

## **Fiscal 2012 Economic Outlook and Basic Stance for Economic and Fiscal Management**

( January 24, 2012  
Cabinet Decision )

### **1. Japanese economy in FY2011**

Severely affected by the Great East Japan Earthquake in March, the Japanese economy got off to a difficult start in FY2011, posting negative growth for the first and second quarter in 2011. The economy then picked up with the supply chain restoring in a short period of time after all-out efforts by both the government and the private sectors toward recovery and reconstruction. After summer, however, the economic recovery slowed due to the appreciation of the yen and deceleration in the world economy stemming from the European sovereign debt crisis.

These circumstances prompted the Government to compile a series of supplementary budgets to support reconstruction efforts and preemptively address downside risks. The economy is expected to be on a recovery track, backed by the policy measures that focus on reconstruction demand.

With regard to prices, the mild deflation is persisting. Consumer prices declined for the third successive year.

Reflecting the negative carry-over effect from FY2010, the real GDP for FY2011 is expected to decrease by around 0.1% despite the pickup in the later periods. The nominal GDP, which more directly reflects people's sentiment toward the economy, is forecast to decrease by around 1.9%.

### **2. Basic Stance for FY2012 Economic and Fiscal Management**

The Government, considering the downside risks stemming from the European sovereign debt crisis and others, will make its best effort to avoid the slowdown of the economy, in addition to working hard for the reconstruction from the Great East Japan Earthquake. The Government will also decisively work to overcome deflation and make an utmost effort to prevent the economy from falling into a vicious cycle between yen appreciation and deflation. To this end, the Government will work together with the Bank of Japan aiming at quickly realizing stable price increase. Concurrently, the Government will work to revitalize the Japanese economy through further developing the “Basic Strategy for Rebirth of Japan<sup>1</sup>” to formulate “Strategy for Rebirth of Japan” by the middle of this year, thereby achieving sustainable economic growth over the medium- to long-term.

The Government will work closely with the Bank of Japan to conduct macroeconomic policy management by respective policy instruments, under the following framework of policy mix.

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<sup>1</sup> Cabinet decision on December 24, 2011.

The close attention should be paid to the economic condition and measures, if necessary, will be taken in a timely and flexible manner.

### **(Fiscal Policy)**

In the short-term, the Government, in addition to promptly realizing reconstruction demand, will preemptively address downside risk of the economy and the risk of hollowing-out of industry stemming from the yen appreciation, by quickly and steadily implementing measures set out in the FY2011 third and fourth supplementary budgets including the “Comprehensive Package Responding to the Yen Appreciation.”<sup>2</sup>

The Government, characterizing the FY2012 budget as “the first-year budget for the Rebirth of Japan,” will give top priority to reconstruction from the Great Earthquake, and move forward to revitalizing Japan’s economy and society through “Priority Items for Revitalizing Japan” and others.

Given the contagion risks of crises in the current international financial markets, the fiscal consolidation is a critical issue to be addressed in tandem with economic growth strategy. To this end, the Government will steadily implement the Comprehensive Reform of Social Security and Tax, and continue to work toward fiscal consolidation with the aim of achieving the goal of “Fiscal Management Strategy”<sup>3</sup>.

### **(Monetary Policy)**

Toward the exit from deflation, the Government expects that the Bank of Japan will conduct appropriate and decisive monetary policy management under further close coordination with the Government.

### **(Foreign Exchange Policy)**

As excessive volatility in the foreign exchange markets has negative impacts on the economic and financial stability, the Government will continue to watch its development and take appropriate measures.

### **(Guard Against Destabilization of International Financial Markets)**

In collaboration with other governments and international organizations, the Government makes efforts to take necessary actions, considering a wide range of measures contributing to secure stability of international financial markets. The Government will work closely with the Bank of Japan, sharing a sense of vigilance against the risk of the destabilization of international financial markets stemming from the European sovereign debt crisis and its impact on the Japanese economy.

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<sup>2</sup> Cabinet decision on October 21, 2011

<sup>3</sup> Cabinet decision on June 22, 2010

### **3. Economic Outlook for FY2012**

In FY2012, the Japanese economy will grow, driven by domestic demand as intensive implementation of full-fledged reconstruction measures is expected to create steady demand and employment.

As for the world economy, major economies are expected to pick up on the assumption that concerted policy efforts by governments in Europe and others will stabilize the international financial and capital markets under the European sovereign debt crisis. This will create an environment favorable to Japan's exports and production.

Accordingly, the Japanese economy is expected to recover moderately.

With regard to prices, the rate of increase in consumer prices is forecast to be approximately 0.1%, owing to such factors as the narrowing GDP gap. The GDP deflator will decline slightly. Reflecting a mild increase in the number of employees, the unemployment rate is set to decrease.

As a consequence, the GDP growth rate in FY2012 is expected to turn positive in both real and nominal terms. The real growth rate is about 2.2%, and the nominal growth rate is about 2.0%.

Downside risks include a further downturn in the overseas economy amid the deepening European sovereign debt crisis, the appreciation of the yen and the subsequent acceleration of hollowing out of industry, and constraints on the electricity supply.

#### **(1) Real Gross Domestic Product**

##### **(i) Private Consumption Expenditure**

Private consumption is expected to maintain its modest uptrend (up by approximately 1.1% from the previous fiscal year) owing to such factors as improvements in employment and income conditions, and the impact of policy measures.

##### **(ii) Private Residential Investment**

Private residential investment should continue to rise (up by approximately 6.3% from the previous fiscal year) thanks to the impact both of improvements in the employment and income conditions, and of policy measures on reconstruction and housing.

##### **(iii) Private Non-Residential Investment**

Private non-residential investment is expected to turn upward (up by approximately 5.1% from the previous fiscal year) despite the appreciation of the yen, owing to increases in corporate earnings and the impact of such policy measures as expanding existing subsidies for locating businesses in Japan.

##### **(iv) Government Expenditure**

Government expenditure will continue to rise above the level of the previous fiscal year (up

by approximately 0.6% from the previous fiscal year) due to increases in social security expenditures and the impact of a series of supplementary budgets for FY2011.

#### **(v) External Demand**

External demand is expected to contribute to the growth positively as the export will increase steadily with the background of a modest turnaround in the world economy, and the imports will increase only moderately (the contribution of external demand to the real GDP growth rate will be approximately 0.4%).

#### **(2) Labor and Employment**

As the continued effects of policy measures to create and support employment is expected the number of employees will continue to rise moderately with a moderate recovery of the economy, (up by approximately 0.8% from the previous fiscal year). The unemployment rate will fall to approximately 4.3%.

#### **(3) Industrial Production**

Industrial production will pick up under the impact of an increase in exports as well as a rise in domestic demand, as a result of full-fledged reconstruction measures (up by approximately 6.1% from the previous fiscal year).

#### **(4) Prices**

The rate of increase in consumer prices will be approximately 0.1%, owing to such factors as the narrowing GDP gap. The domestic corporate goods prices will show a slight increase (up by approximately 0.7% from the previous fiscal year). The GDP deflator will decline slightly (down by approximately 0.2% from the previous fiscal year).

#### **(5) Balance of Payments**

Amid a modest turnaround in the world economy, the trade balance will post a slight surplus, reflecting an increase in exports. The current account surplus will increase moderately. (The current account balance will be approximately 2.5% as a percentage of nominal GDP.)

Note 1: The preparation of these economic forecasts is premised on the economic and fiscal management set out in “2. Basic Stance for FY2012 Economic and Fiscal Management.”

Note 2: The Japanese economy consists mainly of private economic activity, and is influenced by unforeseeable market fluctuations and other changes in the international environment. Accordingly, the above indicators should be recognized as being subject to upside and downside deviations.

(Appendix)

## Main Economic Indicators

	FY2010	FY2011	FY2012	Percentage changes over the previous fiscal year					
	(Actual)	(Estimate)	(Forecast)	FY2010		FY2011		FY2012	
	Trillion yen (Current prices)	Trillion yen (Approx.) (Current prices)	Trillion yen (Approx.) (Current prices)	% (Current prices)	% (Constant prices)	% (Approx.) (Current prices)	% (Approx.) (Constant prices)	% (Approx.) (Current prices)	% (Approx.) (Constant prices)
Gross domestic product	479.2	470.1	479.6	1.1	3.1	-1.9	-0.1	2.0	2.2
Private consumption expenditure	284.2	282.7	285.4	0.0	1.6	-0.5	0.3	1.0	1.1
Private residential investment	13.0	13.5	14.5	2.8	2.3	4.1	2.9	7.3	6.3
Private non-residential investment	62.1	61.0	64.2	2.1	3.5	-1.7	-1.1	5.2	5.1
Increase in private inventory * <sup>1</sup>	-1.5	-2.4	-1.8	(-0.9)	(-1.1)	(0.1)	(0.2)	(0.1)	(0.1)
Government expenditure	117.1	119.8	120.3	0.1	0.5	2.3	2.3	0.4	0.6
Government final consumption expenditure	95.8	97.9	98.3	1.6	2.3	2.2	2.5	0.4	0.8
Public-sector fixed capital formation	21.4	21.9	21.9	-6.1	-6.8	2.0	0.9	0.1	-1.0
Exports of goods and services	73.8	72.5	77.2	14.4	17.2	-1.8	0.0	6.6	6.5
Less: Imports of goods and services	69.5	76.9	80.2	15.5	12.0	10.7	4.6	4.2	3.3
Contribution of domestic demand	/			1.1	2.4	-0.1	0.6	1.7	1.8
Contribution of private demand				1.1	2.3	-0.6	0.0	1.6	1.6
Contribution of public demand				0.0	0.1	-0.0	0.6	0.1	0.2
Contribution of external demand				0.0	0.8	-1.8	-0.7	0.3	0.4
National income	349.3	342.3	349.4	2.0	/	-2.0	/	2.1	/
Compensation of employees	244.3	244.5	246.9	0.5	/	0.1	/	1.0	/
Income from properties	19.8	19.1	19.7	-7.7	/	-3.5	/	2.7	/
Business income	85.2	78.6	82.9	9.2	/	-7.7	/	5.4	/
Labor and employment	Ten thousands	Ten thousands (Approx.)	Ten thousands (Approx.)	%		% (Approx.)		% (Approx.)	
Labor force	6,587	6,538	6,551	-0.3		-0.7		0.2	
Employed persons	6,257	6,243	6,269	-0.1		-0.2		0.4	
Employees	5,469	5,474	5,518	0.2		0.1		0.8	
Unemployment rate	% 5.0	% (Approx.) 4.5	% (Approx.) 4.3	/					
Production	%	% (Approx.)	% (Approx.)	/					
Industrial production	8.9	-1.9	6.1	/					
Prices	%	% (Approx.)	% (Approx.)	/					
Domestic corporate goods price index	0.7	1.9	0.7	/					
Consumer price index	-0.4	-0.2	0.1	/					
GDP deflator	-2.0	-1.8	-0.2	/					
Balance of payments	Trillion yen	Trillion yen (Approx.)	Trillion yen (Approx.)	%		% (Approx.)		% (Approx.)	
Balance of goods and services	5.2	-3.6	-1.7	/					
Trade balance	6.5	-1.6	0.1	/					
Exports	64.5	64.2	69.1	16.0		-0.4		7.6	
Imports	58.0	65.8	69.0	18.4		13.6		4.8	
Current balance	16.1	9.9	12.2	/					
Current balance as a percentage of GDP	% 3.4	% (Approx.) 2.1	% (Approx.) 2.5	/					

\*1 Figures in parentheses represent contribution to GDP growth.

(Note1) The figures for Consumer Price Index are general.

(Note2) The figures for Labor and employment in FY2010 are estimated by Cabinet Office.

(Note3) We have assumed the real growth rate of world GDP (excluding Japan), the yen's exchange rate and the crude oil import price as follows. These assumptions are not projections of the Government.

	FY2010	FY2011	FY2012
Real growth rate of world GDP (excluding Japan) (%)	4.3	3.0	3.1
Exchange rate (yen/dollar)	85.7	78.5	77.5
Crude oil import price (dollar/barrel)	84.4	113.2	113.0

(Remarks)

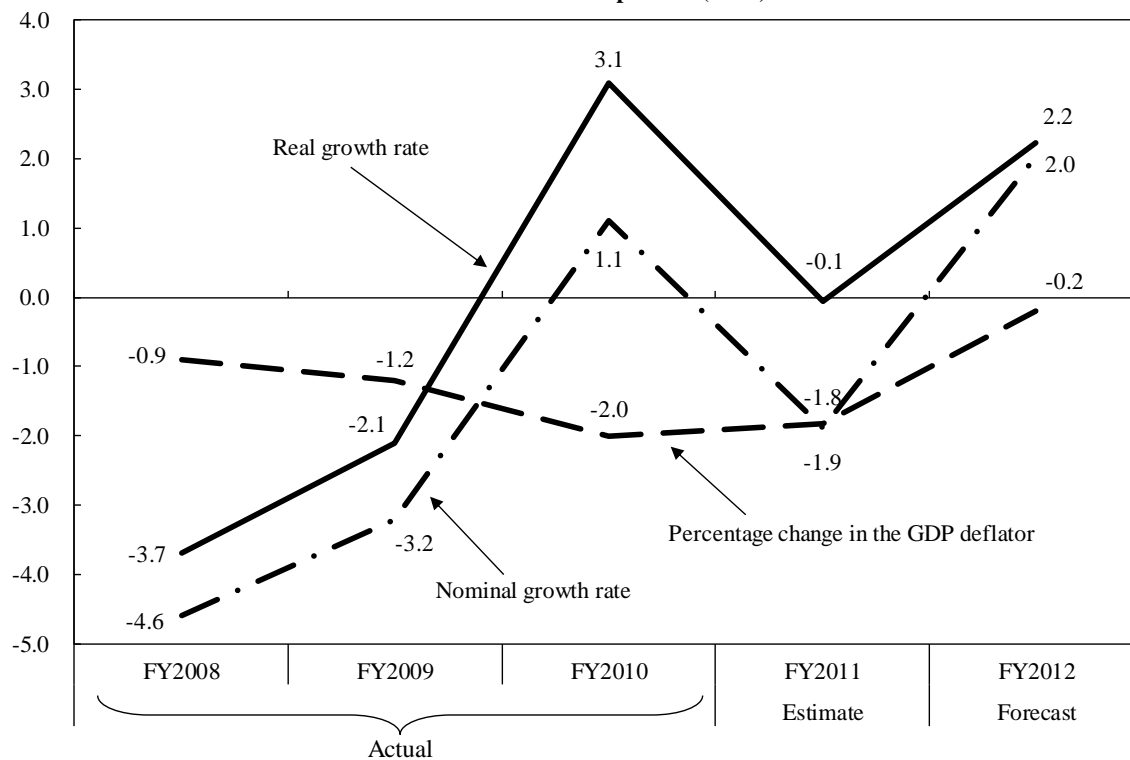
1. The real growth rate of world GDP (excluding Japan) has been calculated based on economic forecasts of international organizations and other institutions.
2. The exchange rate is assumed to stay constant at 77.5 yen/dollar (monthly average from November 1 to 30, 2011) on December 1, 2011 onward.
3. The crude oil import price is assumed to stay constant at 113.0 dollars/barrel (the monthly average spot price of Dubai from November 1 to 30, 2011, plus freight and insurance) on December 1, 2011 onward.

(Reference)

## Main Economic Indicators

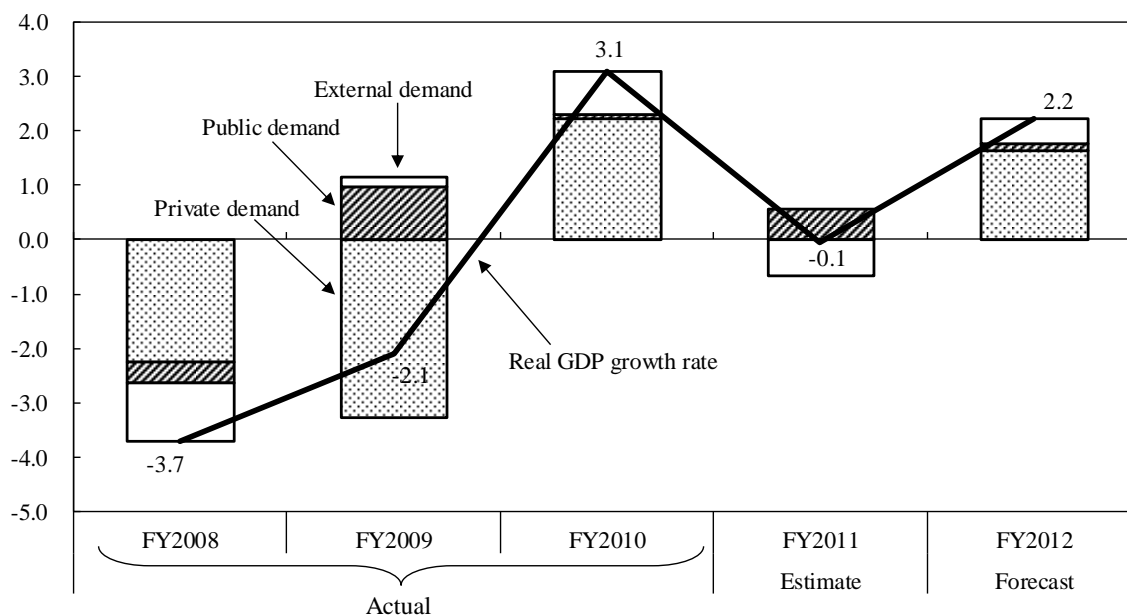
(%, or approximate %)

### 1. Gross domestic product (GDP)



(%, or approximate %)

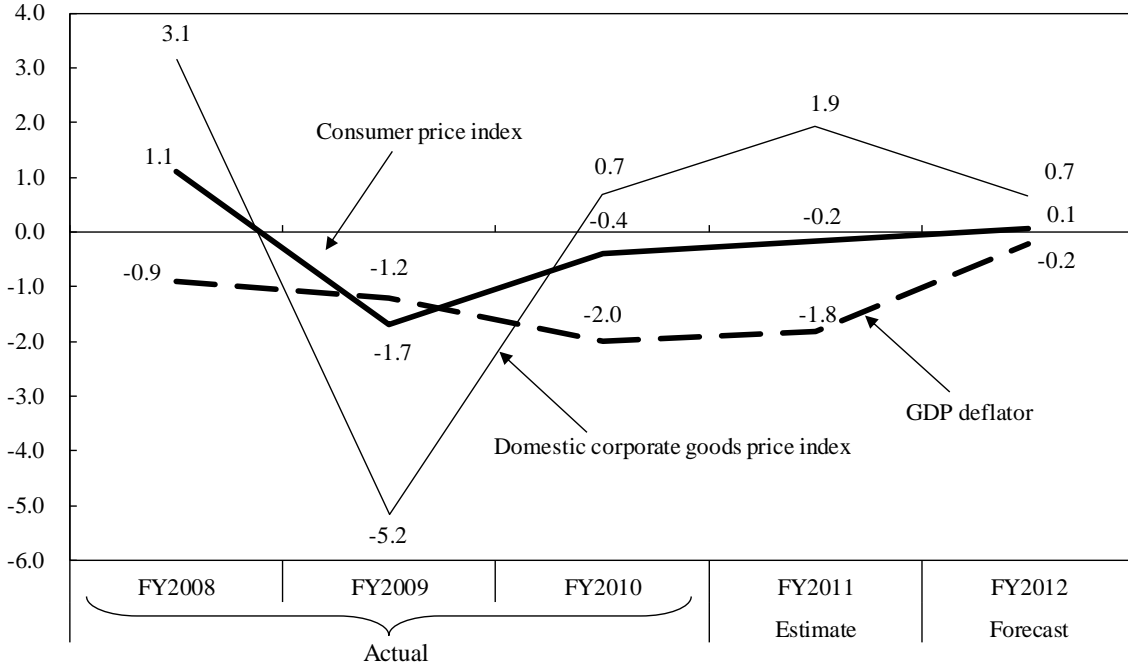
### 2. Real GDP growth rate and contributions to the real GDP growth rate



※Note: Contribution ratios of private demand, public demand, and external demand show their contributions to the real growth rate.

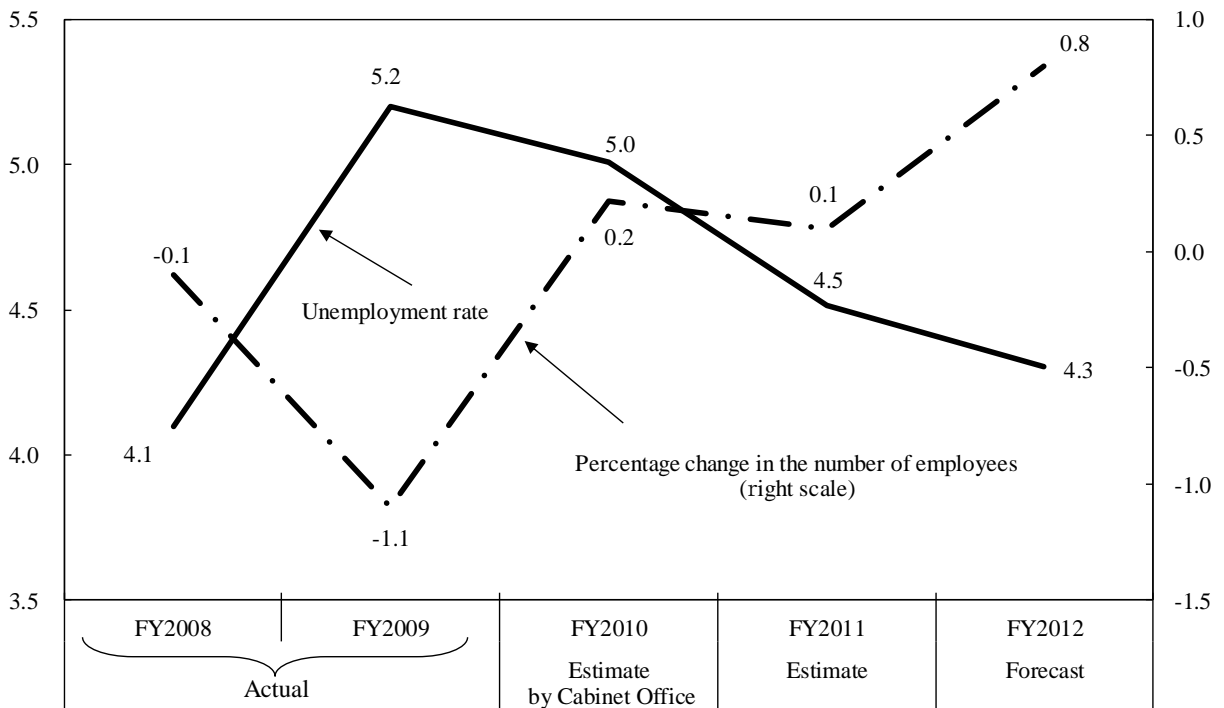
(%, or approximate %)

### 3. Percentage change in price related indices



(%, or approximate %)

### 4. Unemployment rate and the number of employees



※Note: The figures for unemployment rate and the number of employees in FY2010 are estimated by Cabinet Office.