

Daiwa's View

Points of interest regarding Dec BOJ MPM: Review of neutral interest rate and signaling about the pace of rate hikes

- Lower bound for the estimated neutral interest rate might be raised from 1.0% to 1.25%
- Hawkish messaging via outlook for Japan's economic activity/prices, conduct of monetary policy
- BOJ Governor Ueda not expected to show any rate-hiking urgency at post-meeting press conference

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A rate hike is likely at Dec MPM; Focus will be on indications of terminal rate and pace of rate hikes

In [his speech on 1 December](#), Governor Kazuo Ueda stated that “the likelihood of the baseline scenario for economic activity and prices being realized is gradually increasing.” He also revealed that the BOJ was independently gathering additional information on the initial momentum of the spring labor/management wage negotiations ahead of the Monetary Policy Meeting (MPM) on 18-19 December. His comment that the BOJ “will consider the pros and cons of raising the policy interest rate and make decisions as appropriate” suggests the possibility of a rate hike at the December meeting.

At the December MPM, the policy rate is likely to be raised to +0.75%, barring any major market turmoil due to the release of data such as the US jobs report or US CPI before the December meeting. The BOJ will likely cite the following reasons for the rate hike: (1) receding uncertainty regarding future tariff policies and (2) confirmation of momentum towards the initial phase of the spring wage negotiations through statistics (incl. BOJ Tankan) and from hearings. Against this backdrop, we think that the BOJ will conclude that the likelihood has increased that the outlook will be realized.

At [the press conference following the October MPM](#), Governor Ueda mentioned that the BOJ wanted to gather information on the initial momentum of the spring wage negotiations, suggesting that a rate hike in either December or January was anticipated at that time. The choice of December may have been influenced by the current weakness of the yen and the subsequent progress made in communicating with the government. In fact, Prime Minister Sanae Takaichi commented about the weak yen on the 9th, saying that the government “will take appropriate measures as necessary against excessive fluctuations and disorderly movements,” and on the same day, Governor Ueda also pointed out the importance of the impact of currency fluctuations on the inflation outlook. As such, concern about forex rates is shared by both the government and the BOJ.

That said, with the media having already reported about the possibility of a rate hike in December, the hike itself is likely well within expectations. Of particular interest at the meeting will be the BOJ's views on the neutral interest rate (the terminal rate), and wording suggesting the pace of future rate hikes—i.e., changes in wording concerning the economic/price outlook and the conduct of monetary policy—as well as what the Governor says in his regular press conference.

Discussion regarding estimates of neutral rate of interest

During the press conference following his 1 December speech, Governor Ueda made a comment regarding the neutral rate of interest, saying that, if there were another rate hike, the BOJ would like to make its thinking a little clearer at that time. During his 4 December Diet testimony, Ueda also explained that, if the BOJ could narrow it down a bit more in the future, it would make the results public as appropriate. In light of those statements, people will be interested to see whether there will be a quantitative change to the estimated value for the neutral rate of interest, which is currently seen as 1% to 2.5%, or whether the BOJ will only provide qualitative statements.

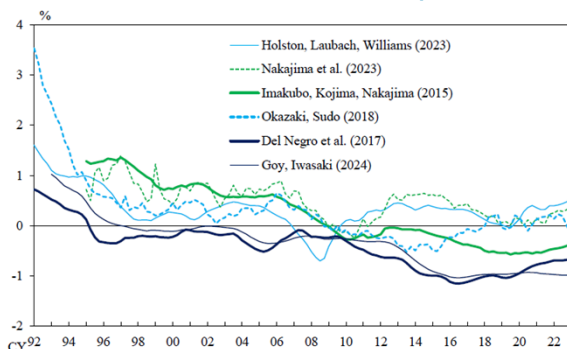
The estimated natural rate of interest published by the BOJ in the Working Paper series and other documents is -1% to 0.5% (as of the period estimated, Jan-Mar 2023)¹. The neutral rate of interest is understood to be the natural rate of interest plus the inflation target (2%). However, the natural rate of interest is inherently a medium- to long-term concept that cannot be directly observed. While it can serve as a point of reference for short-term monetary policy operations, it cannot be a definitive indicator. In January 2025, Deputy Governor Ryoza Himino noted that the natural rate of interest could not be observed directly, and could only be estimated and evaluated by making various assumptions and engaging in complex data processing. The same month, Governor Ueda also commented that the BOJ did not view any particular figure as a wall, but that there would be reactions in the economy as we got very close to the neutral rate.

Therefore, with the estimates for the natural interest rate and neutral interest rate merely being points of reference with a range, short-term monetary policy operations have no choice but to proceed by trial and error while observing the impact on the economy. If the BOJ were to nevertheless venture to conduct a review of the neutral rate, it would very much come across [as a communication tool signaling continued rate hikes, triggered by the current depreciation of the yen](#).

If a review were conducted as part of communication triggered by the weak yen, figures for the neutral rate might be released if the estimated range justified continued rate hikes. Whether or not the lower bound of the range is revised upwards will be of particular interest when determining the leeway for future rate hikes.

Extrapolating based on Hatayama and Iwasaki (2024)², which estimated the equilibrium yield curve referencing the Goy and Iwasaki (2024) model, [which represents the current lower bound estimate, suggests a 21bp increase from the equilibrium level](#). Based on this estimate, it is highly likely that the estimated range will suggest continued rate hikes, with the possibility of the lower bound of the neutral rate of interest being raised from the current 1% to 1.25% at the December meeting. That said, the announcement regarding the neutral rate could come after the press conference following the December meeting or when Ueda makes his next speech on 25 December.

Estimations of Natural Rate of Interest in Japan

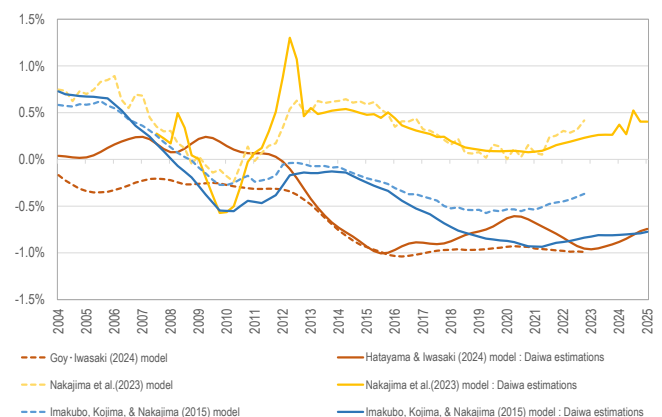


Notes: Del Negro et al. (2017), HLW (2023), Imakubo, Kojima, and Nakajima (2015), Nakajima et al. (2023), and Okazaki and Sudo (2018) were estimated by the authors; Goy and Iwasaki (2024) was estimated by Hatayama and Iwasaki (2024).

Sources: Bank of Japan; Ministry of Finance; Ministry of Health, Labour and Welfare; Ministry of Internal Affairs and Communications; Cabinet Office; Bloomberg; Consensus Economics "Consensus Forecast;" Google Mobility Index.

Source: Reprinted from BOJ materials.

Estimations of Natural Rate of Interest: Update by Daiwa Securities



Source: BOJ, Daiwa; compiled by Daiwa.

Furthermore, as pointed out in [the Summary of Opinions at the October MPM](#), developments involving an expansion of credit have been observed in areas such as real estate and bank lending, suggesting that the impact of rate hikes on the real economy is limited at present. Even if a quantitative estimate of the neutral rate were not released, we anticipate that wording saying

¹ Sugioka, Nakano, and Yamamoto (2024). [Recent Developments in Measuring the Natural Rate of Interest](#). Bank of Japan Working Paper Series.

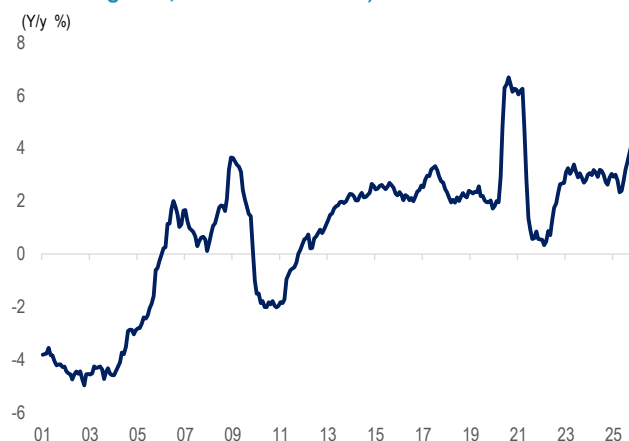
² Hatayama & Iwasaki (2024). [Estimating the Natural Yield Curve in Japan Using a VAR with Common Trends](#). Bank of Japan Working Paper Series

that real interest rates are at an extremely low level will be retained, keeping the nuance that there is still some ways to go until we reach the terminal rate.

◆ **Summary of Opinions at Oct MPM: Opinions on Economic Developments (10 Nov 2025)**

- Expansionary developments have started to be seen on the credit side, such as bank lending mainly for real estate and for mergers and acquisitions, and this shows the effects of having significantly negative real interest rates.
- Given that real interest rates have been significantly negative, attention is warranted on developments in factors such as real estate prices.

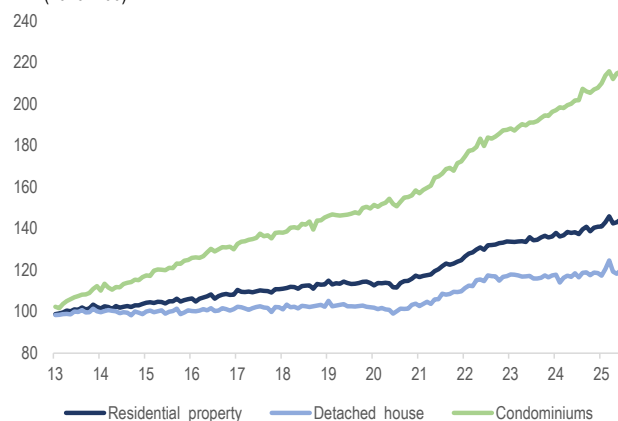
Y/y Change in Average Outstanding Loans (total of major, regional, and *shinkin* banks)



Source: BOJ; compiled by Daiwa.

Property Price Index (residential)

(2010=100)



Source: Ministry of Land, Infrastructure, Transport and Tourism; compiled by Daiwa.

As mentioned above, if the BOJ were to retain the nuance that there was still some ways to go until we reached the terminal rate by either (1) raising the lower bound of the estimated neutral rate or (2) retaining wording saying that real interest rates were at an extremely low level, that message itself would be hawkish. However, as the estimation of the natural rate of interest is merely a point of reference with a range, for near-term policy operations, the BOJ will likely maintain its conventional approach to communication, saying that it will assess the impact on the economy and prices. In short, while there is leeway for the lower bound of the neutral rate to be raised, the range of the estimate itself is not expected to change significantly, and it is unlikely that the specific level would be stated explicitly.

Economy/price understanding, baseline projections for economic activity/prices

We expect the current understanding of Japan's economic activity and prices to remain unchanged from the BOJ's October *Outlook for Economic Activity and Prices* report (*Outlook Report*). In other words, the Bank will likely maintain its assessment that economies (Japan, overseas) have, "Recovered moderately, although some weakness has been seen in part."

Also, in his 1 December speech, Governor Ueda said, "Downside risks to the overall economy have diminished somewhat," while maintaining the previous view that the impact of tariffs has yet to materialize and that, "Overseas economies will slow down temporarily under the impact of tariff policies." In particular, Ueda expressed his view that the key to whether or not this outlook is realized will largely depend on the US, while such uncertainties persist.

Based on that view, the expressions for Japan's economic activity and price outlooks are also expected to remain largely unchanged. In other words, the BOJ will likely maintain its outlook that, for now, Japan's economic growth is "likely to be modest" due to the impact of trade policies and other factors, but thereafter the growth rate is "likely to rise."

That said, the "Summary of Opinions" from the October Monetary Policy Meeting also included the view that even if the impact of tariffs fully materializes, any slowdown in growth would be limited. Furthermore, the FOMC's December Summary of Economic Projections presented an

optimistic US outlook incorporating productivity growth and a forecast of disinflation amid tariffs. If this outlook materializes, we would expect any tariff policy impacts on Japan's growth rate to be quite small. If such an optimistic outlook for the US economy were to gain traction within the BOJ, there is a possibility that expressions such as "the pace of economic growth is temporarily slowing" could be revised in a more positive direction. If such wording is revised, the bar for future rate hikes would likely be lowered.

◆ **Oct Outlook for Economic Activity and Prices: Baseline Scenario of Outlook for Economic Activity (30 Oct 2025)**

Japan's economic growth is likely to be modest, as trade and other policies in each jurisdiction lead to a slowdown in overseas economies and to a decline in domestic corporate profits and other factors, although factors such as accommodative financial conditions are expected to provide support. Thereafter, Japan's economic growth rate is likely to rise, with overseas economies returning to a moderate growth path.

◆ **Summary of Opinions at Oct MPM: Opinions on Economic Developments (10 Nov 2025)**

Even if the impact of U.S. tariff policy becomes pronounced, the expected scale of the impact has become smaller than it was before. Therefore, it is also likely that Japan's economic growth will not be too modest. As a baseline scenario, Japan's economy is expected to continue to grow at a pace slightly above its potential growth rate in both fiscal 2025 and 2026.

Expressions regarding conduct of monetary policy

We expect the December meeting statement to include wording regarding the conduct of monetary policy (wording regarding conduct of monetary policy also provided when rate was hiked in Jan 2025). Among these, the three expressions "real interest rates are at significantly low levels," "in accordance with improvement in economic activity and prices," and "high uncertainties remain" are particularly noteworthy. As mentioned previously, we expect the expression "real interest rates are at significantly low levels" to be maintained.

The wording "in accordance with improvement in economic activity and prices" was added from the April 2025 *Outlook Report* with the aim of indicating the path for interest rate hikes, while taking into account the full implementation of tariff policies. However, if the expression "the pace of economic growth is temporarily slowing" remains in the baseline scenario for economic activity and prices, it is likely that the wording "in accordance with improvement in economic activity and prices" will also be retained.

Meanwhile, in [his November speech](#), policy board member [Asahi Noguchi](#) pointed out that, given the limited impact of tariffs, the BOJ may revert to its basic policy defined as, "If economic activity and prices develop in line with the Bank's outlook, the Bank will gradually adjust the degree of monetary accommodation." If expressions like "the pace of economic growth is temporarily slowing" or "in accordance with improvement in economic activity and prices" are revised in a more positive direction, that could be interpreted as lowering the bar for future rate hikes.

Also, with the recognition that downside risks to the economy, including the impact of tariff policies, have diminished, wording such as "high uncertainties remain" may also be revised to more accommodative expressions. For example, a change to a more limited expression such as, "We will closely monitor the impact of trade policies and other factors in various countries" is conceivable.

That said, in [a 9 December Financial Times interview](#), Ueda indicated that, "Rising food prices or yen depreciation may persist longer than expected, potentially impacting inflation expectations." He also stated that, "The risk of inflation accelerating is not particularly high." Based on these statements, it seems unlikely that Ueda will express an urgency to make further rate hikes at his post-meeting press conference. At that press conference, Ueda will likely touch on the previous policy, specifically, "If the outlook materializes, we will adjust the degree of monetary accommodation."

◆ **Oct Outlook for Economic Activity and Prices: Conduct of Monetary Policy (30 Oct 2025)**

As for the conduct of monetary policy, given that **real interest rates are at significantly low levels**, if the aforementioned 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 that **high uncertainties still remain** regarding the impact of trade and other policies in each jurisdiction, it is important for the Bank to carefully examine factors such as developments in economic activity and prices as well as in financial markets at home and abroad, and judge whether the outlook will be realized, without any preconceptions. With the price stability target of 2 percent, the Bank will conduct monetary policy as appropriate, in response to developments in economic activity and prices as well as financial conditions, from the perspective of sustainable and stable achievement of the target.

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