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May 9, 2011

Bank of Japan

Minutes of the Monetary Policy Meeting

on April 6 and 7, 2011

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

A Monetary Policy Meeting of the Bank of Japan Policy Board was held in the Head Office of the Bank of Japan in Tokyo on Wednesday, April 6, 2011, from 2:00 p.m. to 4:47 p.m., and on Thursday, April 7, from 9:00 a.m. to 1:05 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

Mr. T. Noda

Mr. S. Nakamura

Mr. H. Kamezaki

Mr. R. Miyao

Mr. Y. Morimoto

Ms. S. Shirai

Government Representatives Present

Mr. M. Sakurai, Senior Vice Minister of Finance, Ministry of Finance[2]

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

Mr. Y. Suematsu, Senior Vice Minister for Economic and Fiscal Policy, Cabinet Office[2]

Mr. K. Umetani, Director-General, Economic and Fiscal Management, Cabinet Office[3]

Reporting Staff

Mr. K. Yamamoto, Executive Director[4]

Mr. H. Nakaso, Executive Director (Assistant Governor)

Mr. M. Amamiya, Executive Director

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[1] The minutes of this meeting were approved by the Policy Board at the Monetary Policy Meeting held on April 28, 2011 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] Messrs. M. Sakurai and Y. Suematsu were present on April 7.

[3] Messrs. Y. Kinoshita and K. Umetani were present on April 6.

[4] Mr. K. Yamamoto was present on April 6 from 2:00 p.m. to 2:50 p.m., and on April 7 for the whole of the session.

Mr. N. Kinoshita, Executive Director

Mr. S. Kushida, Director-General, Monetary Affairs Department

Mr. T. Umemori, Deputy Director-General, Monetary Affairs Department[5]

Mr. T. Kato, Head of Policy Planning Division, Monetary Affairs Department

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

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

Mr. T. Sekine, Head of Economic Research Division, Research and Statistics Department

Mr. H. Ono, Director-General, International Department

Secretariat of the Monetary Policy Meeting

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

Mr. T. Tachibana, Director, Deputy Head of Planning and Coordination Division, Secretariat of the Policy Board

Mr. H. Chida, Head of Policy Infrastructure Division, Monetary Affairs Department[5]

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

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

[5] Messrs. T. Umemori and H. Chida were present on April 7.

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

A. Financial Developments in the Disaster Areas

The Great East Japan Earthquake had caused enormous damage to head offices and branches of financial institutions located in the Tohoku region. According to data compiled by the government, about 150 branches, or around 6 percent of the total branches in the region, were still closed as of April 1. In this situation, financial institutions were restoring their closed branches while at the same time shifting their operations from closed branches to neighboring ones as part of their efforts to maintain business operations at the windows.

There was growing demand in the disaster areas at this point for cash to purchase daily necessities, and to meet such demand each financial institution was responding to withdrawal of deposits, not only on business days but also on weekends and holidays. Although the situation regarding deposits at financial institutions had remained stable as a whole, some financial institutions considered that future developments in deposit taking were uncertain.

In the disaster areas, there was a surge in the number of firms requesting postponement of repayments of their loans and of firms making loan inquiries, particularly about working capital at present. Financial institutions were actively responding to these requests and inquiries. Many firms, however, had not fully grasped the extent of the damage caused by the disaster and had not yet reached the stage of deciding policies for rebuilding their businesses. For this reason, financial institutions were not yet able to get an overall picture of demand for funds. It was likely that demand for loans would increase further as moves toward restoration and rebuilding made progress; however, the extent and timing were uncertain at this point.

B. Money Market Operations in the Intermeeting Period

The Bank, in accordance with the guideline decided at the previous meeting on March 14, 2011, had been providing ample funds sufficient to meet demand in financial markets, as evidenced by its provision of funds through same-day funds-supplying operations over a period of successive days, and was doing its utmost to ensure stability in

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

the markets.[7] In this situation, the uncollateralized overnight call rate had generally been declining since the week following the earthquake, and was recently at around 0.06 percent.

C. Recent Developments in Financial Markets

In the money market, interest rates rose somewhat after the earthquake, partly reflecting the heightening of precautionary demand for funds at financial institutions, while at the same time lenders temporarily became more cautious about releasing funds. In response, the Bank had provided a large amount of funds, and interest rates regained stability as a whole. General collateral (GC) repo rates had recently been slightly below the 0.1 percent level. Yields on treasury discount bills (T-Bills) had started to decline after increasing somewhat, and, including those with a one-year maturity, had recently been in the range of 0.10-0.15 percent. Rates on longer-term interbank instruments had been more or less unchanged.

Long-term interest rates decreased somewhat amid declining stock prices, but had risen thereafter due to the pick-up in overseas interest rates and concerns about an increase in the issuance of Japanese government bonds (JGBs). The benchmark rate had recently been at around 1.3 percent. In the secondary market of corporate bonds, the volume of transactions had been low as investors had taken a wait-and-see stance, and yield spreads between corporate bonds and JGBs, mainly those of electric company bonds, had widened. Stock prices had dropped sharply after the earthquake but rebounded somewhat thereafter. The Nikkei 225 Stock Average had recently been at around 9,500 yen. The Tokyo Stock Exchange REIT Index, after temporarily experiencing a substantial drop, exhibited a deceleration in the pace of decline as Japan real estate investment trusts (J-REITs) were increasingly bought back. In addition, credit default swap (CDS) premiums for private firms, after increasing substantially, had essentially started to decrease in a situation where stock prices exhibited a rebound. These developments reflected the fact that, although investors' risk aversion had heightened after the earthquake, financial markets were gradually regaining stability recently, despite some lingering nervousness. In the foreign exchange market, the yen had temporarily appreciated against the U.S. dollar after the

[7] The guideline was as follows:

The Bank of Japan will encourage the uncollateralized overnight call rate to remain at around 0 to 0.1 percent.

earthquake, hitting the range of 76-77 yen, but had depreciated thereafter, initiated by the concerted intervention in exchange markets on March 18, 2011, and had most recently been in the range of 85-86 yen.

D. Overseas Economic and Financial Developments

Regarding U.S. and European financial markets, stock prices in major economies fell temporarily and long-term interest rates came under downward pressure, as investors' risk aversion had heightened due to increased tension over the situation in North Africa and the Middle East and to the disaster in Japan. Thereafter, as an increasing number of market participants shared the view that the effects of the disaster in Japan on the world economy would be limited, stock prices and long-term interest rates recovered and were at levels more or less the same as or slightly higher than at the time of the previous meeting.

As for international commodity prices, while prices of nonferrous metals and grain had shown some signs of adjustments, crude oil prices had climbed due to growing demand from emerging economies, accommodative financial conditions around the world, and uncertainty about the situation in North Africa and the Middle East.

In terms of economic activity, the world economy had continued to recover.

The U.S. economy had continued to recover. Exports had continued to increase, especially to emerging economies, and business fixed investment was rising moderately. Private consumption had been firm mainly due to the effects of the fiscal stimulus measures; nevertheless, balance-sheet adjustments continued to weigh on household spending. Housing investment remained at a depressed level. As for prices, the effects of the rise in international commodity prices were increasing somewhat, while an expansion in downward pressure on prices -- associated with slack in supply and demand conditions in the goods market and the labor market -- was restrained.

Economic activity in the euro area as a whole was recovering moderately, with some differences in pace by country. Exports had continued to increase, and private consumption and business fixed investment had been rising gradually. As for prices, although slack in supply and demand conditions and slower growth in wages continued to exert downward pressure, the year-on-year rate of increase in the Harmonized Index of Consumer Prices (HICP) for all items had risen due to the effects of the earlier depreciation of the euro and the rise in international commodity prices.

The Chinese economy continued to show high growth. Exports and production had been increasing, and growth in private consumption had been firm due mainly to households' increased income levels. Economic conditions in the NIEs and the ASEAN countries had been recovering. In many of these Asian economies, inflationary pressure remained high, reflecting greater utilization of production factors and the effects of the increase in international commodity prices.

As for the effects of the disaster in Japan, it was possible that supply-chain disruptions of automobiles and electrical machinery would exert downward pressure on production in the short term, particularly in Asian economies. Although there was a view that the effects of the disaster would not last for a protracted period and would remain marginal, as restoration of production lines and a shift to substitutes proceeded, this view was attended by a high degree of uncertainty.

E. Economic and Financial Developments in Japan

1. Economic developments

Production had declined significantly in some industries and regions since the earthquake, mainly because production facilities had been damaged, the supply chain had been disrupted, and electric power supply had been constrained. According to interviews with firms, for example, factories that were directly damaged as a result of the disaster had been shut down, and many factories located in places other than the disaster areas were forced to cut back production substantially, particularly that of automobiles, mainly due to a suspension in the supply of parts from factories in the disaster areas and to the effect of blackouts. Production was expected to remain at a low level for the time being, but was likely to start increasing as supply-side constraints were mitigated.

Exports seemed to have dropped sharply since the earthquake. They were likely to remain at low levels for the time being, but were expected to turn upward as supply-side constraints were mitigated, reflecting the continued improvement in overseas economic conditions.

The rate of decline in public investment had started to decelerate gradually. Public investment was expected to increase gradually, mainly due to the restoration of damaged social capital.

With regard to domestic private demand, business fixed investment -- which had been picking up until the earthquake -- was likely to have weakened temporarily due to the subsequent decline in production. Business fixed investment was expected to increase gradually, mainly because damaged facilities would be repaired.

The employment and income situation had remained severe, but the degree of severity had eased somewhat.

As for private consumption, the effects of the disaster had pushed up demand for some daily necessities but seemed to have dampened consumption due to deterioration in sentiment.

Housing investment had started to pick up. It was expected to edge up, as measures to repair the damage caused by the earthquake would be put into effect.

As for prices, the three-month rate of change in the domestic corporate goods price index (CGPI) was rising, mainly due to the increase in international commodity prices, and was expected to continue rising for the time being. The year-on-year rate of decline in the consumer price index (CPI) for all items excluding fresh food had continued to slow, while substantial slack remained in the economy as a whole. The year-on-year rate of change in the CPI was expected to become slightly positive in the near future.

2. Financial environment

As for financial developments since the earthquake, the financial intermediation function had been maintained and smooth fund settlement had also been secured.

Financial conditions had generally continued to ease, while weakness had been observed in the financial positions of some firms, mainly small ones, since the earthquake.

The overnight call rate had remained at an extremely low level, and the declining trend in firms' funding costs had continued. Stimulative effects from low interest rates were still partly constrained given current developments in economic activity and prices. With regard to credit supply, firms had continued to see financial institutions' lending attitudes as improving. In the corporate bond market, new issuance of bonds had been at a pause amid somewhat wider credit spreads on corporate bonds, whereas the issuing conditions for CP had continued to be favorable. As for credit demand after the earthquake, firms, particularly large ones, had shown signs of increasing their demand for working capital as well as accumulating on-hand liquidity, and applications for bank loans were increasing. The financial positions of firms had been improving as a whole, although weakness had been observed in those of some firms, mainly small ones, since the earthquake. Meanwhile, the year-on-year rate of change in the money stock had been at around 2.5 percent.

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

A. Economic Developments

Members discussed economic developments in Japan, placing particular focus on the effects of the disaster. Regarding the current state of Japan's economy, members agreed that it was under strong downward pressure, mainly on the production side, due to the effects of the disaster. Many members said that production facilities had suffered significant damage as a direct result of the disaster, especially in the Tohoku region. Members shared the view that production had declined not only in the disaster areas but also across a wider region, due to considerable constraints on the supply of parts and materials that were produced at factories in the disaster areas. Some members commented that the supply chain disruptions had caused suspension of and contraction in production across a wide range of industries including automobiles, general machinery, electronic parts, and chemicals. Moreover, members agreed that constraints on electric power supply caused by damage to power generating facilities were acting as a factor depressing production, especially in the Kanto and Tohoku regions. On this basis, members concurred that, although it was difficult to grasp the whole picture of the situation at this point, available information -- including anecdotal evidence obtained from firms -- suggested it was highly likely that production had dropped substantially in March 2011.

Members shared the view that the dampening of production had been affecting exports and domestic private demand accordingly. With regard to developments in private consumption, many members noted that the number of new passenger-car registrations had decreased in March by almost 30 percent from the previous month and that sales of electrical appliances, sales at department stores, and sales in the food service industry, as well as outlays for travel, had declined substantially since the earthquake. A few members expressed the view that, in some areas of the economy, a demand shock was becoming evident, in which a decline in consumption was caused by factors including the effects of blackouts and a shortage of goods, widespread voluntary restraint in consumer spending, and deterioration in sentiment following the crisis at the nuclear power plant.

Regarding the outlook for Japan's economy, members shared the view that the economy was likely to remain under strong downward pressure for the time being, mainly on the production side, but was expected to return to a moderate recovery path as supply-side constraints were mitigated and production regained traction. Some members expressed the view that, because demand had not evaporated in the current situation, unlike at the time of the Lehman shock, the economy was basically expected to recover in line with demand as supply-side constraints were eliminated.

As examples of moves aimed at eliminating the constraints on the supply side, a few members noted that many firms had already been making various efforts in the form of resuming operations at less-affected production facilities, utilizing production facilities in western Japan, and securing alternative suppliers. Some members took the view that, as a result of the efforts to restore the supply chain, many firms might be able to reestablish their production systems before the summer of 2011. However, many members said that, even if the supply chain were to be restored smoothly, it was difficult at this point to determine when supply-side constraints would be eliminated as a whole, since the supply capacity for electric power could fall short of the forecasted demand at peak times in the summer.

Members made the following remarks regarding developments on the demand side. Many members said that, since overseas economies had continued to recover, led by high growth in emerging and commodity-exporting economies, Japan's exports were likely to increase as supply-side constraints were eliminated and to begin to serve as one of the driving forces of Japan's economic recovery. A few members commented that, if the recent depreciation of the yen against the U.S. dollar continued, it was likely to boost exports and positively affect business fixed investment through improvement in corporate profits and sentiment. Moreover, some members expressed the view that demand for rebuilding for the purpose of restoring capital stock would gradually take hold. Meanwhile, some members said that developments in business fixed investment and private consumption would be affected partly by the timing of the elimination of supply-side constraints and the consequences of the crisis at the nuclear power plant. One member pointed out that, if such problems continued over an extended period, sentiment could be adversely affected and corporate profits and household income could come under continuous downward pressure; thus, it was quite likely that the economy as a whole would deviate downward from the recovery path projected prior to the earthquake. However, one member said that, in the longer term, if firms, being attentive to various risks, shifted and diversified their production and distribution sites following the disaster, this could generate new demand even beyond a rise in demand associated with the restoration of the supply chain and damaged capital stock. A few members expressed the view that, in the process of rebuilding following the disaster, it would become all the more important to have a perspective on how restoring the social infrastructure and industrial activity could lead to a rise in Japan's productivity and growth potential.

Based on the above discussion, members shared the view that uncertainty regarding the possible effects of the disaster on Japan's economy was extremely high, and it was necessary to continue to closely examine the effects from various aspects, such as the process for eliminating supply-side constraints and developments in demand at home and abroad.

Members discussed the economic and financial conditions abroad and risks to the outlook for Japan's economy related to these conditions. Regarding the U.S. economy, many members said that, although it continued to recover, balance-sheet adjustments in the household sector still weighed on the economy given the developments in the labor and housing markets. With regard to the economy in the euro area, many members noted that a contrast was becoming more apparent between major countries -- such as Germany, which continued to show high growth led by exports -- and some peripheral countries, which faced the sovereign risk problem. Some members commented that, if the European Central Bank leaned more toward monetary tightening in the future due to a concern about inflation, this could result in heightened fiscal problems in some peripheral countries. These members continued that due attention should therefore be paid to the possible effects of such a move on future developments in the European economies and global financial markets. Meanwhile, many members expressed the view that the Chinese economy continued to show high growth, and economic conditions in the NIEs and the ASEAN countries had also been recovering, as domestic demand was firm and exports started to regain momentum. Some members took the opinion that, although many emerging economies had been shifting away from accommodative monetary policies, concerns about an overheating of the economy and inflation had not yet been dispelled. Based on this discussion, members shared the view that there continued to be some upside risks to Japan's economy caused by such factors as faster growth in emerging and commodity-exporting economies. They also agreed that there were downside risks associated with developments in global financial markets and continued uncertainties, albeit reduced, regarding the outlook for the U.S. and European economies.

Many members expressed the view that attention should also be paid to the continued rise in international commodity prices, particularly crude oil prices. Some members referred to the possibility that the high growth in emerging and commodity-exporting economies that lay behind the rise in international commodity prices would lead to an increase in Japan's exports. However, some members said that, if the rise in international commodity prices continued amid the depreciation of the yen against the U.S. dollar, Japanese firms' profits and real purchasing power could decline reflecting deterioration in the terms of trade, which in turn could reduce domestic private demand in Japan.

Members discussed the effects of the disaster in Japan on overseas economies. One member said that the impact on the supply chain had spread internationally, as evidenced by the difficulty in procuring materials and parts from Japan, and that in the United States and Asian emerging countries downward revisions to production plans in some industries such as automobiles had been inevitable. A different member, however, noted that there was a view that exports of Asian emerging economies to Japan, such as those of daily necessities, were likely to increase, and it was therefore difficult to determine at this point which effects -- positive or negative -- would outweigh the other. A few members noted that U.S. and European long-term interest rates and stock prices -- which had increased in volatility immediately after the earthquake -- regained stability thereafter, returning to more or less the same levels as before the earthquake; accordingly, it was likely that the view that the effects of the disaster in Japan on the global economy would be limited was becoming reinforced among an increasing number of global investors.

Members confirmed that the year-on-year rate of decline in the CPI (excluding fresh food) had continued to slow. A few members expressed the opinion that the rises in international commodity prices and in prices of imports such as clothes, against the backdrop of inflation in Asian economies, were factors exerting upward pressure on prices in Japan, and prices were recently somewhat higher than had been expected.

Members concurred that, taking into account developments in, for example, international commodity prices, the year-on-year rate of change in the CPI was expected to become slightly positive in the near future. With regard to the effects of the disaster on prices, some members noted that upward pressure on prices might occur if a bottleneck on the supply side occurred or crude oil prices rose further due to a growing shift back to fossil fuels from nuclear energy, triggered by the crisis at the nuclear power plant. In relation to the outlook for prices, a few members expressed the opinion that, as for developments in the aggregate supply and demand balance, constraints on the supply side would temporarily become severe due to the effects of the disaster. These members continued, however, that slack in supply and demand conditions was likely to return as these constraints were mitigated. On the other hand, one member said that not only would supply-side constraints become severe, but also demand might weaken to a level surpassing the supply-side severity as a result of continuous downward pressure on corporate profits and household income. Based on this discussion, members shared the view that the effects on prices might differ depending on how long the supply shock continued and the extent to which it impacted the demand side. One member commented that discussions regarding the supply-demand balance and prices were important when assessing the economy over the medium to long term, but were not necessarily pertinent to the present situation, in which supply-chain disruptions and electricity shortages were taking place.

B. Financial Developments

As for financial developments since the earthquake, members confirmed that the financial intermediation function had been firmly maintained and smooth funds settlement had been secured. A few members said that (1) Japan's core payment and settlement systems, such as the Bank of Japan Financial Network System (BOJ-NET) and the Zengin System (the clearing system for domestic funds transfers), had been functioning properly; (2) transactions in financial markets were being carried out as usual; and (3) financial institutions in the disaster areas were smoothly conducting business operations by, for example, responding to withdrawal of deposits to meet demand for cash. Some members expressed the opinion that it was very important, from the viewpoint of underpinning the severe economic situation from the financial side and ensuring public confidence, that the financial and settlement systems as well as financial markets remain robust.

Members agreed that financial conditions had generally continued to ease, while weakness had been observed in the financial positions of some firms, mainly small ones.

Many members said that money market rates rose somewhat after the earthquake, reflecting the heightening of precautionary demand for funds, but had regained stability recently as the Bank had provided a large amount of funds. Some members said that long-term interest rates declined temporarily after the earthquake but recently had risen again, to around 1.3 percent, due partly to the effects of the rise in overseas interest rates and to concerns about an increase in the issuance of JGBs to fund restoration and rebuilding.

With regard to developments in the CP market, many members said that issuance spreads on CP had expanded somewhat immediately after the earthquake but had started to narrow thereafter, reflecting the Bank's purchases of CP under repurchase agreements, and therefore the issuing conditions for CP had continued to be favorable recently. On the other hand, as for the corporate bond market, many members noted that new issuance of bonds had been at a pause amid somewhat wider credit spreads on corporate bonds. As the background to this situation, a few members pointed out that firms and investors continued to take a wait-and-see stance, partly because it had become difficult to assess the value of corporate bonds in the market as a whole since yield spreads had widened considerably between JGBs and some electric company bonds, which had previously been the benchmark. Some members, however, said that investors' panic selling was not observed and yield spreads on corporate bonds in the secondary market had been stable as a whole. They continued that, therefore, the situation in the corporate bond market differed significantly from that observed in the period following the failure of Lehman Brothers, when market functioning declined considerably and trading in financial markets was suspended. One member commented that issuing conditions for corporate bonds were likely to improve again as firms and investors searched for new benchmark data and appropriate yield spreads. One member said that the J-REIT market had been relatively firm, because real estate properties in the disaster areas that constituted J-REITs represented just a small proportion and market confidence had increased following the Bank's purchases of J-REITs.

Members agreed that recent surveys revealed weakness after the earthquake in the financial positions of some firms, mainly small ones, although firms' positions had been improving as a whole. Some members noted that due attention should be paid to the possibility that concerns about funding might materialize even in areas other than those hit by the disaster due, for example, to a possible decline in sales and difficulties in collecting accounts receivable.

III. 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 to 0.1 percent.

Members discussed the effects of the increase in the amount of the Asset Purchase Program (hereafter the Program) decided at the previous meeting. Some members once again noted that the CP and corporate bond markets had been stable compared with the situation observed in the period following the failure of Lehman Brothers, and that indicators such as stock prices, which had fallen temporarily after the earthquake, had been recovering again thereafter. Taking these developments into account, many members expressed the view that the increase in the amount of the Program so far had generated certain positive effects, in that it had been reassuring market participants about their funding and had been effective in terms of preventing any deterioration in business sentiment and heightening of risk aversion in financial markets. On this basis, some members expressed the opinion that, at this point, it was important for the Bank to examine the effects of the increase in the amount of the Program, including those of the aforementioned financial market developments on economic activity. A few members said that, while monetary policy could not remove supply-side constraints, it was nevertheless necessary for the Bank to continue monitoring carefully their negative impact from the perspectives of whether they would exert continuous downward pressure on Japan's economy through deterioration in sentiment as well as decreases in corporate profits and household income, and whether the possibility of such a situation would heighten.

In addition, many members expressed the view that, taking into account the extent of the effects of the disaster and the financial developments in disaster areas, the Bank should consider an additional contribution from the financial side. Some members said that, considering its functions as a central bank, the Bank could support lending activity of financial institutions in the disaster areas by providing liquidity, thereby encouraging them to perform their financial functions efficiently. Many members, while noting that demand for living expenses and firms' working capital at present, as well as for funds for restoration and rebuilding, was likely to increase in the disaster areas, pointed to the possibility of financial institutions in these areas becoming weaker in terms of their ability to take deposits, their main source of funding. Based on these views, members agreed that, in addition to the provision of ample funds to the market, it was appropriate for the Bank to introduce a funds-supplying operation that would provide financial institutions in disaster areas with longer-term funds, in order to support their initial efforts to meet demand for funds for restoration and rebuilding. Some members added that, in light of this objective, it was necessary to proceed with the funds provisioning as promptly as possible, and that such an action would also contribute to further reassuring the financial institutions in the disaster areas. One member said that, in the case of funds provisioning, the Bank should clearly distinguish the new funds-supplying operation from both fiscal policy and financing from public financial institutions. The member continued that the Bank should also take care to ensure that it would not become directly involved in the specific allocation of funds to individual firms, nor take on an excessive amount of risk. Based on this discussion, members agreed that it would be appropriate for the Bank to introduce a new framework for providing longer-term funds to the financial institutions in the disaster areas. Moreover, many members expressed the view that it would be desirable for the Bank to consider, together with the framework, a broadening of the range of eligible collateral for money market operations with a view to securing sufficient financing capacity at the financial institutions in disaster areas. Some members, referring to the disaster assistance loans made after the Great Hanshin-Awaji Earthquake, accompanied by the broadening of the range of eligible collateral for money market operations, said that, the circumstances at that time differed somewhat from the present situation, but these measures might serve as a meaningful reference in the current discussion.

Members then discussed specifics of the new framework. Many members were of the opinion that it was appropriate for the Bank -- in order to effectively support restoration and rebuilding efforts in the disaster areas -- to consider financial institutions that had business offices in the disaster areas as eligible counterparties of the new funds-supplying operation. Some members said that, for financial cooperatives, which were deeply rooted in the regional economy and deemed to play a vital role in efforts toward restoration and rebuilding, it was desirable for the Bank to consider a framework for providing them with funds through its counterparty financial institutions.

One member expressed the opinion that, with a view to utilizing the existing framework as much as possible, it would be appropriate to deliberate on a lending method based on the framework for a funds-supplying operation against pooled collateral.

With regard to the total amount of loans, many members expressed the view that it would be appropriate to provide a sufficient amount of loans to financial institutions in disaster areas in an effort to further reassure them. Based on this, some members said that, given that the economic cost of the damage incurred by the Great East Japan Earthquake was estimated to be about twice the amount of the Great Hanshin-Awaji Earthquake, the Bank's total amount of loans could be set at around 1 trillion yen -- twice the amount of disaster assistance loans extended at that time. One member commented that, since it was difficult to determine the size of demand for funds among financial institutions in disaster areas, an increase in the total amount of loans was one option if the initial total amount turned out to be insufficient.

Some members said that it would be appropriate for the Bank to devise ways to prevent concentration of its loans in particular financial institutions in disaster areas, by setting the maximum amount of loans to each financial institution based on such factors as the amount of lending made by each institution, so that the Bank could support their lending activity effectively.

Moreover, some members expressed the view that the Bank should make certain deliberations when setting the conditions for loans, to reassure financial institutions. On this point, many members commented that the duration of each loan could be set at one year to meet the needs for longer-term funds among financial institutions in disaster areas, and the loan rate could be set at as low as 0.1 percent per annum, based on the current policy interest rate.

Many members expressed the view that it would be appropriate to set the deadline for new applications for loans by taking into account the Bank's objective of supporting financial institutions' initial efforts to meet demand for funds for restoration and rebuilding. A few members said that it would also be appropriate to set the deadline for new applications for loans at a relatively distant date to reassure financial institutions in disaster areas.

Many members said that it would be appropriate to deliberate further on broadening the range of eligible collateral for money market operations together with the introduction of a new funds-supplying operation. They continued that, in this case, it was necessary to research and examine the situation of financial assets that could be newly included in the range of eligible collateral and consider possible effects on the Bank's business operations.

Based on the above discussion, members agreed that it would be appropriate to compile a basic preliminary framework for the new funds-supplying operation and make it public immediately after the meeting. In order to create a specific plan based on research on the situation of financial institutions in disaster areas and their needs, the chairman instructed the staff to examine the specifics of the two measures -- namely, a new funds-supplying operation and broadening of the range of eligible collateral for money market operations -- and report back at the next Monetary Policy Meeting.

Lastly, as for the future conduct of monetary policy, members confirmed that the Bank would continue to carefully examine the outlook for economic activity and prices, including the possible effects of the disaster, and take appropriate policy actions as necessary.

A few members said that it was important to work to enhance the growth potential of Japan's economy during the process of rebuilding, and that, from this viewpoint, the Bank needed to thoroughly deliberate on ways that would be appropriate to utilize the existing framework for the fund-provisioning measure to support strengthening the foundations for economic growth. One member -- referring to some recent views that the Bank should underwrite JGBs to fund restoration and rebuilding -- expressed the opinion that such an action might initially seem to work well, but lessons drawn from history showed that it would eventually result in severe inflation and thereby inflict substantial damage on people's living situation. This member continued that the Bank needed to keep working to gain the wider public's understanding on this point. In relation to this, a few members expressed the view that, if confidence in the currency were impaired due to underwriting of JGBs by the Bank as the central bank, this might lead to a rise in long-term interest rates or instability in financial markets, and hamper the smooth issuance of JGBs. One of these members added that confidence in the currency constituted an important part of the infrastructure for Japan's financial and economic activity, and it was very important to firmly maintain such an infrastructure to ensure stability in people's living situation.

IV. Remarks by Government Representatives

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

(1) Due to the effects of the disaster, the Japanese economy was suffering from such problems as damage to firms' production facilities, disruption of the supply chain, and constraints on electric power supply, and the outlook was attended by an extremely high degree of uncertainty.

(2) After the earthquake, the government had been taking actions such as delivering supplies for emergency assistance financed through contingency funds, and, in terms of quasi-governmental financing, setting up special consulting desks as well as providing loans with favorable lending rates. The Diet approved the budget for fiscal 2011 on March 29. Regarding fiscal management, the government considered it necessary to place top priority on making its utmost efforts to deal with the disaster. As necessary measures became clear, the government would continue to promptly implement them by releasing contingency funds and formulating supplementary budgets.

(3) The government would like to express its appreciation for the Bank's swift and appropriate actions after the earthquake, such as increasing the amount of the Asset Purchase Program, which was decided at the previous Monetary Policy Meeting, and providing ample funds to the market. The government would exert every possible effort to support disaster victims as well as restoration and rebuilding. It expected the Bank to continue taking decisive monetary policy actions while considering the effects of the disaster on the economy and markets, as well as the progress of rebuilding. The government welcomed the Bank's initiative to support financial institutions in disaster areas, which was discussed at this meeting, as an action that would contribute to restoration and rebuilding, and it expected the Bank to formulate specifics of the measure diligently so that its implementation would activate support for the disaster areas.

(4) Although there had been media reports that the government might fund rebuilding costs by issuing JGBs to be underwritten by the Bank, the government had never considered this to be an option. In view of the fact that Article 5 of the Public Finance Act

stipulated that government securities should be issued in the market in principle based on lessons from historical experience, the government deemed it necessary to take a cautious stance on the underwriting of government securities by the Bank.

The representative from the Cabinet Office made the following remarks.

(1) The Japanese economy, which was starting to pick up, was surrounded by concerns about the effects of the disaster. The damage to the Japanese economy from the Great East Japan Earthquake was judged to be larger than that caused by the Great Hanshin-Awaji Earthquake.

(2) As for the outlook, it was likely that the disruption in the supply of parts, constraints on electric power supply, the crisis at the nuclear power plant, and the dampening of production due to the disaster would cover a wide area and last for a prolonged period. There were other downside risks to the economy, such as the effects of fluctuations in global financial markets and the rise in crude oil prices. Moreover, amid the current deflationary situation, it was difficult to determine the effects of the disaster on prices at this point, and the government considered it necessary to monitor such effects carefully.

(3) The government, taking into account the effects of the disaster, would do its utmost to achieve stability in the normal routines of people's living situation and of economic activity. In order to accomplish this, the government would first aim to rescind a portion of the budget for fiscal 2011 and decide on the content of a supplementary budget by the end of April, to prepare to assist disaster victims, secure employment, and help businesses start to rebuild. Moreover, it would proceed with efforts to reconstruct the disaster areas. In doing so, the government would work to firmly secure market confidence in public finance.

(4) The Bank had been taking swift responses since the earthquake, including the increase in the amount of the Asset Purchase Program, mainly of the purchases of risk assets. The government hoped that the Bank would take all possible measures to firmly support people's living situation and the economic activity of firms in the disaster areas, placing particular attention on ensuring the needs of these areas, as had been discussed at the meeting, and to ensure stability in financial markets and the financial system while continuing to sufficiently exchange views and keep close contact with the government.

V. Votes

Based on the above discussions, members shared the view 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 to 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 to 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, Mr. T. Noda, Mr. S. Nakamura, Mr. H. Kamezaki, Mr. R. Miyao, Mr. Y. Morimoto, and Ms. S. Shirai.

Votes against the proposal: None.

VI. Discussion on the Statement on Monetary Policy

Members discussed the Statement on Monetary Policy, and it was put 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).

VII. Approval of the Minutes of the Monetary Policy Meeting

The Policy Board approved unanimously the minutes of the Monetary Policy Meeting of March 14, 2011 for release on April 12, 2011.

Attachment 1

April 7, 2011
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,[8] 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 to 0.1 percent.

2. Since the Great East Japan Earthquake occurred, the Bank, with a view to ensuring stability in financial markets, has been providing ample funds sufficient to meet demand in the markets. It further strengthened monetary easing by increasing the amount of the Asset Purchase Program, mainly of the purchases of risk assets, by about 5 trillion yen.

    In addition to such measures, at today's meeting, the Bank judged it necessary to introduce a funds-supplying operation that provides financial institutions in disaster areas with longer-term funds in order to support their initial response efforts to meet the future demand for funds for restoration and rebuilding. The Bank accordingly compiled a preliminary framework for the operation as in Attachment 2. It also judged it appropriate to broaden the range of eligible collateral for money market operations with a view to securing sufficient financing capacity of financial institutions

[8] Voting for the action: Mr. M. Shirakawa, Mr. H. Yamaguchi, Mr. K. G. Nishimura, Mr. T. Noda, Mr. S. Nakamura, Mr. H. Kamezaki, Mr. R. Miyao, Mr. Y. Morimoto, and Ms. S. Shirai.
Voting against the action: None.

in disaster areas. The Chairman instructed the staff to examine the specifics of these two measures and report back at the next Monetary Policy Meeting.

3. Japan's economy is under strong downward pressure, mainly on the production side, due to the effects of the earthquake disaster. Specifically, the earthquake has sharply dampened production in some areas by damaging production facilities, disrupting the supply chain, and constraining electric power supply; exports and domestic private demand have been affected accordingly. The year-on-year rate of decline in the CPI (excluding fresh food) has continued to slow. As for financial developments since the earthquake, the financial intermediation function has been maintained and smooth fund settlement has also been secured. Financial markets have been stable as a whole. Meanwhile, financial conditions have generally continued to ease, while weakness has been observed in the financial positions of some firms, mainly small ones, since the earthquake.

4. According to the Bank's baseline scenario, Japan's economy is likely to remain under strong downward pressure, mainly on the production side, for the time being, but is expected to return to a moderate recovery path -- as supply-side constraints are mitigated and production regains traction -- backed by an increase in exports reflecting the improvement in overseas economic conditions and by a rise in demand for restoring capital stock. The year-on-year rate of change in the CPI is expected to become slightly positive in the near future.[9]

5. In the area of economic activity, there are some upside risks such as faster growth in emerging and commodity-exporting economies due to robust domestic demand and capital inflows from overseas. However, there are downside risks associated with developments in global financial markets and uncertainties, albeit reduced, about the outlook for the U.S. and European economies. Moreover, there is high uncertainty about the possible effects of the earthquake disaster on Japan's economy. Meanwhile, as for the rise in international commodity prices, the high growth in emerging and

[9] The year-on-year rate of change in the CPI is likely to be revised downward with the base-year change scheduled for August 2011.

commodity-exporting economies that lies behind the price rise would lead to an increase in Japan's exports, while a decline in real purchasing power reflecting deterioration in the terms of trade could reduce private domestic demand in Japan. Regarding the outlook for prices, there is a possibility that inflation will rise more than expected if international commodity prices increase further, while there is also a risk that the rate of inflation will deviate downward from the Bank's baseline scenario due, for example, to a decline in medium- to long-term inflation expectations.

6. The Bank will continue to carefully examine the outlook for economic activity and prices, including the possible effects of the disaster, and take appropriate policy actions as necessary.

Attachment 2

Preliminary Framework for the "Funds-Supplying Operation to Support Financial Institutions in Disaster Areas"

1. Eligible Counterparties

   Financial institutions that have business offices in disaster areas and are already counterparties in the Bank of Japan's "funds-supplying operations against pooled collateral at all offices" and wish to be counterparties for this operation.

   For financial cooperatives that are not counterparties of the "funds-supplying operations against pooled collateral at all offices" nor hold current accounts at the Bank, the Bank will consider to provide them with funds through counterparty financial institutions.

   Note that disaster areas are areas designated under the Disaster Relief Act, No. 118, 1947, with regard to the Great East Japan Earthquake -- that is, the whole areas of Iwate, Miyagi, and Fukushima prefectures and some areas of Aomori, Ibaraki, Tochigi, and Chiba prefectures.

2. Form of Loans

   Loans shall be provided against pooled collateral.

3. Duration of Loans

   The duration of each loan shall be one year.

4. Loan Rates

   The loan rate shall be 0.1 percent per annum.

5. Total Amount of Loans

   The total amount of loans shall be 1 trillion yen.

6. Maximum Amount of Loans per Counterparty and Deadline for New Applications for Loans

   The Bank shall determine the maximum amount of loans to each counterparty and the deadline for new applications for loans, taking into account, for example, counterparties' lending conditions in disaster areas.