What the Bank of Japan's surprise move means for the global economy

By Neil Irwin
October 31, 2014 – *The New York Times*

One central bank giveth, and another taketh away.

Two days after the Federal Reserve ended its program of quantitative easing, the Bank of Japan has doubled down on the strategy with a surprise expansion of its program, in which it will now buy 80 trillion yen ($721 billion) worth of Japanese bonds each year with newly created money. If you're keeping score, the era of central bank money printing is over (for now) in the United States and Britain, very much alive in Japan, and maybe-possibly-on-the-verge of arriving in the eurozone.

The Bank of Japan's new action took markets by surprise and drove a 4.8 percent gain in the Japanese stock market and smaller gains across the globe. It also offers a reminder — or perhaps a warning — of just how hard it will be to get the global economy out of its deflationary funk. And a cycle of bad political decision-making, across many countries, is the reason.

The back story is this: At the start of 2013, a new government came into power in Japan, led by Shinzo Abe, promising a series of aggressive measures to jolt the Japanese economy out of its long period of stagnant growth and falling prices. A crucial part of that strategy was the appointment of Mr. Abe's handpicked central bank governor, Haruhiko Kuroda, who promised to do whatever it took to get inflation up to 2 percent in Japan.

The initial results were promising. In early 2013 the yen fell on currency markets, and the Japanese stock market rose sharply. For the first time in two decades, there was palpable buzz around Japan's economic prospects, both inside the country and around the world. "Abenomics" became a household term, at least in households that are interested in international economics.

But since then, neither the rest of the world, nor the rest of the Japanese government, has done much to help Mr. Kuroda.

Within Japan, the fiscal authorities raised a consumption tax this year, aiming to rein in budget deficits in a country with the highest public debt in the world relative to the size of its economy. That created a steep economic contraction in the second quarter, weakness that persisted through the summer.

Meanwhile, Europe has dithered as its economy has ground to a halt, and many major emerging economies have slowed. With the rest of the world slowing down and supplies of oil and many other raw materials rising, the price of most major commodities has fallen sharply since the summer.

So Mr. Kuroda faced slumping Japanese economic growth because of decisions his own government made and downward pressure on prices due to things that happened in the rest of the world. The credibility of his promise to do whatever it took to get to 2 percent inflation was in doubt.

Hence the surprise move Friday. It was a close call — the vote on the bank's policy committee was 5 to 4, not like the unanimity of Mr. Kuroda's earlier tenure. But the theater of it may have been helpful in the psychological aspect of persuading people in Japan that their central bank really is serious about getting higher inflation, and that citizens should make their spending and investment decisions accordingly. Inflation expectations tend to be self-fulfilling.

But while it is nice to see boldness from one of the world's leading central banks — a sharp contrast with the sluggishness of the European Central Bank in responding to dire threats to the eurozone economy — the move does underscore a broader problem that has haunted the global economy the last several years.

Central banks have been the only players in town trying to boost global growth. In the United States, Congress from 2011 to 2013 ignored the pleas of Ben Bernanke, then the Fed chairman, to avoid sharp spending cuts that would depress growth. Right now, the German government is said to be furious at the E.C.B. president, Mario Draghi, for his calls for more public spending by Germany and other financially strong European nations. And the Bank of Japan is now facing a harder job because of the Japanese parliament's eagerness to raise consumption taxes.

In each case, the central bank has gotten little support from its government in trying to encourage growth, and carried more of the burden itself, often in the form of yet more quantitative easing, which has tended to sharply boost asset prices in the financial markets but has had much more questionable effects on job creation and wages.

We've gotten used to central bankers with names like Kuroda, Bernanke, Yellen and Draghi being the primary actors trying to get the global economy on track. Their job would be much easier if their counterparts holding elected office showed the same enthusiasm.