

**Statement by Haruhiko Kuroda, Governor of the Bank of Japan, concerning the Bank's *Semiannual Report on Currency and Monetary Control* before the Committee on Financial Affairs, House of Councillors, on October 28, 2014**

**Introduction**

The Bank of Japan submits to the Diet its *Semiannual Report on Currency and Monetary Control* in June and December. I am pleased to have this opportunity today to talk about developments in Japan's economy and present an overall review of the Bank's conduct of monetary policy.

**I. Economic and Financial Developments in Japan**

First, I will explain economic and financial developments in Japan.

Japan's economy has continued to recover moderately as a trend with a virtuous cycle from income to spending being maintained steadily in both the household and corporate sectors, although some weakness, particularly on the production side, has been observed due mainly to the effects of the decline in demand following the front-loaded increase prior to the consumption tax hike.

In the household sector, the employment and income situation has been improving steadily. Labor market conditions have been tightening steadily. Specifically, the unemployment rate has declined to 3.5 percent, which is roughly the same level as the structural unemployment rate. In addition, in the September *Tankan* (Short-Term Economic Survey of Enterprises in Japan), the employment conditions DI for all industries and enterprises was net "insufficient," and at its highest level since May 1992. Against the backdrop of this improvement in employment conditions, nominal wages per employee have been increasing moderately. The year-on-year rate of change in scheduled cash earnings has been positive, reflecting an increase in base pay in the annual wage negotiation between management and labor this spring, and summer bonuses increased steadily. Reflecting these employment and wage developments, the year-on-year rate of increase in employee income has been accelerating moderately. Turning to household spending, the effects of the decline in demand following the front-loaded increase have been prolonged in durable

goods consumption such as automobiles and in housing investment -- both reflecting the large degree of front-loading of purchases. In addition, through this summer, irregular weather seems to have had adverse effects on private consumption. However, on the back of the steady improvement in the employment and income situation, private consumption has remained resilient as a trend, and the effects of the decline in demand following the front-loaded increase have been waning, except for durable goods including automobiles.

With regard to the corporate sector, Japan's exports have shown some weakness due mainly to the sluggishness in emerging economies, such as some of the ASEAN economies, which are closely tied with Japan's economy. Due mainly to such developments in exports and to inventory adjustments in industries such as those relating to automobiles and housing, for which the effects of the decline in demand following the front-loaded increase have been prolonged, industrial production has been showing some weakness recently. By contrast, business fixed investment has increased moderately as corporate profits have improved. On this point, as shown in the September *Tankan* released at the beginning of this month, business sentiment has stayed at a favorable level, and firms are planning to increase their investment steadily in fiscal 2014, with their projections for profits being revised upward. This indicates that many firms seem to be regarding the decline in demand following the consumption tax hike as temporary.

With regard to the outlook, with a virtuous cycle from income to spending continuing to operate in both the household and corporate sectors, Japan's economy is expected to continue on its moderate recovery trend, and the effects, including those of the decline in demand following the front-loaded increase, are expected to wane gradually.

Financial conditions, which support such economic activity, are accommodative. Firms' funding costs have been hovering at low levels, as seen in the fact that average bank lending rates have declined to historical low levels. Firms have continued to see financial institutions' lending attitudes as being on an improving trend, and issuing conditions for CP and corporate bonds have continued to be favorable. The amounts outstanding of bank lending as a whole and for small firms have been rising moderately, and the year-on-year rate of increase for the former has been in the range of 2.0-2.5 percent.

On the price front, excluding the direct effects of the consumption tax hike, the year-on-year rate of increase in the consumer price index (CPI, all items less fresh food) has been around 1¼ percent, although it has slowed somewhat, reflecting recent developments in energy prices. The price increase since the introduction of quantitative and qualitative monetary easing (QQE) basically reflects an improvement in the output gap and a rise in inflation expectations. Namely, the output gap has been improving, mainly on the labor front, and recently has been at around 0 percent, which is the past long-term average. Inflation expectations have been rising on the whole and this development has been influencing wage and price formation. Looking ahead, the year-on-year rate of increase in the CPI is likely to be around 1¼ percent for some time. Subsequently, it is likely to follow a rising trend again from the second half of this fiscal year and reach around 2 percent -- the price stability target -- around the middle of the current projection period from fiscal 2014 through fiscal 2016.

Risks to the outlook for economic activity and prices include developments in the emerging and commodity-exporting economies, the prospects for the European debt problem, and the pace of recovery in the U.S. economy. Therefore, the Bank will continue to pay close attention to future developments in economic situations, including those in financial markets.

## **II. Conduct of Monetary Policy**

Next, I will explain the Bank's conduct of monetary policy.

In April last year, the Bank introduced the QQE in order to achieve the price stability target of 2 percent in terms of the year-on-year rate of change in the CPI at the earliest possible time, with a time horizon of about two years. Thereafter, the Bank has been implementing the QQE steadily. The QQE has been exerting its intended effects and Japan's economy has been on a path that suggests that the 2 percent price stability target will be achieved as expected.

However, we are only halfway along the path toward achieving the price stability target of 2

percent. The Bank will continue with the QQE, aiming to achieve the price stability target of 2 percent, as long as it is necessary for maintaining that target in a stable manner. If the outlook changes due to the manifestation of risk factors and it is judged necessary for achieving the price stability target, the Bank will make adjustments without hesitation.

Today, we at the Bank will explain the *Semiannual Report on Currency and Monetary Control* for the second half of fiscal 2012. Article 54 of the Bank of Japan Act stipulates that the Bank shall submit this report to the Diet every six months and endeavor to explain its content. It will continue to make every effort in line with the thrust of the Bank of Japan Act so that the report will be submitted and explained to the Diet without delay. The Bank sincerely asks the Diet for its deliberation on the report.

Thank you.