azimut

AZIMUT GLOBAL VIEW

27.07.26

Main Events

Azimut Global Network

- Milan
- Abu Dhabi
- Austin
- Cairo
- Chicago
- Dubai
- Dublin
- Hong Kong
- Estoril
- Istanbul
- Lugano
- Luxembourg
- Mexico City
- Miami
- Monaco
- New York
- Santiago
- São Paulo
- Shanghai
- Singapore
- St Louis
- Sydney
- Taipei

FOMC MEETING — 29.07
The Fed is expected to hold rates in July. Investors will watch for clues on September, when a hike is largely priced in

BOE MEETING — 30.07
The MPC is expected to hold rates. Investors will focus on forward guidance for September, when a hike is roughly 50/50 priced in

BOJ MEETING — 16.07
The BOJ is widely expected to hold rates in July. However, it recently signaled readiness to hike faster than expected.

US NON-FARM PAYROLLS — 23.07
As a key input to the Fed's dual mandate, investors will watch for confirmation of the recent slowdown in U.S. job creation

THE LAND OF THE RISING INFLOWS: THE PROSPECT OF CAPITAL REPATRIATION IN JAPAN

- **Japan's Finance Minister Katayama's recent remarks have revived talk of policy measures aimed at supporting the domestic bond market and the Yen**
- **Japan's domestic investors have allocated trillions abroad since Abenomics - even a partial repatriation of that capital has the potential to prop up both the Yen and Japanese Government bonds**
- **While markets may pressure the administration to act soon, a gradual, multi-year rollout seems the most likely form of implementation**

Recent comments from Japan's Finance Minister Satsuki Katayama have ignited speculation about repatriation flows into Japanese assets. In this report, we provide background on Japan's key domestic investors and portfolio flows, along with our view on the statement's potential implications.

Japan's largest domestic investors are dominated by massive public pension funds and institutional conglomerates:

- Government Pension Investment Fund (GPIF): managing roughly $1.8 trillion in assets, it is the second-largest in the world by AUM, behind Norges Bank Investment Management ($2.1 trillion). GPIF's asset allocation heavily dictates national market trends.
- Life Insurance firms ("Lifers"): companies like Nippon Life Insurance ($600bio), Daichi Life ($270bio), and Meiji Yasuda Life ($300bio).
- Banking Conglomerates: Mitsubishi UFJ Financial Group (MUFG, asset management arm AUM: $650bio), Mizuho Financial Group (asset management arm AUM: $500bio) and Sumitomo Mitsui Financial Group (SMFG, asset management arm AUM: $160bio).

(continued)

- Asset Managers: Nomura Asset Management (Japan's largest wealth manager, $700bio) and Daiwa Asset Management ($300bio);

- Postal Financial Entities: Japan Post Bank ($1.5trio) and Japan Post Insurance ($400bio);

- Cooperative banks: comprised of three major institutional networks, each serving different segments of the economy. Norinchukin Bank ($550bio, Agricultural, Fishery and Forestry), Shinkin banks ($1.2trio, SMEs) and Rokin Labour Banks ($150bio, Workers' cooperatives).

These institutions hold trillions in assets, which historically flowed heavily into global markets due to low domestic interest rates and sluggish performance of domestic equities. The trend of outbound capital flows accelerated with "Abenomics", the economic plan launched in Japan in 2013 by Prime Minister Shinzo Abe. The Government encouraged large institutions (like GPIF) to switch out of low-yielding Japanese Government Bonds into riskier and higher yielding assets, both domestic and foreign. In 2014, GPIF reduced its domestic bond allocation from 60% to 35%, funnelling the freed-up capital into foreign equities and foreign bonds and eventually targeting a 50%/50% split between domestic and foreign assets. Other investors followed suit, contributing to cement Japan's position as of one of the world's top creditor nations. Currently, Japan's Net International Investment Position[1] stands at $3.5trio, matching Germany's as the largest in the world.

While Abenomics succeeded in pushing domestic equities higher, more structural changes have materialized as a consequence of the twin shocks brought about by the COVID-19 pandemic and the Russo-Ukrainian conflict. The confluence of higher inflation—largely driven by rising energy prices—and extensive fiscal stimulus, produced a substantial depreciation of the Japanese Yen (JPY) alongside an upward move in Japan Government Bond (JGB) yields. The election of Sanae Takaichi as Prime Minister, in October 2025, provided further impetus to these trends, given her aggressively expansionary policy leanings. Moreover, the outbreak of conflict in Iran exerted further downward pressure on both JGBs and the JPY, reflecting Japan's heavy reliance on Gulf energy imports.

In light of such developments, it is unsurprising to see official rhetoric shifting towards repatriation. Encouraging domestic institutions to reallocate a portion of their foreign holdings into domestic assets offers an effective way to achieve the desired policy goals—capping JGB yields and the depreciation of the Yen—either as a substitute or as a complement to alternative solutions.

More specifically, if the Bank of Japan (BOJ) tried to stabilize the bond market by purchasing a large amount of JGBs, the JPY would weaken. Similarly, should the BOJ turn aggressively hawkish to re-establish credibility on inflation, the JGB curve would most likely sell off (albeit staging a bear-flattening). Also, recent attempts at propping up the Japanese currency via intervention have proved ineffective in the medium term. Repatriation, on the other hand, would be supportive of both JGBs and the JPY.

With respect to equities, exporters would face headwinds from a stronger domestic currency. However, given how cheap the currency currently is, a 5-10% appreciation could easily be tolerated. Furthermore, a portion of the repatriated capital would flow from foreign to domestic equities.

Among the large Japanese investors, GPIF is by far the most important, given its size and influence on other domestic players' investment decisions. GPIF owns $1.8 trillion in assets, approximately equally split between domestic/foreign bonds and domestic/foreign equities (25% each). It currently holds over $400bio of foreign bonds and a change in allocation would signal a powerful repatriation trend. While GPIF's board reviews its target asset portfolio every five years (current plan: April 2025-March 2030), it allows deviation bands around its asset allocation. These bands are -/+5% for foreign bonds and -/+6% for domestic bonds and foreign/domestic equities. Under these operational bands alone GPIF has the flexibility to rotate roughly $150-200bio back into domestic assets.

A bandwagon effect among other domestic investors, coupled with follow-through from non-domestic players ranging from asset allocators to speculative accounts, could drive total cross-border inflows well beyond $500bio. To put things into context, Japan's top institutional investors ex-GPIF own about $1.7-2.1trillion in foreign assets. A 20% re-calibration into domestic assets, in line with the shift allowed by GPIF's deviation bands, would generate an additional $350-400bio in capital inflows.

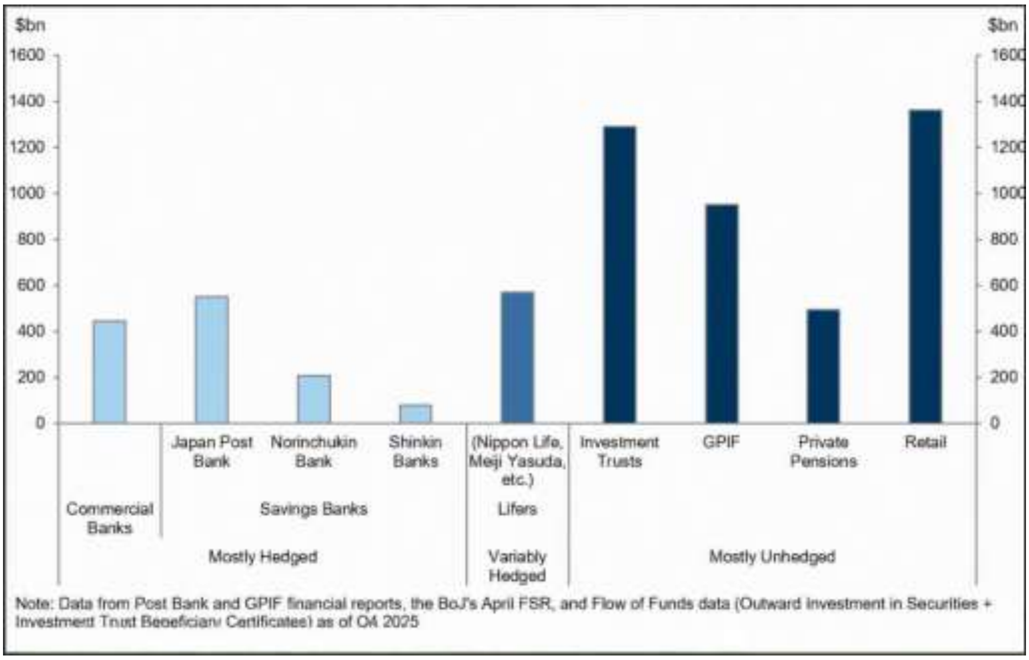
[1] Net International Investment Position (NIIP): The difference between a country's foreign assets and its foreign liabilities.

(continued)

Total household exposure to foreign currency assets currently stands at about $600bio. Japanese Finance Minister Katayama recently announced that the government is considering allowing JGBs to be held in the tax-free Nippon Individual Savings Account (NISA) program to attract retail investors. The combination of attractive levels of JGB yields, an undervalued JPY and tax incentives with the broader push towards repatriation has the potential to unlock an additional $100-150bio of inflows. Furthermore, the prospect of institutional support for the JPY and JGBs would most likely prompt foreign capital to partake in these trends, adding to the overall size of the inflows into Japanese assets.

On the subject of hedging, the chart below outlines FX hedging patterns across key investor groups.

Key Japanese Investor Holdings of Foreign Securities



Source: BoJ, Haver Analytics, GPIF, Japan Post Bank, Goldman Sachs Global Investment Research

Typically, equity investments are left unhedged, as equity returns can absorb FX volatility. On the contrary, Fixed Income assets typically see hedging ratios between 40 and 50%. Worth highlighting that GPIF's core policy benchmark for foreign bonds is officially unhedged.

In a structural repatriation scenario, if JGBs and the JPY are likely to be the main beneficiaries, which international markets stand to lose?

According to Ministry of Finance (MOF) and IMF Coordinated Portfolio Investment Survey (CPIS) data, Japan's foreign portfolio holdings are dominated by the U.S. ($2.3trio), followed by the Cayman Islands ($853bio), France ($204bio), UK ($167 bio), Australia ($137bio), Luxembourg ($122bio), Ireland ($122bio), Germany ($97bio) and Italy ($68bio). With respect to the bond market, the biggest holdings of domestic Japanese investors are in the U.S. ($1 trio+), France ($70-80 bio) and the UK ($40-50 bio), followed by Australia, Germany, and Italy.

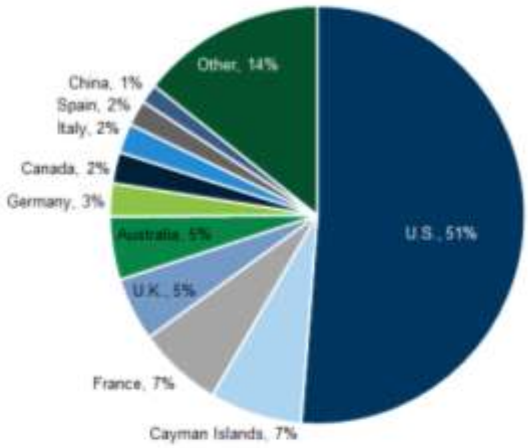
Any liquidation of foreign portfolio assets is likely to focus more on equities, where investors have capital gains, rather than on foreign fixed income securities, where they have losses.

While a gradual approach will most likely universally be preferred to avoid disruption in financial markets, political considerations are also going to play an important role. On this point, frequent hints of "shadow coordination" between the US and Japan—exemplified by recent high level dialogue regarding JPY stability between Finance Minister Katayama and US Treasury Secretary Scott Bessent—as well as the importance of the U.S. defense umbrella over Japan are likely to mean that U.S. Treasuries, and U.S. assets in general, will be handled with extra care.

(continued)

Conversely, the prospect of a political rupture in France, where voters in the second round of the Presidential election will probably have to choose between the far-left candidate Melenchon and the far-right candidate Marine Le Pen, is likely to deter foreign investors from owning French debt, or any investment exposure to the country.

CPIS: Japan Investment in Foreign Debt Securities



Source: IMF Coordinated Portfolio Investment Survey

Another key question relates to the potential timeline of the implementation, particularly considering Japan's institutional framework's propensity to "slow-move".

On this point, we would argue the following:

1. First, the administration will try to strike a balance between "gradual"—to avoid disruption—and "forceful", to incentivize other investors (also foreign) to participate in the shift, thereby amplifying its effectiveness;

2. Second, FinMin Katayama's statements released on July 10th convey a sense of urgency, probably motivated by the need to cap JGB yields in order to be able to continue supporting growth through fiscal spending;

   "[…] we would like to pursue measures to encourage the public to directly enjoy the fruits of Japan's economic growth, starting with households, and then encouraging pension funds, including GPIF, to further invest in Japan's financial assets."

   "[…] we would like to quickly concretize and proceed with a review of the product characteristics of Japanese government bonds for individual investors and the design of new products. This is a policy to improve the attractiveness of Japanese government bonds."

3. Lastly, previous similar episodes saw implementation through multiple phases, with large market moves over an extended period. As an example, Abenomics was first campaigned in late 2012, with the "first arrow" (fiscal stimulus package) launched in January 2013 and QE following in April 2013. Later, in October 2014, the BOJ expanded its QE program and GPIF announced a substantial reallocation toward foreign equities and bonds. The yen depreciated about 30% between late 2012 and late 2013, and a further 10% between late 2013 and late 2014.

To summarize, while it is still too early to draw definitive conclusions, repatriation offers a viable and effective path for the Japanese administration to stabilize the JPY and the domestic bond market. Moreover, the use of repatriation as a stabilization tool may spark broader debate on how countries' relative financial strength is impacted by their Net International Investment Position.

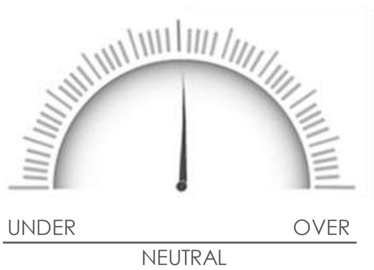
Asset Allocation View

	−	=	+
Equity			
Developed Markets		■	
Emerging Markets		■	
Fixed Income			
Developed Markets Sovereign		■	
Developed Markets Corporate			■
Emerging Markets			■
Commodities		■	
Currencies		*Commentary below*	

− UNDER = NEUTRAL + OVER

Equity

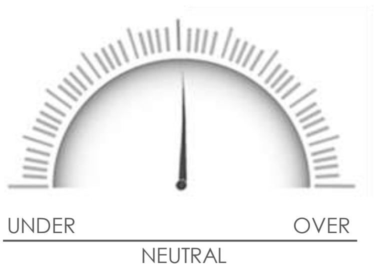
Developed Markets



We maintained the **Neutral** recommendation on Developed Market equities. Rising real interest rates, uncertainties surrounding the Fed's monetary policy under Warsh's leadership and market reactions to upcoming capex announcements by hyperscalers, lofty valuations, unfavorable seasonality, and ever-present geopolitical risks all point to the need for greater caution. However, in light of the ongoing rotation within the major indices and another exceptionally strong earnings season, any correction that may occur is still viewed as an opportunity to accumulate stocks.

US	=	**Europe**	+	**Japan**	=

Emerging Markets



We kept our **Neutral** stance on Emerging Market equities. The same factors—both positive and negative—mentioned above also apply to emerging markets. Perhaps even more so, considering that technology's weight in the EM index is north of 40% and is concentrated in semiconductor and memory manufacturers—that is, the part of the tech sector most dependent on capex by hyperscalers. This is altering the typical features of the EM index, which has always been more value-oriented and closely tied to the economic performance of individual countries. Furthermore, the growing use of leveraged instruments, such as ETFs, is fueling extreme volatility in some markets. The long-term outlook remains positive, but it is advisable to wait for volatility to normalize before further increasing exposure.

Asia ex-Japan	=	**EEMEA**	=	**LATAM**	=

Fixed Income

Developed Markets Sovereign

We have maintained our **Neutral** recommendation on Developed Market sovereign bonds. The level of interest rates continues to depend primarily on whether the Strait of Hormuz remains closed or is reopened. As such, it is not possible to make a clear call on the direction of rates, as it depends on geopolitical factors. Nevertheless, the rise in yields since hostilities resumed has brought rates back to more attractive levels, which already factor in the possibility of further rate hikes by central banks and thus offer a greater margin of safety. However, given the highly uncertain situation, the short- and intermediate segments of the curves continue to be preferred.

EU Core =	**EU Periphery** =	**US Treasury** =	**Japanese JGB** =

Developed Markets Corporate

We kept our **Slightly Overweight** recommendation on Developed Market corporate bonds. The hunt for yield continues, fueled by ample liquidity, with spreads nearing all-time lows. If global growth continues to hold up relatively well, there is no reason to be overly cautious and exit the market prematurely. Within credit, we continue to prefer investment-grade bonds over high-yield.

IG Europe +	**IG US** +	**HY Europe** −	**HY US** −

Emerging Markets

We left our recommendation on Emerging Markets Debt unchanged at **Slightly Overweight**. The reasons are the same as those just outlined for developed countries' corporate bonds.

Local Currency =	**Hard Currency IG** =	**Hard Currency HY** =

Commodities

Our recommendation for commodities remains **Neutral**. We remain cautious on precious metals given headwinds from central bank selling and the higher-yield environment, though our medium- to long-term view stays positive. We're more bullish on industrial metals, driven by growing competition for essential raw materials.

Precious =	**Energy** =	**Industrial** =	**Agricultural** =

Currencies

We have lowered our recommendation on the US Dollar back to **Neutral**. We believe it is unlikely that the Fed will raise rates at this week's meeting. Since market rates indicate a 30% probability of a rate hike, if that does not happen, the dollar could give back some of its recent gains.

Similarly, the recommendation on the Euro has been upgraded to **Neutral** as well. This is not only in relation to the downgrade of the US dollar to neutral, but also to the fact that the ECB has leaked that it may consider another rate hike in September.

The recommendation on the **Chinese Renminbi** remains **Neutral.**

The outlook for other **emerging market currencies** has been confirmed as **Neutral with a bullish bias**, with a preference for currencies of countries that are net exporters of commodities.

Euro	=	USD	+	CNY	=	Other EM	=