

# Fundamental Active Group PM's Monthly Insights

## Authors



**Masashi KAMOHARA, CMA**  
Group Leader &  
Senior Portfolio Manager



**Hideyuki TANIUCHI, CMA/CFA**  
Senior Portfolio Manager

## Market Outlook

We maintain our view that Japanese stock markets will rise gently toward the end of the year. Domestic stock prices fell slightly in October on concerns about rising costs due to soaring energy prices, an event risk around the general election at the end of October and a global economic slowdown, particularly in China, but likely to outperform toward the end of the year given expected corporate earnings growths toward 2022, economic packages expected to be announced following the Lower House election and the valuation gap between domestic and overseas stocks.

The earnings season for the July-September period got into full swing in the final week of October. Ordinary income increased +33% in line with the market estimates. While some companies downgraded their earnings due to delays in production triggered by chip shortages, increases in raw material costs amid aluminium / steel prices and supply-chain bottlenecks, these negative factors are not new with a limited impact on stock prices. Not only the Chinese economy but other emerging economies are picking up. Given utilisation rates of chip / auto parts factories in Malaysia and Vietnam turned up, they should regain lost ground from now on, led by auto makers. In addition, the USD to JPY rate is about JPY114 now, which indicates the Yen is weaker than companies' assumptions. Based on these findings, we believe domestic companies will achieve further earnings growths in the FY2022.

Japan's ruling Liberal Democratic Party (LDP) secured an absolute stable majority in the Lower House election held on 31 October by winning 261 seats. The party achieved a landslide victory amid some concerns among overseas investors that it would lose a majority. Market participants are now pinning hopes on additional economic packages, and the new administration should put into practice a large-scale stimulus package worth several tens of trillions of JPY as pledged without any delay. Prime Minister Kishida is expected to unveil positive fiscal policies in the near term while bearing a medium- to long-term fiscal reconstruction in mind. This spending should prop up the domestic economic recovery that has been stalled by the COVID Delta variant.

The Fed announced it would start tapering its quantitative easing program from November. Meanwhile, it is supposed to maintain accommodative monetary policies for a while given a slow recovery in employment though some people fear interest rate rises at an early stage amid growing inflationary concerns.

While the above-mentioned concerns have gradually eased off after weighing down stock markets in October, valuations of Japanese stocks remain low because earnings recoveries have not been fully priced in the markets. Given an increasing number of companies have announced dividend increases and hikes in pay-out ratio in addition to earnings recoveries, stock prices should bounce back again soon.

## Investment Strategy

Overweight sectors (largest shown first):	Underweight sectors (largest shown first):
Materials	Industrials
Information Technology	Consumer Staples
Financials	Real Estate

Sectors shown are GICS 11 sectors.

We will accelerate the pace of investment in stocks with competitive edges that can pass increased material / logistic costs to their clients and boost profitability amid surging demand for their products. We remain overweight in sectors such as materials and information technology. We will invest in stocks that are expected to enjoy sales expansion toward the FY2022, including server manufacturers and automotive semiconductors, as well as software stocks that will benefit from increased investment in digitalisation by governments and businesses. We will also buy on dip those stocks that are struggling with weak earnings now but likely to benefit from the domestic economic recovery later. In contrast, we take underweight positions in industrials and consumer staples as we think their earnings are relatively weak while their valuations are high.

## Masashi KAMOHARA, CMA

### Senior Portfolio Manager and Group Leader, Fundamental Active Group, Equity Management Department

Mr Kamohara is the Lead Portfolio Manager of the Fundamental Active product. He started his career with Daiwa Securities in 1987 and transferred to Daiwa Institute of Research the following year to become a Japanese equity analyst. He was seconded to their Frankfurt office (between November 1992 and February 1995) and Hong Kong office (between February 1995 and March 1997) as an analyst for European and Asia equities respectively. He transferred to Daiwa International Capital Management, the former entity of Daiwa SB Investments, in 1998 to become a fund manager of international equities.

He became a Japanese equity portfolio manager in October 2000 and has managed the Fundamental Active product since its inception in October 2003.

Mr Kamohara graduated from Kyoto University with a BA degree in Educational Administration (1987).

## Hideyuki TANIUCHI, CFA/CMA

### Senior Portfolio Manager

Mr Taniuchi supports Mr Kamohara in managing the Fundamental Active product.

He started his career with Yamaichi Securities in 1996. He moved to Nikko Asset Management the following year as a trader of equities, convertible bonds and FX. He became a senior portfolio manager of Japanese equity specialising in Growth stocks. He joined Daiwa SB Investments in June 2008 to support Mr Kamohara in managing the Fundamental Active product.

Mr Taniuchi graduated from Tokyo University of Science with BS/Engineering in Industrial Administration (1996).

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## Contact Details

Business Development and Client Relations

Junya OKADA +44 (0)20 7507 6437

Jennifer SANDS +44 (0)20 7507 6424

Marius ERIKSEN +44 (0)20 7507 6438

Email: [uksales@smd-am.co.jp](mailto:uksales@smd-am.co.jp)

Sumitomo Mitsui DS Asset Management (UK) Limited  
5 King William Street, London, EC4N 7DA  
United Kingdom  
[www.smd-am.co.uk](http://www.smd-am.co.uk)

