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November 11, 2024

Bank of Japan

Summary of Opinions at the Monetary Policy Meeting[1,2]

on October 30 and 31, 2024

I. Opinions on Economic and Financial Developments

Economic Developments

- Japan's economy has recovered moderately, although some weakness has been seen in part. It is likely to keep growing at a pace above its potential growth rate, as a virtuous cycle from income to spending gradually intensifies.

- The current situation of Japan's economy is that, while growth in private consumption has remained somewhat weak, production, employment, and income, for example, have seen moderate growth.

- The expanding trend in private consumption is likely to become more evident, since the uptrend in real wages is expected to take hold. It is necessary to continue to closely monitor whether the channels are functioning smoothly, both on the demand side, through which wage increases lead to an expansion in consumption, and the supply side, through which they are passed on to consumer prices.

- When assessing developments in private consumption and economic activity, it is appropriate to use standards that are different from those applied before the COVID-19 pandemic and that do not put too much emphasis on macro data. This is due to, for example, the limit on how much information can be captured on e-commerce, the impact of changes in consumer behavior since the pandemic, and to firms enhancing their pricing strategies since then by using consumer purchasing data.

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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.

- There is a risk of a slowdown in the U.S. economy if long-term interest rates remain elevated for some time. This is because valuation adjustments, as shown in the price-earnings ratio, are likely to lead to a decline in prices of assets including stocks and real estate, thus affecting the real economy, such as in terms of consumption and business fixed investment.
- Given the labor shortages, the necessity of wage hikes is naturally being recognized, including by small and medium-sized firms, and the wage growth rate is expected to continue to be at a high level next year.
- At the October 2024 meeting of the general managers of the Bank's branches, there were many reports that, while small and medium-sized firms had recorded low profits, they had raised wages as a defensive step to retain employees. Considering this, the sustainability of wage hikes is of concern. Although it may take some time, the key to raising wages in a sustainable and positive manner is for small and medium-sized firms to make structural reforms to grow their businesses and thereby increase their productivity.
- There have been a significant number of reports from corporate executives of small and medium-sized firms that they welcome the retracement of the yen's depreciation, and that foreign exchange rates have a larger impact on business management than interest rates. Moreover, various survey results seem to suggest that households also welcome the yen's retracement.
- Due to labor supply constraints that reflect labor shortages, there is a risk that Japan's economic growth will slow through, for example, firms scaling down their businesses by withdrawing from business areas with low profitability.

Prices

- Underlying inflation, measured by the consumer price index (CPI), is expected to increase gradually. In the second half of the projection period of the October 2024 *Outlook for Economic Activity and Prices*, it is likely to be at a level that is generally consistent with the price stability target.
- Looking at the year-on-year rate of change for October in the CPI for Tokyo's 23 wards, while the rates for rice prices and -- due to the rise in rice prices -- dining-out increased, it can be assessed that the developments in the CPI for other items, including services for which prices were revised, were generally in line with the Bank's outlook.

- It has been more than two years since the import price index on a yen basis reached its peak, and one and a half years since it more or less bottomed out. Since previous cases suggest that it takes about six months for import prices to have their greatest effect on the CPI, it is likely that the waning of the effects of import price rises will run its course in the near future.

- There is concern over how prices will be affected by the future course of fiscal policies in Japan and the United States, as well as by developments in foreign exchange rates reflecting these policies.

II. Opinions on Monetary Policy

- The Bank's basic thinking remains that if the outlook for economic activity and prices will be realized, the Bank will adjust the degree of monetary accommodation accordingly. On this basis, the Bank needs to pay due attention to the future course of overseas economies, particularly the U.S. economy, and developments in financial and capital markets. It also needs to examine how these factors will affect the outlook for Japan's economic activity and prices, the risks surrounding them, and the likelihood of realizing the outlook.

- Given that uncertainties over the U.S. economy have decreased, the Bank is entering a phase where it will communicate without using the language of whether it has "enough time." While attention continues to be warranted on various uncertainties, it is important for the Bank to communicate that, at each MPM, it will examine the risks surrounding Japan's economic activity and prices and the likelihood of realizing the outlook for economic activity and prices, based on the data available at the time of each meeting.

- In the United States, interest rates have risen and the dollar has appreciated, as the risk of the economy making a hard landing and the possibility of a significant policy interest rate cut becoming necessary to achieve a soft landing have waned somewhat. It should be noted, however, that these developments reflect not only an improvement in U.S. economic indicators, but also speculations regarding the presidential and congressional elections. Therefore, it cannot be judged at this point that markets are stabilizing. As the Bank has been expecting to raise the policy interest rate at a moderate pace, it has time to monitor the future course of the U.S. economy, including that after the presidential election.

- It is important for the Bank to communicate effectively its core message that "if the outlook for economic activity and prices will be realized, the Bank will continue to raise the policy interest rate accordingly."

- Considering the heightening uncertainties in Japan and abroad, the Bank needs to conduct monetary policy with caution. Therefore, the Bank should maintain the current policy at this meeting.
- The shift to "a state with positive interest rates" entails uncertainties, and it is therefore necessary for the Bank to take time and exercise caution when raising the policy interest rate.
- In its previous five cycles of policy interest rate hikes, the Bank turned to rate cuts after the Federal Reserve cut its rate, but this time is different. Given that there is no pressure on balance sheet adjustments in the financial, corporate, and household sectors in the two economies, substantial monetary easing is not required at this point. The Bank should consider further rate hikes after pausing to assess developments in the U.S. economy.
- With the monetary policies of the Bank and the Federal Reserve moving in opposite directions, the markets, particularly foreign exchange markets, could see large fluctuations. Attention is warranted on the risk that monetary policy normalization over the long run will be hindered if further rate hikes by the Bank trigger a shock in the markets.
- Depending on the result of the U.S. presidential election, markets could see large fluctuations, and it is therefore necessary for the Bank to be well prepared.
- Upside risks to prices have decreased, partly due to a decline in inflation rates in the United States and Europe, and to the effects of progress in price competition in the global market. The Bank should maintain the current policy interest rate for the time being, until it examines various economic data to assess factors such as corporate profits, business fixed investment, private consumption, the cost pass-through rate, and developments in structural business reforms by firms, and becomes more confident about the sustainability of the virtuous cycle between wages and prices.
- It seems that, if economic activity and prices develop as expected, the Bank can follow a path in which it raises the policy interest rate gradually so that the rate will be 1.0 percent in the second half of fiscal 2025 at the earliest. Based on this assumption, it can be considered at this meeting that the Bank has time to monitor developments in economic activity and prices.
- It is difficult for the Bank to show with confidence the medium-term path of the policy interest rate to the markets because there are high uncertainties regarding the level of the neutral interest rate and the transmission mechanism of monetary policy.

- Concerning investment by financial institutions, attention is warranted on a possible increase in risk-taking by those with relatively low risk tolerance. If interest rate levels remain lower than these institutions' targets for investment, they could increase their investment in Japanese government bonds (JGBs) with long maturities to earn carry income.

- There is concern that a tightening of supply and demand conditions of the cheapest-to-deliver (CTD) issues of JGB futures, which is one of the side effects of yield curve control, could lead to a decline in liquidity in the JGB market and to distortions in interest rates. In order to mitigate this, it is important that the Bank continue to encourage counterparties of the Securities Lending Facility to use without hesitation the Bank's measure that enables them to request a reduction in the amount of the CTD issues repurchased by the Bank.

III. Opinions from Government Representatives

Ministry of Finance

- The government's stance is that it will prioritize breaking free from deflation in its economic and fiscal management. As a first step, the government is formulating an economic policy package in accordance with the prime minister's instructions given on October 4. It will decide on comprehensive economic measures and submit the supplementary budget to the Diet.

- The government expects the Bank to conduct monetary policy as appropriate toward sustainable and stable achievement of the price stability target of 2 percent while closely cooperating with the government. Moreover, it expects the Bank to communicate effectively with financial and capital markets, including through its dissemination of information.

Cabinet Office

- The government assesses that Japan's economy is recovering at a moderate pace, although it is still pausing in part. That said, due attention is warranted on factors such as slowdowns in overseas economies.

- Standing on the principle that "a sound economy is the foundation of fiscal health," the government will prioritize breaking free from deflation in its economic and fiscal management, and will aim to achieve a "growth-oriented economy driven by wage increases and investment."

- The government expects the Bank to continue to conduct monetary policy as appropriate toward achieving the price stability target of 2 percent in a sustainable and stable manner, while continuing to closely cooperate and exchange views with the government.