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Forex Medium-Term Outlook

November 2, 2026

Overview of Outlook

USD/JPY lacked clear direction in October. The financial markets' focus has clearly shifted from Japan to France, and the target for currency selling in forex markets has also shifted from JPY to EUR. In other words, JPY has appreciated not because of its own strengths, but because of another currency's weakness, which is a stroke of good fortune for the Japanese government and the BOJ in their efforts to shore up the currency. Meanwhile, there has been no major change in the fundamental JPY trend, so another way to look at it may be that the currency is trapped in a high range of 155-160 against the dollar despite EUR's weakness. Going by IMM futures trading and other data, speculators seem to be swinging toward JPY buying. So, if JPY has failed to appreciate despite the combination of across-the-board EUR weakness and speculative JPY buying, it seems prudent to assume that it is likely to weaken further going forward. In addition to all this, there remain major concerns regarding the 2027 supply-demand climate for JPY. Assuming present economic and financial conditions to continue, with USD/JPY in the 150-160 range and crude prices at around USD 90-100 per barrel, Japan's trade deficit seems quite likely to settle somewhere between JPY 7-12 trillion. Going by past experience, it is difficult to forecast JPY appreciation assuming a trade deficit of this size. The only scenario in which JPY may appreciate is the collapse of the AI-driven market and the subsequent crash in U.S. interest rates. Such a development is quite possible if the Fed makes a sudden dovish pivot in the face of vulnerabilities, such as those even the IMF is warning about, becoming apparent.

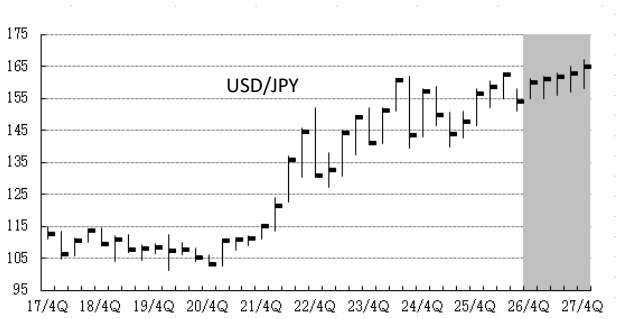
EUR declined sharply in October. The turmoil in French bond markets fueled by the political and economic situation in the country show no signs of abating. Ahead of the French presidential election in spring 2027, the Macron administration has become a lame duck, but skepticism regarding Marine Le Pen, widely seen as his successor, is also unlikely to dissipate easily. For now, with any fundamental fiscal consolidation being put off for until after the election, concerns about the potential erosion of fiscal discipline and the possibility of France's sovereign bonds gradually being downgraded by credit rating agencies will continue to smolder in the bond and forex markets, and this could invite a combination of EUR depreciation and a rise in regional interest rates. When viewed from this lens, it appears inevitable that the ongoing turmoil will continue until after the presidential election. Of course, the bond markets can be stabilized if the ECB were to intervene decisively, but as indicated at the October Governing Council meeting, such a development would be difficult unless the French government showed genuine commitment to fiscal reform. While EUR-denominated assets are the target of sell offs in the financial markets as a whole, there is a break in the trend of JPY depreciation and rising U.S.-Japan interest-rate differentials, with the situation in France currently determining financial market trends in the U.S., Japan, and Europe. As a result, while the Fed and the BOJ take a break from raising interest rates, the ECB will have to continue doing so, but the euro area's economic and financial situations are expected to remain lackluster.

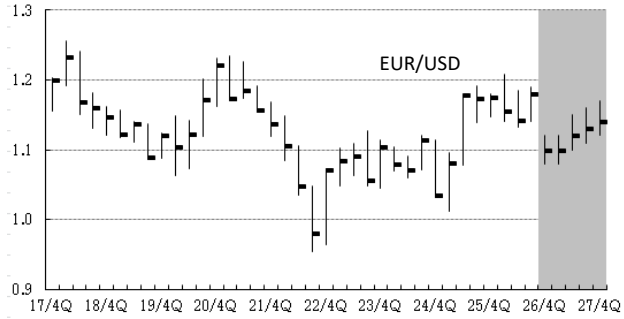
Summary Table of Forecasts

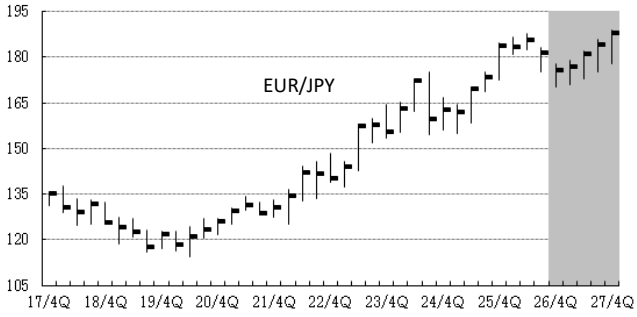
	2026 Jan-Oct (Actual)	Nov-Dec	2027 Jan-Mar	Apr-Jun	Jul-Sep	Oct-Dec
USD/JPY	152.10 ～ 163.99 (157.79)	155 ～ 161 (160)	155 ～ 162 (161)	156 ～ 163 (162)	157 ～ 165 (163)	158 ～ 167 (165)
EUR/USD	1.1105 ～ 1.2084 (1.1167)	1.08 ～ 1.12 (1.10)	1.08 ～ 1.12 (1.10)	1.10 ～ 1.15 (1.12)	1.11 ～ 1.16 (1.13)	1.12 ～ 1.17 (1.14)
EUR/JPY	175.09 ～ 187.95 (176.22)	170 ～ 178 (176)	171 ～ 179 (177)	173 ～ 182 (181)	175 ～ 186 (184)	178 ～ 189 (188)

(Notes) 1. Actual results released around 10 am TKY time on 30 Oct 2026. 2. Source by Bloomberg
3. Forecasts in parentheses are quarter-end levels.

Exchange Rate Trends & Forecasts







USD/JPY Outlook - 2027 JPY Supply-Demand Climate is the Real Concern

JPY Now and Going Forward –One Year into the Takaichi Administration

An Overview of the Past Year

It has been a year since the launch of the Sanae Takaichi administration on October 21, 2025. Of course, the financial market rate movement trend dubbed "Takaichi rates" began on October 4, the day Takaichi was elected president of the Liberal Democratic Party (LDP). The chart to the right shows how various indicators have changed over the past year, starting from before the LDP presidential election. Right from the beginning, many were concerned that expansionary fiscal and monetary policies under the Takaichi administration would result in a combination of JPY depreciation and higher interest rates for the Japanese economy, and things have, in fact, unfolded in line with such projections.

Economic, Financial, and Commodity Market Trends Over Past Year

Indicator	Oct 3, 2025	Oct 2, 2026	Change
Nikkei Stock Average	45769.5	68309.46	≈+50% increase
USD/JPY	147.44	157.84	≈+7% increase
10-Year JGB yield	1.662	3.093	≈+140bps increase
Consumer Price Index (CPI *1)	+3.0% yoy	+2.3% yoy	Remains above 2%
WTI crude oil future price (per barrel)	64.53	102.25	≈+60% increase
U.S.-Japan 10-Year Yield Gap (Nominal)	245bps	218bps	≈27bps narrowing
U.S.-Japan 10-Year Yield Gap (Real, *2)	243ps	29bps	≈214bps narrowing
Trade balance (cumulative for Jan-Sep)	-JPY 2.81 trillion	-JPY 3.316 trillion	Roughly flat

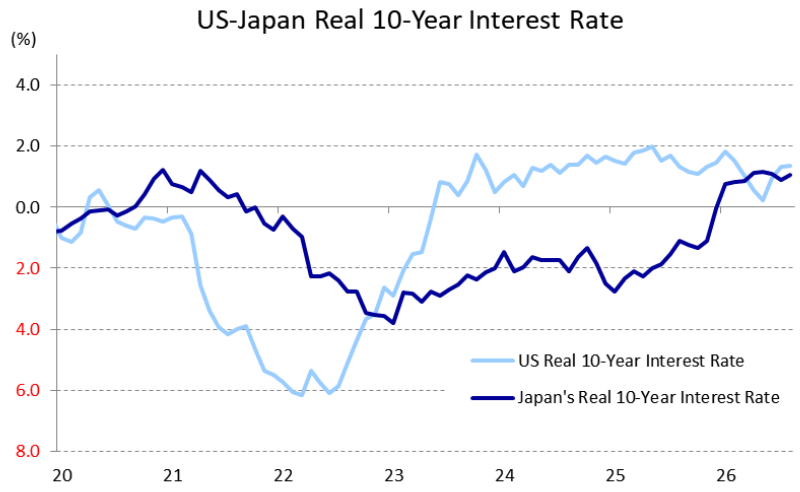
(Source) Bloomberg, etc.; prepared by the Global Foreign Exchange Department, Mizuo Bank.
Comparisons are based on the day preceding the Liberal Democratic Party (LDP) leadership election (October 4, 2025).
*1: Based on the Bank of Japan's Core CPI (excluding special factors).
*2: Compared as of the end of August each year, due to differences in CPI publication timing.

Having said that, it is open to debate to what extent the Takaichi administration's policy management has actually aligned with the concerns. For instance, while forecasts despairing of any rate hikes by the BOJ gained strength at that time, the BOJ has, in fact, implemented three rate hikes over the past year. This amounts to considerable progress toward normalization compared with initial assumptions. Again, when it comes to fiscal policy (framed as "responsible and proactive public finances" by the administration), while the initial budget request for FY 2027 (the first full annual budget for this administration) was the highest on record at around JPY 143 trillion, it may not necessarily be too expansionary if one takes into account that no supplementary budgets are scheduled. It is possible, of course, that the limited-duration two-year food-item consumption tax cut contributed to JPY depreciation and higher interest rates, but this alone fails to explain why 10-year interest rates nearly doubled. Here, one must also consider a straightforward explanation that higher interest rates may simply be reflecting the BOJ's intermittent rate hikes and reduction in government bond purchases. Another possibility is that the bond markets are skeptical of the administration's approach to funding key initiatives, such as those aimed at achieving sustained wage growth or strengthening defense

capabilities, using “special frameworks” or “item-based requests” that do not clearly reveal the funding amount. At any rate, a precise and final assessment of high-profile fiscal policies will only be possible after the final results for FY 2027 become available.

Undesirable Interest Rate Increase?

As a result of the sharp rise in Japanese interest rates, the real U.S.-Japan interest-rate differential has shrunk markedly, bringing Japanese interest rates to nearly the same level as U.S. interest rates (see graph). Looking at just the past year, it has to be said that Japan has outpaced the U.S. in terms of interest rate growth, and it would not have been surprising to see JPY appreciate if this was the main criterion. Of the two factors contributing to real interest-rate growth in Japan – inflation and nominal interest rate growth – the later has a higher contribution, but ultimately, this has not resulted in making JPY more attractive to investors. In other words, the nominal interest rate growth, as reflected in Japanese government bond (JGB) yields, is reflecting an increase in fiscal risks and the accompanying loss of confidence in JPY. In other words, the dominant view in the markets is that this is an “undesirable” interest rate increase.



(Source) Bloomberg; prepared by the Global Foreign Exchange Department, Mizuo Bank

Investors Took Future Rather than Ongoing JPY Supply-Demand into Account

Incidentally, I would like to touch upon changes in the JPY supply-demand climate, which is something I have been regularly monitoring in this report. The trade balance, which reflects JPY supply and demand, posted a deficit of roughly -JPY 3.3 trillion for the January-September period. This amounts to only a slight yoy increase in the deficit. Given the steep rise in crude oil prices since March, the objective assessment would have to be that real-demand-led JPY selling did not deteriorate all that much. However, it is also true that the release of crude oil reserves for four months from March through June helped to prevent a dramatic expansion of the trade deficit. In April, Japan’s trade balance actually posted a surplus (the crude oil import volume fell by a dramatic -62.7% yoy, resulting in a +JPY 282.3 billion trade surplus for the month), a result quite removed from the realities of the Japanese economy. As feared in this report, the trade deficit has been expanding since July, since the finalization of alternative procurement sources, with the deficit expanding to over a trillion for August. The 2027 trade deficit, as analyzed in detail later, may be considerable. I have held firm to my prediction of a weak-JPY scenario based on the assumption of a deterioration in JPY supply and demand since March this year, and it is possible that speculative traders also did the same. Japan’s crude oil import volumes have fully returned to normal since July, and they have been driving an expansion of the trade deficit.

I believe that a net JPY short position was accumulated based on the very simple prediction that the JPY supply and demand balance would worsen going forward even if not deteriorating at the time. In fact, while JPY’s weakening from the 147 level to the 155 level against USD seems likely to have been driven by speculation surrounding the Takaichi administration following its inauguration, JPY weakening from the 155 to a record low of 164 or so against USD may not be merely due to the Takaichi administration. Following the Iran attacks in March 2026, JPY depreciation accelerated due to an increase in JPY net short positions in the IMM currency futures transactions. There is a good possibility that rate trends were driven by speculative trading based on prospective rather than ongoing JPY supply and demand at the time.

Of course, the latest figure as of the writing of this report (reflecting the status as of October 27) is a net JPY long position of +JPY 8.04 billion (incidentally, this is the eighth week in a row that JPY has posted a net long position). While this may have been triggered by U.S. Treasury Secretary Scott Bessent’s “I’m the house” comment or in anticipation of further rate hikes by the BOJ, the fact that JPY remains in the 155-158 range despite this level of speculative JPY buying is something that must be taken seriously. Ultimately, it may be linked to the sharp expansion of the trade deficit since July. However, since this issue does not relate to the Takaichi administration’s fiscal, monetary, or currency policies, it must be discussed from a medium- to long-term perspective.

The Issue is not Whether Cards are Available, but How They are Played

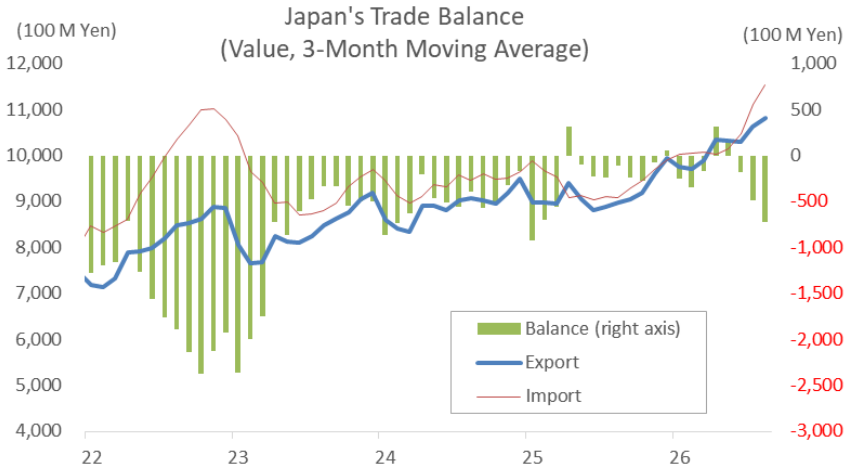
As mentioned at the start of this report, when viewed objectively, the Takaichi administration’s fiscal and monetary policies since its inauguration have not been all that reckless or fundamentally all that different from the policies of the Fumio Kishida or the Shigeru Ishiba administrations. In fact, when it comes to BOJ rate hikes, the pace has been unusually high compared with recent years. Despite this, high interest rates combined with JPY depreciation have persisted under this administration, and one of the reasons behind this may be the image of this administration or, to be honest, its method of communication. Rather than changing the cards available, perhaps simply changing the way they are played (their timing) is sufficient to change the situation.

It is a sad waste that currency (interventions) and monetary (rate hike) policies are not being implemented under conditions that can maximize their effectiveness. Looking back at the developments since October last year, when the Takaichi administration took office, there was a BOJ rate hike two months into the new administration, in December. However, immediately after the new administration took office, various experts who were the brains behind its economic policies insisted on stubbornly emphasizing the effectiveness of expansionary fiscal and monetary policies. This created skepticism regarding the sustainability of rate hikes under the administration. Consequently, the rate hike failed to make a dent in the JPY depreciation trend. Note also that the policy ideas of these economic advisors has drawn criticism even from Bessent, and continue to be a point of contention among market participants even today.
The BOJ kept its monetary policy unchanged in January, but a joint rate check was implemented by U.S. and Japanese authorities as a strong measure against the persistent trend of combined increase in interest rates and JPY depreciation. Following the Iran attacks in March, global inflation resulting from high commodity prices became a cause for concern, and JPY was sold in Japan amid concerns of an expansion in both trade deficits and the domestic-foreign interest rate differential. As mentioned above, the trade deficit did not in fact expand due to the release of crude oil reserves, so my theory is that JPY depreciated as a byproduct of speculative trading based not on current but future JPY supply and demand fears (anybody could see that the trade deficit was bound to expand from summer onward).
Looking at the government and the BOJ's policy responses in recent months, in April, while the BOJ kept its monetary policy unchanged, the government implemented a JPY buying currency intervention. In June, while the BOJ implemented a rate hike, there was no JPY buying currency intervention. In July, there was no rate hike, but a joint JPY buying intervention (through early August) was implemented by Japan and the U.S. In September, as in June, there was a rate hike but no currency intervention.
Therefore, looking back, it is clear that some measure, whether a rate hike or a JPY buying intervention, has been taken to contain JPY depreciation on a monthly basis, but all these measures have been piecemeal and fragmented.
When it comes to rate hikes, their impact has been undermined by opposing votes from reflationists within the BOJ's Policy Board, who are suspected (by the market) to have been appointed in line with the government's preferences. Subtle statements from government representatives also appear to discourage rate hikes, which further prevent them from being as effective as they may otherwise be. Of course, curbing the words and actions of Policy Board members is not an option, as their independence and views must be respected and protected, but it seems rational to think that, if rate hikes are going to be implemented either way, the least one can do is to maximize their effectiveness. If Japan can manage to align its monetary and currency policies perfectly and also use U.S. support to the full, I believe there is scope for reversing the JPY depreciation trend in line with U.S. and Japanese 10-year real interest rates, and other indicators.
Meanwhile, the distortion in real demand (i.e., trade deficit expansion) resulting from the Iran attacks will remain unchanged irrespective of the government's policy management. This aspect of the economy cannot be helped, but it is significant that downward pressure on JPY exerted by this factor will remain a persistent drag on the currency. As I have reiterated many times over the past few years, my position is that, more than discretionary macro policy management, structural factors such as the above are important for understanding the undercurrents causing JPY weakness.

JPY Supply and Demand Climate – 2027 is the Real Concern

A Clear Cliff Ahead

Let us take a look at the trade balance's current state and future prospects. Japan's trade balance for September, recently released by the Ministry of Finance, posted a fifth consecutive month of deficit at -JPY 536.5 billion. The cumulative deficit for the three months since securing alternative procurements (July through September) has hit -JPY 2.2930 trillion. Incidentally, the four months following the Iran attacks (March through June) posted a cumulative trade surplus of +JPY 1.060 trillion thanks to the release of crude oil reserves. As I have been warning since April, we are approaching a trade deficit "cliff." At the current pace, the trade balance for 2026 as a whole looks very likely to post a deficit of -JPY 5~7 trillion, depending on factors such as the extent to which depleted reserves are replenished and the extent to which semiconductor exports accelerate. Further, as also explained in last month's issue of this report, the price of crude oil from the U.S. transported to Japan via the Cape of Good Hope (the main route for alternative procurement) will have a time-lag of roughly 3~3.5 months compared to the spot price. In other words, for the purposes of the 2026 trade balance, crude oil prices should be considered at roughly USD 100 per barrel (even if, by some chance, crude oil prices crash in the near future), so there is little scope for a dramatic reduction in the trade deficit.

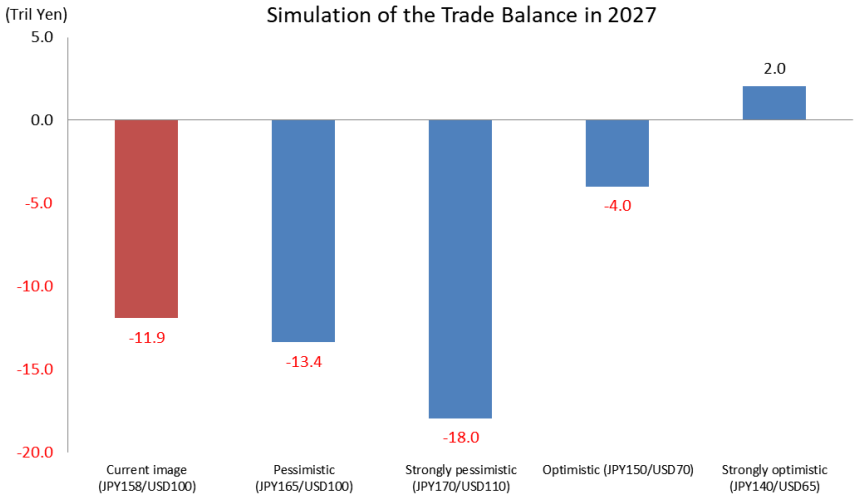


(Source) macrobond; prepared by the Global Foreign Exchange Department, Mizuo Bank

Incidentally, while the main background to the 2026 trade statistics is a sharp rise in imports amid soaring resource prices, there is also an unexpected expansion in semiconductor exports. To that extent, it must be noted, the expansion of the deficit is being checked. As previously reported, both import and export values posted all-time record highs not seen since 1979, the earliest year for which data is available, for 1H of FY 2026 (April-September). However, going forward (and as feared including in IMF analyses – details later), one must be prepared for a decline in the pace of exports if the AI-driven market were to crash. In that event, if JPY weakness and high crude oil prices were to continue to coincide, imports will accelerate, resulting in a rapid pace of trade deficit expansion.

An Early Forecast for 2027

The real problem will emerge in 2027, after alternative procurement has been fully established and reserves are no longer released. Once we factor U.S. crude oil, which has a higher unit price and also takes longer to transport to Japan, into Japanese imports as a "new fixed cost," where will the trade balance head? I would like to lay out the image of the forex-related supply-demand climate created by this new normal. My first premise is based on the forecast trade balance for 2026. I predict JPY 106.0 trillion in export value (factoring in a flat volume but slight increase in price pass-through), and JPY 85.0 trillion in energy import value (+JPY 1.0 trillion compared with the 2026 forecast) against entrenched energy inflation. Based on this premise, I will estimate sensitivity to changes in forex rates and crude oil prices during normal times (i.e., during times without distortions from reserve releases or alternative procurement).



(Source) Ministry of Finance; prepared by the Global Foreign Exchange Department, Mizuo Bank

First, assuming that current rate levels (USD/JPY at 158, crude oil at USD 100 per barrel as of the writing of this report) will be more-or-less normalized, the annual mineral fuel import value is estimated at JPY 32.9 trillion, and the total import value is estimated at JPY 117.9 trillion, resulting in a -JPY 12 trillion or so trade deficit. Incidentally, the highest ever mineral fuel import value was roughly JPY 33.7 trillion in 2022, and the total import value that year was JPY 118.5 trillion. If current USD/JPY and crude oil prices continue, the final result will be quite close to those of 2022, so there is significant concern of posting a deficit of well over -JPY 10 trillion.

Further, in a pessimistic scenario (USD/JPY 165; crude oil at USD 100/barrel), where the U.S.-Japan interest rate gap remains persistently high, or a deadlocked situation in the Middle East causes further JPY depreciation and persistently high oil prices, mineral fuel imports are estimated to increase to JPY 34.4 trillion, pushing the total import value to JPY 119.4 trillion, and the deficit to -JPY 13 trillion. Further, in a strongly pessimistic scenario (USD/JPY 170; crude oil at USD 110/barrel) resulting from an intensification of geopolitical risks, the trade deficit could balloon to -JPY 18 trillion. In this scenario, the BOJ is very likely to consider successive rate hikes to a level exceeding the neutral interest rate level.

Odds Favor Trade Deficit of -JPY 7~12 Trillion

I would like to touch upon the possibility of a return to trade surplus assuming an upside risk for JPY. While such a situation is unlikely to come true, it cannot be completely ruled out as a hypothesis. Based on estimates, in an optimistic scenario (USD/JPY 150; crude oil at USD 70/barrel) against the backdrop of a global economic slowdown or Fed rate cuts, Japan's trade deficit could shrink to -JPY 4 trillion or so; and in a strongly optimistic scenario (USD/JPY 140; crude oil at USD 65/barrel), there could even be a +JPY 2 trillion surplus.

The chart below shows the matrix of expected trade balance for each combination of exchange rate and crude oil prices. It seems obvious that the only scenarios in which a neutral or positive trade balance can be anticipated (grey portions in the figure) are when USD/JPY verges on falling below 150 and crude oil prices trend at around USD 65~70 per barrel. Conditions close to this did exist in 2024~25, resulting in the 2025 trade deficit shrinking to the -JPY 2 trillion level. Taking current financial situations in Japan and abroad as well as the situation in the Middle East into account, the developments certainly point to an upside risk.

Forex rate/crude oil price matrix (potential scenarios for 2027 trade balance)

Forex rate/ Crude oil price	USD60	USD65	USD70	USD75	USD80	USD85	USD90	USD95	USD100	USD105	USD110
JPY135	+4.13	+2.72	+1.31	-0.09	-1.50	-2.91	-4.31	-5.72	-7.13	-8.53	-9.94
JPY140	+3.50	+2.04	+0.58	-0.88	-2.33	-3.79	-5.25	-6.71	-8.17	-9.63	-11.08
JPY145	+2.88	+1.36	-0.15	-1.66	-3.17	-4.68	-6.19	-7.70	-9.21	-10.72	-12.23
JPY150	+2.25	+0.69	-0.88	-2.44	-4.00	-5.56	-7.13	-8.69	-10.25	-11.81	-13.38
JPY155	+1.63	+0.01	-1.60	-3.22	-4.83	-6.45	-8.06	-9.68	-11.29	-12.91	-14.52
JPY160	+1.00	-0.67	-2.33	-4.00	-5.67	-7.33	-9.00	-10.67	-12.33	-14.00	-15.67
JPY165	+0.38	-1.34	-3.06	-4.78	-6.50	-8.22	-9.94	-11.66	-13.38	-15.09	-16.81
JPY170	-0.25	-2.02	-3.79	-5.56	-7.33	-9.10	-10.88	-12.65	-14.42	-16.19	-17.96

(Source) Ministry of Finance, etc.; prepared by the Global Foreign Exchange Department, Mizuo Bank

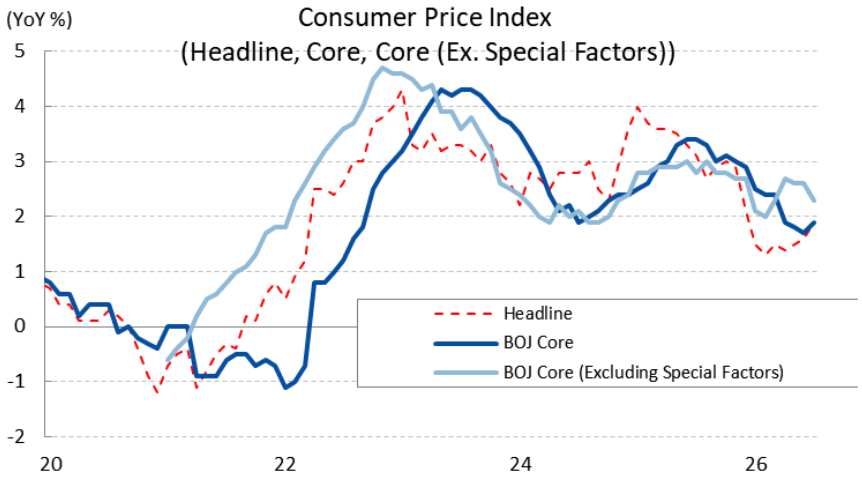
Assuming current economic and financial conditions, i.e., the combination of USD/JPY at 150~160 and crude oil trending at USD 90~100 per barrel (red portion in figure), a trade deficit in the range of -JPY 7~12 trillion seems most likely. Even at the lower end of this range (-JPY 7 trillion), the deficit would be the fifth largest in history, while a -JPY 12 trillion deficit would be the third largest in history. Strong downward pressure on JPY seems unavoidable for some time to come.

With non-energy imports structurally hovering around a high JPY 85 trillion level, Japan cannot achieve a trade surplus unless USD/JPY falls to 140 and crude oil prices fall to USD 65 per barrel. To reiterate my point, Japan was temporarily able to avoid a steep trade deficit "cliff" in 2026 only because the release of reserves served as a bulwark. It is only when the full cost of normal imports under normal conditions manifests in 2027 that the true resilience of JPY supply and demand will be tested.

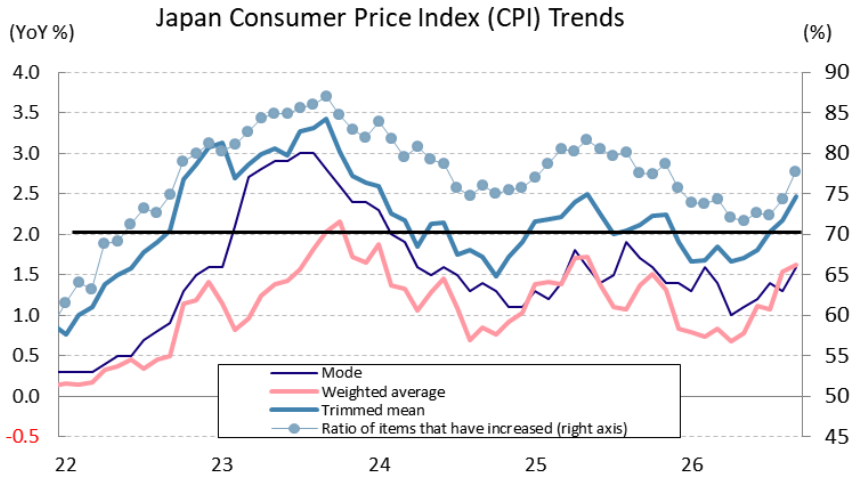
BOJ Monetary Policies Now and Going Forward – "Behind the Curve" Battle Begins

What Does Hitting the +2% Level Imply?

As per market predictions, the BOJ kept its policy rate unchanged at 1.25% in its October 29~30 Monetary Policy Meeting (MPM). The decision was passed by a majority vote of 8 to 1, with the only opposing vote coming from Policy Board Member Hajime Takata, who proposed a +25bp rate hike. Further, as predicted in advance, the Outlook for Economic Activity and Prices (the Outlook Report) indicates an awareness that "underlying CPI inflation" has reached a level that is "generally consistent with the price stability target of 2 percent." Of course, "reaching" the level is different from "becoming established" at that level, which is the state being aimed for. Because of this, the BOJ continues to maintain an accommodative climate, and the need for applying a break on rate hikes is logically comprehensible. However, finally reaching the price stability target of 2%, 13 and a half years after the implementation of "unprecedented monetary easing" under former BOJ Governor Haruhiko Kuroda, is undoubtedly a milestone achievement, and current BOJ Governor Kazuo Ueda's words, "the phase has changed" ring true. The Consumer Price Index (CPI) is growing stably at over +2% by various measures, so the above judgment would not have been inappropriate even earlier (see graphs to the right). Note also that it was made clear at the press conference that the contents of the Outlook Report were supported unanimously by Policy Board members, with no opposing views expressed. One wonders – did the two Policy Board members who cast opposing votes at the September meeting on the grounds of weak inflation growth change their views on inflation over the intervening six weeks? Their change of heart is quite interesting.



(Source) Bloomberg; prepared by the Global Foreign Exchange Department, Mizuo Bank



(Source) Bank of Japan; prepared by the Global Foreign Exchange Department, Mizuo Bank

Moreover, the median of forecasts for the 2027 CPI growth rate was upwardly revised by +0.2pp to +2.6% in the October Outlook Report compared with the previous issue, but the median of forecasts for real GDP growth rate was downwardly revised by -0.1pp to +0.7%. Going by the figures and the risk assessment, one cannot call this a positive

growth in prices; rather, I would say this is a phase when rate hikes aimed at preventing an inflation overshoot should be considered.

Problem Awareness Not Seen in 30 Years

Going by the discussions in the Outlook Report, one of the challenges for the BOJ in the medium term is how to deal with the risk of the underlying inflation rate exceeding +2% in the face of persistently high crude oil prices and other factors. In other words, a new challenge for the BOJ is a "behind the curve" battle. The section below says it all:

- **When the Bank was in the process of raising underlying CPI inflation toward 2 percent, downside risks to prices warranted considerable attention. However, there has recently been a shift in the phase of monetary policy, and looking ahead, it is necessary to pay due attention to keep the risk of underlying CPI inflation deviating upward to a level above the price stability target of 2 percent from materializing and thereby exerting an adverse impact on the economy afterward.**

Common sense says that the measure the BOJ can use to fight the risk of "underlying inflation deviating above the 2 percent target" is sustained rate hikes. Even here, implementing rate hikes in line with market expectations would not dispel skepticism of being behind the curve, therefore rendering the effort pointless; what is needed is rate hikes exceeding market expectations. Given that the BOJ recently embarked on ETF sales at an accelerated pace at a time when global share prices were shaky, one wonders if similar moves cannot be expected of it going forward. Of course, even if the decision was made based on the calculation that it would not have much of an impact given the pace of the sale, the fact remains that it was a bold decision given market conditions at the time (of course, there is also speculation that the decision was politically motivated by the need to secure funds for the national treasury). A risk scenario worth keeping in mind is that the Ueda administration, which has one year left in its term, may embark on the final stages of policy normalization.

At any rate, if the BOJ creates a tighter monetary climate to slow the surge in price growth by continuing to raise interest rates after having publicly acknowledged that the underlying inflation growth rate has reached the 2% target, this will bring it closer to an awareness of the problem than at any time in the past 30 years. Of course, the BOJ is not proclaiming the need for a tighter monetary climate at the current time, given that "reaching" the +2% target is different from "becoming established" at that level. However, to repeat my previous point, the only way to deal with the risk of "underlying inflation deviating above the 2 percent target" is to accelerate the pace of rate hikes. In that process, the main concern is to avoid a rate-hike overkill that negatively impacts the economy, so the gap between the official interest rate and the neutral interest rate level is likely to become more of a point of contention than ever before. With the official interest rate already exceeding 1.1%, which is the lower bound of the neutral interest rate as estimated by the BOJ, future rate hikes will increasingly be viewed in terms of their compatibility with the political landscape as well as public opinion.

The "Next Move" May Depend on AI and France

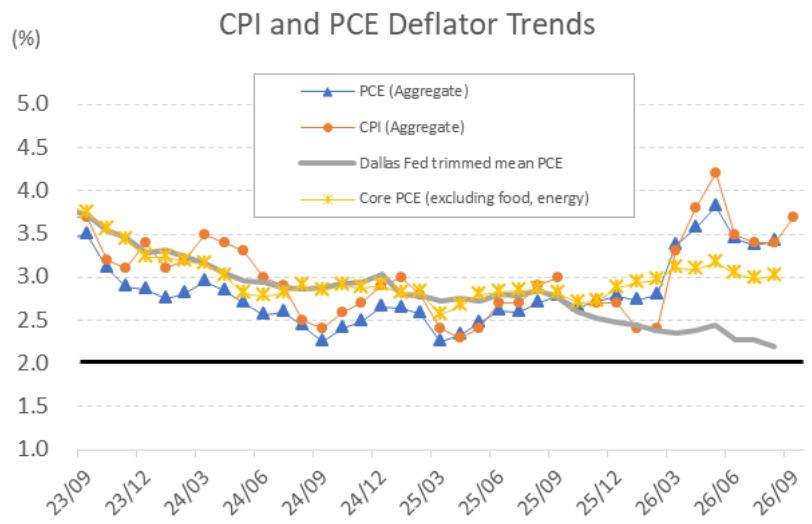
The situation in the Middle East, AI-related demand, and forex trends are the three important factors that continue to be cited as upside risks for inflation. If it is judged, based on these factors, that the risk of underlying inflation growth rate exceeding 2% remains high, the BOJ will continue on its rate-hike path. On the flip side, if the above risk factors weaken, the BOJ is likely to end its rate hike phase. In this context, the situation in the Middle East, which depends on the U.S., remains unpredictable; demand for AI has many inherent vulnerabilities, as warned by the IMF (GFSR); and forex trends, or more specifically the weak-JPY trend, is currently on hold amid across-the-board EUR weakness resulting from the turmoil in France. As seen in October, the simultaneous increase in U.S. and Japanese interest rates combined with JPY depreciation – a situation that was viewed with concern by both Japanese and U.S. authorities – has clearly calmed down since chaos erupted in France.

As I will discuss again later, given the nature of the turmoil in France, it seems unlikely to subside anytime soon, so the situation may be more or less the same at the time of the December MPM. If, for instance, the AI market has cooled compared with the present, and JPY weakness and JPY interest rate increase have also subsided by the December meeting, will the BOJ really go ahead with a rate hike (which is seen as a given at the present time)? Ultimately, if the neutral interest rate can only be accurately determined in retrospect, the BOJ may decide that it would be wise not to squander its limited rate hike opportunities when JPY selling seems on hold and there is less of a sense of urgency to protect the currency. I predict a rate hike in December as my main forecast scenario, but this forecast could change depending on how the situation in France evolves.

U.S. Monetary Policy Now and Going Forward – Increasingly Difficult to Curb JPY Depreciation

Next Move Remains a Rate Hike

At the October 27-28 FOMC meeting, the committee decided by a majority vote to keep the target range for the federal funds rate unchanged at 3.75~4.00%, apparently having prioritized waiting and watching to see what impact the September rate hike (first in three years and two months) would have. However, two members – Governor Lisa D. Cook and Cleaveland Fed President Beth M. Hammack – cast opposing votes, stressing the need for successive rate hikes. The overall assessment of economic activity in the FOMC statement was raised from "expanding at a solid pace" to "expanding at a strong pace," indicating that the rate-hike trajectory is not over. In fact, going by what Fed Chair Kevin Warsh said in his press conference – "Inflation is too high," and "I'm unwilling and unable to call (financial conditions) tight" – it seems that additional rate hikes are the default monetary policy course.

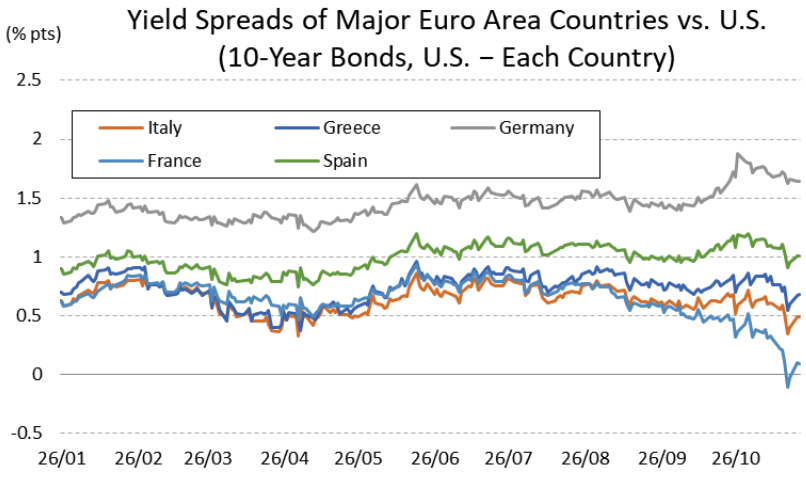


(Source) macrobond; prepared by the Global Foreign Exchange Department, Mizuo Bank

Inflation-related indicators are clearly strong, so the situation is not conducive to stopping rate hikes. In October, the U.S. September CPI drew attention for remaining high (Aggregate: +3.7% yoy; Core: +2.6% yoy), but the core PCE deflator, which is the indicator the FOMC refers to the most, also remained high at +3% yoy, warranting Warsh's assessment of inflation being "too high." Further, U.S. 10-year interest rates, while thought to have peaked, continue to surpass 5.0%, and are feared to potentially impact corporate and household consumption and investment activities going forward. From the standpoint of bringing down 10-year interest rates by suppressing inflation expectations, it seems inevitable that the Fed's next move will be a rate hike. Assuming that a rate hike in October was difficult to implement just ahead of the midterm elections, a +25bp rate hike at the last FOMC meeting of the year (in December) seems highly likely.

A Brief Respite Thanks to France and Impact on Japan

A major reason why the Fed was able to keep the FF rate target range unchanged this time was because of a break in the increase in U.S. interest rates. At the start of October, U.S. 10-year interest rates temporarily hit a nearly 24-year high at 5.36%. If the interest rate had continued to rise to above 5.5%, the Fed would have had to implement a rate hike. However, with the eruption of chaos in France, the financial market trends have begun to change. At one point in October, U.S. and French 10-year interest rate trends inverted (see graph). If this is the result of a "flight to quality," the trend is likely to continue for some time. Yields have also settled for Japanese government bonds.



(Source) macrobond; prepared by the Global Foreign Exchange Department, Mizuo Bank

In the forex markets, meanwhile, while EUR is seeing across-the-board weakness, there is a break in the JPY depreciation trend. To summarize, thanks to the political instabilities in France, U.S. interest rate increases resulting from JPY weakness (as per U.S. authorities) have stabilized, giving U.S. and Japanese currency and monetary authorities the time to pause and think.

To digress briefly from the topic at hand (Fed meetings), there are some concerns for Japan if U.S. interest rates continue to stabilize at the current pace. It has been pointed out that the reason the U.S. is lending its support to Japanese currency policy is because of concerns about rising U.S. interest rates as a result of JPY weakness. This is a reasonable surmise given that the U.S.-Japan joint rate checks in January and the U.S.-Japan joint currency intervention in early August were both conducted immediately following sharp rises in U.S. 30-year interest rates. Therefore, if U.S. interest rates were to stabilize, U.S. incentive to help curb JPY depreciation may weaken.

At any rate, it has to be said that the chaos in France is beginning to impact the dynamics of U.S. and Japanese currency and monetary policies, and may have created a policy environment that allowed both the Fed and the BOJ to keep their policy rates unchanged in October. While both the Fed and the BOJ are expected to implement rate hikes at their December meeting, three months on, both central banks may get away with keeping their policy rates unchanged

again if the intensification of chaos in France results in suppressing both U.S. and Japanese interest rates while promoting JPY appreciation.

Risks to My Main Scenario – Fate of AI Market with Increasing Vulnerabilities

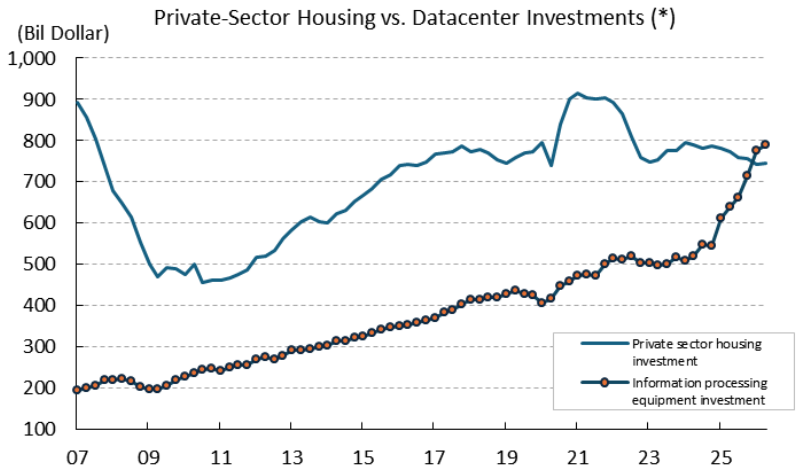
GFSR: Three Major Risks to Financial Markets

In mid-October, the IMF published its World Economic Outlook (WEO) and Global Financial Stability Report (GFSR) one after the other. As usual, the reports brought up many interesting points for discussion, but I would first like to take up the GFSR, which deep-dives into various issues under the subtitle "Resilience, Risk, and Transformation," for discussion. Chapter 1 of the GFSR report is titled "Beneath the Resilience: Rising Risks, Unresolved Vulnerabilities" and comprehensively discusses various potential risks to the financial markets in the medium term.

The chapter begins by presenting (1) AI-driven market correction, (2) a sharp rise in sovereign bond yields, and (3) cyber threats as the "three salient risks to financial markets." None of the issues can be overlooked, but (1) has continued to attract a great deal of attention in recent years. Given that this point has major implications for developed nations in Asia including Japan, I would like to take it up for in-depth analysis here.

AI Investment Built on Thin Ice

AI-related investments have become a major driving force for the financial markets and the global economy in recent years. While over half the U.S. economy is driven by personal consumption, the growth rate itself has been propelled by AI-related investment. Spending toward datacenters, semiconductors, and other related infrastructure have become major deciding factors of how good or poor real economic performance is. Only recently, the U.S. April-June quarter GDP data made the headlines because, for the first time in history, datacenter investment had surpassed private-sector housing investment in the U.S. (see graph). There is no question that AI-related investment is one of the main factors why the global economy has been strong despite offsetting factors following the Iran attacks, resulting in a situation where growth has become dependent on AI investment. This point has been emphasized also in the WEO, released around the same time. For all these reasons, it is important to seriously analyze risks associated with a rollback in AI-related investment.



(Source) macrobond; prepared by the Global Foreign Exchange Department, Mizuo Bank.
*Relates to information processing equipment

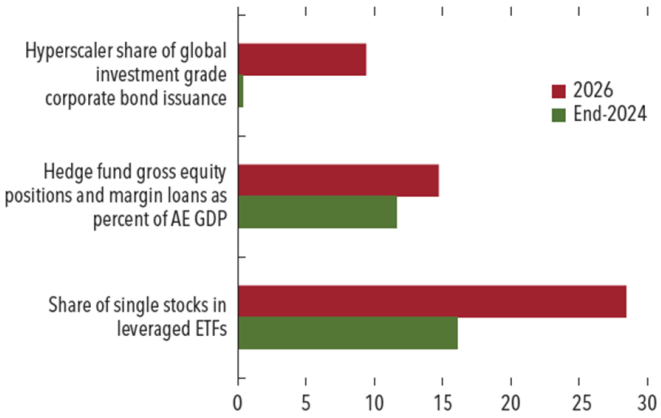
As explained in detail later, the factors supporting AI-related investment are by no means all robust, leaving one feeling that all this investment has been built on thin ice. Consequently, if there is even a slight doubt regarding its profitability, major shockwaves will run through the financial markets. In fact, it was only recently that, immediately following the release of Alphabet's financial statements in July this year, share prices of Alphabet and other hyperscalers (giant cloud-service companies) and AI semiconductor and hardware companies (e.g., NVIDIA) crashed, drawing widespread attention. This did not happen because Alphabet's financial results were poor (rather, they were strong). It happened as a reaction to the perception that the ROI was uncertain; that the cash flows being recovered were not keeping pace with the massive capital expenditures and rapid surge in borrowings, which were approaching a trillion-dollar scale. Since that time, the financial markets' focus, when it comes to AI-related investments, has begun to shift to the extent to which invested capital can generate sustained cash flows. We are now past that phase of the economy when the size of capital investments serves as a factor driving economic growth, and entering a new phase where the appropriateness of that size is beginning to be questioned.

Leveraged Trading by Three Entities

As explained above, while AI investment is driving real economic performance as symbolized by GDP indicators, it is increasingly obvious that similar AI capabilities can be achieved with lower levels of investments, as suggested by Chinese AI, etc. There is, therefore, an increasing trend whereby the size of the investment in itself is being treated as a negative factor in the markets. The aforementioned "Alphabet shock" too, was not the result of poor financial performance, but the fact that the company's capital investment plans had risen to higher levels than originally predicted, and there were concerns over predictions of even higher levels of investment in 2027. With free cash flows turning negative on a quarterly basis as a result of the enormous capital investment burden, even hyperscalers with ample cash generating power are running out of cash and having to issue corporate bonds or increase their reliance on loans. When this reality surfaced, market participants began to question when and to what extent investment from AI infrastructure, despite its significant demand, will be returned to investors in the form of profit rate (margins). Incidentally, the WEO puts forth a scenario whereby the rollback in AI investments could cause a decline in global GDP, investments, and consumption (due to the negative wealth effect) by up to -0.4%, -1.3%, and -0.6%, respectively.

The size of the shock resulting from a rollback in AI investments depends on leverage, with the GFSR pointing out three sources of leverage – (1) corporate bond issuance by hyperscalers, (2) margin loans by hedge funds, and (3) investments in leveraged exchange-traded funds (ETFs) by retail investors (see graph). In other words, leveraged trading by three types of entities (corporations, institutional investors, and individual investors) is focused on the single theme of AI. Naturally, when these positions are unwound, an equally focused mass exodus will occur. With regard to (1), since 2024, the share of hyperscaler issued bonds within the total amount of investment-grade corporate bonds issued globally has increased by over ten times, from under 1% to 10%. Of course, this has not been a major problem, given the amount of cash flows generated from these companies' core businesses, but as mentioned above, the sustainability of ballooning debt costs has been brought into question. With regard to (2), the sum of hedge funds' gross equity positions and margin trading borrowings has increased from 10% to 15% of the GDP of developed countries, reflecting the increase in AI-related stocks' leveraged positions. Finally, with regard to (3), the percentage of single stocks in leveraged ETFs increased from 16% to 28% during the same period. This is the result of individual investors, like institutional investors, using such funds to make concentrated investments in AI-related stocks.

1. Equity Leverage and Debt related to Artificial Intelligence
(Percent)



(Source) IMF; prepared by the Global Foreign Exchange Department, Mizuo Bank

To summarize the current state of affairs, both individuals and institutions are flocking to be a part of the real-economy-based investment plans of hyperscalers, which are business corporations. If these investment plans get derailed, major shockwaves will run through both the real economy and financial markets simultaneously. In the sense that funds with questionable repayment potential are accumulating, this is similar to the subprime mortgage loan problem, but there is no doubt that demand for AI-related investment is on the rise. Even if the potential for AI demand to rise is widely acknowledged, opinions are beginning to be divided regarding the appropriate scale (cost) of investments.

The Dangers of Circular Financing

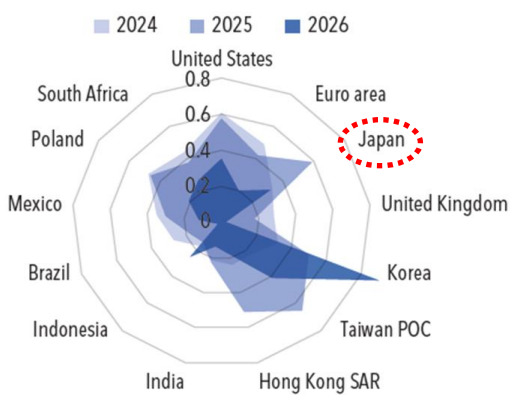
Another issue inherent in AI investment is circular financing. The GFSR points out 14 transactions announced since 2023 of hyperscalers making equity investments to the tune of approximately USD 300 billion in AI companies (startups) with weak financial foundations, complemented by USD 650 billion in debt provision. In return for these contributions, hyperscalers have demanded sales commitments (revenue guarantees) worth roughly USD 1.4 trillion through orders for their own services and semiconductors. In other words, multilayered transactions where hyperscalers demanded orders for their own products in return for loans are taking place in the AI industry to the extent that they have become deeply rooted in the ecosystem. The fact that roughly USD 1.4 trillion in future sales commitment (cloud computing usage fees, semiconductor purchases) is linked to their total contribution (of USD 950 billion or so) makes it obvious that the topline (revenue) growth stories of these hyperscalers are heavily relying on this commitment.

This amounts to AI companies leveraging each other, which is on a different dimension from them being leveraged by the three entities in the previous section. Inevitably, if the business of the startup AI company receiving funding deteriorates, its sales commitment will disappear. The GFSR terms this risk associated with the ecosystem erected by the AI industry "wrong-way risk." When this risk surfaces, the three parties in the previous section will also unwind their leverage simultaneously, forcing the financial markets to undergo severe correction.

Potential Unforeseen JPY Appreciation Risk Scenario

Finally, it is important to consider the areas that may be affected by any corrections to the AI-driven market. The U.S., being the main driver of AI investments, would also be the epicenter of any shock, but sensitivity to the shock varies by country and region. The GFSR focuses on the developed countries/regions in Asia (mainly South Korea, Taiwan, and Japan, in that order) as having high "beta" values (sensitivity) to AI-related stock returns globally. By contrast, the Euro area and UK (as well as most emerging markets) have lower sensitivities (see graph). However, the "lower" sensitivities are merely relative. Taking into account the sharp rise in U.S. equity holdings between 2022 and 2026, it may be difficult to remain fully insulated from corrections in the AI market. As already evidenced by the flow-of-funds statistics, Japan has, unfortunately, chosen this moment in history to steadily move away from savings to

1. Equity Return Beta to the Global AI Index



(Source) IMF; prepared by the Global Foreign Exchange Department, Mizuo Bank

investment, with domestic and foreign equity and investment funds now making up roughly 30% of household financial assets. Given that the U.S. economy also had a roughly 30% equity holding ratio during phases when the “wealth effect” was in high focus, I fear that any major correction in stock prices could transmit financial market shocks to the real economy via a “reverse wealth effect.” Further, if the Fed were to embark on a course of rate cuts to counter the downward pressure on the U.S. economy, which has been propped up by AI-related investment activity primarily centering on hyperscalers, that would cause JPY to appreciate steeply against USD, which itself is likely to damage the balance sheets of the Japanese household sector, which has begun to heavily tilt toward foreign-currency-denominated assets.

At any rate, the GFSR warns that the current AI boom is built upon an unstable leverage structure. For one thing, it would be difficult for fund procurement to continue expanding at its current pace, and for another, there are concerns that signs of a downward adjustment in expected returns, revealed by, say, a corporate earnings report, could lead to a more composite market correction affecting equities, corporate bonds, and private credit. Japan is by no means an unaffected bystander. Rather, from a global perspective, Japan is bound to be significantly impacted by any share price correction. In particular, it must be noted that, if a sharp decline in share prices were to force a real economic slowdown and compel the Fed to adopt a course of rate cuts, this could directly lead to an unexpected JPY appreciation scenario.

EUR Outlook – ECB Caught Between France and Inflation

EUR Area Monetary Policies Now and Going Forward – Time for Concern about Second Round Effects

Macron's Shadow Looms over Mid-Term Resignation

At its October 29 Governing Council meeting, the ECB decided to keep its key policy rate (the deposit facility rate) unchanged at 2.50%. While expressing concern that rising energy prices are pushing up the euro area's Harmonized Index of Consumer Prices (HICP), the ECB opted to adopt a wait-and-see approach. This decision reflects caution regarding upward pressure on interest rates originating in France, which could lead to an unintended tightening effect that would increase the impact of the two most recent rate hikes (in June and September). News emerged just before the meeting that ECB President Christine Lagarde would step down early, in February 2027. While this has spurred discussions about her reasons and future plans, it has long been known that she has no intention of serving out her full term or of running in the French presidential election. A prominent view is that France's "lame duck" Macron administration pressured her to step down early in order to position itself to influence ECB personnel decisions.

President Lagarde stated at the post-Governing Council-meeting press conference that the reason for her mid-term resignation was – "to have the freedom of speech, the freedom of expression and the freedom to engage on matters that are not monetary policy matters." – but this does not seem to be a convincing reason for her to walk away from a position she has held for over seven years with only about half a year remaining in her term. It is possible that, with France's 2027 presidential election in mind, she is seeking to preemptively limit any potential influence that the right-wing presidential candidate Marine Le Pen might have on the appointment of senior ECB officials. The strong political aspect of President Lagarde's views has been noted since the very beginning of her tenure, and it seems this aspect has become even more apparent as she prepares to depart.

The processes of appointing senior ECB officials in the future will be far from straightforward. It will be necessary to give due consideration to such diverse factors as the selection of a successor to Executive Board Member and Chief Economist Philip Lane (whose term expires in May 2027) and the need to strategically balance executive board members' national origins in light of the nationalities of past ECB presidents and even the nationality of the European Commission President (whose term ends in 2029). Given that two of the ECB's four presidents to date have been French (including the most recent one), it is unlikely that the next president will be French, and I plan to discuss this point in more detail in the future.

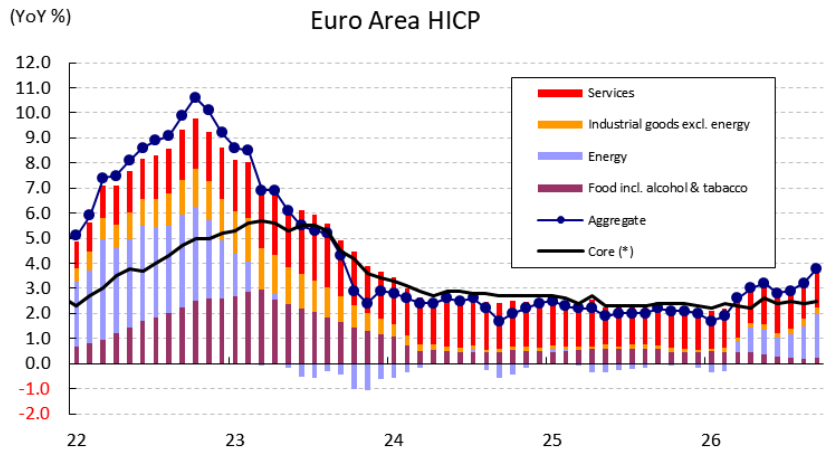
The post-Governing Council-meeting press conference was dominated by questions about President Lagarde's future and there was even a moment when she grew exasperated and asked that the questions be focused on monetary policy instead. If she really wanted to keep the focus on monetary policy, however, one might think she should not have announced her resignation before the meeting. Was there truly such an urgent, pressing reason for her early departure and the early announcement of that departure?

Explicit Mention of "Second Round Effects"

Regarding the core subjects – the euro area's economic and inflation situations – the Governing Council meeting's statement notes that – "The increased magnitude and duration of the energy shock, as well as the implications for indirect and second-round effects, are likely to drive up inflation and lower growth." – and the explicit mention of "second-round effects" was particularly noteworthy. The first journalist called on at the post-Governing Council-meeting press conference said – "for the first time in I don't know how long the mentioning of second-round effects in your press release was quite striking. So does it also mean that the market is about right to expect a rate hike in December, because clearly there is now a risk of second-round effects?" As of the end of the GC meeting, the markets had priced in an approximately 82% probability of a rate hike in December.

In response, President Lagarde explained that second-round effects had already been factored into the staff projections from September and so are not really a newly identified issue, although she admitted that the degree of rises in energy prices and long-term interest rates had been unexpected. She clarified that, while the possibility of a rate hike was considered in light of these two factors, the Governing Council reached a unanimous decision to keep rates unchanged, given that underlying inflation has remained largely stable.

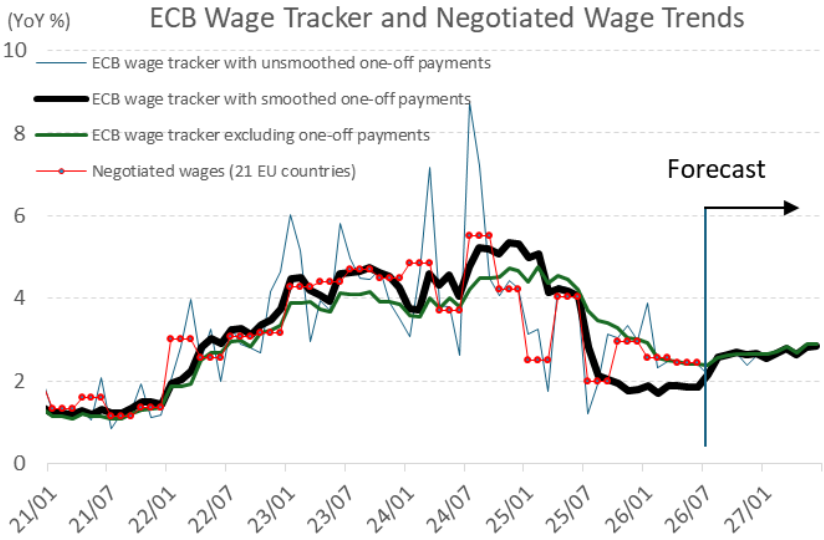
In fact, while overall-basis HICP's yoy growth rate has surged to 4.0% – driven primarily by energy prices – the core-basis index, which more accurately reflects underlying inflation trends, has remained stable at around 2.5% (see graph). That said, lessons learned early in the COVID pandemic period suggest that this pattern is unlikely to last very long. If the upward pressure on general price levels continues, workers and households will inevitably push for higher wages, and the corporate sector will likely shift toward accommodating such wage demands so long as they can be covered by selling-price increases. The ECB is likely to recognize such nascent signs of an inflation surge and, based on recognition of the time lag before tightening measures take full effect, opt for an early interest-rate hike. So it appears reasonable to expect an ECB interest rate hike in December.



(*) Core excl. energy, food, alcohol & tobacco
(Source) Datastream; preparedby the Global Foreign Exchange Department, Mizuo Bank

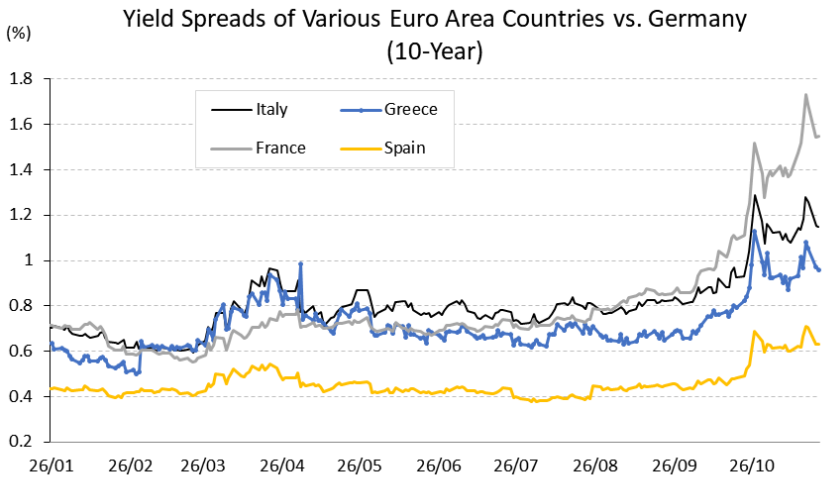
Troubling Signs Regarding Negotiated Wages

The second reporter called on at the press conference posed a more probing question about what interest rate hike discussions took place. In response, President Lagarde acknowledged that both the pros and cons had been debated. She explained that the decision was unanimous, as the period leading up to the December meeting is expected to be "information-rich," providing sufficient justification to wait for further data. She noted that information to be released before the next Governing Council meeting includes another round of staff economic projection, two sets of monthly HICP data, third quarter (July–September) euro area GDP figures, and employment data, along with per employee compensation and negotiated wages data. She also explained that unemployment rate and industrial production figures as well as banking interest rate statistics would be released twice (for September and October) and the November Purchasing Managers' Index (PMI) data was worth taking into consideration. While all of these data are important bases for making decisions about interest rate levels, the negotiated wages trend is arguably the most vital basis for assessing potential "second-round effects." A year ago, there was no expectation that wages would still be on an upward trajectory at this time, but the ECB's wage tracker now projects that wages will begin rising again, with the current period marking a wage-growth-rate nadir (see graph). If this re-acceleration of wage growth coincides with persistently high energy prices, there will naturally be greater risk of a wage-price spiral – the most feared scenario – so interest rate hikes seem to be a foregone conclusion.



(Source) ECB and macrobond; prepared by the Global Foreign Exchange Department, Mizuo Bank

Avoiding Explicit Mention of France



(Source) macrobond; prepared by the Global Foreign Exchange Department, Mizuo Bank

Of course, several questions were raised during the press conference about whether the ECB would intervene in the French government bond market. In response, President Lagarde stated that the rise in long-term government bond yields is a global trend, not limited to the euro area. She expressed the view that various factors are contributing to this – including projected inflation rates, expected interest rate trends, and bond issuances by certain hyperscalers – and repeatedly gave answers that seemed to divert attention away from the French government bond market. Such exchanges happened about three times during the press conference. As can be seen from the trend in the gaps between German bond yields and other euro area members' government bond yields (see graph), it is unreasonable to equate what is happening in French bonds with what is happening globally.

Consequently, without explicitly naming any country, President Lagarde stated that – "Those countries with high debt have to factor into their fiscal policy plans the fact that interest rates are higher, and will probably remain higher, for a period of time. In Europe, if you apply that principle, what it means is that policy measures have to be adopted, as part of a plan that is always submitted to Brussels, and that has to comply with the European fiscal framework." For the ECB to activate its framework for purchasing government bonds (the Transmission Protection Instrument (TPI)), the country in question must be in compliance with EU fiscal rules that cap annual budget deficits at 3% of GDP. If a country is not in compliance, it must have submitted a plan for fiscal consolidation (austerity measures) to the European Commission. In short, President Lagarde was being extremely careful to avoid naming France but made it clear that the TPI cannot be applied to French government bonds, as the country fails to meet these requirements. Given that she is both ECB President and a French national, one can imagine how difficult a position she was in when providing these answers.

ECB's Inability to Act a Stroke of Luck for the U.S. and Japan

While acknowledging the difficulty of activating the TPI, President Lagarde sought to deter speculative activity by stating – "But I would also add that, should market developments threaten the smooth transmission of our monetary policy, including through unwarranted and disorderly market movements, we have instruments available to respond. And the criteria and conditions under which this applies are well known, they are published, and I'm sure you know them."

Nevertheless, in practical terms, it is highly unlikely that the ECB would intervene to address rising French interest rates – which stem purely from domestic political turmoil and fiscal irresponsibility – as doing so would create a moral hazard. Purchasing bonds when a government is unable to present an austerity-focused budget to the European Commission would set a very dangerous precedent. The markets are quite aware of these underlying realities, so President Lagarde's efforts to influence the markets have proven entirely ineffective – French government bond yields have remained at levels far from normal even after the Governing Council meeting. Given the current political situation in France, any substantive fiscal consolidation will effectively be deferred until after the elections. Consequently, concerns about the risk of gradual downgrades of French government bonds by rating agencies and the loosening of fiscal discipline are likely to persist in the bond and foreign exchange markets, making it highly probable that we will continue to see a simultaneous rise in regional interest rates and weakening of EUR.

So long as the ECB remains unable to act, the trend of shunning EUR-denominated assets in the bond and foreign exchange markets is likely to continue – a development that can be seen as a stroke of luck for the United States, which has been struggling with rising interest rates, and for Japan, which has been grappling with rising interest rates along with JPY weakness. How long will this situation continue? We have entered a period in which political instability in France has a direct impact on the outlook for financial markets in Japan, the United States, and Europe.

The Euro Area Economy Now and Going Forward – French Government Bond Concerns Well-Founded

France's Month of Turmoil

The downtrend in French bond prices and weakening of EUR are continuing, driven by concerns about France's fiscal situation and political divisions. These issues have been a factor in financial markets for nearly a month, but the bond market has yet to normalize, and there are growing concerns that the elevated yields on French government bonds may persist for a protracted period. France's recent domestic turmoil began in mid-September, when high school students in Paris suburbs began street demonstrations to protest teacher shortages compounded by long-standing problems regarding aging school facilities. Much like the "Yellow Vest" movement of 2018 (France's longest-running wave of demonstrations in the post-war era), a small spark spread via social media, and the focus of the protests has expanded well beyond demands for better educational environments, evolving into a broader critique encompassing the declining quality of public services (including education), the persistently high cost of living, and, ultimately, the policies of the Macron administration in general. The high cost of living is a fundamental underlying issue, as it prevents teachers from living near certain schools and makes it difficult to recruit adequate numbers of teachers to staff those schools.

There are proven ways in which government funds can alleviate such problems in urban areas with extreme housing cost inflation, such as London's support measures to help "key workers" (such as firefighters and nurses) access affordable housing. Such fiscal interventions are sometimes needed to maintain essential social infrastructure. Furthermore, when this article was written news reports were indicating that the French protests had spurred intensifying movements in Italy, Spain, and Portugal that appear to reflect an increase in social unrest caused by inflation.

More Challenging than "Yellow Vests" Movement

The student-sparked demonstrations have already grown into a general protest movement active throughout France. Major labor unions have announced that on November 5 they would collaboratively organize a cross-sector strike and demonstrations on a nationwide scale. The protests have taken on a comprehensive character, calling for improvements in living conditions – such as the restoration of quality across public services (including education) and wage increases to keep pace with inflation – echoing themes seen in the "Yellow Vests" movement. The Yellow Vests movement began as a backlash against fuel price hikes (including taxes on gasoline). They subsequently evolved into a broader expression of discontent with the Macron administration's economic policies, social inequality, and rural regions' economic decline, and ultimately took the form of large-scale and prolonged demonstrations. It remains unclear whether the current protest wave will surpass the Yellow Vest movement in scale and longevity, but it is fair to say that the situation is already having a significant impact on financial markets. The French government led by President Macron still held a relatively solid parliamentary base when the Yellow Vests movement gained prominence in 2018, and it was that solid base that enabled such political compromises as the freezing of the fuel tax hikes that had triggered the protests before concerns within financial markets could escalate significantly. In contrast, the current French parliament is a hung parliament split into three factions – the center, the far right, and the left – and any decisive policy action risks spurring a no-confidence vote against the government. The parliamentary factionalism has paralyzed government decision-making processes and made compromise responses to the demonstrators impossible, a situation that financial markets find particularly unsettling.

The Yellow Vests movement was sparked by a specific, direct economic burden – fuel taxes – which made it possible to focus on the issue of maintaining purchasing power (living standards) while arguing that the government favors the wealthy while imposing heavy taxes on ordinary people. Consequently, the government was able to contain the situation by reversing the tax hike.

But the issues at stake currently are much broader. The protests appear to be driven by dissatisfaction with the overall macroeconomic environment (particularly inflation) and are resonating across many social strata. It is precisely this dynamic that is causing concern in financial markets.

Public at Front Door, Financial Markets at Back Door

Moreover, the timing of the current unrest is particularly unfortunate. The budget-making processes of euro area member states follow a schedule known as the European Semester. The European Commission (the EU's executive branch) reviews each member state's national reform program and draft budget in advance and monitors them to ensure their policies do not deviate from EU rules. The European Semester operates as an annual cycle, running from November through October of the following year. The current autumn period (September through December) is the most critical phase, when pressure regarding fiscal discipline and budget formulation is at its peak (see chart). In particular, October 15 of each year is the deadline for euro area member states to submit their draft budgetary plans (DBPs) for the following year to the European Commission. Therefore, the current protests have occurred at a time that is extremely inopportune from a political perspective.

Autumn Period of European Semester (Sept. - Dec.)

Time Period	Events/Procedures	Market Impact
Late Sept. - Early Oct.	**Submission of Budget Proposals to National Parliaments:** In France, the draft finance bill (PLF) for the following fiscal year is typically submitted to the National Assembly in early October.	This period often sees an intensification of domestic political conflict, with a sharp rise in the risk of the opposition tabling a motion of no confidence.
October 15	**Deadline for Budget Proposal Submissions to European Commission:** All Eurozone member states are required to submit their Draft Budgetary Plans for the following year to the European Commission in Brussels.	Each country's figures (such as deficit levels and planned spending cuts) are evaluated against common EU standards.
Late November	**Publication of European Commission's Evaluations and Opinions:** The European Commission releases its "Autumn Package," assessing whether each nation's budget proposal complies with EU fiscal rules (Stability and Growth Pact).	Determinations of "non-compliance" or "risk of non-compliance" can lead to corrective action recommendations or even the risk of sanctions – a factor that can influence sovereign bond markets.
December	**Budget Approvals by National Parliaments and European Council:** The final push to pass and enact the budget before the end of the year.	This critical deadline determines whether a compromise is reached, or if the budget is rejected – potentially leading to the government's resignation.

(Source) European Commission; prepared by the Global Foreign Exchange Department, Mizuo Bank

The 2027 budget proposal submitted by the Sébastien Lecornu administration to the National Assembly on October 1 aims to reduce the fiscal deficit (as a percentage of nominal GDP) from 5.4% in 2026 to 5.0% in 2027. Achieving this requires (1) increasing revenue, (2) reducing expenditures, or (3) both. As the public already feels burdened by heavy taxation, the administration has opted for a fiscal consolidation strategy centered primarily on option (2). Specifically, the plan includes revising the inflation indexation of pension payments, freezing increases to civil servant salaries, curbing

healthcare and social security spending, and requiring local governments to cut their own expenditures. These policies will directly contribute to the deterioration of the educational environment (the very issue that triggered the current unrest), so they are bound to trigger an intense public backlash.
Incidentally, the period around November 5 (when the abovementioned nationwide strike and demonstrations are scheduled) coincides with the French National Assembly's deliberations on the 2027 budget bill. As major labor unions join forces to intensify their protests, it is questionable whether the government and ruling coalition will be able to proceed with the planned spending cuts. Should they opt for an easy compromise in negotiations with the opposition, protests within French society may subside, but protests in the financial (bond) markets could intensify. Being positioned between pressure from the public at the front door and pressure from financial markets at the back door, they face a difficult dilemma.

When Will Things Settle Down?
When will this turmoil finally settle down? To answer that question, we need to understand two problems confronting the French political system. The first problem, mentioned above, is the emergence of a "paralysis-prone parliament" – a three-way standoff between the centrist ruling bloc, the far-right National Rally (RN), and the leftist New Popular Front (NFP) coalition – which has been static since the 2024 general election. The second problem is the fact that the next presidential election is fast approaching. The former problem makes it impossible for the French parliament to act flexibly to implement fiscal consolidation measures. Complying with the EU's Excessive Deficit Procedure (EDP) would require massive spending cuts and tax increases. It is unfeasible for a minority government to try to push through such an austere budget, as doing so would almost certainly trigger a no confidence vote. Reflecting the seriousness of France's political impasse is the fact that Prime Minister Sébastien Lecornu is the fourth person to hold the prime minister office in the roughly two years since the 2024 general election (following Gabriel Attal, Michel Barnier, and François Bayrou).
However, the latter problem appears to be the more serious obstacle. With the French presidential election fast approaching (in the spring of 2027), incumbent President Macron is barred from running due to the three-term limit and has effectively become a "lame duck". As the election draws nearer, it becomes increasingly difficult for any political faction to advocate measures that impose hardship on voters, such as moves to maintain pension reforms or cut social security spending, so any meaningful fiscal consolidation will effectively be postponed until after the election. As a result, bond and forex markets' concerns about France's lack of fiscal discipline and the likelihood rating agencies will progressively downgrade French government bonds will persist and continue causing a euro area interest-rate rise and EUR weakening. On October 30, a major U.S. credit rating agency maintained France's long-term issuer rating at "A+" but revised the country's outlook from "stable" to "negative", thereby increasing the likelihood of a future rating downgrade. In light of all this, it appears that the current turmoil may continue until the presidential election is over.
If only a positive post-presidential-election scenario could be envisioned, market anxieties would not necessarily be intensifying. However, as is widely known, it has long been believed that the most likely winner of presidential election is Marine Le Pen, RN's effective leader. (While Jordan Bardella is the official RN party leader, he is Le Pen's protégé and, should she become president, he is widely expected to be her choice for prime minister.) Ms. Le Pen has long championed a populist, expansionary fiscal policy – including cuts to the value-added tax (VAT) on energy and essential goods, lowering the retirement age, opposition to the privatization of public services, and generous subsidies for domestic industries – and financial markets remain wary of what France's economic prospects might be under such a policy regime. Of course, Le Pen is not without a plan for dealing with the current situation. On October 6, she unveiled her "Fiscal Renaissance" plan aiming to reconcile large-scale fiscal consolidation measures with tax cuts and emphasized the urgency of the crisis by warning that – "If the French people do not opt for a political break with the status quo, France is heading toward a de facto default." Specifically, she has pledged that, if elected, she would within 18 months of taking office reduce France's fiscal deficit by EUR71 billion, implement EUR54 billion in tax cuts, and achieve a balanced primary fiscal balance (excluding interest payments). She has set the goal of cutting government spending by over EUR140 billion by the end of her term in 2032 and is aiming to bring the primary balance into surplus and reduce the government debt-to-GDP ratio from 121% in 2027 to 112% – a 9-percentage-point reduction over five years. While such a dramatic 180-degree shift from her previous positions might ordinarily be viewed as a positive development, the current state of government bond yields suggests that she has yet to gain any credibility with the financial markets.

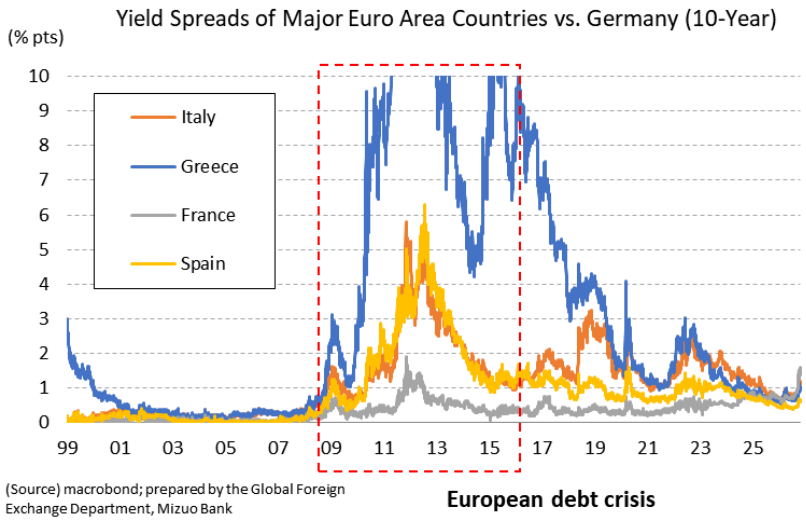
Le Pen to Undergo a "Meloni-style" Transformation?
Some financial market players are anticipating that Ms. Le Pen will transform herself while in office in a manner comparable to the transformation of Italian Prime Minister Giorgia Meloni, and I also believe that is a possibility. Italian Prime Minister Meloni first took office amid concerns that she was a radical right-wing populist, but after forming her government, she shifted to a pragmatic approach, complied with EU fiscal rules and the NATO alliance framework, and has succeeded in earning growing credibility and trust. Today, the Meloni administration is one of the most stable governments in Western Europe. Prime Minister Meloni has garnered praise for her ability to maintain a constructive relationship with United States despite challenges presented by the Trump administration as well as for her ability to take a firm, independent stance when necessary.
Fiscal soundness and cooperation with the Western order are the two key conditions for this "Meloni-zation," but financial markets cannot place their trust in Le Pen until they see how she handles these matters in practice. The earliest point at which the financial markets might truly become convinced of Le Pen's "Melonization" would likely be in the autumn of 2027 (following France's success in completing European Semester processes applicable to 2028). In other words, about a year from now. Le Pen can naturally be expected to make generous pre-election promises to appeal to her core base of low-income and working-class voters in rural areas who desire lower retirement ages and tax

cuts, and the possibility that she is not actually determined to fulfill all those promises in reality has to be given due consideration, yet there will inevitably remain doubts about that. As was the case with Prime Minister Meloni, the bond market is likely to continue demanding risk premiums until Le Pen generates a track record of positive measures. In particular, the market will be hoping to see her make prudent cabinet appointments (such as the selection of a pro-EU, pragmatic technocrat finance minister) and, most importantly, to witness her ability to secure the passage of painful austerity measures in the 2028 budget in line with EU requirements. Given this, there is a risk that French government bonds (and, by extension, EUR) could face downward pressure over the coming year, from the present through the election campaign and continuing until the new administration finalizes a 2028 budget.

Supplement: Euro Area Joint Bonds Now and Going Forward – IMF Recommendations and Expectations

IMF Lauds Euro Area Joint Bonds

The IMF's latest Global Financial Stability Report (GFSR, released in October) includes an analysis encouraging the euro area to adopt common debt issuance. A box in the report, titled "European Union Common Borrowing Has Mitigated Sovereign Bond Market Fragilities," provides empirical evidence on how the existence of common debt has brought stability to the region's sovereign bond markets. As discussed in previous editions of this article, the gaps between the yields of German government bonds and other EU countries' government bonds have narrowed significantly in recent years (see graph). While there has not been the kind of excessive convergence seen prior to the European debt crisis (such as German and Greek bond yields being identical) there is no longer a sense that the euro area bond market is fragmented or that the structure of the single currency area is crumbling.



(Source) macrobond; prepared by the Global Foreign Exchange Department, Mizuo Bank

The GFSR identifies several factors contributing to this, such as improvements in Southern European nations' primary fiscal balances and the ECB's preparedness to implement countermeasures against shocks. Regarding the latter, it is worth noting that when the European sovereign debt crisis first erupted, no framework existed for the ECB to purchase securities – the situation was managed through the Securities Markets Programme (SMP), which was hastily created in 2010 and subsequently discontinued. Since then, the ECB become capable of implementing various asset-purchase mechanisms – such as the public sector purchase programme (PSPP), the outright monetary transactions programme (OMT), the pandemic emergency purchase programme (PEPP), and the transmission protection instrument (TPI) – each with its own distinct name and definition. Although the GFSR refers specifically only to the PEPP and TPI, it is indisputable that the PSPP and OMT played central roles in bringing the sovereign debt crisis to an end. In any case, it is undoubtedly true that the euro area bond market remains stable today precisely because the ECB has established a track record of intervening in the bond market without hesitation during times of crisis.

EU Bonds Inspiring Confidence

However, the latest GFSR does not attribute the narrowing of differentials between the yields of German government bonds and other EU countries' government bonds to the actions of the ECB or the self-help efforts of Southern European nations. In fact, it notes that – "yield convergence continued even after the European Central Bank began reducing its balance sheet in late 2022. Evidence suggests that European Union funding programs played an important role in this process."

One might have expected that an ECB withdrawal from the bond market would trigger a significant rise in yields (as seen currently in the Japanese government bond market as the BOJ reduces its purchases). However, the gaps between yields of German government bonds and of other EU countries' government bonds has continued to narrow. Why is this? The GFSR points to the impact of the European Commission becoming a major and regular issuer of bonds across various maturities through the "Next Generation EU (NGEU)" framework, which was introduced in response to the pandemic. The analysis concludes that joint bonds (hereinafter "EU bonds") have strengthened perceptions of fiscal risk-sharing within the region and successfully alleviated concerns about the risk of default or the collapse of the euro area (which the GFSR refers to as "redenomination risk" associated with euro area countries returning to their former currencies). It is worth noting that the European Commission has adopted a "Unified Funding Approach" since 2023. Rather than issuing bonds specifically for the NGEU, it now issues them under a single "EU Bonds" brand, subsequently allocating the proceeds internally to such specific line items as the NGEU and macro-financial assistance. In other words, although the term "NGEU bond" is frequently encountered, there actually is no such thing as an "NGEU bond".

In any case, the GFSR's assessment appears correct, as the introduction of EU bonds has provided a partial solution to what has long been considered the euro area's greatest structural flaw – the existence of a unified monetary policy alongside fragmented fiscal policies – thereby helping to alleviate extreme concerns in financial markets, such as fears of sovereign defaults or the potential collapse of the euro area. In other words, the creation of EU bonds as a new class

of “safe assets” has provided a psychological pillar inspiring greater confidence throughout the euro area bond market. In this context, the GFSR presents empirical analyses showing a clear weakening in the correlation between asset swap (ASW) spreads (which reflect the credit risk of individual countries) and the Composite Indicator of Systemic Stress (CISS) calculated by the ECB. This suggests a reduction in the risk of shocks spreading (contagion) across the region and in the potential for the single-currency bloc to break apart (redenomination risk). This fact is further underscored by the disappearance of the “flight to safety” into German government bonds, which had previously consistently been seen during times of economic and financial shocks.

Concerns about Post-NGEU Period

The GFSR’s core argument is that promoting risk-sharing through joint bonds could serve as a tool to complement fiscal consolidation, but there is no mention whatsoever of the institutional sustainability of such an arrangement. The crux of the sustainability issue lies in the fact that the NextGenerationEU (NGEU) framework is a time-limited measure, with new borrowing and funding commitments set to conclude by the end of 2026. The more the GFSR emphasizes the merits of EU-issued debt, the more one worries about what will happen to the regional bond market when the joint-debt issuance mechanism is phased out. However, this point remains entirely unaddressed. The NGEU was created with a total envelope of EUR806.9 billion, and it was initially decided that the funds would be split roughly evenly between loans (requiring repayment) and grants. In practice, however, a significant imbalance has emerged, as such “core” EU members as Germany (which enjoy low sovereign borrowing costs) have opted not to apply for loans. Consequently, the grant portion has been fully utilized, while demand for loans has been concentrated primarily among Southern European countries (including Italy, Spain, and Greece). As a result, the NGEU’s approximately EUR360 billion grant component has been fully exhausted, but confirmed applications for NGEU loans stand at only about EUR213 billion, roughly 55% of the EUR385.8 billion available for loans. In other words, EU member states with problematically high debt levels have come to depend on NGEU funding to a disproportionate extent.

Given this, as the expiration of the NGEU framework approaches, there is a need to consider the potential impact of the eventual cessation of the substantial NGEU grants and low-interest loans that have been bolstering public investment and economic growth in Southern European countries. Shortfalls stemming from the withdrawal of NGEU funding will need to be covered by individual countries’ government bond issuance, which is expected to loosen the supply-demand relationship for Southern European countries’ bonds, but the GFSR avoids addressing this point.

EU Bond Retirement Over 30-Year Period

That said, the liquidity of EU bonds will not suddenly evaporate. To avoid placing an excessive burden on the EU (the European Commission) or any individual EU member state, the NGEU framework calls for the repayment of EU bonds to be spread out over the 30-year period from 2028 to 2058. To prevent repayment obligations from clustering around specific maturity dates, the European Commission employs a “laddered” issuance strategy for its benchmark bonds. Currently, the weighted average residual maturity of outstanding EU bonds is managed at approximately 12 to 13 years (with the largest issuance volumes concentrated in the 7–12 year maturity range, followed by the 3–7 year and 15–30+ year segments). Consequently, the influence of EU bonds on capital markets will not vanish overnight, and it is highly unlikely that there will be widespread shocks, such as a sudden substantial widening of the differential between German bond yields and the yields of other EU member’s government bonds. Furthermore, prior to the issuance of EU bonds under the NGEU framework, large-scale joint borrowing by the EU was widely considered legally impossible, as it was viewed as a violation of the no-bailout clause in Article 125 of the Treaty of Lisbon. The fact that a precedent has now been established should serve to curb speculative surges, which tend to intensify during times of crisis.

European Commission investor relations materials released this September[1] include a paper entitled “Continued Capital Market presence of the EU in 2028–2034” that notes that the maturing of NGEU-issued bonds will necessitate ongoing refinancing operations (amounting to EUR40–50 billion annually) and emphasizes that the European Commission will remain a major issuer in capital markets. Notably, between 2026 and 2030, plans call for approximately EUR30 billion per year (totaling EUR150 billion) of EU joint bonds to be issued to fund Security Action For Europe (SAFE) defense-related loans. This suggests that the “joint procurement for defense spending” concept advocated in the Draghi Report and elsewhere is now in the process of being realized.

In any case, the current plan is to gradually reduce the outstanding balance of NGEU-issued bonds during the period from 2028 to 2058 by refinancing existing debt to extend maturities, while simultaneously making net repayments each year to the extent that can be covered by budgets and thereby ensuring the avoidance of major market shocks. Even after the new debt issuance phase concludes, the market depth provided by existing EU bonds (totaling approximately EUR800 billion) will persist for some time and serve as a reassuring factor. That said, from financial markets’ perspective, the gradual disappearance of what have become “euro area common safe assets” by 2058 is not ideal, nor is it desirable from the standpoint of the EU’s capital markets union aspirations. While it is unlikely that a complex challenge with a nearly 30-year time horizon will be resolved immediately, one can only hope that constructive discussions will begin and progress as soon as possible.

[1] European Commission, “EU Investor Presentation (Investing in EU-Bonds & EU-Bills)”. Sep. 29, 2026

Structural Comparison of Current NGEU (2021–2026) and Next MFF (2028–2034)

** Changes in the scale of joint borrowing, forms of support, and repayment policies*

Items	Current: NGEU (2021–2026)	Next: Proposed MFF (2028–2034)	Market/Financial Structure Changes and Implications
Basic Functions/Positioning	"Temporary and time-limited" emergency framework for pandemic recovery (based on Article 122 of Treaty of Lisbon, etc.)	**"Quasi-permanent and policy-driven" fund mobilization mechanism integrated into the MFF (Multiannual Financial Framework)**	Qualitative shift from "exceptional measures" to "permanent European joint procurement tool"
Total Borrowing /Issuance Scale	Total Envelope: Approx. EUR806.9 billion (Actual Disbursement: Approx. EUR573.0 billion: Grants EUR360.0 billion + Loans EUR213.0 billion)	**New Proposal: Over EUR650 billion (Catalyst: EUR150 billion, Crisis: EUR400 billion, Ukraine, etc.) + SAFE Defense: EUR150 billion**	If full amount approved, fundraising capacity equivalent to NGEU to be maintained; but highly likely to be scaled back during negotiations
Primary Support Format	A hybrid of grants (non-repayable aid) and loans (historically, grants account for approx. 63% of total funding)	**Primarily "loans" (policy-based lending) are the main component, crisis response also centered on loan facilities backed by guarantees**	Shift to lending model (member states responsible for repayments) to mitigate opposition from "frugal" states regarding grant allocations
Market Issuance Structure	Single-brand issuance of "EU-Bonds" under Unified Funding Approach	**Continued regular auctions and syndications of "EU-Bonds" and "EU-Bills"**	Unified issuance brands and settlement infrastructure enable stable SSA market liquidity benchmarks
Refinancing/Rollovers	Primary focus on new issuance (utilizing issuance quota for EUR80 billion in second half of 2026 and then annual pace of EUR180 billion)	**Standardized refinancing (rollover) issuance of EUR40–50 billion annually**	Decelerating pace of net new issuance, but refinancing demand prevents "EU bonds" from disappearing from market
Redemption/Repayment Deadlines	Full-scale repayments from 2028, with repayments completed in full by end of December 2058	**Gradual net redemptions from 2028 funded by EU budget (own resources) and repayments by member states**	Net redemptions in parallel with rollovers from 2028 cause outstanding balance to shrink in absence of new issuance
Impact on South-European Sovereign Spreads	Work with PEPP/TPI to greatly narrow South-European government bonds' ASW spreads and stem flight-to-safety selling into German Bunds	**Adoption/nonadoption of new framework to determine effectiveness of measures to contain risk of spreads rewidening**	Significantly scaling back of new framework presents risk of renewed funding pressures on South-European finances due to withdrawal of NGEU grants

(Source) European Commission, etc.; prepared by the Global Foreign Exchange Department, Mizuo Bank

Pivotal Potential of EU's Next Multiannual Financial Framework

The Draghi Report and various EU entities have persistently advocated making EU bonds a permanent source of funding for defense spending and such projects as those for decarbonization and industrial competitiveness enhancement. However, such "frugal" member states as Germany and the Netherlands continue to favor fiscal austerity and remain resistant to the permanent establishment of common EU debt instruments. Although new disbursements under the NGEU framework are set to cease (in 2026) during the next Medium-Term Financial Framework (MFF) period (2028–2034), adjustments are underway to effectively institutionalize the issuance and secondary market for EU bonds by rebranding them under such new labels as defense, Ukraine reconstruction, industrial investment (Catalyst Europe), and crisis responses. In particular, the attempt to institutionalize EU bonds by framing them as a "crisis response" mechanism is poised to become a major point of contention in international finance, and it is a development that warrants close attention.

For example, the Catalyst Europe industrial investment promotion program (with a funding capacity of up to EUR150 billion) is viewed as successor to the NGEU's Recovery and Resilience Facility (RRF), which is considered to be a successful model. This framework would function as a policy-lending instrument, through which the EU raises funds in financial markets and provides low-interest-rate loans to member states and regions for priority investments and structural reforms focused on such themes as the green transition, digitalization, and industrial competitiveness. The balance between loans and grants was a major point of friction during the creation of the NGEU, but current discussions are proceeding with the understanding that loans will be the primary form of support, and this understanding is expected to make reaching a consensus among member states relatively straightforward. Nevertheless, negotiations over which economic sectors are eligible for strategic investments and the extent to which "conditionality" (structural reform requirements) should be imposed are likely to remain difficult.

Separately, a crisis response mechanism with a funding capacity of up to EUR400 billion is being proposed as a permanent framework designed to rapidly mobilize financing in the event of such unforeseen shocks as those stemming from pandemics, energy crises, and geopolitical upheavals. This is an ambitious proposal designed to make EU bonds permanent, but the extent to which Germany and other "frugal" EU states will be willing to compromise on such a proposal remains to be seen. Realistically speaking, the EU can no longer afford to hesitate on this issue if it hopes to compete financially with the United States and China, and given that Germany's influence appears to be waning, the EU's internal disputes on this issue going forward may not be as intense as they once were. An agreement must be reached by the end of 2027 to ensure the new medium-term budget takes effect in January 2028, so in this sense, the year 2027 may be considered a major pivot point determining the EU's future development course.

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