



ORGANISATION FOR ECONOMIC
CO-OPERATION AND DEVELOPMENT

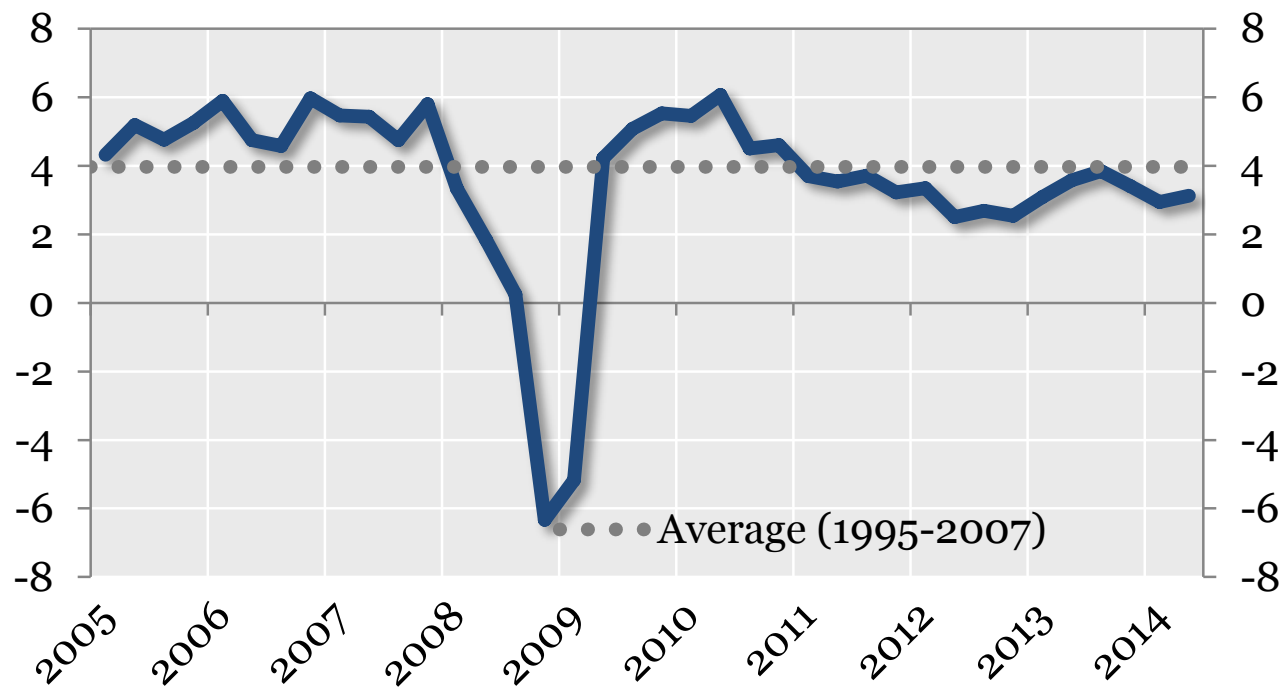
OECD Economic Outlook

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Head, Japan/Korea Desk
November 2014



The global economy is stuck in low gear

World GDP growth
Per cent, seasonally-adjusted annualised rate



Source: Preliminary November 2014 Economic Outlook database.

Trade growth has been weak

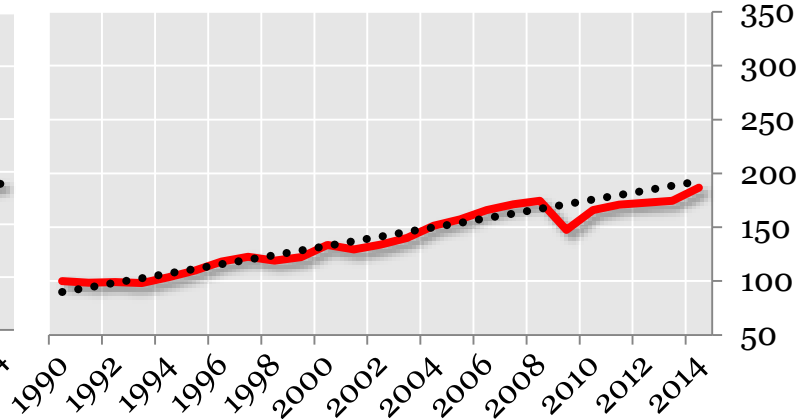
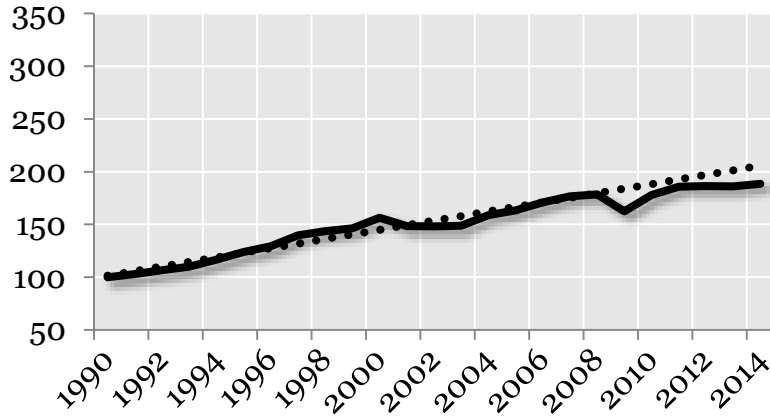
Trade intensity¹

Index, 1990=100

.....Trend (1990-2007)

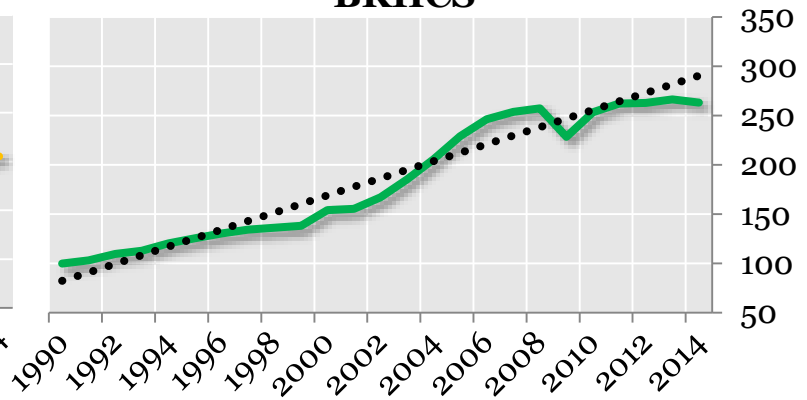
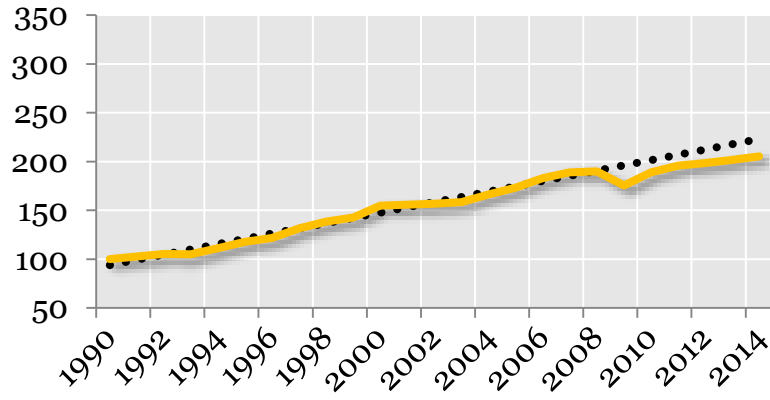
United States

Japan



European Union

BRIICS



1. Index of sum of exports and imports as a ratio of GDP.

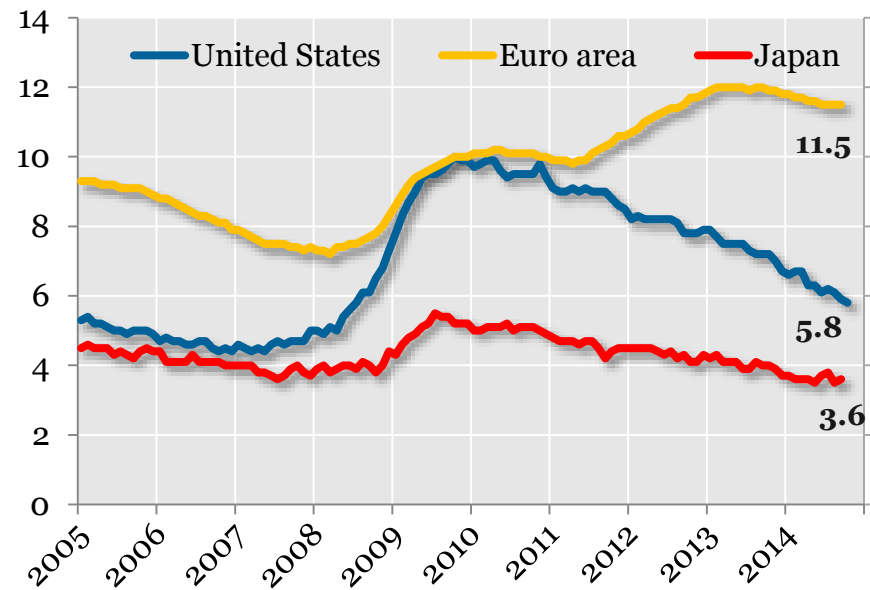
Source: Preliminary November 2014 Economic Outlook database.



Labour market: divergent performance, but overall slack remains

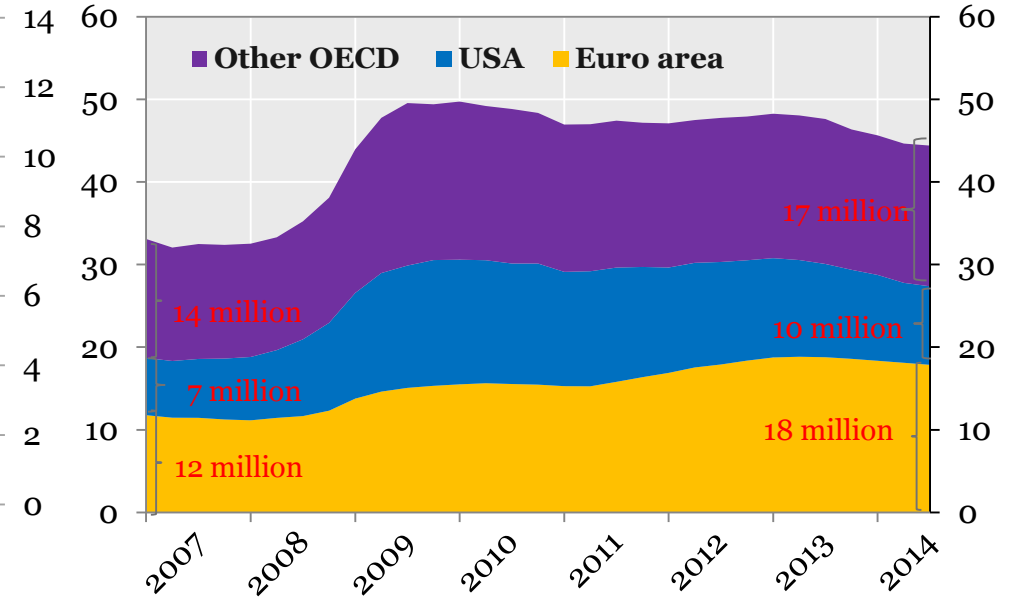
Unemployment rate

Per cent



Number of unemployed persons

Millions



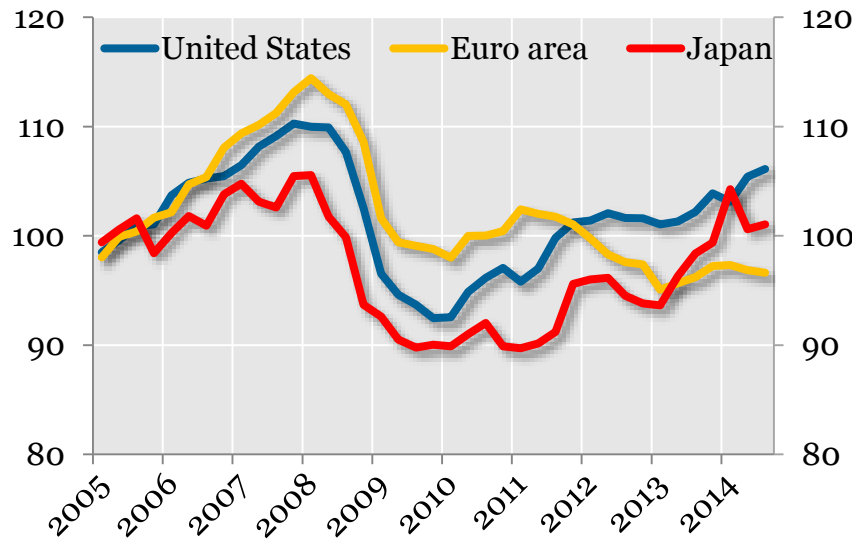
Source: Preliminary November 2014 Economic Outlook database.



Demand patterns are diverging in major advanced economies

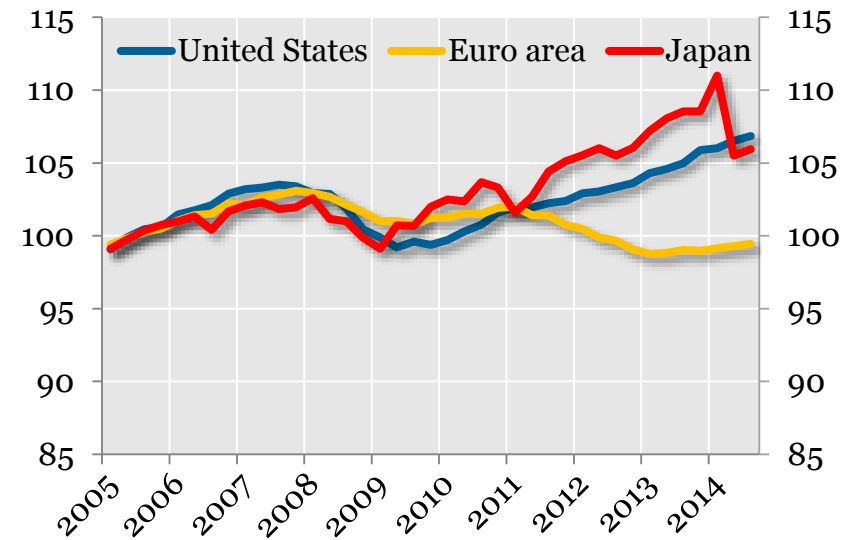
Non-residential investment per capita

Index, 2005 = 100



Private consumption per capita

Index, 2005 = 100

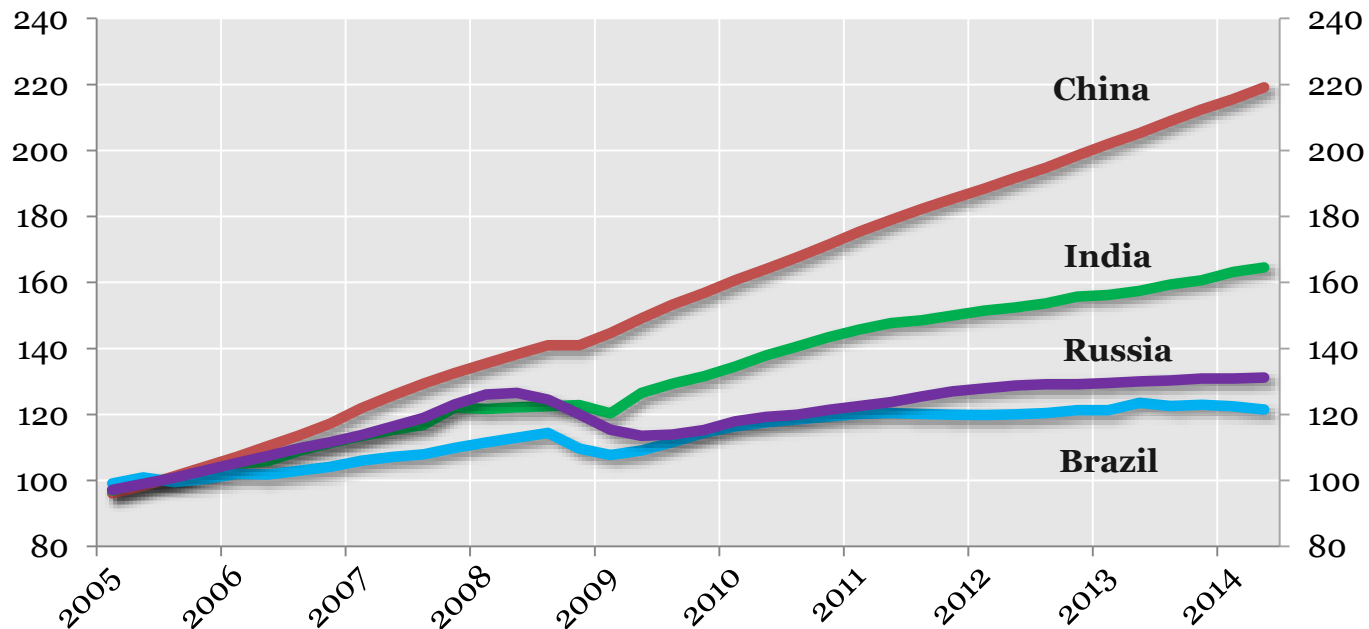


Source: OECD national accounts database; Preliminary November 2014 Economic Outlook database; and OECD calculations.



Trends are also diverging among emerging economies

GDP per capita
Volume, 2005=100



Source: OECD National Accounts database; Preliminary November 2014 Economic Outlook database; IMF WEO database; Central Statistical Organisation, India; and OECD calculations.



Growth projections for 2015-16

GDP

Volume, percentage change

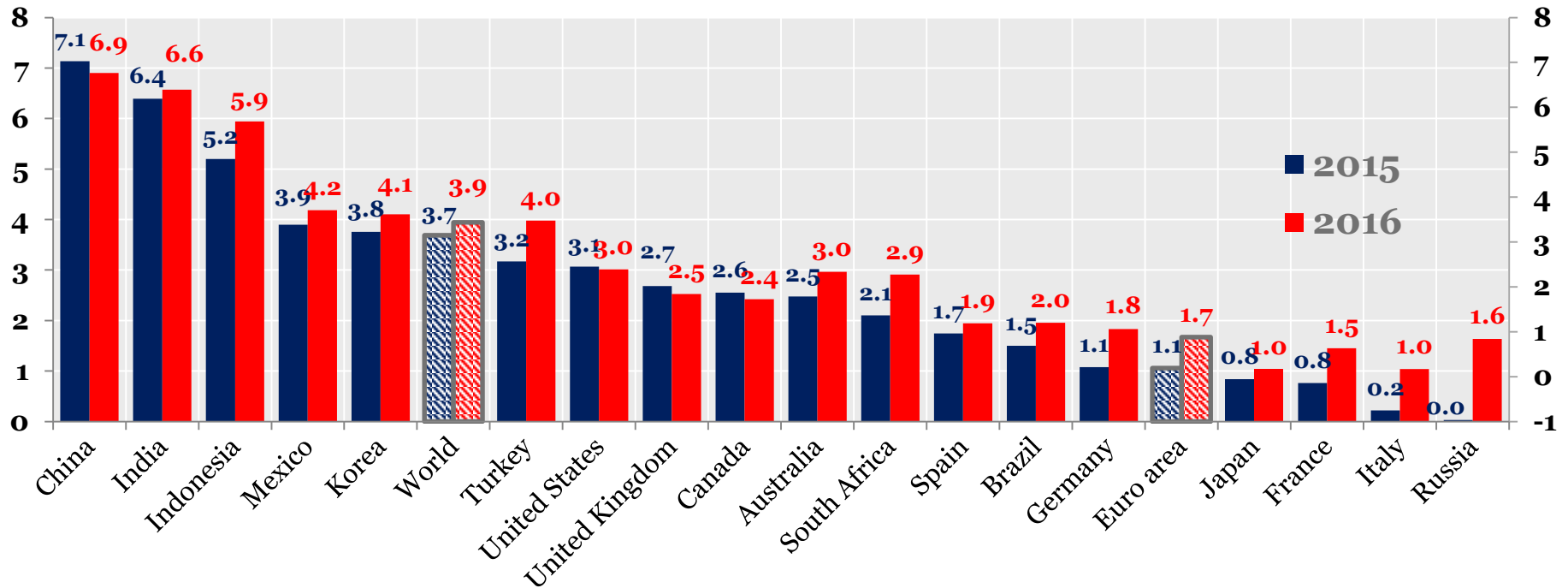
	2013	2014	2015	2016
World	3.1	3.3	3.7	3.9
United States	2.2	2.2	3.1	3.0
Euro area	-0.4	0.8	1.1	1.7
Japan	1.5	0.4	0.8	1.0
China	7.7	7.3	7.1	6.9
India	4.7	5.4	6.4	6.6
Brazil	2.5	0.3	1.5	2.0
Russia	1.3	0.3	0.0	1.6

Source: Preliminary *Economic Outlook* (EO) projections.



Growth projections for 2015-16

GDP growth Per cent



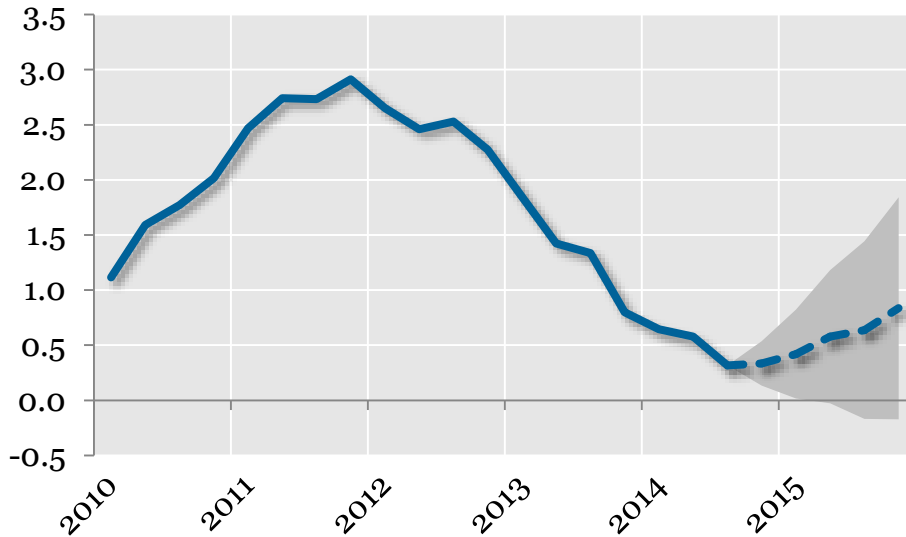
Source: Preliminary November 2014 OECD Economic Outlook database.



The threat of euro area stagnation has risen

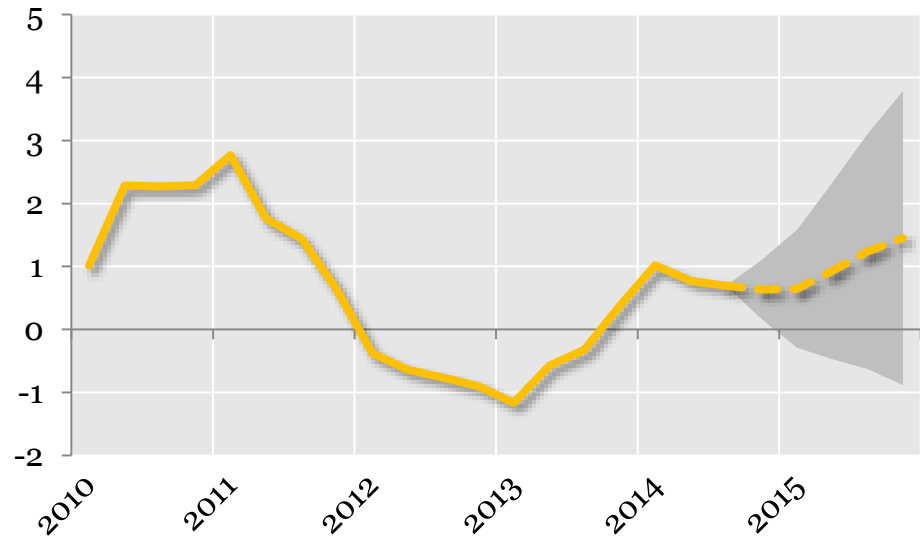
Inflation

HIPC, 12-month percentage change



GDP

Year-on-year percentage change



Note: Shaded bands show +/- one standard deviation based on past variation.

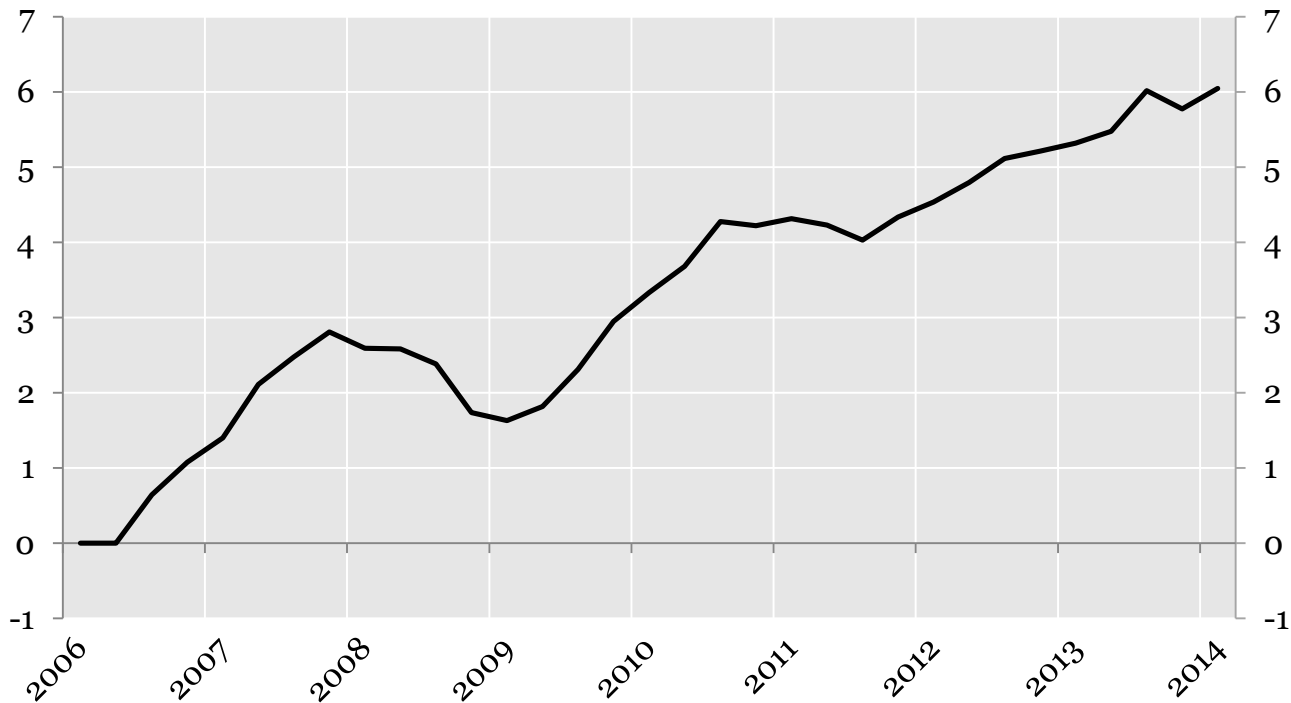
Source: Preliminary November 2014 Economic Outlook database.



The strong net portfolio inflows to emerging economies could reverse

Cumulative net portfolio inflows to BRIICS excluding China

Per cent of GDP, from Q1 2006



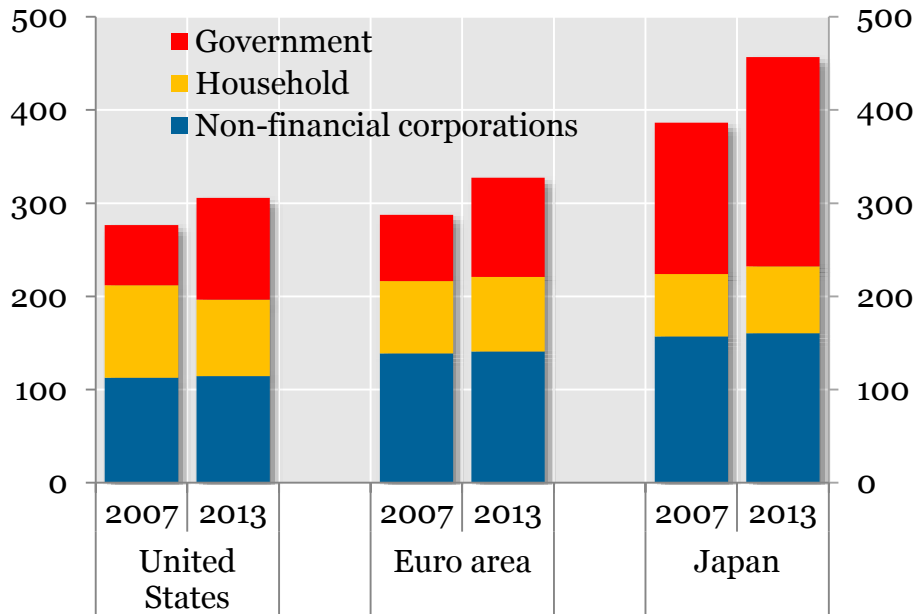
Source: IMF Balance of Payments database; OECD National Accounts database; and OECD calculations.



Advanced economy debt levels are high and credit growth in China is rapid

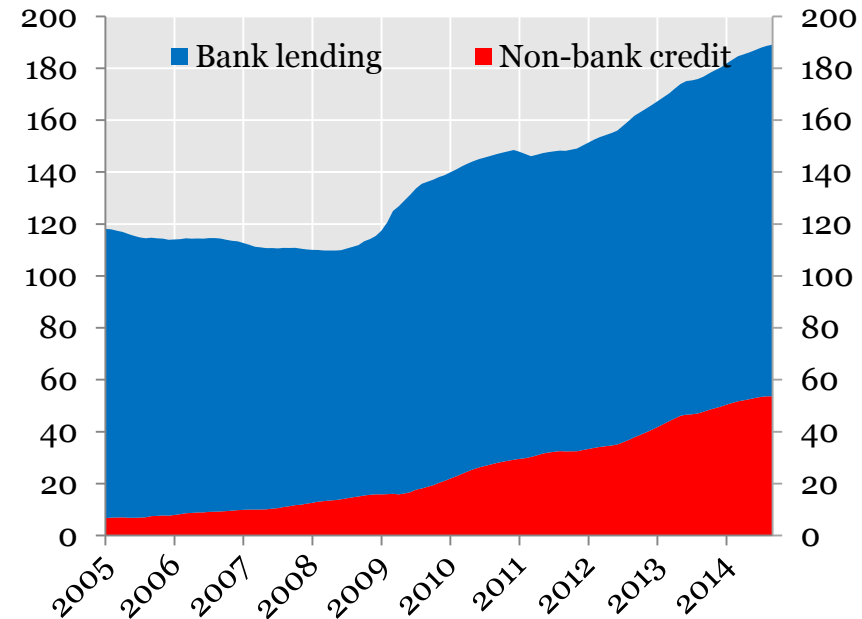
Debt excluding the financial sector

Per cent of GDP



China: credit to non-financial private sector

Per cent of GDP

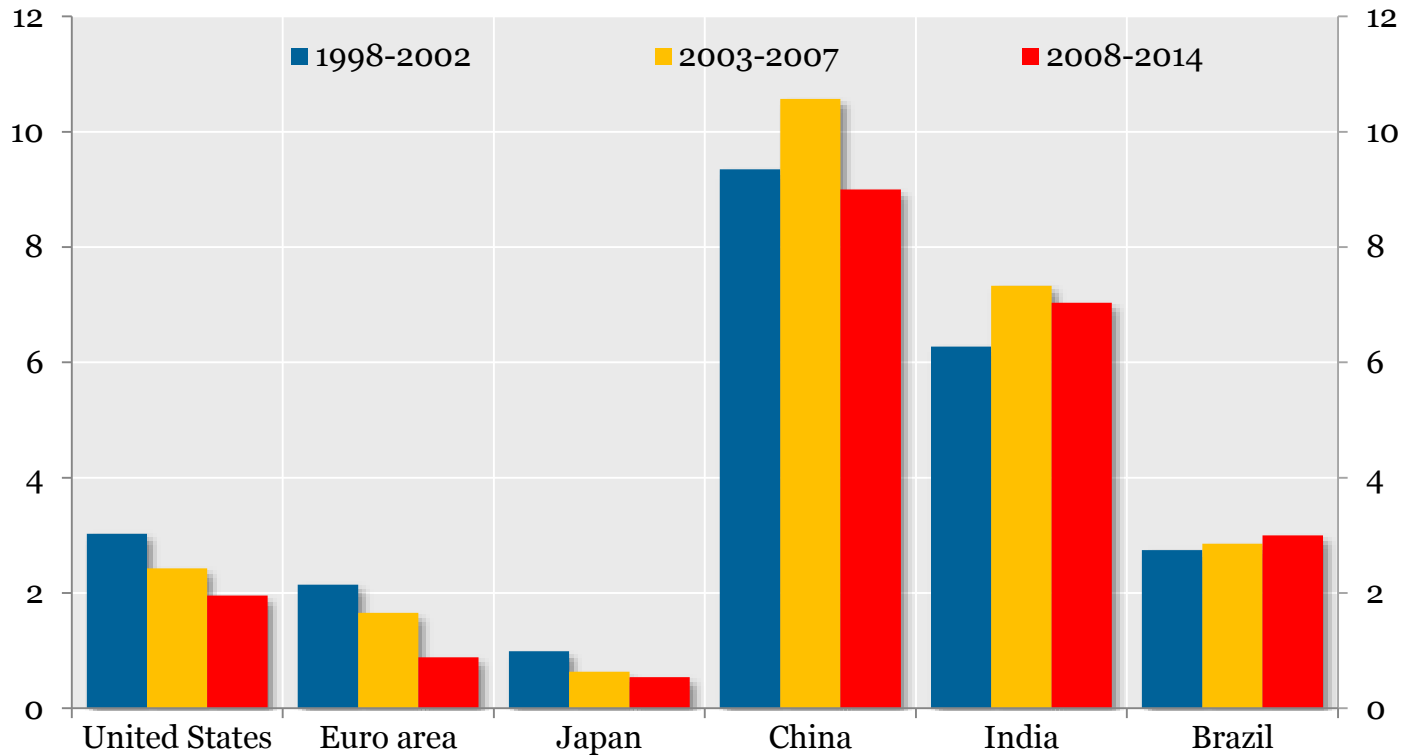


Source: Preliminary November 2014 Economic Outlook database; ECB; OECD Financial accounts; and BIS.



Potential growth rates could fall further

Potential GDP growth *Annual average, per cent*



Source: Preliminary November 2014 OECD Economic Outlook database.



Key messages

Global growth is modest, with widening differences across countries

Financial risks are rising and volatility is set to increase

Potential growth has slowed, interacting with weak demand

Weakness in the euro area is a major concern

Monetary, fiscal and structural policies must all be employed to address risks and support growth



Monetary, fiscal and structural policies need to support growth

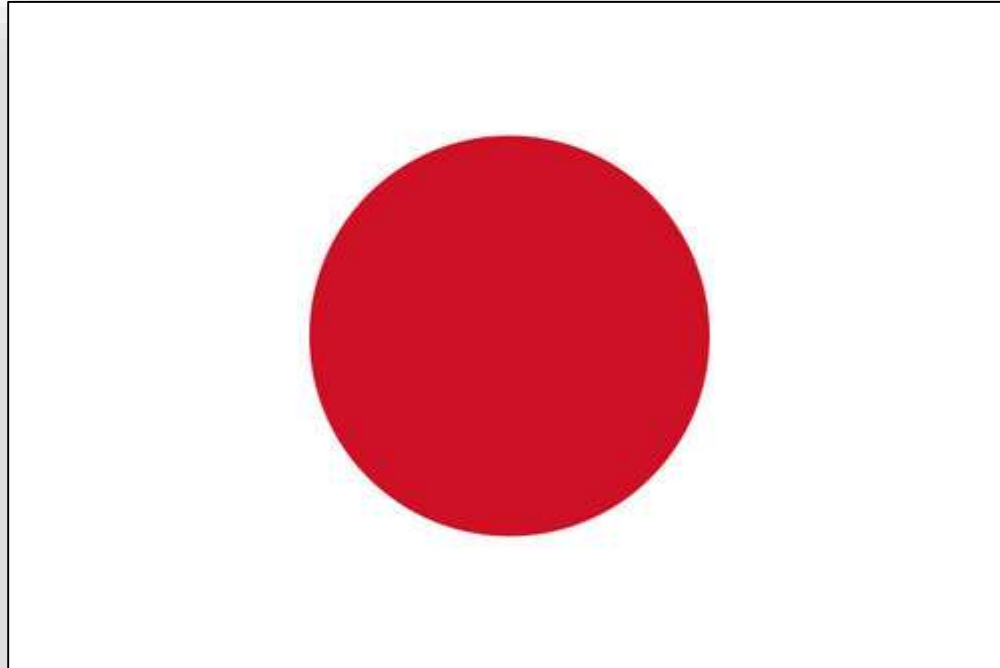
Monetary policy needs to remain accommodative in most countries, and more aggressive QE is needed in the euro area

Fiscal consolidation has progressed significantly, leaving room in many economies to slow the pace of adjustment

Ambitious structural reforms are needed to boost investment, trade and job creation

Significant efforts by G-20 countries to develop comprehensive growth strategies for the Brisbane summit are welcome

JAPAN





Short-term economic projections¹

Percentage changes

	2012	2013	2014	2015	2016
Demand and output (volumes)					
GDP	1.5	1.5	0.4	0.8	1.0
Consumption					
Private	2.0	2.0	-0.9	1.0	1.2
Government	1.7	2.0	0.3	0.3	0.5
Gross fixed investment	3.5	2.6	3.7	-1.0	-0.5
Public ²	3.1	11.3	4.8	-6.8	-17.7
Residential	3.0	8.8	-4.0	-1.5	3.6
Business	3.7	-1.5	5.1	1.0	4.0
Final domestic demand	2.3	2.1	0.3	0.4	0.7
Stockbuilding ³	0.1	-0.3	0.1	0.0	0.0
Total domestic demand	2.3	1.9	0.4	0.4	0.7
Exports of goods and services	-0.2	1.6	7.8	6.2	6.7
Imports of goods and services	5.3	3.4	6.9	3.2	4.6
Net exports ³	-0.9	-0.3	-0.1	0.4	0.3

1. Excluding the second tax hike, which was delayed to 2017.

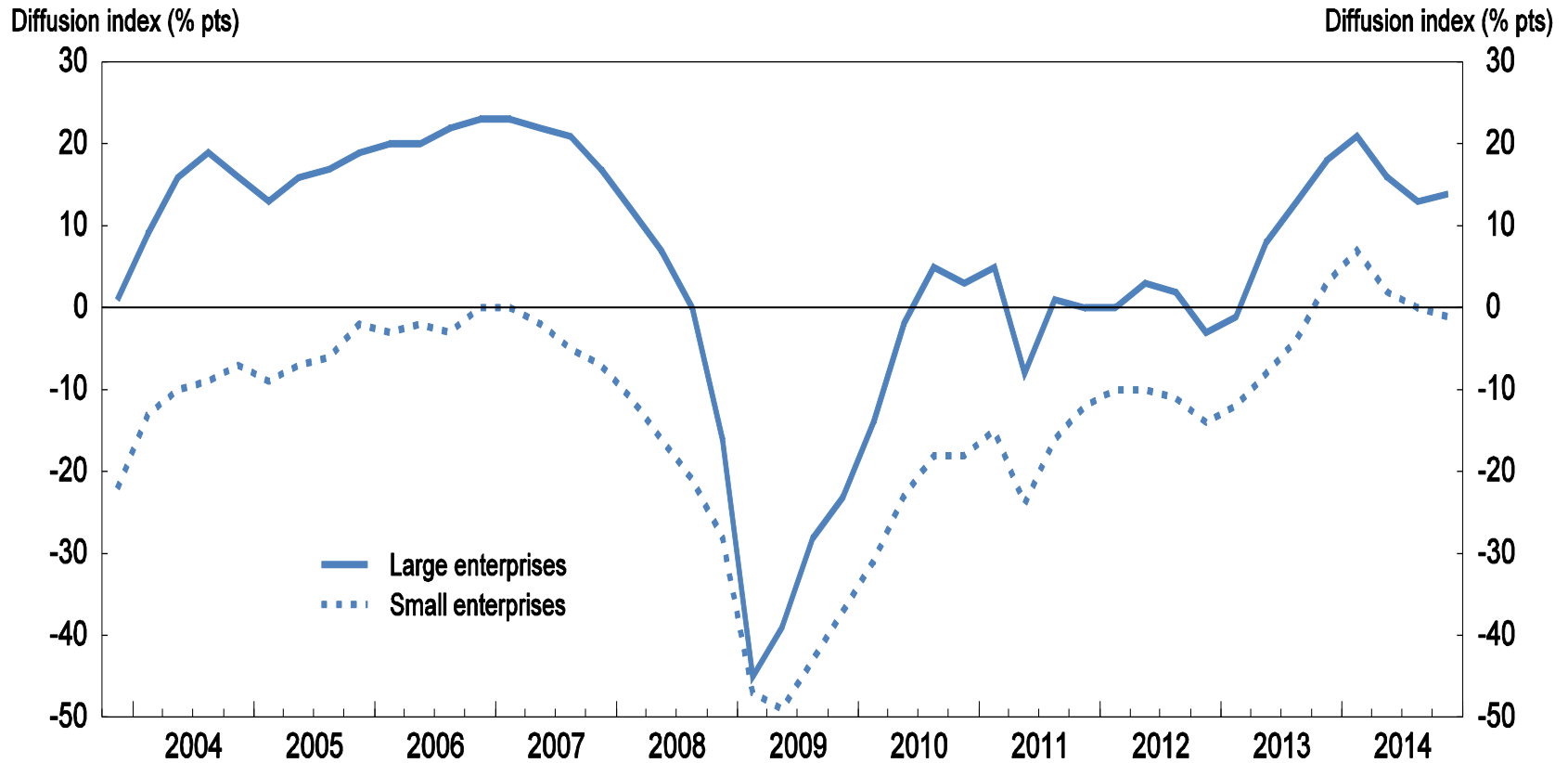
2. Including public corporations.

3. Contribution to GDP growth.

Source: OECD Analytical Database and OECD estimates and projections.



Business confidence remains high in the Tankan Survey¹



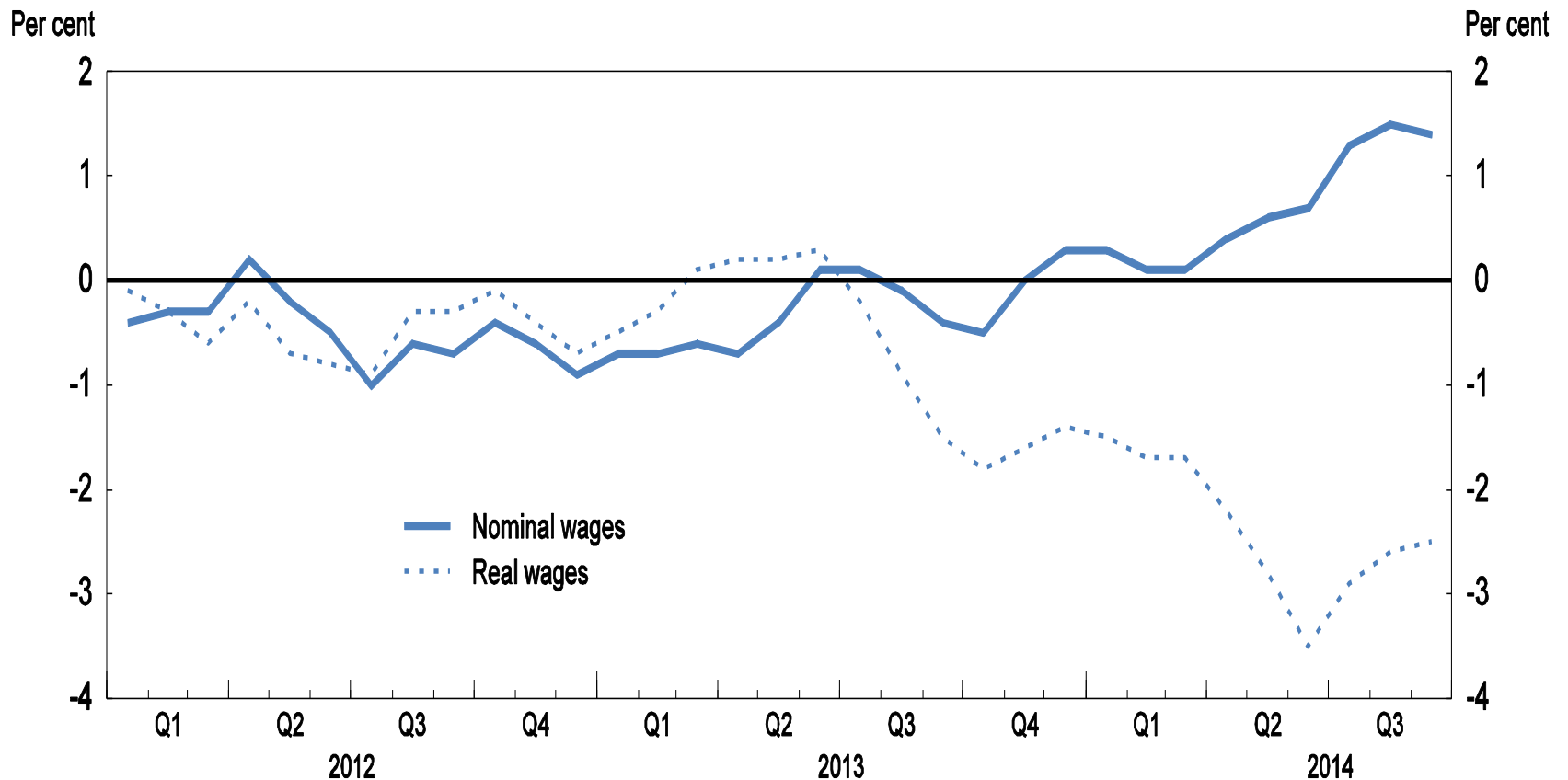
1. Diffusion index of "favourable" minus "unfavourable" conditions. Large enterprises are capitalised at a billion yen or more and small enterprises at between 20 million yen and a 100 million yen. Numbers for the fourth quarter are companies' projections made in September 2014.

Source: Bank of Japan.



Nominal wage increases have not kept pace with inflation

Year-on-year per cent changes¹



1. Total cash earnings (including bonuses). Data are three-month moving averages.
Source: Ministry of Health, Labour and Welfare, OECD calculations and Bank of Japan.



Short-term economic projections

In per cent

	2012	2013	2014	2015	2016
Inflation and capacity utilisation					
GDP deflator	-0.9	0.6	1.6	1.7	1.4
CPI ¹	0.0	0.4	2.9	1.8	1.6
Core CPI ^{1,2}	-0.5	-0.1	1.9	1.6	1.6
Unemployment rate	4.3	4.0	3.6	3.5	3.5
Output gap	-0.7	0.2	-0.2	-0.2	0.0
<i>Memorandum items:</i>					
World trade growth	3.0	3.3	3.0	4.5	5.5
Net government lending (% of GDP)	-8.7	-9.0	-8.3	-7.3	-6.3
Net primary balance (% of GDP)	-7.8	-8.1	-7.2	-6.2	-5.4
Gross debt (% of GDP)	216.5	224.2	230.0	232.8	236.7
Net debt (% of GDP)	129.4	137.2	142.9	146.8	149.6
Household saving ratio (%)	1.3	0.4	1.8	1.9	1.8
Current account (% of GDP)	1.1	0.7	0.1	0.9	1.4

1. Including the impact of the consumption tax hike from 5% to 8% in April 2014.

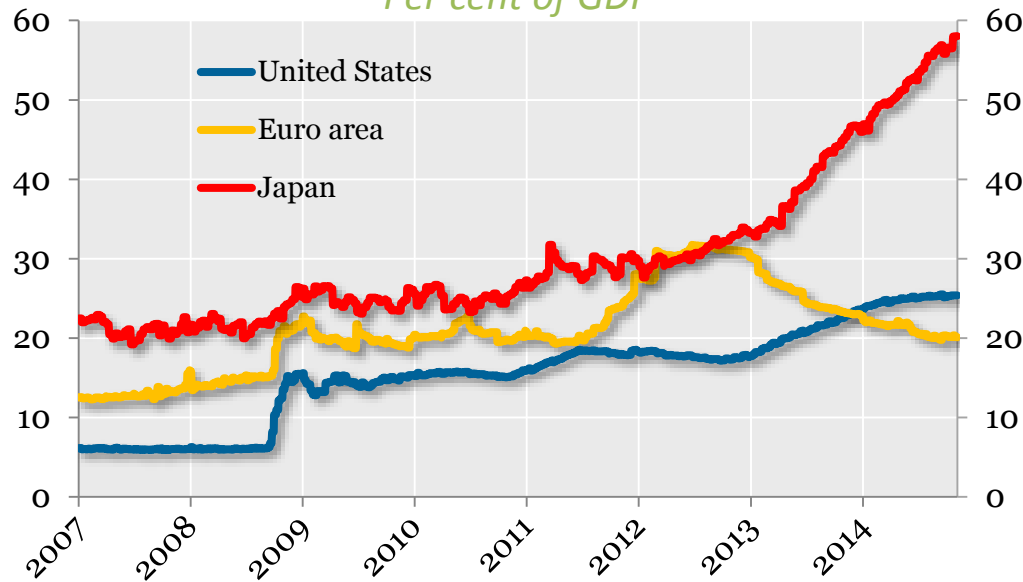
2. The core CPI is the OECD definition, which excludes both food and energy.

Source: OECD Analytical Database and OECD estimates and projections.



The first arrow of Abenomics: bold monetary policy with Quantitative and Qualitative Easing

Central bank assets
Per cent of GDP



Source: Datastream; National Central Banks.

QQE has boosted inflation expectations and pushed underlying inflation into positive territory in late 2013.

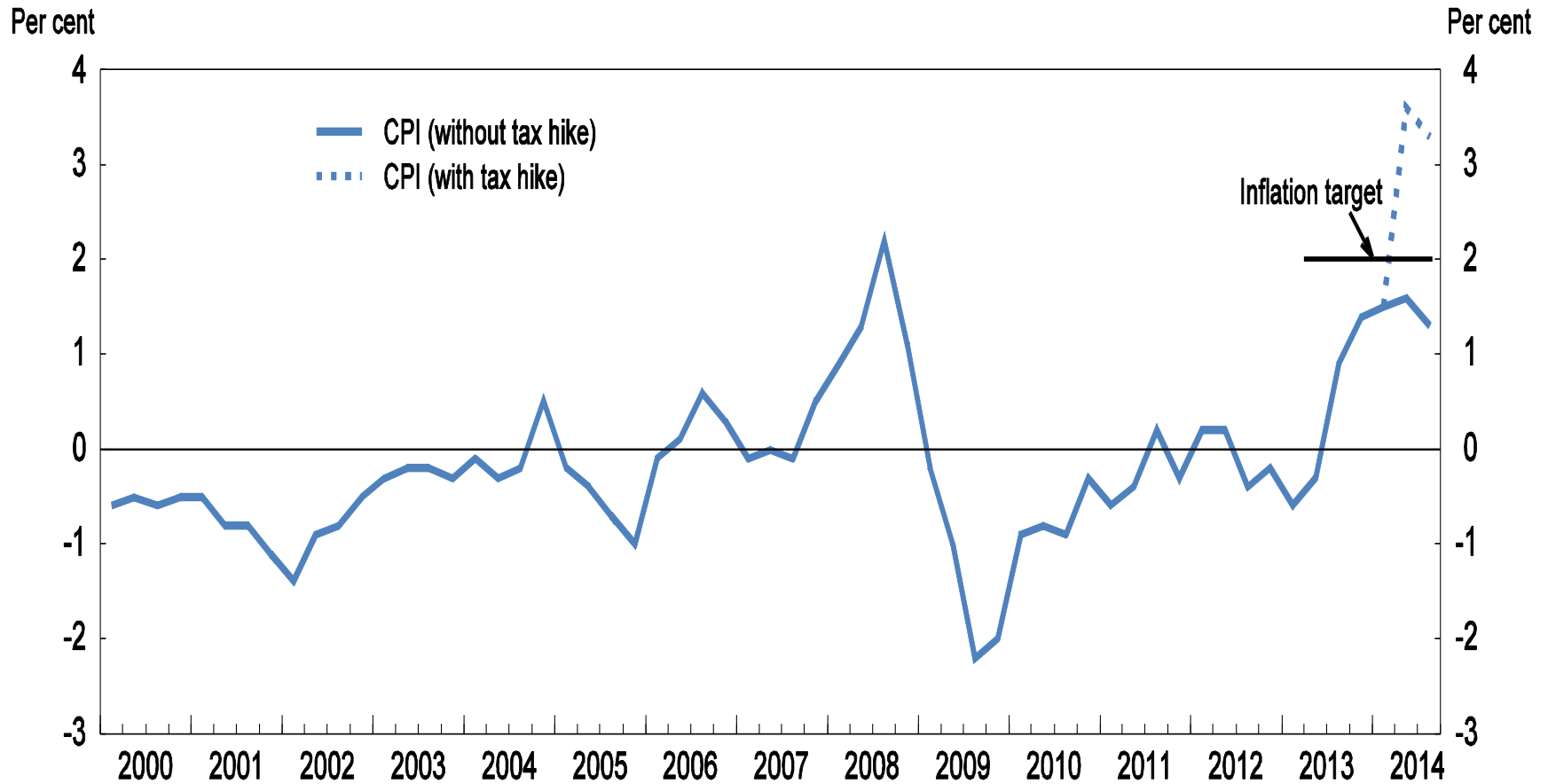
However, inflation, which had risen to 1½ per cent (year-on-year) prior to the tax hike, slowed to around 1% in late 2014 (excluding the tax hike).

The BoJ's "quantitative and qualitative monetary easing" is now increasing the monetary base at an annual pace of about 80 trillion yen per year.



Inflation has fallen since early 2014

Year-on-year percentage change



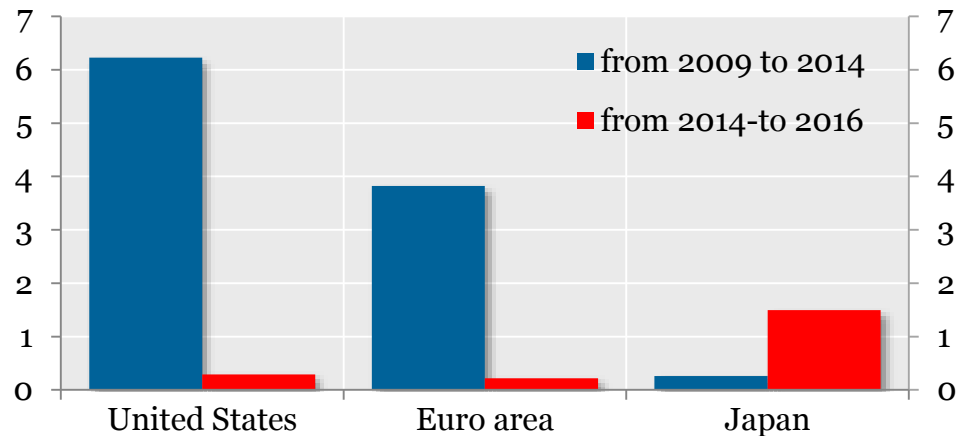
Source: OECD Economic Outlook 96 and Bank of Japan.



The second arrow of Abenomics: flexible fiscal policy

Improvement in underlying primary balance

Per cent of potential output



Source: Preliminary November 2014 Economic Outlook database.

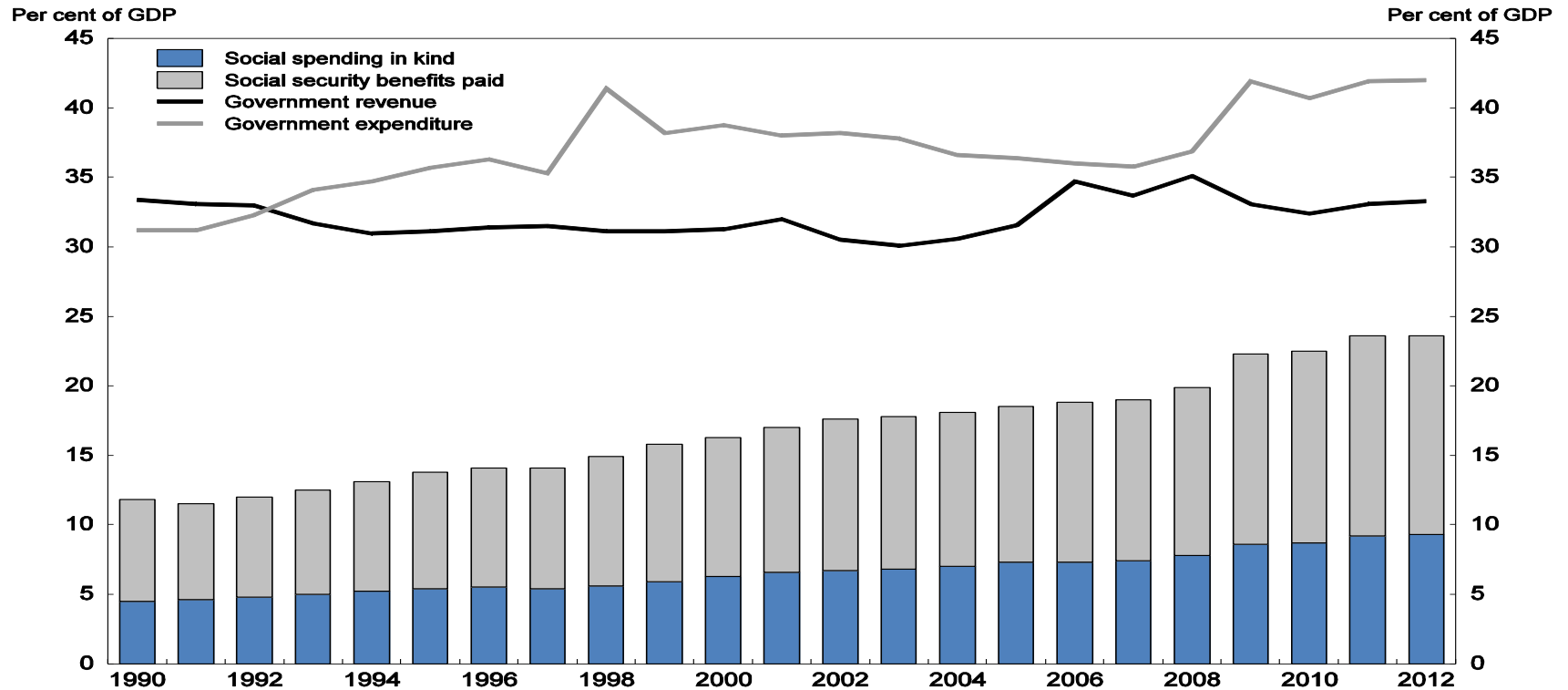
Despite the 2014 tax hike, there was no fiscal consolidation over 2010-14, in part due to the 2011 Great East Japan earthquake.

A small amount of consolidation is expected in 2015-16, due to spending cuts.

Japan must continue to address its fiscal challenges.



Total spending and social welfare spending in Japan

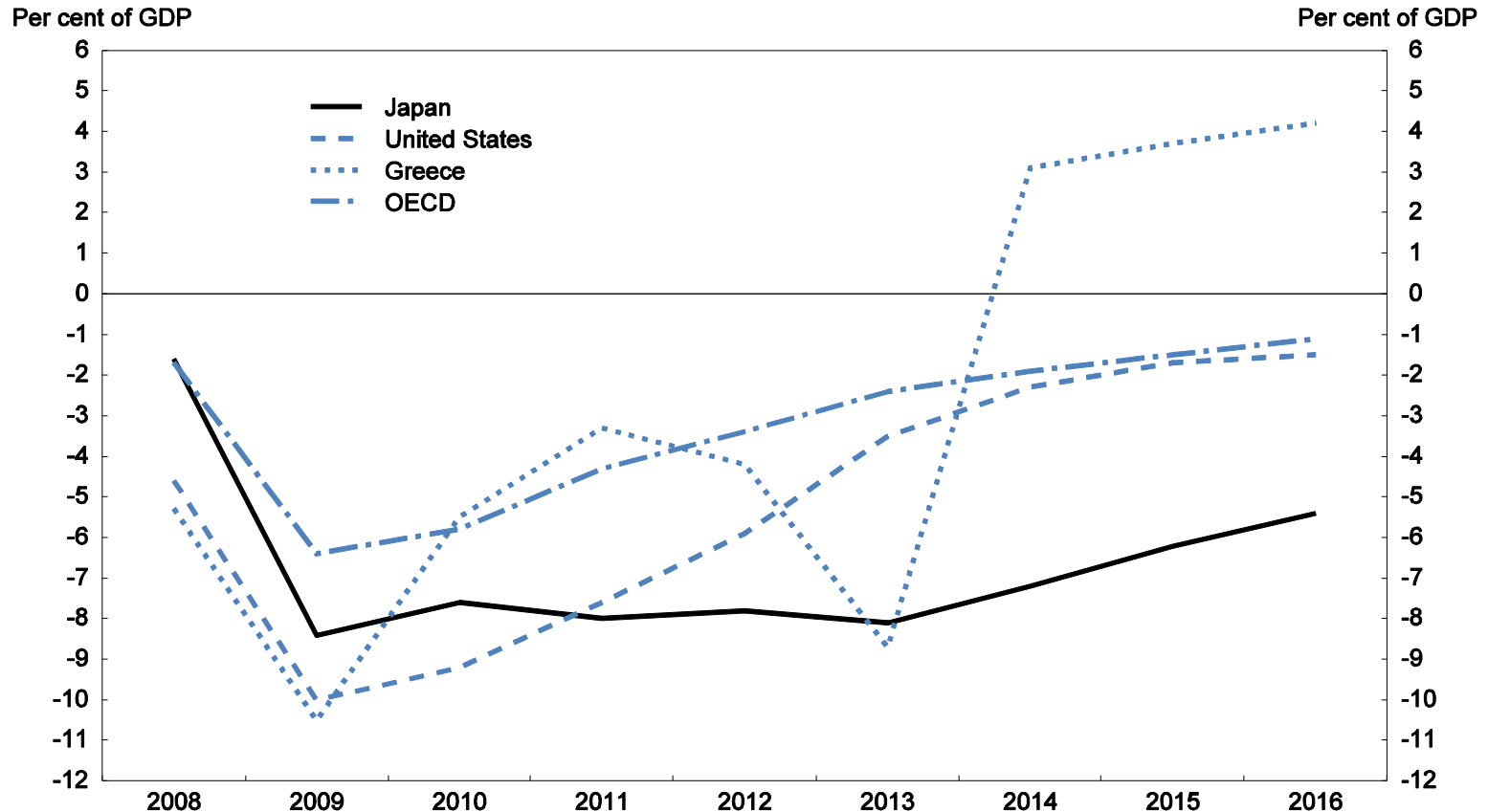


Source: OECD Analytical Database.



Japan's public debt has soared during the past 20 years¹

Primary budget balance on a general government basis



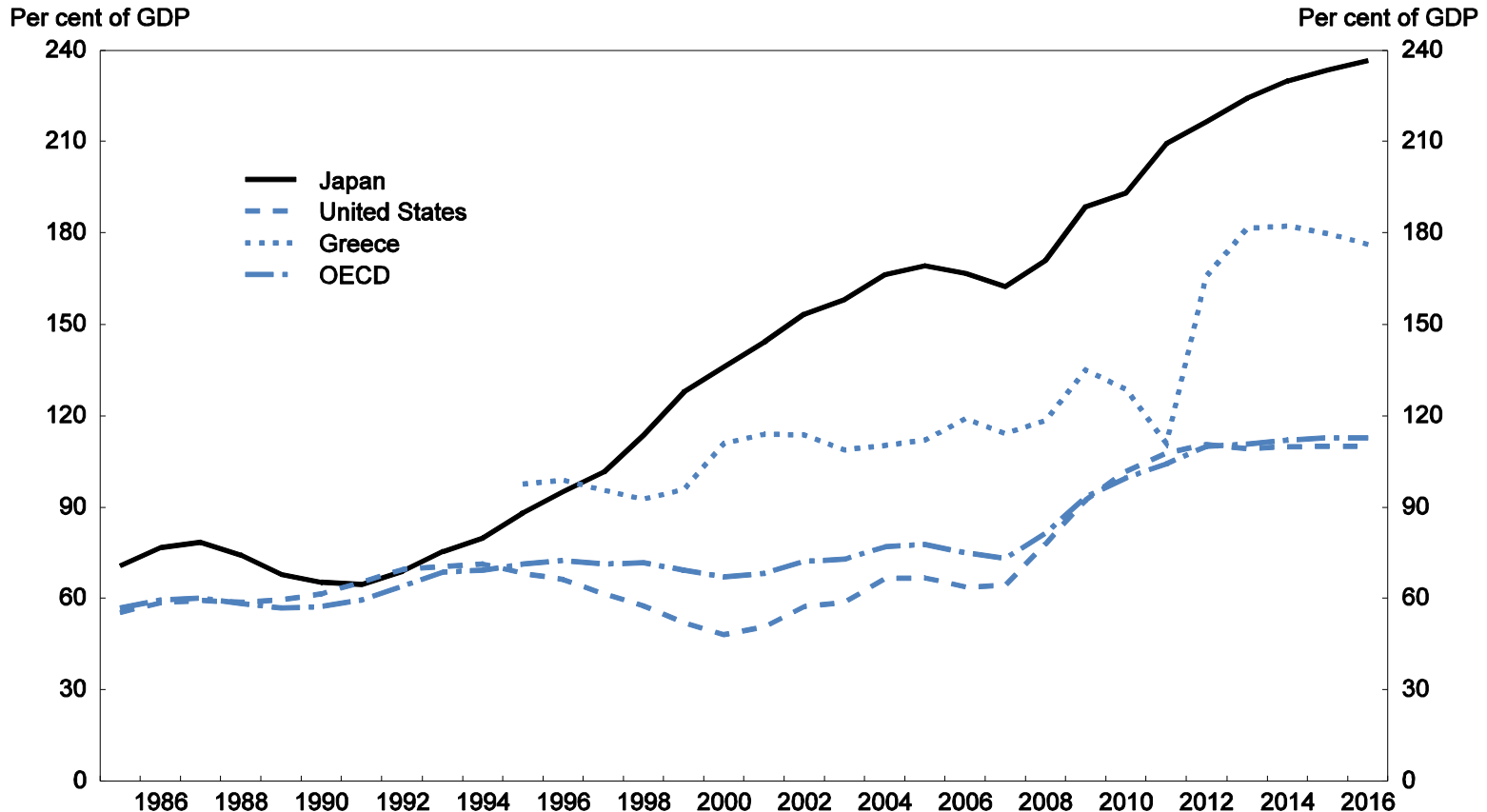
1. OECD estimates for 2014 and projections for 2015-16.

Source: OECD Economic Outlook 96.



Japan's public debt has soared during the past 20 years¹

Gross public debt on a general government basis



1. OECD estimates for 2014 and projections for 2015-16.

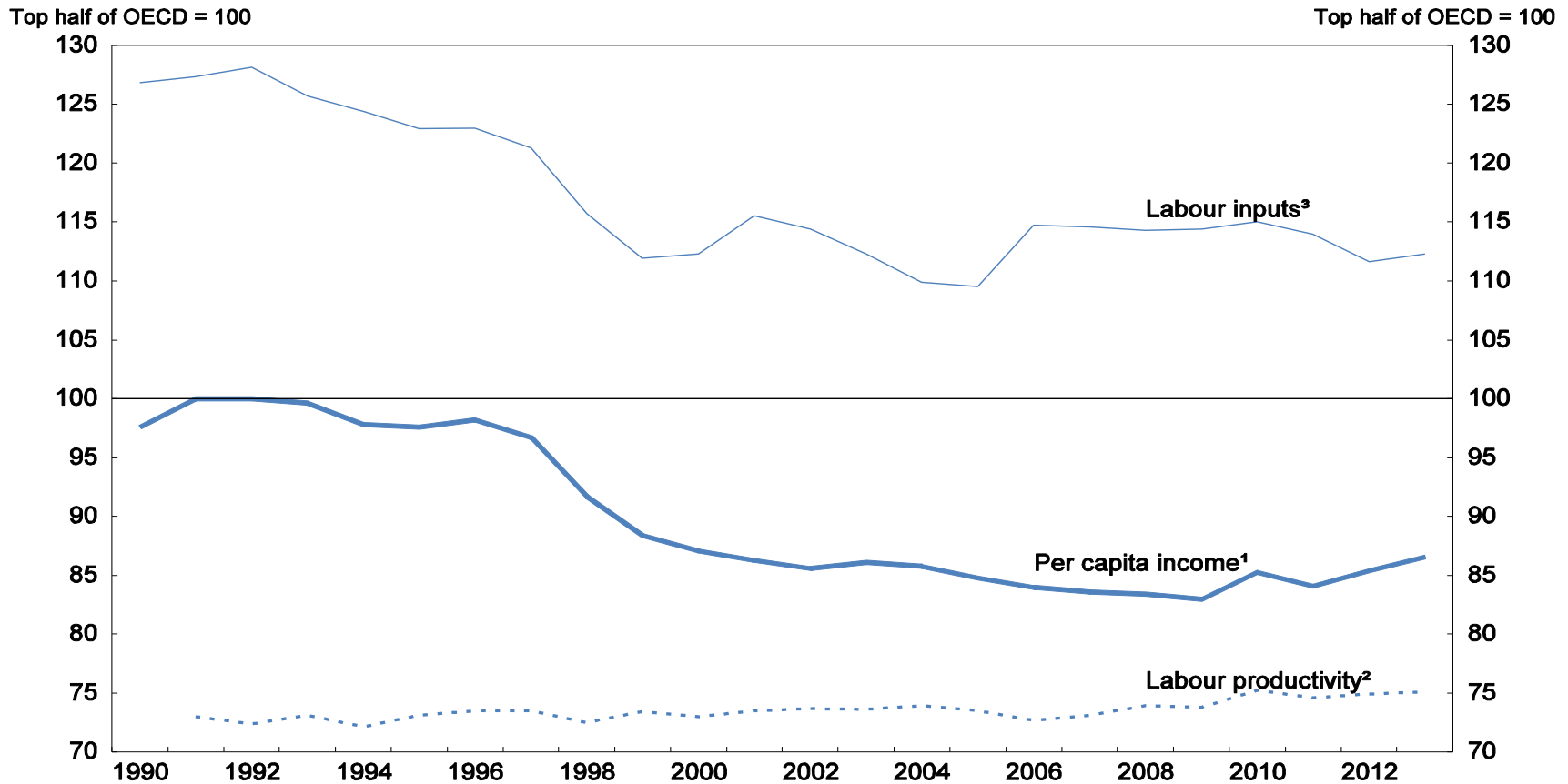
Source: OECD Economic Outlook 96.



**The third arrow of
Abenomics: a growth
strategy that encourages
private-sector investment**



Living standards in Japan have fallen relative to the top half of the OECD



1. Per capita GDP using 2013 PPP exchange rates.

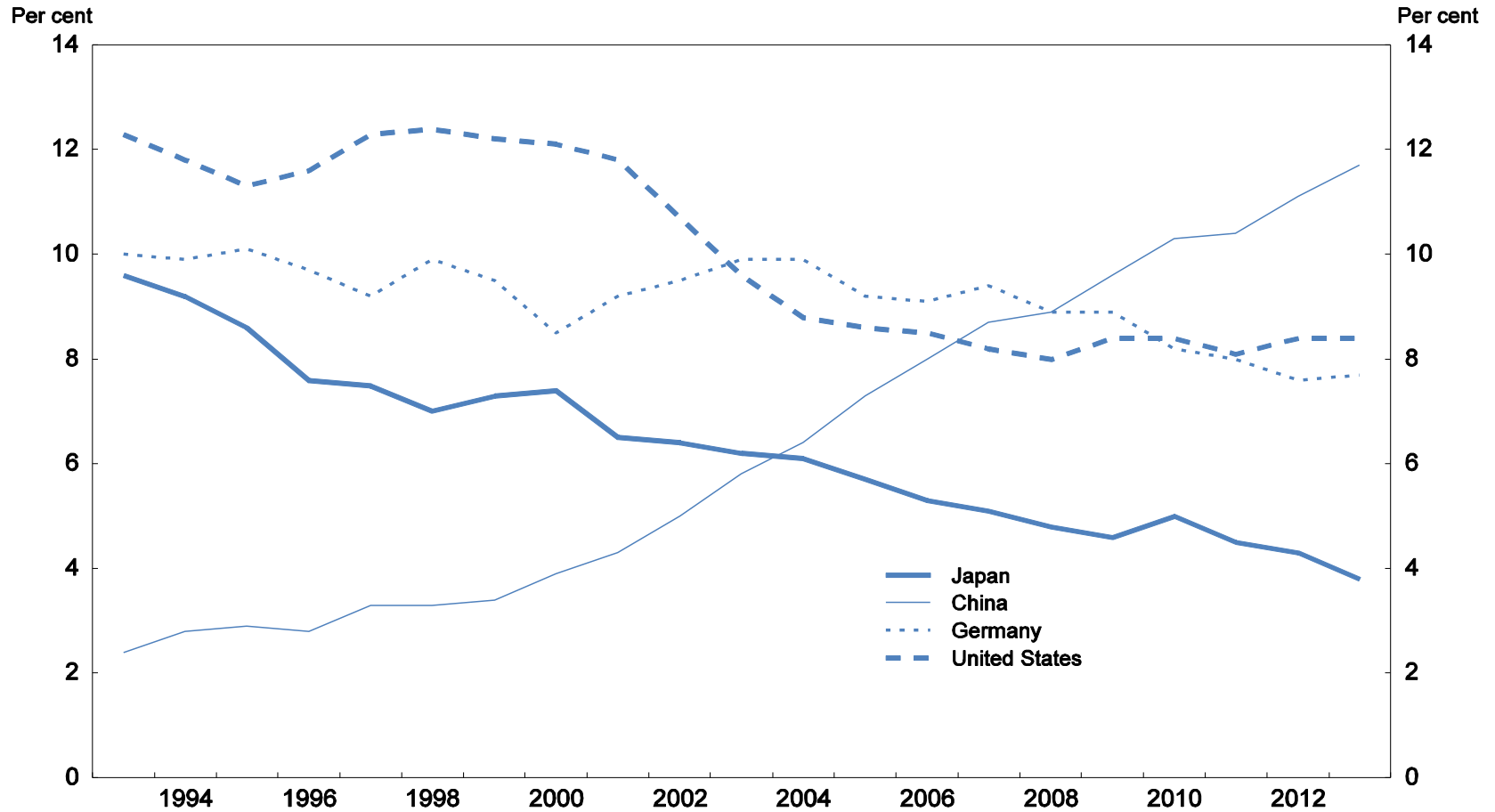
2. GDP per hour of labour input.

3. Total number of hours worked per capita.

Source: OECD Going for Growth Database.

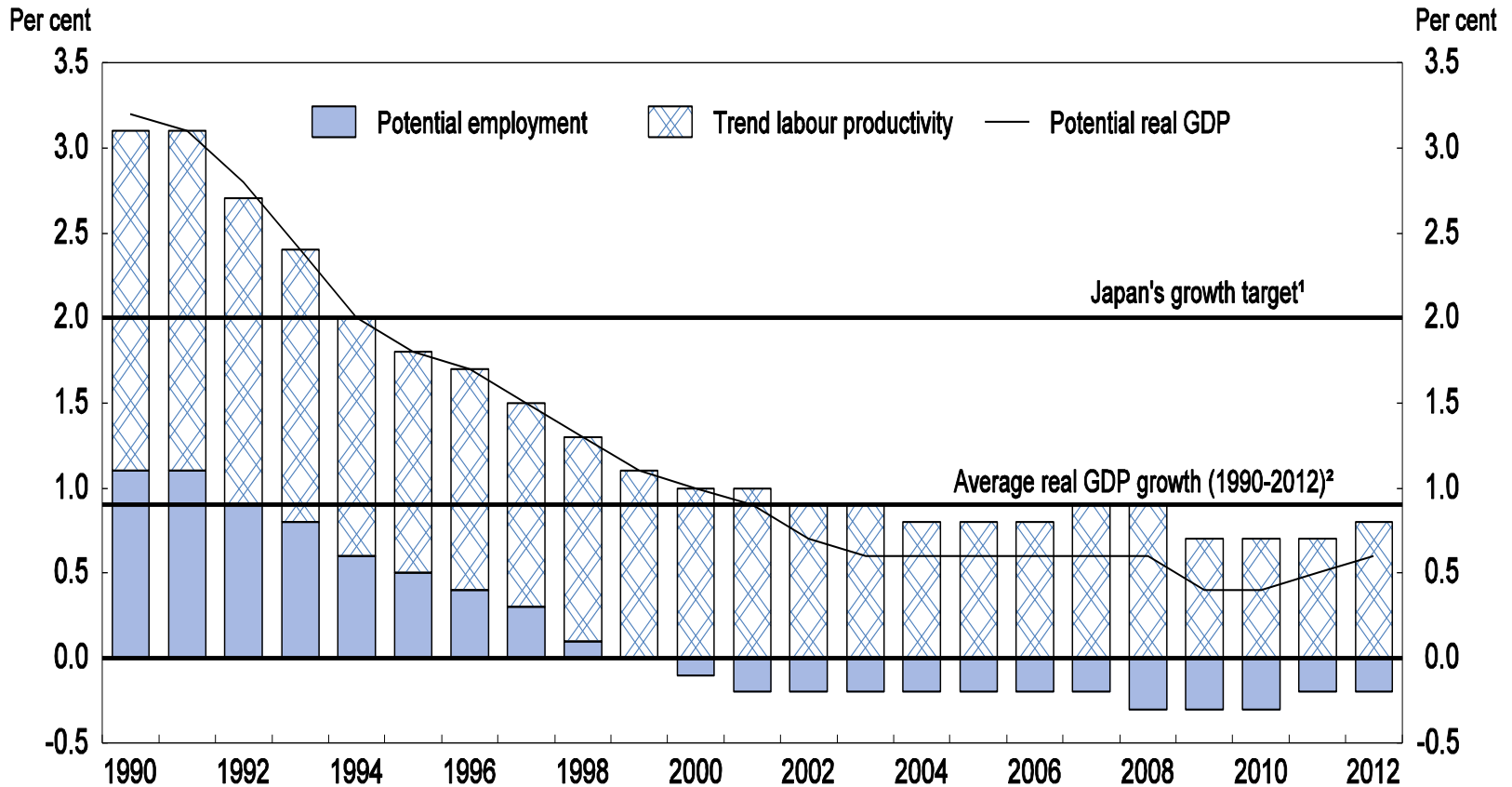


Japan's share of world exports has been falling during the past 20 years



Source: WTO Database.

Japan's potential GDP growth rate has fallen sharply since 2012



1. The 2% target was set in 2009 and maintained by subsequent governments.

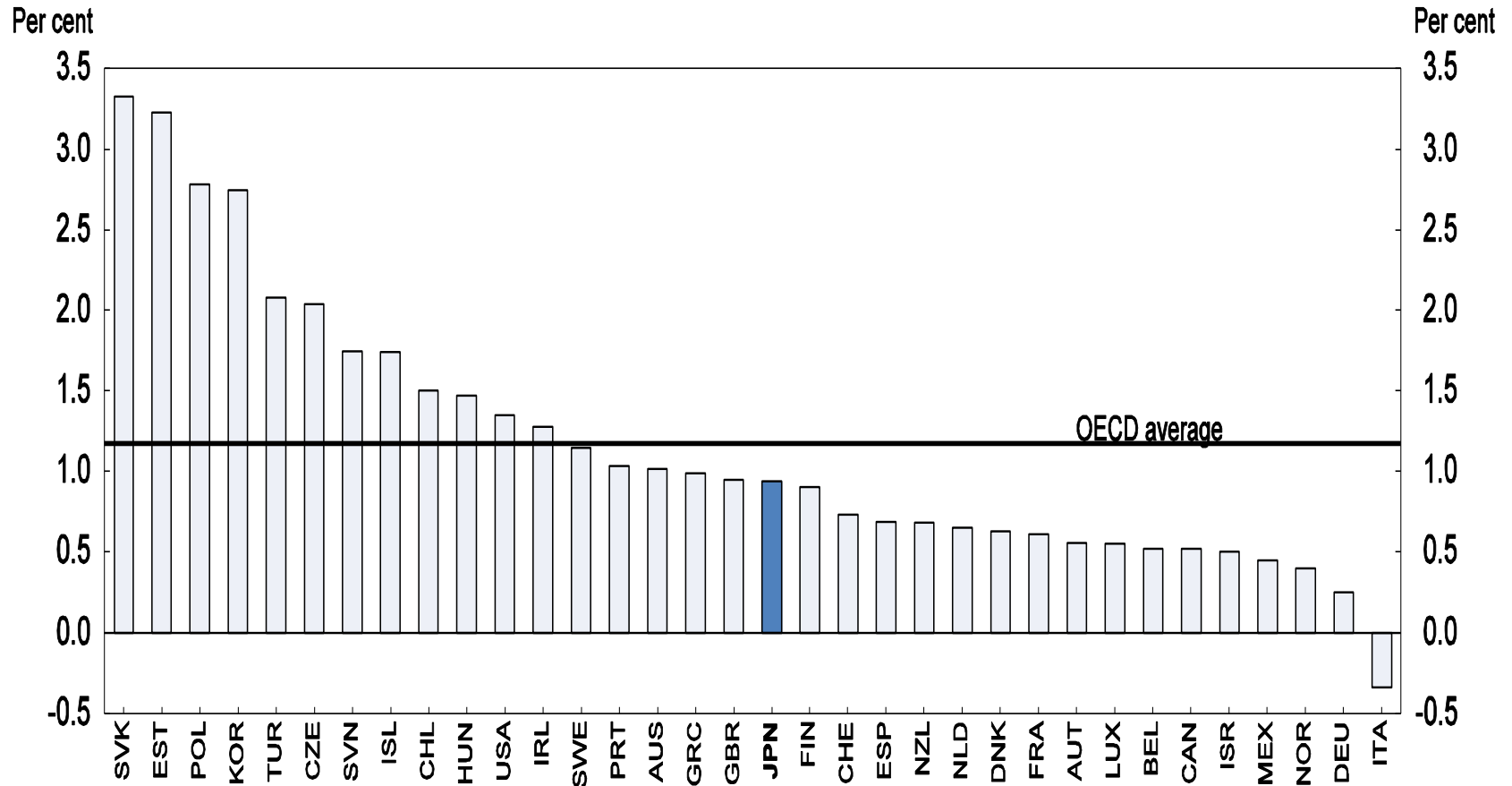
2. Average annual GDP growth in real terms in Japan between 1990 and 2012.

Source: OECD Potential Output Database.



Average labour productivity growth¹ in Japan is already near the OECD average

Average annual growth rate over 2000-13

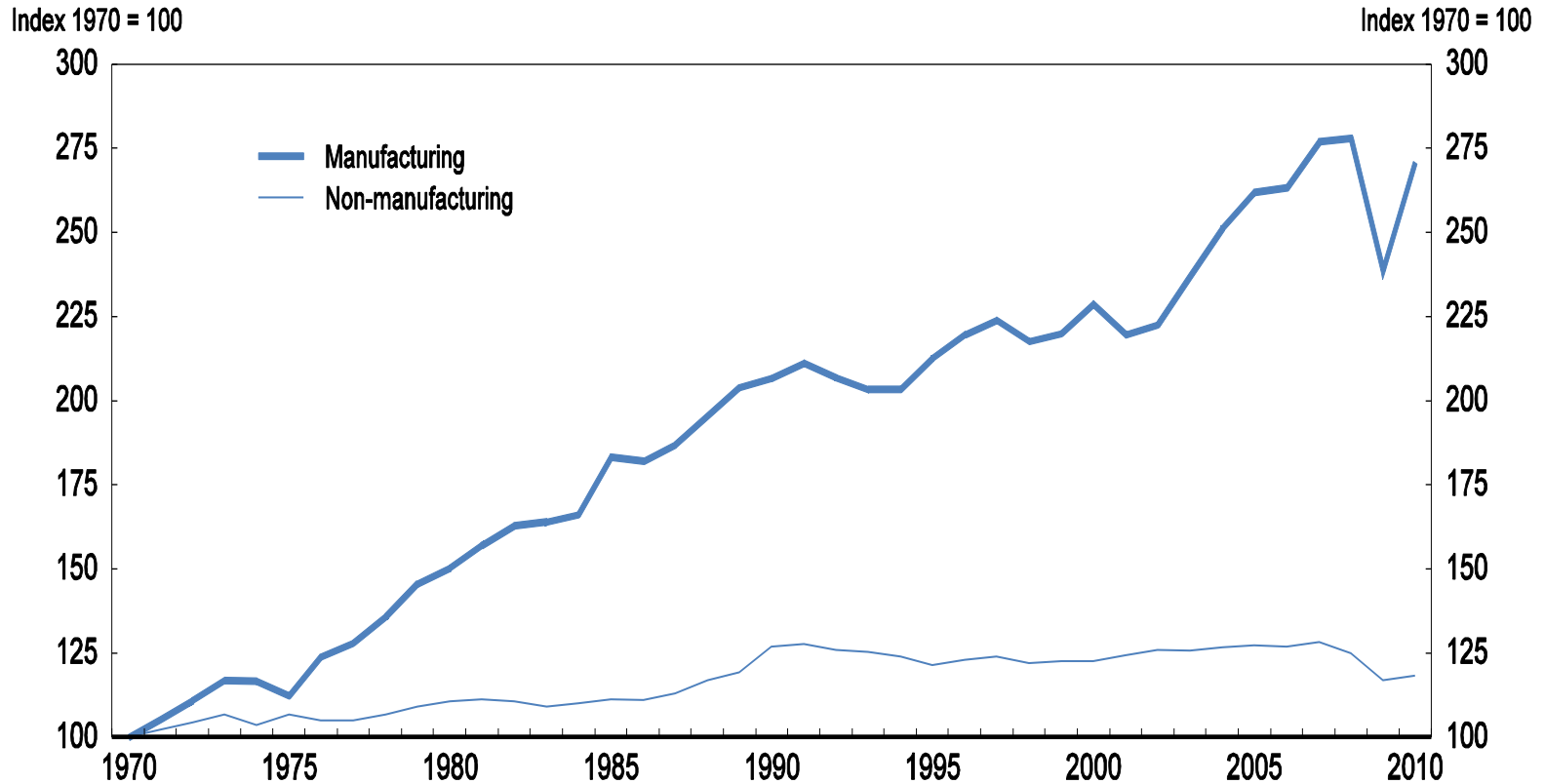


1. Real GDP divided by total employment (including self-employed).

Source: OECD Economic Outlook Database.



The level of total factor productivity in non-manufacturing has declined since 1991

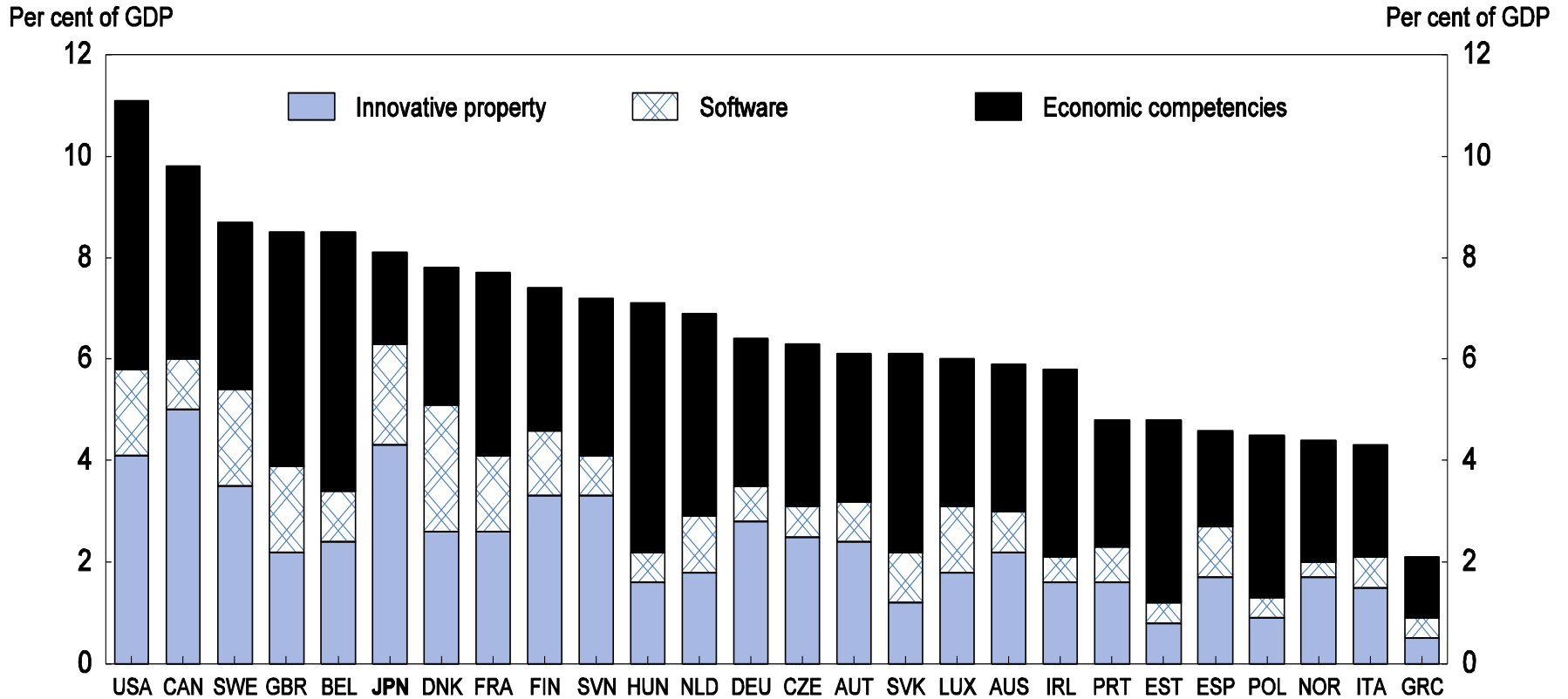


Source: Japan Industrial Productivity Database 2013.



Investment in knowledge-based capital

Per cent of GDP in OECD countries, 2010 or latest year available

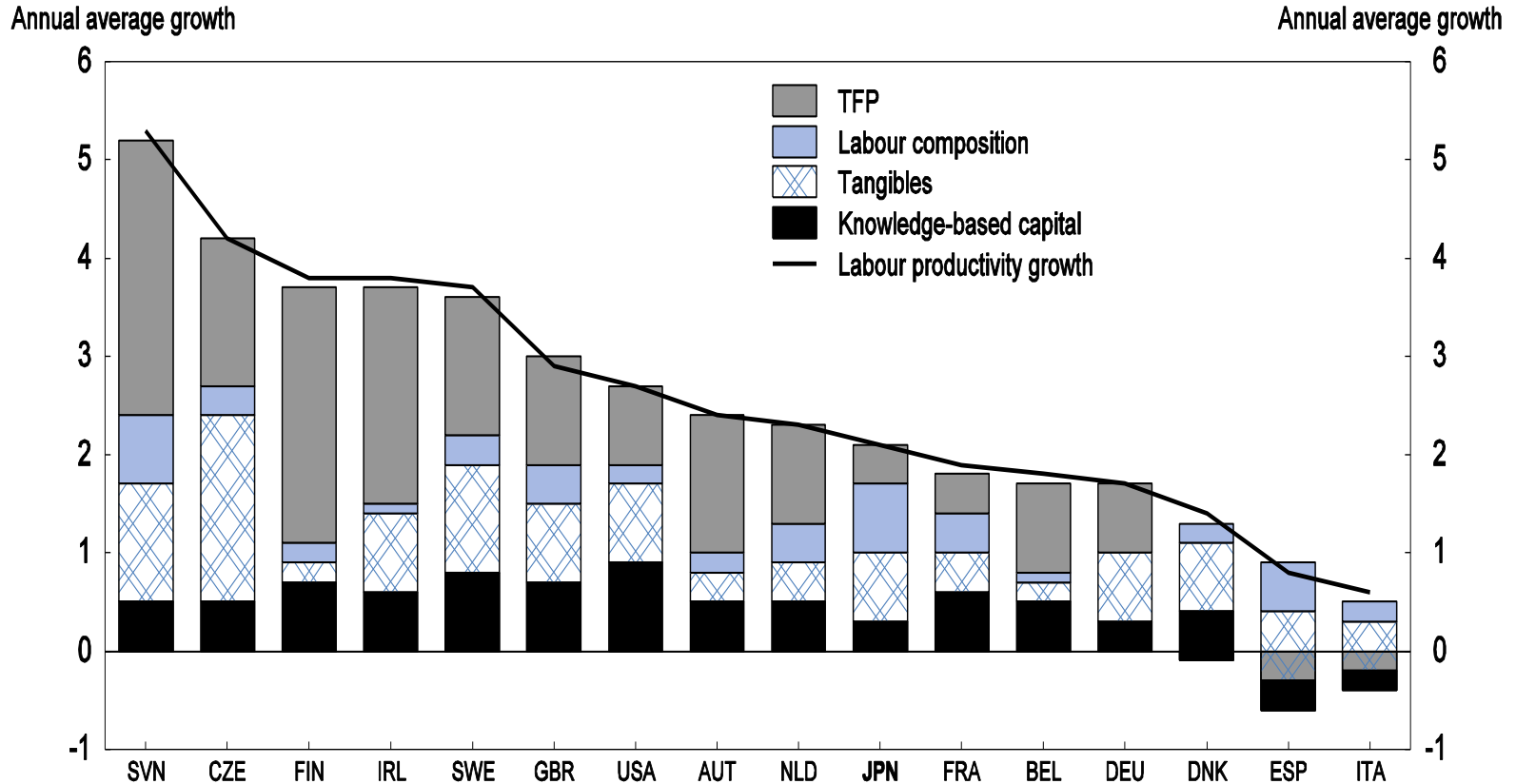


Source: Corrado et al. (2012).



Investment in knowledge-based capital

Contribution to the growth in labour productivity, 1995 to 2007¹



1. Annual average growth rate from 1995 to 2007 of output per hour worked.

Source: Corrado et al. (2012).



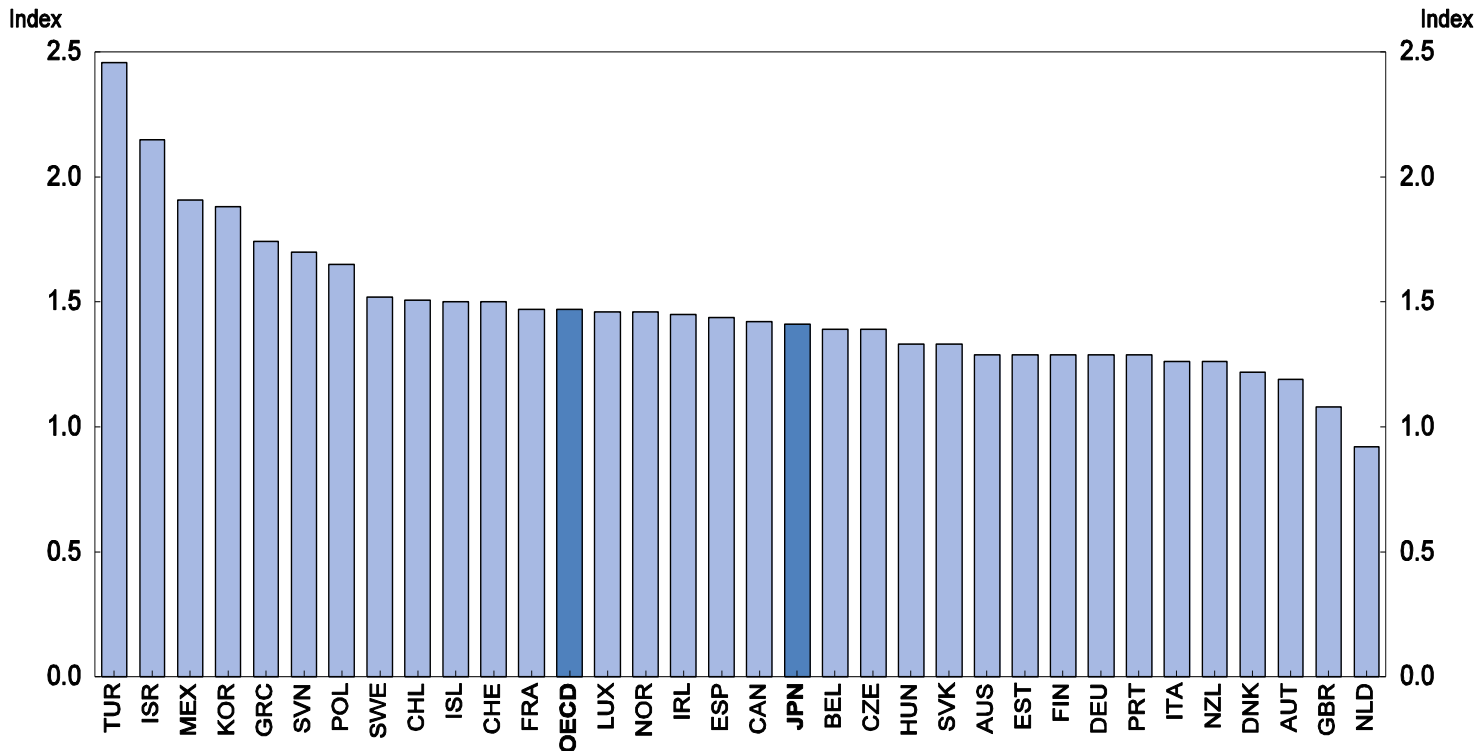
Policies to boost output growth toward the government's 2% target

1. Improve framework conditions

- Corporate governance
- Product market regulations
- International competition (FDI, EPAs, TPP)
- Labour mobility



Japan lags behind frontrunners in overall product market regulation in 2013¹



1. The OECD Indicators of Product Market Regulation are a comprehensive and internationally-comparable set of indicators that measure the degree to which policies promote or inhibit competition. Research shows that the indicators have a robust link to performance. The indicator, based on more than 700 questions, ranges from zero (most relaxed) to three (most stringent).

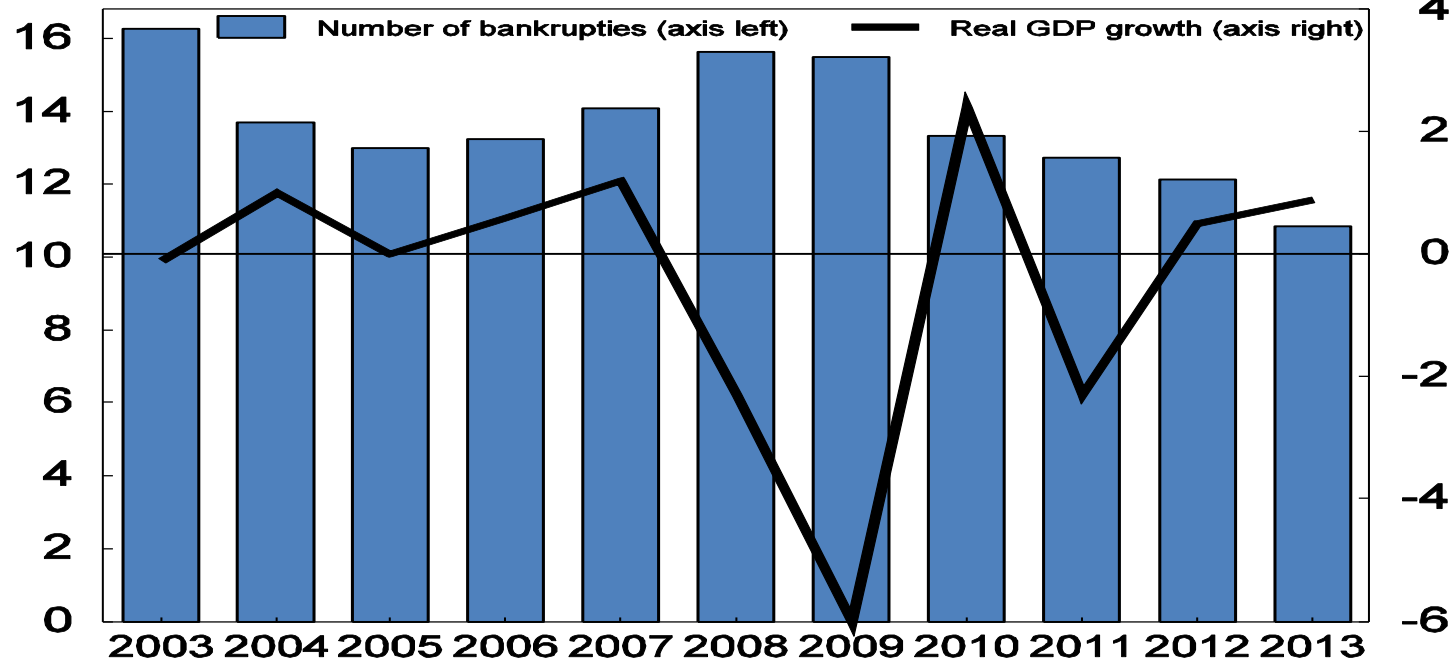
Source: OECD Product Market Regulation Database and Koske et al. (2014).



The number of bankruptcies in Japan is falling

Thousand Yen

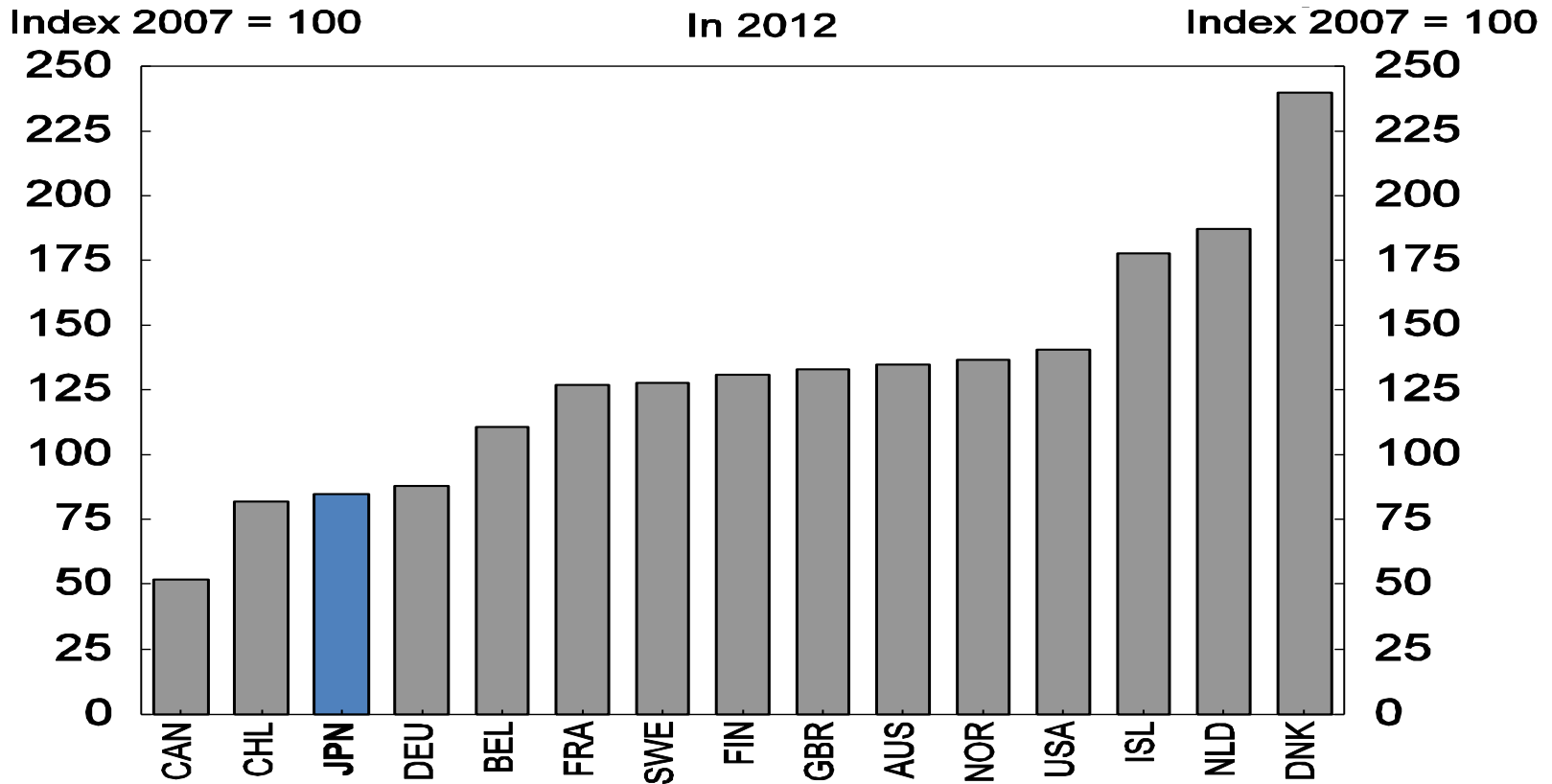
Per cent



Source: SMEA (2014), ADB National Accounts Database, and OECD (2014), *Science, Technology and Industry Scoreboard*.



The number of bankruptcies in Japan has fallen since 2008 despite two crises

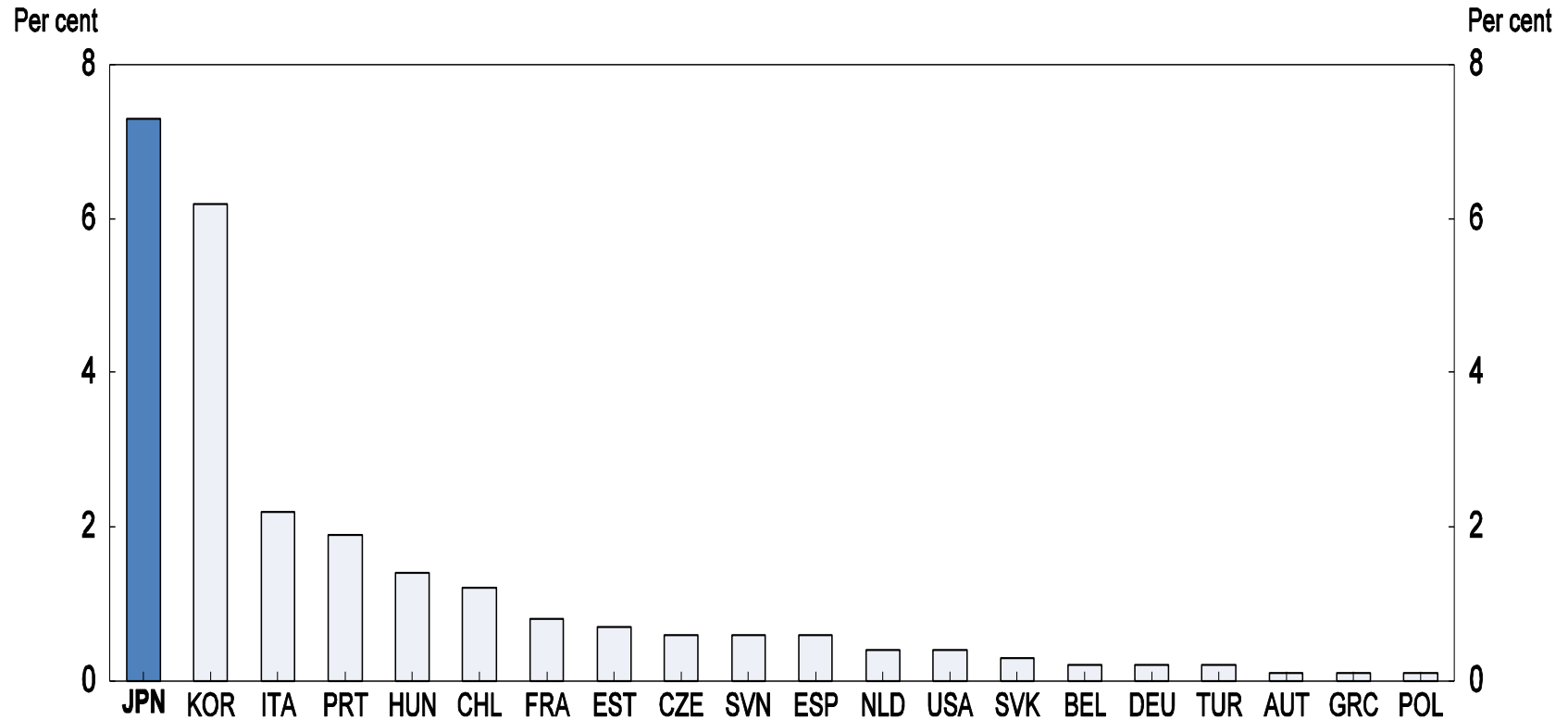


Source: SMEA (2014), ADB National Accounts Database, and OECD (2014), *Science, Technology and Industry Scoreboard*.



Credit guarantees for SMEs in Japan are exceptionally high

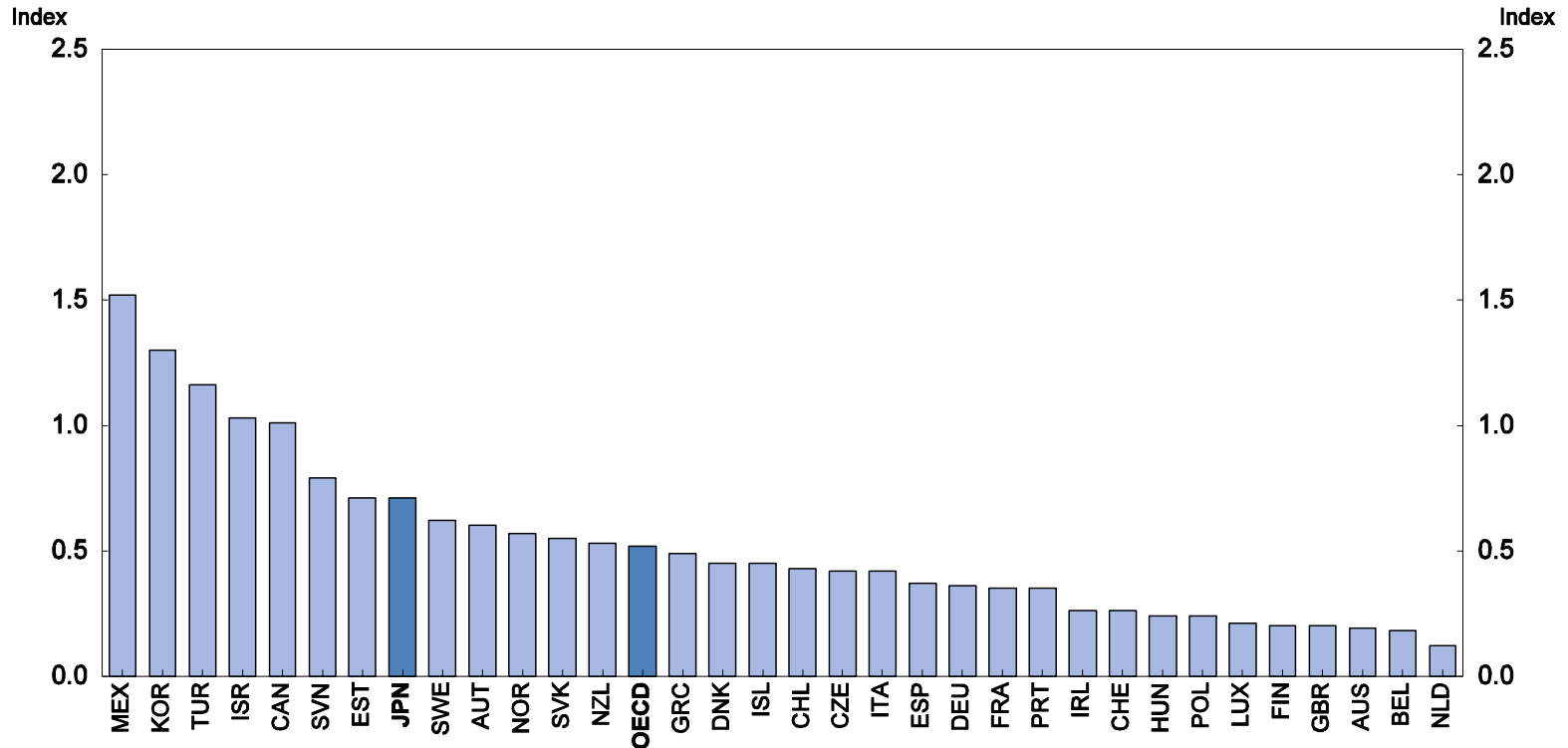
Stock of guarantees as a per cent of GDP in 2010



Source: OECD (2013), *Financing SMEs and Entrepreneurs 2013: An OECD Scoreboard*, OECD Publishing.



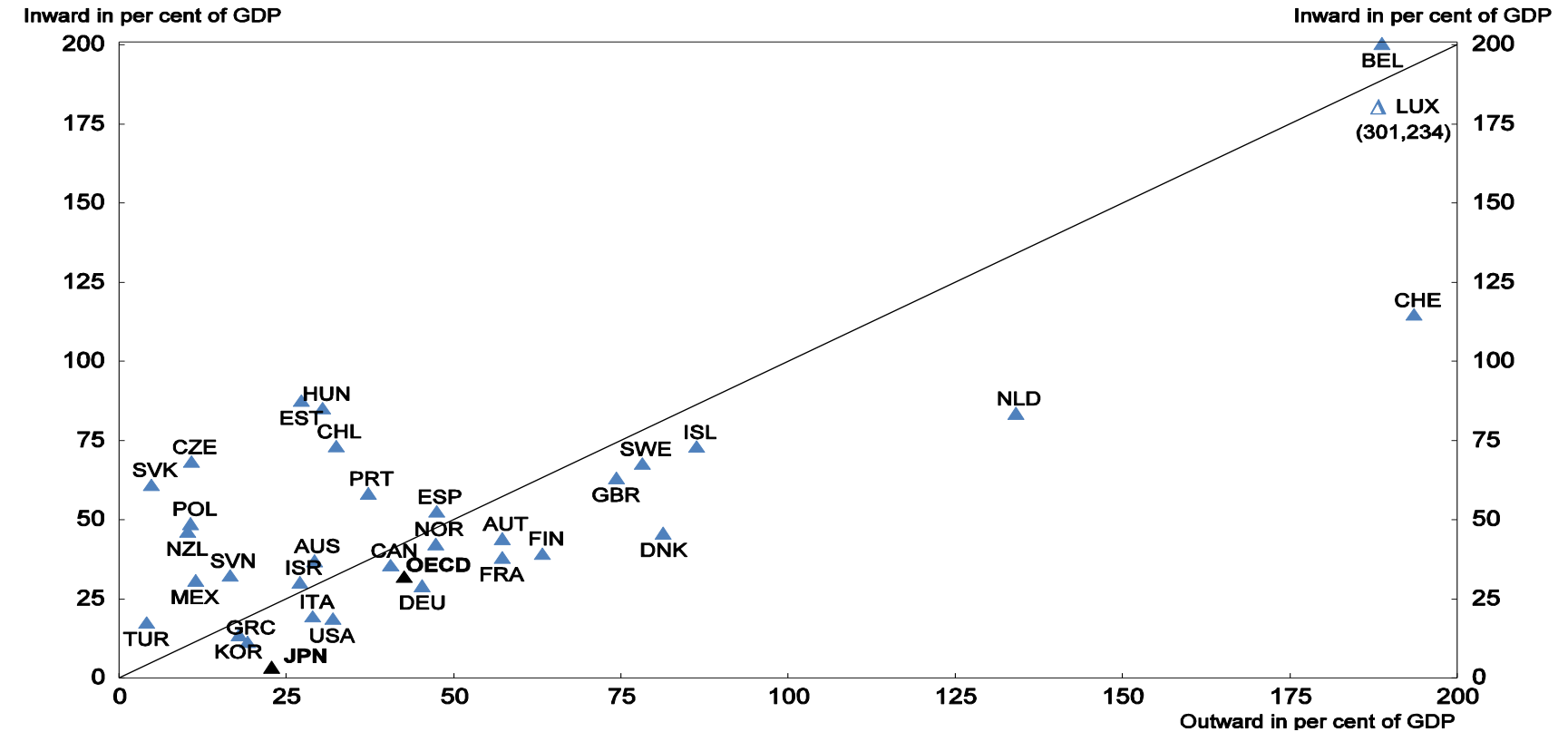
International comparison of barriers to trade and investment in 2013¹



1. The OECD Indicators of Product Market Regulation are a comprehensive and internationally-comparable set of indicators that measure the degree to which policies promote or inhibit competition. Research shows that the indicators have a robust link to performance. The indicator, based on more than 700 questions, ranges from zero (most relaxed) to three (most stringent).

Source: *OECD Product Market Regulation Database* and Koske et al. (2014).

Japan's stock of inward and outward investment is low in 2013



Source: OECD Foreign Investment Database.

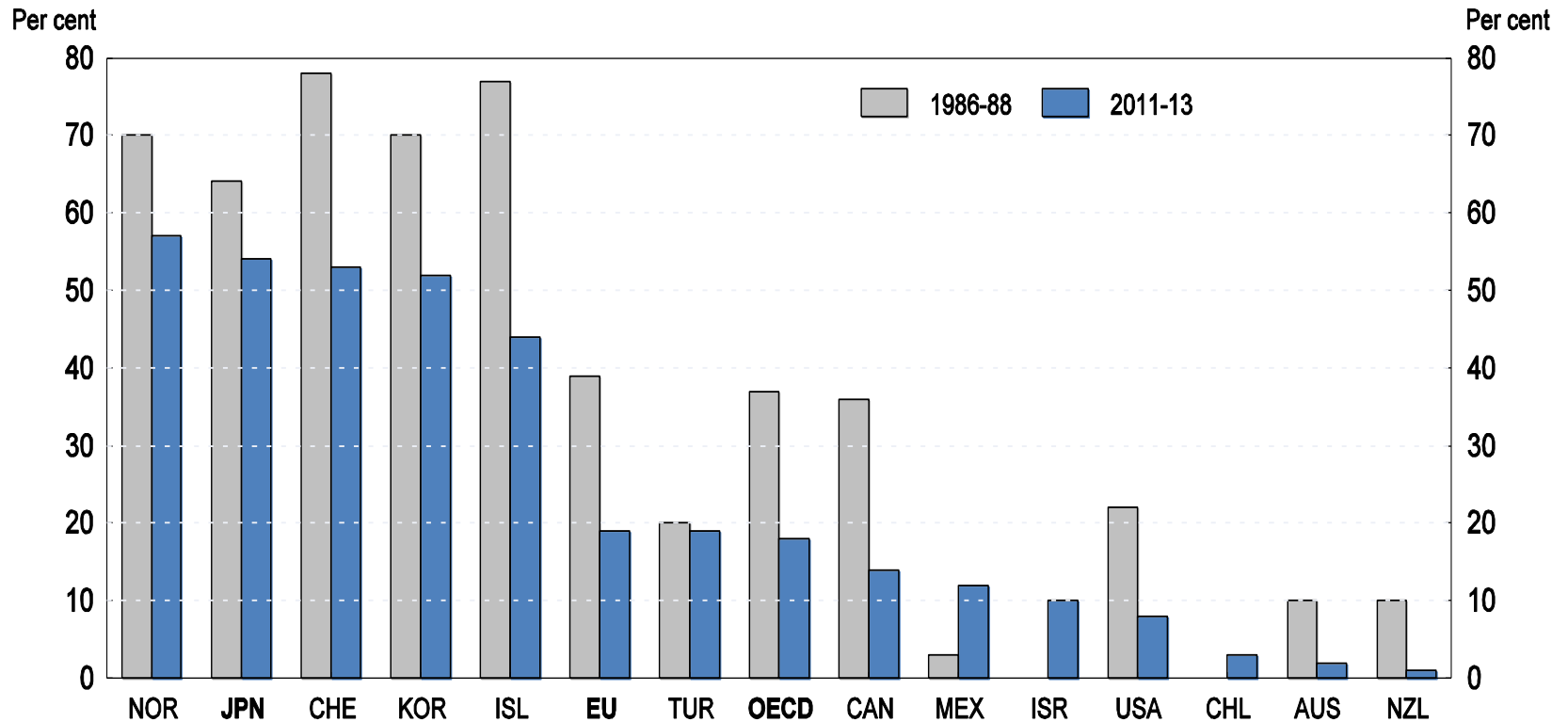


It is important to address the factors limiting inflows of foreign direct investment

1. *Low level of corporate mergers and acquisitions (M&As):* the 2007 law to facilitate “triangular mergers” has not been effective.
2. *The tax system:* a high corporate income tax rate and the short “net operating loss period” discourages FDI inflows.
3. *Corporate governance:* Japan’s corporate governance framework lags behind global standards and the lack of clarity and accountability discourages potential investors.
4. *The regulatory environment:* Unclear administrative practices and unique and rigid standards for certifying consumer goods in Japan are a deterrent to FDI inflows.
5. *Employment:* Japan needs to enhance the flexibility of employment as the lack of mid-career mobility makes it difficult for foreign firms in Japan to secure experienced workers.
6. *Entry of foreign workers:* Given that FDI is also facilitated by the movement of people, rules that restrict the entry of workers can discourage foreign investors.



The Producer Support Estimate¹ for Japan is the second highest in the OECD



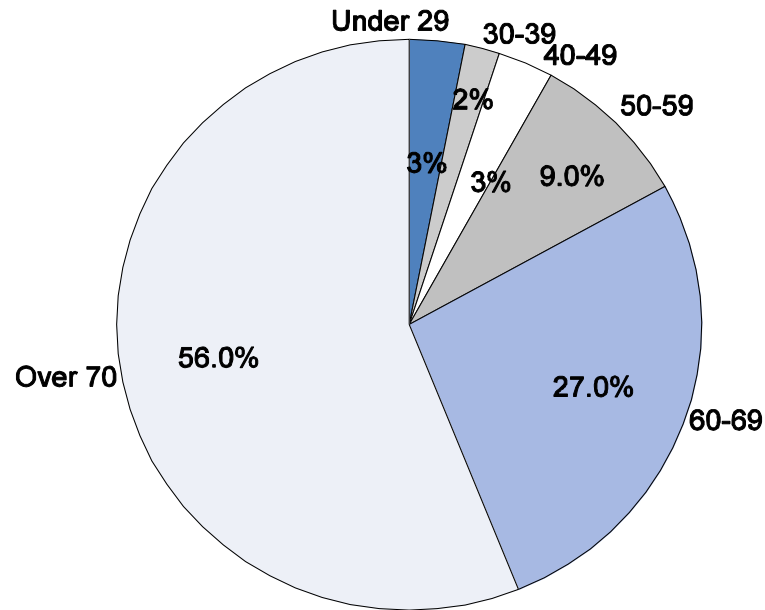
1. Producer support is the annual monetary value of gross transfers from consumers and taxpayers arising from policies that support agriculture, regardless of their nature, as a per cent of the value of gross farm receipts. Countries are ranked according to their 2011-13 levels. Chile, Israel and Slovenia excluded from the OECD total in 1986-88. The EU figure is the EU12 for 1986-88 and the EU27 for 2011-13.

Source: OECD PSE/CSE Database 2014.



Japan's farm workforce is elderly

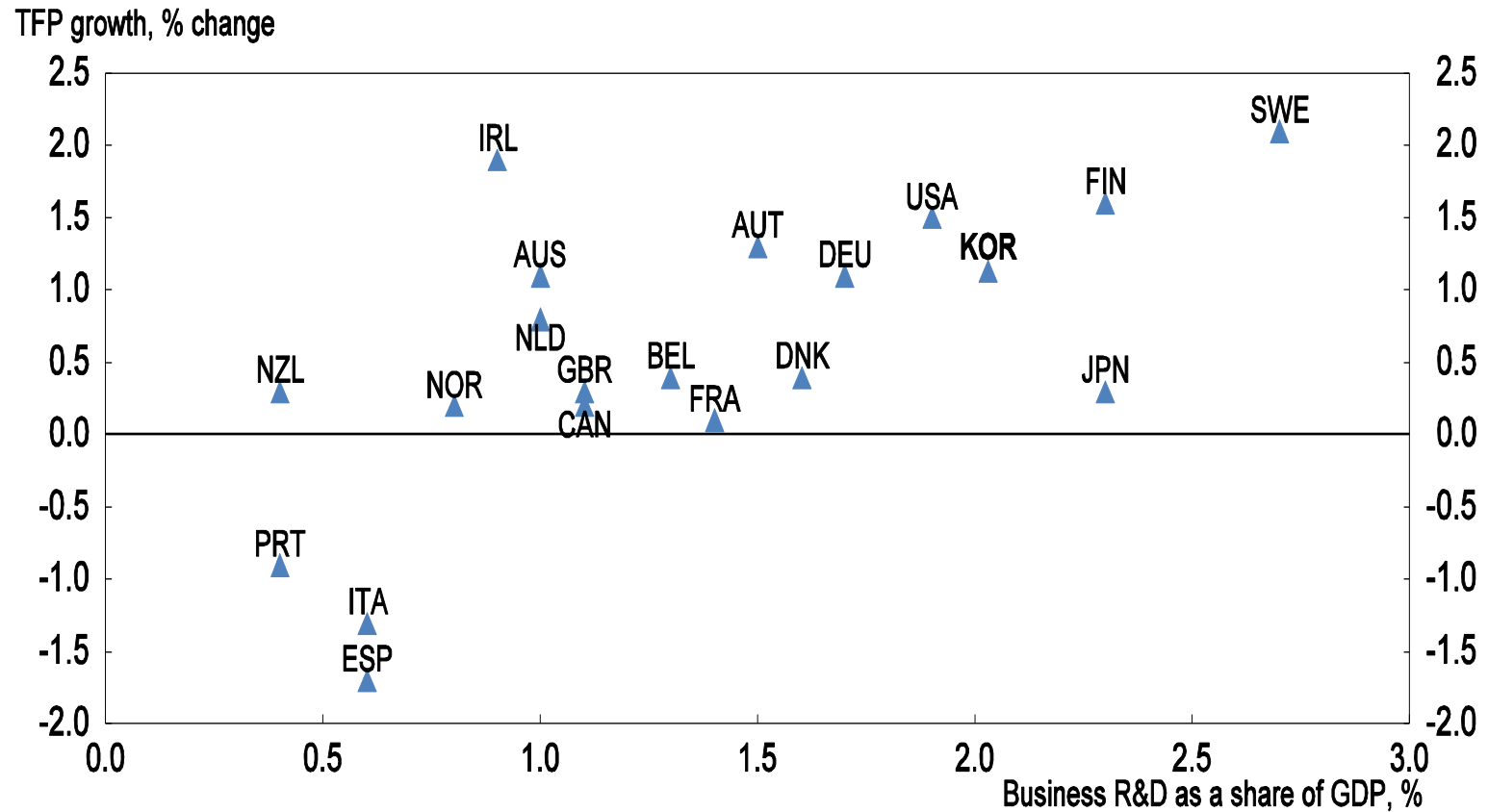
The age distribution of rice farmers in 2010



Source: Ministry of Agriculture, Forestry and Fisheries (2010).

Total factor productivity growth and business R&D intensity

1995-2010



Source: OECD Analytical Database; OECD Long-term Scenario Database; OECD Main Science and Technology Indicators.

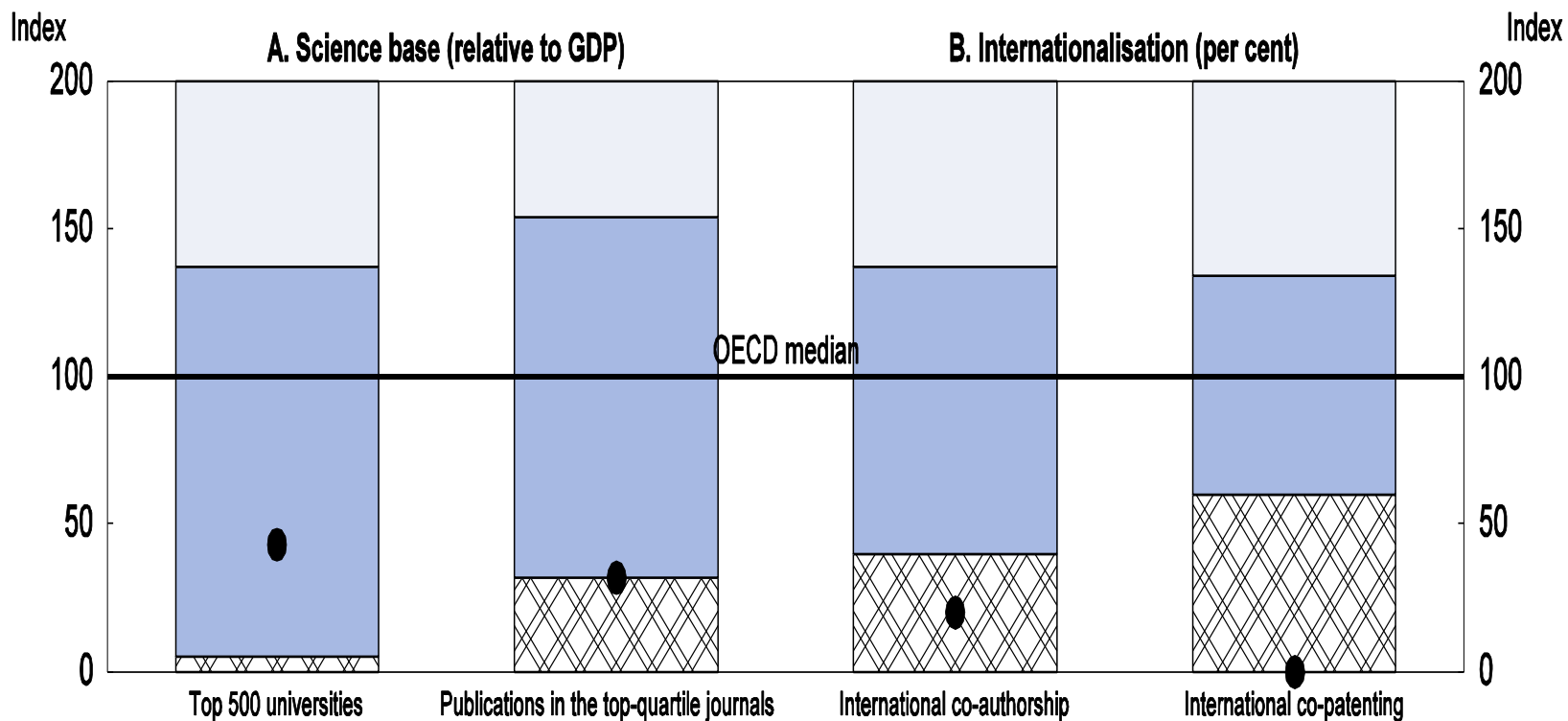


Policies to boost output growth toward the government's 2% target

2. Improve the innovation framework

- Upgrade the quality of universities
- Expand international linkages
- Enhance the role of universities

Comparative performance of national science and innovation systems in 2014



Note: Normalised index of performance relative to the median values in the OECD, which are set at 100. The top performer is set at 200 and the lowest at zero. The fifth-highest performer in the case of the “Top 500 universities” had a score of 137 relative to the OECD median, while the fifth lowest had a score of 5. Japan, with a score of 43, was in the middle range.

Source: OECD (2014), *OECD Science, Technology and Industry Outlook 2014*, OECD Publishing, Paris.



Flows of R&D funds in 2011

A. R&D funding

Allocation of R&D spending by sector performing it					
	Share of total R&D spending	Government	Universities	Business enterprises	Total
Government ¹	17.2	53.5	41.4	5.1	100.0
Universities	5.8	0.4	99.4	0.2	100.0
Business enterprises	76.5	0.7	0.5	98.8	100.0
Foreign sources	0.5	7.1	1.3	91.7	100.0

B. Sector performing R&D

Funding source for R&D performed						
	Share of total R&D performed	Government	Universities	Business enterprises	Foreign sources	Total
Government ¹	9.8	93.9	0.3	5.5	0.3	100.0
Universities	13.2	54.0	43.3	2.7	0.0	100.0
Business enterprises	77.0	1.1	0.0	98.3	0.6	100.0

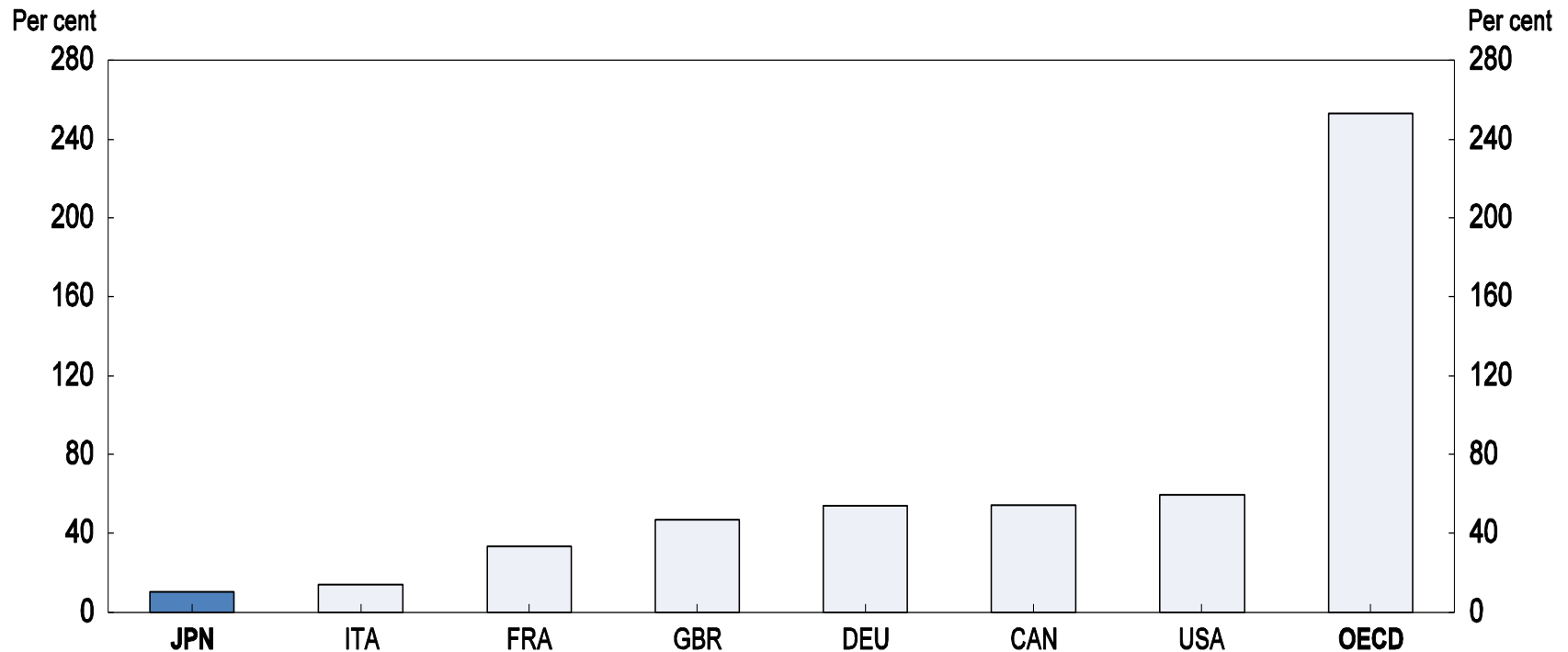
1. Includes private non-profit institutes.

Source: OECD R&D Statistics Database.



Increase in R&D performed in universities in Japan has lagged behind other OECD countries

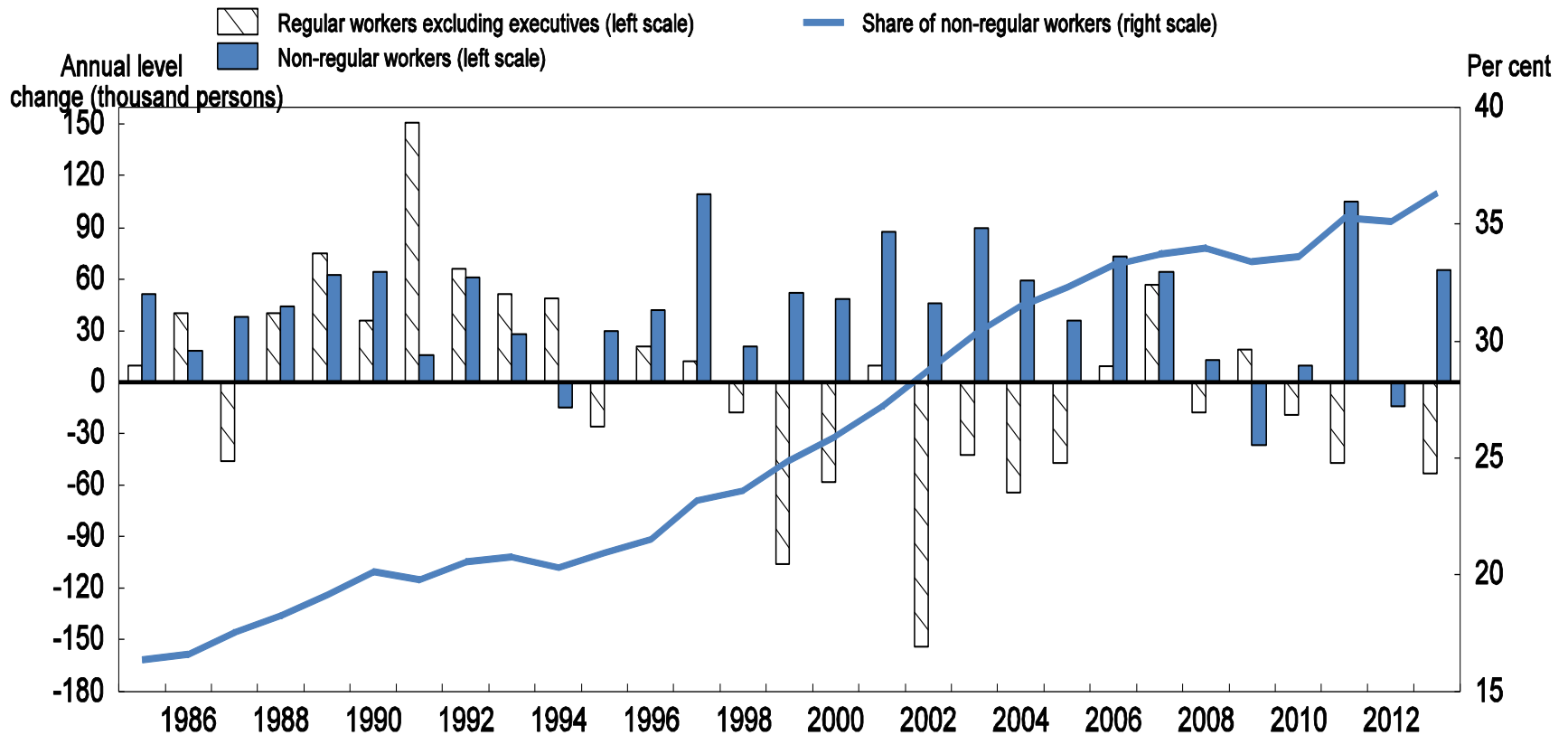
The increase between 2000 and 2012 (or latest year) in real terms



Source: OECD R&D Statistics Database.



The share of non-regular workers is rising¹

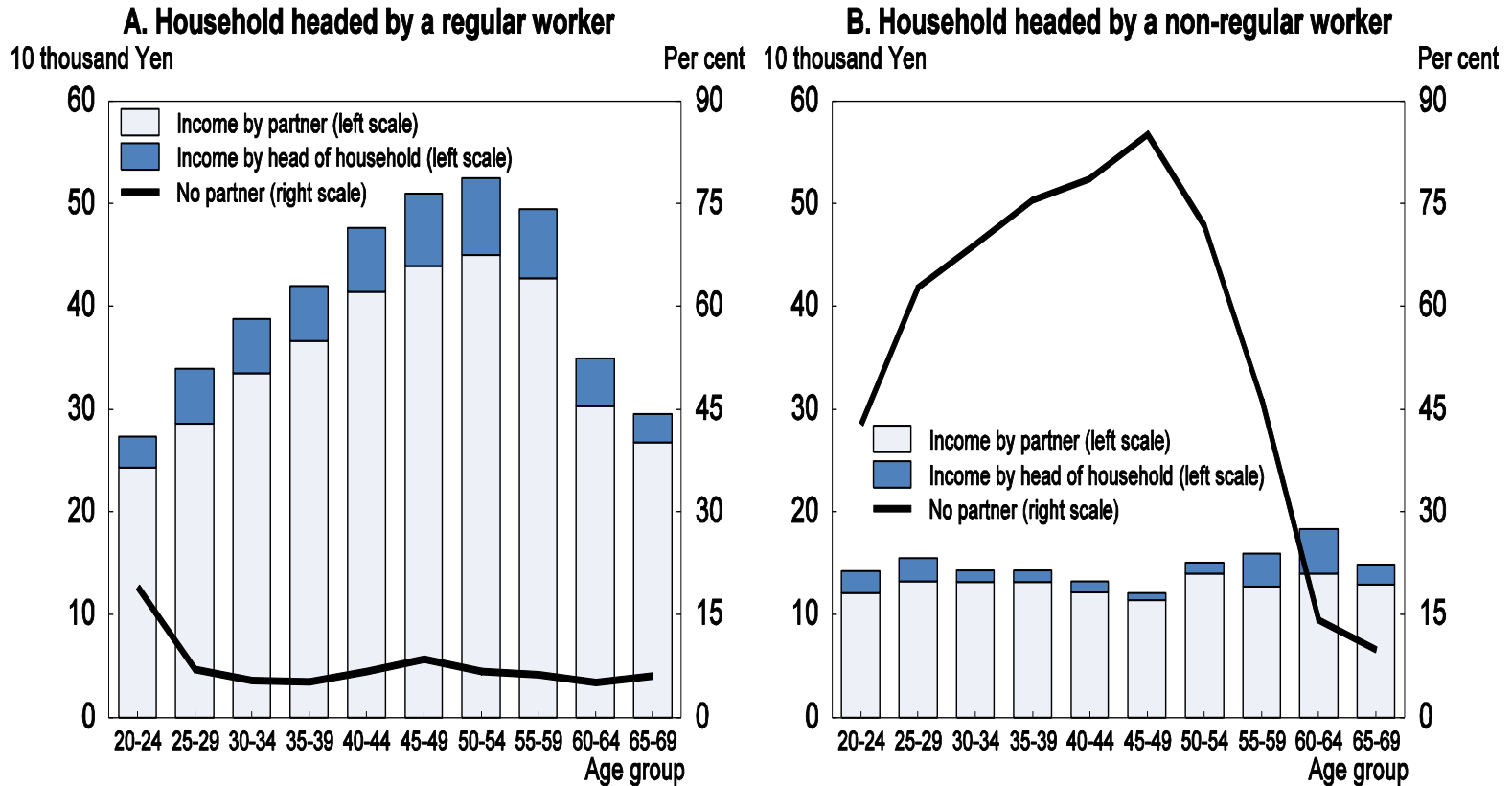


1. Data are for February for each year through 2001 and for the first quarter since 2002.

Source: Ministry of Internal Affairs and Communications, *Labour Force Survey*.



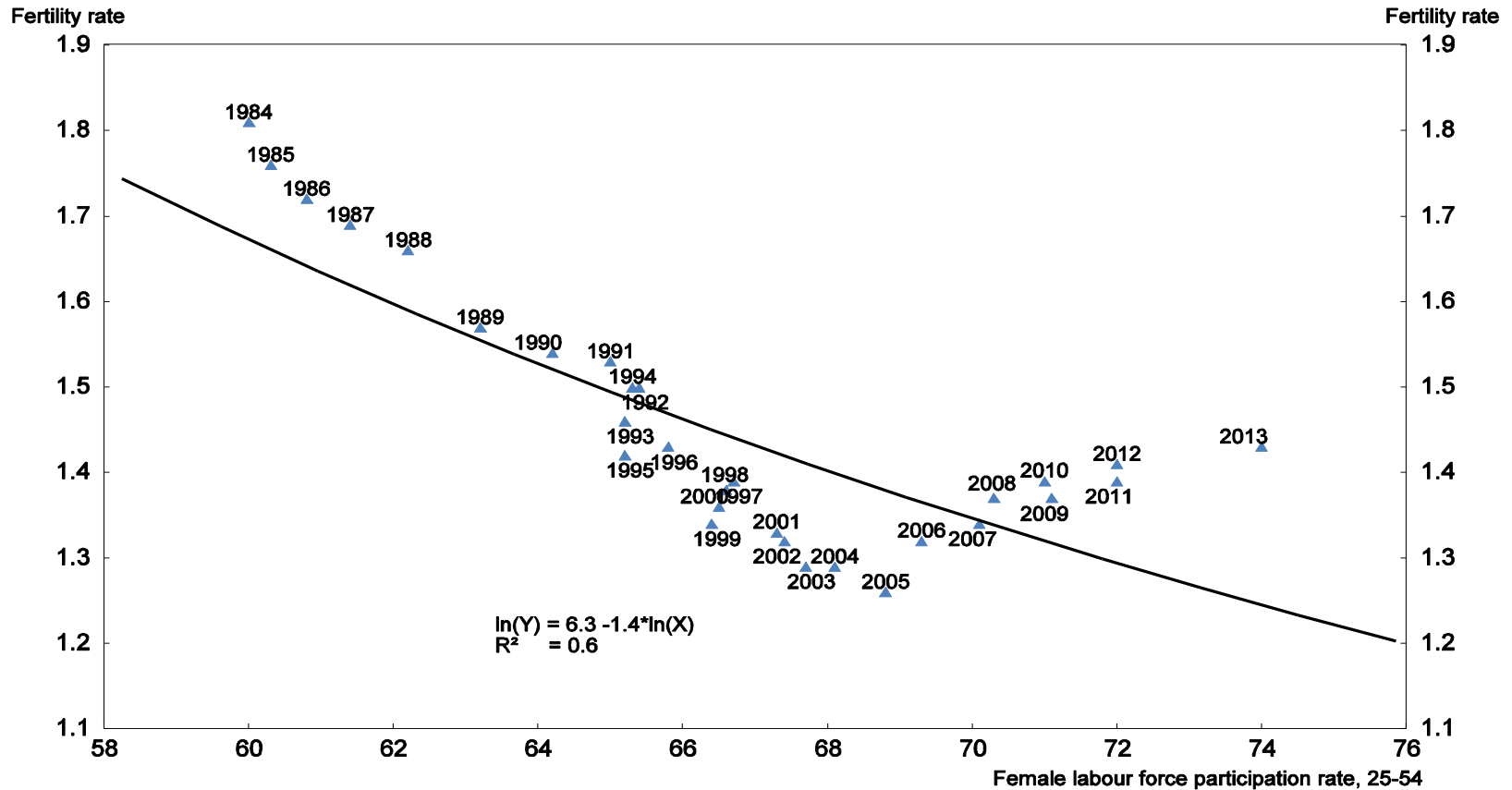
There are large income gaps between regular and non-regular workers



Source: Ministry of Health, Labour and Welfare, 2014 White Paper on Labour Economics.



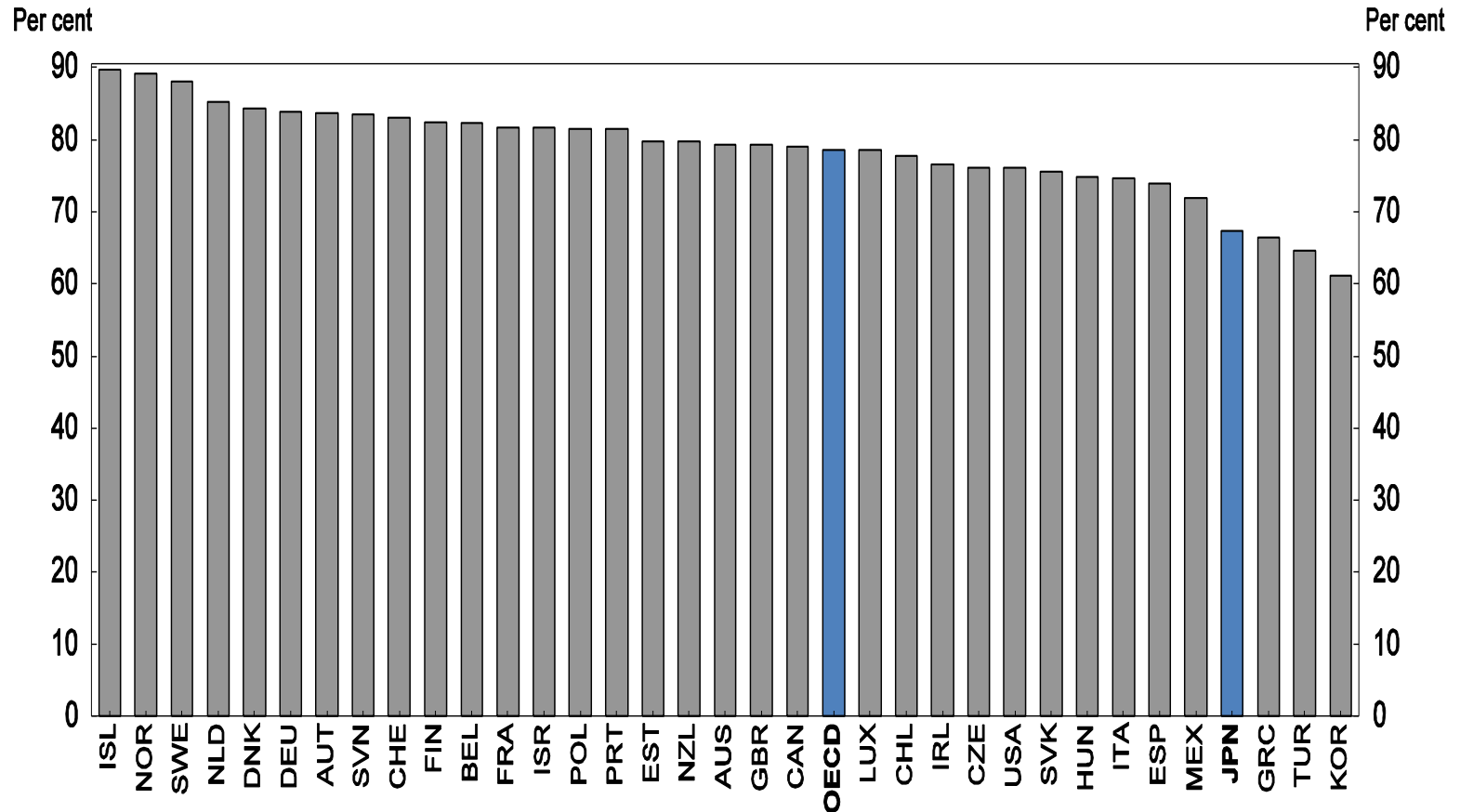
The fertility rate has fallen while female labour force participation has risen



Source: 2013 OECD Economic Survey of Japan.



The employment ratio for women with university degrees¹ in 2012



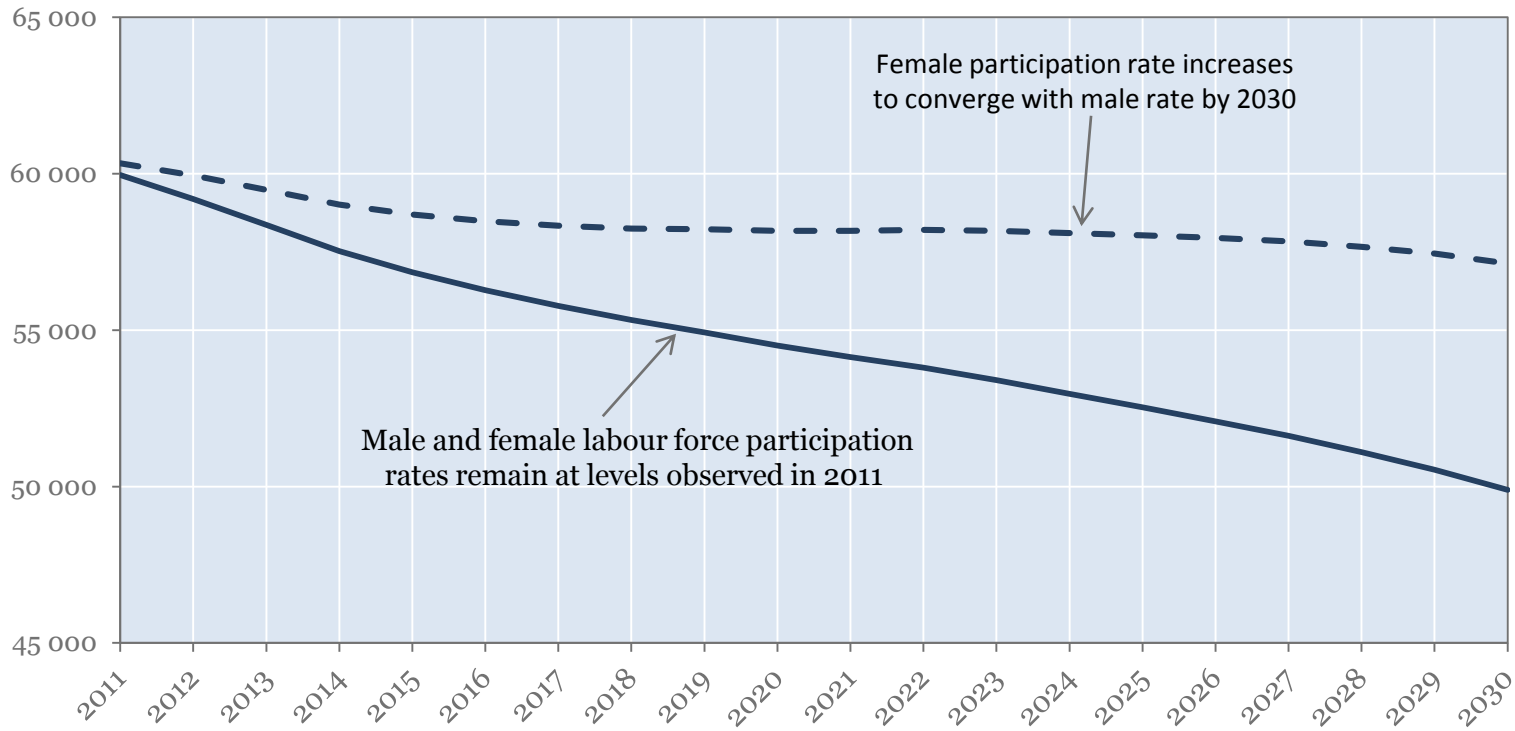
1. Including other types of tertiary education.

Source: OECD Employment Outlook, 2014.



Increasing female employment can help avoid looming labour supply shortages

Projected size of the labour force in thousands of people¹



1. Based on population projections for persons aged 15-64 years and assuming that the labor force participation rate for men remains constant from 2011 to 2030. Source: OECD (2014), "Japan – Advancing the third arrow for a resilient economy and inclusive growth", *Better Policies Series*, OECD Publishing, Paris, April, http://www.oecd.org/japan/2014.04_JAPAN_EN.pdf

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