

Highlights of the Budget for FY2007

December 2006

Ministry of Finance

Basic Concepts of the FY2007 Budget

➤ **Ensure the implementation of the expenditure reform stipulated in “Basic Policies 2006”**

➤ **4.5 trillion yen reduction of new bond issuance – the largest-ever reduction**

➤ **Together with the 1.7 trillion yen debt redemption in the special account for local allocation tax grants, substantial fiscal consolidation of 6.3 trillion yen will be achieved.**

▪ The central government’s debt in the special account for local allocation tax grants (19 trillion yen) is transferred to the general account, and 1.7 trillion yen will be redeemed in FY2007.

➤ **Prioritize budget allocation to such areas as:**

(1) strengthening economic growth

(2) giving those who have failed in business a "second chance" to build a career

(3) addressing the declining birthrate

(4) rebuilding education

General Account Budget (FY2007 Budget)

(billion yen)

	FY2006 (Initial)	FY2007 (Initial)	FY2006→FY2007	Note
(Revenues)				
Tax Revenues	45,878.0	53,467.0	7,589.0	
Non-tax Revenues	3,835.0	4,009.8	174.8	
Government Bond Issues	29,973.0	25,432.0	-4,541.0	Bond dependency ratio: 30.7% (FY2006: 37.6%)
Total	79,686.0	82,908.8	3,222.8	
(Expenditures)				
National Debt Service	18,761.6	20,998.8	2,237.2	Including increases due to the transfer of central government debt in the special account for local allocation tax grants to the general account. Most (1,732.2) is used for the redemption of transferred debt.
Local Allocation Tax Grants	14,558.4	14,931.6	373.2	
General Expenditures	46,366.0	46,978.4	612.4	Including increase due to (1) the rise in the state contribution to basic pension and the expansion of childcare allowance (134.3) and (2) addition of promotion of power resources development tax to the general account (317.9).
Total	79,686.0	82,908.8	3,222.8	

Outline of General Expenditures by Major Expenditure Programs
(FY2007 Budget)

(billion yen)

	FY2006 Budget			FY2007 Budget		
		FY2005→FY2006	% change		FY2006→FY2007	% change
Social Security	20,573.9	193.1	0.9	21,140.9	567.0	2.8
Education and Science	5,267.1	-455.9	-8.0	5,274.3	7.2	0.1
(Science only)	1,331.2	14.2	1.1	1,346.2	15.0	1.1
Former Military Personnel Pensions and Others	998.9	-70.4	-6.6	923.5	-75.4	-7.5
National Defense	4,813.9	-42.5	-0.9	4,801.6	-12.3	-0.3
Public Works	7,201.5	-329.5	-4.4	6,947.3	-254.2	-3.5
Economic Assistance	721.8	-18.6	-2.5	691.3	-30.5	-4.2
ODA (reference only)	759.7	-26.5	-3.4	729.3	-30.4	-4.0
Small and Medium Enterprises	161.6	-11.4	-6.6	162.5	0.9	0.6
Energy	470.9	-24.5	-4.9	864.7	393.8	83.6
Food Supply	636.1	-39.4	-5.8	607.4	-28.7	-4.5
Transfer to the Industrial Investment Special Account	48.1	-22.9	-32.3	20.3	-27.8	-57.8
Miscellaneous	5,122.2	-94.9	-1.8	5,194.6	72.4	1.4
Reserve Funds	350.0	0.0	0.0	350.0	0.0	0.0
Total	46,366.0	-916.9	-1.9	46,978.4	612.4	1.3

Aspects of the FY2007 Budget

➤ **New government bonds: 25,432 billion yen (down 4.5 trillion yen)**

Implement the largest reduction of new bond issuances

- Three straight years of reduction in the amount of new bond issues

FY2003	⇒	FY2004	⇒	FY2005	⇒	FY2006	⇒	FY2007 (trillion yen)
36.4		36.6		34.4		29.97		25.4
	+0.1		-2.2		-4.4	-4.5		

- Together with the 1.7 trillion yen debt redemption in the special account for local allocation tax grants, substantial fiscal consolidation of 6.3 trillion yen will be achieved.

➤ **Ratio of total new bond issues to total revenues: 30.7% (down 6.9 points)**

Three straight years of reductions have brought the ratio close to 30%.

- The second largest improvement.

FY2003	⇒	FY2004	⇒	FY2005	⇒	FY2006	⇒	FY2007
44.6%		44.6%		41.8%		37.6%		30.7%
	+0.0		-2.7		-4.2	-6.9		

➤ **Primary Balance:**

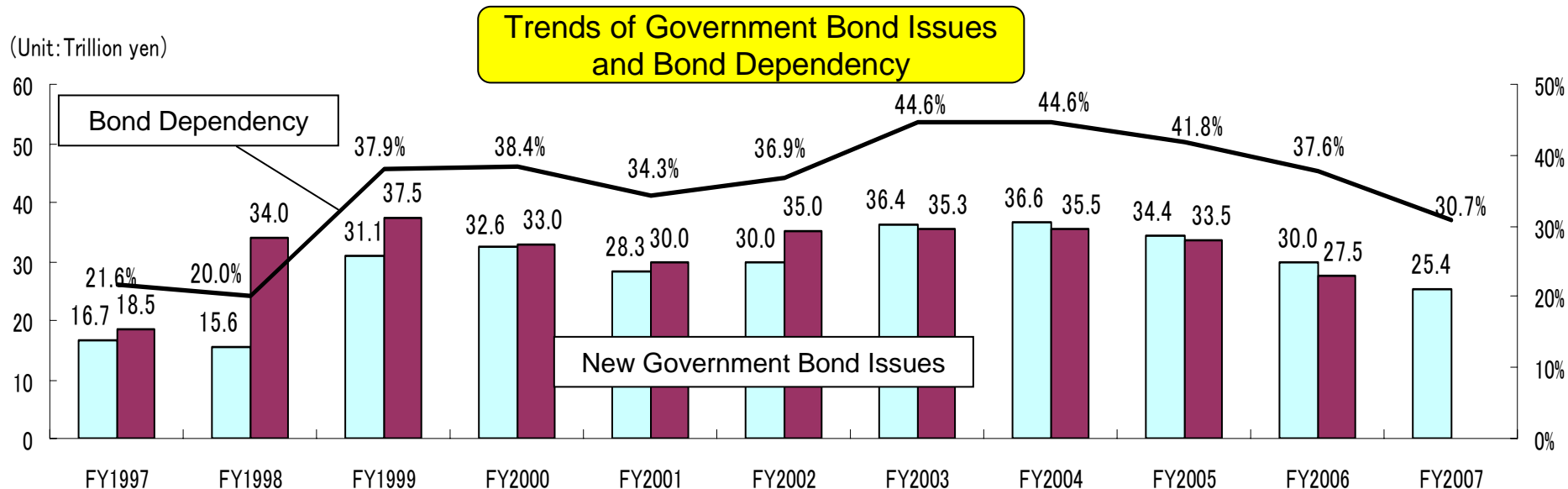
Primary budget deficit in the general account is down 4,433.2 billion yen

Exceed the pace of improvement of the previous fiscal year

- Fourth straight year of improvement since the FY2004 budget

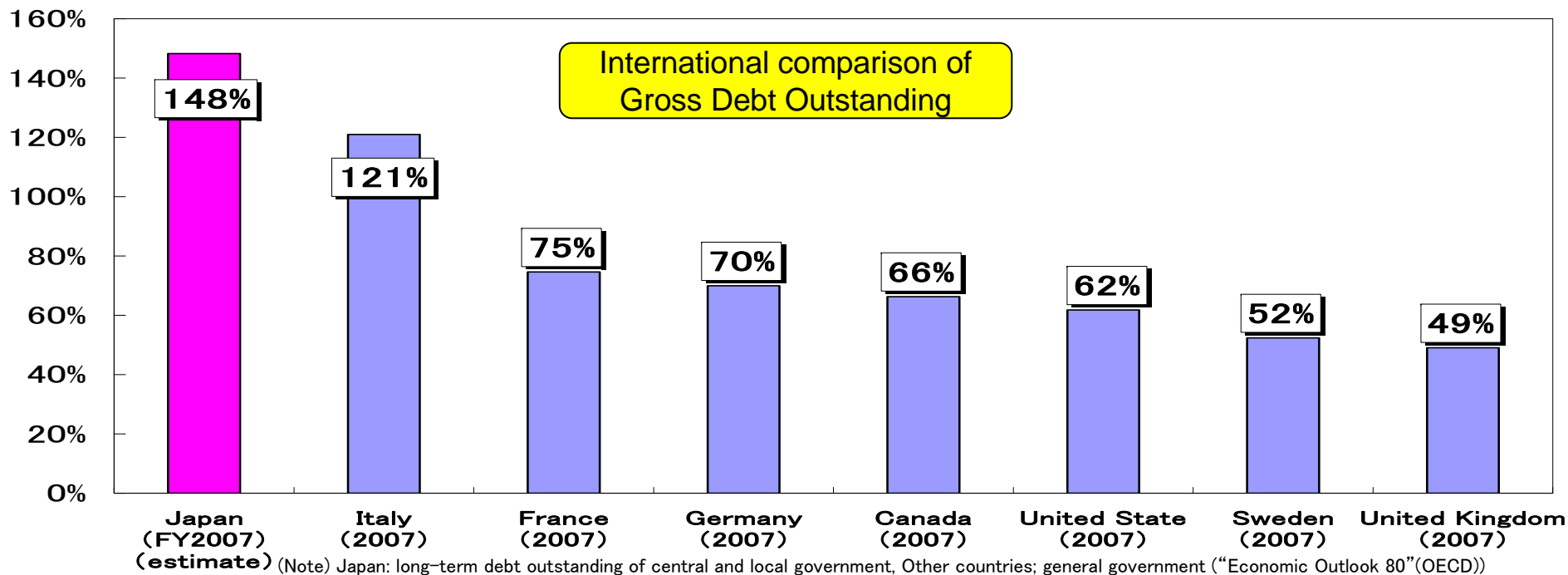
FY2003	⇒	FY2004	⇒	FY2005	⇒	FY2006	⇒	FY2007 (trillion yen)
-19.6		-19.0		-15.9		-11.2		-4.4
	+0.6		+3.1		+4.7	+6.8		

New Government Bond Issues and Debt Outstanding



(Note) Bond Dependency : based on initial budget

Government Bond Issues: Left side; Initial budget, Right side: Settlement (FY2006: Revised)



Strengthening Expenditure Reform ~ Based on “Basic Policies 2006”

Ensure the implementation of the expenditure reform in each area based on the medium-term plan for the reform of expenditures in “Basic Policies 2006”

◆ Social Security

- ▶ Curb the growth in public cost due to population aging by 220 billion yen through the following reforms:
 - Reduce the government contribution to unemployment insurance (-180 billion yen).
 - Review public assistance costs (-40 billion yen).

◆ Local Public Finance

- ▶ Personnel expense of local governments
Cut 0.4 trillion yen through net reduction in the number of public employees by 34,000 people and reform of salaries.
- ▶ Investment: Reduce by 1.5 trillion yen
(Decrease by 3% excluding the reduction of 1.2 trillion yen, which corresponds to the correction of the gap between the Local Public Finance Plan and results).
- ▶ General administration: Increase by 0.5 trillion yen
(Decrease by 1% excluding the correction mentioned above [+0.6 trillion yen])
- ▶ Ensure the total amount of general revenues such as local tax revenues and local tax allocation grants.

◆ Personnel Expenses

- ▶ Number of National Government Employees
 - Reduce the number of national public employees by 2,129 people, which substantially exceeds the FY2006 reduction (1,502 people), to achieve the target of a net reduction of more than 5.7% percent over the course of 5 years beginning in FY2006.
- ▶ National Government Personnel Expense
 - Steadily promote reform of personnel expense by the revision of comparison method of salary level in private and public sector, and salary structural reform.

◆ Public Works

- ▶ Cut public works related expenditures by more than 3 percent from the level in the previous year’s budget, continuing reform.
- ▶ Thoroughly prioritize budget allocation in regional revitalization and strengthening economic growth, and enhance efficiencies by cost reduction and bid system reform, under strict restraint of the total expenditures.

◆ Other Expenditures (ODA, Science & Technology, Defense, Education, etc.)

- ▶ **ODA:** Decrease by 4% through cost reduction and prioritization of budget allocation.
- ▶ **Science & Technology:** Increase by 1.1% by carefully selecting truly necessary expenditures and curbing allocations for low-priority projects.
- ▶ **Defense:** Decrease by 0.3% by further promoting efficiencies, while appropriately responding to issues of Missile Defense and projects related to the realignment of U.S forces in Japan.
- ▶ **Education:** Thoroughly prioritize, with substantial allocation to measures for education reforms, while cutting financial supports, such as subsidies for educational institutions, by 1% based on “Basic Policies 2006.”

Strengthening Expenditure Reform ~ Through revisions of systems and measures

◆ Reform of Special Accounts

- ▶ Enact a law on special accounts
Submit a bill to the next Diet to implement: (1) integration or abolition of special accounts (31→17), (2) adjustment of differences in rules between the general account and special accounts, and (3) promotion of information disclosure, based on the Administrative Reform Law.
- ▶ Utilize the surplus in special accounts for fiscal consolidation
Contribute to fiscal consolidation by 1.8 trillion yen by transferring the surplus in 7 special accounts to the general account under the above law.
- ▶ Cut expenditures completely
Reduce total expenditures to be targeted as the special account reform (except for overlaps between accounts, debt redemptions, and targets of other reforms such as social security reform) by 0.7 trillion yen (FY2006: 12.3 → FY2007: 11.6 trillion yen).

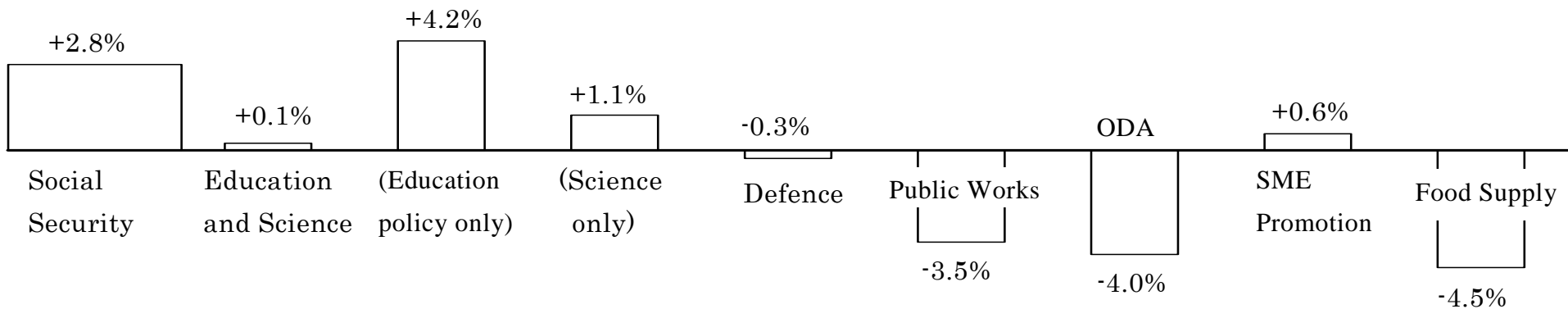
◆ Earmarked Revenues for Roads

- ▶ Conduct a revision in line with “specific measures for reviewing the earmarked revenues for roads” (decided by the Cabinet on 8 Dec. 2006).
- ▶ In the FY2007 budget, by gaining the understanding of taxpayers, realize the spirit of the reform within the existing system, and appropriate 328.6 billion yen for reduction of bond issues by the following:
 - Enlarge the part of general revenues to 180.6 billion yen
 - Do not appropriate 148 billion yen for roads and road related measures because the corresponding amount is included in the FY2006 supplementary budget for disaster relief.

Prioritization of Budget Allocation

Prioritizing budget allocation from the viewpoint of realizing “Creation and Growth” while restraining expenditures as a whole.

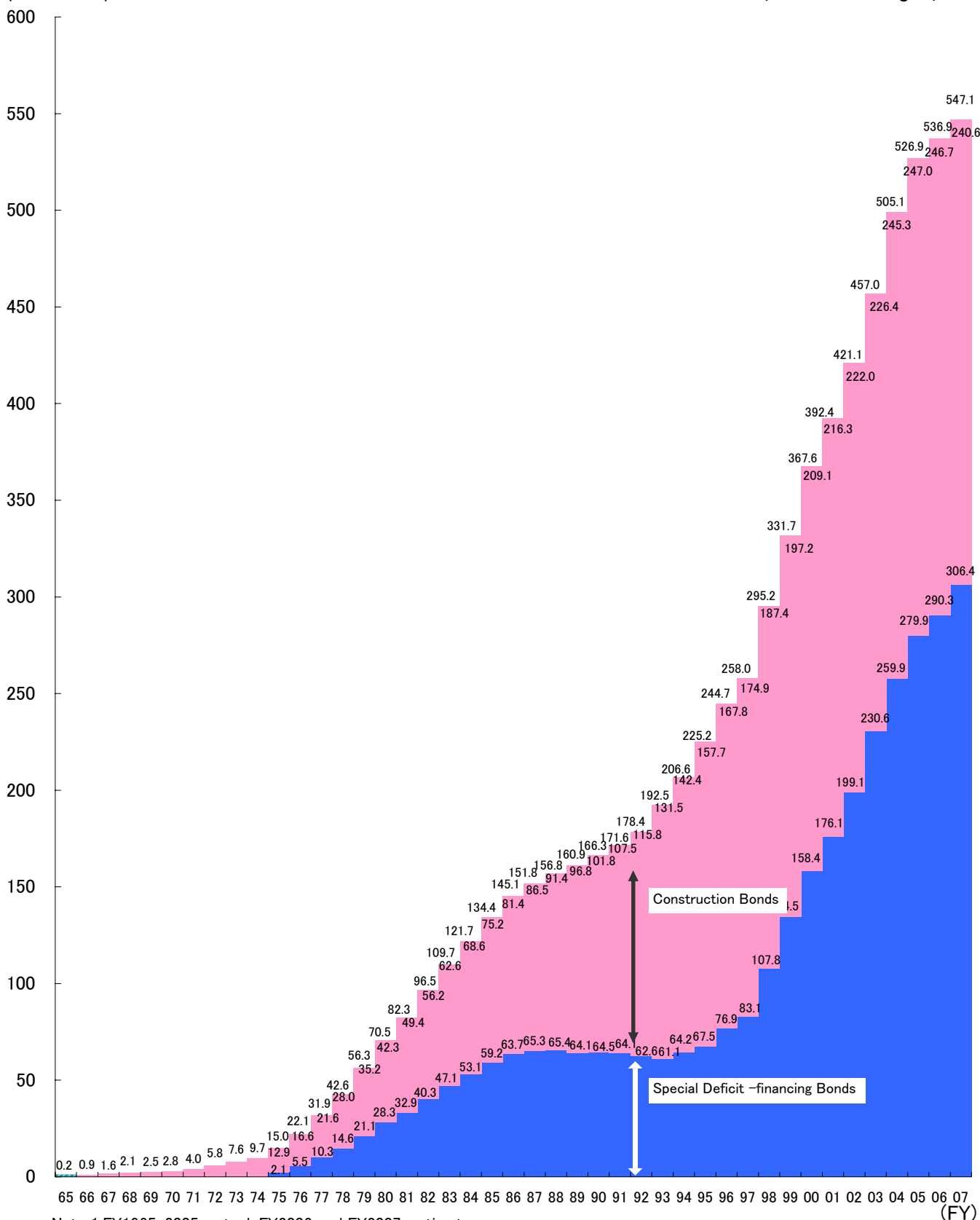
Year-on-Year Percentage Changes in Major Expenditure Categories



Trends of Accumulated Government Bonds Outstanding

(Trillion Yen)

(FY2007 Budget)



Note 1. FY1965–2005: actual, FY2006 and FY2007: estimates.

2. The special deficit-financing bonds outstanding includes refunding bonds for long term debts transferred from JNR Corp. settlement and National Forest Service, etc.

3. The estimates of FY2006 and FY2007 excluding front-loading issuance of refunding bonds is approximately 512 trillion yen, 527 trillion yen, respectively.

Long-term Debt Outstanding (FY2007 Budget)

(Unit : Trillion Yen)

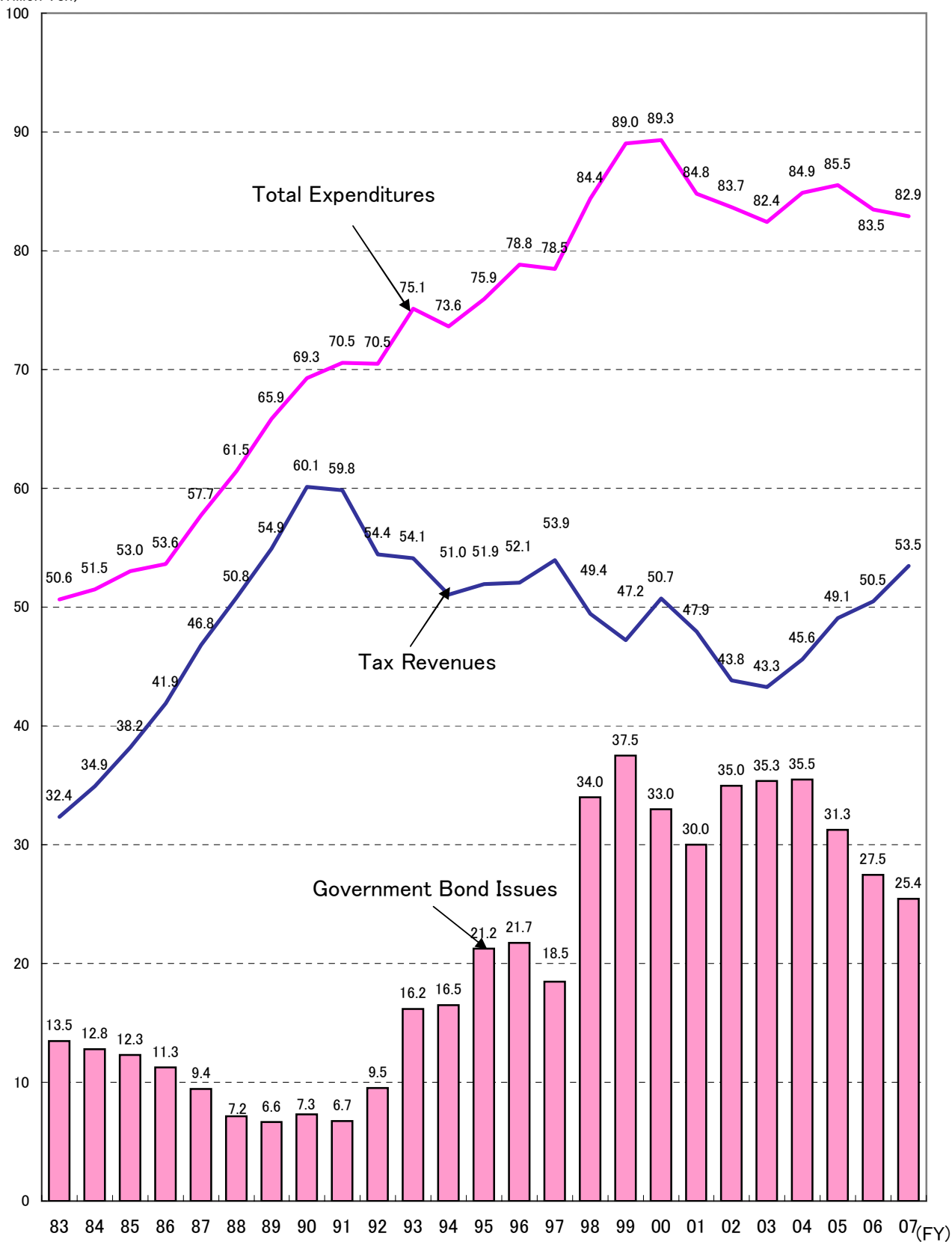
	FY1995 <Settlement>	FY2000 <Settlement>	FY2005 <Settlement>	FY2006 <Revised>	FY2007 < Budget >
Central Gov.	297	491	590 (568)	600 (575)	607 (587)
General Bonds	225	368	527 (504)	537 (512)	547 (527)
Percentage of GDP	45.4	72.9	104.7 (100.1)	105.1 (100.2)	104.8 (101.0)
Local Gov.	125	181	201	201	199
Percentage of GDP	25.1	36.0	40.0	39.4	38.1
Duplication	-12	-26	-34	-34	-33
Total	410	646	758 (735)	767 (742)	773 (753)
Percentage of GDP	82.6	128.1	150.6 (146.1)	150.2 (145.3)	148.1 (144.2)

(Note)

1. GDP for FY2006: estimates, FY2007: forecast
2. Figures in parentheses exclude front-loading issuance of refunding bonds.
3. Government bonds outstanding of Special Account for Fiscal Loan Program Funds is 143 trillion yen as of the end of FY2007.

Trends of General Account Tax Revenues, Total Expenditures, and Government Bond Issues

(Trillion Yen)



Nominal

GDP

(Trillion Yen)

286.3

359.5

483.8

513.3

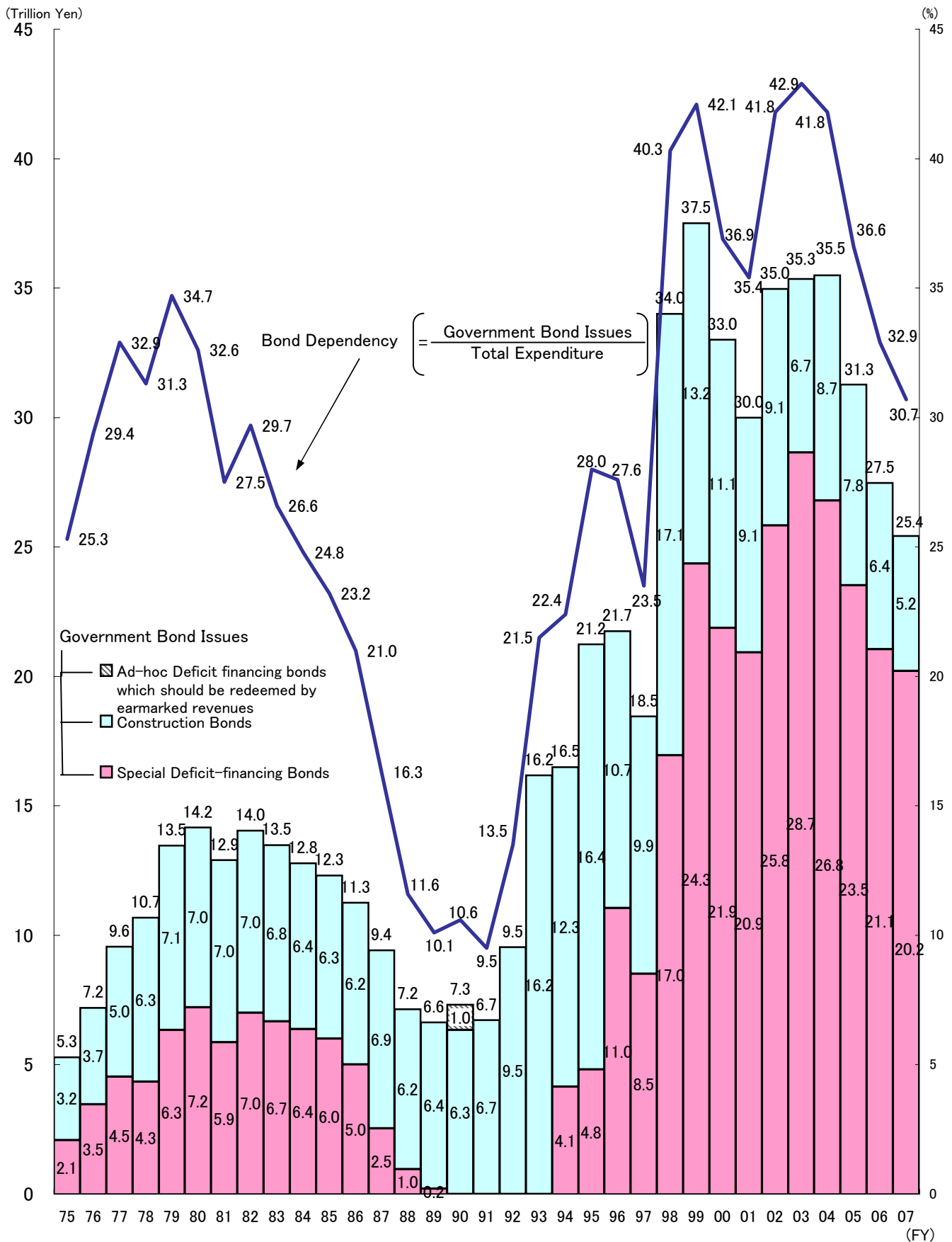
489.9

521.9

(FY2007: estimates)

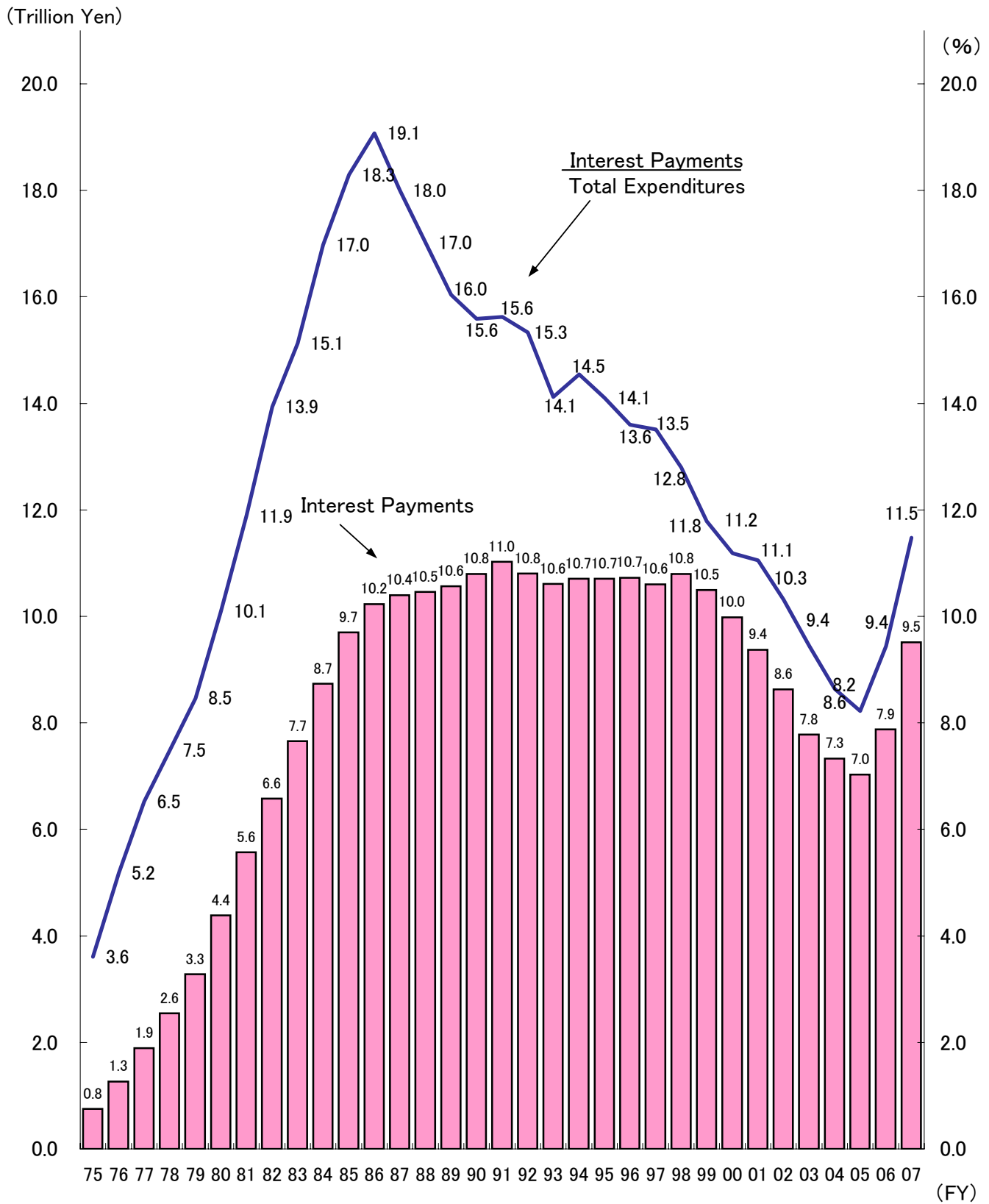
(Note) FY1983–2005: settlement, FY2006: revised, and FY2007: budget.

Trends of Government Bond Issues (FY2007 Budget)



(Note) FY1975-2005: settlement, FY2006: revised, FY2007: budget

Trends of Interest Payment of Government Bonds (FY2007 Budget)



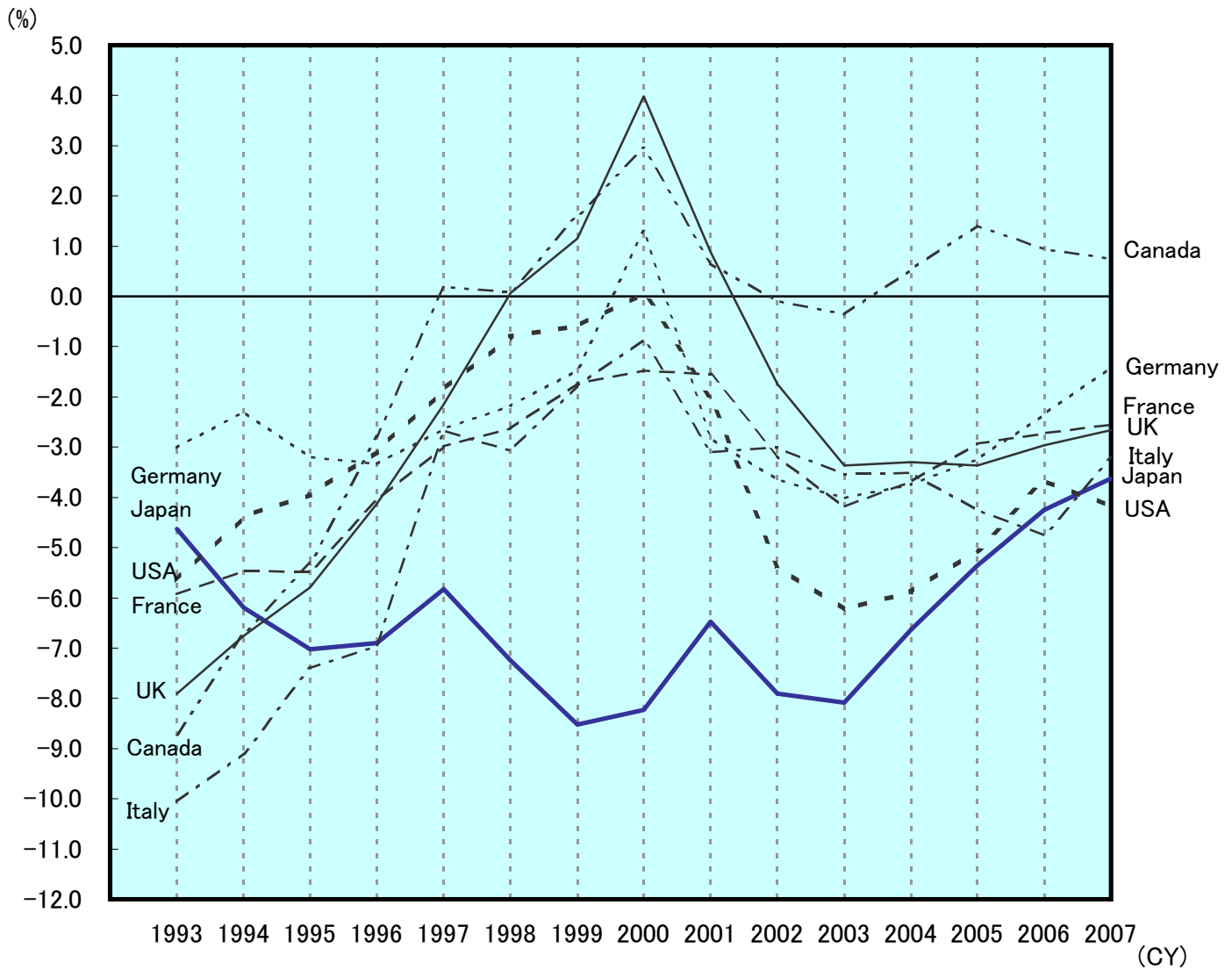
(Note) FY1975–2005: settlement, FY2006: revised, FY2007: budget

General Government Financial Balances (International Comparison)

(As a percentage of GDP)

(CY)	1993	1994	1995	1996	1997	1998	1999	2000	2001	2002	2003	2004	2005	2006	2007
Japan	-4.6	-6.2	-7.0	-6.9	-5.8	-7.2	-8.5	-8.2	-6.5	-7.9	-8.1	-6.6	-5.4	-4.3	-3.6
United States	-5.6	-4.4	-3.9	-3.1	-1.9	-0.8	-0.6	0.1	-2.0	-5.4	-6.2	-5.9	-5.0	-3.7	-4.2
United Kingdom	-7.9	-6.8	-5.8	-4.1	-2.1	0.1	1.2	4.0	0.9	-1.7	-3.4	-3.3	-3.4	-3.0	-2.7
Germany	-3.0	-2.3	-3.2	-3.3	-2.6	-2.2	-1.5	1.3	-2.8	-3.6	-4.0	-3.7	-3.2	-2.3	-1.4
France	-5.9	-5.5	-5.5	-4.1	-3.0	-2.6	-1.7	-1.5	-1.6	-3.2	-4.2	-3.7	-2.9	-2.7	-2.5
Italy	-10.1	-9.1	-7.4	-7.0	-2.7	-3.1	-1.8	-0.9	-3.1	-3.0	-3.5	-3.5	-4.3	-4.8	-3.2
Canada	-8.7	-6.7	-5.3	-2.8	0.2	0.1	1.6	2.9	0.7	-0.1	-0.4	0.5	1.4	0.9	0.8

※ Source: OECD Economic Outlook 80 (December 2006). Figures are calculated on an SNA basis.
 Japan and United States: General government financial balance excluding social security.



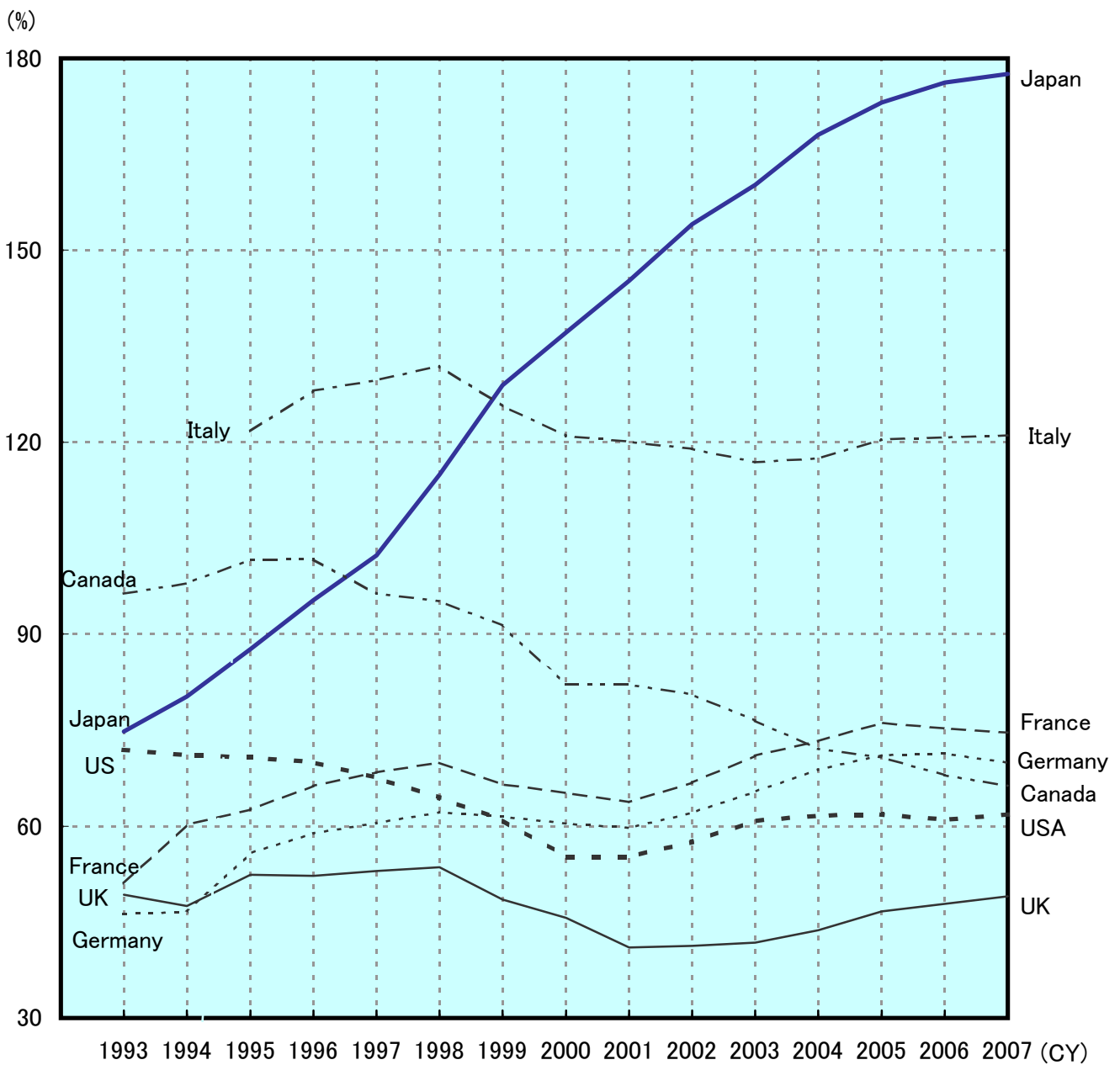
(Note) FY2007 budget is not reflected in the above data.

General Government Gross Debt (International Comparison)

(As a percentage of GDP)

(CY)	1993	1994	1995	1996	1997	1998	1999	2000	2001	2002	2003	2004	2005	2006	2007
Japan	74.7	80.2	87.7	95.3	102.3	114.9	128.9	137.1	145.2	154.0	160.2	168.1	173.1	176.2	177.6
United States	71.9	71.1	70.7	70.0	67.6	64.5	61.0	55.2	55.2	57.5	60.8	61.6	61.8	60.9	61.8
United Kingdom	49.3	47.5	52.4	52.2	53.0	53.6	48.5	45.7	41.0	41.3	41.8	43.7	46.7	47.9	49.0
Germany	46.2	46.6	55.7	58.9	60.4	62.2	61.5	60.4	59.7	62.1	65.4	68.8	71.1	71.3	69.9
France	51.0	60.2	62.6	66.3	68.4	69.9	66.5	65.2	63.8	66.8	71.0	73.3	76.1	75.3	74.6
Italy	-	-	121.8	128.1	129.7	132.0	125.7	121.0	120.1	119.0	116.9	117.5	120.4	120.8	121.0
Canada	96.3	98.0	101.6	101.7	96.3	95.2	91.4	82.1	82.1	80.6	76.5	72.1	70.8	68.0	66.3

※ Source: OECD Economic Outlook 80 (December 2006). Figures are calculated on an SNA basis.



(Note) FY2007 budget is not reflected in the above data.