

## Bank of Japan keeps policy settings unchanged – for now

The BoJ has unanimously decided to maintain its ultra-easing monetary policy as it is still looking for clearer signs of sustainable inflation growth. We believe higher-than-expected inflation, a continued solid economic recovery, and growing pressures from the weaker yen will eventually convince the bank to revise its YCC policy in July



Kazuo Ueda, Governor of the Bank of Japan

**-0.1%** BoJ policy balance rate

As expected

# 0.0% BoJ 10-year yield target

As expected

## The Bank of Japan's no change decision was very much in line with market expectations

The Bank of Japan's (BoJ's) monetary policy statement hasn't changed much at all on its view on the growth and inflation outlook and hasn't given a hint of any exit plans. The BoJ kept its dovish stance by repeating that "the bank will not hesitate to take additional easing measures if necessary".

What is more worth noting, however, is that the BoJ pointed out that wage gains are expected, accompanied by changes in firms' price and wage-setting behaviour. We believe that this is the change of structural and behavioural disinflation factor that the BoJ has been looking for.

To be precise, the latest labour cash earnings data were disappointing despite the surprisingly solid Shunto (Spring wage negotiations) results. Thus, an improvement in earnings is another factor to watch to gauge the BoJ's policy action and we will also see how earnings data unfold in the coming months.

We believe that rising asset prices are another important factor in sustainable inflation. With recent rallies in Japanese equity markets and the gradual rise in housing prices, the positive wealth effect is likely to keep inflation above the BoJ's target, in our view.

## Dovish comments from Governor Ueda

Governor Kazuo Ueda's comments at the press conference were no different from what the statement suggested. Ueda is concerned that the outlook for wage growth is highly uncertain and wants to see clearer signs of sustainable inflation. There were no hints about future policy adjustments in his comments.

However, we still think that the BoJ can change its YCC policy in July for the following reasons:

1. First, the BoJ is likely to upgrade its inflation forecast in the quarterly outlook report in July. That could more easily justify the BoJ's policy action. As mentioned previously, we expect inflation to remain higher for longer than expected.
2. Second, the overall bond market functions have improved, although there have been some fluctuations since December's YCC band widening, and the market is not testing BoJ's YCC upper limit of 10Y JGB. Thus, we believe that the market stress has been reduced, and it is a good time for the BoJ to revisit its YCC policy to reflect changes in market conditions.
3. Third, a weaker yen will likely add more inflationary pressures. If the BoJ continues to maintain its current policy setting, it would risk leaving the BoJ "behind the curve". We believe that Japan's economy is recovering solidly compared to other major economies and will continue to outperform in the future. But, if monetary policy fails to reflect this shift of economic fundamentals and the BoJ keeps its dovish policy, then the yen should depreciate

even more.

4. Lastly, by the time of the July meeting, the US Federal Reserve will have already decided on monetary policy, and where the UST will be is another factor the BoJ should consider.

From now on, we will be closely watching upcoming data releases such as June Tokyo CPI, labour cash earnings, and the movement in JPY, to see if these give a clearer signal of sustainable inflation.

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