Mizuho Brief: US Tariffs & FX

Economics & Strategy | Asia ex-Japan

11 August 2025 |
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"Pay-to-Play" US Extortion & Attendant Risks

In a Nutshell:

- The **widening "pay-to-play" imposition** of US trade/tariff policies suggests a **heavier toll extracted on US trade partners** and the **private sector** at large.
- Nvidia and AMD having to pay 15% of revenues to the US on exports of chips to China is the **latest, but perhaps not the last, iteration** of "play to play" US extortion.
- As discussed before, this **extraction via imposed US imports and/or investments** (into the US) will hit as ***compromised Current Accounts*** and ***increased fiscal burden*** elsewhere.
- In addition, it will inevitably entail **some combination of profit margins and household income/savings confiscated** by the US government.
- The imposition of export levies on chips (to China) threaten **to intensify industrial deflationary pressures for China**, in turn raising the bar for Beijing's anti-involution measures to snap deflation.
- To the extent that Chinese producers export higher costs, **stagflation-type dilemma will mount elsewhere as higher prices collide with negative demand pressures**.
- Why USD May Not Crash Imminently: Perversely, "*Pay (to Play) America" offsetting "Sell America"* could in fact backstop USD decline for now (at notable risk of CNH pressures and AXJ downside), although longer-term USD standing is harmed by eroded trust.

- The **"pay-to-play" US trade extortion continues to widen**. And brazenly so, as it **takes on an extraterritorial dimension**.
- In its latest iteration, which is ***tragically not likely to be the last***, **chipmakers Nvidia** and **AMD are to pay (to the US government) 15% of revenues from chips sales to China**. This effective export levy is so as to secure requisite export licenses.
- In a note* from July, we characterized the *lop-sided* and ***disadvantageous trade deals with the US as*** effectively being ***"pay-to-play" US trade policies*** **being forced on the world** at pain of (even more) debilitating tariffs.
- Specifically, as it pertained to " … ***highly extractive*** **US**(-imposed) ***trade deals*** the **require trade partners literally pay for the benefit of US trade** … *by way of guaranteed US imports* (energy, farm, aircraft, etc.) and/or *investments*.
- And as surmised then, "the resulting **conspiracy of tariffs and "pay-to-play" extractive trade deals** will almost certainly **impose cost** (to trade partners) **via compromised Current Accounts** and/or **increased fiscal burden** …".
- This continues to remain the case. Fact is, **US tariffs/levies/impositions** are *ultimately transfers to the US government* **at the expense of producers** (**profits**), **consumers** (**household income/savings**) and **other governments** (**fiscal resources**).

- In addition, **"pay-to-play" US trade policies making landfall elsewhere as higher costs**, as is the **case with chips to China**, will inevitably **accentuate deflation risks in China** and **stagflation-type of dilemma elsewhere**.
- Specifically, **if Chinese firms are forced to eat into already distressed margins** amid competition and additional costs (e.g. 15% chips surcharge) passed on, it could ***exacerbate China's already problematically entrenched industrial deflationary pressures***.
- This will **heighten the challenge for Beijing to successfully implement its "anti-involution" policies** aimed at snapping widening/entrenching deflation risks.
- And **to the extent that China may be able to export higher costs**, the **resultant inflation** will land ***elsewhere, inconveniently showing up as stagflation-type dilemma*** **amid coincident negative demand pressures**.

  - Why USD May Not Crash Imminently: Perversely, such **forced transfer**, or ***confiscation***, of private sector/trading partner resources is one reason **why the Greenback may not crash imminently**. Especially *as "Sell America" is checked by "Pay(to Play) America"*.
  - But Risks USD May Not Crash Imminently: Although inevitable, possibly irredeemable, **loss of trust enlarges risks to USD and its standing** (as the global reserve currency) in the **longer-run**.
  - Watch CNH & Attendant AXJ Risks: Mounting pressures on China, regardless of signs of reciprocal tariff risks being assuaged, could **dampen CNH and increase downside risks**. Accordingly, **AXJ** will be **vulnerable to bouts of further "Pay (to Play) America" risks**.