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January 27, 2014

Bank of Japan

Minutes of the Monetary Policy Meeting

on December 19 and 20, 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 Thursday, December 19, 2013, from 2:00 p.m. to 4:50 p.m., and on Friday, December 20, from 8:59 a.m. to 11:52 a.m.[1]

Policy Board Members Present

Mr. H. Kuroda, Chairman, Governor of the Bank of Japan

Mr. K. Iwata, Deputy Governor of the Bank of Japan

Mr. H. Nakaso, 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. M. Asakawa, Deputy Vice Minister for Policy Planning and Coordination, Ministry of Finance

Mr. S. Koizumi, Parliamentary Secretary of Cabinet Office, Cabinet Office[2]

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

Reporting Staff

Mr. M. Amamiya, Executive Director

Mr. N. Kinoshita, Executive Director[4]

Mr. K. Momma, Executive Director (Assistant Governor)

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

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[1] The minutes of this meeting were approved by the Policy Board at the Monetary Policy Meeting held on January 21 and 22, 2014 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] Mr. S. Koizumi was present on December 20.

[3] Mr. K. Umetani was present on December 19.

[4] Mr. N. Kinoshita was present on December 19 for the whole of the session, and on December 20 from 8:59 a.m. to 10:20 a.m.

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

Mr. H. Yamaoka, Director-General, Financial Markets Department

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

Mr. S. Kameda, Head of Economic Research Division, Research and Statistics Department

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

Secretariat of the Monetary Policy Meeting

Mr. N. Yoshioka, Director-General, Secretariat of the Policy Board

Mr. N. Fukunaga, Director, Deputy Head of Planning and Coordination Division, Secretariat of the Policy Board

Mr. R. Hattori, Senior Economist, Monetary Affairs Department

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

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 November 20 and 21, 2013, had been providing funds through purchases of Japanese government bonds (JGBs) and other measures.[6] In this situation, the amount outstanding of the monetary base had been in the range of 186-193 trillion yen.

B. Recent Developments in Financial Markets

Money market rates, including longer-term ones, had been at low levels. The uncollateralized overnight call rate had been at a level below 0.1 percent. General collateral (GC) repo rates had been more or less flat at around 0.1 percent. As for interest rates on term instruments, yields on treasury discount bills (T-Bills) had been below the 0.1 percent level for all maturities. Rates on longer-term interbank instruments had been flat.

Long-term interest rates in Japan had recently been in the range of 0.65-0.70 percent as the Bank proceeded with its JGB purchases, although they had risen somewhat, mainly against the background of a slight rise in U.S. long-term interest rates. The Nikkei 225 Stock Average had risen mainly as a positive response to the depreciation of the yen following the rise in U.S. stock prices, which had marked their highest levels, and had recently been in the range of 15,500-16,000 yen. Yield spreads between corporate bonds and JGBs had been narrowing very moderately on the whole, reflecting solid demand from investors, despite a widening in some corporate bond spreads. In the foreign exchange market, the yen had depreciated against the U.S. dollar, mainly reflecting firm U.S. economic indicators and the decision by the Federal Reserve to begin reducing the pace of its asset purchases. The U.S. dollar/yen rate had recently been at around 104 yen.

C. Overseas Economic and Financial Developments

Overseas economies as a whole were picking up moderately, although a lackluster performance was partly seen.

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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 conduct money market operations so that the monetary base will increase at an annual pace of about 60-70 trillion yen.

The U.S. economy had been recovering moderately against the backdrop of steady private demand. Housing investment continued to generally pick up, although the pace had become somewhat moderate. Private consumption had been firm as asset prices continued to rise and the employment situation improved steadily. Exports were also increasing moderately. Reflecting these developments in demand, business sentiment continued to improve, and production as well as business fixed investment were heading toward a pick-up, although the pace remained slow. As for prices, the year-on-year rate of increase in the consumer price index (CPI) for all items less food and energy, or the core CPI, had been more or less flat. In this situation, the year-on-year rate of increase in the CPI for all items had declined, mainly as a result of the drop in energy prices.

Economic activity in Europe was gradually turning toward a pick-up. Private consumption had been picking up, albeit moderately, with consumer sentiment being on an improving trend, although the employment and income situation remained severe. Business fixed investment had bottomed out. In addition, exports were heading toward a pick-up. Reflecting these developments in demand, production had bottomed out. As for prices, slack in supply and demand conditions had been exerting downward pressure on prices, and the year-on-year rate of increase in the Harmonized Index of Consumer Prices (HICP) for all items excluding energy and unprocessed food had been on a declining trend. On the other hand, annual HICP inflation for all items had risen somewhat, partly reflecting the moderation in the year-on-year rate of decline in energy prices. Meanwhile, economic activity in the United Kingdom was recovering, particularly in domestic demand.

With regard to Asia, the Chinese economy continued to see stable growth on the back of firm domestic demand. Stable growth in private consumption continued against the background of a favorable employment and income situation, although effects of the government's frugality campaign continued to be observed in some areas. Fixed asset investment also remained firm. Moreover, exports had been picking up, particularly those to Europe and the United States. With these developments in demand, production had continued to mark relatively high growth, particularly in the machinery industry, including motor vehicles. As for prices, the year-on-year rate of increase in the CPI had been somewhat low as a trend. Regarding the NIEs and the ASEAN countries, while economic developments in the NIEs were picking up somewhat -- driven by growth in exports -- due in part to the improvement in advanced economies, growth momentum in the ASEAN countries had weakened, reflecting the slowdown in domestic demand, and thus developments toward a pick-up in the NIEs and the ASEAN countries had been slow on the whole. As for prices, the year-on-year rates of increase in the CPI generally continued to be at somewhat low levels, although there were differences by country and region. In India, the economy remained in a state of deceleration, particularly in domestic demand.

In global financial markets, developments continued to show no clear direction because, while favorable U.S. economic indicators continued to be released, these aroused speculation among market participants that the Federal Reserve would move forward the timing of a reduction in the pace of its asset purchases. After the Federal Reserve made its decision to begin reducing the pace of its asset purchases, however, market participants -- particularly in advanced economies -- strengthened their risk-taking stance somewhat, partly because the Federal Reserve had presented its intention to maintain accommodative financial conditions to the market. Meanwhile, in emerging markets, foreign exchange rates as well as stock and bond prices had declined, but these drops were marginal. International commodity prices continued to be weak from a relatively longer-term perspective in a situation where recovery in emerging economies lacked momentum, but had recently been rising somewhat on the whole, partly reflecting favorable U.S. and Chinese economic indicators.

D. Economic and Financial Developments in Japan

1. Economic developments

Exports had generally been picking up. Real exports had fallen marginally in the July-September quarter of 2013 on a quarter-on-quarter basis, but rose again in the October-November period relative to that quarter. Exports were expected to increase moderately, mainly against the background of the pick-up in overseas economies.

Public investment continued to increase. It was expected to trend upward for the time being and then become more or less flat at a high level.

Improvement in business sentiment continued and became widespread. In the December 2013 *Tankan* (Short-Term Economic Survey of Enterprises in Japan), the diffusion index for business conditions for all industries and enterprises (the proportion of firms responding that business conditions were "favorable" minus the proportion of those responding that they were "unfavorable") improved for the fourth straight term, reaching the level of the peak in the previous phase of economic expansion. With regard to the diffusion index by industry and size, all categories (large, medium-sized, and small manufacturing and nonmanufacturing firms) were in "favorable" territory. Business fixed investment had been picking up as corporate profits had improved. According to the *Financial Statements Statistics of Corporations by Industry, Quarterly*, business fixed investment in nominal terms fell marginally in the July-September quarter of 2013 on a quarter-on-quarter basis, after having increased markedly in the April-June quarter. On the other hand, the aggregate supply of capital goods -- a coincident indicator of machinery investment -- on a basis excluding transport equipment was more or less flat in the July-September quarter, but rose noticeably in October compared with that quarter. Machinery orders (private sector, excluding orders for ships and those from electric power companies) -- a leading indicator of machinery investment -- kept moving upward in October relative to the July-September quarter, after having increased markedly in that quarter from the previous quarter. Business fixed investment was projected to follow a moderate increasing trend as corporate profits continued to improve. For all industries and enterprises, business fixed investment plans (excluding software investment and including land purchasing expenses) for fiscal 2013 in the December *Tankan* had been revised somewhat upward in comparison to the September *Tankan*.

As for the employment and income situation, supply and demand conditions in the labor market continued to improve steadily, albeit at a moderate pace, and employee income had also shown a pick-up.

Private consumption remained resilient, with improvement in the employment and income situation. As for durable consumer goods, the number of new passenger-car registrations had turned upward since around summer 2013 with the introduction of new models, and had recently shown somewhat strong movements. In addition, sales of household electrical appliances had been steady, albeit with fluctuations. Such movements in durable consumer goods might partly reflect that the front-loaded increase in demand prior to the consumption tax hike, including the ripple effects of an increase in housing investment, had started to become evident. Meanwhile, indicators related to consumer confidence had continued on an improving trend, albeit with fluctuations, after rising at a rapid pace since the start of 2013. Recently, however, they had fallen somewhat significantly in October and bounced back only marginally in November. Private consumption was expected to remain resilient as a trend, supported mainly by improvement in the employment and income situation, albeit with some fluctuations caused by the front-loaded increase and subsequent decline in demand prior to and after the consumption tax hike.

Housing investment had increased, aided partly by the front-loaded increase in demand prior to the consumption tax hike. It was expected to remain resilient as a trend, albeit with some fluctuations caused by the hike.

Reflecting these developments in demand both at home and abroad, industrial production had been increasing moderately. It was expected to continue on such a trend, mainly reflecting developments in demand at home and abroad, albeit with some fluctuations caused by the effects of the consumption tax hike. Judging from interviews with firms and other relevant information, production in the October-December quarter of 2013 was expected to continue to increase, and it was considered that production for the January-March quarter of 2014 would continue increasing in a wide range of industries, with the ongoing moderate recovery in demand both at home and abroad.

As for prices, domestic corporate goods prices were rising moderately relative to three months earlier, mainly against the backdrop of movements in international commodity prices and foreign exchange rates. They were expected to continue to do so for the time being. The year-on-year rate of increase in the CPI (all items less fresh food) was at around 1 percent, and was likely to rise for the time being. Meanwhile, inflation expectations appeared to be rising on the whole, considering the results of various surveys.

2. Financial environment

Financial conditions were accommodative.

The monetary base had increased significantly as asset purchases by the Bank had progressed, and the year-on-year rate of growth had been in the range of 50-55 percent.

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 continued to be favorable. Those for corporate bonds also remained favorable on the whole. Firms' credit demand had been increasing moderately, mainly for working capital and funds related to mergers and acquisitions. Against this backdrop, the year-on-year rate of increase in the amount outstanding of bank lending had been at around 2.5 percent. The amount outstanding of CP and corporate bonds had been more or less around the year-ago level. Firms retained their recovered financial positions. Meanwhile, the year-on-year rate of growth in the money stock had been in the range of 4.0-4.5 percent, mainly due to the increase in bank lending.

3. The fund-provisioning measure to support strengthening the foundations for economic growth and the fund-provisioning measure to stimulate bank lending

On December 6, 2013, the Bank carried out a new loan disbursement, amounting to 223.7 billion yen, under the main rules for the fund-provisioning measure to support strengthening the foundations for economic growth. The outstanding balance of loans disbursed by the Bank under these rules amounted to 3,239.3 billion yen after the new loan disbursement, and thus exceeded 3 trillion yen, as in the previous loan disbursement. The outstanding balance of loans disbursed by the Bank under the special rules for equity investments and asset-based lending (ABL) came to 103.6 billion yen, and that under the special rules for small-lot investments and loans amounted to 7.477 billion yen. As for the special rules for the U.S. dollar lending arrangement, the Bank implemented its new loan disbursement of 0.864 billion dollars, bringing the outstanding balance of loans to 7.369 billion dollars.

On December 16, 2013, the Bank carried out a new loan disbursement, amounting to 1,052.8 billion yen, under the fund-provisioning measure to stimulate bank lending. The outstanding balance of loans disbursed by the Bank amounted to 5,084.3 billion yen after the new loan disbursement, thus exceeding 5 trillion yen.

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

A. Economic Developments

With regard to global financial markets, members shared the recognition that, although developments continued to show no clear direction since the previous meeting due to speculation about the direction of U.S. monetary policy, market participants -- particularly in advanced economies -- had strengthened their risk-taking stance somewhat following the Federal Reserve's decision to begin reducing the pace of its asset purchases.

Some members pointed out that the market response to the Federal Reserve's decision was generally positive, mainly because (1) it was made on the back of continued recovery in the U.S. economy and (2) the Federal Reserve's intention to maintain accommodative financial conditions had been permeating the markets. These members added that attention should continue to be paid to the effects of this decision on emerging economies facing structural problems such as current account deficits. Based on this discussion, members concurred that it was necessary to continue to carefully monitor future developments in global financial markets, including the effects on emerging markets.

Members concurred that, although a lackluster performance was partly seen, overseas economies as a whole were picking up moderately as (1) the U.S. economy had been on a moderate recovery trend, (2) economic activity in Europe was gradually turning toward a pick-up, and (3) the Chinese economy continued to see stable growth on the back of firm domestic demand. As for the outlook, they shared the recognition that overseas economies -- particularly advanced economies -- would continue to pick up. Many members expressed the view that uncertainty concerning overseas economies had declined, mainly reflecting a decrease in uncertainty about the debt ceiling issue and monetary policy in the United States. A few members noted that it had become more likely that the U.S. economy would become the driving force of global economic growth in 2014. In response to this view, one member pointed out that attention needed to be paid to the possibility that the growth in the U.S. economy would not fully offset the adverse effects stemming from the deceleration in emerging economies.

With regard to developments in overseas economies by region, members agreed that the U.S. economy had been recovering moderately against the backdrop of steady private demand. Many members pointed to the improvement in the employment situation, as well as in consumer confidence, which had worsened at one point. As for the outlook, members shared the view that the pace of economic recovery would gradually rise, mainly as accommodative financial conditions would be maintained and the fiscal drag would gradually fade. Furthermore, they shared the recognition that uncertainty surrounding future developments had declined since (1) the U.S. Congress had reached agreement on matters such as the size of fiscal expenditures and (2) the Federal Reserve had decided to begin reducing the pace of its asset purchases. One member, noting that there was uncertainty regarding the extent to which households would increase their debts in order to finance their spending, expressed the view that this might be restraining firms' fixed investment. A few members noted that it seemed unlikely at the moment that households would increase their debts to the levels seen prior to the financial crisis and thereby invigorate consumption. Meanwhile, a few members -- while pointing to the high degree of innovation capacity, as seen in the development of shale gas, and to the continued vigorous investment in research and development -- expressed the view that these factors would underpin the medium- to long-term growth potential of the U.S. economy.

Members shared the recognition that economic activity in the euro area was gradually turning toward a pick-up. Many members expressed the view that, in a situation where business and household sentiment continued to improve, private consumption had been picking up, albeit moderately, and production had bottomed out. As for the outlook, members concurred that, although uncertainty remained concerning the prospects for the European debt problem, the economy was likely to continue picking up on the back of anticipated improvement in external demand in addition to the pick-up in domestic demand. A few members, however, pointed out that attention should be paid to the possibility that elevated real interest rates and appreciation of the currency during the disinflationary trend could lead to a self-fulfilling intensification of downward pressure on prices.

Members agreed that the Chinese economy continued to see stable growth on the back of firm domestic demand. As for the outlook, most members concurred that the economy would maintain stable growth at around the current pace as authorities would likely continue to pay consideration to economic activity while progressing with structural reforms, and on the back of expectations that external demand would continue improving moderately. On the other hand, one member noted that the growth rate could decline moderately, due to the government's stance of restraining infrastructure investment and to corrections to accommodative financial conditions.

Regarding the NIEs and the ASEAN countries, members concurred that developments toward a pick-up had been slow on the whole. Some members, while pointing out that exports from South Korea and Taiwan showed signs of picking up, reflecting the improvement in the U.S. and European economies as well as the stable growth in the Chinese economy, noted that economic growth was slow in the ASEAN countries as domestic demand was restrained due to the tightening of financial conditions. As for the outlook, members shared the recognition that the pace of economic growth in the

NIEs and the ASEAN countries would likely remain relatively slow for the time being, but thereafter would rise again as growth in advanced economies was expected to gain momentum over time.

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

With regard to economic activity, members shared the view that the economy had been recovering moderately. They agreed that a virtuous cycle among production, income, and spending continued to operate, as evidenced by the fact that (1) in the household sector, private consumption and housing investment remained firm as the employment and income situation had been improving; and (2) in the corporate sector, business fixed investment had been picking up as business sentiment had improved. Many members expressed the recognition that the effects of the front-loaded increase in demand prior to the consumption tax hike had already been observed in some parts of the economy. Some members said that it was necessary to carefully examine the extent of the front-loaded increase in demand while acknowledging the difficulty of capturing it on a real-time basis. As for the outlook for the economy, members confirmed the view that, while it would be affected by the front-loaded increase and subsequent decline in demand prior to and after the consumption tax hike, the economy was likely to continue its moderate recovery as a trend as the virtuous cycle among production, income, and spending would continue to operate. One member -- while pointing out that, at the time of the consumption tax hike in 1997, the effects of excesses in production capacity, employment, and debt stemming from the bursting of the bubble had started to fully take hold and concerns about financial system stability had been increasing gradually -- expressed the view that the current economic phase differed from that in 1997. A few members said that the effects of the consumption tax hike -- including those on business and consumer sentiment -- should be examined without making any prejudgment, considering that the economy had experienced a prolonged period of deflation.

Members shared the recognition that, as overseas economies as a whole were picking up moderately, Japan's exports had generally been picking up as well -- albeit with fluctuations -- although the weak momentum remained a matter of concern. A few members expressed the view that exports continued to generally pick up, given that real exports for the October-November period of 2013 had increased relative to the

July-September quarter. As for the outlook, members agreed that exports were likely to increase moderately, mainly against the background of the improvement in overseas economies. They shared the view that the lack of momentum in exports, despite the earlier depreciation of the yen, basically reflected developments in overseas economies. On this basis, some members pointed to the possibility that this lack of momentum might also be affected by structural factors such as the trend progress in Japanese firms' development of overseas business, as well as the decline in their competitiveness.

Members concurred that, although the downward revision in manufacturers' business fixed investment plans in the December 2013 *Tankan* was a matter of concern, business fixed investment had been picking up on the whole, as corporate profits had improved, and was projected to follow a moderate increasing trend. A few members pointed out that business fixed investment was highly likely to follow an increasing trend, albeit moderately, taking into account the following: (1) there was room for a further increase in corporate profits since firms' projected value of the yen against the U.S. dollar in the December *Tankan* was higher than the current level; (2) business fixed investment plans for the second half of fiscal 2013 in the December *Tankan* had been revised upward on the whole; and (3) various policy measures such as tax breaks for business fixed investment would underpin firms' fixed investment. One of these members added that investment to prevent disasters and upgrade obsolete facilities was also expected. One member expressed the view that, while firms' transfer of production to overseas could weigh on domestic business fixed investment in manufacturing and on exports, an increase in firms' profits earned overseas could support Japan's economic growth through an improvement in the balance of income. Meanwhile, with regard to medium- to long-term developments in business fixed investment, one member expressed the opinion that it was important to achieve a heightening in medium- to long-term growth expectations through efforts by both the public and private sectors to strengthen the growth potential of Japan's economy.

As for the employment and income situation, members shared the recognition that supply and demand conditions in the labor market continued to improve steadily, albeit at a moderate pace, and employee income had also shown a pick-up. They agreed that a pick-up in employee income was likely to gradually become clearer as the recovery in economic activity and business performance became evident. One member pointed out that employment conditions were becoming increasingly tight, as evidenced by the fact that

(1) the active job openings-to-applicants ratio had risen and (2) in the December *Tankan*, the diffusion index for employment conditions (the proportion of firms responding that employment was "excessive" minus the proportion of those responding that employment was "insufficient") had registered its largest negative figure since November 1992 for nonmanufacturing and improved for manufacturing, reaching approximately zero. This member then expressed the view that, as for the outlook, positive effects on employee income -- including on scheduled cash earnings -- would spread on the back of the tightening in employment conditions and an improvement in corporate profits, as evidenced by the expected increase in winter bonus payments.

Members shared the recognition that private consumption remained resilient, with improvement in the employment and income situation. They shared the view that the front-loaded increase in demand prior to the consumption tax hike had started to play a role in consumption of durable consumer goods such as motor vehicles. Members concurred that private consumption was likely to remain resilient, supported mainly by improvement in the employment and income situation. One member expressed the opinion that, in addition to the improvement in the income situation, such as the increases in non-scheduled cash earnings and winter bonus payments, the pick-up in consumer sentiment reflecting the recent rise in stock prices would underpin future consumption. A few members pointed out that confidence remained relatively weak, although it had bounced back marginally in November 2013 after falling significantly in October. These members then said that this might be attributable to consumers' awareness of the consumption tax hike, and future developments warranted attention. One of these members pointed out that the rate of inflation -- including the effects of the consumption tax hike -- was likely to be higher than that of wage increases.

Members agreed that industrial production had been increasing moderately, reflecting these developments in demand both at home and abroad, and was likely to continue to do so.

Regarding prices, members shared the view that the year-on-year rate of increase in the CPI (all items less fresh food) was at around 1 percent and likely to rise for the time being, as seen in the CPI for the Tokyo metropolitan area for November, reaching slightly over 1 percent by the end of 2013. Many members pointed to the fact that the year-on-year rate of increase in the CPI (all items less food and energy) for October 2013 had risen to 0.3 percent and that the number of items for which prices had risen had exceeded those for which prices had declined. Based on this evidence, these members said that price rises had been observed not only in energy-related goods but also across a wide range of items. One of these members expressed the view that price indices based on the point-of-sale (POS) data released by private institutions also suggested price rises across a wide range of items other than energy-related goods. Some members said that prices would continue to increase moderately, partly reflecting the rise in medium- to long-term inflation expectations. Meanwhile, a few members expressed the recognition that, although the recent depreciation of the yen was likely to boost prices for the time being, the pace of the rise in the year-on-year rate of increase in the CPI would gradually lessen thereafter. Members shared the recognition that inflation expectations appeared to be rising on the whole, considering the results of various surveys and other information. Regarding medium- to long-term inflation expectations, a few members expressed the view that, although an increasing number of indicators recently suggested that such expectations were more or less unchanged, these expectations were clearly at an increased level from a relatively longer-term perspective and the rising trend was being maintained.

B. Financial Developments

Members concurred that financial conditions in Japan were accommodative. They shared the view that the monetary base had increased significantly, reflecting the progress in asset purchases by the Bank, and that firms' funding costs had been hovering at low levels. Members shared the recognition that firms continued to see financial institutions' lending attitudes as being on an improving trend, issuing conditions for CP continued to be favorable, and those for corporate bonds also remained favorable on the whole. As for firms' credit demand, they concurred that the amount outstanding of bank lending had been increasing moderately and that, in this situation, the year-on-year rate of growth in the money stock had been rising. Many members pointed out that the December 2013 *Tankan* indicated that the diffusion index of financial positions of firms had been improving on the whole, with that of small firms' positions notably reaching a level last seen in August 1991, and then expressed the recognition that such survey results reconfirmed that financial conditions were accommodative.

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

Based on the above assessment of economic and financial developments, members discussed monetary policy for the immediate future.

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 conduct money market operations so that the monetary base would increase at an annual pace of about 60-70 trillion yen.

With regard to the asset purchases, members concurred that it was appropriate for the Bank to continue with the guidelines decided when it introduced quantitative and qualitative monetary easing at the meeting on April 3 and 4, 2013. Specifically, they confirmed the following. First, the Bank would purchase JGBs so that their amount outstanding would increase at an annual pace of about 50 trillion yen, and the average remaining maturity of the Bank's JGB purchases would be about seven years. Second, it would purchase exchange-traded funds (ETFs) and Japan real estate investment trusts (J-REITs) so that their amounts outstanding would increase at an annual pace of about 1 trillion yen and about 30 billion yen, respectively. And third, for CP and corporate bonds, the Bank would continue with these asset purchases until their amounts outstanding reached 2.2 trillion yen and 3.2 trillion yen, respectively, by end-2013; thereafter, it would maintain these amounts outstanding.

With respect to the Bank's thinking behind its conduct of monetary policy, most members shared the recognition that the Bank would continue with quantitative and qualitative monetary easing, aiming to achieve the price stability target of 2 percent, as long as it was necessary for maintaining this target in a stable manner. These members continued that, in doing so, it would examine both upside and downside risks to economic activity and prices, and make adjustments as appropriate. Members expressed the view that it was appropriate for the Bank to continue to steadily pursue quantitative and qualitative monetary easing in accordance with the current guidelines, taking into account that Japan's economic and price developments had been broadly in line with the forecasts presented in October 2013 and that risks -- particularly those surrounding overseas economies -- had decreased.

On the other hand, one member said that, if a rise were to occur in markets' anticipation that quantitative and qualitative monetary easing would continue for a protracted period or extreme additional measures would be implemented in a situation where it was unlikely that the price stability target would be achieved in about two years, this could lead to economic instability in the medium to long term, such as through a buildup of financial imbalances. On this basis, the member said that it was appropriate to change the expression representing the Bank's commitment by stating that the time frame for continuing quantitative and qualitative monetary easing should be restricted to about two years, and that thereafter the Bank would review the monetary easing measures in a flexible manner.

With regard to the effects of quantitative and qualitative monetary easing, members shared the recognition that these continued to firmly take hold, and financial conditions were easing steadily to underpin firms' and households' spending. Regarding how much of an effect could be exerted on longer-term interest rates, they agreed that long-term interest rates in Japan had been stable at low levels under the Bank's massive JGB purchases. Members shared the recognition that, in a situation where nominal interest rates had been stable, real interest rates were declining on the back of a rise in inflation expectations. Meanwhile, a few members, while pointing out that the year-on-year rate of growth in broadly-defined liquidity was rising due, for example, to an increase in investment trusts, expressed the view that portfolio rebalancing, mainly by households, was proceeding steadily.

With regard to mechanisms in which inflation expectations would rise, some members expressed the view that both of the following would operate: (1) a forward-looking mechanism in which fundamental changes in people's expectations would be encouraged mainly through quantitative and qualitative monetary easing; and (2) a backward-looking mechanism in which inflation expectations would rise in adapting to an actual increase in prices. On this basis, these members expressed the recognition that, if the observed inflation rate exceeded 1 percent on a year-on-year basis in the future, the backward-looking mechanism would operate more effectively, and so would the forward-looking mechanism as the price stability target of 2 percent gained more confidence. A different member pointed to the possibility that the simultaneous price increases associated with the consumption tax hikes would contribute to an increase in people's medium- to long-term inflation expectations.

Regarding the Bank's communication to the public, some members said that it was necessary for the Bank to provide a more thorough explanation to the public regarding the path to achieving the price stability target of 2 percent, since there was some skepticism in this regard, particularly in the market. In relation to this issue, a few members noted that, if the Bank facilitated a better understanding of the guideline -- namely, that it "will continue with quantitative and qualitative monetary easing, aiming to achieve the price stability target of 2 percent, as long as it is necessary for maintaining that target in a stable manner" -- this would lead to the smoother transmission of various effects of quantitative and qualitative monetary easing. One member pointed to the need to increase recognition that the expression "as long as it is necessary" in the guideline indicated that the Bank would make judgments based on future prospects. Some members pointed out that the Bank should provide a clearer explanation to the public that the following was already factored into the Policy Board members' baseline scenario of the economic outlook -- that is, that the growth rate for the January-March quarter of 2014 would be elevated due to the front-loaded increase in demand prior to the consumption tax hike, and that the rate for the April-June quarter would temporarily drop as demand subsequently declined.

IV. Remarks by Government Representatives

The representative from the Cabinet Office made the following remarks.

(1) The Japanese economy was on its way to recovery at a moderate pace. As for the outlook, the recovery was expected to take hold as household income and business investment continued to be on upward trends while exports moved toward a pick-up and the effects of a range of policies developed. The government had been working toward accelerating and strengthening the implementation of the growth strategy. It would further work on strengthening the growth potential of the economy by steadily formulating measures based on growth strategy-related acts, such as the Industrial Competitiveness Enhancement Act and the Act on National Strategic Special Zones, both of which had been passed in the extraordinary session of the Diet.

(2) The Cabinet had decided the Economic Measures for Realization of Virtuous Cycles on December 5, 2013. This aimed to (1) mitigate the effects of the consumption tax hike and (2) realize an early return of the Japanese economy to a growth path by enhancing economic growth potential. The government had secured financial resources of a scale

exceeding 5 trillion yen by utilizing, for example, a natural increase in tax revenue, rather than increasing the issuance of government bonds. It expected that the economic impact of the measures on real GDP would be an increase of approximately 1 percent while that on job creation would amount to approximately 250 thousand people. The Cabinet would approve the government's economic outlook for fiscal 2014 -- including the economic impacts of the measures -- on December 21, 2013.

(3) The Cabinet had decided the guidelines for formulating the budget for fiscal 2014 on December 12, 2013. These aimed to create a positive cycle of (1) overcoming deflation and revitalizing the economy as well as (2) fiscal consolidation, by focusing on measures that would contribute to economic growth, after thoroughly reviewing the budget without any exception, including mandatory expenses such as social security. Based on these guidelines, the government would formulate the budget for fiscal 2014. In consideration of the discussions held, for example, at the Government-Labor-Management Meetings, the government had decided to end a year ahead of schedule the special corporate tax for reconstruction that had followed the Great East Japan Earthquake, on the condition that the financial resources for the reconstruction of approximately 25 trillion yen would be secured as previously arranged. The government would realize a positive cycle of the economy by taking advantage of the recent improvement in corporate profits to bring about wage increases.

(4) Deflation was ending in Japan, but the overcoming of deflation was only halfway accomplished. Therefore, the government deemed it necessary to pay due attention to price developments and the downside risks to the economy stemming from the slowdown in overseas economies. It expected the Bank to continue its efforts to achieve the price stability target of 2 percent.

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

(1) The Japanese economy was moving steadily on its upward trend. The overcoming of deflation was still only halfway accomplished, and therefore the government expected the Bank to continue to steadily pursue quantitative and qualitative monetary easing and achieve the price stability target of 2 percent at the earliest possible time.

(2) As part of the economic policy package, decided in October 2013, the government had decided the Economic Measures for Realization of Virtuous Cycles with a national

expenditure of 5.5 trillion yen, which included the end a year ahead of schedule to the special corporate tax for reconstruction that had followed the Great East Japan Earthquake. In order to implement these measures, it also formulated the supplementary budget for fiscal 2013. In line with these measures, it would carry out taxation measures on a scale of 1 trillion yen, including tax breaks for business fixed investment, and encourage cooperative efforts by government, labor, and business communities, thereby mitigating the effects of the consumption tax hike and ensuring that the Japanese economy would see an early return to a growth path.

(3) With regard to the budget for fiscal 2014, the Cabinet had decided the guidelines for its formulation. The government would aim to improve the primary balance of the initial budget for the general account by more than 4 trillion yen and do its utmost to reduce the amount of newly issued government bonds to below the level of fiscal 2013. It would formulate a quality-based budget by emphasizing priorities in the budget allocation to be decided at the forthcoming Cabinet meeting.

(4) As for the tax reform in fiscal 2014, the ruling parties had compiled an outline for tax reform, which contained additional measures to stimulate private investment and consumption, as well as revision of vehicle taxation. Taking into account the ruling parties' outline, the government would prepare to formulate a bill for the tax reform.

(5) In order to accelerate and strengthen the implementation of the Japan Revitalization Strategy, nine related acts, including the Industrial Competitiveness Enhancement Act and the Act on National Strategic Special Zones, had been passed in the previous extraordinary session of the Diet. In addition, the Panel for Vitalizing Financial and Capital Markets had released its recommendations to effectively utilize abundant financial assets held by households, for example, and revitalize the Japanese economy.

(6) Through these measures, the government would promote the enhancement and stabilization of the social security system and pursue fiscal consolidation while enhancing the growth potential of the Japanese economy.

V. Votes

Based on the above discussions, members shared the view that it was appropriate to maintain the current guideline for money market operations, so that the monetary base would increase at an annual pace of about 60-70 trillion yen.

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 conduct money market operations so that the monetary base will increase at an annual pace of about 60-70 trillion yen.

2. A public statement will be decided separately.

Votes for the proposal: Mr. H. Kuroda, Mr. K. Iwata, Mr. H. Nakaso, Mr. R. Miyao, Mr. Y. Morimoto, Ms. S. Shirai, Mr. K. Ishida, Mr. T. Sato, and Mr. T. Kiuchi.
Votes against the proposal: None.

VI. Discussion on the Statement on Monetary Policy

On the basis of the above discussions, members discussed the Statement on Monetary Policy and formed a majority view. One member, however, formulated a proposal, and thus the following two proposals were submitted.

A. Mr. T. Kiuchi's Policy Proposal

With regard to the draft of the statement that formed a majority view, Mr. T. Kiuchi proposed changing the current expression of the Bank's future monetary policy stance that "the Bank will continue with quantitative and qualitative monetary easing, aiming to achieve the price stability target of 2 percent, as long as it is necessary for maintaining that target in a stable manner. It will examine both upside and downside risks to economic activity and prices, and make adjustments as appropriate" to a new expression that "the Bank will aim to achieve the price stability target of 2 percent in the medium to long term. On this basis, it will designate quantitative and qualitative monetary easing as an intensive measure with a time frame of about two years, and thereafter will review the monetary easing measures in a flexible manner." The proposal was then put to a vote.

The proposal was defeated by a majority vote.

Votes for the proposal: Mr. T. Kiuchi.

Votes against the proposal: Mr. H. Kuroda, Mr. K. Iwata, Mr. H. Nakaso, Mr. R. Miyao, Mr. Y. Morimoto, Ms. S. Shirai, Mr. K. Ishida, and Mr. T. Sato.

B. The Chairman's Policy Proposal

The chairman formulated the Statement on Monetary Policy, 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).

VII. Approval of the Minutes of the Monetary Policy Meeting

The Policy Board approved unanimously the minutes of the Monetary Policy Meeting of November 20 and 21, 2013 for release on December 26, 2013.

VIII. Approval of the Scheduled Dates of the Monetary Policy Meetings in January-December 2014

At the end of the meeting, the Policy Board approved unanimously the dates of the Monetary Policy Meetings to be held in the period of January-December 2014 for immediate release (see Attachment 2).

Attachment 1

December 20, 2013

Bank of Japan

Statement on Monetary Policy

1. At the Monetary Policy Meeting held today, the Policy Board of the Bank of Japan decided, by a unanimous vote, to set the following guideline for money market operations for the intermeeting period:

   The Bank of Japan will conduct money market operations so that the monetary base will increase at an annual pace of about 60-70 trillion yen.

2. With regard to the asset purchases, the Bank will continue with the following guidelines:

   a) The Bank will purchase Japanese government bonds (JGBs) so that their amount outstanding will increase at an annual pace of about 50 trillion yen, and the average remaining maturity of the Bank's JGB purchases will be about seven years.

   b) The Bank will purchase exchange-traded funds (ETFs) and Japan real estate investment trusts (J-REITs) so that their amounts outstanding will increase at an annual pace of about 1 trillion yen and about 30 billion yen respectively.

   c) As for CP and corporate bonds, the Bank will continue with those asset purchases until their amounts outstanding reach 2.2 trillion yen and 3.2 trillion yen respectively by end-2013; thereafter, it will maintain those amounts outstanding.

3. Japan's economy has been recovering moderately. Overseas economies as a whole are picking up moderately, although a lackluster performance is partly seen. In this situation, exports have generally been picking up. Business fixed investment has been picking up as corporate profits have improved. Public investment has continued to increase, and housing investment has also increased. Private consumption has remained resilient, with improvement in the employment and income situation. Reflecting these developments in demand both at home and abroad, industrial production has been increasing moderately. Improvement in business sentiment has continued and become widespread. Meanwhile, financial conditions are accommodative. On the price front, the year-on-year rate of change

in the consumer price index (CPI, all items less fresh food) is at around 1 percent. Inflation expectations appear to be rising on the whole.

4. With regard to the outlook, Japan's economy is expected to continue a moderate recovery as a trend, while it will be affected by the front-loaded increase and subsequent decline in demand prior to and after the consumption tax hike. The year-on-year rate of increase in the CPI is likely to rise for the time being.

5. Regarding risks, there remains a high degree of uncertainty concerning Japan's economy, including the prospects for the European debt problem, developments in the emerging and commodity-exporting economies, and the pace of recovery in the U.S. economy.

6. The Bank will continue with quantitative and qualitative monetary easing, aiming to achieve the price stability target of 2 percent, as long as it is necessary for maintaining that target in a stable manner. It will examine both upside and downside risks to economic activity and prices, and make adjustments as appropriate.[Note]

   Such conduct of monetary policy will support the positive movements in economic activity and financial markets, contribute to a rise in inflation expectations, and lead Japan's economy to overcome the deflation that has lasted for nearly 15 years.

[Note] Mr. T. Kiuchi proposed that the Bank will aim to achieve the price stability target of 2 percent in the medium to long term and designate quantitative and qualitative monetary easing as an intensive measure with a time frame of about two years. The proposal was defeated by an 8-1 majority vote. Voting for the proposal: Mr. T. Kiuchi. Voting against the proposal: Mr. H. Kuroda, Mr. K. Iwata, Mr. H. Nakaso, Mr. R. Miyao, Mr. Y. Morimoto, Ms. S. Shirai, Mr. K. Ishida, and Mr. T. Sato.

Attachment 2
December 20, 2013
Bank of Japan

Scheduled Dates of Monetary Policy Meetings in January 2014-December 2014

	Date of MPM	Publication of MPM Minutes	Publication of Outlook Report (The Bank's View)	(Reference) Publication of Monthly Report
Jan. 2014	21 (Tues.), 22 (Wed.)	Feb. 21 (Fri.)	--	23 (Thurs.)
Feb.	17 (Mon.), 18 (Tues.)	Mar. 14 (Fri.)	--	19 (Wed.)
Mar.	10 (Mon.), 11 (Tues.)	Apr. 11 (Fri.)	--	12 (Wed.)
Apr.	7 (Mon.), 8 (Tues.)	May 7 (Wed.)	--	9 (Wed.)
	30 (Wed.)	May 26 (Mon.)	30 (Wed.)	--
May	20 (Tues.), 21 (Wed.)	June 18 (Wed.)	--	22 (Thurs.)
June	12 (Thurs.), 13 (Fri.)	July 18 (Fri.)	--	16 (Mon.)
July	14 (Mon.), 15 (Tues.)	Aug. 13 (Wed.)	--	16 (Wed.)
Aug.	7 (Thurs.), 8 (Fri.)	Sep. 9 (Tues.)	--	11 (Mon.)
Sep.	3 (Wed.), 4 (Thurs.)	Oct. 10 (Fri.)	--	5 (Fri.)
Oct.	6 (Mon.), 7 (Tues.)	Nov. 6 (Thurs.)	--	8 (Wed.)
	31 (Fri.)	Nov. 25 (Tues.)	31 (Fri.)	--
Nov.	18 (Tues.), 19 (Wed.)	Dec. 25 (Thurs.)	--	20 (Thurs.)
Dec.	18 (Thurs.), 19 (Fri.)	To be announced	--	22 (Mon.)

Note: The time of release will be, in principle, as follows.

MPM Minutes will be released at 8:50 a.m.

Outlook for Economic Activity and Prices (Outlook Report):
"The Bank's View" in the Outlook Report will be released at 3:00 p.m., and the full text at 2:00 p.m. on the next business day. As an exception to this principle, the full text of the October 2014 Outlook Report will be released at 2:00 p.m. on November 1 (Sat.), 2014.

Monthly Report of Recent Economic and Financial Developments (Monthly Report):
The Japanese original and the English translation for summary will be released at 2:00 p.m. (the English translation for the full text will be published at 4:30 p.m. on the next business day).