

The Bank of Japan could be just months away from more policy normalisation

The Bank of Japan ended its negative interest rate and yield curve control in March, hoping strong wage growth would boost inflation and consumption. It won't hesitate to take further action if upcoming data confirms a recovery in real wages and consumption



Looking up! The Bank of Japan Governor, Kazuo Ueda, is mulling another rate hike

Expect front-loaded rate hikes in the second half of the year

We expect the Bank of Japan to raise its target rate to 1.0% by the end of 2025. But even if we slowly get there, overall monetary conditions will remain accommodative as real interest rates will remain in negative territory. Don't expect any sudden shock! A 25bp hike in most quarters should be sufficient for the economy to digest the rate increases.

In addition, should inflation fall below the 2% target range, the BoJ needs enough room to react. So we expect the Bank to raise its policy rate target to a range of 0.15-0.25% in July and 0.40-0.50% in October, followed by two more 25bp hikes in the first half of next year.

But what happens in the near term will depend on inflation's path, earnings, and consumption data between now and July. The BoJ's Quarterly Outlook Report will also be closely watched as it

could give a hint as to the Bank's future policy decision. If we are right about inflation staying above 2% and cash earnings rising above 5% from May, the BoJ is likely to hike as early as July.

The surge in wages could be seen in payrolls as early as May

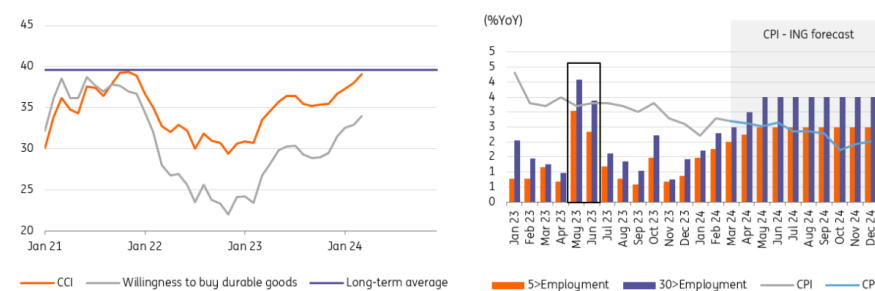
Last year's wage negotiations resulted in a relatively solid 3.6% YoY increase, but consumer prices rose by 3.3%, resulting in no real wage growth at all. However, in 2024, wage growth is expected to exceed 5%, while consumer prices are expected to slow to 2.3%, turning real wage growth positive. History tells us that newly agreed wage increases usually kick in from May onwards. Data on that will be released in early July, just a few weeks before the July Bank of Japan meeting. Also, given the strong corporate earnings this year, we expect larger-than-normal bonus payments to be made, so strong wage growth should pave the way for that BoJ rate hike.

Household consumption has been picking up despite some distractions

After a large dip in the fourth quarter of 2023, retail sales in Japan finally rose on a monthly basis in the first two months of this year despite car sales dropping for the past three months and the major earthquake at the beginning of January. We expect a technical payback in car sales from March as a distinctive factor related to a car safety scandal issue fades.

Given that's a major component of total household spending, it suggests retail sales are set to improve more meaningfully in the second quarter, supported by stronger wage growth and associated consumption. In addition, a leading indicator for household consumption, the consumer confidence index, has been rising for the past six months. Consumers' willingness to buy durable goods has advanced meaningfully as well, suggesting a consumption recovery is ahead of us.

Consumer confidence advanced for six months while real cash earnings is likely to turn positive from May



Source: CEIC, ING estimates

Author

Min Joo Kang

Senior Economist, South Korea and Japan

min.joo.kang@asia.ing.com

Disclaimer

This publication has been prepared by the Economic and Financial Analysis Division of ING Bank N.V. (“ING”) solely for information purposes without regard to any particular user’s investment objectives, financial situation, or means. *ING forms part of ING Group (being for this purpose ING Group N.V. and its subsidiary and affiliated companies)*. The information in the publication is not an investment recommendation and it is not investment, legal or tax advice or an offer or solicitation to purchase or sell any financial instrument. Reasonable care has been taken to ensure that this publication is not untrue or misleading when published, but ING does not represent that it is accurate or complete. ING does not accept any liability for any direct, indirect or consequential loss arising from any use of this publication. Unless otherwise stated, any views, forecasts, or estimates are solely those of the author(s), as of the date of the publication and are subject to change without notice.

The distribution of this publication may be restricted by law or regulation in different jurisdictions and persons into whose possession this publication comes should inform themselves about, and observe, such restrictions.

Copyright and database rights protection exists in this report and it may not be reproduced, distributed or published by any person for any purpose without the prior express consent of ING. All rights are reserved. ING Bank N.V. is authorised by the Dutch Central Bank and supervised by the European Central Bank (ECB), the Dutch Central Bank (DNB) and the Dutch Authority for the Financial Markets (AFM). ING Bank N.V. is incorporated in the Netherlands (Trade Register no. 33031431 Amsterdam). In the United Kingdom this information is approved and/or communicated by ING Bank N.V., London Branch. ING Bank N.V., London Branch is authorised by the Prudential Regulation Authority and is subject to regulation by the Financial Conduct Authority and limited regulation by the Prudential Regulation Authority. ING Bank N.V., London branch is registered in England (Registration number BR000341) at 8-10 Moorgate, London EC2 6DA. For US Investors: Any person wishing to discuss this report or effect transactions in any security discussed herein should contact ING Financial Markets LLC, which is a member of the NYSE, FINRA and SIPC and part of ING, and which has accepted responsibility for the distribution of this report in the United States under applicable requirements.

Additional information is available on request. For more information about ING Group, please visit www.ing.com.