

Daiwa's Economic View

BOJ Governor's speech: Views unchanged from Sep MPM

- More constructive view of Japanese economy
- Focusing on US uncertainty, as at Sep MPM; cautious about near-term rate hike
- Growing sense that Japanese economy on track to achieve BOJ forecasts; changing balance of views among policy board members makes shift in communication more likely

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Key focus is whether Ueda's growing sense that Japanese economy on track resulted in more constructive view

Bank of Japan (BOJ) Governor Kazuo Ueda gave a speech at a meeting with business leaders in Osaka on 3 October. BOJ policy board member Asahi Noguchi's 29 September speech and the 30 September [Summary of Opinions from the recent Monetary Policy Meeting \(MPM\)](#) confirmed that the growing desire to raise interest rates is not confined to the two board members who advocated a rate hike at the September meeting. However, the BOJ appears cautious on some fronts, as evidenced by Mr. Ueda's emphasis at his regular press conference following the September MPM on assessing the impact of tariffs. [The BOJ Tankan](#) released on 1 October also indicated strong trends at corporates and added to the sense that Japan's economy is on track to achieve the BOJ's forecasts. Our focus in today's speech was whether this growing sense that the domestic economy is on track had prompted Mr. Ueda to take a more constructive view compared with the September MPM.

More constructive view of domestic economy; sees inflation as transitory

Mr. Ueda commented in today's speech that the results of the September Tankan survey showed that "business sentiment has been at a favorable level on the whole," reflecting "reduced uncertainty in the outlook." He also noted that capex plans show that "the growth momentum in investment has been maintained," and that anecdotal evidence from companies suggests that they are "committed to firmly moving ahead with investments that are necessary from a medium- to long-term perspective."

Mr. Ueda also noted that "so far there are no signs that the effects [of US tariffs] have spread to Japan's economy as a whole, including business fixed investment and employment and wage developments." While he reiterated the BOJ's baseline scenario in which "overseas economies are likely to decelerate under the impact of tariff policies, putting downward pressure on exports and business fixed investment," the results of the BOJ Tankan clearly gave him greater confidence that Japan's economy and inflation will trend in line with the central bank's forecasts.

On inflation, he also noted that "the rise in food prices, particularly rice prices, is largely driven by temporary supply-side factors rather than a sudden rise in consumer demand" and that current inflation driven disproportionately by food is a temporary phenomenon.

Three near-term "points to monitor": No change in view since Sep MPM

Mr. Ueda also cited three risks to economic activity and prices: "developments in overseas economies," "how US tariff policies will affect profits and the wage- and price-setting behavior of Japanese firms," and "developments in food prices." These are largely in line with his comments at the September post-MPM press conference and indicate that he remains cautious about raising interest rates in the near future given current uncertainties.

On the subject of “developments in overseas economies,” he first discussed the pass-through of tariff costs to output prices and “when and in what form the impact will manifest” particularly in the US. While noting that Fed rate cuts are “expected to support the US economy,” he also noted that “employment risks are tilted to the downside” and in his view “considerable uncertainties remain.” His key checkpoint is the state of the US economy (i.e., the potential for a soft landing).

Turning to tariffs' effect on Japanese firms, Mr. Ueda noted that the high level of profits accumulated by firms should act as a buffer to some extent, and that he expects “the mechanism in which wages and prices rise moderately in interaction with each other [to] essentially remain in place.” However, he also noted that firms may place stronger emphasis on cost-cutting and may weaken their efforts to reflect price increases in wages, and stated that the BOJ will continue to closely examine firms' views to see whether these risks materialize going forward. The momentum of wage hikes in the 6 October BOJ branch manager meeting report will likely be another key checkpoint.

Finally, on developments in food prices, Mr. Ueda discussed risks to both the upside (food inflation could last longer than the BOJ expects) and downside (rising food prices could depress consumer spending and in turn overall inflation). This implies that he does not see major upside risks to inflation at this point.

Given these uncertainties and the downward pressure from the 15% tariff rate, he indicated his caution about a near-term rate hike, stating that “it is important, first of all, to maintain accommodative financial conditions and thereby firmly support economic activity.”

Press conference also unlikely to telegraph rate hike; focus on view of US economy

Mr. Ueda's 3 October speech indicated that his view of the Japanese economy has become more constructive following the upbeat September Tankan. We think the growing sense that the Japanese economy is on track to achieve the BOJ's forecasts and changes in the balance of views among policy board members will make it easier for Mr. Ueda and other BOJ leaders to lean toward raising interest rates.

However, as Mr. Ueda indicated in today's speech, the key checkpoint for the BOJ's next rate hike is the potential for a soft landing in the US. We think he will look to gather as much data as possible on US employment, inflation, economic trends (including Christmas sales), and the Fed's policy stance in forming a view, and at this point we are not surprised that his perceptions are largely unchanged from the September MPM. However, given the BOJ's sense that trends in Japan are on track to achieve its forecasts and the balance of views among its policy board members, we think its communication could shift once it gains a degree of confidence.

We focus at Mr. Ueda's press conference on whether the BOJ expects to form a view on the US economy in the near term or assumes a need to observe over the longer term. However, we think he is likely to indicate that the BOJ will keep an open mind when making policy decisions and remain data-driven given current uncertainty, mainly on the US economy, and the fact that it is still looking for confirmation on several of its checkpoints. In short, we do not expect him to telegraph the timing of the BOJ's next rate hike.

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