BoJ could be blowing a big bubble, says expert

Philip Baker and Vesna Poljak

Andy Xie: quantitative easing is not the answer for Japan. PHOTO: LOUISE KENNERLEY

Highly regarded China expert **Andy Xie** has warned monetary policy alone can't solve Japan's economic growth problem, and thinks the latest round of quantitative easing by the Bank of Japan could end in chaos.

Plans by the BoJ to pump $US1.4 trillion of new cash into its economy – or around 30 per cent of national output – over two years to get their economy moving is a major reason why the Japanese yen is down about 20 per cent against the US dollar since late last year, and the country's sharemarket up around 40 per cent over the same time frame.

But Mr Xie believes it is not going to solve any of the problems and the better way out for Japan is structural reform to revise productivity.

"What the BoJ is doing is forcing the big Japanese insurance companies and pension funds to go abroad," Mr Xie said. "They are being screwed. With such a huge amount of funds in the Asian region the theory is they have to go to the Nikkei or US treasuries and the hedge funds are front running that. What it means is the yen will collapse like the Russian rouble in 1998. What the central bank is doing is they can't see the end game, but the end game is chaos."

Mr Xie doesn't see the need for emergency measures to solve deflation because the economy is showing signs of self-correcting anyway.

The savings surplus has hurt Japan, Mr Xie said. Japan has a trade deficit, but in two years' time it will have a current account deficit.

Japan's problem right now is that the country has not seen this kind of sustained deflation since the 1930s, prompting the radical action by the BoJ. Mr Xie said no other economy does a bubble quite like Japan.

"Japanese people have a bubble once every 50 years. It's not like Chinese people, they have a bubble every 10 months, but once Japan does have a bubble they do it really big," he said.

It is foreigners who are driving down the yen and buying the Nikkei but eventually they have to unload these trades to Japanese investors.

Mr Xie also thinks the Australian dollar could fall to as low as US75¢ to US80¢, which is its more natural level, and that floor could cause a 20 per cent drop in the local housing market.

Commodities are heading towards a prolonged bear market and Chinese demand is likely to be stagnant as economic growth eventually falls to around 5 and 6 per cent.

However, the uncertain outlook for the world's second-largest economy is one reason why Mr Xie thinks the recent sell-off in gold is tipped to be brief.

The amount of money printing by central banks is poised to go beyond the normal threshold and he expects gold to achieve new highs.