

30 October 2026

BOJ gains room from Takaichi as it judges inflation at target

Key takeaways

- The Bank of Japan (BOJ) left short-term rates unchanged at its policy board meeting but indicated that underlying inflation is at its 2% target.
- While Governor Ueda Kazuo was careful not to declare the inflation target achieved, the bank is wary of higher inflation and will work to limit the risk of overshooting its target, continuing the gradual normalization of rates.
- The Takaichi government's need to demonstrate its responsibility to markets gives the bank more room to normalize, though the result is an awkward mix of fiscal expansion and slowing monetary expansion – and possible friction down the road as the bank approaches its terminal rate.

At its policy board meeting on 29-30 October, the Bank of Japan (BOJ) announced that it would leave its policy rate unchanged at 1.25% – with one hawkish dissent from board member Takata Hajime, who argued that monetary policy has entered a new phase justifying a faster move to a neutral rate – but stated in its quarterly Outlook for Economic Activity and Prices (*Tenbō*) that underlying inflation "is at a level that is generally consistent with the price stability target of 2 percent, and is expected to remain at around that level." Although the press covered this statement as an important milestone, the BOJ was careful to note that its work is not completed and stressed that anchoring inflation expectations at 2% will require careful monitoring and policy adjustments. But this meeting suggested that the BOJ has more space to maneuver in normalizing interest rates as the Takaichi government looks to reassure markets that it is not pursuing reflation and respects the bank's independence.

It was widely expected that the BOJ would hold after raising rates at its last meeting in September – reflecting BOJ Governor Ueda Kazuo's desire to assess the impact of rate hikes on the real economy before proceeding with additional rate hikes – and so the

significance of Friday's meeting was less in the policy decision than in the BOJ's signaling that it views underlying inflation as having reached the bank's target (Ueda emphasized that all members of the board agreed) and that it sees upward pressure on prices in the near term from higher energy costs, yen weakness, and the spillover effects of AI-related demand. The bank does not appear ready to hike at a significantly more aggressive pace; Ueda warned that long-term inflation expectations are weakly anchored at 2%, suggesting that the bank will continue to adapt its policies in response to changing conditions to keep inflation around the 2% target.

On the whole, the BOJ appears to have fended off the threat of political interference from the Takaichi government in the normalization of monetary policy. Even if Prime Minister Takaichi Sanae would prefer a more deliberate pace of normalization – and the government has suggested that it is in no rush to declare that deflation is officially over, based on remarks by Economic Revitalization Minister Kiuchi Minoru Friday – the prime minister's efforts to reassure the United States and investors that she is not pursuing "reflationary" policies despite plans to expand government spending mean that the BOJ likely has more room to maneuver in the near term. This tentative truce is presumably conditional on the bank continuing to move at a cautious pace, and there could be more friction as the bank faces a decision on its terminal rate for normalization. But Ueda appears content to focus on the narrower challenge of keeping inflation from overshooting the 2% target and to leave broader questions of macroeconomic strategy to the government; when asked whether it would be appropriate to declare deflation defeated or to revise the 2013 accord between the government and BOJ, the governor said that judging whether deflation has been overcome is a matter for the government to decide and declined to comment on the accord. In the meantime, Ueda appears committed to unwinding the policy legacy of the Kuroda years, as suggested by Friday's announcement that the bank will significantly increase the pace of selling off its ETF holdings, raising it to JPY 860bn annually from JPY 330bn, decreasing the time it will take to sell off its holdings from 112 years to 43 years. (This accelerated pace of sales, which will begin in January 2027, could help the Takaichi government; Finance Minister Katayama Satsuki was quick to note that the resulting increase in the BOJ's payments to the national treasury would be non-tax revenue that the government would consider using in the budgetary process.)

The upshot is an awkward macroeconomic policy mix, with the Takaichi government stepping on the fiscal accelerator – despite its protestations that it is not pursuing reflationary policies – even as the BOJ moves ever so gradually towards the monetary brakes. The question, as yet unanswered by the government, is just how firmly Takaichi will step on the accelerator, which will in turn influence the exchange-rate and interest-rate environment Ueda will have to navigate. While the fiscal question will loom large in 2027, for the moment the bank likely has space to hike again in December.

Tobias Harris
Founder and Principal
Japan Foresight LLC
tobias@japanforesight.com
+1.847.738.4048

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