



Outlook for Japanese Stock Market & Economy

Sumitomo Mitsui DS Asset Management

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-August 2024-

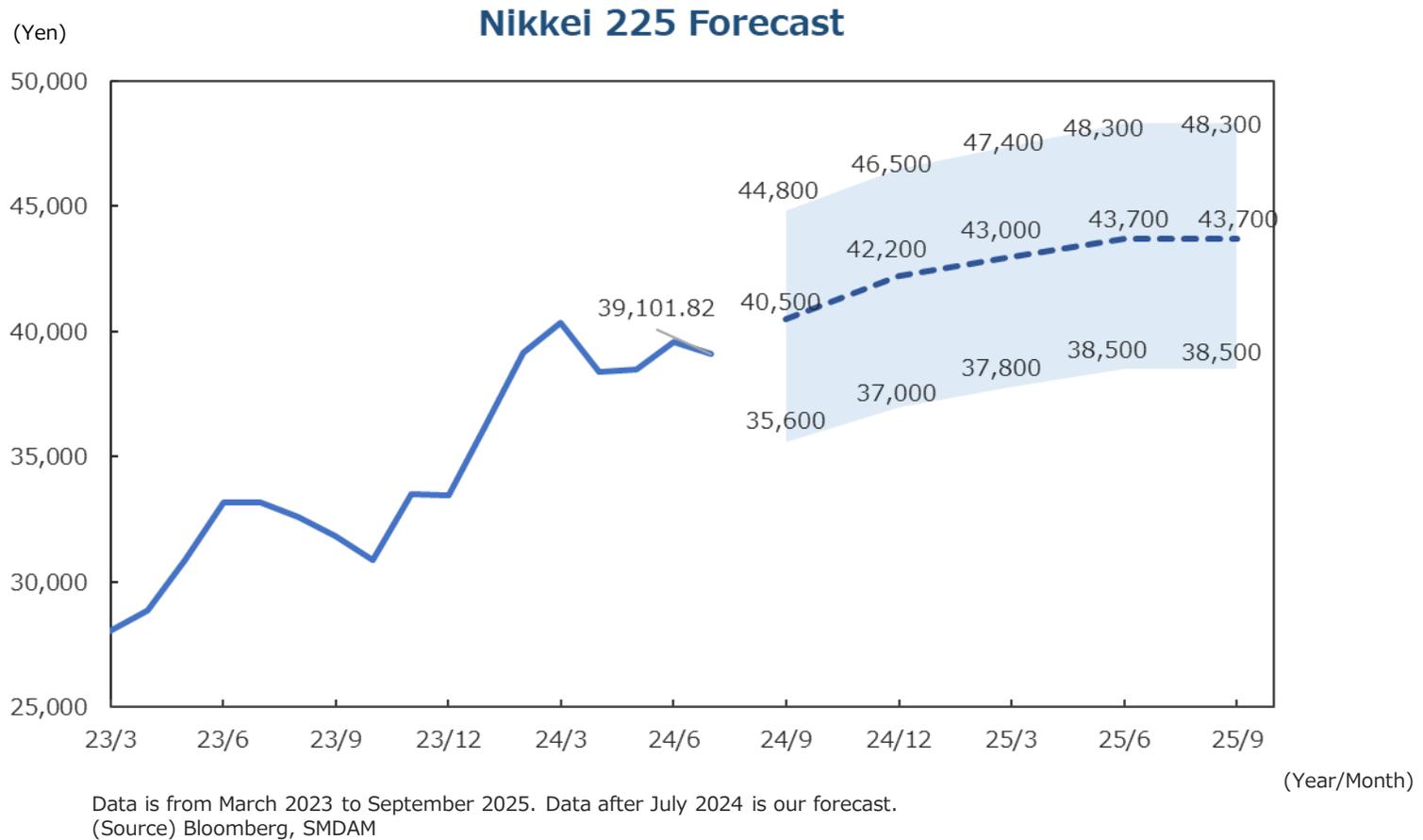


Outlook for Japanese Stock Market

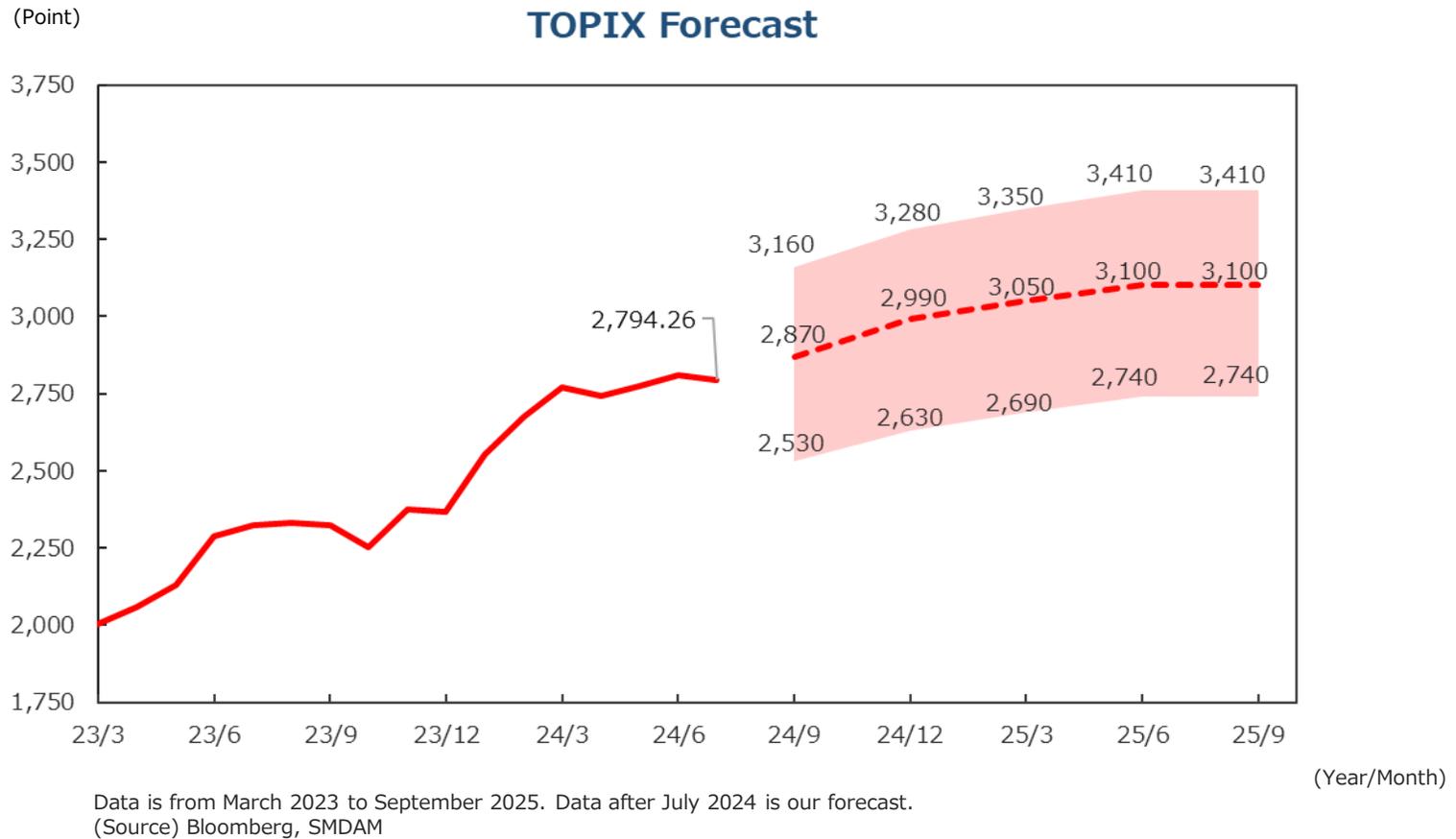
Market Outlook

- We maintain our bullish perspective on the Japanese equity market due to strong corporate earnings and recovery in consumer spending.
- We expect EPS could be boosted by nominal GDP growth and the recovery of the business cycle/momentum of manufacturers' going forward.
- In the short term, the market could face increasing volatility caused by uncertainty over the global economy and monetary policy.
- Our price target for FY 2024 of the Nikkei 225 is at 43,000 and that for TOPIX is at 3,050.
- We expect the wage increase this year and the policy changes by the new administration and the new leadership after the LDP presidential election in autumn.

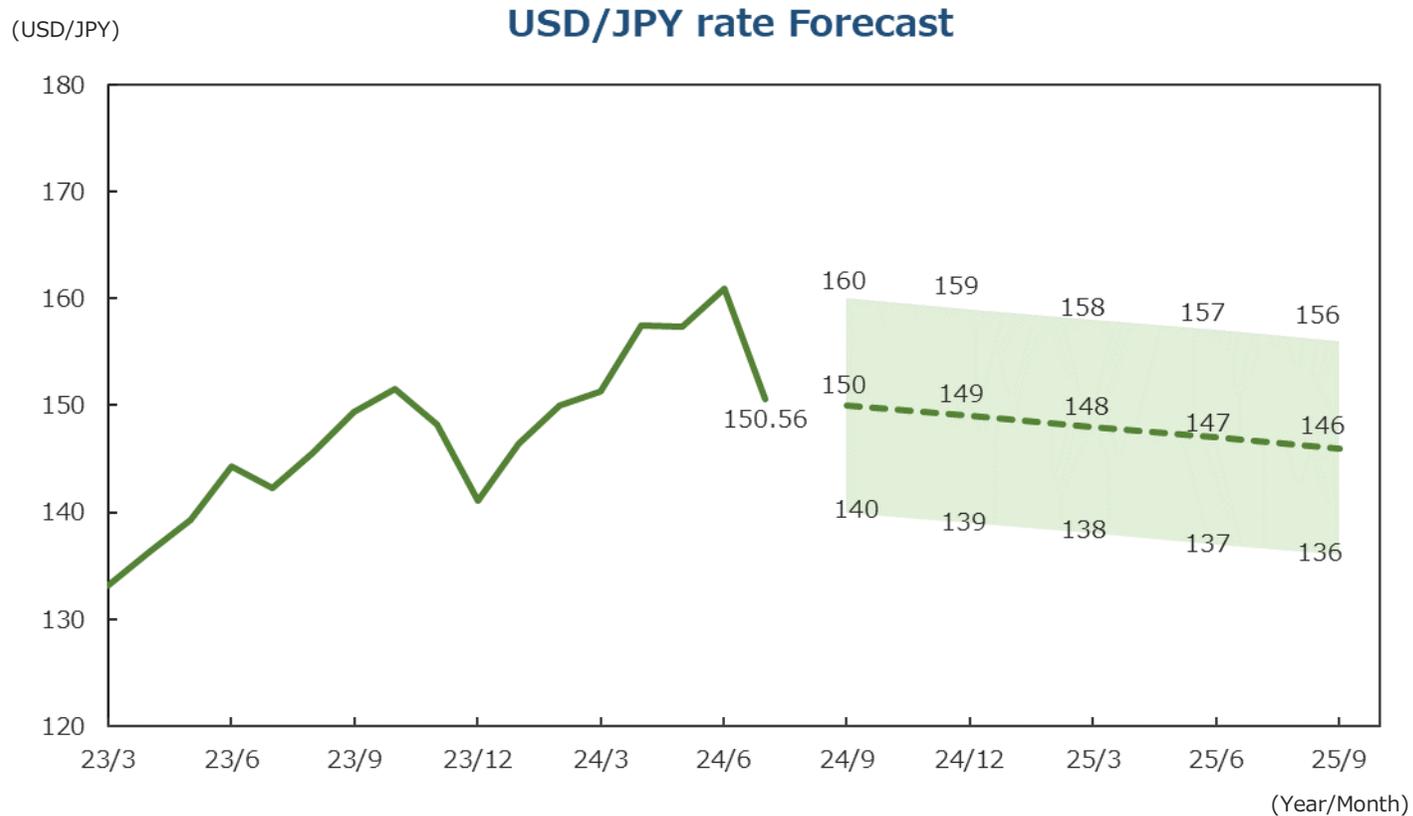
We expect a bullish market to continue going forward



We expect a bullish stock market to continue going forward



Monetary policy pivot weighs on USD/JPY rate ahead



Data is from March 2023 to September 2025. Data after July 2024 is our forecast.
(Source) Bloomberg, SMDAM

Upside / Downside risk scenarios

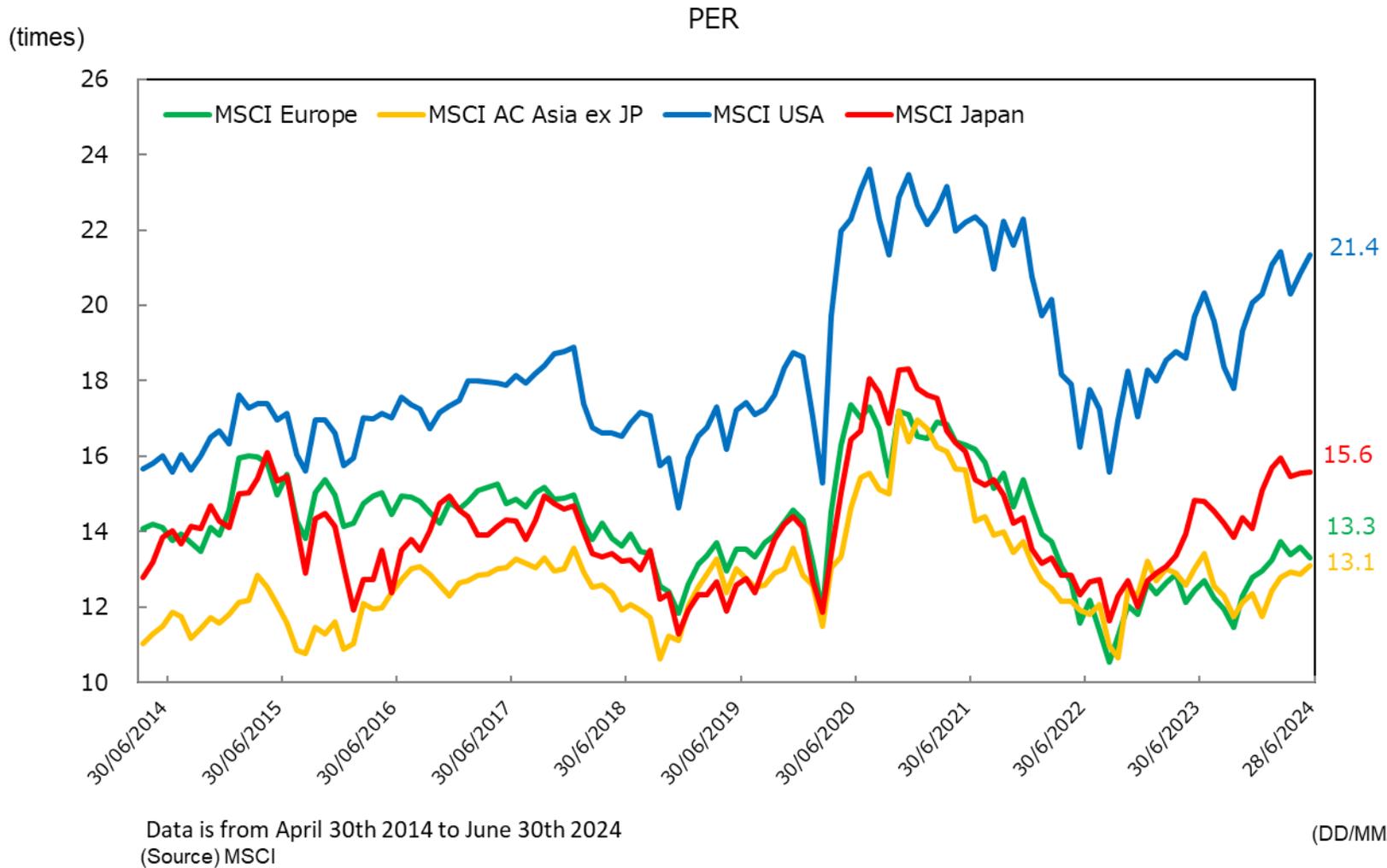
■ Upside Risks

- Growing optimism over virtuous cycle of wage increases and mild inflation
- Further improvement of corporate governance, led by Tokyo Stock Exchange

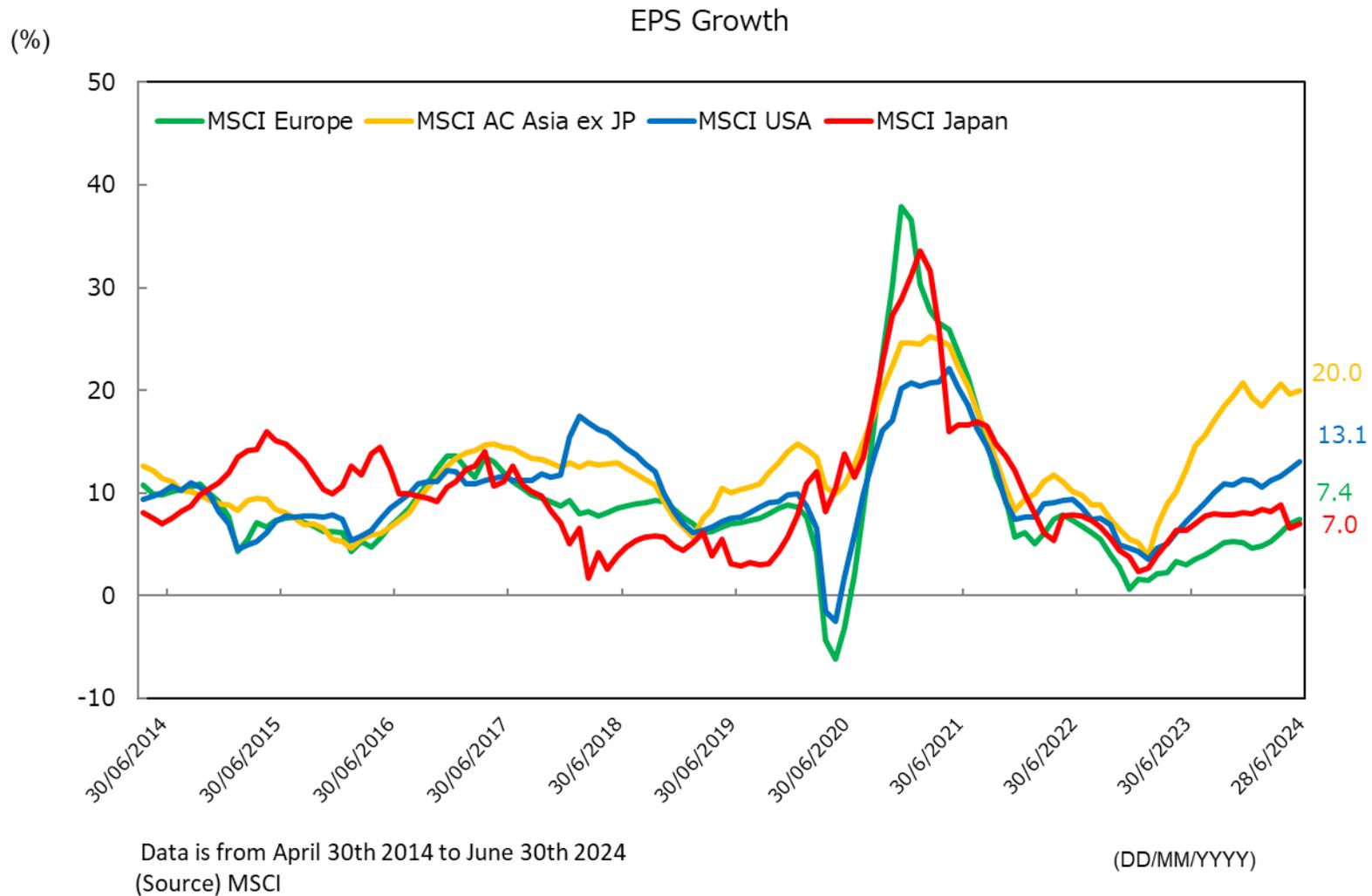
■ Downside Risks

- Tighter fiscal policy to achieve a “Surplus of Primary Balance”
- Excessive and rapid JPY appreciation
- Hasty monetary tightening by the BOJ

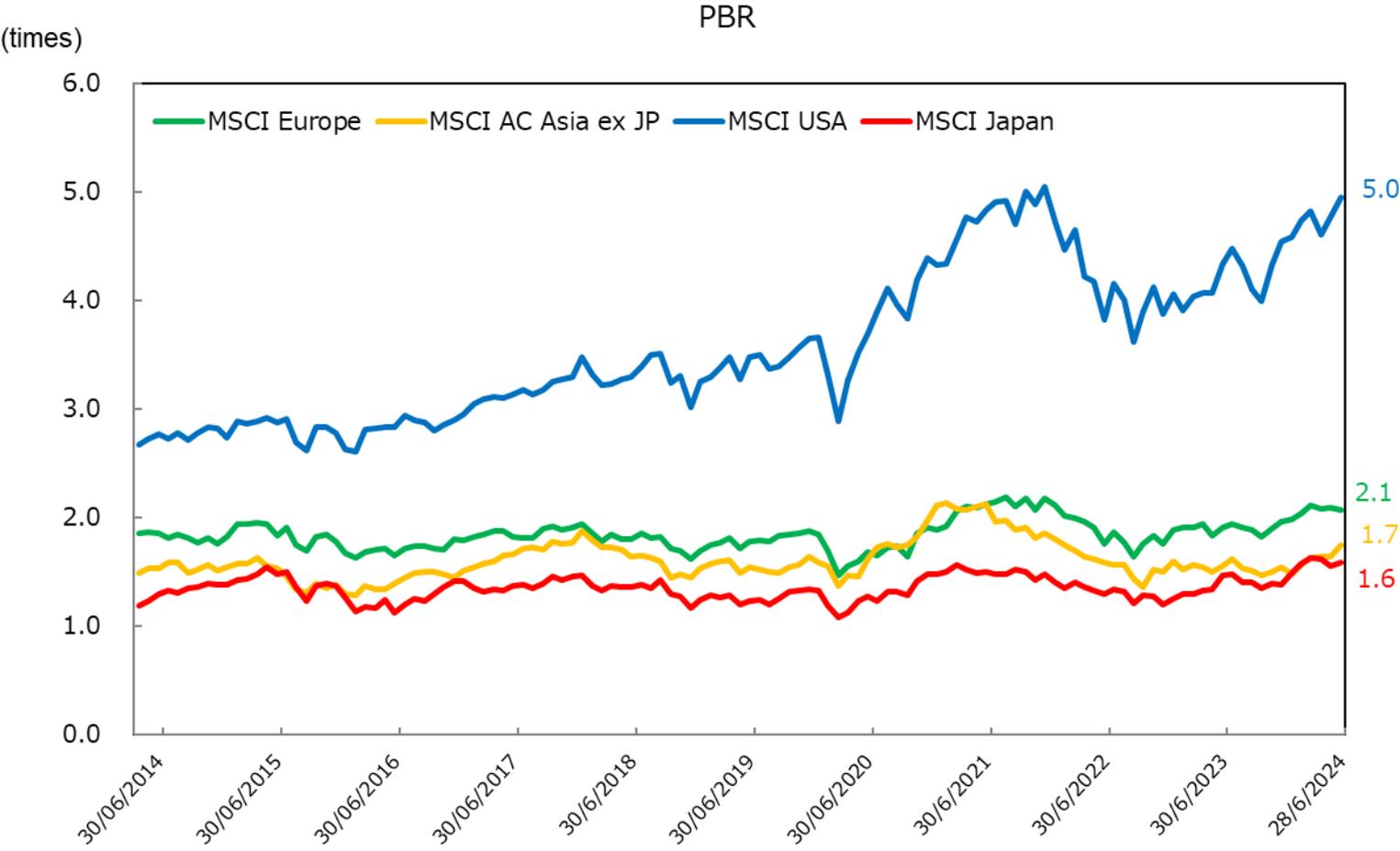
Recent market rally lifts Japan's P/E ratio



Japan's EPS growth slowing and lagging behind peers



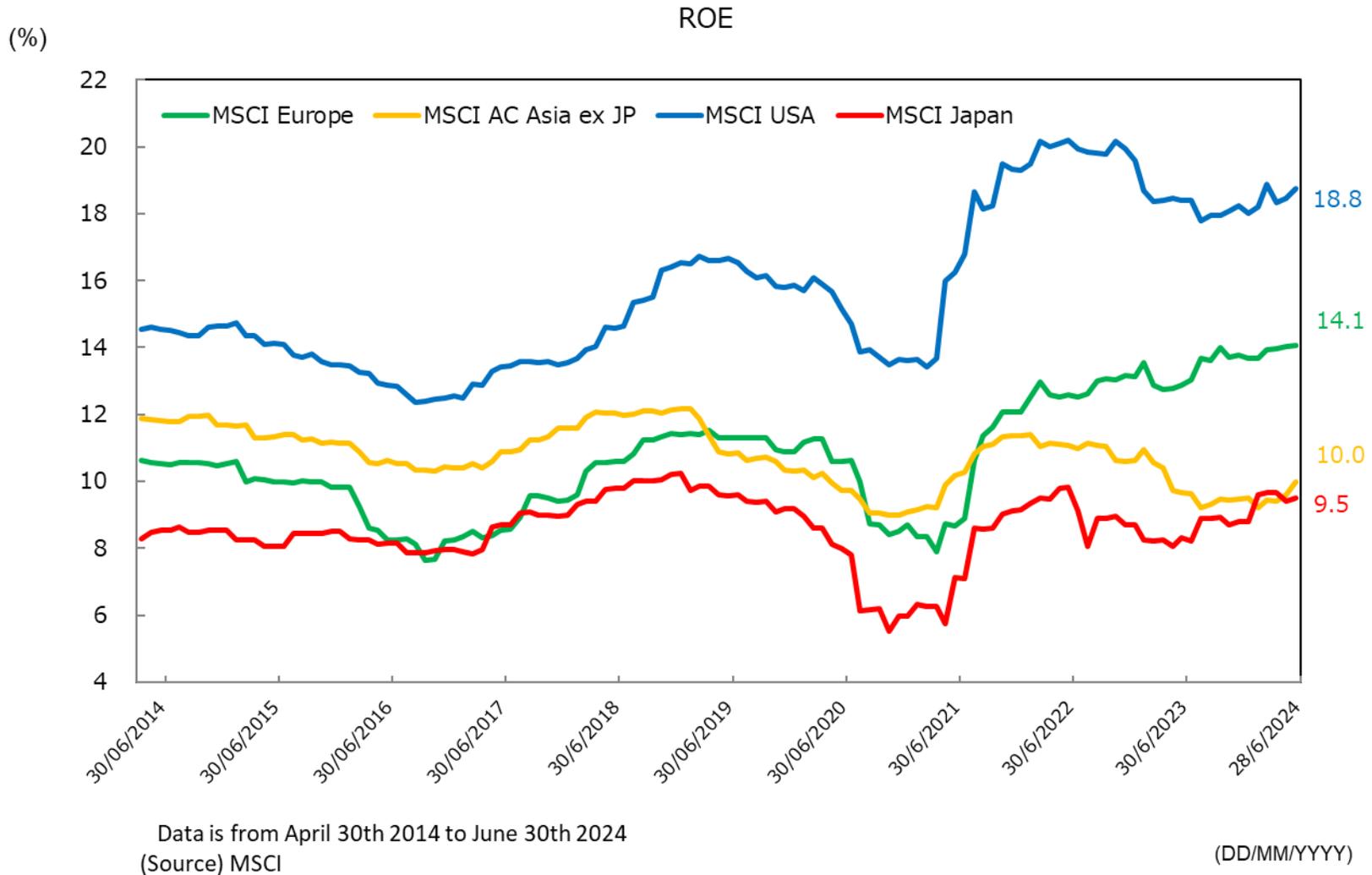
Japan's P/B ratio has room for further improvement



Data is from April 30th 2014 to June 30th 2024
(Source) MSCI

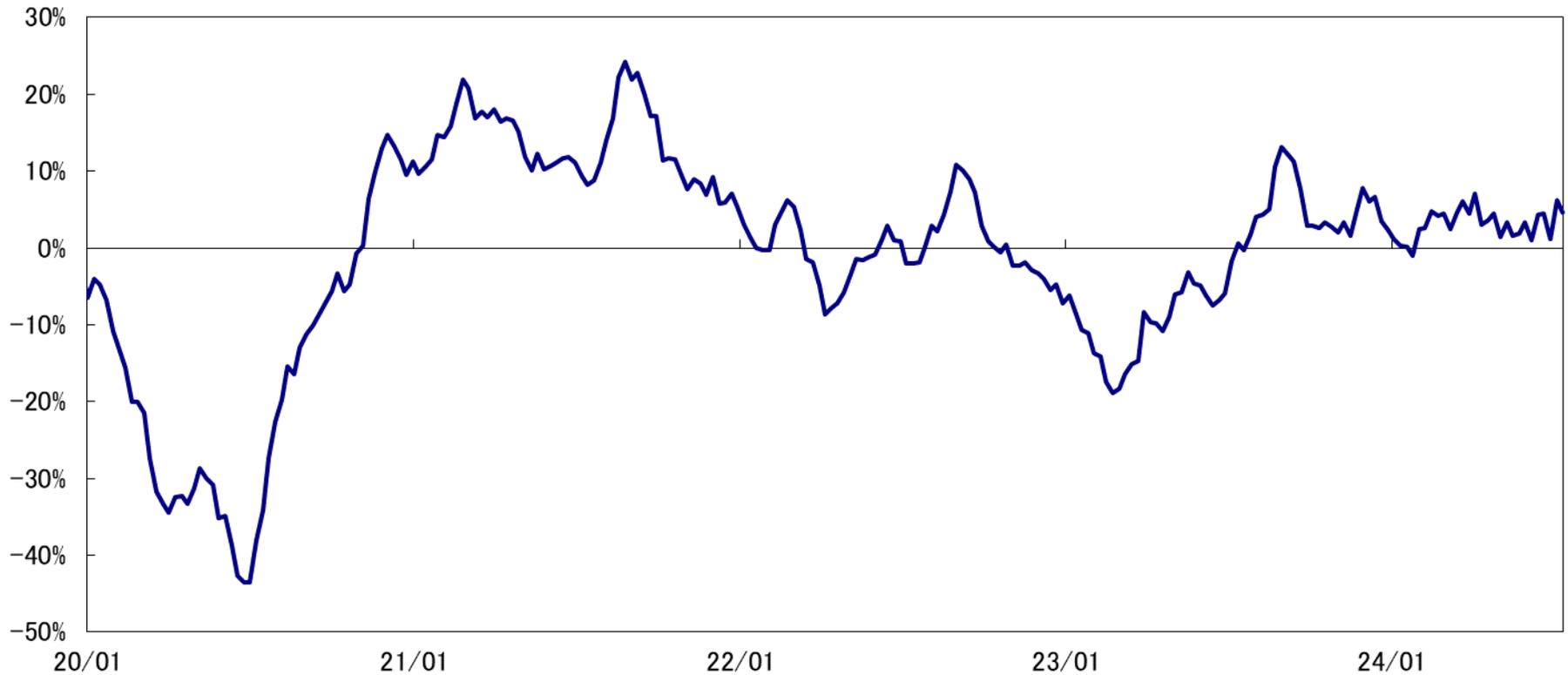
(DD/MM/YYYY)

Earnings growth lifts Japan's ROE



EPS revision remains positive despite lackluster economic figures

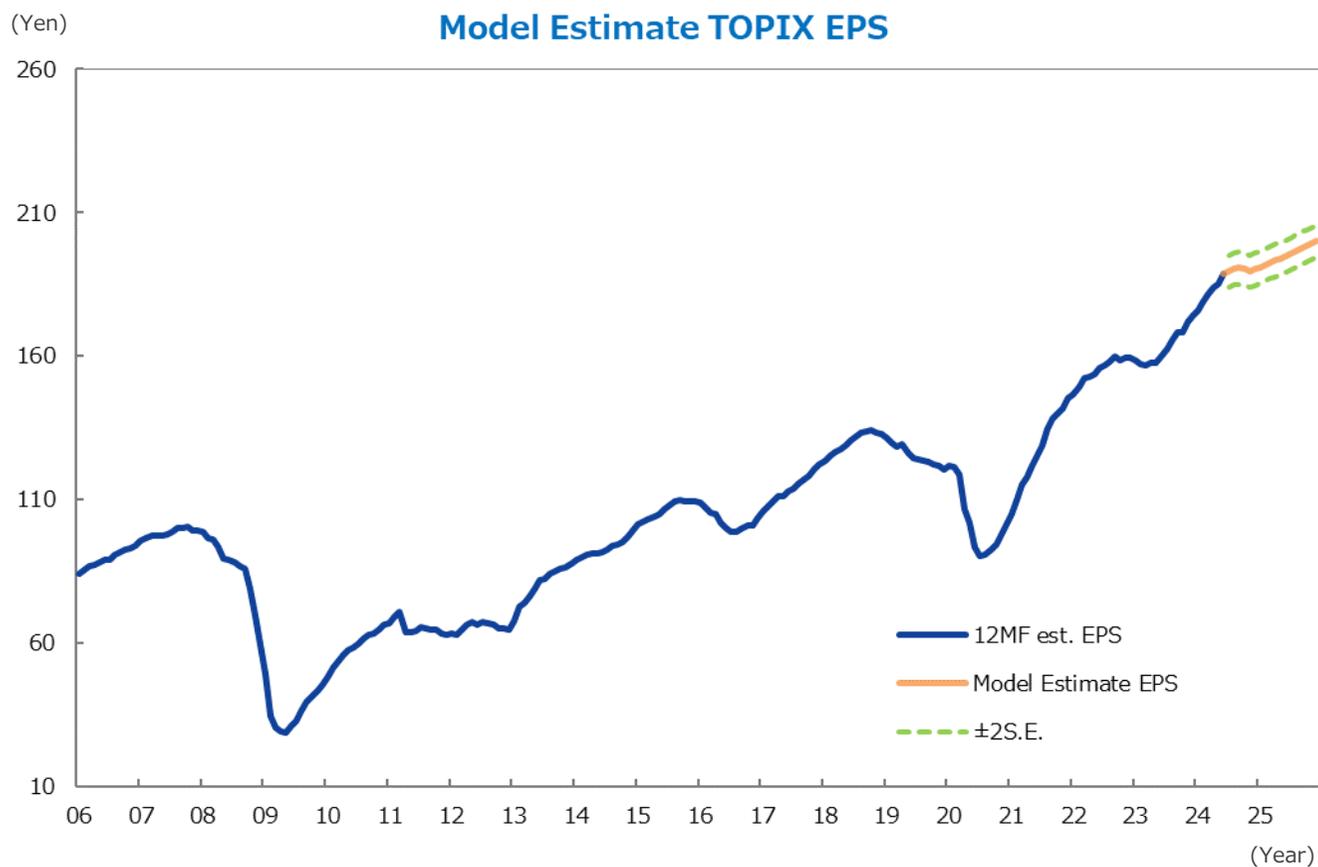
TOPIX Revision Index



Data is from January 2nd 2020 to July 11th 2024
(Source) Datastream, IBES

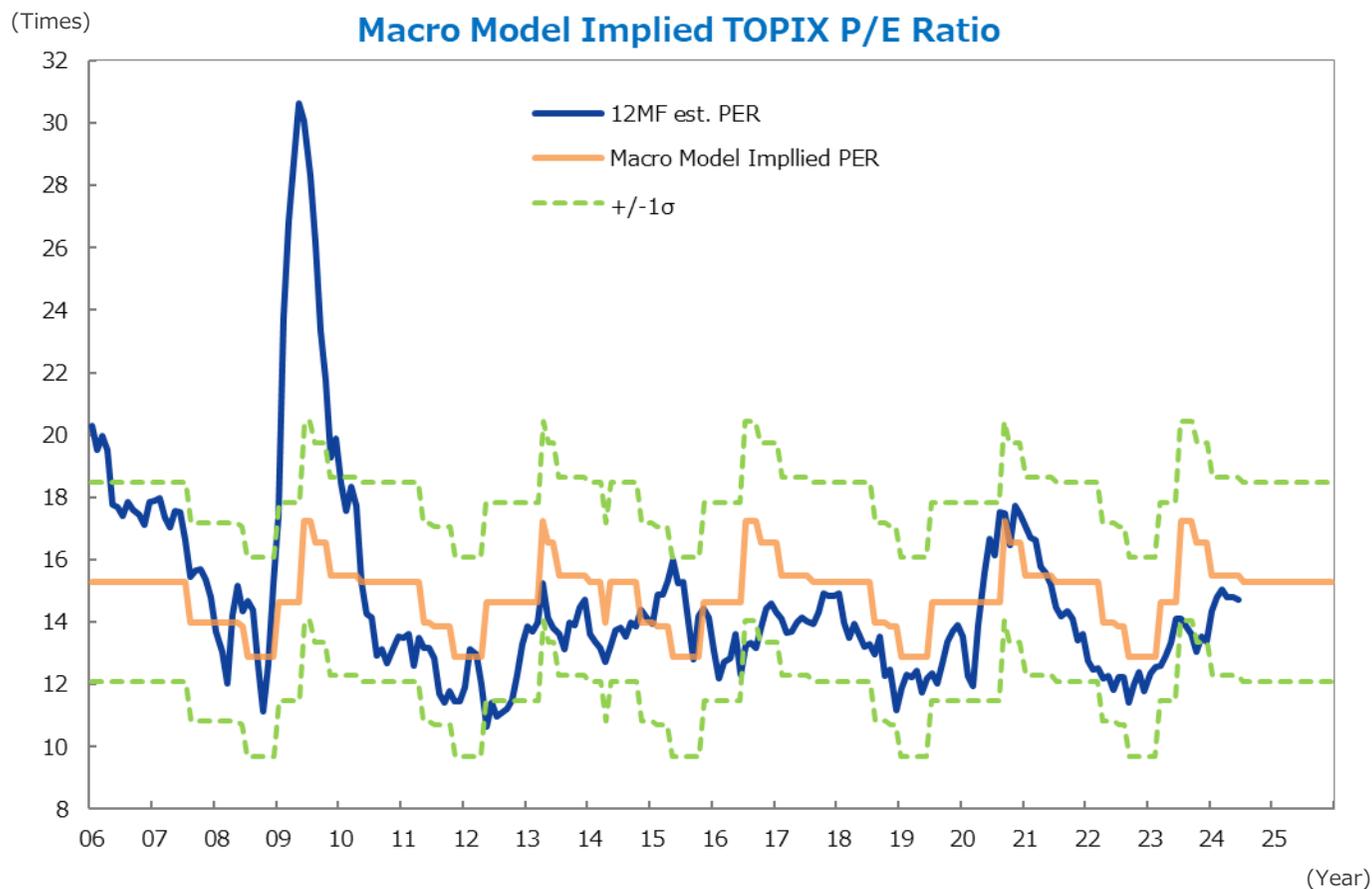
(YY/MM)

Growth of estimate EPS might slow in the near future



Note: Consensus data is from January 2006 to June 2024. Model estimate Data is from July 2024 to December 2025.
Source: SMDAM

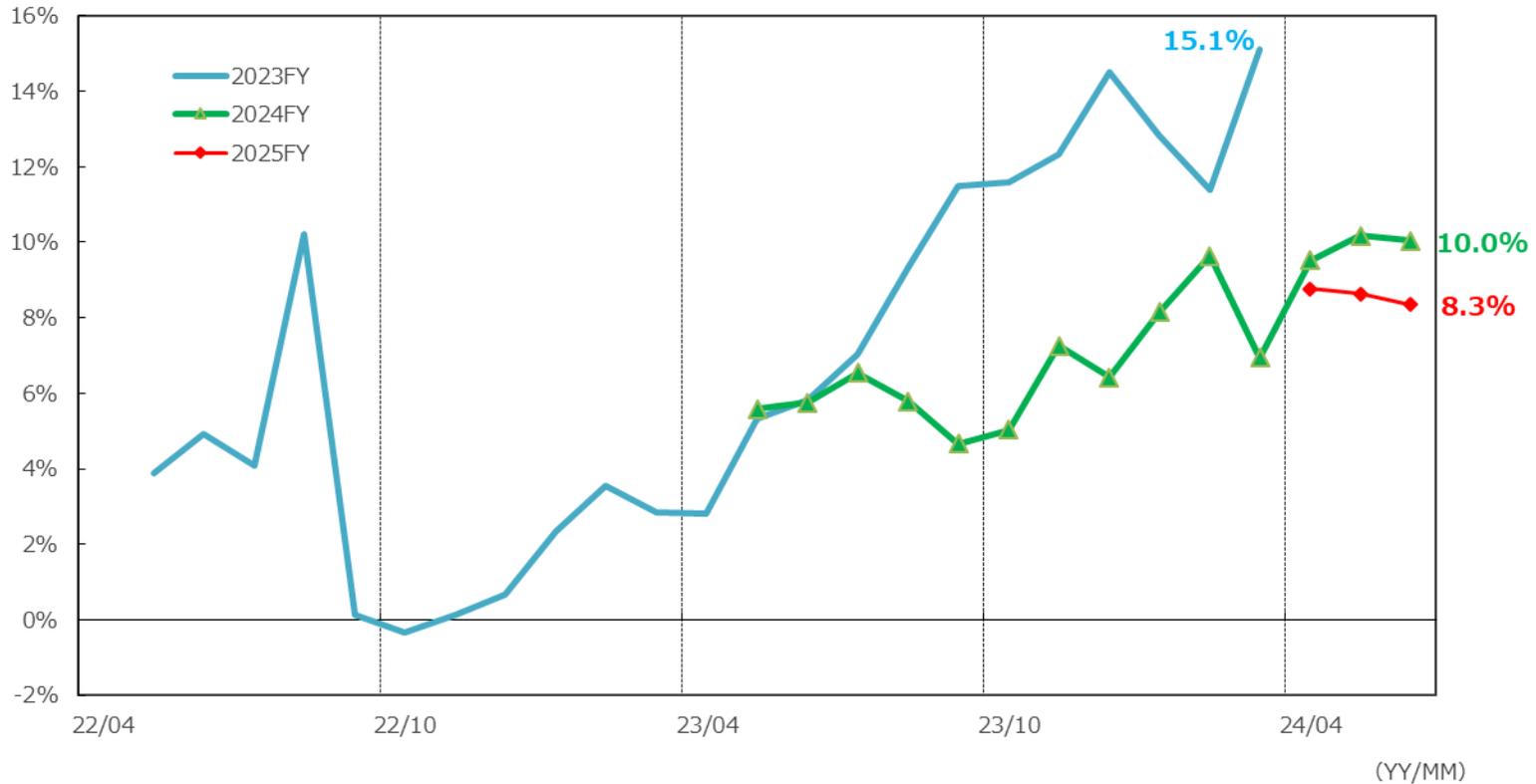
P/E ratio still has room for expansion



Note: Consensus data is from January 2006 to June 2024, Model estimate Data is from February 2006 to December 2025.
Source: SMDAM

Bottom up research indicates steady earnings outlook ahead

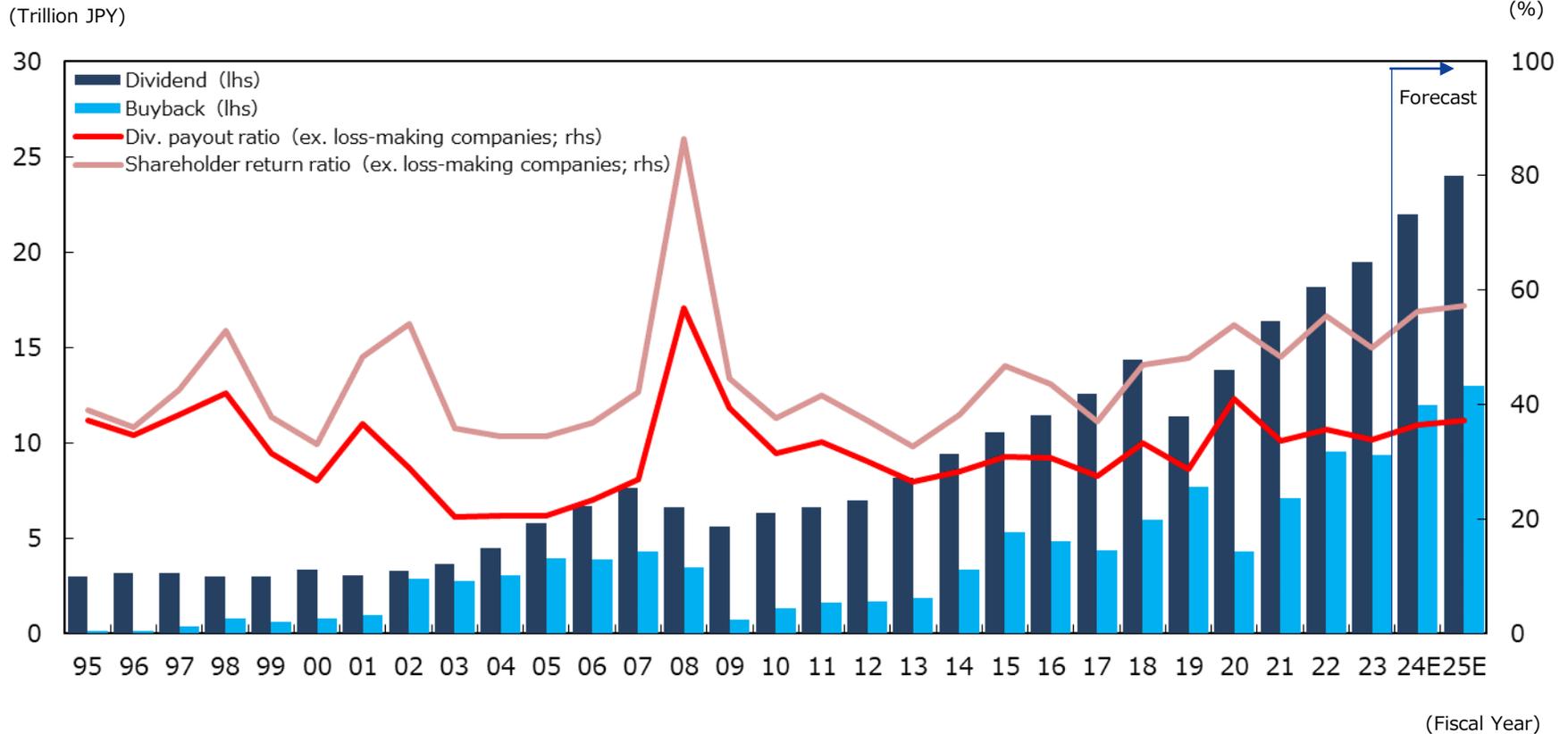
SMDAM Core Research Universe (Excl. Financials) Est. Recurring Profit Growth



Note: Data is as of 10th July 2024, SMDAM Core Universe (Excl. Financials) consists of 386 Japanese companies covered by SMDAM in-house analysts.
Source: SMDAM

Streak of record-breaking dividends and buybacks

Shareholder Return Ratio, Div. Payout Ratio, Dividend Payment, & Share Buyback



Note: Data is from FY1995 to FY2025. FY2024 and FY2025 are forecasts by Daiwa Securities.
 Source: Toyo Keizai, Quick, INDB, Daiwa Securities, SMDAM

Return reversal of Large Cap Growth

Performance Comparison of Russell/Nomura Style Indices

Index	Returns(%)						
	3 Month	6 Month	YTD	1 Year	2 year	3 Year	5 Year
RN Japan Equity	6.68	11.35	19.70	25.07	45.00	48.59	82.91
Total Value	5.60	16.11	25.32	32.63	62.56	77.50	97.63
Top Cap Value	7.69	23.20	34.91	38.71	77.56	98.95	133.15
Large Cap Value	6.14	17.34	27.57	34.19	65.98	83.52	104.32
Mid Cap Value	4.59	11.84	20.77	29.99	53.49	66.88	72.42
Small Cap Value	2.95	10.39	15.31	25.43	47.45	52.17	69.49
Micro Cap Value	4.69	8.74	13.77	24.69	46.66	50.10	65.78
Total Growth	7.73	7.19	14.82	18.09	29.79	25.36	67.37
Top Cap Growth	10.05	9.80	19.54	24.27	36.85	34.91	82.94
Large Cap Growth	8.16	7.83	16.09	19.46	32.03	28.20	73.42
Mid Cap Growth	4.52	4.06	9.68	10.79	23.22	16.65	57.08
Small Cap Growth	3.75	1.50	4.06	6.57	12.17	2.88	23.65
Micro Cap Growth	1.73	-0.72	1.95	4.93	9.89	-2.41	20.54
Top Cap Total	9.10	14.77	25.22	30.18	53.26	59.47	102.33
Large Cap Total	7.22	12.06	21.16	26.22	47.08	51.53	88.54
Mid Cap Total	4.56	8.30	15.67	20.84	38.56	40.79	70.39
Small Cap Total	3.25	6.89	10.83	17.97	32.68	31.10	51.33
Micro Cap Total	3.72	5.48	9.65	17.97	33.37	30.74	50.67

Note : As of 22nd July 2024
(Source) Bloomberg



Outlook for Japanese Economy

Current status & Outlook of Japanese economy

[Current Status]

- **The economy is recovering.** In the first quarter of 2024, economic growth turned negative for the first time in 2 quarters due to a decline in automobile production caused by the safety certification test scandal, the Noto Peninsula earthquake, and a reactionary decline in royalties and receipts for intellectual property rights. While consumer sentiment, represented by the "Economy Watchers Survey" and "Consumer Confidence Index", have been adversely affected by higher inflation, consumer spending, CAPEX, and exports data have been recovering.
- **Inflation is picking up.** Nationwide core CPI rose +2.6% YOY in June, rebounded from +2.5% rise in May. Tokyo Metropolitan Area Core CPI in June rose +2.5% YOY, re-accelerating from +1.9% last month. Inflation was pushed up by energy prices as the policy factor of reduced levies for electricity and gas bills had a large impact.

[Outlook]

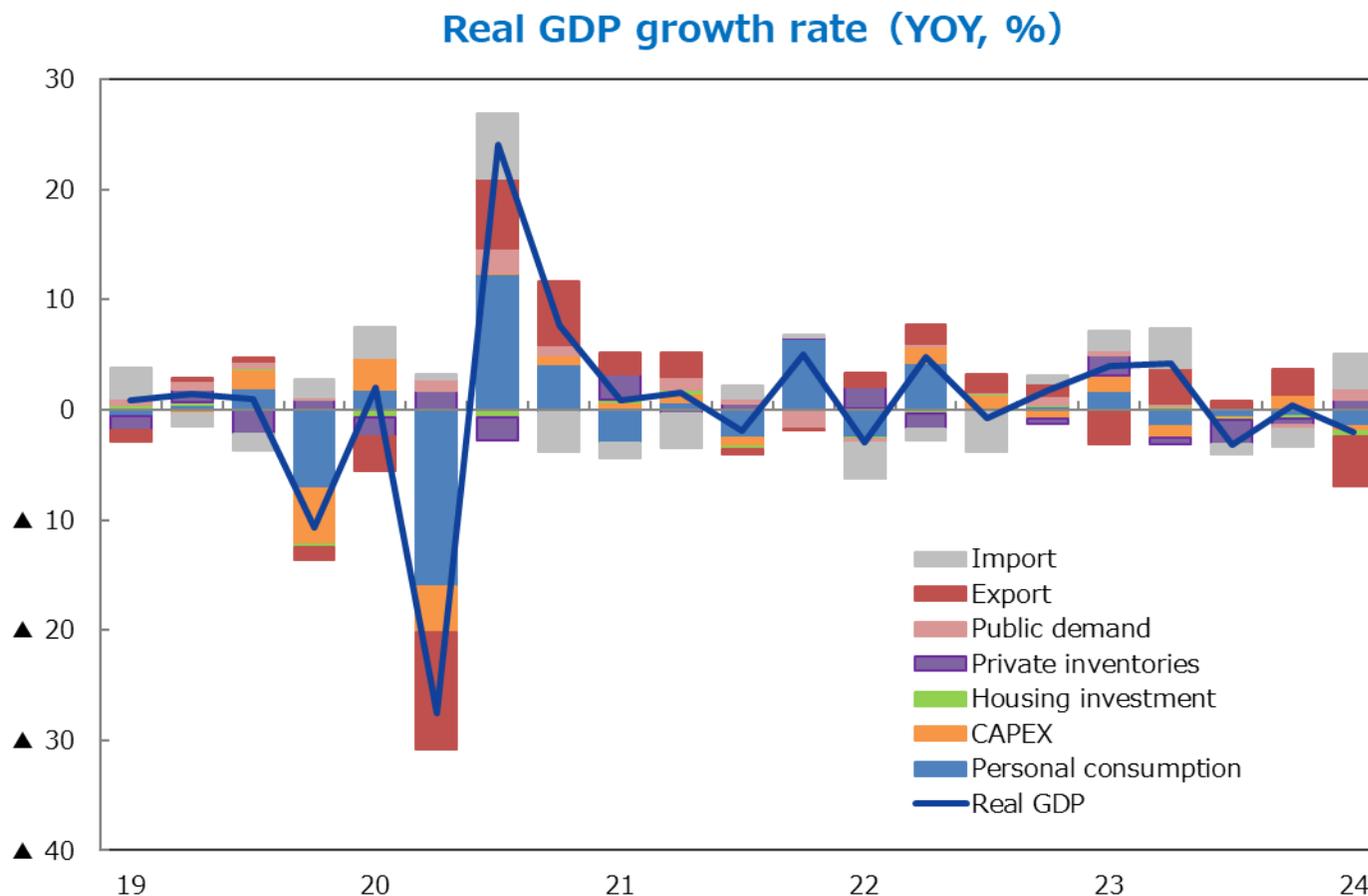
- ① **We have lowered our real GDP growth forecast for FY 2024 to +0.2% from +0.4% and that for FY 2025 to +0.6% from +0.7%.** Figures for FY2024 has been revised downward based on the revision of real GDP figures for Q1 2024, whilst the Japanese economy is expected to return to a moderate growth path from Q2 2024. The economy is expected to recover gradually and avoid recession as temporary downward pressure, caused by factors such as a reduction in automobile production, a major earthquake, and a reactionary decline in royalties on intellectual property rights, is expected to ease. In addition, wage increases, fiscal stimulus, such as tax cuts and benefits, and the resilience of overseas economies could lift the economy going forward. We have slightly lowered our growth forecast as a whole due to an additional monetary tightening by the Bank of Japan at the policy meeting in July.
- ② **While we maintain our core CPI forecast for FY 2024 at +2.5%, we have lowered that for FY 2025 to +2.2% from +2.3%.** The revision for FY 2025 figures is mainly due to a change in the monetary policy and assumptions for fiscal policy against higher living prices. Regarding these measures, utility bill subsidies will be temporarily resumed between August and October 2024, while the gasoline subsidy, which we had previously forecast to be extended, will end at the end of 2024. In FY 2024, the effects of these two measures will mostly offset each other, but in FY 2025, both measures will lift our inflation forecasts. The nationwide core CPI is likely to be +2% by the end of 2025, given the energy boost from the end of subsidies for utility bills and gasoline. Thereafter, core CPI is likely to decelerate again due to the receding energy factor, and core CPI is expected to remain stable at around +2% YOY from around H2 of CY 2025, supported by the rise in service prices accompanied by wage hikes.
- ③ **We expect the government to continue their accommodative fiscal policy.** Prime Minister Kishida said the government will start economic measures in autumn after implementing new counter measures against rising prices. In addition to providing subsidies to low-income households, the government will provide local subsidies to small and medium-sized companies, school lunches, medical and nursing care, logistics and regional tourism. While his statements did not suggest large-scale measures, we will pay close attention to the risk of fiscal policy expansion.
- ④ **The Bank of Japan had decided to raise its policy rate at the July policy meeting to 0.25% from range of 0 - 0.1% and to gradually reduce the volume of JGB purchases from JPY 6 trillion a month to JPY 3 trillion by the end of FY2025. Now we expect the BOJ to raise its policy rate by 0.25% in December 2024, June 2025, and December 2025, and the rate will reach 1.0% by the end of 2025.** The BOJ governor Ueda had repeatedly stressed that the real interest rate is very low and the negative impact of a rate hike on the economy would be limited at a press conference after the central bank's monetary policy meeting. Given this, the hurdle for further monetary tightening is not so high and we expect the BOJ will raise its policy rate again before the end of the year.

Forecast for the Japanese economy

Forecast of annual Real GDP growth and its breakdown							
Fiscal Year	FY19	FY20	FY21	FY22	FY23	FY24 Est	FY25 Est
Real GDP	-0.8%	-3.9%	2.8%	1.6%	1.2%	0.2%	0.6%
Private final consumption expenditure	-0.9%	-4.8%	1.8%	2.7%	-0.6%	-0.1%	0.8%
Private housing investment	2.6%	-7.4%	0.2%	-3.4%	0.6%	-1.8%	-0.9%
Private-sector capital investment	-1.3%	-5.6%	1.7%	3.4%	0.5%	2.1%	0.8%
Private inventory investment	-0.2%	-0.2%	0.5%	0.1%	-0.2%	-0.1%	0.0%
Public fixed capital formation	1.6%	4.8%	-6.5%	-6.1%	4.0%	-1.9%	0.5%
Net export contribution	-0.5%	-0.6%	0.8%	-0.5%	1.5%	-0.1%	0.0%
Exports of goods and services	-2.3%	-9.9%	12.4%	4.9%	3.0%	1.5%	3.0%
Imports of goods and services	0.2%	-6.3%	7.2%	6.9%	-3.2%	1.9%	3.3%
Nominal GDP	0.0%	-3.2%	2.7%	2.4%	5.2%	2.3%	2.4%
GDP deflator	0.8%	0.7%	-0.1%	0.8%	4.0%	2.2%	1.7%
Industrial Production Index	-3.5%	-9.6%	5.6%	-0.3%	-1.9%	1.6%	1.5%
Consumer Price Index (Core)	0.4%	-0.6%	0.1%	3.0%	2.8%	2.5%	2.2%
Domestic corporate goods price index	0.1%	-1.5%	7.1%	9.5%	2.3%	1.9%	1.1%
Employee compensation	2.0%	-1.5%	2.1%	2.4%	1.9%	3.4%	3.6%
Unemployment rate	2.4%	2.9%	2.8%	2.6%	2.6%	2.5%	2.3%
Monetary Policy interest rate (Short term)	-0.10%	-0.10%	-0.10%	-0.10%	0-0.1%	0.50%	1.00%

Note: Rate of increase over the previous year. Net exports are based on the degree of contribution, and the consumer price index (Core) excludes the effects of the consumption tax and free education.
Source: Sumitomo Mitsui DS Asset Management based on data from the Cabinet Office, the Ministry of Internal Affairs and Communications, and the Ministry of Economy, Trade and Industry

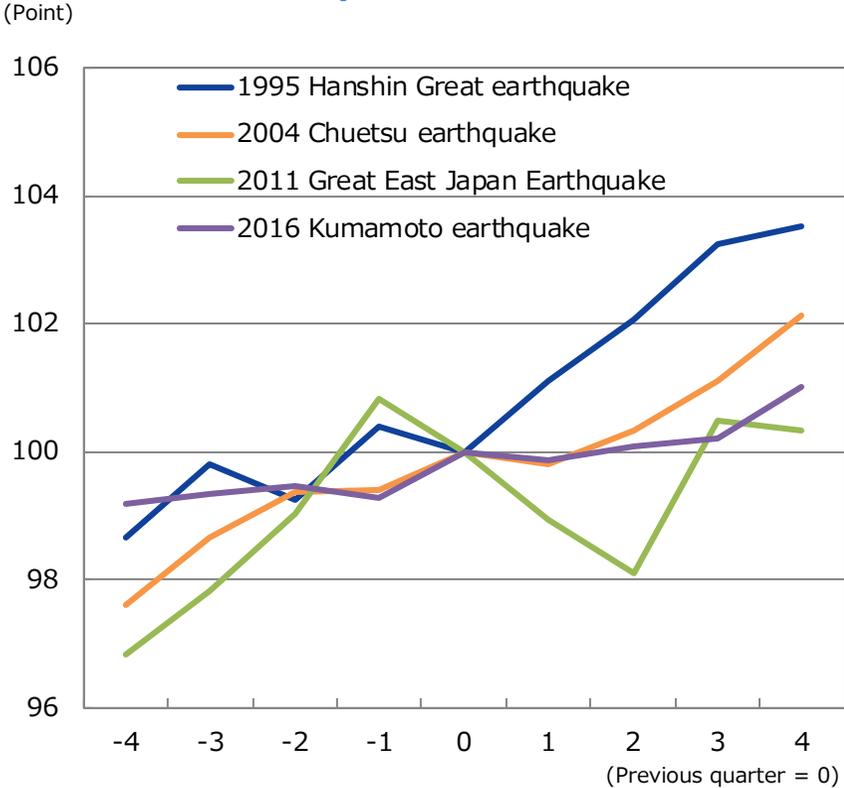
Temporary factors brought Japanese GDP back to negative



Note: Data is from Q1 2019 to Q1 2024.
Source: Cabinet office, SMDAM

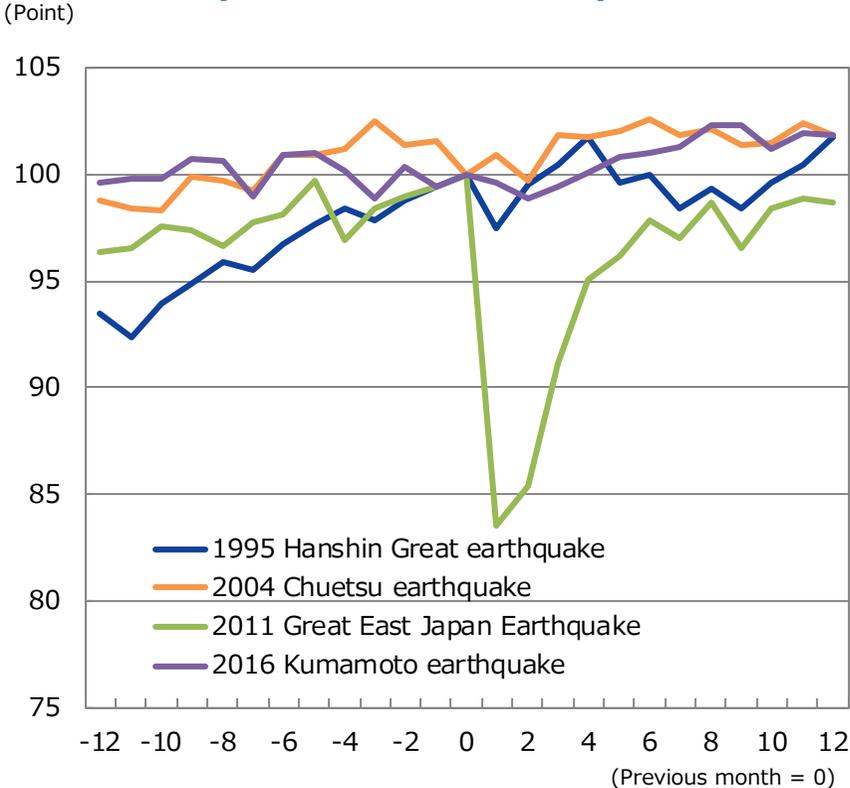
Earthquakes have had short lived impact on the economy

Earthquake & Real GDP



Note: Data of the previous quarter of the earthquake was indexed as 100.
Source: Cabinet office, METI, SMDAM

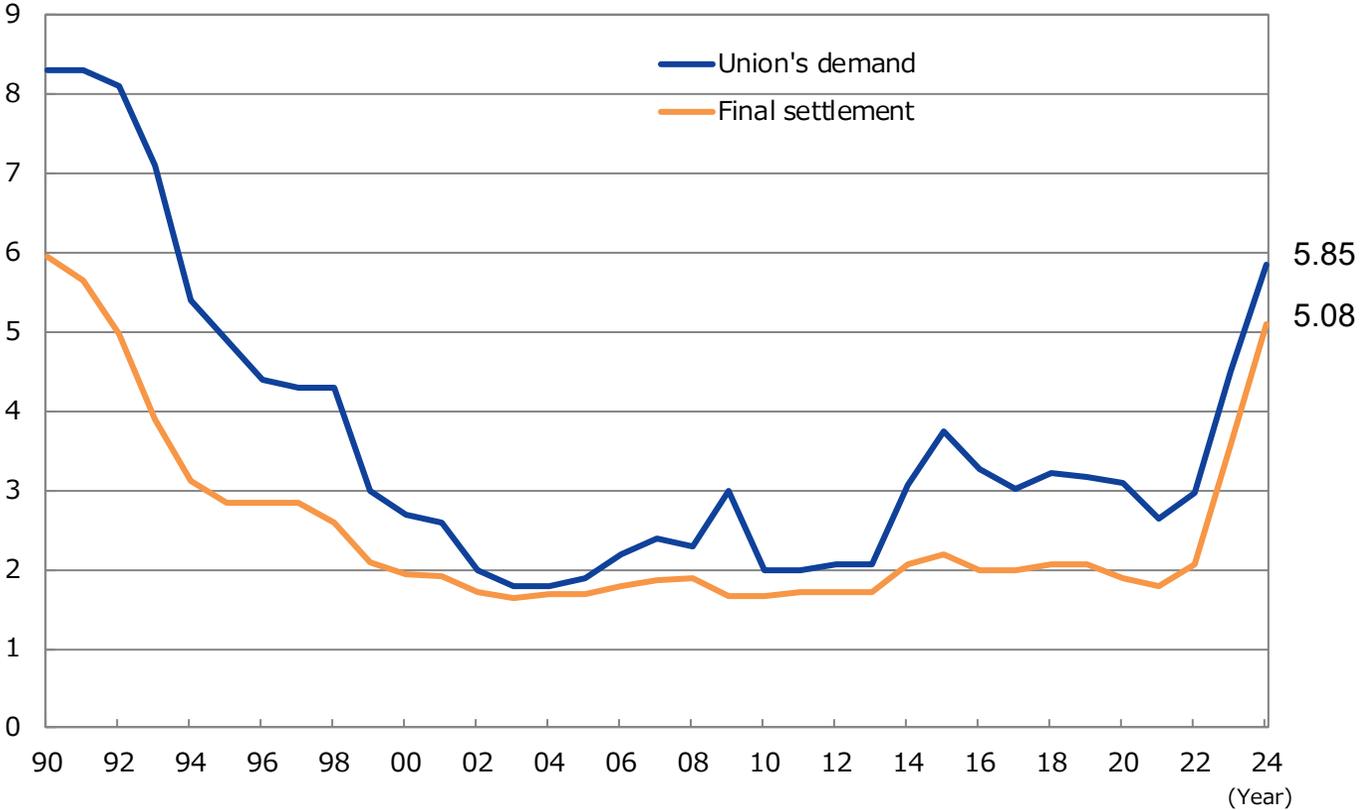
Earthquake & Industrial production



Note: Data of the previous month of the earthquake was indexed as 100.
Source: Cabinet office, METI, SMDAM

Highest wage increase in 33 years

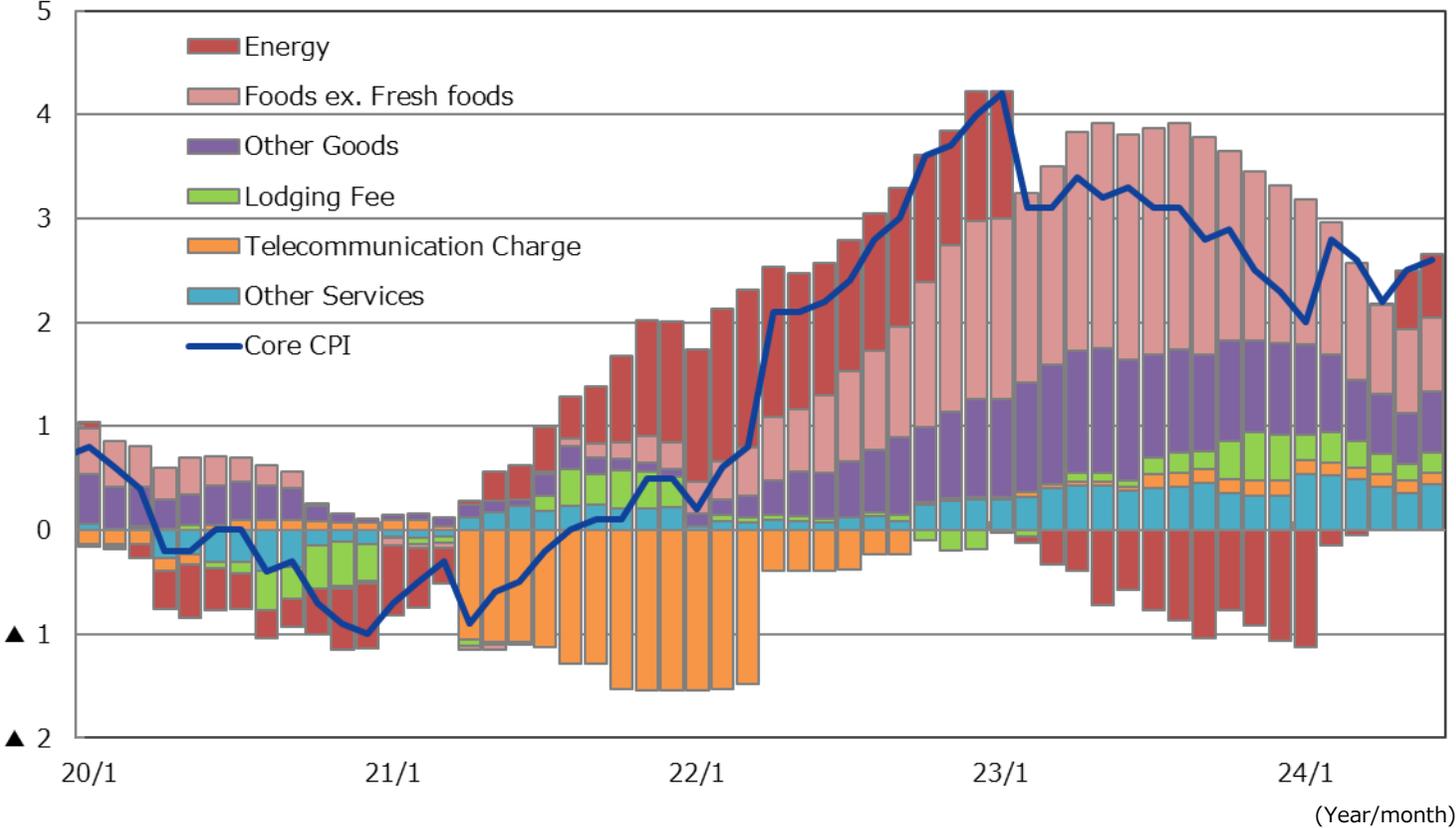
Wage increase (YOY, %)



Note: Data is from FY 1990 to FY 2024.
Source: Japanese Trade Union Confederation, SMDAM

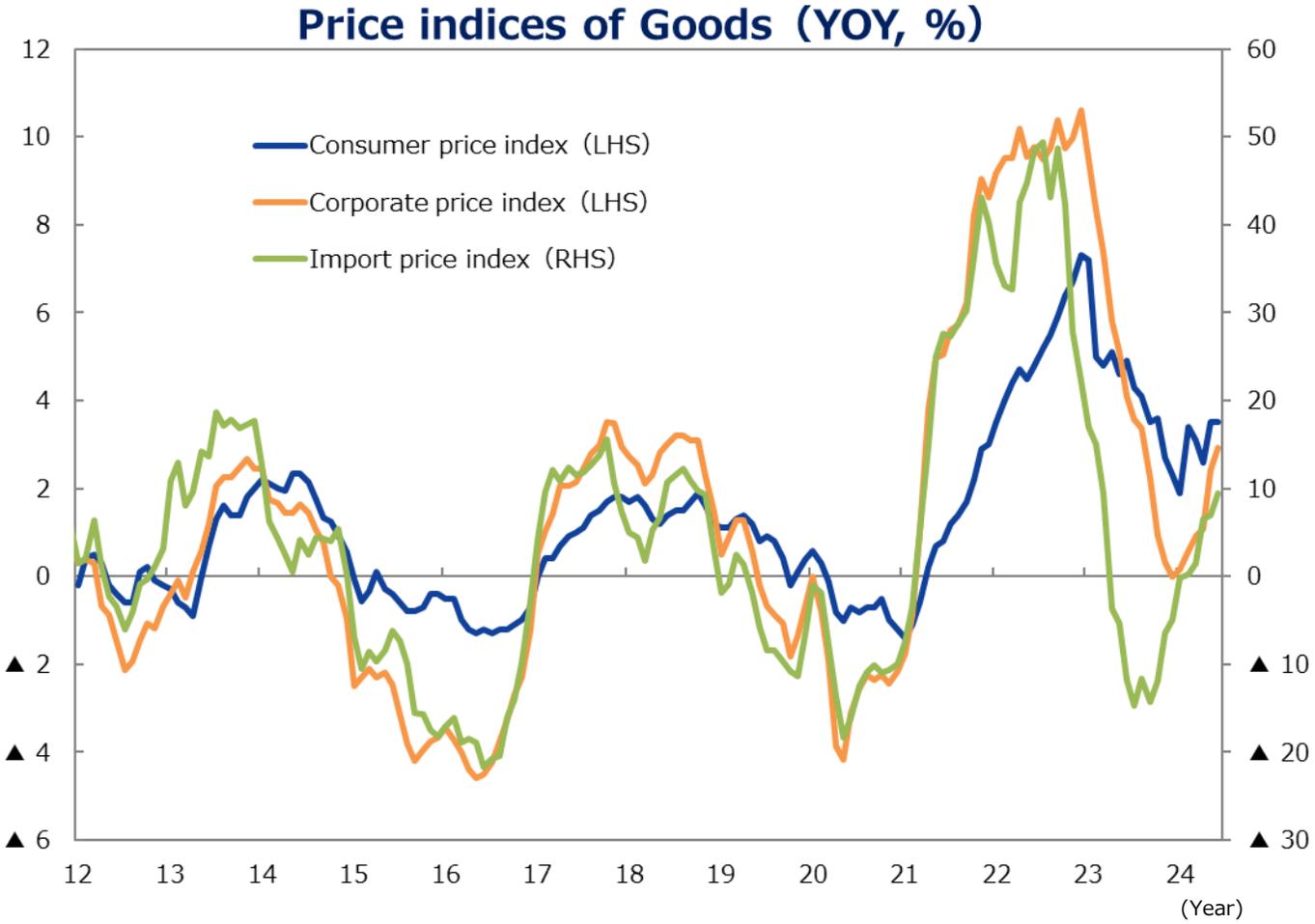
End of utility bill subsidies lifts CPI temporarily

Breakdown of CPI (YOY, %)



Note: Data is from January 2020 to June 2024.
Source: MIAC, SMDAM

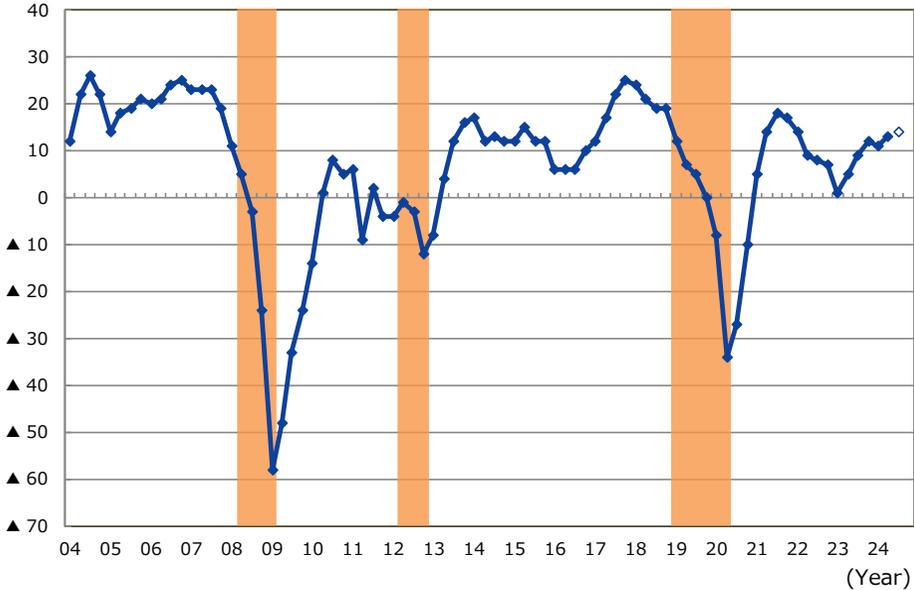
Cost push inflation again?



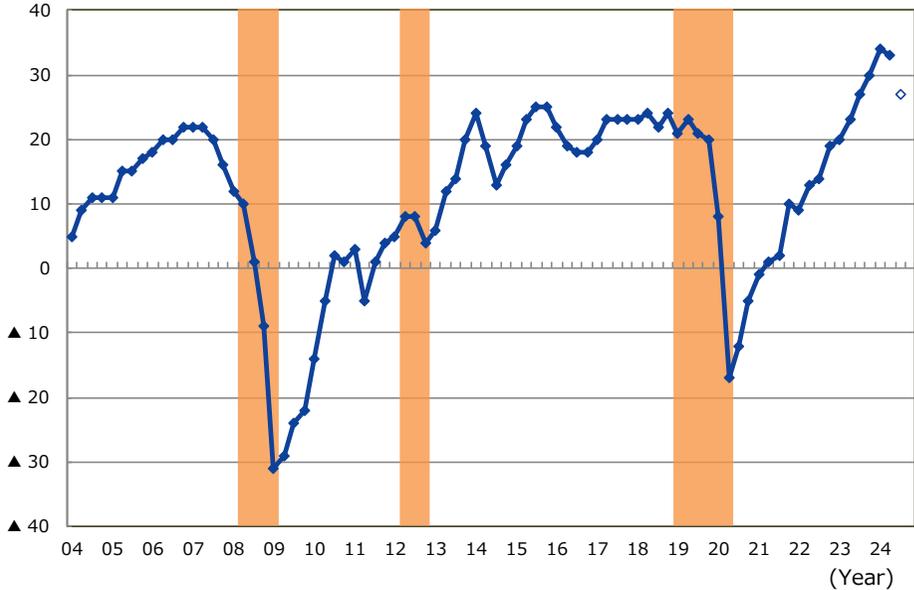
Note: Data is from January 2012 to June 2024.
Source: MIAC, Bloomberg, SMDAM

Non-manufacturers sentiment fell for the first time in 4 years

BOJ business condition DI Large manufacturers (%)



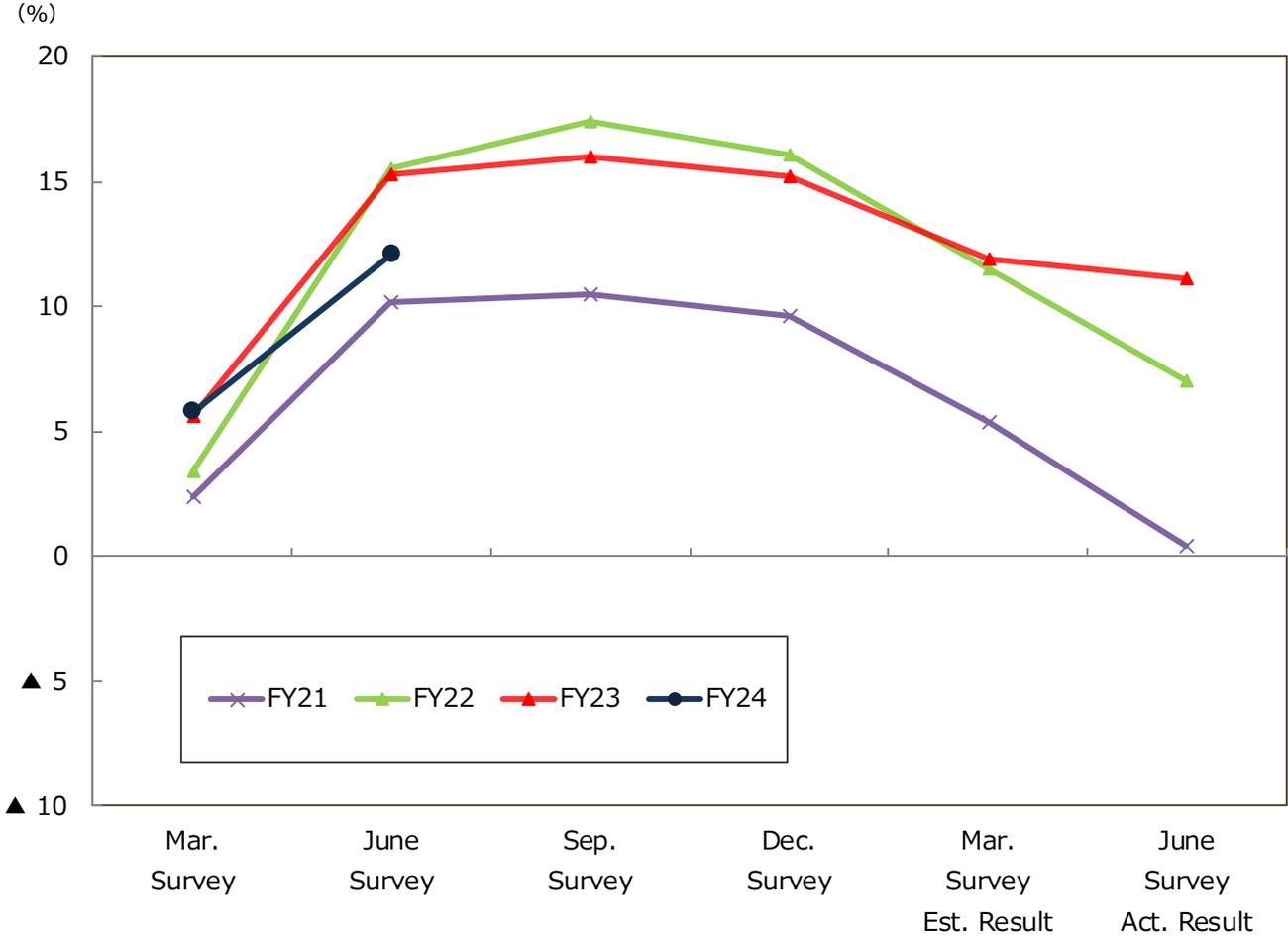
BOJ business condition DI Large non-manufacturers (%)



Note: Data is from Q1 2004 to Q2 2024. The orange shadow are periods of economic recession.
 Source: The Bank of Japan, SMDAM

CAPEX maintains a brighter outlook in 2024

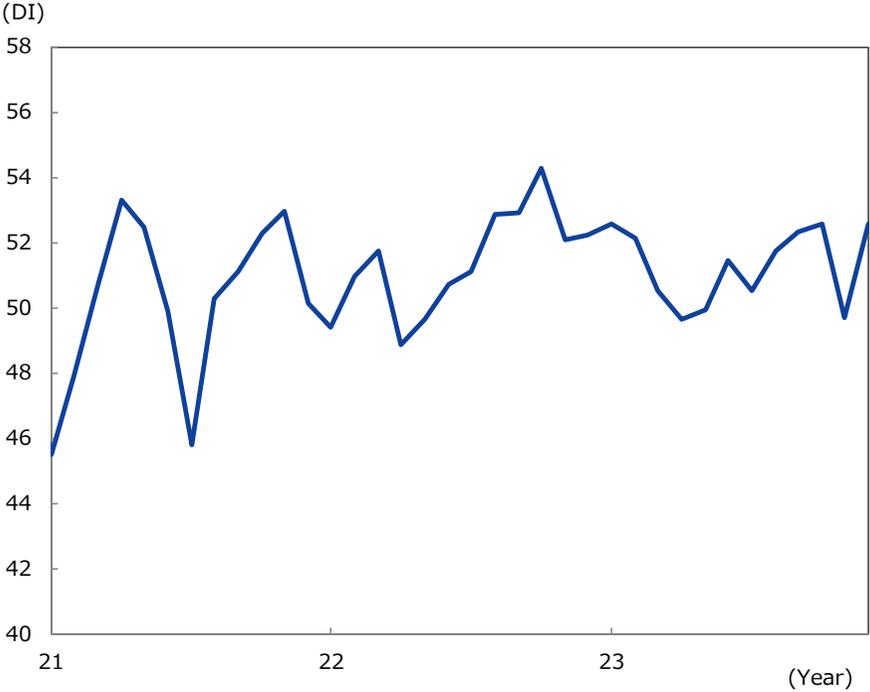
Plan of CAPEX (Inc. Software, Ex. Land and R&D, YOY)



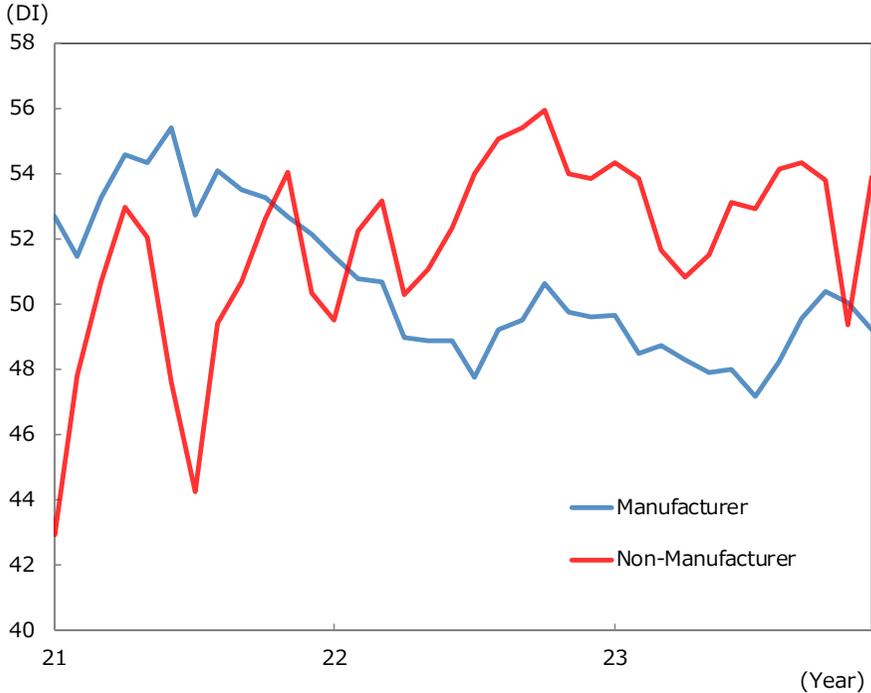
Note: Data is from Q1 FY2021 to Q2 FY2024.
Source: The Bank of Japan, SMDAM

New business and employment condition boost service PMI

Composite PMI



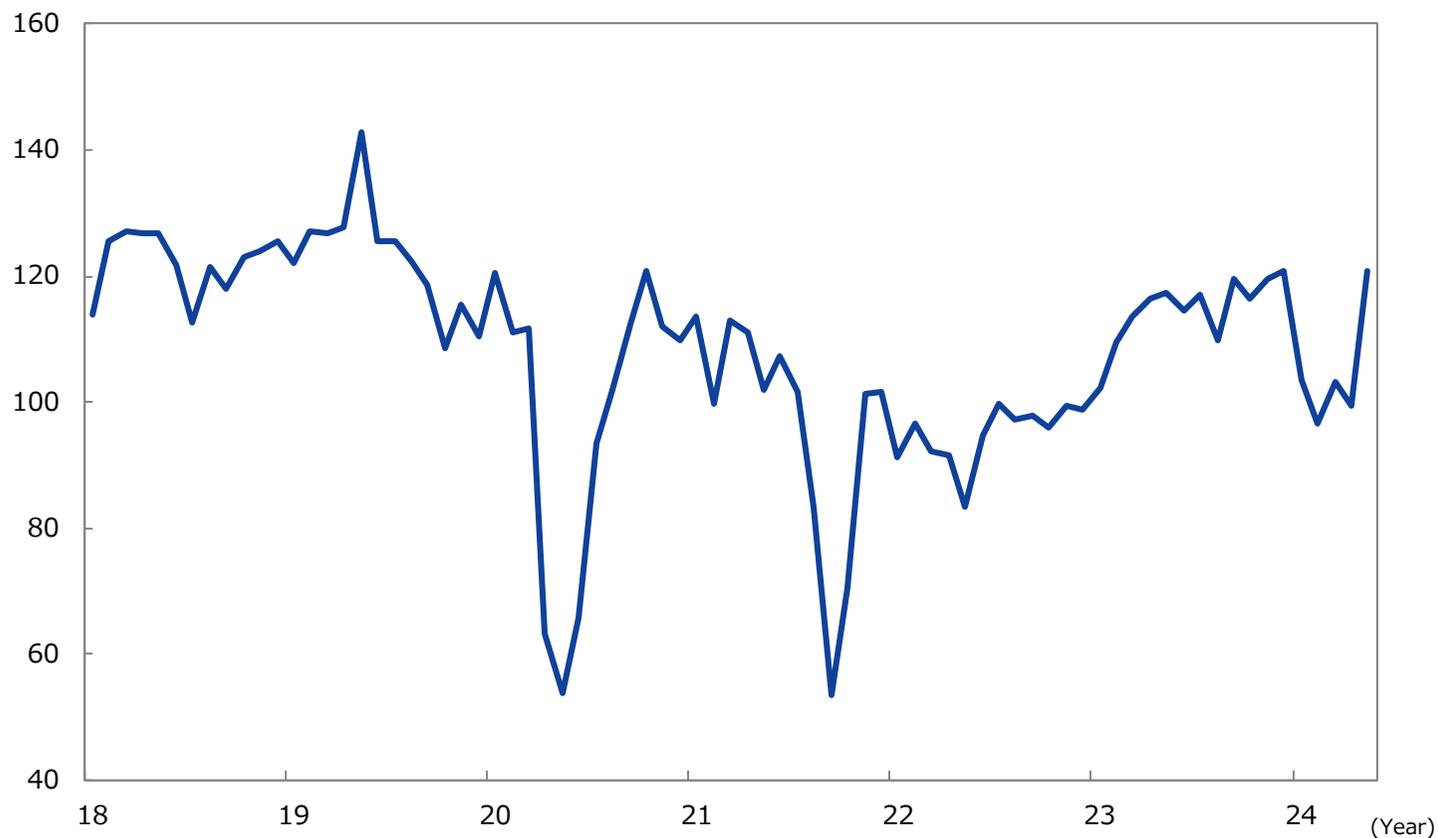
PMI, Manufacturer & Non-Manufacturer



Note: Data is from August 2021 to July 2024.
Source: Bloomberg, SMDAM

Auto production back to normal after temporary pause

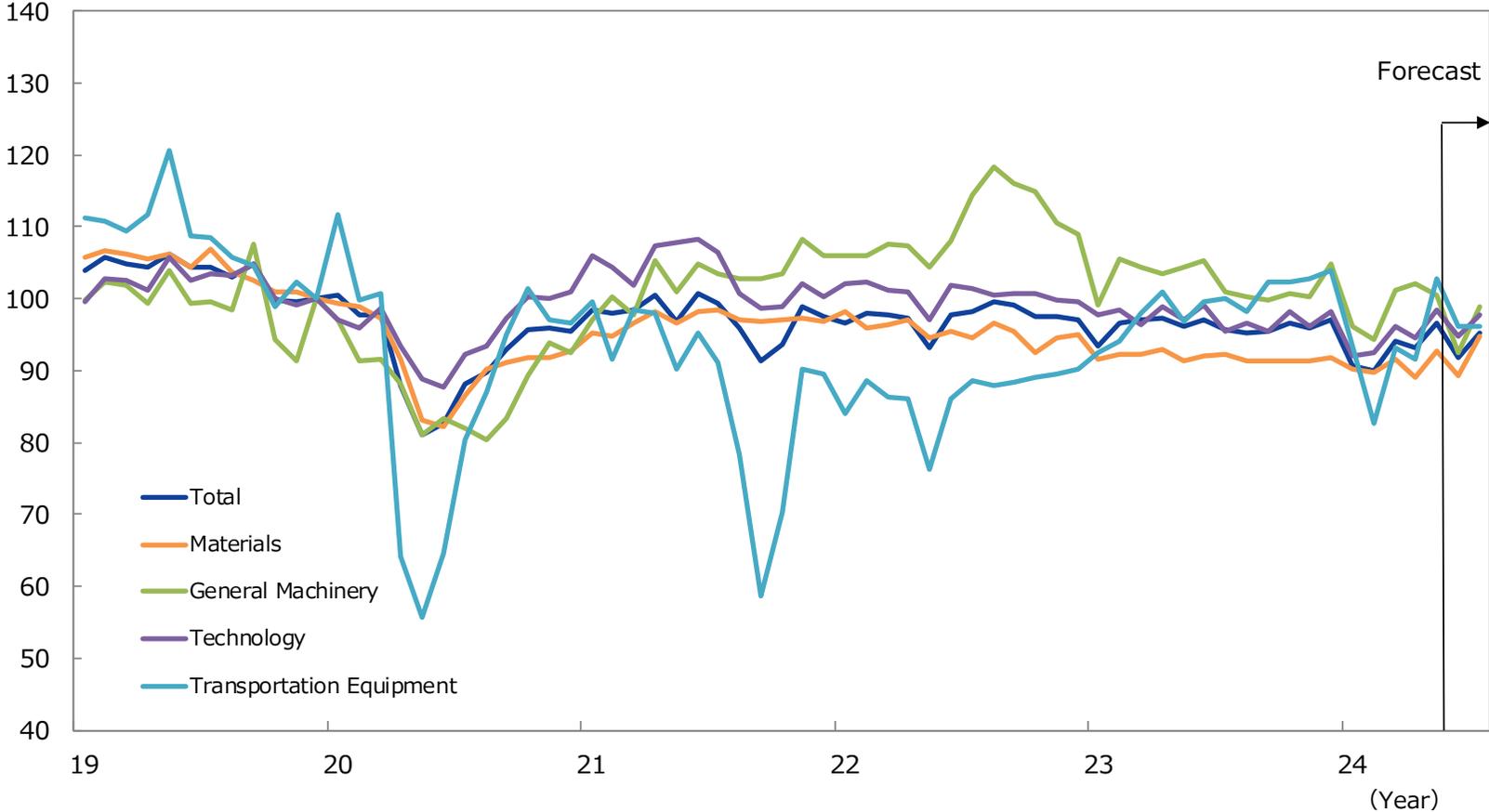
Automobile production (2020=100)



Note: Data is from January 2018 to May 2024.
Source: METI, SMDAM

Rebound of auto production to lift industrial production

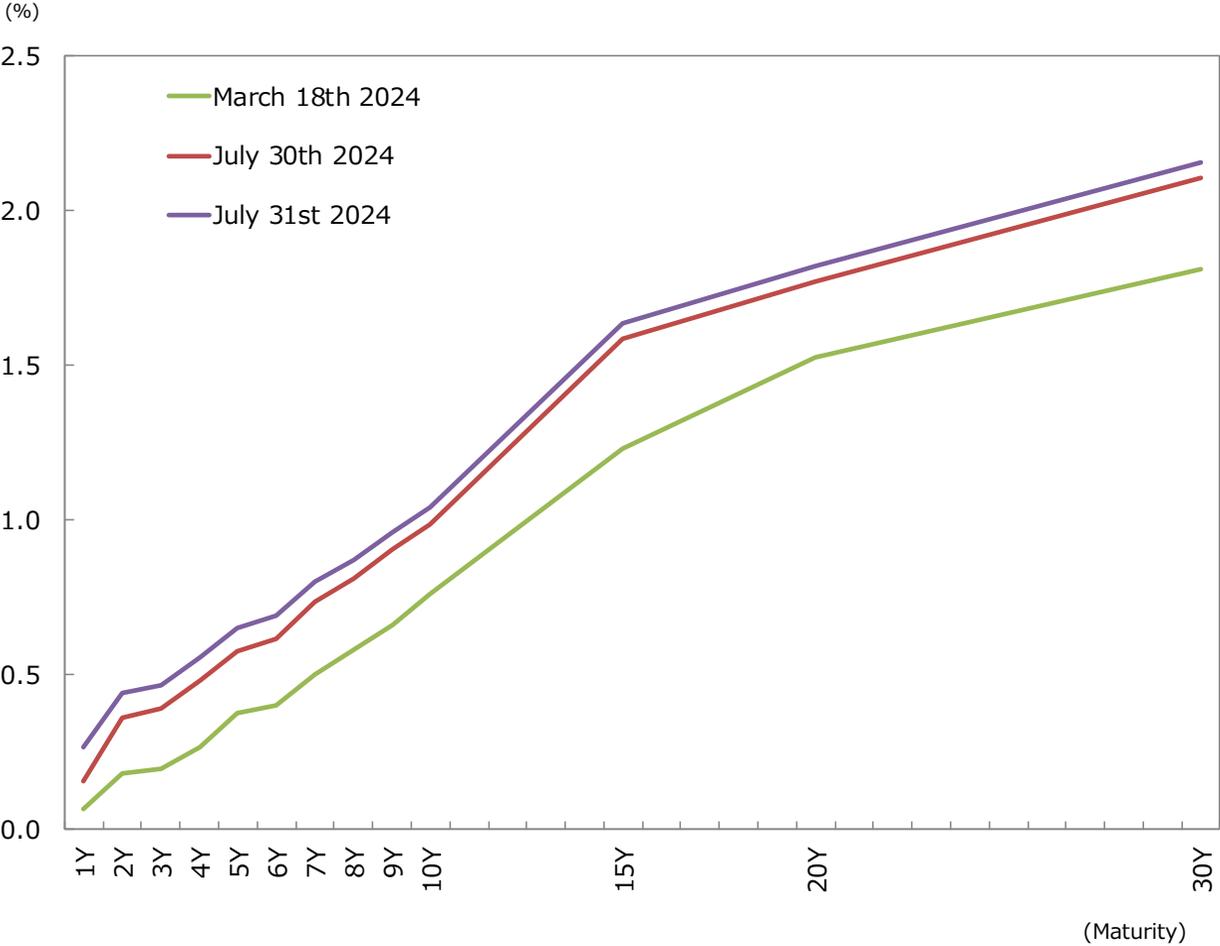
Industrial Production (Dec. 2019=100)



Note: Data is from January 2019 to June 2024. Data after May 2024 is forecasts.
Source: METI, SMDAM

Bear steepening of JGB yield curve due to BOJ's tightening

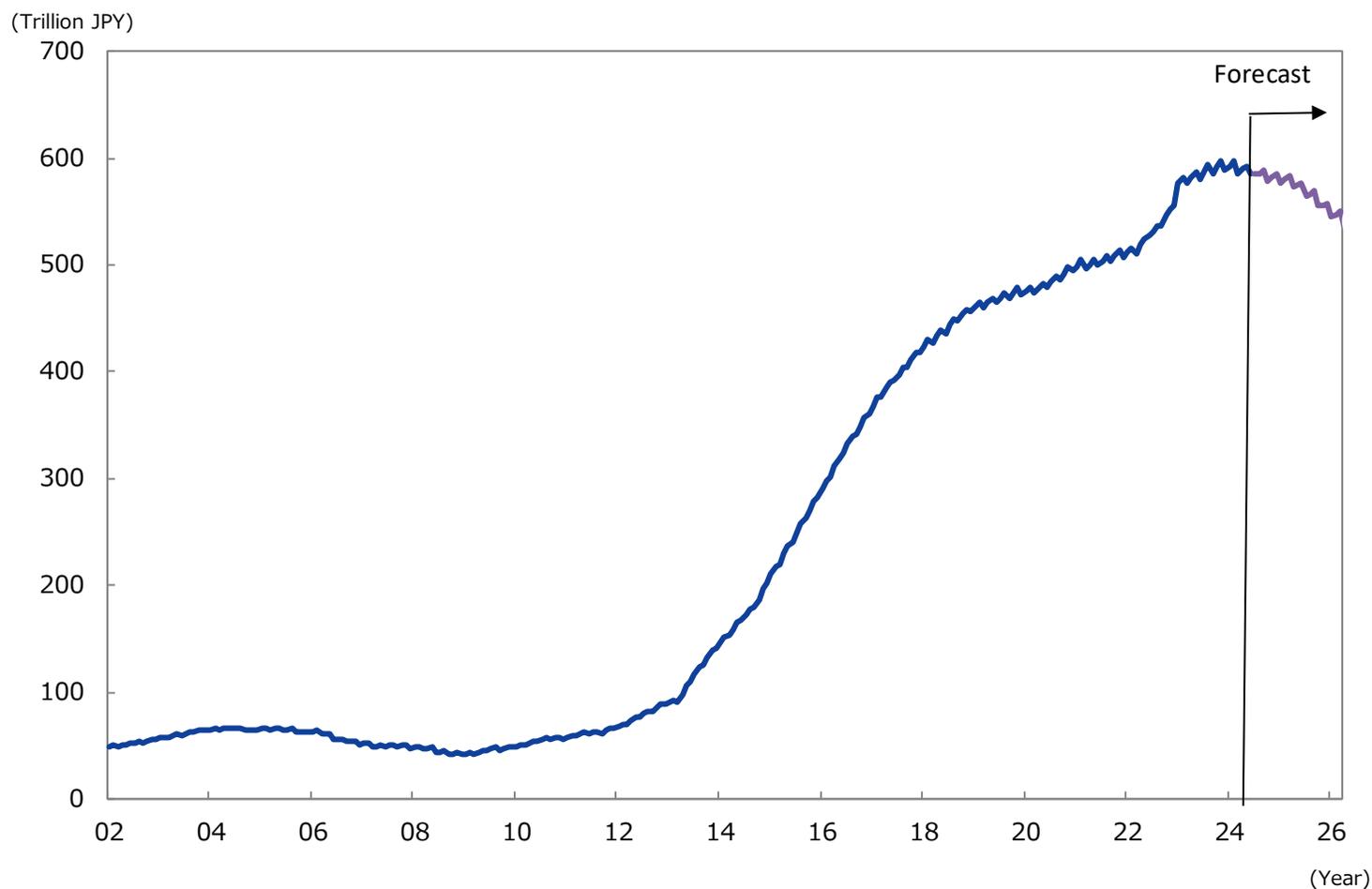
Yield Curve of Japanese Sovereign



Source: Bloomberg, SMDAM

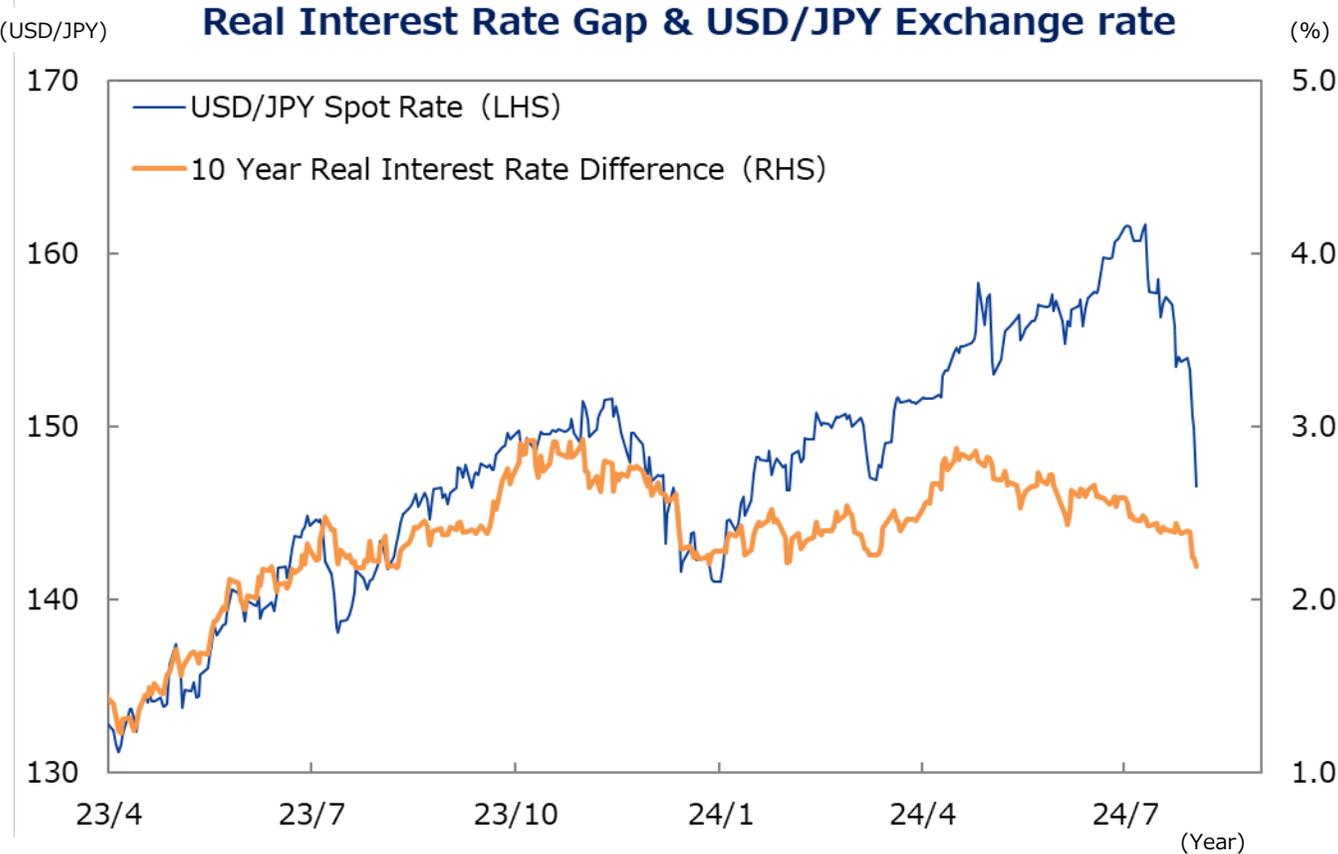
The BOJ to reduce bond purchase by about JPY 0.4 trillion every quarter

BOJ's holding of long term JGB



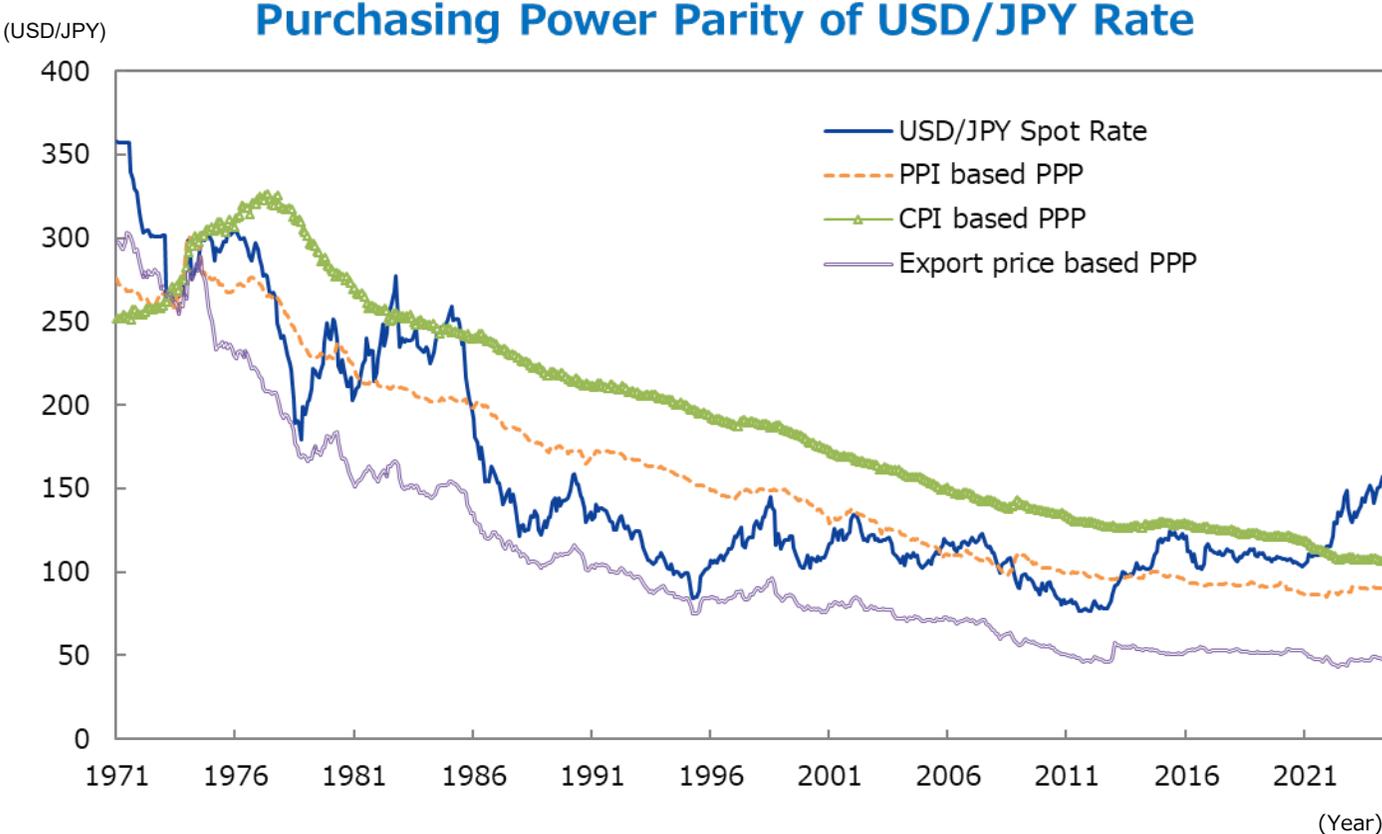
Note: Data is from January 2002 to March 2026. Data after June 2024 is forecasts.
Source: METI, SMDAM

Resuming correlation between interest rate and USD/JPY rate



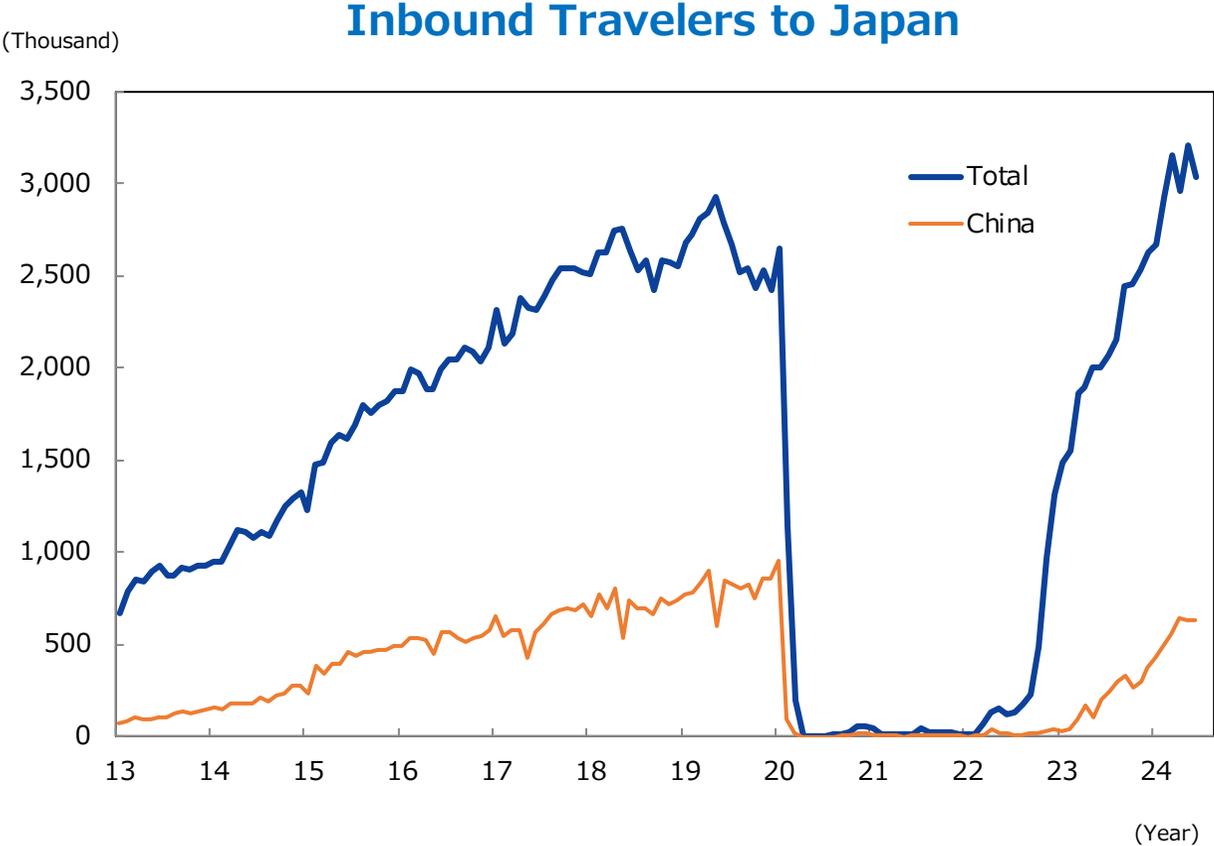
Note: Real interest rates are 10 year government bond yields. Data is from 1st April 2023 to 2nd August 2024.
Source: Bloomberg, SMDAM

Convergence to “purchasing power parity” again?



Note: Data is from January 1971 to June 2024.
Source: DOL, Bank of Japan, SMDAM

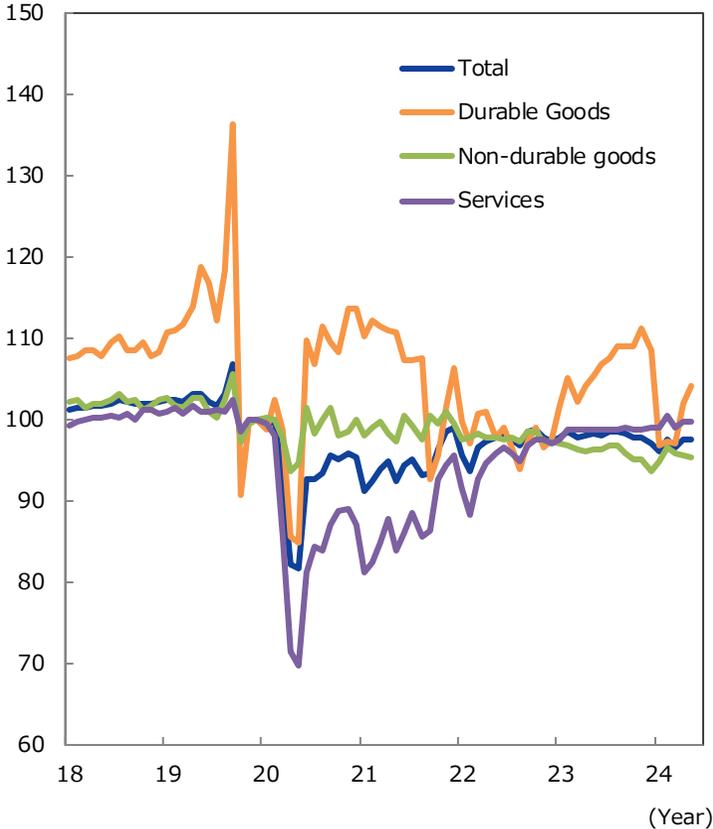
Inbound travel exceeds pre-COVID historical high



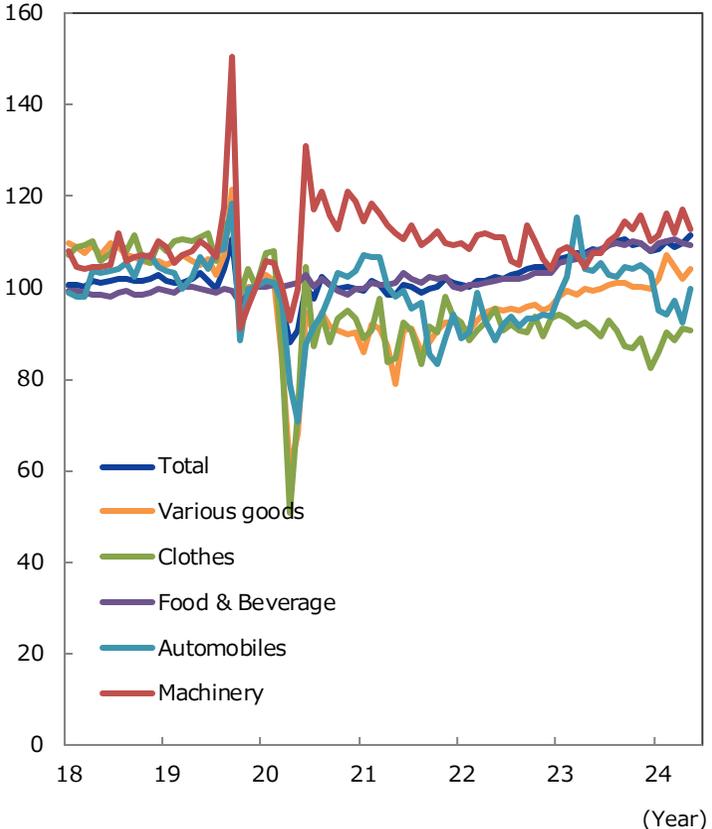
Note: Data is from January 2013 to June 2024. Data is non-seasonally adjusted.
Source: Japan National Tourism Organization, SMDAM

Rebound of autos pushes up retail sales

Consumer Activity Index (Dec. 2019 = 100)



Retail Sales (Dec. 2019 = 100)



Note: Data is from January 2018 to May 2024.
Source; Bank of Japan, METI, and SMDAM

Has PM Kishida's approval rate hit the bottom?

Cabinet approval rate



Note: Data is from January 2013 to July 2024.
Source: NHK, Asahi, Kyodo, Nikkei, Yomiuri, Sankei, Mainichi, Jiji, and SMDAM

Schedule of major events

Year	Month	Date	Event
2024	August	15	Release of Q2 GDP
	September	9	Revision of Q2 GDP
		19-20	Monetary Policy Meeting
		30	Termination of the presidency of the LDP
	October	30-31	Monetary Policy Meeting
November	15	Release of Q3 GDP	
2024	December	9	Revision of Q3 GDP
		18-19	Monetary Policy Meeting Cabinet approval of the initial budget for FY 2025 and the outline for tax reform
2025	January		Ordinary Diet Session Monetary Policy Meeting
	February		Release of 2024 Q4 GDP
	March	25	Expiration of the term of the Bank of Japan's Adachi Policy Board member
			Revision of 2024 Q4 GDP
			Monetary Policy Meeting Enactment of the FY 2025 budget and tax-related bills
	April	13	Start of Osaka Expo Monetary Policy Meeting
	May		Release of 2025 Q1 GDP
June	30	Expiration of the term of the Bank of Japan's Nakamura Policy Board member	
		Revision of 2025 Q1 GDP Monetary Policy Meeting Cabinet's decisions on "Big-boned policy" End of the ordinary Diet session	
July		Election of the House of Councillors	

(Source) Compiled by Sumitomo Mitsui DS Asset Management Co., Ltd.

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