

Economic Research View:

Mr. Shigeru Ishiba becomes the New Prime Minister

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Elections for the president of the Liberal Democratic Party (LDP) concluded on September 27 with an unexpected victory for Mr. Shigeru Ishiba, who will become the next Prime Minister of Japan following a parliamentary confirmation vote on October 1.

The initial market reaction following the election result appears to have reflected his stated policy views. A snap election is reportedly set for October 27, where the LDP is expected to secure another majority. After this election, market focus will shift two main areas. First, details of Ishiba's policies. Financial market participants will reassess how his policies might affect the Japanese economy and financial markets. Second, the duration of the Ishiba administration. Since he has few allies in the LDP, if his approval rate declines he could be left with little support within the ruling party, which could lead to his early resignation.

Mr. Ishiba has a hawkish stance on monetary and fiscal policies

- Mr. Shigeru Ishiba won the Liberal Democratic Party (LDP) presidential election on September 27 (his tenure as the LDP president is three years, until September 2027). He will be nominated as the 102nd Prime Minister in the extraordinary Diet session convened on October 1.
- Following Ishiba's victory, Japanese equity prices fell, the JGB yield declined and the JPY appreciated against the US dollar. I think this initial market reaction reflected his view on monetary, fiscal and economic policies. Simply said, Ishiba has been critical of "Abenomics", a combination of expansionary monetary and fiscal policies introduced by the late Shinzo Abe. Ishiba has also opposed the Bank of Japan's (BOJ) ultra-loose monetary policies introduced under then-Governor Haruhiko Kuroda and has emphasized the importance of fiscal discipline, meaning that he takes a hawkish stance on both monetary and fiscal policies. This has caused the yen to appreciate and put dampening pressure on the JGB yield. In this regard, Ms. Sanae Takaichi, whom Ishiba faced in the second round of voting this time, has been a big supporter for "Abenomics" and has publicly criticized the BOJ's recent interest rate hikes. Therefore, had she won the election, it would have posed a challenge for BOJ Governor Kazuo Ueda.
- That being said, Ishiba has not called for a rapid normalization of the monetary policy. Instead, he emphasizes the importance of "maintaining the direction of monetary accommodations"

to “ensure the end of deflation”. Thus, he will support the BOJ’s further normalization only if inflationary dynamics warrant it.

- With respect to fiscal policy, Ishiba is likely to pursue fiscal discipline. Specifically, he mentioned the possibility of raising the corporate tax rates and increasing tax rates on investment income such as capital gains and dividends. Such tax changes could create headwinds for the economy and the equity market, and that is why the initial reaction from the equity market was a steep sell off.

Although Ishiba says his administration will “inherit the Kishida administration’s policy”, there are some difference in economic policy

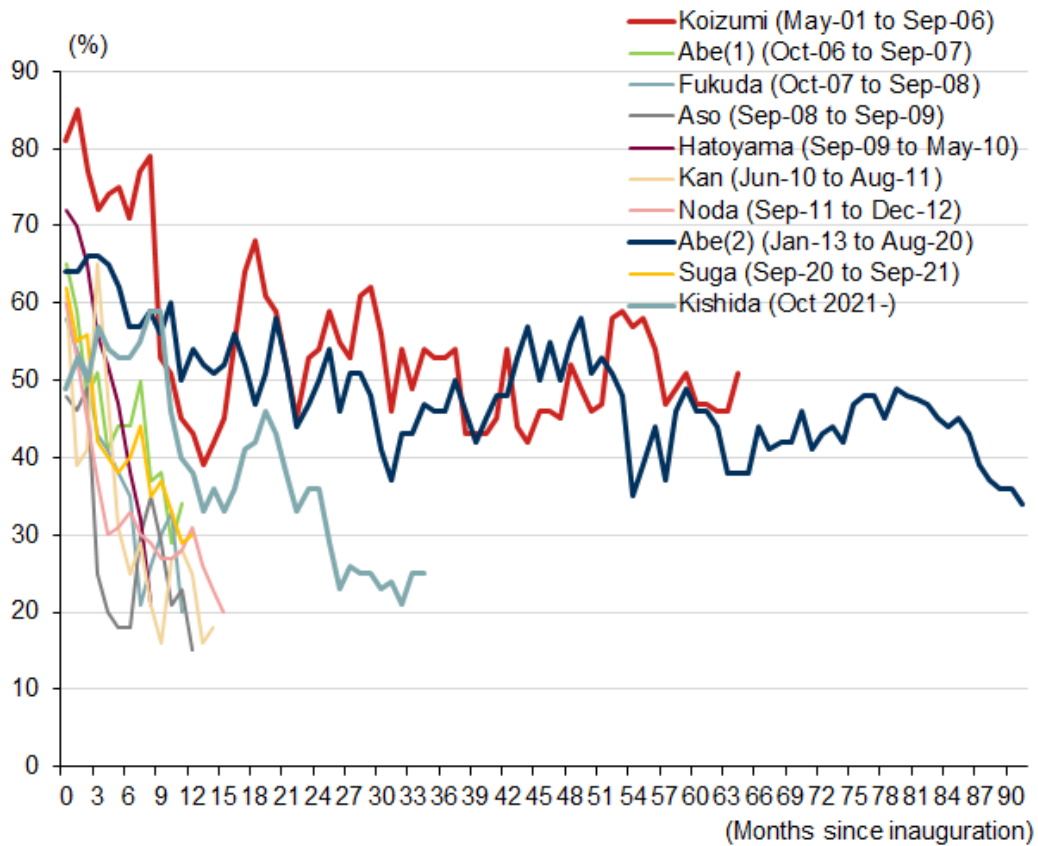
- Ishiba explained that there would be no substantial changes in economic policy, which is why he is retaining Mr. Yoshimasa Hayashi, Chief Cabinet Secretary in the Kishida administration, and will seek to “inherit the policy of the Kishida administration”.
- That being said, there are some differences between the new and former administrations. As previously explained, while Ishiba mentioned the possibility of raising the corporate tax rate and increasing tax rates on investment income, such changes were not scheduled by the Kishida administration.
- In addition, regarding wages, which are crucial for inflationary dynamics, there are two important comments from Ishiba. First, he is committed to raising the minimum wage to 1,500 yen per hour during the 2020s (it is currently 1,055 yen per hour), which is an acceleration of the schedule set by the Kishida administration (it was by mid 2030s) and will be a tailwind for sustainable wage growth. Second, unlike some of the other candidates in this election, Ishiba opposes relaxing employee dismissal regulations. I believe that the high barriers to dismissal have dampened wage growth since the 1990s, so his opposition may pose a headwind to sustainable wage growth.
- With respect to nuclear energy, although he does not oppose it, he has not actively advocated for restarting or replacing nuclear power plants. As a result, it is unlikely that the share of nuclear power in electricity supply will increase significantly, which would have the effect of reducing energy imports or shrinking the trade deficit.

A general election is likely to be held on October 27. The details of the policies and the duration of the administration will be the focus after the general election

- Following the LDP presidential election, Ishiba will dissolve the House of Representatives (lower house) to call a general election, as he said “the sooner the better”. The timing of the election is reportedly set for October 27, though it could be held in early November. As shown in Fig.1, there is a historical pattern of high approval ratings immediately after a Prime Minister’s inauguration (on average, approval ratings exceeded 50% during the first four months). Ishiba aims to hold a general election during this honeymoon period to secure a majority in the lower house.
- There are two main points of focus after the general election. First, the details of Ishiba’s policies. While the initial market reaction was not favorable, financial market participants will reassess how his policies affect the Japanese economy and financial markets as the details get clearer. In this regard, recall that, while Kishida had initially planned to increase the tax rate on investment income in 2021, he withdrew it due to the negative reaction of financial markets and opposition from the business community.

- Second, the duration of the Ishiba administration. Fig.1 shows that, after a honeymoon period, most past administrations experienced declining approval ratings, with the exceptions being the Koizumi administration (2001-2006) and the second Abe administration (2013-2020).

Figure 1. Approval Ratings of Past Administrations



Source: Prepared by Nomura Asset Management Co., Ltd., from NHK materials

Given that Ishiba is said to have few allies within the LDP, if his approval ratings drop, he may not be able to rely on much support. Therefore, the possibility of a short-lived Ishiba administration cannot be ruled out.

*This commentary is based on personal views of the author and does not necessarily represent Nomura Asset Management house view.

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