



# Japanese Stock Market Outlook

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SMAM monthly comments & views  
- July 2015 -



Sumitomo Mitsui Asset Management

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## Executive summary

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### ➤ Japanese Economy

Japan's economic recovery is on track, as robust Exports and Industrial Production lead the moderate growth. Meantime, faltering Consumption is likely to recover on real wages gain and wealth effect.

- SMAM raised real GDP forecast from +1.5% to +1.6% in FY2015 and kept unchanged at +1.9% in FY2016.
- Exports and Industrial Production in April-June are expected to grow at slower pace, and accelerate from 2H 2015 alongside moderate global recovery.
- Private Consumption data shows still soggy, however Consumption will accelerate from June led by higher wages gain and wealth effect on higher stock prices.
- SMAM expects Core-CPI to stay at +0.2% for FY2015 and +1.1% for 2016, which is far below the inflation forecast by BOJ, but the bank is less likely to move to additional easing.

### ➤ Japanese Stock Markets

Current stocks are fairly valued on upbeat corporate earnings. There would be still some room for upward revision in profit forecast based on current currency rates.

- FY2015 corporate profits are expected to be revised upward due to weak JPY.
- Overseas investors were accumulating Japanese equities.
- Downside risk is associated with foreign factors such as geopolitical concerns, uncertainties surrounding monetary policy by Fed and ECB, and possibly negative effects by crude oil price slump.

Notes: Macro and market views are as of June 17<sup>th</sup> and 19<sup>th</sup>, 2015 respectively, and subject to updates thereafter without notice

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# Outlook for Japanese Economy

## SMAM economic outlook for FY15-16

- SMAM raised real GDP forecast to 1.6% from +1.5% for FY2015.
- Private Housing Investment and Private Capital Investment were upgraded for FY2015, whereas Private Consumption Expenditures and Public Capital Investment were downgraded.

	FY12	FY13	FY14E	FY15E	FY16E
Real GDP growth	1.0%	2.1%	-0.9%	1.6%	1.9%
Private Consumption Expenditure	1.8%	2.5%	-3.1%	1.4%	2.0%
Private Housing Investment	5.7%	9.3%	-11.7%	1.3%	4.4%
Private Capital Investment	1.2%	4.0%	0.4%	3.5%	3.2%
Public Consumption Expenditure	1.5%	1.6%	0.4%	0.7%	0.5%
Public Capital Investment	1.0%	10.3%	2.0%	-3.3%	-1.6%
Net Exports (contrib. to GDP growth)	-0.8%	-0.5%	0.6%	0.3%	0.1%
Exports	-1.3%	4.7%	8.0%	6.3%	5.0%
Imports	3.6%	6.7%	3.7%	5.4%	5.2%
Nominal GDP	0.1%	1.8%	1.6%	2.2%	2.4%
GDP Deflator	-0.9%	-0.3%	2.5%	0.6%	0.5%

FY starting April and ending March

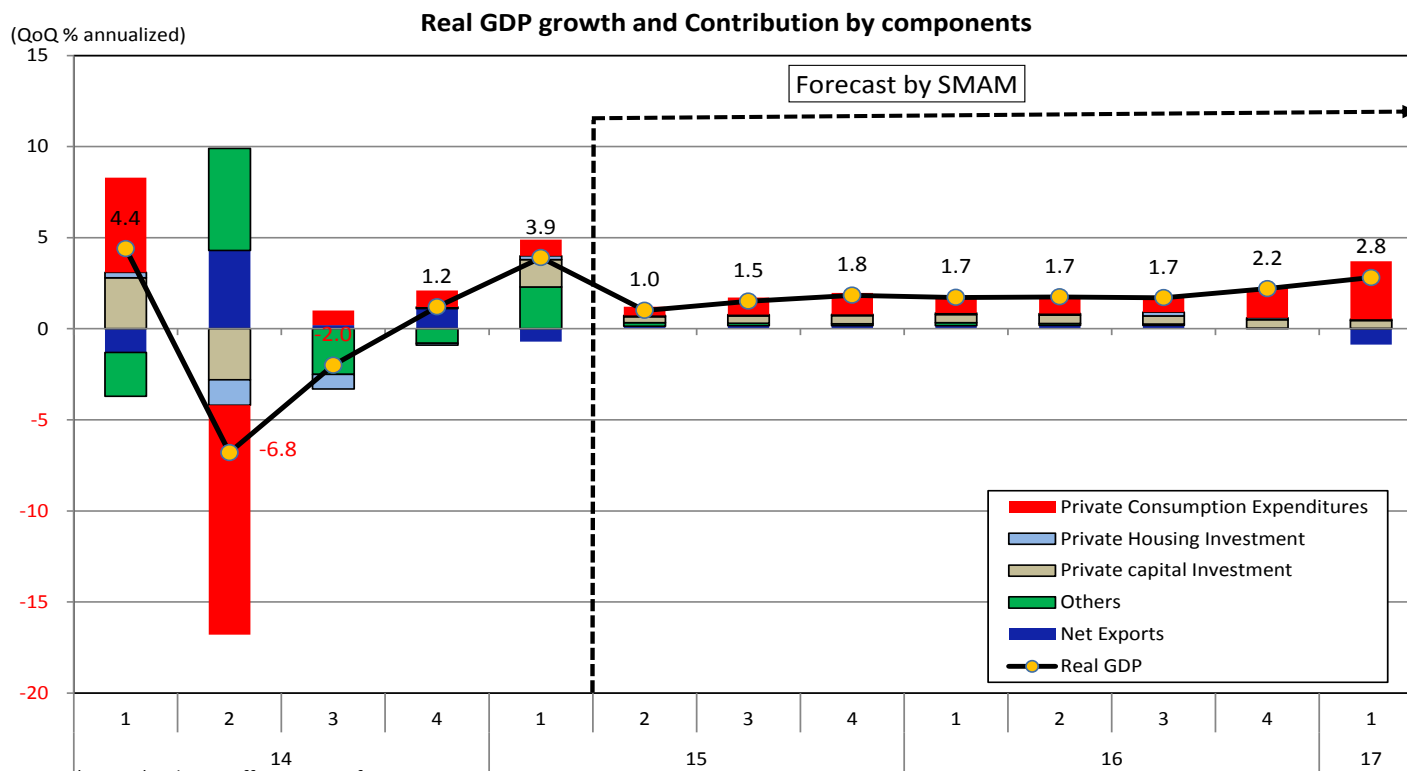
Notes: E=SMAM forecasts. SMAM views are as of June 17<sup>th</sup>, 2015 and subject to updates thereafter without notice

(%, YoY except Net Exports)

Source: Cabinet Office; Bank of Japan, Ministry of Economy, Trade and Industry, Ministry of Internal Affairs and Communications, SMAM forecasts

## Quarterly GDP: Mid-to-high-1% growth after a strong growth in January-March

- Better than expected “Revised” January-March real GDP came in on June 9<sup>th</sup>, soaring to annualized +3.9% QoQ led by strong Private Capital Investment. Private Capital Investment surprisingly jumped +2.7% QoQ, whereas Private Consumption Expenditures added +0.4% QoQ in the period.
- The economy is likely to stay soft in April-June after the strong growth in January-March. SMAM expects the economy to keep a mid-to-high-1% growth underpinned by solid domestic demands and Exports.



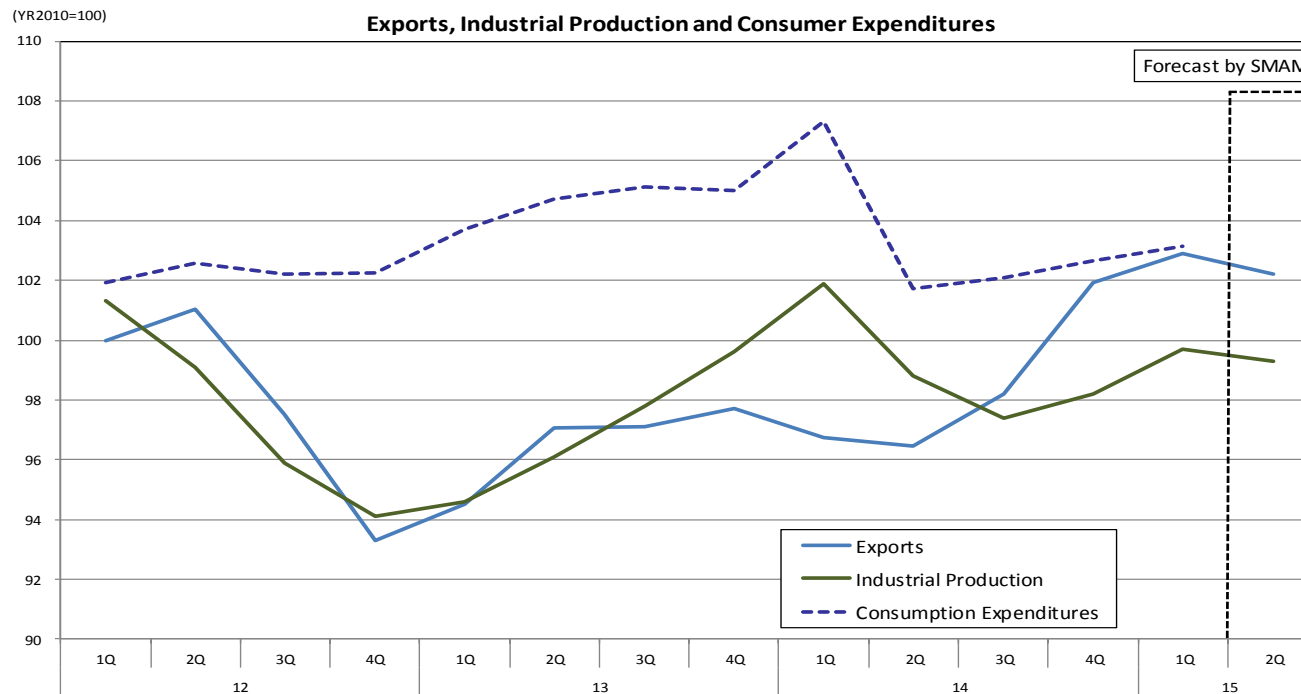
(Source) Cabinet Office, SMAM forecast

Notes: E=SMAM forecasts. SMAM views are as of June 17<sup>th</sup>, 2015 and subject to updates thereafter without notice

Source: Cabinet Office: Ministry of Economy, Trade and Industry, Ministry of Internal Affairs and Communications, SMAM forecasts. The above data is as of June 17<sup>th</sup>, 2015.

## Recovery Process: Exports⇒Production⇒Employment, Confidence⇒Consumption

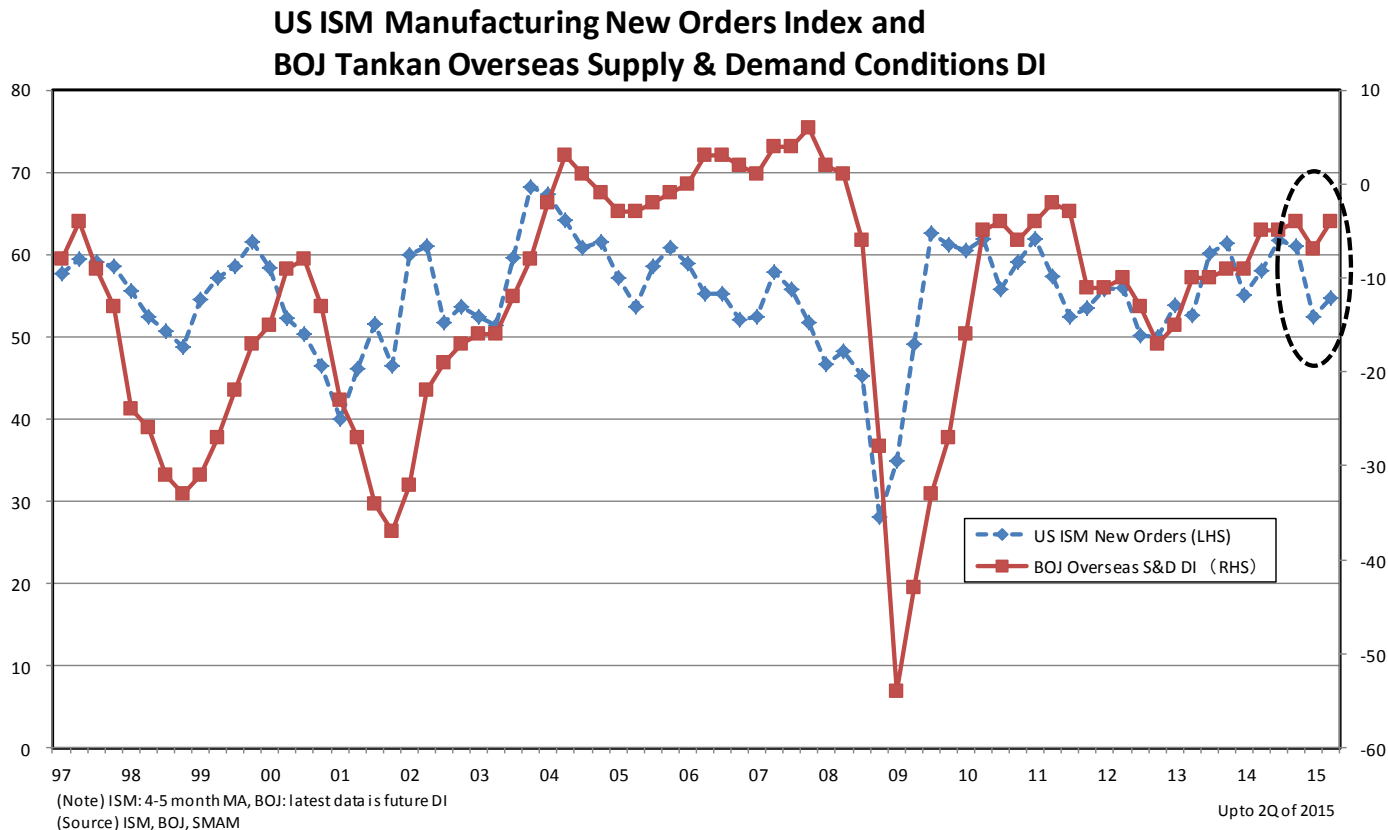
- SMAM forecasts current recovery process in order from Exports to Production and Consumption. The ongoing recovery is at the final stage of Consumption.
- Exports and Industrial Production continue stable growth, and Consumption is eventually picking up.
- SMAM expects Private Consumption Expenditures to recover from April-June quarter although current consumption data remain weak. Wealth effect by rising stock prices and real wages growth will push the Consumption higher.



(Source) Ministry of Economy, Trade and Industry, BOJ, Cabinet Office, SMAM's seasonally adjusted  
\*1: Industrial Production for 2Q 2015 is estimated based on the data of Industrial Production Forecast Index.

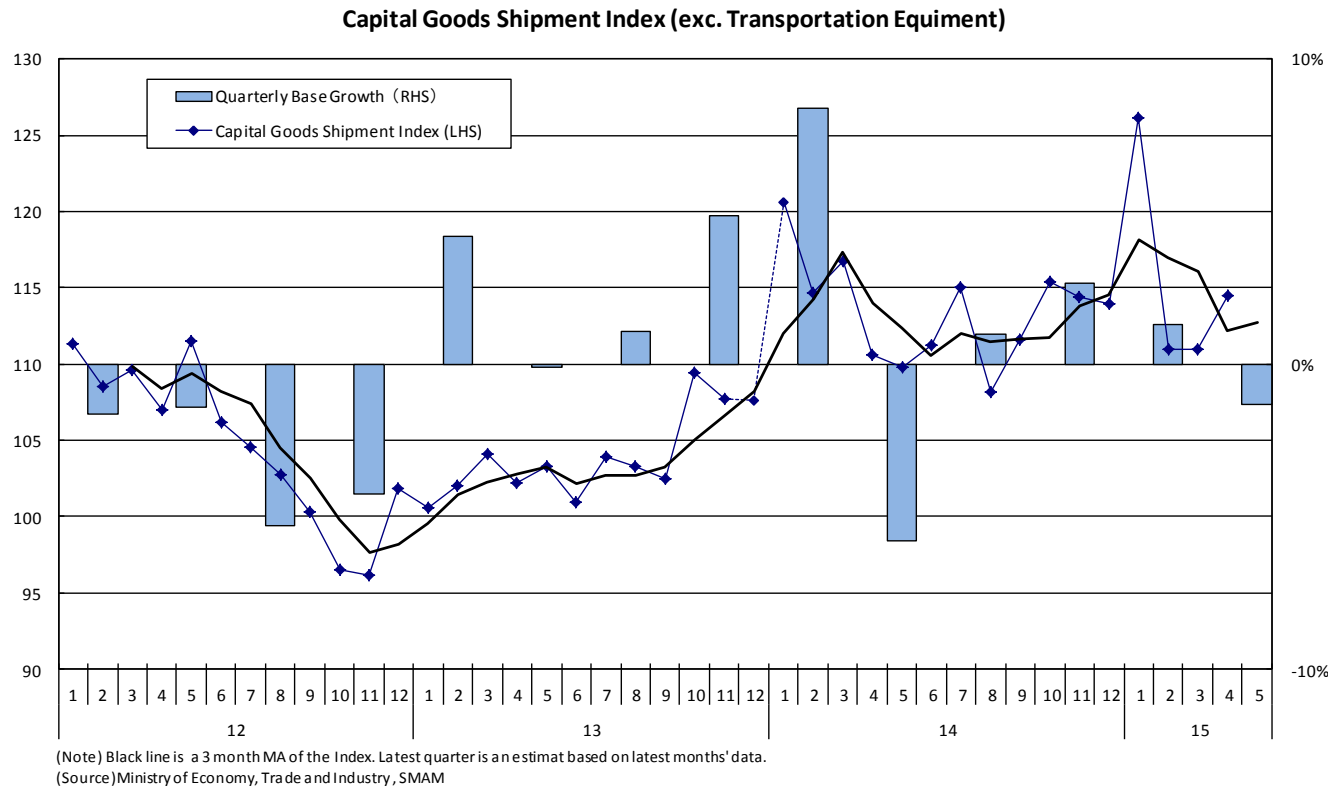
## Exports: Acceleration in July-September after a respite

- April-June Exports are likely to dip temporarily. April Exports slowed to +1.5% MoM hit by US West Coast Harbor strike. Exports will recover from July-September along with a mild US and global recovery.
- Japan's Exports tend to lag behind the US economy by a quarter period. Bank of Japan's Overseas Supply & Demand Condition Diffusion Index and US ISM Manufacturing New Orders Index show correlation. The both leading indicators improved in April-June quarter.



## Private Capital Investment: Moderate growth is expected

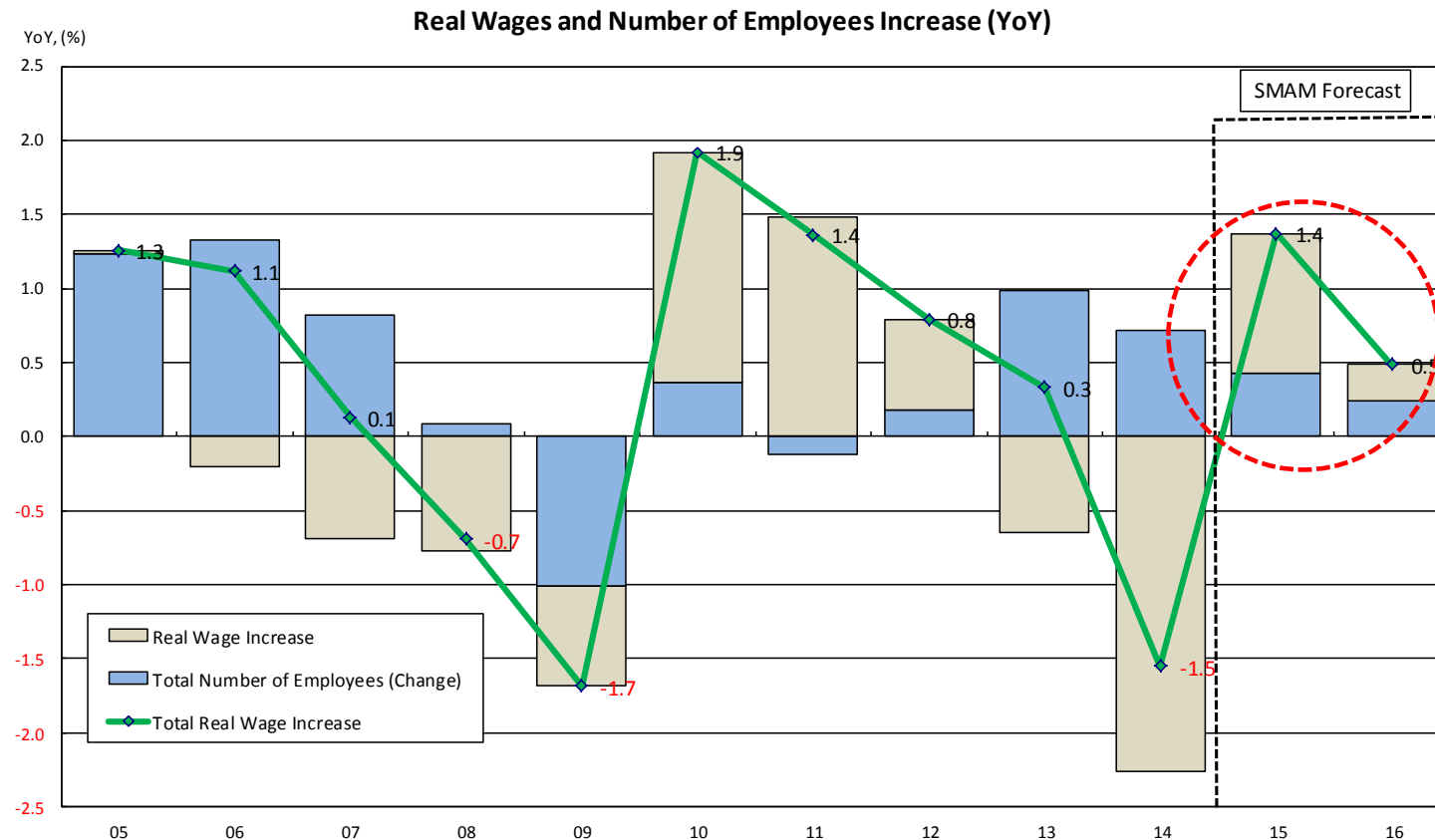
- Better than expected CAPEX related data came in. April Machinery Orders jumped +3.8% MoM after strong Private Capital Investment of +2.7% QoQ in January-March revised real GDP. However, SMAM maintains the forecast for CAPEX to grow at a moderate pace in a mid-to long term.
- CAPEX is likely to slowdown in April-June. April Capital goods shipment (excluding Transportation equipment) receded to -1.3% from January-March. SMAM expects Private Capital Investment to grow at +3.5% and +3.2% for FY2015 and FY2016 respectively.





## Wages: Real wages to grow FY2015

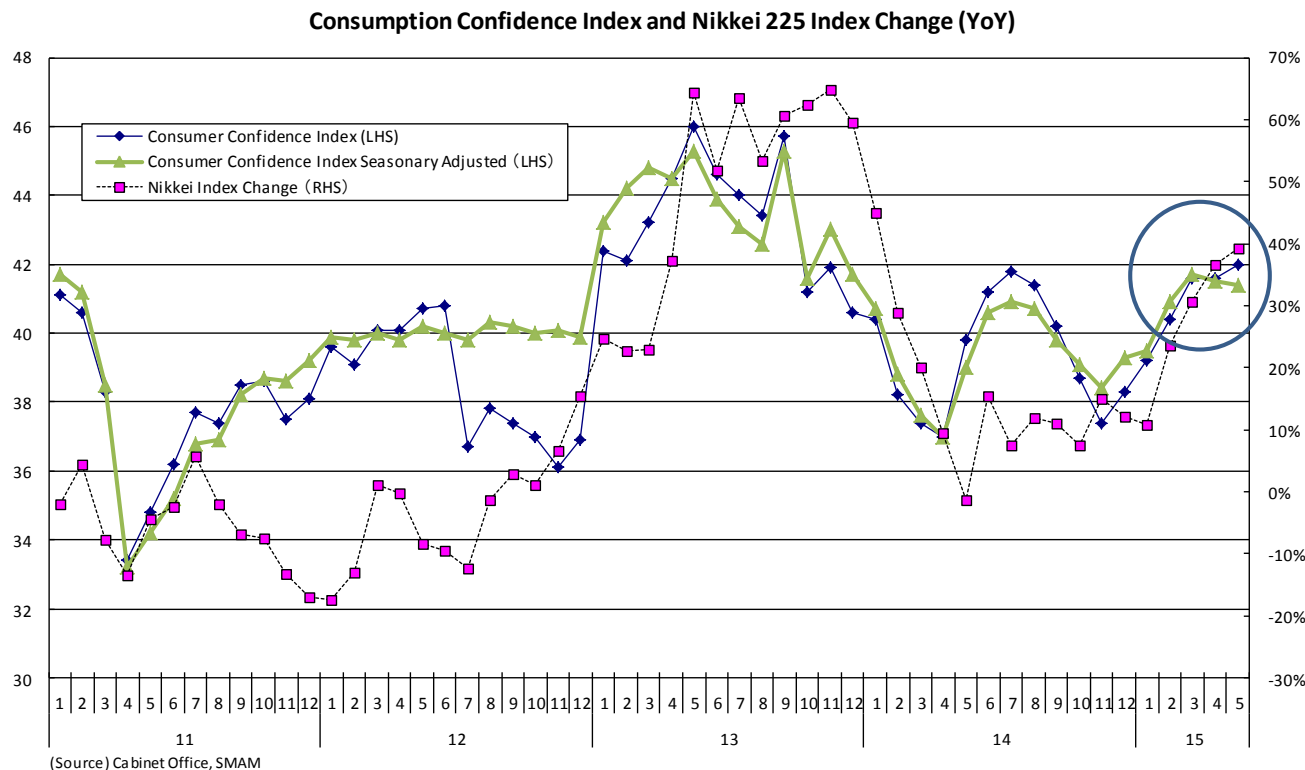
- April Real wages has turned positive on a YoY basis after a dip in FY2014. Nominal wages gained +0.9% YoY and CPI growth remained subdued in April.
- SMAM expects Real wages to grow +1.4% YoY in FY2015.



(Source) Cabinet Office, Ministry of Internal Affairs and Communications , Ministry of Health, Labour and Welfare , SMAM

## Private Consumption: Likely to start recovery in the middle of this year

- April Retail sales were up +5.0% YoY and New car sales in May inched up +1.2% YoY. Private Consumption has not fully recovered yet.
- SMAM expects Consumption to accelerate from June as Nominal wages gain for the FY reflects usually in this season. Wealth effects on higher stock prices will also boost the Consumption. Consumer Confidence Index and Change in Nikkei Index have moved together.



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# Outlook for Japanese Stock Markets

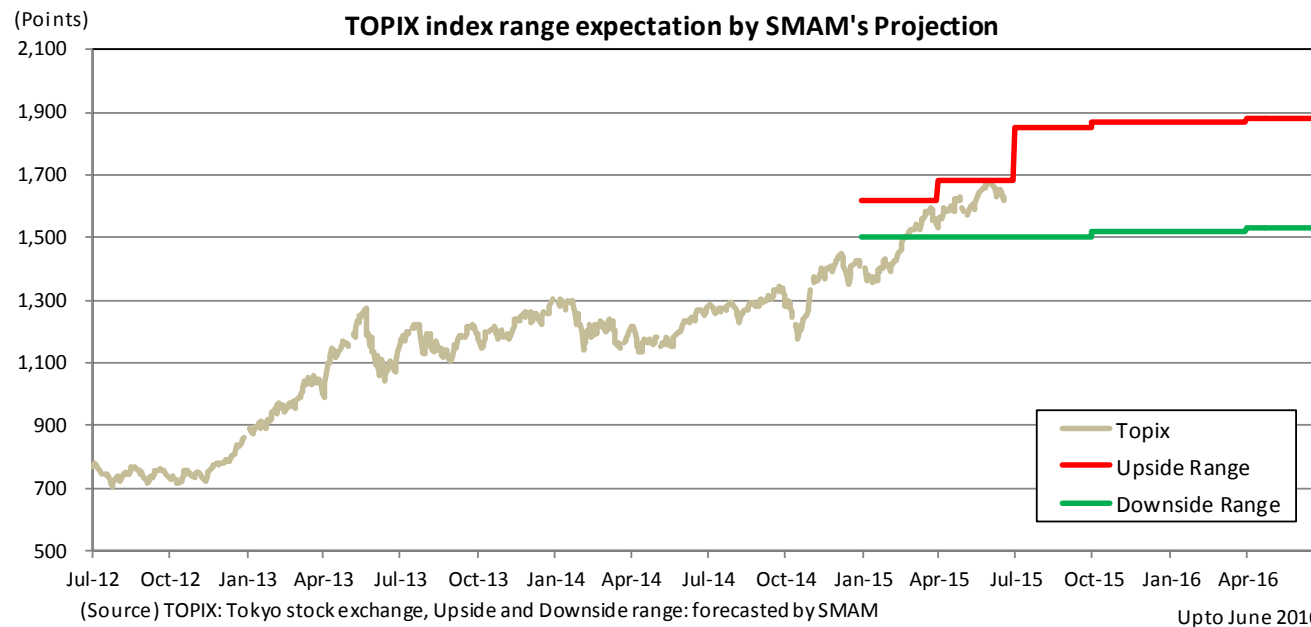
## Stock market outlook: Earnings growth prospects should help the stock market

### SMAM short-term view

- In addition to moderate growth in Production and Exports, Consumption recovery would lift the macro economy. Corporate earnings are expected to continue double digit growth in FY2015.
- The stock market is expected to keep advancing as Japan's reflation policy is very likely to continue until next consumption tax hike in 2017. Increasing expectation for dovish US rate hike should also support the market.

### Longer-term outlook (6-months and beyond)

- For longer-term, we continue to expect the market to track on a modest uptrend, underpinned by US-led global growth, solid corporate earnings and strengthened reflationary policies in Japan. Investors are more likely to focus on earnings upward revision after April-June company reports.



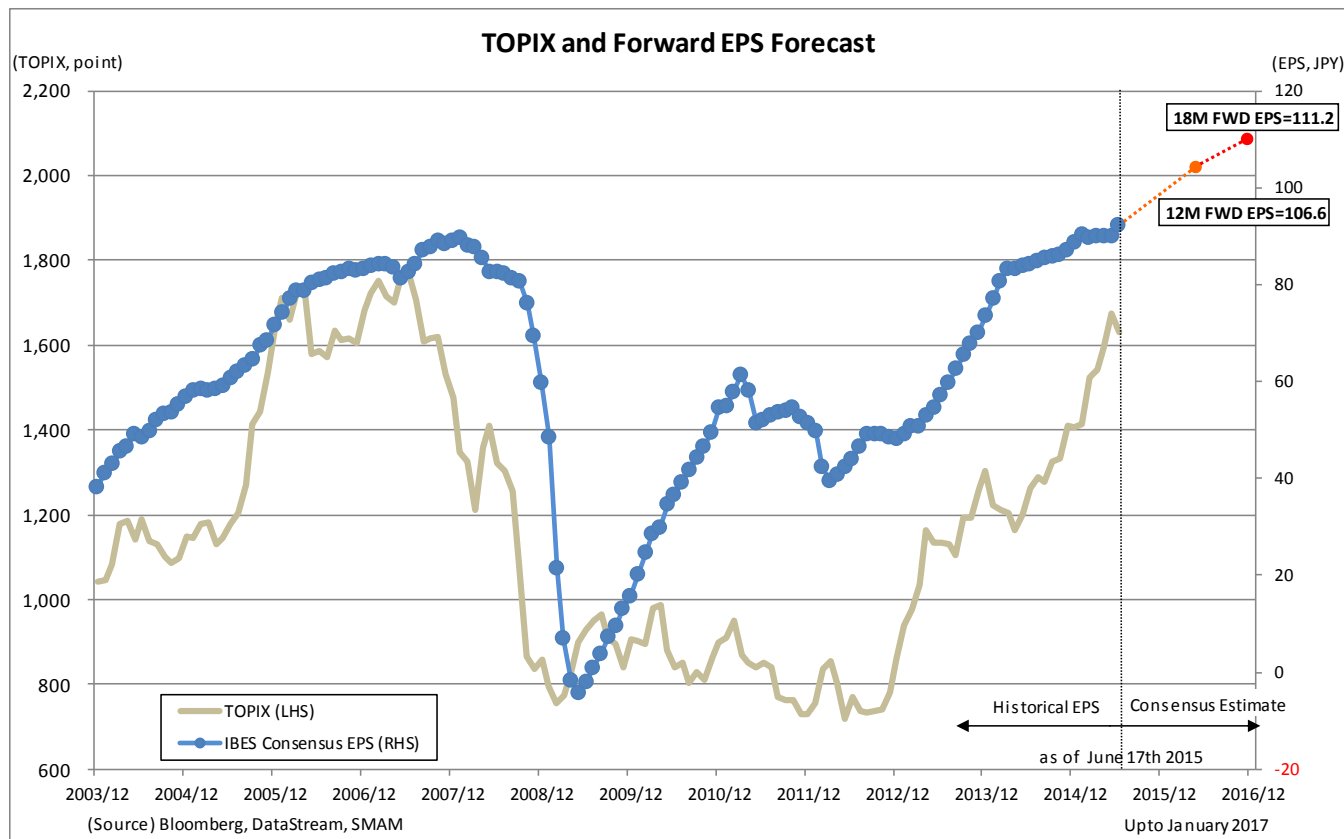
## Base scenario & Upside / Downside risks for our forecasts

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- Our **Base Scenario** is assuming the following views:
  - Global economic recovery to be sustained led by strong US economy
  - Japan's mild recovery from tax-hit weak demand buoyed by higher real wages growth
  - Growing expectation for positive corporate earnings revisions due to weaker JPY
  - Reflationary policy to be continued toward the next consumption tax hike
  
- **Upside Risks** include:
  - Stronger-than-expected global growth
  - Stronger-than-expected measures by Abe government
  
- **Downside Risks** include:
  - Slowdown in global economy
  - Concern over global deflation
  - Increasing geopolitical concerns

## TOPIX / EPS forecast: fairly valued on upbeat forward EPS

- IBES consensus EPS continues rising supported by solid growth prospects. IBES 12 month and 18 month forward EPS are JPY106.6 and JPY111.2 respectively, while TOPIX EPS is currently JPY92.09 as of June 17<sup>th</sup>.
- TOPIX of 1,633.70 as of June 17<sup>th</sup> seems fairly valued as the current P/E's are 14.7x and 15.3x based on the IBES 18 month and 12 month forward EPS forecasts.



## Corporate earnings 1: +18% profit growth forecast in FY2015

- The recurring profits in FY2015 are expected to increase by +18.4% YoY for SMAM core research universe (216 companies). SMAM assumes exchange rates of USD/JPY=120 and EUR/JPY=135 for FY2015. Considering further appreciating USD/JPY to 125, the recurring profits will grow to +20% YoY for the fiscal year.
- On the company guidance (forecasts by company reports), the recurring profits for FY2015 are forecasted to grow by +10.5%, lower than our forecasts, as the guidance of many companies stay conservative and are based on lower USD/JPY of 115 (median USD/JPY=117). The upward revision of profits is very likely unless USD/JPY move lower substantially from the current level.

SMAM Core-Research Companies Earnings Forecasts (excl. Financials) as of June 9th 2015

(JPY billion)

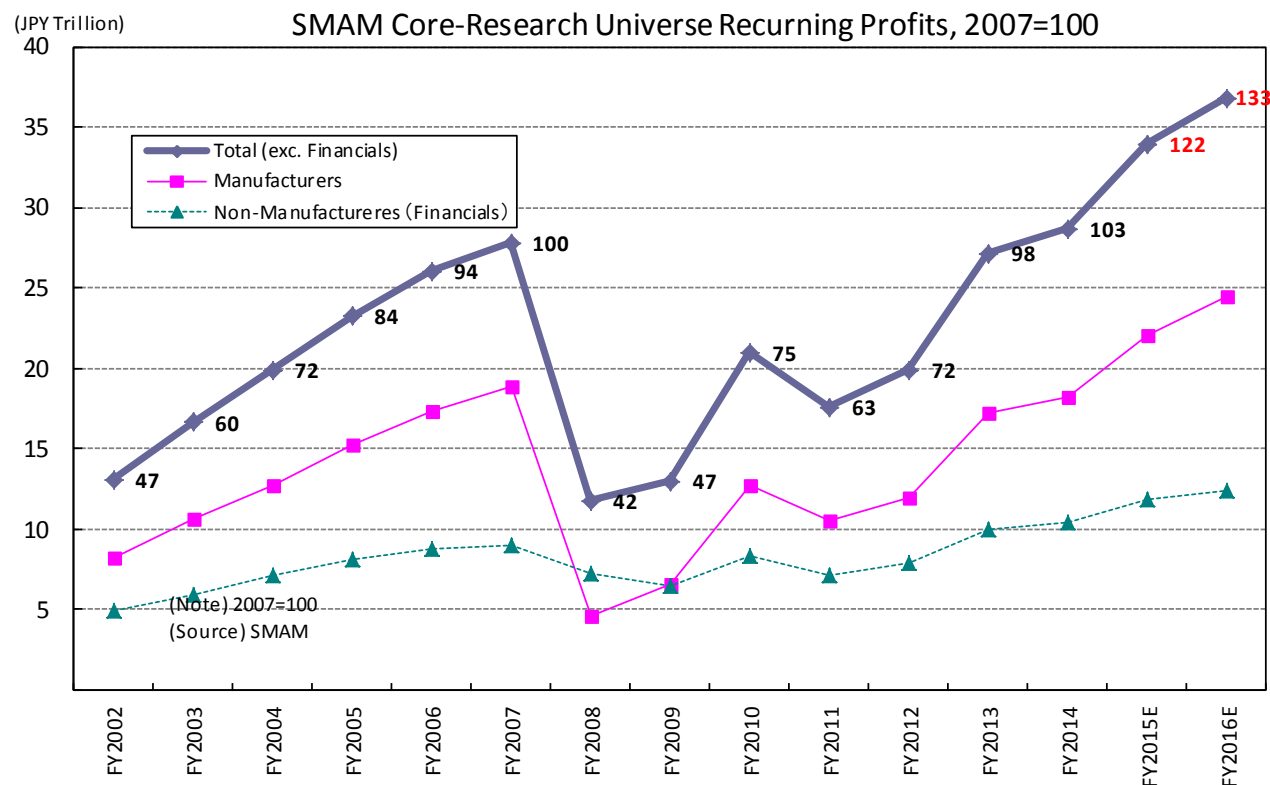
	FY	Sales	YoY	Operating Profit	YoY	Recurring Profit	YoY	Net Profit	YoY
Total (exc. Financials)	FY2013	388,016	3.5%	26,258	6.8%	27,142	9.9%	16,433	28.0%
【216 companies】	FY2014	403,141	3.9%	27,326	4.1%	28,651	5.6%	17,746	8.0%
	FY2015E	412,303	2.3%	32,850	20.2%	33,929	18.4%	21,421	20.7%
	FY2016E	426,128	3.4%	35,497	8.1%	36,822	8.5%	23,348	9.0%
Manufacturers	FY2013	245,501	4.1%	16,770	10.5%	17,166	13.4%	10,303	41.1%
【135 companies】	FY2014	254,515	3.7%	17,571	4.8%	18,214	6.1%	11,488	11.5%
	FY2015E	262,349	3.1%	21,461	22.1%	22,084	21.3%	13,841	20.5%
	FY2016E	271,439	3.5%	23,745	10.6%	24,434	10.6%	15,431	11.5%
Non-Manufacturers	FY2013	142,515	2.7%	9,488	0.9%	9,975	4.8%	6,130	11.9%
【81 companies】	FY2014	148,627	4.3%	9,754	2.8%	10,437	4.6%	6,258	2.1%
	FY2015E	149,954	0.9%	11,389	16.8%	11,845	13.5%	7,581	21.1%
	FY2016E	154,689	3.2%	11,751	3.2%	12,388	4.6%	7,917	4.4%

(Note) Companies in universe were partially replaced.

(Source) SMAM

## Corporate earnings 2: +33% higher profits in FY2016 than historical high in FY2007

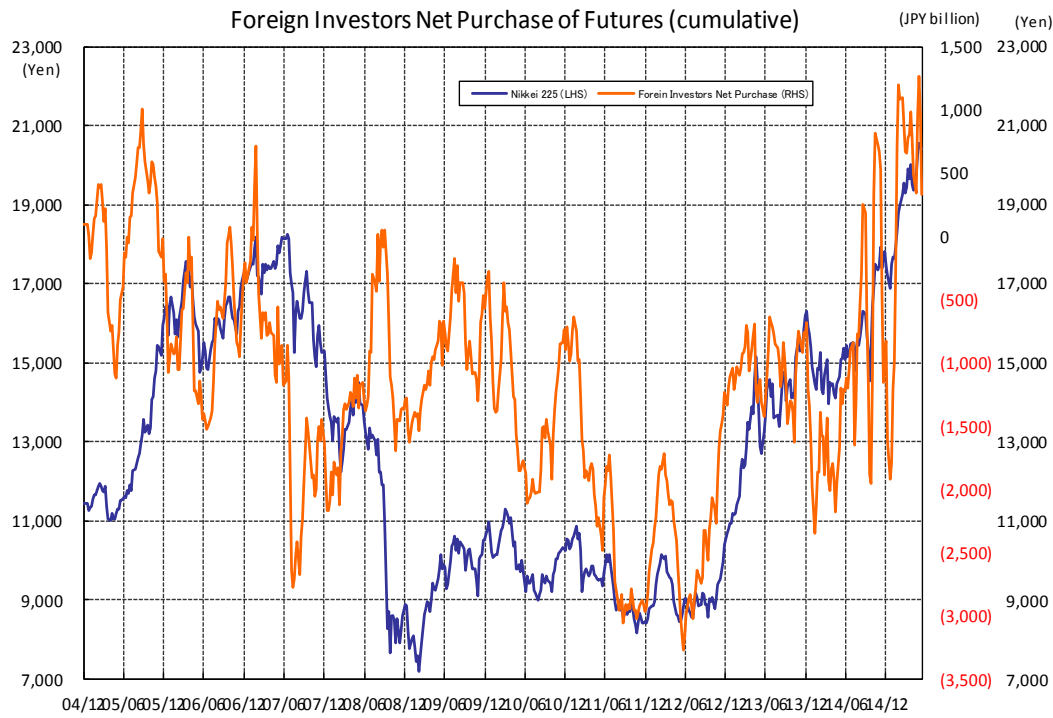
- For FY2016, the recurring profits are expected to continue to grow by +8.5% YoY for SMAM core research universe (216 companies).
- Provided the recurring profits for FY2007 are set at 100, the profits are expected to keep growing to 122 and 133 for FY2015 and FY2016 after renewing the record highs in FY2014.





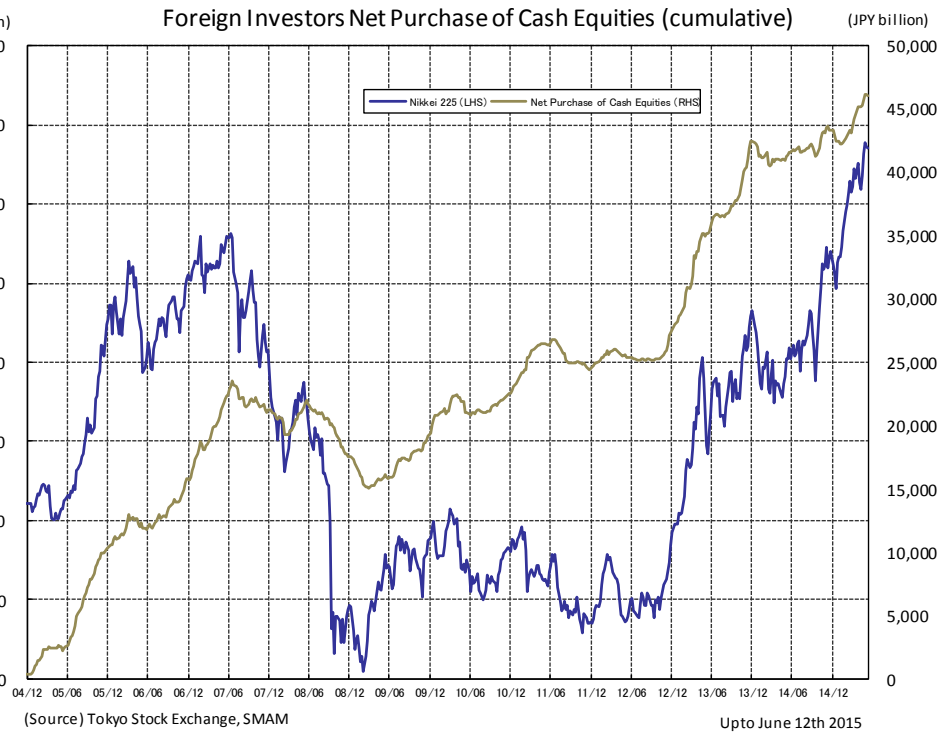
# Supply-Demand balance: Net-long position maintained by overseas investors

- Overseas investors are accumulating net long positions. The cumulative basis total purchase for futures and cash equities for this year (from January 1<sup>st</sup> week to June 2<sup>nd</sup> week) reached JPY6,227 billion and JPY2,697 billion respectively.
- On a futures transaction, the investors took profits in the 1<sup>st</sup> and 2<sup>nd</sup> week in June after aggressively buying in the 3<sup>rd</sup> and 4<sup>th</sup> week in May. On a cash equities transaction, they also took profits in the 2<sup>nd</sup> week in June after a strong buying in the 3<sup>rd</sup> week in May.



(Source) Tokyo Stock Exchange, SMAM

Upto June 12th 2015



(Source) Tokyo Stock Exchange, SMAM

Upto June 12th 2015

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