Japan Insights | Market Strategy by Nozomi Moriya

Market Turmoil and Shifting Flows (Japanese Equities – A Global View from Hong Kong)

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Nozomi Moriya – Chief Strategist (Institutional Clients)

At the start of November, I traveled to Hong Kong to meet with overseas investors. Most of my meetings were with long-term investors, but the city is also home to a broad range of market participants, including hedge funds. In conversations with people in the market, I heard how challenging this year had been for hedge funds and other investors, as well as how portfolios were being adjusted, particularly in AI and semiconductor stocks.

After I returned to Japan, global equity markets came under severe pressure in the wake of the U.S. midterm elections. Selling intensified in AI-related stocks, which had already been correcting, and spread to Japanese equities. The market's decline brought into sharp focus the shifts in fund flows I had heard about in Hong Kong. The episode offers a timely lens through which to examine the global repositioning underway and its implications for Japanese equities.

Shifting Global Flows

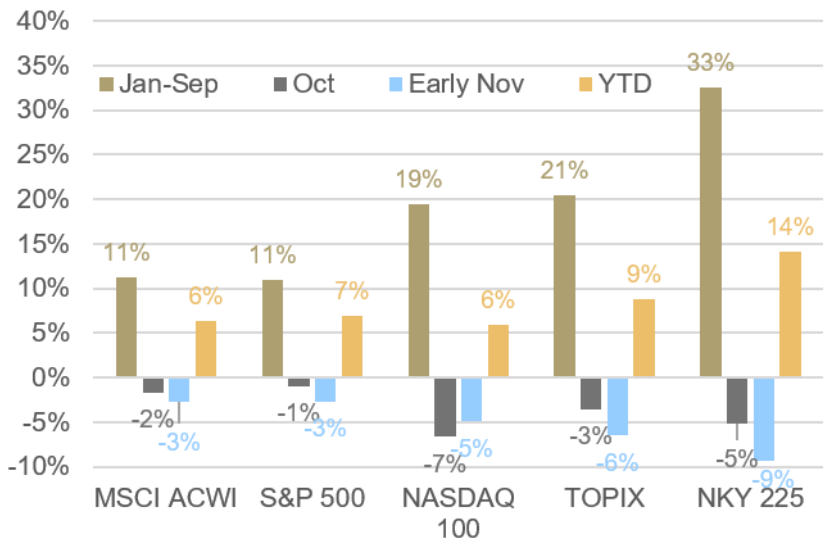
AI-related stocks have driven markets higher this year, while investor positions have increasingly become concentrated in a narrow range of themes and names. More recently, concerns about the returns on massive AI investments have weighed on AI and semiconductor stocks—until recently among the market's biggest winners.

Hedge funds have also felt the effects. Reports indicate that Asian equity long/short strategies fell more than the Nasdaq 100 in October, underscoring the difficult environment for hedge funds. This echoes the concerns I heard in Hong Kong about the challenges of investing this year.

When losses mount, investors may reduce risk by cutting both long and short positions—a process known as "de-grossing." If volatility rises further, trading by macro funds and CTAs (Commodity Trading Advisors) can add to the pressure, amplifying price movements beyond what fundamentals alone would suggest. These dynamics are an important part of the explanation for the latest sharp decline.

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Figure 1. Returns of Major Equity Indices in 2026



Source: Nomura Asset Management based on Bloomberg. Early November data includes MTD until Nov 6.

Spillover to Japanese Equities

The decline in Japanese equities appears to have been strongly influenced by this global repositioning. Selling that began in AI and semiconductor stocks gradually spread across the broader market, producing price moves that were difficult to explain on the basis of sector or company fundamentals alone.

Japanese equities are particularly sensitive to overseas flows. Foreign investors account for a high proportion of cash equity trading, so when global investors reduce risk across their portfolios, selling pressure in Japan can intensify even in the absence of Japan-specific negative news.

That said, the latest moves should not be taken as evidence of a broad retreat from Japanese equities. Overseas investors had been net buyers until shortly before the decline, and the fundamentals of Japanese companies have not changed dramatically in a matter of weeks.

Recent earnings have generally been resilient, with some companies raising their full-year forecasts. Companies have also continued to strengthen shareholder returns, including through share buybacks. The sharp market correction has not been accompanied by a comparable deterioration in corporate earnings power or cash generation.

It is therefore important to distinguish short-term movements in fund flows from the longer-term changes underway in Japanese equities, including resilient corporate performance, efforts to improve capital efficiency, and business restructuring.

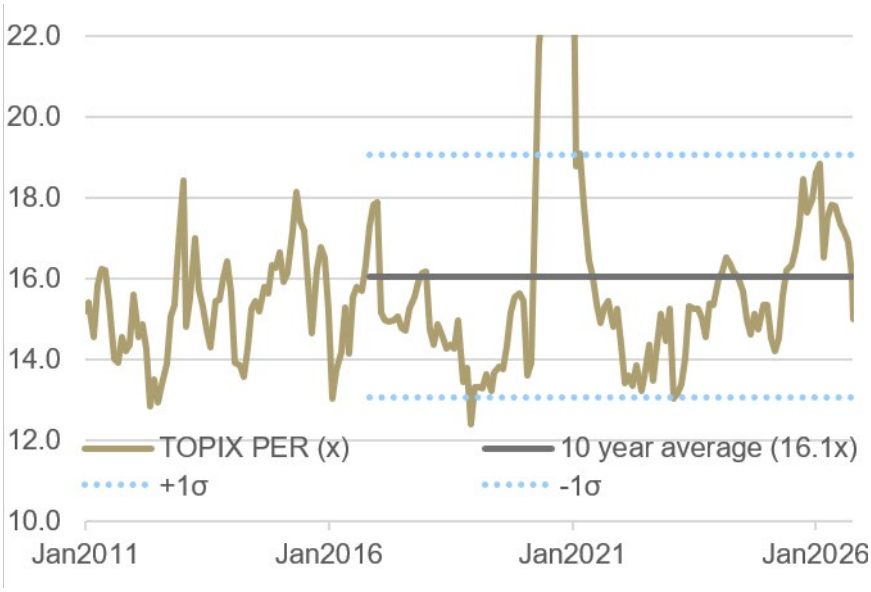
Looking for Investment Opportunities

The latest correction cannot be explained by supply and demand alone. Concerns about the returns on AI investment and elevated valuations have been compounded by uncertainty over possible U.S. policy changes following the midterm elections. Even so, the overall earnings power of Japanese companies and the direction of corporate reform have not fundamentally changed. If flow-driven selling pushes prices beyond what fundamentals warrant, it could present opportunities for long-term investors.

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Valuations are a good place to start when assessing those opportunities. The TOPIX's forward P/E has fallen to around 15, below its 10-year average. As the correction proceeds, valuations may increasingly begin to look attractive.

Figure 2. TOPIX Forward P/E



Source: Nomura Asset Management, based on Bloomberg data. Monthly data from January 2011 to October 2026, supplemented by daily data through November 6.

Price levels and the time horizon also merit attention. As a reference point for gauging the progress of the positioning adjustment, the average purchase level for CTAs and other investors is estimated at around 58,000 on the Nikkei 225 since October 2025, and around 53,000 since June 2025.

The period following the 2024 U.S. presidential election offers a useful comparison. A close race was widely expected, but Trump won decisively, surprising the market. Portfolio repositioning continued in the weeks that followed, while Tesla shares - a prominent example - rose for about a month and a half. A major shift in flows may likewise take time to run its course this time. At the same time, a rapid price adjustment could bring the normalization of supply and demand forward.

Investors should therefore assess not only fundamentals but also the progress of positioning adjustments and the level of valuations. If flow-driven selling pushes more stocks below levels justified by their fundamentals, the resulting dislocation could offer long-term investors an opportunity to identify new investments.

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Nozomi Moriya

Chief Strategist (Institutional Clients)

Nomura Asset Management Co., Ltd. (“Nomura AM”)

Nozomi Moriya is Chief Strategist for Institutional Clients in Japan and overseas at Nomura AM. She joined the firm in September 2026 after more than two decades at UBS, where she worked as an equity analyst covering the Japanese consumer sector before becoming Japan Equity Strategist in 2023.

Drawing on her extensive experience analyzing Japanese companies and industries, she specializes in analyzing Japan’s corporate reforms and connecting bottom-up corporate developments with broader macroeconomic and capital-market trends. She also actively shares her views on Japanese equities with audiences in Japan and abroad, highlighting their global appeal.

She graduated with a B.A. in Economics from the University of Tokyo in 2003.

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  [Calculation formula] Assets amount under contract x fee rate (%) x length of the contract (days) / 365

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