

# Japanese Stock Market Outlook

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SMAM monthly comments & views  
- October 2015 -



Sumitomo Mitsui Asset Management

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## Executive summary

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### ➤ Japanese Economy

Japanese economy was dragged by stalling private consumption and exports though extremely rainy weather is partly blamed for the consumption. Counter measures are expected by the Japanese government and possibly by BOJ as well.

- SMAM cut real GDP forecast from +0.9% to +0.7% for FY2015 and forecast for Sep-Dec quarter was revised from +1.3% to -0.3% thereafter recovering to +0.2% in Jan-Mar 2016.

### ➤ Japanese Stock Markets

Current economic weakness spilling over from China and uncertain US interest rates would linger for a while until positive policy actions are taken by governments and central banks. Underlying corporate earnings are still strong even considering some possible erosion, which should support the Japanese stock market, which is at the lower end of the historical PER range.

- Strong US economy is basically positive. Current uncertainties would be gradually cleared if necessary economic measures are taken globally, which would bring global investors to risk-on mode again.

Notes: Macro and market views are as of September 16<sup>th</sup> and 17<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 cut real GDP forecast from +0.9% to +0.7% for FY2015 and forecast for Sep-Dec quarter was revised from +1.3% to -0.3% thereafter recovering to +0.2% in Jan-Mar 2016.
- Slowing Net Exports and Private Consumption are the main cause though extremely rainy weather has probably dragged the latter temporarily.

	FY12	FY13	FY14	FY15E	FY16E
Real GDP growth	1.0%	2.1%	-0.9%	0.7%	1.1%
Private Consumption Expenditure	1.8%	2.5%	-3.1%	0.1%	1.8%
Private Housing Investment	5.7%	9.3%	-11.7%	2.9%	4.3%
Private Capital Investment	1.2%	4.0%	0.5%	1.6%	2.6%
Public Consumption Expenditure	1.5%	1.6%	0.4%	1.1%	0.4%
Public Capital Investment	1.0%	10.3%	2.0%	1.0%	-0.1%
Net Exports (contrib. to GDP growth)	-0.8%	-0.5%	0.6%	-0.2%	-0.2%
Exports	-1.4%	4.4%	7.9%	-0.7%	2.5%
Imports	3.6%	6.7%	3.6%	0.6%	4.2%
Nominal GDP	0.1%	1.8%	1.6%	1.7%	1.9%
GDP Deflator	-0.9%	-0.3%	2.5%	1.0%	0.8%

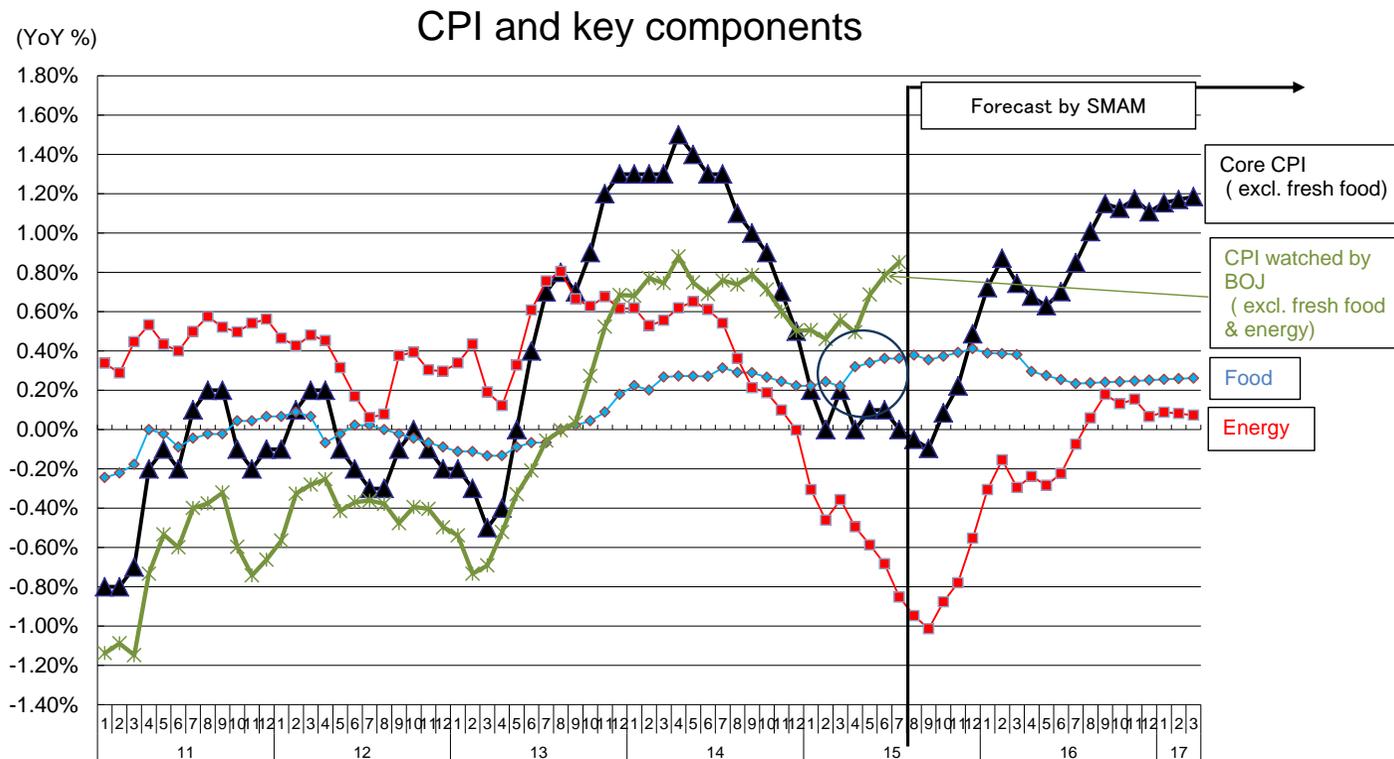
Notes: E=SMAM forecasts. SMAM views are as of Sep 16<sup>th</sup>, 2015 and subject to updates thereafter without notice

(%, YoY except Net Exports)

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

## Price increase in food and other essential items are probably affecting consumer sentiment

- Although overall CPI is hovering around zero due to lower energy prices, weak yen is lifting import prices, which leads to higher prices of food and other essential items as a circle shows in the chart.
- Lower energy prices are helping companies, however, the benefit has not yet reached consumers who are feeling higher cost of living.

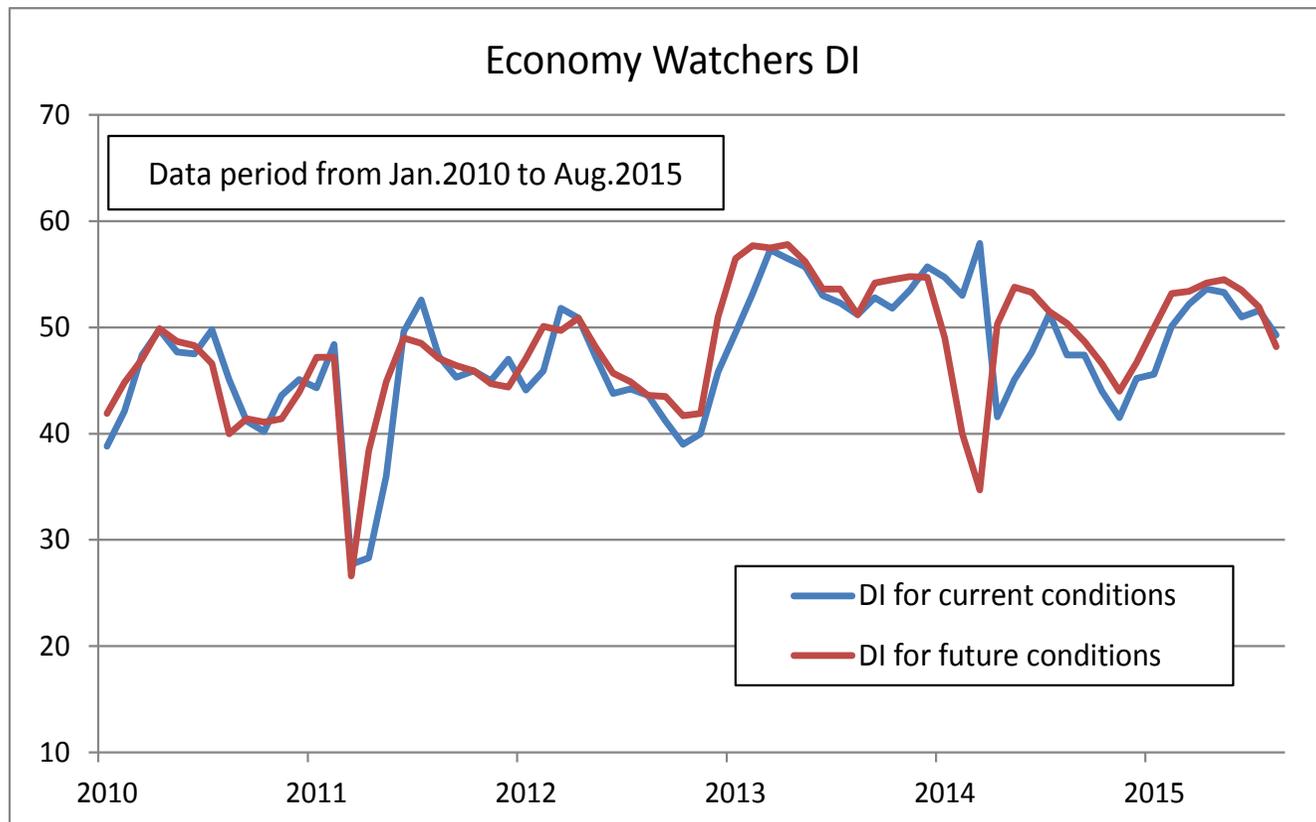


Note: Excluding direct impact from consumption tax hike in April 2014.

(Source) Ministry of Internal Affairs & Communications, forecast by SMAM.

## Consumer sentiment was hit by global uncertainties and declining stock prices

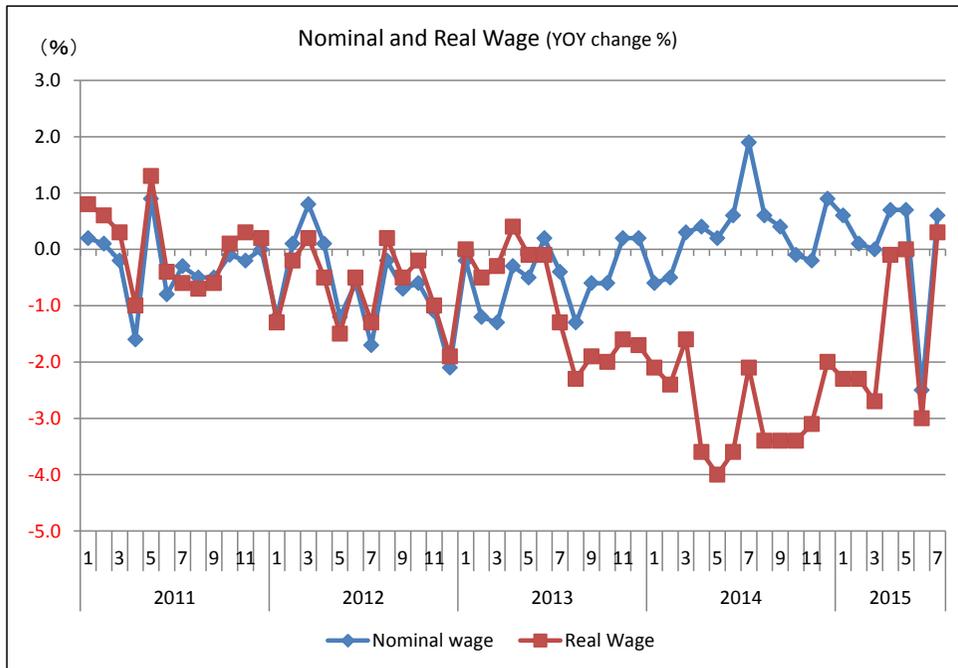
- Economy watchers DI dipped below threshold 50 level both for the current conditions and future conditions, which indicate the surveyed people were feeling the deteriorating living conditions.
- The survey was made in late August when global stock markets were already declining, which probably was one of the reasons behind this decline.



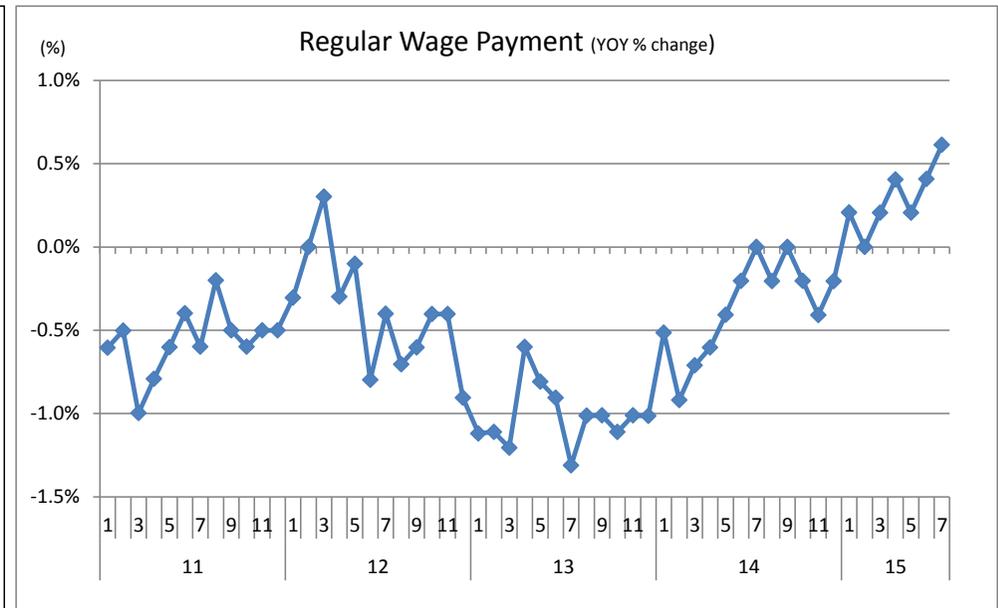
(Source) Cabinet Office

## Positive real wage is one of the bright spots though higher increase is necessary

- Real wage in July increased by +0.3% YOY for the first time after +0.4% achieved in Apr. 2013.
- Nominal regular wage payment or basic salary has been rising and accelerating for 2015 so far.



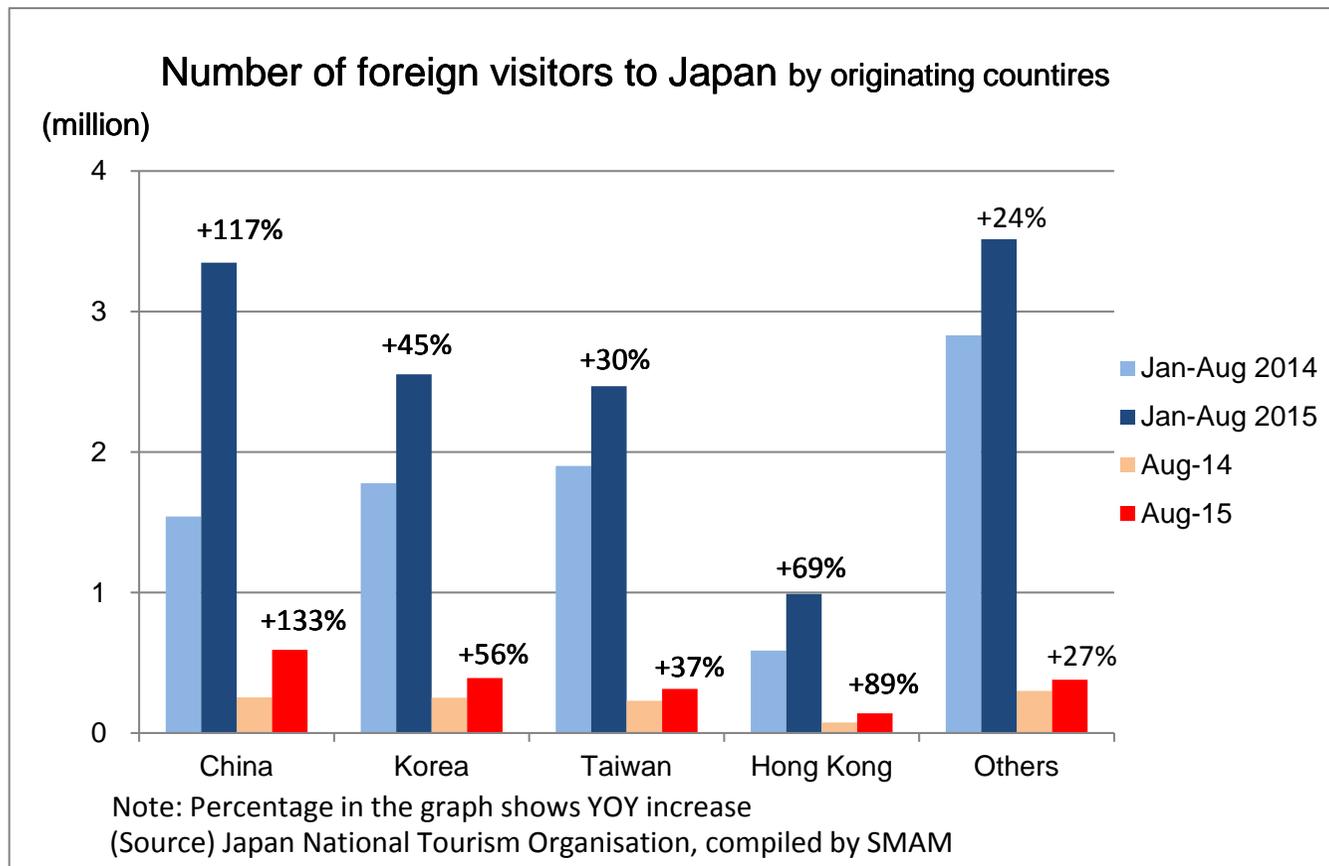
(Source) Ministry of Health, Labor and Welfare.



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## Economic problem in China has not yet visible in tourism

- Number of tourists from China was up +133% in August YOY, more than doubled, which shows no sign of negative effects yet from weak economy and stock markets in China, which might show Chinese consumers are still robust.



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# Outlook for Japanese Stock Markets

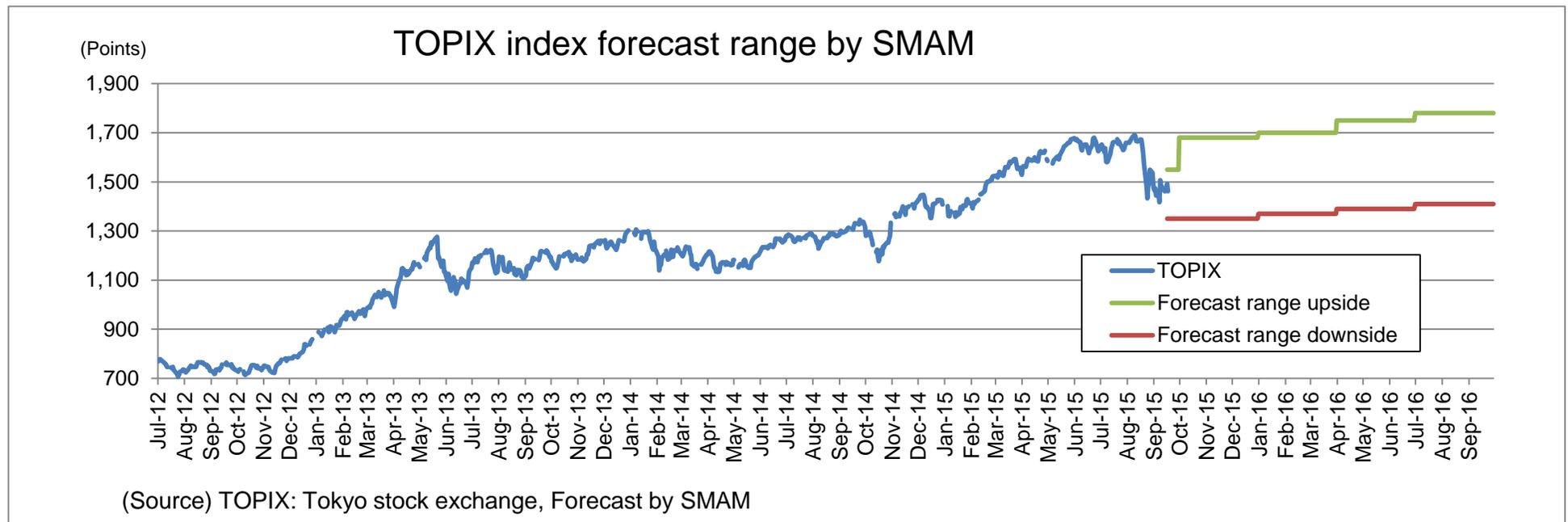
## Stock market outlook: Earnings growth prospects should help the stock market

### SMAM short-term view

- Current economic weakness spilling over from China and uncertain US interest rates would linger for a while until positive policy actions are taken by governments and central banks.

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

- Underlying corporate earnings are still strong even considering some possible erosion, which should support the Japanese stock market, which is at the lower end of the historical PER range.
- Strong US economy is basically positive. Current uncertainties would be gradually cleared if necessary economic measures are taken globally, which would bring global investors to risk-on mode again.



Note: SMAM's Projection is as of September 17th, 2015 and subject to updates without notice

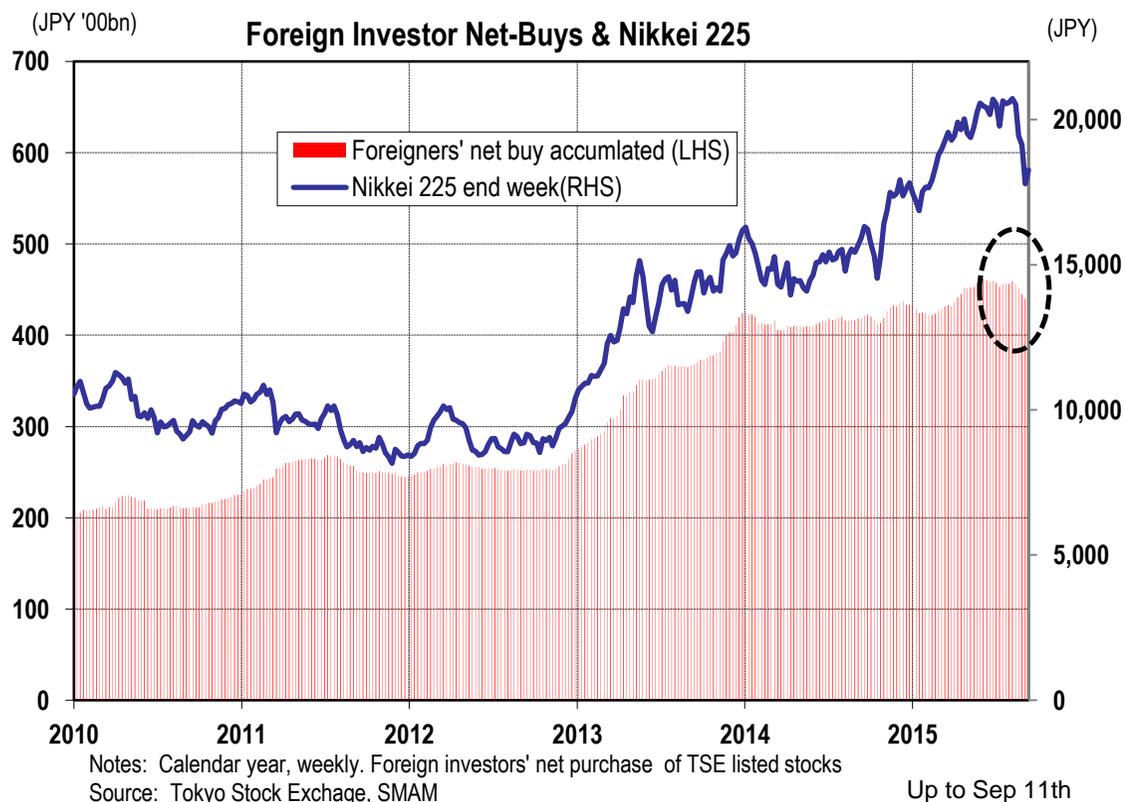
## Base scenario & Upside / Downside risks for our forecasts

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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 private consumption to grow though mildly supported 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:
  - Unexpectedly large impact from the process of US monetary policy normalization
  - Concern over emerging economies including China
  - Increasing geopolitical concerns

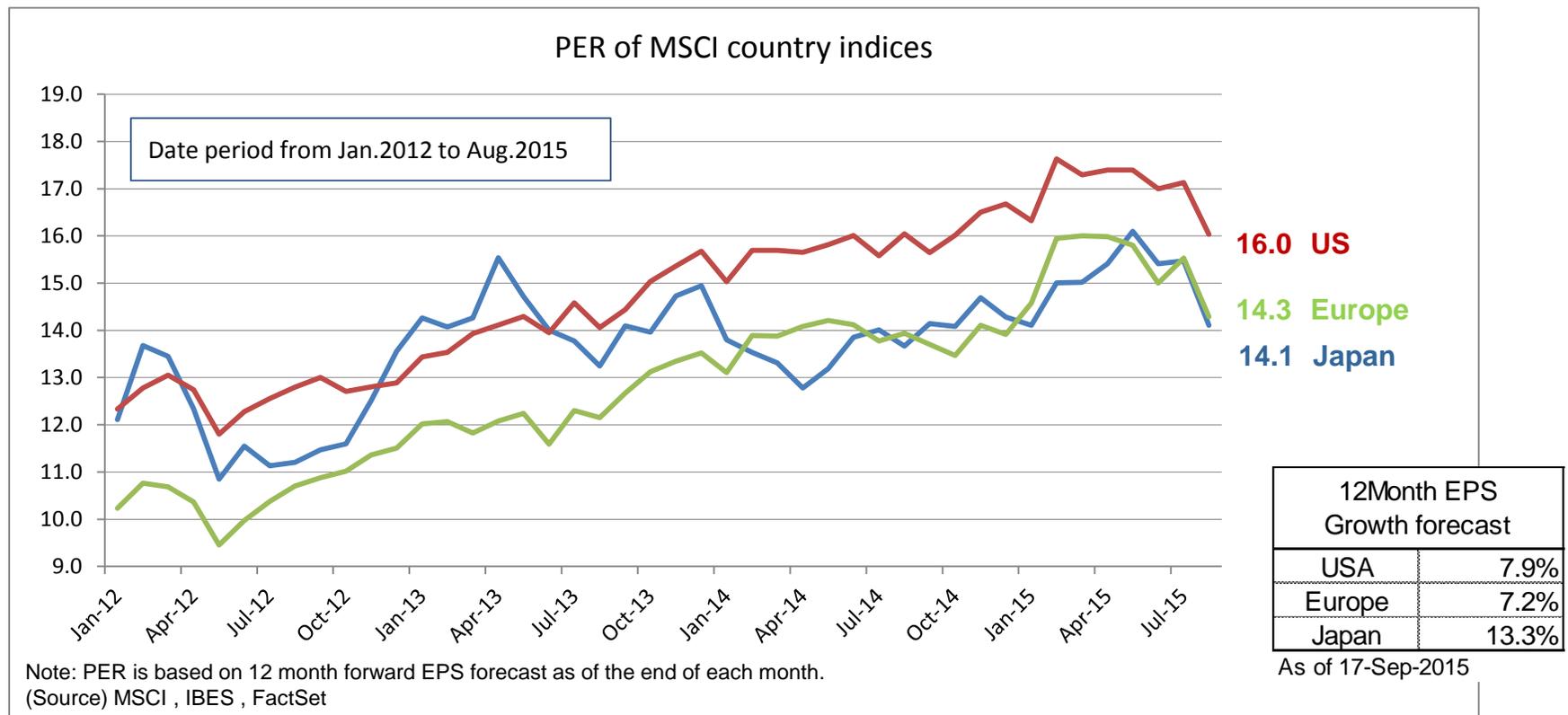
## Supply-Demand balance: Foreign investors shifted risk-off

- Foreign investors sold 2.9 trillion yen Japanese equities in 5 weeks from August 10th to September 11th reflecting risk-off mode spreading globally whereas domestic investors both institutional and individuals were buying on weakness.
- Japan Post is going to be listed on the stock exchange on November 4th, for which good appetite from individual investors is expected if high dividend yield and low PBR is realized as currently assumed.



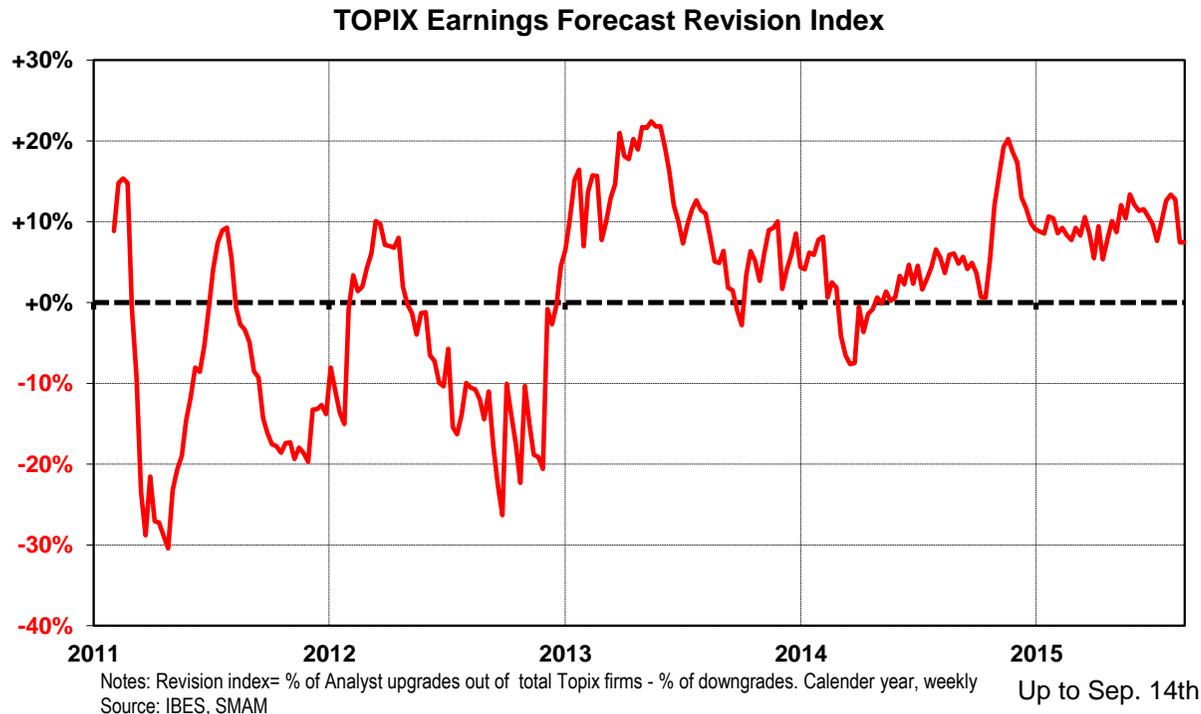
## Japanese stock market valuation came down to lower end of the historical range

- Reflecting further fall in share prices in September, PER based on 12M forward EPS fell to 13's times for MSCI Japan. This is at lower end of the historical PER range for Japanese stocks since Abenomics started in early 2013.
- 12M earnings growth forecast is comparatively high for MSCI Japan at 13.3% compared to 7.9% and 7.2% for USA and Europe respectively.



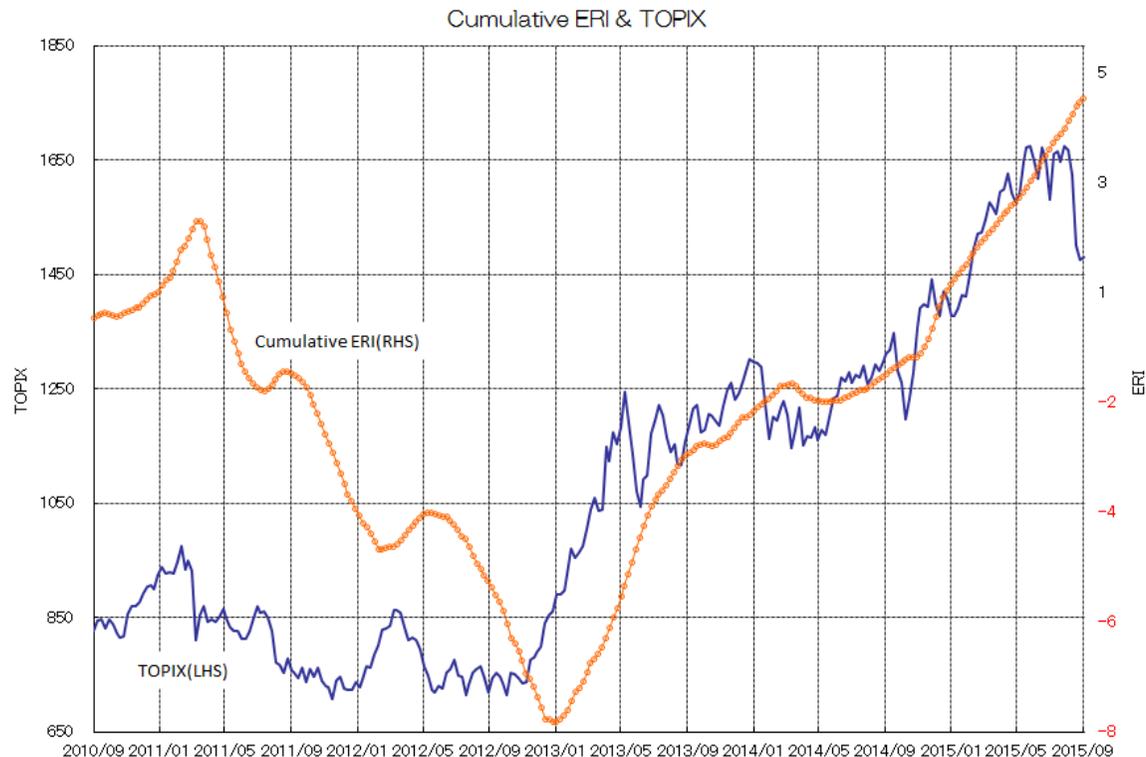
## Earnings forecast for Japanese companies are holding well so far

- Corporate earnings forecast by analysts continues to be revised upward.
- As of September 15<sup>th</sup>, IBES historical EPS for TOPIX was 96.805. 12M forward and 18M forward EPS forecasts were 110 and 114.662, which corresponded to 13.6% and 18.4% EPS growth respectively.



## Recent correction in Japanese stock market could be overdone if earnings sustains

- Earnings Revision Index(ERI) is accumulated to be compared with the move of TOPIX here. Historically, the stock market tends to lead the ERI.
- Even in the historical terms, current downward deviation of TOPIX might be overshoot, though ERI is likely to come down.



(Source) IBES, Tokyo Stock Exchange, compiled by SMAM

## Economy will return to the central agenda for the government

- Controversial National Security Law amendment has passed the National Diet. Economy will return to the central agenda for the government preparing for the Upper House election scheduled in July 2016.
- BOJ could make further monetary easing if economic situation deteriorates seriously. FOMC meetings in the U.S. are going to be closely watched if and when interest rates are raised.

2015 Political & Economic Calendar

Sep.	26th	PM Abe attends the United Nations General Assembly
	27th	End of the National Diet Ordinary Session
Oct.	1st	BOJ "Tankan" Survey
	6-7th	BOJ Monetary Policy Committee Meeting
	27-28th	FOMC meeting in the U.S.
	30th	BOJ Monetary Policy Committee Meeting and "Economy & Inflation Perspective Report" is released
	During the month	Reshuffle of the Cabinet Members and LDP Executives National Diet Extraordinary Session begins Public and Private Dialogue for Enhancing Virtuous Cycle in the Economy
Nov.	4th	Japan Post Listing on TSE
	15-16th	G20
	16th	First Preliminary GDP for Jul-Sep 2015
	18-19th	BOJ Monetary Policy Committee Meeting
	18-19th	APEC Summit Meeting
Dec.	15-16th	FOMC meeting in the U.S.
	17-18th	BOJ Monetary Policy Committee Meeting
	During the month	Proposal of the budgetary plan for FY2016 FY2016 budgetary plan, approval by the Cabinet Outline of the 2016 Tax Reform Proposals, approval by the Cabinet

(Source) SMAM based on various materials

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