

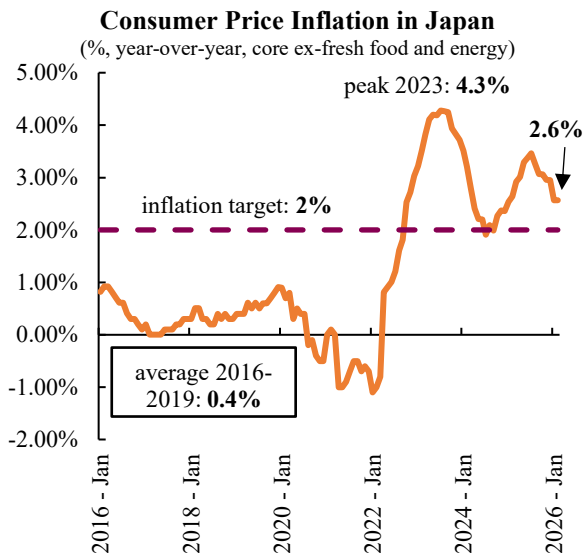
Bank of Japan strengthens its case for further policy rate hikes

After decades of deflationary pressures and exceptionally low interest rates, the Bank of Japan (BoJ) is entering a new policy cycle. Having raised its policy rate to 0.75% in December 2025, the central bank is arriving at a policy environment it has not seen in close to three decades. The transition reflects a structural transformation of Japan’s macroeconomic landscape: from entrenched deflation and negative interest rates to a regime where growth, wages, and prices are normalising.

The BoJ has noted that underlying price dynamics remain on an upward trajectory. Furthermore, the Japanese yen has weakened past the 160 per dollar level for the first time since mid-2024, amplifying the cost of energy and other imports in domestic currency terms. Higher prices of imported inputs translate into consumer prices, as firms pass on higher input cost to their goods. Core measures of prices, which exclude items such as energy and fresh foods, show inflation remains significantly above the 2% target of monetary policy.

In this article, we discuss the key factors underpinning the BoJ’s tightening path.

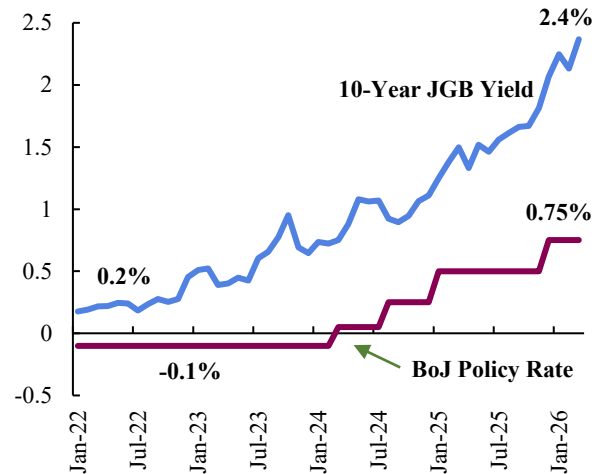
third consecutive year of increases above 5%. Rengo, Japan’s largest union federation, reported average wage demands of close to 6% from over 2,500 member unions, confirming that proactive wage-setting behaviour has become entrenched across the corporate sector. This wage momentum is gradually feeding into services inflation, the component most reflective of domestic demand conditions. In this context, there is increasing confidence that the wage-price mechanism is supporting the case for further policy normalisation.



Source: Haver Analytics, QNB Economics

First, the shift in Japan’s wage-price dynamics calls for additional policy rate increases. The 2026 “Shunto” spring wage negotiations have delivered another round of robust results, with overall wage hikes settling in the range of 5% to 7%, marking the

Japan Policy Rate and Government Yields
 (% monthly, end-of-period)



Source: Bank of Japan, Haver Analytics, QNB Economics

Second, the BoJ’s estimation of the neutral interest rate provides policy space for further gradual tightening. The neutral rate of interest is the level that neither restrains nor stimulates the economy, an interest rate below this level provides stimulus to the economy. The BoJ recently released an updated estimate of Japan’s neutral rate, which in nominal terms places it in a range of 1.1% to 2.5%, reflecting a recovery in Japan’s potential growth rate. At a current policy rate of 0.75%, even a further 25 basis point (b.p.) hike to 1.0% would position the BoJ at the lower bound of the estimated neutral range, meaning that monetary policy would remain slightly accommodative. Thus, the neutral rate framework reinforces the view that the BoJ has room to continue raising rates without exerting a contractionary effect on economic activity.

Third, the geopolitical environment and an energy shock are adding further pressure for the BoJ to continue tightening. The ongoing conflict in the Middle East, which escalated sharply in late February 2026, has triggered a massive energy price shock. Brent crude surged from approximately USD 72 per barrel before the conflict to above USD 110 in late March, a rise of over 50% in a single month. For Japan, which imports nearly all of its oil and sources roughly 90% of it from the Middle East, the implications are directly inflationary. Rising crude prices transmit through fuel, freight, and broader consumer prices, creating an inflationary impulse that reinforces the case for tighter policy. The BoJ's March Summary of Opinions reflected this, with some board members suggesting that rate hikes may

be warranted if energy-driven inflation persists. In this context, the energy shock is strengthening the case for the BoJ to continue normalising monetary policy.

All in all, the BoJ is strengthening its case for policy rate normalization and further rate hikes. The consolidation of a wage-price mechanism, a neutral rate framework that confirms room for further tightening, and geopolitical developments that amplify inflationary pressures all point towards continued policy normalisation. Market expectations broadly signal a rate hike to 1.0% by mid-2026, with the terminal rate likely settling in a range of 1.25% to 1.5% depending on the evolution of wages, energy prices, and the yen.

QNB Economics Team:**[Bernabe Lopez-Martin*](#)**Assistant Vice President - Economics
+974-4453-4643**[Aisha Khalid Al-Thani](#)**Senior Associate - Economics
+974-4453-4647

* Corresponding author

DISCLAIMER: *The information in this publication (“Information”) has been prepared by Qatar National Bank (Q.P.S.C.) (“QNB”) which term includes its branches and affiliated companies. The Information is believed to be, and has been obtained from, sources deemed to be reliable; however, QNB makes no guarantee, representation or warranty of any kind, express or implied, as to the Information’s accuracy, completeness or reliability and shall not be held responsible in any way (including in respect of negligence) for any errors in, or omissions from, the Information. QNB expressly disclaims all warranties or merchantability or fitness for a particular purpose with respect to the Information. Any hyperlinks to third party websites are provided for reader convenience only and QNB does not endorse the content of, is not responsible for, nor does it offer the reader any reliance with respect to the accuracy or security controls of these websites. QNB is not acting as a financial adviser, consultant or fiduciary with respect to the Information and is not providing investment, legal, tax or accounting advice. The Information presented is general in nature: it is not advice, an offer, promotion, solicitation or recommendation in respect of any information or products presented in this publication. This publication is provided solely on the basis that the recipient will make an independent evaluation of the Information at the recipient’s sole risk and responsibility. It may not be relied upon to make any investment decision. QNB recommends that the recipient obtains investment, legal, tax or accounting advice from independent professional advisors before making any investment decision. Any opinions expressed in this publication are the opinions of the author as at the date of publication. They do not necessarily reflect the opinions of QNB who reserves the right to amend any Information at any time without notice. QNB, its directors, officers, employees, representatives or agents do not assume any liability for any loss, injury, damages or expenses that may result from or be related in any way to the reliance by any person upon the Information. The publication is distributed on a complementary basis and may not be distributed, modified, published, re-posted, reused, sold, transmitted or reproduced in whole or in part without the permission of QNB. The Information has not, to the best of QNB’s knowledge, been reviewed by Qatar Central Bank, the Qatar Financial Markets Authority, nor any governmental, quasi-governmental, regulatory or advisory authority either in or outside Qatar and no approval has been either solicited or received by QNB in respect of the Information.*