

in real terms). Private residential and non-residential investment remained weak, both contributing just 0.1 percentage point to real GDP growth in 2011.

The unemployment rate reached 4.6 percent in December 2011, a fairly high level for Japan. The rate was double among persons aged 15 to 24. Difficulties in the employment situation were partly due to the disasters, and have showed signs of improvement since. Industrial production and the economy as a whole picked up slowly, but exports and corporate profits remained weak, with deflationary risks present. The long-standing issues in the Japanese economy that have stunted its growth for the past two decades still persisted, and the Japanese government continued to focus on combatting deflation and yen appreciation, a combination that could generate a vicious cycle for Japanese producers.

Prospects for Japan are positively influenced by its reconstruction spending; real GDP is expected to grow 2.0 percent in 2012, and moderate to 1.7-percent growth in 2013 as that spending is phased out. Downside risks are very significant, as Japan is vulnerable to a possible intensification of the European debt crisis and stands to lose amounts comparable to its projected real output growth under the unfavorable scenario of decreased external demand. Japan is also vulnerable to possible energy supply issues, such as an oil price spike due to political tensions and the slowing down of activity in the Chinese economy.

Eurozone

The embers of the European crisis continued to smolder in 2011, flaring up on several occasions and projecting uncertainty across the global economy. This uncertainty was the key feature in last year's global economic performance, and uncertainty will likely

continue in the short-to-medium term. This is because the resolution of the sovereign debt crisis in the affected countries could ultimately take several forms and require many years to complete. These forms could range from a fiscal union, to a partial or complete breakup of the common currency zone, to the gradual working out of European imbalances through inflation in the North and deflation in the South, to a combination of these and other solutions.

Largely in response to this uncertainty, growth in the eurozone decelerated from 1.9 percent in 2010 to 1.4 percent in 2011, with consumer spending growing just 0.2 percent in 2011 and government spending remaining flat. Accordingly, the contribution from private consumption to total GDP was minimal at 0.1 percentage point, and zero from government spending. Gross fixed capital formation added 0.2 percentage point to GDP growth, and changes in inventories boosted GDP by another 0.1 percentage point. Net exports provided the largest boost (1.0 percentage point) to real GDP growth.

Germany's real GDP increased 3.1 percent, France's by 1.7 percent while Italy showed modest 0.4-percent growth. The renewed fears of escalation of the sovereign debt crisis slowed growth in the fourth quarter sharply and tipped the region back into recession. As a large portion of the sovereign debts of Portugal, Spain and Italy is held by the banks, renewed doubts about the solvency of these countries lowered confidence in the banking sector and drove up the risks associated with financing, which in turn further depressed these economies by restricting private-sector credit. Funding pressures were somewhat alleviated at the end of 2011 by the European Central Bank's long-term refinancing operations, which stabilized market sentiment and reduced uncertainty.