

Value + Alpha Group

PM's Monthly Perspectives

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In September, the MSCI Japan (Net Total Return Local Index) increased due to three factors below. To begin with, investors pinned hopes on the new Prime Minister Yoshihide Suga (PM). The new PM is likely to maintain business-friendly policies given his position as Chief Cabinet Secretary during the second Abe administration (7 years and 8 months). Secondly, the number of new coronavirus cases at home was in a downward trend until late September. Thirdly, upturns in domestic economic indicators as well as the ISM Manufacturing PMI in the US shored up stock prices, though global equities declined due to concerns over additional stimulus measures in the US, with US growth stocks hit with profit-taking.

Policy: Given business-friendly policies held out by new PM Suga, we can be optimistic about domestic stocks

When ex-Prime Minister Shinzo Abe decided to resign in late August, three candidates, namely Yoshihide Suga, Fumio Kishida and Shigeru Ishiba, ran for elections to lead the ruling Liberal Democratic Party (LDP). But Suga won a landslide victory with 377 votes (the total of votes from Diet members and heads of regional party chapters) versus 89 for Kishida and 68 for Ishiba. Given the fact that Suga held out continued support for Abenomics in his election campaign while the other two insisted on its adjustments, Suga will basically follow the predecessor's policies. Below are his biography and policy ideals.

Biography:

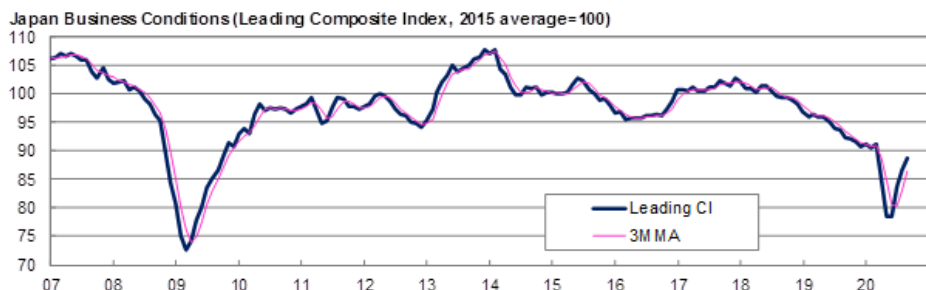
Suga is a self-made legislator as opposed to ex-PM Abe whose grandfather, Nobusuke Kishi, also served as PM in the 1950s. Born the eldest son of a strawberry farm family in rural Akita Prefecture, Suga moved to Tokyo immediately after high school graduation. He worked for a cardboard factory to save for entrance fee for university and enrolled in Hosei University. After graduating from university and working for a private company, Suga served as secretary to a LDP diet member for more than 10 years. He was elected to the Yokohama Municipal Assembly in 1987 and served there for two terms (8 years), making every effort to expand nursery schools. Suga was elected to the House of Representatives in the 1996 election. He belongs to no faction since he withdrew from Kouchikai in 2009. Following Abe's victory in the 2012 general election, Suga was appointed to Chief Cabinet Secretary in the second Abe administration in December 2012. Since then, he has had a key role in its initiatives to attract foreign tourists and workers as well as ones to strengthen the crisis response system in case of missile firings by North Korea.

Policy Ideals:

Suga is planning to follow Abe's economic policies in principle, as he highly appreciates the sharp JPY depreciation and stock price surges during the latest administration. He is also expected to continue accommodative monetary policies, given his support for conventional ones. With regard to fiscal policies, he is against the consumption tax hike in the immediate future despite his commitment to revitalisation of tourism. The biggest difference in this area between Abe and Suga is that the latter puts much emphasis on regulatory reforms. Since he himself experienced a lot of difficulties on the way up to the PM, he is ready to stick the knife into vested interests. He promised a departure from the vertically segmented administrative system, an integration of regional banks, a promotion of competition among telecom carriers and so on in the latest election campaign. Given Suga's comment that he would maintain Abe's direction on foreign policy "centred on the US-Japan alliance," he is expected to pursue the same diplomatic course as Abe by setting the US above China and building relations with neighbouring states upon a strong US-Japan relationship.

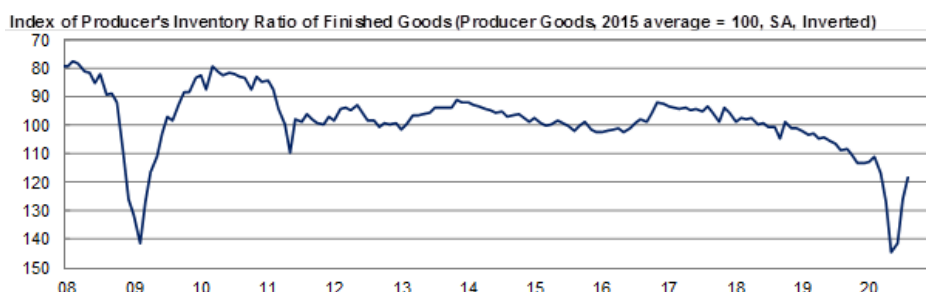
Economy: Japan’s leading indicators show continuing improvements

We are being more optimistic about the domestic economy than last month, given comments from our in-house industry analysts that a variety of statistical data including housing starts, auto production and machinery orders are on a rising trend. Economic indicators also prove it right. Japan’s flash leading index, the composite index of eleven leading indicators (CI) for August rose to 88.8 from 86.7 for the previous month. This means the domestic economy is on the road to recovery after hitting bottom in April/May.



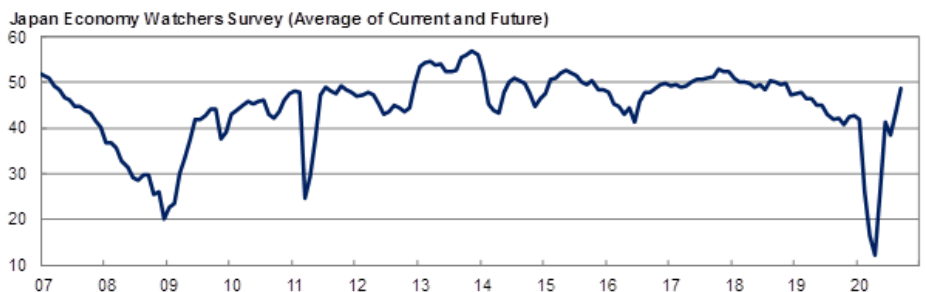
Source: Bloomberg, data correct as of 7 October 2020.

Nine leading indicators are incorporated in the flash CI and 7 of the 9 improved in August. In particular, the index of inventory rates of producer goods and Money Stock (M2) contributed a lot to the upturn. This means a decrease in inventories and monetary easing policies led to a bullish view of the economic outlook. If these inventories continue declining, industry production should also turn up down the road.



Source: Bloomberg, data correct as of 7 October 2020.

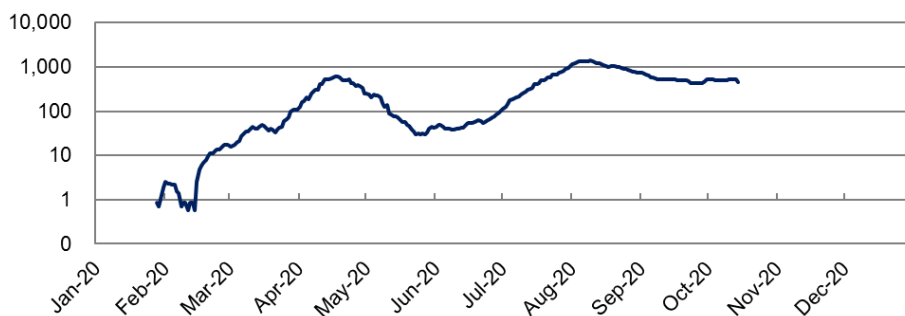
Another important leading indicator, the Economy Watchers Survey (average of current and future) also rose from 43.2 in August to 48.8 in September, which exceeded the consensus forecast of 44.5. According to its comments, the ‘Go To’ Travel campaign (subsidies for domestic tourism) and a change in lifestyle seem to have contributed to the economic recovery.



Source: Bloomberg, data correct as of 8 October 2020.

The ‘Go To’ Travel campaign, which subsidised 35% of tour costs but excluded Tokyo until September, expanded its discount rate to 50% and started to cover Tokyo as well in October. Users of this campaign are increasing because accommodation fees become virtually free if they apply for travel products with meals.

According to Bloomberg, new cases in Japan of coronavirus remain mostly flat these days despite increases in some regions.



Source: Bloomberg, data correct as of 8 October 2020.

Investment Strategy

We expect that the Japanese equity market will advance with the economic recovery and ongoing accommodative monetary policies. Over the long term, more open policies to overseas funds including the improvement in corporate governance as well as policies to boost the immigration intake are also likely to support the market. We identify external factors, such as the outbreak of financial crises and another global recession, as major risks because they might bring about a sharp yen appreciation. Taking these into consideration, we will overweight consumer discretionary sector and stocks with low price/book (P/B) ratios.

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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:

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