Not to be released until 8:50 a.m. Japan Standard Time on Friday, August 3, 2018.

August 3, 2018

Bank of Japan

Minutes of the Monetary Policy Meeting

on June 14 and 15, 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, June 14, 2018, from 2:00 p.m. to 3:32 p.m., and on Friday, June 15, from 9:00 a.m. to 11:34 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. M. Maekawa, Vice Minister for Policy Coordination, Cabinet Office

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

Mr. A. Okuno, Head of Policy Planning Division, 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 July 30 and 31, 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] Mr. M. Kihara was present on June 15.

[3] Mr. T. Kabe was present on June 14.

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. T. Nagano, Senior Economist, Monetary Affairs Department

Mr. H. Inaba, 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 April 26 and 27, 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 0.03 to minus 0.08 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 0.10 to minus 0.15 percent.

The Nikkei 225 Stock Average had fallen through end-May, mainly against the background of heightened uncertainties over political developments in southern Europe and of concern regarding U.S. trade policy, but rose thereafter, partly due to the yen's depreciation, and was moving in the range of 22,500-23,000 yen recently. In the foreign exchange market, the yen had been depreciating somewhat against the U.S. dollar, mainly reflecting a rise in U.S. interest rates. Meanwhile, it had been appreciating against the euro, due mainly to relatively weak economic indicators in Europe.

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, the year-on-year

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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.

rate of change in the personal consumption expenditure (PCE) deflator for all items had been at around 2 percent and that for all items excluding food and energy had been in the range of 1.5-2.0 percent.

The European economy continued to recover, albeit at a somewhat slower pace. Growth in exports had been decelerating somewhat, mainly reflecting past appreciation of the euro. Private consumption had been on an increasing trend, partly supported by improvements in the employment and income situation and consumer sentiment, and business fixed investment also had been on such a trend. With regard to prices, the year-on-year rate of change in the Harmonized Index of Consumer Prices (HICP) for all items had been at around 1.5 percent and that for all items excluding energy, food, alcohol, and tobacco had been at about 1 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, there had been a situation where investors' risk-taking stance had become cautious, as seen, for instance, in temporary declines in stock prices through end-May in many countries, mainly against the background of heightened uncertainties over political developments in southern Europe and of concern regarding the U.S. trade policy. However, the markets had started to regain stability thereafter, as evidenced, for example, by the fact that U.S. stock prices had started to rise, mainly on the back of abatement of uncertainties over developments in southern Europe and solid U.S. economic indicators. Meanwhile, in some emerging economies that were experiencing economic vulnerability such as the "twin deficits" and high inflation, currencies had fallen mainly against the background of the rise in U.S. interest rates. In the commodity market, crude oil prices had been at a high level amid concern in particular over geopolitical risks in the Middle East.

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, and those to emerging economies had picked up for a wide range of items. Exports were expected to continue their moderate increasing trend, mainly for capital goods and IT-related goods.

Public investment had been more or less flat, remaining at a relatively high level. It was likely to remain at such a 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. Looking at the *Financial Statements Statistics of Corporations by Industry, Quarterly*, the ratio of current profits to sales for the January-March quarter of 2018 remained at a historical high level of around 6 percent, supported by solid domestic demand and the growth in overseas economies. According to the second preliminary estimates of GDP for the January-March quarter, the growth rate of real business fixed investment had marked 0.3 percent on a quarter-on-quarter basis, representing a sixth consecutive quarterly increase. 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, 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 the pace of increase in employee income had been accelerating recently. The active job openings-to-applicants ratio had been at a high level, exceeding the peak during the bubble period, 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; real, travel balance adjusted) -- calculated by combining various sales and supply-side statistics -- had declined slightly for the January-March quarter on a quarter-on-quarter basis but thereafter rose significantly for April relative to that quarter. Private consumption was expected 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.

Housing investment had been weakening somewhat, as the number of housing starts in terms of housing for rent had been on a decreasing trend, 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 was likely to continue to increase firmly for the time being on the back of these rises.

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 in the range of 0.5-1.0 percent, and that for all items less fresh food and energy for April remained at 0.4 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 8 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

A. Economic Developments

Regarding global financial markets, members shared the recognition that the markets had temporarily become unstable through end-May, mainly against the background of concern regarding the U.S. protectionist trade policy and heightened uncertainties over political developments in Italy, but had started to regain stability since the beginning of June. Some members said that it was necessary to pay attention to the impact of the rise in U.S interest rates on global capital flows and emerging economies. These members then expressed the view that the recent significant depreciation of the currencies of Argentina and Turkey stemmed from the economic vulnerability of these countries, such as the twin deficits and high inflation. A few members said that the fundamentals of emerging economies had been firm generally, and that the impact of the rise in U.S interest rates on other countries or regions had been limited to this point. However, these members added that, since there had been considerable capital inflows to emerging economies for a protracted period, close examination was required of whether or not monetary policy normalization, such as in the United States, might destabilize global financial conditions.

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 recognition that, although economies such as the European economy had been decelerating somewhat due to temporary factors, an increase in global trade had been positively affecting income and spending in many countries, and there had been no change to the improving trend in the global economy to this point. As for the outlook, members concurred that overseas economies were likely to maintain their firm growth. Many members expressed the view that production and trade activities in the manufacturing sector were likely to be solid globally, and advanced and emerging economies were projected to grow in a well-balanced manner.

With regard to developments in overseas economies by region, members concurred that the U.S. economy had been expanding, as evidenced by the continued solid growth rate of real GDP and by the sustained uptrend in employment. A few members added that expansionary fiscal policy, such as corporate tax cuts, had been exerting upward pressure on the economy. One member pointed out that, amid a moderate increase in the growth rate of average hourly wages, the situation for wages and prices had improved, as seen, for example, in a rise in underlying inflation and signs of a rise in inflation expectations, for which growth had been sluggish. As for the outlook, members shared the view that the economy was likely to continue to expand. On this basis, one member expressed the recognition that close monitoring was required of the effects of the current administration's protectionist trade policy on its economy, particularly the outcome of renegotiation of the North American Free Trade Agreement (NAFTA) and trade friction between the United States and China.

Members shared the recognition that the European economy continued to recover, albeit at a somewhat slower pace. Regarding the slower growth in real GDP for the January-March quarter of 2018 and the recent decline in the Purchasing Managers' Index (PMI), some members expressed the view that these were largely attributable to temporary factors such as the past appreciation of the euro, the unusually severe winter weather in late February, and industrial strikes in some countries. In addition, a few members noted that the economic growth rate for the latter half of 2017, which largely exceeded the potential growth rate, seemed to have been somewhat too high. 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. A few members expressed the recognition that, under appropriate conduct of macroeconomic policy, both private consumption and business fixed investment had been resilient, and economic growth had been stable. 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 had been recovering moderately, mainly on the back of the stable inflation rates. 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 shared the recognition that factors such as U.S. economic policies, negotiations on the United Kingdom's exit from the European Union (EU), and geopolitical risks continued to be regarded as risks to developments in overseas economies. Some members expressed the recognition that uncertainties surrounding overseas economies had heightened somewhat recently. On this point, a few members said that, although the U.S. protectionist trade policy had been criticized at international conferences such as the Group of Seven (G-7) meetings, there were no pronounced signs at the moment that the situation surrounding the policy would improve. Some members pointed out that the unstable political situation in southern Europe, as well as volatile movements in some emerging markets amid the rise in U.S. interest rates, called for attention as risk factors, although their effects had been limited to this point. Meanwhile, one member expressed the view that geopolitical uncertainties surrounding developments such as in North Korea had been waning somewhat compared to a while ago.

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 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 agreed that private consumption had been increasing moderately, albeit with fluctuations, against the background of steady improvement in the employment and income situation. Some members expressed the view that the real GDP growth rate for the January-March quarter of 2018 having registered a negative figure for the first time in nine quarters was largely attributable to temporary factors such as irregular weather and production adjustments for smartphones. One of these members expressed the recognition that, given the firm increase in exports and private consumption since April, the real GDP growth rate would likely return to positive territory. As for the outlook for the economy, members concurred that it 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, mainly against the background of highly accommodative financial conditions and the underpinnings through government spending. One member noted that it was necessary to carefully monitor future developments, as some sentiment indicators relating to private consumption had been relatively weak of late and uncertainties regarding overseas economies recently had been heightening somewhat. A different member pointed out that, with the output gap improving steadily, firms had been working on expanding the production capacity of their goods and services. On this basis, this member expressed the view that, since it would take some time to undergo this process, providing sustained support for firms' proactive efforts by maintaining somewhat tight supply-demand conditions through, for example, accommodative financial conditions, was important for long-term economic growth.

Members shared the recognition that exports had been on an increasing trend on the back of the firm growth in overseas economies. As for the outlook, they concurred that exports would likely continue their moderate increasing trend for the time being on the back of the continued firm growth in the global economy. A few members expressed the recognition that IT-related exports were likely to pick up firmly, on the back of an expansion in demand for data centers and motor vehicles, although their growth had decelerated temporarily since the turn of the year due to global production adjustments for semiconductors. A different member noted the possibility of an impact on Japan's exports if import duties on cars were raised in the United States.

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

Members concurred 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 labor shortage, investment aimed at increasing production capacity had been increasing, supported by favorable developments in exports. Regarding the outlook, members agreed that business fixed investment was likely to continue increasing, mainly on the back of accommodative financial conditions and heightened growth expectations.

As for the employment and income situation, members shared the recognition that supply-demand conditions in the labor market continued to tighten steadily, and that the pace of increase in employee income had been accelerating recently. Some members pointed out that labor market conditions had tightened further, as evidenced, for example, by the fact that the active job openings-to-applicants ratio for regular employees had registered a record high while the unemployment rate took hold at a low level of around 2.5 percent. One member noted that, although the unemployment rate had declined to such a low level, prices continued to show relatively weak developments and the number of those entering the labor market had been increasing to compensate for labor shortage. This member expressed the view that, judging from this situation, Japan's structural unemployment rate might be around 2 percent. Some members pointed out that it was a positive development that wages of non-regular employees kept rising noticeably amid the continued tightening of labor market conditions. One member then said that such a development should start to spread to wages of regular employees, but the sluggishness in the pace of wage increases likely would persist, as evidenced, for instance, by the fact that the rate of base pay increase resulting from this spring's annual labor-management wage negotiations was only slightly higher than that of last year. A different member noted that, in the current situation, there was a tendency toward labor surplus, in relative terms, in industries and types of jobs with high wage levels, while labor shortage was becoming more acute in those with low wage levels. The member expressed the view that this situation might be constraining upward pressure on overall wages. With regard to the outlook, members shared the view that employee income was likely to continue to increase steadily as labor market conditions kept tightening steadily and corporate profits improved. One member said that, in order to stimulate household consumption, it was important to raise wages to a level that outpaced inflation by lifting labor productivity. The member continued that the effects of working-style reforms needed to be examined from this perspective.

Members shared the recognition that private consumption had been increasing moderately, albeit with fluctuations. A few members pointed out that the CAI had declined slightly for the January-March quarter on a quarter-on-quarter basis, mainly due to the rise in fresh food prices and severe weather, but rose firmly for April, partly on the back of the pick-up in automobile sales. 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 past rise in stock prices, as well as by replacement demand for durable goods. One member said that the rise in nominal wages -- albeit at a moderate pace -- was likely to positively influence the underlying trend in private consumption, but the outlook for private consumption could not be viewed optimistically in a situation where the consumption tax hike was scheduled to take place in fiscal 2019.

Members shared the recognition that housing investment had been weakening somewhat against the background of the decreasing trend 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.

As for prices, members concurred that the year-on-year rate of increase in the CPI for all items less fresh food had slowed somewhat recently, being in the range of 0.5-1.0 percent, and that for all items less fresh food and energy remained in the range of 0.0-0.5 percent, partly because price rises by firms had been limited. With regard to the sluggish growth in the CPI since the start of fiscal 2018, some members pointed out that this was partly attributable to short-term factors, such as the yen's appreciation through early spring and price declines in some CPI items with large fluctuations. These members also noted the possibility that the increasingly competitive environment surrounding the retail sector, mainly against the background of consumers' preference for lower prices of goods and services, had discouraged firms from revising prices at the turn of the fiscal year. Some members expressed the view that, from a somewhat long-term perspective, the continued relatively weak price developments remained mainly 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. One member said that inflation had been constrained by what could be regarded as a kind of "social mode" in Japan, which had been brought about by the experience of a prolonged period of low growth and deflation, such as the labor-management-negotiation style of placing priority on the stability of employment over wage increases, firms' cautious price-setting stance reflecting their concern about losing customers, and rate-setting policies for administered prices. Nevertheless, many members, including these members, expressed the recognition that the improvement in the output gap continued to exert upward pressure on wages and prices. Some members added that passing of the rise in labor costs on to sales prices by firms had been partly observed, mainly in the services sector, and prices mainly of dining-out and delivery services had been seeing a steady acceleration in their year-on-year rates of increase. Meanwhile, one member said that firms' efforts, such as reviewing inefficient business models that had become entrenched during past economic downturns, had led to an expansion in the economy's supply capacity. This member continued that, in the short term, such expansion had been working in the direction of easing upward pressure on prices associated with an increase in demand.

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 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. On this basis, one of these members expressed the recognition that it was likely that achieving the price stability target would still take time, given that firms' wage- and price-setting stance remained cautious despite the continuous tightening of labor market conditions. A different member said that, while upward pressure on prices stemming from the rise in firms' costs -- prices of raw materials, delivery costs, and freight transport costs, in addition to labor costs -- had been increasing across the board, firms' margin for raising productivity so as to absorb this pressure had been narrowing gradually. This member commented that, therefore, it was likely that the rise in costs eventually would be passed on to firms' sales prices.

Meanwhile, members shared the recognition that inflation expectations had been more or less unchanged. One member pointed out that some sluggishness observed in the inflation rate recently was to some extent attributable to temporary factors, and therefore the rate was projected to recover. This member added, however, that these developments continued to warrant careful attention, considering that inflation expectations in Japan tended to decline when the actual inflation rate decreased.

Based on this discussion, some members expressed the recognition that it was necessary once again to thoroughly analyze mainly the background of the recent weakness in wages and prices as well as its effects on inflation expectations. Some members said that, in formulating the *Outlook for Economic Activity and Prices* (hereafter the Outlook Report) at the next Monetary Policy Meeting in July, it was important to discuss in detail the outlook for prices and the thinking behind it, including its underlying mechanism as well as risk assessments, and to thoroughly explain these to the public.

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

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, most members noted the following two points: (1) firms' stance was likely to gradually shift toward further 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. One member expressed the recognition that, in the current situation where the actual inflation rate had been sluggish, it was difficult to gain understanding of the explanation that the momentum toward achieving 2 percent inflation was maintained, and therefore it was necessary for the Bank to devise some ways to improve communication to the public. In relation to this, a different member noted that the purpose of monetary policy was not a price increase in the short term, but rather price stability from a longer-term perspective. This member continued that, from such a perspective, it was necessary for the Bank to thoroughly explain to the public that it mainly examined the output gap and inflation expectations, both of which were the major determinants of the trend in price developments, and that, based on the examination, it judged whether or not the momentum toward 2 percent inflation was maintained, for example. One member pointed out that, in judging whether the momentum toward 2 percent inflation would be maintained going forward, it also was important to comprehensively examine firms' behavior regarding their wage and price setting, such as their efforts to raise productivity and the extent of progress in passing costs on to prices, in addition to the aggregate supply-demand balance. Meanwhile, one member expressed the view that, although some indicators implied an excess demand, the momentum toward 2 percent inflation could not be judged as having strengthened recently, since the improvement in the output gap was not clear and inflation expectations had been sluggish.

Members then discussed the Bank's basic stance on conducting monetary policy. Most members shared the recognition that, as there was still a long way to go to achieve the price stability target of 2 percent, it was appropriate for the Bank to pursue powerful monetary easing with persistence under the current guideline for market operations in order to firmly maintain the momentum toward achieving the price stability target. One member said that, with the aim of achieving the price stability target, the Bank -- by continuing with the current monetary policy stance -- should persistently encourage a virtuous economic cycle to take hold. In addition, one member noted that, although the momentum toward 2 percent inflation was maintained, it likely would take a certain amount of time to achieve the target. This member continued that, therefore, it was necessary for the Bank to persistently continue with powerful monetary easing in a sustainable manner while making a sufficient examination of both the positive effects and side effects. A different member commented that, since the recent sluggishness in prices was unlikely to be attributable solely to a mere shortage of demand, it was not necessarily appropriate to adopt a policy that would forcibly push up demand in a short period of time. On this basis, the member expressed the view that it was important to persistently maintain the current accommodative financial conditions, and to this end, the Bank should conduct monetary policy taking into full consideration its sustainability while making sure that severe distortions would not arise in economic and financial conditions. Meanwhile, one member said that, amid sluggish inflation, the importance of achieving the price stability target at the earliest possible time through additional monetary easing had been increasing, considering the outlook for Japan's financial system and overseas economies.

Based on this discussion, many members pointed out that it was important to continue to conduct a multifaceted monitoring and assessment of the positive effects and side effects that could arise from the continuation of powerful monetary easing, including those on the functioning of financial intermediation and the financial system. Some members expressed the recognition that, partly because Japanese financial institutions had sufficient capital bases, there was no problem with the functioning of financial intermediation at this stage. However, these members continued that, as developments in profits of financial institutions had a cumulative impact on their financial strength, it was necessary to continue to carefully examine the effects of the prolonged low-yield environment on such institutions' profits and the functioning of financial intermediation. On this point, one member noted that financial institutions were faced with a rise in unrealized losses on securities and risks of impairment losses at branches with low profitability. This member added that, in continuing with the current monetary policy, it was necessary to take into account the two time frames in which its positive effects and side effects appeared and consider the possible countermeasures against the side effects before they materialized. In response to this, a different member said that the view that low interest rates would impair the functioning of financial intermediation through a deterioration of financial institutions' profitability, and thereby undermine the effects of monetary easing, was subject to question mainly because the average loan-to-deposit ratio of domestic banks was 70 percent or less, while the core function of financial intermediation was taking deposits and lending funds. Meanwhile, some members -- referring to the effects of the Bank's large-scale JGB purchases on the degree of liquidity and functioning of the JGB market -- said that these effects had become evident in various aspects recently. On this point, one member pointed out that JGB yields' responsiveness mainly to U.S. yields had been decreasing recently, and the number of days when inter-dealer transactions of newly issued bonds had not been settled was increasing. A different member expressed the recognition that, at the next Monetary Policy Meeting, in addition to analyzing recent price developments, it was necessary to examine and discuss other issues, such as the effects on the JGB market stemming from continued powerful monetary easing.

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, it was important for the Bank to keep making efforts to gain understanding among the public of the necessity to achieve the price stability target. One of these members expressed the view that setting the price stability target of 2 percent showed Japan's determination to the global community that it would achieve the same nominal growth rate of around 3 to 4 percent as other advanced economies. One member commented that, considering that inflation expectations were not rising easily, it was desirable, when necessary, to make efforts to improve the Bank's communication and enhance the commitment in a broad sense toward achieving the price stability target of 2 percent, with a view to managing the expectations of private entities. A different member expressed the view that the credibility of the Bank's commitment to achieving the price stability target at the earliest possible time was undermined because the description on the timing of reaching around 2 percent inflation had been deleted from the April 2018 Outlook Report. On this basis, the member said that there needed to be an additional commitment that influenced inflation expectations, given that the inflation rate had not been rising recently and inflation expectations had been sluggish. In response to this, a few members expressed the view that the Bank's commitment to achieving the price stability target of 2 percent at the earliest possible time had not changed at all, even though the description related to the outlook for prices had been reviewed. One of these members expressed the recognition that this review had not been perceived as a weakening of the Bank's commitment, judging mainly from market developments since the previous meeting. In relation to this, a different member commented that it was important to gain understanding among the public that the government's and the Bank's respective commitments specified in their joint statement on overcoming deflation and achieving sustainable economic growth were firm. This member continued that, in this regard, it was highly significant that the commitment to the joint statement had been reconfirmed upon the reappointment of the governor.

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 this, one member expressed the view that, when controlling the long-term yields, it was important to conduct market operations more flexibly with a view to maintaining the functioning of financial markets as much as possible.

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 yields 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 create 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 -- with a view to reinforcing the inflation-overshooting commitment and achieving the price stability target of 2 percent at the earliest possible time -- it was appropriate for the Bank to add a commitment that it would take some sort of additional monetary easing measures if the Bank revised downward its assessment of medium- to long-term inflation expectations, which were a particularly important element for the momentum toward achieving the 2 percent target.

IV. Remarks by Government Representatives

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

(1) Progress was being made with discussions on the Basic Policies on Economic and Fiscal Management and Reform 2018 (hereafter the Basic Policies). It was scheduled to be decided by the Cabinet swiftly upon approval of the ruling party on June 15, 2018.

(2) The Basic Policies presented concrete and highly effective plans for achieving fiscal soundness, and the government would continue to work thoroughly toward achieving both economic revitalization and fiscal soundness.

(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 second preliminary estimate of the real GDP growth rate for the January-March quarter of 2018 was minus 0.2 percent on a quarter-on-quarter basis and minus 0.6 percent on an annualized basis. The government deemed that there was no change in its assessment that the Japanese economy was recovering at a moderate pace, given that the rate turned negative after being in positive territory for eight consecutive quarters. As for the outlook, the economy was expected to continue recovering moderately. However,

attention should be given to the uncertainties regarding 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 was scheduled to compile the Basic Policies as well as the Investments for the Future Strategy 2018 on June 15. The Basic Policies would specify that the government would work on "Human Resources Development" and "Supply System Innovation" and create a new category of residence status in order to proceed with accepting foreign personnel with specialized and technical skills, as well as aim at achieving a primary balance surplus by fiscal 2025. Based on these key policies, the government would do its utmost to conduct economic and fiscal management and ensure a virtuous economic cycle.

(3) The government expected the Bank to steadily pursue monetary easing toward achieving the price stability target, 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.

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 following opinions: (1) the possibility of the year-on-year rate of change in the CPI increasing toward 2 percent going forward was low at this point, and (2) with a view to reinforcing the inflation-overshooting commitment and achieving the price stability target of 2 percent at the earliest possible time, if the Bank revised downward its assessment of medium- to long-term inflation expectations, it should take additional monetary 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).

VII. Approval of the Minutes of the Monetary Policy Meeting

The Policy Board approved unanimously the minutes of the Monetary Policy Meeting of April 26 and 27, 2018 for release on June 20.

Attachment
June 15, 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. Japan's economy is expanding moderately, with a virtuous cycle from income to spending operating. Overseas economies have continued to grow firmly on the whole. In this situation,

exports have been on an increasing trend. On the domestic demand side, business fixed investment has continued on an increasing trend with corporate profits and business sentiment maintaining their improving trend. Private consumption has been increasing moderately, albeit with fluctuations, against the background of steady improvement in the employment and income situation. Housing investment has been weakening somewhat. Meanwhile, public investment has been more or less flat, remaining at a relatively high level. 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 in the range of 0.5-1.0 percent. Inflation expectations have been more or less unchanged.

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, mainly against the background of highly accommodative financial conditions and the underpinnings through government spending. Exports are expected to continue their moderate increasing trend on the back of the firm growth 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; 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 3]

[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 the possibility of the year-on-year rate of change in the CPI increasing toward 2 percent going forward was low at this point.

[Note 3] With a view to reinforcing the inflation-overshooting commitment and achieving the price stability target of 2 percent at the earliest possible time, Mr. G. Kataoka dissented, considering that, if the Bank revised downward its assessment of medium- to long-term inflation expectations, it should take additional easing measures, and that it was necessary to include that in the text.