

The Japan Update

23 January 2015

Will Japan and U.S. Stocks Benefit from Market Anomalies in 2015?

Through the careful examination of historical data, it is possible to empirically affirm the existence of several anomalies in the stock market, even though there is not always a clear theory or explanation as to why they exist. One such anomaly that is relevant for the current year is the tendency for Japanese and U.S. stock markets to perform strongly in years for which the final digit is the number five (e.g. 2005, 1995, 1985).

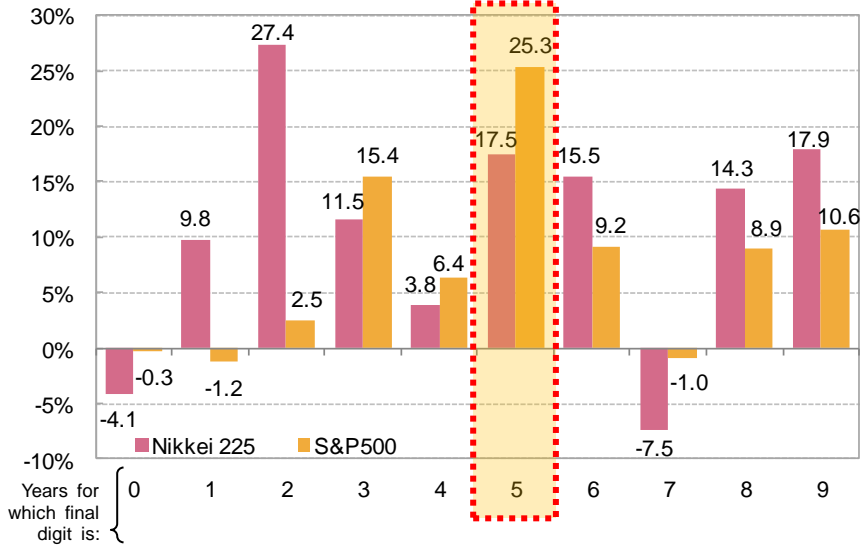
People have attempted to explain this anomaly in several different ways, saying that it may be related to economic and capital investment cycles. However, regardless of how it can be explained, we can confirm that average annual performance of Japanese and U.S. stock markets in the “5” years is relatively strong - 17.5% for Japan and 25.3% for the U.S. – compared to years for which the final digit is something other than five (see chart on below left). Furthermore, if we take a look at the years where overall stock market performance was positive and the years where it was negative, for both Japan and the U.S., the “5” years are the only ones in which there were no years with negative performance (see table on below right). In addition, looking specifically at the U.S., there is another anomaly where stocks perform strongly in years preceding those in which presidential elections are held (which may be explained by heightened expectations for new government policies). Looking at data for each year that preceded presidential election years starting from 1951, 15 out of 16 such years saw positive performance of U.S. stocks, with only one recording negative performance. The next pre-presidential election year is the current year, 2015. So if this anomaly continues, this year could be a good one for U.S. stock prices. If we also take into account that it is often the case that Japanese stocks finish higher in years where U.S. stocks also finish higher, we may be able to look forward to a stronger stock market in Japan this year as well.

The stock market is currently seeing a great deal of volatility due to the drop in crude oil prices and increasing concerns of a Greek euro exit. While investors will need to be on guard for these kinds of risks, in light of projections of record-high earnings per share in both the Japanese and U.S. stock markets in 2015 and still fairly low P/E multiples (e.g. approx. 13x for the Japanese market based on 12-month consensus EPS), in addition to the possibility that stocks in both countries could benefit from the anomaly of 2015 being a “5” year, the Japan and U.S. equity markets will be a strong point of investor focus in the coming year.



Strong Performance of U.S. & Japan Stocks in Years Where Final Digit Is 5

Average Annual Performance (%)



Zero Years of Negative Performance in Years Where Final Digit is 5

No. of Years of Positive/Negative Performance in Years with the Same Final Digit

Years for which final digit is:	Nikkei 225		S&P500	
	Pos.	Neg.	Pos.	Neg.
0	2	5	4	5
1	4	3	4	5
2	4	3	6	3
3	5	2	7	2
4	4	3	6	3
5	6	0	8	0
6	5	1	6	2
7*	1	5	4	3
8	4	2	6	2
9	6	1	6	2

*For one of the years where the final digit is seven (1947), performance for the S&P 500 was flat (neither positive nor negative).

Sources: Nikkei, Inc., S&P Dow Jones Indices LLC, Nikko Asset Management, as of January 2015

Annual data for the Nikkei 225 covers the period from 1949 to 2014 (however, data for 1949 only includes the period covering May 16 to the end of the year). Annual data for the S&P 500 covers the period from 1930 to 2014.

The graphs above are based on past data and are not necessarily indicative of future performance.

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