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February 26, 2007

Bank of Japan

Minutes of the Monetary Policy Meeting

on January 17 and 18, 2007

(English translation prepared by the Bank's staff based on the Japanese original)

A Monetary Policy Meeting of the Bank of Japan Policy Board was held in the Head Office of the Bank of Japan in Tokyo on Wednesday, January 17, 2007, from 2:00 p.m. to 4:01 p.m., and on Thursday, January 18, from 9:00 a.m. to 1:01 p.m.¹

Policy Board Members Present

Mr. T. Fukui, Chairman, Governor of the Bank of Japan

Mr. T. Muto, Deputy Governor of the Bank of Japan

Mr. K. Iwata, Deputy Governor of the Bank of Japan

Ms. M. Suda

Mr. H. Haru

Mr. T. Fukuma

Mr. A. Mizuno

Mr. K. G. Nishimura

Mr. T. Noda

Government Representatives Present

Mr. K. Tanaka, Senior Vice Minister of Finance, Ministry of Finance²

Mr. E. Katsu, Deputy Vice Minister for Policy Planning and Coordination, Ministry of Finance³

Mr. J. Hamano, Vice Minister for Policy Coordination, Cabinet Office

Reporting Staff

Mr. N. Inaba, Executive Director

Mr. A. Horii, Executive Director (Assistant Governor)

Mr. K. Ido, Executive Director

Mr. M. Amamiya, Director-General, Monetary Affairs Department

Mr. S. Uchida, Senior Economist, Monetary Affairs Department

¹ The minutes of this meeting were approved by the Policy Board at the Monetary Policy Meeting held on February 20 and 21, 2007 as "a document which contains an outline of the discussion at the meeting" stipulated in Article 20, Paragraph 1 of the Bank of Japan Law of 1997. Those present are referred to by their titles at the time of the meeting.

² Mr. K. Tanaka was present on January 18.

³ Mr. E. Katsu was present on January 17.

Mr. H. Nakaso, Director-General, Financial Markets Department

Mr. H. Hayakawa, Director-General, Research and Statistics Department

Mr. E. Maeda, Deputy Director-General, Research and Statistics Department

Mr. T. Idesawa, Director-General, International Department

Secretariat of the Monetary Policy Meeting

Mr. Y. Nakayama, Director-General, Secretariat of the Policy Board

Mr. Y. Iino, Adviser to the Governor, Secretariat of the Policy Board

Mr. K. Shigyoh, Director, Secretariat of the Policy Board

Mr. K. Kamiyama, Senior Economist, Monetary Affairs Department

Mr. K. Suzuki, Senior Economist, Monetary Affairs Department

I. Summary of Staff Reports on Economic and Financial Developments⁴

A. Money Market Operations in the Intermeeting Period

The Bank conducted money market operations in accordance with the guideline decided at the previous meeting on December 18 and 19, 2006.⁵ The uncollateralized overnight call rate had been at around 0.25 percent.

B. Recent Developments in Financial Markets

In the money market, interest rates on Euroyen and on three-month financing bills (FBs) were more or less unchanged, despite fluctuations reflecting changes in market participants' expectation regarding the timing of a rise in the policy rate. Interest rates on Euroyen futures had generally been unchanged.

Japanese stock prices had risen against the background of the depreciation of the yen and an improvement in market participants' view of domestic and foreign economic developments. The Nikkei 225 Stock Average was recently in the range of 17,000-17,500 yen.

Long-term interest rates had been more or less unchanged, and were recently at around 1.7 percent.

The yen had depreciated against the U.S. dollar, mainly because U.S. economic indicators had been stronger than market forecasts. It was recently being traded in the range of 119-121 yen to the dollar.

C. Overseas Economic and Financial Developments

The U.S. economy continued to expand, but the pace of growth was decelerating. Housing investment continued to decrease, while business fixed investment continued to increase. Private consumption had been relatively firm recently, but continued to be on a decelerating trend. In this situation, the pace of increase in production and in the number of employees was slowing moderately. As for prices, the pace of increase in the consumer price index (CPI) for all items had been moderate, but the core inflation rate (the CPI for all

⁴ Reports were made based on information available at the time of the meeting.

⁵ The guideline was as follows:

The Bank of Japan will encourage the uncollateralized overnight call rate to remain at around 0.25 percent.

items less food and energy) continued to increase moderately as a trend, mainly reflecting tighter supply-demand conditions due to the economic expansion.

In the euro area, economic recovery continued to be steady, as the increase in production and improvement in corporate profits had led to recovery in business fixed investment and private consumption. The U.K. economy continued to show stable growth.

In China, both domestic and external demand continued to expand strongly. The rate of increase in fixed asset investment remained high, although it had slowed somewhat. Exports continued to show a substantial increase. The NIEs and ASEAN economies continued to expand at a moderate pace on the whole, although the increase in exports seemed to have come to a pause recently.

In financial markets, long-term interest rates in the United States edged up higher as market participants responded to the release of relatively strong economic indicators in a situation where indicators had been showing mixed developments. Meanwhile, U.S. stock prices had been more or less unchanged. Also, in Europe long-term interest rates had risen slightly, while stock prices had been more or less unchanged. In many emerging economies, financial markets had been firm toward the end of 2006, but since the beginning of 2007 stock prices and currencies had generally been relatively weak.

D. Economic and Financial Developments in Japan

1. Economic developments

Exports had continued to increase against the background of the expansion of overseas economies, and were expected to continue to rise as overseas economies taken as a whole continued to expand.

As for domestic private demand, business fixed investment had continued to increase, and was expected to keep increasing since the growth in domestic and external demand and the high levels of corporate profits were likely to be maintained.

Private consumption had been on an increasing trend, although the pace of increase had been only modest. Sales at department stores and supermarkets had continued to be susceptible to weather conditions; they had picked up in August-September, but were relatively weak again in October-November, weighed down by sluggish sales of winter apparel due to the somewhat high temperatures. As for services consumption, sales in the food service industry had continued to trend upward, and outlays for travel, especially

overseas travel, had generally been firm. Private consumption was expected to follow an uptrend, mainly reflecting the gradual increase in household income.

Production had continued to increase against the background of the growth in domestic and external demand. Inventories had been more or less in balance with shipments in the industrial sector as a whole, although inventories of electronic parts and devices had been at a high level relative to shipments. The upward trend in production was expected to continue, reflecting the rise in domestic and external demand, with overall inventories more or less in balance with shipments. However, interviews with firms suggested that the quarter-on-quarter increase in production in the January-March quarter of 2007 was likely to be only marginal, after the high growth in the October-December quarter of 2006, which seemed to have been more than 2 percent.

With regard to the employment and income situation, household income had continued rising moderately in a situation where various indicators had continued to show tighter labor market conditions. The gradual increase in household income was likely to continue against the background that firms were increasingly feeling a shortage of labor and corporate profits were expected to remain high.

On the price front, crude oil prices had been falling somewhat sharply again since the start of 2007, affected by the unseasonably warm weather in the northeastern United States. Prices of nonferrous metals had remained high on the whole, although they had been falling lately, particularly copper. Compared with three-month-earlier levels, domestic corporate goods prices had recently been somewhat lower and were likely to continue to be somewhat lower or stay about the same in the immediate future, due to the drop in international commodity prices. The year-on-year rate of change in the CPI (excluding fresh food, on a nationwide basis) had been on a positive trend. This trend was projected to continue, as the output gap continued to be positive.

Reports at the meeting of general managers of the Bank's branches and the *Regional Economic Report* released on January 12, 2007 confirmed that the economy as a whole was expanding moderately as all the regional economies continued to improve, although there were regional differences.

2. Financial environment

The environment for corporate finance was accommodative. The issuing

environment for CP and corporate bonds was favorable, and the lending attitudes of private banks had continued to be accommodative. Credit demand in the private sector had been increasing. Under these circumstances, the amount outstanding of lending by private banks had been increasing. The amount outstanding of CP and corporate bonds issued was slightly below the previous year's level.

II. Summary of Discussions by the Policy Board on Economic and Financial Developments

A. Economic Developments

On the current state of Japan's economy, members concurred that the economy continued to expand moderately, and was likely to experience a sustained period of growth with domestic and external demand increasing and the positive influence of the strength in the corporate sector feeding through into the household sector.

Members concurred that overseas economies taken as a whole continued to expand, with more economies gaining momentum, and were likely to keep expanding.

On the U.S. economy, members agreed that, despite a continued cooling in housing investment, the deceleration of growth in private consumption remained moderate, mainly reflecting the increase in household income and the drop in gasoline prices. Many members expressed the view that the U.S. economy was becoming more likely to realize a soft landing, noting the following points. First, there were some signs of a bottoming out in housing sales. Second, the Purchasing Managers' Index (PMI) for the manufacturing sector compiled by the Institute for Supply Management (ISM) for December recovered to above 50 percent, the breakeven point between expansion and decline in economic activity in the sector. And third, the decline in crude oil prices was expected to enhance households' real purchasing power. A few members said that, although the U.S. economy was likely to grow at a rate modestly below its potential for a time, it was likely to return to a growth path around its potential growth rate by late 2007. However, many members, including these members, said that both upside and downside risks should continue to be borne in mind, given that the likely extent of future adjustments in the housing market was still uncertain and the core inflation rate (the CPI for all items less food and energy) remained relatively high.

With regard to European economies, members agreed that economic recovery

continued to be steady in the euro area as the increase in production and improvement in corporate profits had led to recovery in business fixed investment and private consumption, and that the U.K. economy continued to show stable growth. On East Asian economies, members concurred that both domestic and external demand continued to expand strongly in China, and the NIEs and ASEAN economies continued to expand at a moderate pace on the whole.

As for developments in crude oil prices, one member said that the decline was unlikely to continue if the global economic expansion continued. A few members expressed the view that the recent decline had been due to the unseasonably warm weather in North America as well as the position adjustment by speculative market participants, and close attention should continue to be paid to developments in crude oil prices because uncertainties regarding the outlook for them were not negligible.

Regarding Japan's economy, members agreed that exports had continued to increase, reflecting the expansion of overseas economies, and were likely to continue to increase. One member said that exports to the United States had continued to be on an uptrend as a whole, although the economic slowdown had had some effects, for example, a slowing of growth in exports of automobile-related goods and a decline in those of construction machinery. This member also commented that, reflecting steady global demand for IT-related goods, exports of them had been increasing on the whole, particularly to China, although those to the NIEs had remained somewhat weak.

As for domestic private demand, members shared the view that business fixed investment continued to increase and was likely to keep increasing, reflecting the ongoing growth in domestic and external demand and also the continuing high level of corporate profits. Some members said that structural factors such as the expansion of profit opportunities reflecting economic globalization and a shortening of investment cycles were also contributing to the increase in business fixed investment. A few members considered that the current pace of growth in the capital stock was not excessive as firms were making investments based on a careful evaluation of their profitability, and said that business fixed investment was likely to keep increasing.

Many members expressed the view that private consumption had been on an increasing trend, although the pace of increase had been only modest, and it was likely to follow an uptrend, mainly reflecting the gradual increase in household income. Some

members said that indicators related to private consumption, including those in the *Family Income and Expenditure Survey*, had improved somewhat, and this seemed to confirm that the sluggishness in private consumption as seen in the GDP statistics for the July-September quarter had been only temporary. Some other members said that, based on interviews with firms, although year-end and new-year sales were generally steady, the pace of increase in sales in the period thereafter seemed to have been only modest. Some members pointed out that the pace of improvement in indicators for consumer sentiment continued to be sluggish. Members agreed that it was most likely that the underlying trend of private consumption would grow stronger as the employment and income situation improved. Some members added, however, that more data were needed in order to be certain. A few members expressed the view that it was unrealistic to expect high growth in private consumption, taking into account the effects of structural factors such as demographic changes.

Members agreed that production had continued to increase and was likely to continue to be on an upward trend against the background of the rise in domestic and external demand. Members also concurred that inventories had been more or less in balance with shipments in the industrial sector as a whole. Some members said that inventories of electronic parts and devices remained at high levels. However, they considered that substantial, widespread inventory adjustments were unlikely, because the shipment-inventory balance had almost stopped deteriorating due to an adjustment in production and an increase in shipments, and also because demand for IT-related goods, especially from overseas, had so far been steady on the whole. One member said, however, that attention should continue to be paid to developments in final demand for IT-related products because they were highly uncertain.

As for the employment and income situation, members concurred that household income had continued rising moderately in a situation where various indicators had continued to show tighter labor market conditions. They also agreed that the gradual increase in household income was likely to continue against the background that firms were increasingly feeling a shortage of labor and corporate profits were expected to remain high. Some members said that, given that firms were taking account of intensifying global competition, the current situation where the increase in wages was sluggish, particularly in regular payments, was unlikely to change substantially. Some members, however,

expressed the view that, despite the sluggish increase in wages, the channels through which the positive influence of the strength in the corporate sector fed into the household sector were not completely blocked: the positive influence was gradually feeding through via certain channels, such as increases in the number of employees, the wages of part-time and temporary workers, bonus payments, and dividends.

With regard to prices, members agreed that, compared with the levels of three months earlier, domestic corporate goods prices had been somewhat lower, due to the drop in international commodity prices, and they were likely to continue to be somewhat lower or stay about the same in the immediate future.

Members concurred that the year-on-year rate of change in the CPI (excluding fresh food, on a nationwide basis) had been on a positive trend, and that this trend was likely to continue, as the output gap continued to be positive. Many members said that it was more important to properly assess the price formation mechanism, in other words how the output gap and unit labor costs influenced prices, through fiscal 2007 than to simply watch developments in the CPI. These members added that, judging from the developments in the output gap and unit labor costs, the underlying trend of inflation pressures seemed to be increasing steadily. One member commented, however, that it continued to be difficult for firms to raise prices as they faced global competition. Some members including this member expressed the view that even though the rate of increase in the CPI would rise gradually as a trend, there still remained uncertainty about the precise pace of its rise.

Some members said that it was likely that the drop in crude oil prices would exert downward pressure on the year-on-year rate of change in the CPI for the immediate future, with the possibility of it temporarily registering zero percent or slightly below zero percent. One of these members added that the preliminary figure for the CPI in the Tokyo metropolitan area suggested that the year-on-year rate of increase in the CPI on a nationwide basis for December was likely to be lower than that of November. A few other members said that it should be noted that a fall in crude oil prices had positive effects on economic activity by improving the terms of trade.

As for developments in asset prices, one member said that, although there were transactions that seemed to indicate a quasi-bubble phenomenon in specific parts of some metropolitan areas, taken as a whole land prices reflected fair value.

B. Financial Developments

On the financial front, members agreed that the financial environment remained accommodative as seen in the fact that the lending attitudes of private banks and the issuing conditions in capital markets were favorable. Some members commented that the effective exchange rate of the yen had declined further reflecting market participants' projection that interest rate differentials between Japan and other economies would persist, and therefore the financial environment was becoming more accommodative.

C. Interim Assessment

Given the above assessment of economic activity, prices, and financial developments in Japan, one member said that the economy had developed broadly in line with the Bank's projection presented in the October 2006 *Outlook for Economic Activity and Prices* (hereafter the Outlook Report). The member noted that the economic growth rate was likely to deviate downward from the October projection of "around 2.5 percent for fiscal 2006" and "around 2 percent for fiscal 2007" to around 2 percent for both fiscal 2006 and 2007. The member continued that this downward deviation was largely attributable to the annual revision of the GDP data for fiscal 2005, which reduced the carry-over effect from fiscal 2005, lowering the year-on-year growth rate for fiscal 2006 by 0.3 percentage point.

In response to this view, most members said that developments in Japan's economy had so far deviated slightly downward from the October projection, mainly due to weaker-than-expected private consumption caused partly by temporary downward pressure stemming from the unfavorable weather conditions. These members agreed that the downward deviation of the growth rate from the projection was also attributable to the annual revision of the GDP data for fiscal 2005, and therefore this point should be noted in the interim assessment.

As for the outlook for Japan's economy, members concurred that the economy was likely to develop broadly in line with the projection, as a virtuous circle of production, income, and spending was likely to remain intact.

Regarding prices, members agreed that domestic corporate goods prices were likely to deviate slightly downward from the expected trajectory, reflecting the drop in

crude oil prices. Members also agreed that consumer prices had so far deviated slightly downward from the projection, partly reflecting the drop in crude oil prices, but they were likely to develop broadly in line with the projection.

One member added that economic expansion and a rise in prices in line with the projection were taking longer to materialize than expected, and there remained uncertainty about future developments in economic activity and prices.

III. Summary of Discussions on Monetary Policy for the Immediate Future

Based on their assessment of the economic and financial situation, members agreed that their basic thinking remained unchanged on the future path of monetary policy: the Bank would adjust the level of the policy interest rate gradually in the light of developments in economic activity and prices, while maintaining the accommodative financial conditions ensuing from very low interest rates for some time.

On this basis, some members commented on the guideline for money market operations for the intermeeting period ahead that it would be appropriate to raise the uncollateralized overnight call rate target from around 0.25 percent to around 0.5 percent. They were of the view that, given that recently released economic indicators did not necessitate a change in the Bank's assessment of the mechanisms underlying Japan's economy, it would be appropriate to adjust the level of the policy interest rate at this juncture so that a desirable course of economic activity and prices would be maintained, and this adjustment would contribute to price stability and sustainable growth in the long term. Regarding risks arising from maintaining the policy interest rate at the current level, they said that the stimulative effect of monetary policy on economic activity and prices might be amplified excessively or expectations that interest rates would remain low for a long time regardless of economic activity and prices might increase.

Against this view, the majority of members said that it would be appropriate to maintain the current guideline for money market operations that the Bank would encourage the uncollateralized overnight call rate to remain at around 0.25 percent. They expressed the view that, although the virtuous circle of production, income, and spending led by an increase in exports reflecting the expansion of overseas economies remained intact, recent economic indicators showed mixed developments and therefore it would be appropriate to continue to carefully examine incoming economic indicators as well as other relevant

information to more accurately assess developments in economic activity and prices. They expressed the view that, in its conduct of forward-looking monetary policy, it was important for the Bank to confirm with a high degree of confidence that economic activity and prices would develop in line with its projections, and in the current situation there was time for further examination. A few of these members added that, when it was confirmed with a high degree of confidence after thorough examination, the Bank should adjust the level of the policy interest rate without delay to prevent expectations from taking hold that interest rates would remain low for a long time regardless of economic activity and prices. Some members raised key factors that required close monitoring, such as developments in overseas economies, particularly the U.S. economy, the course of the household sector, and the environment surrounding prices, and expressed the view that it was important to accurately assess the future trend of Japan's economy by examining these key factors.

Members discussed the Bank's communication of its thinking concerning the conduct of monetary policy. Many members raised the issue of how the Bank should communicate with market participants given the recent large swings in the market's view regarding the timing of a policy change.

Some members pointed out that the term "forward-looking monetary policy" might have been misinterpreted as monetary policy conducted according to a predetermined time schedule. On this point, members agreed that the Bank's conduct of monetary policy should be decided solely based on a thorough discussion of economic activity and prices at every Monetary Policy Meeting, and any policy change should not be made based on a predetermined time schedule or predetermined intervals. Some members noted that, in conducting forward-looking monetary policy, it was a prerequisite that the Bank appropriately assess future developments in economic activity and prices based on a careful examination of economic indicators as well as other relevant information available. These members said that the Bank should make efforts to encourage better understanding among the public of its thinking concerning the future course of monetary policy, which was that it would adjust the level of interest rates gradually in the light of developments in economic activity and prices as had been explained in the October Outlook Report.

Based on the above discussions, members reaffirmed the following: the Bank was not conducting monetary policy based on a predetermined time schedule; the Bank considered it important to make projections regarding economic activity and prices after

carefully examining economic indicators as well as other relevant information available; thus, forward-looking and data-dependent approaches in conducting monetary policy were conceptually consistent; and the Bank should explain these points carefully.

Members also commented on points that the Bank needed to bear in mind in its communication. A few members said that, in communicating with market participants, the Bank should make efforts to encourage better understanding of its assessment of economic and financial developments as well as its basic thinking about the conduct of monetary policy, and added that its explanation should be based on the common understanding reached through discussions at Monetary Policy Meetings.

IV. Remarks by Government Representatives

The representative from the Ministry of Finance made the following remarks.

- (1) Japan's economy continued to recover, but developments should continue to be watched closely as the positive influence of the strength in the corporate sector on the household sector had recently weakened somewhat and some economic indicators such as those related to consumption showed weakness.
- (2) Prices were unlikely to decline continuously, but careful attention should continue to be paid to future price developments since factors such as the fall in crude oil prices were likely to continue to affect them.
- (3) Given the current developments in economic activity and prices, the government considered that it was important that the Bank continue to firmly support the economy based on the Bank's current guideline for money market operations in order to achieve sustainable economic growth with price stability.
- (4) The government would like the Bank to give due consideration to developments in financial markets. In order to prevent financial markets from becoming unstable due to speculation regarding the future conduct of monetary policy, it would also like the Bank to clearly explain its thinking regarding the future course of monetary policy to market participants and the public, along with its view on economic activity and prices in the interim assessment of the October 2006 Outlook Report.

The representative from the Cabinet Office made the following remarks.

- (1) Although the government considered that Japan's economy continued to recover, private

consumption was almost flat in a situation where the pace of growth in income had been decelerating, and the positive influence of the strength in the corporate sector on the household sector had recently weakened somewhat. A comprehensive review of developments in prices suggested that the economy had not yet overcome deflation. Careful monitoring of price movements taking into account risks arising from, for example, developments in overseas economies continued to be necessary.

- (2) With regard to the outlook for economic activity and prices, the government considered that particular attention should be paid to downside risks, since key factors for the future course of Japan's economy would be how developments in overseas economies affected the domestic economy and how the positive influence of the strength in the corporate sector fed through into the household sector, rather than upside risks. The government would like the Bank to fulfill its accountability to the public by clearly explaining, in its interim assessment of the October 2006 Outlook Report, its view regarding the economy's path toward price stability and the deviation of economic activity and prices from the Bank's previous projection.
- (3) Later in the day the Council on Economic and Fiscal Policy would submit to the Prime Minister the draft of the "Direction and Strategy for the Japanese Economy," the new medium-term policy, which was scheduled to be approved by the Cabinet on January 25, 2007 along with the "Fiscal 2007 Economic Outlook and Basic Stance for Economic and Fiscal Management." In order to achieve sustainable economic growth led by private demand based on price stability, it was important for the government and the Bank to make joint efforts, with a shared basic perspective on macroeconomic management. The government would like the Bank to implement effective monetary policy that was consistent with the government's policy efforts and with its outlook for the economy while paying due consideration to developments in financial markets, and to support the economy from the financial side responsibly, taking into account downside risks to the outlook for economic activity and prices.

V. Votes

Based on the above discussions, the majority of members agreed that it was appropriate to maintain the current guideline for money market operations, which encouraged the uncollateralized overnight call rate to remain at around 0.25 percent.

Some members, however, said that they would like to propose that the Bank should raise the uncollateralized overnight call rate target from around 0.25 percent to around 0.5 percent.

As a result, the following proposal was submitted and put to the vote.

Ms. M. Suda, Mr. A. Mizuno, and Mr. T. Noda proposed the following guideline for money market operations for the intermeeting period ahead:

The Bank of Japan will encourage the uncollateralized overnight call rate to remain at around 0.5 percent.

The proposal was defeated by a majority vote.

Votes for the proposal: Ms. M. Suda, Mr. A. Mizuno, and Mr. T. Noda.

Votes against the proposal: Mr. T. Fukui, Mr. T. Muto, Mr. K. Iwata, Mr. H. Haru, Mr. T. Fukuma, and Mr. K. G. Nishimura.

To reflect the majority view, the chairman formulated the following proposal and put it to the vote.

The Chairman's Policy Proposal on the Guideline for Money Market Operations:

The guideline for money market operations for the intermeeting period ahead will be as follows, and will be made public by the attached statement (see Attachment).

The Bank of Japan will encourage the uncollateralized overnight call rate to remain at around 0.25 percent.

Votes for the proposal: Mr. T. Fukui, Mr. T. Muto, Mr. K. Iwata, Mr. H. Haru, Mr. T. Fukuma, and Mr. K. G. Nishimura.

Votes against the proposal: Ms. M. Suda, Mr. A. Mizuno, and Mr. T. Noda.

Ms. M. Suda dissented from the above proposal for the following reasons. First,

it had been confirmed with more confidence that economic activity and prices were likely to develop in line with the Bank's projection. Second, if expectations took hold that interest rates would remain low for a long time regardless of economic activity and prices, there was a risk in the medium to long term of a channeling into larger swings in economic activity and prices, for example, via financial and corporate investment activities. And third, given the time lag between implementation of monetary policy and the materialization of its effects, the Bank should take action before problems arose in order to maintain stable growth.

Mr. A. Mizuno dissented from the proposal for the following reasons. First, it had been confirmed that Japan's economy was likely to continue to expand moderately and that in the long term prices were likely to rise gradually. Second, given this it was natural that the Bank should proceed with normalizing its monetary policy, and a delay in normalization would reduce the predictability of monetary policy actions. Third, the Bank's communication with market participants would become difficult as predictability declined. And fourth, if the Bank did not raise the policy interest rate at this meeting, the Bank might be misinterpreted as approving further depreciation of the yen.

Mr. T. Noda dissented from the proposal for the following reasons. First, it had been confirmed that Japan's economy would continue to expand moderately, very broadly in line with the projection presented in the October Outlook Report, as the virtuous circle of production, income, and spending was likely to remain intact. Second, if the Bank maintained the policy interest rate at its current level, this would increase the risk that the stimulative effect of monetary policy might be amplified, which might lead to larger swings in economic activity and prices. And third, raising the policy interest rate at this meeting would be consistent with the Bank's conduct of forward-looking monetary policy.

VI. Discussion on the Bank's View of Recent Economic and Financial Developments

Members discussed "The Bank's View" in the *Monthly Report of Recent Economic and Financial Developments* (consisting of "The Bank's View" and "The Background"), and put it to the vote.

The Policy Board decided, by a majority vote, the text of "The Bank's View." It was confirmed that "The Bank's View" would be published on January 18, 2007 and the

whole report on January 19, 2007.⁶

Votes for the proposal: Mr. T. Fukui, Mr. T. Muto, Mr. K. Iwata, Mr. H. Haru, Mr. T. Fukuma, Mr. A. Mizuno, Mr. K. G. Nishimura, and Mr. T. Noda.

Votes against the proposal: Ms. M. Suda.

Ms. M. Suda dissented from the above proposal for the following reasons. First, the downward deviation of the GDP growth rate for fiscal 2006 from the projection in the October Outlook Report was largely attributable to the annual revision of the GDP data for fiscal 2005, which reduced the carry-over effect from fiscal 2005, and the underlying trend of economic activity seemed to be broadly in line with the projection. And second, the qualification "although the pace of increase has been only modest" in the assessment of private consumption was unnecessary because the decline in private consumption in the July-September quarter was mainly due to temporary factors, such as unfavorable weather and consumers' reluctance to buy before the introduction of new products, and indicators related to private consumption since October had improved on the whole.

VII. Approval of the Minutes of the Monetary Policy Meeting

The Policy Board approved unanimously the minutes of the Monetary Policy Meeting of December 18 and 19, 2006 for release on January 23, 2007.

⁶ The English version of the whole report was published on January 22, 2007.

Attachment

January 18, 2007

Bank of Japan

At the Monetary Policy Meeting held today, the Bank of Japan decided, by a 6-3 majority vote, to set the following guideline for money market operations for the intermeeting period:

The Bank of Japan will encourage the uncollateralized overnight call rate to remain at around 0.25 percent.