Japanese Fiscal Policy and Public Debt Management

Mar. 8. 2017

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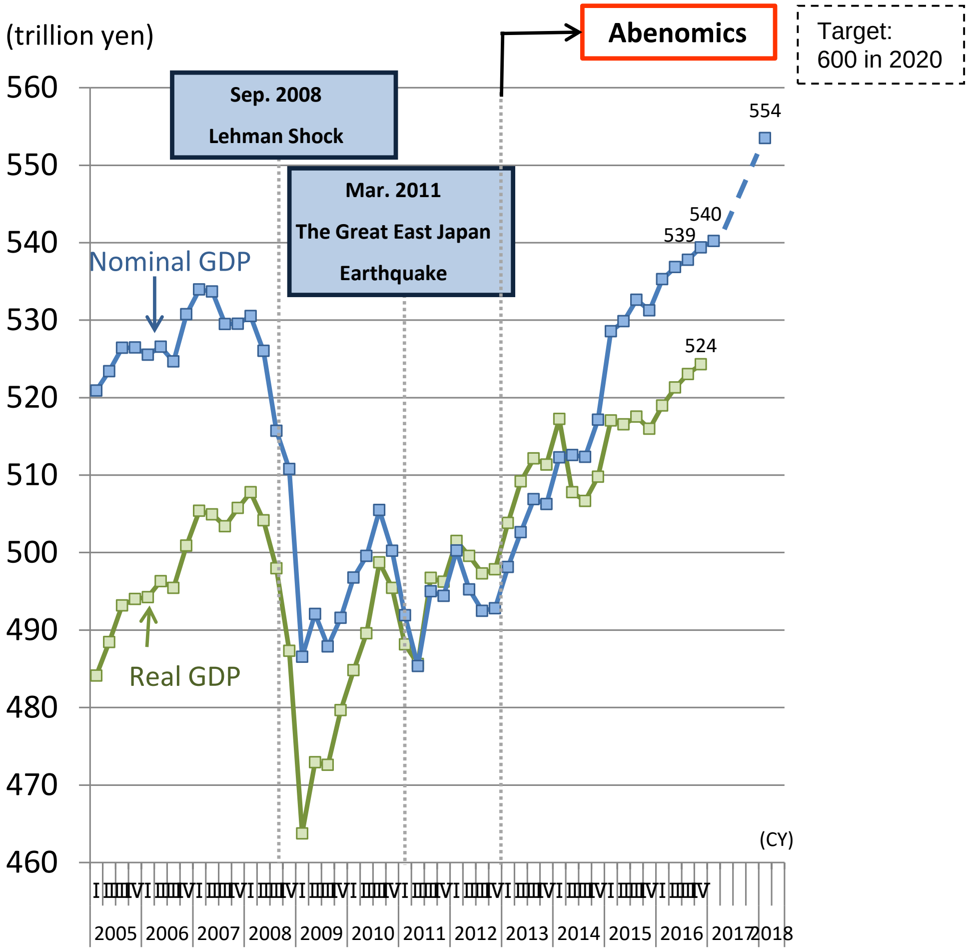
Economic Growth

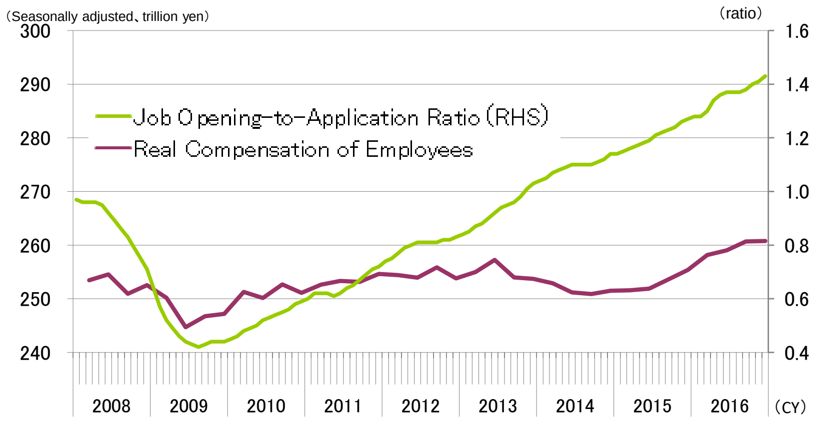


(Source) (actual)Cabinet Office, Government of Japan "Quarterly Estimates of GDP",
(forecast)"Fiscal 2017 Economic Outlook (Dec 2016) "(Nominal GDP)

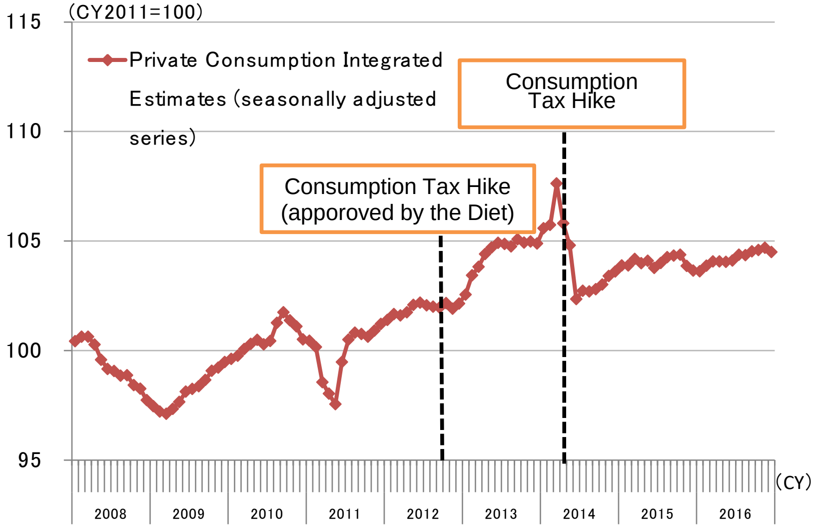
	2008	2009	2010	2011	2012	2013	2014	2015	2016	2016 1Q	2016 2Q	2016 3Q	2016 4Q
Nominal	-2.1	-6.0	2.2	-1.8	0.7	1.7	2.1	3.3	1.3	3.1	1.2	0.7	1.2
Real	-1.1	-5.4	4.2	-0.1	1.5	2.0	0.3	1.2	1.0	2.3	1.8	1.4	1.0

*2016 1Q, 2Q, 3Q, 4Q are annualized base

Employment and Wage



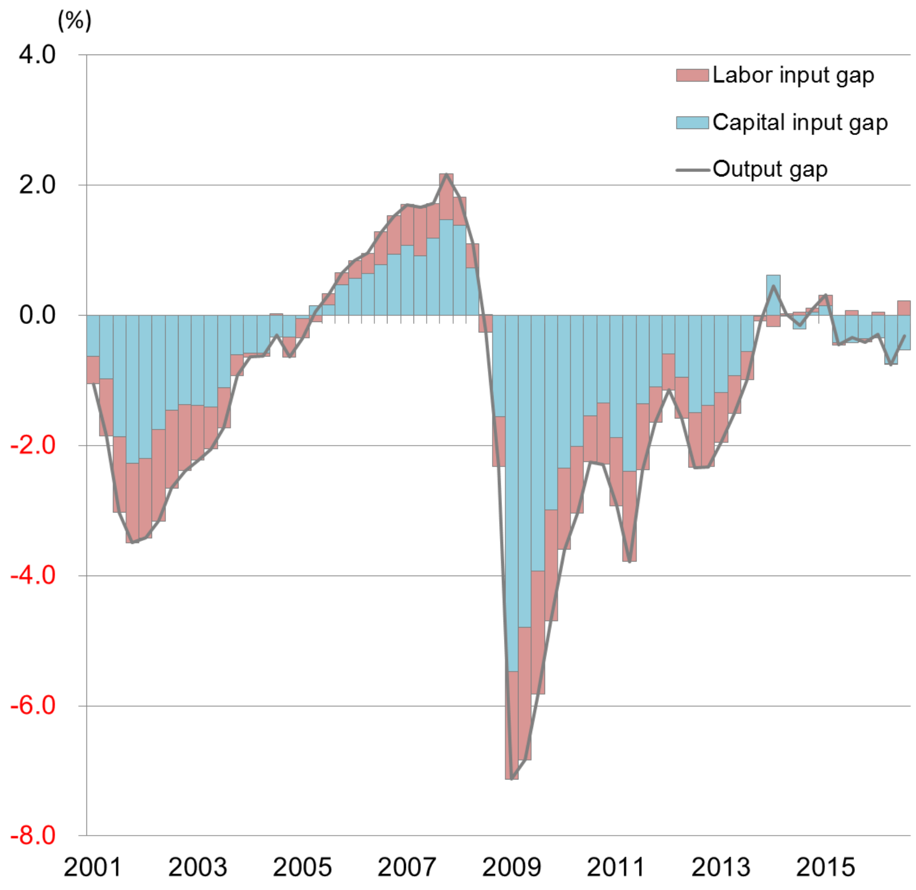
Consumption



3 month average

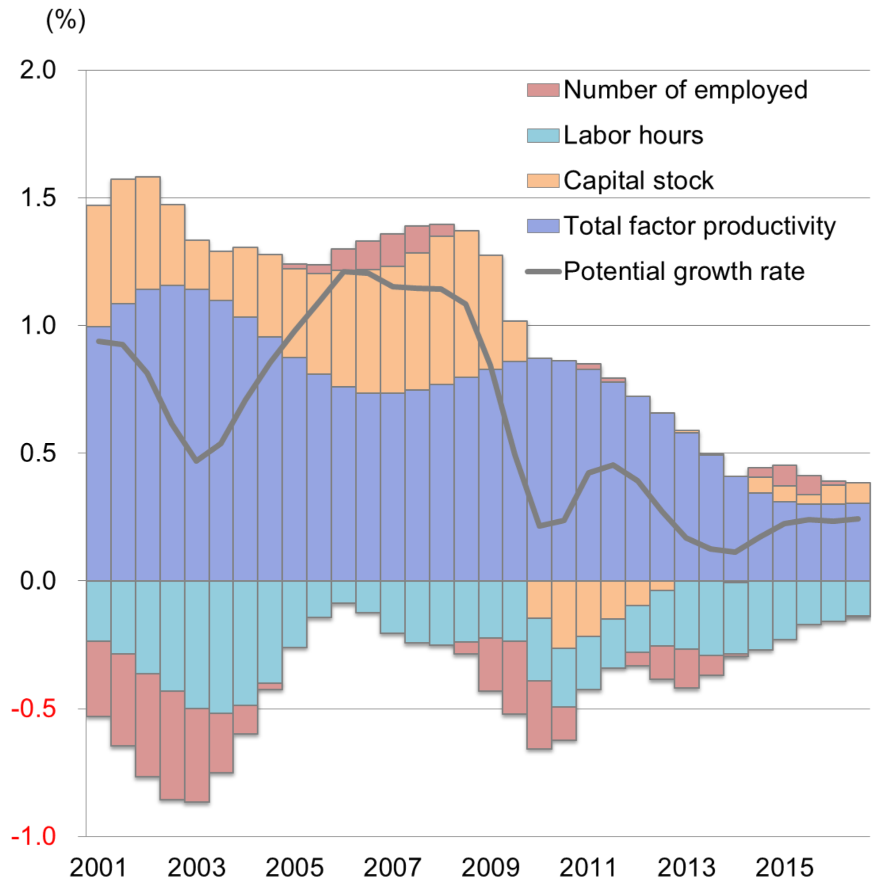
(Source) Cabinet Office, Ministry of Health, Labor and Welfare,
Ministry of Internal Affairs and Communications

Output gap



(Source) Bank of Japan

Potential Growth Rate



(Source) Bank of Japan

Framework of Fiscal Consolidation

Basic Idea of Abenomics

－Pursuing both economic revitalization and fiscal consolidation by using all policy tools

FY2020 Target
- ◇GDP600 trillion yen [2016 : 540 trillion yen]
- ◇Primary surplus of central and local governments [2015:-3.0% of GDP]

Measures
1) Aggressive monetary policy
2) Flexible fiscal policy
3) Growth strategy including structural reform

Benchmarks for Fiscal Reform

2016-18:Total increase of general expenditure from 2015 to 18 [3 years] : 1.6 trillion yen
[cf. Natural annual increase of social security expenditures : 0.64 trillion yen in 2017]

2018: Assess the progress and consider additional expenditure and/or revenue measures as necessary

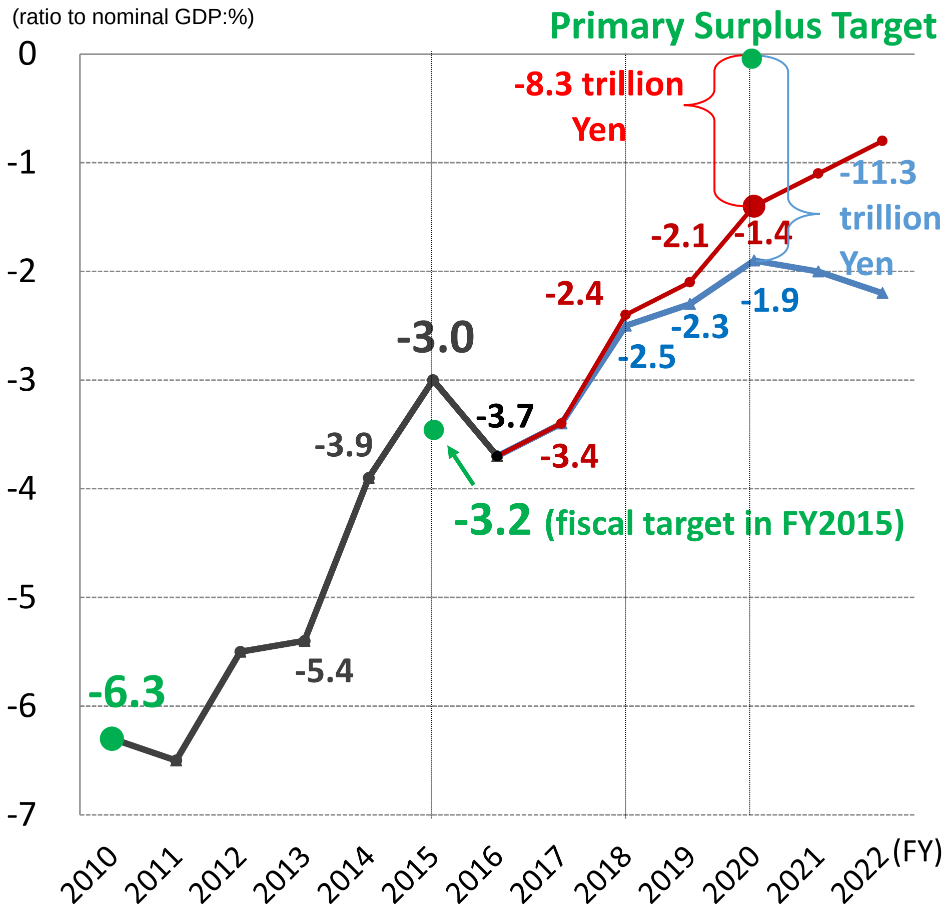
2019: Consumption tax hike (8% → 10%)

Fiscal Shape In the long run

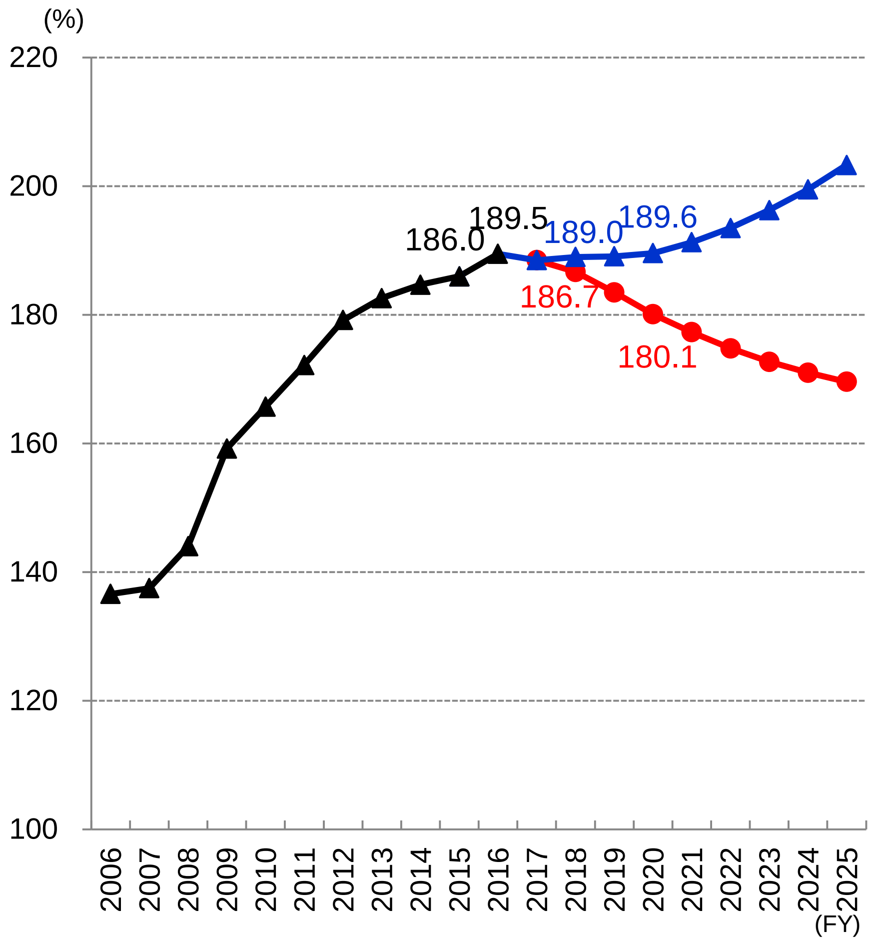
－Stabilize Debt to GDP ratio earlier aiming at steady reduction over the medium term.
[2016 Central and Local Government Debt:189.5%]

－Secure Fiscal sustainability despite population declining and aging society.

PB Projection



Debt to GDP Ratio Projection



●:Economic Revitalization Case

Average Growth Rate(FY2018-2025): Nominal GDP 3.7%, Real GDP 2.2%

Interest Rate: estimate increase up to 4.4% by FY2025

▲:Baseline Case

Average Growth Rate(FY2018-2025): Nominal GDP 1.5%, Real GDP 0.9%

Interest Rate: estimate increase up to 1.9% by FY2025

●⇒●

・Continuing tight expenditure control

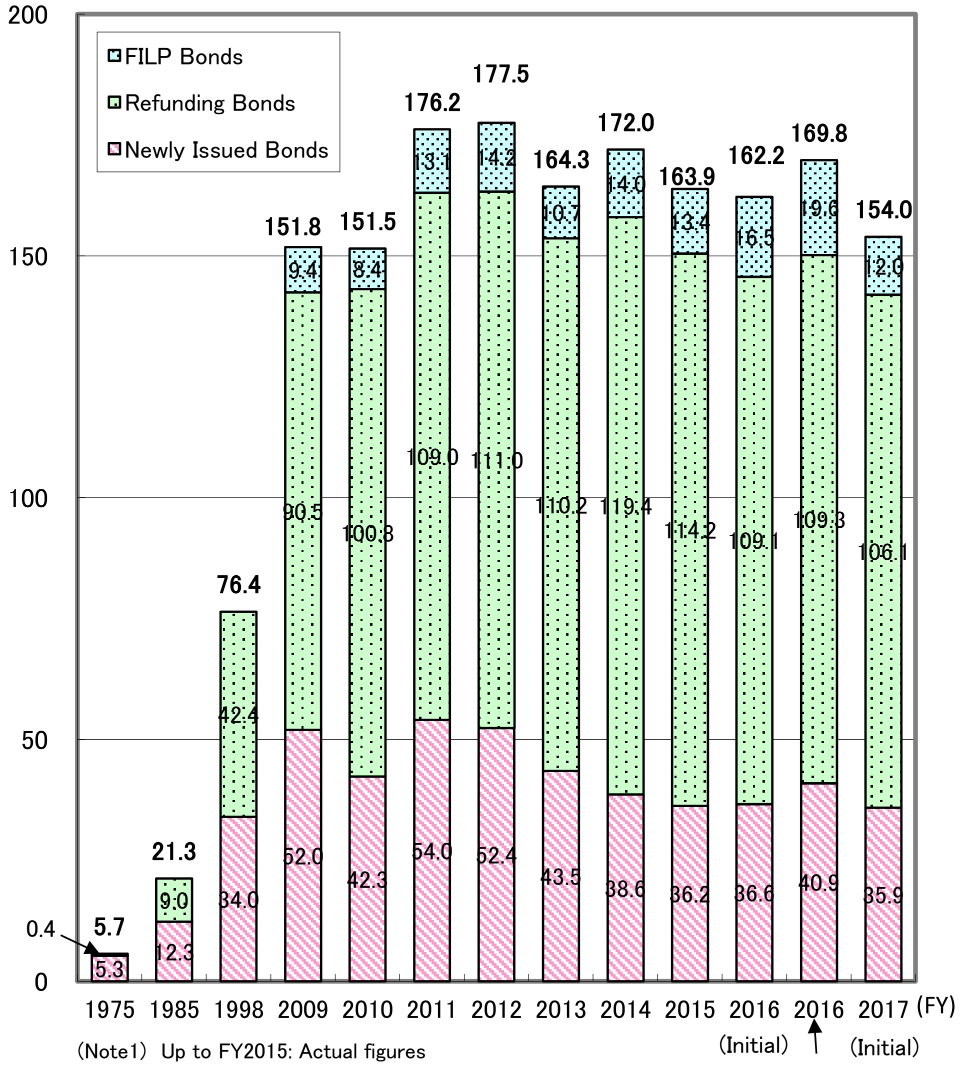
(Total increase of general expenditure from 2015 to 2018: +1.6 trillion yen)

・Additional expenditure and revenue measures following the 2018 interim review

In the Economic Revitalization Case, the ratio of outstanding debt to GDP is projected to decline toward FY2025. However, it should be noted that the long term interest rate is projected to be higher than the nominal GDP growth rate after FY2023, then the existing bonds which had been issued at low interest rates would be refinanced sequentially at higher interest rates.

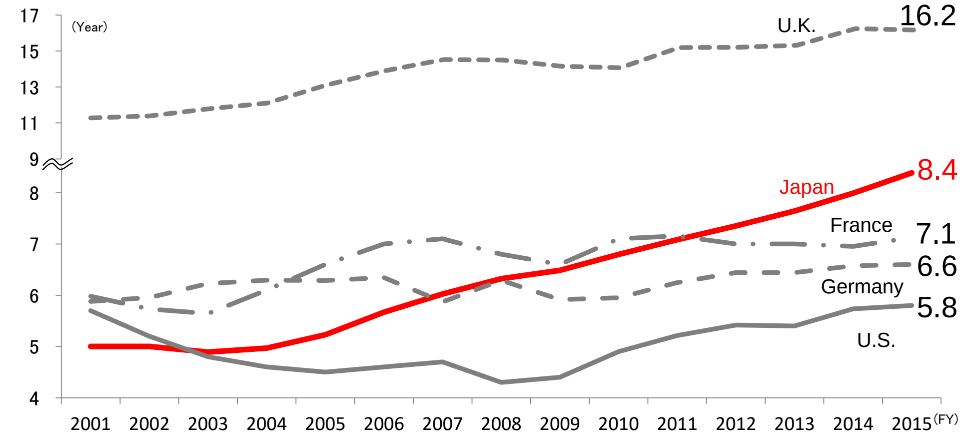
(Source) Cabinet Office

JGB Annual Issuance Amount



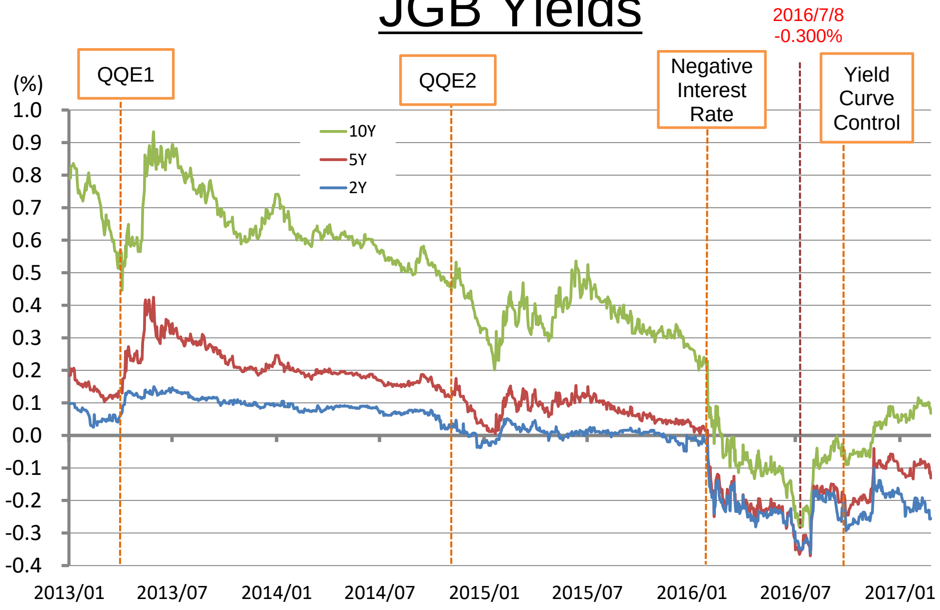
(Note1) Up to FY2015: Actual figures
(Note2) Figures may not sum up to total because of rounding.
(Note3) "Newly Issued Bonds" includes Reconstruciton Bonds and Special Bonds for covering Public Pension Funding.

Average Maturity of JGBs



(Source) Estimated by MOF based on data from websites of OECD and government debt management authorities

JGB Yields



(Source) Bloomberg

FY2017 JGB Issuance Plan

➢ Maturity structure is designed to reflect **investor demands** appropriately, so that the current low interest rate situation should be utilized smoothly and effectively.

- Super long-term (over 10 years): **Effectively increased** carefully assessing potential demand from investors such as life insurance companies, combining normal auctions and "Auctions for Enhanced-Liquidity"
  - Decrease in 20-year（- 1.2 trillion yen）, increase in 40-year（+0.6 trillion yen）
  - Increase in Auctions for Enhanced-Liquidity for Super long-term（+1.2 trillion yen）
- Long-term (10-year JGBs): **Decreased**, reflecting weakened demand in a low interest rate environment（- 1.2 trillion yen）
- Short- to Medium-term (5, 2-year JGBs and 1-year TBs): **Substantially decreased**, based on **diminished demand** under negative interest rate situation（- 4.8 trillion yen）

(unit : trillion yen)

	FY2017	Changes from FY2016
15.5-39 Year	3.0	+0.6
5-15.5 Year	6.6	+0.6
1-5 Year	1.2	±0
Total	10.8	+ 1.2

➢ The amount of Auctions for Enhanced-Liquidity is to be increased in remaining maturity zones where strong market **demands for improved liquidity** exist.

〈Breakdown by Legal Grounds〉

(unit : trillion yen)

	FY2017	Changes from FY2016(initial)
Newly-issued bonds (Construction Bonds and Special Deficit-Financing Bonds)	34.4	− 0.1
Reconstruction Bonds	1.5	− 0.6
FILP Bonds	12.0	− 4.5
Refunding Bonds	106.1	− 3.0
Total	154.0	− 8.2

〈Breakdown by Financing Methods〉

(unit : trillion yen)

	FY2017	Changes from FY2016(initial)
JGB market issuance	148.0	− 4.2
Market issuance (calendar-based)	141.2	− 5.8
Non-Price Competitive Auction Ⅱ etc	6.8	+1.6
Sales for Households	3.0	+1.0
BOJ rollover	3.0	− 5.0
Total	154.0	− 8.2

〈Market Issuance Plan by JGB types〉

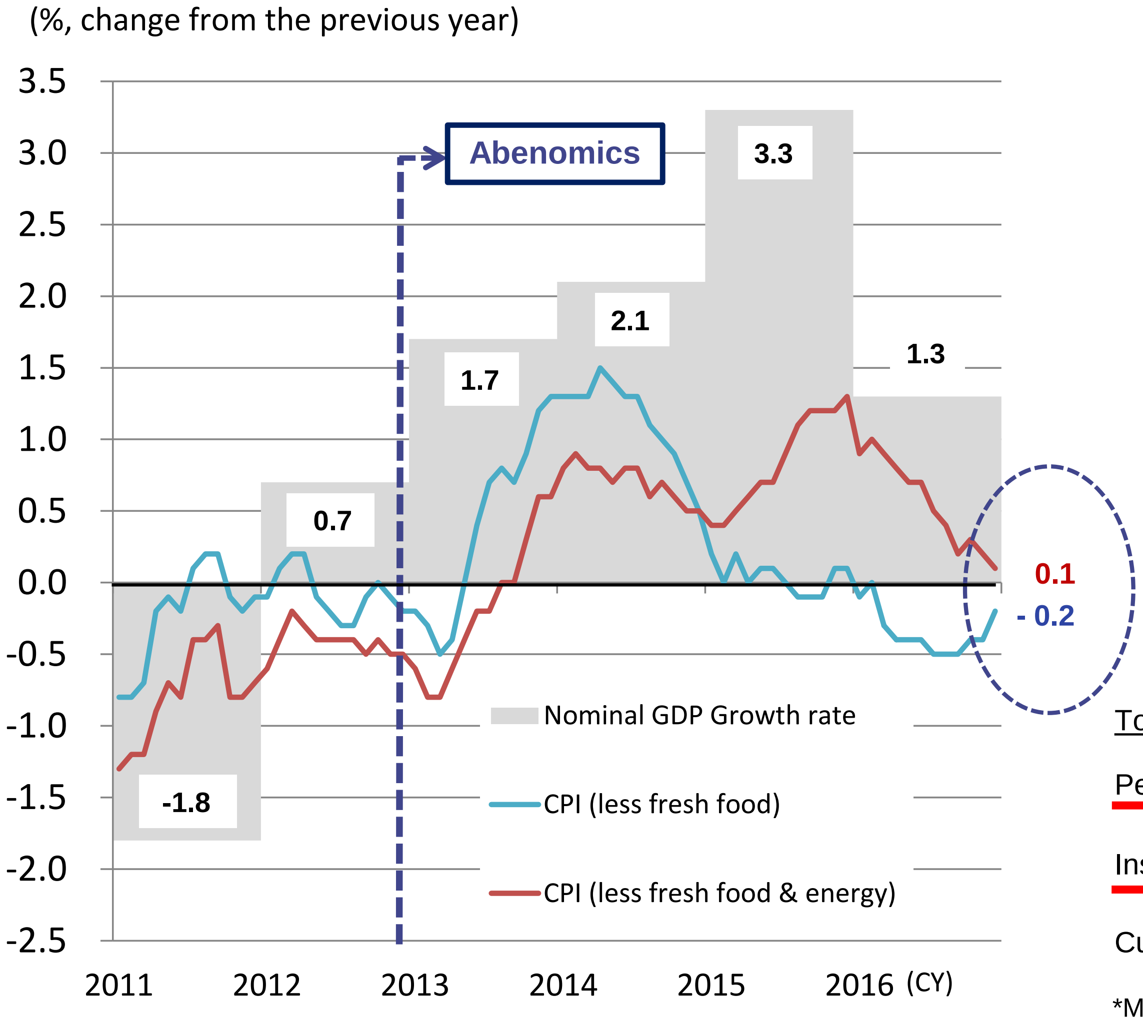
(unit : trillion yen)

	FY2017	Changes from FY2016(initial)
40-Year	3.0	+0.6
30-Year	9.6	±0
20-Year	12.0	− 1.2
10-Year	27.6	− 1.2
5-Year	26.4	− 2.4
2-Year	26.4	− 1.2
TBs(1-year)	23.8	− 1.2
10-Year Inflation-Indexed	1.6	− 0.4
Auctions for Enhanced-Liquidity	10.8	+1.2
Total	141.2	− 5.8

Appendix

CPI and Consumer Confidence

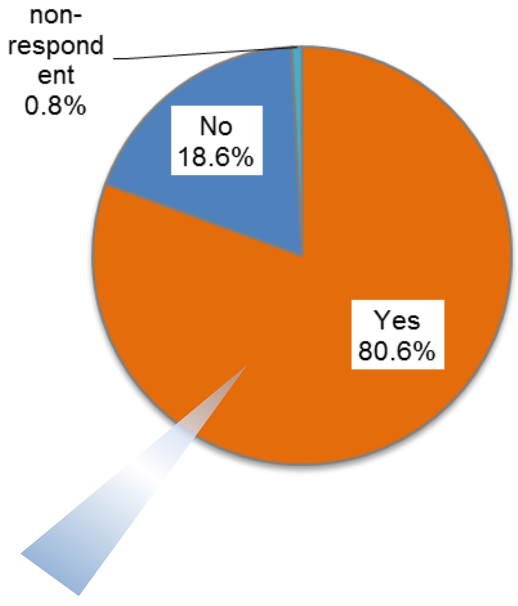
Consumer Price Index



(Note) The effects of consumer tax rate change in April 2014 on CPI are eliminated.
(Source) MOF, Cabinet Office, Ministry of Internal Affairs and Communications, BOJ

"Do you have anxiety about post-retirement life?"

(Research by The Central Council for Financial Services Information)



Top 3 reasons of "Yes"

Pension and insurance	72.5%
Insufficient financial assets	69.5%
Currently uncomfortable about daily lives	41.4%

*Multiple answers allowed

(Source)The Central Council for Financial Services Information

Wage and Employment

(million, %)

	2012	2013	2014	2015	2016
Regular Employees					
Change of Nominal Wages	-0.3	0.4	0.9	0.4	0.8
Number of Employees	33.4	32.9	32.8	33.0	33.6
(change)	(-0.4)	(-1.4)	(-0.5)	(0.8)	(1.5)
Non-regular Employees					
Change of Nominal Wages	1.5	-0.4	0.5	0.5	-0.1
Number of Employees	18.1	19.1	19.6	19.8	20.2
(change)	(0.1)	(5.1)	(2.9)	(0.9)	(1.8)
Total Employees					
Change of Nominal Wages	-0.9	-0.4	0.4	0.1	0.5
Change of Real Wages	-0.9	-0.9	-2.8	-0.9	0.7
Number of Employees	51.5	52.0	52.4	52.8	53.7
(change)	(-0.2)	(0.9)	(0.7)	(0.8)	(1.7)

(Source) : Ministry of Health, Labor and Welfare, Ministry of Internal Affairs and Communications

Growth Strategy

Regulation Reform

- Reduction of Effective Corporate Tax Rate
  —37.00%(2012) → 29.74%(2018)
- Corporate Governance
  (more than 3500 companies)
  —Stewardship Code
  (214 corporate investors)

Japanese stewardship code will be revised in 2017.
(PM Abe's speech in NY (Sep. 2016))

- Electric Power Deregulation
- TPP, Japan-EU EPA
- Agriculture Structural Reform
- Drastic simplification project for regulation and administrative process for foreign investors

The Council for Regulatory Reform started from Sep 2016.
—Cabinet Decision Jun. 2016

Work-style and Labor Market Reform

- Equal pay for equal work
  —guideline released on Dec
- Increase minimum wage
  —3% hike（2016）
- Increase the capacity of child care and elderly care
  —500k for each
  —raise wages for care workers
- Reducing working hours and improving labor productivity
- Lengthen the eligible period for maternity leave benefits
- Utilizing foreign professional
  —World's fastest Green card system
- Income Tax reform
  —To encourage female labor participation(From FY2017)

Submit related Bill in2017

Investment for the Future

- Forth Industrial Revolution（Society5.0）
  —Social application of AI, Robot, IOT
- Industrial Structural Reform
- Medical Care Innovation
- Encouraging Investment for R&D
  —prioritize public investment in growth-enhancing areas
  —support new cutting-edge technologies

Increase Disposable Income
(for low income households)

- Introduce a new government-sponsored scholarship
- Shorten the minimum eligible period for receiving pension from 25 to 10 years

FY 2017 Tax Reforms
Promoting Corporate Investment and Wage Hikes

- Spurring innovation and investment

- Reward higher R&D investment by providing more tax deduction (up to 14% of total R&D expenses).
- Extend the deadline for corporate tax filing by three months to help companies better prepare for dialogue with investors; and expand deductible management remuneration to include a salary that is linked to share price.
- Create a new 20-year tax-exempt Nippon Individual Savings Account (NISA) scheme to offer more safe investment opportunities.

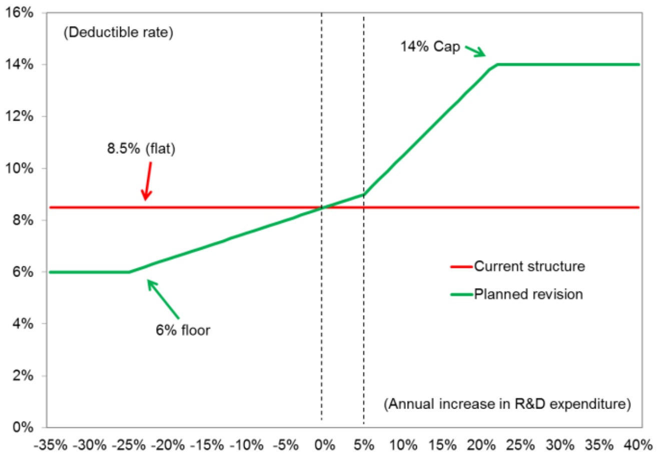
- Boosting wages and encouraging women to work more

- Expand the tax incentive for an increase in salary expense (from 10 to 12% of the increase).
- Raise the income limit for the spousal tax deduction from 1.03 million to 1.5 million.

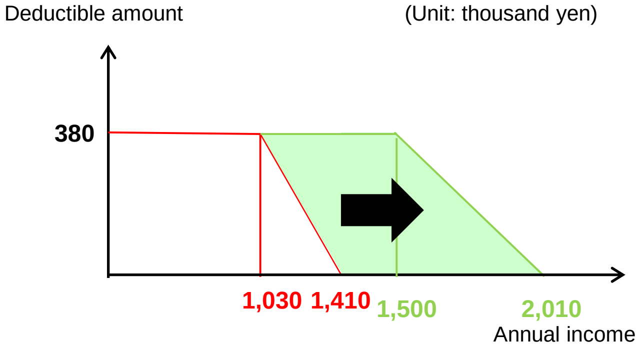
- Others

- Provide tax exemption when foreign visitors purchase *sake* at local breweries.
- Review applicability of inheritance tax for foreign residents to attract highly-skilled foreign workers.

R&D Tax Deduction



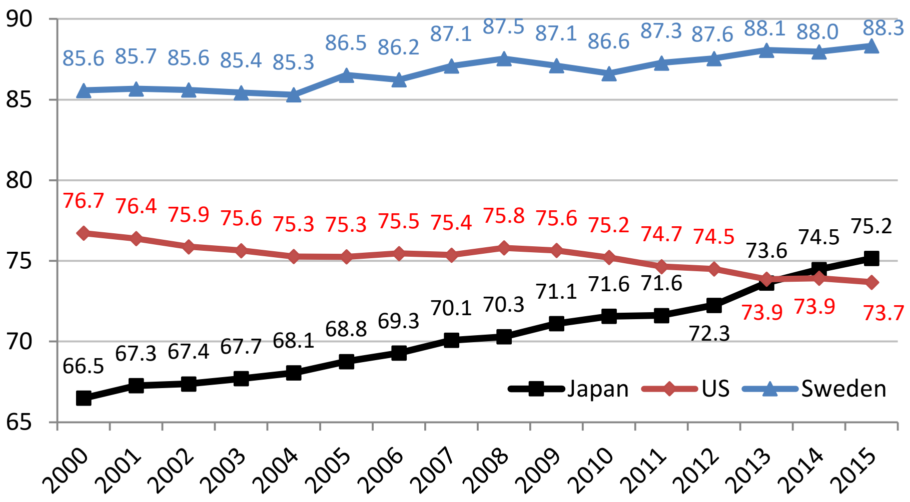
Spousal Tax Deduction



Progress of Structural Reforms and Growth Strategy

Women's labor force participation rate

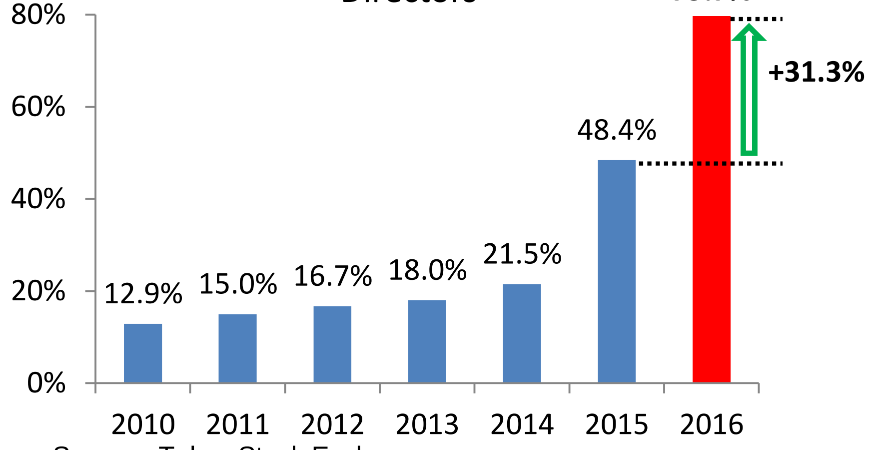
(cross country comparison)



*Age: 25-54 Source: OECD Stat

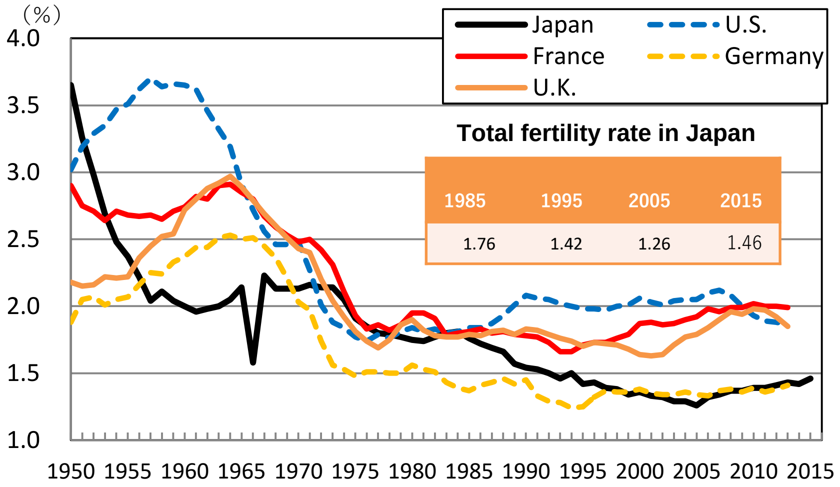
Corporate Governance Reform

Ratio of 1st Section Companies with two or more Independent Directors



Source : Tokyo Stock Exchange

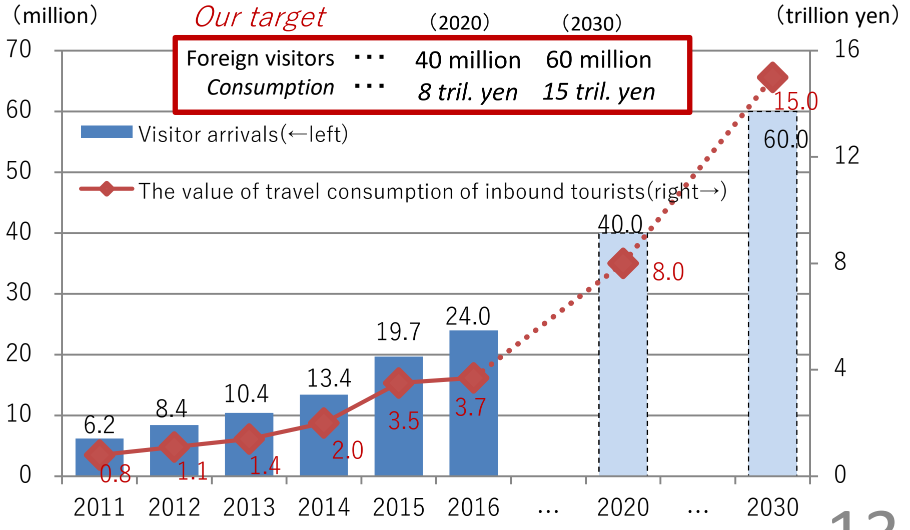
Total fertility rate



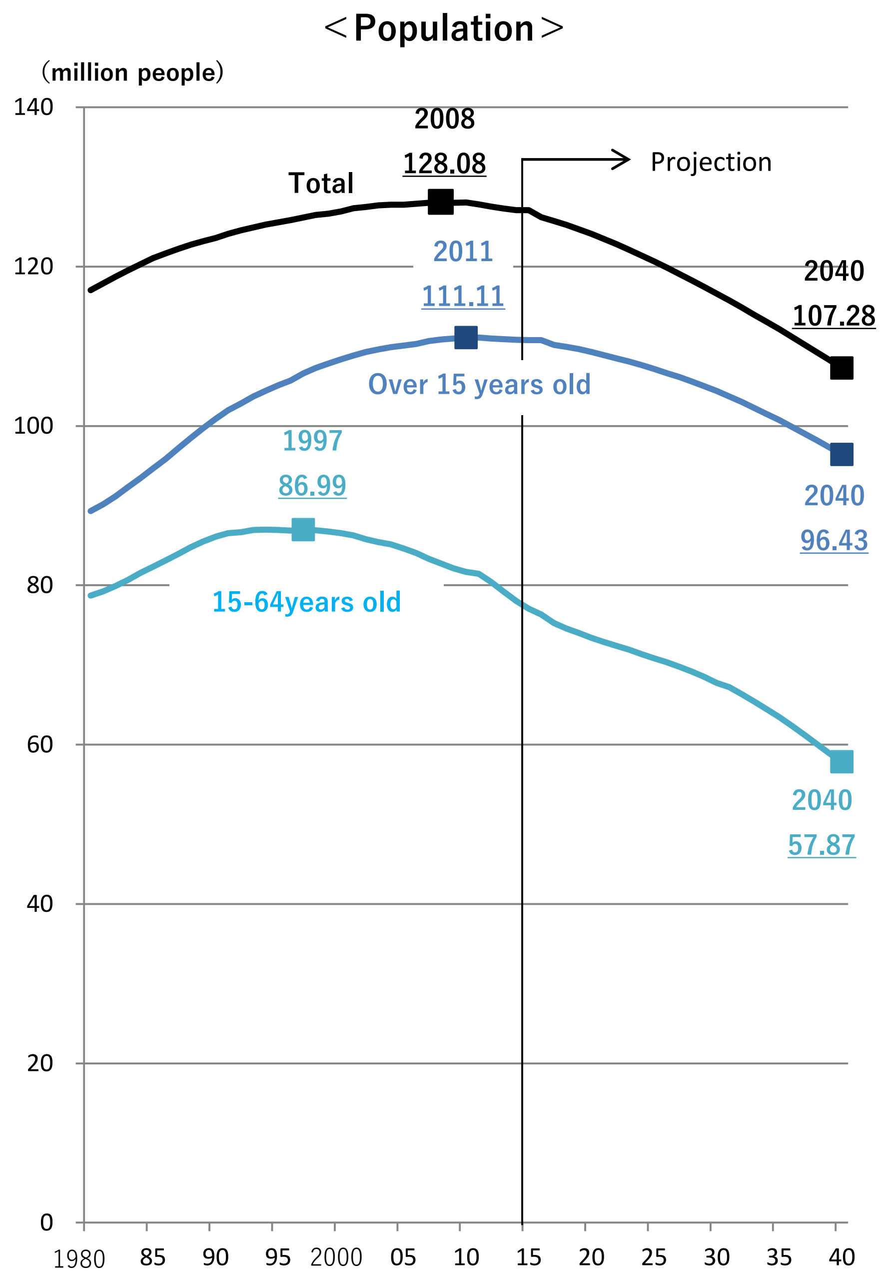
1985	1995	2005	2015
1.76	1.42	1.26	1.46

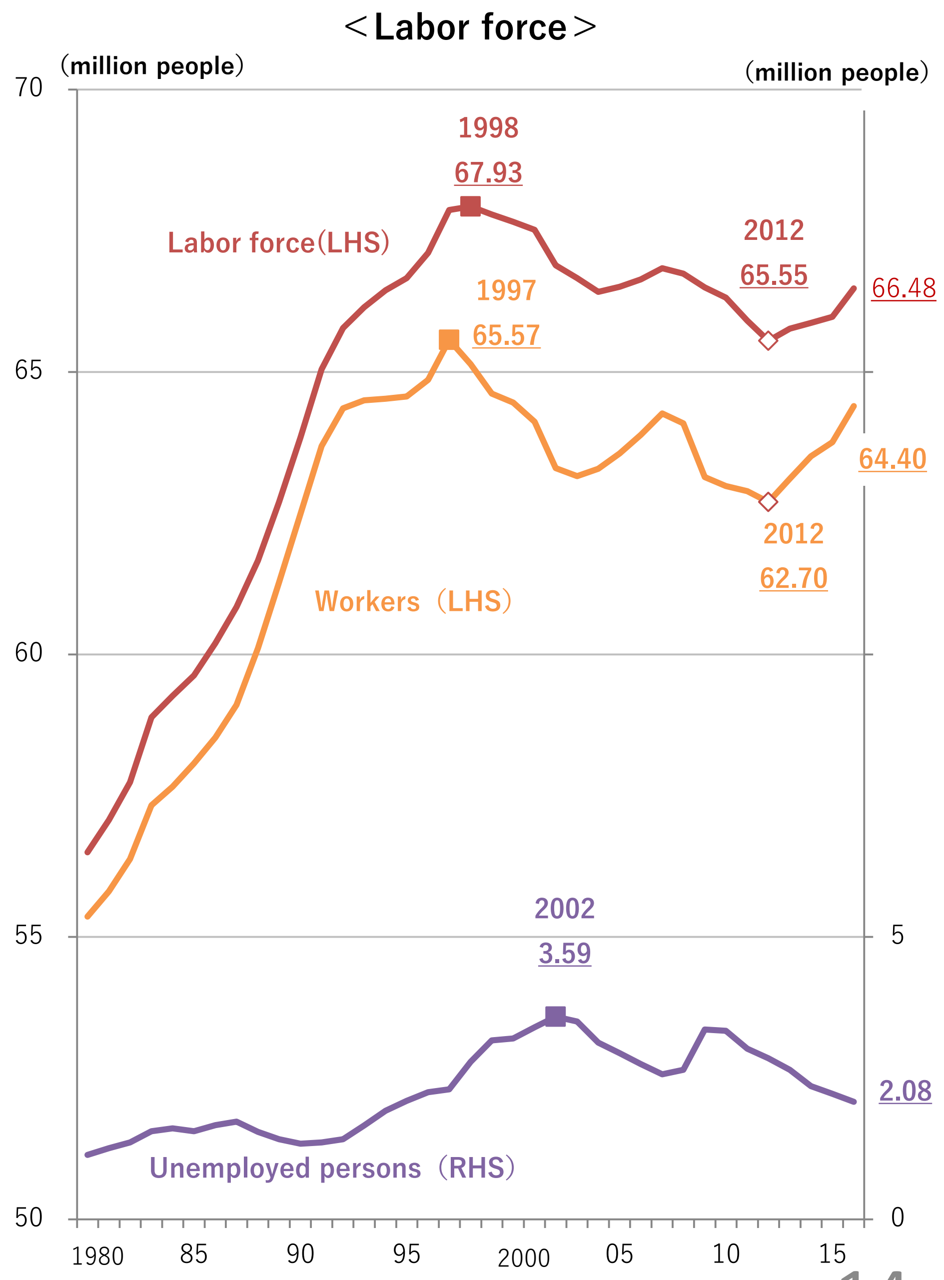
Source: Cabinet Office

Toward a "Tourism-oriented developed nation"



Source: Japan National Tourism Organization

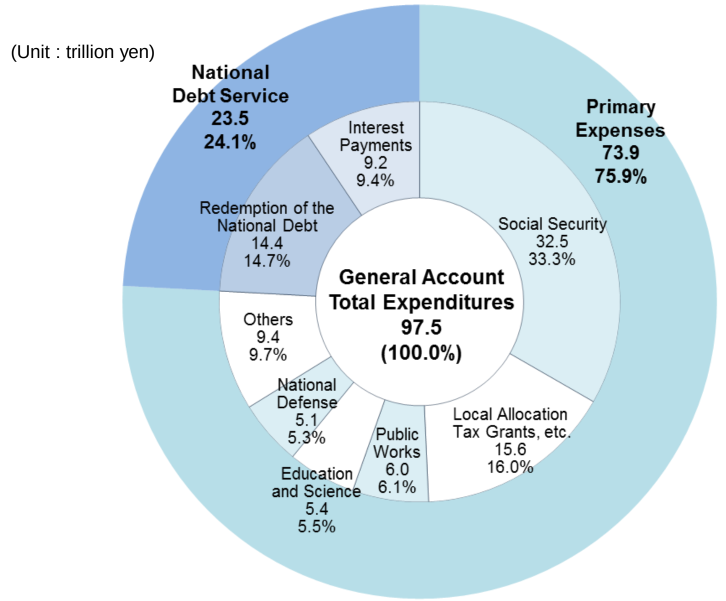


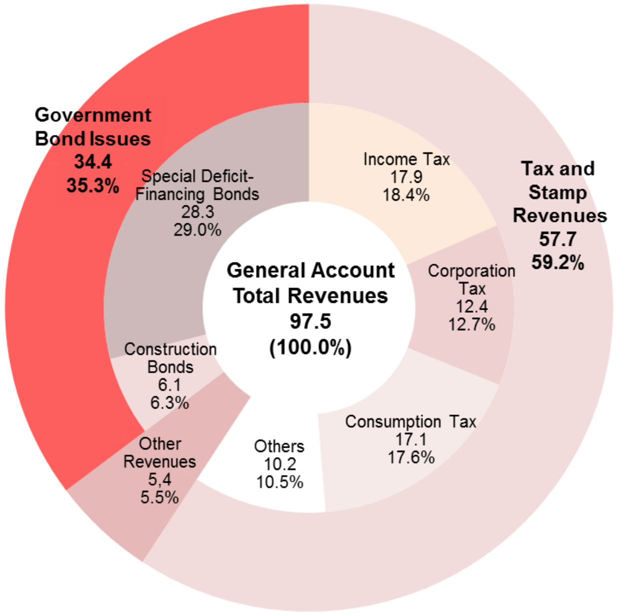


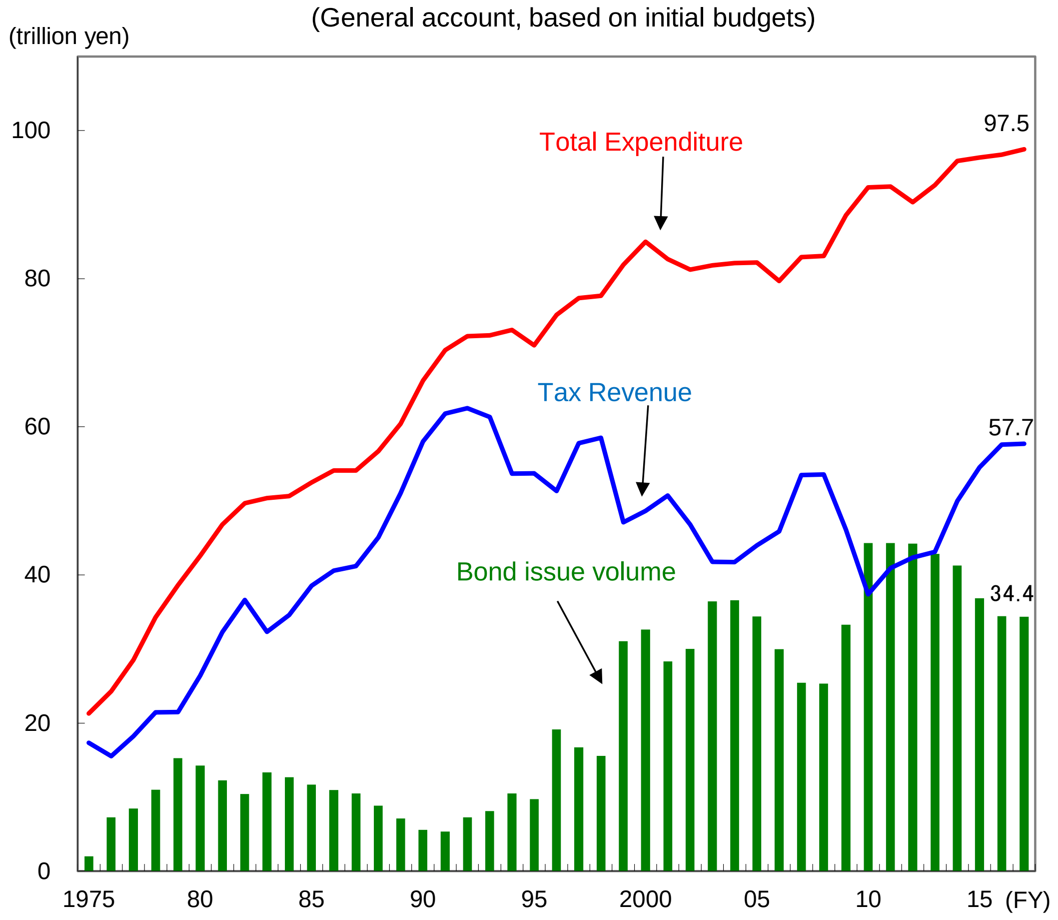
(Source) Ministry of Internal Affairs and Communications, National Institute of Population and Social Security Research

Expenditure and Revenue

FY2017 Initial Budget

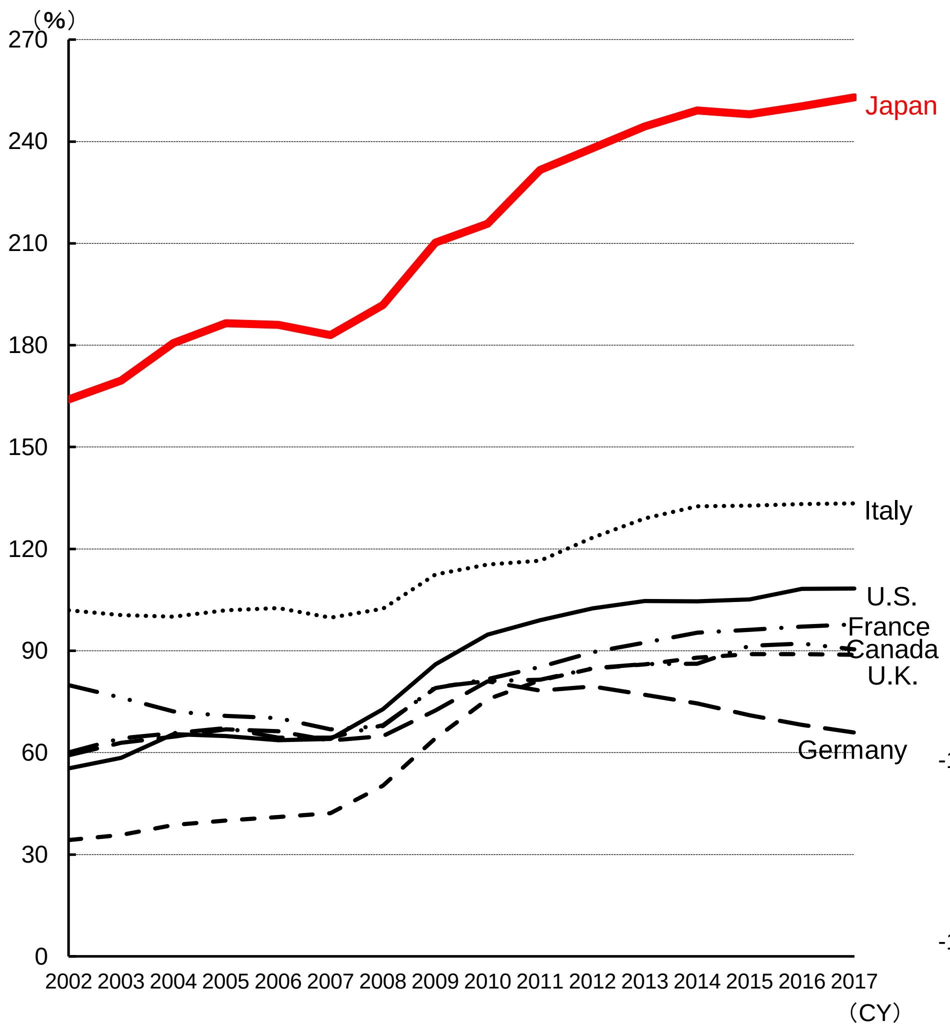






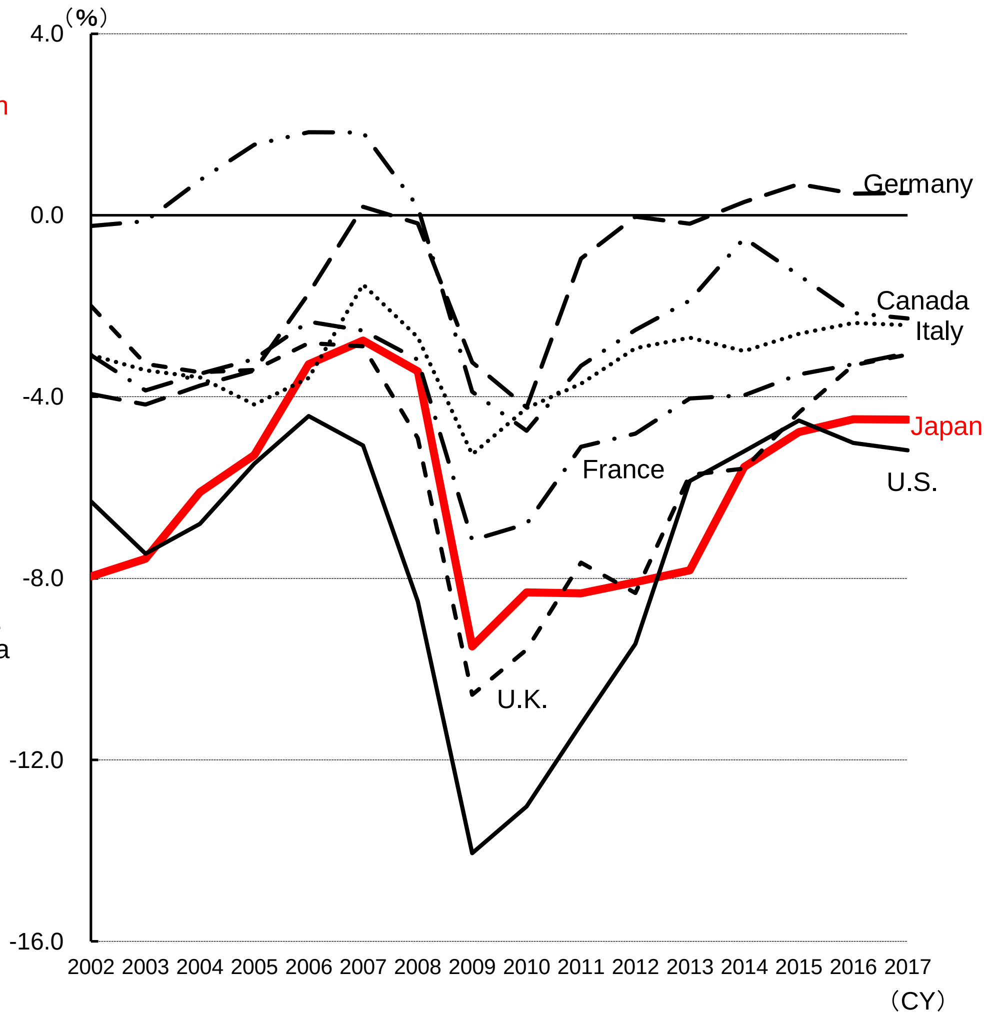
(Note) Figures may not add up to the totals due to rounding.

General Government Gross Debt



(Source) IMF "World Economic Outlook Database"(October 2016).
(Note) FY2017 draft budget data is not reflected.

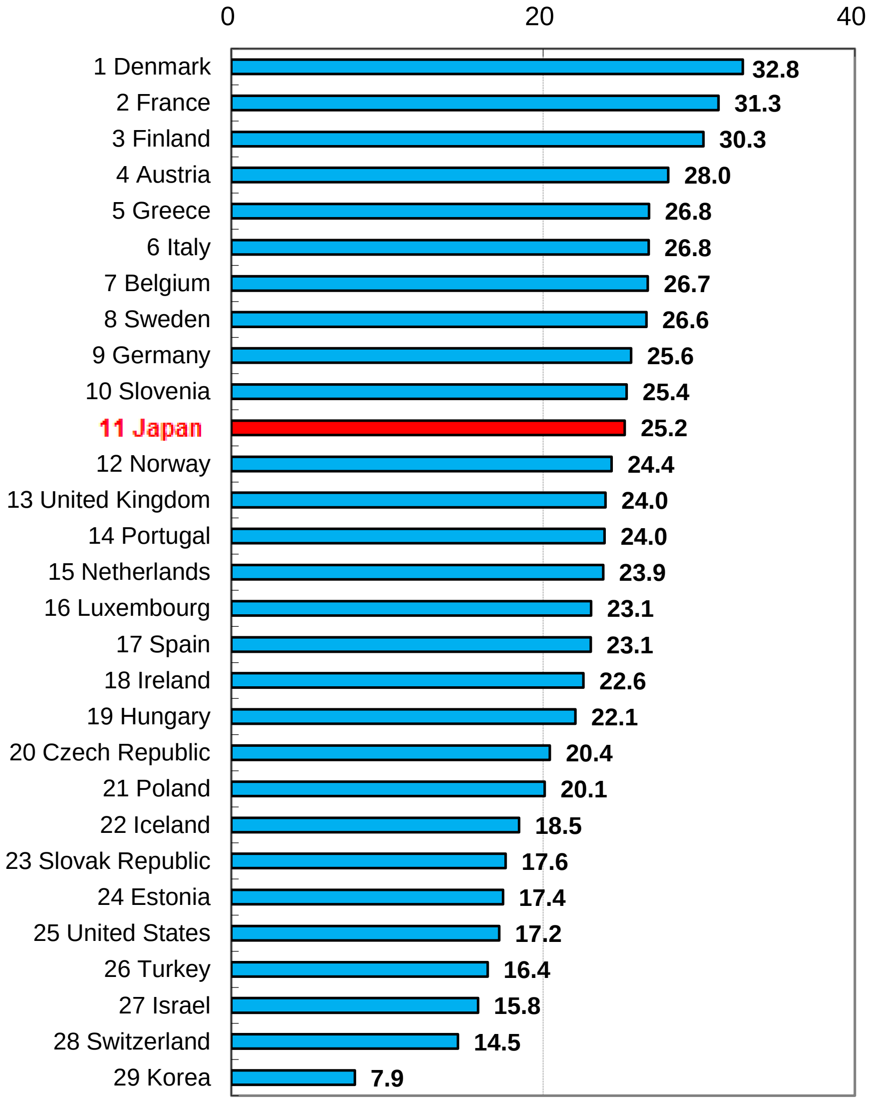
General Government Fiscal balance



(Source) OECD "Economic Outlook 100"(November 2016).
(Note1) Figures represent the general government-based data (including the central/local governments and social security funds), except for Japan and the U.S. where the figures of the social security funds are excluded. The following figures include social security funds.
(Note2) FY2017 draft budget data is not reflected.
(Note3) Figures for Japan are adjusted to exclude special factors.

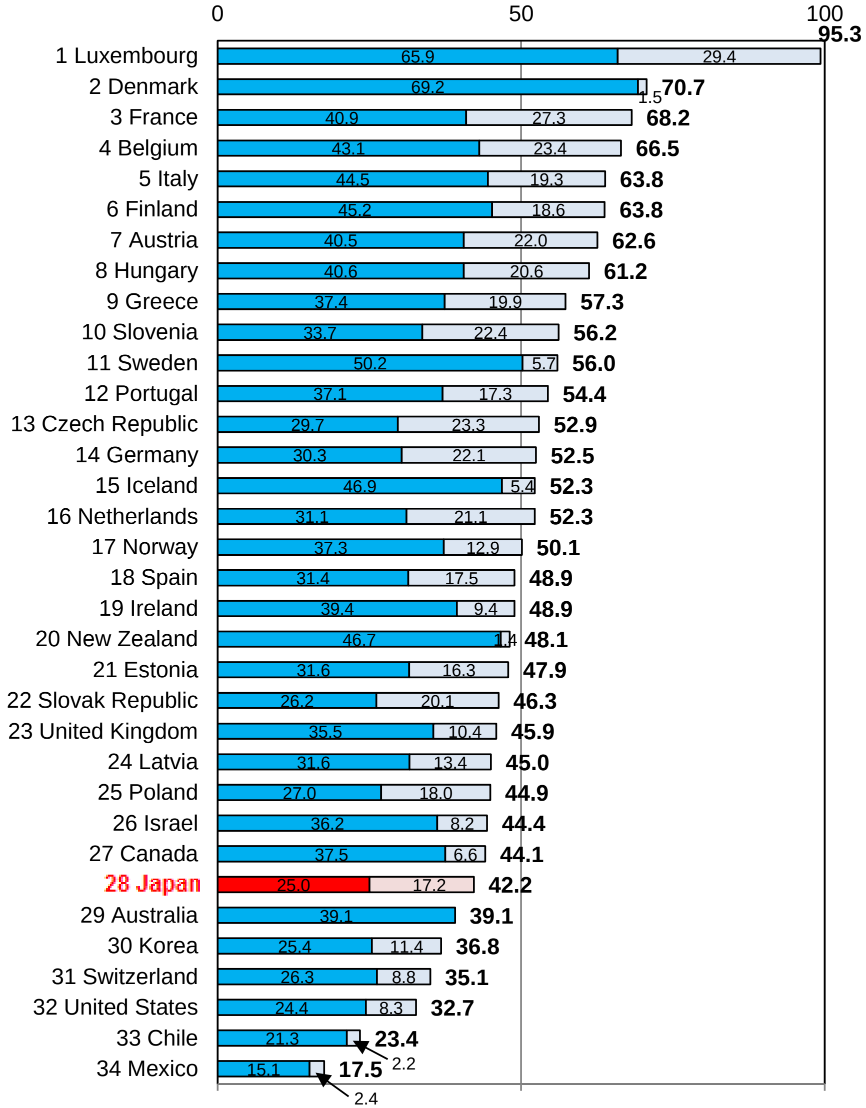
Comparison of OECD Countries

General Government Social Security Expenditures (as a percentage of GDP: 2011)



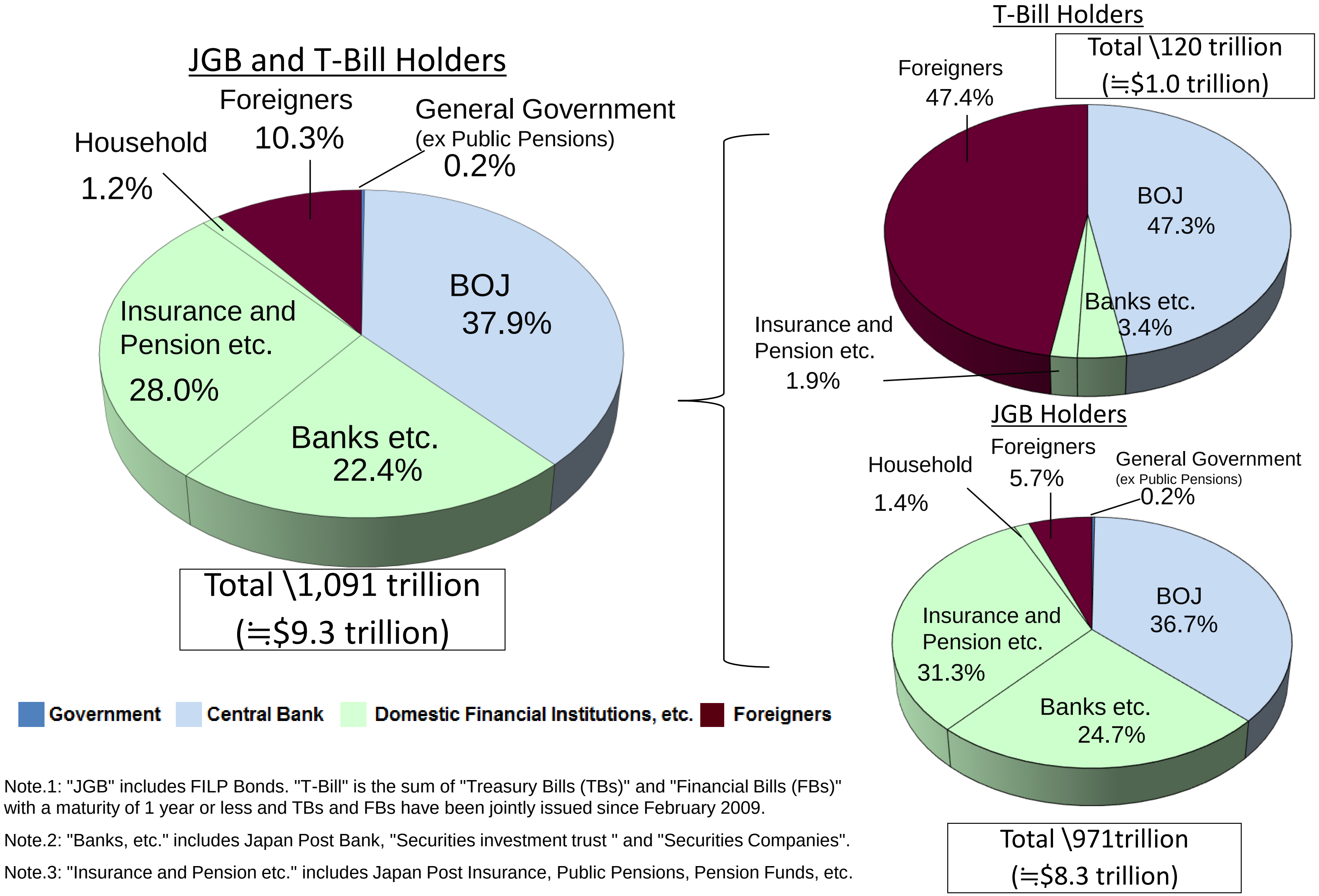
(Source) OECD “National Accounts”, “Revenue Statistics”, EU “Government Finance Statistics”, etc.
(Note1) The data in 2011 is used because no comparable data is available in terms of statistical standards after 2012.
(Note2) Figures represent the general government-based data (including the central/local governments and the social security funds) except for fiscal balance.

Tax and Social Security Contributions Ratio (as a percentage of NI: 2014)



(Source) Cabinet Office, OECD “National Accounts”, “Revenue Statistics”,
(Note) Figures of Iceland are as of CY2013.

Breakdown by JGB and T-Bill Holders (Sep. 2016)



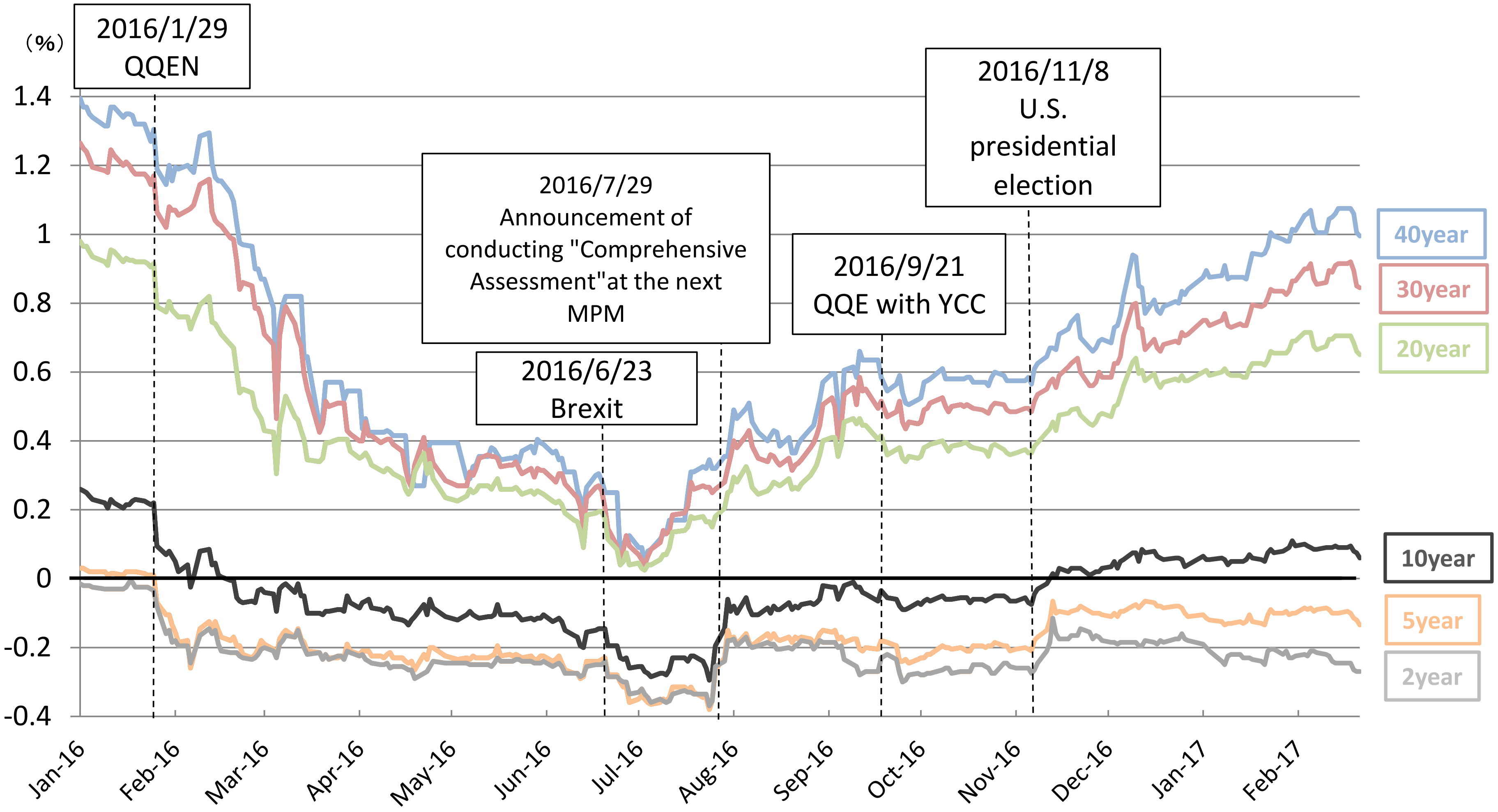
Note.1: "JGB" includes FILP Bonds. "T-Bill" is the sum of "Treasury Bills (TBs)" and "Financial Bills (FBs)" with a maturity of 1 year or less and TBs and FBs have been jointly issued since February 2009.

Note.2: "Banks, etc." includes Japan Post Bank, "Securities investment trust " and "Securities Companies".

Note.3: "Insurance and Pension etc." includes Japan Post Insurance, Public Pensions, Pension Funds, etc.

Source: Bank of Japan “Flow of Funds Accounts (Preliminary Figures)”

JGB yields



(Source) Japan Bond Trading Co.

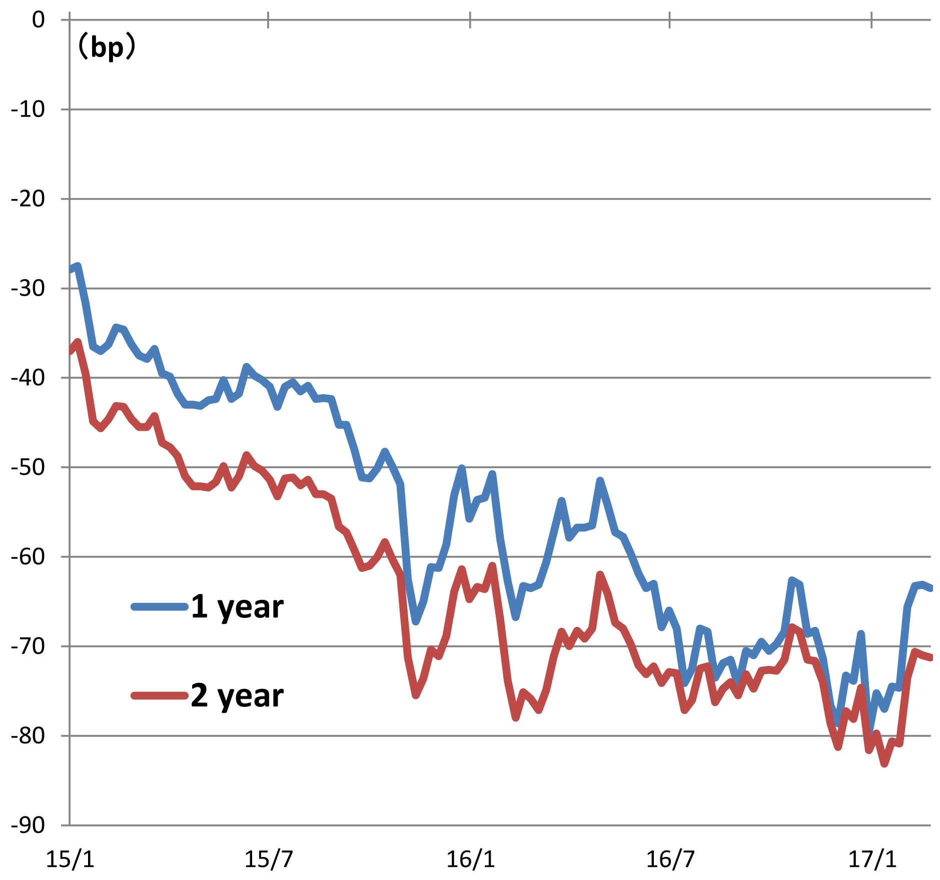
List of Major Countries' Sovereign Ratings

(Long–term debt denominated in home currency on 24 Feb 2017)

	Moody's	S&P	Fitch
Aaa/AAA	U.S. Germany Canada	Germany Canada	U.S. Germany Canada
Aa1/AA+	U.K.(↓)	U.S.	
Aa2/AA	France Korea	U.K.(↓) France Korea	U.K.(↓) France
Aa3/AA-	China(↓)	China(↓)	Korea
A1/A+	Japan	Japan Ireland	China
A2/A			Japan(↓) Ireland
A3/A-	Ireland(↑)		
Baa1/BBB+		Spain	Spain Italy(↓)
Baa2/BBB	Italy(↓) Spain		
Baa3/BBB-		Italy	
Ba1/BB+	Portugal	Portugal	Portugal
Ba2/BB			
Ba3/BB-			
B1/B+			
B2/B			
B3/B-		Greece	
Caa1/CCC+			
Caa2/CCC			Greece
Caa3/CCC-	Greece		
Ca/CC			
C			
SD/RD			

"(↑)"shows that the outlook is positive.
"(↓)"shows that the outlook is negative.

Dollar/Yen Basis Spread



(Source) Bloomberg