

# Capital Markets Strategy

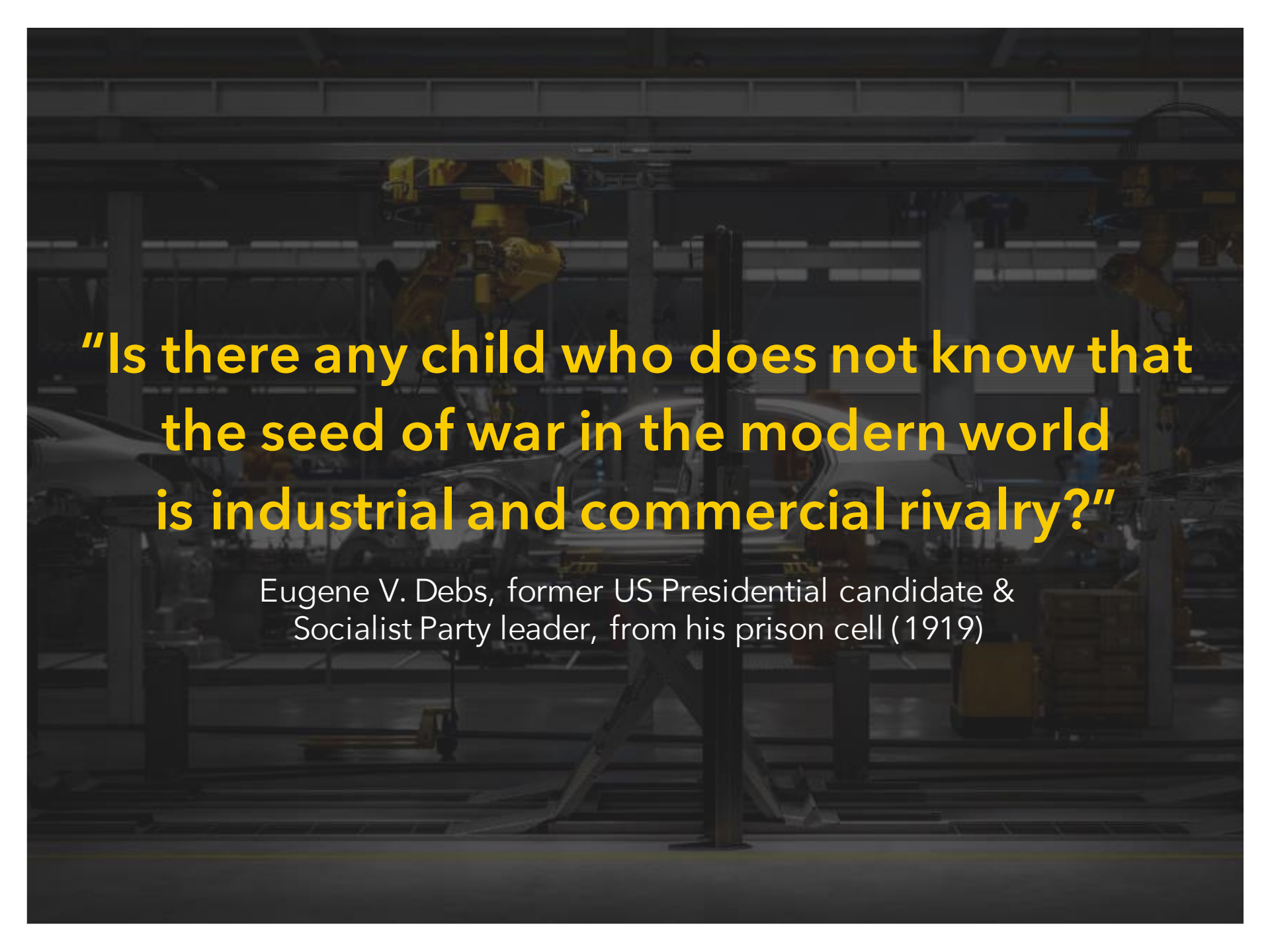
Essential inCights for the C-Suite



## Trade War 2.0 Will Be Different

Observations for Navigating Trade Policy Escalation in 2025

JAN 2025



**"Is there any child who does not know that  
the seed of war in the modern world  
is industrial and commercial rivalry?"**

Eugene V. Debs, former US Presidential candidate &  
Socialist Party leader, from his prison cell (1919)

# AUTHORS



**Tom Joyce**

Managing Director  
Capital Markets Strategist  
New York, NY

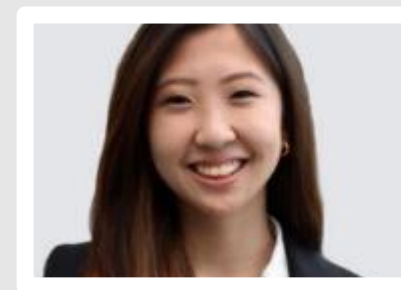
Tom.Joyce@mufgsecurities.com  
(212) 405-7472



**Stephanie Kendal**

Vice President  
Capital Markets Strategist  
New York, NY

Stephanie.Kendal@mufgsecurities.com  
(212) 405-7443



**Angela Sun**

Analyst  
Capital Markets Strategist  
New York, NY

Angela.Sun@mufgsecurities.com  
(212) 405-6952



**Roger Hollingsworth**

Managing Director  
Head of US Government Affairs  
Washington, D.C.

RHollingsworth@us.mufg.jp  
(202) 463-2234



**Alex Anderson**

Vice President  
Government Affairs Office  
Washington, D.C.

AIAnderson@us.mufg.jp  
(202) 463-2226

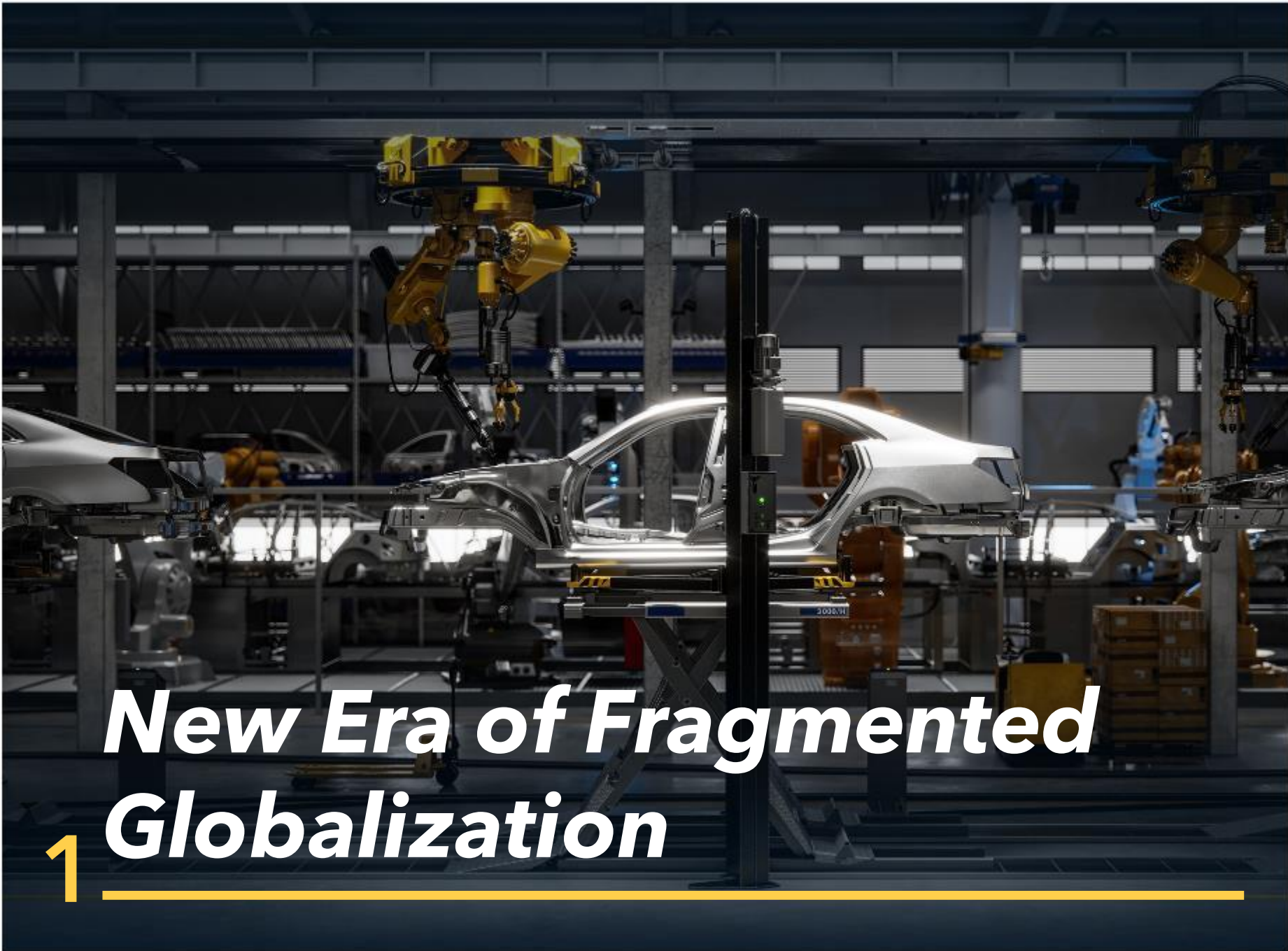


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# *New Era of Fragmented Globalization*

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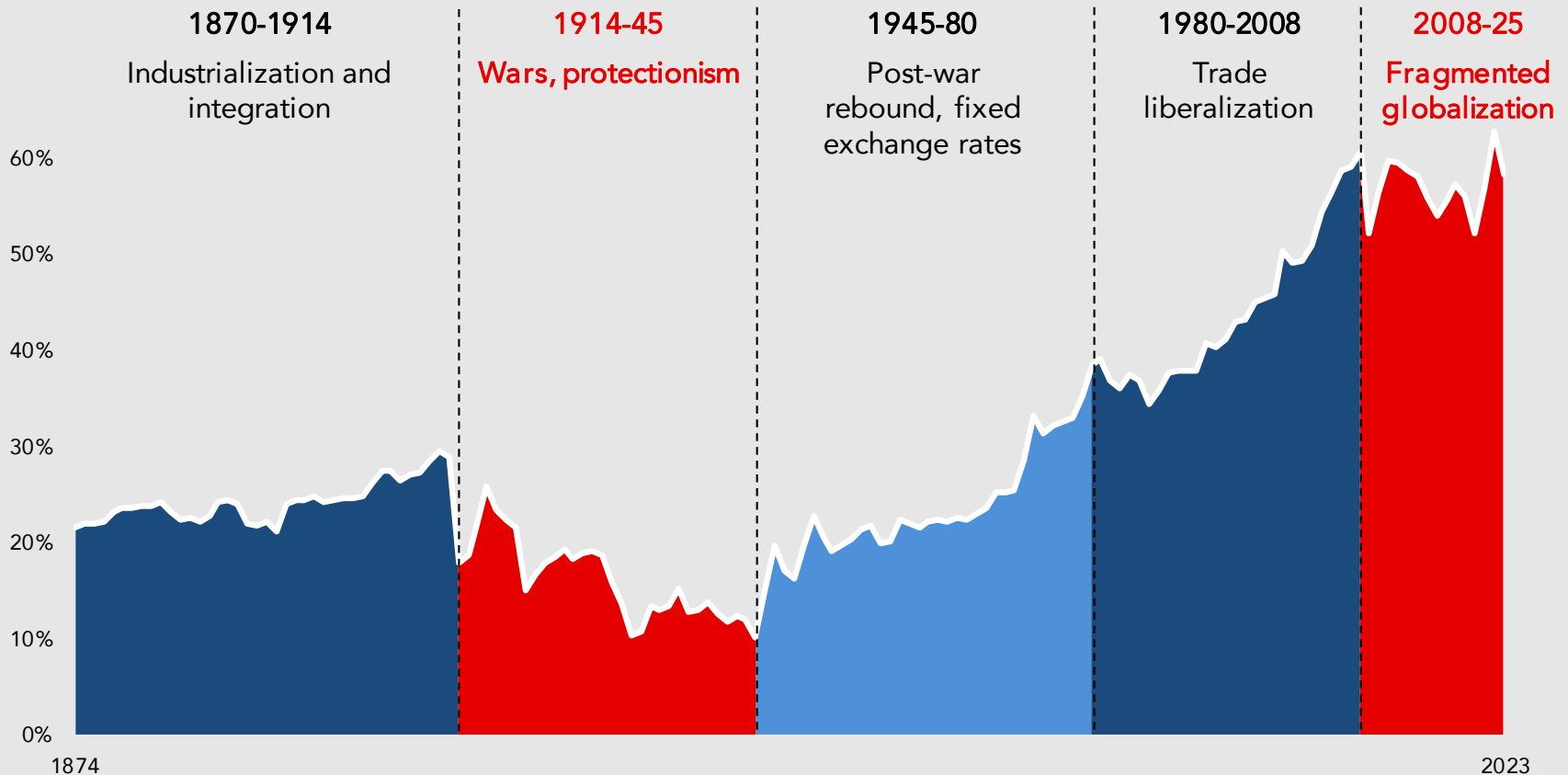
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# New Era of Fragmented Globalization



Following a multi-decade period of trade liberalization and “just-in-time” globally extended supply chains, a new era of “fragmented” globalization (a better term, perhaps, than “de-globalization”) began to emerge after the Great Financial Crisis (GFC) of 2008-9. Since the 2018-19 trade wars, the post WWII period of gradual trade liberalization officially ended, and is unlikely to return anytime soon.

Trade openness (sum of global exports and imports as percent of GDP)

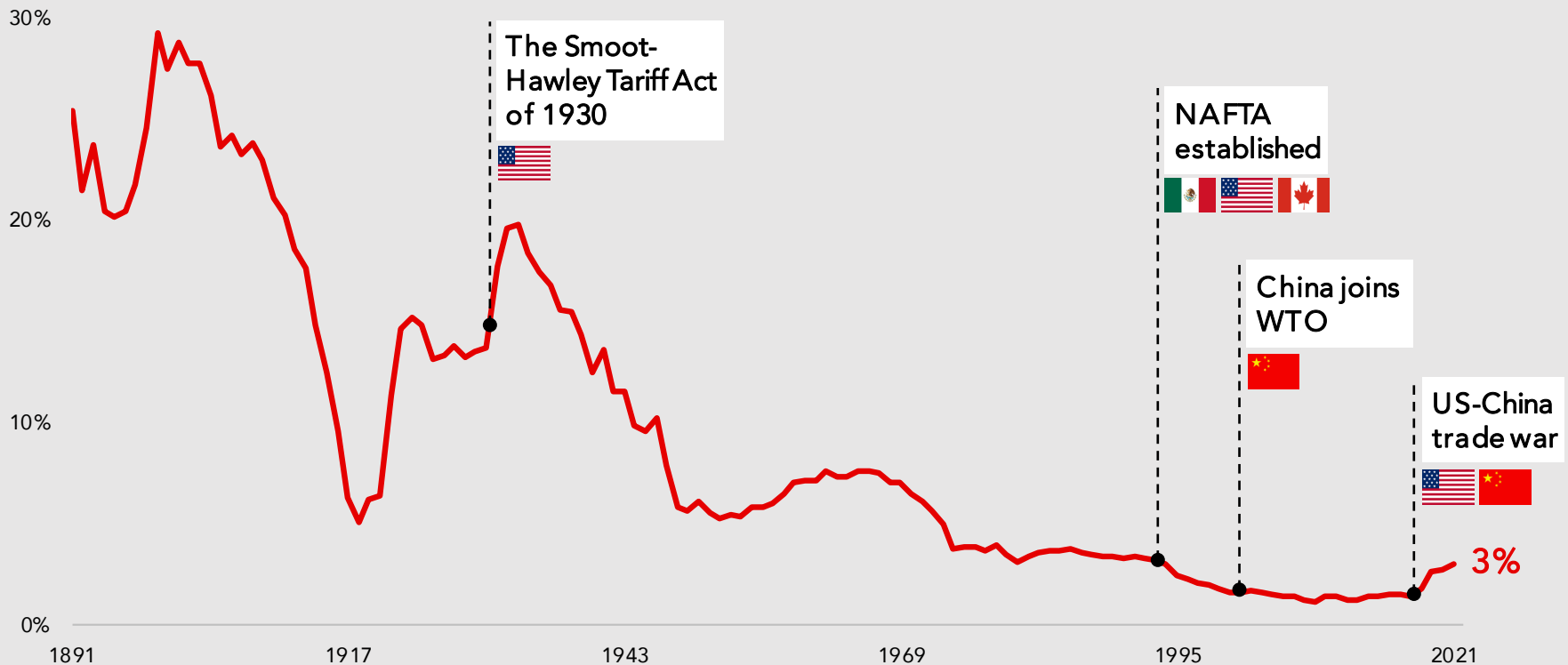


Source: (1) PIIE, “Globalization is in retreat for the first time since the Second World War” (October 2022). Trade openness index is defined as the sum of world exports and imports divided by world GDP. 1870-1949 data is from Klasing and Milonis (2014). 1950-1969 data is from Penn World Tables (10.0). 1990 to 2023 data is from the World Bank.

# Largest Tariff Increase Since Smoot-Hawley in 1930

Over the next two years (2025-26), we expect President Trump to implement the largest increase in US tariffs since the infamous Smoot-Hawley tariffs in 1930. While Trump views tariffs as a tool for economic and negotiating leverage, we do believe that the US and global economy will emerge from Trade War 2.0 with a substantively higher overall level of tariffs.

## US duties collected, % of total imports



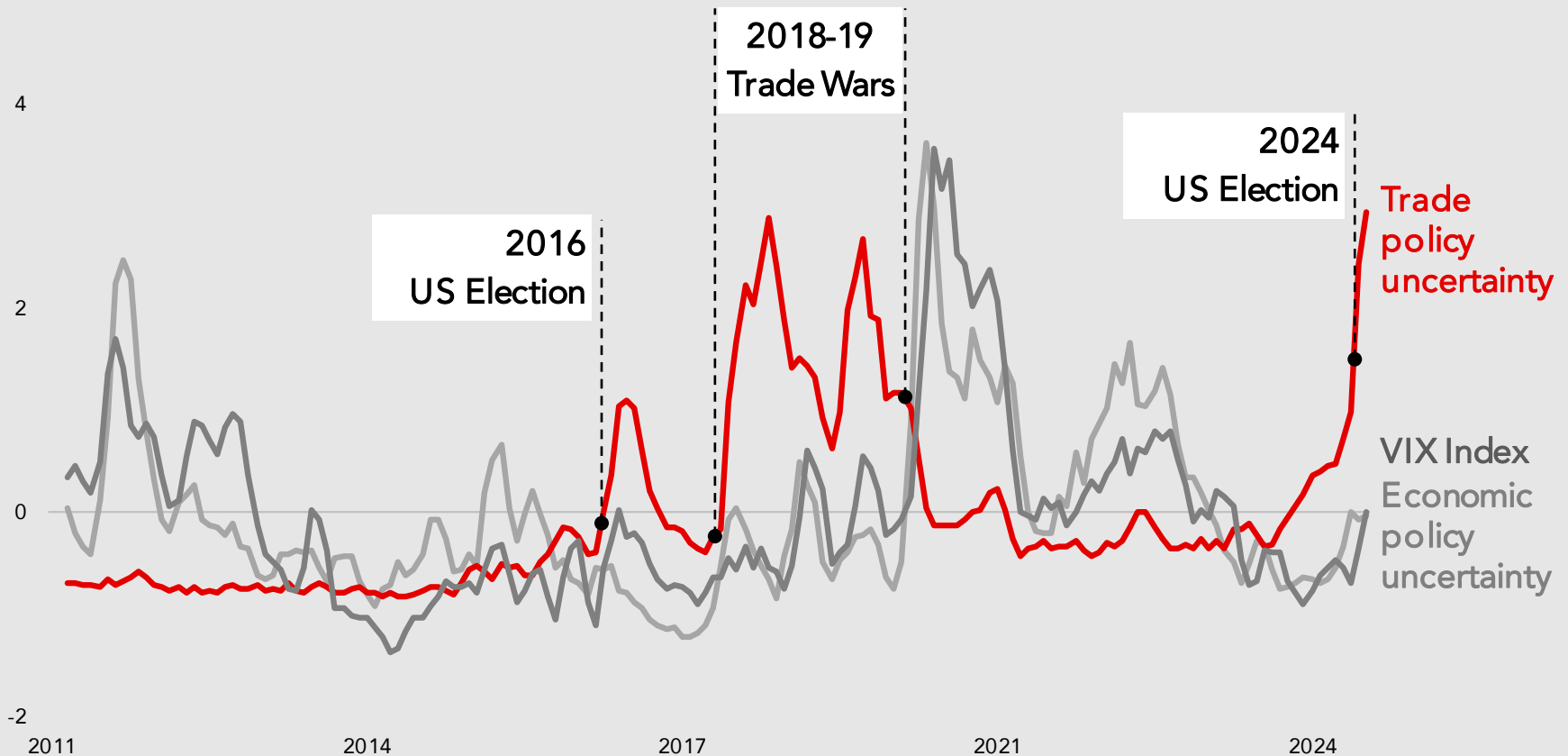
Source: (1) US International Trade Commission, "US Imports for Consumption, Duties Collected, and Ratio of Duties to Value." Table 1.

# Elevated US Trade Policy Uncertainty in 2025



Trade policy uncertainty rose to record highs in 2018-19 and may rise even higher under Trump 2.0, posing downside risk to global trade, growth and markets.

## US economic & trade policy uncertainty



Source: (1) Bloomberg. Dario Caldara. Data through December 31, 2024. Oxford Economics, "Tariff Uncertainty Weighs on Fixed Investment." US policy uncertainty is z-score, 3-month moving average.



# What Can Companies Do to Mitigate Trade Risk?

Sidley Austin LLP's trade and custom's practice has suggested a range of risk mitigation strategies for corporations in navigating the elevated policy risk landscape.

Trade risk mitigation steps for consideration

- 1** ***Pull shipments forward***  
(tariff implementation will be forward-looking, not retroactive)
- 2** ***Include contract provisions that specify tariff risk***  
(i.e., "Trump Majeure" provisions)
- 3** ***Use of foreign trade zones*** to increase tariff efficiency
- 4** ***Diversify supply chains*** to lower risk jurisdictions
- 5** ***Pursue product exclusions***, to the extent such process becomes available again
- 6** ***Pro-actively manage foreign currency exposure*** as target countries lower policy rates and depreciate currencies to absorb tariff costs

Source: (1) Sidley Austin LLP International Trade & Customs Practice (Ted Murphy, Partner).

A photograph of a car chassis on an assembly line. The chassis is silver and is mounted on a yellow and blue conveyor system. The background shows a factory setting with various mechanical parts and equipment.

***Trade War 2.0  
Will be Different***

**2**

# Trade War 2.0 Will Be Different

While Article 1 of the US Constitution delegates the power of tariffs and trade to the US Congress, Congress has delegated much of that power to the President over time. In our view, corporations and market participants globally should shed the conventional wisdom and mindset of the 2018-19 trade wars, and prepare for a new period of trade escalation that is likely to be quite different in speed, scale, implementation and scope.

## Expectations for Trade War 2.0



**More philosophical than tactical:** More pervasive. Episodic. Longer duration. **Not necessarily escalate to de-escalate.** Higher level of tariffs post-escalation.

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**Sooner this time:** Extensive **"Day 1" agenda.** Prior trade war took 3 years to peak (2019).

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**Things can move quickly:** Architect (Greer - USTR) and architecture (US trade law) in place. Initial increases as early as **Feb 2025.** Use of **forward starting dates and escalation schedules.**

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**Less process this time:** More reliance on **IEEPA** and **Section 338** of the Tariff Act of 1930 (**no investigations, faster implementation**), than Section 301 and 232 used previously (which require "investigations" and delayed implementation).

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# Trade War 2.0 Will Be Different

Expectations for Trade War 2.0



**More universal this time:** Larger scale and scope. **More countries. More product categories.** Higher tariff rates.

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**Different targeting approach:** Less product category driven (i.e., washing machines, steel & aluminum). More universal approach (base level of higher tariffs on all products and countries). Escalations **driven more by country of origin than product type.** Allies & adversaries alike.

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**Concurrent expansion of non-tariff escalation tools:** Commerce Department Entity List. **Technology restrictions.** Financial sector access limits. More restrictive cross-border M&A and FDI oversight. Tax and lending incentives for domestic investment.

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**More existential approach to China:** Even more hawkish. Appeal of phase 1 deal. Higher rates. More expansive. **Potential revocation of China's Permanent Normal Trade Relations (PNTR) status.**

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# Trade War 2.0 Will Be Different

## Expectations for Trade War 2.0



**China ready this time:** Formidable policy toolkit and countermeasures  
**"ready to go."**

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**Range of retaliatory measures:** Range of possibilities, not just tariffs  
(digital taxes, entity lists, **critical minerals**).

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**Fewer product based exclusions:** Less opportunity (at least initially) for  
companies to apply for **available product-based exclusions** than in 2018-19.  
Could change over time.

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**Ambiguity as an incentive:** By maximizing policy uncertainty, seeking to  
incentivize domestic US investment by foreign and US companies alike.  
**Re-industrialization of America.**

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**Tariffs becoming core to the foreign policy toolkit:** Not just for trade  
and competition, but also as **a core tool in foreign policy** (border crisis with  
Mexico, Greenland, Panama, NATO negotiations, etc.). General preference for  
tariffs over sanctions.

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# **3** *Sooner This Time*

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# Trade Policy Leadership Team in Place

Jamieson Greer, President Trump's 2.0 US Trade Rep, is a former Chief of Staff for Robert Lighthizer in the USTR during Trump 1.0 and is well versed in US trade law and the 2018-19 policy toolkit. While former USTR Robert Lighthizer does not formally have a position (yet), we expect him to be very active as a trade policy advisor, whether officially or unofficially. While we expect Lighthizer's thumbprint on policy to be formidable, we would also advise corporations globally to be cautious in taking comfort or guidance from moderating voices within the President's Cabinet, as has already been evident during the transition period between the Election and Inauguration.

## Key leaders for Trump 2.0 trade & China policy

### Key Architects



**Jamieson Greer**  
US Trade Representative



**Robert Lighthizer**  
Former USTR  
(Advisory role,  
officially or unofficially)

### Economic & Market Impact



**Scott Bessent**  
Secretary of the Treasury



**Stephen Miran**  
Chair of Council of  
Economic Advisors

### China "Hawks"



**Marco Rubio**  
Secretary of State



**Kevin Hassett**  
Director of National  
Economic Council



**Mike Waltz**  
National Security Advisor



**Howard Lutnick**  
Secretary of Commerce

# Legal Architecture & Policy Toolkit in Place

Compared to the 2018-19 trade wars, look for the new Administration to consider more efficient sections of US trade law to expedite tariffs on counterparties without the long investigation periods and implementation delays of the previously utilized Section 301 China tariffs. **By using Section 338 of the Tariff Act of 1930 and Section 203 of IEEPA, they can impose tariffs without much process (i.e., no investigation; only a Presidential finding or declaration).**

Less process, fewer investigations, rapid implementation

Trade law provision	Purpose / Precedent	Investigation Required?	Process
<b>Section 203, International Emergency Economic Powers Act of 1977 (IEEPA)</b>	<ul style="list-style-type: none"> <li>Unusual and extraordinary threats</li> <li>Used extensively by Trump in first term; sanctioned 3,700 entities; invoked 11 national emergency declaration</li> </ul>	<b>No</b>	President declares national emergency, trade measures can be applied within weeks
<b>Section 338, Tariff Act of 1930</b>	<ul style="list-style-type: none"> <li>Discrimination against US goods</li> <li>Last used in 1949 in respect to trade with China</li> </ul>	<b>No</b>	Allows punitive tariffs up to 50% or blocking imports from offending countries, up to President's discretion
<b>Section 122, Trade Act of 1974</b>	<ul style="list-style-type: none"> <li>Balance of payments issues / dollar stability</li> </ul>	<b>No</b>	President can impose 15% tariffs for 150 days, intended for short-term crises

Source: (1) Bloomberg, "A Roadmap Through Trump's Tariff Realities and Trade War Drama" (Shawn Donnan & Anna Wong). Bloomberg Economics.



# Legal Architecture & Policy Toolkit in Place

The 2018-19 Trump 1.0 trade escalation was centered around legal provisions (301, 232, 201) that required significant process and long investigation periods. For example, the trade advisory team at Sidley Austin notes that the Section 301 China tariff investigation began in April 2017, but tariffs were not imposed until July 2018. They do not expect Trade War 2.0 to rely as heavily on the same statutes (especially for non-China tariffs).

**Less process, fewer investigations, rapid implementation**





Trade law provision	Purpose / Precedent	Investigation Required?	Process
<b>Section 301, Trade Act of 1974</b>	<ul style="list-style-type: none"> <li>• Unfair trade practices</li> <li>• 2018-19 China tariffs</li> </ul>	<p><b>Yes</b></p> <p>US Trade Representative (USTR)</p>	Reports within 12 months, President can impose tariffs
<b>Section 232, Trade Expansion Act of 1962</b>	<ul style="list-style-type: none"> <li>• National defense &amp; economic security</li> <li>• 2018-19 steel &amp; aluminum tariffs</li> </ul>	<p><b>Yes</b></p> <p>US Commerce Department</p>	Reports within 270 days, President decides within 90 days on tariffs
<b>Section 201, Trade Act of 1974</b>	<ul style="list-style-type: none"> <li>• Industries injured by import surges</li> <li>• 2018-19 washing machine &amp; solar panel tariffs</li> </ul>	<p><b>Yes</b></p> <p>US International Trade Commission (USITC)</p>	Report to President within 180 days, President has 60 days to act, measures can be applied up to 4 years

Source: (1) Bloomberg, "A Roadmap Through Trump's Tariff Realities and Trade War Drama" (Shawn Donnan & Anna Wong). Bloomberg Economics.

# Sequencing the Trade War

The 2018-19 trade wars took nearly 1-2 years to begin and reach peak escalation. Look for a more rapid “Day 1” timeline this time, with initial implementation as soon as February 2025.

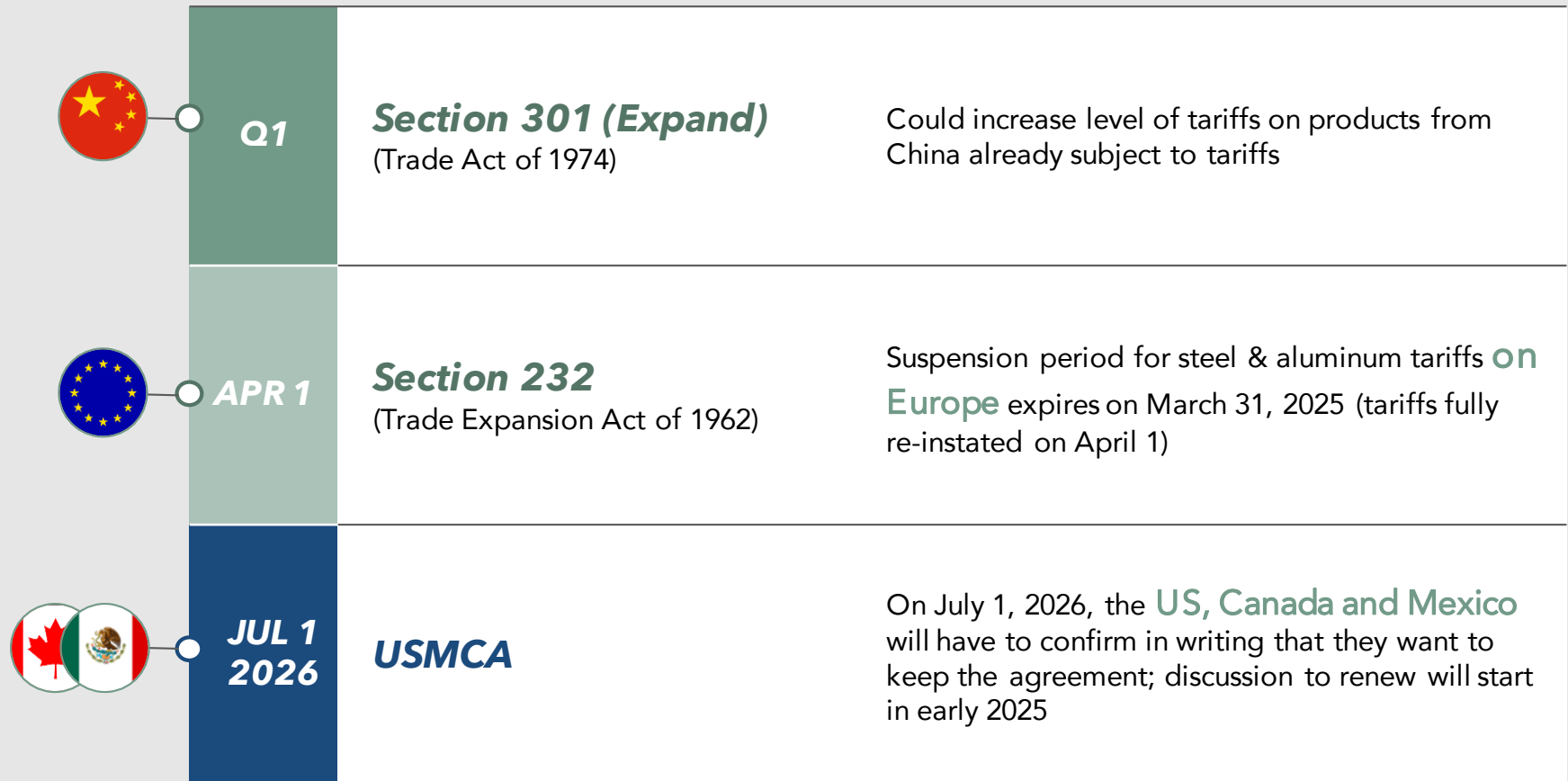
## Potential timeline for Trump 2.0 tariffs

	<b>JAN 2025</b>	<b>Section 338 (New Tariffs)</b> (Tariff Act of 1930)	Could be announced as early as Jan 20 on <b>many or all countries at the same time</b> ; minimum process required (i.e., no investigation period required)
	<b>JAN</b>	<b>Section 203</b> International Economic Emergency Powers Act (IEEPA)	Minimum process required (i.e., no investigation period); could be invoked on <b>China, Mexico and Canada</b> in name of “fiscal” or “immigration” crisis
	<b>Q1</b>	<b>Section 301 (Complaint)</b> (Trade Act of 1974)	Trump could file a formal complaint against <b>China</b> that it is in violation of the Phase One trade deal
	<b>Q1</b>	<b>Section 122</b> (Invoke Balance of Payments Authority)	Trump would have 150 days to impose ad valorem import surcharges (on top of existing) of up to 15%

# Sequencing the Trade War

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## Potential timeline for Trump 2.0 tariffs



# Illustrative Timeline to Appeal US-China Phase 1 Deal

**Enforcement mechanisms are key features of Lighthizer trade agreements.** In light of China's non-compliance with the purchase obligations in the 2020 US-China Phase One deal, the Trump Administration **could file an appeal of the agreement within days of the Inauguration.** This, in turn, would trigger a formal process and timeline that was built into the agreement, leading to potential escalation and even termination of the agreement itself.

**Timeline for Phase One appeal assuming President Trump files formal complaint on or near Jan 20**

1. **Jan 20:** The US could file a formal complaint against China, alleging that it is in violation of the Phase One trade deal.
2. **Feb 3:** China would have 10 working days from receipt of the Appeal to carry out and complete an assessment of the Appeal.
3. **Feb 10:** Officials have 21 calendar days from the date of the receipt of the Appeal to reach a resolution.
4. **Mar 6:** If the Appeal is not resolved by designated officials, the Deputy USTR and China's Vice Minister designate have 45 days from receipt of the Appeal to reach a resolution.
5. **By Apr 6:** If no resolution, the USTR and China's Vice Premier would schedule a meeting within 30 calendar days of the Complaining Party requesting a meeting.
6. **Jun 2025:** Either party is permitted to terminate the Phase One Agreement. The termination would take effect 60 days after the date on which a Party has provided written notice to the other Party, or on such other date as the Parties may decide.

Source: (1) Veda Partners "On Tariffs" (Henrietta Treyz). Tax Foundation. Peterson Institute.





**4** *More Pervasive This Time*

# More Universal Approach This Time

The US has had trade deficits with 106 countries in 2022, up from approximately 80 countries in 1990. Trade war 2.0 will be greater in scale and scope, and markets should not dismiss the possibility of universal tariffs in early 2025 across all products, all countries. At a minimum, we expect a more broad-based announcement involving many product categories and many countries on a scale much larger than the 2018-19 trade wars. In addition, more intense escalation with selected countries is also expected.

■ US trade deficits



## President Trump Tariff Proposals

**5-10%**



Broad-based tariff escalation on many products across many countries (universal tariffs also high risk)

**25-30%**

additional tariffs on China, bringing total to **40-60%**



**5-10%**

tariffs on Mexico and Canada (escalating 5% monthly)



**100-200%**

tariffs on US companies moving production abroad



**100%** tariffs on Chinese EVs made in Mexico



**100%**

tariffs on countries circumventing US dollar trade settlement (i.e., BRICS)

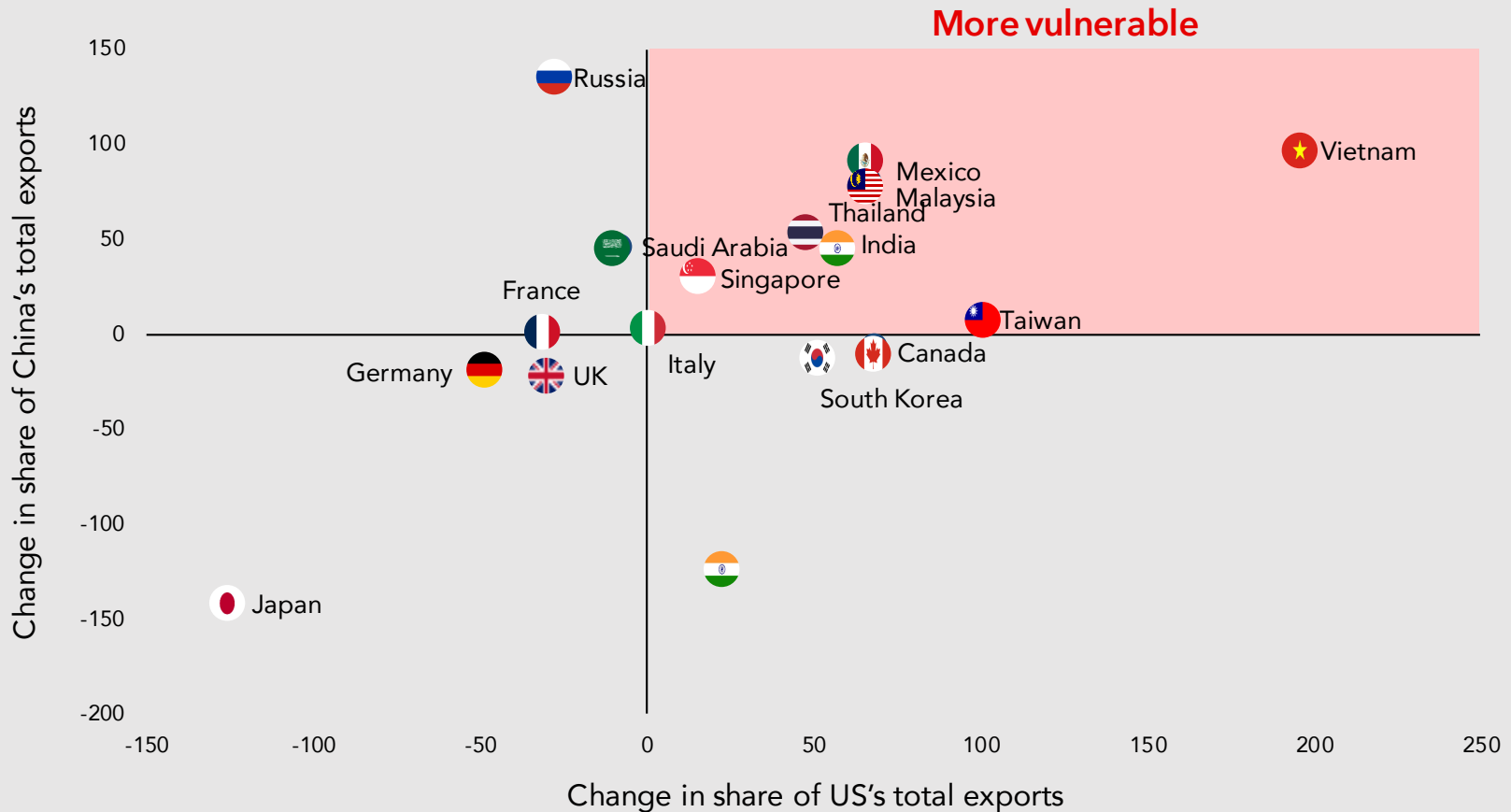


Source: (1) SidleyAustin LLP. World Integrate Trade Solution. Full year data as of 2022.

# Countries More Vulnerable to US Tariff Policy

Following the 2018-19 trade wars, governments and businesses have focused on supply chain diversification to strengthen their resilience to additional trade escalation. However, regions that have increased their trade with China and the US, such as Latin America and South East Asia, are more vulnerable to a Trade War 2.0 scenario.

Change in share of China's total exports vs. change in share of US imports (since 2017)

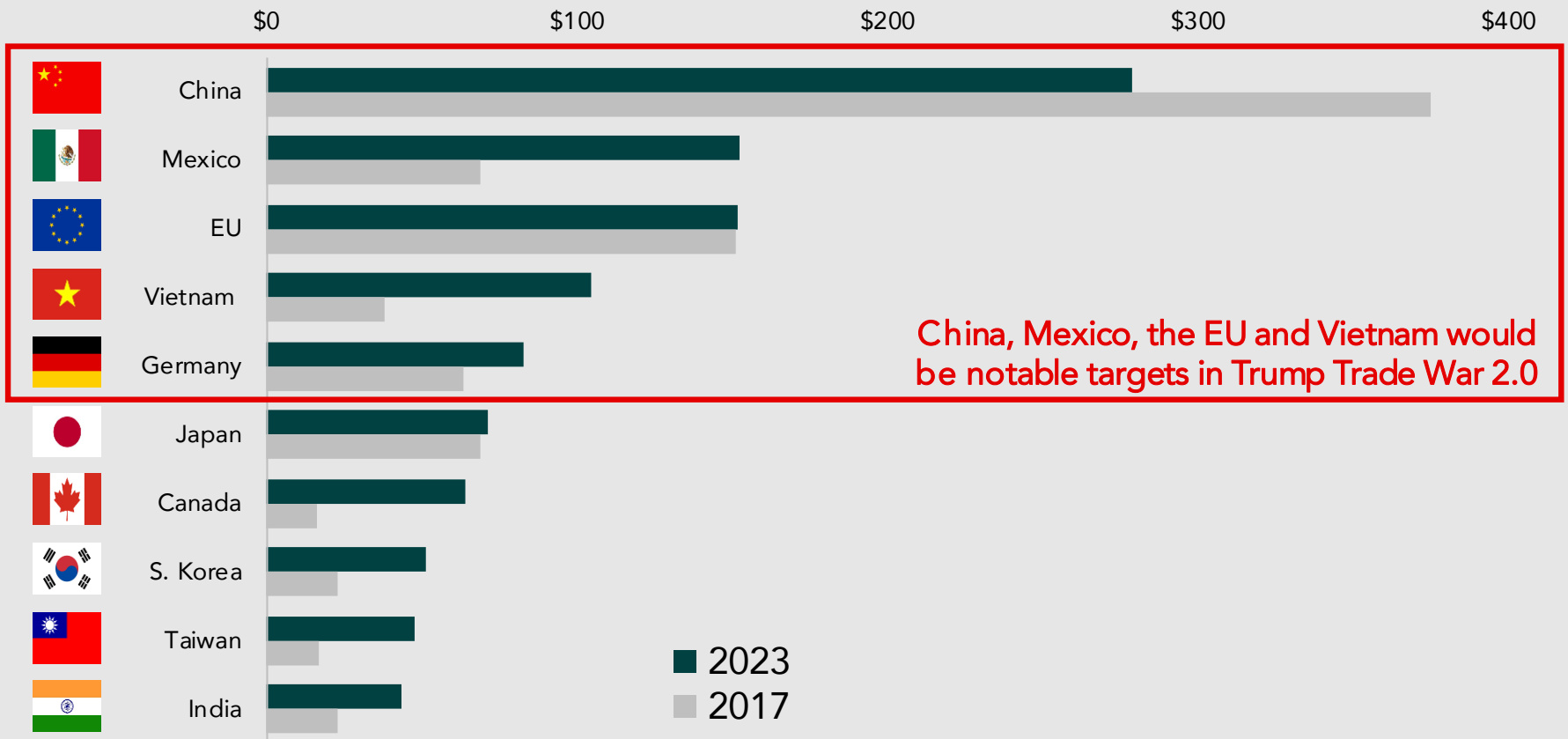


Source: (1) IMF Direction of Trade Statistics. Data as of December 20, 2024.

# Countries with Large US Trade Surpluses More Vulnerable

The US trade deficit with China has declined by nearly \$100 bn since 2017, though has widened with other trading partners in the region, notably Vietnam, South Korea and Taiwan. Look for higher targeted tariffs on both trade counterparties with high surpluses as well as jurisdictions where China supply chains have relocated (i.e., Mexico, Vietnam).

Largest US trade deficits, USD bn









China, Mexico, the EU and Vietnam would be notable targets in Trump Trade War 2.0

Source: (1) US Census Bureau. US trade in goods by country. Nominal USD, not seasonally adjusted, Data as of year end 2023.

# Primary Areas of Impact by Economy

Trade War 2.0 is more likely to be directed toward country of origin than specific product categories. Industries of greater impact will vary by economy.

## Expected impact of higher US tariffs

	Magnitude of Impact	Primary Areas of Impact							
		Tech	Auto	Manufacturing	Steel & Aluminum	Energy / Commodities	Pharma	Chemicals	Food / Agriculture
 Canada	Significant			✓	✓	✓			✓
 Mexico	Significant	✓	✓	✓	✓				✓
 Brazil	Moderate			✓	✓				✓
 EU	Significant		✓				✓		✓
 China	Significant	✓	✓	✓					
 Japan	Significant	✓	✓		✓				







Source: (1) Oxford Economics. Bloomberg. US Census Bureau.



# Primary Areas of Impact by Economy

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## Expected impact of higher US tariffs

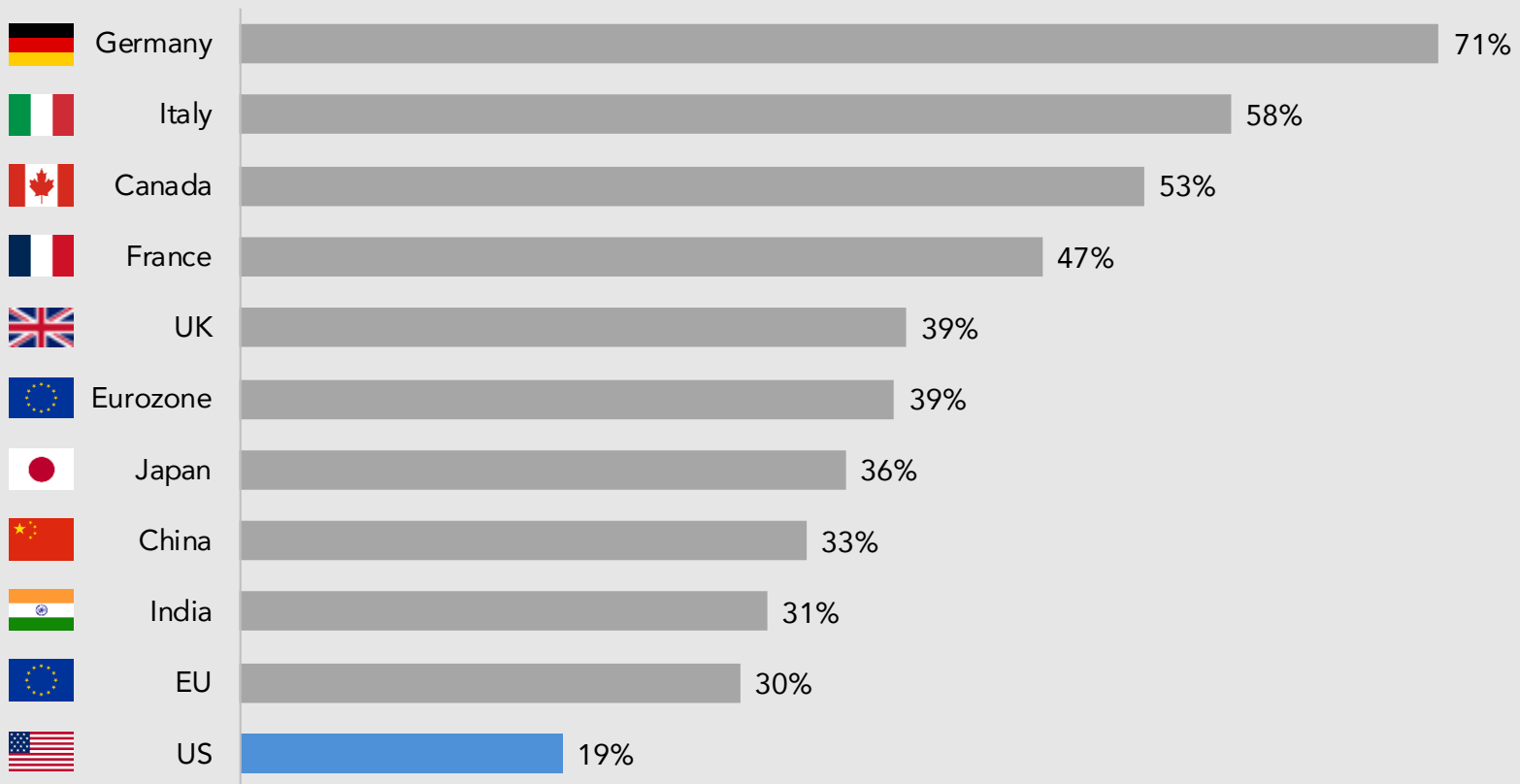
	Magnitude of Impact	Primary Areas of Impact							
		Tech	Auto	Manufacturing	Steel & Aluminum	Energy / Commodities	Pharma	Chemicals	Food
 India	Significant				✓		✓	✓	
 Taiwan	Significant	✓							
 South Korea	Significant	✓	✓	✓	✓				
 Vietnam	Significant		✓	✓					
 Thailand	Moderate	✓		✓					
 Indonesia	Significant					✓			

Source: (1) Oxford Economics. Bloomberg. US Census Bureau.

# Economies More Reliant on Trading “Goods” More Vulnerable

As happened in 2018-19, manufacturing and trade-intensive economies are more vulnerable to trade policy escalation than consumer-driven and services-based economies.

## Goods trade, as % of GDP

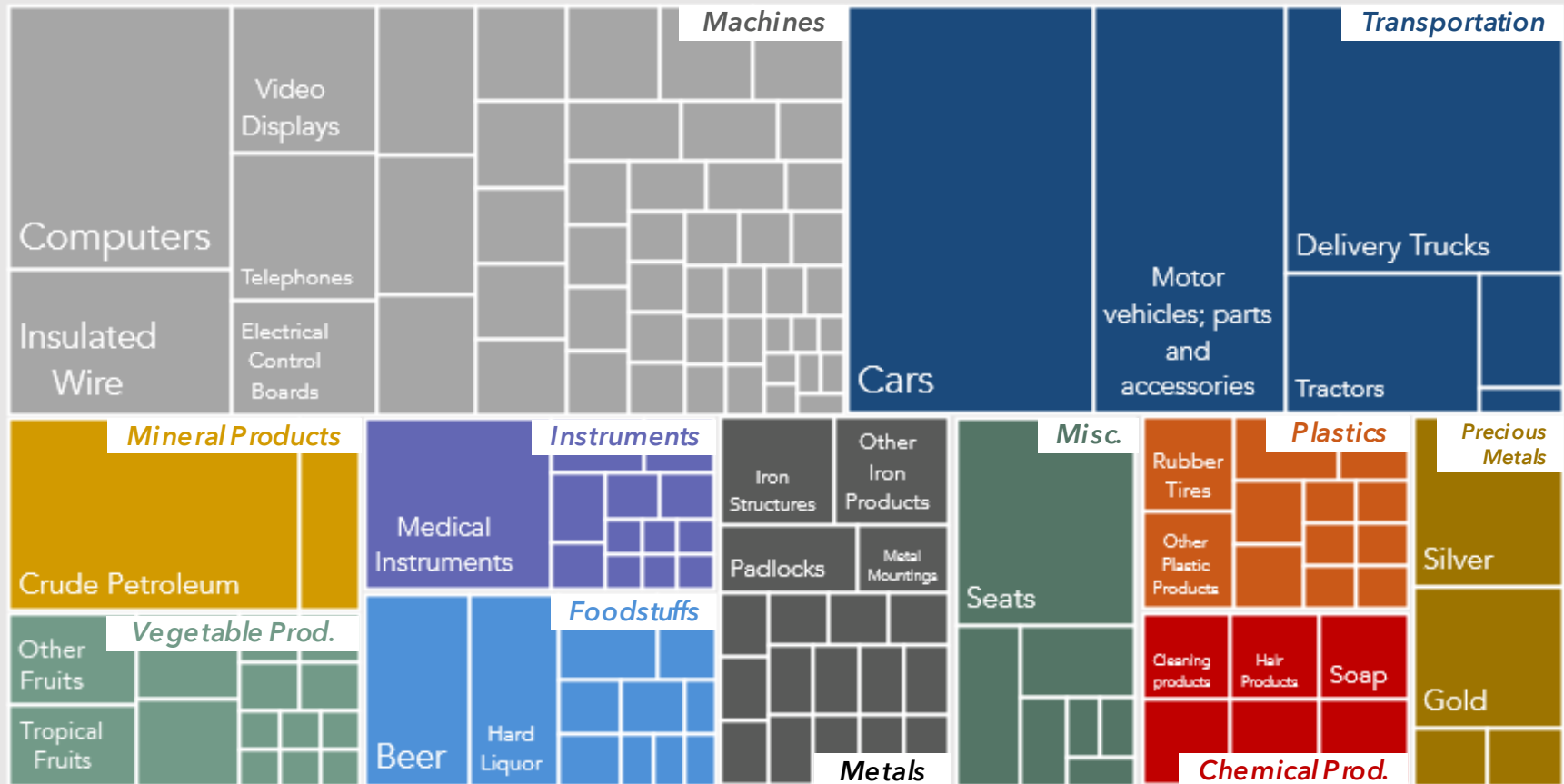


Source: (1) FT, "Tariffs and taxes are not very inflationary." ECB. World Bank. Data is 2023.

# Breakdown of US Imports from Mexico



Share of imports from Mexico

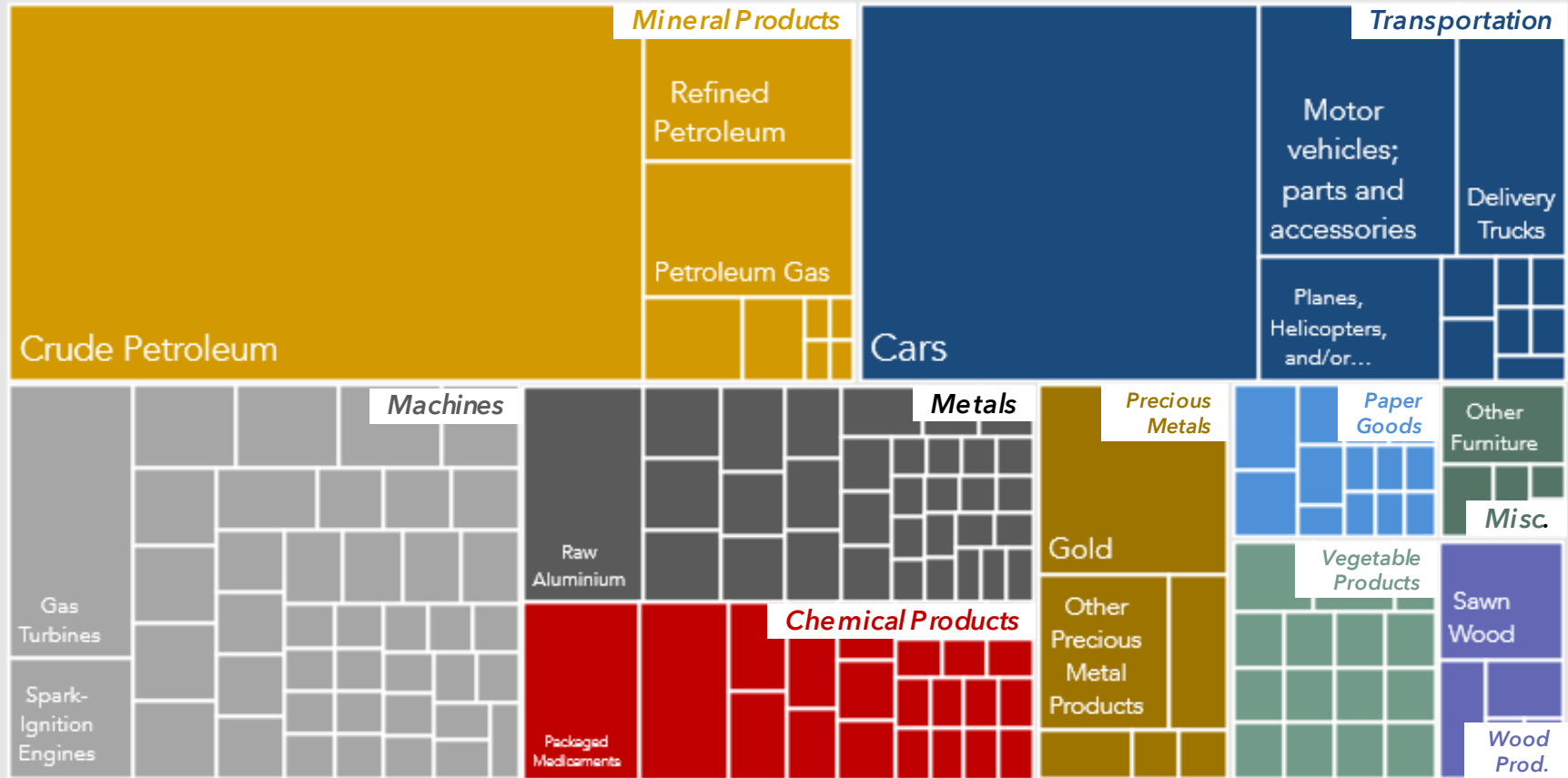


Source: (1) Financial Times, "How to deal with Donald Trump's tariff threats". US Census Bureau. Data for 2023.

# Breakdown of US Imports from Canada



Share of imports from Canada

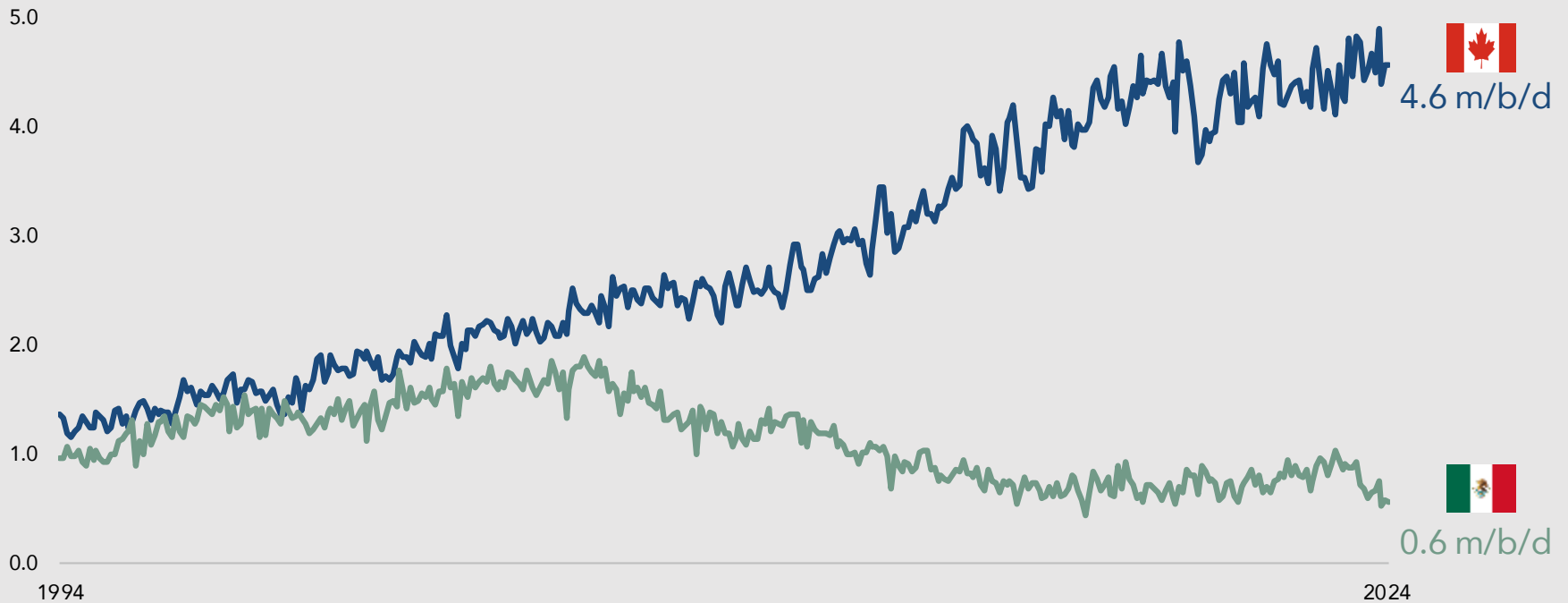


Source: (1) Financial Times, "How to deal with Donald Trump's tariff threats". US Census Bureau. Data for 2023.

# Canada's Energy Sector Potentially Vulnerable

President Trump's focus on US energy expansion, and Canada's large crude oil exports to the US, create an obvious target for US tariff escalation. However, the Administration may be cautious on directly and quickly escalating energy prices for US consumers.

Monthly US crude oil imports from Canada and Mexico, million barrels per day



**Canada is allegedly preparing a basket of retaliatory tariffs > \$100 bn, including outright bans on uranium, potash, copper, nickel, zinc and other critical minerals.**

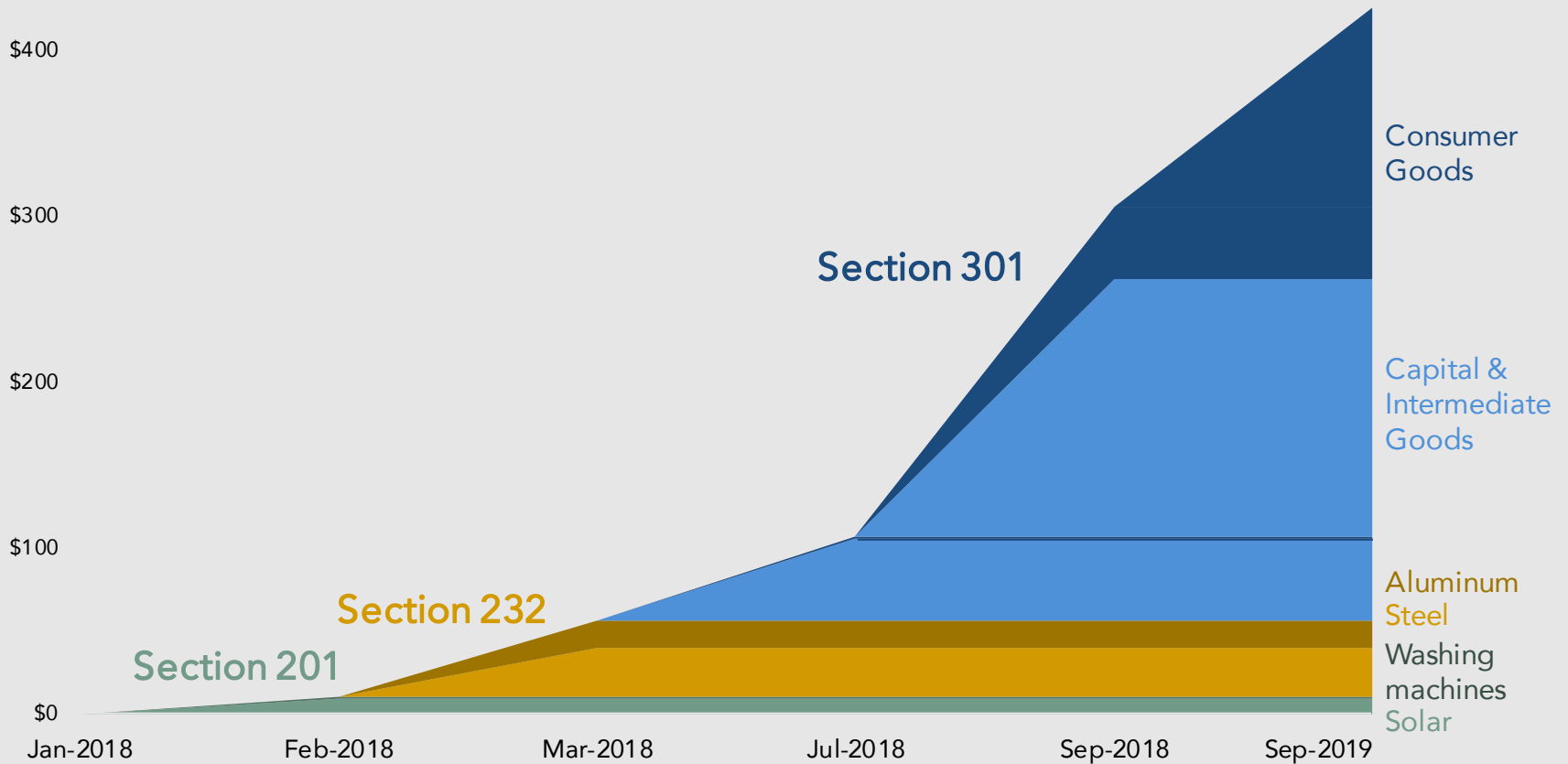
Source: (1) EIA. US imports by country of origin. Data through October 2024.



# Consumer Goods Generally Targeted Later

In the 2018-19 trade wars, consumer goods were generally targeted later than industrial, capital and intermediate goods. The more broad-based and universal approach of Trump 2.0 tariffs make consumer-facing goods comparatively more vulnerable this time. However, forward start dates on tariffs and a monthly escalation schedule provide opportunities to delay the impact.

Value of US import tariffs, USD bn



Source: (1) Federal Reserve. PIIIE. Capital & intermediate goods includes transport goods and others. List 4A assumes that all \$120bn of import tariffs affect consumer goods.



**5** *More Complete  
US-China Decoupling*

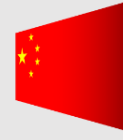
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# Trump's Enduring Legacy: More Complete US-China Decoupling

Longer term, the most enduring legacy of President Trump's two-term policy agenda may prove to be a more complete US-China decoupling across trade, investment, technology and capital markets.

## US decoupling from China

1. Trade wars, tariffs (50-60%)
2. Supply chain movement "away from China"
3. Possible revocation of China's PNTR status
4. Tech licensing restrictions & export controls
5. Inbound & outbound FDI restrictions
6. Outbound investment screenings
7. Capital wars: financial market restrictions
8. Entity List commercial restrictions
9. Social media platform bans
10. Geo-strategic rivalry



## China decoupling from US

1. Retaliatory tariffs
2. Reducing US trade and tech dependency
3. Slowing pace of UST purchases
4. Unreliable entity listings
5. Anti-foreign sanctions enforcement
6. Export controls (minerals & rare earths)
7. Higher regulatory pressure on US corporations
8. Market access restrictions
9. Pivoting away from US agriculture
10. Geo-strategic realignment away from the West

**"After 30 years of globalization, we now face the very real prospect that an economic iron curtain may descend."**

Former US Treasury Secretary, Henry Paulson, in Singapore in November 2018

# Whole of Government Approach to China



The US has adopted a “whole of government approach” on China policy, a rare arena of general agreement among Democrats and Republicans. Notably, US-China policy is emanating from a broad range of institutions with comparatively high and low China expertise, as well as from those with relatively more and less active dialogue with China counterparts and US allies.

## Selected branches and agencies of the US government driving China policy



**CFIUS**

Committee on Foreign Investment  
in the United States



**US Committee for the  
Assessment of Foreign  
Participation in the US  
Telecommunications  
Services Sector**



National Institutes  
of Health

**National Science  
& Technology  
Council**

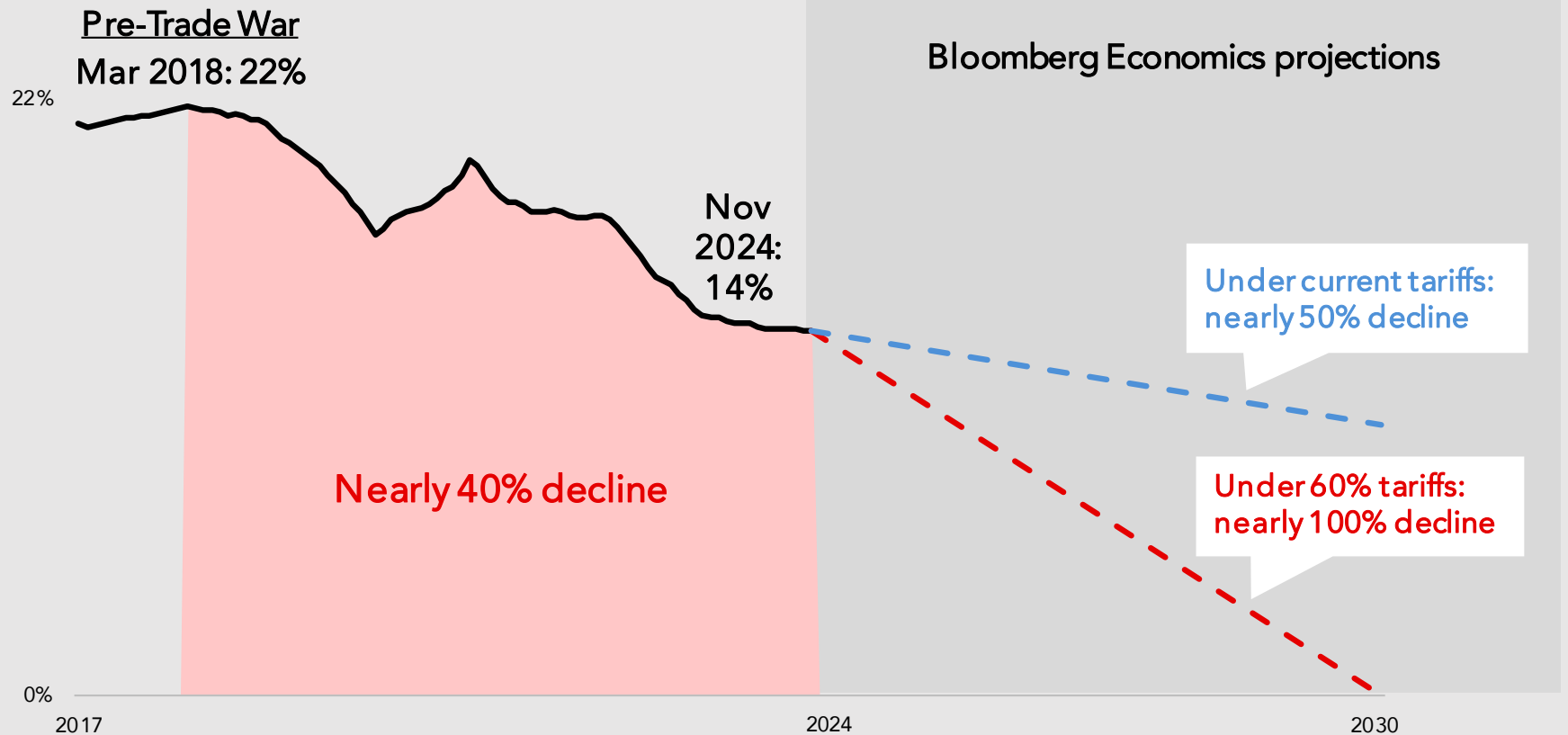


Source: White House. National Archives. “US Strategic Approach to the People’s Republic of China”. Council on Foreign Relations “Timeline: US-China Relations”

# US-China Trade Could Collapse in Trade War 2.0

According to analysis by Bloomberg Economics, **an across the board tariff of 60% would likely reduce US imports from China almost entirely**. In addition, based on the "tit-for-tat" pattern during Trump's first term, China would likely retaliate leading to a reduction in US exports to China to nearly zero, an annual loss of about \$150 bn.

Share of US goods imports from China



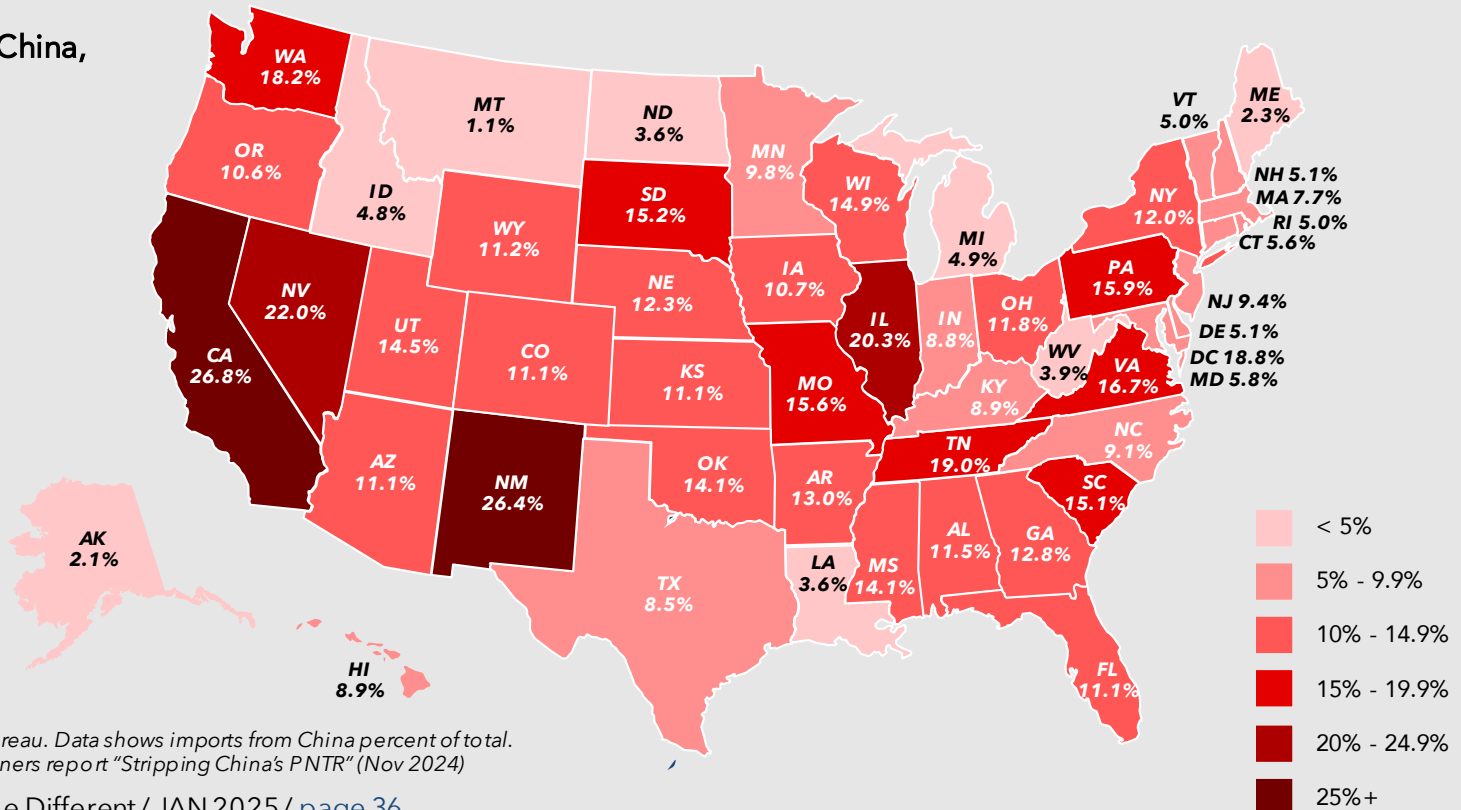
Source: (1) US Census Bureau. Data is rolling 12-month average through November 2024. Bloomberg, "Trump's Endless Trade War Will Damage US as Well as China" (Orlik).



# Revoking China's PNTR Status Will Be Difficult

While the Trump Administration does not need Congress to act on trade, they want Congress to act. Over the last few decades, the US Congress has introduced, but not passed, several bills to revoke China's Permanent Normal Trade Relations (PNTR) status. Though very difficult to do, revoking China's PNTR status would: (1) sharply increase tariffs on all US imports from China; (2) create significant, and much needed, "revenue" for Trump tax and spending priorities; and (3) permanently alter and damage the US-China trade landscape. Though risk for this transformative policy change remains high in 2025, it will be a heavy lift for the very narrow majorities in the US Congress (especially agriculture states) and would receive enormous blowback from the US business community.

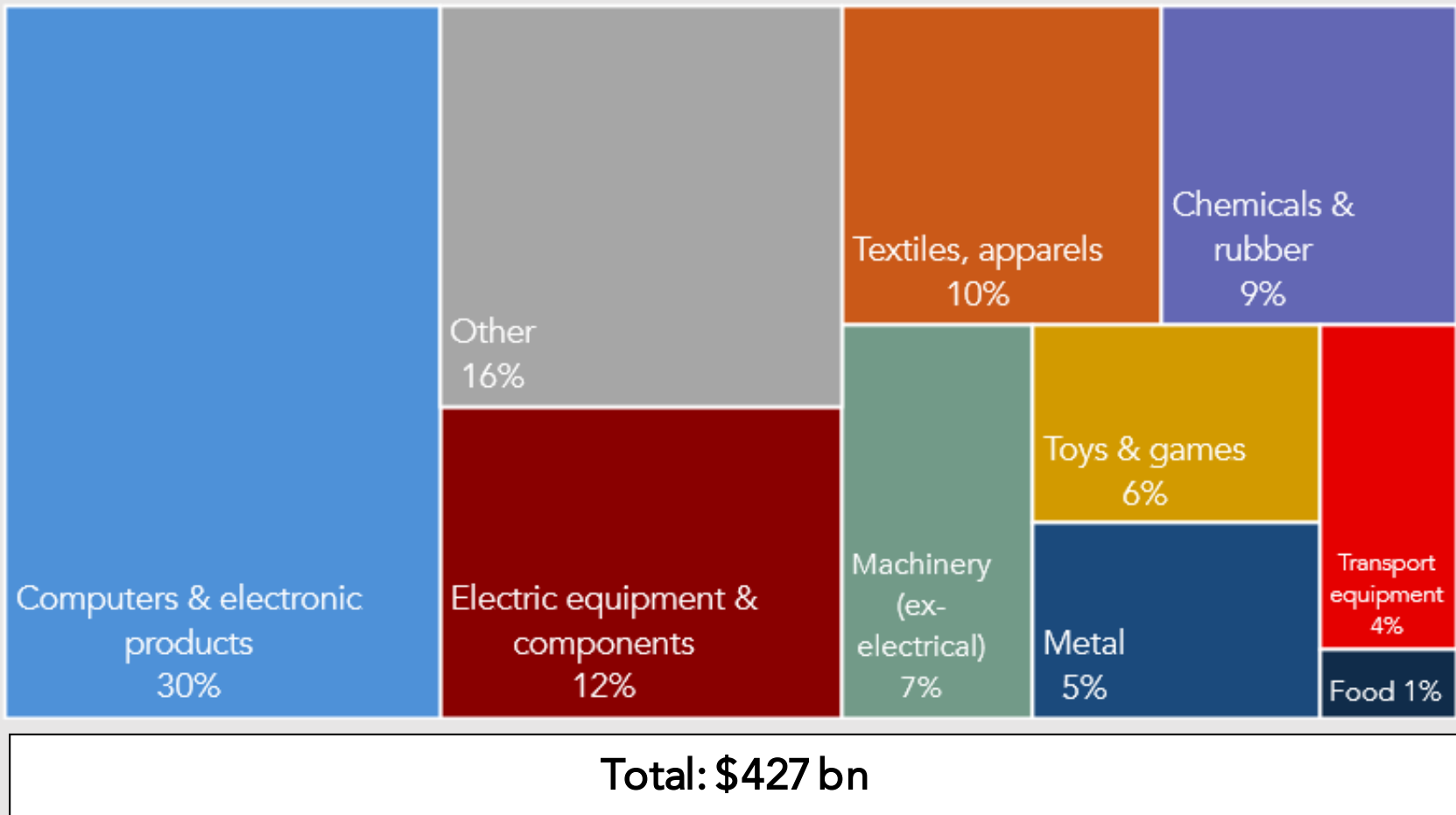
US imports from China, by state (2023)



Source: (1) US Census Bureau. Data shows imports from China percent of total. Henrietta Treyz Veda Partners report "Stripping China's PNTR" (Nov 2024)

# Breakdown of US Imports from China

US imports from China, by value



Source: (1) Fitch. US Census Bureau. Data represents imports for 2023.

# House Select Committee on the CCP



The House Select Committee on the Chinese Communist Party was founded on January 10, 2023 with strong bipartisan support. In the 119<sup>th</sup> Congress sworn in on January 3, 2025, Representative John R. Moolenaar (R - MI) will chair the House Select Committee, with Representative Raja Krishnamoorthi (D - IL) as the top Democrat, focusing on economic and security competition with the Chinese Communist Party.

## Republican members:



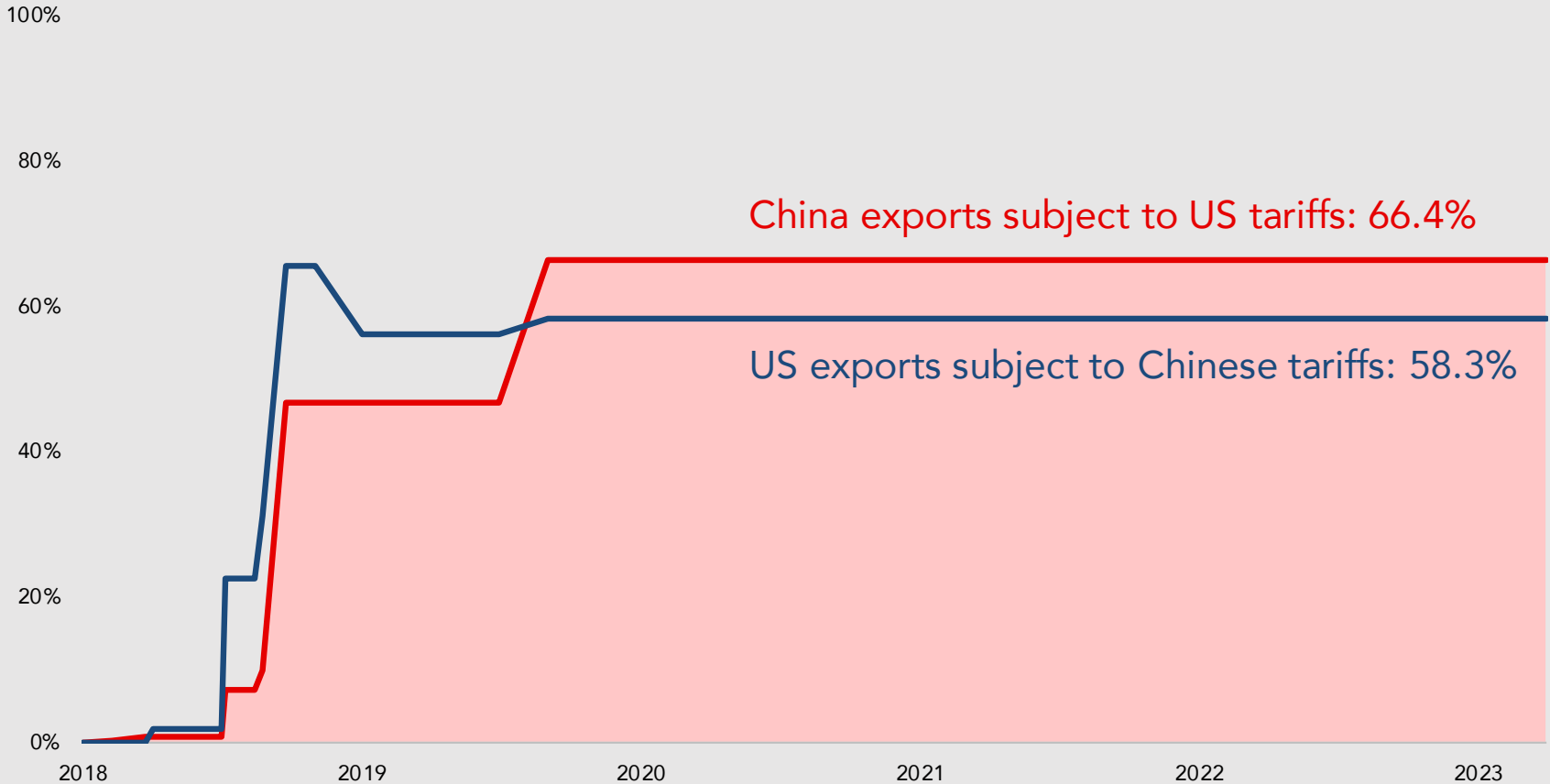
## Democrat members:



# Nearly 2/3 of US-China Trade Already Subject to Tariffs

Today, approximately 2/3 of US-China trade is already subjected to tariffs. President Trump will increase the rate and expand the scale of US imports from China subject to tariffs.

Percent of US-China trade subject to trade war tariffs



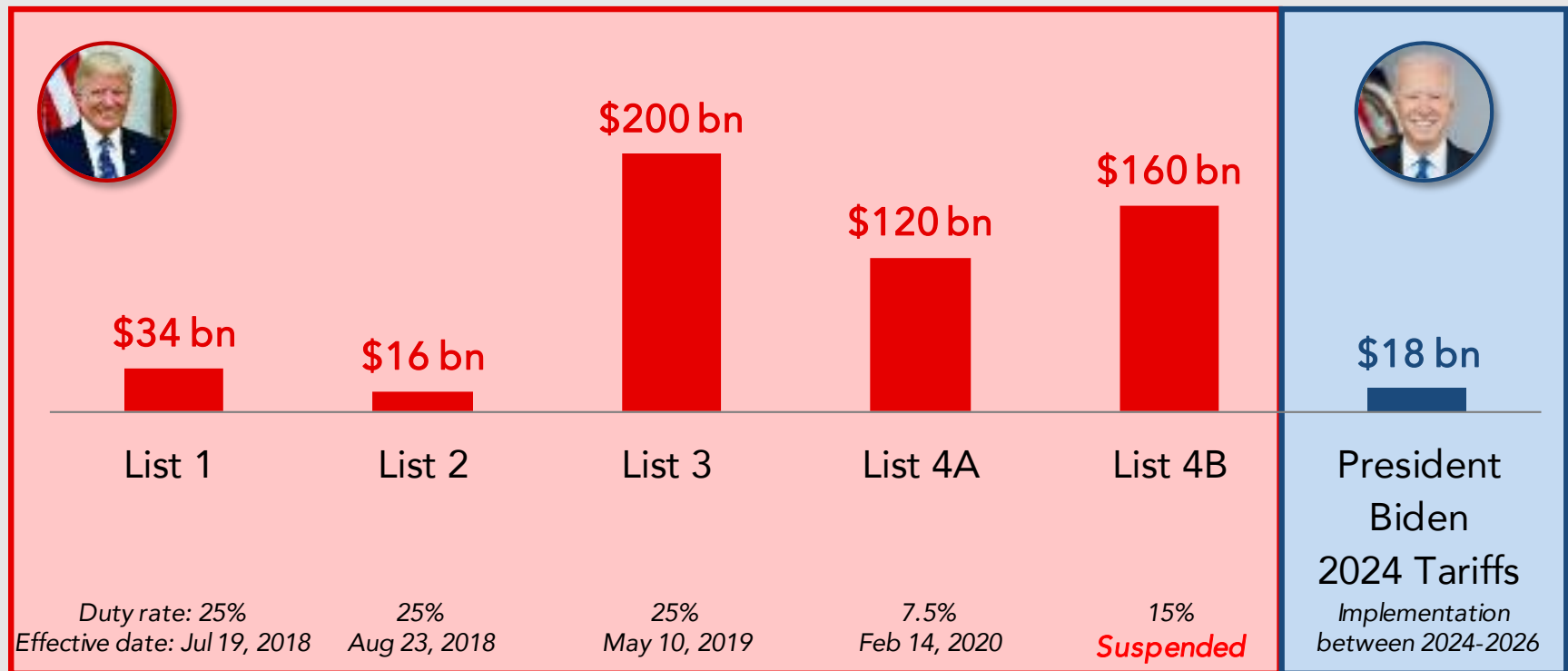
Source: (1) Peterson Institute for International Economics, "US-China Trade War Tariffs" (Chad Bown).

# Existing \$400bn of US-China Tariffs



Between 2018 and 2020, former President Trump announced and implemented tariffs on over \$500 bn of US imports from China, though roughly \$160 bn of “List 4” tariffs were suspended in the subsequent “Phase One” trade deal with China. While comparatively smaller, President Biden’s additional tariffs target industries critical to energy transition, tech leadership and national security such as electric vehicles, semiconductors, solar, manufacturing and defense.

## Section 301 China tariffs based on import good value at time of tariff implementation

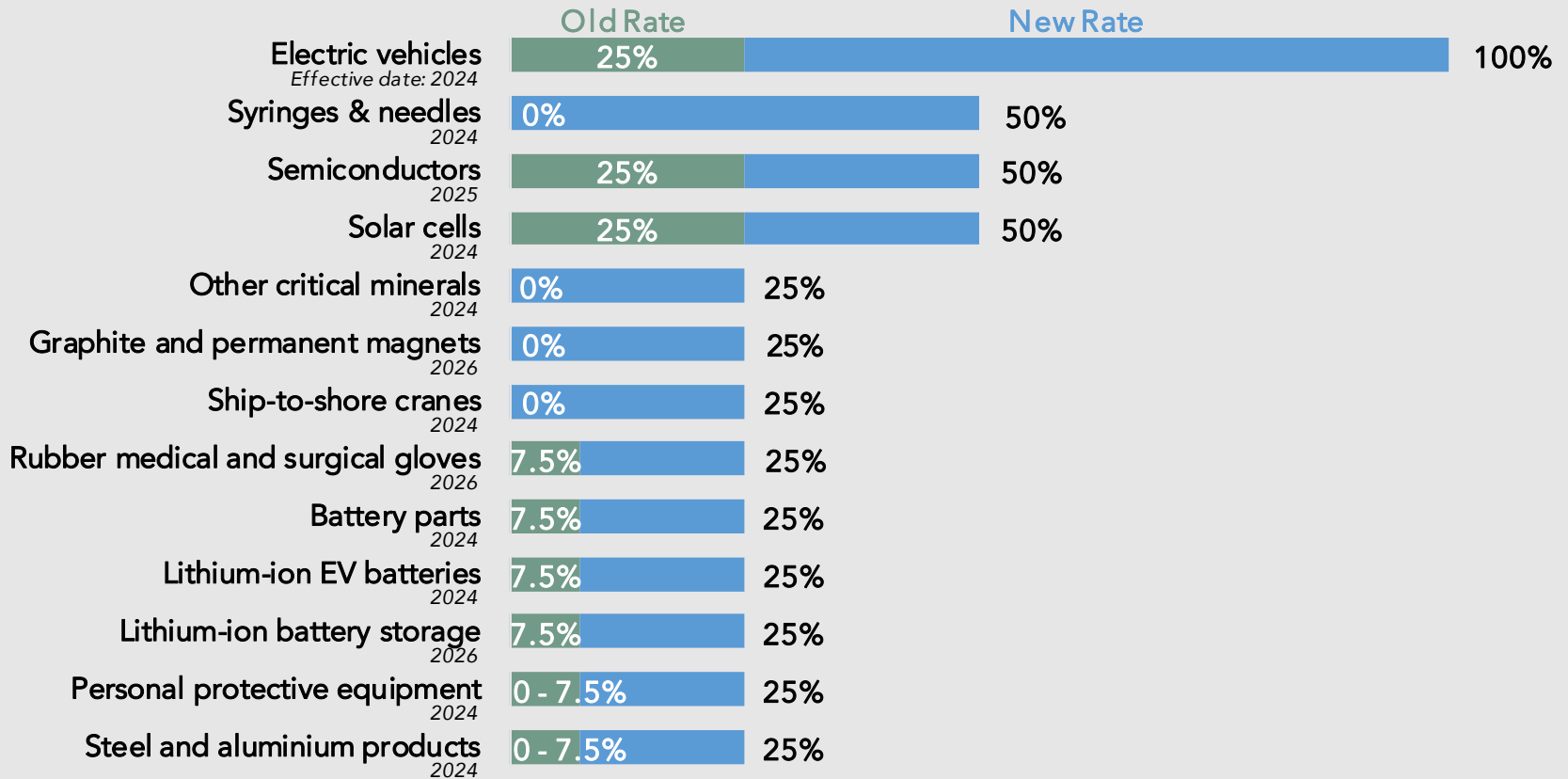


Source: (1) ST&R, “Section 301 Tariffs on China.” Tax Foundation, “Tracking the Economic Impact of U.S. Tariffs and Retaliatory Actions.”

# 2024 Biden Tariffs Targeted Tech & EV

President Biden announced tariffs ranging from 25% to 100% on \$18 bn of US imports from China. While the targeted tariffs further Biden's efforts to support the domestic semiconductor industry and block China from critical emerging technologies, the macro implications are expected to be minimal. The \$18 bn of impacted goods represent just 4% of US imports from China and 0.5% of China's total exports.

## Newly imposed tariff rates on US imports from China by product



Source: (1) The White House, "Fact Sheet: President Biden Takes Action to Protect American Workers and Businesses from China's Unfair Trade Practices". Financial Times, "Why Washington's new tariffs on Chinese clean tech goods matter". Bloomberg, "Biden Adds Tariffs on Chinese Chips, Critical Minerals, EVs". Data as of May 14, 2024.





**6** *China is Ready This Time*

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# China is Ready This Time



China and President Xi Jinping arguably misread President Trump time and again in the 2018-19 trade wars. Not this time. Even with an economy under pressure, China's policy toolkit is formidable and the world's second largest economy has prepared powerful countermeasures to retaliate against US companies and markets. China's response is likely to be measured and surgical, but powerful nonetheless.



**Fiscal stimulus:** extensive policy toolkit still available to support the economy. CNY trillions of additional stimulus available, if needed.



**Currency devaluation:** CNY depreciated 10% in 2018-19 trade war to offset impact of tariffs



**Targeted tariffs:** comparable retaliation directed toward US agriculture and other sensitive sectors



**Export controls:** restrictions on key raw materials and rare earths critical to semiconductors and electronics (lithium, gallium, germanium, antimony)



**Entity list:** expansion of sanctions and "unreliable" entity list directed toward US companies



**Selling USTs:** at ~\$800 bn, China is the 2nd largest foreign holder of US debt



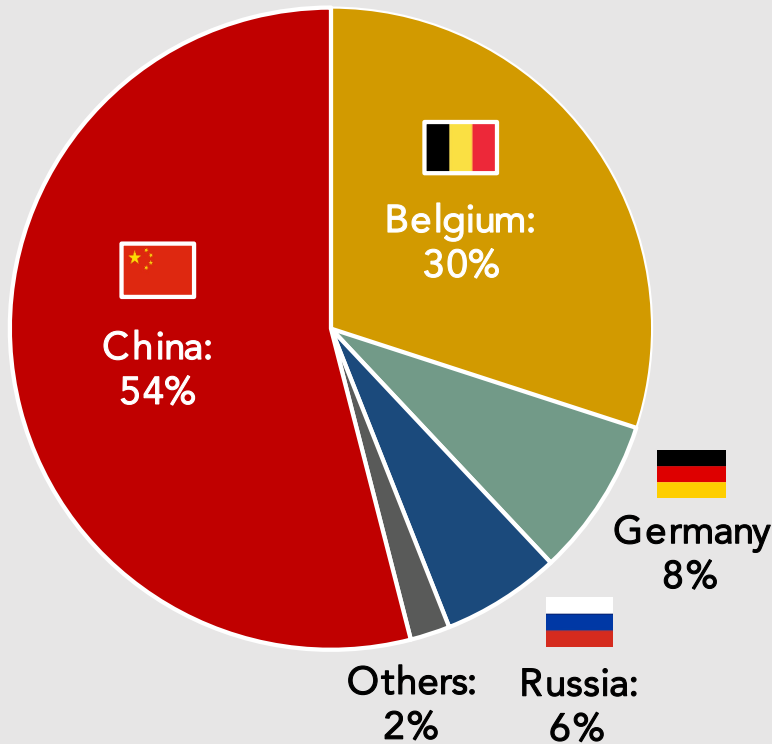
**Redirecting trade:** well underway over last decade. Less exposure to Washington. More outreach to Europe & emerging markets.

Source: (1) FT, "China Arms Itself For Potential Trade War With Donald Trump." OpenSanctions. China's Ministry of Foreign Affairs, Ministry of Commerce. The entity list was enacted in 2020 and first applied in Feb 2023, the anti-foreign sanctions law was passed in June 2021 and first used in July in the same year.

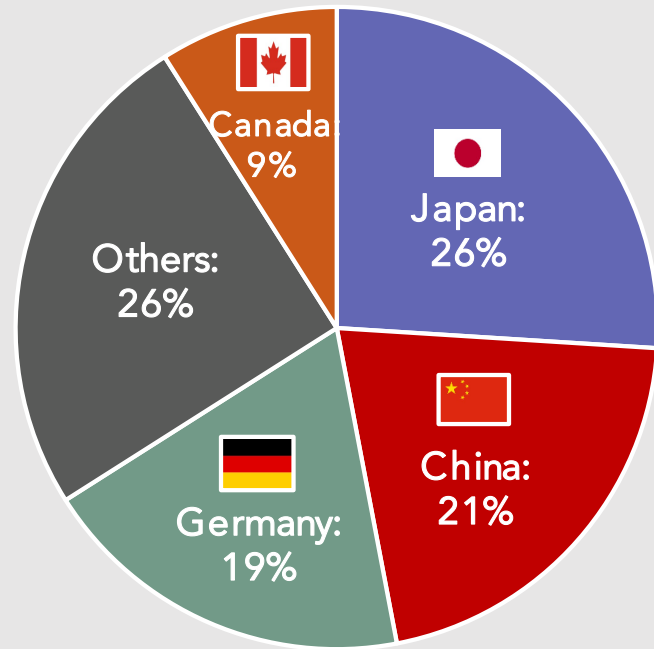
# China's Targeting of Strategic Minerals

In response to the Biden Administration's new package of export controls, China imposed a ban on all exports of gallium, germanium, antimony and superhard materials to the US. China is the top global supplier of dozens of strategic minerals, many used for high-tech and military applications. Following the restrictions that China imposed on gallium and germanium last year, American industries were forced to draw on inventories or source the materials from different countries.

Sources of germanium imported into US, by country



Sources of gallium imported into US, by country



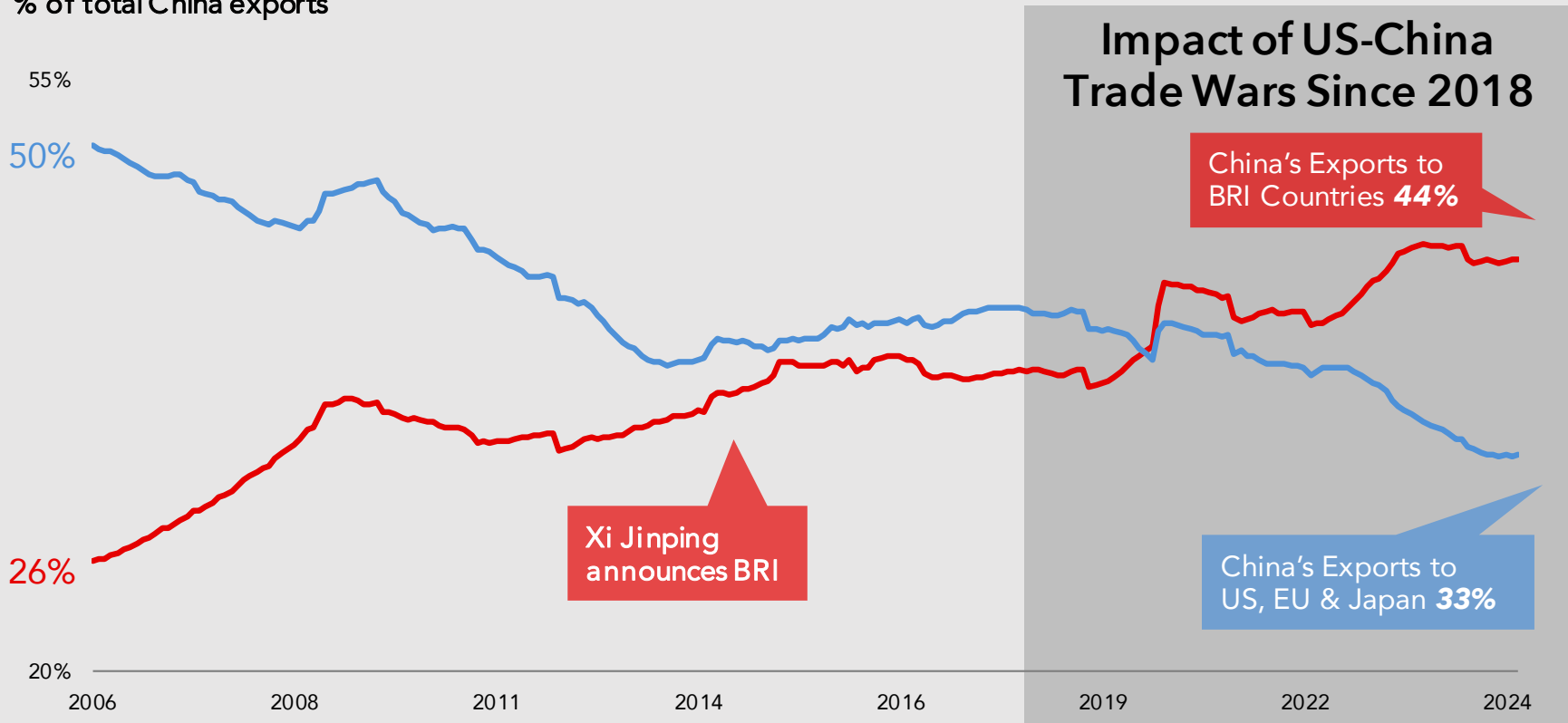
Source: (1-2) US Geological Survey. Data covers 2019-2022 period. Data for germanium is germanium metal only.

# China's Global Trade Realignment



Since announcing the Belt & Road Initiative (BRI) in 2013 and the US-China trade wars which began in 2018, China has accelerated its efforts to reconstruct its global trade footprint in a manner that is more focused on developing (EM) economies, and less dependent on the United States and the Western-dominated post WWII trading architecture (i.e., WTO). Today, Beijing has negotiated bilateral and regional "free trade agreements" (FTAs) with nearly 30 countries accounting for nearly 40% of its \$3.4 trillion in exports in 2023 (world's largest exporter).

% of total China exports



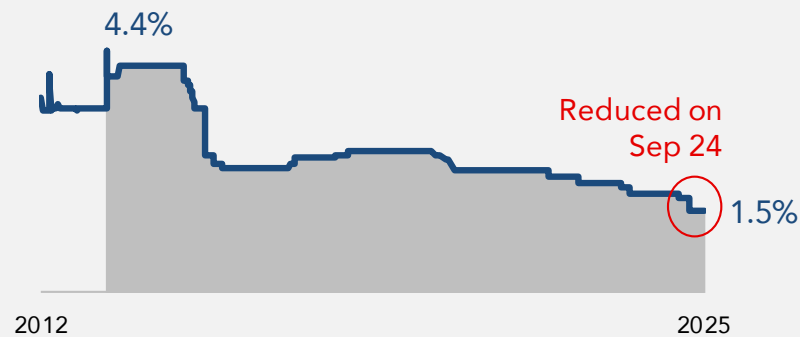
Source: (1) Bloomberg. Data through November 2024. China trade in USD terms. Customs General Administration PRC. Financial Times "China's Plan to Reshape World Trade on Its Own Terms" (Feb 25, 2024).

# China Saving "Dry Powder" for "Trade War"

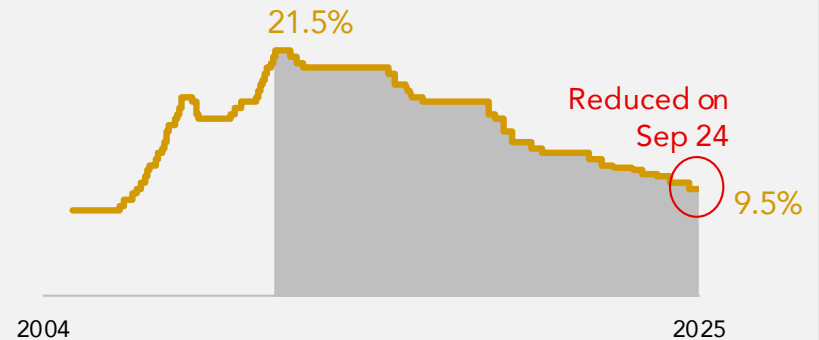


As part of the September 24, 2024 announcement, the PBoC surprised the market with a broad based package of rate cuts, including its largest ever decrease to its 1-year medium term lending facility interest rate. The PBoC continued its efforts to support the economy by lowering the 1-year loan prime rate by 25 bps in October, more than the market expected and the largest reduction on record.

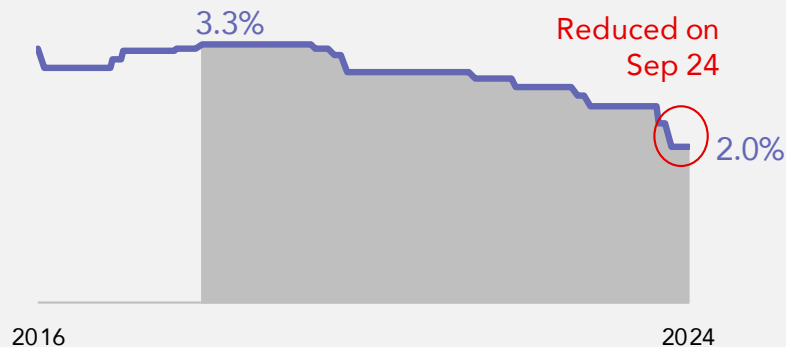
## 7-day reverse repo rate



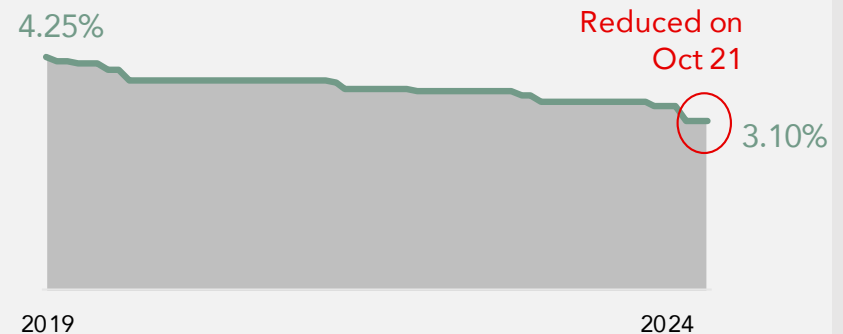
## China reserve ratio for major banks



## 1-yr medium term lending facility interest rate



## 1-year loan prime rate



Source: (1-4) Bloomberg. Data as of January 16, 2025.

# China Saving “Dry Powder” for “Trade War”



Much of President Xi’s COVID-era policy response targeted the supply side of China’s economy. In a sign of renewed economic stress, Xi overcame his reticence with “demand-side” stimulus with a litany of new policy measures announced in late September 2024. Though the market has been expecting even larger policy measures, it appears that Xi is saving “dry powder” in his policy toolkit to evaluate the scale and scope of President Trump’s trade war escalation.

China’s announced policy measures since September 2024



## Monetary Easing

- **7-day reverse repo rate cut by 20bps:** Surprised markets that expected smaller, gradual cuts
- **Reserve requirement ratio (RRR) cut by 0.5%:** This move frees up CNY 1 trillion (\$142 billion) in liquidity and could be followed by another 0.25-0.50% cut later this year
- **1-Year MLF rate cut by 30bps:** Further easing to stimulate credit and investment
- **1-Year & 5-Year loan prime rate cuts by 25bps:** Lower interest rate payments on existing loans; reduce the price of new loans



## Property Market

- **Lower mortgage rates for existing loans:** Aims to provide relief for households, while stimulating household spending and investment
- **Down payment ratio for second homes cut to 15% from 25%:** Aimed at reviving property market activity
- **Affordable housing initiative:** PBoC will fully fund a CNY 300 bn loan initiative to enable SOEs to purchase unsold homes and convert them into affordable housing units



## Capital Markets

- **Debt Swap Plan:** CNY 10 trillion (\$1.4 trillion) program to help local government tackle their “hidden debt” (debt accumulated through local gov financing vehicles), including a CNY 6 trillion increase in debt ceiling
- **CNY 500 bn liquidity support for Chinese stocks:** Funds and brokers now have access to PBOC liquidity to buy stocks, signaling strong support for equity markets.
- **Relending facility:** Relending facility of CNY 300 bn (with an interest rate of 1.75%) to guide banks to support listed companies’ stock buybacks and purchases.

Source: MUFG FX Focus, “Review of China Stimulus Plan and Market Implications” (September 27, 2024). Oxford Economics, “PBoC Offers a Full Package of Stimulus Following the Fed’s Bold Cut” (September 24, 2024). Capital Economics. China Briefing, “Decoding China’s Recent Economic Stimulus Package: What Investors Need to Know.”

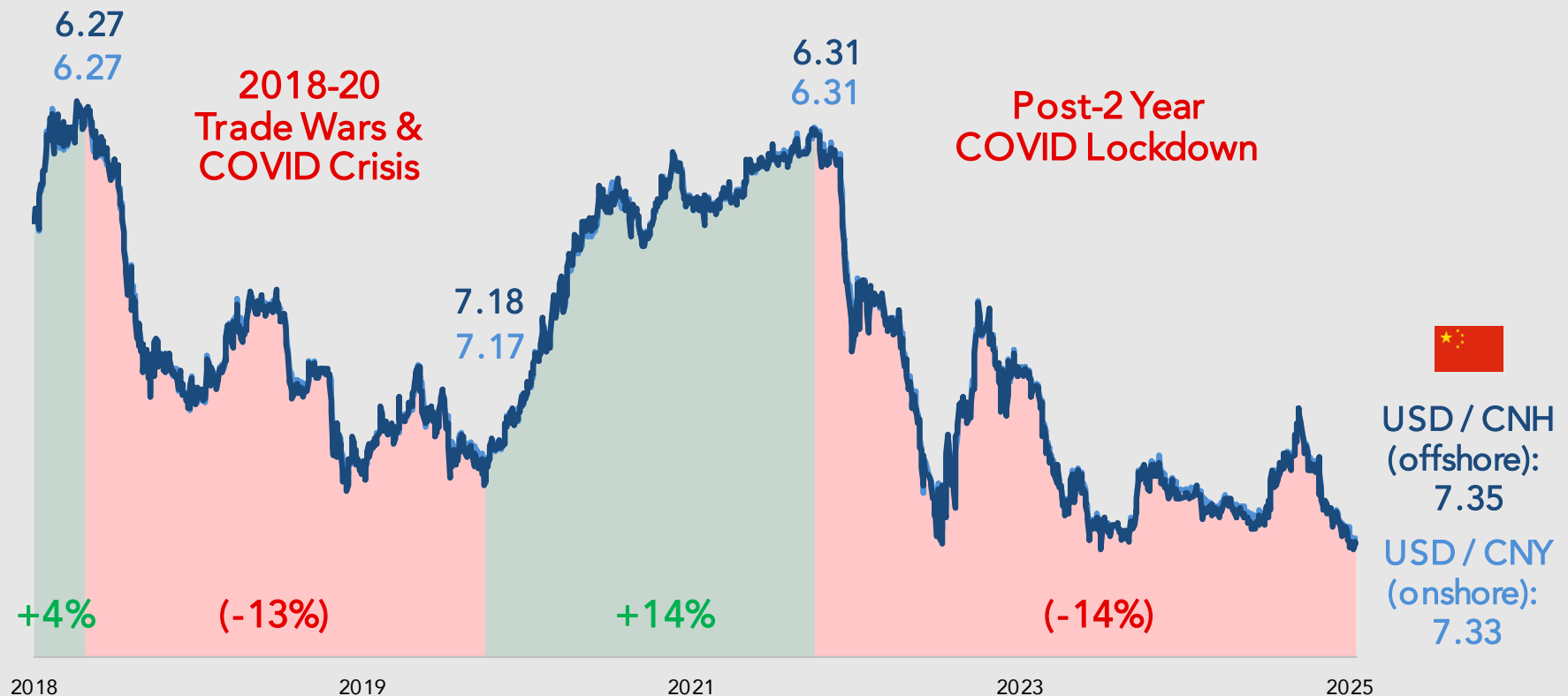


# China's CNY Currency Depreciation



During the 2018-19 trade wars, China's currency depreciated more than 10% to offset the impact of US tariffs. MUFG's FX Strategy team, led by Derek Halpenny, expects Beijing to adopt a "more proactive" fiscal policy in 2025 in response to growth and trade policy headwinds. Assuming average tariffs on US imports from China rise from approximately 20% currently to 40% in 2025, MUFG is forecasting USD/CNY to depreciate to 7.40 in Q1 and 7.50 in Q2.

CNY (onshore) & CNH (offshore) vs. USD



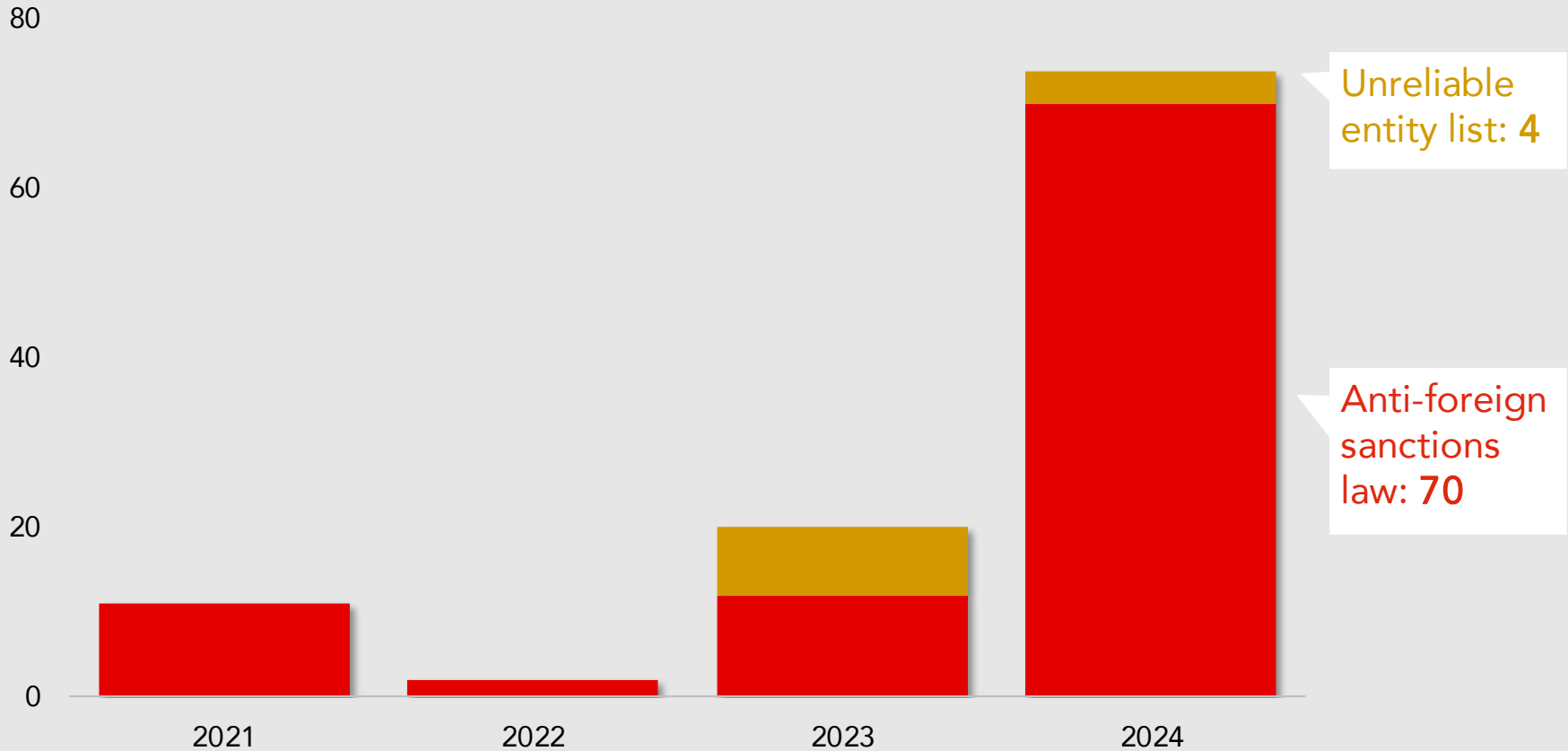
Source: (1) Bloomberg. CNY & CNH graphed vs. USD to show depreciation. Change shows change in CNY vs. USD. Data as of January 16, 2025.

# China's Corporate Sanctions Toolkit



As US-China policy escalation accelerates, China has been adding US entities and companies to both its export control list and its "unreliable entity list." Targeted companies and individuals face punitive measures including restrictions on import / export activities, FDI investment, work permits, residency and China travel.

Number of US individuals and groups under Chinese sanctions



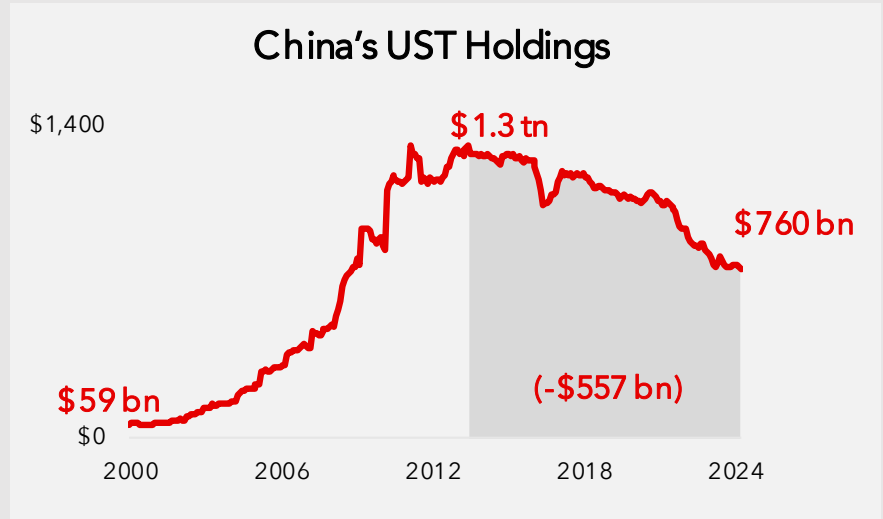
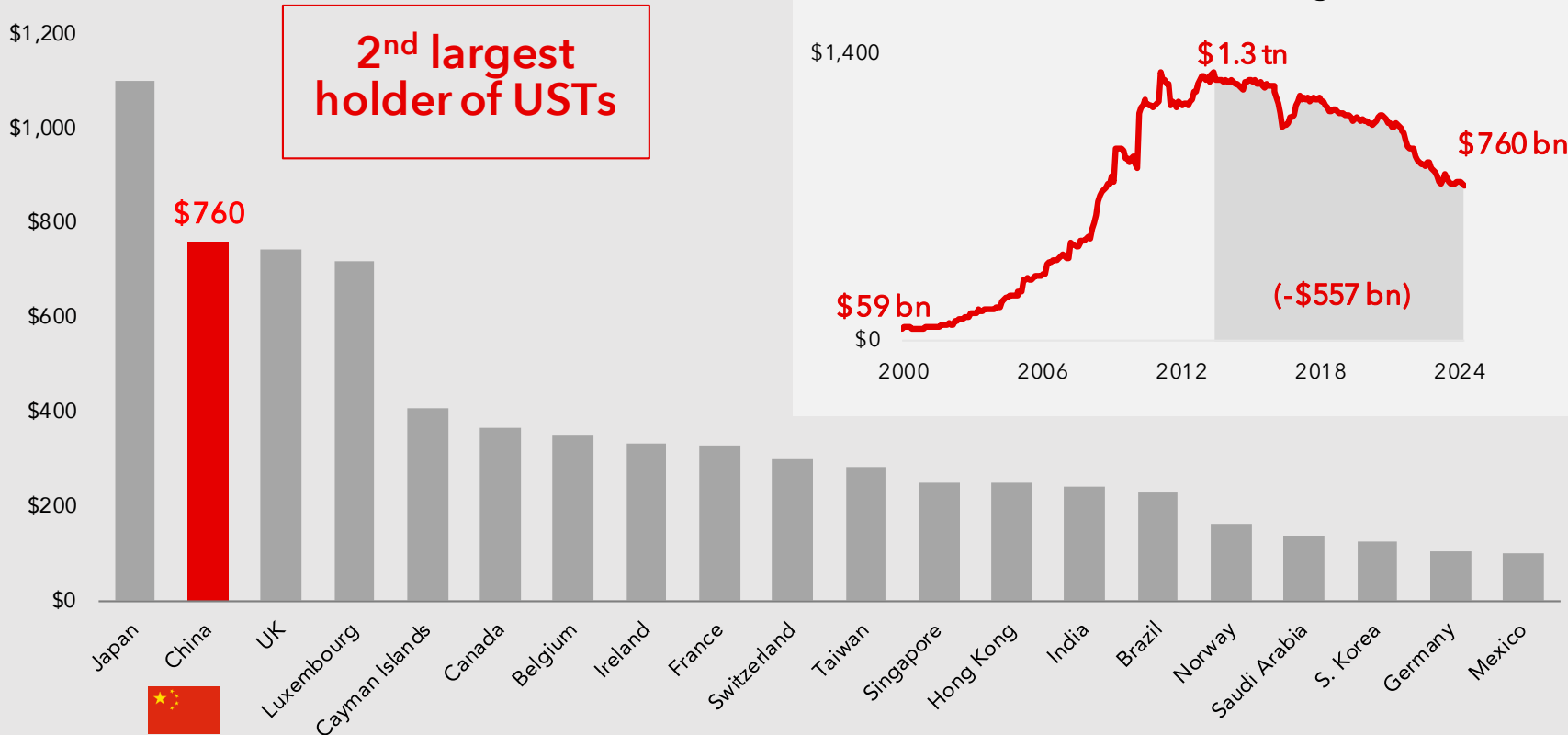
Source: (1) FT, "China Arms Itself For Potential Trade War With Donald Trump." OpenSanctions. China's Ministry of Foreign Affairs, Ministry of Commerce. The entity list was enacted in 2020 and first applied in Feb 2023, the anti-foreign sanctions law was passed in June 2021 and first used in July in the same year.

# China's Formidable UST Holdings



China's holdings of US Treasuries peaked in 2013 at \$1.3 trillion. Despite selling over \$100 bn in USTs over the past year, China is still the second largest foreign holder of US government debt. With \$760 bn (almost 3% of the UST market), even a small demand change in China's appetite for US Treasuries could have a massive signaling impact on UST yields.

Foreign holders of US Treasury securities, USD bn



Source: (1-2) US Department of the Treasury. Data is latest available - October 2024. Reuters "China slips away from Treasuries but sticks with dollar bonds".

# China's Four Red Lines



At the G20 meeting in Lima, Peru in early November 2024, President Xi Jinping signaled to outgoing President Joe Biden that China is willing to improve relations with the US, but is ready for escalation if necessary. Notably, Xi reiterated China's "four red lines" as it relates to US-China policy.

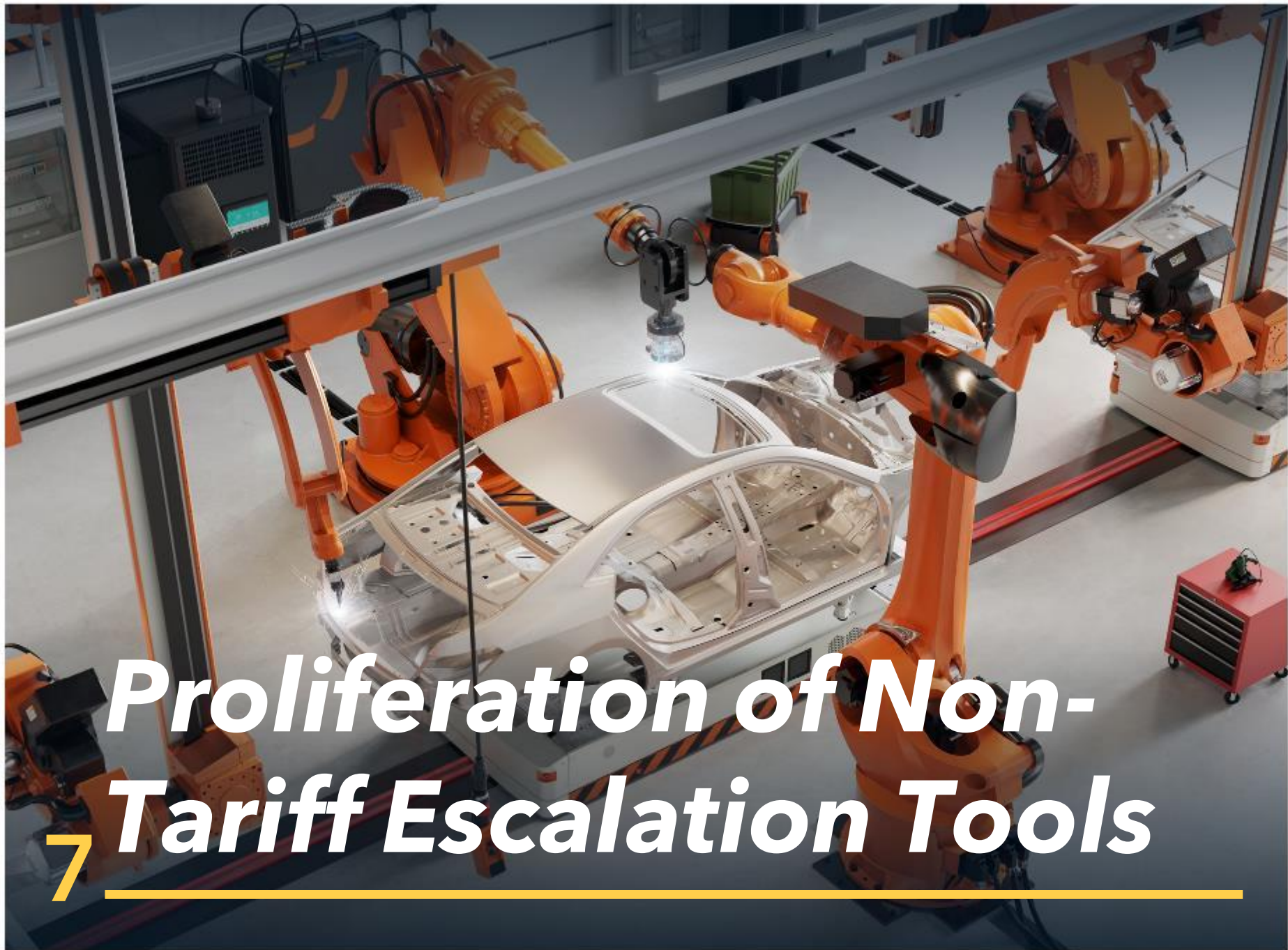
## China's "Four Red Lines"

- 1** Any attempts to undermine the CCP's grip on power
- 2** Any efforts to push China toward democracy
- 3** Any policies to contain China's economic rise (i.e., tariffs, restrictions)
- 4** Any explicit support or encouragement of Taiwan's independence

**"The four red lines must not be challenged. These are the most important guardrails and safety nets for China-US relations."**

***China's President, Xi Jinping, at the G20 Meeting in Lima, Peru (November, 2024)***










# ***7 Proliferation of Non-Tariff Escalation Tools***

# Non-Tariff Legal Architecture Also in Place



In addition to tariffs, we expect President Trump to concurrently expand the already formidable non-tariff toolkit, especially with China, to impose restrictions and competitive barriers on economic activity.

## Selected non-tariff policy toolkit

US policy toolkit	Purpose	Process
 <b>Trading with the Enemy Act (TWEA)</b>	<b>Control trade with enemies during wartime</b>	President has broad authority to determine who is considered an enemy and to regulate such transactions
 <b>Commerce Department "Entity List"</b>	<b>Export controls for national security threats</b>	BIS and Commerce Department interagency review process; majority vote required; no public notice or comment period
 <b>Removal of China's PNTR Status</b>	<b>Allows the US to apply whatever tariff rate it wants to imported goods</b>	Congressional approval required. High risk event for 2025-26.
 <b>Department of Homeland Security UFLPA Entity List</b>	<b>Prohibits companies and entities involved in production of goods using forced labor in the Xinjiang Region from entering the US</b>	Department of Homeland Security manages and updates list; member agency of the Forced Labor Enforcement Task Force can submit recommendation; majority vote required; public can also provide information to be added to list
 <b>OFAC SDN List Sanctions</b>	<b>Protect national security, foreign policy and economy</b>	OFAC manages and updates list based on investigations and findings that the person or entity meets specific criteria for sanctions

Source: (1) Bloomberg, "A Roadmap Through Trump's Tariff Realities and Trade War Drama" (Shawn Donnan & Anna Wong). Bloomberg Economics.

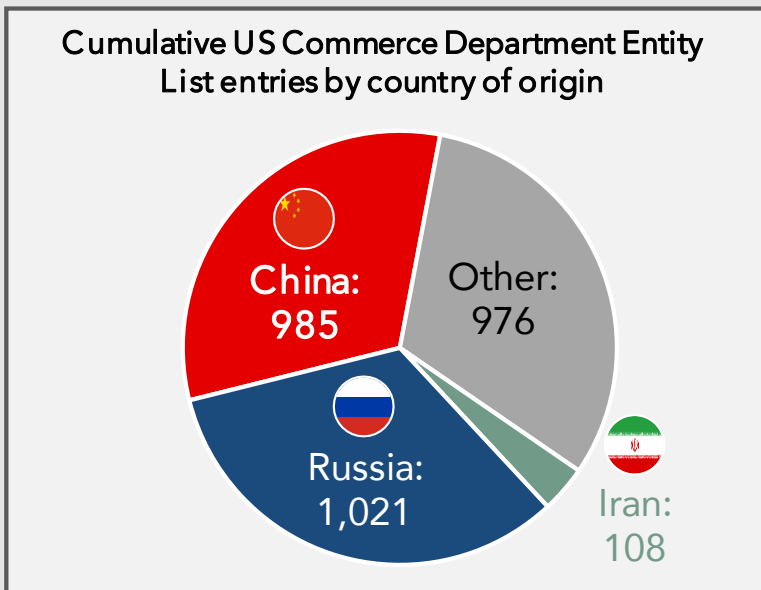


# More Expansive Use of Entity-Specific Restrictions

Since inception in 1997, the US Commerce Department's Entity List has grown to over 3,000 entities and sub-entities. Members of the Entity List are subject to specific licensing requirements which may limit their ability to transact with US entities. Since the trade wars began in 2018, and Russia invaded Ukraine in 2022, China and Russia based companies have dominated new additions to the list.

## Cumulative additions to the US Commerce Department Entity List (1997 – 2025)

3,200



3,090

0  
1997

2025

US China Trade Wars Begin: 749

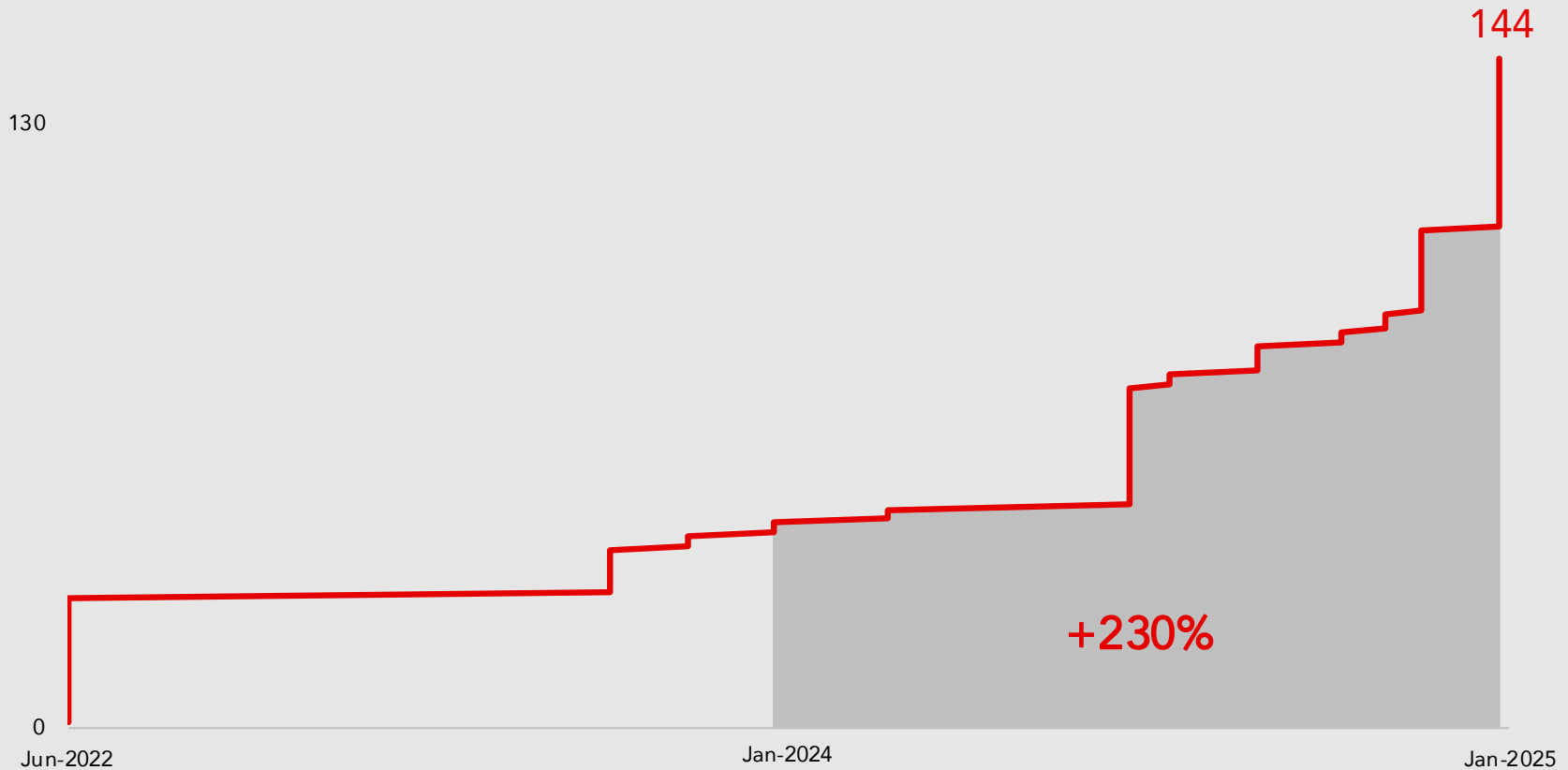
Source: (1-2) Commerce Department. Includes entities and sub-entities but removes duplicate entities. Entities added to the list multiple times are included from their first effective date. Excludes entities with no specified effective date. Data through January 3, 2025. China figures include Hong Kong. Undated entries excluded.

# Department of Homeland Security Restrictions



The US Department of Homeland Security added an additional 37 entities to the Uyghur Forced Labor Prevention Act (UFLPA) Entity List in January 2025, bringing the total number of listed entities to 144 across a number of different industries, including food and agriculture, mineral extraction and processing and manufacturers of inputs to the solar and electronics industries.

## Cumulative additions to the Uyghur Forced Labor Prevention Act (UFLPA) Entity List



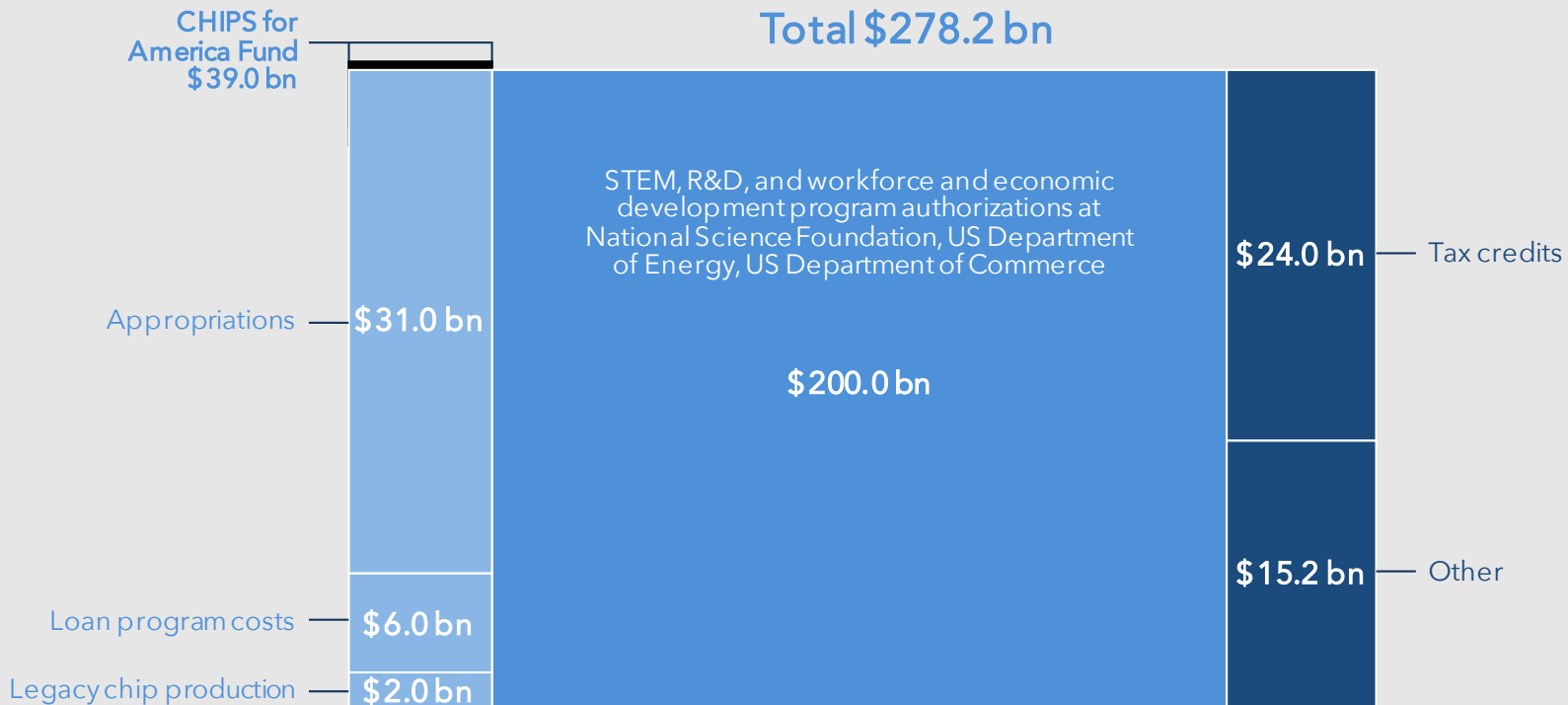
Source: (1) Department of Homeland Security. Data as of November 25, 2024.

# More Domestic Production Tax Incentives



Policy support for the semiconductor industry out of Washington has increased over the last few years through various acts including the Infrastructure Investment & Jobs Act, the Inflation Reduction Act and the Creating Helpful Incentives to Produce Semiconductors (CHIPS) & Science Act. More specifically, The CHIPS Act directs \$280 bn in spending over the next ten years with \$200 bn specific for R&D and commercialization. \$52.7 bn is for semiconductor manufacturing, R&D and workforce development with another \$24 bn worth of tax credits for chip production.

## The \$280 bn US CHIPS and Science Act breakdown



Source: McKinsey & Company, "The CHIPS and Science Act: Here's what's in it" (October 2022).

# US CHIPS Act Restrictive Measures



The Biden administration and US Commerce Department have outlined tight restrictions on new operations in foreign entities of concern (China, Russia, Iran and North Korea) by chipmakers that get federal funds to build in the US.

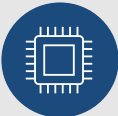
## Restrictions on companies using federal funds from the CHIPS & Science Act



Prohibits recipients of CHIPS incentives funds from using the funds in other countries



Limits recipients of funding from engaging in joint research or technology licensing efforts with a foreign entity of concern that relates to a technology or product that raised national security concerns



Restricted from adding more than 5% to existing capacity and \$100k of investment to any single plant making advanced logic chips (more sophisticated than 28 nanometers) in countries of concern



Limits on adding new production and expanding production capacity beyond 10% of legacy facilities in foreign countries of concern



Classifies list of semiconductors as critical to national security and subject to tighter restrictions



Reinforces US export controls and applies a more restrictive threshold to prevent China from purchasing and manufacturing advanced chips that would enhance their military capabilities

Source: (1) Bloomberg Government, "Biden Stunts Growth in China for Chipmakers Getting US Funds" (March 22, 2023). US Commerce Department, "Commerce Department Outlines Proposed National Security Guardrails for CHIPS for America Incentives Program."

# Broad-Based Tech & Semiconductor Restrictions on China



## Selected US - China technology sector policy actions

May 2019	US national security order to ban Huawei
Feb 2020	US bans government purchases of Huawei gear
Jun 2020	US FCC designates Huawei & ZTE as national security threats
Nov 2020	Executive order prohibiting Americans from investing in 31 tech firms
Dec 2020	4 additional Chinese technology companies added to blacklist
Mar 2021	US FCC blacklists 5 Chinese telecom companies
Apr 2021	US Commerce Department blacklists 7 Chinese supercomputing entities
Apr 2021	US Senate Foreign Relations Committee approves the Strategic Competition Act of 2021
Jun 2021	US Senate passes the Innovation and Competition Act of 2021
Jul 2021	US adds 23 Chinese companies to economic blacklist
Oct 2021	US FCC revokes China Telecom America's services authority
Nov 2021	US blacklists over a dozen Chinese quantum computing companies
Dec 2021	US OFAC adds China's top AI firm to the US's investment blacklist
Dec 2021	US Treasury Department blacklists 8 Chinese technology firms
Dec 2021	US Commerce Department adds 24 more Chinese entities to its "entity list"
Feb 2022	US House of Representatives passes America Competes Act
Feb 2022	US adds 33 Chinese entities to its "unverified list"
Mar 2022	The United States Trade Representative (USTR) doubles down on competition with China in annual report
Mar 2022	SEC releases list of five Chinese companies for possible delisting from US stock markets

Source: (1) Veda Partners (Treyz). China Briefing "US - China Relations in the Biden Era: A Timeline" (Dezan Shira & Associates).

# Broad-Based Tech & Semiconductor Restrictions on China



## Selected US - China technology sector policy actions

Mar 2022	SEC adds Weibo to list of Chinese companies for possible delisting from US stock exchanges
Aug 2022	US passes CHIPS & Science Act
Aug 2022	The US adds another 7 China entities to its export control list
Aug 2022	US and China securities regulators reach agreement on auditing of US-listed Chinese companies
Oct 2022	Commerce Dept. issues two new rules on restricting US & foreign firms shipping high-end microchip manufacturing equipment to China
Oct 2022	Commerce Dept. adds 31 Chinese entities to the "unverified list"
Oct 2022	US announces restrictions on US citizens and green card holders working for certain Chinese semiconductor & AI companies
Dec 2022	US announces ongoing talks with Japan and Netherlands to restrict advanced chip exports to China
Dec 2022	US Congress proposes bill to add Huawei and other Chinese telecom companies to Treasury "specially designated nationals" list
Dec 2022	US Congress proposes ban on Chinese-linked social-media platform TikTok
Dec 2022	Commerce Department adds 36 Chinese companies to "entity list"
Feb 2023	Commerce Department adds 6 Chinese entities to a sanctions list for their support of China's military efforts
Mar 2023	Commerce Department adds 28 Chinese companies to "entity list"
Apr 2023	US Department of Commerce imposes export controls on 12 more Chinese companies
Aug 2023	President Biden issues executive order restricting US investments in Chinese tech

Source: (1) Veda Partners (Treyz). *China Briefing "US - China Relations in the Biden Era: A Timeline"* (Dezan Shira & Associates).



# Broad-Based Tech & Semiconductor Restrictions on China



## Selected US - China technology sector policy actions

Oct 2023	US commerce department adds 42 Chinese entities to export control list for alleged support to Russia's Military
Oct 2023	US further tightens export controls of advanced chips to China
Mar 2024	US Commerce Department adds 28 Chinese companies to "entity list"
Mar 2024	US House of Representatives passes bill to ban TikTok
Apr 2024	President Biden signs bill that will force ByteDance to divest from TikTok
May 2024	US set to increase tariffs on Chinese EVs, solar panels, semiconductors following review of Sec. 301 tariffs starting August 2024
Jun 2024	US Treasury issues draft regulations restricting US investment in sensitive technology sectors in China
Sep 2024	US Commerce Department implements export controls for Quantum computing and other advanced technology
Sep 2024	House of Representatives passes a number of bills targeting Chinese companies and industries
Sep 2024	USTR finalizes China Sec. 301 tariff actions following four-year review
Oct 2024	US Treasury adds two Chinese entities to the Specially Designated Nationals (SDN) list
Oct 2024	US issues final rules on investment restrictions against China targeting semiconductors, AI, and quantum computing
Nov 2024	US advisory panel recommends revoking China's Permanent Normal Trade Relations (PNTR) status
Dec 2024	US further expands chip export controls with 140 additions to the "entity list"
Jan 2025	President Biden unveils new curbs on exporting advanced Nvidia AI chips

Source: (1) Veda Partners (Treyz). China Briefing "US - China Relations in the Biden Era: A Timeline" (Dezan Shira & Associates).

# Restrictions Emanating From US-Dutch-Japan Chip Alliance

In October 2022, the United States unilaterally announced strict export controls on semiconductor technology to China. While US export restrictions have a significant near-term impact on China's chip manufacturing capabilities, to have a more meaningful and longer-term impact, the US needed support from key allies. The Netherlands and Japan are dominant producers of critical chip production equipment necessary for mass-production of semiconductors. In January 2023, the Biden Administration secured a deal with the Netherlands and Japan on semiconductor export controls.



## NETHERLANDS

- Announced export controls on Deep Ultraviolet (DUV) lithography systems (critical to semiconductor manufacturing)
- The announcement does not refer to the US, Japan or China but instead lays out three strategic goals
  - Prevent Dutch goods from contributing to undesirable end use
  - Prevent unwanted long-term strategic dependences
  - Maintain Dutch technological leadership



## JAPAN

- Announced export controls on 23 types of advanced semiconductor manufacturing equipment
- Export controls effective from July 2023
- The announcement did not explicitly reference China or an agreement with the US and Netherlands

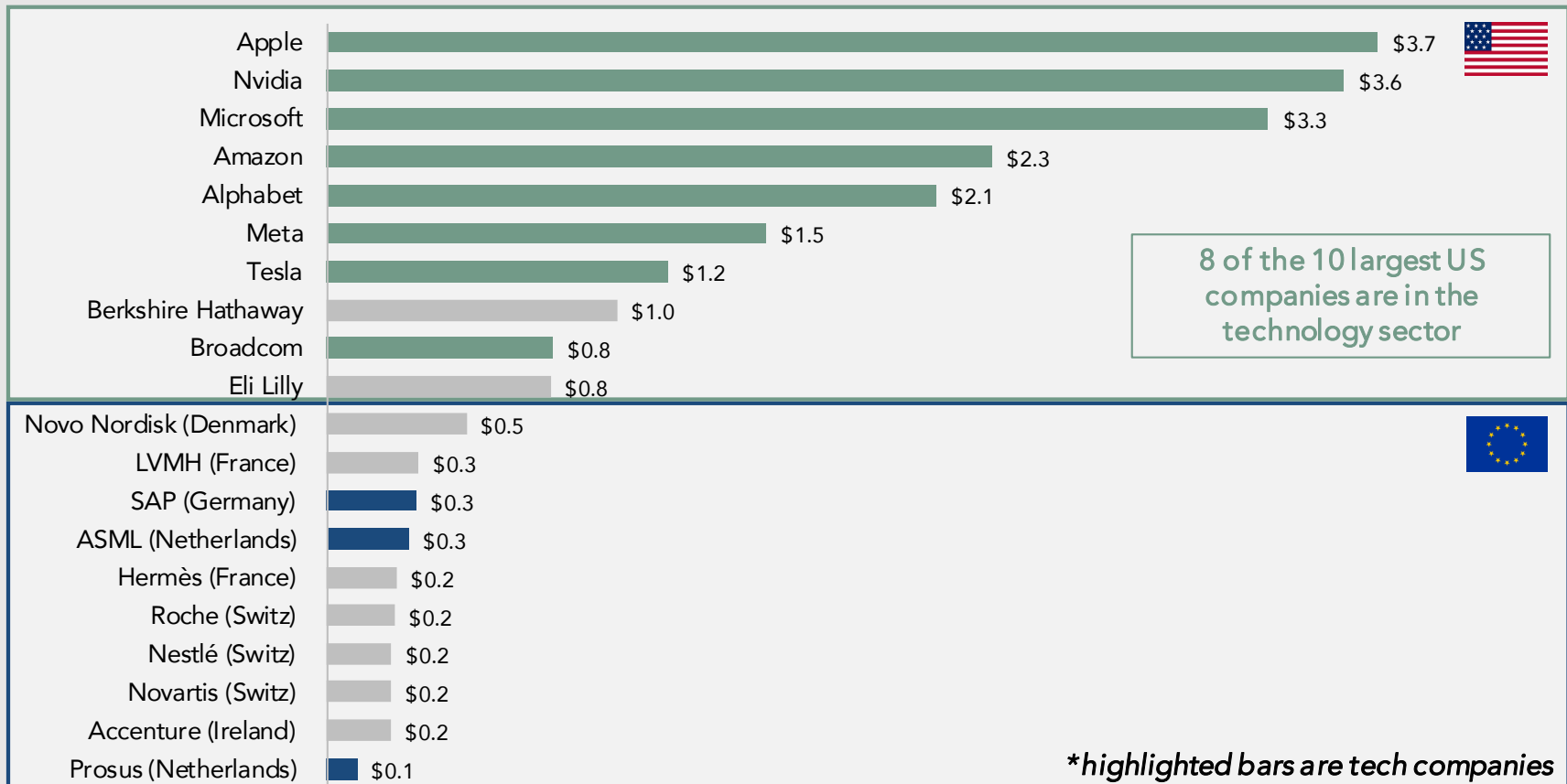
*Source: Center for Strategic & International Studies "Clues to the US-Dutch-Japanese Semiconductor Export Controls Deal Are Hiding in Plain Sight"; "Japan and the Netherlands Announce Plans for New Export Controls on Semiconductor Equipment".*

# Responding to Tariffs with Digital Taxes



China, Europe and other regions may consider responding to President Trump's tariff escalation with other non-tariff tools as well. To this end, the formidable US tech sector is highly vulnerable to retaliation through digital taxes as well as an increase in tech sector anti-trust cases directed toward the largest US tech companies.

## 10 largest companies in the US and EU by market cap, USD tn



Source: (1) Financial Times, "What makes the US truly exceptional". Bloomberg. Data as of December 4, 2024.

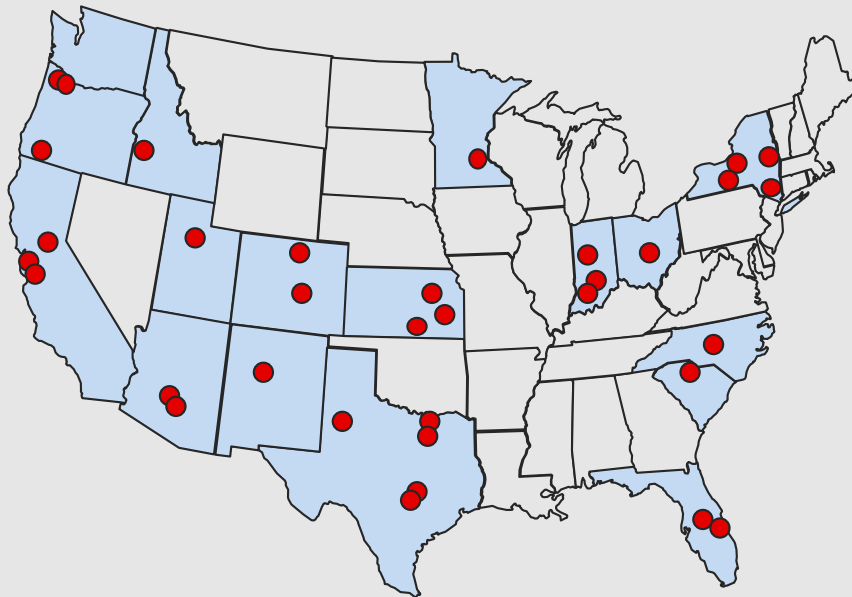
# The Re-Industrialization of America



Since the CHIPS Act was originally introduced in summer 2020, semiconductor companies have announced dozens of new manufacturing, equipment and materials projects. According to the Semiconductor Industry Association, there are over 40 new chip projects underway to expand domestic manufacturing capabilities.

## Announced new and expanded semiconductor projects

● Semiconductors



Company Name	State	Investment
● TSMC	AZ	\$40 billion
● Amkor	AZ	\$2 billion
● Intel	AZ	\$20 billion
● Bosch	CA	
● Akash Systems	CA	\$62 million
● Western Digital	CA	\$350 million
● Broadcom	CO	
● Microchip Technology	CO	\$880 million
● Rogue Valley Microdevices	FL	\$25 million
● SkyWater Technology	FL	
● Micron	ID	\$15 billion
● Trusted Semiconductor Solutions	IN	\$34 million
● Everspin Technologies	IN	
● NHanded Semiconductors	IN	\$236 million
● Reliable Microsystems	IN	\$7 million
● SkyWater Technology	IN	\$1.8 billion
● MediaTek	IN	
● EMP Shield	KS	\$1.9 billion
● Radiation Detection Technologies	KS	\$4 million
● Integra Technologies	KS	\$1.8 billion
● Polar Semiconductor	MN	\$420 million
● Wolfspeed	NC	\$5 million
● Intel	NM	\$3.5 billion
● Menlo Microsystems	NY	\$50 million
● GlobalFoundries	NY	\$1 billion
● IBM	NY	
● Micron	NY	\$20 billion
● Intel	OH	\$20 billion
● Rogue Valley Microdevices	OR	\$44 million
● Microchip Technology	OR	\$800 million
● Intel	OR	
● Analog Devices	OR	\$1 billion
● Pallidus	SC	\$443 million
● X-FAB	TX	\$200 million
● Samsung	TX	\$17.3 billion
● Texas Instruments	TX	\$6 billion
● Texas Instruments	TX	\$30 billion
● NXP	TX	\$2.6 billion
● Texas Instruments	UT	\$11 billion
● Analog Devices	WA	

Source: (1) Semiconductor Industry Association (SIA). Last updated January 23, 2024.

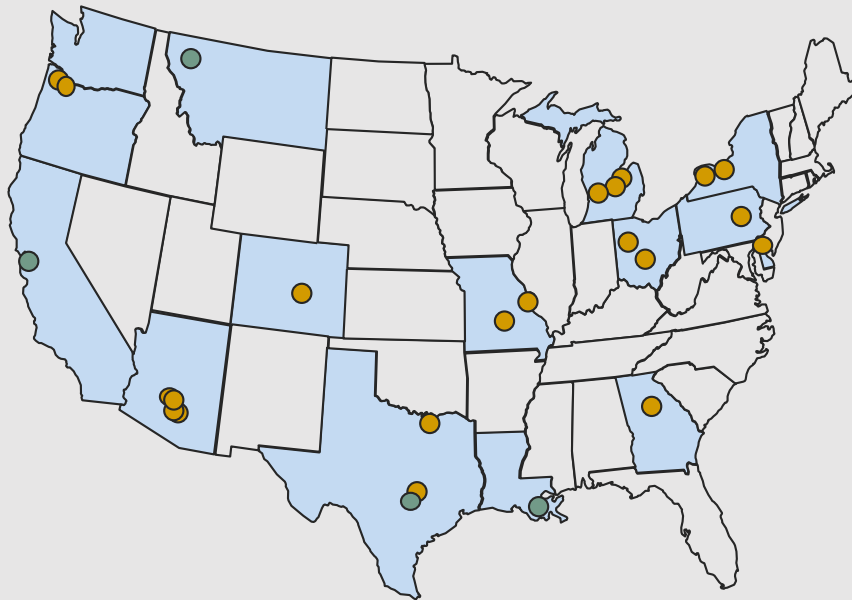
# The Re-Industrialization of America



The projects underway represent new and expanded existing fabs as well as new facilities to supply materials and equipment for manufacturing. The new projects represent over \$180 billion in company investments and could create over 200,000 jobs.

## Announced new and expanded equipment & materials

● Material ● Equipment



Company Name	State	Investment
● JX Nippon Mining & Metal	AZ	
● Air Liquide	AZ	\$60 million
● ASM	AZ	\$324 million
● Linde	AZ	\$600 million
● Sunlit Chemical	AZ	\$100 million
● LCY Chemical	AZ	\$100 million
● Solvay	AZ	\$60 million
● Edwards Vacuum	AZ	
● EMD	AZ	\$28 million
● Yield Engineering Systems	AZ	
● Fujifilm Electronic Materials	AZ	\$88 million
● Chang Chun Group	AZ	\$400 million
● Kanto/Chemtrade JV	AZ	\$250 million
● Applied Materials	CA	
● Entegris	CO	\$600 million
● DuPont Semiconductor Tech.	DE	\$50 million
● Absolics	GA	\$600 million
● K&B Industries	LA	\$12 million
● Mersen USA	MI	\$70 million
● Mersen USA	MI	\$10 million
● SK Siltron CSS	MI	\$300 million
● Hemlock Semiconductor	MI	\$375 million
● Brewer Science	MO	
● GlobalWafers (MEMC)	MO	\$300 million
● Applied Materials	MT	
● Corning	NY	\$139 million
● Edwards Vacuum	NY	\$319 million
● Tosoh SMD	OH	\$20 million
● Chemtrade	OH	\$50 million
● Mitsubishi Gas Chemicals	OR	\$372 million
● EMD	PA	\$300 million
● Schunk Xycarb	TX	
● GlobalWafer (GlobiTech)	TX	\$5 billion
● Applied Materials	TX	
● Shin-Etsu Handotai America	WA	

Source: (1) Semiconductor Industry Association (SIA). Last updated January 23, 2024.



# **8** *Economic Implications*

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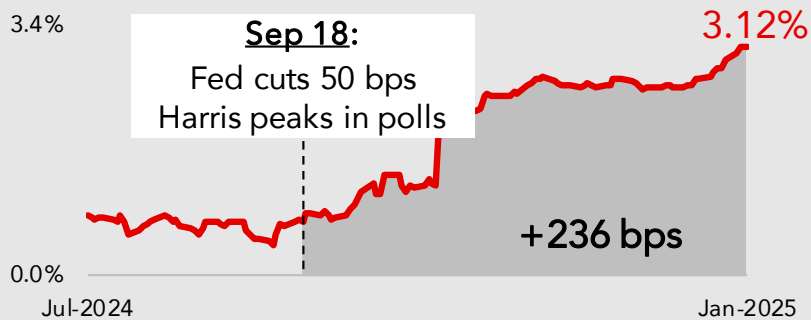


# Higher Inflation Breakevens

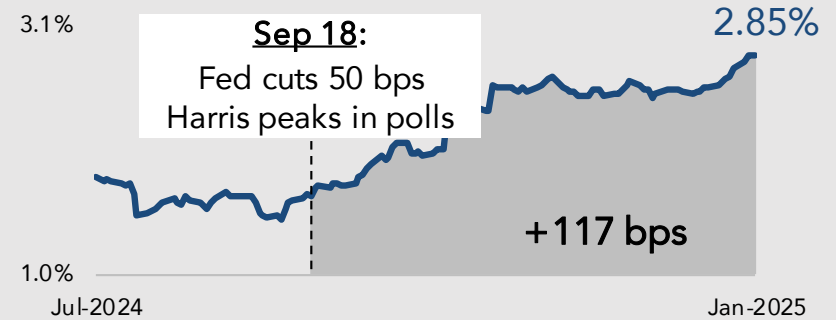


Even as inflation has fallen precipitously over the last two years, rising inflation breakevens suggest investors are on edge about “expected” US inflation. Numerous factors contributing to this uncertainty include: (1) stickiness in core and services inflation; (2) President Trump’s policy positions (fiscal, trade, immigration); (3) the Fed’s pivot to easing; and (4) potential challenges to Fed policy independence. In response to sticky inflation, the Fed has neither tightened rates in recent meetings nor raised its 2% inflation target, but rather, has extended the time period for reaching target inflation to late 2027.

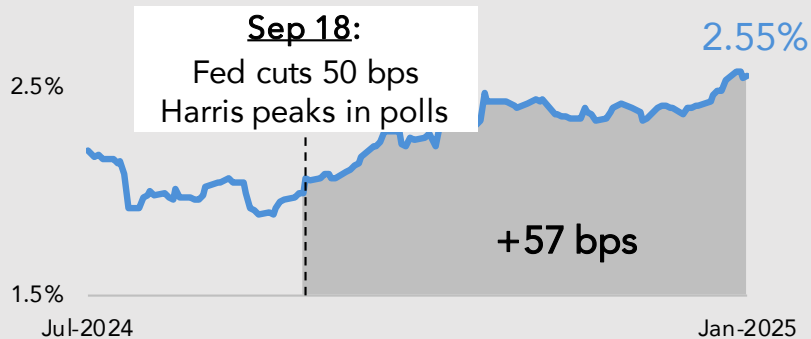
## 1 year US breakeven inflation



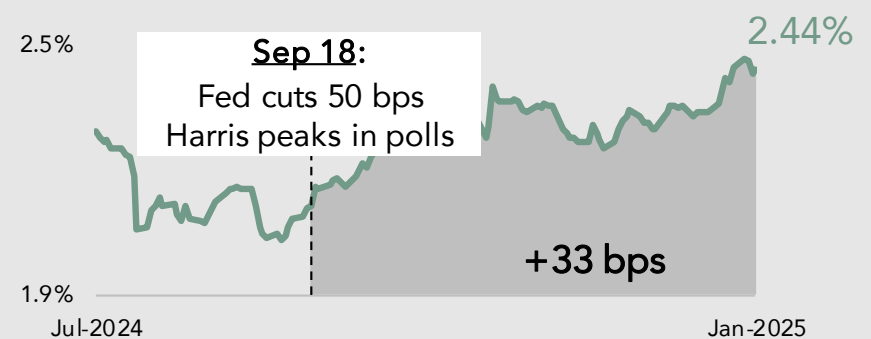
## 2 year US breakeven inflation



## 5 year US breakeven inflation



## 10 year US breakeven inflation



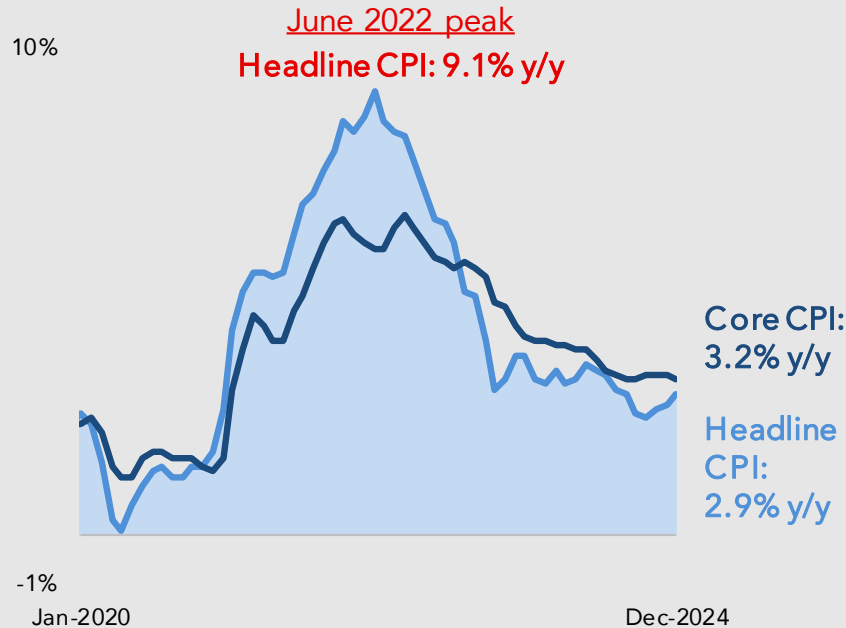
Source: (1-4) Bloomberg. Data as of January 16, 2025.

# "America First" Inflation & "Made in China" Deflation, At Exactly the Same Time

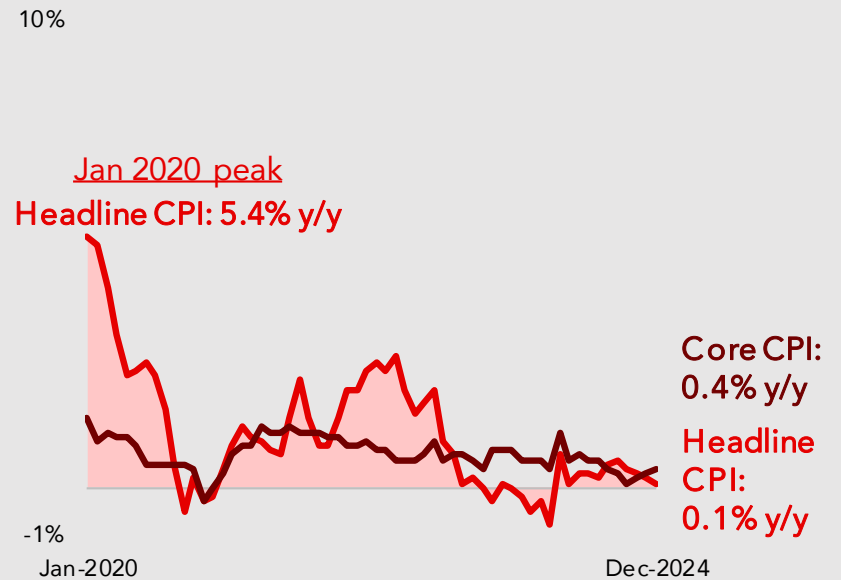
As a result of domestic policy prescriptions across the world's two largest economies, the United States and China are experiencing inflation and deflation, respectively, at exactly the same time. To the extent this policy-induced divergence widens in 2025, which we think is likely, the implications for the global economy may be profound. **Specifically, those economies (i.e., Europe, South Korea) and markets (i.e., oil, EMFX) that are high beta to global trade, China demand and / or a strong US Dollar are especially vulnerable.**



US headline and core CPI, y/y



China headline and core CPI, y/y



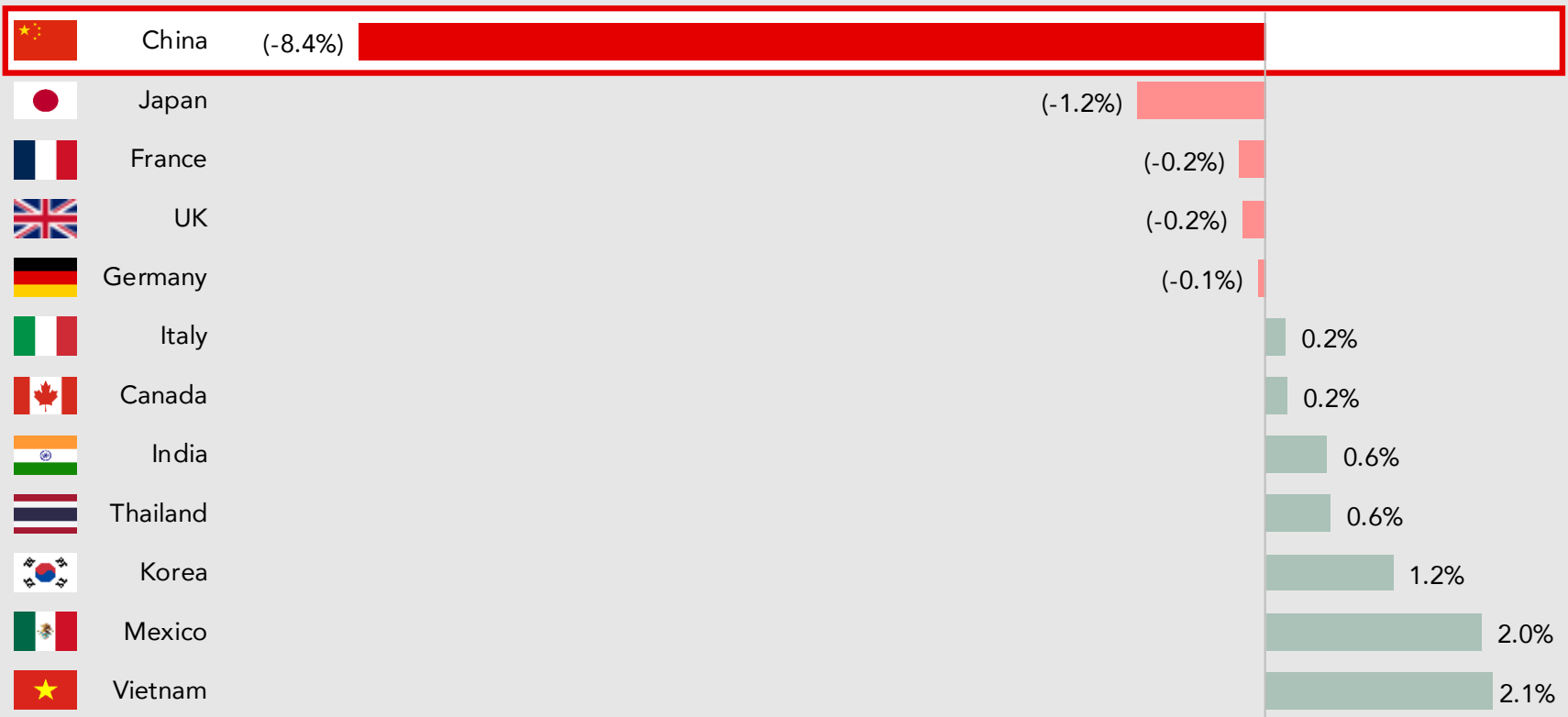
Source: (1-2) Bureau of Labor Statistics. CPI Report December 2024. Bloomberg. Data as of January 16, 2025.

# Restructuring Global Supply Chains



In recent years, the optimistic view of global value chains built up over several decades of globalization has soured considerably. A confluence of recent events - US-China trade wars, COVID crisis and geopolitical shocks - have precipitated a "great reallocation" in global supply chains. For US companies, this involves reducing China risk and building more redundancy and security across countries and companies through a mix of friend-shoring, near-shoring and on-shoring.

## US import market share change since March 2018

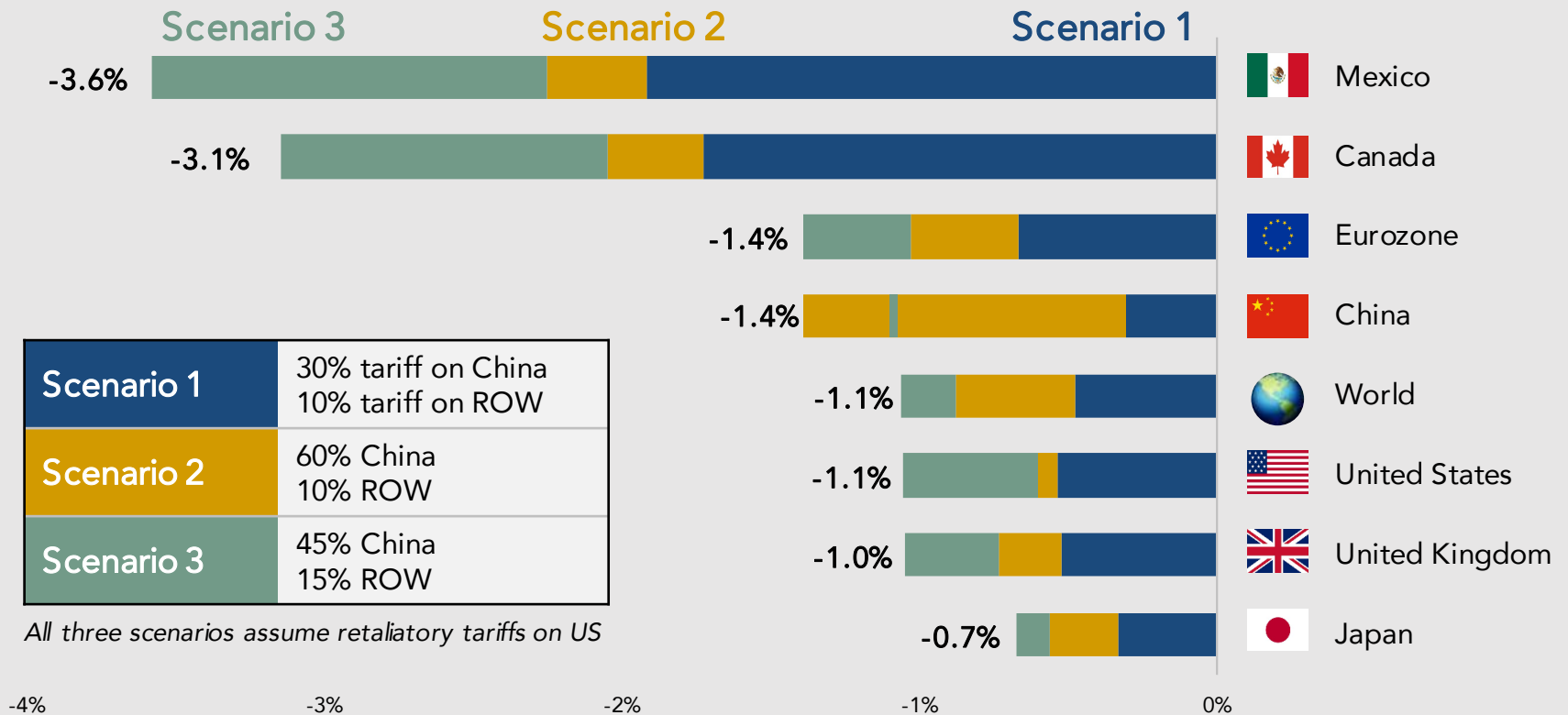


Source: (1) "Global Supply Chains: The Looming Great Reallocation" (Alfaro, Chor). Prepared for the Jackson Hole Symposium, Aug 24-26, 2023 organized by the Federal Reserve Bank of Kansas City. UNComtrade. Change in import market share is rolling 12-month change since March 2018 (US-China trade peak). Latest data is through November 2024. NBER.

# Global GDP Impact of Broad Based Tariffs

In the most extreme scenario Oxford Economics modelled that includes 45% tariffs on China, 15% tariffs on the rest of the world, and retaliatory tariffs on the US, expect world trade to be as much as 10% below the current baseline in the long term while US and world GDP would fall 1% below the baseline. Canada and Mexico, whose exports to the US each account for over 20% of their GDP, would see a significant hit to their economies, pushing them close to or into recession.

Cumulative GDP impacts of blanket tariffs, deviation of GDP from base in Q4 2031

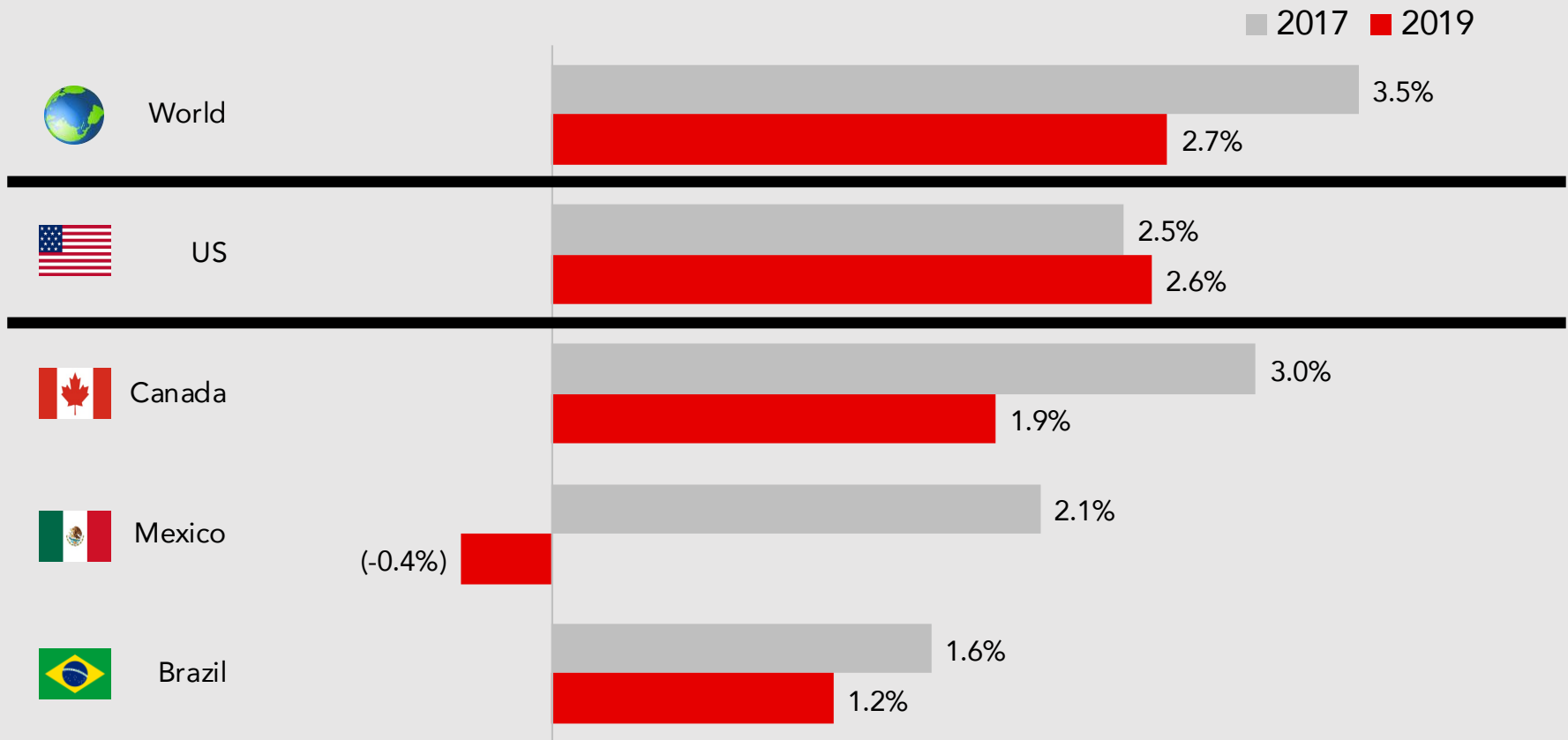


Source: (1) Oxford Economics, "The Global Implications of More Extreme US Tariffs."

# GDP Impact of 2018-2019 Trade Wars

With exports only 11% of GDP, the US economy was more resilient to the 2018-19 trade wars than more export-dependent global economies. Nonetheless, by the summer of 2019, the US yield curve had inverted, signaling US recession risk concerns, and the Fed cut rates in July, September and October of that year.

2017 and 2019 GDP growth by region

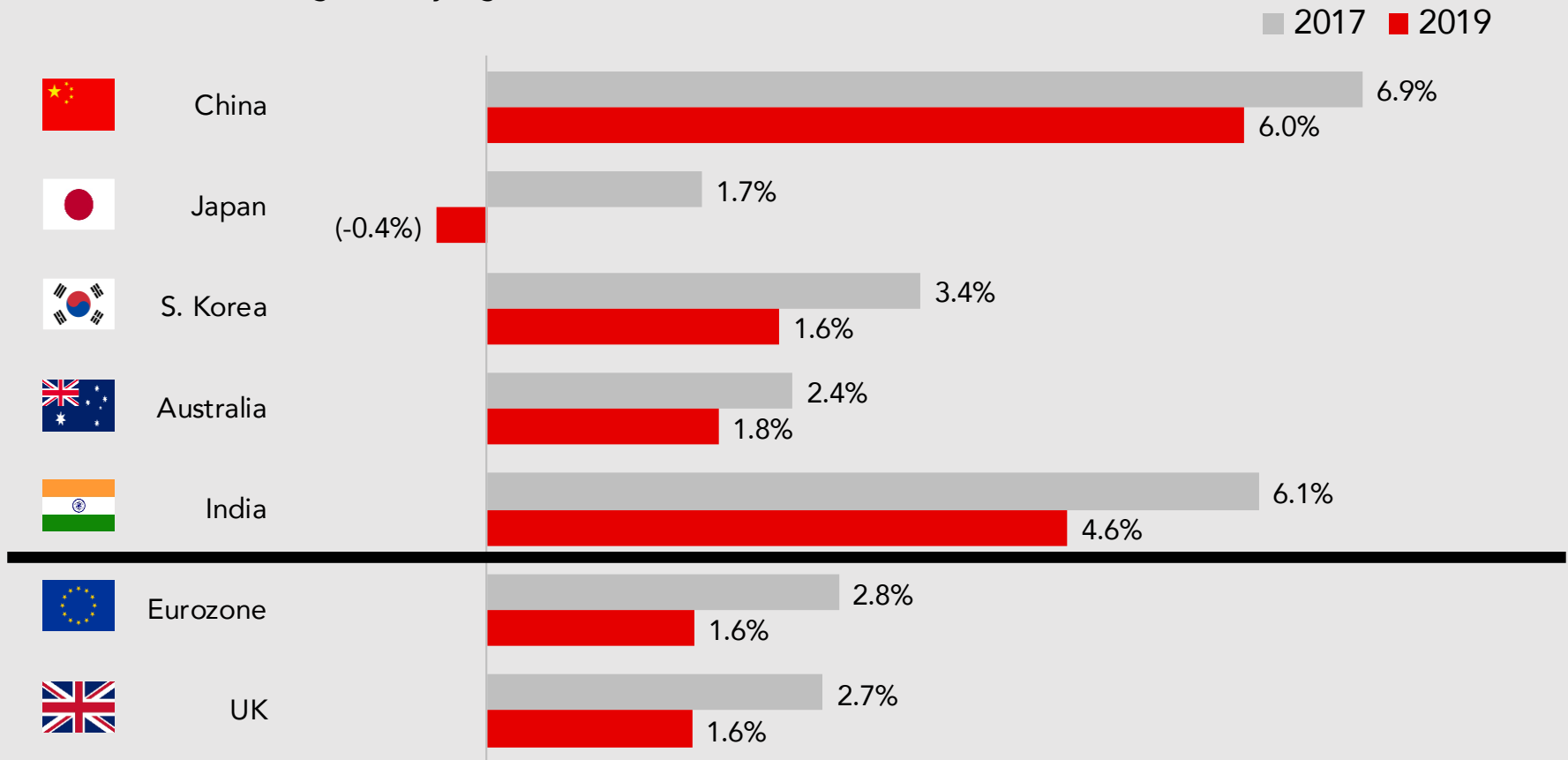


Source: (1) Oxford Economics.

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2017 and 2019 GDP growth by region



Source: (1) Oxford Economics.





## **9** *Market Implications*

# Credit Market Implications of Trade Wars

President Trump's major policy proposals - fiscal expansion via tax cuts, tighter immigration policy and tariffs - would have varying impact on different industries across the credit spectrum. Timing and scale of implementation will be important considerations.

## Trump tariff policy proposals impact across sectors

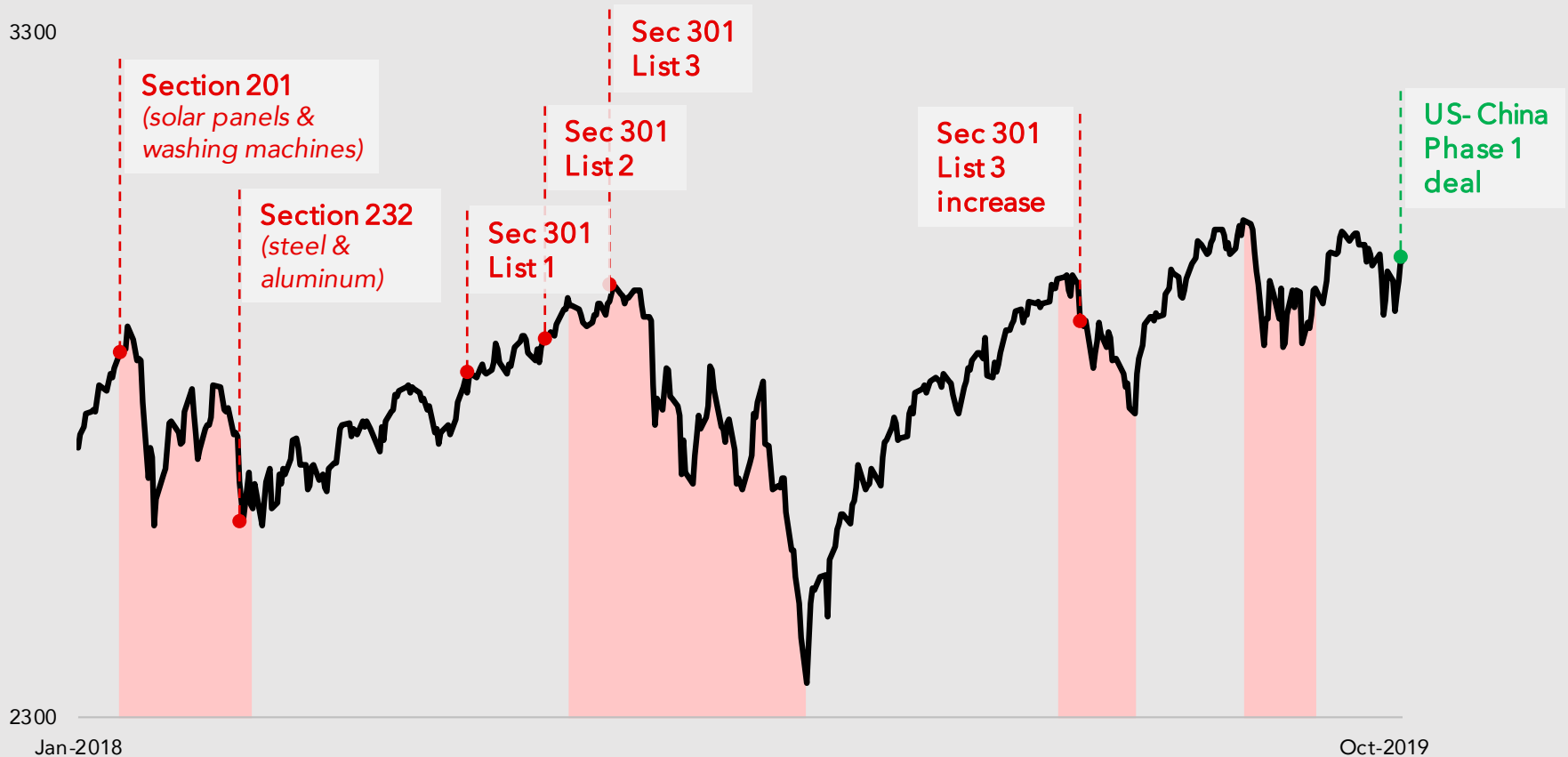
Industry sector	Increased tariffs (10-20% all imports / 60%+ for China)
Banking/Financial Services	Negative
Insurance	Neutral
Automotive	Positive
Basic Industry	Neutral
Capital Goods	Positive
Consumer Goods	Negative
Energy	Negative
Healthcare	Negative
Leisure	Negative
Media	Neutral
Real Estate	Negative
Retail	Very Negative
Technology	Negative
Telecommunications	Neutral
Transportation	Negative
Utilities	Negative

Source: CreditSights, "US IG & Leveraged Finance 2025 Preview: Everything is Awesome!" (Winnie Cisar, Zachary Griffiths). Data as of September 26, 2024.

# Equities & Risk Assets Vulnerable to Trade Policy

As the trade war intensified in 2018, the S&P 500 declined 6% on the year, a sharp drop by historic standards in the absence of a recession. During the 2018-19 escalation, the market also had multiple 5% and 10% corrections, and the Fed was forced to cut policy rates by late 2019 as the yield curve inverted and the economy began to slow down.

## S&P 500 during 2018-19 trade war

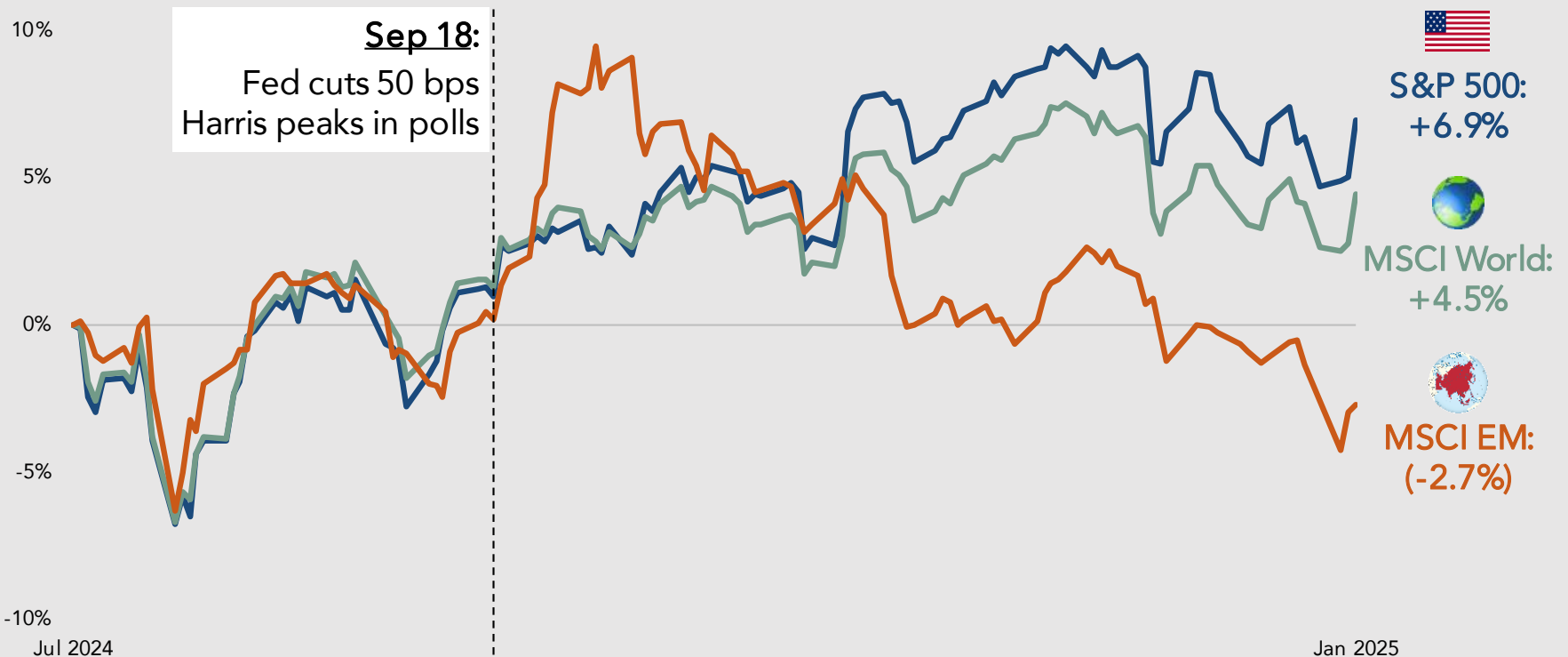


Source: (1) Bloomberg. Data as of January 16, 2025.

# US Stocks Outperforming Global Stocks

Following the US election, the S&P 500 crossed the 6,000 threshold for the first time and has set more than 50 new records in 2024. One of the primary tenets of the so called "Trump trade" is that US stocks outperform global stocks as a result of: (1) the short term positive impact for equities of larger tax cuts passing through to earnings; and (2) the greater relative resilience of the US economy to "trade wars".

## S&P 500 vs. MSCI World since July 21

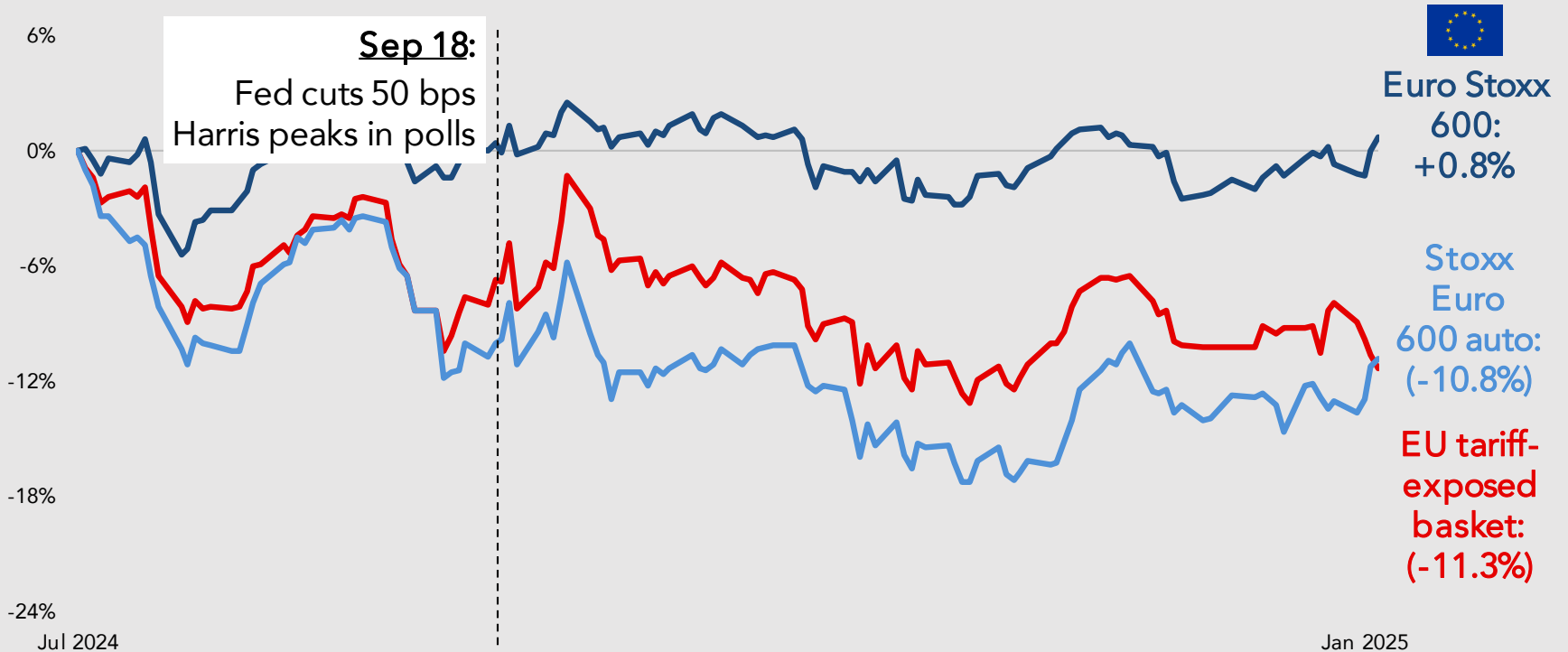


Source: (1) Bloomberg. Data as of January 16, 2025.

# Tariff Exposed Stocks Vulnerable

European export sensitive stocks, led by auto and luxury goods companies, have sharply underperformed broader indices as the probability of a “Trump trade war” has ebbed and flowed in recent months. Notably, we would expect a potential Trump trade war to impact allies and adversaries alike, as it did in 2018-19. Europe would be particularly vulnerable given the exposure of its economy to global trade, global growth and China.

Euro Stoxx 600 vs. European tariff-exposed basket vs. Stoxx Euro 600 auto since July 21

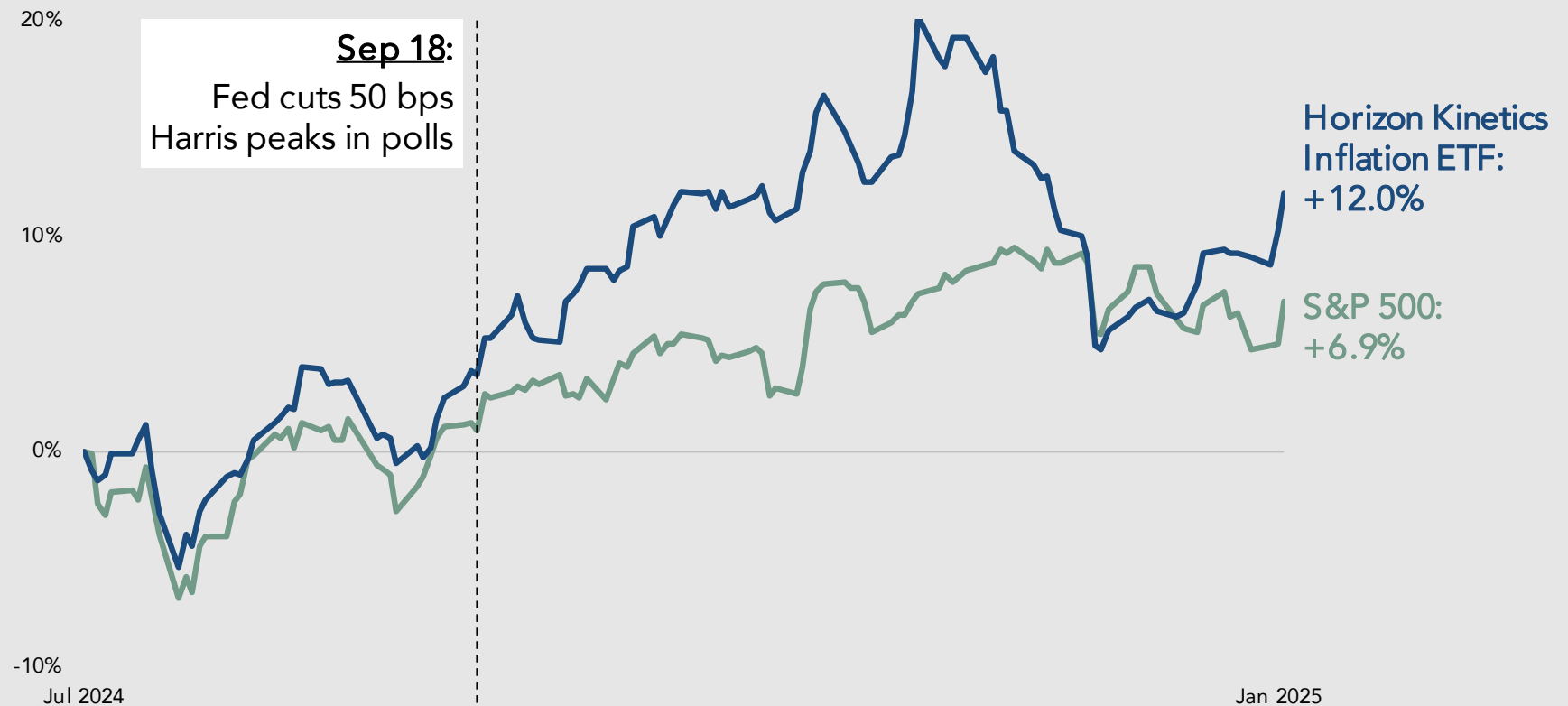


Source: (1) Bloomberg. Data as of January 16, 2025. EU tariff-exposed basket is GS EU Tariffs Exposed. Includes European companies expected to be negatively impacted by the implementation of tariffs on US imports.

# Companies Benefitting from Inflation Outperforming

The bond market is not the only market priced for higher inflation expectations. In equity markets, companies that benefit from rising prices have also been outperforming the broader S&P 500 index since Trump began to close the gap in US polls in late September.

S&P 500 vs. Horizon Kinetics Inflation ETF performance since July 21



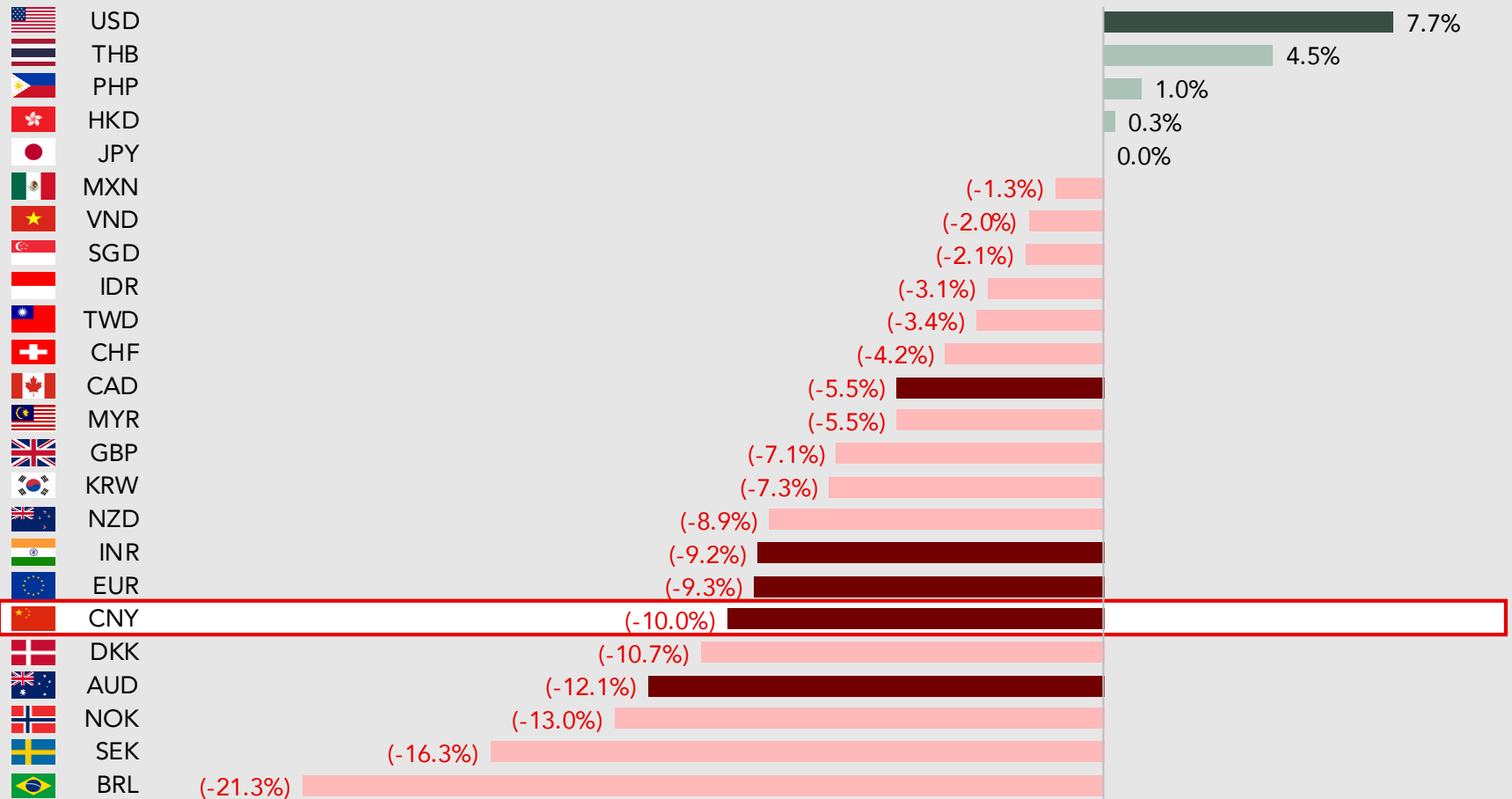
Source: (1) Bloomberg. Data as of January 16, 2025. Horizon Kinetics Inflation ETF fund is actively managed and seeks to achieve its investment objective by investing primarily in companies that are expected to benefit, either directly or indirectly, from inflation.



# Currency Depreciation to Offset Tariffs

Most major DM and EM currencies declined sharply during the 2018-2019 trade wars as global central banks reduced policy rates to offset the economic shock of US tariffs.

FX performance vs. USD during 1<sup>st</sup> Trump presidency trade war period (Feb 2018 – Dec 2019)

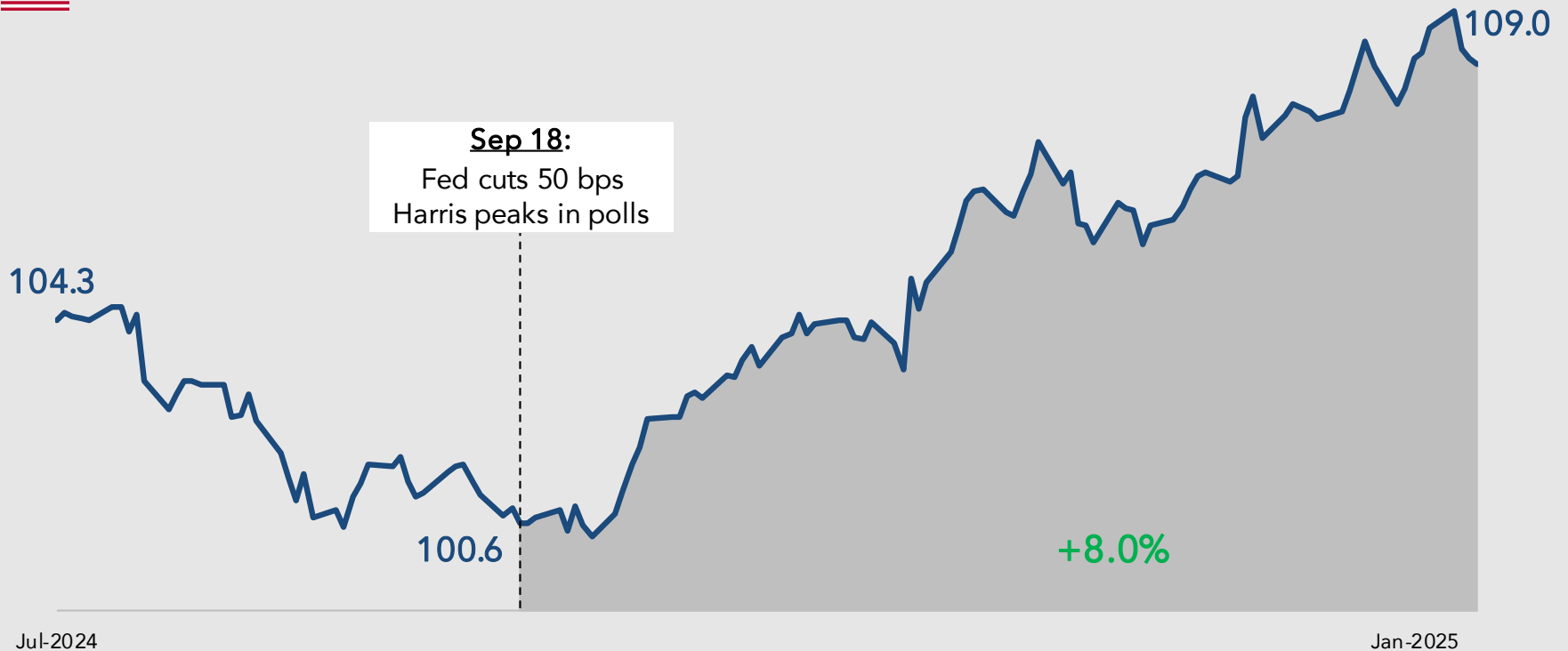


Source: (1) MUFG, "Asia FX Outlook Q4 2024 - Ride with the Tide".

# USD Strengthening

Since Trump's gap in the polls began to tighten in late September, the Dollar has strengthened on the prospect of pro-growth fiscal expansion, upward inflation pressure and the prospect of a "Trump Trade War 2.0." As evident in 2018-19, the Trump trade wars precipitate USD strengthening by virtue of: (1) safe-haven flows; (2) upward pressure on US inflation; (3) higher resilience of less export dependent US economy; and (4) global central bank policy pivots in response to the US tariffs (rate cuts, currency depreciation).

 USD index

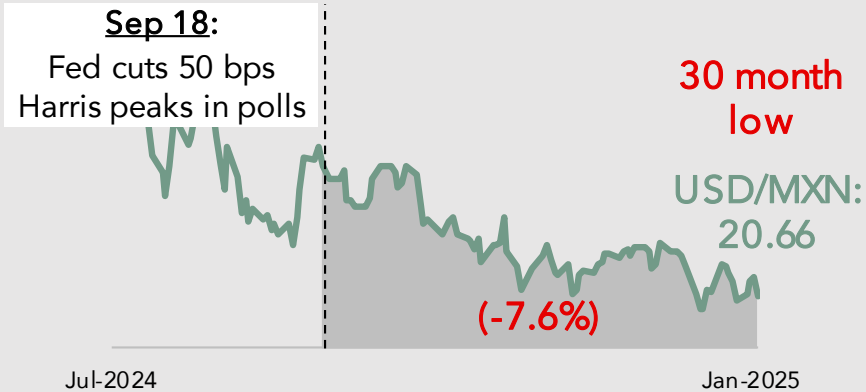


Source: (1) Bloomberg. Data as of January 16, 2025.

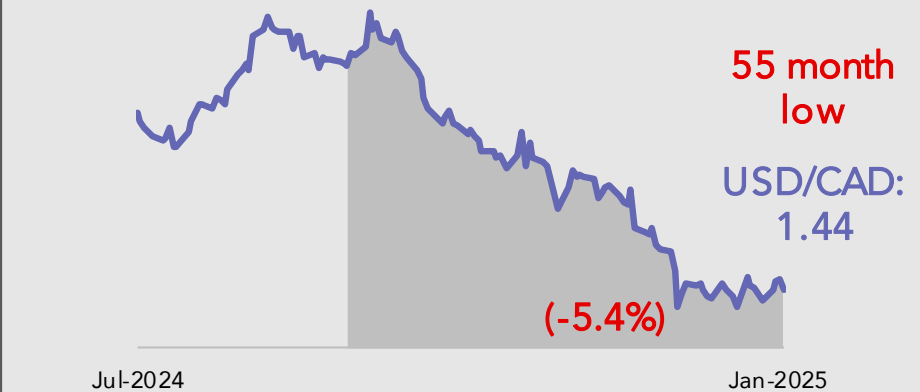
# USD Strengthening



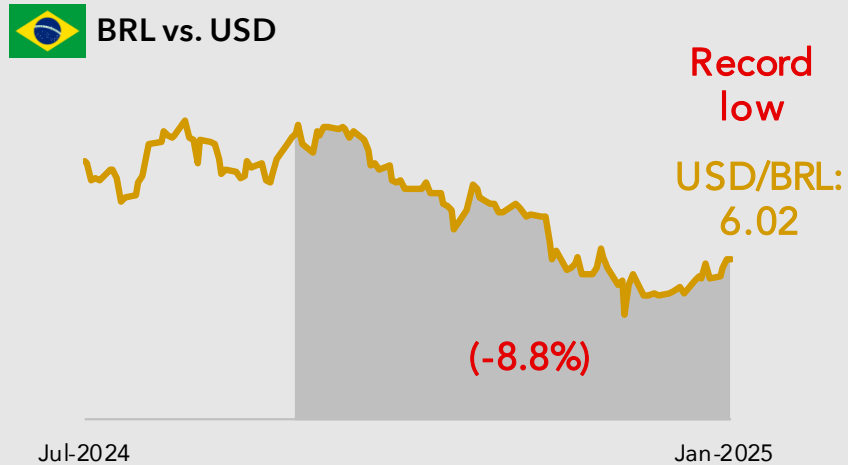
Mexican Peso vs. USD



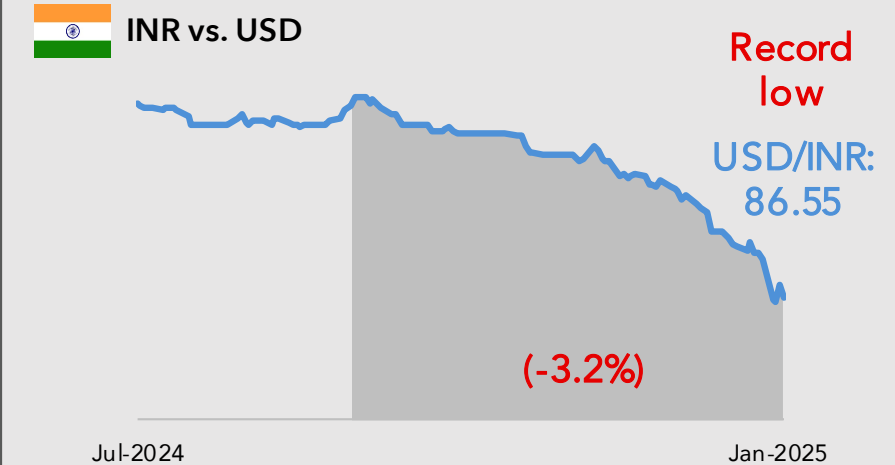
CAD vs. USD



BRL vs. USD



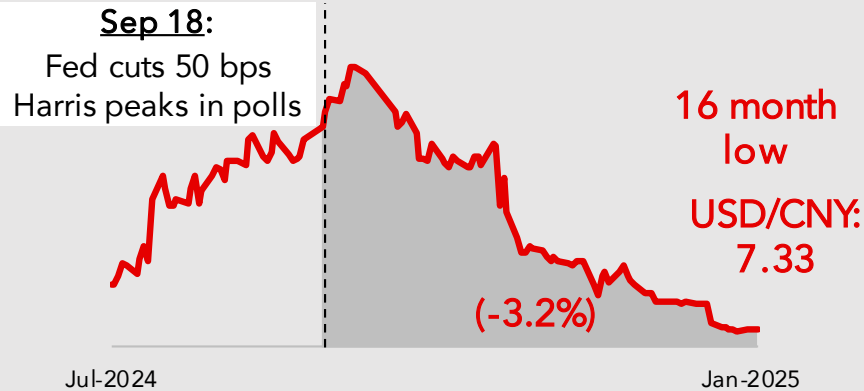
INR vs. USD



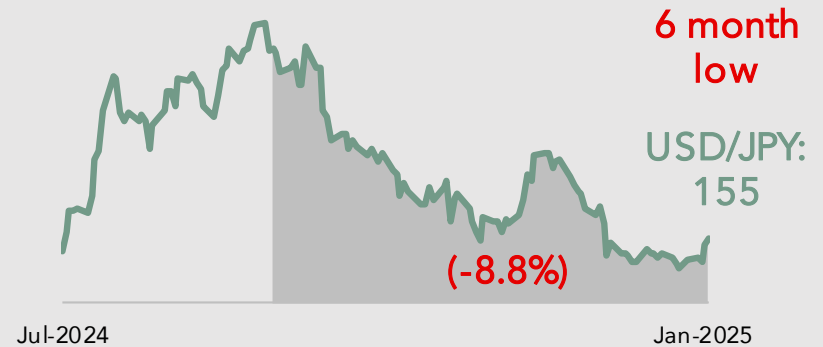
Source: (1-4) Bloomberg. Data as of January 16, 2025. All currencies graphed vs. USD to show depreciation.

# USD Strengthening

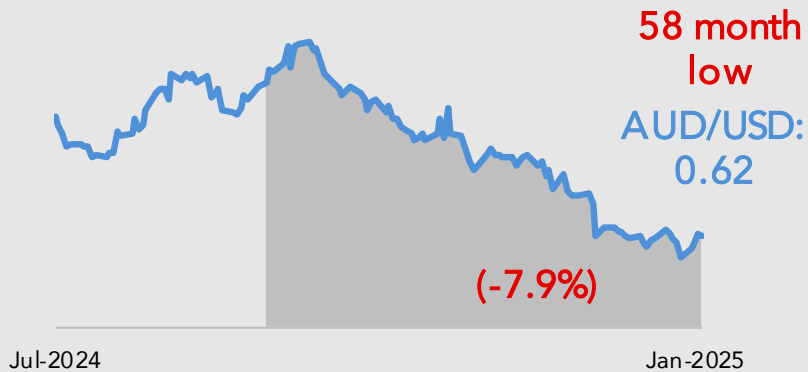
 CNY vs. USD




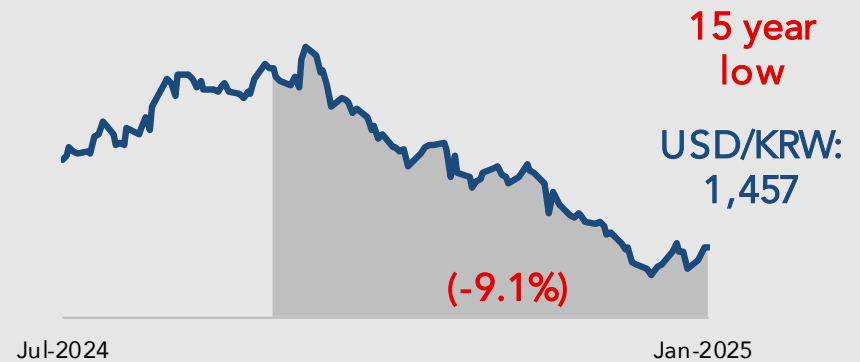
 Yen vs. USD



 AUD vs. USD



 S. Korean Won vs. USD



Source: (1-4) Bloomberg. Data as of January 16, 2025. All currencies graphed vs. USD to show depreciation.

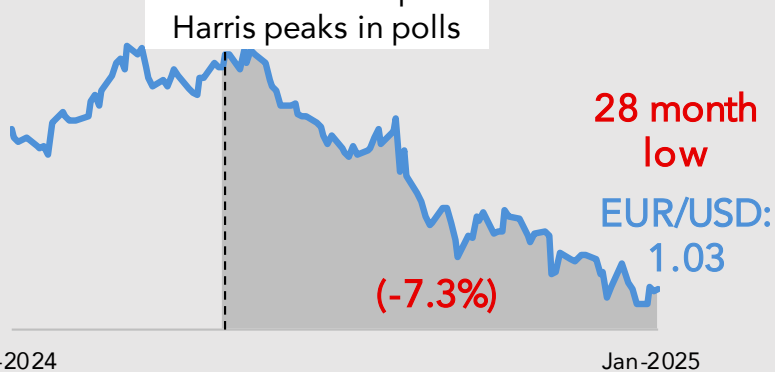
# USD Strengthening



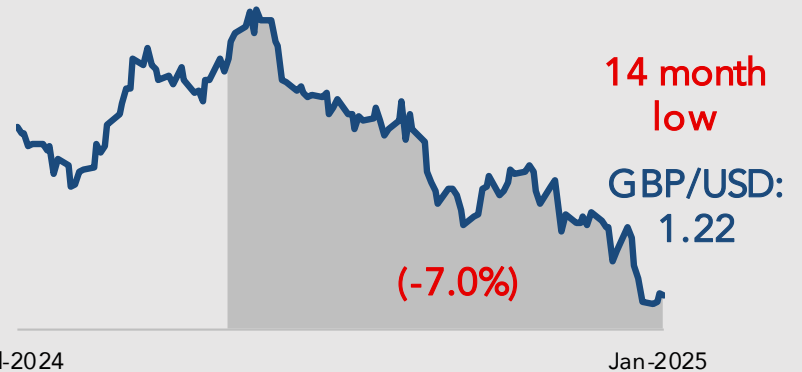
Euro vs. USD

**Sep 18:**

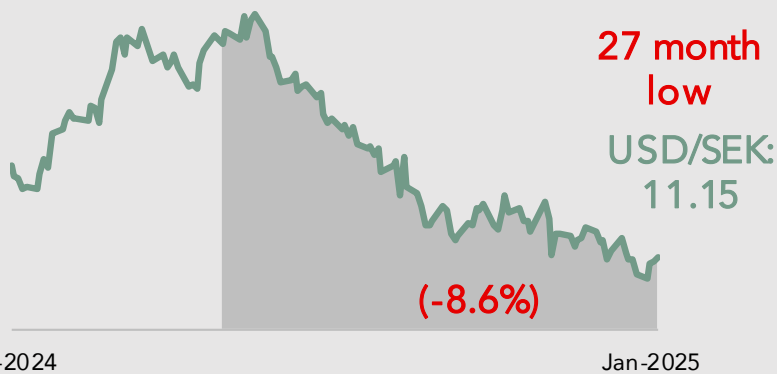
Fed cuts 50 bps  
Harris peaks in polls



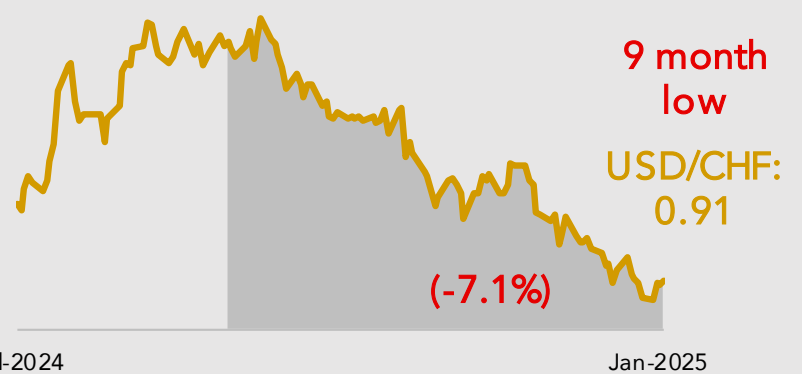
GBP vs. USD



SEK vs. USD



CHF vs. USD



Source: (1-4) Bloomberg. Data as of January 16, 2025. All currencies graphed vs. USD to show depreciation.

A high-angle, wide shot of a modern automotive manufacturing plant. The scene is dominated by a series of yellow robotic arms, likely KUKA models, which are positioned along a production line. These robots are actively welding the metal frames of cars. The car chassis are arranged in a sequence on a conveyor system. The factory environment is clean, industrial, and well-lit, with various structural elements like beams and railings visible. The overall atmosphere is one of precision and automation.

# *Tariffs as Tool of Foreign Policy*

10



# Tariffs as a Tool for Border Security

President Trump is likely to increase tariffs on both Mexico and Canada due to trade deficits as well as to increase leverage in negotiations for the USMCA, which expires in 2026. However, Trump is also likely to utilize forward starting tariffs on an escalation schedule to pressure Mexico to play a significant role in addressing illegal immigration across the US Southern border.



*Image source: Google Earth*

# Tariffs as a Tool in Economic & Geopolitical Rivalry

Massive trade deficits and economic competition are primary drivers of President Trump's trade policy toward China. However, in his second term, look for President Trump to increasingly choose tariffs over sanctions as a tool of foreign policy and geopolitical rivalry.



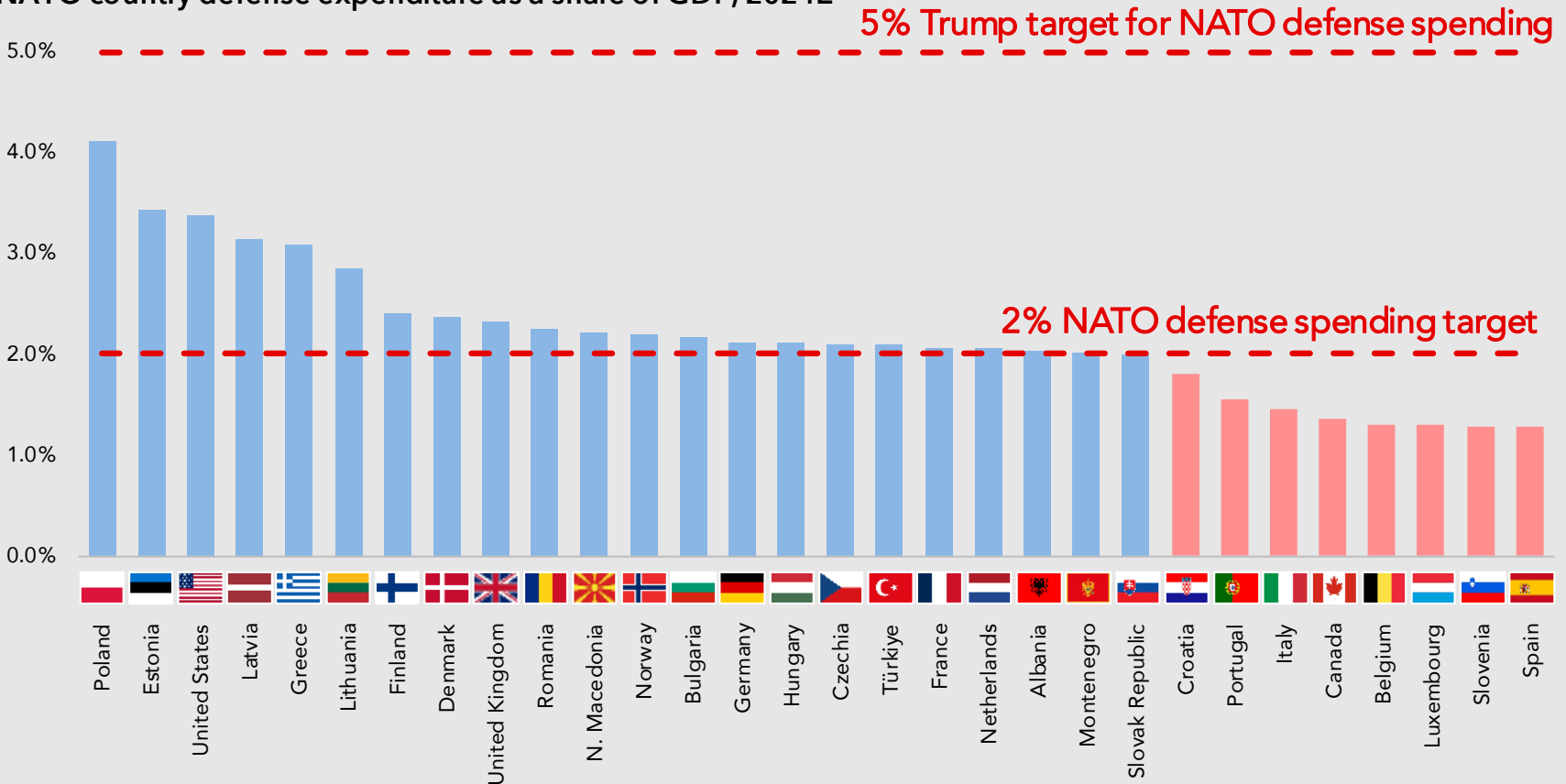
*Image source: Google Earth*

# Tariff Threats to Increase NATO Defense Spending



NATO defense spending declined sharply after the Soviet Union's dissolution in 1991, but began to rise sharply following Russia's 2014 and 2022 invasions of Ukraine. 22 NATO members are expected to meet the 2% of GDP military defense spending targets for 2024, up from 10 countries in 2023 and just three in 2014. While recent Trump demands of 5% NATO defense spending are likely a negotiating level, look for NATO to be a key focus of Trump 2.0 foreign policy.

NATO country defense expenditure as a share of GDP, 2024E



Source: (1) Data based on information provided on NATO's website, calculated as of June 18, 2024. Defense expenditure for 2024 is an estimate. Bloomberg Economics.

# Tariffs to Gain Leverage Over Greenland

Greenland, the world's largest island spanning over 2.2 million square kilometers with access to both the Atlantic and Arctic Oceans, has become a critical geostrategic focal point for the world's superpowers (US, Russia, China) in the Arctic region. It is also has the world's lowest population density (population 57k) and an extraordinary volume of critical minerals, deposits and rare Earths. As an autonomous territory of both Denmark and the European Union, the status of Greenland's political control has become an elevated issue given rising domestic support for its independence movement, as well as President Trump's recent commentary.

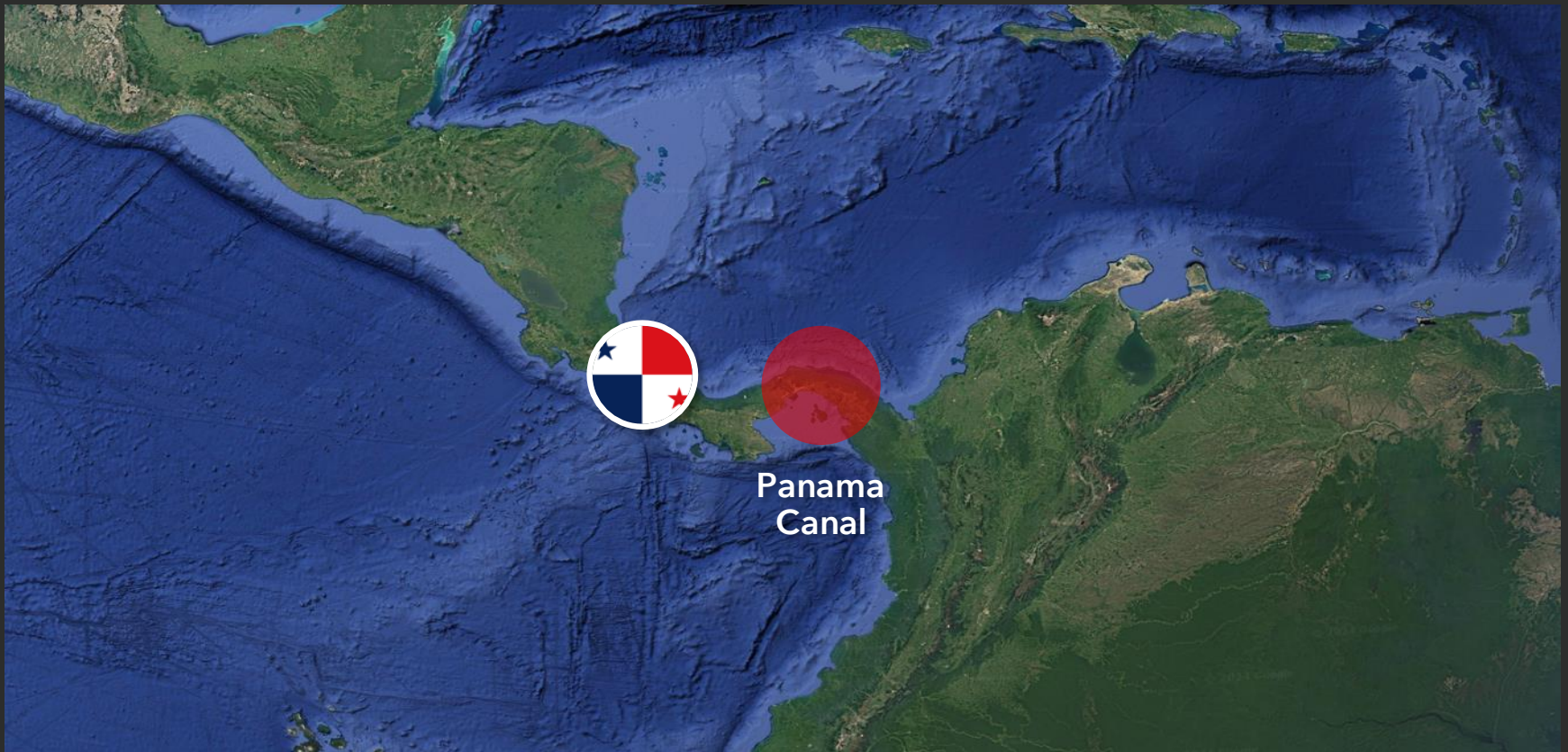


Image source: Google Earth



# Tariffs to Strengthen Control of Key Geo-Strategic Chokepoint

The 51 mile wide Panama Canal is one of the world's most important geostrategic chokepoints, connecting maritime trade between the Atlantic and Pacific Oceans. Built by the United States between 1904-1914, and controlled by the US until 1999 (following a treaty agreement signed by President Carter in 1977), the Canal has become the subject of President Trump assertions on its importance to US security. Rising Chinese influence in recent years has also become a concern.

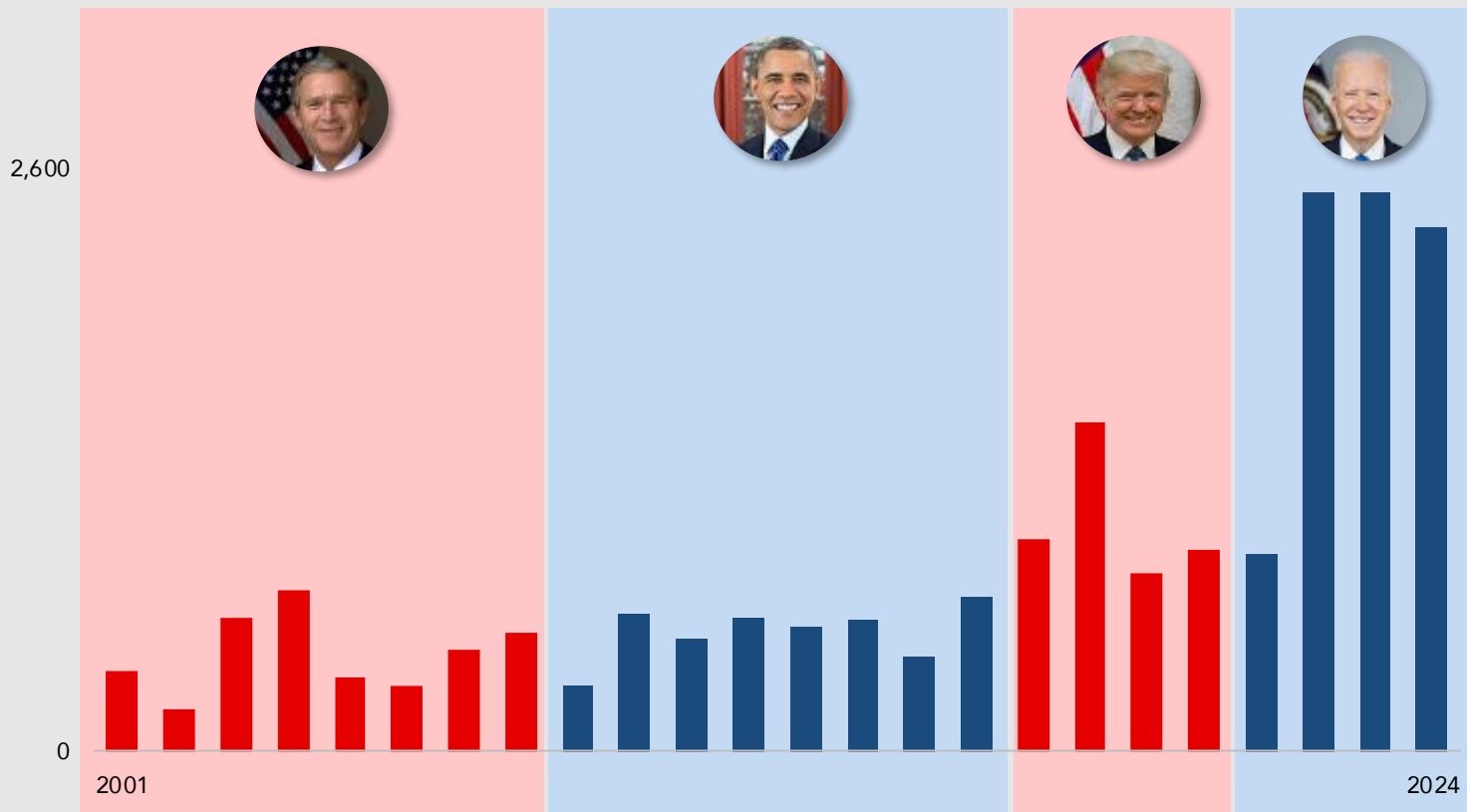


*Image source: Google Earth*

# De-Emphasizing Sanction Tools in Favor of Tariffs

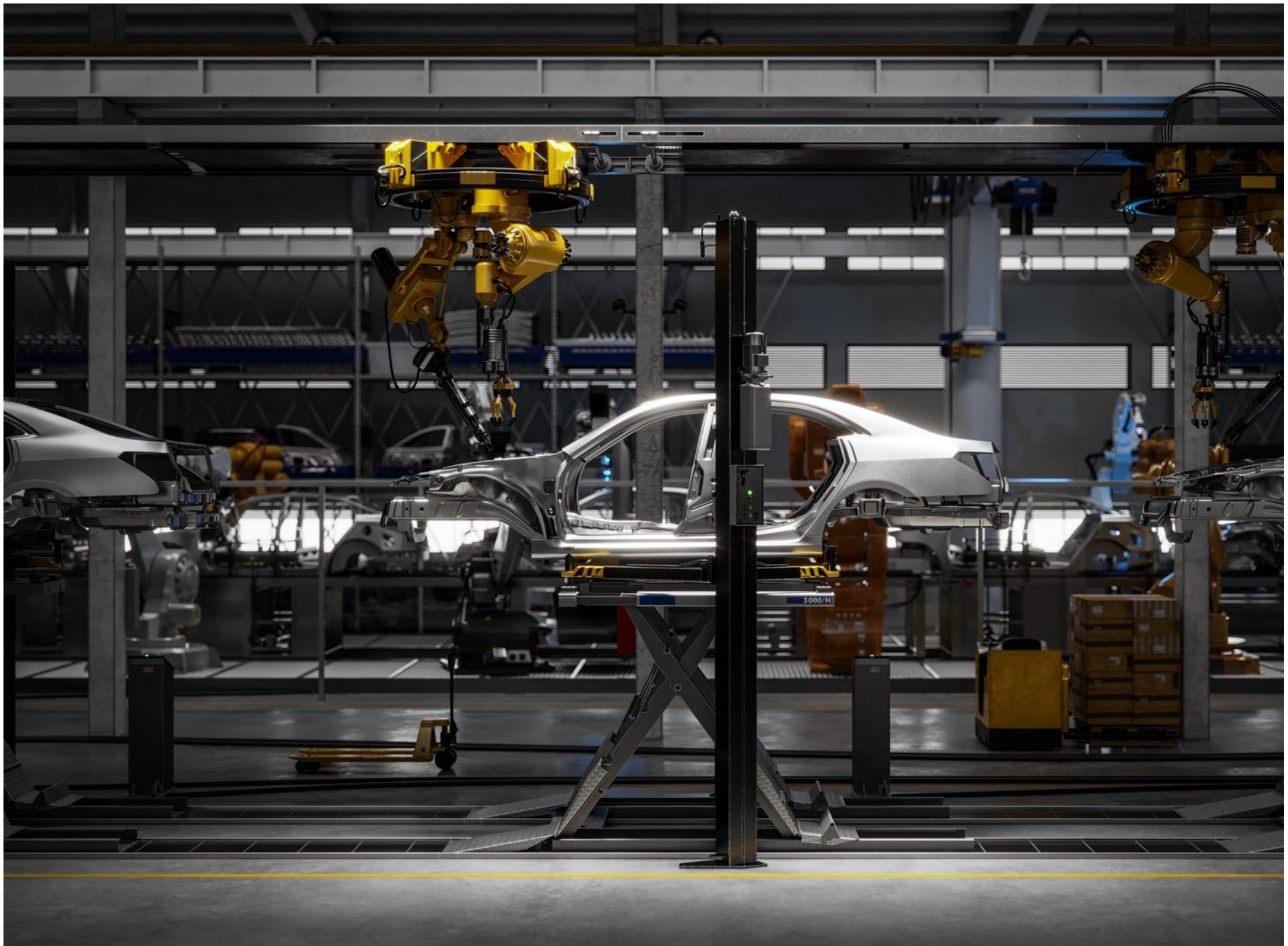
The Executive branch (White House) has numerous punitive tools at its disposal when dealing with foreign countries including industrial policy, tariffs, sanctions, commercial and technology restrictions. President Trump has indicated that he may dial-back existing US sanctions and use them more selectively going forward. **However, a much more expansive use of tariffs is expected in Trump 2.0 trade, economic, currency and foreign policy.**

## New additions to OFAC sanctions



## Cumulative

- Over 12,000 countries, entities & individuals globally












































# 2025 Global Economic Forecasts

The global economy is expected to grow at about 2.7% in 2024, well below its long term 3.5% average, with the US one of the only advanced economies to grow above 2% in the year ahead.

## GDP growth forecasts, y/y

Region / country	2024E	2025E	
<b>North America</b>			
 US	2.8%	2.6%	↓
 Mexico	1.5%	1.7%	↑
 Canada	1.3%	1.5%	↑
<b>Eurozone</b>			
 Spain	3.1%	2.5%	↓
 France	1.1%	0.8%	↓
 Netherlands	0.9%	1.3%	↑
 Italy	0.5%	0.8%	↑
 Germany	(-0.2%)	0.4%	↑
 Ireland	(-0.2%)	4.0%	↑
 Finland	(-0.4%)	1.4%	↑
<b>Other Europe</b>			
 Russia	3.9%	1.7%	↓
 Denmark	2.7%	2.4%	↓
 Türkiye	2.7%	1.9%	↓
 Norway	2.4%	0.8%	↓
 Poland	2.4%	3.3%	↑
 Switzerland	1.3%	1.0%	↓
 Czech Republic	1.0%	2.4%	↑
 UK	0.8%	1.1%	↑
 Sweden	0.6%	2.4%	↑
<b>APAC</b>			
 India	6.4%	6.5%	↑
 Indonesia	5.1%	5.0%	↓
 China	4.8%	4.4%	↓
 Singapore	4.0%	3.1%	↓
 South Korea	2.2%	2.0%	↓
 Australia	1.0%	2.0%	↑
 Japan	(-0.2%)	1.2%	↑
 New Zealand	(-0.3%)	1.2%	↑
<b>LatAm</b>			
 Brazil	3.2%	1.7%	↓
 Chile	2.3%	2.4%	↑
 Colombia	1.8%	2.1%	↑
 Argentina	(-2.3%)	3.6%	↑
<b>MENA</b>			
 UAE	3.7%	4.2%	↑
 Sub-Saharan Africa	3.4%	3.6%	↑
 Egypt	2.9%	4.0%	↑
 Qatar	1.9%	2.1%	↑
 Oman	1.5%	2.1%	↑
 Saudi Arabia	1.4%	3.9%	↑
 South Africa	0.7%	1.5%	↑
 Kuwait	(-2.0%)	2.0%	↑

Source: (1) Oxford Economics. Data as of January 17, 2025.

# 2025 Global Currency Forecasts

Currency pair	Spot (Jan 17)	Q1 2025	Q2 2025	Q3 2025	Q4 2025
EUR / USD	1.03	0.99	1.02	1.05	1.08
GBP / USD	1.22	1.20	1.24	1.28	1.30
USD / JPY	156	154	152	150	148
USD / CNY	7.33	7.40	7.50	7.50	7.40
AUD / USD	0.62	0.59	0.60	0.62	0.64
NZD / USD	0.56	0.54	0.54	0.56	0.58
USD / CAD	1.44	1.45	1.44	1.42	1.39
USD / NOK	11.40	12.02	11.86	11.62	11.02
USD / SEK	11.15	11.72	11.57	11.33	10.83
USD / CHF	0.91	0.94	0.90	0.89	0.87
USD / MXN	20.69	21.75	21.50	21.00	21.00
USD / BRL	6.03	6.40	6.60	6.50	6.40

Source: (1) MUFG Annual Foreign Exchange Outlook - January 2025. (Derek Halpenny). Bloomberg.

# 2025 MUFG Global Rates Forecasts

	Spot (Jan 17)	Q1 2025		Q2 2025		Q3 2025		Q4 2025	
		MUFG	Consensus	MUFG	Consensus	MUFG	Consensus	MUFG	Consensus
Fed Funds	4.50%	4.50%	4.35%	4.25%	4.05%	4.00%	3.90%	4.00%	3.80%
2 yr UST	4.27%	4.38%	4.04%	4.13%	3.90%	4.25%	3.80%	4.00%	3.74%
5 yr UST	4.41%	4.63%	4.09%	4.50%	3.99%	4.38%	3.96%	4.25%	3.93%
<b>10 yr UST</b>	4.61%	<b>4.75%</b>	<b>4.27%</b>	<b>4.75%</b>	<b>4.20%</b>	<b>4.63%</b>	<b>4.18%</b>	<b>4.63%</b>	<b>4.16%</b>
30 yr UST	4.84%	5.00%	4.48%	5.00%	4.42%	4.88%	4.41%	4.88%	4.39%

Source: (1) MUFG Global Macro Research (George Goncalves). Bloomberg. Data as of January 17, 2025. Fed funds is upper bound.

# 2025 MUFG Commodities Forecasts

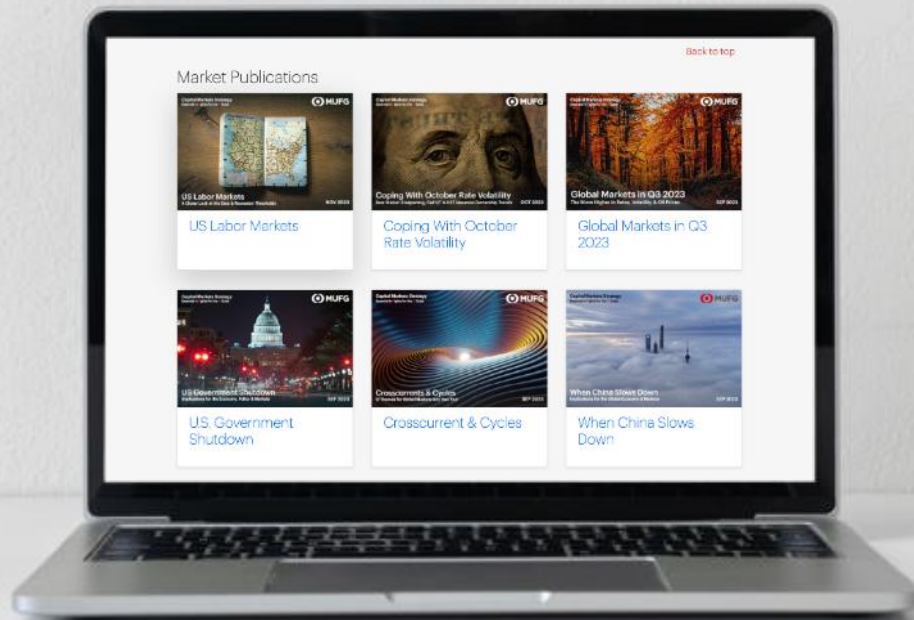
	Spot (Jan 17)	Q1 2025		Q2 2025		Q3 2025		Q4 2025	
		MUFG	Consensus	MUFG	Consensus	MUFG	Consensus	MUFG	Consensus
WTI	<b>\$78</b>	\$68	\$70	\$64	\$71	\$69	\$70	\$72	\$70
Brent	<b>\$81</b>	\$73	\$74	\$69	\$74	\$74	\$74	\$77	\$73
US Nat Gas	<b>\$3.94</b>	\$3.20	\$3.19	\$2.90	\$3.05	\$2.70	\$3.29	\$2.90	\$3.80
Euro Nat Gas	<b>€47</b>	€52	€44	€38	€40	€33	€37	€29	€38

Source: (1) MUFG Commodities Research (Ehsan Khoman). Bloomberg. Data as of January 17, 2025.



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# About the Authors



## **Tom Joyce**

Managing Director  
Capital Markets Strategist  
New York, NY

Tom.Joyce@mufgsecurities.com  
(212) 405-7472

## **Role**

Tom Joyce is a Managing Director and Capital Markets Strategist within MUFG's global capital markets and investment banking business. Based in New York, Tom heads a team that creates customized analytical content for multi-national S&P 500 companies. His team provides in depth analysis on the impact of economic, political, public policy and regulatory dynamics on the US credit, foreign exchange, rates and commodities markets.

## **Experience**

Tom has over 30 years of Investment Banking experience in New York, London, Hong Kong, and San Francisco. Tom created and built the Capital Markets Strategy role, advising corporate C-Suite executives (Boards, CEOs, CFOs, and Treasurers) on the pervasive macro forces driving markets. Tom also presents at dozens of corporate events each year including Board meetings, CEO ExCo sessions, CFO and Treasury off-sites, corporate leadership events and conferences.

## **Education**

Tom's educational background includes a year of study at Oxford University from 1991 - 1992, a Bachelor of Arts in Political Science from Holy Cross College in 1993, and a MBA from Kellogg Business School, Northwestern University in 2000.

## **Personal**

Tom resides in New Canaan, CT with his wife and four sons, where he previously served on the Board of Trustees of the New Canaan Library. Tom also serves on the President's Council of Holy Cross College.

# About the Authors



## Stephanie Kendal

Vice President  
Capital Markets Strategist  
New York, NY

Stephanie.Kendal@mufgsecurities.com  
(212) 405-7443

### Role

Stephanie Kendal is a Vice President in MUFG's Capital Markets Strategy group within the global capital markets and investment banking business. The team provides market based content for corporate clients to assist in strategic decision making. Focus areas include the impact of economic, political, public policy and regulatory dynamics on the US credit, foreign exchange, rates and commodities markets.

### Experience

Stephanie has spent nearly seven years as a Capital Markets Strategist. She is an active member of the University of Michigan recruiting team and is focused on the diversity recruiting effort at MUFG. Stephanie is also a part of MUFG's DEI, Culture & Philanthropy (DCP) Council.

### Education

Stephanie graduated with honors from the University of Michigan's Ross School of Business with a BBA .

### Personal

Stephanie is actively involved in NYC's iMentor program, mentoring high school students with their journey to college graduation. She also volunteers at Experience Camps, a free summer camp program for grieving children.



## Angela Sun

Analyst  
Capital Markets Strategist  
New York, NY

Angela.Sun@mufgsecurities.com  
(212) 405-6952

### Role

Angela Sun is an Analyst in MUFG's Capital Markets Strategy group within the global capital markets and investment banking business. The team provides market based content for corporate clients to assist in strategic decision making. Focus areas include the impact of economic, political, public policy and regulatory dynamics on the US credit, foreign exchange, rates and commodities markets.

### Experience

Angela previously interned at MUFG working in Capital Markets within the Equity Capital Markets and Leveraged Finance divisions. She is also an active member of the Carnegie Mellon University recruiting team.

### Education

Angela graduated with honors from Carnegie Mellon University's Tepper School of Business with a BS in Business Administration with an additional major in Statistics and a minor in Media Design. She was a member of Alpha Kappa Psi business fraternity and the Undergraduate Entrepreneurship Association.





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