Not to be released until 8:50 a.m. Japan Standard Time on Friday, June 19, 2009.

June 19, 2009

Bank of Japan

Minutes of the Monetary Policy Meeting

on May 21 and 22, 2009

(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 Thursday, May 21, 2009, from 2:00 p.m. to 4:14 p.m., and on Friday, May 22, from 9:00 a.m. to 12:28 p.m.[1]

Policy Board Members Present

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

Mr. H. Yamaguchi, Deputy 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. A. Horii, Executive Director (Assistant Governor)

Mr. K. Ido, Executive Director

Mr. H. Nakaso, Executive Director

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

Mr. M. Ayuse, Associate Director-General, Monetary Affairs Department[4]

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[1] The minutes of this meeting were approved by the Policy Board at the Monetary Policy Meeting held on June 15 and 16, 2009 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 May 22.

[3] Mr. C. Kawakita was present on May 21.

[4] Mr. M. Ayuse was present on May 22 from 9:00 a.m. to 9:26 a.m.

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

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

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. Y. Iino, 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. T. Sakamoto, Director, Head, Monetary Operations Planning, Monetary Affairs Department[5]

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

Mr. R. Hattori, Senior Economist, Monetary Affairs Department

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[5] Mr. T. Sakamoto was present on May 22 from 9:00 a.m. to 9:26 a.m.

I. Summary of Staff Reports on Economic and Financial Developments[6]

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 April 30, 2009.[7] The uncollateralized overnight call rate had been at around 0.1 percent.

With a view to ensuring market stability, the Bank continued to conduct money market operations in a flexible manner in response to changes in the market situation, as evidenced by its active purchases of Japanese government securities (JGSs) and CP under repurchase agreements. The Bank also continued to conduct outright purchases of CP and corporate bonds, special funds-supplying operations to facilitate corporate financing, and U.S. dollar funds-supplying operations against pooled collateral.

B. Recent Developments in Financial Markets

Upward pressure on interest rates in Japan's money market was moderating, but the market had remained nervous as seen in the continuation of low market liquidity and insufficient arbitrage across markets. General collateral (GC) repo rates and yields on government bills had been more or less unchanged, but they had remained sensitive to changes in the balance between supply and demand in the markets. Euroyen rates had been on a moderate downward trend, but they had remained at a relatively elevated level, particularly those on term instruments with longer maturities, amid the continued lower volume of transactions. In the CP market, investors had remained highly selective about the issues they purchased, but issuing conditions had been relatively stable due mainly to a decline in firms' demand for liquidity, and issuance rates on CP with high ratings had been below the TIBOR rates.

Japanese stock prices remained unstable, fluctuating daily in response to changes in market sentiment about world economic growth and the stability of the global financial system. The Nikkei 225 Stock Average had been moving in the range of 9,000-9,500 yen recently. Long-term interest rates in Japan had been more or less unchanged, moving in

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[6] Reports were made based on information available at the time of the meeting.

[7] The guideline was as follows:

The Bank of Japan will encourage the uncollateralized overnight call rate to remain at around 0.1 percent.

the 1.40-1.45 percent range recently.

The yen temporarily depreciated against the U.S. dollar, but appreciated thereafter and had recently been at around 95 yen to the dollar.

C. Overseas Economic and Financial Developments

U.S. economic conditions had continued to deteriorate significantly. Home prices continued to be on a declining trend, and housing investment and business fixed investment had been contracting noticeably. Private consumption had been on a downward trend, but the pace of decrease was moderating. In this situation, production had been decreasing, and inventory adjustments were making progress. In the labor market, the number of employees had continued to decline considerably, and the unemployment rate had been rising. Funding conditions for firms and households had remained tight. As for prices, the year-on-year rate of change in the consumer price index (CPI) for all items had been negative for two months in a row, as food prices had remained more or less unchanged and energy prices had been low. The year-on-year rate of increase in the CPI for all items less energy and food, or the core CPI, had been in the range of 1.5-2.0 percent.

Economic conditions in the euro area had continued to deteriorate significantly. Private consumption, business fixed investment, and housing investment had decreased. Exports had continued to decline, but the pace of decline was slowing. As for prices, the year-on-year rate of increase in the Harmonized Index of Consumer Prices (HICP) had declined. Economic conditions in the United Kingdom had also continued to deteriorate significantly, mainly reflecting the ongoing considerable adjustments in the housing market and a declining trend in private consumption.

In China, the deceleration of the economy taken as a whole had come to a halt: although exports had declined, domestic demand continued to show high growth. Economic conditions in the NIEs and the ASEAN countries had continued to deteriorate, but the pace of decrease in exports and production was moderating. Meanwhile, economic growth in India had decelerated significantly. As for prices, the year-on-year rate of increase in the CPI had been on a declining trend in many Asian economies.

Global financial markets remained under strain, although conditions had improved somewhat. Treasury-Eurodollar (TED) spreads and credit spreads on CP had generally decreased to their levels before the failure of Lehman Brothers Holdings Inc. On the other hand, credit spreads on corporate bonds remained at high levels, even though they had decreased on the whole. U.S. and European stock prices had increased, reflecting the view that uncertainty about the financial soundness of financial institutions had diminished following the release of the results of stress tests of the largest U.S. bank holding companies. U.S. and European long-term interest rates had risen somewhat due partly to expectations for a bottoming out of the economy.

D. Economic and Financial Developments in Japan

1. Economic developments

Exports had decreased substantially since fall 2008, mainly due to the deterioration in overseas economic conditions, but they were beginning to level out due to the waning of adjustment pressures on local inventories. They were expected to level out and start recovering, mainly due to progress in adjustments in local inventories.

Public investment had begun to turn upward, mainly reflecting the implementation of the supplementary budgets for fiscal 2008. It was likely to continue increasing for the time being, due to the implementation of various economic measures.

With regard to domestic private demand, business fixed investment had declined substantially, reflecting the significant deterioration in corporate profits. It was likely to continue declining for the time being, given the severe situation in corporate profits and firms' funding and the strong sense of excessive capital stock among firms.

Private consumption had weakened, as the employment and income situation had become increasingly severe. There had been a relatively large decrease in sales at department stores, reflecting further curtailment of purchases by consumers. Sales at supermarkets had also been relatively weak in general. On the other hand, the number of new passenger-car registrations recovered slightly, partly as a result of the implementation of the reduction in automobile taxes. Meanwhile, indicators of consumer sentiment had recovered slightly due to expectations of positive effects from various demand-boosting policy measures and to the decline in retail prices, notably gasoline prices. As the employment and income situation was likely to become increasingly severe, private consumption was likely to remain relatively weak for the time being, although it was expected to be supported by the positive effects of various measures and by the decline in prices.

Housing investment had decreased. It was expected to continue decreasing for the time being, given the sluggishness in housing starts.

Production had decreased substantially since fall 2008, but the decrease was coming to a halt, mainly due to the waning of adjustment pressures on inventories both at home and abroad. It was expected to level out and start recovering as inventory adjustments both at home and abroad progressed further.

The employment and income situation had become increasingly severe, with the labor market slackening substantially and household income decreasing noticeably. Household income was likely to continue declining for the time being due to lagged effects of the earlier substantial decrease in corporate profits and production.

On the price front, commodity prices, which peaked in summer 2008 and dropped substantially thereafter, had recently risen gradually. The three-month rate of change in the domestic corporate goods price index (CGPI) had continued to be negative due to the earlier fall in international commodity prices and the easing of supply and demand conditions for products, but the pace of decline in the CGPI had been moderating. The CGPI was likely to continue decreasing gradually for the time being, as supply and demand conditions for products were likely to remain slack. The year-on-year rate of increase in the CPI (excluding fresh food) had declined to around 0 percent, reflecting the declines in the prices of petroleum products and the stabilization of food prices. It was expected to become negative, mainly due to the above factors and also to increasing slackness in supply and demand conditions in the overall economy.

2. Financial environment

Financial conditions had remained tight, although there had been some easing of tension compared to some time ago. The overnight call rate had remained at an extremely low level. It seemed that firms' funding costs, after declining at the beginning of 2009, had remained more or less unchanged at low levels. However, the stimulative effects from low interest rates had been limited given that economic activity and corporate profits had continued to deteriorate. The amount outstanding of bank lending, especially to large firms, had continued to increase rapidly. Funding conditions for CP and corporate bonds had been improving: the decline in issuance of CP had mainly reflected a weakening of firms' demand for additional liquidity, and an increasing number of firms had been issuing corporate bonds. However, issuance of corporate bonds by firms with low credit ratings had remained subdued, and many firms had continued to see their financial positions as weak and lending attitudes of financial institutions as severe. Meanwhile, the year-on-year rate of change in the money stock had risen to around 2.5 percent.

II. Establishment of Collateral Guidelines on Eligible Foreign Bonds

A. Staff Proposal

With a view to ensuring stability in financial markets by further facilitating the Bank's money market operations, since fall 2008 the Bank, among other actions, had expanded the range of eligible collateral. In this process, the Bank, in coordination with other central banks, examined the feasibility of accepting so-called cross-border collateral -- collateral in the form of securities that were denominated in foreign currencies, issued in foreign countries, and located in foreign jurisdictions. Given the current situation, where domestic and overseas financial markets were starting to show some signs of improvement but were still unstable, it would be appropriate for the Bank to temporarily accept bonds issued by foreign governments as eligible collateral for its provision of credit in order to further facilitate money market operations and thereby ensure stability in financial markets. Specifically, bonds issued by the governments of the United States, the United Kingdom, Germany, and France should be accepted, because they had sufficient creditworthiness and marketability and financial institutions were likely to use them as collateral. The staff would like to propose that the Bank take the necessary steps, such as establishment of Collateral Guidelines on Eligible Foreign Bonds, to enable the Bank to accept bonds issued by the four governments as eligible collateral.

B. Discussion by the Policy Board and Vote

Members agreed that accepting cross-border collateral would further facilitate money market operations and thereby ensure stability in financial markets. A few members said that it was important to set haircuts on cross-border collateral at an appropriate level so as to prevent the Bank from being exposed to excessive foreign exchange risks. In response to this, the staff explained that the haircuts to be applied would be set at a sufficiently conservative level, in view of the risk associated with fluctuations in the prices of bonds issued by the four governments and in foreign exchange rates. One member -- while agreeing with the acceptance of cross-border collateral as a temporary measure to deal with the current situation -- was of the view that it might be worth considering making the measure permanent if it turned out to be appropriate to do so. In response to this, the staff said they considered that the acceptance of cross-border collateral should be a temporary measure to supplement collateral denominated in yen and located in Japan, because it entailed various types of risks that did not apply in the case of yen-denominated collateral located in Japan -- foreign exchange risk accompanying denomination in foreign currencies, legal risk due to application of foreign laws, and operational risk emanating from its location in foreign countries.

Based on the above discussion, members voted unanimously to approve the proposal and agreed that the decision should be made public.

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

A. Economic Developments

Members concurred that overseas economic conditions had continued deteriorating as a whole with the adverse feedback loop between financial and economic activity persisting. Many members, however, said that the pace of deterioration had slowed: for example, in some economies, the effects of expansion of fiscal spending had manifested themselves and production had leveled out with the progress in inventory adjustments. As for the outlook for the global economy, members agreed that uncertainty remained high, as an adverse feedback loop between financial and economic activity had been operating around the world and a vicious circle of decrease in production, income, and spending had been continuing.

Many members said that uncertainty about the soundness of the global financial system had diminished somewhat following the release of the results of stress tests of the largest U.S. bank holding companies, as seen in decreases in credit spreads in various financial markets. These members continued, however, that the disposal of financial institutions' impaired assets would take some time in a situation where economic conditions were continuing to deteriorate.

Turning to the U.S. economy, many members concurred that economic conditions had continued to deteriorate significantly with the adverse feedback loop between financial and economic activity operating. Many members said that private consumption had been on a downward trend, as home prices had continued to fall and the employment and income situation had continued worsening, although some positive signs had been seen in housing investment. These members expressed the view that it was difficult to be optimistic about future consumption, as it was likely that the employment and income situation would continue deteriorating and household balance sheets would consequently take some time to improve.

With regard to the economy of the euro area, members shared the view that economic conditions had continued to deteriorate significantly. Some members, however, noted that the pace of decline in exports was slowing. Meanwhile, a few members said that conditions in Central and Eastern European economies, which had remained severe, continued to pose a downside risk to the economy of the euro area as a whole.

Many members expressed the view that the deceleration of the Chinese economy had come to a halt. They noted that fixed asset investment had been growing rapidly due to positive effects produced by the large-scale economic stimulus package and successive monetary easing measures. A few members said that, in the NIEs and the ASEAN countries, the pace of decline in exports and production had been slowing mainly due to progress in inventory adjustments of IT-related goods, although economic conditions, taken as a whole, had been deteriorating.

Based on the above discussion on economic and financial conditions abroad, members discussed the state of Japan's economy. They concurred that economic conditions had been deteriorating, but exports and production were beginning to level out against the backdrop of progress in inventory adjustments both at home and abroad. As for the outlook for the near term, members agreed on the following assessment: although domestic private demand was likely to continue to weaken, exports and production were likely to level out and start recovering as inventory adjustments made further progress both at home and abroad; in addition, public investment was likely to increase; and the pace of deterioration in economic conditions was therefore likely to moderate gradually, leading to a leveling out of the economy. Members also concurred that this view was generally in line with the projection presented in the *Outlook for Economic Activity and Prices* (hereafter the Outlook Report) released at the end of April.

On the impact of the new type of influenza, members shared the view that, despite an increase in the number of confirmed cases of virus infection in Japan as well as negative effects on daily activities and on tourism and service industries in some areas, the outbreak had not yet had a significant impact on Japan's overall economic activity. Members concurred, however, that if the disease spread further and strong countermeasures were taken, such negative effects might become widespread, and this warranted attention.

With regard to the outlook for economic activity in the latter half of fiscal 2009 onward, members agreed that Japan's economy was likely to start recovering with medium- to long-term expectations of future growth generally unchanged, supported partly by the positive effects of measures to stabilize the financial system and of fiscal and monetary policy measures, in addition to a recovery in overseas economies and improvements in conditions in global financial markets. However, members shared the view that the outlook was attended by a significant level of uncertainty, given that economic activity was likely to be strongly affected by developments in overseas economies and global financial markets.

Regarding developments in each demand component, members agreed that exports were beginning to level out with the progress in adjustments in local inventories. They also concurred that exports were likely to level out and start recovering in the near future. Many members, however, said that the outlook for exports thereafter remained highly uncertain, as it depended on developments in final demand overseas.

Some members said that business fixed investment had declined substantially, reflecting the significant decrease in corporate profits, and it was likely to continue declining for the time being. Some members expressed the view that attention should continue to be paid to the risk that business fixed investment might decline further as a result of a possible downward revision of firms' medium- to long-term expectations of future growth. Meanwhile, a different member noted that the pace of decline in machinery orders was moderating.

Many members said that private consumption had weakened as the employment and income situation had become increasingly severe. A few members said that indicators of consumer sentiment had recovered slightly due to expectations of positive effects from various policy measures and to the stabilization of prices. Many members including these members concurred that private consumption was nevertheless likely to remain relatively weak for the time being given the possibility that the adjustment in employment and wages might intensify further. One member expressed the view that the probability remained high that further reductions in wages would lower consumers' expectations for permanent income and as a result affect private consumption adversely.

Members agreed that the decrease in production was coming to a halt, due to progress in inventory adjustments both at home and abroad. As for the near-term outlook for production, members concurred that it was likely to level out and start recovering as inventory adjustments both at home and abroad progressed further. A few members said that production from the second half of fiscal 2009 depended on final demand overseas, and therefore it was highly uncertain whether a sustainable recovery in production would be realized.

Members agreed that the year-on-year rate of change in the CPI (excluding fresh food) had recently declined, reflecting the declines in the prices of petroleum products and the stabilization of food prices, and was likely to become negative, mainly due to these factors and also to increasing slackness in supply and demand conditions in the overall economy. Some members said that the difference between the number of items whose prices had risen and those whose prices had declined had narrowed further. As for risks to the outlook for prices, some members were of the view that, in a situation where the output gap remained significantly negative, the risk of a decline in firms' and households' expectations about medium- to long-term inflation warranted attention. Meanwhile, some other members said that commodity prices might surge again if, while stimulative fiscal and monetary policies were being maintained worldwide, the world economy started recovering, led mainly by emerging economies, and this warranted attention. One of these members noted that a possible surge in commodity prices might have negative effects on advanced economies through deterioration in the terms of trade.

B. Financial Developments

Members agreed that financial conditions in Japan had remained tight, although there had been some easing of tension. Many members said that issuance rates on CP had declined further and an increasing number of firms had been issuing corporate bonds, suggesting that policy effects had been permeating financial markets. Some members, however, noted the following facts: investors had remained highly selective about the issues of CP and corporate bonds they purchased, and issuance of corporate bonds by firms with low credit ratings had remained subdued; and many firms had continued to see their financial positions as weak and lending attitudes of financial institutions as severe. These members were of the view that funding conditions had polarized among firms. One member said that a possible prolongation of the economic downturn might impair financial institutions' assets further, imposing capital constraints on them, and this might negatively affect corporate financing. A different member expressed the view that, if the economic downturn persisted, firms' cash flow from operating activities might remain low and as a result the market might revert to a very cautious view of firms. Meanwhile, one member said that attention should be paid to market developments including a possible increase in the volatility of longer-term interest rates, given that an increase in Japanese government bond (JGB) issuance was expected.

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

Regarding the guideline for money market operations for the intermeeting period ahead, members agreed that it was appropriate to maintain the current guideline that the Bank would encourage the uncollateralized overnight call rate to remain at around 0.1 percent.

As for the future conduct of monetary policy, members concurred that the Bank should be attentive to downside risks to economic activity and prices and continue to conduct monetary policy steadily in line with measures taken so far, which could be divided into three areas: reducing the policy interest rate, ensuring stability in financial markets by providing ample liquidity, and facilitating corporate financing. Many members -- while admitting that strong effects of policy measures were manifesting themselves in the fact, for example, that interest rates on some CP had fallen below those on government bills -- were still of the view that the Bank should continue to implement steadily the various policy measures already introduced because financial conditions as a whole had remained tight. Some members said that whether or not the Bank would continue with various temporary measures, which were to be terminated on or after September 30, should be determined based on close examination of developments in financial markets and corporate financing.

Members discussed the Bank's communication regarding its assessment of the economy and its conduct of monetary policy. One member expressed the view that, since the market might focus exclusively on the fact that the Bank had upgraded its assessment of the state of the economy, it should carefully explain its view of not only the direction of economic activity but also its level. A different member added that it was also necessary to explain to the public that developments in the economy had generally been in line with the projection presented in the April 2009 Outlook Report. Members were in agreement on these points. One member said that since considerable uncertainty surrounding the outlook for economic activity and prices was stressed in the April 2009 Outlook Report, market participants were expecting that the Bank would continue its accommodative monetary policy for the time being. The member continued that it was desirable that market expectations about future monetary policy be formed based on an outlook for economic and price developments that was shared by the market and the Bank. A different member said that while there was a view in the market that changes in the size of the Bank's balance sheet indicated the degree of effectiveness of its unconventional policy measures to address the dysfunctional state of financial markets, the changes also depended on the degree of improvement in market conditions. The member continued that a careful explanation of the effectiveness of the Bank's policy measures would be necessary, so that the market would understand that the size of the Bank's balance sheet did not by itself provide the basis for proper assessment of policy effectiveness.

V. Remarks by Government Representatives

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

(1) The government understood that the Bank continued to assess Japan's economic and financial conditions as very severe, predicting that, although exports and production were beginning to level out, domestic private demand was likely to continue to weaken, and the year-on-year rate of change in the CPI was likely to become negative partly due to increasing slackness in supply and demand conditions in the overall economy.

(2) The supplementary budget for fiscal 2009 was being deliberated in the Diet, and the government was doing its utmost to obtain the Diet's approval of it as soon as possible.

(3) The government would like the Bank, based on its economic assessment above and taking full account of the government's policy efforts, to continue to support the economy by conducting monetary policy in a flexible and timely manner.

The representative from the Cabinet Office made the following remarks.

(1) The annualized quarter-on-quarter growth rate of real GDP for the January-March quarter fell to minus 15.2 percent, as economic conditions deteriorated rapidly and remained severe. By contrast, some indicators such as those for exports and production had recently shown signs of bottoming out or recovering slightly.

(2) As for the outlook, although the state of the economy was likely to remain severe, it was expected that it would be supported by the weakening of adjustment pressures on inventories and also by the effects of the policy package. At the same time, however, attention should be paid to possible further deterioration in financial and employment conditions and the risk that deflationary expectations might emerge.

(3) The government considered it important that the supplementary budget for fiscal 2009 obtain as soon as possible the Diet's approval and that the policy package to address the economic crisis be swiftly implemented, in order to prevent the economy from falling into a negative spiral.

(4) The government would like to request the Bank to continue ensuring stability in financial markets and facilitating corporate financing. The government would also like the Bank to continue to support the economy by conducting monetary policy in an appropriate and flexible manner, taking account of the downside risks to the economy and prices and also of the government's policy efforts.

VI. 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 0.1 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 0.1 percent.

2. A public statement will be decided separately.

Votes for the proposal: Mr. M. Shirakawa, Mr. H. Yamaguchi, 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.

VII. Discussion on the 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).

VIII. Approval of the Minutes of the Monetary Policy Meeting

The Policy Board approved unanimously the minutes of the Monetary Policy Meeting of April 30, 2009 for release on May 27, 2009.

Attachment

May 22, 2009

Bank of Japan

Statement on Monetary Policy

1. At the Monetary Policy Meeting held today, the Policy Board of 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 0.1 percent.

2. The Bank, among other actions, had expanded the range of eligible collateral since last autumn to ensure stability in financial markets by further facilitating money market operations. In this process, the Bank, in coordination with other central banks, examined the feasibility of accepting the so-called cross-border collateral and decided today to accept bonds issued by the governments of the United States, the United Kingdom, Germany, and France as eligible collateral (see "Collateral Guidelines on Eligible Foreign Bonds").

3. Economic conditions have been deteriorating, but exports and production are beginning to level out against the backdrop of progress in inventory adjustments both at home and abroad. Financial conditions have remained tight, although there has been some easing of tension compared to some time ago. Going forward, although domestic private demand is likely to continue to weaken, exports and production, after leveling

[Note] Voting for the action: Mr. M. Shirakawa, Mr. H. Yamaguchi, 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.

out, are expected to start recovering and public investment to increase. Therefore, the pace of deterioration in economic conditions is likely to moderate gradually, leading to a leveling out of the economy. Meanwhile, 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.

4. The Bank's baseline scenario through fiscal 2010, in which expectations of both medium- to long-term growth and inflation are assumed to remain generally unchanged, projects that the economy will start recovering and the rate of decline in prices will moderate from the latter half of fiscal 2009, supported partly by the positive effects of measures to stabilize the financial system and of fiscal and monetary policy measures, in addition to a recovery in overseas economies and improvements in conditions in global financial markets. If these developments continue, there are prospects for Japan's economy to return to a sustainable growth path with price stability in the longer run. However, given that economic activity and prices are likely to be largely affected by developments in overseas economies and global financial markets, the outlook is attended by a significant level of uncertainty.

5. With regard to risk factors, those that demand attention in the area of economic activity are the continued high downside risks to the economy stemming from future developments in the global financial and economic situation, changes in medium- to long-term growth expectations, and financial conditions in Japan. Regarding the outlook for prices, there is a possibility that inflation will decline more than expected, if the downside risks to the economy materialize or medium- to long-term inflation expectations decline.

6. The Bank, paying attention for the time being to the downside risks to economic activity and prices, 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.