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Assessing the Economic Policy Agenda of the Takaichi Administration:

A constructive alignment with global trends, but fiscal reforms and inflation control remain key issues

Tomohisa Ishikawa*

ishikawa.tomohisa@jri.co.jp

<Summary>

- The Takaichi administration has issued the Basic Policy on Economic and Fiscal Management and Reform(Honebuto) and the Japan Growth Strategy. The agenda seeks to strengthen Japan's supply capacity and earning power through strategic public-private investment, while securing fiscal sustainability through higher tax revenues generated by growth. At a time when state-led industrial policy is returning globally and competition over economic security and critical technologies is intensifying, the emphasis on crisis-management investment and growth investment is broadly consistent with international policy trends.
- Yet the agenda also raises important implementation challenges. The growth strategy covers a wide range of sectors, risking a dispersion of scarce policy resources. To translate public support into stronger potential growth, the government will need a sharper prioritization of strategic sectors, mechanisms to prevent inefficient spending, a credible PDCA cycle to evaluate policy outcomes, institutional designs that crowd in private capital, and closer integration with regulatory reform.
- On fiscal policy, the introduction of a medium- to long-term economic and fiscal plan marks progress by placing budget management within a multiyear framework. However, the absence of concrete targets and deadlines for the debt-to-GDP ratio, the primary balance, and annual expenditure ceilings leaves questions about the effectiveness of fiscal discipline. Budget requests have reached a record high, while many items have been submitted without specified amounts. With Japan's output gap expected to remain positive, expansionary fiscal policy could further intensify inflationary pressures.
- On social security, the proposed refundable tax credit and the goal of restraining the burden on working-age households are welcome. But if the digital infrastructure needed to capture

*Research Director/ General Manger / Chief Economist (Economics Department, JRI).

income and asset information lags behind, the fairness and effectiveness of the system could be undermined. The temporary consumption-tax cut on food should also be reversed as scheduled in two years if Japan is to move credibly toward fiscal consolidation.

- On monetary policy, it is encouraging that the Basic Policy includes language respecting the autonomy of the Bank of Japan. Nevertheless, references to close consultation with the government and reports concerning government requests on government-bond purchases mean that the practical safeguarding of the BOJ's independence remains a central issue.
- The policy direction on regional revitalization and foreign-resident policy is broadly timely. Still, regional revitalization requires execution grounded in local strengths; the secondary-capital concept requires institutional design that reflects national interests and crisis management; and foreign-resident policy needs a long-term vision that incorporates not only social order but also demographics and the changing demand for labor caused by AI and robotics.
- In sum, the administration should pursue stronger growth while building safeguards against indiscriminate spending, and it should do so with equal attention to fiscal consolidation and price stability.

- **This is an English version of "高市政権の経済政策をどうみるか～世界の潮流に沿った点は評価、課題は財政再建とインフレ抑制～" in JRI Viewpoint.**

1. The Basic Policy and Japan Growth Strategy by the Takaichi administration

On July 21, the Takaichi administration approved two core policy documents: the Basic Policy on Economic and Fiscal Management and Reform and the Japan Growth Strategy. Taken together, these documents reveal a clear effort to raise Japan's supply capacity and earning power through strategic public-private investment, while securing fiscal sustainability through the tax revenue gains generated by stronger growth. At the same time, questions remain over whether the administration's commitment to fiscal discipline will be sufficiently credible to maintain market confidence. The agenda also contains distinctive elements of the Takaichi administration, including policies toward foreign residents and regional revitalization. On monetary policy, as Japan enters a phase in which additional tightening is increasingly being considered, a major challenge will be how to maintain an appropriate distance between the government and the Bank of Japan.

Against this backdrop, this report assesses the Takaichi administration's economic policy agenda across five areas: growth strategy; fiscal and social security policy; monetary policy; regional revitalization and the secondary-capital initiative; and policy toward foreign residents.

2. Overview of the Takaichi Administration's Policy Agenda

Viewed as a whole, the Takaichi administration's policy agenda is strongly growth-oriented(Figure1). As state-led industrial policy regains prominence around the world and strategic competition over economic security and critical technologies intensifies, Japan's effort to raise supply capacity through public-private investment is broadly aligned with international trends. On the fiscal front, the administration has presented a medium- to long-term economic and fiscal plan covering fiscal years 2027 through 2040 to advance fiscal sustainability. A multiyear framework for budget management, used in many countries to strengthen fiscal discipline, is an important step toward maintaining confidence in fiscal policy. On monetary policy, the administration has also shown a degree of respect for the independence of the Bank of Japan. In addition, the agenda gives concrete direction in areas of high public interest, including policy toward foreign residents, regional revitalization, and disaster resilience.

Figure1.Summary of Economic policies of Takaichi administration

	Summary	Assessment and Key Challenges
Growth Strategy	• Designates 62 priorities across 17 sectors as strategic growth areas • Commits to growth-enhancing and risk-management investment, including in economic security	• The broad direction is sound and consistent with the global revival of industrial policy. • Key challenges are: (1) an excessively broad sectoral scope; (2) an operating and governance framework that is not yet in place; (3) a lack of clarity on mechanisms to crowd in private investment; and (4) insufficient ambition on regulatory reform.
Fiscal Policy	• Sets out a medium- to long-term economic plan • Removes the term "fiscal consolidation," which had been included since the framework was introduced in 2001	• Establishing a medium- to long-term plan is a welcome step. • Key concerns are: (1) the absence of quantified targets and deadlines; and (2) the abolition of expenditure ceilings.
Social Security	• Introduces a refundable tax credit • Continues reforms to benefits and contributions • Cuts the consumption tax rate on food by 1 percentage point for two years	• The commitment to reducing the burden on the working-age population is welcome. • The principal challenge is whether the consumption tax rate can be risen after two years.
Monetary Policy	• Gives some consideration to the Bank of Japan's independence	• Recognition of central bank independence is positive. However, the emphasis remains on policy coordination with the government, leaving the extent to which the Bank of Japan can preserve its independence uncertain.
Regional Revitalization	• Formulates and implements a Regional Future Strategy	• The explicit commitment to regional revitalization is positive. • The key challenge is to establish effective implementation frameworks for the Regional Future Strategy and the secondary-capital initiative.
Policy toward Foreign Resident	• Promotes orderly coexistence	• Given the rapid increase in the foreign-resident population, stronger measures to maintain order are warranted. • However, the policy may place excessive emphasis on near-term social order. Developing a long-term vision informed by technological trends, demographic change, and other structural factors is an urgent priority.

Source: JRI based on Cabinet Office

Still, significant challenges remain. The growth strategy spans a large number of sectors and could dilute scarce policy resources. Fiscal policy lacks specific numerical targets and deadlines, leaving uncertainty about whether discipline will be enforced in practice. With Japan's output gap expected to remain positive, the government must also explain how it will prevent expansionary fiscal policy from adding to inflationary pressure. Monetary policy raises continuing questions about the proper balance between coordination with the government and

respect for central-bank independence. Policy toward foreign residents requires not only social-order considerations but also a long-term view of how technological change, including AI, will affect labor demand. Regional revitalization and the secondary-capital initiative will likewise depend on credible institutional design and execution.
The following sections examine these issues in greater detail.

3. Growth Strategy: The Next Challenge Is Prioritization

The growth strategy deserves credit for reflecting the direction of global economic policy. The World Bank's Industrial Policy for Development notes that government-led industrial policy is "back with a vengeance." In this context, the Basic Policy's aim of using public action to catalyze private investment, strengthen supply capacity, and raise Japan's earning power is consistent with the broader international trend.
The administration's growth path can be understood in two parts. The first is "crisis-management investment." This includes economic security, food security, energy and resource security, health and medical security, national resilience, and cybersecurity. The objective is to secure Japan's autonomy by reducing vulnerability to economic coercion and social risks. At the same time, by providing the resulting products and services at home and abroad, Japan aims to enhance its indispensability in the global economy and strengthen its bargaining power and security foundation.
The second is "growth investment" aimed at cultivating advanced technologies. The goal is to build the foundations of a strong economy by promoting commercialization in areas where Japan has technological advantages and by fostering innovation that creates hard-to-replicate science, technology, and new value added. Here, too, the Basic Policy implies an emphasis on indispensability, underscoring the administration's strong awareness of economic security. At a time of rising geopolitical risk, advancing a growth strategy with economic security in mind can be regarded as broadly consistent with the international environment. At the same time, several challenges remain. The first is the breadth of targeted sectors. According to the World Bank report cited above, low-income countries designate an average of 13 priority sectors, while advanced economies typically designate fewer than half that number. Against this benchmark, Japan's selection of 17 sectors appears somewhat too broad(Figure2). To make effective use of limited policy resources, the government will need to sharpen its priorities and concentrate support on the most strategically important areas.

Figure2. 17 Strategic Sectors of the Takaichi Administration

1	AI and Semiconductors
2	Digital and Cybersecurity
3	Information and Communications
4	Quantum Technology
5	Defense Industry
6	Aviation and Space
7	Maritime Industries
8	Shipbuilding
9	Advanced Materials (Critical Minerals, Components, and Materials)
10	Synthetic Biology and Biotechnology
11	Drug Discovery and Advanced Medicine
12	Resource and Energy Security / Green Transformation (GX)
13	Fusion Energy
14	Disaster Prevention and National Resilience
15	Port Logistics
16	Food Technology
17	Content Industries

Source: JRI based on Cabinet Office

The second challenge is the governance architecture for implementing industrial policy. The World Bank report emphasizes the importance of politically insulated implementing agencies, low-cost public support, the use of market incentives, and vigilance against macroeconomic risks arising from intervention. The Basic Policy and the Japan Growth Strategy state that, under the Japan Growth Strategy Council, the government will repeatedly operate a PDCA mechanism to specify multiyear measures during the budget process—including the budget-request stage—and to refine or revise those measures in light of implementation status and technological developments, with the 5W1H perspective in mind. This language shows an awareness of the need to avoid indiscriminate spending. However, the concrete institutional arrangements needed to ensure effectiveness are not yet sufficiently clear. Unless carefully designed, industrial policy carries the risk of becoming a channel for inefficient spending. Establishing a credible implementation framework is therefore the next critical task.

The third challenge is whether policy can catalyze private investment. The key will be whether Japan can mobilize not only fiscal resources but also capital from sources such as the Government Pension Investment Fund and NISA accounts. The institutional framework needed to channel such capital into growth investment should be discussed without delay.

The fourth challenge is regulatory reform. While regulatory reform generally does not deliver immediate results, it can limit the need for fiscal outlays and, over the longer term, generate substantial benefits by supporting private-sector growth. The Takaichi administration has not placed strong emphasis on regulatory reform, but precisely now is the time to move it forward.

4. Fiscal Policy: With the Removal of Ceilings, Budget Requests Reach a Record High

The Takaichi administration has presented a medium- to long-term economic and fiscal plan covering fiscal years 2027 through 2040 as part of its effort to achieve fiscal sustainability. The use of fiscal and expenditure plans to manage budget policy over multiple years has been widely adopted overseas to strengthen fiscal discipline, and represents an important step toward maintaining confidence in fiscal management.

The plan deserves credit for including provisions to secure market confidence and strengthen analysis and verification with respect to economic trends, fiscal indicators, and economic and fiscal projections. It also states that the Council on Economic and Fiscal Policy will, in principle, conduct a comprehensive review every five years.

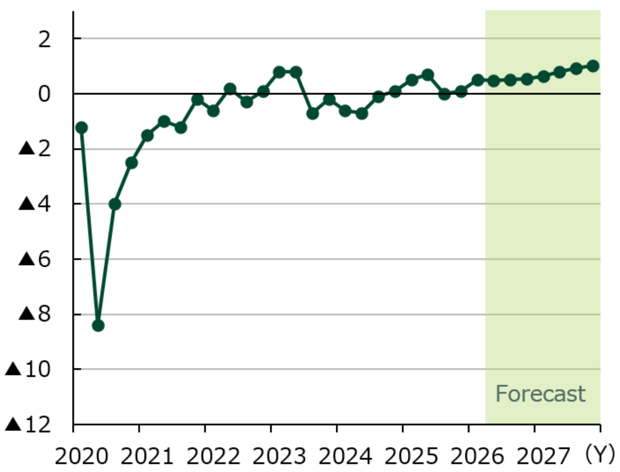
The main weakness is the absence of concrete numerical targets and deadlines. While the plan places the stable reduction of the general-government gross debt-to-GDP ratio at the core of fiscal management, it does not specify either the target level or the timing for achieving it. On the primary balance, the plan states that the government will not mechanically pursue a single-year surplus target, but rather may allow temporary deterioration depending on economic and interest-rate conditions, revenue and expenditure trends, and the need for crisis-management and growth investment. This marks a significant retreat from the previous year’s Basic Policy, which called for achieving a primary surplus between fiscal 2025 and early fiscal 2026 and for reducing the debt-to-GDP ratio toward its pre-pandemic level. The plan also provides no numerical ceiling or benchmark for the annual level of expenditures or government-bond issuance, stating only that the government will examine the fiscal scale consistent with a stable decline in the debt-to-GDP ratio while monitoring tax revenues, reviewing both expenditures and revenues, and maintaining market confidence.

In many other countries, medium-term fiscal plans set specific goals, such as bringing the current budget into surplus by a particular fiscal year or reducing the debt-to-GDP ratio to a specified level by a given date. They often also provide annual expenditure ceilings or benchmarks. To evaluate progress toward fiscal objectives and make appropriate adjustments, Japan should likewise establish clear deadlines and quantitative targets, while providing indicative annual expenditure levels.

The administration has also indicated that no ceiling will be imposed on requests related to growth sectors and crisis-management investment, in order to encourage bold investment. Finance Minister Katayama described the new budget-request guidelines after Cabinet approval as “groundbreaking” and as symbolizing a turning point, adding that they should no longer be called ceilings. Against this backdrop, budget requests reached approximately ¥143 trillion, the highest level on record and well above the ¥122.4 trillion requested for fiscal 2026, marking the fourth consecutive record high. The government had used ¥140.6 trillion—the combined total of the fiscal 2025 supplementary budget and the initial fiscal 2026 budget—as a reference point, but requests have exceeded that amount. Moreover, because some requests are submitted without specified amounts, total expenditures are likely to rise further.

Negotiations between the Ministry of Finance and individual ministries and agencies will intensify toward the end of the year. The key questions will be how the government restrains pressure for higher spending and how it ensures the quality of growth-oriented investment.

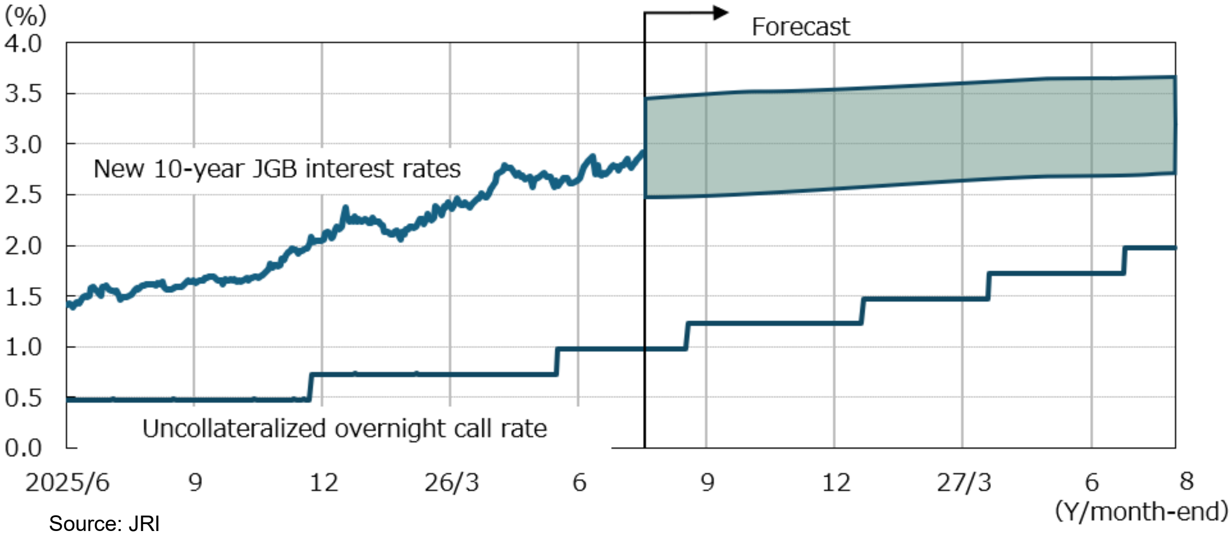
Figure3. GDP gap in Japan(%)



Source: JRI based on Cabinet Office

JRI expects Japan’s output gap to remain in positive territory going forward (Figure 3). At a time when supply-demand conditions are tightening, the government will need to explain carefully how it intends to address the risk that expansionary fiscal policy could further strengthen inflationary pressures. JRI also assumes that the Bank of Japan will continue raising the policy rate by around 0.25 percentage points roughly every six months, ultimately bringing it to about 2 percent. Long-term interest rates are also expected to remain on a gradual upward trend (Figure 4), increasing the likelihood of higher government interest payments. To maintain market confidence in fiscal management during a period of rising interest rates, it is essential that the government set out a clearer path toward fiscal consolidation while also strengthening growth potential.

Figure4. Outlook for Japan's Main Interest



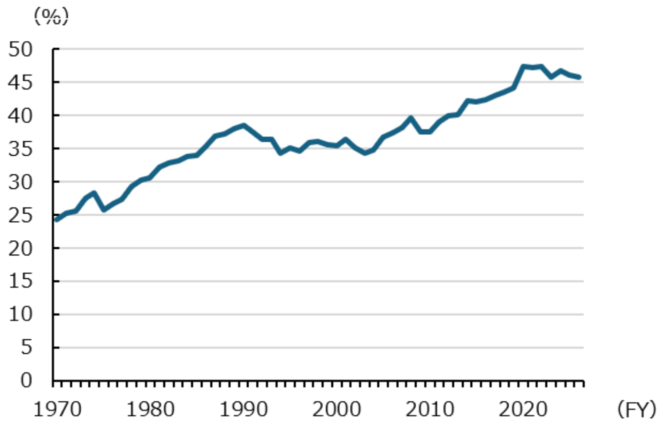
Source: JRI

5. Social Security: Can the Consumption Tax Be Restored Before the Upper House Election Two Years from Now?

In social security, the key measures are the refundable tax credit and the temporary reduction of the consumption tax rate on food as a bridge measure. The refundable tax credit is scheduled for full-scale introduction in fiscal 2029. At the outset, the government plans to begin not with a tax-credit mechanism but with a unified cash-benefit approach, under which the amount equivalent to the tax reduction will be paid in a lump sum. In Japan, the tax and social-security burden on low- and middle-income households has been rising more steeply than in many OECD countries. The proposed measure appears intended not only to correct this trend but also to address the so-called income wall by providing income-linked support that encourages work, rather than functioning merely as a benefit for low-income households. This approach deserves some credit. The fact that the consumption-tax reduction on food is designed as a temporary measure also suggests attention to fiscal discipline.

The Basic Policy also states that, with respect to social-security expenditures, the government will continue reforming benefits and burdens with the aim of halting and eventually reducing the rise in insurance-premium rates for working-age generations, while taking into account not only national-government spending but also total benefit costs, public and premium burdens, and disposable income among working-age households. This signals an intention to curb the national burden ratio, including taxes and social-insurance premiums, which has risen over time (Figure 5). This point is also noteworthy.

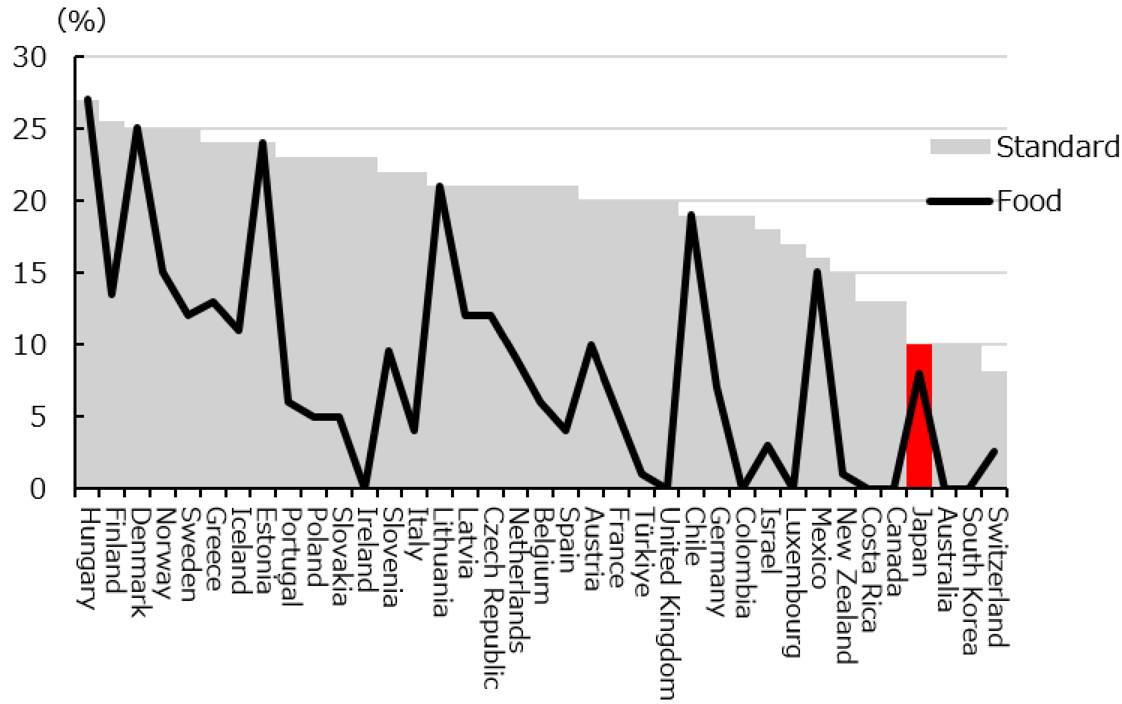
Figure5. National Burden ratio



Source: JRI based on Ministry of Finance

At the same time, challenges remain. First, in prioritizing early implementation of the refundable tax credit, the government may delay the digital infrastructure needed to capture income information accurately. To ensure appropriate taxation and benefits, Japan must move quickly to build the digital foundations needed to identify income and asset information with precision. Second, the major test will be whether the temporarily reduced consumption tax rate can in fact be restored two years from now. Prime Minister Takaichi has acknowledged that the consumption tax is a vital source of social-security funding and has stated that, from the standpoint of fiscal sustainability and market confidence, she will "take responsibility for restoring the tax rate two years from now." However, an Upper House election is scheduled for 2028, and it cannot be ruled out that restoring the rate in April 2029 could become politically difficult. While the prime minister has indicated that an economic contingency clause is unnecessary, she has also referred to the need for a framework that would allow the consumption tax rate to be adjusted flexibly in the event of infectious diseases or major disasters. Uncertainty over future tax-rate changes therefore remains. Through successive policy designs by past administrations, the consumption tax has become a core tax that now accounts for roughly 30 percent of total tax revenue. By international comparison, neither Japan's standard rate nor its tax rate on food is particularly high (Figure 6). It is therefore important to restore the rate as planned so as not to undermine its stability as a source of social-security financing.

Figure6. Value added Tax ratio



Source: JRI based on Ministry of Finance

6. Monetary Policy: Preserving the BOJ's Independence Is Essential

The Basic Policy includes, in a footnote, language stating that specific monetary-policy tools are entrusted to the Bank of Japan, reflecting the intent of Article 3 of the Bank of Japan Act, which stipulates that the BOJ's autonomy in currency and monetary control must be respected. This recognition of the BOJ's independence deserves credit. The wording appears to have been revised in response to the so-called Basic Policy shock, in which market concerns over the BOJ's independence intensified at the draft stage and long-term interest rates rose. From the standpoint of financial-market stability, this revision can be viewed positively.

At the same time, the discussion of Article 4 of the Bank of Japan Act, which provides for communication and consultation between the government and the BOJ, appears in the main text. Given the difference in placement between the main text and the footnote, markets may still perceive that the overall policy direction leaves some room for government involvement in monetary policy.

Media reports have also suggested that Prime Minister Takaichi asked the BOJ governor to purchase government bonds. Although the facts are unclear, such reports themselves could raise market doubts about the BOJ's independence. To reconcile price stability with confidence in fiscal management, the government needs to make clear that it will respect the BOJ's independence while coordinating appropriately and maintaining a clear division of roles.

7. The Regional Future Strategy Begins to Move: The Next Challenge Is Implementation Capacity

On regional revitalization, the government has also set out a policy direction based on the growth strategy. Specifically, the Basic Policy calls for advancing the Regional Future Strategy, implementing strategic industrial-cluster plans that extend beyond prefectural boundaries, expanding the Regional Future Grant, promoting regulatory and institutional reform through special-zone frameworks, and supporting young people's education and employment in light of the implementation status of the Act on Regional Universities and Regional Industrial Creation.

These measures are broadly consistent with the direction of regional revitalization policy that the government has pursued to date. Some observers had expected that the policy priority attached to regional revitalization might decline compared with the Ishiba administration, but the inclusion of a wide range of policy tools in the latest agenda appears to have eased such concerns to some extent.

Still, the challenges are considerable. On the Regional Future Strategy, the direction is appropriate, but policymakers should recognize that similar cluster strategies in the past did not always deliver sufficient results. Successful regions have tended to share several characteristics: they specialize in local strengths; they not only produce high-quality goods and services but also actively communicate them to national and global markets; they make effective use of local universities and other knowledge institutions; and they have leaders capable of driving the region forward with the speed and agility of a start-up. The priority, therefore, should be execution rather than prolonged discussion or planning.

The special-zone system also needs to be strengthened. In many cases, past deregulation under special zones has remained relatively modest. Going forward, the government should allow more fundamental regulatory reforms capable of serving as catalysts for local economies, and should use the special-zone framework as a breakthrough mechanism for broader regulatory reform. The Regional Future Grant should also be subject to careful evaluation so that it does not become a vehicle for indiscriminate subsidies. This is especially important under an administration that has emphasized active fiscal policy. In addition, reforms should be advanced so that regional universities can function as local think tanks. For example, as universities, including regional institutions, face financial constraints, the government could support tax incentives or financial products that help mobilize local capital for the revitalization of regional universities. Appropriate regulatory reforms concerning university asset management should also be considered.

The Basic Policy also explicitly includes the development of a secondary capital as part of efforts to promote disaster prevention, mitigation, and national resilience. The key objectives are to ensure the continuity of national and social functions; to create a more decentralized, multipolar economic structure; and to deploy policy tools, including regulatory reform, that contribute to economic growth. Japan is highly exposed to natural disasters, and the possibility of a Nankai Trough earthquake remains a serious risk. Preparing an alternative location for capital functions is therefore an urgent policy challenge. At the same time, the initiative could also help address the long-standing problem of excessive concentration in Tokyo.

However, as various regions seek designation as a secondary capital, there is a risk that the regional-development dimension may overshadow the gravity of the mission: maintaining the country’s command-and-control functions in the event of a major disaster. The secondary-capital initiative should be clearly positioned not merely as a local revitalization measure, but as a national responsibility to safeguard the country. Moreover, a single prefecture or designated city may not be sufficient to perform the required functions, and deeper discussion is needed on cooperation across prefectural boundaries. The government’s 34th Local Government System Research Council is currently discussing administrative systems and local-government arrangements in metropolitan areas, and the secondary-capital initiative should be coordinated with that debate. Rather than treating the initiative as a stand-alone policy, the government should advance it as part of a broader reform of Japan’s local-governance system.

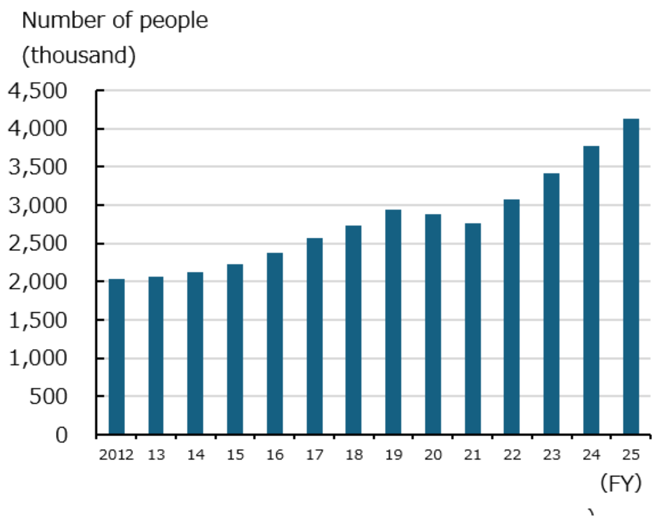
The Basic Policy also states that various institutional tools, including regulatory reform, should be used in the secondary capital. To make this meaningful, the newly designated secondary capital should be positioned as a testing ground for regulatory reform, with special-zone mechanisms and related instruments used effectively.

8. The Takaichi Administration’s Foreign-Resident Policy: A Long-Term Vision Must Go Beyond Order and Account for Technological Change

Under the principle of orderly coexistence, the Takaichi administration is advancing a foreign-resident policy that places particular emphasis on maintaining social order. Specific measures include: responding firmly to illegal conduct and rule violations by some foreign residents, and strengthening efforts to address public anxiety and perceptions of unfairness; using revenue secured through revisions to residence-permit fees and the introduction of the Japan Electronic System for Travel Authorization, or JESTA, to fund foreign-resident policy; vigorously promoting the Zero Illegal Residents Plan and building the institutional capacity needed to address illegal employment; ensuring proper operation of private lodging services in light of disputes with local residents in some cases; and enhancing education for foreign residents on the Japanese language as well as Japan’s institutions and rules.

With the number of foreign residents in Japan exceeding four million (Figure 7), the administration deserves credit for beginning to develop the institutional framework needed to avoid an unplanned expansion of future admissions. This can be viewed as a first step toward orderly coexistence. In other advanced economies, public attitudes toward foreign residents and immigration have become less tolerant than in the past, with governments paying greater attention to controlling inflows and preserving domestic order. Concern has also grown over the weaponization of migrants and refugees, in which large numbers of people are directed toward advanced economies to create social and political disruption, as seen recently in the inflow of many Moroccans into Spain's Ceuta. In this sense, the administration's approach is broadly consistent with the international trend toward maintaining order.

Figure7. Foreign residents



Source: JRI based on Immigration Services Agency of Japan

At the same time, conditions surrounding the acceptance of foreign residents differ significantly by region and industry. Some regions have relatively greater capacity to accept foreign workers, while others face pressure on living infrastructure and administrative services. Labor shortages are severe in certain industries, and many sectors have become increasingly dependent on foreign workers. Policy design therefore should not rely solely on uniform national rules, but should also incorporate fine-grained responses that reflect local capacity and industrial structure.

In addition, foreign-resident policy should more explicitly incorporate the impact of technological innovation on labor demand. The spread of AI and robotics could affect not only white-collar tasks but also blue-collar work. In the United States and China, where AI adoption is advancing rapidly, policy debates increasingly address not only labor shortages but also how to preserve employment in the face of technological substitution. In other words, future policy challenges will not be limited to labor scarcity; they will also include preparing for the possibility of labor surplus.

On August 7, the government held the first meeting of the Working Group on the Basic Approach to the Acceptance of Foreign Nationals. The meeting indicated that policy deliberations would take into account consistency with the comprehensive strategy being developed by the Headquarters for Population Strategy. If measures to address Japan's declining birthrate prove effective, the country's dependence on foreign workers could decline. Ensuring consistency with population strategy is therefore essential.

However, although the socioeconomic impact of foreign residents is included among the issues under consideration, the question of how technological innovation, including AI, will change the required number of foreign workers has not yet been addressed sufficiently. To make foreign-resident policy sustainable, Japan needs a long-term strategy that integrates population dynamics, regional absorption capacity, industry-specific labor shortages, and changes in labor demand driven by AI, robotics, and related technologies.

Taken together, the Takaichi administration's economic policy agenda is broadly aligned with international trends in its emphasis on growth investment and economic security, and its overall direction deserves a positive assessment. At the same time, improving policy effectiveness will require addressing several unresolved issues: narrowing the priority sectors for growth investment, clarifying fiscal discipline, safeguarding the independence of monetary policy, strengthening implementation capacity for regional revitalization and the secondary-capital initiative, and developing a long-term vision for foreign-resident policy. The administration will need to pursue policy management that reconciles stronger growth with fiscal sustainability and price stability.