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Feature Articles

This month's focus: **"Asset Management under a Low Interest Rate Environment"**

This paper aims to evaluate the negative interest rate policy introduced by the Bank of Japan in early 2016. It starts with discussion of the failure so far of the qualitative/quantitative easing of the Bank of Japan to reach the inflation target of 2%. The paper goes on to analyze theoretically the limit of negative interest rates and then reviews the effects on the economy so far by comparing Japan's experience with that of Europe.

Five European central banks have introduced a negative interest rate policy. Although the aim is to revive economic activity through a lower shift in the yield curve and currency depreciation, the new policies are not able to increase bank lending to firms and indeed lead to diminishing profitability on the part of banks. My estimation shows that the ECB could not prevent the euro depreciating against the US dollar by cutting the monetary policy rate. We must thus take into account that the role of interest rates has changed when in negative territory, and rebuild economic and financial models applying the new paradigm.

In 2016, BOJ adopted a negative interest rate policy with quantitative/qualitative monetary easing. As a result, the yield curve of JGBs flattened over ultra-long durations. With BOJ's huge purchases of JGBs from the markets, the liquidity of secondary markets has been adversely affected. Moreover, institutional investors with long liabilities, such as life insurers and pension funds, face difficulties in terms of the asset liability management of their institutions.

