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Bank of Japan

Summary of Opinions at the Monetary Policy Meeting^{1,2} on October 30 and 31, 2023

I. Opinions on Economic and Financial Developments

Economic Developments

- Japan's economy has recovered moderately and is likely to continue to do so. However, there remain extremely high uncertainties surrounding economic activity and prices.
- Upside and downside risks to the outlook for Japan's economy have continued to be fairly high. In particular, uncertainties regarding the U.S. economy have remained despite heightened expectations for a soft landing, and thus close monitoring is warranted on the impact of the economic developments.
- Although households' spending behavior has become more defensive due to price rises, private consumption has been resilient, supported by expectations for wage increases and firms' various measures to promote sales.
- In order to achieve sustained wage increases and a virtuous cycle of growth and distribution, it is necessary that firms' earning power strengthen -- particularly for small and medium-sized firms, which have lagged behind in reforms -- and that their capacity to raise wages increase. Attention is warranted on the extent to which listed firms' earnings estimates for fiscal 2023 will be revised upward in their announcements of financial results for the first half of the fiscal year and whether the rises in earnings will have increasingly positive effects on small and medium-sized firms.

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.

- The key to enhancing Japan's economic growth is the growth of startups, which create new markets and lead the growth in the economy, and improvement in their funding conditions.

Prices

- While the outlook for Japan's inflation rate has been revised upward, this is mainly due to cost-push factors. To achieve the 2 percent target in a sustainable and stable manner, after these factors disappear, the virtuous cycle between wages and prices needs to keep operating in a self-sustaining manner.
- Although the year-on-year rate of increase in the consumer price index (CPI) has started to decelerate, this has been more moderate than projected, since a pass-through of cost increases to selling prices has spread among firms to a greater extent than expected.
- The upward revisions in the outlook for the inflation rate since April are due to price revisions spreading among firms to a greater extent than expected, including in terms of how frequently and how much prices are raised, and the price revisions seem to reflect an economic recovery after the pandemic and expectations for wage increases.
- In order to confirm that the virtuous cycle between wages and prices has intensified, close attention needs to be paid both to next year's annual spring labor-management wage negotiations and to whether the wage increases will be reflected in prices.
- Developments in wage hikes by firms next spring will be a major key to achieving the virtuous cycle between wages and prices.
- There seems to have been a change in firms' behavior of leaving wages unchanged, which had lasted since the bursting of the bubble economy.
- The year-on-year rate of increase in the services producer price index (SPPI), which is sticky and tends to reflect wage developments, has accelerated steadily. Close attention is required on whether upward pressure on prices stemming from wage increases will rise further, including among small and medium-sized firms.
- Firms have been setting wages and prices based on a combination of (1) a pass-through of a rise in import prices, (2) wage hikes, (3) a pass-through of an increase in personnel expenses, and (4) diversifying pricing strategies and increasing the value-added of products. However, developments in all of these factors remain mixed, and underlying inflation needs to continue to be carefully examined.

- It is highly possible that the wage growth to be agreed in next year's base pay negotiations will exceed that agreed this year, as suggested by the fact that this year's inflation outlook of the private sector, which is a starting point for the negotiations, is higher than last year. Considering this possibility, as well as upward movements in inflation expectations and underlying inflation, it seems that achievement of the price stability target is coming into sight. The second half of fiscal 2023 will be an important period for determining whether the target will be achieved.

II. Opinions on Monetary Policy

- Sustainable and stable achievement of the price stability target is not yet envisaged with sufficient certainty at this point, and thus the Bank needs to patiently continue with monetary easing under yield curve control.
- The Bank's stance is that it will continue with the framework of yield curve control and the negative interest rate policy, at least as long as it is necessary for maintaining the price stability target of 2 percent in a stable manner. To confirm that this aim has been achieved, it is necessary to carefully examine future developments in wage hikes and whether the virtuous cycle between wages and prices is operating from both sides.
- With extremely high uncertainties surrounding economies and financial markets at home and abroad, it is appropriate for the Bank to increase the flexibility in the conduct of yield curve control, so that long-term interest rates will be formed smoothly in financial markets in response to future developments.
- As there is still a distance to go before achieving the 2 percent target with the virtuous cycle between wages and prices, it is important for the Bank to keep supporting the momentum for wage hikes through continuation of monetary easing. In this situation, the Bank should maintain the framework of yield curve control while modifying the conduct of it.
- Japanese long-term interest rates have been under unexpected upward pressure that reflects the effects of a rise in U.S. long-term interest rates. Given this situation, while the Bank needs to patiently continue with monetary easing, further increasing the flexibility in the conduct of yield curve control is desirable.
- Given, for example, recent developments in inflation measures and remarks by corporate executives in view of next year's annual spring labor-management wage negotiations, the likelihood of achieving the price stability target of 2 percent in a sustainable and stable

manner seems to have risen further since the July MPM. Therefore, it will be necessary for the Bank to gradually adjust the degree of monetary easing down from its maximum level.

- Although the Bank has gradually reduced the degree of control over the yield curve since last December, the effects of monetary easing have been sufficiently maintained as inflation expectations have risen and real interest rates have been significantly low. At this stage, to strike a balance between the positive effects and side effects, it is appropriate for the Bank to increase the flexibility in the conduct of yield curve control at this MPM.
- Even with some upward movements in nominal long-term interest rates, it is likely that real long-term interest rates will continue to be negative and the effects of monetary easing will remain strong. On the other hand, if the nominal long-term interest rates continue to be strictly capped through fixed-rate purchase operations for consecutive days, there is an increasing risk of large side effects on market functioning and market volatility.
- The decision at this MPM to increase the flexibility in the conduct of yield curve control will lead to improving its resilience through reducing the chance of speculative moves.
- Since the decision at the July MPM to conduct yield curve control with greater flexibility, the functioning of bond markets has improved. However, due to a rise in inflation, investors' expectations of interest rates have risen recently, which has begun to affect firms' long-term financing. In addition, side effects due to strictly controlling long-term interest rates, including a decrease in hedging transactions, need to be avoided.
- In increasing the flexibility in the conduct of yield curve control, it is important to let interest rates be determined by the market as much as possible while preventing sharp fluctuations in them, and to work toward a securing of and recovery in liquidity.
- Increasing the flexibility in the conduct of yield curve control is quite favorable not only in terms of constraining the materialization of side effects and thereby effectively continuing with monetary easing until an exit, but also in terms of smoothly proceeding with normalization of monetary policy while maintaining monetary easing after the future exit.
- In order to avoid unnecessary market speculation, it is important for the Bank to clearly explain to the public that its policy decisions are based on the outlook for economic activity and prices.
- With the future exit from the current monetary policy in mind, it is important for the Bank to encourage price formation by utilizing market functions, to improve market liquidity,

particularly in bond markets, and to provide communication to the market in preparation for a "world where interest rates exist" since interest rates have been low for so long.

- It is still unclear whether wage increases that exceed price rises will be achieved, and revising yield curve control at this time could be perceived as monetary tightening. In order not to lose the opportunity to achieve a virtuous cycle between wages and prices, it is appropriate for the Bank to patiently continue with the current monetary easing for the time being.

III. Opinions from Government Representatives

Ministry of Finance

- With regard to the proposals made at this MPM, the government expects the Bank to make a proper judgment from the perspective of conducting appropriate monetary policy.
- In accordance with the prime minister's instructions, the government is formulating economic measures. It aims to swiftly compile the supplementary budget for fiscal 2023 after the measures are decided and to carry out all possible measures.
- The government expects the Bank to conduct appropriate monetary policy toward achieving the price stability target in a sustainable and stable manner while closely cooperating with the government.

Cabinet Office

- The government considers that the proposals made at this MPM are aimed at enhancing the sustainability of monetary easing measures that are necessary for the Bank to achieve the price stability target in a sustainable and stable manner. It deems it important for the Bank to carefully explain to the public its intention regarding the changes proposed at the meeting.
- The government expects the Bank to continue to conduct appropriate monetary policy toward achieving the price stability target of 2 percent in a sustainable and stable manner, accompanied by wage increases, taking account of developments in economic activity and prices as well as financial conditions.