

How could Japanese stocks return to its bullish trend?

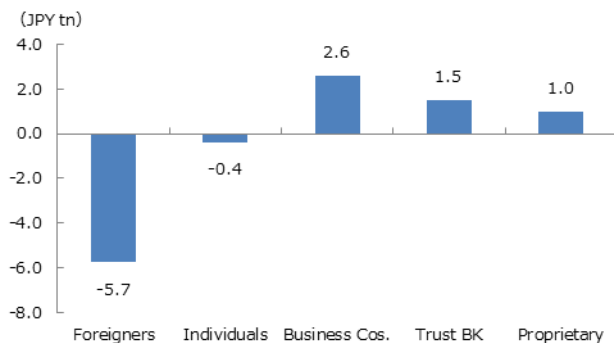
- The Japanese stock market is discounting Brexit delay, and dovish FOMC policy is positive.
- Result of US-China ministerial trade talks was within market expectation and negative factors of Japanese financial results were already reflected in stock price.
- The Japanese stock market is discounting negative events steadily. However, foreign investors' behavior is still the key for strong recovery.

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Important events in-and-out of Japan were over last week. As to Brexit, British Prime Minister Theresa May is supposed to negotiate with EU on Irish border. If they cannot reach agreement by 13 February, there will be a re-vote for the process of Brexit. Market seems to be discounting the possible approval of the extension of Brexit deadline at the end of March and that of transition period to some extent.

Outcome of FOMC was more dovish than expected. Based on the outcome, we expect that US interest rate hike and tapering will be stopped during this year. FOMC's dovish policy is a strong support especially to the stock market as it reduces market's concern over US economic slowdown by interest rate hike.

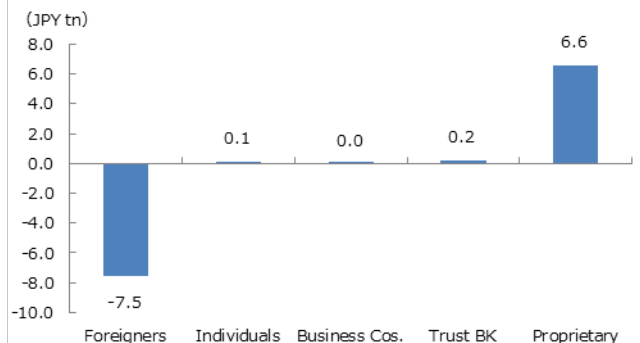
“Diagram 1: Trading Volume by Investor type (Physical)



(Note) Data from 4 Jan to 28 Dec 2018. Total amount including 1st and 2nd Sectors of Tokyo and Nagoya markets.

(Source) SMAM, based on Tokyo Stock Exchange, Inc. data.

“Diagram 2: Trading Volume by Investor type (Futures)



(Note) Data from 4 Jan to 28 Dec 2018. Total amount including Nikkei 225 Futures, Nikkei 225 mini, TOPIX Futures, mini-TOPIX Futures and JPX-Nikkei Index 400 Futures.

(Source) SMAM, based on Tokyo Stock Exchange, Inc. data.

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Although, China announced expansion of imports from US at US-China ministerial trade talks, it was within market expectation. According to announcement by Whitehouse, there are still many unresolved issues other than the progress in 7 items including reinforcement related to technology transfer. However, it seems that continuation of talk was within market expectation, as most of market participants did not expect any agreement in structural problem this time.

After US companies' financial results announcements, the stock prices of Apple and Facebook sharply rose despite the fall in Amazon.com, whose Jan-Mar 2019 sales estimate did not reach market expectation. Japanese financial results related to semiconductor, electric appliances and FA as well as machine tools seemed to be affected by Chinese economic slowdown and Apple Shock. However, it did not surprise the market negatively as it was within market's expectation.

The Japanese stock market is discounting negative events steadily. However, foreign investors' behavior is still the key for strong recovery.

Dow Jones Industrial Average (DJIA) rose 1.32% last week. Meanwhile, Nikkei 225 only rose 0.07% for the same week, lagging behind DJIA. Nikkei 225 seemed to be affected by stronger JPY against USD (USD/JPY rate reached 108.50 at some point on 31 January) as USD weakened against major currencies due to US long term interest rate decline by dovish FOMC outcome.

However, lately Nikkei 225 seems to be testing the bottom as it had discounted important events in-and-out of Japan. In order for Japanese stock to return its bullish trend, foreign investors who had sold Japanese stocks (net of approx. JPY5.7tn) and Japanese stock futures (net of approx. JPY7.5tn) last year, need to be in the situation to consider buying back the stocks (Diagram1&2). Specifically, the situation in which the negative views on global economy will improve due to (1) progress in Brexit and US-China trade friction and (2) improvement in economic indicators of US and China.

***Please note that this report is a translation of Japanese report written on 4 February, 2019.**

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