November 26, 2026

Bank of Japan

Economic Activity, Prices, and Monetary Policy in Japan

Speech at a Meeting with Local Leaders in Yamanashi

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(English translation based on the Japanese original)

I. Economic Activity and Prices

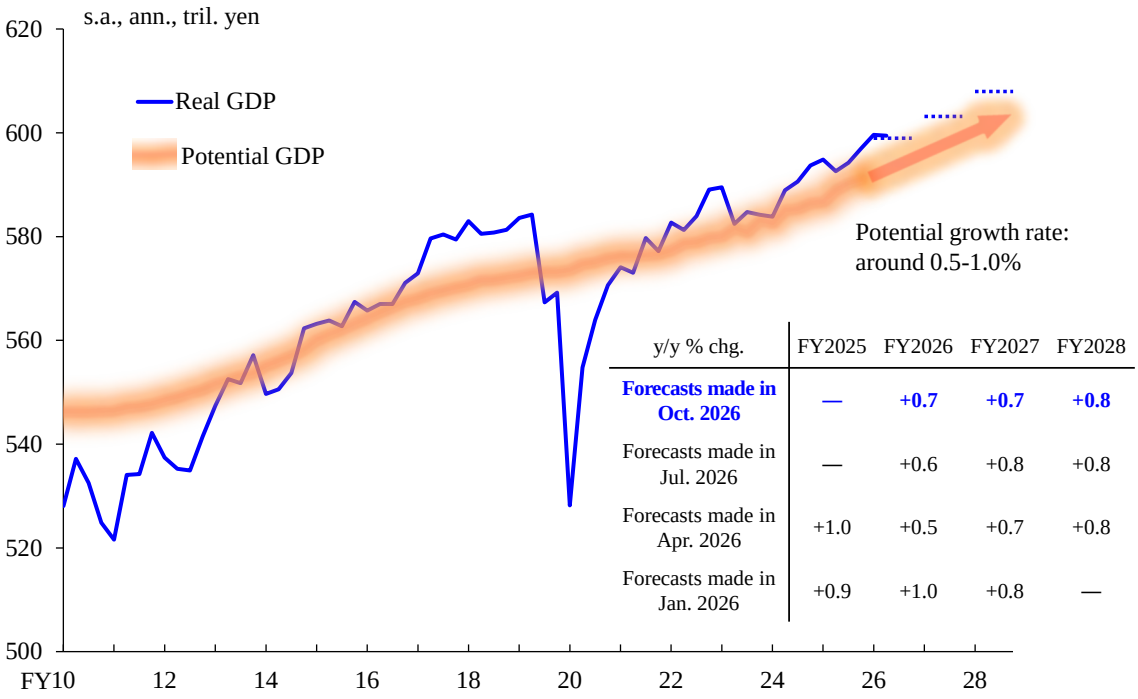
A. Current Situation and Outlook for Economic Activity in Japan

I will begin my speech by talking about developments in economic activity in Japan. The Bank of Japan assesses that the economy has recovered moderately recently, although some weakness has been seen in part, partly due to the impact of the situation in the Middle East. Japan's economy is expected to continue growing moderately, albeit at a decelerated rate. This is because, although the rise in energy and raw material prices since early spring 2026 reflecting the impact of the situation in the Middle East is expected to push down economic activity, the economy is likely to be underpinned by factors such as the government's various measures and accommodative financial conditions, in addition to an increase in global AI-related demand and an improvement in the employment and income situation. Japan's economic growth rate is likely to rise moderately thereafter, since it is projected that the adverse effects of high energy and raw material prices will wane and that a virtuous cycle from income to spending will gradually intensify. Against this backdrop, the latest economic outlook released in October 2026 projected that, through fiscal 2028, Japan's economic growth is likely to remain at a pace around the same level as the potential growth rate, as shown in Chart 1.

In particular, global AI-related demand is, to my surprise, pushing up Japan's economy in a wide range of industries. Initially, my view was that AI-related demand mainly benefited semiconductor-related industries, particularly in South Korea and Taiwan, because they had especially strong competitive advantages. In reality, however, AI-related demand has provided greater-than-expected benefits to Japan's economy because its impact has not only been observed among business fields involving semiconductors but has also spread widely to fields that may not seem directly linked to AI at first glance, such as data centers and supporting business fields, including equipment for generating and supplying power, air-conditioning, and construction.

In fact, at the October 2026 meeting of general managers of the Bank's branches, many branch managers from across the country reported that a wide range of industries within each region has been benefiting from AI-related demand. Moreover, as shown in Chart 2, the diffusion index (DI) for business conditions in the September *Tankan* (Short-Term Economic Survey

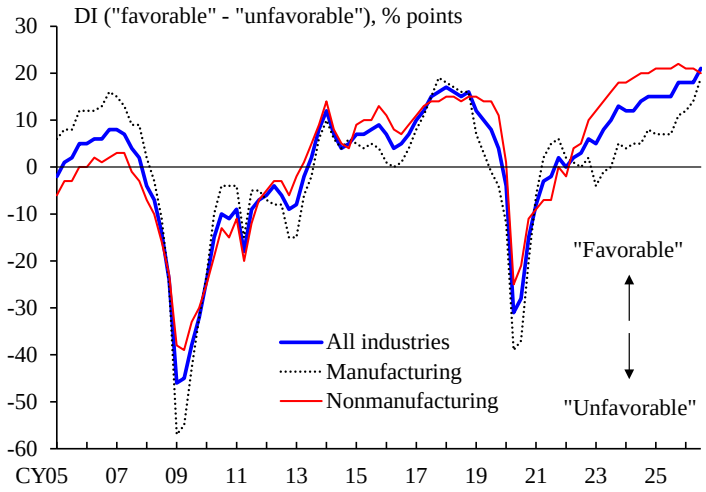
Chart 1: The Bank's Forecasts for Real GDP



y/y % chg.	FY2025	FY2026	FY2027	FY2028
Forecasts made in Oct. 2026	**—**	**+0.7**	**+0.7**	**+0.8**
Forecasts made in Jul. 2026	—	+0.6	+0.8	+0.8
Forecasts made in Apr. 2026	+1.0	+0.5	+0.7	+0.8
Forecasts made in Jan. 2026	+0.9	+1.0	+0.8	—

Note: The dotted lines show the medians of the Policy Board members' forecasts in the October 2026 Outlook Report. Real GDP values for 2026/Q3 onward are calculated by multiplying the actual figure for fiscal 2025 by all successive projected growth rates for each year.
Sources: Cabinet Office; Bank of Japan.

Chart 2: Business Conditions DI



	September 2025	December 2025	March 2026	June 2026	September 2026
All	15	18	18	18	21
Large mfg.	14	16	17	22	24
Small mfg.	1	7	7	9	14
Large nonmfg.	34	36	36	37	35
Small nonmfg.	14	17	16	15	15

Notes: 1. Figures are based on the *Tankan*.
2. In the left panel, figures are for all enterprises.
3. In the right panel, "all" refers to all industries and enterprises.
Source: Bank of Japan.

of Enterprises in Japan) has stayed at a favorable level. What draws attention is that business sentiment has been favorable not only in specific industries but also across a wide range of industries. In terms of firm size, while the June *Tankan* suggested that the benefits of AI-related demand were mainly enjoyed by large manufacturing enterprises, the September *Tankan* showed that these benefits were spreading even to small manufacturing enterprises. It would appear that Japan has a wealth of highly skilled "pick-and-shovel" firms and their suppliers.[1]

It is of course important to continue closely monitoring the impact of the situation in the Middle East, as well as developments in global AI-related demand and in foreign exchange rates, but I believe that Japan's economy will remain resilient.

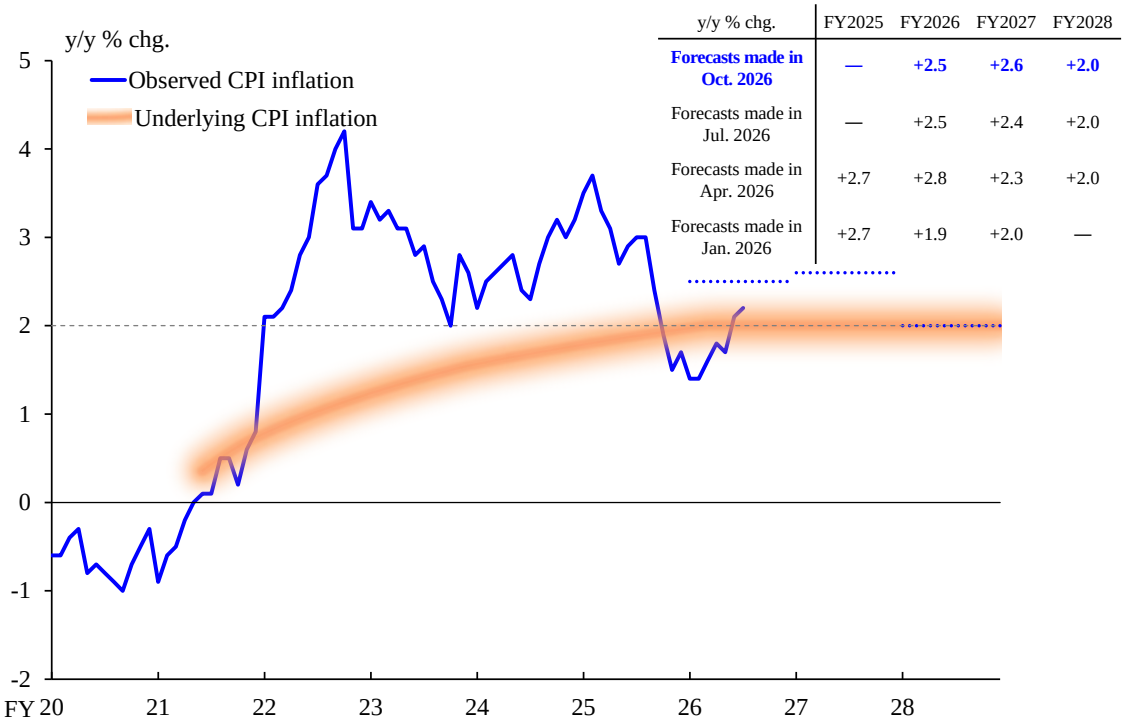
B. Current Situation and Outlook for Prices in Japan

Next, I would like to talk about prices in Japan. Despite factors such as the effects of the government's measures to reduce the household burden of higher energy prices, the year-on-year rate of increase in the consumer price index (CPI) for all items excluding fresh food has been rising moderately, being in the range of 2.0-2.5 percent recently, as shown in Chart 3, as the effects of a rise in import prices have been emerging, with moves to pass on wage increases to selling prices continuing. The Bank's baseline scenario is that the year-on-year rate of increase in the CPI for all items excluding fresh food is likely to accelerate to a level clearly above 2 percent. This is because, with moves to pass on wage increases to selling prices continuing, the rise in crude oil prices is expected to push up prices, mainly of energy and goods, and the rise in the prices of semiconductors and other items, reflecting the increase in global AI-related demand, and the depreciation of the yen thus far are likely to lead to an increase in prices, mainly of durable goods. Thereafter, with the waning of the effects of high crude oil prices, the rate of increase is expected to decline toward around 2 percent. Meanwhile, with a sense of labor shortage continuing to be strong, the mechanism in which wages and prices rise moderately in interaction with each other has been operating, and

[1] In this context, firms that do not directly engage in a new booming business area but instead provide essential tools, equipment, and infrastructure necessary for such a business and its development are referred to as "pick-and-shovel" firms. The term traces back to the California Gold Rush in the mid-19th century, where suppliers of tools, such as pickaxes, profited more consistently than the gold miners themselves.

medium- to long-term inflation expectations are at around 2 percent. In this situation, the Bank's view is that underlying CPI inflation is at a level that is generally consistent with the price stability target of 2 percent, and is expected to remain at around that level.[2]

Chart 3: The Bank's Forecasts for the CPI



y/y % chg.	FY2025	FY2026	FY2027	FY2028
Forecasts made in Oct. 2026	**—**	**+2.5**	**+2.6**	**+2.0**
Forecasts made in Jul. 2026	—	+2.5	+2.4	+2.0
Forecasts made in Apr. 2026	+2.7	+2.8	+2.3	+2.0
Forecasts made in Jan. 2026	+2.7	+1.9	+2.0	—

Notes: 1. Figures for observed CPI inflation are the CPI for all items less fresh food.
2. The dotted lines show the medians of the Policy Board members' forecasts in the October 2026 Outlook Report.
Sources: Ministry of Internal Affairs and Communications; Bank of Japan.

[2] The Bank defines its "price stability target" as "a state where various economic agents including households and firms may make decisions regarding such economic activities as consumption and investments without being concerned about the fluctuations in the general price level." The decision to set the target at 2 percent was made based on three perspectives: (1) the measurement upward bias in the price index; (2) the safety margin that acts as a buffer against the risk of a vicious cycle of declining prices and deteriorating economic activity; and (3) the general public's perception of price developments under which households and firms perceive price stability. On this basis, it was judged appropriate to clearly indicate the target of 2 percent in order to avoid excessive rise and fall of inflation expectations (the anchoring effect), thereby anchoring the sustainable rate of inflation. As I have noted on past occasions, with private housing rent and imputed rent affected by such housing rent generating downward bias, I believe that Japan's CPI has a certain level of downward bias, given the weight of these rents in the CPI. Regarding services prices in the CPI, my view is that, as quality adjustments are difficult, changes in the quality of services may not be sufficiently incorporated, especially during an inflationary phase. Considering these factors, actual inflation may have already exceeded 2 percent, and I therefore believe that it is necessary to pay even more attention to ensuring that the price stability target is achieved.

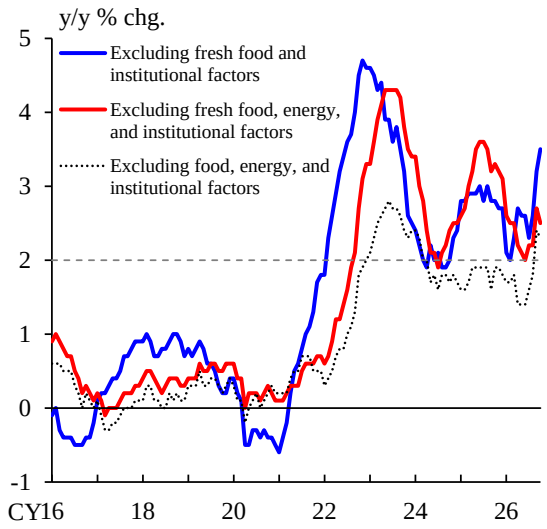
I have so far presented the official view of the Bank. Currently, there is not much of a difference between my own view and the official view of the Bank. Since April 2026, I have believed that underlying CPI inflation has generally reached 2 percent, and the Bank now provides the same assessment. Moreover, the Bank has expressed concern about the risk that underlying CPI inflation will deviate upward to a level above 2 percent, considering various factors that could drive up prices, such as the impact of the situation in the Middle East, the expansion in AI-related demand, and developments in foreign exchange rates; I also share the same view on this matter. In what follows, I would like to elaborate further on these points.

C. Underlying CPI Inflation

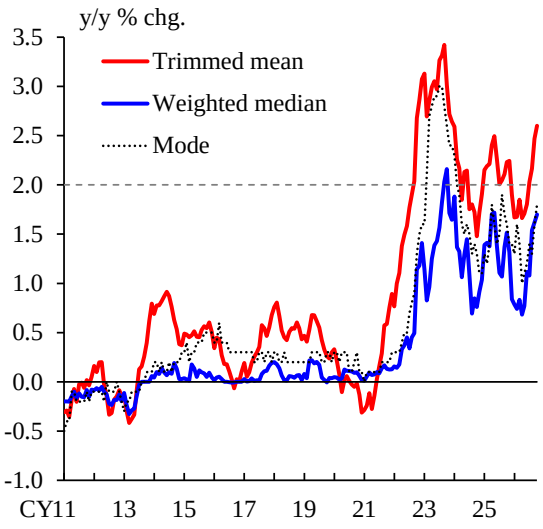
First, let me elaborate on the Bank's assessment that underlying CPI inflation is at a level that is generally consistent with the price stability target of 2 percent. As for price developments on the surface, although the year-on-year rate of increase in the CPI for all items excluding fresh food temporarily declined to a level below 2 percent, this reflects the effects of factors such as the government's measures to reduce the household burden of higher energy prices and policies concerning the provision of free education. Excluding these institutional factors, the rate of increase has been above 2 percent, having risen to around 3.5 percent recently, as shown in Chart 4. Moreover, the rate of increase in the trimmed mean of the year-on-year rate of change in the CPI has recently risen to around 2.5 percent, reflecting price rises for a wide range of goods related to daily necessities and higher prices of food items. The rates of increase in the weighted median and the mode have both recently risen to the range of 1.5-2.0 percent. Meanwhile, looking at the relationship between wages and services prices, with progress in the pass-through of wage increases to services prices of a wide range of items, both wages and services prices have been on a moderate increasing trend, as shown in Chart 5. Medium- to long-term inflation expectations of firms, households, and market participants, which represent their perceptions of price developments, have increased moderately on the whole and are at around 2 percent. The break-even inflation (BEI) rate, derived from inflation-indexed government bonds, has been at around 2 percent, albeit with some fluctuations. I believe that, when considering future price developments, the focus should be placed on the inflation expectations of firms and households, who are the actual drivers of economic activity. I will carefully monitor whether these indicators, which have reached

Chart 4: Underlying Inflation (1)

CPI Excluding Institutional Factors



CPI: Trimmed Mean etc.

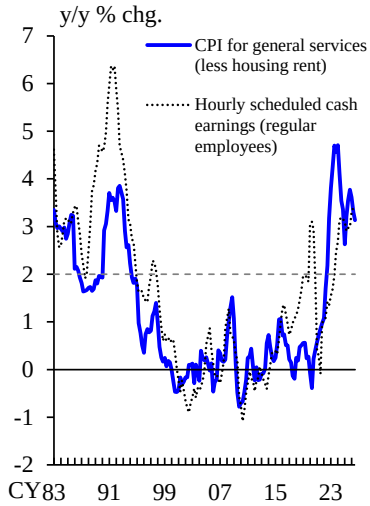


Notes: 1. In the left panel, institutional factors include the effects of the consumption tax rate change, policies concerning the provision of free education (including the free school lunches starting in April 2026), measures to reduce the energy cost burden (such as gasoline prices, electricity charges, and gas charges), the reduction in mobile phone charges in 2021, and travel subsidy programs. Figures are Bank staff estimates.
2. Figures in the right panel are based on Bank staff calculations using the CPI. The CPI figures are Bank staff estimates and exclude institutional factors.

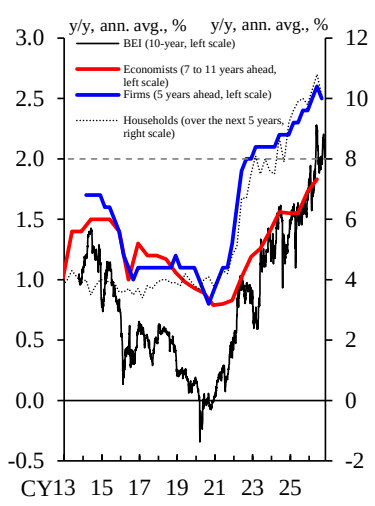
Sources: Bank of Japan; etc.

Chart 5: Underlying Inflation (2)

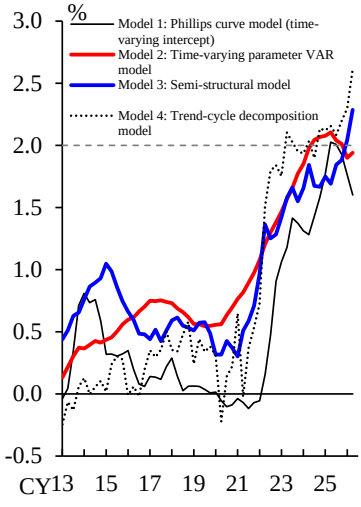
Wages and Prices



Inflation Expectations



Trend Inflation



Notes: 1. In the left panel, figures for the CPI for general services (less housing rent) are Bank staff estimates and exclude institutional factors. Figures for hourly scheduled cash earnings (regular employees) are seasonally adjusted (3-quarter central moving averages); figures from 2016/Q1 onward are based on continuing observations following the sample revisions, and the figure for 2026/Q3 is the July-August average.
2. In the middle panel, figures for economists show the forecasts of forecasters surveyed for the *ESP Forecast*. Figures for households are averages of numerical values for expected inflation rates provided by respondents of the *Opinion Survey on the General Public's Views and Behavior*, and are calculated by excluding 0.5 percent of the highest and lowest figures, respectively, in order to avoid extremes. Figures for firms show the inflation outlook of enterprises for general prices (all industries and enterprises, average) in the *Tankan*.
3. Figures in the right panel are Bank staff estimates. For details, see Bank of Japan, Monetary Affairs Department, "The Concept and Measurement of Underlying Inflation," *Bank of Japan Review Series*, no. 26-E-5 (March 2026).

Sources: Bloomberg; Cabinet Office; Consensus Economics Inc., *Consensus Forecasts*; Google Trends; JCER, *ESP Forecast*; Ministry of Health, Labour and Welfare; Ministry of Internal Affairs and Communications; QUICK, *QUICK Monthly Market Survey <Bonds>*; Bank of Japan.

approximately 2 percent, will rise further. Regarding trend inflation estimated from economic models, all of the models have shown a moderate uptrend, with estimates at around 2 percent.

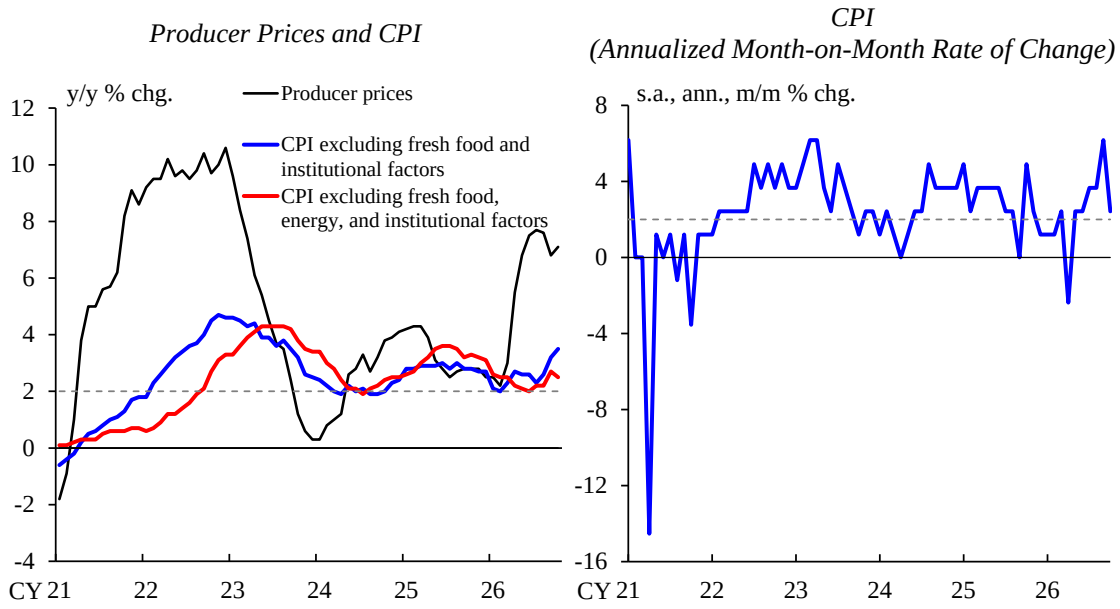
Based on the developments in various indicators I have just outlined, the Bank judges that underlying CPI inflation is at a level that is generally consistent with the price stability target of 2 percent.

D. Upside Risks to Underlying CPI Inflation

Looking ahead, it is necessary to monitor whether underlying CPI inflation will deviate upward to a level above 2 percent. In what follows, I will explain why I take this view.

Let me start with recent price developments. As shown in Chart 6, the rate of increase in the producer price index (PPI) has continued to be high, with the rate for October registering 7.1 percent on a year-on-year basis. This is due to high crude oil prices reflecting the situation in the Middle East, the depreciation of the yen, and the expansion in AI-related demand. As for the breakdown of the PPI, when import prices first rose due to the situation in the Middle

Chart 6: Corporate Goods Prices and Consumer Prices



Notes: 1. In the left panel, institutional factors include the effects of the consumption tax rate change, policies concerning the provision of free education (including the free school lunches starting in April 2026), measures to reduce the energy cost burden (such as gasoline prices, electricity charges, and gas charges), the reduction in mobile phone charges in 2021, and travel subsidy programs. Figures are Bank staff estimates.
2. Figures in the right panel are the CPI for all items less fresh food and energy.
Sources: Ministry of Internal Affairs and Communications; Bank of Japan; etc.

East, price hikes were observed primarily at the upstream stage in the supply chain, such as for petroleum and coal products; the price pass-through of these hikes recently appears to have been spreading to the midstream and downstream stages, for chemicals and related products, plastic products, and beverages and food, among other items.

This cost pass-through has also begun to feed through to consumer prices. The month-on-month rate of increase in the CPI for all items excluding fresh food and energy -- an indicator I watch closely as providing a snapshot of recent CPI developments -- has been accelerating, compared with the rate until early spring. Moreover, developments in the year-on-year rate of increase in the CPI by item for October show that the rate of increase for "domestic non-durable goods," which includes petroleum-derived plastic bags and food wrap, was 12.0 percent, while the rate of increase for "recreational durable goods," which includes laptops and tablet computers (equipped with semiconductors), was 8.2 percent. Both sets of goods have seen high rates of increase recently, which I see as indicating that the effects of high crude oil prices stemming from the situation in the Middle East and of AI-related demand, are becoming evident in consumer prices as well. Survey results indicate that price hikes are scheduled for food and other items in response to the surge in the prices of packaging materials such as food trays, and I see that price hikes resulting from the effects of the situation in the Middle East will become more pronounced at the consumer level.

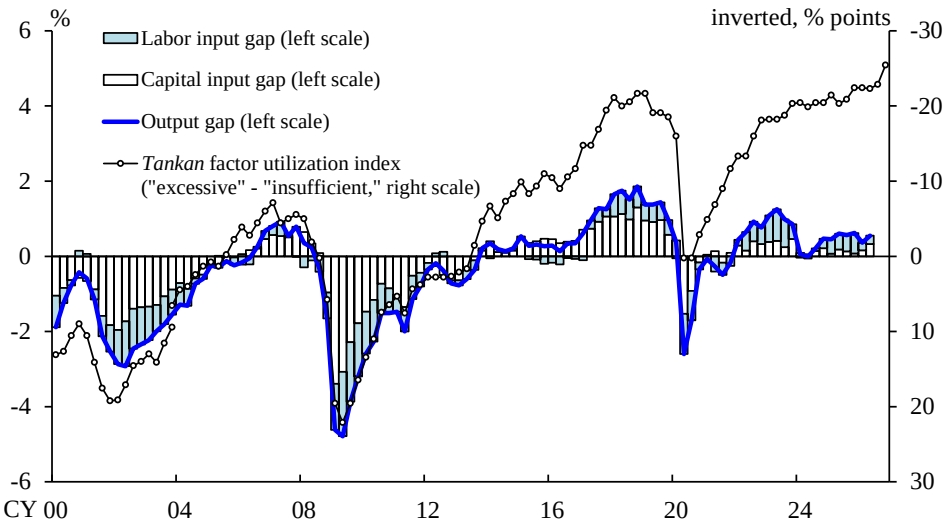
While such developments are factored into the Bank's baseline scenario of the outlook for prices to some extent, recent price developments suggest further upside risks. Moreover, the possibility of further price rises cannot be ruled out, given that the situation in the Middle East remains unclear, AI-related demand continues to be strong, and foreign exchange rate developments could exert additional upward pressure on prices, depending on how they play out. There are views that, if the social implementation of AI progresses, the productivity of the economy as a whole will rise, thereby pushing down prices in the medium to long term. However, I believe that AI will, at least in the short term, exert upward pressure on prices through a tightening of the supply and demand conditions of related goods and services, although it is necessary to closely monitor developments in the AI industry for the time being. Considering this situation, due attention is warranted on whether underlying CPI inflation will deviate upward to a level above 2 percent.

Furthermore, I am concerned that Japan's economy today has established, or has "laid the groundwork for," an environment in which prices are prone to rise.

First, regarding developments in the output gap, the Bank's estimates, as shown in Chart 7, have generally remained positive since 2022, indicating short supply and excess demand, although estimates need to be viewed with latitude, as they may differ depending on the estimation methods and are subject to estimation errors. This shows that prices have been under upward pressure, as demand has outstripped potential supply capacity in the overall economy. In this regard, as shown in Chart 8, the employment conditions DI in the *Tankan*, which indicates firms' perceptions of labor shortage, suggests that firms' sense of labor shortage has continued to be strong. Under these circumstances, firms in some industries may be unable to operate production facilities as they wish to, leading to a decline in capacity utilization rates. If capacity utilization rates decline, the estimated output gap is theoretically subject to a downward bias. In reality, however, lower capacity utilization rates do not necessarily indicate excess supply capacity, and the extent of short supply and excess demand could be greater than suggested by the figures of the output gap. In a situation where the working-age population is expected to decrease further, this state of labor shortage is likely to become more severe, leading to a greater decline in supply capacity. In other words, such labor shortage is projected to exert further upward pressure on prices.

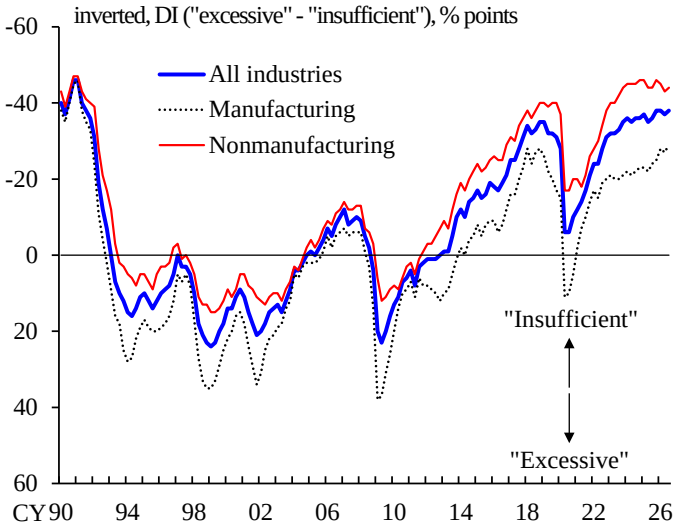
Second, firms' price-setting behavior has become more active. Chart 9 shows the ratio obtained by dividing the proportion of firms responding in the *Tankan* that output prices would rise, by the proportion of firms responding that input prices would rise -- a rough indicator of firms' willingness to pass on costs to prices. From 2022, this indicator rose and has since remained at a high level last seen during the bubble period. As such, with firms' price-setting behavior becoming more active, price shocks, or price rises, including higher import and input prices, are likely to be passed on more easily to producer and consumer prices. In fact, many firms have said that they will continue to pass on increases in shipping and packaging costs, which reflect recent high crude oil prices.

Chart 7: Output Gap



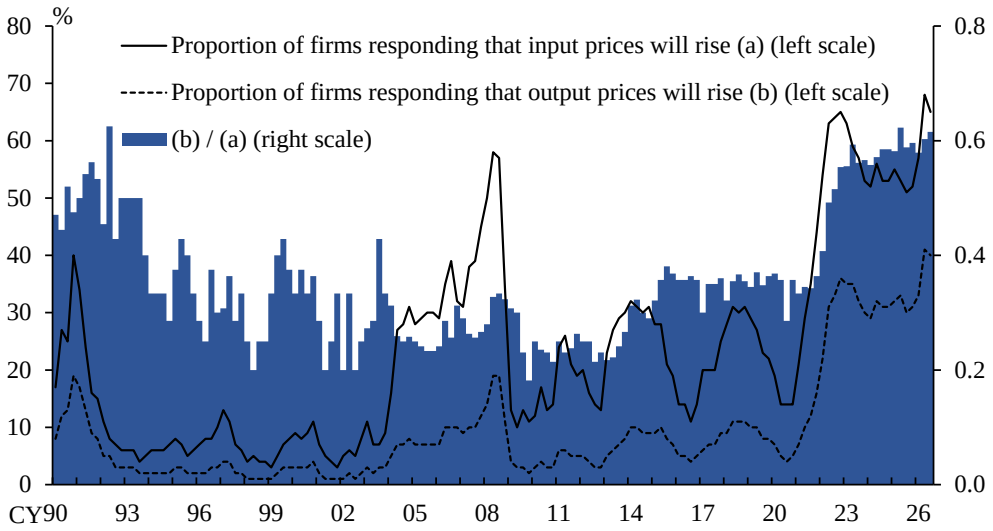
Notes: 1. Figures for the output gap are Bank staff estimates.
2. The *Tankan* factor utilization index is calculated as the weighted average of the production capacity DI and the employment conditions DI for all industries and enterprises. Capital and labor shares are used as weights. There is a discontinuity in the data for December 2003 due to a change in the survey framework.
Source: Bank of Japan.

Chart 8: Employment Conditions DI



Note: Figures are based on the *Tankan*, and are for all enterprises. There is a discontinuity in the data for December 2003 due to a change in the survey framework.
Source: Bank of Japan.

Chart 9: Changes in Firms' Price-Setting Behavior



Note: Figures are based on the *Tankan*, and are for all industries and enterprises. There is a discontinuity in the data for December 2003 due to a change in the survey framework.
Source: Bank of Japan.

The third factor that makes prices prone to rise is developments in medium- to long-term inflation expectations. As I mentioned in referring to Chart 5 earlier, medium- to long-term inflation expectations of firms, households, and market participants are at around 2 percent on the whole. Unlike the United States and Europe, where inflation expectations have been stable at around 2 percent, Japan has seen inflation expectations rise from a low level. It is thus necessary to pay attention to whether inflation expectations rise further as the observed CPI inflation rate continues to be above 2 percent -- in other words, whether firms and households change their behavior based on the premise of a higher inflation rate.

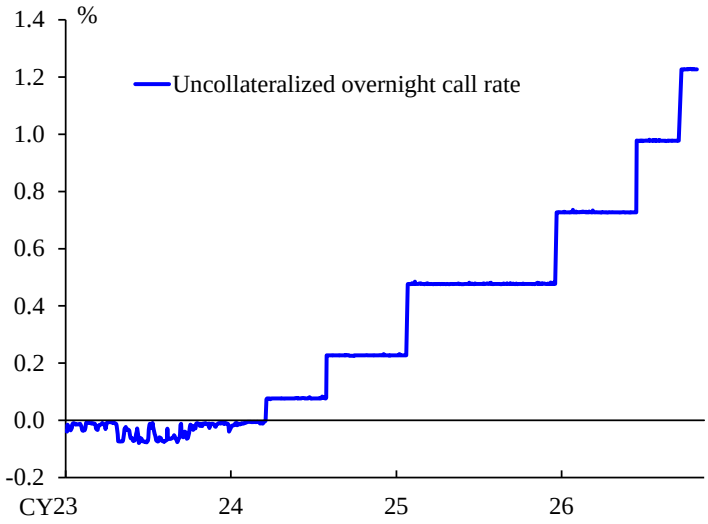
As I have explained, upside risks to prices have already been observed in Japan's economy, and in the event of future shocks that lead to further price rises, economic conditions are susceptible to additional upward deviations in prices. It is therefore necessary to carefully monitor developments in underlying CPI inflation to ensure that it does not deviate upward to a level above 2 percent.

II. Conduct of Monetary Policy

A. Assessment of the Degree to Which Underlying CPI Inflation Is Anchored

I would now like to turn to the Bank's conduct of monetary policy. The Bank conducts monetary policy with the aim of achieving the price stability target of 2 percent in a sustainable and stable manner. Since the changes in the monetary policy framework decided at the March 2024 Monetary Policy Meeting (MPM), the Bank has returned to conventional monetary policy, employing the guidance of the short-term interest rate as a primary policy tool. As shown in Chart 10, after setting the target level of its short-term policy interest rate at around 0 to 0.1 percent at the March 2024 MPM, the Bank has gradually raised the target level in response to an increase in the likelihood of achieving the price stability target and to upside risks to prices; the Bank set it at around 1.25 percent at the September 2026 MPM.

Chart 10: Normalization of Monetary Policy

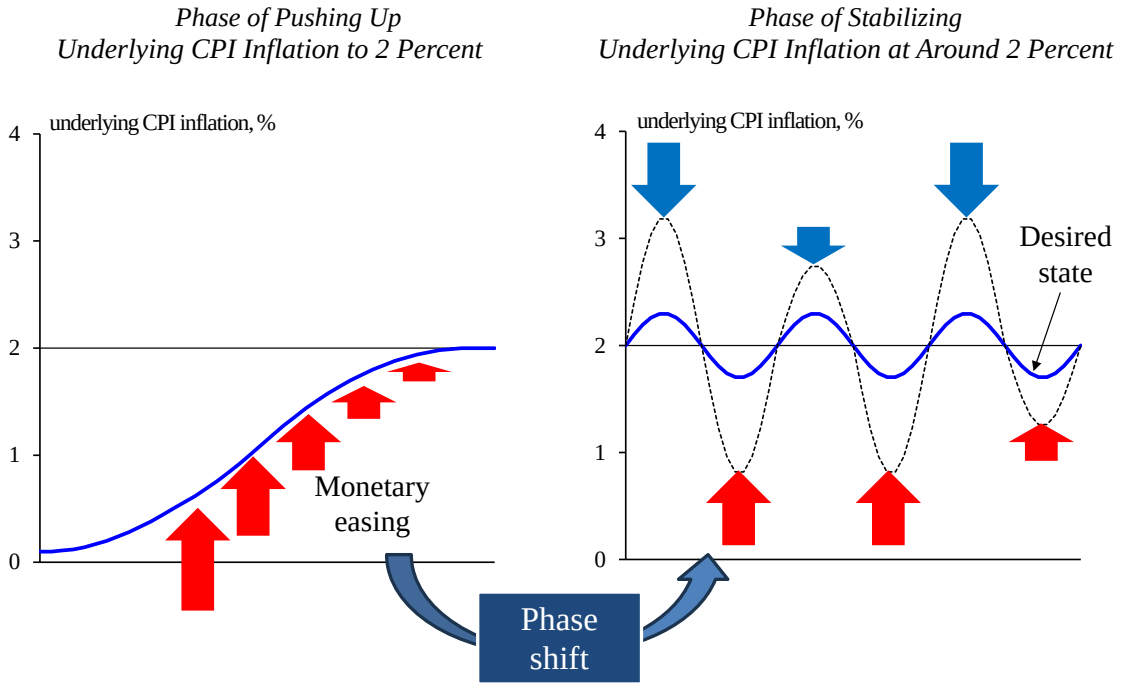


Source: Bank of Japan.

As I mentioned earlier, my view, along with the view of the Bank's Policy Board, is that underlying CPI inflation has generally reached the 2 percent price stability target. I therefore believe that, as shown in Chart 11, the focus of monetary policy has shifted from raising underlying CPI inflation to 2 percent to avoiding further upward deviation and stabilizing it at around 2 percent.

While some take the view that underlying CPI inflation has yet to anchor at around 2 percent, my view differs slightly in nuance. What I mean is that it is only natural for underlying CPI inflation to rise or fall due to the impact of prevailing financial and economic conditions, exogenous shocks, and other factors. I therefore do not think it is something that will "anchor" exactly at 2 percent. Rather, I believe it is the Bank's role to conduct monetary policy appropriately so that underlying CPI inflation remains at a level broadly around 2 percent while keeping fluctuations as small as possible. It can be said that underlying CPI inflation will never anchor permanently at the price stability target: the Bank must continue indefinitely to strive to keep it stable at around 2 percent.

Chart 11: Phase Shift in Monetary Policy



Although underlying CPI inflation will never anchor at exactly 2 percent, the degree to which it is anchored -- or, what could be referred to as the "degree of anchoring" -- still appears to be lower in Japan, where underlying CPI inflation has risen from negative or zero levels, than in the United States and Europe.[3] For example, as I mentioned earlier, it is probably the case that medium- to long-term inflation expectations in Japan are less firmly anchored than those in the United States and Europe, where they have been anchored at a level around 2 percent

[3] For details, see Box 5 of the October 2026 *Outlook for Economic Activity and Prices* (Outlook Report).

for many years. Underlying CPI inflation in Japan is likely to become more firmly anchored, as the Bank conducts monetary policy appropriately and achieves stable inflation of around 2 percent for a prolonged period. Until then, however, the weaker anchoring raises concerns that underlying CPI inflation in Japan could fluctuate substantially if, for example, an exogenous shock occurs. In my view, the Bank therefore needs to respond to such shocks more swiftly and strongly than would be necessary if underlying CPI inflation were anchored more firmly.

B. Neutral Financial Conditions

With underlying CPI inflation having reached a level that is consistent with the price stability target of 2 percent, it is also necessary to bring the policy interest rate closer to the neutral interest rate -- a neutral level that neither heats nor cools economic activity -- as quickly as possible.[4] Otherwise, accommodative financial conditions would push up underlying CPI inflation to a level above 2 percent. The difficulty here is that it is not possible to determine the neutral interest rate *a priori*. In my view, it can only be determined in retrospect, through adjustments to the policy interest rate and careful monitoring of their effects on financial conditions. Another difficult issue is that the neutral interest rate itself can change as financial and economic conditions and the broader social environment evolve.

The question then arises as to how to assess financial conditions. In a nutshell, they cannot be assessed by looking at any single indicator. Specifically, to assess the degree of monetary accommodation or tightening, the Bank needs to examine (1) interest rate developments and (2) funding conditions, as shown in Chart 12.[5] Based on recent developments in these two, my view is that financial conditions remain accommodative and that the policy interest rate is still some way from the neutral level.

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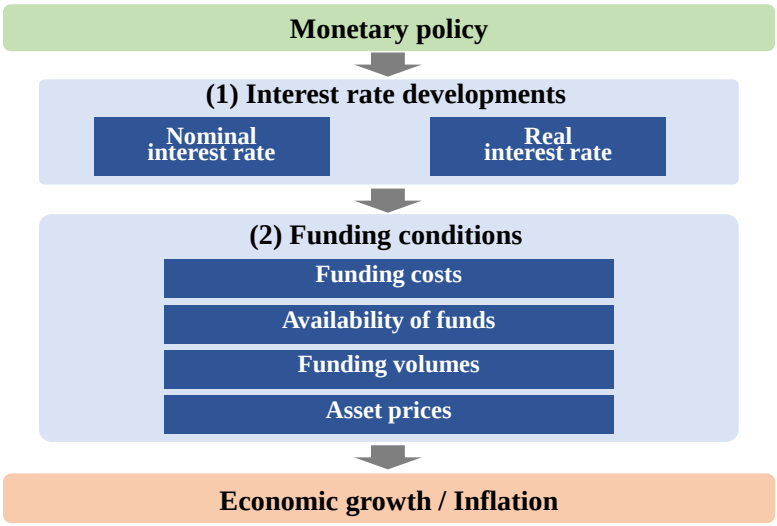
[4] The neutral interest rate is the sum of the natural rate of interest, which is the real interest rate level that is neutral to economic activity and prices, and the expected rate of inflation. The natural rate of interest is defined as the level of the real interest rate that is neutral to economic activity and prices in the sense that it is neither accommodative nor restrictive. Central banks influence real interest rates by controlling nominal interest rates, thereby heating or cooling economic activity.

[5] For details, see Box 6 of the October 2026 Outlook Report.

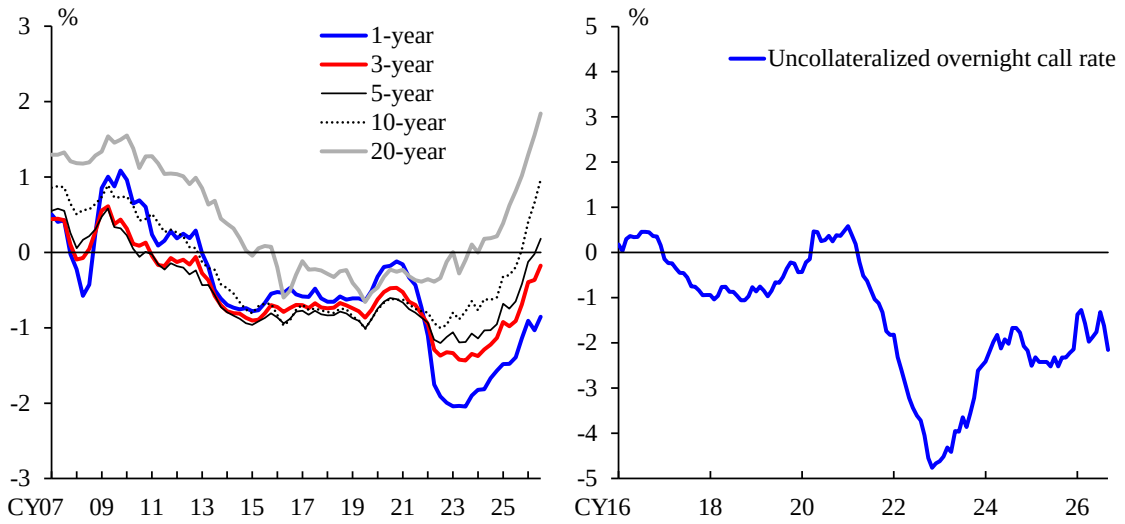
Chart 12: Framework for Assessing Financial Conditions



Source: Bank of Japan.

Let us first look at interest rate developments. Nominal interest rates have generally risen since autumn 2025. Real interest rates -- calculated by subtracting expected inflation rates from nominal interest rates for each maturity -- have remained at low levels, as shown in Chart 13, particularly in the short-term zone, where they have a relatively significant impact on economic activity. From a historical perspective, real interest rates are still accommodative compared with the period of unprecedented monetary easing. Furthermore, it is important to note that positive real interest rates do not necessarily immediately imply tightening conditions.

Chart 13: Real Interest Rates

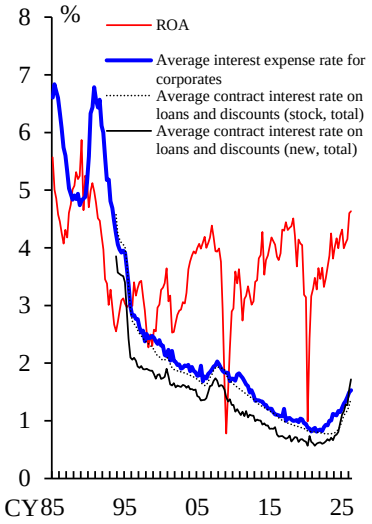


Notes: 1. In the left panel, figures are calculated as nominal JGB yields minus the composite index of inflation expectations (Bank staff estimates). The 20-year real interest rate is calculated by subtracting 10-year inflation expectations from 20-year JGB yields.
2. In the right panel, figures are calculated as the uncollateralized overnight call rate minus the CPI excluding fresh food and institutional factors.
Sources: Bloomberg; Consensus Economics Inc., *Consensus Forecasts*; Ministry of Internal Affairs and Communications; QUICK, *QUICK Monthly Market Survey <Bonds>*; Bank of Japan.

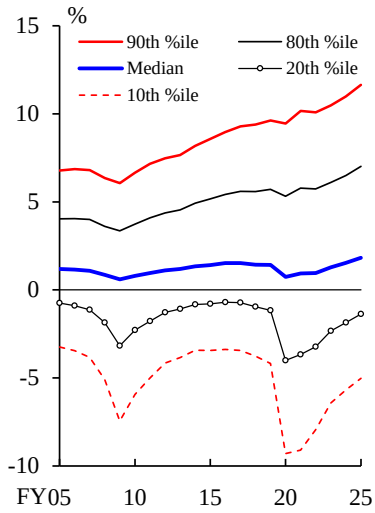
Turning next to funding conditions, funding costs -- including lending rates and issuance rates for CP and corporate bonds -- have increased. However, as shown in Chart 14, the average interest expense rate for corporates on a stock basis has remained sufficiently low relative to their profitability. Developments in operating profits to sales for small and medium-sized firms suggest that many firms are making efforts to further improve profitability and refine their business models so that they can generate profits in a world with positive interest rates. Moreover, corporate bankruptcies due to increased interest payment burdens have been limited. In terms of the availability of funds, as shown in Chart 15, financial institutions' lending attitudes as perceived by firms have remained accommodative, and firms' financial positions have continued to be favorable. As for funding volumes, as shown in Chart 16, the results of the *Senior Loan Officer Opinion Survey on Bank Lending Practices at Large Japanese Banks* and the amount outstanding of bank lending show that demand for funds is still increasing. Furthermore, although asset prices that reflect stock prices and foreign exchange rates are affected significantly by factors other than monetary policy, fluctuations in these asset prices have -- as an indication of financial conditions -- a substantial impact on the economy.

Chart 14: Funding Costs, Operating Profits to Sales, Bankruptcies

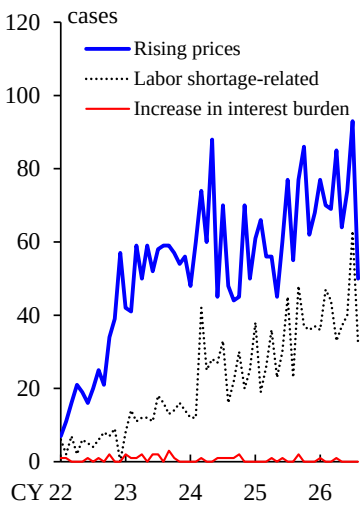
Firms' Funding Costs and Profitability



Ratio of Operating Profits to Sales for SMEs



Bankruptcies by Cause



Notes: 1. In the left panel, ROA is calculated as operating profits divided by total assets. The average interest expense rate for corporates is calculated as interest payments divided by interest-bearing debt. Figures for these items are based on the *Financial Statements Statistics of Corporations by Industry, Quarterly*, and are for all enterprises. Figures exclude "finance and insurance," and those for 2009/Q2 onward also exclude "pure holding companies"; all figures are seasonally adjusted. The average contract interest rates on loans and discounts are based on domestically licensed banks.

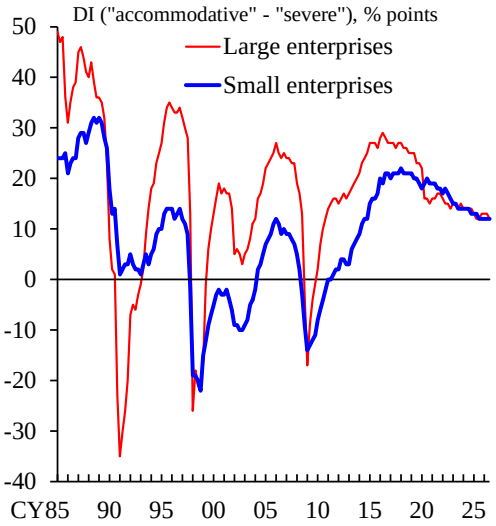
2. Figures in the middle panel are based on the CRD. SMEs covered are those with capital of 100 million yen or less and sales of 100 million yen or more.

3. In the right panel, multiple choices were allowed regarding the causes of bankruptcy.

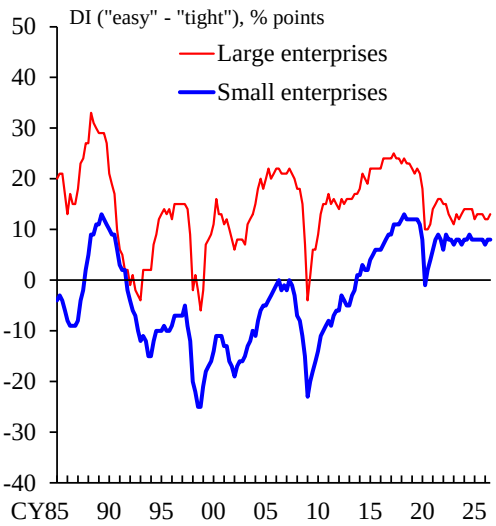
Sources: CRD Association; Ministry of Finance; Tokyo Shoko Research, Ltd.; Bank of Japan.

Chart 15: Lending Attitudes of Financial Institutions and Firms' Financial Positions

Lending Attitudes of Financial Institutions as Perceived by Firms



Firms' Financial Positions

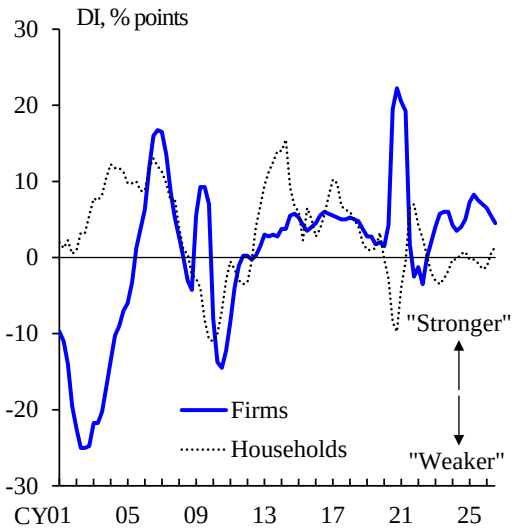


Note: Figures are based on the *Tankan*, and are for all industries. There is a discontinuity in the data for December 2003 due to a change in the survey framework.

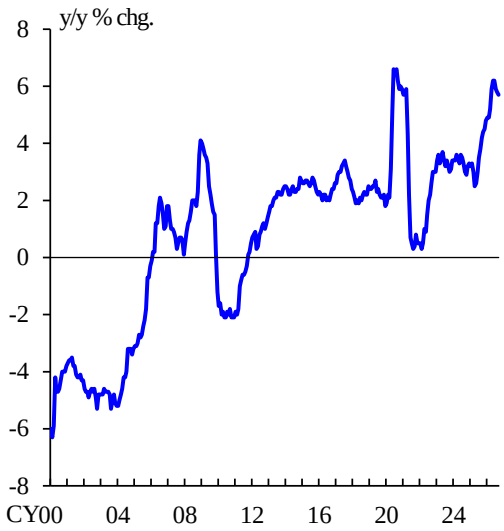
Source: Bank of Japan.

Chart 16: Funding Volumes

DI for Demand for Loans by Borrower Type



Amount Outstanding of Bank Lending



Notes: 1. Figures in the left panel are based on the *Senior Loan Officer Opinion Survey on Bank Lending Practices at Large Japanese Banks*, and indicate changes in demand for loans over the past three months. DI for demand for loans = (percentage of respondents selecting "substantially stronger" + percentage of respondents selecting "moderately stronger" × 0.5) - (percentage of respondents selecting "substantially weaker" + percentage of respondents selecting "moderately weaker" × 0.5). Figures are 4-quarter backward moving averages.
2. Figures in the right panel are monthly averages.
Source: Bank of Japan.

In addition, what I attach even greater importance to than these indicators is the opinion of firms. I believe that firms' opinions provide the clearest reaction to changes in financial conditions such as interest rate hikes. It is important to examine each of these opinions carefully, through anecdotal information from firms and reports at the meeting of general managers of the Bank's branches. This will contribute to the understanding of how far firms' business activities are likely to be restrained -- for example, whether they find it difficult to undertake new investment at current interest rates -- and what changes are occurring in the behavior of households, as firms' customers. Furthermore, when statistical data suggest that demand for funds is not increasing, banks' lending attitudes have tightened, or firms' financial positions are tight, it is also necessary, in considering future policy responses, to carefully assess whether these developments are attributable to monetary policy or to other factors, such as the effects of rising input prices or of institutional regulations.

My own assessment of the current situation, based on the opinions expressed by firms, is that the majority of them perceive the impact on business activity of past policy interest rate hikes

and near-term potential further rate hikes to be limited. Some firms have begun to say that higher interest rates will restrain investment or that they are concerned about future implications. Nevertheless, given that the purpose of interest rate hikes is to stabilize prices by influencing demand, it is, in a sense, only natural that gradually more firms begin to point to an impact on business activity. I believe the Bank is therefore entering a phase in which it is important to carefully monitor how common this opinion becomes, and to comprehensively assess the current monetary policy stance, that is, to confirm whether it is accommodative, neutral, or restrictive.

Given that financial conditions remain accommodative as I mentioned earlier, I believe that the Bank needs to bring the policy interest rate to the neutral level soon.[6] The essential prerequisite for determining the pace of further policy rate hikes is to carefully examine developments in underlying CPI inflation and financial conditions. That said, I believe that, within a few months of each rate hike, the Bank can make a reasonable assessment of financial conditions based on information obtained from interviews with firms and the results of various surveys. While it is necessary to make these assessments "thoroughly," that does not mean "slowly." In my view, the Bank is currently expected to "make haste slowly." Furthermore, as I mentioned earlier, given that underlying CPI inflation in Japan is less firmly anchored at the 2 percent target, I believe the Bank is required to respond swiftly to signs of an upward deviation in prices, including by accelerating the pace of policy interest rate hikes. It is important to remember the Bank's mandated role as the "guardian of price stability," and as such, the Bank must endeavor to prevent underlying CPI inflation deviating upward to a level above the 2 percent price stability target and avoid the adverse effects on the economy that would entail.

Thank you.

[6] I mentioned in my speech on June 25, 2026, that the neutral interest rate is most likely around 2 percent, and my view has not changed, considering the policy change thereafter, the accompanying developments in various indicators, and anecdotal information from firms.