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January 29, 2020

Bank of Japan

Summary of Opinions at the Monetary Policy Meeting^{1,2} on January 20 and 21, 2020

I. Opinions on Economic and Financial Developments

Economic Developments

- Japan's economy has been on a moderate expanding trend, although exports, production, and business sentiment have shown some weakness, mainly affected by the slowdown in overseas economies and natural disasters.
- The probability that the global economy will follow its recovery trend through the middle of this year seems to be increasing.
- Although risks concerning overseas economies remain significant, signs of recovery have started to be observed in part, as seen in the cycle for IT-related goods shifting toward a phase of improvement. Under these circumstances, Japan's economy has maintained its moderate expansion due to the continued firm domestic demand.
- Japan's economy is likely to continue on an expanding trend as the impact of the slowdown in overseas economies on domestic demand is expected to be limited, although the effects of the slowdown are likely to remain for the time being.
- As the underlying trend in domestic demand has been firm, Japan's economy is expected to continue on a moderate expanding trend, also taking into account the additional effects of the government's economic measures.

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.

- Japan's economy has been on a moderate expanding trend. The economy is likely to grow at about the same pace as its potential. However, such effects as of the slowdown in overseas economies warrant attention.
- The government's economic measures are expected to have positive effects that support the expanding trend in the economy in the medium term through a policy mix with monetary policy. That said, risks including the effects of the consumption tax hike continue to warrant attention and the Bank should keep examining these carefully for the time being.
- It remains difficult to be optimistic about developments in Japan's economic activity and prices on the whole. Although uncertainties concerning overseas economies have improved somewhat, as seen in the agreement on the U.S-China economic trade deal and in the progress in the United Kingdom's exit from the European Union (EU), economic indicators in Japan since last October have not been favorable.
- As risks over economic activity at home and abroad have remained significant, it is necessary to carefully assess whether (1) the propensity to consume will not decline due to the consumption tax hike, (2) developments in financial markets will remain favorable amid modest economic activity, (3) a decoupling of the manufacturing and the nonmanufacturing sectors will continue, and (4) some weakness in short-term inflation expectations will not be reflected in medium- to long-term inflation expectations.
- Developments in consumption-related indicators since the consumption tax hike show that recovery in private consumption has been weak. Although there has been improvement in households' sentiment indicators, its pace has been slow compared to that of the tax hike conducted in fiscal 2014.
- There has been an increase in voluntary or early retirement of middle-aged and elderly employees while corporate profits have been at high levels. In a situation where profit levels are high and the employment situation is favorable, it is reasonable that such retirement increases because firms can provide additional retirement benefits easily and workers can find new jobs smoothly. When labor force shifts to places where it is needed more, Japan's overall productivity is likely to rise.
- An estimation suggests that the share of employees who are engaged in routine tasks is relatively large in Japan compared to that in Europe and the United States. Resolution of a mismatch between jobs and employees as well as a rise in average wages could be hampered amid the increasing use of artificial intelligence (AI) and robotic process automation (RPA).

Prices

- The year-on-year rate of change in the consumer price index (CPI) is likely to increase gradually toward 2 percent, mainly on the back of the output gap remaining positive and medium- to long-term inflation expectations rising, although the CPI inflation rate is expected to be affected by such factors as the past decline in crude oil prices for the time being.
- The positive output gap pushes up current prices, which simultaneously brings about the secondary effect of raising inflation expectations in an adaptive manner. Thus, it is appropriate to assess the impact of the output gap on prices in terms of the "area" calculated by multiplying the degree of the positive gap by its duration.
- Although the situation has continued in which prices have not risen easily, mainly reflecting the constraining effects on inflation due to a rise in productivity, the resilience of the economy has been increasing in the sense that it will not go back into deflation. It is important to persistently wait for the inflation rate to accelerate in a situation where the positive output gap is maintained, while examining economic indicators, such as those of employment and business fixed investment.
- Although a virtuous cycle from income to spending has supported price rises, in order to maintain this cycle, it is necessary to continue raising wages as well as improve corporate profits to encourage such continuous wage increases.
- The mechanism in which a positive output gap results in increases in prices and inflation expectations has been operating, but the paces have been slow. Taking into account research results at home and abroad, it is necessary to continue to examine thoroughly the inflation formation mechanism.

II. Opinions on Monetary Policy

- There has been no further increase in the possibility that the momentum toward achieving the price stability target will be lost. It is appropriate to maintain the current guidelines for market operations and asset purchases.
- The Bank should persistently continue with the current monetary policy stance with the aim of continuously encouraging the virtuous cycle of the economy to take hold and thereby achieving the price stability target.

- Since the possibility that the inflation momentum will be lost continues to warrant attention, it is appropriate to maintain a policy stance of being tilted toward monetary accommodation.
- Among advanced economies, Japan is exceptional in that it succeeded in raising the inflation rate after the global financial crisis. However, we are only halfway toward moving out of the so-called Japanification -- that is, secular stagnation where low growth, low inflation, and low interest rates last for a long period -- and the risk that the economy might fall into deflation again continues to warrant attention. Since downside risks to economic activity and prices are still significant, it is necessary to be prepared for a possible economic downturn as one of the risk scenarios. It will become more important to enhance cooperation with the government in terms of fiscal and growth policies.
- Given that quite a long time has passed since the Bank introduced a powerful monetary easing policy, it is becoming more important to continuously make efforts to enhance the sustainability of the policy while weighing up the cumulative effects and side effects.
- The financial system has remained stable on the whole. However, given that the effects of structural problems and the low interest rate environment have continued to accumulate, it is necessary to closely monitor the business conditions of regional financial institutions as well as their efforts made regarding corporate management.
- While some argue that a decline in interest rates reduces interest income of households, which are net depositors, such a decline has positive effects on firms, which are net borrowers. In addition, it also is positive for households in that it brings about improvement in the employment and income situation. In any event, the important thing is whether the utilization rates of labor and capital will be at appropriate levels in the economy as a whole. In a situation of low interest rates in Japan, not only has employment expanded, but also household income and corporate profits have increased, indicating that the current monetary policy has exerted its intended effects.
- Growth in deposits has been about 1 percentage point higher than that in loans, and this trend has continued. The amount outstanding calculated by subtracting firms' deposits from their borrowings has decreased by about 20 percent during the last decade. Under these circumstances, even if interest rates decline further, the effects on economic activity and prices could be limited.
- As for account maintenance fees, the issue is how to balance the service contents and their fair value in a situation where it has been recognized once again that a further improvement

in the functioning of the payment and settlement systems is necessary while avoiding a free ride on such systems, which are part of the social infrastructure. It would be appropriate to distinguish this issue from the discussion over the effects and side effects of monetary policy.

- As side effects stemming from the continuing negative interest rates, some point out the possibility of a decline in inflation expectations due to households' and firms' views on the future becoming more cautious.
- In Europe and the United States, economic policies have been actively discussed amid concern over prolonged low growth and low inflation -- the so-called Japanification. While taking account of fiscal policy and growth strategy, it also would be necessary to review monetary policy in Japan, where low growth and low inflation have been prolonged.

III. Opinions from Government Representatives

Ministry of Finance

- The government submitted to the Diet the supplementary budget for fiscal 2019 totaling about 4.5 trillion yen, with a view to implementing, for example, the economic measures decided by the Cabinet recently. It also submitted to the Diet the budget for fiscal 2020, with a total amount of 102.7 trillion yen, which represents revenues and expenditures in the general account. This aims at achieving both economic revitalization and fiscal consolidation. The government will work to obtain approval from the Diet for these budgets at the earliest possible time so that it can do its utmost with regard to economic and fiscal management.
- The government expects the Bank to continue to work toward achieving the price stability target, taking account of developments in economic activity and prices as well as financial conditions.

Cabinet Office

- The government released the Economic and Fiscal Projections for Medium- to Long-Term Analysis on January 17. In the Economic Growth Achieved Case, the projections show that nominal GDP will reach 600 trillion yen by the end of fiscal 2022 and that a primary balance surplus will be achieved in fiscal 2027. Thus, by pushing forward with steady expenditure reforms, the achievement of the primary balance surplus in fiscal 2025 is expected to come into sight. The government will continue to steadily push forward with its growth strategy and efforts such as expenditure reforms at the same time.

- The government expects the Bank to steadily pursue monetary easing toward achieving the price stability target, taking account of developments in economic activity and prices as well as financial conditions.