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Bank of Japan

Japan's Economy and Monetary Policy

Speech at a Meeting with Business Leaders in Nagoya

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(English translation based on the Japanese original)

Introduction

It is my great pleasure to have the opportunity today to exchange views with a distinguished gathering of business leaders in the Tokai region. I would like to take this chance to express my sincerest gratitude for your cooperation with the various activities of the Bank of Japan's Nagoya Branch.

As the Tokai region is one of Japan's largest exporting bases, we at the Bank, myself included, listen with great interest to the report from the General Manager of the Nagoya Branch at the meeting of general managers of the Bank's branches held quarterly. I am glad to be able to hear your views directly today. Before hearing from you, I would like to talk about developments in economic activity and prices at home and abroad and explain the Bank's thinking on the conduct of monetary policy.

I. Economic Activity and Prices

A. Overseas Economies

I would like to begin by talking about developments abroad. Overseas economies have grown moderately on the whole, although some weakness has been seen in part, reflecting trade and other policies in each jurisdiction.

Please take a look at Chart 1. In its *World Economic Outlook* (WEO), the International Monetary Fund (IMF) revised its projection for the global economy for 2025 downward to 2.8 percent in April this year, taking into account the impact of U.S. tariff policies. Thereafter, however, the IMF continued to make upward revisions, projecting in its latest October WEO that the global economy will maintain growth above 3 percent in both 2025 and 2026. As described, the impact of tariff policies, which for a while was considered to be a factor that would significantly push down the global economy, has so far not materialized to a considerable degree. This can be attributed to three main developments. First, since last summer, many countries and regions have reached agreements in trade negotiations with the United States, and this has led to reduced uncertainty over the outlook. Second, in the United States, the pass-through of tariff costs to selling prices has remained only moderate, and private consumption there has not been pushed down as much as initially feared. I will elaborate on this point later. Third, factors such as greater investment in digital areas

worldwide, mainly in AI-related areas, as well as a rise in demand for replacing smartphones and personal computers, whose sales surged during the COVID-19 pandemic, have been supporting trade and production activity in many countries and regions.

Looking ahead, there is no change to the Bank's view that overseas economies will slow down temporarily under the impact of tariff policies. Thereafter, they are expected to return to a moderate growth path. Developments in the United States, which leads the global economy, will be key to whether or not this outlook is realized.

Please take a look at Chart 2. Looking at business fixed investment in the United States in the left panel, investment by major high-tech firms has recently increased significantly, against the background of expansion in AI-related demand. Please refer to the middle panel. As I mentioned earlier, the pace at which the burden arising from tariff impositions is passed on to consumers in the form of higher prices has remained only moderate so far. Coupled with the wealth effects stemming from the recent high stock prices, private consumption in the United States has been solid. That said, this implies that the corporate sector in the United States has been bearing a considerable portion of the cost burden of tariffs, instead of passing it on to consumers. On this point, the right panel shows that the pace of increase in the number of employees has decelerated recently. While the background to this is complex, including the impact of strict U.S. immigration policies, attention is warranted on the effects on labor market developments of lower corporate profits due to tariff policies.

There are other factors to consider with regard to the U.S. economy, such as the future course of AI-related demand and developments in the private credit market. That said, in light of the developments to date, it appears that downside risks to the economy overall have decreased. The end of the federal government shutdown in mid-November will also lead to reduced uncertainty.

B. Economic Activity and Prices in Japan

Current Situation of and Outlook for Economic Activity

Next, I would like to discuss the current situation of and outlook for economic activity in Japan. The Bank assesses that Japan's economy has recovered moderately, although some weakness has been seen in part. Please take a look at Chart 3. Recently released GDP statistics show that real GDP for the July-September quarter of 2025 recorded negative growth for the first time in six quarters. However, this largely reflects the impact of a reactionary decline following the front-loading of exports seen since early spring due to the increase in tariffs, and it is expected that the negative growth will be only temporary. To exclude such fluctuations, when comparing real GDP in the April-September period this year with the preceding October-March period, the annualized growth rate is 0.9 percent -- above the potential growth rate, which is estimated to be around 0.5 percent. Given this, the Bank views that its basic assessment that Japan's economy has recovered moderately remains unchanged.

Please turn to Chart 4, which shows developments in exports. Automobile-related exports have seen large fluctuations since early spring this year, reflecting factors such as the front-loading and subsequent reactionary decline. That said, exports overall have continued to be more or less flat at high levels, as exports of IT-related goods have been on an uptrend, mainly on the back of solid global AI-related demand. Please take a look at Chart 5. As shown in the upper left-hand panel, corporate profits have remained at high levels on the whole, although downward effects due to tariffs have been seen in some manufacturing industries. The lower left-hand panel shows the financial results of firms listed on the Tokyo Stock Exchange Prime Market. As can be seen, profit projections for fiscal 2025 show a decline for manufacturing firms and an increase for nonmanufacturing firms. Compared with previous projections, however, the projections have been revised upward slightly, including for manufacturing firms, reflecting factors such as reduced uncertainty surrounding tariff policies. In this situation, business fixed investment, shown in the right-hand panel, has been on a moderate increasing trend. Looking at business fixed investment plans for fiscal 2025, firms have maintained an active investment stance, centered on research and development (R&D) in growth areas and on labor saving-related software.

Next, turning to the household sector, please take a look at Chart 6. Looking at developments in private consumption in the left panel, consumption of nondurable goods has continued on a decreasing trend, reflecting consumers' increased thriftiness due to a rise in food prices and other factors. Overall consumption has been resilient, against the background of an improvement in the employment and income situation and the recent pick-up in consumer sentiment on the back of factors such as an increase in summer bonuses and a rise in stock prices. That said, the burden of price increases on households remains high, and due attention to the impact of price increases is therefore warranted.

Regarding the outlook for Japan's economy, it is expected that the negative growth seen in the July-September quarter will be only temporary, as mentioned earlier, and that the economy will return to positive growth. For the time being, Japan's economic growth is likely to be modest, as trade and other policies in each jurisdiction lead to a slowdown in overseas economies. Thereafter, however, Japan's economic growth rate is likely to rise, with overseas economies returning to a moderate growth path.

In terms of risks to this baseline scenario, the Bank's *Outlook for Economic Activity and Prices* (Outlook Report) released at the end of October pointed to various factors, such as developments in overseas economic activity and prices and fluctuations in import prices. That said, regarding tariff policies, which had been the most significant concern over the past few months, the adverse effects in the United States have not materialized to a considerable degree, as mentioned earlier. Moreover, with regard to Japan's economy, there is a growing view that the impact of tariff policies on corporate profits will be limited. Considering these factors among others, it appears that the uncertainty surrounding the outlook for Japan's economy is gradually diminishing.

Current Situation of and Outlook for Prices

Next, I would like to turn to developments in prices. As shown in the left panel of Chart 7, the latest figure for the year-on-year rate of increase in the consumer price index (CPI) for all items excluding fresh food is around 3 percent. Looking at the breakdown, prices of rice and other food products, shown in the blue and light blue bars, have continued to make significant positive contributions. This is likely to be largely attributable to temporary

cost-push factors. Meanwhile, amid moderate recovery in the economy and tighter labor market conditions, the pass-through of wage increases to selling prices has continued, and prices of not only food products but also goods and services have risen moderately. On this point, looking at the distribution of price changes by item in the right panel, the latest distribution in October has been relatively fat on the right tail, reflecting the large number of items, particularly food products, that continue to see price increases at rates of 5 percent or more. That said, compared to the distribution in 2023, when there was a significant impact from higher import prices, the balance between items has clearly improved. As a result, the distribution is beginning to resemble the situation seen in the first half of the 1990s, when Japan's economy experienced an average annual inflation rate of around 2 percent before falling into deflation.

Looking ahead, the year-on-year rate of increase in the CPI for all items excluding fresh food is likely to decelerate temporarily to a level below 2 percent through the first half of fiscal 2026, with the waning of the effects of the rise in food prices, and partly due to the effects of government measures to address rising prices, such as abolishing the former provisional gasoline tax rate. Thereafter, since it is projected that a sense of labor shortage will grow as the economic growth rate rises and that medium- to long-term inflation expectations will rise, it is expected that underlying CPI inflation -- that is, inflation excluding the effects of temporary factors -- and actual inflation will increase and, in the second half of the projection period of the Outlook Report, will be at a level that is generally consistent with the price stability target of 2 percent.

There are various uncertainties surrounding the outlook. Although food price developments are expected to gradually stabilize as mentioned earlier, if new temporary factors pushing up prices arise or if the pass-through of increased personnel expenses and distribution costs to selling prices strengthens, the rise in food prices could persist for longer than expected. Since consumers purchase food items on a frequent basis, if the price rises persist, the CPI could be pushed up through changes in inflation expectations. On the other hand, it is also possible that the CPI could be pushed down, as private consumption could decline through a deterioration in household sentiment. At this juncture, these developments do not appear to be gaining strength, but the Bank will continue to carefully examine various data.

Developments in import prices, including fluctuations in foreign exchange rates, as well as the extent to which such developments will spread to domestic prices may lead prices to deviate either upward or downward from the outlook. In this regard, it is necessary to pay attention to the fact that, with firms' behavior shifting more toward raising wages and prices recently, exchange rate developments are, compared to the past, more likely to affect prices. Attention is also warranted on the possibility that these price developments could affect underlying inflation through changes in inflation expectations.

II. The Bank's Conduct of Monetary Policy

Next, I will talk about the Bank's conduct of monetary policy. If the outlook for economic activity and prices outlined so far is realized, the Bank, in accordance with improvement in economic activity and prices, will continue to raise the policy interest rate and adjust the degree of monetary accommodation. As a premise for this policy stance, looking at Chart 8, the Bank recognizes that real interest rates -- that is, the nominal policy interest rate minus the inflation rate -- are at significantly low levels, considerably below the real interest rate that is neutral to economic activity and prices, which is often referred to as the natural rate of interest in economic terms. In other words, even if the policy interest rate is raised, accommodative financial conditions will be maintained. To use an analogy, raising the policy interest rate under accommodative financial conditions is about a process of easing off the accelerator as appropriate toward achieving stable economic growth and price developments, not about applying the brakes on economic activity.

With this in mind, given factors such as the recent decline in uncertainties surrounding the U.S. economy and tariff policies, the Bank considers that the likelihood of the baseline scenario for economic activity and prices being realized is gradually increasing. The Bank is at the stage where it should examine whether firms' active wage-setting behavior will continue. In particular, it will be important to confirm the momentum of initial moves toward next year's annual spring labor-management wage negotiations. Please take a look at Chart 9. First, looking at the conditions that underlie such moves, the diffusion index (DI) for employment conditions in the *Tankan* (Short-Term Economic Survey of Enterprises in Japan) in the left panel shows that labor shortages have remained acute on the whole, as seen, for example, in nonmanufacturing industries having seen a net "insufficient" of around

the same level as what was observed during the bubble period. The fact that the minimum wage for fiscal 2025 rose by more than 5 percent year on year -- the highest rate on record -- is also highly likely to encourage wage hikes among a wider range of firms.

Meanwhile, corporate profits, which are the source of wage hikes, are expected to remain at high levels on the whole, even after taking into account the impact of tariff policies, as I mentioned earlier. Against this backdrop, the Japanese Trade Union Confederation (Rengo) announced last week its basic policy for next year's annual spring labor-management wage negotiations, setting the target wage increase rate at 5 percent or more, which is the same as in the previous year. On the management side, the Japan Business Federation (Keidanren), for example, has expressed its firm stance toward promoting the further anchoring of wage increases. Moreover, in a survey conducted by the Japan Association of Corporate Executives (Keizai Doyukai) for September, many respondents stated that they planned to raise wages in 2026 by a rate nearly equivalent to or greater than in 2025. At a joint meeting between representatives of the government, labor, and management held last week, the government stated that it would strive to develop an environment for wage increases, including among small and medium-sized firms. In view of the next Monetary Policy Meeting (MPM) to be held on December 18 and 19, the Bank is actively collecting information regarding firms' stance toward raising wages through its Head Office and branches. At the MPM, the Bank will examine and discuss economic activity and prices at home and abroad as well as developments in financial and capital markets, including the point I just mentioned, based on various data and information, and will consider the pros and cons of raising the policy interest rate and make decisions as appropriate.

Looking back, the aggressive macroeconomic policies adopted by the government and the Bank over the past decade have had a strong stimulative effect on Japan's economy. As a result, the mechanism in which both wages and prices rise moderately has been restored. This is the context in which the Bank has been gradually adjusting the degree of monetary accommodation to achieve the price stability target of 2 percent in a sustainable and stable manner. Adjusting the degree of accommodation appropriately -- without being too late or too early -- will be necessary to smoothly achieve the price stability target while ensuring stability in financial and capital markets, and to guide Japan's economy onto a long-term

growth path, which will ultimately lead to the success of the efforts undertaken by the government and the Bank thus far.

Concluding Remarks

Before concluding my speech, I would like to touch on initiatives taken in the Tokai region.

First off, I would like to reiterate that generating and effectively leveraging innovation is crucial for an economy to achieve sustainable growth. Many firms in the Tokai region are strategically investing in R&D and other areas while also moving ahead with reforms to their business portfolios. There is also growing momentum to, for example, support startups with the potential to adopt new business models and cutting-edge technologies. Recently, an increasing number of firms are also actively turning to open innovation in an effort to capitalize on the knowledge of many people.

These moves are emerging not only in the automobile industry, which is said to be undergoing a once-in-a-century transformation, but in other manufacturing and non-manufacturing industries as well, which I find highly encouraging. People in the region have accurately gauged the needs of society, generated a great deal of innovation, and overcome numerous adversities. I have high hopes that such efforts, in a region that is deeply imbued with an entrepreneurial spirit, will continue to drive sustainable growth in the regional economy and, ultimately, in Japan's economy as a whole. The Bank will support these efforts by striving to ensure price stability and financial system stability so that firms here can realize their full potential.

I would like to close today by expressing my hope that the efforts of the Tokai region will bear fruit, and that its economy will continue to develop. Thank you very much for your attention.

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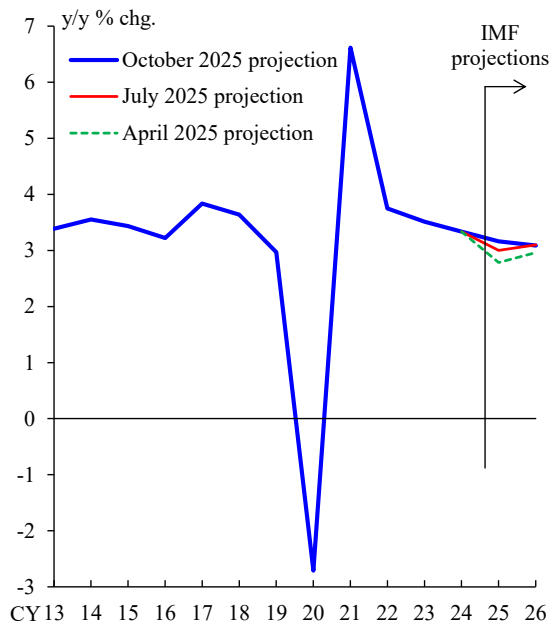
Introduction

I. Economic Activity and Prices

II. The Bank's Conduct of Monetary Policy

Concluding Remarks

Overseas Economies

Global Growth Rate
(IMF Projections)Major Economies' Growth Rates
(IMF Projections)

	CY 2024 [Actual]	CY 2025 [Projections at each point]				CY 2026 [Projections]
		Jan.	Apr.	July	Oct.	
World	3.3	3.3	2.8	3.0	3.2	3.1
United States	2.8	2.7	1.8	1.9	2.0	2.1
Euro area	0.9	1.0	0.8	1.0	1.2	1.1
China	5.0	4.6	4.0	4.8	4.8	4.2

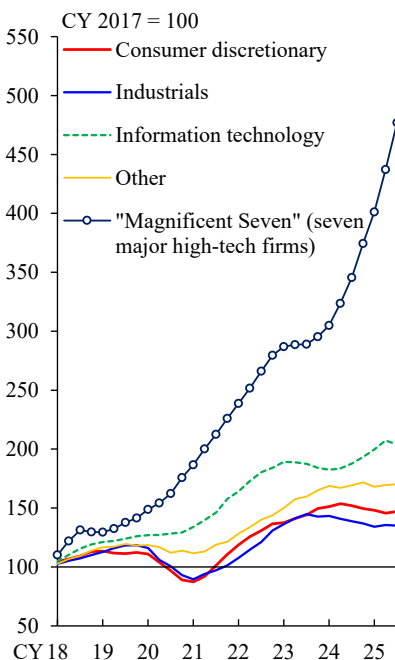
y/y % chg.

Source: IMF.

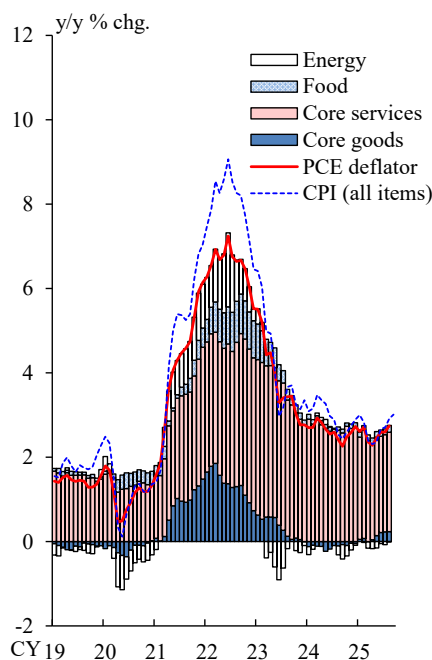
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U.S. Economy

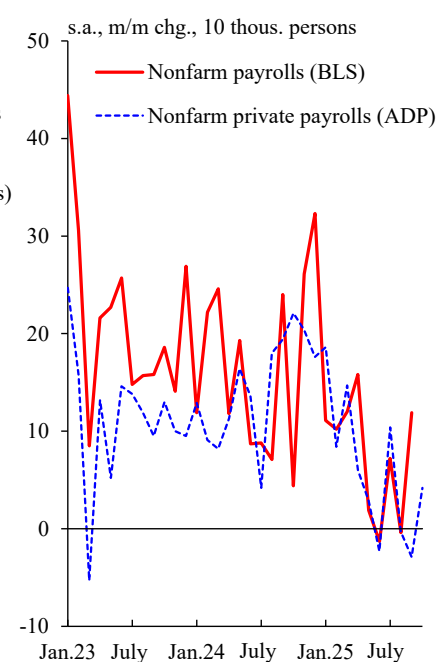
Business Fixed Investment



Consumer Prices



Number of Employees

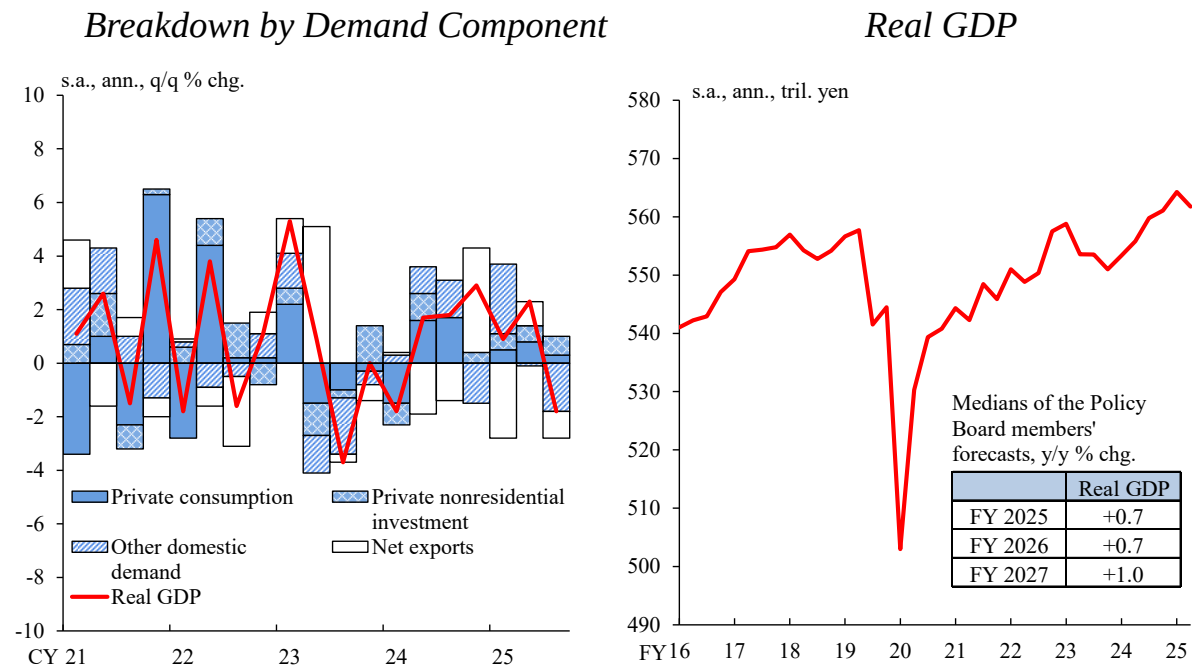


Note: In the left-hand chart, figures are accounting information for firms included in the Russell 3000 at each point. Business fixed investment is the sum of capital spending and R&D expenses. Figures show one-year backward moving averages.

Sources: Haver; Copyright © 2025 by S&P Global Market Intelligence, a division of S&P Global Inc. All rights reserved.

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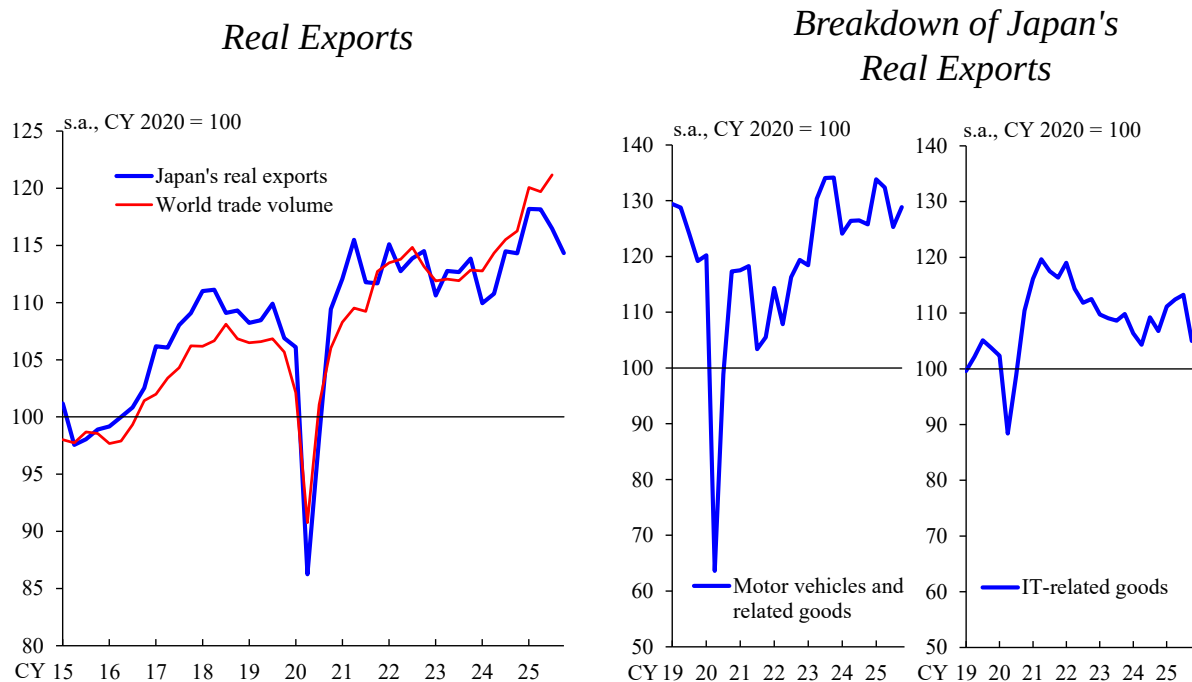
Real GDP in Japan



Sources: Cabinet Office; Bank of Japan.

3

Corporate Sector (1): Exports

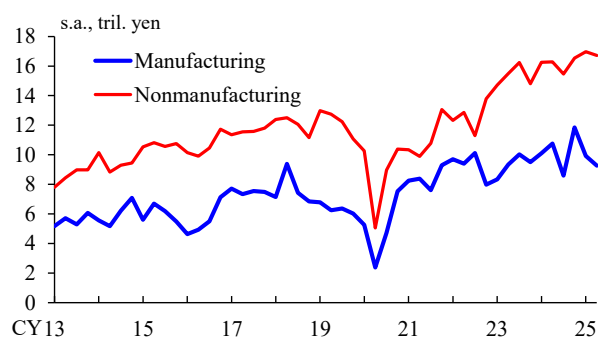


Note: Figures for Japan's real exports for 2025/Q4 are for October. In the left-hand chart, figures for the world trade volume are for real imports.
 Sources: Ministry of Finance; Bank of Japan; CPB Netherlands Bureau for Economic Policy Analysis.

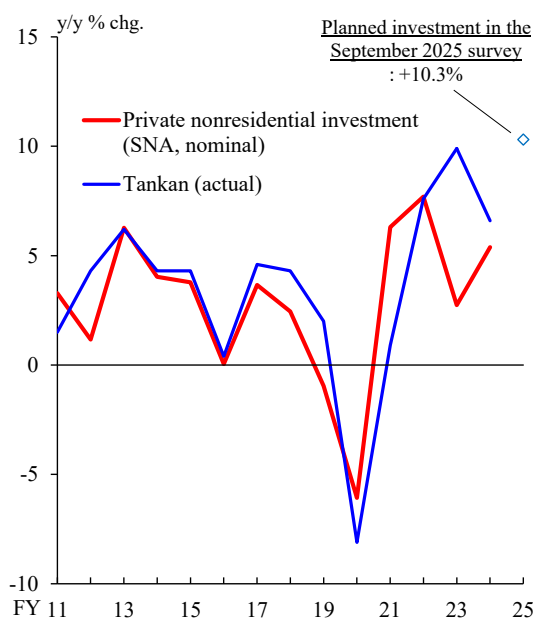
4

Corporate Sector (2): Profits and Fixed Investment

Corporate Profits



Business Fixed Investment



First-Half Financial Results and Full-Year Projections of Listed Firms

	FY25 first-half results	FY25 full-year projections	Revision rate
All industries	-1.7	-2.4	2.7
Manufacturing	-9.4	-5.6	2.1
Nonmanufacturing	10.2	2.6	3.4

Notes: 1. Figures in the upper left-hand chart are current profits based on the *Financial Statements Statistics of Corporations by Industry, Quarterly*, excluding "finance and insurance" and "pure holding companies."

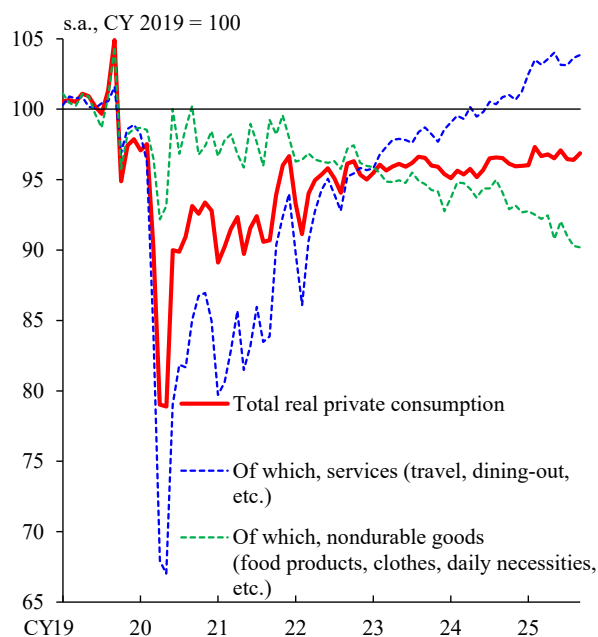
2. Figures in the lower left-hand table are operating profits based on firms' financial results, excluding the finance and insurance industries. The figures are calculated from available data for firms listed on the Tokyo Stock Exchange Prime Market with fiscal years ending in March. Revision rates are changes from previous projections.

3. Figures for *Tankan* (actual) in the right-hand chart include software and R&D investments and exclude land purchasing expenses. R&D investment is not included before the March 2017 survey. The figures are for all industries including financial institutions.

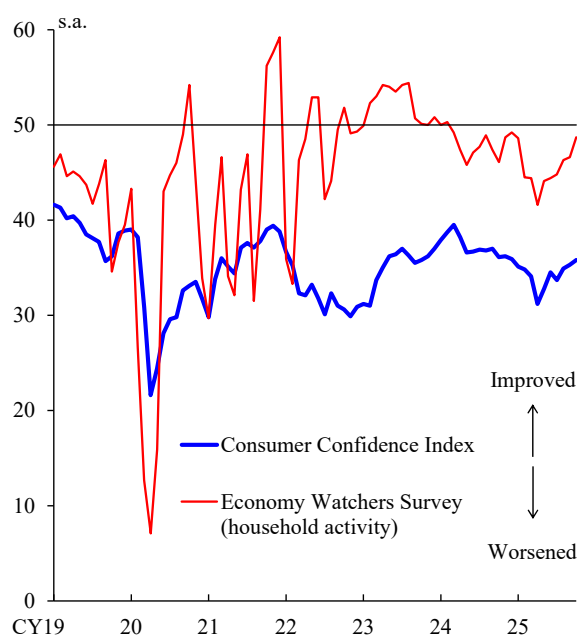
Sources: Ministry of Finance; Bank of Japan; Cabinet Office; LSEG Workspace; QUICK.

Household Sector

Private Consumption



Consumer Sentiment

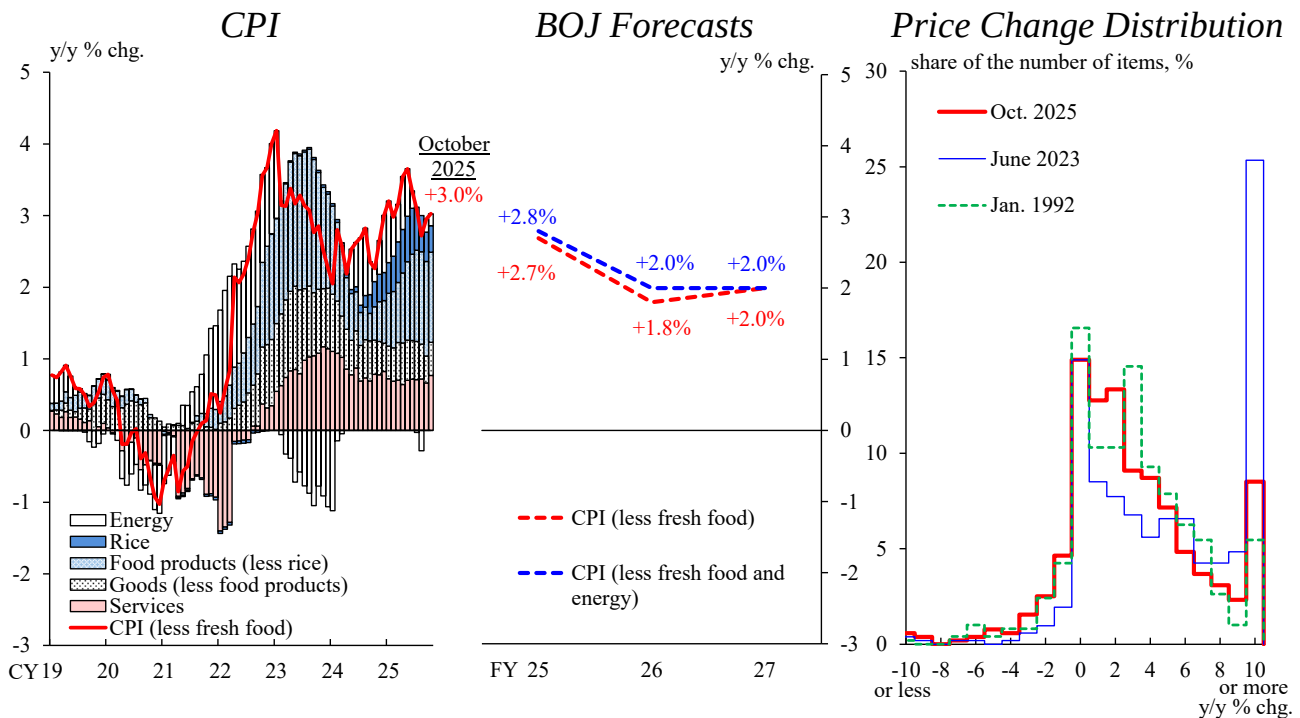


Notes: 1. In the left-hand chart, figures for total real private consumption are the real Consumption Activity Index (travel balance adjusted) based on staff calculations, which exclude inbound tourism consumption and include outbound tourism consumption.

2. In the right-hand chart, figures for the *Economy Watchers Survey* are those for the current economic conditions DI.

Sources: Bank of Japan; Cabinet Office.

Developments in Consumer Prices



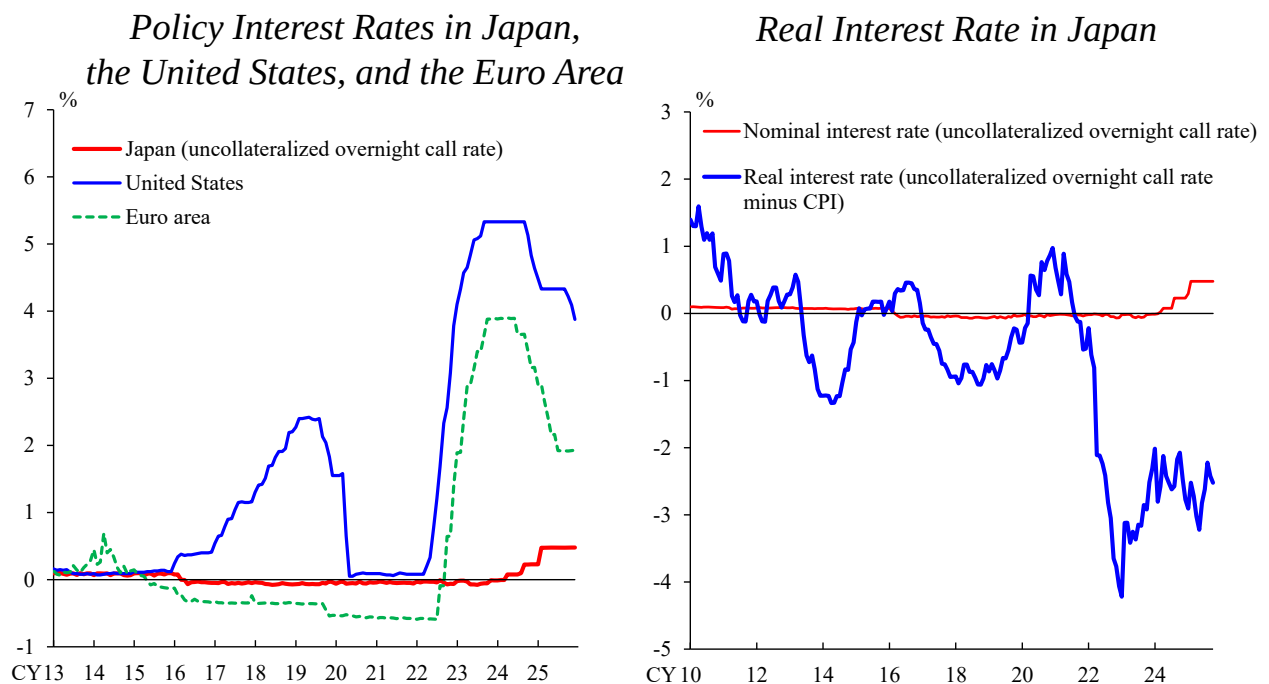
Notes: 1. In the middle chart, figures are the medians of the Policy Board members' forecasts in the October 2025 Outlook Report.

2. In the right-hand chart, items subject to aggregation are those adopted in each base year. Figures indicate the CPI for all items excluding fresh food and energy. Figures are staff estimates and exclude the effects of policies concerning the provision of free education and the effects of travel subsidy programs.

Sources: Ministry of Internal Affairs and Communications; Bank of Japan.

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Policy Interest Rates



Notes: 1. In the left-hand chart, figures for the United States are the effective federal funds rate. Figures for the euro area are the Euro Overnight Index Average (EONIA) prior to October 2019 and the euro short-term rate (ESTR) thereafter.

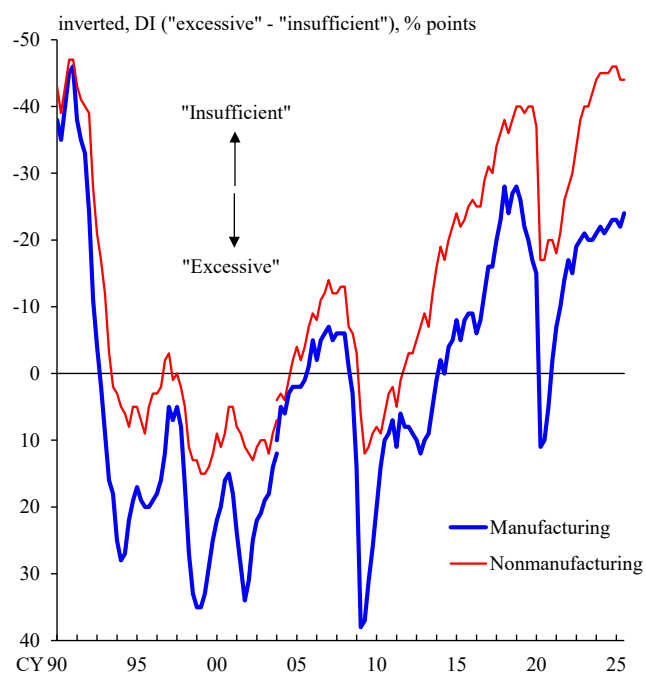
2. In the right-hand chart, CPI indicates the year-on-year rate of increase in the CPI for all items excluding fresh food. Figures for the CPI exclude the effects of consumption tax hikes.

Sources: Bank of Japan; Ministry of Internal Affairs and Communications; Bloomberg.

8

Environment and Developments Surrounding Wages

Employment Conditions DI



Annual Spring Labor-Management Wage Negotiation Stance

Figures in parentheses indicate base pay increase rates

	Rengo Wage increase target	Keidanren Positioning of wage increase	Actual wage increase
CY 2023	Around 5% (Around 3%)	Starting point	3.58% (2.12%)
CY 2024	5% or more (3% or more)	Acceleration	5.10% (3.56%)
CY 2025	5% or more (3% or more)	Anchoring	5.25% (3.70%)
CY 2026	5% or more (3% or more)	Further anchoring	—

Notes: 1. In the left-hand chart, figures are based on the *Tankan*. There is a discontinuity in the data for December 2003 due to a change in the survey framework.

2. In the right-hand table, figures for actual wage increases are aggregate figures released by Rengo.

Sources: Bank of Japan; Japanese Trade Union Confederation (Rengo); Japan Business Federation (Keidanren).