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July 28, 2021

Bank of Japan

Summary of Opinions at the Monetary Policy Meeting^{1,2} on July 15 and 16, 2021

I. Opinions on Economic and Financial Developments

Economic Developments

- 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.
- The global economy has maintained its recovery trend on the whole, although unevenness in the pace of recovery across countries and regions, depending on progress with vaccinations, and uncertainties over the spread of the COVID-19 variants remain.
- Although the level of Japan's economic activity, mainly in the face-to-face services sector, is expected to be relatively low for the time being, the economy is likely to recover, with the impact of COVID-19 waning gradually, mainly due to progress with vaccinations.
- In Japan's economy, downward pressure on consumption is likely to intensify in the short run due to the reinstatement of the state of emergency. However, from a somewhat long-term perspective, the recovery trend in the economy is projected to strengthen due to continuing accommodative financial conditions and an expected increase in business fixed investment.
- The results of recently released statistics, including the June 2021 *Tankan* (Short-Term Economic Survey of Enterprises in Japan), seem to indicate that labor shortage has become somewhat acute, mainly in the manufacturing industry. If employee income picks up in this situation, consumption could gain strength.

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.

- Business performance has improved on the back of increases in exports and production. However, the timing of a full-fledged recovery is likely to be somewhat delayed, reflecting the impact of the resurgence of COVID-19.
- For the time being, there is a risk that economic activity will be under further downward pressure stemming from the spread of COVID-19. On the other hand, if the vaccine rollout accelerates, it could improve by more than expected.
- Although economic activity is expected to improve as vaccinations progress, attention should continue to be paid to the consequences of COVID-19 and downside risks to economic activity and prices under tightening public health measures.
- Japan's economy is likely to recover amid progress with vaccinations. However, attention is warranted on stagnant improvement in employment and subdued stock prices compared with those in Europe and the United States.
- When households invest some of their cash and deposits into stocks or investment trusts from the perspective of appropriate risk diversification and long-term holdings, they are expected to benefit from growth in overseas economies through dividends and other income.
- There have been changes in the environment surrounding foreign exchange markets, such as changes in price-setting behavior of exporting firms, shifts to overseas local production, and the recurrence of purchases of the U.S. dollar as a safe-haven currency in an emergency situation, which was observed last spring. It is necessary to closely monitor how such environmental changes have influence on the transmission channels through which a decline in interest rates affects economic activity.
- Economic activity could be affected in the future in the process of securing fiscal resources for taking measures in response to COVID-19. Therefore, forthcoming discussions on fiscal soundness warrant close attention.

Prices

- The year-on-year rate of change in the consumer price index (CPI) is likely to be at around 0 percent in the short run. Thereafter, it is expected to increase gradually on the back of continued improvement in economic activity.
- The year-on-year rate of change in the CPI has been on an uptrend, when excluding such temporary factors as a reduction in mobile phone charges.

- Firms' price cuts that aim at stimulating demand have not been observed widely. Their price-setting stance is projected to gradually become active with the impact of COVID-19 subsiding.
- Attention should be paid to future developments in international commodity prices, particularly for crude oil, and their impact on producer prices, firms' price-setting behavior, and households' tolerance of price rises.
- Despite rising international commodity prices, no significant change has been seen in inflation expectations, and they are not yet strong enough to achieve the price stability target.

II. Opinions on Monetary Policy

Conduct of Monetary Policy

- The Bank should continue to support financing, mainly of firms, and maintain stability in financial markets by conducting monetary easing through the three measures.
- Although the environment for external funding has remained favorable, there is still weakness in financial positions, particularly of firms. It is appropriate for the Bank to continue to support financing, mainly of firms.
- Even though the year-on-year rate of change in the CPI excluding fresh food is likely to increase on the back of a rise in commodity prices, there is a long way to go to achieve the price stability target of 2 percent and maintain that level in a stable manner. Thus, it is important not to tighten monetary policy prematurely.
- Some advanced economies where large-scale fiscal support measures have been conducted have seen a rise in inflation rates with the economy normalizing on the back of progress with vaccinations, and have started to seek ways to reduce monetary accommodation. Given that the deflationary mindset is strongly entrenched in Japan, the Bank should persistently continue with monetary easing, while cooperating with the government, so as to achieve the price stability target of 2 percent.
- In the conduct of monetary policy, the Bank should strengthen its monetary easing stance with a view to improving the output gap and inflation expectations, and thereby achieve an economic recovery and the price stability target early.

Fund-Provisioning Measure to Support Efforts on Climate Change

- Given the actions taken around the world at present in fields related to climate change, the Bank's new fund-provisioning measure to provide funds against investment or loans that contribute to addressing climate change is appropriate, in that it gives consideration to market neutrality and allows for policy flexibility at the same time.
- The Bank's new fund-provisioning measure is appropriate, in that discipline will be exercised by asking financial institutions to disclose a certain level of information while leaving concrete decisions to them on which investment or loans to be eligible.
- In order to receive funds from the Bank through the new fund-provisioning measure to support efforts on climate change, financial institutions need to disclose a certain level of information both ex ante and ex post from the viewpoint of policy accountability and data collection. Given the importance of transition risks, this measure should cover transition finance. In addition, the policy effects of the measure should be reviewed.
- Taking into account that the external environment surrounding climate change is fluid, the Bank should carefully decide on the scope of the new fund-provisioning measure to support efforts on climate change while paying due attention to the relationship with its mandate.
- For the new fund-provisioning measure, which will be conducted over a long period, the interest rate should be 0 percent and the applied interest rate in the Interest Scheme to Promote Lending also should be 0 percent. In addition, rollovers can be made until the end of fiscal 2030, so that the Bank can effectively provide long-term financing to financial institutions.
- With the fund-provisioning measure to support efforts on climate change, the Bank will make sustained and positive efforts that can contribute to stabilizing the macroeconomy in the long run. Against this backdrop, it is critically important that the Bank clearly explain its stance and strategy toward addressing climate change, so that not only market participants at home and abroad but also each Japanese citizen gain an accurate understanding of the Bank's efforts.
- In Japan, the economy is largely dependent on fossil fuel, and indirect financing has a major role. If the Bank directly intervenes in addressing climate change, various distortions may occur in the financial system. This can be avoided with the new fund-provisioning measure, which will support investment or loans that financial institutions make to address climate change based on their own decisions.

- In order to make economic and social transformation toward addressing climate change, an ecosystem needs to be established where a large amount of funds is invested in a sustainable manner. The Bank should contribute to the transformation by, for example, disseminating necessary information while appropriately grasping changes in the situation abroad, such as ongoing discussions over the introduction of a border carbon tax and the development of a green bond market.
- Undertaking new research and development as well as business fixed investment is essential in achieving a decarbonized society, and they cannot be carried out without economic growth. It is important for the Bank to further conduct research and study with a view to addressing climate change and achieving economic growth simultaneously.
- When addressing climate change from the monetary policy side, it is necessary for the Bank to examine, without having any preconceptions, its impact on economic activity and prices by further carrying out research and study that will form the basis of policy decisions.
- It is important for the Bank to continue with in-depth analysis and research on how specifically climate change will affect the macroeconomy.

III. Opinions from Government Representatives

Ministry of Finance

- At the Group of Twenty (G20) meeting, a wide range of challenges including climate change was discussed, and there has been progress with international cooperation. The Bank's new fund-provisioning measure to support efforts on climate change is in line with this global trend.
- The budget for fiscal 2022 will focus on areas that will drive new growth, including the green society. The government will continue to make efforts toward expenditure reforms and pursue economic revitalization and fiscal soundness.
- The government expects the Bank to conduct necessary measures appropriately, including responses to COVID-19, while cooperating with the government.

Cabinet Office

- In the Cabinet Office's mid-year economic projection, it is expected that Japan's real GDP will recover to the pre-pandemic level within this year and be at a record high for fiscal 2022.

- The government will continue to swiftly conduct vaccinations. Based on the Basic Policy on Economic and Fiscal Management and Reform 2021, it will make efforts to realize strong growth led by private demand and to create an environment where wage increases are possible.
- The government recognizes that the introduction of the Bank's fund-provisioning measure to support efforts on climate change has been decided in a timely manner, in that it is in line with the government's efforts to achieve the green society. It expects the Bank to continue to closely cooperate with the government.