Statement by Masaaki Shirakawa, 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 April 9, 2009

Introduction

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

I. Developments in Japan's Economy

Japan's exports have been decreasing substantially, reflecting the deterioration in overseas economic conditions, and domestic demand has become weaker against the background of declining corporate profits and the worsening employment and income situation in the household sector. Financial conditions have remained tight on the whole, as shown by, for example, an increase in the number of firms reporting that their financial positions are weak and lending attitudes of financial institutions are severe, despite improvements in issuing conditions for CP and corporate bonds. Under these circumstances, economic conditions have deteriorated significantly.

The Bank makes public each quarter Policy Board members' forecasts for economic activity and prices. The median of their most recent forecasts for Japan's economic growth rate in fiscal 2009, released in January 2009, was minus 2.0 percent. At the Monetary Policy Meetings (MPMs) held each month thereafter, Policy Board members shared the view that Japan's economic conditions had become increasingly severe. Recently released economic indicators, such as the March *Tankan* (Short-Term Economic Survey of Enterprises in Japan), have supported this view. It seems highly likely that Japan's economy has become weaker than the January forecasts. The pace of decline in exports and production is expected to moderate as inventory adjustments progress both at home and abroad, but economic conditions are likely to continue deteriorating for the time being due to a further weakening in domestic private demand.

On the price front, domestic corporate goods prices have continued to decline, mainly due to the drop in international commodity prices. CPI inflation (excluding fresh food) has recently moderated reflecting the declines in the prices of petroleum products and the stabilization of food prices, and, with increasing slackness evident in supply and demand conditions, will likely become negative in the future.

There are risks to the outlook for economic activity and prices. Much depends on global financial conditions as well as developments in overseas economies, and particular attention will need to be paid to the downside risks posed to economic activity. In addition, there is the risk of a further weakening in domestic private demand if firms' medium- to long-term growth expectations decline and pressures to adjust capital stock and employment increase. If financial conditions should tighten further, pressures acting to depress economic activity from the financial side might become more marked and the adverse feedback loop between financial and economic activity might intensify. Turning to prices, there is a possibility that the inflation rate will decline further if downside risks to economic activity materialize or if commodity prices fall. In this case, the risk of a decline in the medium- to long-term inflation expectations of firms and households would warrant attention.

II. Conduct of Monetary Policy

In order to support the economy from the monetary policy side, since fall 2008, the Bank has taken various steps, which can be divided into three areas: reductions in the policy interest rate; measures to ensure stability in financial markets; and steps to facilitate corporate financing. Regarding the policy interest rate, the Bank reduced it twice in October and December 2008, and currently encourages the uncollateralized overnight call rate to remain at around 0.1 percent. In order to ensure stability in financial markets, the Bank, as part of the coordinated measures of central banks, has been conducting U.S. dollar funds-supplying operations whereby funds are provided with no explicit ceiling on the total amount. The Bank has also continued to provide ample liquidity in yen, taking measures such as increasing the amount of outright purchases of Japanese government bonds (JGBs) to 21.6 trillion yen per year. To facilitate corporate financing, the Bank has expanded the range of corporate financing instruments eligible as collateral, and has conducted special funds-supplying operations to facilitate corporate financing through which, taking corporate debt as collateral, it provides unlimited funds at a low interest rate. The Bank has also continued to conduct outright purchases of CP and corporate bonds.

Meanwhile, to secure stability in the financial system, the Bank has resumed purchases of stocks held by financial institutions, and is examining the specifics of a scheme to provide subordinated loans to financial institutions.

III. The Future Conduct of Monetary Policy

The outlook for economic activity and prices is highly uncertain at present. The Bank will continue to exert its utmost efforts as the central bank to facilitate the return of Japan's economy to a sustainable growth path with price stability.