi Sanae with direct bond market implications, their intentions have been clear since the start of the Takaichi government. Takaichi is determined to spend more in pursuit of her strategic priorities; achieving this goal at a time of rising interest rates and structural change in the market for Japanese government bonds as the Bank of Japan (BOJ) gradually withdraws demand means that the Takaichi government is continually seeking ways to reassure investors, prevent sharp increases in yields, and otherwise maintain market confidence in the government's finances. The Takaichi government has been engaged in this two-step process – articulating costly policies in its documents while using rhetorical gestures to reassure investors – from the very beginning. (See this note, for example.) Accordingly, since yields rose after the government revealed the draft of its

Basic Policy for Economic and Fiscal Management Reform (the *honebuto*), the Takaichi government has been working especially hard to reassure investors, including adjusting the language of the *honebuto* on monetary policy to assuage concerns about government interference in Bank of Japan (BOJ) decision-making. However, the fact that the government is not reversing its overall approach to fiscal policy means that these rhetorical gestures should be treated less as expressions of the government's intentions than as a form of oral intervention.

As such, unless and until the government provides more details about plans to push the GPIF and other institutional investors to rebalance their portfolios in favor of JGBs and other domestic assets, the government's statements to this end should be approached with equanimity. It is notable that reporting following Katayama's remarks suggests that there is in fact no such plan in hand yet. The GPIF reform process conducted under the second Abe administration was a multi-year process that involved not only rebalancing the fund's portfolio but also fundamentally reforming its management, shifting power away from bureaucrats and the Ministry of Health, Labor, and Welfare (MHLW) to professional money managers. Precisely because of these reforms, it is more difficult for the government to order pension funds to revert to the financial repression of the pre-reform days. The Takaichi government may well want the GPIF and other funds to provide stable demand for JGBs that can put a lid on rising yields, but in the post-reform world it is not enough for senior government officials to express their preferences to this end.

To be sure, financial markets should anticipate that the government will look for ways to shape the structure of the Japanese government bond market in favorable ways, particularly to avoid dependence on foreign investors as the marginal buyers of JGBs. This accounts for the government's recent emphasis on marketing more bonds to Japanese retail investors. It is not surprising that the government might also eventually flesh out plans for encouraging Japanese pension funds to return home. But ultimately, the government's attempts to tinker with or shape demand for JGBs should not distract from the fundamental reality that the Takaichi government is not backing down from its big ticket spending plans, which could have a greater impact on yields than the government's various trial balloons for supporting demand for JGBs.

Tobias Harris
Founder and Principal
Japan Foresight LLC
tobias@japanforesight.com
+1.847.738.4048

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