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July 27, 2020

Bank of Japan

## Summary of Opinions at the Monetary Policy Meeting<sup>1,2</sup> on July 14 and 15, 2020

### I. Opinions on Economic and Financial Developments

#### *Economic Developments*

- Japan's economy has been in an extremely severe situation with the impact of the novel coronavirus (COVID-19) remaining at home and abroad, although economic activity has resumed gradually.
- Japan's economy is likely to improve gradually from the second half of this year, but the pace is expected to be only moderate while the impact of COVID-19 remains. Thereafter, as the impact subsides, the economy is projected to keep improving further with overseas economies returning to a steady growth path.
- Domestic and overseas economies are in a transition phase toward recovery and are likely to improve from the second half of this year. However, the impact of COVID-19 on people's mindset and developments in firms' medium- to long-term growth expectations warrant close monitoring.
- Although Japan's economy has been in a severe situation due to the impact of COVID-19, it has turned to a recovery recently. That said, there are high uncertainties over future developments, mainly in external demand, and the pace of recovery is expected to be only moderate. It is essential to carefully examine economic indicators at home and abroad.
- Japan's economy has been in an extremely severe situation. It is expected to pick up moderately from the second half of 2020. That said, even in fiscal 2022, the economy is unlikely to return

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<sup>1</sup> English translation prepared by the Bank's staff based on the Japanese original.

<sup>2</sup> "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.

to the level reached before the outbreak of COVID-19, since it will take time for a structural change through which the economy can overcome the impact of COVID-19.

- It is highly likely that the impact of COVID-19 will bring about adjustments in business fixed investment and employment in the short run, but it seems that firms' medium- to long-term growth expectations have been maintained thus far.
- With remaining concern over COVID-19, the pace of recovery in Japan's economy is expected to be slow for the time being. We cannot be optimistic about the timing of an economic recovery since it will be delayed further if COVID-19 spreads again.
- While needing to live with COVID-19 is inevitable, the likelihood of economic recovery depends not only on fiscal and monetary policies but also on public health measures; that is, it matters whether such measures can ensure safety and security as well as how those measures can alleviate people's stress when they go out and make close contact with others. Therefore, the recovery path varies among countries or sectors.
- Future developments in economic activity depend on the balance between the consequences of COVID-19 and public health and macroeconomic measures. If the impact of COVID-19 is prolonged, downward pressure on economic activity will continue to be exerted and, as time passes, the solvency problems of households and firms could materialize, employed persons not at work may become unemployed, and a vicious cycle from unemployment to less income and spending would emerge. Uncertainties stemming from changes in the industrial structure that might occur due to the impact of COVID-19 would also make firms and households cautious about their consumption and investment.
- Risks to future developments include the consequences of COVID-19, geopolitical risks, political events, and whether the government's support in each country will continue even after this summer, and they entail extremely high uncertainties. These risks are likely to remain skewed to the downside throughout the projection period.
- While the impact of COVID-19 is expected to be prolonged, downward pressure on wages is likely to continue for the time being.
- Effectively interest-free loans are being provided to small and medium-sized firms through private financial institutions in response to COVID-19 based on the government's economic measures. Such loans will have significant positive effects since they serve as support for firms that have difficulties in raising funds. On the other hand, even after the impact of COVID-19

subsidies, such loans might put downward pressure on spreads on the ordinary loans that will be made.

### ***Prices***

- The year-on-year rate of change in the consumer price index (CPI) is likely to be negative for the time being, mainly affected by COVID-19 and the past decline in crude oil prices. Thereafter, it is expected to turn positive and then increase gradually, mainly due to economic improvement.
- The year-on-year rate of change in the CPI is likely to increase toward achieving the price stability target, although it will take time.
- With the pace of economic recovery being moderate, it is unlikely that prices will regain the momentum toward 2 percent inflation within the projection period.
- The impact of COVID-19 on prices should be carefully examined, including the second-round effects from a somewhat long-term perspective, such as on firms' price-setting behavior and developments in inflation expectations.
- It is difficult to assess how changes in the supply and demand conditions due to the impact of COVID-19 will affect price developments, since they could exert upward and downward pressure on prices and there are risks that are specific to prices in Japan. The formation mechanisms, such as of inflation expectations, should be examined more prudently than before.
- The economic shock of COVID-19 seems to be largely attributable to a negative demand shock. The pace of economic recovery is expected to be slow and that of improvement in the output gap also is likely to be only moderate. As for inflation expectations, there are signs that a decline in short-term expectations is affecting medium- to long-term ones. Under these circumstances, downward pressure will likely be exerted on prices for the time being.

## **II. Opinions on Monetary Policy**

- The enhancement of monetary easing since March has had positive effects in terms of maintaining stability in financial markets and ensuring smooth corporate financing.
- Financial and capital markets as well as corporate financing have remained stable, and the Bank's responses to COVID-19 have been effective. For the time being, it is appropriate for the Bank to thoroughly examine the policy effects.

- It is important for the Bank to continue to support financing, mainly of firms, and maintain stability in financial markets through the following three measures: the Special Program to Support Financing in Response to the Novel Coronavirus (COVID-19); an ample provision of yen and foreign currency funds; and active purchases of assets such as exchange-traded funds (ETFs).
- Amid developments in financial and foreign exchange markets being stable, partly due to swift policy responses by the Bank, the top priority for monetary policy for the time being is to contribute to sustaining businesses and employment by continuing to support corporate financing.
- While continuing with the current monetary policy stance, it is necessary to carefully examine, for example, whether the issue of corporate financing will lead to a solvency problem.
- Downward pressure on prices is likely to intensify in the short run, but medium- to long-term inflation expectations have been generally maintained to this point. It is appropriate to consider the policy responses for achieving the price stability target of 2 percent when the impact of COVID-19 almost subsides.
- For the time being, it is important to continue to closely share information between the government and the central bank as well as among major central banks, assess the adequacy of the existing monetary policy framework, and swiftly make policy responses when necessary. On this basis, attention is warranted on the risks to the financial system if the current policies are conducted for a prolonged period.
- At the time of an economic crisis, it is necessary for fiscal and monetary policies to closely cooperate in an appropriate manner.
- While pursuing their respective roles, it is important for the Bank to cooperate with the government in terms of not only fiscal policy but also policies concerning structural reforms that aim at responding to the "new normal."
- It is appropriate to revise the forward guidance to make it a more powerful one that does not allow deflation to take hold and leads to additional easing measures under the concrete conditions related to prices.
- To ensure that the economy will follow a recovery path, it is necessary for firms to swiftly regain their motivation to plan and conduct growth strategies. Considering this point, the Bank

should carefully examine the effects that monetary policy has on business management from a medium-term perspective.

- Taking into account the experience of the current crisis, the Bank should further examine appropriate monetary policy conduct during the COVID-19 era. It also is necessary to examine the transmission channels and effects of policy measures while paying attention to risks that prices and growth expectations will decline further and that such situation will last for a protracted period.
- Return on equity of financial institutions could decline due to an increase in credit costs and to decreases in lending margins and interest income in the low interest rate environment. In this situation, while also taking into account an accumulation of side effects on the functioning of financial intermediation, it is necessary to examine future developments more carefully than before, including from the monetary policy side, so that deterioration in the real economy will not affect stability of the financial system.

### **III. Opinions from Government Representatives**

#### ***Ministry of Finance***

- The government is proceeding with discussions that mainly regard the Basic Policy on Economic and Fiscal Management and Reform 2020 (hereafter the Basic Policy) and the growth strategy in order to obtain Cabinet decisions on these policies.
- As described in the draft of the Basic Policy, the government will consider without delay implementing what had been decided by the Cabinet and addressing challenges to the reform, thereby working toward achieving both economic revitalization and fiscal soundness.
- The government expects that the Bank will contribute to supporting economic and financial activities by doing its utmost, mainly to ensure smooth corporate financing and maintain stability in financial markets.

#### ***Cabinet Office***

- Under the Basic Policy, the government aims at fully protecting people's lives, livelihoods, employment, and businesses by taking measures against COVID-19 and making responses to natural disasters, which are becoming more frequent and devastating. The government compiled measures to be taken as five pillars, aiming at overcoming challenges that became distinct in the face of the spread of COVID-19 -- such as falling behind in digitalization in the

administrative area and a risk of centralization in Tokyo in terms of crisis management -- and also at realizing a society under the "new normal" at the earliest possible time.

- The government expects the Bank to continue conducting appropriate monetary policy while closely monitoring current and future developments.