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Forecast for the Japanese Economy in Fiscal 2008 and 2009

**— Will Japan's Longest Postwar Recovery Be Followed
by Its Longest Postwar Downturn? —**



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1. Outlook for the Japanese Economy in Fiscal 2008 and Fiscal 2009

-- Will Japan's Longest Postwar Recovery Be Followed by Its Longest Postwar Downturn?

(1) Current State of the Economy

The economy is continuing on a downward trend. The rate of growth in real terms in the July-September quarter was a relatively small minus 0.1%, compared with the previous quarter, but this figure represented the second consecutive quarter of negative growth, while growth was also negative in nominal terms.

By demand component, exports are losing their momentum as a result of the effects of the slowdown in the world economy. Partially in reaction to the major drop in the previous quarter, exports in the July-September quarter made a comeback, but the deceleration of overseas economies, especially those in Europe and the United States, is causing a deterioration in the export environment. Moreover, as a result of an increase in imports, the contribution of net exports to growth was minus 0.2%, which represented the second consecutive quarter of negative contributions to growth.

The slowdown in exports is beginning to have an impact on the domestic economy. The contribution of domestic demand to growth was 0.1%, which, while barely positive, was hardly robust. Industrial production, which is correlated with exports, declined for the third consecutive quarter during the July-September period, and the drop in demand is leading to a deterioration in the conditions for corporate profitability. Also, in part because of growing uncertainty about future trends, private capital investment declined 1.7%, for its third consecutive quarterly decrease.

Although private consumption showed a major drop in the previous quarter, in part because of a reaction to the contribution of the extra day due to leap year in the January-March quarter, it posted a quarter-to-quarter increase of 0.3% in the July-September quarter. This margin of increase was relatively small, however, reflecting the weakness in income growth, rising prices,

the trend toward greater thriftiness, and other factors. In addition, private residential investment—partially in reaction to the sharp drop in the previous quarter—rose a relatively large 4.0% in the July-September quarter, but the underlying trends continue to be quite weak as housing prices are rising.

Comparisons with the same quarter of the previous year, which give a clearer picture of economic trends, show that nominal growth has been negative since the beginning of the year, and growth in real terms in the July-September quarter turned negative for the first time in 25 quarters. The increase in imports due to higher prices of crude oil and raw materials has reduced growth in nominal terms. This factor has now been joined by deceleration of exports along with the slowing of the world economy, and this, in turn, is having a negative effect on private capital investment and consumer spending. As a result, the decline in real growth has become clear.

(2) Outlook for the Economy

① Previous Downturns

How long with the current downturn last? According to data prepared by Japan's Cabinet Office, with a base date of June 1951, the average length of downturns thus far has been 16 months. In most cases, the downturns have ended in somewhat less than 12 months to about 18 months, and recovery has begun thereafter. If the average case is applicable this time, the economy should bottom out around the middle of 2009, and recovery should begin thereafter.

If we select from cases where recessionary conditions were prolonged, one example would be the period following the collapse of Japan's bubble economy, which extended 32 months, from February 1991 through October 1993. At that time, companies were burdened with excessive production capacity, excessive employment, and excessive debt. The post-bubble recession was prolonged by these "excesses," which resulted in deterioration in corporate profitability and a decline in capital investment.

An even longer recession than the one following the collapse of the bubble economy began after the second oil crisis. That downturn lasted 36 months, from February 1980 through February 1983. The burden represented by the simultaneous global recession triggered by the second oil crisis made it quite difficult for the economy to reach the recovery stage.

Fortunately, this time no “bubbles” have emerged in the domestic economy, and conditions in the economic environment are different from those during the recession that followed the bursting of Japan’s economic bubble in the early 1990s. Notwithstanding that, a number of bubbles have emerged in other parts of the world, including those in the housing and natural resource sectors. We might say that the Japanese economy enjoyed the benefits of bubbles elsewhere and was able to expand its exports as well as experience the longest period of recovery during the postwar period. As these bubbles burst and the world economy slows, it is possible that these events could bring a long period of adjustment in the Japanese economy. The current financial crisis has emerged as a result of the bursting of bubbles in certain sectors, and, if, as a result, signs of a simultaneous worldwide recession become stronger, this may result in the longest recession in the postwar period, similar to the downturn that followed the second oil crisis. In the next section, we look at three points that will be important in determining how long the current downturn will last.

② Three Key Points in Considering Future Trends

(a) Sudden Deceleration in the World Economy

The pace of deceleration in the world economy is increasing rapidly, and the words “simultaneous global recession” are being used more and more frequently. In the United States, along with the sharp drop in private residential investment, consumption and capital investment are slowing, thus bringing negative growth in recent periods. The impact of the credit crunch is spreading, especially in the household sector, as evidenced by the sudden drop in automobile sales. Moreover, in Europe, where the housing boom has ended, just as in the United States, and exports to newly emerging industrializing countries are slowing, there are clear signs of an

economic downturn. The deceleration in the world economy, especially in Europe and the United States, is causing deterioration in the export environment and bringing slower growth in the newly emerging economies.

However, even if the world economy is slowing, it is questionable whether growth in the global economy will drop to only 1% or 2% annually for three years, as it did during the simultaneous worldwide slowdown in the early years of the 1980s. The key in this case will be trends in the newly emerging economies. The stagnation in the economies of Europe and the United States will, without question, bring slower growth in the emerging economies, but, on the other hand, we cannot ignore the rise in the endogenous growth potential of these economies, which is supported by the increase in their income levels. In addition, in China, the government will adopt economic stimulus measures totaling about 4 trillion yuan that will provide support for economic growth, which had begun to decline.

Nevertheless, doubts remain about the extent to which the increase in the economic growth rate in China that will result from expansion in public works investment there will bring an increase in exports to China from Japan, because the percentage of exports to local plants in China of materials for parts and other items as well as other producers' goods is high. However, these measures will be positive for the Japanese economy since they are expected to prevent a major weakening in China's economic activity as a whole and will, therefore, avert a sudden deceleration in the Chinese economy.

(b) Drop in Crude Oil Prices

The settling down of inflation in prices of crude oil and other raw materials is a positive development for the Japanese economy. The rise in oil prices, which thus far has placed pressure on corporate profitability and was the main reason why Japan showed a deficit in its international trade accounts in August 2008, has paused, and prices have recently fallen about 60% from their peak levels. As a result of declines in prices of oil and other imported raw materials, Japan's terms of trade (export prices/import prices), which had been on a downtrend, have now begun to show improvement.

As the outflow of income to resource-exporting countries subsides, this will, first of all, bring improvement in corporate profitability and will be a positive development for capital investment. Also, if the decline in input prices leads to reductions in product prices, the rise in consumer prices will also settle down. Or, on the other hand, if wages are increased along with the improvement in profitability, household purchasing power will rise. In any event, these developments will be factors supporting increases in household consumption.

If the deceleration of the world economy is a factor behind the drop in oil prices, then we definitely cannot feel secure about developments going forward. Improvement in Japan's terms of trade will help to create an environment for a bottoming out in the Japanese economy, but, for the economy to actually recover, a necessary condition will likely be an increase in demand, or, more specifically, expansion in exports as a result of recovery in the global economy. However, we should probably view being set free from anxiety about how high oil prices will climb and seeing a decline in the likelihood of a stagflation scenario (where economic stagnation would go hand in hand with inflation) as positive developments.

(c) Signs of Financial Instability in Japan

Recently, however, a new cause for concern has emerged. That is whether there might be a credit contraction in Japan such as those experienced recently in other countries. The number of bankruptcies is increasing, along with the incidence of business failures involving substantial amounts of debt. Along with this, the volume of nonperforming assets on the balance sheets of financial institutions is rising. Although the nonperforming asset problems experienced previously have not reemerged, we must pay attention to trends going forward.

Incidents of bankruptcies caused by deterioration in company financial positions and resulting cash shortages are also emerging. According to the Bank of Japan's *Short-Term Economic Survey of Enterprises in Japan*, the financial position diffusion indices (which measure financial position of enterprises by subtracting the number of "tight" responses in the survey from the number of "easy" responses) are showing signs of deterioration.

According to responses from small and medium-sized companies, the number of “tight” responses has exceeded the number of “easy” responses even during the recently ended prolonged period of recovery and is continuing to rise. On the other hand, among large corporations, there are still many companies responding that their financial positions are “easy,” but the difference between the number of “easy” and “tight” responses is shrinking. Taking these trends into account, the government’s planned additional economic policies, entitled “Livelihood Measures,” include expansion in the credit guarantee allocation offered to businesses by the National Federation of Credit Guarantee Corporations and an increase in the lending allocation of government financial institutions.

In addition, Japanese financial institutions are reporting losses in connection with subprime loan related assets, and the substantial decline in stock market prices is one of the factors that has reduced the capital ratios of financial institutions. Large financial institutions are already planning to increase their capital base through the issuance of additional shares. In addition, there are plans for introducing a scheme for providing infusions of capital from public funds, mainly into regional financial institutions, under the revised law providing for strengthening the functions of financial institutions, which is currently under consideration by the Japanese Diet. Maximum attention and appropriate action will be necessary to prevent the emergence of processes that might lead to a deterioration in the economy as a result of a credit contraction.

(3) Outlook for Fiscal 2008 and Fiscal 2009

In fiscal 2008, as a result of the effects of two exogenous shocks, namely the deceleration in the world economy and the sharp rise in oil prices, negative growth continued during the first half. In the second half, the economic downturn is expected to continue, and negative growth in real terms of 0.6% is forecast for the full fiscal year for the first time in seven years, along with negative growth in nominal terms of 1.3% for the first time in six years.

Following the run-up in oil prices, prices peaked in the summer and began to decline. The trend toward economic deceleration has spread from the United States, which was the epicenter of the subprime loan crisis, to Europe, which has experienced a housing bubble similar to that of the United States, then to China and other emerging economies. As signs of a simultaneous global recession have grown, Japan has been confronted with a weakening of its exports, while trends in other economic activities, including capital investment and household consumption, have become weakened.

In the latter half of the fiscal year, the deceleration in the world economy will become even more pronounced, and the environment for exports from Japan will become substantially tougher. Along with the decrease in exports, the pace of decline in industrial production will also quicken, and the outlook is for the first full year-to-year decline in production in seven years. The marked declines in prices of oil and other raw materials will have a positive impact on corporate profitability, but, as a result of the weakness in sales, especially exports, companies are likely to report their second consecutive year of declining profits. As a result of the deterioration in profitability and growing uncertainty about future trends, companies are reviewing their capital investment plans. Therefore, capital investment, which had already shown a slight decline in the previous fiscal year, is forecast to show a second consecutive annual drop in fiscal 2008.

As corporate profitability deteriorates, increasing wages will become more difficult. The number of employed persons is continuing to decline, thus contributing to a worsening in the household income environment. Consumer prices, which had shown signs of increasing by larger margins, will settle down, and this will have a positive effect on consumer spending. However, since growth in nominal incomes will continue to be lackluster, consumer spending is expected to remain virtually unchanged from the previous fiscal year. Housing investment is forecast to show a further decline in fiscal 2008. Although the adverse effects of revisions in Japan's building codes have diminished, the housing market remains in a downturn as prices have risen, and suppliers of housing, including condominium developers, are adopting a cautious stance.

In fiscal 2009, we are forecasting that there will be no major changes in the environment surrounding the Japanese economy and that the economic downturn will continue. In real terms, we are forecasting negative growth of 0.3% in real terms for the second consecutive year; however, in nominal terms we are expecting expansion of 1.1%. The decline in prices of oil and other imports will push the GDP deflator upward and decrease imports in nominal terms, thus resulting in higher growth in nominal GDP.

We are assuming that the turmoil in world financial markets will gradually subside, as a result of the cooperative policies adopted by countries around the world and other factors; however, growth in the world economy will continue to be low, as in fiscal 2008. As a consequence, Japan's exports will not show a clear recovery trend, and we are forecasting a decline in exports for the fiscal year. Imports are also expected to decline, but the positive contribution of the external sector will drop significantly and become almost neutral.

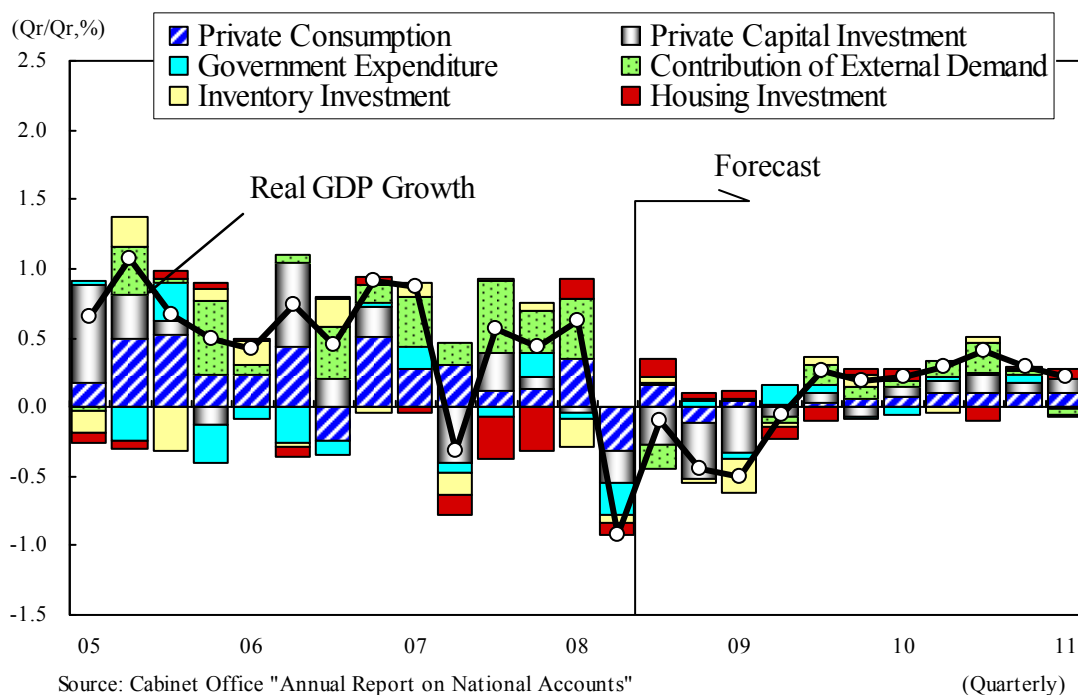
As exports remain weak, industrial production will continue on a downward trend and show a second consecutive year of decline. Conditions for corporate profitability will remain challenging, and recurring profit is forecast to decline for the third consecutive year. Since production will continue to decrease and the profit environment will remain difficult, conditions for recovery in private capital investment will not be favorable. We are therefore forecasting that investment will continue to decline from the previous fiscal year.

The outlook calls for distribution of lump-sum grants from the Japanese government to consumers, which will total about ¥2 trillion, and the start-up of the largest-ever tax relief measures to encourage residential investment. However, the positive impact of these measures on consumption and housing investment will probably be marginal. As the profit environment for corporations remains challenging, the employment environment is likely to continue to deteriorate, with wages and bonuses remaining on a downward trend. The income environment will remain difficult, and consumer spending will probably barely hold its own at the previous year's levels. Moreover, the desire to purchase homes will remain

weak, and housing suppliers will continue to adopt a cautious stance, thus resulting in the third consecutive year of decline in housing investment.

In fiscal 2010, the growth rate of the world economy, which had been declining previously, will accelerate again, and the increase in exports will bring a trend toward the bottoming out and recovery in the Japanese economy. Consumer spending and capital investment are forecast to show gradual expansion. Real growth is forecast to rise to 1.1%, and growth in nominal terms will amount to 0.6%.

Exhibit 1: Real GDP Growth (seasonally adjusted)



2. Forecasts of Economic Activity by Sector

(1) Corporations

- Corporations completed their disposal of negative assets left over from Japan's bubble economy, and their financial positions and profitability have recovered substantially since 2000. Accordingly, the risks of a major downturn in production, capital investment, or other aspects of corporate activities have receded.
- At present, however, production is declining because of slower growth in exports of automobiles, digital-related products (semiconductors and LCDs), general machinery, 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. Although inventories have not reached a level that will require a major adjustment in production, the monitoring of trends will be necessary going forward.
- As a result of the deceleration in the domestic and overseas economies, corporate profits are declining, and private capital investment is decreasing. Investments for the renewal of equipment and for increasing value added to remain competitive are still necessary, and excess production capacity has not built up to levels such as those that existed after the bursting of Japan's economic bubble. However, there is a strong sense of uncertainty about future economic trends in Japan and overseas, and this may lead to a prolonged period of adjustment in capital investment.
- The level of recurring profits had exceeded the peak levels attained previously during Japan's bubble era and the time of the IT boom and continued to rise to record levels, but profitability has begun to decline. This has been due to higher costs, including increases in raw material prices, personnel costs, and depreciation charges, combined with the effects of the deceleration in the world economy, including weakness in domestic and international sales, including exports. The more recent declines in raw materials prices and the improvement in Japan's terms of trade will both be beneficial for corporate profitability; however, until the world economy begins to recover, a robust upward trend in

profitability will be unlikely.

(2) Households

- Although employment compensation is continuing to rise, the pace of increase is slowing. On the other hand, prices are rising at a faster rate, thereby increasing the sense of burden on household finances. As a result, consumer spending is expected to remain virtually level.
- The employment environment had been improving—as a result of the economic recovery, the retirement of members of the baby boom generation, and other factors—but is now deteriorating along with the rise in unemployment accompanying the weakness in corporate activities. The number of self-employed persons among employed persons is declining, and the number of employed persons is expected to fall, principally in manufacturing and other industries where production will decline going forward.
- Looking ahead, there is a strong possibility that wages, which have continued to show little growth, will decline and that companies will cut bonuses and other wage components as corporate performance deteriorates. Although price increases will settle down, the income environment is expected to become more challenging and consumption will remain virtually level.
- In the area of residential investment, although the sons and daughters of the baby-boom generation had been purchasing their first homes, the market has unavoidably stagnated since the revision in Japan's building code in June 2007. Even after the effects of the building code revision have run their course, housing sales have remained lackluster because of continuing high prices of housing and the effects of uncertainty regarding future trends. In addition, the slower growth in the number of households in the medium-term will also have a restraining effect on residential investment.

(3) Government

- Following the collapse of Japan's bubble economy, the structure of government finances deteriorated rapidly and the public sector has continued to issue a large volume of government bonds. Also, along with the decline in nominal economic growth rates and major tax cuts, government tax revenues have declined. Moreover, on the expenditure side, social welfare costs have risen as the population has aged demographically, 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, to implement structural reforms, the government suspended major spending programs aimed at stimulating the economy, and spending on public works projects was reduced. Moreover, local governments are experiencing fiscal difficulties and have continued to reduce their spending on public works. Along with the economic recovery, tax revenues began to expand again, but the government has basically maintained its policy of making structural reforms in its finances. Therefore, 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 financial 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. Also, under the administration of Prime Minister Taro Aso, some have expressed the view that the tight restraints on government expenditures should be loosened. Accordingly, we anticipate that the government's final consumption expenditures, principally social welfare payments, will continue to expand.
- 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 the 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 clearly on a decelerating trend. The United States is generally expected to report continued negative growth in the October-December quarter. Europe has now reported negative growth for two consecutive quarters for the first time since the introduction of the euro. Even in the emerging economies, where rapid growth has prevailed thus far, the momentum of growth appears to be pausing as a result of fluctuations in raw material prices and the deterioration in the economies of Europe and the United States.
- From now through the first half of 2009, the outlook is for the trend toward deceleration in the world economy to continue. Thereafter, from the latter half of 2009, as financial markets settle down, domestic demand in the emerging economies, which has remained relatively solid, is expected to be the driving force that will enable the world economy to gradually move out of the worst phase of the current downturn.
- As a result of the slowdown in growth, especially in Europe and the United States, Japan's exports are expected to begin to trend downward. In addition, the economies of Asia will be influenced by the lackluster performance in the economies of Europe and the United States. Exports to the emerging economies, which have been a driving factor for the increase in exports, are expected to remain weak for the time being. We expect exports will return to a rising trend after the middle of fiscal 2009.
- Along with weakness in the domestic economy, Japan's real imports are expected to follow a declining trend; however, the contribution of the external sector to real GDP will shrink in fiscal 2009 and become virtually neutral. On the other hand, the trade surplus in nominal terms is expected to begin to rise as a result of the decline in raw material prices. As a result, the outlook is for Japan's current account surplus to

begin to rise again in fiscal 2009.

3. Forecasts for Prices and Financial Markets

- Since the latter half of 2008, prices of raw materials, especially oil and metals, have dropped sharply, and upstream inflationary pressures have diminished. However, along with the rising manufacturing production capacity and expansion in demand in China and other emerging economies, upstream inflationary pressures from resources and other items will continue to put deflationary pressure on industrial products downstream.
- The effects of the decline in raw material prices are reaching the domestic price level in Japan. These declines have become a factor pushing down the prices of materials, including petrochemical products and nonferrous metal products, and, as a result, the rates of increase in corporate goods prices are slowing. Although consumer prices have risen, principally those of energy and food products, the rates of increase are diminishing.
- Regarding monetary policy, following the lifting of the monetary policy of quantitative easing in March 2006, the process of normalizing monetary policy to raise interest rates from their excessively low levels began. However, as a result of the turbulence in financial markets created by the subprime loan issue and the recognition of the risk of a downturn in the domestic and overseas economies, in October 2008, interest rates were lowered as part of Japan's stance of reinforcing and cooperating with the monetary policies of the countries of Europe and the United States. The Bank of Japan is expected to continue its policy of monetary easing until the turbulence in financial markets settles down and the uncertainty regarding the domestic and overseas economies subsides.
- Since the economic downturn is expected to continue and the rate of increase in prices to decline, long-term interest rates are expected to remain at low levels. 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 Japan's continuing current account surpluses, the appreciation of the yen 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. As a result of the impact of the financial crisis, the euro has declined in value, and the currencies of resource-producing economies have depreciated along with the decline in raw material prices. However, trends 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 regions.

Exhibit 2: Outlook for Fiscal 2008-2010

	FY2006 (actual)	FY2007 (actual)	Forecast ↘			Yr/Yr, %
			FY2008 (forecast)	FY2009 (forecast)	FY2010 (forecast)	
Nominal GDP	1.7	0.7	-1.3	1.1	0.6	
Real GDP	2.5	1.7	-0.6	-0.3	1.1	
Contribution of domestic demand	1.7	0.5	-1.1	-0.4	0.7	
Private consumption	1.8	1.7	0.2	0.2	0.6	
Housing investment	0.2	-13.3	-2.7	-0.7	0.5	
Private capital investment	5.6	-0.1	-4.2	-3.3	2.1	
Contribution of inventory investment	0.2	-0.0	-0.2	-0.1	0.0	
Government expenditure	-1.8	0.2	-0.9	0.7	0.1	
Public investment	-9.1	-1.8	-5.6	-2.4	-3.5	
Government final consumption expenditure	0.1	0.7	0.2	1.3	1.0	
Contribution of external demand	0.8	1.3	0.5	0.1	0.4	
Export of goods and services	8.4	9.5	0.7	-1.6	3.4	
Import of goods and services	3.1	2.0	-2.2	-2.3	1.3	
GDP deflator	-0.8	-1.0	-0.7	1.4	-0.6	

	FY2006 (actual)	FY2007 (actual)	Forecast ↘			Yr/Yr, %
			FY2008 (forecast)	FY2009 (forecast)	FY2010 (forecast)	
Current account balance (trillion yen)	21.2	24.5	18.2	25.7	25.2	
balance on goods (trillion yen)	10.5	11.7	6.0	14.4	13.1	
balance on service (trillion yen)	-2.3	-2.6	-2.0	-2.1	-2.0	
balance on income (trillion yen)	14.2	16.8	15.6	14.9	15.6	
Industrial production	4.6	2.6	-3.7	-4.2	1.2	
Unemployment rate(%)	4.1	3.8	4.1	4.5	4.5	
New housing starts(annualized, ten thousand units)	128.5	103.6	109.9	107.9	108.4	
Domestic corporate goods prices	2.0	2.2	4.2	-0.6	1.2	
Consumer prices	0.3	0.2	1.5	0.2	0.4	
excluding freshfood	0.1	0.3	1.5	0.2	0.4	
Yen/U.S.Dollar	116.9	114.2	100.9	98.6	102.3	
Uncollateralized call rates (O/N) (%)*	0.209	0.505	0.300	0.300	0.300	
Newly issued government bond yields (10years) (%)	1.77	1.60	1.53	1.56	1.68	
WTI future price (near month contract, US dollar/barrel)	64.9	82.2	89.9	62.0	68.5	
Dubai crude oil prices (US dollar/barrel)	60.9	77.3	84.0	58.4	65.0	

* actual=average, forecast=end of period

Exhibit 3: Outlook for Calendar 2008-2010

	CY2006 (actual)	CY2007 (actual)	Forecast			Yr/Yr, %
			CY2008 (forecast)	CY2009 (forecast)	CY2010 (forecast)	
Nominal GDP	1.4	1.4	-1.1	0.7	0.5	
Real GDP	2.4	2.2	0.3	-1.0	1.0	
Contribution of domestic demand	1.6	1.1	-0.6	-1.0	0.6	
Private consumption	2.0	1.7	0.7	0.0	0.5	
Housing investment	0.9	-9.5	-7.9	0.8	0.0	
Private capital investment	4.3	2.0	-2.2	-5.5	1.4	
Contribution of inventory investment	0.2	0.1	-0.2	-0.2	0.1	
Government expenditure	-2.0	0.1	-0.6	0.2	0.2	
Public investment	-8.1	-2.5	-4.4	-3.3	-3.8	
Government final consumption expenditure	-0.4	0.7	0.3	1.0	1.1	
Contribution of external demand	0.8	1.1	0.9	0.0	0.4	
Export of goods and services	9.7	8.6	4.9	-3.5	3.1	
Import of goods and services	4.2	1.7	-0.1	-3.8	1.0	
GDP deflator	-1.0	-0.8	-1.3	1.7	-0.5	

	CY2006 (actual)	CY2007 (actual)	Forecast			Yr/Yr, %
			CY2008 (forecast)	CY2009 (forecast)	CY2010 (forecast)	
Current account balance (trillion yen)	19.8	24.8	18.0	25.2	25.2	
balance on goods (trillion yen)	9.5	12.3	5.2	14.2	13.1	
balance on service (trillion yen)	-2.1	-2.5	-2.1	-2.1	-2.0	
balance on income (trillion yen)	13.7	16.3	16.3	14.6	15.6	
Industrial production	4.5	2.8	-1.2	-5.9	0.6	
Unemployment rate (%)	4.1	3.9	4.0	4.4	4.6	
New housing starts(annualized, ten thousand units)	129.0	106.1	111.1	107.9	108.3	
Domestic corporate goods prices	2.2	1.8	4.7	-0.6	1.3	
Consumer prices	0.3	0.0	1.4	0.5	0.3	
excluding freshfood	0.1	0.0	1.6	0.4	0.3	
Yen/U.S.Dollar	116.3	117.8	103.7	97.0	101.8	
Uncollateralized call rates (O/N) (%)*	0.113	0.474	0.300	0.300	0.300	
Newly issued government bond yields (10years) (%)	1.74	1.68	1.50	1.54	1.65	
WTI future price (near month contract, US dollar/barrel)	66.2	72.3	101.1	58.8	67.5	
Dubai crude oil prices (US dollar/barrel)	61.6	68.4	94.8	54.8	64.0	

* actual=average, forecast=end of period

Exhibit 4: 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	0.2	-0.1	0.2	-1.2	-0.5	-0.1	1.1	0.3	0.7	-0.9	0.5	
	1.4	1.2	0.4	-0.1	-0.9	-1.7	-1.5	-0.9	0.8	1.9	1.1	0.6	
Real GDP	-0.3	0.6	0.4	0.6	-0.9	-0.1	-0.4	-0.5	-0.1	0.3	0.2	0.2	
	2.0	1.8	1.8	1.4	0.7	-0.1	-0.8	-2.1	-1.0	-0.7	-0.1	0.6	
Contribution of domestic demand (Qr/Qr,%)	-0.5	0.0	0.1	0.2	-0.9	0.1	-0.5	-0.5	0.0	0.1	0.1	0.2	
Private consumption	0.5	0.2	0.2	0.6	-0.6	0.3	-0.2	0.1	0.0	0.0	0.1	0.1	
	1.6	1.9	1.5	1.7	0.5	0.4	0.2	-0.4	0.2	-0.1	0.2	0.3	
Housing investment	-3.9	-8.4	-9.8	5.1	-3.1	4.0	1.6	1.8	-2.5	-3.2	1.2	2.7	
	-2.9	-11.5	-21.7	-16.6	-15.8	-4.5	7.5	4.2	4.9	-2.4	-2.8	-1.9	
Private capital investment	-2.6	1.8	0.5	-0.3	-1.4	-1.7	-2.6	-2.1	-0.4	0.5	-0.4	0.5	
	0.2	0.2	-0.1	-0.6	0.7	-3.1	-5.8	-7.7	-6.8	-4.8	-2.4	0.2	
Contribution of inventory investment (Qr/Qr,%)	-0.2	0.0	0.0	-0.2	0.0	0.0	0.0	-0.2	0.0	0.1	0.1	0.0	
Government expenditure	-0.3	-0.4	0.8	-0.2	-1.1	0.1	0.2	-0.2	0.7	0.2	-0.1	-0.2	
	0.0	0.1	0.8	0.1	-0.8	-0.5	-1.2	-1.1	0.7	0.9	0.5	0.5	
Public investment	-2.8	-1.9	0.2	1.0	-5.5	0.4	-0.7	-1.0	0.5	-0.4	-1.5	-2.3	
	-2.8	-0.5	-1.8	-2.0	-6.9	-4.7	-5.0	-6.1	-1.3	-1.9	-2.4	-3.2	
Government final consumption expenditure	0.2	0.1	0.8	-0.5	-0.1	0.1	0.3	0.0	0.7	0.4	0.2	0.2	
	0.4	0.3	1.4	0.6	0.4	0.3	-0.2	0.3	1.0	1.5	1.3	1.5	
Contribution of external demand (Qr/Qr,%)	0.2	0.5	0.3	0.4	0.0	-0.2	0.0	0.0	0.0	0.1	0.1	0.0	
Export of goods and services	2.0	2.6	2.6	3.4	-2.6	0.7	-2.4	-1.6	-0.8	1.1	0.8	0.4	
	7.8	8.7	10.4	11.1	6.0	4.2	-1.0	-5.8	-4.0	-3.6	-0.4	1.6	
Import of goods and services	1.1	-0.5	1.0	1.2	-3.0	1.9	-2.9	-1.6	-0.5	0.2	0.3	0.3	
	1.4	1.4	2.2	3.0	-1.4	1.1	-2.8	-5.5	-3.1	-4.7	-1.6	0.3	
GDP deflator (Yr/Yr,%)	-0.5	-0.6	-1.3	-1.5	-1.6	-1.6	-0.7	1.2	1.8	2.7	1.2	0.0	

	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	3.4	4.3	5.9	6.3	6.6	6.5	6.4	
balance on goods (trillion yen)*	3.1	3.3	3.0	2.3	1.6	0.1	1.3	3.2	3.7	3.8	3.5	3.4	
balance on service (trillion yen)*	-0.6	-0.6	-0.7	-0.7	-0.5	-0.4	-0.6	-0.6	-0.6	-0.5	-0.5	-0.5	
balance on income (trillion yen)*	4.3	4.0	4.2	4.3	4.0	4.1	3.9	3.7	3.5	3.7	3.9	3.9	
Industrial production (Qr/Qr, %)	0.6	1.7	0.9	-0.7	-0.8	-1.3	-4.0	-1.5	-0.7	-0.2	-0.1	0.3	
(Yr/Yr, %)	2.3	2.6	3.3	2.3	1.0	-1.4	-6.5	-7.6	-7.4	-6.1	-2.4	-0.8	
Unemployment rate (%)*	3.8	3.8	3.8	3.8	4.0	4.1	4.2	4.3	4.3	4.4	4.6	4.6	
New housing starts(annualized, ten thousand units)	125.4	80.9	95.5	114.2	111.7	113.4	106.1	109.2	107.5	108.5	107.4	109.3	
Domestic corporate goods prices (Yr/Yr,%)	1.7	1.6	2.3	3.5	4.9	7.1	3.3	1.4	-1.0	-1.9	-0.6	0.8	
Consumer prices (Yr/Yr,%)	-0.1	-0.2	0.5	0.9	1.4	2.2	1.2	0.9	0.6	0.1	0.1	0.1	
excluding freshfood (Yr/Yr,%)	-0.1	-0.1	0.5	1.0	1.5	2.3	1.3	1.0	0.6	0.1	0.1	0.1	
Yen/U.S.Dollar	120.7	117.8	113.1	105.2	104.5	107.6	97.5	94.0	96.5	98.0	99.5	100.5	
Uncollateralized call rates (O/N) (**)	0.514	0.498	0.501	0.506	0.507	0.506	0.300	0.300	0.300	0.300	0.300	0.300	
Newly issued government bond yields (10years) (%)	1.74	1.72	1.56	1.39	1.61	1.51	1.50	1.50	1.50	1.55	1.60	1.60	
WTI future price (near month contract, US dollar/barrel)	65.0	75.4	90.7	97.9	124.0	118.0	64.7	53.0	57.0	61.0	64.0	66.0	
Dubai crude oil prices (US dollar/barrel)	64.8	70.0	83.3	91.2	116.9	113.8	57.4	48.0	53.0	57.5	60.5	62.5	

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