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December 27, 2024

Bank of Japan

Summary of Opinions at the Monetary Policy Meeting[1,2]
on December 18 and 19, 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.

- Indicators have continued to show that economic activity and prices have been in line with the path toward realizing the Bank's outlook. Given this, the likelihood of realizing the outlook has increased.

- While the U.S. economy has been solid, there are high uncertainties at this point surrounding the economic policies of the incoming administration. It will be necessary to examine the effects of these policies.

- The U.S. economy could accelerate again in the near future, rather than making a soft landing, because the economy has been resilient and is expected to be underpinned by factors such as the fiscal policies of the new administration. On the other hand, markets could see large fluctuations due to, for example, the release of indicators. It is therefore necessary to closely examine developments in the economy until expectations for the economy bottoming out emerge.

- Regarding uncertainties over the U.S. economy, the focus has shifted more toward upside risks than downside risks, compared with how it was in August.

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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.

- The policies of the new U.S. administration could affect foreign exchange markets by causing inflation, which could lead to higher interest rates, and, in turn, a stronger U.S. dollar. That said, attention should also be paid to the possibility that the administration will aim at a weaker U.S. dollar to focus on export industries.

- Financial and capital markets have remained relatively stable. The yen has remained considerably weak compared with a while ago. If exchange rate misalignment grows, this could trigger larger shocks when such misalignment is adjusted.

- From the perspective of confirming that the virtuous cycle between wages and prices has intensified, a little more information is needed regarding future wage developments, such as the momentum toward next year's annual spring labor-management wage negotiations.

- Looking at employment-related indicators, labor shortages are expected to become more acute. It is therefore highly likely that fairly high wage hikes will be achieved next year, led by large firms that have capacity for raising wages.

- Solid wage growth that is consistent with price rises of 2 percent can be expected at next year's annual spring labor-management wage negotiations. This reflects a paradigm shift in corporate behavior, in that firms now regard wage hikes as a premise to secure their workforce, rather than as a form of giving back profits to employees.

- Many small and medium-sized firms have raised wages as a defensive step, which has made it difficult for them to raise wages while making business fixed investment. In this situation, it is likely that the employees of such firms have some concerns over the sustainability of wage hikes.

- Consumer attitudes toward price increases are still severe, and firms have had no choice but to be hesitant in sufficiently passing on wage increases to selling prices. It will therefore likely take time for wage increases to lead to a sufficient expansion in private consumption and to a rise in services prices through a pass-through of cost increases to selling prices. It will be important to examine whether there is a change in the mindset of consumers, which has been at the root of the problem.

- Private consumption has remained solid against the price rises so far, but downside risks to consumption could heighten if inflation expectations rise further. The way in which private consumption is assessed through various price indicators will be extremely important.

- Firms need to continue their efforts to improve earning power to sustainably raise wages, which represent the value brought by employees. Meanwhile, regional financial institutions are expected to strengthen their follow-up support to small and medium-sized firms so that such firms can make structural reforms to step up the scale of their businesses.

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.

- It seems that actual price developments have been strong, reflecting factors such as a surge in rice prices and a rise in services prices, which are considered to be relatively sticky. However, as inflation expectations have been stable, Japan's economy is not in a state where prices will rise at an accelerated pace.

- The month-on-month rate of increase in the CPI (all items less fresh food and energy, seasonally adjusted) has clearly accelerated since June, generally maintaining an increase of around 3.5 percent on an annualized basis.

II. Opinions on Monetary Policy

- If its outlook for economic activity and prices will be realized, the Bank will adjust the degree of monetary accommodation accordingly. In this regard, the Bank needs to judge the timing of the adjustments after carefully examining various data and information.

- In order to decide whether to raise the policy interest rate, the Bank should, on the domestic front, focus on developments in wages, services prices, and private consumption. On the external front, it should focus on developments in the U.S. economy and the policy conduct, as well as developments in financial and capital markets reflecting these factors. It is therefore appropriate for the Bank to examine developments in the run-up to next year's annual spring labor-management wage negotiations and the situation surrounding the new U.S. administration.

- There are high uncertainties over the course of discussions on tax and fiscal policy in Japan and over the policy stance of the new U.S. administration taking office at the beginning of

2025. Thus, from the perspective of risk management, it is appropriate for the Bank to maintain the current monetary policy at this meeting.

- At this stage, the upside risks to prices do not suggest a pressing need to raise the policy interest rate. Import prices have been stable and yen carry trade positions have not been built up. On the domestic front, the cumulative increase in wages over the past three years has not caught up with that in prices, and it is therefore desirable that relatively high wage increases are achieved in 2025.

- If economic activity remains on track, the timing of the adjustments of the policy interest rate should depend on two factors: (1) the pace at which the rate hikes need to progress, calculated backward from the time the goal is expected to be reached; and (2) the assessment of both upside and downside risks to prices observed at the time of each MPM. From this perspective, it is appropriate for the Bank to maintain the current monetary policy at this meeting.

- Although there have been positive signs, accompanied by a decline in the labor share in larger firms and in small and medium-sized firms with relatively large-scale businesses, the improvement in the earning power of many small and medium-sized firms is still not strong. In addition, there are high uncertainties regarding overseas economies, including the European and Chinese economies being slow to recover and developments in U.S. economic policy. As it is necessary to confirm the progress in economic improvement at home and abroad using data, it is appropriate for the Bank to maintain the current monetary policy for the time being.

- Japan's economic activity and prices have been in line with the Bank's outlook as of March 2024. While there remain uncertainties regarding overseas economies, Japan's economy is in a state where the degree of monetary accommodation can be adjusted.

- Underlying inflation has been increasing steadily, while the risk of the Bank falling behind the curve is limited. The Bank will likely decide to raise the policy interest rate in the near future, but at this point it is necessary for the Bank to be patient and monitor the uncertainties over the U.S. economy until those uncertainties subside.

- The Bank is in a phase where it should slightly ease off the accelerator of monetary easing, so that it can slow down when necessary while avoiding harsh braking.

- With economic activity and prices developing in line with the Bank's outlook, risks to prices have become more skewed to the upside. Thus, adjusting the degree of monetary accommodation in a forward-looking, timely, and gradual manner, based on data and anecdotal information, will contribute to the sound development of the national economy through achieving price stability.

- As price increases have continued for three years, the rise in import prices -- mainly reflecting the depreciation of the yen -- will likely lead to a further increase in underlying inflation and thereby to the achievement of the price stability target. Given this, it is necessary for the Bank to adjust the degree of monetary accommodation in a preemptive manner.

- The Bank should show that policy interest rate hikes that are deemed realistic will have a limited impact on its finances, and that therefore its financial soundness will be maintained.

III. Opinions from Government Representatives

Ministry of Finance

- By swiftly and appropriately implementing the policies in the economic policy package and the supplementary budget for fiscal 2024, the government will bring about economic conditions that allow wage increases to consistently outpace inflation, thereby advancing the transition to a "growth-oriented economy driven by wage increases and investment."

- 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 uncertainties such as downside risks to overseas economies.

- The government will swiftly and steadily implement the economic policy package and the supplementary budget so that it can do its utmost to enable a transition away from an economy oriented toward cost cutting to a growth-oriented 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 closely cooperate and exchange views with the government.