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August 8, 2024

Bank of Japan

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

on July 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.

- Economic activity and prices have been on track, as seen in the results of this year's annual spring labor-management wage negotiations being reflected in wages.

- Although private consumption has not been so strong, it is likely to remain resilient. Not only is this due to factors such as cuts in income tax and inhabitant tax, it is also because the results of this year's annual spring labor-management wage negotiations are likely to be further reflected in wages and summer bonus payments have been favorable.

- Private consumption appears to lack momentum based on macroeconomic statistics, but microeconomic data have shown some strong developments. Private consumption has therefore not necessarily been weak.

- Weakness has been seen mainly in private consumption, as real wages have continued to decline, since the rise in prices has been greater than the growth in nominal wages. The economic situation is expected to improve over time as long as momentum in nominal wage growth is maintained. That said, Japan is currently in a phase in which it is important to

[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.

patiently monitor if waves of wage hikes will permeate the economy and increase sustainability.

- Prolonged negative real interest rates can cause income transfer from fund providers, including the household sector, to fund users, who are less burdened in real terms. It is necessary to bear this in mind when assessing economic and financial developments.

- There is a growing difference in business performance between firms, depending on how well they have adapted to the new economic environment. It has therefore become difficult to grasp the true state of the economy merely by observing general trends.

- Structural issues of Japan's economy lie in subdued consumption due to the declining birthrate and aging population, and the industrial structure generating low profits. The new Nippon Individual Savings Account (NISA) program is expected to stimulate consumption through a sustained increase in income based on financial assets. It is also expected that fostering businesses with high international competitiveness will lead to industrial clusters and an expansion in exports, which will likely affect growth-oriented small, medium-sized, and larger firms in the form of an increase in investment for domestic capacity expansion and a rise in employment.

Prices

- Underlying inflation, measured by the consumer price index (CPI), is expected to increase gradually. In the second half of the projection period, it is likely to be at a level that is generally consistent with the price stability target.

- Medium- to long-term inflation expectations have risen and the results of this year's annual spring labor-management wage negotiations have started to be reflected in the statistics. Considering this and other factors, a virtuous cycle between wages and prices has likely begun to operate, and underlying inflation has shown steady progress toward 2 percent.

- The likelihood of achieving the inflation target has increased further. That said, upside risks to prices require attention, since a rising number of industries have seen supply shortages and excess demand as a result of labor shortages.

- Upward pressure on prices is likely to remain because of tight labor market conditions and the effects of the upper limits on working hours, in addition to the rise in import prices due to inflation overseas and the past depreciation of the yen.

- Apart from the achievement of the price stability target in a strict sense, it is necessary to recognize that households in particular have started to become more conscious of the likelihood of the target being achieved, with inflation now in its third year above 2 percent.

II. Opinions on Monetary Policy

- Japan's economic activity and prices have been developing generally in line with the Bank's outlook. The year-on-year rate of change in import prices has turned positive again, and upside risks to prices require attention. It is therefore appropriate for the Bank to raise the policy interest rate and adjust the degree of monetary accommodation from the perspective of sustainable and stable achievement of the price stability target.

- Japan's economic activity and prices after the policy changes this March have been developing generally as expected. The current economic situation seems to be favorable enough that the Bank can raise the significantly low policy interest rate to some degree.

- Real interest rates are at their most negative levels in the past 25 years, and the degree of monetary accommodation, based on various indicators, has been significantly above its average during the period of quantitative and qualitative monetary easing (QQE).

- Even if the Bank raises the policy interest rate, the nominal interest rate will continue to be at a highly accommodative level of 0.25 percent, and there is no change in the Bank's stance to firmly support the economy.

- Normalization of monetary policy must not be an end in itself, and future policy needs to be conducted carefully.

- Given the current environment surrounding prices, it may be time to consider raising the policy interest rate slightly. It should be noted that raising the rate at a moderate pace means an adjustment in the degree of monetary accommodation in accordance with underlying inflation, which will not have monetary tightening effects.

- Assuming that the price stability target will be achieved in the second half of fiscal 2025, the Bank should raise the policy interest rate to the level of the neutral interest rate toward that time. As the level of the neutral rate seems to be at least around 1 percent, in order to avoid rapid hikes in the policy interest rate, the Bank needs to raise the policy interest rate in a timely and gradual manner, while paying attention to how the economy and prices respond.

- After the policy changes proposed at this MPM, if it is confirmed that prices will develop in line with the Bank's outlook and that positive corporate behavior -- such as solid business fixed investment, sustained wage hikes, and a continued pass-through of cost increases to selling prices -- will be maintained, it will be necessary to proceed with further adjustment of the degree of monetary accommodation as appropriate.
- While it is not that the Bank cannot raise the policy interest rate at all at present, it is necessary to more carefully assess how the economic situation has improved with wage hikes becoming widespread, based on relevant data, as there are many datasets showing somewhat weak developments in, for example, the economic growth rate and private consumption.
- Since there is little data confirming sustainable growth in Japan's economy at this point, the Bank should decide on changing the guideline for money market operations after assessing key economic data at the next MPM. I am therefore in dissent with raising the policy interest rate at this MPM.
- In principle, long-term interest rates are to be formed in financial markets, and it is appropriate for the Bank to reduce its purchase amount of Japanese government bonds (JGBs) in a predictable manner, while allowing enough flexibility to support stability in the JGB markets.
- In order to allow interest rates to be determined by the market, the Bank should, in principle, proceed with the reduction of its purchase amount of JGBs according to the plan, in a straightforward manner.
- The plan for the reduction of the Bank's purchase amount of JGBs is aimed at promoting a more active role for markets, not at monetary tightening.
- It is desirable for the Bank to reduce its purchase amount of JGBs steadily at a moderate pace. The outcome of the "Bond Market Group" meetings indicates that market participants' views on the reduction vary widely. Therefore, the risk of market disruption arising from one-sided expectation formation is not high.
- The reduction of the Bank's purchase amount of JGBs can be carried out without surprising the market if done prudently by, for example, reducing monthly purchases at an even pace each calendar quarter over a period slightly longer than a year and a half, to about 3 trillion yen, and by conducting an interim assessment while allowing flexibility to make nimble responses.

- It is expected that there will be a wider range of investors as long-term interest rates are formed more freely in the JGB markets.

- Reducing the Bank's purchase amount of JGBs can be seen as being the same as issuing JGBs, in that it increases JGB supply in the market. Given this, it can be considered that, with the reduction proposed at this MPM, the market will enter a phase of historically large JGB issuances. With possible changes in the structure of JGB holdings in mind, it is important for the Bank to monitor developments in the market and investor behavior.

- There is a long way to go to normalize the Bank's balance sheet, and the side effects of its large amount of JGB holdings will likely remain for some time. It is necessary to continue to carefully monitor market functioning and other factors.

III. Opinions from Government Representatives

Ministry of Finance

- The government will make steady progress toward achieving both economic revitalization and fiscal consolidation, based on the Basic Policy on Economic and Fiscal Management and Reform 2024.

- The government expects the Bank's reduction of its purchase amount of JGBs to be conducted as appropriate while giving due consideration to stability in the bond market and other factors. The government considers that the change in the policy interest rate has been judged necessary for achieving the price stability target of 2 percent, and it expects the Bank to explain its policy intention carefully to the public.

- 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.

Cabinet Office

- Regarding the reduction of the Bank's purchase amount of JGBs, the government expects the Bank to take action flexibly as necessary, depending on the situation, while communicating with the market as appropriate. The government also expects the Bank to carefully explain its policy intention to the public in the case of a policy interest rate hike, so that it does not have unexpected effects on financial and capital markets and the real economy.

- 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 cooperate closely with the government and monitor the virtuous cycle between wages and prices.