

Fundamental Active Group PM's Monthly Insights

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Market Outlook

We expect Japanese stock markets to be volatile in June. Recently, Japan's stock markets, mainly large caps, have shown strong movements led by a significant inflow from foreign investors. The following are regarded as major factors for the strong stock prices: (1) an easy financial environment is maintained and real interest rates are negative in Japan; (2) the stock prices are underpinned by a recovery in domestic demand with reopening; (3) there is much room for the markets to receive the inflow because investors generally had a light position in them. If this month's report of the Monthly Labor Survey indicates a surge in domestic wage growth, it would encourage a view that the Japanese economy has been recovering. Then, the relative superiority of Japan stocks would be sustainable.

The earnings guidance for FY 2023 provided relief, although there remained significant uncertainty regarding corporate earnings outlooks due to unclear overseas macroeconomic environment. The corporate earnings would moderately shift to a growing trend in light of a recent weaker JPY despite concerns over a delayed recovery in China's manufacturing industry. Many companies have announced measures for the enhancement of their shareholder returns to improve their return on equity (ROE) and price-to-book (P/B) ratio. Since April 2023, buyback announcements by Japanese companies have been proceeding at a similar pace to FY 2022 when buybacks reached an all-time high, although buyback announcements from mega banks seemed to be postponed. The significant capacity that business corporations have for purchasing Japanese stocks is favourable for supply and demand dynamics.

The valuation of Japanese stocks that had been strongly undervalued recovered to a price earnings ratio of around 14 times, the average in the past 10 years, following recent surges in their stock prices. The rapid hike in the valuation is reasonable as it is possible to explain that the markets have anticipated potential revision index's return to positive territory. The recent inflow from foreign investors into the market can be seen as the initial wave. If progress in Japanese companies' structural reforms is acknowledged, subsequent waves are likely to follow. However, technical indicators, including the up-down ratio, are overheating as a result of a rapid increase in stock prices since May. The stock markets may focus on the dissolution of the House of Representatives and a general election after June 21, when the current ordinary Diet session will end. Then, the markets are likely to be volatile in the second half of the month because of short-term investors who are betting on the dissolution.

Note:

Above names are for example purposes and SMDAM is not recommending or advising these stocks.

Investment Strategy

Overweight sectors (largest shown first):	Underweight sectors (largest shown first):
Consumer Discretionary	Industrials
Information Technology	Consumer Staples
Communication Services	Health Care

Sectors shown are GICS 11 sectors.

GICS sector wise, we will continue to overweight consumer discretionary, information technology, and communication services. We will invest mainly in stocks which (1) are expected to improve their profitability through their efforts such as price pass-through, (2) will realise a decrease in raw material and procurement costs, or (3) are expected to increase dividends and buy back shares more than anticipation. In addition, we will focus on companies with a low price-to-book (P/B) ratio that are expected to improve their business structure and capital policy. Then, we will increase the weight on large blue chips whose prices have lagged because we anticipate foreign investors to continue purchase Japanese stocks in the medium term. On the other hand, we will continue underweight in industrials and consumer staples sectors from the view point of earnings growth rate and valuation. We will decrease the weight on semiconductor equipment stocks whose prices jumped because of expectations for growing demand for AI semiconductors.

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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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