

Not to be released until 8:50 a.m.
Japan Standard Time on Thursday,
November 27, 2008.

November 27, 2008

Bank of Japan

Minutes of the Monetary Policy Meeting

on October 14, 2008

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

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Secretariat of the Policy Board, Bank of Japan

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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 Tuesday, October 14, 2008, from 8:30 p.m. to 9:34 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

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

Reporting Staff

Mr. H. Yamaguchi, Executive Director

Mr. K. Yamamoto, Executive Director

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

Mr. M. Ayuse, Associate Director-General, Monetary Affairs Department

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

¹ The minutes of this meeting were approved by the Policy Board at the Monetary Policy Meeting held on November 20 and 21, 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.

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

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

Mr. T. Sakamoto, Director, Head, Monetary Operations Planning, Monetary Affairs Department

Mr. Y. Nakaone, Director, Deputy Head, Monetary Operations Planning, Monetary Affairs Department

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

I. Remarks on the Purpose of the Unscheduled Monetary Policy Meeting

The chairman first explained the reason for calling the unscheduled Monetary Policy Meeting as follows.

- (1) Strains in global financial markets stemming from the subprime mortgage problem had increased further. At the Group of Seven (G-7) meeting held on October 10, the G-7 Finance Ministers and Central Bank Governors Plan of Action was finalized, and countries around the world had been introducing series of measures, for example, measures to enable financial institutions to raise capital from public sources.
- (2) In this situation, central banks in major economies had been introducing various measures to provide liquidity. The Bank of Japan announced on October 8 that it would examine possible ways to enhance the effectiveness of monetary operations. In the joint statement released on October 13, the Federal Reserve in the United States and three European central banks announced that they would conduct tenders of U.S. dollar funding at fixed interest rates and permit counterparties in these operations to borrow any amount they wished against the appropriate collateral. The Bank of Japan announced that it would be considering the introduction of similar measures.
- (3) One appropriate response by the Bank to the situation would be to introduce measures to enhance the effectiveness of money market operations, in order to facilitate them and maintain the smooth functioning of the money market as well as ensure stability in financial markets.

II. Summary of Staff Reports on Financial Market Developments

With regard to recent global financial market developments, the staff reported that stock prices had dropped substantially in Japan, the United States, and Europe, but had surged recently. Long-term interest rates had been rising with large fluctuations. In foreign exchange markets, appreciation of the yen and the U.S. dollar as well as depreciation of the euro continued, but there had been some movement in the opposite direction in each currency recently. In credit markets, U.S. and European corporate bond spreads had expanded widely particularly in the financial sector, and credit default swap (CDS) premiums continued to be elevated. In U.S. dollar funding markets, interest rates on overnight instruments had been fluctuating considerably and those on term instruments remained at an elevated level. U.S. dollar Libor-OIS spreads remained significantly

widened. Liquidity in foreign exchange swap markets was low, and there continued to be intense funding strains in markets for U.S. dollar funds maturing beyond the year-end.

In Japanese financial markets, repo transactions continued to be difficult, and repo rates remained at an elevated level. Distortion in Japanese government securities (JGS) markets had increased, particularly in the inflation-indexed bond and floating-rate bond markets, due partly to the decline in the functioning of the repo market. In the CP market, credit spreads between JGSs and CP at issuance were on a widening trend. With regard to asset-backed commercial paper (ABCP), most of it had been issued with backup lines of credit provided by private banks.

III. Summary of Staff Reports on Measures to Enhance the Effectiveness of Money Market Operations

In view of recent developments in financial markets at home and abroad, the staff reported that they would make the following adjustments to the Bank's money market operations, in addition to proposing measures that required approval at the Monetary Policy Meeting (see Section IV below).

First, as a measure to improve liquidity in the Japanese government bond (JGB) repo market, the Bank would lower the minimum fee rates applied to its securities lending facility from 1 percent to 0.5 percent as a temporary measure that would apply through January 16, 2009. Second, as a measure to facilitate corporate financing in the market, the Bank would increase the frequency and the size of CP repo operations. And third, the Bank would work to ensure that sufficient funds maturing beyond the year-end would be available by starting its operations to supply such funds at an earlier date.

IV. Staff Proposal of Introduction of Measures to Enhance the Effectiveness of Money Market Operations That Required Approval at the Monetary Policy Meeting

Against the background of recent developments in global financial markets, liquidity pressures in U.S. dollar short-term funding markets remained intense. In Japanese financial markets, liquidity had declined in the JGB repo market, and corporate financing via the markets had become somewhat difficult for certain firms. In this situation, the staff would like to propose that the Bank take the necessary steps to introduce

measures to adjust its money market operations with a view to safeguarding stability in Japanese financial markets as well as facilitating money market operations. First, the Bank should amend the Principal Terms and Conditions for the Purchase/Sale of Japanese Government Securities with Repurchase Agreements to expand the range of JGBs eligible for its repo operations by adding floating-rate bonds, inflation-indexed bonds, and 30-year bonds to the list of eligible JGBs. Second, the Bank should establish the Temporary Rules regarding Eligibility Standards for Asset-Backed Commercial Paper and Dematerialized Asset-Backed Commercial Paper to temporarily broaden the range of eligible ABCP by accepting debt obligations guaranteed by the Bank's counterparty financial institutions as collateral. And third, the Bank should amend the Principal Terms and Conditions for U.S. Dollar Funds-Supplying Operations against Pooled Collateral to introduce U.S. dollar funds-supplying operations whereby an unlimited amount of funds would be provided at a fixed rate set for each operation against pooled collateral.

The Bank announced on October 8, 2008 that it would "swiftly examine possible ways to further enhance the effectiveness of monetary operations," and the staff was therefore proposing a set of measures that required approval at the Monetary Policy Meeting, while measures pertaining to the Bank's reserve system were under review.

V. Summary of Discussions by the Policy Board

A. Discussions on the Staff Proposal

Members first discussed recent developments in financial markets, and confirmed that issues had arisen in the following areas: liquidity in the JGB repo and CP markets; availability of funds maturing over the year-end; and liquidity in short-term U.S. dollar funding markets. Members concurred that it was necessary that the Bank, as a central bank, take appropriate measures to address these issues. Members then discussed the efficacy of and the points to be aware of in each of the following proposed measures: expansion of the range of JGBs eligible for the Bank's repo operations; broadening of the range of ABCP eligible as collateral; and introduction of further measures to enhance U.S. dollar funds-supplying operations against pooled collateral. The discussion concluded with members in agreement that it would be appropriate to approve the staff proposal.

Regarding the proposed expansion of the range of JGBs eligible for the Bank's repo operations, one member said that it would be necessary to clearly explain that it was

different in nature from the expansion of the range of those eligible for its outright purchases. Another member said that in order to maintain the soundness of the Bank's assets, the broadening of the range of eligible ABCP should be introduced as a temporary measure as in the staff proposal. Regarding the proposed introduction of an auction method that would provide U.S. dollar funds at a fixed rate, one member commented that, although there was a possibility that it might impair the proper functioning of the market mechanism, it would be necessary in order to address the issue of U.S. dollar liquidity. Another member said that it would be appropriate to adopt the auction method that would provide funds at a fixed rate, so that U.S. dollar funding in the Tokyo market would not be disadvantageous compared with funding in the U.S. and European markets. One member also pointed out that the Bank should swiftly review its reserve system.

B. Discussions on Monetary Policy for the Immediate Future

The Policy Board decided at the previous Monetary Policy Meeting held on October 6 and 7, 2008 to maintain the current guideline for money market operations that the Bank would encourage the uncollateralized overnight call rate to remain at around 0.5 percent. Since an unscheduled Monetary Policy Meeting was being held today, it was necessary for the Policy Board to once again decide the guideline for money market operations for the intermeeting period. Members agreed that it would be appropriate to maintain the current guideline until the next Monetary Policy Meeting to be held on October 31, 2008, as only a limited number of economic and price indicators had been released since the previous meeting and it would be appropriate to hold thorough discussions on economic and price situation at the next meeting, closely examining the various indicators to be released toward the end of October.

VI. Remarks by Government Representatives

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

- (1) In the statement released on October 8, the Bank announced that it would examine "possible ways to further enhance the effectiveness of monetary operations" in response to the current financial crisis.
- (2) In addition, at the G-7 meeting held on October 10, finance ministers and central bank governors agreed that they would "take all necessary steps." The government

considered that these commitments had been received very positively so far by the market in each of the G-7 countries.

- (3) The government would respect the Bank's decision at this meeting, since the measures proposed would be introduced based on the result of further deliberations at the Bank following the October 8 statement and on the G-7 agreement.

The representative from the Cabinet Office made the following remarks.

- (1) The government welcomed the measures proposed at this meeting as they would be timely and appropriate measures that were also in line with the G-7 Finance Ministers and Central Bank Governors Plan of Action released on October 10.
- (2) Given the rapid changes in financial markets, the government would like to continue to monitor carefully developments in financial markets worldwide as well as their effects on the Japanese economy, and would respond appropriately to the situation.
- (3) The government would like to request the Bank to continue to implement monetary policy in a timely and appropriate manner, and to firmly support the economy from the financial side in view of the current severe economic situation.

VII. Votes

A. Vote on Amendments to the Principal Terms and Conditions for the Purchase/Sale of Japanese Government Securities with Repurchase Agreements

Members voted unanimously to approve the staff proposal and agreed that the decision should be made public.

B. Vote on the Guideline for Money Market Operations

To reflect the view of members, 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 0.5 percent.

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.

VIII. Timing for Approval of the Minutes of the Monetary Policy Meeting

The Policy Board discussed when to approve the minutes of this unscheduled meeting, as the Rules concerning Policy Board Meetings stipulated that the Policy Board should approve the minutes of Monetary Policy Meetings at the first subsequent meeting. The Policy Board then decided to approve the minutes of this meeting at the Monetary Policy Meeting to be held on November 20 and 21, 2008 and release them after the meeting, instead of approving them at the first subsequent meeting on October 31, 2008, taking into account practical constraints due to the shortness of the intermeeting period ahead. The Policy Board also confirmed that, as had been previously announced, they would approve the minutes of both the previous unscheduled meeting held on September 29, 2008 and the scheduled meeting on October 6 and 7 at the meeting on October 31, 2008 and release them after the meeting.

Attachment

October 14, 2008

Bank of Japan

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.

^[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.