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May 6, 2021

Bank of Japan

Minutes of the Monetary Policy Meeting

on March 18 and 19, 2021

(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, March 18, 2021, from 2:00 p.m. to 3:46 p.m., and on Friday, March 19, from 9:00 a.m. to 12:32 p.m.[1]

Policy Board Members Present

Mr. KURODA Haruhiko, Chairman, Governor of the Bank of Japan
Mr. AMAMIYA Masayoshi, Deputy Governor of the Bank of Japan
Mr. WAKATABE Masazumi, Deputy Governor of the Bank of Japan
Mr. SAKURAI Makoto
Ms. MASAI Takako
Mr. SUZUKI Hitoshi
Mr. KATAOKA Goushi
Mr. ADACHI Seiji
Mr. NAKAMURA Toyoaki

Government Representatives Present

Mr. NAKANISHI Kenji, State Minister of Finance, Ministry of Finance[2]
Mr. SHINKAWA Hirotsugu, Deputy Vice-Minister for Policy Planning and Coordination, Ministry of Finance[3]
Mr. AKAZAWA Ryosei, State Minister of Cabinet Office, Cabinet Office[2]
Mr. TAWA Hiroshi, Vice-Minister for Policy Coordination, Cabinet Office[3]

Reporting Staff

Mr. UCHIDA Shinichi, Executive Director
Mr. YAMADA Yasuhiro, Executive Director[4]
Ms. SHIMIZU Tokiko, Executive Director (Assistant Governor)

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[1] The minutes of this meeting were approved by the Policy Board at the Monetary Policy Meeting held on April 26 and 27, 2021, 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. Nakanishi and Akazawa were present on March 19.

[3] Messrs. Shinkawa and Tawa were present on March 18.

[4] Messrs. Yamada and Masaki were present on March 18 from 3:17 p.m. to 3:43 p.m.

Mr. KAIZUKA Masaaki, Executive Director

Mr. SHIMIZU Seiichi, Director-General, Monetary Affairs Department

Mr. IIJIMA Kota, Head of Policy Planning Division, Monetary Affairs Department

Mr. MASAKI Kazuhiro, Director-General, Financial System and Bank Examination Department[4]

Mr. OTANI Akira, Director-General, Financial Markets Department

Mr. KAMEDA Seisaku, Director-General, Research and Statistics Department

Mr. KAWAMOTO Takuji, Head of Economic Research Division, Research and Statistics Department

Mr. FUKUMOTO Tomoyuki, Director-General, International Department

Secretariat of the Monetary Policy Meeting

Mr. NAKAJIMA Takeshi, Director-General, Secretariat of the Policy Board

Mr. HONDA Hisashi, Director, Deputy Head of Planning and Coordination Division, Secretariat of the Policy Board

Mr. FUKUDA Eiji, Deputy Director-General, Monetary Affairs Department[5]

Mr. YANO Masayasu, Head of Policy Infrastructure Division, Monetary Affairs Department[5]

Mr. HIGASHI Masato, Senior Economist, Monetary Affairs Department

Mr. TSUCHIKAWA Akira, Senior Economist, Monetary Affairs Department

Mr. NAGAE Shinichiro, Senior Economist, Monetary Affairs Department[5]

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[5] Messrs. Fukuda, Yano, and Nagae were present on March 19.

I. Summary of Staff Reports on Economic and Financial Developments[6]

A. Market Operations in the Intermeeting Period

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 of which were decided at the previous meeting on January 20 and 21, 2021, the Bank had been conducting purchases of Japanese government bonds (JGBs).[7] 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.

The Bank had conducted purchases of CP and corporate bonds and the Special Funds-Supplying Operations to Facilitate Financing in Response to the Novel Coronavirus (COVID-19) to support financing, mainly of firms, under the Special Program to Support Financing in Response to the Novel Coronavirus (COVID-19). In addition, with a view to maintaining stability in financial markets, the Bank had provided ample funds flexibly, mainly through purchases of JGBs and the conduct of the U.S. dollar funds-supplying operations, and had actively purchased exchange-traded funds (ETFs) and Japan real estate investment trusts (J-REITs).

B. Recent Developments in Financial Markets

In the money market, interest rates on both overnight and term instruments generally had been in negative territory. With regard to interest rates on overnight instruments, the uncollateralized call rate had been in the range of around minus 0.01 to minus 0.02 percent; general collateral (GC) repo rates had been in the range of around minus 0.06 to minus 0.09 percent. As for interest rates on term instruments, yields on three-month treasury discount bills (T-Bills) had been more or less flat.

The Nikkei 225 Stock Average had risen, mainly on the back of heightened expectations for a global economic recovery that reflected, for example, additional economic measures in the United States and progress with the vaccine rollout. Long-term interest rates had been at around 0 percent under yield curve control. As for liquidity in the JGB market, a comparison of the February 2021 *Bond Market Survey* with the November 2020 survey

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6 Reports were made based on information available at the time of the meeting.

7 The target level of the long-term interest rate was as follows:

The Bank will purchase a necessary amount of JGBs without setting an upper limit so that 10-year JGB yields will remain at around zero percent. While doing so, the yields may move upward and downward to some extent mainly depending on developments in economic activity and prices.

showed that the diffusion index (DI) for the degree of bond market functioning (the proportion of institutions responding that bond market functioning was "high" minus the proportion of those responding that it was "low") had been more or less flat. In the foreign exchange market, the yen had been depreciating against both the U.S. dollar and the euro, mainly reflecting interest rate developments in Japan, the United States, and Europe.

C. Overseas Economic and Financial Developments

Overseas economies had picked up, although the impact of a resurgence of COVID-19 remained in part. While the number of confirmed new cases of COVID-19 had turned downward in many economies, public health measures had been eased and people's movements had become somewhat active recently in the United States and some emerging economies. On the other hand, European economies had been cautious on the whole toward the easing of public health measures, mainly due to vigilance against the spread of new variants, and thus economic activities in Europe remained under somewhat strong downward pressure, mainly in the face-to-face services industry. Also, in China, the services industry, such as travel-related services, seemed to have been pushed down as people's movements during the Lunar New Year holidays were restricted in response to the fact that new cases of COVID-19 were confirmed in the country from the end of 2020 through January 2021. Thus, the impact of the resurgence of COVID-19 on the face-to-face services industry remained, although it had begun to wane. Meanwhile, business sentiment in the manufacturing sector continued to improve clearly on a global basis, partly due to continued favorable conditions in IT-related goods and the effects of the additional economic measures in the United States decided in December 2020. In addition, the production level of this sector and the trade volume had clearly been above the pre-pandemic levels seen around spring 2020. As for the outlook, overseas economies were likely to improve, partly supported by aggressive macroeconomic policies taken mainly by advanced economies, with the impact of COVID-19 waning gradually. That said, it was highly likely that the pace of improvement would vary across economies, reflecting factors such as the differences in the pace of the vaccine rollout. In addition, there remained extremely high uncertainties over this outlook. In particular, attention was warranted on, for example, the consequences of COVID-19 and their impact on overseas economies, the effects of aggressive macroeconomic policies taken by the United

States and other economies on economic activities and prices, and developments in global financial markets that reflected such factors.

With regard to developments in overseas economies by region, the U.S. economy had picked up. Private consumption also had picked up, mainly for goods consumption, due in part to the effects of the government's measures to compensate for the decline in household income, with the number of confirmed new cases of COVID-19 decreasing. Housing investment had increased clearly, with mortgage rates staying at low levels. As for the corporate sector, business sentiment continued to improve and production had increased steadily. Under these circumstances, business fixed investment had picked up, mainly for machinery investment.

The European economy had been pushed down, mainly for the services industry, with the continuing impact of the resurgence of COVID-19. Private consumption seemed to remain under downward pressure, partly due to the expiration of the value-added tax rate reduction measure in Germany, while relatively strict public health measures were being continued on the whole, although the number of confirmed new cases of COVID-19 had decreased compared to a while ago. With regard to the corporate sector, although business sentiment in the services industry had deteriorated, that in the manufacturing industry continued to improve, and exports and production had also picked up. Under these circumstances, business fixed investment had started to pick up from a state of depression.

The Chinese economy continued to recover. Exports had increased. Private consumption had increased, mainly owing to an improvement in the employment and income situation, although the impact of COVID-19 remained in part. Fixed asset investment continued to rise in a wide range of industries on the back of recovery in demand at home and abroad and firm corporate profits. Under these circumstances, production also continued to increase.

Emerging economies other than China had picked up. The NIEs and the ASEAN countries had seen a pick-up in economic activity, mainly for exports, although domestic demand remained depressed in some economies. The economies of India, Brazil, and Russia had picked up.

With respect to overseas financial markets, in advanced economies, long-term interest rates had increased significantly and stock prices had also risen, mainly due to heightened expectations for an economic recovery that reflected, for example, the additional economic measures in the United States and progress with the vaccine rollout. In the foreign exchange market, the U.S. dollar had appreciated, reflecting the rise in U.S. interest rates, and currencies in emerging economies had generally depreciated. Crude oil prices had increased, mainly on the back of expectations for a global economic recovery and of the continuation of a coordinated reduction in output by oil-producing economies.

D. Economic and Financial Developments in Japan

1. Economic developments

Japan's economy had picked up as a trend, although it remained in a severe situation due to the impact of COVID-19 at home and abroad. Regarding the outlook, the economy was likely to continue picking up, supported by a recovery in external demand, accommodative financial conditions, and the government's economic measures. However, the pace of improvement was expected to be only moderate for the time being, particularly in face-to-face services consumption, while vigilance against COVID-19 continued.

Exports and industrial production continued to increase. Looking at real exports by goods, the growth momentum in exports of automobile-related goods had leveled off recently, mainly due to a peaking-out of pent-up demand and the effects of a shortage of semiconductors. IT-related exports had increased clearly because demand had been firm for a wide range of goods, including those related to smartphones and personal computers as well as parts for data centers and on-board equipment for motor vehicles, although fluctuations arising from the impact of the Lunar New Year holidays had been seen. Exports of capital goods had increased, partly supported by a global increase in machinery investment and by firm exports in semiconductor production equipment that reflected an expansion in digital-related demand. As for the outlook, the pace of increase in exports and production was expected to decelerate for the time being, mainly for automobile-related goods, due to the peaking-out of pent-up demand and the effects of the shortage of semiconductors. However, exports and production were likely to continue increasing, supported by a global recovery in demand for business fixed investment and steady digital-related demand.

Corporate profits and business sentiment had improved on the whole, although weakness had been seen in industries such as face-to-face services. Looking at the *Financial Statements Statistics of Corporations by Industry, Quarterly*, current profits for all industries and enterprises for the October-December quarter of 2020 (seasonally adjusted) had registered improvement for two consecutive quarters, recovering to a level slightly above that in the October-December quarter of 2019, which was before the outbreak of COVID-19. Business fixed investment had picked up, although weakness had been seen in some industries. The aggregate supply of capital goods -- a coincident indicator of machinery investment -- had picked up, mainly for digital-related goods such as personal computers and goods related to base stations and 5G networks, on the back of improvement in corporate profits. With large-scale Olympic Games-related construction having almost completed, private construction completed (nonresidential) -- a coincident indicator of construction investment -- remained on a moderate declining trend, also reflecting the effects of a decrease in construction of stores and accommodation facilities, mainly by the eating and drinking as well as accommodations industries. As for the outlook, an uptrend in business fixed investment was likely to gradually become evident, supported by improvement in corporate profits and accommodative financial conditions, although construction investment by the face-to-face services industry was expected to remain weak for the time being.

A pick-up in private consumption had paused recently due to increased downward pressure on consumption of services, such as eating and drinking as well as accommodations. As for goods consumption, automobile sales had increased from spring 2020, but this had paused of late, mainly brought about by the effects of supply-side constraints due to a shortage of semiconductors. Sales of household electrical appliances maintained their moderate uptrend on the back of an increase in stay-at-home demand. Food and daily necessities had been firm on the back of the expansion in stay-at-home consumption, albeit with some fluctuations depending on the situation with COVID-19. Services consumption had decreased somewhat significantly from December 2020 through January 2021 due to self-restraint from going outside, reflecting the reinstatement of the state of emergency, and to the impact of a suspension of the "Go To Travel" campaign. After having declined markedly in December, mainly reflecting self-restraint from having year-end parties upon the resurgence of COVID-19, dining-out for January decreased to a level below that seen in June 2020 due to business hour cuts, reflecting the reinstatement of the state of emergency. As for travel, domestic travel had declined due to the suspension of the "Go To Travel" campaign and self-restraint from going outside that reflected the reinstatement of the state of emergency, and the number of overnight guests for January 2021 decreased to a level seen around summer 2020. There was still almost no overseas travel due to continued travel restrictions. Based on anecdotal information from firms, statistics published by industry organizations, and high-frequency indicators such as the number of people going outside, developments in private consumption since February 2021 were as follows. While goods consumption was highly likely to have remained steady on the whole, face-to-face services consumption seemed to have remained generally subdued, although signs of a waning in downward pressure on such services consumption had been observed in part. Regarding the outlook, with the state of emergency also lifted in the Tokyo metropolitan area and the impact of COVID-19 waning, private consumption was likely to pick up again. That said, the pace of improvement was highly likely to be moderate, mainly for face-to-face services, as long as vigilance against COVID-19 continued.

The employment and income situation remained weak due to the impact of COVID-19. As for the employment situation, according to the *Labour Force Survey*, the year-on-year rate of change in the number of employed persons had registered a negative figure of around minus 1 percent, mainly due to a decrease in non-regular employees in the face-to-face services industry. The year-on-year rate of decline in total hours worked per employee had been decelerating from the bottom hit around spring 2020, but had accelerated again of late, mainly for the accommodations as well as eating and drinking services industries, due to the impact of the reinstatement of the state of emergency. With regard to labor market conditions, the active job openings-to-applicants ratio had been more or less flat at a level slightly above 1, mainly due to an increase in job openings that reflected a pick-up in economic activity. The labor force participation rate had increased, recovering recently to the peak level seen around the end of 2019, since those who had been out of the labor market in the April-June quarter of 2020, mainly seniors and women, had been returning to it. The unemployment rate remained more or less flat, at around 3 percent of late. Total cash earnings had declined, mainly due to decreases in special cash earnings (winter bonuses) and non-scheduled cash earnings. As for the outlook, the decline in employee income was likely to come to a halt, reflecting the pick-up in economic activity and improvement in business performance.

As for prices, the year-on-year rate of change in the consumer price index (CPI, all items less fresh food) had been negative, mainly affected by COVID-19 and the past decline in crude oil prices. With regard to the outlook, it was also likely to be negative for the time being.

2. Financial environment

Financial conditions had been accommodative on the whole but those for corporate financing remained less so, as seen in weakness in firms' financial positions.

Inflation expectations had weakened somewhat.

Firms' demand for funds that stemmed mainly from a decline in sales and a rise in precautionary demand, both of which were due to the impact of COVID-19, remained at a high level, although an increase in demand by large firms in particular had leveled off. With regard to credit supply, financial institutions' lending attitudes as perceived by firms had been accommodative. Issuing conditions for CP and corporate bonds had been favorable on the whole. Firms' funding costs had been hovering at extremely low levels. In this situation, the year-on-year rate of increase in the amount outstanding of bank lending had been at around 6 percent. That in the amount outstanding of CP and corporate bonds had been at a relatively high level but the pace had slowed compared with a while ago. The environment for external funding remained accommodative owing to the Bank's and the government's measures, as well as efforts made by financial institutions. The number of bankruptcies of firms had also been at a low level. However, although firms' financial positions had improved moderately, they remained weak, mainly reflecting the decline in sales due to the impact of COVID-19.

The year-on-year rate of increase in the monetary base had been at around 20 percent, and that in the money stock had been at around 9.5 percent.

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

A. Economic Developments

Members shared the view that sentiment in global financial markets had followed an improving trend through mid-February, mainly on the back of heightened expectations for an economic recovery. They continued, however, that the markets had been nervous thereafter, due mainly to a surge in U.S. Treasury bond yields. One member expressed the opinion that a rise in these yields seemed to reflect growing expectations for a pick-up in economic activity owing to large-scale fiscal spending and the wider vaccine rollout. A few members expressed the view that, if U.S. Treasury bond yields rose excessively going forward, attention should be paid to the risks that the U.S. economy would be pushed down through a decline in housing investment and that there would be outflows of funds from emerging economies. One member pointed out that the increase in U.S. Treasury bond yields could be limited going forward by vigorous demand for bonds from U.S. banks for which loan-to-deposit ratios and lending margins had declined, as with the case in Japan.

Members concurred that overseas economies had picked up, although the impact of the resurgence of COVID-19 remained in part. Some members expressed the view that there were differences in the situation regarding COVID-19 and the vaccine rollout across countries and regions, and thus the pick-up had been uneven. One member added that the industries experiencing large declines in business activities had been limited and fixed. One member pointed out that global production and the world trade volume had been improving to a degree that exceeded the pre-pandemic levels. As for the outlook, members shared the recognition that overseas economies were likely to improve, partly supported by aggressive macroeconomic policies taken mainly by advanced economies, with the impact of COVID-19 waning gradually. That said, they continued that it was highly likely that the pace of improvement would vary across economies, reflecting factors such as the differences in the pace of the vaccine rollout. Some members pointed out that risks to future developments included the consequences of COVID-19, the effects of aggressive U.S. macroeconomic policies, as well as the tension between the United States and China, and that these entailed high uncertainties.

With regard to overseas economies by region, members shared the recognition that the U.S. economy had picked up. Some members expressed the view that it was on a firm pick-up trend, mainly reflecting large-scale fiscal spending and the wider vaccine rollout. One member was of the opinion that nonfarm payroll employment had been regaining its pace of improvement on the back of a substantial increase in employment in the entertainment and recreation as well as accommodations industries that reflected the easing of public health measures.

Members shared the view that the European economy had been pushed down, mainly for the services industry, with the continuing impact of the resurgence of COVID-19. A few members expressed the view that the impact of COVID-19 becoming prolonged was of concern, as uncertainties over the vaccine rollout had been heightening and public health measures had been extended and tightened in some economies.

Members concurred that the Chinese economy continued to recover. A few members expressed the opinion that it was returning to a growth path at a much faster pace than other economies as COVID-19 had been contained early in China.

Members shared the view that emerging economies had picked up. However, one member pointed out that future developments entailed high uncertainties, mainly against the background of concern over the resurgence of COVID-19 and a delay in the vaccine rollout.

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

With regard to economic activity, members concurred that the economy had picked up as a trend, although it remained in a severe situation due to the impact of COVID-19 at home and abroad. Some members expressed the view that, although the economy continued to show positive growth in the second half of 2020, it was highly likely to temporarily register negative growth for the January-March quarter of 2021 due to downward pressure on the face-to-face services industry that reflected the resurgence of COVID-19 since autumn 2020. However, a few members were of the opinion that economic activities of industries other than the face-to-face services industry had been maintained to a considerable extent, unlike spring 2020, when economic activities had been constrained in a wide range of sectors.

As for the outlook for economic activity, members shared the recognition that Japan's economy, with the impact of COVID-19 waning gradually, was likely to follow an improving trend, supported by a recovery in external demand, accommodative financial conditions, and the government's economic measures. However, they continued that the pace of improvement was expected to be only moderate while vigilance against COVID-19 continued. Members agreed that, specifically, downward pressure on face-to-face services consumption was likely to remain in the short run due to the impact of the resurgence of COVID-19 since autumn 2020. They also shared the view that, thereafter, as the impact of COVID-19 subsided globally, the economy was projected to continue improving with overseas economies returning to a steady growth path. One member expressed the opinion that a bipolarization between the manufacturing industry -- which had been improving -- and the face-to-face services industry -- which remained stagnant -- was expected to continue until the spread of COVID-19 subsided to a certain extent.

Turning to current developments, members shared the recognition that exports and production continued to increase. One member was of the opinion that a declining trend in exports had been seen since before the outbreak of COVID-19, but that it might be undergoing a phase shift recently. As for the outlook, members shared the view that the pace of increase in exports and production was expected to decelerate for the time being, mainly for automobile-related goods, due to the peaking-out of pent-up demand and the effects of the shortage of semiconductors; however, exports and production were likely to continue increasing, supported by a global recovery in demand for business fixed investment and steady digital-related demand.

Members shared the recognition that business fixed investment had picked up, although weakness had been seen in some industries. A few members expressed the view that, excluding sectors being significantly affected by COVID-19, it seemed that firms' business fixed investment stance was gradually becoming active again. A different member expressed the opinion that corporate profits had improved on the whole, and the pace of the pick-up in business fixed investment had been steadier than expected. As for the outlook, members shared the view that an uptrend in business fixed investment was likely to gradually become evident, supported by improvement in corporate profits and accommodative financial conditions, although construction investment by the face-to-face services industry was expected to remain weak for the time being. One member expressed the opinion that, in the manufacturing industry, some firms seemed to be making investments for the post-COVID-19 era, which involved addressing environmental issues and other challenges. Meanwhile, one member pointed out that the recent improvement in corporate profits was attributable to cost reductions by firms and various support measures by the government, and that it varied considerably among firms; therefore, it was necessary to carefully examine the sustainability of the improvement.

With regard to private consumption, members agreed that its pick-up had paused recently due to increased downward pressure on consumption of services, such as eating and drinking as well as accommodations. Some members expressed the view that consumption related to face-to-face services remained in a severe situation due to the impact of the spread of COVID-19 and the reinstatement of the state of emergency. However, a few members expressed the opinion that the decline in private consumption had been limited compared with that observed when the state of emergency was declared in 2020. As for the outlook, members shared the view that, with the impact of COVID-19 waning, private consumption was likely to pick up again, partly supported by the government's demand stimulus measures. They then stated that, however, the pace of improvement was likely to be moderate, particularly in face-to-face services consumption, as long as vigilance against COVID-19 continued. One member expressed the opinion that downward pressure on private consumption was likely to continue to be exerted for the time being, particularly on face-to-face services consumption, as weakness in the employment and income situation continued. A different member noted that households might shift to spending the savings that they had accumulated temporarily.

Members concurred that the employment and income situation remained weak due to the impact of COVID-19. One member expressed the opinion that wages continued to show weak developments, and the annual spring labor-management wage negotiations were likely to result in a relatively weak outcome this year. As for the outlook, members shared the view that the decline in employee income was likely to come to a halt, reflecting the pick-up in economic activity and improvement in business performance. One member pointed out that corporate profits had recovered and wages were also likely to head toward improvement while lagging behind such recovery. One member was of the opinion that, as long as vigilance against COVID-19 remained, employment adjustment pressure might continue to be exerted in the face-to-face services industry, mainly on non-regular employees, and that this possibility should be monitored with caution.

As for prices, members agreed that the year-on-year rate of change in the CPI had been negative, mainly affected by COVID-19 and the past decline in crude oil prices, and that inflation expectations had weakened somewhat. However, some members expressed the view that, excluding temporary factors such as the decline in energy prices, the year-on-year rate of change in the CPI remained slightly positive, and that prices had been firm compared with the decline in economic activity. A few members expressed the opinion that price cuts that aimed at stimulating demand had not been observed widely. Meanwhile, one member noted that attention should be paid to the fact that indicators for capturing the underlying trend in the CPI had declined further.

With regard to the outlook, members shared the recognition that the year-on-year rate of change in the CPI was likely to be negative for the time being, mainly affected by COVID-19 and the past decline in crude oil prices. They continued that, thereafter, it was expected to turn positive and then increase gradually, since downward pressure on prices was projected to wane gradually along with economic improvement and the effects of such factors as the decline in crude oil prices were likely to dissipate. One member expressed the opinion that downward pressure on prices had not increased further, with the output gap narrowing within negative territory. Some members pointed out that, although such factors as mobile phone-related price cuts represented temporary price fluctuations in particular sectors, the possible effects of such factors on inflation expectations warranted vigilance. Meanwhile, one member was of the opinion that, taking into account that it would take considerable time for the output gap to turn positive, it was difficult to envisage CPI inflation approaching the 2 percent target in the near future.

As for risks to economic activity and prices, members agreed that there had been extremely high uncertainties over the consequences of COVID-19 and the magnitude of their impact. They also shared the view that it was necessary to pay close attention to whether, while the impact of COVID-19 remained, growth expectations would not decline substantially and the smooth functioning of financial intermediation would be ensured. Some members expressed the view that the start of the vaccine rollout in Japan was a positive move, but attention should continue to be paid to developments regarding COVID-19 for the time being. A few members -- noting, for example, the spread of new variants -- expressed the opinion that risks regarding the impact of COVID-19 were skewed to the downside. One member pointed out that there was still a higher risk of deflation than of inflation in Japan, as inflation expectations had weakened somewhat and wages had not risen readily. Meanwhile, one member noted that downside risks had been contained since there had been no signs of an increase in industries that showed deterioration in business conditions due to COVID-19. This member was also of the opinion that, in Europe and the United States, there had been cautious views on rises in inflation rates, and thus the Bank should carefully examine both upside and downside risks with regard to how prices would develop in Japan after the pandemic ended.

B. Financial Developments

Regarding financial conditions in Japan, members concurred that those for corporate financing remained less accommodative, as seen in weakness in firms' financial positions. However, they shared the view that the environment for external funding had been accommodative owing to the Bank's and the government's measures, as well as active efforts made by financial institutions, and that financial conditions had been accommodative on the whole. One member expressed the opinion that unemployment and bankruptcies of firms had been mitigated compared with the degree of deterioration in economic activity. One member pointed out that it was necessary to continue to carefully monitor firms' financial positions through the fiscal year-end.

III. Summary of Staff Reports and Discussions by the Policy Board on "Assessment for Further Effective and Sustainable Monetary Easing"

A. Staff Reports

The staff reported the following, based on their analysis of the developments in economic activity and prices under Quantitative and Qualitative Monetary Easing (QQE) with Yield Curve Control.

It was confirmed that the situation where the inflation rate did not rise easily continued because the complex and sticky mechanism of adaptive inflation expectations formation in Japan was deeply entrenched. Elastic labor supply and a rise in firms' labor productivity had consequently constrained inflation as well. The impact of COVID-19 had put downward pressure on prices recently.

Under these circumstances, QQE with Yield Curve Control had kept real interest rates at low levels and improved financial conditions. As a result, the output gap had expanded in positive territory and positive inflation had taken hold. In addition, due to tightened labor market conditions, labor force participation of women and seniors had increased and firms had improved their labor productivity. This showed that favorable economic developments continued under large-scale monetary easing. Against this background, positive moves toward addressing the medium- to long-term challenges facing Japan's economy had been observed.

The analysis of the policy effects of QQE with Yield Curve Control confirmed that the policy framework had been effective in pushing up economic activity and prices through a decline in interest rates. Specifically, the policy effects had been transmitted mainly through a decline in funding costs and favorable conditions in financial and capital markets. Moreover, the effects of the decline in interest rates on economic activity and prices were relatively large for short- and medium-term interest rates. An excessive decline in super-long-term interest rates could have a negative impact on economic activity by, for example, undermining people's sentiment. Meanwhile, fewer market participants expected short-term interest rate cuts to be an option for additional easing compared with the time immediately after the introduction of the negative interest rate policy.

With regard to the effects on the functioning of the JGB market, the findings indicated that, if fluctuations in interest rates stayed within a certain range, they would have positive effects on market functioning without impairing the effects of monetary easing.

As for the effects on the functioning of financial intermediation, due to prolonged low interest rates and structural factors such as the declining population, financial institutions' core profitability remained on a downtrend and was likely to continue to do so. Prolonged downward pressure on financial institutions' profits might (1) lead to a gradual pullback in financial intermediation and, on the other hand, (2) increase the vulnerability of the financial system, mainly as a result of financial institutions' search for yield behavior.

With respect to the operation of the Complementary Deposit Facility, there was a gap between the actual Policy-Rate Balances and the "hypothetical" Policy-Rate Balances, which were calculated based on the assumption that arbitrage transactions fully took place, and the gap had been widening recently. In order to address this situation, the Bank could make technical adjustments to compress the unused amounts of Macro Add-on Balances and a portion of the Policy-Rate Balances by reviewing some parts of the method to calculate the limit of the Macro Add-on Balances under the Complementary Deposit Facility.

The findings suggested that purchases of assets such as ETFs had the effect of lowering risk premia, and that the effects of purchases per single amount tended to be larger (1) the lower the level of stock prices relative to their trend, (2) the higher the volatility, (3) the larger the rate of decline in stock prices immediately before the conduct of purchases, and (4) the larger the size of purchases. On the other hand, some points to note had been raised with regard to ETF purchases. One was that the Bank's indirect shareholding ratio in some ETF component firms tended to increase much more rapidly through such purchases in the case of ETFs tracking the Nikkei 225 Stock Average or the JPX-Nikkei Index 400 (JPX-Nikkei 400) than ETFs tracking the Tokyo Stock Price Index (TOPIX).

Regarding the effectiveness of the inflation-overshooting commitment, the results of simulations using a macroeconomic model showed that a "makeup strategy" was desirable in Japan; that is, when the observed inflation rate was below the inflation target, monetary policy should be conducted by also referring to the past inflation rates for some period of time.

B. Discussions by the Policy Board

Based on the above staff reports, members discussed the "Assessment for Further Effective and Sustainable Monetary Easing."

With respect to the policy effects, members agreed that QQE with Yield Curve Control had had positive effects in line with the intended mechanism. One member expressed the opinion that, even after COVID-19 subsided, it was important that the Bank persistently continue with monetary easing and thereby maintain a positive output gap and encourage wage increases. One member pointed out that the channel via financial and capital markets had contributed considerably to pushing up the output gap. A few members expressed the view that, even with the positive effects of the current monetary easing policy, the situation where the inflation rate did not rise easily continued, mainly because it took time to change the perception of inflation that had become entrenched during the deflation period, as adaptive expectations formation was complex and sticky. One of these members noted that the fact that expectations formation was largely adaptive implied that, if people actually continued to experience inflation, their perception of it could change accordingly. One member was of the view that the results of a personally conducted analysis suggested that, as the inflation rate rose to more than 1 percent, the Phillips curve would steepen and the responsiveness to the output gap would increase.

As for the effects on the functioning of the JGB market, some members expressed the recognition that, while a balance between maintaining market functioning and controlling interest rates was important in conducting yield curve control in a sustainable manner, it was reconfirmed that fluctuations in interest rates within a certain range would not impair the effects of monetary easing. A few members expressed the opinion that, as the Bank had allowed long-term interest rates to move more flexibly in July 2018, the range had temporarily widened and the functioning of the JGB market had improved, although it narrowed again thereafter. One member pointed out that it was important to allow for fluctuations only within a range that would not undermine the recovery in the real economy.

With regard to the effects on the functioning of financial intermediation, some members were of the view that it was necessary to assess developments in the financial system minutely because side effects on the financial system accumulate over time. One member expressed the opinion that achieving the price stability target at the earliest possible time was the best prescription for containing the side effects of monetary easing. This member added that, if such side effects became a matter of concern for additional monetary easing, one option could be to show in advance possible measures to mitigate them.

Regarding purchases of assets such as ETFs, some members said that the findings suggested that large-scale purchases during times of heightened market instability were effective.

With respect to the inflation-overshooting commitment, some members expressed the view that, in order to make clear that monetary easing would be continued for a long period, the inflation-overshooting commitment, through which the Bank implemented a "makeup strategy," was extremely important. One of these members added that, since a deflationary risk was a matter of concern at present, the commitment showed the Bank's strong stance that it would not head toward an exit easily. Meanwhile, one member noted that simply adopting a "makeup strategy" did not necessarily lead to achievement of the price stability target.

Moreover, a few members were of the opinion that it was important for the Bank to disseminate information and carry out public relations activities so that the public would deepen its understanding of the necessity of the price stability target of 2 percent, which was a global standard, the mechanism toward achieving it, and the role of various measures conducted under the target.

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

Based on the above deliberations, members discussed the Bank's policy actions.

As for the basic stance on monetary policy, members agreed that it was appropriate for the Bank to continue with powerful monetary easing under the framework of QQE with Yield Curve Control, which had been effective in pushing up economic activity and prices, with a view to achieving the price stability target of 2 percent. They shared the assessment that, to this end, it was important to continue with monetary easing in a sustainable manner and make nimble and effective responses without hesitation to counter changes in developments in economic activity and prices, as well as in financial conditions. One member expressed the opinion that, under the commitment to conducting monetary easing into the future, it was important to maintain the current policy framework in a more stable manner.

In this regard, members continued to discuss policy actions to conduct further effective and sustainable monetary easing.

With respect to the conduct of yield curve control, many members expressed the view that it was appropriate to establish a scheme under which the Bank could cut short- and long-term interest rates nimbly while considering the impact on the functioning of financial intermediation. Some of these members were of the opinion that this scheme would be effective in changing the views of market participants who saw the possibility of interest rate cuts as limited. Some members expressed the opinion that the Bank specifically could apply certain interest rates as an incentive, linked to the short-term policy interest rate, to financial institutions' current account balances, corresponding to the amount outstanding of funds that had been provided through its fund-provisioning measures. One of these members said that applying different incentives in accordance with the type of the Bank's fund-provisioning measures would be a possible option. One member pointed out that a scheme under which the Bank linked the incentives with an increase in the amount outstanding of lending by financial institutions could have synergistic effects in terms of monetary easing; however, depending on the way the Bank provided incentives, the easing effects might be undermined by upward pressure on market interest rates.

Members also concurred that reviewing the method to calculate the Macro Add-on Balances under the Complementary Deposit Facility, which had been explained by the staff, would contribute to the smooth conduct of the negative interest rate policy.

Members then discussed the range of fluctuations in long-term interest rates. A few members expressed the opinion that it was appropriate to clarify the range that was consistent with the guideline for market operations in order to conduct yield curve control flexibly during normal times. On this basis, these members said that the Bank could clearly indicate in the policy statement that the range of fluctuations would be between around plus and minus 0.25 percent from the target level. One member noted that the flexibility of long-term interest rates moving within the range of around plus and minus 0.25 percent from the target level was desirable since it prevented bond market participants who had lost their profit opportunities from exiting that market and helped maintain the price stabilization function of the market. Some members expressed the view that, as for the upper limit of the range of fluctuations, it was appropriate to respond strictly to developments in those rates so as to continue to exert easing effects. One of these members expressed the opinion that the Bank could devise a way to strengthen its fixed-rate purchase operations to strictly set an upper limit on interest rates when necessary. Some members expressed the view that, as for the lower limit of the range of fluctuations, when the yields temporarily fell below the lower limit, it was not necessary for the Bank to strictly respond to such developments. Meanwhile, a few members noted that it was appropriate for the Bank to reiterate that an excessive decline in super-long-term JGB yields could have a negative impact on economic activity from a long-term perspective by, for example, undermining people's sentiment. Based on this, members concurred that, under the continuing impact of COVID-19 in particular, it was appropriate for the time being to conduct yield curve control with a priority on stabilizing the entire yield curve at a low level.

With regard to purchases of ETFs and J-REITs, most members shared the view that, based on the analysis that large-scale purchases of such assets during times of heightened market instability were effective, it was appropriate for the Bank to enhance their sustainability and nimbleness through conducting them more flexibly in a prioritized manner than before. One member expressed the opinion that, in order to do so, the Bank could make revisions to the guidelines for purchasing assets such as ETFs so that it could purchase ETFs and J-REITs as necessary while maintaining the upper limits on annual paces of increase in their amounts outstanding. A few members noted that, if the Bank conducted such purchases as necessary, this would give considerable discretion to the staff; therefore, when such a purchase was made, it would be appropriate for the staff to immediately report to the members of the Policy Board. One member pointed out that these revisions to the guidelines for purchasing assets such as ETFs would be made in order to conduct purchases more effectively, and therefore it was necessary to be careful so as to avoid a misunderstanding that the Bank had adopted a less accommodative stance on monetary policy. In addition, some members were of the opinion that, with regard to the purchases of ETFs, in order to avoid its indirect shareholding ratio from rising in particular ETF component firms, the Bank could make revisions to eligibility regarding ETFs to be purchased so that it would only purchase those tracking the TOPIX, the index with the largest number of component stocks.

Meanwhile, some members expressed the opinion that, given that monetary easing was expected to be continued for a long time, with a view to paying further attention to developments in the financial system, it would be appropriate to have the Financial System and Bank Examination Department staff regularly attend Monetary Policy Meetings and explain such developments. One member noted that the purpose of paying attention to developments in the financial system would not be for the Bank to make consideration of financial institutions' profits but to enable nimble conduct of effective monetary easing.

Based on the members' proposals, the chairman requested that the staff provide an outline of possible policy measures.

The staff provided an explanation on possible policy measures, which consisted of the following.

(1) Conduct of Yield Curve Control

(a) With a view to enabling the Bank to cut short- and long-term interest rates nimbly while considering the impact on the functioning of financial intermediation, the Bank could establish the Interest Scheme to Promote Lending. The summary would be as follows.

(i) The Bank would apply certain interest rates as an incentive to financial institutions' current account balances, corresponding to the amount outstanding of funds that had been provided through its various fund-provisioning measures to promote financial institutions' lending. The applied interest rates would be linked to the short-term policy interest rate.

(ii) Eligible fund-provisioning measures would be categorized into three groups in view of providing different incentives in accordance with these measures. Specifically, the applied interest rate for Category II would be the absolute value of the short-term policy interest rate, and a higher rate would be applied for Category I and a lower rate for Category III.

(iii) For now, the applied interest rates could be as follows. Funds provided through the Special Funds-Supplying Operations to Facilitate Financing in Response to the Novel Coronavirus (COVID-19) against loans that financial institutions made on their own would fall under Category I and an interest rate of 0.2 percent would be applied; funds provided through the same operations against loans other than those for Category I and against private debt pledged as collateral would fall under Category II and an interest rate of 0.1 percent would be applied; and funds provided through the Loan Support Program and the Funds-Supplying Operation to Support Financial Institutions in Disaster Areas would fall under Category III and an interest rate of 0 percent would be applied.

(b) In addition, the Bank could modify the method to calculate the Macro Add-on Balances under the Complementary Deposit Facility in order to narrow the gap between the actual Policy-Rate Balances and the "hypothetical" Policy-Rate Balances, which were calculated based on the assumption that arbitrage transactions had fully taken place.

(c) In order to conduct yield curve control flexibly during normal times, the Bank could make clear that the range of 10-year JGB yield fluctuations would be between around plus and minus 0.25 percent from the target level.

(d) The Bank could introduce "fixed-rate purchase operations for consecutive days" as a powerful tool to set an upper limit on interest rates, through which it would conduct the fixed-rate purchase operations consecutively for a certain period of time. When the yields temporarily fell below the lower limit, the Bank would not strictly respond to such developments.

(e) For the time being, under the continuing impact of COVID-19, the Bank could conduct yield curve control with a priority on stabilizing the entire yield curve at a low level.

(2) Purchases of ETFs and J-REITs

(a) The Bank could maintain the upper limits on annual paces of increase in the amounts outstanding of ETF and J-REIT purchases, which were originally set as a temporary measure in response to the impact of COVID-19, and conduct purchases as necessary under these limits. When a purchase was made, it should be immediately reported to the members of the Policy Board.

(b) With regard to ETF purchases, the Bank could only purchase ETFs tracking the TOPIX. As for ETFs composed of stocks issued by firms that actively invested in physical and human capital, the Bank could only purchase those that were managed so that they tracked the indices it deemed eligible in accordance with the eligibility criteria for indices.

(3) Participation of the Financial System and Bank Examination Department at the Monetary Policy Meetings

At the Monetary Policy Meetings when the *Outlook for Economic Activity and Prices* is decided (four times a year), staff of the Financial System and Bank Examination Department could attend the meeting and explain developments in the financial system to the Policy Board.

(4) Purchases of CP and corporate bonds

With a view to simplifying the guideline for CP and corporate bond purchases, the guideline could be that the Bank would purchase these assets with an upper limit on the amount outstanding of about 20 trillion yen in total until the end of September 2021. A certain amount would continue to be purchased even after the purchases in response to the impact of COVID-19 ended.

Members concurred that, for further effective and sustainable monetary easing, it was appropriate for the Bank to take policy actions as outlined by the staff. A few members expressed the view that the Bank's policy actions proposed at this meeting would strengthen the policy framework of monetary easing, in that they would enhance the sustainability of the Bank's policy conduct and enable it to make nimble and effective responses. These members expressed the opinion that the Bank's indication at this meeting that the range of fluctuations in long-term interest rates would be between around plus and minus 0.25 percent from the target level would only clarify the previous concept, which had a certain degree of latitude -- namely, about double the range of around plus and minus 0.1 percent from the target level. Some members pointed out that the Bank's consideration of the side effects was made solely to enable nimble conduct of effective monetary easing, and it was necessary to avoid a misunderstanding that the Bank had adopted a less accommodative stance on monetary policy only because it had taken measures to address the side effects. One member expressed the opinion that it was desirable that the policy framework -- which would be enhanced in terms of nimbleness and sustainability through the Bank's policy actions proposed at this meeting -- continue to be the basic guideline for its monetary easing for a few years to come.

Furthermore, members discussed <u>policy actions in response to the impact of COVID-19</u>. They agreed that the three monetary easing measures -- namely, (1) the Special Program to Support Financing in Response to the Novel Coronavirus (COVID-19), (2) an ample provision of yen and foreign currency funds without setting upper limits, and (3) purchases of assets such as ETFs -- had been exerting their intended effects. Members shared the recognition that it was important for the Bank to continue to support financing, mainly of firms, and maintain stability in financial markets through the three monetary easing measures. On this basis, they concurred that, for the time being, the Bank would closely monitor the impact of COVID-19 and not hesitate to take additional easing measures if necessary.

Members also expressed their opinions on <u>various points to take into account in relation to the conduct of monetary policy</u>. One member expressed the view that, in order to be prepared for shocks that could occur in the future as well, it was important for the Bank to make policy responses swiftly and effectively if necessary while firmly maintaining a framework that allowed for exchanging information and cooperating with the government and other major central banks, and with full consideration of securing stability in financial markets and the financial system. One member said that it was necessary to encourage corporate behavior that would lead to improvement in firms' and households' growth expectations and inflation expectations, and to support financial institutions' efforts that underpinned such corporate behavior and the strengthening of the functioning of financial activities through, for example, enhancement of the corporate bond market. In addition, this member pointed out that a wider range of areas were becoming difficult to capture using traditional statistics, mainly due to changes in corporate behavior that reflected digitalization, and it was important to deepen analysis on the effects of such changes on the economy, financial conditions, and other areas.

With respect to yield curve control, members shared the recognition that 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 the following guideline was appropriate. 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 a necessary amount of JGBs without setting an upper limit so that 10-year JGB yields would remain at around 0 percent.

On this point, one member expressed the opinion that it was desirable to further strengthen monetary easing by lowering short- and long-term interest rates, with a view to responding to an increase in downward pressure on prices and encouraging firms to make active business fixed investment for the post-COVID-19 era.

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. First, it would purchase ETFs and J-REITs as necessary with upper limits of about 12 trillion yen and about 180 billion yen, respectively, on annual paces of increase in their amounts outstanding. Second, the Bank would purchase CP and corporate bonds with an upper limit on the amount outstanding of about 20 trillion yen in total until the end of September 2021.

With respect to the Bank's stance on its future conduct of monetary policy, members shared the view that it 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, and (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.

With regard to the measures that the Bank had introduced and strengthened since March 2020 in response to the impact of COVID-19, members concurred that it would continue to support financing, mainly of firms, and maintain stability in financial markets through (1) the Special Program to Support Financing in Response to the Novel Coronavirus (COVID-19), (2) an ample provision of yen and foreign currency funds without setting upper limits mainly by purchasing JGBs and conducting the U.S. dollar funds-supplying operations, and (3) purchases of ETFs and J-REITs with upper limits of about 12 trillion yen and about 180 billion yen, respectively, on annual paces of increase in their amounts outstanding.

Regarding its policy stance for the time being, members agreed that the Bank would closely monitor the impact of COVID-19 and not hesitate to take additional easing measures if necessary. Based on this, most members shared the view that, as for policy rates, it would expect short- and long-term interest rates to remain at their present or lower levels.

On this point, one member was of the opinion that, in order to avoid Japan's economy returning to deflation, further coordination of fiscal and monetary policy was necessary and it was appropriate for the Bank to revise the forward guidance for the policy rates to relate it to the price stability target, thereby committing itself to conducting monetary policy based on concrete conditions.

V. Remarks by Government Representatives

Based on the above discussions, the government representatives requested that the chairman adjourn the meeting. The chairman approved the request. (The meeting adjourned at 11:33 a.m. and reconvened at 12:05 p.m.)

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

(1) The government considered that the findings of the assessment and the Bank's policy actions based on them were appropriate, and thus expected the Bank to implement said actions.

(2) The government would continue to work together with the Bank and make efforts to support the Japanese economy and stabilize financial markets.

The representative from the Cabinet Office made the following remarks.

(1) The second preliminary estimate of the real GDP growth rate for the October-December quarter of 2020 had registered positive growth for two consecutive quarters. Although the Japanese economy was still below the pre-pandemic level, the government considered that this was a reminder of the potential resilience of the economy.

(2) The government had decided to lift the state of emergency in four prefectures as of March 21. While paying attention to the burden on the medical treatment system that would arise when the vaccine rollout for the elderly started in April and to the future course of new variants, it would continue to do its utmost to contain the resurgence of COVID-19 and carry out targeted and effective support measures for those seriously affected economically.

(3) The government expected that the findings of the assessment at this meeting and the resultant revisions to the manner of the policy conduct while continuing with monetary easing would enhance the sustainability and nimbleness of monetary easing measures. It therefore considered that it was important for the Bank to provide a thorough explanation to the public.

(4) The government expected the Bank to continue to closely cooperate with the government in order to bring about an early recovery of the Japanese economy from the impact of COVID-19, and to conduct appropriate monetary policy while closely monitoring, for example, the impact of a rise in U.S. interest rates on financial and capital markets.

VI. Votes

A. Vote on "Assessment for Further Effective and Sustainable Monetary Easing"

Based on the above discussions, to reflect the view of the members, the chairman formulated a proposal on "The Bank's View" in the "Assessment for Further Effective and Sustainable Monetary Easing" and put it to a vote.

The Policy Board decided the proposal by a unanimous vote.

B. Vote on the Guideline for Market Operations

To reflect the majority view of the members, the chairman formulated the following proposal on the guideline for market operations 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 a necessary amount of JGBs without setting an upper limit so that 10-year JGB yields will remain at around zero percent.

Votes for the proposal: Mr. KURODA Haruhiko, Mr. AMAMIYA Masayoshi, Mr. WAKATABE Masazumi, Mr. SAKURAI Makoto, Ms. MASAI Takako, Mr. SUZUKI Hitoshi, Mr. ADACHI Seiji, and Mr. NAKAMURA Toyoaki.

Votes against the proposal: Mr. KATAOKA Goushi.

Mr. Kataoka dissented, considering that it was desirable to further strengthen monetary easing by lowering short- and long-term interest rates, with a view to responding to an increase in downward pressure on prices and encouraging firms to make active business fixed investment for the post-COVID-19 era.

C. Vote on the Guideline for Asset Purchases

To reflect the view of the members, the chairman formulated the following proposal on the guideline for asset purchases and put it to a vote.

The Policy Board decided the proposal by a unanimous vote.

The Chairman's Policy Proposal on the Guideline for Asset Purchases:

The guideline for asset purchases other than JGB purchases will be as follows.

1. The Bank will purchase ETFs and J-REITs as necessary with upper limits of about 12 trillion yen and about 180 billion yen, respectively, on annual paces of increase in their amounts outstanding.

2. The Bank will purchase CP and corporate bonds with an upper limit on the amount outstanding of about 20 trillion yen in total until the end of September 2021.

Votes for the proposal: Mr. KURODA Haruhiko, Mr. AMAMIYA Masayoshi, Mr. WAKATABE Masazumi, Mr. SAKURAI Makoto, Ms. MASAI Takako, Mr. SUZUKI Hitoshi, Mr. KATAOKA Goushi, Mr. ADACHI Seiji, and Mr. NAKAMURA Toyoaki.

Votes against the proposal: None.

D. Vote on "Establishment of 'Principal Terms and Conditions of the Interest Scheme to Promote Lending'"

Members voted unanimously to approve "Establishment of 'Principal Terms and Conditions of the Interest Scheme to Promote Lending'," which represented the aforementioned staff reports.

E. Discussion on the Statement Entitled "Further Effective and Sustainable Monetary Easing"

On the basis of the above discussions, members discussed the statement "Further Effective and Sustainable Monetary Easing." Mr. Kataoka expressed the opinion that, in order to avoid Japan's economy returning to deflation, further coordination of fiscal and monetary policy was necessary and it was appropriate for the Bank to revise the forward guidance for the policy rates to relate it to the price stability target.

Based on this discussion, the chairman formulated the statement "Further Effective and Sustainable Monetary Easing" and put it to a vote. The Policy Board decided the text by a unanimous vote. It was confirmed that the statement would be released immediately after the meeting (see Attachment 1).

VII. Approval of the Minutes of the Monetary Policy Meeting

The Policy Board approved unanimously the minutes of the Monetary Policy Meeting of January 20 and 21, 2021, for release on March 24.

Attachment 1
March 19, 2021
Bank of Japan

Further Effective and Sustainable Monetary Easing

1. Assessment for Further Effective and Sustainable Monetary Easing

At the Monetary Policy Meeting held today, the Bank of Japan conducted an assessment for further effective and sustainable monetary easing (see Attachment 2). Based on the findings, the Bank judged that the following basic stance on monetary policy was important: with a view to achieving the price stability target of 2 percent, the Bank will continue with monetary easing in a sustainable manner and make nimble and effective responses without hesitation to counter changes in developments in economic activity and prices, as well as in financial conditions.

In this regard, the Bank will take the following actions.

(1) With a view to enabling the Bank to cut short- and long-term interest rates nimbly while considering the impact on the functioning of financial intermediation, the Bank will establish the Interest Scheme to Promote Lending. In this scheme, interest rates, which will be linked to the short-term policy interest rate, will be applied to a certain amount of financial institutions' current account balances (see Attachment 3).

(2) In order to conduct yield curve control flexibly during normal times, the Bank will make clear that the range of 10-year Japanese government bond (JGB) yield fluctuations would be between around plus and minus 0.25 percent from the target level. At the same time, it will introduce "fixed-rate purchase operations for consecutive days" as a powerful tool to set an upper limit on interest rates when necessary.

(3) The Bank will purchase exchange-traded funds (ETFs) and Japan real estate investment trusts (J-REITs) as necessary with upper limits of about 12 trillion yen and about 180 billion yen, respectively, on annual paces of increase in their amounts outstanding. While these upper limits were originally set as a temporary measure in response to the impact of the novel coronavirus (COVID-19), the Bank will maintain them even after COVID-19 subsides.

2. Conduct of Monetary Policy for the Intermeeting Period

Given the current situation of and the outlook for economic activity and prices, which are described in Attachment 4, the Policy Board of the Bank decided upon the following with regard to the conduct of monetary policy.

(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 a necessary amount of JGBs without setting an upper limit so that 10-year JGB yields will remain at around zero percent.

(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 ETFs and J-REITs as necessary with upper limits of about 12 trillion yen and about 180 billion yen, respectively, on annual paces of increase in their amounts outstanding.

b) The Bank will purchase CP and corporate bonds with an upper limit on the amount outstanding of about 20 trillion yen in total until the end of September 2021.

3. Future Conduct of Monetary Policy

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 continue to support financing mainly of firms and maintain stability in financial markets through (1) the Special Program to Support Financing in Response to the Novel

Coronavirus (COVID-19), (2) an ample provision of yen and foreign currency funds without setting upper limits mainly by purchasing JGBs and conducting the U.S. dollar funds-supplying operations, and (3) purchases of ETFs and J-REITs with upper limits of about 12 trillion yen and about 180 billion yen, respectively, on annual paces of increase in their amounts outstanding.

For the time being, the Bank will closely monitor the impact of COVID-19 and will not hesitate to take additional easing measures if necessary, and also it expects short- and long-term policy interest rates to remain at their present or lower levels. [Note 2]

[Note 1] Voting for the action: Mr. KURODA Haruhiko, Mr. AMAMIYA Masayoshi, Mr. WAKATABE Masazumi, Mr. SAKURAI Makoto, Ms. MASAI Takako, Mr. SUZUKI Hitoshi, Mr. ADACHI Seiji, and Mr. NAKAMURA Toyoaki. Voting against the action: Mr. KATAOKA Goushi. Mr. Kataoka dissented, considering that it was desirable to further strengthen monetary easing by lowering short- and long-term interest rates, with a view to responding to an increase in downward pressure on prices and encouraging firms to make active business fixed investment for the post-COVID-19 era.

[Note 2] Mr. Kataoka dissented, considering that, in order to avoid Japan's economy returning to deflation, further coordination of fiscal and monetary policy was necessary and it was appropriate for the Bank to revise the forward guidance for the policy rates to relate it to the price stability target.

Attachment 2

Assessment for Further Effective and Sustainable Monetary Easing

The Bank's View

I. Findings of the Assessment

A. Developments in Economic Activity and Prices under Quantitative and Qualitative Monetary Easing (QQE) with Yield Curve Control

QQE with Yield Curve Control, which the Bank introduced in September 2016 based on the findings of the Comprehensive Assessment, has the following three aims. The first, with a view to achieving the price stability target of 2 percent, is to maintain the output gap in positive territory for as long as possible, given that the mechanism of inflation expectations formation in Japan is largely adaptive. The second is to introduce a framework in which the Bank controls interest rates to appropriate levels while taking into consideration both the positive and side effects of monetary easing, with the expectation that monetary easing will be prolonged. The third is to strengthen the forward-looking element of inflation expectations formation with the inflation-overshooting commitment.

Following the Comprehensive Assessment, the situation where the inflation rate does not rise easily has continued, mainly because (1) the mechanism of adaptive inflation expectations formation in Japan is complex and sticky, (2) elastic labor supply has constrained wage increases, and (3) a rise in firms' labor productivity has absorbed upward pressure on costs. The impact of the novel coronavirus (COVID-19) has put downward pressure on prices recently. Under these circumstances, QQE with Yield Curve Control has kept real interest rates at low levels and improved financial conditions through a decline in funding costs as well as favorable conditions in financial and capital markets. As a result, the output gap has expanded in positive territory and positive inflation has taken hold with improvement in the employment and income situation. In addition, due to the improved output gap and tightened labor market conditions, labor force participation of women and seniors has increased and firms have improved their labor productivity. This shows that favorable economic developments have continued under the Bank's large-scale monetary easing. Against this background, positive moves toward addressing the medium- to long-term challenges facing Japan's economy have been observed.

With a view to achieving the price stability target of 2 percent, it is appropriate for the Bank to continue with QQE with Yield Curve Control, which has been effective in pushing up economic activity and prices.

B. Policy Effects of QQE with Yield Curve Control

QQE with Yield Curve Control has been effective in pushing up economic activity and prices through a decline in interest rates. Specifically, the Bank found the following: (1) the policy effects have been transmitted mainly through a decline in funding costs and favorable conditions in financial and capital markets; (2) the effects of the decline in interest rates on economic activity and prices are relatively large for short- and medium-term interest rates; and (3) an excessive decline in super-long-term interest rates could lead to anxiety about the future sustainability of the functioning of financial activities in a broader sense and have a negative impact on economic activity by, for example, undermining people's sentiment.

C. Effects on the Functioning of the Japanese Government Bond (JGB) Market and Financial Intermediation

Under yield curve control, the Bank controls short- and long-term interest rates to appropriate levels. That said, if fluctuations in interest rates stay within a certain range, they will have positive effects on market functioning without impairing the effects of monetary easing. It is important to strike an appropriate balance between maintaining market functioning and controlling interest rates by allowing interest rates to fluctuate to a certain degree, mainly in response to developments in economic activity and prices. From this perspective, as a measure to strengthen the framework for continuous powerful monetary easing, the Bank decided in July 2018 to conduct yield curve control flexibly, and such flexible conduct has been effective in terms of maintaining the functioning of the JGB market.

Due to prolonged low interest rates and structural factors such as the declining population, financial institutions' core profitability has remained on a downtrend and is likely to continue to do so. In the *Outlook for Economic Activity and Prices*, the Bank, based on the *Financial System Report*, has been examining financial imbalances from a longer-term perspective. It was found that prolonged downward pressure on financial institutions' profits may (1) lead to a gradual pullback in financial intermediation and, on the other hand, (2) increase the vulnerability of the financial system, mainly as a result of financial institutions' search for yield behavior.

D. Effects of Exchange-Traded Fund (ETF) and Japan Real Estate Investment Trust (J-REIT) Purchases

ETF and J-REIT purchases have been containing instability in the market by lowering risk premia. In addition, the effects of purchases tend to be greater the higher the instability in financial markets and the larger the size of purchases. This suggests that large-scale purchases during times of heightened market instability are effective.

E. Inflation-Overshooting Commitment

Given that the mechanism of adaptive inflation expectations formation in Japan is complex and sticky, it is necessary to push up inflation under QQE with Yield Curve Control through improvement in the output gap. At the same time, the forward-looking element of inflation expectations formation is important, and in order to strengthen this, the Bank in September 2016 adopted the inflation-overshooting commitment. Through this commitment, the Bank commits to continuing to expand the monetary base until the year-on-year rate of increase in the observed consumer price index (CPI, all items less fresh food) exceeds the price stability target of 2 percent and stays above the target in a stable manner. With this extremely strong commitment, in that the Bank promises to continue with monetary easing based on observed CPI inflation rather than the outlook for CPI inflation, it aims to strengthen people's confidence that the price stability target of 2 percent will be achieved. The "makeup strategy," which is the strategy this commitment is implementing, was examined in this assessment using an economic model. The results of simulations reconfirmed that it was appropriate to employ this strategy as the Bank's monetary policy conduct. Thus, the Bank will continue to pursue the inflation-overshooting commitment.

II. Policy Actions

A. Conduct of Yield Curve Control

1. Establishment of the Interest Scheme to Promote Lending

Cutting short- and long-term interest rates is an important option as a nimble and effective additional easing measure. It is appropriate to cut those rates while considering the impact on the functioning of financial intermediation. With this in mind, the Bank will introduce a scheme which mitigates the impact on financial institutions' profits to a certain degree at the time of rate cuts depending on the amount of their lending. In this scheme, the Bank will apply certain interest rates as an incentive to financial institutions' current account balances, corresponding to the amount outstanding of funds that have been provided through its various fund-provisioning measures to promote financial institutions' lending. The applied interest rates will be linked to the short-term policy interest rate (see Attachment 3).

The eligible fund-provisioning measures and the incentives will be categorized into three groups. As for now, funds provided through the Special Funds-Supplying Operations to Facilitate Financing in Response to the Novel Coronavirus (COVID-19) against loans that financial institutions make on their own will fall under Category I and an interest rate of 0.2 percent will be applied; funds provided through the Special Funds-Supplying Operations to Facilitate Financing in Response to the Novel Coronavirus (COVID-19) against loans other than those for Category I and against private debt pledged as collateral will fall under Category II and an interest rate of 0.1 percent will be applied; and funds provided through the Loan Support Program and the Funds-Supplying Operation to Support Financial Institutions in Disaster Areas will fall under Category III and an interest rate of 0 percent will be applied. Depending on the situation, the interest rates and the eligible fund-provisioning measures for each category will be changed as necessary at the Monetary Policy Meetings (MPMs).

This scheme will also contribute to enhancing the effectiveness of the additional easing measure of cutting short- and long-term interest rates. Market participants who are not expecting short- and long-term interest rate cuts as an option for additional easing tend to point to the impact on the functioning of financial intermediation. The scheme will enable the Bank to cut those rates more nimbly while considering such impact.

In addition, given developments in financial institutions' current account balances at the Bank since the introduction of the negative interest rate policy, the Bank will modify the method to calculate the Macro Add-on Balances under the Complementary Deposit Facility in order to narrow the gap between the actual Policy-Rate Balances and the "hypothetical" Policy-Rate Balances, which are calculated based on the assumption that arbitrage transactions fully take place.

2. Clarification of the range of fluctuations in long-term interest rates
When the framework for continuous powerful monetary easing was strengthened in July 2018, the Bank, with a view to striking an appropriate balance between maintaining market functioning and controlling interest rates, announced to allow long-term interest rates (10-year JGB yields) to move upward and downward in about double the range, which was previously between around plus and minus 0.1 percent from the target level. Given that there have been times when the range of actual fluctuations in interest rates has become narrow, the Bank considers it appropriate to make clear

that the range of 10-year JGB yield fluctuations would be between around plus and minus 0.25 percent. That said, when, in particular, the yields temporarily fall below the lower limit in day-to-day movements, the Bank will not strictly respond to such developments.

3. Introduction of "fixed-rate purchase operations for consecutive days"
One measure to stop a significant rise in interest rates is the fixed-rate purchase operations, through which the Bank purchases an unlimited amount of JGBs with certain maturities at fixed rates. With a view to further strengthening this operation, the Bank will introduce "fixed-rate purchase operations for consecutive days," through which it will conduct the fixed-rate purchase operations consecutively for a certain period of time.

4. Conduct of yield curve control for the time being
The Bank expects 10-year JGB yields to move within the range of around plus and minus 0.25 percent from the target level. An excessive decline in super-long-term JGB yields could have a negative impact on economic activity from a long-term perspective. That said, under the continuing impact of COVID-19 in particular, the Bank will conduct yield curve control with a priority on stabilizing the entire yield curve at a low level.

B. Asset Purchases and Others
1. Purchases of ETFs and J-REITs
The Bank will purchase ETFs and J-REITs as necessary with upper limits of about 12 trillion yen and about 180 billion yen, respectively, on annual paces of increase in their amounts outstanding. While these upper limits were originally set as a temporary measure in response to the impact of COVID-19, the Bank will maintain them even after COVID-19 subsides. When a purchase is made, it shall be immediately reported to the members of the Policy Board.

With regard to ETF purchases, the Bank will only purchase ETFs tracking the Tokyo Stock Price Index (TOPIX), which is an index with the largest number of component stocks.[8]

2. Purchases of CP and corporate bonds
The Bank will purchase CP and corporate bonds with an upper limit on the amount outstanding of about 20 trillion yen in total until the end of September 2021. A certain amount will continue to be

[8] As for ETFs composed of stocks issued by firms that actively invest in physical and human capital, the Bank will only continue to purchase those that are "managed so that they track the indices the Bank deems eligible in accordance with the eligibility criteria for indices."

purchased even after the purchases in response to the impact of COVID-19 end.

3. Participation of the Financial System and Bank Examination Department at the MPMs

At the MPMs when *the Outlook for Economic Activity and Prices* is decided (four times a year), staff of the Financial System and Bank Examination Department will attend the meeting and explain developments in the financial system to the Policy Board.

Attachment 3

Outline of the Interest Scheme to Promote Lending

1. Purpose

The Bank will establish a scheme to apply certain interest rates as an incentive to financial institutions' current account balances, corresponding to the amount outstanding of funds that have been provided through its various fund-provisioning measures to promote financial institutions' lending. The applied interest rates will be linked to the short-term policy interest rate. This scheme will enable the Bank to cut short- and long-term interest rates more nimbly while considering the impact on the functioning of financial intermediation.

2. Eligible Fund-Provisioning Measures and Incentives

The eligible fund-provisioning measures and the incentives will be categorized into three groups as described below. The applied interest rate for Category II will be the absolute value of the short-term policy interest rate, and a higher rate will be applied for Category I and a lower rate for Category III.

[Today's Decision]

	Applied interest rate (incentive)	Eligible fund-provisioning measure
Category I	0.2%	➢ Special Funds-Supplying Operations to Facilitate Financing in Response to COVID-19, when funds are provided against loans made by financial institutions on their own
Category II	0.1%	➢ Special Funds-Supplying Operations to Facilitate Financing in Response to COVID-19, when funds are provided against loans other than those for Category I and against private debt pledged as collateral
Category III	0%	➢ Loan Support Program ➢ Funds-Supplying Operation to Support Financial Institutions in Disaster Areas

Note: For all categories, twice as much as the amount of increase in loans will be included in the Macro Add-on Balances in current accounts held by financial institutions at the Bank.

(Reference) Hypothetical example of the short-term policy interest rate being minus 0.2 percent

<table>
<tr><th></th><th>Applied interest rate (incentive)</th><th>Eligible fund-provisioning measure</th></tr>
<tr><td>Category I</td><td>Higher than 0.2%</td><td rowspan="3">To be decided in line with the purpose of this scheme</td></tr>
<tr><td>Category II</td><td>0.2%</td></tr>
<tr><td>Category III</td><td>Lower than 0.2%</td></tr>
</table>

Attachment 4

Economic Activity and Prices in Japan: Current Situation and Outlook

1. Japan's economy has picked up as a trend, although it has remained in a severe situation due to the impact of the novel coronavirus (COVID-19) at home and abroad. Overseas economies also have picked up, although the impact of a resurgence of COVID-19 has remained in part. In this situation, exports and industrial production have continued to increase. In addition, corporate profits and business sentiment have improved on the whole. Business fixed investment has picked up, although weakness has been seen in some industries. The employment and income situation has remained weak due to the impact of COVID-19. A pick-up in private consumption has paused recently due to increased downward pressure on consumption of services, such as eating and drinking as well as accommodations. Housing investment has declined moderately. Public investment has continued to increase moderately. Financial conditions have been accommodative on the whole but those for corporate financing have remained less so, as seen in weakness in firms' financial positions. On the price front, the year-on-year rate of change in the consumer price index (CPI, all items less fresh food) has been negative, mainly affected by COVID-19 and the past decline in crude oil prices. Inflation expectations have weakened somewhat.

2. Japan's economy, with the impact of COVID-19 waning gradually, is likely to follow an improving trend, supported by a recovery in external demand, accommodative financial conditions, and the government's economic measures. However, the pace of improvement is expected to be only moderate while vigilance against COVID-19 continues. Specifically, downward pressure on face-to-face services consumption is likely to remain in the short run due to the impact of the resurgence of COVID-19 since last autumn. Thereafter, as the impact of COVID-19 subsides globally, the economy is projected to keep improving further with overseas economies returning to a steady growth path. The year-on-year rate of change in the CPI (all items less fresh food) is likely to be negative for the time being, mainly affected by COVID-19 and the past decline in crude oil prices. Thereafter, it is expected to turn positive and then increase gradually, since downward pressure on prices is projected to wane gradually along with economic improvement and the effects of such factors as the decline in crude oil prices are likely to dissipate.

3. With regard to risks to the outlook, there have been extremely high uncertainties over the consequences of COVID-19 and the magnitude of their impact on domestic and overseas economies. In addition, it is necessary to pay close attention to whether, while the impact of COVID-19 remains, firms' and households' medium- to long-term growth expectations will not decline substantially and the smooth functioning of financial intermediation will be ensured with financial system stability being maintained.