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# Japan | Economic and Financial Market Outlook

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JAN. 2026

**Daiwa**  
Asset Management



## Forecast for Economy, Interest Rates, Equity Markets, REITs, and Foreign Exchange

## How to read the table

... Forecast revised upward (previous estimates)

... Forecast revised downward (previous estimates)

	Real GDP (YoY, %)			
	Actual figures	Estimates		
	2024	2025	2026	2027
US	2.8	1.5	2.0 ← ( 1.6 )	1.8
Japan	▲ 0.2	0.6	0.8	0.8
Euro	0.9	1.4	1.4	1.4

## Monetary Policy Outlook

US	<ul style="list-style-type: none"> <li>2026: Anticipates a total interest rate cut of 0.50 percentage points. Expected to cap at 3.00-3.25%.</li> </ul>
Japan	<ul style="list-style-type: none"> <li>Anticipates rate hikes of 0.25 percentage points roughly every six months. Expected to cap at 1.5%.</li> <li>Government bond purchases reduction: From April 2026, the quarterly reduction amount will be compressed from the current level of approximately ¥400 billion to ¥200 billion as a general rule.</li> </ul>
Euro zone	<ul style="list-style-type: none"> <li>With the central bank deposit rate reaching 2%, considered neutral, and the economy and prices stable, the policy rate is expected to remain unchanged for an extended period.</li> <li>Redeemed bonds will not be reinvested, and no active sales are planned</li> </ul>

	Policy Interest Rate (%)				10-Year Government Bond Yield (%)			
	Actual figures	Latest figures	Estimates		Actual figures	Latest figures	Estimates	
	End of 2024	As of 2025/12/22	End of 2026	End of 2027	End of 2024	As of 2025/12/22	End of 2026	End of 2027
US*1	4.50	<b>3.75</b>	3.25	3.25	4.6	<b>4.2</b>	4.1	4.3
Japan	0.25	<b>0.75</b>	1.25	1.50	1.1	<b>2.1</b>	2.0 ← ( 1.7 )	2.0 ← ( 1.7 )
Euro*2	3.00	<b>2.00</b>	2.00	2.00	2.4	<b>2.9</b>	2.4	2.2

1. US policy rate is the upper limit of the FF rate guidance target

2. The policy rate for the Euro area is the Central Bank deposit rate, and the 10-year government bond yield is the German government bond yield.

Source: Actual values from government and statistical bureaus of each country and Bloomberg; forecast values from Daiwa Asset Management

		Equity Index							
		Actual figures		Latest figures		Estimates			
		End of 2024	Annual Rate of Change	As of 2025/12/22	YTD Rate of Change	End of 2026	Annual Rate of Change	End of 2027	Annual Rate of Change
US	S&P500	5,882	+23%	<b>6,878</b>	+17%	7,400	+8%	8,000	+8%
	DJIA	42,544	+13%	<b>48,363</b>	+14%	50,000	+3%	54,000	+8%
Japan	TOPIX	2,785	+18%	<b>3,405</b>	+22%	3,750	+10%	4,000	+7%
	Nikkei 225 Index	39,895	+19%	<b>50,402</b>	+26%	56,000	+11%	60,000	+7%
Euro	STOXX600	508	+6%	<b>587</b>	+16%	600	+2%	640	+7%
		REIT							
		Actual figures		Latest figures		Estimates			
		End of 2024	Annual Rate of Change	As of 2025/12/22	YTD Rate of Change	End of 2026	Annual Rate of Change	End of 2027	Annual Rate of Change
US	NAREIT Index	24,843	+9%	<b>25,523</b>	+3%	32,000 ← ( 30,000 )	+25%	35,300 ← ( 33,000 )	+10%
Japan	TSE REIT Index	1,653	-9%	<b>1,999</b>	+21%	2,100 ← ( 2,000 )	+5%	2,150 ← ( 2,100 )	+2%
		Exchange Rate (vs. JPY)							
		Actual figures		Latest figures		Estimates			
		End of 2024	Annual Rate of Change	As of 2025/12/22	YTD Rate of Change	End of 2026	Annual Rate of Change	End of 2027	Annual Rate of Change
USD		157	+11%	<b>157</b>	+0%	146 ← ( 144 )	-7%	142 ← ( 140 )	-3%
EUR		163	+5%	<b>185</b>	+13%	168 ← ( 165 )	-9%	162 ← ( 160 )	-4%

Source: Bloomberg for actual values, Daiwa Asset Management for forecast values



## Economy

### Continued Improvement in Manufacturing; Capital Investment Plans Remain Solid

In the December Tankan survey by the Bank of Japan, the business conditions DI for large manufacturers improved for the third consecutive quarter to 15, while non-manufacturers maintained a high level at 34. Although the automobile sector, which is sensitive to US tariff policies, declined slightly, its outlook was revised upward from the previous survey. Corporate capital investment plans also remain solid, indicating that, at present, the downward pressure on the economy from US tariff policies is limited. However, looking ahead, a significant decline in FY2025 recurring profits is expected in manufacturing, particularly in the automobile sector. In addition, deterioration in Japan-China relations and the impact of the conclusion of the Osaka-Kansai Expo raise concerns about a drop in inbound consumption, which warrants attention.

### Maintaining Wage Increase Momentum Comparable to FY2025

The Bank of Japan's Tankan Employment Conditions DI indicates that labor shortages among companies have become increasingly severe against the backdrop of population decline and an aging society. This trend is particularly pronounced in non-manufacturing sectors, especially services. In FY2025, the nationwide weighted average increase in the minimum wage was 66 Yen, marking a record high, with all prefectures exceeding 1,000 Yen. Such developments are likely to broaden the scope of wage hikes. Furthermore, the BOJ's early-December report on 'Trends in Wage Increase Stance for FY2026' confirmed that, despite downward pressure on corporate earnings from US tariff policies, wage increase momentum comparable to FY2025 has been maintained.

### 2026 Budget Proposal to Test Market Confidence

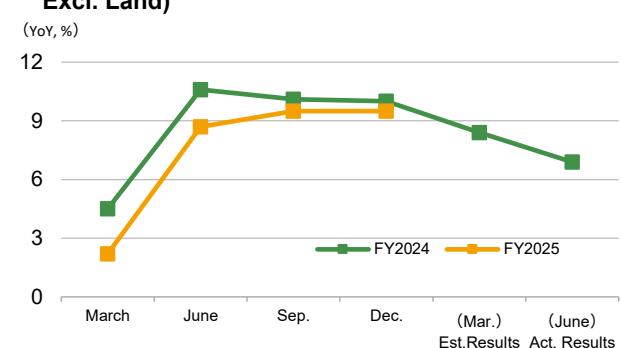
The government is proceeding with the formulation of the initial budget proposal for FY2026. General account expenditures are expected to exceed 120 trillion Yen, surpassing the record-high FY2025 budget. Although the ruling parties (LDP and JIP) narrowly secured a majority in the House of Representatives, they still fall short of a majority in the House of Councillors. To ensure passage of the budget, cooperation from opposition parties that continue to advocate expansionary fiscal policy remains essential, creating an environment conducive to larger spending. On the revenue side, the FY2026 ruling party's tax reform outline included numerous tax cuts prior to securing funding sources. With long-term interest rates reaching 2% and growing concerns over rising debt-servicing costs, Takaichi administration has entered a critical phase to determine the future of its "Responsible Proactive Fiscal Policy".

(Written by Satsuki Yuba, Research Department)

#### BoJ Tankan (Business Conditions DI)



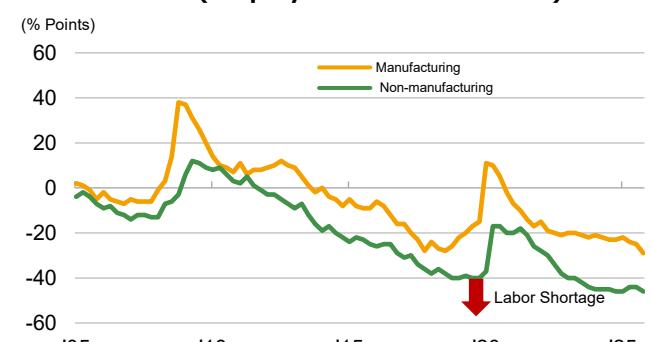
#### Capital Investment Trends (Incl. Software & R&D, Excl. Land)



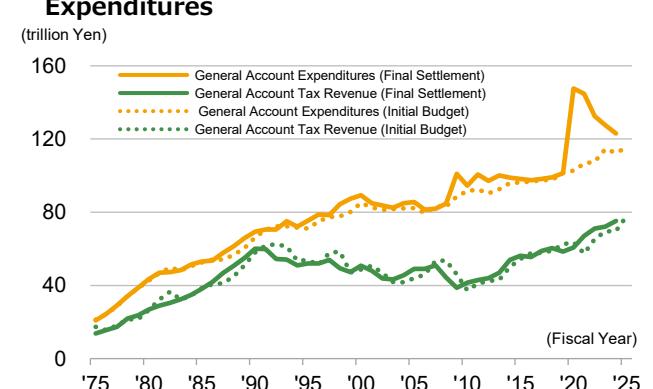
※ This chart illustrates the revision pattern of annual capital investment plans across all sizes and industries, based on six survey rounds from the initial March survey to the June survey of the following year when actual results are confirmed, showing YoY changes at each round.

Source: Bank of Japan; Complied by Daiwa Asset Management

#### BoJ Tankan (Employment Conditions DI)



#### Trends in General Account Tax Revenue and Total Expenditures



※ The latest values are based on final settlement for FY2024 and initial budget for FY2025  
Source: Ministry of Finance; Complied by Daiwa Asset Management



## Equity

### Nikkei Flat While TOPIX Hits New High

Following the sharp rally through October and the emergence of skepticism toward AI-related stocks, the Nikkei has lost upward momentum and continues to hover around the 50,000 mark. In contrast, TOPIX, which better reflects overall market movements, has delivered solid performance, repeatedly hitting new highs. Against a backdrop of structural changes in macro, micro, and supply-demand dynamics, we believe Japanese equities remain in the midst of a medium- to long-term upward trend.

### Earnings Momentum Remains Strong

Japanese companies' earnings momentum remains strong. Although tariff impacts had been a concern, both April–June and July–September results delivered positive surprises, exceeding analysts' expectations. This has reduced downside risk to earnings and raised expectations for the next fiscal year. In fact, earnings forecasts have been revised upward, and TOPIX's projected EPS for FY2026 has been increased. The outlook is also favorable, with a significant profit increase expected in FY2026.

### Upward Shift in Valuation Range

The TOPIX PER has risen above its historical range, but we do not consider it overvalued. Given the progress in structural changes mentioned earlier, we believe the range has likely shifted upward. We estimate the TOPIX PER at around 16 times by the end of 2026, but if structural changes accelerate, there is a possibility of a further upward shift in PER, which could lead to Japanese equities rising beyond our current assumptions.

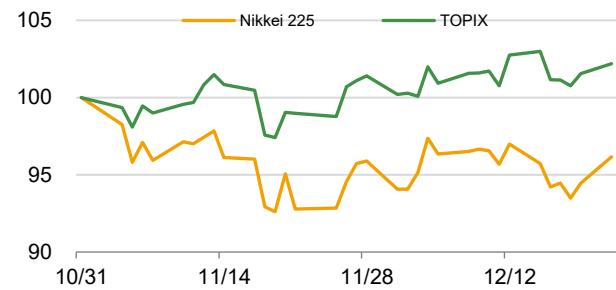
### Will Inflows from Overseas Investors Accelerate?

Since April 2025, inflows into Japanese equities from overseas investors have been on an upward trend. In addition to expectations of further revaluation driven by rising ROE in Japanese stocks, if the Yen appreciates moderately in the currency market as we forecast, US Dollar-based returns will improve and attract global investors' attention. Investors who remain underweight in Japanese equities may face an increasing 'risk of not holding.' We believe overseas investors' positions in Japanese equities are still light, leaving significant room for additional inflows.

(Written by Kazunori Tatebe, Research Department)

### Nikkei 225 and TOPIX Price Movements Since November

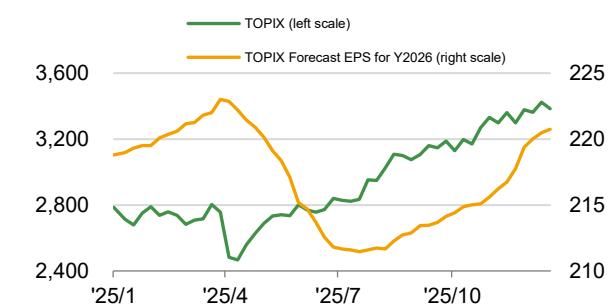
(Indexed with October 31, 2025 = 100)



※ The latest value is December 22<sup>nd</sup> 2025

Source: Bloomberg; Compiled by Daiwa Asset Management

### TOPIX Estimated EPS Continues to Be Revised Upward



※ Estimated EPS is 12 months forward, based on consensus; latest value as of December 19

Source: FactSet; Compiled by Daiwa Asset Management

### Possibility of Upward Shift in TOPIX PER Range

(times)

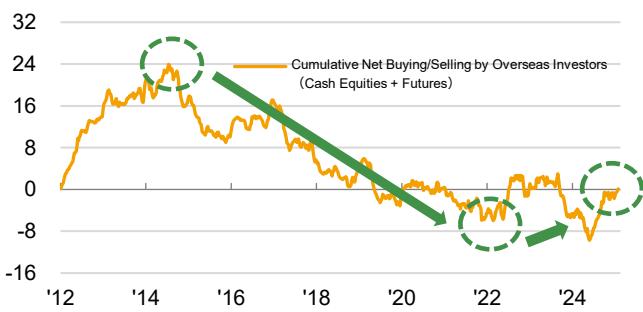


※ The early Abenomics period and the COVID-19 period were special circumstances, and are shown in gray. Latest value as of December 19

Source: FactSet; Compiled by Daiwa Asset Management

### Foreign Investors' Japan Equity Positions Remain Light

(trillion Yen)



※ Trading amounts by investor category are cumulative totals from November 2012 through December 12

Source: Bloomberg; Compiled by Daiwa Asset Management



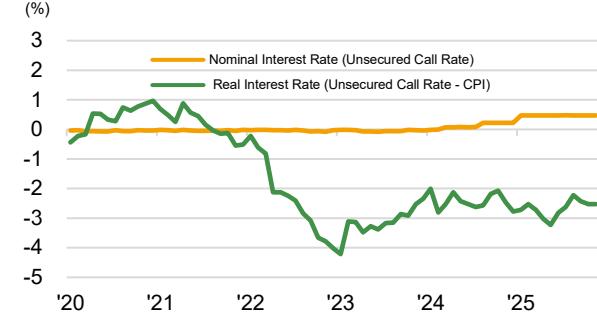
## Interest Rates

### Poised to Continue Rate Hikes: " Still Far from " Neutral Rate "

At its December monetary policy meeting, the Bank of Japan decided, in line with market expectations, to raise the policy rate to 0.75%. The statement noted that the mechanism for wages and prices to rise moderately is likely to be maintained. At the press conference, Governor Ueda stated that 'real interest rates remain significantly negative, and accommodative financial conditions will continue,' and added that 'there is still some distance to the lower bound of the neutral rate,' signaling a continuation of the rate hike path. Based on this stance, we expect rate hikes to occur roughly every six months going forward, with a terminal rate of 1.5%. Reflecting the upward revision in market expectations for the final rate level, we have raised our long-term interest rate outlook. While concerns over fiscal deterioration surrounding the FY2026 initial budget proposal may rekindle risks of worsening bond supply-demand conditions, considering the relationship with two-year policy rate expectations, we anticipate long-term rates will remain elevated near 2% for the time being.

(Written by Satsuki Yuba, Research Department)

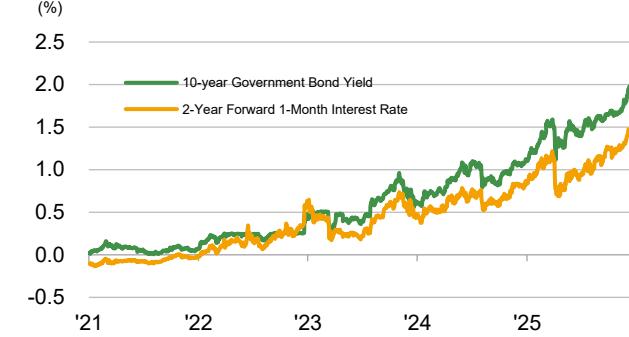
#### Policy Interest Rate (%)



※ CPI excludes fresh food, YoY change (consumption tax adjusted), Unsecured Call Rate is month-end value, latest value is November 2025

Source: Ministry of Internal Affairs and Communications, Bloomberg; Complied by Daiwa Asset Management

#### 10-year Government Bond Yield and 2-Year Forward 1-Month Interest Rate (%)



※ 2-year forward 1-month interest rate corresponds to 2-year forward policy rate expectation

※ Latest value as of December 22, 2025

Source: Bloomberg; Complied by Daiwa Asset Management

## J - REIT

### Upward Revision of Index Outlook

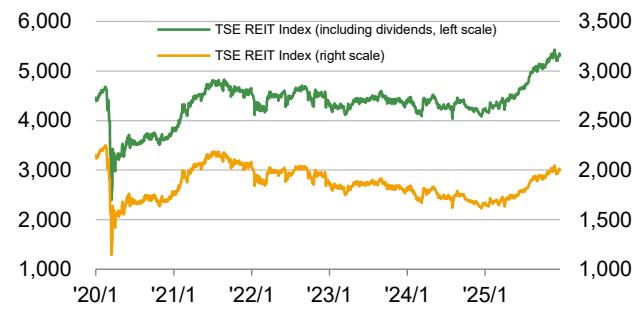
In early December, the Tokyo Stock Exchange REIT Index adjusted to around 1,950 due to concerns over deteriorating supply-demand conditions stemming from rising long-term interest rates and public offerings. However, from mid-month onward, it rebounded and recovered to around 2,000.

We have revised our forecast for the TSE REIT Index to 2,100 at end-2026 (previously 2,000) and 2,150 at end-2027 (previously 2,100). While the increase in borrowing costs due to rising interest rates is a negative factor, we raised our profit growth assumptions on the back of a rental market performing better than expected. In addition, we judged that the risk premium required for the J-REIT market has declined, driven by expectations for sustained profit growth, and therefore revised our outlook upward.

The key focus for 2026 will be public offerings. While concerns remain about supply-demand deterioration from public offerings, such offerings could also serve as a growth driver for the J-REIT market by boosting per-share dividend growth. We are watching closely to see which factor the market prioritizes.

(Written by Kazuhiko Arai, Global Asset Management Department)

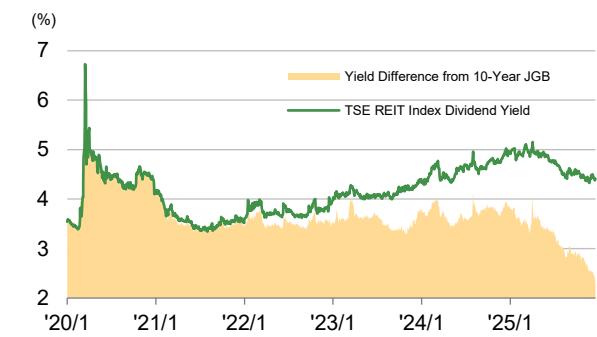
#### Trend of the Tokyo Stock Exchange REIT Index



※ Latest value as of December 22, 2025

Source: Bloomberg; Complied by Daiwa Asset Management

#### Trend of the Dividend Yield for the Tokyo Stock Exchange REIT Index (%)



※ Dividend yield is based on the actual performance of the past 12 months

※ The latest value is as of December 22nd, 2025

Source: Bloomberg; Complied by Daiwa Asset Management



## U S D o l l a r

### USD/JPY Rises as Yen Weakness Outpaces Dollar Decline

Over the past month, both the Yen and the US Dollar have weakened against other currencies (see right chart, 25 currencies), leaving USD/JPY with only minor fluctuations. Concerns over Japan's fiscal deterioration contributed to Yen weakness, while risk-on sentiment drove both Yen and US Dollar lower. Domestic and overseas interest rates rose, but the impact of rates on exchange movements was limited. However, given expectations that the Fed will not rush additional rate cuts, and the BOJ will not hasten further rate hikes, Yen weakness has recently outweighed Dollar weakness, causing USD/JPY to edge higher.

### Signs of Narrowing Yen Weakness Beyond Interest Rate Differentials

Based on the recent Japan-US real interest rate differential, USD/JPY should be around 141–144 Yen, but the current level is well above that. The main reason is that Yen weakness persisted during the risk-on environment in the second half of 2025. In addition, the Takaichi administration's fiscal expansion contributed to selling of Japanese bonds and the Yen, further driving Yen depreciation beyond what the rate differential would suggest. However, since late November, there have been signs that the gap from the level implied by the Japan-US real interest rate differential is narrowing, and we expect the trend to shift toward Yen appreciation and Dollar depreciation going forward.

### Yen Strengthens, Dollar Weakens on US Economic Slowdown Concerns

The recent strength in US economic indicators, which exceeded market expectations and pushed up the US Economic Surprise Index, has supported risk-on-driven Yen weakness. However, the index is now declining. The positive impact on the economy from tariff reductions may also have run its course. Although US tariff rates have fallen, they remain higher than before, meaning their negative effects are likely to persist for some time. In addition, reduced wealth effects and a slowdown in Dollar depreciation are expected to act as factors for economic deceleration. As the US Economic Surprise Index declines, risk-on-driven Yen weakness will fade, and we expect USD/JPY to fall.

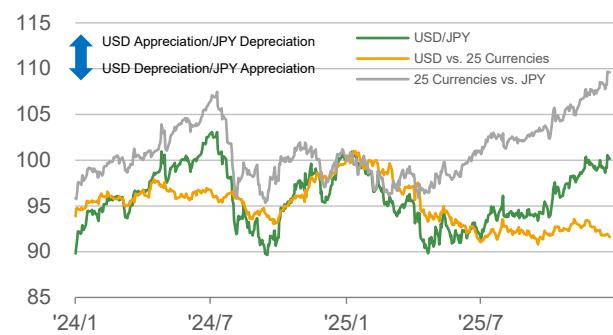
### Commodity Price Declines Signal Drop in USD/JPY

In the second half of 2025, US interest rates declined while risk-on sentiment persisted, driving commodity prices higher along with Yen weakness and Dollar strength. A correlation has been observed between the commodity index and USD/JPY, and for now, market risk appetite appears to hold the key for both. Recently, risk-on sentiment has slowed, and there are signs of a decline in commodity prices, particularly in energy. As economic sentiment weakens, we expect commodity prices—including non-energy sectors—to fall further, accompanied by Yen appreciation and Dollar depreciation.

(Written by: Yuji Kameoka, Research Department)

#### Exchange Rates of USD/JPY and Other Currencies

(January 2025 = 100)

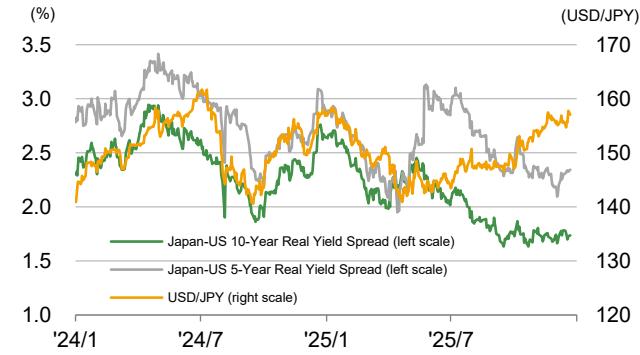


※Weighted average of exchange rates for 25 currencies based on April 2022 trading volumes

※The latest value is December 22<sup>nd</sup>, 2025

Source: BIS and LSEG; Compiled by Daiwa Asset Management

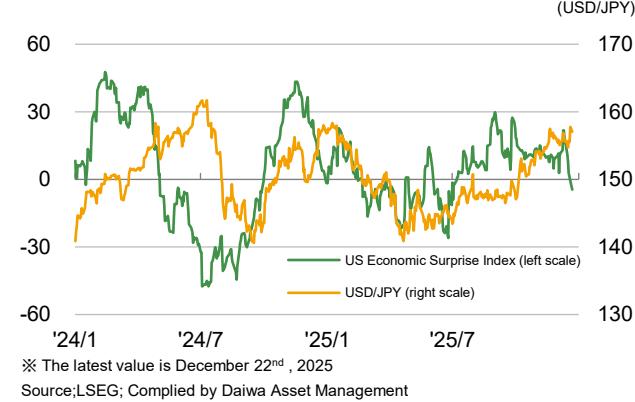
#### Japan-US Real Interest Rate Differential and USD/JPY



※The latest value is December 22<sup>nd</sup>, 2025

Source: LSEG; Compiled by Daiwa Asset Management

#### US Economic Surprise Index and USD/JPY



※The latest value is December 22<sup>nd</sup>, 2025

Source: LSEG; Compiled by Daiwa Asset Management

#### Commodity Composite Index and USD/JPY



※ The latest value is December 22<sup>nd</sup>, 2025

Source: LSEG; Compiled by Daiwa Asset Management



## Euro

### Expecting a Shift to Euro Weakness and Yen Strength

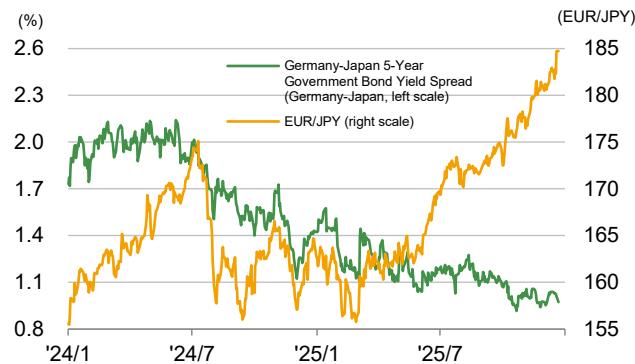
Risk-on sentiment and concerns over Japan's fiscal deterioration have driven Euro strength and Yen weakness. Recently, both Japanese and German interest rates have risen, limiting the impact of rates on EUR/JPY, but we see room for relative declines in German rates and Euro weakness. Looking ahead, as the positive effects of US tariff reductions fade and economic sentiment in major countries peaks, the risk-on pressure for Yen depreciation is expected to recede, leading to a shift toward Euro weakness and Yen strength.

### Euro-Dollar Exchange Rate Moving Toward Stabilization

The Euro strengthened against the US Dollar. This was partly due to sustained expectations for additional Fed rate cuts, while expectations for further ECB rate cuts receded, and German interest rates rose relative to US rates. However, we believe there is limited scope for Euro appreciation against the US Dollar from an interest rate perspective, as Eurozone economic sentiment and expectations for ECB rate hikes are unlikely to increase significantly. Looking ahead, global economic slowdown concerns are expected to generate risk-off pressure for Euro weakness and US Dollar strength, leading to stabilization in the Euro-US Dollar exchange rate.

(Written by: Yuji Kameoka, Research Department)

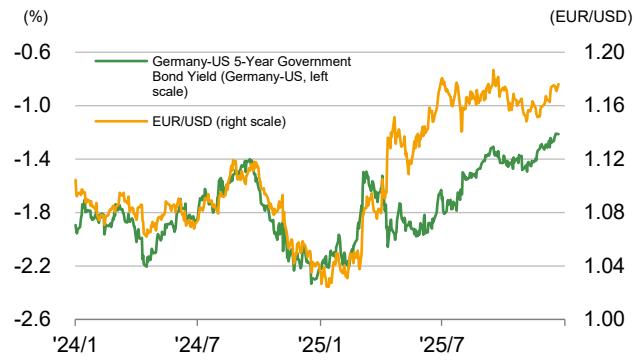
#### 5-year German-Japanese Government Bond Rate Differential and EUR/JPY Exchange Rate



※ The latest value is December 22<sup>nd</sup>, 2025

Source: LSEG; Complied by Daiwa Asset Management

#### 5-year German-US Government Bond Rate Differential and EUR/USD Exchange Rate



※ The latest value is December 22<sup>nd</sup>, 2025

Source: LSEG; Complied by Daiwa Asset Management

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