

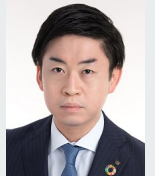
Daiwa's View

BOJ shifting from steady-paced rate hikes to event-driven approach

- Economic resilience maintained even under supply constraints amid materialization of upside risks to prices
- Shift in policy conduct premised on continued rate hikes and move towards an event-driven approach
- Distance to the neutral rate and a more flexible rate-hike path (implications of front-loading and acceleration)
- Political policy constraints formed amid pursuit of both strong economic growth and stable inflation

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Economic structure in which growth slows but does not collapse

The BOJ's assessment of economic conditions in the "Summary of Opinions" at the April Monetary Policy Meeting (MPM) was framed not merely as a phase of slowdown, but as a state in which deceleration and resilience coexist. While the deterioration in the terms of trade due to higher crude oil prices is acting as a drag on growth, corporate earnings remain at high levels. With wage hikes continuing and various government measures also providing support, the economy as a whole is maintaining its recovery trend.

As a result, even amid the presence of an exogenous shock in the form of higher energy prices, the economy has continued to withstand the pressure without weakening significantly. At the same time, differences across industries have also been observed—while the impact of higher import prices is strongly evident in the oil and chemicals sectors, prices have risen in the IT sector supported by external demand.

◆ Opinions on Economic Developments in Summary of Opinions at Apr MPM (12 May 2026)

The increased burden caused by a deterioration in the terms of trade has been shared between firms, households, and the government, through, for example, the pass-through of cost increases to selling prices by firms and the provision of gasoline subsidies by the government. **With high levels of profits having been accumulated in the corporate sector and expectations for wage hikes as a result of the annual spring labor-management wage negotiations, Japan's economy appears to be reasonably resilient to downward pressure.**

Prices are framed as skewed to the upside

The discussion on prices formally includes risks in both directions, but it is notable that the overall assessment is clearly skewed to the upside. The relationship in which wages and prices rise in interaction with each other has been maintained, and there is a shared view that the underlying inflation will follow a path of gradual increase. On top of this, developments in crude oil prices against the backdrop of the situation in the Middle East would appear in the short term as a broad-based increase in costs, and, if prolonged, as stronger price increases through supply constraints.

By contrast, downside risks to prices are limited to cases in which a "full-fledged disruption of supply chains" occurs. Taking into account the possibility of quantitative constraints centered on petrochemical products, supply-side constraints would act as a factor pushing up prices. Furthermore, given the adaptive nature of inflation expectations, the progress in pass-through of costs to prices, and the confirmed continuation of wage hikes, the current environment is one in which temporary cost increases are easily reflected in underlying inflation.

◆ Opinions on Prices in Summary of Opinions at Apr MPM (12 May 2026)

For many years, all available policy measures from both monetary and fiscal sides have been mobilized to overcome deflation. Against this backdrop, the government's various measures have become established, and **inertia in wage increases and in the pass-through of cost increases to selling prices is in effect, giving rise to the risk of higher inflation due to the rise in crude oil prices.**

The Middle East situation is recognized as a supply-constraint shock

The situation in the Middle East is being framed not so much as uncertainty, but rather as a shock accompanied by supply constraints. In addition to constraints on crude oil supply, board members pointed out spillover effects to resources as a whole, restrictions on navigation through the Strait of Hormuz, and the possibility of quantitative constraints on petrochemical products. All of these would act as supply-side constraints in the direction of pushing up prices.

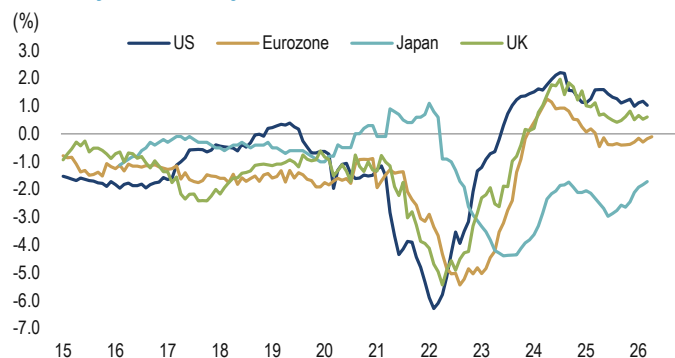
Given that monetary and fiscal conditions remain accommodative (with sentiment as seen from stock prices remaining firm) and that price pass-through behavior is becoming entrenched, the current phase is one in which the conditions are in place for higher crude oil prices to spill over into a broad range of prices.

Monetary policy is becoming premised on “continued rate hikes”

The policy decision was to maintain the status quo for the time being — that is, to wait and see — because the future course of the situation in the Middle East remains unclear. At the same time, the opinions of policy board members included views such as “it is quite possible that the Bank will raise the policy interest rate from the next MPM onward, even if the future course of the situation in the Middle East remains unclear” and “barring evident signs of an economic slowdown, the Bank should raise the policy interest rate soon.” As such, the direction of policy is toward an early rate hike, including at the next meeting.

As before, there is also a shared recognition of the need to adjust the degree of monetary accommodation, taking into account that real interest rates remain at extremely low levels and that the underlying rate of inflation is rising.

Real Policy Rates in Major Nations



Source: Fed, ECB, BOE, BOJ, US Department of Labor, Ministry of Internal Affairs and Communications, Eurostat, Office for National Statistics; compiled by Daiwa.

Note: Real policy interest rate is calculated by subtracting core inflation rate from policy interest rate. (Core-core CPI is used for Japan).

Policy framework shifting away from being dependent on the outlook towards being responsive to risks

The most important thing in this “Summary of Opinions” was the change in the policy framework. A proposal was made to review the previous wording “in accordance with improvement in economic activity and prices.” [This signifies a shift away from a framework in which policy changes are made after having confirmed that the outlook was achieved and towards a framework in which policy responses are made in accordance with risks.](#) As a result of this change, policy decisions will be made in response to changes in prices and the external environment, rather than in response to the passage of time.

In particular, the most noteworthy part of this “Summary of Opinions” with regard to the path for rate hikes was that there was a weakening of the constraint associated with the previously assumed pace of one rate hike every six months. Specifically, while the opinion was voiced that “it will be appropriate for the Bank to return to the previous pace of rate hikes,” there were also views that “there will be a need to raise the policy interest rate to the level of the neutral interest rate at an earlier timing,” that “it will be necessary for the Bank to continue to raise the policy

interest rate at intervals of a few months,” and that “it will be necessary to accelerate the pace of rate hikes without hesitation.”

In this respect, the opinions were clearly consistent with remarks by BOJ officials reported by Jiji Press. The article in question reported that, **when raising rates in a risk-responsive manner when the probability of achieving the outlook has declined, the timing of rate hikes will become event-driven, rather than following a pace of something like once every six months.** This indicates the view that the timing of rate hikes should be determined flexibly in response to changes in conditions, such as crude oil prices and yen depreciation.

Furthermore, the same report also indicated an awareness that the kind of steady-paced rate hikes that were seen before the imposition of Trump tariffs are no longer appropriate. This is consistent with the shift from rate hikes at a fixed pace to hikes at a pace that varies depending on certain conditions, mentioned in the latest “Summary of Opinions.” It was also confirmed that monetary policy action is currently deemed necessary in light of the progress made with price pass-through, unlike when authorities looked through past inflationary pressure during the crude oil price surge in 2022.

Opinions on Monetary Policy in Summary of Opinions at Apr 2026 MPM

Opinions on Monetary Policy	
1	Given that underlying CPI inflation has been approaching 2 percent and real interest rates are at significantly low levels, it is appropriate that the Bank continue to raise the policy interest rate and adjust the degree of monetary accommodation, in response to developments in economic activity and prices as well as financial conditions.
2	While Japan's economic growth rate is expected to be at around the same level as the potential growth rate for the time being, the Bank may need to address the risk of prices deviating upward. Considering such circumstances, with regard to the guideline for the conduct of monetary policy, it is desirable to revise the previous wording, "in accordance with improvement in economic activity and prices."
3	It is difficult to foresee the impact of the situation in the Middle East, and the Bank needs to adopt a wait-and-see approach at this meeting.
4	Given that inflation expectations in Japan are considered to be adaptive to some degree, the Bank should maintain the current policy interest rate at this meeting, with the year-on-year rate of increase in the CPI (all items less fresh food) for March remaining below 2 percent due in part to the waning of the past rise in food prices.
5	At this juncture, a policy interest rate hike that prioritizes the containment of inflation is highly likely to have adverse effects on economic developments, including employment and production. On the other hand, the Bank is also not in a situation where a policy interest rate cut is possible. Given that the future course of the situation in the Middle East is unclear, it is most appropriate for the Bank to maintain its current monetary policy.
6	The situation in the Middle East remains unclear, and the current circumstances do not suggest a pressing need to quickly raise the policy interest rate. However, given that the impact on Japan's economy will become apparent to some degree, it is quite possible that the Bank will raise the policy interest rate from the next MPM onward, even if the future course of the situation in the Middle East remains unclear..
7	It is unlikely at present that a strong wage-price spiral will emerge in domestic industries, and given the current level of underlying inflation, there is no need to take hasty action at this point. However, barring evident signs of an economic slowdown, the Bank should raise the policy interest rate soon.
8	Although it seems unlikely that the impact of the situation in the Middle East will be limited and ease in the short term, market sentiment as observed in stock prices has remained solid despite the rise in crude oil prices. Firms' price-setting behavior in response to rising prices has become more active, and risks to prices are skewed to the upside. It is appropriate for the Bank to adjust the degree of monetary accommodation in line with its mandate of achieving price stability from the perspective of safeguarding people's livelihoods and contributing to their peace of mind.
9	Japan's real policy interest rate is by far at the lowest level globally, and it is necessary for the Bank to continue to adjust the negative real interest rate in preparation for the second-round effects of price rises.
10	While downside risks to economic activity and upside risks to prices could both heighten, in conducting monetary policy, it is necessary to pay due attention, in particular, to keep the risk of inflation significantly deviating upward from materializing and thereby exerting an adverse impact on the economy afterward.
11	Since the main risk factor for a downward deviation in economic activity is a rise in prices, the Bank should make it a priority to carry out its mission as the "guardian of price stability" and thereby contain a downward deviation of economic activity.
12	In a situation where the potential growth rate remains resilient and Japan's economy recovers moderately, it is appropriate for the Bank to proceed further with the normalization of the policy interest rate by raising the policy rate when the real interest rate declines reflecting price rises.
13	The policy interest rate is still some way from the neutral interest rate, and it will be necessary for the Bank to continue to raise the policy interest rate at intervals of a few months. Furthermore, in the case where upside risks to prices increase, it will be necessary to accelerate the pace of rate hikes without hesitation.
14	If recovery in crude oil supply comes in sight, it will be appropriate for the Bank to return to the previous pace of rate hikes. Meanwhile, if tension over the situation in the Middle East becomes prolonged, there will be a need to raise the policy interest rate to the level of the neutral interest rate at an earlier timing to prevent underlying inflation from deviating upward. That said, if disruptions in supply chains become significant, it will be desirable for the Bank to maintain accommodative financial conditions without raising the policy interest rate.
15	It is not desirable for the Bank to be perceived as always signaling a policy interest rate hike in advance. It is necessary for the Bank to explore how best to communicate its policies.

Source: BOJ; compiled by Daiwa.

Political constraints: Compatibility with growth remains a condition

The policy path ahead is based on the premise of continued rate hikes, while also including the possibility that the pace could be brought forward relative to previous assumptions. Previously, it had been assumed that the neutral rate (around 1.5%) would be reached through rate hikes every six months, but that assumption has weakened this time. The possibility that the number of rate hikes will increase in response to upside risks to prices, and that the terminal rate will move higher, is now being recognized, with 2% clearly coming into view.

At the same time, what has become clear as a difficult point in the conduct of monetary policy is that political constraints continue to exist. In this "Summary of Opinions," the Cabinet Office pointed out that "Toward achieving both strong economic growth and stable inflation, it is important that monetary policy be conducted as appropriate." This expression, "achieving both strong economic growth and stable inflation," is one that Prime Minister Sanae Takaichi and Minister of State for Economic and Fiscal Policy Minoru Kiuchi have repeatedly used.

◆ Cabinet Office's Opinions in Summary of Opinions at Apr MPM (12 May 2026)

• **Toward achieving both strong economic growth and stable inflation, it is important that monetary policy be conducted as appropriate.** The government expects the Bank to conduct monetary policy as appropriate toward achieving the price stability target of 2 percent in a sustainable and stable manner, while paying due attention to factors such as economic developments at home and abroad and closely cooperating with the government in accordance with the spirit of the Bank of Japan Act and of the joint statement of the government and the Bank.

The same context was also confirmed at the latest meeting of the Council on Economic and Fiscal Policy. At the meeting, private-sector members, taking into account the situation in the Middle East, proposed that they "expect the implementation of appropriate monetary policy, while also paying attention to supply-demand conditions for funds." As a response to a short-term supply shock, this calls for flexibility in policy, while at the same time requiring consideration for economic conditions. The council also stated that, in light of the importance of policy coordination between the government and the BOJ toward achieving both "strong economic growth" and "stable inflation," it would "confirm the status of these initiatives as appropriate."

This series of expressions does not deny rate hikes themselves, but it indicates that compatibility with growth is shared as a prerequisite in the conduct of monetary policy. In addition, indirect constraints remain on the degree of freedom in monetary policy, including the continued attendance of government officials (ministers) at meetings.

◆ Materials at the 6th meeting of the Council on Economic and Fiscal Policy on 11 May 2026 (submitted by expert members)

- We expect the BOJ to implement appropriate monetary policy while closely monitoring price fluctuations, including expectations, and also paying attention to supply-demand conditions for various funds in the market.
- **In light of the importance of policy coordination between the government and the BOJ toward achieving both "strong economic growth" and "stable inflation," the Council on Economic and Fiscal Policy will confirm the status of these initiatives as appropriate.**

Conclusion: Policy is being detached from the timeline

Based on the above, we can say that the Japanese economy is withstanding downward pressure from higher crude oil prices, and, under these conditions, upside risks to prices originating from supply constraints have become dominant. In this environment, monetary policy is premised on continued rate hikes, but the timing and pace of those hikes will not be based on the conventional timeline. Rather, they will be determined in response to changes in the environment, such as crude oil prices and forex rates.

The latest "Summary of Opinions" can be said to indicate that the BOJ's policy has shifted from a steady-paced rate-hike path every six months to an event-driven path that changes in response to risks. That is what is meant by "in response to developments in economic activity and prices as well as financial conditions," and this policy must not be politically driven.

On 12 May, US Treasury Secretary Scott Bessent said that he was confident BOJ Governor Kazuo Ueda would successfully guide monetary policy. And, as stated in the “Summary of Opinions,” “Since the main risk factor for a downward deviation in economic activity is a rise in prices, the Bank should make it a priority to carry out its mission as the ‘guardian of price stability’ and thereby contain a downward deviation of economic activity.”

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