Macroprudential Policy and Initiatives by the Bank of Japan

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Outline

Introduction

- I. Issues Involved in Implementing Macroprudential Measures
- II. The Bank's Initiatives on the Macroprudential Front
- III. The Relation between Monetary Policy and Macroprudential Policy
- IV. The Bank's Recent Conduct of Monetary Policy

Types of Macroprudential Policy Measures

| Type of instrument | Examples |
|--|--|
| Limits calibrated to borrower risk characteristics | Loan-to-value caps, debt-to-income limits, limits on foreign currency lending |
| Absolute limits | Aggregate or sectoral credit growth ceilings, limits on exposure by instrument |
| Limits on leverage | Size-dependent leverage limits or asset risk weights |
| Limits on financial system concentration | Limits on interbank exposures |
| Capital | Time-varying capital requirements |
| Provisioning | Countercyclical/dynamic provisioning |
| Liquidity risk | Loan-to-deposit limits, core funding ratios, reserve requirements |
| Currency risk | Limits on open currency positions or on derivatives transactions |

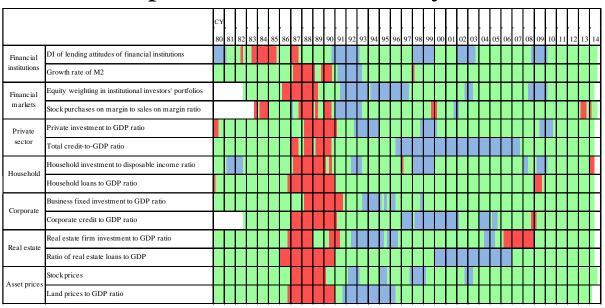
Sources: Bank for International Settlements (BIS); Bank of Japan.

Chart 2

Issues Involved in Implementing Macroprudential Measures

- (1) Implementation of effective measures with appropriate timing
- (2) Communication to the public at the time of policy implementation
- (3) Prevention of leakage of policy effects

Heat Map of Financial Activity Indexes



Heat map of Financial Activity Indexes

Red (darkest areas): overheating (a rise above the upper threshold)

Blue (second darkest areas): overcooling (a decline below the lower threshold)

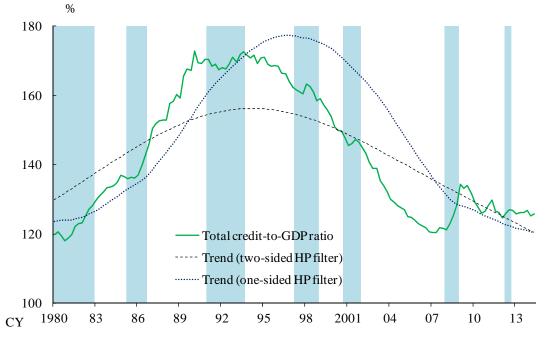
Green (most lightly shaded areas): everything in between

White: periods without data

Sources: Bloomberg; Ministry of Finance; Tokyo Stock Exchange; Cabinet Office; Japan Real Estate Institute; Bank of Japan.

Chart 4

Total Credit-to-GDP Ratio



Notes: 1. Shaded areas indicate economic recession periods.

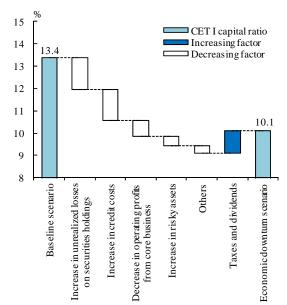
2. The two-sided HP filter is a method for extracting a trend from all available data using the Hodrick Prescott filter. The one-sided HP filter is a method for extracting a trend from the data available for a time period using the Hodrick Prescott filter.

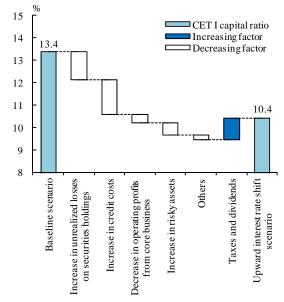
Sources: Cabinet Office; Bank of Japan.

Macro Stress Testing Results

Scenario of an economic downturn

Scenario in which a rise in interest rates causes an economic downturn





Note: Internationally active banks are counted. For details on the macro stress testing assumptions and estimation methods, see the October 2014 issue of the *Financial System Report* on pages 86-104.

Source: Bank of Japan.

Chart 6

Bank of Japan Act

Article 1

- (1) The purpose of the Bank of Japan, or the central bank of Japan, is to issue banknotes and to carry out currency and monetary control.
- (2) In addition to what is prescribed in the preceding paragraph, the Bank of Japan's purpose is to ensure smooth settlement of funds among banks and other financial institutions, thereby contributing to the maintenance of stability of the financial system.

Article 2

Currency and monetary control by the Bank of Japan shall be aimed at achieving price stability, thereby contributing to the sound development of the national economy.

Expansion of the Quantitative and Qualitative Monetary Easing (QQE)

- ➤ Accelerating the annual pace of increase in the monetary base from about 60-70 trillion yen to about 80 trillion yen.
- ➤ Increasing the annual pace of the Bank's JGB holdings from about 50 trillion yen to about 80 trillion yen.
- Extending the average remaining maturity of JGB purchases from about 7 years to about <u>7-10 years</u>.
- ➤ Increasing the Bank's holdings of ETFs and J-REITs so that the annual paces of increase are tripled to about <u>3 trillion yen</u> and about <u>90 billion yen</u>, respectively.