Flash Economics

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Japan, beneficiary of capital transfers in shares and bonds?

Japan has long pursued a strategy of investing in the rest of the world in order to benefit from higher returns on capital than those available in Japan.

However, this situation is likely to change, and Japan is likely to become a destination for capital flows, in equities and bonds, from both Japanese and foreign investors.

With regard to bonds, the sharp rise in long-term interest rates in Japan, resulting from relatively high inflation and policies to support demand through public deficits, could make the Japanese bond market more attractive.

As for equities, investors may be concerned about the high valuation of the US market and the weak growth outlook in Europe. With its strong industrial base (electronics, machine tools and robots, metallurgy, steel, shipbuilding, chemicals, automotive, etc..), Japan may be attractive as an alternative investment to US technology companies.

If there is a significant repatriation of capital, in bonds and equities, from the United States and the Euro zone to Japan, long-term interest rates will rise and stock market indices will fall in the United States and Europe.

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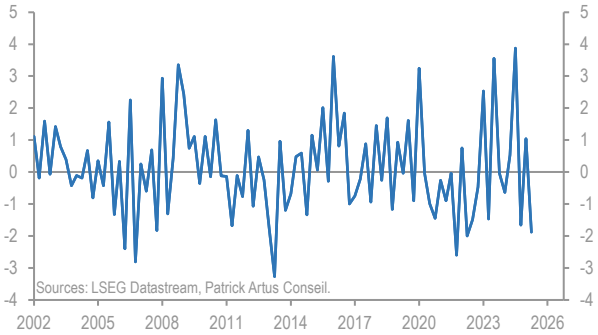
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Japan is traditionally a buyer of bonds and shares in the rest of the world

Japanese investors traditionally have a **strategy of investing in equities and bonds in the rest of the world**, which allows them to benefit from higher bond yields and corporate profitability than in Japan.

Chart 1 shows Japan's **net portfolio investments** in the rest of the world.

Chart 1
Japan: Net portfolio investment* (as % of nominal GDP)



* A positive portfolio investment balance corresponds to an increase in Japan's net external assets, whereas a negative balance implies a reduction in these net assets.

Chart 2 shows the **net stock of portfolio investments** held by Japan in the rest of the world.

Chart 2
Japan : Net portfolio investment position
(as % of nominal GDP)

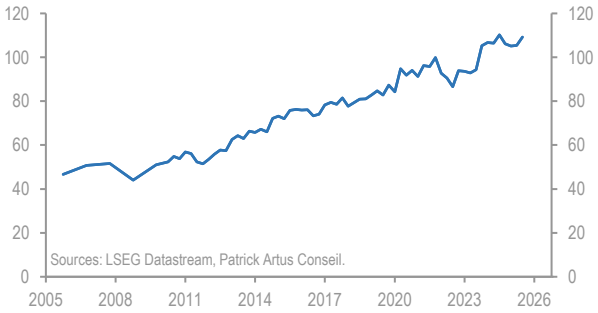
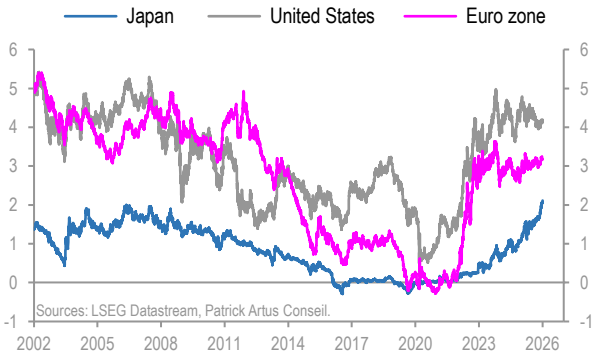


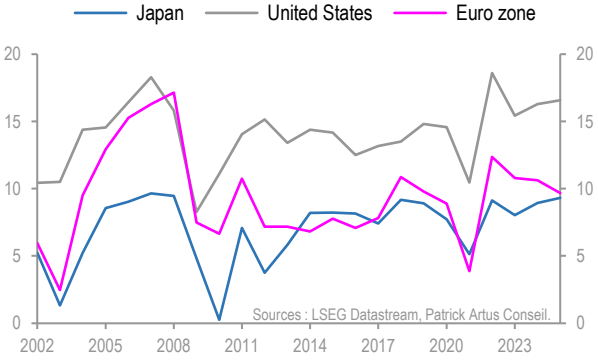
Chart 3 shows the **10-year interest rate** on government debt in Japan, the United States and the Euro zone.

Chart 3
Interest rate on 10-year government bonds (as %)



Finally, **Chart 4** shows the **ROE of companies in Japan**, the United States and the Euro zone.

Chart 4
RoE



It is clear that it was logical for Japan to invest in the rest of the world and accumulate significant net foreign assets (**Chart 5**).

Chart 5
Japan: Net foreign assets (as % of nominal GDP)

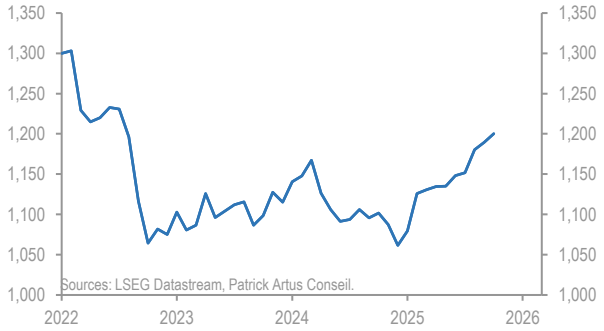


Bond yields will continue to rise in Japan

However, this situation, in which Japanese investors are encouraged to buy US bonds or shares, is set to change significantly.

Let's start with bonds. **Inflation and core inflation in Japan have been hovering around 3% since the summer of 2022. This has pushed the 10-year interest rate on Japanese government bonds up from 0% to 2.08%**. In addition, the yen stopped depreciating against the dollar in mid-November 2025. **We can therefore expect Japanese holdings of US Treasuries (Chart 6) and European government bonds to decline in the future**, especially as the Bank of Japan is expected to raise its base rate (currently 0.75%) further, which is pushing up Japan's long-term interest rates (the 30-year interest rate is currently 3.41%).

Chart 6
United States: Holdings of Treasuries by Japan
(USD bn)



Japanese equities will be attractive

After stagnating in 2024 and early 2025, the Nikkei index rose sharply (by 26% since the beginning of July 2025).

The Japanese stock market should benefit from:

- Concerns about the valuation of US technology companies;
- Weak growth and deindustrialisation in the Euro zone.

Investors should note:

- The very large size of industry in Japan (29% of GDP);
- The significance of R&D expenditure (3.2% of GDP);
- The advanced level of technology (robots, electronic components, telephony, etc.).

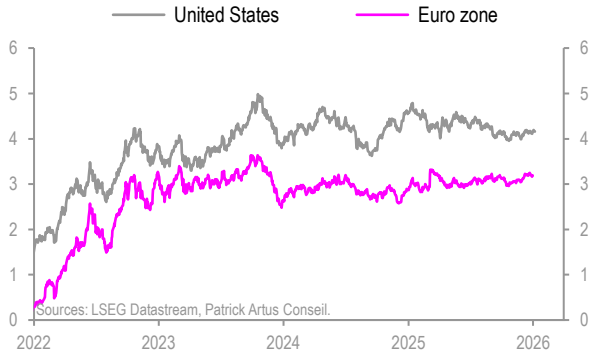
We can therefore expect **investors to make arbitrage decisions that favour Japanese equities and disadvantage US and European equities**.

Summary: a threat to bond markets and equity markets in the United States and the Euro zone

If, as we believe, Japanese investors are more attracted to their domestic bond and equity markets (due to rising long-term interest rates in Japan, growing mistrust of US tech stocks' valuations and weak growth in Europe), we should see:

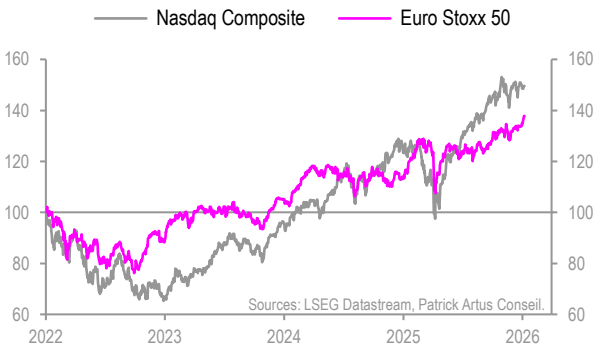
- A rise in long-term interest rates in the US and the Euro zone (Chart 7);

Chart 7
Interest rate on 10-year government bonds (as %)



- A weakening equity market, particularly in the United States (Chart 8), and especially for technology stocks.

Chart 8
Stock market indices (01.01.2022 = 100)



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