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February 19, 2013

Bank of Japan

Minutes of the Monetary Policy Meeting

on January 21 and 22, 2013

(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, January 21, 2013, from 2:00 p.m. to 4:52 p.m., and on Tuesday, January 22, from 7:59 a.m. to 12:42 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. R. Miyao

Mr. Y. Morimoto

Ms. S. Shirai

Mr. K. Ishida

Mr. T. Sato

Mr. T. Kiuchi

Government Representatives Present

Mr. S. Yamaguchi, 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. A. Amari, Minister of State for Economic and Fiscal Policy, Cabinet Office[2]

Mr. Y. Nishimura, Senior Vice Minister, Cabinet Office[2]

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

Reporting Staff

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

Mr. H. Hayakawa, 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 February 13 and 14, 2013 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. S. Yamaguchi, A. Amari, and Y. Nishimura were present on January 22: for the whole of the session, from 10:55 a.m. to 12:42 p.m., and from 7:59 a.m. to 10:49 a.m., respectively.

[3] Messrs. S. Sato and K. Matsuyama were present on January 21.

Mr. N. Kinoshita, Executive Director

Mr. K. Momma, Executive Director

Mr. S. Uchida, Director-General, Monetary Affairs Department

Mr. T. Umemori, Director-General for Policy Infrastructure, 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. K. Kamada, Head of Economic Research Division, Research and Statistics Department

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

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

Mr. T. Kawamoto, Senior Economist, Monetary Affairs Department

[4] Messrs. T. Umemori and H. Kanno were present on January 22.

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 December 19 and 20, 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 around 0.075 to 0.085 percent.

With regard to the operation of the Asset Purchase Program, undersubscription had occurred frequently in the Bank's fixed-rate funds-supplying operation against pooled collateral, mainly in operations with relatively long maturities, as market participants shared the perception that there was an excess of liquidity in the money market and speculated that the interest rate applied under the complementary deposit facility might be lowered. As for the Bank's outright purchases of both Japanese government bonds (JGBs) and treasury discount bills (T-Bills), steady accumulation of the amount outstanding of these assets had progressed. Concurrently, the bid rates in these assets declined.

B. Recent Developments in Financial Markets

Money market rates, including longer-term ones, had been stable at low levels. General collateral (GC) repo rates had been at around 0.1 percent. As for interest rates on term instruments, yields on T-Bills including those with longer maturities had declined marginally, and had recently been at a level slightly below 0.1 percent. Rates on longer-term interbank instruments had declined very slightly.

With regard to long-term interest rates, yields on 2- and 5-year JGBs had declined marginally. Yields on 10-year JGBs temporarily rose to 0.80-0.85 percent, due in part to market concerns about deterioration in the supply and demand balance resulting from an increase to be made in the issuance of JGBs -- such as the increase that had been decided in the supplementary budget for fiscal 2012 -- as U.S. long-term interest rates had increased, mainly because the "fiscal cliff" had been avoided. However, these 10-year JGB yields had recently fallen to around 0.75 percent against the backdrop of solid demand from

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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.

investors. The Nikkei 225 Stock Average had risen mainly due to the depreciation of the yen, as U.S. and European stock prices had increased against the backdrop of the avoidance of the fiscal cliff, and had recently been in the range of 10,500-11,000 yen. Prices for Japan real estate investment trusts (J-REITs) had also been increasing. As for yield spreads between corporate bonds and JGBs, although those on some corporate bonds continued to be wide due to concerns over deterioration in issuer companies' business performance, those on other corporate bonds were more or less unchanged at low levels on the whole, reflecting continued solid demand from investors. The yen had depreciated against the U.S. dollar and temporarily entered the 90-91 yen range because of speculation about policies and expansion of Japan's trade deficit -- regarded as a reason to sell the yen -- while U.S. long-term interest rates rose.

C. Overseas Economic and Financial Developments

Overseas economies remained in a deceleration phase.

The U.S. economy generally continued to recover at a moderate pace, particularly in the household sector, although signs of weakness were observed in the corporate sector. The pace of growth in exports and production had slowed, and business sentiment continued to be cautious. Given these developments, business fixed investment had been relatively weak. In the household sector, on the other hand, while the balance-sheet repair weighing on the economy had gradually been mitigated and as the employment situation followed a modest improving trend, private consumption continued to increase moderately. Housing investment had also been showing clear signs of picking up, albeit at a depressed level. As for prices, the year-on-year rate of increase in the consumer price index (CPI) for all items decelerated, reflecting the decline in energy prices. However, the year-on-year rate of increase in the CPI for all items less food and energy, or the core CPI, had been more or less flat.

Economic activity in Europe had receded slowly. As a result of the weakening of sentiment and the effects of fiscal austerity, both business fixed investment and private consumption had been declining. Growth in exports was sluggish as well. Given these developments, production was decreasing. However, signs of a halt to a further deterioration in business sentiment had started to appear. As for prices, while slack in supply and demand conditions was exerting downward pressure on prices, the year-on-year rate of increase in the Harmonized Index of Consumer Prices (HICP) for all items decelerated somewhat, reflecting the decline in energy prices. Meanwhile, economic activity in the United Kingdom had been sluggish.

With regard to Asia, the Chinese economy remained in a state of slowdown, but had shown signs of stabilizing. Private consumption had been firm on the back of a favorable employment and income situation. The slowdown in the pace of increase in fixed asset investment had come to a halt due to rises in infrastructure investment and real estate investment. Under these circumstances, domestic demand as a whole had been firm. Exports, albeit with some fluctuations, had also shown signs of stabilizing. Reflecting these developments in demand at home and abroad, signs of stabilizing had been observed in production, although its growth momentum remained slow. Regarding the NIEs and the ASEAN countries, these economies had generally been picking up, but the pace continued to be moderate in the corporate sector. Exports and production had shown signs of stabilizing but remained relatively weak, and growth in business fixed investment, particularly in the NIEs, had been sluggish. On the other hand, private consumption had been firm, especially in the ASEAN countries. As for prices, in some of these Asian economies, there was still upward pressure on prices amid the continued wage inflation caused by tight labor market conditions, but inflation rates remained more or less flat. In India, the economy continued to be in a state of deceleration.

In global financial markets, investors' risk aversion had been abating, mainly on the back of the fact that (1) initiatives to overcome the European debt problem had been making some progress as seen in, for example, the agreement reached in establishing a single banking supervisory mechanism in Europe following the introduction of various safety valves -- such as the modalities by the European Central Bank (ECB) for undertaking Outright Monetary Transactions (OMTs) and the European Stability Mechanism (ESM) -- and (2) the fiscal cliff had been avoided in the United States. While yields on government bonds issued by some peripheral European countries had declined, interest rates in the United States and Germany had increased. Meanwhile, U.S. and European stock prices had been rising. With regard to corporate bond markets in the United States and Europe, credit spreads had generally narrowed, especially on corporate bonds with low ratings, and the issuance of high-yield bonds had increased. The funding conditions of European financial institutions had recently been even more stable. Spreads between interest rates on euro-denominated term instruments and overnight index swap (OIS) rates had also remained flat at low levels. Meanwhile, in emerging and commodity-exporting economies, stock prices had been firm in a situation where capital inflow into these economies -- through investment funds in particular -- had been showing signs of an increase, and a growing number of currencies had been appreciating in the foreign exchange markets.

D. Economic and Financial Developments in Japan

1. Economic developments

Exports and industrial production had decreased, mainly due to the fact that overseas economies remained in a deceleration phase. Real exports had declined significantly in the October-November period relative to the July-September quarter of 2012, after having registered a large quarter-on-quarter decrease. Industrial production continued to move down in the October-November period relative to the July-September quarter, after having declined for two quarters in a row since the April-June quarter. The pace of decline, however, had moderated slightly, as the effects of the decline in car sales due to the ending of some measures to stimulate demand for automobiles had diminished. Exports were expected to start picking up as overseas economies gradually emerged from the deceleration phase. Industrial production was also expected to start picking up, in line with the improvements in exports, as domestic demand remained resilient, partly due to the effects of various economic measures. Judging from interviews with firms and other relevant information, industrial production as a whole for the January-March quarter of 2013 was projected to be more or less flat, in view of expectations for the production of transport equipment to turn markedly upward and that of general machinery to decrease at a reduced pace.

Public investment continued to increase, primarily in that related to reconstruction following the earthquake disaster. It was expected to continue trending upward, supported by the effects of various economic measures. However, due to the effects of bottlenecks on the supply side, such as a labor shortage in the construction industry, attention should be paid to the risk of a delay in the progress of public works.

Business fixed investment had shown some weakness on the whole, as that in manufacturing had declined due to the drop in exports and industrial production, although resilience had been observed in nonmanufacturing. With regard to machinery orders, those in manufacturing continued to fall in the October-November period relative to the July-September quarter of 2012, after having declined for two quarters in a row since the April-June quarter, whereas those in nonmanufacturing increased in the October-November period relative to the July-September quarter, after having been more or less level in the April-June and July-September quarters. Business fixed investment was projected to remain relatively weak for the time being, mainly in manufacturing, but to follow a moderate increasing trend thereafter, partly due to investment related to disaster prevention and energy.

The employment and income situation continued to be severe and the improvement in supply and demand conditions in the labor market had peaked out.

Private consumption remained resilient and the effects of the decline in car sales due to the ending of some measures to stimulate demand for automobiles had diminished. The number of new passenger-car registrations, including those for small cars with engine sizes of 660 cc or less, fell back significantly through October but picked up thereafter for two consecutive months, in November and December. Sales at department stores and supermarkets climbed in October and November, notably in apparel, as a result of lower temperatures. Private consumption was expected to remain resilient as a trend, with the effects of the decline in car sales continuing to diminish.

Housing investment had generally been picking up, supported in part by reconstruction of disaster-stricken homes, and was expected to continue to do so.

As for prices, international commodity prices had been more or less level. The three-month rate of change in the domestic corporate goods price index (CGPI) had been more or less flat. The CGPI was expected to move slightly upward for the time being, reflecting movements in foreign exchange rates. The year-on-year rate of change in the CPI (all items less fresh food) was currently around 0 percent. For the time being, it was expected to be around minus 0.5 percent due to the reversal of the previous year's movements in energy-related and durable consumer goods, and thereafter was likely to be around 0 percent again.

2. Financial environment

Financial conditions were accommodative.

The overnight call rate remained at an extremely low level, and firms' funding costs had been hovering at low levels. With regard to credit supply, firms continued to see financial institutions' lending attitudes as being on an improving trend. Issuing conditions for CP and corporate bonds remained favorable on the whole as demand from investors continued to be solid, although some firms inevitably faced difficulty in issuing corporate bonds and were experiencing a widening of issuance spreads on CP, mainly due to deterioration in business performance. 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 change in the amount outstanding of bank lending had been positive. The year-on-year rate of change in the amount outstanding of corporate bonds had turned positive, whereas that of CP had been negative. 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, within the range of 2-3 percent.

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

A. Economic Developments

In terms of <u>global financial markets</u>, members agreed that, although developments required continued attention, investors' risk aversion had been abating, mainly on the back of the fact that (1) initiatives to overcome the European debt problem had been making some progress as seen in, for example, the agreement reached in establishing a single banking supervisory mechanism in Europe following the introduction of various safety valves -- such as the modalities by the ECB for undertaking OMTs and the ESM -- and (2) the fiscal cliff had been avoided in the United States.

Members concurred that <u>overseas economies</u> as a whole remained in a deceleration phase as economic activity in Europe continued to recede slowly, although some positive developments had been observed in parts of the U.S. and Chinese economies. As for the outlook, they shared the recognition that overseas economies were likely to remain in the deceleration phase for the time being but gradually emerge from the phase and turn to a moderate recovery thereafter, on the assumption that global financial markets would remain stable on the whole.

Members shared the recognition that the U.S. economy generally continued to recover at a moderate pace, particularly in the household sector, although signs of weakness were observed in the corporate sector. Most members expressed the view that the avoidance of the fiscal cliff had reduced the downside risks to the U.S. economy, and consequently to the global economy. Furthermore, many members noted that housing investment had been showing clear signs of picking up. Some members said that signs of recovery were also observed, for example, in exports, production, and business fixed investment. As for the outlook, members concurred that the U.S. economy was likely to continue recovering at a moderate pace, supported by accommodative financial conditions. Some members commented that the effects of such factors as the expiration of the payroll tax cut and future developments related to the debt ceiling problem would warrant attention. One member noted that attention should also be paid to the fact that indicators for sentiment had recently been deteriorating.

Members shared the recognition that economic activity in the euro area had receded slowly. A few members pointed out that the negative effects had been spreading even to core countries such as Germany. As for the outlook, members shared the view that the euro area economy would likely still lack momentum for recovery on the whole as fiscal austerity measures would continue to be implemented for the time being, particularly in peripheral countries.

Most members shared the recognition that the Chinese economy remained in a state of slowdown, but had shown signs of stabilizing. Some members noted that positive signs had begun to be observed mainly in exports and fixed asset investment in a situation where private consumption had been firm. As for the outlook, most members shared the view that the economy would register higher growth gradually. One of these members expressed the view that, although there was a possibility that the Chinese economy would not succeed in making a smooth transition to stable growth, it would likely continue to post relatively high growth at least during 2013, which would push Japan's economic growth rate upward. A different member took the view that the pace of recovery in the Chinese economy was quite slow compared to the projection made in autumn 2012, when signs of recovery began to be observed, and its growth pace would remain moderate since it was expected that the Chinese government would implement tightening measures due to concerns about, for example, overheating in the real estate market.

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

Members agreed that the economy remained relatively weak, as exports and industrial production had decreased -- mainly due to the fact that overseas economies remained in a deceleration phase -- and as business fixed investment had shown some weakness on the whole. Many members expressed the view that public investment continued to increase, housing investment had generally been picking up, and private consumption remained resilient. Members shared the recognition that the effects of the decline in domestic car sales due to the ending of some measures to stimulate demand for automobiles had diminished. Some members said that there were signs that the decrease in industrial production was coming to a halt as seen in, for example, a rise in the production forecast index for two consecutive months, in December 2012 and January 2013. Some members pointed out that the recent correction in the yen's appreciation and the rise in stock prices had contributed to the pick-up in business sentiment. One member said that the recession since April 2012 might have been only an eight-month "mini-recession" that reached a bottom in November. A different member expressed the view that attention should be paid to the point that consumer sentiment had been deteriorating recently in a situation where winter bonus payments had declined, and non-scheduled hours worked and the number of new job openings in manufacturing had decreased.

As for the outlook for the economy, members shared the recognition that it was likely to level off more or less for the time being, and thereafter return to a moderate recovery path as domestic demand remained resilient, partly due to the effects of various economic measures, and as overseas economies gradually emerged from the deceleration phase. Some members were of the view that the possibility of Japan's economy returning to a moderate recovery path had heightened to a considerable degree, taking into account that (1) tail risks surrounding overseas economies had decreased and (2) the effects of the government's emergency economic measures, the depreciation of the yen, and the rise in stock prices would become apparent. A few of these members expressed the view that signs of recovery were likely to become evident from around spring 2013. On the other hand, one member expressed the opinion that there was still concern regarding whether the signs of stabilization seen in, for example, industrial production would continue to be seen, since the decreasing trend in exports had not come to a clear halt, and therefore it was difficult to judge that the path to recovery was in sight.

Regarding prices, members agreed that the year-on-year rate of change in the CPI (all items less fresh food) was currently around 0 percent. They continued that, for the time being, it was likely to turn negative due to the reversal of the previous year's movements in energy-related and durable consumer goods, and thereafter was likely to be around 0 percent again. A few members expressed the recognition that factors including the materialization of the effects of (1) the economic slowdown in the latter half of 2012 and (2) a subsequent sluggishness in wages could also exert downward pressure on prices for the time being. One of these members said that it was possible that the year-on-year rate of decline in the CPI (all items less fresh food) might temporarily register around 0.5 percent due to the fact that in the previous year (1) the prices of petroleum products had risen, reflecting developments in international commodity prices; and (2) the prices of durable consumer goods in the CPI basket such as air conditioners and televisions had gone up due to the switch in the survey specifications. A few members expressed the view that, thereafter, the year-on-year rate of change in the CPI was likely to start rising as the aggregate supply and demand balance improved. A few other members said that, if the recent trend of the yen's depreciation continued, this could be expected to have positive effects on prices through an improvement in economic activity and a rise in inflation expectations. One member expressed the view that the effects of the yen's depreciation in boosting prices were not particularly significant; therefore, attention should instead be paid to the possibility that a significant weakening in prices for the time being could exert downward pressure on firms' and households' inflation expectations.

B. Financial Developments

Members concurred that financial conditions in Japan were accommodative.

Members agreed that money market rates, including interest rates on term instruments, had been extremely stable, as the Bank had been pursuing powerful monetary easing and the soundness of financial institutions' balance sheets had been maintained. While noting that bank lending rates remained at low levels, they shared the recognition that indicators related to financial institutions' lending attitudes as perceived by firms, as well as to the financial positions of firms, remained at improved levels -- exceeding the average for the period since 2000. Members shared the view that issuing conditions for CP and corporate bonds remained favorable on the whole, as demand from investors continued to be solid.

C. Interim Assessment

Given the above assessment of recent developments, members shared the view that, compared with the forecasts in the baseline scenario presented in the October 2012 *Outlook for Economic Activity and Prices* (hereafter the Outlook Report), the forecasts of economic growth would likely be somewhat lower for fiscal 2012, but higher for fiscal 2013, partly due to the effects of various economic measures, and broadly in line with the October forecasts for fiscal 2014. Many members explained that they had raised their outlook because they had partially incorporated into the main scenario the fact that the yen was depreciating and stock prices were rising as efforts by a wide range of entities toward strengthening the growth potential of Japan's economy were likely to make progress. One of these members said that (1) the potential growth rate was likely to gradually increase from around 0.5 percent at present to the 0.5-1.0 percent range over the next few years; and (2) firms' expectations for economic growth were likely to increase over the projection period -- which covered fiscal 2012 through 2014 -- reflecting, somewhat in advance, the gradual increase in the potential growth rate. A different member expressed the view that, from the latter half of 2013, it was likely that the U.S. economy would recover at a faster pace than had been expected.

With regard to the forecasts of prices in the baseline scenario, members shared the view that the forecasts for the year-on-year rate of change in the CPI (all items less fresh food) were basically unchanged from those presented in the October 2012 Outlook Report. They shared the recognition that the basic mechanism, which formed the basis of this outlook, had not changed from that in October: namely, that the inflation rate would gradually rise as Japan's economy grew at a pace above its potential and the aggregate supply and demand balance improved through fiscal 2014 and, accordingly, the expected inflation rates of firms and households were likely to rise moderately. Many members expressed the view that the year-on-year rate of change in the CPI would move closer to 1 percent toward the end of the projection period -- namely, through fiscal 2014. A few members said that it was likely to rise above 1 percent after the projection period -- fiscal 2015 or thereafter -- as the growth potential of Japan's economy strengthened, owing partly to efforts by the government. One member expressed the view that, as efforts by a wide range of entities toward strengthening competitiveness of Japan's economy made actual progress, thereby raising firms' profitability as well as productivity, firms' and households' expectations for future income would improve, and this might eventually generate a desirable inflation in which an improvement in the pricing power of firms and a continuous increase in wages would occur simultaneously. A different member noted that, with regard to the median of the Policy Board members' forecasts, it appeared likely that the majority of the members had assumed that the responsiveness of prices to the aggregate supply and demand balance had lessened, considering that the forecasts for CPI remained almost unchanged while those for economic growth on the whole were higher than in October. In response, a few members said that they were expecting the inflation rate to rise beyond the projection period, and therefore price responsiveness had not necessarily lessened when taking into consideration a longer period. One member noted that the change in the outlook for the price situation was evident in the forecast distribution chart for prices, in which the possibility of deviating downward had decreased compared with the October 2012 Outlook Report, while the possibility of deviating upward had increased. A different member expressed the recognition that the structural reforms laid out by the government would affect the inflation rate after a considerable lag, through an improvement in economic activity. This member continued that it was therefore increasingly important to hold discussions with a longer-term perspective.

In terms of the economic outlook, members noted the following upside and downside risk factors: (1) developments in global financial markets and overseas economies; (2) uncertainty with regard to firms' and households' medium- to long-term growth expectations; (3) uncertainty with regard to the effect of the consumption tax hike; and (4) various problems regarding Japan's fiscal sustainability. They shared the recognition that the first risk factor -- namely, risks regarding developments in global financial markets and overseas economies -- warranted particular attention. On this point, members concurred that a high degree of uncertainty remained concerning Japan's economy, including the prospects for the European debt problem, the momentum toward recovery for the U.S. economy, the possibility of emerging and commodity-exporting economies making a smooth transition to the sustainable growth path, and the effects of the recent developments in the relations between Japan and China. One member commented that attention should be paid to the fact that, if U.S. long-term interest rates rose, mainly reflecting speculation about monetary policy in the United States, then Japanese long-term interest rates would likely be subject to upward pressure. A different member noted that, as short-term capital inflow into Asian emerging economies was being observed, there was growing risk that such capital inflow could unwind. Members shared the view that the following were upside and downside risk factors specific to the outlook for prices: (1) uncertainty associated with the responsiveness of prices to the aggregate supply and demand balance; (2) developments in firms' and households' medium- to long-term inflation expectations; and (3) developments in import prices. One member commented that the effects on prices of developments in the so-called shale revolution in the United States also warranted attention. A different member expressed the opinion that, if developments such as the moderate rises in the potential growth rate and expected inflation rates brought about by progress in efforts to strengthen the growth potential of Japan's economy did not proceed as anticipated, this could become a downside risk factor for economic activity and prices. Another member said that uncertainty with regard to the outlook for economic activity and prices for fiscal 2013 and 2014 was considerably greater than that in previous projections. Most members shared the recognition that upside and downside risks to the outlook were generally balanced. Meanwhile, one member expressed the view that the member was giving attention to downside risks in terms of both economic activity and prices, while a different member expressed the view that this member was doing so only in terms of prices.

III. Summary of Staff Reports and Discussions by the Policy Board on the Review of "Price Stability"

A. Staff Reports

The staff reported the following in response to the chairman's instruction at the Monetary Policy Meeting held on December 19 and 20, 2012 to examine necessary issues concerning "price stability."

First, there was the issue of what the term "price stability" represented. The Bank of Japan Act stipulated that the Bank should conduct monetary policy based on the principle that monetary policy was aimed at "achieving price stability, thereby contributing to the sound development of the national economy." According to the Bank's *Opinion Survey on the General Public's Views and Behavior,* approximately 80 percent of the respondents -- irrespective of sex or age -- consistently viewed a price rise as "rather unfavorable." This suggested that for the general public "price stability" was not a situation in which prices simply rose but an environment where the economy improved in a balanced manner, accompanied by a recovery in employment, wages, and corporate profits, and consequently it led to moderate inflation.

Second, there was the issue of how "price stability" could be defined in numerical terms. In expressing "price stability" as a numerical value, three perspectives should continue to be taken into consideration: (1) the measurement bias in the price index; (2) the safety margin that acted as a buffer against the risk of a vicious cycle of declining prices and deteriorating economic activity; and (3) the general public's perception of price developments under which households and firms perceived "price stability." In relation to these perspectives, the following respective points were considered to be applicable: (1) regarding the CPI in Japan, the extent to which the measurement bias had to be taken into consideration appeared to be small on the whole; (2) in order to ensure a somewhat higher nominal interest rate in the medium to long term in a situation where the real GDP growth rate per capita was declining, it was deemed appropriate to allow some safety margin; and (3) it was highly likely that the inflation rate at which the general public perceived price stability had been low in Japan, as the inflation rate had been lower than those in major economies overseas for a number of years. These points regarding the three perspectives had not changed materially from those in the past.

Third, there was the issue of how the mechanism of rising inflation that would achieve "price stability" would work. Since the 1990s, Japan had been facing a chronic shortage of demand, reflecting the fact that its economic growth rate had declined as a trend mainly due to (1) balance-sheet adjustments following the bursting of the bubbles; and (2) a delay in adjusting Japan's economic structure in response to changes in the environment surrounding its economy, such as the progressive aging of the population and increasing globalization. Under these circumstances, firms' growth expectations in the medium to long term had shown a trend decline, and this had caused the actual inflation rate to fall, which also partly reflected Japanese firms' behavioral tendencies to reduce wages and engage in price competition. These falls in the actual inflation rate had exerted downward pressure on expected medium- to long-term inflation rates. Considering these developments, in order for Japan's economy to overcome deflation as early as possible and return to a sustainable growth path with price stability under the constraints of the zero lower-bound on the nominal policy interest rate, it was vital to improve the aggregate supply and demand balance by strengthening the economy's growth potential concurrently with support from the financial side.

B. Discussions by the Policy Board

Based on the above staff reports, members discussed the "price stability" that the Bank aimed to achieve in the conduct of monetary policy.

With regard to the interpretation of "price stability," members shared the recognition that, in view of the principle of the conduct of monetary policy, stipulated in the Bank of Japan Act, that monetary policy should be aimed at "achieving price stability, thereby contributing to the sound development of the national economy," "price stability" must be achieved on a sustainable basis. Some members expressed the view that, as in the past, such "price stability" was defined conceptually as a state where various economic agents including households and firms would be able to make decisions regarding such economic activities as consumption and investments without being concerned about the fluctuations in the general price level.

Members shared the recognition that, in order to achieve this "price stability," it was necessary for the Bank to conduct monetary policy flexibly by examining various risk factors, including those related to financial imbalances, while taking into account that the effects of monetary policy permeating economic activity, and thereafter prices, required a considerable and variable time lag.

Members concurred that, in formulating a numerical expression for sustainable "price stability," the three perspectives should be taken into consideration: (1) the measurement bias; (2) the safety margin; and (3) the general public's perception of price developments. They then shared the recognition that the result of the review based on these perspectives had not changed materially. Regarding the point that the Bank judged the "price stability goal in the medium to long term" to be in a positive range of 2 percent or lower in terms of the year-on-year rate of change in the CPI, and that it set a goal of 1 percent for the time being, a few members expressed the view that the year-on-year rate of change in the CPI would likely move much closer to 1 percent -- equivalent to the Bank's goal for the time being -- during the projection period, and therefore it was necessary at this time to present the specific level of inflation that the Bank considered as sustainable "price stability" after the projection period. Many members -- referring to the fact that the government had shown its intention to aggressively pursue steps for strengthening the competitiveness and growth potential of Japan's economy -- expressed the opinion that, as such steps made progress, the actual rate of inflation would be expected to rise and, accordingly, the inflation rate at which the general public perceived price stability would be likely to rise as well. A few members said that the level of inflation rate that the Bank should aim for over the medium to long term was likely to be higher than 1 percent, in view of the need for the safety margin, taking into account the zero lower-bound on nominal interest rates. A few other members were of the opinion that, if the Bank were to aim for an inflation rate of 2 percent -- the level other advanced economies aimed to achieve -- this would contribute to maintaining a balance in currency values from a long-term perspective. Based on this discussion, most members expressed the view that it was desirable to designate the specific numerical expression for price stability as 2 percent in terms of the year-on-year rate of change in the CPI.

Members also discussed what the Bank ought to call the inflation rate that was consistent with "price stability" on a sustainable basis. On this point, many members expressed the view that, when the "price stability goal in the medium to long term" had been introduced in February 2012, there had been concern regarding the possibility that, if the term "target" were used, it might be construed as meaning rigidly conducting monetary policy, with only price developments taken into account. However, these members continued that, owing in part to the Bank's subsequent communication, awareness of the importance of flexibility in the conduct of monetary policy was spreading steadily. Based on this situation, members concurred that using the expression of "price stability target" as a replacement for "price stability goal" was a transparent and appropriate way to explain the Bank's thinking on price stability.

Meanwhile, a few members expressed the opinion that, while agreeing to use the expression of "price stability target" as a replacement for "price stability goal," it was appropriate for the Bank to maintain the numerical expression of "in a positive range of 2 percent or lower in terms of the year-on-year rate of change in the CPI and 1 percent for the time being," and commit to do its utmost to achieve the target. These members explained their reasoning as follows. First, 2 percent in terms of the year-on-year rate of change in the CPI had rarely been achieved in the past two decades, and based on the general public's current perception of price developments that was built on such past experience, the 2 percent inflation rate was considerably higher than the inflation rate that was considered at this point to be consistent with sustainable price stability. Second, this suggested that, even if the central bank were to set 2 percent inflation as a target, this alone was highly unlikely to substantially influence inflation expectations, and thus it was unreasonable to conduct monetary policy with the aim of achieving such an ambitious target. Third, efforts by a wide range of entities toward strengthening the growth potential of Japan's economy were essential in order to achieve the 2 percent target, but if the 2 percent target were set before such efforts made progress and the effects of these efforts were confirmed, this could impair the credibility of monetary policy or disturb communication with financial markets due to considerable uncertainty regarding achievement of the target. In response, some members, while concurring that there would be difficulty in achieving 2 percent inflation if the current situation were taken as a premise, expressed the view that it was meaningful to review the numerical expression at this time because clarification of the stance that policy authorities would work together -- specifically, that the Bank would pursue monetary easing with the aim of achieving 2 percent inflation while the government aggressively pursued steps for strengthening the competitiveness and growth potential of the economy -- would likely be effective in terms of exerting influence on firms' and households' inflation expectations. One of these members said that the optimal inflation rate should be considered by taking into account the future developments in economic activity and prices without depending too much on the general public's current perception of price developments. A different member added that it was implausible to assume that the low inflation expectations currently held by the general public that were based on past low inflation rates would not change. This member continued that various studies suggested that a considerable proportion of people formed their inflation expectations by factoring in the future polices and resultant changes in economic conditions, and therefore it was reasonable to try to exert influence on the formation of expectations of those who had such a tendency.

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

Based on the above discussion on economic and price developments, as well as "price stability," members shared the recognition that it was necessary at this time to take additional steps to provide monetary accommodation decisively in order for Japan's economy to overcome deflation as early as possible and return to a sustainable growth path with price stability under the Bank's mission stipulated in the Bank of Japan Act. On this basis, members discussed monetary policy for the immediate future in detail.

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.

With regard to the operation of the Asset Purchase Program (hereafter the Program), members shared the recognition that, with a view to clearly presenting the Bank's stance of pursuing aggressive monetary easing -- aiming to achieve the "price stability target" -- it was desirable to introduce a method to continue purchasing a certain amount of financial assets every month without setting any termination date.

On this basis, the chairman requested that the staff explain whether this open-ended asset purchasing method was feasible, particularly in terms of the following points: (1) the relationship between the amount of monthly purchases and the total size of the Program; and (2) the room left for additional purchases of the respective financial assets in view of the Bank's risk tolerance and the market size of these assets. The staff provided the following explanation.

(1) As for the relationship between the amount of monthly purchases and the total size of the Program, assuming, for example, that every month the Bank purchased 2 trillion yen of JGBs with the same remaining maturities as those purchased recently, the amount outstanding of JGBs purchased under the Program would reach 48 trillion yen after a certain period of time and be maintained at that level. Likewise, the amount outstanding of T-Bills would reach 30 trillion yen, assuming that the Bank purchased 10 trillion yen of them every month. As for CP and corporate bonds, assuming that the Bank purchased 1 trillion yen of them every month, the amounts outstanding of these assets would essentially be maintained. To sum up, assuming, for example, that the Bank purchased 2 trillion yen of JGBs, 10 trillion yen of T-Bills, and 1 trillion yen of

CP and corporate bonds -- thus totaling 13 trillion yen -- the total size of the overall Program would be maintained at a level that was about 10 trillion yen higher than at present. It must be noted, however, that the level would fluctuate somewhat depending on the remaining maturities of financial assets purchased.

(2) The Bank would be able to make these purchases given the stock and flow -- the amount outstanding in the markets and the amount of issuance -- of each type of financial asset. Moreover, the amount of risk incurred by an increase in the total size of the Program could be absorbed by the Bank's capital.

In response to this explanation, members discussed the specifics of the open-ended asset purchasing method. They concurred that, after completing the current purchasing method at end-2013, it was appropriate from January 2014 to introduce a method to continue purchasing a certain amount of financial assets every month without setting any termination date. One of these members said that, while it was possible to propose the immediate introduction of the new asset purchasing method at this meeting, the member would prefer to give priority to delivering a clear message that represented the consensus of the Bank's Policy Board. Members also shared the recognition that, in 2014, when the year-on-year rate of change in the CPI was likely to increase to 1 percent, it was appropriate -- from the viewpoint of steadily implementing monetary policy in a continuous manner with the aim of achieving the 2 percent "target" -- to purchase financial assets totaling about 13 trillion yen per month for some time, in order to increase the total size of the Program by about 10 trillion yen and maintain it at that level. This 13 trillion yen corresponded to purchases of 2 trillion yen of JGBs, 10 trillion yen of T-Bills, and 1 trillion yen of CP and corporate bonds. A few members noted that, as it was likely to take considerable time before the "price stability target" was achieved, and given, for example, that economic and price developments as well as the effects of cumulative monetary easing were likely to become increasingly uncertain with the passage of time, purchasing a certain amount of financial assets every month for some time without setting any termination date would clearly represent the Bank's monetary easing stance. A few members pointed out that an increase in purchases of T-Bills was also important from the viewpoint of exerting influence on the foreign exchange market through a decline in yields in the short term. Meanwhile, a few members said that one option, for example, was to extend the remaining maturity of JGBs to be purchased under the Program up to around five years.

As for the term to pursue aggressive monetary easing through the continuation of purchases of financial assets and a virtually zero interest rate policy, many members expressed the view that it was appropriate for the Bank to continue with each respective policy measure as long as it judged appropriate, with the aim of achieving the "price stability target" at the earliest possible time. In response, a few members said that, at present, they were against setting the "price stability target" at 2 percent in terms of the year-on-year rate of change in the CPI, and thus were also against linking to the target a period during which purchases of financial assets and the virtually zero interest rate policy would be continued. These members expressed the view that it was appropriate at present to pursue a year-on-year rate of increase in the CPI of 1 percent for the time being, and that in doing so, it was desirable to clearly present that the Bank had no policy intention to prematurely withdraw the monetary easing measures before the rate of increase reached 1 percent. One member -- while noting that one possibility would be to extend the Bank's projection period by one year, and continue with the virtually zero interest rate policy and the open-ended asset purchasing method until the median of the Policy Board members' CPI forecasts for the extended projection period exceeded 1.5 percent -- said that, at this meeting, the member would follow the majority view of the Policy Board. A different member was of the view that the virtually zero interest rate policy was an orthodox measure to strengthen monetary easing by influencing market expectations on future short-term interest rates, and that the degree of experience gained from this policy in terms of its effects, including side effects, had differed from that gleaned from purchases of financial assets. The member continued that it therefore was appropriate to continue with the virtually zero interest rate policy, thereby demonstrating the Bank's firmer determination, until the Bank judged that 2 percent in terms of the year-on-year rate of increase in the CPI was in sight. In response, one member expressed the view that emphasizing the difference between the effects, including side effects, of the virtually zero interest rate policy and purchases of financial assets might entail a risk of reducing the policy duration effects, which were strong at present. A different member said that the guidance for the future conduct of monetary policy should fully take into account the high uncertainties regarding (1) future economic and price developments, as well as (2) the effects of cumulative monetary easing. Members, noting that the Bank of Japan Act stipulated the principle that monetary policy should be aimed at "achieving price stability, thereby contributing to the sound development of the national economy," shared the recognition that therefore -- regardless of how the Bank might present its future monetary policy stance -- it was necessary under this principle to ascertain whether there was any significant risk to the sustainability of economic growth, including from the accumulation of financial imbalances, taking into consideration that it took considerable time before the effects of monetary policy permeated the economy.

Regarding the policy coordination between the government and the Bank for the purpose of overcoming deflation and achieving sustainable economic growth, the chairman proposed the following.

(1) The Bank had been pursuing powerful monetary easing, and in order for this easing to lead to overcoming deflation early and achieving sustainable economic growth with price stability, it was important that firms and households make use of the accommodative financial conditions in a more vigorous manner and produce positive efforts, thereby encouraging further permeation of monetary easing effects through economic activity. If such a situation materialized, the effects of monetary easing would be maximized. Therefore, the role of the government was important in creating a more favorable environment to this end. On this point, the new administration indicated its stance to formulate measures for strengthening the competitiveness and growth potential of Japan's economy and to promote them strongly, and the Bank expected that the government would surely implement such measures.

(2) Under the "price stability target," which was to be introduced, the Bank would pursue monetary easing and aim to achieve this target at the earliest possible time. The Bank, under its virtually zero interest rate policy, had been conducting large-scale purchases of government securities in order to further pursue monetary easing, and the amount of such purchases would be increased further. It was becoming increasingly important to ensure that the public did not perceive such purchases of government securities as having been conducted for the purpose of monetization.

(3) Taking into account this situation, although the government and the Bank had always maintained a close dialogue, for the Bank to fulfill its mission, namely, "achieving price stability, thereby contributing to the sound development of the national economy," it was important at this time to clearly acknowledge each other's roles and strengthen their policy coordination, and to indicate this intention to the public in the form of a joint

statement. By doing so, it would be possible to further enhance policy effects. It appeared that the Bank shared with the government recognition of the importance of strengthening their policy coordination while the Bank conducted monetary policy based on its own judgment and responsibility.

(4) As for the specifics of the joint statement, the Bank's staff had made a draft with the government, on which basis discussion would be requested.

In response to the proposal, members discussed the release of the "Joint Statement of the Government and the Bank of Japan on Overcoming Deflation and Achieving Sustainable Economic Growth." They concurred that it was significant that the government and the Bank would strengthen their coordination in order to overcome deflation and achieve sustainable economic growth. Most members pointed to the fact that Japan's economy had recently shown signs of a pick-up and was in an important phase of returning to a moderate recovery path, and that the government had announced that it would formulate measures for strengthening the growth potential of Japan's economy and promote them strongly. These members expressed the opinion that, taking account of such factors, it was extremely important that the government and the Bank -- in supporting Japan's economic recovery -- clearly indicate to the public their stance at this time that they would strengthen their coordination and work together. One of these members expressed the view that, in deciding on the joint statement, it was essential to ensure the proper balance between the Bank's independent role and the importance of exchanging views with the government -- both of which were stipulated in the Bank of Japan Act. This member continued that the joint statement under discussion at this meeting provided such a balance. On this basis, this member acknowledged that the government respected the Bank's independence, especially since in the joint statement (1) the wording "policy coordination" was being used, and (2) it was stated that the Bank was responsible for the specifics of the conduct of monetary policy. Some members said that it was also important that the government firmly ensure the credibility of fiscal management in proceeding with coordination. A few other members expressed the view that it was unsure whether the government and the Bank sufficiently shared a common understanding regarding the challenge Japan's economy faced, and therefore some more time should be devoted to deliberating on the desirable policy coordination. One of these members said that it was necessary to face the hard reality that, in order to achieve a steady inflation rate of 2 percent in a situation where the labor force was declining by 0.6 percent on an annual basis, a significant rise in productivity was required. Another member expressed the view that, if it was not clearly stated in the joint statement that the government would share responsibility with the Bank to achieve the 2 percent target in terms of the year-on-year rate of change in the CPI, the effectiveness of exerting influence on firms' and households' inflation expectations might be limited.

V. Remarks by Government Representatives

The representative from the Cabinet Office made the following remarks.

(1) The government was satisfied with the draft of the joint statement, and planned to formally announce the statement at a press conference by the Prime Minister, which was to be held in the afternoon on January 22, 2013.

(2) The Japanese economy had shown weakness recently due to deceleration of the world economy, and due attention should be paid to downside risks such as developments in overseas economies. Recent price developments indicated that the economy remained in a mild deflationary situation. Meanwhile, since the inauguration of the Second Abe Cabinet at end-2012, correction of the yen's appreciation and an upturn in stock prices had been observed in expectation of an economic recovery. The government needed to ensure that these signs of improvement led to realizing economic recovery via appropriate policy management.

(3) Based on this recognition, the government would aim to overcome the prolonged appreciation of the yen and deflationary recession as well as increase employment and income, in order to revitalize the economy, by adopting a three-pronged strategy consisting of bold monetary policy, flexible fiscal policy, and a growth strategy that promoted private investment. As the first step toward this end, the government had recently released the "Emergency Economic Measures for the Revitalization of the Japanese Economy." Through these measures, the government would avoid a further deterioration of the economy and make a transition to a growth strategy that would generate sustainable growth.

(4) The joint statement, which was to be agreed on January 22, could be regarded as representing a "regime change," in that it indicated a strong determination and clear commitment to overcoming deflation at the earliest possible time. The government

strongly expected that this new framework would facilitate the elimination of deflationary expectations. As noted in the joint statement, the government would formulate measures for strengthening the competitiveness and growth potential of the Japanese economy and promote them strongly, while working to ensure the credibility of fiscal management.

(5) According to the Bank's interim assessment of the October 2012 Outlook Report, its projections for the year-on-year rate of change in the CPI for fiscal 2013 and fiscal 2014 were 0.4 percent and 0.9 percent, respectively, which were below the "price stability target" of 2 percent to be introduced at this meeting. The government strongly expected the Bank to pursue bold monetary easing in order to achieve the target at the earliest possible time.

(6) The Council on Economic and Fiscal Policy would regularly review the progress in the conduct of macroeconomic policies, including monetary policy, and the current condition and future prospects of prices in the context of the "price stability target" under the policies. The government would like the Bank to effectively utilize the meetings of the Council and maintain accountability to the public.

(7) The government deemed the proposal made at this meeting to introduce the open-ended asset purchasing method to be a timely action, as it would enable the Bank to continuing purchasing financial assets with the aim of achieving the "price stability target." The government strongly expected the Bank to pursue bold monetary easing in order to achieve the target of 2 percent.

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

(1) The Japanese economy had shown weakness due to the yen's appreciation and deceleration of the world economy. High uncertainty about the prospects for overseas economies posed downside risks to the Japanese economy. Since the inauguration of the new Cabinet, correction of the yen's appreciation and an upturn in stock prices had been observed. The government deemed it important to ensure that these developments led to the realization of economic recovery via appropriate policy management.

(2) The government would aim to overcome the prolonged appreciation of the yen and deflationary recession as well as increase employment and income by adopting the

aforementioned three-pronged strategy. The Cabinet had recently formulated the "Emergency Economic Measures for the Revitalization of the Japanese Economy," and decided a supplementary budget for fiscal 2012. It would put forth efforts to submit the supplementary budget to the Diet.

(3) In the "Joint Statement of the Government and the Bank of Japan on Overcoming Deflation and Achieving Sustainable Economic Growth," the Bank would set the "price stability target" at 2 percent for the first time and present its determination to achieve this target at the earliest possible time. The government welcomed this joint statement, which would represent a major review of the Bank's monetary policy framework.

(4) At this meeting, the Bank also proposed the introduction of a monetary easing measure -- namely, the open-ended asset purchasing method. The government welcomed this measure as it underpinned the Bank's strong determination to achieve the "price stability target" at the earliest possible time.

(5) Given that a bold monetary policy was expected to eliminate deflationary expectations and generate positive effects through the foreign exchange markets, the government deemed that this comprised the most important area of the three-pronged strategy. The government would implement the other two strategies: a flexible fiscal policy and a growth strategy that promoted private investment. Through these strategies, it would aim to generate actual demand in the Japanese economy and a virtuous cycle in which stimulated corporate activity would lead to increases in employment and income. The government deemed that these efforts, together with the Bank's monetary easing, would result in overcoming the deflationary recession and achieving sustainable economic growth.

(6) In light of the significance of monetary policy in overcoming deflation, the government expected the Bank to enforce aggressive monetary easing under the "price stability target" of 2 percent, which was indicated in the joint statement, and to conduct monetary policy vigorously and decisively with a firm resolve, in order to achieve the target at the earliest possible time.

VI. 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. R. Miyao, Mr. Y. Morimoto, Ms. S. Shirai, Mr. K. Ishida, Mr. T. Sato, and Mr. T. Kiuchi.
Votes against the proposal: None.

B. Vote on "The 'Price Stability Target' under the Framework for the Conduct of Monetary Policy"

Next, members discussed the statement "The 'Price Stability Target' under the Framework for the Conduct of Monetary Policy," including a description of the Bank's basic thinking about the "price stability target," which was to be introduced, and put it to a vote. The Policy Board decided the statement by a majority vote. It was confirmed that the statement would be released immediately after the meeting (see Attachment 2).

Votes for the proposal: Mr. M. Shirakawa, Mr. H. Yamaguchi, Mr. K. G. Nishimura, Mr. R. Miyao, Mr. Y. Morimoto, Ms. S. Shirai, and Mr. K. Ishida.

Votes against the proposal: Mr. T. Sato and Mr. T. Kiuchi.

Mr. T. Sato and Mr. T. Kiuchi dissented from the introduction of the "price stability target" at 2 percent in terms of the year-on-year rate of change in the CPI, for the following reasons: (1) 2 percent in terms of the year-on-year rate of change in the CPI had rarely been achieved in the past two decades, and based on the general public's current perception of price developments that was built on such past experience, the 2 percent inflation rate was considerably higher than the inflation rate that was considered at this point to be consistent with sustainable price stability; (2) this suggested that, even if the central bank were to set 2 percent inflation as a target, this alone was highly unlikely to exert a substantial influence on inflation expectations, and thus it was unreasonable to conduct monetary policy with the aim of achieving such an ambitious target; and (3) efforts by a wide range of entities toward strengthening the growth potential of Japan's economy were essential in order to achieve the 2 percent target, but if the 2 percent target were set before such efforts made progress and the effects of these efforts were confirmed, this could impair the credibility of monetary policy or disturb communication with financial markets because of considerable uncertainty regarding the achievement of the target.

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

With a view to taking additional steps to provide monetary accommodation decisively and achieve the "price stability target" -- which was to be introduced -- at the earliest possible time, members shared the recognition that it was appropriate to introduce the open-ended asset purchasing method for purchases of financial assets conducted through the Program. "Amendment to 'Principal Terms and Conditions for the Asset Purchase Program'" was then put to a vote. Members voted unanimously to approve the amendment and agreed that the decision should be made public accordingly.

D. Vote on "Joint Statement of the Government and the Bank of Japan on Overcoming Deflation and Achieving Sustainable Economic Growth"

Members then discussed "Joint Statement of the Government and the Bank of Japan on Overcoming Deflation and Achieving Sustainable Economic Growth," and it was put to a vote. The Policy Board decided the statement by a majority vote. It was confirmed that it would be made public accordingly (see Attachment 4).

Votes for the proposal: Mr. M. Shirakawa, Mr. H. Yamaguchi, Mr. K. G. Nishimura, Mr. R. Miyao, Mr. Y. Morimoto, Ms. S. Shirai, and Mr. K. Ishida.
Votes against the proposal: Mr. T. Sato and Mr. T. Kiuchi.

Mr. T. Sato and Mr. T. Kiuchi dissented from the joint statement with the government that assumed the introduction of the "price stability target" of 2 percent in terms of the year-on-year rate of change in the CPI, for the same reasons they opposed the draft of "The 'Price Stability Target' under the Framework for the Conduct of Monetary Policy."

VII. Discussion on the Statement Entitled "Introduction of the 'Price Stability Target' and the 'Open-Ended Asset Purchasing Method'"

Next, members discussed the statement "Introduction of the 'Price Stability Target' and the 'Open-Ended Asset Purchasing Method,'" which included a description of (1) the introduction of the "price stability target," (2) the introduction of the "open-ended asset purchasing method," and (3) the joint statement by the government and the Bank, and formed a majority view. One member expressed the view that it was appropriate to set a separate period for which the virtually zero interest rate policy would remain effective, in order to further pursue aggressive monetary easing under the new target for price stability, and wished to formulate a proposal. As a result, the following two proposals were submitted.

A. Mr. R. Miyao's Policy Proposal

With regard to the draft of a statement that formed a majority view, Mr. R. Miyao proposed to (1) delete "a virtually zero interest rate policy" from the sentence regarding the Bank's future monetary policy stance, and (2) create a separate section in which to add the following description: "The Bank will aim to achieve a year-on-year rate of increase in the CPI of 2 percent and continue with a virtually zero interest rate policy until it judges this rate of increase to be in sight. By doing so, together with measures such as the aforementioned asset purchases, the Bank will further pursue aggressive monetary easing. At the same time, it will ascertain whether there is any significant risk to the sustainability of economic growth, including from the accumulation of financial imbalances." The proposal was then put to a vote.

The proposal was defeated by a majority vote.

Votes for the proposal: Mr. R. Miyao.
Votes against the proposal: Mr. M. Shirakawa, Mr. H. Yamaguchi, Mr. K. G. Nishimura, Mr. Y. Morimoto, Ms. S. Shirai, Mr. K. Ishida, Mr. T. Sato, and Mr. T. Kiuchi.

B. The Chairman's Policy Proposal

The chairman formulated the statement "Introduction of the 'Price Stability Target' and the 'Open-Ended Asset Purchasing Method,'" 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 1).

VIII. Approval of the Minutes of the Monetary Policy Meeting

The Policy Board approved unanimously the minutes of the Monetary Policy Meeting of December 19 and 20, 2012 for release on January 25, 2013.

Attachment 1
January 22, 2013
Bank of Japan

Introduction of the "Price Stability Target" and the "Open-Ended Asset Purchasing Method"

1. At the Monetary Policy Meeting held today, the Policy Board of the Bank of Japan took additional steps to provide monetary accommodation decisively. Specifically, the Bank decided to (1) introduce the "price stability target," and (2) introduce the "open-ended asset purchasing method" (i.e., to purchase assets without setting any termination date) under the Asset Purchase Program. Furthermore, the Bank decided to release the joint statement with the Government.

(1) Introduction of the "price stability target"[1]

The Bank held the discussion concerning its thinking on price stability and decided to introduce the "price stability target." In addition, the Bank decided to release "The 'Price Stability Target' under the Framework for the Conduct of Monetary Policy" (see Attachment 2).

The Bank recognizes that the inflation rate consistent with price stability on a sustainable basis will rise as efforts by a wide range of entities toward strengthening competitiveness and growth potential of Japan's economy make progress. Based on this recognition, the Bank sets the price stability target at 2 percent in terms of the year-on-year rate of change in the consumer price index (CPI).

Under the price stability target specified above, the Bank will pursue monetary easing and aim to achieve this target at the earliest possible time. Taking into consideration that it will take considerable time before the effects of monetary policy permeate the economy, the Bank will ascertain whether there is any significant risk to the sustainability of economic growth, including from the accumulation of financial imbalances.

(2) Introduction of the "open-ended asset purchasing method"[2]

The Bank will pursue aggressive monetary easing, aiming to achieve the above-mentioned price stability target, through a virtually zero interest rate policy and purchases of financial assets, as long as the Bank judges it appropriate to continue with each policy measure respectively.[3, 4] With respect to the Asset Purchase Program, after completing the current purchasing method, from January 2014, the Bank will introduce a method of purchasing a certain amount of financial assets every month without setting any termination date. Particularly, for some time, following the introduction of this method, the amount of monthly purchases is specified at about 13 trillion yen, 2 trillion yen of which is JGBs (see Attachment 3 for the purchases of financial assets). As a result of these measures, the total size of the Asset Purchase Program will be increased by about 10 trillion yen in 2014 and is expected to be maintained thereafter.

In the pursuit of monetary easing, taking into consideration that it will take considerable time before the effects of monetary policy permeate the economy, the Bank will ascertain whether there is any significant risk to the sustainability of economic growth, including from the accumulation of financial imbalances.

(3) Joint statement of the Government and the Bank of Japan[5]

The Bank decided to release the statement titled "Joint Statement of the Government and the Bank of Japan on Overcoming Deflation and Achieving Sustainable Economic Growth" with the Government (see Attachment 4).

2. The Policy Board also decided, by a unanimous vote, 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. Overseas economies remain in a deceleration phase. In global financial markets, investors' risk aversion has abated, although developments require continued attention.

4. Japan's economy remains relatively weak. Exports and industrial production have decreased, reflecting the aforementioned developments in overseas economies. Business fixed investment has shown some weakness on the whole, although resilience has been observed in nonmanufacturing. In contrast, public investment has continued to increase, and housing investment has generally been picking up. Private consumption has remained resilient and the effects of the decline in car sales due to the ending of some measures to stimulate demand for automobiles have diminished. Meanwhile, financial conditions in Japan are accommodative. On the price front, the year-on-year rate of change in the CPI (all items less fresh food) is around 0 percent.

5. With regard to the outlook, Japan's economy is expected to level off more or less for the time being, and thereafter, it will return to a moderate recovery path as domestic demand remains resilient partly due to the effects of various economic measures and overseas economies gradually emerge from the deceleration phase. For the time being, the year-on-year rate of change in the CPI is expected to turn negative due to the reversal of the previous year's movements in energy-related and durable consumer goods, and thereafter, it is likely to be around 0 percent again.

6. Compared with the forecasts presented in the October 2012 *Outlook for Economic Activity and Prices*, growth prospects will likely be somewhat lower for fiscal 2012, but they will likely be higher for fiscal 2013 partly due to the effects of various economic measures. Growth prospects for fiscal 2014 will likely be broadly in line with the October forecasts. With regard to prices, the year-on-year rate of change in the domestic corporate goods price index will likely be somewhat higher especially for fiscal 2013 mainly due to movements in foreign exchange rates. The year-on-year rate of change in the CPI (all items less fresh food) will likely be broadly in line with the October forecasts.

7. Regarding risks, there remains a high degree of uncertainty concerning Japan's economy, including the prospects for the European debt problem, the momentum toward recovery for the U.S. economy, the possibility of emerging and commodity-exporting economies making a smooth transition to the sustainable growth path, and the effects of the recent bilateral relationship between Japan and China.

8. The Bank recognizes that Japan's economy faces the critical challenge of overcoming deflation as early as possible and returning to the sustainable growth path with price stability. This challenge will be met through the combination of efforts by a wide range of entities to strengthen the economy's growth potential and support from the financial side. Based on this recognition, the Bank will, as mentioned above, pursue aggressive monetary easing. The Bank expects that the Government will surely implement measures, specified in the "Joint Statement," such as carrying out bold regulatory and institutional reforms, and furthermore, steadily promote measures aimed at establishing a sustainable fiscal structure.

[1] 7-2 majority vote (Voting for the action: Mr. M. Shirakawa, Mr. H. Yamaguchi, Mr. K. G. Nishimura, Mr. R. Miyao, Mr. Y. Morimoto, Ms. S. Shirai, and Mr. K. Ishida. Voting against the action: Mr. T. Sato and Mr. T. Kiuchi.) Mr. T. Sato and Mr. T. Kiuchi dissented from setting the price stability target at 2 percent in terms of the year-on-year rate of change in the CPI.

[2] The introduction of the "open-ended asset purchasing method" was decided by a unanimous vote.

[3] Mr. T. Sato and Mr. T. Kiuchi dissented from aiming to achieve the price stability target of 2 percent, through a virtually zero interest rate policy and purchases of financial assets, as long as the Bank judges it appropriate to continue with each policy measure respectively.

[4] Mr. Miyao proposed to continue with a virtually zero interest rate policy until the Bank judges 2 percent in terms of the year-on-year rate of increase in the CPI to be in sight. The proposal was defeated by a majority vote. Voting for the proposal: Mr. R. Miyao. Voting against the proposal: Mr. M. Shirakawa, Mr. H. Yamaguchi, Mr. K. G. Nishimura, Mr. Y. Morimoto, Ms. S. Shirai, Mr. K. Ishida, Mr. T. Sato, and Mr. T. Kiuchi.

[5] 7-2 majority vote (Voting for the action: Mr. M. Shirakawa, Mr. H. Yamaguchi, Mr. K. G. Nishimura, Mr. R. Miyao, Mr. Y. Morimoto, Ms. S. Shirai, and Mr. K. Ishida. Voting against the action: Mr. T. Sato and Mr. T. Kiuchi.) Mr. T. Sato and Mr. T. Kiuchi dissented from the inclusion of the sentence, "the Bank sets the price stability target at 2 percent in terms of the year-on-year rate of change in the consumer price index."

(Appendix 1)

Forecasts of the Majority of Policy Board Members

y/y % chg.

	Real GDP	Domestic CGPI	CPI (all items less fresh food)
Fiscal 2012	+1.0 to +1.1 [+1.0]	-1.2 to -1.1 [-1.2]	-0.2 to -0.1 [-0.2]
Forecasts made in October 2012	+1.4 to +1.6 [+1.5]	-1.2 to -0.9 [-1.1]	-0.1 to -0.1 [-0.1]
Fiscal 2013	+1.9 to +2.5 [+2.3]	+0.4 to +1.0 [+0.8]	+0.3 to +0.6 [+0.4]
Forecasts made in October 2012	+1.3 to +1.8 [+1.6]	+0.1 to +0.7 [+0.5]	+0.2 to +0.6 [+0.4]
Fiscal 2014	+0.6 to +1.0 [+0.8]	+3.8 to +4.5 [+4.1]	+2.5 to +3.0 [+2.9]
Forecasts made in October 2012	+0.2 to +0.7 [+0.6]	+3.7 to +4.4 [+4.2]	+2.4 to +3.0 [+2.8]
Excluding the effects of the consumption tax hike		+0.9 to +1.6 [+1.2]	+0.5 to +1.0 [+0.9]
Forecasts made in October 2012		+0.8 to +1.5 [+1.3]	+0.4 to +1.0 [+0.8]

Notes: 1. Figures in brackets indicate the median of the Policy Board members' forecasts (point estimates).

2. The forecasts of the majority of the Policy Board members are constructed as follows: each Policy Board member's forecast takes the form of a point estimate -- namely, the figure to which he or she attaches the highest probability of realization. These forecasts are then shown as a range, with the highest figure and the lowest figure excluded. The range does not indicate the forecast errors.

3. Individual Policy Board members make their forecasts with reference to the view of market participants regarding the future course of the policy interest rate -- a view that is incorporated in market interest rates.

4. The scheduled consumption tax hikes for 2014 and 2015 -- of 8 percent and 10 percent, respectively -- are incorporated in the forecasts. In terms of the outlook for the CGPI and the CPI, individual Policy Board members make their forecasts based on figures excluding the direct effects of the consumption tax hike.

5. The forecasts for the CGPI and the CPI for fiscal 2014 that incorporate the direct effects of the consumption tax hike are constructed as follows. First, the contribution to prices from the tax hike is mechanically computed on the assumption that the tax increase will be fully passed on for all taxable items. The domestic CGPI will be pushed up by 2.9 percentage points and the CPI by 2.0 percentage points. Second, these figures are added to the forecasts made by the Policy Board members.

6. The CPI using the Chain-Weighted Index Formula has also been released as a reference. Based on this chain-weighted index, the year-on-year rate of change in the CPI toward the latter half of the projection period may be slightly lower than the above forecasts based on the Fix-Weighted Index Formula.

7. The ranges shown below include the forecasts of all Policy Board members.

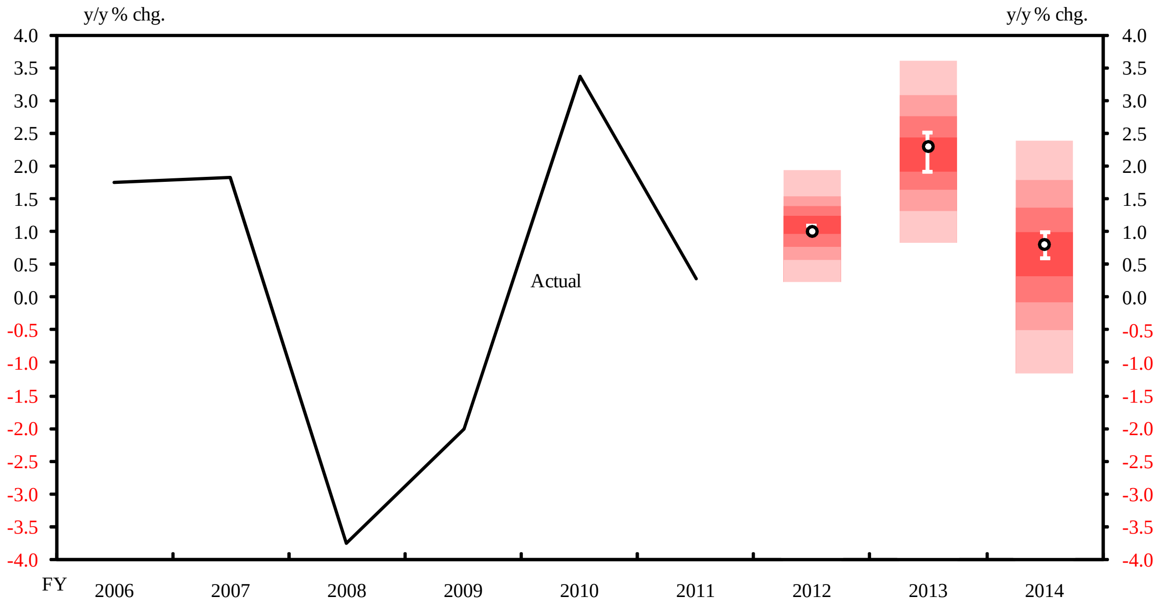
y/y % chg.

	Real GDP	Domestic CGPI	CPI (all items less fresh food)
Fiscal 2012	+0.9 to +1.1	-1.2 to -1.1	-0.2 to -0.1
Forecasts made in October 2012	+1.2 to +1.7	-1.3 to -0.8	-0.1 to 0.0
Fiscal 2013	+1.8 to +2.5	+0.3 to +1.1	+0.1 to +0.7
Forecasts made in October 2012	+1.0 to +1.8	-0.2 to +0.8	-0.1 to +0.6
Fiscal 2014	+0.2 to +1.3	+3.3 to +4.7	+2.4 to +3.0
Forecasts made in October 2012	+0.1 to +0.8	+3.3 to +4.5	+2.2 to +3.0
Excluding the effects of the consumption tax hike		+0.4 to +1.8	+0.4 to +1.0
Forecasts made in October 2012		+0.4 to +1.6	+0.2 to +1.0

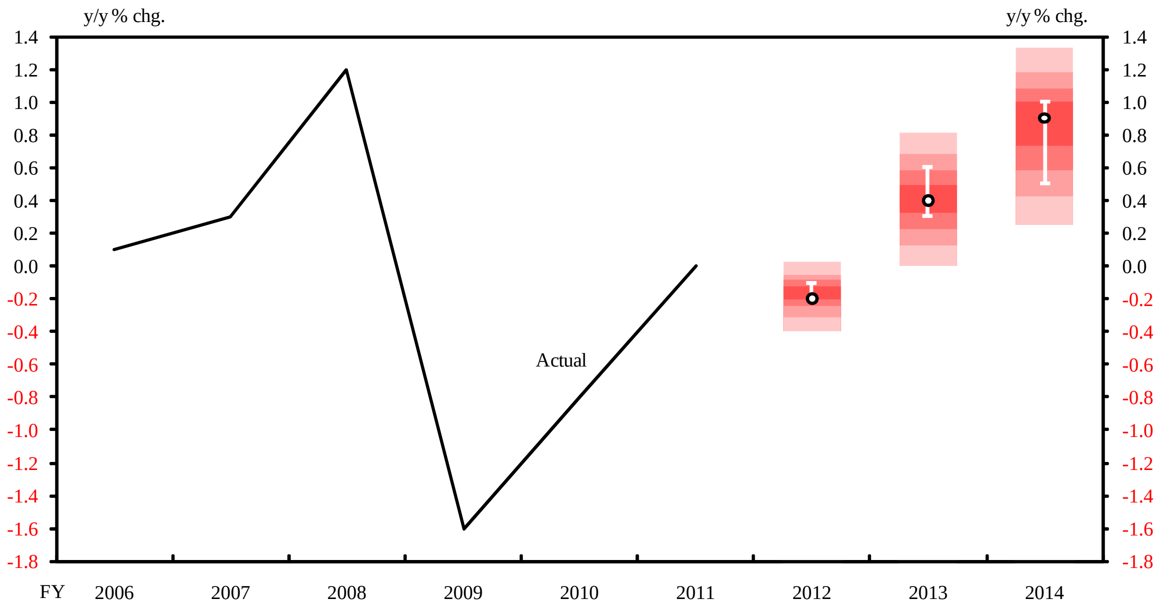
(Appendix 2)

Forecast Distribution Charts of Policy Board Members

(1) Real GDP



(2) CPI (All Items Less Fresh Food)



Notes: 1. Based on the aggregated probability distributions (i.e., the Risk Balance Charts) compiled from the distributions of individual Policy Board members, the Forecast Distribution Charts are compiled as follows. First, upper and lower 10 percentiles of the aggregated distributions are trimmed and second, colors indicated below are used to show the respective percentiles of those distributions.

Upper 40% to lower 40%	Upper 30 to 40% & lower 30 to 40%	Upper 20 to 30% & lower 20 to 30%	Upper 10 to 20% & lower 10 to 20%

2. For the process of compilation of the Risk Balance Charts, see the box on page 9 of the April 2008 *Outlook for Economic Activity and Prices* .

3. The circles in the bar charts indicate the median of the Policy Board members' forecasts (point estimates). The vertical lines in the bar charts indicate the range of the forecasts of the majority of Policy Board members.

4. The forecast for the CPI excludes the direct effects of the scheduled consumption tax hikes.

Attachment 2

January 22, 2013

Bank of Japan

The "Price Stability Target"
under the Framework for the Conduct of Monetary Policy

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." At the Monetary Policy Meeting held today, the Policy Board reviewed the "price stability goal in the medium to long term" adopted in February 2012, in light of the above-mentioned principle. As a result, it decided to introduce the "price stability target" and restate the framework for the conduct of monetary policy.

2. "Price stability" is defined conceptually as "a state where various economic agents including households and firms may make decisions regarding such economic activities as consumption and investments without being concerned about the fluctuations in the general price level." Therefore, "price stability" must be the one on a sustainable basis.

3. The newly-introduced "price stability target" is the inflation rate that the Bank judges to be consistent with price stability on a sustainable basis. The Bank recognizes that the inflation rate consistent with price stability on a sustainable basis will rise as efforts by a wide range of entities toward strengthening competitiveness and growth potential of Japan's economy make progress. Based on this recognition, the Bank sets the "price stability target" at 2 percent in terms of the year-on-year rate of change in the consumer price index (CPI) -- a main price index.

4. Previously, the "price stability goal in the medium to long term" was in a positive range of 2 percent or lower in terms of the year-on-year rate of change in the CPI and the Bank set a goal at 1 percent for the time being. This time, replacing a "goal" with a "target" and setting that target at 2 percent in terms of the year-on-year rate of change

in the CPI are based on the following recognition.

The Bank recognizes that the inflation rate consistent with price stability on a sustainable basis will rise as efforts by a wide range of entities toward strengthening competitiveness and growth potential of Japan's economy make progress. Today's expected rate of inflation has been shaped over the years. As the strengthening of growth potential makes progress going forward, the actual rate of inflation would gradually rise and accordingly the expected inflation rate of households and firms is likely to rise as well. Going forward, as prices are expected to rise moderately, it is judged appropriate to clearly indicate the target of 2 percent in order to anchor the sustainable rate of inflation.

Switching from a "goal" to a "target" reflects an increasing awareness regarding the importance of flexibility in the conduct of monetary policy in Japan. The effects of monetary policy permeating economic activity and thereafter prices require a considerable and variable time lag. The conduct of monetary policy has to be flexible by examining various risk factors, including those related to financial imbalances, in addition to the assessment of current developments and outlook for economic activity and prices, from the perspective of achieving sustainable growth with price stability. Such understanding has been widely shared around the globe; particularly, in the aftermath of the global financial crisis, major economies of the world have come to emphasize flexibility in the conduct of monetary policy -- by, for example, publicly articulating the importance of paying due attention to financial system stability. Over the last year, there has been an increasing awareness of such understanding in Japan as well. In such circumstances, it is judged transparent and appropriate to use the expression, "target," in order to explain the Bank's thinking on price stability.

5. In order for Japan's economy to overcome deflation as early as possible and return to a sustainable growth path with price stability, efforts by a wide range of entities to strengthen growth potential are crucial. The Bank will continue to thoroughly examine the progress toward strengthening growth potential and the ensuing developments in the expected inflation rate of households and firms. In the meantime, the Government has shown its intention to aggressively pursue steps for strengthening competitiveness and growth potential of Japan's economy and to steadily promote

measures aimed at establishing a sustainable fiscal structure.

6. The Bank will continue to conduct monetary policy, based on its assessment of economic activity and prices from two perspectives, in the context of the "price stability target."

   The first perspective is examining, as regards economic activity and prices over the next two years or so, whether the outlook deemed most likely by the Bank of Japan follows a path of sustainable growth under price stability.

   The second perspective is examining, in a longer term, various risks that are most relevant to the conduct of monetary policy aimed at achieving sustainable growth under price stability. In particular, financial imbalances will be examined as a risk that will significantly impact economic activity and prices when they materialize, although the probability of their emergence is low.

   The Bank of Japan will, in light of deliberations from the two perspectives described above, outline the current view on monetary policy, and disclose it periodically mainly in the *Outlook for Economic Activity and Prices* (Outlook Report).

Attachment 3

Amount of Monthly Purchases under the Asset Purchase Program

from January 2014

Total amount:	**about 13 trillion yen**
JGBs:	about 2 trillion yen
T-Bills:	about 10 trillion yen

Notes: 1. Based on the average residual maturities of JGBs and T-Bills that have recently been purchased, the total size of the Asset Purchase Program, through the above-mentioned monthly purchases, will be increased by about 10 trillion yen in 2014 and is expected to be maintained thereafter.

2. For financial assets other than JGBs and T-Bills, the Bank will aim to maintain the amount outstanding of those assets.

3. For fixed-rate funds-supplying operation against pooled collateral, the Bank will aim to maintain about 25 trillion yen.

4. In addition to purchases under the program, the Bank regularly purchases JGBs at the pace of 21.6 trillion yen per year.

Attachment 4

Joint Statement of the Government and the Bank of Japan on Overcoming Deflation and Achieving Sustainable Economic Growth

1. In order to overcome deflation early and achieve sustainable economic growth with price stability, the Government and the Bank of Japan will strengthen their policy coordination and work together as follows.

2. 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, and is responsible for maintaining financial system stability. The Bank aims to achieve price stability on a sustainable basis, given that there are various factors that affect prices in the short run.

   The Bank recognizes that the inflation rate consistent with price stability on a sustainable basis will rise as efforts by a wide range of entities toward strengthening competitiveness and growth potential of Japan's economy make progress. Based on this recognition, the Bank sets the price stability target at 2 percent in terms of the year-on-year rate of change in the consumer price index.

   Under the price stability target specified above, the Bank will pursue monetary easing and aim to achieve this target at the earliest possible time. Taking into consideration that it will take considerable time before the effects of monetary policy permeate the economy, the Bank will ascertain whether there is any significant risk to the sustainability of economic growth, including from the accumulation of financial imbalances.

3. The Government will, in order to revitalize Japan's economy, not only flexibly manage macroeconomic policy but also formulate measures for strengthening competitiveness and growth potential of Japan's economy, and promote them strongly under the leadership of the Headquarters for Japan's Economic Revitalization. Those measures include all possible decisive policy actions for reforming the economic structure, such as concentrating resources on innovative research and development, strengthening the

foundation for innovation, carrying out bold regulatory and institutional reforms and better utilizing the tax system.

In addition, in strengthening coordination between the Government and the Bank of Japan, the Government will steadily promote measures aimed at establishing a sustainable fiscal structure with a view to ensuring the credibility of fiscal management.

4. The Council on Economic and Fiscal Policy will regularly review the progress in the conduct of macroeconomic policies including monetary policy, the current condition and future prospects of prices in the context of the price stability target under those policies, economic and fiscal situation including employment conditions, and progress in economic structural reform.