

Impact of US's Yen devaluation claim on the Japanese equity

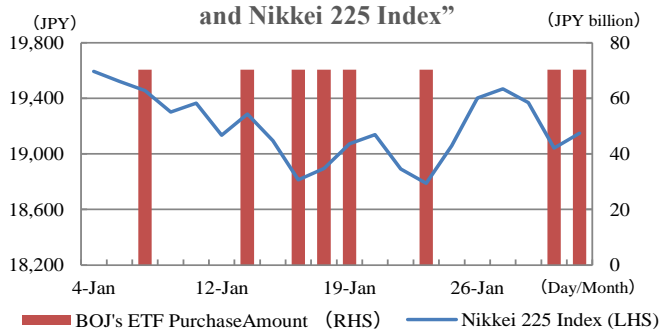
- Financial markets kept relatively calm against US President Donald Trump's statement on exchange rate policy as it was not representing the basic policy of US government.
- Japanese equity was supported by (i) generally positive corporate performance, (ii) ETF purchase by BOJ and (iii) ongoing monetary policies of both US and Japan.
- Japanese equity market is likely to remain unstable responding to US President Trump's statements and actions for the time being. Focus will be on details of US economic policies and their effectiveness.

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On 31st January 2017, US President Trump criticized exchange rate policies of Japan and China accusing both countries are devaluating their currencies. With this statement, JPY strengthened temporarily against USD to 112.08 during New York time zone on the same day. Later on, USD/JPY rate continued to trade sideways around 113 yen. Meanwhile, Nikkei 225 Index rose on 1st February 2017 from the day before and closed weak on 2nd February 2017.

It appears that JPY did not appreciate sharply and Japanese equity did not fall sharply immediately after the Trump's statement. To begin with, the statement was made during the course of discussion with US pharmaceutical companies over (i) drug price reduction and (ii) expansion of manufacturing capacity in the US. It was not intended to be announced as the US government's basic policy on exchange policy. Hence, the market did not largely react, and kept relatively calm.

“Chart 1: BOJ's ETF Purchase Amount and Nikkei 225 Index”



(Note) Data period is from 4th January 2017 to 1st February 2017.
Amount of ETF excludes “ETFs to Support Firms Proactively Investing in Physical and Human Capital”.

(Source) SMAM, based on Bloomberg L. P. data.

“Table 1: Timetable of Trump Administration”

Timetable		Events
Feb.	10th	Japan-US Summit
	28th	Speech of US President Trump at joint meeting of US Congress
Mar.	Early Part	Budget Message
Mar.	15th	Deadline of raising the US's debt ceiling
Apr.	15th	Deadline of budget resolution
	15th	Report to Congress on international economic and exchange rate policies
	30th	100 days from US President Trump's inauguration

(Source) SMAM, based on publicly available material.

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We can find other reasons to explain why Japanese equity market did not fall sharply. Currently in Japan, it is the company results announcement season of October - December 2016 quarter of companies that end their fiscal year in March. We believe that (i) progress of JPY depreciation and recovery of commodity market after the US presidential election and (ii) cyclical recovery of emerging market economy have led to upward revision of full-fiscal-year earnings estimates in some cases, and this underpinned Japanese equities. In addition, BOJ purchased ETFs every day from 30th January through 1st February (Chart 1) . We believe that this also dispelled uncertainty over price fall of Japanese stocks.

Meanwhile, BOJ decided to maintain current monetary policy at Monetary Policy Meeting held on 30th and 31st January and Federal Reserve Board (FRB) also decided to maintain current monetary policy at Federal Open Market Committee on 31st January and 1st February. Financial markets were stable as both decisions were in line with market expectations. However, at present, continuation of accommodative monetary policy by BOJ and FRB's policy to raise interest rates at a moderate pace seems to bode well with Japanese equity.

Japanese equity market is likely to remain unstable responding to US President Trump's statements and actions for the time being. Focus will be on details of US economic policies and their effectiveness

However, both Japanese equity and USD/JPY rate are likely to remain volatile responding to US President Trump's statements and actions for the time being. Immediate important event is an upcoming Japan-US Summit scheduled on 10th February 2017 (Table 1). Regarding this event, the market will focus on (i) any specific demand relating to auto trading from US or not and (ii) any reference to USD/JPY exchange rate or not. There could be a fear that financial markets might react to sharp JPY appreciation and Japanese equity fall, if there is any criticism made on devaluation of JPY by US President Trump, as we believe impact on the financial markets is incomparable to that of the statement made towards US pharmaceutical companies on 31st January 2017.

Also, US President Trump is slated to speak at the joint meeting of US Congress on 28th February 2017 and announce the outline of policy management. Because of this, Budget Message (presentation of draft of budget for next fiscal year by US President Trump to US Congress) is expected to be postponed to March. Finally, details of economic policies will become clear after these events. As we believe effectiveness of US economic policies will have a large impact on Japanese equity, the key will be cooperative relationship between US President and US Congress.

*** Please note that this report is a translation of Japanese report written on 2nd February, 2017.**

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