



# Outlook for Japanese Stock Market & Economy

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-May 2024-



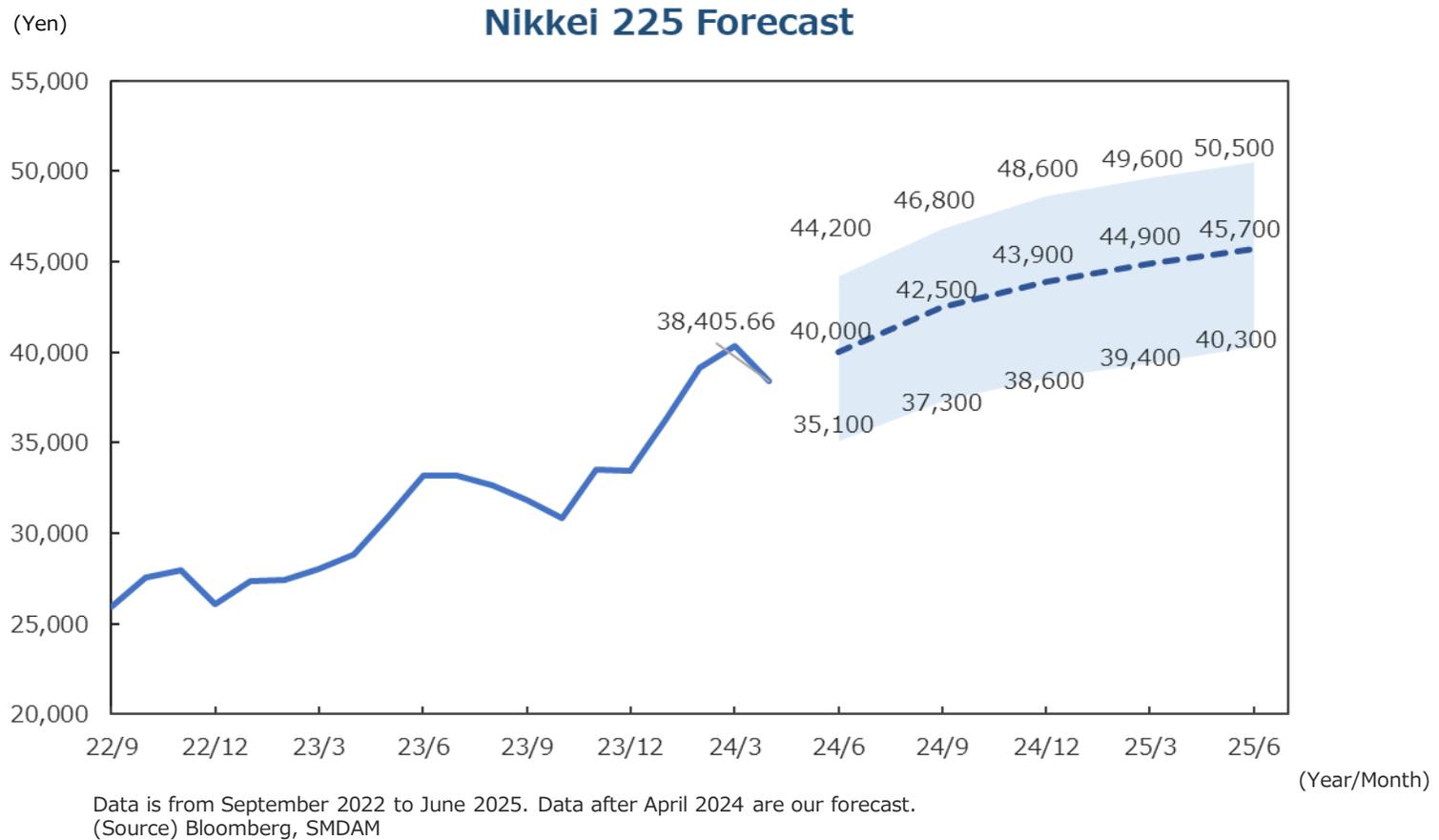
# Outlook for Japanese Stock Market

## Market Outlook

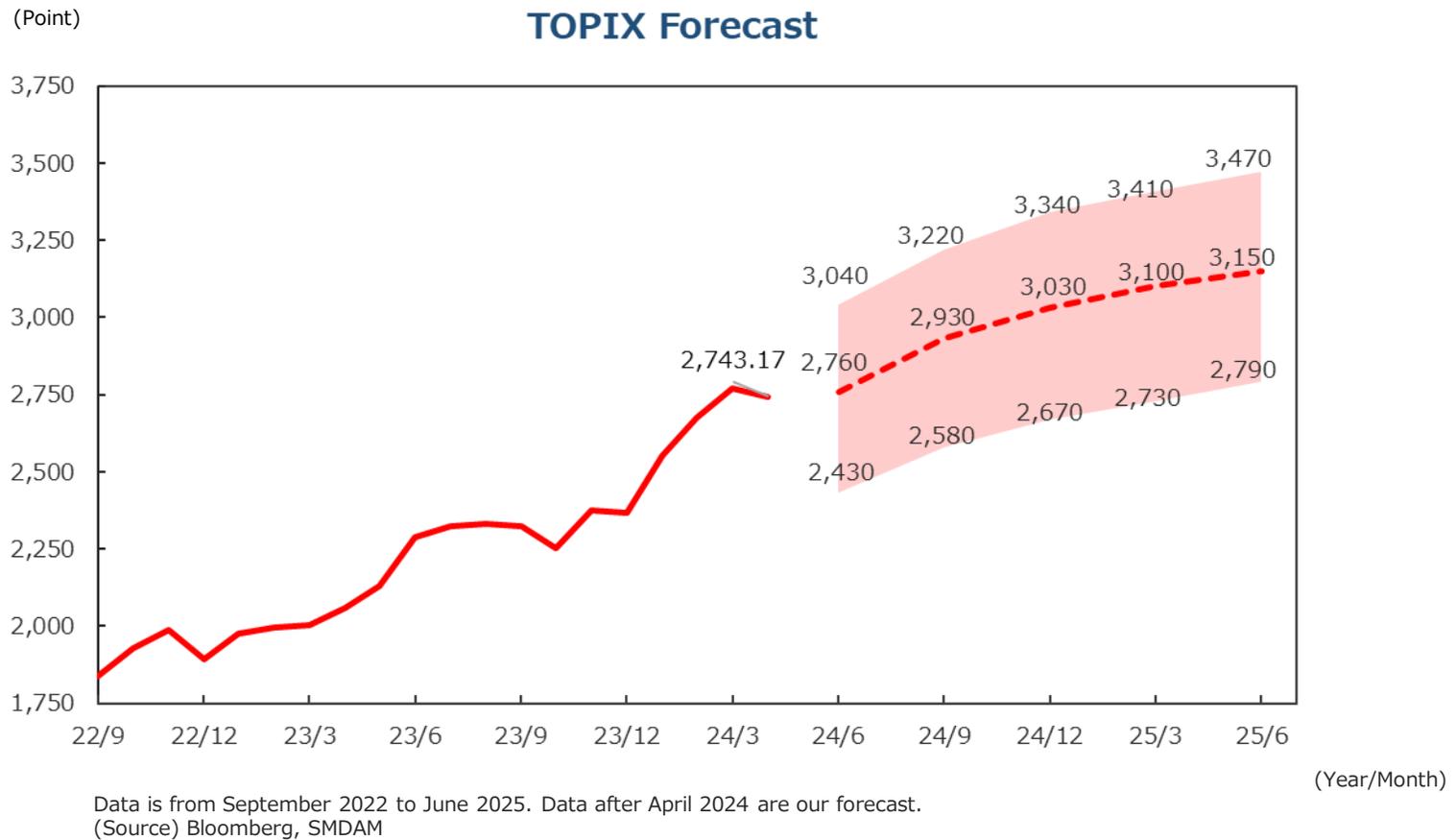
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- We believe corporate earnings will continue to drive the Japanese stock market higher. The solid increase in nominal GDP and the accelerating business cycle of manufacturers could boost EPS for the current year and beyond.
- We maintain our price target for the Nikkei 225 in 2024 at 43,900, and that for TOPIX at 3,030.
- The virtuous cycle of “wage increase and inflation”, along with expectations for further fiscal expansion by “Post-Kishida” new cabinet after the presidency election of the ruling Liberal Democratic Party (LDP) in September, could provide another boost to the equity market.
- In the short term, the market could face increased volatility due to speculation over the monetary policy and foreign exchange rates.

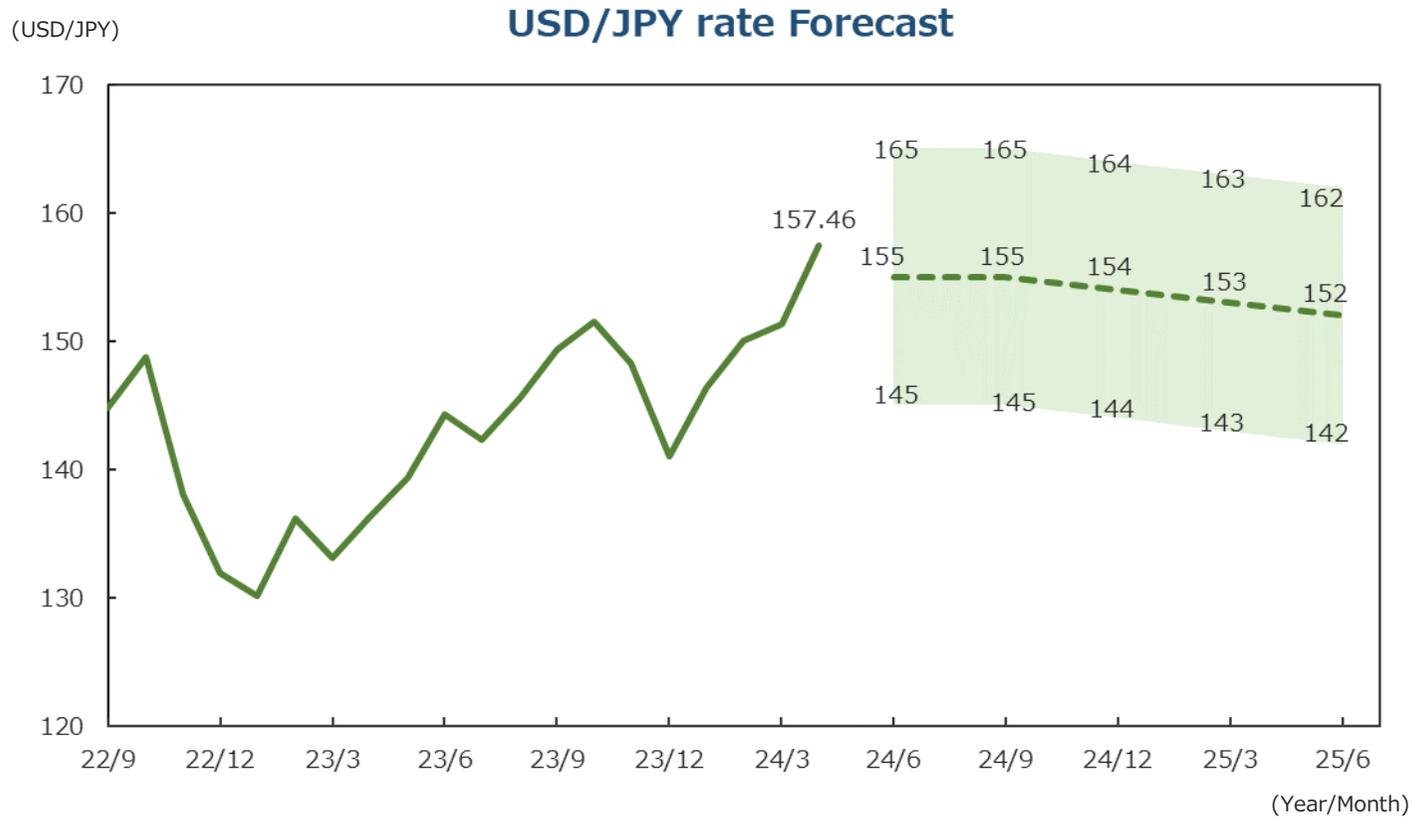
# We expect a bullish stock market going forward



# We expect a bullish stock market going forward



# Strong US economy lift Dollar/Yen forecast range



Data is from September 2022 to June 2025. Data after April 2024 are our forecast.  
(Source) Bloomberg, SMDAM

# Upside / Downside risk scenarios

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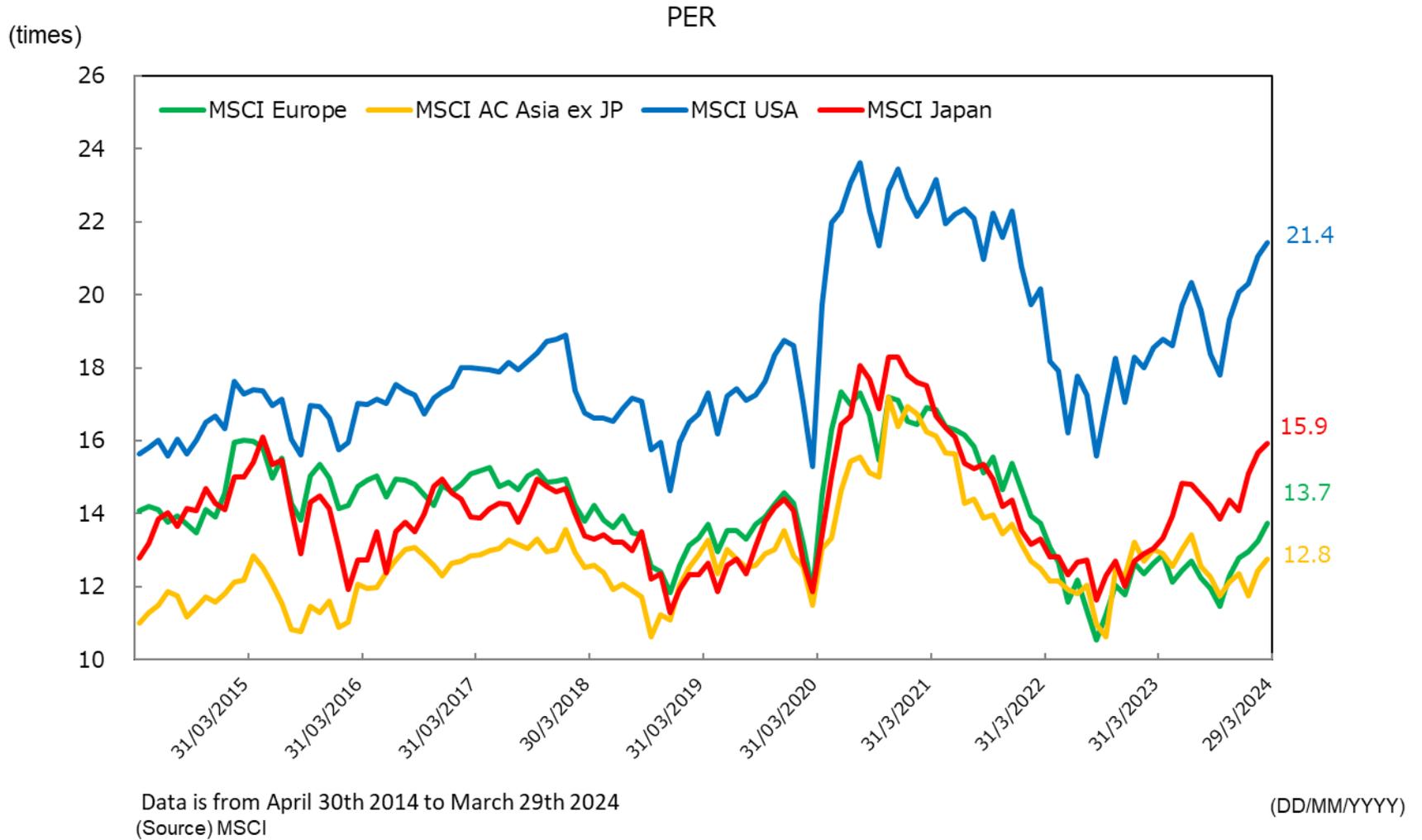
## ■ Upside Risks

- Growing optimism over virtuous cycle of mild inflation and wage increases
- Prolonged accommodative monetary policy by the Bank of Japan

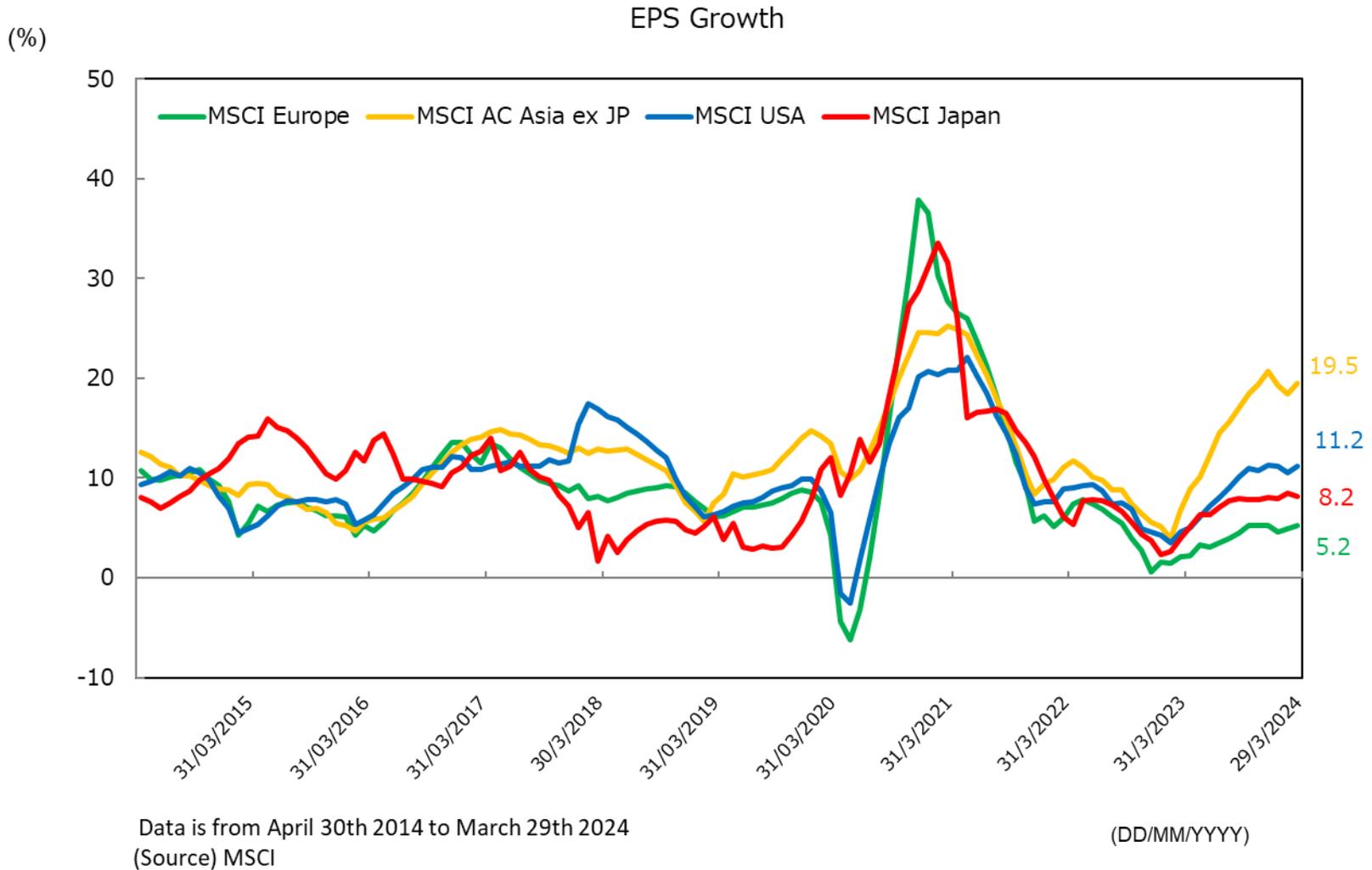
## ■ Downside Risks

- Excessive and rapid JPY appreciation
- Hasty tightening by the BOJ
- Political turmoil triggered by the split of the ruling LDP

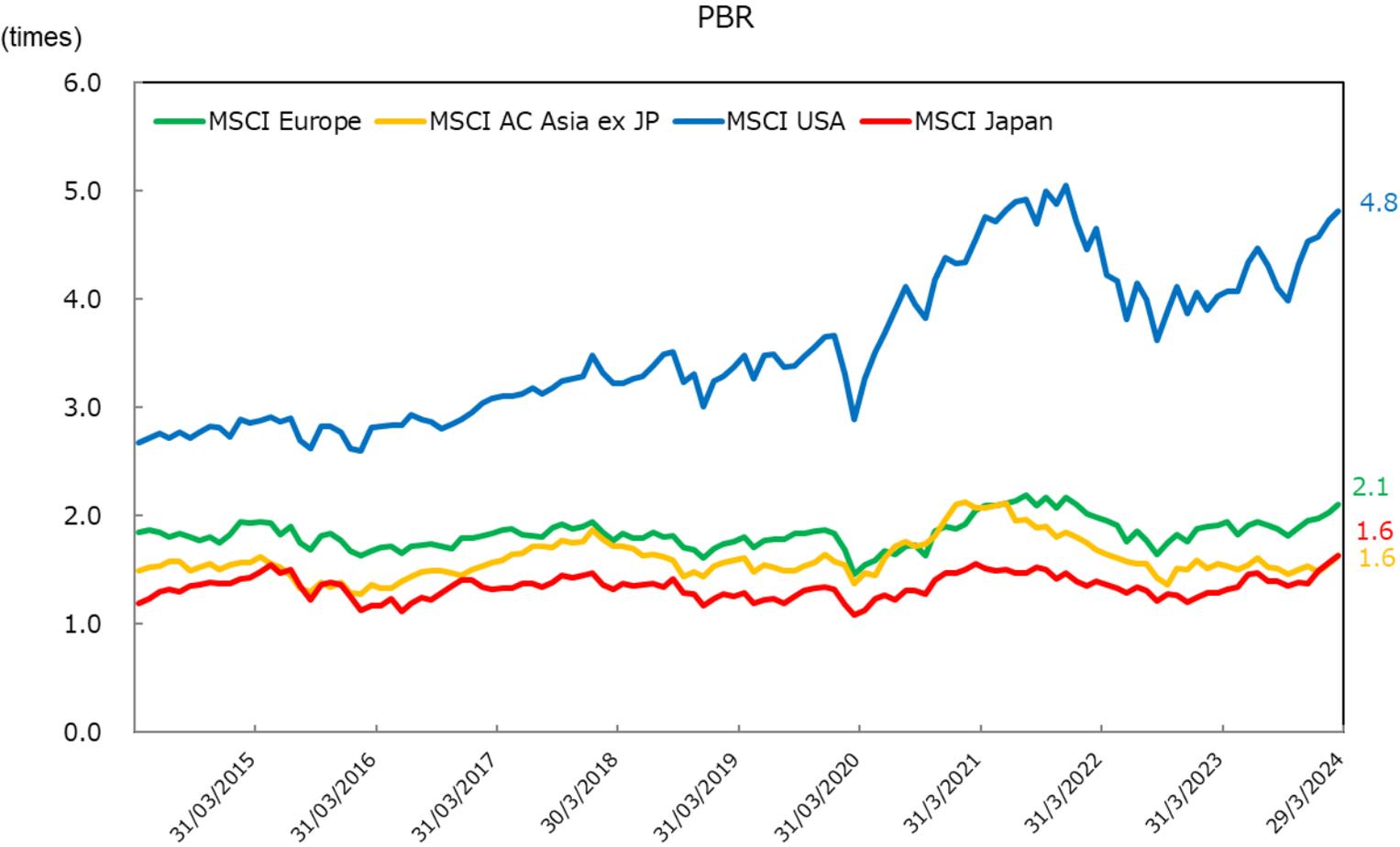
# Recent market rally boosts Japan's P/E ratio



# Earnings growth outlook remains solid



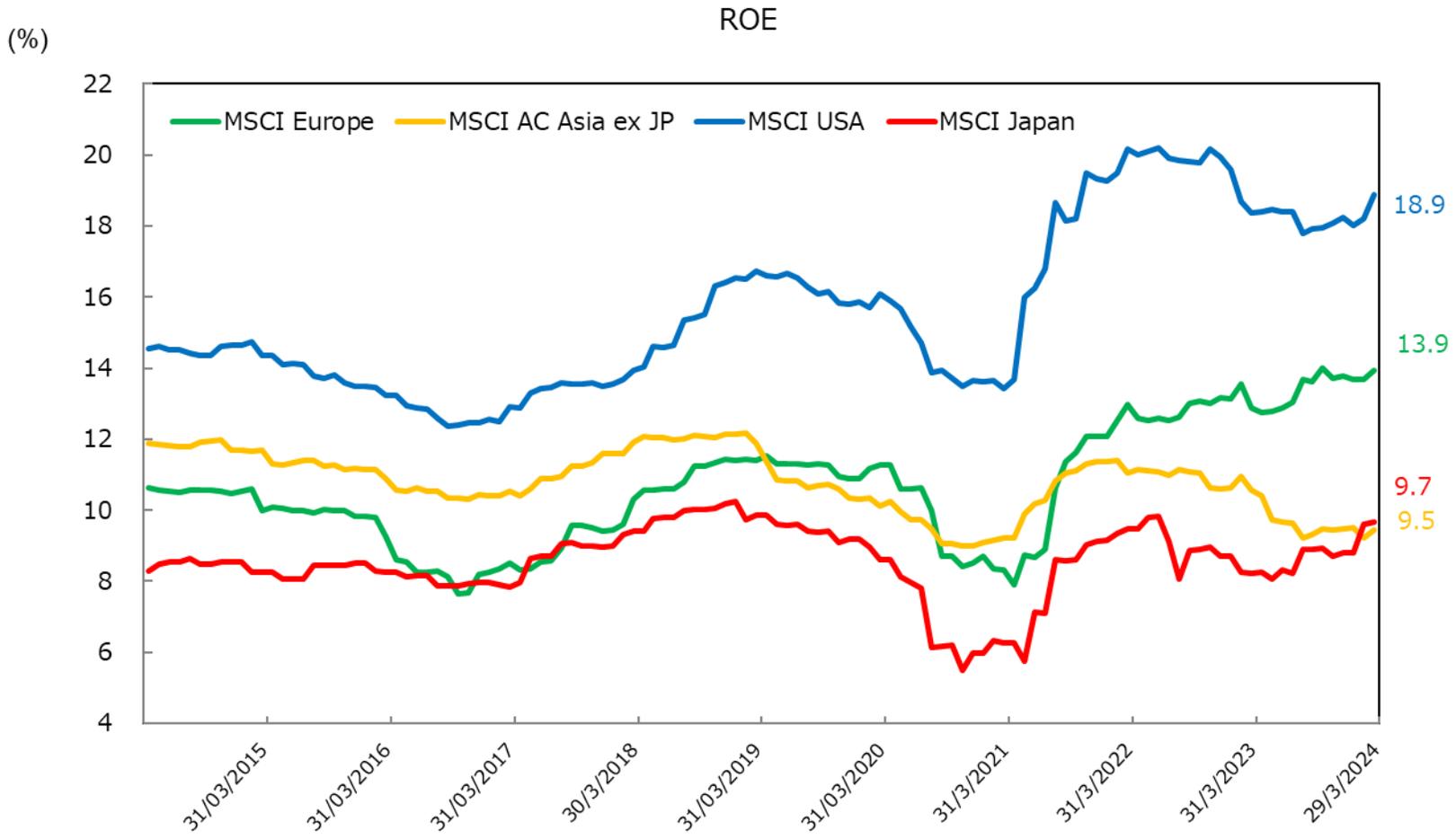
# Japan's P/B ratio catching up with Asian peers



Data is from April 30th 2014 to March 29th 2024  
 (Source) MSCI

(DD/MM/YYYY)

# Japan' ROE surpassed Asian peers

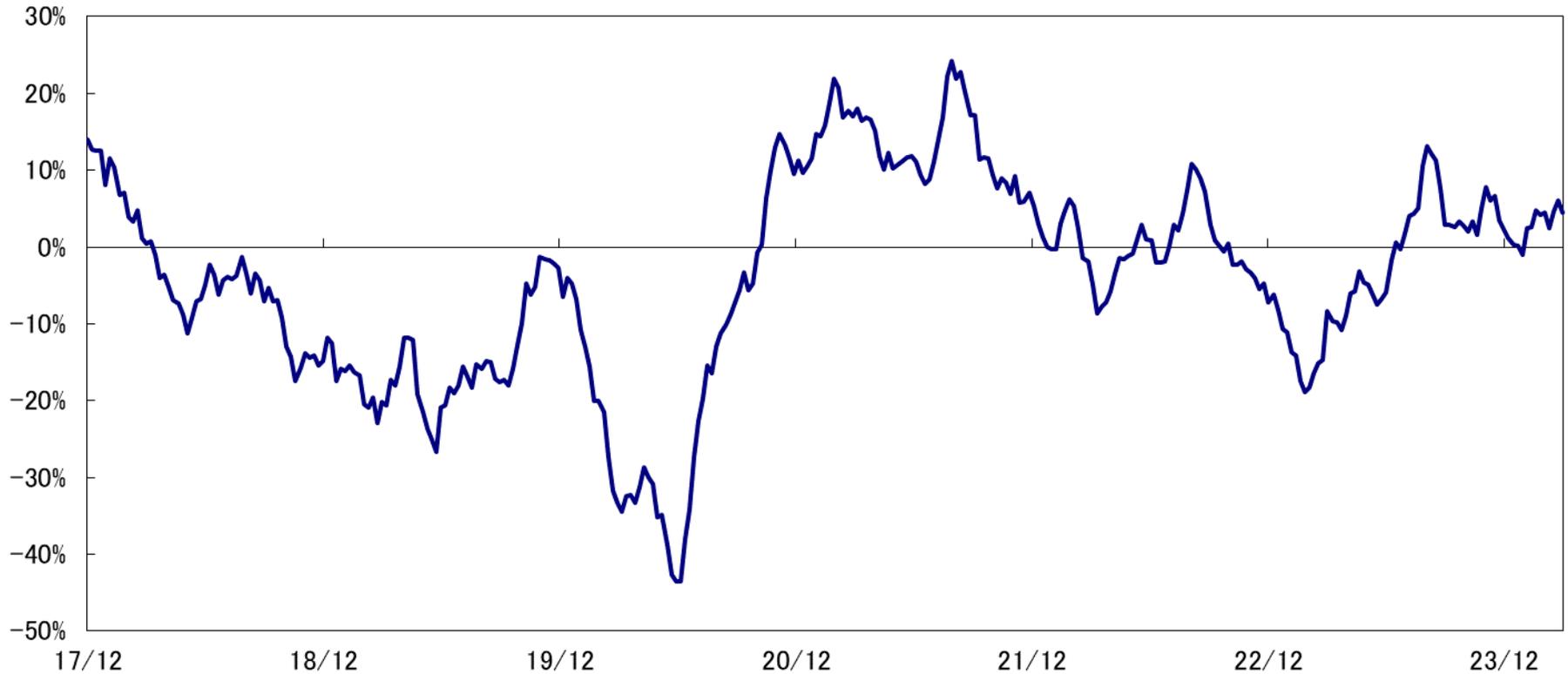


Data is from April 30th 2014 to March 29th 2024  
 (Source) MSCI

(DD/MM/YYYY)

# EPS revision remains positive despite lackluster economic data

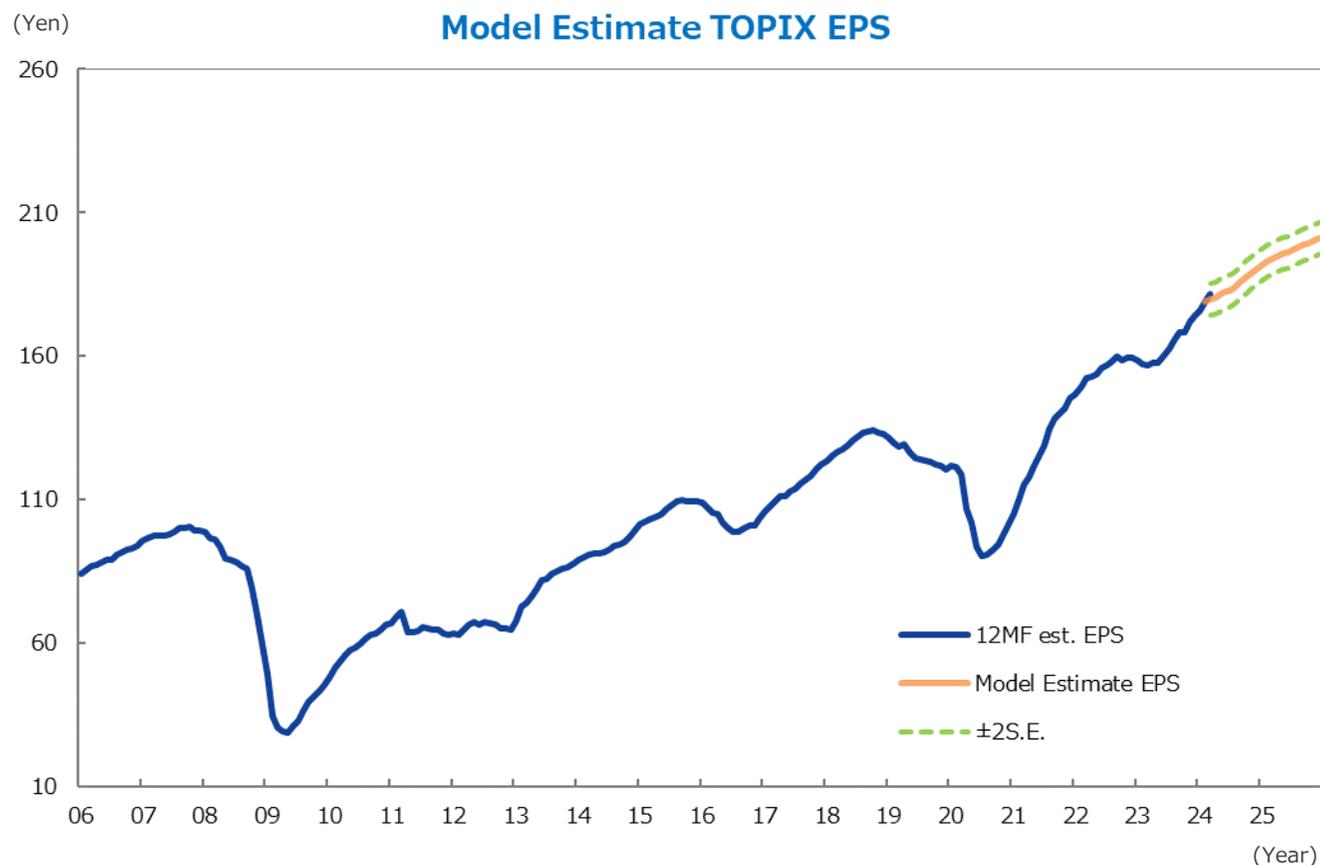
TOPIX Revision Index



Data is from December 28th 2017 to March 29th 2024  
(Source) Datastream, IBES

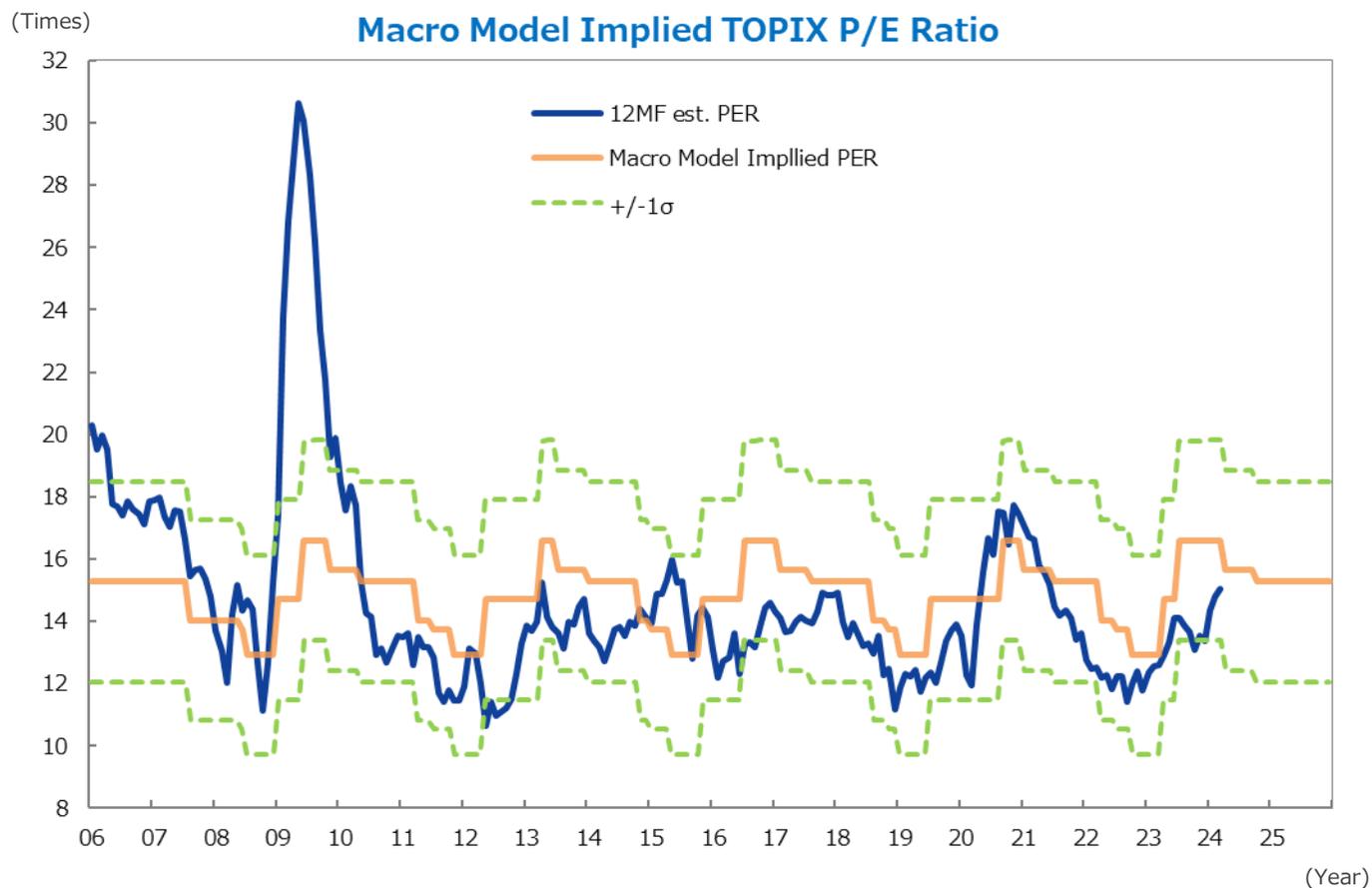
(YY/MM)

# Quant model indicates positive earnings outlook going forward



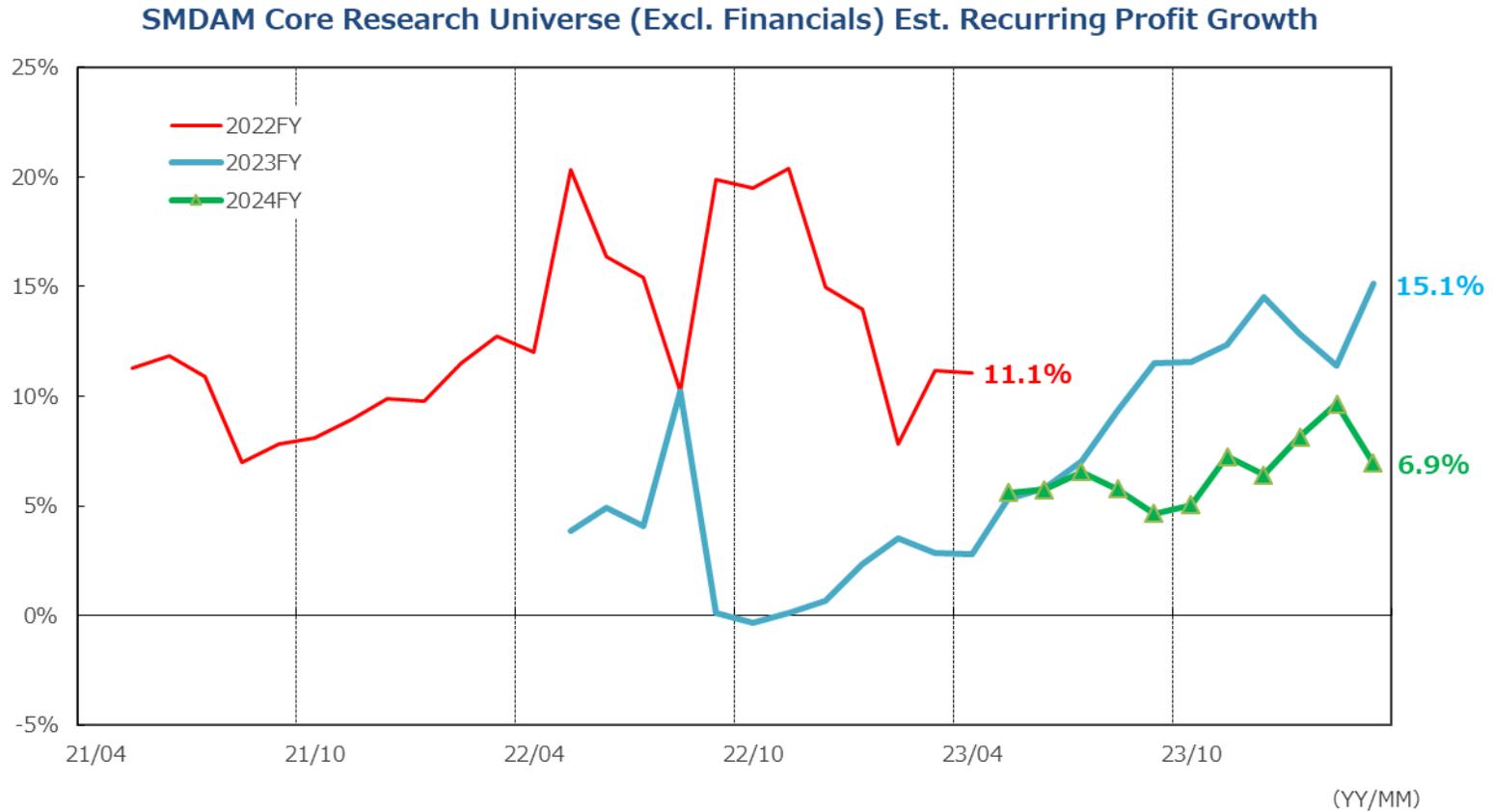
Note: Consensus data is from January 2006 to March 2024. Model estimate Data is from April 2024 to December 2025.  
Source: SMDAM

# Recent rally boost P/E ratio to the fair value of quant model



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

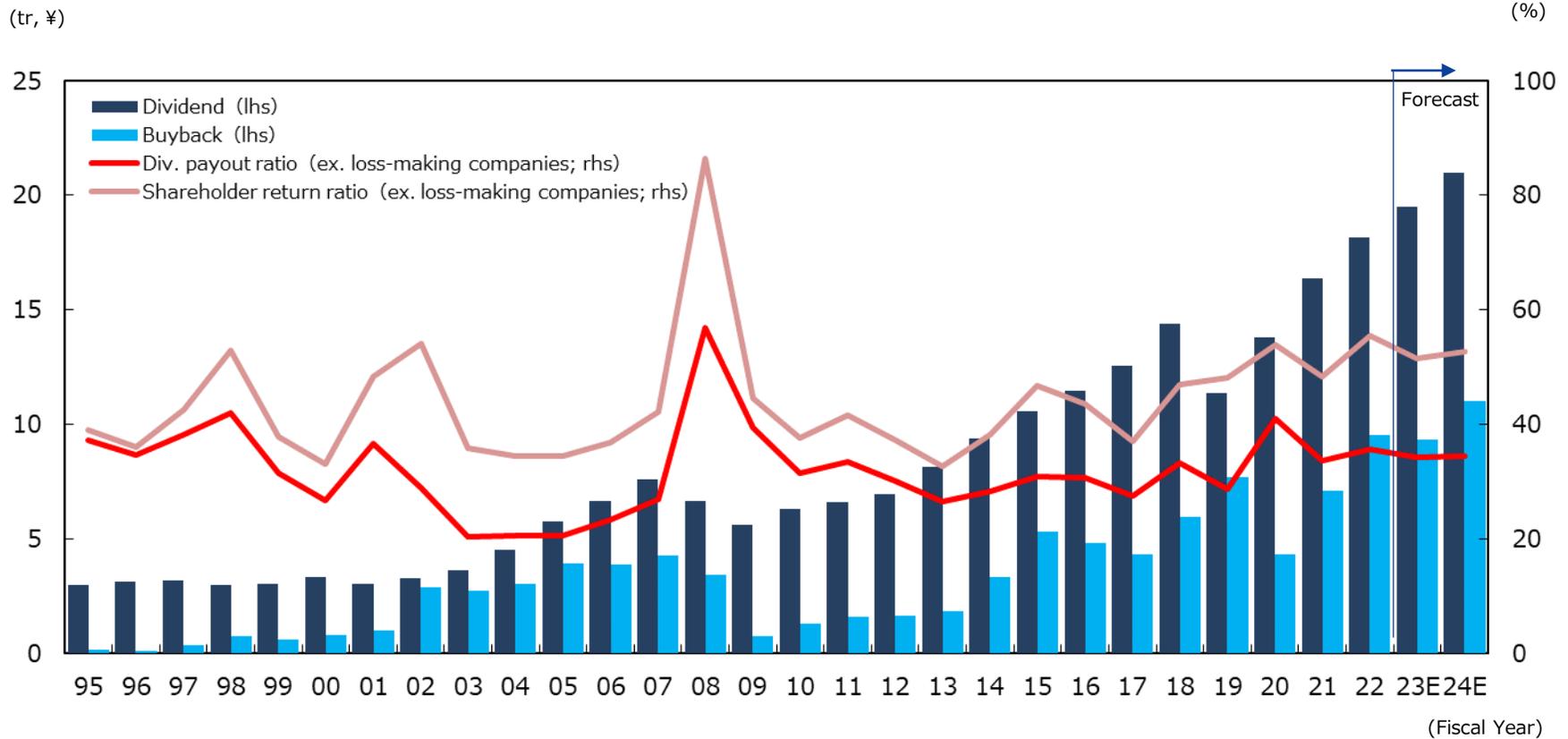
# Bottom up research shows steady earnings growth ahead



Note: Data is as of 8th April 2024, SMDAM Core Universe (Excl. Financials) consists of 373 Japanese companies covered by SMDAM in-house analysts.  
Source: SMDAM

# Record-breaking growth of dividends and buybacks continues

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



Note: Data is from FY1995 to FY2024. FY2023 and FY2024 are forecasts by Daiwa Securities.  
 Source: Toyo Keizai, Quick, INDB, Daiwa Securities, SMDAM

# Large cap value keep dominating the market

## Performance Comparison of Russell/Nomura Style Indices

Index	Returns(%)						
	3 Month	6 Month	YTD	1 Year	2 year	3 Year	5 Year
<b>RN Japan Equity</b>	<b>6.51</b>	<b>16.12</b>	<b>12.29</b>	<b>31.15</b>	<b>40.19</b>	<b>34.97</b>	<b>63.83</b>
Total Value	10.83	18.15	17.63	43.59	57.73	63.23	74.99
Top Cap Value	15.91	21.57	24.49	53.40	66.42	84.01	108.42
Large Cap Value	11.45	18.76	19.13	46.02	58.81	68.40	80.71
Mid Cap Value	7.28	16.09	14.17	37.81	50.40	51.26	49.02
Small Cap Value	7.97	15.31	10.94	32.92	52.44	41.53	51.00
Micro Cap Value	5.16	13.52	7.88	28.12	47.46	39.45	47.43
Total Growth	2.71	14.52	7.66	20.05	25.00	12.31	51.65
Top Cap Growth	4.47	18.85	10.67	25.77	29.01	18.34	65.95
Large Cap Growth	3.08	15.34	8.54	21.76	26.86	14.30	56.74
Mid Cap Growth	0.45	9.03	4.61	14.60	22.83	7.24	41.79
Small Cap Growth	-0.49	7.52	0.16	6.40	10.46	-3.39	14.71
Micro Cap Growth	0.26	8.86	0.53	6.08	10.05	-6.65	15.33
Top Cap Total	8.74	19.57	15.77	37.08	44.12	43.47	82.29
Large Cap Total	6.81	16.75	13.22	32.70	41.04	37.08	68.63
Mid Cap Total	4.17	12.88	9.77	26.56	36.81	28.41	50.49
Small Cap Total	4.64	12.21	6.65	22.19	34.90	22.31	37.05
Micro Cap Total	3.47	11.89	5.31	20.59	34.14	22.67	37.49

Note : As of 17th April 2024  
(Source) Bloomberg



# Outlook for Japanese Economy

# Current status & Outlook of Japanese economy

## [Current Status]

- **The economy is standing still.** Though real GDP in Q4 of 2023 was revised upward to show the first positive growth in 2 quarters, Q1 of 2024 is expected to be negatively affected by the reduction in automobile production owing to the issue of certification test frauds and the Noto Peninsula earthquake. Business and consumer confidence, however, are generally firm and the economy is not in a major slump.
- **Inflation is slowing down.** The nationwide core CPI rose 2.8% YOY in February, up from 2.0% in the previous month, primarily due to the reduced impact of subsidies on electricity and gas bills. However, in March, the core CPI for the Tokyo metropolitan area was up 2.4% from a year earlier, down slightly from 2.5% a month earlier. The decline in cost-push pressure from import prices, continues to push down inflation.

## [Outlook]

- ① **We have maintained our real GDP growth forecast for FY 2023 at +1.3% and that for FY 2025 at +0.7%, and we have lowered our estimate for FY 2024 from +0.7% to +0.5%.** The main reason for the downward revision in FY 2024 was a reduction in consumer spending due to rising prices. It is highly likely that the economy contracted in Q1 2024 due to temporary factors such as a reduction in automobile production related to the issue of illegal certification tests, the Noto Peninsula earthquake, and a reaction to royalties and receipts from intellectual property rights. However, we expect a gradual recovery to follow this temporary pause of the economy, avoiding any major setbacks, supported by rising wages, economic measures (including fixed tax cuts and benefits), and the resilience of overseas economies.
- ② **While we have maintained our core CPI forecast for FY 2023 at +2.8%, we have raised that for FY 2024 from +2.4% to +2.8% and that for FY 2025 from +2.0% to +2.1% respectively.** The upward revisions in FY 2024 and FY 2025 were mainly due to higher renewable energy levies, the end of subsidies for electricity and gas bills, and changes in exchange rates and crude oil price assumptions. Increase in the renewable energy levy and end of subsidies on electricity and gas bills will lift core CPI around 3% after May 2024. Following that, core CPI is likely to slow down against the background of the abatement of these pushing factors and the reduction of cost push pressure originating from import prices. However, the core CPI is expected to remain stable at around 2% from H2 of 2025, supported by the rise in service prices following the improvement in wages.
- ③ **We expect the government to continue their accommodative fiscal policy.** In November 2023, Prime Minister Kishida's Cabinet approved "comprehensive economic measures to overcome deflation." The measures, which amount to 20.9 trillion yen on a national and local spending basis, include measures to counter high prices, support for growth sectors, and national infrastructure resilience. Flat rate tax cuts are expected to take effect in June 2024. In fiscal policy we should pay close attention to the risk of further expansion aimed at raising the approval ratings of the Cabinet and the ruling Liberal Democratic Party, which have declined significantly owing to "slush fund scandal".
- ④ **We have changed our monetary policy forecasts. We expect the Bank of Japan will raise interest rate by 0.25% in October 2024, April 2025, and October 2025 to lift the policy rate to 0.75%.** The main reasons for our changes in the monetary policy forecasts include an upward revision of inflation and communication by the Bank of Japan. For the former reason, the core CPI is expected to exceed 2% YOY going forward, which would justify further tightening by the central bank. As for the latter, the BOJ governor Ueda expressed confidence that the results of the Union's spring negotiation will be reflected in prices in the summer and autumn, suggesting that he might decide to raise interest rates. Previously, the BOJ had been expected to take time to assess the spread from wages to prices, but we have changed our view. The risk for this scenario is the acceleration of rate hikes due to the weakening yen.



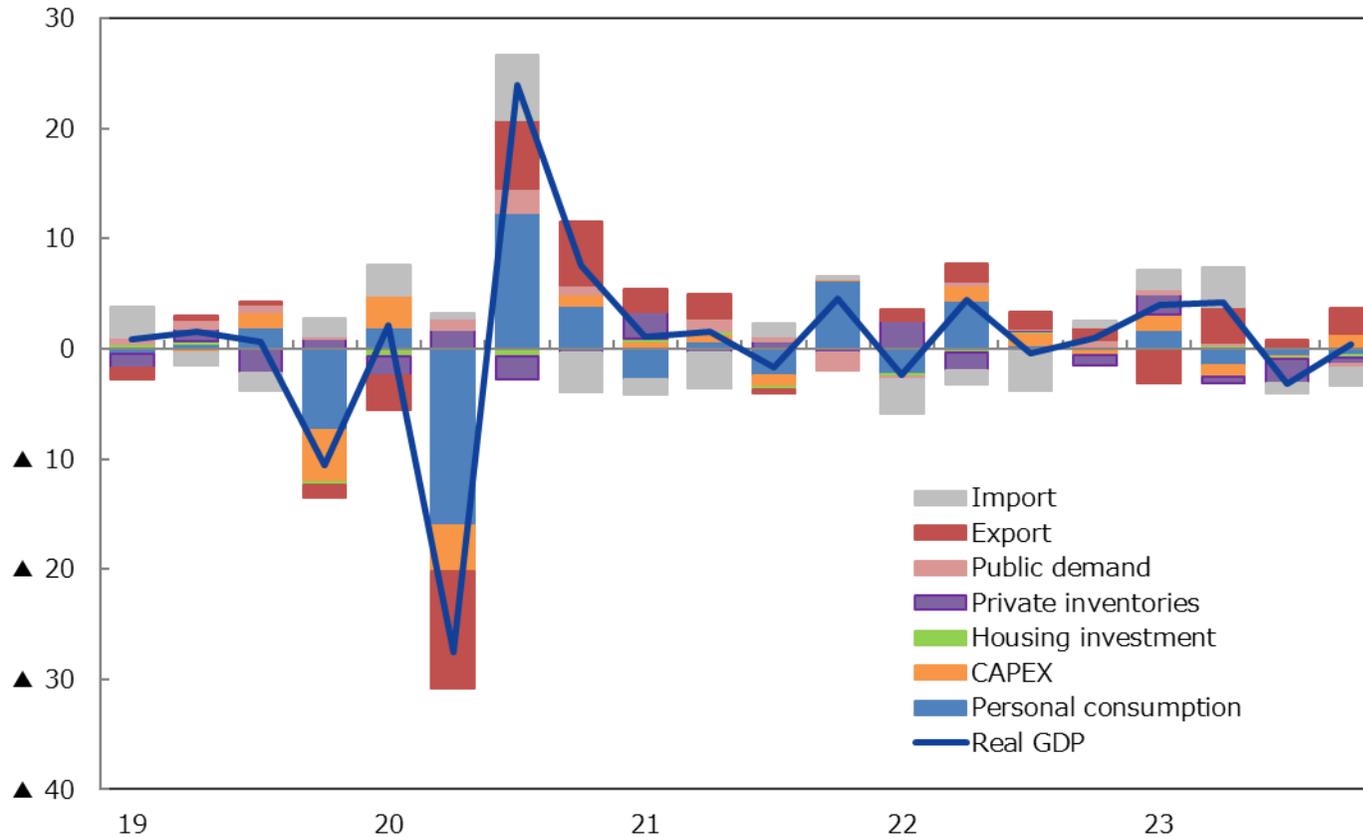
# Forecast for the Japanese economy

Forecast of annual Real GDP growth and its breakdown								
Fiscal Year	FY19	FY20	FY21	FY22	FY23 Est	FY24 Est	FY25 Est	
Real GDP	-0.8%	-4.1%	2.7%	1.4%	1.3%	0.5%	0.7%	
Private final consumption expenditure	-0.9%	-5.1%	1.5%	2.5%	-0.5%	0.3%	1.0%	
Private housing investment	2.5%	-7.2%	-0.6%	-3.0%	1.4%	-0.3%	-1.0%	
Private-sector capital investment	-1.2%	-5.4%	2.3%	3.1%	0.5%	1.4%	0.8%	
Private inventory investment	-0.2%	-0.3%	0.4%	0.2%	-0.3%	-0.2%	0.0%	
Public fixed capital formation	1.6%	4.9%	-6.5%	-3.1%	3.0%	0.8%	0.7%	
Net export contribution	-0.5%	-0.6%	0.8%	-0.6%	1.4%	0.1%	-0.2%	
Exports of goods and services	-2.3%	-9.9%	12.4%	4.5%	3.4%	2.6%	2.3%	
Imports of goods and services	0.2%	-6.3%	7.1%	7.2%	-3.4%	2.3%	3.3%	
Nominal GDP	0.0%	-3.4%	2.5%	2.0%	5.2%	2.6%	2.3%	
GDP deflator	0.8%	0.7%	-0.1%	0.7%	3.9%	2.1%	1.6%	
Industrial Production Index	-3.6%	-9.7%	5.7%	-0.3%	-1.9%	1.5%	1.2%	
Consumer Price Index (Core)	0.4%	-0.6%	0.1%	3.0%	2.8%	2.8%	2.1%	
Domestic corporate goods price index	0.1%	-1.5%	7.1%	9.4%	2.3%	1.5%	1.1%	
Employee compensation	2.0%	-1.5%	2.1%	2.0%	1.9%	3.6%	3.6%	
Unemployment rate	2.4%	2.9%	2.8%	2.6%	2.5%	2.5%	2.3%	
Monetary Policy interest rate (Short term)	-0.1%	-0.1%	-0.1%	-0.1%	0-0.1%	0.3%	0.8%	

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

# Japanese economy avoids technical recession

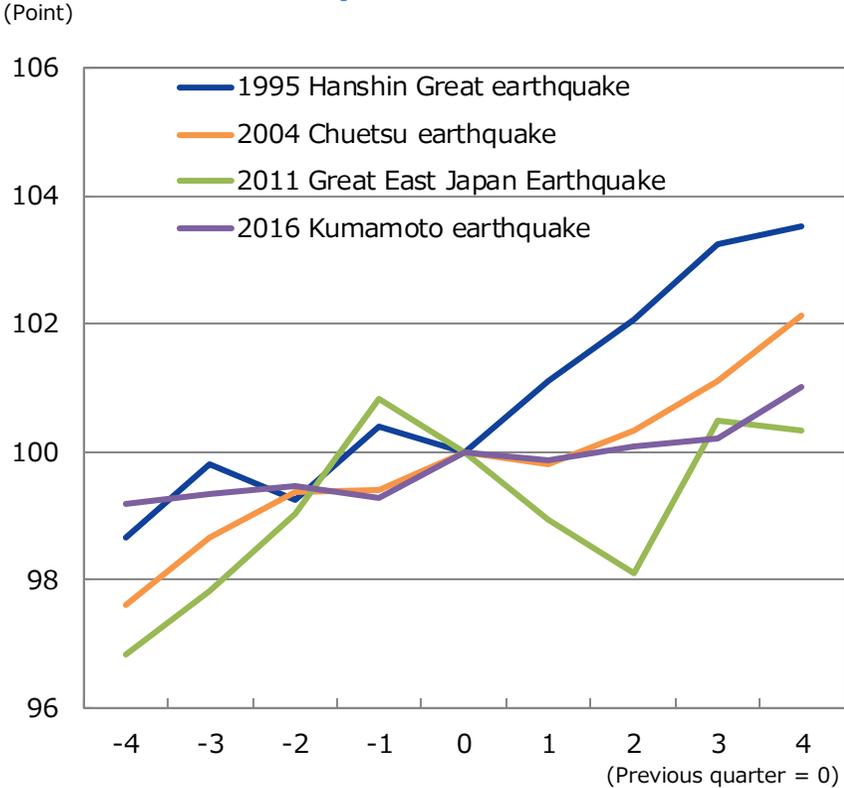
## Real GDP growth rate (YOY, %)



Note: Data is from Q1 2019 to Q4 2023.  
Source: Cabinet office, SMDAM

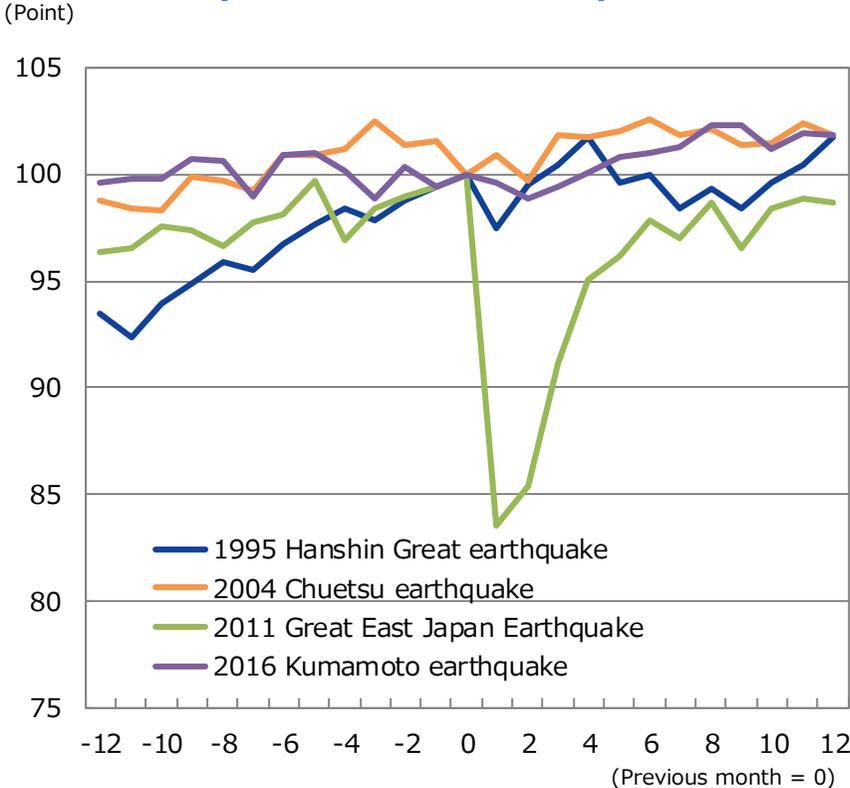
# Earthquakes had historically marginal impact on the economy

### Earthquake & Real GDP



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

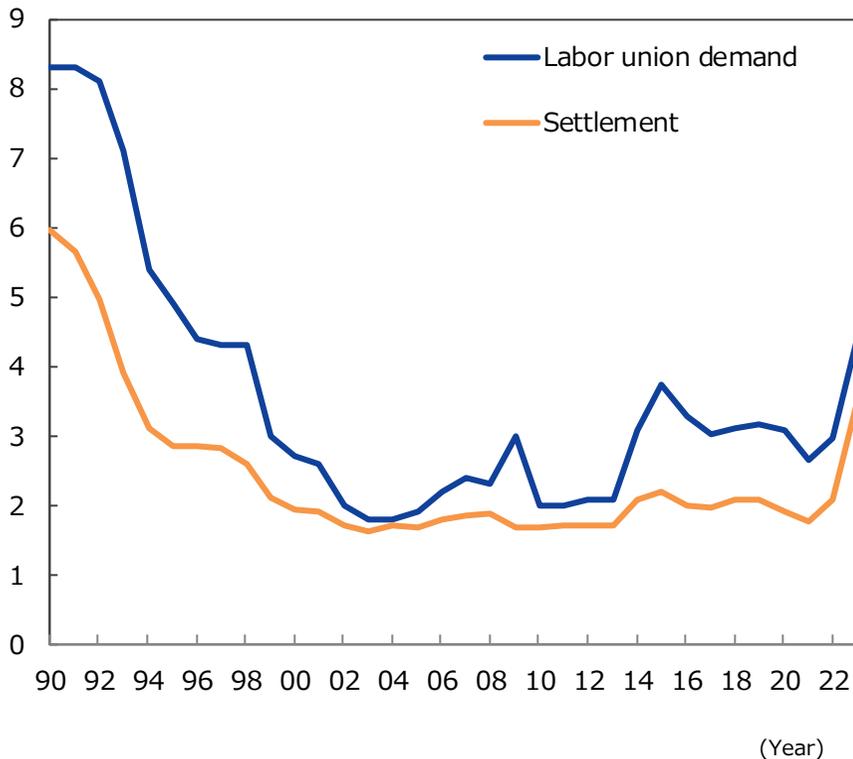
### Earthquake & Industrial production



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

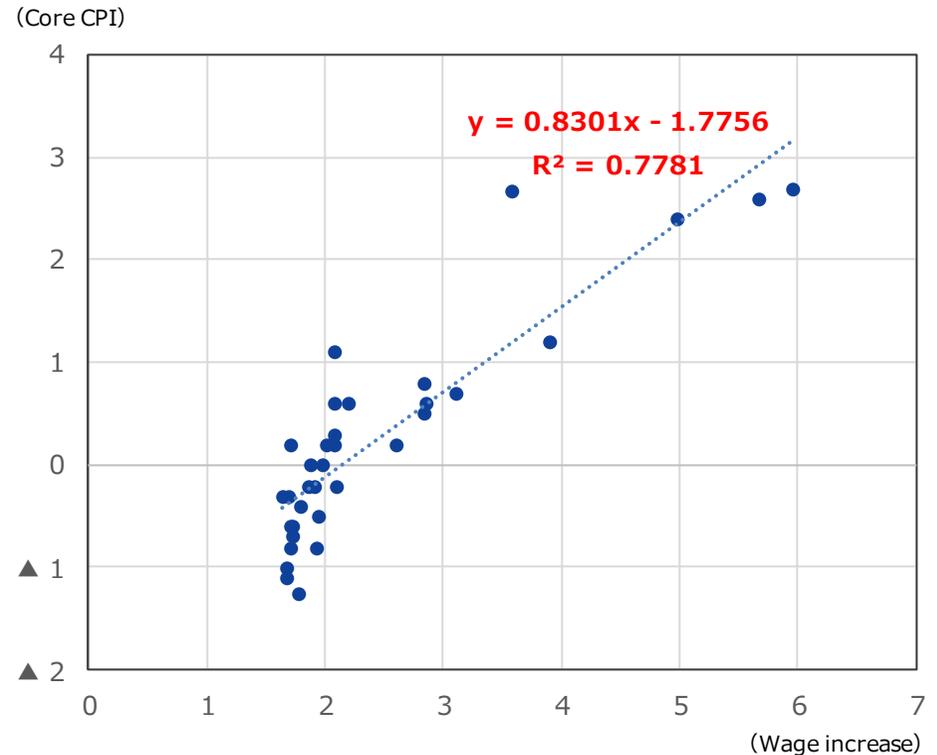
# Why we expect a virtuous cycle of wage hike & inflation in Japan

## Wage increase demand & settlement (YOY, %)



Note: Data is from FY 1990 to FY 2023.  
Source: Japanese Trade Union Confederation, SMDAM

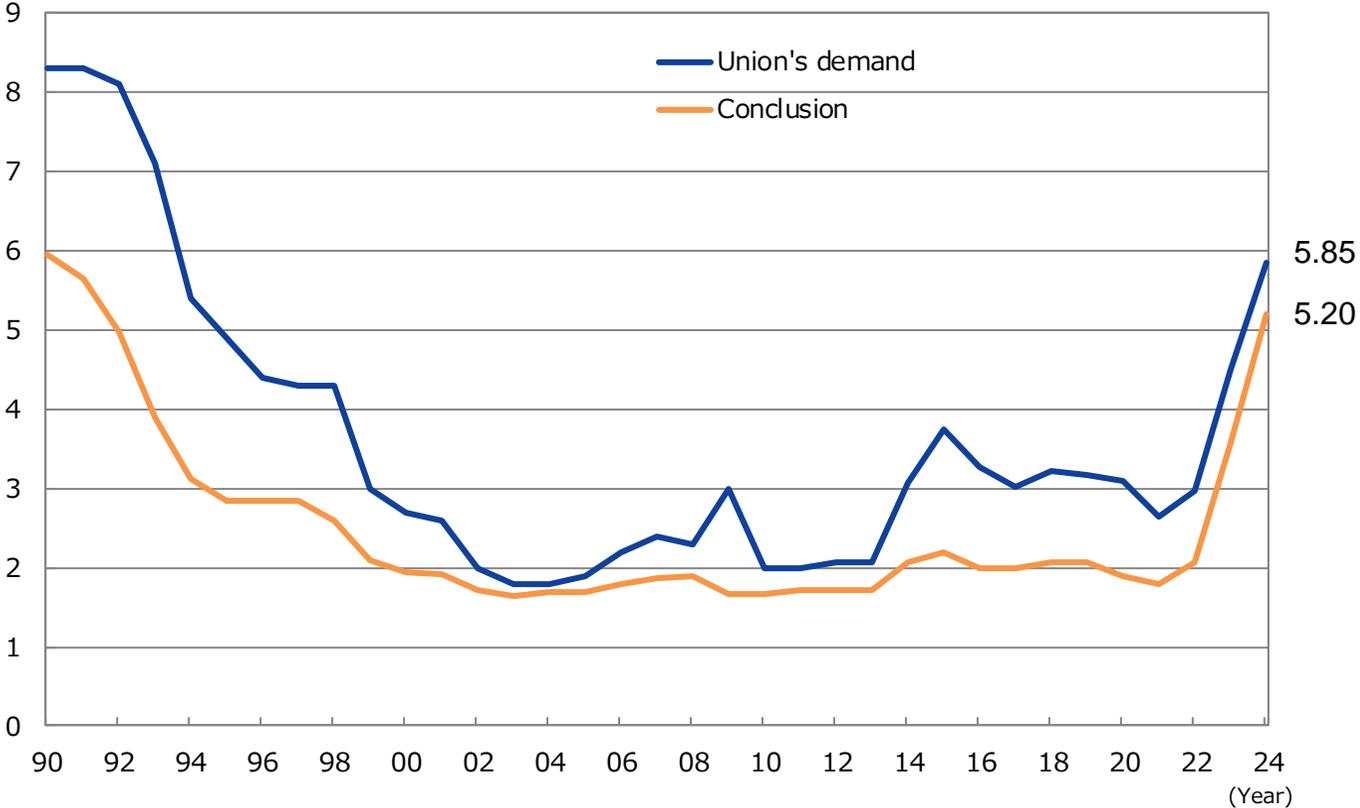
## Wage increase & Core CPI (YOY, %)



Note: Data is from FY 1990 to FY 2022. Core CPI is excluding food, except for alcohol, & energy  
Source: MIAC, Japanese Trade Union Confederation, SMDAM

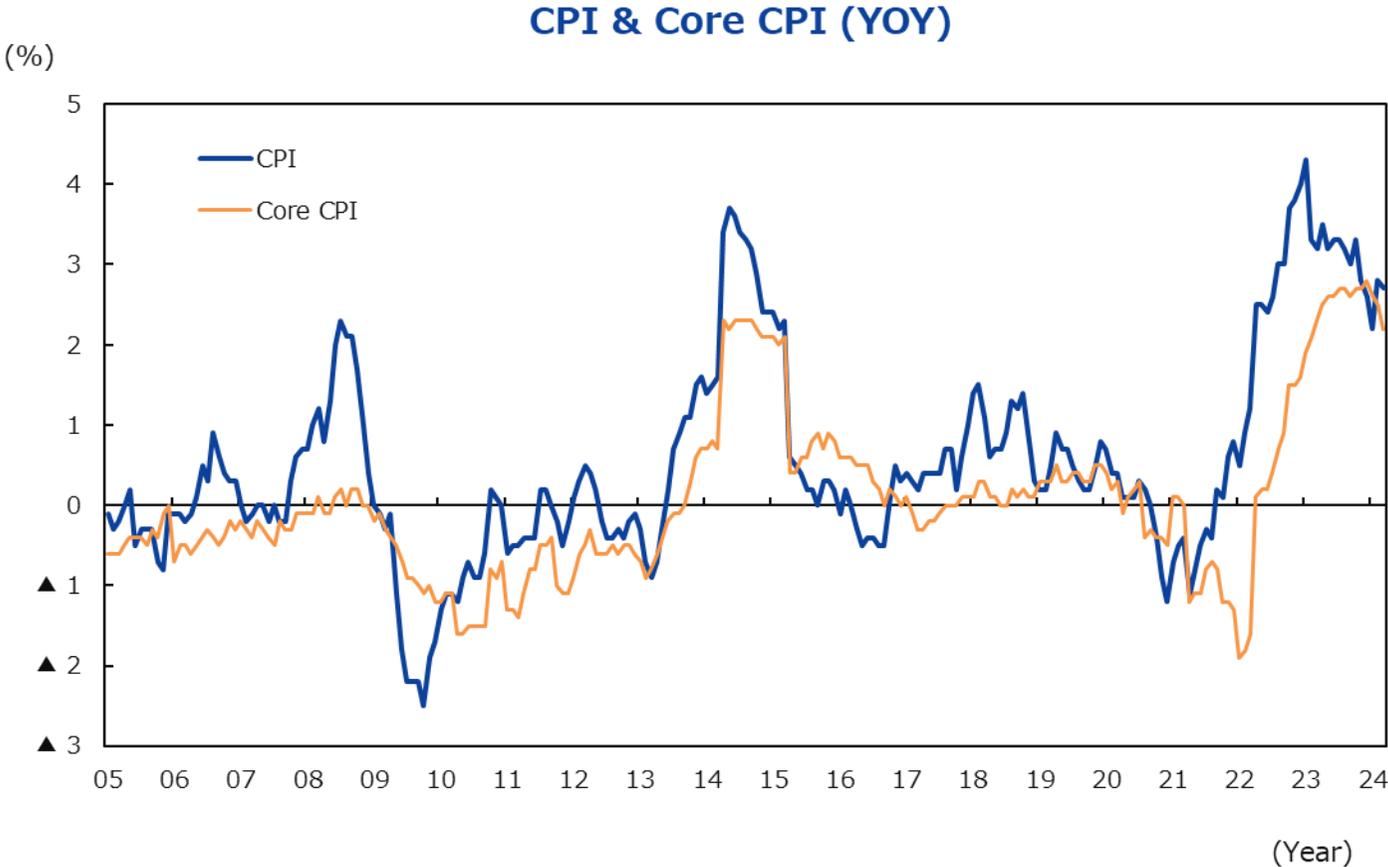
# Highest wage increase in 33 years in Japan

### Wage increase (YOY, %)



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

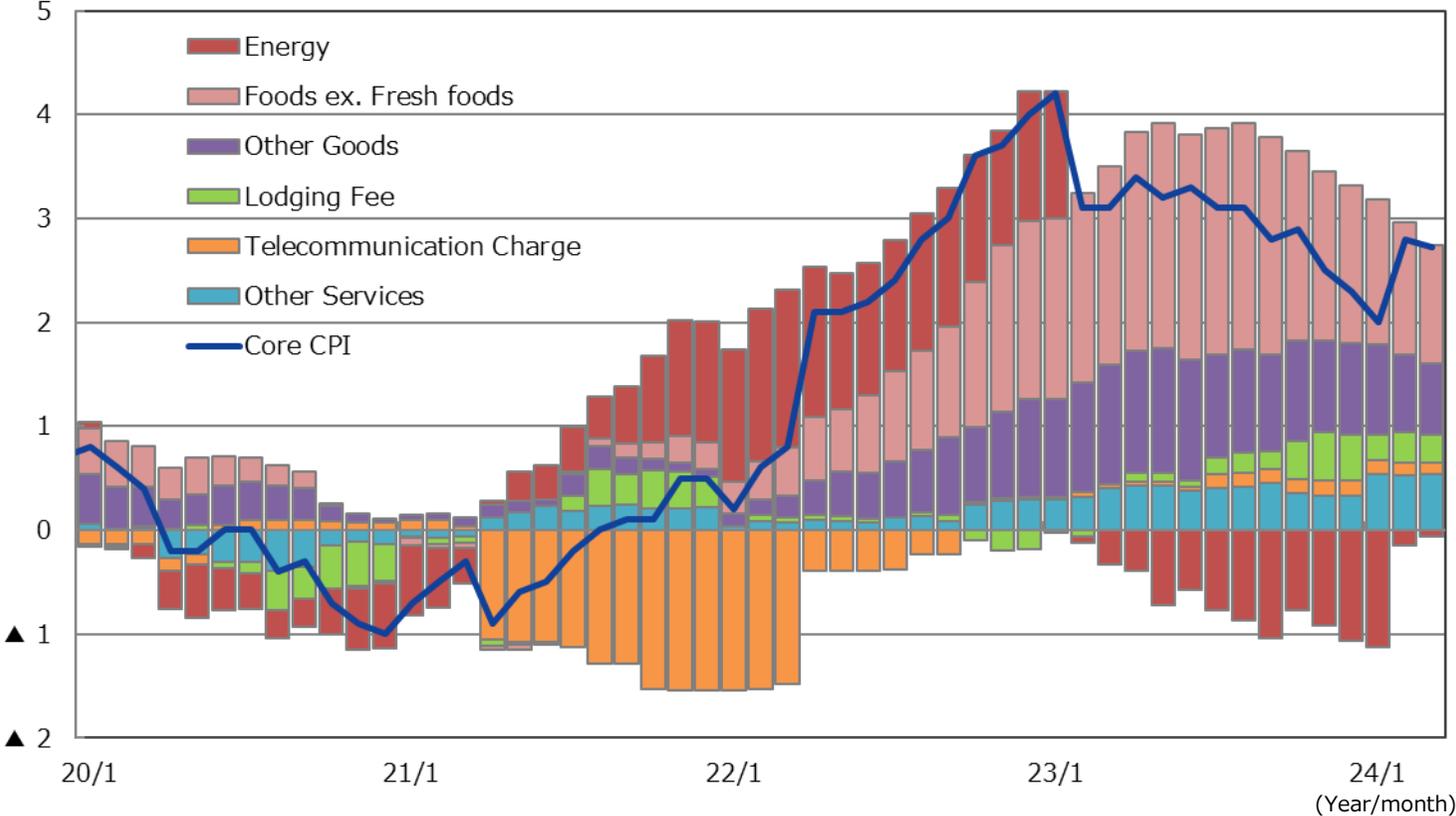
# CPI reaccelerate before reaching to BOJ target of “2%”



Note: Data is from January 2005 to March 2024, Core CPI is excluding food, except for alcohol, & energy.  
Source: MIAC, Bloomberg, SMDAM

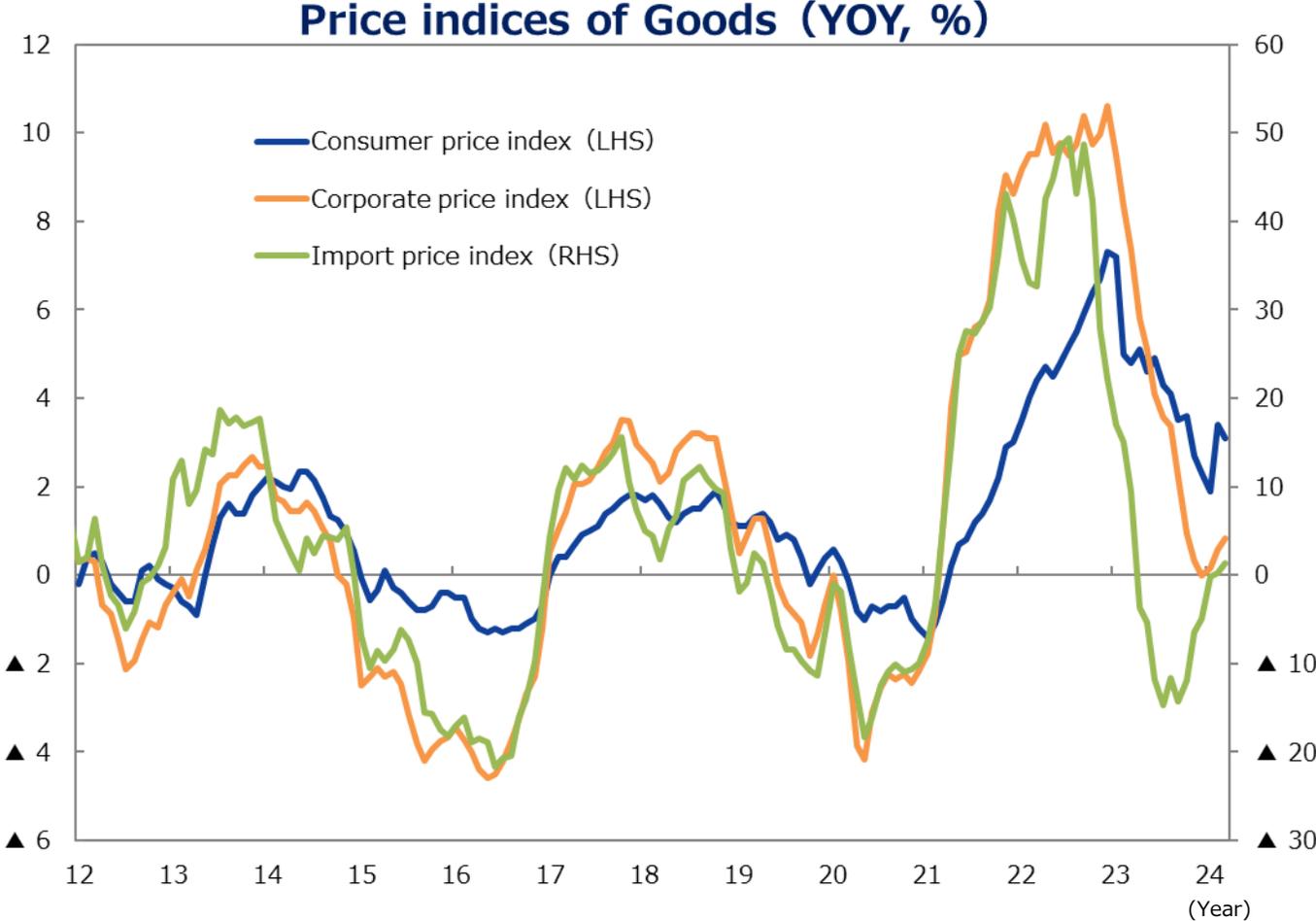
# End of subsidies for utility bills lift CPI from February

Breakdown of CPI (YOY, %)



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

# Bottoming input prices lift CPI again?



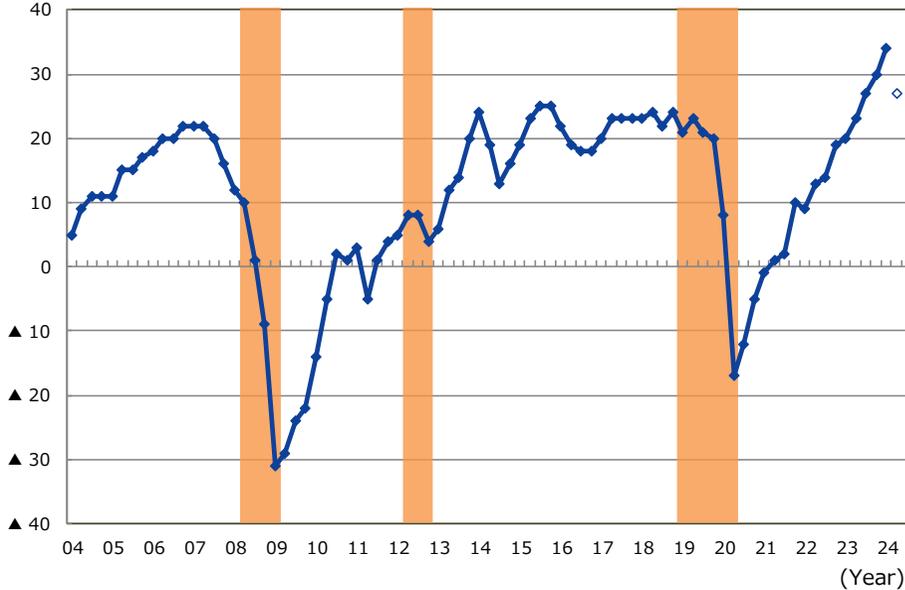
Note: Data is from January 2012 to March 2024.  
 Source: MIAC, Bloomberg, SMDAM

# Divergence of business sentiment between manufacturers and services

BOJ business condition DI Large manufacturers (%)



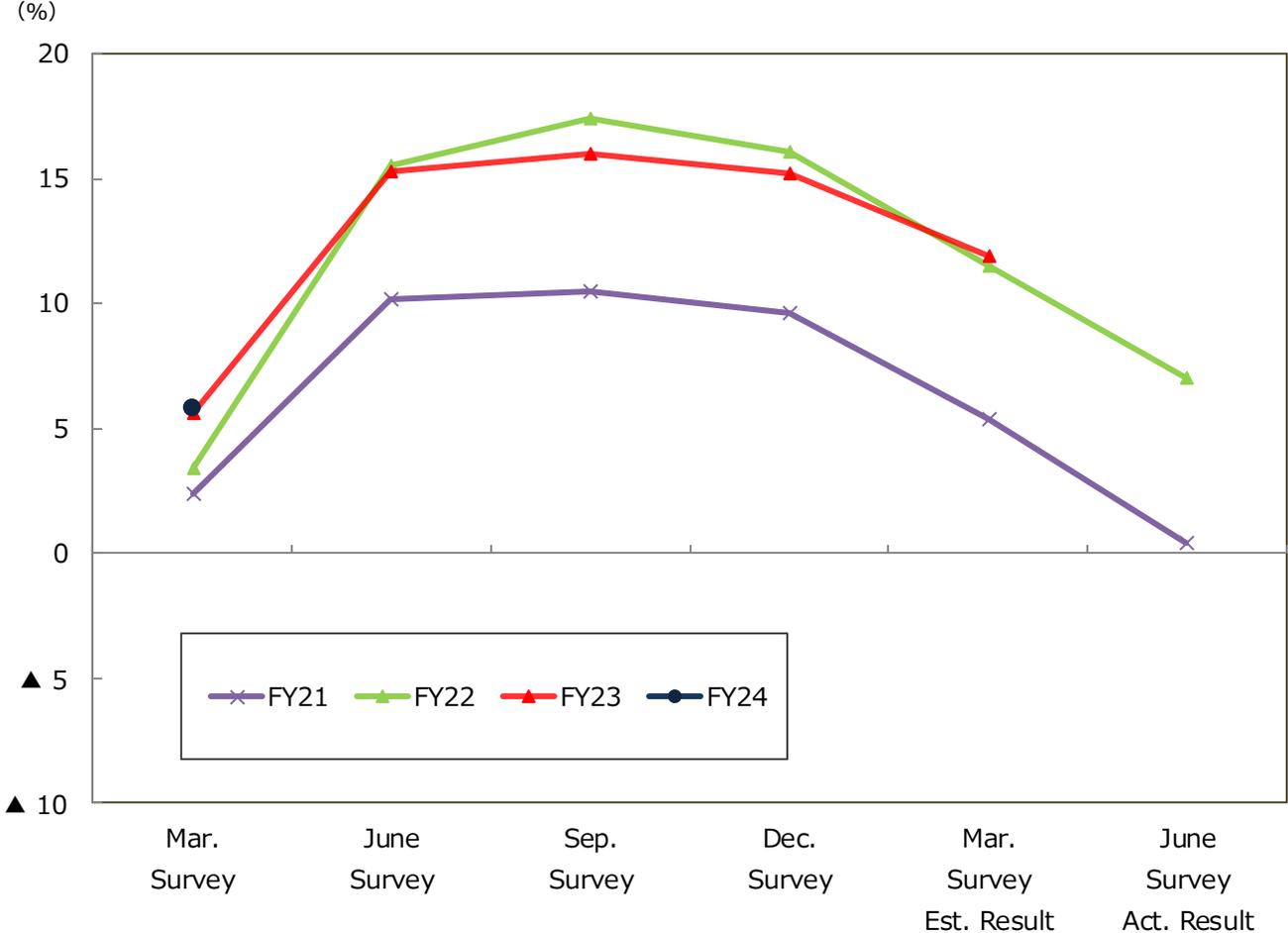
BOJ business condition DI Large non-manufacturers (%)



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

# CAPEX maintains a brighter outlook in 2024

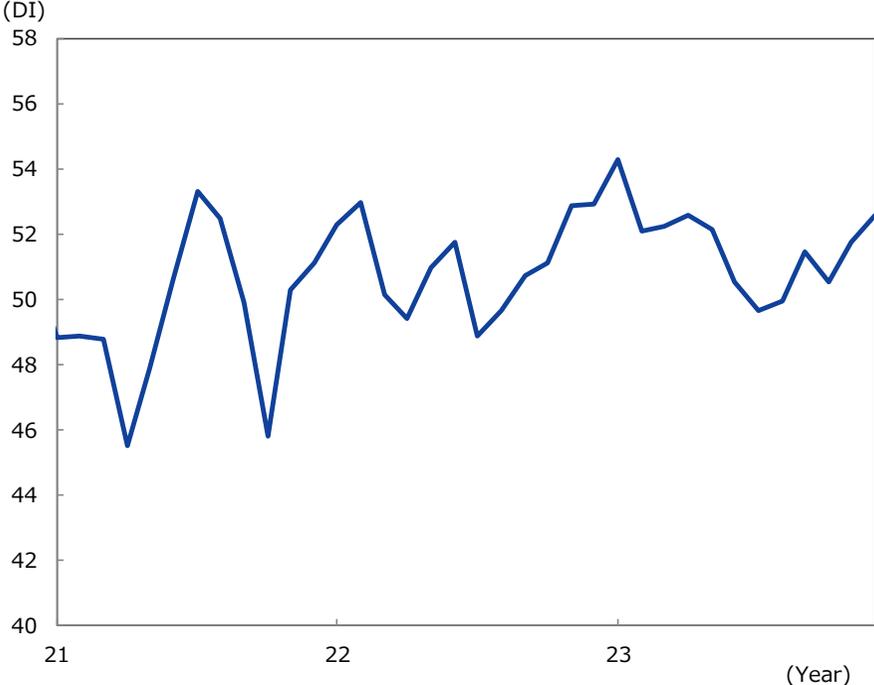
Plan of CAPEX (Inc. Software, Ex. Land and R&D, YOY)



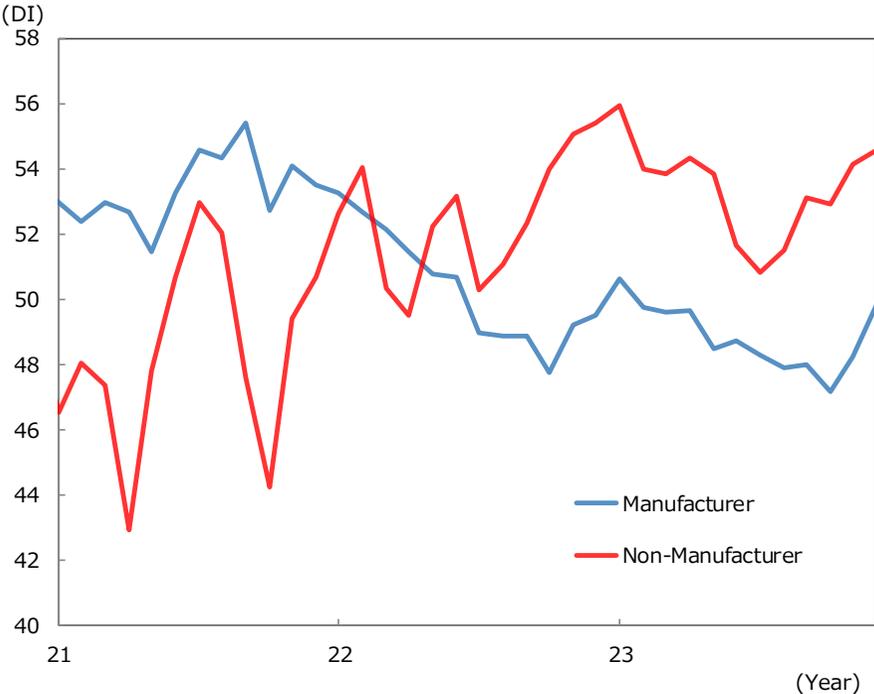
Note: Data is from Q1 FY2020 to Q1 FY2024.  
Source: The Bank of Japan, SMDAM

# Recovery of manufacturers' production and new order boost PMI

### Composite PMI



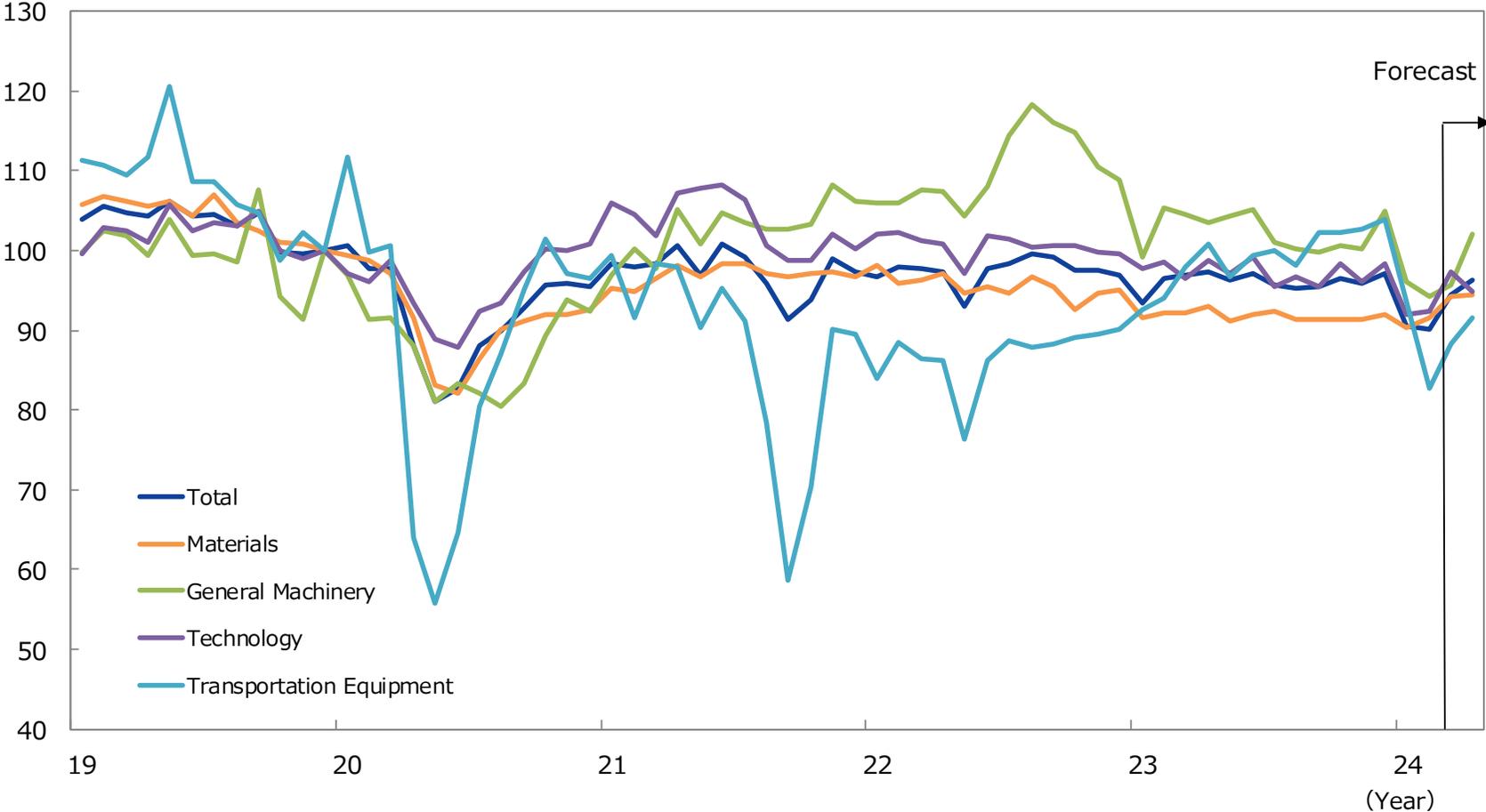
### PMI, Manufacturer & Non-Manufacturer



Note: Data is from May 2021 to April 2024.  
Source: Bloomberg, SMDAM

# Resuming auto production to lift industrial production ahead

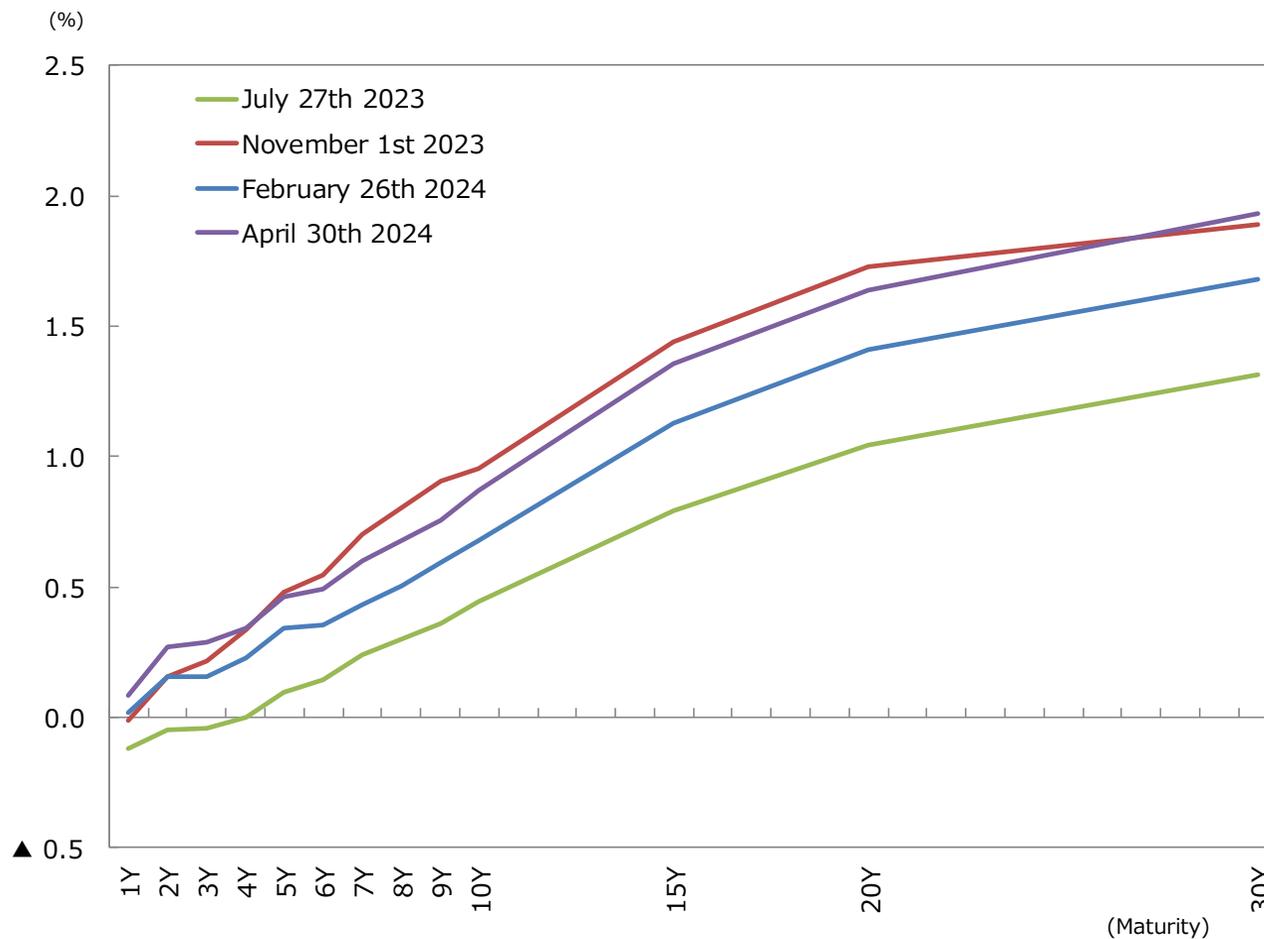
## Industrial Production (Dec. 2019=100)



Note: Data is from January 2019 to February 2024. Data after March 2024 are forecasts.  
Source: METI, SMDAM

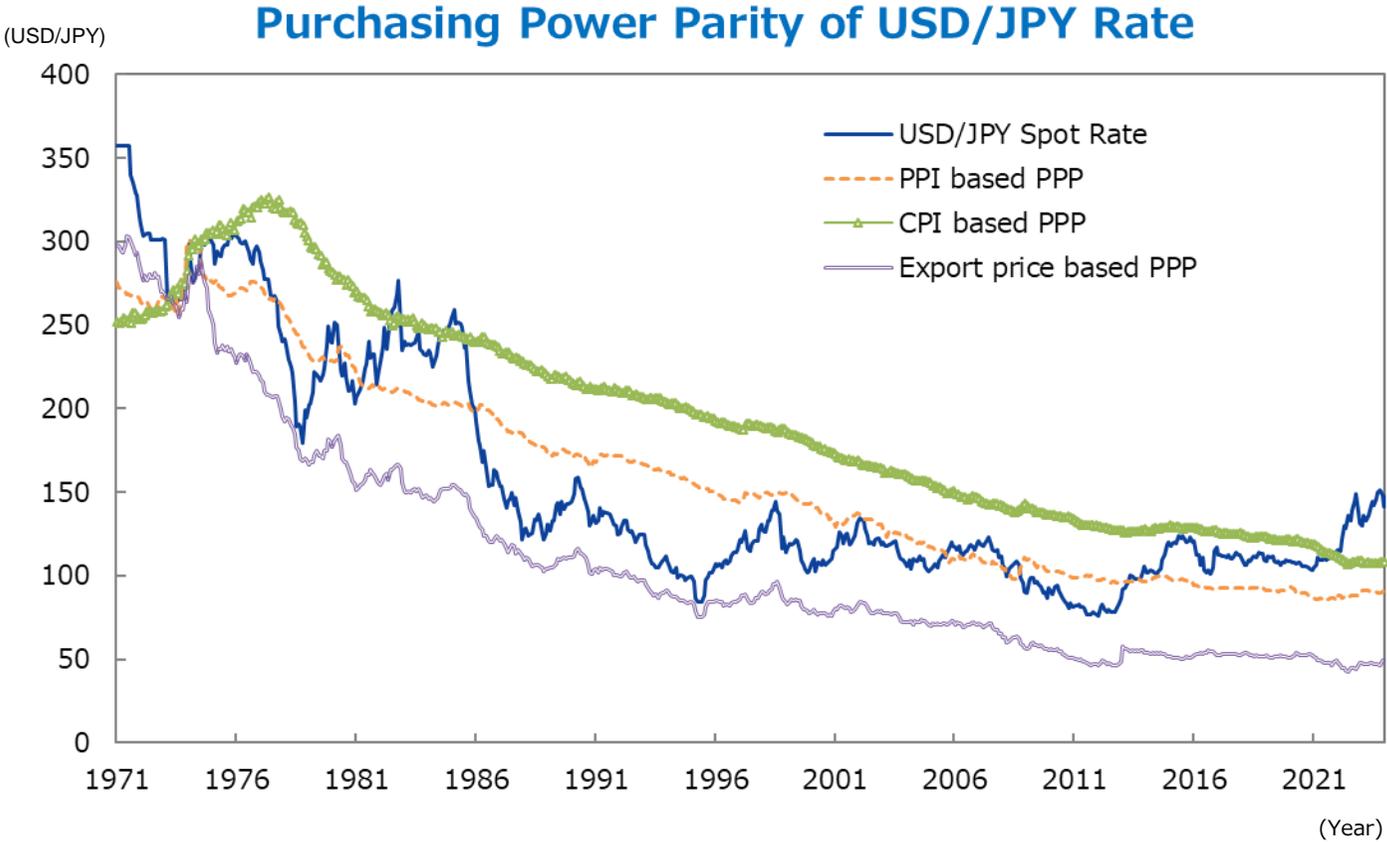
# JGB yield start pricing next move by the BOJ

## Yield Curve of Japanese Sovereign



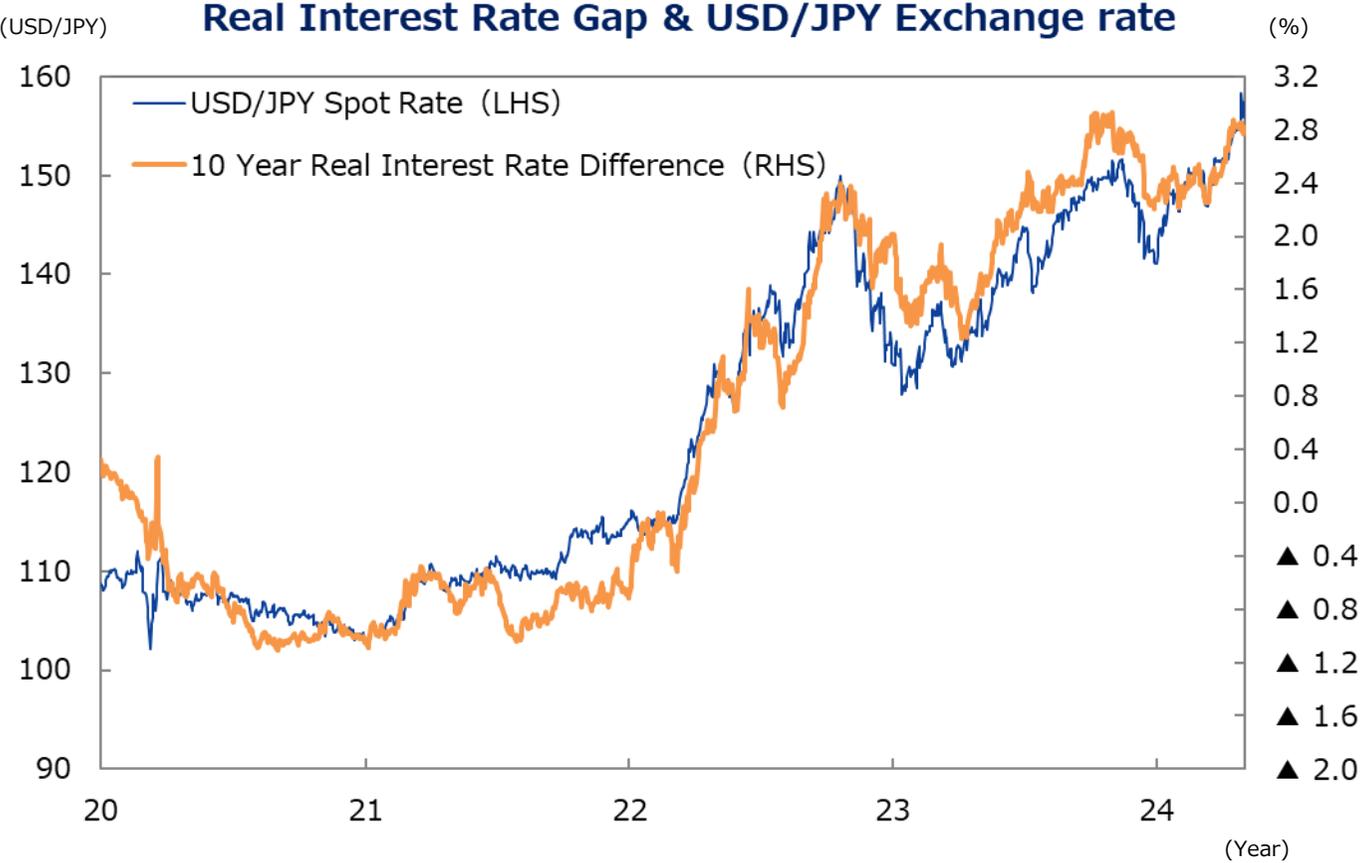
Source: Bloomberg, SMDAM

# USD/JPY rate diverges from purchasing power parity



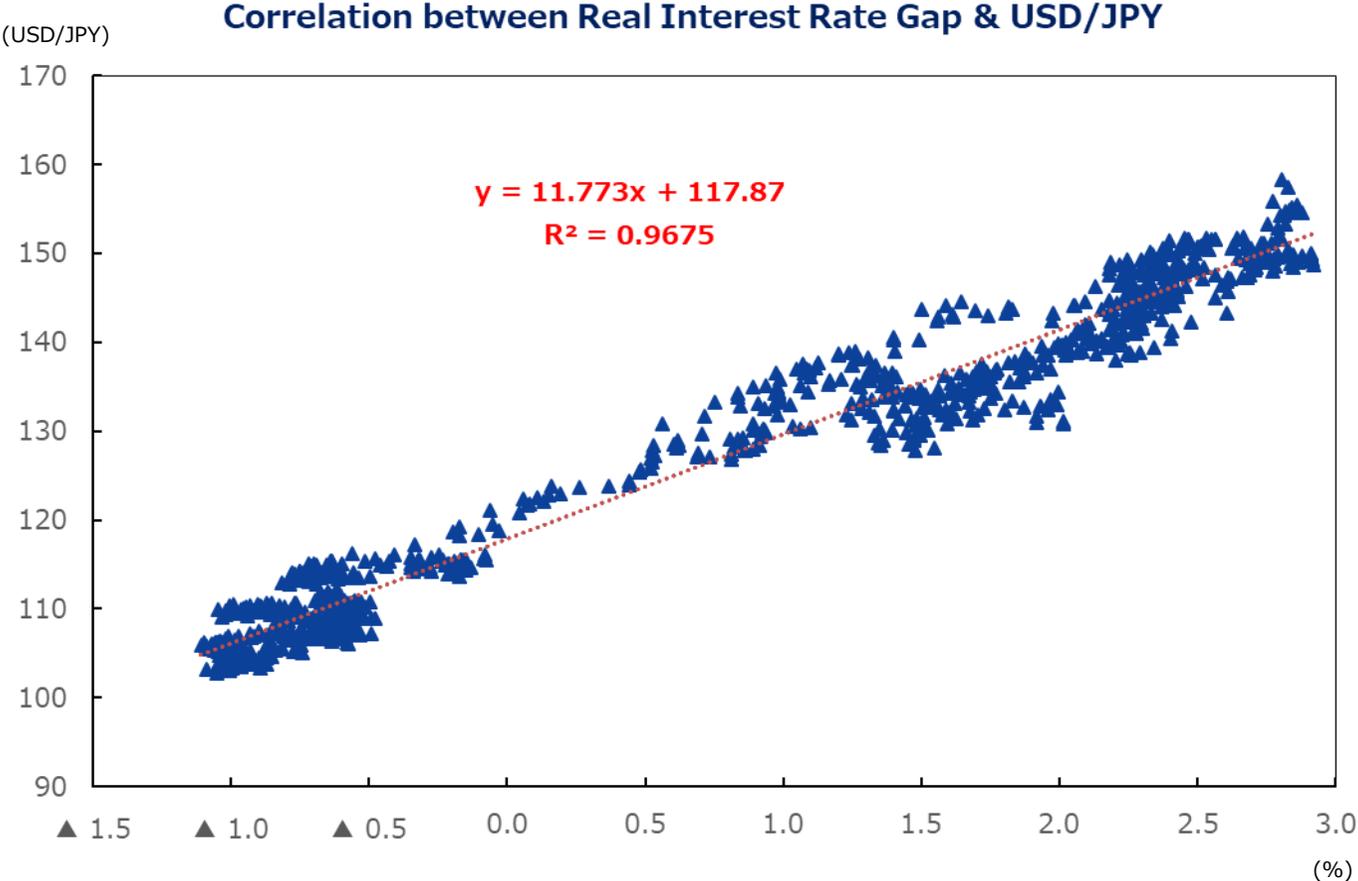
Note: Data is from January 1971 to March 2024.  
Source: DOL, Bank of Japan, SMDAM

# USD/JPY rate keeps correlation with real yield gap



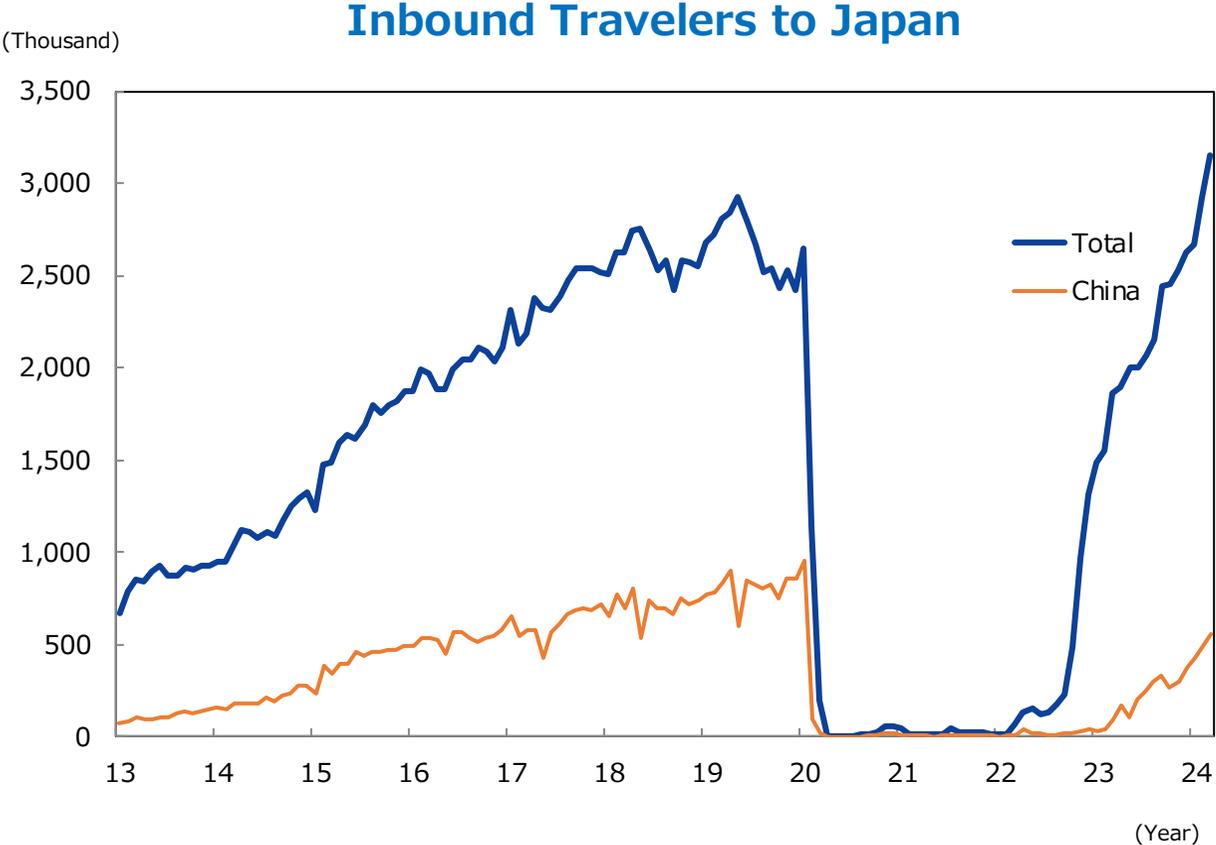
Note: Real interest rates are 10 year government bond yields. Data is from 1st January 2020 to 30th April 2024.  
Source: Bloomberg, SMDAM

# USD/JPY rate keeps correlation with real yield gap



Note: Real interest rates are 10 year government bond yields. Data is from 1st April 2020 to 30th April 2024.  
Source: Bloomberg, SMDAM

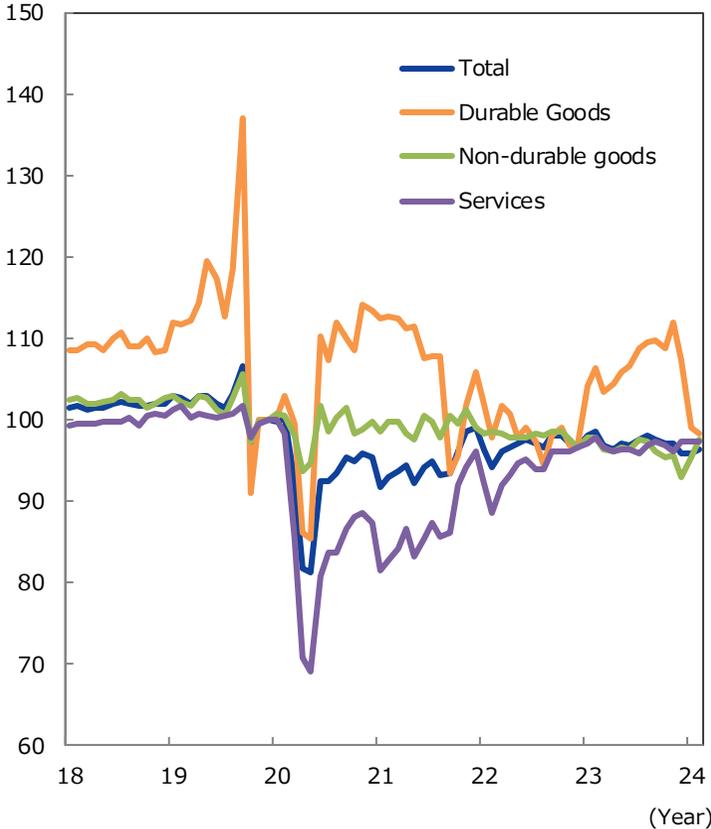
# Inbound travel breaks historical high, over 3 million per month



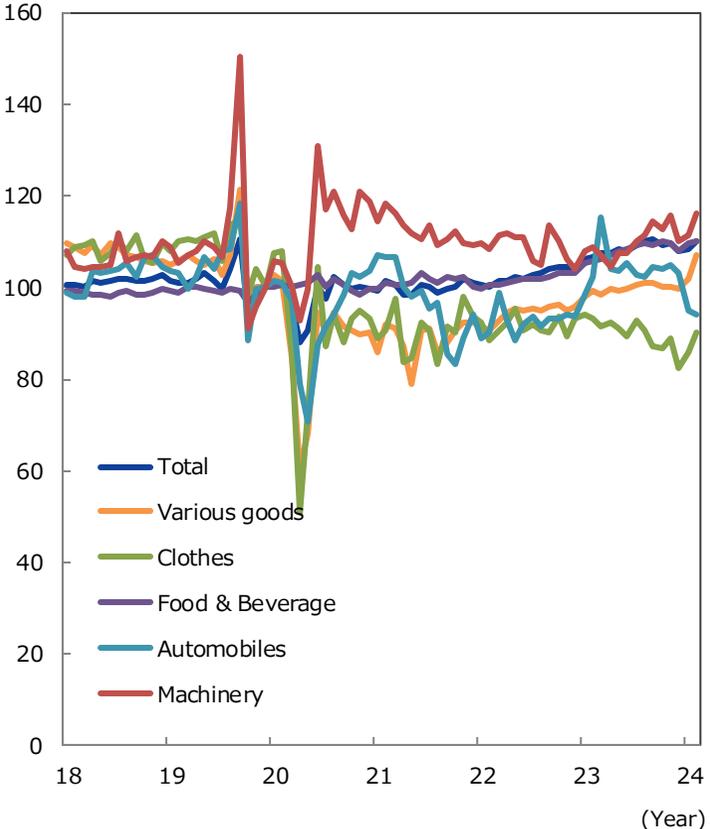
Note: Data is from January 2013 to March 2024. Data is non-seasonally adjusted.  
Source: Japan National Tourism Organization, SMDAM

# Suspension of auto production pushed down durable goods sales

Consumer Activity Index (Dec. 2019 = 100)



Retail Sales (Dec. 2019 = 100)



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

# Ruling LDP completely defeated in the by-elections

## Cabinet approval rate



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

## Schedule of major events

Year	Month	Date	Event
2024	May	16	Release of Q1 GDP
		21	Multi-faceted review of Second workshop
	June	10	Revision of Q1 GDP
		13-14	Monetary Policy Meeting Cabinet decision on the broad policy End of the ordinary Diet session
		30-31	Monetary Policy Meeting Summation of annual spring wage negotiations (final session)
		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	
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	

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

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