

Kishida – Japan’s 100th prime minister



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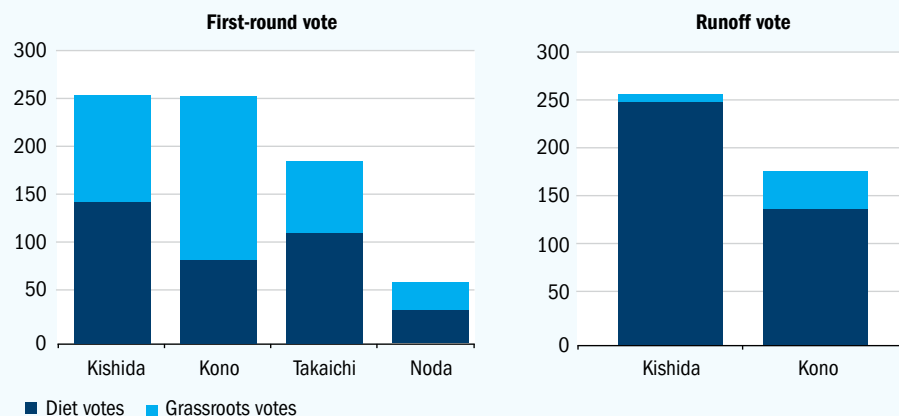
- Fumio Kishida, Japan’s 100th prime minister, represents political continuity. He looks to create a virtuous growth/wealth redistribution cycle and manage long-term challenges.
- Kishida seeks wage hikes via tax reform and supports the middle class through education/housing aid. Monetary easing policy stays, while more than ¥30 trillion additional fiscal support is expected.
- Yoshihide Suga’s departure reduces the chance of an unfavorable outcome in the lower house election for the ruling party, which bodes well for the Japanese equity market into next year.

Results of the LDP presidential election: Two surprises

Fumio Kishida won a victory in the Liberal Democratic Party of Japan (LDP) presidential election, taking 60% of votes in the runoff. Kishida becoming the next prime minister is not surprising, as consensus expected either Kishida or Taro Kono (the current vaccine minister) would be elected, but there were two surprises. The first was that even though people expected Kishida and Kono to perform a close race — as they had the most support in public polls by far — the outcome showed a wide margin.

The second surprise was that in terms of Diet votes, Kono was elbowed into third position after a very strong showing for Sanae Takaichi, the former internal affairs and communications minister and a strong believer of Abenomics. Not only does this imply she will be set for a senior position in the new Cabinet, it also implies she may be one of the strongest contenders for the first female prime minister in due course.

► **Figure 1: The vote**



Source: www.jimin.jp/news/information/202062.html, 09/29/21.

Who is Kishida and what are his policy agendas?

Fumio Kishida (64) hails from a political family and is a distant relation to former Prime Minister Kiichi Miyazawa. He was formerly a banker and had previously lost to Suga in last year's leadership election. Kishida has held key roles in the Japanese government, such as minister of foreign affairs, minister of defense, and chairman of the Policy Research Council Board — which is one of the key positions to obtain the qualification to lead the LDP.

People close to him characterize Kishida as a rather quiet, unassuming but well-balanced person. This is not a bad thing domestically, as he seems to have a good rapport with bureaucrats across the ministries. More interestingly, former Prime Minister Shinzo Abe essentially delivered this victory to Kishida by cleverly scheming behind the scenes while supporting Takaichi on the surface. Given the delicate political tactics behind the scenes, Abe may have influence over Kishida's policies going forward as the kingmaker.

Monetary and fiscal policy

Kishida has confirmed plans to maintain expansionary fiscal and monetary policies. We expect the imminent supplemental budget announcement (expected to be approximately ¥30 trillion) should further support the economy and therefore corporate profits. The state of COVID emergency measures have just been lifted in Japan and as social distancing measures are relaxed further, we can expect a pickup in reopening activities to support the recovery in the service economy.

Kishida looks to restart the “Go-to-Travel” and “Go-to-Eat” campaigns (budgeted at ¥1.3 trillion) to help reignite economic activities in industries such as retail, restaurant, travel and entertainment. On the monetary policy side, we expect Kishida to support the Bank of Japan's (BoJ) current monetary easing policy to get the domestic economy back on track from the COVID shock. Kishida clearly mentioned during his campaign that he will work with the Bank of Japan to achieve the 2% inflation target; however, we shouldn't forget that a Kishida government is likely to propose the next BoJ governor in April 2023. Moreover, Kishida has previously voiced doubts over the BoJ's excessively accommodative monetary policy.

Wealth redistribution policy

There are a few key themes, such as redistribution of wealth, COVID, disaster preventions, energy and digital transformation, which help to understand more about what Kishida wants to achieve. While Kishida highly values Abenomics in terms of GDP/corporate profits recovery and job/wage growth, he argues that these benefits haven't effectively trickled down to the middle class. Kishida has advocated the need to redistribute wealth since Japan's economic policy has led to an excessive gap between rich and poor. He believes making the middle class bigger and stronger is key for sustainable economic growth in Japan, as the middle class is the major driver of consumption.

Kishida's idea is to reallocate a portion of tax revenues from investment income to subsidize areas such as education and rental housing expense in order to generate a

middle-class second wind. Large corporations would be required to fairly distribute earned excess profits to employees, business partners and shareholders. Kishida is also aiming for a wage hike for poorly paid workers in strenuous jobs, such as caregivers, nurses and childcare workers.

He also plans on ¥15 trillion of investments for natural disaster preventions over the next five years and has called for greater support of companies in technology and innovation as he looks to create a “digital garden city” or digitalization society if you will — aimed at revitalizing regional economies through digitalization.

There are also several measures dedicated to the science and technology fields. One is the ¥10 trillion university fund to generate funding to support academic research infrastructure; the other is to establish a science and technology adviser under his direct supervision. A direct impact on growth is hard to quantify at this moment, but it does highlight his focus on scientific and technological innovation.

Energy policy

Energy is another area to keep our eyes on. Policy on carbon neutrality has material implications for the Japanese economy. According to the Global Energy Policy Research, reducing CO2 emissions by 46% by 2030 (which current Prime Minister Suga presented at the UN Climate Action Summit) is going to create a burden of more than ¥20 trillion annually if solar power alone were used. This would likely be a material drag on the Japanese economy through a higher carbon tax and expensive electricity bill. Given this backdrop, Kishida has highlighted the importance of the fuel recycling policy and is looking to restart reactors and preserve Japan's nuclear technology. While Japan faces a relatively high risk from earthquakes, Kishida's nuclear policy stance is well supported by the business community.

Foreign policy

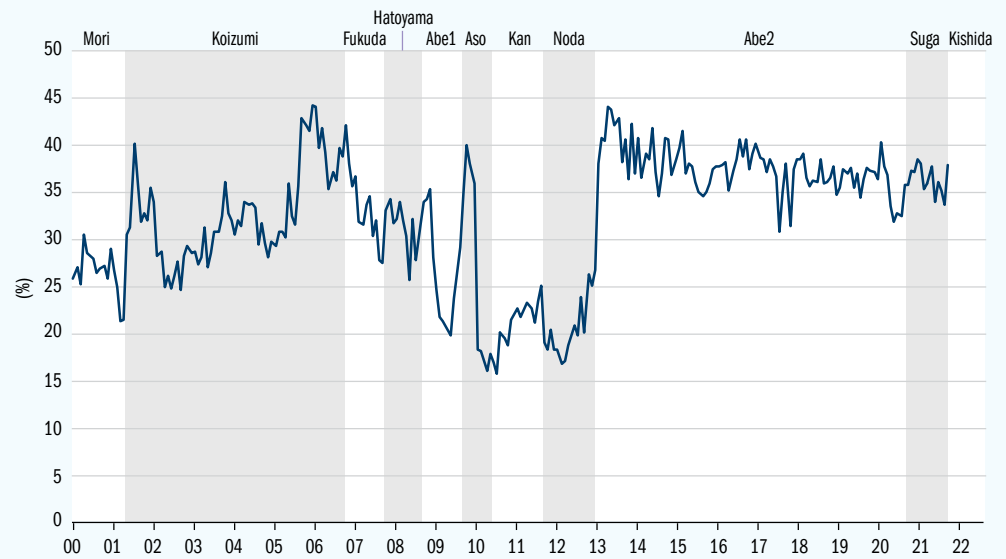
Kishida had held key positions on the diplomatic front, as the longest serving Minister of Foreign Affairs and as Minister of Defense. He put a high priority on a strong alliance with the U.S. and is concerned about China's aggressive military actions these days. While he has advocated continuing dialogue with China, he has also promised to take a harder line with the military. He has supported boosting Japan's defense budget amid increases in Chinese activity in the East China Sea.

Upcoming election of the House of Representatives is key for equity market

As we wrote in a recent piece on Japanese politics,¹ despite the change in prime minister, the outlook for Japan's political landscape should be viewed as positive by investors as it is likely that a ruling coalition (LDP + Komei Party) continues to hold a majority. Judging from the fact that, in all polls, support for the LDP snapped back by around 8–10 points after Suga announced he would not run for the LDP presidential election, the LDP is likely to get through the upcoming general election.

Japan's equity market has been sensitive to election results for the House of Representatives historically and defines the administration's stability going forward. The Japanese equity market has historically performed well before and after the general election — certainly in the last 14 elections since 1979. The Topix index posted positive returns, with a 93% chance one month into the general election, and a 57% chance for six months and for 12 months after the election.² We believe this could be a catalyst for Japanese equities to further appreciate from here after already generating around a 15% return year to date, in local currency terms.

► Figure 2: LDP approval rating



Source: NHK, SMBC Nikko, 09/29/21.

If the LDP were able to retain its single majority, we can expect a positive market reaction. Providing the coalition party (LDP + Komei) doesn't lose more than 72 seats — a scenario we now view as unlikely given the imminent exit of the increasingly unpopular Suga — the risk/return trade-off on Japanese equity returns looks encouraging. Undemanding valuations coupled with the expected economic normalization from rapidly rising vaccination rates should also help.

The schedule for the general election hasn't been announced, but Japan's Constitution and Public Offices Election Act require it to be held by November 28 at the latest.

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¹ Topix hits 30-year high as PM Suga announces resignation, Columbia Threadneedle Investments, September 2021.

² Past performance does not guarantee future results.

Past performance does not guarantee future results. It is not possible to invest directly in an index.

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