

## PM'S MONTHLY PERSPECTIVES VALUE + ALPHA GROUP

### Market Outlook & Investment Strategy

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Author: Takuya KAMIISHI  
Portfolio Manager

In April, the TOPIX index increased due to better-than-expected economic indicators in the US and China, receding concerns over trade frictions between the US and China, and the yen depreciation against the USD. The view on the world economy improved after the US Manufacturing Report on Business, China's ISM manufacturing index and China's total social financing (TSF) topped their market consensus respectively. News which suggested an easing of US-China trade wars was also welcomed by investors since the US and China are two biggest trading partners for Japan. The yen depreciation against the USD also helped to progress Japanese equities. Share prices moved little in late April ahead of the ten-day consecutive holidays from 27 April.

**Earnings: Recurring profits for the January-to-March quarter increased by +17% YoY. The guidance for the FY19 was conservative.**

The earnings announcement season for the January-to-March quarter got under way. As of 26 April, 95 companies in the Daiwa 200, an index consisting of major TSE 1st section stocks, announced their earnings results. Recurring profits for the January-to-March quarter increased by +17% YoY, according to Daiwa Securities. Companies' guidance for recurring profits in FY2019 is an increase of +2% YoY, which is conservative as usual. Sectors such as machinery and electronic components suffered a sharp drop in stock prices after the companies released conservative guidance due to uncertainties over the timing of their recovery.

#### Positives

**Kyudenko:** Both the revenue and the operating profit (OP) beat consensus forecasts. Orders for utility work increased on the back of strong construction demands such as electricity and air-conditioning.

**NS Solutions (NSSOL):** Both the revenue and the OP beat consensus forecasts. Orders increased thanks to voracious demands for IT investments. Investors welcomed the company's OP guidance, because it topped the market consensus against the company's tendency to offer conservative guidance.

#### Negatives

**Komatsu:** The company's revenue and OP guidance missed consensus forecasts, while its OP was in line with the consensus forecast. Although the company is known to present conservative guidance, investors were disappointed when the company reiterated its conservative view on demands for mining machineries at the earnings announcement.

**Murata Manufacturing:** Both the revenue and the OP excluding impairment losses beat consensus forecasts, while its OP guidance missed the consensus forecast. The unexpectedly low revenue guidance in communication modules mainly for iPhone spread concerns over a decline in production volumes and a replacement of parts manufacturers.

**Monetary Policy: The Bank of Japan (BoJ) fine-tuned its policy but there were no changes in either policy interest rates or the asset purchasing policy. The bank is likely to maintain its current accommodative monetary policy for a while.**

The BoJ stayed with the status quo in policy interest rates and asset purchasing policy at the policy board meeting held on 25 April, while partially modifying three points below. Overall there were no big surprises, therefore we hold our view that the BoJ is unlikely to make changes to its accommodative monetary policy in the short term.

#### **Clarification of forward guidance**

The BoJ revised its forward guidance and pledged to keep extremely low interest rates until at least the spring of 2020. This is a result of the current uncertainties over overseas economies and the impact of consumption tax hike on the domestic economy and price trends.

The consumption tax hike is scheduled for October this year, and it is said to take at least two quarters to weigh its impact on the economy. So it makes sense that the BoJ set the target ending period at the spring next year.

#### **Expansion of eligible collateral for the Bank's provision of credit including corporate bonds**

The BoJ lowered a threshold rating of corporate bonds from "A" to "BBB" without any change in their holdings including commercial papers (CP). So this is not seen as a quantitative monetary easing step.

#### **Effective use of exchange-traded funds (ETF) by offering short-term loans**

The BoJ added a sentence, saying that it "is considering an introduction of new system to lend its ETF holdings for a certain period to market participants". This wording's intention should be to complement the liquidity which was reduced by its ETF purchases and to promote the sustainability of its policies. The investment strategy to buy influential stocks has been popular up until now, but this trend would change if the plan above comes true.

#### **Investment Strategy**

We expect that the Japanese equity market will rally, given an ongoing accommodative monetary policy by the Bank of Japan, affordable stock prices and the moderate expansion of the global economy. Over the long term, the improvement in governance at Japanese companies, policies which are open to overseas funds and pro-immigration policies will receive recognition from the world. We identify that the sharp yen appreciation is caused by external factors, such as the escalation of trade frictions and the worldwide recession, which are both major risks. Taking these into consideration, we maintain our overweight positions in the late cyclical sectors, such as industrials (commercial & wholesale trade). However, if the economy slows down further than our expectations, we might raise the ratio of defensive stocks in preparation for a recession.

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The author's biography has been provided below:

## Takuya KAMIISHI, CMA – Portfolio Manager

Mr KAMIISHI joined Daiwa SB Investments in 2009 and covered US & European equities as a strategist from 2010 to 2013. He moved to Hong Kong in 2013 as an analyst for the auto & industrials sector in Asia Pacific ex-Japan equity. In 2015, he returned to Japan and covered the IT & services sector as a Japan equity analyst. In 2016, he became a portfolio manager in the Value + Alpha group.

Mr KAMIISHI obtained a BA degree in Economics from Keio University (2009) in Japan.

Note: Daiwa SB Investments Ltd. (DSBI) merged with Sumitomo Mitsui Asset Management Company, Limited (SMAM) on 1 April 2019.

## Contact Details

### Arnaud GÉRARD

Head of Business Development and Client Relations

Phone: +44 (0) 20 7597 7035

Email: [arnaud.gerard@daiwasbi.co.uk](mailto:arnaud.gerard@daiwasbi.co.uk)

Daiwa SB Investments (UK) Ltd.  
5 King William Street  
London EC4N 7DA, United Kingdom

[www.daiwasbi.co.uk](http://www.daiwasbi.co.uk)

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