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The failure of the BOJ's approach is now obvious Deflation is ending, the yen is weakening and stocks are rising

The divide between the differing logic is clear

Movements in financial markets are logical. Musha Research strongly adheres to the belief that 'only more consistent logic will lead to successful investments'. Times like now when this belief is right on target occur only rarely. I am convinced that the current logic shows that we are on the verge of a switch to a long-term upturn in the stock market and a long-term downturn for the yen.

The logic is clear and simple. Now that the United States has succeeded in avoiding deflation, the following chain of events is taking place.

- (1) The U.S. economy has avoided the deflation that happened in Japan and is now on a growth trajectory.
- (2) The Fed's creative financial measures (quantitative easing) were the decisive factor behind the U.S. economic recovery and prevention of deflation.
- (3) These events have proven that the BOJ was mistaken to say that 'deflation was not our fault because we did everything possible to prevent it'.
- (4) Either voluntarily or passively, the BOJ must make a major shift away from its previous logic and initiatives.
- (5) Once the BOJ clearly positions itself at the forefront of the fight against deflation, a strong yen and falling stock prices, we will see the end of the strong yen, deflation and falling stock prices in Japan.

Criticism of the mistaken pessimistic view of the U.S. economy

The key points for everything are the U.S. economic recovery, the economy's ability to sustain medium and long-term growth, and the selection of surprisingly accurate policies. I strongly believe in these three points. A remarkably large number of so-called 'experts' constantly created an erroneous image of the U.S. economy. This image planted the seeds of unnecessary pessimism. For a thorough discussion of this subject, please read Key Strategy Issues (our insight analysis report) No. 294, 'The U.S. economy is advancing to a new stage of growth – 'The U.S. has the world's only economy able to sustain medium and long-term growth', which will be released this week.

The BOJ's approach has been defeated and the groundwork for a policy shift is in place

If we agree that the U.S. economy has been revived, the next question is whether or not the BOJ will change. Many people are pessimistic. These pessimists are the same people who believe in the BOJ's stance that 'deflation was not our fault because we did everything possible to prevent it'. But these people should adopt a humble attitude about the facts. BOJ Deputy Governor Kiyohiko Nishimura said, "the BOJ will take new actions that are not in economics textbooks. This is a time when new financial theories can be created." Mr. Nishimura's statement shows that the BOJ is willing to learn a lesson from the United States and start using creative financial initiatives with a perspective that extends well into the future. This position indicates that within the BOJ as well there is an increasing level of interest in learning from the success of the United States.

The insincerity of Mr. Shirakawa – Self-vindication cannot be accepted

BOJ Governor Masaaki Shirakawa gave a speech in New York on April 18. He stated, "considering that the Japanese financial conditions are probably the most expansionary among developed economies, the failure of Japan to shake off modest deflation can mostly be explained by its deteriorating growth potential." Mr. Shirakawa also said that, "we should not have the illusion that there are no limits to the power of central banks.

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Central banks cannot reasonably deliver solutions to structural issues” (Source: The Yomiuri Shimbun, April 20). To put it bluntly, these words sound like the whimpering of a dog that has lost a fight. Mr. Shirakawa will probably be unable to retain this stance because of the intense criticism. There is no feeling of honestly acknowledging the success of U.S. financial initiatives and accepting responsibility for the situation in Japan. Politicians, investors, corporate executives and others who are actually responsible for what happened in Japan are unlikely to accept this posture of self-vindication by Mr. Shirakawa.

Furthermore, financial markets will probably study Mr. Shirakawa’s speech in order to try to determine what the BOJ will do next.

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