Global Macro Research

21 May 2025

5:58 minute read

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Japan-US trade talks: A roadmap

Following the US-UK deal and the 90-day reprieve on US-China tariffs, attention is turning to other potential deals. Japan is likely to offer concessions on tariffs and purchase agreements, while trying to keep deeper issues such as currency and defence off the table. Either way, trade uncertainty will keep the BoJ on hold for the rest of this year.

Key Takeaways

- Japan's negotiating stance with the US on tariffs has gradually become firmer, potentially emboldened by recent developments in US-China negotiations.
- Some concessions on the Japanese side are highly feasible. A reduction in Japanese tariffs on US imports, expanded purchase quotas, and increased investment in US-based production are all on the table.
- However, Japan is likely to maintain a tough stance on currency, defence, and regulatory standards. There was even a brief hint from the Japanese side about the potential to weaponise Japan's large holdings of US Treasuries in the negotiations. While this threat is extremely unlikely to be followed through, it is a signal that Japan could hold firm on key issues.
- Even if a framework agreement is finalised before the initial 90-day moratorium concludes in early July, the economic implications will remain uncertain.
- The BoJ and Cabinet Office will begin incorporating the parameters of any deal into their forecasts by the end of Q3, but the BoJ will likely treat these with caution.
- In our assessment, the uncertainty in forecasting is likely to postpone the next rate increase until at least January 2026.

Japan as a roadmap for other trade negotiations

Now that the Trump administration has managed to box tick one easy trade negotiation win (the UK) and make headway with the toughest negotiator (China), focus turns to the next group. Japan, South Korea and India were among the first to begin talks, with expectations that they will strike "deals" well before the first 90-day tariff moratorium expires.

Japan makes an interesting case study for the other nations. It is one of the closest economic and political Asian allies of the US, a large investor into US manufacturing, and occupies a central position in the global value chain.

Progress so far: An amicable start gives way to a more defiant stance

On 2 April, Japan faced a 10% universal tariff, a 24% country-specific "reciprocal" tariff, and a 25% tariff on autos and parts.

Japan did not retaliate like China and the EU. Instead, it dispatched a trade delegation to Washington and responded via domestic policy. Fuel and electricity subsidies, along with corporate financing support, were announced to counteract any economic hit.

By mid-April, the tone from US officials turned negative. Treasury Secretary Scott Bessent emphasized the need to address the weak yen, implying currency manipulation was at play.

The US-Japan security treaty was labelled as "one-sided" by President Donald Trump to maximise trade concessions and increase Tokyo's payments for defence.

But by early May, Japan and the US agreed to expedite tariff negotiations with the aim of agreeing a Memorandum of Understanding (MoU) by June, well ahead of the 9 July expiration of the 90-day reprieve.

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However, the tone from the Japanese side has since hardened. There were thinly veiled threats of using US Treasury holdings as leverage in trade talks, as mentioned in an interview by Finance Minister Katsunobu Kato.

Japan has also stressed that trade talks need to be kept separate from issues such as currency and defence.

US-China talks are likely to have emboldened Japan to push back on more aggressive calls from the US. Furthermore, China lifting the critical minerals export ban to the US will alleviate tension for Asian semiconductor manufacturers caught tiptoeing between US and China.

Next steps: Principal areas of discussion and waymarks to watch

At the time of writing, Japan's top trade negotiator, Ryosei Akazawa, was holding firm. Determined to protect the agricultural sector from US imports and pushing for full removal of all tariffs imposed, including autos and parts, as well as the baseline 10% "reciprocal" tariff. Akazawa was quoted by Bloomberg to have remarked that it would be "beneficial to communicate with other nations on tariffs". There is no evidence of regional coordination yet, however Japan is influential across APAC and could pose an additional challenge for the US if a number of countries were to coordinate a response.

Based on the current trajectory of talks, the principal areas of discussion are likely as follows:

Tariff reductions and/or quotas

US ask: lower Japanese tariffs and non-tariff barriers on US agricultural exports including rice, soy, corn, meat.

Japan possible concession: gradual tariff reduction or expanded quotas like what was offered in the Comprehensive and Progressive Agreement for Trans-Pacific Partnership (CPTPP) and EU-Japan EPA frameworks;

increased imports of US liquid natural gas (LNG) as well as plans to secure long-term investment in Alaskan LNG supply.

Auto sector concessions

US ask: more American-made auto imports and reduced reliance on Japanese car exports.

Japan possible concession: commitments to increase US-based production while pushing back on blanket tariffs on Japanese cars.

Agriculture and food safety

US ask: increased imports and looser sanitary and phytosanitary barriers.

Japan possible concession: potential increase in corn imports for ethanol fuel and biomass purposes given limited domestic production.

It is possible that US food safety standards are recognised for certain categories or that inspection protocols are streamlined. However, these measures are highly politically sensitive.

The farmer's lobby, JA-Zenchu, was particularly concerned about plans to import rice from the US, stating the imports would threaten long-term food security.

FX transparency

US ask: prevent currency manipulation and ensure a free-floating yen. Rumours of a multilateral currency accord reemerged following reports that South Korean and US officials met to discuss FX last week.

Japan possible concession: agreement to transparency of reporting and disclosures of any FX intervention should appease any doubts over free-floating nature of yen, but Japan remains highly unlikely to formally manipulate USDJPY to levels acceptable to US.

Supply-chain security

US ask: collaborate to reduce dependency on China and secure supply chains for semiconductors, rare earths and AI components.

Japan possible concession: there could be some joint projects and investment incentives offered to "friend-shore" some sensitive sectors, but rare earths remain a challenging ask.

Japan is walking a diplomatic fine line between China and the US here as it is dependent on China's supply of critical minerals.

Digital trade and data flow

Mutual interest: make this an area of strategic alignment rather than conflict. Both sides want open digital markets and data flows across borders especially financial services, cloud computing and AI development.

*Possible outcom*e: data-localisation mandates might be banned. Align with CPTPP- and USMCA-style digital provisions. Japan's domestic laws compatible with US privacy standards.

An important waymark will be who participates in discussions

Early discussions in April saw Japan's Chief Trade Negotiator Ryosei Akazawa and US Treasury Secretary Scott Bessant leading the respective teams.

However, in the latest APEC meeting Japan sent junior negotiators to meet with US Trade Representative Jamieson Greer, signalling little intention of meaningful talks.

When can we forecast with confidence?

Phase 1: the current landscape has limited visibility. Key variables are still unresolved, so macro forecasts beyond the next quarter remain speculative.

The Bank of Japan (BoJ) has flagged risks in either direction for the economic assumptions.

Phase 2: the period between June and September should bring greater clarity.

By this point some framework agreement is expected, which should bring clarity over the magnitude of tariffs, trade quotas, and initial plans for supply-chain security across chips and critical materials.

The government plans to submit additional economic stimulus measures ahead of the July upper house elections, which are expected to be implemented by autumn.

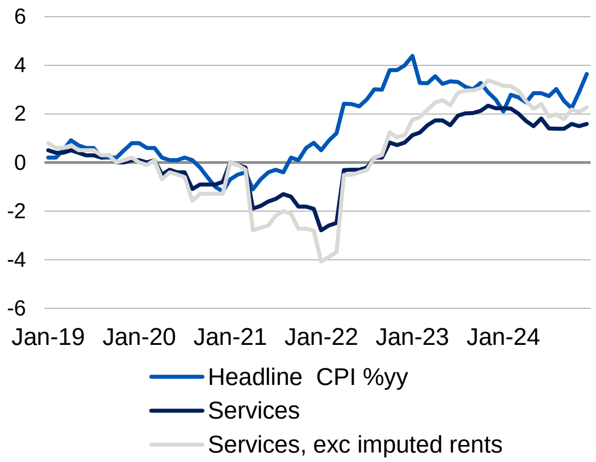
Phase 3: by late 2025 there should be greater forecasting confidence, especially if operational trade rules, tariff schedules, and enforcement mechanisms are in place.

The BoJ should at that point be able to start communicating a clearer monetary policy path.

Q1 GDP was weaker than consensus and contracted by 0.2% quarter over quarter. Consumption was flat, but net trade was a significant drag. However, business investment remained resilient. Structural demographic challenges have encouraged corporates to invest in labour-saving automation. Software investment accounts for about 10% of capex each year and should support growth over the coming years.

Going forward, GDP will also receive fiscal support in the form of a supplementary budget. Ahead of the upper house election on 22 July, there is increased pressure to lower consumption tax. These have historically proved difficult to reverse, so we expect the government to consider other fiscal measures such as support for households to counter inflation and to corporates to counter the tariff shock.

Figure 1: Headline inflation surges on food prices, although services inflation is gradually moderating



Source: Haver, Aberdeen, May 2025

Over the short term we expect a drag on growth from trade uncertainty, but the impact should be short-lived and shallow.

The outlook for medium-term inflation outlook will become clearer. Feedthrough of “Shunto” wage negotiations into realised wages and inflation will be clearer. Recent inflation pressures have been driven by food inflation while core services inflation remains subdued (Figure 1).

Carefully timing the next BoJ move

Amid this uncertainty, in the May monetary policy meeting Governor Kazuo Ueda stressed a lack of confidence in the central bank’s own forecasts. Credible growth and inflation forecasts are unlikely until a comprehensive trade framework with reciprocal and sector tariffs is agreed.

While the BoJ can begin incorporating deal parameters by the end of Q3, it is unlikely to rely on forecasts until at least Q4.

The domestic political timetable will also likely influence the timing of the next rate hike.

The upper house elections are due to be held in July. The Liberal Democratic Party (LDP) remains in the lead, albeit with weaker polling in recent weeks.

A supplementary budget is expected in autumn, while a budget bill is expected to be debated in December. The prospect of this deficit expansion, alongside building worries about the US fiscal position, are reasons why long-end JGB yields have been rising sharply in recent days. Demand has dropped against the backdrop of heavy long-end JGB issuance.

Either way, the economic package should be in place by January next year, providing a decent policy backdrop for the BoJ to consider hikes. The broad contours of a trade framework with the US should also be in place.

Overall, the timeline of tariff talks, domestic politics and fiscal timetable suggests the best time for the BoJ to resume hikes will be January 2026, when the accompanying forecasts in the Economic Outlook will help steer communication.

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AA-290525-194234-42

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