



September 23, 2025

## Morning Briefing

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### On Japan's Politics & China's Alibaba

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Check out the accompanying [chart collection](#).

**Executive Summary:** Two recent shockers have unnerved Japanese investors—the resignation of Japan's Prime Minister Ishiba and the tapering of the BOJ's stock market supporting ETF purchases. Bond Vigilantes, fearing that Japan's huge debt will only swell under Ishiba's successor, have driven 20-year government bond yields to a 25-year high, William reports. Neither frontrunner for the PM job is an economic reformer; either would likely continue the same old easy-money policies that have sapped Japan's animal spirits. ... And in a surprising twist, Jack Ma—the Alibaba co-founder who vanished after criticizing the Chinese government—is back and leading the government's charge to dominate global AI markets.

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**Weekly Webcast.** If you missed Monday's live webcast, you can view a replay [here](#).

**Japan I: Political Tremors Spook Markets.** Investors in Japanese government bonds (JGBs) have been reeling over political tremors in Tokyo. Now it's stock investors' turn.

In recent months, the Bond Vigilantes were triggered by the Liberal Democratic Party's (LDP) dismal showing in the [July 20 election](#). That forced the LDP to partner with pro-tax-cut opposition parties to maintain a governing majority. Fears of budget-busting fiscal loosening pushed 20-year yields to the highest [since 1999](#) ([Fig. 1](#)).

Prime Minister Shigeru Ishiba's resignation announcement on [September 7](#) added to bond market jitters. In his 11-plus months as leader, Ishiba pushed back against tax cuts. Now, as LDP officials begin campaigning for the premiership, bond investors are rightly worried that the biggest public [debt burden](#) in the developed world is about to swell ([Fig. 2](#)).

Let's look closer at these investor unnerving politics:

(1) *Frontrunners don't reassure markets.* The two [frontrunners](#) for the top job are Agriculture Minister [Shinjiro Koizumi](#) (44) and former Economic Security Minister [Sanae Takaichi](#) (64), the same rivals Ishiba defeated to become premier on [October 1, 2024](#). Koizumi's victory

would represent a generational shift in the fastest-aging developed nation; a victorious Takaichi would be Japan's first female leader.

Neither has a track record of economic reform, as Japan needs. Either might favor a return to the stimulus-heavy fiscal policies that earned Tokyo the same S&P Global credit rating (A+) as [Bermuda and Iceland](#)—not a higher rating befitting its global status. That could put the political establishment on a collision course with the Bank of Japan (BOJ), which is pursuing a course of quantitative tightening (QT) ([Fig. 3](#) and [Fig. 4](#)).

(2) *BOJ tapering throttles back market support.* One reason the bond market has been on edge is US tariffs, which, back in May and June, wreaked havoc in the US Treasury market. Another: The BOJ slowed the ginormous [JGB purchases](#) it's been making since 2013.

Now, add in stocks, too. Last week, the BOJ shook the equities market by announcing plans to throttle back on purchases of exchange-traded funds (ETFs). Since 2018, its balance sheet—laden with JGBs and ETFs—has topped the size of Japan's [\\$4 trillion economy](#). The BOJ's ETF holdings are worth roughly ¥37 trillion (\$251 billion), with a marked-to-market value around twice that, or [¥75 trillion](#) (\$508 billion).

The markets have taken for granted that the BOJ would remain the investment “[whale](#)” supporting the Nikkei 225 Stock Average, which last week [topped 45,000](#) for the first time ([Fig. 5](#)). Now, as BOJ Governor Kazuo Ueda extends QT efforts in bonds to stocks, too, equity investors are in a whirl. Could the BOJ's withdrawal efforts pull the tatami mat out from under a stock market that last week rose to all-time highs?

Granted, there are valid reasons for investors' bullishness on Japanese equities. [Beginning in 2014](#), under then-Prime Minister Shinzo Abe, Tokyo tweaked corporate governance standards to increase returns on equity. So-called “Abenomics” prodded companies to add more outside directors, unwind cross-shareholdings with friendly companies, and give shareholders a louder voice.

Yet pledges to shake up Japan's underlying economy and increase competitiveness have proceeded glacially. Even as Nikkei bulls worried that the market had gotten ahead of its skis, though, the BOJ's epic purchases kept the overall market aloft. Until now, perhaps.

**Japan II: Fiscal Worries Abound.** Ueda spent the [last 30 months](#) working to normalize a Japanese rate spectrum that's been at zero [since 1999](#). So far, the BOJ has hiked short-term rates to a [17-year high](#) of 0.5% ([Fig. 6](#)). It also has swapped quantitative easing (QE)

for QT, including ETFs at this point.

This tapering effort could become political in a hurry. Rising debt yields could complicate the next prime minister's ability to placate opposition parties with tax cuts. Withdrawing from stocks, meanwhile, could send the market sharply lower, resulting in a negative wealth effect.

Here's some background perspective:

(1) *Stagflation worries*. Japanese households aren't feeling good about the economy. With a [2.7% y/y core CPI inflation rate](#) outpacing wage gains and Asia's No. 2 economy expected to grow just [0.7% y/y](#) this year, stagnation worries abound ([Fig. 7](#) and [Fig. 8](#)). So Japan's next leader won't enjoy much of a honeymoon period.

(2) *Abenomics redux?* Many political wonks think Koizumi, the scion of a political dynasty, is Ishiba's most likely successor. His economic philosophy/priorities are an open question, but most observers assume he'll maintain the easy-money priorities of the last decade-plus.

Takaichi is [staunchly against](#) interest rate hikes and explicitly for doubling down on Abenomics, with its weak yen policies and fiscal profligacy. Many economists agree that 26 years of zero rates and 24 years of QE deadened Japan's [annual spirits](#). It took the onus off a revolving door of governments to level playing fields, reduce bureaucracy, incentivize innovation, and empower women. Corporate CEOs had fewer incentives to innovate, restructure, and take risks.

More of the same will do little to help Japan keep pace with a burgeoning China.

(3) *The China threat*. For all China's challenges with a property crisis and deflation, President Xi Jinping's government is [investing big](#) in dominating sectors, including electric vehicles (EVs), renewable energy, artificial intelligence (AI), semiconductors, robotics, biotechnology, and myriad others.

Two-plus decades of papering over Tokyo's failure to recalibrate growth engines is catching up with the LDP. The current two-person race between premier candidates likely to pursue the same-old-same-old policy mix has the Bond Vigilantes worried.

Other wildcard lawmakers who some observers think have a distant shot at winning the premiership likewise would represent continuity—and Japan arguably has had too much

continuity. These include: Chief Cabinet Secretary [Yoshimasa Hayashi](#); former Minister for Economic Security Takayuki Kobayashi; and former LDP Secretary-General Toshimitsu Motegi.

(4) *Cost of continuity*. The LDP has led Japan with only two brief interruptions since 1955. And even when its prime ministers were deemed reformist—including Koizumi’s father [Junichiro Koizumi](#) (2001-06) and [Shinzo Abe](#) (2012-20)—they prioritized stimulus over supply-side upgrades to raise Japan’s innovation game.

For all China’s troubles, it’s had big, splashy corporate successes like EV phenomenon BYD and the AI game-changer DeepSeek, while Japan’s policy mix is geared toward supporting legacy giants like Toyota, Panasonic, and Nippon Steel.

It’s wise for the BOJ to reduce its dominance over stocks. The question is whether investors agree. And whether the next government will take steps that further damage the BOJ’s credibility and Tokyo’s debt troubles.

**China Tech I: Alibaba Aims To Lead Xi Jinping’s AI Charge.** After roughly five years in the wilderness, Alibaba Group billionaire Jack Ma is back in action to help lead China’s campaign to own the global AI game.

Ma’s return is arguably the biggest corporate news out of China since the last time the e-commerce behemoth he co-founded was in the global headlines for all the wrong reasons. In [October 2020](#), President Xi Jinping launched a great leap backwards with his draconian crackdown on China’s tech billionaires and their internet platforms.

It started with a no-holds-barred speech Ma gave in Shanghai on October 24, 2020. Ma argued that Xi’s regulators are clueless about innovation, complaining that “we cannot manage the future with outdated approaches.” He accused China’s banks of operating with a “[pawn shop](#)” mentality that limits the nation’s potential.

The response from Communist Party bigwigs was immediate and harsh. The \$37 billion initial public offering of Ma’s fintech spinoff Ant Group, which was planned weeks later, was cancelled, while Ma effectively was “[disappeared](#).”

Let’s explore what Jack Ma’s return to Alibaba means for China’s AI dreams:

(1) *Face of Chinese tech*. Ma, 61, is now in the headlines for the right reasons. The fact that

he's being feted in Beijing—and sighted in Hangzhou, where [Alibaba is headquartered](#)—is a huge deal, especially with Ma pledging to help Xi morph China into the global leader of all things AI.

Earlier this year, China's DeepSeek fired a shot across the West's bow. The startup's open-source AI model using less-advanced chips had shares in [America's Nvidia](#) and [Dutch giant ASML](#) reeling. And it got Silicon Valley's undivided attention.

(2) *Scaling up Xi's ambitions.* Now here comes Ma, China's most globally celebrated tech success story, scaling up Xi's ambitions to put China at the forefront of AI. In late August, China's answer to Amazon reported yet another [AI-driven surge](#). Alibaba said AI-related revenue “maintained triple-digit year-over-year growth for the eighth consecutive quarter.”

Alibaba is investing aggressively in AI infrastructure, while offering an ever-expanding array of services involving its cloud computing business. The unit is key to Alibaba's ability to monetize AI. Thanks in part to a booming cloud computing business—up 26% y/y in the quarter ending June—Alibaba posted Q2 revenue of [nearly \\$35 billion](#), a 2% y/y rise. Net income jumped an annualized 78%.

(3) *'Made in China 2025' paying off.* Between the DeepSeek shock in January and Alibaba's ambitions, the “Made in China 2025” initiative, launched by Xi in 2015, is scoring its biggest public-relations wins to date. AI optimism is largely behind the [45% surge](#) in the CSI 300 index over the last 12 months ([Fig. 8](#)).

**China Tech II: Xi's Contradictory AI Policies.** Xi's vision could also be Alibaba's Achilles' heel. The most immediate risk is how Alibaba effectively [declared war](#) on e-commerce rivals JD.com and Meituan. Though Alibaba is technically run by trusted Ma allies [Joseph Tsai](#) and [Eddie Wu](#), Ma reportedly was a key force behind aiming \$7 billion in subsidies at countering JD alone. Such moves, however, could put Alibaba on a collision course with Xi's efforts to stop [aggressive price competition](#).

Ma's stumble is also a stark reminder that there's still a more powerful force than the latest wave of financial innovation: the state. Ma is the mainland version of an oligarch who thrives at the pleasure of Xi's party, which carefully chooses its monopolies. Any founder who gets too big for its britches, expands too quickly globally, or tests Beijing's tolerance levels risks being “Jack Ma-ed,” including the man himself.

Here's more:

(1) *Beijing's control-freak ways.* A hallmark of the Xi era that began in 2012 is ever-increasing state control. Xi pledged to allow market forces to play a “decisive” role in economic decision-making. But the state sector continues to dominate; vital supply-side reforms remain on the drawing board; media freedom is moving backwards; and, thanks to Xi's tech crackdown, Wall Street still worries that China is “uninvestable.”

The very nature of AI presents Team Xi with a bull market in wildcards. As Beijing endeavors to translate wins like DeepSeek into wider gains for the \$18 trillion economy, it may find US innovators less of a threat than Beijing.

(2) *Tipping the global balance.* China views AI as a tool that could tip the balance of global power in its favor—much as the US overtook the UK's industrial dominance by perfecting electricity, motor vehicles, and game-changing machinery.

Xi's inner circle seems to think it can create strong guardrails to ensure AI is compatible with state control, much as it turned the internet and social media into surveillance tools to tighten authoritarian control. For party bigwigs, commandeering AI technology to promote ideological bias and censorship will be a feature, not a bug.

(3) *Overinvestment in AI, too?* But tech disruption tends to come more from the ground up than from the top down.

Duplicating DeepSeek's success will require massive investment to keep up with the physical infrastructure arms race—not to mention surging energy costs. It hardly helps that the US is limiting China's access to cutting-edge chips and related equipment. And China's track record of overinvestment and overcapacity, mixed success picking winners and losers, and privatizing top-down decision-making is bound to undermine its AI ambitions.

Global investors do have alternatives, no matter how much potential China boasts in the AI realm. AI leaders, it follows, are always just one sharp-tongued critique of Xi's governing style away from “getting Jack Ma-ed” too.

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## Calendars

**US: Tues:** S&P Global C-PMI, M-PMI & NM-PMI 54.6, 51.8 & 53.8; Richmond Fed Manufacturing Index -9; Powell; Bostic; Bowman. **Wed:** MBA Mortgage Applications; New Home Sales 650,000; Daly. (Source: FX Street)

**Global: Tues:** Eurozone S&P Global C-PMI, M-PMI & NM-PMI 51.1, 50.7 & 50.6; Germany S&P Global C-PMI, M-PMI & NM-PMI 50.5, 50.0 & 49.5; France S&P Global M-PMI & NM-PMI 50.2 & 48.9; UK M-PMI & NM-PMI 47.2 & 53.6; UK CBI Industrial Trends Orders -30; Japan M-PMI 50.2; Mauderer. **Wed:** Germany Ifo Business Climate Index Headline, Current Assessment & Expectations 89.2, 86.5 & 92.0; Japan Jibun Bank M-PMI 50.2. (Source: FX Street)

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## Strategy Indicators

**S&P 500/400/600 Forward Earnings ([link](#)):** During the September 19 week, forward earnings rose simultaneously for all three indexes for the 15th time in 17 weeks. LargeCap's forward earnings rose for an 18th straight week, its longest winning streak since it did so for 38 weeks through the September 13, 2024 week. MidCap's has dropped in just two of the 18 weeks since it bottomed during the May 16 week. SmallCap's has risen for 17 straight weeks since it bottomed during the May 23 week, its longest winning streak since it did so just over four years ago for 25 weeks through the August 27, 2021 week. LargeCap's forward earnings rose 0.3% w/w to its 16th straight weekly record high. MidCap's gained 0.4% w/w to its third straight weekly record high, after last hitting that mark five months earlier during the April 4 week. SmallCap's rose 0.3% w/w to a 22-month high and is 9.4% below its June 2022 record. LargeCap's forward earnings has soared 30.5% from its 54-week low during the week of February 1, 2023; MidCap's is 10.7% above its 55-week low during the week of March 10, 2023; but SmallCap's has lagged considerably and is up just 6.1% from a very recent 42-month low during the May 23 week. These three indexes' forward earnings downtrends from mid-2022 to early 2023 and again during Trump's Tariff Turmoil were relatively modest compared to their deep double-digit percentage declines during the Great Virus Crisis and the Great Financial Crisis. Here are the latest consensus earnings growth rates for 2024, 2025, and 2026: LargeCap (9.7%, 10.4%, 13.8%), MidCap (0.4, 2.2, 17.6), and SmallCap (-10.2, 3.5, 18.2).

**S&P 500/400/600 Valuation ([link](#)):** Valuations were mostly higher for these three indexes during the September 19 week. LargeCap's forward P/E rose 0.2pt w/w to 22.6, reaching its highest level since the January 8, 2021 week when forward earnings was still recovering from the Covid-19 shutdown. It's now 5.6pts above the seven-month low of 17.0 during the October 27, 2023 week. That compares to a 30-month low of 15.1 at the end of September 2022 and an 11-year low of 11.1 during March 2020. MidCap's forward P/E was steady w/w at 16.2, down from a 32-week high of 16.4 the week before that. It's now 0.9pts below its



40-month high of 17.1 during the November 29 week and 4.0pts above the 12-month low of 12.2 in October 2023. That compares to a record high of 22.9 in June 2020 when forward earnings was depressed and an 11-year low of 10.7 in March 2020. SmallCap's forward P/E rose 0.1pt w/w to an eight-month high of 15.7. It's 2.8pts above its 17-month low of 12.9 during the April 4 week and 5.1pts above its 14-year low of 10.6 in September 2022, but remains 1.4pts below its 41-month high of 17.1 during the November 29 week. That compares to a record high of 26.7 in early June 2020 when forward earnings was depressed, and a record low of 10.2 in November 2009 during the Great Financial Crisis. The forward P/Es for the SMidCaps have been mostly below LargeCap's since August 2018. MidCap's P/E is at a 28% discount to LargeCap's P/E, up from a 26-year low 29% discount during the April 10 week, which matched its similar 29% discount during the July 5, 2024 week. That compares to a 19% discount during the March 2, 2023 week, which matched its best reading since October 14, 2021. SmallCap's P/E is at a 29% discount the LargeCap's P/E, up from a 13-month-low 33% discount during the August 7 week. That compares to a 23% discount during the November 29 week, which was its best reading since the March 2, 2023 week. It's now just 5ppts above its 24-year-low 34% discount during the July 5, 2024 week. SmallCap's P/E is at a 3% discount to MidCap's, up from a 13-month low 6% discount at the end of July and a 20-year-low 10% discount in late 2021. Prior to that, from 2003 to 2018, SmallCap's P/E had been mostly above MidCap's, and both were above LargeCap's.

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