Toward the Revitalization of the Japanese Economy
-Target of the Growth Strategy

November 6, 2013

Norihiro Ishiguro
Vice-minister for International Affairs
Ministry of Economy, Trade, and Industry
Challenges the Japanese Economy has Faced
Serious Impact of the “Lost Two Decades” on the Japanese Economy

- Japanese GDP has slumped since the 1990s.
  - Japanese global competitiveness slipped – from #1 in 1990 to #26 in 2011 (IMD world competitiveness rankings)
  - Per-capita GDP also slid – from #3 in 2000 to #18 in 2011 (Source: IMF World Outlook Database)

Based on the data of “National Accounts Statistics” (Jan-Mar 2013): Cabinet Office
Since the bursting of the bubble economy, domestic CAPEX has seriously declined in the process of debt reduction. CAPEX has been limited within depreciation costs.

Rising emerging economies and intensifying global competition among companies have provided low-cost competition.

In recent years, terms of trade (export / import prices) have become worse compared with US. etc.

Average salary per capita has become stagnated since the bursting of the bubble economy.
Increasing Saving, Slumping Consumption, Continuous Deflation

- Saving Rate is on the rise based on anxiety about the future.
- As a result, domestic consumption has stagnated.

One of the main factors of deflation

The saving rate of worker’s households and “anxiety about old age”

Private-sector final consumption expenditure

Consumer price Index (Composite: except perishable foods)

Saving Rate is on the rise based on anxiety about the future. As a result, domestic consumption has stagnated.

Percentage of the people who feel anxiety about their old age (%)

(Source) “Family budget survey” by the Ministry of Internal Affairs and Communications and “Opinion survey on people’s lives” by the Cabinet Office

“System of National Accounts” Cabinet Office (based on the data of OECD stat)

FY2012: ▲ 0.2%

※Comparison with the previous year.

Source: “Consumer Price Index” Ministry of Internal Affairs and Communications
Dropping Tax Revenue, Budget Rigidity

- Tax revenue (Income Tax, Corporate Tax) has been on a declining trend since around the 90’s.
- Social security expenses in the general account expenditures exhibit an increasing trend.

Japanese debt is unprecedented among developed countries (228.4% of GDP 2013*).

*OECD “Economic Outlook 93”

Trend of the Major Tax Revenue of General Account

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<tr>
<th>Year</th>
<th>Income Tax</th>
<th>Corporate Tax</th>
<th>Commodity Tax, etc.</th>
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(Notes) Based on the final account for FY 2001 and before.
Based on the revised budget for FY 2012 and the budget for FY 2013.
Source: Ministry of Finance HP

Breakdown of the General Account Expenditures

- National debt payment
- Local allocation tax, etc.
- Social security expenses
- Others: educational and expenditure, defense-related expenditure, public works projects-related expenditures

(Notes) Based on the final account for FY 2000 and before.
Based on the budget for FY 2013.
Source: Ministry of Finance HP
Structures of “Downward Spiral” the Japanese Economy has faced

**[Economy]**

- Sluggish Capital Investment
- Stagnated Corporate Profits

**[Finance]**

- Decline in Tax Revenue
- Expansion of Fiscal Deficit
- Expansion of Social Security Expenses

**“Downward Spiral”**

- Continued Deflation → Decline in Expected Growth Rate
- Worsening Employment Situation → Decline in Labor Income
- Slumping Domestic Consumption
- Anxiety about the Future
- Increasing Domestic Saving
- Stagnated Corporate Profits
- Sluggish Capital Investment

→ Continued Deflation → Decline in Expected Growth Rate
Scenario of the Japanese Economic Recovery
–From “Downward Spiral” to a “Virtuous Cycle”
1. Price-stability target and bold monetary policy: The First arrow
   - Price-stability target (2% inflation) within about two-year time frame
     - Expand consumer spending through assets effects
     - Create inflationary expectations, end deflationary mindset and induce Investment

2. Flexible fiscal policy: The Second arrow
   - Massive ¥10 tril. fiscal stimulus package (FY2012 supplementary budget)
     - Stimulate demand for avoiding economic collapse/achieving economic recovery

3. Growth strategy: The Third arrow
   - Ensure overcoming deflation and accelerate economic growth led by private sector
   - Aim at fiscal consolidation through economic growth
The Japanese economy shifted from negative to positive growth.

### GDP Growth Rate

- **July-September 2012**: Minus 3.5%
- **January-March 2013**: Plus 4.1%
- **April-June 2013**: Plus 3.8%

(All figures are in real terms.)

### Exports

- **July-September 2012**: Minus 2.7%
- **April-June 2013**: Plus 0.7%

(Exports increased, contribution of net exports (in real terms) to GDP.)

### Consumption

- **July-September 2012**: Minus 1.0%
- **April-June 2013**: Plus 1.7%

(Consumption is starting to pick up, contribution of final consumption expenditures by households (in real terms) to GDP.)

### Capital Investment

- **July-September 2012**: Minus 12.9%
- **January-March 2013**: Plus 0.9%
- **April-June 2013**: Plus 6.5%

(Private capital investment (nominal terms): Pre-Lehman Shock level Approximately \$70 trillion, Fiscal 2012 Approximately \$63 trillion.)

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Although private capital investment has largely bottomed up, the level of investment is around 10% lower than the pre-Lehman Shock level.

Change from previous quarter and contribution are annual rate.
Today, I have decided to raise the consumption tax rate by 3%, increasing it from the current 5% to 8%, as was specified by law. There is no time to lose in securing financial resources to stabilize social security and rebuild the severe fiscal situation.

**Schedule for tax increase**

- **At present**: 5%
- **April 2014**: 8%
- **October 2015**: 10%

To be adjusted based on economic climate, etc.

**Economic policy package (decided on October 1)**

Including:

1. **Policies to prop up economic growth**
   - Implementing the Growth Strategy (reform of regulations and systems to stimulate private-sector investment, etc.)
   - Tax Incentives (to promote capital investment, business restructuring and venture/start up investment, etc.)

2. **Joint effort by the government, employees and employers to create a virtuous economic cycle**
   - Discussions in the conference among government, workers and employers
   - Revision and expansion of tax credit for wage increases
   - Consider abolishing the surtax for earthquake disaster reconstruction one year ahead of schedule

3. **Formulation of an economic package**
   - As large as 5 tril. yen
   - To be decided in December 2013
< 3 Key Points of the Growth Strategy Aiming at Mid-term Structural Reforms>

(1) Proactive Corporate Management

(2) Maximum Utilization of Human Resources

(3) Creation of Dynamism through Abolishing Excessive Regulations
• Recent cases of proactive management decisions aiming for higher profitability
  ➔ Need to extend such movements

**Bold domestic investment**

**Komatsu**
Mid-range management plan (2013-2015)
• Build leading-edge/energy-saving facilities in main factories
• Also achieve innovative production efficiency

Aim to cut electric power consumption to half at factories in Japan

**Business integration for global expansion**

- Hitachi
  - Hydropower operation
- Mitsubishi Electric
  - Hydropower operation
- Mitsubishi Heavy Industries
  - Hydropower operation

Hitachi Mitsubishi Hydro Corporation

Spherical Valve delivered to Purulia Hydro Power Plant in India

**Global integration across borders**

- Tokyo Electron
  - #1 *domestic* market share in semiconductor production equipment
  - Their strengths in technology and production complement each other.

- Applied Materials
  - #1 *global* market share of semiconductor production equipment

Merger
Expected to be completed in later half of 2014
Strengthen Profitability with Proactive Corporate Management

- Assist “proactive corporate management” intensively for three years by bold tax incentives
  - Convert “expectations” (to throw away deflation mindset) into “actions” (towards sustainable virtuous cycle)
    - Promote productivity-enhancing capital investment
    - Promote business restructuring and venture/start up investment
      (to redistribute management resources from less competitive industry to areas that will be the source of new growth)
- Promote productivity-enhancing corporate initiatives (NOT mere scale expansion)
  (improve ROA, “carve outs” and integration of low profitability sectors, etc.)

**Bold Tax Incentives**

- Tax incentives for promoting capital investment (see App. 1)
- Tax incentives promoting business restructuring (carve outs & integration of business) (see App. 2)
- Tax incentives for promoting venture/start up investment (see App. 3)

Together with tax incentives for promoting R&D, for raising wages, and for promoting investment by small and medium enterprises, the amount of tax cut is approximately \(1\) tril.
Tax reform implemented in FY 2012
- Permanent tax reduction (cut corporate tax rate and broaden the tax base)
- Corporate surtax for earthquake disaster reconstruction (FY2012-2014)

Review abolishing the surtax one year ahead of schedule, assuming that economic growth in the immediate term be translated into wage increase

(Conclusion to be arrived at in December)

5% cut in effective corporate tax rate (including local taxes)
40.69% (-FY2011) → 38.01% (FY2012-14) → 35.64% (FY2015-)
< 3 Key Points of the Growth Strategy Aiming at Mid-term Structural Reforms>

(1) Proactive Corporate Management

(2) Maximum Utilization of Human Resources

(3) Creation of Dynamism through Abolishing Excessive Regulations
Another great source of potential lying dormant in Japan is the power of women.

I will transform dramatically the Japan that is grappling with the feeling of being caught in an impasse because it "still limits its executive talent pool to the male, 50 percent of its population."

In Japan, a great many women quit their jobs when they get married or have children, even though they are still very highly skilled and capable. I am convinced that if such women rise to action, Japan will be able to enjoy dynamic growth.

We need to eradicate the words “children on the waiting list for childcare.” **We will prepare, as one massive effort, childcare arrangements for 200,000 children over this year and next, and arrangements for 400,000 children over a five-year period.** As of this summer, we already succeeded in achieving our goal of preparing places for 120,000 children.
Need to harness the power of women under the decreasing trend in productive population (Many female workers in their prime have to unwillingly leave their jobs due to childbirth, etc.) (3 million potential female workers are left unutilized.)

Diversity management through utilizing a wider range of talent including women increases innovation and improves productivity in companies.

Stock markets have begun evaluating such corporate efforts.

Female participation contributes to increase in consumption through increased household income.

Potential female labor force: About 3 million

Labor participation rate for women

The stock performance of the corporations making efforts to increase female compared to TOPIX average

CAR to TOPIX (average) for corporations awarded for the promotion of gender equality

Source: Daiwa Institute of Securities Quants Capital Markets Co., Ltd. Financial and Securities Research Institute "Quants Information" June 14, 2011

“100 best companies for diversified management” awarded by METI as of the FY2012

Toshiba Corporation
- Project to develop 3-D displays by female employee ideas
- Series of home appliances named “Mama-gokoro” (Moms’ viewpoints)

Shiseido Co., Ltd.
- Products with emphasis on organoleptic characteristics by female planner
- Win the top share: shampoos and hair conditioners
Second Careers for the Elderly

- Need to utilize the power of the elderly, in addition to women (As of 2020, the population aged 65 or over will reach about 3%).
- Begin utilizing the immense knowledge and experiences of the elderly in different fields

Examples of utilizing the knowledge, skills and ideas of the elderly

The University of Tokyo Monozukuri instructor school
- Provided instruction courses for the elderly who have experience of production management
- Enable them to apply know-how they have in different fields or industries
- The alumni work as instructors at SMEs or community schools.

Increase in human resources for managing hospitals and nursing services

Examples:
- Division manager in a large trading house: retired early and plan managerial strategies for a hospital
- Member of a large steel company: chief clerk at a hospital improve profitability by shortening patients’ hospital stays and streamlining nurses’ work
- Regional banker: find another job in the management team of a hospital in the region

Population transition and estimates

Increasing Labor Market Flexibility to Improve Productivity

- Insufficient movement of workers to growth fields
  - Caused by the employment paradigm based on lifetime employment, which used to contribute to high economic growth

- Enhance more flexible labor market and utilize in growth fields the human resources kept unutilized in companies
  - Provide assistance for workers to improve career prospects or to develop expertise in a new field
  - Start to reform rules of employment to realize various ways of working (review the minimum period of limited-term employment, introduce diversified full-time employment, realize flexible working hours, etc.)

Improving productivity by reducing mismatches and smoothly moving workers to growth areas
Utilizing diverse human resources and enhancing flexibility of labor market improve corporate profitability and create new industries.

Wage increases through profitability improvements expand consumption and improve further corporate profitability. (a virtuous cycle of the economy)

Aim to start such virtuous cycle through measures including:
- establishment of a conference among government, workers and employers
- revision and expansion of tax credit for wage increases (see App. 5)

### Trend for Wage Increases This Spring

**Seven & i Holdings Co., Ltd.**
- Monthly pay of regular employees: **5,229 yen**
- (major subsidiary: Seven Eleven)
- *54 companies in the group will implement similar policy*

**Lawson**
- Annual average salary: **3%**
- by raising lump-sum payment
- (employees from their late 20’s to 40’s)

**Toyota**
- Lump-sum payment: **270 thousand yen**
- (per year) to regular workers

**Hitachi**
- Lump-sum payment: **24 thousand yen**
- (per year) to regular workers

Source: Announcement by companies and press reports
Attract Human Resources from Overseas

- Review the points-based preferential immigration system for foreign professionals
  - Increase the number of people accepted through this system
    (about 430 since the program was introduced in 2012)
- As a part of the university reform, increase the number of foreign researchers
  - Offer some 1,500 full-time positions for overseas researchers over the next 3 years

Review of the immigration process for highly-skilled foreign professionals

Overview

- Introduced in May 2012 to attract skilled professionals who can contribute to Japan’s economic growth, and to create new job opportunities within Japan
- Assesses individuals based on criteria such as educational background, career history and annual income
  Provides preferential immigration treatment based on the total number of points

Objectives for review

- Relax annual income criteria
  (e.g. reviewing the definition of annual income to include rewards from overseas institutions)
- Reduce the time that foreign nationals are required to reside in Japan before being eligible for permanent resident status (from 5 years to 3 years)
- Consider preferential treatment for family members who accompany foreign professionals
< 3 Key Points of the Growth Strategy Aiming at Mid-term Structural Reforms>

(1) Proactive Corporate Management

(2) Maximum Utilization of Human Resources

(3) Creation of Dynamism through Abolishing Excessive Regulations
In order to resolve Japanese social challenge of aging society, some companies:

- produce high-end medical devices that meet medical practice needs
- provide services that public health insurance doesn't sufficiently offer to the elderly

Health care industry has significant potential as a new market

However, existing regulation systems constrains increasing the market size

Medical Device Making Use of SME Manufacturing Technology

New Service for the Elderly not Covered by Public Health Insurance

Example. Tailor-made Joint Prostheses
- Apply its propeller manufacturing technique for tankers.
- Develop less-wearing and durable joint prostheses suited for Japanese body type and lifestyle.

Nakashima Medical Co., Ltd, (Okayama pref. Capital: 50 million yen Employees: 153)

Example. Rehabilitation guidance by easy exercise

[Example] Konami Sports and Life Co., Ltd. (Fitness club)

[Example] Seven-Meal Service Co., Ltd. (Home-delivered meal)

Productivity Improvement in Nursing Care Business

[Example] ORIX Living Corporation
(Use of nursing-care robots contributes to improving the productivity of nursing service.)

Provide meal delivery, which used to be done by family, as a new service
Early authorization system

Drastically speed up the time necessary for authorization

Establishing new approach to accelerate deregulation.

In the field of healthcare, uncertainties exist in conducting business.
(e.g.) How far a company, in cooperation with medical organizations, can advice for health checks.

(1) Establish a system to verify the legality of “Grey Zones” business.

(2) Following a proposal made by corporations, create a system to ease regulations on a company basis.

Major revisions in the related bills of the Pharmaceutical Affairs Law, etc.

(1) Speed up the certification for innovative medical devices.
- Extend the scope of certification by private third-party organizations
- Public certification focusing on innovative medical devices and accelerating speed

(2) Faster authorization in Regenerative Medicine. (see. app. 6)
- Establish an early authorization system.
  Enables a company to put regenerative medicine products on the market with conditions and a deadline by confirming efficacy in a certain number of patients.

Medical organization
Manufacturer and distributor
Patients

In the field of healthcare, uncertainties exist in conducting business.
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Revision of the Pharmaceutical Affairs Law, and Creation of a New Framework for Regulatory Reform

- Revise Pharmaceutical Affairs Law (As part of the regulatory reform in the field of healthcare)
- Fall Diet Session
- Establish new approach to accelerate deregulation which harnesses corporate technology and ingenuity will
Creating New Businesses and Reforming in the Electric Utility Systems

- An energy management system enables control of an energy supply using batteries and other devices.

- New business strategies are being developed.
  e.g.) “Smart houses” with HEMS
  (add high values by installing a set of related equipment when newly built)

- Electric power industry reform for the first time in 60 years:
  - induces new entry of players who will provide services meeting customer demands
  - accelerates development of new businesses and triggers innovation

Energy Control Using an Energy Management System

Implementing Reforms of the Electricity System (See App.8)

1st stage (by around 2015)
- Establishment of the Organization for Cross-regional Coordination of transmission Operators (OCCTO).
  → nation-wide grid system

2nd stage (by around 2016)
- Full liberalization of the retail market.

3rd stage (by around 2018 - 2020)
- Separation of transmission and distribution sector.
  Full liberalization of retail rates.
Creating Dynamism by Promoting Economic Partnership

- Only approximately 20% of Japan’s total trade value is with FTA partner countries and regions.
- Enhance economic partnerships such as TPP, RCEP, Japan-China-Korea FTA, Japan-EU FTA and encourage Japanese companies to expand their business into overseas markets (see App. 9)

**Economic partnership deepens in various parts of the world**

**Enhance economic partnership including TPP, RCEP, Japan-China-Korea FTA, Japan-EU FTA**

- **2011**
  - Total trade: 1.7 billion dollars (2011)
  - FTA in effect: 19%
  - Asia: 16%
  - Others: 70%

**USA-EU FTA**
- Announced to start negotiations in June, 2013

**South Korea-EU FTA**
- Went into effect provisionally in July, 2011

**South Korea-USA FTA**
- Went into effect in March, 2012

**Singapore-EU FTA**
- Concluded negotiations in December, 2012

**Japan-China-Korea FTA**
- Launched negotiations in March, 2013

**Japan-EU EPA**
- Launched negotiations in April, 2013

**Vietnam-EU FTA**
- Launched negotiations in June, 2012

**Malaysia-EU FTA**
- Launched negotiations in December, 2010

**MERCOSUR**
- Went into effect in 1995

**ASEAN**
- Went into effect in January, 1993

**RCEP**
- Launched negotiations in May, 2013

**North America**
- **NAFTA**
  - Went into effect in 1994

**Latin America**
- **TPP**
  - Welcomed Japan's participation in April, 2013

**Europe**
- **EU Customs Union**
  - Went into effect in 1968

- **Japan-EU EPA**
  - Launched negotiations in April, 2013

- **Japan-China-Korea FTA**
  - Launched negotiations in March, 2013

- **Japan-EU EPA**
  - Launched negotiations in April, 2013
Change the Scenario of “Downward Spiral” into a “Virtuous Cycle”

- Support proactive corporate management including aggressive capital investment
  → **Increase corporate profits**
- Make good use of underutilized high quality employment including women and elderly
  → **Improve labor income**
- Encourage such activities through abolishment of excessive regulations
  → **Facilitate an environment conducive to dynamism in companies**

**Realize a “virtuous cycle”**

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**[Economy]**

- Active Capital Investment
  - Increasing Corporate profit

  - Exit from Deflation
    → Expansion of Expected growth Rate

  - Revitalizing Domestic Consumption

  - Overcoming Anxiety of the future

**[Finance]**

- Increasing Tax Revenue

  - Overcoming Fiscal Deficit

  - Expanding High-Quality Employment
    → Improving Labor Income

**Virtuous Cycle**