

Haruhiko Kuroda: The Bank's Semiannual Report on Currency and Monetary Control

Statement by Mr Haruhiko Kuroda, Governor of the Bank of Japan, before the Committee on Financial Affairs, House of Councillors, Tokyo, 22 November 2016.

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Introduction

The Bank of Japan submits to the Diet its *Semiannual Report on Currency and Monetary Control* in June and December. I am pleased to have this opportunity today to talk about developments in Japan's economy and present an overall review of the Bank's conduct of monetary policy.

I. Economic and Financial Developments in Japan

At the Monetary Policy Meeting (MPM) held on November 1, the Bank released the *Outlook for Economic Activity and Prices* (Outlook Report), which presents its projections for Japan's economic activity and prices through fiscal 2018. Based on this, I will first explain economic and financial developments in Japan.

Japan's economy has continued its moderate recovery trend, although exports and production have been sluggish due mainly to the effects of the slowdown in emerging economies. With regard to the outlook, it is likely to continue growing at a pace above its potential through the projection period — that is, through fiscal 2018 — with a virtuous cycle from income to spending being maintained in both the corporate and household sectors, on the back of highly accommodative financial conditions and the effects of the government's large-scale stimulus measures, as well as the recovery in overseas economies.

On the price front, the year-on-year rate of change in the consumer price index (CPI, all items less fresh food) has been slightly negative due to the effects of the decline in energy prices. As for the outlook, it is likely to be slightly negative or about 0 percent for the time being, and as the aggregate supply and demand balance (the output gap) improves and medium- to long-term inflation expectations rise, it is expected to increase toward 2 percent — the price stability target — in the second half of the projection period. The timing of the year-on-year rate of change in the CPI reaching around 2 percent will likely be at the end of the projection period — that is, around fiscal 2018. Thus, the momentum toward achieving the price stability target of 2 percent seems to be maintained. However, it is somewhat weaker than the previous outlook made in the July Outlook Report, and thus developments in prices warrant careful attention going forward.

II. Conduct of Monetary Policy

At the September 2016 MPM, the Bank conducted a comprehensive assessment of the developments in economic activity and prices, as well as of the policy effects since the introduction of quantitative and qualitative monetary easing (QQE). Based on its findings, with a view to achieving the price stability target of 2 percent at the earliest possible time, the Bank introduced “QQE with Yield Curve Control,” which is a new framework for strengthening monetary easing. This framework consists of two major components.

The first is “yield curve control.” QQE, which was introduced in April 2013, has brought about improvements in economic activity and prices mainly through the decline in real interest rates, and Japan's economy is no longer in deflation, which is commonly defined as a sustained decline in prices. With “yield curve control,” the Bank seeks to bring about such a decline in real interest rates by controlling short-term and long-term interest rates. It will work toward the

formation of the most appropriate yield curve with a view to maintaining the momentum toward achieving the price stability target of 2 percent, while taking account of developments in economic activity and prices as well as financial conditions. Specifically, in the guideline for market operations — which is decided at and released after every MPM — the Bank will set two interest rate levels: the short-term policy interest rate to be applied to current accounts held by financial institutions at the Bank, and the target level of yields on 10-year Japanese government bonds (JGBs). It will conduct JGB purchases aiming to achieve the target level of the long-term interest rate specified by the guideline, while indicating the approximate amount of JGBs to be purchased.

The second is an “inflation-overshooting commitment.” In order to achieve the price stability target of 2 percent, it is necessary to drastically convert the deflationary mindset among people and raise inflation expectations. On this point, inflation expectation formation in Japan is still largely adaptive, and thus tends to be strongly affected by the observed inflation rate. Against this backdrop, the Bank introduced a very powerful commitment to “continue expanding the monetary base until the year-on-year rate of increase in the observed CPI (all items less fresh food) exceeds the price stability target of 2 percent and stays above the target in a stable manner.” By presenting its strong determination to achieve the price stability target, the Bank aims to enhance the credibility of achieving 2 percent among the public and to raise inflation expectations in a more forceful manner.

At the MPM held on November 1, the Bank decided to maintain the guideline for market operations in which the short-term policy interest rate is set at minus 0.1 percent and the target level of 10-year JGB yields is set at around zero percent. It will make policy adjustments as appropriate, taking account of developments in economic activity and prices as well as financial conditions, with a view to maintaining the momentum toward achieving the price stability target.

Thank you.