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June 20, 2018

Bank of Japan

Minutes of the Monetary Policy Meeting

on April 26 and 27, 2018

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

A Monetary Policy Meeting of the Bank of Japan Policy Board was held in the Head Office of the Bank of Japan in Tokyo on Thursday, April 26, 2018, from 2:00 p.m. to 3:21 p.m., and on Friday, April 27, from 9:00 a.m. to 11:56 a.m.[1]

Policy Board Members Present

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

Mr. M. Amamiya, Deputy Governor of the Bank of Japan

Mr. M. Wakatabe, 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. S. Kuwabara, Executive Director

Mr. E. Maeda, Executive Director

Mr. S. Uchida, 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 June 14 and 15, 2018 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 April 27.

[3] Messrs. T. Kabe and M. Maekawa were present on April 26.

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. Nagahata, Senior Economist, Monetary Affairs Department

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

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

A. 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 March 8 and 9, 2018, 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 0.04 to minus 0.07 percent. As for interest rates on term instruments, yields on three-month treasury discount bills (T-Bills) had been more or less unchanged on average and recently had been in the range of minus 0.15 to minus 0.20 percent.

The Nikkei 225 Stock Average had fallen through late March, mainly against the background of weak U.S. stock prices, but followed a rising trend thereafter, partly due to the yen's depreciation, and was moving in the range of 22,000-22,500 yen recently. In the foreign exchange market, the yen had appreciated temporarily against the U.S. dollar, mainly over concern regarding U.S.-China trade policy, but had been depreciating since late March with such concern diminishing somewhat. Meanwhile, it had also been depreciating somewhat against the euro.

C. Overseas Economic and Financial Developments

Overseas economies continued to grow firmly on the whole.

The U.S. economy had been expanding. Exports had been on an increasing trend. Private consumption had been on an uptrend, supported in part by a favorable employment and income situation, while business fixed investment also had been increasing firmly, mainly on the back of improvement in business sentiment. As for prices, both the

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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.

year-on-year rate of increase in the personal consumption 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 firmly. Exports had been on an increasing trend. Private consumption also had been on an increasing trend, partly supported by improvements in the employment and income situation and consumer sentiment, while business fixed investment had been on such a trend as well. 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. As for prices, the year-on-year rate of change in the consumer price index (CPI) had been at around 2 percent. In the NIEs and the ASEAN countries, domestic demand had been resilient, as business and household sentiment had improved, with exports being on an increasing trend. Economic activity in Russia and Brazil had been recovering moderately, mainly on the back of stable inflation rates. In India, the economy had been recovering moderately, particularly in domestic demand.

With respect to overseas financial markets, investors' risk-taking stance temporarily had become cautious, mainly due to concern regarding the U.S.-China trade policy, as seen, for instance, in a decline in stock prices through mid-March in these two countries in particular. However, stock prices had rebounded thereafter, mainly in advanced economies, on the back of the abatement of investors' pessimistic views and of favorable corporate earnings. In the commodity market, crude oil prices had risen, reflecting heightened geopolitical risks in the Middle East. U.S. long-term interest rates had risen somewhat since mid-April, mainly due to an increase in inflation expectations that was led by the rise in crude oil prices.

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 the firm growth in overseas economies. Those to advanced economies continued on their increasing trend when fluctuations were smoothed out; those to emerging economies had picked up for a wide range of items including capital goods and intermediate goods to Asia. Exports would likely continue their moderate increasing trend for the time being, mainly for capital goods and IT-related goods, and thereafter were expected to continue to do so with the growth in overseas economies continuing.

Public investment had been more or less flat, remaining at a relatively high level. It was likely to decline as the positive effects resulting from the government's large-scale stimulus measures formulated in fiscal 2016 diminished, but was projected to remain at a relatively high level, mainly underpinned by Olympic Games-related construction.

Business fixed investment continued on an increasing trend with corporate profits and business sentiment maintaining their improving trend. 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 monthly fluctuations. Business fixed investment was likely to continue increasing for the time being, mainly on the back of an improvement in corporate profits, accommodative financial conditions, and heightened growth expectations. Thereafter, its pace of increase was likely to decelerate gradually as pressure to adjust accumulated capital stock heightened.

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 declined to around 2.5 percent.

Private consumption had been increasing moderately, albeit with fluctuations, 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 -- had increased, albeit with fluctuations mainly stemming from weather conditions. Private consumption was expected to follow a moderate increasing trend for the time being, supported by an increase in employee income and the wealth effects stemming from the past rise in stock prices, as well as by replacement demand for durable goods. Thereafter, private consumption was expected to continue its moderate increasing trend, although it was likely to temporarily turn to a decline due to the scheduled consumption tax hike.

Housing investment had been weakening somewhat, as the number of housing starts in terms of housing for rent had decreased, mainly reflecting a peaking-out in demand for tax saving.

Industrial production had been on an increasing trend against the background of rises in demand at home and abroad. It would likely continue to increase firmly for the time being on the back of these rises, and thereafter continue on a moderate increasing trend with the growth in overseas economies.

As for prices, the rate of increase in the producer price index (PPI) relative to three months earlier -- adjusted for the effects of seasonal changes in electricity rates -- had been decelerating, reflecting developments in international commodity prices and foreign exchange rates. The year-on-year rate of change in the CPI for all items less fresh food was around 1 percent, while the rate of change for all items less fresh food and energy remained at around 0.5 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 had been more or less unchanged. Long-term real 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, such as for funds for business fixed investment, had been increasing. Against this backdrop, the year-on-year rate of increase in the amount outstanding of bank lending had been at around 2 percent. The year-on-year rate of increase in the amount outstanding of CP and corporate bonds had been at a relatively high level. Firms' financial positions had been favorable.

The monetary base had been increasing at a high year-on-year growth rate of around 10 percent. The year-on-year rate of growth in the money stock had been in the range of 3.0-3.5 percent.

II. Summary of Discussions by the Policy Board on Economic and Financial Developments and the April 2018 *Outlook for Economic Activity and Prices*

A. Economic Developments

Regarding global financial markets, members shared the recognition that investors' risk-taking stance had temporarily become cautious, mainly against the background of concern regarding the U.S.-China trade policy, but that the markets had started to regain stability since late March as such concern diminished somewhat. In terms of the outlook, they agreed that uncertainties surrounding U.S. economic policies had not been dispelled, and thus it was necessary to continue to pay close attention to the impact of these uncertainties on global capital flows and Japan's economic activity and prices. One member added that developments in U.S. long-term interest rates and credit spreads warranted vigilance, as they could affect U.S. nonfinancial firms with low credit ratings and emerging economies, as well as give rise to changes in global financial markets, in the event of an abrupt rise or widening triggered by some factor.

With respect to overseas economies, members shared the recognition that they continued to grow firmly on the whole. They agreed that, amid vigorous trade activities continuing globally, advanced economies continued to improve steadily and emerging economies had been recovering moderately overall. One member expressed the view that the Global Purchasing Managers' Index (PMI) for March 2018 had declined somewhat from the previous month but that this was a temporary fluctuation due to adjustments in the supply of semiconductors. As for the outlook, members concurred that overseas economies were likely to maintain their firm growth. A few members expressed the recognition that the likelihood of the firm growth in overseas economies being sustained was increasing, as suggested by the fact that international organizations and central banks recently had been revising their economic growth forecasts upward for major countries and regions. In relation to this, one member pointed out that, with regard to the U.S. economy, while an overheating often occurred immediately before a recession, the pace of the recent recovery was more moderate compared with the past and such an overheating had not been observed.

The member continued that this situation in the United States would serve to enhance the sustainability of global economic expansion. On this basis, many members expressed the recognition that due attention should be paid to protectionist U.S. trade policy and possible reactions to it from other countries, as these could have a significant impact on not only the economies of the countries concerned but also the global economy as a whole.

With regard to developments in overseas economies by region, members concurred that the U.S. economy had been expanding, as evidenced by the continued relatively high growth rate of the real GDP and by the sustained uptrend in employment. One member added that wide improvement in business sentiment continued, with the Institute for Supply Management (ISM) indices for both manufacturing and nonmanufacturing at high levels. Meanwhile, a different member, pointing out that sales of passenger cars had weakened, said that attention should be paid to the effects of interest rate rises on consumers' purchasing power. As for the outlook, members shared the view that the economy was likely to continue to expand. One member was of the view that expansionary fiscal policy would exert upward pressure on the U.S. economy going forward.

Members shared the recognition that the European economy continued to recover firmly, with both domestic and external demand on an uptrend. Some members added that, although the rapid recovery since the second half of 2017 seemed to have come to a halt, the economy had been firm, as confirmed by the PMI for manufacturing and for services remaining at high levels. A different member expressed the view that appropriate conduct of macroeconomic policy -- such as adjusting the speed of fiscal consolidation flexibly to the extent that economic recovery would not be disrupted -- had been contributing significantly to the recovery of the European economy. As for the outlook, members concurred that the European economy would likely continue its recovery.

Members shared the recognition that emerging economies had been recovering moderately overall. They agreed that the Chinese economy continued to see stable growth on the whole. One member added that exports had been on an uptrend and that private consumption had been resilient against the background of a favorable employment and income situation. As background to the stable growth, a few members pointed out that the Chinese authorities had been responding to economic fluctuations in a timely manner. Members concurred that, in the NIEs and the ASEAN countries, with exports being on an increasing trend, domestic demand also had been resilient, mainly reflecting improvements in business and household sentiment and the effects of economic stimulus measures. They shared the recognition that commodity-exporting economies such as Russia and Brazil had been recovering moderately, mainly on the back of the stable inflation rates and the effects of monetary easing measures. As for the outlook, members agreed that emerging economies were likely to continue their moderate recovery overall. They shared the view that the Chinese economy was likely to broadly follow a stable growth path as authorities conducted fiscal and monetary policies in a timely manner.

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, as perceived by both large and small firms, continued to be proactive.

Based on the above deliberations on economic and financial conditions abroad and financial conditions in Japan, 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 that business fixed investment also continued on an increasing trend with corporate profits and business sentiment maintaining their improving trend. Regarding the household sector, members shared the view that private consumption had been increasing moderately, albeit with fluctuations, against the background of steady improvement in the employment and income situation. Meanwhile, some members pointed to the possibility that, based on the March 2018 *Tankan* (Short-Term Economic Survey of Enterprises in Japan) and the reports at the April 2018 meeting of general managers of the Bank's branches, some firms had come to experience increased supply-side constraints such as shortages in labor and parts. One of these members noted that efforts on the part of firms having faced supply-side constraints -- namely, to raise productivity and make investment aimed at increasing production capacity -- would support an expansion in the economy's supply capacity, thereby raising its long-term growth potential. On this basis, the member pointed out that such recent changes surrounding firms could be regarded as dissipation of the negative hysteresis that had arisen in the past, such as firms' inefficient business processes. A different member said that, amid a gradual increase in supply-side constraints, it was becoming increasingly important to address structural reforms including labor market reform.

Members shared the recognition that exports had been on an increasing trend on the back of growth in overseas economies. One member pointed out that, in the recent *Tankan* surveys, the diffusion index (DI) for overseas supply and demand conditions for products for large manufacturing enterprises (the proportion of firms responding that there was "excess demand" minus the proportion of those responding that there was "excess supply") had been indicating excess demand for the first time in about ten years. The member continued that the economy had been driven by sectors such as motor vehicles and general-purpose machinery, which were linked to a wide range of industries, on the back of robust growth in the global economy. As for the outlook, members concurred that exports would likely continue their increasing trend for the time being, with global production and trade activities in the manufacturing sector remaining at a favorable level, and thereafter were likely to continue their moderate increasing trend on the back of growth in overseas economies.

Members agreed that public investment had been more or less flat, remaining at a relatively high level.

Members shared the recognition that business fixed investment continued on an increasing trend with corporate profits and business sentiment maintaining their improving trend. A few members expressed the view that, in addition to investment aimed at saving labor and improving business efficiency in order to address the labor shortage, investment aimed at increasing production capacity also had been increasing, mainly on the back of growth in exports. One member pointed to the possibility that the increase in business fixed investment had been brought about not only by a decline in real interest rates but also by heightened long-term growth expectations. Regarding the outlook, members agreed that business fixed investment was likely to continue increasing, mainly on the back of an improvement in corporate profits, accommodative financial conditions, and heightened growth expectations. One member noted that, although the pace of increase in business fixed investment was likely to decelerate gradually, mainly against the background of cyclical adjustments in capital stock, firms might be revising the required level of capital stock upward amid a continuing expansion in global demand for IT-related goods. One member expressed the recognition that, considering the downtrend in the working-age population, an uptrend in labor-saving and efficiency-improving investment would likely continue.

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. Some members pointed out that labor market conditions had tightened further, as evidenced by the unemployment rate declining to around 2.5 percent. One of these members noted that firms had been working proactively to secure human resources by, for example, employing a wider scope of workers, including those who lived in areas outside of large cities, and that an increasing number of those who had given up seeking a job for many years under the prolonged deflation had also started to participate in the labor force. With regard to this spring's annual labor-management wage negotiations, some members commented that they regarded it as favorable that a base pay increase had taken place for five consecutive years and its growth rate had exceeded that of the previous year. One of these members, however, said that wage growth had not accelerated as much as expected, compared to the high level of corporate profits.

Members shared the recognition that private consumption had been increasing moderately, albeit with fluctuations, against the background of steady improvement in the employment and income situation. One member noted that the recent relatively weak developments in the CAI had been partly attributable to temporary factors such as a surge in fresh food prices brought about by irregular weather. In the outlook, members shared the view 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 past rise in stock prices, as well as by replacement demand for durable goods. One member expressed the recognition that, if corporate profits remained favorable, the employment and income situation would continue to improve and an increasing trend in private consumption would be maintained.

Members shared the recognition that housing investment had been weakening somewhat against the background of the decrease in the number of housing starts in terms of housing for rent, mainly reflecting a peaking-out in demand for tax saving.

Members shared the view that industrial production had been on an increasing trend against the background of rises 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 these rises, and that thereafter it was likely to continue on a moderate increasing trend with the growth in overseas economies.

As for prices, members concurred that the year-on-year rate of change in the CPI for all items less fresh food and energy was at around 0.5 percent, partly because price rises by firms continued to be limited, while the rate of change for all items less fresh food was around 1 percent. On this basis, they agreed that, excluding the effects of energy prices, prices as a whole continued to show relatively weak developments compared to the economic expansion and the steady tightening in the labor market. Members shared the recognition that these developments were attributable to the fact that the mindset and behavior based on the assumption that wages and prices would not increase easily had been deeply entrenched among firms and households. Meanwhile, they concurred that inflation expectations had been more or less unchanged. One member expressed the view that, in the long run, inflation expectations seemed to have been rising gradually, but as observed prices had been relatively weak, it was taking time to dispel the deflationary mindset and raise inflation expectations.

B. Outlook for Economic Activity and Prices

In formulating the April 2018 *Outlook for Economic Activity and Prices* (hereafter the Outlook Report), with regard to the baseline scenario of the outlook for Japan's economic activity, members shared the view that the economy was likely to continue its moderate expansion. They shared the recognition that, in fiscal 2018, 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, mainly against the background of highly accommodative financial conditions and the underpinnings through government spending. Members also agreed that exports were likely to continue their moderate increasing trend on the back of the firm growth in overseas economies. Based on this discussion, they shared the view that Japan's economy was likely to continue growing at a pace above its potential in fiscal 2018. Members shared the recognition that, in fiscal 2019 and fiscal 2020, Japan's economy was likely to continue on an expanding trend supported by external demand, although the growth pace was projected to decelerate, reflecting a slowdown in domestic demand. They then agreed that the projected growth rates through fiscal 2019 were somewhat higher compared with those presented in the January 2018 Outlook Report.

As for economic activity through fiscal 2018, members shared the view that business fixed investment was likely to continue increasing amid accommodative financial conditions, led mainly by investment intended for domestic capacity expansion in line with the economic expansion, Olympic Games-related investment, and labor-saving investment to address the labor shortage. They concurred that private consumption was also likely to follow a moderate increasing trend as the employment and income situation continued to improve. Members agreed that public investment would probably remain at a relatively high level, mainly reflecting the supplementary budget for fiscal 2017 and Olympic Games-related demand, although the positive effects resulting from the government's past stimulus measures were likely to diminish moderately. Regarding fiscal 2019 and fiscal 2020, they concurred that the pace of increase in private consumption was projected to be moderate, mainly because it was likely to temporarily turn to a decline due to the effects of the scheduled consumption tax hike in October 2019. Members agreed that the pace of increase in business fixed investment was likely to decelerate gradually through fiscal 2020, mainly reflecting cyclical adjustments in capital stock after the prolonged economic expansion, as well as Olympic Games-related demand peaking out; they continued that, however, the deceleration was likely to be moderate, due partly to growing demand for fixed investment stemming from the increase in exports. Meanwhile, members shared the view that, while the scheduled consumption tax hike was likely to affect the GDP growth rates through two channels -- (1) the front-loaded increase and subsequent decline in demand prior to and after the consumption tax hike and (2) the effects of a decline in real income -- their negative impact on the growth rates, although subject to considerable uncertainties, was likely to be smaller than that on the rate for fiscal 2014, when the last consumption tax hike took place.

In relation to <u>the effects of economic activity on prices</u>, members discussed the point that prices continued to show relatively weak developments compared to the economic expansion and the steady tightening of labor market conditions. They shared the recognition that firms' wage- and price-setting stance had been affected by the mindset and behavior, based on the assumption that wages and prices would not increase easily, having been deeply entrenched among firms and households. With regard to firms' wage-setting stance, one member noted that, given, for example, the firms' experience of severe funding conditions during the global financial crisis, it seemed that employees -- acknowledging firms' prioritization of accumulating funds in order to be prepared for risks -- continued to take the stance of accepting firms' cautious approach toward wage increases. One member pointed out that, among globally operating Japanese firms, those for which productivity in overseas business operations was higher than that in domestic business operations tended to be more cautious about raising wages in Japan. Regarding firms' price-setting stance, some members noted that many firms continued to avoid passing a rise in labor costs on to prices by raising productivity through labor-saving investment and streamlining of their business processes. One member then said that, although such efforts to raise productivity might reduce upward pressure on prices in the short run, this situation was unlikely to last in the long run since these efforts might raise the long-term growth potential of Japan's economy and increase demand through expectations for rises in permanent income and corporate profits.

Meanwhile, some members commented on the point that prices continued to show relatively weak developments compared to the economic expansion and other factors. They pointed to the possibility that, compared with other countries, the Phillips curve for Japan was at a lower level and sloped very moderately. Some members then expressed the view that, in order to achieve the 2 percent price stability target, it was necessary to raise people's inflation expectations and shift the Phillips curve upward. One member said that, given that a steady, although weak, relationship was observed between the output gap and prices, it was necessary to maintain the positive output gap through a decline in real interest rates. One member expressed the view that, if the unemployment rate declined further, prices eventually would start to rise in line with the Phillips curve, and therefore it was important to continue to firmly pursue powerful monetary easing until then.

Members then discussed the fact that there had been some positive changes in the environment surrounding prices. Many members expressed the view that the upward pressure on prices stemming from the rise in firms' costs had continued to increase, partly due to a continued clear uptrend in hourly scheduled cash earnings of part-time employees and a rise in input prices. One member noted that a base pay increase was likely to take place for the fifth consecutive year in the annual spring labor-management wage negotiations in 2018, with the rate of increase exceeding that of last year, and a rise in prices of raw materials also had been observed. This member continued that moves to pass on the increased costs to prices had been spreading gradually, as evidenced by the DI for output prices (the proportion of firms responding that output prices had risen minus the proportion of those responding that they had fallen) for small enterprises in the March 2018 *Tankan* having turned positive for the first time in 27 years. A few members expressed the view that these moves to raise observed prices had played a role in the indicators of inflation expectations showing a bottoming out or even a rise for some indicators recently.

Members exchanged views regarding the outlook for prices. Most members shared the view that, although the year-on-year rate of increase in the CPI had continued to show relatively weak developments, excluding the effects of a rise in energy prices, the rate of change was likely to continue on an uptrend within positive territory 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. These members agreed that, comparing the current projections with those presented in the January 2018 Outlook Report, the projected rates of increase in the CPI through fiscal 2019 were more or less unchanged.

Members then discussed in detail the mechanism through which the year-on-year rate of change in the CPI would increase toward 2 percent. First, most members agreed that the output gap had widened steadily within positive territory on the back of the steady tightening of labor market conditions and a rise in capital utilization rates. These members shared the recognition that, going forward, as the economy continued its moderate expansion, the output gap was likely to widen further within positive territory in fiscal 2018 and remain substantially positive in fiscal 2019 and fiscal 2020. Next, most members shared the recognition that medium- to long-term inflation expectations were likely to follow an increasing trend and gradually converge to around 2 percent. As background to this, these members pointed to the following: (1) in terms of the adaptive component, with the improvement in the output gap, firms' stance was likely to gradually shift toward raising wages and prices and the observed inflation rate was likely to rise steadily, and (2) in terms of the forward-looking component, the Bank would pursue monetary easing through its strong commitment to achieving the price stability target.

In response to these discussions, one member expressed the view that, although the current tightening of labor market conditions to some extent had led to firms' positive stance in making new fixed investments and raising wages, this was not strong enough to push up observed prices through a shift in their stance toward raising prices. This member continued that the functioning of the process -- in which a rise in the trend inflation rate, brought about through the adaptive expectation formation mechanism, further raised the observed inflation rates -- was weak as well.

Members also discussed upside and downside risk factors to the baseline scenario of the outlook for economic activity and prices. Regarding the outlook for economic activity, they noted the following four upside and downside risk factors: (1) developments in overseas economies; (2) the effects of the scheduled consumption tax hike; (3) firms' and households' medium- to long-term growth expectations; and (4) fiscal sustainability in the medium to long term. With regard to the developments in overseas economies, some members expressed the view that it was necessary to continue paying attention to the risk that U.S. economic policies and geopolitical events would affect the global economy mainly through adjustments in stock prices and fluctuations in long-term interest rates. In relation to this point, some members noted that it was necessary to closely monitor developments in the recent protectionist U.S. trade policy and their effects in particular. In addition, members shared the recognition that the effects of the scheduled consumption tax hike were subject to considerable uncertainties, as it was likely that the effects of the front-loaded increase and subsequent decline in demand prior to and after the consumption tax hike, and of the decline in real income, would depend on consumer sentiment, the employment and income situation, and developments in prices at each respective point in time. On this basis, they concurred that, with regard to the outlook for economic activity, upside and downside risks were generally balanced in fiscal 2018, but risks were skewed to the downside for fiscal 2019 onward.

As for upside and downside risks to prices, members pointed to the following three factors: (1) developments in firms' and households' medium- to long-term inflation expectations; (2) the fact that there were items for which prices were not particularly responsive to the output gap; and (3) developments in foreign exchange rates and international commodity prices going forward. With regard to the first factor, they agreed that there was a risk that a rise in inflation expectations would lag behind if it took time for firms' stance to shift toward raising wages and prices and inflation consequently remained relatively sluggish. In addition, members shared the view that, with regard to goods and services that were difficult to differentiate, their prices might also constrain the acceleration of inflation if competition among firms intensified further, due mainly to changes in the distribution system and deregulation. On this basis, they shared the recognition that, regarding the outlook for prices, risks were skewed to the downside, especially those concerning developments in medium- to long-term inflation expectations.

Following the above discussions, members discussed the description on the outlook for prices in the Outlook Report. Many members pointed out that, although the timing of reaching around 2 percent inflation, which had been presented up through the January 2018 Outlook Report, was merely a projection, some market participants perceived this projection as a deadline for achieving 2 percent inflation, linking changes in said timing to policy adjustments, and this view was deeply entrenched among them. Some members expressed the recognition that attracting excessive attention merely to forecast figures would not be appropriate from the perspective of communication with the markets, as there were various uncertainties regarding the outlook for prices, including the possibility that it might take a fair amount of time before actual inflation started to affect inflation expectations. Based on this discussion, most members expressed the view that it was appropriate to cease providing a description on the projected timing of achieving the price stability target, starting with the April 2018 Outlook Report, so as to clarify that the timing of reaching around 2 percent inflation was not a specific deadline by which the target would be achieved. Meanwhile, one member, noting that clearly stating the timing of achieving the price stability target in the Outlook Report had served to reinforce the Bank's commitment to anchoring the inflation rate at 2 percent at the earliest possible time, expressed concern over the possibility that a review of the description discussed at this meeting could weaken the effects of the commitment. Based on these opinions, members concurred that it was necessary to clearly explain that, even if the description on the projected timing of reaching around 2 percent inflation were to be reviewed, the Bank's stance on conducting monetary policy -- namely, to aim at achieving the price stability target of 2 percent at the earliest possible time -- would not change at all.

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 <u>conducting monetary policy</u>, 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, these 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, which had been more or less unchanged recently, were likely to rise steadily as further price rises came to be observed widely. Taking these into account, most members shared the recognition that it was appropriate for the Bank to persistently pursue powerful monetary easing under the current guideline for market operations. Many members expressed the view that, as there was still a long way to go to achieve the price stability target of 2 percent, it was necessary to maintain the current highly accommodative financial conditions. One member said that, with the aim of achieving the price stability target, the Bank -- by continuing with the current monetary policy -- should persistently encourage a virtuous economic cycle to take hold. A different member commented that, although the momentum toward achieving the price stability target had been maintained, it might take time to raise inflation expectations through the adaptive formation mechanism. In this respect, the member expressed the opinion that it therefore was important for the Bank to continue to pursue the current powerful monetary easing with persistence.

Members discussed the Bank's basic stance on conducting monetary policy. Some members pointed out that it was important to continue to conduct a multifaceted monitoring and assessment of the positive impacts and side effects of the current monetary easing policy -- including its effects on the functioning of financial intermediation and the financial system. A few members commented that, as developments in profits of financial institutions had a cumulative impact on their financial strength, attention should be paid to the effects of the prolonged low-yield environment on financial institutions' profits and the functioning of financial intermediation. On this basis, some members, including these members, expressed the view that, given, for example, that Japanese financial institutions had sufficient capital bases, there was no significant problem with the functioning of financial intermediation at this stage. Meanwhile, a few members expressed the recognition that structural problems associated with demographic changes and technological innovation -- which would have an impact on financial institutions' business environment -- and the effects of monetary easing should be analyzed and discussed independently of each other.

One member commented that, in the course of the inflation rate increasing toward 2 percent and the economy's growth potential rising, the effects of monetary easing measures would be enhanced; therefore, it would be necessary to consider appropriate policy conduct without preconception while taking into account its effects on the supply-demand balance and the financial system. A different member expressed the opinion that, in order to continue with powerful monetary easing, the Bank needed to constantly consider enhancing its sustainability. One member pointed out that, looking at recent developments in corporate bond issuance and bank lending, monetary easing effects -- stemming from the decline in long-term real interest rates -- on economic activity and prices could be becoming smaller. This member continued that it was important to make further consideration concerning the desirable shape of the yield curve, given the cumulative impact of monetary easing on financial institutions' financial strength becoming increasingly severe. A different member expressed the view that, although some market participants were anticipating an early interest rate hike, if interest rates were to be actually raised, it was possible that bond and stock prices would fall and firms' profitability would deteriorate due to the yen's appreciation, thereby causing a substantial adverse impact on financial institutions' profits. Meanwhile, one member said that the possibility of the Bank achieving the price stability target by fiscal 2020 seemed low under the current guideline for market operations. This member commented that it therefore was necessary to encourage a further widening of the output gap within positive territory by taking additional easing measures and a rise in inflation expectations through reinforcing the inflation-overshooting commitment.

Members also discussed the Bank's strategy for communication to the public regarding the conduct of monetary policy. Some members said that, in order to continue with powerful monetary easing, the Bank needed to constantly aim to gain consensus among the public on the necessity of achieving the price stability target of 2 percent. One of these members added that it was important to gain the wider public's understanding that the Bank's monetary policy was not simply meant to raise prices, but was conducted for the purpose of "contributing to the sound development of the national economy" through price stability. One member pointed out that, in order to enhance the effectiveness of monetary policy in a situation where the Bank persistently continued with the current monetary easing, it was necessary to make efforts to give a clear explanation on the meaning of "exit" and "normalization," and gain understanding among the public that the Bank could respond flexibly depending on developments in economic activity and prices as well as financial conditions. A different member commented that, while there was criticism that the Bank was reluctant to communicate to the public regarding an exit from monetary easing, such criticism was unfounded as the Bank thus far had been taking every opportunity to explain specifically the issues surrounding an exit and the various policy tools that could be used in that event. This member then said that it was important for the Bank to continue to thoroughly explain to the public that, at this point, it was difficult to explain specifically what tools to employ at an exit, and in what order, as these could differ depending on developments in economic activity and prices as well as the interest rate environment going forward, and such explanation instead could cause confusion in the market. Another member -- noting that the key to effective conduct of the current policy was the Bank's commitment -- said that, in order to anchor inflation expectations at 2 percent, it was desirable to continue further research and discussions as to whether there were any measures to reinforce the commitment.

Meanwhile, one member said that it was important that the significance of the joint statement of the government and the Bank -- in which their respective roles in overcoming deflation and achieving sustainable economic growth were described -- be confirmed at the start of the new term of the Governor and Deputy Governors of the Bank. A different member said that, in the case where risk factors to achieving the price stability target were likely to materialize, it might be appropriate for the government and the Bank to consider taking specific actions in light of the principle of the joint statement, and to deliberate on and conduct the most suitable measures.

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.

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 expressed the opinion that, taking account of risk factors through fiscal 2020 such as the scheduled consumption tax hike in Japan and a possible economic downturn in the United States, the Bank should aim to achieve a situation in which the inflation rate would overshoot 2 percent at the earliest possible time. This member continued that, to this end, it was appropriate for the Bank to purchase JGBs so that yields on JGBs with maturities of 10 years and longer would broadly be lowered further.

With regard to asset purchases other than JGB purchases, 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. On this basis, one member said that policy effects and the possible side effects of the purchases of risky assets including ETFs should continue to be examined from every angle, while keeping in mind that such purchases were conducted as one of the components of the policy package to achieve the price stability target.

With respect to the Bank's thinking behind its future conduct of monetary policy, most 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.

In response to this, one member said that it was appropriate for the Bank to clearly state the timing of achieving the price stability target and -- with a view to reinforcing the inflation-overshooting commitment -- introduce a new commitment that it would take additional easing measures if there was a delay in the timing of achieving the target due to domestic factors.

IV. Remarks by Government Representatives

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

(1) The government and the Bank together recently had reconfirmed that they would commit to their joint statement upon the reappointment of Governor Haruhiko Kuroda. With a view to doing its utmost to conduct economic and fiscal management in order to create economic conditions that allowed for the scheduled consumption tax hike in October 2019, the government would continue to commit to the joint statement and carry out all possible measures while working closely with the Bank, and aim at overcoming deflation and realizing strong economic growth.

(2) The government expected the newly appointed members of the Policy Board, led by Governor Haruhiko Kuroda, to continue exercising leadership toward achieving the price stability target of 2 percent.

(3) The budget for fiscal 2018 was approved by the Diet on March 28, 2018. The government would work to swiftly and steadily implement the budget in order to ensure a virtuous economic cycle and achieve sustainable economic growth.

(4) 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 government expected Governor Haruhiko Kuroda, who had been reappointed recently, and the two Deputy Governors of the Bank, who had newly taken office, to respond to expectations both at home and abroad by drawing on their diverse experiences and accomplishments.

(2) The Japanese economy was recovering at a moderate pace and was expected to continue to do so. 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.

(3) The commitment of the government and the Bank to the joint statement was reconfirmed recently. The government would thoroughly fulfill its role specified in the joint statement, such as promoting measures to strengthen the competitiveness and growth potential of the economy and those aimed at establishing a sustainable fiscal structure.

(4) The government would continue to do its utmost to promote "Supply System Innovation" and "Human Resources Development." With regard to fiscal soundness, it would adhere to its commitment to the target of achieving a surplus in the primary balance. With the consumption tax hike scheduled for October 1, 2019, the government would deliberate specific measures to smooth out demand fluctuations expected to occur around the time of the tax hike.

(5) The government deemed it appropriate to review the description on the timing of achieving the price stability target in the Outlook Report. It expected the Bank to fully explain its thinking to the public.

(6) The government expected the Bank to continue to steadily pursue monetary easing toward achieving the price stability target as specified in the joint statement, 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. M. Amamiya, Mr. M. Wakatabe, 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, taking account of risk factors through fiscal 2020 such as the consumption tax hike and a possible economic downturn in the United States, it was desirable to further strengthen monetary easing, and that it was appropriate for the Bank to purchase JGBs so that yields on JGBs with maturities of 10 years and longer would broadly be lowered further.

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. M. Amamiya, Mr. M. Wakatabe, Mr. Y. Harada, Mr. Y. Funo, Mr. M. Sakurai, Ms. T. Masai, Mr. H. Suzuki, and Mr. G. Kataoka.
Votes against the proposal: None.

C. Vote 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 following opinions: (1) the timing of achieving the price stability target should be clearly stated, and (2) with a view to reinforcing the inflation-overshooting commitment, if there was a delay in the timing of achieving the price stability target due to domestic factors, the Bank should take additional easing measures, and it was necessary to include that in the text.

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).

VI. Discussion regarding the Outlook Report

Members discussed the draft of "The Bank's View" in the April 2018 Outlook Report (consisting of "The Bank's View" and "The Background") and formed a majority view.

To reflect the majority view, the chairman formulated a proposal on "The Bank's View" and put it to a vote.

The Policy Board decided the text of "The Bank's View" by a majority vote. It was confirmed that "The Bank's View" would be released immediately after the meeting on April 27, 2018 and the whole report would be made public on April 28. Mr. G. Kataoka opposed the description relating to the CPI, considering that the possibility of the year-on-year rate of change increasing toward 2 percent during the projection period was low at this point, and that, with a view to maintaining the Bank's commitment to its conduct of monetary easing, the timing of reaching around 2 percent inflation should continue to be clearly stated in "The Bank's View."

Votes for the proposal: Mr. H. Kuroda, Mr. M. Amamiya, Mr. M. Wakatabe, Mr. Y. Harada, Mr. Y. Funo, Mr. M. Sakurai, Ms. T. Masai, and Mr. H. Suzuki.

Votes against the proposal: Mr. G. Kataoka.

VII. Approval of the Minutes of the Monetary Policy Meeting

The Policy Board approved unanimously the minutes of the Monetary Policy Meeting of March 8 and 9, 2018 for release on May 7.

Attachment

April 27, 2018

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. 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 consumer price index (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 2]

[Note 1] Voting for the action: Mr. H. Kuroda, Mr. M. Amamiya, Mr. M. Wakatabe, 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, taking account of risk factors through fiscal 2020 such as the consumption tax hike and a possible economic downturn in the United States, it was desirable to further strengthen monetary easing, and that it was appropriate for the Bank to purchase JGBs so that yields on JGBs with maturities of 10 years and longer would broadly be lowered further.

[Note 2] Mr. G. Kataoka dissented, considering that (1) the timing of achieving the price stability target should be clearly stated, and (2) with a view to reinforcing the inflation-overshooting commitment, if there was a delay in the timing of achieving the target due to domestic factors, the Bank should take additional easing measures and that it was necessary to include that in the text.