Provisional translation

Fiscal 2014 Economic Outlook and Basic Stance for Economic and Fiscal Management

January 24, 2014
Cabinet Decision

1. Japanese Economy in FY2013

In FY2013, the Japanese economy has been broadly recovering mainly in domestic demand, including private consumption as households' and firms' sentiment improved due to the policy effect of the integrated “three-arrows” strategy that consists of “aggressive monetary policy” “flexible fiscal policy” and “a growth strategy that promotes private investment”.

Business investment is picking up, influenced by the increase in corporate earnings, and the economic recovery is expected to become more solid as employment and income conditions will improve.

In these circumstances, consumer prices (general) are expected to show the first upward trend in five years, by about 0.7%, due in part to the BOJ’s policy effects of “quantitative and qualitative monetary easing.”

Consequently, the real GDP growth rate for FY2013 is projected to be approximately 2.6%, and the nominal growth rate is expected to be about 2.5%.

2. Basic Stance for FY2014 Economic and Fiscal Management

The government will accelerate and strengthen implementations of the “Japan Revitalization Strategy”[1] in order to lead the recent movement toward economic recovery into sustainable economic growth. To enhance the growth potential of the Japanese economy, the government will boldly promote the three action plans incorporated in the above-mentioned strategy by utilizing both the Industrial Competitiveness Enhancement Act and the Act on National Strategic Special Zones in a proactive manner and concentrating the allocation of policy resources in the said action plans.

At the same time, the government, management executives and workers should work together, while playing respective roles, in order to link the

[1] Cabinet decision dated June 14, 2013

expanding corporate earnings to income growth and the expansion in employment and investment. In this way, virtuous cycles for further expansion in corporate earnings will be realized through increases in consumption and investment. Moreover, the government will steadily implement the “Economic Policy Package”[2] including “Economic Measures for Realization of Virtuous Cycles”[3] (hereinafter referred to as “economic measures”), not only to mitigate the rush demand and recoil reduction which is expected to occur with the hike in the consumption tax rate to be implemented in April 2014 and address downside risks for the economy, but also to improve the growing economic strength and realize virtuous cycles leading to sustainable economic growth.

With regard to the combined ratio of primary deficit to GDP of the national and local governments, the government aims to halve the ratio compared to the FY2010 level by FY2015, and achieve a primary surplus by FY2020. To this end, it will strive for improvement based on the “Basic Framework for Fiscal Consolidation: Medium-term Fiscal Plan”[4]. Accordingly, as for the fiscal budget for FY2014, the government will drastically review budget items including social security-related costs and other compulsory costs without allowing any sanctuary and then will prioritize policies and measures that should contribute to economic growth.

Through the above-mentioned efforts, the government aims to realize overcoming deflation, revitalizing the economy, and fiscal consolidation.

The government expects that the Bank of Japan achieves the 2 percent price stability target at the earliest possible time.

3. Economic Outlook for FY2014

In FY2014 the Japanese economy is expected to recover, supported by firm domestic demand continuing from the previous fiscal year and resulting in gradual realization of a virtuous cycle, partly brought about by the implementation of the economic measures shown in the “2. Basic Stance for FY2014 Economic and Fiscal Management”, while we need to pay attention to the rush demand and recoil reduction associated with the planned hike in the consumption tax rate.

[2] “Consumption Tax Rate Hike and Local Consumption Tax Rate Hike, and the Relevant Response Measures” (Cabinet decision dated October 1, 2013)
[3] Cabinet decision dated December 5, 2013
[4] Cabinet approval dated August 8, 2013

With regard to prices, the rate of increase in consumer prices is expected to be about 3.2%[5], higher than the previous fiscal year, while the rate of change in the GDP deflator is anticipated to turn to a positive figure. In this way, steady progress toward overcoming deflation is expected in tandem with continuous improvement in the labor market.

Consequently, the real GDP growth rate for FY2014 is expected to be approximately 1.4%, and the nominal growth rate is projected to be about 3.3%.

Downside risks include the following: developments in financial and capital markets, developments in overseas economies such as Asian emerging nations, and constraints on the electric supply.

(1) Real Gross Domestic Product

(i) Private Consumption Expenditure

A moderate increase (up by approximately 0.4% from the previous fiscal year) will continue due to the improvement in employment and income conditions and effects of economic measures, etc.

(ii) Private Residential Investment

While the growth rate will turn into a negative figure (down by about 3.2% from the previous fiscal year), the level will remain almost the same as that of the previous fiscal year not only because of the improvement in employment and income conditions but also because of reconstruction efforts and housing-related policy effects, etc.

(iii) Private Non-Residential Investment

Non-residential investment will continue to increase (up by approximately 4.4% from the previous fiscal year), owing to increases in exports and production, higher corporate earnings, and policy effects, etc.

(iv) Government Expenditure

Government spending will increase because of steady implementation of economic measures and an increase in social security-related costs, etc. (up by approximately 0.7% from the previous fiscal year).

[5] The figure includes an increase of about 2.1% due to the planned hike in the consumption tax rate.

(v) External Demand

External demand will increase as the world economy recovers moderately. (The contribution of external demand to real GDP growth rate will be about 0.2%).

(2) Labor and Employment

Under the current and anticipated economic recovery, the number of employees will continue to increase (up by approximately 0.5% from the previous fiscal year) partly because of job creation effects of economic measures. The unemployment rate will decline (to approximately 3.7%).

(3) Industrial Production

Industrial production will continue to increase (up by approximately 3.3% from the previous fiscal year), owing to increases in exports and domestic demand, etc.

(4) Prices

The consumer price index (general) will rise by approximately 3.2%. The domestic corporate goods price index is estimated to rise by approximately 3.9%. The rate of increase in GDP deflator is expected to turn positive (up by about 1.9% from the previous fiscal year).

(5) Balance of Payments

The trade deficit is expected to narrow moderately due to an increase in exports on the back of a moderate recovery of the world economy. The current account surplus will increase moderately. (The current account balance will be approximately 0.9% 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 FY2014 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 indicators above should be recognized as being subject to upside and downside deviations.

(Appendix)

Main Economic Indicators

	FY2012	FY2013	FY2014	Percentage changes over the previous fiscal year					
	(Actual)	(Estimate)	(Forecast)	FY2012		FY2013		FY2014	
	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	472.6	484.2	500.4	-0.2	0.7	2.5	2.6	3.3	1.4
Private consumption expenditure	288.1	295.9	304.2	0.6	1.5	2.7	2.5	2.8	0.4
Private residential investment	14.0	15.5	15.4	4.7	5.3	10.1	7.3	-0.4	-3.2
Private non-residential investment	64.6	65.6	68.8	0.5	0.7	1.4	0.4	5.0	4.4
Increase in private inventory *1	-1.9	-3.0	-1.8	(-0.1)	(-0.1)	(-0.2)	(-0.2)	(0.2)	(0.2)
Government expenditure	118.1	123.4	126.7	0.5	1.4	4.5	4.3	2.6	0.7
Government final consumption expenditure	97.1	98.7	101.7	0.5	1.5	1.6	1.7	3.1	1.5
Public-sector fixed capital formation	21.0	24.8	25.0	1.1	1.3	17.9	16.1	0.9	-2.3
Exports of goods and services	70.4	79.4	84.8	-0.7	-1.2	12.7	4.0	6.8	5.4
Less: Imports of goods and services	80.8	92.5	97.7	4.5	3.8	14.5	4.2	5.7	3.5
Contribution of domestic demand				0.6	1.5	3.0	2.7	3.3	1.2
Contribution of private demand				0.5	1.1	1.9	1.6	2.6	1.0
Contribution of public demand				0.1	0.3	1.1	1.1	0.7	0.2
Contribution of external demand				-0.8	-0.8	-0.6	-0.1	-0.0	0.2
National income	351.1	362.9	370.5	0.6		3.4		2.1	
Compensation of employees	246.0	248.6	253.6	0.1		1.1		2.0	
Income from properties	21.5	23.6	24.4	3.8		9.7		3.3	
Business income	83.6	90.7	92.5	1.1		8.5		1.9	
Labor and employment	Ten thousands	Ten thousands (Approx.)	Ten thousands (Approx.)	%		% (Approx.)		% (Approx.)	
Labor force	6,555	6,567	6,567	-0.3		0.2		0.0	
Employed persons	6,275	6,309	6,323	-0.1		0.5		0.2	
Employees	5,511	5,563	5,592	0.2		0.9		0.5	
Unemployment rate	% 4.3	% (Approx.) 3.9	% (Approx.) 3.7						
Production	%	% (Approx.)	% (Approx.)						
Industrial production	-2.9	2.4	3.3						
Prices	%	% (Approx.)	% (Approx.)						
Domestic corporate goods price index	-1.1	1.9	3.9						
Consumer price index	-0.3	0.7	3.2						
GDP deflator	-0.9	-0.1	1.9						
Balance of payments	Trillion yen	Trillion yen (Approx.)	Trillion yen (Approx.)	%		% (Approx.)		% (Approx.)	
Balance of goods and services	-9.4	-11.6	-11.5						
Trade balance	-6.9	-10.1	-10.0						
Exports	61.6	68.7	73.6	-1.7		11.6		7.2	
Imports	68.5	78.8	83.6	3.6		15.1		6.1	
Current balance	4.4	4.2	4.7						
Current balance as a percentage of GDP	% 0.9	% (Approx.) 0.9	% (Approx.) 0.9						

*1 Figures in parentheses represent contribution to GDP growth.

(Note 1) The figures for Consumer Price Index are general.

(Note 2) Excluding the effects of the consumption tax hike to be estimated mechanically, consumer price index (general) is expected to be about 1.2% and GDP deflator is expected to be about 0.7%.

(Note 3) The figures for “Labor and employment” in FY2012 represent a year-on-year rate of change using national figures, including supplemental estimates concerning Iwate, Miyagi and Fukushima prefectures.

(Note 4) We have assumed the real growth rate of the world GDP (excluding Japan), the yen's exchange rate, and the crude oil import price as below. These assumptions are neither projections nor outlook of the government but are solely for the sake of this preparation work.

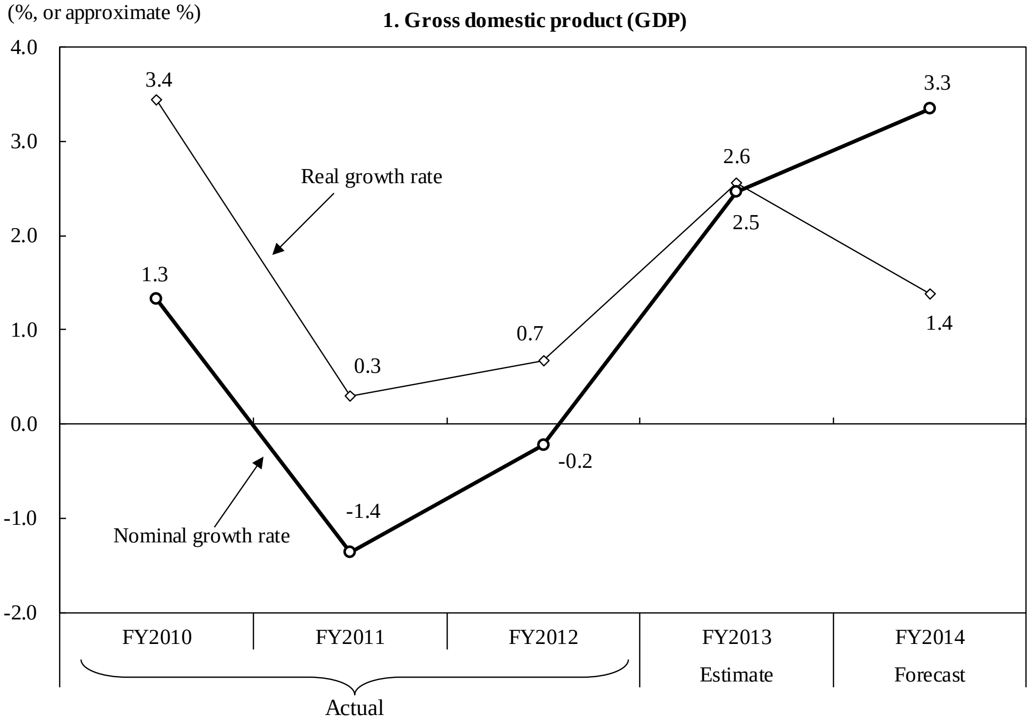
	FY2012	FY2013	FY2014
Real growth rate of world GDP (excluding Japan) (%)	2.8	2.6	3.3
Exchange rate (yen/dollar)	83.1	99.2	100.0
Crude oil import price (dollar/barrel)	113.4	109.0	110.1

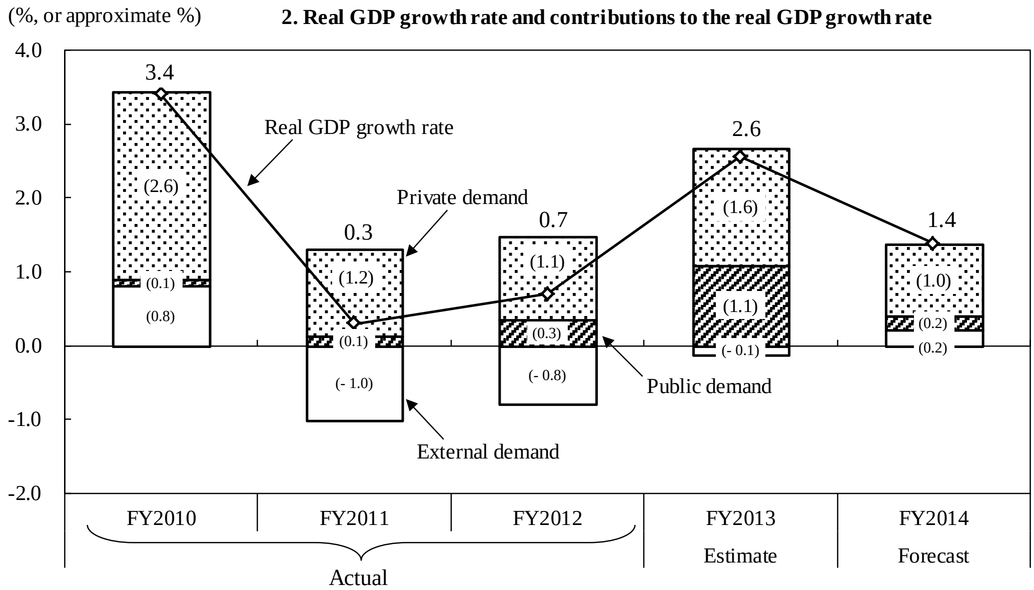
(Remarks)

1. The real growth rate of the 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 100.0 yen/dollar (average from November 1 to 29, 2013) on December 2, 2013 onward.
3. The crude oil import price (the average spot price of Dubai, plus freight and insurance) is assumed to stay constant at 110.1 dollars/barrel on December 1, 2013 onward. The spot price of Dubai is assumed to stay constant on December 2, 2013 onward at the average price from November 1, 2013 to November 29, 2013.

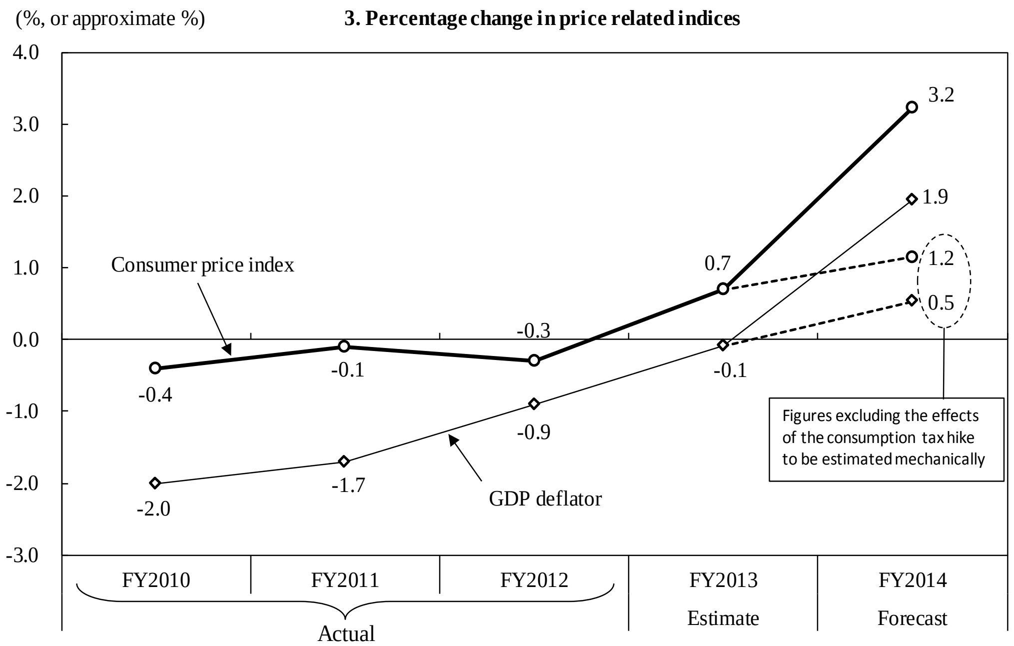
(Reference)

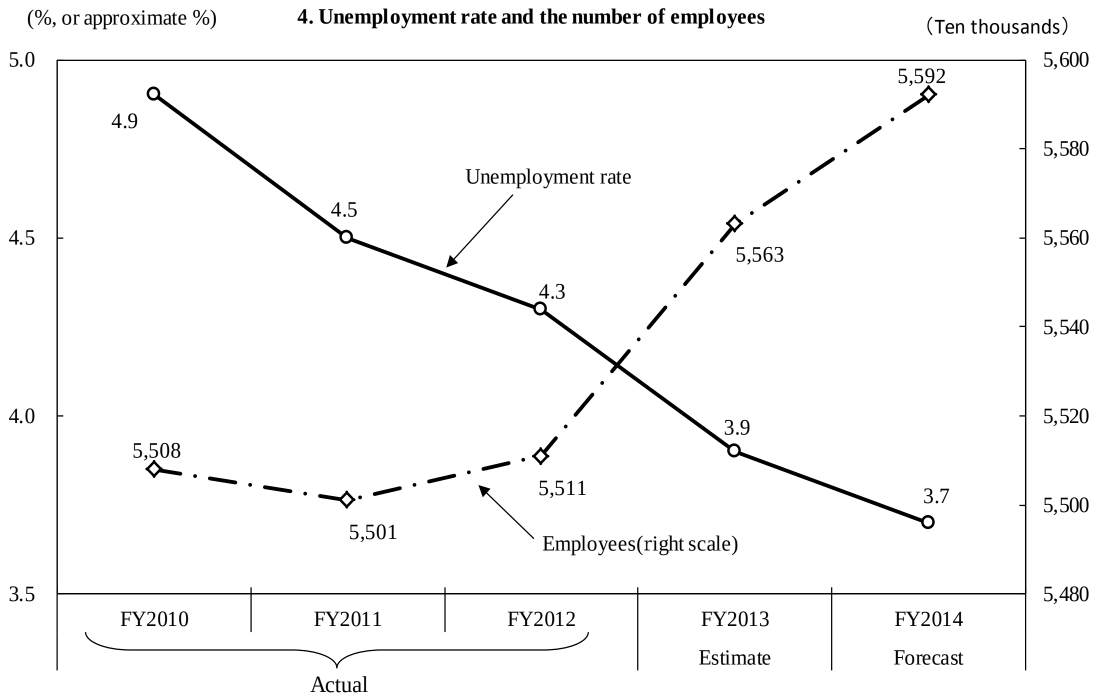
Main Economic Indicators





※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
4.0
3.0
2.0
1.0
0.0
-1.0
-2.0
-3.0
Consumer price index
GDP deflator
3.2
1.9
1.2
0.5
0.7
-0.3
-0.4
-0.1
-0.1
-0.9
-1.7
-2.0
Figures excluding the effects of the consumption tax hike to be estimated mechanically
FY2010
FY2011
FY2012
FY2013
FY2014
Actual
Estimate
Forecast


(%, or approximate %)
4. Unemployment rate and the number of employees
（Ten thousands）
5.0
4.5
4.0
3.5
5,600
5,580
5,560
5,540
5,520
5,500
5,480
Unemployment rate
Employees(right scale)
4.9
4.5
4.3
3.9
3.7
5,508
5,501
5,511
5,563
5,592
FY2010
FY2011
FY2012
FY2013
FY2014
Actual
Estimate
Forecast