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Bank of Japan to expand the limits of QQE.
The implications.

Economic Data: 3QGDP will slow to 0.8% (no surprise)

- Final Composite PMI 49.1 vs preliminary 49.8 and falling from 51.5 in prior month.
- Final October services PMI 49.7 vs preliminary 50.3 and falling from52.8 in prior month.
- Q3 GDP growth will likely slow: The consensus forecast for Japan's Q3 GDP (due 14-Nov) looks for 0.8% annualized growth, following a downwardly revised 1.3% in Q2. Domestic demand was solid, but this is because consumers rushed to beat the consumption tax hike.

Central bank: Board members debated room for additional easing, and likely to rethink its tapering

- In fact, Kuroda reiterated last week that QQE will remain at least through spring 2020. Why? Many members expressed (in BoJ's last minutes) the view attention should be paid to the risks of a narrowing in the positive output gap (that pushes down inflation). Members recognized the possibility that the momentum toward achieving the price stability target would be lost. In plain language, this means that they will have to delay again the fulfillment of their price objective. In other words, **they will have to continue expanding the limits of the expansionary monetary policy.**
- Time to rethink Tapering? The BOJ could be on course to shrink its bond holdings next year for the first time in a decade if purchases continue to taper at the current rate, with gross purchases likely totaling ¥49.4T in 2020, compared with at least ¥55.9T in redemptions. The prospect of a fall in debt holdings may prompt the BOJ to rethink its tapering or even overhaul its policy.
- The context does not help: Kuroda dampened projections over growth, saying that “the expected pickup in global economic growth will likely be delayed”. As a result, he pointed the bank's

readiness to ease policy "without hesitation" if risks threaten to derail its inflation goal.

The consequences & Outlook

- If, as I anticipate, Japan, along with all European nations, continue to export negative yields (see how Toyota Finance has issued Japan's first zero-rate corporate bond on 25-Oct, as subzero yields spill over from government bonds to private-sector debt), this will continue to have the inevitable correspondence in the rest of the global debt market (especially in the USD denominated bond market, both in the emerging and HY universe), causing the bond yields of these issuers to continue their downward trend.
- Outlook:
    - Japanese equity: Underweight (With a +16.4% gain YTD, and considering FY19 profit growth expected at +3.1%, and PE multiple at 16x -using our 2019 EPS target-, we consider that have reached our exit point).
    - Japanese Government Bonds: Underweight. Real yields are lower in JGBs than in UST bonds, and with the 10Y JGB controlled at 0% there is little prospect that Japanese real yields will rise
    - EM bonds in USD: Overweight (specially in those countries with decreasing inflation and fiscal reforms. Preferred issuers: Brazil, Peru, India, Indonesia, Philippines and Turkey)

Best