

26 December 2025 (No. of pages: 2)

Japanese report: 18 December 2025

# Will the Takaichi Administration's Fiscal Policy Lead to Further Yen Depreciation?

*Expansionary fiscal stimulus leads to a weaker yen the following year*

Economic Research Dept. **Hirohito Hatanaka**

## Summary

- The Sanae Takaichi administration, championing “responsible and proactive public finances,” approved comprehensive economic measures in November, with the supplementary budget underpinning it passing in December. The scale of the measures reached 42.8 tril yen, making it the sixth largest economic stimulus in history, following those implemented during the periods affected by the international financial crisis of 2008, the COVID-19 pandemic, and Russia's aggression against Ukraine. In recent years, economic measures exceeding the increase in tax revenue and non-tax revenue have been formulated continuously, leading to a normalized net increase in public debt.
- The yen has been weakening amid market speculation about the Takaichi administration's expansionary fiscal policy stance. According to the Mundell-Fleming model, an expansion in fiscal spending should lead to an appreciation of the domestic currency, but many existing empirical studies report that an expansionary fiscal spending shock leads to a depreciation of the domestic currency. The author's analysis of Japan showed that a 1% increase in the real government debt balance leads to a 0.9% depreciation of the real effective exchange rate one year later through an increase in imports.
- The Takaichi administration included measures to combat rising prices as the first pillar of its comprehensive economic measures. However, if fiscal spending expansion leads to pressure for yen depreciation, this will become a factor pushing up domestic prices. To prevent such effects, it is crucial to steadily reduce the real government debt balance. The Takaichi administration aims to achieve fiscal soundness by strengthening growth potential. However, boosting real GDP solely

through expanded fiscal spending will make it difficult to reduce the government debt-to-GDP ratio. Unless the goal is to achieve real debt reduction through inflation, the administration should continue aiming for a primary balance surplus.