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November 6, 2017

Bank of Japan

Minutes of the Monetary Policy Meeting

on September 20 and 21, 2017

(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 20, 2017, from 2:00 p.m. to 3:44 p.m., and on Thursday, September 21, from 9:00 a.m. to 12:08 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. Y. Harada

Mr. Y. Funo

Mr. M. Sakurai

Ms. T. Masai

Mr. H. Suzuki

Mr. G. Kataoka

Government Representatives Present

Mr. M. Kihara, State Minister of Finance, Ministry of Finance[2]

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

Mr. T. Ochi, State Minister of Cabinet Office, Cabinet Office[2]

Mr. M. Maekawa, Vice Minister for Policy Coordination, Cabinet Office[3]

Reporting Staff

Mr. M. Amamiya, Executive Director

Mr. S. Kuwabara, Executive Director

Mr. E. Maeda, Executive Director (Assistant Governor)

Mr. T. Kato, 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 October 30 and 31, 2017 as "a document describing an outline of the discussion at the meeting" stipulated in Article 20, paragraph 1 of the Bank of Japan Act of 1997. Those present are referred to by their titles at the time of the meeting.

[2] Messrs. M. Kihara and T. Ochi were present on September 21.

[3] Messrs. T. Kabe and M. Maekawa were present on September 20.

Mr. A. Okuno, Head of Policy Planning Division, Monetary Affairs Department

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

Mr. T. Sekine, Director-General, Research and Statistics Department

Mr. H. Ichiue, Head of Economic Research Division, Research and Statistics Department

Mr. Y. Nakata, Director-General, International Department

Secretariat of the Monetary Policy Meeting

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

Mr. H. Nakamoto, Director, Deputy Head of Planning and Coordination Division, Secretariat of the Policy Board

Mr. K. Tamura, Senior Economist, Monetary Affairs Department

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

I. Summary of Staff Reports on Economic and Financial Developments[4]

A. Money Market Operations in the Intermeeting Period

The Bank, in accordance with the short-term policy interest rate of minus 0.1 percent and the target level of the long-term interest rate, both decided at the previous meeting on July 19 and 20, 2017, had been providing funds through purchases of Japanese government bonds (JGBs) and other measures.[5] In this situation, 10-year JGB yields had been at around 0 percent, and the shape of the JGB yield curve had been consistent with the guideline for market operations.

B. Recent Developments in Financial Markets

In the money market, interest rates on both overnight and term instruments had generally been in negative territory. The uncollateralized overnight call rate had been in the range of around minus 0.03 to minus 0.06 percent. As for interest rates on term instruments, yields on three-month treasury discount bills (T-Bills) had been in the range of minus 0.10 to minus 0.15 percent recently.

The Nikkei 225 Stock Average had fallen somewhat through early September 2017 in a situation where the yen had been appreciating against the U.S. dollar, but rebounded thereafter and was moving in the range of 20,000-20,500 yen recently. In the foreign exchange market, the yen had appreciated temporarily against the U.S. dollar, mainly reflecting a heightening of geopolitical risks, but depreciated thereafter, while investors' risk aversion had moderated. Meanwhile, it had been depreciating against the euro, mainly due to waning uncertainties surrounding political situations in Europe.

C. Overseas Economic and Financial Developments

Overseas economies continued to grow at a moderate pace on the whole.

The U.S. economy continued to recover firmly, mainly in household spending, owing to a steady improvement in the employment and income situation. Exports had been on a moderate increasing trend, while business fixed investment also continued to pick up. As for prices, both the year-on-year rate of increase in the personal consumption

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

[5] The target level of the long-term interest rate was as follows:

The Bank will purchase JGBs so that 10-year JGB yields will remain at around zero percent.

expenditure (PCE) deflator for all items and that for all items excluding food and energy had been at around 1.5 percent.

The European economy continued to recover steadily. Exports had been increasing moderately. Private consumption had been increasing, partly supported by improvements in the labor market and consumer sentiment, while business fixed investment also had been on a moderate increasing trend. With regard to prices, both the year-on-year rate of change in the Harmonized Index of Consumer Prices (HICP) for all items and that for all items excluding energy and unprocessed food had been in the range of 1.0-1.5 percent. Meanwhile, the pace of economic recovery in the United Kingdom had been slowing as the rise in prices had been weighing on private consumption.

With regard to emerging economies, the Chinese economy continued to see stable growth on the whole, partly due to the effects of authorities' measures to support economic activity. In the NIEs and the ASEAN countries, domestic demand had been resilient, as business and household sentiment had improved, with exports increasing as a trend. Economic activity in Russia and Brazil had picked up, mainly on the back of the bottoming out of commodity prices earlier. In India, the economy had been heading toward recovery, albeit with some fluctuations due to the effects of the introduction of the Goods and Services Tax (GST). As for prices in emerging economies, inflation rates had been more or less flat in many countries and regions.

With respect to overseas financial markets, U.S. and European long-term interest rates had declined through early September 2017, mainly due to concern over geopolitical risks, but started to rise thereafter. Meanwhile, stock prices had been at high levels on the whole in many countries, mainly against the backdrop of favorable corporate earnings, and capital inflows to emerging economies continued.

D. Economic and Financial Developments in Japan

1. Economic developments

Japan's economy was expanding moderately, with a virtuous cycle from income to spending operating.

Exports had been on an increasing trend on the back of a pick-up in emerging economies. Those to advanced economies continued on their increasing trend; those to emerging economies had picked up, led mainly by electronic parts and intermediate goods to Asia. Exports were projected to continue on their moderate uptrend, especially for IT-related and capital goods.

Public investment had been increasing. It was likely to increase moderately as the implementation of the second supplementary budget for fiscal 2016 progressed and thereafter remain more or less flat at a high level.

Business fixed investment had been on a moderate increasing trend with corporate profits improving. Looking at the *Financial Statements Statistics of Corporations by Industry, Quarterly* (FSSC), the ratio of current profits to sales clearly had been improving, and the figure for the April-June quarter of 2017 had recorded a historically high level, supported in part by firm domestic demand and growth in overseas economies. According to the second preliminary estimate of GDP for the April-June quarter, real business fixed investment had marked an increase of 0.5 percent on a quarter-on-quarter basis. Machinery orders and construction starts in terms of planned expenses for private and nondwelling construction -- both of which were leading indicators of business fixed investment -- continued on an increasing trend, albeit with large monthly fluctuations. Business fixed investment was likely to continue increasing moderately, mainly on the back of an improvement in corporate profits, accommodative financial conditions, and heightened growth expectations.

As for the employment and income situation, supply-demand conditions in the labor market continued to tighten steadily and employee income had increased moderately. The active job openings-to-applicants ratio had followed a steady improving trend, and the unemployment rate had been at a level below 3 percent.

Private consumption had increased its resilience against the background of steady improvement in the employment and income situation. The consumption activity index (CAI) -- calculated by combining various sales and supply-side statistics -- for the April-June quarter of 2017 had marked a relatively high increase, and that for July was more or less flat compared with that quarter. Private consumption was expected to follow a moderate increasing trend, supported mainly by an increase in employee income, as well as replacement demand for durable goods.

Housing investment had been more or less flat.

Industrial production had been on an increasing trend against the background of increases in demand at home and abroad. It was likely to continue to increase firmly for the time being on the back of the increases in demand at home and abroad.

As for prices, the producer price index (PPI) compared with three months earlier had risen slightly, reflecting developments in international commodity prices and foreign exchange rates. The year-on-year rate of change in the consumer price index (CPI) for all items less fresh food was around 0.5 percent. The rate of change for all items less fresh food and energy had been at around 0 percent. With regard to the outlook, the year-on-year rate of change in the CPI (all items less fresh food) was likely to continue on an uptrend and increase toward 2 percent, mainly on the back of an improvement in the output gap and a rise in medium- to long-term inflation expectations.

2. Financial environment

Financial conditions were highly accommodative.

Inflation expectations remained in a weakening phase. Real long-term interest rates -- calculated as long-term interest rates minus medium- to long-term inflation expectations -- had been negative.

Firms' funding costs had been hovering at extremely low levels. With regard to credit supply, financial institutions' lending attitudes -- as perceived by firms -- had been highly accommodative. Issuing conditions for CP and corporate bonds had been favorable. Firms' credit demand had been increasing, such as for funds related to mergers and acquisitions, as well as for those for business fixed investment. Against this backdrop, the year-on-year rate of increase in the amount outstanding of bank lending had been on a moderate accelerating trend and was in the range of 3.0-3.5 percent recently. The year-on-year rate of increase in the amount outstanding of CP and corporate bonds had accelerated. Firms' financial positions had been favorable.

The monetary base had been increasing at a high year-on-year growth rate of around 15 percent. The year-on-year rate of growth in the money stock had been at around 4 percent.

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

A. Economic Developments

Regarding global financial markets, members shared the recognition that, although there temporarily had been concern over geopolitical risks associated with the situation in North Korea, investors' risk aversion generally had been seen only in part, as evidenced, for example, by the fact that U.S. and European stock prices had been at high levels and capital inflows to emerging economies continued. Meanwhile, a few members expressed the view that, as risks might not be fully factored into current market prices, more attention needed to be paid than before to the possibility that market participants' sentiment would change suddenly, triggered by, for example, a heightening of geopolitical risks.

With respect to overseas economies, members agreed that, as the global recovery in trade activity continued, advanced economies continued to recover steadily and emerging economies had picked up on the whole. On this basis, they shared the recognition that overseas economies continued to grow at a moderate pace on the whole. As for the outlook, members concurred that overseas economies were likely to continue to grow moderately as advanced economies continued growing steadily and the recovery in emerging economies took hold on the back of the steady growth in advanced economies and the effects of policy measures taken by emerging economies.

With regard to developments in overseas economies by region, members concurred that the U.S. economy continued to recover firmly, mainly in household spending, as seen, for example, in the fact that the real GDP growth rate on an annualized quarter-on-quarter basis for the April-June quarter of 2017 was 3.0 percent, registering higher growth than that for the January-March quarter. As for the outlook, they shared the view that the economy was likely to continue to see firm growth driven by domestic private demand. However, some members said that, in the short run, attention should be paid to the possibility that the damage caused by the powerful hurricanes would exert downward pressure on the economy. Regarding the recent developments in the automobile market in the United States, one member pointed out that it was becoming difficult to expect an increase in new car sales, mainly reflecting the decline in used car prices brought about by excess supply, as well as the rise in auto loan interest rates. A different member, noting that the year-on-year rate of increase in prices had been rising only moderately compared to the pace of economic recovery, said that it was necessary to carefully examine this situation, including the factors behind it, because such development in prices would affect the pace of future policy rate hikes by the Federal Reserve.

Members shared the recognition that the European economy continued to recover steadily, with both domestic and external demand increasing moderately. One member added that the recovery trend in economic activity had become evident in peripheral countries such as Greece and Portugal, and that it was reassuring that concerns over the financial sector in Europe had abated somewhat. As for the outlook, members concurred that the economy would likely follow a moderate recovery trend, while factors such as uncertainty regarding negotiations on the United Kingdom's exit from the European Union (EU) were likely to weigh on economic activity.

Members shared the recognition that emerging economies had picked up on the whole. Of these economies, they shared the view that, although the pace of increase in fixed asset investment had been slowing, the Chinese economy continued to see stable growth on the whole, as evidenced, for example, by the fact that exports had been picking up as a trend and private consumption had been resilient. One member, noting that China's producer prices had been on an increasing trend, expressed the recognition that it was necessary to examine whether this suggested that the worldwide disinflationary trend was changing. In the NIEs and the ASEAN countries, members concurred that, with exports increasing as a trend, domestic demand also had been resilient, mainly reflecting improvements in business and household sentiment and the effects of economic stimulus measures. They also agreed that economic activity in commodity-exporting countries such as Russia and Brazil had picked up, mainly reflecting the bottoming out of commodity prices earlier and the effects of the monetary easing measures. As for the outlook, members agreed that emerging economies were likely to see gradual increases in their growth rates, due mainly to the effects of the economic stimulus measures and the spread of the effects of steady growth in advanced economies. They shared the view that the Chinese economy was likely to broadly follow a stable growth path as authorities conducted fiscal and monetary policy in a timely manner.

Regarding risks to developments in overseas economies, members shared the recognition that uncertainties remained high, including those over U.S. economic policy management, negotiations on the United Kingdom's exit from the EU, and geopolitical risks.

One member said that, although the schedule for the balance sheet normalization program released by the Federal Reserve had been more or less in line with market expectations, interest rate formation during the actual reduction in the Federal Reserve's asset holdings and the effects of the program on global capital flows warranted attention.

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 agreed that the economy was expanding moderately, with a virtuous cycle from income to spending operating. As for developments in the corporate sector, they shared the recognition that exports had been on an increasing trend and business fixed investment had been on a moderate increasing trend with corporate profits recording a historically high level. Regarding the household sector, members shared the view that private consumption had increased its resilience against the background of steady improvement in the employment and income situation. One member, referring to the fact that the real GDP growth rate for the April-June quarter of 2017 had marked a sixth consecutive quarterly increase for the first time in 11 years, added that this also provided evidence that Japan's economy continued to achieve well-balanced growth in both the corporate and household sectors. A different member expressed the view that the duration of the current economic expansion had likely reached that of the so-called Izanagi boom, but the pace of the current expansion was moderate and therefore economic distortions caused by an overheating of the economy would be small. As for the outlook for the economy, members concurred that Japan's economy was likely to continue its moderate expansion. On a more specific note, they shared the recognition that domestic demand was likely to follow an uptrend, with a virtuous cycle from income to spending being maintained in both the corporate and household sectors, on the back of highly accommodative financial conditions and fiscal spending through the government's large-scale stimulus measures.

Members shared the recognition that exports had been on an increasing trend on the back of a pick-up in emerging economies. A few members pointed out that, although exports for the April-June quarter of 2017 had decreased slightly on a quarter-on-quarter basis, they increased noticeably for the July-August period compared with that quarter, and therefore no change had been observed in the increasing trend in exports as a whole, driven mainly by IT-related and capital goods. As for the outlook, one member expressed the view that, given the slowdown in new car sales in the United States, it was necessary to hold a cautious view regarding future developments in exports of automobiles to that country. Members, including this member, then concurred that Japan's exports were likely to continue on their moderate uptrend for the time being, as suggested, for example, by the Purchasing Managers' Index (PMI) for Japanese manufacturers' new export orders.

As for public investment, many members pointed out that the second supplementary budget for fiscal 2016 had started full-scale implementation, as seen, for example, in a relatively large increase in the real public fixed capital formation for the April-June quarter of 2017. On this basis, members agreed that it was appropriate to revise the Bank's assessment upward to one stating that public investment "has been increasing" from the previous one stating that it "has been turning toward an increase."

Members shared the recognition that business fixed investment had been on a moderate increasing trend with corporate profits improving. One member noted that it was highly likely that real business fixed investment on a GDP basis for the April-June quarter was somewhat weaker than the actual condition for such investment, due to the change in the sample used in the FSSC. Regarding the outlook, members agreed that business fixed investment was likely to continue increasing moderately, mainly on the back of accommodative financial conditions and heightened growth expectations. Some members expressed the recognition that labor-saving investment, including software investment, was also likely to be on an increasing trend as firms faced a more acute labor shortage. Moreover, some members pointed out that the growth in business fixed investment had been relatively low despite the fact that corporate profits and internal reserves had been at record high levels. On this point, one member expressed the view that firms had increased their cash and deposit holdings so as to be prepared for shocks that were difficult to anticipate. The member continued that, recently, this partly reflected their concern over the new U.S. administration's economic policy management and geopolitical risks. One member noted that, in light of historical data, the ratio of the amount outstanding of firms' cash and deposit holdings to total assets was approaching the level that firms deemed most appropriate. This member then expressed the view that there would be a gradual rise in the number of firms that would use their cash and deposit holdings for business fixed investment as well as research and development. Meanwhile, a different member was of the view that the expanding trend in business fixed investment would likely remain moderate, considering that capacity utilization rates and growth expectations had not increased enough in the manufacturing sector.

As for the employment and income situation, members shared the recognition that supply-demand conditions in the labor market continued to tighten steadily and employee income had increased moderately. One member said that, amid the situation of steady improvement in the output gap, the degree of labor market tightness had been at around or close to the peak level during the bubble period. Some members noted that, although developments in wages of regular employees remained sluggish, wages of part-time employees -- which were sensitive to labor market conditions -- clearly had improved. With regard to the outlook, members shared the view that employee income was likely to continue to increase moderately as labor market conditions kept tightening steadily and corporate profits improved. One member expressed the view that an increase in labor force participation rates -- including those for women and the elderly -- had thus far operated as a factor that eased labor market conditions, but there was a limit to such additional supply capacity, and therefore upward pressure on wages would heighten in due course. On this point, one member noted that the employment rate had declined compared with that during the 1990s, and that, among those not in the labor force, there were a large number of people who wished to work. The member then said that, since there remained an excess supply capacity in the labor market, upward pressure on wages was likely to be limited for the time being. In response, one member pointed out that it was necessary to assess the decline in the employment rate by taking into account the effects of a structural factor -- the aging of the population.

Members shared the recognition that private consumption had increased its resilience against the background of steady improvement in the employment and income situation. A few members pointed out that, despite the bad weather conditions in summer 2017 and heightened uncertainty over the situation in North Korea, the improving trend in consumer sentiment had been maintained. One member added that the decline in employment uncertainty -- such as that related to unemployment and difficulty in finding jobs -- and the continued improvement in real income for each household had contributed to the recent improvement in consumer sentiment. Moreover, a different member said that inbound tourism consumption by foreign visitors to Japan was recovering, and high-end goods that matched consumer values had started to be sold at department stores. In the outlook, members concurred that private consumption was likely to follow a moderate increasing trend, supported by an increase in employee income and the wealth effects stemming from the rise in stock prices, as well as replacement demand for durable goods.

Members shared the recognition that housing investment had been more or less flat.

Members shared the view that industrial production had been on an increasing trend against the background of increases in demand at home and abroad. Regarding the outlook, they agreed that industrial production was likely to continue to increase firmly for the time being on the back of the increases in demand at home and abroad.

As for prices, members concurred that the year-on-year rate of change in the CPI (all items less fresh food) was around 0.5 percent, and that the rate of change for all items less fresh food and energy had been at around 0 percent, partly as price rises by firms continued to be limited. Most members shared the recognition that prices had been relatively weak despite the steady tightening of labor market conditions amid the moderate expansion of the economy. As the background to this, one member noted -- in addition to a decline in prices of and charges for mobile phones -- the intensification of competition in the retail sector that partly reflected an expansion of e-commerce business. Some members pointed out that a large number of firms had been avoiding passing a rise in labor costs on to prices by making labor-saving investment and streamlining business process -- for example, discontinuation of business late at night. On this point, some members expressed the view that firms generally maintained a cautious price-setting stance as the deflationary mindset persisted among the public.

In terms of the outlook for prices, most members shared the view that the year-on-year rate of change in the CPI was likely to continue on an uptrend and increase toward 2 percent, mainly on the back of the improvement in the output gap and the rise in medium- to long-term inflation expectations. Some members expressed the recognition that, in view of a further tightening of labor market conditions going forward, it would become more difficult for firms to absorb labor costs, and therefore moves to pass on these costs to prices would spread gradually. One member expressed the view that consumers' acceptance of a rise in prices would gradually increase with the improvement in the employment and income situation. Regarding these views, a few members pointed out that there had been a gradual but steady increase recently in cases where firms made efforts to raise their prices and other firms followed suit, mainly in labor-intensive sectors such as home delivery services and eating and drinking services, as well as real estate lessors in city centers. Many members expressed the recognition that labor-saving investment and a streamlining of firms' business process should be assessed as positive moves that would lead to improving firms' productivity and raising the growth potential of the economy as a whole. These members then said that such efforts by firms would lead to restraining prices temporarily, but in the somewhat longer term, they were expected to exert upward pressure on prices through, for example, rises in growth expectations. A few members pointed out that, in order to further raise people's growth expectations, the government's growth strategy also was important.

Members said that, according to the indicators of inflation expectations that had become available since the previous meeting, short-term inflation expectations had bottomed out on the whole, and medium- to long-term expectations had generally been flat or had declined somewhat. They then shared the recognition that inflation expectations as a whole remained in a weakening phase. Most members, however, shared the view that, as observed prices rose, due mainly to a shift in firms' stance toward raising wages and prices and the effects of the past rise in crude oil prices, people's inflation expectations were likely to increase through the adaptive expectation formation mechanism.

In response to the above discussion, one member expressed the opinion that, although the year-on-year rate of change in the CPI was likely to increase for the time being to around 1 percent, reflecting developments in crude oil prices and foreign exchange rates, such progress would be temporary, and that the possibility of the rate of change increasing toward 2 percent from 2018 onward was low at this point. As background to this opinion, the member pointed out that, at present, there remained an excess supply capacity in both capital stock and the labor market.

B. Financial Developments

Members concurred that financial conditions in Japan were highly accommodative. They shared the view that, under Quantitative and Qualitative Monetary Easing (QQE) with Yield Curve Control, firms' funding costs had been hovering at extremely low levels and financial institutions' lending attitudes also continued to be proactive. One member, referring to the fact that financial institutions' lending rates on new loans seemed to be bottoming out on the whole recently, expressed the recognition that actual developments in lending rates remained on a declining trend after adjusting for factors such as longer lending periods.

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.

With regard to conducting monetary policy, most members shared the recognition that, although it was necessary to carefully examine the fact that firms' wage- and price-setting stance remained cautious, the momentum toward achieving the 2 percent price stability target was being maintained. As background to this, many members noted the following two points: (1) firms' stance was likely to gradually shift toward raising wages and prices with the steady improvement in the output gap, and (2) medium- to long-term inflation expectations were likely to rise steadily as further price rises came to be observed widely. Some members said that due attention should be paid to the uncertainties regarding the timing of when firms' stance would shift toward raising wages and prices and the pace at which inflation expectations would rise through the adaptive expectation formation mechanism. One member then pointed out that, under these circumstances, it was important to persistently maintain the current highly accommodative financial conditions. A different member said that it was possible that it would take some time to achieve the price stability target, and therefore ensuring the sustainability of the policy was likely to become increasingly important. This member continued that it was necessary to also take into account that the longer it took to achieve the target, the higher the uncertainty in the external environment. Following this discussion, most members shared the view that it was appropriate for the Bank to persistently pursue powerful monetary easing under the current guideline for market operations, thereby supporting improvement in economic activity and prices.

With respect to yield curve control, members shared the recognition that, since the previous meeting, the JGB yield curve had been formed smoothly in a manner consistent with the guideline for market operations. Regarding the Bank's JGB purchases, they reconfirmed that, under the current policy framework, the Bank had been conducting the purchases so as to achieve the target level of the long-term interest rate specified by the guideline for market operations, and therefore the amount of such purchases varied to some extent depending on financial market conditions.

Members also discussed the issue pointed out by some market participants that yield curve control was embedded with problems as a policy framework -- for example, in the face of declining U.S. and European long-term interest rates, yield curve control tended to cause the yen's appreciation through the narrowed interest rate differentials between Japan and these economies. One member said that, in the daily conduct of market operations, the Bank did not assume a specific range of the target level of 10-year JGB yields of "around 0 percent," nor did it rule out the possibility of such yields becoming negative. One member expressed the recognition that yield curve control as a monetary policy framework aimed to encourage the formation of the yield curve that was deemed most appropriate for maintaining the momentum toward achieving the 2 percent price stability target, and that it was not meant to change the target levels of interest rates in a mechanical manner in response to developments in overseas interest rates. A few members noted that, if progress in the yen's appreciation -- caused by the narrowed interest rate differentials between Japan and other economies and a heightening of geopolitical risks, for example -- were to have a large impact on Japan's economy, and thus the momentum toward achieving the price stability target could not be maintained, the Bank would change the guideline for market operations as appropriate. These members then said that the framework of yield curve control itself was not problematic and instead enabled the Bank to make flexible adjustments.

Based on the above discussions, regarding the guideline for market operations for the intermeeting period, most members expressed the view that it was appropriate for the Bank to maintain the following guideline. First, as for the short-term policy interest rate, it would apply a negative interest rate of minus 0.1 percent to the Policy-Rate Balances in current accounts held by financial institutions at the Bank. Second, as for the long-term interest rate, the Bank would purchase JGBs so that 10-year JGB yields would remain at around 0 percent. With regard to the amount of JGBs to be purchased, it would conduct purchases at more or less the current pace -- an annual pace of increase in the amount outstanding of its JGB holdings of about 80 trillion yen -- aiming to achieve the target level of the long-term interest rate specified by the guideline.

On this point, one member argued that monetary easing effects gained from the current yield curve were not enough for 2 percent inflation to be achieved around fiscal 2019. As background to this, this member noted the following two points: (1) in a situation where it was likely that an excess supply capacity remained in capital stock and the labor market, and considering that a consumption tax hike was scheduled in October 2019, a further increase in demand was necessary in order to sufficiently raise prices, and (2) from the viewpoint of generating such an increase in demand, it was questionable whether the current yield curve in real terms was sufficiently accommodative relative to the natural yield curve.

In response to this opinion, a different member expressed the view that the level of the current yield curve in real terms was substantially below that of the natural yield curve for all maturities, and was sufficiently accommodative even compared with past monetary easing phases. Some members said that the current framework of QQE with Yield Curve Control incorporated a mechanism in which the effects of accommodative monetary policy would be further enhanced through a decline in real interest rates and a rise in the natural rate of interest, with the economy continuing to expand moderately and the inflation and potential growth rates rising. Moreover, some members, noting that due attention should be paid to the impact of powerful monetary easing on financial markets and financial institutions, expressed the recognition that it was necessary to avoid a situation in which the functioning of financial intermediation was hampered and the timing of achieving 2 percent was delayed as a result.

With regard to <u>asset purchases other than JGB purchases</u>, members shared the recognition that it was appropriate for the Bank to implement the following guideline for the intermeeting period. First, it would purchase exchange-traded funds (ETFs) and Japan real estate investment trusts (J-REITs) so that their amounts outstanding would increase at annual paces of about 6 trillion yen and about 90 billion yen, respectively. Second, as for CP and corporate bonds, it would maintain their amounts outstanding at about 2.2 trillion yen and about 3.2 trillion yen, respectively.

With respect to <u>the Bank's thinking behind its future conduct of monetary policy</u>, members shared the view that the Bank would (1) continue with QQE with Yield Curve Control, aiming to achieve the price stability target of 2 percent, as long as it was necessary for maintaining that target in a stable manner, (2) continue expanding the monetary base until the year-on-year rate of increase in the observed CPI (all items less fresh food) exceeded 2 percent and stayed above the target in a stable manner, and (3) make policy adjustments as appropriate, taking account of developments in economic activity and prices as well as financial conditions, with a view to maintaining the momentum toward achieving the price stability target.

IV. Remarks by Government Representatives

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

(1) The application of budget requests for fiscal 2018 was closed on August 31, 2017, and the government would proceed with the budget formulation toward the year-end. The total amount of the budget requests and demands for the general account submitted by ministries had turned out to be about 100.96 trillion yen, an increase of about 3.5 trillion yen from the fiscal 2017 budget.

(2) The budget for fiscal 2018 was for the final fiscal year of the focus period for reform set forth in the Plan for Economic and Fiscal Revitalization; across all expenditure items, the government would continue to firmly strengthen the Abe administration's initiatives that had been made so far toward expenditure reform. In formulating a budget, the government would closely examine requests and demands and draw up a budget that focused intensively on the administration's high-priority issues including measures to promote "Human Resources Development," based primarily on the benchmark of general expenditures presented in the Plan for Economic and Fiscal Revitalization, thereby working on achieving both economic growth and fiscal consolidation.

(3) The government expected the Bank to continue to work toward achieving the price stability target under QQE with Yield Curve Control, in light of developments in economic activity and prices, as well as financial conditions.

The representative from the Cabinet Office made the following remarks.

(1) The Japanese economy was on a moderate recovery. The second preliminary estimate of the real GDP growth rate for the April-June quarter of 2017 was 0.6 percent on a quarter-on-quarter basis and 2.5 percent on an annualized basis. It registered positive growth for the sixth consecutive quarter, representing high growth last seen in the January-March quarter of 2015. As for the outlook, the economy was expected to

recover moderately, supported partly by the effects of the government's policies, while the employment and income situation continued to improve. However, attention should be given to the uncertainty in overseas economies and the effects of volatility in financial markets. In assessing price developments, it was important to comprehensively examine a wide range of price indicators, including the GDP deflator.

(2) The government considered that, together with "Supply System Innovation" -- which was placed at the core of the growth strategy -- "Human Resources Development" was the most important theme. With regard to this development, the government had set up the Council for Designing 100-Year Life Society and held the first meeting on September 11. The government would proceed with discussions mainly on matters such as the securing of opportunities for people to receive education, promotion of recurrent education, reform of universities and other higher education institutions, diversification of personnel hiring practices by firms, diversification of employment of the elderly, and reforms of social security toward the creation of such security for people across all generations. The government was proceeding with discussions, with a sense of urgency, to compile an interim report by the end of this year, followed by a basic concept document scheduled for release in the first half of next year.

(3) The government expected the Bank to steadily work toward achieving the price stability target of 2 percent, in light of developments in economic activity and prices, as well as financial conditions.

V. Votes

A. Vote on the Guideline for Market Operations

Based on the above discussions, to reflect the majority view of the members, the chairman formulated the following proposal and put it to a vote.

The Policy Board decided the proposal by a majority vote.

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

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

1. The Bank will apply a negative interest rate of minus 0.1 percent to the

Policy-Rate Balances in current accounts held by financial institutions at the Bank.

2. The Bank will purchase JGBs so that 10-year JGB yields will remain at around zero percent. With regard to the amount of JGBs to be purchased, the Bank will conduct purchases at more or less the current pace -- an annual pace of increase in the amount outstanding of its JGB holdings of about 80 trillion yen -- aiming to achieve the target level of the long-term interest rate specified by the guideline.

Votes for the proposal: Mr. H. Kuroda, Mr. K. Iwata, Mr. H. Nakaso, Mr. Y. Harada, Mr. Y. Funo, Mr. M. Sakurai, Ms. T. Masai, and Mr. H. Suzuki.
Votes against the proposal: Mr. G. Kataoka.

Mr. G. Kataoka dissented, considering that, since there remained an excess supply capacity in capital stock and the labor market, monetary easing effects gained from the current yield curve were not enough for 2 percent inflation to be achieved around fiscal 2019.

B. Vote on the Guideline for Asset Purchases

To reflect the view of the members, the chairman formulated the following proposal to implement the guideline for asset purchases for the intermeeting period and put it to a vote: (1) to purchase ETFs and J-REITs so that their amounts outstanding would increase at annual paces of about 6 trillion yen and about 90 billion yen, respectively, and (2) to maintain the amounts outstanding of CP and corporate bonds at about 2.2 trillion yen and about 3.2 trillion yen, respectively.

The Policy Board decided the proposal by a unanimous vote.

Votes for the proposal: Mr. H. Kuroda, Mr. K. Iwata, Mr. H. Nakaso, Mr. Y. Harada, Mr. Y. Funo, Mr. M. Sakurai, Ms. T. Masai, Mr. H. Suzuki, and Mr. G. Kataoka.
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. Mr. G. Kataoka expressed the opinion on the outlook for the CPI that, although the year-on-year rate of change in the CPI was likely to increase for the time being, reflecting developments in crude oil prices and foreign exchange rates, the possibility of the rate of change increasing toward 2 percent from 2018 onward was low at this point.

Based on this discussion, 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 July 19 and 20, 2017 for release on September 26.

Attachment

September 21, 2017

Bank of Japan

Statement on Monetary Policy

1. At the Monetary Policy Meeting held today, the Policy Board of the Bank of Japan decided upon the following.

   (1) Yield curve control

   The Bank decided, by an 8-1 majority vote, to set the following guideline for market operations for the intermeeting period. [Note 1]

   The short-term policy interest rate:

   The Bank will apply a negative interest rate of minus 0.1 percent to the Policy-Rate Balances in current accounts held by financial institutions at the Bank.

   The long-term interest rate:

   The Bank will purchase Japanese government bonds (JGBs) so that 10-year JGB yields will remain at around zero percent. With regard to the amount of JGBs to be purchased, the Bank will conduct purchases at more or less the current pace -- an annual pace of increase in the amount outstanding of its JGB holdings of about 80 trillion yen -- aiming to achieve the target level of the long-term interest rate specified by the guideline.

   (2) Guidelines for asset purchases

   With regard to asset purchases other than JGB purchases, the Bank decided, by a unanimous vote, to set the following guidelines.

   a) The Bank will purchase exchange-traded funds (ETFs) and Japan real estate investment trusts (J-REITs) so that their amounts outstanding will increase at annual paces of about 6 trillion yen and about 90 billion yen, respectively.

   b) 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.

2. Japan's economy is expanding moderately, with a virtuous cycle from income to spending operating. Overseas economies have continued to grow at a moderate pace on the whole. In

this situation, exports have been on an increasing trend. On the domestic demand side, business fixed investment has been on a moderate increasing trend with corporate profits improving. Private consumption has increased its resilience against the background of steady improvement in the employment and income situation. Meanwhile, public investment has been increasing and housing investment has been more or less flat. Reflecting these increases in demand both at home and abroad, industrial production has been on an increasing trend, and labor market conditions have continued to tighten steadily. Financial conditions are highly accommodative. On the price front, the year-on-year rate of change in the consumer price index (CPI, all items less fresh food) is around 0.5 percent. Inflation expectations have remained in a weakening phase.

3. With regard to the outlook, Japan's economy is likely to continue its moderate expansion. Domestic demand is likely to follow an uptrend, with a virtuous cycle from income to spending being maintained in both the corporate and household sectors, on the back of highly accommodative financial conditions and fiscal spending through the government's large-scale stimulus measures. Exports are expected to continue their moderate increasing trend on the back of the improvement in overseas economies. The year-on-year rate of change in the CPI is likely to continue on an uptrend and increase toward 2 percent, mainly on the back of an improvement in the output gap and a rise in medium- to long-term inflation expectations. [Note 2]

4. Risks to the outlook include the following: the U.S. economic policies and their impact on global financial markets; developments in emerging and commodity-exporting economies; negotiations on the United Kingdom's exit from the European Union (EU) and their effects; prospects regarding the European debt problem, including the financial sector; and geopolitical risks.

5. The Bank will continue with "Quantitative and Qualitative Monetary Easing (QQE) with Yield Curve Control," 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 continue expanding the monetary base until the year-on-year rate of increase in the observed CPI (all items less fresh food) exceeds 2 percent and stays above the target in a stable manner. The Bank will make policy adjustments as appropriate, taking account of developments in economic activity and prices as well as financial conditions, with a view to maintaining the momentum toward achieving the price stability target.

[Note 1] Voting for the action: Mr. H. Kuroda, Mr. K. Iwata, Mr. H. Nakaso, Mr. Y. Harada, Mr. Y. Funo, Mr. M. Sakurai, Ms. T. Masai, and Mr. H. Suzuki. Voting against the action: Mr. G. Kataoka. Mr. G. Kataoka dissented, considering that, since there remained an excess supply capacity in capital stock and the labor market, monetary easing effects gained from the current yield curve were not enough for 2 percent inflation to be achieved around fiscal 2019.

[Note 2] Mr. G. Kataoka opposed the description on the outlook for the CPI, considering that, although the year-on-year rate of change in the CPI was likely to increase for the time being reflecting developments in crude oil prices and foreign exchange rates, the possibility of the rate of change increasing toward 2 percent from 2018 onward was low at this point.