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All Signal, No Noise

MARKET ANALYSIS

MNI BoJ Review – July 2025

Meeting Date: Wednesday July 30 to Thursday July 31, 2025.

Link To Statement: https://www.boj.or.jp/en/mopo/mpmdeci/mpr_2025/k250731a.pdf

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MNI Point Of View: Cautious Amid Trade Uncertainty

The Bank of Japan (BoJ) concluded its July 30–31 Monetary Policy Meeting (MPM) by keeping its benchmark interest rate unchanged at 0.50%, in line with market expectations. The decision was unanimous (9-0), signaling broad agreement within the Policy Board to adopt a cautious approach amid persistent uncertainty surrounding the economic impact of U.S. tariffs and the inflation outlook.

While business sentiment has improved following last week's US-Japan trade deal, Governor Kazuo Ueda made clear that the central bank remains in "wait-and-see" mode. The BoJ is closely monitoring how the newly imposed 15% US tariffs will influence Japan's exports, corporate profits, and broader activity. Although the agreement has reduced some uncertainty, Ueda emphasised that the full implications will take time to materialise.

In the press conference following the meeting, Ueda noted that underlying inflation has not yet reached the 2% target and reiterated the need for more data before considering another rate hike. He downplayed the risk of falling behind the curve, stating that wage and price dynamics must be firmly established before further tightening. He stressed the importance of confirming that wage gains are sustainably feeding into price increases—an essential condition for the BoJ's inflation-targeting framework.

The BoJ's quarterly economic outlook was somewhat more optimistic about the second half of the fiscal year (October 2025 to March 2026), citing expected wage growth and eventual improvement in economic activity. However, it struck a cautious tone on near-term momentum. The report warned that Japan's growth is "likely to moderate" due to trade-related headwinds and weakening global demand, expected to depress corporate profits and weigh on exports in the short term.

Despite this near-term pessimism, the Bank slightly raised its growth forecast for FY2025 and revised up its inflation outlook across FY2025–FY2027, largely due to persistent food price increases and expectations for rising wages. These revisions, however, were modest and insufficient to trigger a policy shift.

The BoJ's reluctance to commit to a rate hike timeline contrasts with earlier market expectations. Some analysts had anticipated a more hawkish pivot in July, possibly setting the stage for an October hike. This view was based on assumptions that the BoJ's earlier pessimism in May was an overreaction to tariffs. Yet Ueda carefully avoided signaling any change in trajectory, reinforcing the Bank's risk-averse stance.

We maintain our baseline forecast that the next rate hike is most likely to occur at the January 2026 MPM. By then, the BoJ will have accumulated several months of post-trade deal data and be better positioned to evaluate the tariffs' impact on the economy and inflation. To that end, the Bank will likely need confirmation that the new tariffs are not significantly derailing Japan's growth path, and evidence that wage growth momentum remains intact, even amid possible declines in corporate earnings.

That said, risks to the timing of the next rate hike are two-sided. Should external conditions worsen—such as further tariff escalation or a broader global slowdown—a delay into mid-2026 is plausible. Conversely, if downside risks from trade prove manageable, or if the yen depreciates sharply, the BoJ may hike earlier than anticipated.

Some analysts also believe domestic politics could influence monetary policy direction. The ruling LDP's plenary session on August 8 may set the stage for an early party leadership election following recent electoral setbacks. While Prime Minister Ishiba is not expected to be immediately ousted, political uncertainty could constrain the BoJ's ability to signal a near-term policy shift. Once the political environment stabilises post-August and if economic conditions remain resilient, they argue the BoJ could begin laying the groundwork—possibly through media briefings—for an October rate hike.

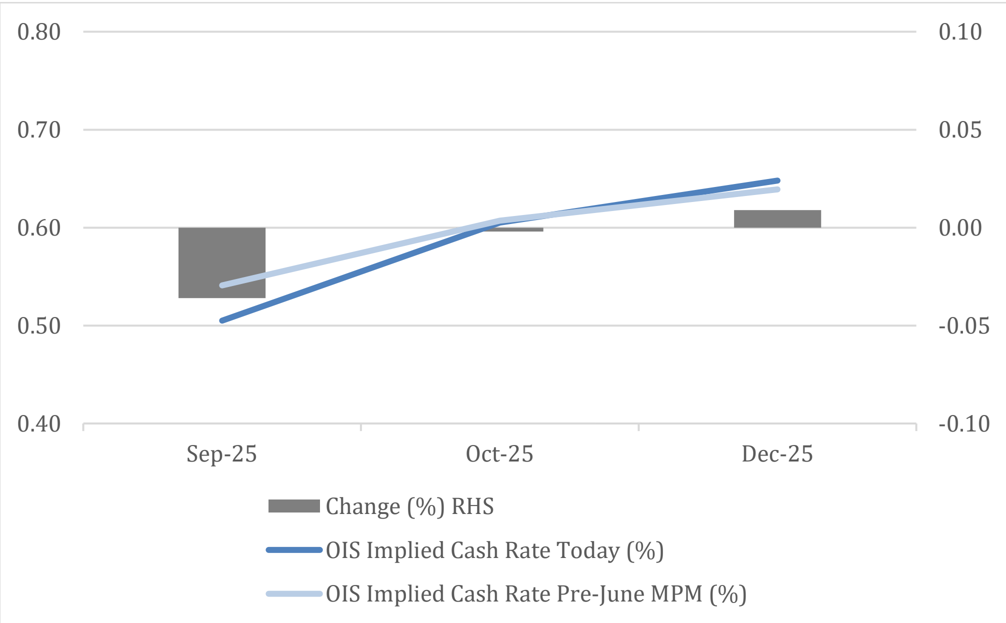
In short, while the July MPM brought no policy changes, it reinforced the BoJ's cautious, data-dependent stance amid complex trade dynamics, subdued inflation, and political uncertainty. The bar for another rate hike remains high, but not insurmountable, especially if wage and price dynamics continue to improve and external risks moderate.

BoJ Market Pricing: Two Thirds Of A Hike Priced By YE

At the time of writing, BoJ-dated OIS pricing was little changed versus yesterday's pre-MPM levels and slightly mixed across meetings compared to pre-June MPM levels, reflecting continuing uncertainty regarding economic growth, driven largely by recent external shocks — particularly changes in US tariff policy.

- Markets had been positioned for a cautious, wait-and-see approach from the BoJ at this meeting.
- Current OIS pricing implies just a 11% probability of a 25bp hike in September, rising to 40% by October and 68% by December — a notable shift from mid-February, when a hike by September was fully priced in.

Figure 1: BoJ-Dated OIS – Today Vs. Pre-June MPM



Source: Bloomberg Finance LP / MNI

MNI BoJ WATCH: Ueda Says To Gradually Raise Rates

By Hiroshi Inoue
Jul 31, 2025

TOKYO - Bank of Japan Governor Kazuo Ueda maintained his stance of gradually raising the policy interest rate after the BOJ earlier on Thursday unanimously kept it unchanged at 0.5% as widely expected on the back of high uncertainties over the outlook for output and inflation, but he gave little guide as to timing, insisting that the decision will be data-dependent.

The BOJ could consider raising the policy rate if the likelihood increases that underlying CPI inflation is anchored around 2%, even if it remains slightly below that level, Ueda told a news conference.

"Underlying CPI inflation hasn't risen to 2% but it is rising steadily but slowly, and moving toward 2%," Ueda said, adding that U.S. tariffs would put downward pressure on the economy and inflation, though the scale of that impact is still hard to discern, with data distorted by front-loading. (See MNI POLICY: Uncertainty Pushes Back Likely BOJ Hike Timing)

The Bank revised up its median projection for inflation this fiscal year to 2.7% from the 2.2% envisaged in April, mainly due to higher rice prices, and changed its assessment of the balance of risk to prices to "generally balanced", from the downside risks perceived in April.

WAGE HIKES

The current yen-dollar exchange rate, at around JPY149.50, is roughly in line with the BOJ's assumptions, Ueda said, though he added that Bank continues to carefully monitor forex moves and their impact on economic activity and prices.

Wage hikes for fiscal 2026 will be a key determinant for BOJ policy, and Ueda said that upward pressure on pay from labour shortages and this year's higher inflation must be weighed against a drop in profits, particularly at major manufacturers, caused by a slowing global economy. (See MNI POLICY: BOJ Expects US Tariffs To Pressure Japan Profits)

There is little risk that the BOJ will fall behind the curve in tightening policy, Ueda said, adding that the Bank maintains its stance of gradually raising the interest rate if underlying CPI inflation converges toward the 2% price target as projected, with real interest rates staying at low levels.

In its Outlook Report, the BOJ raised its median inflation forecasts for fiscal 2026 and 2027 to 1.8% and 2.0%. from April's 1.7% and 1.9%, respectively.

The next policy-setting meeting is scheduled for Sept 18-19.

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Sell-Side Views

CIBC: "The Bank of Japan left rates unchanged at 0.50% as widely expected, with the 9-0 vote indicating little (if any) debate within the MPC. Although business optimism has grown in the wake of last week's US-Japan trade deal, a July hike was never really on the table. We and other forecasters viewed this meeting as "too soon" amid uncertainty on how 15% US tariffs will impact Japanese activity and data."

- The BoJ's updated quarterly outlook maintained a relatively downbeat tone on current economic momentum but was more optimistic on the 2nd half of the current fiscal year (from October 2025 through March 2026). The first line of the economic outlook warned that "Japan's economic growth is likely to moderate, as trade and other policies in each jurisdiction lead to a slowdown in overseas economies and to a decline in domestic corporate profits." After the near-term tariff-induced slowdown, however, the outlook notes that "Japan's economic growth rate is likely to rise."
- "In our view, Ueda's comments on CPI forecasts and policy reaction are not surprising. As we reiterated in the July 25th FX Weekly, the BoJ does not place high importance on monthly CPI readings. The central bank's main focus continues to be wage inflation. Despite the fact that monthly core CPI is still well above 3%, Governor Ueda still reiterated today that "the underlying price trend is rising but still below 2%." That comment does acknowledge incremental gains – Ueda noted that underlying inflation will keep strengthening. However, his other comments still indicated lingering uncertainty, particularly on tariff impacts. The outlook still noted that there is "high uncertainty" on how trade policies evolve – that is a slight upgrade from April/May, when the BoJ assessed global trade policies as having "extremely high uncertainty."
- "On the tariff-side, Ueda maintained a "wait and see" message, similar to Fed Chair Powell hours earlier. The governor noted that the BoJ will be closely monitoring developments to see how the 15% tariffs impact activity data. On the positive side, both Ueda and the quarterly outlook noted that rising wages are expected in the second half of this fiscal year (from October 2025 through March 2026)."
- "As such, we maintain our view for a January 2026 hike. Even though Ueda was positive on the US-Japan trade deal, he also noted that he did not think the "fog around tariffs" will suddenly clear. By waiting until January, the BoJ will have several months of post-trade deal data to observe."

Goldman Sachs: "The Bank of Japan (BOJ) held its Monetary Policy Meeting (MPM) on July 30-31. As was widely expected, it decided to maintain its policy rate guidance at 0.5%. At the press conference following the policy meeting, BOJ Governor Ueda said that uncertainties receded somewhat with the US-Japan trade agreement reached, and the conviction in realizing the BOJ's economic and price outlook has increased to some extent. That said, he explained that, although a trade agreement has been reached, Japan faces higher a tariff rate, and the effect on the Japanese economy and prices is highly uncertain. Given the higher tariffs, he stated that the BOJ's central outlook calls for a slowdown in growth and a softer underlying inflation trend, which will likely be confirmed in hard data going forward."

- "Questioned on whether rate a hike would be possible amid deteriorating hard economic data and a softening inflation rate, Governor Ueda explained that important factors in judging the next rate hike would be whether the moderate wage and price rises generated by the mechanism of wage growth feeding into inflation and circling back to wage growth again is not jeopardized amid a temporary deceleration in wages and inflation. Usually, the previous year's inflation rate is referenced at the annual shunto spring wage negotiation. We think, therefore, that Governor Ueda's remarks imply that when judging the timing of the BOJ's next rate hike, it will be important to affirm that underlying inflation is moderately rising, reflecting wage growth and the momentum of next year's shunto wage agreement."
- "On underlying inflation, Governor Ueda referred to the BOJ's calculated weighted median CPI, trend component in the CPI for services as examples of underlying inflation indices, as well as medium-to-long term inflation expectations. He noted that most of these measures are moderately rising but have not reached 2% yet, although he said the effect of rising food prices on them needs more attention than in the past. He repeated that he sees little risk of the BOJ falling behind the curve."
- "Considering all the above, we expect the BOJ to opt to maintain the policy rate as a precautionary measure for the time being. With underlying inflation and long-term inflation expectations not yet reaching

2%, and no sign of any financial imbalance, we see no particular need for the BOJ to urgently raise rates. With uncertainties still high, we think the BOJ is likely to maintain its wait-and-see stance from a risk management perspective. The January 2026 MPM remains our base case for the next rate hike.
- "We believe there are two prerequisites for the BOJ to hike again. The first is for the BOJ to confirm that the impact of tariff increases on the real economy is not that large, or that Japan's economic growth trajectory will not be derailed by the impact."
- "We believe the BOJ will also want to confirm wage growth momentum despite a deterioration in corporate earnings due to tariff increases. The BOJ focuses on underlying inflation in its conduct of monetary policy, and base pay increases in the shunto spring wage negotiations are closely related to underlying inflation. Wage increase momentum in next year's shunto negotiations can be confirmed at the earliest from the end of the year to the beginning of next year, after the December 2025 MPM."
- "However, uncertainties surrounding the timing of the next rate hike are high. Depending on US tariff policy and overseas economic developments, the next hike could be delayed. On the other hand, if the downward pressure on wages and prices (via the impact of higher tariffs on the real economy and lower corporate earnings) is not as strong as the BOJ fear, or if the yen were to depreciate rapidly, the next rate hike could be sooner than anticipated."

JPM: "The BoJ kept the policy rate unchanged and revised its inflation outlook and risk balance upward, as widely expected."

- "The Outlook Report shows a clear retreat from the significant pessimism observed in May, as we had expected. Inflation forecasts have been raised, with the projection for FY2025 significantly revised upward by 0.5%-pt to 2.7%oya. The forecast for FY2026 has also been revised up by 0.1%-pt to 1.8%. The fact that this remains below the 2% target helps justify the BoJ's decision not to implement a rate hike at this meeting."
- "The risk assessment in the Outlook Report has also been revised up in various respects. The uncertainty surrounding trade policies, previously described as "extremely high," has now been adjusted to simply "high," and the risk concerning the inflation outlook, previously considered to be "skewed to the downside", has been revised to "generally balanced". In fact, the risk balance indicated by the Policy Board members has shifted from a significant downside risk at the previous meeting to a more balanced view. Additionally, regarding the overseas economic and price outlook, upward risks brought about by the recent moves toward fiscal expansion in the US and Europe, which were not mentioned in the previous report, have now been addressed."
- "In the press conference, Governor Ueda clearly avoided indicating the timing of the next rate hike. He reiterated the BoJ's policy that the Bank would continue to raise rates as confidence in achieving the 2% inflation target in the medium to long term increases. Although he stated that the likelihood of achieving the inflation outlook had improved compared to the previous meeting, he remained vague about the points he wanted to confirm before the next rate hike. At the same time, he also repeated the argument introduced in May that the momentum of underlying inflation might temporarily stall in the coming quarters, suggesting that the upward revision of the inflation outlook for FY2025 alone would not determine the direction of monetary policy, thus downplaying the revisions in the Outlook Report. Amidst this, many media reports questioned whether the BoJ's rate hikes were lagging, reflecting domestic dissatisfaction with recent high inflation and yen depreciation, as well as calls from the business community for inflation control through rate hikes. The Governor reiterated that the risk of the BoJ falling behind the curve is not high at the moment, but it is extremely unusual for so many questions from reporters to demand rate hikes from the BoJ."
- "The main rationale supporting the BoJ's delay in rate hikes seems to be the outlook that inflationary pressures will weaken due to a deterioration in global demand. Governor Ueda stated that, regarding the impact of tariffs on the Japanese economy, he is not particularly concerned about the direct impact of higher tariffs on Japanese industries themselves, but rather places more emphasis on the pathway through changes in U.S. demand. If this is the case, what the BoJ is focusing on is likely the trajectory of global demand. However, this hurdle does not seem particularly high. The Governor also mentioned that even if growth slightly underperforms, the current low level of policy rates must be taken into account. Thus, we think the condition for the BoJ's additional rate hikes is likely that the economy does not fall into recession even if global demand slows down."

Societe Generale: “The BoJ maintained its policy rate at 0.5% at today’s meeting. In addition, the bank released its Outlook for Economic Activity and Prices, i.e. the Outlook Report. The growth forecast for FY25 was revised up slightly, while these for FY26 and FY27 were unchanged from the May forecasts. In addition, the core CPI forecast for FY25 was revised up significantly to 2.7% from 2.2% in April, due to food inflation. The FY26 and FY27 figures were also revised up slightly.”

- “Moreover, there were some changes vs the previous statements. The BoJ replaced the word “extreme” with “high” regarding the level of uncertainty in foreign trade policies and economies. In addition, the inflation risk balance was adjusted upward to “generally balanced” from “downside for FY25 and FY26”and the BoJ also started to mention the inflationary impact from rising labour & logistics costs, factors that we have consistently pointed out.”
- “In the press conference, Governor Ueda said that the likelihood of achieving 2% underlying inflation was slightly greater than its May Outlook Report. Moreover, he also said that downside risks to the economy still remain, as the full impact of tariffs has yet to be confirmed, but that the primary focus would be on upside risks to prices.”
- “Going forward, we continue to expect the BoJ to raise its policy rate in October. Given the current steady progress in underlying inflation, one possible trigger for a rate hike would be whether the FY26 growth forecast, as announced in the October Outlook Report, approaches the 1% level seen in January. Given agreements on tariff negotiations and future economic measures, we expect the FY26 growth forecast may approach 1%.”
- “Going forward, we continue to expect the BoJ to raise its policy rate in October. Given the current steady progress in underlying inflation, one possible trigger for a rate hike would be whether the FY26 growth forecast, as announced in the October Outlook Report, approaches the 1% level seen in January.”

TD: “Despite the US-Japan trade deal, the BoJ remains cautious as the Bank emphasized that it wants to assess the impact from tariffs in the hard data. We suspect politics is the larger factor at play for the dovishness as Japan is in a tricky political period after the ruling coalition lost the Upper House election. Next key event is the LDP's plenary session of its Parliament members on August 8 and once the political situation settles, the BoJ can always voice its opinion for an October hike through media leaks.”

- “Governor Ueda also struck a dovish tone during the press conference, emphasizing that the BoJ wants to assess the economic impact from the 15% US tariffs that was agreed upon in the US-Japan deal. We suspect politics is the larger factor at play for the dovishness as Japan is in a tricky political period after the ruling coalition lost the Upper House election.”
- “Next key event is the LDP's plenary session of its Parliament members on August 8. Rumor is that the agenda for the meeting is to push for an early party presidential election to replace PM Ishiba after his back-to-back losses in the Lower and Upper House elections. We don't expect PM Ishiba to be forced out as he still has support from the LDP rank and file members.”
- “We still maintain our call for an October hike as we suspect political uncertainty is restraining the BoJ from actively voicing that a rate hike is on the table soon. Once the political situation settles after August 8 and if the Japanese economy holds up well, the Bank would likely give ample notice (through media leaks) that it is considering an October hike.”
- “Questions on fiscal policy were also fielded and Governor Ueda commented that it will examine the impact of fiscal policy once decided. In our previous note, we warned that fiscal deterioration risks are being priced in by markets given the current political situation, but we doubt the BoJ will put off hikes to suppress yields as these long-term yield moves should be separately tackled by the MoF.”