Daiwa Securities

Daiwa's View

Key points for Jan BOJ meeting: Will rate-hiking pace accelerate?

- Yen depreciation may accelerate rate-hiking pace
- How widespread is recognition of higher-than-expected prices?

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Rate hike baseline is "every six months," but risk of acceleration on yen depreciation

We expect the BOJ to emphasize two factors when deciding its next interest rate hike, specifically (1) verification of impacts following the December 2025 rate hike and (2) wage increase results from the 2026 spring labor-management wage negotiations, along with the extent to which higher wages are feeding through to higher prices. If these conditions are met and if the likelihood of the underlying rate of inflation rising toward 2% increases, the BOJ would most likely proceed with an additional policy rate hike to 1%. The current baseline scenario is for interest rate hikes to occur roughly once every six months.

That said, if concerns about higher-than-expected prices become more pronounced due to factors such as yen depreciation, the prospect of an earlier-than-planned interest rate hike would become more realistic. On 15 January, Bloomberg reported that yen depreciation could increase the likelihood of achieving the Bank's price stability target and/or lead to an earlier rate hike (citing individuals familiar with the matter).

If an early rate hike is anticipated, a viable option could be an additional rate hike at the April meeting, when FY28 economic and price projections are newly established and the first tally of spring labor-management wage negotiation results are finalized. At the next policy meeting, participants will likely interpret the pace of future rate hikes based on the content of the *Outlook for Economic Activity and Prices* report (*Outlook Report*) and BOJ Governor Kazuo Ueda's remarks at the post-meeting press conference.

Expect BOJ to maintain status quo at Jan meeting; focus on higher-than-expected price risks, rate-hiking pace

The BOJ's 8 January branch managers' meeting report indicated robust wage-setting behavior and the Tokyo CPI for December also confirmed signs of disinflation. The current state of the economy and prices is progressing as anticipated by the BOJ. Meanwhile, we assume the BOJ is now in a phase of carefully assessing the impact of its previous rate hike. So, we expect the Bank to make a unanimous decision to maintain the status quo at its 22-23 January Monetary Policy Meeting.

However, the Summary of Opinions for the December 2025 meeting confirmed that concerns are growing over higher-than-expected prices stemming from forex and fiscal policy developments. The 8 January branch managers' meeting report also introduced comments such as, "In response to increased costs due to the recent yen depreciation, we are considering the need to pass on these costs to our customers." This suggests growing concerns, especially about higher prices stemming from yen depreciation. The exchange rate, which stood in the USD/JPY155 range as of the December meeting, briefly weakened to the USD/JPY159 range following a media report that the Lower House will be dissolved at the opening of the regular Diet session set to convene on 23 January.

Under these circumstances, in the January *Outlook Report* we will mainly focus on (1) numerical projections and risk balance for the economy/prices and (2) changes in the distribution of projections (chart) among policy board members. During Ueda's post-meeting press conference, attention will turn to the risk of higher-than-expected prices due in large part to forex trends, as well as the rate-hiking pace and conditions in light of those risks.

Outlook for economic activity and prices: Expect downward price revisions on economic measures

The factors contributing to the changes to the outlooks since the previous *Outlook Report* are: (1) reduced uncertainty for the global economy, (2) effects of the government's economic measures, and (3) further yen depreciation.

We expect the BOJ to revise its real GDP forecast upward to +0.9% for FY25 (previously +0.7%) and +0.8% for FY26 (previously +0.7%) in its January *Outlook Report*. We also expect the growth rate for FY27 to remain unchanged. These upward revisions reflect reduced uncertainty surrounding the US economy and tariffs, as well as the effects of the economic measures implemented by the Japanese government.

The numerical growth for FY25 appears substantial, but that is due to the impact of a large growth rate carryover effect[1] from the previous year. We assume a +0.6% increase for FY25 due to that carryover effect and a +0.1 to +0.2% increase in FY26 for the same reason. All told, these points suggest that, in reality, the economic situation will be better in FY26.

Regarding the price outlook, while we expect core CPI to remain unchanged for FY25 and FY27, we think the outlook for FY26 will be revised downward to +1.7% (previously +1.8%). Meanwhile, we expect core-core CPI to be revised upward to +2.9% for FY25 (previously +2.8%). While yen depreciation and an improving output gap push up prices, the government's economic measures will apply downward pressure on prices, particularly around FY26.

The main items in the government's economic measures aimed at lowering prices include (1) electricity and gas subsidies implemented from February to April 2026 (based on timing of their reflection in CPI), (2) gasoline subsidies expanded through December 2025, and (3) implementation of free private high school education and free elementary school lunches in April 2026. It remains unclear to what extent policy board members had factored in each of the government's policies at the time of the previous (Oct) *Outlook Report*. However, if all of these factors were incorporated anew, we could estimate that core CPI for FY25 would be lowered by around 0.16% and core CPI for FY26 would be lowered by around 0.35%. In other words, excluding the effects of economic stimulus measures, a somewhat larger upward revision is expected.

Also, we expect the price outlook for FY27 to remain unchanged at +2.0%. This will likely allow the BOJ to maintain its previous view that, "underlying CPI inflation and the rate of increase in the CPI (all items less fresh food) will increase gradually and, in the second half of the projection period of the October 2025 *Outlook for Economic Activity and Prices*, will be at a level that is generally consistent with the price stability target." Meanwhile, board members Hajime Takata and Naoki Tamura are expected to submit dissenting opinions regarding the price outlook[2], as they did at the December meeting.

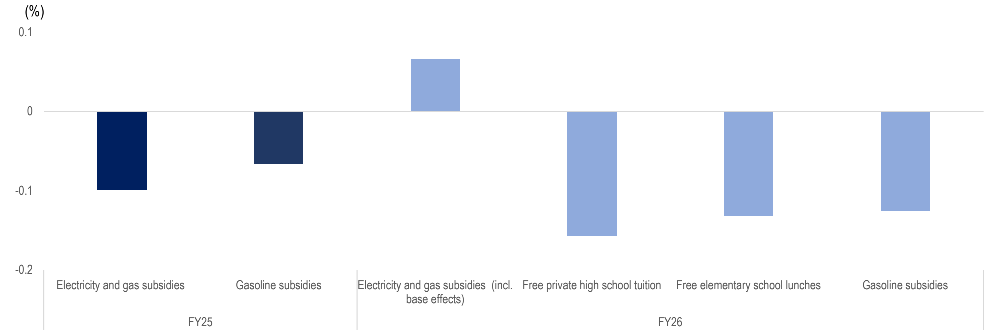
[1] The "growth rate carryover effect" refers to a phenomenon in which high GDP levels at the end of a fiscal year inflate apparent annual growth rates, even when actual new growth is small.
[2] Takata Hajime opposed the description regarding the outlook for prices, considering that the level of the rate of increase in the CPI, including underlying CPI inflation, already had generally reached the price stability target. Tamura Naoki opposed the description regarding the outlook for underlying CPI inflation, considering that underlying CPI inflation was likely to be at a level that was generally consistent with the price stability target from the middle of the projection period.

BOJ Policy Board Members' Projections (median, y/y %)

	Real GDP			Core CPI			Core core CPI		
	Oct 2025*	**Jan 2026****	Our forecasts	Oct 2025*	**Jan 2026****	Our forecasts	Oct 2025*	**Jan 2026****	Our forecasts
FY25	+0.7 %	**+0.9 %**	+0.9 %	+2.7 %	**+2.7 %**	+2.8 %	+2.8 %	**+2.9 %**	+3.1 %
FY26	+0.7 %	**+0.8 %**	+0.9 %	+1.8 %	**+1.7 %**	+1.8 %	+2.0 %	**+2.0 %**	+2.1 %
FY27	+1.0 %	**+1.0 %**	+1.0 %	+2.0 %	**+2.0 %**	+1.9 %	+2.0 %	**+2.0 %**	+2.1 %

Source: BOJ; compiled by Daiwa.
Note: Our forecasts are based on our current economic and inflation outlook.
**BOJ projections. **Our estimates for policy board member projections (highlighted in light blue).*

Impact of Government's Economic Package on Core CPI (y/y growth)



Source: BOJ; compiled by Daiwa.
Note: The new electricity and gas subsidies will have a downward effect on Feb-Apr 2026 CPI. However, the subsidies for Feb-Mar 2026 are particularly large, so the inclusion of their base effects will contribute to pushing up CPI in FY26.

Risk balance and conduct of monetary policy: Rate hike policy unchanged, but prices may rise

We see a high likelihood that the risk balance for the economic outlook, previously described as "risks are skewed to the downside for fiscal 2026" will be revised to "generally balanced" as uncertainty surrounding the US economy and tariffs diminishes.

Meanwhile, the balance of risks for the FY26 price outlook could quite plausibly result in the assessment that, "risks are skewed to the upside" when taking into account not only the reduced downside risks to the economy, but also the numerous concerns about upside price risks in the Summary of Opinions for the December meeting, as well as the continued yen depreciation even after the December rate hike. If the risk balance for prices is judged to have shifted upward, the possibility of an early rate hike (Apr-Jun quarter) would likely come into focus.

We should also pay attention to the number of policy board members pointing out upside risks. In other words, attention will focus on whether recognition of upward price pressures spreading beyond the most hawkish members of the policy board (namely Takata and Tamura).

Forecasts for Economic Risk Balance Chart

	FY25		FY26		FY27	
	Oct 2025*	Jan 2026**	Oct 2025*	Jan 2026**	Oct 2025*	Jan 2026**
Upside	2	0	2	2	0	0
Downside	3	0	4	1	0	0
Balanced	4	9	3	8	9	9
Assessment	Generally balanced				–	

Source: BOJ; compiled by Daiwa.
**BOJ projections. **Our estimates (highlighted in light blue).*

Forecasts for Price Risk Balance Chart

	FY25		FY26		FY27	
	Oct 2025*	Jan 2026**	Oct 2025*	Jan 2026**	Oct 2025*	Jan 2026**
Upside	3	0	3	2	2	2
Downside	2	0	2	0	1	0
Balanced	4	9	4	7	6	7
Assessment	Generally balanced		Risks are skewed to upside		–	

Source: BOJ; compiled by Daiwa.
**BOJ projections. **Our estimates (highlighted in light blue).*

We see no significant changes in the economy and price risk factor items themselves. That said, descriptions of overseas economic and price trends are likely to be revised upward, reflecting a reduction in downside risks. Also, new wording regarding the deterioration of Japan-China relations may be added. Regarding descriptions of forex trends, we expect the Bank will maintain its conventional wording, "With firms' behavior recently shifting more toward raising wages and prices, exchange rate trends are, compared to the past, more likely to affect prices."

The wording for the conduct of monetary policy will largely follow the phrasing from the December meeting. In other words, we expect the BOJ to maintain its policy of raising interest rates described as, "Given that real interest rates are at significantly low levels, if the baseline scenario for economic activity and prices outlined so far is 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."

Ueda's press conference: Any indication of caution regarding forex?

At Ueda's post-meeting press conference, attention is likely to focus on upside price risks, particularly forex trends, as well as the pace and conditions for rate hikes in light of those risks.

As for forex trends, Ueda said at the December meeting, "As corporate wage and price-setting behavior becomes more proactive, we want to remain vigilant (in regards to exchange rates possibly impacting prices)." At the press conference following the next meeting, while closely monitoring the impact of yen depreciation on underlying prices, there is a possibility that a more cautious tone could be adopted.

Meanwhile, the results of the 2026 spring labor-management wage negotiations have yet to be announced and, given the need to verify any negative effects from the previous rate hike, the Bank will likely maintain its stance of preserving policy flexibility and freedom at this juncture. In other words, it is unlikely that the pace and conditions for rate hikes will be clearly specified and so we expect the BOJ to instead indicate a continuation of its data-dependent approach.

Turning to the neutral rate of interest, as indicated in the press conference following the December 2025 meeting, the BOJ will maintain its stance of "carefully verifying economic and price trends." A similar verification stance will be stressed at Ueda's press conference following the next meeting, which will indicate a step-by-step assessment based on trends for the real economy.

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