Can the 2% Price Stability Target Be Achieved by Japan?

There has been no slowing in the rise of prices. Looking at the trends in the Consumer Price Index (all items less fresh food), in the most recent April statistics, the CPI recorded a year-on-year increase rate of 3.5%, greatly surpassing the price stability target (2%), and price increases have remained above 2% for 37 consecutive months (see Figure 1). The April figures included a 98.6% year-on-year increase in the price of non-glutinous rice. The rise in food prices less fresh food is pushing up prices overall.

In simple terms, it would not be out of line to conclude that the price stability target has been achieved, but in its *Outlook for Economic Activity and Prices* (Outlook Report) released on May 1, the Bank of Japan (BOJ) conversely revised its forecast regarding prices downwards. The year-on-year increase rate in the CPI (all items less fresh food; the median forecast of the Policy Board members) is forecast to be 2.2% in fiscal 2025 (revised downward by 0.2 percentage points from January), 1.7% in fiscal 2026 (revised downward 0.3 percentage points), and 1.9% in fiscal 2027, which was forecast for the first time. The outlook is that a level generally consistent with the target will finally be achieved from the second half of fiscal 2026. The flip side of that means that the target might not be achieved until the first half of fiscal 2026. The basis for concluding that the target has not been reached at present is that the rises in import prices and food prices which have been pushing up consumer prices are expected to settle down from now, and that viewpoint is also supported by how the indices calculated by the BOJ showing the underlying price movements (trimmed mean, weighted median, and mode) are presently holding at below 2% (see Figure 1).

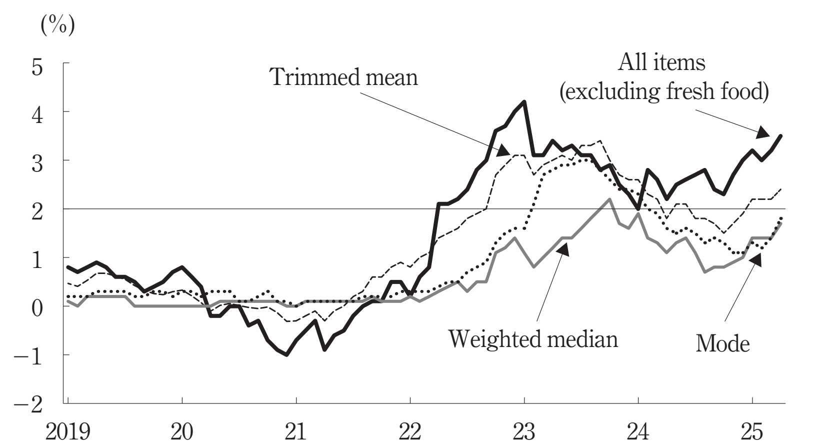
Looking at the *ESP Forecast Survey* compiled by the Japan Center for Economic Research (the outlooks of 37 leading economists), the average viewpoint is that the growth rate of the CPI (all items less fresh food) began to decelerate after peaking in the January–March quarter of this year (up 3.1% year-on-year), and will drop below 2% in the January–March quarter of next year. By fiscal year, the ESP forecast projects 2.26% for fiscal 2025 and 1.68% for fiscal 2026, showing no great difference from the BOJ outlook. The difference with the BOJ is that the leading economists expect the growth rate to remain flat at around 1.7% even in the second half of fiscal 2026, and do not anticipate prices to rise again toward 2% nor the price stability target to be achieved.

On the other hand, these projections greatly differ from the opinions about prices among the general public. Looking at the expectations for the inflation rate in one year in the March survey of the most recent *Opinion Survey on the General Public's Views and Behavior*, which is conducted quarterly by the BOJ, it becomes clear that consumers are expecting an inflation rate of 10% or more in one year with an average projection of 12.2% and a median projection of 10.0% (see Figure 2). What is noteworthy is that the rate had already reached 10% in the December 2022 survey when a CPI increase rate of more than 2% was becoming established, and has generally remained at 10% ever since. Of course, you need to discount the facts that the data tends to be high as it exceeded 2% in 2019–2020 when the actual inflation rate was between 0% and 1% and the experience of price rises in goods close at hand has a great impact. Regardless, consumers' viewpoint on prices greatly exceeds the price stability target.

Then, how should we look at prices going forward? First, we have to pay attention to domestic factors such as the extent to which wage hikes are being passed on to price increases as well as the price trends of rice and other foods. The future of the closely watched Trump tariffs is difficult to predict, but it is natural to assume that tariffs will remain in one form or another. From this standpoint, outlining the impact of the Trump tariffs divided into the short term and the middle to long term, over the short term, there is a high likelihood of stagnant demand on a global level from the increase in tariffs. As a result, there will be a negative impact on the Japanese economy, which is highly dependent on trade, and pressures pushing down prices are expected to intensify. On the other hand, over the middle to long term, to one extent or another, the division of the global economy into blocs will be unavoidable. This will result in an unraveling of the efficient division of labor and restrictions on the supply of various goods, which will intensify the pressure toward higher prices.

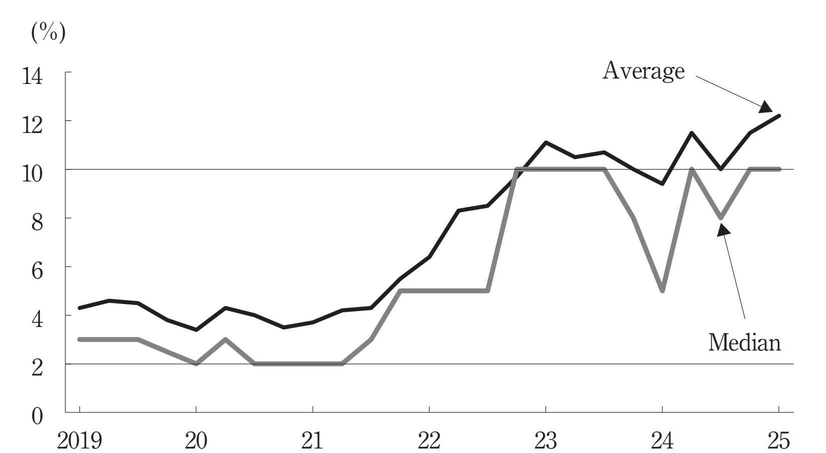
The absolute level of Japanese interest rates is low, and up until now it was understood that the BOJ's next move would be to raise interest rates. However, if the likelihood of realizing the BOJ's scenario whereby price rises are to taper off once but then resume toward 2% from the second half of fiscal 2026 decreases, the hurdle to an interest rate hike will become higher. Conversely, if skyrocketing prices do not ease and continue in line with consumers' price outlook, it will become necessary to quickly raise interest rates to curb inflation. It is likely to remain difficult to discern which viewpoint is correct because numerous variables are intertwined.

Figure 1: Transition of the Consumer Price Index



Note: The trimmed mean is the average after removing 10% of the increase rate figures on both ends. The weighted median is the price change rate of items at the center of the price change distribution by item.
Source: Ministry of Internal Affairs and Communications, Bank of Japan

Figure 2: Consumer Viewpoint on the Inflation Rate in One Year



Source: *Opinion Survey on the General Public's Views and Behavior* by Bank of Japan