# Chapter I

# Japanese Economy and Labor Situation

## 1 The Current Status of the Japanese Economy and Its Future Prospects

### Overview: The "Lost Two Decades" after the Collapse of the Bubble and the Present State of the Japanese Economy

Taking a long-term view of Japan's economy, the real economy posted high growth of more than 5% in the second half of the 1980s. This high growth in the real economy was also reflected in financial and securities markets, as well as in the asset value of companies. With stock prices reaching an all-time high of ¥38,915 at the end of 1989, Japanese companies were acquiring foreign companies and assets, encouraged in part by the impact of the strong yen at a time when corporate mergers and acquisitions (M&A) were a major trend. In response to these moves, Japan was highly praised by other advanced nations as the world's number one. However, on reaching 1990, asset prices such as stock prices and land values immediately began to fall, and this decline was not stopped for a long time. Following this collapse of the so-called economic bubble, Japan entered a prolonged economic slowdown.

Thereafter, on at least three occasions to date, Japan has experienced deep recessions that could be described as the worst since the Second World War. Firstly, the decline in stock prices and land values that had been underway since 1990 eventually extended so far as to result in the bankruptcy of major financial institutions in November 1997, immediately after which a severe financial shrinkage began, which plunged Japan into a deep recession. Lending by financial institutions continued to decline sharply from 1998 and continued to fall for a long time, until a moderate increase reversed this process in mid-2005. Moreover, the unemployment rate (3.5% in November 1997) rose sharply in 1998, reaching 4.8% in June 1999, and the employment environment became more and more severe. In particular, with regard to the employment of those who had newly graduated from university, the period from graduation in around March 1994 to around 2005 is generally called the employment ice age, when it continued to be extremely difficult to find employment. The university graduate employment rate underwent a sustained decline from 66.6% for those graduating in March 1997, falling to 55.1% in March 2003.

The second recession occurred at the end of 2000 until the first half of 2002, when the financial shrinkage was still underway, caused by a worldwide recession in the field of semiconductors. Focusing primarily on electrical appliances, there was a major decrease in production in export-related areas of manufacturing industry; coupled with the deflationary effects of the financial shrinkage, this led to the unemployment rate beginning to rise from around May 2001, reaching 5.5% – the highest-ever rate – in June 2002 and again in August of that year. With regard to the job market for university graduates, as mentioned above, the job market for those graduating in March 2002 and March 2003 in particular was exceedingly harsh.

The third recession covers the period from September 2008, when the so-called "Lehman shock" (the bankruptcy of Lehman Brothers) took place, until the present day. From January 2002, the Japanese economy continued a moderate recovery (the period up to October 2007 alone became the longest since the war), and lending by financial institutions began to increase again from mid-2005, but from the end of 2007, in response to the worldwide economic slowdown, the economic situation became patchy. At this point in time, the Lehman Shock occurred. In Japan, exports of goods such as motor vehicles fell significantly, which led to a major decrease in production in machinery-related industries. This decrease in production swiftly spilled over into all industries, as a result of the interindustry-relation effect, becoming a very fast-paced recession that was the largest since the war, with the index of industrial production demonstrating a fall of 30% compared with the previous year toward the first half of 2009. In addition, as if to add insult to injury, the Great East Japan Earthquake occurred in March 2011, when the economy had not yet completely recovered from the Lehman Shock.

The Great East Japan Earthquake disaster initially caused catastrophic damage to production activity and employment in the Tohoku region; in particular, the suspension of operations by auto parts makers and others sparked a major supply shock to the Japanese economy and overseas markets. And although production subsequently made a quick recovery, thanks mainly to automobile manufacture, exports posted a year-on-year decrease for five successive months. Moreover, after the accident at TEPCO's Fukushima No.1 nuclear power plant, Japan's energy sources shifted significantly toward thermal power generation, leading to a massive increase in imports of crude oil and natural gas. As a result, Japan suffered a trade deficit for two successive years in FY2011 and FY2012 (Note 1).

From the second half of 2011, the yen reached a historically high value, triggered by the crisis of government debt in Greece and other southern European nations. This delivered a crippling blow to Japan's socio-economy, just as it was heaving under the weight of recovery and reconstruction measures after the Great East Japan Earthquake disaster. Although the economy had started to make a recovery of sorts after the disaster, this historically strong yen forced it back into recession for almost a year from the end of 2011.

Thus, over almost 20 years since the collapse of the bubble economy, Japan has been struck by a number of recessions. In recent years, apart from exceptions such as corporate profits, which have been achieving record highs, most economic indicators, including stock prices, GDP, capital investment, employee incomes and average wage levels, have either remained below the levels they were at in late 1997, when the financial shrinkage began, or are currently at levels below the 1997 levels after having exceeded them at one point. It is because of this that the period is referred to as the "lost decade" or the "lost two decades".

At the end of 2012, former Prime Minister Shinzo Abe was elected for a second term after a five-year hiatus. Now, at Abe's own initiative, the government set out an economic policy centered on "three pillars" (bold monetary policy, flexible fiscal policy and a growth strategy that encourages private investment), and is currently working to flesh out the specific content of this policy. Based only on the economic trends in the few months between the start of the new administration and the time of writing, the Abe administration's new economic policy – in tandem with the announcement of a plan for "an entirely new dimension of monetary easing" by the Bank of Japan's new Governor – has firstly brought a significant swing to a weaker yen on foreign exchange markets. The expectation that this will vastly improve corporate performance – particularly among export-related companies – has been welcomed by stock markets and triggered a rise in share prices, leading the economy toward a new phase.

## Financial Shrinkage being a Major Reason for the Prolonged Recession

Why has the recession (lost period) lasted so long? Opinions may differ from expert to expert, but in this author's view, the biggest reason lies in financial shrinkage.

At the time in the 1990's, amidst the progressive introduction of current value accounting, the major fall in asset prices was detrimental to the assets (stock) not only of financial institutions, but also of ordinary companies, and in order to deal with the reduction of excessive debt, they were compelled to achieve cost reductions (flow adjustment) by cutting back production and employment. This was the occurrence of the so-called "three excesses" (capacity, employment, debt).

With regard to this mechanism, it is currently a well-known phenomenon, with the term "balance-sheet recession" having been coined, but in the early 1990s, when the fall in asset prices had only just begun, there was no awareness in Japan of what this might bring about. As the economic growth rate had not decreased by a particularly great amount, there was not even any awareness that an economic slowdown had begun. Triggered by a book written by an expert, in the autumn of 1992, when about two and a half years had passed since the fall in asset prices had commenced, people started to be aware that an economic slowdown had begun that was different from those experienced hitherto. The delay in recognizing the recession might also be one reason why it became so prolonged.

However, it did not stop here. As stated above, stemming from the failure of major financial institutions at the end of 1997, financing shrank over a long period of time. Finance is truly the lifeblood of economic activity: it is behind all production activities, with the provision of operating capital (discounting of bills), as well, of course, as finance for capital investment. As a result of this shrinkage, economic activity itself was forced to contract, and a succession of companies went bankrupt.

With regard to the cause of financial shrinkage, firstly, it is related to the structure in which, unlike in the USA (Note 1), Japanese financial institutions held a large quantity of cross-owned company shares. The major decline in stock prices and land values resulted in a swift, large-scale deterioration in the financial situation of financial institutions. In addition, it was caused by finance provided to companies rapidly becoming bad debts due to the prolonged recession, and also by an impact from moves toward international finance-institutional reforms, through which financial institutions at that time were forced to strengthen their equity ratio. As well as speeding up the recovery of debts from companies, in order to ensure that the inevitable asset deterioration was not aggravated, these financial institutions curbed new lending to a significant degree (Note 2).

## The Economic Policy of the Government and the Bank of Japan and Structural Issues in the Japanese Economy

In response to these recessions, the government implemented a series of emergency economic measures. In addition to pump-priming government expenditure, the government used public funds (taxes) to introduce capital injections to financial institutions, in order to ensure that the deterioration of loan assets into bad loans and counter-measures to deal with this would not restrict the loan functions of these financial institutions.

Meanwhile, the Bank of Japan also promoted a zero-interest rate policy, particularly from the second half of the 1990s. After the turn of the century, it then promoted a policy of quantitative easing as a new financial policy (a measure to combat deflation) and provided commercial banks with vast amounts of liquidity.

After that, with a mild economic recovery underway, the Bank of Japan was seen to explore the possibility of an "exit policy", but up to the Lehman Shock, in the same way as the central banks of other advanced countries in the West, it adopted the unusual measure of widespread purchases not only of government bonds, but also of the securities of companies held by financial institutions, such as company bills, corporate bonds and CP, seeking to build up a supply of liquidity to the market.

However, despite these economic policies of the government and the Bank of Japan, the Japanese economy continued to experience low growth in the long term. It is believed that excessively low growth rates give rise to a vicious circle by causing the anticipated growth rate to decline, which brings about a structural stagnation in capital expenditure, as a result of which the low growth rate continues. In order to promote an internationally-competitive, technology-oriented nation, aggressive investment is essential (Note 3). Moreover, low growth not only causes increases in unemployment and wage stagnation, but also tears apart socioeconomic systems through such issues as the dissolution of employees' pension funds and health insurance unions by companies that cannot sustain the increase of costs due to the aging of the population, conjointly with operational deterioration resulting from low interest rates, or major decreases in the national pension scheme receipt rate.

Major issues can also be seen elsewhere in terms of the economic structure. The biggest issue is believed to be the delay in improving (reforming) the economic structure. This problem can be seen as being symbolic of the business strategy of Japanese companies against the strong yen and the resultant performance of the Japanese economy since the 1980s. With regard to the strong yen and the recession, many Japanese companies responded by transferring their production hubs overseas and implementing cost reductions and operational rationalization based on an approach of "selection and concentration". At that time, taking into consideration the fact that the rate of return on investment (investment efficiency) had been diminishing for a long time and that cost competition had become increasingly harsh due to the strong yen, this was rational behavior for companies. However, what remained as a result were an even stronger yen and the hollowing-out of domestic industry and employment. Rational behavior at the microeconomic level brought about even more deflationary tendencies and the contraction of domestic production at the macroeconomic level. What brought about the "fallacy of composition" was perhaps the fact that the government did not join together with the business community to create new industries and seek a strategic switchover in the industrial structure, and did not implement initiatives, either, that would lead to the development of projects that would attract businesses and investment from overseas utilizing yen being bought, although the government had such a plan. This is a problem that many experts have been united in pointing out.

Secondly, various labor problems will be taken up in detail in the chapters that follow, such as the hollowing-out of employment, the explosion in the number of non-permanent workers, long working hours concentrated at specific workers, and the long-term stagnation of wages; although they are problems that have emerged as a result of the deterioration of the economic situation, they themselves form one of the most serious economic problems facing Japan at present.

Thirdly, the economies of Japan's provinces are exhausted and stagnating. In combination with the deterioration of local government finances, it has also been affected by the fact that public investment has been on the decrease for a long time. The current state of the provincial economies is very serious and, as if to add insult to injury, the impact of the Great East Japan Earthquake is giving rise to even greater concern.

Finally, because a large quantity of government bonds were issued as part of the aforementioned fiscal stimulus, Japan's public bond balance increased dramatically from the 1990s onwards, reaching 1.98 times GDP in 2010 (incidentally, with regard to the figures for other countries, 0.93 times for the USA, 0.81 for the UK, 0.92 for France and 0.80 for Germany =OECD survey), giving Japan far and away the highest proportion among all advanced countries. Furthermore, government bonds account for more than 30-40% of the national budget in each fiscal year, and outstanding debt is rising further. The steep rise in the public bond balance is increasing the sense of anxiety about the future destabilization of government bond markets and whether it might not result in crowding out private capital investment funds.

## Recent Economic Trends and the Future Outlook

Recent trends in the Japanese economy were introduced briefly in the overview explanation at the start of this chapter. To close the chapter, the recent economic situation will be summarized in slightly more detail.

## The Immediate Post-Lehman Recession

In Japan, bank loans started to increase again from around the middle of 2005, when capital investments also turned the corner. By around the second half of 2008, GDP and capital investment were both approaching their levels before the financial shrinkage at the end of 1997. In employment, too, there were palpable signs of a long-awaited recovery; for example, the university graduate employment rate continued to rise significantly between 2006 and 2008 (both as of March 31). Then came the Lehman Shock.

The impact of the Lehman Shock dealt a severe blow to the global economy, including Japan. In Japan's case, however, the mechanism of the ensuing recession seems to have differed slightly from that in other developed nations, as explained below.

It all started with the failure of subprime loans (housing loans for low earners), the equivalent of a collapsed housing bubble, in the United States. Riding the prevailing global tide of financial instruments, these subprime loans had been securitized through complex combinations with a variety of securitized products, as a way of dispersing risk. These were then traded in large volume on the world's financial markets, ultimately leading to a loss of credit confidence that spread through the world's financial markets from around 2007. The downward spiral of confidence even affected blue chip securities, which began to lose value on the markets, until in September 2008, the major US investment bank Lehman Brothers went bankrupt. For a while after this, raging confusion on financial markets caused the entire financial system itself to cease functioning.

In other words, at the heart of the recession suffered by the US and Europe after the Lehman Shock lay financial shrinkage similar to that experienced by Japan from the end of the 1990s. For this reason, it is imagined that the deflationary effect on economic activity was both prolonged and relentless in the US and Europe. By contrast, Japanese financial institutions are thought to have held relatively small quantities of financial securities linked to US subprime loans. It would be fair to say, in fact, that hardly any shrinkage of finance (supply) was caused by financial institutions in Japan.

In that case, what made the recession in Japan increase in severity? The US recession had the effect of vastly reducing Japan's exports of automobiles and others, and this in turn caused a huge downturn in domestic production in Japan. Indeed, it was a recession caused by a fall in demand. Production output by Japan's auto manufacturing industry is relatively large, and in terms of its structure, it has strong input-output connectivity with many other industries and trades, with a broad base of supporting industries. For this reason, a decline in production due to falling export demand had wide-ranging implications for Japan's economy as a whole.

As will emerge in subsequent chapters, the Lehman Shock not only caused mass unemployment and redundancies, but also gave rise to many social problems. Firstly, many day laborers dispatched to manufacturing industries were laid off, but because workers who had moved out of company housing could not afford apartment rents, many of them started to camp out at Internet cafés and public parks in cities. This so-called "haken-mura" (temp workers village) problem later triggered a sudden increase in applications for livelihood support benefits, creating a huge political headache. Meanwhile, the employment environment for school leavers and young people had been expected to turn upwards, due to ongoing mass retirements by the "baby boomer" generation from 2007 onwards. However, the numbers hired fell sharply, ushering in another harsh employment environment.

## The Impact of the Great East Japan Earthquake Disaster on Japan's Economy

Before the economy could fully recover from the Lehman Shock, the Great East Japan Earthquake disaster struck.

Worst hit by the disaster was the Tohoku region. Home to suppliers of materials and parts in the manufacturing industry, this region is a vital supporting framework for Japan as a nation of technology. The damage suffered by these manufacturers made it difficult for them to supply parts and other essential products to other companies, including some overseas, leading to suspended production and a drastic decline in utilization ratios. The Tohoku region is also one of Japan's most important centers for agriculture and fishery. The destruction of production sites and the ensuing radiation pollution caused a sharp fall in agricultural and fishery produce, or even halted shipments altogether. This not only confronted farmers in Tohoku with massive financial losses, but also led to confusion and significant impact on markets and ordinary households all over Japan.

With regard to production, domestic production suffered a historically large decrease in March 2011; the month-on-month decline of 16.2% was the worst for a single month since statistical records began. This just reveals how greatly suspended operations by auto part makers and others affected the supply of goods in the early stages after the Great East Japan Earthquake disaster.

After that, however, production recovered rapidly. It would be fair to say that such rapid recovery was brought about by the efforts of industries and individual companies, which supported each other in seconding employees to damaged affiliates and working hard to locate new sources of parts. Corporate bankruptcies in the Tohoku region increased at a heightened tempo for a while after the disaster, but since many of the affected companies were parts manufacturers and others supplying producers all over Japan, disaster-related insolvencies were spread across the whole country, rather than being concentrated in Tohoku. Furthermore, the SME Financing Facilitation Act, initially enacted as temporary legislation applicable with a time limit of one year, has so far been extended by about three years through two extensions by March 2013. This has assisted many small and medium enterprises. Thanks to these various supporting factors, domestic production activity appears not to have fallen into such a severe situation as was initially feared, and has thus been able to overcome the impact of the Great East Japan Earthquake disaster.

Where, then, did the problems occur? Firstly, in the international balance of payments. After the accident at TEPCO's Fukushima No.1 nuclear power plant, imports of crude oil and natural gas suddenly increased, causing the trade balance to fall into the red.

Moreover, the impact on agriculture, fisheries and dairy farming was by no means small, including their market conditions. As noted above, the Tohoku region is home to some of Japan's most important fishing grounds, and many of these were destroyed by the massive tsunami, or buried in rubble. Refrigeration and other facilities at fishing ports were also destroyed, making fishery activity impossible for a considerable time. At the time of writing, landed catches have yet to return to pre-disaster levels in a number of fishing ports. Meanwhile, shipments of rice, vegetables, beef, tea leaves and other produce were forcibly suspended whenever contamination by radioactive substances was discovered. They could only be resumed when the government declared them safe, in line with the Act on Special Measures Concerning Nuclear Emergency Preparedness. Even after resumption had been permitted, damaging rumors caused a protracted and ongoing slump, with wholesale prices for dressed carcasses falling to around half of the previous year's level. Combined with other damaging factors, this caused enormous economic hardship to farmers (Note 5).

## The Current State of Japan's Economy under "Abenomics"

As briefly mentioned in the overview at the beginning, the policies espoused by the Abe administration from the end of 2012, in tandem with bold monetary easing by the Bank of Japan, have at the time of writing caused a significant swing toward a weaker yen and higher share prices.

What is actually going on in Japan at the moment? At least as far as this author is concerned, the aims of the economic policy set out by the new Abe administration appear to have had a positive impact on forward sentiments by investors and the public (known in economics as "expectation"). This in itself is of immense significance. This is because, as stated above, Japan has experienced repeated recessions and a long period of continuously low growth over the last 20 years or so. As a result, the sentiment that there could not possibly be a major leap forward or growth in the economy for the foreseeable future (i.e. an extremely low expected growth rate) has taken a firm hold within the national consciousness. Private capital investment, the driving force behind economic growth, has been stagnant over the long term. This is partly because the cooling down of expectation has made investors and companies feel pessimistic about future business prospects and put a brake on investment. It is also because there was a certain amount of "capital flight" overseas.

The economic policy of the Abe administration–based on the three central pillars of bold monetary policy, flexible fiscal policy and a growth strategy that encourages private investment–has been dubbed "Abenomics". While it has had a positive impact on people's expectations, Abenomics has sparked a degree of controversy among economists. Firstly, the Abe administration has asked the Bank of Japan to boost inflation, as if deflation were the cause of recession. In response, the Bank of Japan, under its new Governor, recently decided to instigate a 2% rise in consumer prices by two years from now (Note 6). But did deflation really cause the recession? Based on the rationale that deflation arises from economic activity, this economic policy would appear theoretically flawed. Secondly, is it actually possible to inflate prices through financial policy alone? An important point here is that quantitative easing itself has already been promoted for some considerable time. Even if not a "new dimension", private company bonds, CPs and other financial instruments not conventionally bought by the BOJ have been purchased in large volume as an "exceptional measure". As detailed in Note 7, the base money supply has grown to considerably large proportions. As far as this author is concerned, whether it will after all lead to an increase in capital demand by private companies, and particularly an increase in capital investment, seems an important point; this very point, one feels, will define whether Abenomics will be successful or not.

The economic policy of the Abe administration is now entering a decisive phase in determining whether it will be successful or not. Attention will be on the outcome of the "three pillars" from now on (Note 8).

Notes:

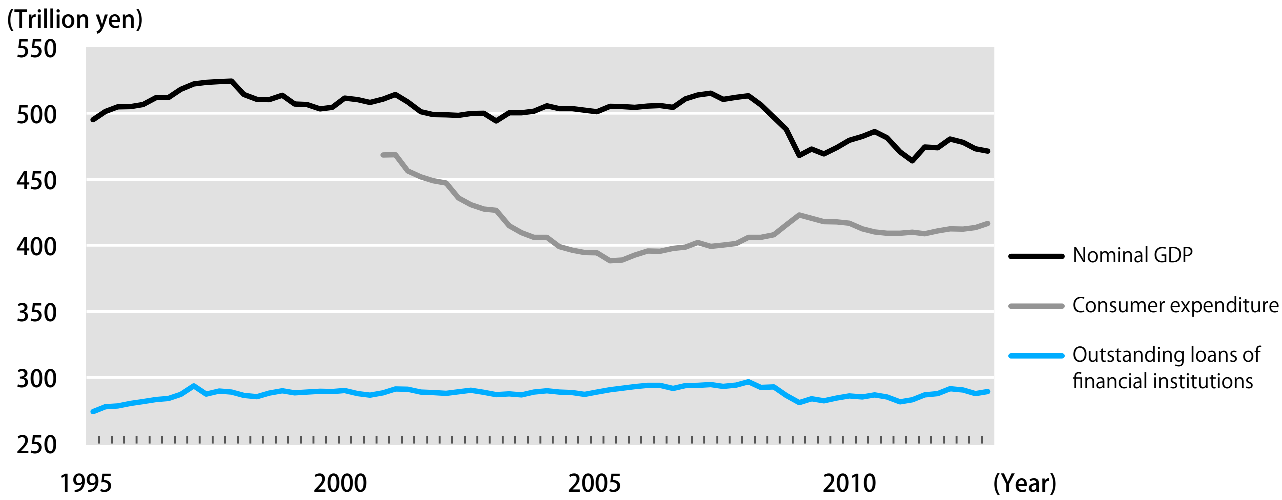
1. In Japan, the surplus in the income balance, one of the components of the current account (the balance between outgoing and incoming revenues between domestic firms and overseas subsidiaries, affiliates, etc.), has vastly expanded since around 2004. Since FY2005, it has exceeded the surplus in the trade balance, another component of the current account. As this situation is still continuing today, the current account has not fallen into the red even if the trade balance has gone into deficit recently.
2. In the USA, as early as 1933, immediately after the Great Depression, the Glass–Steagall Act was enacted, prohibiting commercial banks from investing in company shares, which was one of the causes of the depression, to achieve the separation of duties by bank type.
3. The outstanding loans of financial institutions continued to decrease from late 1997 to mid-2005. Usually, a decrease in stock data is an extremely abnormal economic phenomenon.
4. The economist J. A. Schumpeter argued in his Theory of Economic Development, the original of which was in German translated under this title in the English version, that creative destruction and innovation have an important role to play in economies. In addition, at the same time, he emphasized that credit creation is vital to innovation. In relation to this paper, which also refers to financial shrinkage, this will be a crucial point that we ought to recall.
5. A word should be added on the state of recovery and reconstruction after the Great East Japan Earthquake disaster. At the time of writing, it is already two years since the disaster struck. Although the government and affected local authorities have completed their initial disaster response measures, the reconstruction effort has yet to start in earnest. This situation was partly affected by problems in the government's administrative procedures and structures. In some more serious cases, the affected authorities were unable to formulate plans for reconstruction promotion and development stipulated by the government, because they had no employees capable of working out a blueprint and concept for reconstruction needed to start the reconstruction work. This has consequently delayed the reconstruction effort as a whole. On the other hand, delays have also arisen in some local authorities ravaged by the massive tsunami because it is taking time to secure candidate land for relocation to higher ground. Thus, the reconstruction work is generally taking much longer than expected, and the disaster-affected residents are also unhappy with delays in the recovery effort. Following the explosion at TEPCO's Fukushima No.1 nuclear power plant in Fukushima Prefecture, meanwhile, residents living near the plant were forced into temporary evacuation to avoid radiation exposure, but some of these still do not know when they will be able to return to their homes. This is further hampering the progress of countermeasures.
6. At the same financial policy decision meeting at the beginning of April 2013, it was also decided that the balance of base money supplied to the market by the Bank of Japan (see Note 7 below) would be doubled over the next two years. This would be done by expanding the objects of government bond purchase from previous levels (by including bonds with more than two years left to maturity, but sometimes also 10-year, 20-year and other very long-term bonds), and purchasing risk assets such as ETFs (index-linked exchange-traded funds) and REITs (real estate investment trusts) owned by private financial institutions, among other moves. At a press conference after the meeting, the new Governor is said to have termed these decisions collectively as "an entirely new dimension of monetary easing".
7. As one instrument of financial policy, base money (the sum of the balance of bank notes issued by the Bank of Japan and reserves deposited by commercial banks in the Bank of Japan (current deposits)) has itself been "piled up" at quite a high tempo over the last few years (see Table 1; the rate of increase was more than 6 % year-on-year from the beginning of 2009 and more than 5 % from the second half of 2010 following the renewed economic slump, and has continued to post two-digit increases since the Great East Japan Earthquake disaster in March 2011). However, the balance of deposits in commercial banks (M2, M3, etc.) has only increased by around 2%. The basic reason for this is that, even if financial institutions allocate their increased capital specifically to purchasing government bonds, etc., the increased capital is not being linked to loan for capital investment and operating capital for private companies.
8. As far as the author is concerned, the priority should above all be on fiscal discipline. If the market were to lower its valuation of Japanese government bonds, it would cause huge write-downs and asset deterioration in private financial institutions, and the financial shrinkage starting in 1997 could be repeated. However, an important point that most clearly distinguishes this situation from that one is that even the Bank of Japan now owns massive volumes of government bonds exceeding 100 trillion yen. If the government bond market were to fall significantly, the Bank of Japan would also suffer a certain appraisal loss. This would almost certainly cause mass confusion on financial markets, and in that situation, would the Bank of Japan be able to adequately fulfil its given role as the ultimate provider of finance? Partly to avoid this kind of situation, ensuring the greater soundness of fiscal discipline is just as important to Japan's economy today as flexible fiscal policy, if not more so.
   Three points should be mentioned in this regard. Firstly, there have been media reports of ongoing confusion in the government bond

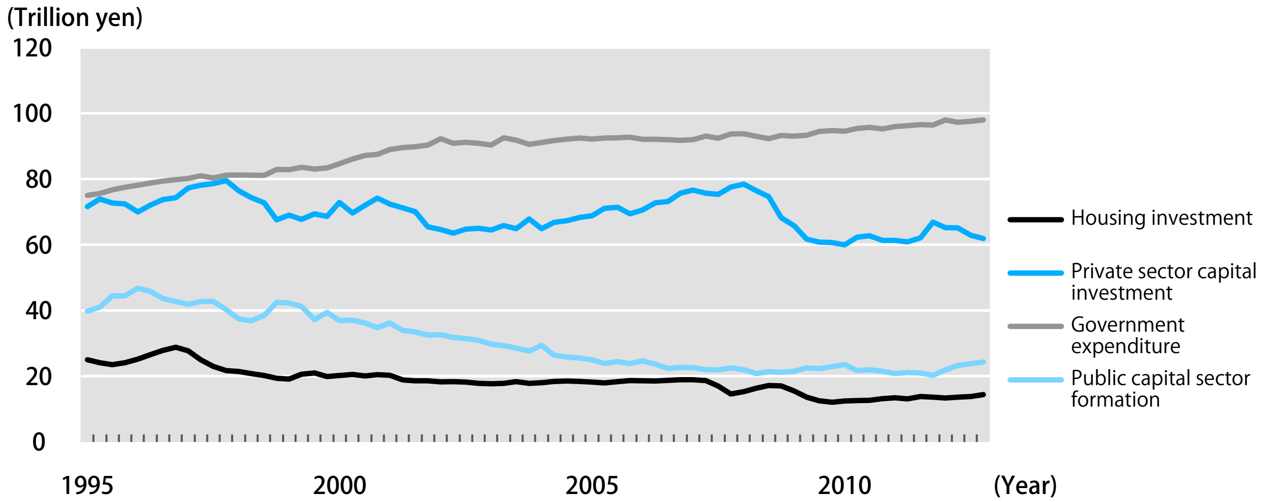
market over the last few weeks. This demands some scrutiny. Is it merely, as reported in the media, a case of confusion because, for example, the structure of pre-maturity terms for government bonds subject to bidding is different to what it used to be? Or is it a sign that this "new dimension of monetary easing" by the central bank is no longer welcome, from the viewpoint of various financial institutions? The new Governor has apparently asserted a stance of valuing "dialog" with the market, and it will be indeed being challenged.

Secondly, there are also media reports that, given the current ultra-low interest rates, issues of corporate bonds have been increasing over the last month or two, mainly among large corporations, or that more companies are considering making issues. In itself, this situation is very similar to that back in early 1987, when many companies suddenly started promoting equity finance (raising capital by issuing new shares). At the time, the capital raised was appropriated to buying land and shares. This time, as well as having learnt the lessons of the asset bubble, cross-holding of shares between companies has been vastly reduced, while capital procurement based on corporate bonds is unlike that based on shares. For these reasons, the situation will probably not develop in the way it did back then. Nevertheless, still other media reports suggest that many large corporations took advantage of the historically strong yen to carry out mergers and acquisitions (M&A) of overseas companies, while the recovery of corporate earnings over the last few years has helped large corporations to pay off a lot of their interest-bearing debts. In light of this, a matter of keen interest is how the capital raised through bond issues will be used.

Thirdly, talk of the trade balance going into deficit is somewhat worrying in connection with the government bond market. A negative trade balance causes a decrease in currency supply coming into the country. For this reason if none other, under the situation that financial institutions may feel less inclined to purchase government bonds, for example, it is not beyond possibility that, seen overall, this could cause a squeeze on capital entering the government bond market.

**Figure I-1 Developments in GDP, Capital Investment and the Outstanding Loans of Financial Institutions (All Nominal Values)**

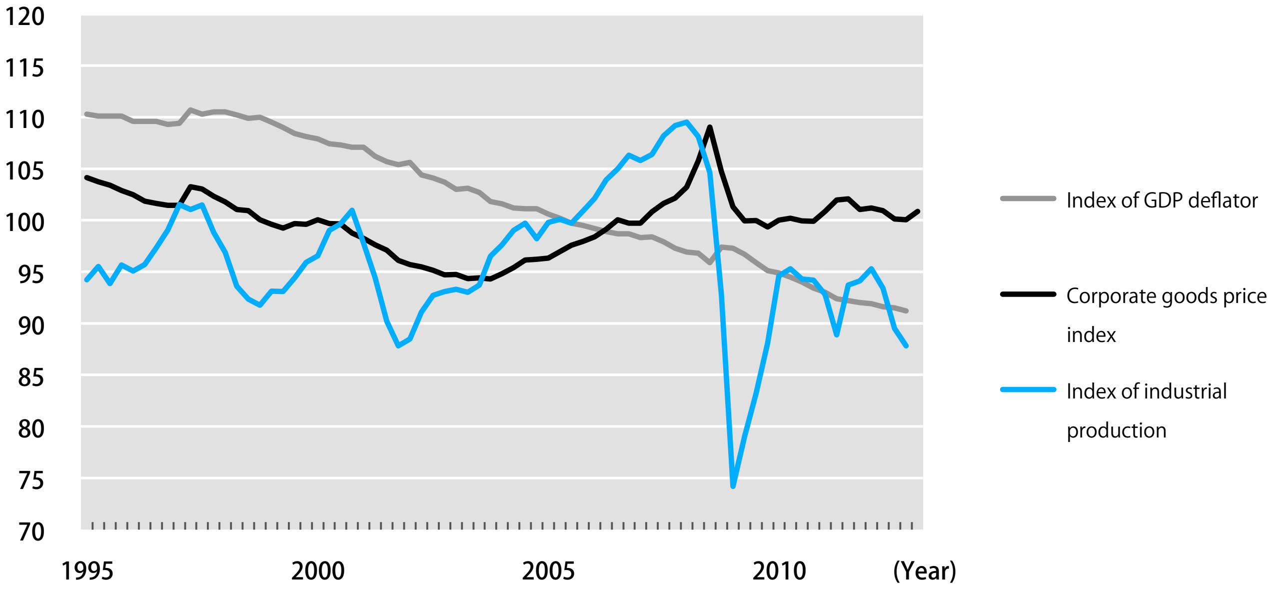



Note: Nominal GDP and each component element are seasonally-adjusted figures for each quarter. The figures for outstanding loans of financial institutions were compiled from the three-monthly average of the monthly data. In addition, it was not possible to obtain data for the outstanding loans of financial institutions before the October-to-December period 2000 on the Bank of Japan website.

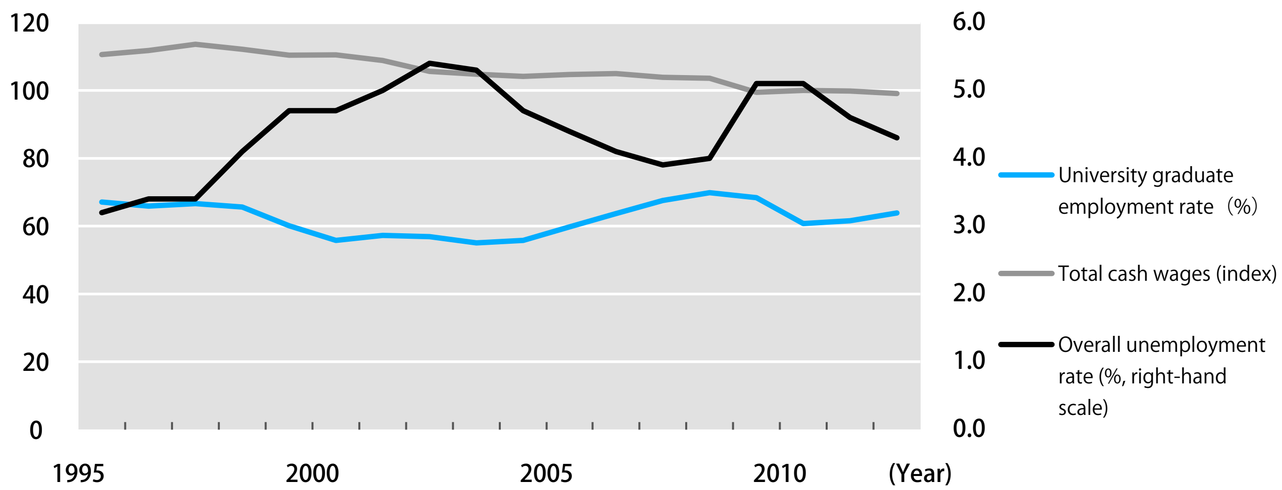
(Continued)

## Figure Ⅰ-2 GDP Deflator, Corporate Goods Prices and Industrial Production Indices (Seasonally Adjusted for Each Quarter)




Note: GDP deflator and industrial production indices are based on 2005 average = 100; corporate goods price index is based on 2010 average = 100

## Figure Ⅰ-3 Labor-related Indicators




Note: In the index for total cash wages, 2010 average = 100

## Table I-4 Trends in the Trade Balance, Share Prices, the Yen Exchange Rate and Other Indicators after the Great East Japan Earthquake Disaster

| | Trade balance (100 million yen) | | Nikkei stock average (month-end closing price; yen) | Yen rate (Tokyo Inter-bank, central rate vs US $, monthly average | Corporate bankruptcies (year-on-year; % ) | Base money (year-on-year; % ) | Money supply (M2) (year-on-year; % ) |
|---|---|---|---|---|---|---|---|
| | | Exports (y-o-y change; % ) | | | | | |
| 2011.1 | - 3,994 | 2.89 | 10,237.92 | 82.63 | 2.85 | 5.5 | 2.3 |
| 2 | 7,203 | 9.71 | 10,624.09 | 82.53 | - 8.49 | 5.6 | 2.4 |
| 3 | 2,368 | - 1.36 | 9,755.10 | 81.79 | - 9.32 | 16.9 | 2.6 |
| 4 | - 4,120 | - 12.66 | 9,849.74 | 83.35 | - 0.62 | 23.9 | 2.7 |
| 5 | - 7,713 | - 9.78 | 9,693.73 | 81.23 | 9.67 | 16.2 | 2.7 |
| 6 | 1,299 | - 1.02 | 9,816.09 | 80.51 | - 5.53 | 17.0 | 2.8 |
| 7 | 1,418 | - 2.26 | 9,833.03 | 79.47 | 5.12 | 15.0 | 3.0 |
| 8 | - 6,903 | 4.15 | 8,955.20 | 77.22 | 0.52 | 15.9 | 2.7 |
| 9 | 3,723 | 3.01 | 8,700.29 | 76.84 | - 10.18 | 16.7 | 2.7 |
| 10 | - 2,089 | - 2.74 | 8,988.39 | 76.77 | - 5.63 | 17.0 | 2.8 |
| 11 | - 5,889 | - 3.06 | 8,434.61 | 77.54 | 3.85 | 19.5 | 3.0 |
| 12 | - 1,468 | - 6.95 | 8,455.35 | 77.85 | - 8.85 | 13.5 | 3.2 |
| 2012.1 | - 13,897 | - 8.49 | 8,802.51 | 76.97 | - 2.56 | 15.0 | 3.1 |
| 2 | 953 | - 1.95 | 9,723.24 | 78.45 | 10.41 | 11.3 | 2.9 |
| 3 | - 12 | 7.29 | 10,083.56 | 82.43 | - 0.10 | - 0.2 | 3.0 |
| 4 | - 4,371 | 11.13 | 9,520.89 | 81.49 | - 7.53 | - 0.3 | 2.6 |
| 5 | - 8,049 | 11.56 | 8,542.73 | 79.70 | 5.08 | 2.4 | 2.2 |
| 6 | 1,122 | - 1.46 | 9,006.78 | 79.32 | - 12.59 | 5.9 | 2.3 |
| 7 | - 3,761 | - 7.45 | 8,695.06 | 79.02 | - 2.28 | 8.6 | 2.3 |
| 8 | - 6,636 | - 5.25 | 8,839.91 | 78.66 | - 12.18 | 6.5 | 2.4 |
| 9 | - 4,747 | - 10.54 | 8,870.16 | 78.17 | 0.59 | 9.0 | 2.4 |
| 10 | - 4,513 | - 5.98 | 8,928.29 | 78.97 | 6.07 | 10.8 | 2.3 |
| 11 | - 8,508 | - 4.04 | 9,446.01 | 80.87 | - 3.40 | 5.0 | 2.1 |
| 12 | - 5,723 | - 6.89 | 10,395.18 | 83.64 | - 4.74 | 11.8 | 2.6 |
| 2013.1 | - 14,798 | 6.76 | 11,138.66 | 89.18 | - 10.20 | 10.9 | 2.7 |
| 2 | - 6,713 | - 3.31 | 11,559.36 | 93.21 | - 12.09 | 15.0 | 2.9 |
| 3 | - 2,224 | 0.33 | 12,397.91 | 94.75 | - 19.62 | 19.8 | 3.1 |