Yield Curve Control and Balance Sheet

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The views presented here are those of the author and do not necessarily reflect those of the Bank of Japan
1. BOJ’s Balance Sheet

**Assets**

- Others
- ETF • REIT
- CP • Corporate bonds
- Funds-Supplying Operations against Pooled Collateral
- JGB

**Liabilities and Net assets**

- Others
- Banknotes
- Current deposits

Source: Bank of Japan.
2. Balance Sheets of Major Central Banks (Ratio to nominal GDP)

Sources: Cabinet Office; Bank of Japan; Federal Reserve; BEA; ECB; Eurostat; Haver.
3. Overview of BOJ’s Monetary Policy

- New Monetary Policy Framework Since September 2016

New framework comprises of **Yield Curve Control** and **Inflation-Overshooting Commitment**.

**Yield Curve Control (YCC)**

**Inflation-Overshooting Commitment**

Sources: Bloomberg; Cabinet Office; Bank of Japan; Federal Reserve; BEA; ECB; Eurostat.
4. Where Are We Now?
- Halfway toward the price stability target of 2%

Sources: Bank of Japan; Ministry of Internal Affairs and Communications.
Notes: Latest data for Output Gap as at the October-December quarter of 2016. CPI data as at the January-March quarter of 2017.
Benefits

✓ Possible to **work directly on lowering the long-term rate**.
✓ An announcement of a target that clarifies perceptions could prompt the **rate to move down without purchasing securities in significant quantity**.

Remarks or drawbacks

✓ **Adjustments in the cap** would likely be needed.
✓ **Substantial volatility** in central bank securities holdings.
✓ **Complications for exit** from targeting approaches.

6. How Different is YCC from Previous Unconventional Measures?

① Pursuance of the *most appropriate yield curve*.
   ✓ Lowering borrowing costs.
   ✓ Avoiding too low super-long rates.

② Highly *sustainable* framework.
   ✓ Little concern about scarcity of JGBs for purchases.

③ *Flexible* tool for adjustments according to economic developments.
   ✓ Possible to change target rate as with conventional policy.
7. Framework of YCC
- How Can BOJ Control JGB Yield Curve?

- Purchases JGBs across all maturities in a substantial scale.
- Increases or decreases the amount of JGB purchases.
- Conducts fixed-rate JGB purchase operations.
- Conducts fixed-rate funds-supplying operations for up to 10 years.
- Announces the schedule for JGB purchase operations, while determining the amount on the day of the operations.
8. 9-Month Experience of YCC (1)

Source: Japan Bond Trading.
9. 9-Month Experience of YCC (2)

- Fixed-rate Operations and Major Changes in Amounts

Source: Japan Bond Trading.
10. Developments in JGB Yield Curve

Source: QUICK.
11. Gross/Net JGB Purchases by BOJ

Source: Bank of Japan.
12. Channels through which YCC Affects JGB Yields

① Stock effects
✓ BOJ’s accumulation of JGB holdings would exert persistent downward pressure on JGB yields.

② Flow effects
✓ Market participants are taking for granted the ongoing JGB purchase operations.

③ Signaling effects
✓ Fixed rate operation in early February effectively provided counterparties with an opportunity to sell JGBs at strike price, thereby enhancing market confidence in YCC.
13. USA Case (1942-51) : Overview

- Long-term Treasury bond yield was capped at 2.5%, and short-term Treasury bill yield was pegged at 0.375% (until July 1947).

- The policy was driven by wartime finance requirements rather than monetary policy considerations.

- The cap on long-term rates was binding only from late 1947 to December 1948 when large securities purchases were required.

- Prior to 1947, low inflation and pegging of the TB rates at 0.375% helped long-term rates to stay below the ceiling. The FED accumulated bills in its portfolio.

- Inflation pressures eventually led to the Treasury-Fed Accord of 1951, which discontinued the interest rate cap.
14. USA Case(1942-51) : Fed Balance Sheet

## 15. USA Case (1942-51) : Comparison with BOJ’s YCC

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16. Closing

A key question: Does YCC entail balance sheet risks?

✓ Amount of JGB purchases may change in order to achieve the intended JGB yield curve.

✓ Fluctuations of JGB purchases, though did exist, were not necessarily significant during past 9 months.

✓ Appropriate and timely operations and proper communication might avoid significant expansion of JGB purchases.

✓ Most importantly, appropriate adjustment of targets according to economic developments would alleviate potential balance sheet risks.