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September 22, 2008

Bank of Japan

Minutes of the Monetary Policy Meeting

on August 18 and 19, 2008

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

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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 Monday, August 18, 2008, from 2:00 p.m. to 4:51 p.m., and on Tuesday, August 19, from 9:00 a.m. to 12:25 p.m.[1]

Policy Board Members Present

Mr. M. Shirakawa, Chairman, Governor of the Bank of Japan

Mr. K. G. Nishimura, Deputy Governor of the Bank of Japan

Ms. M. Suda

Mr. A. Mizuno

Mr. T. Noda

Mr. S. Nakamura

Mr. H. Kamezaki

Government Representatives Present

Mr. W. Takeshita, Senior Vice Minister of Finance, Ministry of Finance[2]

Mr. C. Kawakita, Deputy Vice Minister for Policy Planning and Coordination, Ministry of Finance[3]

Mr. B. Fujioka, Vice Minister for Policy Coordination, Cabinet Office

Reporting Staff

Mr. H. Yamaguchi, Executive Director

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

Mr. K. Ido, Executive Director

Mr. K. Yamamoto, Executive Director

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

Mr. T. Sekine, Associate Director-General, Monetary Affairs Department

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

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[1] The minutes of this meeting were approved by the Policy Board at the Monetary Policy Meeting held on September 16 and 17, 2008 as "a document describing an outline of the discussion at the meeting" stipulated in Article 20, paragraph 1 of the Bank of Japan Act of 1997. Those present are referred to by their titles at the time of the meeting.

[2] Mr. W. Takeshita was present on August 19.

[3] Mr. C. Kawakita was present on August 18.

Mr. K. Momma, Director-General, Research and Statistics Department

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

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

Secretariat of the Monetary Policy Meeting

Mr. K. Osugi, Director-General, Secretariat of the Policy Board

Mr. K. Shigyoh, Director, Deputy Head of Secretarial Services for the Board, Secretariat of the Policy Board

Mr. T. Kato, Senior Economist, Monetary Affairs Department

Mr. A. Otani, Senior Economist, Monetary Affairs Department

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

I. Summary of Staff Reports on Economic and Financial Developments[4]

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 July 14 and 15, 2008.[5] As a result, the uncollateralized overnight call rate had been at around 0.5 percent.

B. Recent Developments in Financial Markets

In the money market, Euroyen rates and interest rates on term instruments, such as yields on financing bills (FBs) and treasury bills (TBs), had been more or less flat. Interest rates on Euroyen futures, particularly those with distant contract months, had decreased, reflecting more cautious views about the outlook for Japan's economy.

Japanese stock prices had been unstable: they rallied temporarily in the middle of July, following U.S. and European stock prices, but fell back again in the latter half of July reflecting factors such as uncertainty about the outlook for Japan's economy and corporate performance. The Nikkei 225 Stock Average had been moving at around 13,000 yen recently.

Long-term interest rates had declined, reflecting those in the United States and Europe and more cautious views about the outlook for Japan's economy. They had recently been in the 1.4-1.5 percent range.

The yen continued to depreciate against the U.S. dollar, and had recently been traded in the range of 109-111 yen against the dollar.

C. Overseas Economic and Financial Developments

Growth in the U.S. economy had remained sluggish. A substantial decline in housing investment continued, and home prices were falling. Private consumption had continued to be more or less unchanged, and the deceleration in business fixed investment had also continued. In this situation, industrial production had been on a downward trend and the number of employees had continued to decline. As for prices, the year-on-year

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[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 0.5 percent.

rate of increase in consumer prices had been elevated, not only in terms of the consumer price index (CPI) for all items but also the CPI for all items less energy and food, or the core CPI, which registered a year-on-year rate of increase of around 2.5 percent.

A slowdown in the economy of the euro area had become somewhat more evident. The pace of increase in business fixed investment had decelerated. Exports had been on a moderate uptrend, but survey results continued to suggest that their growth was likely to slow. In addition, housing investment had been on a declining trend, and private consumption had been more or less unchanged reflecting the rise in energy and food prices and uncertainty about the outlook for the economy. As for prices, the year-on-year rate of increase in the Harmonized Index of Consumer Prices (HICP) remained at a high level, reflecting the continuing rise in energy and food prices. The U.K. economy had been decelerating mainly due to significant adjustments in the housing market.

In China, both domestic and external demand continued to expand strongly. India's economy continued to show relatively high growth, although it was slowing moderately. The NIEs and ASEAN economies had so far continued to expand at a moderate pace supported by firm growth in domestic demand although exports continued to decelerate. However, some signs of a slowdown in domestic demand had been observed recently in the NIEs and ASEAN economies. As for prices, the year-on-year rate of increase in the CPI for all items had risen in many Asian economies due to the rise in energy and food prices.

Global financial markets remained unstable due mainly to concerns about further losses that U.S. and European financial institutions might incur and about the possibility of a further slowdown of the world economy. Adjustments in markets for securitized products had continued, and credit spreads had been at high levels. In the U.S. and European financial markets, stock prices had risen, mainly reflecting the decline in crude oil prices. U.S. long-term interest rates had risen slightly mainly reflecting the rise in stock prices, although they declined temporarily due partly to weakening of market expectations of a rate increase by the Federal Reserve. European long-term interest rates had fallen due in part to deterioration in the market's view of the economy and weakening of market expectations that the European Central Bank (ECB) would raise its key interest rates. Monetary policy had been tightened in many emerging economies due to increased inflationary pressures.

D. Economic and Financial Developments in Japan

1. Economic developments

The pace of increase in exports had slowed. Growth in exports was expected to remain only modest for the time being, due to the slowdown in overseas economies.

In relation to domestic private demand, corporate profits had been decreasing mainly due to the deterioration in the terms of trade, and business fixed investment had been leveling off. Growth in business fixed investment was likely to remain sluggish for the time being, as corporate profits were expected to continue decreasing.

Private consumption had been relatively weak, mainly due to sluggish growth in household income and the increase in prices of petroleum products and food. Sales of electrical appliances had continued to increase steadily, assisted by strong sales of digital appliances such as flat-panel televisions, but the growth in the number of new passenger-car registrations had been sluggish partly due to high gasoline prices. Sales at department stores had declined, and those at supermarkets had been relatively weak. As for services consumption, outlays for travel, especially overseas travel, had also been weak recently partly due to increases in fuel surcharges added to airfares, while growth in sales in the food service industry had continued to be sluggish. Consumer sentiment had become more cautious as a result of the continued rises in prices of petroleum products and food. Growth in private consumption was likely to be sluggish for the time being, as household income was expected to remain more or less flat and prices were likely to continue rising.

The recovery in housing investment had stalled. The number of housing starts, a leading indicator of housing investment, continued to pick up until January 2008, but this recovery had since stalled. This seemed to be mainly due to the softness in sales of condominiums and further increases in prices of structural steel. Housing investment was expected to be more or less flat for the time being, given the stalling of housing starts.

Production had been relatively weak and, in light of developments in demand both at home and abroad, was expected to remain relatively weak for the time being. Inventories had risen somewhat as shipments had been relatively weak, and the shipment-inventory balance had accordingly deteriorated slightly.

As for employment and income, growth in household income had recently been sluggish. The year-on-year rate of increase in nominal wages per worker had declined. Household income was projected to remain more or less level.

On the price front, commodity prices remained elevated, although they had lately fallen back somewhat. The three-month rate of increase in the domestic corporate goods price index (CGPI) had been high, mainly due to the rise in commodity prices. It was likely to continue to be positive for the time being, with the effects of the rise in commodity prices remaining, but the pace of increase was likely to slow. The year-on-year rate of increase in the CPI (excluding fresh food) was around 2 percent. It was expected to be somewhat higher over the coming months but to moderate gradually thereafter, reflecting developments in prices of energy and food.

2. Financial environment

The environment for corporate finance was accommodative on the whole. Credit demand in the private sector had been increasing moderately. Issuing conditions for CP and corporate bonds had been favorable as a whole, although they had tightened for firms with low credit ratings and in some industries. The lending attitudes of private banks had continued to be generally accommodative, and the amount outstanding of lending by private banks, notably to large firms, had been increasing, although that of lending to small firms had been below the previous year's level. Funding costs for firms had remained more or less unchanged. The financial positions of firms as a whole had continued to be favorable, but those of small firms had deteriorated somewhat. The year-on-year rate of growth in the money stock (M2) was around 2 percent.

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

A. Economic Developments

Members agreed on the following assessment of <u>the current state of Japan's economy</u>: economic growth had been sluggish against the backdrop of high energy and materials prices and weaker growth in exports; while growth would likely remain sluggish for the time being, the economy was unlikely to experience a significant downturn, as there was no excess in production capacity and labor, and was expected to return gradually onto a moderate growth path as commodity prices leveled out and overseas economies moved out of their deceleration phase.

Members agreed that, although <u>overseas economies</u> taken as a whole had been expanding, the pace of growth was slowing and downside risks remained elevated, mainly reflecting the disruptions in global financial markets and sluggish growth in the U.S. economy.

Members shared the view that global financial markets remained unstable due mainly to concerns about further losses that U.S. and European financial institutions might incur and to growing concerns about the outlook for the world economy. Some members said that attention should be paid to possible further losses that U.S. financial institutions might incur, resulting for example from increases in reserves for credit losses due to an increase in consumer loan delinquencies and a decline in commercial real estate prices and from buybacks of auction rate securities (ARSs).

Members concurred that growth in the U.S. economy had remained sluggish. One member said that, in the housing market, some positive developments had been observed, such as an increase in the number of regions where home prices had risen. However, a few other members were of the view that home prices continued to be on a substantial decline on the whole, and there were no signs of the housing market bottoming out. As for the outlook, some members expressed the view that the period of sluggishness in the U.S. economy might be prolonged mainly due to the abatement of the effects of tax rebates, which had boosted private consumption, a further decline in home prices, a more cautious stance among financial institutions on lending, and a slowdown in the world economy. Based on these assessments, members agreed that there was considerable uncertainty regarding when and how the negative feedback loop between financial markets, asset prices, and economic activity would diminish.

With regard to European economies, members shared the view that a slowdown in the economy of the euro area had become somewhat more evident. Many members were of the view that in addition to the sluggish economic activity in Spain and Italy, a slowdown in domestic and external demand of the German economy had become evident. One of these members expressed the view that the negative effects of the sluggishness of the U.S. economy were spreading to European economies.

On Asian economies, members concurred that, while China and India continued to show high growth, in the NIEs and ASEAN economies the pace of growth in exports had been slowing and there had been signs of a slowdown in domestic demand against the backdrop of the rise in energy and food prices. Some members said that China might to some degree ease its macroeconomic policy stance of restraining the overheating of the economy, reflecting deterioration in business performance of exporters. These members also said that inflationary pressures there remained strong and, therefore, future developments in economic activity and prices in the Chinese economy warranted close monitoring.

Regarding global price developments, members agreed that global inflationary pressures remained high, reflecting elevated commodity prices, particularly crude oil prices. A few members said that, reflecting moves to regulate futures markets and the deceleration of the world economy, crude oil prices had been declining recently and consequently there had appeared a view in markets that concerns about global inflation had subsided somewhat. On the other hand, some members expressed the view that crude oil prices were unlikely to decline greatly, given that the prolonged rise in crude oil prices reflected stronger demand for crude oil relative to supply, mainly from emerging economies. One member added that attention should continue to be paid to the risk that inflationary pressures might increase further globally, as financial conditions worldwide remained accommodative.

Members concurred that the pace of increase in Japan's exports had slowed, and that growth in exports was likely to remain only modest for the time being, due to the slowdown in overseas economies. A few members expressed the view that the recent slowing of Japan's export growth reflected the deceleration of the world economy. One member said that attention should be paid to the effects on Japan's exports of the more pronounced slowdown in European economies and of the weakness in domestic demand in Asian economies.

In relation to domestic private demand, members agreed that corporate profits had been decreasing mainly due to the deterioration in the terms of trade, and business fixed investment had been leveling off. They also concurred that growth in business fixed investment was likely to remain sluggish for the time being, as corporate profits were likely to continue decreasing. Some members, however, noted that firms' capital stock did not seem to be excessive. Also, some members remarked that some large firms had been taking a positive attitude toward investment aimed at, for example, energy and resource saving, responding to the new relative-price structure. On the other hand, some members expressed the view that small firms' appetite for fixed investment had weakened as a result of a decrease in their profits due to the rise in energy and materials prices.

Members concurred that private consumption had been relatively weak against the background of the continued increase in prices of petroleum products and food. Some members said that the rise in prices had reduced households' real purchasing power, and this had made household spending behavior cautious. Members concurred that growth in private consumption was likely to be sluggish for the time being, as it was likely that household income would remain more or less flat and prices would continue rising.

As for employment and income, members shared the view that growth in household income had recently been sluggish and that it was likely to remain more or less level for some time. One member noted that firms were restraining labor costs further as part of their moves to cut back spending. A different member expressed the view that labor market conditions had been gradually weakening, reflecting the sluggish growth of the economy. Some members noted, however, that there had been no signs of excess in employment.

Members concurred that the recovery in housing investment had stalled, and housing investment was likely to be more or less flat for the time being.

Members agreed that production had been relatively weak and was likely to remain so for the time being. A few members said that future developments required close monitoring, as the index of industrial production declined in the April-June quarter for the second consecutive quarter, and the projected figures for July and August suggested negative growth. One member expressed the view that attention should be paid to the risk of unintended accumulation of inventories, mainly of IT-related goods.

As for prices, members said that the three-month rate of increase in the CGPI had been high, mainly due to the rise in commodity prices, and that, with the effects of the rise in commodity prices remaining, the CGPI was likely to continue increasing for the time being, but the pace of increase was likely to slow.

Members concurred that the year-on-year rate of increase in the CPI (excluding fresh food) was rising mainly due to the rise in prices of petroleum products and food, and that the CPI inflation rate was likely to be somewhat higher over the coming months but to moderate gradually thereafter. As in previous meetings, members exchanged views regarding the effects on general prices of the rise in energy and materials prices. A few members expressed the view that whether or not second-round effects had emerged should be assessed based on points such as the following: whether the rise in general prices had been contained within the extent of the pass-through of increases in energy and materials prices and whether a wage-price spiral had started to appear. Many members then said that there had been no signs of second-round effects to date, as evidenced by the fact that (1) firms had not raised their sales prices to an extent exceeding increases in input costs, although they continued to pass higher costs on to sales prices; and (2) wages remained level. As the background to this, one of these members raised the following points: the economy was not overheated, unlike at the time of the first oil crisis; this assessment was supported by various data and other information; and the labor market had become flexible. This member added, however, that the current rise in energy and materials prices was characterized by a long-term upward trend against the background of the worldwide growth in demand, especially demand from emerging economies, and that attention to the risk that possible changes in inflation expectations of firms and households would generate such effects should not be slackened merely because second-round effects had not emerged so far. A different member also said that, given the accommodative financial conditions worldwide, attention to inflationary risks should not be relaxed just because crude oil prices had been declining recently and there had been no signs of a wage-price spiral developing. Based on these discussions, one member said that although it was difficult to accurately detect emergence of second-round effects, the Bank should continue to carefully assess the price situation, examining various data and other information.

B. Financial Developments

Members concurred that financial conditions in Japan remained accommodative on the whole. They also agreed that issuing conditions for CP and corporate bonds had been favorable as a whole, although they had tightened for firms with low credit ratings and in some industries, and that the lending attitudes of financial institutions had been generally accommodative. A few members noted, however, that the number of bankruptcies of construction and real estate firms had been increasing and conditions for corporate bond issuance by them had been deteriorating. One member said that the environment for small firms' financing -- for example, the lending attitudes of financial institutions to them -- was becoming more severe, and future developments required careful monitoring.

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

Based on the above discussions on economic and financial developments, members shared the following view: (1) Japan's economic growth had been sluggish against the backdrop of high energy and materials prices and weaker growth in exports; (2) while growth would likely remain sluggish for the time being, there was no excess in production capacity and labor, and the economy was expected to return gradually onto a moderate growth path as commodity prices leveled out and overseas economies moved out of their deceleration phase; and (3) the CPI inflation rate (excluding fresh food) was currently around 2 percent due to the rise in prices of petroleum products and food, and was expected to be somewhat higher over the coming months but to moderate gradually thereafter. Based on the discussion, members made an assessment in terms of the first perspective, that is to say, they assessed the most likely outlook for economic activity and prices. They agreed that the probability of Japan's economy returning onto a sustainable growth path with price stability was relatively high. One member was of the opinion that the likelihood of Japan's economy experiencing a deep adjustment phase was small because there was no excess in production capacity and labor. A different member expressed the view that the accommodative financial environment would continue to support Japan's economic growth. Meanwhile, a few members said that a slowdown in European and Asian economies had become clear since the previous meeting, and this had caused deceleration in export growth and a decrease in production in Japan. One member was of the view that the growth prospects for Japan's economy had shifted downward compared with those presented in July's interim assessment of the April 2008 *Outlook for Economic Activity and Prices*.

Members then made an assessment in terms of the second perspective, that is to say, they examined the risks that they considered most relevant to the conduct of monetary policy, including risks that had a longer time horizon than the first perspective. Regarding economic developments, members shared the following view: (1) global financial markets remained unstable as evidenced by the high levels of various credit spreads and continued instability in stock prices, both of which reflected concerns about further losses that U.S. and European financial institutions might incur and about the outlook for economies worldwide; (2) there were downside risks to the world economy, mainly reflecting sluggish growth in the U.S. economy; (3) weaker income generation reflecting developments in commodity prices could potentially weigh on domestic private demand; and (4) although the economy was under no pressure to adjust production capacity and labor, downside risks to the economy demanded attention. As for prices, members agreed on the following view: (1) global inflationary pressures remained high given the high commodity prices, particularly crude oil prices; and (2) in Japan, it was necessary to be mindful of upside risks to inflation due to changes in, for example, the inflation expectations of households and the price-setting behavior of firms in addition to developments in energy and materials prices. A few members were of the opinion that, if the downside risks to the economy turned out to decrease, there would be an increased risk that prolonging the period of accommodative financial conditions would lead to swings in economic activity and prices. In relation to this, one member said that the Bank should continually examine whether the level of the policy interest rate was appropriate, employing various methods, for instance, assessing the relationship between the real interest rate and the potential growth rate. A few members expressed the view that attention should continue to be paid to inflationary risks because energy and materials prices were on a long-term upward trend against the background of the growth in demand, especially demand from emerging economies, and also because financial conditions had been accommodative worldwide. A few other members commented that downside risks to the economy had further increased recently. One of these members added that the risk that the economy might return onto a growth path later than expected also warranted attention. Based on the discussion, members agreed that, in conducting monetary policy, the Bank should continue to pay attention to both downside risks to economic growth and upside risks to inflation.

On the guideline for money market operations for the intermeeting period ahead, members agreed that, given the assessment of economic activity and prices described above, it would be appropriate to maintain the current guideline that the Bank would encourage the uncollateralized overnight call rate to remain at around 0.5 percent.

Members concurred that the following thinking on the monetary policy stance for the future remained unchanged: the Bank, while maintaining the smooth functioning of the money market, would carefully assess the future outlook for economic activity and prices, closely considering the likelihood of its projections materializing as well as factors posing upside or downside risks, and would implement appropriate policies in an accordingly flexible manner.

IV. Remarks by Government Representatives

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

(1) Japan's economy was weakening recently due to the surge in crude oil and food prices and the slowdown in the global economy, particularly the U.S. economy. It was expected to remain weak for the time being. Prices, especially those related to crude oil and food, were rising due mainly to higher prices of imported materials, and this was reflected in both domestic corporate goods prices and consumer prices. At the same time, attention should be paid to the following factors: (1) wage growth had decelerated; and (2) the rise in materials prices was likely to level off as suggested by the recent drop in crude oil prices in the futures markets.

(2) The government would promptly present an overall picture of comprehensive measures for pursuing life security in order to respond to the worldwide surge in crude oil and food prices and to concerns about possible further deterioration of the economy.

(3) The government would like the Bank to continue to support the economy from the financial side taking into account the economic situation mentioned above.

(4) The government would also like the Bank to continue to clearly explain to the public and market participants its view on economic activity and its thinking on the conduct of monetary policy.

The representative from the Cabinet Office made the following remarks.

(1) Japan's economy was weakening recently, mainly because exports were weakening and production was decreasing. The economy was likely to remain weak for the time being, and it might weaken further, depending mainly on future developments in the U.S. economy, stock prices and exchange rates, and crude oil prices. Consumer prices and the domestic demand deflator had risen, while the pace of decrease in the GDP deflator had accelerated. Close attention should therefore be paid to developments in prices, together with those in economic activity.

(2) Given the recent economic situation, for example the surge in crude oil and food prices, the government had been working to formulate comprehensive measures for pursuing life security. It would promptly present an overall picture of the measures and implement them step by step, without delay.

(3) In order to ensure sustainable economic growth led by private demand and achieve a

stable inflation rate, it was important for the government and the Bank to implement their policies based on the shared basic perspective on macroeconomic management.

(4) The government would like to request the Bank to implement monetary policy in a timely and appropriate manner that was consistent with the government's policy efforts and its outlook for the economy, and to firmly support the economy from the financial side in view of downside risks to the outlook for the economy.

V. Votes

Based on the above discussions, 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 0.5 percent.

To reflect this 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:

1. The guideline for money market operations for the intermeeting period ahead will be as follows.

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

2. A public statement will be decided separately.

Votes for the proposal: Mr. M. Shirakawa, Mr. K. G. Nishimura, Ms. M. Suda, Mr. A. Mizuno, Mr. T. Noda, Mr. S. Nakamura, and Mr. H. Kamezaki.

Votes against the proposal: None.

VI. Discussion on the Public Statement "Statement on Monetary Policy"

Members discussed the "Statement on Monetary Policy," and put it to the vote. The Policy Board decided the text by a unanimous vote. It was confirmed that the statement would be released immediately after the meeting (see Attachment).

VII. Approval of the Minutes of the Monetary Policy Meeting

The Policy Board approved unanimously the minutes of the Monetary Policy Meeting of July 14 and 15, 2008 for release on August 22, 2008.

Attachment

August 19, 2008

Bank of Japan

Statement on Monetary Policy

1. At the Monetary Policy Meeting held today, the Bank of Japan decided, by a unanimous vote,[Note] 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 0.5 percent.

2. Economic growth has been sluggish against the backdrop of high energy and materials prices and weaker growth in exports. While growth will likely remain sluggish for the time being, it is expected to return gradually onto a moderate growth path as commodity prices level out and overseas economies move out of their deceleration phase. The CPI inflation rate (excluding fresh food) is currently around 2 percent, highest since the first half of 1990s, due to increased prices of petroleum products and food. It is expected to be somewhat higher over the coming months but to moderate gradually thereafter. Thus it is likely that the economy will return onto a sustainable growth path with price stability.

3. With regard to risk factors, global financial markets remain unstable and there are downside risks to the world economy, particularly the U.S. economy. In addition, weaker income generation reflecting developments in commodity prices could

[Note] Voting for the action: Mr. M. Shirakawa, Mr. K. G. Nishimura, Ms. M. Suda, Mr. A. Mizuno, Mr. T. Noda, Mr. S. Nakamura, and Mr. H. Kamezaki.
Voting against the action: None.

potentially weigh on domestic private demand. Although the economy is under no pressure to adjust production capacity and labor, these downside risks to the economy demand attention. On prices, global inflationary pressures remain high. In Japan, it is necessary to be mindful of upside risks due to changes in the inflation expectations of households and the price-setting behavior of firms in addition to developments in energy and materials prices. Meanwhile, if the downside risks to the economy turn out to decrease, there will be an increased risk that prolonging the period of accommodative financial conditions will lead to swings in economic activity and prices.

4. The Bank, while maintaining the smooth functioning of the money market, will carefully assess the future outlook for economic activity and prices, closely considering the likelihood of its projections as well as factors posing upside or downside risks, and will implement its policies in an accordingly flexible manner.