



# Outlook for Japanese Stock Market & Economy

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-March 2025-



Sumitomo Mitsui DS Asset Management



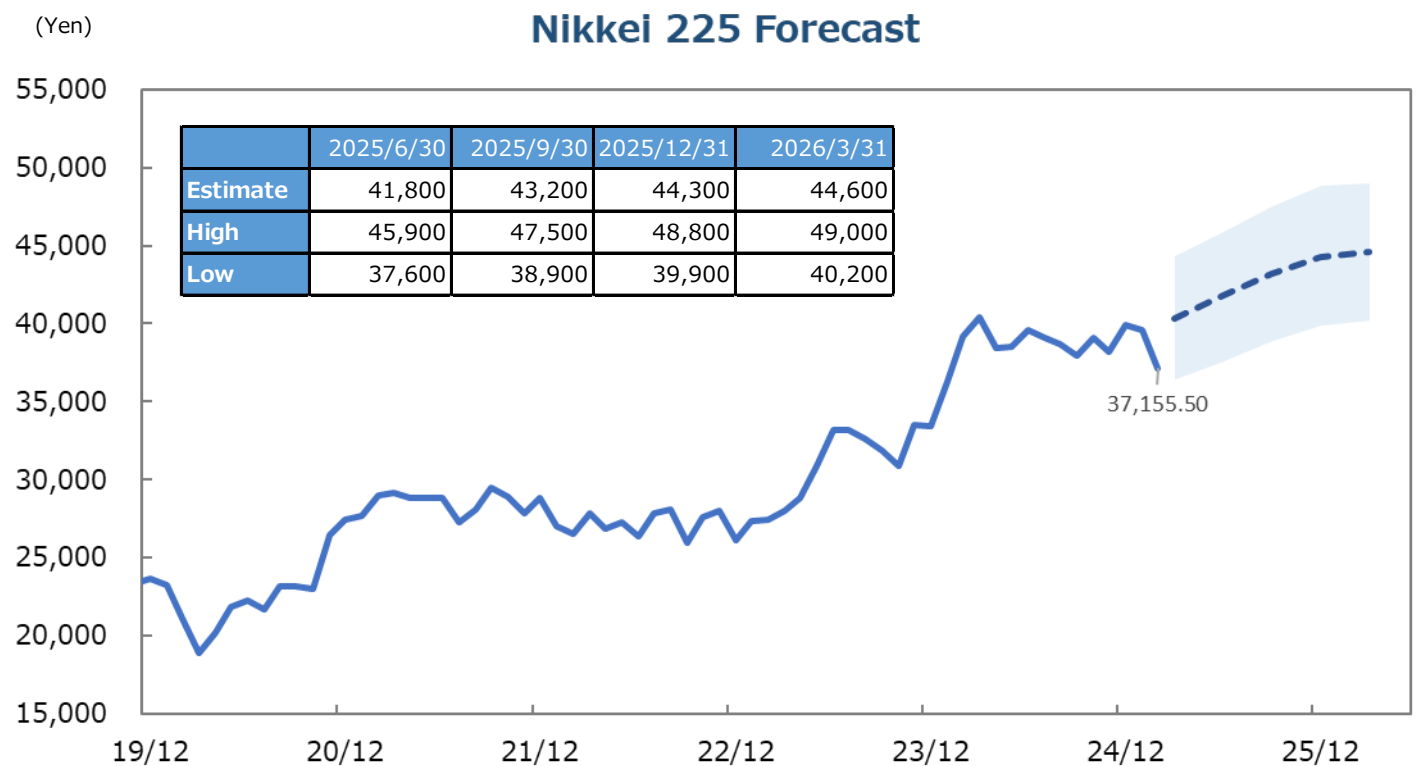
# Outlook for Japanese Stock Market

## Market Outlook

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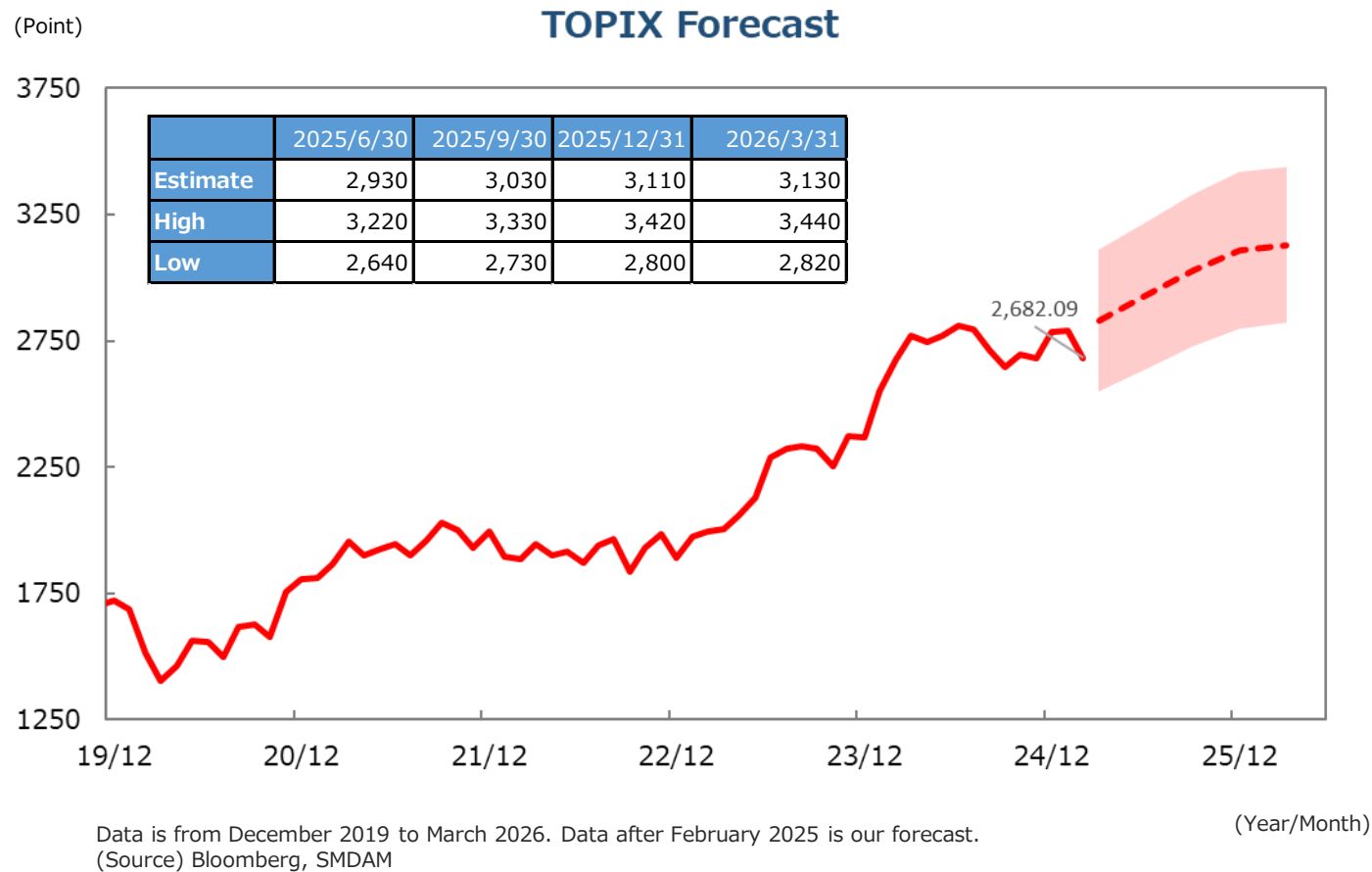
- We expect the Japanese stock market to break out of its current trading range towards the north once the uncertainty over the U.S. economic policies subsides, especially regarding “Trump tariffs”.
- We are bullish on Japanese stocks due to the steady progress of the Japanese economy, with rising wages and prices, improving corporate governance, and aggressive share buybacks.
- We have slightly lowered our target price of the Nikkei 225 as of the end of 2025, from 45,400 to 44,300, due to the changes in the FOREX market forecast.
- While concerns about a rate hike by the Bank of Japan weigh on the stock market, we expect the market will resume its long term bullish trend once the positive aspects of Japan's economic normalization, from deflation to mild inflation, are better understood.

# We see bullish perspective of Japanese equity

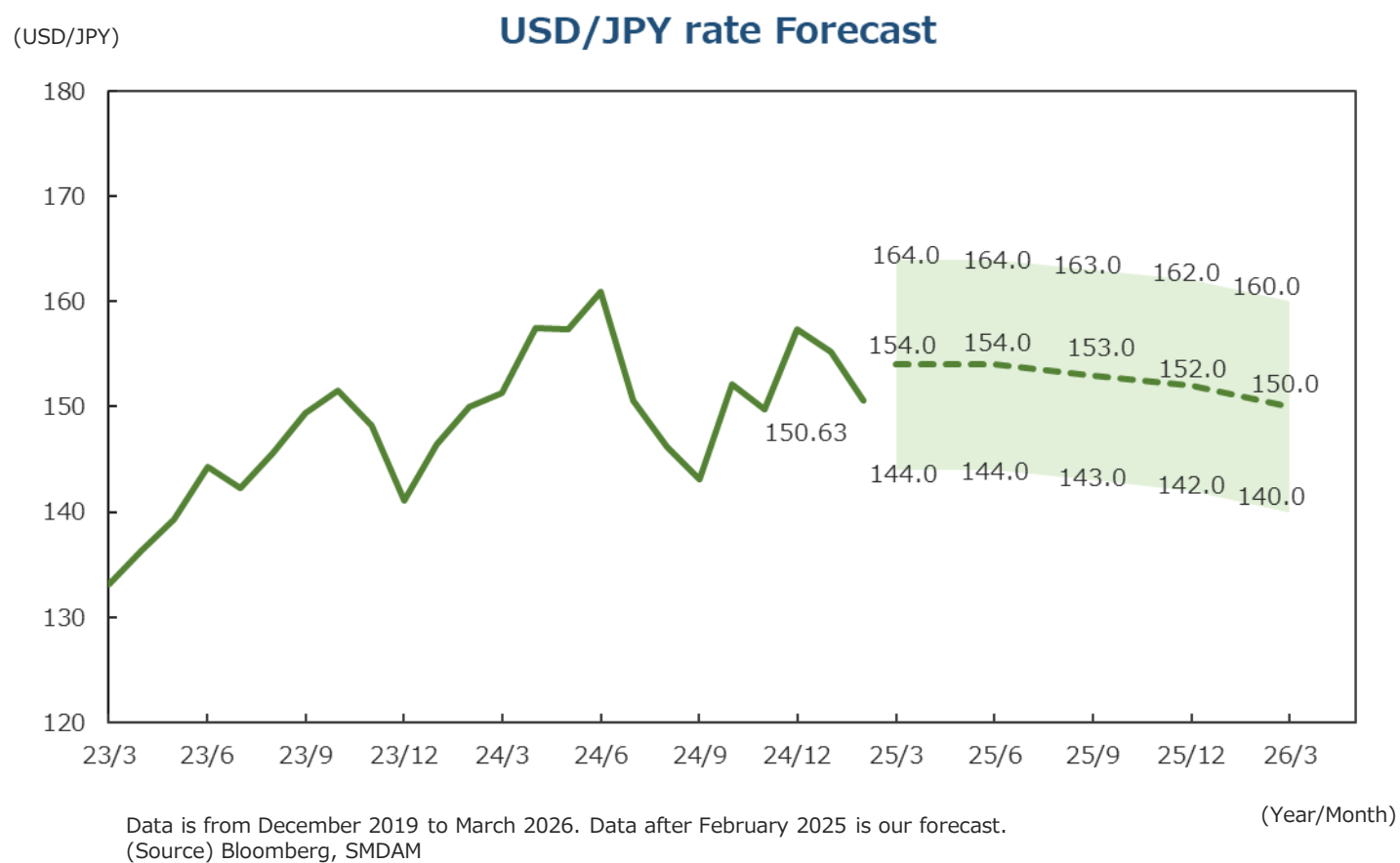


Data is from December 2019 to March 2026. Data after February 2025 is our forecast.  
(Source) Bloomberg, SMDAM

# We see bullish perspective of Japanese equity



# Narrowing interest rate gap weigh on USD/JPY rate



# Upside / Downside risk scenarios

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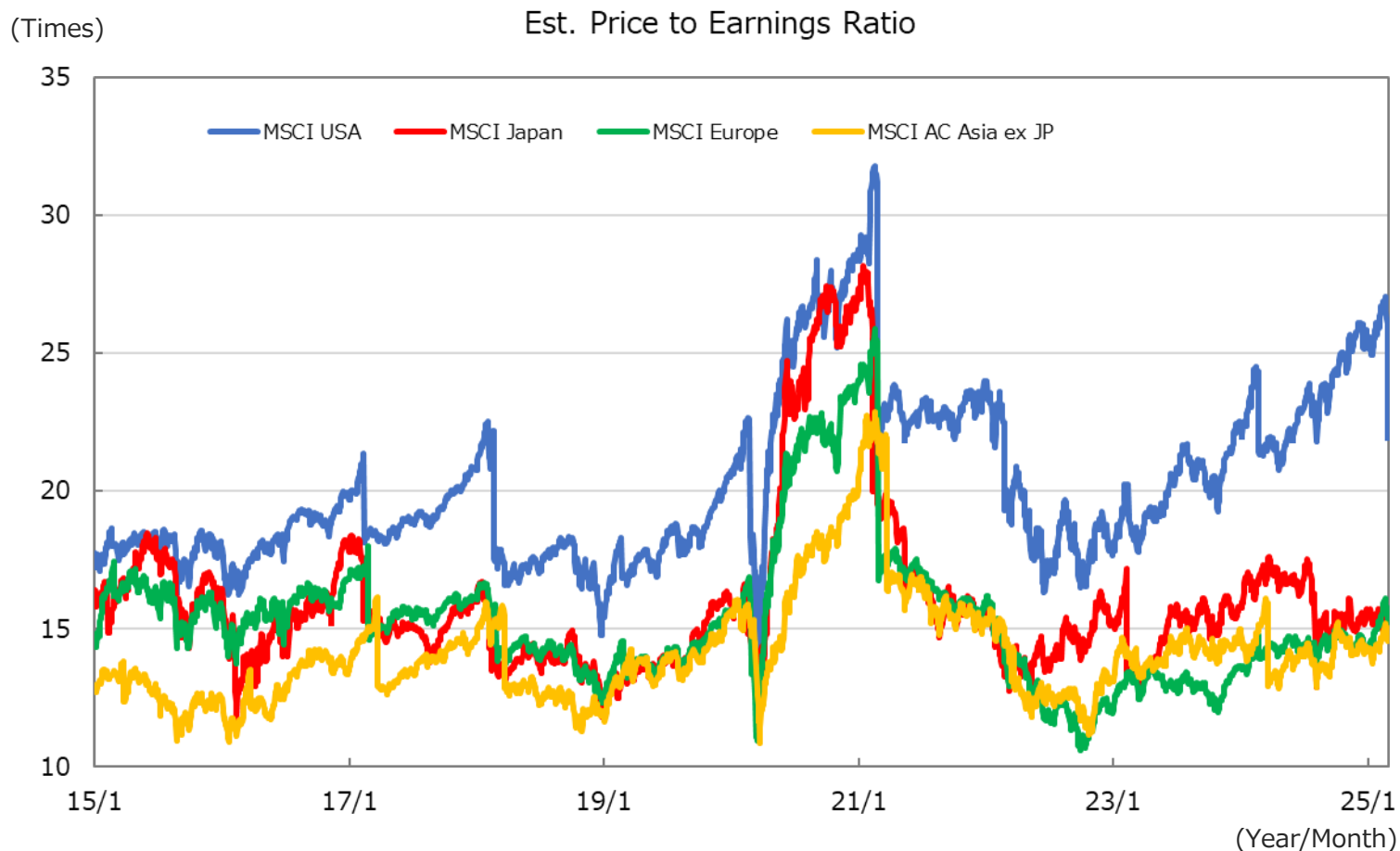
## ■ Upside Risks

- An increase in the terminal rate of economic growth due to the end of deflation
- Further improvements in corporate governance, driven by the Tokyo Stock Exchange

## ■ Downside Risks

- A slowdown in wage increases
- Excessive and rapid appreciation of the JPY
- Stagnation in the business cycle of the manufacturing sector

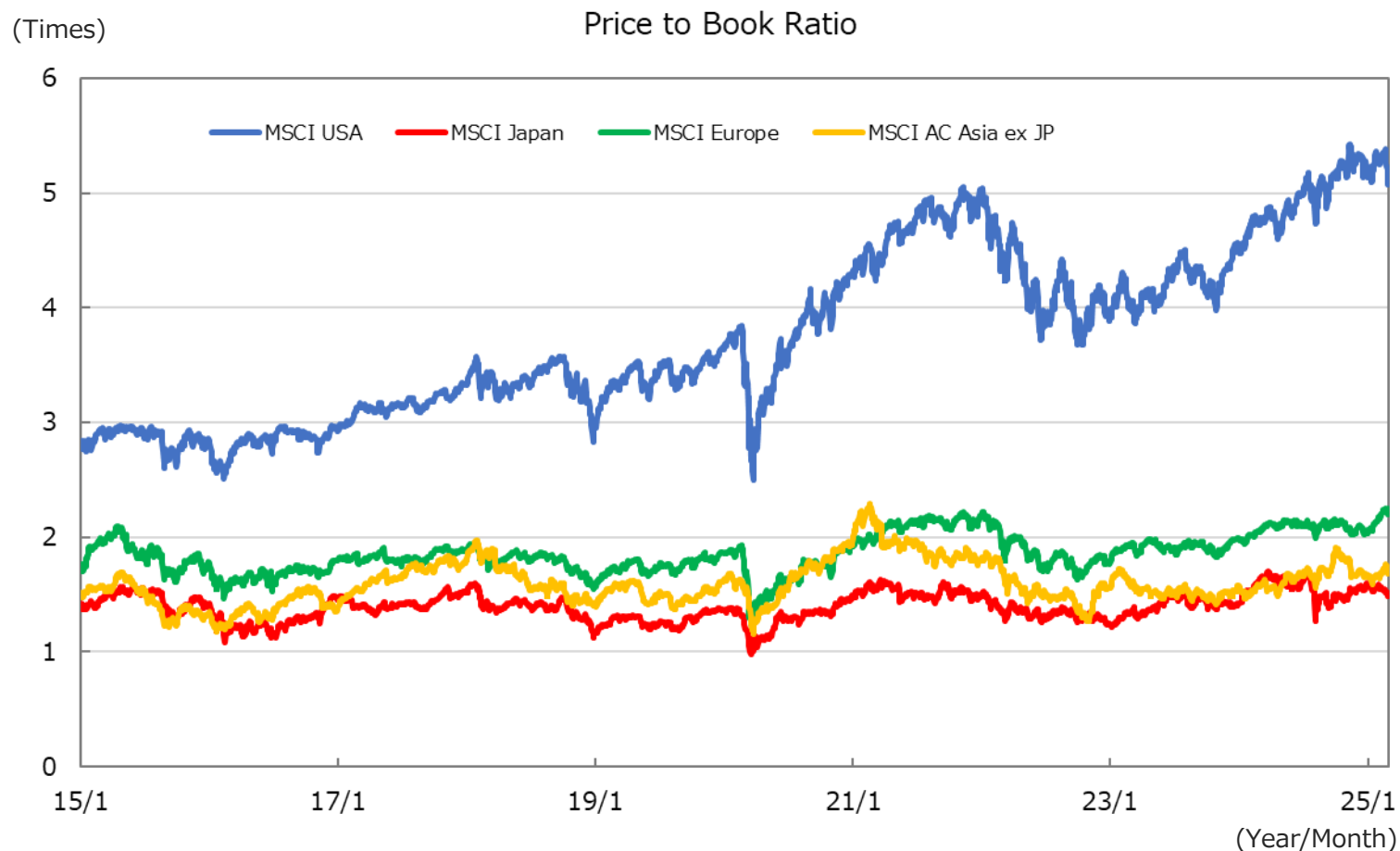
# P/E ratio has fairly valued steady earnings growth ahead



Data is from January 2015 to February 2025.  
(Source) SMDAM, Bloomberg

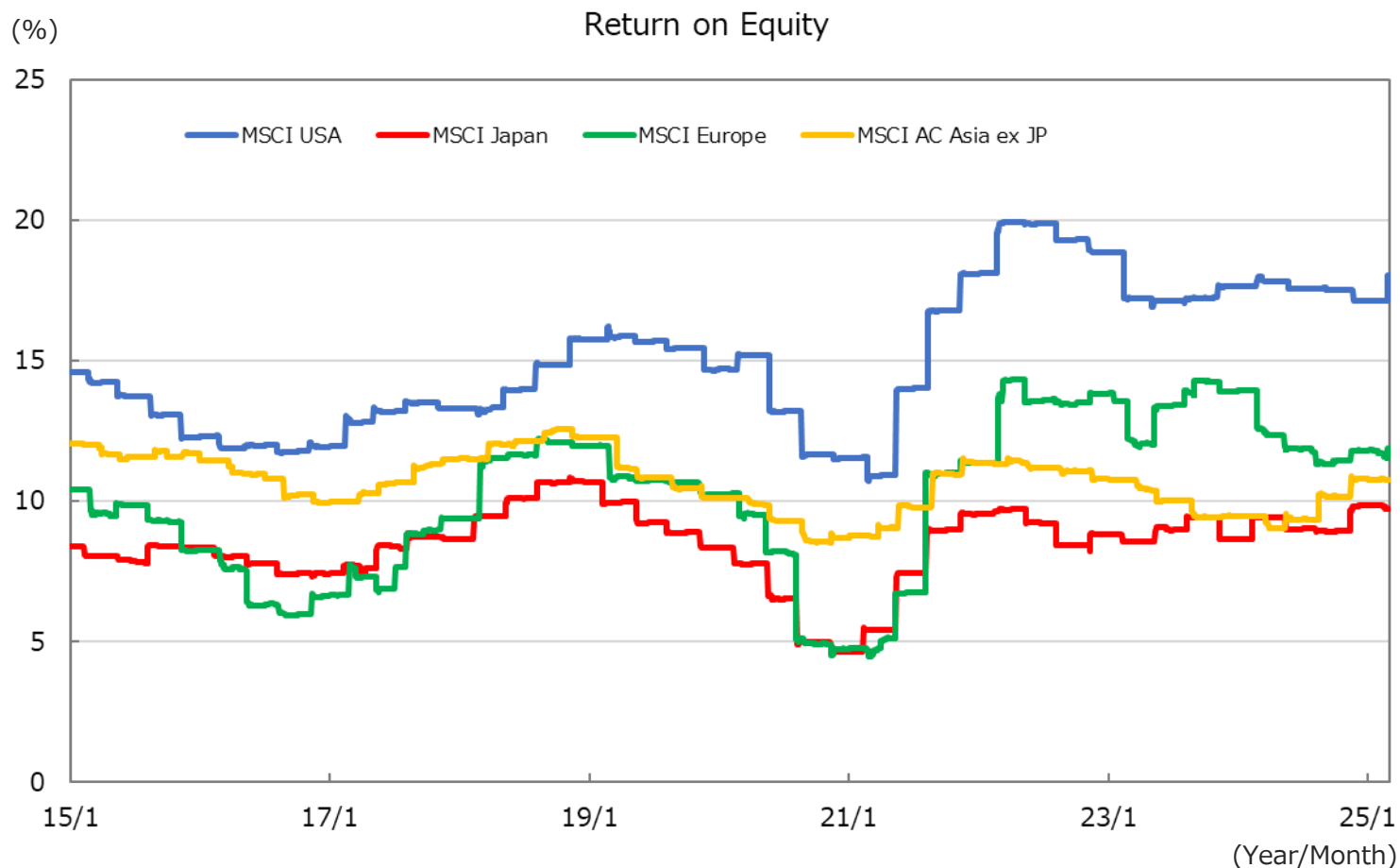


# Japan's Price to Book ratio lags behind global peers



Data is from January 2015 to February 2025.  
(Source) SMDAM, Bloomberg

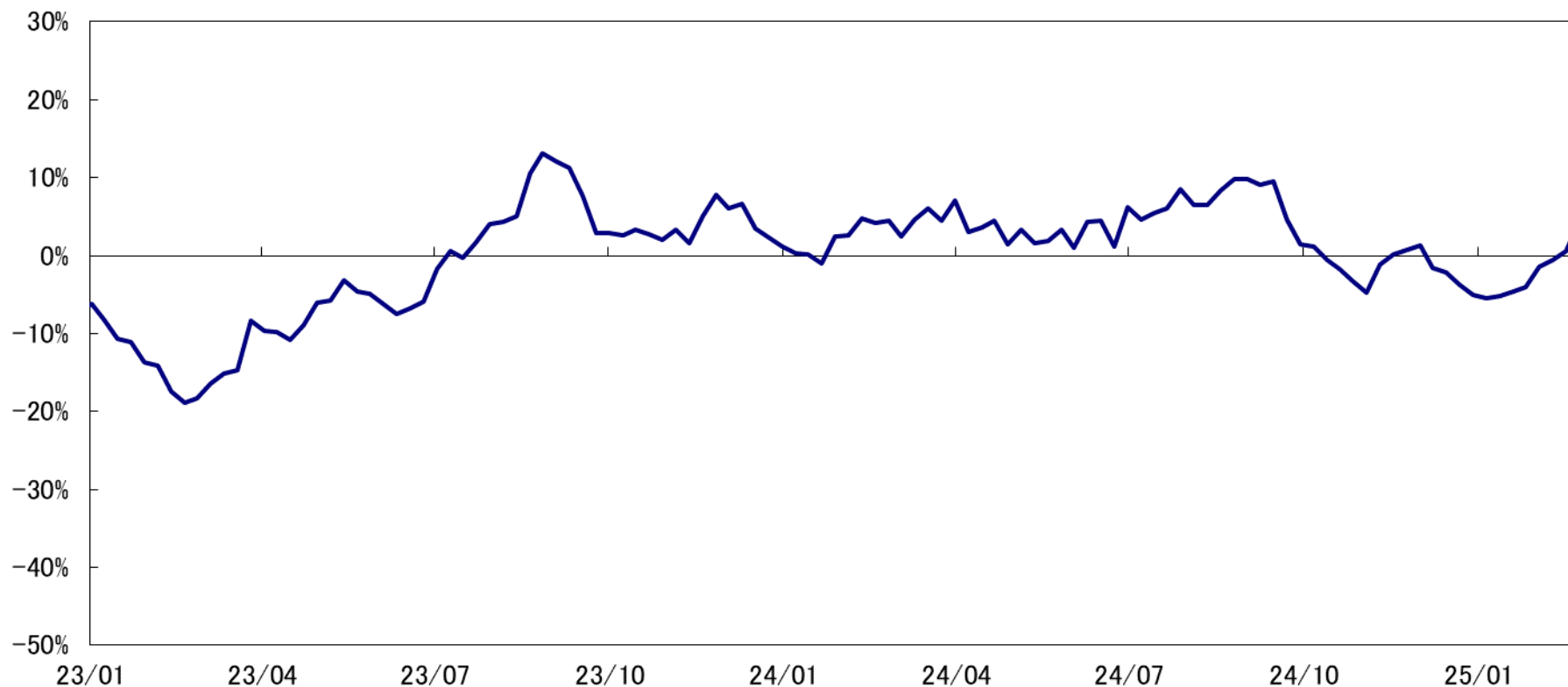
# Earnings growth boosts Japan's ROE closer to double digits



Data is from January 2015 to February 2025.  
(Source) SMDAM, Bloomberg

# EPS revisions turned positive despite global political turmoil

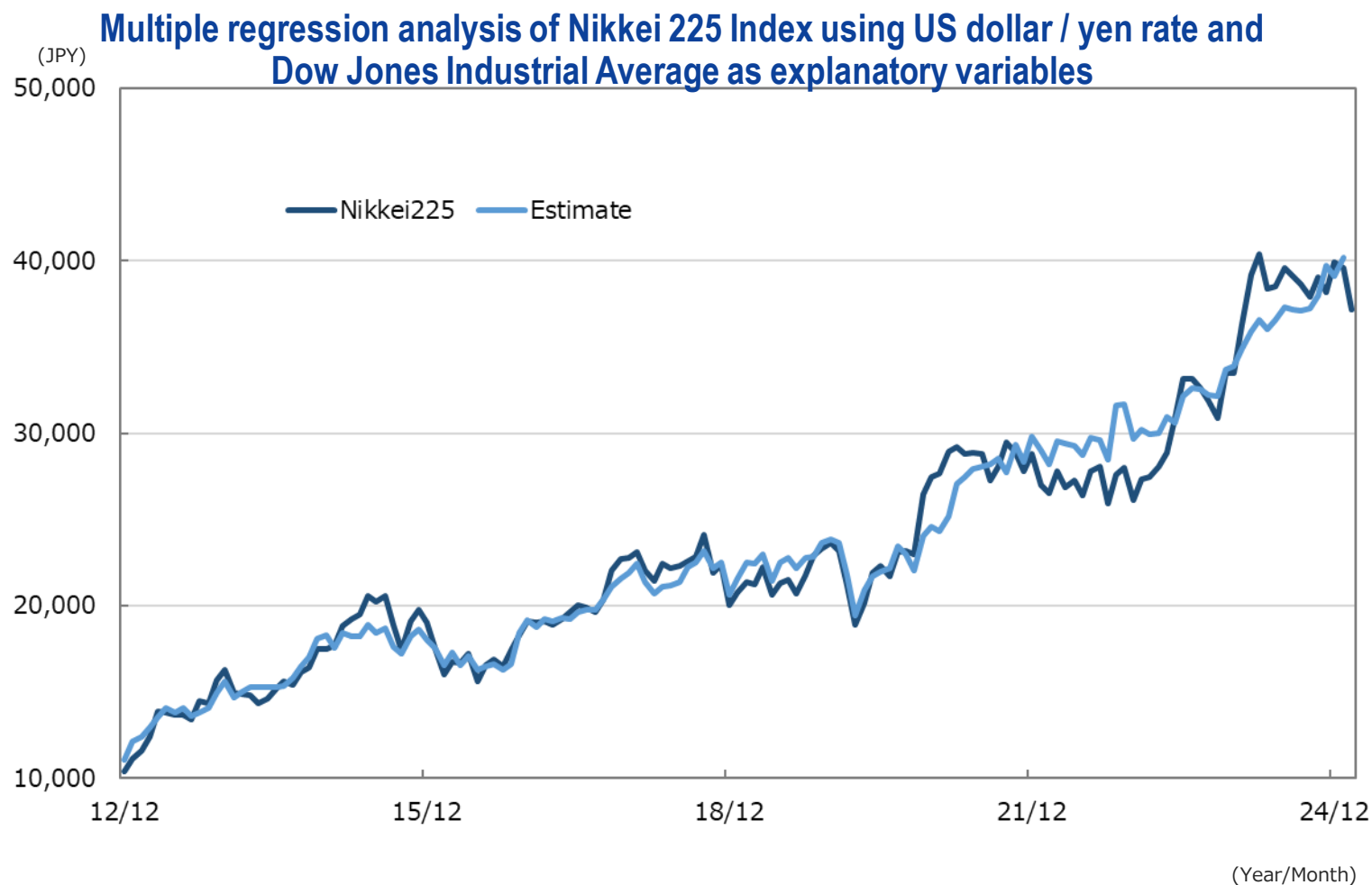
TOPIX EPS Revision Index



Data is from January 5th 2023 to February 27th 2025  
(Source) Datastream, IBES

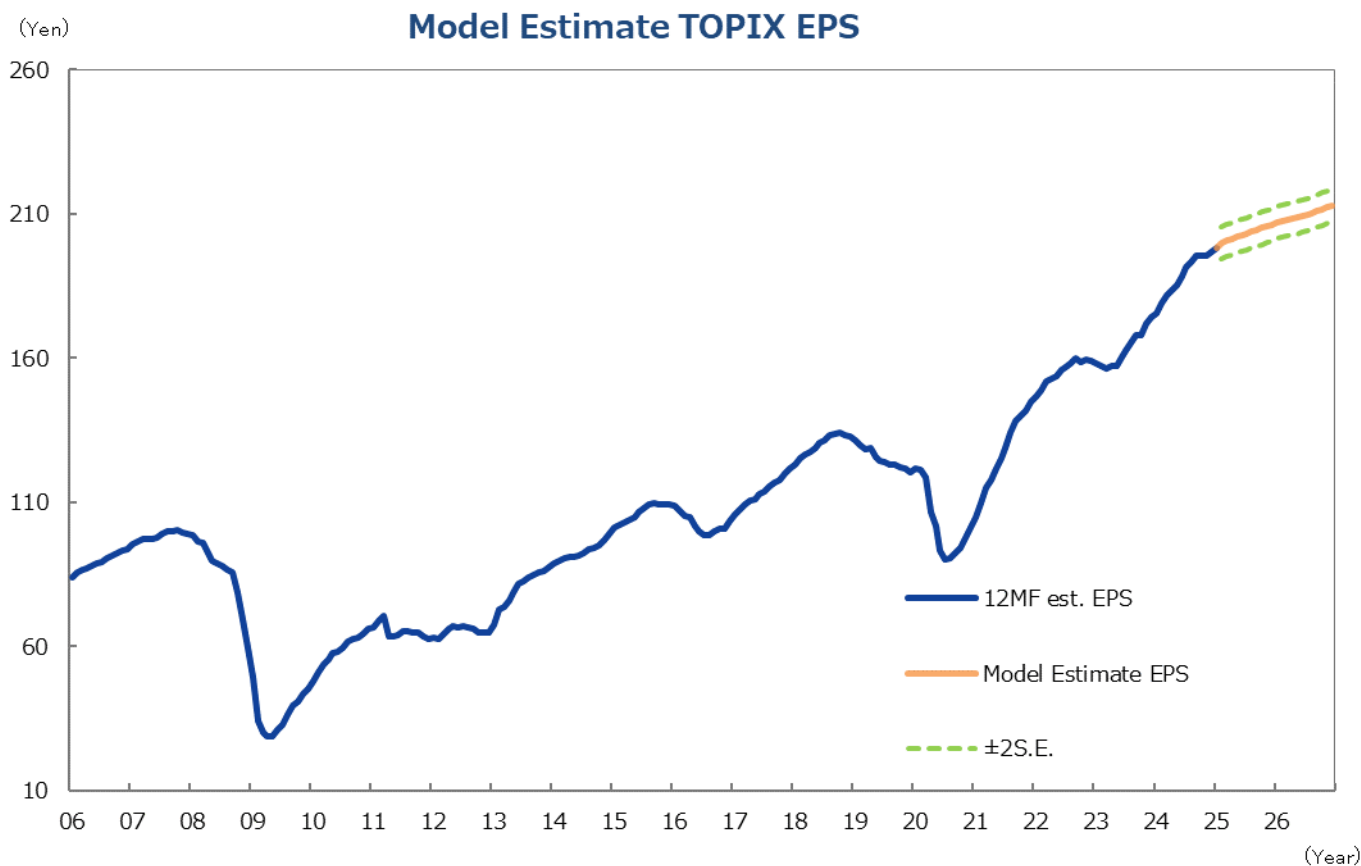
(YY/MM)

# Nikkei 225: 5% below fair value, one Standard deviation away



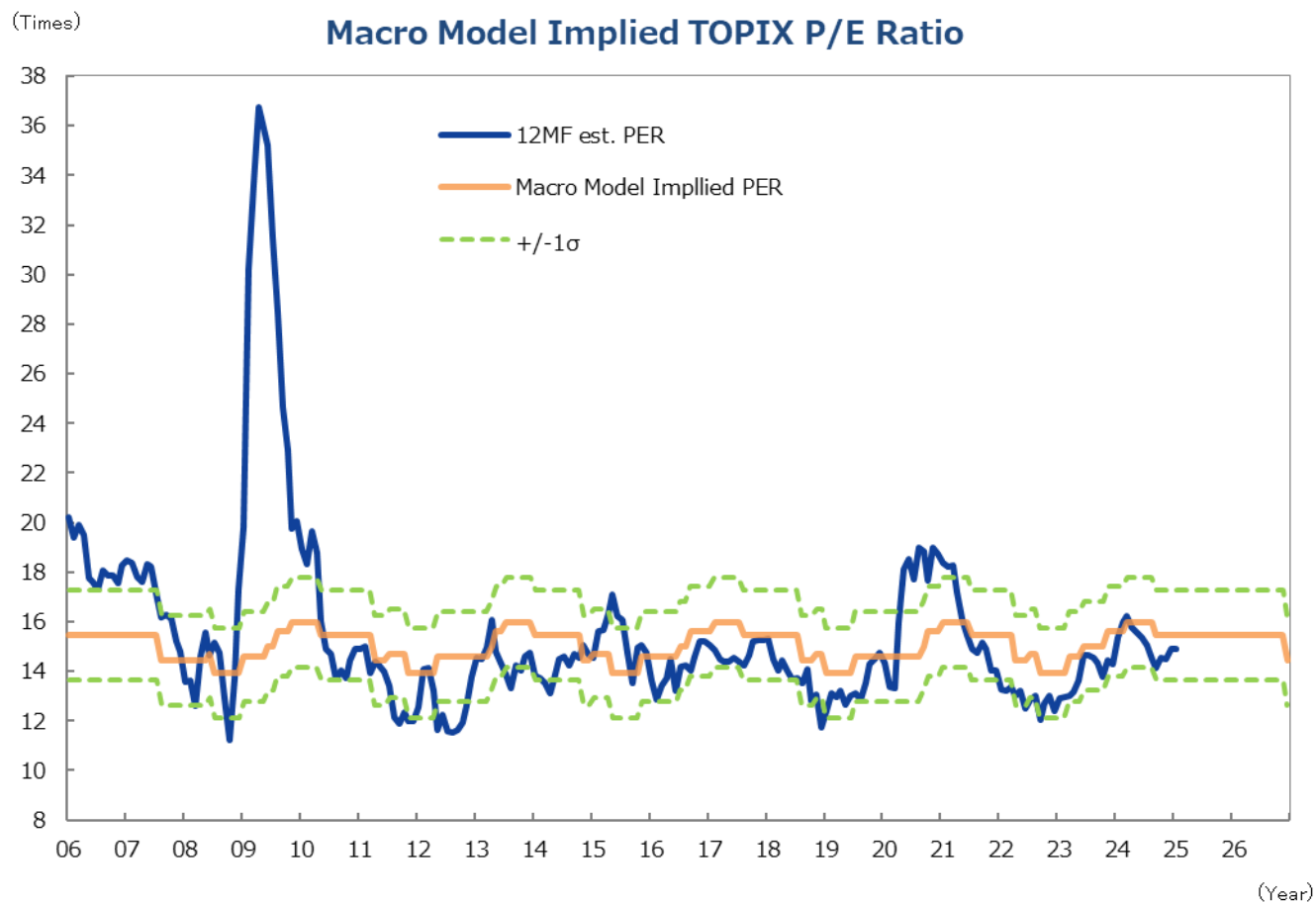
Data is from December 2012 to February 2025.  
(Source) SMDAM, Bloomberg

# Quant model suggests EPS will maintain upward trend



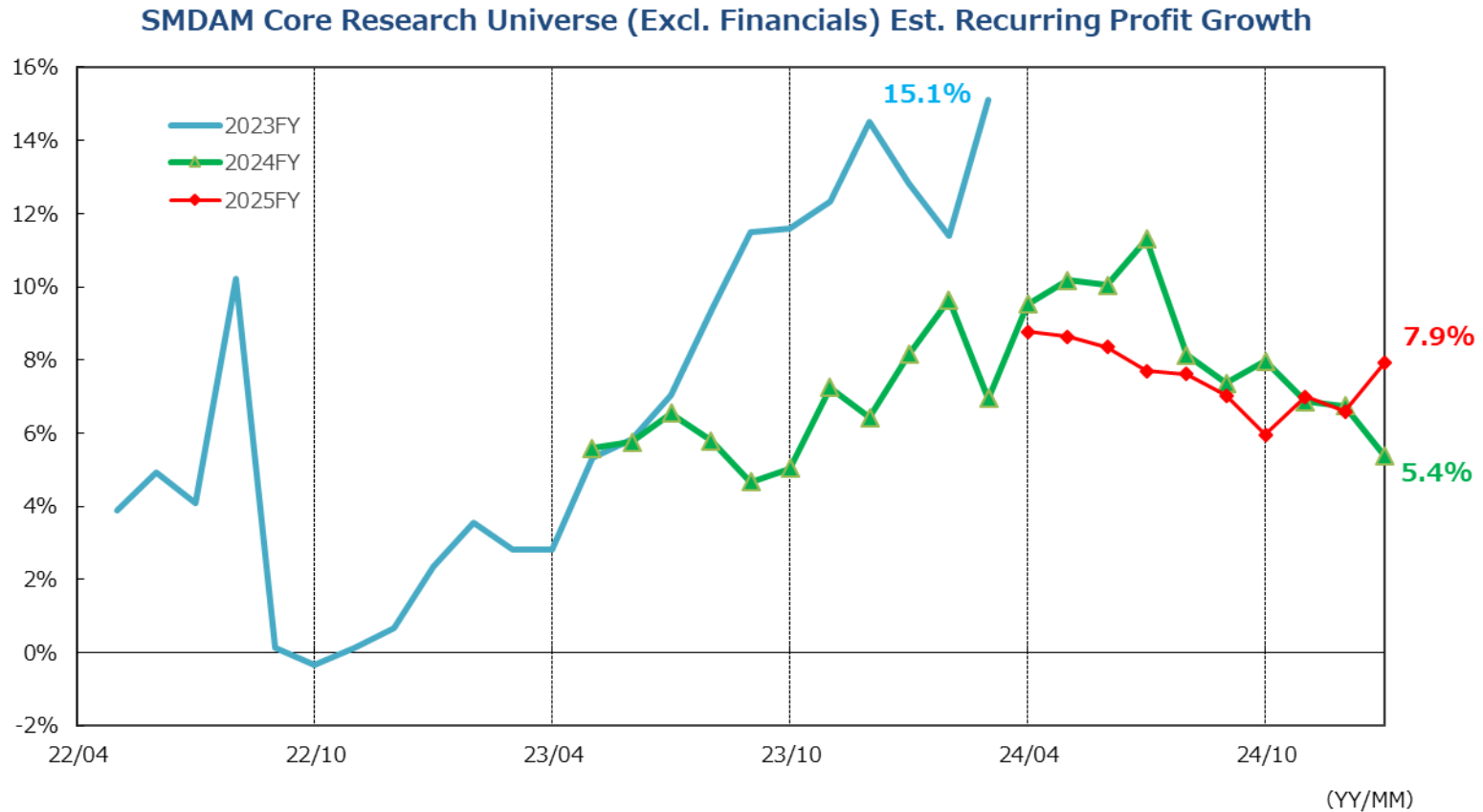
Note: Consensus data is from January 2006 to January 2025. Model estimate Data is from February 2025 to December 2026.  
Source: SMDAM

# TOPIX is currently trading with an attractive P/E ratio



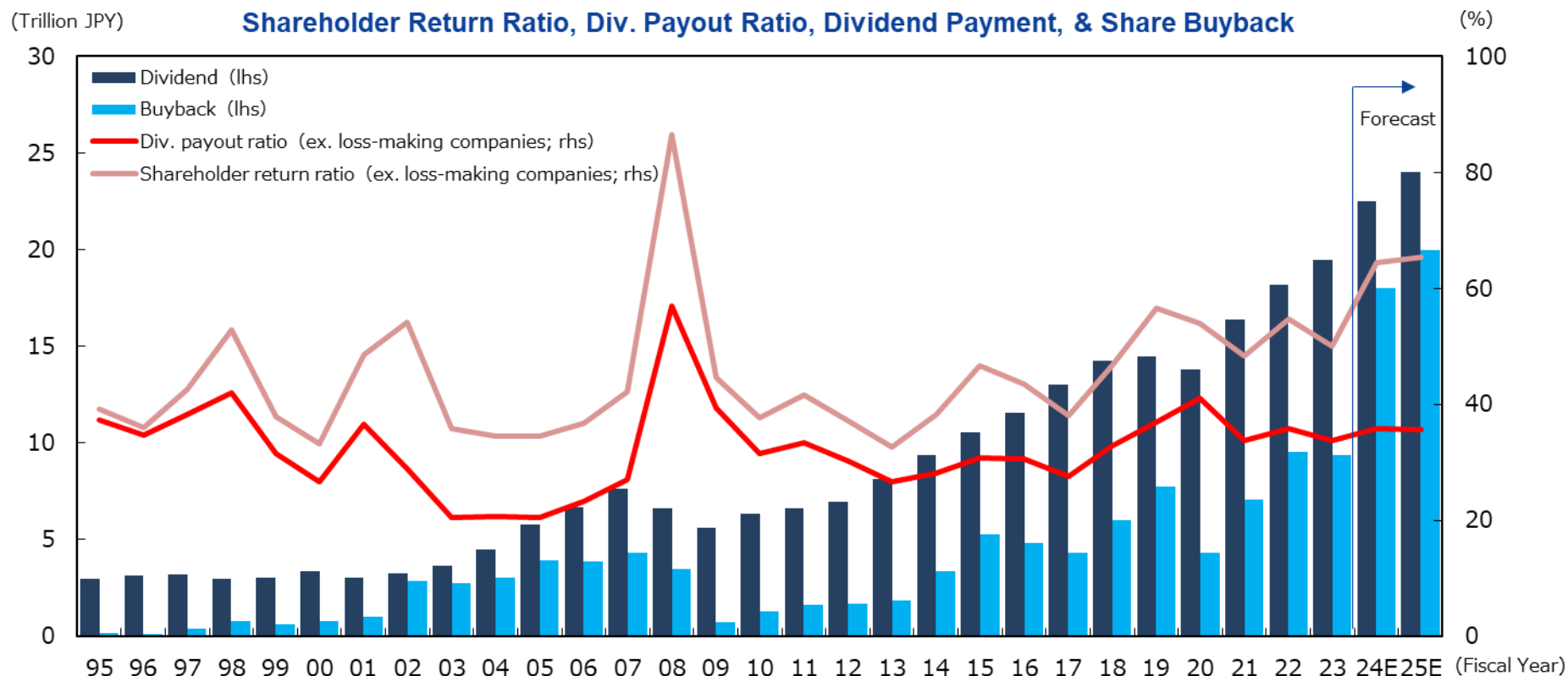
Note: Consensus data is from January 2006 to January 2025. Model estimate Data is from December 2006 to December 2026.  
Source: SMDAM

# SMDAM analysts expects steady earnings growth ahead



Note: Data is as of 12th February 2025, SMDAM Core Universe (Excl. Financials) consists of 398 Japanese companies covered by SMDAM in-house analysts.  
Source: SMDAM

# Streak of record-breaking dividends and share buybacks



Note: Data is from FY1995 to FY2025. FY2024 and FY2025 are forecasts by Daiwa Securities.  
Source: Toyo Keizai, Quick, INDB, Daiwa Securities, SMDAM



# Value is king in Japan from short to long term

## Performance Comparison of Russell/Nomura Style Indices

Index	Returns(%)						
	3 Month	6 Month	YTD	1 Year	2 year	3 Year	5 Year
<b>RN Japan Equity</b>	<b>-0.25</b>	<b>-0.28</b>	<b>-3.64</b>	<b>0.68</b>	<b>35.05</b>	<b>42.82</b>	<b>78.69</b>
Total Value	1.75	3.09	-2.45	4.41	46.36	63.26	100.08
Top Cap Value	0.32	3.20	-5.13	2.11	54.17	74.46	122.19
Large Cap Value	1.76	2.99	-2.53	3.98	48.02	65.59	104.00
Mid Cap Value	3.39	3.07	0.48	6.17	41.12	55.53	83.64
Small Cap Value	1.72	3.39	-2.10	6.32	38.81	52.97	82.96
Micro Cap Value	2.54	3.24	-1.58	5.91	35.34	49.71	78.33
Total Growth	-2.31	-3.47	-4.89	-2.80	24.67	25.17	57.72
Top Cap Growth	-3.67	-4.62	-6.41	-3.99	28.73	28.08	64.06
Large Cap Growth	-2.15	-3.51	-4.83	-2.58	26.81	26.96	61.14
Mid Cap Growth	1.44	-0.78	-1.09	0.74	24.08	25.60	56.55
Small Cap Growth	-3.61	-3.09	-5.30	-4.67	8.23	11.29	30.98
Micro Cap Growth	-3.69	-6.20	-4.85	-11.23	0.32	6.34	25.78
Top Cap Total	-2.02	-1.59	-5.87	-1.59	39.13	46.58	86.62
Large Cap Total	-0.26	-0.51	-3.72	0.44	36.51	44.03	81.36
Mid Cap Total	2.60	1.40	-0.15	3.76	33.14	40.80	75.08
Small Cap Total	-0.17	1.02	-3.22	2.12	26.52	35.55	62.43
Micro Cap Total	0.54	0.16	-2.60	-0.04	22.97	33.79	60.87

Note : As of 28th February 2025  
(Source) Bloomberg





## Outlook for Japanese Economy



# Current status & Outlook of Japanese economy

## [Current Status]

- **The economy is recovering.** While statistics related to consumer spending are mixed, CAPEX remains steady in areas such as software, capital goods and total supply, according to the Bank of Japan's "Tankan" economic survey. Additionally, exports, which had slightly declined in January, are also recovering. So far, the growing uncertainty over the US economic policies has had a limited impact on the business sentiment in Japan.
- **Inflation is on an upward trend.** Nationwide core CPI rose by +3.0% YOY in December, up from +2.7% in November, and the Tokyo Metropolitan Area core CPI rose by +2.5% YOY in January, up from +2.4% in December. The rise in both Nationwide and the Tokyo Metropolitan Area core CPI was mainly driven by energy prices, following the reduction of government emergency measures implemented to cope with the extreme heat in summer. Additionally, cost-push pressure from the depreciation of the JPY in FOREX market and rising rice prices also contributed to the upward trend.

## [Outlook]

- ① **While we have raised our real GDP growth forecast for FY 2024 from +0.5% to +0.8% and for FY 2025 from +1.0% to +1.3%, we have maintained our estimate for FY 2026 at +0.9%.** We maintain our expectation that the Japanese economy to continue its moderate growth trajectory, supported by wage increases, a steady appetite for CAPEX (such as labor-saving, digitalization, greening, urban development, and construction of semiconductor factories), economic measures, and the resilience of overseas economies.
- ② **We have raised core CPI forecast for FY 2024 from +2.6% to +2.7%, that for FY 2025 from +2.2% to +2.6%, and that for FY2026 from +1.9% to +2.0%.** The upward revision is mainly due to changes in the assumption of FOREX market and a hike in food prices. Looking ahead, we expect the JPY to appreciate gradually and cost-push pressure from import prices to ease. Additionally, we assume rice prices will correct their recent excessive rise and stabilize gradually, thanks to the Japanese government's release of stockpiled rice. On the other hand, inflation will likely remain stable due to rising service prices driven by wage hikes. We forecast core CPI to decelerate slightly but still maintain a momentum of around +2.0% YOY.
- ③ **We expect the government to adopt accommodative fiscal policies.** Prime Minister Ishiba focuses on completely combating the long-lasting deflation of the past few decades. In November, the Cabinet approved a comprehensive economic measure aimed at "ensuring people's safety and security and sustainable growth." Regarding tax cuts, an agreement has been reached between the ruling party and the opposition Democratic Party for the People, "DPP", to raise the minimum taxable income and abolish the provisional tax rate on gasoline. However the DPP seems to be losing the power to negotiate with the government, as the Japan Innovation Party, which emphasizes on education support for high school students and free school lunches, and the ruling party have already reached an agreement on the fiscal budget.
- ④ **We have maintained our forecast for the Bank of Japan's monetary policy.** We expect the BOJ to raise its policy rate to 0.75% in July 2025, 1.00% in January 2026, and 1.25% in January 2027. We anticipate that the BOJ will raise interest rate gradually towards the lower bound of a neutral interest rate (between 1% to 2.5%) at a pace of once every six months until the rate reaches 1% and then once a year thereafter. The BOJ and the governor Ueda will decide on further rate hikes by focusing on the underlying trend of inflation, especially about the wage and service prices. While there is a risk of an accelerated pace of the rate hike in the event of higher CPI due to the currency depreciation, there is also a risk of a delay in the rate hike if the Japanese economy is negatively impacted by the new US tariffs, delays in wage increases among mid-to-small businesses, and the Ishiba administration's restraint on monetary tightening, as they are concerned about the negative impact on the upcoming House of Councillors election this summer.

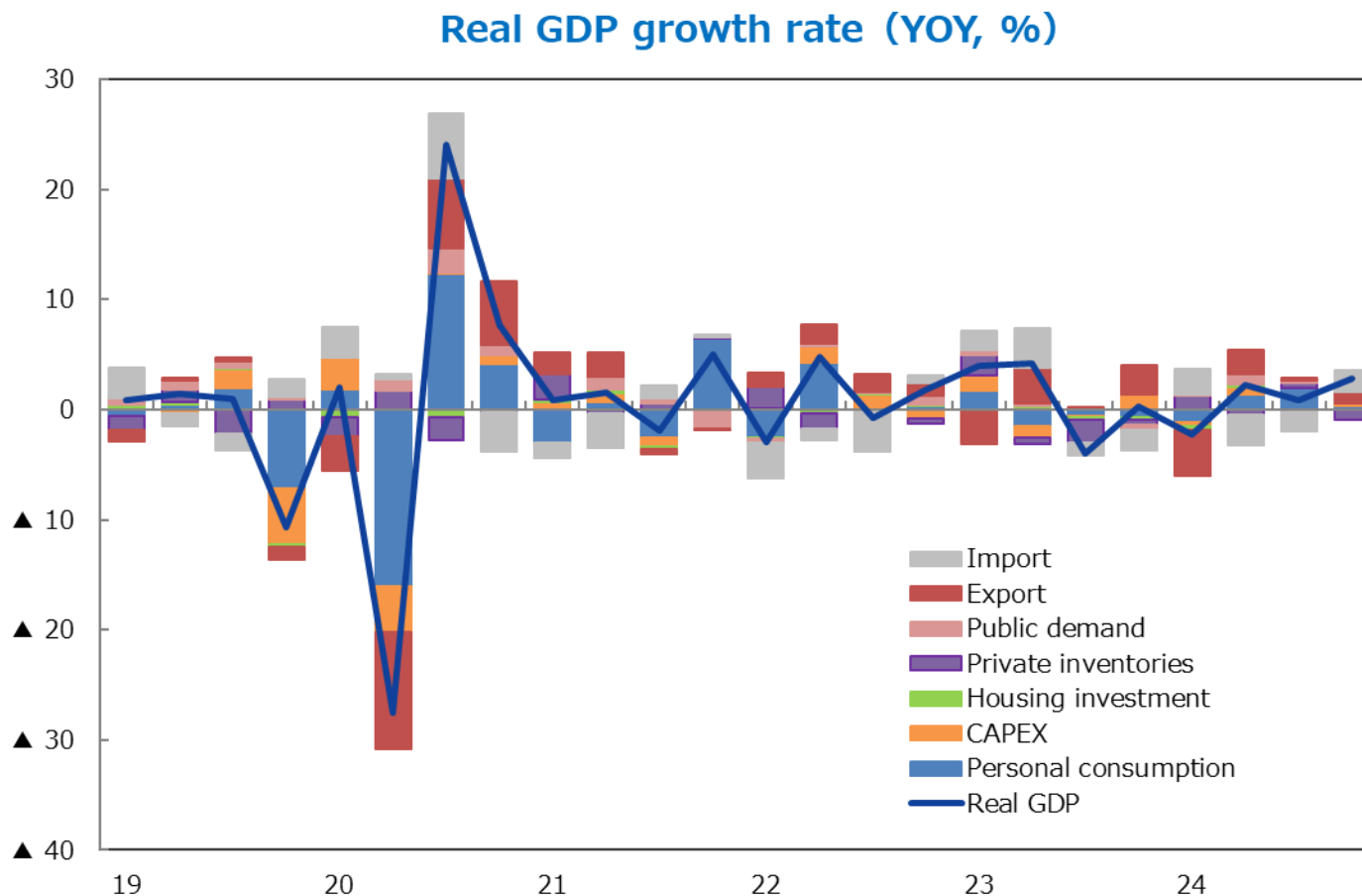
# Forecast for the Japanese economy

Forecast of annual Real GDP growth and its breakdown						
Fiscal Year	FY21	FY22	FY23	FY24 Est	FY25 Est	FY26 Est
Real GDP	3.0%	1.4%	0.7%	0.8%	1.3%	0.9%
Private final consumption expenditure	1.8%	2.6%	-0.4%	0.8%	0.9%	0.8%
Private housing investment	0.3%	-2.6%	0.8%	-1.2%	-0.7%	-1.1%
Private-sector capital investment	3.2%	3.6%	-0.1%	2.0%	1.4%	1.6%
Private inventory investment	0.5%	0.0%	-0.3%	0.0%	0.0%	0.0%
Public fixed capital formation	-6.4%	-5.5%	-0.3%	1.7%	0.3%	0.7%
Net export contribution	0.8%	-0.5%	1.4%	-0.3%	0.3%	0.2%
Exports of goods and services	12.5%	4.9%	2.8%	1.9%	4.1%	3.7%
Imports of goods and services	7.3%	7.3%	-3.3%	3.3%	2.7%	2.9%
Nominal GDP	2.9%	2.3%	4.9%	3.6%	3.4%	2.6%
GDP deflator	-0.1%	0.9%	4.2%	2.8%	2.2%	1.7%
Industrial Production Index	5.6%	-0.3%	-1.9%	-0.7%	1.6%	1.5%
Consumer Price Index (Core)	0.1%	3.0%	2.8%	2.7%	2.6%	2.0%
Consumer Price Index (BOJ Core)	-0.8%	2.2%	3.9%	2.2%	2.3%	2.1%
Domestic corporate goods price index	7.1%	9.6%	2.4%	3.1%	2.1%	1.5%
Employee compensation	2.1%	2.5%	1.9%	4.5%	3.6%	3.5%
Unemployment rate	2.8%	2.6%	2.6%	2.5%	2.4%	2.3%
Monetary Policy interest rate (Short term)	-0.10%	-0.10%	0-0.1%	0.50%	1.00%	1.25%

Note: Rate of increase over the previous year. Net exports are based on the degree of contribution, and the consumer price index (Core) excludes the effects of the consumption tax and free education.

Source: Sumitomo Mitsui DS Asset Management based on data from the Cabinet Office, the Ministry of Internal Affairs and Communications, and the Ministry of Economy, Trade and Industry

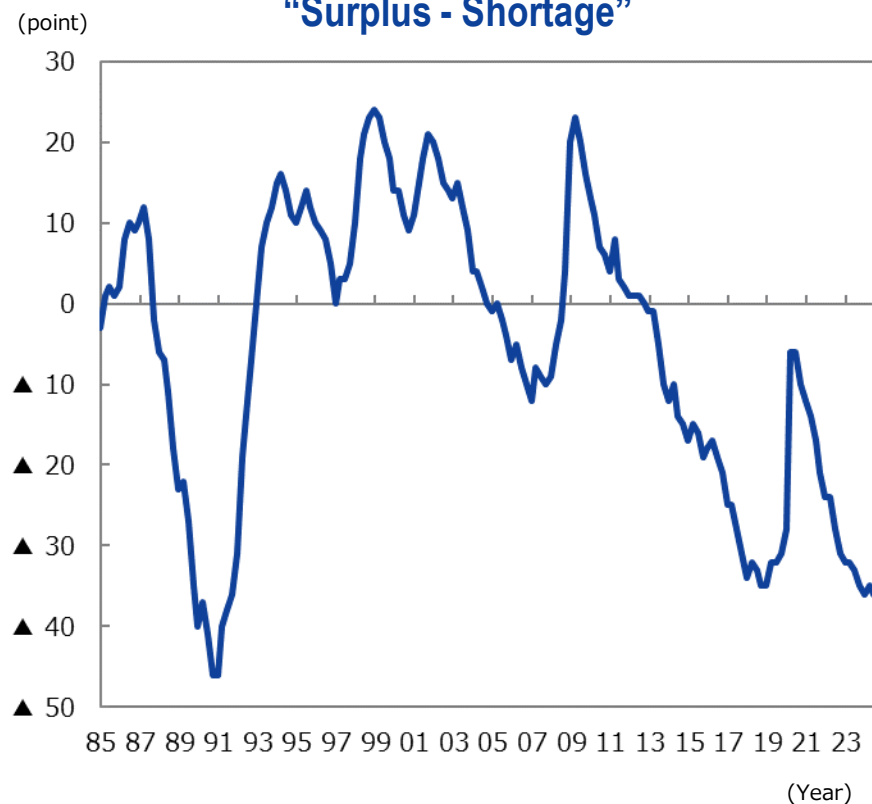
# The Japanese economy resumes its growth trend



Note: Data is from Q1 2019 to Q4 2024.  
Source: Cabinet office, SMDAM

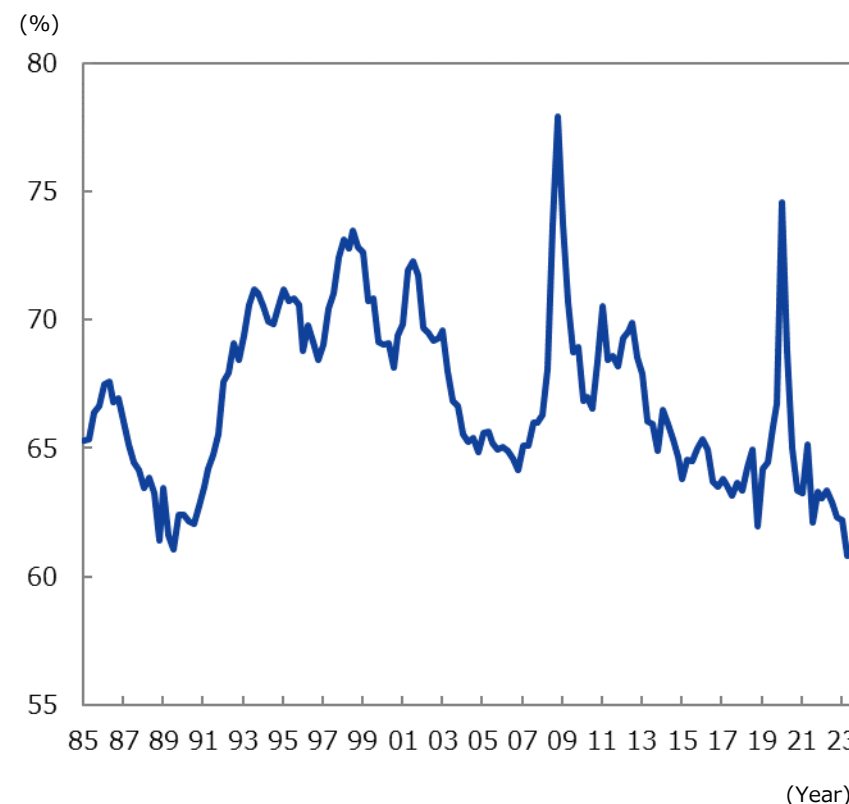
# Conundrum of the Japanese labor market

## Employment Sufficiency Index "Surplus - Shortage"



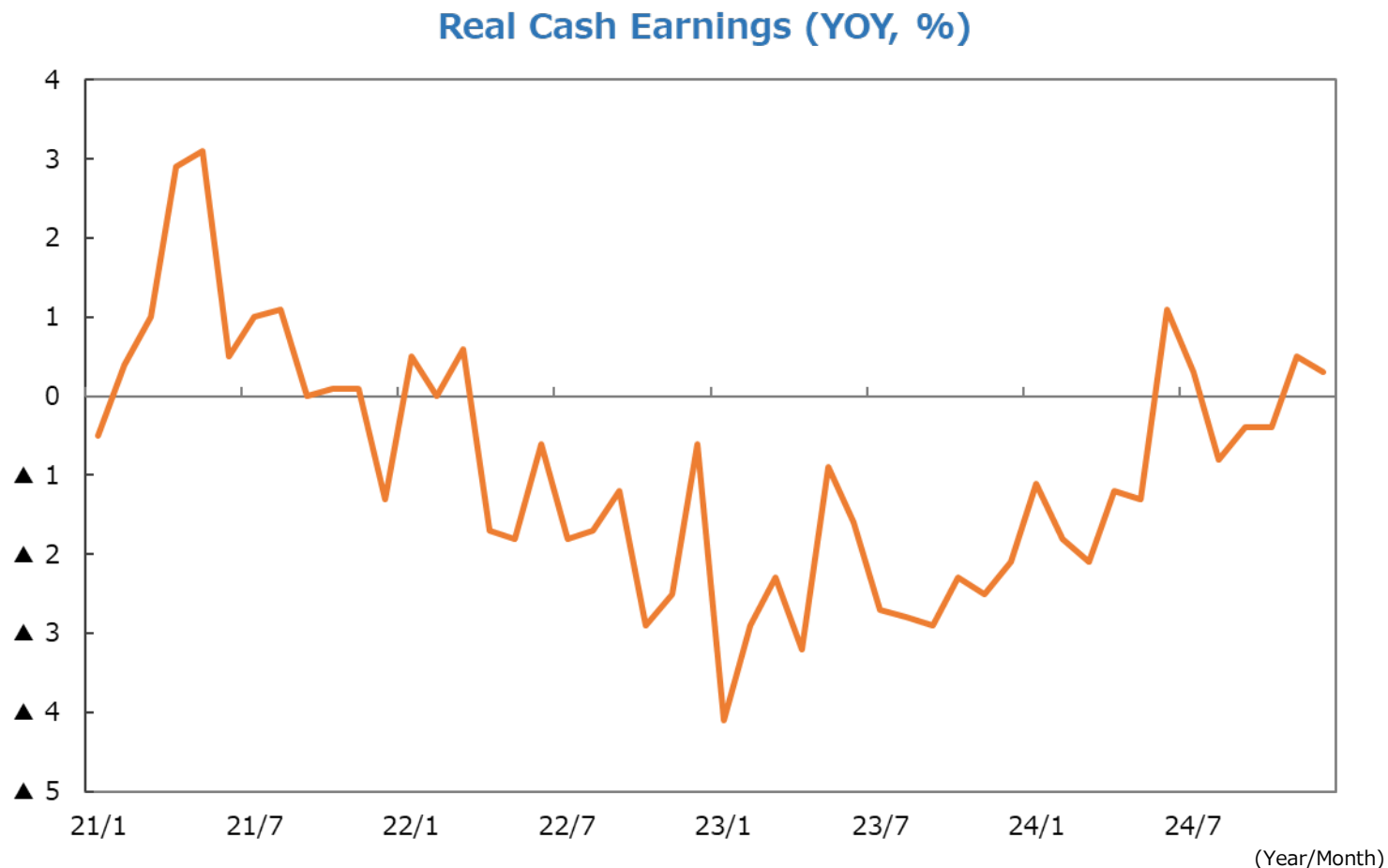
Note: Data is from April 1985 to December 2024.  
Source: The bank of Japan, SMDAM

## Labor Share of Added Value



Note: Data is from April 1985 to April 2024.  
Source: Ministry of finance, SMDAM

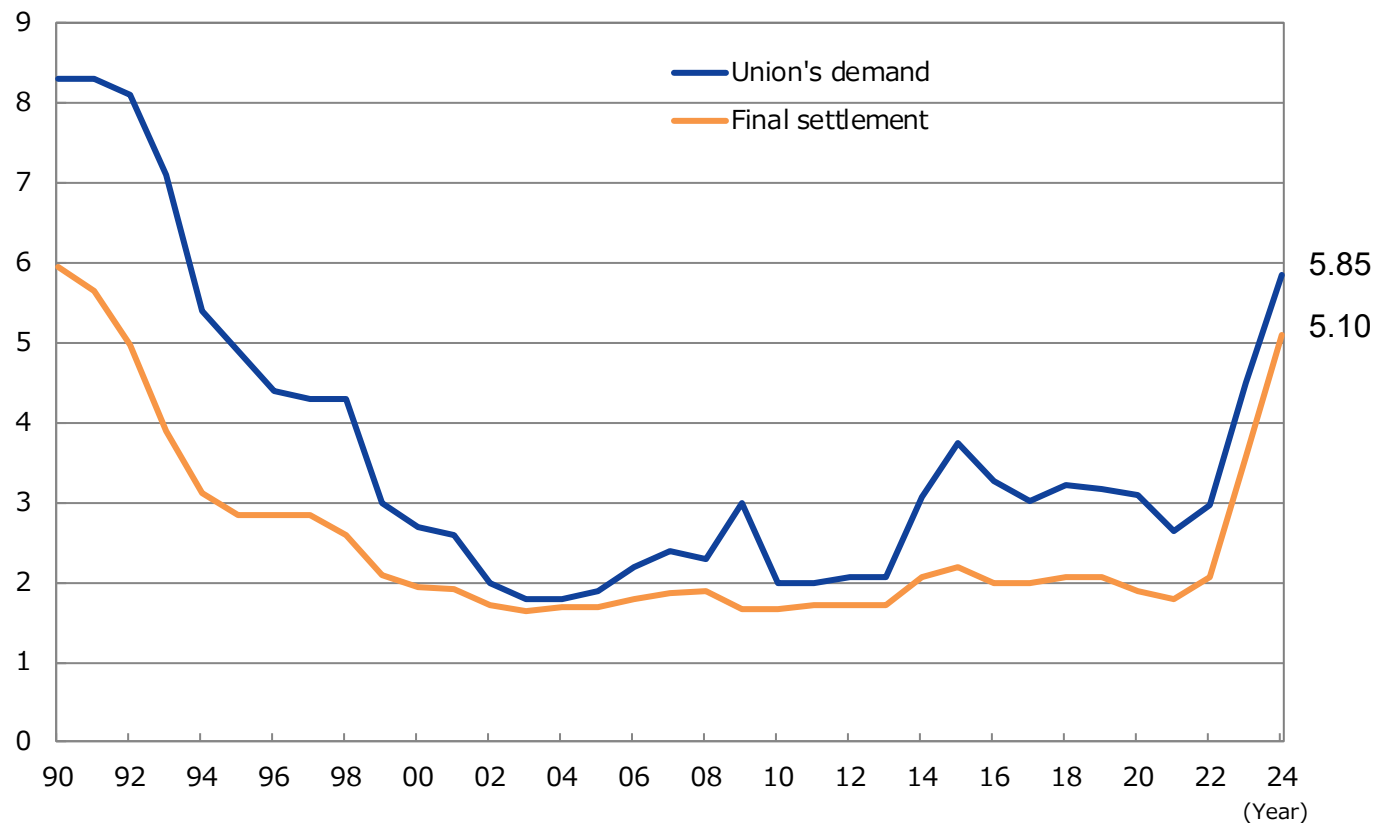
# Wage increases start beating inflation



Note: Data is from January 2021 to December 2024.  
Source: Japanese Trade Union Confederation, SMDAM

# Highest wage increase in 33 years

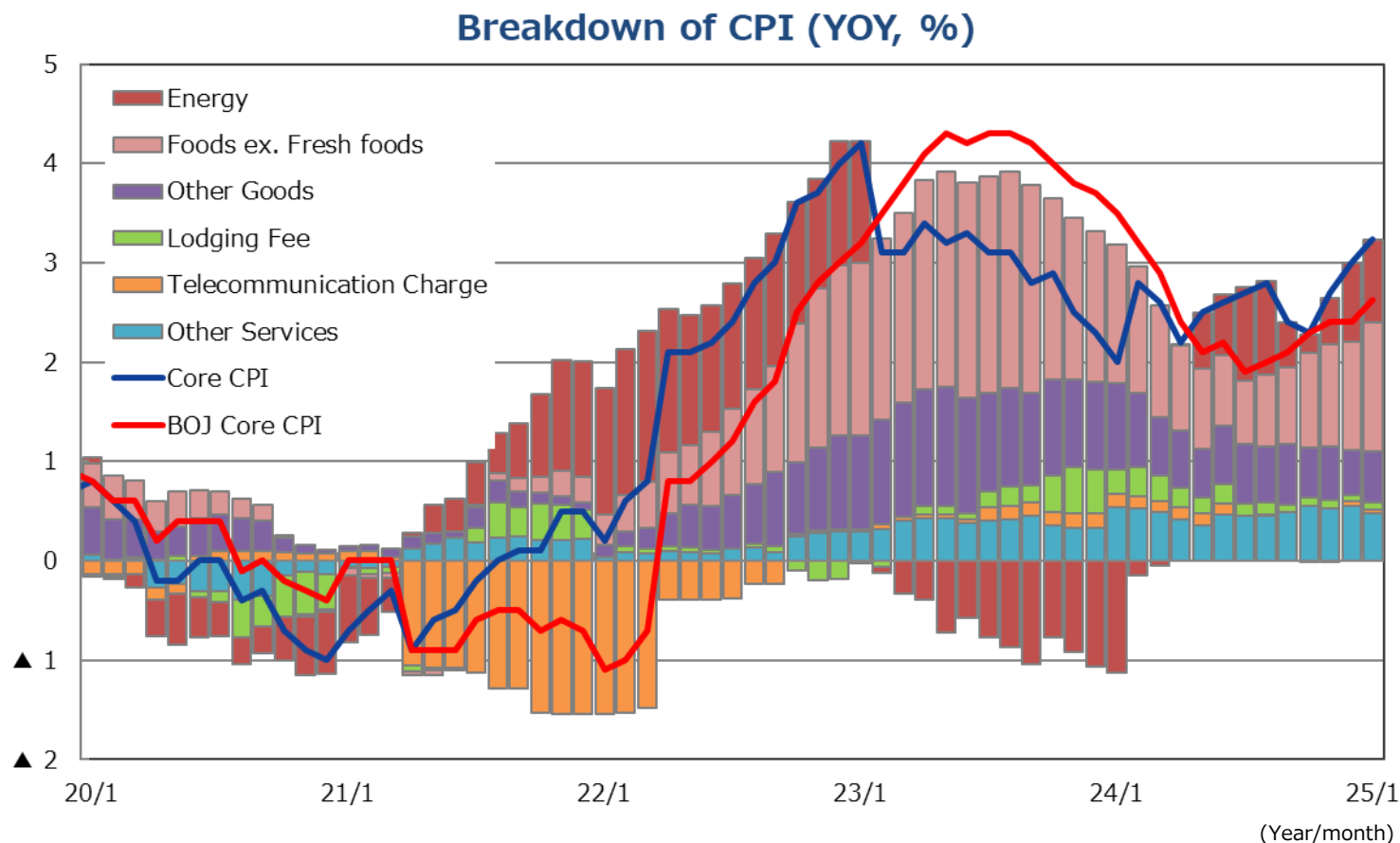
Wage increase (YOY, %)



Note: Data is from FY 1990 to FY 2024.  
Source: Japanese Trade Union Confederation, SMDAM

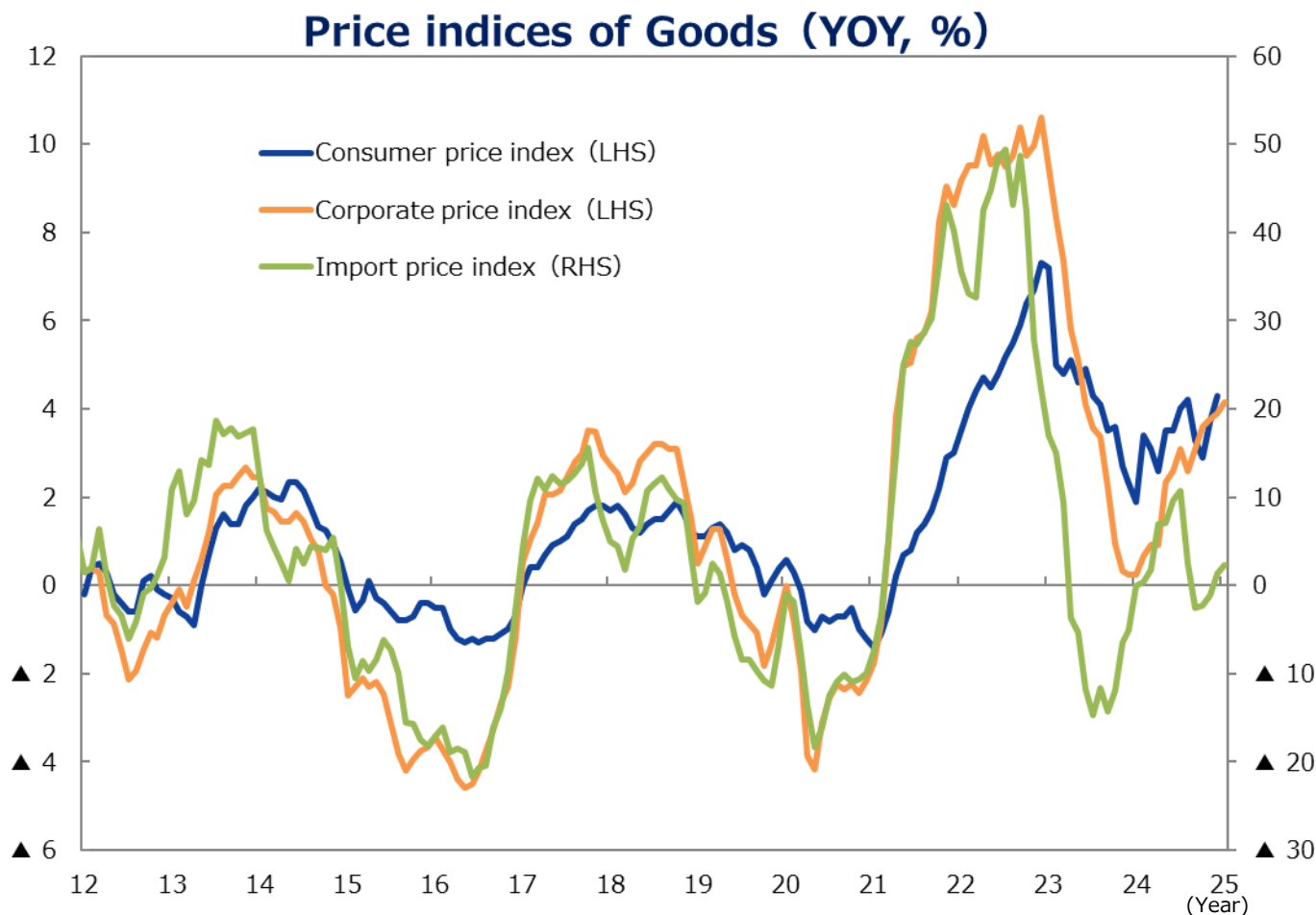


# Consumers feel unprecedented price pressure in 30 years



Note: Data is from January 2020 to January 2025.  
Source: MIAC, SMDAM

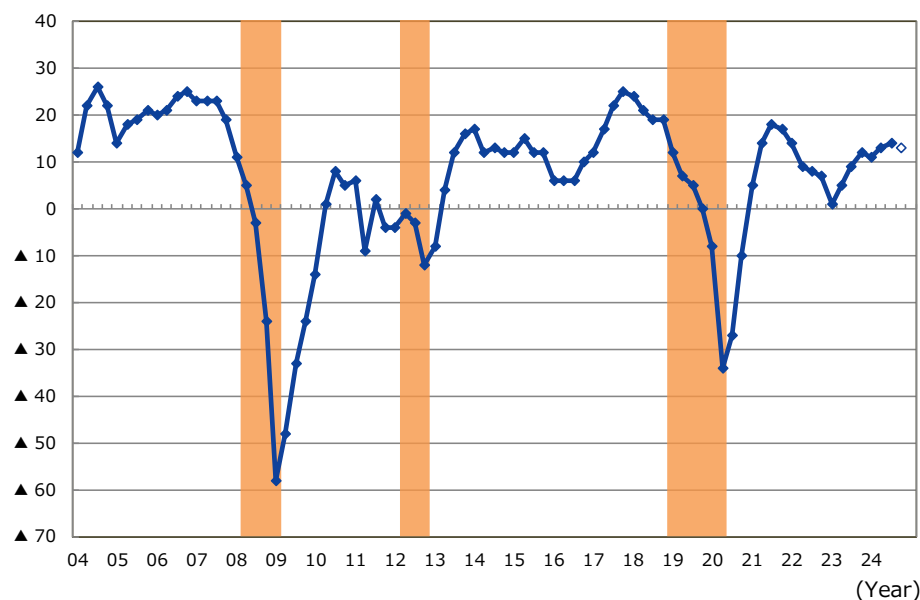
# Corporate price rising despite weakening import prices



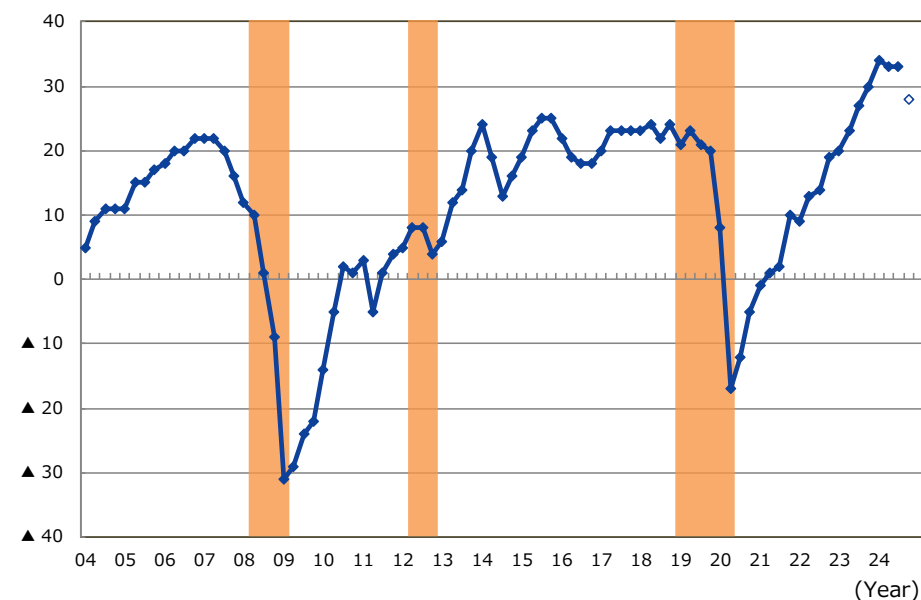
Note: Data is from January 2012 to January 2025.  
Source: MIAC, Bloomberg, SMDAM

# Improvement in business sentiment appears to have stalled

BOJ business condition DI Large manufacturers (%)



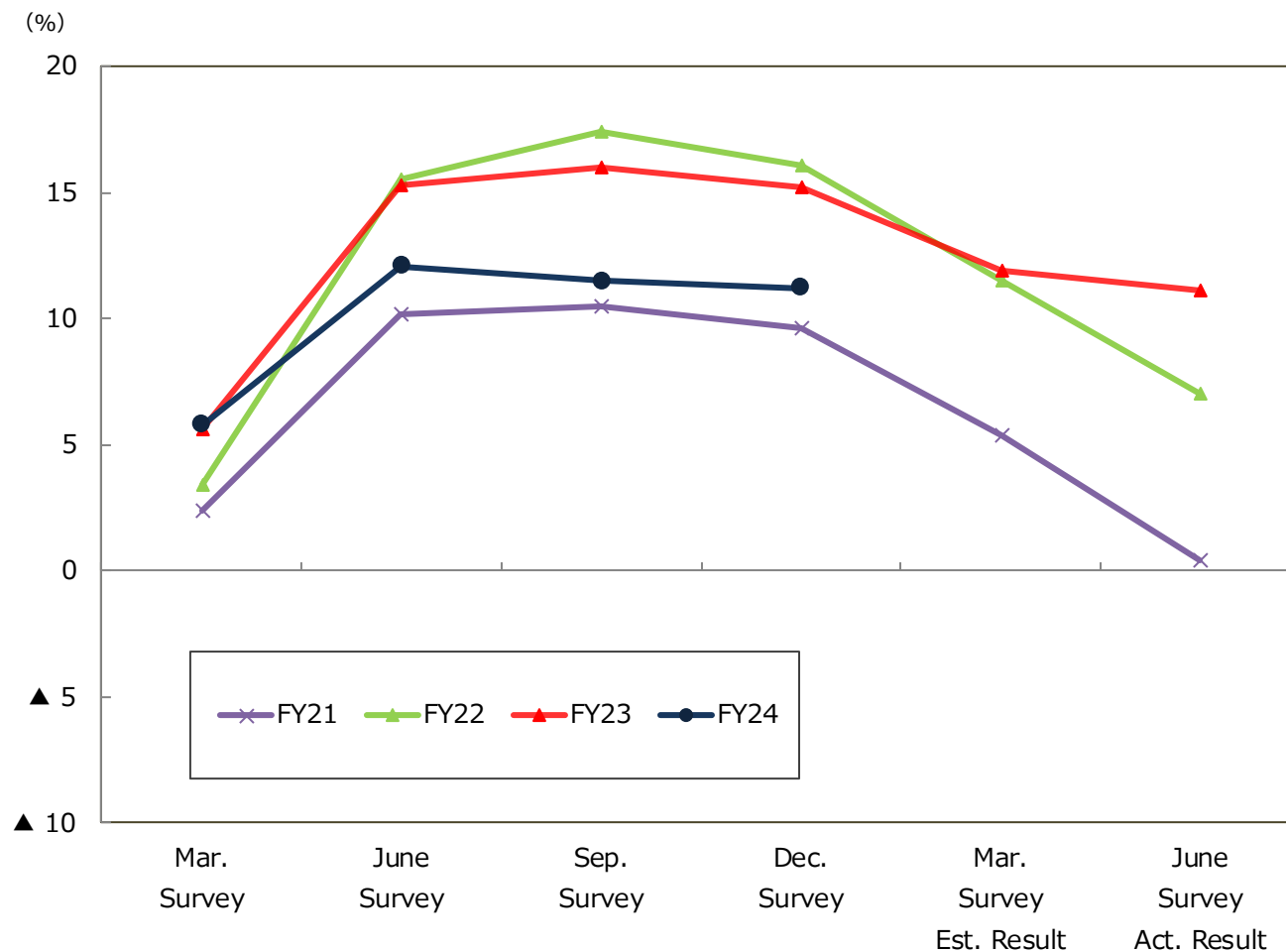
BOJ business condition DI Large non-manufacturers (%)



Note: Data is from Q1 2004 to Q4 2024. The orange shadow represents periods of economic recession.  
Source: The Bank of Japan, SMDAM

# Appetite for CAPEX keeps momentum so far

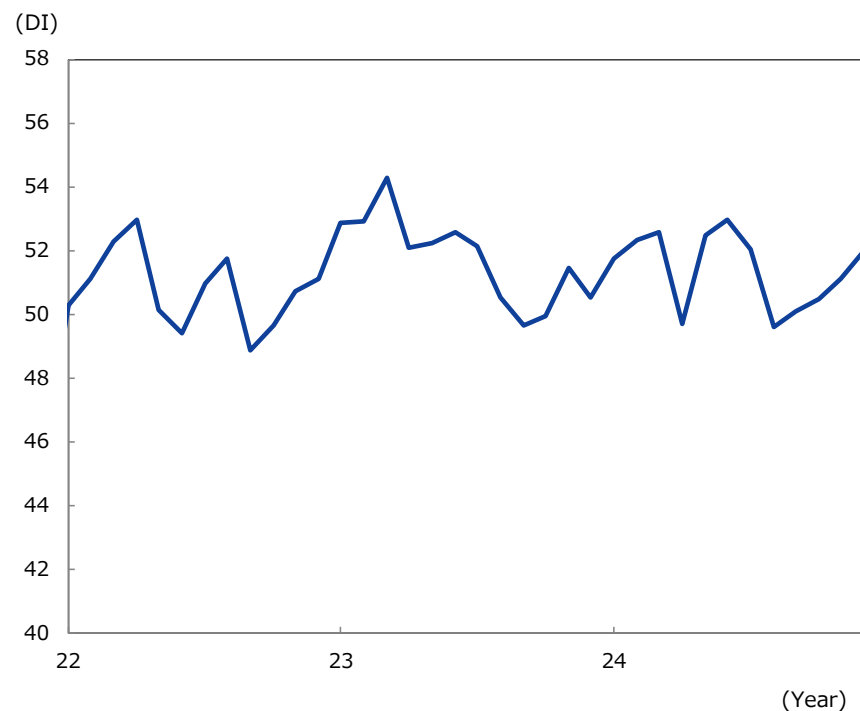
## Plan of CAPEX (Inc. Software, Ex. Land and R&D, YOY)



Note: Data is from Q1 FY2021 to Q4 FY2024.  
Source: The Bank of Japan, SMDAM

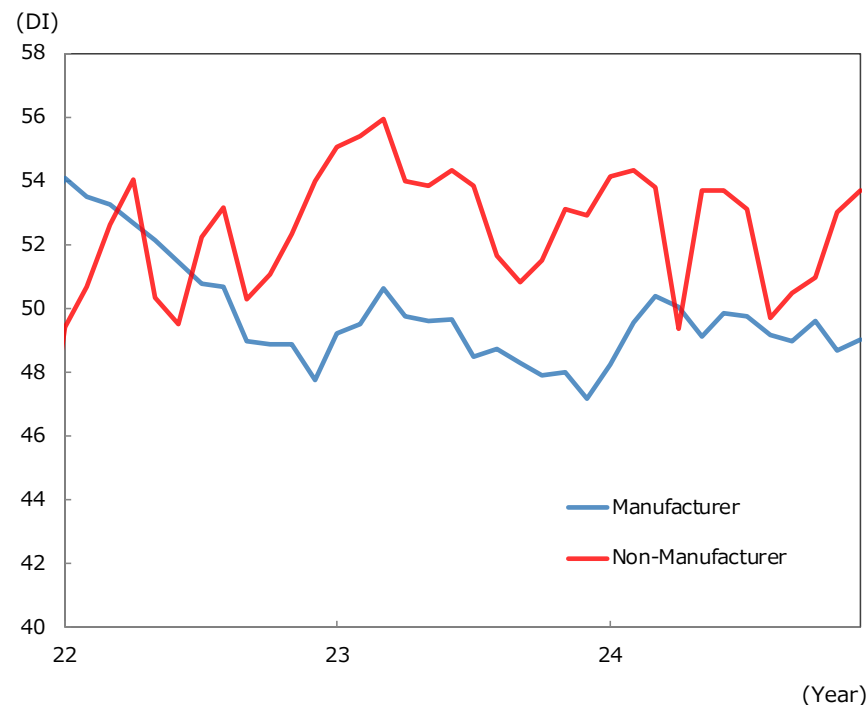
# Non-manufacturers lead recovery in business sentiment

## Composite PMI



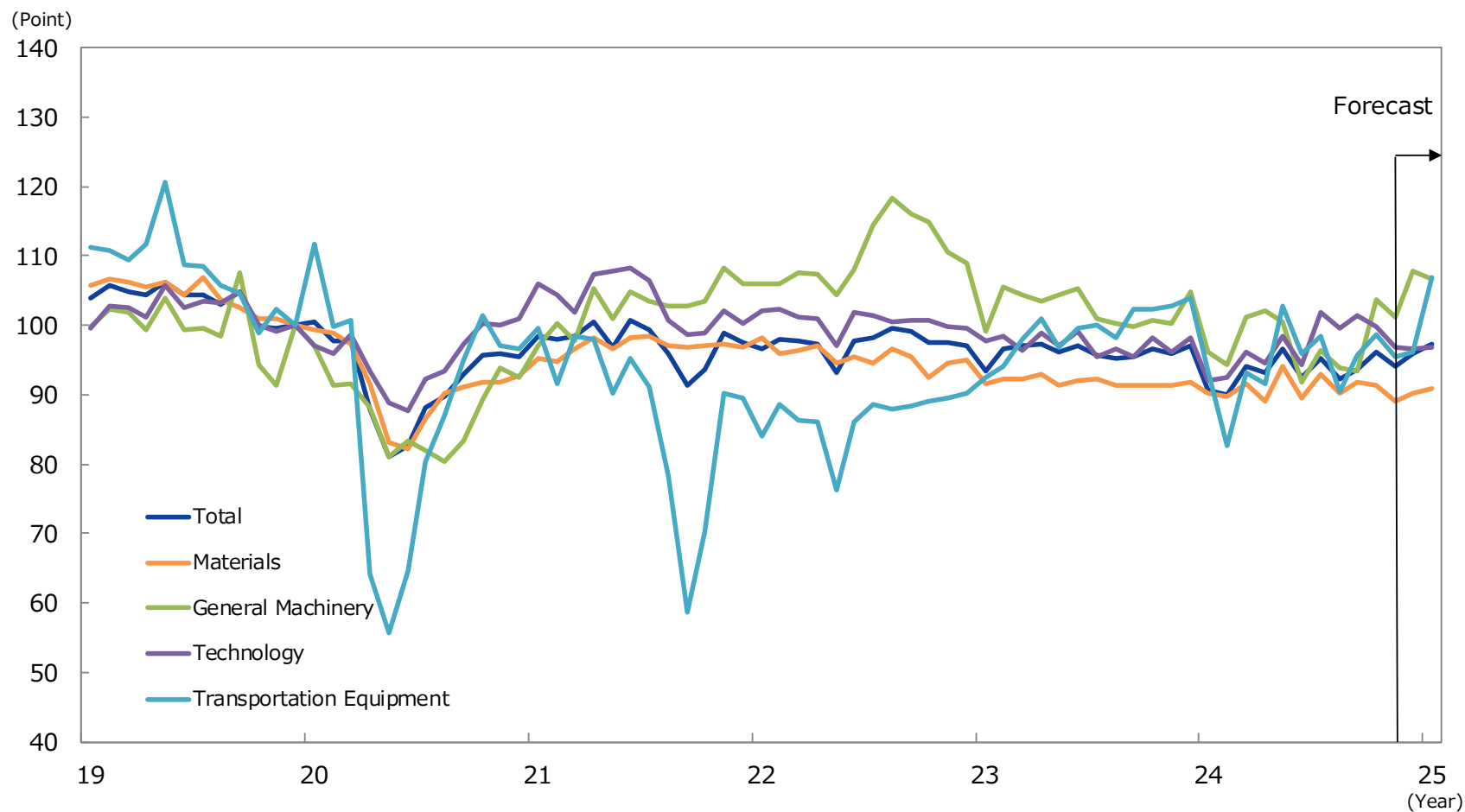
Note: Data is from February 2022 to February 2025.  
Source: Bloomberg, SMDAM

## PMI, Manufacturer & Non-Manufacturer



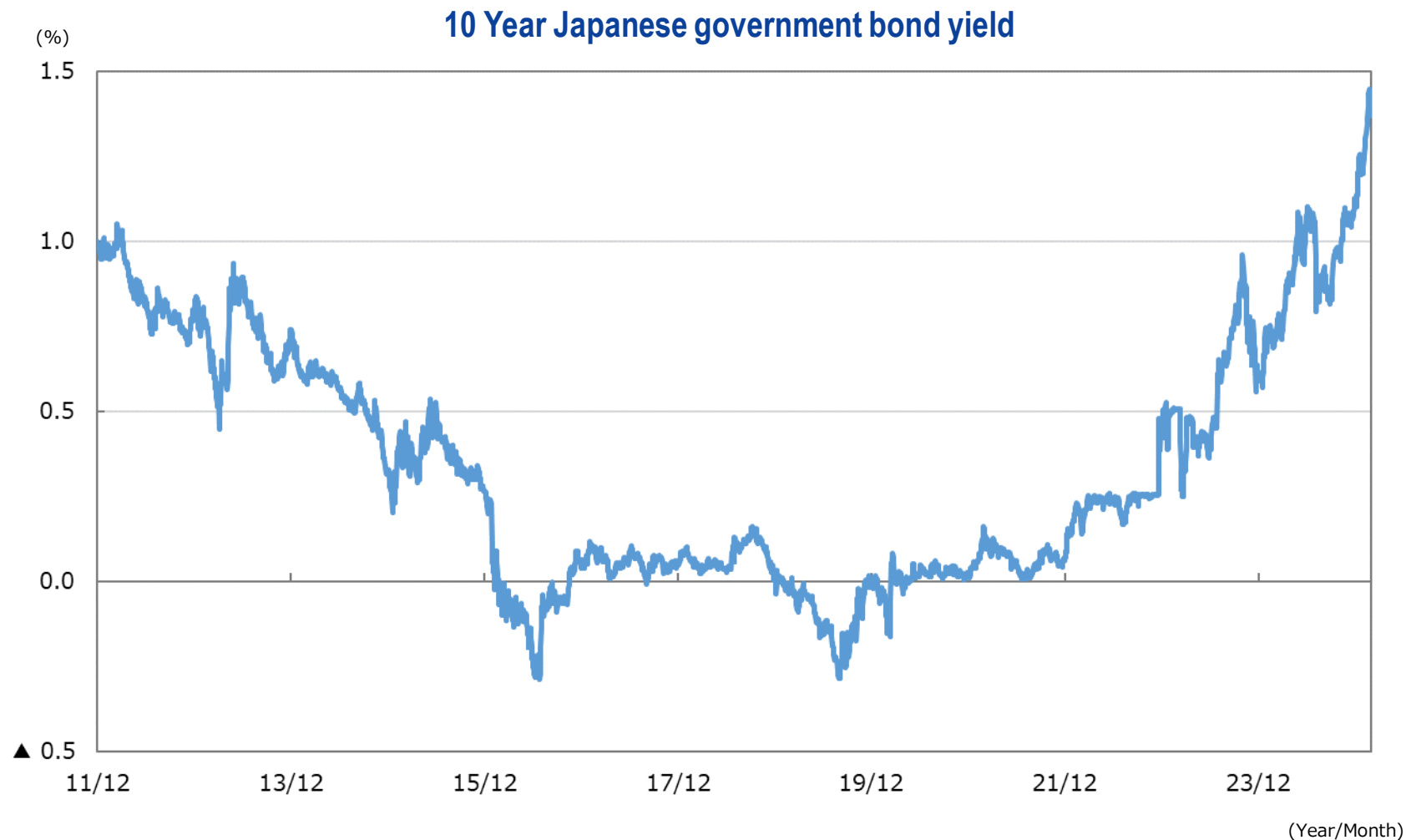
# Autos to boost Industrial production in the near future

## Industrial Production (Dec. 2019=100)



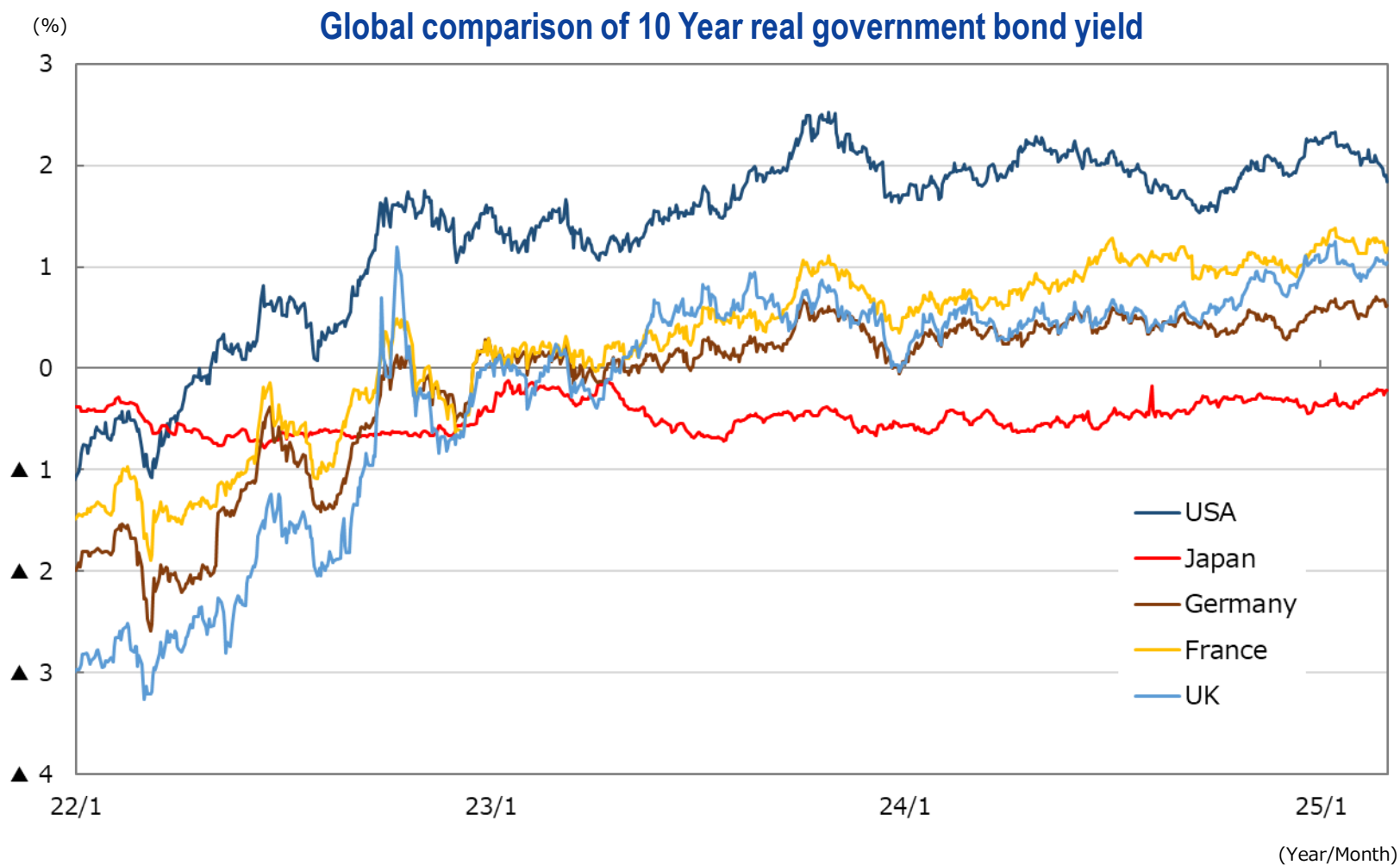
Note: Data is from January 2019 to January 2025. Data after November 2024 is forecasts.  
Source: METI, SMDAM

# Growing expectation for further monetary tightening



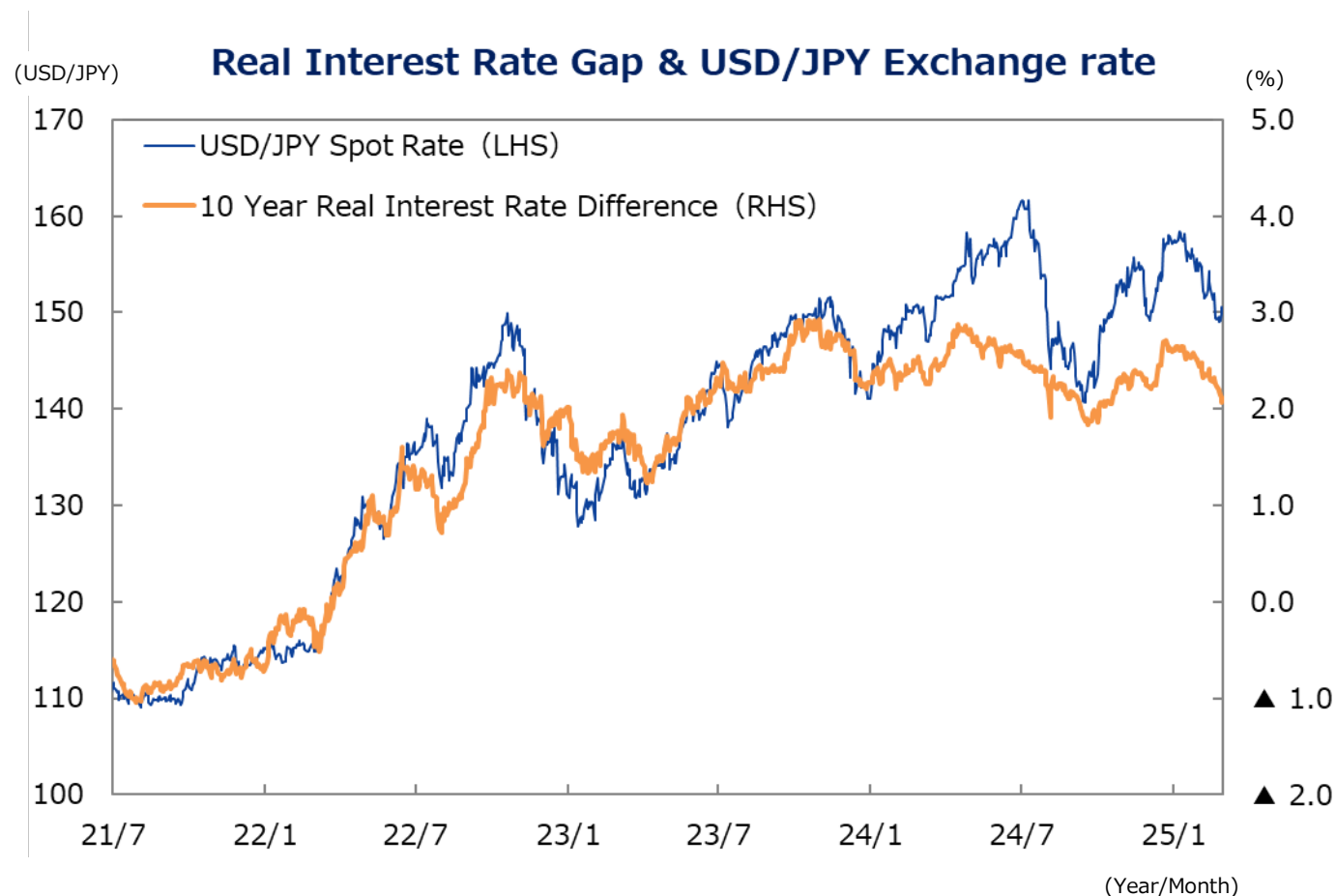
Note: Data is from 31st December 2011 to 28th February 2025.  
Source: Bloomberg

# Reason why Japanese interest rates rises further



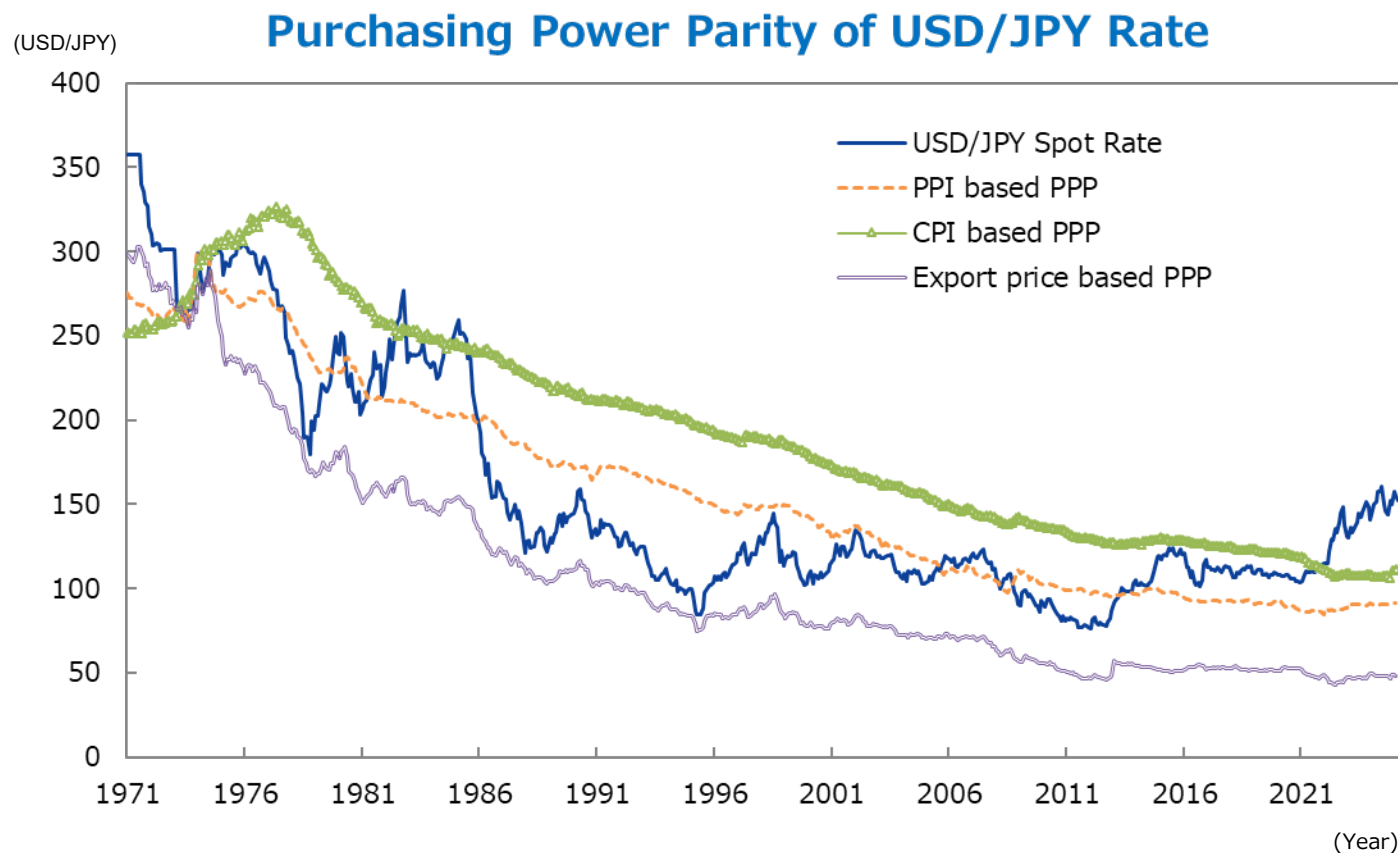


# Interest rate gap suggests further room for the yen's appreciation



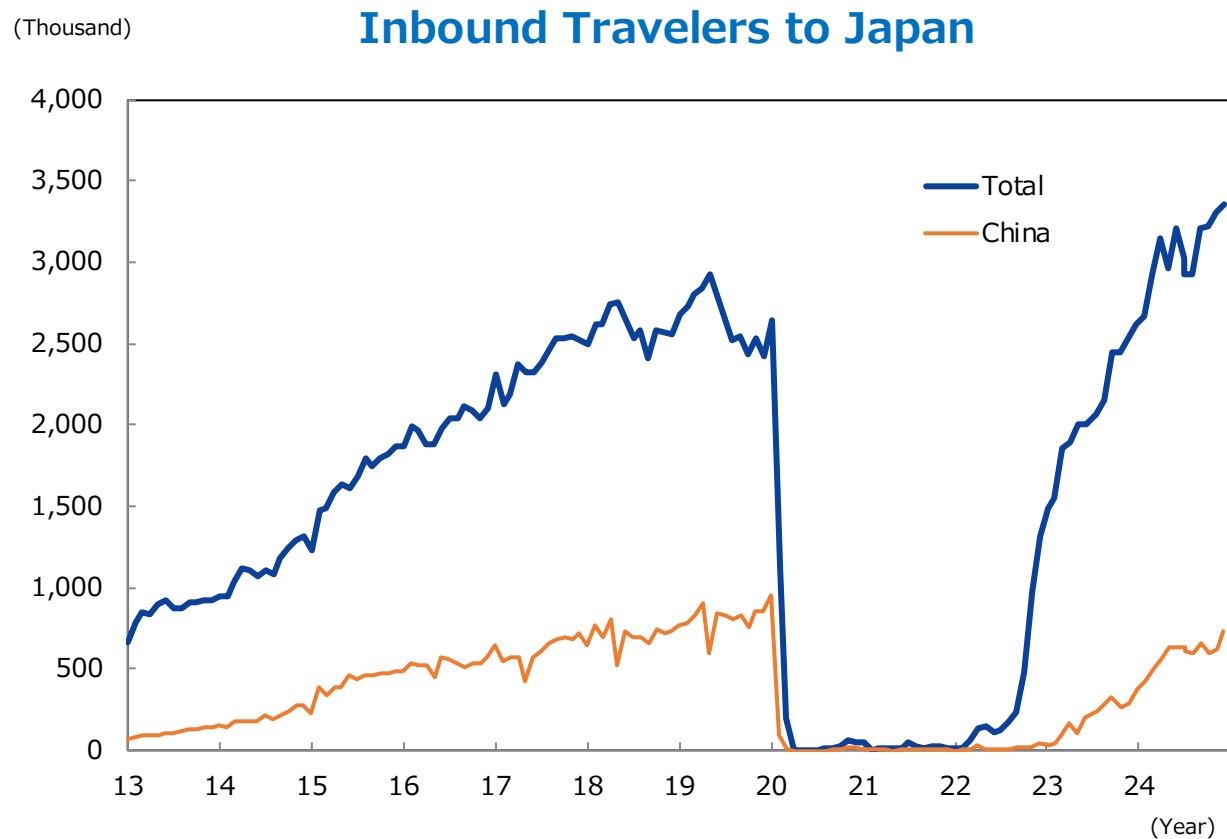
Note: Data is from 1st July 2021 to 28th February 2025.  
Source: Bloomberg

# PPP also suggests big room for the yen's appreciation



Note: Data is from January 1971 to January 2025.  
Source: DOL, Bank of Japan, SMDAM

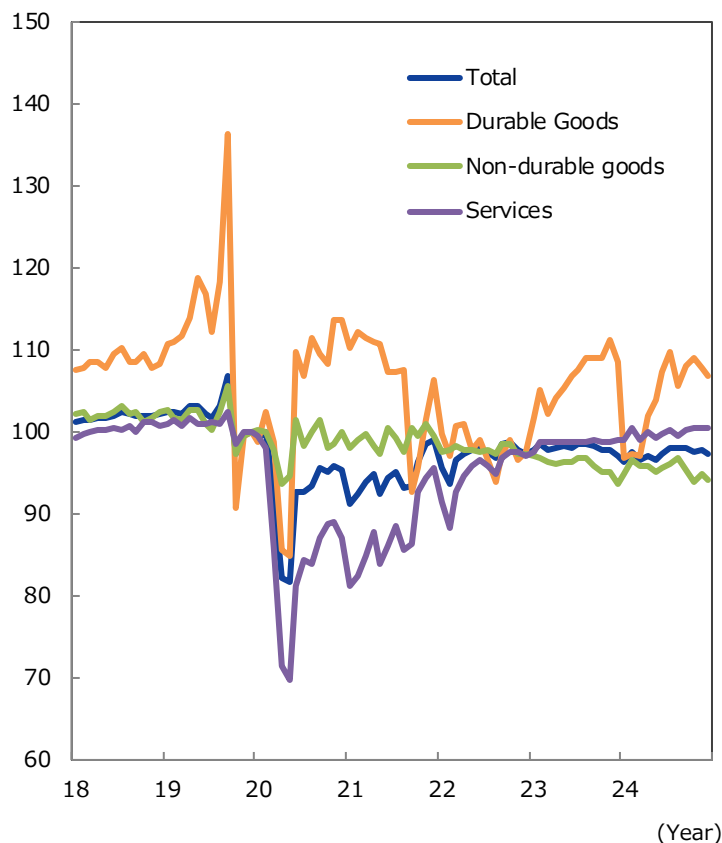
# Inbound travel keeps strong momentum



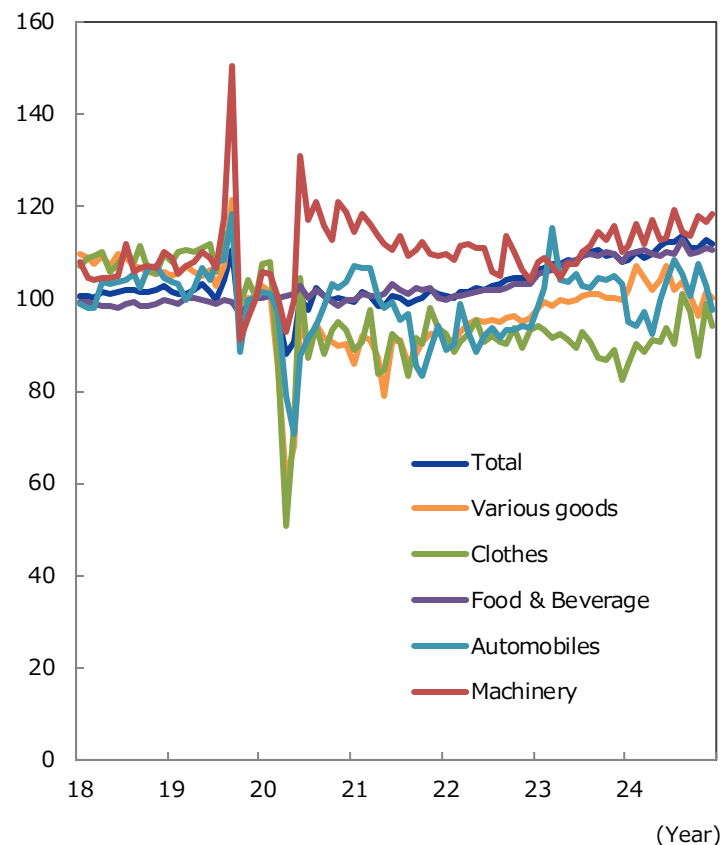
Note: Data is from January 2013 to December 2024. Data is non-seasonally adjusted.  
Source: Japan National Tourism Organization, SMDAM

# Demand for durable goods support consumer activities

Consumer Activity Index (Dec. 2019 = 100)



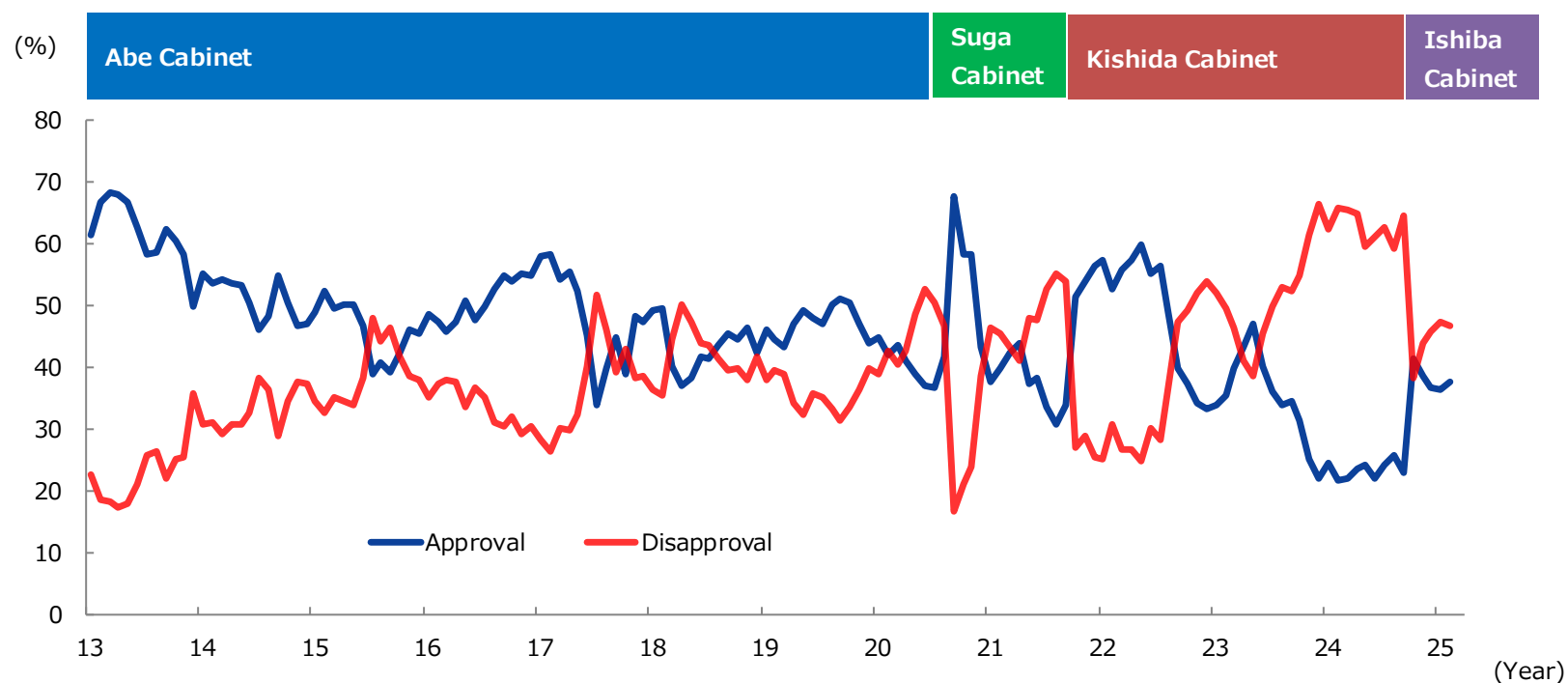
Retail Sales (Dec. 2019 = 100)



Note: Data is from January 2018 to December 2024.  
Source; Bank of Japan, METI, and SMDAM

# PM Ishiba will face a tough election battle this summer

## Cabinet approval rate



Note: Data is from January 2013 to February 2025.  
Source: NHK, Asahi, Kyodo, Nikkei, Yomiuri, Sankei, Mainichi, Jiji, and SMDAM

# Schedule of major events

Year	Month	Date	Event
2025	March	11	Revision of 2024 Q4 GDP
		14	Release of the results of spring negotiations of Trade Union Confederation
		18-19	Monetary Policy Meeting
		25	Expiration of the term of the Bank of Japan's Adachi Policy Board member Enactment of the FY 2025 budget and tax-related bills
	April	13	Start of Osaka Expo
		30-5/1	Monetary Policy Meeting
	May		Release of 2025 Q1 GDP
	June	9	Revision of 2025 Q1 GDP
		16-17	Monetary Policy Meeting Cabinet's decisions on "Big-boned policy"
			End of the ordinary Diet session
		30	Expiration of the term of the Bank of Japan's Nakamura Policy Board member
	July		Final results of spring negotiations of Trade Union Confederation
		22	Election of the Tokyo Metropolitan Assembly Member
		28	Election of the House of Councillors
	August		Release of 2025 Q2 GDP
	September		Revision of 2025 Q2 GDP
		18-19	Monetary Policy Meeting
	October	29-30	Monetary Policy Meeting
	November		Release of 2025 Q3 GDP
	December		Revision of 2025 Q3 GDP
		18-19	Monetary Policy Meeting
			Cabinet approval of the initial budget for FY 2026 and the outline for tax reform

(Source) Compiled by Sumitomo Mitsui DS Asset Management Co., Ltd.



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