

per capita government debt among the major industrial countries and the government resorts to the long-term bond market to balance its books. The lower than expected rate of economic growth this fiscal year has resulted in reduced government revenues and a worsening of the government's fiscal problems, prompting former Prime Minister Suzuki late last year to declare a "state of fiscal emergency". Measures associated with this include a freeze on pay increases for public servants, reduced agricultural subsidies and restructuring of the finances of the deficit-ridden national railway.

The performance of the yen on international exchanges remains weak. This is primarily the result of a net capital outflow attracted by higher American interest rates. The capital outflow has compounded the difficulties of servicing the Government's large budget deficit, and the cheaper yen threatens in time to renew inflationary pressures by increasing the cost of imports. Japan's principal trading partners are, on the other hand, highly sensitive to any appearance of export-led growth that might be fuelled by an unrealistically weak yen.

Japan has largely won its fight against inflation (the CPI is increasing at an annual rate of about 3.2%) and unemployment remains remarkably low in comparison to most countries (2.4%). Interest rates, at around 5.5%, do not approach the high levels in North America.

The outlook for the Japanese economy is uncertain, with recovery in early 1983 unlikely in the absence of favourable external factors such as the recovery of the USA economy. Although in the past Japan has played an important role as a locomotive force for a depressed world economy, at this juncture it is evident that the Japanese themselves are expecting world economic recovery in part to contribute to the recovery of the Japanese economy.

#### Foreign Relations

Japanese foreign policy has consistently sought to ensure the physical security of the Japanese islands and the continued economic well-being of the Japanese people. In recent years there has been the growing realization that the achievement of these objectives will require Japan to play a larger role, both politically as well as economically, in international affairs. This has been encouraged by Canada.

It is unlikely that the new Nakasone administration will radically alter Japan's foreign policy priorities in either the economic or political domain. It