

# Navigating a Shifting Economic and Political Landscape

## *Dinner Speech at Deutsche Bundesbank Hamburg* 07 July 2025

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### 1. Foreword

Es ist mir eine große Freude und Ehre, hier heute in der schönen Hansestadt Hamburg vor Ihnen sprechen zu dürfen! Ich würde mir wünschen, meine Ansprache weiter auf Deutsch halten zu können. Um Ihnen aber meine Gedanken besser vermitteln zu können, werde ich nun auf Englisch fortfahren. (Thank you very much for your kind words. It is my pleasure and honor to speak to you here today in the beautiful hanseatic city of Hamburg. I wish I could go on with the speech in German. But in order to better convey my thoughts to you, I will now continue in English.)

First and foremost, I want to thank Uwe Nebgen, President of the Regional Office of Bundesbank in Hamburg, for helping me arrange my sentimental journey to the *Hansestadt*, where I was brought up as a young boy in the late 1960s. It is amazing that the wonderful time I spent with my family and friends remains still so vivid in my memory, when I cannot even remember what I had for breakfast this morning. Perhaps the beautiful sight of Lake Alster has downloaded memories stored deeply inside my brain.

At that time, the harbor was Hamburg's core industrial quarter with big flourishing shipyards. During this period the ship-building industry was also quickly rising in Japan, reaching almost half of global production in the mid-1970s, as **Chart 1** shows. But those days are long gone. By around 2010, Japan was completely overtaken by South Korea and China and lost competitiveness even for high value-added ships like LNG carriers. Japan also stopped building cruise ships. As a matter of fact, very recently, Nippon Yusen, one of the big three shippers in Japan, purchased a cruise ship from Meyer Werft named "Asuka III", which is now in the Port of Yokohama, waiting for her maiden voyage.

### 2. Implications of Trump 2.0

#### A move to a new global economic order

Let me first talk about what I see as implications of Trump 2.0 policies. With the arrival of President Trump in the Oval Office, we are undergoing a sweeping change in the global economic and political landscape. President Trump's policies seem to be driven by the recognition that the past globalization

did more harm than good to the US in that it created a powerful external competitor and resulted in persistent trade imbalances against the US, while internally, inequality widened.

I think we are at an inflection point, where the US is trying to replace the global economic order, which was their own creation, with a new one that better serves their national interest. In my view, the US wants three things: a) Correcting trade imbalances, b) preservation of the US dollar as the key currency, and c) more defense spending by allied nations.

Let me provide you with my perspectives on each of these three points, starting with the trade imbalances. We do not know what will come out of the ongoing trade negotiations between Japan and the US on reciprocal tariffs. As shown in **Chart 2**, the US plans to impose a reciprocal tariff rate of 24% including the baseline 10%. Separately they have imposed a 25% tariff rate on automobiles, where the crucial interest of the Japanese economy lies. But I think it is unlikely that the US administration will withdraw its tenacious tariff policies. In the meantime, I sense a possibility that some form of deal may be struck in other areas of mutual interest.

For example, the US Administration approved the acquisition of US Steel by Nippon Steel. It may pave the way for production in the US of high-end steel products for domestic manufacturers including the auto industry. Meanwhile, President Trump signed an Executive Order titled “Restoring America’s Maritime Dominance”, which suggests collaboration with Japanese and South Korean ship-building industries. This coincides with a Japanese initiative to form a united front of three shippers and four ship-builders to promote developing next-generation vessels such as liquified CO<sub>2</sub> carriers. The initiative aims at *Making Japan’s Maritime Industry Great Again*.

On the issue of preservation of the value of the USD, we know that the US authorities want to retain USD supremacy as the key currency. Trade imbalances generate global USD circulation, because the dollars US importers pay to exporters are cycled back to the US through the global financial system. This circulation underpins the status of the USD as the key currency. Investment in US Treasury securities by global investors is one of the main recycling channels. In this cycle, US Treasury securities function as risk-free benchmark instruments. Given the large fiscal deficits to be filled, the US has no alternative but to continue to rely on external financing provided by global investors.

I do not think the USD supremacy will be overtaken any time soon given the dominant role it plays in the global economy. But it will likely face more challenges, as cracks appeared in the almighty USD. Shortly after Liberation Day of April 2nd, there was a brief period when the value of dollar assets including stocks, bonds and exchange rates plunged as if a “Minsky Moment” had arrived. During this period, as shown in **Chart 3**, Japan experienced a record high level of capital inflow totaling to JPY8.2 trillion (€48 billion). This may have reflected global investors’ diversification away from the USD.

Japan helps the US preserve the value of the USD and fill the fiscal deficit, because it is the single largest purchaser of US Treasury securities. As **Chart 4** shows, it has a total outstanding of \$1.1 trillion including \$960 billion investment out of its foreign exchange reserves. This contrasts with German reserves, a substantial portion of which is held in gold, as I understand. Japan’s commitment to continue to be a stable underwriter of US Treasury securities, I personally think, can potentially be a powerful “card” to play against President Trump’s tariff policy.

## Governor Mayekawa’s extraordinary experience

I now want to move on to the third argument raised by the US, which is to require its allied partners of increased spending for national defense. This has much to do with the question of how Japan should address the growing geopolitical tensions. Before answering this question, let me introduce an extraordinary story of a former Bank of Japan(BOJ) Governor named Haruo Mayekawa. He passed away

in 1989 but is still remembered as the man who brought the BOJ back into the international central banking community during the post-war era. His long international experience, which dated back to the prewar period, won the trust of his fellow central bankers.

In October 1988, as a junior officer, I had a chance to dine with Mr. Mayekawa and his wife at a traditional German restaurant in Berlin. He was invited as a special guest to the International Monetary Fund (IMF) Annual Meeting held in Berlin that year. Over a good wine, he became a little more eloquent than usual and started to tell us the following story.

Berlin was a special place, he began. The BOJ, after its foundation in 1882, had established several overseas offices. In 1941, Mr. Mayekawa was assigned to the BOJ's Rome Office. World War II had broken out. After the surrender of Italy, he moved to the BOJ's Berlin Office, where he stayed until the final days of the war in Europe. He described to us what life was like in the bunkers of Berlin in those days.

Then, after the fall of Berlin, he fled via the Siberian Railway to Manchuria, a part of China under Japanese control at the time. This was possible because Japan and the Soviet Union had still maintained a Neutrality Pact. From Manchuria he took a ship back to Japan. Had he decided to remain in Manchuria, he might have been caught up in the military offensive by the Soviet Union following its declaration of war on Japan in August 1945. When Mr. Mayekawa finally returned home and stood in his doorway, Mrs. Mayekawa told us, she was so surprised that she first looked to see whether he had feet -- because in Japan it is thought that ghosts do not have feet. She had assumed he was no longer alive, because he had been reported missing.

Mr. Mayekawa is the only governor in the history of central banking who experienced three unconditional surrenders in wartime, in Italy, Germany, and then in Japan. At the restaurant, looking at the colorful and prosperous lights of the Kurfürstendamm, he concluded his story by telling us how much he cherished peace and how much he thought sound economic development mattered.

## Addressing geopolitical tensions

His story is a sober reminder of the geopolitical environment we are in today. So is the map in **Chart 5**. With the four disputed islands in the North, which were occupied by the Russian forces after Japan's surrender, a Peace Treaty has not yet been concluded between Japan and Russia. We feel the same way about the big neighbor as the Finns do. Neither do we have a diplomatic relationship with North Korea (DPRK). They occasionally test-fire missiles over Sea of Japan. The daughter of a former employee of the BOJ Branch Office in Niigata was abducted by North Korea in 1977 and still missing 48 years on. The Bank is supporting the mother who hasn't given up. China, which Japanese people provided with support to develop its economy in the post-war period out of genuine good will and a sense of guilt for causing the suffering of the Chinese people during war time, has now grown into an economic and military super-power.

Although Ukraine is geographically far away from Japan, how the War in Ukraine is going to end will have implications for tensions in the Taiwan Strait. Unlike Germany, we do not have NATO. Neither do we have an equivalent of the EU in this part of the world. Therefore, I think we have little option but to reinforce strategic interdependence with the United States.

### 3. What Japan should do in the shifting economic and political landscape

#### Guardian of free trade

So, what should Japan do in this shifting economic and political landscape? First, Japan should contribute to fostering what is still left of the multilateral free trade system to prevent the global economy from further fragmentation. Japan should take on a leadership role in enhancing closer collaborations with those countries in the Asia Pacific and Europe that share common values and objectives. Expanding the CPTPP (Comprehensive and Progressive Agreement for Trans-Pacific Partnership) is a typical example where Japan can continue to play a leading role. Given its track record, Japan should not hesitate to become a guardian of free trade.

#### Higher labor productivity

Second, Japan should continue with steadily promoting policies to achieve its unaccomplished goals. There are two challenges that I think must be addressed imminently. One is the need for structural reforms aimed at improving labor productivity. **Chart 6** illustrates the urgency of such structural reforms. Here, Japan's real GDP growth rate is decomposed into labor productivity growth and rate of change in the number of employed persons, or labor input more broadly. We can see from the chart that during the 1980s, robust economic expansion was supported by strong productivity growth and a growing workforce. Over time, however, both factors have declined steadily, with labor force contribution turning negative in the 2000s.

Going forward, the demography predicts an increasingly negative contribution of labor input to growth. It is obvious from the chart that this must be more than offset by improvement in labor productivity in order to maintain positive growth. What this chart suggests is that, for any country with a shrinking population, including Germany, structural reforms to improve labor productivity require high policy priority.

**Chart 7** compares movements in potential growth rates of Japan and Germany since the 1980s. At a glance, we can see in common a downward long-term trend shown in solid black lines. The bars in different colors show contributing factors. Japan, shown on the left side, saw a sharp contraction in capital stock (shown in pink) during the deflation after the bubble burst in the early 1990s. This was compounded by the decline in labor input (in green). More recently improvements in total factor productivity (TFP in blue), which represents innovation, are contributing to the recovery of the potential growth rate.

Germany, shown on the right side, initially saw a robust rise in its potential growth rate, reaping the benefits of globalization unleashed by détente and the fall of Berlin Wall. More recently, however, the potential growth rate is declining due mostly to a continuous erosion in TFP. In the current context, I think both Japan and Germany need structural reforms aimed at elevating labor productivity by promoting capital expenditure and innovation.

#### Sustainable fiscal structure

The other challenge for Japan is the restoration of a sustainable fiscal structure. The horizontal axis in **Chart 8** shows debt outstanding and the vertical axis shows fiscal deficit as measured in terms of ratios to nominal GDP of selected countries. Germany retains ample flexibility even after the “debt-brake” is removed. In contrast, Japan is an outlier. The US is also not well-positioned with its large fiscal deficit.

Fiscal sustainability is of particular importance because the BOJ in March 2024 embarked on monetary policy normalization by lifting all the unconventional monetary policy measures that had been employed. In addition to policy rate hikes, the BOJ started its Quantitative Tightening (QT) by reducing its holdings of Japanese Government Bonds (JGBs).

**Chart 9** shows the BOJ's QT game plan. It holds JPY580 trillion (€3.4 trillion) of Japanese Government Bonds (JGBs), which accounts for almost half of the total outstanding. The chart on the right side indicates the pace of quarterly reduction in the outstanding of the BOJ's JGB holdings. The pace is going to accelerate over time. As shown in the left chart, it is expected to reduce the outstanding to 485 trillion by March 2027, which is a 16% contraction from the period right before the start of QT.

As the BOJ recedes as the most dominant buyer of JGBs, somebody else must fill the gap unless the fiscal deficit is reduced dramatically. Traditional domestic investors such as banks will have limited capacity because they are under tougher regulations. Inevitably, therefore, overseas investors will be relied upon as JGB underwriters. **Chart 10** shows overseas investors currently account for 12% of the total market outstanding (including T-Bills). This share is expected to rise over time.

Overseas investors tend to require higher premia and thus higher interest rates in view of Japan's high debt outstanding. This will be exacerbated if the rating of JGBs by foreign rating agencies is downgraded. As you see on **Chart 11**, it has declined over time to single A, which is the lowest but one among the G7 countries. A lower rating implies a higher cost of funding for Japanese banks in the global financial markets. Therefore, establishing a sustainable fiscal structure with a view to ensuring the credibility of fiscal management is an imminent mission for Japan.

## Interoperable carbon credit market

As I mentioned, strategic interdependence with the US is indispensable when it comes to issues related national security. But building a resilient economic zone with the Asia Pacific countries with whom we share the same values is no less important in securing stability in the region. ASEAN economies in this respect are particularly promising given their potential for sustained growth.

One initiative that may be worth noting in this respect is the ongoing collaboration in the region to create a network of interoperable carbon credit markets. This is an initiative driven by the private sector, recognized by the APEC governments. **Chart 12** illustrates what we envisage. It shows, as an example, a case in which an Indonesian electric power company reduced carbon emissions through the early retirement of a coal-fired power plant, replacing it with a cleaner plant that burns LNG. In order to recover the huge cost for the new plant, a part of the reduced emissions can be sold as carbon credits to domestic as well as overseas markets like Tokyo, Singapore, Hong Kong, Sydney or elsewhere in the region. Business companies in the region can purchase carbon credits to partially offset their carbon emissions. In this way, the economies across the region can collectively become green quicker than otherwise.

This year we moved to a new phase and launched a "Pathfinder Initiative", where volunteering exchanges and platforms in the region plan to run pilot projects testing connections among exchanges and exploring cross-border transactions using blockchain technologies. Decarbonization in the Asia Pacific region remains an important joint policy objective. Notwithstanding the US absence, or perhaps all the more for that reason, the economies in the region are united and committed to advancing the initiative. I think Japan can play an integral role in leading the collective efforts.

## 4. Concluding remarks

Shortly before my trip to Hamburg I visited my mother who is now in her nineties and lives in a nursing home. She said she remembers nice days in Hamburg sixty years ago with my late father, who was an attaché at the Japanese General Consulate, and her young children. My parents belong to the generation that survived the air raids in the final days of WW II. Just like your parents and grandparents, they worked diligently to achieve Wirtschaftswunder (economic wonder) transforming our nations into economic powers from the rubble of war. I want to conclude my presentation by expressing my hope that Germany and Japan, by working closer, can achieve another Wirtschaftswunder and contribute to a stable and peaceful world in this shifting economic and political landscape. Thank you very much for your attention. Ich danke Ihnen für Ihre Aufmerksamkeit.

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July 7<sup>th</sup>, 2025

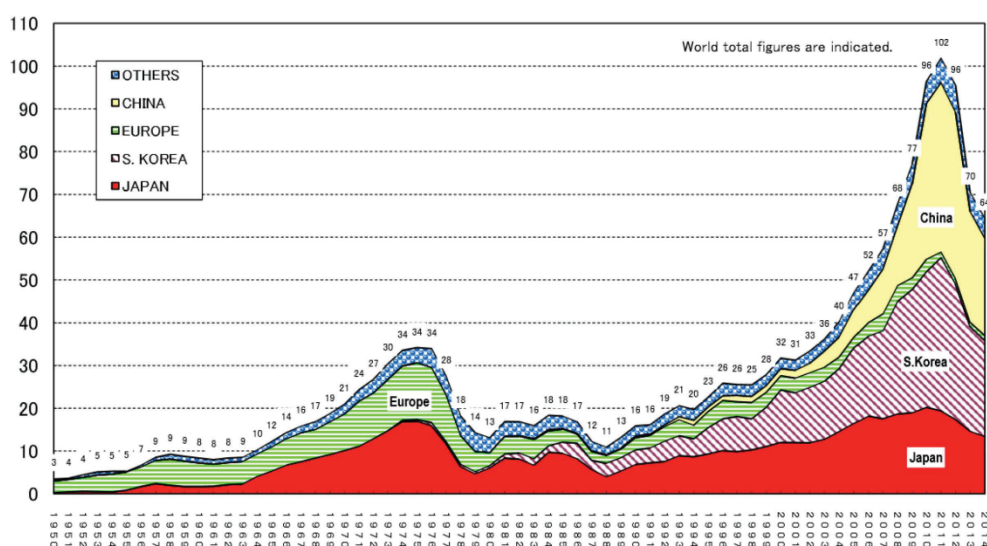
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World Completions of Ships Over 100 Gross Tonnes, 1950-2014 by Area  
(in Thousands of Gross Tonnes)



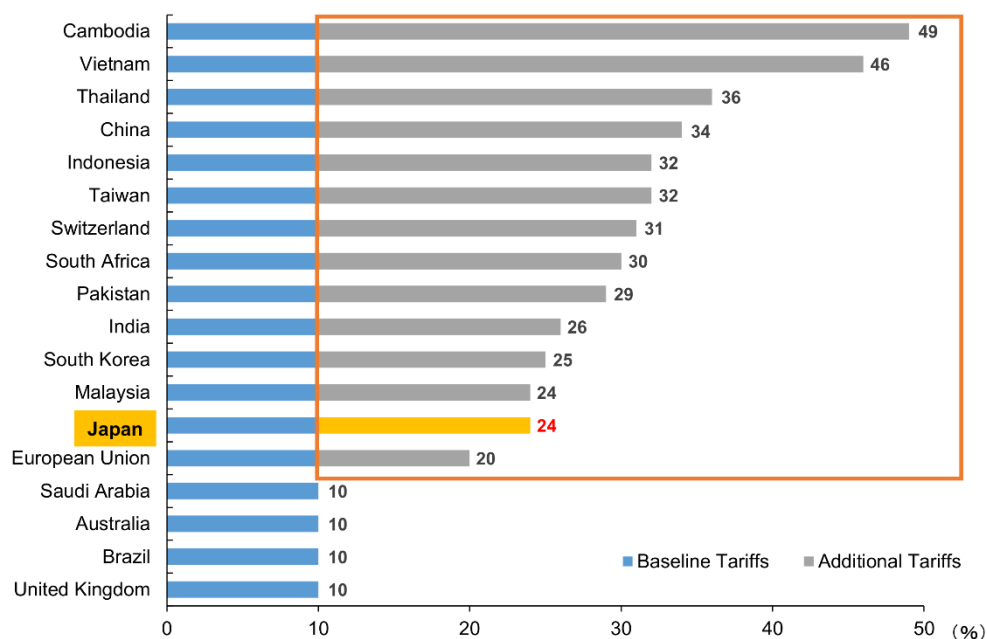
Note 1: World completions by IHS include tankers (i.e. LNG/LPG, chemicals, crude oil, oil products, others liquids), bulkers (i.e. bulk dry, bulk dry/oil, self-discharging bulk dry, other bulk dry, general cargo), passenger/general cargo, container, refrigerated cargo, Ro-Ro cargo, passenger/ro-ro cargo, passenger (cruise ships), passenger ships, other dry cargo, fish catching and other fishing, offshore supply and other.

Note 2: Ships with less than 1,000 GT (e.g. fishing vessels, tugs) as well as yachts are not included in international shipbuilding statistics like Clarkson. IHS Fairplay takes all ships with 100 GT and more into consideration but yachts are not included. However, these market segments are important for the German shipbuilding industry and consequently included in the VSM statistics.

Note 3: Statistics prior to 1968 are based on launches.

Source: Peer Review of the German Shipbuilding Industry (OECD), Shipbuilders' Association of Japan, 2015, based on statistics of HIS (formerly Lloyd's Register)

## Reciprocal Tariff Rates for Major Countries & Regions

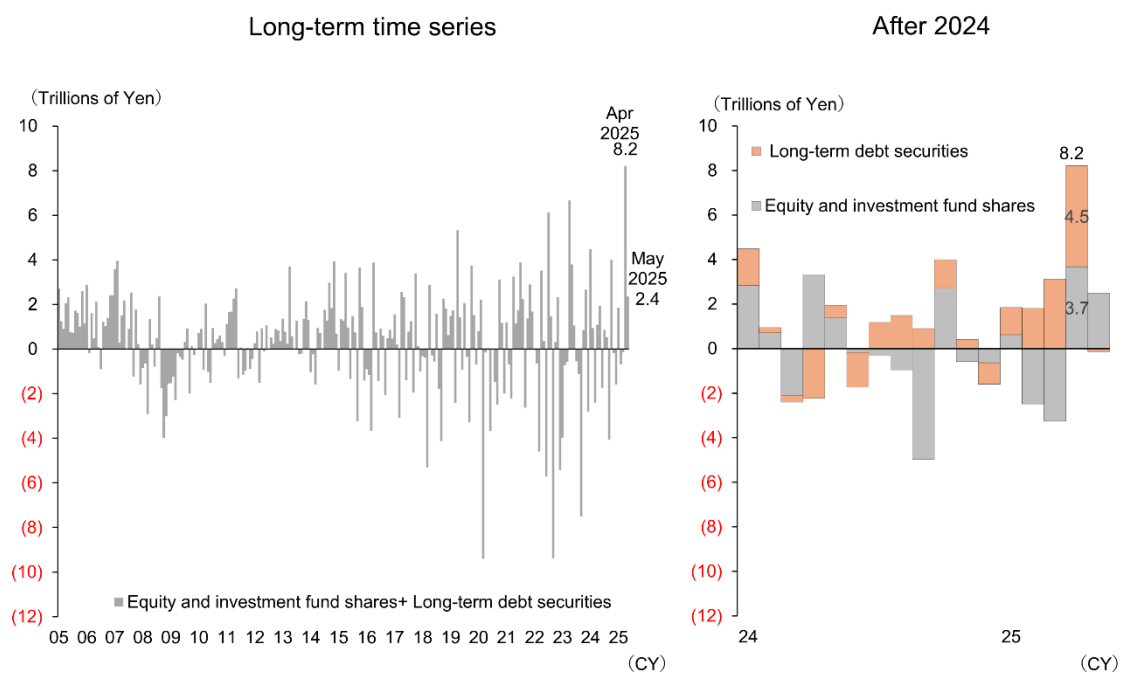


Source: The White House; compiled by DIR.

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## Portfolio Investment into Japan (Monthly)



Note: Based on Reports from Designated Major Investors. The most recent value is at the end of May 2025.

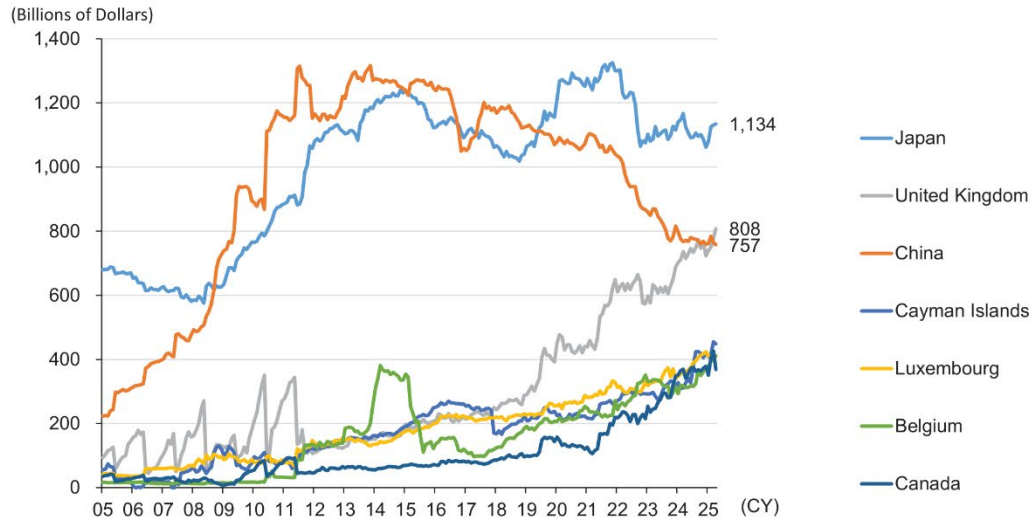
Source: Ministry of Finance; compiled by DIR.

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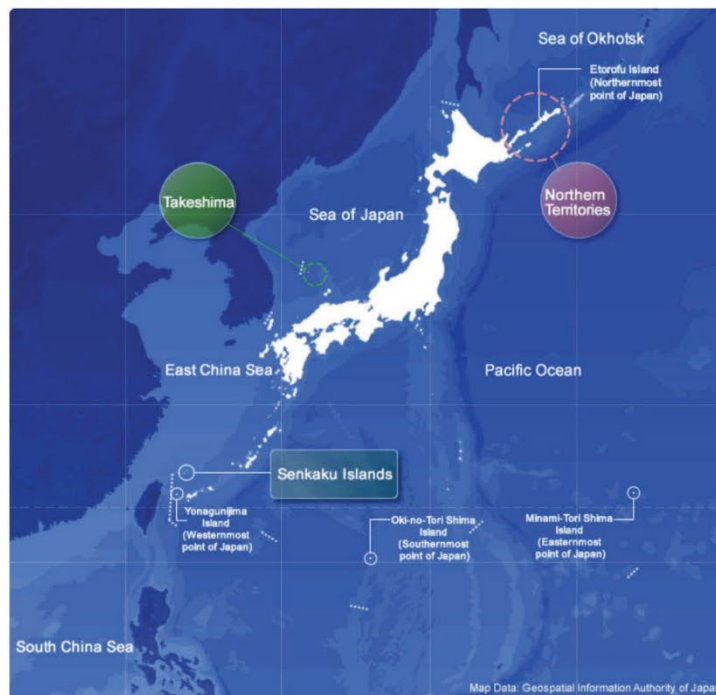


## US Treasury Securities Holdings by Country



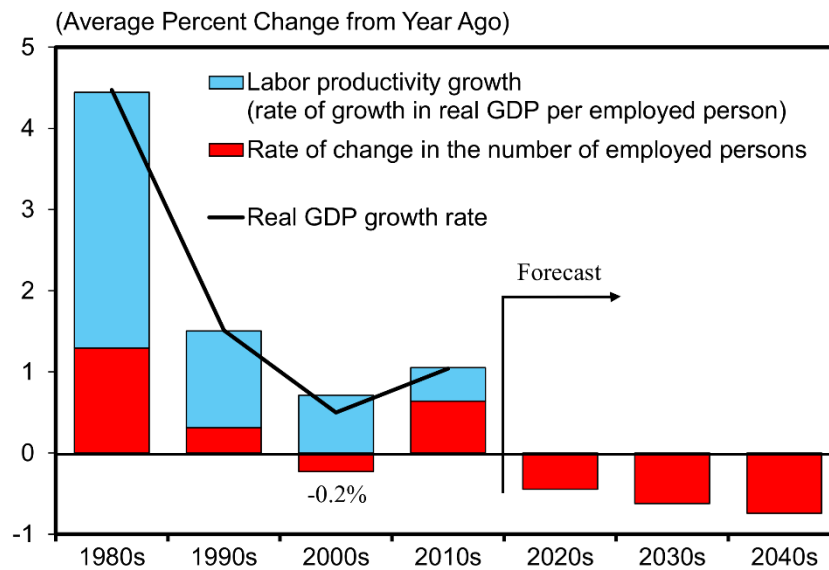
Note: The most recent value is at the end of April 2025.  
Source: U.S. Treasury, Haver Analytics; compiled by DIR.

## Japan's Geopolitical Environment



Source: Ministry of Foreign Affairs, Geospatial Information Authority of Japan (map data)

## Japan's Real GDP and Labor Productivity Growth



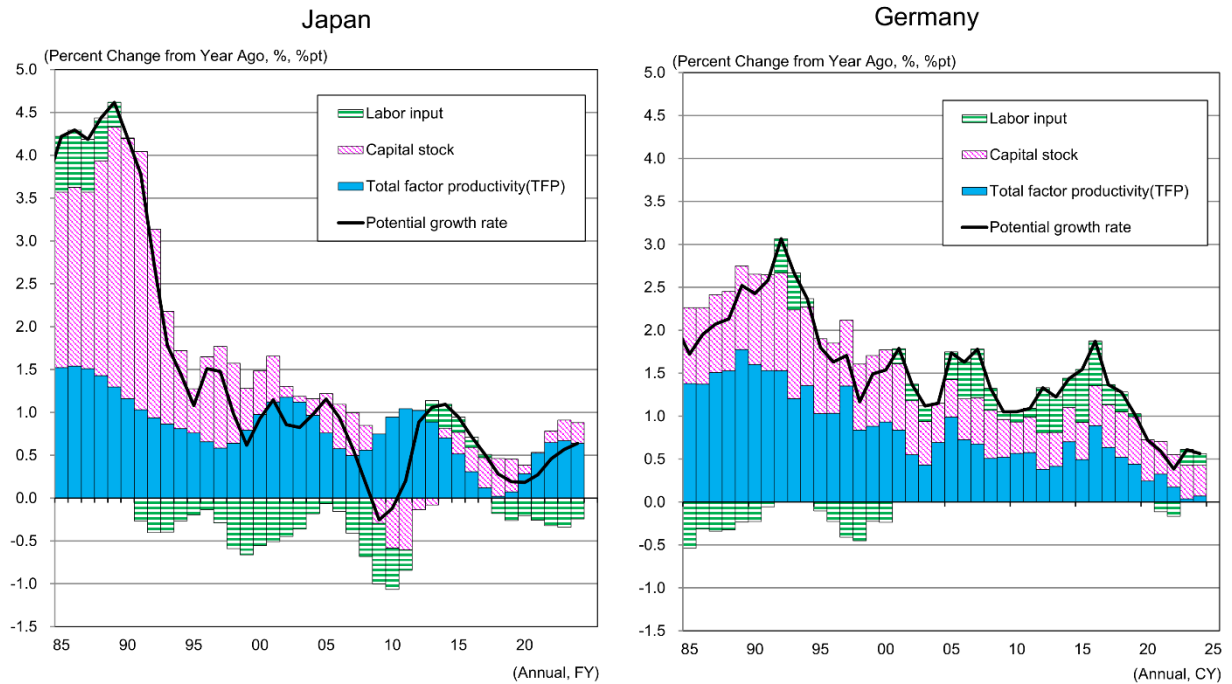
Note: Fiscal-year basis. The rates of change in the number of employed persons from 2025 onward are calculated using the population outlook (medium variant) and projected labor force participation rates (assuming the labor force participation rate for each age/sex group remains the same as in 2024).  
1980s data are calculated using data from 1982 to 1989.  
1990s, 2000s, 2010s data are calculated using data from 1990~1999, 2000~2009, 2010~2019 respectively.

Source: Cabinet Office, Ministry of Internal Affairs and Communications, National Institute of Population and Social Security Research, INDB; Compiled by DIR.

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## Potential Growth Rates of Japan and Germany

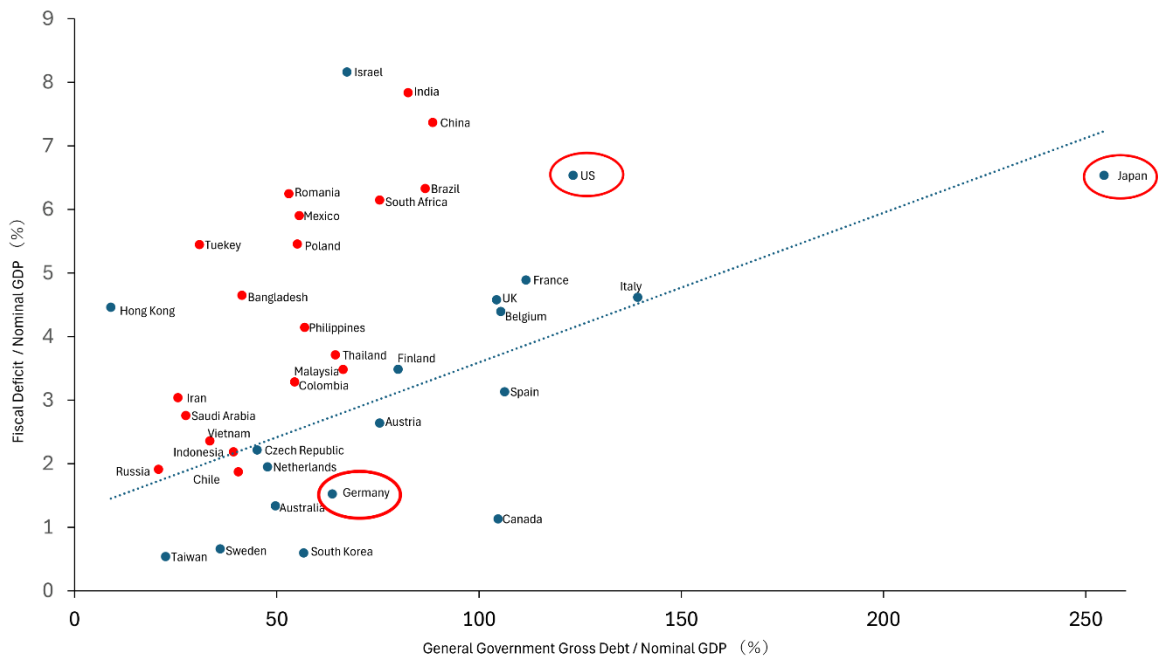


Source: BOJ, German Council of Economic Experts; compiled by DIR.

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## Fiscal Deficit and General Government Gross Debt to GDP

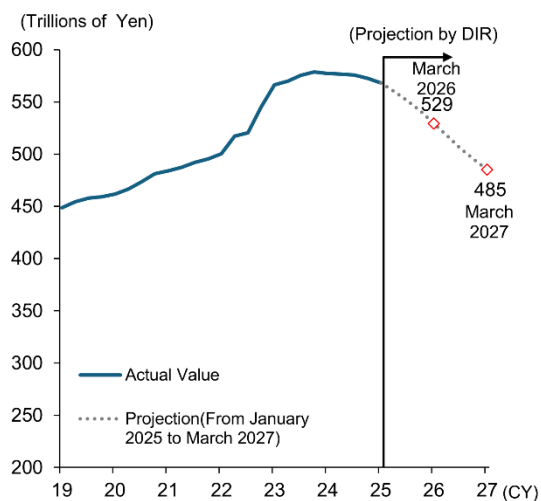


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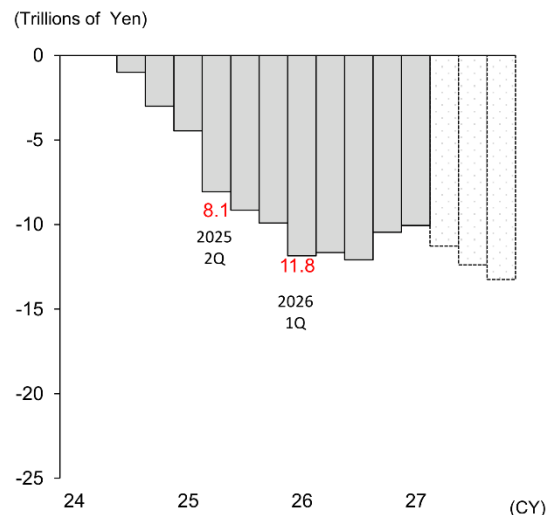
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## Projected Balance of Government Bonds Held by BOJ

Projected Balance of Government Bonds Held by the Bank of Japan



Trends in the Amount of Reduction in Government Bond Holdings by Quarter



Note 1: Based on the monetary policy meeting in June 2025.

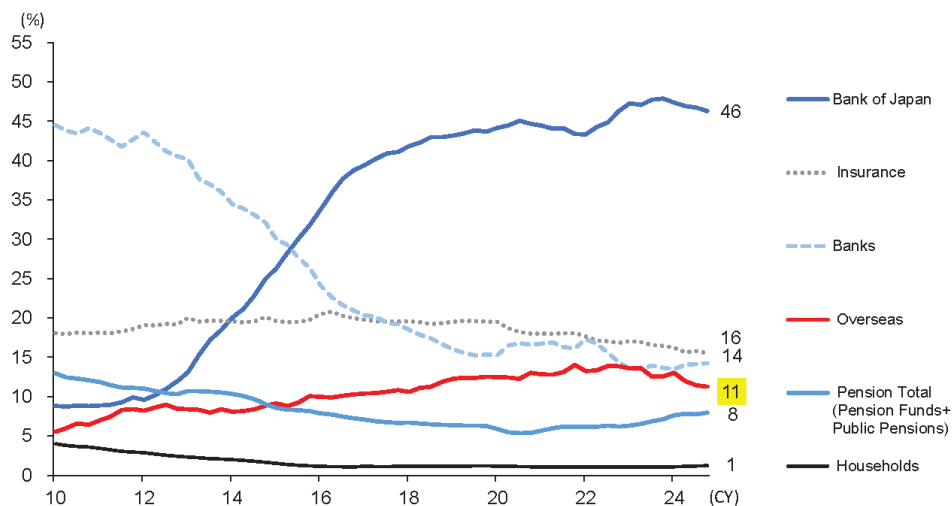
Note 2: It is assumed that the balance will be reduced as decided at the monetary policy meeting in June 2025 until March 2027. It is assumed that similar policies will be maintained after March 2027.

Source: Bank of Japan; compiled by DIR.

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## Distribution of Japanese Government Bond Holders



Note 1: Japanese government bonds include FILP bonds and treasury discount bills.

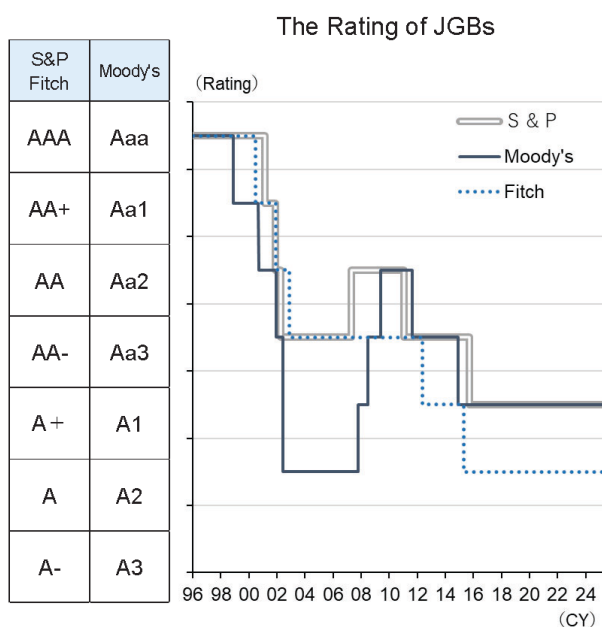
Note 2: Banks include securities investment trusts and securities companies.

Source: Bank of Japan; compiled by DIR.

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## Ratings of JGB and International Comparisons



Source: S&P Global, Fitch Ratings, Moody's; compiled by DIR.

### Comparison of Government Bond Ratings

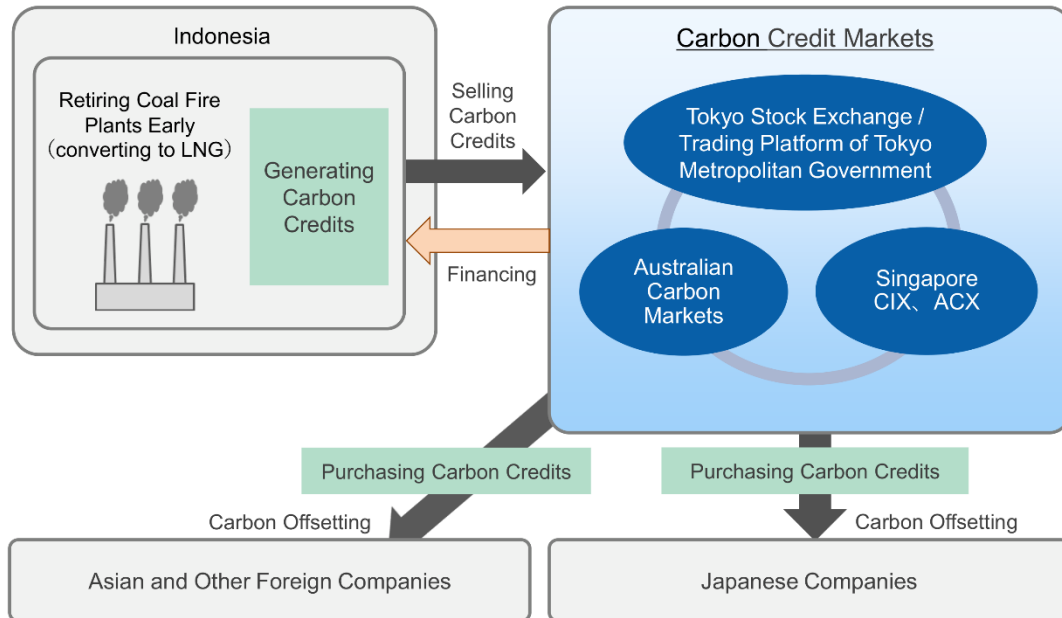
	S&P	Fitch	Moody's
Germany	AAA	AAA	Aaa
Canada	AAA	AA+	Aaa
US	AA+	AA+	Aa1
UK	AA	AA-	Aa3
France	AA-	AA-	Aa3
Japan	A+	A	A1
Italy	BBB+	BBB	Baa3

Note: In domestic currency denomination.  
Source: Bloomberg; compiled by DIR.

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## Illustration of Generating Carbon Credits to Promote Decarbonization



Source : Various Sources; compiled by DIR.

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