Japanese stocks are on the rise

- The Tokyo Stock Exchange (TSE) reported on Sunday that in the fourth week of May foreign investors were net buyers of Japanese stocks for a ninth consecutive week. We believe that recent reform by Japanese companies is leading to increased foreign purchases of Japanese stocks.

- In terms of ROE (Return on Equity) and PBR (valuation of share prices in terms of net assets), Japanese stocks rank among the lowest of the major economies (Fig. 1). The chart indicates that low ROE is the cause of this low PBR. However, with the TSE urging listed companies to take steps to boost ROE and PBR, Japanese stocks are starting to make progress, with corporate leadership now heeding this call to action.

Will ROE continue to improve?

- The buying and selling of Japanese stocks by foreign investors generally tends to be linked to the ROE of Japanese companies (Fig. 2). In recent years, foreign investors have been reluctant to invest in Japanese equities because their earning power has been lagging compared to that of overseas stocks.

- Recently though, in response to the TSE's call for reform companies have begun to make effective use of surplus reserves, such as via share buybacks, and the TOPIX's real ROE has increased by more than 0.4% points from the end of the fiscal year in March to the most recent quarter, indicating movement toward improving profitability. As the ROE gap between Japanese stocks and those of other developed countries begins to narrow, foreign investors have purchased more than 4 trillion yen (app. USD$29bn) worth of Japanese stocks over the period.

Figure 1. ROE (Return on Equity) and PBR (Price to Book Ratio) of stock indices in major countries

\[ y = 0.3052x - 1.5721 \]

\[ R^2 = 0.7918 \]

Period: As of June 1, 2023

Figure 2. ROE Gap - Japanese vs Developed (4-week moving average) and accumulated foreign investor transactions

\[ \text{ROE Gap} = \text{Japanese stocks} - \text{Developed country stocks} \]

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