

# Japan Event Flash

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**Mitsubishi UFJ Trust and Banking  
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## The Future of the Takaichi Trade

Japan's Liberal Democratic Party secured a historic landslide victory in the February House of Representatives election, leading to the formation of the second Takaichi Cabinet on the 18<sup>th</sup> February. Initially, expectations surrounding the Takaichi administration's proposed 'responsible proactive fiscal policy' fueled speculation that the so-called Takaichi trade (stock market gains, yen depreciation, rising interest rates) would gain momentum. In reality, however, the stock market rallied while yen depreciation paused, and interest rates declined. Has the Takaichi Trade truly come to an end? We believe that while the upward trend in stocks will likely continue for the time being, a sense of pause has already emerged in yen depreciation and rising interest rates. In other words, the Takaichi Trade may have reached a turning point in certain respects.

Regarding equities, against a backdrop of robust fundamentals, a bull market (rising stock prices) appears likely to take hold (Exhibit 1). The Q3 FY2025 earnings season for TOPIX constituents (companies with February or March fiscal year-ends) has concluded, with overall solid results. Specifically, cumulative ordinary profits for Q3 rose 7.7% year-on-year (YoY) overall. Manufacturing fell 4.0% YoY, while non-manufacturing saw YoY increase of 16.3% (excluding SoftBank Group, it rose 3.5% YoY). Sectors with significant ordinary profit growth included banks, which benefited from widening interest margins following the Bank of Japan's rate hikes, and electrical machinery, which captured growth in demand for AI and data centers. Conversely, sectors with significant declines in ordinary profits included transportation equipment, adversely affected by Trump tariffs.

While full-year FY2025 ordinary profit had faced consensus expectations of a temporary decline due to Trump tariff headwinds, current market forecasts (QUICK Consensus) project a +7.2% year-on-year increase overall, with company forecasts at +5.8%. This suggests a potential profit increase at year-end. Considering that the previous 15% reciprocal tariffs imposed by the U.S. on Japan have been invalidated, while replacement tariffs at the same rate have been introduced, the impact of the U.S.'s new tariff policy on Japanese corporate earnings is considered to be largely neutral.

Although AI-related stocks have shown volatile price movement since the start of the 2026 year, this reflects a shift in capital within the equity market, with cyclical stocks outperforming instead. This does not indicate deteriorating risk sentiment. We believe the supply-demand environment for Japanese stocks remains tight.

Looking ahead, the Japanese stock market is expected to see further gains. This is underpinned by the Takaichi administration's expansionary fiscal policies, improving corporate earnings, and revisions to the Corporate Governance Code, which are facilitating more effective use of cash by Japanese companies (such as further proactive shareholder return measures). Against the backdrop of instability in U.S. politics, if capital continues to flow out of the United States, Japanese stocks could benefit from the resulting capital inflows. While the Nikkei Stock Average is projected to reach 58,000 by the end of March 2027, it could potentially exceed expectations and surpass 60,000 within a relatively short period.

On the other hand, regarding foreign exchange, we do not expect the “Takaichi trade” (yen depreciation) to accelerate from here.

The dollar-yen rate had risen to the 157 yen level before the Lower House election due to expectations of a landslide victory for the LDP. However, when the LDP did indeed win the election decisively, short year positions were unexpectedly unwound, causing the rate to temporarily fall to the 152 yen level (Exhibit 2).

The post-election yen appreciation can be attributed to several factors:

1. Heightened vigilance over potential currency intervention following Finance Vice-Minister Mimura's remarks cautioning against yen weakness.
2. Increased awareness that the LDP's landslide victory would give the Takaichi administration a very solid governing foundation, potentially strengthening fiscal discipline considerations.
3. Heightened expectations for the feasibility of growth strategies under the Takaichi administration, spurring active buying of Japanese assets.

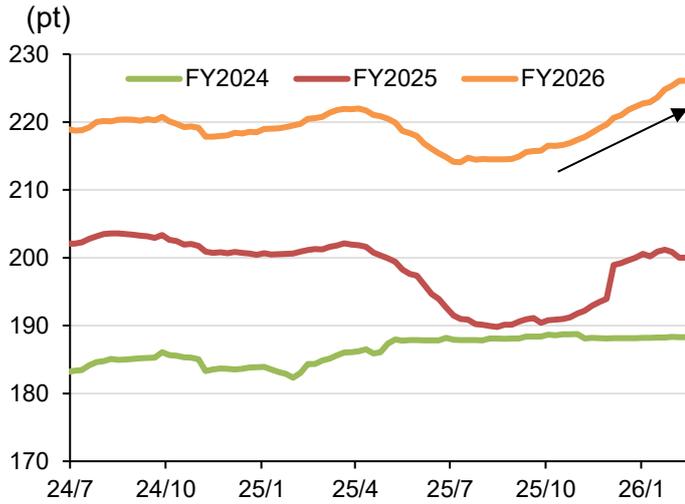
Looking ahead, as market participants gain a better understanding of Prime Minister Takaichi's responsible proactive fiscal policy, excessive yen-selling pressure stemming from concerns over fiscal deterioration is expected to subside. While advocating proactive fiscal policy, Prime Minister Takaichi has pledged to maintain fiscal discipline by reducing the debt-to-GDP ratio. Indeed, according to the Cabinet Office's medium-to-long-term economic and fiscal projections (January 2026), if nominal growth can be sustained at around 3% over the medium to long term, the debt-to-nominal GDP ratio is projected to decline gradually over the next decade (Exhibit 3). Considering factors such as Japanese households actively increasing investments in overseas assets, Japan's widening digital deficit, and the high appeal of yen carry trades, we anticipate yen depreciation environment to persist. However, we do not foresee a sharp acceleration in yen weakness due to caution surrounding potential currency intervention by Japanese and U.S. authorities. The dollar-yen exchange rate is likely to trade within a range centered around 155 yen.

Furthermore, regarding fixed income, we do not anticipate the Takaichi trade (rising interest rates) accelerating from here.

The 30-year bond yield rose to the 3.8% range ahead of the Lower House election on expectations of a LDP landslide victory. However, when the LDP did indeed win by a large margin, short positions were unexpectedly unwound, causing the yield to temporarily fall to the 3.3% range and the yield curve to flatten (Exhibit 4). The post-election decline in ultra-long-term bond yields (over 10 years) likely stems from market expectations, similar to the foreign exchange market, that the LDP's landslide victory and the resulting strong foundation for the Takaichi administration will heighten concerns about stronger fiscal discipline. Furthermore, expectations grew that the supply-demand dynamics for ultra-long-term bonds would improve. This was because life insurers, holding bonds under the policy reserve matching category, would likely no longer require impairment charges, eliminating the need to sell bonds that have experienced significant price declines.

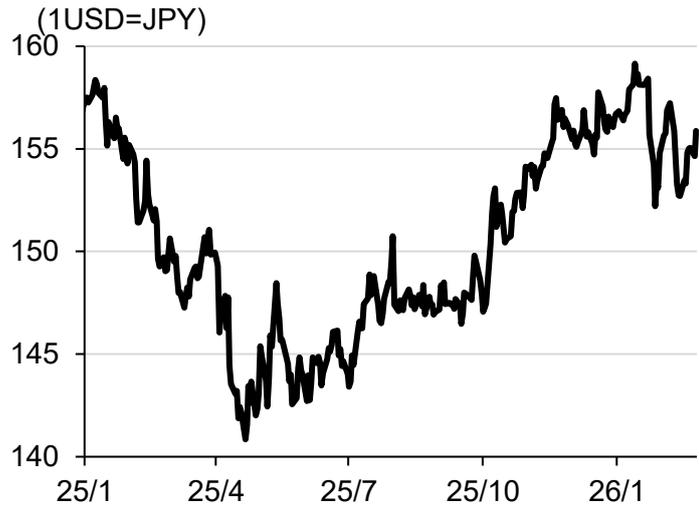
Looking ahead, whilst Japanese long-term interest rates are likely to rise gradually toward the mid-2% range as the Bank of Japan steadily raises rates, concerns about loose fiscal policy under the Takaichi administration have receded. This suggests a significant rise in ultra-long-term bond yields will be avoided. In our view, the phase of substantial interest rate increases appears to have ended.

**Exhibit 1: TOPIX EPS Consensus Forecast**



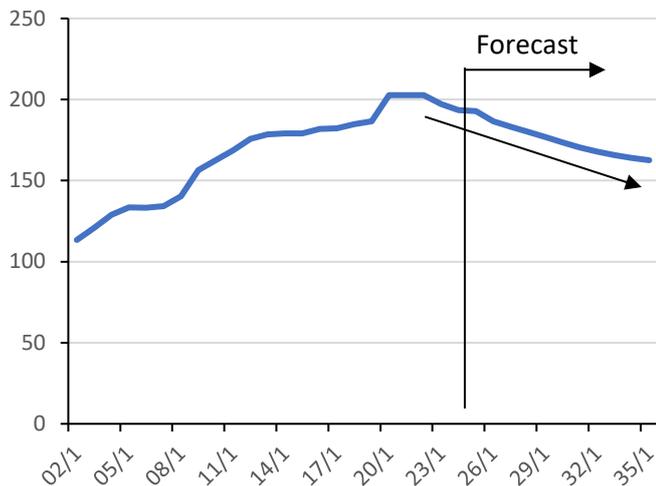
Source: LSEG, MUFG: Trust Bank

**Exhibit 2: USD/JPY**



Source: Bloomberg, MUFG: Trust Bank

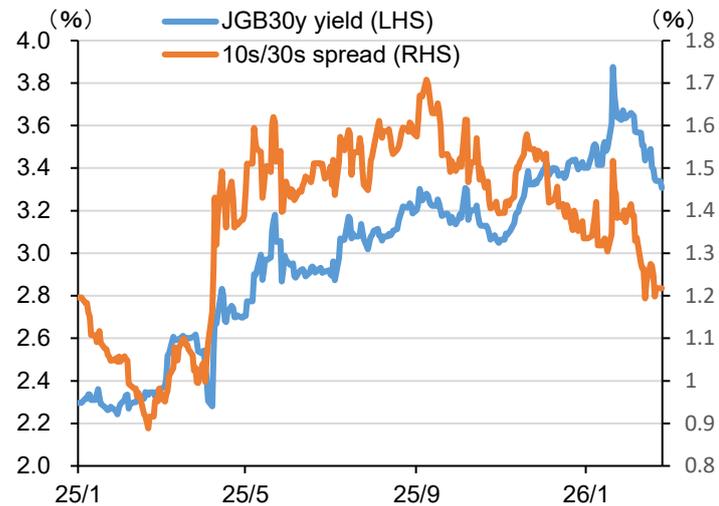
**Exhibit 3: Debt-to-nominal GDP ratio**



Note: Cabinet Office estimates for the growth transition scenario (nominal GDP annual growth rate of 3%)

Source: Cabinet Office, MUFG: Trust Bank

**Exhibit 4: JGB 30y bond yield and 10s/30s spread**



Source: Bloomberg, MUFG: Trust Bank

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