Not to be released until 8:50 a.m. Japan Standard Time on Friday, August 14, 2009.

August 14, 2009

Bank of Japan

Minutes of the Monetary Policy Meeting

on July 14 and 15, 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 Tuesday, July 14, 2009, from 2:00 p.m. to 4:05 p.m., and on Wednesday, July 15, from 9:00 a.m. to 1:30 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. S. Kagawa, Deputy Vice Minister for Policy Planning and Coordination, Ministry of Finance

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. N. Yoshioka, Deputy Director-General, Monetary Affairs Department[2]

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

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

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

---

[1] The minutes of this meeting were approved by the Policy Board at the Monetary Policy Meeting held on August 10 and 11, 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. N. Yoshioka was present on July 15.

Mr. T. Sekine, 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. Tachibana, Director, Deputy Head of Secretarial Services for the Board, Secretariat of the Policy Board

Mr. T. Sakamoto, Director, Head, Monetary Operations Planning, Monetary Affairs Department[3]

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

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

[3] Mr. T. Sakamoto was present on July 15.

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 June 15 and 16, 2009.[5] 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. In outright purchases of CP and corporate bonds and in U.S. dollar funds-supplying operations against pooled collateral, bidding was sluggish, as financial institutions' demand for liquidity had declined reflecting a recovery in market functioning.

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 had been more or less unchanged, but they had remained sensitive to changes in the balance between supply and demand in the market. Interest rates on term instruments showed the following developments. Yields on government bills, including those with a one-year maturity, had been in the 0.1-0.2 percent range recently. Euroyen rates had been on a moderate downward trend but had remained at a relatively elevated level, especially those with longer maturities, amid the continued lower volume of transactions. In the CP market, issuing conditions had been relatively stable due mainly to a decline in firms' demand for liquidity, and issuance rates on some CP with high ratings had been below yields on government bills. Issuance rates on CP with low ratings had been on a downward trend in general.

---

[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 0.1 percent.

Japanese stock prices had been relatively weak recently, partly reflecting a somewhat less optimistic view of economic growth around the world, and the Nikkei 225 Stock Average had been moving in the range of 9,000-9,500 yen. Long-term interest rates in Japan had been falling since the middle of June, following a decline in U.S. long-term interest rates. The benchmark rate had been moving at around 1.3 percent recently.

The yen appreciated against the U.S. dollar, moving in the range of 90-95 yen to the dollar, as expectations for U.S. economic recovery had weakened somewhat recently.

C. Overseas Economic and Financial Developments

Global economic conditions had stopped worsening.

U.S. economic conditions had continued to deteriorate, but the pace of deterioration was moderating. Home prices continued to be on a declining trend, and housing investment and business fixed investment had been contracting noticeably. Meanwhile, the level of private consumption was broadly unchanged, owing partly to the effects of fiscal stimulus measures. Cutbacks in production had continued, and inventory adjustments were making progress. In the labor market, although the number of employees had continued to decline considerably and the unemployment rate had been rising, there were signs that the pace of decline in the number of employees was slowing. Funding conditions for firms and households had remained tight, but had improved somewhat. As for prices, the year-on-year rate of change in the consumer price index (CPI) for all items had been negative, as food prices had declined slightly 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, but the pace of deterioration was slowing gradually. Business fixed investment and housing investment had decreased. Exports and private consumption 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, but the pace of deterioration was moderating.

The Chinese economy was growing at a faster rate, led mainly by domestic demand. Exports had decreased, but growth in private consumption had been firm and the pace of increase in fixed asset investment had accelerated further. Economic conditions in the NIEs and the ASEAN countries had stopped worsening, as seen in the fact that exports had increased and private consumption had leveled out. Meanwhile, the deceleration of economic growth in India had come to a halt. With regard to prices, the year-on-year rate of increase in the CPI had been on a declining trend in many Asian economies.

As for global financial markets, money markets were regaining stability, as seen in the fact that Treasury-Eurodollar (TED) spreads and credit spreads on CP had generally been at their levels in around August 2007. On the other hand, credit spreads on corporate bonds, particularly those with low ratings, remained at high levels, even though they had been on a decreasing trend. U.S. and European stock prices had declined, reflecting weaker-than-expected economic indicators such as U.S. labor statistics. Long-term interest rates in the United States had declined due not only to the fall in U.S. stock prices but also to strong bids in Treasury securities auctions. Long-term interest rates in Europe had also declined, following their U.S. counterparts.

D. Economic and Financial Developments in Japan

1. Economic developments

Exports decreased substantially from autumn 2008 mainly due to the deterioration in overseas economic conditions, but they had recently picked up, primarily reflecting the waning of adjustment pressures on overseas inventories. They were expected to continue recovering, mainly due to progress in adjustments in overseas inventories.

Public investment had increased. It was likely to continue increasing 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 remained generally weak, although there had been some signs of picking up, with the support of effects of various measures and price declines. Sales at department stores had continued to decrease significantly, reflecting further curtailment of purchases by consumers. On the other hand, the year-on-year rate of decrease in the number of new passenger-car registrations had moderated, mainly due to the reduction in automobile taxes. Meanwhile, indicators of consumer sentiment had recovered slightly due to various demand-boosting policy measures in addition to the decline in retail prices. Private consumption was likely to remain generally weak amid the worsening employment and income situation.

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

Production decreased substantially from autumn 2008 but had picked up recently, mainly due to the waning of adjustment pressures on inventories both at home and abroad. It was expected to continue recovering, primarily because of progress in inventory adjustments both at home and abroad.

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 decreasing for the time being due to lagged effects of the earlier substantial decrease in corporate profits and production.

On the price front, commodity prices had been more or less flat recently. The three-month rate of change in the domestic corporate goods price index (CGPI) had continued to be slightly below 0 percent mainly reflecting the easing of supply and demand conditions for products. 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 change in the CPI (excluding fresh food) had turned negative, mainly because the prices of petroleum products were lower than the high levels of a year earlier, in addition to the ongoing substantial slack in the overall economy. The decline in the CPI (excluding fresh food) was expected to continue accelerating for the time being, primarily because the prices of petroleum products were lower than the high levels of a year earlier.

2. Financial environment

Financial conditions, while remaining generally tight, had continued to show signs of improvement. The overnight call rate had remained at an extremely low level, and in this situation firms' funding costs had further declined, mainly due to declines in issuance rates on CP and corporate bonds, as well as in bank lending rates. However, the stimulative effects from low interest rates had been limited given the low level of economic activity and corporate profits. The amount outstanding of bank lending, especially to large firms, had continued to increase at a relatively fast pace, although the pace of increase had slowed. Issuing conditions for CP and corporate bonds had improved further: the decline in issuance of CP had mainly reflected a weakening of firms' demand for additional liquidity and working capital, 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. Under these circumstances, although many firms had continued to see their financial positions as weak and lending attitudes of financial institutions as severe, the financial situation in these regards had improved somewhat for both large and small firms. Meanwhile, the year-on-year rate of change in the money stock had been at around 2.5 percent.

II. Amendment to Temporary Rules regarding the Bank's Transactions with the Development Bank of Japan Inc. (DBJ) Related to Money Market Operations

A. Staff Proposal

The DBJ, with the aim of providing commitment lines to firms as part of its crisis response operations authorized by the government, had recently requested that the Bank expand the purposes for which it was allowed to participate in the Bank's money market operations: the DBJ's participation had been allowed, under temporary rules, only when its purpose was to purchase CP, and the DBJ's request was that the Bank allow its participation also when the purpose would be to provide commitment lines to firms. The staff would like to propose that the Bank accept the DBJ's request and take the necessary steps.

B. Discussion by the Policy Board and Vote

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 stopped worsening. As for the outlook, many members said that they were likely to recover gradually against the background of further progress in inventory adjustments and the positive effects of fiscal and monetary policy measures. Members also agreed that risks to the outlook were still tilted to the downside and uncertainty surrounding the outlook for the global economy remained high. Some members were of the view that recent signs of a trend toward economic recovery primarily reflected a waning of serious market concern and inventory adjustment pressures, both of which had surged following the failure of Lehman Brothers Holdings Inc. in autumn 2008, and that it still would take some time to adjust various excesses that had accumulated over the past several years.

Members discussed the state of global financial markets. Some members noted that money markets around the world had remained stable, against the background of provision of ample liquidity by central banks. However, one of these members said that arbitrage in the markets was not necessarily working in a sufficient manner and the functioning of the markets still depended heavily on provision of liquidity by central banks. Many members referred to the fact that stock prices and long-term interest rates, both of which had risen since around spring 2009 in the United States and some other countries, were on a declining trend. They were of the opinion that the decline was attributable to market participants' revisions to their excessively optimistic views about the economic outlook, primarily in light of the release of weaker-than-expected economic indicators in the United States. Some of these members added that stock prices and long-term interest rates continued to be sensitive to changes in market sentiment regarding developments in the world economy and the stability of the global financial system.

Turning to the U.S. economy, members concurred that economic conditions had continued to deteriorate but the pace of deterioration was moderating. Some members noted that inventory adjustments had continued to make progress. Regarding the housing market, a few members said that the pace of decline in home prices had been moderating as the fall in home sales was coming to a halt. As for the outlook, most members were of the opinion that the U.S. economy was likely to level out and start recovering on the back of progress in inventory adjustments. Some of these members, however, said that the pace of recovery in private consumption warranted conservative forecasting given that the employment situation had continued worsening, as evidenced by the rising unemployment rate and weaker-than-expected employment data. Some members expressed the view that it would take some time for the problem of financial institutions' impaired assets to be solved, and for adjustments of household balance sheets to be completed. In relation to this, one member noted that it also might be necessary to check whether or not the pace of U.S. economic recovery was being forecasted too conservatively based on Japan's post-bubble experience.

With regard to the economy of the euro area, members concurred that economic conditions had continued to deteriorate but the pace of deterioration was slowing gradually. Many members said that, although car sales had started to increase on the back of the effects of policy measures, private consumption as a whole remained on a declining trend because of the continued worsening in the employment and income situation. One member noted that the environment for exports to outside the euro area was starting to improve, as evidenced by an increase in orders received in Germany from abroad. A few members said that, notwithstanding this demand situation, progress in inventory adjustments had been slower than in other economies such as the United States. As for risks to the outlook, one member expressed the view that the effects of fiscal measures might wear off before private demand picked up. A different member noted the possibility that economic conditions in Central and Eastern European countries might weaken further.

Members concurred that the Chinese economy was growing at a faster rate, led mainly by domestic demand. Many members were of the view that the pace of increase in fixed asset investment had accelerated further and growth in private consumption had been firm following implementation of the large-scale stimulus package. In terms of the outlook, some members said that close attention should be paid to the possibility that asset markets might overheat, considering the sharp increase in loans to real estate firms. A few members expressed the view that it was highly uncertain whether the Chinese economy could continue to expand if the initial effects of the fiscal expansion disappeared before exports regained growth momentum. Meanwhile, some members said that economic conditions in the NIEs and the ASEAN countries had stopped worsening, as evidenced by exports and production having increased and private consumption also starting to improve reflecting positive effects of the policy measures.

Based on the above discussions on economic and financial conditions abroad, members discussed the state of Japan's economy. They concurred that Japan's economic conditions had stopped worsening. They also agreed that, although business fixed investment had declined substantially and private consumption had remained generally weak, public investment had increased, exports and production had picked up, and business sentiment, especially at large manufacturers, had stopped deteriorating. However, some members added that developments in business sentiment varied greatly depending on the industry and the size of the firm.

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, they shared the view that, against the background of progress in inventory adjustments both at home and abroad, economic activity would be greatly influenced by developments in final demand, and therefore the outlook was attended by a significant level of uncertainty stemming mainly from developments in overseas economies and global financial markets.

Regarding developments in each demand component, members agreed that exports had picked up with the progress in adjustments in overseas inventories. A few members expressed the view that accelerated growth in China's domestic demand was leading to an increase in Japan's exports to China. As for the outlook, members agreed that exports were likely to continue recovering for the time being. One member added, however, that there was significant uncertainty regarding developments in overseas economies from the latter half of fiscal 2009, when adjustments in overseas inventories were likely to be completed, and thus developments in Japan's exports also were subject to significant uncertainty.

Most members said that business fixed investment had declined substantially, reflecting the significant deterioration in corporate profits, and it was likely to continue declining for the time being. Some members referred to the fact that fixed investment plans for fiscal 2009 had been revised downward in survey results released in June, and commented that firms were being cautious about investing when the level of capacity utilization remained low and the outlook for the economy was highly uncertain. Most 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.

Many members said that private consumption had remained generally weak, while there were some signs of a pick-up attributable to the positive effects of various policy measures and the decline in prices. A few members were of the opinion that policy effects had materialized, particularly in sales of cars and electrical appliances. Many members including these members were of the view that in the severe employment and income situation, households were curtailing spending further, for example, by holding back their purchases of expensive goods. Many members said that firms' adjustments in employment and wages might intensify further. Based on the above discussion, members agreed that private consumption was likely to remain generally weak for the time being.

Members agreed that <u>production</u> had picked up mainly due to the waning of adjustment pressures on inventories both at home and abroad. They also agreed that it was likely to continue recovering for the time being with further progress in inventory adjustments. Some members, however, saw the pick-up in production as a rebound following the rapid production cuts that began in autumn 2008, and said that the pace of recovery in production was highly uncertain considering that adjustments of excesses in capital stock and employment were likely to continue both at home and abroad.

Many members said that <u>the CPI (excluding fresh food)</u> had fallen on a year-on-year basis, mainly due to the prices of petroleum products being lower than the high levels of a year earlier, in addition to the ongoing substantial slack in the overall economy. As for the outlook, members agreed that the year-on-year decline in the CPI was likely to continue accelerating for the time being, but then moderate from the latter half of fiscal 2009 as the effects of the previous year's developments in prices of petroleum products abated. Many members said that there were both upside and downside risks to the outlook for prices. A few members expressed the view that it was uncertain when and to what extent an improvement in the supply-demand balance of the economy would reduce downward pressure on prices. Some members said it was possible that the size of the negative output gap was being overestimated, given that some of the existing capital stock had become obsolete due to changes in industrial structure. Moreover, a few members expressed the opinion that it was necessary to continue monitoring developments in primary commodity prices because they continued to rise from the beginning of 2009, although they had again declined slightly recently. Meanwhile, in view of the significant deterioration in the supply-demand balance of the economy and the continuing fall in prices, some members said that attention should be paid to a possible decline in firms' and households' expectations about medium- to long-term inflation.

B. Financial Developments

Members agreed that financial conditions, while remaining generally tight, had continued to show signs of improvement. Some members commented that funding costs of financial institutions and firms had been on a downtrend, as evidenced by the fact that the risk premium embedded in interest rates on term instruments maturing beyond end-September 2009 -- the end of a semiannual book closing period for many Japanese firms -- was small, and that issuance rates on CP, even with relatively low ratings, had declined. As for corporate funding activity, a few members noted that the amount of corporate bond issuance through public offering in June marked a historical high and an increasing number of firms had been issuing corporate bonds. They expressed the view that the functioning of the CP and corporate bond markets had been recovering steadily. Nevertheless, many members including these members were of the view that the polarization of firms' funding conditions continued, as evidenced by the fact that issuance of corporate bonds by firms with low credit ratings had remained difficult. Members concurred that in this situation many firms had continued to see their financial positions as weak and lending attitudes of financial institutions as severe, although both large and small firms' financial situation in these regards had improved somewhat. Some members expressed the view that the situation might be preventing firms from becoming optimistic about future funding conditions, because the pace of future economic recovery following completion of inventory adjustments remained highly uncertain amid the severe situation in corporate profits.

C. Interim Assessment

Given the above assessment of economic activity, prices, and financial developments, members agreed with the following projections: economic growth prospects remained broadly unchanged from those presented in the *Outlook for Economic Activity and Prices* (hereafter the Outlook Report) released in April 2009, and the rates of price change would likely be somewhat higher in fiscal 2009, due mainly to the rise in crude oil prices, but broadly in line with the previous projections for fiscal 2010.

With regard to economic growth prospects, most members expressed the view that the growth rate was likely to be negative in fiscal 2009 and recover to about 1.0 percent in fiscal 2010. Members discussed the fact that their numerical forecasts in this interim assessment were lower on the whole than those in the April 2009 Outlook Report. One member expressed the view that it was appropriate to show clearly the lower forecast figures and state that economic developments nevertheless had been broadly in line with the projection in the April 2009 Outlook Report. Some members argued that it was more important to articulate that Policy Board members attached the greatest importance to the qualitative assessment of the mechanism underlying economic and price developments and that the assessment had not changed from that in the April Outlook Report. As for prices, most members were of the view that the year-on-year rates of change in both the CGPI and the CPI (excluding fresh food) were likely to be negative in fiscal 2009, and that the rates of decline were likely to be somewhat less in fiscal 2010.

Based on this discussion, members agreed that there were prospects for Japan's economy to return to a sustainable growth path with price stability in the longer run, but the outlook was attended by a significant level of uncertainty stemming mainly from developments in overseas economies and global financial markets.

With regard to risk factors, members concurred that downside risks to the economy stemming from future developments in the global financial and economic situation, changes in firms' medium- to long-term growth expectations, and financial conditions in Japan continued to warrant attention, as noted in the April Outlook Report. As for risks to the outlook for prices, they agreed that attention should also be paid to the possibility that the downside risks to the economy would materialize or medium- to long-term inflation expectations would decline. One member added that upside risks to prices stemming from rises in primary commodity prices also required attention.

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, they concurred that the Bank should be attentive to downside risks to economic activity and prices for the time being and 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.

Members discussed various temporary measures regarding money market operations that had been introduced since autumn 2008.

Members reached a consensus that a decision to continue with outright purchases of CP and corporate bonds and special funds-supplying operations to facilitate corporate financing should be made based on the assessment of developments in financial markets and in corporate financing as a whole, and should also be consistent with the basic principles described in the statement Outright Purchases of Corporate Financing Instruments, released in January 2009. Most members said that financial conditions remained generally tight, as evidenced by the fact that the polarization of funding conditions continued between firms with high and low credit ratings, and uncertainty in the pace of future economic recovery might be preventing firms from becoming optimistic about future funding conditions. Members then agreed that the effective periods of these measures should be extended in order to continue to facilitate corporate financing. Many members noted that these measures had played a significant role in facilitating corporate financing amid the financial crisis that began in autumn 2008, and that special funds-supplying operations to facilitate corporate financing had contributed to ensuring stability in interest rates on term instruments. These members expressed the opinion that current financial conditions still required these supportive measures. Some members commented that, in the Bank's outright purchases of CP, bids had fallen well short of the Bank's offers since March, but such purchases had continued to play the role of a safety valve and had been relieving market participants' funding concerns. One member said that termination of these measures at this point would have a considerable negative impact on market sentiment, although the need for the Bank to continue these measures had decreased significantly, as evidenced by a substantial decline in the Bank's purchases of CP.

Members also concurred that when considering an extension of the effective periods of various temporary measures, the Bank should bear in mind that, unlike in the period up to the end of fiscal 2008, financial conditions were showing signs of improvement. On this basis, they agreed that there should be a reevaluation by the year-end of whether financial conditions continued to require the support of various temporary measures, and thus the effective periods of these measures should be extended for three months. Some members said that further improvement in the situation would justify termination of the measures or a review for possible revisions at the year-end -- when the extended effective periods expired -- but another extension might become necessary if the Bank's judgment was that the situation had not improved sufficiently. They added that the need for the Bank to extend the effective periods of these measures again should be considered without any predetermined view.

Some members said that special funds-supplying operations to facilitate corporate financing might be a cause for side effects such as the fall of issuance rates on CP with high ratings below yields on government bills, but a review or termination of these operations should be decided based on not only their influence on certain markets and side effects but also developments in and the impact on financial markets and corporate financing as a whole. A few other members said that, while the market was giving considerable credit for the stability in interest rates on term instruments to the Bank's special funds-supplying operations to facilitate corporate financing, it was the Bank's provision of ample funds as a whole, including provision of funds with a relatively long maturity against pooled collateral, that had proved to be effective.

Members concurred that the effective periods of <u>the expansion in the range of corporate debt and asset-backed CP (ABCP) eligible as collateral</u> should be extended for three months in line with the extension of the effective period of special funds-supplying operations to facilitate corporate financing.

As for <u>U.S. dollar funds-supplying operations against pooled collateral</u>, members, while admitting that bidding was sluggish due partly to the abatement of serious market concern, agreed that these operations had continued to function as a safety valve in a situation where the market was still anxious about U.S. dollar funding. Many members noted that, based on such understanding, the U.S. dollar liquidity swap arrangements between the Federal Reserve and other central banks had been extended. Given this, members concurred that the Bank should extend the effective periods of both the U.S. dollar-yen swap arrangement with the Federal Reserve and its U.S. dollar funds-supplying operations against pooled collateral, in order to continue to ensure stability in financial markets. They also noted that the effective periods should be extended to February 1, 2010, the same as for the U.S. dollar liquidity swap arrangements between the Federal Reserve and other central banks.

Many members said that <u>the complementary deposit facility</u> should be discussed, taking account of the fact that the Bank had introduced this facility to provide sufficient liquidity while maintaining the policy interest rate at around its targeted level through money market operations. Based on this understanding, members agreed that, as financial conditions remained generally tight and downside risks to economic activity still warranted attention, the effective period of the complementary deposit facility should also be extended to continue to ensure stability in financial markets by providing ample liquidity. Some members, noting that this facility formed the floor of market interest rates and thus was playing an important role as an infrastructure for money market operations, said that the form of the facility should be examined with reference to the framework of money market operations by other central banks.

V. Remarks by Government Representatives

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

(1) Japan's economic conditions had stopped worsening as a whole, as exports and production had picked up. However, the economy was still in a difficult situation: business fixed investment was decreasing substantially, reflecting the severe situation in corporate profits; private consumption had remained relatively weak as the employment and income situation had become increasingly severe; and housing investment was decreasing. A similar assessment was made at this meeting.

(2) The government was doing its utmost to swiftly put into action all the measures provided in the policy package to address the economic crisis, including the provision of commitment lines by the DBJ, for which the Bank had decided to amend its temporary rules at this meeting.

(3) The government expected the Bank to continue to support the economy from the financial side by conducting monetary policy in an appropriate and flexible manner, in parallel with the government's policy efforts described above.

The representative from the Cabinet Office made the following remarks.

(1) Japan's economy, while in a difficult situation, was showing signs of picking up recently, reflecting improvement in exports and production and the effects of the policy package. Regarding short-term prospects, however, there remained concerns that the employment situation would worsen further. Moreover, attention should be paid to the risk that the

economy might be depressed further by the influence of the global financial crisis and a possible further slowdown in overseas economies. Furthermore, the risk of deflation warranted attention, as the negative output gap was widening substantially.

(2) The government would steadily implement the policy package to address the economic crisis and other measures, in order to pursue its top priority of achieving economic recovery in the near term. The government would conduct its economic and fiscal policies based on the Basic Policies 2009 for Economic and Fiscal Reform, which provides a roadmap for achieving the three goals of reassurance, vitality, and responsibility.

(3) The government expected the Bank to continue to conduct monetary policy in an appropriate and flexible manner, while maintaining close contact with the government, in order to facilitate the return of the Japanese economy to a sustainable growth path with price stability. The government welcomed today's discussion about an extension of the period for which various policy measures, such as the special funds-supplying operations to facilitate corporate financing, would remain in effect, in view of persisting concerns about the stability of the global financial system and a worldwide recession. The government would also like the Bank to continue to closely examine the situation in corporate financing and respond with appropriate measures as necessary.

VI. Votes

A. Vote on the Guideline for Money Market Operations

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 a 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.

B. Votes on Amendments to Principal Terms and Conditions for Money Market Operations

With a view to continuing to facilitate corporate financing and to ensure market stability, members agreed that it was appropriate to extend the period for which temporary measures, such as outright purchases of CP and corporate bonds and special funds-supplying operations to facilitate corporate financing, would remain in effect.

To reflect this view, the chairman formulated a proposal and put it to a vote.

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

VII. Discussion on the Statement on Monetary Policy

Members discussed the Statement on Monetary Policy, and put it to a 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 1).

VIII. Approval of the Minutes of the Monetary Policy Meeting

The Policy Board approved unanimously the minutes of the Monetary Policy Meeting of June 15 and 16, 2009 for release on July 21, 2009.

Attachment 1

July 15, 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 1] 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. In order to continue facilitating corporate financing and ensuring market stability, the Bank decided, by a unanimous vote,[Note 2] to extend the period for which temporary measures, such as outright purchases of CP and corporate bonds and special funds-supplying operations to facilitate corporate financing, will remain in effect (see Attachment 2).

3. Japan's economic conditions have stopped worsening. Public investment is increasing and exports and production are picking up. Business sentiment, especially of large manufacturing firms, has stopped deteriorating. On the other hand, business fixed investment is declining sharply mainly reflecting weak corporate profits. Private consumption, while there are some signs of a pick-up due mainly to the effects of

---

[Note 1] 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.

[Note 2] 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.

various policy measures, remains generally weak amid the worsening employment and income situation. Meanwhile, financial conditions, while remaining generally tight, have continued to show signs of improvement. The year-on-year rate of change in the CPI (excluding fresh food) has turned negative mainly due to the prices of petroleum products lower than the high levels of a year earlier, in addition to the ongoing substantial slack in the overall economy.

4. With noticeable progress having already been made in inventory adjustments both at home and abroad, economic activity will be greatly influenced by developments in final demand. The Bank's baseline scenario through fiscal 2010, in which expectations of medium- to long-term growth are assumed to remain generally unchanged, projects that the economy will start recovering 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. With regard to prices, the year-on-year rate of decline in the CPI will likely accelerate for the time being. However, assuming that medium- to long-term inflation expectations remain stable, the rate of decline in the CPI is expected to moderate from the latter half of fiscal 2009 as the effects of the changes in the prices of petroleum products abate. 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, the outlook is attended by a significant level of uncertainty stemming mainly from developments in overseas economies and global financial markets.

5. Compared with the projections presented in the April 2009 *Outlook for Economic Activity and Prices*, growth prospects remain broadly unchanged. With regard to prices, the year-on-year rate of change in the domestic corporate goods price index and the CPI (excluding fresh food) will likely be somewhat higher in fiscal 2009 than the April projections due mainly to the rise in crude oil prices, but is expected to be broadly as projected in fiscal 2010.

6. 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 firms' 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.

7. 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.

Appendix 1

Forecasts of the Majority of Policy Board Members

y/y % chg.

	Real GDP	Domestic CGPI	CPI (excluding fresh food)
Fiscal 2009	-3.7 to -3.0 [-3.4]	-6.0 to -5.8 [-5.9]	-1.5 to -1.2 [-1.3]
Forecasts made in April 2009	-3.7 to -3.0 [-3.1]	-7.6 to -6.9 [-7.5]	-1.6 to -1.4 [-1.5]
Fiscal 2010	+0.6 to +1.1 [+1.0]	-2.1 to -1.5 [-2.1]	-1.2 to -0.7 [-1.0]
Forecasts made in April 2009	+0.8 to +1.5 [+1.2]	-2.4 to -1.4 [-1.8]	-1.1 to -0.8 [-1.0]

Notes: 1. Figures in brackets indicate forecast medians.

2. The forecasts of the majority of Policy Board members are constructed as follows: each Policy Board member's forecast takes the form of a point estimate, namely, the figure to which he or she attaches the highest probability of realization. These forecasts are then shown as a range, with the highest figure and the lowest figure excluded. It should be noted that the range does not indicate the forecast errors.

3. Individual Policy Board members make their forecasts with reference to the view of market participants regarding the future course of the policy interest rate -- a view that is incorporated in market interest rates.

4. The range shown below includes the forecasts of all Policy Board members.

y/y % chg.

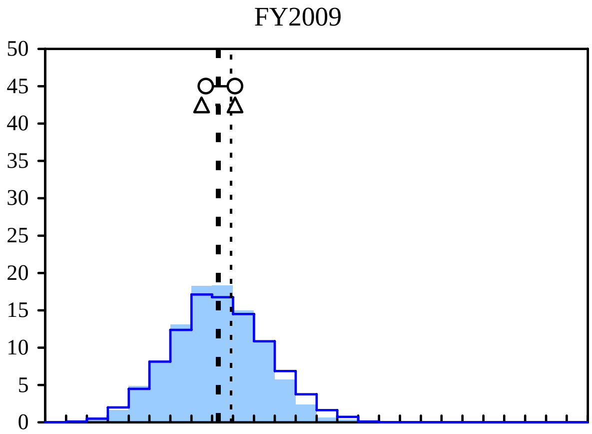
	Real GDP	Domestic CGPI	CPI (excluding fresh food)
Fiscal 2009	-3.8 to -3.0	-6.2 to -5.7	-1.6 to -1.2
Forecasts made in April 2009	-3.8 to -2.5	-7.8 to -6.8	-1.8 to -1.2
Fiscal 2010	+0.5 to +1.5	-2.1 to -1.4	-1.2 to -0.6
Forecasts made in April 2009	+0.7 to +1.5	-2.6 to -1.3	-1.2 to -0.4

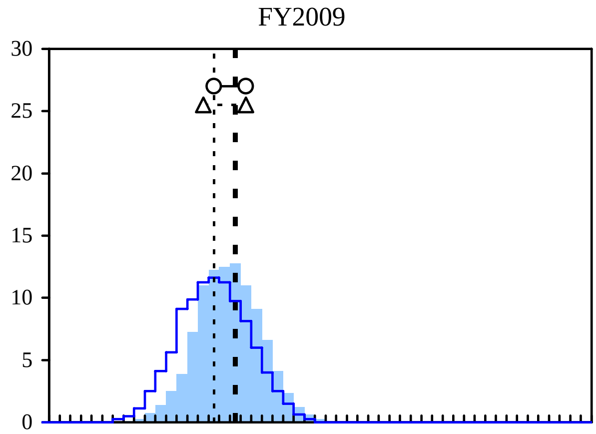
Appendix 2

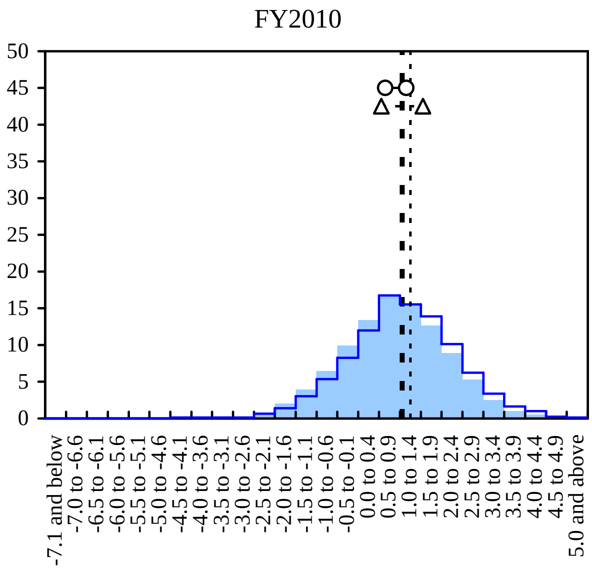
Risk Balance Charts

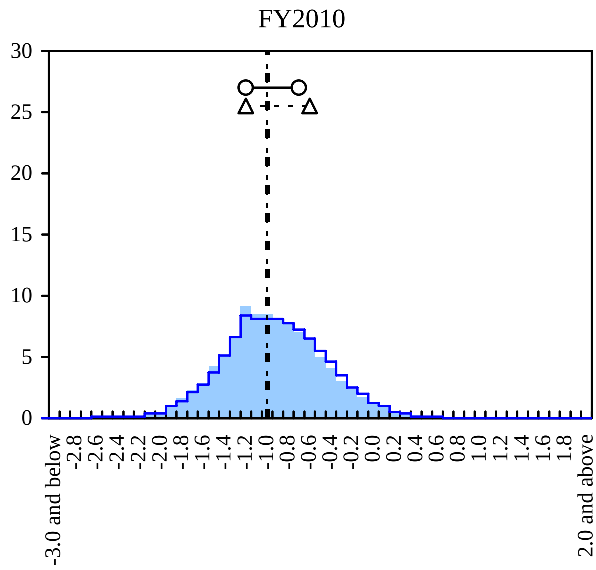
(1) Real GDP

(2) CPI (Excluding Fresh Food)









Notes: 1. Vertical axes in the charts represent probability (%), while horizontal axes represent the year-on-year percentage changes in the respective indicators. Bar charts represent the probability distributions in July 2009, and solid lines represent those in April 2009.

2. Vertical dashed heavy lines indicate the median of the Policy Board members' forecasts (point estimates). ○——○ indicates the range of the forecasts of the majority of Policy Board members. △- - - -△ indicates the range of the forecasts of all Policy Board members.

3. Vertical dashed thin lines indicate the median of the Policy Board members' forecasts (point estimates) in April 2009.

4. For the process of compilation of the Risk Balance Charts, see the box on page 9 of the April 2008 *Outlook for Economic Activity and Prices.*

Attachment 2

Extensions of Various Temporary Measures

1. Outright purchases of CP (extended to December 31, 2009 from September 30, 2009)
2. Outright purchases of corporate bonds (extended to December 31, 2009 from September 30, 2009)
3. Special funds-supplying operations to facilitate corporate financing (extended to December 31, 2009 from September 30, 2009)
4. Expansion in the range of corporate debt eligible as collateral (extended to March 31, 2010 from December 31, 2009)
5. Expansion in the range of asset-backed commercial paper eligible as collateral (extended to March 31, 2010 from December 31, 2009)
6. Complementary deposit facility (extended to January 15, 2010 from October 15, 2009)
7. U.S. dollar funds-supplying operations (extended to February 1, 2010 from October 30, 2009)