

Economic Commentary

FICC Research Dept.

Tokyo CPI for May: Sticky inflation?

- Progress passing on higher costs to prices for goods/services
- With cost-push pressures easing, focus on how long passing on higher costs to prices will continue
- Electricity/gas subsidies to place roughly 0.3% drag on CPI in Aug-Oct
- Even though price decline from release of stockpiled rice limited, still see drag of about 0.2% on CPI

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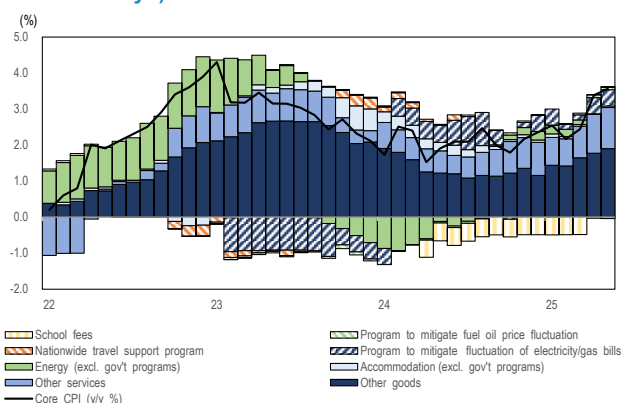


Tokyo CPI for May: Progress passing higher costs to prices could increase inflation stickiness

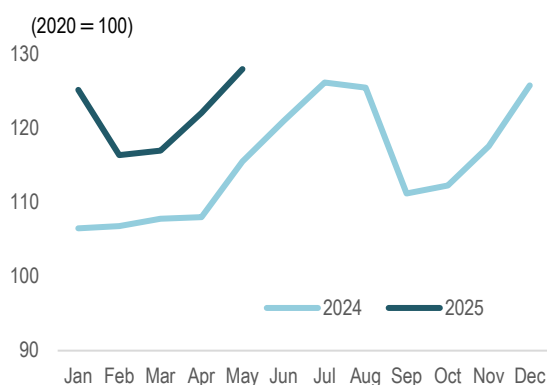
Tokyo core CPI (all items excluding fresh food) for May 2025 was +3.6% y/y, higher than the +3.4% reading in April and higher than the market median forecast of +3.5%. Core-core CPI (all items excluding fresh food and energy) was +3.3%, stronger than the +3.1% result for April. In his opening remarks at an international conference held on 27 May 2025, BOJ Governor Kazuo Ueda pointed out that Japan is, "Facing another supply shock in the form of rising food prices." Currently, the impact of these supply shocks could increase the stickiness of inflation through progress passing on higher costs to prices.

The factors that contributed to the stronger-than-expected reading were: (1) continued progress passing on higher costs to prices for food-related products and (2) progress passing on higher costs to general service prices amid rising input costs.

Government subsidies for electricity and gas fees concluded in April 2025. These subsidies placed a roughly 0.16% drag on Tokyo CPI (all items) for April. Electricity and gas fees rose compared to the previous month, boosted by the dropping off of these subsidies. That said, electricity fees for May 2024 rose significantly from April of that year due to an increase in the unit price of the renewable energy surcharge. Including this base effect, the difference in the y/y contribution for electricity fees from April 2025 was -0.04% and the contribution difference for energy overall was -0.02%. As such, energy factors did not contribute to the current CPI rise.

Chart 1: Breakdown of Contributions to Core CPI (in ward-area of Tokyo)

Source: Ministry of Internal Affairs and Communications (MIC); compiled by Daiwa.

Chart 2: Price Levels for Electricity

Source: MIC; compiled by Daiwa.

Confirmed widespread passing on of higher costs to goods/services prices; focus now on continuation of that trend

Food prices (excl. fresh food) rose 6.9% y/y (+6.4% in Apr). Since July 2024, the y/y increase has continued to expand, but the rise in prices, which was initially centered on ingredients such as rice, has now shifted to processed products. Specifically, prices for processed food products such as cooked curry, cooking oil, and sushi (boxed lunches) rose in May. Also, even in the case of dining out, there was a 5.9% y/y increase (+5.7% in Apr). Items contributing to this increase included grilled chicken, soba noodles, and bowls of rice topped with beef.

The passing on of higher costs to prices for these processed foods are expected to persist for now due to rising costs since the summer of 2024. However, fresh food prices in May fell 2.5% m/m, mainly due to fresh vegetables (-6.9%). In addition to declining prices for these fresh foods, the release of government stockpiles of rice is also expected to lower rice prices. So, the view that cost-push inflation will gradually subside and end-2025 core CPI will decline to around 2% remains unchanged.

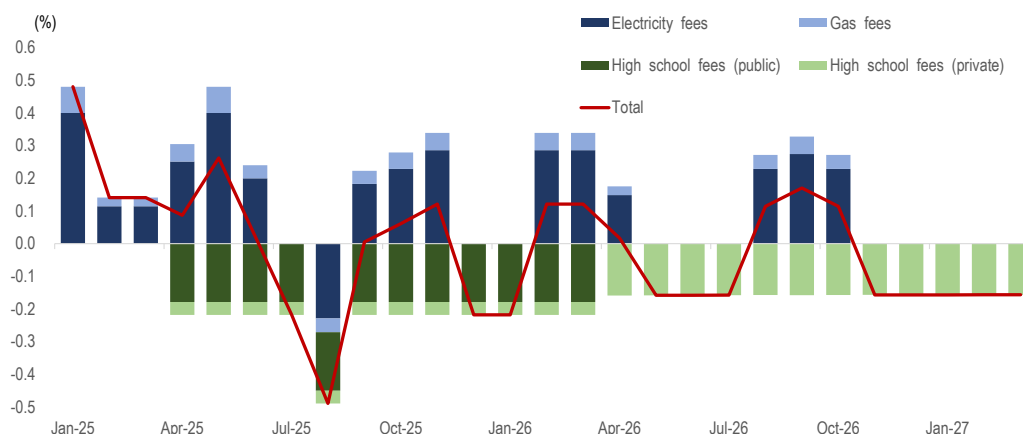
However, the trend of passing on higher costs to prices is spreading beyond food products. As for the recreation & culture-related services category, in addition to higher lodging fees, fees are rising for beauty salon treatments, golfing, and lessons (swimming, others). Indeed, prices for general services were +2.4% y/y (+2.2% in Apr).

Overall, if this trend of passing higher costs to prices expands to an even wider range of items, we cannot rule out the possibility that cost-push pressures will become more entrenched. That said, there is also the possibility that cost-push pressures, particularly for food, could decline sharply due to the release of government stockpiles of rice. With prices subject to both upside and downside risks, the focus will be on how long the trend of passing on higher costs to prices will continue.

Gov't steps to combat high prices: Electricity/gas subsidies to place 0.3% drag on CPI in Aug-Oct

The effects of the government's new measures to combat high prices will be reflected in future CPI figures. On 27 May, the government held a meeting at its Comprehensive Response Headquarters for US Tariff Measures. Here, as part of its "Emergency Package in Response to US Tariff Measures," the government decided to utilize contingency reserves to reduce electricity/gas fees for general households for the three-month period from July to September. This three-month subsidy period is based on the month of electricity/gas usage and is scheduled to be reflected in CPI based on the billing month. As a result, we can expect drags of about 0.27% for August and October 2025 CPI, along with a drag of roughly 0.33% for September 2025 CPI.

Chart 3: Impact of Government's Inflation Response on Nationwide Core CPI (incl. base effects)



Source: MIC; compiled by Daiwa.

Release of stockpiled rice, rice price decline limited, but drag of about 0.2% on CPI

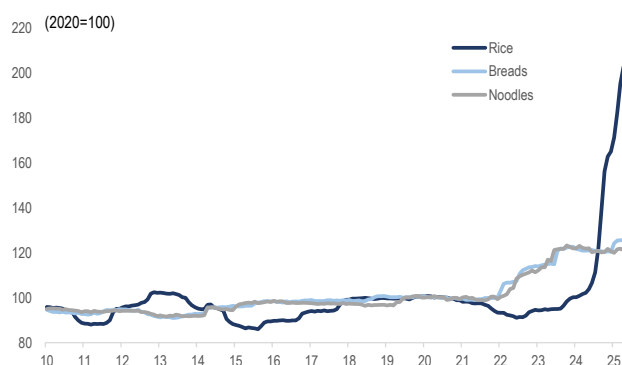
Agriculture Minister Shinjiro Koizumi aims to reduce the price of rice, currently around ¥4,300 per 5kg, to a ¥2,000-3,000 range. A decision was made to release 100,000 tons of rice produced in 2021 and 200,000 tons of rice produced in 2022, for a total of 300,000 tons of stockpiled rice. This time, the government will sell directly to retailers through discretionary contracts, bypassing collection and wholesale.

The three possible factors contributing to the current rise in rice prices are considered to be (1) Supply shortages due to unfavorable weather conditions causing poor harvests and distribution delays, (2) Increased demand due to growth in demand from tourists visiting Japan, and (3) Inability to pass on higher cost to prices since 2021. The Ministry of Agriculture, Forestry and Fisheries estimates the annual demand for rice used for staple foods at 6.74 million tons. The release of rice stockpiles will cover about 4.5% of domestic demand.

Here, we want to consider the appropriate rice price based on the relative price difference with bread and noodles, which are also staple foods. Looking at the CPI trends for rice, bread, and noodles, there are now significant fluctuations in the price of rice. However, since 2010, the prices for rice, bread, and noodles generally trended around the same level (Chart 4).

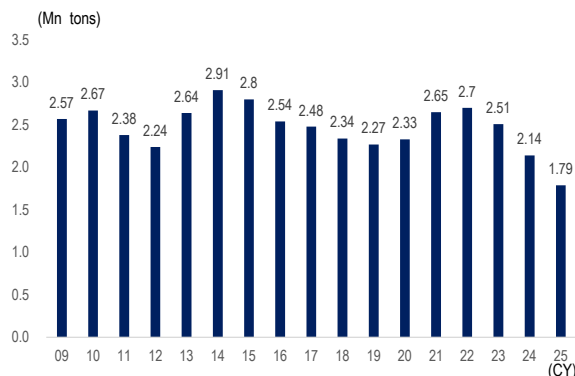
Assuming that the price for rice falls back to the same level as the price for bread and noodles, that would suggest a price drop of around 36% for rice, to around ¥2,700 per 5kg. However, as of March 2025, private sector inventories stood at only 1.79 million tons, which is insufficient to cover the shortfall compared to past inventory levels (generally between 2.3 million and 2.6 million tons) (Chart 5). Also, demand for rice among overseas tourists visiting Japan is at an all-time high. As such, there is a possibility that the supply situation until now will not be enough to meet demand. Therefore, it is unlikely that rice prices will fall back to an appropriate level.

Chart 4: Nationwide Price Indices for Rice, Bread, and Noodles



Source: MIC; compiled by Daiwa.

Chart 5: Private Sector Inventories at end-Mar

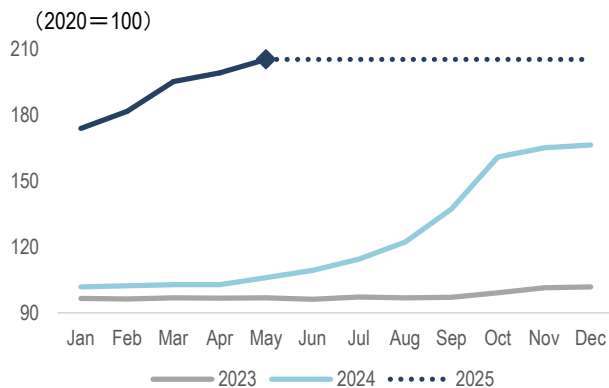


Source: Ministry of Agriculture, Forestry and Fisheries; compiled by Daiwa.

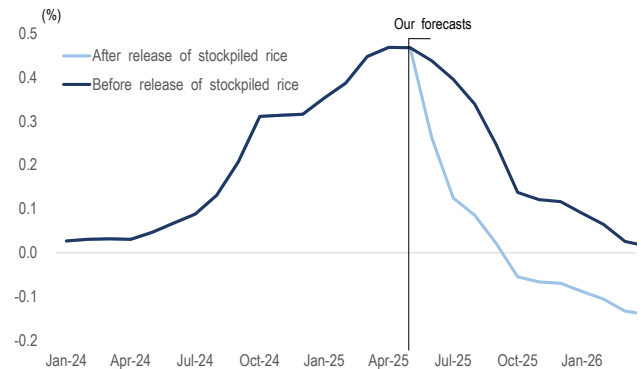
If the release of stockpiled rice causes the “typical” price of rice to fall to around ¥3,000, that would likely produce a drag of around 0.15% on the Tokyo core CPI. The Japanese CPI is calculated based on surveys conducted by researchers who visit major retailers and collect data on the sales prices of typical brands and specifications of goods. At this point, the products with the largest sales at each surveyed store, known as “typical products,” are selected for the survey.

This means that even if the stockpiled rice is released at a price of ¥2,000, as long as it does not become a “typical product,” its price will not be directly reflected in the CPI. Basically, changes for the prices of “typical products” are not reflected in CPI until the prices of other blended rice varieties are impacted according to the release of stockpiled rice. For that reason, the impact on consumer prices is expected to be relatively moderate.

However, falling rice prices would have a significant impact on the CPI going forward. Tokyo core CPI for May 2025 was +3.6% y/y. The contribution to this figure from rice was approximately 0.47% (contribution to April's nationwide CPI was approximately 0.6%), indicating that the surge in rice prices is having a significant impact on current prices. That said, even if rice prices remain unchanged going forward, the y/y rate of increase for the CPI will gradually decline (Chart 6). Also, if the typical rice price falls to around ¥3,000, the y/y contribution to core CPI is expected to fall to roughly zero in September 2025. Depending on the extent to which the release of stockpiled rice pushes down prices, we should be mindful of the possibility that CPI may be pushed down rapidly due to drags from a decline in rice prices from June 2025 onwards.

Chart 6: Price Level for Rice (in ward-area of Tokyo)


Source: MIC; compiled by Daiwa.

Chart 7: Contribution (y/y) of Rice Prices to Tokyo Core CPI


Source: MIC; compiled by Daiwa.

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