

Japan Macro Watch

PM Ishiba resigns - First take and outlook

Select Subject

PM Ishiba steps down 1.5 months after the election

Prime Minister (PM) Shigeru Ishiba announced his resignation on 7 September. The ruling Liberal Democratic Party (LDP)-Komeito coalition's loss of its majority in the 20 July Upper House elections prompted an ongoing political debate about if Ishiba would stay or go. Ultimately, he announced his resignation ahead of the 8 September vote on an early LDP leadership election, which was effectively a no-confidence motion from within his own party.

LDP leadership vote to take place in end-Sep/early Oct

The ruling LDP will vote to elect a new leader now that Ishiba has indicated he will step down. The party has yet to announce the timing and method for the election, but the Nikkei indicates that a decision is likely within this week. The 5 September Yomiuri Shimbun reported on calls from within the LDP for the election to follow the normal procedure that allows party members to vote; this would likely mean it is held between end-September and early October (see [Q&A on LDP's leadership race](#), 23 July).

Little visibility on leadership vote

The candidates for new LDP leader are likely to put themselves forward in the coming days, but at this point there is no market consensus on who will run and who will could win. However, we think the market will base its outlook on the candidates who stood in September 2024 given that (1) they need to obtain recommendations from 20 Diet members and (2) less than a year has elapsed since the previous race (Exhibit 1). The most likely candidates for next LDP leader cited in August opinion polls indeed ran in 2024 (Exhibit 2). We note that Ishiba and former PM Fumio Kishida have explicitly ruled themselves out.

Focus on shifting internal LDP dynamics

The key points to watch will be individual member of parliament (MP)s' announcements of their candidacy and election pledges, and internal party dynamics including the support of a handful of powerful MPs. The weightings for MPs' and party members' votes in the first-round leadership ballot will differ depending on whether the LDP opts for the normal voting process, but in either case MPs' votes will have a very high weighting in the runoff election (Exhibit 3). Ultimately, the race will likely come down to where the party's now-disbanded major factions—which still retain considerable influence—put their support (Exhibit 4).

In the previous LDP leadership race, Sanae Takaichi, Yoshimasa Hayashi, and Toshimitsu Motegi received endorsements from numerous MPs in their (former) factions, while Shinjiro Koizumi and Takayuki Kobayashi drew endorsements from a broad range of factions including independents (among them the Suga group) (Exhibit 5).

(continued overleaf)

08 September 2025

Economics
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Fiscal policy implications

Among the candidates who ran in the previous LDP leadership race, Takaichi has indicated that she supports the consumption tax cuts advocated by major opposition parties, while Kobayashi has indicated that he may consider them. However, Hayashi and Koizumi (both members of the Ishiba cabinet) have indicated caution (Exhibit 6). The market is likely to focus on candidates' fiscal policy stances.

However, the key point is that unless the ruling coalition can quickly call a general election and regain its Lower House majority, it would continue to operate as a minority government in both houses whoever wins the LDP leadership election. We think the government is likely to adopt a more expansionary stance in the fiscal debates from the autumn given the need to secure the cooperation of one or more opposition parties, all of which are calling for procyclical fiscal policy (see [Ruling coalition loses Upper House majority - First take and outlook](#) 21 July 2025).

The choice of next LDP leader will also have a major impact on the relationship between the ruling and opposition parties. Some potential candidates are widely known to have close relationships with the opposition, and this could influence the outcome of the leadership race as the LDP looks ahead to likely fraught negotiations with opposition parties as a minority government. We would also note that to become PM, the next LDP president will need to secure a majority vote in the prime ministerial election to be held in the Diet immediately after the autumn extraordinary session begins, which will require some cooperation from opposition parties (either votes or abstentions).

Monetary policy implications

The potential candidates for LDP leader have not made clear their stances on monetary policy, making it difficult to definitively discuss implications. With the exception of Takaichi, who explicitly opposed rate hikes during last year's LDP leadership race, and Taro Kono, who endorsed them, many candidates stated only that they would respect the Bank of Japan (BoJ)'s independence and did not state any clear position.

Some market participants appear to be convinced that Takaichi's appointment as PM would hamper the BoJ's ability to raise rates, but it is unclear at this point whether she would continue to advocate dovish monetary policy after the LDP's Upper House election loss. In either case, we would not expect the BoJ to overturn its core stance of basing rate-hiking decisions on inflation and the economic outlook, but BoJ may get more cautious about the rate hikes to gather more supporting data.

That said, we think the political landscape will remain volatile through early October, making it even more difficult to raise rates both at the next monetary policy meeting (MPM) on 19 September and at the 30 October meeting. We continue to expect the next rate hike to come in January 2026, followed by a gradual pace with one hike every six months or so (see [BoJ Watch: July MPM SOP hawkish, but in line with the market pricing](#), 8 August).

- Takayasu Kudo, Japan Economist

Rates: Fiscal and political risks are mounting for JGBs

The JGB yield curve steepened slightly in response to Ishiba's resignation announcement, and JGB futures (September contract) rose versus the close of the previous week. As noted, we think the new LDP leader will be in favor of procyclical fiscal policy, but bond market positioning does not appear sharply skewed at this point.

We think the rise in JGB futures (Sep contracts) since the early Monday reflects (1) the slowing US labor market and (2) the fact that 12 September is the final day of trading for September contracts and the rollover to December contracts is expected to ramp up in earnest going forward.



With loans under the BoJ's lending support scheme set to mature on 12 September, we think the market would factor in fiscal risk by shorting the December contract (see [Japan Rates Watch: Yen rates market's September focus points 04 September 2025](#)).

Our basic view on JGBs is unchanged despite Ishiba's resignation announcement. Japan's promised \$550bn investment in the US heightens the risk of an increase in Fiscal Investment Loan Program (FILP) bond issuance, and we have a generally bearish view on yen duration. We therefore think shorting the December invoice spread would be an attractive strategy in the near term.

- Tomonobu Yamashita, Rates Strategist

FX implications

We have argued that the market would focus on implications of PM Ishiba's potential resignation on fiscal policy and potentially on monetary policy (see: [Japan Viewpoint: Q&A on LDP's leadership race 23 July 2025](#)). As noted above, the new leader could be more open to fiscal spending. While leading candidates and hence ultimate implications for the FX market remain uncertain, risks are skewed to looser fiscal policy as the LDP lost the election with opposition parties calling for more spending and criticizing the lack of the government's fiscal measures. Whoever becomes the new LDP president, he or she needs support from at least one opposition party to be elected as PM and pass budget so fiscal risk would not be fully removed in any case.

Moreover, certain candidates may call for keeping monetary policy easy. While the BoJ would conduct monetary policy based on data, political support for its policy would be desired for smooth policy implementation. The result of the LDP's presidential election is unlikely to change the direction of bias, but it may impact the timing and the pace of rate hikes at a margin.

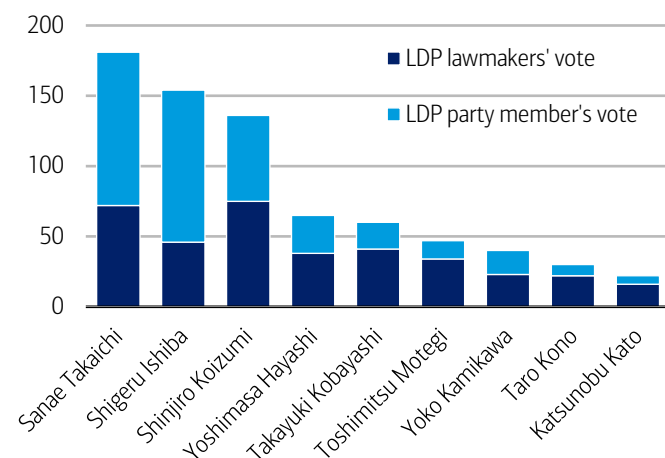
Our view has been to stay short yen while Ishiba's resignation risk remains high and until the risk of a loose macro policy mix under new leadership is sufficiently priced. USD/JPY may trade up to 149-150 in the near-term. After that, it would depend on who prevails as the new leader. If a fiscal dove, such as Sanae Takaichi, prevails, USD/JPY is likely to break 150 decisively. Long CHF/JPY may be the cleanest trade to express JPY's fiscal risk given CHF's healthy fiscal profile and increasing risk premium for USD and JPY, the traditional safe haven currencies (see: [FX Viewpoint: G10 FX: more of the same please 08 September 2025](#)).

- Shusuke Yamada, FX/Rates Strategist



Exhibit 1: The vote count in the first round of the previous LDP presidential election in Sep '24

The market will likely base its outlook on the candidates who stood in September 2024. Takaichi, Ishiba, Koizumi received the most votes in the first round.

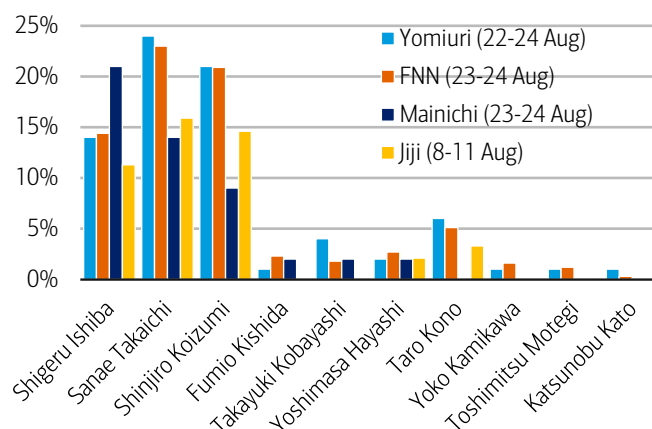


Source: BofA Global Research

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Exhibit 2: LDP's potential next prime ministers in public opinion polls (August survey, response rate)

The most likely candidates for next LDP leader cited in August opinion polls indeed ran in 2024 – Ishiba, Takaichi, and Koizumi.



Source: BofA Global Research, news reports *Mainichi and FNN include support rates for opposition parties

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Exhibit 3: Vote weight in LDP presidential election

Emergency election would have smaller weight in party member votes in the first round

Regular or emergency	Voting round	MP votes*	Party member votes
Regular election	First round	1 vote per MP (297)	Equal weight (297)
	Final round**	1 vote per MP (297)	47 votes (1 vote per prefectural representative)
Emergency election	First round	1 vote per MP (297)	141 votes (1 vote per 3 representatives per prefecture = $47 \times 3 = 141$)
	Final round**	1 vote per MP (297)	47 votes*** (1 vote per prefectural representative)

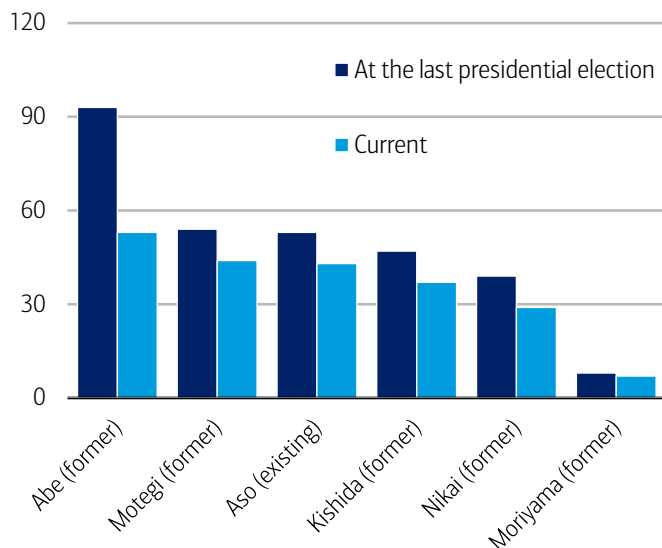
Source: BofA Global Research, LDP *Based on Lower House data and the result of the Upper House election this month. **If no candidate won majority. *** Based on information from Mainichi online on Aug 31, 2020

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Exhibit 4: The number of current lawmakers in the major former factions

The race will likely come down to where the party's now-disbanded major factions—which still retain considerable influence—put their support

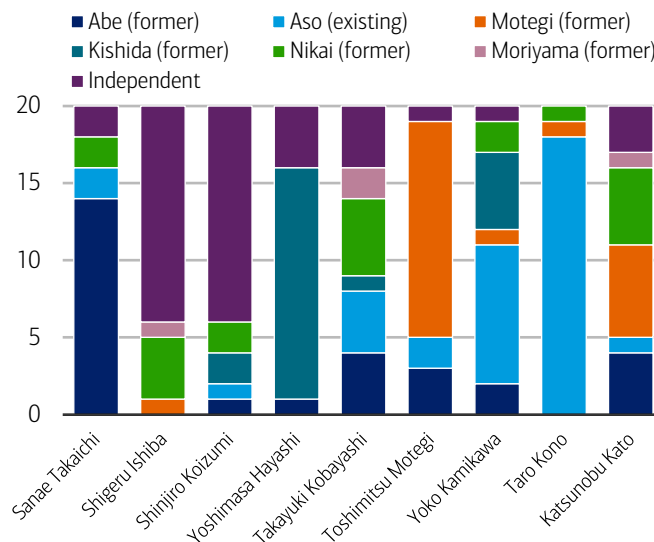


Source: BofA Global Research

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Exhibit 5: The factional breakdown of endorsers in last election

Takaichi and Hayashi received endorsements from numerous MPs in their (former) factions, while Koizumi and Kobayashi drew endorsements from a broad range of factions including independents



Source: BofA Global Research

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Exhibit 6: The key profiles and policy stances of the candidates in the previous LDP presidential election in Sep '24

Candidates differ on fiscal policy but share procyclical bias; little monetary policy impact, but Oct rate hike less likely

	Age	Main position	Faction	Fiscal policy	Monetary policy*
Takaichi Sanae	64	Former Minister in charge of Economic Security	Abe	Insists consumption tax cut	Opposes rate hikes
Shigeru Ishiba	68	Current Prime Minister	Ishiba	Fiscal discipline	Respects BoJ independence
Shinjiro Koizumi	44	Current Agricultural Minister	None	Cautious on consumption tax cut	Respects BoJ independence
Yoshimasa Hayashi	64	Current Chief Cabinet Secretary	Kishida	Cautious on consumption tax cut	Respects BoJ independence
Takayuki Kobayashi	50	-	Nikai	Open to tax cut	-
Toshimitsu Motegi	69	Former Minister of Foreign Affairs, Former Secretary General	Motegi	Fiscal discipline	Supports rate hikes
Yoko Kamikawa	72	Former Minister of Foreign Affairs	Kishida	-	-
Taro Kono	62	Former Digital Minister	Aso	Opposes consumption tax cut	Pushes rate hikes
Katsunobu Kato	69	Current Minister of Finance	Motegi	Opposes consumption tax cut	-
Fumio Kishida	68	Former Prime Minister	Kishida	Cautious on consumption tax cut	-

Source: BofA Global Research. Note: The candidates are listed in order of votes received in the first round of the previous LDP leadership election. *Remarks made during last year's LDP leadership election.

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