

**Basic Policies for Economic and Fiscal Management and Structural Reform 2006  
(Summary)**

**Chapter 1 Current Status of the Japanese Economy and Our Next Objectives**

**1. Embarking on a “Decade of New Challenges”**

**(Bright prospects and the coming of new opportunities)**

The Japanese economy, having come out of the tunnel of long-term stagnation and become lean in form, is finally ready to offer bright prospects for the future. Now, we are about to embark on a “decade of new challenges.”

The first challenge is to seize various opportunities surrounding Japan. Although the Japanese economy tends to be regarded with a negative emphasis on the declining and aging of the population, if we calmly look at the environment surrounding Japan, we can find many new growth potentials.

Examples:

- The core country of Asia as a world’s growth center
- The most advanced energy-saving systems and technology in the world
- The consumer market seeking sophistication and high quality

Mounting the challenge to fully realize this growth potential will be the key to creating a new Japan.

**(Domestic and overseas issues facing Japan)**

However, the environment surrounding Japan not only holds opportunities, but also Japan-specific issues that must be overcome. The second challenge is to bravely overcome these various issues.

Fiscal problems that emerge under the process of the declining and aging of the population create serious inequality between generations. These problems need to be promptly addressed by the current generation which is receiving the benefits, as their responsibility and at their own expense. It is not acceptable for the current generation to leave its own debts to voiceless future generations for repayment.

There are also various issues and risks overseas. After a period in which major countries fully enjoyed the benefits of globalization, the world has entered a period in which countries must watch for the side effects of globalization more closely than ever. Japan needs to actively overcome the issues it faces while fulfilling its own international responsibilities.

### **(Addressing the disequilibrium in Japan)**

Turning our eyes to people's lives in Japan, there are such problems as the risk of wider gaps in educational and employment situations, particularly among younger generations, increased concerns about the future due to the dramatic changes in the employment environment, social unrest caused by heinous crimes committed by students and young people, and gaps between urban and rural areas. We are required to overcome such new disequilibrium as our third challenge.

It is necessary to build a 21st century-style "peaceful and affluent Japanese society" that attains economic growth and maintains a safe and secure society at the same time, while achieving expanded equilibrium.

### **(Firmly maintaining the structural reform path)**

These three new challenges can be met by firmly maintaining and reinforcing the structural reform path that we have been taking. The key to conquering the challenges is to implement intensive and thoroughgoing reform at a speed exceeding the movements in the world.

From now on, with the awareness that we are at a critical stage for passing on an affluent and secure Japan to future generations, it is essential for us to make further reform efforts toward the "decade of new challenges."

These three challenges should not be addressed independently. A robust and dynamic economy is a requisite basis for achieving fiscal consolidation and building a safe, secure, flexible and accommodating society. At the same time, achieving fiscal consolidation will also be one of the biggest growth policies, while a vibrant society backed by safety and security is indispensable for enhancing the growth potential.

Through promoting the reform by considering the economy and finance as one, we need to realize a virtuous cycle of enhancing the growth potential and achieving fiscal consolidation.

## **2. Objectives for the Basic Policies 2006**

The structural reform has apparently produced significant results in terms of macroeconomic performance. Gaps between local economies have been narrowed to some degree with the macroeconomic recovery, but it is necessary to spread the achievements of the structural reform throughout the nation by further driving the self-help efforts of the individual regions.

The foundation for the Japanese economy's new leap forward has been solidified

through promotion of the reform over the past five years. Thus, in the Basic Policies 2006, we indicate efforts to address the three priority issues in the “decade of new challenges” in order to pass on an affluent and secure Japan to future generations based on this foundation.

**(i) Enhancing the growth potential and international competitiveness**

Enhancing the growth potential is the basis of all economic policies. With respect to the issues that the Japanese economy is facing with the advent of the decline and aging of its population, we must overcome it by developing a strategy to leverage productivity improvements, technology innovations, and utilization of Asia’s dynamism.

**(ii) Advancing fiscal consolidation**

With the aim of achieving fiscal consolidation, it is essential to draw up the Integrated Reform of Expenditures and Revenues and to make utmost efforts toward its actualization. In this process, the reform should take a basic stance to rectify the current structure, which would leave the debts to future generations, at the earliest possible stage, and to make citizens feel reassured by establishing sustainable social security systems.

**(iii) Achieving a safe, secure, flexible and accommodating society**

There is growing public concern about the future, and strong public interest in safety and security not only in internal affairs, but also in external relations, while there are also increasing needs for access to diverse options and second-chance opportunities at every life-stage. In light of these circumstances, the Government will achieve a safe, secure, flexible and accommodating society by effectively using the fruits of economic growth.

## **Chapter 2 Efforts to Enhance the Growth Potential and International Competitiveness**

*In the Decade of New Challenges, it is important to achieve an affluent, strong, and attractive Japanese economy, and indicate that there is a bright future waiting beyond the reform by making efforts to enhance the growth potential and international competitiveness. The essential points in making these efforts are to focus on science and technology as well as information technology (IT) innovations, and link them with productivity improvements and economic expansion.*

### **1. Enhancing the growth potential by promoting the Economic Growth Initiative**

#### **(1) Strengthening international competitiveness**

- The Government will strategically implement measures to create new innovation with due consideration to their contribution to economic growth.
- The Government will promote various measures toward making Japan a nation built on tourism, and securely attain the targeted number of foreign tourists to Japan (10 million people) by 2010.
- The Government will conduct further negotiations for economic partnership agreements (EPA) mainly with Asian countries in line with the “EPA Timetable” attached to the “Strategy in the Globalizing Economy”. As a result, the value of trade with countries having concluded EPAs with Japan is expected to account for 25% or more of Japan’s total trade value by the year 2010.
- The Government will steadily perform its international pledge to increase its ODA volume by 10 billion U.S. dollars over the next five years. To this end, it will make active use of yen loans. In addition, it will set comprehensive cost reduction targets for ODA. A timetable for cost reduction will be drawn up for this purpose.
- On the basis of the “New National Energy Strategy”, the Government will strategically develop natural resources and energy policies.

#### **(2) Improving productivity (Innovation in the IT and service industries)**

- Aiming at bringing the percentage of businesses using IT for optimizing their business management to the world’s top class within the next five years, industry-academia-government collaborations will be made to implement an IT productivity improvement campaign and develop IT-related human resources.
- The Government will implement a service industry productivity improvement campaign.

With an objective of expanding the market size of the six priority areas of services to 70 trillion yen by 2015, the Government will take intensive measures to realize high-quality and efficient services including increased emphasis on the establishment of comprehensive local healthcare service frameworks.

**(3) Revitalizing local economies and small and medium-sized enterprises (SMEs) (community revitalization strategy)**

- The Government will advance the development of new technology using local resources, tourism promotion through the creation of industrial tourist attractions, ecotourism, utilizing culture, art and sports, promotion of community businesses, and local consumption of local products.
- Capitalizing on the wisdom and motivation of local SMEs, the Government will promote SMEs' development of new products and services that use local resources.
- The Government will enhance the growth potential of cities through the creation of favorable urban space, such as increasing parks and other greenery, and expansion of the real estate investment market. It will also promote independent and creative urban renaissance projects nationwide, implemented by various parties.

**(4) Creating new demand through resolute implementation of the reform**

In addition to creating demand through innovations, the Government will create new demands through reform efforts including the opening up of public services to the private sector and relevant regulatory reforms.

**(5) Establishing Institutional infrastructures to improve productivity**

**> Human resources**

- The Government will improve the quality of education by revising the Courses of Study and conducting nationwide academic ability surveys, and it will aim at attaining the world's top level scores in international academic ability surveys by 2010.
- The Government will improve the foreign student system, and promote the interchange of young people between Japan and elsewhere in Asia as well as other countries. It will also consider increasing the acceptance of talented experts including in areas that are currently not publicly regarded as specialized or technical areas, while giving due consideration to the problems involved.

**> Equipment**

- The Government will accelerate the depreciation cycle of production means.

- With respect to social capital that contributes to strengthening international competitiveness, the Government will develop those that are truly necessary for the next generation in an intensive, efficient, and strategic manner, while efficiently and strategically conducting appropriate maintenance and renewal of such social capital.

**> Money**

- The Government will strengthen efforts including the development of domestic financial bases so that Japan will become the core of Asia's money flow.

**> Technology**

- The Government will strengthen intellectual property protection further, for example with steps to realize the world's fastest patent examination system and the "Treaty on the Non-proliferation of Counterfeit and Pirated Goods (provisional title)."

**> Knowledge**

- The Government will establish the institutional bases for organizational restructuring such as triangular mergers, trust systems, and fair rules for mergers and acquisitions.

**2. Reforming systems and rules to enhance the strengths of the private sector**

Through measures including regulatory reforms, the Government will fully draw out the vigor of the private sector, as well as establish fair and transparent markets to maintain and increase market vitality.

**(1) Conducting regulatory reforms**

- While following up on the achievements of regulatory reforms to date, the Government will strengthen coordination between the promoting organizations concerned. It will also consider a promotion system for overall regulatory reforms and compile a definitive plan by the end of FY2006.

**(2) Maintaining and improving market vitality and confidence**

- From the viewpoint of enhancing market discipline, such as ensuring appropriate information disclosure and improving the market surveillance function, the Government will smoothly implement the quarterly reporting system, and promote international convergence of accounting standards, based on the international movement to achieve mutual recognition of accounting standards by 2009.

### **(3) Reforms of systems supporting the public sector**

- With respect to the injunctions sought by consumer associations, the Government will consider the introduction of such a system in the Act Concerning Prohibition of Private Monopolization and Maintenance of Fair Trade and the Act Against Unjustifiable Premiums Misleading Representations while giving consideration to the state of implementation of the amended Consumer Contract Act starting in the middle of 2007, and draw a tentative conclusion by 2007.

- While determining what the future will be for nonprofit organization (NPO) activities that can respond in detail to the diversifying social needs and issues, the Government will steadily make efforts to encourage NPO activities in various fields. Regarding specified NPOs incorporated under the Law to Promote Specified Nonprofit Activities, the Government will consider reviewing the system while also referring to the reform of the public-interest corporation system, and draw a conclusion around the summer of 2007.

## **Chapter 3 Advancing Fiscal Consolidation**

### **1. Integrated Reform of Expenditures and Revenues**

#### **(1) Basic approach to the Integrated Reform of Expenditures and Revenues**

##### **(i) Fulfilling accountability to the public**

- The Government must fulfill its accountability to the public by simply indicating the overall picture of the expenditure reform and the revenue reform from an integrated and medium to long-term perspective.

##### **(ii) Maintaining and strengthening the Koizumi Cabinet's efforts to advance fiscal consolidation**

- Based on the idea of *no growth without reform* and the reform achievements to date, the Government will continue to make efforts to advance fiscal consolidation under the concept of the integrated reform on the economy and public finance.

##### **(iii) Enhancing the growth potential and advancing fiscal consolidation at the same time**

- The Government must consistently and continuously conduct well-balanced economic and fiscal management that regards enhancing the growth potential and advancing fiscal consolidation as being both inseparable and necessary.

##### **(iv) Giving consideration to the macroeconomy and responding flexibly**

- The Government will flexibly respond in the event that the economy indicates a considerable slowdown, such as decelerating the pace of the efforts for advancing fiscal consolidation.

##### **(v) Placing emphasis on prudence**

- In order to gain the confidence of the public and market, the Government will rely on a "prudent economic assumption," with a nominal growth rate of approximately 3%.

## **(2) Roadmap and targets for advancing fiscal consolidation**

### **Phase II (FY2007 to early 2010s)**

- The Government will make the same extent of efforts for advancing fiscal consolidation as in Phase I (Advancing of fiscal consolidation by the Koizumi Cabinet from FY2001 to FY2006), and achieve a surplus in the primary balance of the central and local governments combined by FY2011.
- With the aim to restore the primary balance of the financially-pressed central government as much as possible, the Government will promote financial reconstruction while securing a central and local balance.
- The local governments will maintain a surplus trend by reducing their expenditure while keeping the reduction pace with that of the central government and, in terms of revenue, securing the total amount of general revenues required.

### **Phase III (early 2010s to mid-2010s)**

- Even after achieving a surplus in the primary balance, the central and local governments will continue their efforts to improve the primary balance, and secure a certain amount of surplus. In doing so, while maintaining steady economic growth, they will ensure the prevention of a divergence in the ratio of debts of the central and local governments to GDP, and stable reduction of the ratio.
- With respect to the central government alone, as well, the Government will aim to prevent a divergence in the ratio of debts of the central government to the GDP and reduce the ratio in a stable manner.

## **(3) Reform principles and the direction of efforts**

**Principle 1** Minimize the increase of burden on citizens by thoroughly streamlining the Government

**Principle 2** Enhance the growth potential and make use of the results for improving citizens' lives and advancing fiscal consolidation

**Principle 3** Clarify the priorities and reduce expenditures without exception

**Principle 4** Make cooperation between the central and local governments to conduct financial reconstruction while securing a central and local balance

**Principle 5** Establish social security systems that do not leave the debts to future generations

**Principle 6** Take bold steps to reduce the government assets and downsize its balance sheet

**Principle 7** Use the revenue from any new burdens on citizens for the benefit of citizens themselves instead of using it to expand the public sector

#### **(4) Toward attaining the Phase II targets**

##### **(i) Approach to advancing fiscal consolidation**

- Under a prudent assumption with a nominal economic growth rate of approximately 3%, the required amount for achieving a surplus in the primary balance of the central and local governments combined in FY2011 (the required amount of expenditure reduction or revenue increase) will be approximately 16.5 trillion yen.
- It is important that the Government securely implements the measures necessary for attaining the targets while bearing in mind the five-year reform process.
- The portion that is still short of the required amount after conducting expenditure reduction (approximately 11.4 to 14.3 trillion yen) will be supplemented by the increased revenue realized through revenue reform.

##### **(ii) Expenditure reform**

- Insufficient expenditure reduction will increase the burden on citizens. The Government will minimize the increase of burden on citizens by conducting a zero-based review of the expenditure without sanctuaries.
- The Government will conduct expenditure reform with emphasis on the appropriate areas, even encompassing institutional reform.
- In order to make realistic response for achieving a surplus in the primary balance, the Government will conduct necessary verifications and reviews on the details of the expenditure reform every fiscal year until FY2011.

#### **(5) Revenue reform**

- The gap between the required amount of achieving a surplus in the primary balance (approximately 16.5 trillion yen) and the amount of expenditure reduction will be supplemented mainly through tax reform.
- The main basic issues or policy issues that the Japanese tax system needs to address in the medium to long-term are as follows:
  - (i) Securing stable financial resources for the expected remarkable increase in social security benefits;
  - (ii) Enhancing the international competitiveness of the Japanese economy and contributing to economic revitalization;
  - (iii) Addressing the rapid fall of birthrate and enhancing child-raising support measures;

and

(iv) Increasing local tax sources in order to further promote decentralization.

In order to deal with these needs, the Government needs to implement fundamental and integrated reform throughout the entire tax system.

- The Government must secure the required revenue on a net basis. In particular, with regard to designating the consumption tax more clearly as a stable source for social security benefits, the Government will take into account the link between the benefits and the revenue sources.

- The reformed tax system must be constitutionally capable of attaining the medium- to long-term target(respective stable reduction in the ratio of debts to GDP of the central and local governments)in a structurally sustainable manner.

- While the overall tax reform should be implemented as early as possible in principle, the Government should select the best timing for implementation of the respective reforms by precisely determining the economic and social trends, the transition in tax revenue, and the progress status of the expenditure reform.

- With respect to tax reform, the Basic Policies 2005 sets forth that the Government will aim to draw a conclusion around the end of the concentrated consolidation period (FY2005 and FY2006), and the Outline of Tax Reform of the Ruling Parties specifies that the Government will aim to fundamentally reform the tax system including consumption tax around FY2007. Therefore, the Government will devote itself to tax reform in accordance with these ideas.

## **(6) Integrated Reform of Expenditures and Revenues in Phase III**

### **(i) Basic reform policy**

- Toward attaining the Phase III targets, the Government must engage consistently in the Integrated Reform of Expenditures and Revenues, while maintaining the continuity from Phase II. Additionally, the Government will aim to secure stable financial resources for social security, and grow out of the structure of leaving its debts to future generations.

### **(ii) Medium to long-term *options***

- Combinations of expenditure reform and revenue reform that take into account a certain amount of the combined as well as the respective primary surplus of the central and local governments will serve as the medium to long-term *options* for the Integrated Reform of Expenditures and Revenues toward attaining the Phase III targets.

- These *options* will first be considered by paying attention to the ratio of government

expenditure to GDP. It is also necessary to make verifications from the viewpoint of securing stable financial resources for social security.

- With respect to the scale of expenditure, various options will be considered based on the maximum efforts for expenditure reduction in Phase II and national awareness about the level of administrative services provided.

- In terms of revenue, efforts must be made to improve the balance so that, together with the expenditure reduction efforts, the target (respective stable reduction in the ratio of debts to GDP of the central and local governments) can be achieved.

#### **(7)Future efforts**

The Government will promote concretization of the Integrated Reform of Expenditures and Revenues in accordance with the policy above.

### **2. Efforts for achieving a *lean and efficient government***

#### **(Secure implementation of postal privatization)**

- The Government will smoothly and securely implement postal privatization starting in October 2007.

#### **(Promotion of policy-based finance reform and review of incorporated administrative agencies)**

- The Government will steadily promote policy-based finance reform toward the complete shift to the new system in FY2008. The Government will also review the overall operations and organization of incorporated administrative agencies.

#### **(Increase of municipalities that require no local allocation tax)**

- The Government will aim at increasing the number of municipalities that do not need to depend on local allocation tax, by setting a specific target, such as half of the cities with a population of 200,000 or more.

#### **(Reform of government assets and debts)**

- Based on the Law on Administrative Reform Promotion, the Government will reduce its assets by approximately 140 trillion yen with the aim to halve the ratio of government assets to the GDP by the end of FY2015.

- With respect to national property, approximately 12 trillion yen of proceeds are anticipated from selling the property over the next ten years. Furthermore, the

Government will promote effective use of the property (including running the facility around the clock) using the know-how of the private sector.

- Additionally, the Government will reduce the loans of the Fiscal Loan Fund by over 130 trillion yen within the next ten years.
- The Government will also move the existing assets off the balance sheet by selling or securitizing them by hearing the opinions of private experts, if the merit exceeds the cost.

**(Promotion of special accounts reform)**

- In accordance with the Law on Administrative Reform Promotion, the Government will aim to promote the special accounts reform in a planned manner within about five years starting in FY2006.
- The Government will promptly consider earmarked revenue sources for road improvement on the premise of incorporating them into general revenue, and draft a concrete proposal by the end of 2006 while gaining the understanding of taxpayers.

**(Reform of statistic system)**

- The Government will establish an organization that acts as a core *control tower* for developing and coordinating statistics on a government-wide basis in the Cabinet Office. The Government will present a bill for drastically reforming the statistics law system to the next ordinary session of the Diet, and promote statistics development based on the Basic Policies 2005.

## **Chapter 4 Achieving a safe, secure, flexible and accommodating society**

*By effectively using the fruits of economic growth, the Government will achieve a 21st century style “peaceful and affluent Japanese society” while achieving expanded equilibrium.*

### **1. Comprehensive reform of social security systems**

#### **(Integrated review of social security)**

- In order to build social security systems that are sustainable in the long-term, it is necessary to review both the social security benefits and the burdens, and to balance the systems with the economy and finance. The Government will promote integrated review of the overall social security systems while giving consideration to role sharing among self-help, mutual help, and public help, as well as between tax and premiums, and impartiality between generations and that within the same generation.

- With regard to social security benefits, the Government will continue to make reform efforts from a medium to long-term perspective, while verifying the effects of institutional reforms to date, and make constant reviews so that they will be kept within a scope bearable by citizens. Additionally, the Government will secure stable financial resources for social security in order to stop leaving its debts to future generations.

#### **(Medical care)**

- The Government will drive improvements in the quality and efficiency of medical services, including the following: standardization of medical services, promotion of comprehensive ICT introduction such as complete digitization and online transmission of medical fee bills, development of new medical fee systems such as increased use of fixed-amount payment according to patient characteristics, strengthening of insurer functions, and study on what appropriate end-of-life care should be.

#### **(Pension)**

- The Government will raise its share contributions to the basic pension scheme to one-half by FY2009, after conducting the necessary drastic tax reform for securing stable financial resources.

#### **(Nursing care and others)**

- The Government will promote prevention of the need for nursing care from the viewpoint of smoothly implementing reform of the nursing care insurance system.

## **2. Supporting opportunities for second-chance**

In order to achieve a fair society in which individual citizens can fully demonstrate their abilities and characteristics, and are deservedly rewarded for their efforts, the Government will build a mechanism that provides access to diverse options at the respective stages of people's lives and that allows for social mobility, making the gap between *winners and losers* flexible.

### **(1) Building a flexible and diverse social system compatible with double-track life**

- The Government will promote review of the system to recruit new graduates all at once.
- The Government will aim at securing equal treatment for regular and part-time workers.
- The Government will promote efforts that will allow working people to restudy.

### **(2) Supporting people so that they can have a second-chance in ways that meet individual circumstances**

- The Government will support people who failed in business and those who retired as a result of corporate restructuring.
- The Government as a whole will support people with disabilities and those who are ill.
- The Government will support young people (e.g. "freeters" aged between 25 and 34), women and the aged, etc who mount new challenges.

## **3. Promoting comprehensive measures against the falling birthrate**

In order to reverse the declining trend of birthrate, the Government will raise again the question of what social awareness lies behind the falling birthrate, and encourage people to reaffirm the importance of passing on life to the next generation, and nurturing life as well as the importance of family. Also, it will comprehensively address the causes of anxiety for young generations. It is necessary to drastically increase, strengthen, and change the measures against the falling birthrate.

- (1) The Government will promote implementing measures to support child raising according to the child's growth stages from the mother's pregnancy/delivery to the upper secondary school/university student stage, as well as reforming the ways of working.
- (2) In order to reform the awareness of society, the Government will promote national campaigns for restoring the bonds of family and community.

#### **4. Coping with the risks in daily life**

Ensuring national safety and security is one of the most important responsibilities of the Government. In addition, this serves as one basis for revitalization of the Japanese economy. Now that our country has entered a new economic era, it is necessary for both the public and private sectors to make efforts to establish appropriate role-sharing and cooperative relationships with each other in order to cope with the various risks in daily life.

- Disaster control measures (prevention measures for natural disasters such as large-scale earthquakes, large-scale floods and sediment-related disasters, tsunamis and storm surges and heavy snowfall; these include the creation of hazard maps and the development of framework for swiftly communicating disaster prevention-related information)
- Public safety and order measures, measures for crime victims, ensuring safety of the environment surrounding children
- International safety and security efforts, anti-terrorism measures (thorough implementation of information collection/analysis and the watching/guarding of important facilities and public transportation; promotion of measures for the protection of citizens)
- Restoring safety and confidence (preventing the recurrence of falsification of earthquake-resistance data; improving the safety of public transportation; maintaining and improving the food supply capacity)
- Conserving the global environment and establishing a Sound Material-Cycle Society (acceleration of efforts, including reduction of greenhouse gas emissions and measures for forest sinks; development of environmental technology)
- Continental shelf surveys (firm implementation of marine surveys (around Japan))

#### **5. Developing an environment in which citizens can live a well-off life**

- The Government will promote early childhood education by enhancing measures to reduce preschool education-related burdens on parents and guardians in the short term, while, in step with the revenue reform, it will comprehensively consider issues including the financial resources and systems required for making early childhood education free of charge in the future.
- The Government will strengthen the educational functions of school, home, and community, and provide educational support for children with disabilities.
- The Government will develop environments for cultivating familiarization with culture and arts in schools and communities.

- The Government will make effort to achieve a lifelong sports society and improve Japan's ability to compete in international sporting events. Additionally, the Government will engage in measures to secure and increase the opportunities for children to do physical exercises in schools and communities.
- The Government will reinforce measures to promote the vocational independence of young people not in education, employment or training (NEET).

## **Chapter 5 Basic Approach to the FY2007 Budget**

### **1. Prospective economic trend and the approach to economic and fiscal management in the short-term**

- While the world economy will continue to recover steadily, the Japanese economy is expected to see improvements in both the corporate and household sectors in FY2006, and achieve autonomous and sustainable economic growth in FY2007.
- The Government will promote efforts on structural reform in a more full-fledged and comprehensive manner with focus on the expansion of private demand and employment.
- To ensure sustainable economic growth led by private-sector demand under stable price conditions, the Government and the Bank of Japan (BOJ) will make joint efforts. The Government will further accelerate and deepen structural reforms. The BOJ is expected, considering market trends, to exercise effective monetary policy management, which will be consistent with the Government's efforts and economic conditions, so that the BOJ will continue to support the economy responsibly.

### **2. Direction of the FY2007 budget**

The FY2007 budget is an important starting point where the Government will be required to show its attitude toward the new reform in the next five years, as indicated in Chapter 3.

In order to have the budget symbolize that the Government has taken the first step forward with responsibility toward achieving fiscal consolidation, the Government will set strict Baseline Requests that maintain the conventional reform efforts, and review the expenditure with emphasis on the appropriate areas.

- Since the FY2007 budget is an important budget that marks the start of the Phase II reform designed for ensuring the achievement of a surplus in the primary balance, the Government will steadily put into practice the ideas mentioned in Chapter 3.
- Based on the Law on Administrative Reform Promotion, the Government will sort and review its operations, and streamline and improve the efficiency of administration more exhaustively.
- Each ministry and agency will abolish or reduce the amount of budget request for existing measures when requesting a budget for new measures.
- The Government will promote reform for maintaining and improving the quality and reducing the costs of public services by actively using market testing (reform of public services through introduction of competition).

## **Closing Remarks**

Since the foundation of the Council on Economic and Fiscal Policy in 2001, the Government has enhanced the system of deciding economic and fiscal policies and related policies in a manner that achieves compliance and consistency as a whole, rather than in a ministry-specific manner, with the central role played by the Council on Economic and Fiscal Policy chaired by the Prime Minister.

With regard to the management of economic and fiscal policies, the process of policy decisions for the reform has become established. First, the direction of reform is clarified in the Basic Policies (Big-boned Policies) that exhaustively cover important issues. Then, the Council on Economic and Fiscal Policy draws up the Overall Picture of the Budget and creates the Guidelines for Formulation of the Budget. Through this process, a direction is given to the budget for the following fiscal year with clear specification of the priorities.

At the same time, the Council on Economic and Fiscal Policy formulates the Basic Policies for Economic and Fiscal Policy Management and Structural Reform to conduct a rolling revision. By doing so, the medium-term targets, including achievement of a surplus in the primary balance and a breakaway from deflation, have been clarified, and short-term economic and fiscal policies have been operated in compliance with these targets.

In the future, it is necessary to further strengthen the reform efforts while maintaining these achievements.

Specifically, the Government will formulate, as early as possible, new basic policies on medium-term economic and fiscal management, which combine the Integrated Reform of Expenditures and Revenues and the economic growth strategy, and which incorporate the overall macroeconomic trend. In addition, the Government will maintain and strengthen the policy deciding process of the Basic Policies, the Overall Picture of the Budget, and the Guidelines for Formulation of the Budget. In this process, it is necessary to further increase the compliance between economic management and fiscal management by, for instance, checking the economic trend outlook at mid-year, and to increase the compliance between expenditure and revenue, such as discussing expenditure reform and tax reform as one. In addition, the Government will further strengthen coordination with organizations that are deeply related to the reform promoted by the Council on Economic and Fiscal Policy.