



Interview: Intermediary Functions of Banks Have Declined — Limits of Monetary Policies Have Been Exposed

IKEO Kazuhito, Professor at Keio University

--- The Bank of Japan (BOJ), which had maintained that it would “do anything possible” to achieve the target year-on-year consumer price index increase rate of 2%, decided to adopt a negative interest rate policy.



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Ikeo: As BOJ Governor Kuroda Haruhiko said, there are still things the BOJ can do in the area of monetary policies. But that does not mean there are “effective measures” remaining. When I say “effective measures,” I am referring to policy measures that produce results which surpass adverse reactions in their own way and change the economy for the better. Whether the negative interest rate policy falls under this category is open to question. I think the latest BOJ decision actually revealed the limits of monetary policies in the sense that further easing would not be very effective. It is better for the BOJ to think about a “retreat” scenario instead of thinking about further “evolving” quantitative and qualitative easing.

--- Why do you think the negative interest rate policy cannot be viewed as “effective”?

Ikeo: The difference between interest rates in Japan and overseas (mainly those in the United States) can be expected to expand when short-term interest rates are guided into the negative range. The expanded difference will prevent the appreciation of the yen and promote its depreciation in foreign exchange markets. I think that’s the way things are. However, the prevention of the yen’s excessive appreciation aside, there is room for debate on the degree of the positive effects of promoting the further weakening of the yen and what that means for the current Japanese economy. I think it’s better to simply take advantage of the falling prices for imported products such as crude oil.

The interest rate on current deposits at the BOJ will have an adverse effect on certain kinds of revenue at private banks when the rate falls below zero. It is feared that this change will damage the financial intermediary function of private banks or their function to smoothly supply funds to



individuals and companies.

--- A negative interest rate will be applied to a portion of the money private banks place in current accounts at the BOJ. The BOJ is saying that the negative interest rate will only have a limited effect on revenue at banks.

Ikeo: Even if the negative effect on revenue at private banks is limited, that does not mean their financial intermediary functions escape unscathed. The thing that matters most for financial intermediary functions is the portion of current BOJ deposits that are made. Banks may refrain from gathering deposits as a means of response if an interest rate is imposed on the funds they gathered and deposited at the BOJ.

There are already reports that major private banks are thinking about introducing account maintenance charges on ordinary deposits made by leading companies. The introduction of these charges may cause interest rates on these deposits to fall into the negative range in effect and reduce the deposits. I feel that the intermediary functions of gathering funds and lending them are beginning to decline.

--- There are people who say that private banks will stop putting their money in the BOJ's current accounts and start lending more money when interest rates fall below zero.

Ikeo: The real reason for sluggish lending is the lack of sufficient demand from credible companies and individuals for funds in the absence of expectations for growth in the Japanese economy. It's hard to expect bank financing to expand greatly simply because the interest rate on current deposits fell from 0.1% to negative 0.1%.

--- Don't we usually see corporate financing costs go down and investment become more active when the long-term interest rates decline?

Ikeo: Financing may definitely become easier for certain credible companies. But the decline in the financial intermediary functions of private banks may gradually have a negative effect on small and medium companies that find it hard to raise funds in capital markets. Taking a look at the bigger picture, I think this risk holds more weight. As someone who has studied the functions of financial systems, this is a point that I cannot overlook.

--- What kind of monetary policies should the BOJ adopt if the switch to the negative interest rate policy proves ineffective?

Ikeo: The BOJ does not need to abandon monetary easing policies all together. I believe the BOJ must continue to hold interest rates down around 0%, taking into account the current conditions of the Japanese economy. There is little room for the emergence of new effects that overcome adverse



reactions, even if greater ingenuity is exercised on monetary policies. That is where the problem lies. This has been revealed by quantitative and qualitative monetary easing policies, through which a large volume of government bonds have been purchased. I think the quantitative and qualitative monetary easing policies with negative interest rates the BOJ introduced on this occasion will only produce similar results.

--- So what should the government do to stimulate the economy?

Ikeo: There is little room for fiscal spending, considering the serious conditions of state finance. Ultimately, no matter how tedious it may sound, the only thing we can do is to elevate the competence of the Japanese economy by honestly advancing growth strategies. Quantitative and qualitative monetary easing was a quick-term operation for achieving the year-on-year consumer price index increase of 2% in a period of about two years. The government should consider switching to an endurance contest framework now that its design has failed to materialize. Unless it does so, the only things that will grow larger are the economic side effects.

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IKEO Kazuhito

Professor at Keio University

He is a doctor of economics who graduated from the Faculty of Economics at Kyoto University in 1975. He has held his current position since 1995. Ikeo is also extremely knowledgeable of problems involving corporate governance. He is 63 years old.
