Chapter 1 : Current and Future Status of the Global Economy in Transition

Section 2 Major countries and regions: current status and issues

1. The economy of the United States

(1) The U.S. economy in a moderate recovery phase

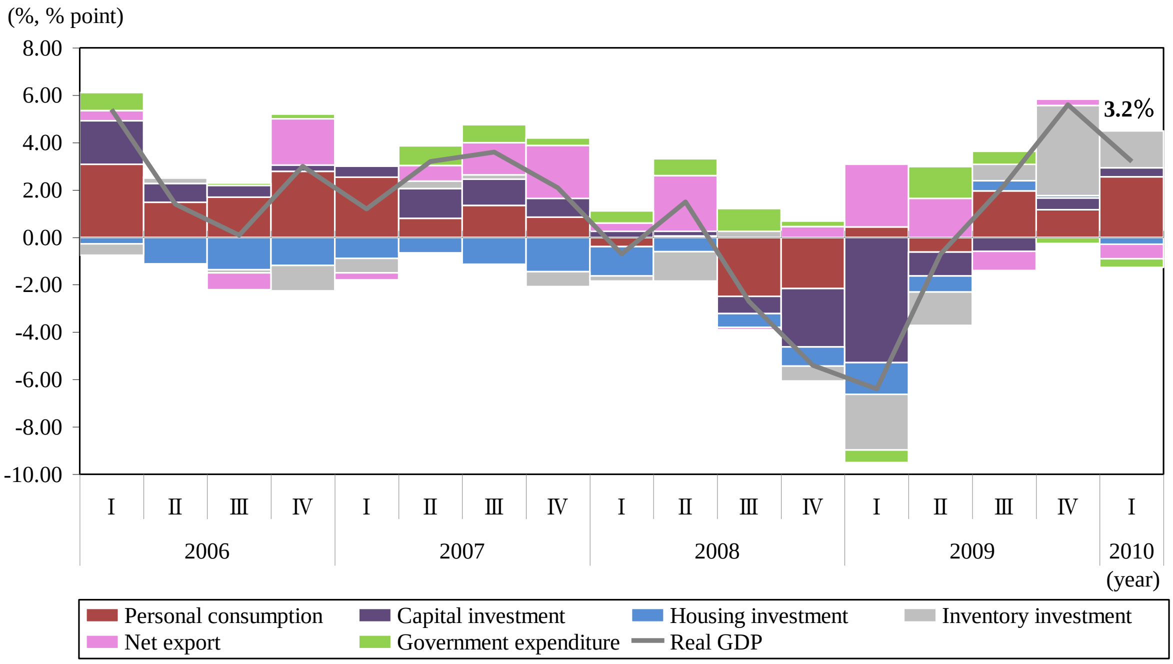
The U.S. economy is gradually reviving, with the support of the large-scale economic stimulus measures executed by the government, the monetary easing measures taken by the Federal Reserve Board (FRB), and the reexpansion of the world economy. However, there are still issues facing sustainable growth, such as continued high unemployment. Below, we will summarize and examine the current status of the U.S. economy, and the issues it faces.

(A) GDP Growth

The preliminary data for real GDP growth from the first quarter of 2010 posted a quarter-on-quarter annualized rate of 3.2%, marking a third consecutive quarter of growth (see Figure 1-2-1-1). The U.S. real GDP growth rate registered a fourth consecutive quarter of negative growth, starting from the third quarter of 2008 when the Lehman shock occurred, showing a decline of 2.7%, 5.4%, 6.4% and 0.7% on a quarter-on-quarter annualized rate basis.[1] However, due to factors including the substantial economic measures implemented by the government and the monetary relaxation policy arranged by the FRB, real GDP rebounded and achieved a growth 2.2% in quarter-on-quarter annualized rate in the third quarter of 2009 and continued to grow strongly, marking 5.6% in the following quarter, partially due to inventory investment, the decline of which drastically slowed down, and capital investment, which also took a favorable turn. The preliminary data for GDP growth in the first quarter of 2010 showed a 3.2% quarter-on-quarter annualized rate growth due to factors such as a large increase in personal consumption.

1-2-1-1 US Trends in Real GDP Growth and Contributions by Demand Item

[1] It is the first time to register four consecutive quarters of negative growth since the start of current statistics of 1947.



Note: Seasonally adjusted. Year-on-year change. The data for the 1st quarter of 2010 is based on an immediate report.
Source: United States Department of Commerce

(B) Personal consumption

Personal consumption, which accounts for 70% of U.S. GDP, showed signs of recovery, supported by the effects of government policy. Personal consumption showed improvement in the third quarter of 2009, posting a quarter-on-quarter annualized rate of 2.8%. A breakdown of personal consumption for the period confirms the significant contribution to the increase in automobile purchases made by the government-driven Car Allowance Rebate System[2], which promoted replacing of old cars with new (see Figure 1-2-1-2). Although automobile purchases declined after the fourth quarter with the end of the scheme, total personal consumption remained positive for three successive quarters.

Although personal consumption has begun to recover, it is only weakly supported by income. In the United States, where drastic employment regulations have been brought into effect following the financial crisis, the growth of wages remains weak. Looking at factors driving fluctuations in disposable income, we find that tax cuts (maximum $400 per person), a part of wider economic measures, and a temporary benefit for pensioners ($250) contributed to improving income before the period from March to May 2009. However, since June 2009, the effect of economic stimulus programs on income has been wearing off. The growth in wages remains weak and is hindering full-scale recovery of personal consumption (see Figure 1-2-1-3).

Besides income, the environment remains severe for personal consumption owing to factors such as continuing tight credit conditions and balance sheet adjustments in a household sector burdened with excessive debt.

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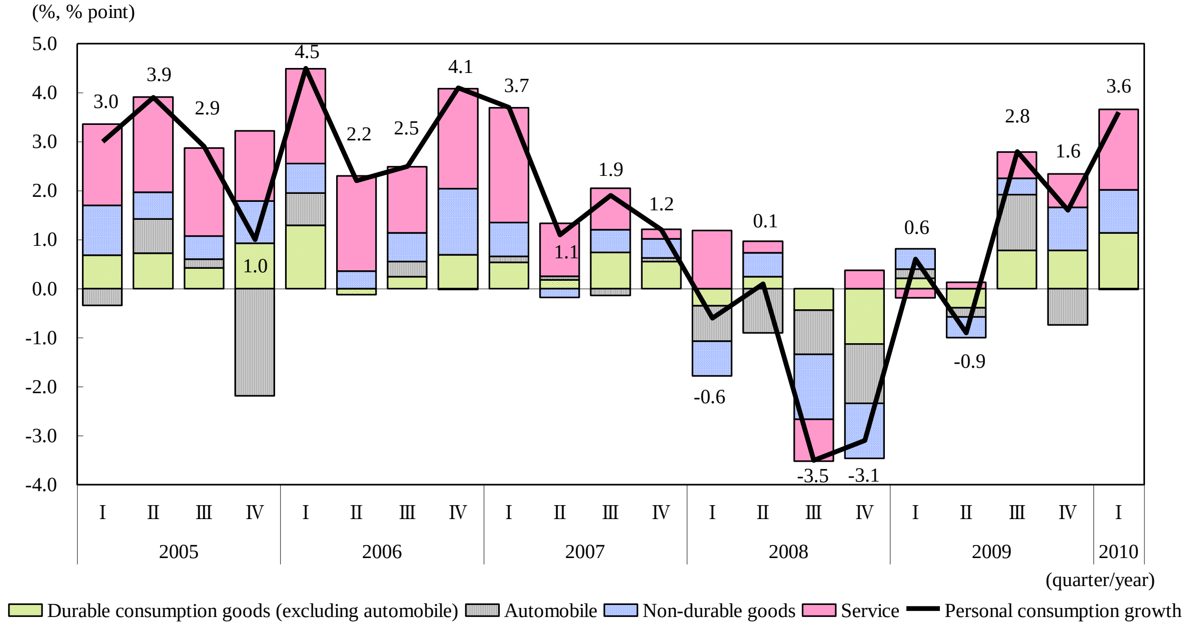
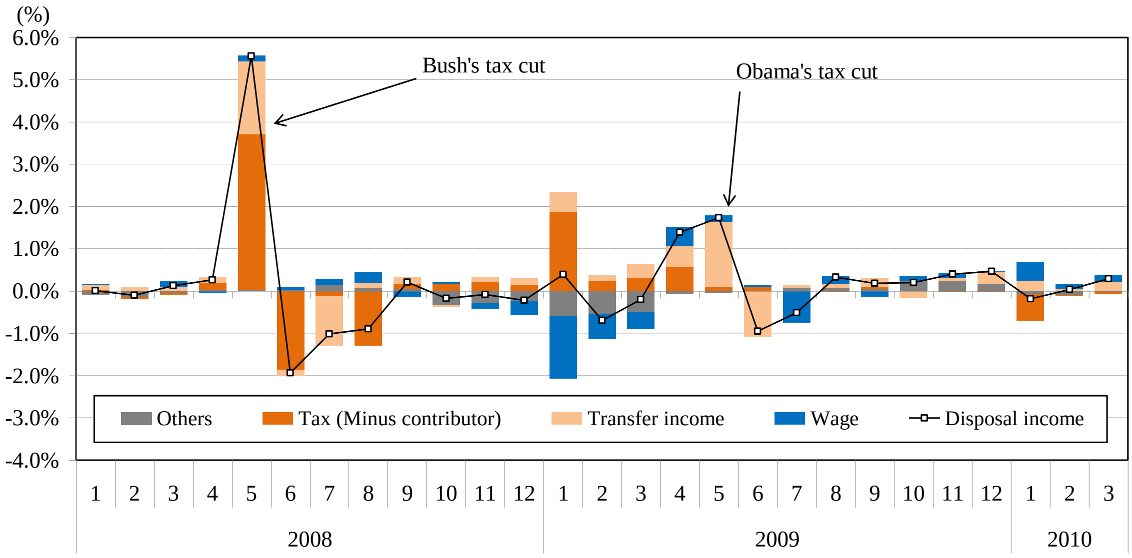
2 Car Allowance Rebate System was established in June 2009 to facilitate environmental measures and to support the automobile industry. The conditions of this Car Allowance Rebate System which grants up to 4,500 of subsidy are: (i) Model of 1984 to 2001, (ii) Trade a usable used-car in for energy efficiency 18 miles or less per gallon, and (iii) Purchase or lease an energy-efficient car of $45,000 or less. A dealer is accountable for abolishing the vehicle not reselling it. According to the U.S. Department of Transportation, the applications for 691,000 cars worth $2,880 million were submitted and the plan promoted the shift from large-sized vehicles to energy-efficient small models. Moreover, in "The Economic Analysis of the Car Allowance Rebate System("Cash for Clunkers"), Council of Economic Advisers (CEA) estimated that this system would push up the baseline of car sales by 330,000 cars in 2009 and reduce the sales by 70,000 to 80,000 cars with the reverse effect in 2010.

1-2-1-2 US Trends in Contribution by Personal Consumption Expenditure



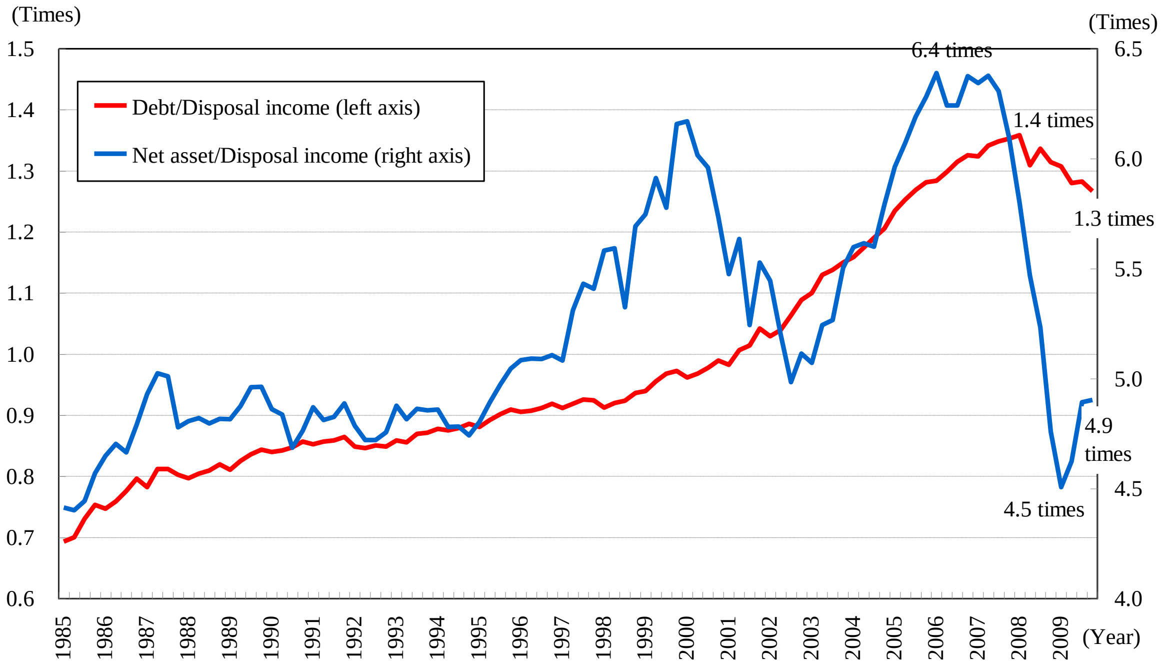
Note: Seasonally adjusted. Year-on-year change. The data for the 1st quarter of 2010 are based on an immediate report.
Source: United States Department of Commerce

1-2-1-3 Causes of Changes in US Disposable Income



Source: United States Department of Commerce (Month/year)

1-2-1-4 Trends in US Household Debt and Net Assets



Source: FRB

1-2-1-5 US Household Net Assets

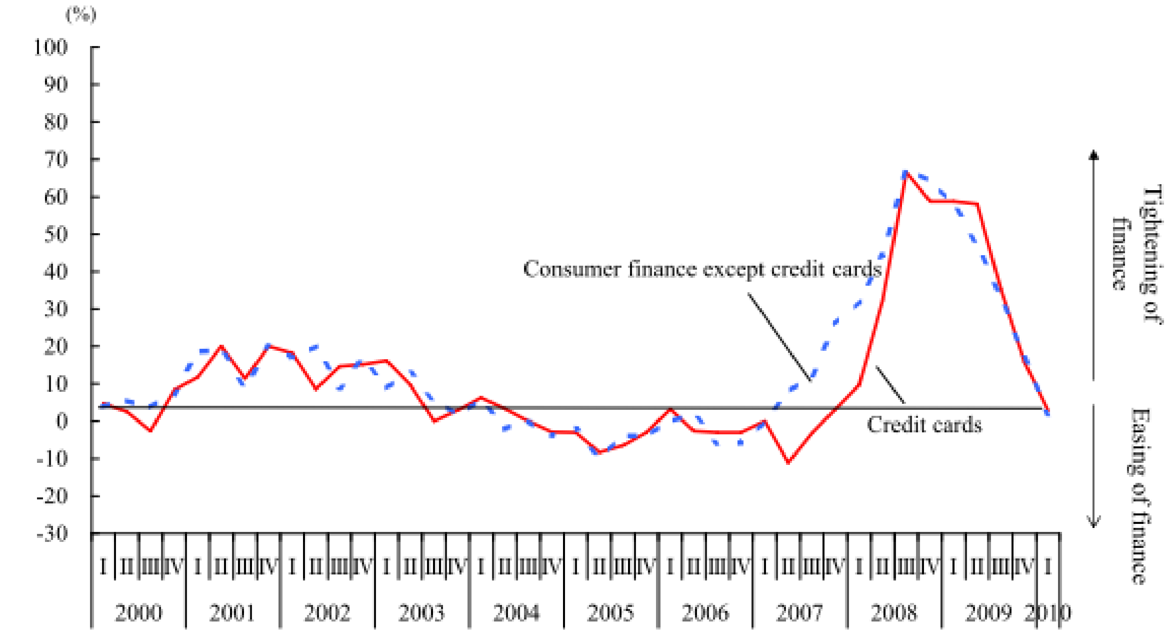
(US$ billion)

	2005	2006	2007	2008	2009
Net asset	59,580	64,464	64,484	51,404	54,176
Net asset increase ratio (%)	12.1	7.9	-1.2	-21.8	3.4
Net asset changes	6,694	4,885	19	-13080	2773
Changes in market value of owned asset	6,386	4,693	-748	-14052	1750
Real estate	3,096	652	-2226	-4484	-1008
Shares	919	2,097	767	-3612	1691
Mutual fund	194	342	201	-1382	555
Own capital for self-employed business	1,686	498	-1	-1462	-822
Life insurance and pension reserve	491	1,104	511	-3112	1334
Disposal income	9,487	10,111	10,578	10,799	11,050
Net asset disposal income ratio (times)	6.3	6.4	6.1	4.8	4.9
Household saving ratio (%)	1.4	2.4	1.7	2.7	4.3

Source: FRB

The balance sheet for the household sector shows that the ratio of disposable income to net assets at the end of the fourth quarter of 2009 was 1:4.9 (see Figure 1-2-1-4). From the end of 2008 through to the end of 2009, the net assets of the sector increased by $2,773 billion, while the increase in retained assets was only $1,750 billion. The difference was due to debt redemption. After the household sector curbed consumption and strengthened debt adjustments, the savings rate increased from 2.7% in 2008 to 4.3% in 2009. Although the ratio of disposable income to debts declined to 1:1.3 at the end of the fourth quarter of 2009 from its peak of 1:1.4 at the end of the first quarter of 2008, excessive debt adjustment still represents a serious issue for further recovery (see Table 1-2-1-5).

1-2-1-6 Changes in Lending Attitudes of US Financial Institutions (Consumer Credit)

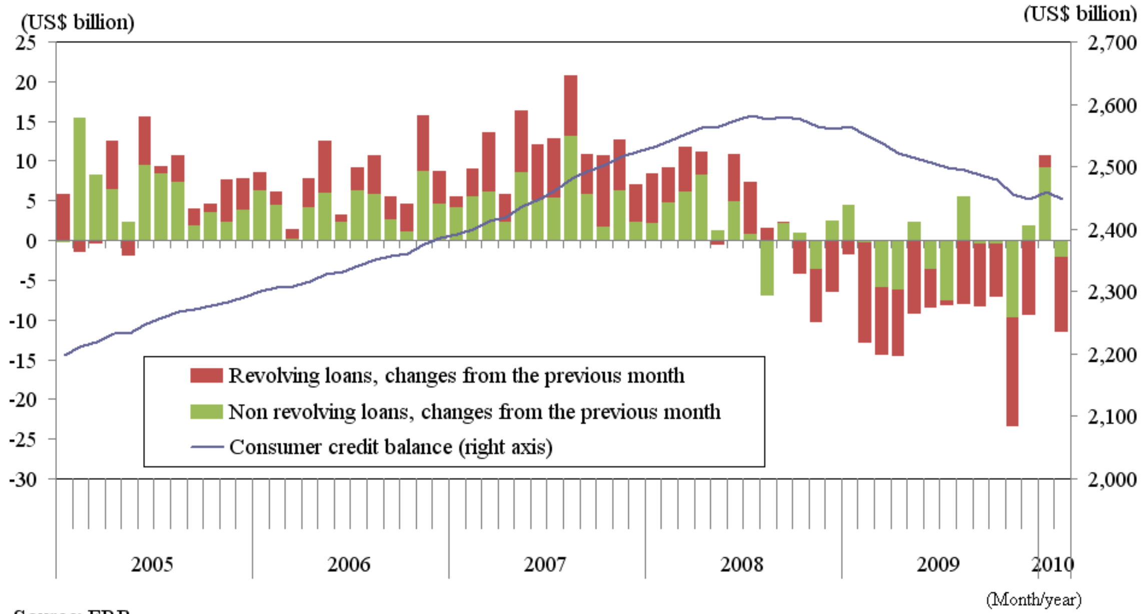


Note: The ratio of the number of banks that tightened lending standard after the previous survey after deducting the number of banks that eased the standards in total

Source: FRB

The lending (consumer credit) climate among financial institutions continues to harden, although the pace of this is slowing (see Figure 1-2-1-6). While the consumer credit balance has been shrinking, revolving loans mainly for credit cards posted a steeper drop (see Figure 1-2-1-7). The decrease of the balance of consumer credit has been influenced not only by the tightening stance on lending, but also by consumers' cautiousness towards borrowing money with their credit cards.

1-2-1-7 Trends in US Consumer Credit Balance



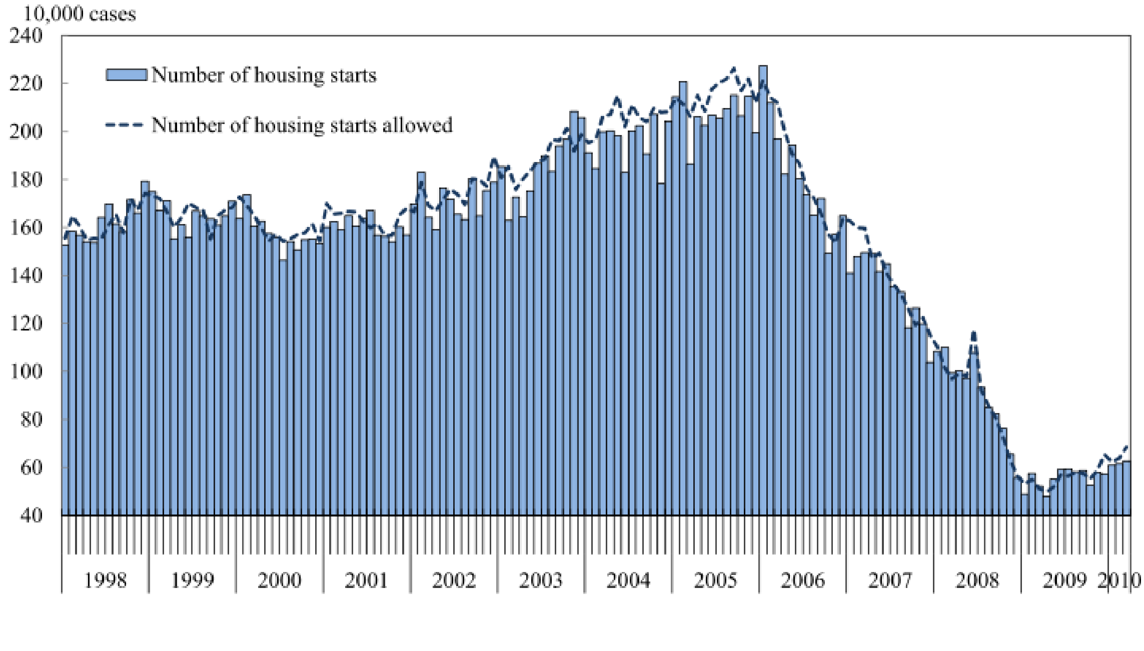
Source: FRB

(C) The housing market

After fifteen quarters, housing investment took a turn for the better, registering a quarter-on-quarter annualized growth of 18.9% in the third quarter of 2009, and stayed positive for the second consecutive quarter, registering a 3.8% increase in the fourth quarter. However, it ended at minus

10.9% (preliminary data) in the first quarter of 2010 (see Figure 1-2-1-1). The number of new homes being built and the number of new-home building permits, while remaining low, have shown steady progress; the number of new and existing homes being sold has been alternating between growth and decline. This has been due to a surge in last-minute demand, and the ensuing reverse effect, caused by the extension in both scope and time (from November 2009 to April 2010) of the tax cut program, which offered up to an $8,000 tax break to new-home buyers[3] (see Figure 1-2-1-8 and Figure 1-2-1-9). The delinquency rate for mortgage loans and the ratio of loans provided for houses undergoing foreclosure both remain high, and progress towards house price recovery is faltering at best (see Figure 1-2-1-10).

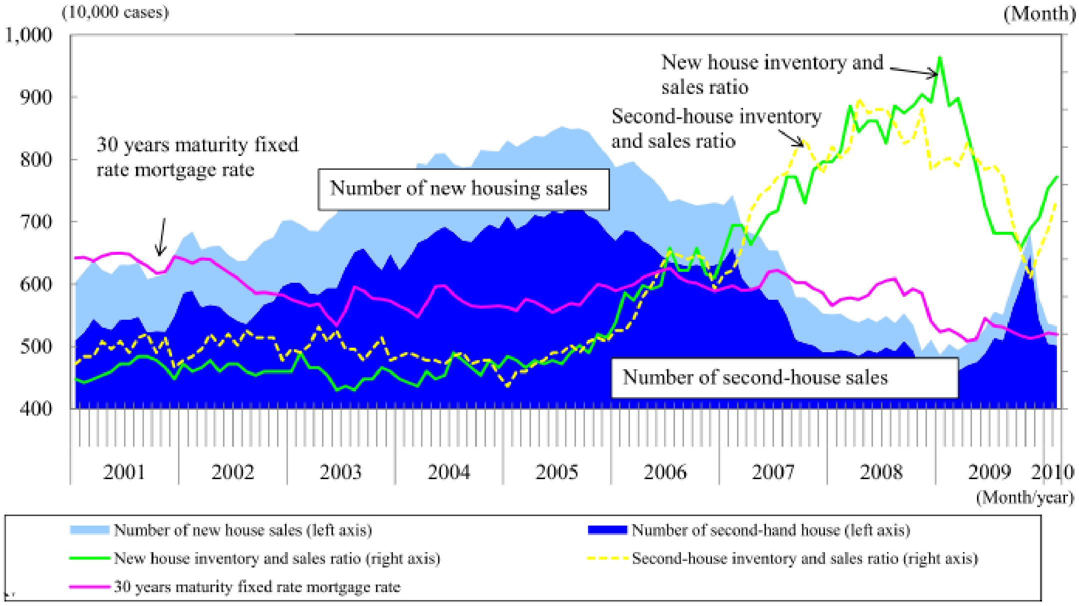
1-2-1-8 Transition of Housing Starts in USA



Note: Seasonally adjusted. Converted to annual rate.
Source: United States Department of Commerce

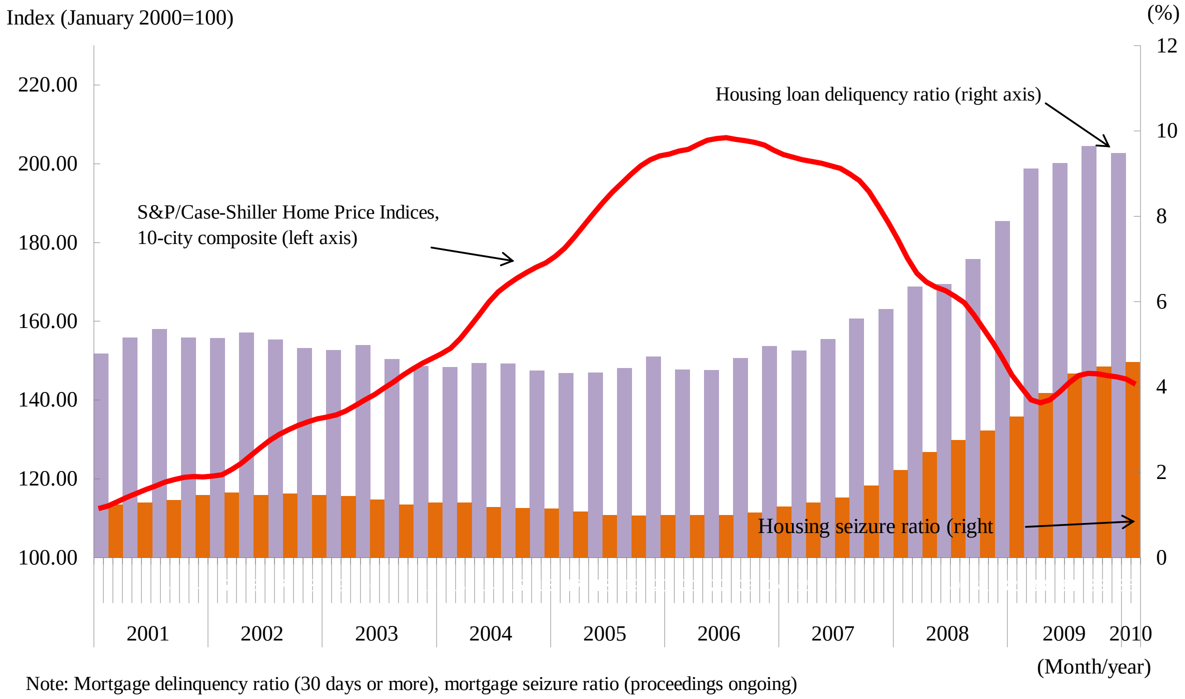
1-2-1-9 Trends in New and Old Home Sales, Inventory Sales Ratio and Home Loan Interest

[3] The tax cut program for new home buyers was extended till April 2010. In addition, a bill to grant up to $6,500 tax break to non-new home buyers passed in the beginning of November.



Note: 1. Seasonally adjusted. Converted to annual data.
2. Inventory sales ratio is the index to represent the volume of housing inventory indicated as the number month of inventory based on current housing demand assuming that there is no additional supply of housing. National Association of Realtors estimates ordinary inventory sales ratio to be about 4 to 5 months.
Source: United States Department of Commerce, National Association of Realtors

1-2-1-10 Trends in US Home Prices, Home Loan Delinquency Ratio and Seizure Ratio



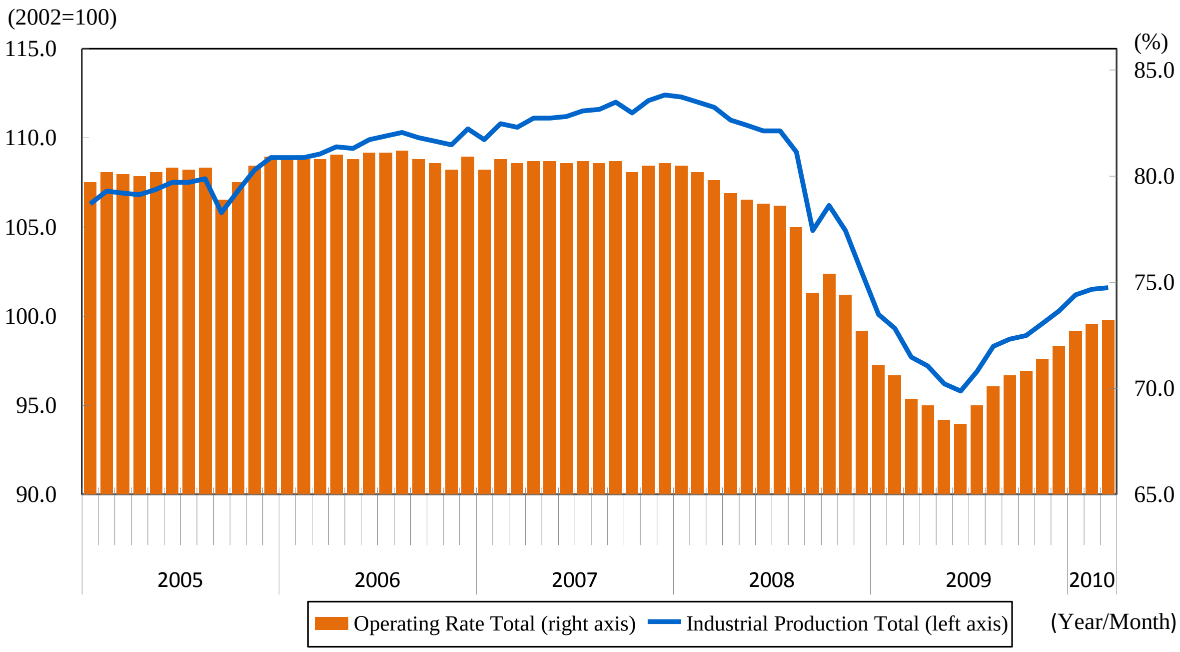
Note: Mortgage delinquency ratio (30 days or more), mortgage seizure ratio (proceedings ongoing)
Sources: Standard & Poor's, Mortgage Bank Association

(D) Capital investment

Activity is reviving in corporate production, primarily due to the recovery of the world economy (see Figure 1-2-1-11). The rate of operation for production facilities is increasing together with expanding production。 However, the level is still way below the average of the period from 1972 to 2008 (80.9%).

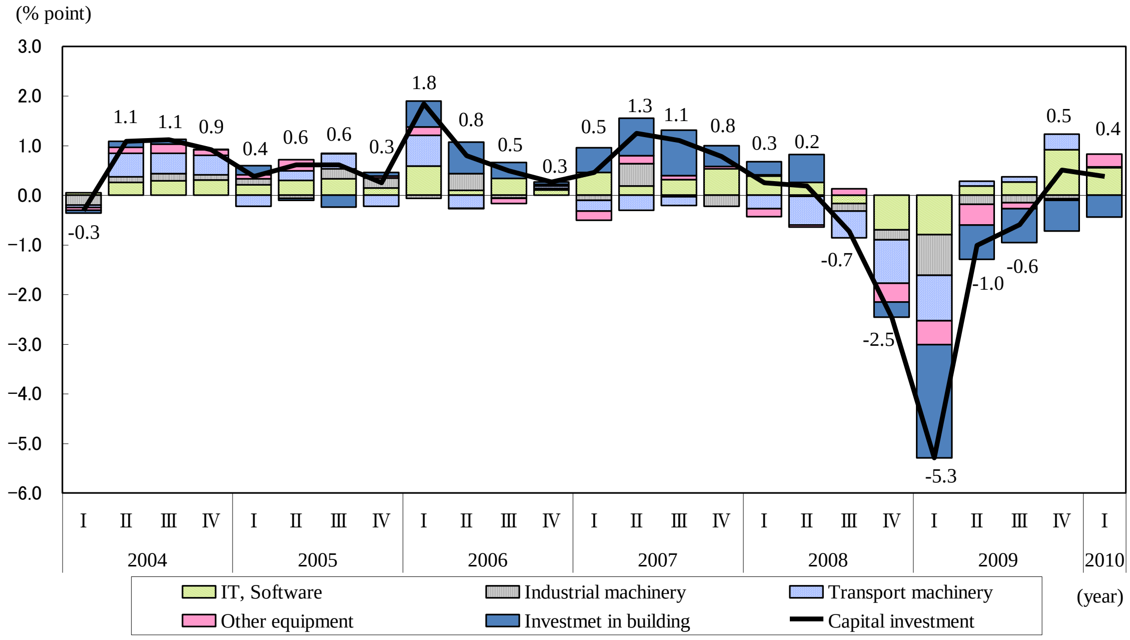
Meanwhile, capital investment took a favorable turn, registering a quarter-on-quarter annualized increase of 5.3% in the fourth quarter of 2009 – the first increase in six quarters – and recording a second successive period of growth in the first quarter of 2010, marking a 4.1% increase (preliminary data) (see Figure 1-2-1-1). While IT and software investment is recovering, investment in structures is continuously showing a significant drop owing to prolonged issues in commercial real estate (see Figure 1-2-1-12 and Figure 1-2-1-13).

1-2-1-11 Trends in US Industrial Production Index and Operating Ratio



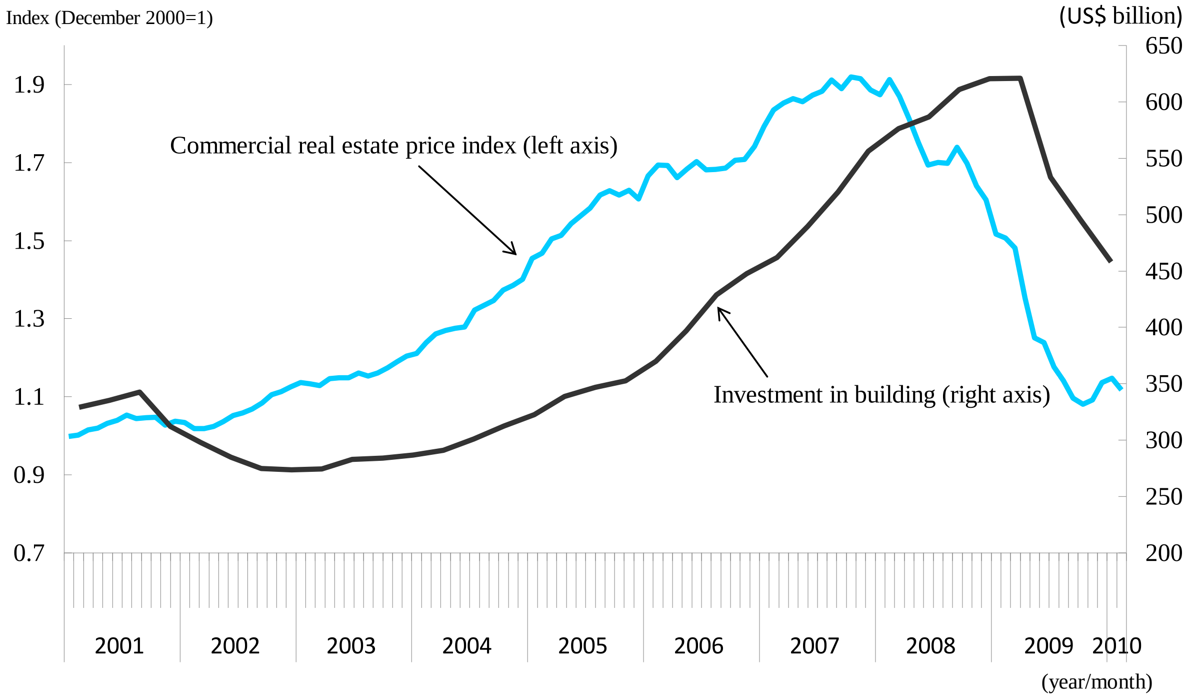
Note: Seasonally adjusted.
Source: FRB

1-2-1-12 Breakdown of US Infrastructure Investments (Contribution to Real GDP Growth Rate)



Note: The data for the 1st quarter of 2010 is based on an immediate report.
Source: United States Department of Commerce

1-2-1-13 Trends in US Investments in Construction and Commercial Real Estate Price Index

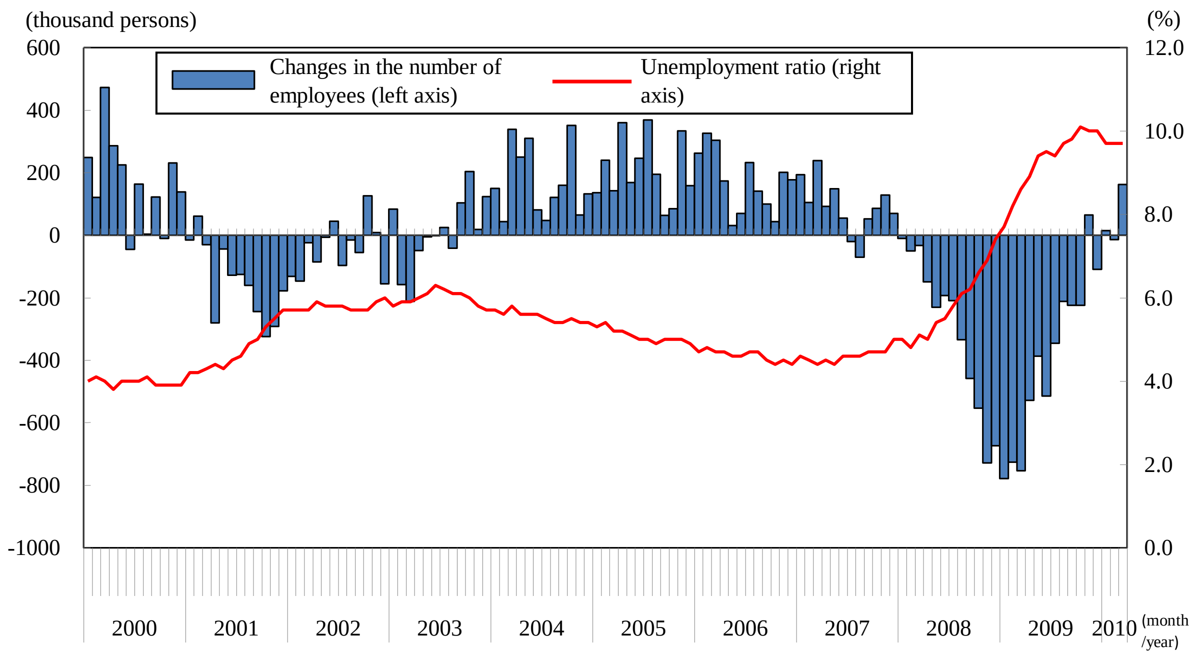


Sources: United States Department of Commerce, Massachusetts Institute of Technology Center for Real Estate (MIT CRE)

(E) Employment

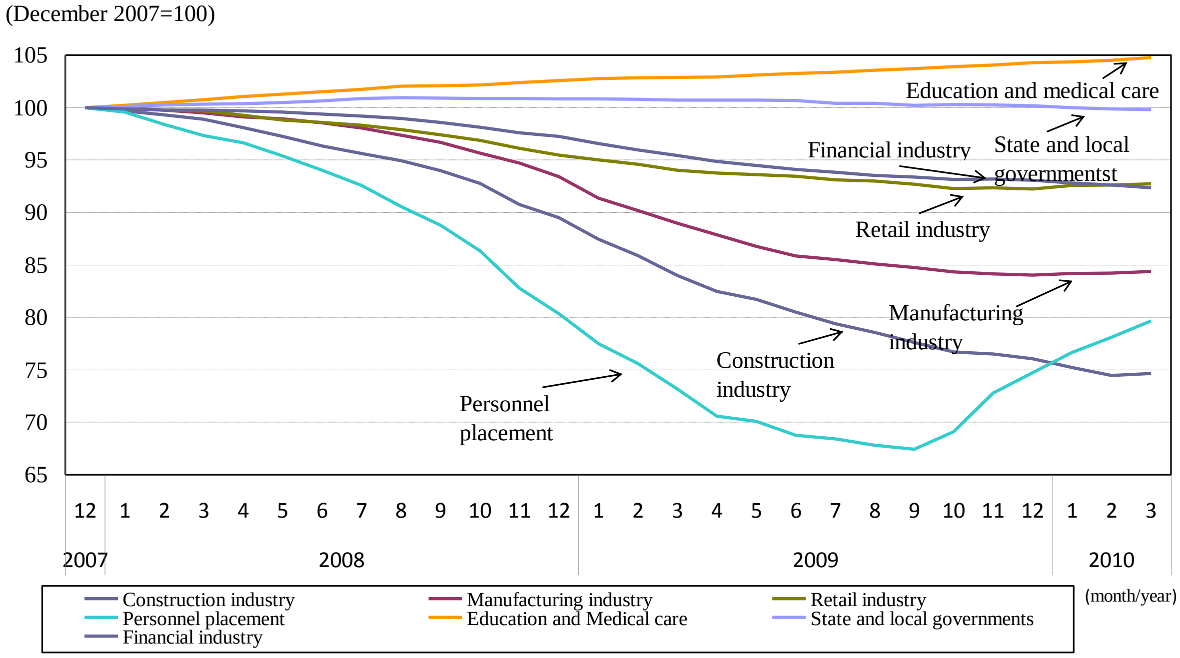
Although the employment situation has picked up since the worst period, severe conditions continue. With large-scale employment regulations, the decrease in U.S. non-agricultural employment began to slow. However, the unemployment rate (excluding military personnel) remains high (see Figure 1-2-1-14).

1-2-1-14 Trends in US Changes in Number of Non-Agricultural Workers and Unemployment Rate



Notes: Seasonally adjusted. Year-on-year change (Changes in the number of employees)
The data for February and March of 2010 are preliminary.
Source: United States Department of Commerce

1-2-1-15 Trends in Number of Employed in Major US Industries



Notes: Data for December 12 after the US went into recession was used as abase, 100 to convert other data into index. The data for February and March of 2010 are preliminary.

Source: United States Department of Labor

A breakdown of the number of employees by sector shows that the figures for temporary dispatch workers, regarded as a leading indicator, took a favorable turn in October 2009. Employment in the manufacturing, retail and construction industries are following this trend and their respective decreases are slowing (see Figure 1-2-1-15). However, the financial industry, which has seen a series of bankruptcies among regional banks[4], and State and local governments,[5] which are also in financial difficulties, are continuing to reduce staff numbers. The education and health service sectors are showing an increase.

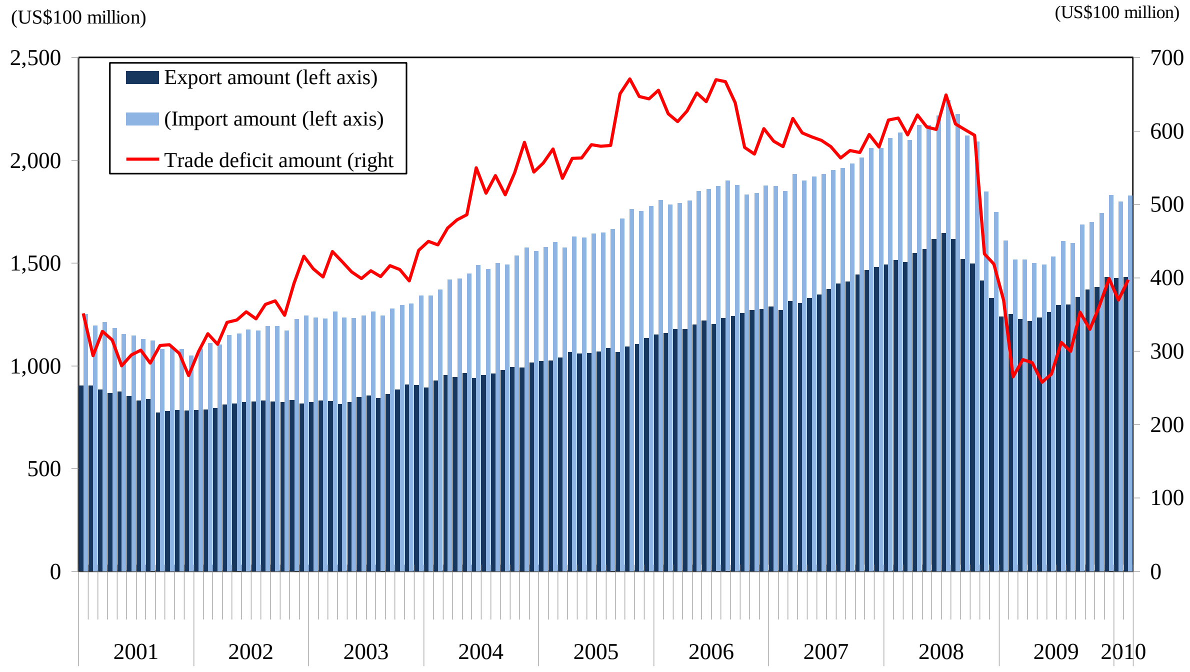
(F) Trade

Set against a backdrop of moderate economic recovery, the trade deficit is again in an expansion phase (see Figure 1-2-1-16). A year-on-year comparison of the accumulated trade balance (excluding the service industry and before seasonal adjustment) by country and region for the period from January to February 2010 shows overall improvement of the trade balance with Asian countries, with an increasingly favorable balance with NIEs (Hong Kong, Korea, Singapore and Taiwan) and a stable trade deficit with China (see Figure 1-2-1-17).

4 Please refer to 1.(2) "Risk factor, "Delay of the recovery of the financial system functions" of Chapter 1 Section 1.

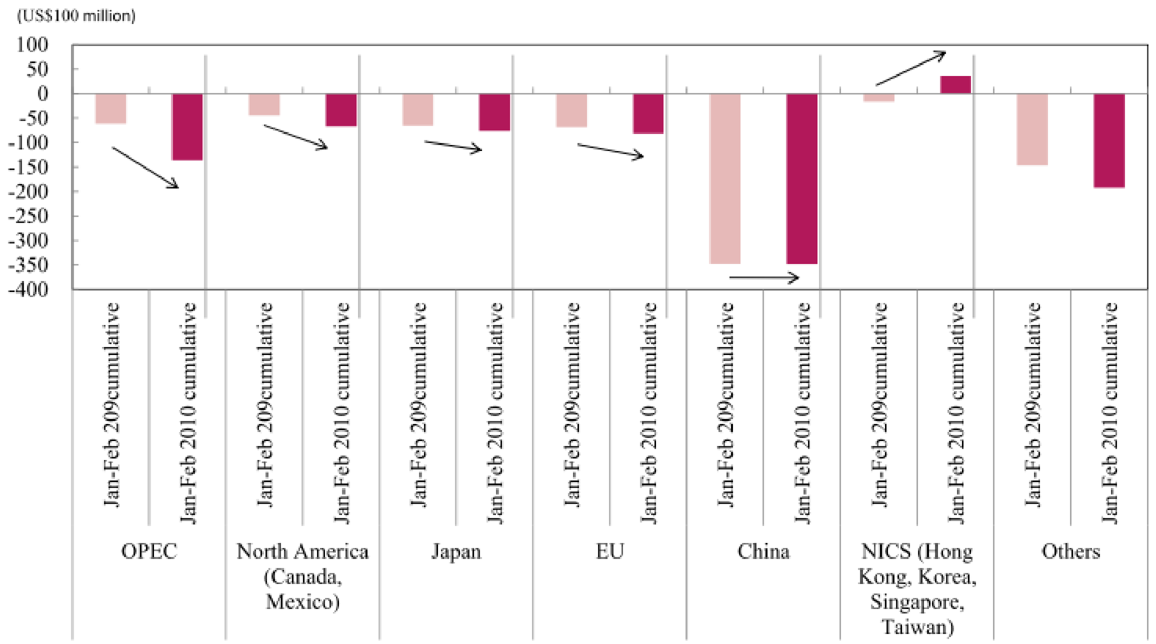
5 The share of State and Local government staff to the total employee was 15% as of 2009.

1-2-1-16 Trends in US Balance of Trade



Note: Balance of international payments, seasonally adjusted
Source: United States Department of Commerce

1-2-1-17 Trends in US Balance of Trade by Country/Region

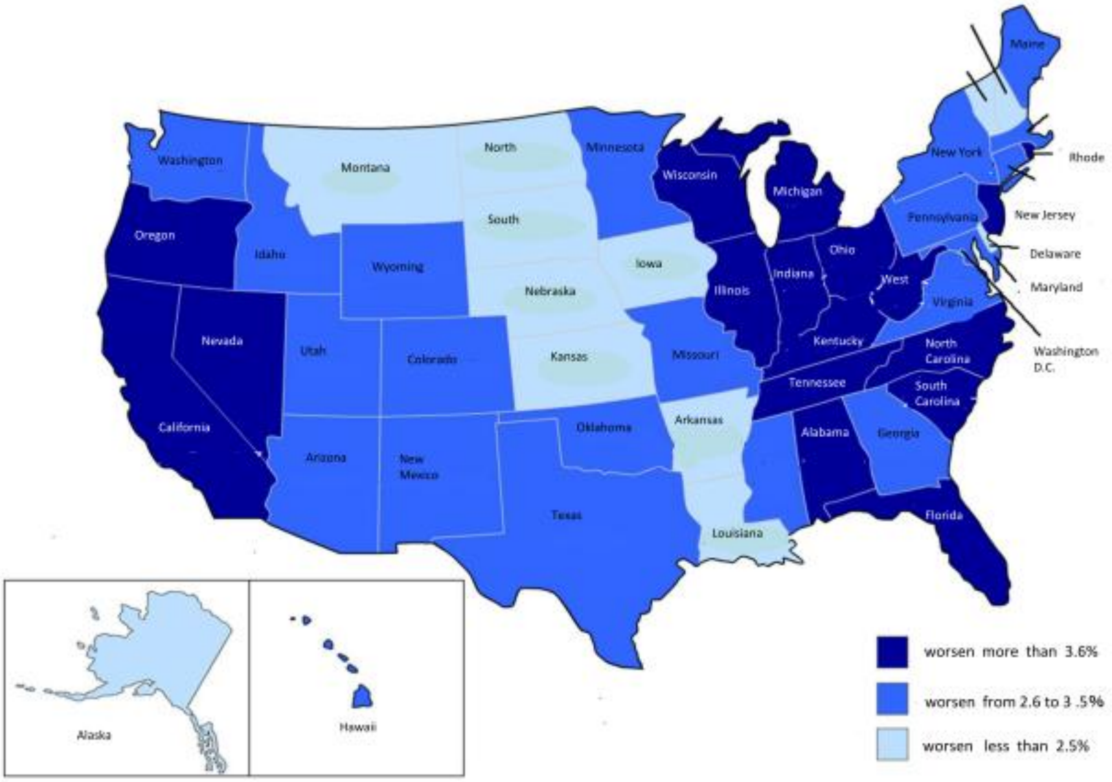


Note: Customs clearance basis, before seasonal adjustment.
Source: United States Department of Commerce

(G) Regional economy

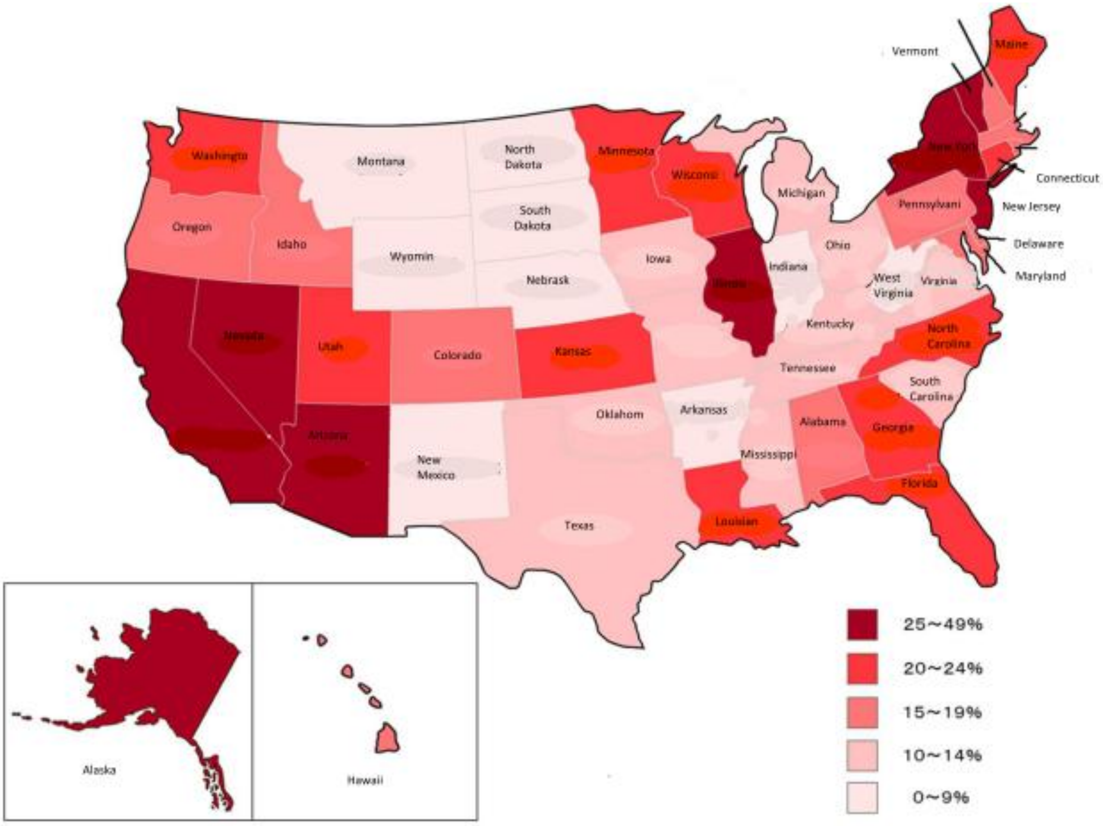
The U.S. economy is gradually recovering. However, the situation varies widely state-by-state. When the U.S. unemployment rate worsened from 5.8% in 2008 to 9.3% in 2009, significant drops in employment rates were observed in the West and East coast areas, substantially impacted by the bursting of the housing market bubble, and also in the Great Lakes area, which was affected by bankruptcies among automobile manufacturers (see Figure 1-2-1-18).

1-2-1-18 Extent of Changes in US Unemployment Rate (2008-2009)



Source: United States Departure of Commerce

1-2-1-19 Revenue-expenditure gap in the U.S (forecast for fiscal year of 2010)



Note: revenue-expenditure gap(%) = (revenue-expenditure) / general expenditure *100

Source: Congressional Budget Exchange (CBO)(2010) “Police for Increasing Economic Growth and Employment in 2010 and 2011”

The financial conditions for state governments remain severe. According to an estimate by the Congressional Budget Office (CBO) of the United States, revenue for the fiscal year 2010 shrank to about half of expenditure in states such as California and Illinois[6] (see Figure 1-2-1-19). Despite $75.5 billion in financial support that the Federal Government provided to them before the end of March 2010[7], state and local governments are experiencing continued fiscal deficits[8].

(H) Prices

Prices remain stable and low. The increase in the Consumer Price Core Index (which excludes energy and food product prices as these fluctuate considerably) remains 2% down compared to the previous year, and inflation is being contained[9] (see Figure 1-2-1-20).

1-2-1-20 Trends in US Consumer Price Index

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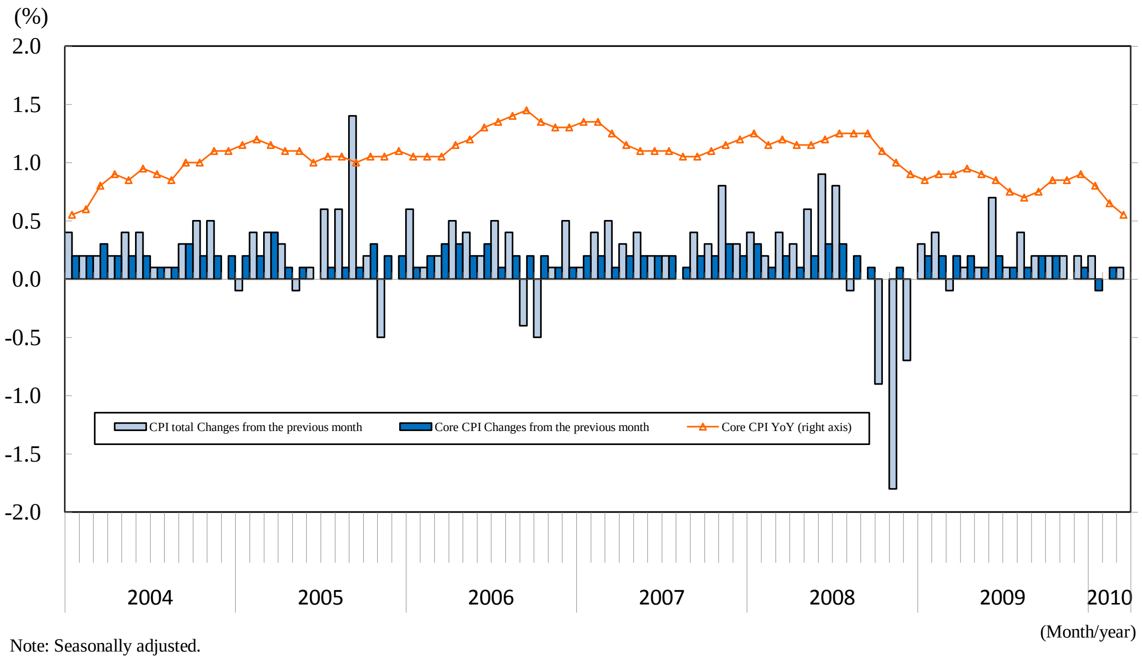
6 In the U.S. many States and Local governments impose themselves the balanced fiscal management policy. Therefore, if a fiscal deficit occurs, in principle, it is necessary to reduce revenue by adjusting employees or increase taxes in the fiscal year.

7 “The Economic Impact of the American Recovery and Reinvestment Act of 2009, Third Quarterly Report” by Council of Economic Advisers (CEA) (2010)

8 According to the U.S. Department of Commerce, the total treasury budget for State and Local government has been recording the budget deficit since the fourth quarter of 2007.

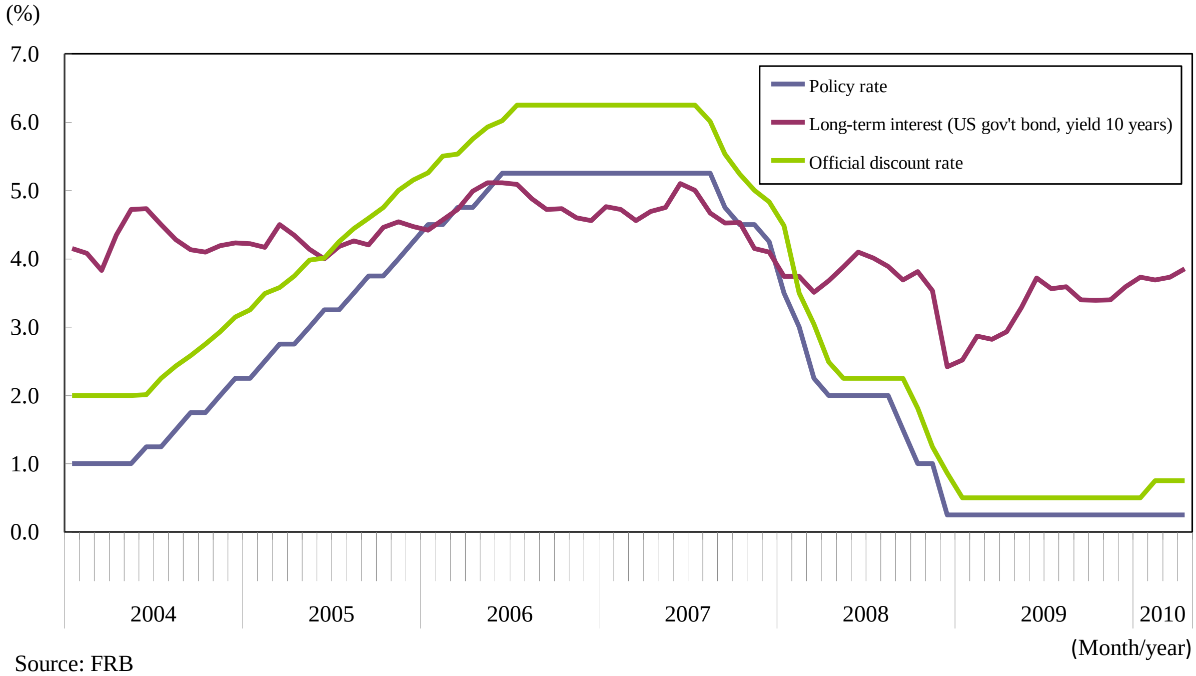
9 Consumer Price Core index of January 2010 has dropped from the previous month on seasonally-adjusted base for the first time after 27 years since December 1982 recording minus 0.1%.



Note: Seasonally adjusted.

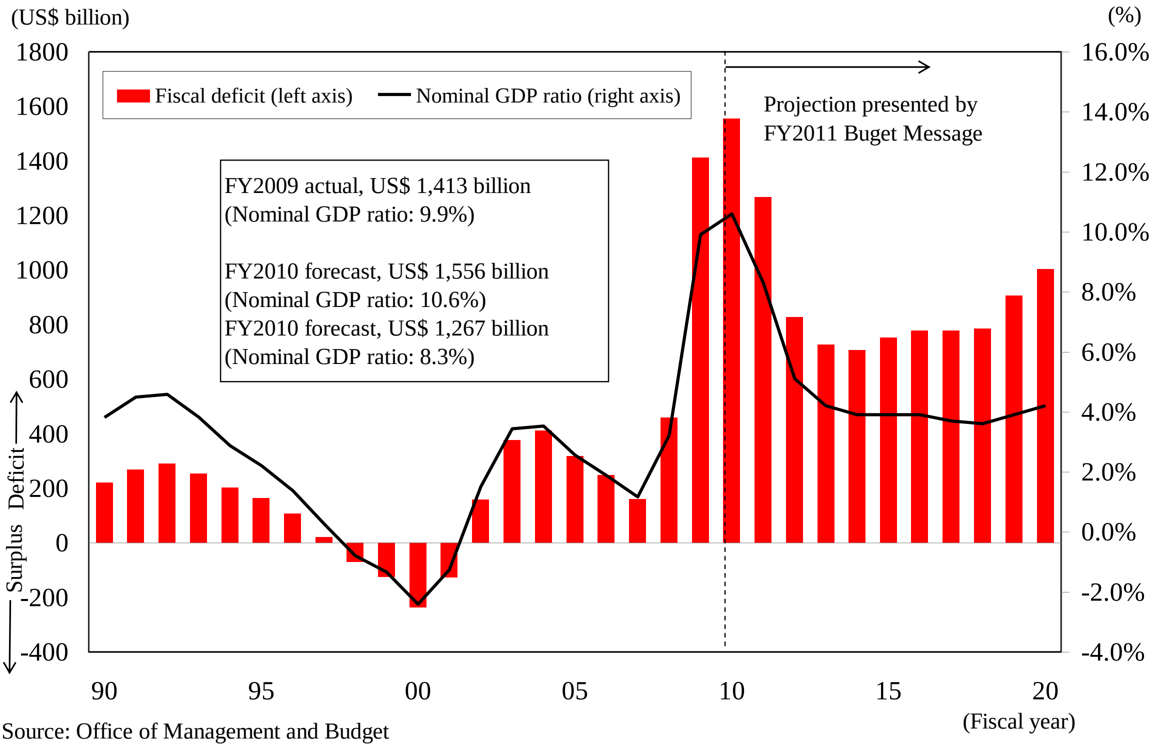
Source: United States Department of Labor

1-2-1-21 Trends in US Policy Rate, Long-term Interest (US Govt 10 yr Bond), and Official Discount Rate



Source: FRB

1-2-1-22 Trends in US Fiscal Deficit



Source: Office of Management and Budget

(I) Interest rates

On February 18, 2010, the FRB increased the official discount rate from 0.5% to 0.75%, confirming continued improvement in the financial market (see Figure 1-2-1-21). The policy interest rate (Federal funds target rate) remains low, having stayed in the range from 0% to 0.25% since December 2008. The long-term interest rate (U.S. treasury 10-year bond yield) has been hovering around 3%.

(J) Public finance

On February 1, 2010, President Obama submitted his Budget Message for the fiscal year 2011 (for the period from October 2010 to September 2011). Partially due to an aggressive expenditure plan to restore the employment market, the fiscal deficit of the financial year 2011 will be $1,267 billion, which is 8.3% of nominal GDP, and will exceed $1 trillion for the third consecutive year (see Figure 1-2-1-22).

(2) Status of the American Recovery and Reinvestment Act (ARRA) and Troubled Asset Relief Program (TARP)

(A) Status and economic effects of the "American Recovery and Reinvestment Act" (ARRA)

Based on the American Recovery and Reinvestment Act of 2009 (ARRA), enacted on February 17, 2009, the United States has launched its largest ever economic stimulus program, spending a total of $787.2 billion, equivalent to 5.5% of U.S. nominal GDP[10]. The allocation of the total $787.2 billion from this stimulus package has been set at $184.9 billion for the fiscal year 2009, $399.4 billion for the fiscal year 2010, and $209.9 billion for the period covering the fiscal years 2011 to 2019[11] (see Figure 1-2-1-23). The Council of Economic Advisors (CEA) estimated the total revenue increase and tax cuts resulting from ARRA would reach $373.4 billion by March 31, 2010 (of which the tax cut portion would be $162.5 billion)[12]. With regard to the economic effects, according to CEA analysts the ARRA had contributed 0.7%, 1.4-1.7%, 2.1-2.5% and 2.1-2.5% of the GDP growth increase during the second, third and fourth quarters of 2009 and the first quarter of 2010, respectively. In addition, the CEA claims that ARRA further supported economic expansion by creating or maintaining between 2.23 and 2.825 million jobs[13].

(B) Status of the Troubled Asset Relief Program (TARP)

The Troubled Asset Relief Program (TARP) is a financial stabilization program that was created under the previous administration (i.e. the Bush administration), and is based on the Emergency Economic Stabilization Act of 2008 (EESA), which came into force on October 3, 2008. After the Obama administration took office, a more comprehensive framework of economic measures based on the Financial Stability Plan announced on February 2009 was established, with TARP as its core. This framework consists of a total of 12 programs to support areas including the financial system, the automobile industry, the securitization of assets, and the housing market. It authorized the U.S. Treasury Department to inject up to $700 billion of public funds. The allocations for the financial system, the automobile industry, the securitization of assets, and the housing market are $319.7 billion, $84.8 billion, $90.0 billion and $50.0 billion, respectively. As of February 2010, a total of $378.1

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10 The U.S's nominal GDP in 2009 was some $14 trillion.

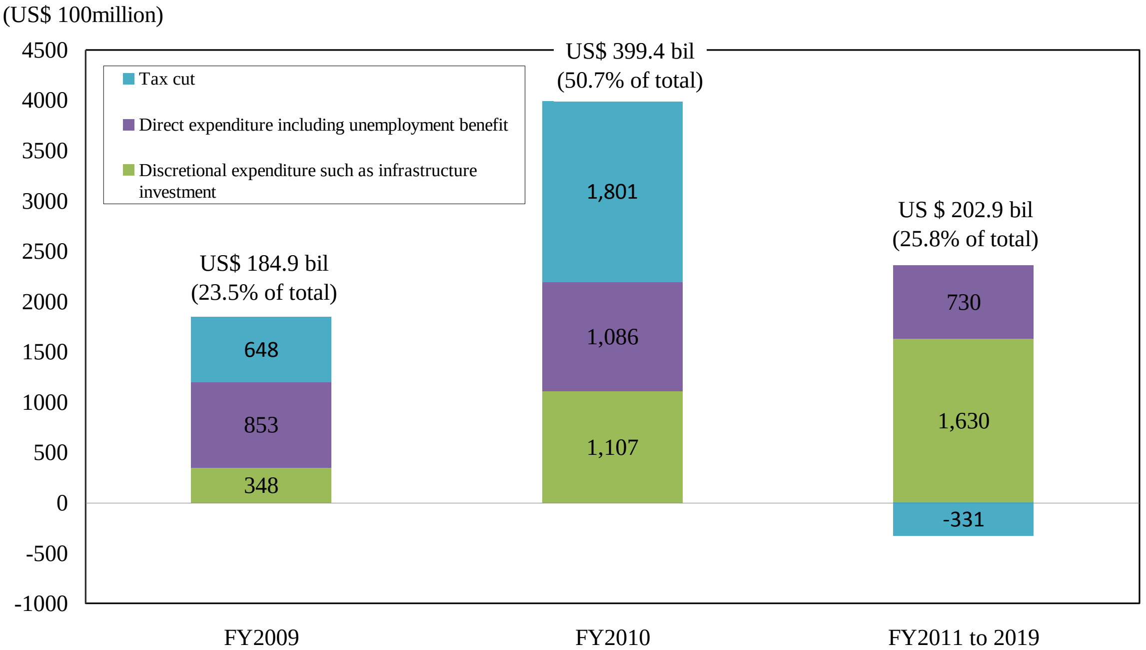
11 "Estimated Macroeconomic Impacts of the American Recovery and Reinvestment Act of 2009" by Congressional Budget Office (CBO) (2009) In addition, "The Budget and Economic Outlook: Fiscal Years 2010 to 2020" issued by CBO in 2010 upwardly revised the cost estimate for the economic stimulus measures from $782.0 billion to maximum $862.0 billion

12 "The Economic Impact of the American Recovery and Reinvestment Act of 2009, Third Quarterly Report" by CEA (2010)

13 "The Economic Impact of the American Recovery and Reinvestment Act of 2009, Third Quarterly Report" by CEA (2010)

billion has been spent and $173.6 billion of this spending has been reimbursed[14].

1-2-1-23 Expected US Economic Policies



Note: Assumption of (Congressional Budget Office) CBO execution

Source: CBO

With tension in the financial market easing, TARP's mission is also coming to an end. While the public fund injection program of the Treasury Department has been extended to October 3, 2010, some programs, including the Capital Purchase Program (CPP), the Capital Assistance Program (CAP), the Targeted Investment Program (TIP), the Asset Guarantee Program (AGP) and the Auto Supplier Support Program (ASSP), have already ended.

(3) Issues for the U.S. economy: job market recovery

As mentioned earlier, the U.S. economy is enjoying a period of moderate recovery, supported by factors such as the large-scale economic stimulus programs implemented by the government, the monetary easing measures taken by the FRB, and the reviving world economy. However, following the financial crisis substantial employment adjustments were conducted in the U.S., income growth remains low, and consumption has failed to pick up. While income remains stagnant, the delinquency rate for mortgage loans has been increasing and the increase in supply in the housing market as a result of foreclosures is pushing house prices down. The corporate sector has improved its level of production; however, there is reluctance to create new jobs due to the widening gap between domestic supply and demand. The rate of unemployment remains high, and local governments do not have sufficient funds to support the large numbers of unemployed. As a result, the Federal Government has decided to provide financial support to local governments, but this is pushing up government expenditure.

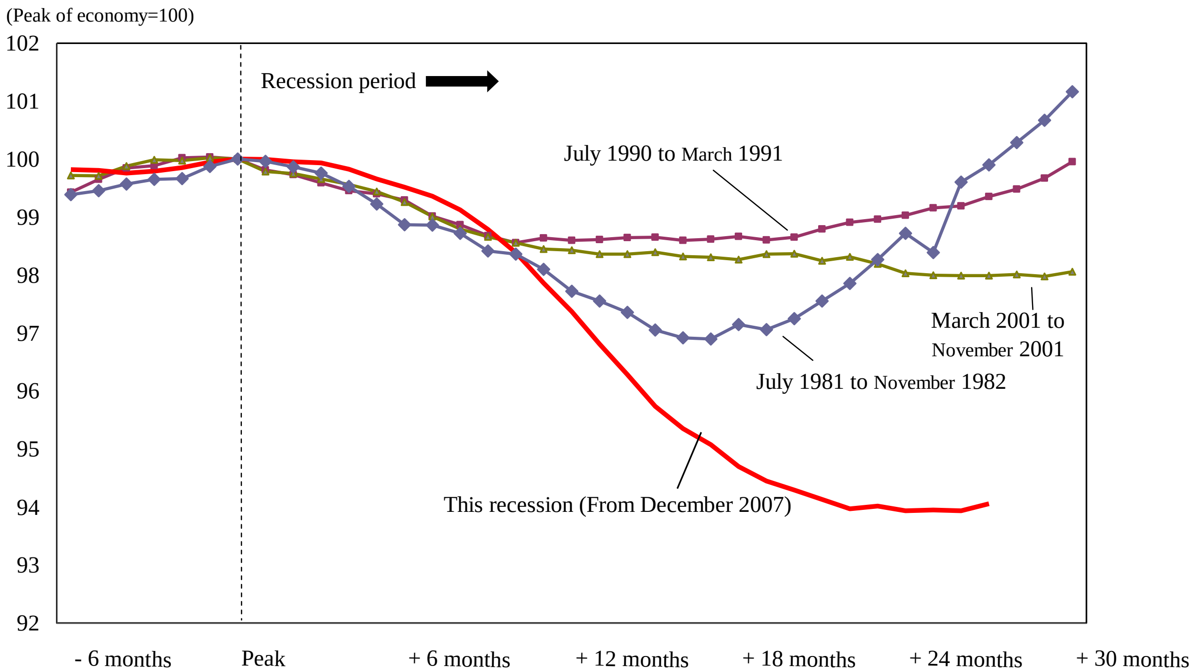
"Recovery in the job market" is the key to sustainable economic growth in the U.S. We will focus on the U.S. job market and give further analysis below.

[14] "Troubled Assets Relief Program (TARP), Monthly 105 (a) Report" by the U.S. Department of the Treasury (2010)

(A) A labor market facing its worst crisis since WWII

As of April 2010, the fall in the number employed in non-agricultural work during the recession[15] has exceeded 8 million. This represents a 6% decrease from the peak, and is the worst drop in employment since World War II (see Figure 1-2-1-24). Although the current unemployment rate is lower than the worst recorded post-war rate of 10.8% (for November and December 1982), the fall from the peak has been the largest yet seen in the post-war period (see Figure 1-2-1-25).

1-2-1-24 Trends in Number of Employed Compared to Previous Recession Recoveries in US



Note: Previous economic peak announced by the National Bureau of Economic Research (NBER) was considered as a base, 100 for indexation.
The data for February and March 2010 are preliminary.
Source: United States Department of Commerce

Recent economic data shows a sharp increase in the long-term unemployed. Over 40% of people have been unemployed for longer than 27 weeks[16], the highest ratio in history (see Figure 1-2-1-26). Comparison of temporary and permanent dismissals of dispatch staff (where permanent dismissal means with no intention to rehire later), reveals that the proportion of permanent job closures is overwhelmingly high. Therefore, it may be assumed that once someone loses his or her job, it will be very difficult to find another one[17] (see Figure 1-2-1-27). In addition, the ratio of part-time to full-time employees is at a record high. This is due to a surge in the number of employees who are forced to make do with a part-time job despite wanting to find a full-time position (see Figure

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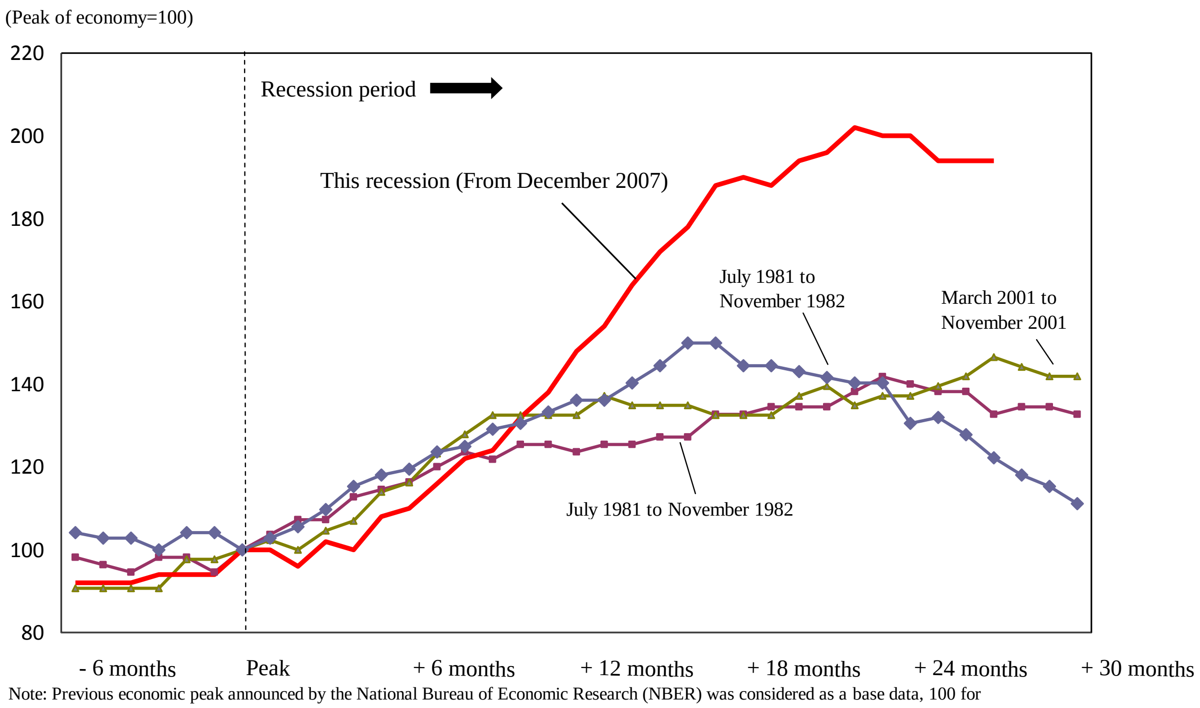
[15] The National Bureau of Economic Research made an announcement on December 1, 2008 that the U.S. economy has peaked in December 2007 and been in the recession phase since then. The period of this recession made a record of the longest recession after the World War II exceeding the previous record of 17 months from July 1981 to December 1982.

[16] The U.S. Department of Labor releases the employment data by classifying the period into the following four: (i) less than 5 weeks, (ii) from 5 weeks to 14 weeks, (iii) from 15 weeks to 26 weeks, and (iv) longer than 27 weeks.

[17] "Jobless Recovery Redux?" by Mary Daly, Bart Hobijn and Joyce Kwok (2009) analyzed the future employment trend by using the following two as reference: (i) the economic recovery phase of 1982 to 1983 that observed the increase in the outflow from unemployment, which means the new employment increased (ii) the economic recovery scenario which demonstrated "economic recovery without employment" not increasing the outflow from unemployment from 1991 to 1992. This report pointed out that the increase in non-voluntary part-time workers and the permanent closure of job opening. It also forecasted that the unemployment rate would peak at near 11% in the middle of 2010 and maintain the level over 9% till the end of 2011.

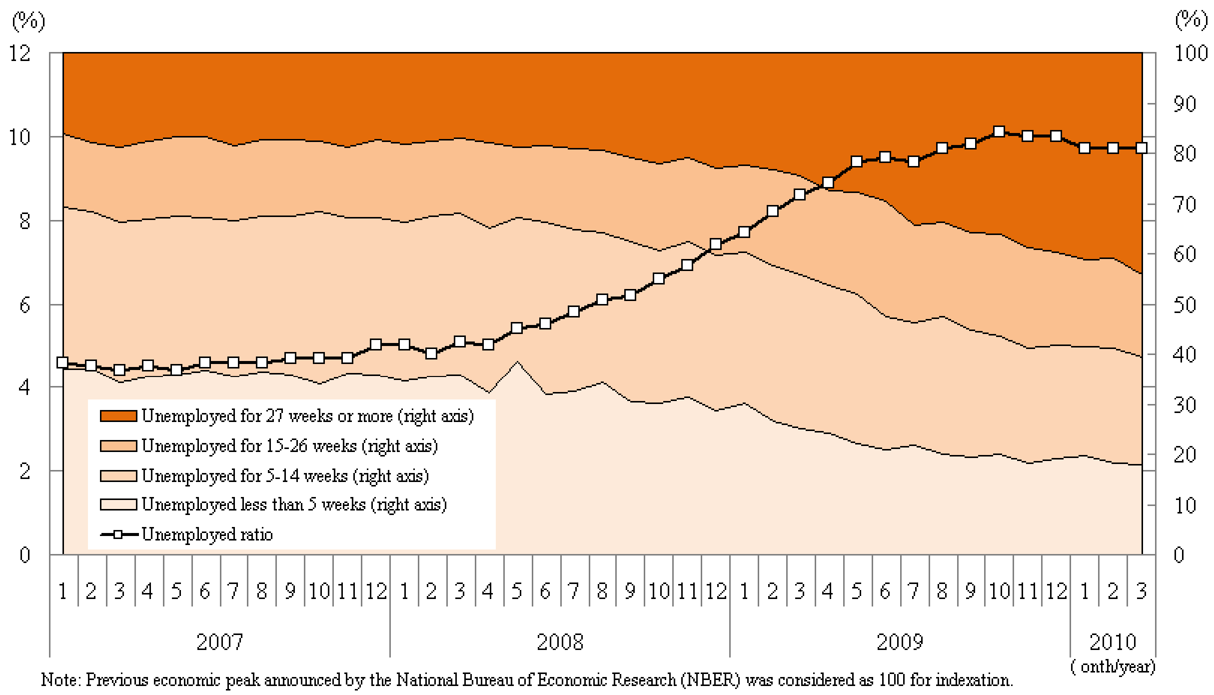
1-2-1-28).

1-2-1-25 Trends in Unemployment Rate Compared to Previous Recession Recoveries in US



Note: Previous economic peak announced by the National Bureau of Economic Research (NBER) was considered as a base data, 100 for indexation. The data for February and March 2010 are preliminary.
Source: United States Department of Commerce

1-2-1-26 Trends in US Unemployed Workers Share and Unemployment Rates by Period

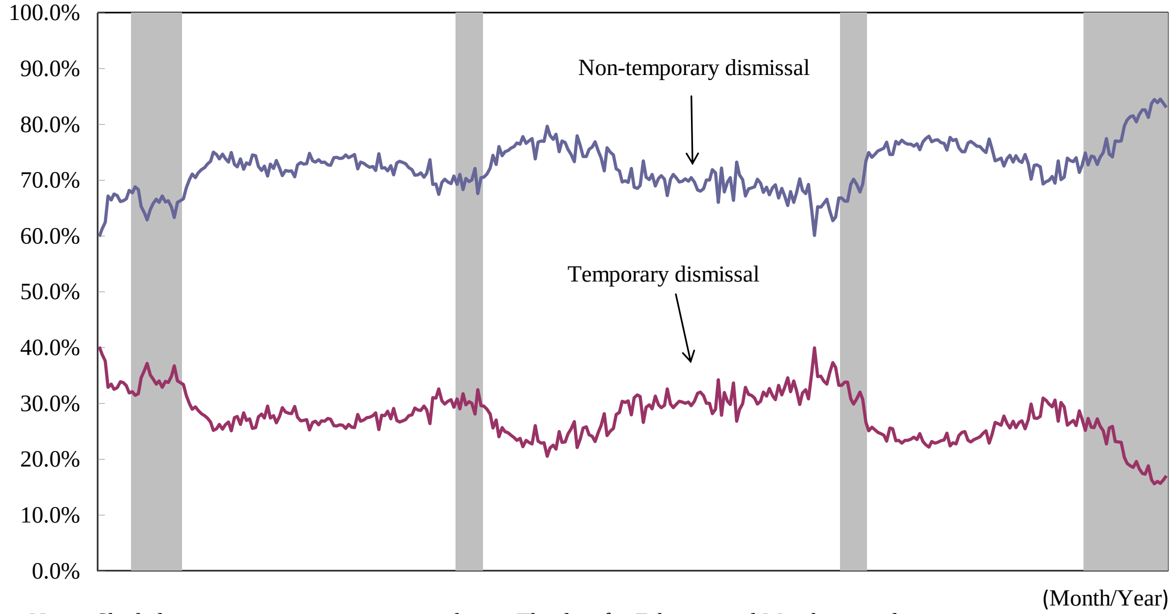


Note: Previous economic peak announced by the National Bureau of Economic Research (NBER) was considered as 100 for indexation.
The data for February and March 2010 are preliminary.
Source: United States Department of Commerce

(B) A possible change in Okun's law, and its background

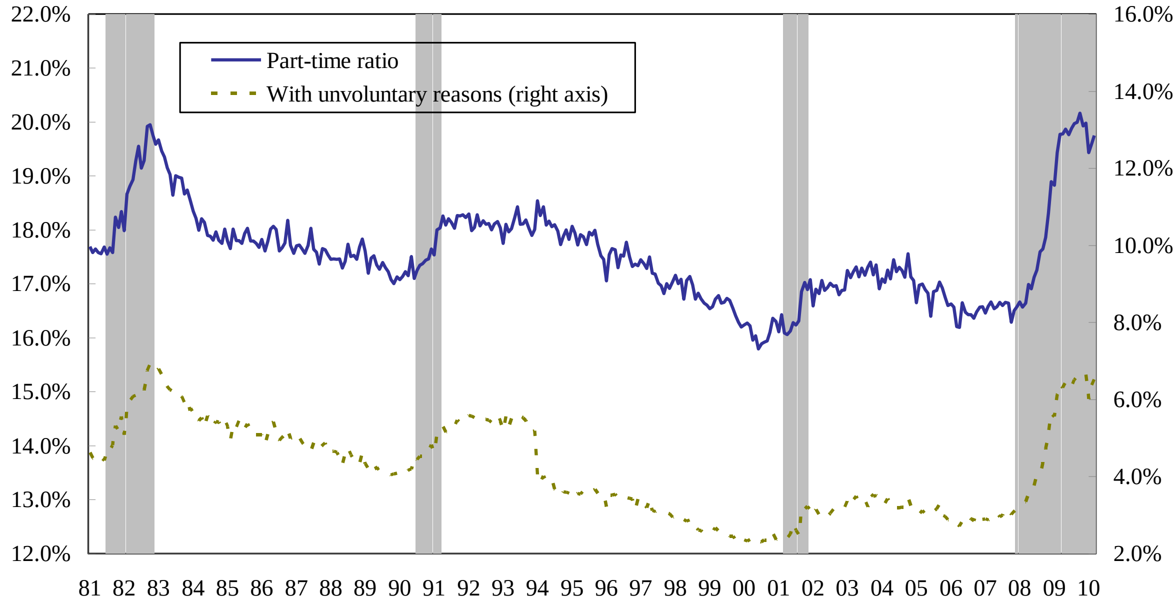
While U.S. real GDP growth registered a 2.2% increase in the third quarter of 2009 and was up 5.6% in the fourth quarter of the same year, the unemployment rate remains high. It is known that there is a long-term stable inverse correlation between fluctuation in the real GDP growth rate and the unemployment rate (Okun's law[18]). During the current recession, the unemployment rate has significantly worsened and this has spurred the argument that the relationship may be changing[19]. The analysis of the actual data after 2009 shows that this time the correlation is deviating significantly upwards from the theoretical value (trend-line), and indicates that an unprecedented "recovery without employment" is in progress (see Figure 1-2-1-29).

1-2-1-27 Trends in Share of Temporary Dismissals and Non-Temporary Dismissals in US



Notes: Shaded areas are economic recession phases. The data for February and March are preliminary.
Source: United States Department of Labor

1-2-1-28 Trends in US Ratio of Part Time Workers



Notes: Shaded areas are economic recession phases. The data for February and March are preliminary.
Source: United States Department of Labor

[18] "Potential GNP: Its Measurement and Significance" by Arthur M. Okun (1962) and "Unemployment and Potential Output in the 1980s" by Robert J. Gordon and Peter K. Clark (1984).

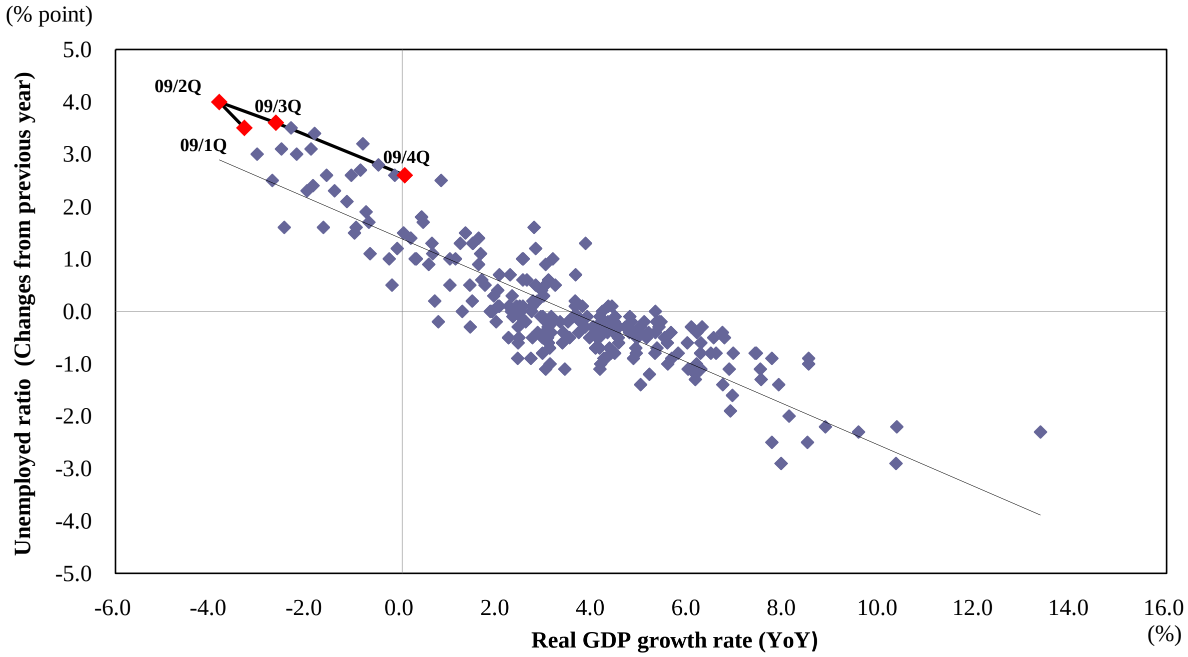
[19] This includes, for example, "The Outlook for the Economy and Monetary Policy" by Janet L. Yellen (2010) and "Okun's Law and the Unemployment Surprise of 2009" by Mary Daly and Bart Hobijin (2010).

One of the factors behind this change is the drastic improvement of labor productivity. Indeed, even after the real GDP growth rate rebounded in the third quarter of 2009[20], American companies have continued to achieve a sizable improvement in labor productivity by reducing per-unit labor costs, thereby securing profits (see Figure 1-2-1-30). There is also improvement in companies' cash flows. Under these circumstances, once corporate investment activity recovers, there is a possibility that the balance of supply and demand in the labor market will gradually improve (see Figure 1-2-1-31).

(C) Recovery of employment

Following the large-scale employment regulations, the contraction in the rate of employment is coming to a halt. However, as discussed below, only a slow recovery, rather than a sudden expansion, in employment is expected.

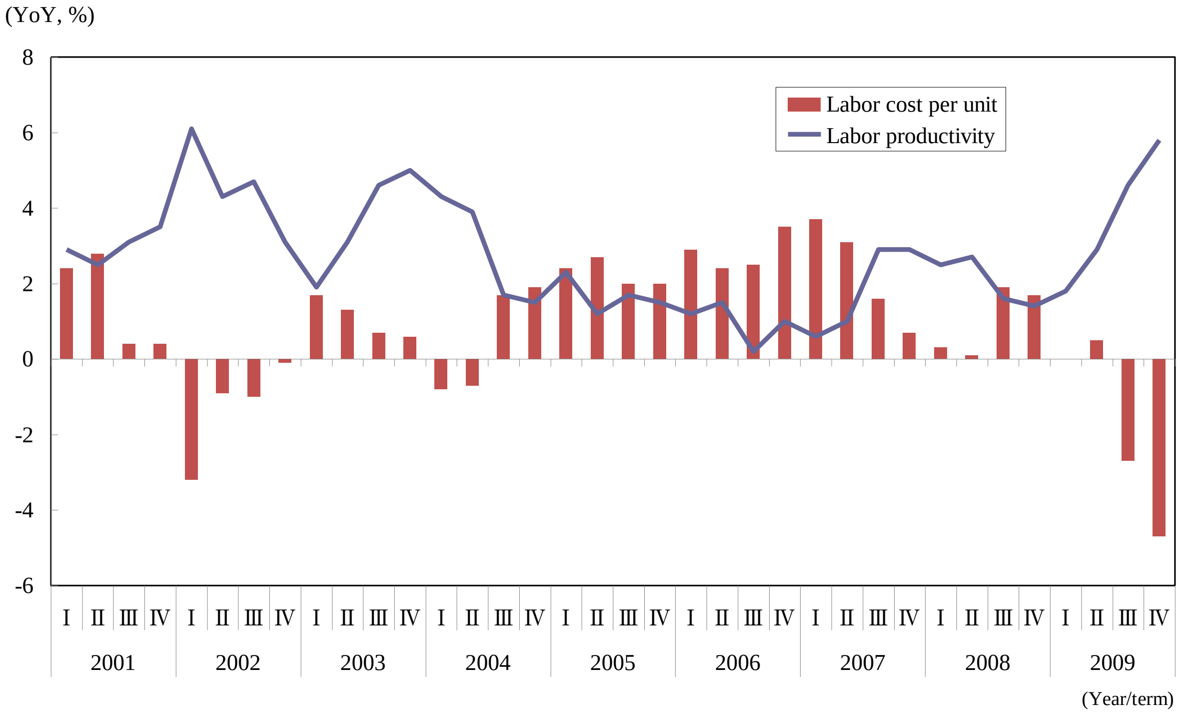
1-2-1-29 US GDP Growth Rate and Unemployment Rate (Q1 1949-Q4 2009)



Source: United States Department of Commerce, United States Department of Labor

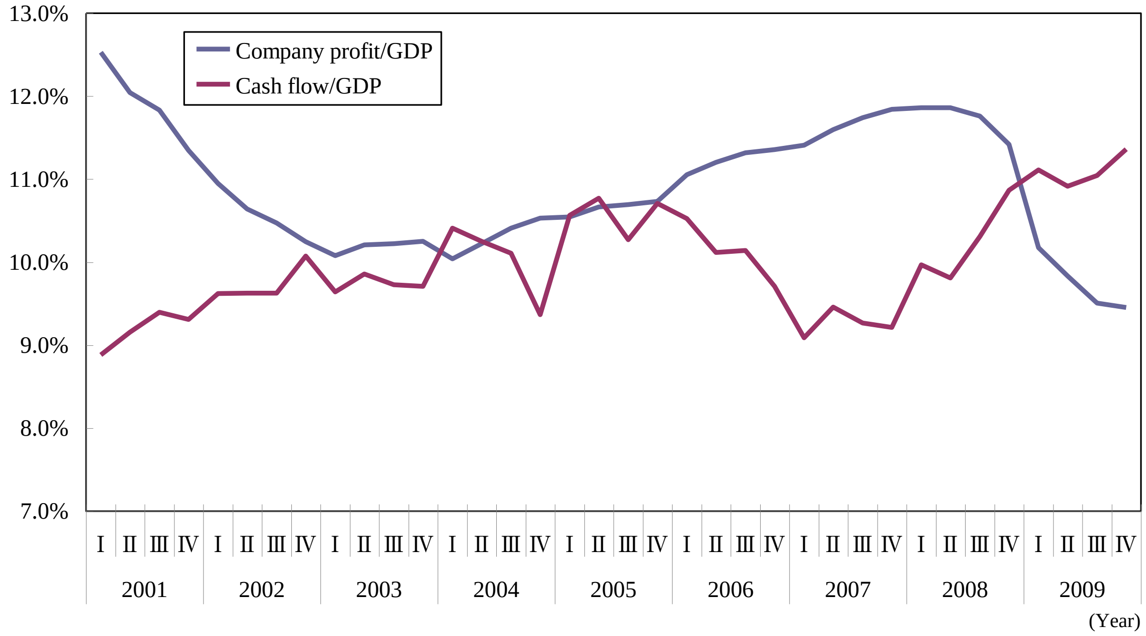
[20] According to the U.S. Department of Commerce, after turning into growth recording an year-on-year 5.3% increase in the first quarter of 2009, the corporate profits before taxes increased from the same period of the previous year in the second , third and fourth quarter by 3.7%, 10.8% and 8.0%, respectively.

1-2-1-30 Trends in US Labor Productivity and Per Unit Labor Costs



Source: United States Department of Commerce

1-2-1-31 US Corporate Profits (Pre-tax) and Cash Flow

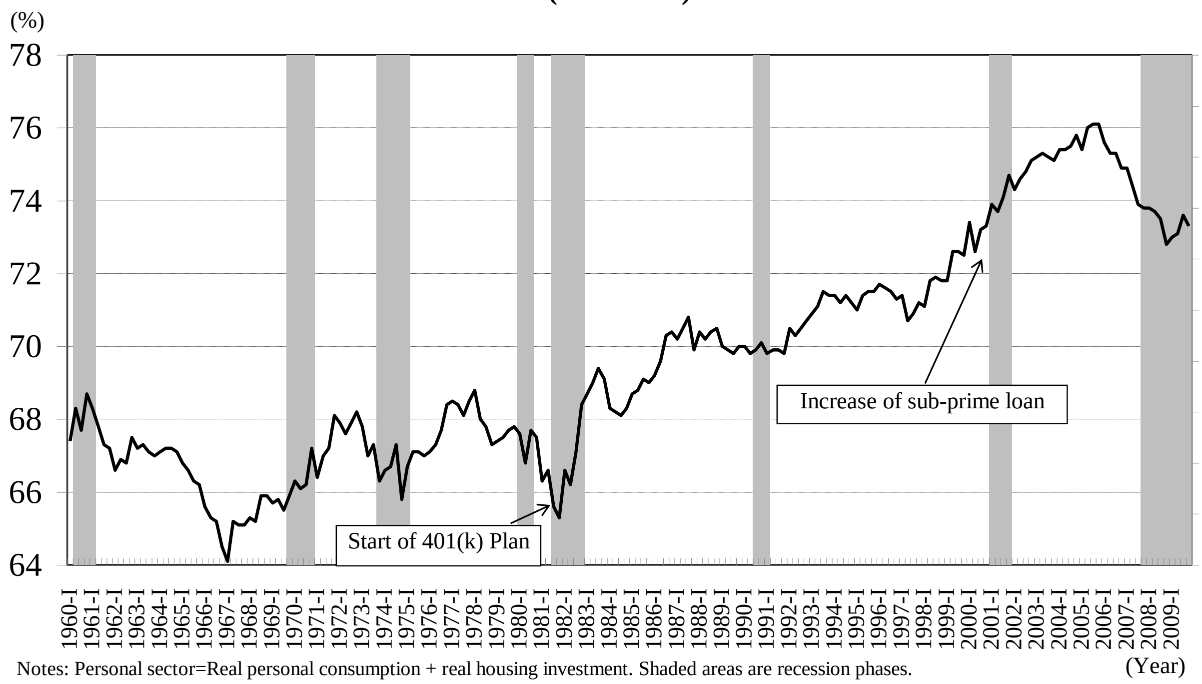


Source: United States Department of Commerce

(a) A household sector with excessive debt

The U.S. household sector's balance sheet shows the ratio of debts to disposable income declined from its peak of 1:1.4 in the first quarter of 2008 to 1.3 in the fourth quarter of 2009. However, the adjustments of excessive debts have not yet been completed (see (1) The U.S. economy in a moderate recovery phase (B) Personal consumption). In the U.S., where drastic employment regulations were brought into effect as a result of the financial crisis, growth in income remains weak and it is difficult to foresee any strong expansion in consumption in a household sector so burdened with excessive debt.

1-2-1-32 Household Finances vs GDP in US (Real Base)



Notes: Personal sector=Real personal consumption + real housing investment. Shaded areas are recession phases.
Source: United States Department of Commerce

The factors behind the increase in U.S. personal consumption and the growth of the real economy include: (i) excess liquidity brought about by the monetary easing measures led by developed countries (ii) excess saving worldwide as a result of rapid growth in emerging countries, and (iii) securitization methods developed in response to the declining expected profitability of the world market, which has stimulated excess demand in the U.S. while financing its economy. The U.S. current account deficit swelled to exceed 6% of nominal GDP in 2006; however, overseas capital continued to flow into the market, far surpassing the size of the deficit[21]. At the same time, constraints on the liquidity of the household sector were significantly relaxed, and various financial products and services for households, in particular residential mortgage-backed products such as home equity loans[22] and cash-out refinancing[23], were introduced, supporting vigorous consumption. The U.S. household sector, which represents the sum of real personal consumption and real housing investment, reached 76% of GDP in 2005 (see Figure 1-2-1-32). However, the outbreak of the financial crisis triggered by the collapse of the housing bubble changed the situation completely. While the liquidity constraints in the household sector are rapidly becoming tighter[24], the sector currently lacks the factors needed to support growth.

As long as the environment for personal consumption remains severe and future trends in demand are difficult to foresee, companies may become cautious about increasing their numbers of employees.

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21 Please refer to Chapter 1. Section 1, 2.

22 It is a loan that uses the net value of owned house (which means that the net asset value that deducted housing loan balance from current evaluation value) as collateral and the net value will serve as the loan limit.

23 It is to increase a loan matching to the appreciated value of housing asset when an existing housing loan will be replaced with another one.

24 "JUTAKUSHISAN, RYUDOSEISEIYAKU, KAKEISHOHI/BEIKOKUNO KEIKEN" by Yoichi Matsubayashi (2009) stated that the liquidity constraint ratio of household sector gradually decreased after 1990 marking as low as 0.1 in the middle of the 2000s. However, it increased to about 0.8 after 2008. According to his analysis, the data revealed that almost 80% of U.S. household are all facing to the liquidity constraint.

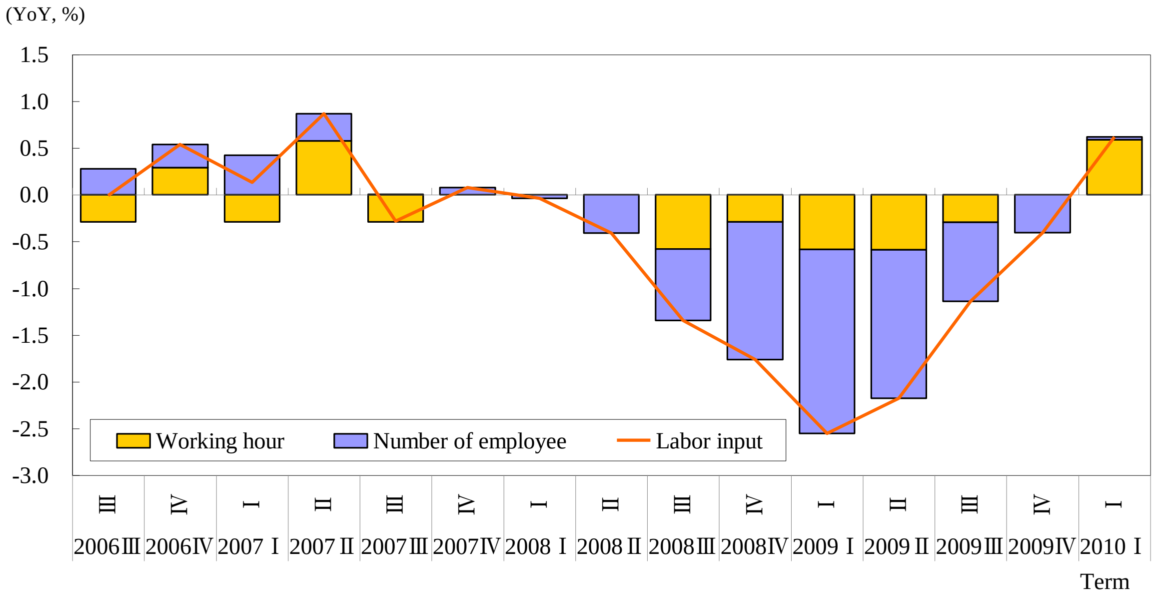
(b) Corporate sector working hour adjustments

In the current recession, American companies are promoting not only a reduction in the number of employees, but also an adjustment in working hours. Thereby, companies will be able to increase the working hours of their existing labor force if business improves. As mentioned earlier, the ratio of part-time workers to full-time is at a record high. Even if the demand for labor recovers, companies will be able to accommodate the changes by increasing the working hours of existing employees and converting their part-time workers to full-time employees. Therefore, an increase in employee numbers will not easily take place. Although input from labor rebounded in the first quarter of 2010, the contributing factor was however increased working hours (see Figure 1-2-1-33).

(c) Weak employment recovery among small and medium enterprises

Small and medium enterprises (SMEs) comprise 99.7% of the total number of American companies[25]. SMEs are therefore a highly significant presence in the U.S. economy: SME employment figures are in excess of 50% of the total number employed in the private sector, and SMEs have produced a 64% increase in overall employment over the past 15 years. Although SMEs usually serve as an engine of employment growth during an economic recovery phase, the recovery strength of SMEs has been weak this time around (see Figure 1-2-1-34). According to a study by the United States National Federation of Independent Business (NFIB), the number of SMEs which responded that they plan to reduce their workforce over the next three months exceeded the number that responded that during the same period they plan to increase employment, and this trend is ongoing. The survey confirmed that SMEs are cautious about increasing employment (see Figure 1-2-1-35).

1-2-1-33 Trends in US Labor Input



Notes:1. YoY base, 2. Labor input = Number of employees x Weekly average working hours
Source: United States Department of Labor

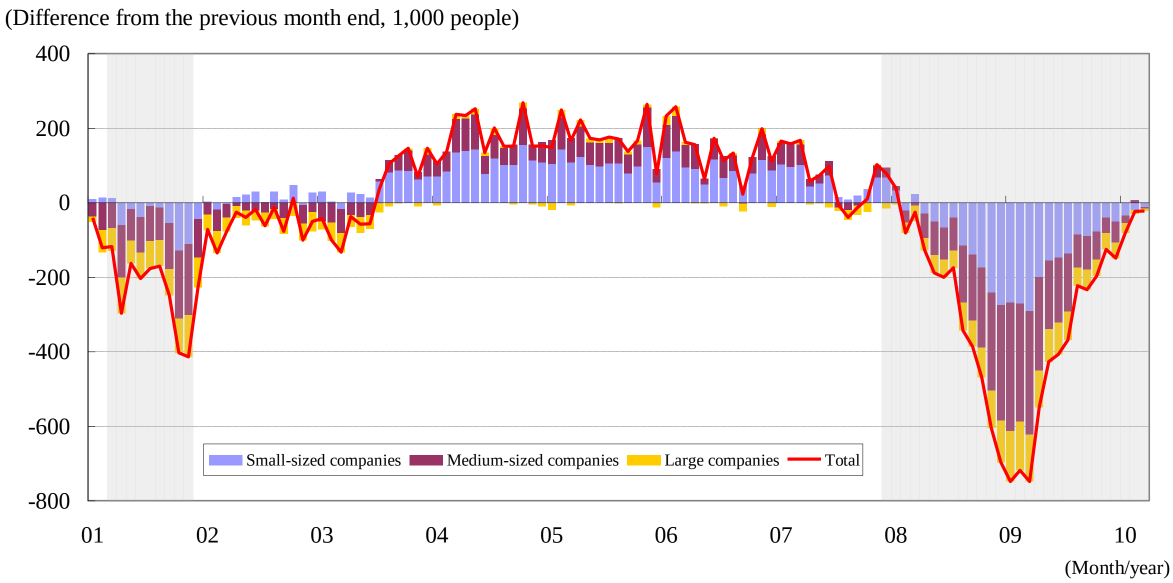
[25] The U.S. Small Business Administration (SBA) defines the companies with less than 500 people of employees as "small-to- medium sized businesses".

The Bank of Japan commented in 2010 that since SMEs are more dependent on borrowing from banks, the hardened stance among the latter toward lending has had a larger impact on the reduction of employment among SMEs compared to larger companies[26]. A partial explanation of why the reduction in employee numbers among SMEs has progressed so dramatically in the current recession may therefore be found in the banks' stricter attitude towards lending (see Figure 1-2-1-36).

(d) Prolonged employment recovery period

Looking at employment recovery trends (the pattern of variation until employment recovers its peak level) for past recessions, it can be seen that during the recession of 1974, it took 18 months for the number of employed to return a peak. Since then, the employment recovery period has been getting longer and longer, with figures of 26 months, 33 months and 49 months for the recessions of 1981, 1990 and 2001, respectively. It is therefore to be assumed that it will take a long time for employment levels to return to the peak level recorded in December 2007, especially when one considers that the drop in the of number of employees this time has been is the largest since World War II.

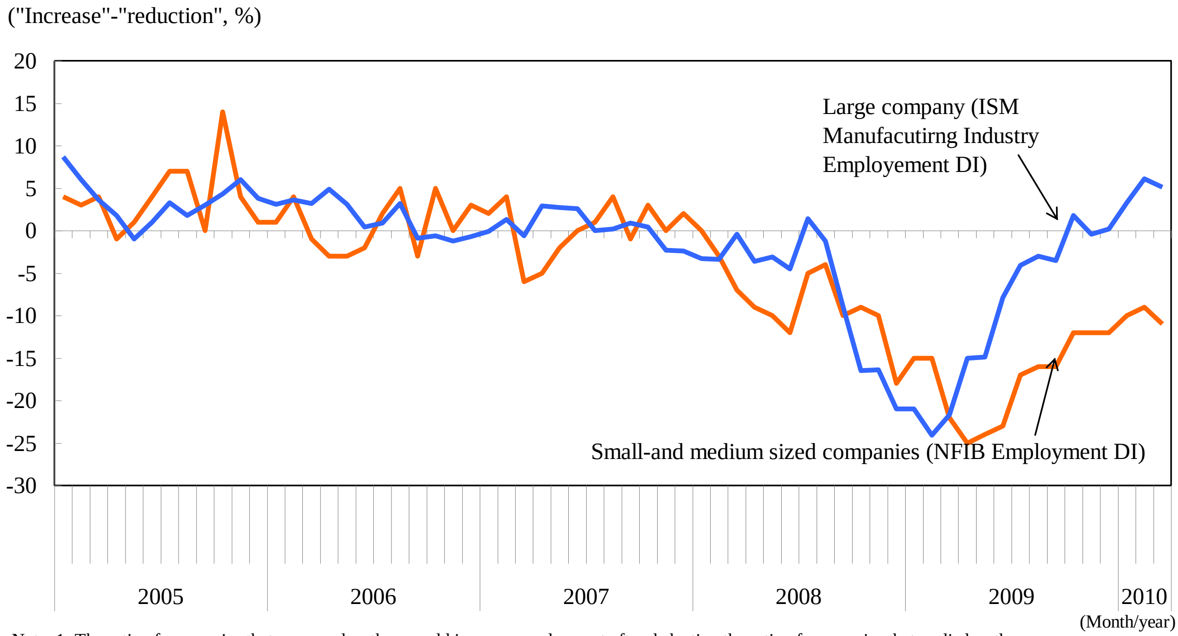
1-2-1-34 Trends in Changes in US Employees by Size of Company



Note: 1. Large companies holds 500 employees or more, Middle-sized companies 50 to less than 500, small-sized companies less than 50 employees.
2. Shaded areas are recession phases.
Source: Automatic Data Processing (ADP)

[26] "OUBEINIOKERU ROUDOSHIJOUTO GINKOUKASHIDASHISHIJOUNO CHOUSE".

1-2-1-35 Employment Plan for US SMEs and Large Companies



Note: 1. The ratio of companies that answered as they would increase employment after deducting the ratio of companies that replied as the would decrease employment.
2. ISM Manufacturing Industry Employment DI changed the standard from 50 to 0.
Source: Institute of Supply Management (ISM), National Federation of Independent Business (NFIB)

The IMF has conducted a systematic analysis of unemployment trends and recovery phases during recessions for the past 30 years, using the data from developed countries as a model (2010a)[27]. As a result, it has found that overall employment growth during recovery phases is moderate. Furthermore, since the crisis affecting developed countries this time derives from finance-related issues associated with the collapse of house prices, the IMF anticipates that employment recovery in some countries should not be expected for some time to come (see Figure 1-2-1-37).

(D) Direction of government policy under the Obama administration

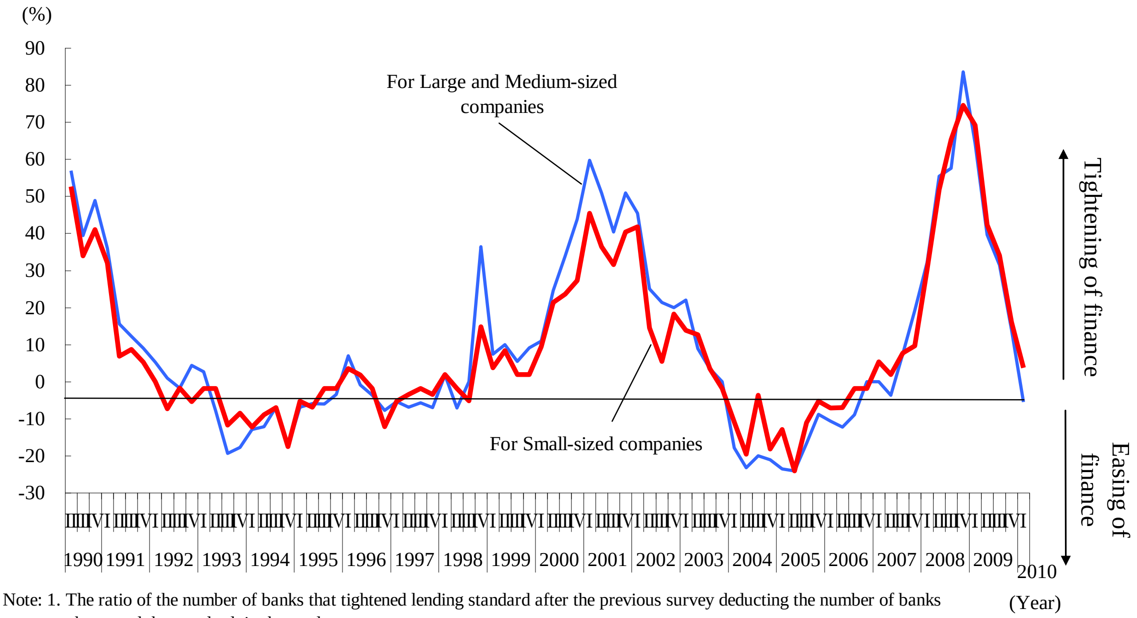
In his State of the Union Address on January 27, as well as appealing to the achievement of measures that he has taken since his inauguration, President Obama stressed that during his second year in office, the government will present clear employment measures and realize job creation by supporting SMEs and investment in the areas of environment and energy (see Figure 1-2-1-38). Moreover, he has set a goal to “double the size of export in 5 years”, a target which should generate jobs for 2 million American citizens.

The Hiring Incentives to Restore Employment (HIRE) Act was enacted on March 18 as one of these additional employment measures, and will provide tax benefits to employers hiring workers from among the unemployed. Moreover, a bill to extend the period of tax cuts, which had been about to end, got through the House of Representatives in December 2009 and was approved with amendments by the Senate in March 2010. Many members of the Lower House subsequently spoke out against the amended bill, insisting it breaches the neutrality of fiscal policy. Further amendment has therefore

[27] World Economic Outlook [IMF(2010a)] (April 2010) Sampling countries are Australia, Austria, Belgium, Canada, Denmark, Finland, France, Germany, Greek, Ireland, Italy, Japan, the Netherlands, New Zealand, Norway, Portugal, Spain, Sweden, Switzerland, the United Kingdom and the United States.

been scheduled to be carried out between the two houses. In addition, a bill to provide tax breaks on capital gains from SME stocks has also passed the Lower House and is due to be discussed in the Upper House.

1-2-1-36 Changes in Financing from US Financial Institutions (Loans to Businesses)

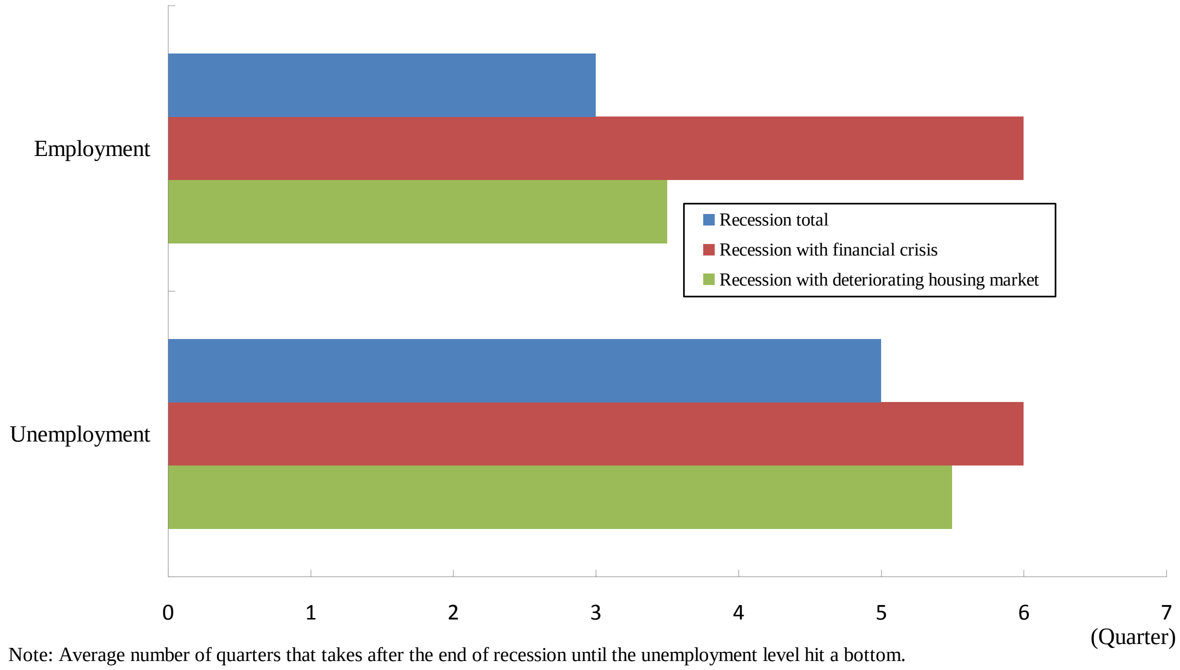


Note: 1. The ratio of the number of banks that tightened lending standard after the previous survey deducting the number of banks that eased the standard, in the total.

2. Large and medium-sized companies: Annual sales $50 million or higher, Small-sized companies: Annual sales less than $50 million

Source: FRB

1-2-1-37 Length of Time Until Employment Recovers



Note: Average number of quarters that takes after the end of recession until the unemployment level hit a bottom.

Source: World Economic Outlook, April 2010 (IMF)

Now in its second year, the Obama administration has been pushing forward with reform in the areas of health care[28], financial regulation[29], climate change and energy[30], as well as promoting employment

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[28] In February, Obama administration presented a plan for the way out regarding the health care reform that observed a large difference of opinions in terms of the introduction of public insurance and financial resources between the Upper and Lower House aiming to obtain the agreement at supra-partisan Health Care Reform Summit held on February 25. However, it didn’t gain the support from the Republican Party. In his speech of March 3, President Obama called for the adaptation of the bill within a few weeks to the U.S.

measures. The administration is striving to improve the competitiveness of the corporate sector in order to achieve an increase in exports and transform a U.S. economy which, before the financial crisis, had been characterized by debts, consumption and imports, into one that is driven by savings, production and exports.

While the Obama administration has been promoting various reform and infrastructure investment programs, as it pledged to do under the "American Recovery and Reinvestment Act" (ARRA), fully enacted in 2010, we need to watch how the U.S. will extend these efforts in order to realize long-term sustainable growth and change its economic structure.

1-2-1-38 Content of US President Obama's State of the Union Address

Economy and Financial crisis

- ☐ We have recovered most of the money we spent on the banks. To recover the rest, I have proposed a fee on the biggest banks.
- ☐ As we stabilized the financial system, we also took steps to get our economy growing again, save as many jobs as possible, and help Americans who had become unemployed. Because of the steps we took (such as extension and increase of unemployment benefits and various tax cuts), there are about two million Americans working right now who would otherwise be unemployed. And we are on track to add another one and a half million jobs to this total by the end of the year.
- ☐ Jobs must be our number one focus in 2010, and that is why I am calling for a new jobs bill.

Creation of jobs

- ☐ I'm proposing that we take $30 billion of the money Wall Street banks have repaid and use it to help community banks give small businesses the credit they need to stay afloat.
- ☐ I am also proposing a new small business tax credit – one that will go to over one million small businesses who hire new workers or raise wages. While we're at it, let's also eliminate all capital gains taxes on small business investment; and provide a tax incentive for all businesses, large and small, to invest in new plants and equipment. (It is time to) give those tax breaks to companies that create jobs in the United States of America.
- ☐ The House has passed a jobs bill that includes some of these steps. I urge the Senate to do the same.

Financial reform

- ☐ A strong, healthy financial market makes it possible for businesses to access credit and create new jobsThe House has already passed financial reform with many of these changes. And if the bill that ends up on my desk does not meet the test of real reform, I will send it back.

Health care reform

- ☐ The approach we've taken would give small businesses and uninsured Americans a chance to choose an affordable health insurance plan. It would require every insurance plan to cover preventive care.
- ☐ According to the Congressional Budget Office (CBO), our approach would bring down the deficit by as much as $1 trillion over the next two decades. Let us finish the job for the American people.

Fiscal policies

- ☐ (We) have added another $1 trillion to our national debt. Starting in 2011, we are prepared to freeze government spending for three years. Spending related to our national security, Medicare, Medicaid, and Social Security will not be affected. But all other discretionary government programs will. We've already identified $20 billion in savings for next year.
- ☐ To help working families, we will extend our middle-class tax cuts. But at a time of record deficits, we will not continue tax cuts for oil companies, investment fund managers, and those making over $250,000 a year.
- ☐ I will issue an executive order that will allow us to go forward (to solve the national debt issue.) And when the vote comes tomorrow, the Senate should restore the pay-as-you-go law (Without the revenue to offset, new expenditure will not be approved).

Innovation (Energy and climate changes)

- ☐ We need to encourage American innovation.
- ☐ (We will invest in) a new generation of safe, clean nuclear power, advanced biofuels and clean coal technologies. (We will realize) a comprehensive energy and climate bill. (The House has passed) such a bill last year. This year, I am eager to help advance the bipartisan effort in the Senate.

Trade

- ☐ We set a new goal: We will double our exports over the next five years.
- ☐ (This) increase will support two million jobs in America.
- ☐ To help meet this goal, we're launching a National Export Initiative that will help farmers and small businesses increase their exports, and reform export controls.
- ☐ We have to seek new markets aggressively, just as our competitors are. If America sits on the sidelines while other nations sign trade deals, we will lose the chance to create jobs on our shores.
- ☐ But realizing (the benefits of trade deals) also means enforcing those agreements so our trading partners play by the rules.
- ☐ And that's why we will continue to shape a Doha trade agreement that opens global markets, and why we will strengthen our trade relations in Asia and with key partners like South Korea, Panama, and Colombia.

Measures for the middle –lass

- ☐ Last year I asked Vice President Biden to chair a task force on Middle-Class Families. We're nearly doubling the child care tax credit, and making it easier to save for retirement by giving every worker access to a retirement account. We're working to lift the value of home. This year, we will step up re-financing (of mortgages)

National security

- ☐ We have strengthened partnerships from the Pacific to South Asia to the Arabian Peninsula.
- ☐ In Afghanistan, our troops can begin to come home in July of 2011.
- ☐ We will have all of our combat troops out of Iraq by the end of this August.
- ☐ At April's Nuclear Security Summit, we will bring forty-four nations together behind a clear goal: securing all vulnerable nuclear materials around the world in four years.
- ☐ These diplomatic efforts have also strengthened our hand in dealing with those nations (North Korea and Iran) that insist on violating international agreements.

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congress. On March 21, the bill was barely approved and passed into law on March 23.

[29] Financial regulatory reform bill was passed the Lower House in December 2009 and the Upper House in May 2010. Meanwhile, on January, President Obama announced Volker Rule, which is new restrictions on size and scope of financial institutions and called for a large-scale financial institutions to bear the burden of financial crisis in the form of levy.

[30] In July 2009, a comprehensive bill that includes energy measures and Cap and Trade passed the Lower House. In the Upper House, the framework of supra-partisan energy and climate change bill was released in December 2009. Now, the framework is now under discussions to form a bill. The discussion is based on the results from COP15 held in Copenhagen of 2009, however, the progress is not clear.