Japan Equity Market Outlook

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-August 2026-

Summary

Japan Equity Outlook

In July, TOPIX rose 0.2%, its fourth consecutive monthly gain, while the Nikkei 225 fell 8.1%, its first decline in four months. Concerns over Fed tightening prompted profit-taking in AI and semiconductor stocks amid questions over excessive investment, delayed monetization, and high valuations. The semiconductor-heavy Nikkei suffered, while banks and domestic-demand stocks supported TOPIX. AI investment and US monetary policy remain key. US hyperscalers' surging data-center spending faces scrutiny over power constraints, financing, and returns, but medium-term AI adoption and demand should continue expanding. We expect a Fed rate hike this year to contain persistent demand-driven inflation. If tightening is gradual, it should not derail the US recovery or earnings growth, allowing US and Japanese equities to trend moderately higher despite volatility.

Economic and Monetary Policy

Our base case is continued global and domestic recovery, supported by AI demand and fiscal expansion, although prolonged Middle East tensions and the effective closure of the Strait of Hormuz pose risks. With central banks increasingly vigilant on inflation, we expect further BOJ normalization after June's hike and a Fed hike this year. Intervention has temporarily reversed yen weakness, but elevated US rates should sustain a stronger dollar.

Key Drivers for Japan's Stock Market

Japanese equities remain supported by the end of deflation, governance reform, and improving capital efficiency. The Takaichi administration's growth investment and economic-security policies may provide additional tailwinds.

Risks and Events

Downside risks include sharply higher US real or Japanese long-term yields, weaker AI earnings, oil-driven deterioration in Japan's terms of trade, Japan-China tensions, and rapid yen appreciation. Upside potential comes from faster AI monetization, concrete Takaichi growth measures, and stronger recognition of governance reforms.

Outlook for the Japanese Economy

SMDAM Forecasts: Japanese Economy

Forecasts as of 17 Jul 2026		FY22 (A)	FY23 (A)	FY24 (A)	FY25 (A)	FY26 (E)	FY27 (E)
Real GDP	(yoy, %)	1.4	0.0	0.5	0.8	0.8	1.1
Private Consumption	(yoy, %)	2.5	▲ 1.0	0.1	1.3	1.0	1.2
Private Resid. Investment	(yoy, %)	0.6	1.8	▲ 0.7	▲ 3.3	0.5	▲ 0.0
Private Capex	(yoy, %)	3.9	▲ 0.1	0.8	2.0	1.2	2.3
Public Investment	(yoy, %)	▲ 4.5	▲ 0.1	0.1	▲ 0.5	1.6	0.6
Net Exports (contribution)	(%point)	▲ 0.6	1.2	▲ 0.3	▲ 0.1	0.1	▲ 0.1
Exports	(yoy, %)	4.7	3.1	2.7	2.0	0.6	2.6
Imports	(yoy, %)	7.3	▲ 2.2	4.0	2.6	0.2	3.4
Nominal GDP growth	(yoy, %)	2.6	4.7	3.7	4.1	2.9	3.0
GDP deflator	(yoy, %)	1.2	4.8	3.2	3.3	2.1	1.9
Industrial production	(yoy, %)	▲ 0.3	▲ 1.9	▲ 1.5	▲ 0.2	1.8	1.2
CPI (less fresh food & institutional factors)	(yoy, %)	4.0	2.8	2.7	2.7	3.2	2.2
Unemployment Rate	(%)	2.6	2.6	2.5	2.6	2.5	2.4
Policy Rate	(End of Period, %)	▲ 0.1	0-0.1	0.50	0.75	1.25	1.75

Note: Forecasts by SMDAM.
Source: SMDAM

Economic and Asset Price Outlook for Key Regions

SMDAM Forecasts: Major Economies, Rates and FX

Forecasts as of 22 Jul 2026		2025 Q4	2026 Q1	Q2	Q3	Q4	2027 Q1	Q2	Q3
GDP Growth Rate									
United States	(saar, %)	0.5	2.1	1.9	2.6	2.0	1.9	1.9	2.0
Japan	(saar, %)	0.7	1.8	0.9	0.6	0.8	0.7	2.0	0.8
Euro Area	(saar, %)	0.7	▲ 0.9	1.2	1.2	1.2	1.5	1.6	1.6
China	(yoy,%)	4.5	5.0	4.3	4.5	4.6	4.5	4.6	4.5
Inflation									
United States	(core PCED, yoy, %)	2.8	3.1	3.4	3.4	3.4	2.9	2.7	2.6
Japan	(core CPI, yoy, %)	2.8	1.8	1.5	1.8	2.7	3.4	1.5	1.5
Euro Area	(yoy, %)	2.1	2.0	3.2	3.1	3.2	2.9	2.2	2.2
China	(yoy, %)	0.6	0.9	1.2	1.0	1.0	0.3	0.2	0.2
Policy Rates									
United States	(End of Period, %)	3.5-3.75	3.5-3.75	3.5-3.75	3.75-4.0	4.0-4.25	4.0-4.25	4.0-4.25	4.0-4.25
Japan	(End of Period, %)	0.75	0.75	1.00	1.00	1.25	1.25	1.50	1.50
Euro Area	(End of Period, %)	2.00	2.00	2.25	2.50	2.50	2.50	2.50	2.50
China	(End of Period, %)	1.40	1.40	1.40	1.40	1.40	1.40	1.30	1.30
Long-term Rates									
US 10Y	(End of Period, %)	4.17	4.32	4.47	4.70	4.80	4.80	4.80	4.80
Japan 10Y	(End of Period, %)	2.06	2.35	2.68	2.85	2.95	3.00	3.00	3.10
Germany 10Y	(End of Period, %)	2.86	3.00	2.86	3.20	3.30	3.30	3.30	3.30
FX									
USD/JPY	(End of Period)	156.7	158.7	162.6	166.0	167.0	167.0	167.0	167.0
EUR/JPY	(End of Period)	184.1	183.4	185.7	189.2	188.7	187.0	187.0	187.0
Stock Prices									
TOPIX	(End of Period)	3,409	3,498	3,995	4,100	4,150	4,200	4,200	4,200
Nikkei 225	(End of Period)	50,339	51,064	70,062	69,700	70,600	71,400	71,400	71,400

		2024 (yoy,%)	2025 (yoy,%)	2026 (yoy,%)	2027 (yoy,%)
GDP Growth Rate					
United States	(saar, %)	2.8	2.1	2.2	2.0
Japan	(saar, %)	0.5	0.8	0.8	1.1
Euro Area	(saar, %)	0.9	1.5	0.5	1.4
China	(yoy,%)	5.0	5.0	4.6	4.5
Inflation					
United States	(core PCED, yoy, %)	2.9	2.8	3.3	2.7
Japan	(core CPI, yoy, %)	2.7	2.7	2.4	1.1
Euro Area	(yoy, %)	2.4	2.1	2.9	2.3
China	(yoy, %)	0.2	0.0	1.0	0.2

Note: Japan is FY-based.

Note: Forecasts by SMDAM.

Source: SMDAM

Assessment of Kioxia's Impact on TOPIX EPS and P/E

Earnings, PER and EPS of TOPIX Companies and Kioxia

	Market cap: (a)	Share price: (b)	Net income: (c)				PER: (d)=(a)/(c)				EPS: (f)=(b)/(d)				EPS growth		
	as of Jul. 31	as of Jul. 31	FY25	FY26	FY27	FY28	FY25	FY26	FY27	FY28	FY25	FY26	FY27	FY28	FY26	FY27	FY28
	(JPY tn)	(points/yen)	(JPY tn)	(JPY tn)	(JPY tn)	(JPY tn)	(x)	(x)	(x)	(x)	(points/yen)	(points/yen)	(points/yen)	(points/yen)	(%)	(%)	(%)
TOPIX companies, aggregate basis	1,333.2	4,003.3	68.5	78.3	87.6	93.6	19.5	17.0	15.2	14.2	205.8	235.0	263.1	281.2	14.2	11.9	6.9
Kioxia	25.5	46,500.0	0.6	5.4	7.1	8.1	46.0	4.7	3.6	3.1	1,011.8	9,831.0	12,873.4	14,808.8	871.6	30.9	15.0
Excluding Kioxia	1,307.8	4,003.3	68.0	72.9	80.6	85.5	19.2	17.9	16.2	15.3	208.1	223.1	246.6	261.8	7.2	10.5	6.2

Note: FY26–FY28 figures are based on Bloomberg consensus. The impact on TOPIX EPS and P/E is a simplified estimate based on Bloomberg aggregate data.
Source: SMDAM and Bloomberg

- Based on Bloomberg consensus estimates, Kioxia's sharp earnings growth raises FY26 TOPIX EPS growth from 7.2% excluding the company to 14.2% including Kioxia—a boost of approximately 7 percentage points. Kioxia also contributes around 11.9 points, or approximately 5%, of the FY26 TOPIX EPS estimate of 235.0.
- Meanwhile, Kioxia's FY26 forecast P/E of 4.7x is well below the 17.9x for TOPIX excluding the company, likely reflecting the cyclical nature of the memory market and the risk of future earnings volatility. Thus, while Kioxia's earnings growth lifts TOPIX EPS, it lowers the TOPIX aggregate FY26 P/E by approximately 0.9x.
- Applying a uniform P/E of 19x to the FY26 TOPIX EPS estimate of 235.0 implies a TOPIX level of 4,465. However, the FY26 P/E for TOPIX including Kioxia is 17.0x, 0.9x below the 17.9x excluding the company. Assuming a similar impact on the target multiple, a simplified adjustment of 0.9x from 19x results in an adjusted multiple of 18.1x and an implied TOPIX level of approximately 4,254. This adjustment is a simplified estimate based on the current difference between the aggregate P/E multiples and may vary with changes in Kioxia's earnings outlook and market valuation.
- Our top-down TOPIX forecast uses macro-model-based EPS estimates as its foundation, while the final index target also takes into account the impact of Kioxia's substantial earnings fluctuations on TOPIX EPS growth and valuation.

This Month's Topic (1): Japan's Policy Dynamics

July opinion polls highlighted a decline in approval for the Takaichi Cabinet. An NHK survey conducted on July 10–12 showed approval edging down from 60% in June to 58%. More pronounced declines were recorded in surveys conducted on July 24–26: approval fell from 69% to 57% in the Yomiuri poll and from 68% to 58% in the Nikkei poll. Nevertheless, approval remained above 50% in all surveys. The decline likely reflects insufficient explanations of key policies, including revisions to the Imperial House Law, and dissatisfaction with the limited progress in addressing inflation.

Debate over the administration's flagship inflation-relief measure—a consumption-tax cut on food—failed to produce a bipartisan agreement. **On July 30, Prime Minister Takaichi announced a plan to reduce the tax rate on food and beverages from 8% to 1% for two years from April 2027 and effectively eliminate the burden for low- and middle-income households through additional benefits**. Following internal LDP coordination, the government aims to pass legislation during the autumn Diet session. However, it remains unclear whether the required funding can be secured without deficit-financing bonds. Opposition from the restaurant industry, system changes for businesses, and compensation for lower local tax revenue are additional challenges.

On July 21, the government approved its growth strategy and annual economic and fiscal policy guidelines. The strategy promotes public- and private-sector investment in 17 areas, including AI and semiconductors, defense, aviation, and space. The guidelines seek to achieve both a "strong economy" and fiscal sustainability, targeting a steady decline in the debt-to-GDP ratio rather than focusing narrowly on the annual primary balance. However, the overall FY2027 budget remains unclear. Key questions include funding for strategic investment, the budget's total size, and new government-bond issuance.

Institutional reforms are also intended to translate the growth strategy into corporate action. The revised Corporate Governance Code requires boards to establish and regularly review policies covering growth investment, business portfolios, and resource allocation. Guidelines issued on August 3 also encourage investment in intangible assets, including IP, brands, data, and human and organizational capabilities. These measures aim to redirect corporate resources toward growth and improve capital efficiency and potential growth.

Meanwhile, concerns about expansionary fiscal policy and the administration's preference for monetary accommodation drove JGB yields higher and weakened the yen in July. **Discussion also emerged over whether the GPIF should increase its investment in domestic assets**. After Japanese intervention and a US rate check on July 30, Japan and the US conducted coordinated intervention on July 31. Intervention may slow depreciation but cannot reverse structural pressures from a worsening trade balance and growing overseas investment.

The BOJ kept its policy rate at 1.0%, although board member Takata proposed 1.25%. **Governor Ueda emphasized upside inflation risks**, strengthening expectations of a September or October hike.

Cabinet and party reshuffles, food-tax-cut design, the autumn Diet session, and the FY2027 budget will now test the administration. If declining approval weakens policy execution, Japanese equities could lose an important source of support.

This Month's Topic (2): Potential Expansion of GPIF Investment in Domestic Assets

As yen interest rates rise and the currency weakens, some government officials have suggested that pension funds, including the Government Pension Investment Fund (GPIF), should increase their investment in domestic financial assets.

Q: How large is GPIF, and how much does it hold in yen bonds?
A: GPIF managed approximately ¥293.6 trillion as of end-March. Its new five-year portfolio allocates 25% each to domestic bonds, foreign bonds, domestic equities, and foreign equities, with permitted deviation ranges. Domestic bonds accounted for 26.9%, or about ¥79 trillion.

Q: Has GPIF supported government bonds before?
A: Before its 2014 reform, GPIF's 60% domestic-bond allocation made it a stable holder of JGBs. Concerns over excessive concentration and low expected returns led to reductions to 35% in 2014 and 25% in 2020. The current portfolio maintains the 25% target.

Q: Could the basic portfolio be changed soon?
A: Although the five-year plan was adopted only last fiscal year, annual reviews make changes institutionally possible. In practice, however, revising expected returns, risks, and consistency with pension finances would require extensive procedures. GPIF's president has also reiterated that investments must be made solely in beneficiaries' interests.

Q: Could GPIF use its deviation range to buy more JGBs?
A: Domestic bonds have a target allocation of 25%, with a permitted deviation range of ±6 percentage points, allowing the share to rise to 31%. From the current 26.9%, this theoretically leaves around ¥12 trillion of additional capacity. However, GPIF would need to explain which assets it would reduce and how the change would improve overall risk and return.
Higher domestic yields have improved expected bond returns, strengthening the medium-term rationale for increasing holdings. Yen bonds diversify equity risk, carry no currency risk, and match yen-denominated pension liabilities. Purchases could therefore be justified as long-term portfolio management rather than market support.

Q: Could GPIF stop yen yields from rising?
A: Purchases could improve sentiment and near-term supply-demand conditions, but their lasting effect would be limited. BOJ purchase reductions and continued government issuance mean the private sector must absorb more JGBs, while GPIF's purchasing capacity and timeframe are finite.

Q: What other measures could support demand?
A: Proposals include making retail JGBs eligible for NISA accounts and granting inheritance-tax incentives. Critics cite conflicts with the shift from savings to investment and concerns over tax fairness. Moreover, if households fund JGB purchases by withdrawing bank deposits, banks' own capacity to buy bonds may decline.

Q: What are the implications for equities and the yen?
A: Even limited yield restraint could ease corporate financing costs and support Japanese equities. If purchases were funded by selling foreign assets, they could generate yen buying, although hedging and execution methods would determine the actual effect. GPIF should therefore be viewed not as the primary tool for reversing yen weakness, but as playing a supplementary role in moderating the simultaneous rise in yen yields and depreciation of the yen, thereby helping stabilize Japan's equity risk premium.

Trends in Major Asset Prices

TOPIX (Daily)

Note: Latest data are for 31 Jul 2026

Source: SMDAM and Bloomberg

S&P500 (Daily)

Note: Latest data are for 31 Jul 2026

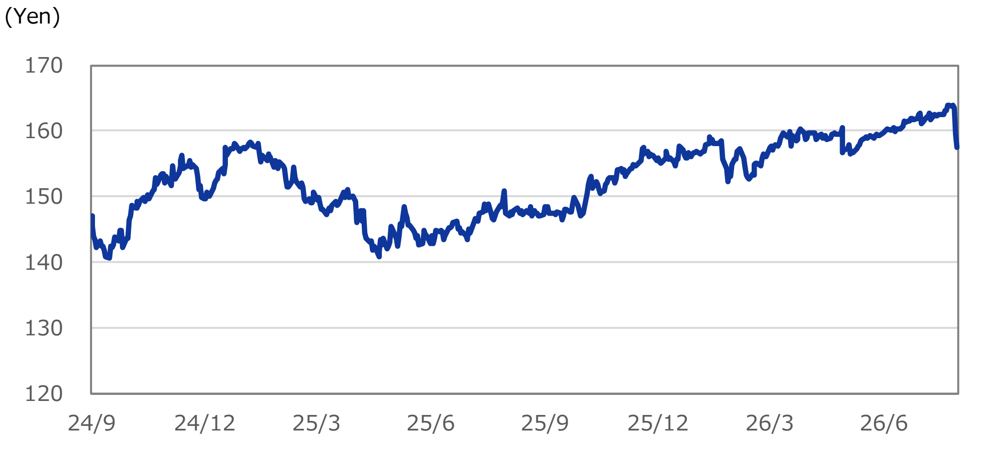
Source: SMDAM and Bloomberg

Japan 10-Year Government Bond Yield (Daily)

Note: Latest data are for 31 Jul 2026

Source: SMDAM and Bloomberg

USD/JPY (Daily)



Note: Latest data are for 31 Jul 2026

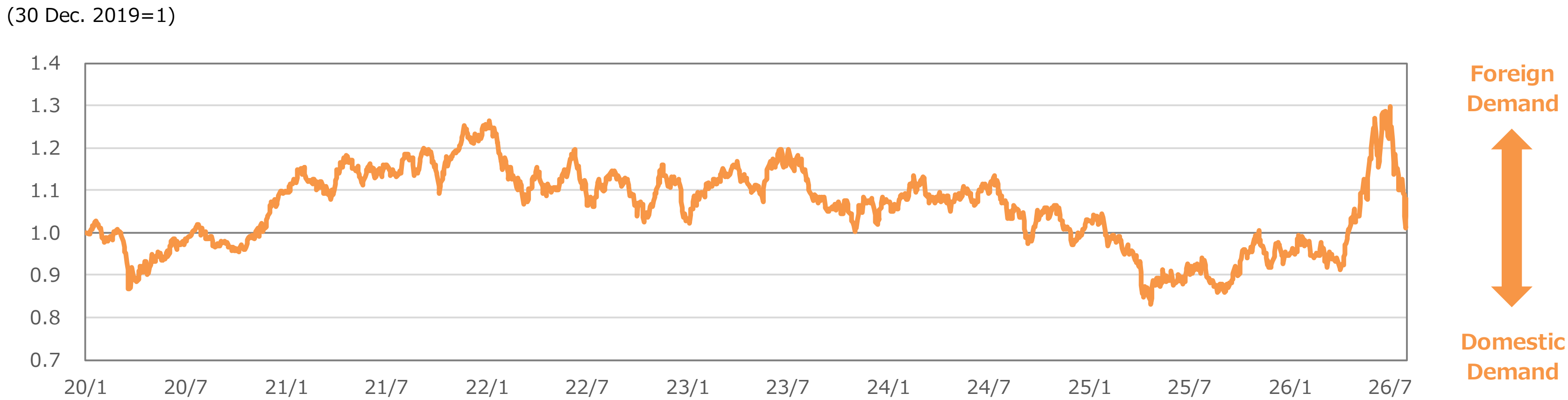
Source: SMDAM and Bloomberg

Trends in Value/Growth and Foreign/Domestic Demand for Japanese Stocks

Japanese Stocks: Value/Growth (Daily)

Note: Latest data are for 31 Jul 2026. Value/Growth represents Russell Nomura Total Market Value Index vs Growth with Dividend.
Source: SMDAM and Bloomberg

Japanese Stocks: Foreign Demand/Domestic Demand (Daily)

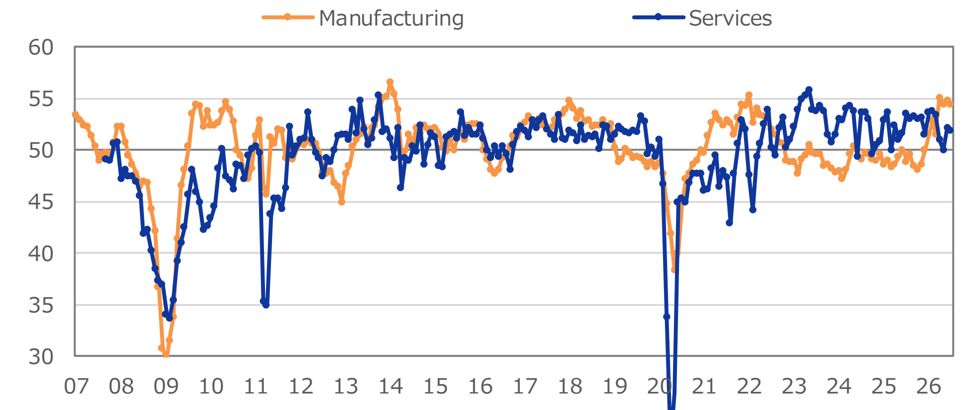


Note: Latest data are for 31 Jul 2026. Foreign/Domestic Demand represents Nikkei Global Exposure 50 vs Domestic.
Source: SMDAM and Bloomberg

Japanese Economic Indicators (1)

PMI

(sa, >50=improvement since previous month)

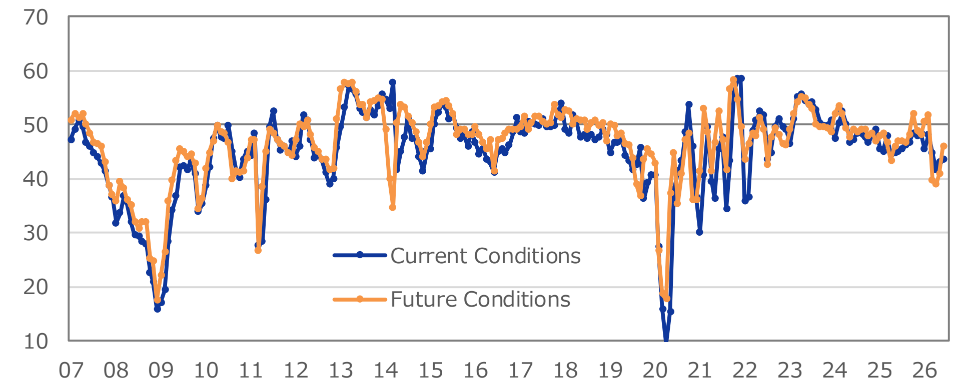


Note: Latest data are for Jul 2026 (Y)

Source: SMDAM and S&P Global

Economy Watchers Survey

(sa, DI)

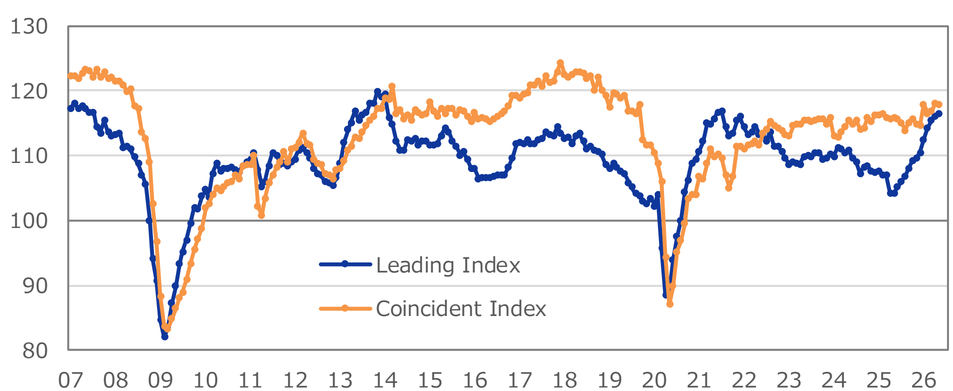


Note: Latest data are for Jun 2026 (Y)

Source: SMDAM and Cabinet Office

Index of Business Conditions

(sa, 2020=100)

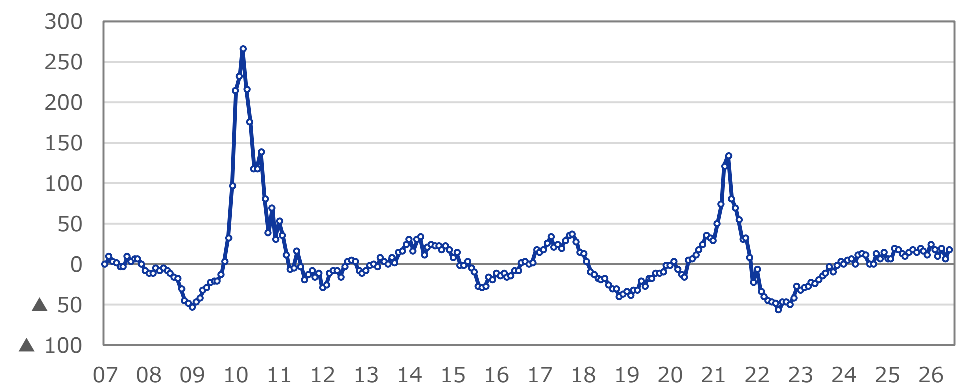


Note: Latest data are for May 2026 (Y)

Source: SMDAM and Cabinet Office

Machine Tools (Orders YoY - Order Backlogs YoY)

(%)



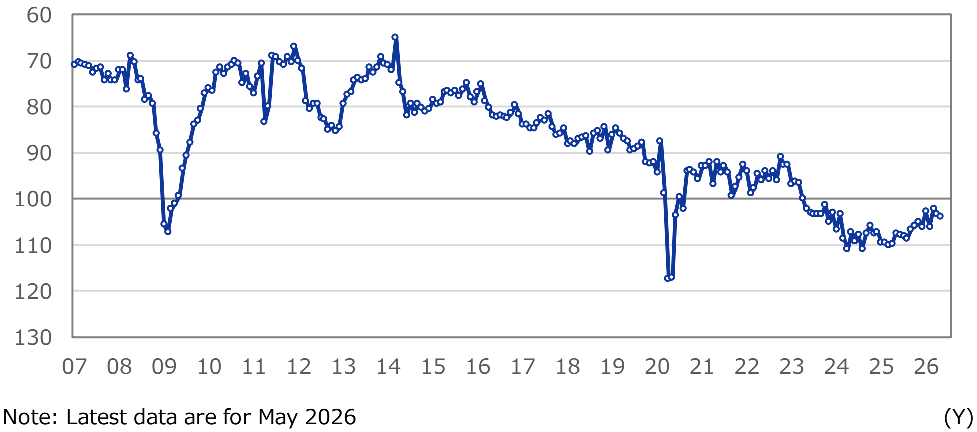
Note: Latest data are for Jun 2026 (Y)

Source: SMDAM and Japan Machine Tool Builders' Association

Japanese Economic Indicators (2)

Index of Producer's Inventory Ratio of Final Demand Goods

(sa, 2020=100, Inverted)

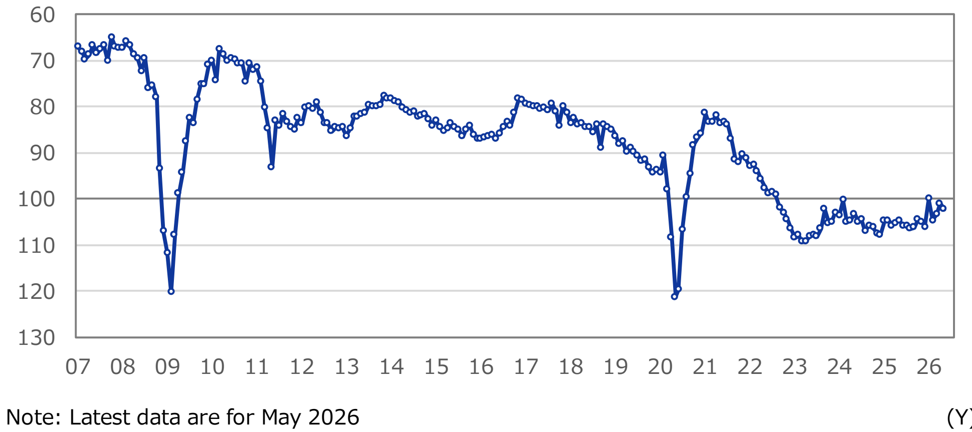


Note: Latest data are for May 2026

Source: SMDAM and Cabinet Office

Index of Producer's Inventory Ratio of Producer Goods

(sa, 2020=100, Inverted)

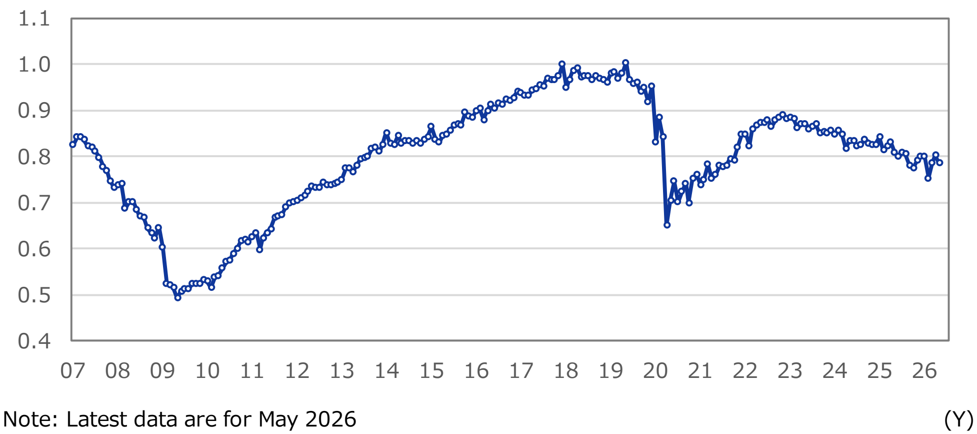


Note: Latest data are for May 2026

Source: SMDAM and Cabinet Office

New Job Offers (Excluding New School Graduates)

(sa, million persons)

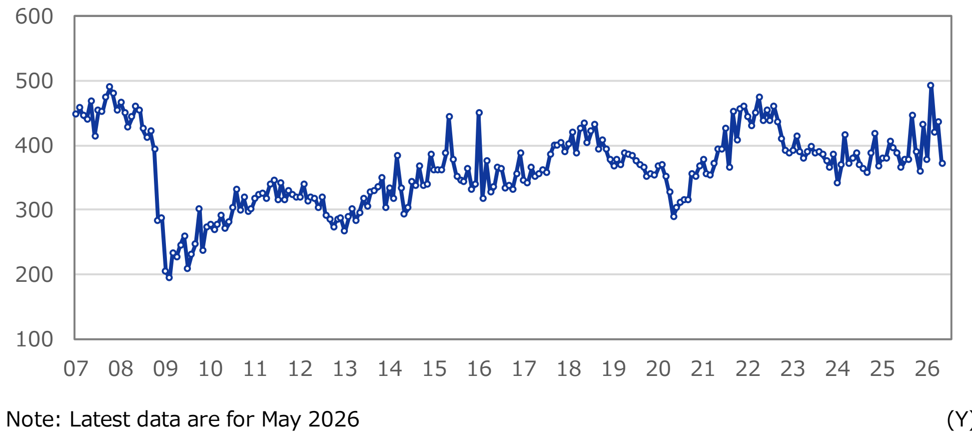


Note: Latest data are for May 2026

Source: SMDAM and Cabinet Office

Machinery Orders at Constant Prices (Manufacturing)

(sa, billion JPY)



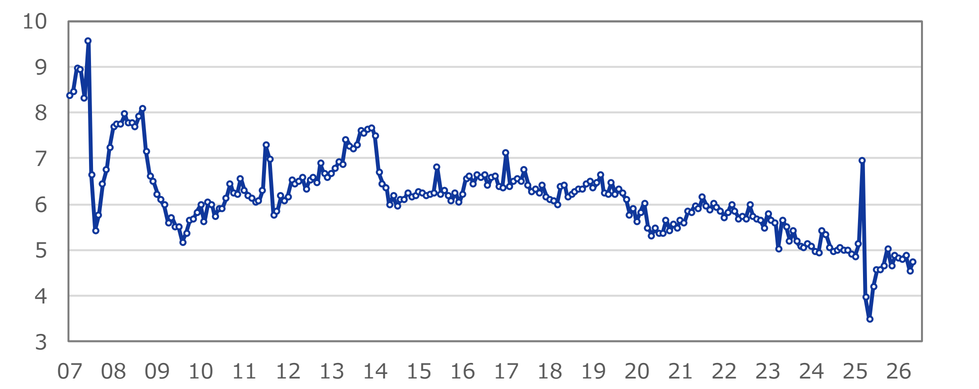
Note: Latest data are for May 2026

Source: SMDAM and Cabinet Office

Japanese Economic Indicators (3)

Total Floor Area of New Housing Construction Started

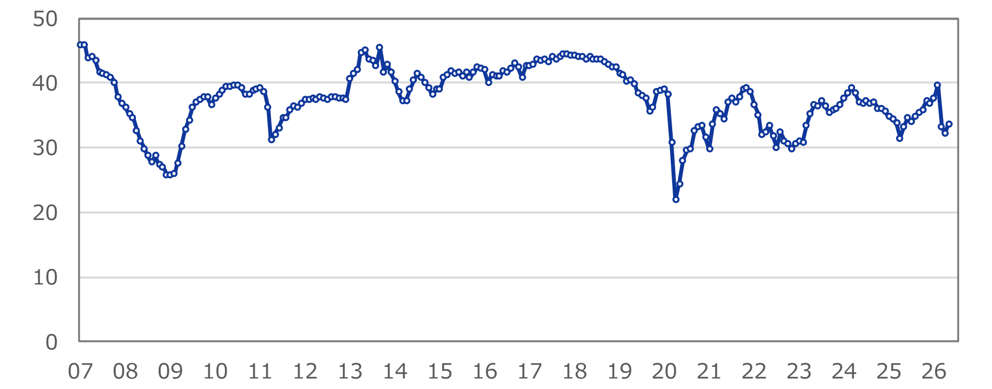
(million ㎡)



Note: Latest data are for May 2026 (Y)

Source: SMDAM and Cabinet Office

Consumer Confidence Index

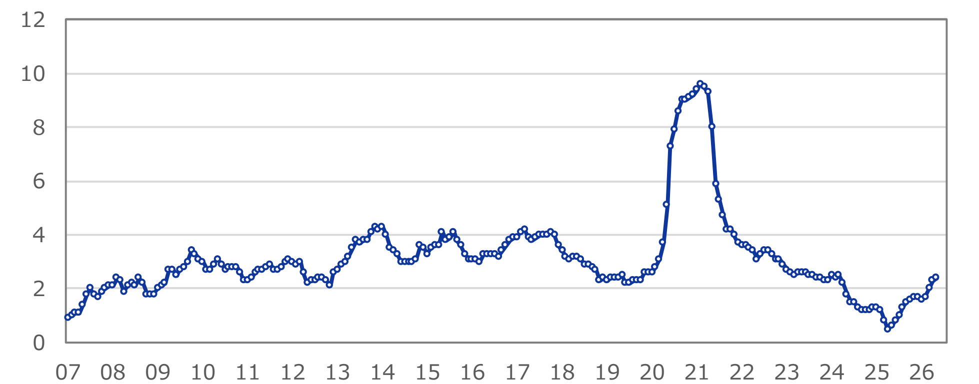


Note: Latest data are for May 2026 (Y)

Source: SMDAM and Cabinet Office

M2(YoY)

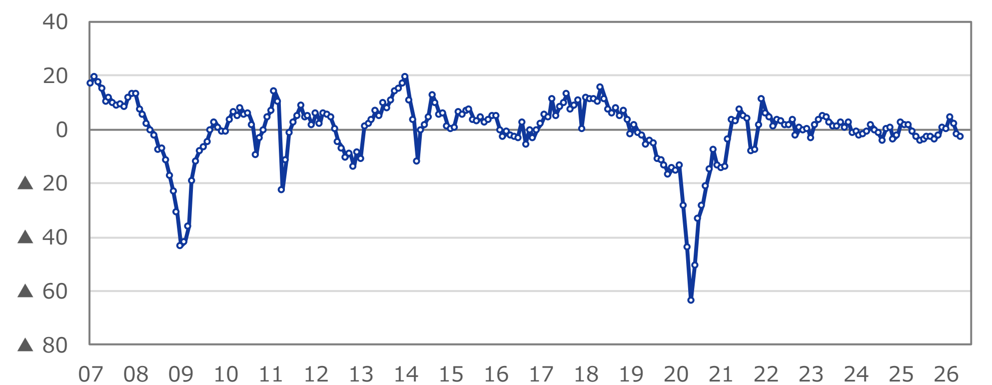
(%)



Note: Latest data are for May 2026 (Y)

Source: SMDAM and Cabinet Office

Sales Forecast DI of Small Businesses



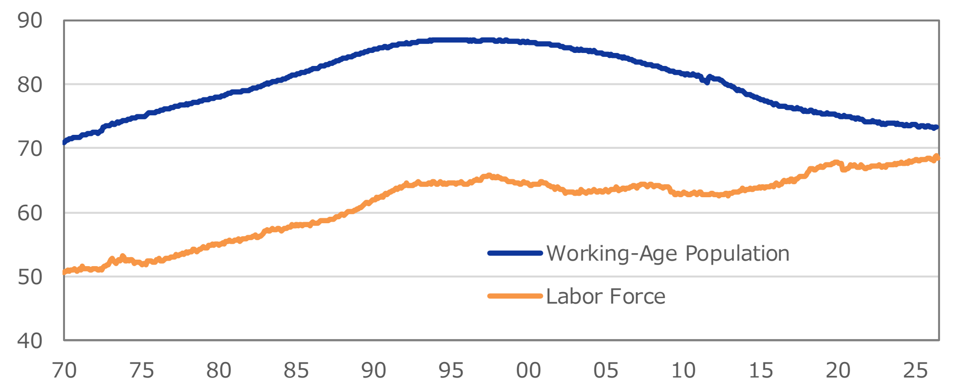
Note: Latest data are for May 2026 (Y)

Source: SMDAM and Cabinet Office

Japanese Economic Indicators (4)

Working-Age Population and Labor Force

(sa, million persons)

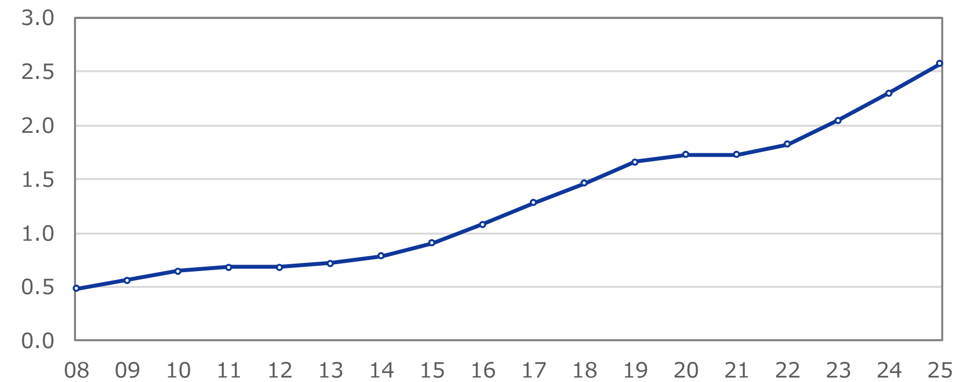


Note: Latest data are for May 2026 (Y)

Source: SMDAM and MIC

Number of Foreign Workers

(million persons)

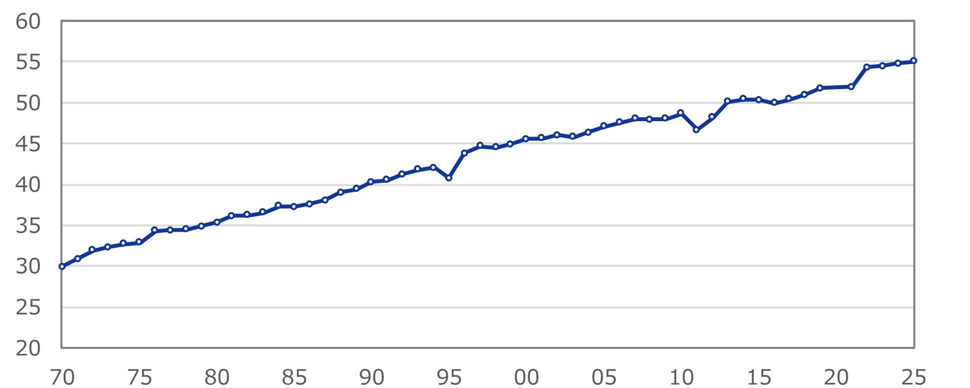


Note: Latest data are for 2025 (Y)

Source: SMDAM and MHLW

Number of Households

(million)

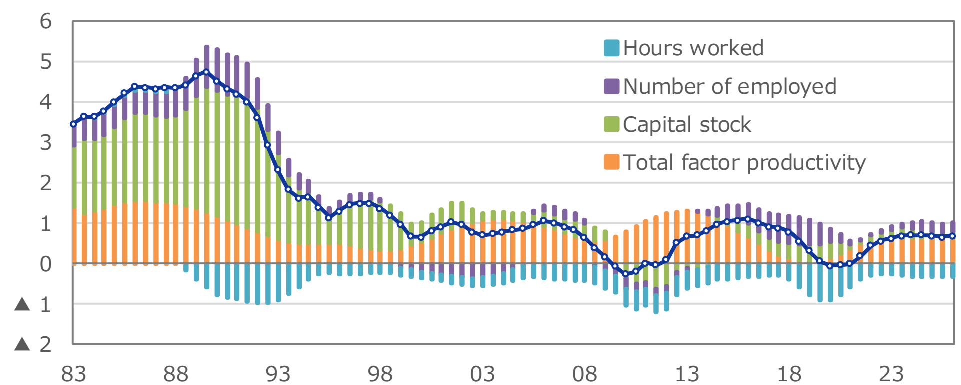


Note: Latest data are for 2025 (Y)

Source: SMDAM and Cabinet Office

Potential Growth Rate

(%)

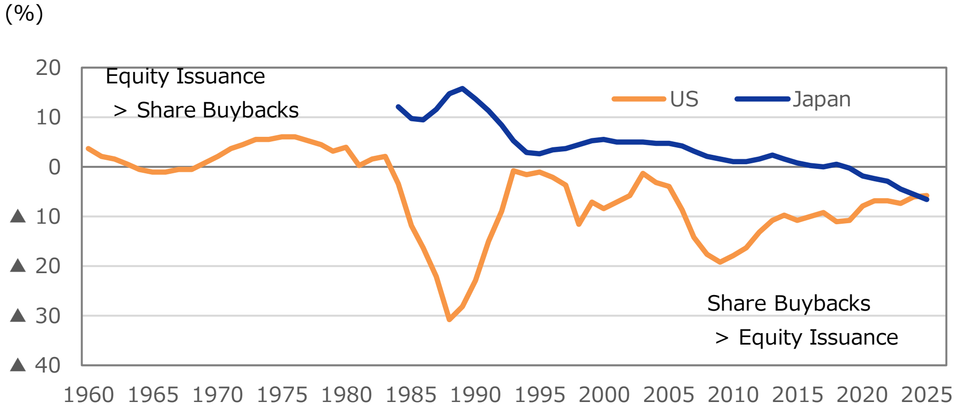


Note: Latest data are for 1Q 2026 (Y)

Source: SMDAM and BoJ

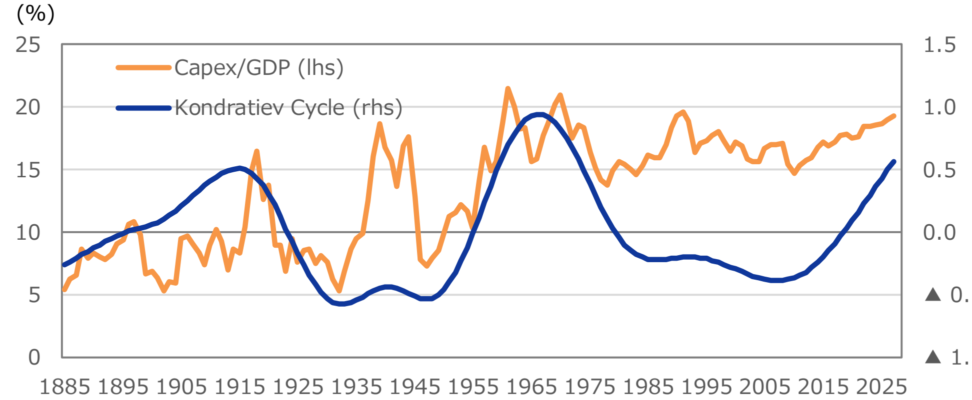
Japanese Economic Indicators (5)

Net Equity Issuance in Japan and the US



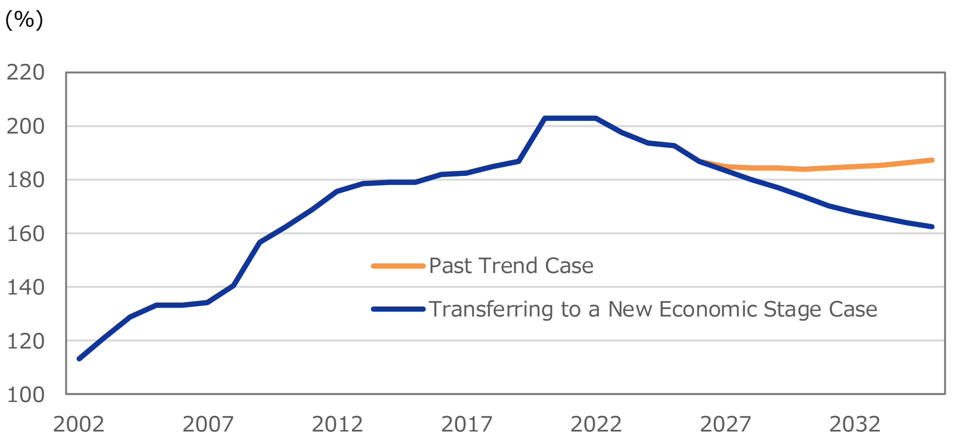
Note: Latest data are for 2025. (Y/FY)
Note: Net Equity Issuance / Market Cap (5Y MA)
Source: SMDAM, BoJ and FRB

Japan Capex/GDP Ratio (Long-Term Trend) and Kondratiev Cycle



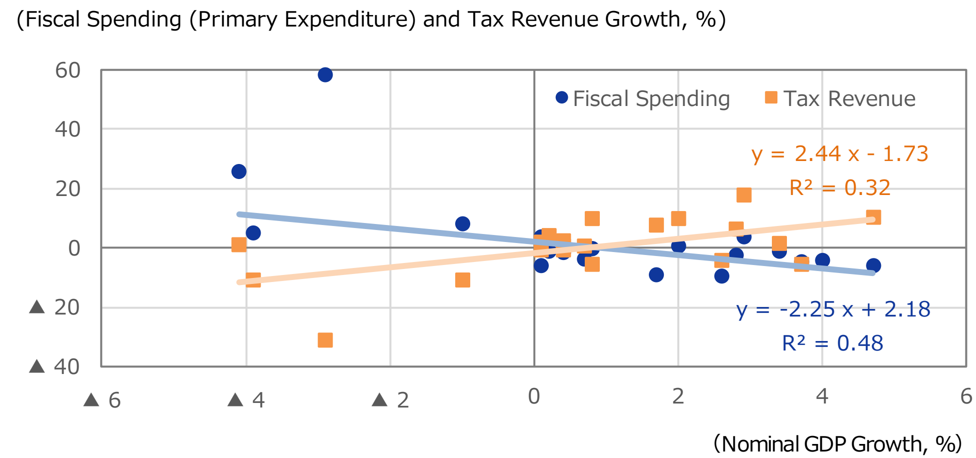
Note: Latest data are for 2027 (including some forecasts) (Y)
Note: Kondratiev Cycle is statistically derived as a 40 to 70 year cycle from the Capex/GDP ratio.
Source: SMDAM and Cabinet Office

Debt-to-GDP Projection (Medium to Long Term) by Cabinet Office



Note: Latest data are for 2035 (including some forecasts) (FY)
Note: New Economic Stage assumes 3% nominal growth. Source: SMDAM and Cabinet Office

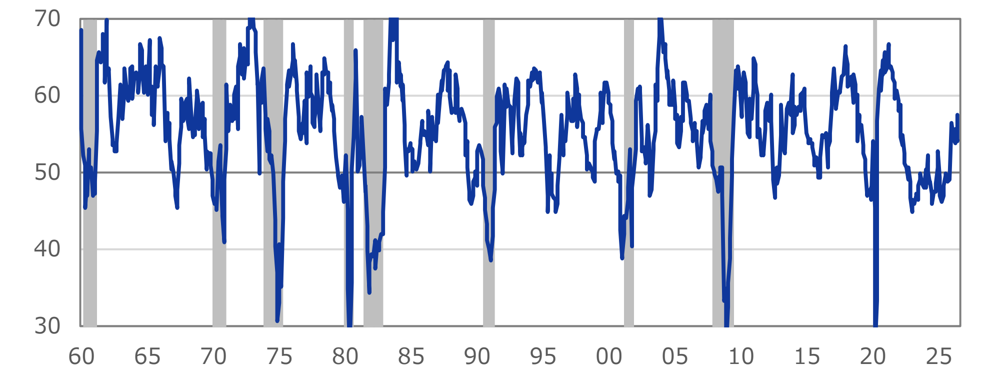
Fiscal Spending, Tax Revenue, and Nominal GDP Growth



Note: The Data covers FY2003 to 24, and the regression line is calculated excluding outliers.
Source: SMDAM and Cabinet Office

US Economic Indicators

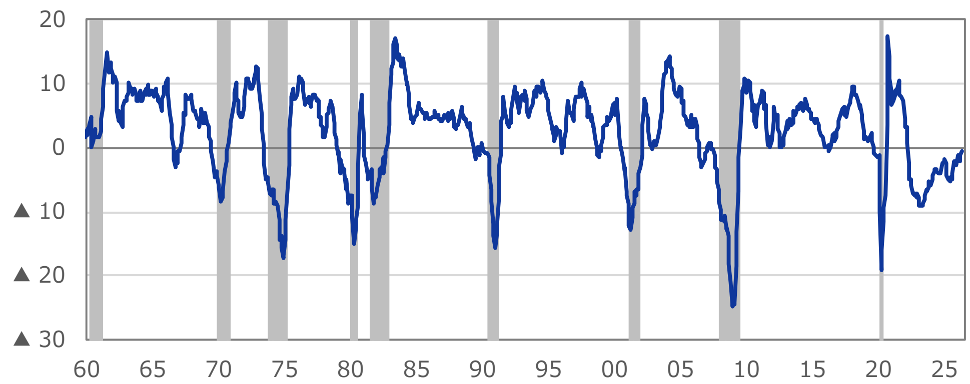
ISM Manufacturing PMI (Average of Production and New Orders)



Note: Latest data are for Jul 2026. The shaded areas represent periods of recession.
Source: SMDAM and ISM

Conference Board Leading Economic Index

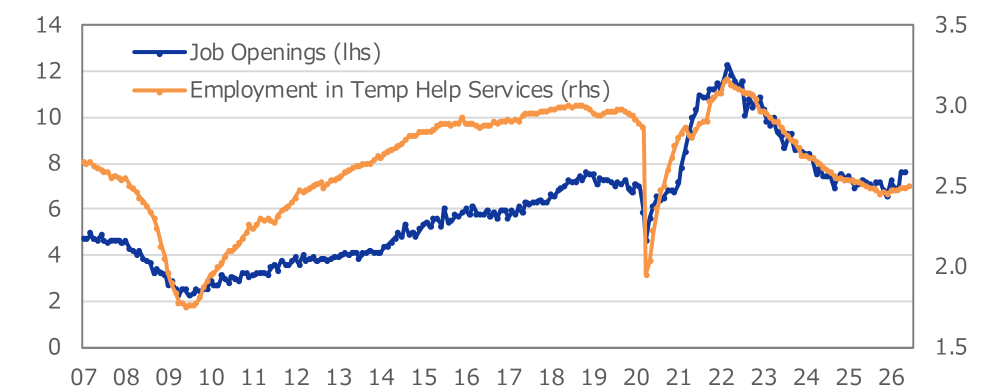
(6-Month Annual Change)



Note: Latest data are for Jun 2026. The shaded areas represent periods of recession.
Source: SMDAM and Conference Board

Job Openings and Employment in Temporary Help Services

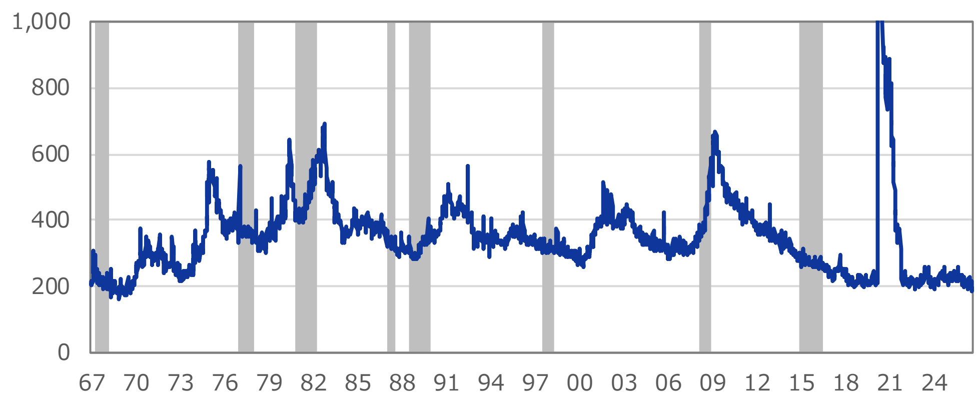
(sa, million persons) (sa, million persons)



Note: Latest data are for Jun 2026
Source: SMDAM and Bureau of Labor Statistics

Initial Jobless Claims

(sa, thousand persons)

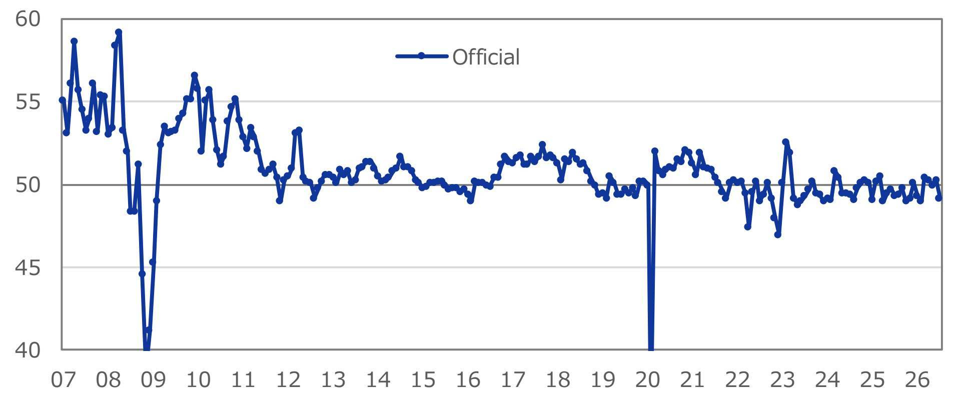


Note: Latest data are for 24 Jul 2026. The shaded areas represent periods of recession.
Source: SMDAM and Department of Labor

Overseas Economic Indicators

China Manufacturing PMI

(sa, >50=improvement since previous month)

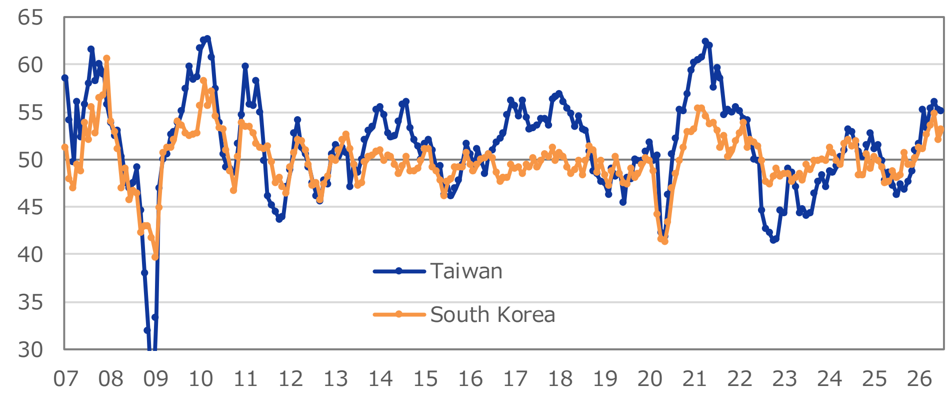


Note: Latest data are for Jul 2026

Source: SMDAM and China Federation of Logistics & Purchasing

Manufacturing PMI (Taiwan, South Korea)

(sa, >50=improvement since previous month)

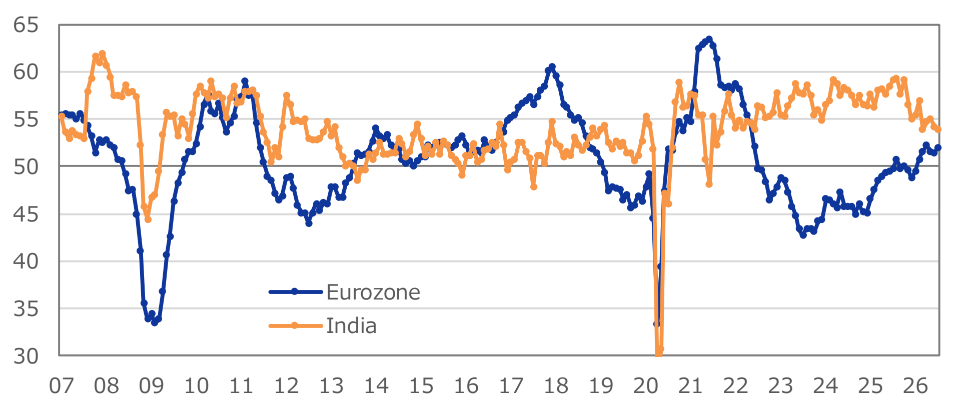


Note: Latest data are for Jul 2026

Source: SMDAM and S&P Global

Manufacturing PMI (Eurozone, India)

(sa, >50=improvement since previous month)

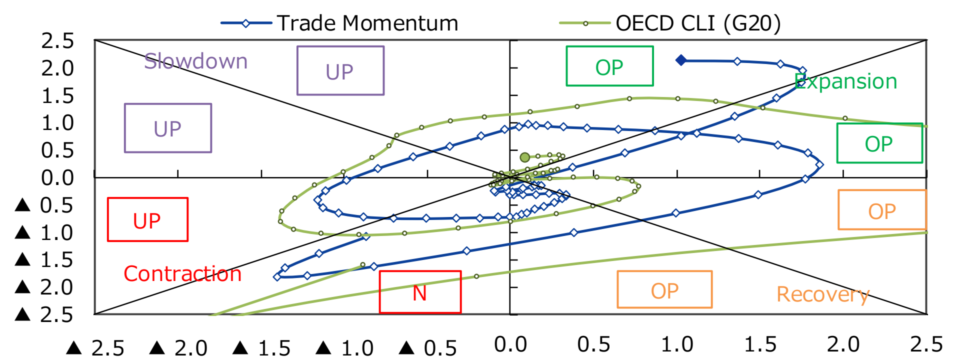


Note: Latest data are for Jul 2026

Source: SMDAM and S&P Global

Trade Momentum & OECD Composite Leading Indicator (CLI) Phases

Trade Momentum (Z-score) / OECD CLI Level (Index - 100)



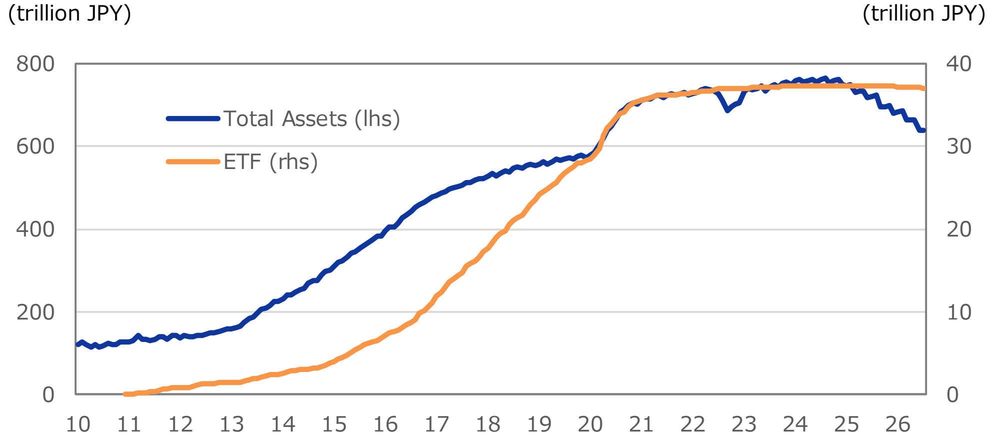
Note: Latest data are for Jun 2026

Note: Trade momentum shows cycles from indicators; OP/N/UP = past Japan stock performance

Source: SMDAM, OECD, S&P Global, LSEG and Bloomberg

BOJ Monetary Policy (1)

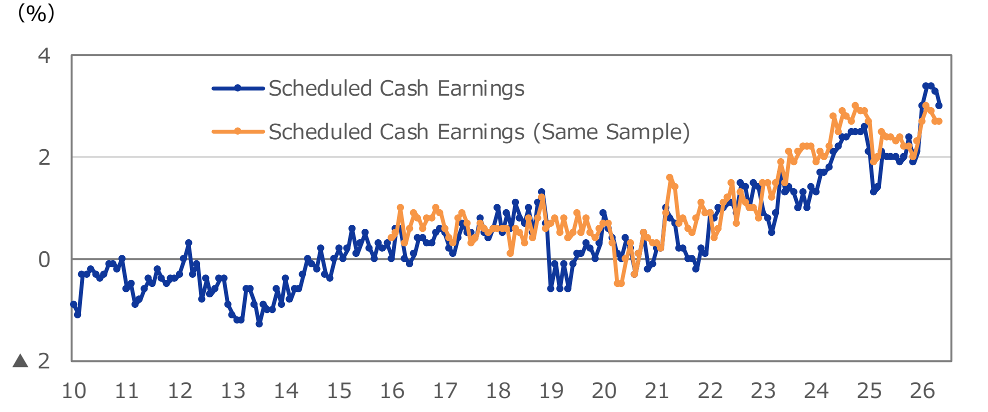
The Bank of Japan's Balance Sheet



Note: Latest data are for Jul 2026

Source: SMDAM and BoJ

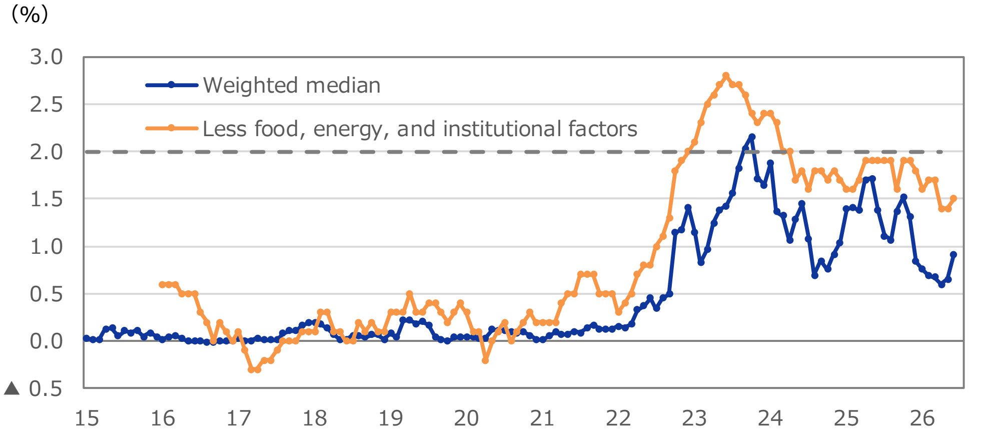
Nominal Wages (Scheduled Cash Earnings, YoY)



Note: Wage surveys change samples yearly. "Same Sample" uses only the same samples as the previous year to avoid gaps caused by such changes.

Note: Latest data are for May 2026 Source: SMDAM and MHLW

Indicators for Core CPI (YoY)



Note: Latest data are for Jun 2026

Source: SMDAM and BoJ

10-year Breakeven Inflation Rate

Note: Latest data are for 31 Jul 2026

Source: SMDAM and Bloomberg

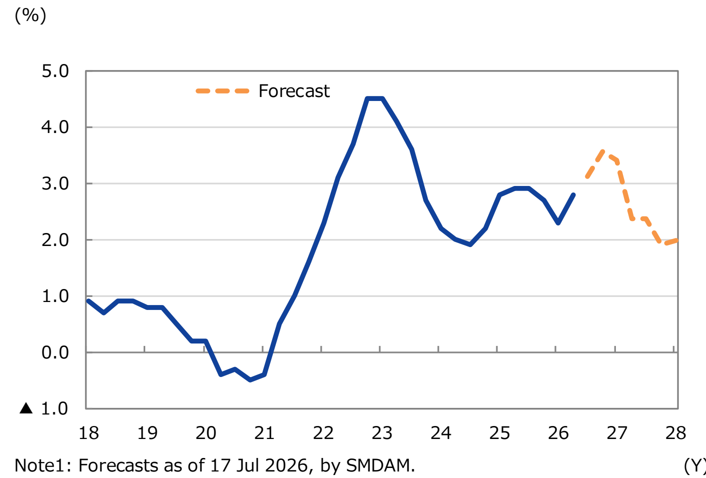
BOJ Monetary Policy (2)

BOJ Monetary Policy Developments (Quarter-End and Latest)

	Mar 2026	Jun 2026	Jul 2026
O/N call rate	around 0.75%	Around 1.0% (rate hike)	Around 1.0%
Rate on Deposit Facility	0.75%	1.0%	1.0%
Objection to the monetary policy guideline	Committee member Takata opposed the policy of maintaining the current level and proposed an increase to around 1.00%.	Committee member Asada dissented, arguing that the Bank should maintain the guideline for money market operations.	Committee member Takata opposed the policy of maintaining the current level and proposed an increase to around 1.25%.
Conduct of Monetary Policy	Given that real interest rates are at significantly low levels, if the outlook for economic activity and prices will be realized, the Bank, in accordance with improvement in economic activity and prices, will continue to raise the policy interest rate and adjust the degree of monetary accommodation.	Given that underlying CPI inflation has been approaching 2 percent and financial conditions have been accommodative, the Bank will continue to raise the policy interest rate and adjust the degree of monetary accommodation, in response to developments in economic activity and prices as well as financial conditions. In this regard, it will consider the timing and pace of adjustment, while closely monitoring the impact of the future course of the situation in the Middle East on Japan's economic activity and prices and examining the likelihood of realizing the baseline scenario of the outlook for economic activity and prices and the risks to the outlook.	Given that underlying CPI inflation has been approaching 2 percent and financial conditions have been accommodative, the Bank will continue to raise the policy interest rate and adjust the degree of monetary accommodation, in response to developments in economic activity and prices as well as financial conditions. In this regard, it will consider the timing and pace of adjustment, while examining the likelihood of realizing the baseline scenario of the outlook for economic activity and prices and the risks to the outlook, including the impact of the situation in the Middle East, the expansion in AI-related demand, and developments in foreign exchange rates.
JGB purchases	No Change	The Bank will reduce the planned amount of its monthly purchases of JGBs by, in principle, about 200 billion yen each calendar quarter until January-March 2027. From April 2027, the amount of its monthly purchases of JGBs will be about 2 trillion yen.	No Change
ETF Purchases	No Change	No Change	No Change

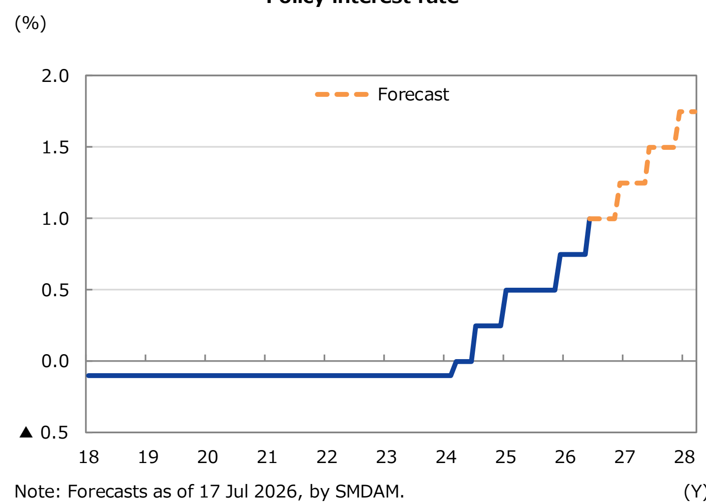
Note: Data as of 31 Jul 2026
Source: SMDAM and BOJ

CPI (less fresh food & institutional factors, YoY)



Note1: Forecasts as of 17 Jul 2026, by SMDAM.
Note2: Consumption tax-adjusted.
Source: SMDAM and BOJ

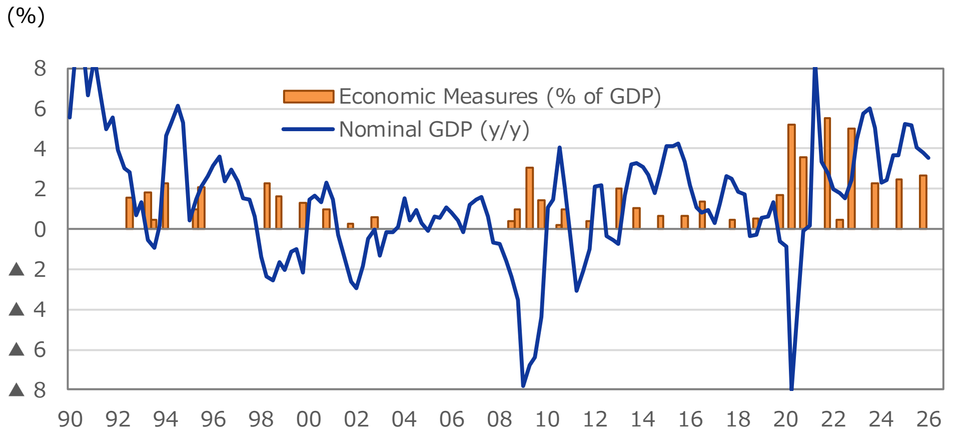
Policy interest rate



Note: Forecasts as of 17 Jul 2026, by SMDAM.
Source: SMDAM and BOJ

Japan’s Fiscal policy

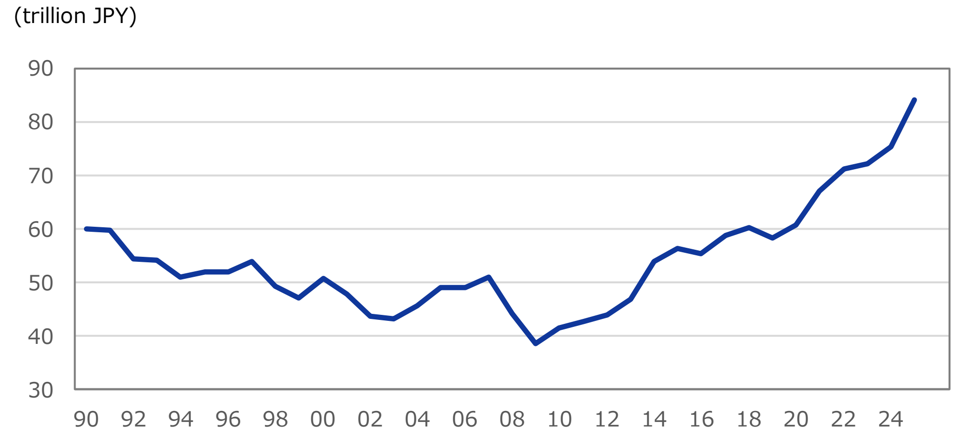
Government Economic Measures and Nominal GDP Growth Rate



Note: Latest data are for 1Q 2026. Economic measures are budget-backed amounts.

Source: SMDAM and Cabinet Office

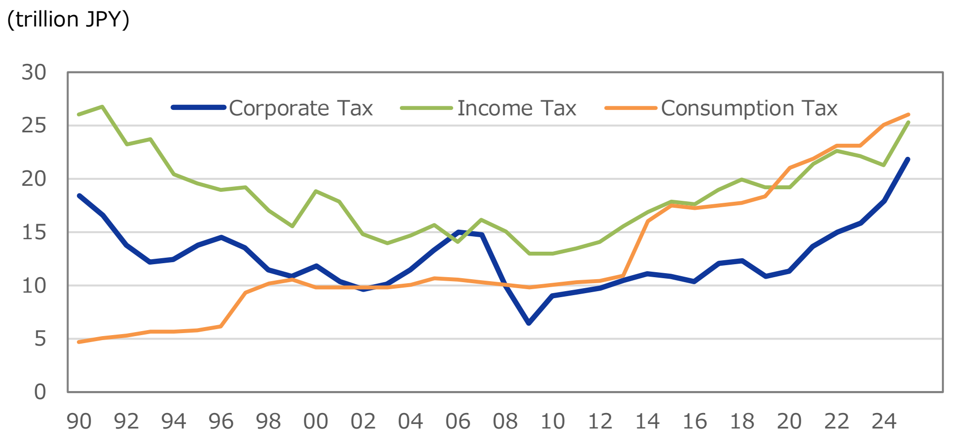
Japan's Tax Revenue



Note: Latest data are for FY2025

Source: SMDAM and MoF

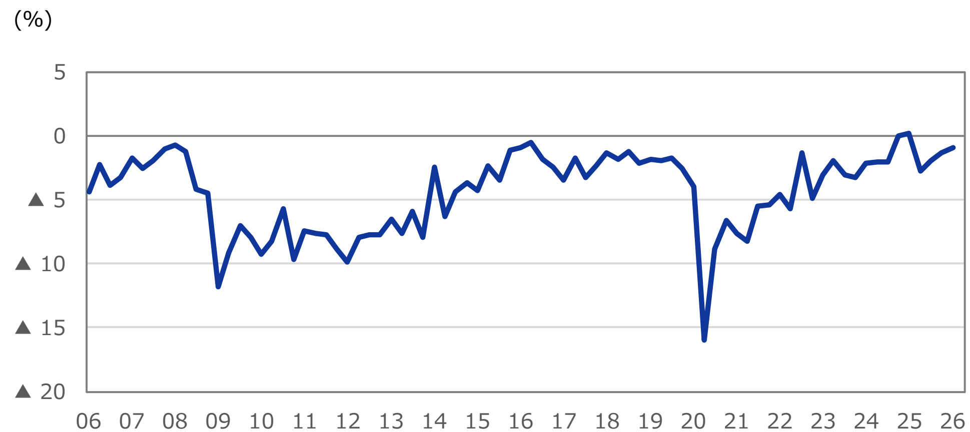
Breakdown of Tax Revenue



Note: Latest data are for FY2025

Source: SMDAM and MoF

Japan's Fiscal Balance (as a Percentage of GDP)

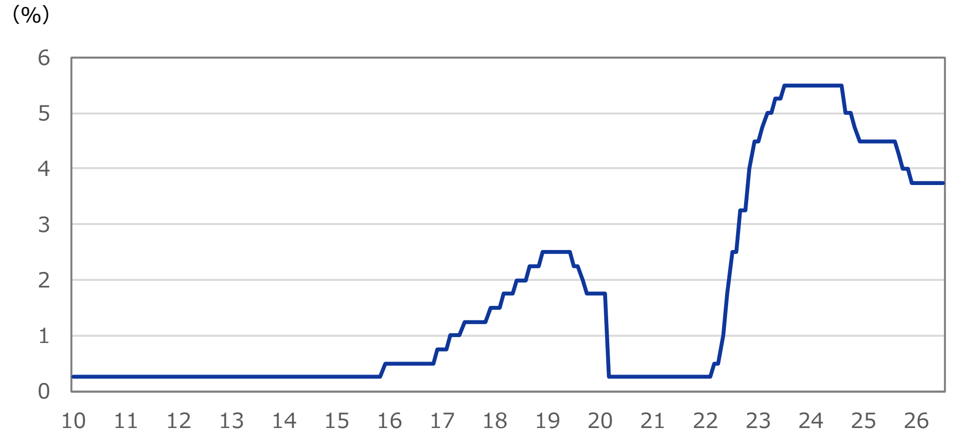


Note: Latest data are for 1Q 2026

Source: SMDAM and BoJ

Overseas Monetary Policy

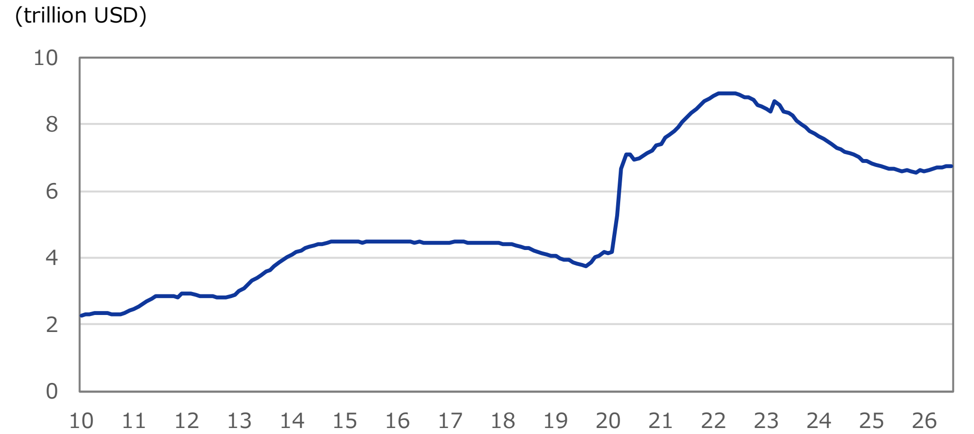
Federal Funds Target Rate (Upper Bound)



Note: Latest data are for Jul 2026

Source: SMDAM and FRB

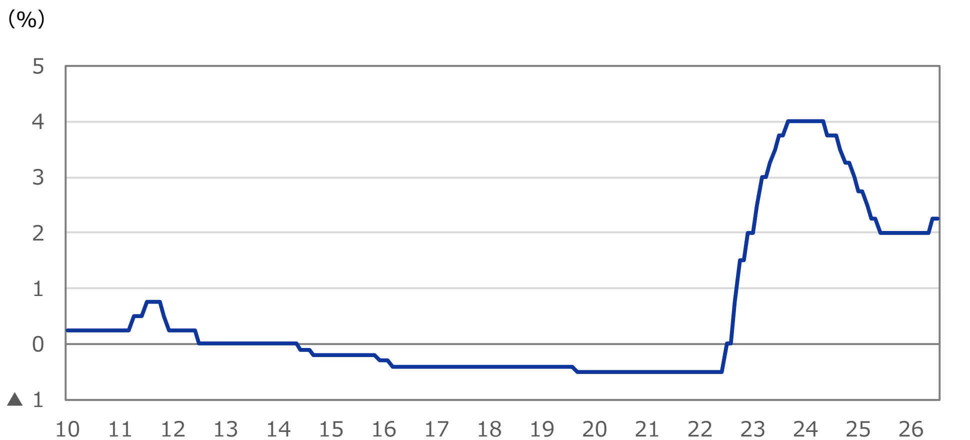
Federal Reserve Total Assets



Note: Latest data are for Jul 2026

Source: SMDAM and FRB

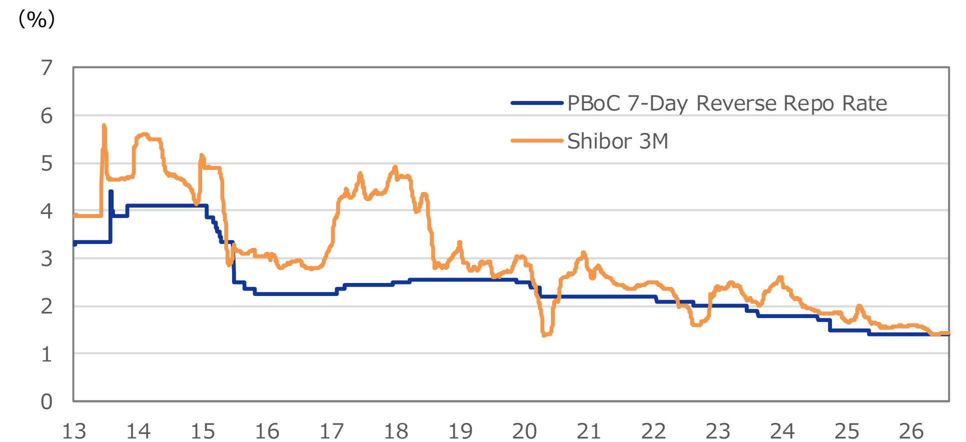
ECB Deposit Facility Announcement Rate



Note: Latest data are for Jul 2026

Source: SMDAM and ECB

China's Short-Term Interest Rates

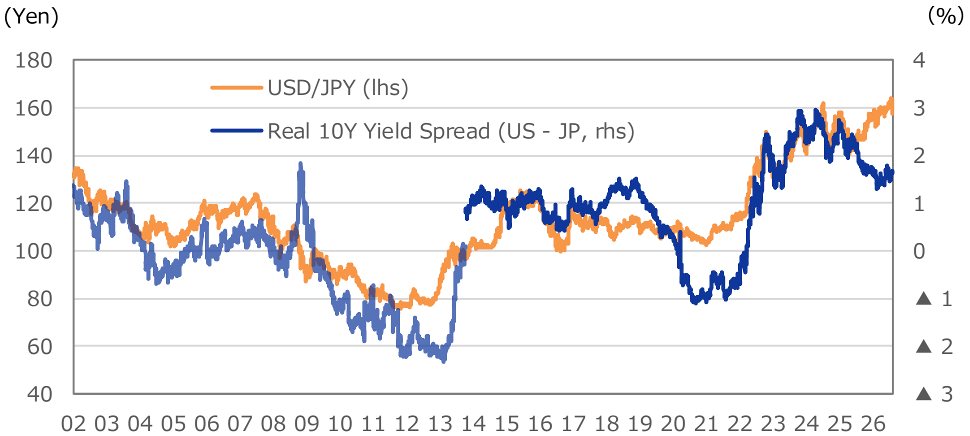


Note: Latest data are for 31 Jul 2026

Source: SMDAM, PBoC and Bloomberg

USD/JPY

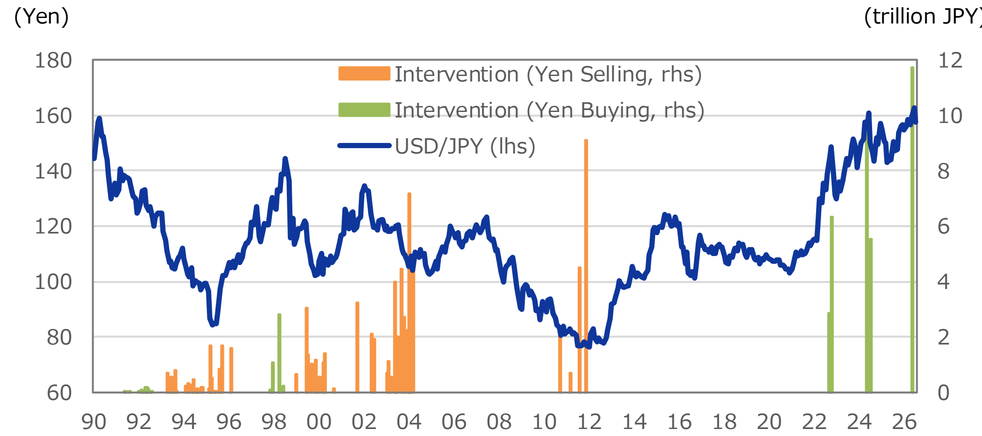
USD/JPY and Real Interest Rate Differential



Note: Latest data are for 31 Jul 2026. Japan's real rate pre-Oct. 8, 2013, based on core CPI.

Source: SMDAM and Bloomberg

USD/JPY and Intervention



Note: Latest data are for Jul 2026

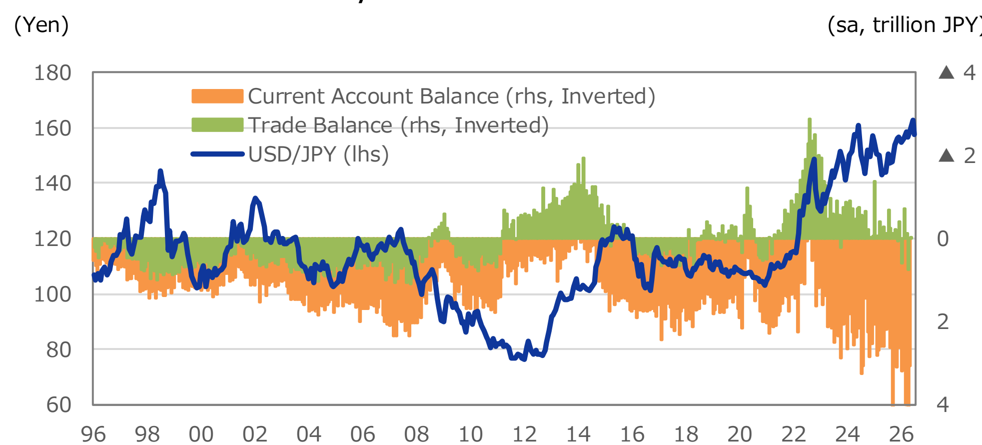
Source: SMDAM, MoF and Bloomberg

JPY Real Effective Exchange Rate

Note: Latest data are for Jun 2026

Source: SMDAM and BoJ

USD/JPY and External Balances



Note: Latest data are for Jul 2026

Source: SMDAM, MoF and Bloomberg

Earnings Forecast:

Bottom-Up Corporate Earnings Forecast for Japan

Forecasts as of 15 Jun 2026	FY24 billion JPY (A)	FY25 billion JPY (A)	FY26 billion JPY (E)	FY27 billion JPY (E)	FY25 YoY, % (A)	FY26 YoY, % (E)	FY27 YoY, % (E)
Revenue							
Total (Ex-Financials)	688,760	707,743	764,815	796,418	+2.8	+8.1	+4.1
Manufacturing	405,212	414,512	452,488	471,783	+2.3	+9.2	+4.3
Non-Manufacturing	283,549	293,231	312,327	324,635	+3.4	+6.5	+3.9
Total (Ex-Financials, Ex-SoftBank G)	681,517	699,944	756,280	787,333	+2.7	+8.0	+4.1
Operating Profit							
Total (Ex-Financials)	60,181	63,364	77,383	83,354	+5.3	+22.1	+7.7
Manufacturing	33,638	33,323	47,838	54,938	▲ 0.9	+43.6	+14.8
Non-Manufacturing	26,543	30,041	29,545	28,416	+13.2	▲ 1.6	▲ 3.8
Total (Ex-Financials, Ex-SoftBank G)	55,750	56,083	73,148	82,590	**+0.6**	**+30.4**	**+12.9**
Ordinary Profit							
Total (Ex-Financials)	62,528	66,984	81,070	86,528	+7.1	+21.0	+6.7
Manufacturing	35,920	35,650	49,534	56,459	▲ 0.8	+38.9	+14.0
Non-Manufacturing	26,608	31,334	31,536	30,069	+17.8	+0.6	▲ 4.6
Total (Ex-Financials, Ex-SoftBank G)	60,823	60,850	76,835	85,764	**+0.0**	**+26.3**	**+11.6**
Profit After Taxes							
Total (Incl. Financials)	52,161	56,259	68,135	71,826	+7.9	+21.1	+5.4
Total (Ex-Financials)	42,718	44,485	57,212	59,631	+4.1	+28.6	+4.2
Manufacturing	24,106	22,488	34,758	39,550	▲ 6.7	+54.6	+13.8
Non-Manufacturing	18,612	21,997	22,455	20,081	+18.2	+2.1	▲ 10.6
Total (Ex-Financials, Ex-SoftBank G)	41,565	39,482	53,962	59,920	▲ 5.0	+36.7	+11.0

Note1: Forecasts by SMDAM.

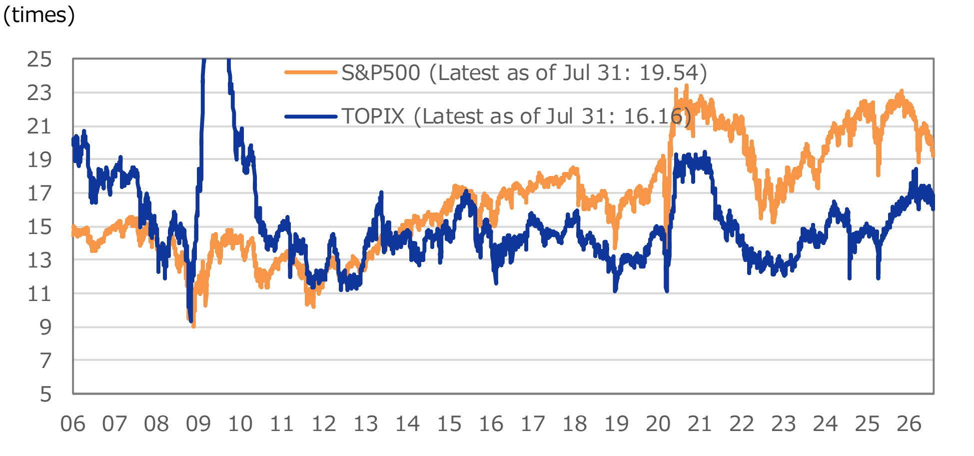
Note2: FX assumptions are USD/JPY at 159 and EUR/JPY at 186. A 1 JPY depreciation vs. USD increases ordinary profit by approximately 0.5%.

Note3: Coverage includes 402 Total (Incl. Financials), 376 Total (Ex-Financials), 226 Manufacturing, and 150 Non-Manufacturing stocks.

Note4: Aggregated earnings figures are based on in-house corporate forecasts and provided for reference only. Accuracy is not fully guaranteed.

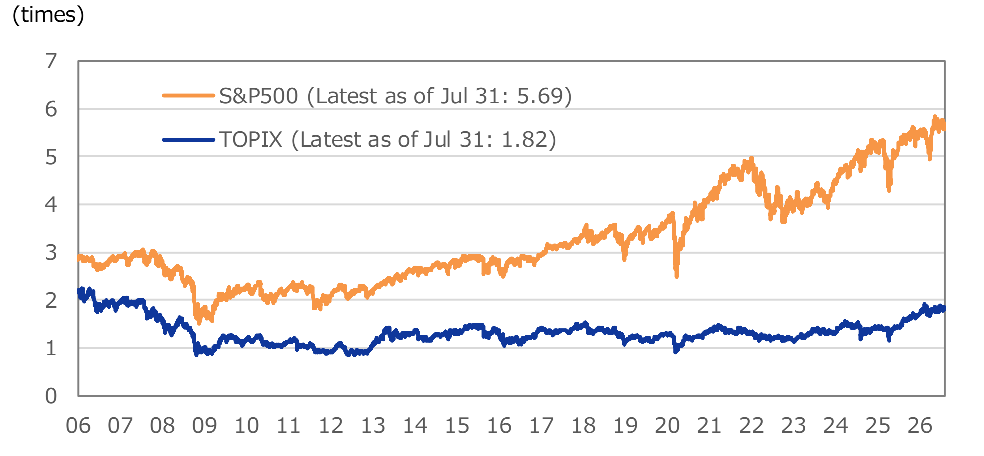
Valuation (1)

S&P 500 and TOPIX 12-Month Forward P/E Ratio



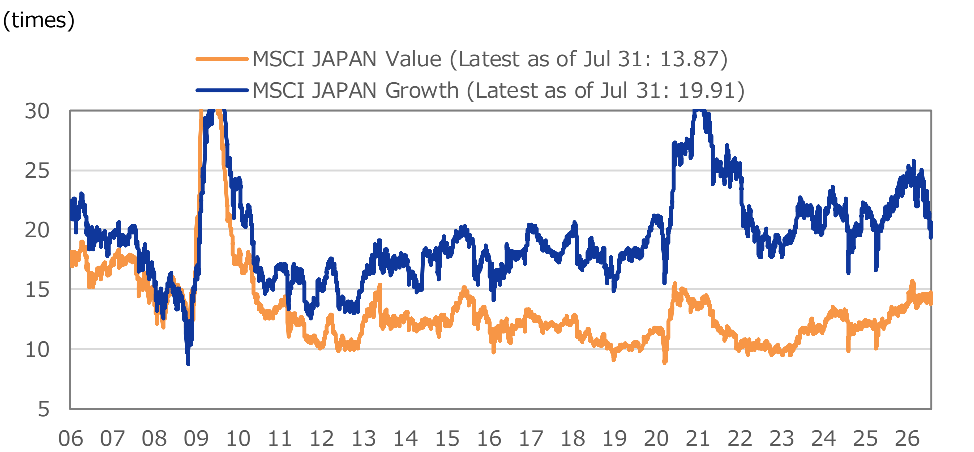
Note: Latest data are for 31 Jul 2026
Source: SMDAM and Bloomberg

S&P 500 and TOPIX Historical P/B Ratio



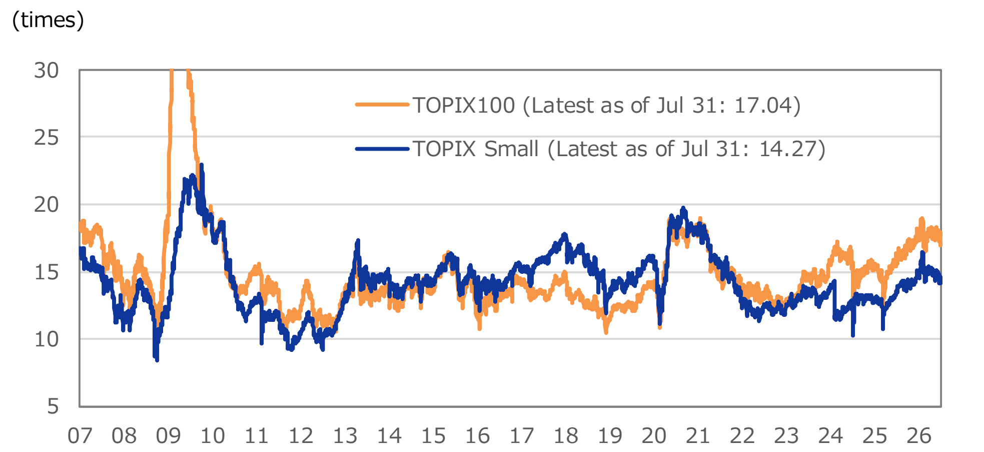
Note: Latest data are for 31 Jul 2026
Source: SMDAM and Bloomberg

MSCI Japan 12-Month Forward P/E Ratio



Note: Latest data are for 31 Jul 2026
Source: SMDAM and Bloomberg

TOPIX 100 and TOPIX Small 12M Forward P/E Ratio



Note: Latest data are for 31 Jul 2026
Source: SMDAM and Bloomberg

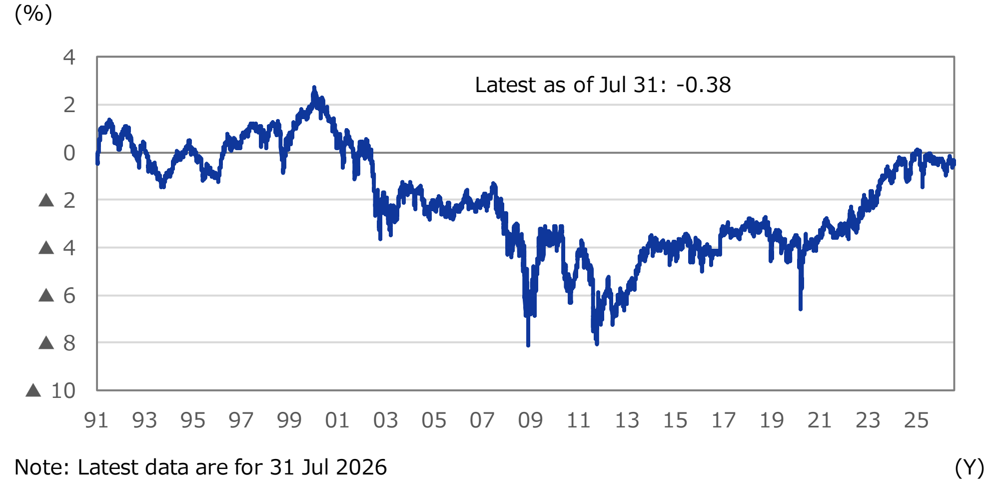
Valuation (2)

TOPIX Yield Spread (10Y JGB - Earnings Yield)

Note: Latest data are for 31 Jul 2026

Source: SMDAM and Bloomberg

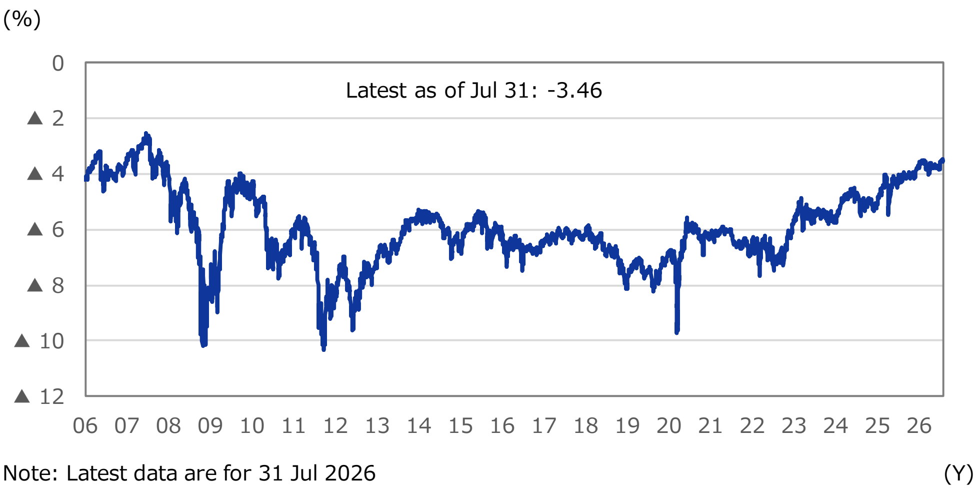
S&P 500 Yield Spread (10Y UST - Earnings Yield)



Note: Latest data are for 31 Jul 2026

Source: SMDAM and Bloomberg

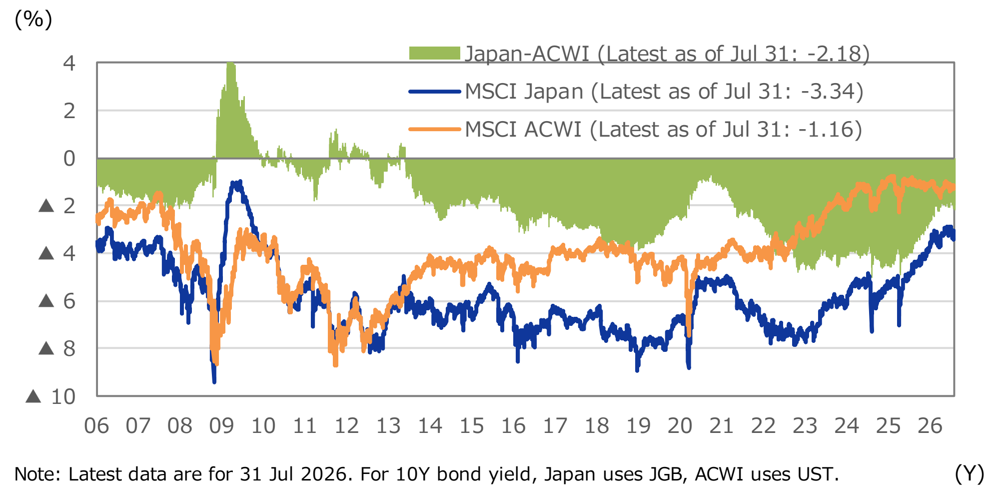
STOXX Europe 600 Yield Spread (10Y Bund - Earnings Yield)



Note: Latest data are for 31 Jul 2026

Source: SMDAM and Bloomberg

MSCI Japan and ACWI Yield Spread (10Y Bond Yield - Earnings Yield)



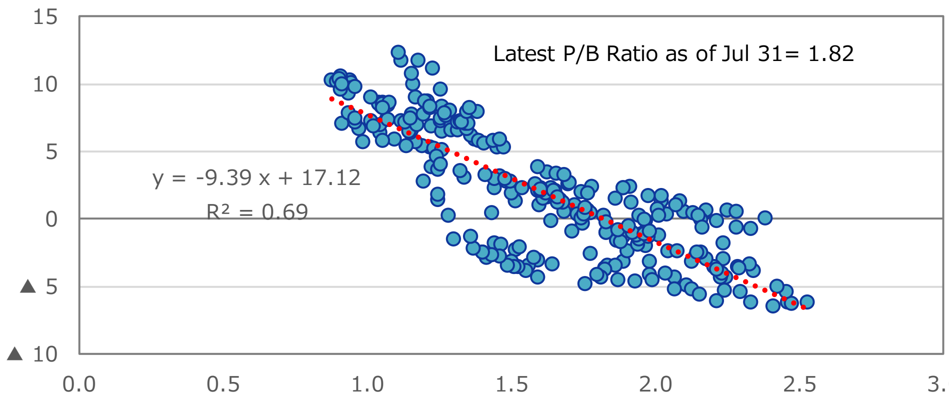
Note: Latest data are for 31 Jul 2026. For 10Y bond yield, Japan uses JGB, ACWI uses UST.

Source: SMDAM and Bloomberg

Valuation and Return

TOPIX Historical P/B Ratio and 10Y Annualized Return (From Oct. 1993)

10Y Annualized Return (%)

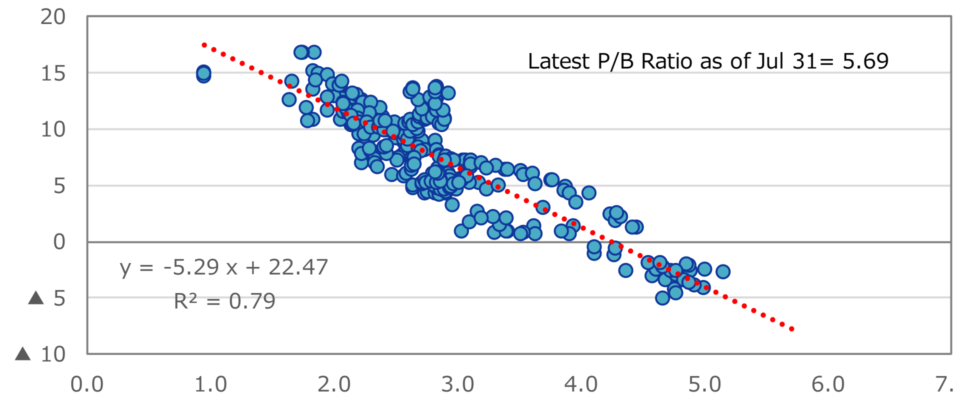


Note: Latest data are for Jul 2026 TOPIX Historical P/B Ratio (times)

Source: SMDAM and Bloomberg

S&P500 Historical P/B Ratio and 10Y Annualized Return (From May 1990)

10Y Annualized Return (%)

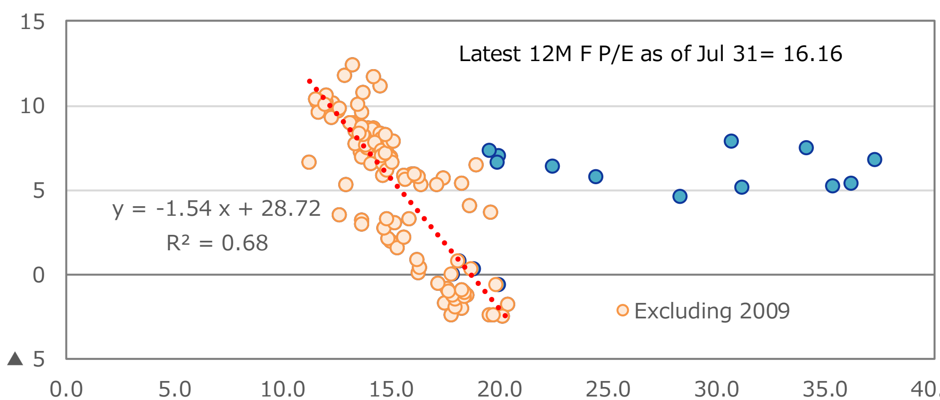


Note: Latest data are for Jul 2026 S&P500 Historical P/B Ratio (times)

Source: SMDAM and Bloomberg

TOPIX 12M Forward P/E and 10Y Annualized Return (From Jul. 2005)

10Y Annualized Return (%)

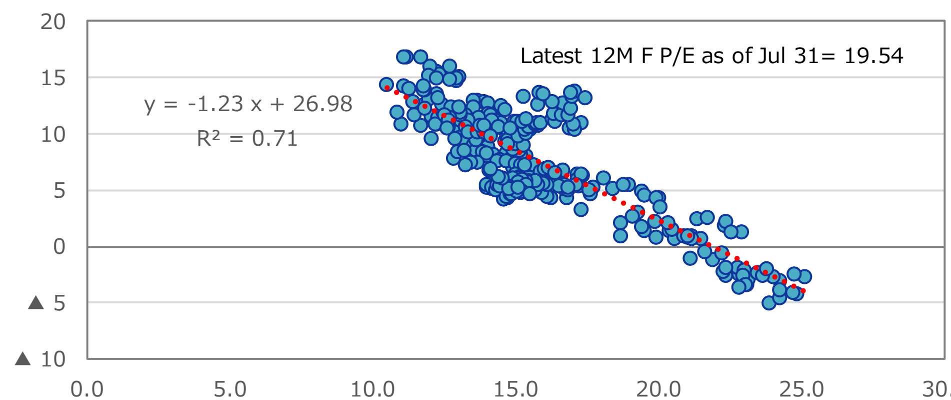


Note: Latest data are for Jul 2026. The blue dots show 2009 data. TOPIX 12M Forward P/E (times)

Source: SMDAM and Bloomberg

S&P500 12M Forward P/E and 10Y Annualized Return (From Jan. 1990)

10Y Annualized Return (%)

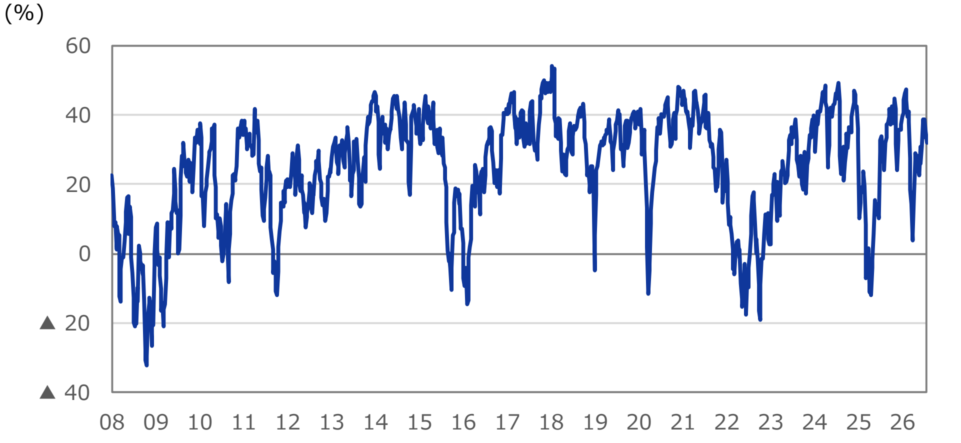


Note: Latest data are for Jul 2026 S&P500 12M Forward P/E (times)

Source: SMDAM and Bloomberg

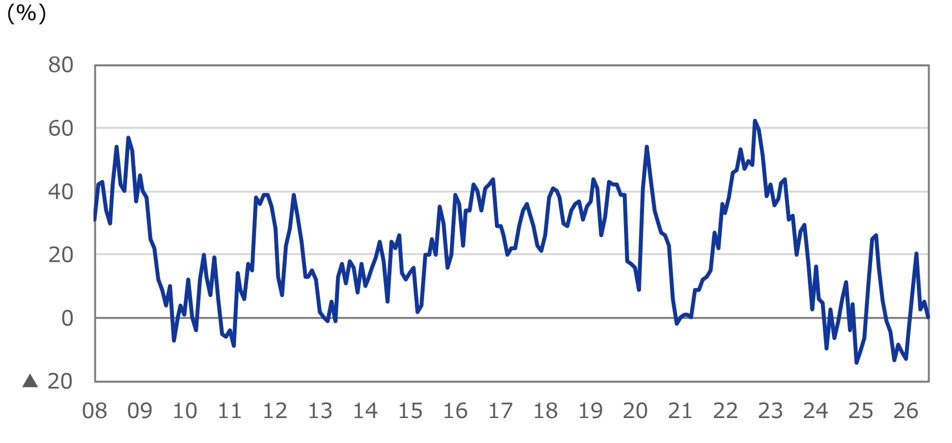
Stock Market Sentiment and Supply-Demand

Investors Intelligence Bull-Bear Spread



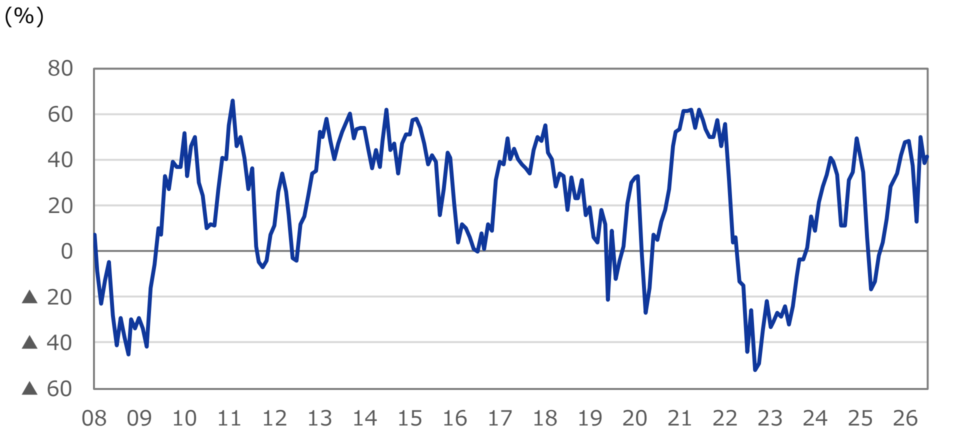
Note: Latest data are for 24 Jul 2026
Source: SMDAM and LSEG

FM Survey: Cash Net Balance



Note: Latest data are for Jul 2026
Source: SMDAM and BofA

FM Survey: Equities Net Balance



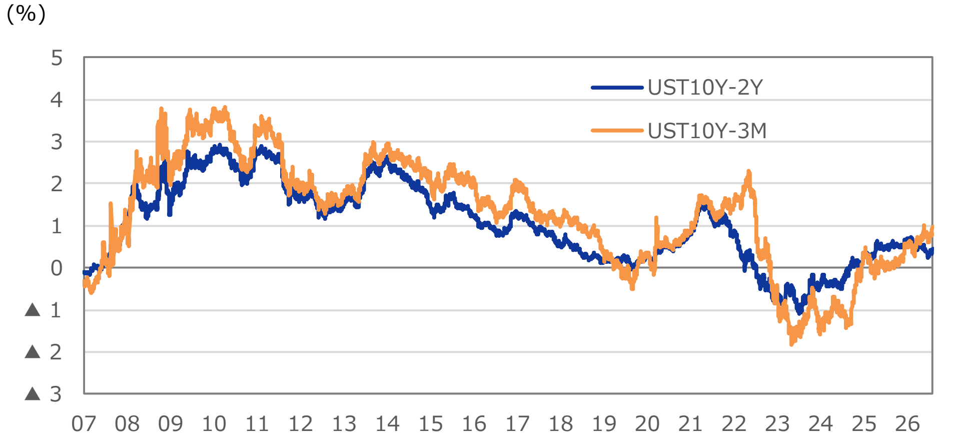
Note: Latest data are for Jul 2026
Source: SMDAM and BofA

FM Survey: Japanese Equities Net Balance

Note: Latest data are for Jul 2026
Source: SMDAM and BofA

Risk Indicators

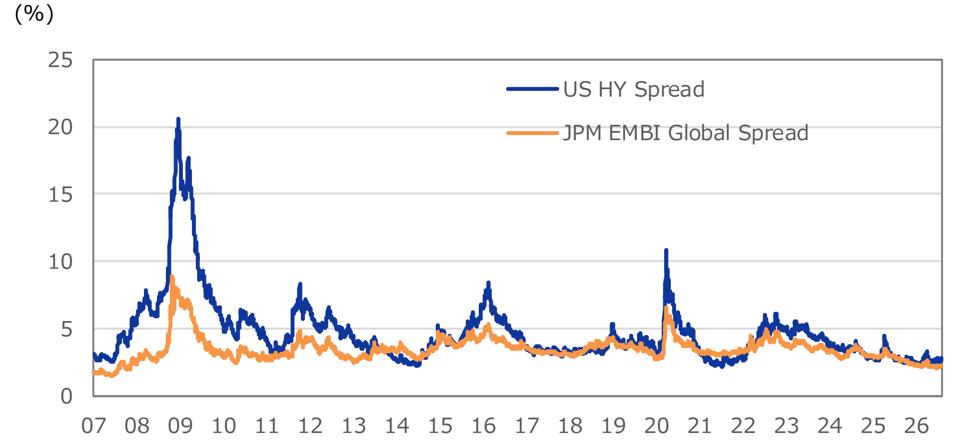
US Yield Curve Spread



Note: Latest data are for 31 Jul 2026

Source: SMDAM and Bloomberg

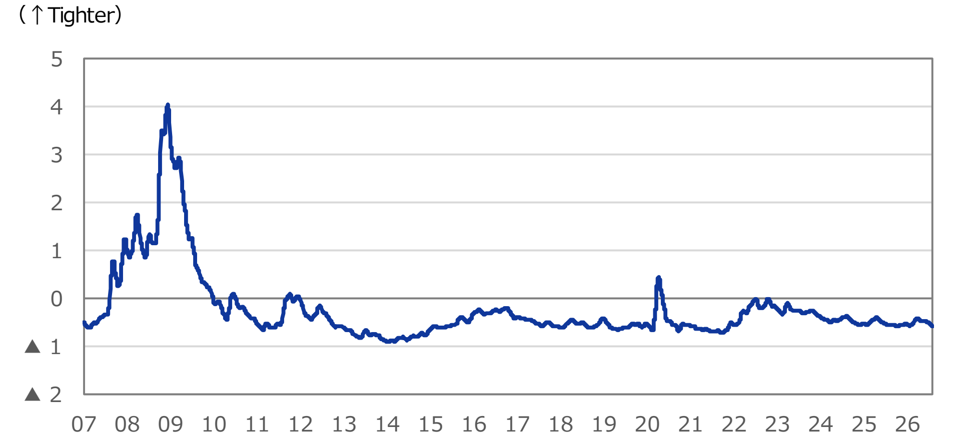
US HY Spread and EM Spread



Note: Latest data are for 31 Jul 2026

Source: SMDAM and Bloomberg

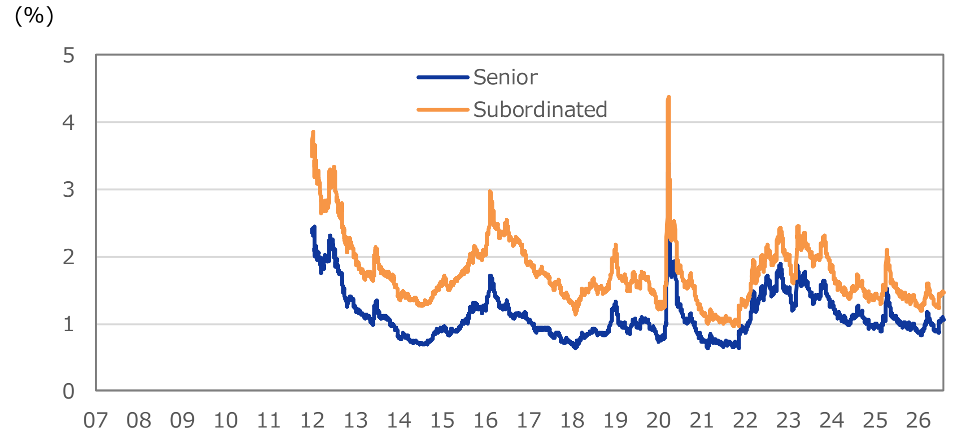
Chicago Fed Adjusted National Financial Conditions Index (ANFCI)



Note: Latest data are for 31 Jul 2026

Source: SMDAM, Chicago Fed and Bloomberg

USD IG Financials OAS

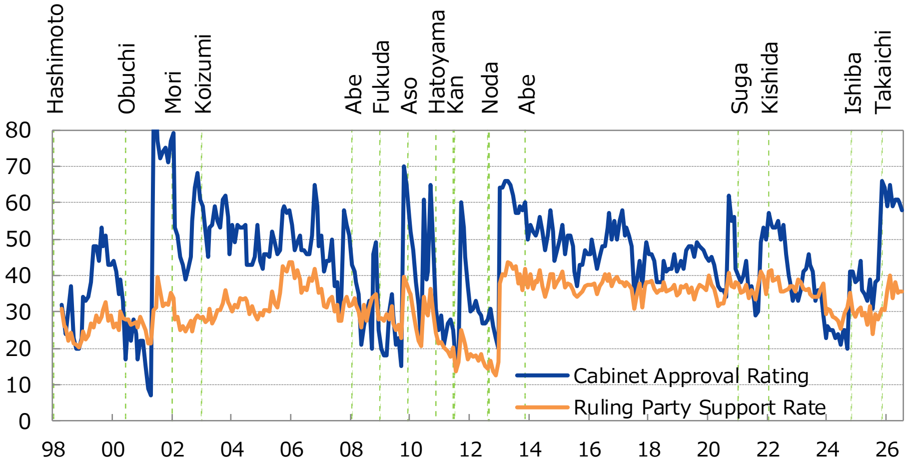


Note: Latest data are for 31 Jul 2026. OAS = Option-Adjusted Spread

Source: SMDAM and Bloomberg

Japanese Politics:

Cabinet Approval Rating and Ruling Party Support Rate (%)



Source: SMDAM and NHK

Note: Latest data are for Jul 2026

Seats in Lower and Upper Houses Note: As of 31 Jul 2026

	Lower House seats	Upper House seats
Liberal Democratic Party	316	101
Nippon Ishin / Japan Innovation Party	36	19
Ruling parties	**352**	**120**
Centrist Reform Alliance / Constitutional Democratic Party	48	40
Centrist Reform Alliance / Komeito		21
Democratic Party For the People	28	25
Reiwa Shinsengumi	0	5
Japanese Communist Party	4	7
Sanseito	15	15
Team Mirai	11	2
Others + Vacancies	7	13
Majority	**233**	**125**
Total	**465**	**248**

Source: SMDAM, the House of Representatives and the House of Councillors

Political Calendar and Key Events

Feb 18	2nd Takaichi Cabinet launched
Feb 25	**Potential successors to BOJ's Noguchi (late Mar) and Nakagawa (late Jun) are both reflationists.**
Mar 19	Japan–U.S. summit
March?	**Growth Strategy Council drafts investment roadmap**
Jun 5	**Supplementary budget (¥3tn+) passed**
Jun 16	**BOJ meeting: rate hiked to 1%**
Jul 21	**Cabinet approved Basic Policy and Growth Strategy**
Jul 21	**Corporate Governance Code revised**
early Aug	**Cabinet decision on cutting the VAT on food**
Late Aug	FY2027 budget requests due
Autumn?	**Extraordinary Diet; FY2026 supplementary budget**
Oct 30	BOJ meeting: possible rate hike
Dec	**FY2027 budget draft and tax reform outline**
By year-end	**Three National Security Documents revised**

Source: SMDAM and various media reports

Outlook for the Takaichi Administration

Stronger political leverage	LDP holds 2/3 in Lower House; can override Upper House rejection
Political stability	No national elections until summer 2028 (Upper House)
Fiscal expansion risk	Pushing proactive fiscal policy will likely lead to a larger budget

Sanaenomics: Key Policy Outlook

Policy	Expected direction	Watchpoints
Responsible proactive fiscal policy	Fiscal targets loosen; drop single-year PB surplus; focus on debt/GDP	FY26 supplementary budget
	Shift to main budget; **FY27 initial budget to expand sharply**	FY2027 budget draft
Growth & resilience investment	Support AI/ship/space/energy/defense; **up to ¥10tn** potentially allocated	FY26 supp; FY27 budget
Revise security documents	Broaden defense exports; **defense/GDP target could rise 2%→3% (+¥6tn)**	FY2027 budget
Two-year cut in food VAT	**Zero tax: ¥5T cut. 1% likely. Starts Apr 2027. Key: funding**	Autumn extraordinary Diet

Note: As of 31 Jul 2026

Governance (1): Revised CG Code highlights the importance of growth investments

Overview of the Revisions to the Corporate Governance Code

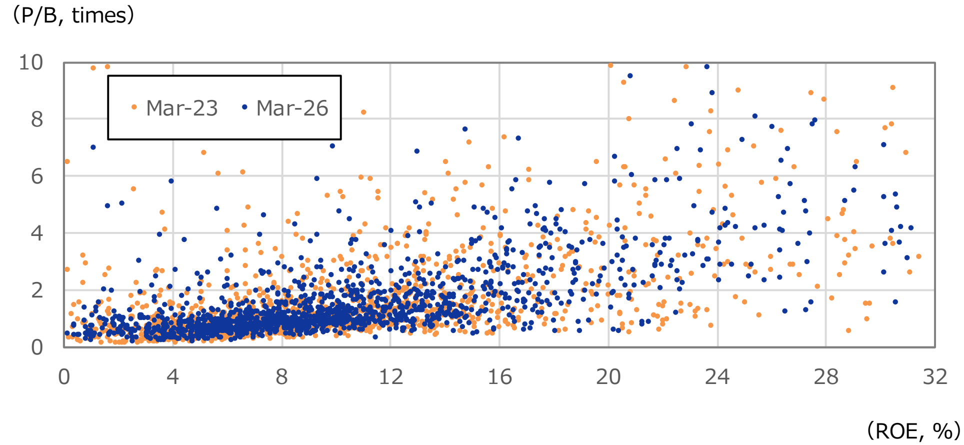
Note: Data as of 31 Jul 2026

Theme	Direction of the Proposed Revisions
Overall	To encourage companies to focus on essential initiatives for mid-to-long-term value creation (e.g., appropriate resource allocation for growth), the revisions limit "comply or explain" principles to abstract/conceptual ones. New "Interpretative Guidelines" were established with specific details and backgrounds to support effective implementation. **Aiming for the "substantiation of the Code" by returning to its original principle-based spirit**, listed companies are expected to implement practices aligned with each principle's intent based on their specific circumstances.
Promotion of Growth Investments	The revisions specify the importance of growth investment initiatives as the board's role/responsibility. Specific examples include: 1. Building a growth trajectory toward company goals. 2. **Explaining specific actions for resource allocation (e.g., capex, R&D, human/intellectual capital investments, and business portfolio reviews) to achieve growth.** 3. **Continuously verifying if resource allocation aligns with disclosed management strategies/plans for growth. The revisions cite verifying whether financial assets (like cash/deposits) and physical assets are effectively utilized for growth investments.** Holding such assets is not entirely denied; maintaining appropriate cash levels can be part of resource allocation if the company can explain its necessity and rationality.
Enhancement of Board Functions	Considering the increasing proportion of independent outside directors and the improving environment for their supervisory functions, the revisions emphasize the importance of their roles/responsibilities, securing quality/quantity, and ensuring independence to enhance their effectiveness. It also adds that the functions of the secretariat (e.g., corporate secretary), which plays a key role in supporting directors including the chair and outside directors, should be strengthened.
Pre-AGM Disclosure of Securities Report	The revised principles cite **submitting the Annual Securities Report before the general shareholder meeting (AGM) as a key example of securing an appropriate environment for exercising voting rights. The Interpretative Guidelines supplement that submitting the report at least 3 weeks before the AGM is most desirable, and pushing back the AGM date can be considered as an option.**

Source: SMDAM and FSA

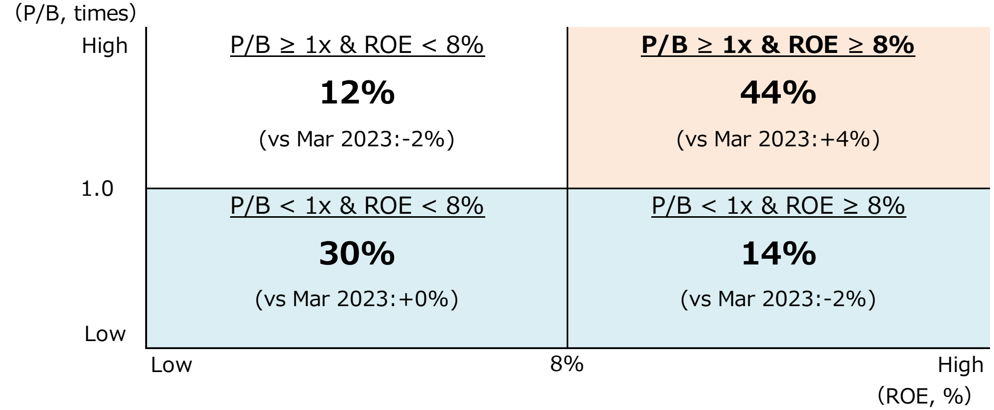
Governance (2): Corporate Response to TSE's Cost of Capital Conscious Management Request

Shifts in P/B and ROE Distribution of TSE Prime Companies Before and After the Call for Capital Cost and Stock Price-Conscious Management



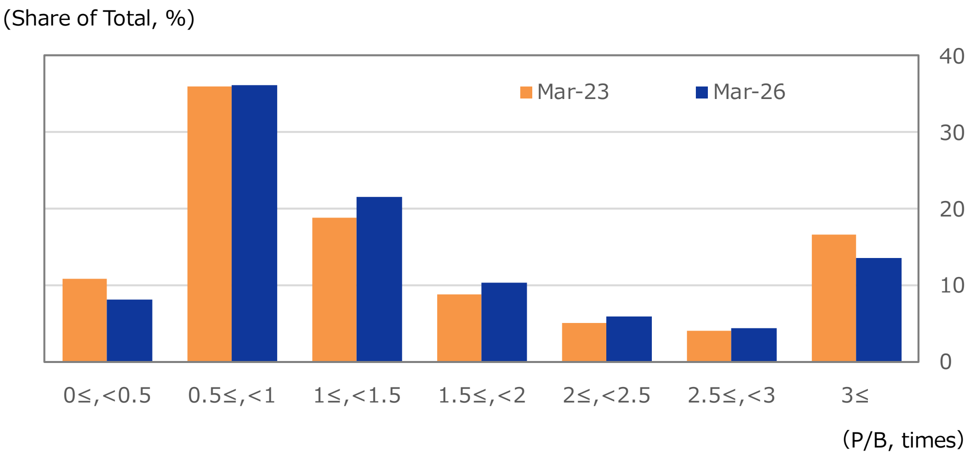
Source: SMDAM and Bloomberg

P/B & ROE Distribution in TSE Prime Companies Pre-/Post-Call for Capital Cost and Stock Price-Conscious Management (Mar 2026, Share of Total)



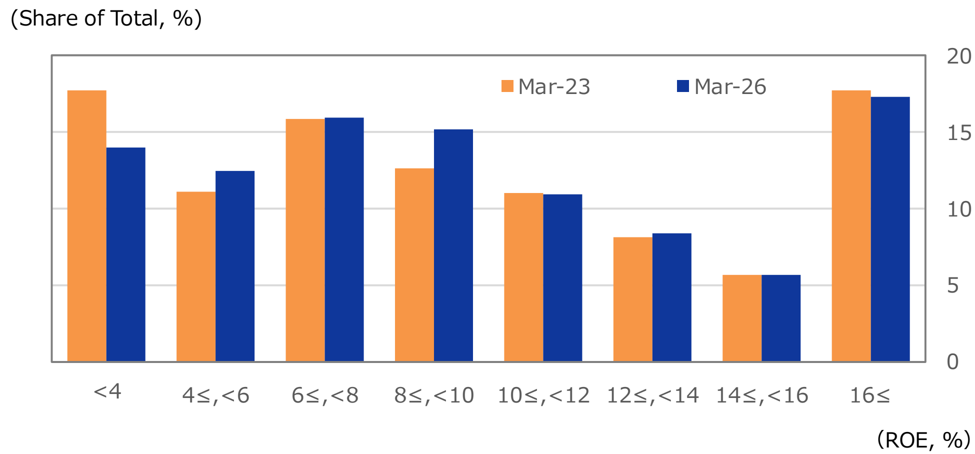
Source: SMDAM and Bloomberg

Shifts in P/B Distribution of TSE Prime Companies Before and After the Call for Capital Cost and Stock Price-Conscious Management



Source: SMDAM and Bloomberg

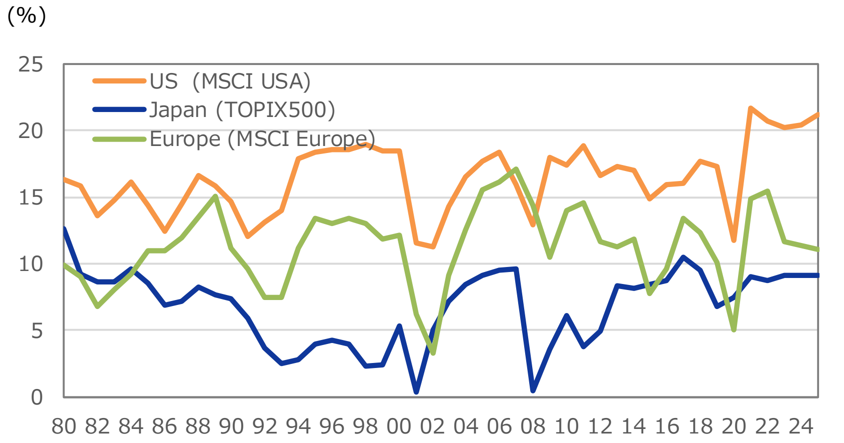
Shifts in ROE Distribution of TSE Prime Companies Before and After the Call for Capital Cost and Stock Price-Conscious Management



Source: SMDAM and Bloomberg

Governance (3): ROE

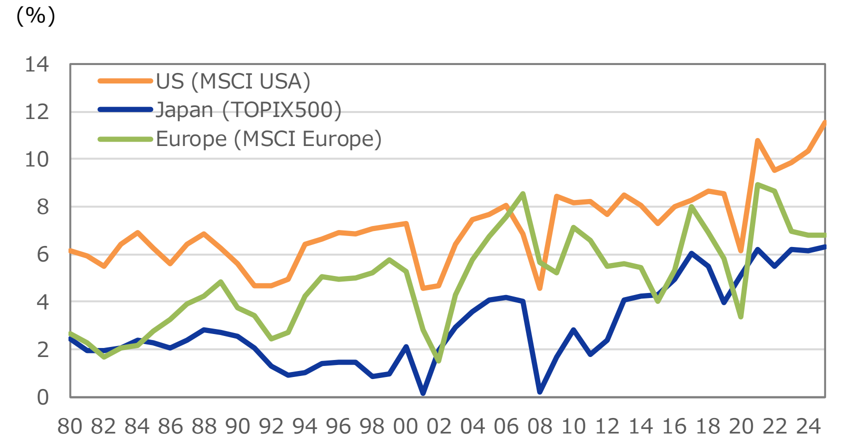
Long-term Trends of ROE in Japan, the US, and Europe



Note: Latest data are 2025. Excl. Financials (Japan: also Trading Cos)

Source: SMDAM and Daiwa Securities

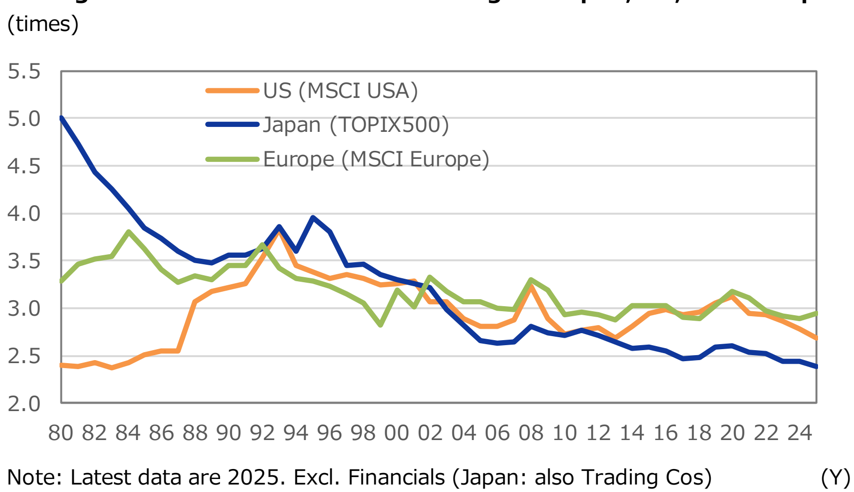
Long-term Trends of Net Profit Margins in Japan, US, and Europe



Note: Latest data are 2025. Excl. Financials (Japan: also Trading Cos)

Source: SMDAM and Daiwa Securities

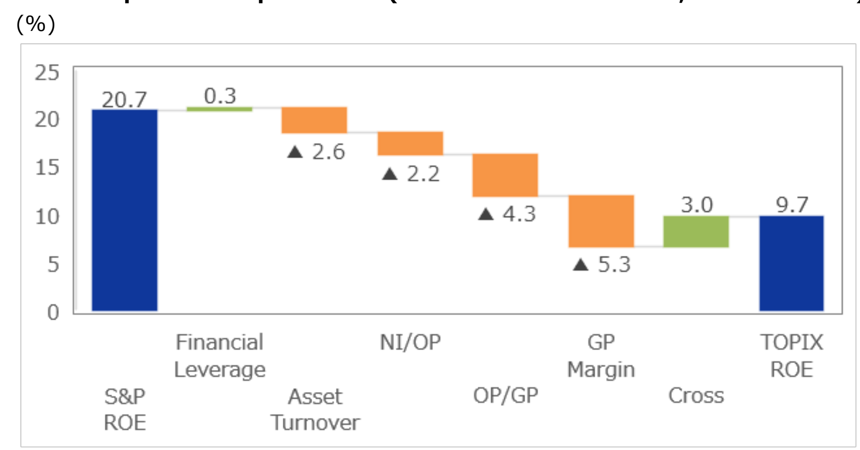
Long-term Trends of Financial Leverage in Japan, US, and Europe



Note: Latest data are 2025. Excl. Financials (Japan: also Trading Cos)

Source: SMDAM and Daiwa Securities

ROE Comparison: Japan vs US (TOPIX 500 vs S&P 500, Ex-Financials)



Note: Latest Data as of 31 Jul 2026

Source: SMDAM and Bloomberg

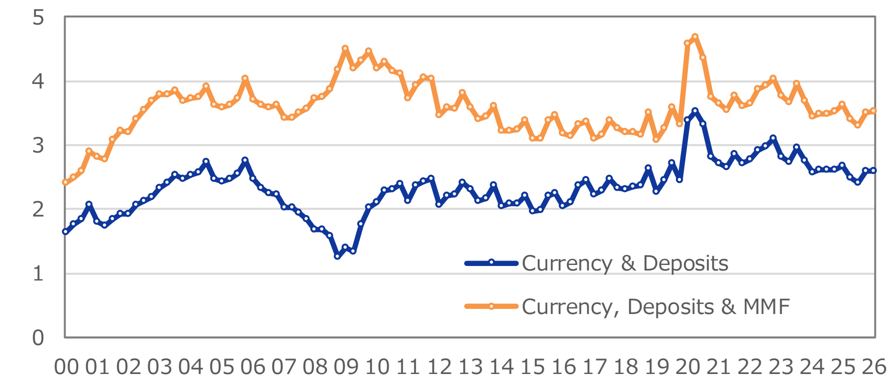
Governance (4): Effective Cash Utilization

Cash Ratio in B/S of Japanese Non-Financial Corporations

Note: Latest data are for 1Q 2026

Source: SMDAM and BoJ

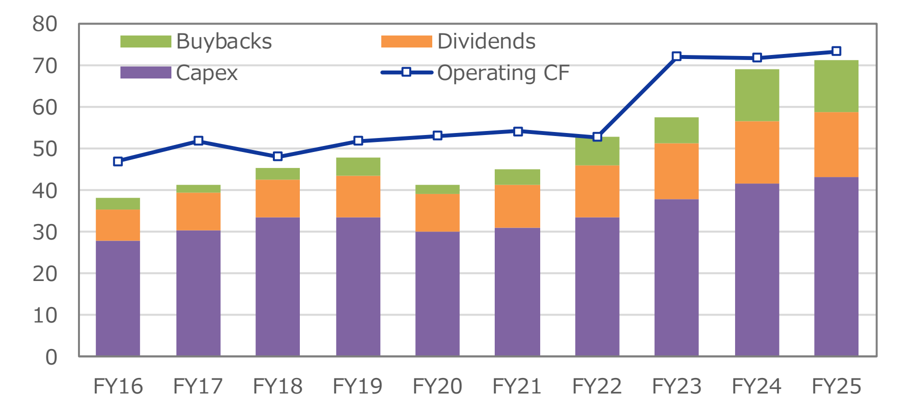
Cash Ratio in B/S of US Non-Financial Corporations



Note: Latest data are for 1Q 2026

Source: SMDAM and FRB

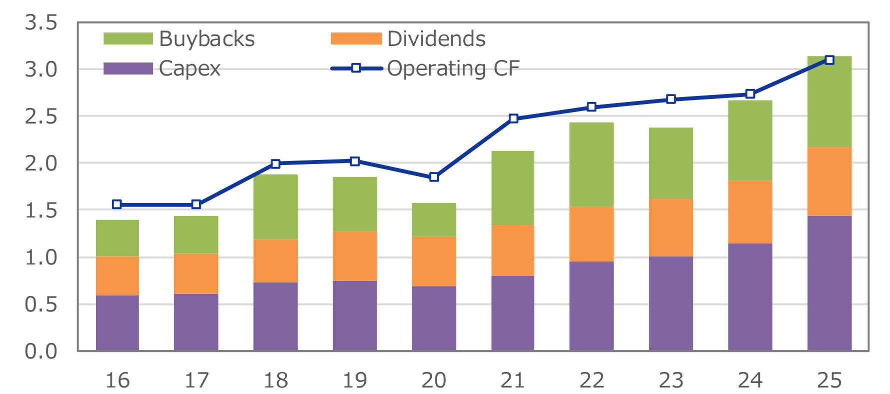
OCF, Investment, and Shareholder Returns for TOPIX 500 Companies



Note: Excludes Financials. Latest data are for FY2025.

Source: SMDAM and Bloomberg

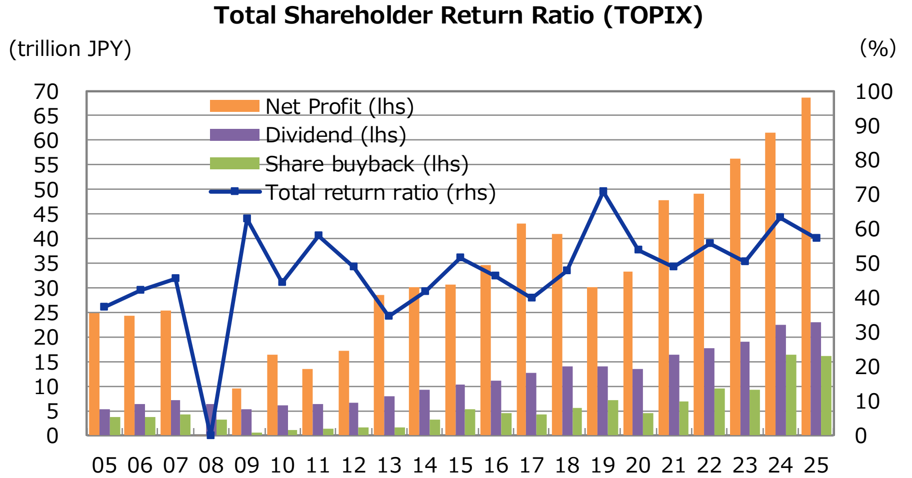
OCF, Investment, and Shareholder Returns for S&P 500 Companies



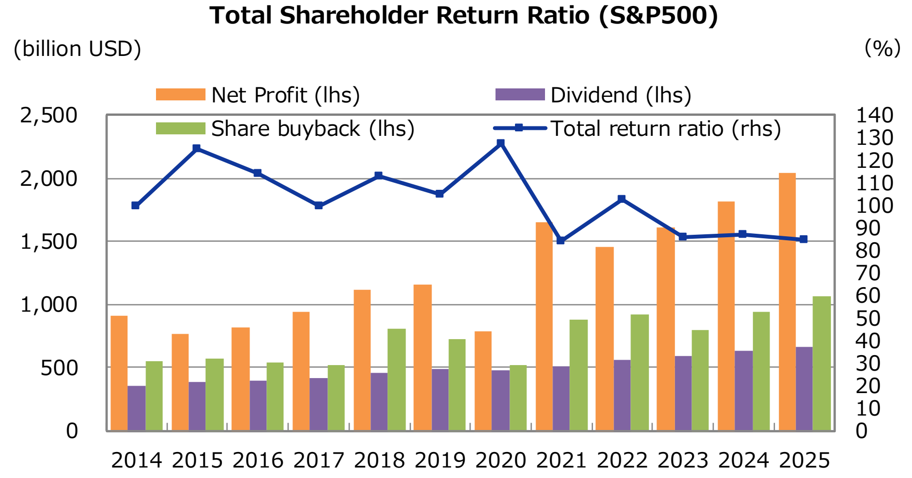
Note: Latest data are for 2025

Source: SMDAM and Bloomberg

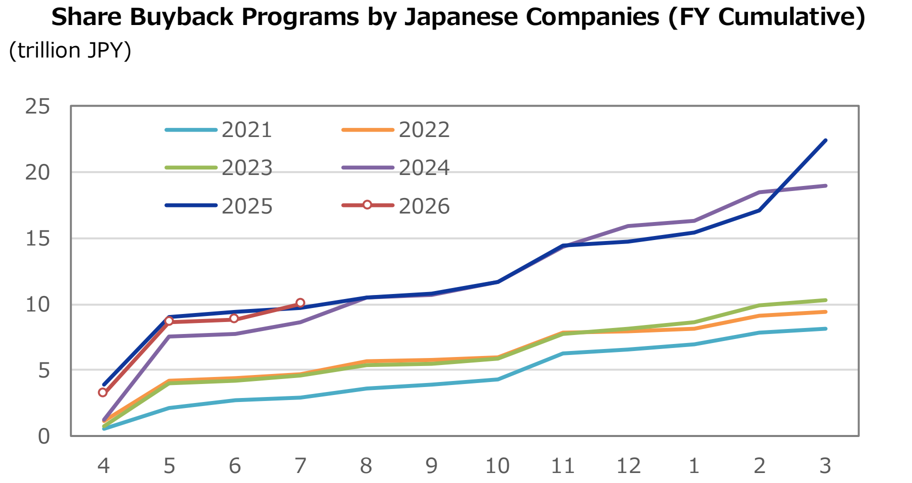
Governance (5): Shareholder Returns



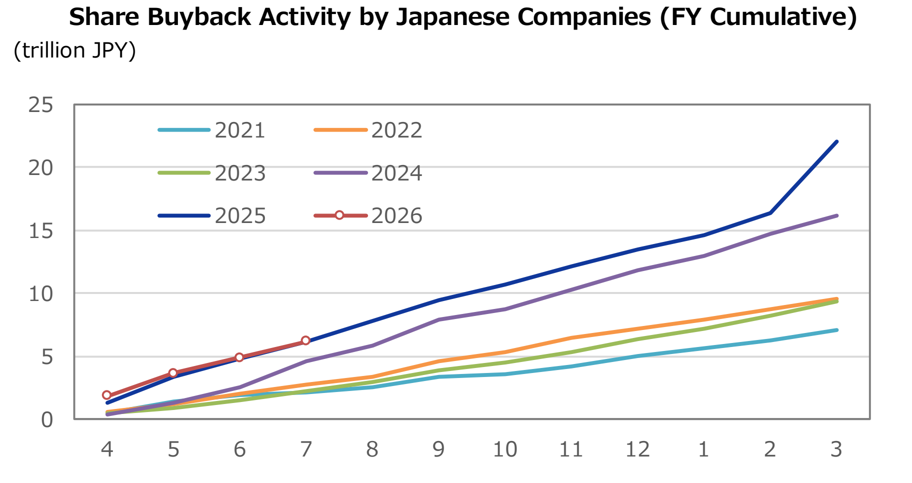
Note: Latest data are for FY2025
Source: SMDAM, Tokai Tokyo Securities, and Bloomberg



Note: Latest data are for 2025
Source: SMDAM, Tokai Tokyo Securities, and Bloomberg



Note: Latest data are for Jul 2026
Source: SMDAM and INDB

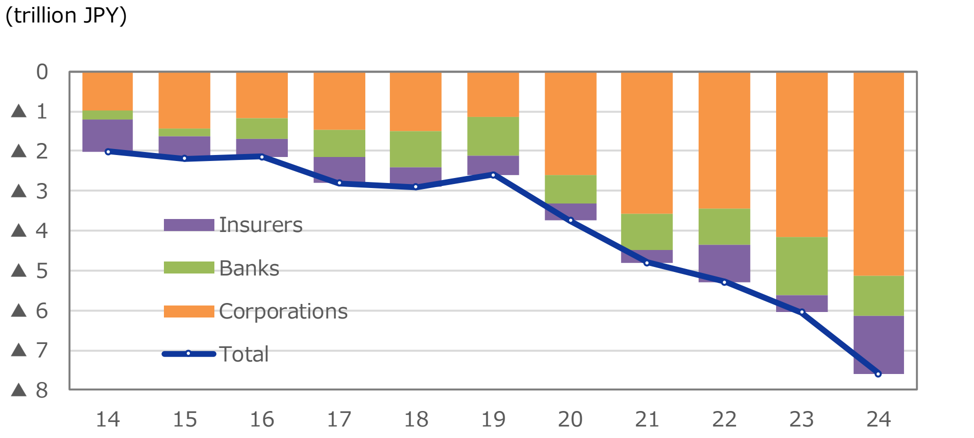


Note: Latest data are for Jul 2026
Source: SMDAM and INDB

Sumitomo Mitsui DS Asset Management

Governance (6): Ownership Structure & Shareholder Meetings

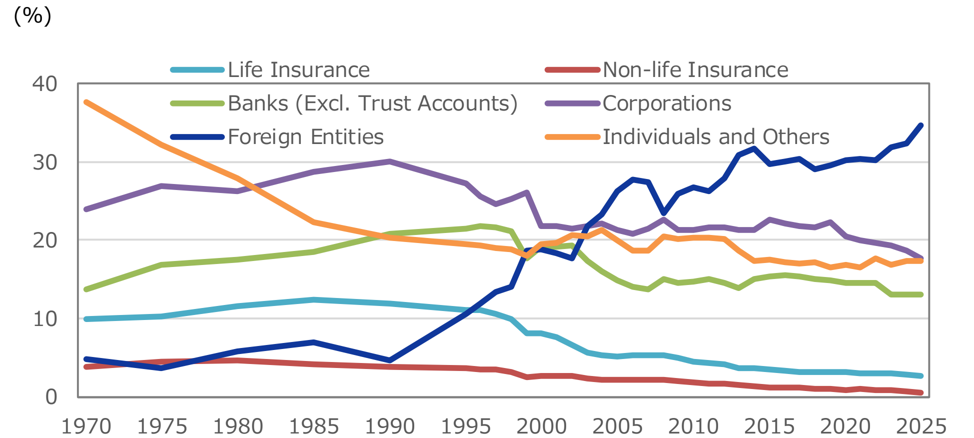
Cross shareholding unwinding



Note: Latest data are for FY2024

Source: SMDAM and Tokai Tokyo Securities

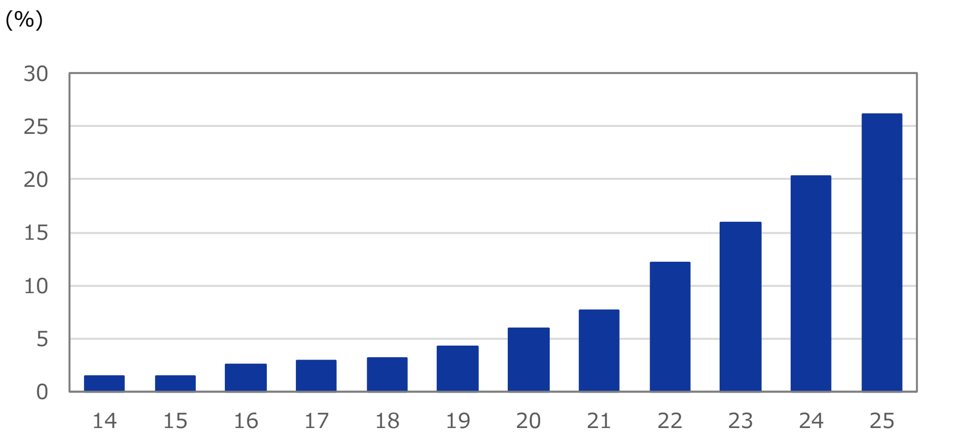
Distribution of Equity Ownership by Shareholder Type



Note: Latest data are for FY2025

Source: SMDAM and JPX

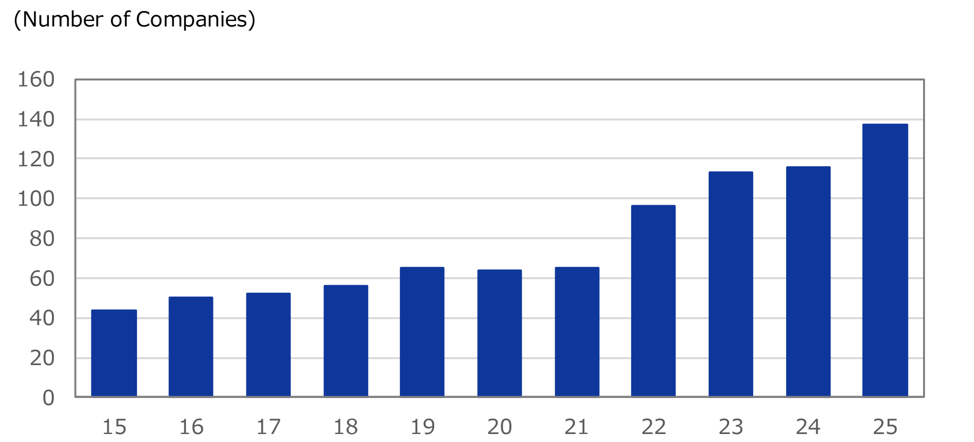
Percentage of Companies with a Majority of Independent Outside Directors



Note: Latest data are for FY2025

Source: SMDAM and JPX

Number of Shareholder Proposals

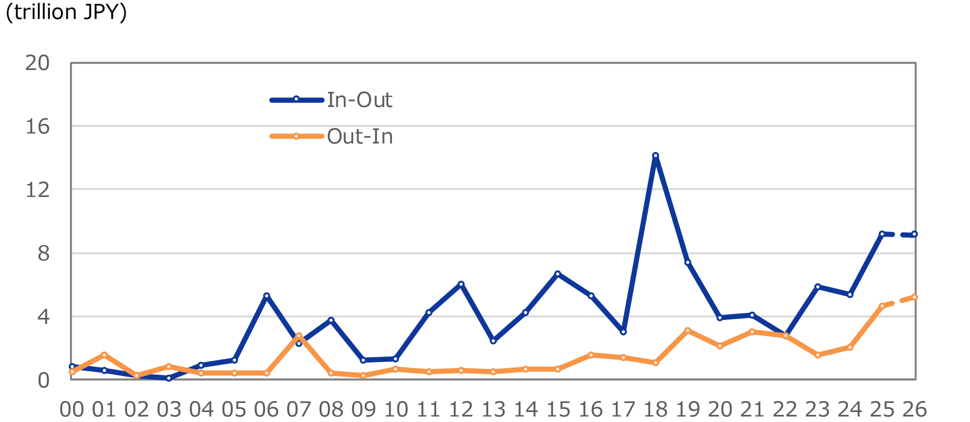


Note: Latest data are for FY2025

Source: SMDAM and Japan Institute of Business Law

Governance (7): Rising Takeover Risk

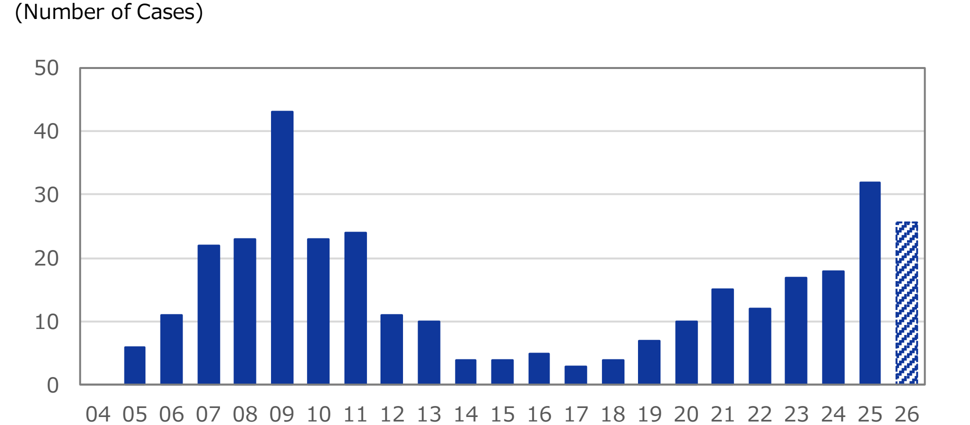
Trends in M&A Deal Value Involving Japanese Companies



Note: Latest data are for 2026. 2026 is annualized through Jul

Source: SMDAM and Bloomberg

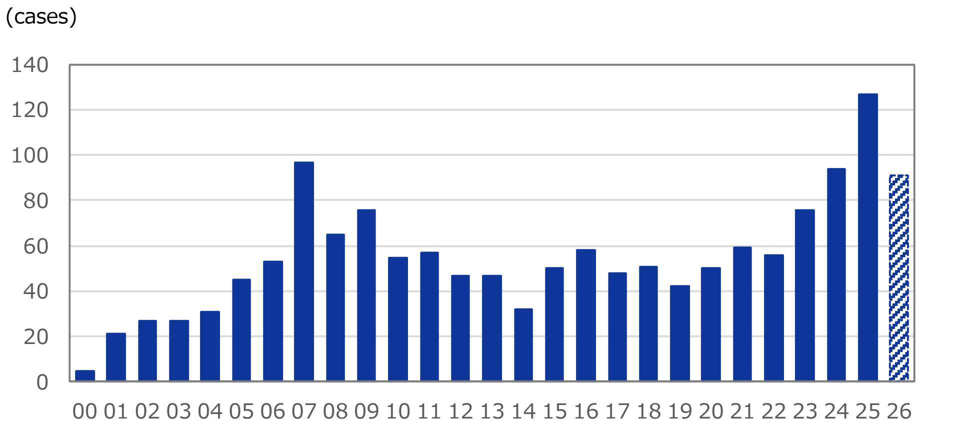
Trends in MBO Transactions



Note: Latest data are for 2026. 2026 is annualized through Jul

Source: SMDAM and Bloomberg

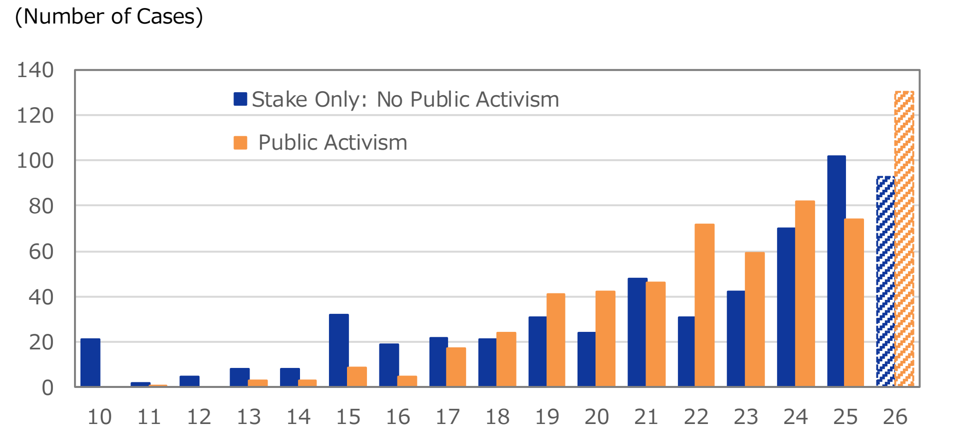
Trends in Number of TOBs (TSE Listed Companies)



Note: Latest data are for 2026. 2026 is annualized through Jul

Source: SMDAM and Bloomberg

Activist investor activity



Note: Latest data are for 2026. 2026 is annualized through Jul

Source: SMDAM and Bloomberg

NISA

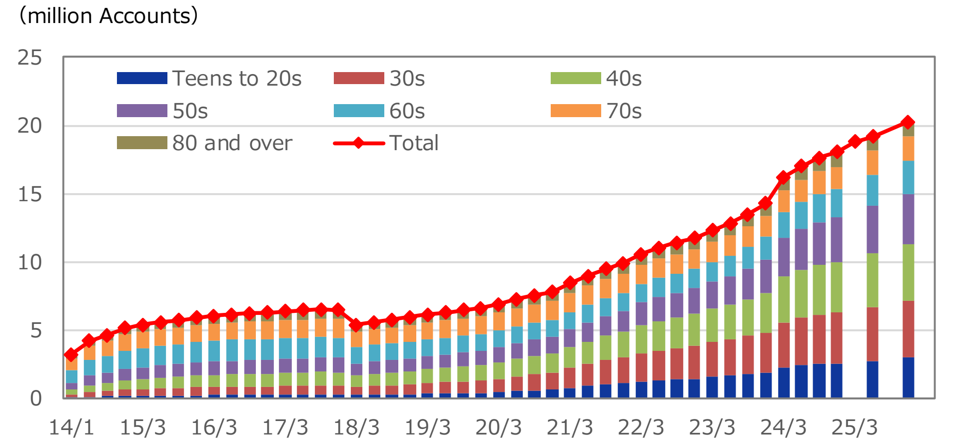
Comparison of old and new NISA (Tax free investing program like UK ISA)

	Old NISA		NEW NISA		
	Tsumitate NISA	General NISA	Tsumitate Quota	Growth Quota	Kodomo NISA
Lifetime Limit	JPY 8 mn	JPY 6 mn	JPY 18 mn (JPY 12 mn for Growth Quota)		JPY 6 mn
Annual Limit	JPY 0.4 mn	JPY 1.2 mn	JPY 1.2 mn	JPY 2.4 mn	JPY 0.6 mn
Tax Exemption Period	20 years	5 years	No Limit		No Limit
Availability for Combined Use	No		Yes		
Investment Option	FSA selected Investment trusts and ETFs	Listed stocks, ETFs, REITs and Investment trusts	FSA selected Investment trusts and ETFs	Listed stocks, ETFs, REITs and Investment trusts	FSA selected Investment trusts and ETFs
Target Age	18 and older		18 and older		0–17 years old

Source: SMDAM and FSA

Note: As of 31 Jul 2026

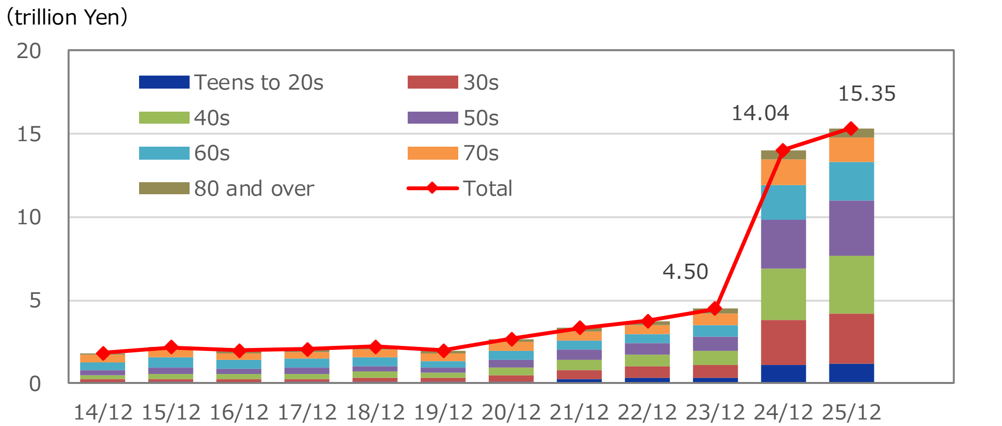
Number of NISA Accounts by Age Group



Note: Latest data are for end-Dec 2025; some age breakdowns unpublished. (Y/M)

Source: SMDAM and Japan Securities Dealers Association

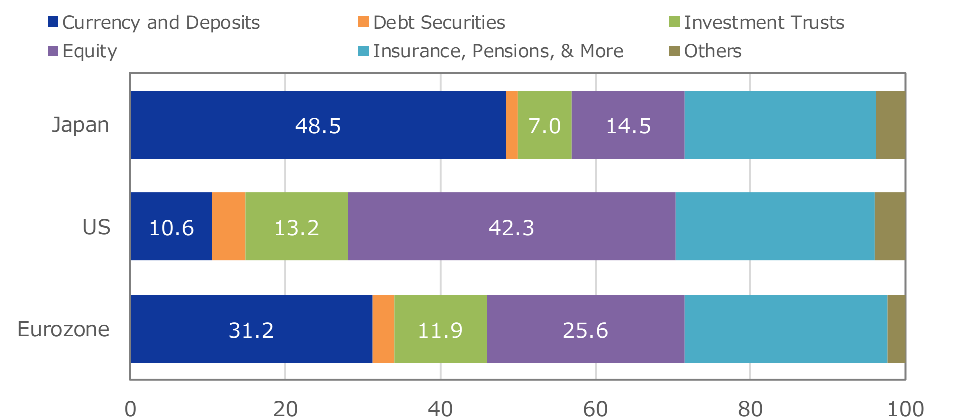
Annual Purchase Amount in NISA Accounts by Age Group



Note: Latest data are for end-Dec 2025. (Y/M)

Source: SMDAM and Japan Securities Dealers Association

Financial Assets held by Households (As of December 2025)



(%)

Source: SMDAM, BoJ, FRB and ECB

Event Schedule: Focus— Consumption tax cuts, the cabinet reshuffle, and the initial FY2027 budget

	Date	Japan	Date	U.S.	Date	Other Regions
July to September 2026	Q3? Q3?	Decision on zero tax for food products? Cabinet reshuffle?	Aug	Jackson Hole Economic Symposium		
October to December	**Dec** **By year-end?**	**Cabinet Approval of the 27 FY Budget Proposal and Tax Reform Outline** **Revision of the three key national security documents**	Oct? **Nov 3** **Dec?**	US Treasury Semi-annual Currency Report **U.S. midterm elections** **Final reports of five Fed task forces**		
January to March 2027	Jan Mid-Mar	Opening of the Ordinary Diet Session Key Response Day for Spring Wage Negotiations	Jan	The Opening of the U.S. Senate and House of Representatives	Jan Mar	IMF World Economic Outlook National People's Congress of China
April to June	Apr Q2? Jun? End-Jun	Unified local elections Successor nominations for BOJ Board Members Takata and Tamura (Terms expire Jul 23, 2027) Cabinet's approval of the Basic Policy Closing of the Ordinary Diet Session	Jun?	US Treasury Semi-annual Currency Report	Apr Apr Jun	IMF and World Bank Spring Meetings IMF World Economic Outlook G7 Summit
July to September	Jul 23 **Sep**	Terms of BOJ Board Members Takata & Tamura expire **LDP presidential election**	Aug	Jackson Hole Economic Symposium	Jul	IMF World Economic Outlook

Source: Compiled by SMDAM

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