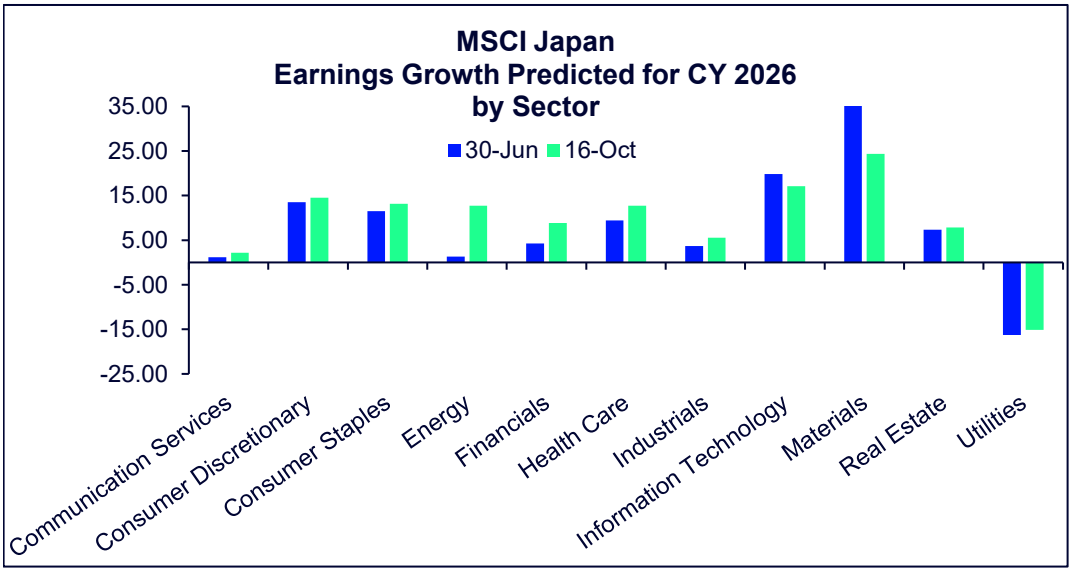
STATE STREET INVESTMENT MANAGEMENT

COMMENTARY
October 16, 2025

Mind on the Market

Chart of the Week



Source: FactSet, MSCI. Data as of 10/16/2025.

Analyst expectations for 2026 earnings growth across Japanese sectors have generally strengthened since the June estimates, signaling a more optimistic outlook. The only exceptions are the Information Technology and Energy sectors, which are experiencing a normalization in earnings following previously elevated expectations. As the country awaits the confirmation of Sanae Takaichi as Prime Minister, which is complicated by the LDP's lack of majority in parliament, policy initiatives will begin to take shape—potentially benefiting select industries as such defense, advanced manufacturing and energy infrastructure —we will closely monitor how sector-specific earnings forecasts respond. A deeper analysis of Japanese equities follows below.

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Weekly Highlights

Nikkei 225 YTD Performance	Nikkei 225 NTM PE	Nikkei 225 NTM PEG
26.29%	20.83x	3.26

Source: FactSet. Data as of 10/15/2025.

Japan’s Next New Chapter

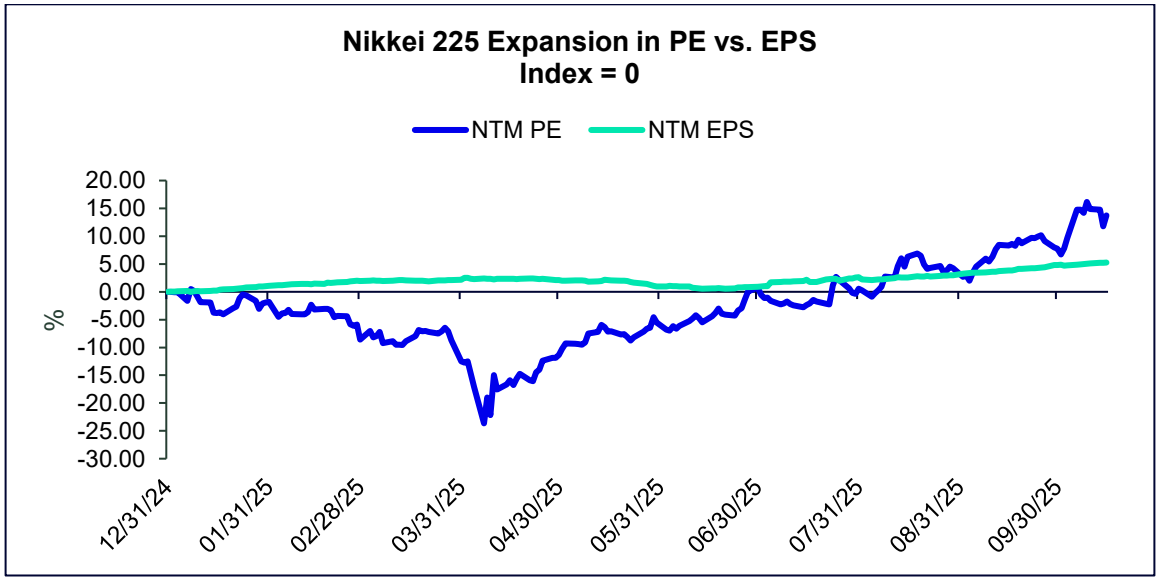
Japanese equities have delivered strong year-to-date performance, with the Nikkei 225 up 26% and the TOPIX up 18% in USD terms. This rally has been driven by reflationary momentum, corporate governance reforms, and a more favorable earnings outlook. Markets received an additional boost following the recent election of Sanae Takaichi as leader of the Liberal Democratic Party, positioning her as Japan’s likely next prime minister.

Domestically, Japan continues to grapple with rising living costs, demographic headwinds, and shifts in global trade dynamics. A new leader—particularly one with a protectionist stance—may offer a sense of renewal. Takaichi’s policy agenda includes fiscal expansion, technological nationalism, and defense modernization. If her ambitions can overcome political fragmentation, they may benefit sectors tied to domestic demand and government spending.

Despite strong year-to-date performance, Japan has faced subdued earnings growth for much of the year. The MSCI Japan index is projected to deliver just 2% earnings growth for calendar year 2025. Contributing factors include tariff-related distortions in exports and pricing, sector-specific challenges (particularly in the auto industry), muted domestic demand, and ongoing policy uncertainty from the Bank of Japan. However, the outlook brightens for 2026, with earnings growth expected to reach 10%.

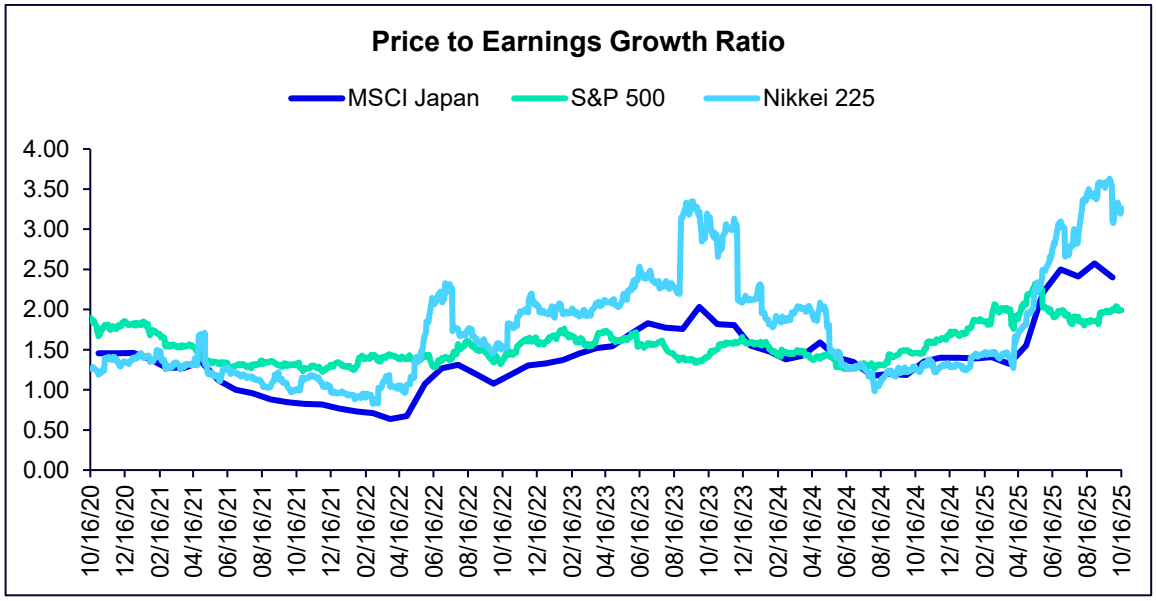
Valuations in Japan have expanded meaningfully this year, with the Nikkei now trading at 20.8x forward price-to-earnings (NTM PE), a notable rise from the post-Liberation Day lows of 13x. Over the past six months, valuation expansion has notably outpaced earnings growth. The NTM PE ratio has increased by approximately 13%, while NTM EPS has grown just 5%. This divergence may reflect investor optimism

tied to the emergence of new leadership, with expectations of supportive policy and improved long-term earnings potential.



Source: FactSet. Data as of 10/15/2025.

Excitement around Japan's earnings prospects has also pushed the PEG ratio to new heights, with the Nikkei reaching a PEG of 3.2, higher than the S&P 500's PEG ratio of 1.9.



Source: FactSet, MSCI, S&P. Data as of 10/15/2025.

In reviewing Takaichi's policy agenda, we've considered sectoral implications and how they may influence market performance going forward. Among her key objectives is positioning Japan in the global technology race, with a strong push for digital sovereignty. Echoing priorities seen in other developed economies, Takaichi has emphasized artificial intelligence, quantum computing, and semiconductor self-sufficiency. Her support could bolster Japan's technology and semiconductor sectors, though this would also depend on an easing of U.S.–China tensions, as China has restricted exports of critical minerals such as gallium and germanium—key inputs for chipmaking—disrupting global supply chains.

Energy will also play a critical role in powering these advanced technologies. Takaichi has highlighted energy security and the development of next-generation nuclear power as strategic priorities. If successfully implemented, her policies could benefit industries tied to domestic demand and government-led fiscal expansion.

Another key policy objective is Takaichi's plan to double defense spending to approximately 2% of GDP by 2027. This initiative is expected to direct government funding toward companies involved in domestic arms production, satellite protection, and cybersecurity infrastructure.

These broader themes have already been reflected in market performance. Year-to-date, the Energy and Utilities sectors of MSCI Japan are up 25% and 28%, respectively. Technology has gained 24%, with the semiconductor industry surging 43%. Notably, MSCI Japan's Information Technology sector is trading at 22x next-twelve-month earnings, a discount to the U.S. IT sector, which trades at 30x NTM PE.

Japanese equities have rallied on optimism around structural reforms and fiscal support, even as earnings growth this year has remained modest. Looking ahead, the outlook has improved with rising earnings estimates, and the emergence of new leadership. Though investors have already placed a premium on future earnings growth from Japan, Takaichi's policy agenda could further enhance performance and profitability in select segments of the equity market.

Please stay tuned for an upcoming piece by our colleagues, Masahiko Loo and Krishna Bhimavarapu, exploring Takaichi's political roots and her potential impact on Japan's economy.

Source: FactSet, MSCI. Data as of 10/15/2025 in USD unless otherwise stated. Past performance is not a reliable indicator of future performance. Index returns are unmanaged and do not reflect the deduction of any fees or expenses.

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*This figure is presented as of June 30, 2025 and includes ETF AUM of $1,689.83 billion USD of which approximately $116.05 billion USD in gold assets with respect to SPDR products for which State Street Global Advisors Funds Distributors, LLC (SSGA FD) acts solely as the marketing agent. SSGA FD and State Street Investment Management are affiliated. Please note all AUM is unaudited.

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