

Outline of “Basic Policy on Economic and Fiscal Management and Reform 2015”

~Without economic revitalization, there can be no fiscal consolidation~

Chapter 1: Current situation, challenges and basic policies for the Japanese economy

1. Current situation and challenges of the Japanese economy

(1) Current economic and fiscal situation

Through the advancement of the “three arrows strategy” in an integrated manner, the Japanese economy is reaching a favorable condition on both the micro and macro fronts for the first time in nearly a quarter of a century. As a result, both “overcoming deflation and revitalizing the economy” and “fiscal consolidation” have made major progress.

(2) Challenges

- (i) Extending the virtuous economic cycle, (ii) realizing potential growth, and (iii) vitalizing local economies will be required in order to overcome deflation and achieve sustainable growth over the medium to long term. In addition, the government is required to undertake reforms in order to eliminate inefficient expenditures and improve the quality of public services.
- Since the fiscal situation is still severe in Japan, with public debt amounting to roughly twice GDP and still growing, achieving both economic revitalization and fiscal consolidation is an important challenge. In order to address this challenge, a concrete plan has been formulated this time (Chapter 3 of this Basic Policy).

2. Advancing to the next stage of reconstruction after the Great East Japan Earthquake

- As reconstruction advances to the next stage, the government seeks to complete reconstruction work as soon as possible within the ten-year reconstruction period, especially in the areas hit by both the earthquake and tsunami.
- In line with the progress of reconstruction, the government will constantly review reconstruction work and budgeting according to stage of procedure in order to make these truly useful in disaster areas.
- The government will move forward with measures for reactor decommissioning, dispose of contaminated water, develop intermediate storage facilities, and transport removed soil.

Chapter 2: Priorities for extending virtuous economic cycle and achieving medium- to long-term growth

1. Boosting Japan's potential and making reforms for the future

(1) Improving the business environment and creating growth markets toward strengthening earning power

The government will promote the sophistication of the economic structure and the achievement of higher value-added, continue improving the terms of trade, boost productivity in the service sector, address the needs of micro-, small- and medium-sized enterprises, and ensure smooth funding to strengthen sectors making productivity improvements. In addition, it will advance regulatory reform and attract direct investment into Japan, secure a stable and inexpensive supply of resources and energy, turn the agriculture, forestry, and fisheries industry into a growth industry, promote tourism, and reform ways of taking leave, etc.

(2) Strengthening coordination with growing global markets

While continuing to work toward an early conclusion of the Trans-Pacific Partnership (TPP) in a way that maximizes Japan's national interests, the government will move forward with other economic partnership negotiations, including the Japan-EU Economic Partnership Agreement (EPA), the Regional Comprehensive Economic Partnership (RCEP) in East Asia, and the Free Trade Agreement (FTA) among Japan, China and the Republic of Korea. The government will also promote the entry of Japanese companies into global markets.

(3) Realizing a national system for innovation and reforming the industrial structure with IT and robotics

To become “the most innovation friendly country in the world,” Japan will build a national system of innovation that induces a virtuous cycle involving human resources, knowledge, and funding from businesses, universities, and research institutes. It will also advance reforms in the industrial structure using IT and robotics, as well as the integration of ICT in healthcare and other fields.

2. Exert power of diverse human resources, especially empowering women and reforming education

(1) Exert power of diverse human resources such as women and young people

The government will accelerate its efforts to realize a society where all women can shine. It will improve systems for enabling women to realize their choice of way of working. It will strive to promote the empowerment of young people and realize a life-long active society. It will create an environment where highly skilled foreign workers and students from overseas can readily take advantage of their skills.

(2) Supporting marriage, childbirth, and childcare

To reverse the declining birthrate trend by around 2020, the five-year period starting in FY2015 is designated as the “Intensive Implementation Period for Stemming the Declining Birthrate,” with advancing child poverty countermeasures. In this period, necessary funds will be secured and invested intensively and effectively. The government will advance social care services for children, and measures to prevent child abuse.

(3) Implementing educational reform and promoting culture, the arts and sports,

The government will implement comprehensive educational reform. Japan will work to reach the world's highest level of academic skills. The government will carry out university reforms. It will aim for a nation built on culture and the arts, as well as on sports.

3. Regional reinvigoration that supports virtuous cycle in local economies

(1) Vitalizing Local economies

The government will deepen regional reinvigoration by inducing “earning capability,” “comprehensive powers,” and “private knowledge” in the regions. Based on the “Basic Policies for Overcoming Population Decline and Vitalizing Local Economies in Japan 2015”, the government will promote its policy package for regional reinvigoration.

(2) Regional reinvigoration

The government will promote regional reinvigoration, urban renaissance, the development of Okinawa, and decentralization reforms.

(3) Efforts toward hosting the Tokyo 2020 Olympic and Paralympic Games

While dynamically advancing efforts toward hosting the Tokyo 2020 Olympic and Paralympic Games, the government will enhance regional interaction and revitalization through the Host City/Town Concept and other measures. It will also promote “visit Japan” campaigns and improve the environment for accommodating visitors from overseas.

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

(1) Diplomacy, national security and defense

The government will dynamically advance strategic diplomacy. Along with the core Japan-U.S. alliance, it will expand and deepen its cooperative relationships with other countries in light of the National Security Strategy. Based on the National Defense Program Guidelines, etc., it will efficiently develop the country's effective and integrated defense capabilities.

(2) National resilience, disaster prevention and reduction

Under the Fundamental Plan for National Resilience, the government will take focused and efficient actions. It will also take precautionary measures for disaster prevention and reduction against potential natural disasters, including future large-scale earthquakes such as the predicted Nankai Trough Earthquake and Tokyo Inland Earthquake.

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

The government will take necessary steps to ensure the safety and security of citizens, including taking measures based on the “Strategy to Make Japan the Safest Country in the World”, counterterrorism and cybersecurity measures. It will also promote measures to secure the safety and security of consumers.

(4) Contributing to the global environment

The government will reduce greenhouse gas emissions and take other measures to curb global warming, as well as taking initiatives to create a recycling-oriented society.

Chapter 3: Framework of “Integrated Economic and Fiscal Reforms” - “The Plan to Advance Economic and Fiscal Revitalization¹”

1. Current economic and fiscal situation and challenges

- Through the advancement of the “three arrows strategy” in an integrated manner, both “overcoming deflation and revitalizing the economy” and, “fiscal consolidation” have made major progress. However, public finances and the social security system will not be sustainable in their current state. To address this situation, the Abe Cabinet will further strengthen the measures which have been implemented over the past three years, through proceeding with the following three pillars; “overcoming deflation and revitalizing the economy”, “reforming expenditure measures”, and “reforming revenue measures”.
- The government will carry out “Integrated Economic and Fiscal Reforms” as a social reform package with the participation not only of the government but also broadly of the whole nation.

2. Basic concept of the plan

- With the basic policy that “Without economic revitalization, there can be no fiscal consolidation”, the government will formulate “The Plan to Advance Economic and Fiscal Revitalization” which covers a five-year period (FY2016-FY2020). Reforms of expenditure and revenue measures will also aim to contribute to economic revitalization.
- As for reforming expenditure measures, the government will work on “Industrialization in public-related services”, “Incentive reform”, and “Innovation in public services”. Without reducing the quality or standards level of public services, the reforms will constrain public spending while mitigating the downward pressure on the economy. Across all expenditure items, the Abe Cabinet will further strengthen the measures which have been implemented over the past three years and proceed with a thorough review without any exceptions. Local governments will also proceed with thorough reviews in accordance with the central government’s efforts.
- On the revenue side, while improving the economic environment, a hike of the consumption tax rate to 10% will be implemented in April 2017. Further increases in revenue will be attained through promotion of “sophistication of the economic structure and achievement of higher value-added”, which will sustain stable economic growth.

3. Targets, the scenarios to achieve, and the reform process

- Through “Integrated Economic and Fiscal Reforms”, the government will firmly maintain its fiscal consolidation targets², and aim to achieve a primary

¹ This plan includes the fiscal consolidation plan.

² The government aims to achieve a primary surplus of the central and local governments by FY2020, thereafter the government will seek to steadily reduce the public debt to GDP ratio (“Medium-term Fiscal Plan (Cabinet Approval on August 8, 2013)”)

surplus by FY2020, while reducing the primary deficit to GDP ratio.

Thereafter, the government will seek to steadily reduce the public debt to GDP ratio over the medium- to long-term.

- In line with overcoming deflation and revitalizing the economy, interest rates and the fiscal balance will be carefully monitored.
- Intensive efforts will be made in the first three years (FY2016-FY2018), which are designated as the “Intensive Reform Period.” An expert panel investigation committee will be formed to embody the reform process and key performance indicators (KPIs) promptly. The committee will also conduct the progress management of reforms, check the reforms, and assess them.
- The government will assess the progress of reforming expenditure and revenue measures by using benchmarks such as approximately 1% of the primary deficit to GDP ratio in FY2018. Regarding general expenditures of the central government, the government is making efforts for expenditure reform in line with the past achievements of the Abe Cabinet, without presupposing an increase except in social security expenditure due to population aging, while taking into account a decline in total population and changes in wages and prices. Regarding social security expenditures, the government carries out the enhancement of social security with the increase in consumption tax revenues, while considering the effects of population aging and the trend of increase in social security expenditure under the Abe Cabinet. It should be noted that the government will seek to control the year on year expenditure flexibly, not evenly. Local government expenditures shall be also controlled in line with the efforts by the central government. Through using these benchmarks³, the government reviews the progress of expenditure and revenue reform. It will consider additional expenditure and/or revenue measures to achieve the fiscal consolidation target of FY2020 if necessary while holding another pillar of the reform, “overcoming deflation and economic revitalization”.
- Toward the hike of the consumption tax rate to 10% in April 2017, the government will appropriately respond to issues as necessary to ensure a suitable economic environment for smooth implementation of the hike.

4. Concept and approach for reforming expenditure measures, etc.

(1) Industrialization in public-related services

The government will effectively utilize private-sector knowledge, funding, and other resources to make public services more efficient and improve their quality. It will effectively utilize existing public capital stock, which has not been

³ Regarding the benchmark of general expenditures of the central government, the trend of the past three years under the Abe Cabinet, indicating that an essential increase of approx. 1.6 trillion yen, shall be continued until FY 2018 with consideration of the future economic situation and price movements, etc. Regarding local government expenditures which will be controlled in line with the efforts of the central government, the total amount of general revenue sources which would be necessary for stable fiscal management of local governments including those receiving local allocation tax grants, shall be maintained substantially at the same level as in the FY2015 Fiscal Plan of Local Governments until FY2018, and not below.

adequately utilized. It will also promote the creation of new private-sector services.

(2) Incentive reform

The government will build mechanisms that encourage changes in the mindset and actions of each citizen, business, and local government, etc. It will advance reforms to improve mechanisms which sufficiently work on them as incentives.

(3) Innovation in public services

The government will focus on “Thorough visualization of public services”, “Thorough implementation of the PDCA cycle based on evidence”, and “Simplification and Standardization of operations by utilizing the My Number (social security and tax numbers) system and IT”.

5. Basic policy and important challenges for reforms in each major policy area

Reforming expenditure measures shall be advanced without any exceptions.

Especially, social security, local-government administrative and fiscal reform, and cross-sectorial initiatives will be the key areas of expenditure reform.

(1) Social security

- While steadily advancing the comprehensive reforms of social security and tax, the government will also work on reforms aimed at realizing economic revitalization, fiscal consolidation, and securing the sustainability of the social security system.
- The government makes efforts for enhancing efficiency and promoting institutional reforms, under the benchmark where the recent trend of social security expenditures shall be sustained until FY2018, considering the achievements of the three years of economic revitalization and reforms under the Abe Cabinet, which include the trend over the past 3 years that the essential increase of social security expenditures was approximately equivalent to the level caused by population aging (approximately 1.5 trillion yen in 3 years), the future economic situation and price movements, etc. Including these considerations, the government aims to keep the increase in social security expenditures within the levels equivalent to the sum of the expected increase due to population aging and the planned enhancement of social security based on the hike in consumption tax rate, etc. toward FY2020.
- These reforms will include improvement of the delivery systems of healthcare and long-term care, prevention of lifestyle-related diseases and long-term care through incentive reform, promotion of industrialization in public-related services, ensuring fairness in contribution based on ability to pay, optimization of benefits, reforms associated with remuneration for medical treatment in terms of drug prices and dispensing, and reforms related to pharmaceuticals including promotion of the use of generic drugs.

(2) Social infrastructure improvement

Under the medium- to long-term outlook, the government will proceed with improvement of social infrastructure in a planned manner while enhancing its efficiency including in the area of the management. The government will fully utilize the existing facilities and institutional measures. It will also advance focused initiatives in order to ensure that stock effects are fully capitalized, while concentrating resources on prioritized areas in light of the declining population, and clarifying the priority and time line for the focused areas. The stock of public facilities will be optimized through proper management and operation. A broad

range of PPP/PFI projects will be promoted, including concessions.

(3) Local-government administrative and fiscal reform, and cross-sectorial initiatives

The government will reform the local allocation tax grants system for vitalizing local areas and for establishing a mechanism where the local governments which are making efforts are properly supported. It will make expenditures more efficient across the central and local governments. It will aim to achieve both improving efficiency in public administration and improving public services based on users' needs. It will work on wider use of IT and operational service reforms through the introduction of the My Number system, and the "visualization" of information related to public services.

(4) Education, science and technology, foreign diplomacy, and national security and defense, etc.

In the area of education, science and technology, the government will improve the efficiency of the budgets, based on the declining birthrate, promote the introduction of private-sector funding, and work on enhancing the quality of the budget and its prioritization. ODA will be utilized properly, efficiently, and strategically. The government will efficiently develop defense capabilities based on the "Medium-Term Defense Program".

(5) Reforming revenue measures and compression of assets and liabilities

The government will strive to ensure continued economic growth and increasing tax revenue. It will achieve the increase in revenue through the "sophistication of the economic structure and achievement of higher value-added", among other measures. In order to maintain and promote sustained economic growth along with establishing a steady revenue resource without hampering economic growth, the government will proceed with a comprehensive overhaul of the tax system. By focusing on the young generation that will play a key role in future growth, the government will reconstruct the social foundation for economic growth. It will proceed with a compression of assets and liabilities.

Chapter 4: Guiding principles in budget formulation for FY2016

1. Principles of economic and fiscal management

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

- The government will continue with early implementation of the budget in order to secure the realization of a virtuous economic cycle and widely deliver the benefits of Abenomics to local economies in a speedy manner. It will also work on ensuring that wage increases take root and on improving the environment for investment.
- The government expects the Bank of Japan to achieve its price stability target of 2%, in light of the economic situation and price movements.

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

The government will conduct economic and fiscal management in accordance with "The Plan to Advance Economic and Fiscal Revitalization." In the budget for FY2016, which is the first year of the plan, the government will make major

progress for expenditure reforms, etc.

2. Guiding Principles in compiling the budget for FY2016

- In compiling the FY 2016 Budget, the budgets of ministries will fully reflect the expenditure reforms based on the concept of this plan, including “industrialization in public-related services,” “incentive reform,” and “Innovation in public services.”
- On the expenditure side, the government will eliminate inefficient expenditures and conduct strict prioritization to compile an effectively focused budget.
- On the revenue side, the government will steadily proceed with increasing tax revenue through measures such as broadening the tax base, improving the taxation infrastructure, and securing non-tax revenue, etc.