

# World Economic Outlook Update

## Uncertainty Lingers even after the Deals

September 16, 2025

\*Translated from the original Japanese version released on August 26, 2025 (slightly modified)

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# Summary

## Uncertainty Lingers even after the Deals

### ▽ Real GDP growth projections (YoY%)

	World Share  2023 (%)	2024	2025	2026	Change from 2025 Feb. forecast (%points)	
		Estimate	Forecast	Forecast	2025	2026
<b>World</b>	<b>100</b>	<b>3.3</b>	<b>2.9</b>	<b>2.8</b>	<b>▲0.1</b>	<b>▲0.1</b>
<b>Advanced Economies</b>	<b>40.7</b>	<b>1.8</b>	<b>1.4</b>	<b>1.3</b>	<b>▲0.2</b>	<b>▲0.1</b>
United States	15.0	2.8	1.7	1.5	▲0.5	▲0.5
Euro Area	11.9	0.9	0.9	0.9	+0.2	0.0
United Kingdom	2.2	1.1	1.1	1.1	+0.2	+0.2
Japan	3.5	0.1	1.1	0.6	0.0	0.0
<b>Developing Economies</b>	<b>59.3</b>	<b>4.3</b>	<b>3.9</b>	<b>3.8</b>	<b>0.0</b>	<b>▲0.1</b>
China	18.7	5.0	4.5	4.2	+0.3	+0.3
India	7.9	6.7	6.4	6.0	▲0.1	▲0.3
ASEAN-5	5.1	4.6	4.0	3.9	▲0.2	▲0.3
Central, Eastern Europe	7.8	3.5	1.8	2.1	▲0.2	▲0.1
Latin America	7.3	2.4	2.2	2.2	▲0.1	▲0.2
Middle East, Central Asia	7.3	2.4	3.4	3.2	▲0.3	▲0.5
Sub-Saharan Africa	3.2	4.0	4.0	3.9	0.0	▲0.2

**World economy:** Global economic growth will slow down below the milestone of 3% in 2025 at +2.9% year-on-year and +2.8% in 2026. As the impact of US tariff measures slows down international trade in the second half of 2025 and beyond, downward pressure on the economy will have a stronger impact in 2026.

**Tariff negotiations:** Tariff agreements are reached in major countries, but higher tariffs are maintained. The tariff agreement should be seen as a temporary “landing point” as renewed pressure and renegotiation may occur depending on the implementation status of commitments to the United States. Tariffs on China are expected to remain unchanged due to continued postponement amid strong retaliatory pressure from China.

**Rethinking the Trump administration:** The Trump administration is leaning to opportunism, correcting its course according to market reactions rather than dogmatically promoting MAGA policies. It is also motivated to weaponize “uncertainty”, intentionally maintaining its policy uncertainty to retain negotiating advantage

**U.S. economy:** The economy stalled mainly in the labor market. In the second half of the year, the passing through movement of tariff hikes on domestic prices are expected to strengthen, and inflationary pressures will weigh on the economy, while fiscal policy and solid AI-related investments will support the economy. A soft landing is expected.

**China's economy:** The housing market remains sluggish for a long time. Once imposed extremely high U.S. tariff rates were suspended in May, but remaining relatively high tariff rates will weigh on the economy. Fiscal policy support is limited.

**Outside the U.S.:** Amid increasing U.S. policy uncertainty, other countries are seeking to strengthen trade relations outside the U.S., such as through FTA/EPA negotiations (‘paradoxical globalization’). On the other hand, there are concerns that U.S. tariff measures will motivate China to increase exports of cheap goods to non-U.S. economies and intensify trade frictions.

**JPY/USD market:** The fluctuations in the market over tariff negotiations have subsided for now. The market is expected to remain range-bound for the time being, but there are several risk factors. If the risk related to fiscal concerns lingering in both Japan and the United States occurs, it is possible that risk-averse trading will dominate the market.

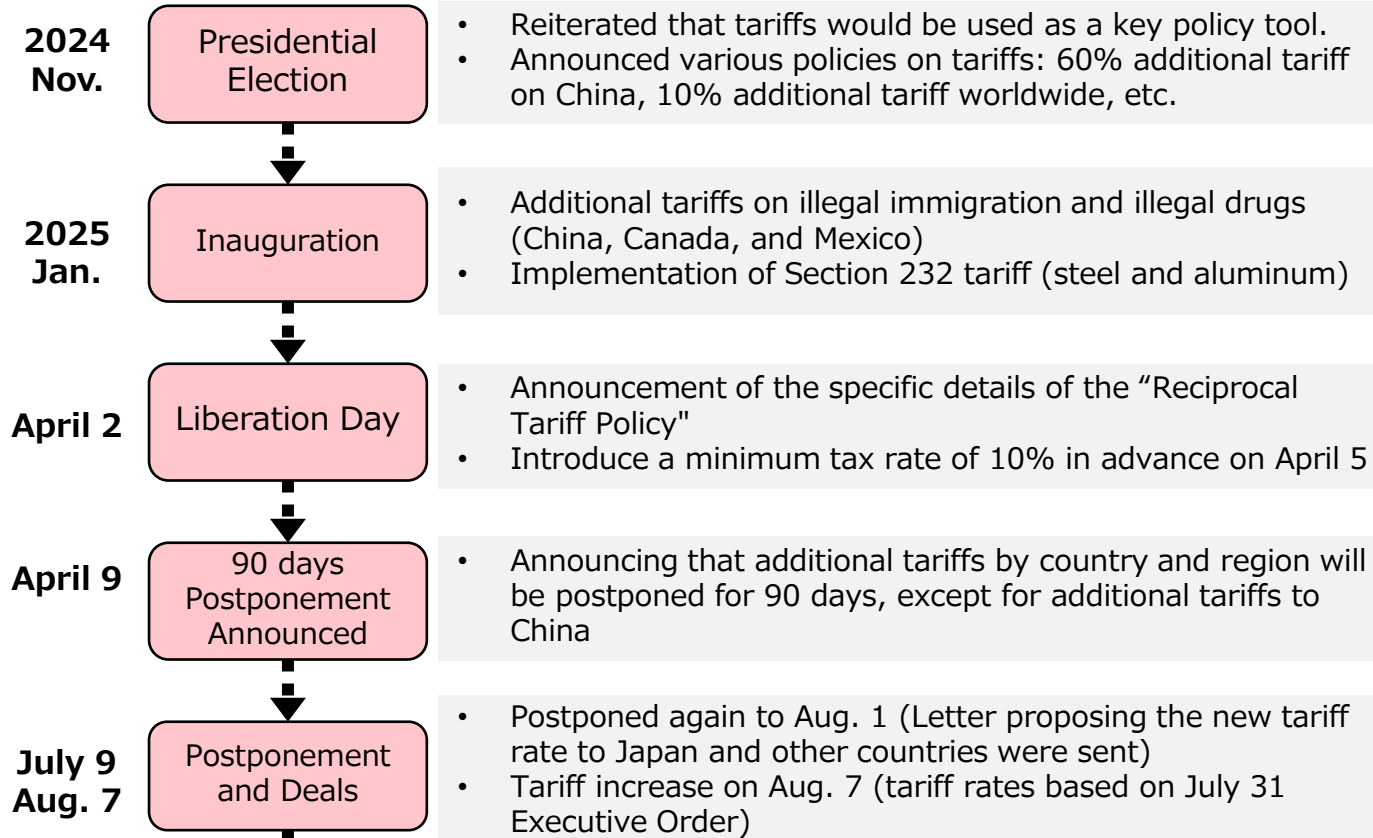
**Commodity market:** Downward pressure due to the economic slowdown is generally strong on many commodities, while copper, which is underpinned due to digitalization demand, is expected to remain relatively stable.

\*Composition of each group and region is based on that of the IMF. ASEAN-5 refers to Indonesia, Malaysia, Thailand, the Philippines and Singapore. Global share is calculated on a (PPP) basis. The range of revision is based on comparison with our institute's forecast as of Feb. 2025, which assumed additional tariffs of 10% worldwide and 60% to China.

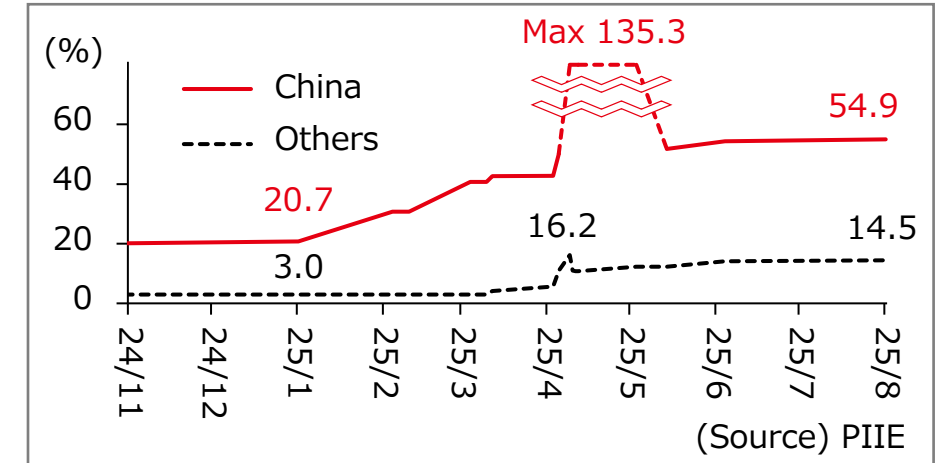
(Source) Marubeni Institute

# Trade negotiations: Review

## Additional tariffs were broadly implemented regardless of the existence of deals



▽ U.S. average effective tariff rates



.....▶ Stock prices, dollar, and U.S. treasury bonds simultaneously plummet.

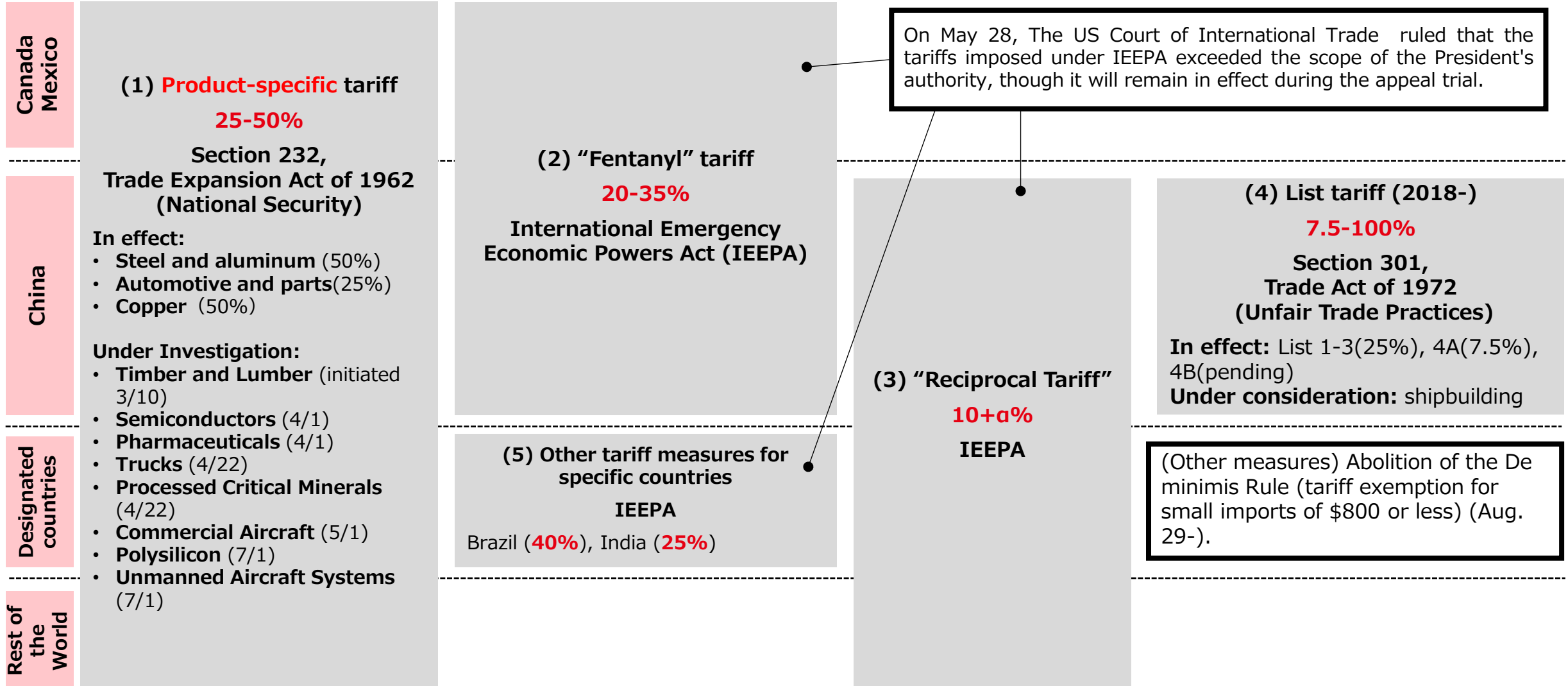
.....▶ The U.K., Japan, ASEAN, EU, etc. announced agreements.  
The U.S. and China agree to postpone tariff measures again (until Nov. 10)

### What's Next

- U.S.-China negotiations (Trump-Xi meeting at APEC and/or G20 summits)
- Negotiations with no-deal countries (e.g. India, Brazil, Taiwan, Switzerland, South Africa)
- Article 232 Tariffs (semiconductors, pharmaceuticals, wood, trucks, critical minerals, commercial aircraft, polysilicon, drones)

# Trade negotiations: Trump tariffs overview

## Multi-layer tariff measures complicates U.S. trade barriers



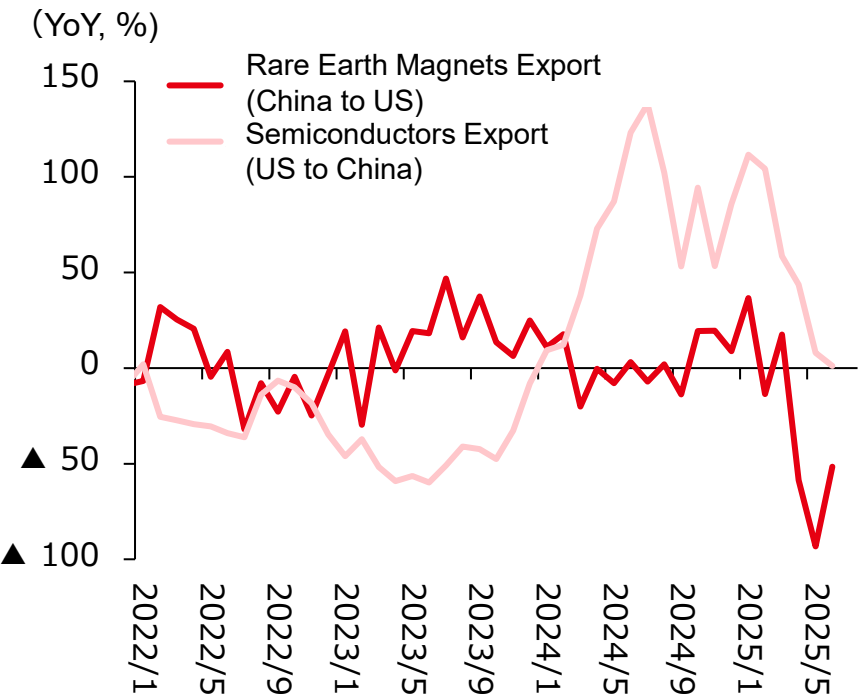
(Source) White House

# Trade negotiations: U.S. and China

## Trade talks stuck as neither side have strong motivation to continue

- The United States and China held their third trade negotiations at the end of July, extending the tariff pause for 90 days. Rare earth exports have become a bargaining card for China, leading to the U.S. side considering extending the suspension of extremely high tariff rates and partially easing semiconductor export restrictions.
- Tariffs on China continue to exceed 50% on an average effective tariff rate, and China's exports to the United States have declined significantly since April. There is a possibility that a summit meeting is reached and a certain thaw can occur by the end of the year. Yet, even if such a political rapprochement is achieved, the stalemate in trade negotiations is expected to continue. In the long term, both the United States and China will intensify “De-risking” strategy, the efforts to reduce economic dependence on the opponent.

### ▽Rare Earth Magnets & Semiconductors



(Source) ITC, General Administration of Customs of China

### ▽The Outlook of U.S.-China Relations

	Outlook		Impact on the economy and industry
	China	US	
Tariff	Continued suspension of additional tariffs		<ul style="list-style-type: none"><li>• High tariffs on China weigh on its external demand</li><li>• The rise in U.S. tariffs on countries other than China has reduced the need for detoured exports and production transfers.</li></ul>
Minerals	Turning into a bargaining card and maintaining export controls	Supporting the purification and separation of heavy rare earths and the production of rare earth magnets	<ul style="list-style-type: none"><li>• The supply shortage of critical minerals continues. Widely influenced by steel alloys, motors, semiconductors, etc.</li><li>• In the medium to long term, it is likely that dependence on China will continue to decrease..</li></ul>
Technology	Strengthening export controls on critical refining and manufacturing technologies*	Partial relaxation of semiconductor export restrictions to China	<ul style="list-style-type: none"><li>• Technology exports and production transfers from China stagnate</li><li>• In the medium to long term, the export regulation of advanced semiconductors to China is strengthening. China moves to in-house production</li></ul>

\*Gallium refining and battery cathode material production

(Source) Marubeni Institute

# Trade negotiations: Deals with UK, Japan, EU and South Korea

Commitments to US Investment amount to \$1.5 Trillion in total with no practical scheme explained

	U.S. tariff-related contents	Other contents
<b>UK</b>	<ul style="list-style-type: none"> <li>Reciprocal tariff 10%</li> <li>Automobile tariff 10% (MFN * tariff 2.5% + 7.5%, allocation of 100,000 units per year)</li> <li>Designing a duty-free quota for aluminum and steel tariffs (details not yet announced)</li> <li>Additional tariff exclusions for aerospace products</li> </ul>	<ul style="list-style-type: none"> <li>"Supply Chain Security" Provisions for Steel, Aluminum, Pharmaceuticals, etc. (designed to exclude Chinese companies from the US-UK supply chain.)</li> <li>Tax-free quotas for beef and ethanol imported from the United States, etc.</li> </ul>
<b>Japan</b>	<ul style="list-style-type: none"> <li>Reciprocal tariff 15% (MFN tariff included, MFN tariff rate is MFN tariff for anything over 15)</li> <li>Automobile tariff 15% (MFN 2.5% + 12.5%)</li> <li>Semiconductor and pharmaceutical tariffs agreed to "not be inferior to other countries"</li> </ul>	<ul style="list-style-type: none"> <li>In nine areas of importance for economic security, government-affiliated financial institutions (JBIC*, NEXI*, etc.) will provide investment, loans, and loan guarantees of up to \$550 billion for investment in the United States. The profit distribution ratio of Japan and the United States in the investment is 1:9.</li> <li>Expansion of imports of U.S. agricultural products, semiconductors, aircraft, defense equipment, LNG, etc. Alaska LNG project consideration. * U.S. side announced: 75% increase in U.S. rice imports</li> <li>Approval of the U.S. Federal Motor Vehicle Safety Standard (FMVSS). Appropriate review of the operation of clean energy vehicle subsidies</li> </ul>
<b>EU</b>	<ul style="list-style-type: none"> <li>Reciprocal tariff 15% (MFN tariff included, MFN tariff for items exceeding 15%) Automobile, pharmaceutical, and semiconductor tariff 15% (MFN 2.5% + 12.5%)</li> </ul>	<ul style="list-style-type: none"> <li>\$600 billion in new investment in the United States.</li> <li>\$750 billion in U.S. energy imports by 2028.</li> <li>Mass purchase of US-made military equipment.</li> <li>Responding to digital trade barriers and reviewing hygiene certifications for pork and dairy products.</li> </ul>
<b>South Korea</b>	<ul style="list-style-type: none"> <li>Cross-taxation 15%</li> <li>Automobile tariff 15% (MFN 2.5% + 12.5%)</li> <li>Semiconductor and pharmaceutical tariffs agreed to "not be inferior to other countries"</li> </ul>	<ul style="list-style-type: none"> <li>Investment in the United States of \$350 billion (\$150 billion in shipbuilding, \$200 billion in semiconductors, nuclear power plants, secondary batteries, biotechnology, etc.). The U.S. government is responsible for purchasing the products.</li> <li>\$100 billion in U.S. energy imports.</li> </ul>

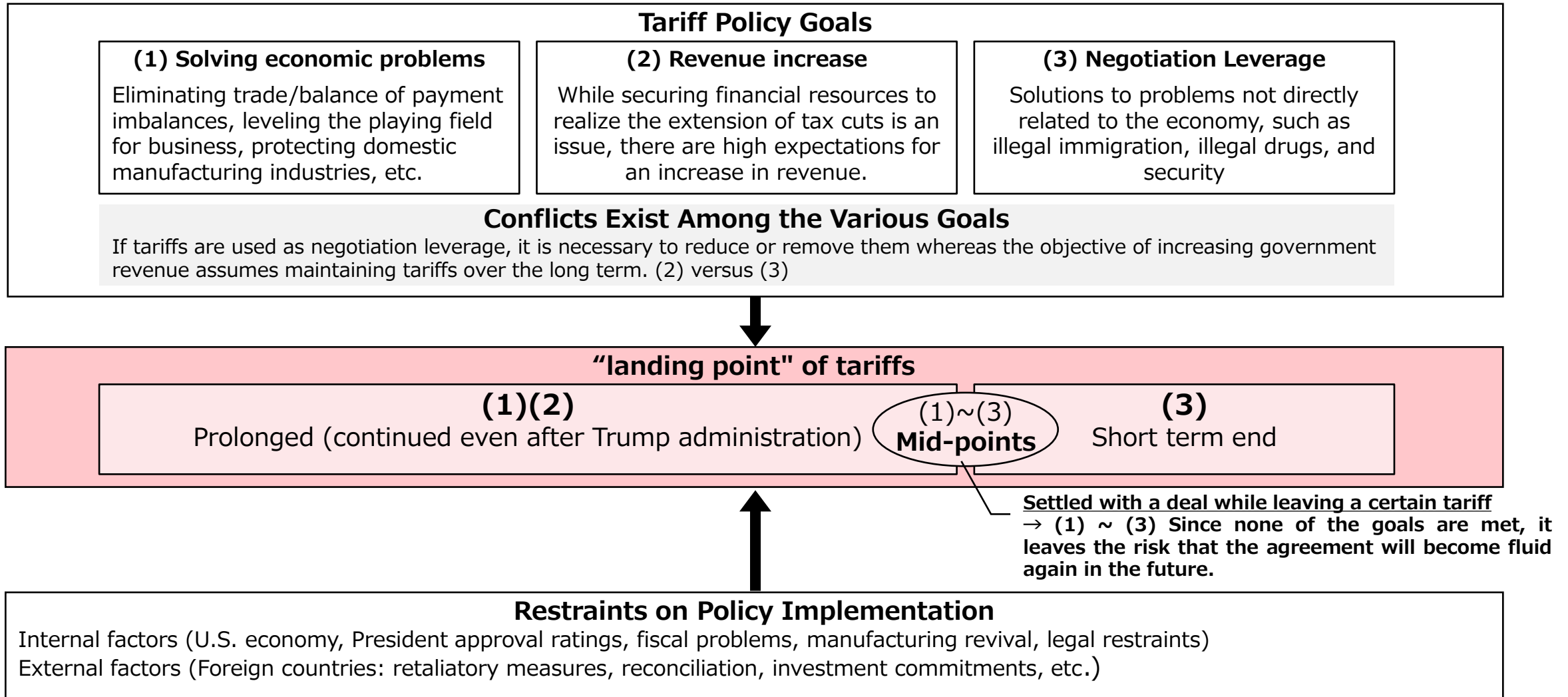
- Global direct investment stocks in the U.S.: \$5.7 trillion (UBO\* basis, the end of 2024), +6.2% YoY (+\$333.2 billion)
- Japan's direct investment stocks in the U.S.: \$819.2 billion (UBO basis, the end of FY2024) ● Exports to the U.S.: \$141.6 billion (FY2024) ● Imports to the U.S.: \$85 billion (FY2024)
- JBIC's loan balance: 15.8 trillion yen (\$105.7 billion, March 2025) ● Guaranteed balance: 1.3 trillion yen (\$8.9 billion) ● Loan guarantee approval: 1.5 trillion yen (\$10.1 billion, FY2024)
- EU direct investment stocks in the U.S.: \$2.2 trillion ● South Korea's direct investment stocks in the U.S.: \$93.2 billion ● EU energy imports from the U.S.: \$83 billion (2024)
- Japan's rice MA\* quota: Of the 770,000 tons in the MA quota, 350,000 tons are imported from the U.S.. The others are from Thailand (290,000 tons), Australia (70,000 tons), China (40,000 tons).

\*MFN (MFN), JBIC (Japan Bank for International Cooperation), NEXI (Nippon Export and Investment Insurance), MA (Minimum Access), UBO (Ultimate Beneficial Owner)  
(Source) White House, U.S. Department of Commerce, Japan's Ministry of Economy, Trade and Industry, JBIC, etc.

# Trade negotiations: Scenario and End State

Tentative "landing point" is likely to be in the middle of the different tariff measure goals

## ▽ Structure to determine the "landing point" of tariffs

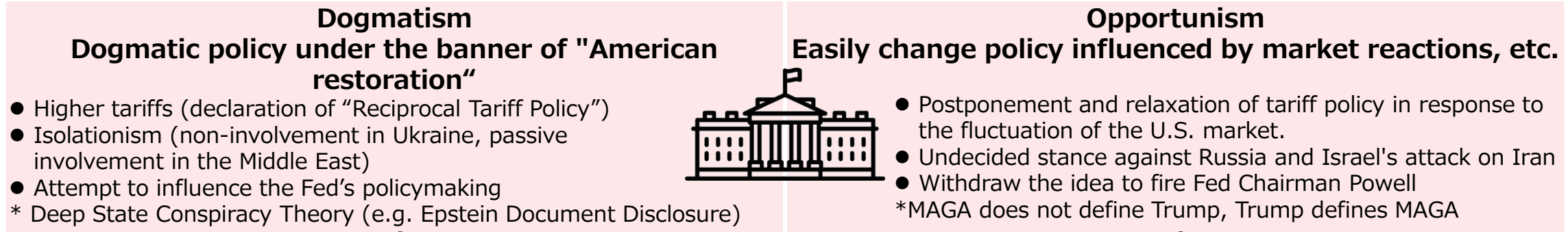




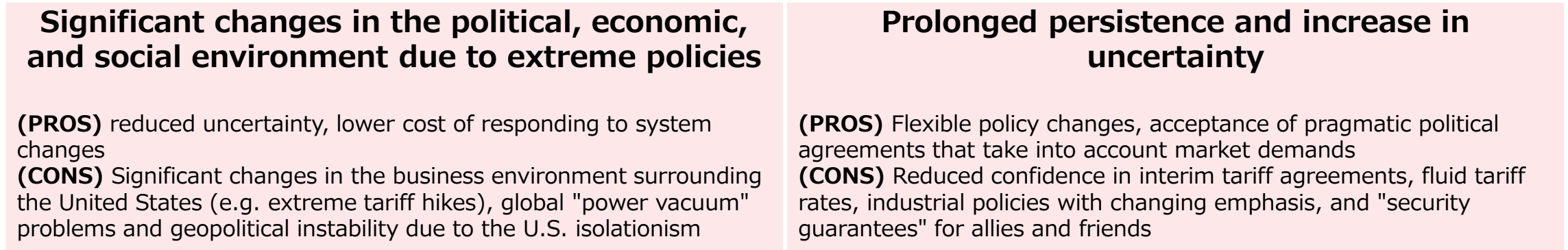
# Trump administration leans to Opportunism

## Less changes, more uncertainty

### ▽ Contradictory labels of Trump administration



### ▽ Risks related



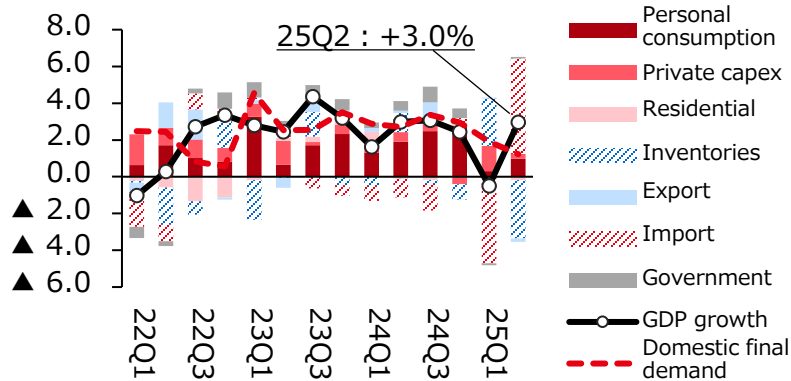
Leaning towards

# US Economy: Overview

## The U.S. economy is slowing but still on the course of Soft-landing

### ▽Real GDP growth

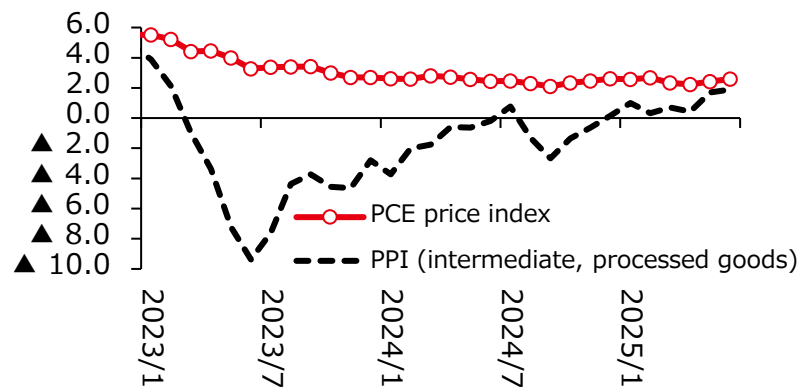
(QoQ%, seasonally adjusted annual rate)



(Source) U.S. Department of Commerce

### ▽Inflation

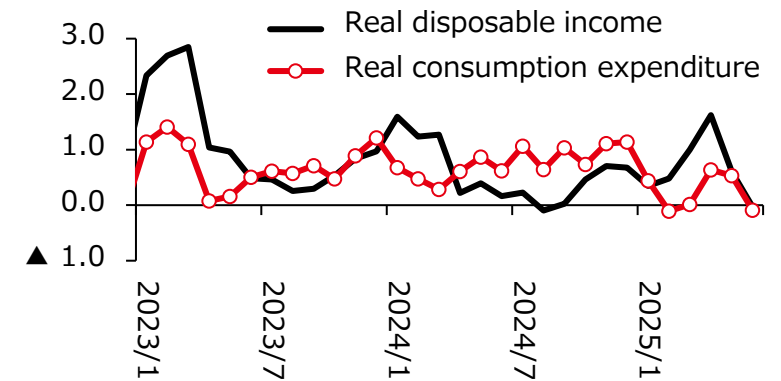
(YoY%)



(Source) U.S. Department of Commerce

### ▽Private Consumption

(YoY%, 3M moving average)

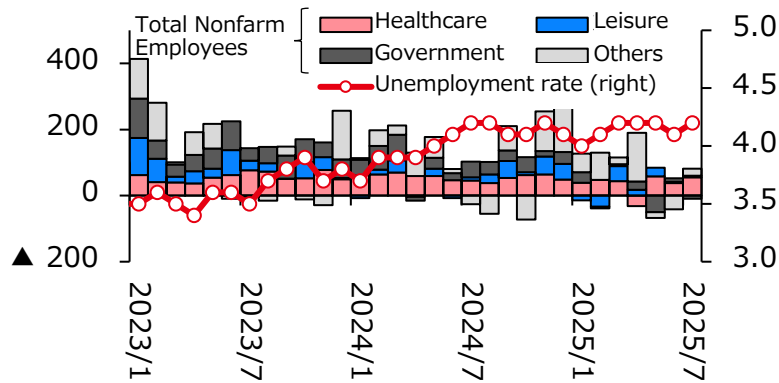


(Source) U.S. Department of Commerce

### ▽Labor Market

(QoQ, thousand, seasonally adjusted)

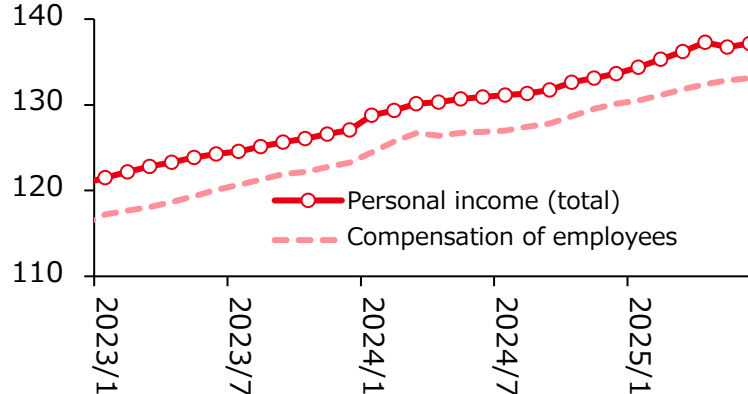
(%)



(Source) U.S. Department of Labor

### ▽Personal Income

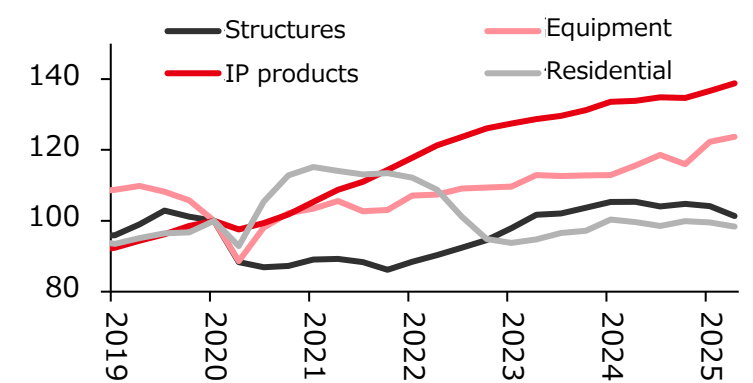
(2020/1=100, current)



(Source) U.S. Department of Commerce

### ▽Private Fixed Investment

(2020/1=100, constant)



(Source) U.S. Department of Commerce

# US Economy: One Big Beautiful Bill (OBBB)

In the short term, it will exert a certain economic stimulus effect, but fiscal soundness is far away.

## ▽OBBB Provisions

Individual Provisions	<ul style="list-style-type: none"> <li>Strengthening and making tax cuts for individuals during the first Trump administration (TCJA: originally scheduled to expire at the end of 2025)</li> <li>Permanentization of child support tax credit, primary expansion of tax credit for the elderl</li> <li>Expanding State and Local Tax (SALT) Deductions</li> <li>Elimination of tip taxation, overtime pay, and auto loan taxation (Tax year 2025~28, with upper limit on deduction), etc.</li> </ul>
Business provisions	<ul style="list-style-type: none"> <li>Permanent immediate depreciation of R&amp;D expenses in U.S.</li> <li>Immediate 100% amortization of manufacturing capital expenditures, etc. (subject to term)</li> <li>Permanentize tax credits on income from pass-through entities</li> <li>Revision and abolition of tax credit programs for EVs, clean energy, etc. under the Inflation Reduction Act (IRA)</li> </ul> <p>* The retaliatory tax regime (Section 899) targeting foreign companies and investors included in the House bill was removed after the G7 countries agreed to exempt U.S. companies from Global Minimum Tax (GMT) rules.</p>
Others	<ul style="list-style-type: none"> <li>International tax system: Tax rate increase on Global Intangible Low-Taxed Income (GILTI), Base Erosion and Abuse prevention Tax (BEAT), etc.</li> <li>Raising the federal debt ceiling by \$5 trillion</li> </ul>

## ▽Forecast of the effect on federal fiscal and economic growth

	Fiscal balance (2025-34 Cumulative, Trillion USD)			Real GDP growth rate (%pt)		
	Increase in primary deficits	Net Interest Outlays	Total	2028	2034	2054
Tax Foundation	▲3.0	▲0.7	▲3.8	+1.51	+1.25	+1.21
Tax Policy Center	▲3.1	▲1.1	▲4.2	+0.34	+0.51	+0.60
University of Pennsylvania	▲3.6	—	—	—	▲0.30	▲4.60
Budget Lab at Yale	▲3.1	▲1.7	▲4.8	+0.51	▲0.21	▲3.31

(Source) Tax Foundation Tax Policy Center, Pennsylvania Univ., Yale Univ.

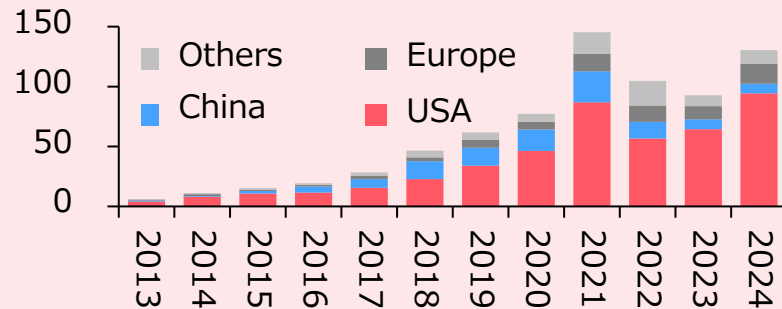
# US Economy: The Economic Impact of AI Investments

**Solid CAPEX supports economy in the short-term while several risks are in the long-term**

## ▽ Current

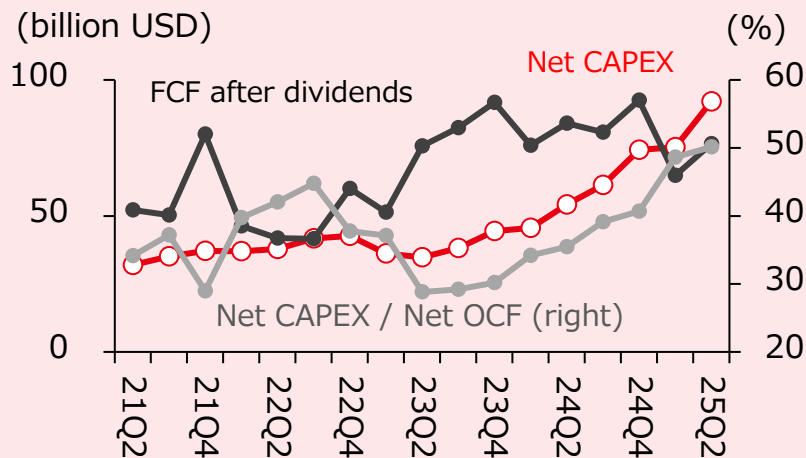
### ▽ Private AI Investment

(billion, constant 2021 USD)



### ▽ US Tech Companies' CAPEX

(billion USD)



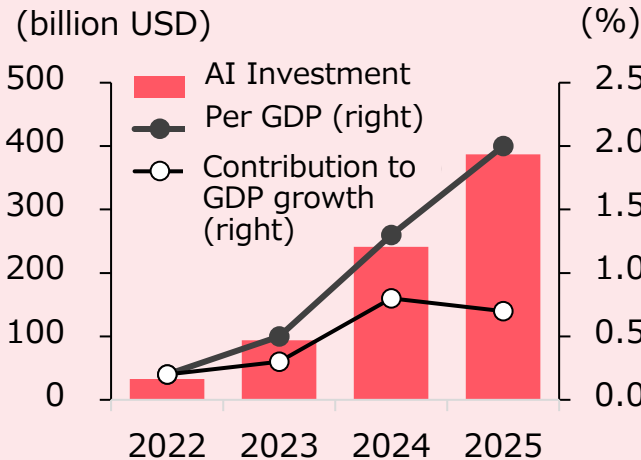
\*total CAPEX of GAFAM and NVIDIA (including CAPEX outside US)

## ▽ Short-term

**Solid growth in AI investment is a short-term positive impact on macroeconomic trends**

- US AI investment is expected to rise to 2% of GDP in 2025 (pushing up GDP by 0.7%pt). Driving capital investment while other industries are weakening.

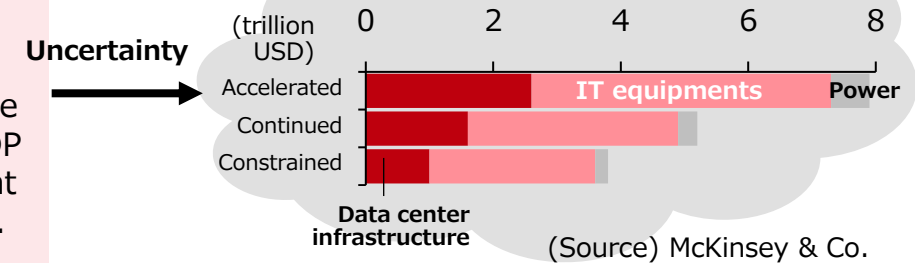
### ▽ U.S. AI Investment and Its Impact on GDP



※Exante Data estimate

## ▽ Long-term

### ▽ AI-related Data Center Investment (World, 2025-30)



(Source) McKinsey & Co.

### < Risks surrounding AI-related investments >

#### ● Innovation

While the smooth development of AI-related technologies is accompanied by uncertainty, new technologies may make existing technologies obsolete

#### ● Overinvestment

Overcapacity due to rapid increase in DC and power infrastructure amid uncertain computational demand and electricity demand forecasts

#### ● Productivity

Retreat of excessive expectations for productivity improvement due to stagnation of utilization and implementation in real business

#### ● Labor market

Labor substitution through the introduction of AI, widening employment and income disparities, and hollowing out the middle class

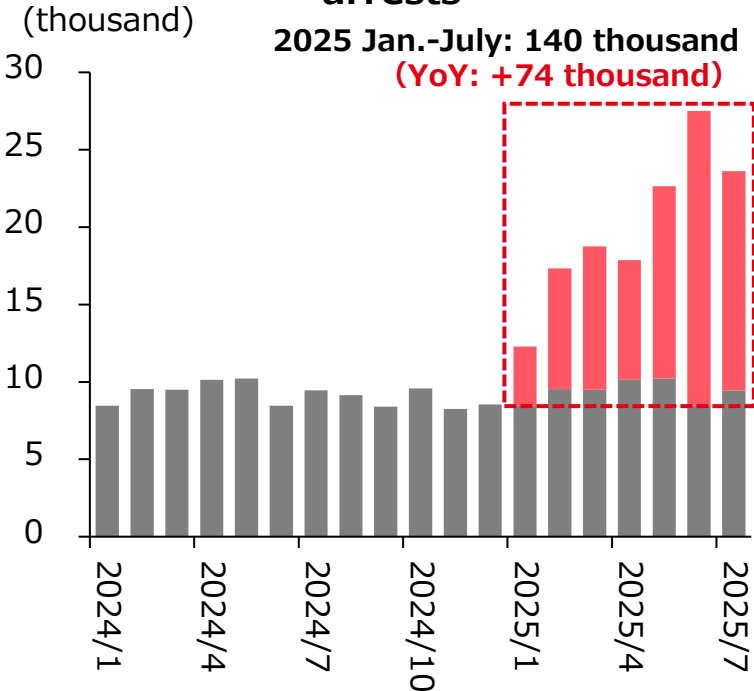
# US Economy: Trump 2.0 and Labor Market Risks

## Illegal immigration regulations and government employee reduction measures

The Trump administration’s illegal immigration regulations and government employee cuts are likely to destabilize the U.S. labor market from both supply and demand sides:

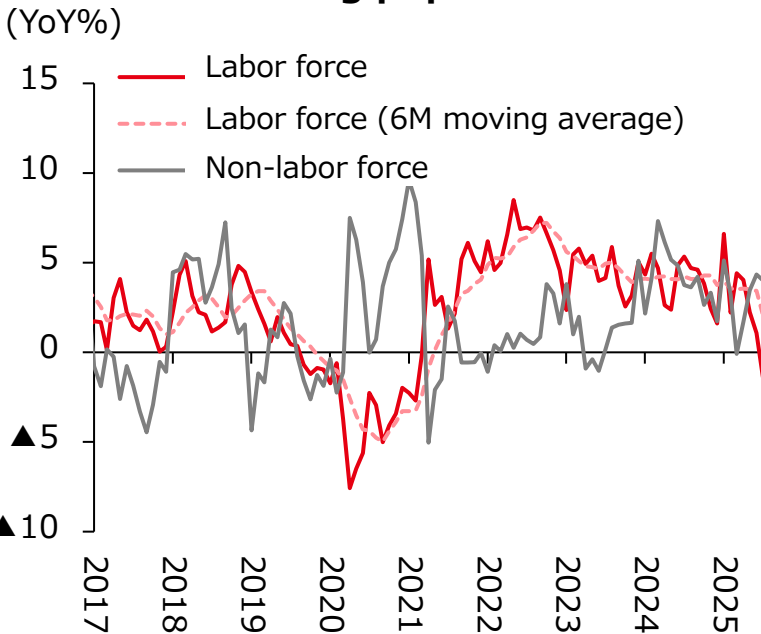
- **Crackdown on illegal immigration:** The number of illegal immigration arrests from January to July 2025 was 140,000, an increase of 74,000 compared to the same period last year as the crackdown is getting stricter.
- **Shrinking immigrant workers:** According to the U.S. Department of Labor’s survey (including illegal immigrants), the foreign-born working force in July fell below the previous year for the first time in more than four years. The stricter crackdown on illegal immigration is reportedly making some fear to show up in workplaces among immigrants.
- **Government employee reduction:** The number of federal government employees decreased by 77,000 YoY in July.

▽ Number of illegal immigration arrests



(Source) Deportation Data Project

▽ Foreign-born working and non-working population



(Source) US Labor Department, Current Population Survey (CPS)

▽ Reduction of government staff

(thousand)	July 2025	July 2024	YoY (thousand)
Non-farm Employees	159,227	157,771	+1,456
Private	136,877	135,580	+1,297
Government	22,350	22,191	+159
Federal	2,938	3,015	▲77
State	5,176	5,102	+74
Local	14,236	14,074	+162

(Source) US Labor Department

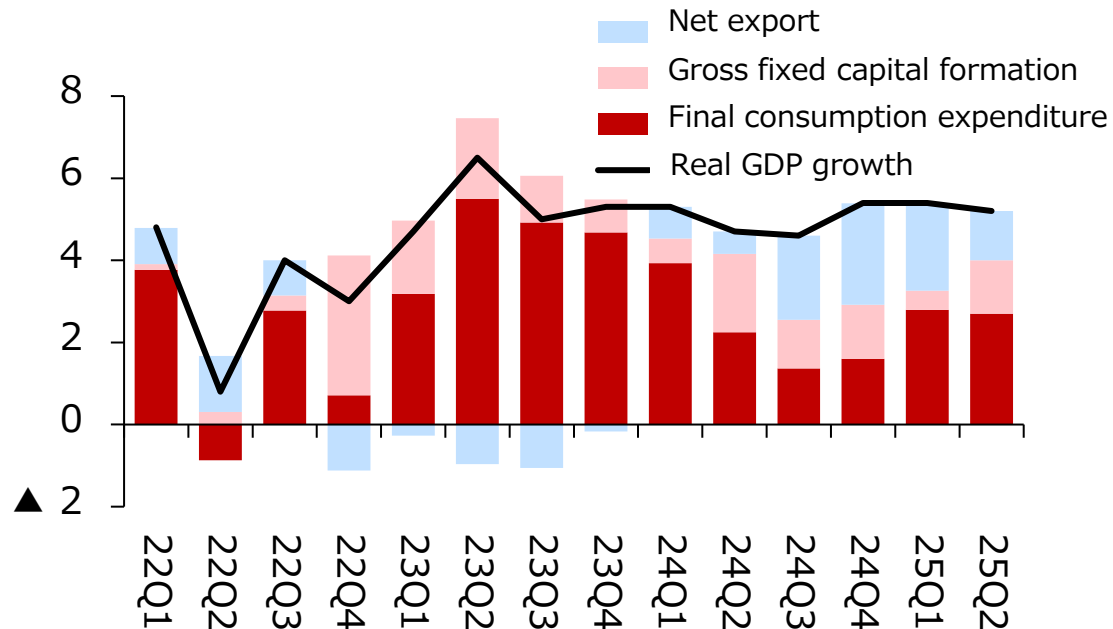
# China's Economy: Overview

## Slow down concerns persist amongst Housing recession and Trump tariffs

- **Current situation:** Real GDP growth in 2025Q2 slowed slightly to +5.2% YoY. The contribution to GDP growth of Final consumption expenditures were sluggish at +2.7%pts and that of net exports also shrunk to +1.2%pts due to the decrease of exports to U.S. Gross fixed capital formation increased its contribution to GDP growth to +1.3%pts with the government's stimulus program for equipment renewals.
- **Outlook:** Private consumption is expected to remain broadly stable. By contrast, fixed-asset investment will likely be dragged down by a protracted slump in housing market and the excess capacity problem. U.S. tariff rates on China remain high despite the May trade truce, and continued weakness in exports to the United States will further weigh on China's economic growth. Against this backdrop, GDP growth in 2025 is projected to slow to around 4%.

### ▽Real GDP Growth

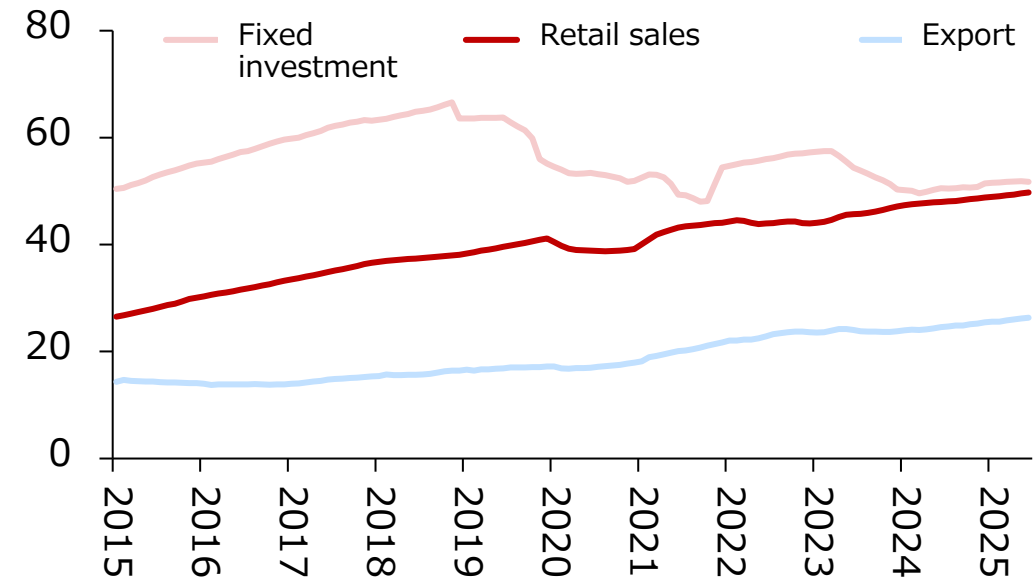
(YoY%, Contribution to GDP growth %pt)



(Source) National Bureau of Statistics of China

### ▽Key Economic Indicators

(12M moving total, trillion CNY)



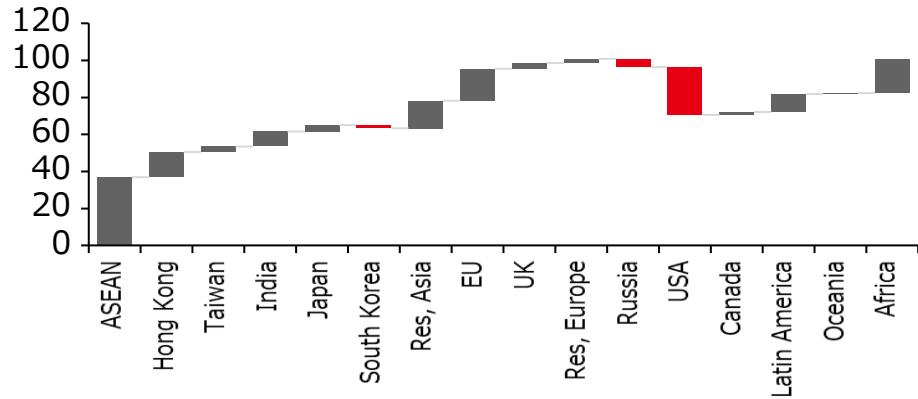
(Source) National Bureau of Statistics of China, Customs General Administration, WIND

# Is China really Exporting “Deflation”? (1)

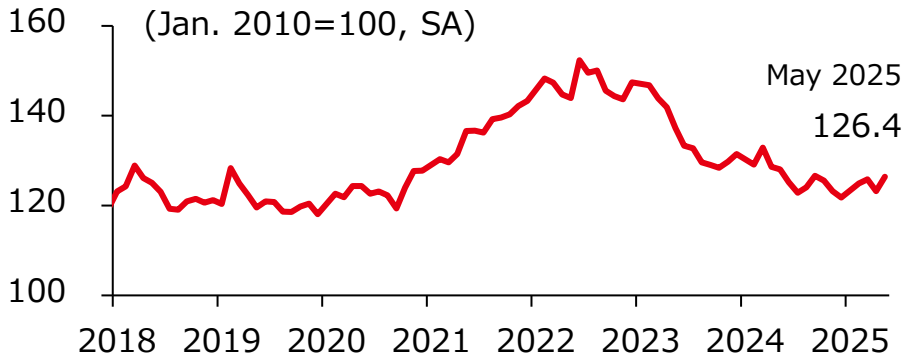
Headline export price is not significantly down while specific sectors face cheap Chinese goods

(1) China Export (25H1, YoY)

(billion USD)



(2) China Export Price



● While the headline export price has not declined since the mid-2024, Significant price down have been reported in certain items such as steel, solar panels, automobiles, plastics, apparel.

<25H1>

United States

Tariff measures

(1) Export Down

China

(1) Export Up  
(2) Export price Down?

(4) Trade friction

Non-US

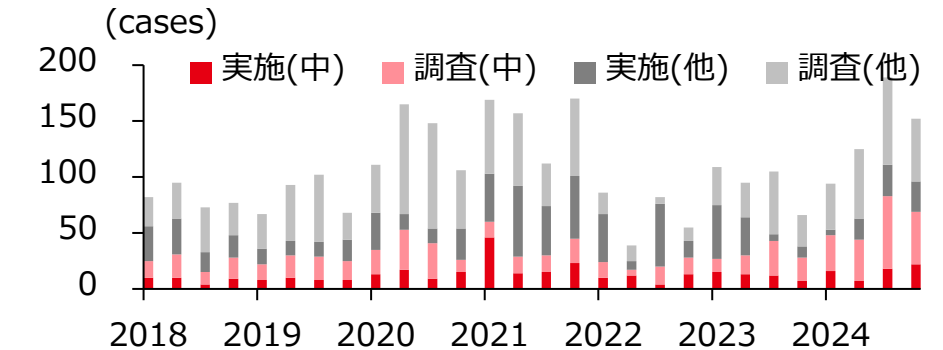
(3) Export Up

(3) Non-US import/export (Jan.-May 2025, YoY)

(billion USD)	(1)	(2)	(1)	(2)
World	+70.0	+200.2	South Korea	▲1.4 ▲2.9
Vietnam	+12.4	+20.8	Japan	+2.6 +1.4
Thailand	+6.5	+6.8	Taiwan	+2.8 +24.3
Indonesia	+4.2	+3.0	Australia	▲0.5 +9.4
Malaysia	+2.0	+4.9	Brazil	▲0.9 +1.4
Philippines	+1.3	+1.2	Chile	+2.1 +2.3
Cambodia	+1.4	+0.7	Mexico	▲0.3 +12.6
Laos	+0.1	+0.8	Canada	+1.7 ▲2.9
India	+7.0	+9.7	Turkey	+0.3 ▲0.1
Bangladesh	▲0.8	+0.7	South Africa	+0.2 +3.6

(1) Import from China, (2) Export to US. Highlight: (1)>(2)

(4) WTO Anti-Dumping Investigation /Implementation



● Regulations on cheap e-commerce business such as Temu and SHEIN ● Anti-dumping measures for steel products



# Is China really Exporting “Deflation”? (2)

## Typical export shift from US to ASEAN / China's total export increased

▽ Exports to China in the first half of '25 (highlight export destinations with a year-on-year change of more

million USD			25H1	24H1	25H1-24H1	YoY(%)	Goods (YoY, million USD)	
Total			1,810,879	1,710,352	+100,527	+5.9		
Asia			913,559	835,308	+78,251	+9.4		
	ASEAN		323,137	286,192	+36,944	+12.9		
		Vietnam	93,341	78,195	+15,146	+19.4	Home appliances (6,568) Home appliances (1,713) Home appliances (2,316) Home appliances (1,300) Transport equipment (999)	Electric equipment (4,656) Transport equipment (1,627) Electric equipment (1,444) Electric equipment (1,155) Mineral fuels (▲1,228)
		Thailand	50,623	41,483	+9,139	+22.0		
		Indonesia	40,603	35,281	+5,322	+15.1		
		Malaysia	51,803	48,573	+3,230	+6.7		
		Philippines	28,092	26,265	+1,827	+7.0		
		Singapore	41,310	40,877	+434	+1.1		
		Hong Kong		150,842	137,270	+13,572		+9.9
	India		65,294	57,302	+7,992	+13.9		
	Japan		77,761	74,161	+3,600	+4.9	Electric equipment (1,246)	N-reactors, Boilers (1,708)
	Taiwan		39,080	36,065	+3,015	+8.4	Electric equipment (2,282)	N-reactors, Boilers (1,072)
	Bangladesh		10,986	11,856	▲869	▲7.3	Chemicals (▲1,708)	Base metals (▲1,307)
	South Korea		71,102	72,864	▲1,761	▲2.4		
Saudi Arabia		26,986	23,835	+3,150	+13.2			
Oceania			42,624	41,978	+646	+1.5		
Europe			370,253	352,126	+18,127	+5.1		
	EU	267,537	250,376	+17,161	+6.9	Home appliances (4,369)	N-reactors, Boilers (3,149)	
	United Kingdom	40,365	37,267	+3,098	+8.3	Home appliances (1,032)		
	Russia	47,197	51,722	▲4,524	▲8.7			
	North America			239,996	264,149	▲24,153	▲9.1	
	United States	215,632	241,491	▲25,859	▲10.7	Home appliances (▲12,798)	Electric equipment (▲7,045)	
	Canada	24,224	22,515	+1,709	+7.6			
Latin America	*including Mexico		141,327	131,783	+9,543	+7.2		
Africa			103,049	85,007	+18,042	+21.2		

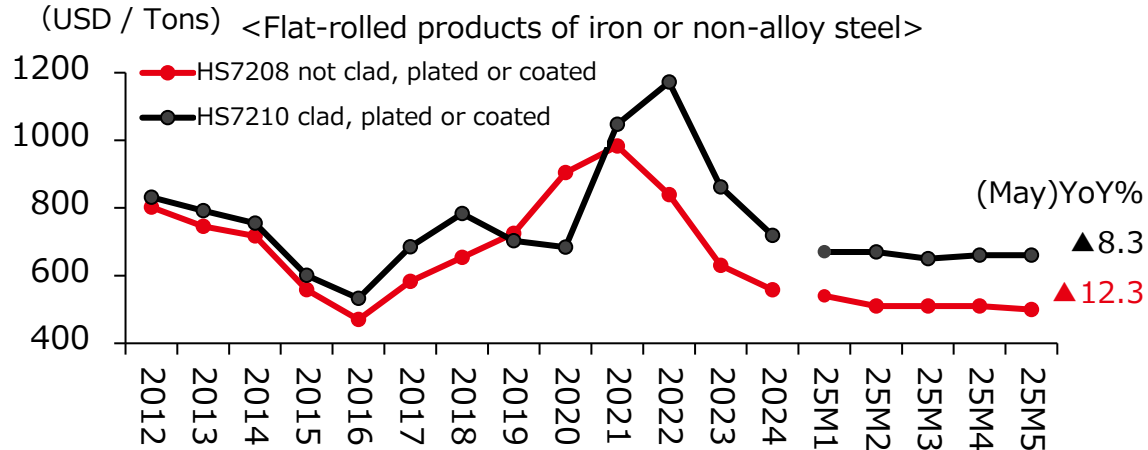
(Source) General Administration of Customs of China



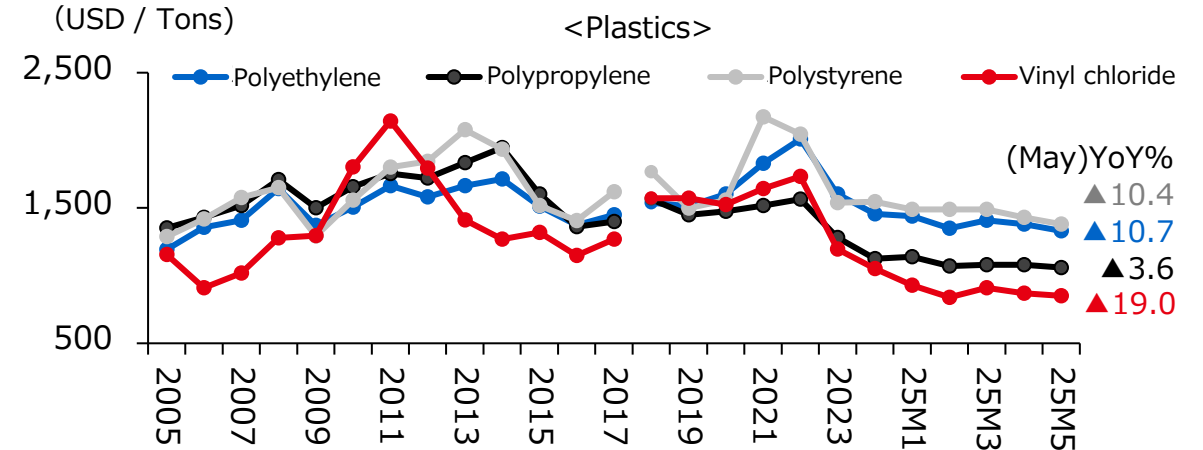
# Is China really Exporting “Deflation”? (3)

Prices of certain items continue to decline significantly.

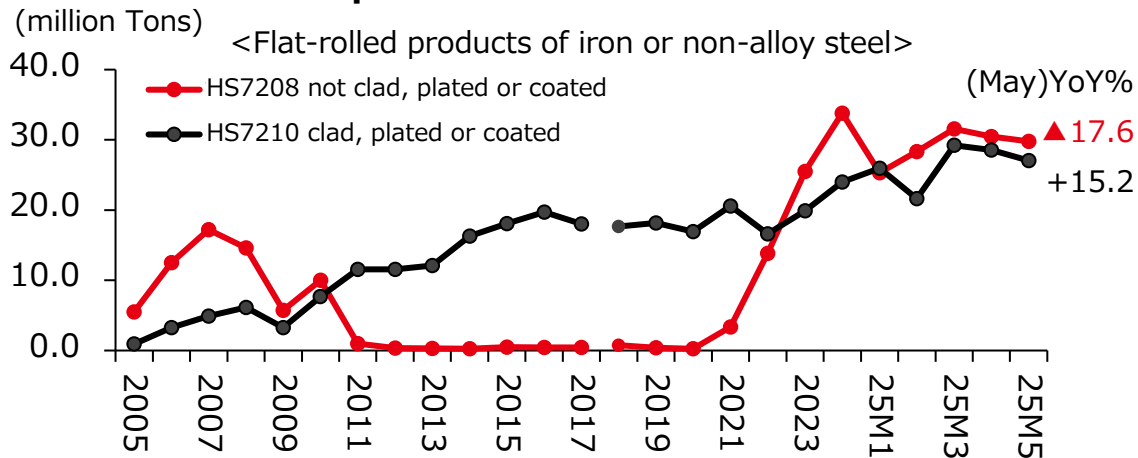
## ▽ Export price from China



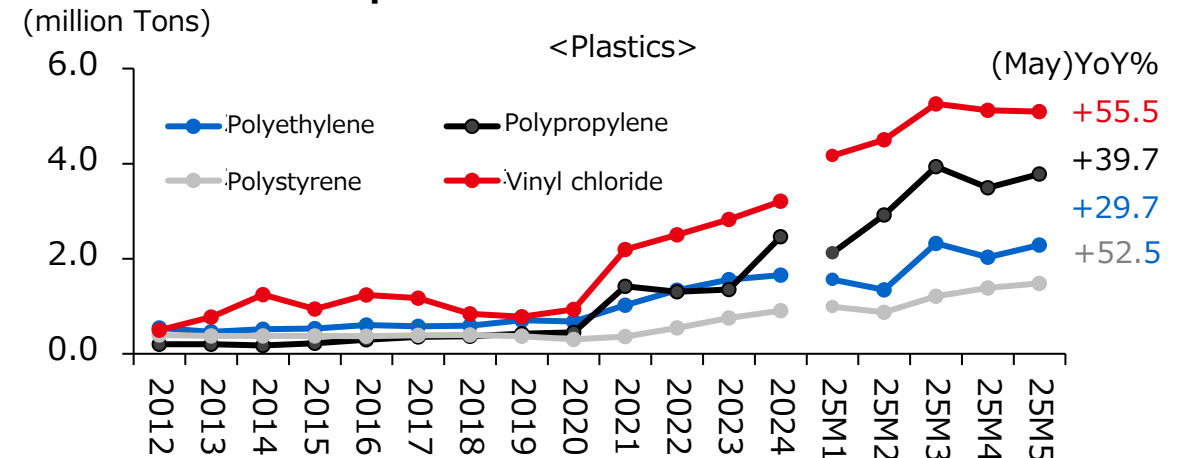
## ▽ Export price from China



## ▽ Export value from China



## ▽ Export value from China



\*vinyl chloride (HS3904), polypropylene (3902), polyethylene (3901), polystyrene (3903)

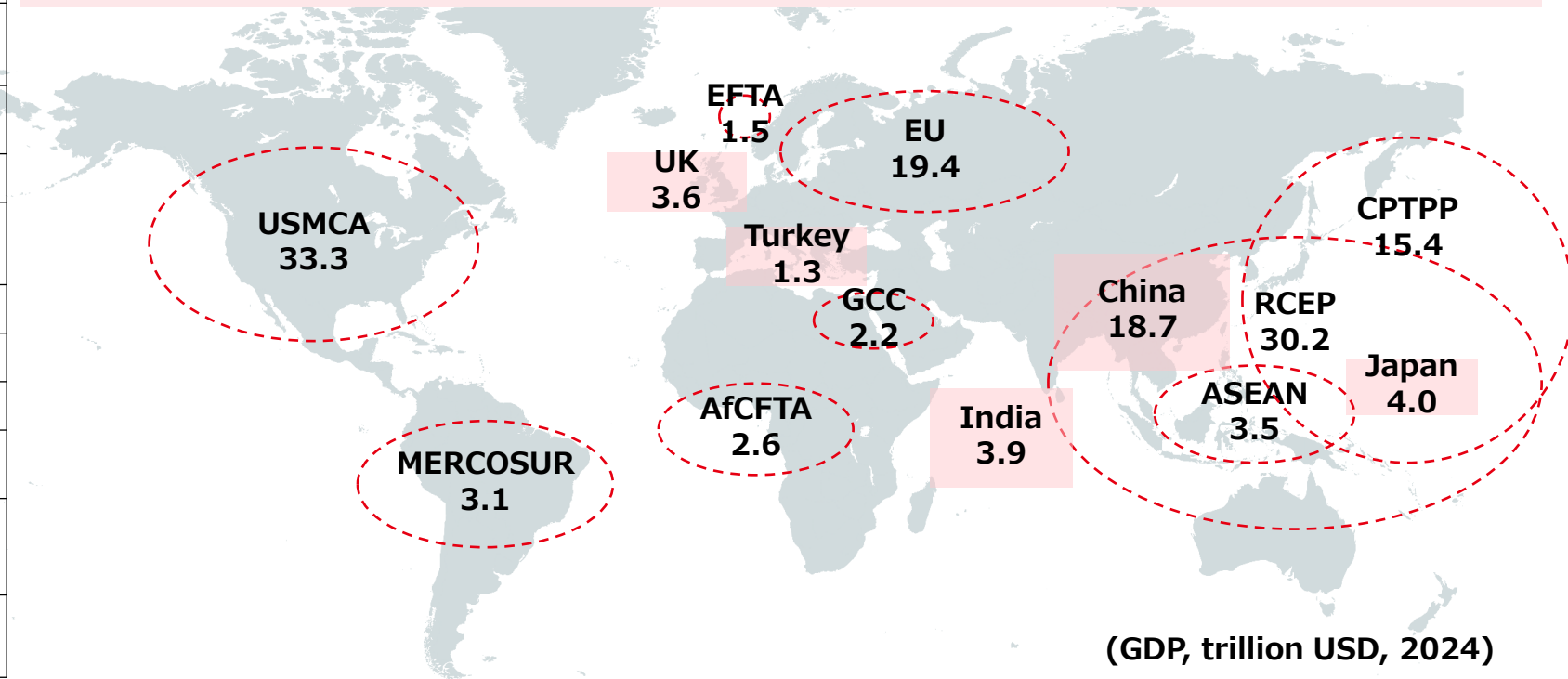
# “Paradoxical Globalization” as hedging Trump risks

As the risk of US market rises, countries seek for Plan B in non-US markets

## ▽ FTA/EPA

Agreed / Signed	EFTA / Thailand	2025/1 signed
	UAE / Malaysia	2025/1 signed
	UK / India	2025/7 signed
	EFTA / Malaysia	2025/6 signed
	EU / Indonesia	2025/7 agreed
	EFTA / MERCOSUR	2025/7 agreed
In Negotiations	EU / Thailand	(goal) agreed by the end of 2025
	EU / Malaysia	Restarted in Jan. 2025
	EU / Philippines	Restarted in Oct. 2024
	EU / India	(goal) agreed by the end of 2025
	EU / Australia	Started in Apr. 2025
	EU / UAE	Started in Apr. 2025
	NZ / India	Started in Mar. 2025
	GCC / Malaysia	Started in May 2025
	MERCOSUR / Vietnam	(goal) politically agreed by the end of 2025
	Canada / ASEAN	(goal) politically agreed by the end of 2025

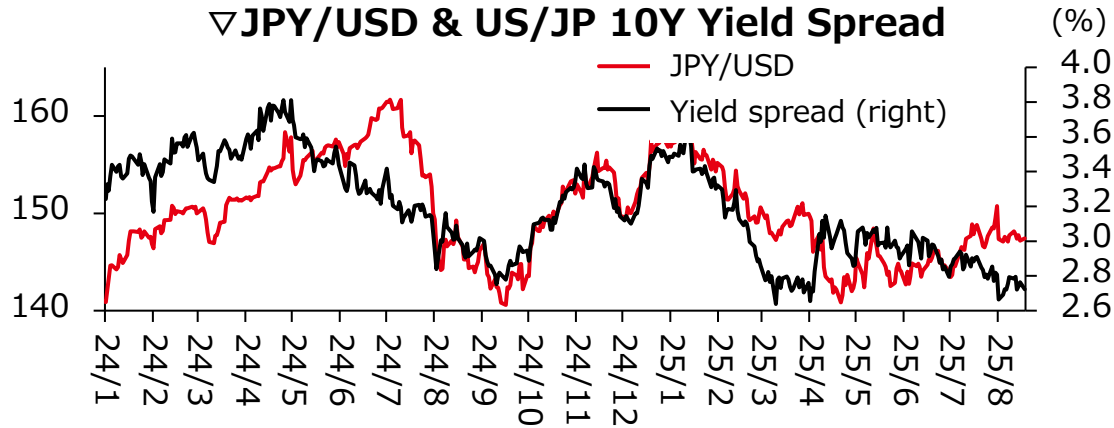
- **Paradoxical Globalization:** The destabilization and increase in costs of trade with the United States due to the Trump administration's tariff policy may ironically accelerate the development of non-US trade markets. This trend can be coordinated with certain countries' economic strategy such as India (manufacturing exports), ASEAN (export destination diversification) and GCC countries (growth of non-oil economies).
- **Not straight road, though:** India's caution about opening up the domestic market is deeply-rooted, and emerging countries are also facing challenges in meeting the environmental standards required by the EU. Japan is trying to expand multilateral frameworks such as the CPTPP and RCEP\*, but some countries are very wary of RCEP, which includes China as a member.



(Source) IMF

# “Fiscal Dominance” in JPY/USD Market

JPY/USD market after tariff deals will basically be range-bound, but there remains several risks



## Main Scenario

Fluctuations in FX market calmed down as major countries have made deals with the U.S. The outlook of JPY/USD is based on a range-bound market, but there are several risks.

## ▽Outlook for the Japanese and U.S. economies

	United States	Japan
Economy	Slowdown	Slowdown
Prices	Inflation (Tariff effect)	Inflation (Food price)
Monetary policy	Cautious Easing (50 bps cut during 2025)	Cautious Tightening (25 bps hike during by Mar. 2026)
Fiscal policy	Deficit increase (OBBB > Tariff revenue)	Goal of Surplus postponed (Basic Policy 2025)

## Highlight: Fiscal Dominance in both US and Japan

- Under Trump 2.0, the market began to reconsider the credibility to US dollar.
- In Japan, fiscal discipline has loosened under long-term monetary easing. As a result, Bank of Japan's rate hike can significantly increase the interest payment burden.
  - the impact of fiscal concerns on monetary policy and markets is increasing both in Japan and the United States (= Fiscal Dominance). Fiscal Dominance can weaken the correlated relations between U.S.-Japan interest rate gap and JPY/USD market.

## ▽Major Risks

**(JPY ↑) Risk-off:** Stock prices are moving in the high price range in countries and regions around the world, and the trend of risk-on is intensifying worldwide. On the other hand, if the market's optimistic scenario is significantly revised in the future, risk-off yen buying may intensify.

**(JPY ↑) US economy:** The July employment report showed signs of a change in the labor market. In the future, if the slowdown in the U.S. economy becomes clear, such as an unexpected rise in the unemployment rate, expectations for interest rate cuts by the Federal Reserve (Fed) will increase, and pressure on the yen will intensify.

**(JPY ↑) US inflation :** If inflation rises sharply due to the pass-on of tariff costs to the point where the Fed is forced to change its easing policy, risk aversion will take precedence over interest rate preference even as US interest rates remain high, and the pressure on the yen will intensify.

**(JPY ↑) US fiscal concern:** If U.S. fiscal concerns rise and uncontrollable interest rates rise, it will put pressure on the dollar to sell.

**(JPY ↓) Japan's economy:** Although the Bank of Japan maintains its interest rate hike policy, if it does not raise interest rates under the uncertainty of the impact of US tariffs on the economy, the pressure on the yen will intensify.

**(JPY ↑) Japan's inflation:** Against the backdrop of Japan's current high prices, if the expected inflation rate rises further and a rapid interest rate hike is forced, the pressure on the yen to appreciate will intensify.

**(JPY ↓) Japan's fiscal concern:** The proportion of overseas investors in the trading volume of ultra-long-term bonds has increased. If concerns about the stable digestion of government bonds increase, it will lead to yen selling pressure.



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