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Asset Management One

Japanese Stocks

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Japanese stock valuations have expanded significantly

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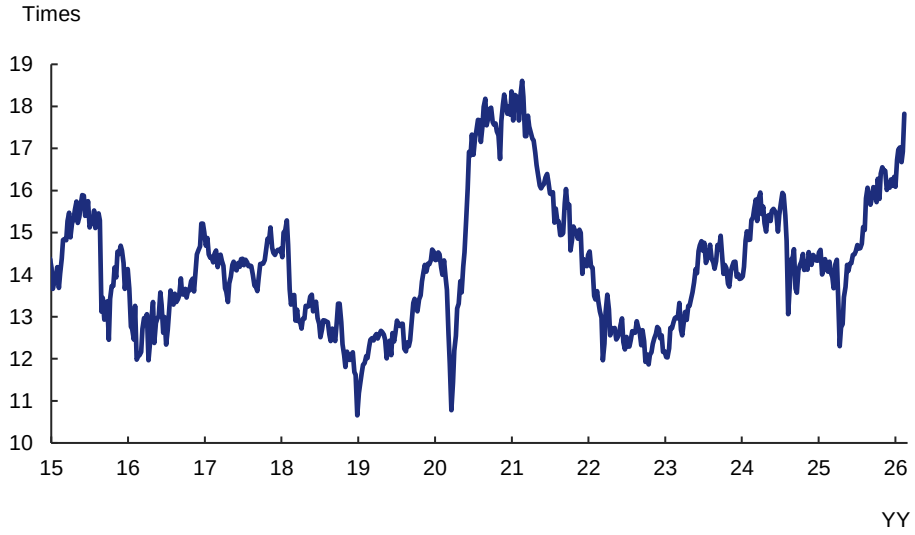
Japanese stocks rebounded sharply from their April 2025 low, which followed the announcement of U.S. reciprocal tariffs. The market strengthened further following the Liberal Democratic Party's landslide victory in the Lower House election. This rally appears to reflect heightened expectations for the economic policies of the new Takaichi administration.

When viewed through the lens of the forward Price to Earnings (P/E) ratio, TOPIX valuations have reached levels that significantly exceed their historical range, excluding the COVID-19 pandemic period (Figure 1). Concerns about potential overvaluation have emerged among some market participants.

On the other hand, the forward P/E ratio for the S&P 500, a leading U.S. stock index, has recently settled above 20 times, significantly exceeding its historical range. This is primarily driven by the high P/E ratios of large-cap tech stocks, which are pushing up the P/E of the benchmark index. To some extent, these high P/E ratios are justified by the strong earnings growth of large-cap tech companies. This raises the question of whether such a substantial rise in the P/E ratio is also justified in Japan, as it is in the U.S.

Figure 1: Forward P/E Ratio for Japanese Stocks (MSCI Japan)



Source: LSEG Data & Analytics, Asset Management One Co., Ltd.
Note: 1. Weekly data from 2 January 2015 to 13 February 2026
2. Based on 12-month forward estimates

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Since last year, the rise in ROE ratio has been notable

The Price to Earnings (P/B) ratio, which can be expressed as the product of P/E ratio and ROE (return on equity) ratio, has also risen significantly (all figures in this report are based on forecasts for the next 12 months). In spring 2023, the Tokyo Stock Exchange requested listed companies to improve capital efficiency. Specifically, it urged companies to address situations where their P/B ratio remained below 1x. To raise P/B ratio (and P/E ratio), which are influenced by market valuation, companies are pursuing various measures to enhance ROE ratio. Examining the trend of ROE ratio for the MSCI Japan index, which represents Japanese equities, shows a continuous rise, surpassing the 10% level that had previously been considered a near-term target (Figure 2). Looking at MSCI Japan's sector indices (11 sectors), the rise in ROE ratio for financial stocks has been particularly pronounced since the COVID-19 pandemic (Figure 3). The key drivers include rising long-term interest rates amid persistent inflation, the resulting expansion of interest margins, and improved capital efficiency through the unwinding of cross-shareholdings and share buybacks. Both macroeconomic factors and corporate efforts appear to have contributed to the increase in ROE ratio.

Figure 2: Forward ROE Ratio and Forward P/B Ratio for Japanese Stocks

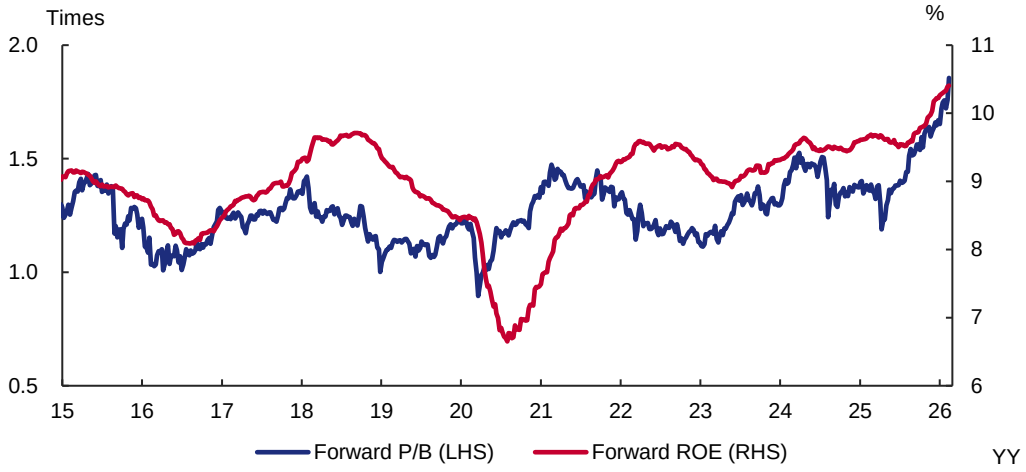

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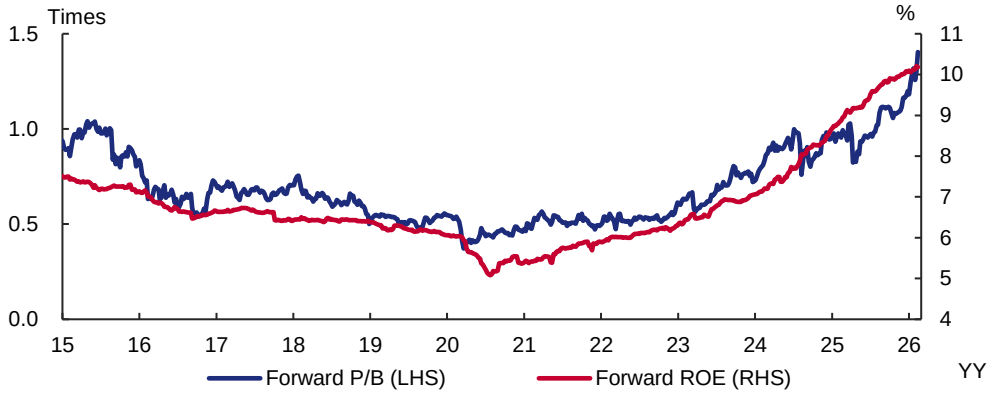
Figure 3: Forward ROE Ratio and Forward P/B Ratio for Financial Stocks



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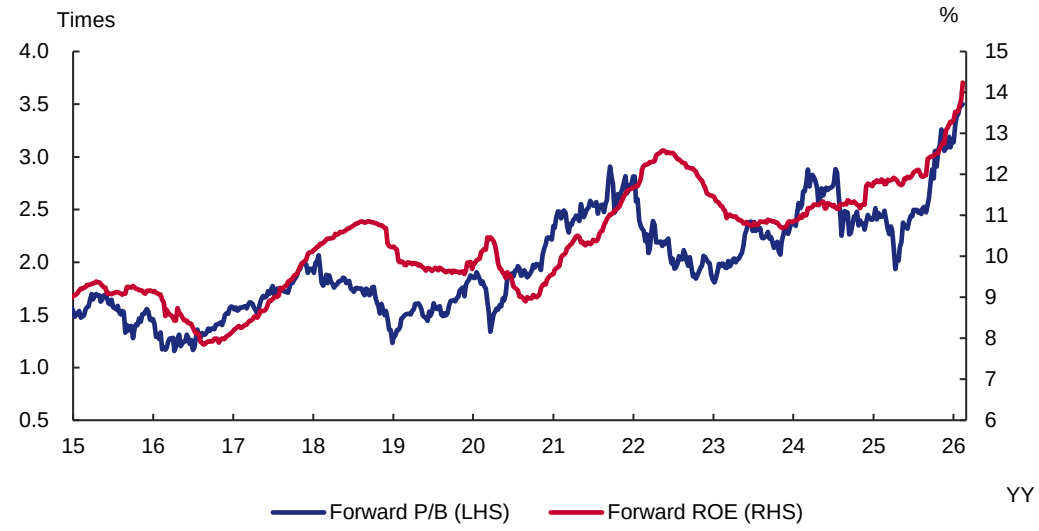
ROE ratio shows an upward trend across a wide range of industries

Furthermore, while the ROE ratio of information technology stocks reveals cyclical patterns spanning several years, the medium to long-term trend remains upward. Additionally, the pace of increase has accelerated recently in the short term (Figure 4).

Since the start of this year, the U.S. stock market has seen selling pressure in software stocks and related stocks, reflecting concerns over potential disruption from AI (artificial intelligence). In Japan, however, the impact on the overall stock market has been more limited compared to the U.S., partly because there are not many large-cap software stocks. On the other hand, hardware stocks, such as semiconductor manufacturing equipment, are seen as being in a situation where expectations for long-term profit growth are likely to strengthen, benefiting from the expansion of AI-related capital investment.

Figure 4: Forward ROE Ratio and Forward P/B Ratio for Information Technology Stocks



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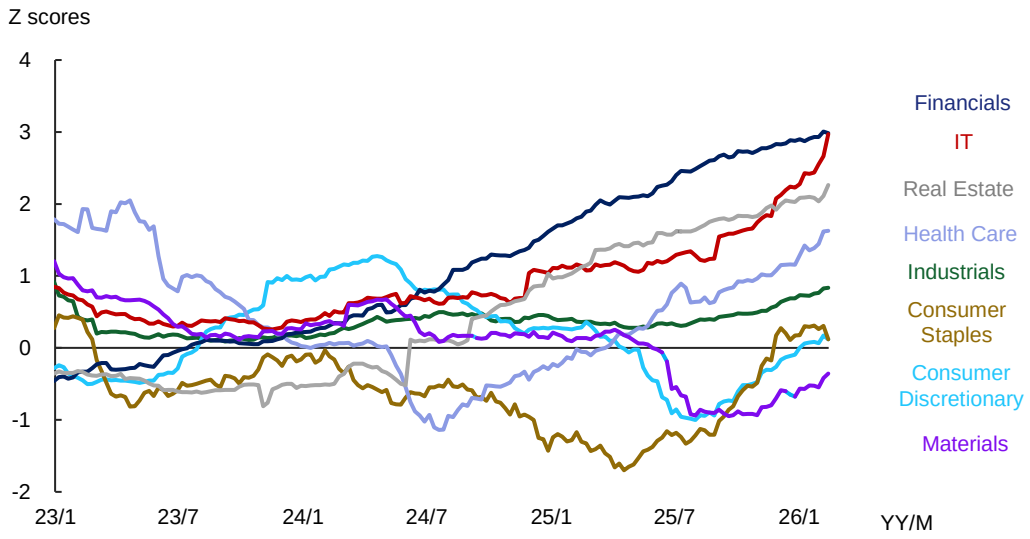
Looking at the degree of deviation from the long-term average ROE ratio across MSCI Japan's sector indices, a broad range of sectors show an upward trend (Figure 5). Beyond financials and information technology, sectors such as real estate and healthcare exhibit significantly larger upward deviations. Against the backdrop of entrenched inflation and improving capital efficiency, this suggests the possibility that ROE ratio has entered an upward trend over the medium to long-term.

Figure 5: Deviation from the Long-Term Average ROE Ratio



Source: LSEG Data & Analytics, Asset Management One Co., Ltd.
Note: 1. Weekly data from 6 January 2023 to 13 February 2026
2. The score indicates how many standard deviations the ROE at each point in time deviates from the long-term average (2015 to present).
For example, a Z-score of 2 means it deviates by 2 standard deviations (+2σ).
3. Display the 8 sectors excluding Energy, Utilities, and Communication Services from the MSCI Japan Sector Index (11 sectors)

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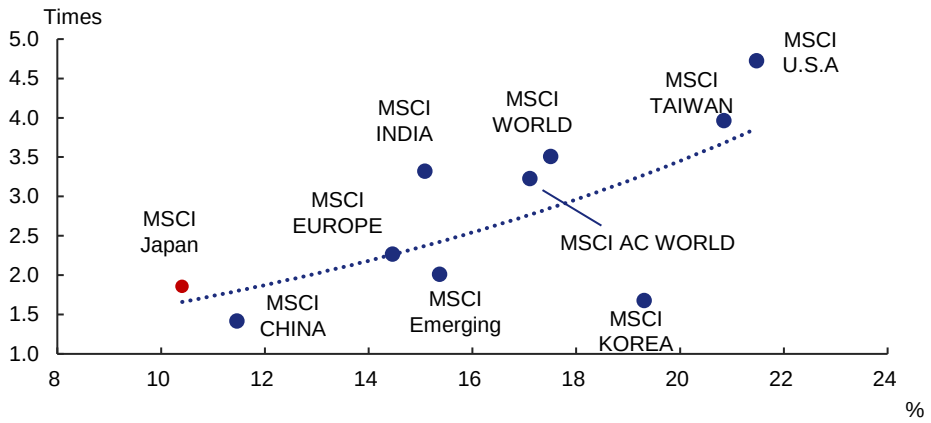
From an international comparative perspective, Japanese stocks do not appear significantly overvalued

Japanese stocks have seen their P/B ratio rise alongside increasing ROE ratio. Figure 6 presents an international comparison of the relationship between P/B ratio and ROE ratio based on the latest data. Japan is positioned close to the trend line. From this perspective, Japanese stocks do not appear significantly overvalued when viewed through the lens of P/B ratio.

Furthermore, Japan's ROE ratio remains relatively low not only compared to the U.S. but also relative to other countries and regions. Significant room for improvement in capital efficiency is still seen across industries beyond financials and information technology. Should the upward trend in ROE ratio become established across a broader range of sectors, Japanese stocks' P/B ratio is expected to rise further.

From a macro perspective, the entrenchment of inflation in Japan is considered a major factor driving the rise in ROE ratio. Going forward, attention will focus not only on corporate efforts to improve capital efficiency, supported by policy measures, but also on whether the overall productivity of the Japanese economy will increase.

Figure 6: The Relationship between ROE Ratio and P/B Ratio (International Comparison)



Source: LSEG Data & Analytics, Asset Management One Co., Ltd.
Note: 1. As of 13 February 2026
2. Use MSCI country/region index values
3. The horizontal axis represents forward ROE, and the vertical axis represents forward P/B
4. The dotted line is an exponential approximation

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