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June 21, 2016

Bank of Japan

# Minutes of the Monetary Policy Meeting

## on April 27 and 28, 2016

(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 27, 2016, from 2:00 p.m. to 4:01 p.m., and on Thursday, April 28, from 9:00 a.m. to 11:54 a.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. K. Ishida**

**Mr. T. Sato**

**Mr. T. Kiuchi**

**Mr. Y. Harada**

**Mr. Y. Funo**

**Mr. M. Sakurai**

Government Representatives Present

Mr. M. Sakai, State Minister of Finance, Ministry of Finance[2]

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

Mr. M. Nishikawa, Vice Minister for Policy Coordination, Cabinet Office

Reporting Staff

Mr. M. Amamiya, Executive Director

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

Mr. S. Kuwabara, Executive Director

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

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[1] The minutes of this meeting were approved by the Policy Board at the Monetary Policy Meeting held on June 15 and 16, 2016 as "a document describing an outline of the discussion at the meeting" stipulated in Article 20, paragraph 1 of the Bank of Japan Act of 1997. Those present are referred to by their titles at the time of the meeting.

[2] Mr. M. Sakai was present on April 28.

[3] Mr. M. Ota was present on April 27.

Mr. H. Koguchi, Deputy Director-General, Monetary Affairs Department[4]

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

Mr. E. Maeda, Director-General, Financial Markets Department

Mr. T. Sekine, Director-General, Research and Statistics Department

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

Mr. S. Nagai, Director-General, International Department

Secretariat of the Monetary Policy Meeting

Mr. R. Yanagihara, Director-General, Secretariat of the Policy Board

Mr. H. Nakamoto, Director, Deputy Head of Planning and Coordination Division, Secretariat of the Policy Board

Mr. K. Suzuki, Head of Policy Infrastructure Division, Monetary Affairs Department[4]

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

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

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

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[4] Messrs. H. Koguchi and K. Suzuki were present on April 27 from 3:02 p.m. to 4:01 p.m.

## I. Summary of Staff Reports on Economic and Financial Developments[5]

### A. Money Market Operations in the Intermeeting Period

The Bank, in accordance with the guideline decided at the previous meeting on March 14 and 15, 2016, had been providing funds through purchases of Japanese government bonds (JGBs) and other measures.[6] In this situation, the amount outstanding of the monetary base had been in the range of 360-387 trillion yen.

### B. Recent Developments in Financial Markets

In the money market, interest rates on both overnight and term instruments had been in negative territory or at about 0 percent. The uncollateralized overnight call rate, after entering the April reserve maintenance period, had declined to a level slightly above minus 0.1 percent. As for interest rates on term instruments, yields on three-month treasury discount bills (T-Bills) had been at around minus 0.2 percent on average but had fluctuated largely, depending mainly on the supply-demand balance at the time, temporarily declining to around minus 1 percent.

The Nikkei 225 Stock Average had fallen, due primarily to the appreciation of the yen, but then rebounded, mainly led by a rise in U.S. stock prices, and was moving in the range of 17,000-18,000 yen recently. In the foreign exchange market, the yen had appreciated against the U.S. dollar, mainly reflecting expectations that the pace of the policy interest rate hike by the Federal Reserve would be moderate. It had depreciated recently, however, mainly due to speculation over the outcome of this Monetary Policy Meeting (MPM) of the Bank. The yen also had appreciated somewhat against the euro, but had depreciated recently. Yields on 10-year JGBs had moved somewhat further into negative territory, due in part to a tight supply-demand balance and declines in U.S. and German long-term interest rates.

### C. Overseas Economic and Financial Developments

Overseas economies continued to grow at a moderate pace, but the pace of growth had somewhat decelerated, mainly in emerging economies.

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

[6] 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 80 trillion yen.

The U.S. economy had been on a recovery trend, assisted by firm household spending, although the industrial production sector had lacked momentum, mainly against the background of the appreciation of the U.S. dollar and the slowdown in emerging economies. As for prices, the year-on-year rate of increase in the personal consumption expenditure (PCE) deflator for all items excluding food and energy had been in the range of 1.5-2.0 percent. That for all items had been around 1.0 percent, mainly due to the decline in energy prices.

The European economy maintained its moderate recovery as private consumption continued to increase, although exports had shown some weakness. With regard to prices, the year-on-year rate of change in the Harmonized Index of Consumer Prices (HICP) for all items had been at around 0 percent, mainly due to the decline in energy prices, but that for all items excluding energy and unprocessed food had been at around 1 percent. Meanwhile, economic activity in the United Kingdom continued to recover, led mainly by domestic demand.

With regard to emerging economies, the Chinese economy maintained its stable growth on the whole, but the pace of growth had decelerated somewhat, mainly in exports and production. In India, the economy had been growing steadily, particularly in domestic demand, partly in reflection of expectations for structural reforms and of monetary easing effects. On the other hand, economic activity in the NIEs and the ASEAN countries had been decelerating somewhat as exports and production continued to be weak, although the effects of economic stimulus measures had been observed. Economic activity in Brazil and Russia remained severe as exports had been sluggish, mainly due to low commodity prices, and as domestic demand also had declined. As for prices in emerging economies, inflation rates had been more or less flat at low levels in many countries and regions. However, inflation rates remained at high levels in some economies.

Regarding global financial markets, long-term interest rates in the United States and Europe had declined while stock prices had risen slightly, as expectations had increased since the Federal Open Market Committee (FOMC) meeting held on March 15 and 16, 2016, that the pace of the policy interest rate hike by the Federal Reserve would be moderate. Currencies and stock prices in emerging economies had risen somewhat as commodity prices followed a rising trend and the correction of the appreciation of the U.S. dollar continued.

**D. Economic and Financial Developments in Japan**

1. Economic developments

Japan's economy continued its moderate recovery trend, although exports and production had been sluggish, due mainly to the effects of the slowdown in emerging economies.

The pick-up in exports had paused recently, due mainly to the effects of the slowdown in emerging economies. While automobile-related exports, mainly those to the United States and Europe, had increased firmly, albeit with fluctuations resulting from the supply-chain disruptions caused by a steel plant accident, capital goods exports continued to be relatively weak because of capital stock overhang in emerging and commodity-exporting economies. IT-related export growth also had been sluggish recently, mainly due to weakness in smartphone-related exports to East Asia. Exports were projected to remain more or less flat for the time being, but thereafter were expected to increase moderately on the back of emerging economies moving out of their deceleration phase.

Public investment had been on a moderate declining trend, albeit remaining at a high level. It was expected to gradually level off, albeit with some fluctuations.

Business fixed investment had been on a moderate increasing trend as corporate profits had been at high levels. According to the March 2016 *Tankan* (Short-Term Economic Survey of Enterprises in Japan), business sentiment had generally stayed at a favorable level but had become cautious, mainly reflecting the slowdown in emerging economies. Firms nevertheless had generally maintained their plans to increase fixed investment firmly in the March *Tankan*, and machinery orders continued to show a solid increase, albeit with some fluctuations. Business fixed investment was projected to continue to see a moderate uptrend on the back of corporate profits at high levels and highly accommodative financial conditions.

As for the employment and income situation, supply-demand conditions in the labor market continued to improve steadily and employee income had increased moderately.

Private consumption had been resilient against the background of steady improvement in the employment and income situation, although relatively weak developments had been seen in some indicators. According to various sales statistics, retail sales had been somewhat weak recently, due in part to the effects of declining stock prices and increasing cautiousness in consumer sentiment, in a situation where the effects of sluggish sales of seasonal merchandise resulting from the irregularly warm winter remained. On the other hand, services consumption such as dining-out and travel had been increasing firmly recently. Private consumption was expected to remain resilient with the employment and income situation continuing to improve steadily, albeit with relatively weak developments remaining in some indicators.

As for housing investment, the pick-up had paused recently, partly reflecting a sluggish increase in demand for condominiums due to higher prices.

Industrial production continued to be more or less flat, and most recently the supply-side constraints caused by the Kumamoto Earthquake were exerting downward pressure. As for the outlook, supply-chain disruptions resulting from the earthquake were expected to exert downward pressure on production in the short run. It was projected to remain more or less flat for the time being as a trend, in a situation where effects of the slowdown in overseas economies would remain, mainly in emerging economies.

As for prices, the producer price index (PPI) continued to decline relative to three months earlier, reflecting movements in international commodity prices and foreign exchange rates. The year-on-year rate of change in the consumer price index (CPI) for all items less fresh food was about 0 percent. The rate of increase for all items less fresh food and energy had continued its steady rising trend since spring 2015, and after having registered a year-on-year rate of increase of 1.3 percent for December 2015, it had slowed down somewhat in January through March 2016, registering a year-on-year rate of increase of 1.1 percent for three consecutive months. Looking at annual price changes across all items less fresh food, the share of price-increasing items minus the share of price-decreasing items had been moving at levels clearly above the peak in 2008, albeit with some fluctuations. With regard to the outlook, the year-on-year rate of change in the CPI (all items less fresh food) was likely to be about 0 percent for the time being, due to the effects of the decline in energy prices.

2. Financial environment

Financial conditions were highly accommodative.

The monetary base had increased significantly as asset purchases by the Bank had progressed, and the year-on-year rate of growth had been in the range of 25-30 percent.

Firms' funding costs had been hovering at extremely low levels. With regard to credit supply, financial institutions' lending attitudes -- as perceived by firms -- had been improving further and were significantly accommodative. Issuing conditions for CP and corporate bonds continued to be favorable. Firms' credit demand had been increasing moderately, mainly for working capital and funds related to mergers and acquisitions. Against this backdrop, the year-on-year rate of increase in the amount outstanding of bank lending had been around 2 percent. Firms' financial positions had been favorable. The year-on-year rate of growth in the money stock had been in the range of 3.0-3.5 percent, mainly due to the increase in bank lending. Meanwhile, inflation expectations had weakened recently, although they appeared to be rising on the whole from a somewhat longer-term perspective.

3. Loan disbursement under the Fund-Provisioning Measure to Stimulate Bank Lending

In mid-March 2016, the Bank carried out a new loan disbursement, amounting to 2,346.2 billion yen, under the Fund-Provisioning Measure to Stimulate Bank Lending. The outstanding balance of loans disbursed by the Bank amounted to 24,422.0 billion yen after the new loan disbursement.

## II. Introduction of the Funds-Supplying Operation to Support Financial Institutions in Disaster Areas of the 2016 Kumamoto Earthquake and Other Measures

### A. Staff Reports

Although it was still difficult to determine the total economic cost of the damage incurred by the Kumamoto Earthquake, there was a possibility that this could be a considerable amount when compared with large-scale earthquakes in the past. Therefore, the staff proposed that the Bank introduce a funds-supplying operation to support financial institutions in disaster areas and ease the collateral eligibility standards for debt of companies in these areas.

### B. Discussion by the Policy Board and Vote

Members shared the recognition that, with a view to supporting disaster areas from the financial aspect in their efforts toward restoration and rebuilding, it was appropriate to introduce the funds-supplying operation reported by the staff. One member said that, while the Bank had devoted its utmost efforts to maintaining the financial infrastructures since the Kumamoto Earthquake had occurred -- such as smooth supply of banknotes and proper operation of the payment and settlement systems -- it should continue to contribute to restoration and rebuilding of the economy in disaster areas by supporting financial institutions in these areas with this measure. On this basis, "Establishment of 'Principal Terms and Conditions for the Funds-Supplying Operation to Support Financial Institutions in Disaster Areas of the 2016 Kumamoto Earthquake'" was put to a vote. Members voted unanimously to approve the proposal. They agreed that an outline of the decision should be included in the Statement on Monetary Policy. As for the details, they concurred that the staff should accordingly make these public after the meeting.

## III. Amendment to "Principal Terms and Conditions of Complementary Deposit Facility"

### A. Staff Reports

At the MPM held in March 2016, the Bank decided that, with the aim of further supporting financial institutions' efforts to increase lending, in cases where a financial institution increased the amount outstanding of borrowing from the Bank through the Loan Support Program and the Funds-Supplying Operation to Support Financial Institutions in Disaster Areas, twice as much as the amount of the increase would be added to the financial institution's Macro Add-on Balance. In view of this decision, the staff proposed that the Bank amend the Principal Terms and Conditions of Complementary Deposit Facility.

### B. Discussion by the Policy Board and Vote

"Amendment to 'Principal Terms and Conditions of Complementary Deposit Facility'" was put to a vote. Members voted unanimously to approve the proposal. They concurred that the staff should accordingly make this public after the meeting.

## IV. Summary of Discussions by the Policy Board on Economic and Financial Developments and the April 2016 *Outlook for Economic Activity and Prices*

### A. Economic Developments

Members shared the recognition that, although <u>global financial markets</u> had regained their calmness compared to a while ago, it remained difficult for market participants to actively take risks amid the persistent uncertainty regarding future developments in the global economy. One member expressed the view that, while overseas financial markets had started to regain their stability, Japan's financial markets had not yet overcome the turbulence. Members agreed that close attention should continue to be paid to the developments in global financial markets and their effects on Japan's economic activity and prices.

Members shared the recognition that overseas economies continued to grow at a moderate pace, but the pace of growth had somewhat decelerated, mainly in emerging economies. One member noted that the degree of deceleration in emerging economies had been larger than expected. As for the outlook, members concurred that overseas economies were likely to remain in a state of slight deceleration for the time being, but to moderately increase their growth rates as advanced economies would continue to see firm growth and emerging economies would move out of their deceleration phase on the back of the developments in advanced economies.

With regard to developments in overseas economies by region, members concurred that the U.S. economy had been on a recovery trend, assisted by firm household spending on the back of an increase in employment, although the industrial sector had lacked momentum, mainly against the background of the appreciation of the U.S. dollar to date and the slowdown in emerging economies. As for the outlook, they shared the view that the economy was likely to continue to recover, mainly in private demand, led by the firmness in household spending, reflecting accommodative financial conditions, although the industrial sector was likely to lack momentum for the time being.

Members shared the recognition that the European economy maintained its moderate recovery as private consumption continued to increase, although exports had shown some weakness, mainly due to the effects of the slowdown in emerging economies. As for the outlook, they concurred that the economy would likely continue to see a moderate recovery, mainly on the back of improvement in the employment and income situation under accommodative financial conditions.

Members agreed that the Chinese economy maintained its stable growth on the whole, but the pace of growth had decelerated somewhat, mainly in exports and production, due to downward pressure from an overhang of production capacities and inventory adjustments in the manufacturing sector. One member, pointing out that the pace of increase in fixed asset investment had been accelerating somewhat, expressed the view that the economic slowdown was coming to a halt. As for the outlook, members shared the view that the economy was likely to broadly follow a stable growth path as authorities proactively carried out both fiscal and financial measures to support economic activity, although the growth pace was likely to be somewhat slower, mainly in exports and production.

Members shared the view that emerging economies had been decelerating, mainly in exports and production. They continued that, in Asia, exports and production had been relatively weak, due mainly to sluggish demand for IT-related goods, while economic conditions in commodity-exporting countries such as Brazil and Russia continued to be severe. As for the outlook, members shared the view that emerging economies would move out of their deceleration phase, mainly due to the effects of the recovery in advanced economies and economic stimulus measures both on the financial and fiscal fronts, after remaining in a state of deceleration for the time being.

Members concurred that financial conditions in Japan were highly accommodative. They shared the view that, under Quantitative and Qualitative Monetary Easing (QQE) with a Negative Interest Rate, firms' funding costs had been hovering at extremely low levels and the monetary base had increased significantly, reflecting the progress in asset purchases by the Bank. Some members pointed out that, since the Bank's decision to introduce QQE with a Negative Interest Rate, the JGB yield curve across all maturities was decreasing, and that accordingly, a benchmark rate for lending to firms, interest rates on housing loans, and the issuance rates for CP and corporate bonds clearly had declined. Members agreed that firms' financial positions had been favorable as (1) financial institutions' lending attitudes -- as perceived by firms -- had been improving further and were significantly accommodative and (2) issuing conditions for CP and corporate bonds continued to be favorable. They shared the recognition that firms' credit demand had been increasing moderately, mainly for working capital and funds related to mergers and acquisitions, and that the amount outstanding of bank lending, including that to small firms, had been increasing moderately. A few members pointed out that the diffusion index for the lending attitude of financial institutions in the March 2016 *Tankan* and the results of the *Senior Loan Officer Opinion Survey on Bank Lending Practices at Large Japanese Banks* (Loan Survey) showed that financial conditions had become more accommodative since the introduction of QQE with a Negative Interest Rate.

Based on the above deliberations on economic and financial conditions abroad and financial conditions in Japan, members discussed the state of Japan's economy.

With regard to economic activity, members shared the recognition that the economy continued its moderate recovery trend, although exports and production had been sluggish, due mainly to the effects of the slowdown in emerging economies. They shared the view that a virtuous cycle from income to spending had been operating in both the household and corporate sectors, while pointing out that corporate profits had been at record high levels and labor market conditions remained tight. However, one member said that, since the aggregate income formation was likely to lose momentum, the probability that the virtuous cycle would pick up steam did not seem to be increasing.

Members agreed that the pick-up in Japan's exports had paused recently, due mainly to the effects of the slowdown in emerging economies. As for the outlook, they shared the view that exports as a whole were likely to remain more or less flat for the time being, mainly due to the slowdown in overseas economies, the recent appreciation of the yen, and the effects of the Kumamoto Earthquake. They continued that exports were likely to increase moderately thereafter, however, on the back of emerging economies moving out of their deceleration phase.

Members agreed that business fixed investment had been on a moderate increasing trend as corporate profits had been at high levels. They shared the view that it was likely to maintain a moderate uptrend on the back of corporate profits at high levels. One member noted that business fixed investment plans in the March 2016 *Tankan* showed that firms had maintained their positive fixed investment stance. A different member expressed the recognition that, if concern over a slowdown in the global economy heightened, this could affect business fixed investment by increasing cautiousness in firms' sentiment. This member continued that careful attention therefore should be paid to future developments.

As for the employment and income situation, members concurred that employee income had increased moderately with supply-demand conditions in the labor market continuing to improve steadily, and that it was likely to continue to do so as labor market conditions kept improving and corporate profits remained at high levels. One member pointed out that the pace of decline in the unemployment rate had decelerated, and expressed the view that 2 percent inflation was hard to achieve without a decline in the unemployment rate to below 3 percent.

Members shared the recognition that, although relatively weak developments had been seen in some indicators, private consumption had been resilient against the background of steady improvement in the employment and income situation and was likely to remain so. A few members expressed the recognition that the recent relative weakness in private consumption was attributable not only to the irregularly warm winter, but also to factors such as the deterioration in consumer sentiment, reflecting the turbulence in the financial markets. Some members expressed the view that private consumption would increase its resilience because employee income was likely to continue rising. A few members pointed to the possibility that the cautiousness in consumption reflected developments in the spending activity of pensioners who were unlikely to benefit from the effects of improvement in the employment situation.

Members shared the recognition that industrial production continued to be more or less flat, and that most recently the supply-side constraints caused by the Kumamoto Earthquake were exerting downward pressure. As for the outlook, they shared the view that it was likely to remain more or less flat for the time being as a trend, in a situation where effects of the slowdown in overseas economies would remain, mainly in emerging economies, although there were high uncertainties, such as the effects of the earthquake. On this basis, members shared the recognition that it was necessary to continue to make a careful assessment of the effects that the recent earthquake could have on the regional economy as well as on Japan's economy.

As for prices, members concurred that the year-on-year rate of change in the CPI (all items less fresh food) was about 0 percent and was likely to remain at this level for the time being due to the effects of the decline in energy prices.

**B. Outlook for Economic Activity and Prices**

With regard to the baseline scenario of the outlook for Japan's economic activity, members concurred that, although sluggishness was likely to remain in exports and production for the time being, domestic demand was likely to follow an uptrend, with a virtuous cycle from income to spending being maintained in both the household and corporate sectors, and exports were likely to increase moderately on the back of emerging economies moving out of their deceleration phase. On this basis, they shared the recognition that Japan's economy was likely to be on a moderate expanding trend through fiscal 2018, continuing to grow at a rate generally above its potential, although fluctuations due to a front-loaded increase and subsequent decline in demand prior to and after the consumption tax hike planned in April 2017 were expected. Members agreed that the projected growth rates were somewhat lower, influenced mainly by weaker exports that reflected the slowdown in overseas economies, compared with those presented in the January 2016 *Outlook for Economic Activity and Prices* (hereafter the Outlook Report).

Regarding developments in economic activity for fiscal 2016, members concurred that, although exports were likely to continue exhibiting sluggishness for the time being, they would probably head toward a moderate increase thereafter on the back of emerging economies moving out of their deceleration phase. They shared the recognition that in the second half of the fiscal year, the front-loaded increase in demand prior to the consumption tax hike scheduled in April 2017 was likely to push up domestic private demand. Members shared the view that in fiscal 2017, while household spending was likely to be affected by a demand decline after the consumption tax hike, exports would probably continue increasing moderately owing to overseas economic growth, and business fixed investment was likely to maintain its moderate increasing trend, supported, for example, by accommodative financial conditions, heightened growth expectations, and increases in Olympic Games-related demand. They concurred that in fiscal 2018, it was likely that exports would increase moderately and domestic private demand would increase, while the effects of the demand decline after the consumption tax hike would dissipate. Members shared the recognition that, throughout the projection period, which covered through fiscal 2018, Japan's potential growth rate would probably follow a moderate increasing trend, pushing up the economy's growth pace in the medium to long term.

In terms of <u>the outlook for prices</u>, most members shared the view that (1) as the underlying trend in inflation steadily rose, the year-on-year rate of change in the CPI was likely to accelerate toward 2 percent, (2) the timing of reaching around 2 percent was likely to be during fiscal 2017, assuming that crude oil prices would rise moderately from the recent level, and (3) thereafter, the year-on-year rate of change in the CPI was likely to be around 2 percent on average. These members concurred that the projected rate of increase in the CPI for fiscal 2016 was lower compared with that presented in the January 2016 Outlook Report, mainly reflecting downward revisions in projections for GDP growth and wage developments. On the other hand, a few members expressed the recognition that the rate of change in the CPI would not reach around 2 percent during the projection period.

Members discussed the output gap and medium- to long-term inflation expectations, both of which were the main factors that determined the underlying trend in inflation. First, they agreed that the output gap was more or less unchanged on the whole, as the tightening of labor market conditions continued while an improvement in manufacturers' capacity utilization rates had been delayed against the background of the slowdown in emerging economies. As for the outlook, members shared the recognition that the tightening of labor market conditions was likely to continue and capacity utilization rates were likely to increase again as exports and production picked up. They continued that the output gap was therefore likely to move into positive territory and gradually increase further from the second half of fiscal 2016, albeit with fluctuations due to the front-loaded increase in demand prior to the scheduled consumption tax hike.

With regard to medium- to long-term inflation expectations, members shared the view that these had weakened recently, although they appeared to be rising on the whole from a somewhat longer-term perspective. They agreed that market indicators and survey results regarding inflation expectations had weakened recently. They shared the view that, on the other hand, firms had maintained their willingness to increase prices, and consumers seemed to be accepting these increases, benefiting from an improvement in the employment and income situation. Regarding firms' wage-setting stance, some members expressed concern over the fact that the base pay increase resulting from this year's wage negotiations had been somewhat lower than that in 2015, mainly at large firms, in part because the turbulence in global financial markets since the start of 2016 had negatively affected the sentiment of both labor and management. In response, some members expressed the view that the base pay increase achieved for a third consecutive year in this year's wage negotiations and the spread of wage increases even to small firms could be assessed as positive developments. On this basis, one member expressed the opinion that the key was the degree to which firms would increase prices in fiscal 2016 and to what degree consumers would accept such increases. On this point, a different member expressed the view that, going forward, firms' price-setting stance would likely shift further toward raising prices again, with improvement in consumer sentiment.

Members also discussed upside and downside risk factors to the baseline scenario of the outlook for economic activity and prices. Regarding the outlook for economic activity, members noted the following upside and downside risk factors: (1) uncertainty regarding developments in overseas economies; (2) the effects of the consumption tax hike scheduled to take place in April 2017; (3) firms' and households' medium- to long-term growth expectations; and (4) fiscal sustainability in the medium to long term.

As upside and downside risks to prices, members pointed to the following four factors: (1) developments in firms' and households' medium- to long-term inflation expectations; (2) developments in the output gap, particularly in labor market conditions; (3) the responsiveness of inflation to the output gap; and (4) developments in import prices.

On this basis, members shared the recognition that risks to Japan's economic activity and prices remained skewed to the downside with high unpredictability regarding the outlook for the global economy and considerable uncertainty over developments in medium- to long-term inflation expectations.

**V. Summary of Discussions on Monetary Policy for the Immediate Future**

Based on the above assessment of economic and financial developments, members discussed monetary policy for the immediate future.

Members shared the recognition that the underlying trend in inflation was important in conducting monetary policy. They also shared the view that it had been improving steadily, judging from developments in the output gap and inflation expectations. Many members -- noting that a base pay increase was taking place for a third consecutive year and wage increases had been spreading even to small firms -- expressed the recognition that the mechanism in which inflation rose moderately accompanied by wage increases had been operating steadily. On this basis, most members shared the view that the year-on-year rate of increase in the CPI was likely to accelerate toward 2 percent -- the price stability target -- as the underlying trend in inflation steadily rose, given that the Bank would steadily pursue QQE with a Negative Interest Rate. A few members expressed a more cautious view on the outlook for the underlying trend in inflation, for reasons such as the following: (1) the direct positive effects of the past yen depreciation on CPI inflation were likely to wane gradually as the yen's depreciation trend against the U.S. dollar came to a halt, and (2) the base pay increase resulting from the wage negotiations between workers and management this spring was somewhat lower than that in 2015, and there was a high degree of uncertainty as to whether firms' price- and wage-setting stance would shift further toward raising prices and wages again.

Members discussed policy implications of the lower projected rate of increase in the CPI for fiscal 2016 compared with the January 2016 projection, which was mainly attributable to downward revisions in projections for GDP growth and wage developments -- while previous revisions to the CPI projection were primarily attributable to the change in assumed crude oil prices. In this regard, most members expressed the recognition that, although the projected rate of increase in the CPI for fiscal 2016 was lower, a virtuous cycle from income to spending was maintained in both the household and corporate sectors, and the mechanism in which inflation rose moderately accompanied by wage increases also had been operating steadily. On this basis, most members concurred that QQE with a Negative Interest Rate had already produced its effects clearly, in that it had lowered various interest rates, and going forward, the policy effects would steadily spread to economic activity and prices. These members also agreed that it was appropriate at present to examine the extent of the permeation of policy effects, because it took some time to see the penetration of monetary policy effects and because it could be even more difficult for positive changes to emerge in circumstances such as those in evidence today, where turbulence in global financial markets continued. One member noted that the decline in interest rates brought about by the negative interest rate policy would exert positive effects on a wide range of economic entities, not only by lowering interest payments but also by stimulating demand. This member continued that it was necessary for the Bank to explain this point patiently in its communication with the public. A different member said that the negative interest rate policy, as did QQE, aimed at reducing the real interest rate to a level below the natural rate of interest.

Some members pointed out that, under QQE with a Negative Interest Rate, supply-demand conditions in the JGB and some other financial markets had become extremely tight. A few of these members expressed the view that, in such a situation, the Bank should conduct asset purchases in a more flexible manner in accordance with financial market conditions.

Based on the above discussions, regarding <u>the guideline for money market operations for the intermeeting period</u>, most members expressed the recognition 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 80 trillion yen.

With regard to the asset purchases, most members shared the recognition that it was appropriate for the Bank to implement the following guideline for the intermeeting period. First, it would purchase JGBs so that their amount outstanding would increase at an annual pace of about 80 trillion yen. With a view to encouraging a decline in interest rates across the entire yield curve, the Bank would conduct purchases in a flexible manner in accordance with financial market conditions. The average remaining maturity of the Bank's JGB purchases would be about 7-12 years. Second, it would purchase exchange-traded funds (ETFs) and Japan real estate investment trusts (J-REITs) so that their amounts outstanding would increase at annual paces of about 3.3 trillion yen and about 90 billion yen, respectively. And third, for CP and corporate bonds, the Bank would maintain their amounts outstanding at about 2.2 trillion yen and about 3.2 trillion yen, respectively.

As for the policy rate, most members shared the recognition that it was appropriate to continue applying a negative interest rate of minus 0.1 percent to the Policy-Rate Balances in current accounts held by financial institutions at the Bank.

With respect to the Bank's thinking behind its future conduct of monetary policy, most members shared the view that the Bank would (1) continue with QQE with a Negative Interest Rate, aiming to achieve the price stability target of 2 percent, as long as it was necessary for maintaining this target in a stable manner, and (2) examine risks to economic activity and prices, and take additional easing measures in terms of three dimensions -- quantity, quality, and the interest rate -- if it was judged necessary for achieving the price stability target. Some members noted that risks to economic activity and prices continued to be skewed to the downside, particularly those regarding developments in overseas economies and in medium- to long-term inflation expectations. These members emphasized that, going forward, the Bank should carefully examine risks at each MPM and take additional easing measures without hesitation if it was judged necessary. One of these members commented that the Bank needed to thoroughly explain to the public that (1) its commitment to realizing the price stability target of 2 percent was unchanged, and (2) a decision at this MPM to maintain its current monetary policy did not indicate a change in the Bank's thinking behind its conduct of monetary policy.

On the other hand, a few members argued that the negative interest rate policy would impair the functioning of financial markets and financial intermediation as well as the stability of the JGB market. In addition, one of these members said that marginal effects of QQE had been diminishing, and such effects had already been outweighed by the side effects. The member's argument was as follows. First, the Bank should reduce the annual pace of increase in the amount outstanding of its JGB holdings to a level below the initial pace, in view of further possible phased reductions. Second, it should make changes to the time frame for achieving the price stability target -- to the medium to long term -- and conduct monetary policy that gave due consideration to risks such as a buildup of financial imbalances. This member expressed the recognition that even more emphasis should be placed on financial system stability. In response, one member said that most of the arguments against the negative interest rate policy concerned a decrease in banks' profitability, but the only way for banks to gain stable profits was to revitalize the economy as a whole.

**VI. Remarks by Government Representatives**

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

(1) At the Meeting of Directors-General of Local Finance Bureaus held on April 27, 2016, reports that included the effects of the recent Kumamoto Earthquake on each region were made by the local finance bureaus. The Ministry of Finance would continue to carefully monitor the effects of the earthquake on each region and work to thoroughly implement the necessary measures in an appropriate manner. In order to provide support for the people affected by the disaster and promptly restore the affected areas, the government first of all approved, on April 20, the use of 2.3 billion yen included in the budget for fiscal 2016 as emergency funds to procure supplies that were needed for those affected during evacuation for the time being. Moreover, on April 24, the prime minister gave instructions to formulate a supplementary budget to respond to the Kumamoto Earthquake. Through the implementation of the supplementary budget, the government would provide for expenses needed to support the people affected by the disaster, including allowances to secure housing. It also would establish a Kumamoto Earthquake Recovery Emergency Fund in order to swiftly advance the rebuilding of the businesses of those affected by the disaster, the recovery of infrastructure such as roads

and facilities, and the removal of debris. Given the prime minister's instruction to promptly submit the supplementary budget to the Diet, the government was proceeding with its efforts to submit it in mid-May. The government considered the Bank's introduction at this meeting of a funds-supplying operation to respond to the Kumamoto Earthquake as entirely appropriate.

(2) With regard to the earlier implementation of the budget, the government would aim to conclude contracts mainly for public works on around 80 percent of the 12.1 trillion yen in the budget for fiscal 2016, which was approved by the Diet on March 29, by the end of September and likewise work to swiftly implement the budget for other expenses that were feasible for earlier implementation. The government would make efforts to deliver benefits from the budget for fiscal 2016 to the people as swiftly as possible through an earlier implementation of the budget, and thereby respond appropriately to the downside risks to the Japanese economy.

(3) The government expected the Bank to continue to work toward achieving the price stability target in light of economic activity and prices.

The representative from the Cabinet Office made the following remarks.

(1) The Japanese economy was on a moderate recovery, while weakness could be seen recently. According to the provisional results of wage negotiations between workers and management this spring, base pay increases, which only rarely had been made before the Abe administration, were expected for a third consecutive year at many firms. As for the outlook, the economy was expected to head toward a moderate recovery, supported partly by the effects of the government's policies, while the employment and income situation continued to improve. However, attention should be given to the increased uncertainty in overseas economies and the effects of fluctuations in the financial and capital markets. In addition, full attention should be given to the economic impact of the Kumamoto Earthquake. In assessing price developments, it was important to comprehensively examine a wide range of price indicators, including the GDP deflator, which showed the price of value added.

(2) On March 29, 2016, the budget for fiscal 2016 was approved by the Diet. In order to respond appropriately to downside risks to the Japanese economy, such as a slowing down of overseas economies, the government would work to bring forward the

implementation of the budget, in addition to the supplementary budget for fiscal 2015, and make sure that their effects were produced promptly. The damage caused by the Kumamoto Earthquake had been tremendous; the government would make sure to provide support for the daily lives of those affected by the disaster, and also work on promoting early recovery of the local economies and industries. The government expected that, with the funds-supplying operation decided at this meeting to support financial institutions in the disaster areas, restoration and rebuilding in these areas would be fully supported from the financial aspect. At the Council on Economic and Fiscal Policy held on April 25, Efforts toward the Achievement of a 600 Trillion Yen Economy was compiled. The government would incorporate the necessary institutional and regulatory reforms into the Plan to Realize the Dynamic Engagement of All Citizens and the Basic Policies to build a stronger positive cycle of growth and distribution.

(3) The government expected the Bank to work steadily to achieve the price stability target of 2 percent in light of economic activity and prices. In addition, the government expected the Bank to continue to thoroughly communicate its negative interest rate policy and to make efforts such that its policy effects would be fully realized. The government deemed it important that the Bank fully explain to the public its thinking, including the reasons for somewhat deferring the projected timing of the year-on-year rate of change in the CPI reaching the price stability target of 2 percent.

## VII. Votes

### A. Vote on the Chairman's Policy Proposal on the Guideline for Money Market Operations

Based on the above discussions, to reflect the majority view of the members, the chairman formulated the following proposal and put it to a vote.

The Policy Board decided the proposal by a majority vote.

**The Chairman's Policy Proposal on the Guideline for Money Market Operations:**

The guideline for money market operations for the intermeeting period will be as follows.

The Bank of Japan will conduct money market operations so that the monetary base will increase at an annual pace of about 80 trillion yen.

Votes for the proposal: Mr. H. Kuroda, Mr. K. Iwata, Mr. H. Nakaso, Mr. K. Ishida, Mr. T. Sato, Mr. Y. Harada, Mr. Y. Funo, and Mr. M. Sakurai.
Votes against the proposal: Mr. T. Kiuchi.

**B. Vote on the Chairman's Policy Proposal on the Guideline for Asset Purchases**

To reflect the majority view of the members, the chairman formulated the following proposal to implement the guideline for asset purchases for the intermeeting period, and put it to a vote: (1) to purchase JGBs so that their amount outstanding would increase at an annual pace of about 80 trillion yen, to conduct purchases in a flexible manner in accordance with financial market conditions -- with a view to encouraging a decline in interest rates across the entire yield curve -- and to make the average remaining maturity of the Bank's JGB purchases about 7-12 years; (2) to purchase ETFs and J-REITs so that their amounts outstanding would increase at annual paces of about 3.3 trillion yen and about 90 billion yen, respectively; and (3) to maintain the amounts outstanding of CP and corporate bonds at about 2.2 trillion yen and about 3.2 trillion yen, respectively.

The Policy Board decided the proposal by a majority vote.

Votes for the proposal: Mr. H. Kuroda, Mr. K. Iwata, Mr. H. Nakaso, Mr. K. Ishida, Mr. T. Sato, Mr. Y. Harada, Mr. Y. Funo, and Mr. M. Sakurai.
Votes against the proposal: Mr. T. Kiuchi.

**C. Vote on the Chairman's Policy Proposal on the Policy Rate**

To reflect the majority view of the members, the chairman formulated a proposal to continue applying a negative interest rate of minus 0.1 percent to the Policy-Rate Balances in current accounts held by financial institutions at the Bank, and put it to a vote.

The Policy Board decided the proposal by a majority vote.

Votes for the proposal: Mr. H. Kuroda, Mr. K. Iwata, Mr. H. Nakaso, Mr. K. Ishida, Mr. Y. Harada, Mr. Y. Funo, and Mr. M. Sakurai.

Votes against the proposal: Mr. T. Sato and Mr. T. Kiuchi.

Mr. T. Sato and Mr. T. Kiuchi dissented considering that an interest rate of 0.1 percent should be applied to current account balances excluding the amount outstanding of the required reserves held by financial institutions at the Bank, because negative interest rates would impair the functioning of financial markets and financial intermediation as well as the stability of the JGB market.

**D. Vote on Mr. T. Kiuchi's Policy Proposal on the Guidelines for Money Market Operations and Asset Purchases**

With regard to the guideline for money market operations for the intermeeting period, Mr. T. Kiuchi proposed that the Bank conduct money market operations so that the monetary base would increase at an annual pace of about 45 trillion yen. In addition, with regard to the guideline for asset purchases, he proposed the following: (1) to purchase JGBs so that their amount outstanding would increase at an annual pace of about 45 trillion yen, to conduct purchases in a flexible manner in accordance with financial market conditions -- with a view to encouraging a decline in interest rates across the entire yield curve -- and to make the average remaining maturity of the Bank's JGB purchases about seven years; (2) to purchase ETFs and J-REITs so that their amounts outstanding would increase at annual paces of about 1 trillion yen and about 30 billion yen, respectively; and (3) to maintain the amounts outstanding of CP and corporate bonds at about 2.2 trillion yen and about 3.2 trillion yen, respectively. The proposal was then put to a vote.

The proposal 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. K. Ishida, Mr. T. Sato, Mr. Y. Harada, Mr. Y. Funo, and Mr. M. Sakurai.

**E. Vote on the Statement on Monetary Policy**

On the basis of the above results of votes, the chairman formulated the Statement on Monetary Policy, and put it to a vote. The Policy Board decided the text by a unanimous vote. It was confirmed that the statement would be released immediately after the meeting (see Attachment).

**VIII. Discussion regarding the Outlook Report**

Members discussed the draft of "The Bank's View" in the April 2016 Outlook Report (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, he proposed a new expression that "the timing at which around 2 percent will come into sight is projected to be during fiscal 2017." Second, with regard to the description on the first perspective, he proposed changing the current expression that Japan's economy "is judged as likely to achieve around 2 percent inflation" to a new expression that it "is judged as likely to head toward achieving around 2 percent inflation." The proposal was then put to a vote.

The proposal 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. K. Ishida, Mr. T. Kiuchi, Mr. Y. Harada, Mr. Y. Funo, and Mr. M. Sakurai.

Mr. T. Kiuchi formulated a proposal to make the following changes. First, with regard to medium- to long-term inflation expectations, he proposed a new expression that they "are likely to remain stable." Second, with regard to the outlook for prices, he proposed a new expression that the year-on-year rate of change in the CPI "is likely to be about 0 percent for the time being, and thereafter accelerate very moderately." Third, with regard to the future conduct of monetary policy, he proposed a new expression that "the Bank will, with the aim to achieve the price stability target of 2 percent in the medium to long term, continue to provide consistent support from the financial side. It will continue with asset purchases and a virtually zero interest rate policy as long as each of these policy measures is deemed appropriate under flexible policy conduct based on the examination from the two perspectives of the monetary policy framework." The proposal was then put to a vote.

The proposal 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. K. Ishida, Mr. T. Sato, Mr. Y. Harada, Mr. Y. Funo, and Mr. M. Sakurai.

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 released immediately after the meeting on April 28, 2016 and the whole report would be made public on April 29.

Votes for the proposal: Mr. H. Kuroda, Mr. K. Iwata, Mr. H. Nakaso, Mr. K. Ishida, Mr. Y. Harada, Mr. Y. Funo, and Mr. M. Sakurai.
Votes against the proposal: Mr. T. Sato and Mr. T. Kiuchi.

Mr. T. Sato and Mr. T. Kiuchi dissented for the reasons presented in each of the aforementioned proposals.

**IX. Approval of the Minutes of the Monetary Policy Meeting**

The Policy Board approved unanimously the minutes of the Monetary Policy Meeting of March 14 and 15, 2016 for release on May 9.

Attachment

April 28, 2016

Bank of Japan

**Statement on Monetary Policy**

1. At the Monetary Policy Meeting (MPM) held today, the Policy Board of the Bank of Japan decided upon the following.

   (1) Quantity Dimension: The guideline for money market operations

   The Bank decided, by an 8-1 majority vote, to set the following guideline for money market operations for the intermeeting period:[Note 1]

   The Bank of Japan will conduct money market operations so that the monetary base will increase at an annual pace of about 80 trillion yen.

   (2) Quality Dimension: The guidelines for asset purchases

   With regard to the asset purchases, the Bank decided, by an 8-1 majority vote, to set the following guidelines:[Note 1]

   a) The Bank will purchase Japanese government bonds (JGBs) so that their amount outstanding will increase at an annual pace of about 80 trillion yen. With a view to encouraging a decline in interest rates across the entire yield curve, the Bank will conduct purchases in a flexible manner in accordance with financial market conditions. The average remaining maturity of the Bank's JGB purchases will be about 7-12 years.

   b) The Bank will purchase exchange-traded funds (ETFs) and Japan real estate investment trusts (J-REITs) so that their amounts outstanding will increase at annual paces of about 3.3 trillion yen[7] and about 90 billion yen, respectively.

   c) As for CP and corporate bonds, the Bank will maintain their amounts outstanding at about 2.2 trillion yen and about 3.2 trillion yen, respectively.

[7] Of about 3.3 trillion yen, 300 billion yen is used in line with the implementation of a program for purchasing ETFs composed of stocks issued by firms that are proactively investing in physical and human capital, as decided at the MPM held in December 2015.

(3) Interest-Rate Dimension: The policy rate

The Bank decided, by a 7-2 majority vote, to continue applying a negative interest rate of minus 0.1 percent to the Policy-Rate Balances in current accounts held by financial institutions at the Bank.[Note 2]

2. In addition, with a view to supporting financial institutions in disaster areas affected by the Kumamoto Earthquake in their efforts toward meeting demand for funds for restoration and rebuilding, the Bank decided by a unanimous vote to introduce a funds-supplying operation for these financial institutions. The specifics of this operation are the following: the total amount of loans is set at 300 billion yen; the Bank will provide loans at a zero interest rate; and twice as much as the amount outstanding of financial institutions' borrowing through this operation will be added to their Macro Add-on Balances, to which a zero interest rate is applied.

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[Note 1] Voting for the action: Mr. H. Kuroda, Mr. K. Iwata, Mr. H. Nakaso, Mr. K. Ishida, Mr. T. Sato, Mr. Y. Harada, Mr. Y. Funo, and Mr. M. Sakurai. Voting against the action: Mr. T. Kiuchi. Mr. T. Kiuchi proposed that the Bank will conduct money market operations and asset purchases so that the monetary base and the amount outstanding of its JGB holdings will increase at an annual pace of about 45 trillion yen, respectively. The proposal was defeated by a majority vote.

[Note 2] Voting for the action: Mr. H. Kuroda, Mr. K. Iwata, Mr. H. Nakaso, Mr. K. Ishida, Mr. Y. Harada, Mr. Y. Funo, and Mr. M. Sakurai. Voting against the action: Mr. T. Sato and Mr. T. Kiuchi. Mr. T. Sato and Mr. T. Kiuchi dissented considering that an interest rate of 0.1 percent should be applied to current account balances excluding the amount outstanding of the required reserves held by financial institutions at the Bank, because negative interest rates would impair the functioning of financial markets and financial intermediation as well as the stability of the JGB market.