Daiwa's Economic View

BOJ June MPM Summary of Opinions: Emphasizes inflation overshoot, will look to assess economy after summer

- Consensus is to watch and wait amid ongoing uncertainty
- May take until after summer to assess state of real economy
- But BOJ emphasizes upside risks to inflation
- Key focus at July MPM: Comments on balance of risks to economy/inflation

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Consensus is to watch and wait amid ongoing uncertainty

The Bank of Japan (BOJ) released the Summary of Opinions from its 16-17 June Monetary Policy Meeting (MPM) on 25 June. The opinions confirmed that uncertainty about tariffs remains extremely high, and that the core consensus at the central bank is to maintain current policy for now.

That said, we note one opinion that "With inflation being at levels higher than expected, the Bank may face a situation where it should adjust the degree of monetary accommodation decisively, even when there is high uncertainty". We suspect this came from policy board member Naoki Tamura, who stated in a speech on 25 June (the same day the Summary was released) that "I believe that the Bank may face a situation where it should act decisively, despite heightened uncertainties".

However, we think many policy board members are focused on "downside risks to economic activity" (i.e., the negative impact on underlying inflation) even though "prices have been somewhat higher than expected". At this point, only a minority of opinions support raising interest rates in the near future.

Opinions on economic developments: To examine real economy after summer

In views on economic developments, board members noted the worsening soft data ("a deterioration in sentiment reflecting elevated food prices and U.S. tariff policy"), but "much of the hard data...has been relatively solid" and "the Bank needs to take some time to examine the magnitude of the impact on the real economy." BOJ Governor Kazuo Ueda commented at his regular press conference following the June MPM that developments in 2H (from July) 2025 will be key, and that the BOJ will therefore be watching the period from summer onward in assessing the real economy.

Export prices have already fallen sharply, confirming that Japanese firms are bearing some of the cost of tariffs. Tariffs are clearly having a negative impact, particularly on manufacturing industries. However, some firms such as Subaru, Mitsubishi Motors, and Toyota Motor are moving to raise selling prices in the US.

We see two ways in which tariffs could directly affect Japanese firms: (1) a decline in their price competitiveness as they raise US domestic sales prices, and (2) an increase in their costs due to the burden of higher tariffs. Given companies' cost and earnings structures, (1) would result in a limited decline in margins given the decline in sales volume, revenue, and variable costs that would result from an increase in US domestic sales prices. However, if companies bear the cost of tariffs and lower export prices as per point (2), this would likely result in a greater decline in margins as sales volume and variable costs remain largely unchanged while revenue declines.

The above signals the importance of companies' response to tariffs. In addition, the BOJ would need to monitor the impact on exports, production, and corporate earnings, which we think it will take some time to assess.

We also need to monitor global (particularly US) economic trends to assess their impact on the Japanese economy. On 24 June, Fed Chair Jerome Powell indicated that the Fed "would expect to see meaningful effects in June, July, August," suggesting a need to carefully assess the direction of the US economy over the summer. The US economic outlook will also be an important factor in the BOJ's policy decisions, and we think it will continue to watch and wait in the near term.

The Summary of Opinions also included the view on economic developments that "Japan's economy has entered a phase where attention is warranted on the possibility that developments overseas will spread to Japan". This is consistent with Mr. Ueda's comments regarding the new plan for reducing JGB purchases that the BOJ approved at its June MPM, that it is moving promptly to reduce purchases to avoid a negative impact on the economy. We think this reflects the BOJ's heightened concerns about the risk of a negative impact on the real economy after the recent rise in superlong JGB yields spilled over to shorter maturities.

◆ Opinions on Economic Developments in Summary of Opinions at Jun MPM (released on 25 Jun 2025)

- While much of the hard data for April and May has been relatively solid, it is likely that the effects of tariff policies are yet to materialize.
- According to anecdotal information from firms in a wide range of industries, including small and medium-sized firms, some have been withholding judgment about the impact of U.S. tariff policy amid the difficulty of determining the direction that the policy will take, given the lack of information. While the impact of U.S. tariff policy will certainly exert downward pressure on firms' sentiment, the Bank needs to take some time to examine the magnitude of the impact on the real economy.
- Anecdotal information from firms suggests that, despite the impact of U.S. tariff policy, many firms will (1) continue to raise wages to address labor shortages; (2) continue to make high levels of business fixed investment, including investment in digital transformation and efficiency-improving investment; and (3) make solid investment to strengthen profits to address shareholders' expectations.
- Although the direct impact of U.S. tariff policy has not been observed so far, Japan's economy has been somewhat stagnant, mainly against the background of a deterioration in sentiment reflecting elevated food prices and U.S. tariff policy.
- The situation of government bond markets around the world has been a major topic of discussion, such as at international meetings. Japan's economy has entered a phase where attention is warranted on the possibility that developments overseas will spread to Japan.

Views on prices emphasize upside risks

However, several opinions argued that inflation is "higher than expected". Mr. Ueda commented at the press conference after the June MPM that there are substantial downside risks to the economy and prices. This suggests that while inflation is now on the high side, the BOJ sees considerable downside risk to underlying inflation from tariffs, but cannot rule out the potential for the balance of risks to inflation to quickly return to neutral if the risk from tariffs eases.
The Summary of Opinions also mentions that "Europe, the United States, and China and other emerging economies have all leaned toward accommodative policies on both the fiscal and monetary fronts. Against this backdrop, Japan's economy could unexpectedly be pushed up or experience inflationary pressure." If accommodative fiscal and monetary policy mitigates the impact of tariffs, the Japanese economy and inflation could still return to their pre-tariff (i.e., on-track) trajectory in April.

The minutes of the April MPM released on 20 June also showed one policy board member arguing that "even if the GDP growth rate and the year-on-year rate of increase in the CPI developed in line with the outlook presented at this meeting, it was quite possible that underlying CPI inflation would be at a level that was generally consistent with the price stability target in the first half of the projection period of the April 2025 *Outlook Report*, depending on firms' and households' inflation expectations and firms' wage- and price-setting behavior." Evidence to support this view is gradually emerging.

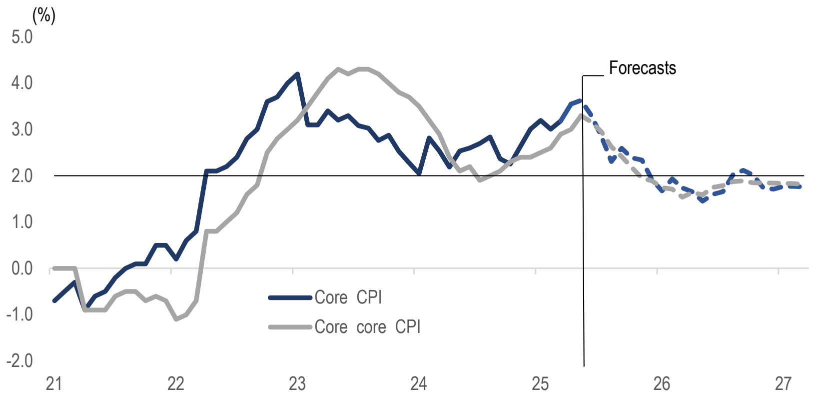
In a 25 June speech, BOJ policy board member Naoki Tamura noted that "attention is also warranted on upside risks to prices. In this situation, I believe there is a good possibility that the price stability target will be achieved earlier than expected." At the subsequent press conference, Mr. Tamura also noted the growing risk of an overshoot for prices caused by rising private service prices and by price hikes for the food items that are a key concern for households.
However, the BOJ's current baseline forecast is for underlying inflation to slow due to factors such as slowing GDP growth. We also expect CPI inflation to slow to around 2% y/y through end-2025. This is because current CPI inflation is mainly cost-push in nature, and we expect the y/y uptrend in food and energy prices to gradually slow.

While downside risks to inflation are easing at this point, we think a skew toward upside risks would require (1) further progress with passing through costs, and (2) new supply shocks such as a weaker yen or higher oil prices. We therefore do not think the BOJ is behind the curve at this point.

◆ **Opinions on Prices in Summary of Opinions at Jun MPM (released on 25 Jun 2025)**

- Although uncertainty regarding trade policies remains extremely high, on the domestic front, wage developments have been solid, and the CPI has been slightly higher than expected.
- Rice prices have almost doubled compared with the previous year. This rise in rice prices has pushed up the CPI considerably and has also spread to prices of related items. As the price of rice -- which is a staple food in Japan -- could affect perceived inflation and inflation expectations, it is necessary to closely monitor developments in rice prices.
- Europe, the United States, and China and other emerging economies have all leaned toward accommodative policies on both the fiscal and monetary fronts. Against this backdrop, Japan's economy could unexpectedly be pushed up or experience inflationary pressure.
- Although the CPI has been higher than expected, the pass-through of higher wages to services prices seems to have plateaued.

Chart 1: CPI Forecasts



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

Key focus at July MPM: Comments on balance of risks to economy/inflation

We focus at the July MPM on changes in the BOJ's views on the balance of risks (downside risks) to the economy and inflation. We think the moderate recent pick-up in inflation makes downside risks to inflation more likely to be reset to neutral in the July *Outlook Report*. However, we think it will take time to assess downside risks to the economy.

In terms of domestic factors, we think economic developments from summer through autumn will be key to assessing downside risks to the economy; provided there is no major negative impact, we think the balance of risks to the economy, which currently skew to the downside, could begin to swing back toward neutral.

However, tariffs are likely to have an impact mainly on manufacturing industries, and we think the BOJ is unlikely to raise interest rates in the near term unless upside risks to prices emerge. At this point, our base case is for the next rate hike to come in Jan-Mar 2026.

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Chart 2: Opinions on Monetary Policy in Summary of Opinions at Jun 2025 MPM

	Opinions on Monetary Policy
1	If its outlook for economic activity and prices will be realized, the Bank, in accordance with improvement in economic activity and prices, will continue to raise the policy interest rate and adjust the degree of monetary accommodation. In this regard, considering the extremely high uncertainties, it is important for the Bank to judge whether the outlook will be realized, without any preconceptions.
2	Even if Japan's economic activity and prices develop in line with the baseline scenario, it is likely that economic growth will moderate and that the improvement in underlying CPI inflation will be sluggish temporarily, and there is high uncertainty and downside risks surrounding trade policies. Given this, the Bank should, at this point, maintain accommodative financial conditions with the current interest rate level and thereby firmly support the economy.
3	Even though prices have been somewhat higher than expected, it is appropriate for the Bank to maintain its current stance regarding the conduct of monetary policy, given the downside risks to economic activity stemming from U.S. tariff policy and the situation in the Middle East.
4	With extremely high uncertainty in the outlook, it is necessary to examine economic developments and other factors. It is therefore appropriate for the Bank to maintain the current policy interest rate for the time being.
5	With inflation being at levels higher than expected, the Bank may face a situation where it should adjust the degree of monetary accommodation decisively, even when there is high uncertainty.
6	It is desirable for the Bank to further reduce its purchase amount of Japanese government bonds (JGBs) to ensure that long-term interest rates are formed more freely. On the other hand, with the reduction of the purchase amount progressing, if the pace of the reduction is too fast, this may have an unforeseen impact on market stability. In formulating a plan for the reduction, it is necessary to strike a balance between these two factors.
7	The plan decided for the reduction of the Bank's purchase amount of JGBs aims at avoiding adverse effects on economic activity and prices due to rapid fluctuations in interest rates while allowing the rates to be determined, in principle, by the market. It will be necessary for the Bank to clearly explain that this plan does not in any way aim at giving considerations to the fiscal situation.
8	While it is desirable for the Bank to reduce its share of JGB holdings as swiftly as possible, if it proceeds too hastily with the reduction, the adjustments may end up taking more time, as was the case when the Federal Reserve had to discontinue its quantitative tightening (QT) in 2019. If the Bank reduces its purchase amount of JGBs significantly and then increases the amount again, this could unnecessarily increase the risk of confusion in the market during the reduction process.
9	The Bank needs to continue the reduction of its purchase amount of JGBs, as the functioning of the JGB markets is on its way to recovery. Considering the weak recovery in Japan's economy, heightened uncertainty in the outlook, and the JGB holding capacity of the market, it is appropriate for the Bank to slow the pace of reduction in its purchase amount to 200 billion yen from April 2026, from the perspective of risk management, and to conduct an interim assessment in June 2026.
10	It is desirable for the Bank to slow the pace of reduction in its purchase amount of JGBs from April 2026, from the perspective of further smooth conduct of monetary policy. However, this does not mean that the Bank has changed its stance on monetary policy conduct.
11	Given that the Bank has purchased a large amount of JGBs, the reduction of its purchase amount will increase the supply of JGBs to the market. Taking this into consideration, it can be said that the market is in a phase with one of the largest supplies of JGBs compared to the past. To prevent the market from becoming unstable, it is necessary to adjust the reduction of the purchase amount, taking into account the amount of JGB supply in the past, and to carefully examine how the market responds.
12	The Bank can proceed more cautiously with the reduction of the JGB purchase amount on a flow basis in fiscal 2026, when the Bank will enter the next phase of the reduction process toward reaching the final level of the purchase amount. In addition, the Bank should consider what would be the optimal size of its balance sheet, from both the asset and liability sides.
13	The Bank should allow long-term interest rates to be determined by the market and its participants, and should therefore normalize the level of the amount outstanding of its JGB holdings as soon as possible. By doing so, it is important to increase, at the earliest possible time, the capacity in financial markets to absorb shocks.
14	Excess reserves seem to be at abundant levels. It is therefore necessary for the Bank to proceed steadily with the reduction of its purchase amount of JGBs, and thereby normalize its balance sheet.
15	Regarding the reduction of its purchase amount of JGBs, the Bank needs to consider how to set the final level of the purchase amount from a long-term perspective, along with the future course of the reduction in the size of its balance sheet.
16	If the Bank reduced the amount of its monthly outright purchases of JGBs to, for example, about 1 trillion yen, developments regarding its purchases would no longer be discussed in the market. It is not necessary to stick rigidly to making the purchase amount zero.
17	Increased volatility in the super-long-term zone may spill over to the entire yield curve, thereby spreading unintended tightening effects to the market as a whole. The yield curve formed under stable market conditions can be considered an important financial infrastructure. It is necessary to ensure the stability of the market while maintaining close communication among authorities.

Source: BOJ; compiled by Daiwa.

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