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- BOJ continues to view wage–inflation dynamics as the key determinant for further rate hikes. While April is the earliest plausible timing, the BOJ may wait until June/July.
- Final wage outcomes this year remain uncertain. Rengo has called for a 5% wage increase, but firms face a weaker profit environment.
- BOJ appears ready to stabilize the JGB market in the event of an exceptional yield surge or market dysfunction, using a range of policy tools.
- Managing interest rates, capital flows, and the exchange rate simultaneously presents a dilemma.
- Stabilizing the yen would remain primarily the responsibility of the MOF through unilateral or coordinated FX interventions.

January meeting takeaways

The Bank of Japan kept its policy rate unchanged at 0.75% at the January 23 meeting. On the economic outlook, the BOJ upgraded its growth forecasts, revising FY25 GDP growth to 0.9% from 0.7% and FY26 growth to 1.0% from 0.7%. Core-core CPI inflation forecasts were also revised higher, to 3.0% from 2.8% for FY25 and to 2.2% from 2.0% for FY26.

On the interest rate outlook, Governor Ueda noted that wage hikes are having an increasing impact on prices, and that April’s statistics will be a key factor when considering future rate hikes.

In response to the surge in JGB yields, Ueda stated that the BOJ will conduct bond market operations nimbly in exceptional cases to promote stable yield formation.

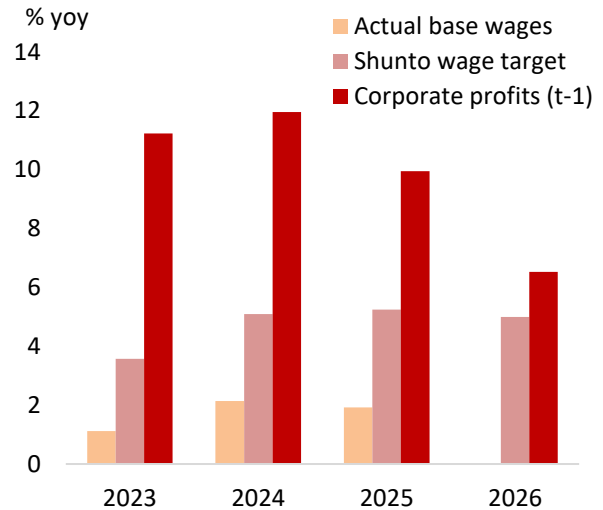
Regarding the weakening of the JPY, Ueda said that exchange rate movements may have a greater impact on inflation than before and therefore warrant close attention.

Interest rate outlook

The BOJ appears to continue to view wage–inflation dynamics as the key determinant for further rate hikes. April looks to be the earliest plausible timing for the next move, once the initial results of the spring wage negotiations become available. However, the BOJ may choose to wait until June or July, when more comprehensive wage data are released. Rengo

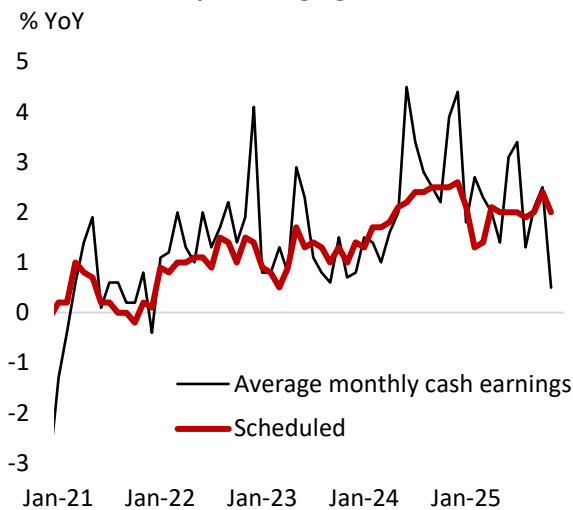
has publicly called for a 5% wage increase in the 2026 spring negotiations, following last year's strong outcome of 5.25%. That said, firms are facing a somewhat weaker profit environment, with corporate profits rising 6.5% y/y in 1Q–3Q25, down from 10% in 2024. As a result, final wage outcomes this year remain uncertain. **We currently expect the BOJ to deliver the next 25bp rate hike in July, raising the overnight call rate to 1.00%.**

Japan: Shunto wage target vs. actual wages



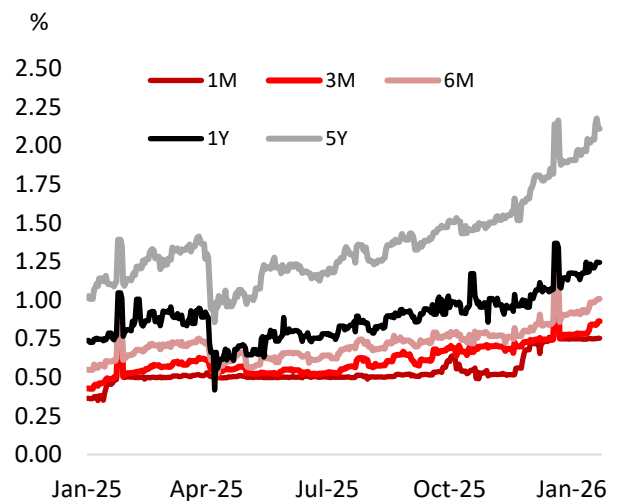
Sources: CEIC, DBS

Japan: Wage growth



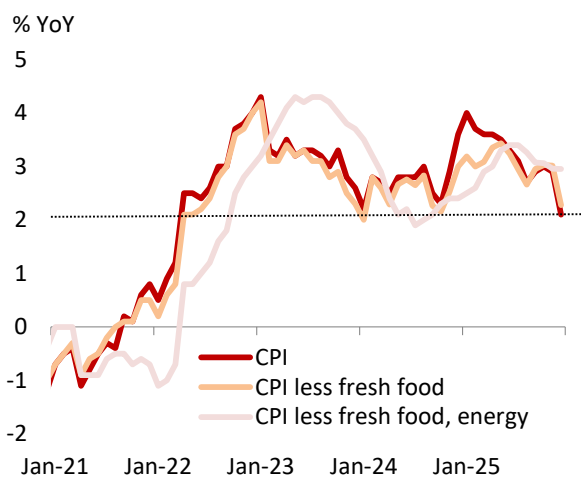
Sources: CEIC, DBS

Market implied BOJ policy rate



Sources: Bloomberg, DBS

Japan: CPI inflation



Sources: CEIC, DBS

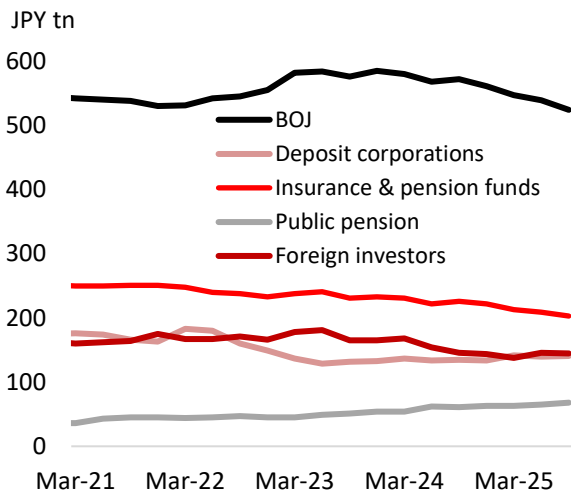
JGB implications

The BOJ also appears ready to step in to stabilize the JGB market in the event of an exceptional surge in yields or market dysfunction. It has several tools at its disposal, including increasing bond purchases outside preset schedules, conducting fixed-rate operations, adjusting the pace of quantitative tightening, and potentially reactivating yield curve control. The BOJ remains the largest

holder of JGBs, accounting for over 40% of the outstanding stock.

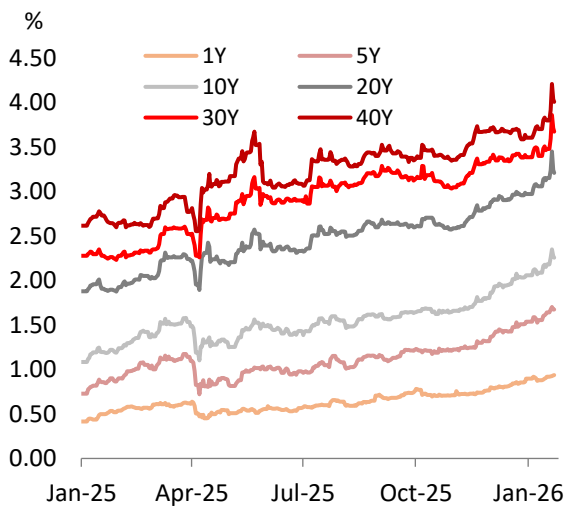
Ministry of Finance, relying on unilateral or coordinated FX interventions.

JGB and T-bill holdings, by investor



Sources: Bloomberg, DBS

JGB yields



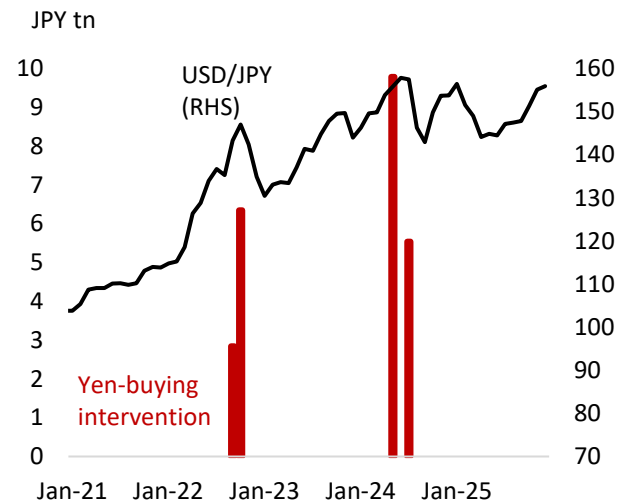
Sources: Bloomberg, DBS

JPY implications

The BOJ faces a dilemma in managing interest rates, capital flows, and the exchange rate simultaneously. If it keeps short-term rates unchanged while stabilizing long-term yields through JGB market interventions, it may need to tolerate renewed depreciation pressure on the JPY. Yen stabilization would therefore remain primarily the responsibility of the

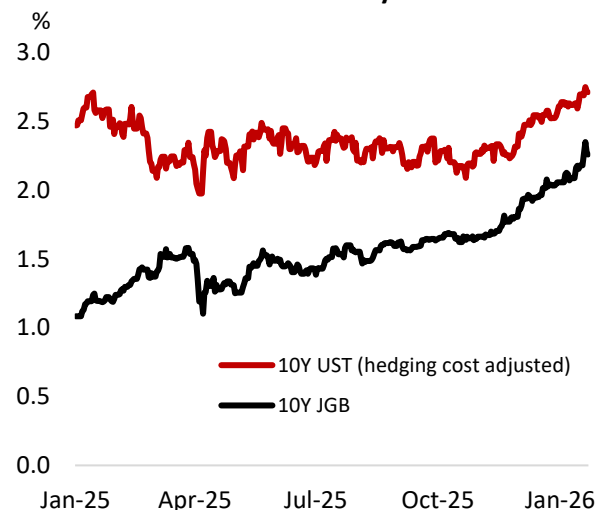
An automatic market stabilizer exists. If JGB yields rise above 3%, they would become relatively more attractive to Japanese banks and insurance companies compared with UST yields (assuming a 50% FX hedge ratio), prompting a rotation of assets from USTs to JGBs. Such flows by Japanese financial institutions could help to support the JPY.

Japan: FX intervention operations



Sources: CEIC, DBS

UST vs. JGB yields



Sources: Bloomberg, DBS

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