# The 2025 G4 outlook

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# Key views in a nutshell

- **Macro:**
  - US growth outperformance vs Europe accelerates. Tariffs exacerbates the problem. Labour market slowdown the risk vs business activity holding up.
  - European growth struggling from a slow easing cycle, China liquidity trap and a lack of fiscal easing. Service inflation in Europe to slow faster than expected but goods inflation a key risk to all with rising natural gas prices.
  - Strong Service growth in Japan keeps it’s cycle de-correlated from peers. BOJ to hike rates slowly but with political risks ahead (US tariffs, Japan election risks).
  - UK data to deteriorate in early Q1 after the budget impact on employment becomes clearer. BOE to become more forward looking less Service CPI driven.

- **Central banks:**
  - Fed to cut less (~4% terminal by Sep25) than European peers (1.5% ECB, 3.25% BOE by Sep25).
  - Japan remains on a hiking path to 1% by early 2026.

## Key views in a nutshell

- **FX:**

**USD strength in early Q1** (EUR 1.01), followed by mild weakness Q2 onwards (1.05 end 2025) after maximum tariff pain is priced in and US data surprises turn lower.

GBP to no longer shine vs peers in Q1 (1.21) as BOE accelerates rate cut path.

USD/JPY to rise to 160 in Q1 as we price in maximum tariff pain, but then fall into end 2025 as the BOJ hiking cycle narrows rate differentials.

- **Rates:**

USD-EUR beta decoupling to continue (short USD duration vs long EUR duration) on the back of fundamentals (macro, fiscal, Fed-ECB divergence).

GBP duration will rally once data turns south more sustainably.

  – **Steepening across the G3**, but for EUR and GBP rates it will be front-end/belly driven, while in USD it will be long-end driven (higher inflation and real risk premia).

JPY rates to continue to sell off as the BoJ delivers further hikes. JGB curve to flatten into the super long end as this part of the curve remains more supported by domestic and foreign demand.

# Events to track, risks to follow

- **Potential tradable narratives in 2025**

### Q1 2025

- **Macro:** Do US data surprises turn lower in January thanks to the rates selloff in Oct/Nov? Does the new UST secretary use the quarterly refunding announcement to increase coupon issuance? Rising European natural gas prices to boost CPI and challenge the idea of 50bps cuts?
- **Politics:** Trump inaugurated 20th Jan. Executive orders issued in quick succession, how quickly and how far do tariffs go? Do we see weaker NFP prints due to deportations and DOGE job cuts? Germany's Federal election delivers a new coalition in Feb, do they reform the debt brake or suspend it again? Will EU leaders tighten Russian sanctions before talks begin? With US protectionism – is EU reform alive or dead?

### Q2 2025

- **Macro:** Does UK data deteriorate after the budget in a way that triggers back-to-back BOE cuts (as we expect)? Does China finally respond to tariffs with a proper fiscal stimulus? Does the US tariff plan lead to positive reforms in the EU (such as capital markets union or as Draghi suggested an EU wide industrial plan). Do the 2025 Shunto negotiations trigger another leg of BoJ hikes repricing?

- **Politics:** After escalating pressure on Russia to come to the table in Q4/Q1 do we see a ceasefire agreed in Ukraine lead to sanctions relief, lower energy and commodity prices? Does UK Chancellor Reeves' spending review and multi-year plan spook or relief GBP markets?

### Q3 2025

- **Macro:** By the end of summer we should be approaching the end of cutting cycles by the ECB, BOE and Fed. The monetary easing we've had since 2024 leads to a rebound in cyclical indicators. Does a rebound in macro and commodity prices lead to markets pricing in a hiking cycle and the end of the EUR duration rally? Or does US tariff induced excess supply in Europe and China lead to negative rates becoming a possibility again?

- **Politics:** After a messy cohabitation, does Le Pen withdraw support and allow for fresh snap elections in France? Does it lead to an anti-EU rightward shift once again or do the left of centre parties outperform and drive-up French issuance plans?

### Q4 2025

- **Macro:** Does US QT come to an end in 2025 and provide relief for US duration just as we gear up for the impact of US tax cuts/reform? Does the market price in the chance of higher terminal rates in Japan for 2026 after raising rates to 2006/07 levels already? Is this the moment where we price in negative rates for Europe in 2026?

- **Politics:** Two years after the Hamas-led attack on Israel, does Netanyahu achieve his aims and agree to ceasefires with Hamas in Gaza or does the more friendly US administration lead to hawkish actions towards Iran?

# The 2025 outlook - US

# The US Macro background

- **Growth:** Above trend (Nowcasting 2.5% vs Fed's 1.8% trend assumption).

- **Inflation:** 2.6% CPI, above target and momentum bouncing.

- **Unemployment:** Comfortably holding at 4.1% despite a weak NFP, remember Powell's red line at 4.3%. The next print likely to bounce thanks to reversing Hurricane impact.

- **The Fed:** Mizuho US Econ sees **potential for skipping Dec or Jan**. NFP to bounce back, data stronger than previous SEP forecasts and uncertainty over tariff impact might urge caution in cutting rates.

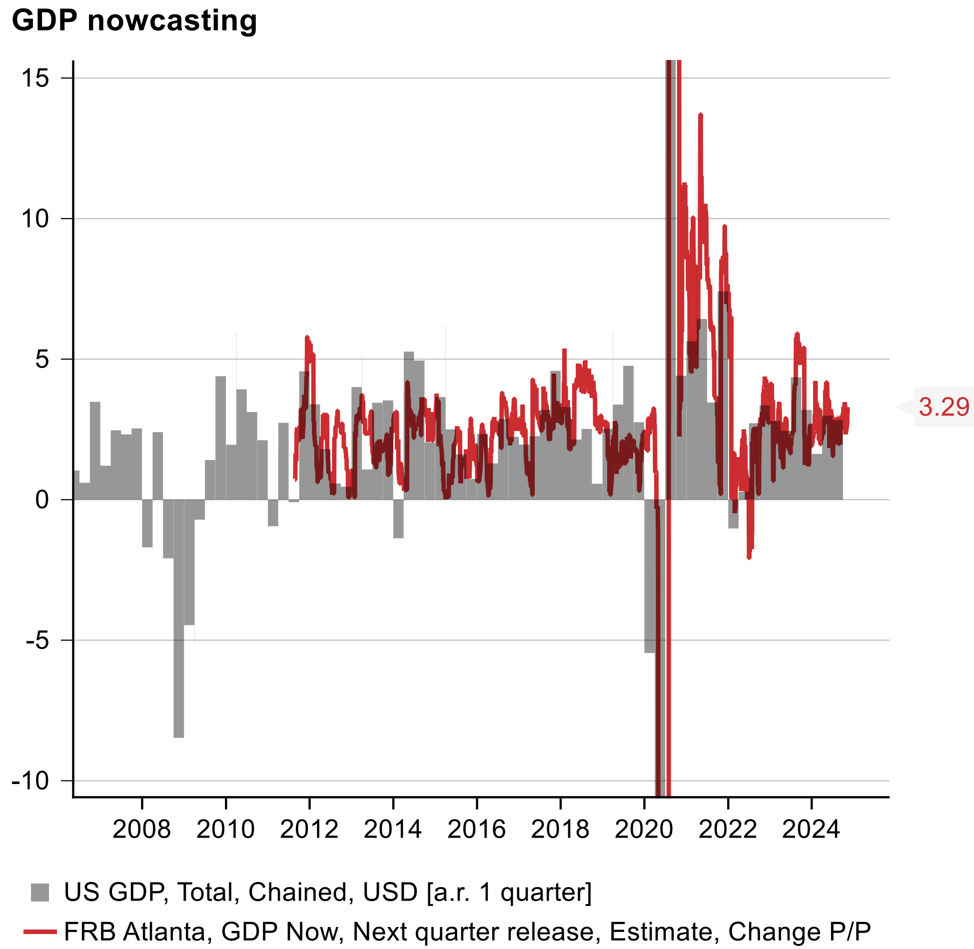
- **The USD:** US exceptionalism was in play before the election, now we add on top tariffs lowering European and Chinese competitiveness. **EUR 1.03 by Dec, 1.01 in Jan**. Then we've priced peak tariff and perhaps USD data surprises turn in Jan to allow a mild EUR recovery back to **1.05 by end 2025**.

- **Rates:** We're looking for **4.60% in UST10yr by end 2024 and 5% by end 2025**, the front end has already done a lot of the lifting in October/Nov selloff. The USD FX tariff trade will remain clearer for markets, but we are looking at higher issuance in US, UK, Japan and potential China when they respond to tariffs in Q1. Will term premium please stand up?

# US Growth

1. **Despite gloomy manufacturing surveys, Nowcasting has US GDP above 2.5%**
2. **With consumer credit growth in a weak place, but it might recover**

## US GDP nowcasting




## SLO survey suggests consumer credit growth might recover

# US Inflation

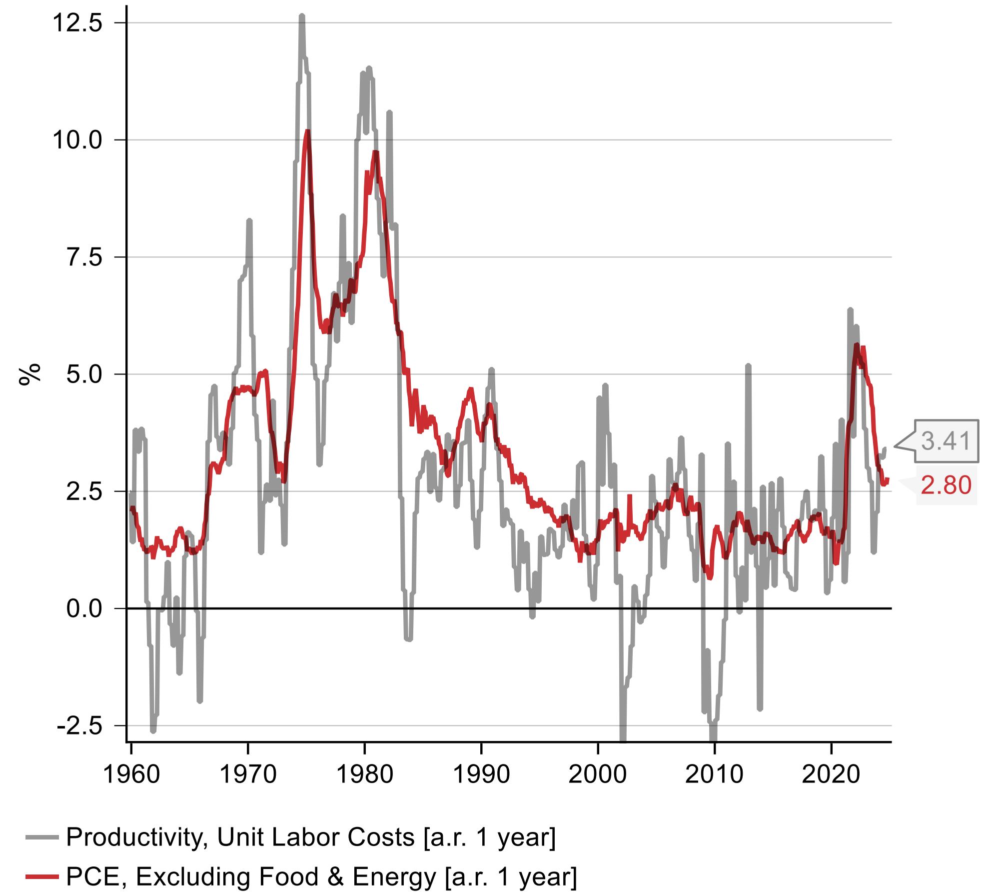
1. **US PPI suggests a low risk of headline CPI rebounding**
2. **Unit Labour costs collapsing suggests core PCE to drop too**

## US PPI vs CPI

**PPI vs CPI**


## Unit Labour costs vs PCE

**Unit Labour costs lead core PCE?**

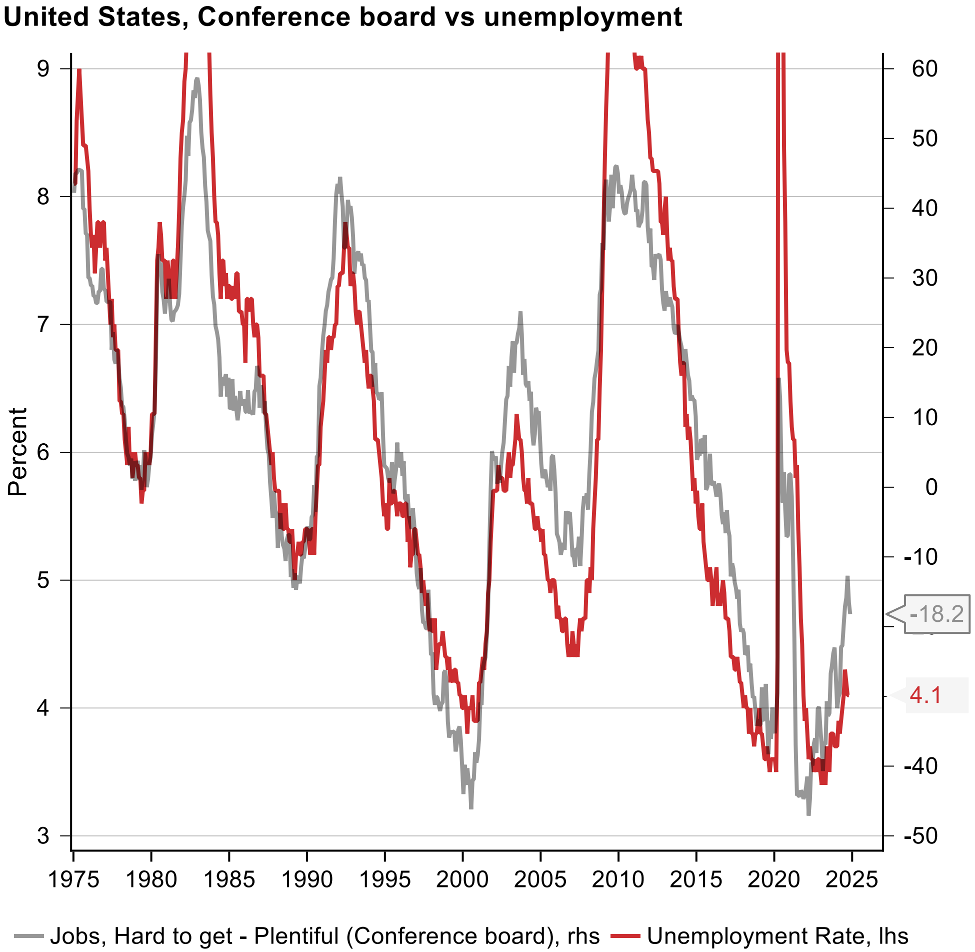



*Source: Macrobond, Bloomberg*

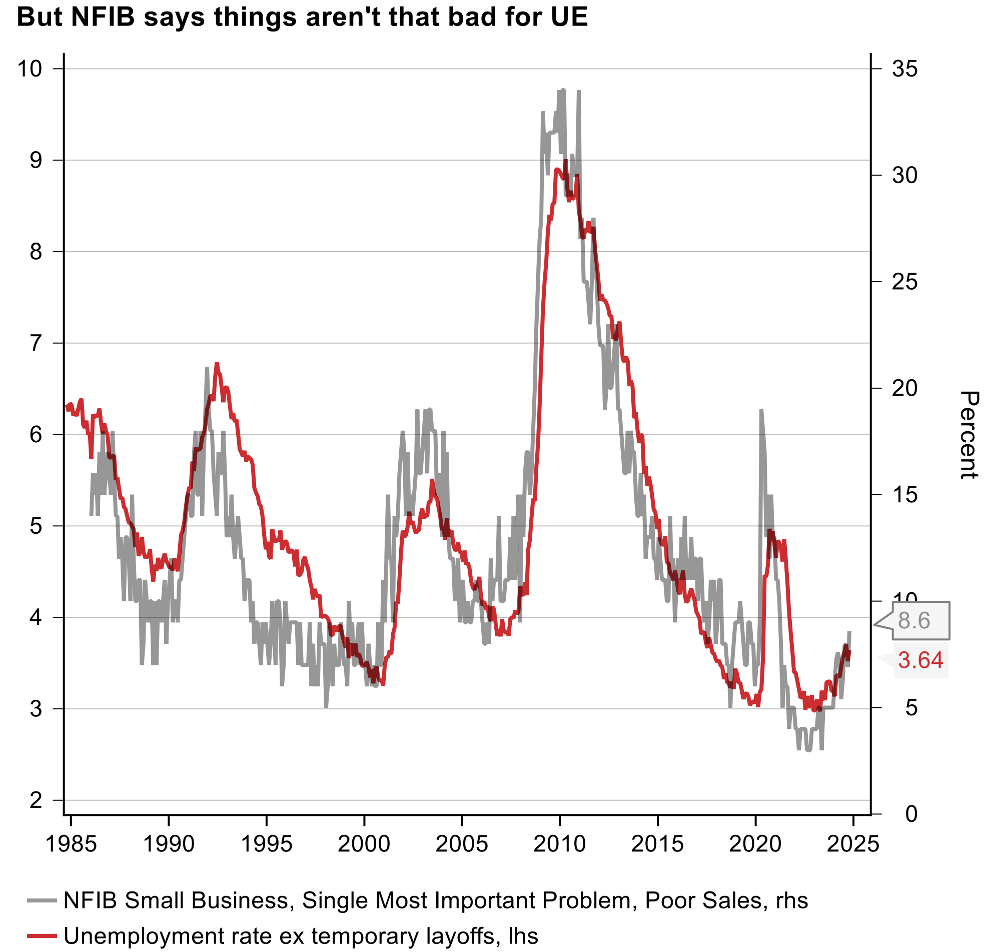
# US Labour

1. **Will Unemployment weaken as much as the conference board suggests? We doubt at that pace.**
2. **NFIB might be a better gauge of Labour market strength.**

## Very dovish Fed forecasts rely on very gloomy surveys




## NFIB would argue things aren't that bad



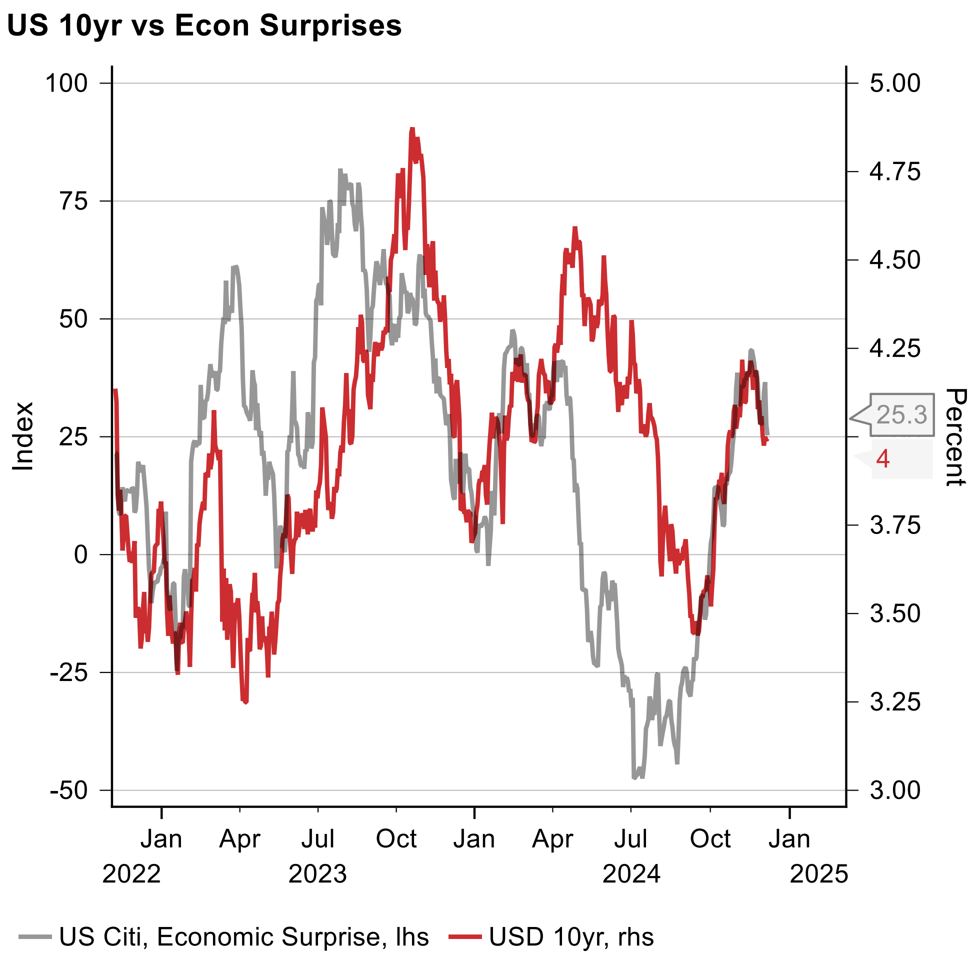


*Source: Macrobond, Bloomberg*

# US Rates

- **Can USTs continue to selloff if data surprises are turning?**
- **Can we continue to price out Fed cuts in 2025 if oil remains contained?**

## US 10yr vs Econ surprises



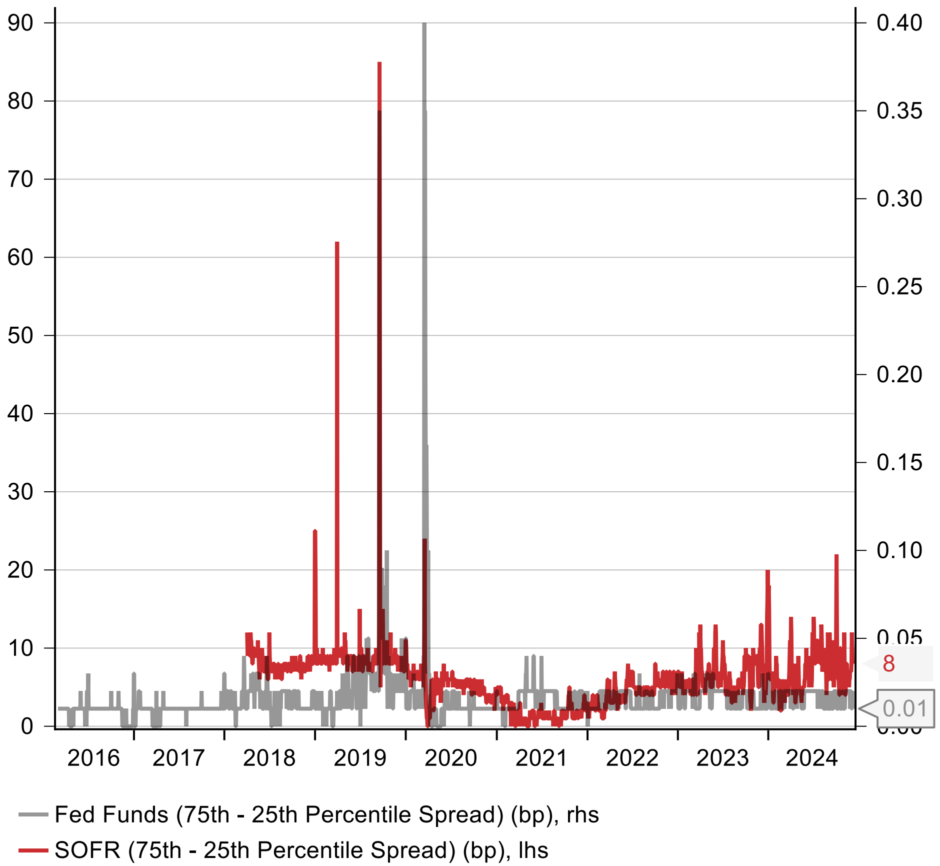

## Fed pricing vs oil

# USD liquidity conditions (1)

- **The last quarter-end brought wobbles in USD liquidity. Will this repeat around year end?**
- **Fed argues that reserves are still ample.**

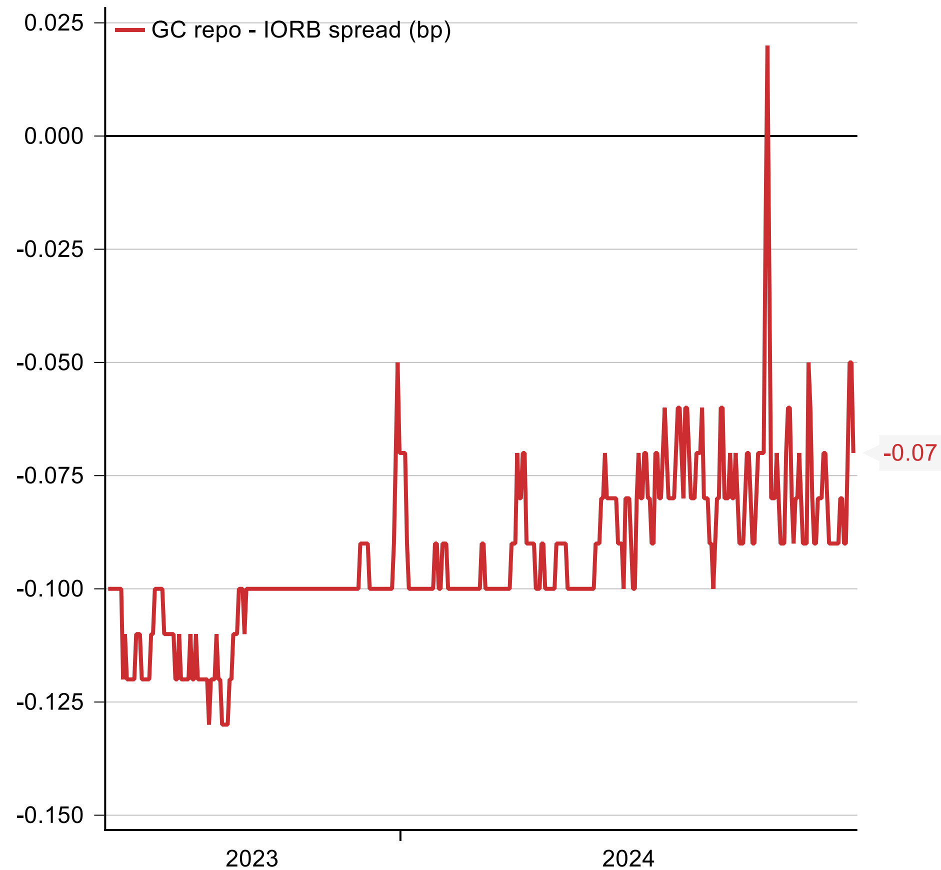
## September showed higher dispersion in SOFR…

**Fed Funds vs SOFR dispersion**




## … and a move to positive GC repo – IORB spread!

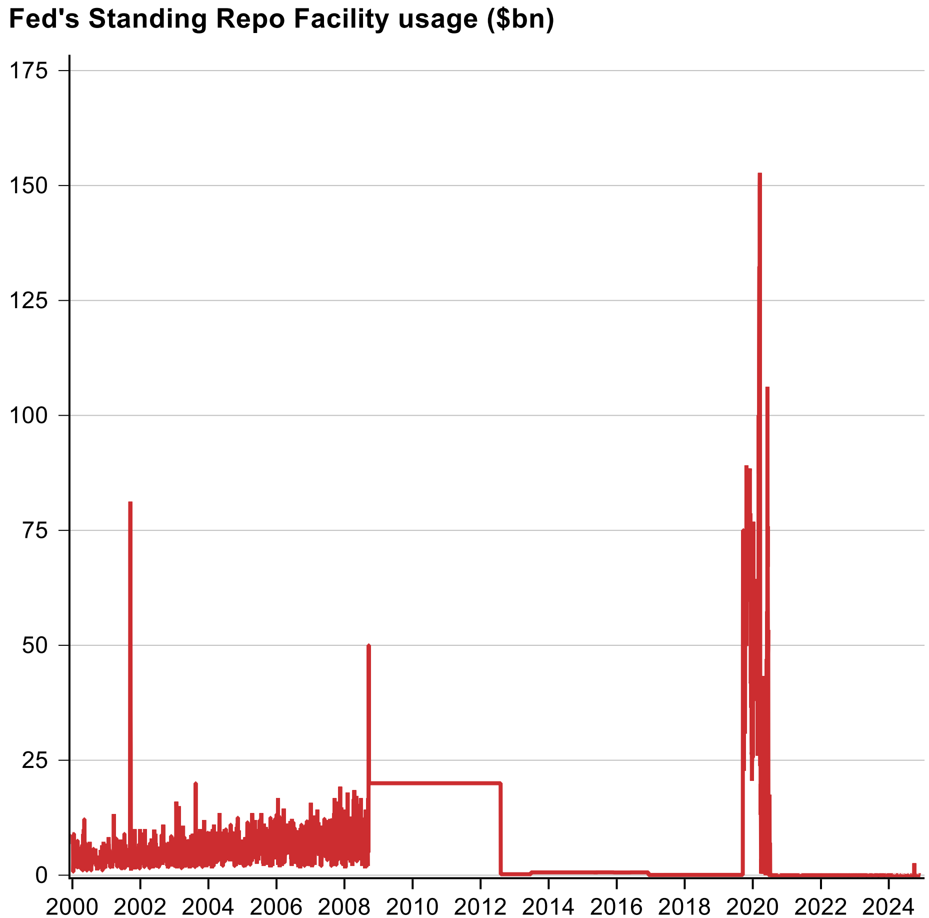
**GC repo vs IORB spread**



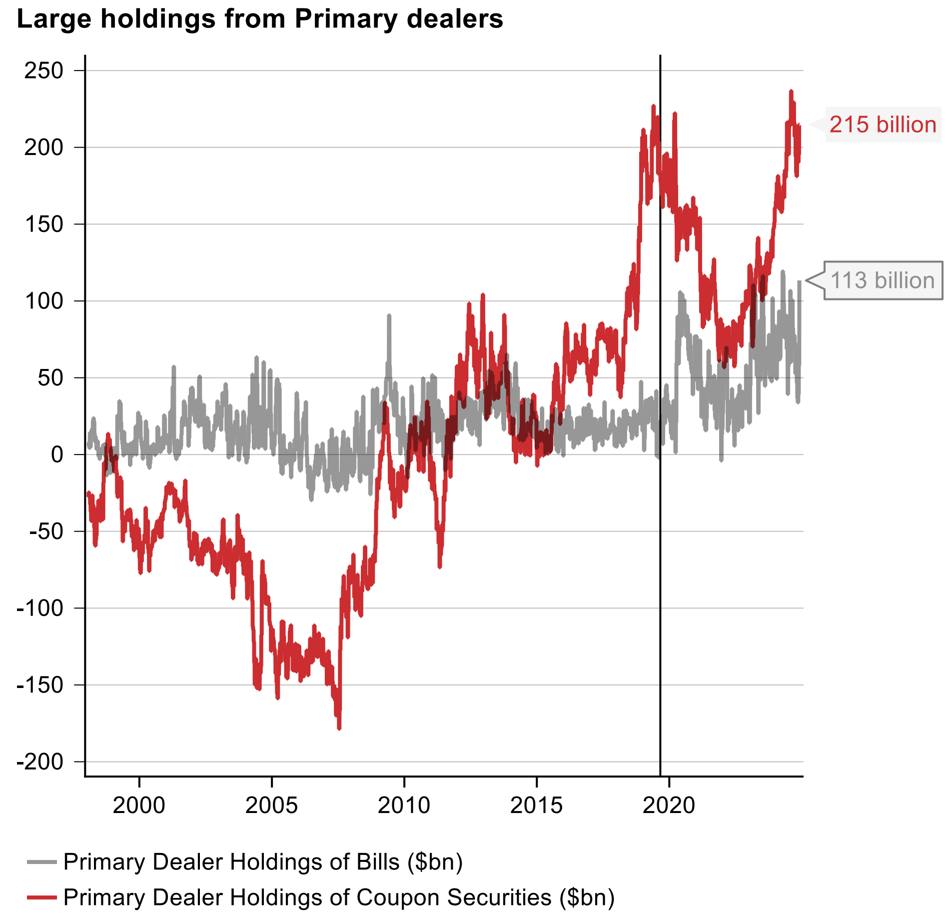
# USD liquidity conditions (2)

- **Unusual moves that require close tracking.**
- **We think there is a high chance that the September wobbles come back around year end.**

## Fed's SRF tapped for the first time in years in Sep24




## Primary dealers' holdings also approaching previous stress levels

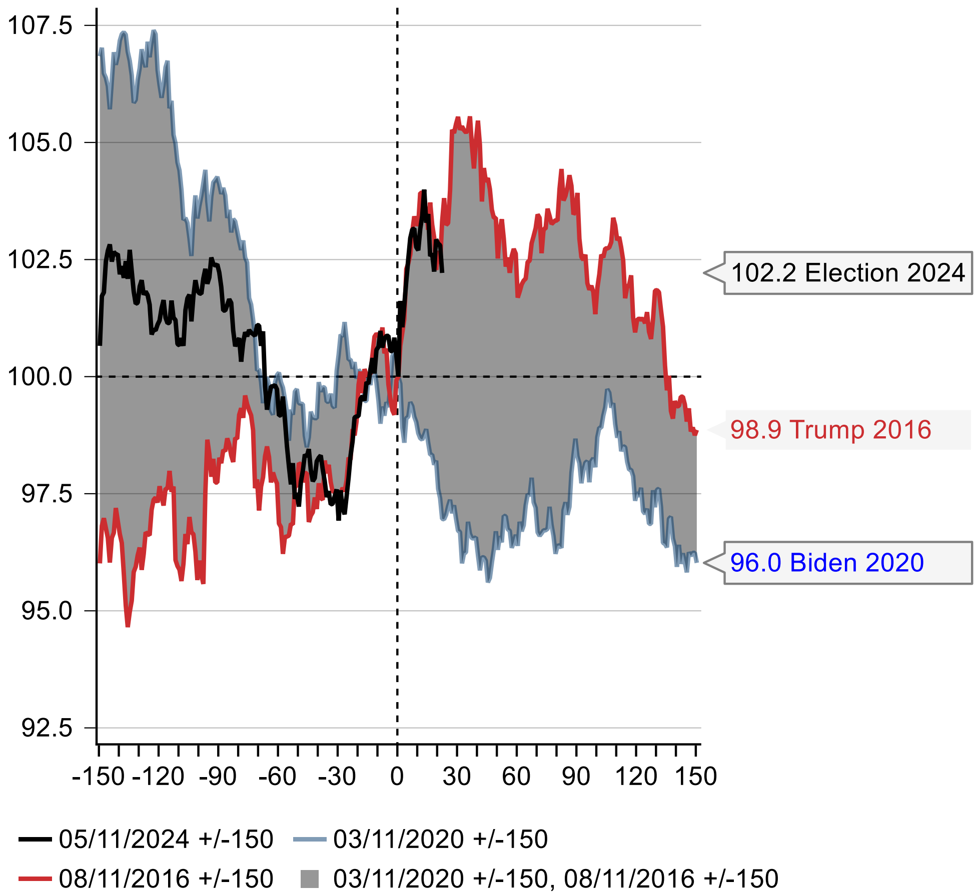


# USD FX

- **So far the USD is following the 2016 election path very closely**
- **UK and EA Econ surprises drifting into the dovish quadrant**

## DXY into elections

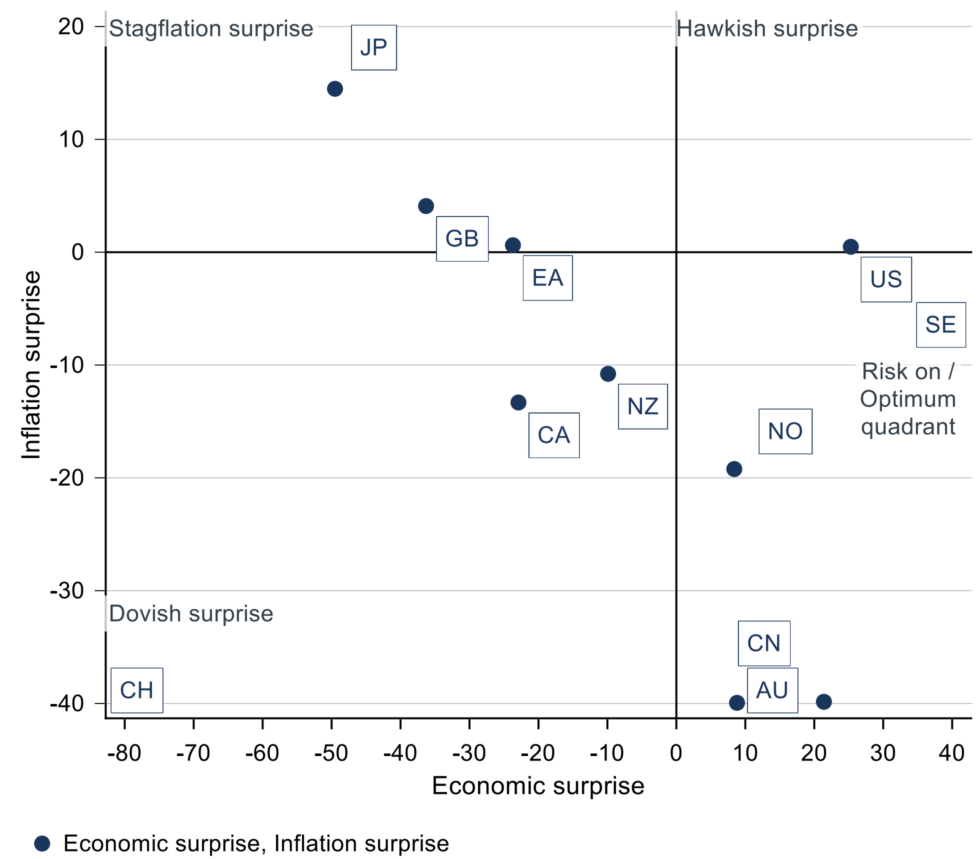
**DXY trading days into the previous two elections**




## Economic vs Inflation surprise (current levels)

**Economic vs inflation surprise**

Source: Citi



# The 2025 outlook - EA

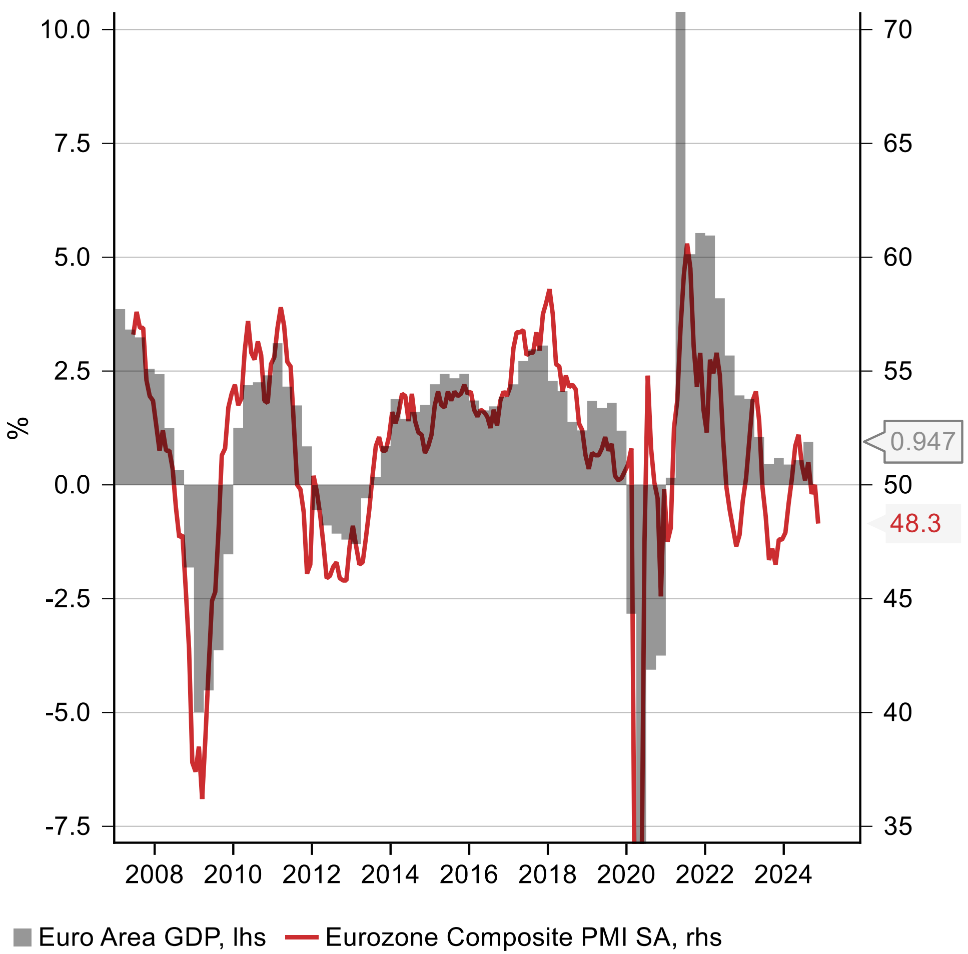
# The Euro Area Macro background

- **Growth:** Composite PMI at 48.1. The potential for a rebound in cyclical indicators next year has been dimmed by a lack of proper fiscal stimulus in China, French and German budget constraints and now US protectionism risks. But recent monetary easing should lead to a rebound in H2 2025.
- **Inflation:** At 2.3% and rising thanks to energy costs. It may lead to restraint from the ECB at December's meeting with just a 25bps cut, not 50bps.
- **Unemployment:** Unemployment at 6.3% in September, a record low and below equilibrium. Italy and Spain UE are falling, but Germany rising. Vacancies (official and Indeed data) are generally falling and the EC's expected employment indicator too.
- **ECB:** 25bps in Dec, depends on next CPI release, PMIs and US tariffs whether we accelerate to steps of 50bps. We doubt it for now until perhaps late Q1 if needed. **Terminal rate at 1.5%** in Q3 2025.
- **The EUR:** **1.03 in Dec, 1.01 to parity in Jan**. To then price maximum tariff pain and recover from Q2 back to **1.05 by Dec25**.
- **Rates:** 10Y Bund yields moving towards the **2.0% handle** into year end and move sustainably below that in 2025 as markets price in more cuts and a "below-neutral" terminal rate.
- **EGB spreads:** We are **bearish OATs** (10Y to move towards 100bp vs Bund in 2025) and **bullish peripheral EGBs**. We would use any relief-widening to add Italian and Spanish risk – better politics and growth outlook.

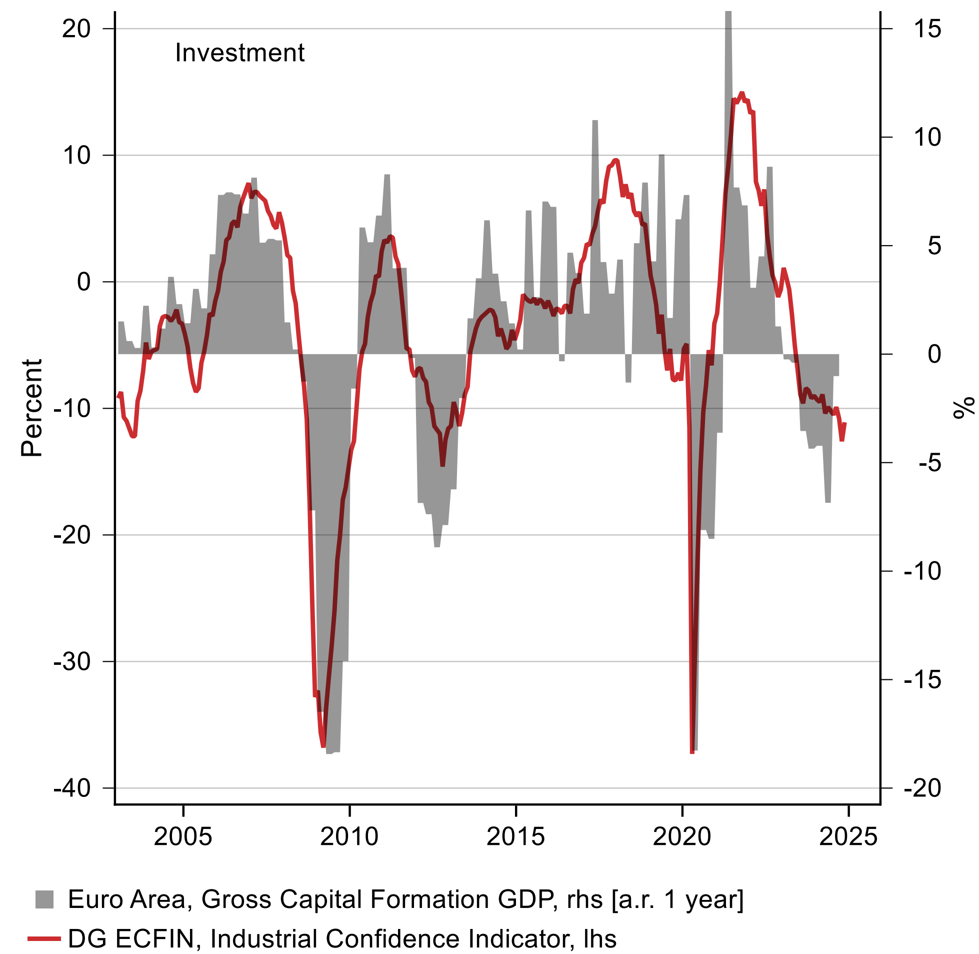
# Growth

- **The Euro Area economy looks weak. Services has been the positive story over the summer, but not anymore.**
- **Consumption expected to turn while investment remains weak. Rebound only expected to come in 2025.**

## Euro area PMIs vs GDP




## Euro area investment GDP vs investment intentions



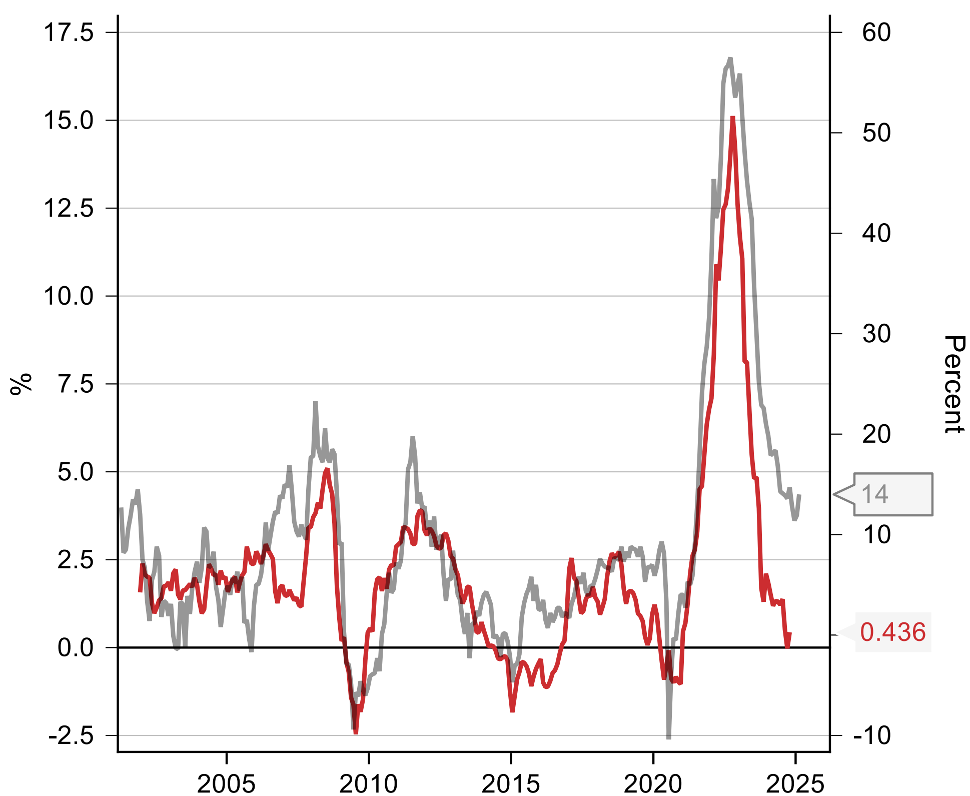

*Source: Macrobond, Bloomberg*

## Inflation

- **In the goods sector, China's exporting deflation means a strong rebound remains unlikely. Energy to put some pressure in the near term.**
- **Services inflation bounced in Summer (both Euros, Olympics helped) – surveys say a decline to come.**

### Euro CPI (Goods) vs Euro Commission survey

**Euro Area - Goods inflation**




EC Retail Trade conf, Price Expectations 3m ahead, rhs [lag 3 months]
HICP, Goods, lhs [a.r. 1 year]

### Euro CPI (Services) vs Euro Commission survey

**Euro Area - Services Inflation**


EC Services conf, Price Expectations 3m ahead, rhs [lag 9 months]
HICP, Services, lhs [a.r. 1 year]


*Source: Macrobond, Bloomberg*

# Labour

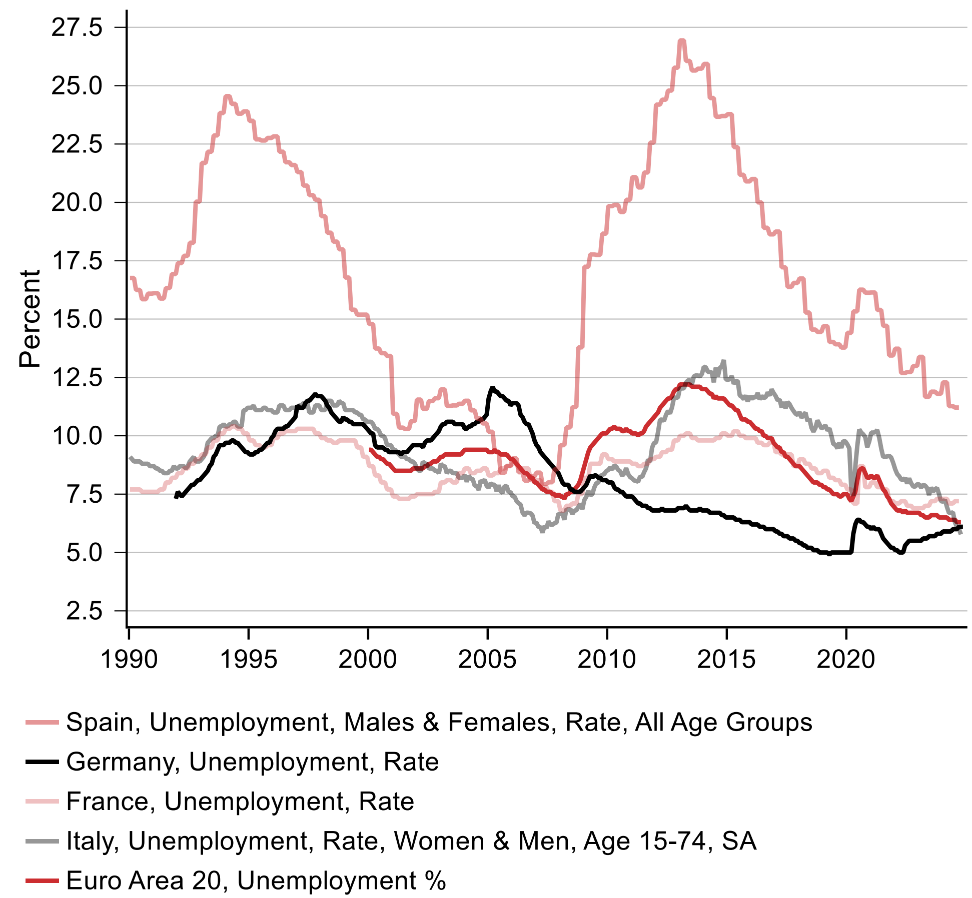
- **Wage pressures will likely fade from here, suggesting less inflationary pressures.**
- **Unemployment rates tell different stories. Bottom line: no major recession on the cards.**

## Wage pressure should fade in 2025

**Euro area price expectations from firms lead labour costs?**


## Euro area unemployment: a story of divergence

**Unemployment rates**



# Growth

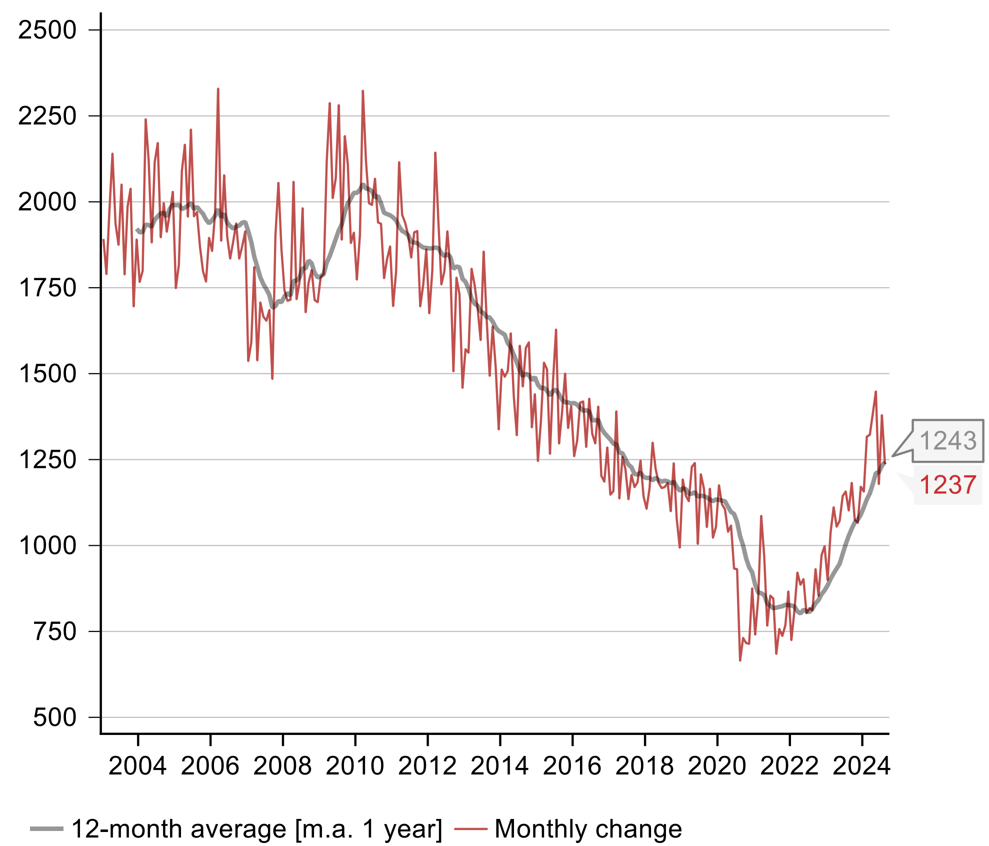
- **Germany is under a structural and cyclical downturn.**
- **Chinese stimulus may be insufficient. Outlook for growth and employment looks bleak.**

## Euro vs German PMI Manufacturing


## Germany Bankruptcies

**Bankruptcies are on the rise again**

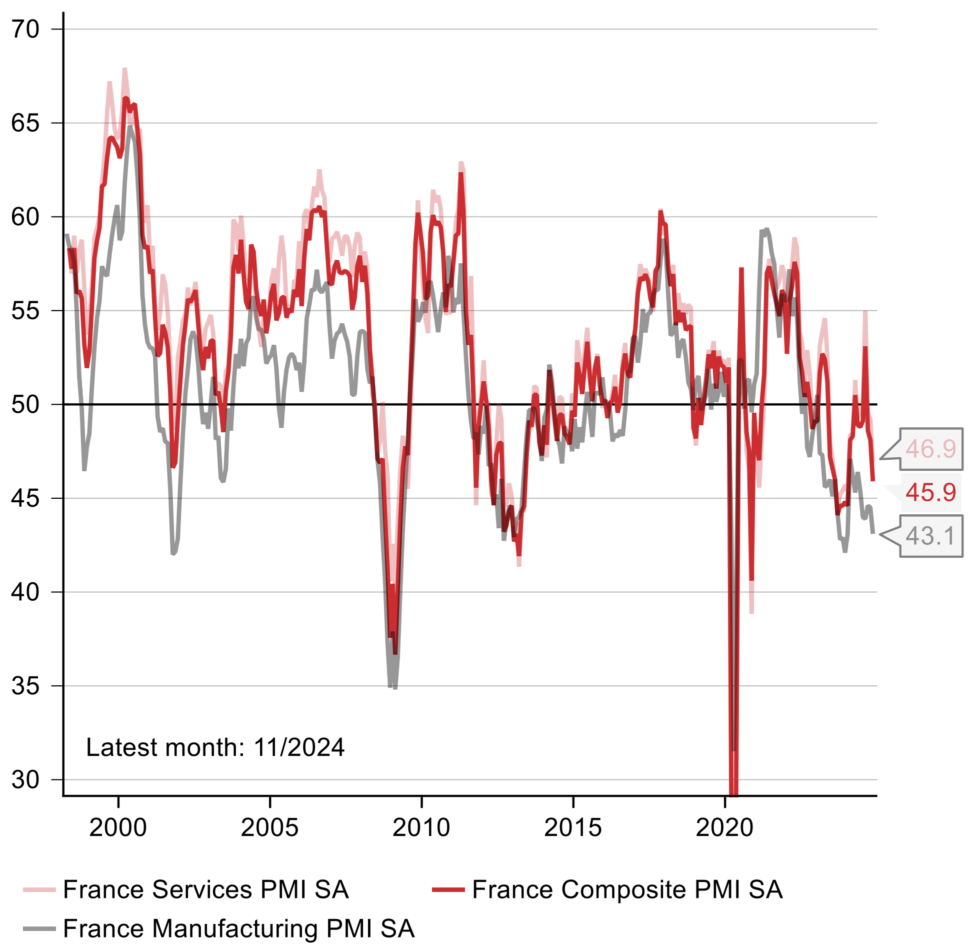
Germany - Bankruptcies, total proceedings filed



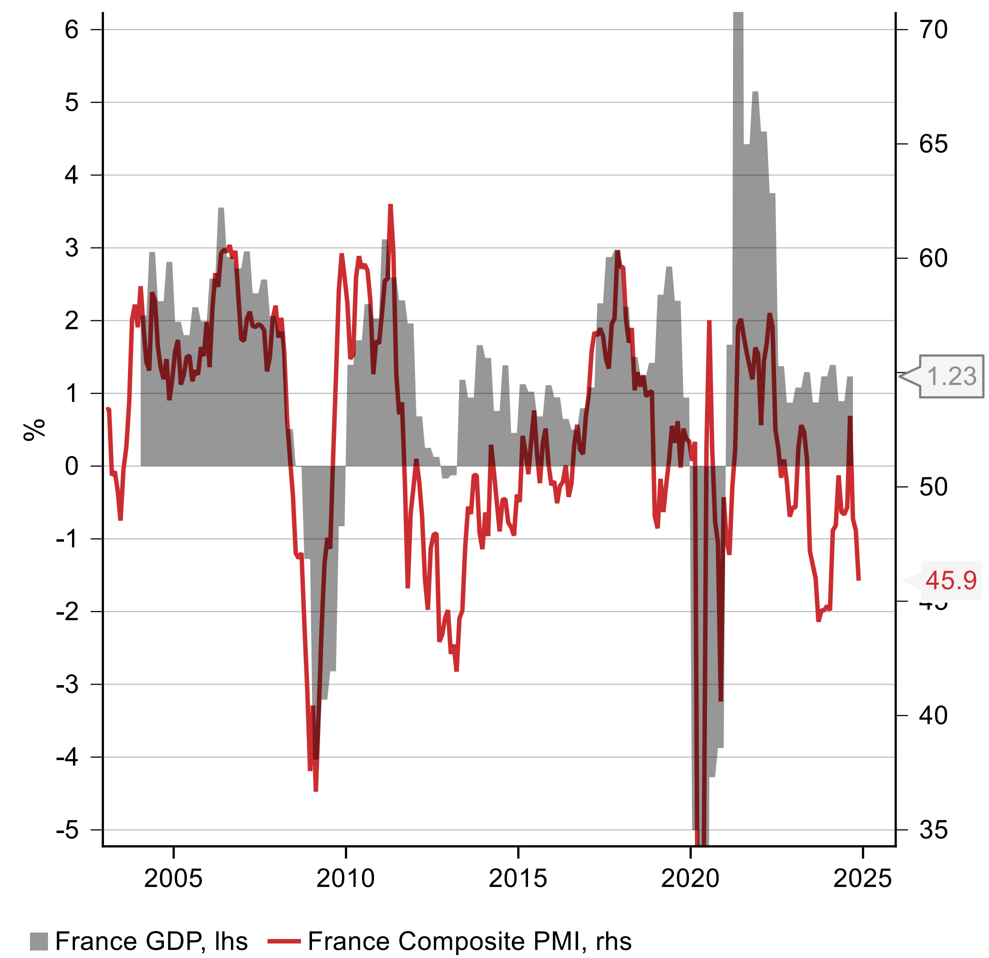
# Growth

- **France enjoyed a nice summer due to the Olympics, but the positive story is now fading.**
- **Politics and sentiment remain a big constraint on growth.**

### France PMIs



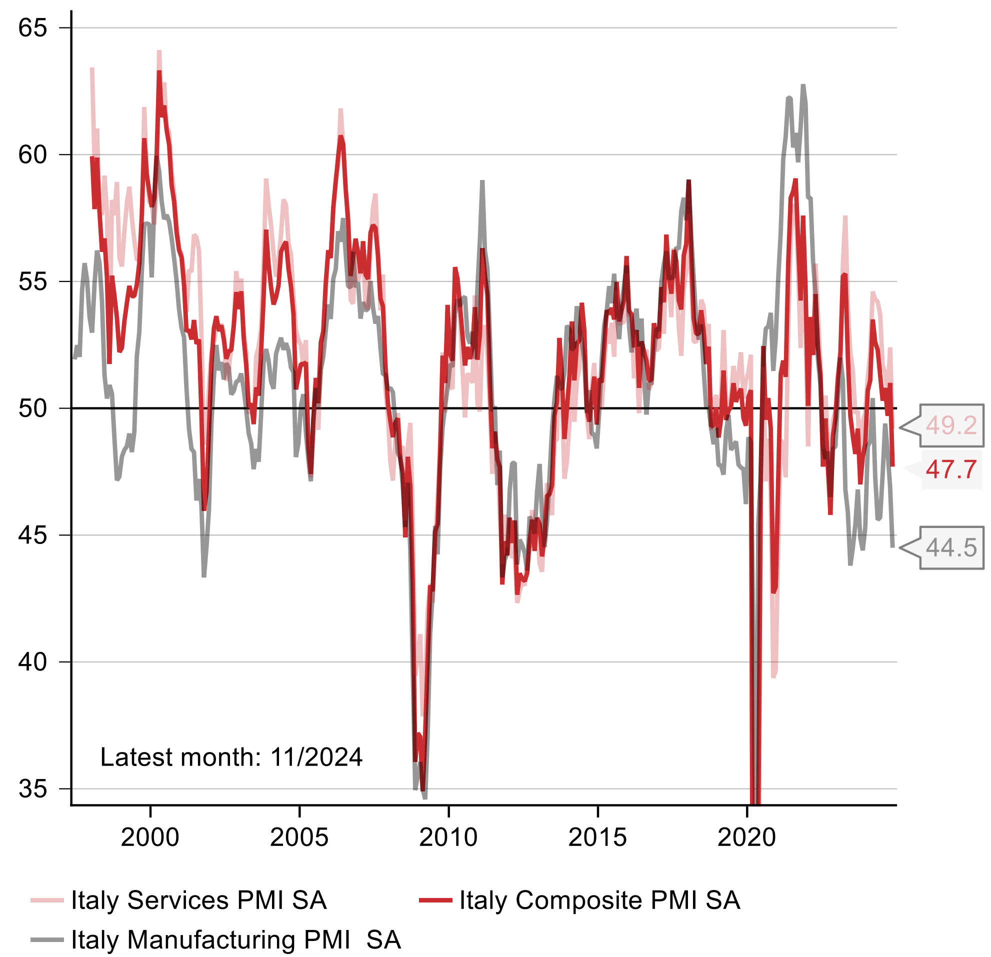

### France PMI vs GDP



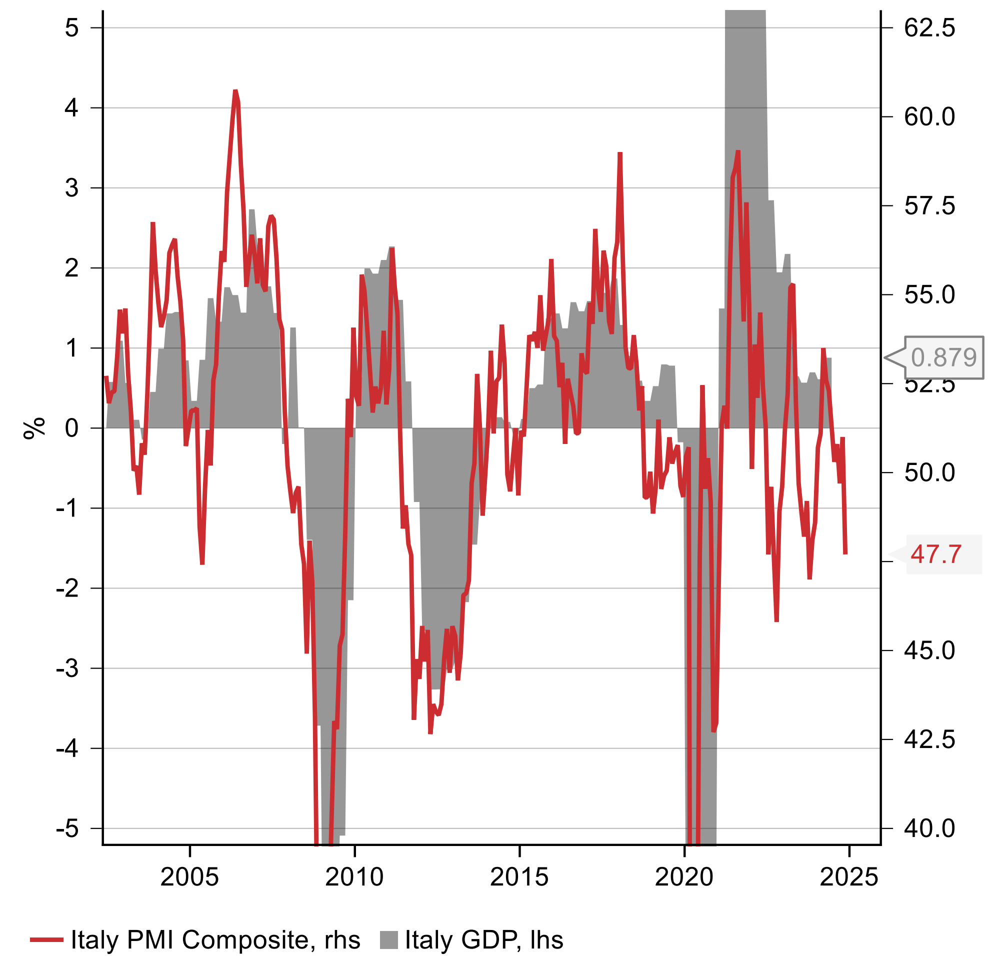
# Growth

- **Holding on, but not as good as other peripherals. Low inflation and consumption have kept it afloat.**
- **The question is whether Italy goes back to above-trend growth of 1%.**

## Italy PMIs




## Italy PMIs vs GDP

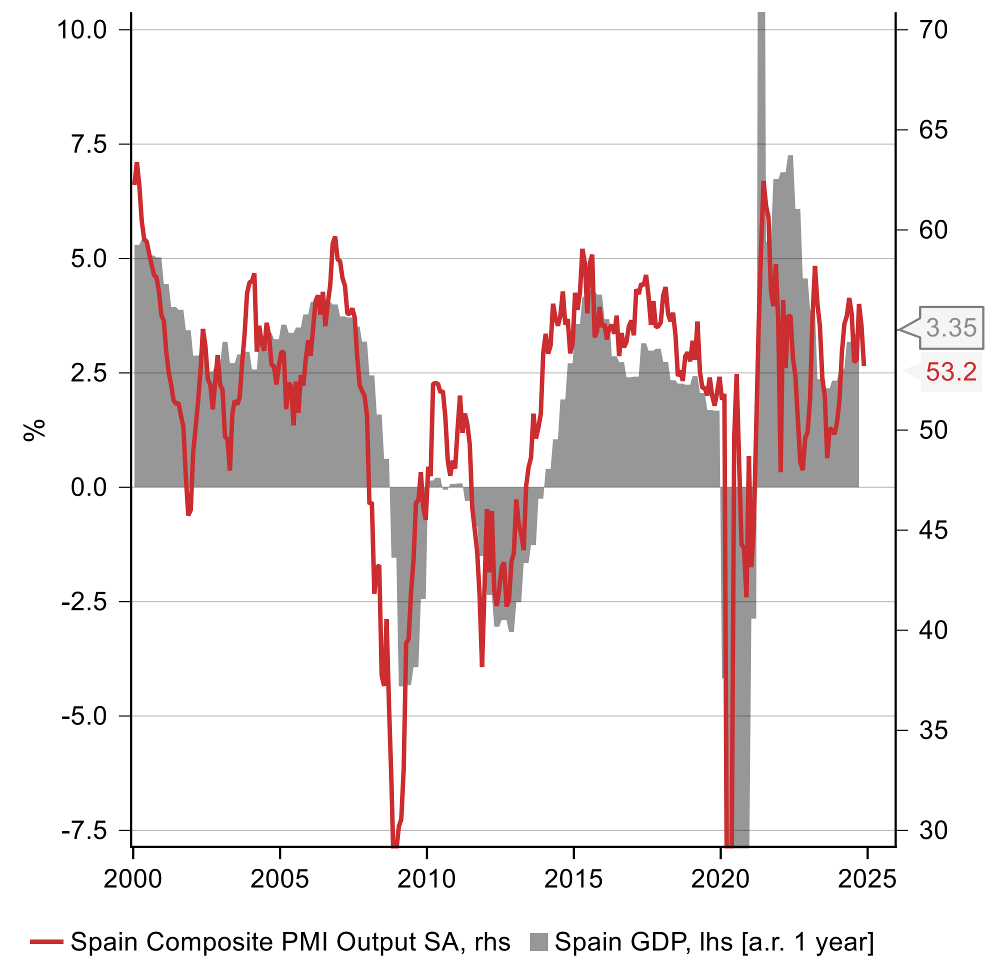


# Growth

- **Spain has been the success story this year, with growth outperforming thanks to services.**
- **Outlook remains positive, some deceleration likely but still expected to stay slightly above trend growth.**

## Spain PMIs


## Spain PMIs vs GDP

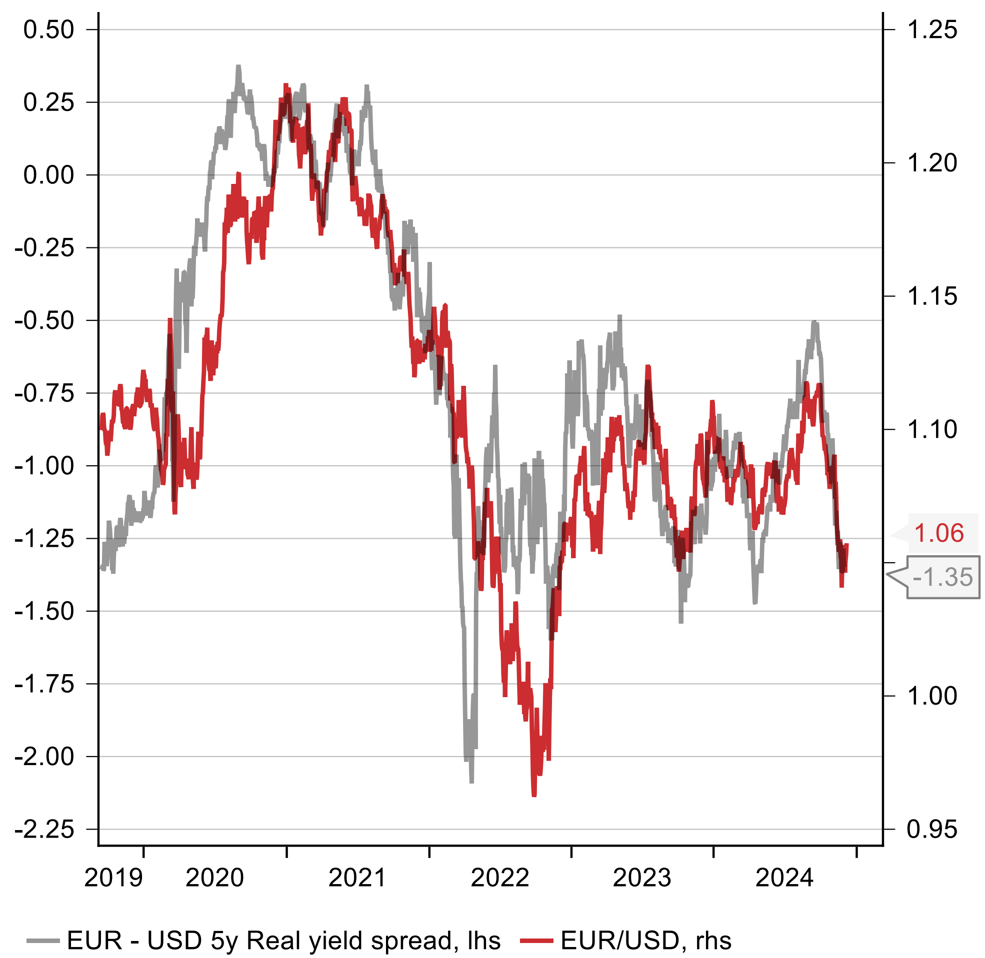



Source: Macrobond, Bloomberg

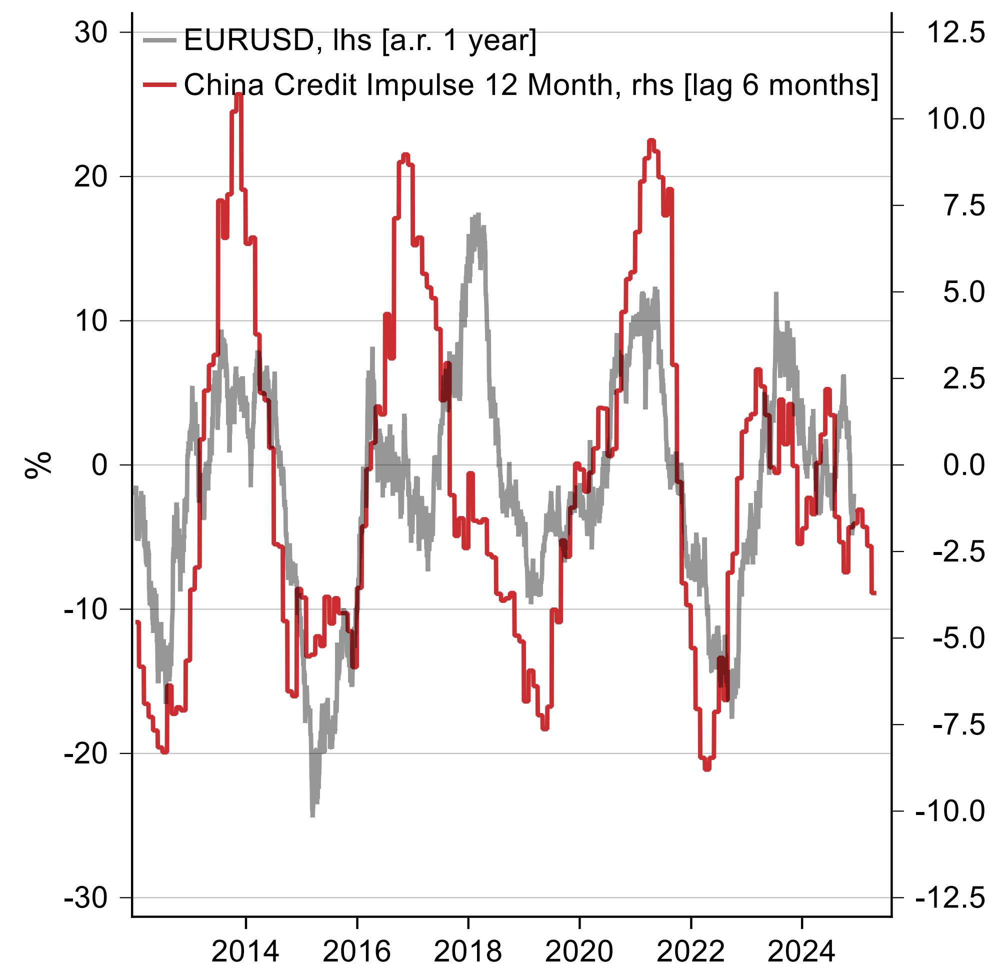
# EUR FX

- **EUR is tracking Real yields extremely closely**
- **But China's credit impulse suggests downside in the six months ahead**

## EUR vs Real yields



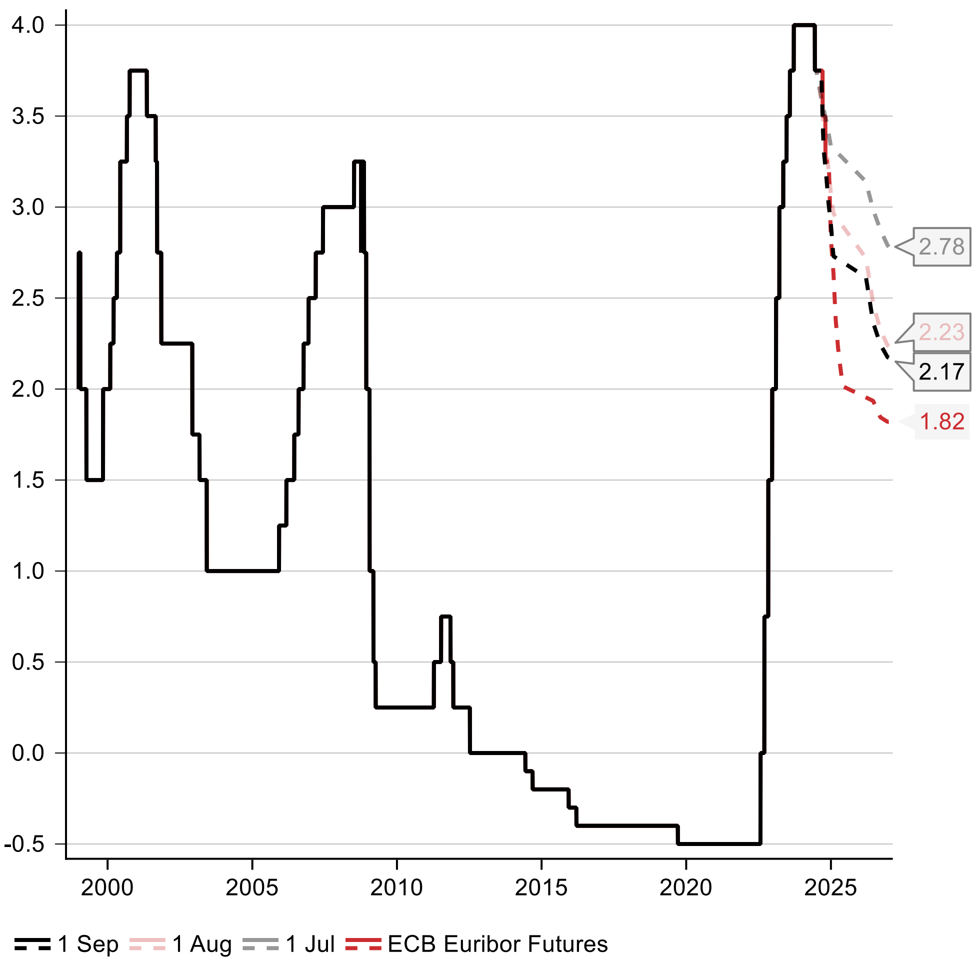

## China's credit impulse a leading indicator of EUR – downside ahead



# EUR Rates

- **The market has been pricing a higher chance of larger cuts but what about terminal rates?**
- **We think financial conditions are too tight and argue for a lower terminal (1.5%).**

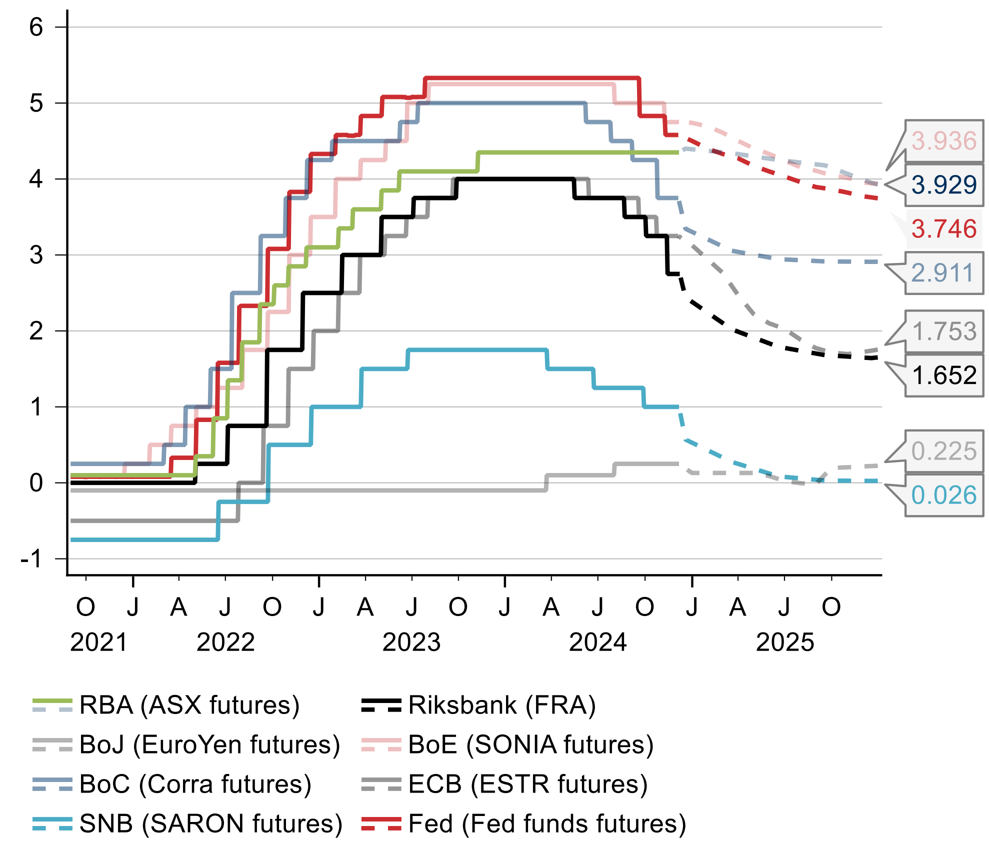
## ECB pricing (futures) – by end 2026




## Cycles compared

**The end of the hiking cycle has come**

Central banks' policy rates and market-implied rate trajectories



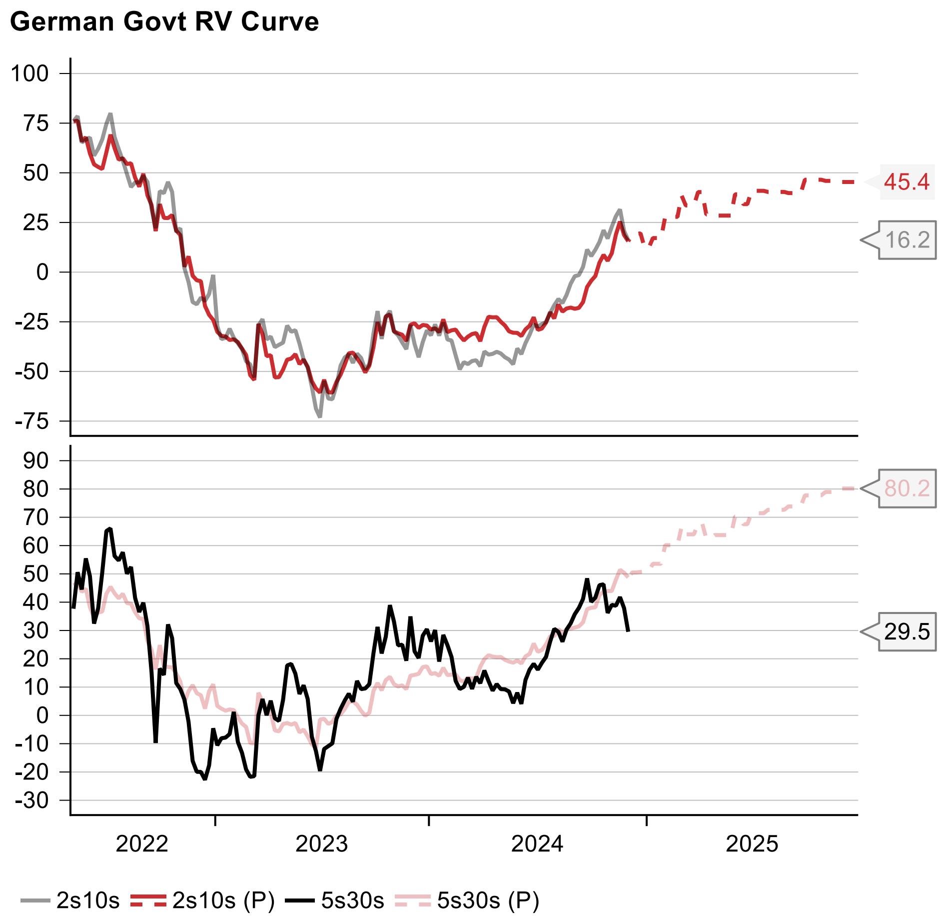



*Source: Macrobond, Bloomberg*

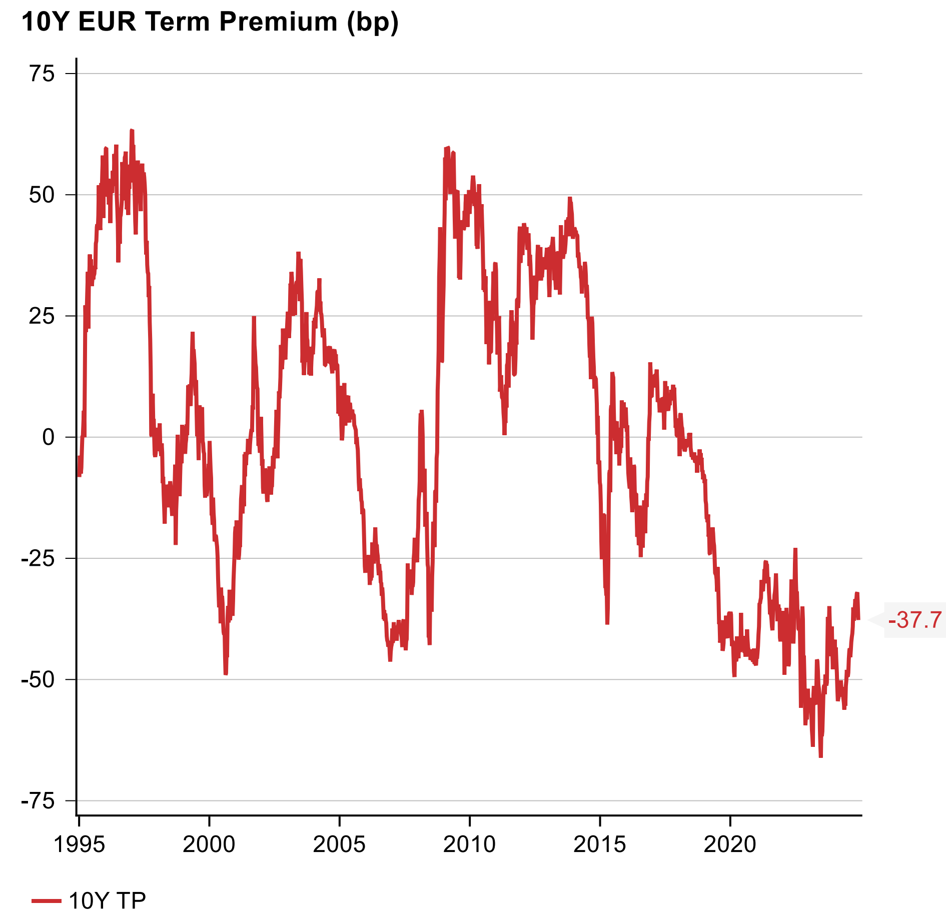
# Rates – Curve

- **As term premia normalises further and the front-end rallies, we expect more steepening of the curve.**
- **Less steepening in 2s10s vs 5s30s due to growth concerns (and lower neutral rates)?**

## Slope to normalise further




## Term premia remains relatively compressed



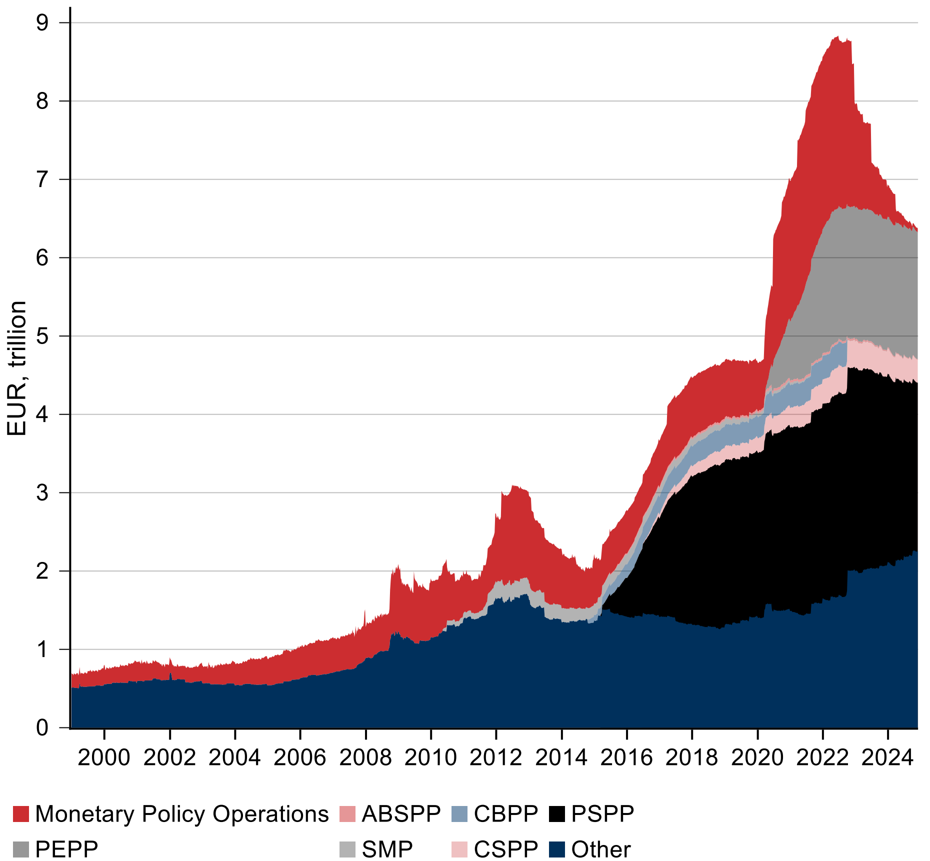

Source: Macrobond, Bloomberg

# ECB – Balance Sheet

- **The balance sheet will keep decreasing in 2025, with no more APP + PEPP reinvestments.**
- **Excess liquidity remains abundant and there is still room to collapse down further.**

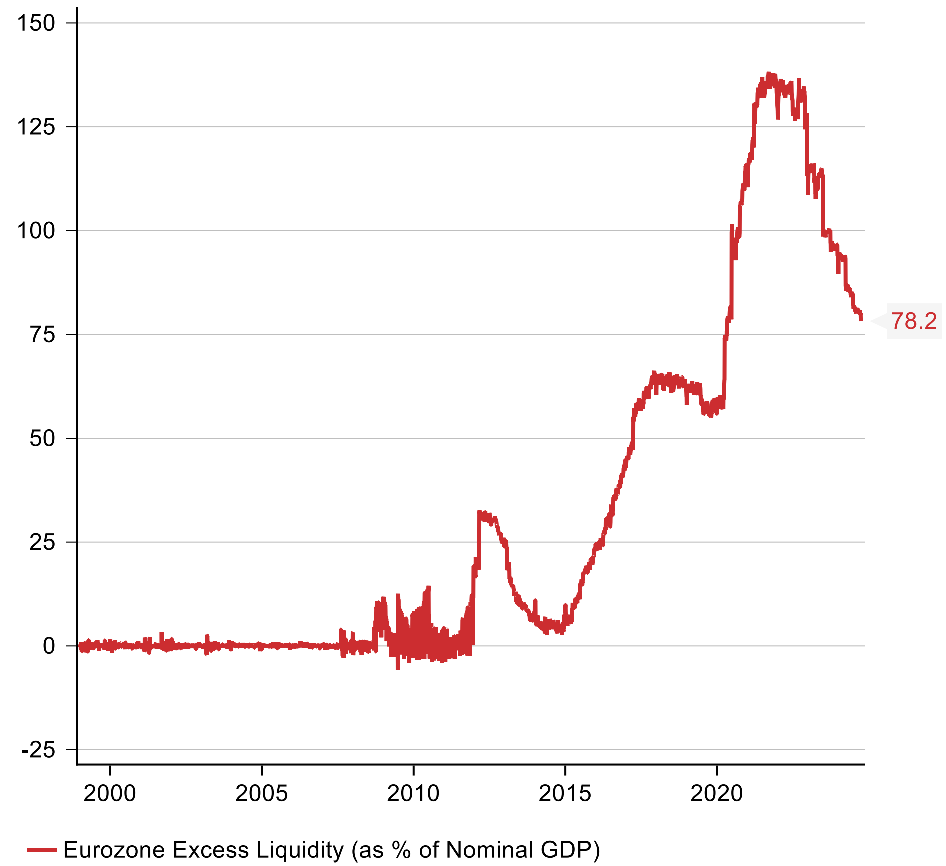
## No more reinvestments in 2025

**Breakdown of ECB balance sheet**




## Still way to go until pre-covid levels are achieved

**Eurozone Excess Liquidity (as % of Nominal GDP)**





*Source: Macrobond, Bloomberg*

# Rates – EGB Spreads (1)

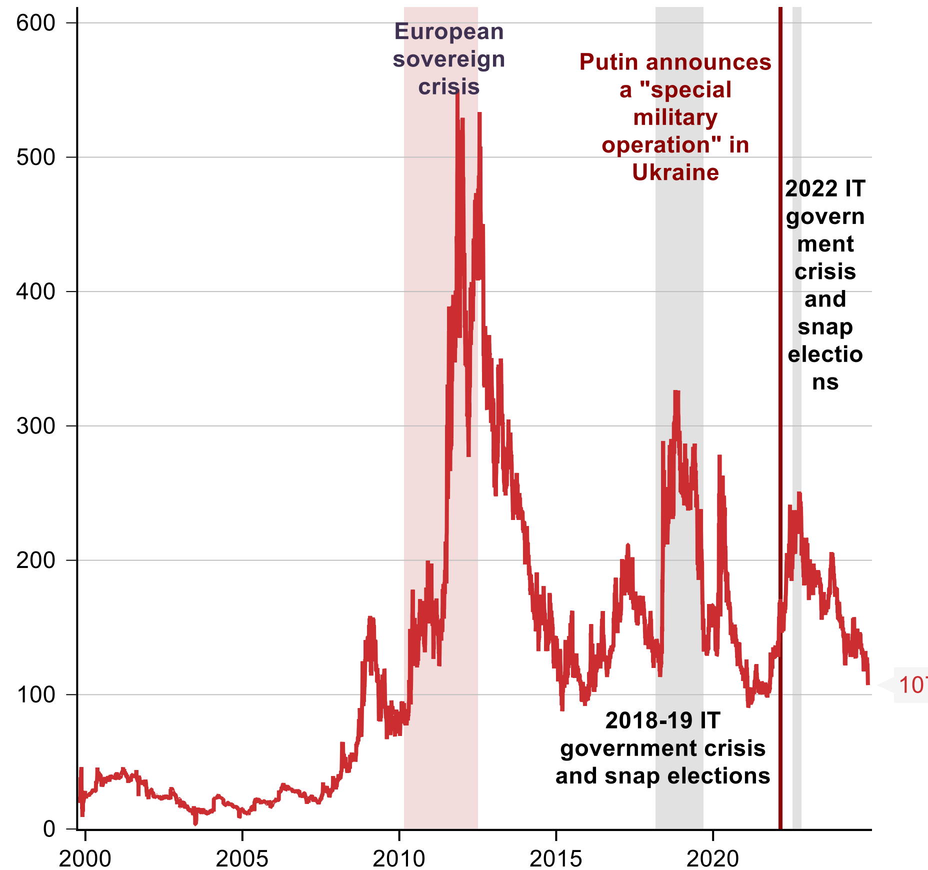
- **We remain bearish OATs in both short and medium term due to political fragility and debt burden. 75-85bp is our FV.**
- **No major rating upgrades to put a cap on further tightening in BTP-Bund spreads, but we remain constructive. 120-130bp is our current FV range. Further growth outperformance to see the spread moving tighter.**

## French spreads unlikely to go back to pre-election levels

**10Y OAT-Bund spread (bp)**


## BTPs have been one of the big winners

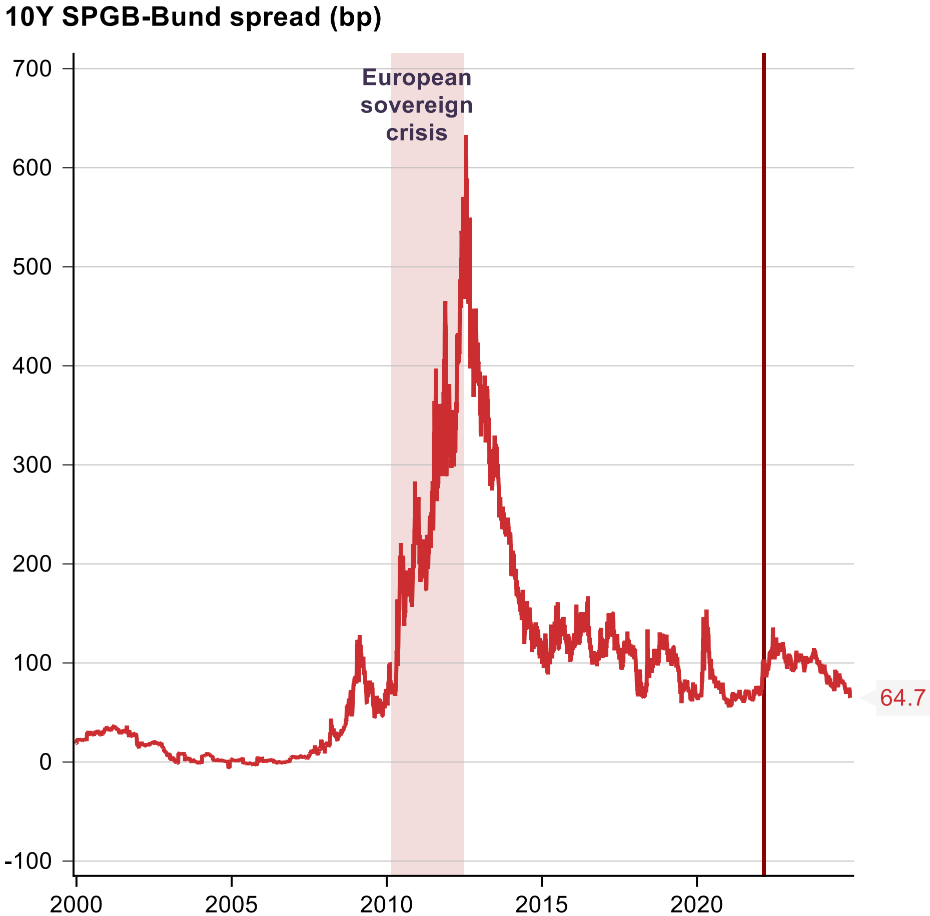
**10Y BTP-Bund spread (bp)**



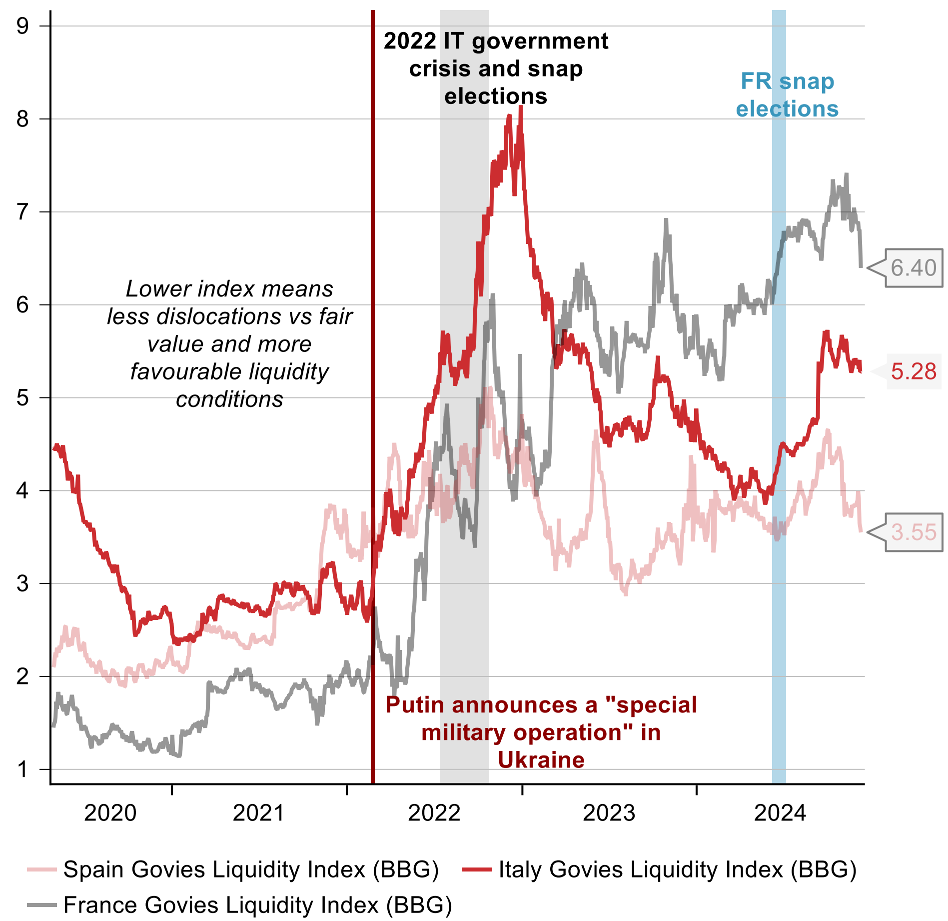
# Rates – EGB Spreads (2)

- **Spain has been one of the success stories of 2024 in EGB land, but the trade looks crowded now, especially with floods being a potential risk (more issuance?).**
- **French outflows have been positive for Spain. SPGBs are still a good investment that could see further outperformance, but the upside may be capped for now.**

## Spain: a success story that looks a bit crowded



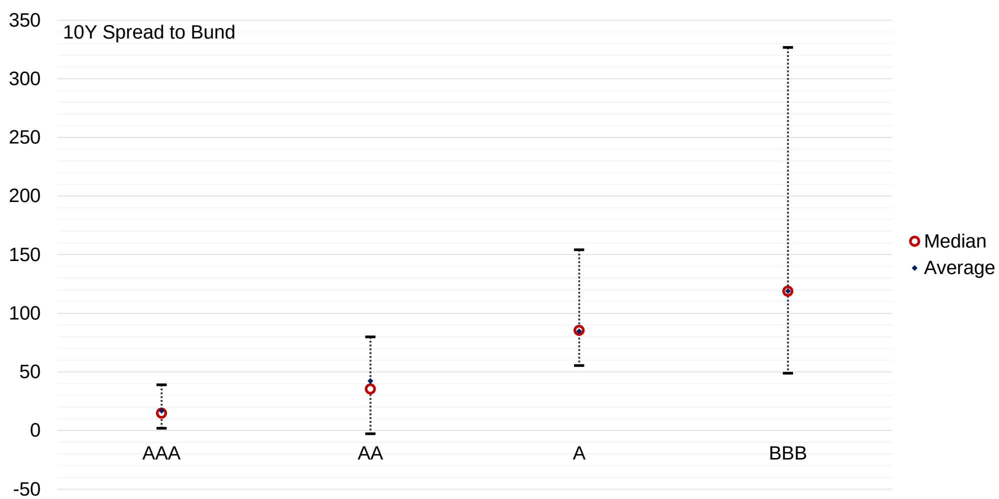

## Spain enjoys a much stable market backdrop



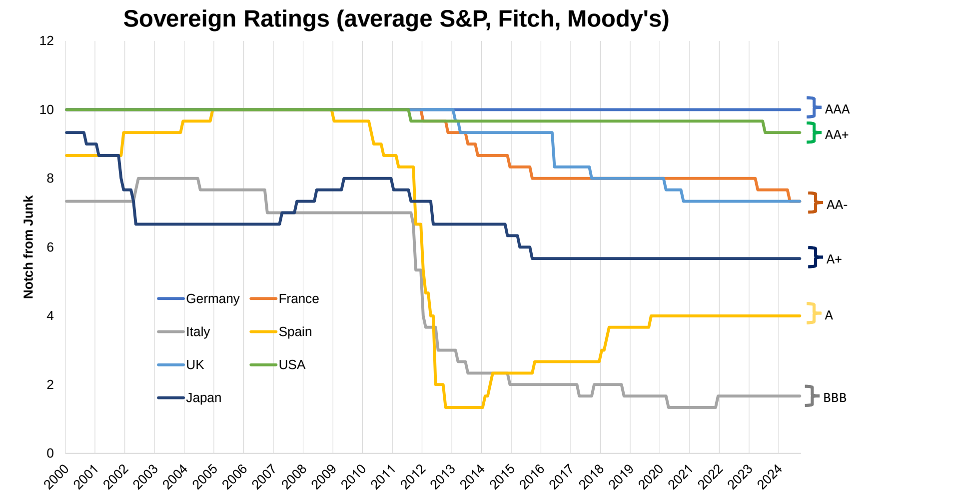

*Source: Macrobond, Bloomberg*

# Rates – EGB Spreads (3)

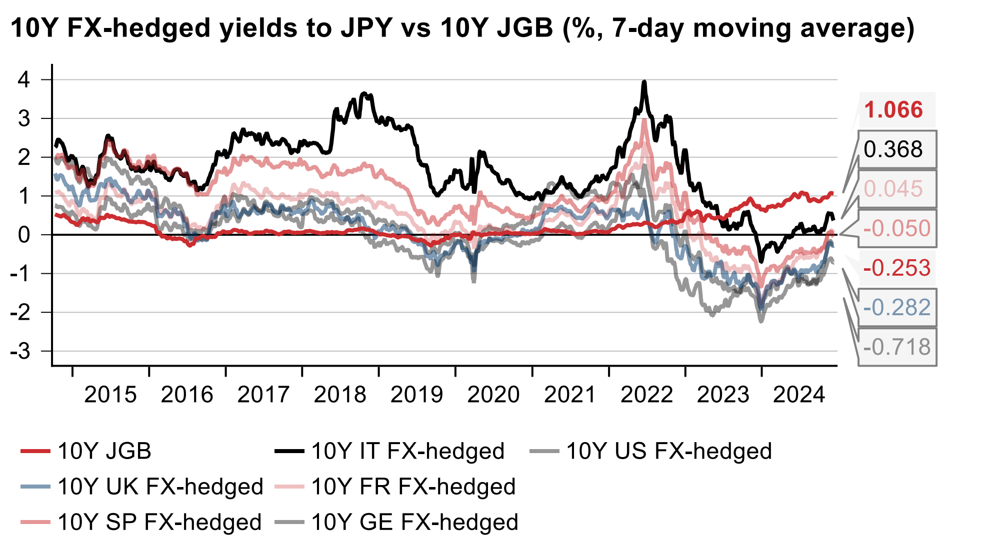
## Fair-value Bund spreads according to rating bucket



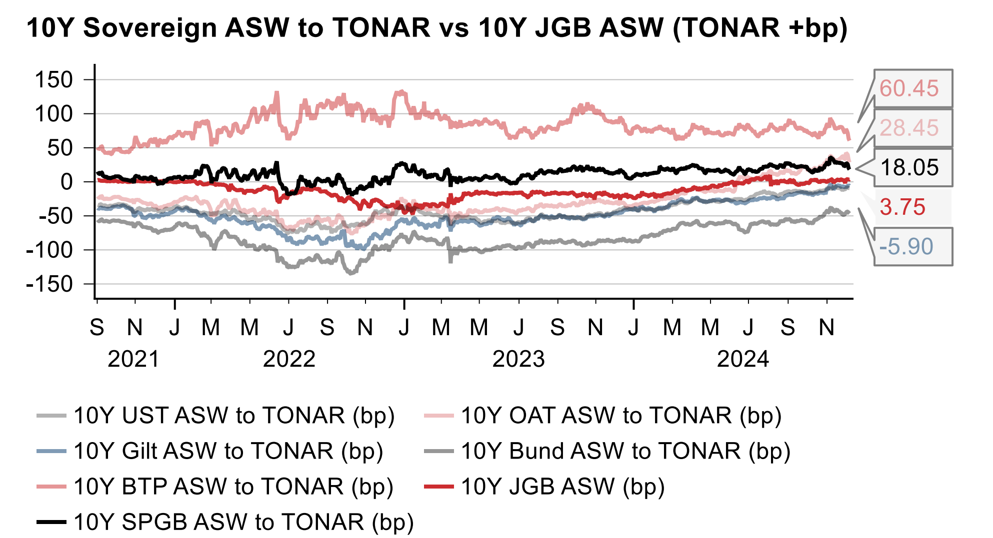

## Ratings snapshot




## FX-hedges are not attractive for JP investors (only IT)




## Peripherals provide a good pick-up to JP investors



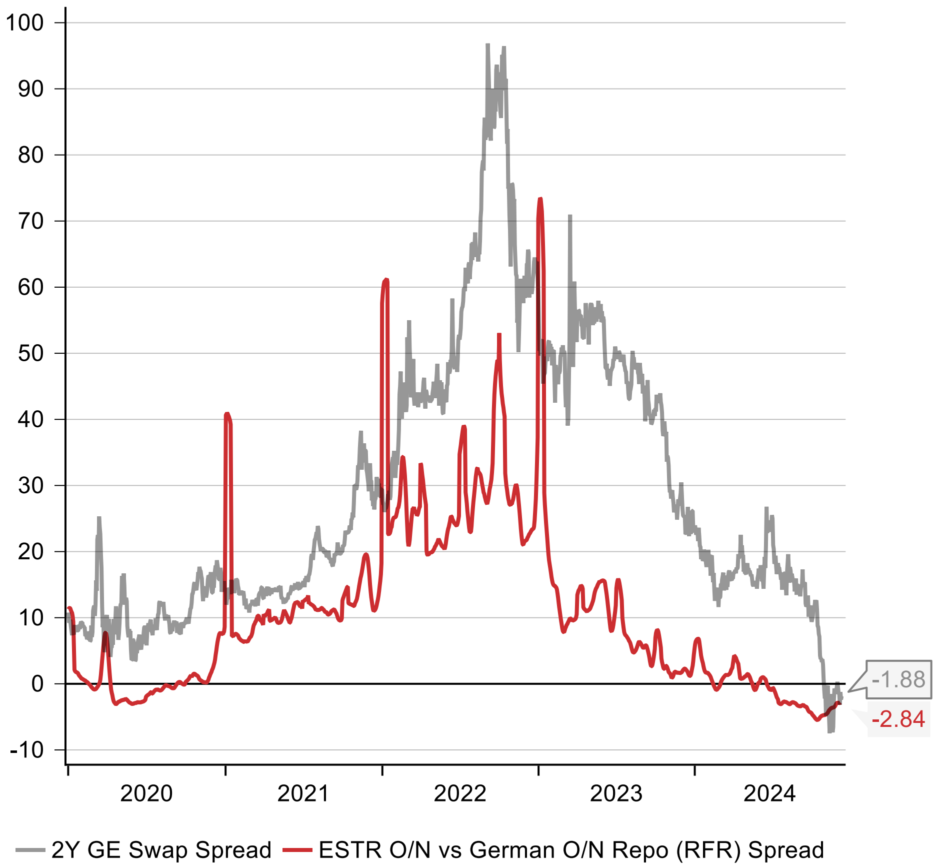

MIZUHO *Source: Macrobond, Bloomberg*

# Swap spreads

- **A regime shift to collateral abundancy and positive German net supply has driven a tightening of EUR swap spreads.**
- **We don't envisage a large widening unless EUR rates vol picks up notably and paying hedges are put on.**

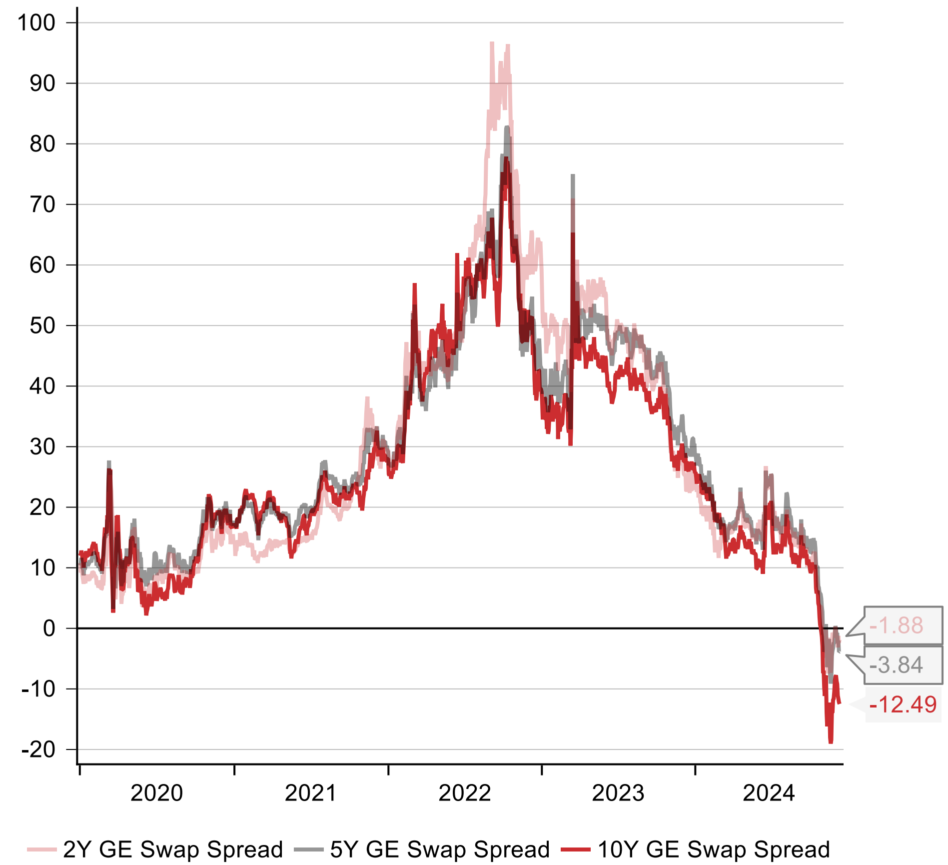
## Bund specialness: a thing of the past

**Bund specialness (in repo) proxy**




## The front-end drives the directionality in other tenors

**German ASW structure (bp, vs ESTR)**




*Source: Macrobond, Bloomberg*

# The 2025 outlook - UK

# The UK Macro background

- **Growth:** UK growth has held up but at low levels (<1% GDP). Data continues to miss, including the last PMIs and retail sales. The positive fiscal impulse from the recent budget is unlikely to hit growth next year as forecasted by the OBR thanks to NI tax hike impact on employment and the investment rules likely to slow its rollout. Instead the UK is likely to be dragged lower by European and Chinese growth concerns.

- **Inflation:** CPI at 2.3% but services at 5.0%. The BOE expects relatively stable services CPI in the next two quarters around 5.0% and headline to rise. Core inflation needs more time to stabilise. On headline, PPI signals a path below 2% in headline CPI ahead.

- **Unemployment:** Unemployment slowly climbing at 4.3% and private sector wages slowing in recent months but no sign of the slowdown triggering a more dovish BOE who are still concerned about "inflation persistence" and "sticky wages" (we don't share that concern).

- **BOE:** Small chance of a Dec cut (depends on next CPI release). **Terminal rate at 3.25%** in Q3 2025.

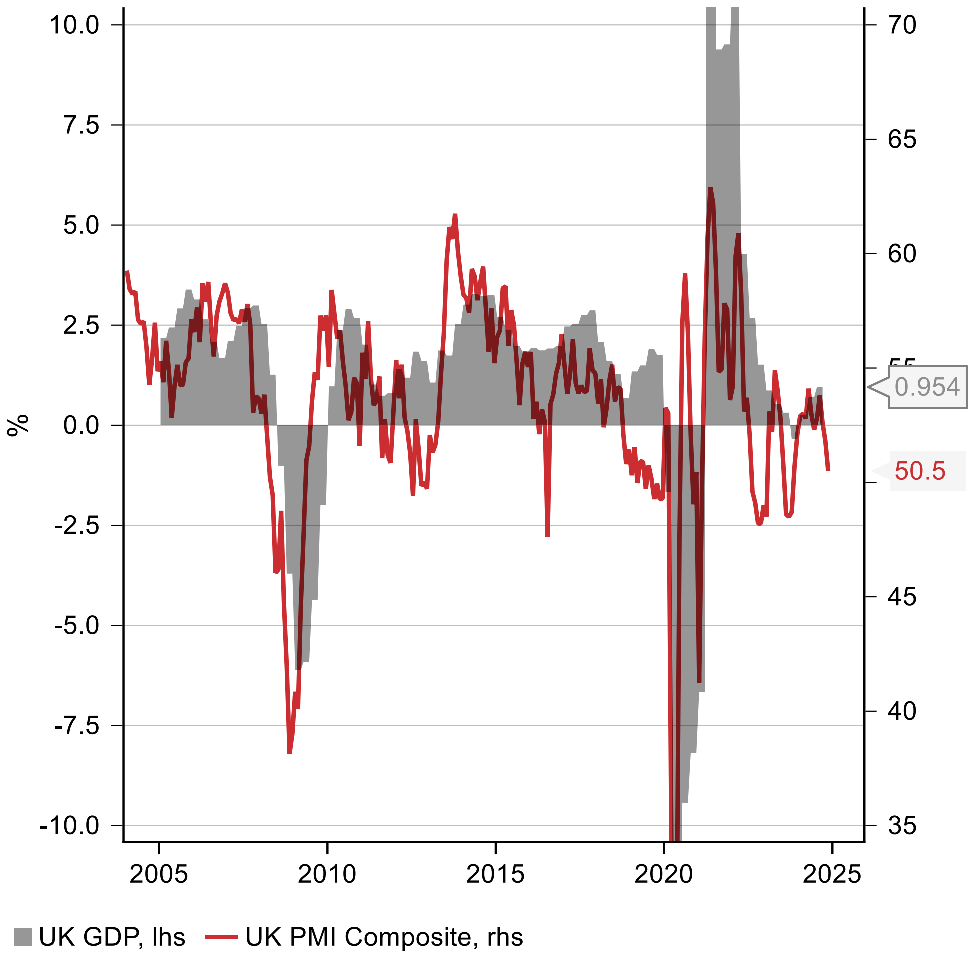
- **GBP/USD:** **1.23 in Dec, 1.21 in Jan**. With **a recovery to 1.30 by end 2025.**

- **Rates:** 10Y Gilt yields to **stay around 4.35% into year end and move towards 4.10% in 2025** as markets price in a more dovish BOE and a lower terminal rate.

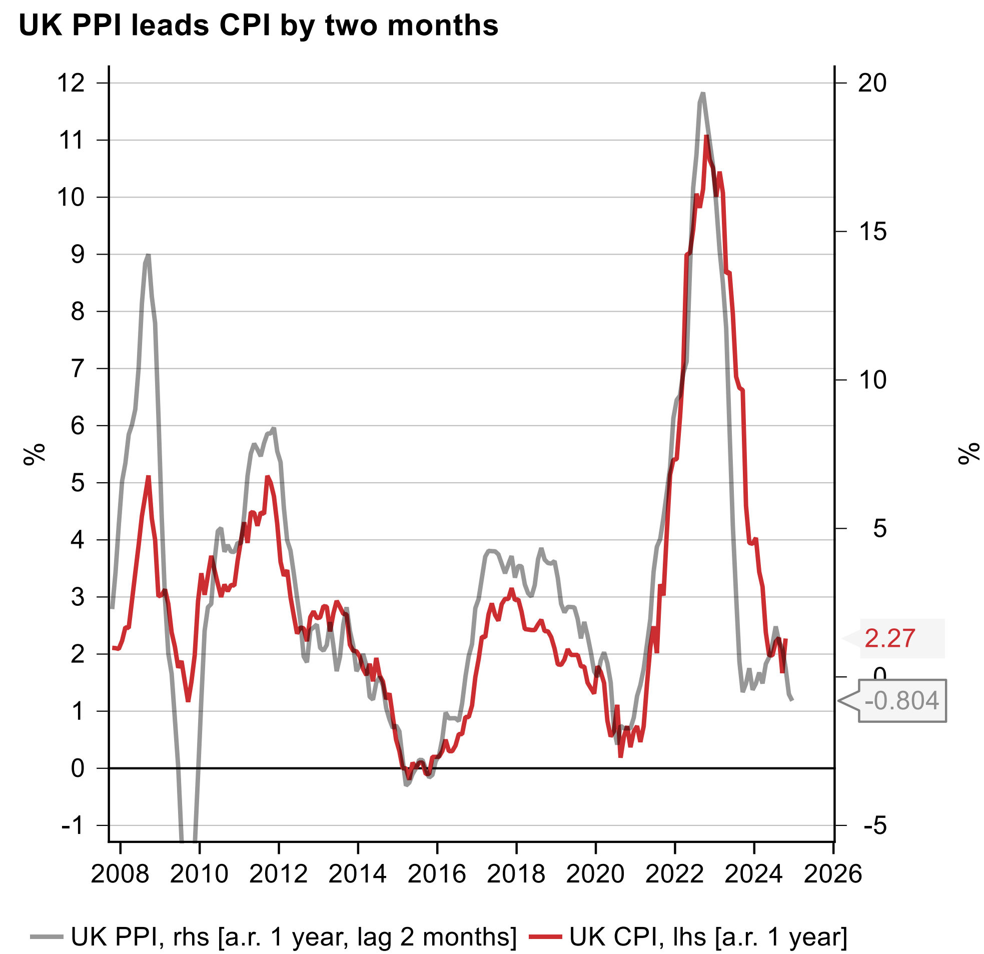
# Growth and inflation

- **Most of recent UK GDP growth is inventories and government. Last PMIs were soft.**
- **Core remains too high, but this type of inflation needs more time to stabilise.**

## UK PMI vs GDP



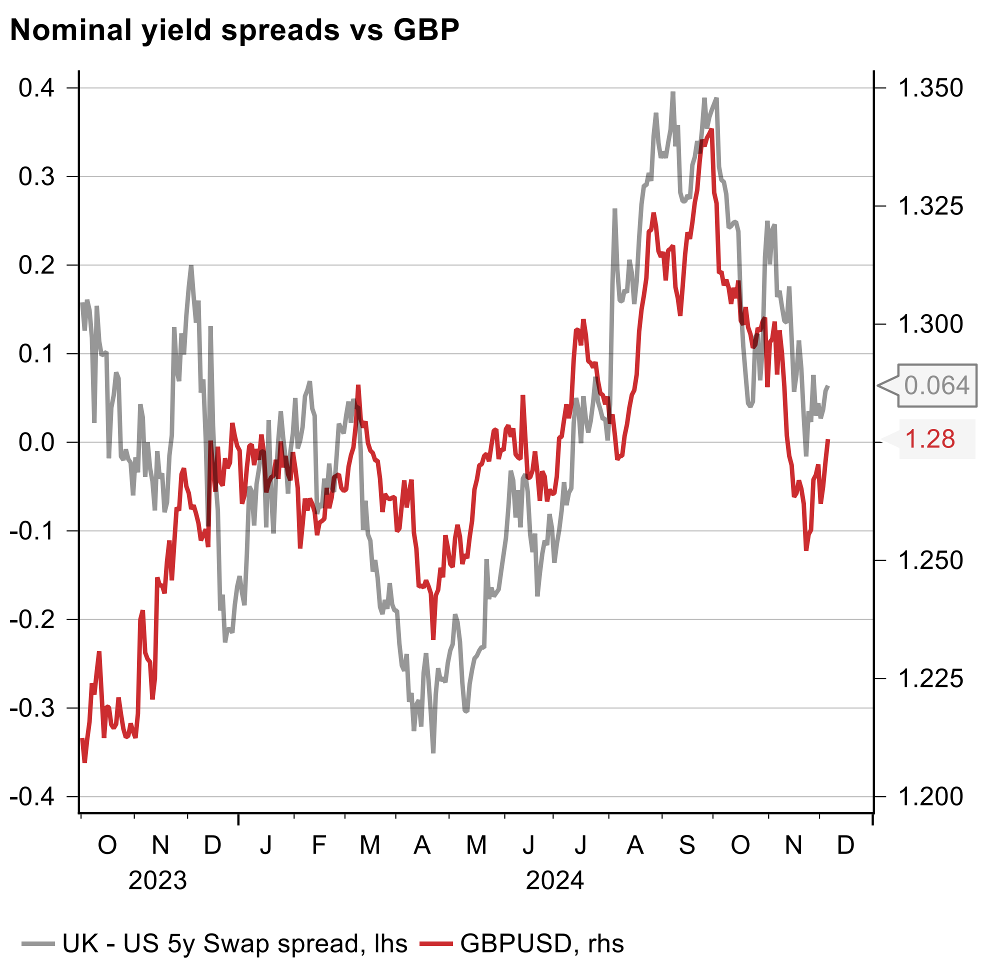

## The UK's inflation problem is over estimated



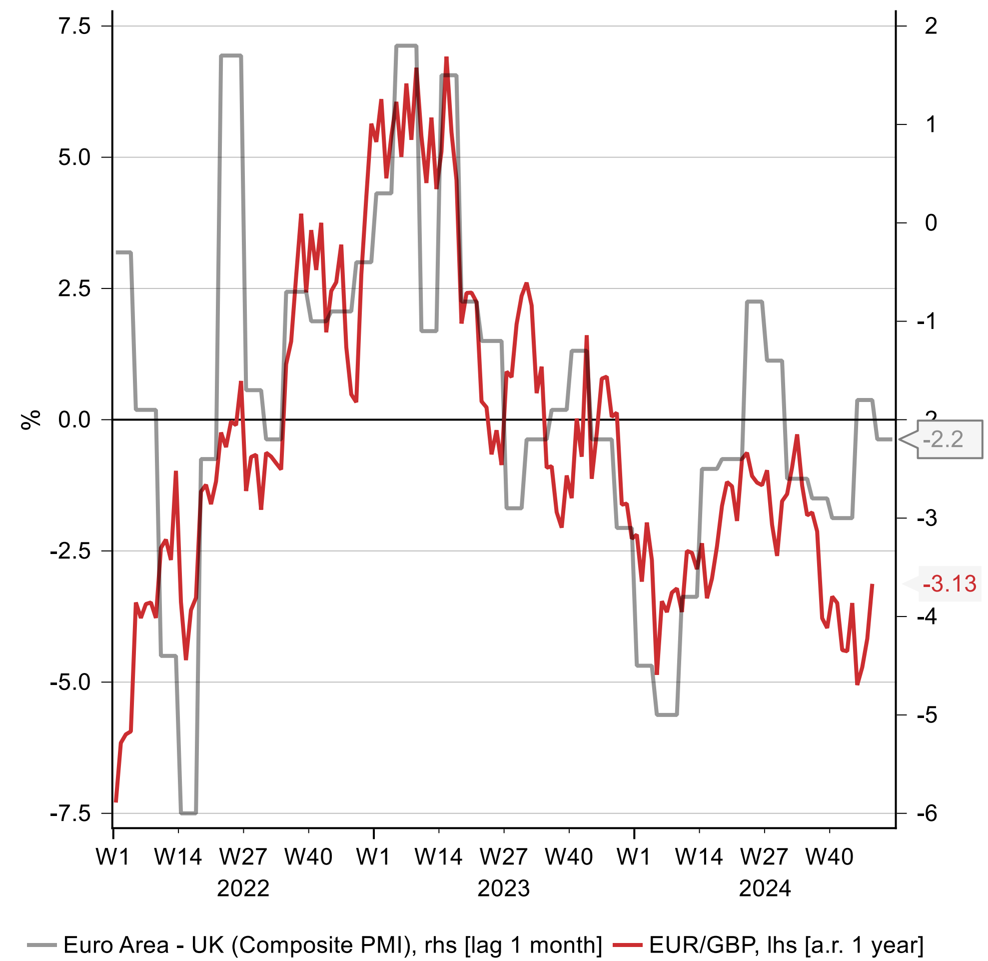
# GBP FX

- **GBP looks cheap vs rates**
- **But expensive vs growth differentials**

## GBP/USD vs 5yr swap spreads



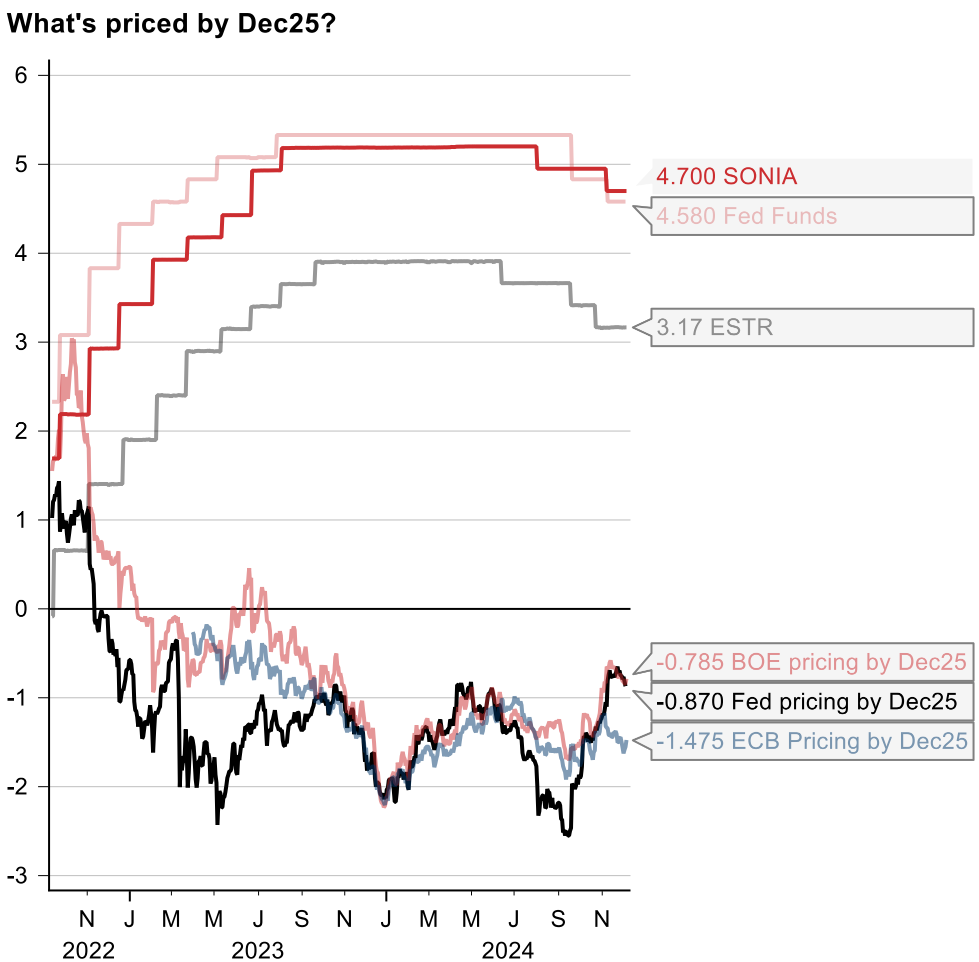

## EUR/GBP (y/y%) vs growth differentials



## UK Rates (1)

- **Is the UK really just following the US in its cycle? Or will it end up looking more European?**
- **With CPI close to 2%, is the current level of rates pricing too high?**

### The UK remains very correlated to US front end rates




### SONIA 1y1y vs Headline CPI

# UK Rates (2)

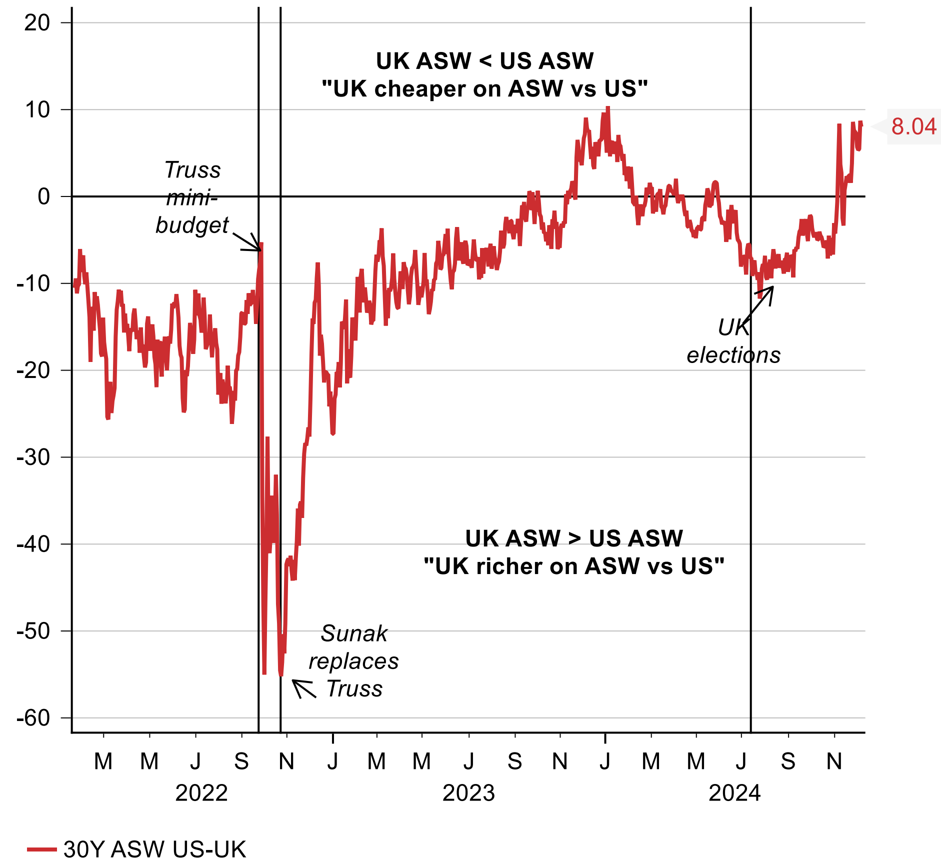
- **The spooky UK Budget and the upside in the last CPI mean that long GBP duration positions will have to wait. Similar story for the steepening of the curve.**
- **ASW remain depressed and there's no sign of turnaround. But 5s30s on ASW is starting to look attractive.**

## 5s30s likely to steepen on data misses

**Gilts 5s30s (bp)**


## The repricing of the UK credit is evident in the ASW space

**30Y ASW US-UK (ASW defined as Swap - Cash)**



# The 2025 outlook - Japan

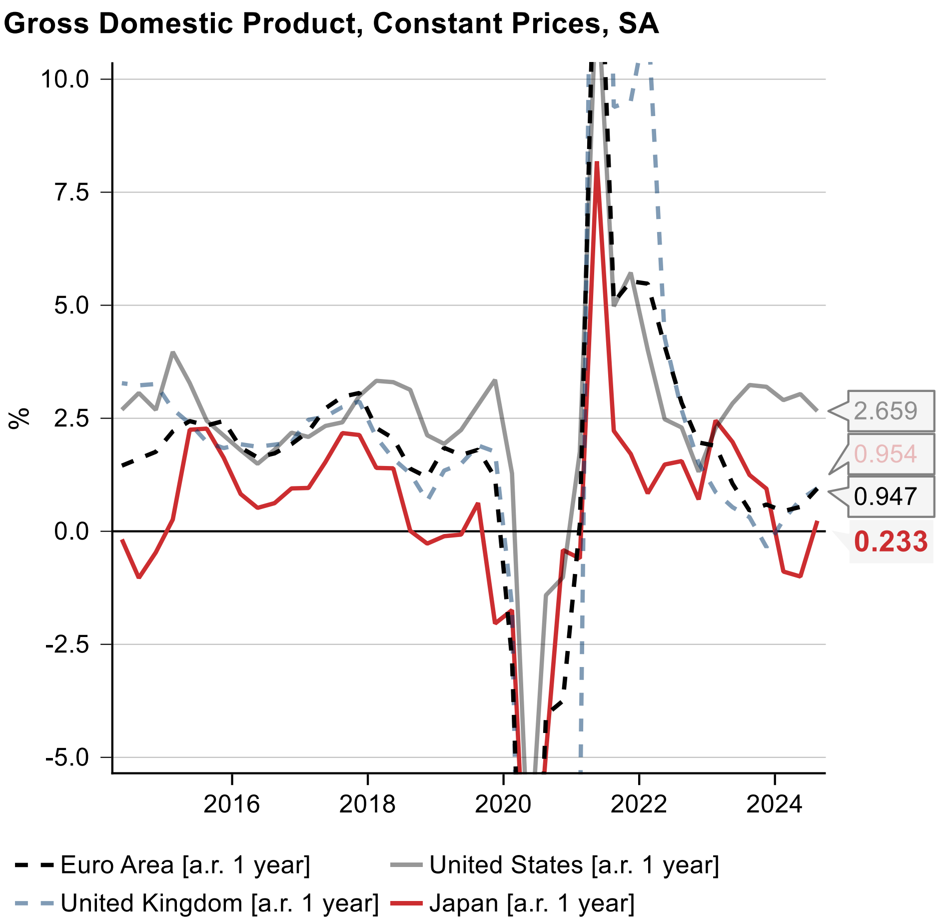
# The Japan Macro background

- **Growth:** Japanese economy will continue to expand slowly but steadily. Thanks to raising wages and government support include handout for low-income household and the resumption of subsidies to electricity and gas, consumption will be a main driver for growth. Capital investments will also support the growth, given that high profits and intensity for investment by Japanese corporation. External demand will be fragile against the background of Chinese sluggish demand and uncertainty around tax policy by US next government.
- **Inflation:** Headline CPI at 2.5%, core at 1.8%. But JPY strength since August could take up to 1% off headline CPI in the next three months with services also slowing if the relationship to FX holds.
- **Labour:** Full time workers' scheduled cash earnings (common office series), which the BOJ considers the most important wage indicator, hovers around 2.9%-3.0%. The 3% growth rate has long been the BOJ's benchmark for achieving a virtuous cycle between wages and prices.
- **Politics:** A minority government formed for the first time since 1994, which need support from the opposition parties especially the DPFP to pass the budget in the Parliament and avoid passing a no-confidence motion against the Cabinet. The policies the DPFP insists upon are deemed costly and inflationary.
- **BOJ:** We expect the next 25bps hike in January in a bi-annual hiking cycle, with a terminal rate of 1% in 2026. The fate of which is clearly tied to USD/JPY levels, the closer to 160 we trade the more likely a hike is to come.
- **USD/JPY:** USD/JPY at 157 (Dec-24), 154 (Dec-25) with the risk of 160 in Q1 if and when tariffs are announced.
- **Rates:** 1y1y continues to break higher at 0.78% (up since last month), at the low end of where we expect policy rates to be next year (0.75-1.00%). We expect to see a re-emergence of the upside pressure in JGB yields as wages continue to increase and the BoJ leans hawkish as USDJPY rises (if and when tariffs are levied). We expect this repricing to continue into the end of the year.

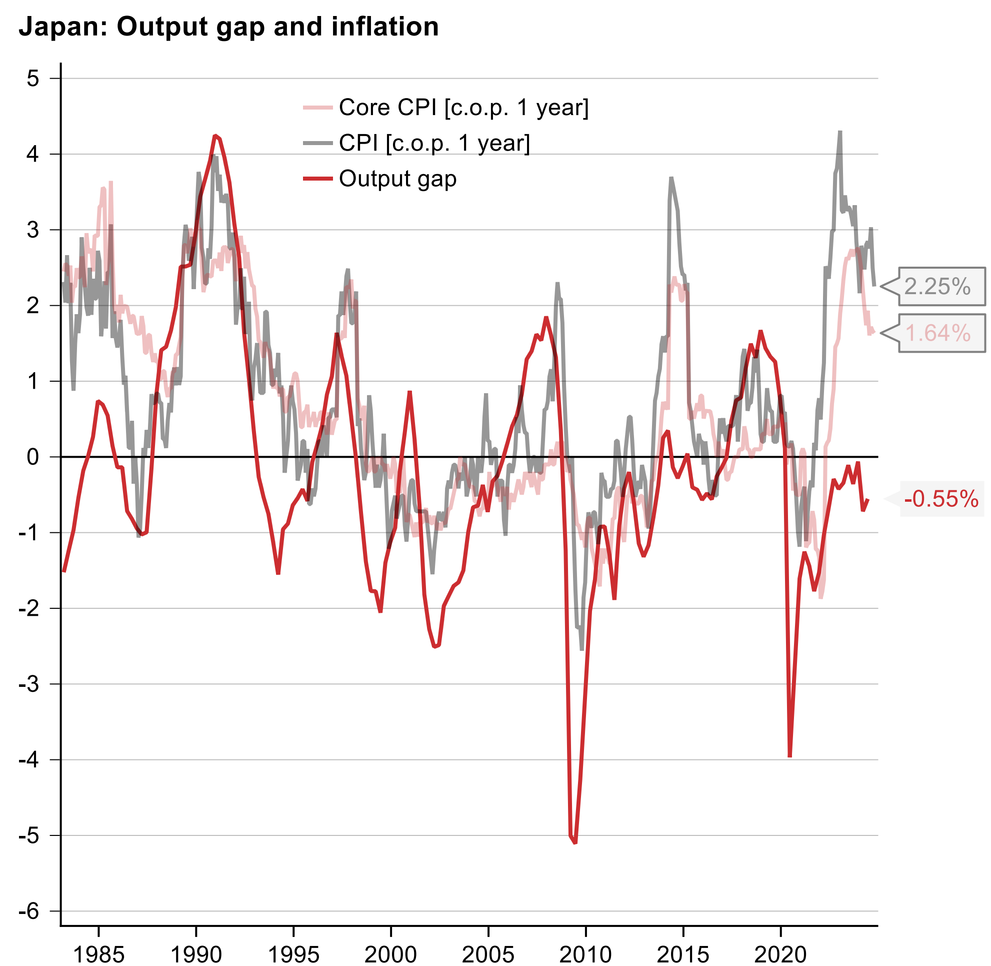
# Growth

- **The main issue for the BOJ is Japan has a negative output gap/low growth**

## Japan GDP vs peers




## Japan output gap






*Source: Macrobond, Bloomberg*

# Growth

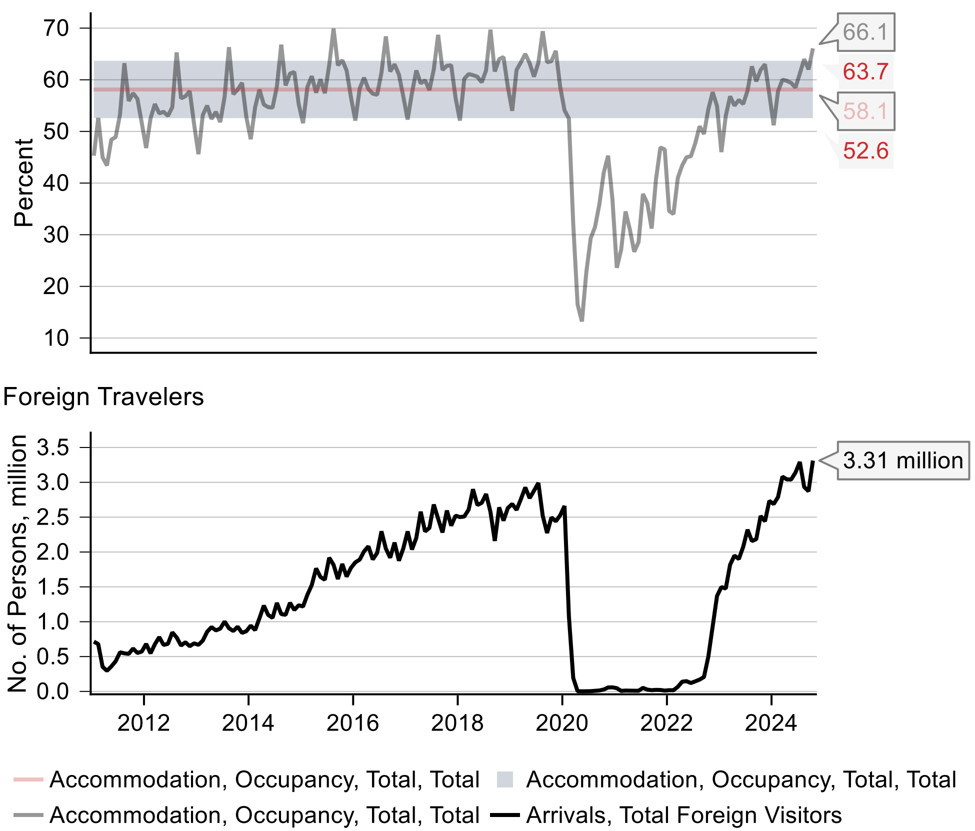
- **But Tourism in Japan is on fire, Services inflation is likely to be supported ahead**

## Japan tourism

**Japan tourism**

Source: MLIT, JNTO

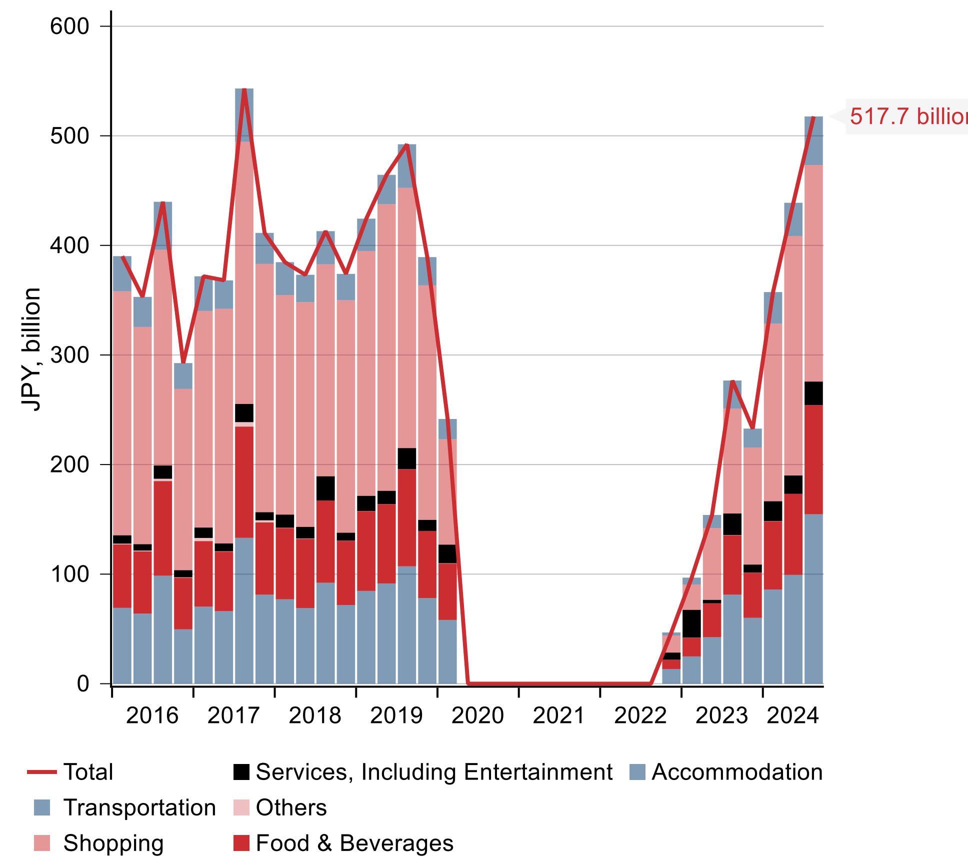
Accomodation occcupancy rate




## Japan tourism spending from China

**Japan: tourism spending per category, travelers from China**

Source: Japanese Ministry of Land, Infrastructure, Transport & Tourism

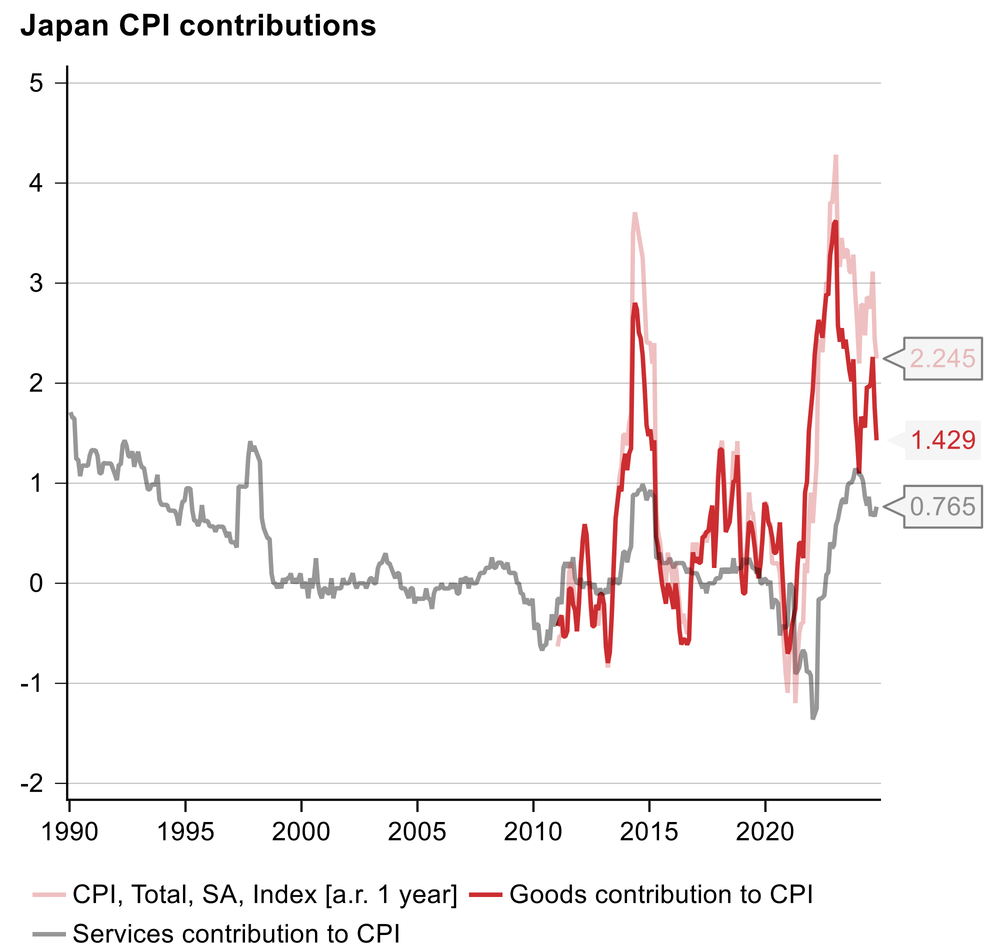



*Source: Macrobond, Bloomberg*

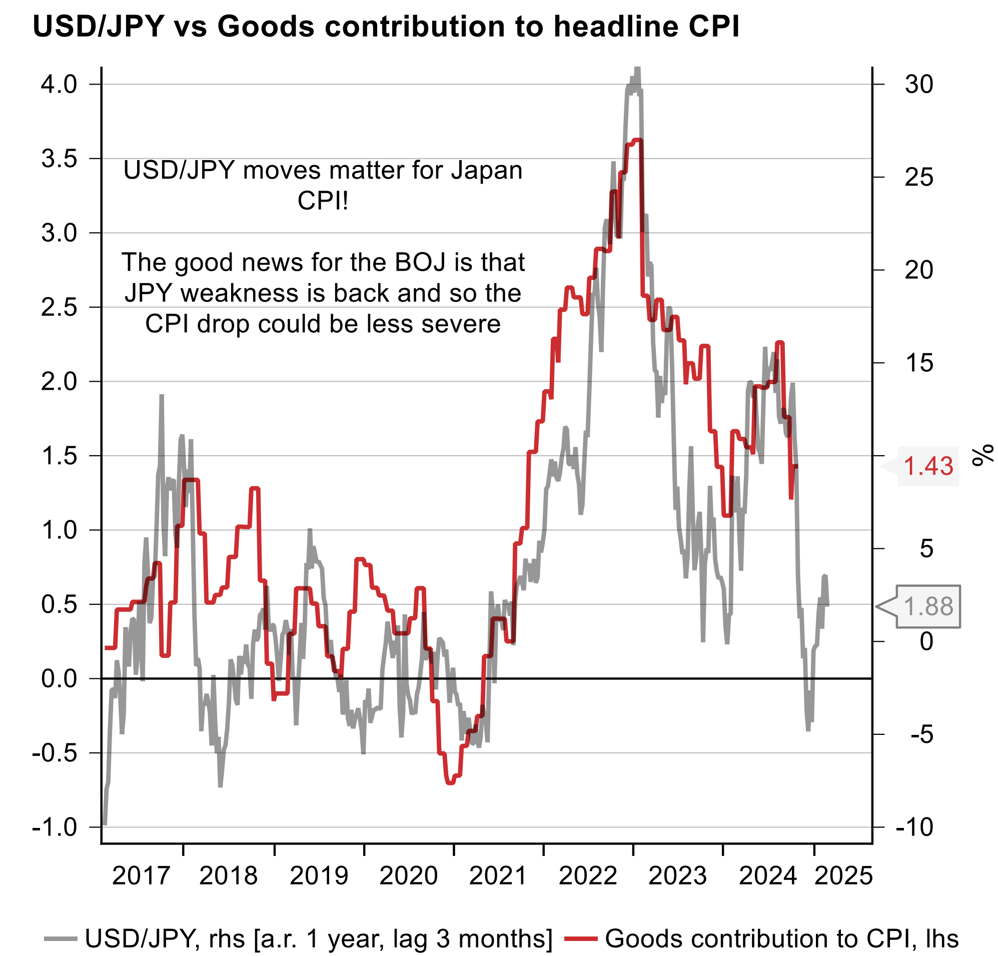
# Inflation

- **Japan's inflation is mostly driven by goods, which are very sensitive to the FX**
- **USD/JPY would suggest a big move lower in goods CPI**

## Japan CPI contributions



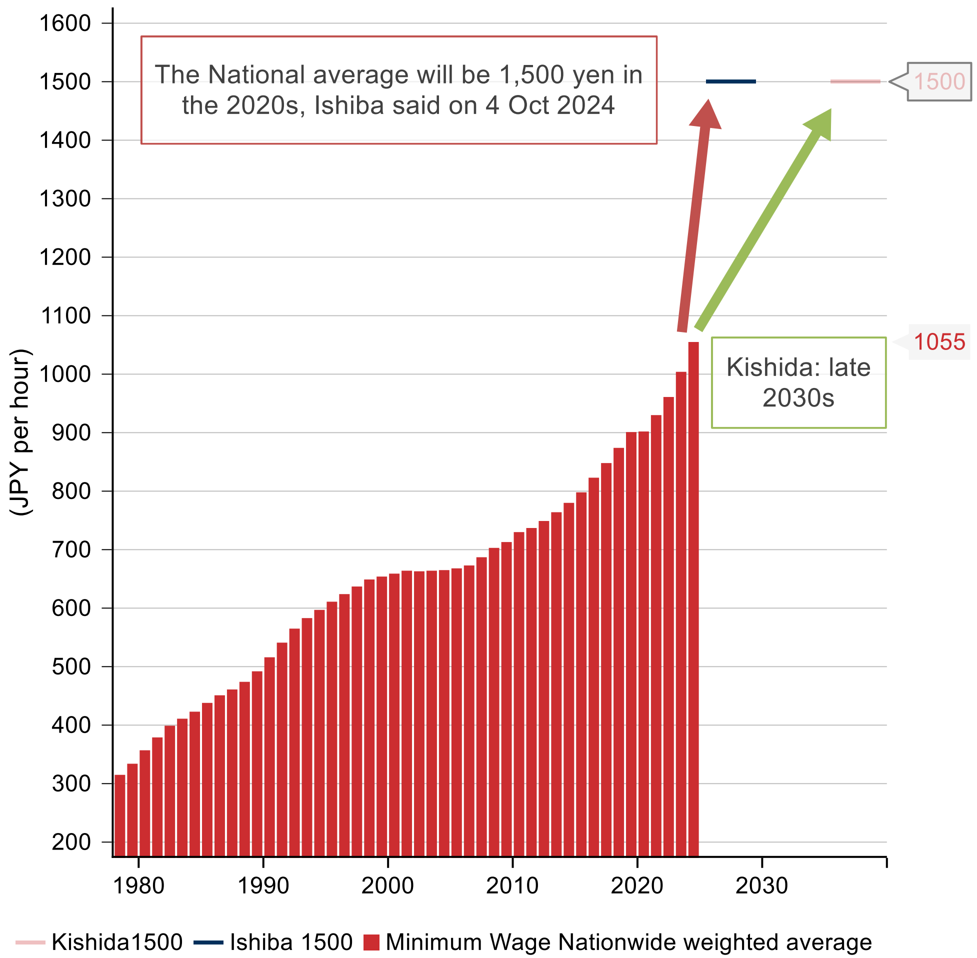

## USD/JPY does lead goods CPI in Japan by three months



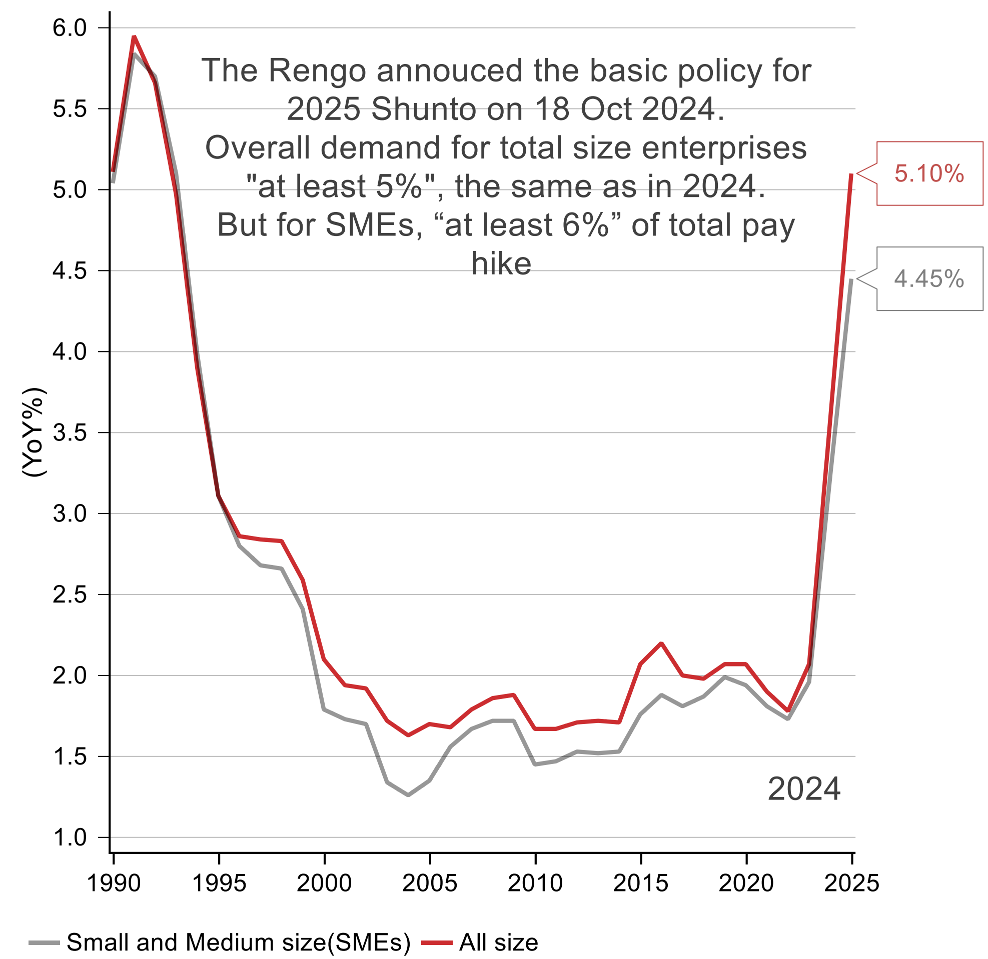
# Labour markets

- **Japanese Leaders are piling pressure on firms to raise wages**
- **At a rate not seen since the 1990s**

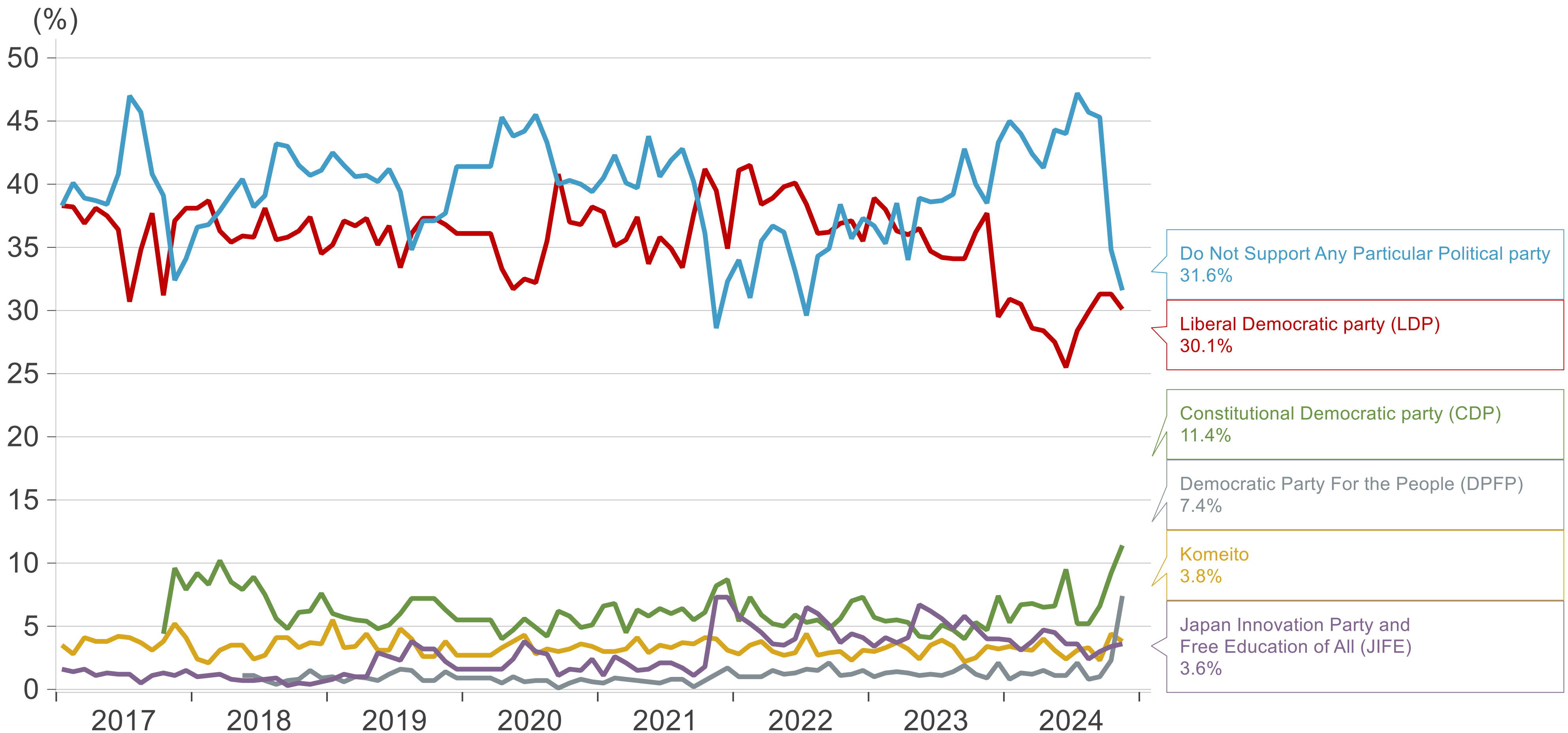
## Minimum wage Nationwide weighted average




## Results of Shunto (Total pay increases)



# Politics: LDP-Komeito coalition lost ground and must seek support from the opposition




Note: As of 01 November 2024
(Source: NHK, Macrobond, Mizuho)

# The Policy recommended by the DPFP is costly and inflationary

Chart 3. Major policies advocated by the DPFP

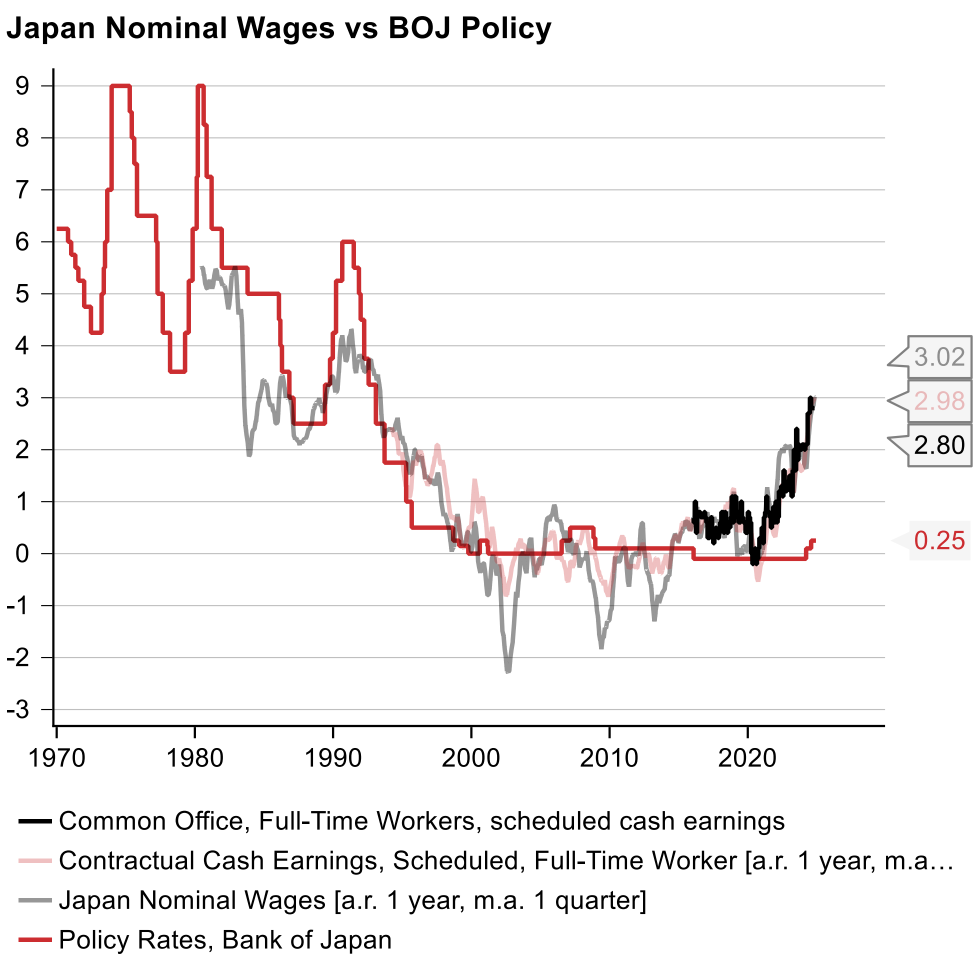
| | |
|---|---|
| "High-pressure economy" | Fiscal stimulus and monetary easing aimed at achieving +4% nominal wage growth (2% inflation + 2%) |
| Consumption tax cut | Consumption tax rate to be lowered from 10% to 5% (at a cost of around JPY11.5 trillion) until +4% nominal wage growth is achieved |
| Increase in "annual income barrier" | Combined total for income tax basic deduction and salary income deduction to be increased from JPY1.03 million (annual income) to JPY1.78 million (cost: JPY7.6 trillion/year) |
| Tax breaks for growth-sector investments | Promotion of investment in sectors including semiconductors, storage batteries, AI, and "Web 3.0" |
| Support for parenting and education | Increased childcare allowances and scholarships with income restrictions abolished |
| Free education | Free tuition through senior high school, free school meals and school trips |
| Doubling of the budget for education and science & technology | Annual issuance of around JPY5 trillion in "education bonds" |
| Unfreezing of gasoline tax trigger clause | Lower gasoline and light oil prices (cost: JPY1.5 trillion/year) |
| Reduced burden on today's workers | Increase in government's percentage contribution to the "Late-Stage Medical Care System for the Elderly", which currently accounts for around half of the social security premiums paid by workers |
| Nuclear energy policy | Reactors to be rebuilt and increased in number |
| Cryptocurrency tax cut | Cryptocurrency investments to be covered by the 20% "separate self-assessment taxation" system |

Source: Compiled by Mizuho Securities Fixed Income Research from DPFP policy pamphlet and various media reports

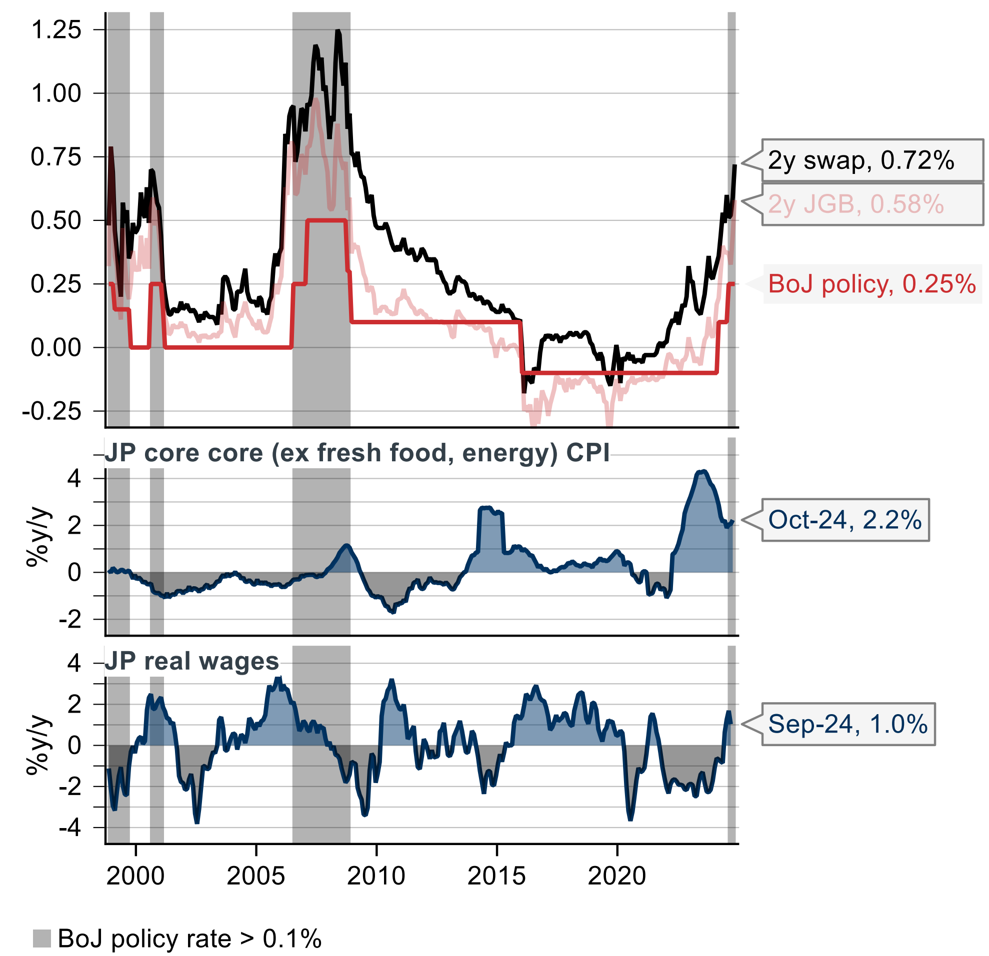
# BOJ

- **Japan has 1990s levels of wage growth but 00's levels of interest rates**
- **When BOJ policy was last 0.25%, 2yr swaps priced 0.75-1.00% vs 0.7% today**

## 1990s wage growth but 2007 policy




## BOJ policy vs CPI & real wages



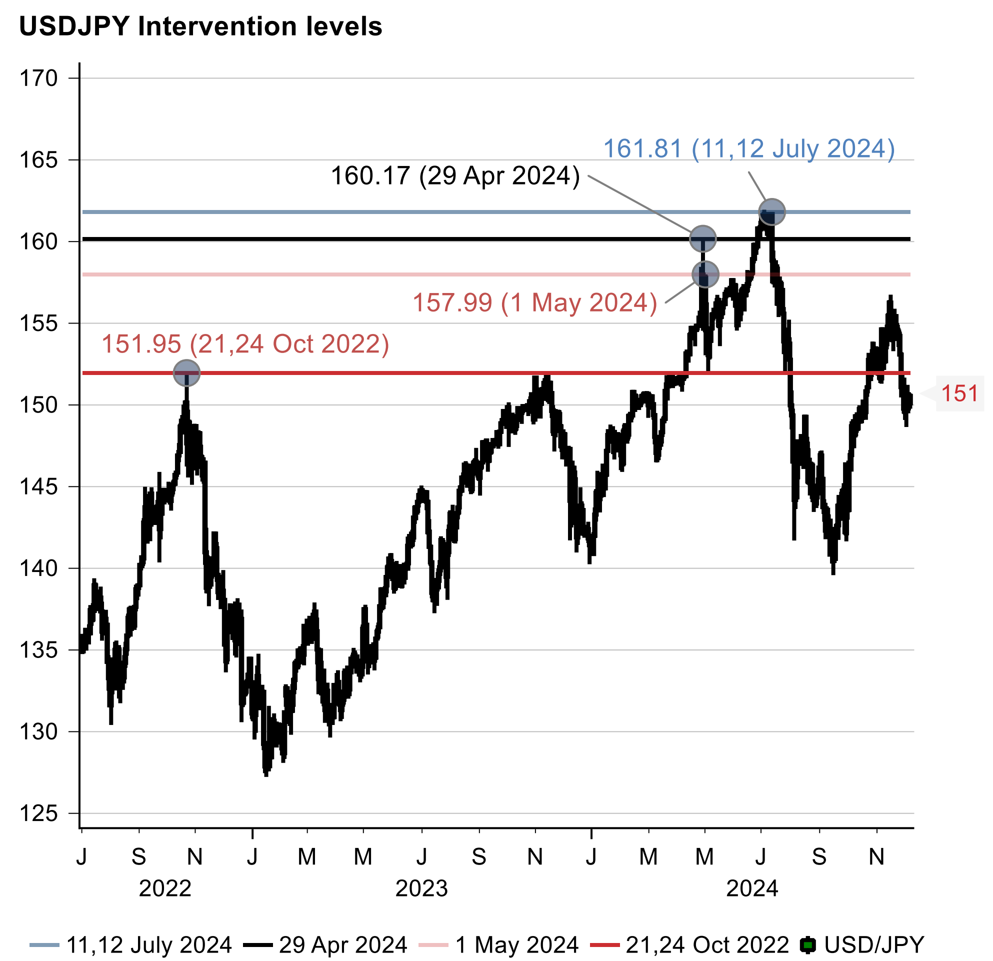



*Source: Macrobond, Bloomberg*

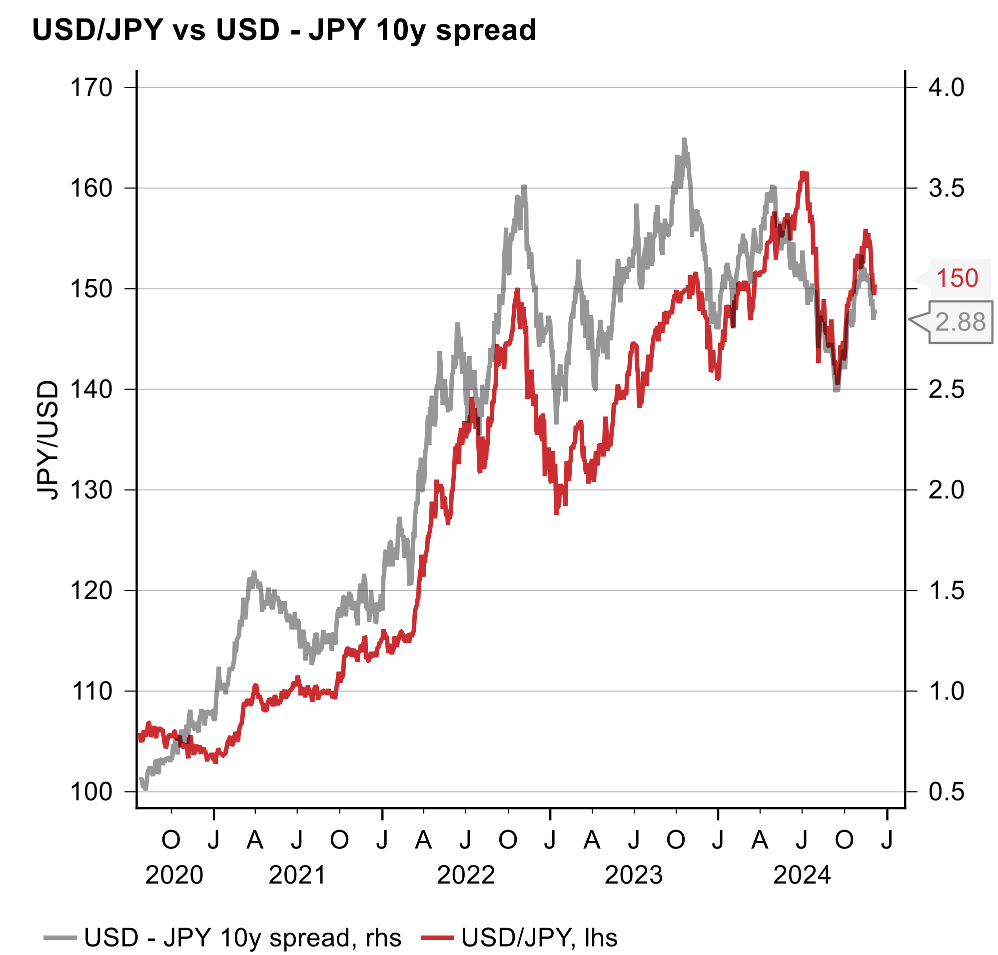
# JPY FX

- **At what level should we expect FX intervention?**
- **JPY remains very tied to long end rates spreads**

## USD/JPY intervention levels




## USD/JPY vs 10yr spread



## Rates

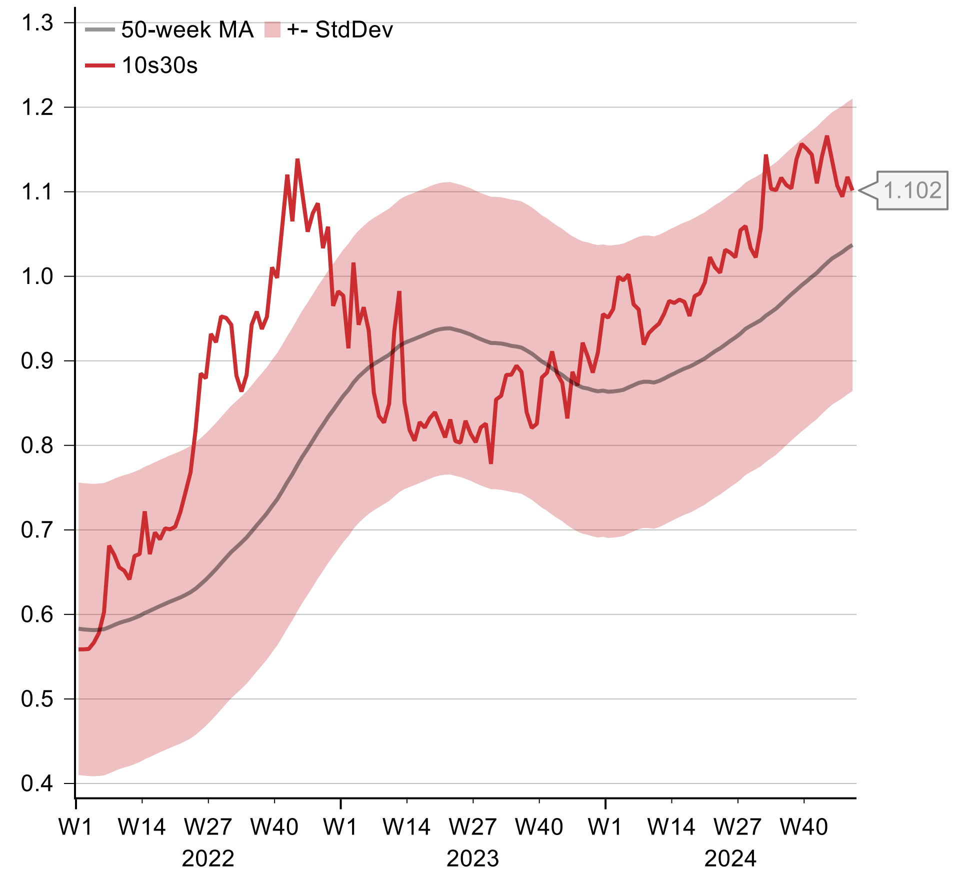
- **Ueda has left the door open to further hikes. December is possible, we think January is more likely.**
- **10s30s hasn't been able to steepen more. Some buying in 30Y JGB ASW lately. We like flatteners.**

### Keep paying front-end JPY swaps: towards 1%

**Markets are pricing too little for the BoJ (%)**


### Super long end may flatten if politics allow for it

**JGB 10s30s looks steep (bp)**




*Source: Macrobond, Bloomberg*

# Mizuho forecasts

# Mizuho FX, Policy and Rates Forecasts

| Policy rates | 02-Dec | Dec-24 | Mar-25 | Jun-25 | Sep-25 | Dec-25 | Δ 2025 |
|---|---|---|---|---|---|---|---|
| Fed (mid point) | 4.625 | 4.625 | 4.375 | 4.125 | 3.875 | 3.875 | -75bps |
| ECB (depo) | 3.25 | 3.00 | 2.50 | 2.00 | 1.50 | 1.50 | -175bps |
| BoE | 4.75 | 4.75 | 4.25 | 3.75 | 3.25 | 3.25 | -150bps |
| BoJ | 0.25 | 0.25 | 0.50 | 0.50 | 0.50 | 0.75 | 75bps |

| Rates | | 02-Dec | Dec-24 | Mar-25 | Jun-25 | Sep-25 | Dec-25 | Dec-26 |
|---|---|---|---|---|---|---|---|---|
| **USTs** | 2Y | 4.22 | 4.25 | 4.40 | 4.40 | 4.45 | 4.50 | 4.30 |
| | 5Y | 4.12 | 4.35 | 4.35 | 4.35 | 4.45 | 4.60 | 4.35 |
| | 10Y | 4.23 | 4.60 | 4.50 | 4.65 | 4.80 | 5.00 | 4.50 |
| | 30Y | 4.40 | 4.55 | 4.50 | 4.50 | 4.60 | 4.70 | 4.60 |
| **Germany** | 2Y | 1.91 | 2.05 | 1.70 | 1.50 | 1.65 | 1.70 | 2.15 |
| | 5Y | 1.88 | 2.15 | 1.75 | 1.51 | 1.55 | 1.64 | 2.10 |
| | 10Y | 2.05 | 2.25 | 1.85 | 1.75 | 1.95 | 2.05 | 2.25 |
| | 30Y | 2.28 | 2.40 | 2.20 | 2.19 | 2.25 | 2.40 | 2.60 |
| **UK Gilts** | 2Y | 4.24 | 4.22 | 4.00 | 3.80 | 3.85 | 4.00 | 3.65 |
| | 5Y | 4.10 | 4.15 | 3.90 | 3.70 | 3.80 | 3.90 | 3.70 |
| | 10Y | 4.25 | 4.35 | 4.25 | 4.10 | 4.15 | 4.30 | 4.25 |
| | 30Y | 4.77 | 4.85 | 4.75 | 4.70 | 4.80 | 5.00 | 4.90 |
| **JGBs** | 2Y | 0.61 | 0.50 | 0.55 | 0.60 | 0.80 | 1.15 | 0.85 |
| | 5Y | 0.74 | 0.70 | 0.70 | 0.70 | 0.90 | 1.20 | 0.95 |
| | 10Y | 1.07 | 1.15 | 1.10 | 1.20 | 1.45 | 1.65 | 1.40 |
| | 30Y | 2.28 | 2.25 | 2.15 | 2.20 | 2.40 | 2.45 | 2.35 |

| FX | 02-Dec | Dec-24 | Mar-25 | Jun-25 | Sep-25 | Dec-25 | Dec-26 |
|---|---|---|---|---|---|---|---|
| EUR/USD | 1.05 | 1.03 | 1.01 | 1.03 | 1.04 | 1.05 | 1.10 |
| USD/JPY | 150 | 157 | 160 | 158 | 156 | 154 | 150 |
| GBP/USD | 1.26 | 1.23 | 1.21 | 1.25 | 1.28 | 1.30 | 1.32 |
| EUR/GBP | 0.83 | 0.84 | 0.84 | 0.82 | 0.82 | 0.81 | 0.83 |
| EUR/JPY | 157 | 162 | 162 | 163 | 162 | 162 | 165 |
| GBP/JPY | 190 | 193 | 193 | 198 | 199 | 199 | 198 |
| DXY | 107 | 109 | 111 | 109 | 108 | 107 | 102 |

| GDP & CPI by country | | 2023 | 2024 | 2025 |
|---|---|---|---|---|
| *GDP:* | *US* | 3.20 | 3.10 | 3.00 |
| | *Euro Area* | 0.50 | 0.70 | 1.30 |
| | *UK* | 0.10 | 0.90 | 1.80 |
| | *Japan* | 1.80 | -0.30 | 1.20 |
| *CPI:* | *US (PCE)* | 3.70 | 2.60 | 2.30 |
| | *Euro Area* | 5.40 | 2.40 | 2.10 |
| | *UK* | 7.40 | 2.70 | 2.00 |
| | *Japan (core-core)* | 3.90 | 1.90 | 1.60 |

**Fed policy forecast by Mizuho Securities US. Macro forecasts by Mizuho Research & Technologies, Ltd.*
*Forecasts for USD and USTs by Mizuho EMEA.*
*Differences reflect the EMEA strategy teams risk assessment on the markets pricing of the outlook.*

*Source: Macrobond, Bloomberg*

# Central Banks

| FED | Forecast: Mizuho Securities USA (MSUSA) (Steven Ricchiuto, Alex Pelle) | | Market pricing* (Fut, as of: 15:6 on 2/12) |
|---|---|---|---|
| Current rate (mid point) | 4.625% | Rates remain restrictive at these levels. | |
| 2024 Dec meeting | 4.625% | Skip Dec & Jan meetings. | 4.43% |
| 2025 Dec meeting | 3.875% | 25bps cuts: March, June, Sept to 4% terminal. | 3.83% |
| 2026 Dec meeting | 3.875% | Terminal rate reached by Sept 2025 | 3.70% |
| Peak | 5.375% | July 2023 - Sept 2024. | |
| Mizuho EMEA FICC Strategy view | *NFP rebound next month = "skip" in Dec or Jan? But risk data surprises to turn lower in Jan.* | | |
| Balance sheet reduction: QT (active and passive) | | | |
| 2025 | QT ending Oct 2025, risks skewed to earlier. | | |

| BoJ | Forecast: Mizuho EMEA (Jordan Rochester & Evelyne Gomez-Liechti) | | Market pricing* (Fut, as of: 15:6 on 2/12) |
|---|---|---|---|
| Current rate | 0.25% | Still on track toward neutral rate. | |
| 2024 Dec meeting | 0.25% | No more hikes this year, Jan more likely than Dec. | 0.41% |
| 2025 Dec meeting | 0.75% | A lot depends on USD/JPY, but every six months. | 0.75% |
| 2026 Dec meeting | 1.00% | If no global recession takes place. | 0.84% |
| Peak | 1.00% | Reaches terminal rate in mid-2026. | |
| Mizuho EMEA FICC Strategy view | *A 25bps hike in Jan still live with Dec less likely. But Politics and USD/JPY the key variable.* | | |
| Balance sheet - QE | | | |
| 2025 | JPY 3.3tn per month (YE). | | |
| 2026 | JPY 1.7tn per month (YE). | | |

| ECB | Forecast: Mizuho EMEA (Jordan Rochester & Evelyne Gomez-Liechti) | | Market pricing* (Fut, as of: 15:6 on 2/12) |
|---|---|---|---|
| Current rate (depo) | 3.25% | Rates remain restrictive at these levels. | |
| 2024 Dec meeting | 3.00% | 25bps cuts: Dec. | 2.82% |
| 2025 Dec meeting | 1.50% | 25bps cuts: Jan, Mar, Apr, Jun, July, Sep | 1.72% |
| 2026 Dec meeting | 1.50% | Terminal rate reached by Sep 2025 | 1.83% |
| Peak | 4.00% | Sep 2023 (end of hiking cycle) - June 2024 (start of cutting cycle). | |
| Mizuho EMEA FICC Strategy view | *ECB on a 25bps per meeting path, we expect a lower terminal rate than the market.* | | |
| Balance sheet - QT (active and passive) | | | |
| 2025<br>2026 | Passive QT with no APP or PEPP reinvestment. | | |

| BoE | Forecast: Mizuho EMEA (Jordan Rochester & Evelyne Gomez-Liechti) | | Market pricing* (Fut, as of: 11:27 on 6/12) |
|---|---|---|---|
| Current rate | 4.75% | Rates remain restrictive at these levels. | |
| 2024 Dec meeting | 4.75% | 25bps cuts: Skip Dec, but a closer call than priced | 4.63% |
| 2025 Dec meeting | 3.25% | 25bps cuts: Feb, March, May, June, Aug. | 3.94% |
| 2026 Dec meeting | 3.25% | Terminal rate reached by Aug 2025 | 3.79% |
| Peak | 5.25% | Aug 2023 (end of hiking cycle) - Aug 2024 (start of cutting cycle). | |
| Mizuho EMEA FICC Strategy view | *Bailey to be less hawkish than fiscal stimulus risks imply. Nov CPI to be weaker than expected.* | | |
| Balance sheet - QT (active and passive) | | | |
| Sept 2024 to 2025 | £100bn | In line with recent history and towards the BoE's Preferred Minimum Range of Reserves (PMRR). | |
| Sept 2025 to 2026 | £100bn | | |

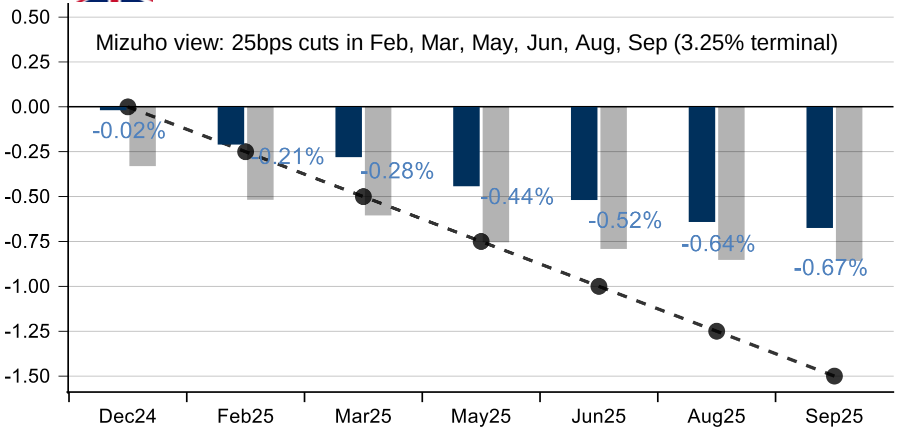
**EMEA (BoE and ECB)**
Jordan Rochester: Mizuho Bank Ltd (MHBK), Head of FICC Strategy
Evelyne Gomez-Liechti: Mizuho International Plc (MHI), Mizuho EMEA Multi-Asset Strategist
**Mizuho Americas (FED)** – ***sourced but not authors of this piece.***
Steven Ricchiuto: Mizuho Securities USA (MSUSA), US Chief Economist
Alex Pelle: Mizuho Securities USA (MSUSA), US Economist

Dominic Konstam: Mizuho Securities USA (MSUSA), Head of Macro Strategy
For more Mizuho Securities USA content, see the portal at RESP MIZR in the Bloomberg Terminal.

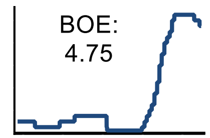
*Source: Macrobond, Bloomberg*

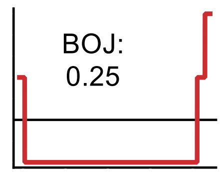
# What's priced in?

**BoE**

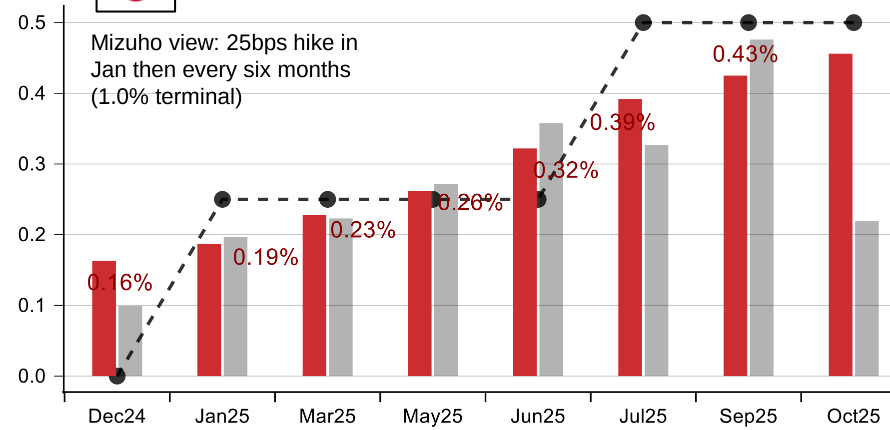



Change in BoE rate priced [Value at] Mizuho view [Value at]
One month ago [Value at -1m]



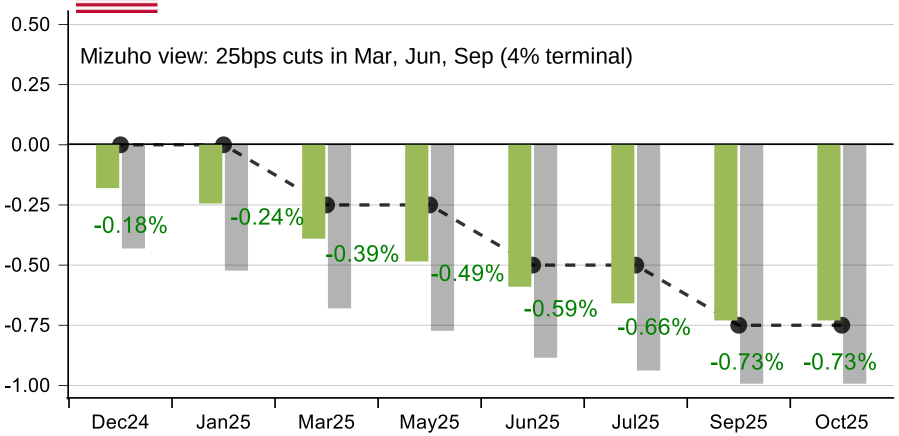




**BoJ**

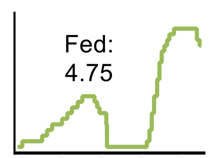


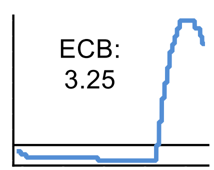

Change in BoJ rate priced [Value at] Mizuho View [Value at]
One month ago [Value at -1m]

**FED**

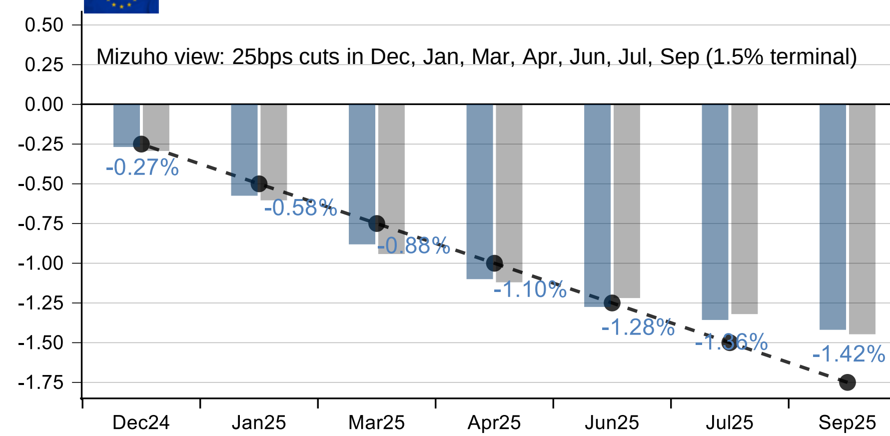



Change in FED rate priced [Value at] Mizuho View [Value at]
One month ago [Value at -1m]




**ECB**




Change in ECB rate priced [Value at] Mizuho View [Value at]
One month ago [Value at -1m]

# Cross Currency Basis

# XCCY Basis

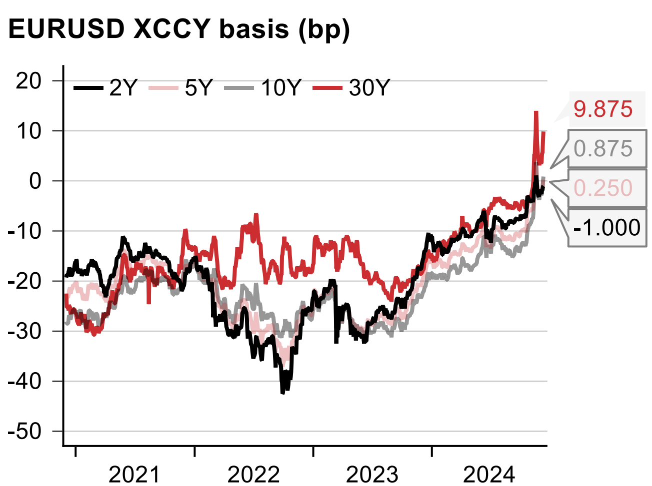
- **Dollar premium:** USD funding has been and continues to be cheap. Dollar liquidity remains relatively healthy despite some spikes in SOFR rates. The Fed doesn't seem concerned and is looking to keep QT in place for now. This will likely prevent an aggressive widening and a much higher dollar premium in the near and medium term. Short-term, we see risks of some wobbles around year end. Yankees remain attractive vs other currencies, which means 2025 may be another year of notable USD deals.

- **EURUSD:** Reverse EUR paper has been one of the key reasons why the basis has tightened another leg. Levels to issue in USD and even GBP are looking much more attractive than usual. EUR swap spreads have collapsed due to higher bond yields. This has also increased the cost of issuing in EUR. Additionally, European SSAs have been struggling to gather size in the EUR market, which suggests more reverse EUR issuance ahead (and in 2025). The paying momentum can continue. The only way we widen from here is either via a strong risk-off tone or USD liquidity becoming very scarce towards year end.

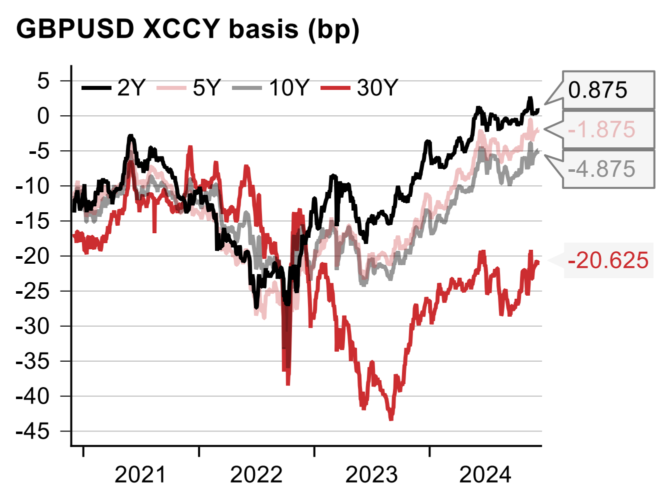
- **GBPUSD:** GBPUSD XCCY continues to exhibit a dislocation in the long end. This is the part of the curve that is more sensitive to large sell-offs in long-end Gilts. We think the curve (10s30s) will fail to normalise completely due to some new type of BPA (Bond Purchase Agreement) flow, attractiveness to issue in GBP (shout-out to EDF's 40Y GBP deal), and lack of strong appetite to buy GBP duration at the moment. The front end of the XCCY curve remains above parity and we expect it to remain around that area given the ongoing liquidity squeeze from the BoE. This will also make GBPUSD XCCY much more resilient to any future risk-off widening.

- **USDJPY:** There are several paying drivers currently at play that may print another leg to the tightening theme. Future BoJ hikes, subdued interest from Japanese investors to buy hedged overseas assets, and attractive levels in JGB ASW all support the paying momentum. Where we think the tightening momentum may fail to gather much more traction is in the very short-end. Scarcer USD liquidity may cause some knee-jerk widening in the very short-end.

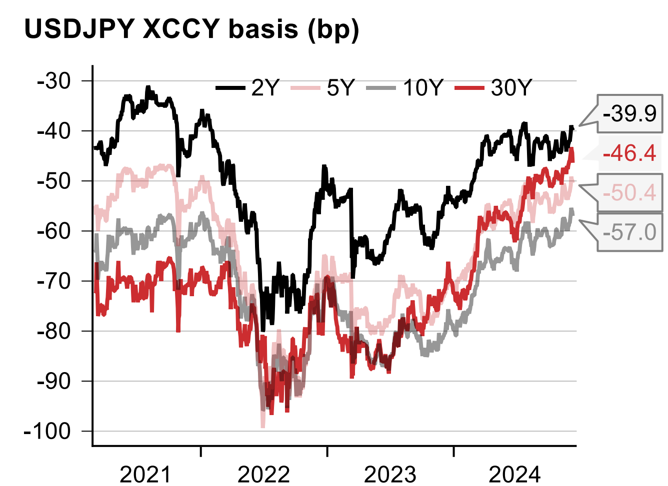
## EURUSD: paying flow can continue




## GBPUSD long-end unlikely to catch-up




## Paying drivers still at play in USDJPY



# Swap spreads

# Swap Spreads

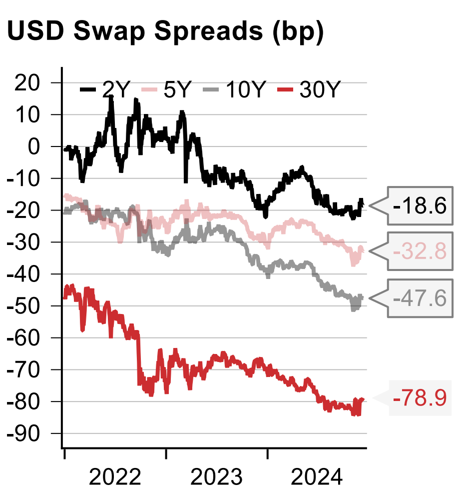
- **USD:** UST supply will continue to be elevated, which together with no QT end in sight and the natural receiving interest from real-money investors in rate cutting cycles should all continue to pressure swap spreads wider (more negative). 10Y+ area is the most vulnerable to tighten (bonds underperforming swaps). Debt sustainability concern will also keep the pressure on spreads. We would use any widening (bonds outperfoming swaps) to go short spreads.

- **EUR:** Collateral abundance and positive net supply have been behind the latest tightening in EUR swap spreads. We don't see any change in themes into year end. Front-end spreads should start to find a floor while the rest of the curve adjusts to tighter front-end spreads. Swap outperformance may prevail in the medium term, particularly if the new German government suspends the debt brake. In 2025, we see higher chances of widening as Bunds rally below 2.0%.

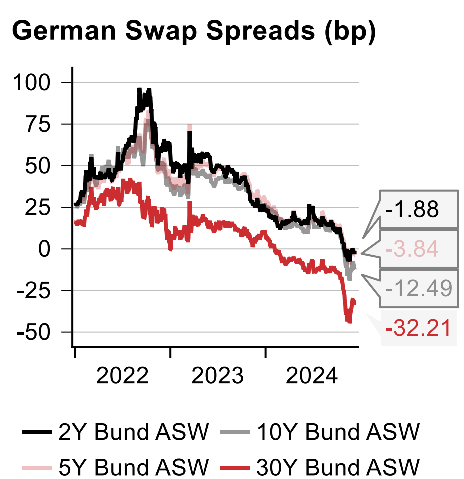
- **GBP:** Swap spreads remain depressed and the UK budget has driven another leg of the move. Gilts are now cheaper on ASW vs USTs. This is mostly a demand-supply mismatch (record levels of Gilt issuance!) and a lack of love towards the UK credit. Looking ahead, if the rate cut repricing that we expect materialises, we should see Gilts outperforming swaps as real investors should feel more confident in buying Gilts, which would help swap spreads find a floor.

- **JPY:** Worries about larger issuance have pressured swap spreads lower, but markets have failed to print new lows. We think we have seen the lows in swap spreads and with the new BoJ's purchase reduction, we think swap spreads will continue to tighten gradually, especially in the belly part of the curve. The super long-end space is seeing sporadic buying, which is driving has driven swap spreads tighter.

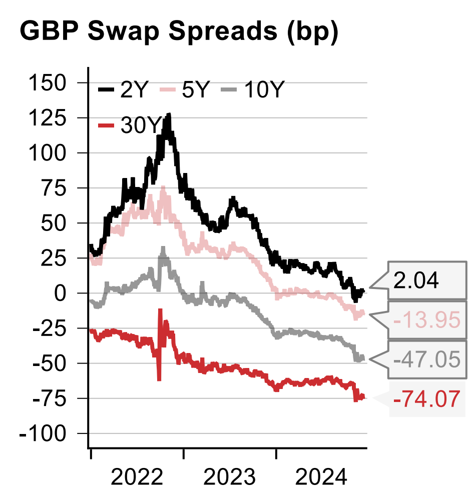
## USD: unlikely to rebound



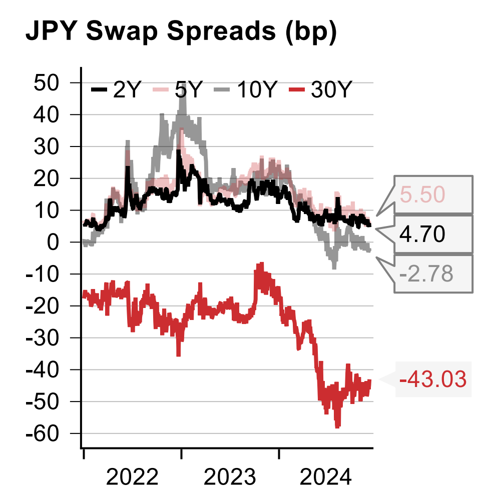

## EUR: swaps likely to outperform




## GBP: tightening due in 2025




## JPY: bouncing back gradually



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