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June 26, 2017

Bank of Japan

Summary of Opinions at the Monetary Policy Meeting^{1,2} on June 15 and 16, 2017

I. Opinions on Economic and Financial Developments

Economic Developments

- Japan's economy has been turning toward a moderate expansion. Economic activity has been broadly in line with the projection. In order for the Bank to revise upward its economic assessment, it is necessary to confirm that a positive output gap has been taking hold while examining various economic indicators.
- Japan's economy has been turning toward a moderate expansion. While external demand has been on an increasing trend, positive developments also have been observed in indicators of domestic demand such as business fixed investment and private consumption. Whether the pace of economic expansion will be maintained warrants attention for some time.
- It is appropriate for the Bank to assess that overseas economies "have continued to grow at a moderate pace on the whole," as virtuous cycles are starting to operate in Russia and Brazil, for which economic recovery had been lagging behind that in other economies.
- Uncertainty regarding the financial sector in Europe seems to have waned to a considerable degree, as seen in the progress in addressing the nonperforming loan problems in Italy and Spain. This is likely to exert positive effects on the economy.
- Exports have been on an increasing trend with global trade activity becoming active. Business fixed investment has been on a moderate increasing trend, reflecting positive

¹ English translation prepared by the Bank's staff based on the Japanese original.

² "Summary of Opinions at the Monetary Policy Meeting" is made through the following process: (1) each Policy Board member and government representative makes a summary of opinions that she/he presented at the Monetary Policy Meeting (MPM) under a certain word limit and submits this to the Governor of the Bank of Japan, who serves as the chairman of the MPM, and (2) the chairman edits those opinions as his responsibility.

developments in corporate profits, as seen in the ratio of current profits to sales for all industries and firm sizes having marked its historical high for two consecutive quarters.

- With regard to the assessment of the underlying trend in private consumption, it is appropriate to express it as having "increased its resilience," taking into account, for example, an increase in the Consumption Activity Index (CAI).
- The rate of change in the CAI has been positive for four consecutive quarters since the April-June quarter of 2016. Private consumption appears to be gaining momentum recently. The propensity to consume has seen a halt to its declining trend, and turned to an increase after hitting bottom in the July-September quarter of 2016.
- Positive developments in the economy have been gaining momentum, led by a tightening of labor market conditions. Under such circumstances, an increase in wages has been observed and private consumption has increased its resilience. Firms' initiatives to raise productivity -- such as investment to improve business efficiency and labor-saving investment -- are starting to make progress.
- Firms are concerned about the increase in fixed costs amid low growth expectations. In achieving wage increases driven by a labor shortage, it is important to implement structural policy that would raise growth expectations.

Prices

- The year-on-year rate of change in the consumer price index (CPI) is likely to continue on an uptrend and increase toward 2 percent, mainly on the back of an improvement in the output gap and a rise in medium- to long-term inflation expectations.
- The fact that an increasing number of small and medium-sized firms are raising their wages is significant for achieving higher inflation. It is reassuring that the rate of increase in base pay at small and medium-sized firms is exceeding that at large firms, according to the latest results of this year's annual spring labor-management wage negotiations.
- The rates of increase in wages and prices have not been accelerating despite improvements in corporate profits and the output gap. At the July MPM, when the July *Outlook for Economic Activity and Prices* (Outlook Report) is to be compiled, the outlook for prices should be discussed thoroughly while carefully examining developments in wages and prices since the turn of this fiscal year.

- It is projected that fiscal 2017 will be a year in which, due to a labor shortage amid an upturn in overseas economies, an improvement in labor productivity and a corresponding increase in real wages can be realized, particularly at small and medium-sized firms. Private consumption is expected to turn to a moderate increasing trend, and a virtuous cycle in which firms can pass on their wage increases to a rise in retail prices is likely to be in place.
- Although raising labor productivity through cutbacks in services that firms provide will bring about a decline in unit labor costs in the short run, it will work as upward pressure on prices from the demand side, mainly through increases in real wages and employee income, from a relatively long-term macroeconomic perspective.
- Although the year-on-year rate of change in the CPI is likely to gradually increase toward 2 percent, a remarkable improvement has yet to be seen. It would take some time for the inflation rate to accelerate, as the formation of inflation expectations is adaptive.
- While upward pressure of energy-related prices on the year-on-year rate of change in the CPI is gradually fading out, downward pressure of mobile phone-related prices on it is expected to be protracted.
- Room for a further increase in labor productivity of the services sector through cutbacks in services that firms provide seems to remain large. There is still a long way to go before wage increases stemming from the tightening in labor markets lead to price rises.

II. Opinions on Monetary Policy

- The most effective way to achieve the price stability target of 2 percent is to continue with the current monetary policy so as to keep improving the output gap, reducing the unemployment rate, and raising the active job openings-to-applicants ratio.
- Sluggish inflation is partly attributable to structural factors such as people's concerns over the future and the adaptive formation mechanism of inflation expectations. The price stability target cannot be achieved easily within a short time frame. It is crucial to maintain accommodative financial conditions and keep the economy expanding as long as possible.
- Although there is still a long way to go to achieve the price stability target of 2 percent, quantitative and qualitative monetary easing (QQE) has achieved improvement in employment, a steady increase in private consumption, and improvement in fiscal conditions. The ratio of fiscal deficit to nominal GDP on an SNA basis has declined by about 4.5

percentage points, excluding the effects of the consumption tax hike, since the introduction of QQE. Given these achievements, it is necessary to continue with the current monetary easing policy with persistence and wait for a steady increase in demand, a further decline in the unemployment rate and consequent wage increases, higher inflation, and a rise in inflation expectations.

- The Bank should continue with the current monetary policy with the aim of persistently encouraging the virtuous cycle to take hold and completely overcoming deflation while fostering people's better understanding of the price stability target of 2 percent.
- It is important to firmly maintain the price stability target of 2 percent due to the upward bias of the CPI, the need to secure room for the monetary policy response, and the fact that the 2 percent target is a global standard.
- An improvement in economic activity, together with the expansion in the Bank's asset size, is the main background for the recent growing interest in the policy exit. With the improvement in economic activity continuing going forward, the Bank needs to be accountable for its thinking on monetary policy management, in order not to raise concern among market participants.
- The financial situations of a central bank account for one of the factors that underpin the credibility of a currency. I am of the view that the credibility of the yen depends to a large extent on not only the credibility of the Bank but that of the country as a whole, and thus is determined by several perspectives.
- The fundamental issue for a policy exit is that its timing cannot be foreseen, given that achieving the price stability target of 2 percent is still considerably distant.
- I am of the view that the price stability target of 2 percent is a constraint on the flexibility of monetary policy. The Bank should change this target to a medium- to long-term one and improve its communication with the financial markets and financial institutions concerning the path toward normalizing monetary policy.
- It is a positive development that the current yield curve has been formed in a manner consistent with the guideline for market operations, due in part to a rise in the yields on treasury discount bills (T-Bills).
- In theory, the stock effect would be in place with the progress in the Bank's Japanese government bond (JGB) purchases. It would become easier for the Bank to control 10-year

JGB yields with a smaller amount of purchases, and the sustainability of the policy thereby would be enhanced.

- In most of the recent months, the pace of long-term JGB purchases has been below the approximate amount to be purchased -- that is, an annual pace of increase in the amount outstanding of the Bank's JGB holdings of about 80 trillion yen. However, if the current pace of purchases continues, the Bank cannot avoid the situation where the JGB purchases will become more difficult through next year. It is therefore necessary to reduce the pace of purchases to an annual pace of increase of 45 trillion yen, in order to secure the stability and sustainability of JGB purchases.

III. Opinions from Government Representatives

Ministry of Finance

- The Cabinet recently decided the Basic Policies on Economic and Fiscal Management and Reform 2017, which maintains the aim of achieving both the target of a 600 trillion yen economy in terms of GDP and the fiscal consolidation target.
- The government would continue to proceed with economic revitalization and steadily promote expenditure and revenue reform.
- The government expects the Bank to continue to work toward achieving the price stability target under "QQE with Yield Curve Control" in light of developments in economic activity and prices, as well as financial conditions.

Cabinet Office

- The real GDP growth rate for the January-March quarter of 2017 registered positive growth for five consecutive quarters.
- On June 9, the Cabinet decided the Basic Policies on Economic and Fiscal Management and Reform 2017 as well as the Investments for the Future Strategy 2017. The government would work toward improving productivity through investments in human resources and realizing Society 5.0. On the same day, the Cabinet also decided the Regulatory Reform Work Plan and the Basic Policies for Overcoming Population Decline and Vitalizing Local Economy in Japan 2017.

- The government expects that the Bank will work steadily toward achieving the price stability target of 2 percent in light of developments in economic activity and prices, as well as financial conditions.