Deloitte.
デロイト トーマツ

トーマツ.

'This newsletter is translated from the Japanese edition distributed on February 23rd.
Center for Risk Management Strategy at Deloitte Touche Tohmatsu LLC.

# Global Risk Watch Newsletter

## Will 2018 also be the year of fiscal policy?, etc.

Global Risk Watch Vol.35
28 February 2018

==========================================================================

≪index≫

1. # Will 2018 also be the year of fiscal policy? (Tsuyoshi Oyama)
2. # Enhanced cryptocurrency regulation (Shiro Katsufuji)
3. # Will the Big-Boned Policy point to fiscal reforms? (Toshikazu Kumagai)
4. Seminars, Conferences & Publications

==========================================================================

### 1. Overview Macroeconomic and Financial Risks (Trends & Topics)

**# Will 2018 also be the year of fiscal policy? (Tsuyoshi Oyama, Partner/Head of Center for Risk Management Strategy (CRMS) at Deloitte Touche Tohmatsu LLC/Deloitte Asia Pacific Risk and Capital Management Leader)**

Some of my readers might be a little confused by this month's title – "Will 2018 also be the year of fiscal policy?" as I had just last month I asked "Will 2018 be the year of monetary policy?" This is not necessarily me changing my mind, but instead it means that both monetary and fiscal policies are likely to be facing significant changes during this year in a somewhat combined manner.

Recently, we observed clearer signs of the price and wage rises in the US that I spoke about last month, and they have finally sparked the long awaited, or even feared, adjustment to both the high prices of asset markets (including both the stock and bond markets) and a jump .in long-term interest rates. Still, even though the current US ten year bonds rate is around 2.9%, this is much higher than last year's rates which were lower than 2.5%. Real interest rates remain very low, from a historical point of view. Consequently, we saw a large correction in stock prices, but this fall was, in general, quickly followed by recovery. As well, while there were worries over the impact of US long-term interest rate rises on the currencies of emerging economies, the current exchange rates have kept relatively calm. All of this is to say that the impact of rate rises was not yet big enough to trigger an upset of the global apple cart.

The show has not yet ended, however. The next act may be a US inflation rate that actually confirms rates rises are accelerating. It was the sharp +2.9% YoY rise in wages, reported in early February, which sparked the recent large-scale stock price correction. Following on that, we saw the core CPI move +0.35% MoM after January's high rise. Also, the negative effect on YoY CPI due to the decline in mobile phone service prices since March 2017 will be lessened from March 2018, which will probably accelerate this rise even more. Moreover, the mid-to-long-term trend in the US budget deficit is even more worrying for long-term interest rates. In addition to the large-scale corporate and individual tax cuts passed at the end of last year, the Democrats and the Republicans agreed to drastically increase the limits of government spending. While the agreement (and the dodged government shutdown) could be seen as good news, when considered with the tax-cuts the outlook for the American budget deficit is definitely problematic. On top of all of this, President Trump also announced a USD 1.5 trillion infrastructure spending package in his recent State of the Union address.

Looking around the world, the US is not the only country that is rapidly expanding its budget deficit. Emerging economics like India and the Philippines are spending vast sums on infrastructure investments. This may not stop at budget deficits, but will also greatly, and negatively, impact the current accounts balances. The same trend might also be seen soon in other countries such as Mexico, Brazil, and Italy – countries that are having a big election in the coming months and could elect populist leaders. As well, China has not been able to curb the problem of growing budget deficits of local governments. And finally Japan, the country with the world's largest government debt to GDP ratio, is pushing the deadline for reaching a primary balance surplus further and further into the future. As the government passes the largest supplementary budget in these times of plenty, we can see Japan's fiscal discipline get laxer and laxer.

When seen in this light, the theme for 2018 is not only how monetary policy will be normalized after price rises accelerate, but also how much long-term interest rates will increase as a result of loosened fiscal policy. In this year, we might see some answers to the questions of whether aggressive public spending will mitigate the lengthy global saving glut, or whether a superheated economy and budget deficits instead spark a jump in long-term interest rates, putting an abrupt end to the current goldilocks situation.