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March 19, 2018

Bank of Japan

Summary of Opinions at the Monetary Policy Meeting^{1,2} on March 8 and 9, 2018

I. Opinions on Economic and Financial Developments

Economic Developments

- Japan's economy is expanding moderately, with a virtuous cycle from income to spending operating. Going forward, it is likely to continue expanding on the back of highly accommodative financial conditions and underpinnings through the government's past stimulus measures.
- Japan's economy is expanding moderately. Further tightening is being seen in terms of both labor and capital, and firms are starting to work on expanding their production capacity. It is important that the virtuous cycle in which such strong demand encourages firms to make progress in their reforms will be maintained over a long period.
- Japan's economy has been growing in a well-balanced manner, with both the supply and demand sides improving. The negative hysteresis -- such as firms' inefficient business processes, their negative stance toward investment, and a decrease in the labor force participation rate -- that has become entrenched through the prolonged shortage of demand and deflation has been dissipating, along with an expansion in demand.
- Quantitative and qualitative monetary easing (QQE) is a policy that brings about improvement in not only prices but also the economy as a whole, including production and employment, and it has made considerable achievements. For instance, although the

¹ English translation prepared by the Bank's staff based on the Japanese original.

² "Summary of Opinions at the Monetary Policy Meeting" is made through the following process: (1) each Policy Board member and government representative makes a summary of opinions that she/he presented at the Monetary Policy Meeting (MPM) under a certain word limit and submits this to the Governor of the Bank of Japan, who serves as the chairman of the MPM, and (2) the chairman edits those opinions as his responsibility.

structural unemployment rate was formerly said to be around 3.5 percent, the actual unemployment rate has continued to decline and registered 2.4 percent recently.

- The weak recovery in household consumption since last summer is of concern. It is necessary to pay due attention to the extent to which the favorable effects resulting from an increase in exports spread to the household sector through wage increases.
- Although corrections in financial markets at home and abroad since February do not appear to have had large negative effects so far on the real economy, which has been firm, their effects on sentiment should be carefully monitored. Developments surrounding North Korea continue to be considered as a geopolitical risk.
- The effects of the recent fluctuations in financial markets -- such as a rise in U.S. interest rates, declines in U.S. and Japanese stock prices, and a heightening of market volatility -- on financial institutions' financial conditions need to be carefully examined.
- If the current trends of the appreciation of the yen and the decline in stock prices become prolonged, business fixed investment and consumption will be restrained due to negative wealth effects and a deterioration of households' and firms' balance sheets, and the profits of export industries will decrease due to the adverse effects on exports. As these will constrain wages and prices, there will be a risk of a delay in achieving the price stability target.

Prices

- The year-on-year rate of change in the consumer price index (CPI) is likely to continue on an uptrend and increase toward 2 percent, mainly on the back of an improvement in the output gap and a rise in medium- to long-term inflation expectations.
- As the start of the new fiscal year approaches, there have been signs of changes in firms' price-setting stance, as seen in price rises being widely reported by the media.
- In forecasting future developments in wages and prices, it is worth paying close attention to the results of the annual spring labor-management wage negotiations.
- In terms of projecting price developments, the key is to what extent wage developments after the annual spring labor-management wage negotiations will improve individual firms' price-setting stance and consumers' acceptance of price rises.

- Although wage increases by firms have been at around 2 percent for the past few years, real wages registered negative growth in 2017 on a year-on-year basis. Close attention should be paid to whether the rate of increase in wages including bonuses will be sufficient to push up the year-on-year rate of change in real wages to positive territory.
- The year-on-year rate of change in the CPI (all items less fresh food) is likely to increase moderately toward 2 percent. However, moves to raise prices have not been pronounced, and it is likely to take time to dispel the deflationary mindset.
- The momentum of inflation is not strong enough to achieve the price stability target of 2 percent early.

II. Opinions on Monetary Policy

- Considering that there is still a long way to go to achieve the price stability target of 2 percent, it is appropriate to pursue powerful monetary easing with persistence under the current guideline for market operations in order to firmly maintain the momentum toward achieving the price stability target.
- There is no change in the judgment that it is necessary to continue pursuing powerful monetary easing with persistence so that highly accommodative financial conditions are maintained.
- The Bank should continue with the current monetary policy with the aim of persistently encouraging the virtuous cycle to take hold and achieving the price stability target.
- The Bank should aim to achieve the price stability target while gaining consensus among the public on the importance of overcoming deflation.
- Amid the inflation rate increasing toward 2 percent and the potential growth rate rising going forward, the effects of monetary easing measures will be enhanced. It will be necessary to consider appropriate policy conduct while taking into account such changes in the environment as well as the side effects of the measures.
- Looking at recent developments in the Japanese government bond (JGB) and corporate bond markets, as well as in bank lending, the effects of the decline in the long-term real interest rates on economic activity and prices could be becoming smaller than expected. It is important to consider the desirable shape of the yield curve while taking these effects into consideration.

- Since the introduction of QQE, Japan's economy has reached a state of no longer being in deflation. It is important to augment the momentum of the virtuous cycle that has emerged during this process through additional easing measures -- that is, having yields on JGBs with maturities of 10 years and longer broadly lowered further and reinforcing the inflation-overshooting commitment -- and thereby put an end to deflation.
- The purchases of risky assets including exchange-traded funds (ETFs) are carried out as part of the policy package aiming at achieving the price stability target, and their policy effects and the possible side effects should continue to be examined from every angle.
- As developments in profits of financial institutions have a cumulative impact on their financial strength, there will be a risk of a pullback in financial intermediation if the low-yield environment is further prolonged.
- As there is still a long way to go to achieve the price stability target of 2 percent, this is not the phase in which the Bank should consider "normalization" -- that is, gradually reducing the degree of monetary accommodation -- in a concrete manner. However, the Bank needs to explain to market participants so that they can fully understand that "normalization" is still in the process of monetary accommodation and completely different from monetary tightening, which aims at reducing the positive output gap. Such explanation will also be beneficial in smoothly proceeding with "normalization" in the future.
- If there is a heightened risk that achieving the price stability target will be delayed, additional monetary easing will be needed; however, as there is not ample room for further monetary easing, fiscal policy is also necessary in overcoming deflation. In that regard, it is desirable to aim at achieving a surplus in the primary balance by setting an appropriate quantitative target in light of developments in economic activity and prices, as well as financial conditions.
- Among the dissenting views with QQE, some represent what is called cognitive dissonance in the field of psychology. This is the situation of feeling uncomfortable when confronted with a new fact that is contrary to belief. When one recognizes the fact that the economy is improving, contrary to his belief that QQE would not improve the economy, he tries to reduce the discomfort by denying the fact or insisting that the economy will surely deteriorate in the future although it is currently improving.

III. Opinions from Government Representatives

Ministry of Finance

- The budget for fiscal 2018 was approved by the House of Representatives recently and is being deliberated in the House of Councillors.
- The government considers that early passage of the budget is the most important measure for stimulating the economy, and it will continue to work toward promptly obtaining the Diet's approval of the budget and related bills in order to ensure a virtuous economic cycle and achieve sustainable economic growth.
- The government expects the Bank to continue to work toward achieving the price stability target under "QQE with Yield Curve Control" in light of developments in economic activity and prices, as well as financial conditions.

Cabinet Office

- With regard to the work style reform bills, the government will completely remove all items related to the amendments concerning the discretionary working system, but will aim at obtaining the Diet's approval of the remaining parts during the current session.
- The government will conduct a detailed study and present a direction regarding systems for accepting foreign personnel with specialized and technical skills.
- The government will prepare to submit to this session of the Diet the Comprehensive and Progressive Agreement for Trans-Pacific Partnership, known as the TPP-11, and related domestic bills.
- The government expects that the Bank will work steadily toward achieving the price stability target of 2 percent in light of developments in economic activity and prices, as well as financial conditions.