

JAPAN'S YEN WEAKNESS HAS CHANGED THE COMPETITIVE LANDSCAPE

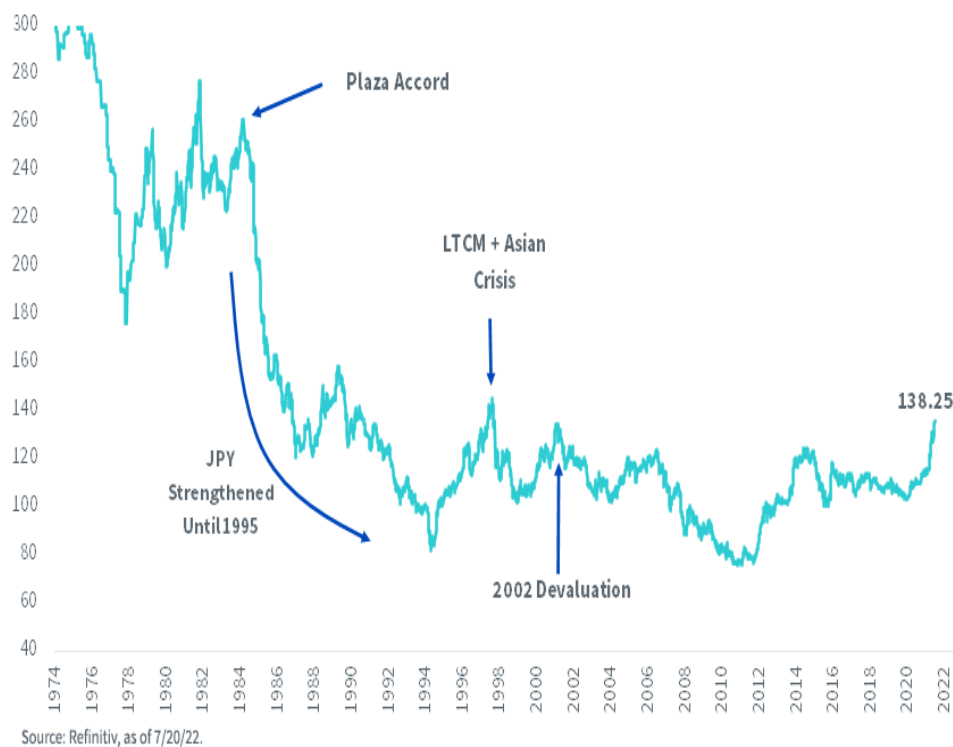
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We are living through another chapter in the decade-old currency wars—and Japan is winning.

After a bold move from ¥103 to ¥138 per dollar in less than two years, suddenly the Japanese yen is at a weakness level not seen since 1998.

The yen's collapse is even more remarkable when you consider that Japan's [consumer price inflation](#) was 2.5% over the last year—a far cry from the 9.1% rate in the U.S. (figure 1).

Figure 1: Japanese Yen per U.S. Dollar

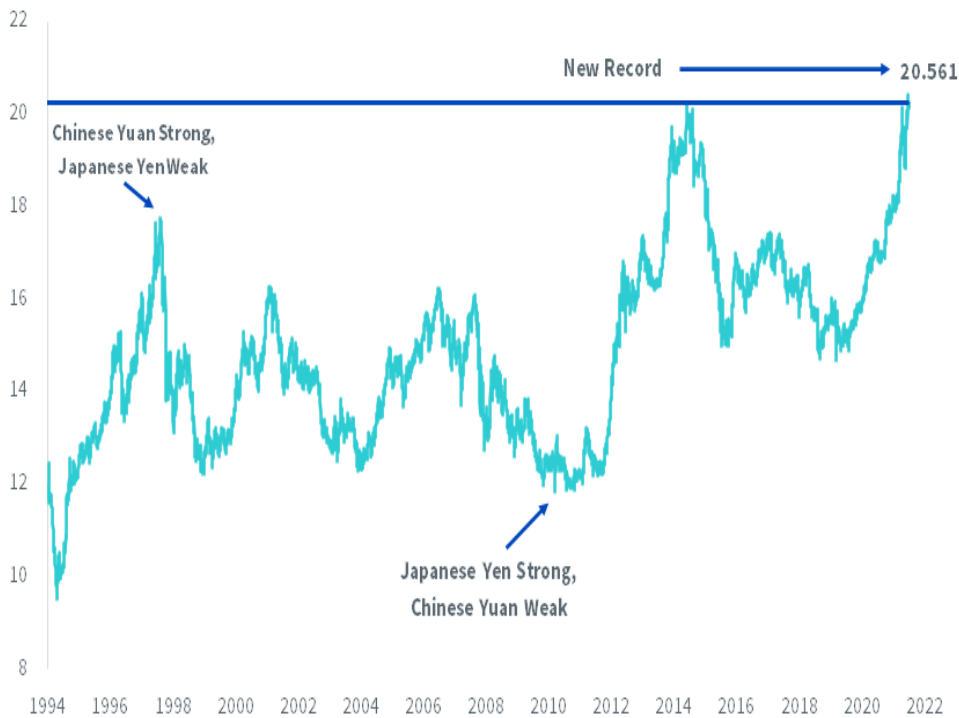


Dollar-yen isn't the only pair that matters. There is also a moment of truth happening right now between the yen and the Chinese yuan.

Each country is the other's largest regional trade rival, so it's notable that the yen is attempting to break through ¥20.56 per Chinese yuan, which would mark uncharted weakness for Japan's currency (figure 2).

It has created a situation in which Japanese corporations are becoming increasingly price competitive against companies based in China.

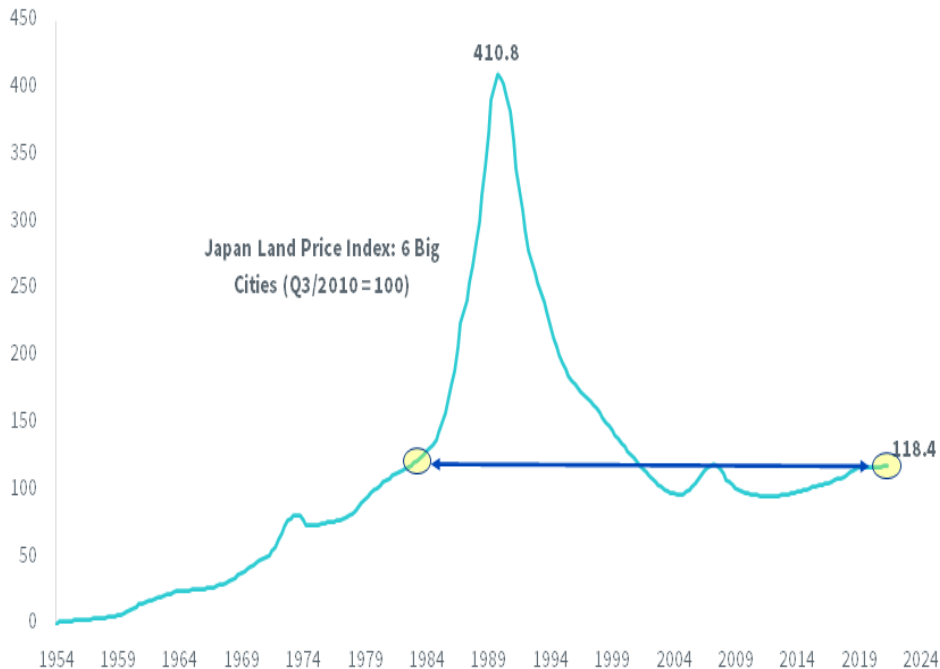
Figure 2: Japanese Yen to Chinese Yuan Exchange Rate



Source: Refinitiv, as of 7/15/22.

Unlike the U.S., which may have to spend the next few years contending with a housing market that appears to be rolling over, Japan's speculative juices found their ugly end over three decades ago (figure 3).

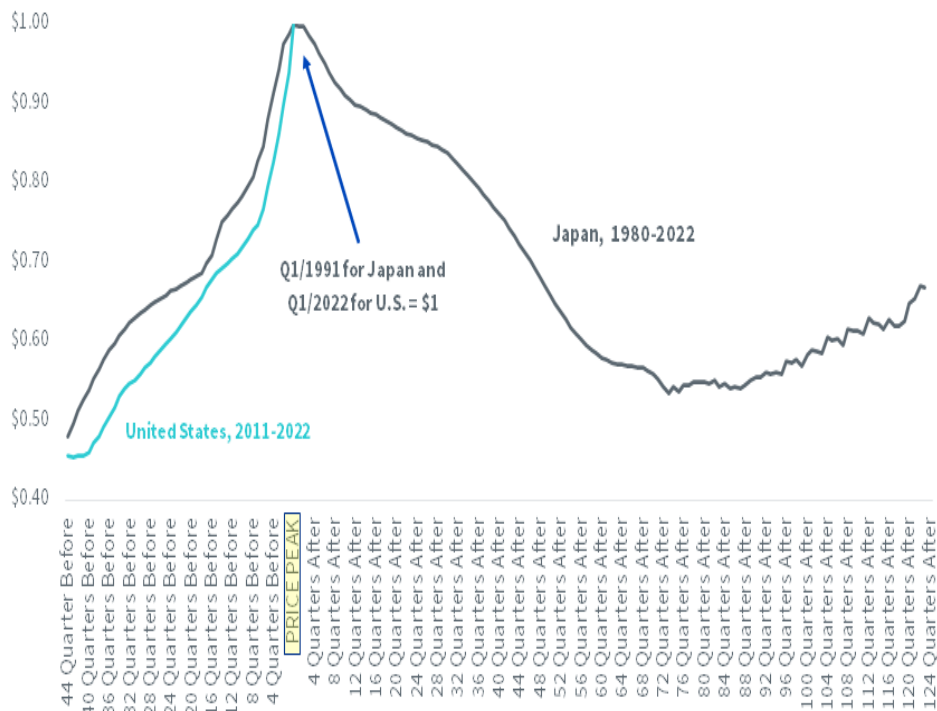
Figure 3: Japan's Land Prices Are at 1983 Levels



Source: Refinitiv, Japan Real Estate Institute, as of Q1/22.

Interestingly, U.S. residential property prices appreciated more in the last 11 years than Japan's did in the final 11 years of its [bull market](#), which were from 1980–1991 (figure 4).

Figure 4: U.S. Residential Property Price Appreciation, 2011–2022, Overlaid on Japan

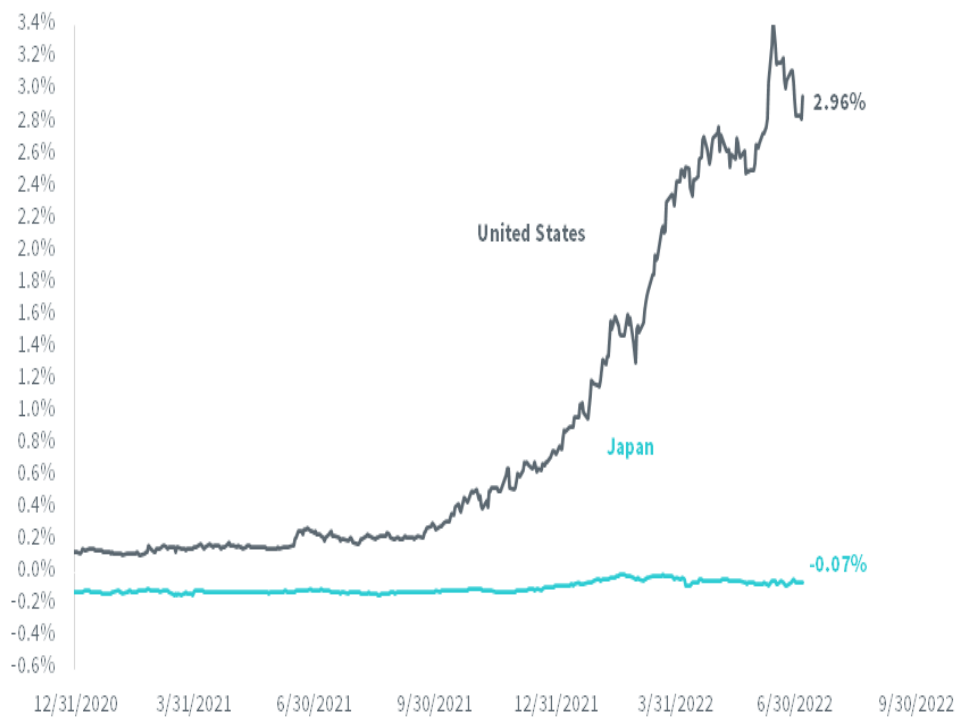


Source: Refinitiv, as of Q1 22.

But because asset prices in the U.S. have melted up, now we have a relative value set-up that favors Japan from a “TINA” framework.

The acronym means “There Is No Alternative” available to investors beyond just biting their tongue and buying up stocks, because you couldn’t—past tense—find any yield in U.S. bonds. Though the TINA arithmetic has faded in the U.S. because of rising rates, Japan’s bond yields refused to follow along, owing to the country’s central bank bond purchases (figure 5).

Figure 5: 2-Year Government Bond Yield



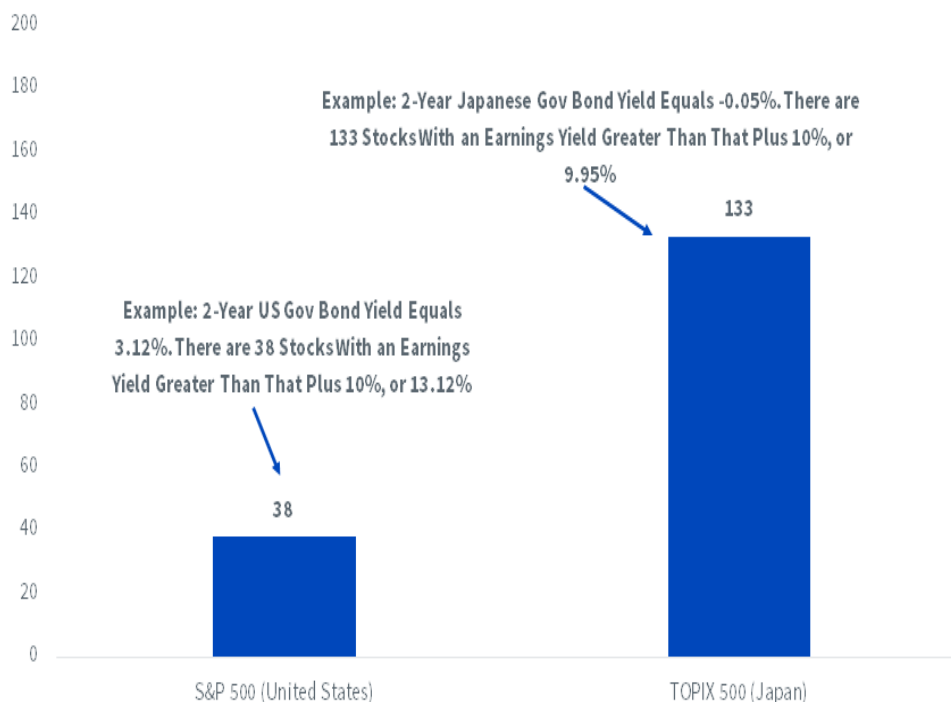
Source: Refinitiv, as of 7/15/22.

Try this exercise: make a list of all S&P 500 stocks that have an earnings yield that is at least 10 percentage points higher than the yield on two-year Treasuries.

There are 38 such companies.

In Japan, if you run the same exercise on the [TOPIX 500](#), the screen comes up with 133 stocks that have earnings yields that are 10 points higher than two-year JGBs (figure 6).

Figure 6: Number of Index Members with Earnings Yields More than 10% Higher than Domestic 2-Year Government Bonds



Source: Refinitiv, as of 6/28/22.

Figure 7 shows another stock-to-bond comparison: the broad market earnings yield gap over 10-year sovereigns. Japan's TOPIX 500 offers a spread of 737 [basis points \(bps\)](#) over near-zero [yielding](#) JGBs, considerably more than the 161 bps spread offered by the S&P 500.

Figure 7: Stock Market Earnings Yield Minus 10-Year Government Bond Yield

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We have two Japan ETFs, one that hedges the yen and one that does not.

If you want to avoid owning the stocks in yen, the one to review is the [WisdomTree Japan Hedged Equity Fund \(DXJ\)](#).

For investors that want Japanese stocks without the currency hedge, consider the [WisdomTree SmallCap Dividend Fund \(DFJ\)](#).

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Consumer Price Index (CPI) : A measure that examines the weighted average of prices of a basket of consumer goods and services, such as transportation, food and medical care. The CPI is calculated by taking price changes for each item in the predetermined basket of goods and averaging them; the goods are weighted according to their importance. Changes in CPI are used to assess price changes associated with the cost of living.

Bullish : a position that benefits when asset prices rise.

TOPIX 500 Index : A capitalization-weighted index designed to measure the performance of the 500 most liquid stocks with the largest market capitalization that are members of the TOPIX.

Basis point : 1/100th of 1 percent.

Yield : The income return on an investment. Refers to the interest or dividends received from a security that is typically expressed annually as a percentage of the market or face value.