

JAPAN EQUITY MONTHLY

May 2018

Japanese equities gained in April

The Japanese equity market rose in April, with the TOPIX (w/dividends) climbing 3.55% on-month and the Nikkei 225 (w/dividends) rising 4.73%. Stocks started the month lower after the Bank of Japan's Tankan business sentiment survey showed weakening business sentiment amongst large manufacturers and as concerns over an escalation of trade friction between the US and China grew. The market subsequently moved upward after the Chinese president announced measures towards market liberalisation, including cuts to automobile import tariffs, thus alleviating trade war concerns. In addition, stocks benefitted from easing anxiety over political tensions in the Middle East given the limited impact of US military action in Syria as well as the improving Japanese earnings outlook as the yen began to weaken against the US dollar.

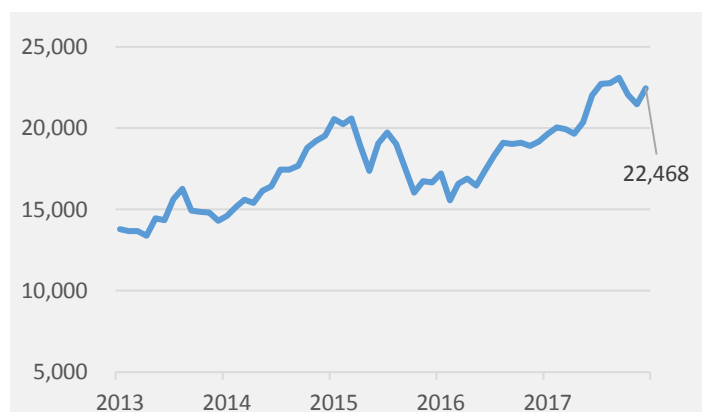
Of the 33 TSE sectors, 31 sectors including Electric Power & Gas, Insurance, and Oil & Coal Products posted gains during the month, while two sectors—Services and Pharmaceuticals—declined.

Exhibit 1: Major Indices (Last Month and Historic Changes)

Index	Mth-end	1-mth	3-mth	6-mth
Nikkei 225	22,467.87	4.7%	-2.7%	2.1%
JGB Yield	0.055	+0.006	-0.030	-0.016
JPY/USD	109.27	2.8%	0.4%	-3.6%
JPY/EUR	132.17	0.9%	-2.4%	0.2%
MSCI World	2,086.51	1.0%	-5.7%	2.4%

Source: Bloomberg, as at 30 April 2018

Exhibit 2: Nikkei 225



Source: Bloomberg, as at 30 April 2018

JPY likely to range-trade in the medium term

The JPY's strength over the past few months has been a cause for concern for investors, as it has spurred worries of a negative earnings impact on Japanese exporters. Manufacturers' confidence, as measured by the Tankan survey, has also worsened slightly. Our expectation is that the JPY will trade in a narrow range in the medium term. In our opinion, the JPY could reach 108 against the USD in September 2018, and 105 in March 2019. As a result, we do not expect the JPY to be a significant source of support to the equity market over the next fiscal year.

That said, we remain positive on the Japanese stock market: we forecast that the Nikkei could reach 23,500 as at March 2019. While we see the USDJPY remaining relatively stable over the fiscal year, we continue to expect Japanese stocks to be supported by volume growth. Healthy demand from the US will likely underpin Japanese exports such as textiles (chemical fiber) and machines.

BOJ could loosen yield curve control by FY19

During its meeting in April, the Bank of Japan (BOJ) kept its policy steady, but removed the timeframe it had set for hitting its 2% inflation target. While this was unexpected, markets took the news relatively well. According to BOJ Governor Kuroda, the decision to remove the deadline was made to minimise investor speculation about central bank policy actions. Our view is that the removal of the inflation timeframe gives the central bank more flexibility in implementing policy. Over the fiscal year, we see the BOJ loosening its yield curve control policy. Our expectation is for the 10-year JGB yield to reach 25 basis points in 2019, from virtually zero today. However, we do not expect changes in the short end of the curve, where we see yields remaining negative.

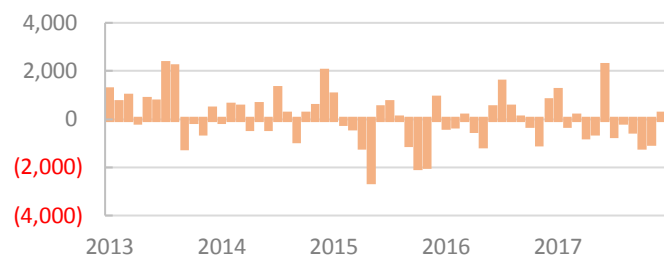
Abe could benefit if North Korea talks go well

Elsewhere, the spectre of trade war and lingering geopolitical concerns are likely to be sources of increased volatility in stock markets this year. With Japan, South Korea and China now appearing to present a united front on North Korea, we will be monitoring the upcoming talks between North Korea and the US. If the North Korea talks go well, Prime Minister Abe has a chance to gain on the reputational front and improve his prospects in September's LDP elections. While scandals have hurt his approval ratings at home, Prime Minister Abe continues to be well-supported by overseas markets, as he brings a high level of policy forecastability.

Exhibit 3: Major Market Indices



Japan Equity Net Purchase from Overseas (JPY bil.)



Source: Bloomberg, as at 30 April 2018

Exhibit 4: Major Index Performance, Indicators, and Valuation

Index	1-mth	3-mth	6-mth	1-yr	5-yr
Nikkei 225	4.7%	-2.7%	2.1%	17.0%	63%
JGB Yield (%pt)	+0.006	-0.030	-0.016	+0.055	-0.802
JPY/USD	2.8%	0.4%	-3.6%	-2.0%	9%
JPY/EUR	0.9%	-2.4%	0.2%	8.8%	1%
MSCI World	1.0%	-5.7%	2.4%	11.1%	42%
TOPIX	3.6%	-3.2%	0.6%	16.0%	56%
TPX-100 (Large)	3.6%	-3.5%	0.1%	14.5%	47%
TPX-400 (Mid)	3.8%	-2.9%	1.2%	16.5%	68%
TPX-Small	2.8%	-3.0%	2.2%	23.2%	84%

Sector (TPX-17)	1-mth	3-mth	6-mth	1-yr	5-yr
Elc Appl&Prec	1.7%	-5.8%	-1.2%	22.9%	83%
IT & Service	2.1%	-0.7%	-0.4%	17.4%	97%
Auto&Trns Eqp	3.6%	-5.3%	-1.0%	12.0%	21%
RawMatl & Chm	2.1%	-2.7%	1.1%	21.3%	105%
Banks	4.7%	-6.5%	-3.2%	4.0%	14%
Machinery	1.8%	-10.8%	-2.8%	17.3%	56%
Transprt&Logi	6.7%	-0.9%	2.3%	13.2%	53%
Const & Matl	4.6%	-3.5%	-2.9%	18.4%	88%
Fincl ex Bank	6.6%	-3.0%	2.5%	11.1%	33%
Foods	3.7%	-2.6%	-1.8%	8.5%	66%
Retail Trade	4.7%	5.1%	11.3%	20.4%	81%
Pharmceutical	-0.4%	-0.7%	2.3%	11.7%	68%
Commr & WhTrd	5.9%	0.0%	9.8%	26.4%	65%
Real Estate	8.2%	-1.2%	6.9%	16.6%	4%
Steel&Nonfer	4.0%	-11.0%	-8.4%	7.7%	20%
Elc Pwr & Gas	9.9%	11.6%	4.9%	8.3%	6%
Engry Resourc	8.4%	-1.7%	20.1%	37.1%	44%

Valuation	Mth-end	3-mth	6-mth	1-yr	5-yr
TOPIX					
Div. Yield (e)	2.1%	1.9%	1.9%	2.1%	1.9%
Price/Earn (e)	14.1	15.8	15.7	14.2	14.5
Price/Book	1.3	1.4	1.4	1.2	1.2
MSCI World					
Div. Yield (e)	2.5%	2.4%	2.4%	2.5%	2.7%
Price/Earn (e)	15.9	17.1	18.0	17.3	14.3
Price/Book	2.2	2.4	2.3	2.2	1.9

Market Indicator	Mth-end	3-mth	6-mth	1-yr	5-yr
Daily Turnover	49	55	56	53	48
Market Cap.	669	665	671	589	399
Net Purchase Overseas	207	-1,933	-3,200	-1,174	3,945

Source: Bloomberg, as at 30 April 2018

(e) stands for consensus estimates by Bloomberg.

Turnover and market cap in JPY tril.

Net Purchase (JPY bil.) from Overseas is cumulative monthly.

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