



Outlook for Japanese Stock Market & Economy

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-November 2024-

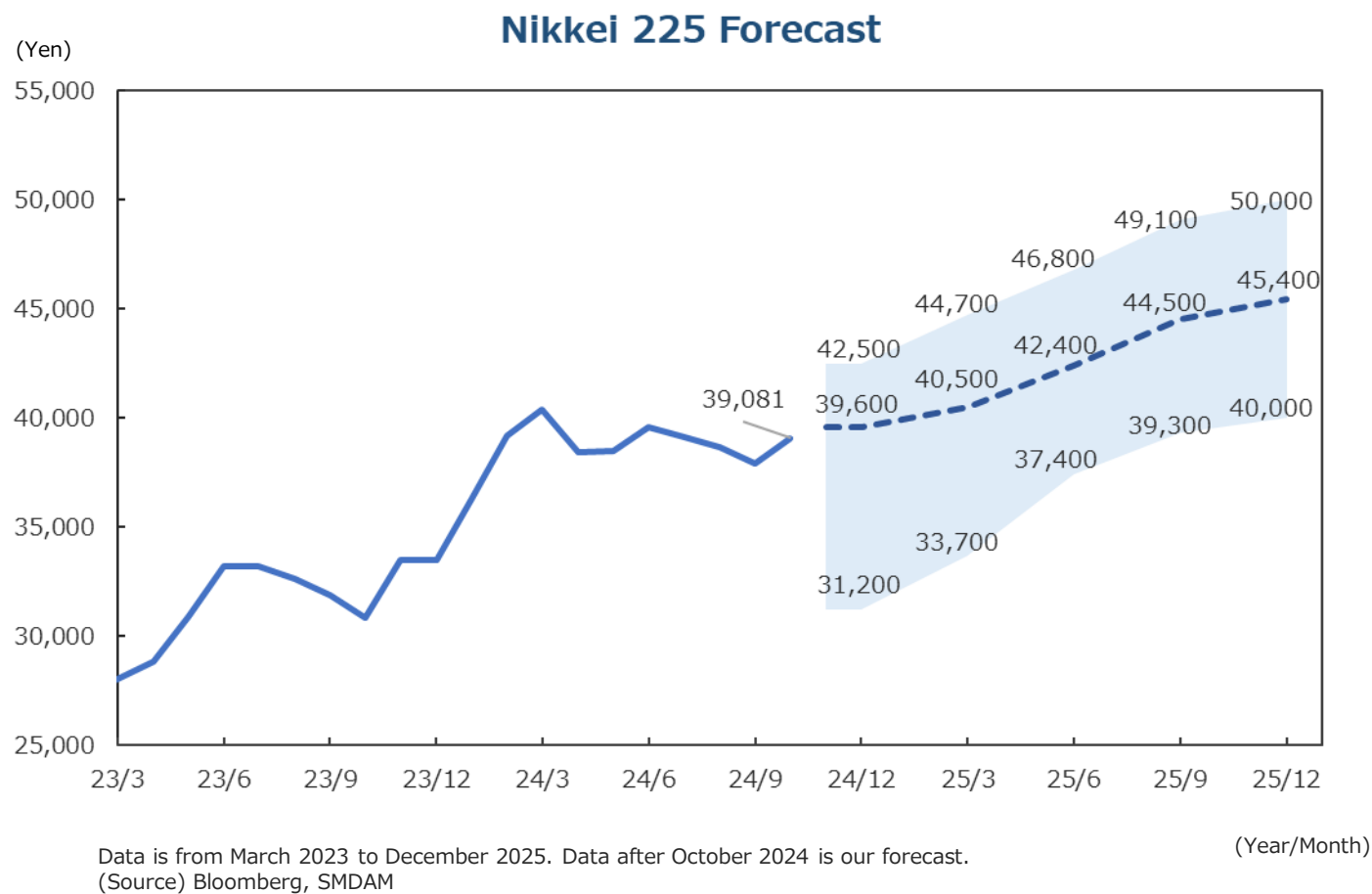


Outlook for Japanese Stock Market

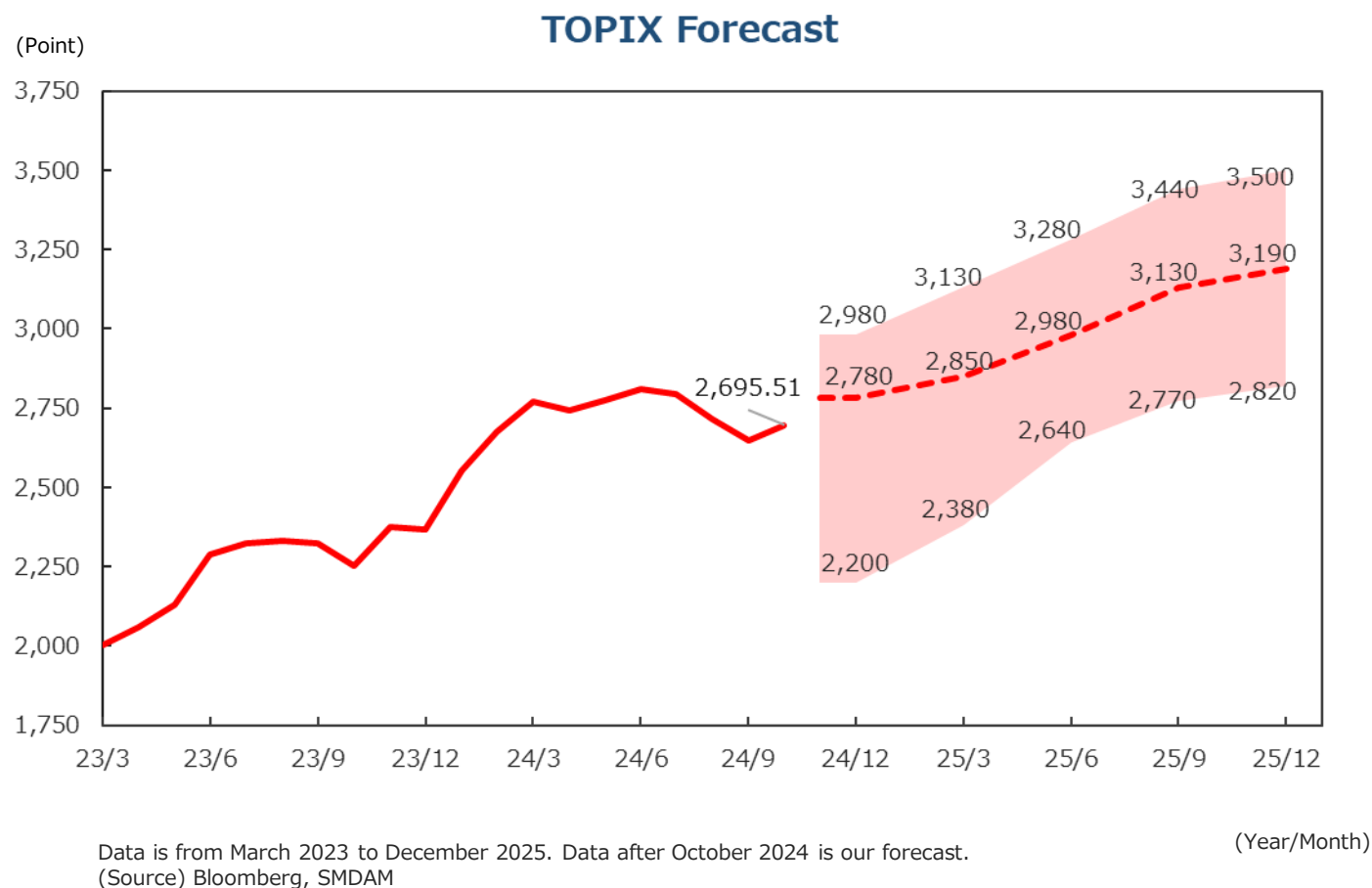
Market Outlook

- Though the ruling coalition of LDP and Komeito suffered a historic defeat in the snap general election on October 27th, losing their majority in the House of Representatives, the Japanese stock market had already factored in such a scenario. As a result, buybacks have been dominating the market in the days following the election.
- We anticipate the recent range trade may be followed by a bullish rally once the future path of US monetary policy becomes clearer and market volatility settles.
- We estimate the Nikkei 225 will surpass the 40,000 mark again in the near future and reach 45,000 by the end of CY 2025.
- The election result have had both positive and negative effects on the market, but as it stands, the positive seems to outweigh the negatives slightly. PM Ishiba and his administration are likely to change their economic policy to be more accommodative and market-friendly to maintain support without holding the decisive power in the Diet.

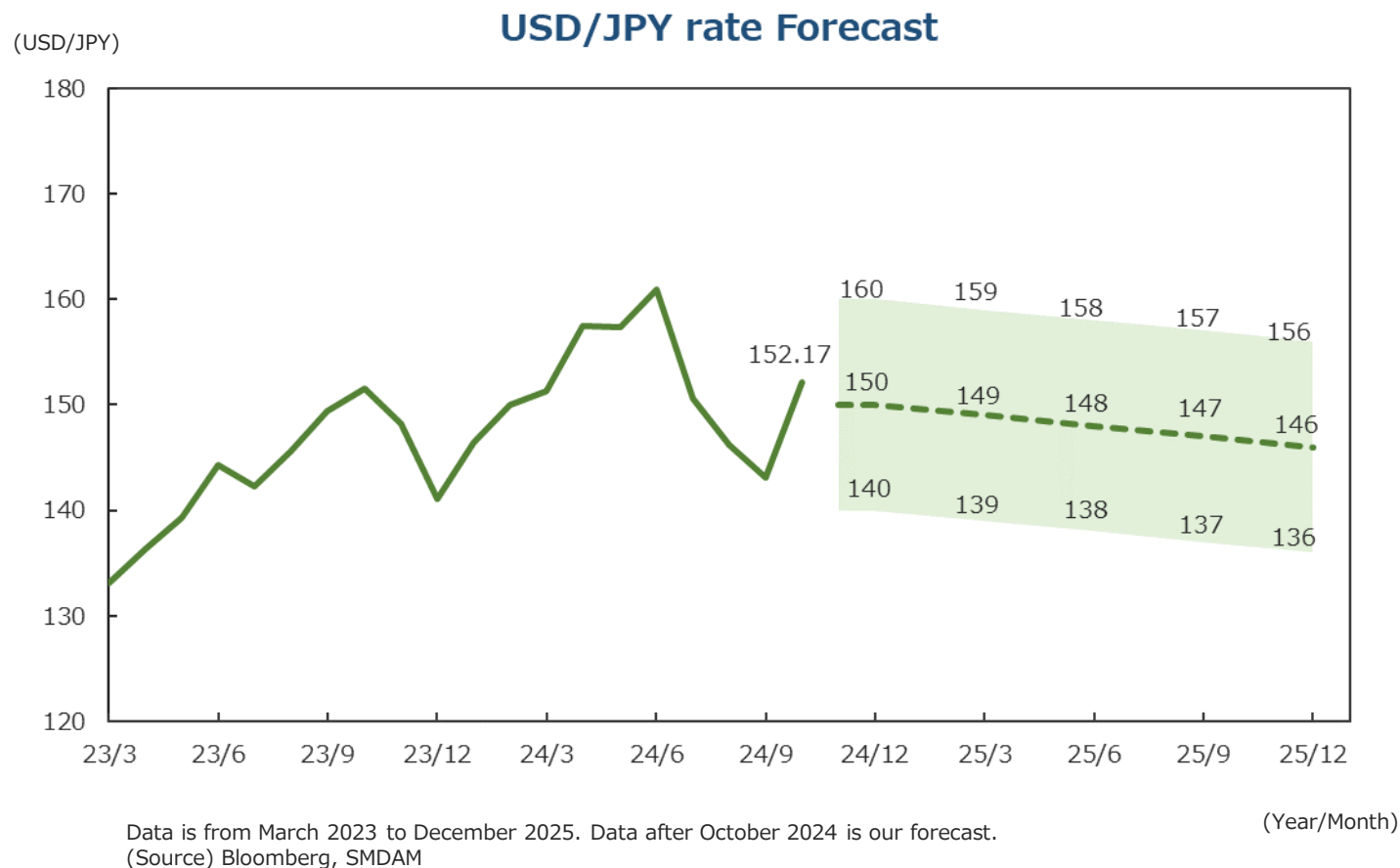
We foresee bullish perspective of Japanese equities



We foresee bullish perspective of Japanese equities



Narrowing interest rate gap weighing on USD/JPY rate ahead



Upside / Downside risk scenarios

■ Upside Risks

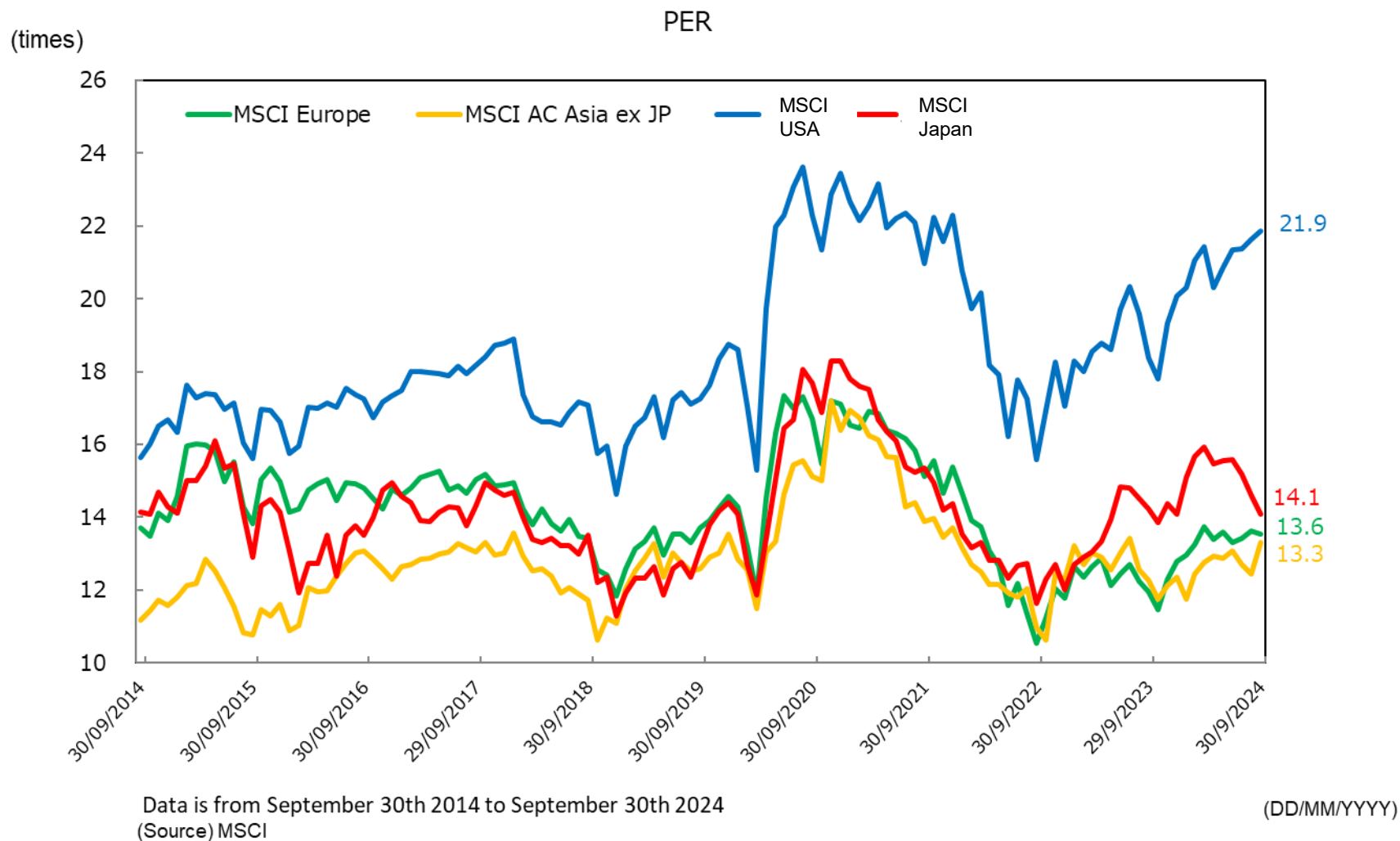
- Diminishing concerns over the US economy
- Further improvements of corporate governance, led by Tokyo Stock Exchange

■ Downside Risks

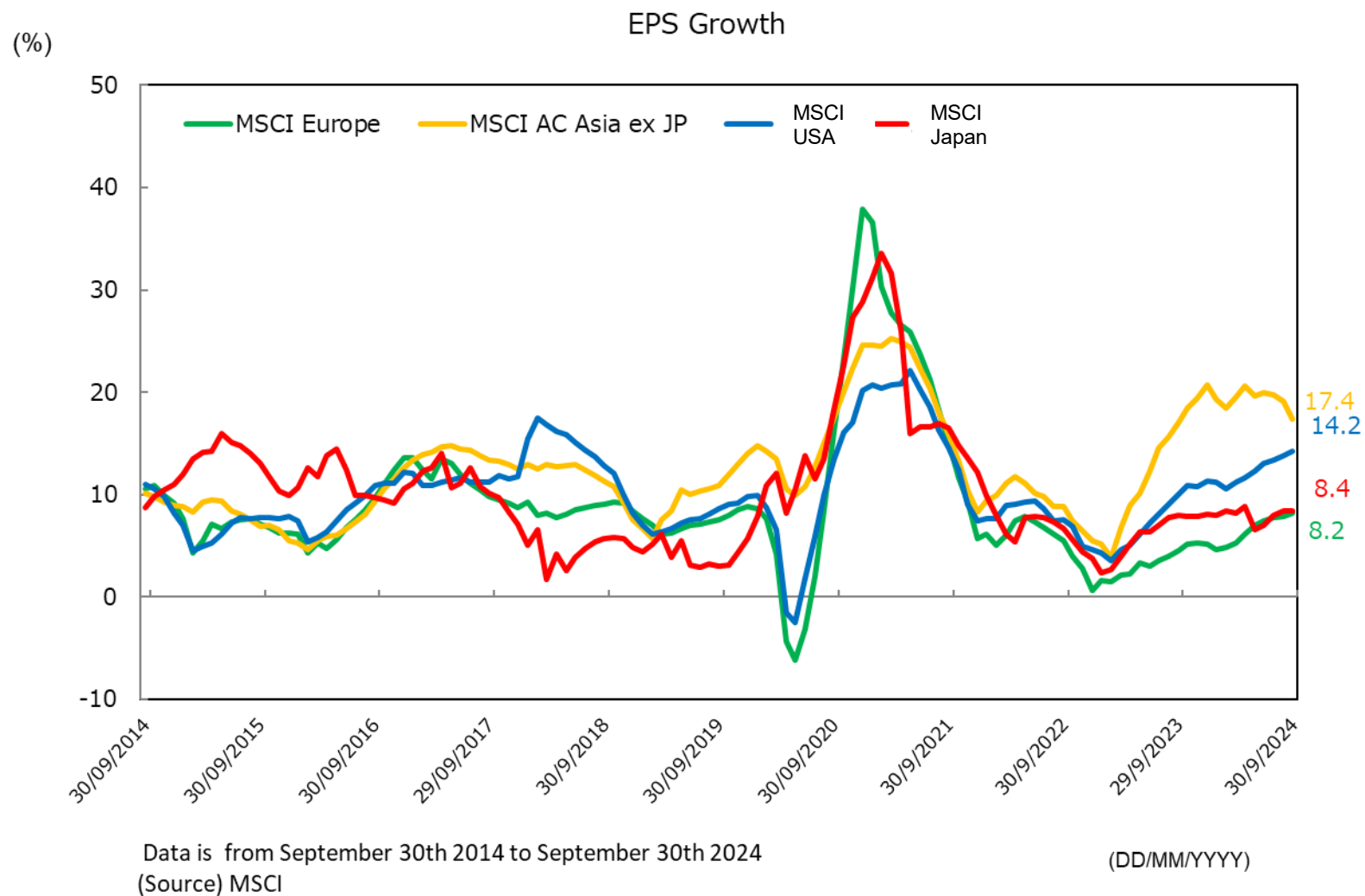
- Tighter fiscal policy aimed at achieving the primary surplus
- Excessive and rapid appreciation of the JPY, impacting the corporate earnings
- Growing political uncertainty



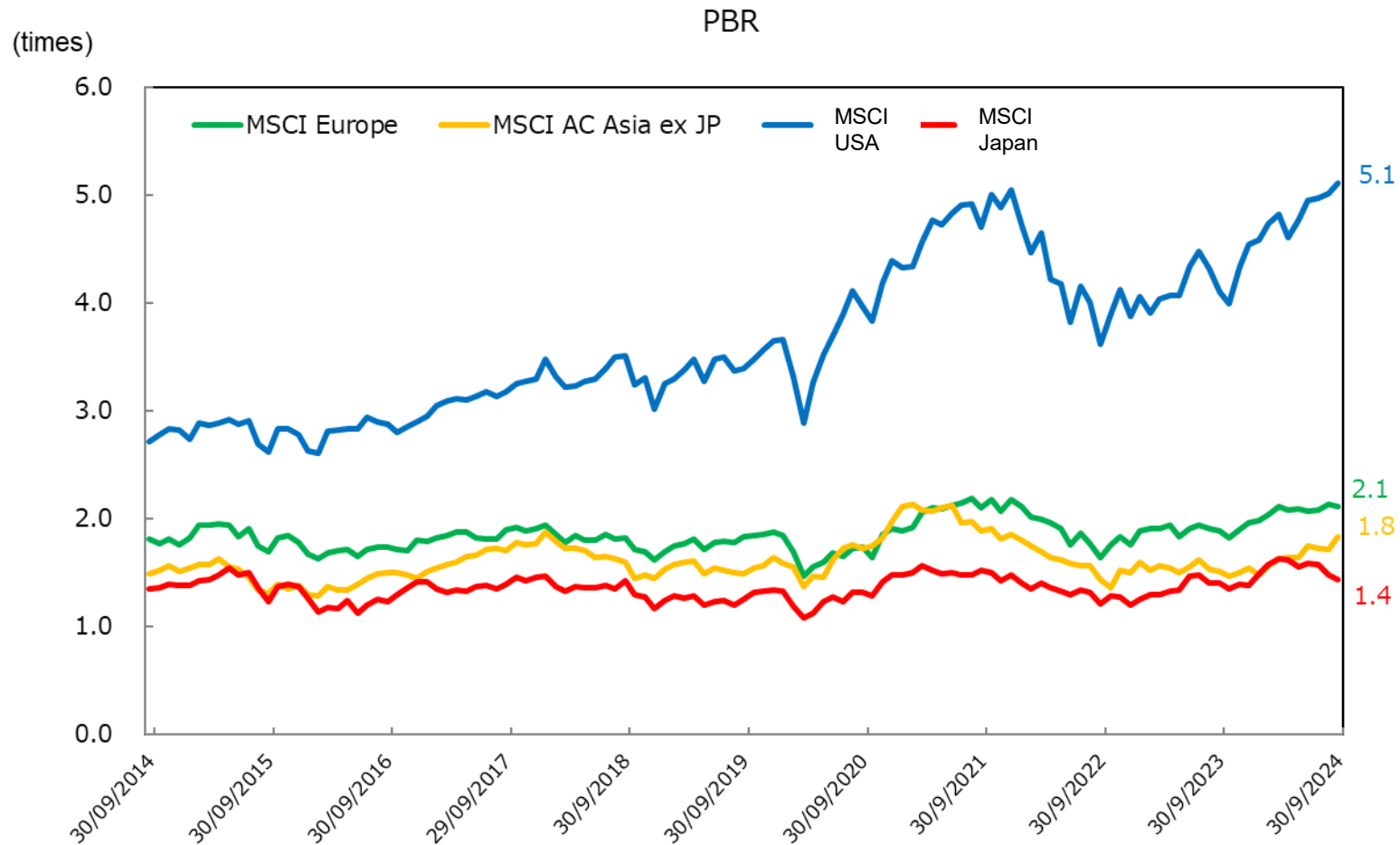
P/E ratio declined sharply due to recent market correction



Earnings growth keeps its momentum



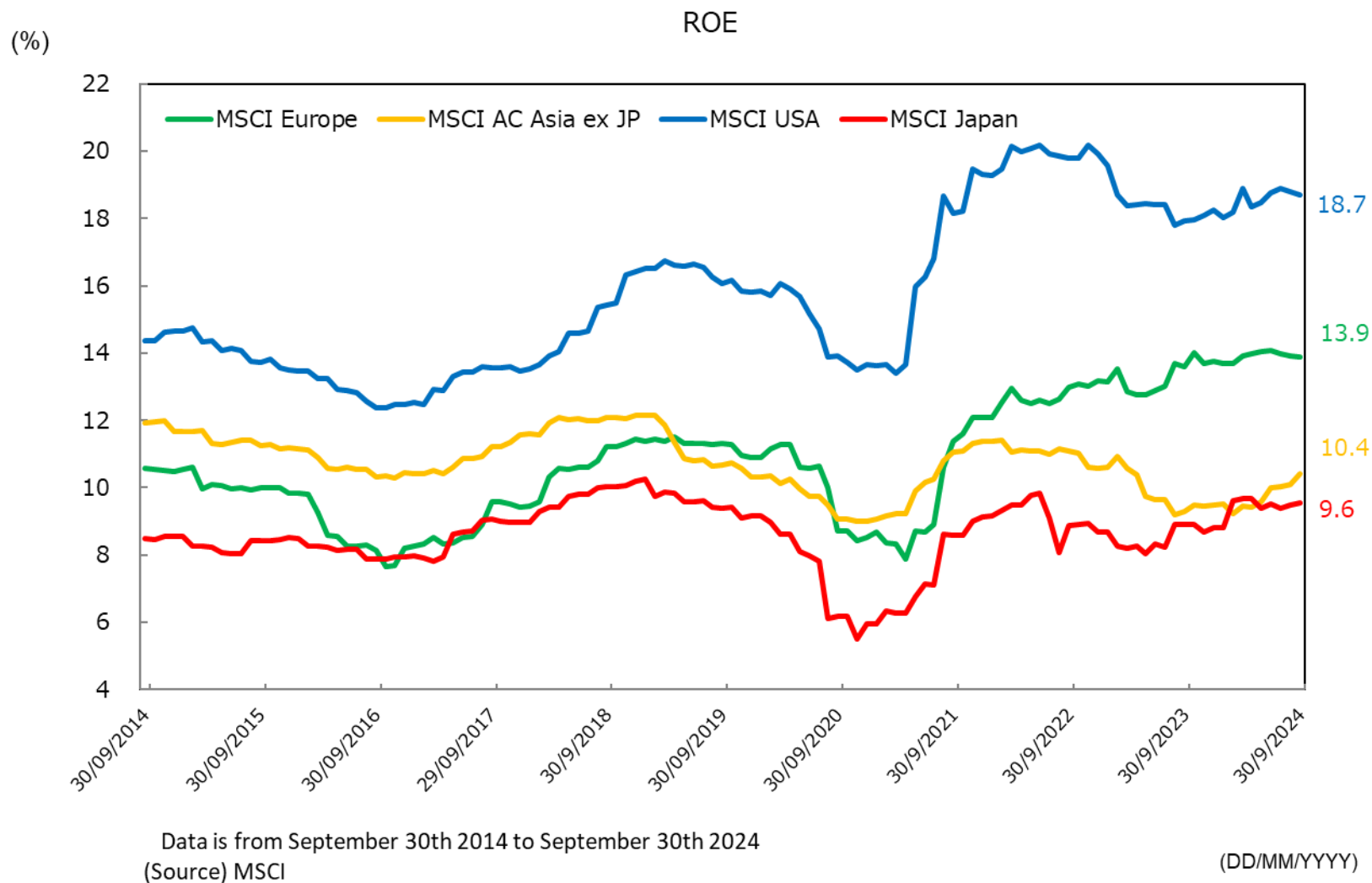
Market correction brought P/B ratio to the lowest in 2024



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

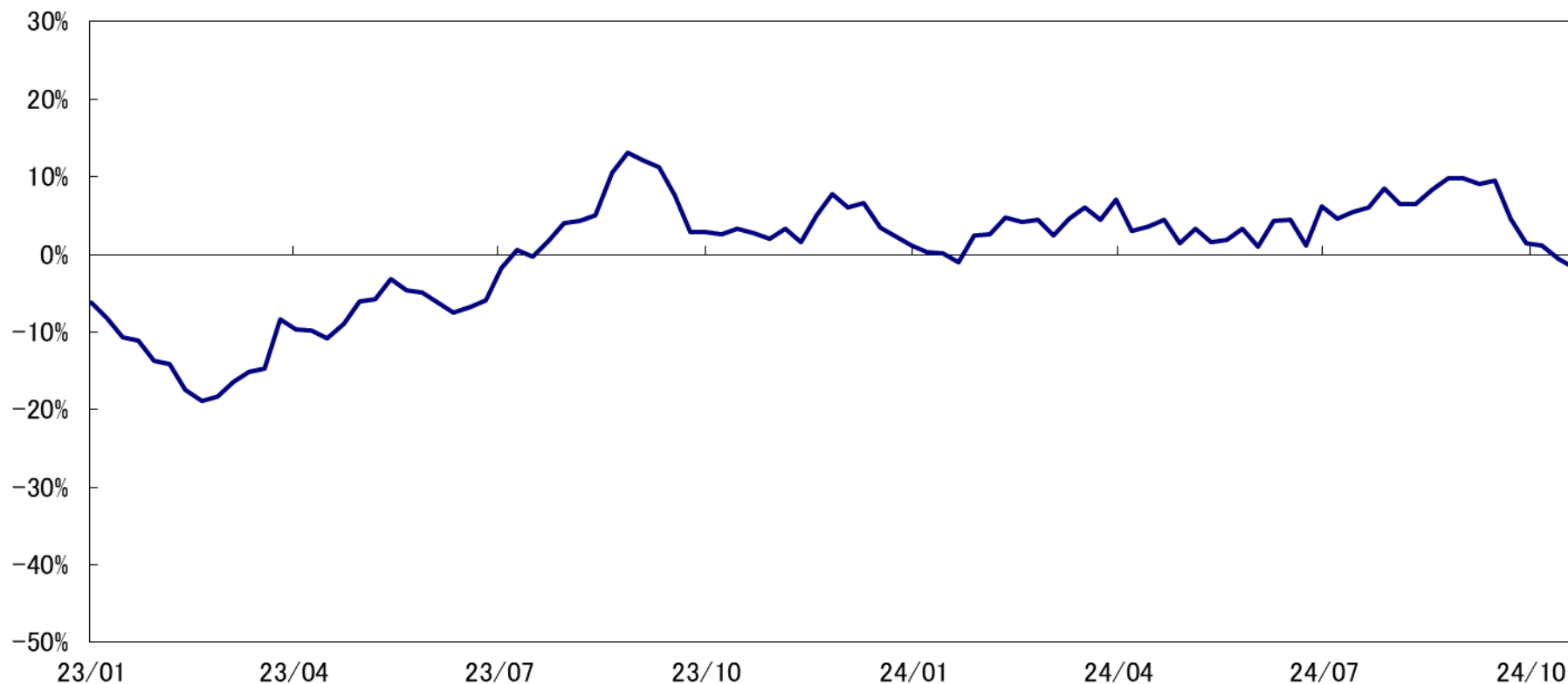
(DD/MM/YYYY)

Earnings growth maintains upward trend of ROE



Earnings revision turned negative just before reporting season

TOPIX Revision Index

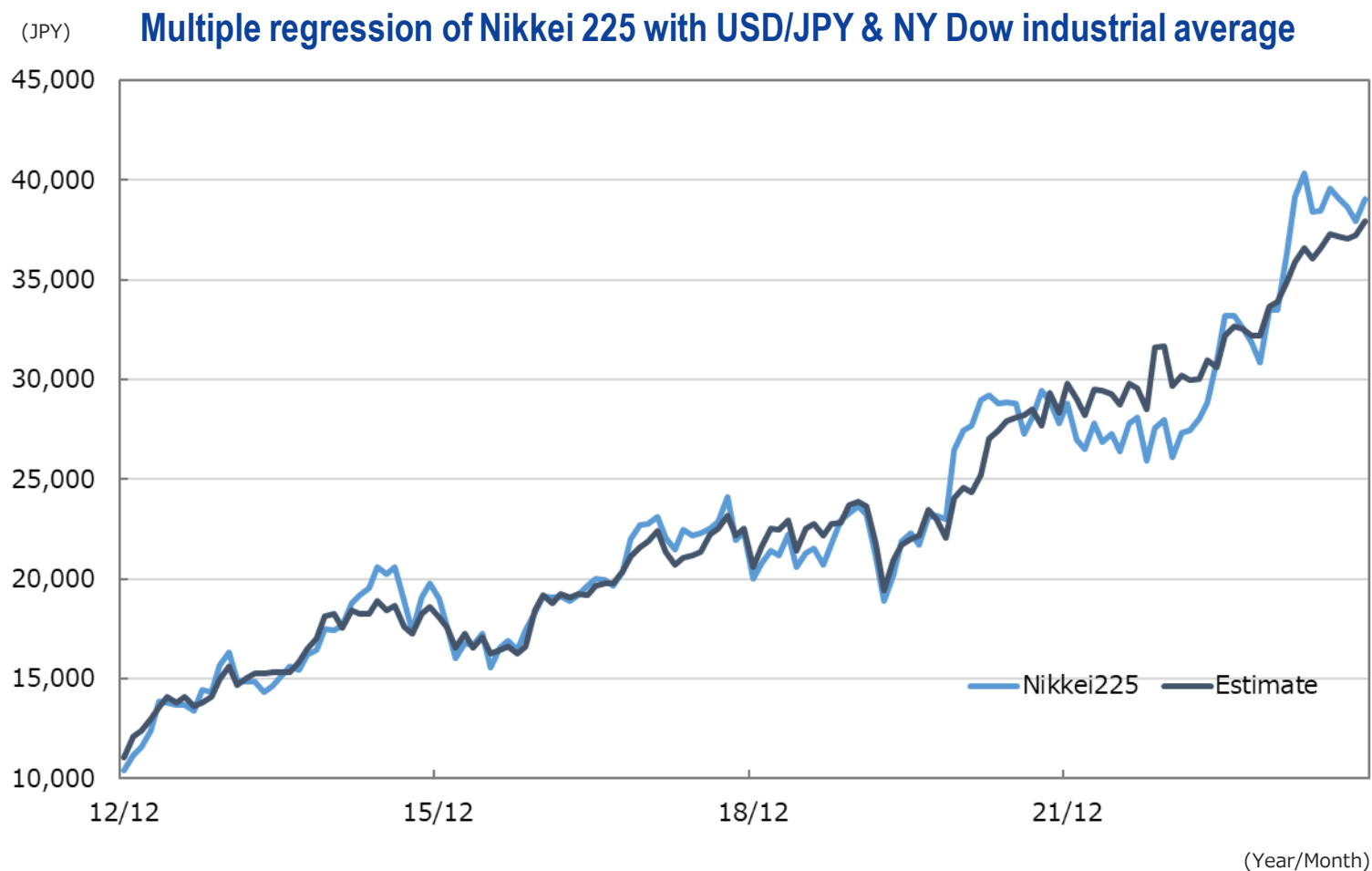


Data is from January 5th 2023 to October 24th 2024
(Source) Datastream, IBES

(YY/MM)



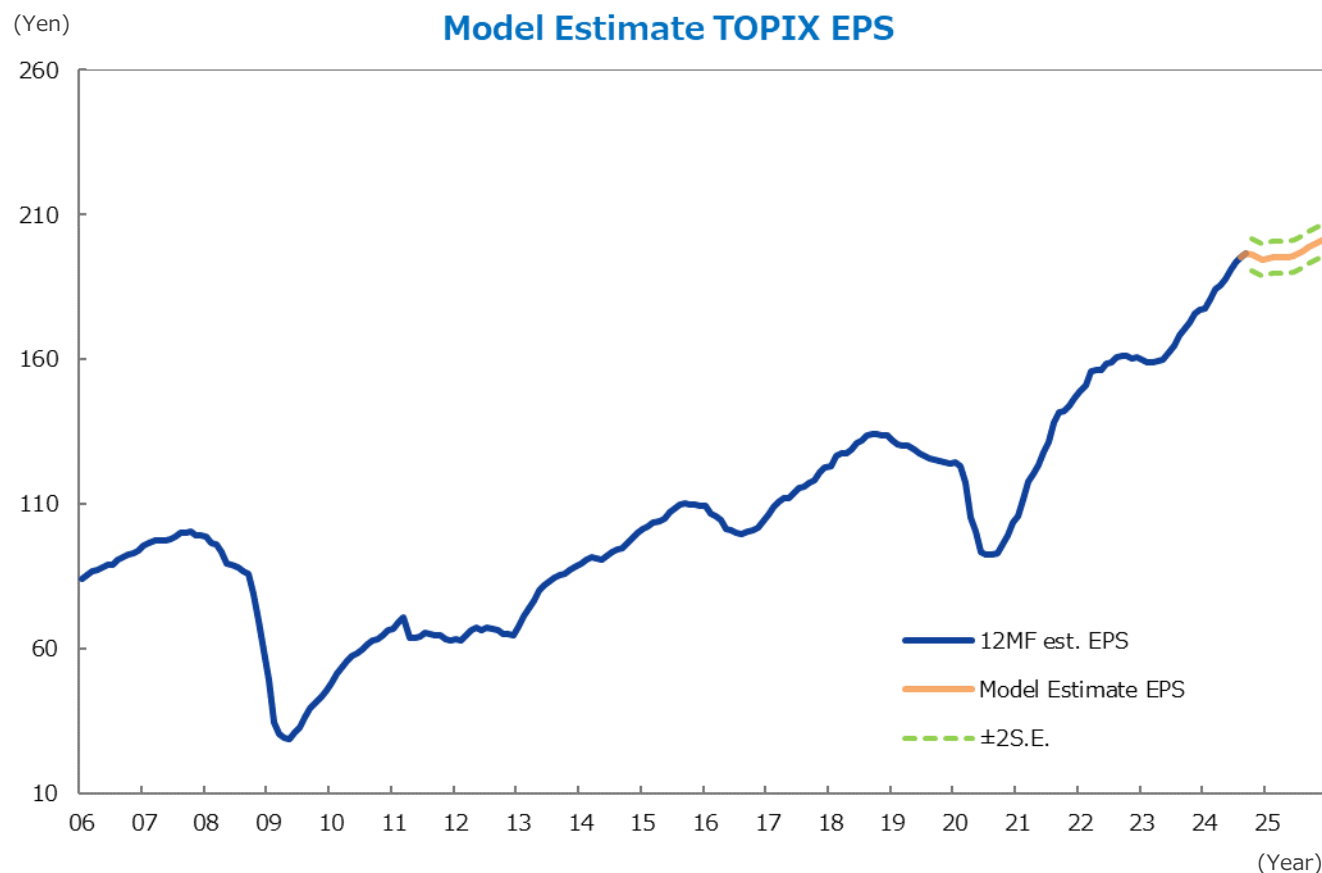
Stronger USD/JPY and rally of US equity lift Nikkei 225



Data is from December 2012 to October 2024.
(Source) SMDAM, Bloomberg

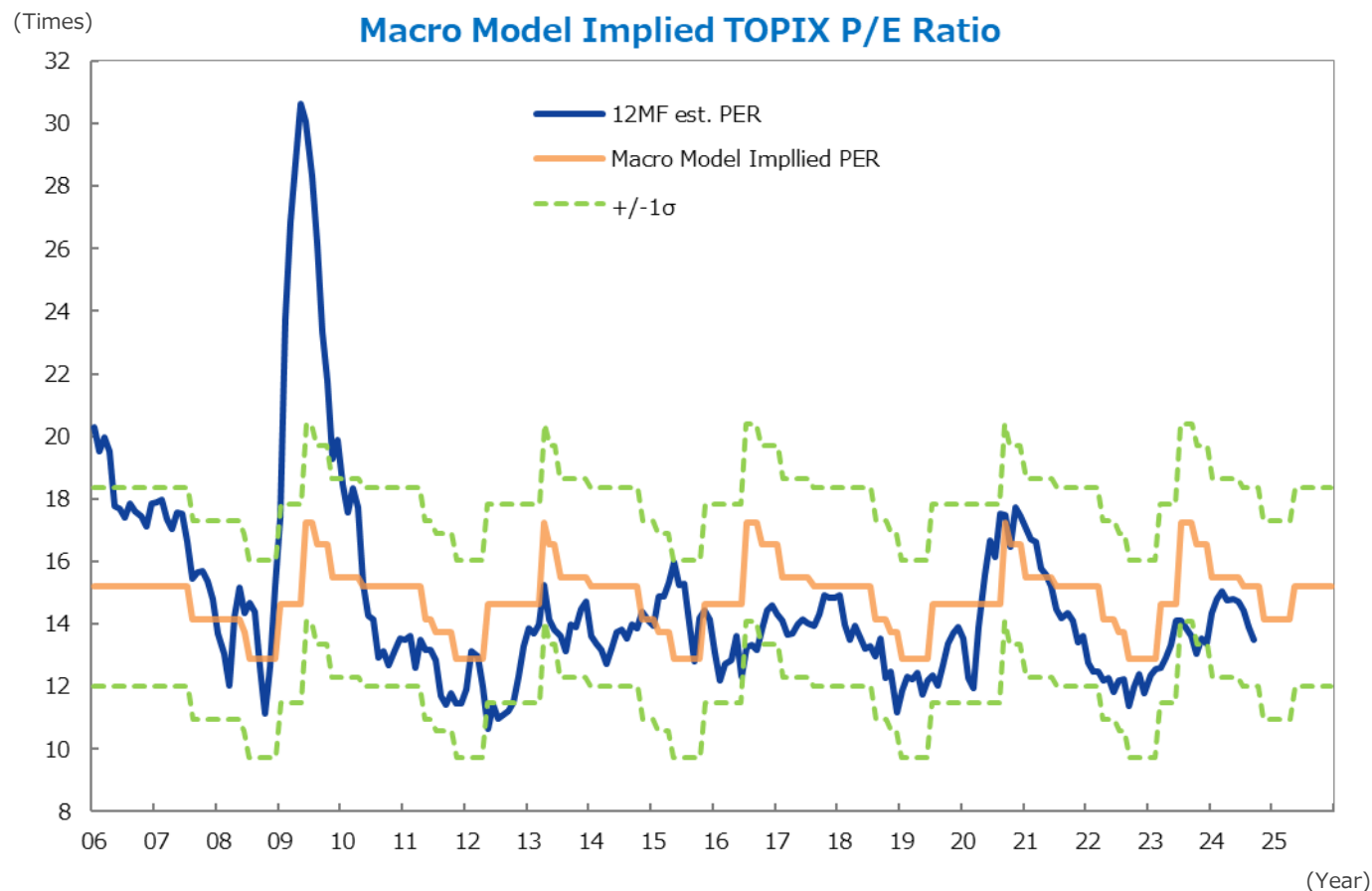


Quant model indicates EPS growth to slow in the near future



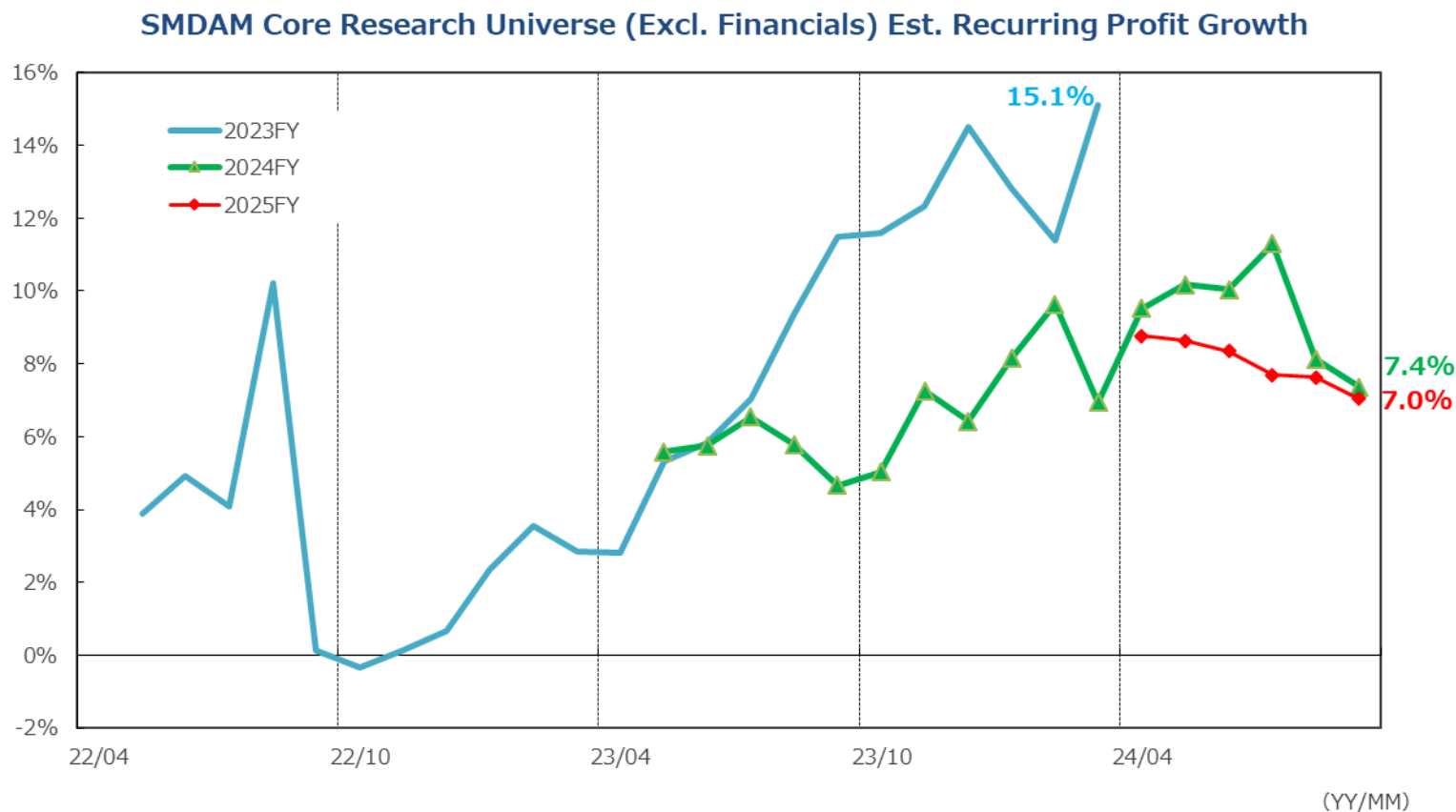
Note: Consensus data is from January 2006 to September 2024. Model estimate Data is from October 2024 to December 2025.
Source: SMDAM

P/E ratio has declined temporally as quant model had predicted



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

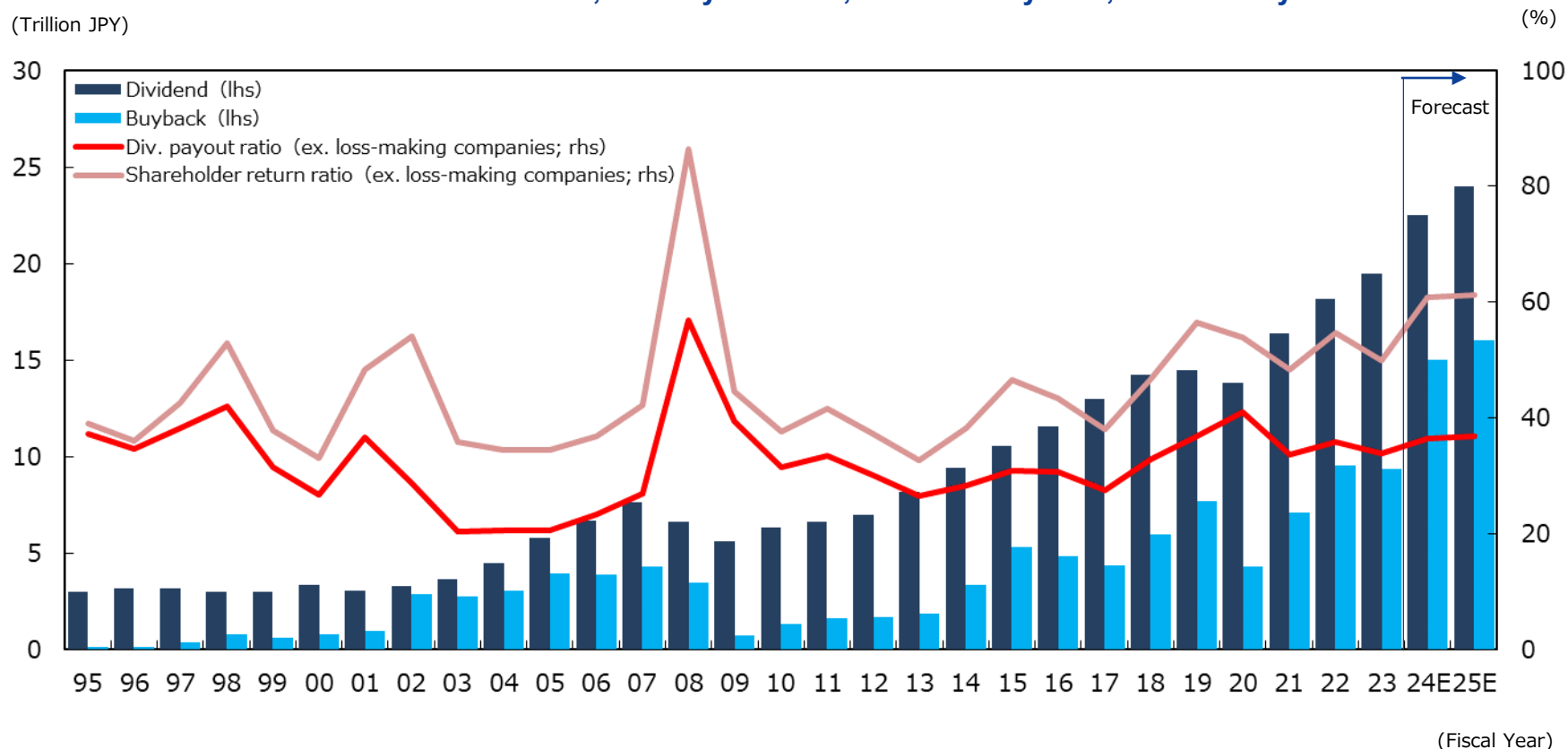
SMDAM in-house analysts see slowing earnings momentum



Note: Data is as of 10th October 2024, SMDAM Core Universe (Excl. Financials) consists of 398 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

Big swing from large value to 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	-6.83	-0.55	11.76	18.37	40.70	31.83	62.22
Total Value	-8.61	-3.10	15.13	18.22	52.77	55.59	74.28
Top Cap Value	-11.17	-4.05	20.40	20.79	62.18	68.59	102.04
Large Cap Value	-9.32	-3.41	16.22	18.71	55.07	59.02	79.19
Mid Cap Value	-7.42	-2.76	12.35	16.62	46.82	47.96	52.29
Small Cap Value	-5.07	-1.65	10.29	15.99	42.81	41.04	53.60
Micro Cap Value	-5.63	-0.71	8.26	15.40	40.09	38.86	48.08
Total Growth	-5.12	1.93	8.84	18.83	30.09	12.39	49.15
Top Cap Growth	-7.19	1.83	10.81	22.15	36.71	17.07	60.17
Large Cap Growth	-5.40	1.97	9.65	19.55	32.65	14.32	53.70
Mid Cap Growth	-1.75	2.27	7.53	14.89	25.55	9.50	43.03
Small Cap Growth	-2.48	1.54	1.97	12.65	10.62	-2.87	15.51
Micro Cap Growth	-4.22	-2.08	-1.59	9.35	6.10	-9.10	12.01
Top Cap Total	-8.78	-0.54	14.35	21.28	47.23	37.26	76.84
Large Cap Total	-7.24	-0.56	12.55	18.99	42.71	33.38	66.36
Mid Cap Total	-4.97	-0.57	10.11	15.81	36.29	28.00	52.24
Small Cap Total	-4.11	-0.47	6.97	14.57	29.40	22.40	38.74
Micro Cap Total	-5.18	-1.16	4.81	13.25	27.85	21.24	36.51

Note : As of 24th October 2024
(Source) Bloomberg





Outlook for Japanese Economy



Current status & Outlook of Japanese economy

[Current Status]

- **The economy is recovering.** Although some economic statistics, such as the “industrial production (August)”, have been weaker than expected due to the arrival of large typhoons, corporate production forecasts have been optimistic. The Bank of Japan's September “Tankan survey” indicates stable business conditions, and CAPEX plans remain solid. The negative impact of the slowdown in overseas economies, which has been a concern, has also been limited.
- **Inflation is easing.** Nationwide core CPI rose +2.4% YOY in September, down from +2.8% in August, while Tokyo Metropolitan Area core CPI rose by +2.0% YOY in September, down from +2.4% in August. These declines reflect the decrease in electricity and gas prices supported by the government emergency measures to cope with the extreme heat.

[Outlook]

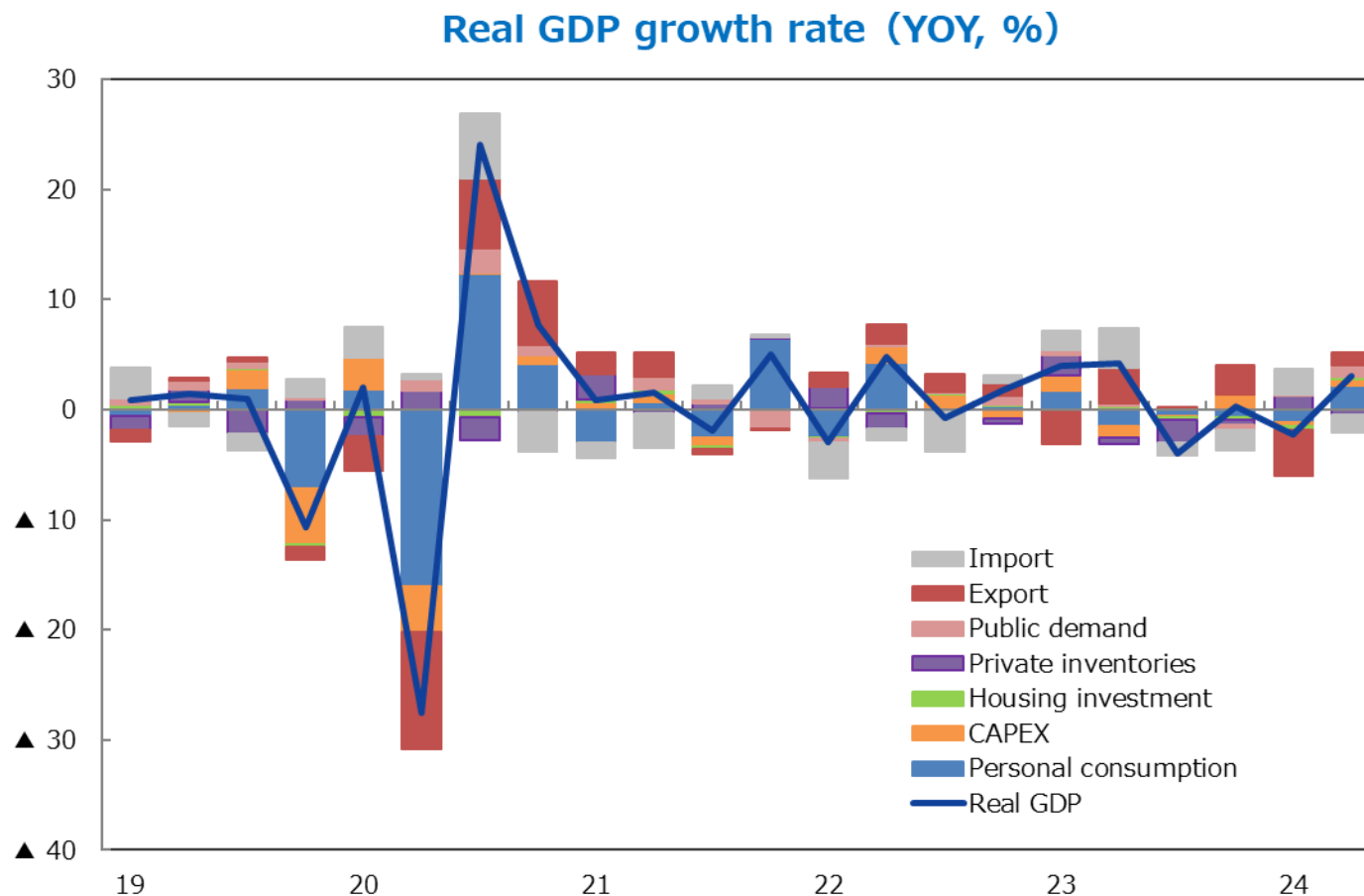
- ① **While we have maintained our real GDP growth forecast for FY 2024 at +0.4%, we have raised our estimate for FY 2025 from +0.7% to +1.0%.** The upward revision for FY 2025 reflects a change in our estimation of the size of the fiscal stimulus. Given the Ishiba administration's proactive stance towards economic measures, we now assume fiscal stimulus totaling as much as JPY 25 trillion from both central and local governments. We expect the Japanese economy to return to a moderate growth path on the back of wage hikes, solid capital expenditure (labor-saving, digitalization, greening, urban development, and semiconductor factory construction), a resilient overseas economy, and government economic measures.
- ② **We have maintained our core CPI forecast for FY2024 at +2.5%, whilst we have lowered our estimate for FY 2025 from +2.0% to +1.8%.** The downward revision for FY 2025 reflects the possibility of extending measures to counter higher inflation, such as subsidies for electricity, gas, and gasoline. Our assumption is that these measures will be reduced to half of the current scale and implemented from January to September 2025, given the upcoming House of Councillors election next summer. We estimate core CPI is likely to slow to around +1.5% YOY by the summer of 2025 due to inflation-countering measures and weakening cost-push pressure from import goods. On the other hand, wage increases are likely to lead to higher service prices. We expect core CPI will rebound to +2% YOY by the end of FY2025 as the impact of the subsidies recedes.
- ③ **We assume the new government to adopt accommodative fiscal policies.** Prime Minister Ishiba has confirmed that he will continue the Kishida administration's policies and has designated the next three years as a focused period to fully overcome deflation. In the short term, the administration has called for the formulation of economic measures with three pillars: “countering high prices,” “promoting growth in both the national and local economies,” and “ensuring the public safety and security.”
- ④ **We have changed our forecast for the Bank of Japan's monetary policy.** The new forecasts of policy rates are 0.50% in January 2025, 0.75% in July 2025 and 1.00% in January 2026 (previously: 0.50% in December 2024, 0.75% in July 2025 and 1.00% in January 2026). We have slightly delayed the timing of the next rate hike due to PM Ishiba administration's cautious stance on raising interest rates. The BoJ is expected to proceed with the next rate increase after conducting the comprehensive research on the domestic economy, inflation, and the overseas economy, particularly focusing on the United States in the “Outlook Report” in January 2025, with careful coordination with the government. After that, rate hikes are expected to be done at a gentle pace of about once every six months.

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%	3.1%	1.6%	0.8%	0.4%	1.0%
Private final consumption expenditure	-0.9%	-4.8%	1.8%	2.7%	-0.6%	0.6%	1.0%
Private housing investment	2.6%	-7.4%	0.3%	-3.3%	0.3%	-1.5%	-0.9%
Private-sector capital investment	-1.3%	-5.7%	3.2%	4.1%	0.3%	2.0%	1.5%
Private inventory investment	-0.2%	-0.2%	0.5%	0.1%	-0.2%	0.0%	0.0%
Public fixed capital formation	1.6%	4.9%	-6.5%	-6.1%	0.7%	0.0%	0.1%
Net export contribution	-0.5%	-0.6%	0.8%	-0.5%	1.4%	-0.3%	0.0%
Exports of goods and services	-2.3%	-10.0%	12.5%	4.9%	2.8%	2.1%	3.2%
Imports of goods and services	0.2%	-6.3%	7.4%	7.3%	-3.2%	3.5%	3.2%
Nominal GDP	0.0%	-3.2%	3.0%	2.5%	4.9%	3.1%	2.7%
GDP deflator	0.8%	0.7%	-0.1%	0.9%	4.0%	2.7%	1.7%
Industrial Production Index	-3.5%	-9.6%	5.6%	-0.3%	-1.9%	0.2%	2.3%
Consumer Price Index (Core)	0.4%	-0.6%	0.1%	3.0%	2.8%	2.5%	1.8%
Domestic corporate goods price index	0.1%	-1.5%	7.1%	9.6%	2.4%	2.1%	0.7%
Employee compensation	2.0%	-1.5%	2.1%	2.4%	1.8%	3.8%	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

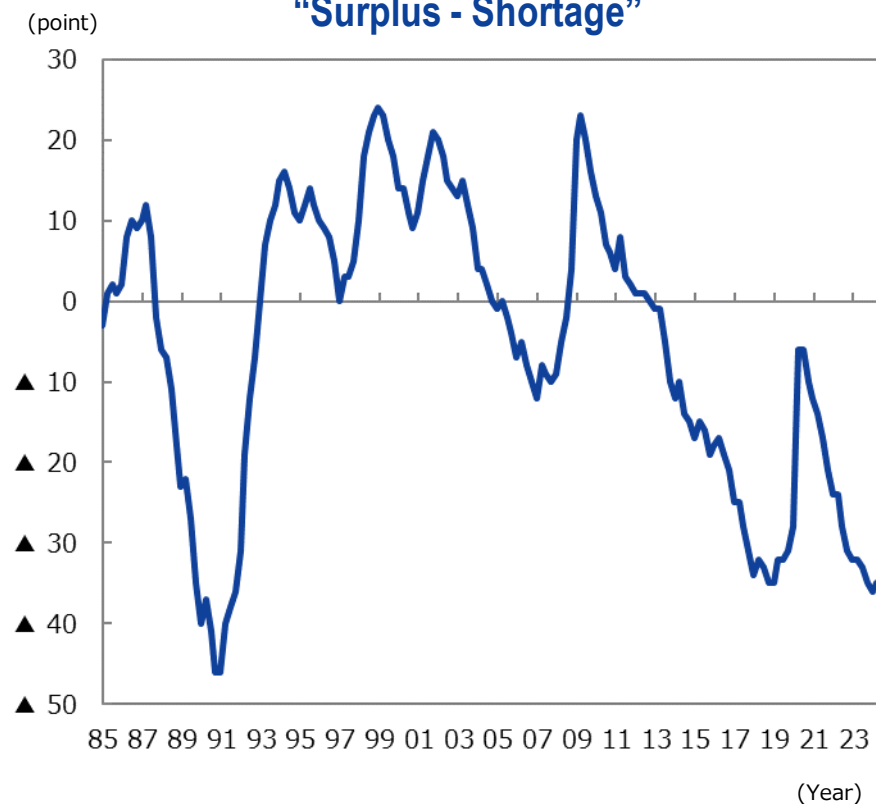
GDP growth back to be positive again



Note: Data is from Q1 2019 to Q2 2024.
Source: Cabinet office, SMDAM

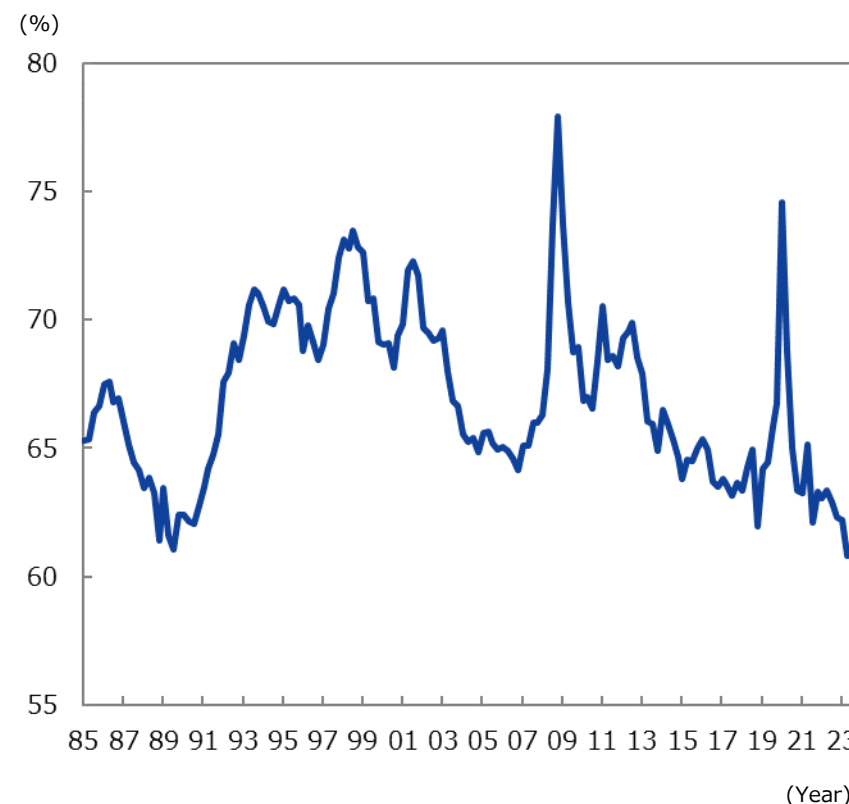
Conundrum of Japanese labor market

Employment Sufficiency Index “Surplus - Shortage”



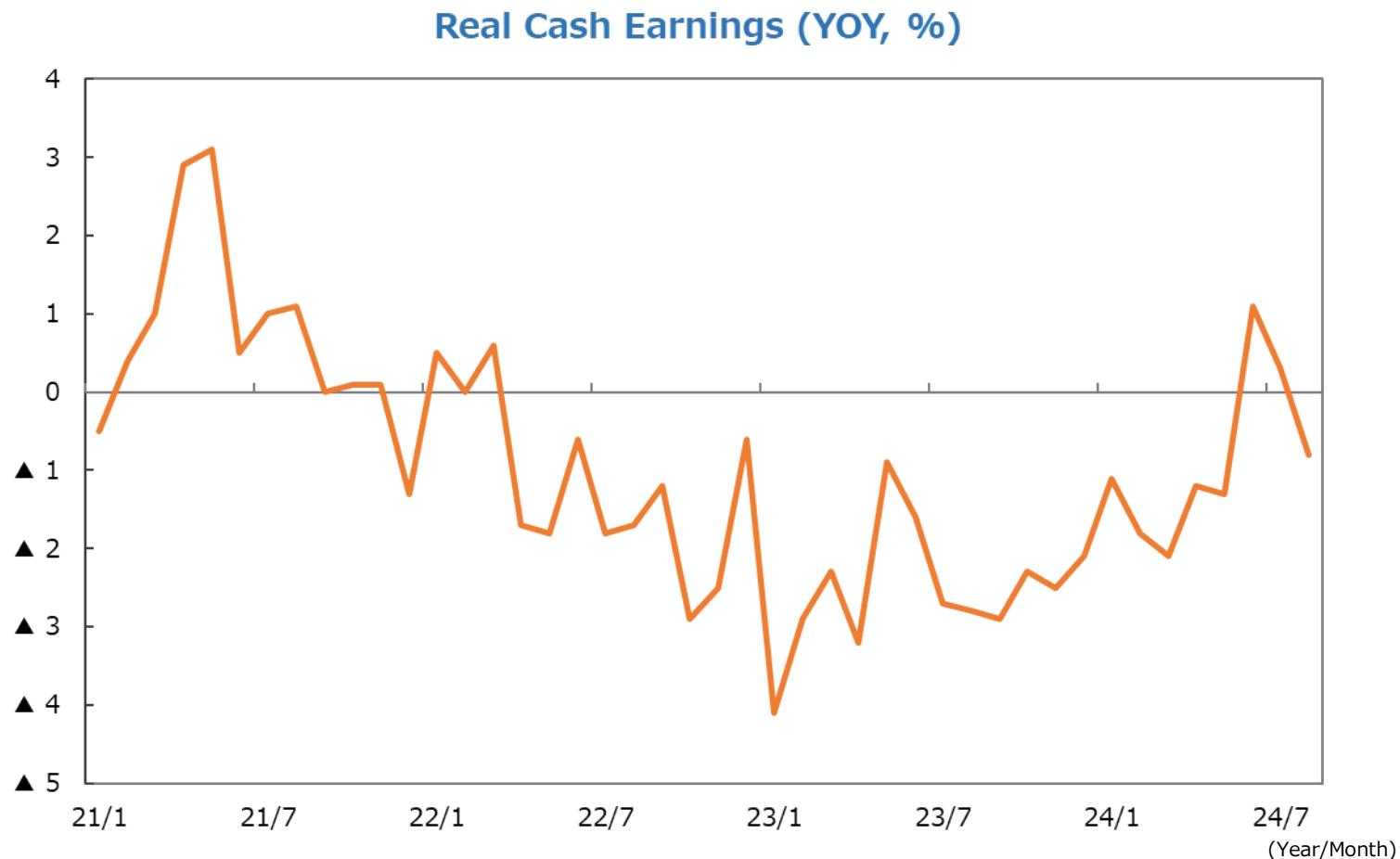
Note: Data is from April 1985 to September 2024.
Source: The bank of Japan, SMDAM

Labor Distribution Rate



Note: Data is from April 1985 to April 2024.
Source: Ministry of finance, SMDAM

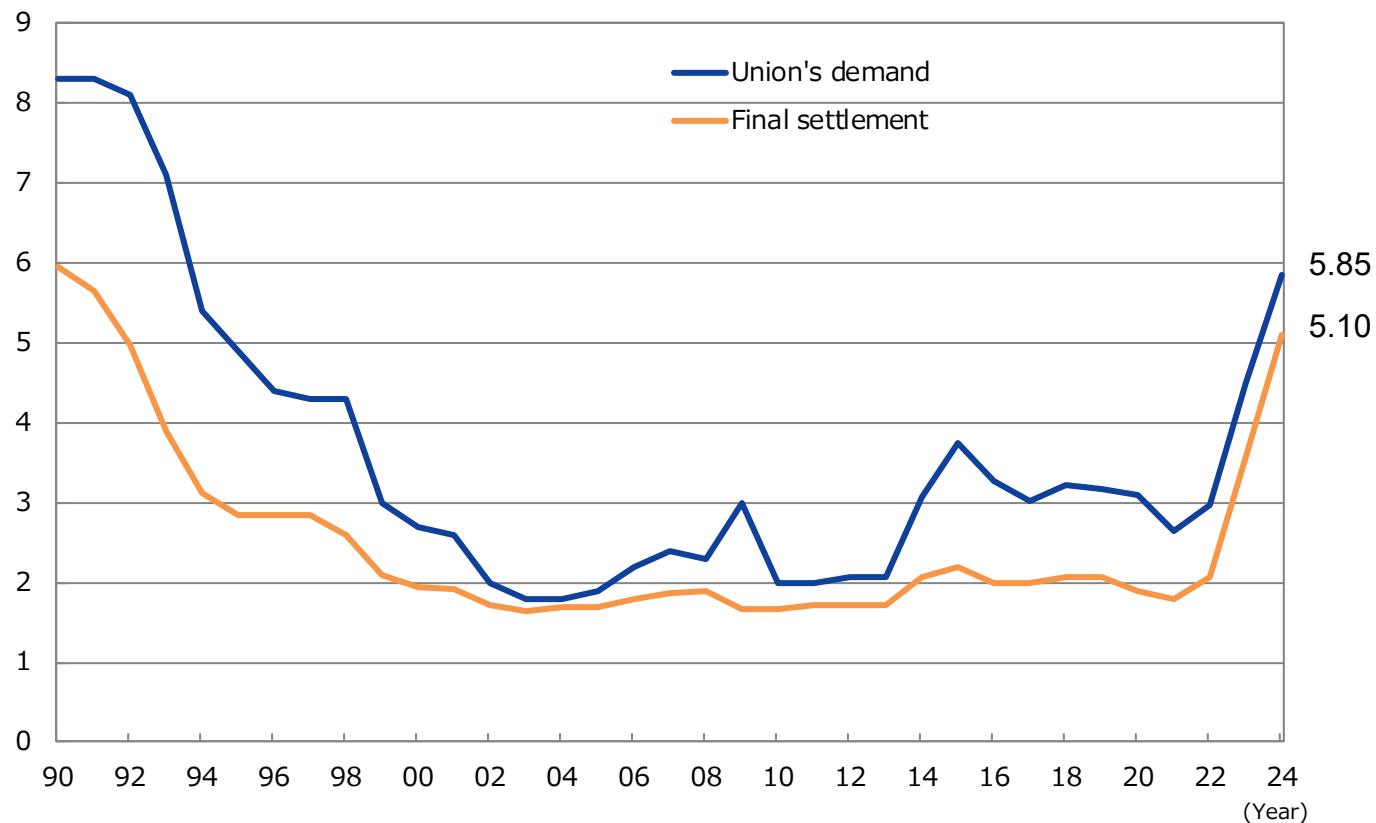
Real wage growth sank into negative again



Note: Data is from January 2021 to August 2024.
Source: Japanese Trade Union Confederation, SMDAM

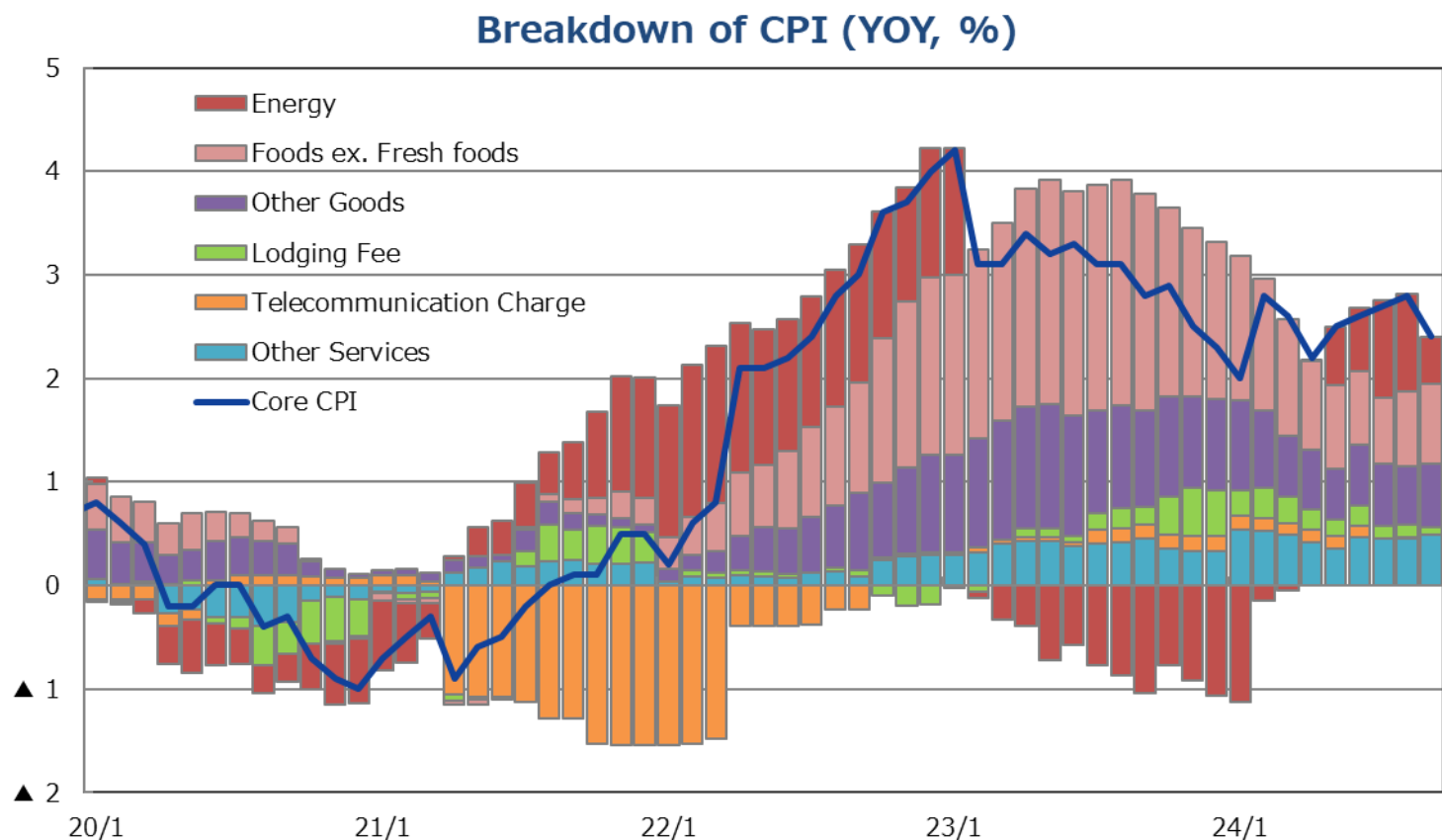
Highest wage increase in 33 years

Wage increase (YOY, %)



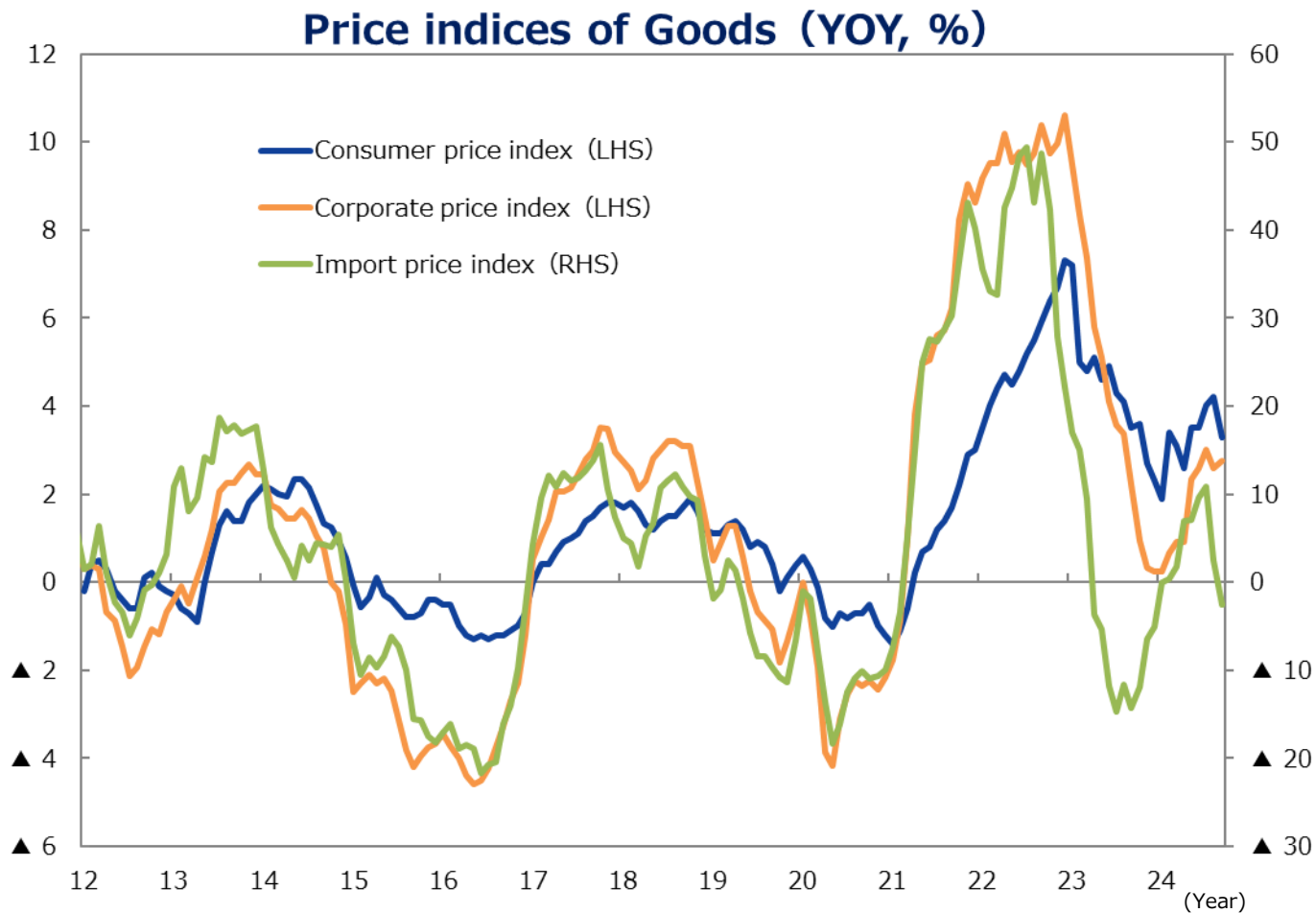
Note: Data is from FY 1990 to FY 2024.
Source: Japanese Trade Union Confederation, SMDAM

Subsidies for utility bills cause major swing of CPI



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

Importers enjoy widening profit margin

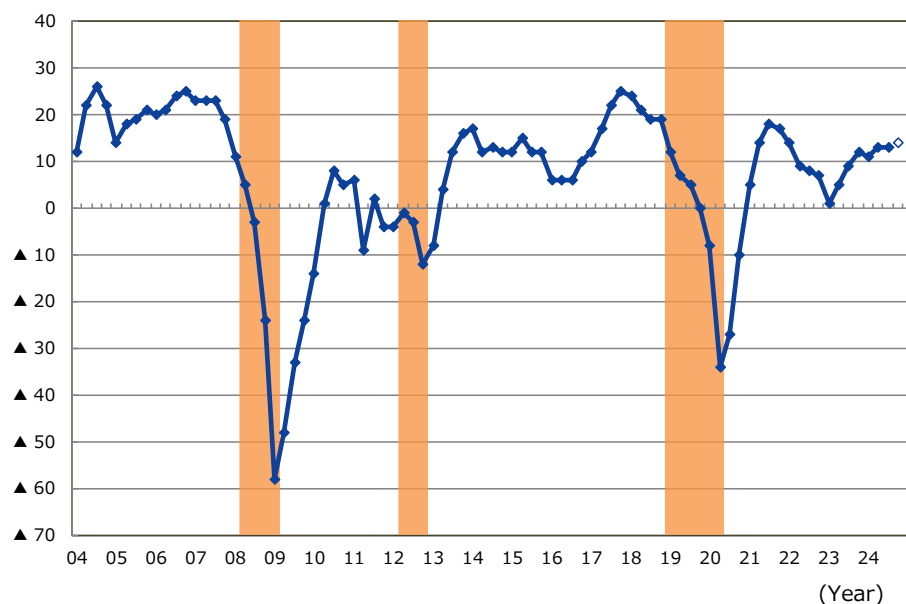


Note: Data is from January 2012 to September 2024.
Source: MIAC, Bloomberg, SMDAM

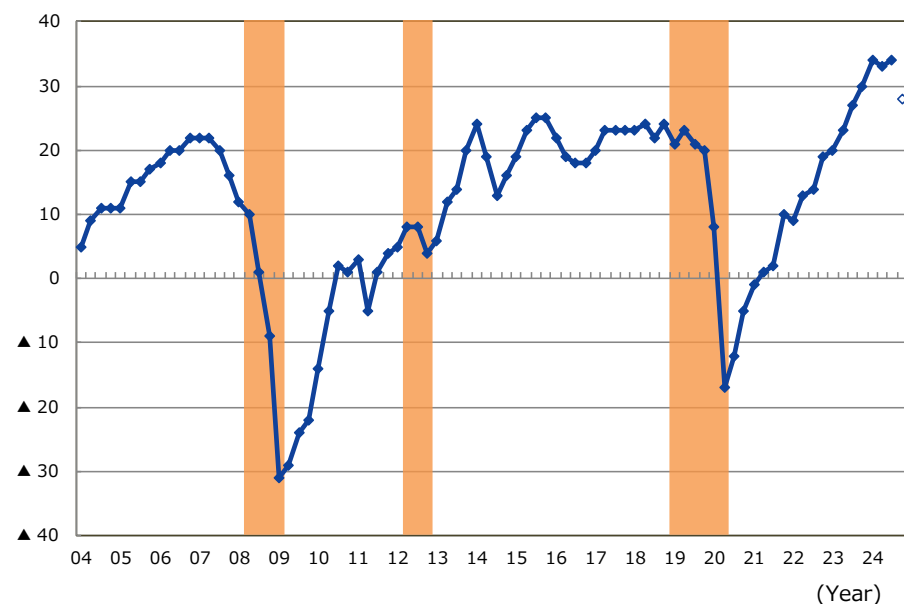


Improvement in business sentiment appears to have stalled

BOJ business condition DI Large manufacturers (%)

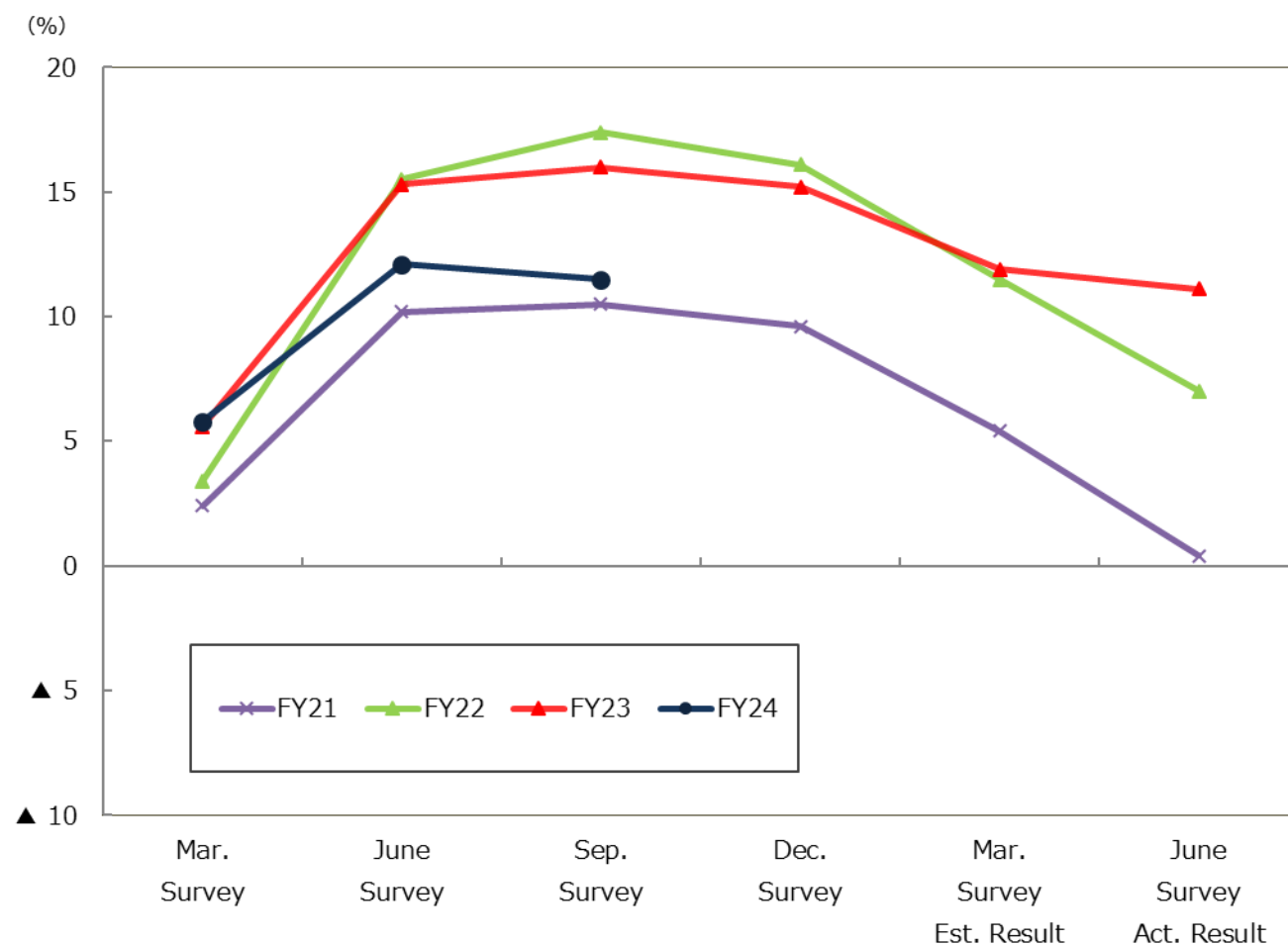


BOJ business condition DI Large non-manufacturers (%)



Note: Data is from Q1 2004 to Q3 2024. The orange shadow represents periods of economic recession.
Source: The Bank of Japan, SMDAM

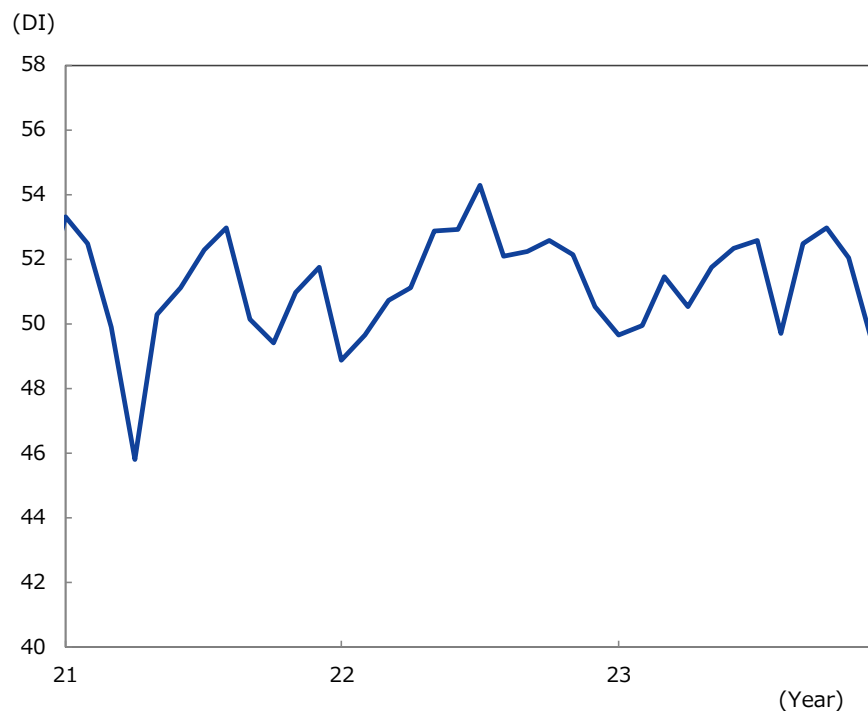
Uncertainty over the global economy gradually weighing on CAPEX



Note: Data is from Q1 FY2021 to Q3 FY2024.
Source: The Bank of Japan, SMDAM

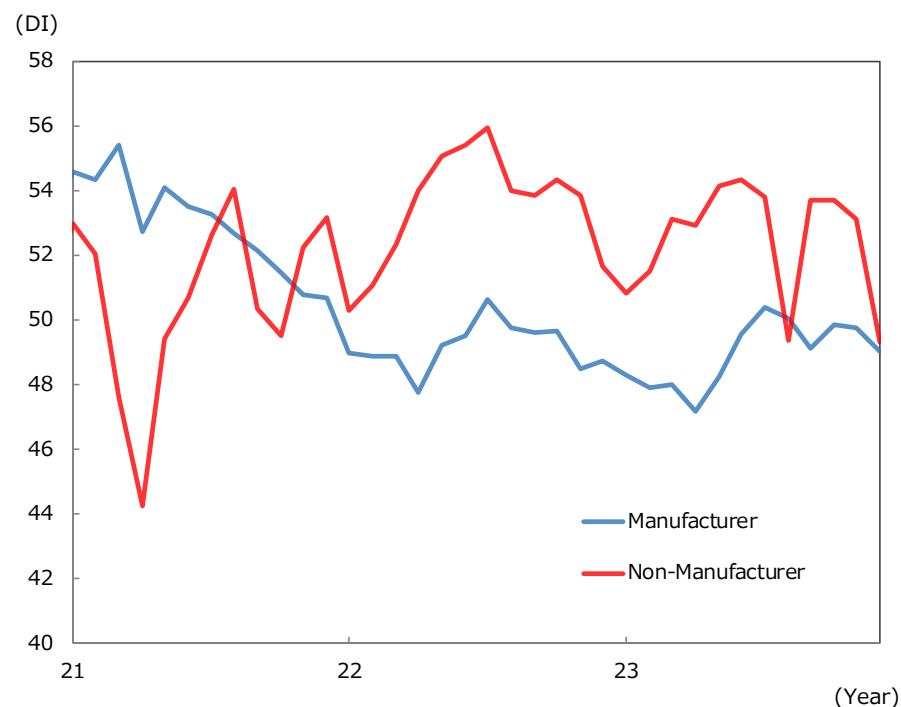
Higher prices and slowing new orders weigh on business sentiment

Composite PMI



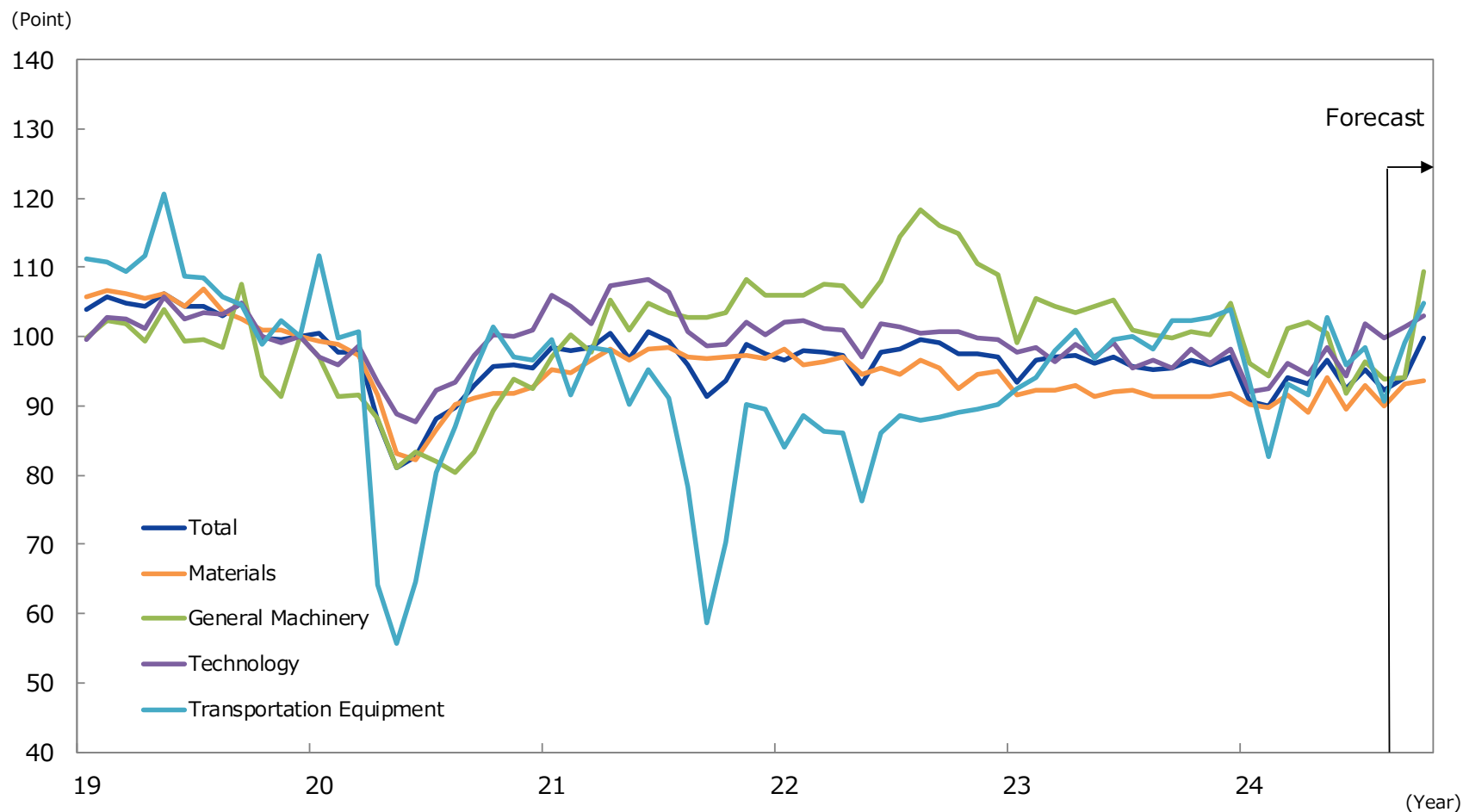
Note: Data is from November 2021 to October 2024.
Source: Bloomberg, SMDAM

PMI, Manufacturer & Non-Manufacturer



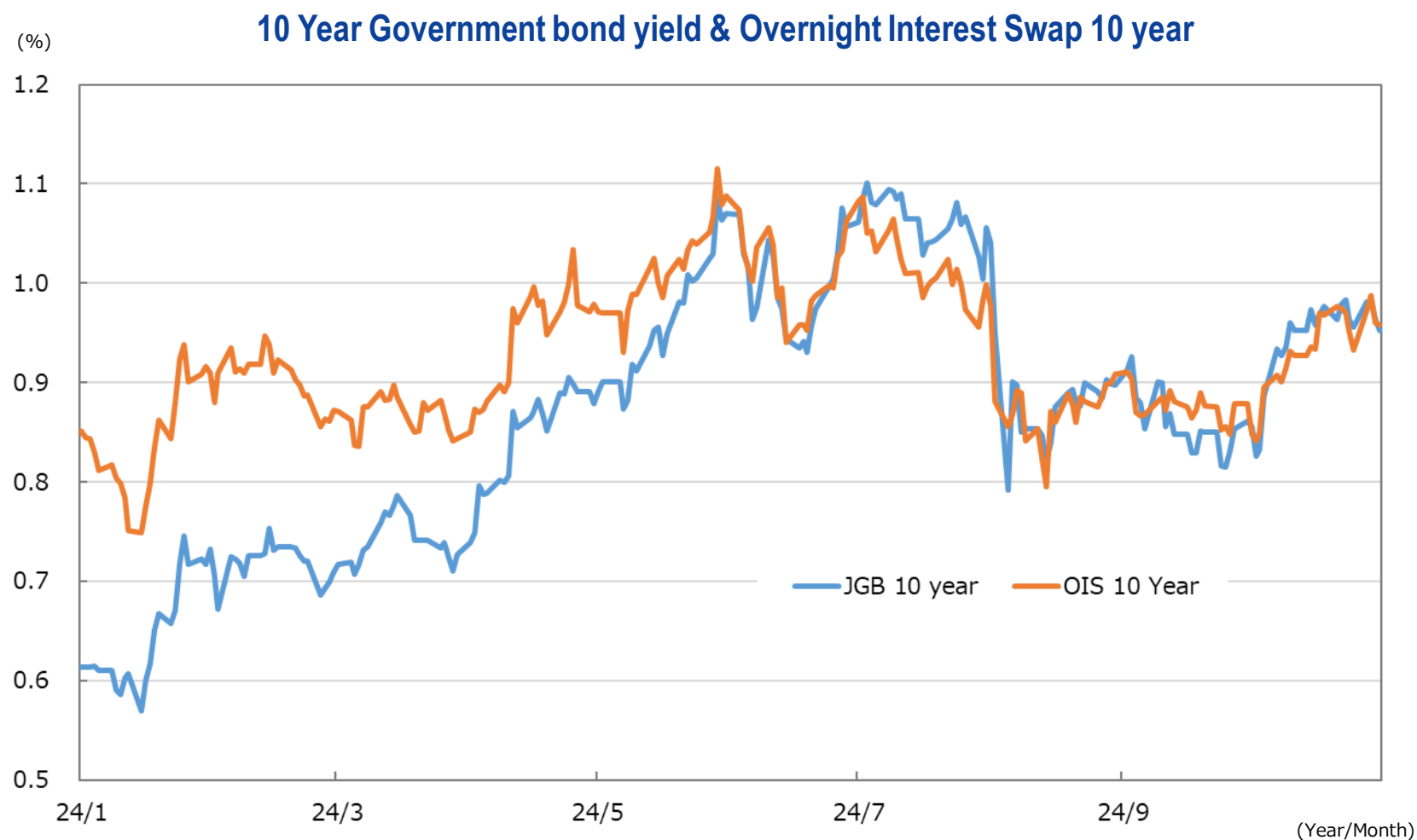
Auto & machinery to boost industrial production going forward

Industrial Production (Dec. 2019=100)



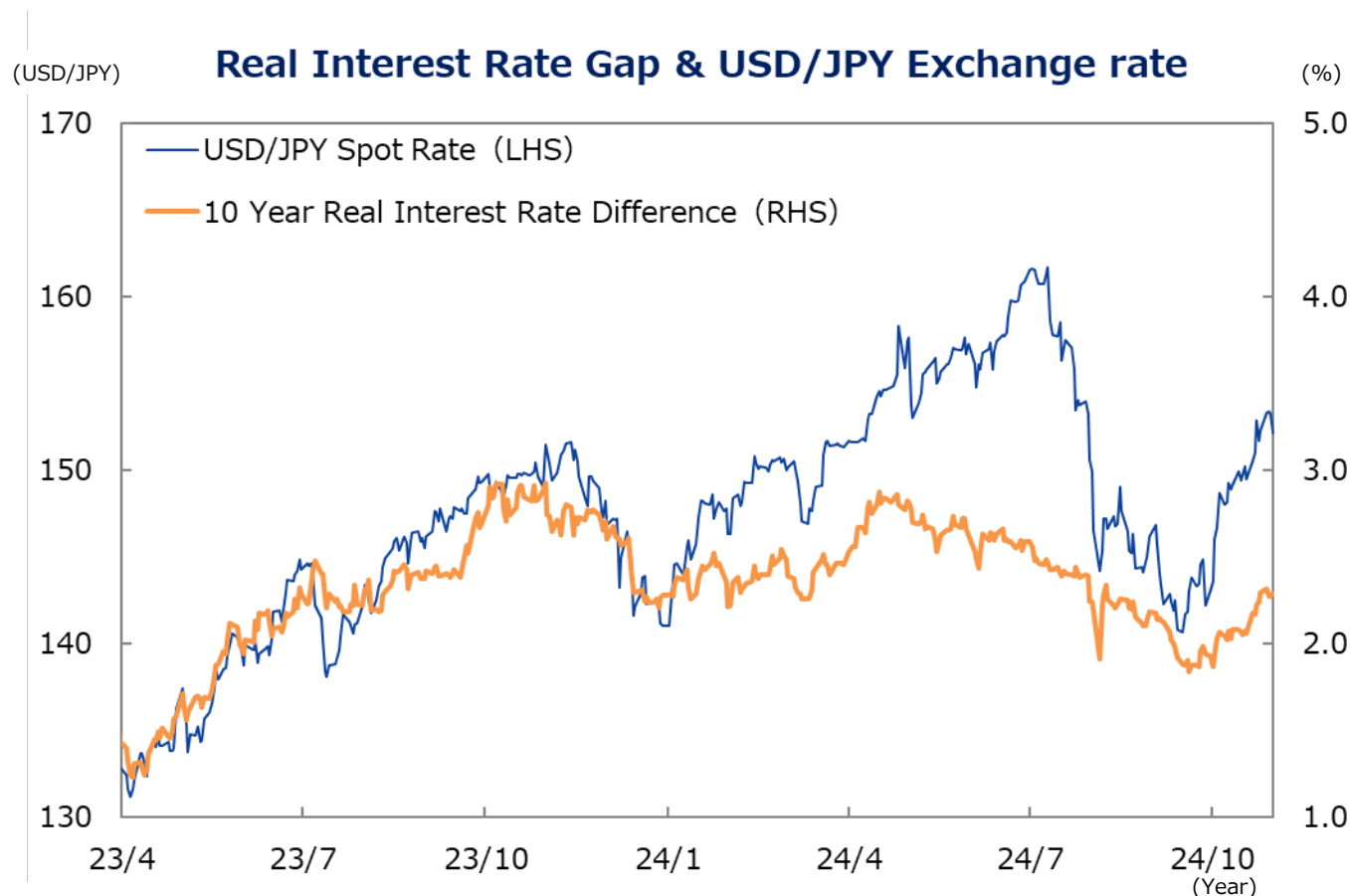
Note: Data is from January 2019 to October 2024. Data after August 2024 is forecasts.
Source: METI, SMDAM

Financial market has not priced in the next rate hike yet



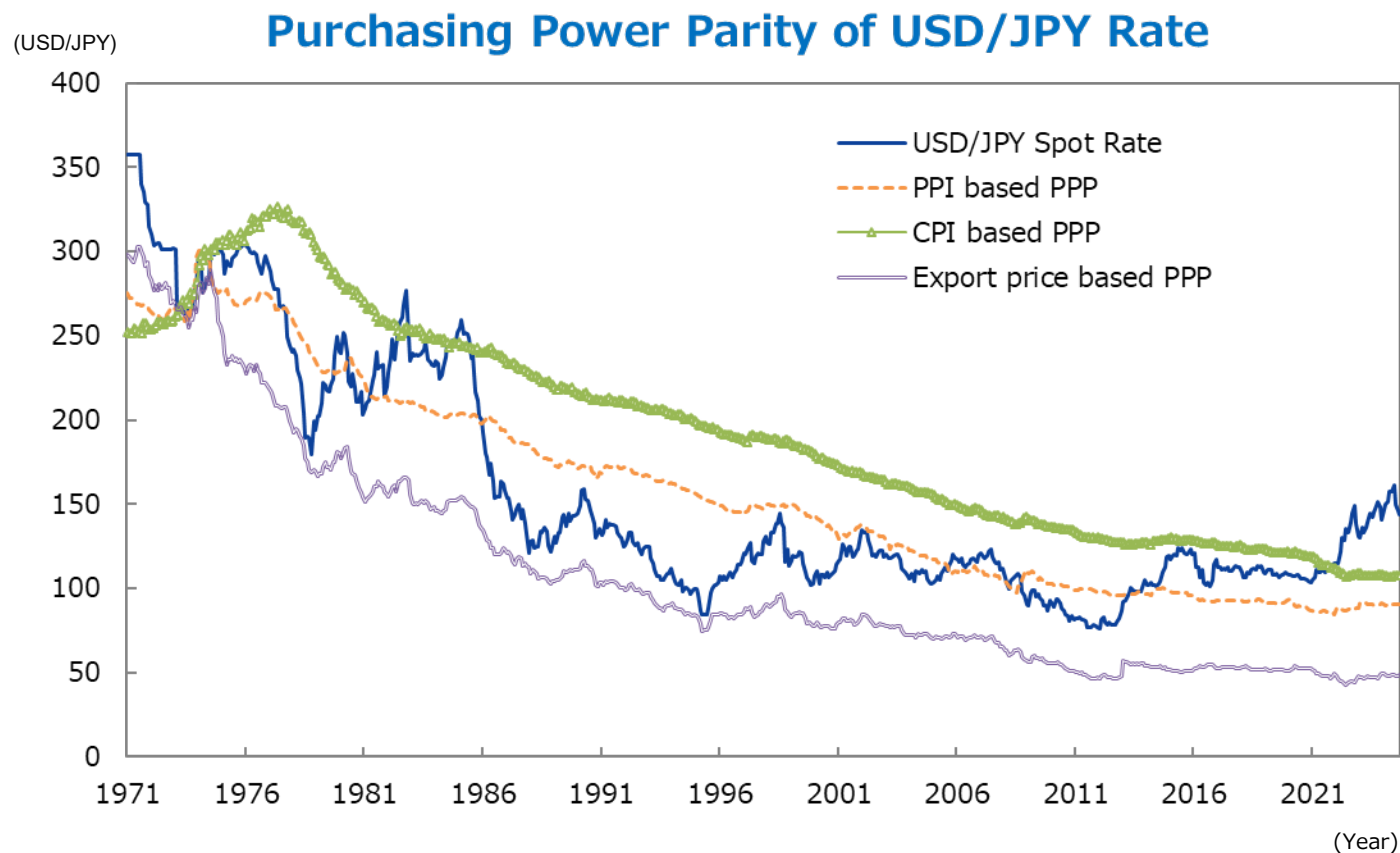
Note: Data is from 1st January 2024 to 31st October 2024.
Source: Bloomberg

Divergence of USD/JPY & interest rate gap due to Trump rally



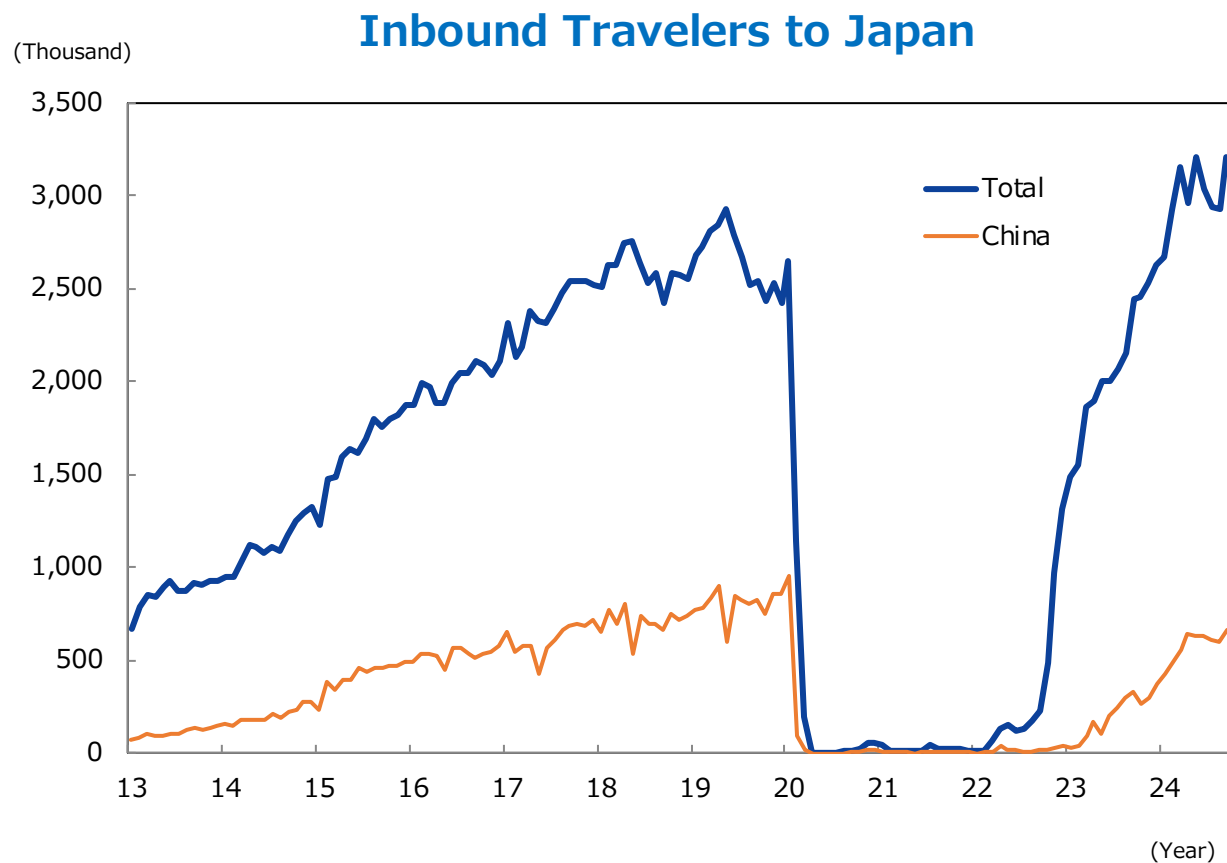
Note: Real interest rates are 10 year government bond yields. Data is from 1st April 2023 to 31st October 2024.
Source: Bloomberg, SMDAM

Unexpected strength of US economy keeps JPY undervalued



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

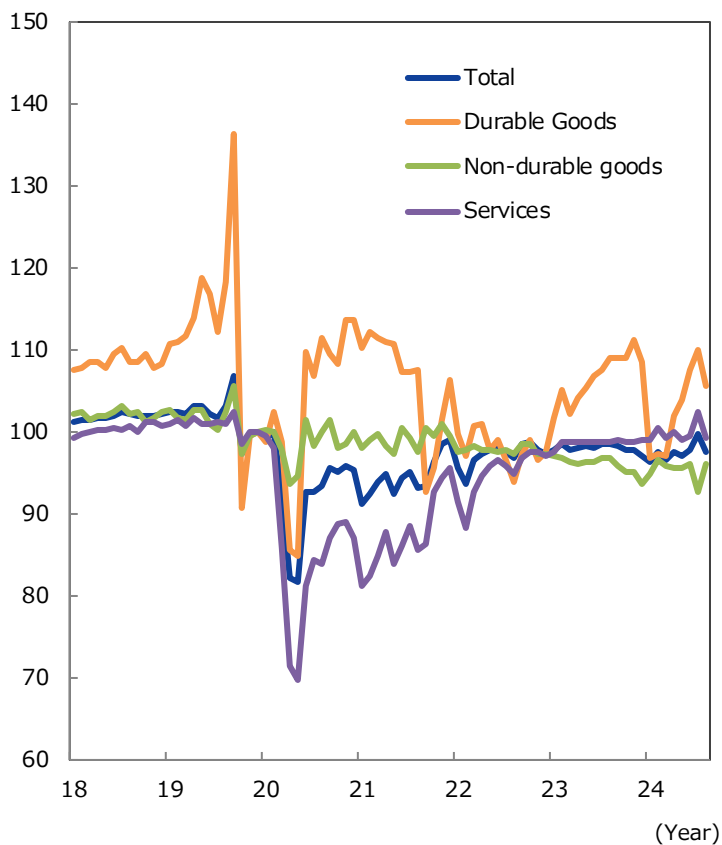
Inbound travel remains strong at record levels



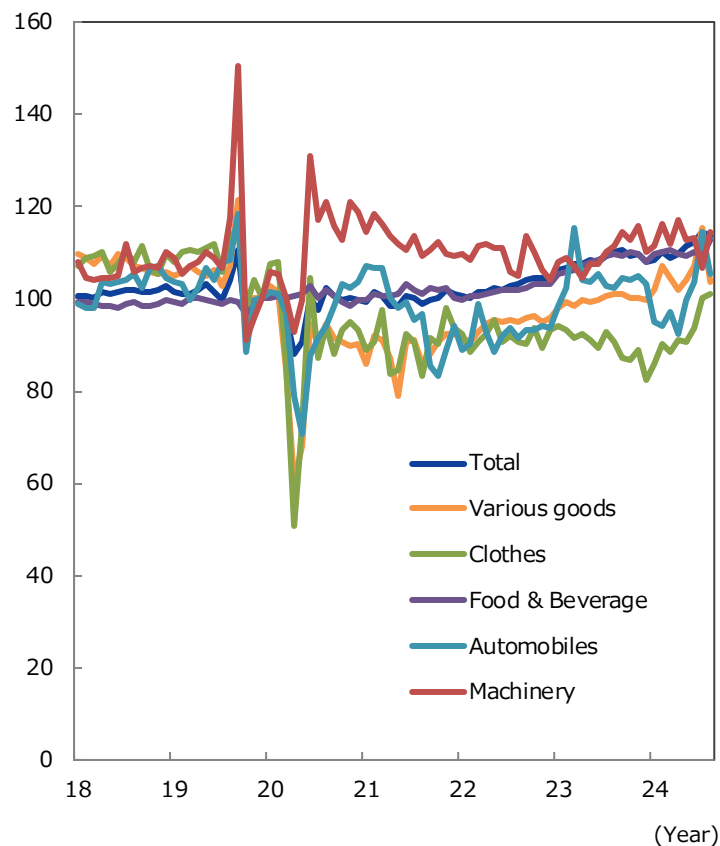
Note: Data is from January 2013 to September 2024. Data is non-seasonally adjusted.
Source: Japan National Tourism Organization, SMDAM

Momentum of auto sales recovery peaked

Consumer Activity Index (Dec. 2019 = 100)



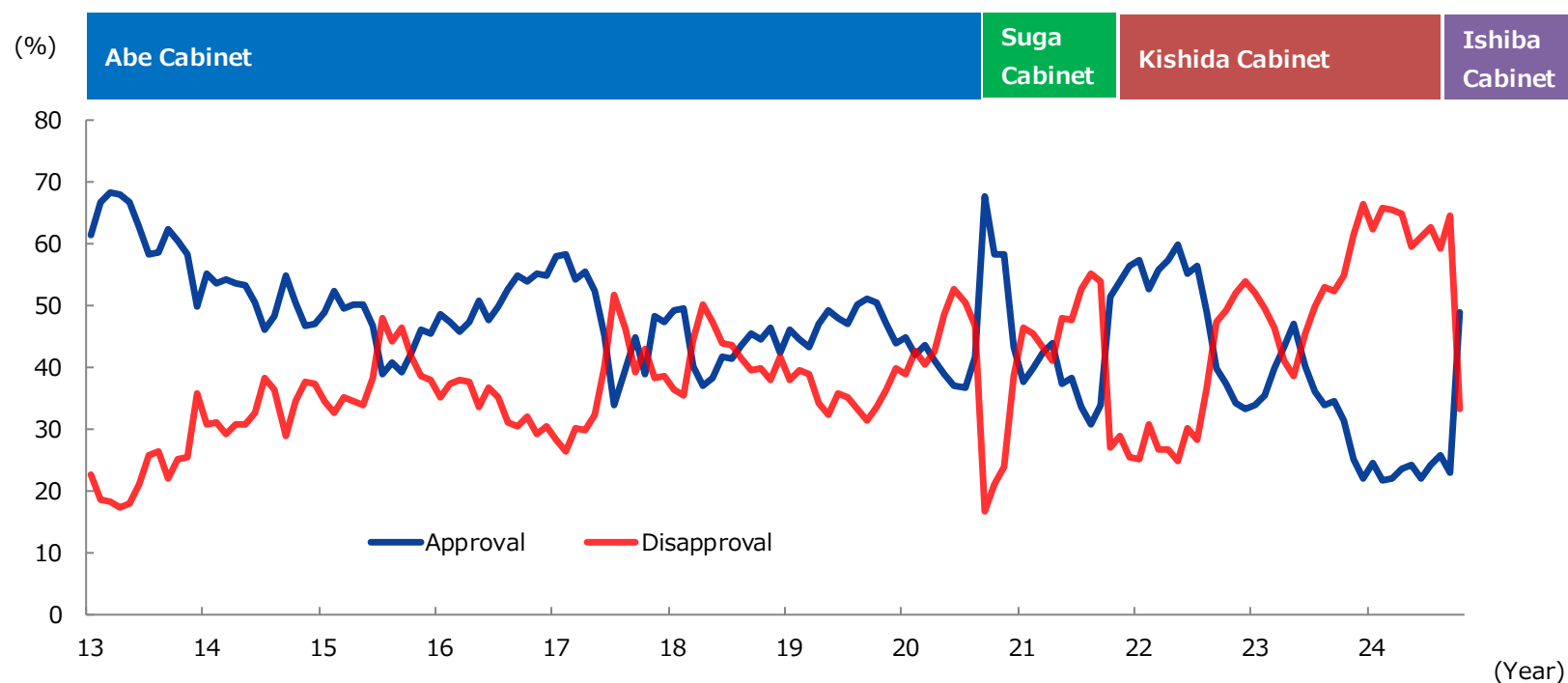
Retail Sales (Dec. 2019 = 100)



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

Political uncertainty weighs on the market even after the election

Cabinet approval rate



Note: Data is from January 2013 to October 2024.

Source: NHK, Asahi, Kyodo, Nikkei, Yomiuri, Sankei, Mainichi, Jiji, and SMDAM

Schedule of major events

Year	Month	Date	Event
2024	November	15	Release of Q3 GDP Cabinet decision on economic measures Cabinet decision on supplementary budget for FY 2024
	December	9 18-19	Revision of Q3 GDP Monetary Policy Meeting Diet resolution of FY 2024 supplementary budget Cabinet approval of the initial budget for FY 2025 and the outline for tax reform
2025	January	23-24	Ordinary Diet Session Monetary Policy Meeting
	February		Release of 2024 Q4 GDP
	March	25 18-19	Expiration of the term of the Bank of Japan's Adachi Policy Board member Revision of 2024 Q4 GDP Release of the results of spring negotiations of Trade Union Confederation Monetary Policy Meeting Enactment of the FY 2025 budget and tax-related bills
	April	13 30-5/1	Start of Osaka Expo Monetary Policy Meeting
	May		Release of 2025 Q1 GDP
	June	16-17 30	Revision of 2025 Q1 GDP Monetary Policy Meeting Cabinet's decisions on "Big-boned policy" End of the ordinary Diet session Expiration of the term of the Bank of Japan's Nakamura Policy Board member
	July	28	Election of the House of Councillors Final results of spring negotiations of Trade Union Confederation
	August		Release of 2025 Q2 GDP
	Septemebr	18-19	Revision of 2025 Q2 GDP Monetary Policy Meeting
	October	29-30 30	Monetary Policy Meeting Expiration of the term of the House of Representatives
	November		Release of 2025 Q3 GDP
	December	18-19	Revision of 2025 Q3 GDP 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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