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FLASH NOTE – BOJ'S UEDA HOLDS BACK FROM SIGNALING DEC HIKE, TAKEAWAY IS Y155 TOLERABLE THOUGH Y160 NOT

Bank of Japan governor Ueda has held back from any obvious steps to prepare the market for a December rate hike in his highly anticipated speech Monday Japan time, though he signaled that the BoJ remains on a normalization path and the timing of the next move would be data-dependent at a time when the data has been moving in a favorable direction.

In particular, he did not characterize Yen weakness as creating upside risk to the inflation forecast, which would have been code for an imminent hike.

Given the turmoil that followed the BoJ's hike in July, we think the Japanese central bank will to the extent possible prepare the market in a relatively explicit way for its next move – though more by way of a discussion of progress and risks to the outlook than calendar-type guidance, which we think Ueda is keen to resist.

The speech did not obviously prepare the market, and his comments – which were constructive but careful – seemed most consistent with our existing baseline of a hike in January, which we reaffirm.

At the same time, Ueda – like Powell – is asserting more optionality over the timing of the next move in light of Trump-related uncertainty, so we do not think December is excluded if the Yen were to plunge further in the period ahead.

One takeaway for us from the lack of a currency-related rate signal is that the BoJ can tolerate Y155 under Trump risks at least near term as not obviously generating excessive inflation pressures in the context of constructive but slow-moving domestic data.

We think the debate would swing in favor of an early hike however if a further sharp fall in the Yen were to put the Japanese currency in danger of breaching Y160.

We have written before about how the BoJ is in danger of being whipsawed by Trump policy shocks with Yen weakness creating upside inflation risk, but trade uncertainty threatening a currently promising wage round and prospects for domestically generated inflation in 2025.

Ueda said it will likely take time to get clarity on Trump policies and the implications for the global economy. In the interim the BoJ will try to stick to the prior plan to move rates up again once in the coming months, January is the base case, December if the currency tanks near-term.

Ueda reiterated that the BoJ continues to believe that provided the economy evolves along the path seen in its projections, it will be appropriate over time to gradually raise interest rates from current deeply negative real levels.

The BoJ had previously set three conditions that had to be met before the Policy Board would begin to consider when to raise rates again: confidence in the US soft landing, stability in global markets and continued progress in the domestic Japanese data.

Ueda's analysis suggested these three preconditions are well on the way to being met, with increased likelihood of a US soft landing, market conditions that are generally better though susceptible to "geopolitical risks" and solid business investment along with firming consumption as nominal wage increases, with more signs of wage-related service prices increases.

Looking forward, he said the BoJ would be monitoring two key indicators – global growth (in particular US) and whether wage increases and wage-related price pressures were continuing to strengthen.

Ueda – somewhat controversially – flagged alongside ongoing downside risk in the US, upside risk to inflation from future data and "policy conduct". It was unclear whether this "policy conduct" was a reference to Trump, the Fed, or the Fed under Trump shocks.

On the wage front Ueda emphasized the signs are currently positive, with a labor market that is tight both structurally and cyclically, and the Rengo union confederation making an opening demand of 5 per cent.

The unspoken risk however is the one we have emphasized – that Trump trade war uncertainty could lead the big exporters to pull back from a strong wage round, in which case weaker SMEs would follow suit, weakening the domestic inflation dynamic.

The BoJ ought to have better visibility on this by January, even though the actual outcome will not be clear until March/April.

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