The Bank of Japan maintains its policy rate settings and JGB purchases

The Bank of Japan has disappointed the market again with a vague announcement to reduce its purchases by an unspecified amount at an unspecified point in time. The market will have to wait until the July meeting to hear more

The Bank of Japan, Tokyo

0.1% Target range (Upper Bound)

As expected

Lack of detail on JGB purchase plans

As widely expected, the Bank of Japan kept its policy rates unchanged between 0% to 0.1%. But against market expectations, the central bank decided to announce its JGB purchase programme in detail at the July meeting.

Reading through the statement, it is unclear how the BoJ will decide on the size of the purchases, as it notes that it will seek input and views from market participants. It sounds as though things are still undecided, aside from the choice to make an announcement in July. BoJ Governor Kazuo Ueda's comments at the press briefing were also rather vague. While Ueda mentioned that the reduction should be substantial, he also stressed that the process should be flexible and there is no certainty about how long the reduction will last.

Based on Ueda's comments, it is unlikely that the BoJ will immediately taper at its July meeting. Instead, it is likely to take a phased approach, starting with a small reduction (less than one trillion yen) from the end of 2024 and then gradually increasing it over 6-12 months.

We expect a rate hike in July as inflation is likely to accelerate

Ueda was, however, more explicit about rate hikes in our view. He confirmed that the BoJ will adjust policy rates if inflation accelerates as expected, and that a July rate hike is possible depending on data conditions. While this is a somewhat principled answer, between now and the 31 July meeting we have the May and June CPI readings and the July Tokyo CPI. In our view, these will come in above 3% or close to it from the current 2.5%, therefore fulfilling the conditions for a July rate hike.

With wage growth expected to be solid from May onwards, there is also a good chance that demand driven inflation will pick up, which is what the BoJ needs to see. We expect inflation, wage, and consumption conditions to drive a rate hike in July.

Yen softens, some eye 160 again

USD/JPY has traded higher after the BoJ failed to offer much support to the yen today. It seems many in the market are now looking for USD/JPY to push onto 160 and test whether policymakers in Tokyo are prepared to intervene again.

We are not so sure that USD/JPY needs to move substantially higher. The first reason is that US yields are dropping and may well drop further as US price data gives the Federal Reserve more confidence to cut rates in September. Yesterday's soft US May PPI data could point to a core US PCE price as low as 0.1% month-on-month when it is released on 28 June. This should keep US yields on the soft side particularly at the short end of the curve.

The second reason is that global FX volatility levels are rising on French political risk and some high-profile declines in some of the world's favourite carry trade target currencies such as the Mexican peso. Higher volatility should discourage fresh carry trade strategies and limit the yen's downside.

With regards to FX intervention, we very much doubt Japanese policymakers are expecting FX sales alone to put a lid on USD/JPY. However, what it may well tell us as it did during the successful intervention campaign in September/October 2022 is that Tokyo believes US rates are about to turn lower. We have some sympathy with that view and favour USD/JPY moving back below 155 over coming months.

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