

August 2008

Forecast for the Japanese Economy in Fiscal 2008 and 2009

— Recovery or Recession? That May Not Be the Key Issue —



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1. Outlook for the Japanese Economy in Fiscal 2008 and Fiscal 2009 -- Recovery or Recession? That May Not Be the Key Issue.

(1) Current State of the Economy

(a) GDP Data for the April-June Quarter Show Weakness in the Economy

A growing number of observers are coming to the conclusion that the Japanese economy is already slipping into recession, and concerns about future trends are growing. GDP data for the April-June quarter of 2008 suggested a deterioration in economic conditions. The real growth rate fell to minus 0.6% compared with the previous quarter (minus 2.4% at an annualized rate), the first negative figure in a year. In nominal terms, the growth rate dropped to minus 0.7% (minus 2.7% at an annualized rate).

Private consumption, private capital investment, and private residential investment—key components of domestic demand—all showed declines in the April-June quarter. Together, the contribution of domestic demand, including these three components, was minus 0.6 percentage point, thus acting as a strong drag on economic growth. The weakness in consumption for the April-June quarter was in part due to the relatively high growth in the January-March quarter, owing to the extra day in February due to 2008 being a leap year, as well as the adverse impact on real incomes of rising prices and other factors. The decline in capital investment may have been due to the negative impact of deteriorating profitability as a result of the run-up in raw material prices and the slowdown in overseas economies. In the housing investment area, the sharp decline resulting from the impact of revisions in Japan's building code appears to be running its course, but rising prices of homes are weighing heavily on housing market activity.

On the other hand, the contribution of the external sector, which had been making a positive contribution to growth, fell sharply to 0.0 percentage point in the April-June quarter, and had a neutral effect on growth. Exports declined for the first time in 13 quarters, because of the slowdown in the

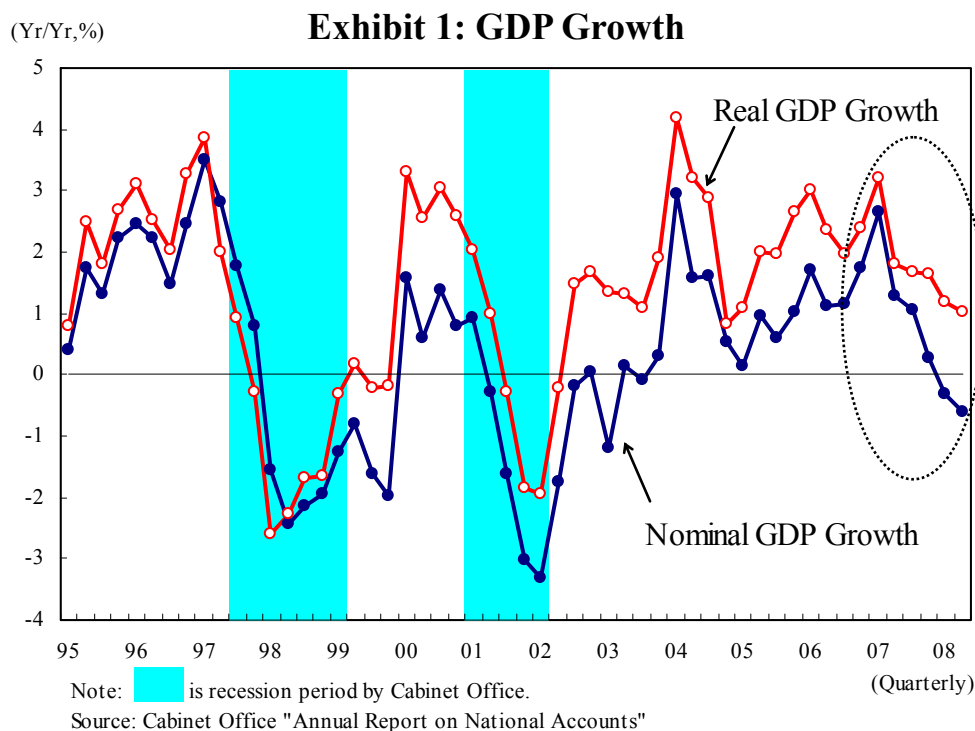
world economy, principally in Europe and the United States.

The GDP deflator, which measures price movements in the economy as a whole, was down 1.6% compared with the same quarter of the previous fiscal year, continuing below the previous year because of the effects of the large increases in crude oil and other import prices. However, after excluding the effects of changes in export and import prices, the domestic demand deflator was up 0.6% from a year earlier, thus confirming the spread of inflationary pressures in the domestic economy.

(b) From Recovery to Recession

Growth rates calculated over the same quarters of the previous year, which provide a clearer view of trends in the economy, show that the deceleration in the Japanese economy has continued for more than a year (Exhibit 1). As a result of the slowdown in the world economy, centered around the United States, the pace of expansion in Japan's exports has slowed and capital investment has weakened, influenced by deterioration in corporate profitability. In addition, the effects of the deceleration in the corporate sector have spread to the household sector because of restraints on corporate personnel costs and increases in sales prices. Moreover, nominal growth has now shown negative growth for two consecutive quarters; its weakness is even more pronounced than the slowdown in real growth, and this is in part due to the spreading effects of the run-up in prices of crude oil and other raw materials.

Signs of an economic downturn have also emerged in indexes of industrial production and the business condition indexes, which are more sensitive to trends in the economy. The index of industrial production in the April-June quarter fell a marginal 0.8% from the previous quarter, but this was the second consecutive quarter of decline. Past examples indicate that two consecutive quarters of decline are a sign of an economic downturn, and views are growing stronger, that this time also, the economy is moving into recession. In addition, the business condition coincident index (composite index (CI)), which shows overall trends in the economy, has been on a downward trend since fall 2007, and the government's outlook has indicated the possibility of a downturn.



Nevertheless, even if the economy is moving into a downward trend, it has not been caused by the factors that have caused recessions in the past, such as the need for adjustments in inventory buildups, excess capital stock, or inflation due to overheating of the economy. For this reason, it seems unlikely that the economy will slip sharply into recession due to the adjustment process on the one hand, but, on the other, it is difficult to predict when the economy will recover when the adjustments are completed.

(2) Changes in the Environment Surrounding the Japanese Economy

(a) Evolution in the Growth Mechanism in the Medium Term

Concerns about future economic trends are increasing. This may be because the economy has moved from a recovery phase to a period of slowdown, but concerns are spreading that there may have been changes in the medium-term growth mechanism for Japan and the world economy.

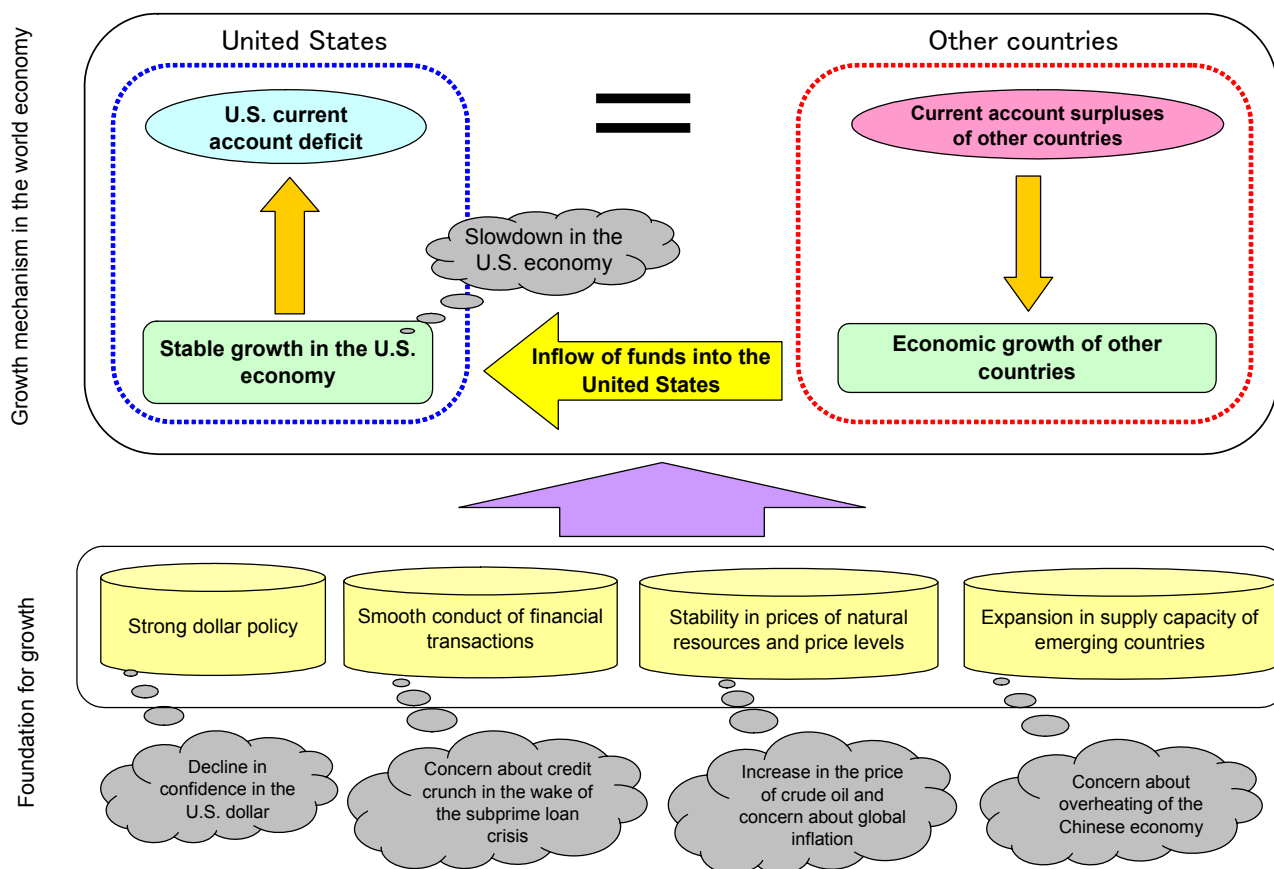
Among factors that have supported high growth in the world economy thus

far, one of the first has been firm expansion in demand in the United States. The U.S. population is growing at about 1% annually, in part because of the inflow of immigrants. In addition, per capita incomes are rising and expansion in consumer spending is driving the economy. To meet rising demand, since U.S. domestic supply capacity is insufficient, imports are essential. The need for imports has been met through industrialization of emerging economies, such as China. From the point of view of the world economy, expanding demand in the United States has been met through expansion in the supply capacity, principally in emerging countries. As a result, this has made rapid growth in the world economy possible, and, as the U.S. current account deficit has increased, countries and regions outside the United States have shown increasing current account surpluses.

It has been pointed out that these current account imbalances cannot continue. However, as the United States has adhered to a strong dollar policy, investments from overseas have flowed into U.S. bonds and stocks, thus creating a continuing recycling of funds back into the United States and thus providing a mechanism for driving world economic growth. In addition, during the first half of the first decade of the 21st century, prices of crude oil and other resources were relatively low. Even after these prices began to rise in recent year, prices of industrial goods have remained stable, as production capacity in the emerging countries has increased. Price stability and the resulting low interest rates made possible high, sustainable growth rates in the world economy.

Now, however, the outlook for this growth mechanism in the world economy has become cloudy and distortions are appearing. Concerns are mounting about a range of issues that may impede growth of the global economy. These include the slowdown in the world economy, especially in the United States; the sharp rises in prices of crude oil and other resources and global inflationary pressures; and the turmoil in world financial markets in the wake of the subprime loan crisis (Exhibit 2).

Exhibit 2: Growth Mechanism in the World Economy and Emergence of Uncertainties and Distortions



(b) More Difficult for Japanese Companies to Earn Profits and for Individuals to Earn Higher Incomes

If the growth mechanism in the world economy undergoes change, this will have an influence on growth of the Japanese economy. First, since growth in the international economy has slowed, principally in Europe and the United States, exports, which have provided support for economic recovery thus far, are decelerating and growth in industrial production is slowing.

At the same time, the terms of trade are deteriorating because of the sharp increases in prices of crude oil and other resources, thus putting corporate profits under pressure. In addition, this change is occurring suddenly, thus creating uncertainties about future trends among corporate management. The deterioration of corporate profitability and growing uncertainty about

future trends will both tend to restrain the drive to invest among corporations.

In addition, as the environment for profits worsens, corporations will take measures to restrain personnel costs, including wages, while at the same time pass on increases in their costs to the prices they charge consumers. Therefore, the purchasing power of households will decline, caught in a bind between stagnant incomes and rising prices of goods and services. Since consumers are likely to take stronger steps to cut corners, they will restrain their spending even more.

However, even as corporate profitability deteriorates, certain capital investments are necessary for corporations to increase competitiveness, and capital spending is continuing to be firm. In addition, the increase in consumer prices is gradual and household incomes are rising marginally; consumer spending has, therefore, not shown a significant decline.

Changes in underlying conditions—namely, the deceleration of economies overseas and increases in prices of raw materials—will speed up the flow of income going overseas, thus making it more difficult for Japanese corporations to earn profits and for individuals to earn higher incomes. For corporations, this will mean “being busy but not being profitable,” and for individuals, it will mean “working harder without becoming better off.” Even under these conditions, however, the current state of the Japanese economy is that capital investment is just barely remaining level and consumer spending is maintaining its current levels.

(3) Outlook for the Japanese Economy

(a) Changes in the Economic Environment that Will Determine the Future Course of the Japanese Economy

Since times are not easy for corporations or individuals, will they weather the difficulties they confront, and will the Japanese economy continue to grow? This depends in large measure on what course the changes that have emerged in the world economic environment take going forward.

First, the high world economic growth rate of 5% that continued through 2007 is beginning to slow. It will probably be difficult to attain this level again. However, growth rates in the emerging economies and resource-producing countries, while declining, will remain high, and the world economy as a whole is assumed likely to continue to grow at about 4% annually. In 2001, following the collapse of the IT boom, world economic growth dropped to between 2% and 2.5%, but we believe such a major drop is unlikely this time. The world economic environment will continue to be favorable for the Japanese economy.

Also, looking ahead, resource prices are expected to remain at high levels. Since crude oil prices (West Texas Intermediate (WTI)) will continue in the US\$110 to US\$130 per barrel range, we assume the rate of increase over the previous year will decline. However, even if the increases in resource prices subside upstream, the trend downstream toward passing price increases on to consumers will continue. The transition to the new price structure will be a factor contributing to improvement in profitability for companies positioned upstream, but for companies downstream, it will mean an increase in input costs, and will be a factor putting pressure on profitability.

The profit environment for corporations will continue to be challenging, but even if profits decrease to some degree, the level of profitability will still be relatively high. In addition, the fact that corporations have eliminated excess capital equipment and employment will be factors contributing to stability in corporate activities. Following the end of the era of rapid growth for the Japanese economy in the middle of the 1970s and subsequently, Japanese companies had chronic excess capital equipment and employment, with the exception of Japan's economic bubble years, but in the third recovery period following the bursting of the bubble, these excesses were eliminated as a result of economic recovery. At present, because of the economic slowdown, some companies—principally small and medium-sized enterprises—are experiencing some feeling of excess, but to a much smaller degree in comparison with past periods. Even if the environment for profitability becomes somewhat difficult, we do not believe capital investment will drop sharply as a result of excess capital

equipment.

As higher costs are passed on to companies downstream, these costs will spread to consumer prices, and real incomes of individuals will decline. If inflation rises at the consumer level, this may have a significant adverse impact on consumer spending behavior. However, we believe that the rate of increase in consumer prices over the previous year will not continue to rise higher than 2% but, as crude oil prices settle down, will rise moderately at somewhat above 1%. Rising consumer prices may be viewed as a reason for increasing wages in nominal terms, but this will not lead to the kind of upward spiral that occurred at the time of the first oil crisis, when wages were increased substantially more than the increase in prices; this, in turn, led to additional price increases. If wages are increased in line with the rise in prices, this will not put undue pressure on corporate profitability and will prevent a decline in real wages of consumers, thus leading to firmness in consumer spending.

(b) Outlook for Fiscal 2008 and Fiscal 2009

In fiscal 2008, ending March 31, 2009, as a result of two exogenous shocks—the slowdown in the world economy and the rise in crude oil prices—the fiscal year began with negative growth, for the first time in a year, in the April-June quarter, as previously mentioned. During the rest of fiscal 2008, the economy is expected to go through a process of absorbing these shocks. We are forecasting real economic growth of 1.2% for fiscal 2008. This will be lower than real growth in fiscal 2007, when revisions in Japan's building code caused a substantial drop in private residential investment. In nominal terms, we are looking for growth of 0.9%, which will mean the continuation of positive growth from the previous fiscal year, but by a relatively small margin.

Although the world economy will decelerate, overall growth will be about 4%, led especially by China and other emerging countries. In addition, we expect crude oil prices to remain at a high level, but believe there will be a pause in the sharp oil price rises. For this reason, no additional shocks will restrain the growth of the Japanese economy, and the contribution of the

external sector will continue to be positive. As a result of these factors, the Japanese economy will remain stable during the fiscal year.

Nevertheless, the operating environment for corporate profitability will remain challenging, and there will continue to be little or no growth in individual incomes. As a result of these two factors, growth in private capital and personal consumption will be marginal. In addition, since consumer prices will continue to rise as higher raw material prices are passed on downstream, expansion in consumer spending will be restrained by the erosion of real incomes.

In residential investment, the effects of the changes in the building code have diminished, but the housing market has cooled off as prices have increased. In addition, condominium developers and other suppliers of housing have adopted a more-cautious stance. For this reason, no major rebound in resident investment is expected in fiscal 2008 to follow the marked drop in fiscal 2007. In addition, we are forecasting that cuts in government public works spending will continue because of the continuation of measures to restructure government finances.

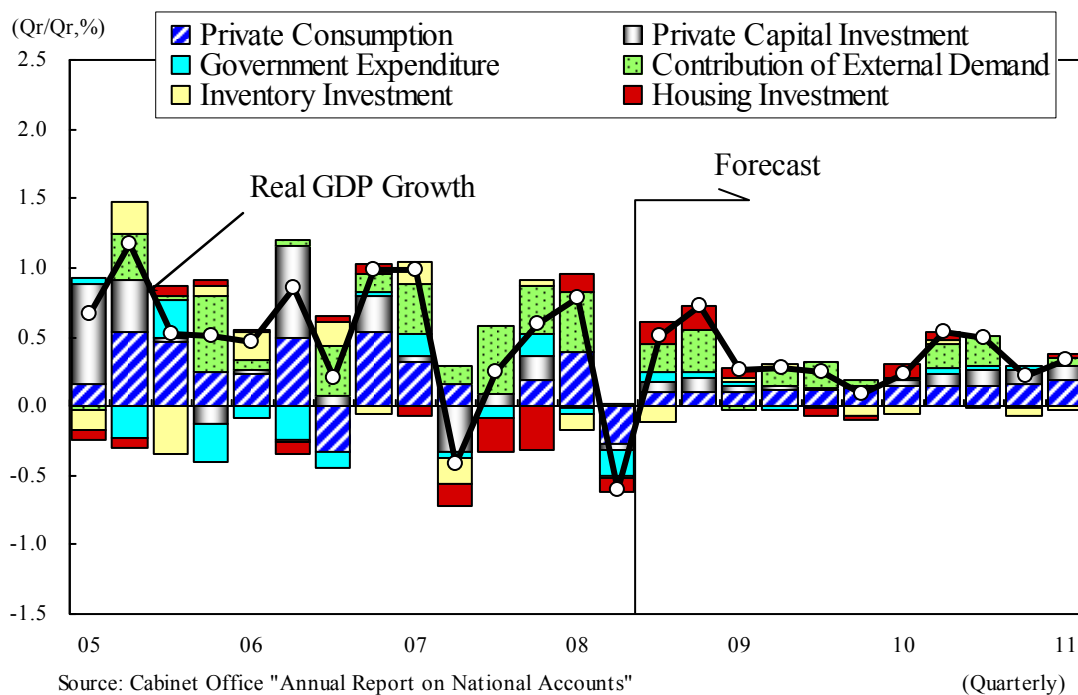
In fiscal 2009, Europe and the United States, which have experienced deceleration in growth, will begin to bottom out; however, on the other hand, the adjustment in oil prices will be completed and they may begin to rise again. However, the basic economic picture will not change from fiscal 2008, as relatively firm economic growth continues in the world economy and raw material prices remain at a high level. Therefore, growth rates will not experience a major decline, but, at the same time, there are no strong reasons suggesting an increase in growth rates. We are forecasting growth in real terms of 1.3% in fiscal 2009, virtually the same as in fiscal 2008.

Note that, since the increase in import prices resulting from the rise in crude oil prices will run its course, the GDP deflator will become positive. At the same time, since imports in nominal terms will settle down, we are looking for relatively high nominal growth of 2.5% in fiscal 2009.

Since raw material prices will settle down at relatively high levels, the pace of growth in exports will rise slightly, and corporate profitability will begin to bottom out. However, private capital investment will not be significantly influenced by fluctuations in corporate profitability and is likely to continue on a moderate upward trend. On the other hand, the increase in consumer prices will settle down at about 1% at an annual rate, but rises in wages will remain moderate. Since real incomes will not change significantly, we are not expecting a strong rate of growth in consumer spending, but believe marginal increases will continue.

In fiscal 2010, the environment surrounding the Japanese economy will not change significantly, and we are forecasting real growth of 1.4% and growth in nominal terms of 2.4%. Consumer spending and private capital investment, the two main pillars of domestic demand, will continue to rise gradually. Along with the recovery in the world economy, we are anticipating steady increases in exports.

Exhibit 3: Real GDP Growth (seasonally adjusted)



(4) Recovery or Recession? That May Not Be the Key Issue

A consensus seems to be emerging that the Japanese economy reached a “peak” in the October-December quarter of 2007 and has now slipped into a downturn. The next issue to receive attention will be when the economy will reach “bottom” and begin to recover. However, we believe that conditions may continue without a clear peak or bottom.

Even though the world economy is slowing, the rate of growth remains at a relatively high level. Although prices of resources will continue to be high, there will be a pause in the sharp increases in these prices experienced thus far. Moreover, while consumer prices may rise, there is not likely to be an inflationary surge. If we assume these conditions will continue, we believe that the Japanese economy, even as it continues to undergo some deceleration, will continue to grow. In addition, if we remind ourselves that the financial positions and earnings structures of Japanese corporations have improved compared with the past, even though the economy may experience a downturn, the adjustment will not be a deep one and the economy is likely to remain on a firm footing.

At the same time, even if the economy manages to continue its present rate of growth, corporations are likely to experience difficulties in generating profits. Also, as we enter an era of some degree of inflation, growth in individual incomes in real terms will continue to be weak. The Japanese economy, therefore, appears likely to remain an environment where it will be difficult for companies to earn profits and for individuals to earn higher incomes.

On the other hand, as economic growth fails to rise to higher levels, some sectors may experience weakness. Individual proprietors and households living on pensions without any income earners are experiencing strong uncertainty about the future, and the decline in their consumption is sharper than the consumption of households supported by regularly employed workers. Also, while it is true that, compared to conditions following the bursting of Japan’s economic bubble, the financial and earnings positions of companies have improved substantially, this applies mainly to large

companies that had ample room for restructuring their operations. Medium-sized, small, and very small enterprises probably do not have much capacity for withstanding the effects of the recent slowdown in the economy and the increase in raw material prices. Moreover, even if the overall growth rate of the economy is boosted by expansion in exports, it will be difficult for regions that have no significant export industries to grow.

These considerations raise a number of structural issues for the Japanese economy that cannot be fully addressed simply by asking whether the economy is recovering or slipping into recession. One of these is that changes are taking place in the underlying conditions that have supported export-led growth in the medium term. Another is that the Japanese economy is confronting deterioration in its terms of trade as a result of sharp increases in prices of resources, making it more difficult for Japanese companies to earn profits and for individuals to earn higher incomes. The feeling is growing that approaches employed thus far will not enable Japan to break through the current impasse.

The previous notion that “the economy is slipping into recession, therefore, an economic policy package is needed,” will not satisfactorily address the issues we are now confronting. To break through the current impasse, we must rely on the know-how and drive of individual companies in the private sector. The roles the government should play are the implementation of measures to create an operating environment that makes it easier for the private sector to move and take initiatives and, at the same time, the implementation of a bare minimum of measures for those sectors that will suffer severely from structural economic changes.

2. Forecasts of Economic Activity by Sector

(1) Corporations

- Corporations have completed their disposal of negative assets left over from Japan's bubble economy, and their financial positions and profitability have recovered substantially. Accordingly, the risks of a major downturn in production, capital investment, or other aspects of corporate activities have receded.
- At present, trends in production have weakened because of slower growth in exports of automobiles, digital-related products (semiconductors and LCDs), and other items as well as a slowdown in private capital investment. As a result of the slackening of demand in Japan and overseas, industrial shipments have weakened, and inventories are rising in some industries. However, compared with the past, companies have implemented improved inventory management systems, and the level of inventories has not reached a level that will require a major adjustment.
- If production stalls temporarily, as a result of the slowdown in overseas economies and the inventory adjustment in digital-related products, and this leads to a weakening of corporate earnings, this will restrain expansion in capital investment. At present, there are movements in progress to implement such adjustments, but, in the medium term, the upward trend in production will continue and capital investments for installing new equipment and maintaining competitiveness through enhancing the value added of products will be necessary. Therefore, the slowdown in capital investment is expected to be mild and the upward trend will continue.
- As a result of the improvement in corporate profitability and recovery in the economy, recurring profit among corporations has already exceeded the previous peaks, reached during Japan's bubble economy and the IT boom, and has continued to set new records. Although certain factors are causing a deterioration in the corporate profit environment, including the run-up in raw material prices, increases in personnel costs, and rising depreciation charges, companies were still able to report increases in profits because of gains in sales in Japan and

overseas. Recently, however, the rise in raw material costs has become increasingly severe, and trends toward deceleration in the world economy have become more widespread. As a result, corporate profitability has begun to decline; however, as these various factors settle down, the upward trend in profitability is expected to resume.

(2) Households

- Household incomes are continuing to rise, but the pace of increase is gradual. On the other hand, prices are rising at a faster rate, and households are beginning to feel the burden. For this reason, the increase in consumer spending has paused.
- The employment environment—which had improved along with the recovery in the economy, the retirement of members of the baby-boom generation, and other factors—is now weakening as shown by increases in the ratio of unemployed persons and other factors. Going forward, the population of labor force age individuals will reach a ceiling, and growth in the number of persons employed will slow. The employment environment is expected to gradually become more severe.
- Wages, which had been stagnant, are continuing to show marginal increases, principally in the regular wage category, reflecting the increase in consumer prices. However, because of the decline in household purchasing power as a result of rising prices, increases in consumer spending are expected to be restrained.
- In the area of residential investment, although the sons and daughters of the baby-boom generation are now purchasing their first homes, a number of factors, in addition to the slowing of growth in the number of households in the medium term, are expected to restrain growth in housing investment in the years ahead. These include the delays in the start-up of construction of condominiums and large-scale housing projects caused by the implementation of revisions to Japan's building code in June 2007, rising costs of housing because of higher land prices in urban areas and the run-up in material costs, and other factors.

(3) Government

- Following the bursting of Japan's economic bubble, the structure of government finances deteriorated rapidly and the public sector has continued to issue a large volume of government bonds. Along with the decline in nominal economic growth rates, the government made major reductions in taxes that have resulted in a drop in tax revenues. Moreover, on the expenditure side, as the population has aged demographically, social welfare costs have risen, and, as a result of the implementation of major government spending programs to stimulate the economy in the 1990s, expenditures for public works increased
- After the year 2000, because of the government's goal of making structural reforms in its finances, spending on public works was reduced, and no major spending programs to stimulate the economy were implemented. Moreover, local governments have also continued to reduce their spending on public works because of their own financial difficulties. Along with the economic recovery, tax revenues began to expand again, but the government has basically continued policies for making structural reforms in its finances. Accordingly, on an annual basis, further cuts in public works spending are expected to continue at the national and local levels.
- To reduce its fiscal deficit, the government is working to restrain its expenditures through systemic reforms to control government final consumption expenditures, including social welfare expenses. However, even if these reforms are implemented, they will probably only succeed in lowering the pace of expansion in these expenditures. In addition, the administration of Prime Minister Yasuo Fukuda appears to be moving backward on some reforms. We anticipate that the government's final consumption expenditures, principally social welfare payments, will continue to increase.
- Reductions in public-sector capital formation, at both the national and local levels, are continuing, and the ratio of these public investments to GDP has declined substantially. For this reason, concern is mounting that Japan may not be able to sustain necessary social capital if cuts in public-works investments continue. The financial positions of national and local governments remain weak, and the decline in public-sector

investment spending is expected to continue, but there is a possibility that the pace of decline may be more moderate going forward.

(4) Trends in Overseas Economies

- The world economy is continuing on an expansionary trend. Although the economies of Europe and United States are experiencing a temporary slowdown, growth in the emerging economies is pushing world growth rates upward. The risks seem remote for a reemergence of concerns about the management of financial institutions in Europe and the United States or a downturn in the world economy as a whole because of a “hard landing” involving a collapse in the value of the U.S. dollar. However, there are a number of concerns going forward, including overheating in the economies of the emerging countries, including China, and the increase in price of oil. There is also a possibility that rising consumer prices in countries around the world could dampen economic performance.
- Even if a temporary slowdown occurs, the world economy is expected to continue to expand, and the rising trend in Japan’s exports will continue. The expansion in the overseas production of Japanese companies will be one factor restraining exports, but we are forecasting that demand for exports from Japan will expand because of growth in the emerging economies and resource-producing nations, and expanding demand for electronic parts, principally in the rest of Asia.
- The rate of growth in Japan’s real imports is smaller than the rate of growth in real exports, but real imports are on an upward trend. Although growth in Japan’s domestic demand will be moderate, production capacity in China and other emerging economies will expand, and since Japanese companies will proceed with their strategies of the international division of production, Japan’s imports of products and parts, mainly from Asia, will expand. In addition, plateauing of the prices of primary products at high levels will push the value of imports upward.
- We are expecting continued growth in both Japan’s exports and imports, as the trade dependence of the Japanese economy continues to increase. Net exports will continue to make a positive contribution to Japan’s

economic growth. Moreover, reflecting the overseas expansion of Japanese companies, dividends and other income from their overseas subsidiaries are expanding, and income from monetary assets held overseas is also increasing. As a result, Japan's surplus in the income accounts of its balance of payments has already exceeded the levels of the country's trade surplus.

3. Forecasts for Prices and Financial Markets

- At present, increases in prices of crude oil and other raw materials, including metals, have paused, but they remain at higher levels than in past. On the other hand, the supply capacity of China and other emerging economies is expanding, and, because of this and other factors, prices of industrial products are being held in check, with inflationary pressures upstream and deflationary pressures downstream continuing.
- Rising prices of raw materials are also having an impact on Japan's domestic prices. There is evidence that basic materials industries, in particular, are working to shift the rise in their costs to their final product prices, and domestic corporate goods prices are increasing at a faster pace. There are also signs that higher costs are being passed on to consumers, principally in the fields of energy and food products, and, as a consequence, consumer prices are trending upward.
- Regarding monetary policy, following the lifting of the quantitative policy of monetary easing in March 2006 and the ending of the zero-interest rate policy in July, a further increase in interest rates was implemented in February 2007. The process of normalizing monetary policy to raise interest rates from their excessively low levels and permit the interest rate mechanism to operate properly has begun. However, as a result of the turbulence in financial markets created by the subprime loan issue, policy interest rates have been left unchanged because of the risk of downtrends in the domestic and overseas economies. The turbulence in financial markets is subsiding, and, when uncertainties in domestic and overseas economies recede, we believe further slight increases in interest rates will resume.

- Long-term interest rates are expected to rise moderately along with the economic recovery and the resumption of increases in policy interest rates. Stock prices appear to be relatively undervalued, but when financial markets regain stability, we expect they will rise. In foreign exchange markets, beginning in the latter half of 2007, the U.S. dollar has lost value against the yen because of substantial reductions in U.S. interest rates and market uncertainty. However, despite the rise in Japan's current account surplus, yen appreciation has not gained momentum when viewed from a longer time span. In addition, the currencies of emerging economies are continuing to appreciate gradually against the yen and the U.S. dollar. The increase in the value of the euro has been checked, and the currencies of resource-producing countries are now moving in tandem with resource prices. Economic conditions in the three major economic centers of Japan, the United States, and Europe tend to be linked, and we are basically looking for stability among the currencies of these three regions.

Exhibit 4: Outlook for Fiscal 2008-2010

	FY2006 (actual)	FY2007 (actual)	Forecast ↘			Yr/Yr, %
			FY2008 (forecast)	FY2009 (forecast)	FY2010 (forecast)	
Nominal GDP	1.7	0.6	0.9	2.5	2.4	
Real GDP	2.5	1.6	1.2	1.3	1.4	
Contribution of domestic demand	1.7	0.3	0.2	0.8	1.0	
Private consumption	1.8	1.4	0.5	0.8	1.0	
Housing investment	0.2	-13.3	-0.5	4.2	3.3	
Private capital investment	5.6	-0.1	1.2	1.0	2.0	
Contribution of inventory investment	0.2	-0.0	-0.1	0.0	-0.1	
Government expenditure	-1.8	0.2	-0.4	0.1	0.3	
Public investment	-9.1	-1.8	-5.3	-3.1	-3.0	
Government final consumption expenditure	0.1	0.7	0.7	0.9	1.0	
Contribution of external demand	0.8	1.2	0.9	0.5	0.4	
Export of goods and services	8.4	9.5	3.8	4.8	4.0	
Import of goods and services	3.1	2.1	-1.6	2.4	2.0	
GDP deflator	-0.8	-1.0	-0.2	1.2	1.0	

	FY2006 (actual)	FY2007 (actual)	Forecast ↘			Yr/Yr, %
			FY2008 (forecast)	FY2009 (forecast)	FY2010 (forecast)	
Current account balance (trillion yen)	21.2	24.5	22.5	28.7	32.9	
balance on goods (trillion yen)	10.5	11.7	9.8	14.6	17.8	
balance on service (trillion yen)	-2.3	-2.6	-2.3	-2.5	-3.0	
balance on income (trillion yen)	14.2	16.8	16.2	17.8	19.3	
Industrial production	4.6	2.6	-0.6	0.8	1.0	
Unemployment rate(%)	4.1	3.8	4.1	4.2	4.3	
New housing starts(annualized, ten thousand units)	128.5	103.6	111.5	113.1	114.1	
Domestic corporate goods prices	2.0	2.2	5.0	2.0	2.2	
Consumer prices	0.3	0.2	1.5	1.1	1.2	
excluding freshfood	0.1	0.3	1.5	1.1	1.2	
Yen/U.S.Dollar	116.9	114.2	108.1	112.3	113.9	
Uncollateralized call rates (O/N) (%)*	0.209	0.502	0.500	1.000	1.500	
Newly issued government bond yields (10years) (%)	1.77	1.60	1.58	1.70	1.90	
WTI future price (near month contract, US dollar/barrel)	64.9	82.2	117.2	116.3	124.5	
Dubai crude oil prices (US dollar/barrel)	60.9	77.3	112.6	112.8	121.0	

* actual=average, forecast=end of period

Exhibit 5: Outlook for Calendar 2008-2010

	Forecast					Yr/Yr, %
	CY2006 (actual)	CY2007 (actual)	CY2008 (forecast)	CY2009 (forecast)	CY2010 (forecast)	
Nominal GDP	1.4	1.3	0.2	2.8	2.1	
Real GDP	2.4	2.1	1.2	1.3	1.2	
Contribution of domestic demand	1.6	0.9	0.1	0.8	0.8	
Private consumption	2.0	1.5	0.8	0.6	1.0	
Housing investment	0.9	-9.5	-6.9	6.5	2.7	
Private capital investment	4.3	2.1	0.6	1.1	1.4	
Contribution of inventory investment	0.2	0.1	-0.2	0.0	-0.1	
Government expenditure	-2.0	0.1	-0.3	0.1	0.2	
Public investment	-8.1	-2.5	-4.3	-3.8	-3.2	
Government final consumption expenditure	-0.4	0.7	0.6	1.0	0.9	
Contribution of external demand	0.8	1.1	1.2	0.5	0.4	
Export of goods and services	9.7	8.6	6.3	3.9	4.4	
Import of goods and services	4.2	1.8	-0.3	1.1	2.6	
GDP deflator	-1.0	-0.8	-1.0	1.4	0.9	

	Forecast					Yr/Yr, %
	CY2006 (actual)	CY2007 (actual)	CY2008 (forecast)	CY2009 (forecast)	CY2010 (forecast)	
Current account balance (trillion yen)	19.8	24.8	21.2	28.0	31.6	
balance on goods (trillion yen)	9.5	12.3	8.8	14.3	16.9	
balance on service (trillion yen)	-2.1	-2.5	-2.4	-2.3	-2.9	
balance on income (trillion yen)	13.7	16.3	16.2	17.3	18.8	
Industrial production	4.5	2.8	0.0	0.7	0.8	
Unemployment rate (%)	4.1	3.9	4.0	4.1	4.2	
New housing starts(annualized, ten thousand units)	129.0	106.1	111.4	113.0	113.9	
Domestic corporate goods prices	2.2	1.7	5.1	2.2	2.2	
Consumer prices	0.2	0.0	1.4	1.2	1.1	
excluding freshfood	0.1	0.0	1.5	1.1	1.2	
Yen/U.S.Dollar	116.3	117.8	106.9	111.6	113.4	
Uncollateralized call rates (O/N) (%)*	0.113	0.472	0.500	0.750	1.250	
Newly issued government bond yields (10years) (%)	1.74	1.68	1.52	1.66	1.85	
WTI future price (near month contract, US dollar/barrel)	66.2	72.3	114.2	113.8	123.0	
Dubai crude oil prices (US dollar/barrel)	61.6	68.4	108.8	110.3	119.5	

* actual=average, forecast=end of period

Exhibit 6: Outlook for 2008-2009 (Quarterly)

	Forecast												Qr/Qr, %
	FY2007				FY2008				FY2009				Yr/Yr, %
	4-6	7-9	10-12	1-3	4-6	7-9	10-12	1-3	4-6	7-9	10-12	1-3	
Nominal GDP	-0.5	0.0	-0.1	0.2	-0.7	0.8	1.4	0.9	0.4	0.5	0.1	0.5	
	1.3	1.1	0.3	-0.3	-0.6	0.1	1.6	2.4	3.5	3.3	1.9	1.5	
Real GDP	-0.4	0.2	0.6	0.8	-0.6	0.5	0.7	0.3	0.3	0.2	0.1	0.2	
	1.8	1.7	1.6	1.2	1.0	1.3	1.4	0.9	1.9	1.5	0.9	0.8	
Contribution of domestic demand (Qr/Qr,%)	-0.6	-0.2	0.3	0.3	-0.6	0.3	0.4	0.3	0.2	0.1	0.1	0.2	
Private consumption	0.3	0.0	0.3	0.7	-0.5	0.2	0.2	0.2	0.2	0.2	0.2	0.3	
	1.3	1.7	1.2	1.4	0.6	0.7	0.6	0.1	0.8	0.8	0.8	0.9	
Housing investment	-4.3	-7.3	-9.8	4.3	-3.4	5.3	5.4	2.0	0.0	-2.0	-1.0	2.9	
	-2.9	-11.5	-21.7	-16.6	-15.6	-4.5	11.7	9.4	13.4	5.4	-1.0	0.0	
Private capital investment	-2.1	0.6	1.1	-0.1	-0.2	0.5	0.6	0.3	0.2	0.1	0.1	0.3	
	0.1	0.3	0.0	-0.7	1.3	1.3	1.0	1.1	1.5	1.1	0.8	0.7	
Contribution of inventory investment (Qr/Qr,%)	-0.2	0.0	0.0	-0.1	0.0	-0.1	0.0	0.0	0.0	0.0	-0.1	-0.1	
Government expenditure	-0.2	-0.4	0.8	-0.2	-0.9	0.4	0.2	0.1	-0.1	0.0	0.0	0.0	
	0.0	0.1	0.8	0.1	-0.7	0.0	-0.7	-0.3	0.6	0.3	-0.1	-0.2	
Public investment	-2.6	-2.0	0.1	1.0	-5.2	0.2	-0.5	-0.6	-0.9	-0.9	-1.2	-0.7	
	-2.8	-0.5	-1.8	-2.0	-6.9	-4.6	-4.8	-5.4	-2.2	-3.1	-3.6	-3.2	
Government final consumption expenditure	0.2	0.1	0.9	-0.5	0.1	0.5	0.3	0.3	0.1	0.2	0.2	0.2	
	0.4	0.3	1.4	0.6	0.5	1.0	0.4	1.1	1.1	0.9	0.8	0.6	
Contribution of external demand (Qr/Qr,%)	0.1	0.5	0.3	0.4	0.0	0.2	0.3	0.0	0.1	0.2	0.0	0.0	
Export of goods and services	1.9	2.6	2.7	3.4	-2.3	0.9	1.7	0.7	1.4	1.4	1.0	0.9	
	7.8	8.6	10.4	11.1	6.4	4.6	3.6	0.9	4.8	5.3	4.6	4.8	
Import of goods and services	1.2	-0.3	0.8	1.2	-2.8	-0.2	0.1	0.8	0.8	0.5	0.9	0.9	
	1.4	1.5	2.3	3.1	-1.3	-1.1	-1.8	-2.1	1.1	2.2	3.0	3.1	
GDP deflator (Yr/Yr,%)	-0.5	-0.6	-1.3	-1.5	-1.6	-1.1	0.2	1.5	1.6	1.7	1.0	0.7	

	Forecast												Yr/Yr, %
	FY2007				FY2008				FY2009				
	4-6	7-9	10-12	1-3	4-6	7-9	10-12	1-3	4-6	7-9	10-12	1-3	
Current account balance (trillion yen)*	6.4	6.3	6.2	5.6	4.8	4.8	6.2	6.7	7.5	7.0	7.3	7.3	
balance on goods (trillion yen)*	3.1	3.3	3.0	2.3	1.7	1.8	2.5	3.4	3.4	3.5	4.0	3.8	
balance on service (trillion yen)*	-0.6	-0.6	-0.7	-0.7	-0.6	-0.6	-0.5	-0.6	-0.5	-0.5	-0.7	-0.7	
balance on income (trillion yen)*	4.3	4.0	4.2	4.3	4.0	4.3	3.8	4.4	5.1	4.8	4.2	4.8	
Industrial production (Qr/Qr, %)	0.6	1.7	0.9	-0.7	-0.8	-1.0	0.9	0.5	0.1	0.2	0.0	0.2	
(Yr/Yr, %)	2.3	2.6	3.3	2.3	1.0	-1.9	-1.4	-0.5	0.6	1.6	1.0	0.5	
Unemployment rate (%)*	3.8	3.8	3.8	3.8	4.0	4.1	4.1	4.1	4.1	4.2	4.1	4.2	
New housing starts(annualized, ten thousand units)	125.4	80.9	95.5	114.2	111.7	110.6	110.4	114.7	113.5	112.2	112.6	115.6	
Domestic corporate goods prices (Yr/Yr,%)	1.7	1.6	2.3	3.4	4.8	7.1	4.9	3.1	2.4	1.8	1.8	2.0	
Consumer prices (Yr/Yr,%)	-0.1	-0.2	0.5	0.9	1.4	1.8	1.5	1.3	1.2	1.1	1.0	1.0	
excluding freshfood (Yr/Yr,%)	-0.1	-0.1	0.5	1.0	1.5	1.8	1.5	1.3	1.2	1.1	1.0	1.0	
Yen/U.S.Dollar	120.7	117.8	113.1	105.2	104.5	108.3	109.5	110.3	111.3	112.0	112.8	113.0	
Uncollateralized call rates (O/N) (%)**	0.514	0.497	0.493	0.506	0.507	0.500	0.500	0.500	0.500	0.750	0.750	1.000	
Newly issued government bond yields (10years) (%)	1.74	1.72	1.56	1.39	1.61	1.55	1.55	1.60	1.60	1.70	1.75	1.75	
WTI future price (near month contract, US dollar/barrel)	65.0	75.4	90.7	97.9	124.0	123.0	112.0	110.0	112.0	115.0	118.0	120.0	
Dubai crude oil prices (US dollar/barrel)	64.8	70.0	83.3	91.2	116.9	119.0	108.0	106.5	108.5	111.5	114.5	116.5	

*seasonally adjusted ** actual=average, forecast=end of period