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All Signal, No Noise

MARKET ANALYSIS

MNI BoJ Review – June 2025

Meeting Date: Monday June 16 to Tuesday June 17, 2025.

Link To Statement: https://www.boj.or.jp/en/mopo/mpmdeci/mpr_2025/k250617a.pdf

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MNI Point Of View: Few Surprises Although QT Taper Mildly More Dovish

At its latest policy meeting, the Bank of Japan (BoJ) decided to keep its policy rate unchanged at 0.50%, a move fully expected by markets and consensus economists. The decision was made by a unanimous 9-0 vote from the Monetary Policy Committee (MPC), reflecting little internal debate about near-term rate hikes.

The primary focus of the meeting was the pace of quantitative tightening (QT) beyond the near term. The BoJ confirmed it will continue reducing its Japanese Government Bond (JGB) purchases by ¥400 billion per quarter through the first quarter of 2026. However, from the second quarter of 2026 through the first quarter of 2027, it will slow that pace to ¥200 billion per quarter, a decision backed by an 8-1 vote. The lone dissenter, Naoki Tamura, advocated for maintaining the faster ¥400 billion taper to allow market forces to play a greater role in determining long-term interest rates.

This slightly more dovish outcome was not unexpected, as markets had been prepared following prior guidance and signals from the BoJ's Bond Market Group. Governor Kazuo Ueda clarified during his press conference that no decisions have been made regarding the bond purchase plan beyond the second quarter of 2027, and that further plans would be discussed during the interim review in June 2026.

In the JGB market, attention is increasingly focused on the steepening yield curve, particularly in super-long maturities. 30-year and 40-year JGB yields reached record highs in May, driven largely by a supply-demand imbalance. As the BoJ continues to taper its purchases, increased supply has not been met with enough demand from institutional investors, leading to elevated yields in the super-long sector.

The BoJ's policy statement maintained its existing economic and inflation outlook, aside from technical changes to incorporate recent higher inflation prints. Governor Ueda reiterated during his press conference that there had been no major change in the structure of the Japanese economy or inflation dynamics since the last update in May. This continuity aligns with Ueda's past communication style, which tends to stick closely to the published outlook.

Importantly, Ueda stated that the BoJ may consider raising interest rates without needing to see clear-cut new signs of rising inflation, should the economic outlook and forecast trajectory warrant such action. This comment indicates a slightly more flexible approach to future tightening, even if near-term policy remains steady.

He also highlighted ongoing external risks, particularly from unresolved US-Japan trade tensions. Despite negotiations, the two countries have yet to reach an agreement, with Japan particularly concerned about potential US tariffs on autos—a sector that plays a key role in Japan's GDP, employment, and is a bellwether for wage trends across the economy.

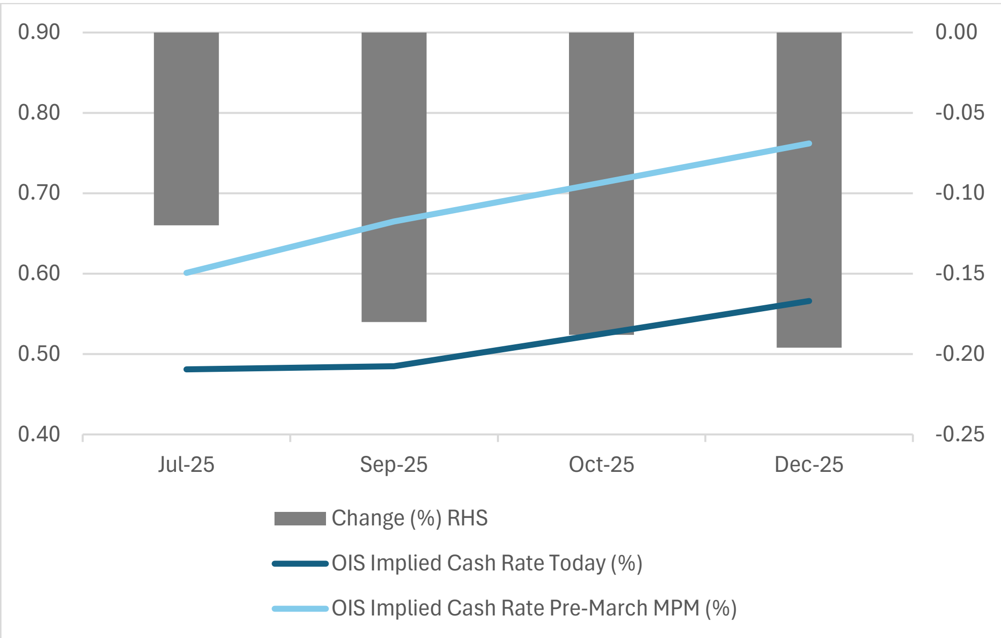
Overall, the BoJ continues to signal a gradual, data-dependent approach to policy normalisation, balancing market stability, inflation developments, and global uncertainties as it proceeds with cautious tapering into 2026 and beyond.

BoJ Market Pricing: Marginally Softer Than Pre-MPM Levels

BoJ-dated OIS pricing has softened modestly following yesterday's policy meeting.

- Heading into the meeting, markets were assigning just a 2% probability to a 25bp rate hike, increasing to 24% by September and 62% by December.
- Post-meeting pricing now implies only a 2% chance of a hike in July, 19% by September, and 54% by December—further extending the dovish repricing that began in mid-February, when a hike by September had been fully priced in.
- Across meetings through December 2025, pricing is now 12–15bps lower than pre-March MPM levels, reflecting heightened concerns over economic growth, particularly due to recent external shocks such as evolving US tariff policy.

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



Source: Bloomberg Finance LP / MNI

MNI BoJ WATCH: Ueda Flags Gradual Hikes, Warns Of JGB Risks

By Hiroshi Inoue
Jun 17, 2025

TOKYO - Bank of Japan Governor Kazuo Ueda on Tuesday insisted that the BOJ will raise rates if necessary, but stressed uncertainty after a meeting which saw another hold as well as a decision to reduce the pace of its tapering of bond purchases following poor responses to 30-year government auctions.

“Given that real interest rates are at significantly low levels, we will raise the rate to adjust the degree of easy policy, if the probability of achieving the 2% price target increases,” Ueda told reporters, declining to say whether a hike could come in July or otherwise in the near future.

“Looking ahead, hard data will show the impact of the U.S. tariffs on the economy, and we are attentive as to how these might evolve and whether the high headline consumer price index will affect underlying CPI inflation,” he said, adding that the impact of the U.S. tariffs on economy and prices will be clearer in or after the second half of this year.

Ueda said the overall outlook for the economy and prices has not changed significantly from the previous meeting on April 30-May 1. While the BOJ needs to closely watch the impact of the recent rise in crude oil prices, the year-on-year increase in CPI caused by higher input costs is set to wane toward the end of 2025, he said.

“Underlying CPI inflation is rising steadily, but it is still below 2% and has not accelerated,” Ueda said, “The risk is small that the BOJ will fall behind the curve.”

Still, the BOJ needs to monitor the risk that higher headline CPI caused by the rise in prices of food products including rice affects underlying inflation.

BOND TAPER

“We are focused on whether the rise in crude oil prices expands or is prolonged, and whether it will affect inflation expectations,” Ueda said, warning that U.S. trade policy could exert downward pressure on corporate profits in Japan.

Earlier in the day, the BOJ board decided to unanimously keep the policy interest rate unchanged at 0.50% for a third consecutive meeting, and decided by 8-to-1 to slow the pace of its reductions in bond purchases to JPY200 billion per quarter from April 2026 to March 2027 from the current pace of JPY400 billion.

“We took JGB market stability and the improvement of market functioning into consideration,” Ueda said, “If the pace of reducing JGB purchases is too fast, it would increase JGB volatility, which would have negative impact on the economy.”

As a result of the decision, the scale of JGB purchases by the BOJ will fall to JPY2.1 trillion in Q1 2027 from JPY2.9 trillion in Q1 2026. The BOJ will conduct an interim assessment of the bond taper program in June 2026.

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Sell-Side Views

CIBC: "There was little surprise in the BoJ decision, namely a unanimous decision for rates to remain at 0.50%. The central bank kept the taper plan unchanged through March 2026 at 400 trn yen per quarter - that was one of the more hawkish aired views in the 20 May "Bond Market Group" meetings. However, as 40y JGBs remained relatively stable, it looks as though the market isn't overly concerned about the mildly hawkish taper stance."

- "For April 2026 onward, the new taper schedule is 200 trn yen per quarter (the previous July 2024 plan had no tapering after Q1 2026). It was more dovish than expected, but the market already anticipated a post 2026 taper after some of the "hints" in the Bond Market Group meeting."
- "The BoJ policy statement still held a modestly upbeat tone on the economic outlook, noting that private consumption is moderately increasing, while exports and industrial production are "more or less flat as a trend," though the BoJ did mention possible frontloading. On inflation, the BoJ statement still noted that "underling CPI inflation is likely to be sluggish," but was still upbeat on the outlook saying "medium-to-long term inflation expectations will rise."
- "We would note that the Ueda underlined in the post event press briefing the potential impact of tariffs on both winter bonuses allied to next year's annual spring wage talks. Such warnings underline the economic ramifications of the failure to agree a trade deal. Moreover, we would note that Ueda detailed that the BoJ can be patient in terms of the policy narrative given that inflation expectations are still anchored below 2%. As ever its inflation expectations rather than the current rate of price growth that matters for policymakers."

CBA: "As the BoJ indicated, there are high uncertainties regarding the outlook for economic activity and prices, and by extension, the future path of monetary policy. Strong inflation, sharply lower US tariffs and/or a material depreciation in the JPY can encourage the BoJ to resume rate hikes sooner than we forecast. On the flip side, the BoJ may be forced to delay rate hikes or even return to rate cuts if the Japanese economy slows much more than expected. But the BoJ will be keen to avoid a return to negative interest rates in our view."

- "The BoJ's decision to slow the pace of QT is likely to have limited macroeconomic impact. Instead, the move reflects the BoJ's efforts to reduce its presence in the JGB market while limiting market disruptions. According to the BoJ, long term interest rates should be formed in financial markets in principle."

JPM: "Today's decision is not necessarily a dovish one. While the BoJ's communication focuses on the change in gross purchase amount, the true focus should be on the net change in the BoJ's JGB holdings. In this regard, the decision is merely a deceleration in the reduction pace, and even if it becomes JPY200 billion per quarter from 2Q26 onwards, the BoJ's QT pace will continue to accelerate. Based on the current redemption schedule of the BoJ's JGB holdings, the BoJ will reduce its holdings by about JPY33 trillion in 2025 and JPY46 trillion in 2026. Whether intentional or not, the BoJ's communication, focusing on the pace of reduction in gross purchases, may be giving the market the wrong impression that the Bank's QT will slow down."

- "On the other hand, by slowing the pace of reduction this time, some market participants may continue to expect the BoJ to maintain its large-scale JGB purchases, which could hinder improvements in market functionality."
- "In the press conference, Governor Ueda stated that while reductions should be pursued based on the principle that long-term yields should be formed in the market, the Board balanced this with considerations for market stability to prevent excessive future volatility. This decision seems to be a consideration for market stability in the short term, but it leaves uncertainty regarding the future outlook."

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- “Governor Ueda’s press conference essentially followed the May outlook report, emphasizing the future risks posed by tariffs, and stated that there is no significant change in the view this time. However, this seemed somewhat strained, as reporters questioned the impact of the US-China agreement since May, the assessment of upward inflation risks, and the gap between the BoJ’s view on underlying inflation and significantly higher inflation performance.”
- “We maintain our expectation that the BoJ’s outlook will be revised upward in the July report, paving the way for an additional rate hike in October.”

Societe Generale: “In the press conference, Governor Ueda said that there has been no significant change in the overall structure of Japan's economy and price trends since the May assessment. In addition, he also said that it is possible the BoJ may opt to raise rates without clear evidence of another upward turn in the data, depending on the broader economic outlook and the trajectory of the forecasts.”

- “Looking ahead, we continue to expect the BoJ to raise rates in October or December. Our reasons for this are as follows. 1) The BoJ's May meeting was less dovish than many people had expected and at today’s meeting, the BoJ concluded that there has been no significant change from its May assessment. 2) The extent of price pass-through to services has also begun to gradually increase. 3) The sensitivity of the inflation rate to a strong yen and low oil prices may be declining. 4) Wage growth is expected to remain solid due to structural labour shortages. 5) Future fiscal policy may push up the growth forecast by around 0.2%. 6) As a result of Japan-US tariff negotiations, a 10% tariff export quota may be introduced on some automobiles exported to the US. 7) Impacts of additional tariffs on growth and inflation may be more limited than most people expect. 8) Demand for digitalization and labour-saving investments is structurally strong.”

TD: “Today's BoJ decision was a straightforward one with a unanimous 9-0 vote to keep the target rate unchanged at 0.5%, but the spotlight was on the BoJ's QE taper plans. The BoJ announced that it will cut its QE taper pace by ¥200bn/qtr from April 2026 (next fiscal year) but retain its current taper pace of ¥400bn/qtr until then. We await further MoF guidance on issuance plans after this Friday's primary dealer meeting. As for the BoJ, we change our call, pushing out the next hike from July to October, which would take the Target rate to 0.75%.”

- “The QE taper decision was not a surprise to most given the various media leaks prior to the meeting, which speaks to Governor Ueda's preference to announce major policy shifts in a predictable manner. From January-April 2027, the BoJ aims for QE purchases at ¥2.1tn/qtr in January-April 2027 which imply a 16-17% decrease in its JGB holdings compared to before the QE taper.”
- “Shifting over to the policy rate outlook, Governor Ueda was dovish once again, asserting that the BoJ "is not falling behind the curve on inflation". Specifically, these remarks on inflation and the economy read dovish.”
- “However, we disagree with the remarks on inflation as it's clear that it's becoming a contentious issue domestically, in part driven by soaring rice prices. Price pressures are broadening again if we look at the share of items that recorded an increase in core CPI and the alternative measures of CPI that the Bank tracks. These are in a steady uptrend.”