

February 14, 2012

Bank of Japan

The Price Stability Goal in the Medium to Long Term

1. The Bank of Japan conducts monetary policy based on the principle that the policy shall be aimed at "achieving price stability, thereby, contributing to the sound development of the national economy." In doing so, price stability must be the one sustainable in the medium to long term.
2. At today's Monetary Policy Meeting, the Policy Board of the Bank introduced "the price stability goal in the medium to long term" as a part of its efforts to further clarify the determination to overcome deflation and achieve sustainable growth with price stability.
3. "The price stability goal in the medium to long term" is the inflation rate that the Bank judges to be consistent with price stability sustainable in the medium to long term. The Bank judges that "the price stability goal in the medium to long term" is in a positive range of 2 percent or lower in terms of the year-on-year rate of change in the consumer price index (CPI) and, more specifically, set a goal at 1 percent for the time being. Prior to today's introduction of the goal, the "understanding of medium- to long-term price stability" showed a range of inflation rates that each Policy Board member understood as price stability from a medium- to long-term viewpoint.
4. At today's meeting, the Board confirmed that the following elements of basic thinking about "price stability" agreed in the past, which form the basis of "the price stability goal in the medium to long term," were still relevant.
 - (1) Conceptual definition: "Price stability" is a state where economic agents such as households and firms may make decisions regarding economic activities without being concerned about the fluctuations in the general price level.
 - (2) Time frame: Price stability should be pursued over the medium to long term by making economic and price forecasts from a sufficiently long-term viewpoint.
 - (3) Main indicator: The basic indicator for the evaluation of price developments is a price index that covers goods and services consumed by households and which the public at large is accustomed to. In particular, the CPI is important in light of its favorable

attributes including timeliness.

5. In expressing "the price stability goal in the medium to long term" in specific inflation rates, following the exercise in the past reviews, the Board examined the rate from three perspectives: measurement bias in a price index; the safety margin that acts as a buffer against the risk of a vicious cycle of deflation and stagnation; and the rate of inflation at which households and firms perceive price stability, i.e. the general public's perception of price developments. It also deems necessary to consider high uncertainty surrounding the future developments such as structural changes in Japan's economy and global economic environment. For this reason, the Board decided to express "the price stability goal in the medium to long term" in specific inflation rates by making some allowances as "a positive range of 2 percent or lower in terms of the year-on-year rate of change in the CPI." Within this range, the Board decided to set a goal at 1 percent for the time being to clarify the inflation rate which the Bank's monetary policy aims to achieve.
6. "The price stability goal in the medium to long term" will be reviewed once a year in principle.