

Fundamental Active Group PM's Monthly Insights

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Market Outlook

Japanese stock markets are expected to gain ground in June. Until May, the Japanese equity market has been firm relative to other developed economies, but still remained in a range. Three factors that have kept a lid on stock prices, namely 1) the protracted Russia/Ukraine issue followed by rising resource prices, 2) supply chain disruptions due to the Shanghai lockdown and 3) concerns over the acceleration of monetary tightening in the US. These factors still exist but should gradually disappear from June onwards. The Chinese economy, which had put a strong downward pressure on the global economy, is turning up. Meanwhile, the US year-on-year inflation rates is likely to peak out, and the Fed is unlikely to continue sharp rate hikes beyond September given a decrease in housing sales at the moment. Japanese equities are widely undervalued given they are trading at only 12 times their earnings per share despite the weaker yen. We assume foreign investors will pour money into domestic stock markets from now on.

The Japanese economy is heading in a positive direction. Japan's industrial production and exports have been weak but should rebound when the Shanghai lockdown is lifted. Japan will raise its limit on foreign arrivals from 10 June, marking the latest step in a gradual reopening of its borders following the easing of Covid-19 measures. The government is now likely to refrain from including the target deadline to achieve a primary balance surplus, which was originally set in FY2025, in the Basic Policy on Economic and Fiscal Management and Reform 2022. The government seemed to show a willingness to exit from structural deflation/ recession by making clear that "it will implement flexible macroeconomic management without hesitation in order to combine an autonomous growth led by private demand and a breakaway from deflation by promoting bold monetary policies, flexible fiscal policies and growth strategies that stimulate private investment at the same time."

While it was not surprising that domestic companies announced conservative earnings guidance for the fiscal 2022 with cost increases due to rising resource prices in mind, we expect them to make record-high profits this fiscal year backed by the normalisation of the economy, the weak JPY and price increases. Total shareholders' returns are likely to expand further if their corporate performances remain strong. Stock prices of those that announced better-than-expected dividend increases or share buyback programs at the earnings results briefing sessions have been performing well.

Investment Strategy

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

Sectors shown are GICS 11 sectors.

Investment Strategy ^{cont.}

We will maintain a bullish stance on external demand-led companies as well as manufacturers that can benefit from the weak yen. We take overweight positions in information technology and materials. We maintain overweight positions in server/automotive chip makers that are expected to enjoy sales growths in 2022, software developers that will benefit from increased investments in digitalisation by businesses and governments, stocks that afford to return their earnings to shareholders and those that will enjoy benefits of higher resource/energy prices. We will invest in those that are expected to beat their guidance by raising their product prices along with rising inflation, while accumulating those that can benefit from the normalisation of domestic economic activity and the supply-chain recovery in China. On the other hand, we will take underweight positions in industrials and consumer staples as their earnings are relatively weak and their stocks are overvalued, while reducing the weights of financial stocks that have rallied so far following announcements on share buybacks.

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Mr Taniuchi manages the Fundamental Active product with Mr Kamohara.

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 manage the Fundamental Active product and became the Group Leader in 2021.

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

Masashi KAMOHARA, CMA

Senior Portfolio Manager

Mr Kamohara is a Portfolio Manager for 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).

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