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March 16, 2012

Bank of Japan

Minutes of the Monetary Policy Meeting

on February 13 and 14, 2012

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

A Monetary Policy Meeting of the Bank of Japan Policy Board was held in the Head Office of the Bank of Japan in Tokyo on Monday, February 13, 2012, from 2:00 p.m. to 4:34 p.m., and on Tuesday, February 14, from 9:01 a.m. to 12:38 p.m.[1]

Policy Board Members Present

Mr. M. Shirakawa, Chairman, Governor of the Bank of Japan

Mr. H. Yamaguchi, Deputy Governor of the Bank of Japan

Mr. K. G. Nishimura, Deputy Governor of the Bank of Japan

Mr. S. Nakamura

Mr. H. Kamezaki

Mr. R. Miyao

Mr. Y. Morimoto

Ms. S. Shirai

Mr. K. Ishida

Government Representatives Present

Mr. Y. Fujita, Senior Vice Minister of Finance, Ministry of Finance[2]

Mr. S. Sato, Deputy Vice Minister for Policy Planning and Coordination, Ministry of Finance[3]

Mr. K. Ishida, Senior Vice Minister, Cabinet Office[2]

Mr. K. Matsuyama, Vice Minister for Policy Coordination, Cabinet Office[3]

Reporting Staff

Mr. K. Yamamoto, Executive Director

Mr. H. Nakaso, Executive Director (Assistant Governor)

Mr. M. Amamiya, Executive Director

Mr. N. Kinoshita, Executive Director

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[1] The minutes of this meeting were approved by the Policy Board at the Monetary Policy Meeting held on March 12 and 13, 2012 as "a document describing an outline of the discussion at the meeting" stipulated in Article 20, paragraph 1 of the Bank of Japan Act of 1997. Those present are referred to by their titles at the time of the meeting.

[2] Messrs. Y. Fujita and K. Ishida were present on February 14.

[3] Messrs. S. Sato and K. Matsuyama were present on February 13.

Mr. K. Momma, Director-General, Monetary Affairs Department

Mr. T. Umemori, Deputy Director-General, Monetary Affairs Department[4]

Mr. K. Kamiyama, Head of Policy Planning Division, Monetary Affairs Department

Mr. S. Aoki, Director-General, Financial Markets Department

Mr. E. Maeda, Director-General, Research and Statistics Department

Mr. T. Sekine, Head of Economic Research Division, Research and Statistics Department

Mr. H. Ono, Director-General, International Department

Secretariat of the Monetary Policy Meeting

Mr. Y. Iino, Director-General, Secretariat of the Policy Board

Mr. T. Tachibana, Director, Deputy Head of Planning and Coordination Division, Secretariat of the Policy Board

Mr. H. Chida, Head of Policy Infrastructure Division, Monetary Affairs Department[4]

Mr. H. Kamiguchi, Senior Economist, Monetary Affairs Department

Mr. M. Kasai, Senior Economist, Monetary Affairs Department

[4] Messrs. T. Umemori and H. Chida were present on February 14 from 10:10 a.m. to 12:38 p.m.

I. Summary of Staff Reports on Economic and Financial Developments[5]

A. Money Market Operations in the Intermeeting Period

The Bank, in accordance with the guideline decided at the previous meeting on January 23 and 24, 2012, had been providing ample funds sufficient to meet demand in financial markets and was doing its utmost to ensure stability in the markets.[6] In this situation, the uncollateralized overnight call rate had been in the range of 0.070 to 0.090 percent.

In the Bank's U.S. dollar funds-supplying operation against pooled collateral, the total bidding amount decreased reflecting the steady improvement in U.S. dollar funding conditions.

B. Recent Developments in Financial Markets

In the money market, interest rates had been stable as the sense of an abundance of liquidity continued to be strong amid the Bank's provision of ample funds. General collateral (GC) repo rates had been at around 0.1 percent. As for interest rates on term instruments, yields on treasury discount bills (T-Bills), including those with longer maturities, had been stable at around 0.1 percent. Rates on longer-term interbank instruments had been more or less unchanged.

Strains in U.S. dollar funding conditions were abating, as evidenced by the fact that major funds providers such as money market mutual funds (MMMFs) had eased their cautious attitudes toward releasing funds to European financial institutions. The U.S. dollar funding premium in the foreign exchange swap markets -- that is, the spread between the FX swap-implied U.S. dollar rate and U.S. dollar LIBOR -- had been at around zero for funding from the yen while that for funding from the euro had been on a narrowing trend, although it remained at a relatively high level.

The benchmark long-term interest rate had generally been more or less flat at a low level, although it fluctuated in correlation with developments in U.S. long-term interest rates. Japanese stock prices had been steady in tandem with firm U.S. stock prices, and the closing price of the Nikkei 225 Stock Average temporarily recovered to the 9,000 yen

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[5] Reports were made based on information available at the time of the meeting.

[6] The guideline was as follows:

The Bank of Japan will encourage the uncollateralized overnight call rate to remain at around 0 to 0.1 percent.

level for the first time in three months. In the foreign exchange market, the yen had fluctuated against the U.S. dollar on the back of the fact that Japan's trade balance had turned to a deficit as well as prospects that interest rates would continue to be low for a protracted period in the United States. The yen had recently been in the range of 77.5-78 yen to the dollar.

C. Overseas Economic and Financial Developments

The pace of recovery of the world economy was slowing.

The U.S. economy continued to recover at a moderate pace despite the burdens of balance-sheet repair, and some improvement had recently been observed, mainly in employment and private consumption. The number of employees continued to increase moderately and the unemployment rate had been declining recently. Consumer sentiment had recovered to the level registered before summer 2011 and car sales were increasing, due in part to the removal of supply-side constraints. Exports and business fixed investment rose moderately and production stayed on an increasing trend. On the other hand, housing investment remained at a depressed level with housing prices exhibiting weakness. As for prices, while slack in supply and demand conditions in the goods and labor markets continued to exert downward pressure on prices, the year-on-year rate of increase in the consumer price index (CPI) for all items decelerated due to a decline in the year-on-year rate of increase in energy prices. Meanwhile, the year-on-year rate of increase in the CPI for all items less food and energy, or the core CPI, accelerated to some extent because the shelter index continued to rise moderately.

Economic activity in the euro area was increasingly sluggish. Growth in exports was sluggish owing to the slowdown in the world economy, and the rate of increase in business fixed investment had slowed. Private consumption was more or less unchanged. Under these circumstances, production was declining. Household and business sentiment showed signs of a pick-up in Germany, but it remained weak, particularly in some peripheral countries. As for prices, although the year-on-year rate of increase in the Harmonized Index of Consumer Prices (HICP) for all items remained at a relatively high level, it had declined somewhat due to the effects of an earlier fall in international commodity prices. Meanwhile, the level of economic activity in the United Kingdom was more or less unchanged.

With regard to Asia, the Chinese economy continued to show high growth as a whole. The rate of increase in exports was slowing and that in production was decelerating to some extent; however, private consumption and fixed asset investment maintained high growth. The growth rate of the Indian economy had decelerated due to the cumulative effects of monetary tightening. The pace of economic growth in the NIEs and the ASEAN countries was also slowing to some extent. As for domestic demand in the NIEs and the ASEAN countries, while the rate of increase in business fixed investment seemed to be slowing, private consumption remained firm. In a situation where the decline in exports to advanced economies was coming to a halt, the pace of decline in exports and production had been moderating, aided partly by the waning effects of the disruption caused by the flooding in Thailand. In many of these Asian economies, core inflation rates were at relatively high levels, mainly reflecting the higher wage inflation caused by tight labor market conditions. On the other hand, inflation rates for all items were declining at a moderate pace due mainly to a halt in the surge in prices of fresh food.

Tensions in global financial markets regarding the European debt problem had abated somewhat compared with the situation around the end of 2011. The funding conditions of European financial institutions continued to improve as the effects of the 36-month longer-term refinancing operations conducted by the European Central Bank (ECB) became more pronounced. Spreads between interest rates on euro-denominated term instruments and overnight index swap (OIS) rates were narrowing, and those between interest rates on U.S. dollar-denominated term instruments and OIS rates had begun to contract. Regarding funding conditions for long-term credit, issuance of bank debentures was increasing as their credit spreads tightened. Although long-term interest rates in the United States and Germany had fallen significantly at one point toward the end of January 2012 because of heightened expectations for monetary easing in the United States, they had risen thereafter in reflection of favorable developments in the U.S. employment indicators and expectations for progress to be made in addressing the Greek debt problem. The yield spreads of government bonds issued by European countries over German government bonds had tightened for most of these countries. With regard to the credit markets in Europe and the United States, there were signs that yield spreads between corporate bonds and government bonds were narrowing to some extent, although they remained at high levels. U.S. stock prices had risen, as had stock prices in Europe, particularly those of financial stocks. As for financial markets in emerging economies, many of these had recently seen a rise in their stock prices and an appreciation in their currencies reflecting heightened expectations for monetary easing on a global basis.

D. Economic and Financial Developments in Japan

1. Economic developments

Exports and production remained more or less flat, mainly due to the effects of a slowdown in overseas economies and the yen's appreciation. On a monthly basis, they increased in December as the effects of the flooding in Thailand eased. They were expected to continue to be essentially flat for the time being and increase moderately thereafter, mainly reflecting a pick-up in the pace of recovery in overseas economies.

Public investment had stopped declining. It was expected to increase gradually, mainly due to the restoration of damaged social capital.

Business fixed investment had been on a moderate increasing trend, aided partly by the restoration of disaster-stricken facilities. It was expected to continue on this moderate uptrend, partly due to efforts by firms to restore and reconstruct disaster-stricken facilities as well as to strengthen earthquake resistance and business continuity systems, although it would be affected by the slowdown in overseas economies and the yen's appreciation for the time being.

The employment and income situation continued to be severe, although there were signs of improvement.

Private consumption remained firm, due in part to a recovery in demand that had been temporarily restrained after the earthquake disaster. This situation was expected to continue as the employment situation gradually headed toward improvement.

Housing investment had generally been picking up. It was expected to increase gradually, mainly due to the reconstruction of disaster-stricken homes.

As for prices, international commodity prices had increased somewhat recently, although they remained essentially flat. The three-month rate of change in the domestic corporate goods price index (CGPI) had been more or less flat, reflecting movements in international commodity prices. The CGPI was expected to stay this course for the time being. The year-on-year rate of change in the CPI (all items less fresh food) was currently around 0 percent and was expected to stay at this level for the time being.

2. Financial environment

Financial conditions continued to ease.

The overnight call rate remained at an extremely low level, and firms' funding costs declined moderately. Stimulative effects from low interest rates were still partly constrained given current developments in economic activity and prices. With regard to credit supply, firms continued to see financial institutions' lending attitudes as being on an improving trend. Issuing conditions for CP continued to be favorable. Those for corporate bonds also remained favorable on the whole. As for credit demand, firms showed signs of increasing their demand mainly for working capital and funds related to mergers and acquisitions. Against this backdrop, the year-on-year rate of increase in the amount outstanding of bank lending had risen. The year-on-year rate of increase in the amount outstanding of CP had become somewhat higher while that of corporate bonds had recently been slightly negative, partly because some issuers had shifted to the CP market. In these circumstances, firms retained their recovered financial positions on the whole. Meanwhile, the year-on-year rate of change in the money stock had been positive at around 3 percent.

II. Summary of Discussions by the Policy Board on Economic and Financial Developments

A. Economic Developments

As for global financial markets, members agreed that funding conditions of European financial institutions continued to improve as the effects of the provision of a large amount of funds by the ECB -- mainly through the 36-month longer-term refinancing operations -- were spreading, and that against this background, tensions in global financial markets regarding the European debt problem had abated somewhat compared with the situation around the end of 2011. Some members expressed the view that tensions had lessened somewhat not only in the short-term funding market but also in the long-term government bond market and the credit market. On this basis, members shared the recognition that due attention needed to be paid to the possibility that tensions in the markets could intensify again, as many uncertain aspects remained with regard to the following measures to respond to the problem: (1) correcting imbalances mainly through fiscal reform and strengthening competitiveness in each country; (2) expanding the financial firewall to contain market disruptions; and (3) enhancing fiscal governance within the euro area.

With regard to overseas economies, members concurred that, although the pace of growth had slowed mainly due to the European debt problem and to the cumulative effects of monetary tightening in emerging and commodity-exporting economies, some improvement had recently been observed in the U.S. economy. As for the outlook, they shared the view that the pace of growth was likely to continue to slow for the time being, particularly in the euro area economy, but would probably pick up thereafter led by emerging and commodity-exporting economies.

Members agreed that economic activity in the euro area was increasingly sluggish on the whole, as the effects of the European debt problem were spreading through a deterioration in business and household sentiment as well as a more cautious lending stance by financial institutions. With regard to the German economy, many members pointed out that some improvement had recently been observed in business and household sentiment. As for the outlook, members shared the view that economic activity in the euro area would continue to be quite sluggish for the time being against the background of continuing fiscal austerity and financial institutions' reduction of their assets. They also shared the view that, depending on developments in the European debt problem, growth in the European economy -- and consequently in the global economy as a whole -- could turn out to be significantly weaker than expected via instability in the financial system in particular, and that it was therefore necessary to continue to pay due attention to future developments.

Members shared the view that the U.S. economy continued to recover at a moderate pace, and that some improvement had recently been observed despite the burdens of balance-sheet repair. Most members referred to indicators related to employment and private consumption as examples of the improvement observed of late. Some of these members pointed to the possibility that the mechanism for a self-sustained recovery, by which the effects of favorable conditions in the corporate sector fed through into the household sector, was starting to operate. As for the outlook, members concurred that the U.S. economy was likely to continue to recover at a moderate pace supported by accommodative financial conditions. Some members cited weak housing prices and a further reduction in fiscal spending as factors that would restrain the recovery to only a moderate pace.

Members shared the view that the pace of growth in emerging and commodity-exporting economies had moderated somewhat on the whole, mainly due to the impact of a decrease in exports induced by a slowdown in European economies, as well as the effects of a decline in real purchasing power -- incurred by the earlier rise in prices -- and of the cumulative effects of monetary tightening. A few members said that, although economic conditions in the NIEs and the ASEAN countries continued to be adversely affected by the slowdown in European economies, exports were picking up due to the waning effects of the flooding in Thailand. As for the outlook, members agreed that, in a situation where room for monetary easing was expanding following a decline in inflation rates, the growth rates of emerging and commodity-exporting economies would increase again as domestic demand remained firm, mainly due to a recovery in households' real purchasing power. Some members noted that, in some of these economies, the monetary policy stance had switched from tightening to easing in response to a decline in inflation rates.

Based on the above deliberations on economic and financial conditions abroad, members discussed the state of Japan's economy.

Regarding recent developments in the economy, members agreed that Japan's economic activity had been more or less flat, mainly due to the effects of the slowdown in overseas economies and the appreciation of the yen, but that domestic demand had been firm due in part to reconstruction-related demand after the earthquake disaster. They shared the view that exports and production remained more or less flat, mainly due to the effects of the slowdown in overseas economies and the yen's appreciation. One member -- referring to the fact that the level of production in December 2011 had exceeded the previous-month projection for the first time in seven months -- said that downward pressure on production seemed to be easing. A different member expressed the opinion that the progress seen worldwide in inventory adjustments in IT-related goods was positively affecting the export and production of these goods. Members concurred that business fixed investment had been on a moderate increasing trend, aided partly by the restoration of disaster-stricken facilities. Some members commented that attention needed to be paid to the effects of the dampening in corporate profits and consequent delayed pick-up in stock prices. A few members noted that indicators of business sentiment had improved slightly.

Members shared the view that private consumption remained firm due in part to a recovery in demand that had been temporarily restrained after the earthquake disaster. Some members pointed out that the number of new passenger-car registrations increased substantially in January 2012, mainly due to the reintroduction of subsidies for purchasers of environmentally friendly cars. Members agreed that housing investment had generally been picking up and public investment had stopped declining. With regard to the fact that Japan's trade balance in 2011 had turned to a deficit for the first time in 48 years, one member noted that, although the trade balance would remain in deficit for the time being, the current account was unlikely to move into deficit as the amount of surplus in the balance of income would significantly exceed that of the trade deficit.

As for the outlook for the economy, members shared the view that Japan's economic activity would remain more or less flat for the time being, but thereafter the economy was likely to return to a moderate recovery path as the pace of recovery in overseas economies picked up, led by emerging and commodity-exporting economies, and as reconstruction-related demand after the earthquake disaster gradually strengthened. On this basis, members agreed that the economic outlook continued to entail a high degree of uncertainty regarding the prospects for and outcome of the European debt problem, the supply and demand balance for electricity, and the effects of the yen's appreciation. One member said that, in a situation where it was highly uncertain whether economic growth and price stability could be achieved at the same time in emerging economies, the unpredictability of the situation in the Middle East, particularly in terms of Iran, also warranted careful monitoring. A different member said that attention needed to be paid to the fact that the level of economic activity in Japan remained low.

Members agreed that the year-on-year rate of change in the CPI (all items less fresh food) was currently around 0 percent and likely to stay at this level for the time being. A few members added that a continuation of the year-on-year declines in the CPI for all items less energy and food and in the GDP deflator should be borne in mind. One of these members said that the factors behind the divergence between developments in the GDP deflator and those in the CPI could be summarized as (1) the price-setting behavior of exporting firms in the phase of the yen's appreciation, (2) the price-setting behavior of importing firms in a situation where materials prices had been rising, and (3) the effects of significant improvement in the quality of capital goods and some other types of goods. On this basis, this member continued that, in evaluating price developments, it was appropriate to examine a wide range of price indicators while using the CPI as the main indicator.

B. Financial Developments

Members agreed that financial conditions in Japan continued to ease.

Members agreed that money market rates had been extremely stable, as the Bank had been pursuing powerful monetary easing and the soundness of financial institutions' balance sheets had been maintained. They shared the view that issuing conditions for CP remained favorable, as did those for corporate bonds on the whole. They were of the view that firms' funding costs had declined moderately, and that the availability of funds remained on an improving trend. With regard to the fact that the year-on-year rate of decline in the total amount of funds raised by the private sector was slowing, some members said that they were paying attention to this development as it was a positive sign for economic activity. In relation to this, a different member, noting that the total amount of funds raised by the private sector had fallen significantly, said that attention should be paid to the fact that its level remained low. A few members noted that households' and firms' short-term inflation expectations had recently declined slightly. One of these members expressed the opinion that careful attention should be paid to such developments, since they could lead to a slowdown in the pace at which the rate of inflation converged with the level considered stable from a medium- to long-term perspective, that is, the inflation anchor.

III. Summary of Discussions on Monetary Policy for the Immediate Future

In discussing monetary policy for the immediate future, members began with deliberations on the Bank's strategy for communication to the public regarding the conduct of monetary policy, primarily because (1) members had long shared the recognition that it was necessary to keep deliberating on an enhanced strategy for the Bank's communication regarding the conduct of monetary policy; (2) against this background, at the previous meeting on January 23 and 24, 2012, some members reiterated the need to review the "understanding of medium- to long-term price stability" (hereafter "understanding") and how the Bank presented its commitment to the policy duration based on the "understanding," given that the Federal Reserve had been discussing its strategy for communication; and (3) there was renewed and increased attention to central banks' determination to achieve price stability following the Federal Reserve's announcement of the introduction of its "longer-run goal" for price stability.

Members first discussed the "understanding" -- that is, the level of inflation that each Policy Board member understood, when conducting monetary policy, as being consistent with price stability over the medium to long term.

Regarding the "understanding," most members acknowledged that there was a view that it did not effectively communicate the Bank's policy stance, and recognized that one factor behind this view was that the Bank had provided the understanding of individual Policy Board members, which represented the level of inflation that each member considered to be consistent with price stability sustainable over the medium to long term, and that each member considered the Bank should aim to achieve. These members said that, while its basic thinking was unchanged on price stability -- such as with regard to the conceptual definition, time frame, and main indicator -- it might be possible for the Bank to further clarify the price stability it aimed to achieve by releasing an inflation rate that represented a judgment by the Bank, or consensus among all the Policy Board members, instead of continuing to release the level of inflation that represented the understanding of individual Policy Board members. Based on these views, members discussed a numerical expression that could represent the consensus among all the Policy Board members as the inflation rate judged to be consistent with price stability sustainable over the medium to long term.

Some members noted that, in formulating a specific numerical expression, the Policy Board should continue to take three perspectives into consideration: (1) a measurement bias in the price index; (2) the safety margin that acted as a buffer against the risk of a vicious cycle of deflation and stagnation; and (3) the rate of inflation at which households and firms perceived price stability -- that is, the public's perception of price developments. One of these members expressed the view that it was necessary to retain a somewhat larger safety margin given the limited room to conduct additional fiscal policies. Meanwhile, the other members commented that there was no significant change in their thinking with respect to the three perspectives compared with the time when the "understanding" had been reviewed in April 2011. Many members expressed the view that it was desirable to present the numerical expression as a single figure to clearly represent the Bank's policy stance. However, these members continued that, taking into account the high degree of uncertainty surrounding future developments, such as structural changes in Japan's economy and movements in the global economic environment, the need to denote the inflation rate with a degree of latitude was not insignificant. Some members expressed the view that it was appropriate for the time being to aim to achieve an inflation rate of 1 percent, which had been presented as the point around which each member's "understanding" centered, considering that the current level of inflation perceived by the public was relatively low. These members continued, however, that the Bank could take this opportunity to change the numerical expression to one that took account of the possibility that the inflation rate the Bank should aim to achieve could surpass 1 percent in the longer run. A few of these members said that a numerical expression of 1 to 2 percent was one option. One member commented that, from a long-term perspective, the Bank should aim to achieve an inflation rate that many other major economies commonly pursued -- at present, 2 percent -- so that the foreign exchange rate would not move to a long-term trend of being one-sided. A different member said that it was not necessarily essential for the Bank to aim to achieve the same level of inflation, given that the economic situation facing Japan differed from those faced by other major economies. In response, some members said that there was no need to significantly change the existing expression; namely, that the current "understanding" on the basis of a year-on-year rate of change in the CPI was "a positive range of 2 percent or lower, centering around 1 percent." Based on this discussion, members agreed that the inflation rate that the Bank should aim to achieve ought to be set at 1 percent for the time being, and that it would be appropriate to express the inflation rate with a degree of latitude as "a positive range of 2 percent or lower in terms of the year-on-year rate of change in the CPI," since the inflation rate that the Bank should aim to achieve over the medium to long term could change in the longer run.

Members also discussed what the Bank ought to name the inflation rate that was consistent with price stability sustainable over the medium to long term, and that it should aim to achieve. Many members expressed the view that the connotation of the term "understanding" that the Bank had used thus far might suggest that the Bank was passively waiting for a recovery in the economic and price situation, and thus did not effectively communicate the Bank's active stance in its efforts to achieve price stability. Some members commented that (1) the term "target" suggested that monetary policy would be conducted in an automatic manner in response to short-term fluctuations in prices, so as to maintain a certain level of inflation; (2) the terms "target" and "definition" had rigid and inelastic connotations, and therefore it would not be appropriate to use these terms in a situation of a high degree of uncertainty surrounding future developments such as structural changes in Japan's economy and movements in the global economic environment; and (3) as with the term "understanding," "benchmark" would entail some vagueness in terms of representing the Bank's policy stance. Based on this discussion, members agreed that it would be appropriate to refer to the aforementioned inflation rate that was consistent with price stability sustainable over the medium to long term as "the price stability goal in the medium to long term."

Members next discussed <u>the Bank's commitment aimed at generating policy duration effects</u> based on the "understanding."

Members shared the view that it was desirable for the Bank to clarify its policy stance by -- in addition to introducing "the price stability goal in the medium to long term" -- revising the expression representing the Bank's commitment to the policy duration, which had been articulated as being until the Bank judged that price stability was in sight on the basis of the "understanding." They then concurred that it was appropriate for the Bank to further clarify the conditions for its future conduct of monetary policy by stating that, for the time being, it would pursue powerful monetary easing with the aim of achieving the goal of 1 percent in terms of the year-on-year rate of increase in the CPI, and continue to do so until it judged that the 1 percent goal was in sight. They also agreed that the Bank's policy stance would be more effectively communicated if the Bank, taking into account policy measures that had been implemented other than the virtually zero interest rate policy, expressed its policy conduct that was committed to generating policy duration effects in a more accurate and active manner. They continued that this could be done by replacing the existing expression -- namely, that the Bank would maintain the virtually zero interest rate policy -- with the new expression, that is, that the Bank would pursue powerful monetary easing by conducting its virtually zero interest rate policy and by implementing the Asset Purchase Program (hereafter the Program) mainly through the purchase of financial assets. Some members commented that the new expression would make it clearer that the Bank was committed to implementing any additional measures, if deemed necessary. One of these members said that such revision of the expression would enhance policy duration effects. With regard to how the duration of monetary policy commitment should be presented, a different member expressed the view that, instead of presenting it with a link to a specific time or to the figure of a specific indicator released, the Bank's current way of presenting it with a link to policy authorities' projections for economic activity and prices was desirable from the standpoint of ensuring stability in expectations for future monetary policy, as well as maintaining the credibility of the Bank's policy. A few members said that, in the future conduct of monetary policy, it was important that the Bank make continued efforts to confirm that no significant risk, such as the accumulation of financial imbalances, could be identified from the viewpoint of ensuring sustainable economic growth. These members continued that the Bank should endeavor to communicate this point to the public in an appropriate manner.

Members shared the view that it was desirable that the Bank not only review its strategy for communication to the public but also implement measures to further enhance monetary easing, for the purpose of backing the clarification of its policy stance with action that would enhance the effects of such clarification. A few members said that this combination of policy measures was expected to further increase monetary easing effects by influencing longer-term interest rates or firms' and households' decision making. Moreover, members shared the view that, from the perspective of further supporting recent positive developments from the financial side and better ensuring the economy's return to a moderate recovery path amid a continued high degree of uncertainty surrounding economic developments both at home and abroad, the implementation of measures to enhance monetary easing at this time was important. Based on these views, members discussed the specifics of the measures to enhance monetary easing.

With regard to <u>the Program</u>, most members expressed the view that it was appropriate for the Bank to substantially increase the total size by about 10 trillion yen for the purpose of backing the clarification of its policy stance with action. These members shared the view that, considering the current financial environment in particular, the increase in the Program should be earmarked for the purchase of Japanese government bonds (JGBs). A few of these members said that it was appropriate to complete the increased purchases by the end of 2012. Some members noted that, if the Bank decided to increase the amount of JGB purchases by about 10 trillion yen at this meeting, together with regular purchases to meet a trend increase in banknote demand, this would result in the purchase of a large amount of JGBs at the pace of about 40 trillion yen per year. They continued that it was important for the Bank to clearly recognize and explain to the public that these JGB purchases were not conducted for the purpose of monetization. Some members expressed the opinion that the goal of overcoming deflation would be achieved through efforts to strengthen growth potential and via support from the financial side, and that it was important for business firms, financial institutions, the government, and the central bank to continue making efforts in their respective roles.

Regarding the guideline for money market operations for the intermeeting period ahead, members agreed that it was appropriate to maintain the current guideline that the Bank would encourage the uncollateralized overnight call rate to remain at around 0 to 0.1 percent.

As for the fund-provisioning measure to support strengthening the foundations for economic growth, many members noted that the deadline for applications for new loans was March 31, 2012, and said that it was imperative to examine in the near future whether it was necessary to extend the deadline. Some of these members, recognizing that strengthening growth potential continued to be the major challenge for Japan's economy, expressed the view that it was appropriate to consider extending the deadline, and in doing so, examine whether further refinement in the formulation of the measure was possible. Some members said that it was likewise imperative to examine whether it was necessary to extend the deadline for new applications for loans under the funds-supplying operation to support financial institutions in disaster areas before its expiration on April 30, 2012. In consideration of these remarks, it was decided that the staff would report back at the next Monetary Policy Meeting, primarily on the results of their examination of whether it was necessary to extend the deadline for applications for new loans under the fund-provisioning measure to support strengthening the foundations for economic growth. Meanwhile, members reaffirmed that the Bank would do its utmost to ensure that the European debt problem would not threaten the stable conditions in Japan's financial markets, and consequently financial system stability. In this regard, one member noted that, as for the Bank's U.S. dollar funds-supplying operation against pooled collateral, although demand for funds supplied through the operation had weakened in light of the lessened tensions in global financial markets regarding the European debt problem, it was important that the

Bank continue to regularly conduct the operation and ensure financial market stability against the risk of a reemergence of strains in U.S. dollar funding conditions.

IV. Remarks by Government Representatives

The representative from the Ministry of Finance made the following remarks.

(1) Japan's real GDP growth rate for the October-December quarter of 2011, released on February 13, 2012, had turned negative. As for the outlook, the Japanese economy was expected to continue to pick up moderately. However, the government was highly concerned that there were significant downside risks to the economy -- mainly stemming from the further slowing down of overseas economies, due to concern over the financial system triggered by the European sovereign debt crisis and to the effects of the crisis on financial markets, and also from the prolonged appreciation of the yen.

(2) The government obtained the Diet's approval of the fourth supplementary budget for fiscal 2011 on February 8, 2012. It would continue to do its utmost to promptly obtain the Diet's approval of the budget for fiscal 2012. Furthermore, the government would work on reforms in line with the draft plan of the comprehensive reform of the social security and taxation systems decided on January 6, primarily by submitting to the Diet related bills on fundamental reform of the tax system -- including amendments to the Consumption Tax Act -- by the end of fiscal 2011. In doing so, the government would continue to aim to secure stable financial resources for social security functions and at the same time achieve fiscal consolidation.

(3) In order to overcome deflation, the government placed importance on making its utmost efforts in close cooperation with the Bank with regard to the future of economic management. The government welcomed, as a timely and vigorous action, the Bank's discussion at this meeting about increasing the total size of the Program by about 10 trillion yen, and about introducing "the price stability goal in the medium to long term" and aiming to achieve an inflation rate of 1 percent for the time being. It hoped that the Bank would conduct monetary policy appropriately and decisively while continuing to sufficiently exchange views and keep close contact with the government.

The representative from the Cabinet Office made the following remarks.

(1) Japan continued to be in a chronic situation where it was difficult to overcome deflation. It seemed that factors behind deflation were the negative output gap, the decline in firms' expectations for Japan's economic growth, and prolonged deflationary expectations in the private sector. The government would like to reemphasize that, in order to smoothly carry out the comprehensive reform of the social security and taxation systems, it was necessary for the government and the Bank to work more closely and take a firmer stance on overcoming deflation, a task Japan had confronted for over a decade.

(2) In order to overcome deflation, the government had been making efforts to narrow the negative output gap by implementing expansionary fiscal policies to be effected through a series of supplementary budgets. Furthermore, with a view to raising the potential growth rate and increasing the private sector's appetite for investment, the government advanced its efforts to strengthen Japan's growth potential by accelerating the implementation of the "New Growth Strategy" and drawing up concrete plans for the "Strategy for Rebirth of Japan."

(3) The government expected the Bank to make its utmost efforts in the conduct of monetary policy in parallel with these government measures, so that measures to overcome deflation would produce visible results. On January 25, 2012, the Federal Reserve set the longer-run goal for inflation at the rate of 2 percent, as measured by the annual change in the price index for personal consumption expenditures. The government took the view that the aim of this action was to increase the transparency of the Federal Reserve's conduct of monetary policy and, together with the commitment to continuing monetary easing, thereby improve market expectations.

(4) The Bank was proposing new measures at this meeting. The government deemed this appropriate because it was in line with the worldwide trend of increasing the transparency of the conduct of monetary policy and enhancing accountability to the public. The government expected the Bank to continue to make efforts to increase transparency.

V. Votes

A. Vote on the Guideline for Money Market Operations

Based on the above discussions, members shared the view that it was appropriate to maintain the current guideline for money market operations, which encouraged the uncollateralized overnight call rate to remain at around 0 to 0.1 percent.

To reflect this view, the chairman formulated the following proposal and put it to a vote.

The Chairman's Policy Proposal on the Guideline for Money Market Operations:

1. The guideline for money market operations for the intermeeting period ahead will be as follows.

> The Bank of Japan will encourage the uncollateralized overnight call rate to remain at around 0 to 0.1 percent.

2. A public statement will be decided separately.

> Votes for the proposal: Mr. M. Shirakawa, Mr. H. Yamaguchi, Mr. K. G. Nishimura, Mr. S. Nakamura, Mr. H. Kamezaki, Mr. R. Miyao, Mr. Y. Morimoto, Ms. S. Shirai, and Mr. K. Ishida.
>
> Votes against the proposal: None.

B. Vote on "Amendment to 'Principal Terms and Conditions for the Asset Purchase Program'"

Members shared the view that it was appropriate to increase the total size of the Program by about 10 trillion yen, and to earmark such an increase for the purchase of JGBs. "Amendment to 'Principal Terms and Conditions for the Asset Purchase Program'" was then put to a vote. The Policy Board approved the amendment by a unanimous vote. It was confirmed that it would be made public after the meeting.

VI. Discussions on the Public Statements

A. Enhancement of Monetary Easing

On the basis of the above deliberations, members discussed the statement Enhancement of Monetary Easing, which included a description of three measures: (1) the introduction of "the price stability goal in the medium to long term"; (2) the clarification of the determination to pursue monetary easing; and (3) the increase in the total size of the Program, with a view to clarifying the Bank's policy stance and further enhancing monetary easing in order to overcome deflation and achieve sustainable growth with price stability. The statement was then put to a vote. The Policy Board decided the text by a unanimous vote. It was confirmed that the statement would be released immediately after the meeting (see Attachment 1).

B. The Price Stability Goal in the Medium to Long Term

Members discussed the statement The Price Stability Goal in the Medium to Long Term, which included a description of the Bank's basic thinking about "the price stability goal in the medium to long term" it had newly introduced, and put it to a vote. The Policy Board decided the text by a unanimous vote. It was confirmed that the statement would be released immediately after the meeting (see Attachment 3).

VII. Approval of the Minutes of the Monetary Policy Meeting

The Policy Board approved unanimously the minutes of the Monetary Policy Meeting of January 23 and 24, 2012 for release on February 17, 2012.

Attachment 1

February 14, 2012

Bank of Japan

Enhancement of Monetary Easing

1. At the Monetary Policy Meeting held today, the Policy Board of the Bank of Japan made the following decisions.

   (1) The Bank publishes "the price stability goal in the medium to long term" as the inflation rate consistent with price stability sustainable in the medium to long term.[7] The Bank judges "the price stability goal in the medium to long term" to be within a positive range of 2 percent or lower in terms of the year-on-year rate of change in the CPI and, more specifically, sets a goal at 1 percent for the time being.

   (2) For the time being, the Bank will pursue powerful monetary easing by conducting its virtually zero interest rate policy and by implementing the Asset Purchase Program mainly through the purchase of financial assets, with the aim of achieving the goal of 1 percent in terms of the year-on-year rate of increase in the CPI. The Bank will continue pursuing the powerful easing until it judges that the 1 percent goal is in sight on the condition that the Bank does not identify any significant risk, including the accumulation of financial imbalances, from the viewpoint of ensuring sustainable economic growth.

   (3) The Bank increases the total size of the Asset Purchase Program by about 10 trillion yen, from about 55 trillion yen to about 65 trillion yen. The increase in the Program is earmarked for the purchase of Japanese government bonds.[8] By fully implementing the Program including the additional expansion decided today, by the

[7] See "The Price Stability Goal in the Medium to Long Term" for more details.

[8] See Attachment 2 for the allocation of the increase in the Program.

end of 2012, the amount outstanding of the Program will be increased by about 22 trillion yen from the current level of around 43 trillion yen.[9]

2. The Policy Board also decided, by a unanimous vote,[10] to set the following guideline for money market operations for the intermeeting period:

   The Bank of Japan will encourage the uncollateralized overnight call rate to remain at around 0 to 0.1 percent.

3. Japan's economic activity has been more or less flat, mainly due to the effects of a slowdown in overseas economies and the appreciation of the yen. On the other hand, financial conditions in Japan have continued to ease. On the price front, the year-on-year rate of change in the CPI (all items less fresh food) is around 0 percent.

4. The outlook for Japan's economy continues to entail high uncertainty regarding the prospects and outcomes of the European debt problem, the supply and demand balance of electricity and the effects of the yen's appreciation. Recently, however, tensions in global financial markets regarding the European debt problem have abated somewhat since around the end of 2011. Some improvement has recently been observed in the U.S. economy despite the burdens of balance-sheet repair. In Japan's economy, domestic demand has been firm due in part to reconstruction-related demand after the earthquake disaster.

5. Amid continued high uncertainty surrounding economic developments both at home and abroad, the Bank has judged it necessary to further support recent positive developments from the financial side and better ensure the economy's return to a moderate recovery path. For this purpose, the Bank has decided to clarify its monetary policy stance and to further enhance monetary easing at today's meeting in order to overcome deflation and achieve sustainable growth with price stability. The Bank will continue to pursue powerful monetary easing and will also engage in efforts to support strengthening the foundations for Japan's economic growth as a central bank.

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[9] In addition to purchases under the Program, the Bank regularly purchases Japanese government bonds at the pace of 21.6 trillion yen per year.

[10] Voting for the action: Mr. M. Shirakawa, Mr. H. Yamaguchi, Mr. K. G. Nishimura, Mr. S. Nakamura, Mr. H. Kamezaki, Mr. R. Miyao, Mr. Y. Morimoto, Ms. S. Shirai, and Mr. K. Ishida.
Voting against the action: None.

Meanwhile, the Bank will do its utmost to ensure that the European debt problem will not threaten the stable conditions in Japan's financial markets and, consequently, the financial system stability.

6. Japan's economy currently confronts the long-term and structural challenge of a declining trend in growth rates amid rapid population aging. Tackling such a challenge is indispensable in order to establish a new basis for economic growth. The goal of overcoming deflation will be achieved through such efforts to strengthen growth potential and support from the financial side. With this in mind, it is important for business firms, financial institutions, the government, and the central bank to continue making efforts in their respective roles.

Attachment 2

Increase in the Asset Purchase Program

1. Allocation of the increase

(trillion yen)

	Program size at the time of establishment	Program size before the increase	Amount of increase	Program size after the increase
Total size	**About 35**	**About 55**	**About +10**	**About 65**
Asset purchases	5.0	20.0	+10.0	30.0
Japanese government bonds[Note]	1.5	9.0	+10.0	19.0
Treasury discount bills	2.0	4.5	—	4.5
CP	0.5	2.1	—	2.1
Corporate bonds	0.5	2.9	—	2.9
Exchange-traded funds (ETFs)	0.45	1.4	—	1.4
Japan real estate investment trusts (J-REITs)	0.05	0.11	—	0.11
Fixed-rate funds-supplying operation against pooled collateral	30.0	35.0	—	35.0
Three-month term	20.0	20.0	—	20.0
Six-month term	10.0	15.0	—	15.0

Note: In addition to purchases under the Asset Purchase Program, the Bank regularly purchases Japanese government bonds at the pace of 21.6 trillion yen per year.

2. The Bank intends to complete the increased purchases by around the end of 2012.

Attachment 3

February 14, 2012

Bank of Japan

The Price Stability Goal in the Medium to Long Term

1. The Bank of Japan conducts monetary policy based on the principle that the policy shall be aimed at "achieving price stability, thereby, contributing to the sound development of the national economy." In doing so, price stability must be the one sustainable in the medium to long term.

2. At today's Monetary Policy Meeting, the Policy Board of the Bank introduced "the price stability goal in the medium to long term" as a part of its efforts to further clarify the determination to overcome deflation and achieve sustainable growth with price stability.

3. "The price stability goal in the medium to long term" is the inflation rate that the Bank judges to be consistent with price stability sustainable in the medium to long term. The Bank judges that "the price stability goal in the medium to long term" is in a positive range of 2 percent or lower in terms of the year-on-year rate of change in the consumer price index (CPI) and, more specifically, set a goal at 1 percent for the time being. Prior to today's introduction of the goal, the "understanding of medium- to long-term price stability" showed a range of inflation rates that each Policy Board member understood as price stability from a medium- to long-term viewpoint.

4. At today's meeting, the Board confirmed that the following elements of basic thinking about "price stability" agreed in the past, which form the basis of "the price stability goal in the medium to long term," were still relevant.

   (1) Conceptual definition: "Price stability" is a state where economic agents such as households and firms may make decisions regarding economic activities without being concerned about the fluctuations in the general price level.

   (2) Time frame: Price stability should be pursued over the medium to long term by making economic and price forecasts from a sufficiently long-term viewpoint.

   (3) Main indicator: The basic indicator for the evaluation of price developments is a price

index that covers goods and services consumed by households and which the public at large is accustomed to. In particular, the CPI is important in light of its favorable attributes including timeliness.

5. In expressing "the price stability goal in the medium to long term" in specific inflation rates, following the exercise in the past reviews, the Board examined the rate from three perspectives: measurement bias in a price index; the safety margin that acts as a buffer against the risk of a vicious cycle of deflation and stagnation; and the rate of inflation at which households and firms perceive price stability, i.e. the general public's perception of price developments. It also deems necessary to consider high uncertainty surrounding the future developments such as structural changes in Japan's economy and global economic environment. For this reason, the Board decided to express "the price stability goal in the medium to long term" in specific inflation rates by making some allowances as "a positive range of 2 percent or lower in terms of the year-on-year rate of change in the CPI." Within this range, the Board decided to set a goal at 1 percent for the time being to clarify the inflation rate which the Bank's monetary policy aims to achieve.

6. "The price stability goal in the medium to long term" will be reviewed once a year in principle.