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October 10, 2014

Bank of Japan

Minutes of the Monetary Policy Meeting

on September 3 and 4, 2014

(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 Wednesday, September 3, 2014, from 2:00 p.m. to 4:32 p.m., and on Thursday, September 4, from 9:00 a.m. to 12:02 p.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. H. Sakota, Deputy Vice Minister for Policy Planning and Coordination, Ministry of Finance

Mr. M. Maekawa, Director-General, Economic and Fiscal Management, Cabinet Office

Reporting Staff

Mr. M. Amamiya, Executive Director

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

Mr. S. Kuwabara, Executive Director

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

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

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[1] The minutes of this meeting were approved by the Policy Board at the Monetary Policy Meeting held on October 6 and 7, 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.

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

Mr. S. Nagai, 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. Y. Komaki, Senior Economist, Monetary Affairs Department

Mr. S. Watanabe, Senior Economist, Monetary Affairs Department

I. Summary of Staff Reports on Economic and Financial Developments[2]

A. Money Market Operations in the Intermeeting Period

The Bank, in accordance with the guideline decided at the previous meeting on August 7 and 8, 2014, had been providing funds through purchases of Japanese government bonds (JGBs) and other measures.[3] In this situation, the amount outstanding of the monetary base had been in the range of 238-245 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 and general collateral (GC) repo rates had generally been at levels below 0.1 percent. As for interest rates on term instruments, yields on treasury discount bills (T-Bills) had been at an extremely low level. Interbank rates had been flat.

Yields on 10-year JGBs had decreased somewhat amid declining interest rates in advanced economies, particularly in Europe, and had recently been at around 0.5 percent. The Nikkei 225 Stock Average had fallen temporarily, reflecting concerns about geopolitical risks, but had increased thereafter, mainly in response to the rise in U.S. and European stock prices. It had recently been in the range of 15,500-16,000 yen. Yield spreads between corporate bonds and JGBs continued to narrow very moderately as a trend, reflecting solid demand from investors. In the foreign exchange market, the yen had depreciated against the U.S. dollar, and the U.S. dollar/yen rate had recently been in the range of 104-105 yen. The euro had depreciated against the dollar.

C. Overseas Economic and Financial Developments

Overseas economies -- mainly advanced economies -- had been recovering, albeit with a lackluster performance still seen in part.

The U.S. economy steadily continued on its moderate recovery, led by private demand. Private consumption remained firm, on the back of a continued rise in asset prices and steady expansion in employment. Housing investment had been on a moderate

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

[3] 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.

pick-up trend. Exports also remained on an increasing trend. Reflecting these developments in demand, business sentiment and the momentum in production activity remained firm, and the pick-up in business fixed investment had recently become increasingly evident. 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 climbed, particularly for services such as medical care and related items as well as rent. Meanwhile, the year-on-year rate of increase in the CPI for all items had been higher than that in the core CPI, because energy and food price increases had been somewhat pronounced.

The European economy continued to recover moderately, although its momentum was slowing somewhat. Private consumption had shown a moderate recovery, with the continued improving trend in consumer sentiment, although the employment and income situation remained severe. Business fixed investment continued to see movements toward a pick-up, particularly in Germany. On the other hand, although exports to the United States and China continued to increase, those to emerging economies had decreased, and thus the pace of the pick-up in exports overall had slowed recently. Reflecting these developments in demand and heightened geopolitical risks, the growth momentum in the manufacturing industry had slowed. On the other hand, sentiment and business activity in the services industry had been steady. As for prices, slack in supply and demand conditions in the goods and labor markets was exerting downward pressure on prices, and the year-on-year rates of increase in both the Harmonized Index of Consumer Prices (HICP) excluding energy and unprocessed food and the HICP for all items remained low. Meanwhile, economic activity in the United Kingdom continued to recover, led mainly by domestic demand.

With regard to Asia, the Chinese economy continued to see stable growth due to policy measures from both the monetary and fiscal sides to underpin economic activity and to improvements in external demand. Exports had increased, particularly those to the United States and Europe as well as to some Asian countries. On the other hand, although fixed asset investment had been underpinned by public investment, its pace of increase had slowed, mainly in real estate investment. Stable growth in private consumption continued against the background of a favorable employment and income situation. The pace of growth in production, particularly of machinery for shipment overseas, had been stable on the whole. Economic developments in the NIEs were generally picking up somewhat on the back of recovery in external demand, although differences by country stood out somewhat. On the other hand, growth momentum in the ASEAN economies remained weak on the whole -- especially in Thailand -- although improvements were starting to spread in exports and private consumption. In India, the economy was bottoming out on the back of recovery in exports and a pick-up in private consumption.

As for prices of emerging economies, there were differences by country and region. Specifically, the year-on-year rates of increase in the CPI had been at low levels as a trend in China, the NIEs, Thailand, and Central and Eastern Europe. On the other hand, inflation rates in Brazil, Russia, and South Africa had been rising again, mainly due to the effects of the earlier depreciation of their currencies and the increase in food prices. Inflation rates in Malaysia and the Philippines had also been rising somewhat.

Global financial markets were showing signs of returning to a situation where stock prices were high and long-term interest rates were at low levels in an environment of low volatility, as concerns about geopolitical risks had eased somewhat. Markets in emerging economies had generally been calm in a situation where inflow of funds continued, in particular to stock markets, although some markets had shown nervousness associated with the situation in Russia. Regarding international commodity prices, while prices of industrial metals had risen, those of crude oil and agricultural products continued to decline.

D. Economic and Financial Developments in Japan

1. Economic developments

Exports had shown some weakness. Real exports had declined slightly for two consecutive quarters in the January-March and April-June quarters of 2014 on a quarter-on-quarter basis, but marked a slight increase in July relative to the April-June quarter. Exports were expected to head for a moderate increase, mainly against the background of the recovery in overseas economies.

Public investment had more or less leveled off at a high level. It was expected to continue to stay at around this level, due to the effects of the supplementary budget for fiscal 2013 and to the early implementation of the initial budget for fiscal 2014.

Business fixed investment had increased moderately as corporate profits had improved. Corporate results of listed companies for the April-June quarter had on the whole shown a slight increase in profits that exceeded market expectations, and business sentiment had generally stayed at a favorable level. As for the outlook, firms were likely to maintain their positive attitude toward business fixed investment, and business fixed investment was projected to follow a moderate increasing trend as corporate profits continued their improving trend.

As for the employment and income situation, supply and demand conditions in the labor market continued to improve steadily, as evidenced by the continued rise in the job openings-to-applicants ratios and the moderate improving trend in the unemployment rate. Regarding wages, nominal wages per employee had picked up, as non-scheduled cash earnings and special cash earnings had increased and as scheduled cash earnings had stopped declining and were heading toward a pick-up. The year-on-year rate of increase in employee income had been climbing moderately.

Private consumption remained resilient as a trend with the employment and income situation improving steadily, and the effects of the subsequent decline in demand following the front-loaded increase prior to the consumption tax hike had gradually begun to wane. Although sales at retail stores in real terms had increased at a significantly accelerated pace in the January-March quarter due to the front-loaded increase in demand, and had fallen back substantially in the April-June quarter due to the decline in demand following the front-loaded increase, they increased slightly in July relative to the April-June quarter. Sales at department stores and supermarkets had tended to pick up since May. The number of new passenger-car registrations had marked a substantial decline in April, and had been almost flat since May. Sales of household electrical appliances in real terms had decreased significantly in the April-June quarter, and were flat in July compared with the April-June quarter. The latest interviews with firms suggested that, in sectors relating to retail sales as a whole, the effects of the decline in demand following the front-loaded increase seemed to have been waning gradually, but the pace of pick-up had slowed somewhat, due in part to the effects of the recent irregular weather. Private consumption was expected to remain resilient with the employment and income situation continuing to improve steadily, and the effects of the decline in demand following the front-loaded increase were expected to wane further.

As for housing investment, a subsequent decline following the front-loaded increase continued. It was expected to regain its resilience gradually with the employment and income situation continuing to improve steadily, supported as well by accommodative financial conditions, while the effects of the decline following the front-loaded increase were expected to remain for the time being.

Industrial production had recently shown some weakness, mainly reflecting the subsequent decline in demand following the front-loaded increase and sluggishness in exports, although it continued to increase moderately as a trend. It was expected to follow a moderate increasing trend, albeit with some weakness remaining for the time being, and the effects of the decline in demand following the front-loaded increase were expected to wane gradually.

As for prices, excluding the direct effects of the consumption tax hike, producer prices were rising moderately relative to three months earlier. The year-on-year rate of increase in the CPI (all items less fresh food) was around 1¼ percent. With regard to the outlook, producer prices were expected to continue rising moderately for the time being, and the year-on-year rate of increase in the CPI (all items less fresh food) was likely to be around 1¼ percent for some time. Meanwhile, inflation expectations appeared to be rising on the whole.

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 at around 40 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 and corporate bonds continued to be favorable. 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 in the range of 2.0-2.5 percent. Firms' financial positions had improved further. Meanwhile, the year-on-year rate of growth in the money stock had been at around 3 percent, mainly due to the increase in bank lending.

3. The fund-provisioning measure to support strengthening the foundations for economic growth

On September 5, 2014, the Bank was scheduled to carry out a new loan disbursement, amounting to 656.8 billion yen, under the main rules for the fund-provisioning measure to support strengthening the foundations for economic growth (hereafter the Growth-Supporting Funding Facility). The outstanding balance of loans disbursed by the Bank under these rules would amount to 3,736.0 billion yen after the new loan disbursement. The outstanding balance of loans disbursed by the Bank under the special rules for equity investments and asset-based lending (ABL) was scheduled to be 100.4 billion yen, and that under the special rules for small-lot investments and loans to be 8.596 billion yen. The outstanding balance of loans under the special rules for the U.S. dollar lending arrangement was scheduled to be 11.95 billion dollars.

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

A. Economic Developments

Members shared the view that global financial markets had been returning to a situation where interest rates were declining and at the same time stock prices were rising amid decreasing volatility, as concerns about geopolitical risks had eased somewhat. On this basis, they shared the recognition that it was necessary to continue to monitor future developments in the international situation and how they would affect global financial markets and the global economy. Some members pointed to the risk of a rise in volatility, triggered mainly by changes in market participants' views on each country's economic activity and prices as well as policy conduct. One member added that overseas long-term interest rates, which had been on a declining trend, were recently showing signs of bottoming out, reflecting a clear improvement in the U.S. economy.

Members concurred that overseas economies -- mainly advanced economies -- had been recovering, albeit with a lackluster performance still seen in part of the emerging economies. As for the outlook, they shared the recognition that overseas economies -- mainly advanced economies -- would continue to recover moderately.

With regard to developments in overseas economies by region, members agreed that the U.S. economy steadily continued on its moderate recovery, led by private demand, as private consumption had been firm on the back of improvement in the employment situation and such positive movements were spreading to the corporate sector, leading to the pick-up in business fixed investment, which had become increasingly evident. As for the outlook, they shared the view that the economy was likely to gradually accelerate its pace of recovery.

Members shared the recognition that the euro area economy was recovering moderately, as firms' and households' sentiment continued to improve in a situation where the area's financial markets had been stable, although the economy's momentum was slowing somewhat. At the same time, they shared the view that it was necessary to keep paying attention to the continued moderate disinflationary trend. A few members pointed to the possibility that medium- to long- term inflation expectations were declining. As for the outlook, members agreed that the economy would likely continue to recover under accommodative financial conditions, but the pace would probably remain moderate, given structural problems such as excess debt. Some members expressed concern about the effects of the Russian-Ukrainian problem on the euro area economy. One member said that the results yet to be released of the asset quality review and stress tests conducted on major European banks, as well as the recapitalization measures based on these results, were important to the outlook for restoration of the financial intermediary function of the European banking system and for the euro area economy.

Members agreed that the Chinese economy continued to see stable growth as the government's mini-stimulus measures were producing effects and exports were increasing. As for the outlook, they concurred that the economy would generally maintain stable growth at around the current pace. A few members added that the risk of larger adjustments in the real estate market warranted attention. One member commented that the current structural reforms were likely to have positive effects on the Chinese economy in the long run and that domestic demand remained firm. A different member, noting that it would not be easy for the economy to shift from being external demand-driven to being domestic demand-driven, pointed to the possibility that, in the course of such structural change, the economy would decelerate more than expected.

With regard to emerging economies including the NIEs and the ASEAN economies, members shared the view that emerging economies as a whole remained lackluster in terms of growth, although the number of countries and regions where economic activity had been picking up had been increasing gradually as the positive effects of recovery -- mainly in the U.S. and Chinese economies -- had been spreading. On this basis, they shared the view that the pace of growth in emerging economies was likely to gradually rise since the recovery trend in advanced economies was likely to continue.

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 concurred that the economy continued to recover moderately as a trend, as a virtuous cycle from income to spending had been operating steadily in both the household and corporate sectors, although the subsequent decline in demand following the front-loaded increase prior to the consumption tax hike was still observed and exports and production had shown some weakness. As for the outlook for the economy, they shared the view that it was likely to continue its moderate recovery trend, and the effects of the decline in demand following the front-loaded increase prior to the consumption tax hike were likely to wane gradually.

Members agreed that Japan's exports continued to show some weakness. Some members pointed out that this reflected to some extent structural factors such as the shift of Japanese manufacturers' production sites to overseas. A few members noted that, although real exports for July had increased, it was necessary to examine whether they would continue to do so in a sustainable manner. As for the outlook, members shared the view that exports were likely to head for a moderate increase, mainly against the background of the recovery in overseas economies. Meanwhile, one member pointed out that the recovery in business fixed investment in Europe and emerging economies had been lackluster, and expressed the view that it would take some time for exports to start increasing steadily.

Members shared the view that business fixed investment had increased moderately, mainly on the back of the continued improvement in corporate profits, and was projected to follow a moderate increasing trend. A few members noted that an increase in profits from overseas business operations had been pushing up large firms' profits. Moreover, some members expressed the view that firms had maintained their positive attitude toward business fixed investment on the back of firm business sentiment.

As for the employment and income situation, members shared the view that, in a situation where supply and demand conditions in the labor market continued to improve steadily, employee income had increased moderately and was likely to continue to do so. A few members noted that, in the *Monthly Labour Survey*, (1) scheduled cash earnings had turned positive on a year-on-year basis, which seemed to indicate that the impact of a rise in base pay had started to appear in the data; and (2) the rate of increase in special cash earnings had been climbing as well, reflecting the increase in summer bonus payments. A few members pointed out that, although real wages calculated using the inflation rate that included the effects of the consumption tax hike had declined, their year-on-year rate of change had registered positive growth when excluding such effects. One member said that, in order to increase income, including base pay, an arrangement involving the government similar to the one made last year might also be necessary this year. Meanwhile, one member noted that the pace of improvement in the employment situation had slowed somewhat, as evidenced, for example, by the rise in the unemployment rate. This member continued that this could be attributable to the fact that exports and production had recently shown some weakness. A different member commented that it was necessary to closely monitor whether the economy's capacity to generate income would be maintained, given that developments in employment and income lagged behind those in the economy in general.

With regard to the effects of tight labor market conditions on wages, one member noted that the rate of increase in wages could remain moderate owing to lackluster growth in aggregate demand in a situation where the economic growth rate had not been rising, due in part to labor supply constraints. A different member noted that firms had been working to draw out the potential labor supply, and thus there was a possibility that wages were increasing moderately and the potential growth rate was rising on the back of increases on both the demand and supply sides of the labor market. Another member said that investment to promote labor saving by firms facing labor shortages could boost labor productivity, leading to an increase in the growth potential of Japan's economy.

With respect to private consumption, members agreed that the effects of the subsequent decline in demand following the front-loaded increase were still observed but had gradually begun to wane on the whole. They shared the view that, regarding household spending, given the significant scale of the front-loaded increase in demand with regard to the consumption of durable goods including motor vehicles and housing investment, the pace of recovery in such demand from the subsequent decline was moderate.

They noted, however, that sales at department stores and supermarkets had been following a pick-up trend, with monthly fluctuations taken into consideration. Some members pointed out that the effects of the irregular summer weather were making it difficult to grasp underlying developments in recent consumption. These members then said that the improvement in sales at major department stores for August indicated that consumption had been resilient. Moreover, some members referred to the fact that developments in consumption indicated by the *Family Income and Expenditure Survey* -- demand-side statistics -- had recently been somewhat weak compared to those indicated by sales-side statistics. These members then pointed to the possibility that, in view of the results of the *Monthly Labour Survey*, the income growth of households currently being surveyed might have been lower than the underlying level, and thus their consumption growth might be downward biased. With regard to the outlook, members shared the view that private consumption was likely to remain resilient as the employment and income situation continued to improve steadily, and as consumer sentiment had also been improving. Meanwhile, one member noted that it was necessary to carefully examine developments in consumption given that some indicators for household sentiment showed relatively weak developments.

Members agreed that industrial production had recently shown some weakness, mainly reflecting the effects of the subsequent decline in demand following the front-loaded increase, although it continued to increase moderately as a trend. In this regard, some members pointed out that inventory adjustments were taking place in some industries, such as automobiles. With regard to the outlook, members shared the view that, based on the production forecast index and survey results, industrial production was likely to follow a moderate increasing trend, albeit with some weakness remaining for the time being, and the effects of the decline in demand following the front-loaded increase were likely to wane gradually. Meanwhile, one member pointed to the need to pay attention to the risk that inventory adjustments in the automobile industry would spread to other industries.

Regarding <u>prices</u>, members concurred that, excluding the direct effects of the consumption tax hike, the year-on-year rate of increase in the CPI (all items less fresh food) was likely to be around 1¼ percent for some time, albeit with some temporary slowdown in the rate of increase. Most members shared the view that, thereafter, the rate of increase was likely to follow a rising trend again from the second half of fiscal 2014 as the output gap continued to improve steadily and medium- to long-term inflation expectations rose. In relation to this, a few members expressed the view that firms' moves to pass on increases in costs, including labor costs, to sales prices would lead to pushing up general prices. On the other hand, one member pointed out that price indices based on retail sales data had recently been on a declining trend, and said that attention should be paid to the risk that firms' price-setting stance might change in a situation where the subsequent decline in demand following the front-loaded increase became protracted. On the subject of inflation expectations, some members commented that the breakeven inflation rates were declining recently. On this point, many members noted that it was important to continue to carefully monitor developments in inflation expectations, using various indicators such as (1) surveys conducted on households, firms, and economists as well as (2) market interest rates.

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 agreed that firms' financial positions had improved further, as firms continued to see financial institutions' lending attitudes as being on an improving trend and issuing conditions for CP and corporate bonds continued to be favorable. They shared the view that firms' credit demand had been increasing moderately, and that the amount outstanding of bank lending, including that to small firms, had been increasing moderately.

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 maintain their amounts outstanding at about 2.2 trillion yen and about 3.2 trillion yen, respectively.

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, as such easing had been exerting its intended effects.

On the other hand, one member expressed the view 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 continued 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. Furthermore, this member added that additional measures to stimulate demand carried the risk of growing financial imbalances or weakening the public's recognition of the need for structural reforms.

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. Many members expressed the recognition that the decline in overseas interest rates had also contributed to the stability of long-term interest rates in Japan at low levels recently. One member commented that, judging from various indicators, liquidity in the JGB market had not declined thus far but it was necessary to continue to analyze the effects the Bank's JGB purchases would have on the liquidity in the JGB market and on interest rate formation. Meanwhile, a different member said that, if the market judged that the government's commitment to achieving fiscal consolidation had weakened, there was a risk that monetary easing effects would be hindered through an expansion in risk premiums.

With regard to the Growth-Supporting Funding Facility, one member expressed the hope that, considering the increase in the amount of loans disbursed, the effective use of the facility would support private institutions' efforts to strengthen the growth potential of Japan's economy.

IV. Remarks by Government Representatives

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

(1) The real GDP growth rate for the April-June quarter of 2014 -- which had been released on August 13 -- was minus 6.8 percent on an annualized quarter-on-quarter basis, mainly due to the reaction in the Japanese economy after a last-minute rise in demand before the consumption tax increase. Averaging out the real GDP figures for the January-March and April-June quarters -- in order to grasp the economic trends by excluding the effects of the significant swing from the last-minute rise in demand to the subsequent decrease -- the average real GDP for the January-June period exceeded not only the level in the same period of the previous year but also the level in the preceding October-December quarter. In addition, the employment situation had been improving steadily. Based on these developments, the government acknowledged that the Japanese economy was on a moderate recovery trend, and the reaction after a last-minute rise in demand before the consumption tax increase was easing. It 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) The government had compiled and released on September 3 the fiscal 2015 budget requests based on requests submitted by ministries and agencies in accordance with the guidelines for budget requests for fiscal 2015, which had been approved by the Cabinet on July 25. The total amount of the fiscal 2015 budget requests and demands for the general account submitted by ministries and agencies was about 101.7 trillion yen, an increase of about 5.8 trillion yen from the fiscal 2014 budget. Fiscal 2015 was the deadline set to achieve the national and local governments' primary balance target of halving the ratio of the fiscal deficit to GDP. The Economic and Fiscal Projections for Medium- to Long-Term Analysis -- which had been released by the Cabinet Office recently -- suggested that achievement of the target was in sight. However, the projected figure differed from the target by only a small amount, and therefore such an achievement could not be viewed optimistically at all, and the government was in no position to reduce its efforts either on the revenue or expenditure sides. During the process of budget formulation going forward, it was necessary for the government to thoroughly examine the details of the budget requests and demands to ensure achievement of the target. The government would continue to work toward attaining both economic growth led by private demand and fiscal consolidation targets.

The representative from the Cabinet Office made the following remarks.

(1) The first preliminary estimate of the real GDP growth rate for the April-June quarter of 2014 -- which had been released by the Cabinet Office on August 13 -- was minus 6.8 percent on an annualized quarter-on-quarter basis, registering negative growth for the first time in two quarters, mainly due to the reaction after a last-minute rise in demand before the consumption tax increase. Averaging out the real GDP figures for the January-March and April-June quarters -- in order to grasp the economic trends by excluding the effects of the swing from the last-minute rise in demand to the subsequent decrease -- the average real GDP for the January-June period exceeded not only the level in the same period of the previous year but also the level in the preceding October-December quarter. In addition, developments in home appliance sales and sales at department stores showed a pick-up, and the employment situation was improving steadily. Based on these developments, the government considered that the Japanese economy was on a moderate recovery trend, and the reaction after a

last-minute rise in demand before the consumption tax increase was easing. As for the outlook, it would pay attention to the downside risks to the Japanese economy, such as the lengthening of the reaction after a last-minute rise in demand and the slowing down of overseas economies.

(2) On September 3, the Cabinet had been reshuffled; the government would continue to give top priority to promoting economic revitalization and thus commit to doing its utmost to overcome deflation and implement the growth strategy. On this basis, it would further ensure the path to economic recovery and deliver such recovery to every corner of Japan. One of the biggest challenges for the Cabinet was the creation of vital and prosperous local communities. In this regard, a minister in charge of overcoming the population decline and vitalizing local economy in Japan had been appointed and the Headquarters for Overcoming Population Decline and Vitalizing Local Economy in Japan had been established. The government would thoroughly address the issue of the various structural problems facing Japan, such as the declining and progressively aging population. It would also make full-fledged efforts to build up local regions so that they would be transformed into places where young people could feel pride and have dreams and hopes for the future, and where everyone could live with peace of mind. The government expected the Bank to continue its efforts to achieve the price stability target of 2 percent.

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. Mr. T. Kiuchi, however, formulated a proposal, and thus 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).

VII. Approval of the Minutes of the Monetary Policy Meeting

The Policy Board approved unanimously the minutes of the Monetary Policy Meeting of August 7 and 8, 2014 for release on September 9, 2014.

Attachment

September 4, 2014

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 maintain their amounts outstanding at about 2.2 trillion yen and about 3.2 trillion yen respectively.

3. Japan's economy has continued to recover moderately as a trend, although the subsequent decline in demand following the front-loaded increase prior to the consumption tax hike has been observed. Overseas economies -- mainly advanced economies -- have been recovering, albeit with a lackluster performance still seen in part. Exports have shown some weakness. Business fixed investment has increased moderately as corporate profits have improved. Public investment has more or less leveled off at a high level. Private consumption has remained resilient as a trend with the employment and income situation improving steadily, and the effects of the decline in demand following the front-loaded increase have gradually begun to wane. As for housing investment, a decline following the front-loaded increase has continued. Reflecting these developments in demand both at home and abroad, industrial production has recently shown some weakness, although it has continued to

increase moderately as a trend. Meanwhile, financial conditions are accommodative. On the price front, the year-on-year rate of increase in the consumer price index (CPI, all items less fresh food), excluding the direct effects of the consumption tax hike, is around 1¼ percent. Inflation expectations appear to be rising on the whole.

4. With regard to the outlook, Japan's economy is expected to continue its moderate recovery trend, and the effects of the subsequent decline in demand following the front-loaded increase prior to the consumption tax hike are expected to wane gradually. The year-on-year rate of increase in the CPI is likely to be around 1¼ percent for some time.

5. Risks to the outlook include developments in the emerging and commodity-exporting economies, the prospects for the European debt problem, and the pace of recovery in the U.S. economy.

6. Quantitative and qualitative monetary easing (QQE) has been exerting its intended effects, and the Bank will continue with the QQE, 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]

[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 the QQE 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.