Economic Trends

Daiichi Life Research Institute

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Commentary on the Council on Economic and Fiscal Policy (October 29, 2026)

~Towards Concrete Implementation of Radical Budgeting Overhaul, and Policy Formation Anticipating Economic and Social Transformations Driven by AI~

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(Executive Summary)

○ Positioning the FY2027 budget as the "First Year of Responsible Active Fiscal Policy," three main approaches were outlined to enhance the predictability and policy effectiveness of growth and crisis management investments:①Utilization of the "Strong and Prosperous Japan" Investment Framework、②Transition to an initial-budget-centered management、③Refinement of tax revenue estimates and securing of fiscal resources

○ For restructuring social mechanisms premised on AI, a comprehensive policy response was proposed from four perspectives:①Productivity improvement and labor market response、②Strengthening cybersecurity、③Ensuring autonomy and independence、④Adapting to change and structural education reform

○ Author's Policy Recommendations:

①Fundamental Refinement of Tax Revenue Estimation Methods: Given the reality that tax revenues have significantly exceeded initial estimates at settlement due to structural shifts toward a growth-oriented economy, the causes of divergence must be accurately analyzed to enhance estimation precision.

②Utilization of Foreign Exchange Special Account Surplus and Retained Funds: Since buffers against exchange rate risks are sufficient due to yen depreciation, the outdated retention rule should be revised to continuously allocate the full surplus to general account revenue. Mid-to-long-term management of excess retained funds should also be re-evaluated with reference to overseas precedents.

③Enhancing Macro Productivity and Addressing Distributional Structures: Beyond simple AI adoption, structural changes such as organizational reform and labor mobility must be encouraged. Furthermore, vigilance is needed regarding risks of declining labor shares and depressed natural interest rates resulting from capital deepening and wealth concentration.

④Formulating Japan-Specific AI Employment Measures: Unlike overseas trends, AI-driven automation in Japan is most likely to affect administrative female employees, non-regular workers, and redundant middle-aged/senior staff. Reskilling support and labor safety nets should prioritize these groups alongside fostering high-skilled talent.

1. Introduction

At the Council on Economic and Fiscal Policy held on October 29, 2026, discussions focused on "Concrete Implementation of Radical Budgeting Overhaul" and "Towards Policy Formation Anticipating Economic and Social Transformations Driven by AI."

Based on the meeting documents, this report summarizes the main discussion points from the Council meeting and outlines the author's opinions and recommendations.

2. Concrete Implementation of Radical Budgeting Overhaul

Positioning the FY2027 budget as the "First Year of Responsible Active Fiscal Policy," three key proposals were made to execute the fundamental budgeting overhaul outlined in the Basic Policies 2026. The objective is to increase the predictability of growth and crisis management investments to unlock sustainable innovation and economic growth.

Developing a Budget System Connecting the "Strong and Prosperous Japan" Investment Framework to Growth Strategies:

Integrating Multi-Year Fiscal Measures with Action Plans: Starting from priority areas in the "Japan Growth Strategy Action Plan" (to be finalized at year-end), the scale and timing of public/private investments and support policies for subsequent fiscal years should be clarified to ensure predictability for private sector investment. Sufficient multi-year funds should be secured in special accounts, particularly for areas crucial to economic security.

Shifting Budget Assessment from "Cutting Amounts" to "Refining Policy Design": Rather than merely adjusting single-year budget requests, assessments should evaluate private investment inducement effects, multi-year necessity, and future fiscal burdens to enhance overall policy quality.

Leveraging Expertise and Managing Policy Portfolios: Government expertise should be enhanced alongside external professional insights for progress monitoring and evaluation. The entire investment framework and policy tools (subsidies, tax incentives, fiscal loans) should be managed as a "policy portfolio," scaling down low-effect programs and reallocating resources to high-impact areas.

Ending Habitual Reliance on Supplementary Budgets & Transitioning to Multi-Year Budget Management:

Initial-Budget-Centered Operation: Continuously required measures should be funded via initial budgets, restricting supplementary budgets strictly to emergencies, disasters, or sudden macroeconomic shifts.

Frameworks Supporting Multi-Year Predictability: Treasury debt contract authorizations and funds should be utilized appropriately according to business characteristics.

Refining Tax Revenue Estimates and Securing Revenue Sources:

Refining Tax Revenue Estimation: Past divergence factors should be analyzed in close coordination with the Cabinet Office's macroeconomic forecasts to raise accuracy and transparency.

Securing Non-Tax Revenues: Considering the financial status of the Foreign Exchange Special Account, available non-tax revenues must be precisely captured and allocated as funding sources.

3. Towards Policy Formation Anticipating Economic and Social Transformations Driven by AI

Recognizing that the widespread adoption of AI will cause profound economic and social transformations, four proposals were submitted to redesign social mechanisms holistically rather than treating AI merely as an isolated industrial sector.

Improving Productivity via AI and Addressing Labor Market Needs:

Maximizing Productivity: AI should be leveraged both to increase value-added (revenue expansion/cost reduction) and to reduce working hours, positioning Japan as an "Advanced AI User Nation." Support for AI for Science and AI-driven startups should be accelerated.

Employment, Human Resources, & Safety Nets: Deliberations on labor laws and regulatory reforms (including expanding discretionary labor systems) should be accelerated to reflect AI-driven productivity gains in compensation. Job-matching functions via Job Tag and economic buffer systems for displaced workers must be established.

Updating Systems and Metrics: Legal and transaction frameworks suited for AI agents and new market practices should be reviewed, alongside developing evaluation metrics that capture AI usage costs (e.g., token fees) against value-added.

Strengthening Cybersecurity:

To counter AI-driven cyber attacks and personal data breaches, public and private sectors must collaborate to consolidate incident reporting under the National Cyber Directorate, secure web systems, reinforce supply chain defenses, and manage data robustly.

Ensuring Autonomy and Independence (AI Sovereignty):

To avoid structural subordination to foreign "frontier model" providers, Japan must solidify its position as an indispensable supplier in key component sectors such as semiconductors and physical AI. Simultaneously, domestic AI technical capabilities, model alternatives, and business continuity plans (BCP) must be maintained.

Flexibly Adapting to AI-Driven Changes & Educational Reform:

Japan should actively participate in international public-private discussions (such as the Davos Forum and Global AI Summit) and accelerate comprehensive domestic debate on AI's macroeconomic impacts.

School curricula must be fundamentally reformed from traditional rote memorization/calculation toward cultivating "learning agility for new skills" and self-driven "initiative (starting power)." Educational AI usage guidelines should be continually updated to elevate Japan's school AI utilization frequency from the bottom of OECD rankings.

4. Author's Policy Recommendations

Based on the above discussions, the author presented the following policy recommendations regarding "Budgeting Overhaul" and "AI-Driven Policy Formation" during the Council meeting.

A. Eliminating Divergence Between Tax Revenue Estimates and Settlement Results

Analysis: Over the last four years, actual tax revenues at settlement exceeded initial estimates by an annual average of 2.3 trillion yen for income tax (11.3% divergence) and 1.6 trillion yen for corporate tax (9.7% divergence).

Proposal: This is not a temporary anomaly; the transition to a growth-oriented economy with rising wages and prices since 2020 has altered the structural relationship between economic growth and tax revenue. The government must accurately analyze these structural shifts and fundamentally refine its tax revenue forecasting models.

B. Continuous Utilization of Foreign Exchange Special Account Surplus & Retained Funds

Analysis: Under current rules established in 2010, foreign exchange surplus funds are retained until cumulative reserves reach 30% of foreign assets. However, due to yen depreciation, total valuation gains have pushed the actual risk buffer to 45%, far exceeding the 30% threshold.

Proposal: The government should move past outdated 2010 benchmarks and continuously transfer 100% of annual flow surpluses to the general account for FY2027 and beyond. Furthermore, mid-to-long-term management of excess retained funds (>40%) should be re-examined by studying G7 asset/liability management practices (e.g., Canada returning foreign reserve gains to government coffers).

C. Promoting Macro Productivity & Monitoring Distributional Structures

Analysis: While capital expenditure on data centers and semiconductors is surging, transforming this into macro-level productivity requires organizational restructuring and labor reallocation rather than isolated software adoption.

Proposal: Policy must facilitate these structural changes. Additionally, attention must be paid to long-term distributional shifts: as AI drives capital deepening, value-added may increasingly accrue to capital rather than labor, lowering the labor share. This concentration of wealth risks depressing consumer demand and lowering the natural rate of interest over time.

D. Constructing a Japan-Specific AI Employment Safety Net

Analysis: While overseas AI adoption primarily squeezes entry-level youth employment, Japan's labor market structure differs. In Japan, AI-driven automation poses the greatest displacement risk to female administrative staff, non-regular employees, and surplus middle-aged/senior corporate personnel.

Proposal: System redesigns for the AI era must look beyond elite tech talent to establish targeted reskilling programs, smooth labor mobility pathways, and robust safety nets specifically tailored to these vulnerable demographic groups.

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