The Growing Risk of an Extended Recession—Short-term Economic Forecast (FY 2008–2010)

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We believe that Japan's economy peaked out in late 2007 and entered a downturn. Real GDP contracted for the second consecutive quarter in July-September 2008, and repercussions from the financial crisis will likely extend the negative growth into the second half of fiscal 2008. As a result, we estimate real GDP will contract -0.9 % in fiscal 2008 for the first annual contraction since shrinking -0.8% in fiscal 2001. The economy will bottom out in the second half of fiscal 2009 as overseas economies recover. However, growth will remain slow due mainly to the sluggish U.S. economy, where household balance sheets need to be cleaned up. Japan's economy will continue to perform below the potential growth rate, posting negative growth of -0.8% in fiscal 2009 and recovering to a modest 0.8% pace in fiscal 2010.

1. Impact of the Growing Global Recession

1. Second Consecutive Quarter of Negative Growth

Japan's economy is believed to have peaked out in late 2007 and entered a contractionary phase. In the second quarter (April-June) of 2008, real GDP shrank -0.1% from the previous quarter (-3.7% annualized rate), followed by another -0.5% decline (-1.8% annualized) in Q3, thus marking two consecutive quarters of negative growth. The main causes of the downturn are sluggish export growth and decline of business fixed investment, reaffirming that the disruption of the recovery led by the corporate sector and export growth is now complete.

Exports rose 0.8% in Q3 from the previous quarter for the first time in two quarters. Nonetheless, the growth was disappointing after the -2.6% plunge in Q2, and also fell well below theQ3 import growth of 2.3%. As a result, external demand contributed a negative -0.2 -percentage point to real GDP growth in Q3. Exports to the U.S. and European markets have already slumped, and are slowing to key emerging and developing economies.

Exhibit 1 IMF Projections for the World (November 2008)

(% yoy change)

	2006	2007	Projections 2008	Projections 2009
World output	**5.1**	**5.0**	**3.7**	**2.2**
Advanced economies	3.0	2.6	1.4	−0.3
U.S.	2.8	2.0	1.4	−0.7
Euro area	2.8	2.6	1.2	−0.5
Japan	2.4	2.1	0.5	−0.2
U.K.	2.8	3.0	0.8	−1.3
NIEs	5.6	5.6	3.9	2.1
Emerging & developing economies	7.9	8.0	6.6	5.1
Russia	7.4	8.1	6.8	3.5
China	11.6	11.9	9.7	8.5
India	9.8	9.3	7.8	6.3
Brazil	3.8	5.4	5.2	3.0
ASEAN-5	5.7	6.3	5.4	4.2
Middle East	5.7	6.0	6.1	5.3

Source: International Monetary Fund, *World Economic Outlook Update,* November 6, 2008.

Business fixed investment in Q3 fell a sizable -2.0% from the previous quarter, following on a similar 2.1% decline in Q2. Squeezed by rising costs from high commodity prices and sluggish revenues due to declining exports, corporate earnings have deteriorated markedly, leading to an increasingly conservative investment stance.

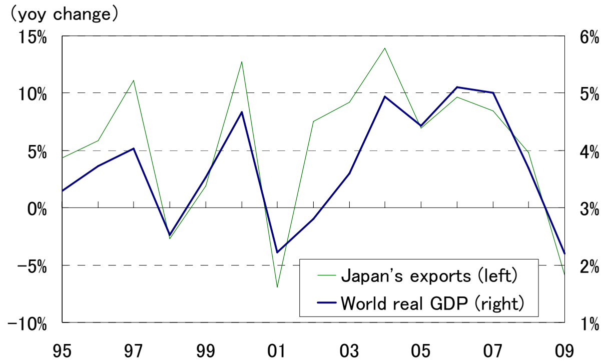
2. Negative Growth Hits the U.S. and Europe

Other advanced economies also contracted in Q3 — real GDP fell -0.5% from the previous quarter in the U.S., -0.8% in the euro area, and -2.0% in the U.K. In addition, China decelerated from a brisk 10.1% year-on-year pace in Q2 down to 9.0% in Q3, showing that emerging and developing economies are also being affected.

Even as the economic downturn continues to spread globally, the impact of the financial crisis triggered by the Lehman Brothers failure (September 15) has just begun to unfold. With Europe and the U.S. already expected to continue negative economic growth in Q4 and beyond, the financial crisis can only exacerbate the downturn.

According to an IMF projection released in November 2008, world real GDP growth will decelerate from 5.0% in 2007 to 3.7% in 2008 and 2.2% in 2009. This projection sharply downgrades the previous projection released just one month earlier by -0.2% for 2008 and -0.8% for 2009. The 2% growth rate projected in 2009 is comparable to the low growth experienced in the 1998 Asian currency crisis and 2001 collapse of the IT bubble.

Exhibit 2 Forecast for World Real GDP and Japan's Exports



Notes: Shows IMF forecast for 2008 and 2009 world real GDP, and our forecast for Japan's exports of goods and services.
Sources: IMF, *World Economic Outlook*; Cabinet Office, *Quarterly Estimates of GDP*.

Since Japan's exports tend to track the growth of the world economy, the current export decline is likely to accelerate in the future.

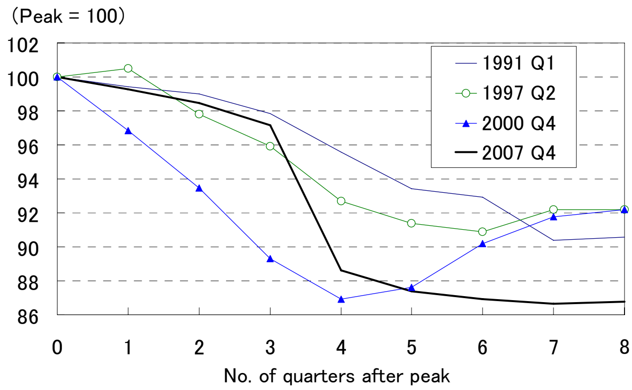
3. Industrial Output Falling Faster Than After the IT Bubble

After peaking out in Q4 2007, industrial production slipped fairly moderately during 2008 (-0.7% sequential decline in Q1, -0.8% in Q2, and -1.3% in Q3), especially in light of the economic downturn.

However, the October data showed a -3.1% monthly decline from the previous month. Meanwhile, the November *Survey of Production Forecast in Manufacturing* revealed expectations of a -6.4% decline in November and -2.9% decline in December. By industry, transport equipment, which suffered sharp export declines to the U.S. and Europe, expects to slash output by -12.4% in November and -12.1% in December. Considering the large ripple effects this will have across many other industries, we expect the scope of production adjustments to spread in the future.

Based on the October output data and November production forecast data for November and December, we estimate that industrial production in Q4 will plummet -8.6% from the previous quarter. On a quarterly basis, the deterioration will likely eclipse the -4.4% sequential decline when the IT bubble collapsed in Q3 2001, and become the worst on record since data collection began in 1978. In addition, the magnitude of adjustment from the peak is also likely to rival that of the IT bubble's collapse (Exhibit 3).

Exhibit 3 Industrial Production in Previous Contractions



Note: For the contraction starting in 2007 Q4, the peak date is assumed, and index values for the fourth quarter (Q4 2008) onward are based on our forecast.
Source: METI, *Industrial Production Indices.*

2. Impact of Falling Oil Prices

1. Relief from the Deteriorating Terms of Trade

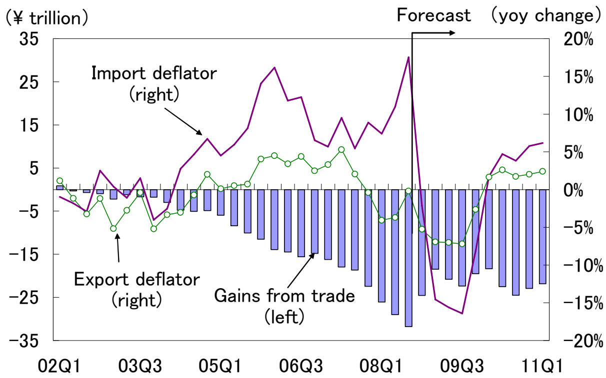
Amid the severe conditions surrounding Japan's economy, one bright spot has been the sharp fall in oil and commodity prices.

Soaring commodity prices have saddled the economy for a long time. Due to Japan's high dependence on oil imports, surging oil prices directly boost import prices and impair the terms of trade, causing more income to flow abroad. The gains from trade, which measures the outflow of real income stemming from the disparity between export and import deflators, deteriorated to -31.8 trillion yen in Q3 2008. The 13 trillion yen expansion from a year ago is equivalent to 2% of GDP.

The outflow of income has reduced domestic real purchasing power, thereby weakening domestic demand. In other words, import price increases have squeezed corporate earnings and dampened business fixed investment. Meanwhile, as companies began passing on part of the cost increases downstream to final goods prices, the real purchasing power of households diminished, thereby dampening personal consumption.

However, the WTI futures oil price, which almost reached 150 USD per barrel in mid July, subsequently plummeted due to the global economic slowdown, and has recently settled in the 40 USD range. Import inflation, which surged to 27.2% (year-on-year) in August 2008, subsequently turned negative to -8.6% in November. As a result, the terms of trade have stopped deteriorating. The BOJ terms of trade index has improved for three consecutive months, rising 1.6 points in September 2008, 1.9 points in October, and 2.2 points in November.

Exhibit 4 Forecast for Export and Import Deflators, and Gains from Trade



Source: ESRI, *Quarterly Estimates of GDP.*

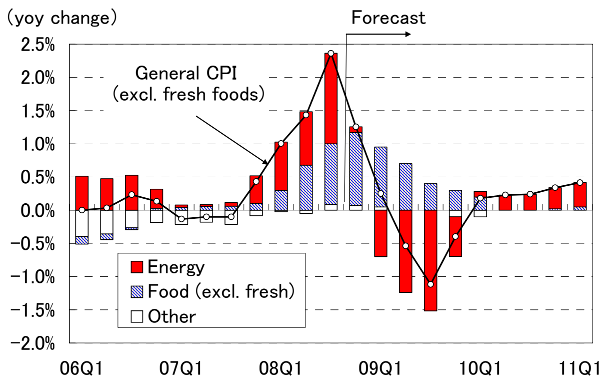
In the GDP data, we expect the losses from trade to have bottomed out at -31.8 trillion yen in Q3, and to start shrinking in Q4. In view of the strong yen, we expect the import deflator to turn negative in the double-digit range (year-on-year) in Q1 2009. As a result, the losses from trade in Q1 2009 will abate to -18.5 trillion yen, thus shrinking by over 10 trillion yen in half a year.

While the improving terms of trade should boost Japan's struggling domestic economy, we must note that falling commodity prices reflect a slowdown in world demand. Thus the global economic downturn not only reduces import prices and costs within Japan, but also depresses Japan's exports and sales revenue, thereby suppressing corporate earnings. Since foreign economies are not expected to recover until mid 2009 at the earliest, we predict that the benefits from the improving terms of trade will be offset by declining exports. To fully benefit from the improving terms of trade, exports must recover in step with the overseas recovery, which can happen no sooner than mid 2009.

2. CPI Inflation to Peak Out

The decline of import prices has already impacted domestic prices. The domestic corporate goods price index, which surged 7.4% from a year ago in August 2008 (the largest increase in approximately 27 years), slowed to 2.8% in November. Meanwhile, the general CPI excluding fresh food also jumped 2.4% in July and August, slowing to 1.9% in October.

Exhibit 5 Forecast for CPI Inflation



Source: MIC Statistics Bureau, *Consumer Price Index.*

The main cause of CPI inflation has been rising energy prices, particularly gasoline prices. Due to plunging oil prices, the retail price of regular gasoline plummeted from a peak of 185 yen per liter in August (according to data from the Oil Information Center), to approximately 120 yen, and is expected to slide further. Another major cause of CPI inflation, food price increases, will be increasingly difficult to pass on as demand softens amid the economic downturn. As a result, we predict that after peaking out at 2.3% year-on-year in Q3 2008, CPI inflation (general, excluding fresh food) will decline to 1% in Q4 2008, 0% in Q1 2009, and turn negative in Q2 2009.

By fiscal year, we predict CPI inflation will rise from 0.3% in fiscal 2007 to 1.3% in fiscal 2008, turning negative to -0.5% in fiscal 2009 for the first time in five years, and then rising a modest 0.3% in fiscal 2010.

2. GDP Deflator to Turn Positive Temporarily

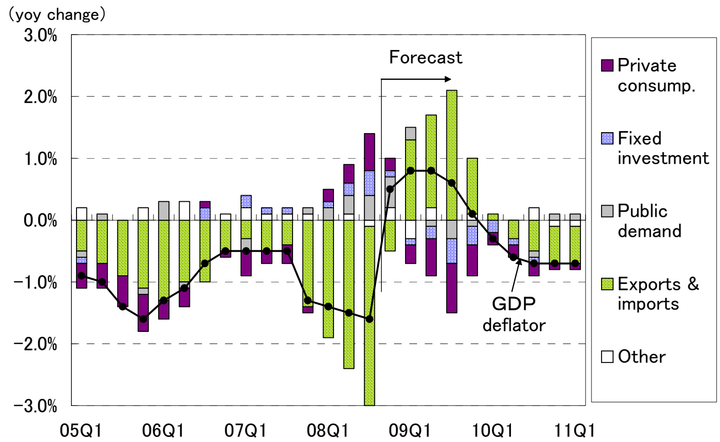
The GDP deflator plunged -1.5% (yoy) in Q2 2008 and another -1.6% in Q3 2008. As seen by CPI inflation in excess of 2%, higher import prices have been passed on to domestic prices, causing the domestic demand deflator to surge from 0.9% (yoy) in Q2 2008 to 1.4% in Q3. However, this move was more than offset by the import deflator's surge from 11.0% (yoy) in Q2 to 17.5% in Q3, pushing down the GDP deflator.

The GDP deflator, which has been consistently negative for over a decade since Q2 1998, now appears poised to turn positive in Q4 2008. This is because the surging import deflator, which kept the GDP deflator down in the past, will likely turn negative due to plummeting commodity prices and the strong yen. But while lower import prices will help reduce domestic prices, domestic price inflation will decline only moderately in the near term because import price declines will not be fully passed on, and time lags will also occur.

We predict that the GDP deflator will turn positive to 0.5% (yoy) in Q4 2008, but only for a limited time. First, as the economic downturn causes the output gap to widen, downward pressure will mount on domestic prices. Second, in fiscal 2010, as the world economic recovers, oil prices will rise and cause the import deflator to turn upward.

We predict the GDP deflator will decline -0.4% in fiscal 2008, rise 0.3% in fiscal 2009, and decline -0.7% in fiscal 2010.

Exhibit 6 Forecast for GDP Deflator



Source: ESRI, *Quarterly Estimates of GDP*.

3. Economic Forecast to Fiscal 2010

1. Limited Effect of Economic Stimulus

In response to the worsening financial crisis and economy, the government announced a 26.9 trillion yen additional economic stimulus package on October 30 (Measures to Support Peoples' Daily Lives). It largely echoes features of the package announced by the Fukuda Cabinet (Comprehensive Immediate Policy Package: Easing Public Anxiety) on August 29. Although the latest package calls for as much as 26.9 trillion yen in public spending, the outlays expected to expand demand are rather limited.

A limited stimulus effect is expected from the proposed 2 trillion yen cash benefit for households. Whereas the Fukuda Cabinet had proposed a fixed income tax cut of the same magnitude, the cash benefit was chosen instead on the basis that more households would receive the benefit including low income households who pay no income taxes. Otherwise, the macroeconomic impact of the two alternatives is identical.

Our forecast assumes that the 2 trillion yen cash benefit will be disbursed by the end of fiscal 2008. However, since the second supplementary budget necessary to fund the package will not be submitted to the Diet until January, our timeline has come under doubt.

According to our macroeconomic model, the 2 trillion yen cash benefit would boost annual private consumption by 0.2% and real GDP by 0.1%. Even if the cash benefit is disbursed during fiscal 2008, most of the impact will spill over into fiscal 2009—specifically, real GDP will increase by 0.04% in fiscal 2008 and 0.09% in fiscal 2009. The total stimulus effect will thus be less than the actual cash benefit outlay, which comprises 0.4% of GDP. This is because households are expected to save rather than consume much of the increase in disposable income, thus diluting the stimulus effect.

Exhibit 7 Predicted Effect of 2 Trillion Yen Cash Benefit (contribution to growth)

	Change in real GDP	Change in private consumption
FY 2008	0.04%	0.07%
FY 2009	0.09%	0.21%
Total	0.13%	0.28%

Note: We assume the cash benefit is disbursed in Q1 2009.

2. Economy to Bottom Out in Second Half of Fiscal 2009

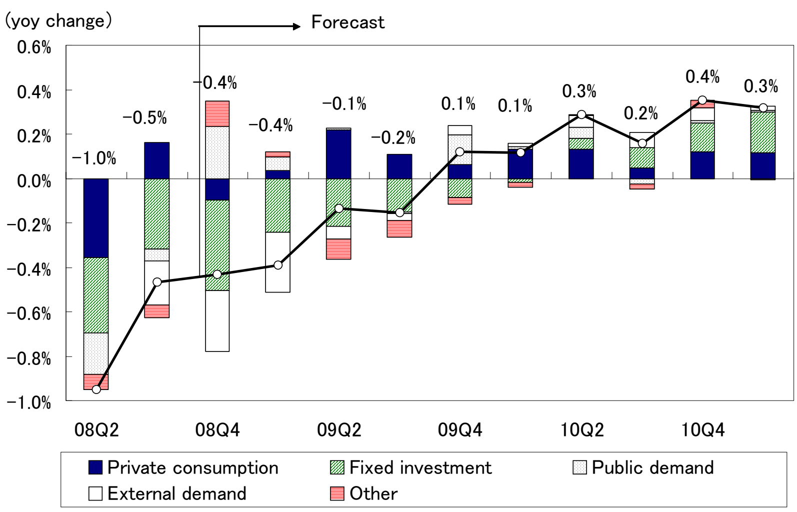
While the economic downturns in the U.S. and Europe were relatively mild in Q3 2008, both are expected to worsen in Q4 in the wake of the financial crisis after the Lehman Brothers' collapse. As a result, Japan's already sluggish exports are likely to decelerate even faster, weighing down the economy in the near term.

The household sector, which has been resilient thus far, will not be immune from the corporate sector's deterioration. This is because as declining exports and revenues trim corporate earnings, companies will be compelled to slash output and investment, prompting employment and wage adjustments. With layoffs already underway, we predict the unemployment rate will deteriorate from 3.7% in October 2008 to almost 5% in late fiscal 2009. As a result, the household sector will lose momentum and fail to offset the corporate sector's weakness.

In the absence of a driving sector, we predict the negative growth of the past two quarters will continue in Q4 2008 and Q1 2009. As a result, real GDP will decline -0.9% for fiscal 2008, the first annual decline since the -0.8% decline in fiscal 2001.

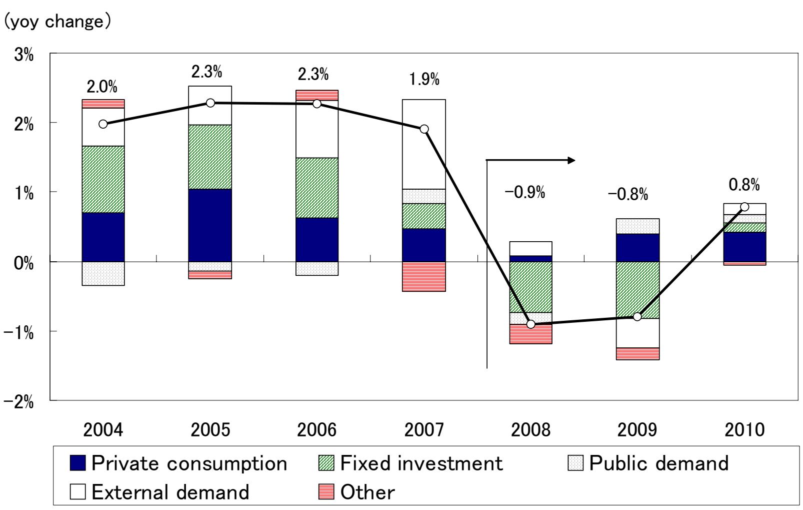
At the G-20 Summit on Financial Markets and the World Economy in November, leaders affirmed that they will implement additional monetary and fiscal measures as necessary to overcome the financial crisis. As a result, we predict the U.S. and other overseas economies will recover

Exhibit 8 Forecast for Real GDP (quarterly)



Source: ESRI, *Quarterly Estimates of GDP*.

Exhibit 9 Forecast for Real GDP (annual)



Source: ESRI, *Quarterly Estimates of GDP*.

in the second half of 2009, helping to drive Japan's exports toward recovery.

However, with households in the U.S. reeling from the housing meltdown and stock market slump, consumption will be restrained until household balance sheets are cleaned up. Thus personal consumption will likely remain sluggish even after the recession ends, limiting the U.S. economy's growth.

While we predict Japan's economy will bottom out in the second half of 2009, low growth rates of overseas economies will likely cause Japan's export growth to fall short of the pace achieved in the 2002 recovery. As a result, the economy will recover at a pace below the potential growth rate, seen as in the mid to upper 1% range. Thus we predict real GDP growth will remain negative at -0.8% in fiscal 2009, followed by a modest 0.8% recovery pace in fiscal 2010.

By demand component, private consumption in fiscal 2008 will grow 0.1% from a year ago due to the deteriorating job and income environment, and the decrease of real purchasing power due to inflation. In fiscal 2009, despite a boost from the cash benefit and increase of real income due to deflation, consumption will only grow 0.7% due to deteriorating corporate earnings impact jobs and wages, followed by 0.7% growth in fiscal 2010.

Residential investment will decline -2.0% in fiscal 2008 despite a rebound from the -13.0% plunge in fiscal 2007 associated with the building code revision. Momentum has already ebbed due in large part to weak condominium sales. In fiscal 2009, we predict residential investment will grow 2.0% for the first time in five years on the strength of the enhanced tax credit for housing loans, but then recede to 0.3% growth in fiscal 2010.

Due to slumping profits, business fixed investment will drop -4.6% in fiscal 2008 for the first time in six years, followed by a larger -5.4% decline in fiscal 2009. In fiscal 2010, investment will recover to 1.0% growth on the strength of an earnings recovery.

The contribution of external demand to GDP growth will decline from 1.3% in fiscal 2007 to 0.2% in fiscal 2008. Reflecting the economic downturn abroad, export growth will plunge from 9.3% (yoy) in fiscal 2007 to 0.3% in fiscal 2008, turning negative to -4.5% in fiscal 2009 for the first time in eight years. As a result, in fiscal 2009 external demand will make a negative contribution of -0.4% to GDP growth. In fiscal 2010, the overseas recovery will boost Japan's exports to 3.0% growth (yoy), such that external demand once again makes a positive 0.2% contribution to GDP growth.

Exhibit 10 Business Cycle Reference Dates

Cycle	Trough	Peak	Trough	Duration (months)		
				Expansion	Contraction	Total
No. 1		Jun 1951	Oct 1951		4	
No. 2	Oct 1951	Jan 1954	Nov 1954	27	10	37
No. 3	Nov 1954	Jun 1957	Jun 1958	31	12	43
No. 4	Jun 1958	Dec 1961	Oct 1962	42	10	52
No. 5	Oct 1962	Oct 1964	Oct 1965	24	12	36
No. 6	Oct 1965	Jul 1970	Dec 1971	57	17	74
No. 7	Dec 1971	Nov 1973	Mar 1975	23	16	39
No. 8	Mar 1975	Jan 1977	Oct 1977	22	9	31
No. 9	Oct 1977	Feb 1980	Feb 1983	28	36	64
No. 10	Feb 1983	Jun 1985	Nov 1986	28	17	45
No. 11	Nov 1986	Feb 1991	Oct 1993	51	32	83
No. 12	Oct 1993	May 1997	Jan 1999	43	20	63
No. 13	Jan 1999	Nov 2000	Jan 2002	22	14	36
No. 14	Jan 2002	(Oct 2007)		(69)		

Note: For cycle no. 14, October 2007 peak reference date is assumed.
Source: Cabinet Office

Over the postwar era, the average recession has lasted 16 months. However, this includes many short recessions in the rapid growth era through the 1960s. If we start from the stable growth era of the 1980s, recessions have averaged 24 months in length. The current recession will also be roughly two years long if the next trough arrives as predicted in the second half of fiscal 2009. However, if overseas economies fail to recover, Japan's recession could easily extend as long as the post-bubble recession (32 months) or even the global recession after the second oil shock (36 months).

3. Forecast for Monetary Policy

At the BOJ Monetary Policy Meeting on October 31, 2008, the Bank lowered its target for the uncollateralized overnight call rate from 0.5% to 0.3%, noting that "adjustments in the world economy stemming from financial crises in the United States and Europe have further increased in severity," and citing the "decreased upside risks to inflation." Moreover, in order "to maintain accommodative financial conditions," the Bank also effected "a further increase in the flexibility of money market operations" by lowering the basic loan rate of the complementary lending facility from 0.75% to 0.50%, and introducing a complementary deposit facility (which pays interest on excess reserve balances) with a deposit rate of 0.1%. The overnight call rate is expected to stabilize between the 0.1% deposit rate and 0.5% loan rate.

At the meeting, the median outlook of board members called for real GDP growth of 0.1% in fiscal 2008 and 0.6% in fiscal 2009. However, new economic data for Q3 2008 makes negative growth almost certain in fiscal 2008, and the market consensus expects more negative growth in fiscal 2009.

Since recent economic data points to a sharp deterioration of the economy, we predict the Bank will be compelled to downgrade its economic assessment and outlook, and to lower the overnight call rate again from 0.3% to 0.1% in fiscal 2008. While our standard scenario sees no further changes through fiscal 2010, deteriorating conditions could trigger zero-interest rate and quantitative easing policies.

Exhibit 11 Forecast for the U.S.

(% change, unless otherwise noted)

	Fiscal year				FY 2008				FY 2009				FY 2010			
	2007	2008	2009	2010	4-6	7-9	10-12	1-3	4-6	7-9	10-12	1-3	4-6	7-9	10-12	1-3
		Forecast →					Forecast →		Forecast →				Forecast →			
Real GDP (seq. annualized)	2.0	1.2	−1.7	0.8	0.9	2.8	−0.5	−5.1	−2.8	−0.8	−0.3	0.2	0.9	1.6	1.8	2.0
Personal consumption (seq. annualized)	2.8	0.3	−1.8	1.4	0.9	1.2	−3.7	−4.1	−2.4	−0.6	0.5	1.2	1.5	1.9	2.0	2.3
Nonresid. fixed investment (seq. annualized)	4.9	2.2	−8.2	0.5	2.4	2.5	−1.5	−14.4	−11.5	−8.3	−5.8	−3.4	0.8	4.7	6.9	8.5
Residential investment (seq. annualized)	−17.9	−21.0	−13.5	3.6	−25.0	−13.3	−17.6	−23.5	−13.1	−9.0	−5.2	−1.4	4.1	9.1	13.6	13.5
Change in priv. inventories (contribution)	−0.4	−0.2	−0.1	0.1	−0.0	−1.5	0.6	−0.1	−0.3	−0.2	−0.0	0.0	0.1	0.1	0.2	0.2
Net exports (seq. annualized)	0.6	1.4	0.6	−0.4	0.8	2.9	1.1	0.6	0.9	0.5	−1.0	−0.7	−0.3	−0.3	−0.2	−0.5
CPI (seq. annualized)	2.9	4.0	−0.8	1.4	4.3	5.0	6.7	−6.0	−3.0	−1.0	0.8	1.4	1.6	1.8	1.9	2.0
Unemployment rate (avg)	4.6	5.8	7.8	8.4	4.9	5.3	6.0	6.8	7.2	7.7	8.0	8.2	8.3	8.4	8.5	8.5
Federal funds rate target (end)	4.25	0.50	0.25	1.00	2.25	2.00	2.00	0.50	0.25	0.25	0.25	0.25	0.25	0.25	0.50	1.00
10-year Treasury yield (avg)	4.6	3.7	2.9	3.8	3.7	3.9	3.8	3.3	2.5	2.7	3.0	3.5	3.6	3.7	3.8	3.9

Exhibit 12 Forecast for the Euro Area

(% change, unless otherwise noted)

	Fiscal year				FY 2008				FY 2009				FY 2010			
	2007	2008	2009	2010	4-6	7-9	10-12	1-3	4-6	7-9	10-12	1-3	4-6	7-9	10-12	1-3
		Forecast					Forecast →		Forecast →				Forecast →			
Real GDP (yoy change)	2.6	1.0	−0.8	0.6	2.1	1.4	0.6	−0.1	−1.1	−1.0	−0.8	−0.3	0.2	0.5	0.8	1.0
(seq. annualized rate)					2.7	−0.7	−0.8	−1.5	−1.2	−0.4	0.0	0.4	0.8	0.8	1.0	1.2
Domestic demand (yoy contribution)	3.2	0.9	−0.5	0.6	1.6	1.0	0.7	0.3	−0.6	−0.4	−0.8	−0.3	0.2	0.5	0.7	0.9
Private final consumption (yoy change)	1.6	0.3	−0.6	0.6	1.2	0.4	−0.0	−0.5	−0.8	−0.7	−0.7	−0.3	0.2	0.5	0.7	0.9
Fixed capital formation (yoy change)	4.4	1.5	−1.3	0.7	3.7	2.6	0.9	−0.6	−2.3	−1.5	−0.9	−0.4	0.2	0.6	0.9	1.1
External demand (yoy contribution)	0.3	0.1	−0.3	0.0	0.5	0.4	0.0	−0.3	−0.5	−0.6	−0.0	−0.0	0.0	0.0	0.0	0.0
HICP (yoy change)	2.1	3.3	1.4	1.8	3.4	3.6	3.8	2.4	1.7	1.4	1.0	1.6	1.7	1.7	1.8	1.8
Unemployment rate (avg)	7.4	7.5	8.2	8.6	7.2	7.4	7.5	7.7	8.0	8.2	8.3	8.4	8.5	8.6	8.6	8.6
ECB policy rate (end)	4.00	2.50	1.50	1.50	4.00	4.00	4.25	2.50	1.50	1.50	1.50	1.50	1.50	1.50	1.50	1.50
10-year govt. bond yield (avg)	4.2	4.0	3.4	3.7	3.9	4.4	4.2	3.6	3.2	3.3	3.4	3.5	3.6	3.7	3.8	3.8
EUR in USD (avg)	1.37	1.46	1.23	1.29	1.50	1.56	1.50	1.28	1.20	1.20	1.25	1.25	1.25	1.30	1.30	1.30
EUR in JPY (avg)	156	151	107	118	158	163	162	123	102	102	113	113	113	117	121	124

Exhibit 13　Forecast for Japan

(% sequential change, unless otherwise noted)

	Fiscal year				FY 2008				FY 2009				FY 2010			
	2007	2008	2009	2010	4-6	7-9	10-12	1-3	4-6	7-9	10-12	1-3	4-6	7-9	10-12	1-3
		Forecast →					*Forecast* →		*Forecast* →				*Forecast* →			
Real GDP (seq. change)	1.9	-0.9	-0.8	0.8	-1.0	-0.5	-0.4	-0.4	-0.1	-0.2	0.1	0.1	0.3	0.2	0.4	0.3
(seq. change annualized)					-3.7	-1.8	-1.7	-1.6	-0.5	-0.6	0.5	0.5	1.2	0.6	1.4	1.3
(yoy change)					0.7	-0.5	-1.5	-2.3	-1.4	-1.1	-0.5	-0.1	0.4	0.7	0.9	1.2
Domestic demand <contribution>	<0.7>	<-1.1>	<-0.3>	<0.6>	<-0.9>	<-0.3>	<-0.2>	<-0.1>	<-0.1>	<-0.1>	<0.1>	<0.1>	<0.2>	<0.1>	<0.3>	<0.3>
Private demand <contribution>	<0.5>	<-0.9>	<-0.6>	<0.5>	<-0.7>	<-0.2>	<-0.4>	<-0.2>	<-0.1>	<-0.1>	<-0.1>	<0.1>	<0.2>	<0.1>	<0.3>	<0.3>
Public demand <contribution>	<0.2>	<-0.2>	<0.2>	<0.1>	<-0.2>	<-0.1>	<0.2>	<0.1>	<0.0>	<-0.0>	<0.1>	<0.0>	<0.1>	<-0.0>	<0.0>	<0.0>
External demand <contribution>	<1.3>	<0.2>	<-0.4>	<0.2>	<-0.0>	<-0.2>	<-0.3>	<-0.3>	<-0.1>	<-0.0>	<0.0>	<0.0>	<0.1>	<0.1>	<0.1>	<0.0>
Private final consumption expenditure	0.9	0.1	0.7	0.7	-0.7	0.3	-0.2	0.1	0.4	0.2	0.1	0.2	0.2	0.1	0.2	0.2
Housing investment	-13.0	-2.0	2.0	0.3	-2.6	3.9	3.9	0.2	-0.8	-0.7	0.4	0.6	-0.2	-0.5	0.6	0.1
Business fixed investment	2.3	-4.6	-5.4	1.0	-2.1	-2.0	-2.6	-1.6	-1.4	-1.0	-0.6	-0.1	0.3	0.6	0.9	1.2
Government final consumption expenditure	2.2	0.1	1.5	1.0	-0.9	-0.3	1.1	0.5	0.2	0.0	0.7	0.1	0.4	-0.0	0.2	0.1
Public investment	-5.8	-4.3	-1.1	-1.9	-1.2	0.4	1.3	-0.6	-0.9	-0.4	0.1	-0.2	-0.8	-0.6	-0.6	-0.3
Exports	9.3	0.3	-4.5	3.0	-2.6	0.8	-2.8	-2.6	-1.2	-0.7	0.4	0.5	0.9	1.2	1.1	0.9
Imports	1.8	-1.4	-2.8	2.8	-3.0	2.3	-1.7	-1.3	-1.2	-0.7	0.2	0.6	0.9	1.1	1.1	1.1
Nominal GDP	1.0	-1.3	-0.5	0.1	-1.4	-0.7	0.7	0.2	-0.9	-0.4	0.6	0.3	-0.8	-0.1	0.7	0.6

Key Indicators

(% change, unless otherwise noted)

	Fiscal year				FY 2008				FY 2009				FY 2010			
	2007	2008	2009	2010	4-6	7-9	10-12	1-3	4-6	7-9	10-12	1-3	4-6	7-9	10-12	1-3
		Forecast →					*Forecast* →		*Forecast* →				*Forecast* →			
Domestic corporate goods price index (yoy change)	2.3	3.9	-3.6	0.6	4.9	7.1	2.8	0.9	-2.7	-6.1	-3.3	-2.1	-0.6	0.3	1.2	1.4
Consumer price index (yoy change)	0.4	1.3	-0.4	0.3	1.4	2.2	1.3	0.3	-0.5	-1.1	-0.4	0.2	0.2	0.3	0.3	0.4
CPI excluding fresh food (yoy change)	0.3	1.3	-0.5	0.3	1.5	2.3	1.3	0.2	-0.5	-1.1	-0.4	0.2	0.2	0.3	0.3	0.4
Current account balance (trillion yen)	24.5	19.3	22.0	20.9	19.2	13.7	20.8	23.4	22.3	19.0	23.3	23.4	21.5	18.5	21.7	21.8
Current account balance (as % of nominal GDP)	4.8	3.8	4.3	4.1	3.8	2.7	4.1	4.6	4.4	3.8	4.6	4.6	4.3	3.7	4.3	4.3
Unemployment rate (%)	3.8	4.1	4.7	4.7	4.0	4.1	4.0	4.3	4.5	4.7	4.8	4.9	4.9	4.8	4.7	4.6
Housing starts (millions)	1.04	1.10	1.16	1.15	1.12	1.13	1.07	1.07	1.12	1.17	1.17	1.17	1.16	1.15	1.15	1.15
Uncollateralized overnight call rate (end, %)	0.50	0.10	0.10	0.10	0.50	0.50	0.30	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10
10-year JGB yield (OTC quote, averge, %)	1.6	1.5	1.3	1.6	1.6	1.5	1.4	1.3	1.3	1.3	1.3	1.4	1.5	1.5	1.7	1.7
JPY per USD (average)	114	98	89	93	105	108	96	85	85	90	90	90	90	93	95	95
Oil price (CIF, USD/barrel, average)	78	89	50	65	109	130	63	53	50	50	50	50	60	60	70	70
Current profit (yoy change)	-3.3	-15.8	-4.5	3.4	-10.5	-22.4	-17.8	-13.7	-10.2	-6.1	-2.3	1.8	2.4	3.5	3.3	4.5

Sources: ESRI, *Annual Report on National Accounts*; METI, *Industrial Production Indices*; MIC Statistics Bureau, *Consumer Price Index*; MOF, *Financial Statements Statistics of Corporations*; others.