

(English translation prepared by the Bank's staff based on the Japanese original)

June 15, 2011

Bank of Japan

Monthly Report of Recent Economic and Financial Developments¹

June 2011

Summary

Japan's economy continues to face downward pressure, mainly on the production side, due to the effects of the earthquake disaster, but is showing some signs of picking up.

After the earthquake, production and exports declined sharply and domestic private demand also weakened. Although such downward pressure remains, production and domestic private demand have recently been showing some signs of picking up, with supply-side constraints starting to ease and household and business sentiment improving somewhat.

Japan's economy is likely to continue facing downward pressure for the time being, mainly on the production side, but is expected to return to a moderate recovery path as production regains traction with further easing of supply-side constraints.

An increase in production is likely to become more noticeable as supply-side constraints ease further. In this situation, exports are also expected to turn upward reflecting the improvement in overseas economic conditions. Business fixed investment, housing investment, and public investment are expected to increase gradually, mainly due to growing demand for the purposes of restoring capital stock. Meanwhile, private consumption is expected to pick up partly due to the improvement in household sentiment as production recovers.

On the price front, the three-month rate of change in domestic corporate goods prices is rising, mainly due to the increase in international commodity prices. The

¹ This report is based on data and information available at the time of the Bank of Japan Monetary Policy Meeting held on June 13 and 14, 2011.

year-on-year rate of change in consumer prices (excluding fresh food) is slightly positive.

The rate of increase in domestic corporate goods prices is expected to slow for the time being, reflecting movements in international commodity prices. The year-on-year rate of change in consumer prices is expected to remain slightly positive.²

The weighted average of the overnight call rate has been below the 0.1 percent level, and interest rates on term instruments have been more or less unchanged. Meanwhile, compared with last month, the value of the yen against the U.S. dollar has risen, while long-term interest rates and stock prices have remained at more or less the same levels.

Financial conditions have generally continued to ease, although weakness has been observed in the financial positions of some firms, mainly small ones, since the earthquake.

The overnight call rate has remained at an extremely low level, and the declining trend in firms' funding costs has continued. Stimulative effects from low interest rates are still partly constrained given current developments in economic activity and prices. With regard to credit supply, firms have continued to see financial institutions' lending attitudes as being on an improving trend. Issuing conditions for CP have continued to be favorable, and those for corporate bonds have improved and become favorable as a whole. As for credit demand, firms have recently shown signs of increasing their demand for working capital. Against this backdrop, the year-on-year rate of decline in bank lending is slowing. The amount outstanding of corporate bonds has exceeded the previous year's level and that of CP has been around the year-ago level. In these circumstances, firms have retained their recovered financial positions on the whole, although weakness has been observed in those of some firms, mainly small ones, since the earthquake. Meanwhile, the

² The base year for the consumer price index (CPI) is scheduled to be changed to 2010 in August 2011, and year-on-year figures retroactive to January 2011 will be revised accordingly. This rebasing is likely to cause the year-on-year rate of change in the CPI to be revised downward.

year-on-year rate of change in the money stock has been in the range of 2.5-3.0 percent.