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May 27, 2013

Bank of Japan

Minutes of the Monetary Policy Meeting

on April 26, 2013

(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 Friday, April 26, 2013, from 9:02 a.m. to 1:30 p.m.[1]

Policy Board Members Present

Mr. H. Kuroda, Chairman, Governor of the Bank of Japan

Mr. K. Iwata, Deputy Governor of the Bank of Japan

Mr. H. Nakaso, Deputy Governor of the Bank of Japan

Mr. R. Miyao

Mr. Y. Morimoto

Ms. S. Shirai

Mr. K. Ishida

Mr. T. Sato

Mr. T. Kiuchi

Government Representatives Present

Mr. S. Yamaguchi, Senior Vice Minister of Finance, Ministry of Finance

Mr. K. Matsuyama, Vice Minister for Policy Coordination, Cabinet Office

Reporting Staff

Mr. M. Amamiya, Executive Director

Mr. N. Kinoshita, Executive Director

Mr. K. Momma, Executive Director (Assistant Governor)

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

Mr. K. Kamiyama, Head of Policy Planning Division, Monetary Affairs Department

Mr. S. Aoki, Director-General, Financial Markets Department

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

Mr. K. Kamada, Head of Economic Research Division, Research and Statistics Department

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

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[1] The minutes of this meeting were approved by the Policy Board at the Monetary Policy Meeting held on May 21 and 22, 2013 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.

Secretariat of the Monetary Policy Meeting

Mr. N. Yoshioka, Director-General, Secretariat of the Policy Board

Mr. N. Fukunaga, Director, Deputy Head of Planning and Coordination Division, Secretariat of the Policy Board

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

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

I. Summary of Staff Reports on Economic and Financial Developments[2]

A. Money Market Operations in the Intermeeting Period

The Bank, in accordance with the guideline decided at the previous meeting on April 3 and 4, 2013, had been providing funds through purchases of Japanese government bonds (JGBs) and other measures.[3] In this situation, the amount outstanding of the monetary base had been in the range of 140-157 trillion yen.

B. Recent Developments in Financial Markets

Money market rates, including longer-term ones, had been at low levels. The uncollateralized overnight call rate had been at a level below 0.1 percent. General collateral (GC) repo rates had been at around 0.1 percent. As for interest rates on term instruments, yields on treasury discount bills (T-Bills) including those with longer maturities rose somewhat, and had recently been at around 0.1 percent. Rates on longer-term interbank instruments had declined very slightly.

With regard to long-term interest rates, yields on 2- and 5-year JGBs had been picking up, due in part to a subsidence in expectations for lowering the interest rate applied under the complementary deposit facility. Yields on 10- and 20-year JGBs had also been increasing. Specifically, they had declined significantly immediately after the previous meeting, but increased thereafter, primarily reflecting market participants' cautious investment stance, which stemmed from heightening volatility. Those yields had recently started to decline again, however, since the volatility had decreased as a positive response to the Bank's decision to revise the operational outline for outright purchases of JGBs, and because the bidding had gone relatively smoothly over time. The Nikkei 225 Stock Average had been on a rising trend as a positive response to policy decisions made at the previous meeting and the subsequent further depreciation of the yen. Prices for Japan real estate investment trusts (J-REITs) had been increasing, but exhibited signs of a halt to the sharp rise since autumn 2012. Yield spreads between corporate bonds and JGBs were more or less unchanged at low levels on the whole, reflecting solid demand from investors, although those on some corporate bonds remained wide due to concerns over deterioration

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

[3] The guideline was as follows:

The Bank of Japan will conduct money market operations so that the monetary base will increase at an annual pace of about 60-70 trillion yen.

in issuer companies' business performance. In the foreign exchange market, the yen had been depreciating significantly against the U.S. dollar, following policy decisions made at the previous meeting.

C. Overseas Economic and Financial Developments

Overseas economies had been moving out of the deceleration phase that had continued since last year and were gradually heading toward a pick-up.

The U.S. economy had been on a moderate recovery trend and improvement had begun to spread to corporate activity as well. Exports were bottoming out. Business sentiment, which had been cautious for a while, was on an improving trend, and business fixed investment had begun to pick up. Although effects of the expiration of the payroll tax cut had been observed, private consumption had been increasing moderately on the whole as the employment situation followed an improving trend. Housing investment had also been picking up steadily, although it remained at a depressed level. On the back of these developments in demand at home and abroad, production had returned to an increasing trend. As for prices, the year-on-year rate of increase in the consumer price index (CPI) for all items had decelerated somewhat, mainly as a result of the decline in energy prices. However, the year-on-year rate of increase in the CPI for all items less food and energy, or the core CPI, had been more or less flat.

Economic activity in Europe continued to recede slowly. Exports had begun to bottom out and further deterioration in business and household sentiment was coming to a halt on the whole, albeit with some differences in degree by country. Nevertheless, both business fixed investment and private consumption had been declining, primarily as a result of continuing fiscal austerity. Given these developments, production continued to decrease, reflecting sluggish domestic demand. As for prices, while slack in supply and demand conditions was exerting downward pressure on prices, the year-on-year rates of increase in both the Harmonized Index of Consumer Prices (HICP) for all items and the HICP excluding energy and unprocessed food had declined somewhat. Meanwhile, economic activity in the United Kingdom had been sluggish.

With regard to Asia, the Chinese economy had been stabilizing in reflection of firm domestic demand. Private consumption had been firm on the back of a favorable employment and income situation. The pace of increase in fixed asset investment had been solid, mainly due to rises in infrastructure investment and real estate investment. Exports were heading toward a pick-up. Reflecting these developments in demand at home and abroad, production had been stabilizing as well. Regarding the NIEs and the ASEAN countries, these economies had been picking up on the whole, but the pace continued to be moderate in the corporate sector. Exports were gradually heading toward a pick-up and production had shown signs of stabilizing. Nevertheless, growth in business fixed investment, particularly in the NIEs, had been sluggish as business sentiment remained cautious. Meanwhile, private consumption had been firm, especially in the ASEAN countries, where consumer sentiment was on a rising trend on the back of the favorable employment and income situation. As for prices, inflation rates had generally been more or less flat, although there were regional differences. In India, the economy remained in a state of deceleration.

In global financial markets, some sentiment had become cautious due to adjustments in optimistic views regarding the pace of recovery in the global economy following the release of economic indicators that were weaker than market expectations. European stock prices declined, and developments in U.S. stock prices lacked momentum, although they had been moving in a high range. Long-term interest rates in the United States and Germany also declined. Nevertheless, the tail risk that the European debt problem might lead to global financial market turmoil and a significant global economic downturn had generally decreased owing to the introduction of various backstops, and investors' risk aversion remained abated on the whole. In peripheral European countries, yields on government bonds had been declining despite uncertainty remaining over the situation in Italy and Slovenia. The funding conditions of European financial institutions at the time of the Bank's previous Monetary Policy Meeting temporarily tightened somewhat following the disruptions associated with financial support for Cyprus, but regained stability thereafter. Specifically, the credit spreads of bank debentures -- which had widened temporarily -- had started to narrow again, and spreads between interest rates on euro-denominated term instruments and overnight index swap (OIS) rates had remained flat at low levels. With regard to corporate bond markets in the United States and Europe, credit spreads had been more or less unchanged on the whole, and the issuance of high-yield bonds continued to be steady. Meanwhile, in a situation where the capital inflow into emerging and commodity-exporting economies -- through investment funds in particular -- was decreasing, these economies' stock prices had generally been declining and the currencies of commodity-exporting economies had been weak.

D. Economic and Financial Developments in Japan

1. Economic developments

Exports showed evidence of bottoming out as changes in real exports had become positive on a month-on-month basis in March 2013, and as those in the January-March quarter had risen by 1.5 percent on a quarter-on-quarter basis, marking an increase for the first time in three quarters.

As for public investment, the amount of public construction completed -- a measure that reflected the progress of public works -- continued to move up, albeit marginally, by 0.4 percent in the January-February period compared with the October-December quarter of 2012, after having risen for four quarters in a row through that quarter on a quarter-on-quarter basis. The value of public works contracted -- a measure that reflected public works orders -- recently decreased after having been more or less flat at a relatively high level since the April-June quarter of 2012, but this drop was expected to be temporary.

While improvement in business sentiment had become clear, there had been signs of a halt to the decrease in the aggregate supply of capital goods, and the proportion of small firms that had carried out business fixed investment had increased in the January-March quarter. Nevertheless, it was still difficult to judge whether business fixed investment as a whole had stopped decreasing, considering that machinery orders remained weak.

Many indicators for private consumption provided signs that it was becoming increasingly resilient, as seen in, for example, the climb in sales at department stores and chain stores assisted partly by (1) the improvement in consumer sentiment, primarily reflecting the rise in stock prices; and (2) the upward pressure resulting from higher temperatures.

Regarding housing investment, sales of newly built condominiums in the Tokyo metropolitan area were generally on an increasing trend, and the contract ratio for new condominiums, reflecting the number purchased in the initial month of sale, had generally been above 70 percent, the benchmark for assessing market conditions.

As for prices, international commodity prices had been exhibiting sluggish movements lately. The three-month rate of change in the domestic corporate goods price index (CGPI) continued to be positive -- registering an increase of 0.8 percent in March after rising by 1.1 percent in February -- reflecting movements in foreign exchange rates. The year-on-year rate of change in the CPI (all items less fresh food) had been slightly negative, due to the reversal of the previous year's movements in durable consumer goods and energy-related goods.

2. Financial environment

Financial conditions were accommodative.

With regard to credit supply, firms continued to see financial institutions' lending attitudes as being on an improving trend. Issuing conditions for CP and corporate bonds remained favorable on the whole. As for credit demand, firms showed signs of increasing their demand mainly for working capital and funds related to mergers and acquisitions, while the year-on-year rate of increase in the amount outstanding of bank lending had risen somewhat. Meanwhile, firms retained their recovered financial positions on the whole.

II. Summary of Discussions by the Policy Board on Economic and Financial Developments and the April 2013 *Outlook for Economic Activity and Prices*

A. Economic Developments

In terms of global financial markets, members shared the recognition that the tail risk that the European debt problem might lead to global financial market turmoil and a significant global economic downturn had decreased owing to the introduction of various backstops, and that investors' risk aversion remained abated.

Members concurred that overseas economies had been moving out of the deceleration phase that had continued since last year and were gradually heading toward a pick-up. As for the outlook, they shared the view that the growth rates of these economies -- in particular, the United States and China -- would gradually pick up, albeit moderately, as global financial markets would remain generally stable. On this basis, one member pointed out that a series of economic indicators released in the United States and China since the previous meeting were weaker than market expectations, although these indicators did not influence the members' view that overseas economies would continue to generally pick up. In relation to the forecast for global growth presented in the *World Economic Outlook* released in April 2013 by the International Monetary Fund (IMF), which was revised downward from that made in January, a different member noted that it was necessary to pay attention to the risk that the timing of a pick-up in growth rates would be delayed. On the other hand, one member, while admitting that there were concerns -- triggered by the recent weak economic indicators -- over whether overseas economies would recover, expressed the view that these economies were likely to gradually recover since (1) no particular turmoil -- such as that seen in the past few years -- was observed in European economies; and (2) a recovery in the U.S. housing market was becoming full-fledged.

Members shared the recognition that the U.S. economy had been on a moderate recovery trend, with the household sector being resilient, and that improvement had begun to spread to the corporate sector as well. On the point that some economic indicators such as retail sales had lacked strength recently, one member said that the momentum for economic recovery had nevertheless been maintained as the number of employees was increasing steadily on the whole. A different member pointed to a possibility that households' expected income might have decreased, in a situation where adjustments in household debt had been protracted and slack in supply and demand conditions in the labor market had persisted after the Lehman shock. As for the outlook, members concurred that the economy was likely to continue recovering at a moderate pace, supported by accommodative financial conditions.

Members shared the recognition that economic activity in the euro area continued to recede slowly. As for the outlook, they shared the view that, on the whole, the euro area economy was likely to continue receding slowly, as fiscal austerity measures continued to be implemented for the time being, particularly in peripheral countries. One member expressed the recognition that, with the gradual pick-up in the global economy, the economies in the euro area -- especially in core countries -- were likely to gradually emerge from a recession induced by a pick-up in exports, but this would take considerable time.

Members shared the recognition that the Chinese economy had been stabilizing in reflection of firm domestic demand. On this basis, some members -- pointing to the fact that the real GDP growth rate for the January-March quarter of 2013 had slowed, and that materials industries such as iron and steel had continued to make production adjustments --

expressed the view that the economic recovery was not yet full-fledged. A different member noted that improvements in the Chinese economy had recently fallen off somewhat, affected by the government's measures to restrain the rise in real estate prices and its efforts to promote frugality, but that the economy remained on a gradual recovery path. As for the outlook, members shared the view that the economic recovery would become evident as exports would gradually pick up amid firm domestic demand, although the pace of economic growth was likely to be more moderate than before.

Regarding the NIEs and the ASEAN countries, members concurred that these economies had been picking up on the whole, but that the pace of the pick-up remained moderate in the corporate sector. As for the outlook, they shared the view that, in a situation where solid private consumption underpinned these economies, the pace of recovery was likely to increase in turn as exports picked up gradually.

Members concurred that financial conditions in Japan were accommodative. In terms of the outlook, they shared the view that such conditions were likely to ease further with improvement in economic conditions, because quantitative and qualitative monetary easing was likely not only to work through such transmission channels as long-term interest rates and asset prices, but also to lower real interest rates through a pick-up in expected inflation rates caused by fundamental changes in expectations.

Regarding financial market developments following the introduction of quantitative and qualitative monetary easing, members agreed that the bond market in particular had temporarily shown somewhat large fluctuations immediately thereafter, but the market had recently regained stability due in part to the Bank's decision to revise the operational outline for outright purchases of JGBs. In this regard, a few members noted that the Bank's large-scale JGB purchases -- which would lead to downward pressure on interest rates -- and its strong determination to achieve the "price stability target" at the earliest possible time -- which would lead to upward pressure on interest rates -- might initially have been perceived by market participants as contradictory, and this perception had led to fluctuations in financial markets. One of these members added that potential instability remained in the bond market. A different member commented that a rise in interest rates amid the Bank's large-scale purchases of JGBs could indicate a pick-up in expected inflation rates and an underlying upturn in economic activity. One member said that, because financial institutions' rebalancing of their portfolios depended on developments in nominal interest rates, there was concern that such rebalancing would be delayed as a result of a rise in interest rates. Regarding the recent rise in asset prices, one member -- referring to some concern being raised over an asset bubble -- expressed the view that this rise reflected the fundamentals, such as corporate profits, and therefore could not be regarded as an overvaluation. Meanwhile, some members expressed the recognition that, in order for quantitative and qualitative monetary easing to be sufficiently effective, it was necessary that the Bank ensure market stability by explaining its policy intentions thoroughly and conducting money market operations in an appropriate manner.

Based on the above deliberations on economic and financial conditions abroad, as well as Japan's financial conditions, members discussed the state of Japan's economy. They shared the view that exports had recently bottomed out and were likely to pick up, supported by a moderate recovery in overseas economies and the yen's depreciation in the foreign exchange market. Members agreed that public investment was likely to continue increasing at a high level for the time being, mainly reflecting various economic measures and increases in the budget associated with reconstruction after the earthquake disaster. Some members expressed the view that private consumption had been increasingly resilient, as evidenced by growing sales of high-end goods brought about by improvement in sentiment and wealth effects, mainly reflecting the rise in stock prices. On this basis, a few members added that private consumption at present was firmer relative to the employment and income situation, and therefore attention should be paid to its sustainability. One member expressed the view that housing investment had become active, as seen in the increasing trend in sales of condominiums. Based on this discussion, members concurred that the economy had stopped weakening and had shown some signs of picking up.

Members agreed that the year-on-year rate of change in the CPI (all items less fresh food) had been slightly negative. Some members said that, according to breakeven inflation (BEI) rates -- that is, the expected inflation rates calculated from the information content in inflation-indexed bonds -- and to the results of various surveys, markets' and households' inflation expectations had been rising recently. In response, one member noted that developments in these rates and survey results might have factored in the heightened possibility of the consumption tax hikes, and therefore it could not be directly interpreted from such developments that inflation expectations had risen. On the other hand, a different member noted that BEI rates had been rising since the end of November

2012, and that the pace had been accelerating since the Bank's decision to introduce quantitative and qualitative monetary easing. This member then expressed the view that this development reflected market views regarding the Bank's "regime change" in its monetary policy, rather than a rise in expectations for the consumption tax hikes.

B. Outlook for Economic Activity and Prices

In terms of the projection period in the *Outlook for Economic Activity and Prices* (hereafter the Outlook Report), many members pointed to the fact that the effects of monetary policy required a certain time lag to permeate economic activity and prices, and that at present the projection periods for the forecasts made and released by many central banks were for around three years. These members then suggested that, taking into account these facts, the Bank should consider extending the projection period. Some members said that it would be meaningful at this time -- when the Bank introduced quantitative and qualitative monetary easing as a measure to achieve the price stability target at the earliest possible time, with a time horizon of about two years -- to secure a projection period of sufficient length to enable the Bank to thoroughly examine policy effects. A few members -- while acknowledging this meaningfulness -- pointed out that, since the extension of the projection period would heighten uncertainty regarding the outlook, it would not necessarily contribute to enhancing the transparency of the Bank's communication to the public. Based on this discussion, members concurred that it was appropriate for the Bank to move up by six months the release of its forecasts covering the projection period through fiscal 2015 and extend the projection period to around three fiscal years, to present the Bank's recognition of the outlook for Japan's economic activity and prices in a clear and intelligible manner.

With regard to the baseline scenario of the outlook for Japan's economic activity, members shared the following view: (1) the economy was likely to return to a moderate recovery path around mid-2013, mainly against the background that domestic demand remained resilient due to the effects of monetary easing as well as various economic measures, and that growth rates of overseas economies gradually picked up; and (2) thereafter, while Japan's economy would be affected by the front-loaded increase and subsequent decline in demand prior to and after the two scheduled consumption tax hikes, it was likely to continue growing at a pace above its potential, as a trend, as a virtuous cycle among production, income, and spending was maintained. On this basis, they agreed that, compared with the projection in the January 2013 interim assessment, Japan's economic growth rates were likely to be higher than the ones presented in January, mainly due to the introduction of quantitative and qualitative monetary easing, an improvement in financial market conditions, and an increase in public investment.

Regarding developments in economic activity in fiscal 2013, members shared the view that, in a situation where a virtuous cycle among production, income, and spending would start working, triggered by increases in public investment and exports, the economy was likely to return to a moderate recovery path around mid-2013. They concurred that the growth rate for fiscal 2013 was projected to be significantly elevated given that a considerable front-loaded increase in demand prior to the consumption tax hike was anticipated in the second half of the fiscal year. They shared the recognition that, from fiscal 2014 toward fiscal 2015, while affected by fluctuations in demand stemming from the scheduled consumption hikes, the economy was likely to continue growing at a pace above its potential, as a trend, as positive developments in domestic private demand were likely to continue, supported by increasing exports and monetary easing effects.

In terms of the outlook for prices, excluding the direct effects of the consumption tax hikes, most members expressed the view that the year-on-year rate of change in the CPI was likely to follow a rising trend, reflecting factors such as the improvement in the aggregate supply and demand balance as well as the rise in medium- to long-term inflation expectations, and it was likely to reach around 2 percent -- the price stability target -- toward the latter half of the projection period. One member pointed out the importance of the process in which the economic and price situation would improve in line with the baseline scenario and the general public would accordingly expect the economic and price situation to move in line with this scenario. This member then said that, with such a virtuous cycle in place, the general public's short-term inflation expectations, the medium- to long-term inflation anchor, and the actual rate of inflation would rise through a reinforcement of each other. As for price developments prior to and after the consumption tax hikes, one member pointed out that price increases by retailers -- in accordance with the extent to which supply and demand balance improved -- might be postponed due to concerns over further downward pressure on consumption. Regarding inflation expectations, one member expressed the recognition that fundamental changes in firms' and households' deflationary expectations would materialize as the year-on-year rate of increase in the CPI continued to rise. A few members said that it was important for the Bank to present its strong determination to achieve the price stability target in order to eliminate deflationary expectations, which had taken root in Japan's economy under a long period of deflation. One of these members added that, taking into account the developments in various markets during the intermeeting period, which reflected policy effects factored in particularly by foreign investors, it was likely that domestic economic entities would increase their inflation expectations as economic activity improved. In response, a few members pointed out that it seemed difficult to achieve around 2 percent inflation toward the latter half of the projection period, since it was highly uncertain whether changes in inflation expectations would lead to a rise in the actual rate of inflation, as was how the former would lead to the latter. One of these members added that, if the Bank presented a projection on the inflation rate with high uncertainty and the actual rate turned out to be lower, there was a significant concern that this could undermine the credibility of the Bank's outlook for prices and its monetary policy.

Members also discussed upside and downside risk factors to the baseline scenario.

Regarding the outlook for economic activity, members noted the following upside and downside risk factors: (1) developments in global financial markets; (2) uncertainty regarding developments in overseas economies; (3) firms' and households' medium- to long-term growth expectations; (4) the extent of the front-loaded increase and subsequent decline in demand prior to and after the consumption tax hikes; and (5) fiscal sustainability in the medium to long term. With regard to developments in overseas economies, members shared the view that the U.S. economy might post higher growth, mainly against the background of progress in balance-sheet repair, strengthening of monetary easing effects, especially in the housing market, and the positive impact of new energy sources. They continued that, on the other hand, the economy might also register lower growth, mainly due to fiscal problems. One member pointed out that there was a risk that the Chinese economy would not make a smooth transition to stable growth and instead register lower growth, given that many industries in the economy were burdened with excess capital stock for which significant adjustments could take place in the process of declining growth expectations. A different member expressed the view that, even if the growth rates of overseas economies rose as expected, this might not lead to increases in Japan's exports and production of capital goods and parts -- for which it had a competitive advantage -- and in related business fixed investment in the case of a delay in the recovery of business fixed investment worldwide. With regard to firms' and households' medium- to long-term growth expectations, one member noted that, if the government's regulatory and institutional reforms did not make progress and firms' efforts to tap potential demand did not proceed, there was a risk that such expectations would not rise. As for the effects of the consumption tax hikes, one member expressed the view that, under the extremely accommodative financial conditions, if the increase in inflation rates -- in part reflecting the effects of the rise in the consumption tax rate -- were considerably higher than the public expected, there was a risk that the effects of a decline in the real income of households would be greater than those expected by the Bank. This member then said that it was important to also garner the public's recognition of the outlook for prices, including the effects of the rise in the consumption tax rate. With regard to fiscal sustainability in the medium to long term, members shared the recognition that there was a possibility that Japan's economy would deviate upward from the baseline scenario if the path toward fiscal consolidation became evident and people's concerns regarding the future were alleviated.

Members pointed to the following as upside and downside risk factors specific to the outlook for prices: (1) developments in firms' and households' medium- to long-term inflation expectations; (2) the responsiveness of prices to the aggregate supply and demand balance; and (3) developments in import prices. With regard to medium- to long-term inflation expectations, members shared the view that, while there was a possibility that firms' and households' inflation expectations might not readily rise, due to their possible formation reflecting moderate price declines in the past, there was also a possibility that they would rise relatively quickly in response to fundamental changes in expectations. On the responsiveness of prices to the aggregate supply and demand balance, members concurred that, under a highly competitive environment sustained over time, it was uncertain whether firms would raise prices and wages in accordance with the extent to which the supply and demand balance tightened. In relation to developments in import prices, one member pointed out that, as the global economy recovered amid continued worldwide monetary easing, the uptrend in international commodity prices might accelerate due in part to the effects of the so-called financialization of commodities, and prices in Japan might post a higher increase following a rise in import prices.

Based on this discussion on upside and downside risk factors to the outlook for Japan's economic activity and prices, members shared the recognition that there was high uncertainty regarding developments in overseas economies and medium- to long-term inflation expectations in particular, and that attention should continue to be paid to the effects of these developments on Japan's economic activity and prices.

Based on the above considerations, members assessed the economic and price situation from two perspectives.

Members made an assessment in terms of <u>the first perspective</u>; an assessment of the baseline scenario of the outlook for economic activity and prices through fiscal 2015. Most members expressed the view that Japan's economy was likely to achieve around 2 percent inflation and return to a sustainable growth path toward the latter half of the projection period. Counter to this view, a few members said that it seemed difficult to achieve around 2 percent inflation toward the latter half of the projection period.

Members then made an assessment in terms of <u>the second perspective</u>; the examination of the risks considered most relevant to the conduct of monetary policy. With regard to economic activity, they shared the recognition that upside and downside risks could be assessed as being balanced, although uncertainty remained high, including over developments in overseas economies. Most members expressed the view that risks on the price front also could be assessed as being largely balanced, although considerable uncertainty surrounded developments in medium- to long-term inflation expectations. Counter to this view, one member pointed out that risks were tilted to the downside. Members then reaffirmed that, in examining financial imbalances from a longer-term perspective, there was no sign at this point of excessively bullish expectations in asset markets or in the activities of financial institutions; nevertheless, due attention needed to be paid to the fact that financial institutions' holdings of JGBs remained at an elevated level while the amount outstanding of government debt had shown a cumulative increase. One member noted that prices of various assets had risen under large-scale monetary easing in advanced economies. This member continued that it was necessary to carefully examine risks associated with such rises because, given the experience of the Lehman shock, once there were changes in an asset market, these could affect a wide range of markets and in turn exert significant effects on economic activity. With regard to the descriptions of the assessments of the economic and price situation from the two perspectives in "The Bank's

View" in the Outlook Report, one member said that the Bank should provide the descriptions in relevant sections appropriately, rather than together in an independent chapter, to enhance clarity and intelligibility for the public.

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

Members discussed 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 conduct money market operations so that the monetary base would increase at an annual pace of about 60-70 trillion yen.

With respect to the future conduct of monetary policy, most members shared the view that the Bank would continue with quantitative and qualitative monetary easing, aiming to achieve at the earliest possible time the price stability target of 2 percent with a time horizon of about two years, as long as it was necessary to maintain this target in a stable manner. These members continued that, in doing so, it would examine both upside and downside risks to economic activity and prices, and make adjustments as appropriate. In response to this view, one member expressed concern that, in a situation where it seemed difficult to achieve the price stability target in about two years, if a rise were to occur in markets' anticipation that quantitative and qualitative monetary easing would continue for a protracted period, or that extreme additional measures would be implemented, this could lead to economic instability in the medium to long term, such as through a buildup of financial imbalances. On this basis, this member said that it was appropriate to change the expression representing the Bank's commitment by stating that the time frame for continuing quantitative and qualitative monetary easing should be restricted to about two years, and that when this time frame came to an end, the Bank would review the monetary easing measures in a flexible manner. The member continued that this would ensure the credibility of monetary policy in financial markets. A different member expressed the recognition that the price stability target was meant to be a flexible framework, and the Bank should avoid giving rise to a possible misunderstanding that its ultimate goal was to achieve the specific inflation rate of 2 percent. This member continued that the price stability target could be judged to have been achieved when it was fairly possible to envisage the inflation rate reaching 2 percent based on developments in wages, for example.

In contrast, another member said that, now that the 2 percent inflation rate was set as a target, it was necessary for the Bank to conduct monetary policy so that the inflation rate would reach this level in about two years.

With regard to JGB purchases, members shared the view that the Bank's appropriate action -- such as the decision to revise the operational outline for outright purchases of JGBs in view of market participants' opinions -- had led to market stability. They also shared the recognition that, in order to continue with the smooth conduct of large-scale JGB purchases, it was important for the Bank to implement these purchases carefully while maintaining a close dialogue with market participants. Regarding the effects of JGB purchases on liquidity in the JGB market and the repo market, a few members, noting that the Bank had already relaxed the terms and conditions under the Securities Lending Facility (SLF), expressed the opinion that it should continue to deliberate on measures to prevent a decline in liquidity. As for concern about large-scale purchases leading to monetization, some members were of the view that it was essential for the Bank to gain the public's understanding by thoroughly explaining that its JGB purchases were solely conducted for the purpose of monetary policy and reiterating that it would not monetize the government debt. In terms of the average remaining maturity of JGBs to be purchased, one member said that, if the Bank forced itself to make the average remaining maturity of its JGB holdings about seven years, this would impose a substantial burden on the JGB market. This member continued that it was therefore appropriate to allow for a range in maturities.

As for maintaining the Bank's financial soundness, one member expressed the view that the significance of this was increasing further in a situation where the Bank was proceeding with large-scale purchases of financial assets under quantitative and qualitative monetary easing, and therefore it should continue to deliberate on this matter.

IV. Remarks by Government Representatives

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

(1) The government acknowledged that overcoming prolonged deflation was the top-priority task for the Japanese economy at present. It deemed that the role the Bank's monetary policy had to play in overcoming deflation was extremely important, and welcomed that the Bank was strongly committed to pursuing bold monetary easing,

particularly through the introduction of quantitative and qualitative monetary easing with the aim of achieving the price stability target of 2 percent at the earliest possible time.

(2) Regarding the April 2013 Outlook Report to be released after the meeting, the government deemed that the Bank's discussion on presenting a course toward achieving the price stability target of 2 percent contributed to fulfilling its accountability to the markets and the public. The government expected the Bank to continue to steadily pursue quantitative and qualitative monetary easing and achieve the target at the earliest possible time.

(3) The government would steadily proceed with its efforts toward implementing a flexible fiscal policy, as well as measures for strengthening the growth potential of the Japanese economy. It would do its utmost to obtain the Diet's approval of the fiscal 2013 budget and formulate a growth strategy by mid-2013. The government would also do its utmost to implement policy measures in a seamless manner toward overcoming the deflationary recession so that the benefits of economic growth would be widely distributed among the public.

(4) The government attached substantial importance to the Bank's reference to the description in the joint statement that the government would "steadily promote measures aimed at establishing a sustainable fiscal structure" in deciding at the previous meeting on April 3 and 4 to temporarily suspend the "banknote principle." The government considered fiscal consolidation a task that must be tackled now in order to bear fruit, and not as one for the future. At the Group of Twenty (G-20) Finance Ministers and Central Bank Governors' Meeting held on April 18 and 19, the Minister of Finance had explained that (1) the government would formulate a medium-term fiscal plan by mid-2013; and (2) it was determined to facilitate the economic environment, and thus would raise the consumption tax rate as scheduled. The government would do its utmost to achieve fiscal consolidation -- concurrently with economic revitalization -- by, in particular, formulating a medium-term fiscal plan by mid-2013 to achieve the fiscal consolidation targets to which the government had internationally committed itself.

The representative from the Cabinet Office made the following remarks.

(1) The Japanese economy had been showing signs of picking up recently, while weakness could be seen in some areas. As for the outlook, the economy was expected to resume its recovery gradually, supported mainly by the improvement in export conditions and the effects of the policy package and monetary policy, as well as the improvement in confidence. Recent price developments indicated that the economy remained in a mild deflationary situation. However, households' inflation expectations continued to rise and signs of improvement had been observed in the diffusion index for firms' perception of changes in output prices. In the course of the spring wage negotiations, some signs of economic growth accompanied by an increase in income had been observed so far; these included rises in bonus payments, hikes in the proportion of firms increasing their base pay, and increases in hourly wages of part-time workers.

(2) At the Council on Economic and Fiscal Policy held on April 22, 2013, the government confirmed the progress of the emergency economic measures. Excluding local public bodies, the proportion of projects for which contracts were concluded with private firms and actual work was ready to start had risen from around 15 percent in March 2013 to around 61 percent in April, and was expected to rise to around 93 percent by June. The government would continue to steadily manage the progress of the emergency economic measures so that their effects would emerge at the earliest possible time. Moreover, at the Council on Economic and Fiscal Policy, the government held discussions on the roadmap for achieving both the revitalization of the Japanese economy and fiscal consolidation. It would deliberate on the direction of the general framework of fiscal consolidation for the compilation of the Basic Policies for Economic and Fiscal Management. Furthermore, the government was holding discussions on a new growth strategy and planned to formulate it by mid-2013. With regard to the Trans-Pacific Partnership (TPP) Agreement, which was a pillar for the growth strategy, a ministerial meeting was held on April 20. Japan was scheduled to be officially approved as a TPP negotiating partner upon completion of current members' respective domestic processes.

(3) The government welcomed that the Bank was pursuing bold monetary easing, particularly by deciding to introduce quantitative and qualitative monetary easing with the aim of achieving the price stability target of 2 percent at the earliest possible time.

It expected the Bank to achieve the target at the earliest possible time, as the Bank's outlook for prices in the April 2013 Outlook Report to be released after the meeting, moved closer to 2 percent. The government also expected the Bank to provide a sufficient explanation on the effects of the recent monetary easing and its outlook for prices at the Council on Economic and Fiscal Policy.

V. Votes

A. Vote on the Guideline for Money Market Operations

Based on the above discussions, members shared the view that it was appropriate to maintain the current guideline for money market operations, so that the monetary base would increase at an annual pace of about 60-70 trillion yen.

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:

The guideline for money market operations for the intermeeting period ahead will be as follows, and will be made public by the attached statement (see Attachment).

> The Bank of Japan will conduct money market operations so that the monetary base will increase at an annual pace of about 60-70 trillion yen.

Votes for the proposal: Mr. H. Kuroda, Mr. K. Iwata, Mr. H. Nakaso, Mr. R. Miyao, Mr. Y. Morimoto, Ms. S. Shirai, Mr. K. Ishida, Mr. T. Sato, and Mr. T. Kiuchi.

Votes against the proposal: None.

B. Decision regarding the *Outlook for Economic Activity and Prices*

Members discussed the draft of "The Bank's View" in the *Outlook for Economic Activity and Prices* (consisting of "The Bank's View" and "The Background"), and formed a majority view.

Mr. T. Sato, however, formulated a proposal to make the following changes. First, with regard to the outlook for prices toward the latter half of the projection period, he proposed to change the current expression that the year-on-year rate of change in the CPI "is likely to reach around 2 percent" to a new expression that "2 percent in terms of the year-on-year rate of increase in the CPI will come into sight." Second, with regard to the baseline scenario for the outlook for economic activity and prices, he proposed changing the current expression that "Japan's economy is judged likely to achieve around 2 percent inflation" to a new expression that "Japan's economy is judged likely to head toward achieving around 2 percent inflation." Third, with regard to risks on the price front, Mr. Sato proposed changing the current expression that risks "can be assessed as being largely balanced" to a new expression that "upside and downside risks are rather asymmetric." The proposal was then put to a vote, and was defeated by a majority vote.

Votes for the proposal: Mr. T. Sato.

Votes against the proposal: Mr. H. Kuroda, Mr. K. Iwata, Mr. H. Nakaso, Mr. R. Miyao, Mr. Y. Morimoto, Ms. S. Shirai, Mr. K. Ishida, and Mr. T. Kiuchi.

Mr. T. Kiuchi formulated a proposal to make the following changes. First, with regard to the outlook for prices toward the latter half of the projection period, he proposed to change the current expression that the year-on-year rate of change in the CPI "is likely to reach around 2 percent -- the price stability target" to a new expression that "the rate of increase in the CPI is expected to rise moderately." Second, with regard to the future conduct of monetary policy, Mr. Kiuchi proposed changing the current expression that "the Bank will continue with quantitative and qualitative monetary easing, aiming to achieve the price stability target of 2 percent, as long as it is necessary for maintaining that target in a stable manner. It will examine both upside and downside risks to economic activity and prices, and make adjustments as appropriate" to a new expression that "the Bank will aim to achieve the price stability target of 2 percent in the medium to long term. On this basis, it will designate quantitative and qualitative monetary easing as an intensive measure with a time frame of about two years, and will review the monetary easing measures in a flexible manner when this time frame comes to an end." The proposal was then put to a vote, and was defeated by a majority vote.

Votes for the proposal: Mr. T. Kiuchi.

Votes against the proposal: Mr. H. Kuroda, Mr. K. Iwata, Mr. H. Nakaso, Mr. R. Miyao, Mr. Y. Morimoto, Ms. S. Shirai, Mr. K. Ishida, and Mr. T. Sato.

Ms. S. Shirai formulated a proposal to (1) improve the descriptions with regard to assessments of the economic and price situation from two perspectives, enhancing clarity and intelligibility; and (2) clarify the descriptions of risk factors. Regarding the first issue, she proposed to describe the respective assessments from the first and second perspectives at the end of Section I, entitled "Baseline Scenario of the Outlook for Economic Activity and Prices in Japan," and Section II, entitled "Upside and Downside Risks," so that they would appear in relevant sections in a comprehensive manner. As for the second issue, with regard to the effects of the consumption tax hikes -- one of the upside and downside risks to economic activity -- Ms. Shirai proposed to describe more clearly the risk of a decline in the real income of households. The proposal was then put to a vote, and was defeated by a majority vote.

Votes for the proposal: Ms. S. Shirai.
Votes against the proposal: Mr. H. Kuroda, Mr. K. Iwata, Mr. H. Nakaso, Mr. R. Miyao, Mr. Y. Morimoto, Mr. K. Ishida, Mr. T. Sato, and Mr. T. Kiuchi.

To reflect the majority view, the chairman formulated a proposal on "The Bank's View" and put it to a vote. The Policy Board decided the text of "The Bank's View" by a majority vote. It was confirmed that "The Bank's View" would be made public on April 26, 2013 and the whole report on April 27, 2013.

Votes for the proposal: Mr. H. Kuroda, Mr. K. Iwata, Mr. H. Nakaso, Mr. R. Miyao, Mr. Y. Morimoto, Ms. S. Shirai, and Mr. K. Ishida.
Votes against the proposal: Mr. T. Sato and Mr. T. Kiuchi.

Mr. T. Sato and Mr. T. Kiuchi dissented mainly because they held a more cautious view of the outlook for prices compared with the expression in "The Bank's View." Ms. S. Shirai assented as she had no objection to the content of "The Bank's View" itself, although she had formulated her proposal from the viewpoint of enhancing clarity and intelligibility and clarifying the descriptions of risk factors.

VI. Approval of the Minutes of the Monetary Policy Meeting

The Policy Board approved unanimously the minutes of the Monetary Policy Meeting of April 3 and 4, 2013 for release on May 2, 2013.

Attachment

April 26, 2013

Bank of Japan

Statement on Monetary Policy

At the Monetary Policy Meeting held today, the Policy Board of the Bank of Japan decided, by a unanimous vote, to set the following guideline for money market operations for the intermeeting period:

> The Bank of Japan will conduct money market operations so that the monetary base will increase at an annual pace of about 60-70 trillion yen.