Marketing Communication
August 2023

Value + Alpha Group

PM's Monthly Perspectives

Author

Takuya KAMIISHI, CMA
Lead Portfolio Manager

The MSCI Japan index rose on easing concerns about US rate hikes, expectations of Chinese stimulus measures, and strong corporate earnings results, although stronger yen, the BOJ's widening of the long-term rate band, and selling of Japanese stocks ETFs to secure cash for dividend payments weighed on the market. In detail, concerns over further rate hikes in the US have eased as both the consumer price index (CPI) and the producer price index (PPI) dropped more than expected. And the fact that Chinese state media reported that the Chinese government had asked banks to extend the deadline of repayment of the loans to real estate developers and was considering additional support for the beleaguered property sector was well received by equity investors. In addition, the Japanese stock market was also supported by positive earnings results from the majority of Japanese companies. However, the BOJ's decision that it will give greater flexibility to its yield curve control (YCC) and raise the caps on the fluctuation of long-term rates from 0.5% to 1.0% caused Japanese stocks to somewhat underperform. Further, stronger Japanese yen against the US dollar and many Japanese stock ETFs selling their holdings to raise the cash for dividend payments, as many Japanese passive equity ETFs have their earnings date in July, also weighed on the Japanese equity market.

Earnings: Japanese companies reported strong earnings results for April-June period

The earnings announcement season for the April-June quarter got under way. As of 31 July, approximately 35% of major listed companies (excluding financials and listed subsidiaries of a listed company) on the Prime Section of the Tokyo Stock Exchange (TSE) announced their earnings results. According to Daiwa Securities, the aggregate sales and operating income increased +8% and +34%, respectively. Looking at actual operating income of the TOPIX 500 companies for the April-June quarter of 2023, 43% of them announced higher operating income than analysts' consensus estimates by +10% or more, and 26% announced income falling short of the consensus by -10% or more.

As fund managers, we simply feel that the earnings season was positive for Japanese stocks as many companies' earnings results were better than previously expected. The reasons for the good results are threefold: 1) the unit sales price rose due to an increase in selling prices and inflation; 2) the costs of raw materials, electricity and transportation were lower than the companies had assumed; and 3) the yen weakened. However, demand from China and for hard disk drives (HDD) and consumer durables was weak and earnings results at companies related to these missed analyst estimates. Major earnings results are as follows:

Positives

Toyota Tsusho Corp.: This automobile-related trading company exceeded consensus estimates for earnings per share (EPS). Toyota Motor's car production volume was about +10% higher than Toyota Tsusho expected, and Toyota Motor's automobile sales were strong due to the acceleration of motorisation in non-resource-rich countries in Africa, and the company was able to maintain a high level of vehicle sales margins. In addition, Toyota Tsusho was able to minimise the impact of the deterioration in market conditions for semiconductors and steel-related goods, which had been a concern, by taking a lean inventory approach. Moreover, its CFO commented that the company was discussing increasing shareholder returns since shareholders' equity had accumulated to a certain extent.

Sumitomo Mitsui DS Asset Management

Positives (cont.)

Lawson, Inc.: This convenience store topped consensus estimates for sales and operating income. In addition to strong sales due to a recovery in the flow of people and inflation, sales of movies and entertainment tickets were also strong due to the recovery in the flow of people. And in addition to sales promotion expenses that the company was able to reduce due to strong sales, electricity bills, which had been rising, were not as expensive as the company had assumed due to lower resource prices, etc.

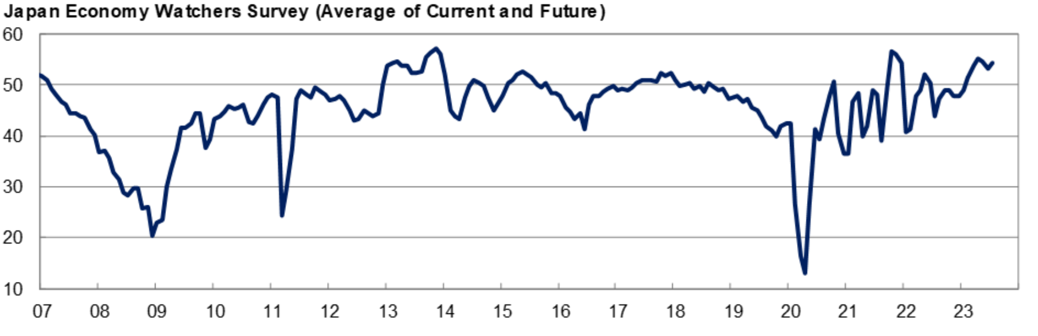
Negatives

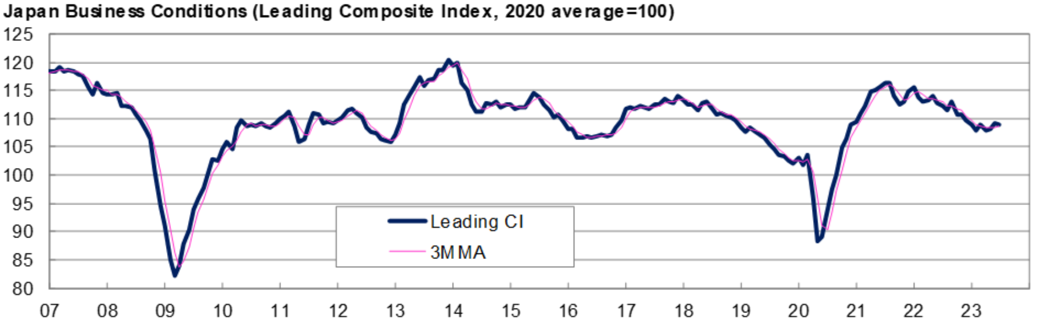
Fanuc Corp.: This robot and factory automation (FA) system manufacturer missed analyst consensus estimates for sales and operating profit, and revised down its FY2023 full-year operating profit guidance. Its robot orders received came to a halt due to user companies' considerable progress in capital investment for electric vehicles (EVs) and lithium-ion batteries (LiBs), and profits fell due to a decline in plant capacity utilisation. In addition, the FA system inventory in China is said to be accumulating to an unprecedented level, and said to have exceeded the actual demand even considering its increase due to supply chain disruptions.

CyberAgent, Inc.: This company, engaged in advertising agency, game, and media businesses, missed analyst consensus estimates for sales and operating profit, and revised down its FY2023 full-year operating profit guidance. Sales of high-margin games that had made big hits slowed more than expected, and the trend of declining profit margins continued in the advertising agency business. In addition, its key performance indicators (KPIs) for the media business such as monthly active users (MAUs) and advertising sales did not grow as expected.

Economy: Japan's composite leading indicator is rising, leading to a positive impact for Japan's Economic Outlook

Japan economy watchers survey (average of current and future) which we prioritise the most among the Japan's leading economic indicators was 54.25 in July, up from 53.20 in June. The July figure is considerably higher than the average of the past, and it would be one of the key reasons to judge that Japan's economic outlook is positive compared with other countries. Considering the reasons why the figure was good based on comments made by survey respondents, we can pick up following 3 points; (1) reopening of festivals, events and travel boost consumption and employment (2) heat wave boosts seasonal items such as beverage/ice cream/swimsuits/yukata (informal cotton kimono)/travel bags/UV skincare products to solid level (3) continued strong sale and production of automobiles. Another leading economic indicator showed improvement in May-June compared with March-April. Japan's economic outlook is relatively positive.





Source: Bloomberg, as of 8 August 2023.

Note: Above names are just for showing examples and SMDAM is not recommending or advising these stocks.

Investment Strategy

We expect that the Japanese equity market will move sideways in the short term due to the tug-of-war between a global economic slowdown and expectations of a change in the management policy of Japanese companies with a P/B ratio below 1x driven by TSE policy. Over the long term, policies that are more open to foreign capital, including improvement in corporate governance, as well as policies to boost the immigration intake, are likely to support the market. We identify external factors, such as the outbreak of financial crisis and global recession, as major risks, and we believe that the probability of such risk materialising is 50% or higher. Taking these into consideration, we will overweight low-P/B companies with large net-cash positions.

Takuya KAMIISHI, CMA
Lead Portfolio Manager, Value + Alpha Group

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.

Disclaimers

Issued by Sumitomo Mitsui DS Asset Management (UK) Limited. Registered in England and Wales.

Registered office 100 Liverpool Street, London, EC2M 2AT; registered number 1660184. Authorised and regulated by the Financial Conduct Authority.

Past performance is not a reliable indicator of future performance and may not be repeated. An investment's value and the income deriving from it may fall, as well as rise, due to market fluctuations. Investors may not get back the amount originally invested.

The data contained in this document is for information purposes only. It is correct to the best of our knowledge at the date of issue and may be subject to change. The client legal agreement will take precedence over this document. This document is not legally binding and no party shall have any right of action against Sumitomo Mitsui DS Asset Management (UK) Limited, in relation to the accuracy or completeness of the information contained in it or any other written or oral information made available in connection with it. Nothing in this document or any related presentation shall be deemed to constitute investment advice, nor shall we be deemed to be an investment advisor unless formally appointed as such, or as discretionary investment manager, by way of written agreement.

The information contained in this presentation is to be used by the professional client that this document is issued to only. This product is not available in the EEA or to EEA domiciled persons.

Risk warning: On 1 January 2021 the UK left the EU transitional arrangements and no longer benefits from passporting rights into EEA countries.

Contact Details

Business Development and Client Relations
Daisuke ISHIHARA: +44 (0)20 7507 6436
Chloé CHOQUIN: +44 (0)20 7507 6424
Email: uksales@smd-am.co.jp

Sumitomo Mitsui DS Asset Management (UK) Limited
100 Liverpool Street, London EC2M 2AT
United Kingdom
www.smd-am.co.uk