

# Path toward Overcoming Deflation

*Speech at a Meeting with Business Leaders in Nagoya*

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Introduction

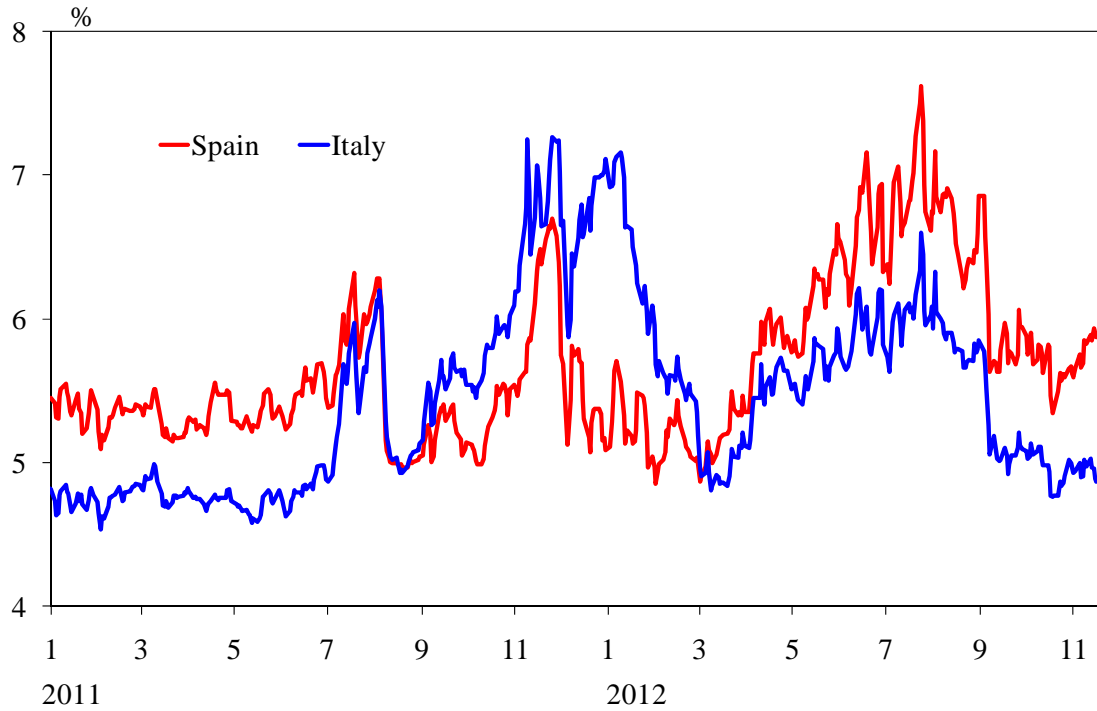
1. Developments in Overseas Economies and in Exchange Rates
2. Recent Developments in and the Outlook for Japan's Economy
3. Recent Conduct of Monetary Policy
4. Path toward Overcoming Deflation

Concluding Remarks

Chart 1

Nervousness in financial markets due to the European debt problem has subsided compared with around this time last year.

*Interest Rates on 10-Year Government Bonds in Spain and Italy*



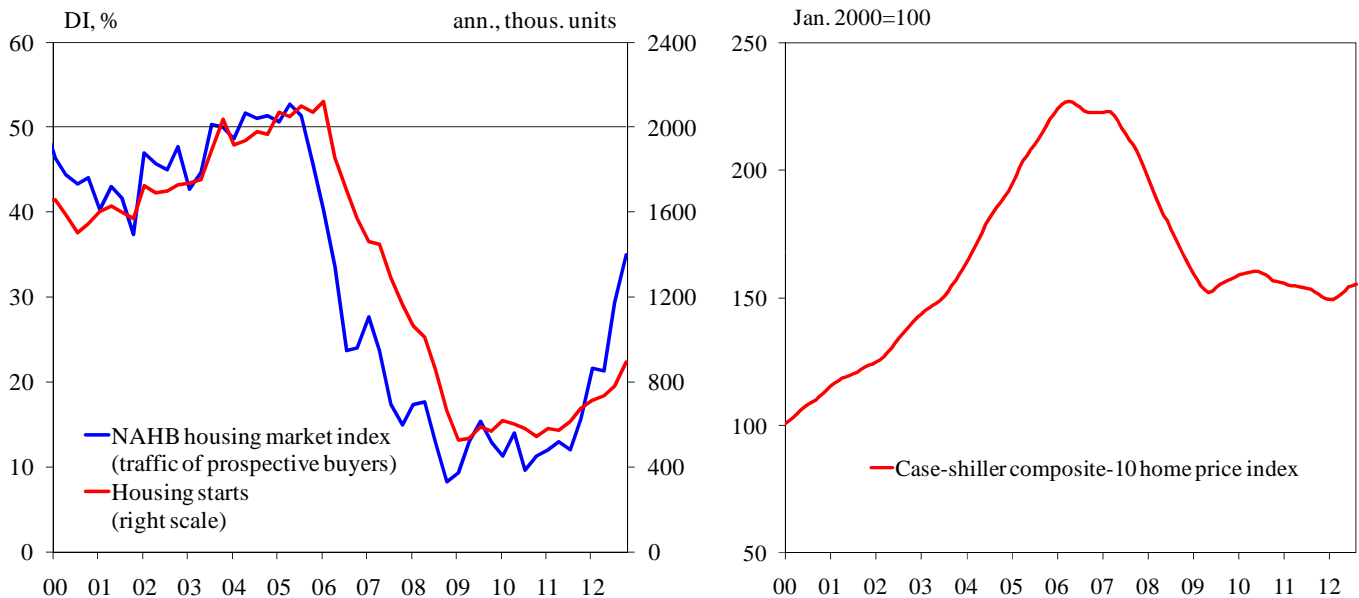
Source: Bloomberg.

Chart 2

U.S. housing investment appears to be bottoming out despite its continued low level.

*Housing Starts*

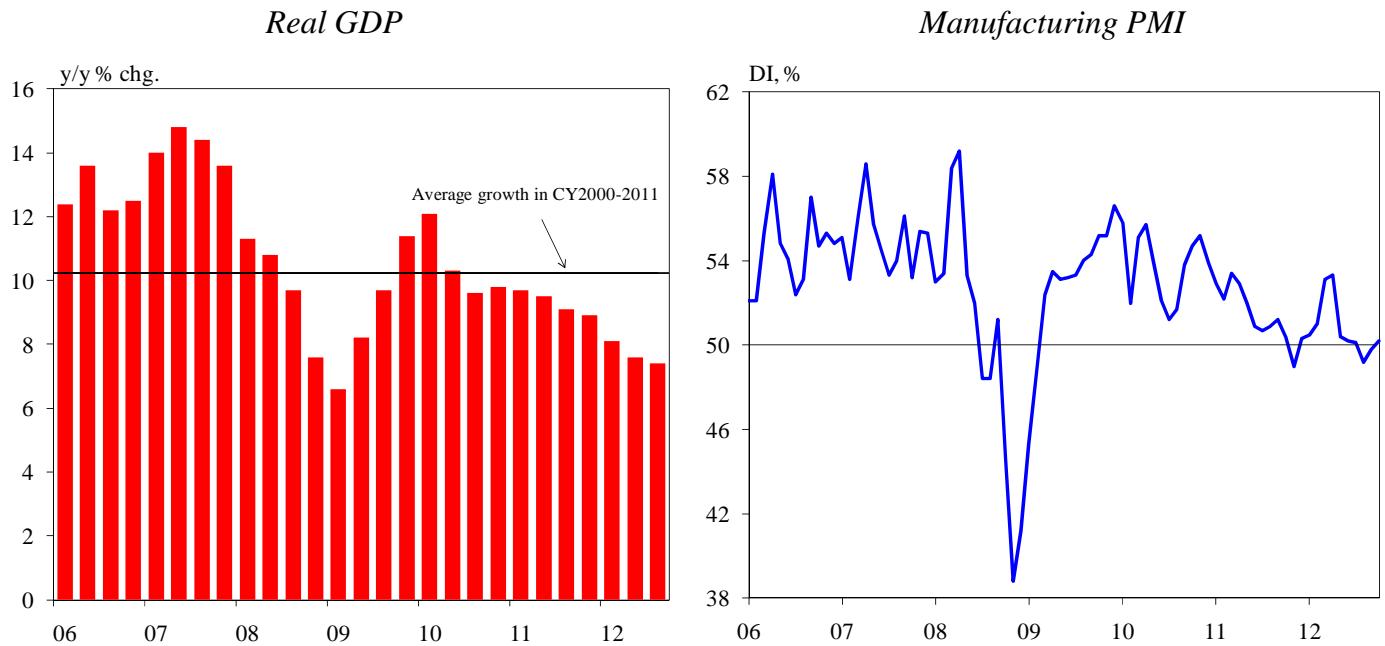
*Housing Prices*



Note: The NAHB housing market index is created by the NAHB using data derived from the result of survey conducted on construction enterprises. Sources: Census Bureau; NAHB; S&P.

Chart 3

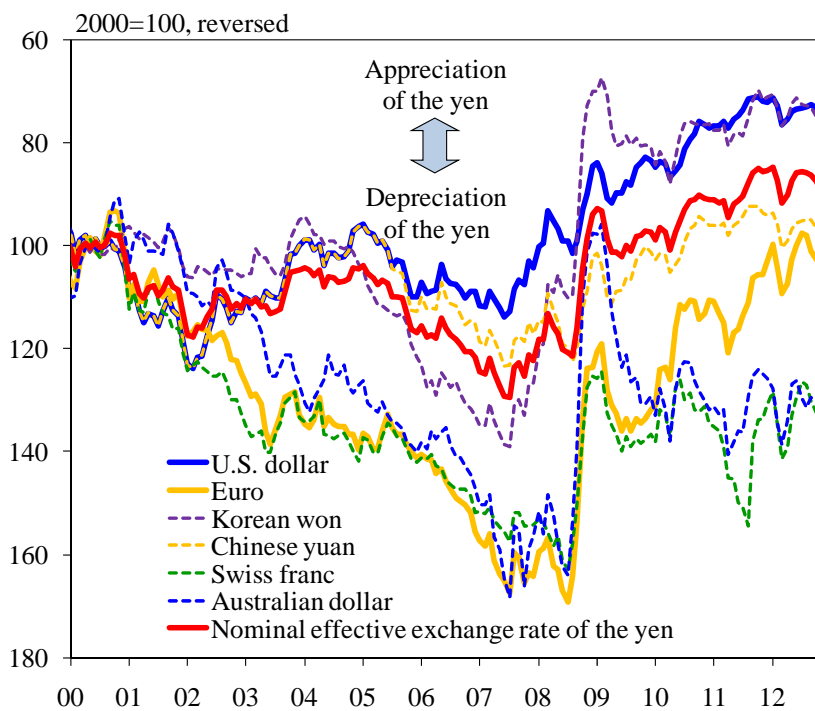
Deceleration of the Chinese economy has been prolonged, although the growth rate remains at a high level.



Note: A reading of 50 percent on manufacturing PMI generally indicates a turning point between economic expansion and contraction in the manufacturing sector.  
Source: National Bureau of Statistics of China.

Chart 4

Swings in the Yen's Exchange Rates



	% chg.			
	Nov. 2002 ↓ Nov. 2007	Nov. 2007 ↓ Nov. 2012	Nov. 2007 ↓ Nov. 2011	Nov. 2011 ↓ Nov. 2012
U.S. dollar	-8.6	-27.6	-30.2	3.8
Euro	33.7	-36.9	-35.4	-2.2
Korean won	20.4	-38.9	-43.5	8.1
Chinese yuan	1.9	-13.8	-18.5	5.7
Swiss franc	19.0	-13.7	-13.5	-0.2
Australian dollar	45.9	-16.1	-21.4	6.8
Nominal effective exchange rate of the yen	9.0	-26.5	-29.3	3.9

Note: Positive figures indicate a depreciation of the yen, and vice versa.

- Notes: 1. The nominal effective exchange rate is an indicator that measures the overall value of individual currencies. It is derived by calculating the weighted average of each currency's exchange rate against other currencies using the annual value of each country's trade with its counterparties as its weights.  
2. The effective exchange rates are based on the broad indices of the BIS effective exchange rate. Figures for November 2012 have been calculated using the Bank of Japan's nominal effective exchange rate of the yen.  
3. The nominal effective exchange rate in this chart is calculated by using the inverse of the indices released by the BIS such that a rise in the figures indicates a depreciation of the yen, and vice versa.

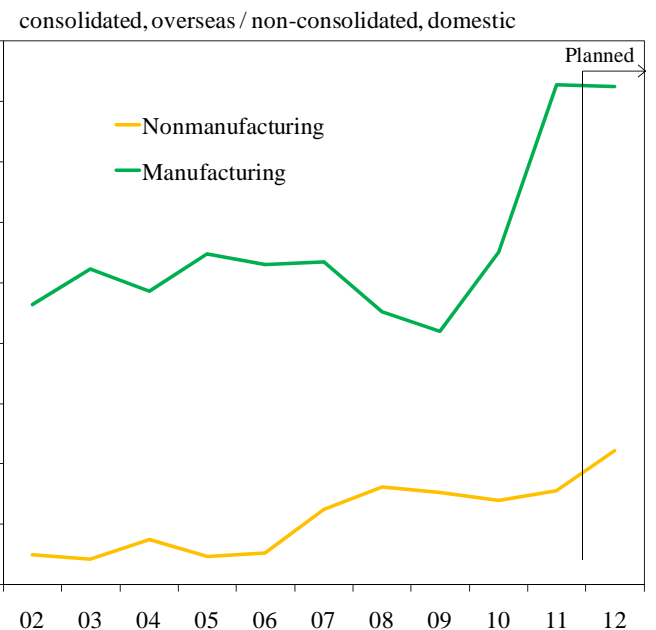
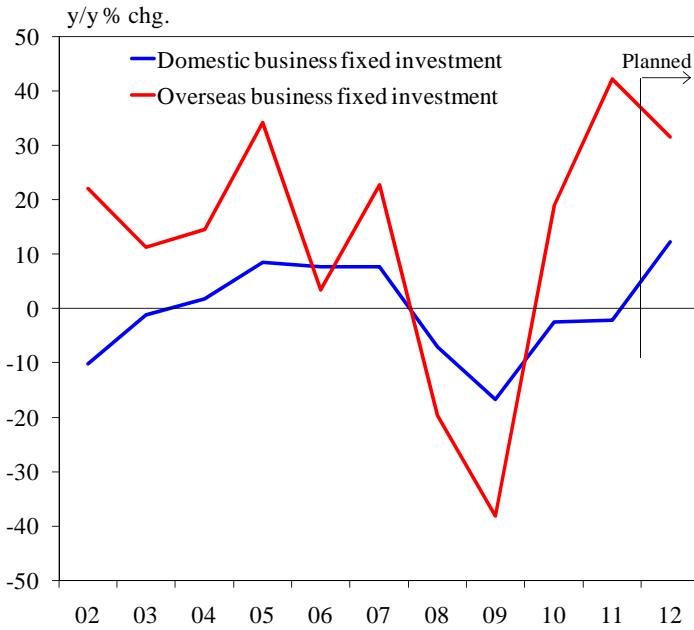
Sources: BIS; Bloomberg; Bank of Japan.

Chart 5

The share of overseas business fixed investment has been rising further in recent years against the background of expansion of the overseas market.

*Domestic and Overseas Business Fixed Investment*

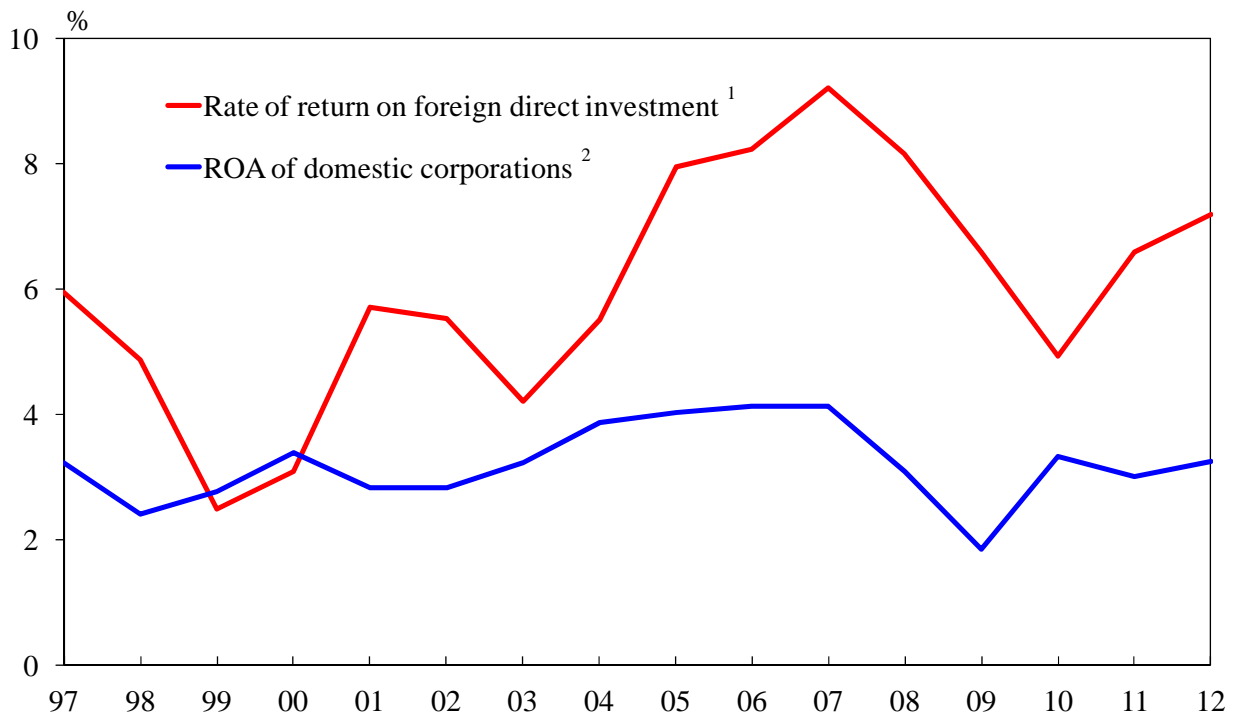
*Ratio of Overseas Business Fixed Investment to Domestic Business Fixed Investment*



Source: Development Bank of Japan.

Chart 6

Rates of return on investment overseas are relatively high.



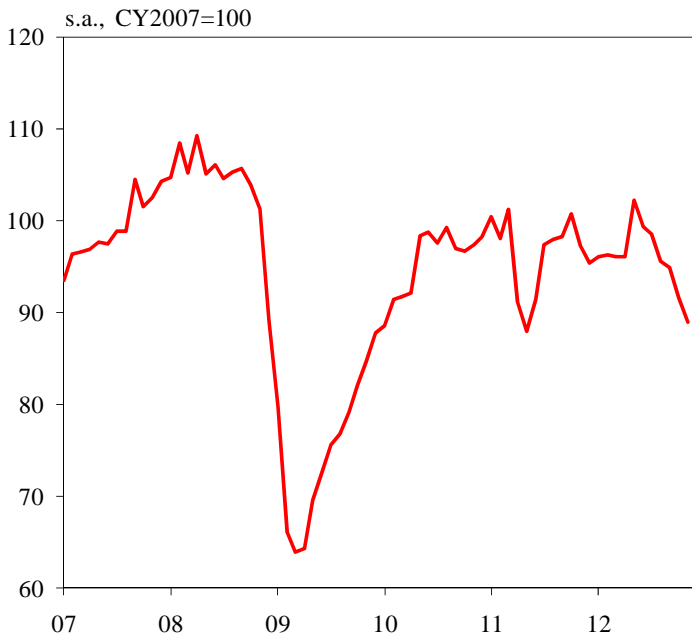
Notes: 1. Figures are calculated as direct investment income (based on the "Balance of Payments") divided by direct investment assets.  
 2. Figures are calculated as operating profits divided by total assets, based on all-size enterprises and all industries, and exclude finance and insurance.  
 3. Figures for 2012 are January-June averages.

Sources: Ministry of Finance; Bank of Japan.

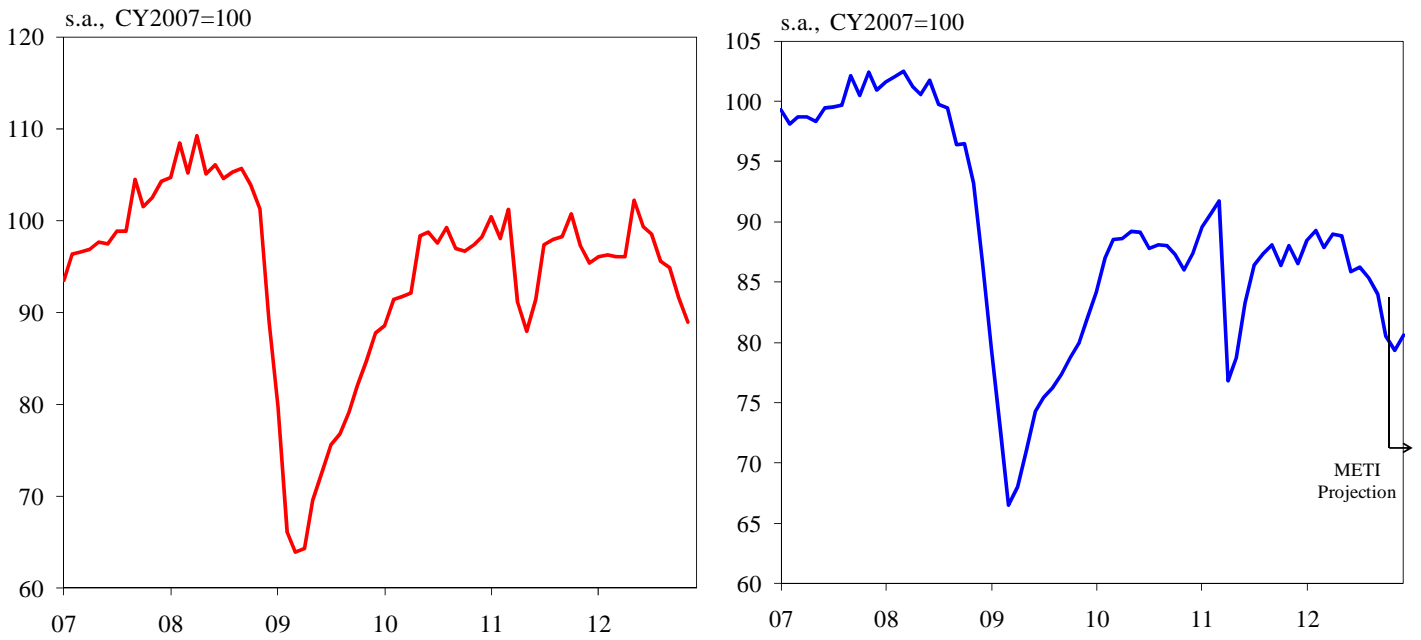
Chart 7

Exports and production are decreasing, mainly due to the prolonged deceleration in overseas economies.

*Real Exports*



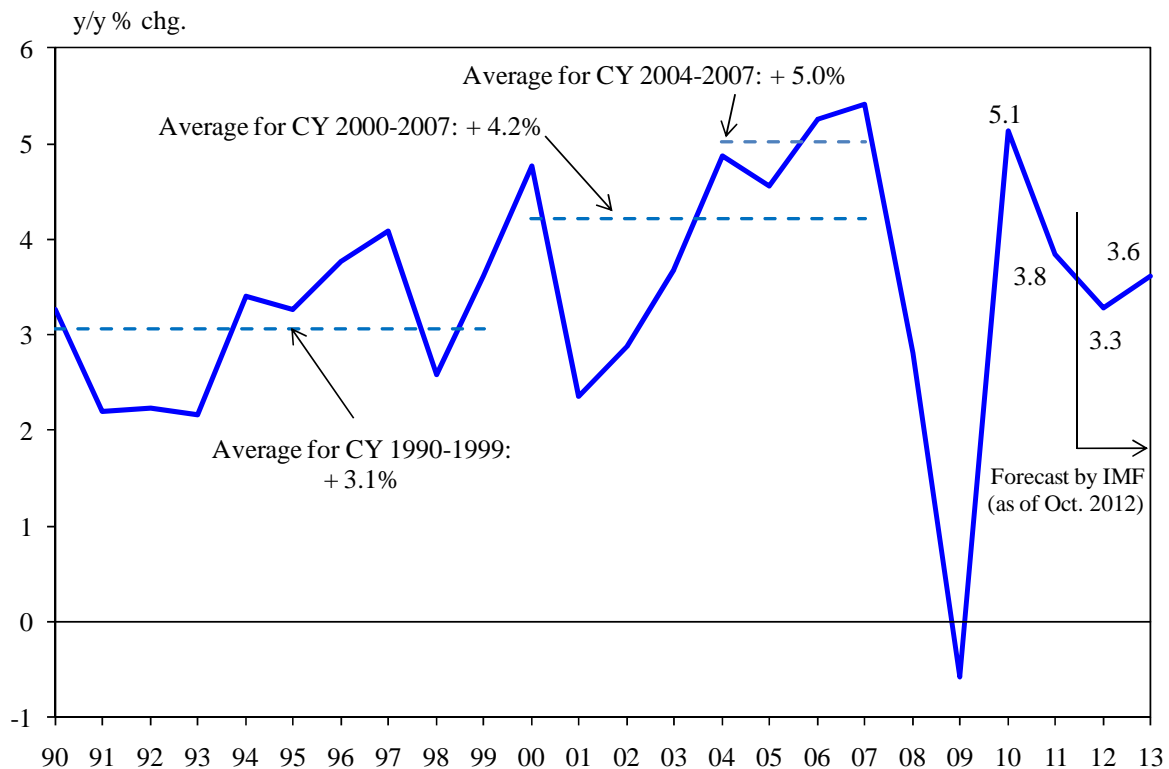
*Industrial Production*



Sources: Bank of Japan; Ministry of Economy, Trade and Industry.

Chart 8

The global economy registered high growth at an average of 5 percent from 2004 toward 2007.



Note: Figures are calculated using GDP based on purchasing power parity (PPP) shares of the world total from the IMF.  
Source: IMF.

Chart 9

The pace of economic recovery in the United States and Europe after the bursting of the bubble has been moderate compared with that in the case of Japan.

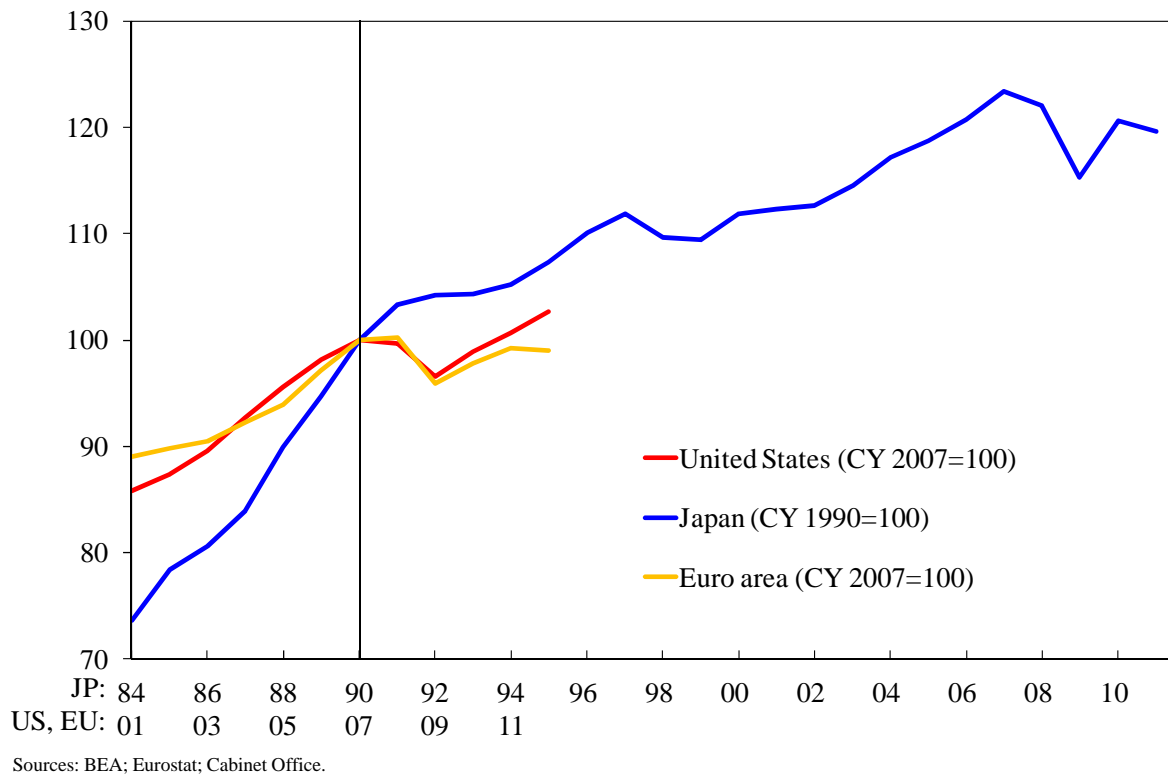
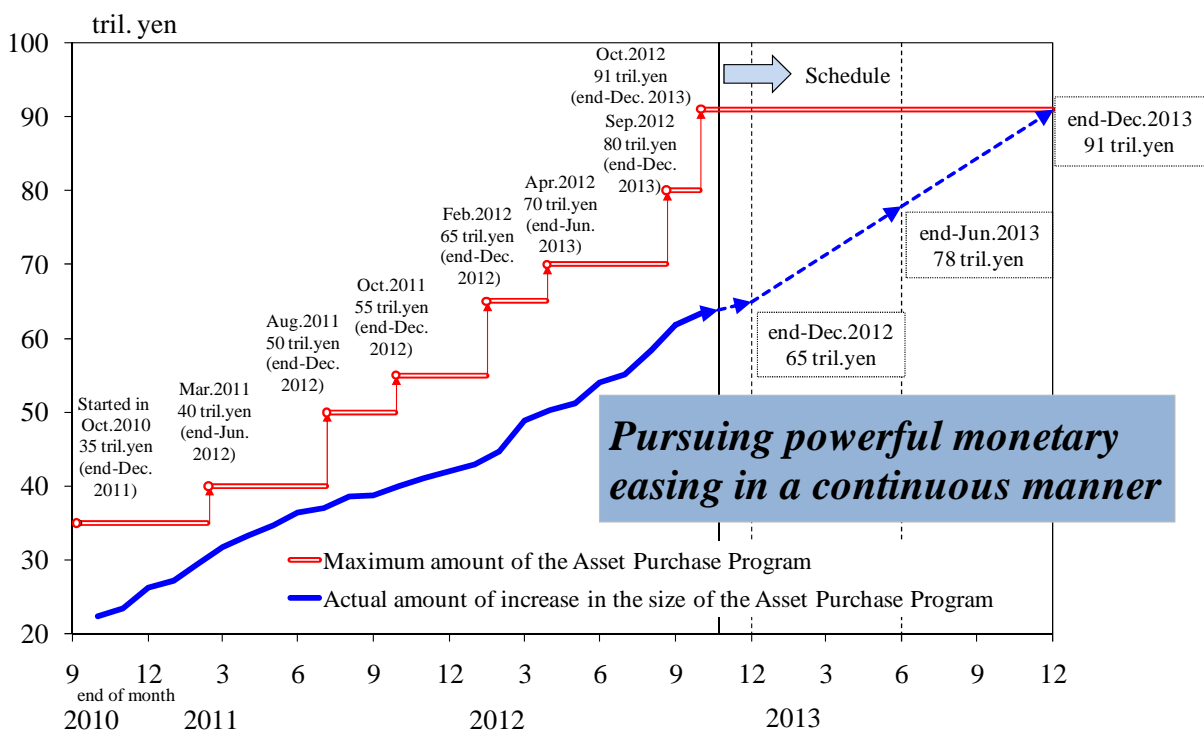


Chart 10

The Bank increased the size of the Asset Purchase Program by a total of about 21 trillion yen in September and October 2012.



Note: Dates in parentheses indicate the intended timescale for completing the increase.

## Establishment of "Stimulating Bank Lending Facility."

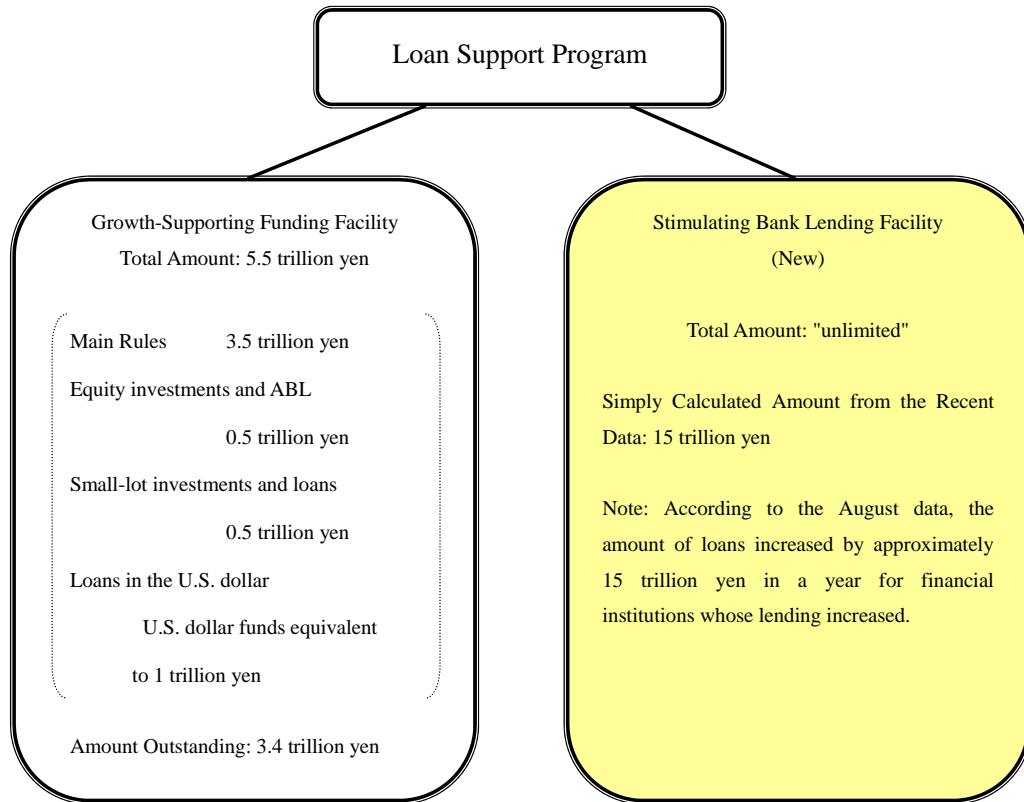
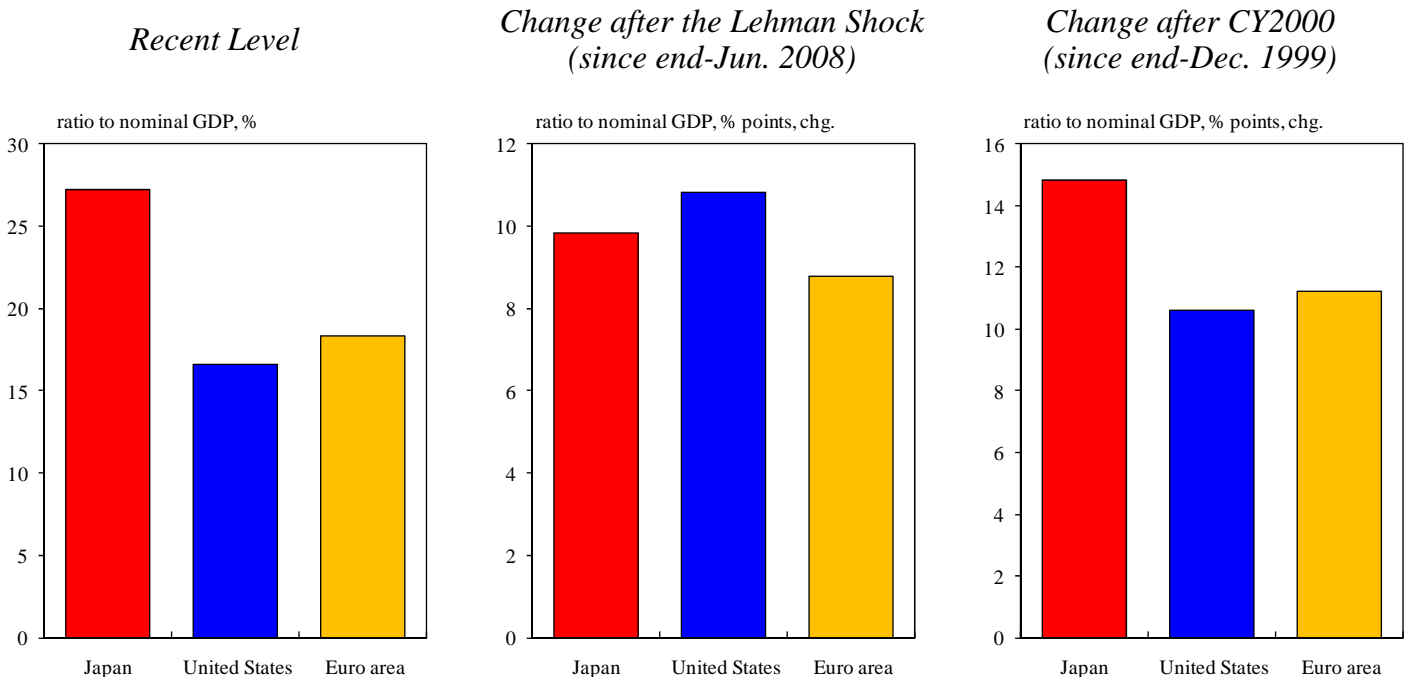


Chart 12

Looking at the monetary base, percentage point changes in its ratio relative to GDP since the Lehman shock have been more or less the same as in Europe and the United States, where the monetary base is thought to have been increased aggressively during this period.



Sources: Bank of Japan; Cabinet Office; FRB; BEA; ECB; Eurostat.

Chart 13

If firms and households actually take advantage of accommodative financial conditions, this would improve economic activity and lead to favorable price developments.

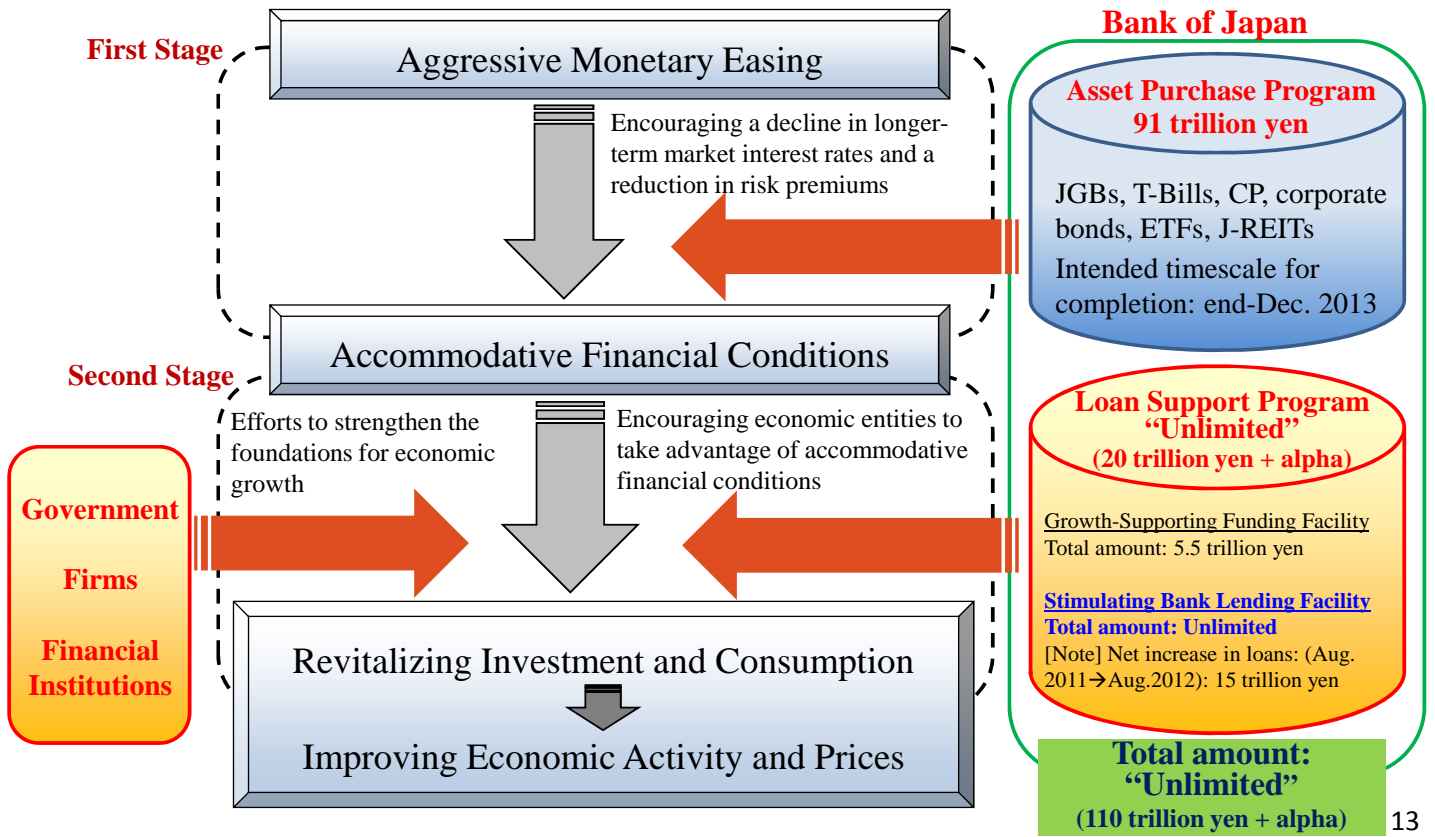
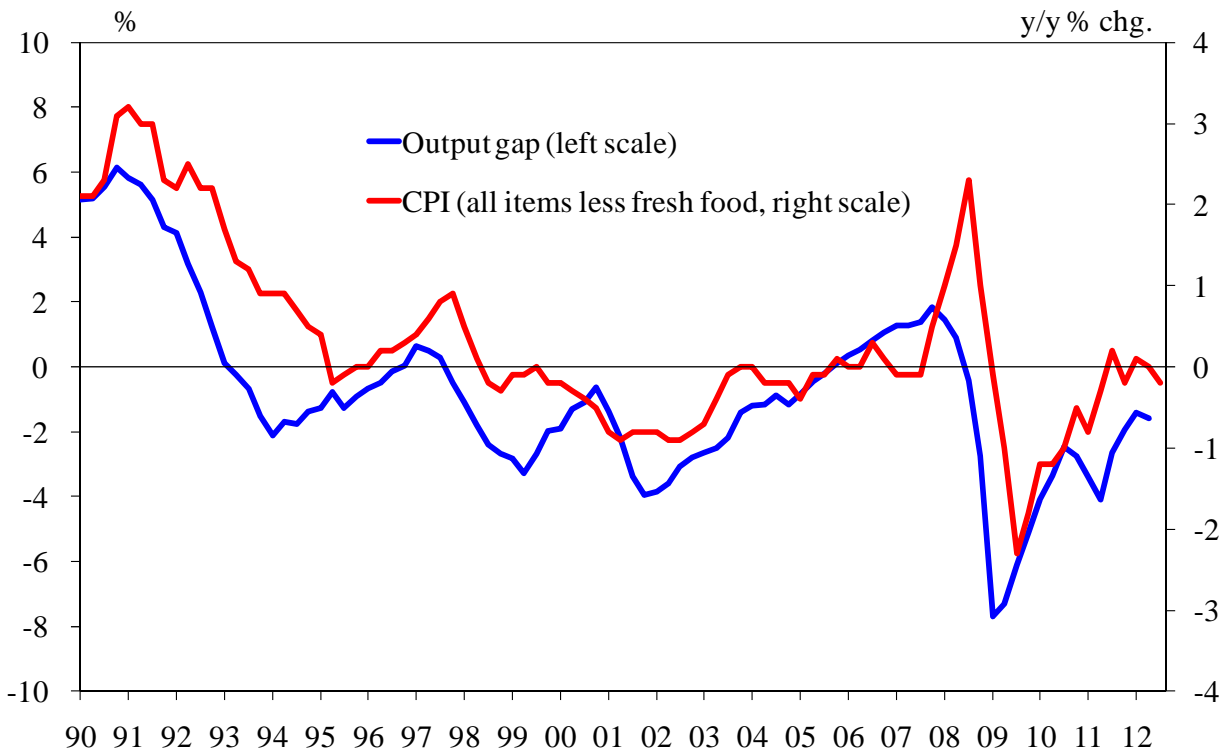


Chart 14

The rate of decline in the CPI has been slowing in reflection of the gradual shrinking of the output gap following its expansion after the Lehman shock.

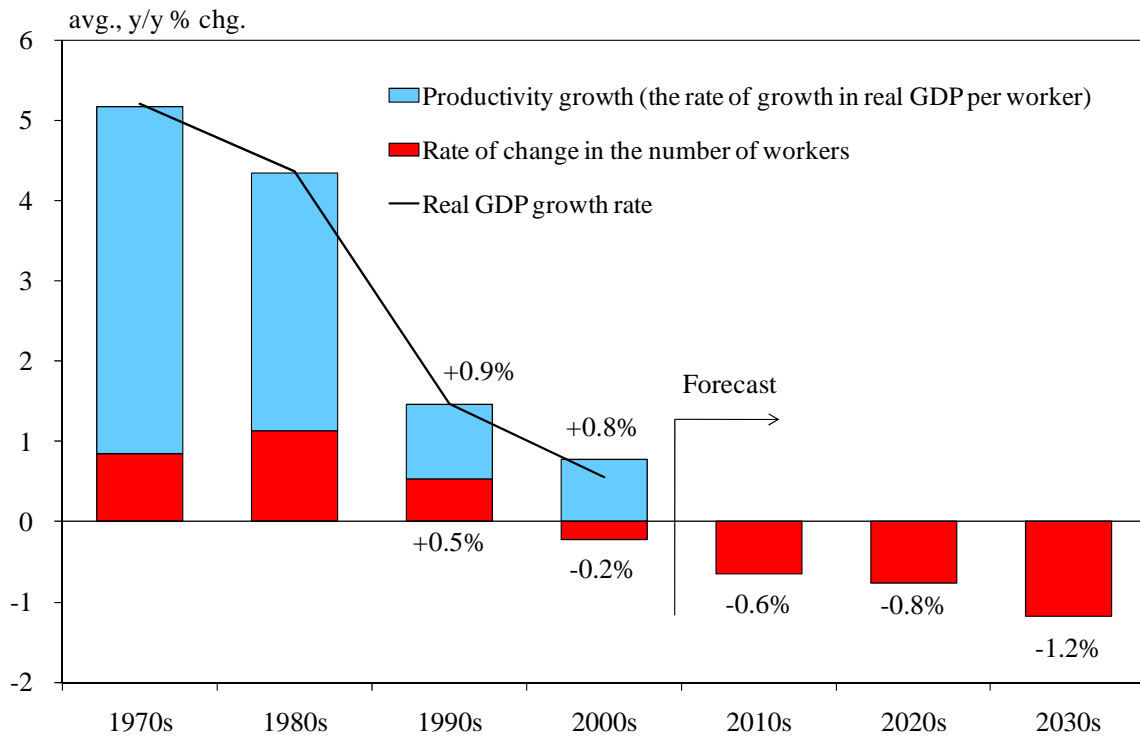


Note: The output gap is estimated by the Research and Statistics Department, Bank of Japan.  
Sources: Ministry of Internal Affairs and Communications; Bank of Japan; Cabinet Office, etc.



Chart 15

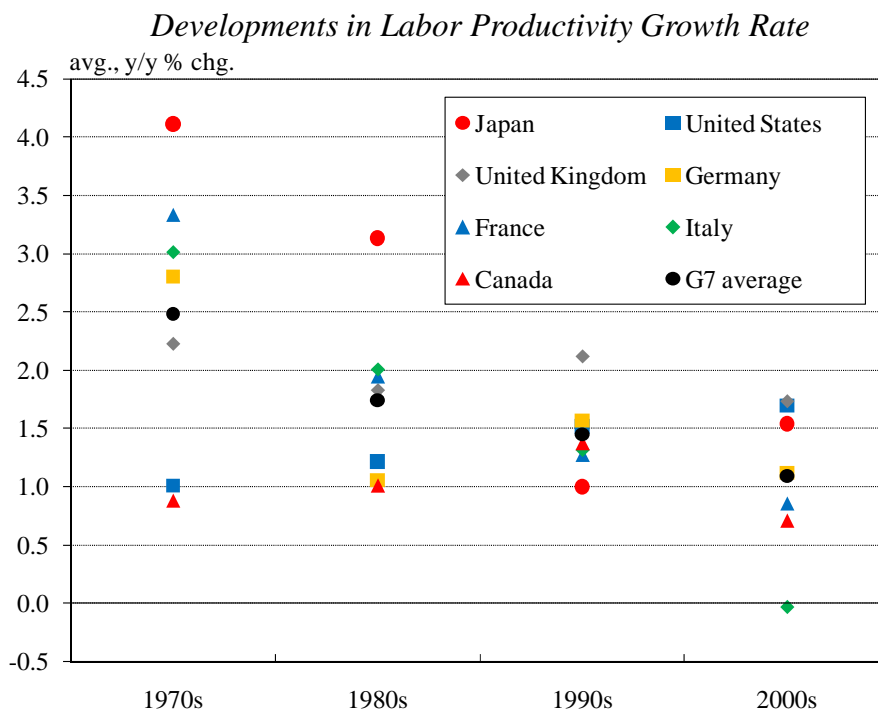
A decline in the number of workers causes Japan's trend growth rate to decline.



Note: The rates of change in the number of workers from fiscal 2011 onward are calculated using the projected future population (medium variant) and the projected labor force participation rates (assuming that the labor force participation rates in each age/sex group remain the same as those in 2010).  
Sources: Cabinet Office; Ministry of Internal Affairs and Communications; National Institute of Population and Social Security Research.

Chart 16

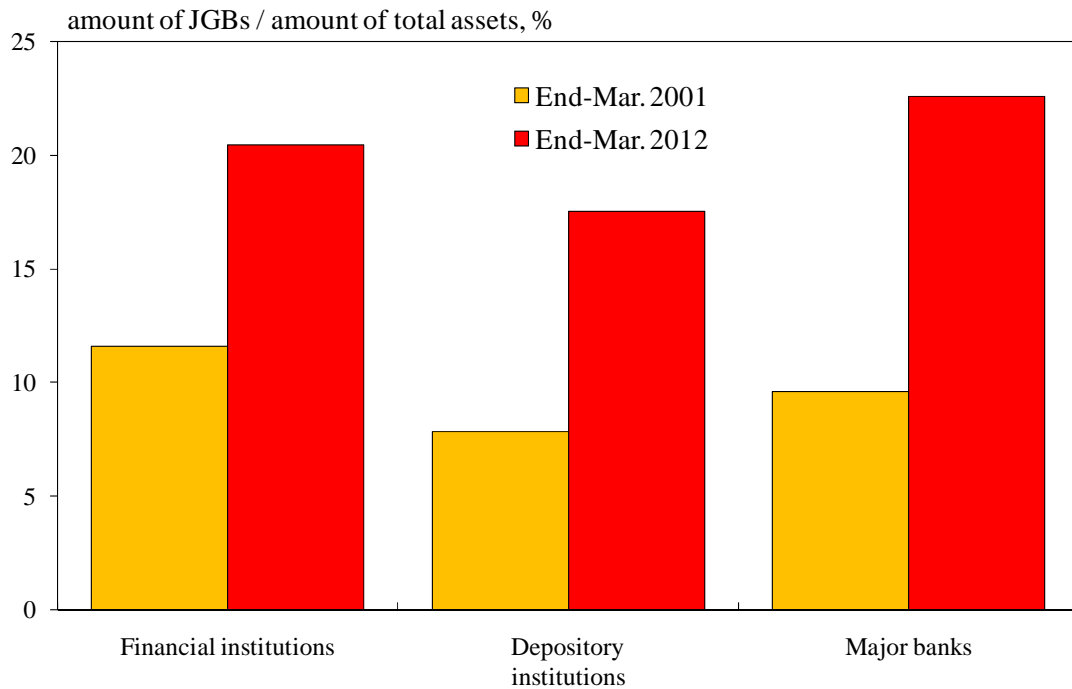
The average labor productivity growth rate in G-7 countries since the 1990s is 1.3 percent.



Notes: 1. Labor productivity = real GDP / number of workers  
2. To eliminate the effects of the financial crisis after the Lehman shock, figures for the 2000s are the averages for 2000 through 2008. Figures for the 1970s are the averages for 1971 through 1979.  
Sources: OECD; Cabinet Office; Ministry of Internal Affairs and Communications.

Chart 17

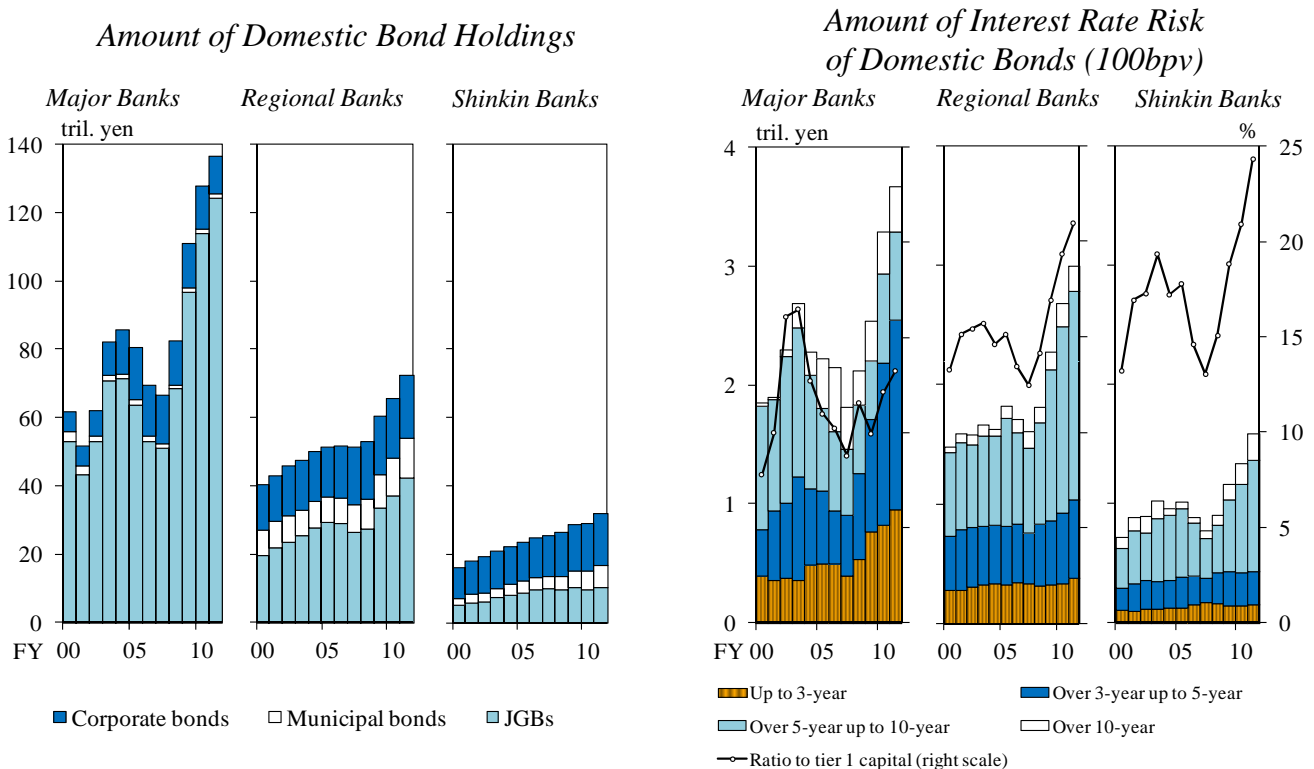
Japanese financial institutions have been increasing their amount of JGB holdings to around 20 percent as a share of total assets.



Note: 1. Financial Institutions include depository institutions, insurance and pension funds, nonbanks, and public financial institutions.  
 2. Major banks refer to 11 banks: Mizuho Bank, The Bank of Tokyo-Mitsubishi UFJ, Sumitomo Mitsui Banking Corporation, Resona Bank, Mizuho Corporate Bank, Saitama Resona Bank, Mitsubishi UFJ Trust and Banking Company, Mizuho Trust and Banking Company, Sumitomo Mitsui Trust Bank (The Chuo Mitsui Trust and Banking Company) and The Sumitomo Trust and Banking Company, Shinsei Bank, and Aozora Bank.  
 Source: Bank of Japan.

Chart 18

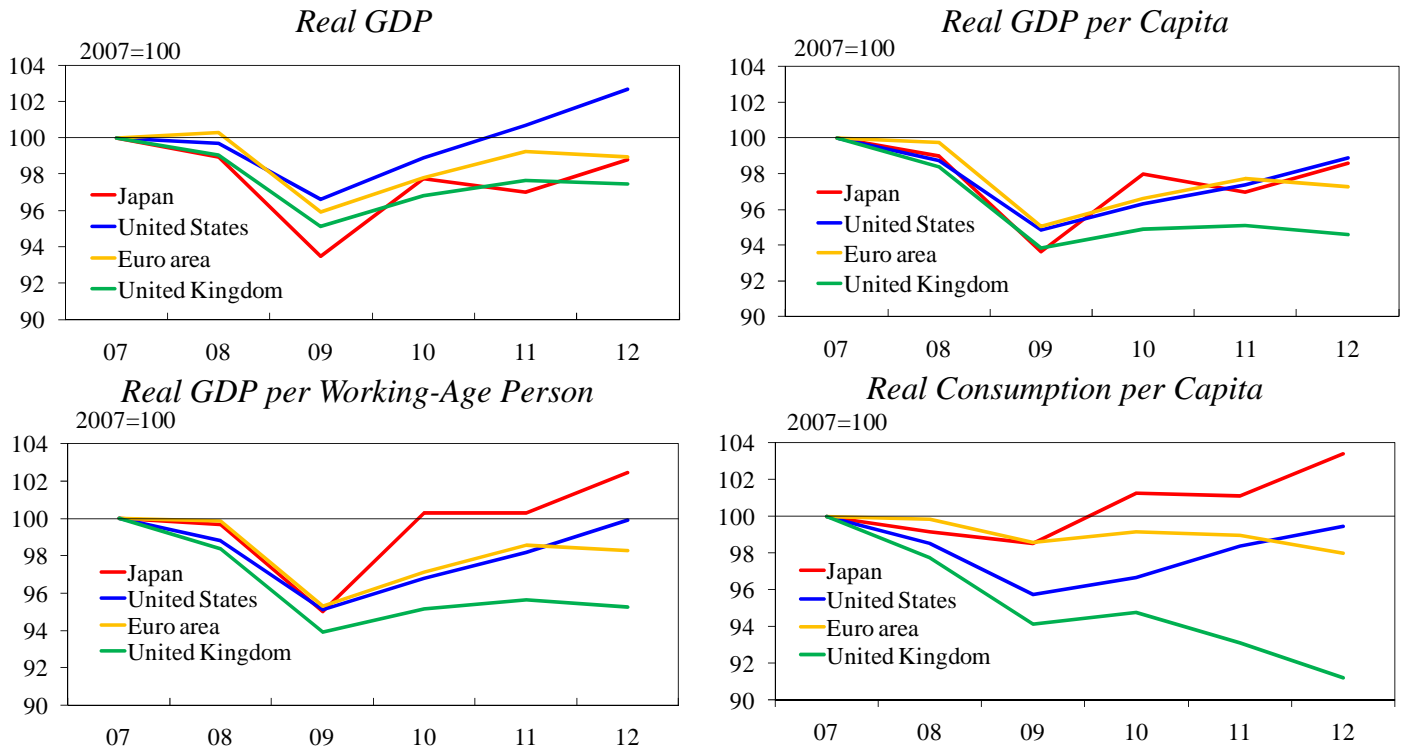
Financial institutions' interest rate risk stemming from an increase in JGB holdings is heightening.



Note: 100bpv refers to the amount of interest rate risk calculated under the assumption that interest rates of all maturities would rise simultaneously by 1 percentage point.  
 Source: Bank of Japan.

Chart 19

Japan's real GDP per working-age person and real consumption per capita have exceeded the levels for 2007.



Notes: 1. A working-age person refers to those between 15 and 64 years old.

2. Figures for real GDP, real GDP per capita, and real GDP per working-age person for 2012 are January- September averages. Figures for real consumption per capita for 2012 are January-June averages. Figures for the population and the working-age population for 2012 are calculated using the growth rate for 2011.

Sources: Cabinet Office; World Bank; BEA; Eurostat; ONS.