

**Outline of the Basic Policies
for the Economic and Fiscal Management and Reform 2014**

Chapter 1: Achievements to date of Abenomics and challenges facing the Japanese economy

1. Ending deflation and revitalizing the Japanese economy

- The Japanese economy has been showing signs of robustness, such as positive growth for six consecutive quarters chiefly driven by implementing the "three-arrows" strategy in an integrated manner.
- The government will continue to support the sustained demand growth as part of its efforts to ensure an exit from deflation. The closing gap between supply and demand is providing a valuable opportunity to promote such challenges as creating new jobs, increasing investments, and expanding business frontiers. Seizing this opportunity, the government will push further ahead with its growth strategy.
- The challenges ahead include (i) coping adequately with a consumption fall after a last-minute rise in demand before a consumption tax increase, (ii) strengthening and deepening the growth strategy to further expand the economic virtuous cycle, thereby achieving economic growth driven by private demand, (iii) implementing institutional and system reforms toward a promising future for Japan, and (iv) achieving fiscal consolidation that is compatible with economic revitalization.
- Government, Labor and Corporate Management will work in collaboration to follow up on the outcomes of last year's agreement and to discuss desirable improvement for employment, wages and related systems.

2. Charting a basic direction toward progress in economic revitalization

- The key to progress in economic revitalization is to boost value-added productivity through improved total factor productivity (TFP) including enhancing both the quantity and quality of labor and capital. From this viewpoint, innovation (including the development of a national system of innovation) and corporate governance are very important. Promoting stable medium- to long-term investment will boost the supply of funds for growth.
- The government will do its utmost to ensure that the fruits of the growth strategy will be enjoyed in every corner of the country.

3. Reconstructing Tohoku from the Great East Japan Earthquake as a land of creativity and potential

The government will accelerate even further the reconstruction process, which is entering a new stage. Given the shrinking and aging population of Japan, the goal is to create a "New Tohoku" as a model for Japan as well as for the world. The central government will take the lead in decommissioning the reactors and cleaning up the tainted water.

4. Reforming institutions and systems that affect the future of Japan

In order to change the momentum around 2020 away from a rapidly declining and extremely

aging population, the government needs to undertake reforms. The government tries to reshape Japan where

- (i) a population of about 100 million is maintained in 50 years with a stable demographic structure;
- (ii) the economy is open to the world, innovations are continually produced, and high value-added goods and services are produced;
- (iii) society, institutions, and systems are in place that empower people to unlock their potential according to their willingness, personalities and capabilities;
- (iv) local communities are in place where jobs are available and sustainable livelihoods are ensured; and
- (v) institutions, culture, and public-spiritedness that constitute the foundations of society are nurtured.

It is essential to maintain the vitality of local communities, stem the tide of over-concentration in Tokyo, and overcome a low birthrate and a shrinking population. The government will set up a headquarters for pushing ahead with an integrated policy designed to achieve these goals.

Chapter 2: Priorities toward progress in economic revitalization and medium-to long-term development

1. Enhancing and exploiting the capacity of human resources, especially empowering women and rebuilding education

(1) Empowering women and reforming gender-based labor practices

The government will pursue a society where women can shine. To this end, the government will work to fundamentally reform labor institutions and practices with regard to gender and work-life balances. It will allow for both men and women to manage their jobs together with childbirth, childcare and aged care according to their willingness and capabilities.

(2) Rebuilding education and promoting sports, cultural and artistic activities

The government will implement comprehensive measures to rebuild education. It will work to achieve world-class academic standards and university reforms. A declining birth rate calls for strong efforts to enhance the quality of education. The government will aim for a national education cursus based on sports, culture and arts.

(3) Empowering young people by offering multiple career development paths

The government will work to ensure that multi-layered and multi-tracked paths to career development are available, so that people who have failed in their career development will have a second chance. It will also work to ensure that non-regular workers will be better treated and given opportunities for education and training. In addition, the government will enhance human resource development so that people will be able to capitalize on their capacity throughout their lives. It will also work to secure and develop human resources where a shortage of workers is of concern.

(4) Stemming the declining birth rate

The government will greatly increase resource allocation for this purpose with solid financial backing. It will also study out-of-the-box solutions, including special assistance to parents who have three or more children.

(5) Capitalizing on a long healthy life expectancy to activate society

The government will take various measures to foster a life-long active society where the elderly can stay healthy longer and where their experiences and capabilities are put to better use. It will also consider how to enable senior citizens who wish to remain in workforce until the age of 70.

2. Reforming Japan's economic structure through innovation and other means to put the economy on a private demand-led growth path

(1) Innovation

The government will work to reform Japan's industrial structure dynamically. Specific measures will include implementing the Comprehensive Strategy on Science, Technology and Innovation 2014, boldly carrying out regulatory and institutional reforms, increasing the supply of medium- to long-term growth funds, and utilizing ICT. We aim to embark on corporate tax reform to be more growth-oriented. To that end, we aim to reduce the percentage level of the effective corporate tax rate down to the twenties in several years. We will start the first phase reduction from the next fiscal year. As regards the revenue sources to fund such rate reduction, including the fact that the Japanese economy is pulling out of deflation and showing structural improvements, in order to be consistent with the FY2020 target to achieve primary surplus, permanent revenues will be secured through such measures as broadening the tax base and so forth. We will continue to discuss this issue towards the end of this year when we will reach conclusions on the specifics.

(2) Corporate governance

It is important that businesses enhance their earning capacity through improved corporate governance and managerial assistance from local financial institutions and pass along an appropriate portion of their profits to various stakeholders. The government will create an environment where sound and robust businesses are nurtured.

(3) An open country

The government will continue to work toward an early conclusion of the TPP (Trans-Pacific Partnership). The Council for Promotion of Foreign Direct Investment to Japan will identify potential investment opportunities and invite foreign investment. Note that utilizing human resources from overseas is not an immigration policy. The government will study ways to utilize such human resources within the framework of the Technical Intern Training Program under review and the National Strategic Special Zones in terms of empowering women.

(4) Natural resources and energy

The government will address rising energy costs and work to secure an affordable and stable supply of natural resources and energy. Respecting the judgment of the Nuclear Regulation Authority, the government will resume operation of nuclear power plants.

(5) Regulatory reforms

The government will closely review existing regulations. Focus will be placed on developing the health and medical industries, allowing for various and flexible working styles, opening up new fields of business, turning agriculture into a growth industry, and promoting inward direct investment in Japan.

3. Building an attractive local community and revitalizing agriculture, forestry and fisheries and SMEs

(1) Creating a “New Tohoku”

The government will seek to realize five visions for a “New Tohoku” (including a community that offers a safe environment where vibrant and healthy children are nurtured). It will help to rebuild a self-reliant and sustainable community. In the process, the government will promote cooperation with a wide range of stakeholders in both the public and private sectors.

(2) Preparing for the Tokyo Olympic and Paralympic Games in 2020

Toward the Tokyo Games, the government will work to make sufficient preparations, taking into account globalization, the revitalization of regions, promotion of tourism, and diffusion of environmental and scientific technology.

(3) Revitalizing both urban and rural areas through tourism and human interaction, promoting decentralization, and supporting integration and revitalizing processes

Focus will be placed on rural revitalization, city regeneration, the development of Okinawa, and decentralization. In addition, the government will conduct a bold review on providing governmental services and policies from a long-term perspective to overcome difficulties due to a rapidly declining and extremely aging population.

(4) Creating vitality for agricultural, forestry and fisheries and the regions

The government will strive to double the average income for farmers and other rural residents over a decade under the Plan to Create Vitality for Agricultural, Forestry and Fishery Industries and Local Communities. It will also work to enhance the competitiveness of the agricultural industry and ensure food security.

(5) Advance in mid-tier enterprises, SMEs, and micro enterprises

Mid-tier enterprises, SMEs, and micro enterprises support the local economy, communities, and employment. The government will assist these enterprises in expanding their business in Japan and abroad, securing human resources, and utilizing local resources. It will also encourage young people and women to start up their own businesses.

4. Securing the foundations for a safe and secure life and a sustainable economy and society

(1) Strategic diplomacy, national security and defense

The government will work to enhance its comprehensive diplomatic capacity for strategic diplomacy. It will also strengthen the strategic civil information activities. Under the NSC, the government will pursue a more strategic and systematic national security policy. In accordance with the National Defense Program Guidelines, the government will efficiently develop comprehensive defense capabilities.

(2) National resilience, disaster prevention and reduction

Under the Basic Plan for National Resilience and its action plan, the government will take focused and efficient actions. It will also take precautionary measures against large-scale natural disasters in preparation for a devastating earthquake such as the Nankai Trough or directly beneath Tokyo.

(3) Safety and security of citizens (public safety, consumer policy, etc.)

The government will take the necessary steps to ensure the safety and security of citizens, including taking measures based on “the strategy for the creation of the world’s safest country, Japan” and for securing the safety and security of consumers.

(4) Contribution to the global environment

The government will address global environmental problems, take measures against global warming, and pursue a recycling-oriented, nature-symbiotic society.

Chapter 3: A virtuous cycle involving economic revitalization and fiscal consolidation

1. Guiding principles in pursuing both economic revitalization and fiscal consolidation

The government will strive to halve the ratio of the primary deficit of the national and local governments to GDP, compared to the FY2010, by FY2015 and achieve a primary surplus by FY2020. Taking into account the compilation of the national budget for FY2015, the government will delineate without delay a prospect that is consistent with these targets. The Council on Economic and Fiscal Policy will review economic and fiscal developments every six months and assess progress in fiscal consolidation. We aim to embark on corporate tax reform to be more growth-oriented. To that end, we aim to reduce the percentage level of the effective corporate tax rate down to the twenties in several years. We will start the first phase reduction from the next fiscal year. As regards the revenue sources to fund such rate reduction, including the fact that the Japanese economy is pulling out of deflation and showing structural improvements, in order to be consistent with the FY2020 target to achieve primary surplus, permanent revenues will be secured through such measures as broadening the tax base and so forth. We will continue to discuss this issue towards the end of this year when we will reach conclusions on the specifics. (Repetition)

2. Principles in prioritizing and streamlining major expenditure items

In prioritizing expenditures and streamlining them for greater efficiency, a review needs to be conducted across discretionary and required expenses, with no exceptions.

(1) Social security reform

The government will streamline and optimize social security benefits with a focus on health and elderly care expenditure. Special emphasis will be placed on (i) optimizing the system for health and elderly care delivery; (ii) strengthening the functions of insurers and promoting disease prevention and health management; (iii) working to revise the remunerations for elderly care and medical treatment; (iv) promoting reforms associated with prescribed medicines and their prices; (v) reexamining the pension system; and (vi) addressing the issue of livelihood protection and assistance for the needy.

(2) Social infrastructure development

By making the most of the private sector vitality through PPP/PFI among others, the government will systematically develop social infrastructure to support such aspects as enhancing Japan's international competitiveness, revitalizing regions, bolstering national resilience, promoting disaster prevention and reduction, and repairing dilapidated facilities. In the process, it will streamline these aspects for greater efficiency. Promoting social infrastructure development by design in a planned way, it will make a shift in focus to the management of social infrastructure.

(3) Local-government administrative and fiscal systems

As economic revitalization progresses, the government will make a shift from crisis response mode to normal mode. At the same time, it will work to make the regions vibrant. The

government will also work to improve the transparency and predictability of local finances.

3. Public sector reforms

(1) Wider use of IT and operational, administrative and civil service reforms

The Government CIO (Chief Information Officer) will lead the way in curbing operational costs as well as streamlining and reorganizing information infrastructure in the central and local governments. The government will hold a Ministerial Council on E-Government and press ahead with the policy by wider use of IT across all ministries. It will also implement administrative and civil service reforms.

(2) Improving the quality of public finances

The Council on Economic and Fiscal Policy will improve its capacity by strengthening its checking and proposing functions based on analyses. It will also make efforts to enhance the effectiveness of PDCA, and to coordinate in drawing up and revising a relevant plan by each ministry. The government will ensure the transparency of public finances, promote public service reforms, restrict the creation of new special funds and the additional financing of existing funds, and reveal the performance of such funds.

Chapter 4: Guiding principles in compiling the national budget for FY2015

1. Principles in economic and fiscal management

(1) The current and future developments of the economy, and principles in economic and fiscal management in the short-term

The government will continue to carefully monitor the recovery process of consumption from its fall due to front loaded demand shift caused by the recent hike in the consumption tax rate. It will also continue to implement the “three-arrows” strategy in an integrated manner. In addition, the government will execute swiftly the supplementary budget for FY2013 and the budget for FY2014. Furthermore, it will take measures conducive to a virtuous economic cycle and private demand-led economic growth.

(2) Measures to be taken in light of medium- to long-term economic and fiscal prospects

- While ensuring an exit from deflation and economic revitalization, the government will do its utmost to achieve the goal of halving the primary deficit in terms of its ratio to GDP in FY2015 in line with the Medium-term Fiscal Plan, as in the budget for FY2014.
- By the end of 2014, the government will decide whether or not to go ahead with the plan to raise the consumption tax to 10% in accordance with the Supplementary Provision of the Comprehensive Tax Reform Act. The Council on Economic and Fiscal Policy will carry out necessary studies to make a comprehensive assessment of the economic situation.

2. Guiding Principles in compiling the national budget for FY2015

In light of this set of basic principles as well as the Revised Japan Revitalization Strategy 2014 and the Medium-term Fiscal Plan, the government will strive to achieve two goals simultaneously: (i) economic revitalization driven by private demand and (ii) fiscal consolidation. In the process, it will meticulously prioritize budget items to compile a highly strategic budget.