

Japan Equity Strategy

3Q results and market outlook; raising year-end targets

Investment Strategy

3Q results solid; raising year-end targets for equities

Profits in 3Q rose sharply. Margins improved across the board and companies increased their "earnings power." However, companies with high sales exposure to Europe or China or with several kinds of raising costs saw earnings deteriorate. As such, 3Q results were a contrast of negatives and positives.

Based on 3Q results and our scenarios explained below, we raise our year-end targets for Japanese equities. Our new forecasts are 41,000 for the Nikkei 225 and 2,850 for the TOPIX (previously 38,500 and 2,715). We believe the conditions are in place for the Nikkei to break through its 1989 record high, with 40,000 just a passing point.

Real wages/manufacturing cycle to recover from Apr-Jun

We see the risk of a rapid correction, as the market is increasingly being dominated by trading in stocks with large index weights. However, we see no real need for concern about the outlook. This "single-focus market" reflects the outsize earnings contributions of certain large companies, which is not removed from fundamentals. The earnings estimate revision index improved further for Apr-Jun and Jul-Sep, suggesting more companies are likely to report an upturn in earnings. Improvement in the revision index is likely to be spurred by growth in real wages for domestic demand-related sectors and by a recovery in the manufacturing cycle for overseas demand-related sectors.

More corp. reforms/buybacks in May with full FY-results

3Q results included a raft of management initiatives to improve capital efficiency. Amid pressure from the TSE, we expect even more companies to disclose measures to improve P/B multiples and capital efficiency when they release full-year earnings and medium-term business plans in May. As part of this trend, share buybacks are likely to increase substantially. Companies that say they are currently considering reforms tend to have smaller market caps and significant scope to fund buybacks. If more companies report a recovery in earnings for Apr-Jun, investor focus could broaden to small cap stocks, supporting even firmer market trends. Exhibit 25 shows a list of quality cyclical stocks and Exhibit 26 is a list of stocks that beat 3Q earnings forecasts.

19 February 2024

Investment Strategy
Japan

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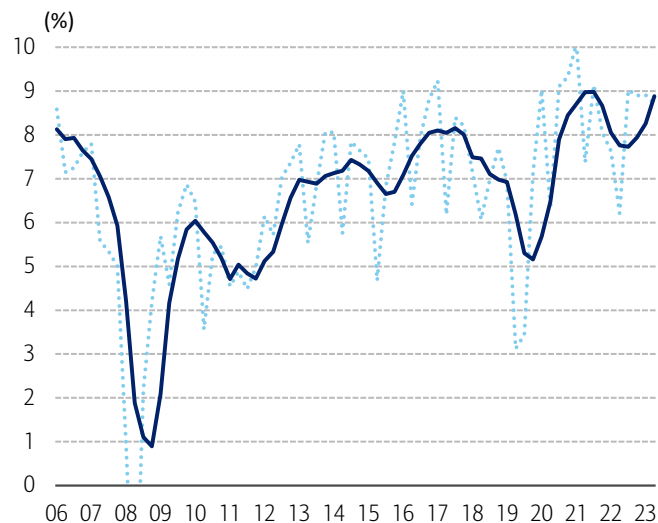
3Q results: Solid with a mix of positives and negatives

First we summarize 3Q (Oct-Dec) FY3/24 results. Earnings were solid overall. However, as discussed below, there was a mix of positives and negatives. TOPIX constituents with fiscal years ending in February or March (excluding SoftBank Group) reported strong growth in 3Q profits. Growth came in at 4.0% for sales, 16.7% for OP, 20.6% for RP and 24.9% for NP (Exhibit 6). (Exhibit 7; 1-3Q cumulative total: net sales: +5.1%, OP +16.7%, RP+13.5%, NP +14.7%).

Margins improved across the board on price hikes, the weak yen and cheaper raw materials, lifting so-called "earnings power" (Exhibit 1). Excluding SoftBank, profit growth in the manufacturing sector (NP +33.3%) outstripped growth in the non-manufacturing sector (+11.5%), reversing the recent trend. This reflected a large rise in profits in the transportation equipment sector, suggesting the manufacturing cycle is bottoming. However, there were also some negatives in 3Q results. Looking at profit growth for companies with high sales exposures to Japan, the US, Europe and China, companies oriented to Japan or the US saw a steep rise in profits, while those focused on Europe or China posted sluggish growth. There is a growing gap in earnings performance (Exhibit 2). Some companies reported weaker-than-expected earnings, reflecting less success with pushing through price hikes and curbing labor, logistics and raw material costs.

Exhibit 1: TOPIX RP margin (fiscal year ending in Mar or Feb, ex SBG)

TOPIX RP margin continued to increase



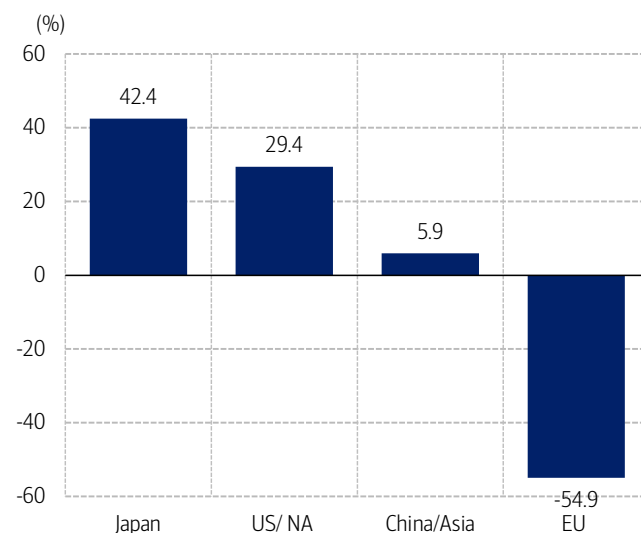
Source: QUICK, BofA Global Research

Note: based on TOPIX companies with fiscal year ending on February and March. Dotted line shows 4-quarter MA.

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Exhibit 2: 3Q RP growth by region (% YoY of aggregate sum)

Companies with higher US/ Japan sales exposure tend to have higher RP growth in 3Q vs. those with higher China/ EU sales exposure



Source: QUICK, BofA Global Research

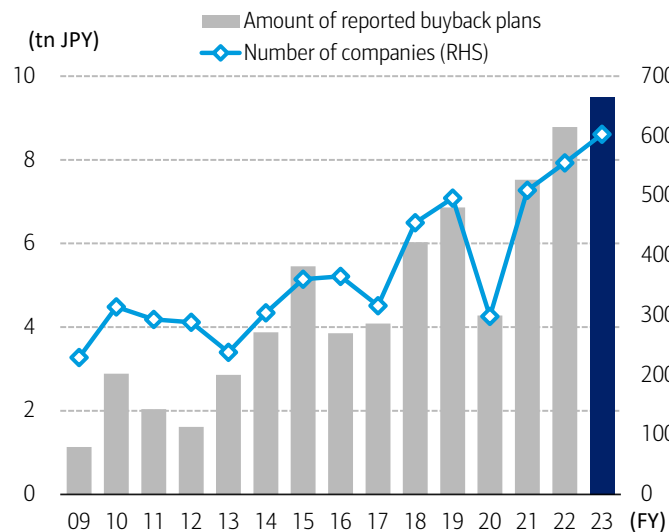
Note: we screen TOPIX companies with fiscal year ending in March with 1) mkt cap above 100 bn JPY; 2) regional sales ratio above 30%.

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What was the picture for shareholder returns in 3Q? Momentum was strong overall. Both the total value of buybacks and the number of companies repurchasing shares were at their highest levels since FY09 (Exhibit 3). The market has typically seen an increase in buybacks when share prices are falling, but the increase this year amid the strong rally is evidence that Japanese companies are changing their stance on capital efficiency. The upward revision to dividend forecasts also exceeds the 10-year average (Exhibit 4).

Exhibit 3: TOPIX cumulative buyback value and plans (FYTD)

Record-high buyback number and value since 2009



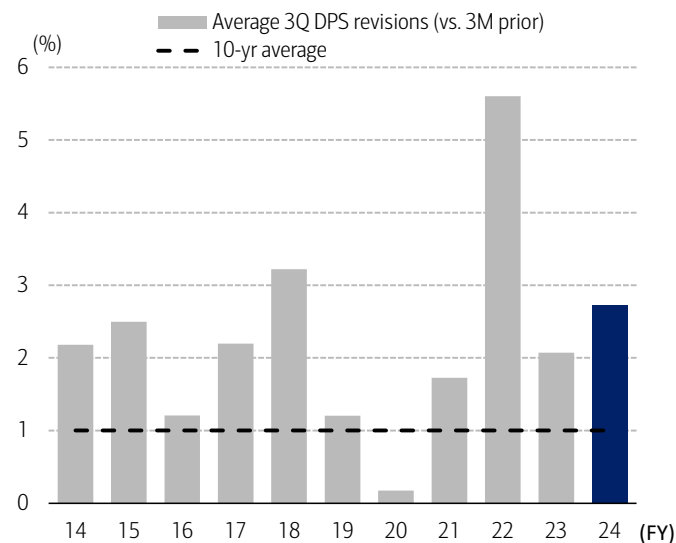
Source: QUICK, BofA Global Research

Note: we aggregate share buybacks from Apr 1 to Feb 14 for each fiscal year.

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Exhibit 4: % average DPS revisions (vs. 3-month prior) during 3Q earnings

The average DPS revisions surpassed its 10-yr average



Source: QUICK, BofA Global Research

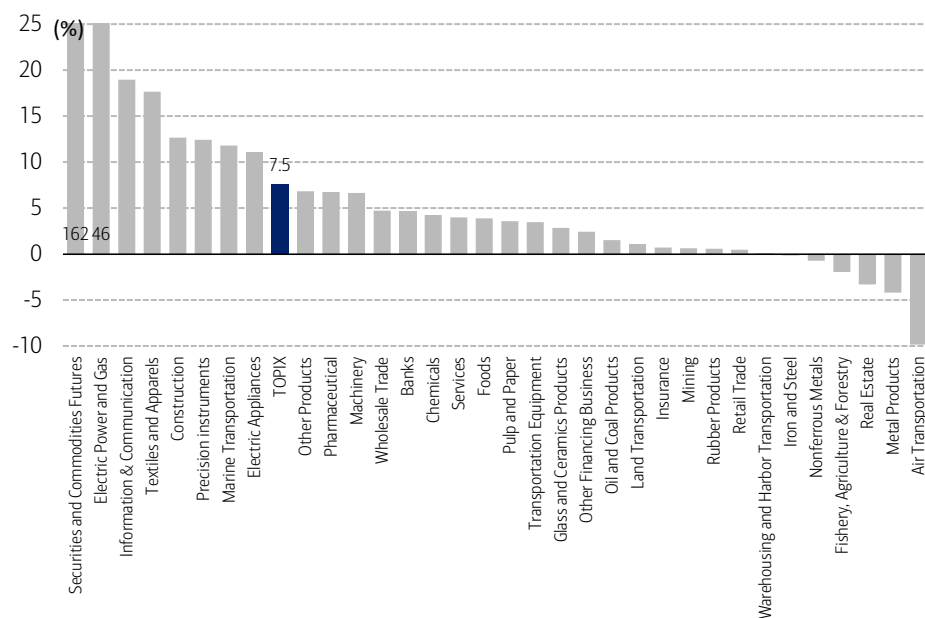
Note: Based on TOPIX companies with fiscal year ending in March. Based on corporate guidance.

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Guidance was raised 9.9% for RP and 8.6% for NP, but is probably still conservative. Progress toward full-year guidance was 83.7% for RP and 83.6% for NP, both above 75% (Exhibit 7). Forex assumptions (¥138.9/USD, ¥149.5/EUR) are based on a stronger yen than prevailing rates. Also, RP guidance is 7.5% below consensus expectations (Exhibit 5). Full-year results appear to be on track to beat guidance.

Exhibit 5: % deviation of consensus vs. corporate guidance (RP, Feb & Mar TOPIX companies)

The overall corporate guidance still 7.5% below market consensus



Source: QUICK, BofA Global Research

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Exhibit 6: Oct-Dec earnings statistics for companies with fiscal year ending in Mar or Feb

3Q RP (ex-SBG) grew 20.6%; corporates upgraded RP guidance by 9.9%

Sector names	Oct-Dec results (FY3/24 & FY2/24, YoY%)				Fiscal year corporate guidance revisions (%)			
	Sales	Operating profit	Recurring profit	Net Income	Sales	Operating profit	Recurring profit	Net Income
TOPIX	4.0	16.7	33.0	44.7	2.0	6.3	9.9	8.6
TOPIX (Ex SBG)	4.0	16.7	20.6	24.9	2.0	6.3	9.9	8.6
Manufacturing industries	5.8	21.7	30.0	32.0	3.1	6.7	13.0	12.0
Non-manufacturing industries	-0.3	9.6	33.5	65.3	-0.1	6.0	7.7	6.6
Non-manufacturing industries(Ex SBG)	-0.4	9.6	3.1	10.0	-0.1	6.0	7.7	6.6
Financial industries	14.8	15.2	40.6	40.6	9.2	-1.9	4.0	3.5
Foreign demand oriented	10.1	20.2	27.4	29.8	5.4	13.2	18.6	18.1
Electric Appliances	1.2	-2.1	12.0	10.3	1.1	-5.4	-1.1	-1.0
Transportation Equipment	17.4	47.6	43.0	51.1	9.4	38.6	43.6	45.3
Machinery	7.6	10.0	25.5	31.9	1.6	-3.0	-1.1	-2.5
Precision instruments	7.7	-11.4	-2.7	-11.8	2.6	-18.8	-26.0	-14.5
Cyclical	-1.4	28.7	9.8	8.7	-0.5	-0.8	4.8	2.9
Chemicals	-2.4	8.7	20.4	13.7	-3.7	-14.9	-3.7	-15.1
Wholesale Trade	-1.0	3.6	-3.6	-4.8	0.4	5.3	3.7	5.3
Iron and Steel	0.5	4.1	3.4	12.5	-2.9	7.4	7.8	17.7
Nonferrous Metals	2.4	71.3	80.8	141.9	0.3	-3.4	4.7	-1.4
Glass and Ceramics Products	3.1	23.8	28.3	25.6	1.1	8.9	14.2	17.2
Textiles and Apparels	-0.1	2.3	14.3	87.7	-3.5	-31.5	-22.0	-22.5
Oil and Coal Products	-5.2	1.9	1.9	1.5	3.4	33.8	39.9	47.2
Rubber Products	8.4	37.8	35.8	54.5	5.3	22.5	24.6	22.3
Marine Transportation	-4.7	-33.6	-77.1	-73.0	5.9	13.6	15.6	4.4
Pulp and Paper	-1.7	276.6	8.4	2.7	-3.1	-12.0	-6.7	-8.8
Mining	-20.4	-48.0	-45.5	-39.5	7.2	31.4	33.7	32.5
Domestic demand oriented	3.7	-2.2	48.8	78.2	0.6	2.9	4.6	6.4
Retail Trade	2.8	14.6	17.2	26.7	1.4	5.8	6.5	4.6
Information & Communication	4.0	-18.8	133.5	399.6	0.2	1.6	0.1	2.5
Land Transportation	4.6	33.0	32.2	22.0	-0.9	13.4	16.6	17.2
Construction	9.1	-0.3	0.3	-6.6	0.8	-5.8	-4.7	-1.6
Other Products	0.0	-4.5	9.3	9.9	1.7	-2.5	7.8	21.9
Services	-0.6	-1.3	-8.9	-11.1	-0.3	-0.4	0.8	0.7
Metal Products	6.1	24.6	45.0	18.6	1.4	1.5	9.9	11.9
Air Transportation	13.4	11.7	27.7	29.9	2.3	34.5	62.5	53.8
Warehousing and Harbor Transportation	-8.9	-14.0	-11.7	9.0	-27.7	-23.6	-24.4	-23.8
Financials	13.4	5.0	34.7	36.1	5.7	0.5	3.6	3.3
Banks	24.8	--	36.9	29.5	6.8	--	2.5	0.4
Insurance	3.5	--	63.2	93.6	11.0	--	8.0	14.3
Securities and Commodities Futures	39.3	19.4	54.6	-14.3	--	--	--	--
Real Estate	3.1	-6.3	-10.2	-2.8	-0.1	1.2	2.0	2.0
Other Financing Business	8.7	13.4	8.4	20.9	0.7	-1.9	-1.5	0.8
Defensives	-9.3	90.9	114.4	14.6	-1.9	6.7	14.4	7.2
Pharmaceutical	1.3	-25.7	-27.8	-27.5	3.3	-23.6	-15.6	-21.8
Electric Power and Gas	-19.0	3.8	3.5	1.3	-5.7	31.1	38.1	25.3
Foods	2.7	18.0	22.3	13.8	0.2	10.8	10.2	10.0
Fishery, Agriculture & Forestry	0.1	2.3	9.1	65.1	1.3	5.6	11.4	12.7

Source: BofA Global Research, QUICK

Note: SBG = SoftBank Group.

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Exhibit 7: Cumulative (1Q-3Q) earnings statistics for companies with fiscal year ending in Mar or Feb

Cumulative (1-3Q) RP (ex-SBG) grew 16.7%, with 83.2% cumulative RP progress rate

Sector names	Apr-Dec (1Q-3Q) cumulative results (FY3/24 & FY2/24, YoY%)				Cumulative progress rate vs. FY corporate guidance (%)			
	Sales	Operating profit	Recurring profit	Net Income	Sales	Operating profit	Recurring profit	Net Income
TOPIX	5.1	16.7	17.3	20.4	74.6	80.0	83.2	83.7
TOPIX (Ex SBG)	5.1	16.7	13.5	14.7	74.6	80.0	83.2	83.7
Manufacturing industries	6.3	11.4	13.0	19.1	74.7	77.7	81.2	81.4
Non-manufacturing industries	0.8	30.5	14.4	12.3	73.9	81.8	84.4	85.7
Non-manufacturing industries(Ex SBG)	0.8	30.5	4.9	-1.4	73.7	81.8	84.2	85.5
Financial industries	17.6	3.0	41.5	49.2	75.8	83.4	85.0	86.2
Foreign demand oriented	11.3	21.5	23.9	32.0	74.9	75.2	79.7	79.2
Electric Appliances	1.4	-13.1	-7.4	-4.4	74.5	70.4	76.4	72.5
Transportation Equipment	19.7	72.2	62.2	78.2	74.5	81.3	83.1	86.3
Machinery	8.1	6.2	8.7	9.1	76.0	76.9	81.8	83.2
Precision instruments	6.6	-23.5	-17.3	25.5	73.9	75.8	76.8	81.4
Cyclical	-3.6	-6.0	-21.0	-24.4	74.1	79.5	83.2	82.4
Chemicals	-4.1	-17.7	-16.3	-16.0	74.5	84.1	85.2	86.7
Wholesale Trade	-4.3	-2.6	-12.7	-13.6	74.2	74.4	83.2	79.0
Iron and Steel	4.0	-4.5	-6.2	-0.4	74.4	75.6	85.5	85.5
Nonferrous Metals	-0.2	0.5	-18.8	-30.0	74.5	71.1	77.8	77.2
Glass and Ceramics Products	5.2	19.8	39.7	65.3	73.9	79.2	83.3	88.6
Textiles and Apparels	-1.1	-21.1	-21.1	-21.3	71.4	69.9	72.8	71.7
Oil and Coal Products	-10.0	13.2	13.7	23.4	74.4	73.1	73.9	75.4
Rubber Products	9.7	64.7	44.9	70.9	73.8	75.8	81.6	85.8
Marine Transportation	-7.9	-31.6	-78.2	-80.2	74.9	95.8	96.0	100.9
Pulp and Paper	2.3	148.0	116.9	485.5	69.8	67.3	67.0	66.6
Mining	-1.7	-0.7	-11.0	-8.1	69.3	69.1	71.3	69.2
Domestic demand oriented	5.7	8.5	15.9	13.1	74.1	81.7	83.8	86.1
Retail Trade	4.1	18.3	17.4	12.1	74.4	74.2	74.0	87.7
Information & Communication	5.6	-6.4	11.8	16.9	73.9	85.5	90.5	90.2
Land Transportation	7.4	55.2	55.9	27.4	75.1	92.0	93.0	94.1
Construction	11.3	8.2	7.3	9.5	72.8	66.2	69.9	69.5
Other Products	3.5	2.0	5.9	8.6	77.7	84.3	83.2	82.5
Services	2.1	-1.4	-0.5	-10.1	73.9	80.4	83.4	83.8
Metal Products	6.0	14.2	11.8	10.1	73.5	69.7	74.4	69.6
Air Transportation	23.3	152.8	183.0	197.6	72.9	75.2	80.2	78.6
Warehousing and Harbor Transportation	-11.3	-21.2	-19.8	-16.4	74.4	74.9	77.6	83.6
Financials	16.2	2.6	35.4	42.7	75.9	82.8	85.2	85.3
Banks	30.2	-0.8	27.5	30.1	76.3	85.3	86.0	86.1
Insurance	5.2	--	145.0	225.9	69.8	65.6	66.1	64.8
Securities and Commodities Futures	58.2	85.2	83.5	49.1	89.7	82.0	92.0	95.4
Real Estate	5.7	0.9	-3.5	1.7	71.8	76.2	77.4	73.9
Other Financing Business	5.0	2.8	4.1	13.5	74.4	82.8	84.2	85.2
Defensives	-1.1	246.0	298.2	1049.9	74.4	86.0	87.9	87.6
Pharmaceutical	4.4	-19.0	-24.7	-24.9	75.2	82.4	85.2	82.7
Electric Power and Gas	-6.1	5.6	5.0	2.8	73.3	91.6	93.0	91.6
Foods	4.9	20.1	23.6	47.6	75.3	81.4	83.2	86.6
Fishery, Agriculture & Forestry	3.1	11.7	9.5	20.7	71.3	81.6	83.6	87.4

Source: BofA Global Research, QUICK

Note: SBG = SoftBank Group

Year-end targets raised to 41,000 for Nikkei 225, 2,850 for TOPIX

Based on recent earnings trends and our scenarios explained below, we raise our year-end targets for Japanese equities. Our new forecasts are 41,000 for the Nikkei 225 and 2,850 for the TOPIX (previously 38,500 and 2,715).

Last year, we explained that record highs for Japanese equities were within reach in 2024 if three conditions aligned: (1) sustained wage inflation (with Shunto spring wage talks key), (2) serious reforms to address capital efficiency, and (3) stabilization in the US economy (see Japan Year Ahead 2024, 29 November). More recently, we flagged growing upside risk for Japanese equities (see [Japan Insight](#), 30 January). We believe the above three conditions now look increasingly likely and we raise our P/E assumption from 14.3x to 14.8x. We also revise up our N/T ratio from 14.2x to 14.5x, taking into account sustained inflows from overseas investors. We see the Nikkei 225 exceeding its 1989 record high by the end of 2024, with 40,000 just a passing point. TOPIX could also reach an all-time high, depending on the rate of improvement in the earnings estimate revision index.

Exhibit 8: TOPIX, Nikkei forecasts and top-down EPS estimates

We expect TOPIX/Nikkei 225 to reach 2,850pt/¥41K in 2024

	TOPIX EPS	TOPIX EPS (YoY)	TOPIX (pt)	Nikkei225 (yen)
Mar '23 (A)	145.0	3.7%	2,004	28,041
Dec '23 (E)	166.3	14.7%	--	--
Dec '24 (E)	--	--	2,850	41,000
Dec '24 (previous)	--	--	2,715	38,500
Mar '25 (E)	181.2	9.0%	--	--
Mar '26 (E)	196.3	8.3%	--	--

Source: BofA Global Research

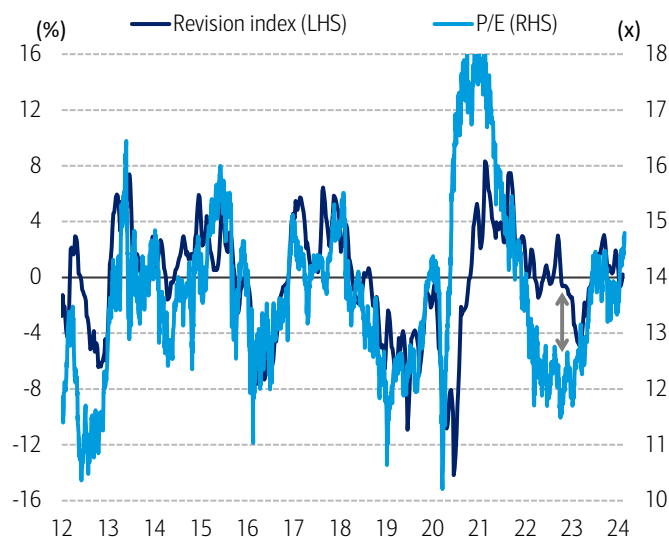
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Caution with "Single-focus market"

Next we discuss our scenarios for the market outlook. First, investors' recent focus on stocks with large index weights – what we call the "single-focus market" – is fraught with risk. Although we have raised our year-end targets, we see the risk of volatility near term from the recent rally. While the TOPIX P/E is below its historical peak, it is higher than the level indicated by the earnings estimate revision index (Exhibit 9). The Nikkei 225 P/E is even higher. 3Q results suggest the index could be revised up slightly, but it is not enough to justify the increase in P/E (Exhibit 10).

Exhibit 9: TOPIX revision index and 12-month forward P/E

TOPIX P/E, albeit far from the historical peak level, appears to have surpassed the level that earnings revision implies



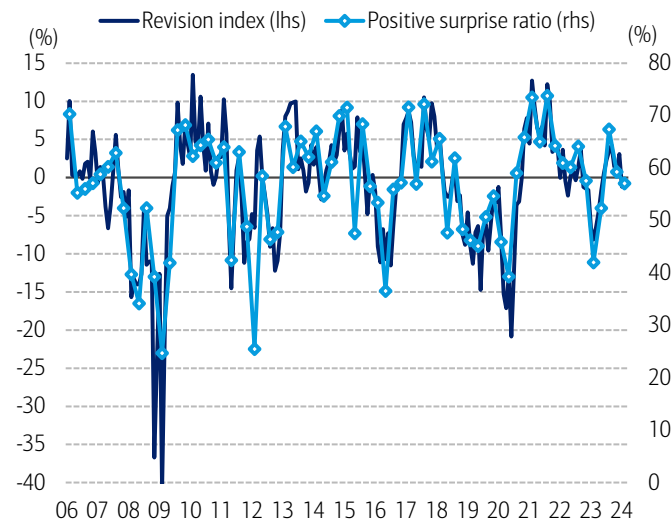
Source: BofA Global Research, Refinitiv

The revision index (4 weeks moving average), P/E is based on I/B/E/S consensus estimate for 12-month forward EPS.

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Exhibit 10: TOPIX revision index and results surprise ratio

3Q earnings surprise ratio suggests no sharp upgrades of revision index



Source: BofA Global Research, Refinitiv, Bloomberg

Note: The results positive surprise ratio is the percentage of companies that reported quarterly EPS that beat the Bloomberg consensus estimate. It is a mechanical calculation that does not take into account the degree of divergence. The revision index (I/B/E/S consensus estimate for 12-month forward EPS) is for one quarter ahead.

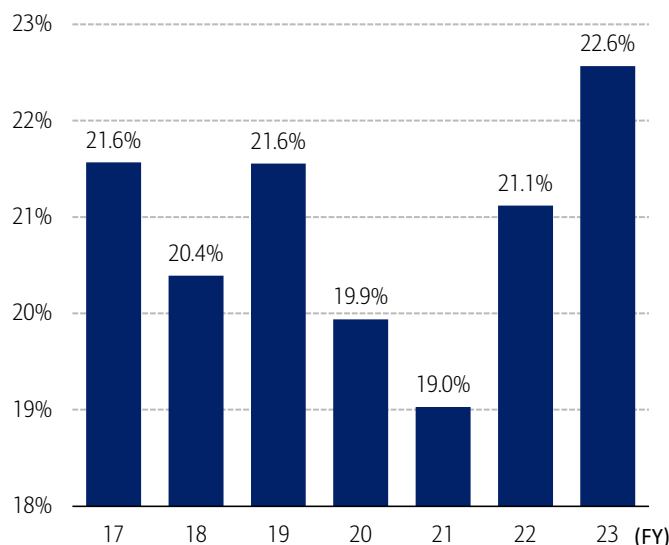
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However, the broader market trend is important. Assuming there is a near-term correction (which may not materialize given strong market momentum), we see upside potential in the Apr-Jun and Jul-Sep quarters, for several reasons. First, the "single-focus market" is not an unexplainable trend removed from fundamentals. Some market movements look overblown, but the broader trend reflects the outsize earnings contributions of certain large companies. Second, the macro cycle is on an upward path. The earnings estimate revision index recovered for Apr-Jun and Jul-Sep, suggesting more companies are likely to report an upturn in earnings.

Going back to the first point, the top 10 stocks by market cap (excluding SoftBank) account for a large proportion of earnings in the current fiscal year (Exhibit 11). This explains why the positive earnings surprise was not that significant compared with the rate of overall profit growth. For example, the outperformance by the TOPIX Core 30 – an unlikely phenomenon in recent years – is being supported by strong EPS (Exhibit 13). Actual upward revisions to EPS are likely to exceed the size of revisions indicated by the revision index, which is compiled from the number of upward and downward revisions made by analysts.

Exhibit 11: Percentage of cumulative RP (1Q-3Q) contribution from top 10 companies in terms of mkt cap

FY23 saw larger earnings contribution from top 10 mkt-cap companies



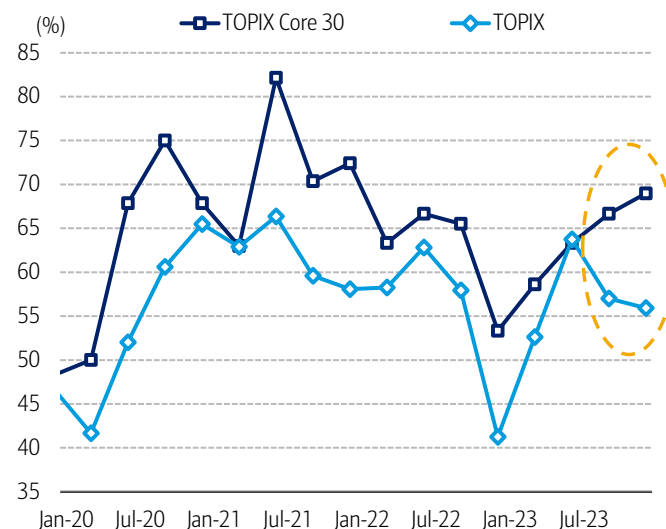
Source: BofA Global Research, QUICK

Note: based on TOPIX companies with fiscal year ending in March. Excluding SoftBank Group among top 10 mkt cap companies.

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Exhibit 12: Earnings positive surprise ratio of TOPIX Core 30 and TOPIX

The earnings surprises of TOPIX Core 30 names continued to improve

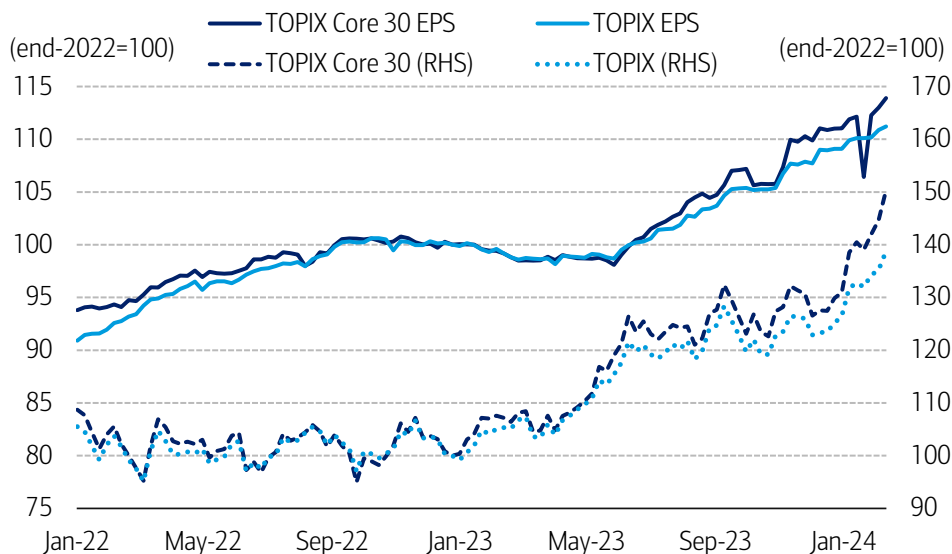


Source: BofA Global Research, Bloomberg

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Exhibit 13: EPS and index price of TOPIX and TOPIX Core 30

The outperformance of TOPIX Core 30 since last year was underpinned by the earnings strength



Source: BofA Global Research, Refinitiv

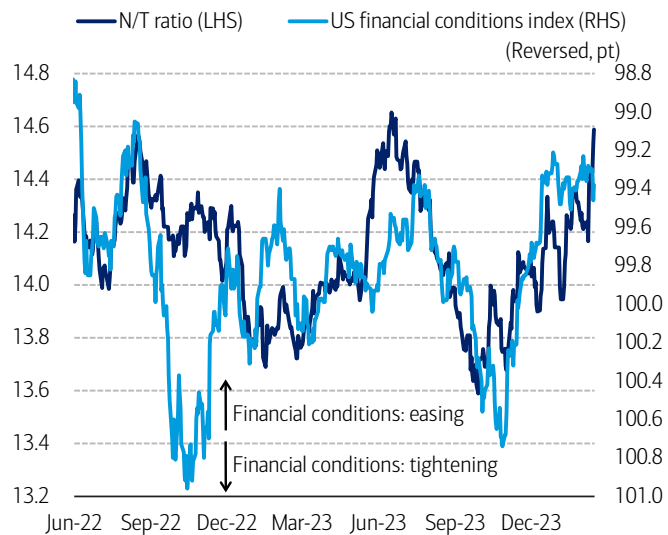
Note: EPS is based on I/B/E/S consensus estimate for 12-month forward estimate.

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The current macroenvironment also seems to be conducive to the "single-focus market." The N/T ratio tends to rise when financial conditions are accommodative (Exhibit 14) and foreign funds are flowing into the market (Exhibit 15), which is happening now. This pattern is unlikely to change much as long as investors expect the Fed to cut rates. However, upside to the US January CPI and PPI needs watching. We need to confirm whether there are any signs that the disinflationary trend in the US is losing momentum.

Exhibit 14: N/T ratio and US financial conditions index

N/T ratio tends to increase along with easing US financial conditions

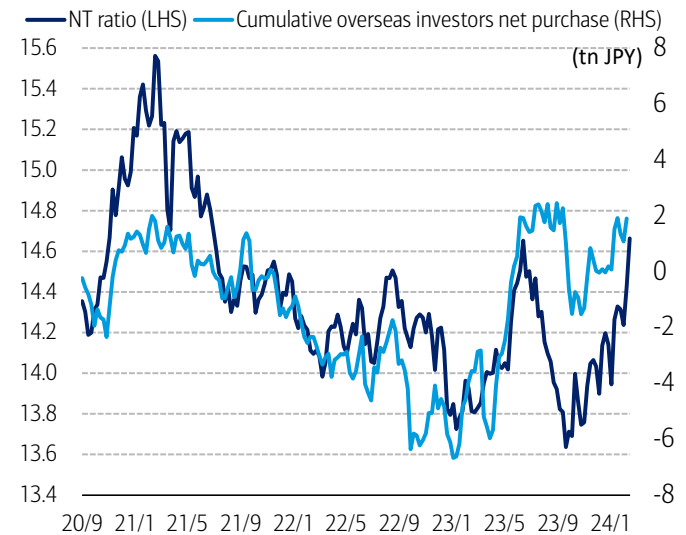


Source: BofA Global Research, Bloomberg

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Exhibit 15: N/T ratio and overseas investors' cumulative net purchases

N/T ratio tends to rise along with net overseas net inflows



Source: BofA Global Research, QUICK

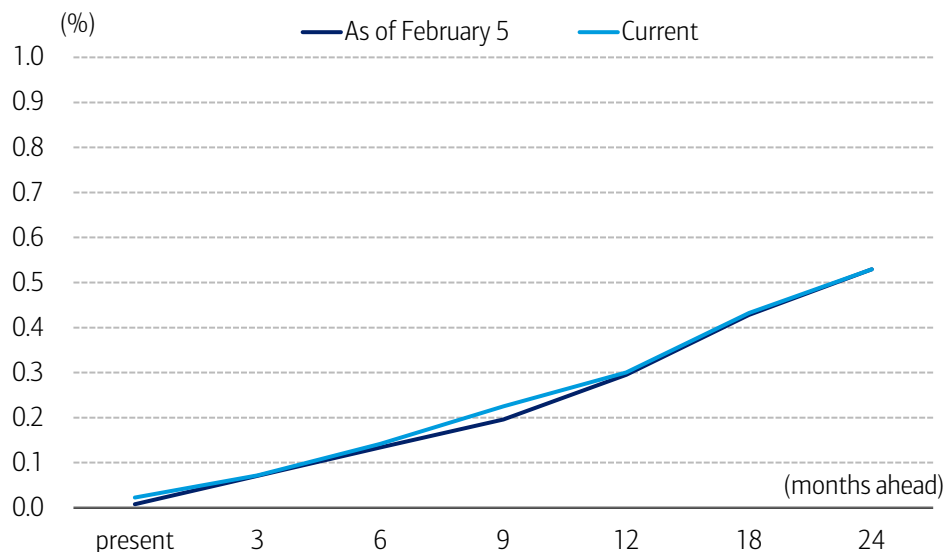
Note: we aggregate both cash equities and futures for cumulative overseas investors net purchases.

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The speech by BoJ Deputy Governor Shinichi Uchida on 8 February also had a large impact on the market. The BoJ is watching the market's assumption that the policy rate will rise to only around 0.5% over the next two years (Exhibit 16). In his speech, Uchida said, "Nonetheless, the Bank does not project that inflation will significantly exceed 2%." This signaled that rate hikes could only reach about 0.5% over the next two years (with core CPI at 2%, the actual policy rate would still be below -1.5%; the content of the speech was in line with our economists' expectations that the BoJ will adjust policy at the March or April meeting; see [Japan Watch](#), 31 January).

Exhibit 16: The OIS pricing of the BoJ's policy rate

The market anticipates a gradual hiking cycle to 0.5% 2-years ahead



Source: BofA Global Research, Bloomberg

Note: based on the 5 Feb data shown in the file of BoJ's Deputy Governor Uchida's speech (on 8 Feb)

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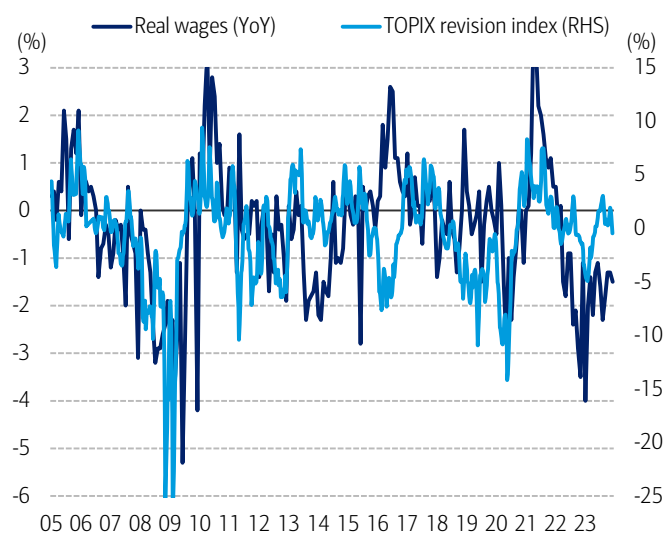
Real wages and manufacturing cycle to recover from Apr-Jun

Two macroeconomic forces are driving the improvement in the earnings estimate revision index. First, growth in real wages. Our economists forecast a base-up rate of around 3% in the FY24 Shunto spring labor negotiations (see [Wages update](#), 6 February). If the actual increase is consistent with this forecast, the market could start factoring in growth in real wages. With headline inflation now stabilizing, real wages are likely to begin rising in Apr-Jun after the wage negotiations. The BoJ does not expect the impact of the negotiations to be fully reflected in monthly wages until the summer, so real wages could turn positive from the second half of the Jul-Sep quarter.

Spring wage talks tend to be influenced by the previous year's inflation rate (Exhibit 18). Last year, the high rate of inflation eroded consumers' real income and also led to the divergence in earnings performance. While wages are likely to rise this year, inflation has started to subside. "Second-year" inflation tends to create this benign mix.

Exhibit 17: Real wages and TOPIX revision index

TOPIX revision index tends to improve when real wages increase



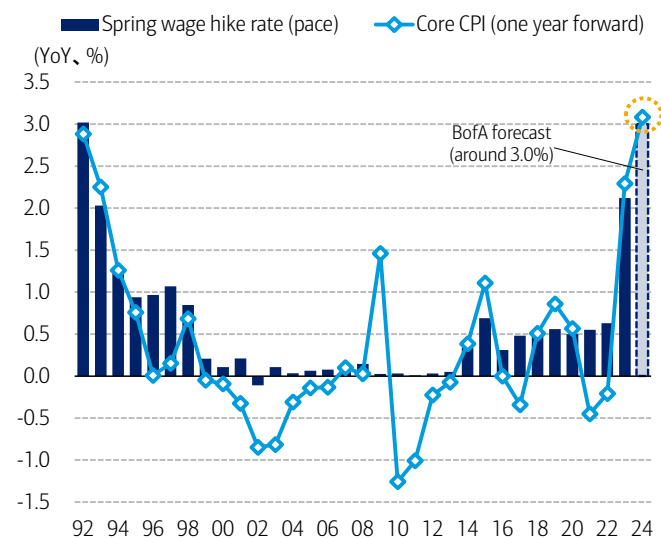
Source: BofA Global Research, Refinitiv, INDB

Note: Real wages exclude the impact of consumption tax hike; based on common business since 2016. Based on I/B/E/S 12-month forward EPS estimate, 4 week MA for revision index

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Exhibit 18: Spring wage hike rate and core CPI

We expect a c. 3% wage growth in 2024 (vs. 2.1% last year)



Source: BofA Global Research, Ministry of Health, Labour and Welfare, RENGO

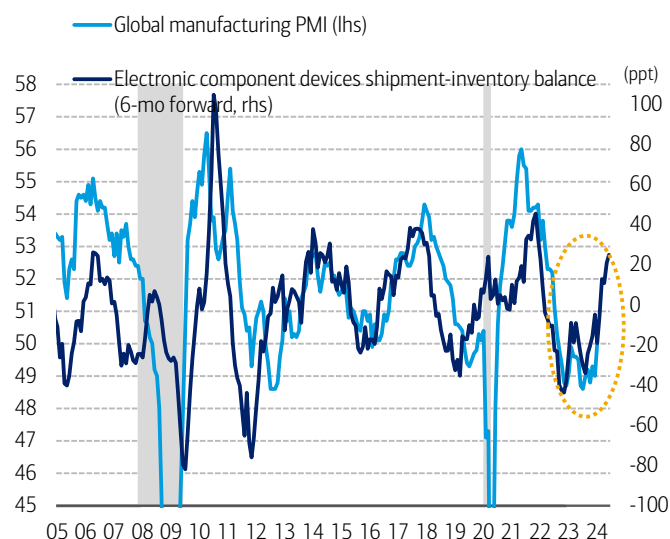
Note: We calculate the calendar average for the core CPI

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Second, the recovery in the manufacturing cycle. The shipment-inventory balance for electronic components and devices, a strong leading indicator, points to recovery (Exhibit 19). For Japanese companies, which have a high ratio of manufacturing activity, the direction of the cycle is of critical importance. While there are likely to be some fluctuations, we expect the recovery in the revision index to gain momentum in Apr-Jun before becoming more pronounced in Jul-Sep (Exhibit 20). Another key factor for earnings visibility will be comments by companies in year-end results showing confidence in earnings recovery from 2H FY24. The cycle could also gain further momentum if the Fed successfully starts to cut rates (our forecast is June), pushing down funding costs.

Exhibit 19: Global manufacturing PMI and the shipment-inventory balance of electronic components

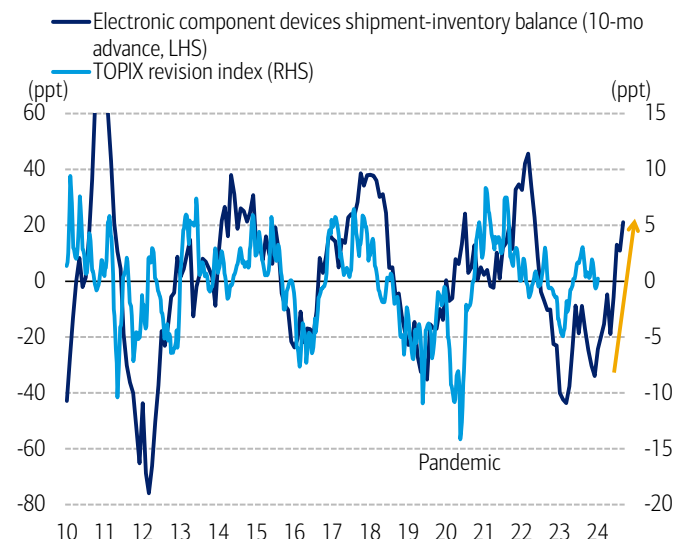
Manufacturing cycle (every 3-4 years) could be in the bottoming phase



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Exhibit 20: TOPIX revision index and the shipment-inventory balance of electronic components

Leading indicator implies further improvement of the revision index



Note: Based on I/B/E/S 12-month forward EPS estimate, 4 week MA for revision index.

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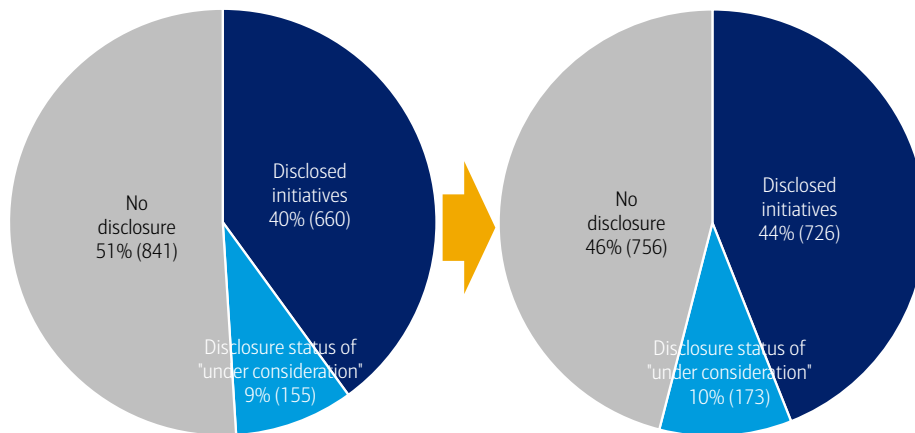
More corporate reforms and buybacks in May with full FY-results

What about corporate reforms? 3Q results included a raft of management initiatives to improve capital efficiency. Nippon Television Holdings made some striking changes to its shareholder return policy, and Mitsubishi Corp's ¥500bn share buyback was described as a "monster buyback" by the Financial Times. Activist investors are calling on Mitsui Fudosan to buy back ¥1tn worth of shares and sell its holdings in Oriental Land. After the FSA called on insurers to sell their cross-shareholdings (see Japan P&C insurance, 14 February), SOMPO Holdings declared its intention to unwind all its strategically held shares.

A growing number of companies are likely to disclose initiatives to improve P/B multiples and capital efficiency. The latest disclosure status list released by the TSE on 15 February, which aims to increase the "shame factor" for Japanese companies falling short on these metrics, shows progress is already being made, with 5% more companies disclosing or considering measures compared with the initial list on 15 January (Exhibit 21). We expect even wider disclosure of these measures in May when companies release full-year results and medium-term business plans. As part of this trend, share buybacks are likely to increase substantially. Since last year, in fact, we have seen an increase in buybacks as more companies have announced reform measures (Exhibit 22). On 15 January when the TSE published its first "name-and-shame" list, companies that had disclosed reform measures outperformed (Exhibit 23).

Exhibit 21: Status of Disclosure on “Action to Implement Management that is Conscious of Cost of Capital and Stock Price” (left: as of 15 Jan; right: as of 15 Feb)

More companies disclosed their initiatives

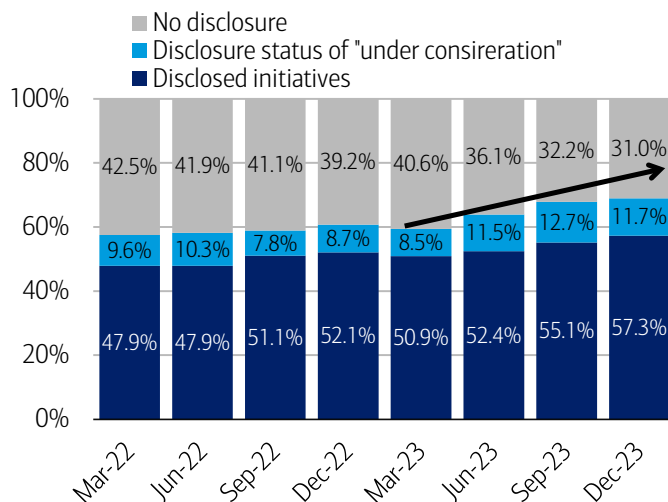


Source: BofA Global Research, JPX

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Exhibit 22: % of share buybacks by JPX disclosure status

Companies with JPX disclosure tend to increase share repurchases



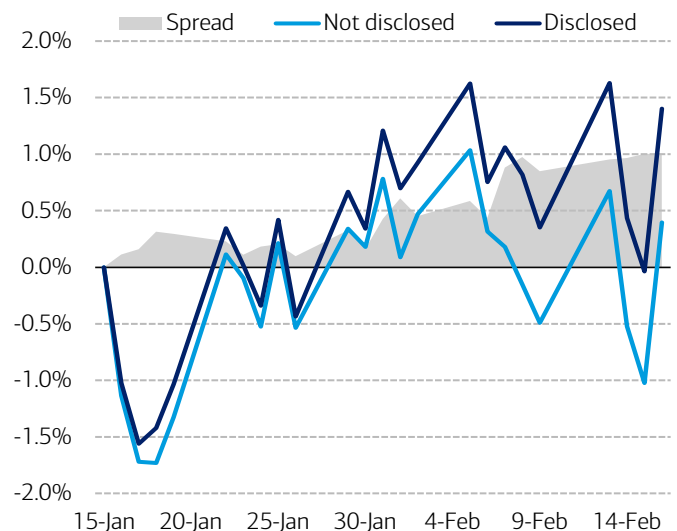
Source: BofA Global Research, JPX, QUICK

Note: Based on Prime Market. We aggregate buyback number based on JPX disclosure status.

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Exhibit 23: Performance gap by JPX disclosure status

Disclosed companies tend to outperform those with no disclosures



Source: BofA Global Research, JPX, QUICK

Note: Based on Prime Market. We calculate the performance gap based on JPX disclosure status

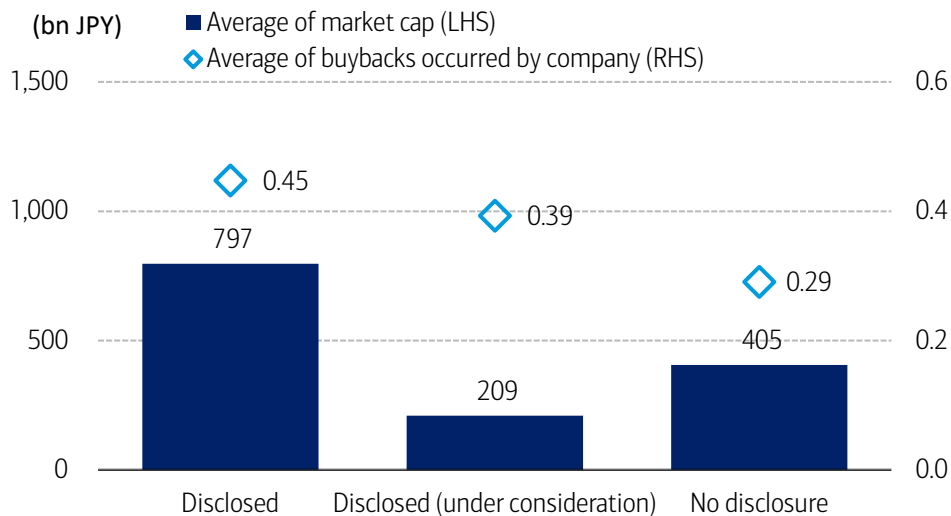
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To summarize, we expect the "single-focus market" to continue through the end of the Jan-Mar quarter, but the earnings estimate revision index is likely to improve in Apr-Jun and Jul-Sep, spurred by growth in real wages for domestic demand-related stocks and by a recovery in the manufacturing cycle for overseas demand-related stocks. Improvement in the revision index indicates more companies are seeing a recovery in earnings. We also anticipate an increase in share buybacks around the full-year results reporting season as more companies disclose measures to improve P/B and capital efficiency. In particular, we highlight companies that say they are currently considering reforms, as they tend to have smaller market caps and have significant scope to fund buybacks (Exhibit 24). If more companies report a recovery in earnings for Apr-Jun, investor focus

could broaden to include small cap stocks, supporting even firmer market trends. We assume the 2024 market peak will follow a double-top pattern, with the first peak in the second half of Apr-Jun or the first half of Jul-Sep, and the second peak near the end of the year.

Exhibit 24: JPX initiatives: Average mkt cap, average buyback per company by JPX disclosure status

We see scope for “Under consideration” companies to conduct share repurchases



Source: BofA Global Research, JPX, QUICK
Note: Based on Prime Market.

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Exhibit 25 shows a list of quality cyclical stocks favored by overseas investors in the current market environment (high beta/high ROE stocks with low leverage and prospects for solid earnings in next fiscal year). Highlights show stocks that reported 3Q results above expectations. However, caution is needed in periods when market trends are disrupted by fund inflows from overseas investors.

We also provide Exhibit 26, which lists companies that outperformed 3Q expectations and have disclosed guidance that is more bearish than consensus.

Exhibit 25: High Beta/ High ROE/ low leverage stocks with resilient earnings expectations next fiscal year (3Q earnings beats highlighted)

Large caps with ROE (FY2) above 8%, financial leverage below 3, beta above 1, FY2 RP growth above -2% and RP revision ratio above -2%

TSE	Name	Sector	Mkt cap (tn JPY)	RP growth (FY2, %)	RP revision (FY2, vs. 3 months prior, %)	ROE (FY2, %)	Beta (6m)	Financial leverage (x)	3Q result vs. QUICK consensus (%)	YTD relative return (% vs TOPIX)
7203	TOYOTA MOTOR CORP	Transportation Equipment	55.2	-0.4	21.1	13.3	1.5	2.6	8.9	21.4
8035	TOKYO ELECTRON LTD	Electric Appliances	15.9	27.9	6.7	24.7	1.5	1.5	15.4	23.5
9983	FAST RETAILING CO LTD	Retail Trade	12.4	8.9	19.2	16.2	1.1	1.8		7.0
4063	SHIN-ETSU CHEMICAL CO LTD	Chemicals	12.0	9.7	0.3	14.5	1.1	1.2	-3.5	-8.7
8058	MITSUBISHI CORP	Wholesale Trade	11.5	-1.2	6.6	10.9	1.4	2.7	-2.9	20.1
6501	HITACHI LTD	Electric Appliances	11.5	8.6	6.4	11.4	1.3	2.5	5.2	9.0
6098	RECRUIT HOLDINGS CO LTD	Services	10.7	0.5	4.8	15.0	1.1	1.7	1.5	-8.1
8001	ITOCHU CORP	Wholesale Trade	10.5	2.9	0.6	15.4	1.4	2.7	-1.8	5.4
7267	HONDA MOTOR CO LTD	Transportation Equipment	9.3	5.7	2.5	8.6	1.5	2.2	0.7	6.0
4568	DAIICHI SANKYO CO LTD	Pharmaceutical	8.8	18.5	-1.6	11.7	1.3	1.7	35.3	14.1
4519	CHUGAI PHARMACEUTICAL CO LTD	Pharmaceutical	8.6	5.9	12.2	18.5	1.1	1.2	0.7	-3.5
6902	DENSO CORP	Transportation Equipment	7.7	28.1	2.0	11.6	1.4	1.7	-38.5	12.7
7741	HOYA CORP	Precision Instruments	6.3	12.3	0.2	23.4	1.1	1.3	-3.4	-5.8
6981	MURATA MANUFACTURING CO LTD	Electric Appliances	6.2	19.5	4.1	10.5	1.2	1.2	-4.2	-10.3
6723	RENEAS ELECTRONICS CORP	Electric Appliances	5.3	17.8	3.0	17.5	1.3	1.6	-3.2	-7.1
6146	DISCO CORP	Machinery	4.7	39.0	24.1	28.2	1.3	1.4	-0.6	16.3
6503	MITSUBISHI ELECTRIC CORP	Electric Appliances	4.7	8.8	-0.4	8.2	1.3	1.7	3.7	-2.9
4543	TERUMO CORP	Precision Instruments	4.1	15.1	4.8	10.5	1.0	1.4	0.7	8.6
8002	MARUBENI CORP	Wholesale Trade	4.0	1.4	2.1	14.0	1.5	2.8	3.3	-2.2
4901	FUJIFILM HOLDINGS CORP	Chemicals	3.8	9.7	0.1	8.2	1.0	1.5	-4.7	0.1
6920	LASERTEC CORP	Electric Appliances	3.6	55.1	2.5	43.7	1.3	2.5	22.5	1.0
5401	NIPPON STEEL CORP	Iron & Steel	3.4	8.5	3.0	9.3	1.1	2.3	7.3	-3.4
6752	PANASONIC HOLDINGS CORP	Electric Appliances	3.4	10.6	-0.3	9.2	1.2	2.2	8.2	-9.9
7269	SUZUKI MOTOR CORP	Transportation Equipment	3.3	8.8	9.3	12.8	1.1	2.2	-1.5	0.1
6762	TDK CORP	Electric Appliances	3.0	28.6	9.3	10.1	1.3	2.2	8.1	7.3
6701	NEC CORP	Electric Appliances	2.6	19.6	2.0	8.5	1.1	2.5	-1.3	7.2
1605	INPEX CORP	Mining	2.5	1.9	4.7	8.7	1.1	1.6	-2.9	-5.5
4307	NOMURA RESEARCH INSTITUTE LT	Information & Communication	2.5	11.2	-0.2	19.9	1.1	2.1	0.5	-7.4
7735	SCREEN HOLDINGS CO LTD	Electric Appliances	1.9	6.8	15.2	19.4	1.2	1.9	1.1	44.0
6988	NITTO DENKO CORP	Chemicals	1.8	9.5	-0.5	11.8	1.1	1.3	2.6	16.0
6869	SYSMEX CORP	Electric Appliances	1.7	14.7	0.3	13.7	1.1	1.4	-3.2	-4.6
4091	NIPPON SANSO HOLDINGS CORP	Chemicals	1.7	-0.4	7.0	11.6	1.2	3.0	5.0	0.7
7202	ISUZU MOTORS LTD	Transportation Equipment	1.6	4.6	-0.3	12.9	1.2	2.3	13.5	3.4
7259	AISIN CORP	Transportation Equipment	1.5	28.1	4.0	8.7	1.4	2.4	-37.0	-3.0
9697	CAPCOM CO LTD	Information & Communication	1.5	12.5	-1.8	23.8	1.1	1.3		19.9
7272	YAMAHA MOTOR CO LTD	Transportation Equipment	1.5	6.8	6.1	14.8	1.5	2.3	-2.5	5.0
1812	KAJIMA CORP	Construction	1.5	8.3	-1.5	10.8	1.1	2.6	4.5	4.8
5411	JFE HOLDINGS INC	Iron & Steel	1.4	6.9	-1.9	8.8	1.1	2.6	0.8	-7.0
9766	KONAMI GROUP CORP	Information & Communication	1.4	9.7	3.2	13.9	1.1	1.5		21.9
6479	MINEBEA MITSUMI INC	Electric Appliances	1.2	40.8	-1.2	11.3	1.3	2.1	-4.9	-5.7
6504	FUJI ELECTRIC CO LTD	Electric Appliances	1.2	9.2	1.5	12.4	1.3	2.3	7.3	33.0
6383	DAIFUKU CO LTD	Machinery	1.2	15.0	0.3	13.2	1.1	1.7	7.9	3.8
4704	TREND MICRO INC	Information & Communication	1.2	25.1	28.7	21.6	1.1	2.1	-11.9	7.1
9009	KEISEI ELECTRIC RAILWAY CO	Land Transportation	1.2	25.0	0.9	10.4	1.1	2.4	11.6	-1.8
7261	MAZDA MOTOR CORP	Transportation Equipment	1.1	-0.6	18.8	11.7	1.4	2.3	-3.2	3.3
7936	ASICS CORP	Other Products	1.0	15.5	20.9	19.7	1.5	2.3	1.7	20.5
6305	HITACHI CONSTRUCTION MACHINE	Machinery	0.9	5.3	1.5	13.4	1.4	2.5	-6.0	1.5
6361	EBARA CORP	Machinery	0.9	14.7	18.5	14.8	1.4	2.2	15.9	3.5
1911	SUMITOMO FORESTRY CO LTD	Construction	0.9	8.7	9.6	13.2	1.1	2.4	8.3	-10.1
5334	NITERRA CO LTD	Glass & Ceramics Products	0.8	2.3	9.1	13.7	1.0	1.6	2.8	16.8
4183	MITSUI CHEMICALS INC	Chemicals	0.8	56.2	-1.7	10.8	1.1	2.6	-10.6	-14.5
4527	ROHTO PHARMACEUTICAL CO LTD	Pharmaceutical	0.7	10.1	3.6	14.4	1.1	1.5	0.5	-2.5
6370	KURITA WATER INDUSTRIES LTD	Machinery	0.7	13.5	2.2	9.7	1.1	1.7	3.6	-2.8
6845	AZBIL CORP	Electric Appliances	0.7	0.1	2.8	12.0	1.1	1.5	10.6	-7.6
5101	YOKOHAMA RUBBER CO LTD	Rubber Products	0.6	11.2	5.6	9.9	1.2	1.9	-0.4	1.6
6113	AMADA CO LTD	Machinery	0.6	2.5	7.5	8.2	1.3	1.3	-0.9	-3.4
8136	SANRIO CO LTD	Wholesale Trade	0.6	15.9	8.0	24.0	1.0	1.8	8.8	6.9
5929	SANWA HOLDINGS CORP	Metal Products	0.6	-0.1	10.4	15.5	1.2	1.8	2.1	9.0
6856	HORIBA LTD	Electric Appliances	0.6	13.3	26.0	12.4	1.0	1.6	12.3	8.5
4186	TOKYO OHKA KOGYO CO LTD	Chemicals	0.5	14.0	12.7	11.5	1.3	1.4	2.1	21.0
3116	TOYOTA BOSHOKU CORP	Transportation Equipment	0.5	-0.9	2.8	12.1	1.3	2.5	3.8	0.2

Source: BofA Global Research, QUICK

Note: Universe consists of TOPIX stocks with mkt cap above 450 bn JPY, screened based on the following conditions: ROE (FY2) above 8%, financial leverage below 3, beta above 1 and relatively resilient FY2 earnings above -2, RP revision above -2 over the last 3 months; listed in descending order of mkt cap. We highlight names with RP earnings beats (vs. QUICK consensus). This is a screen and not a recommended list either individually or as a group of stocks and options. Investors should consider the fundamentals of the companies and their own individual circumstances / objectives before making any investment decisions.

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Exhibit 26: Stocks with at least 5% 3Q earnings beats

Mkt cap above 400 bn JPY, 3Q earnings (OP or NP if OP is not available) above consensus at least 5%

TSE	Name	Sector	Mkt cap (bn JPY)	3Q result vs. QUICK consensus (%)	RP growth (FY1, %)	PER (FY2)	ROE (FY2, %)	YTD relative return (%, vs TOPIX)
7203	TOYOTA MOTOR CORP	Transportation Equipment	55,226	8.9	71.4	12.4	13.3	21.0
8035	TOKYO ELECTRON LTD	Electric Appliances	15,903	15.4	-29.3	37.2	24.7	29.9
6501	HITACHI LTD	Electric Appliances	11,455	5.2	-4.1	18.8	11.4	9.7
4568	DAIICHI SANKYO CO LTD	Pharmaceutical	8,785	35.3	48.1	49.8	11.7	14.2
4502	TAKEDA PHARMACEUTICAL CO LTD	Pharmaceutical	6,883	22.8	-69.3	30.2	4.4	-3.1
6857	ADVANTEST CORP	Electric Appliances	5,016	8.1	-50.6	51.0	23.9	37.3
6201	TOYOTA INDUSTRIES CORP	Transportation Equipment	4,651	10.7	25.5	18.2	5.7	13.7
6954	FANUC CORP	Electric Appliances	4,045	11.0	-25.8	30.1	8.0	-13.7
5401	NIPPON STEEL CORP	Iron & Steel	3,418	7.3	-25.2	7.0	9.3	-3.4
6752	PANASONIC HOLDINGS CORP	Electric Appliances	3,404	8.2	44.4	9.0	9.2	-9.9
9020	EAST JAPAN RAILWAY CO	Land Transportation	3,379	8.5	129.2	16.3	7.5	-1.1
6762	TDK CORP	Electric Appliances	2,954	8.1	3.3	18.4	10.1	7.0
4507	SHIONOGI & CO LTD	Pharmaceutical	2,167	24.3	-10.1	14.7	11.9	-6.6
4523	EISAI CO LTD	Pharmaceutical	1,934	18.1	24.2	33.8	6.9	-20.2
5020	ENEOS HOLDINGS INC	Oil & Coal Products	1,893	6.2	57.1	8.6	7.2	2.7
8601	DAIWA SECURITIES GROUP INC	Securities & Commodity Futures	1,670	7.2	64.5	16.8	6.9	-0.4
5802	SUMITOMO ELECTRIC INDUSTRIES	Nonferrous Metals	1,646	18.0	11.9	11.9	7.1	7.4
9202	ANA HOLDINGS INC	Air Transportation	1,588	20.9	53.2	12.4	13.2	-4.4
7202	ISUZU MOTORS LTD	Transportation Equipment	1,579	13.5	13.3	8.6	12.9	5.0
9021	WEST JAPAN RAILWAY CO	Land Transportation	1,545	11.5	100.1	15.3	9.0	-5.0
4528	ONO PHARMACEUTICAL CO LTD	Pharmaceutical	1,286	6.2	22.3	11.3	13.5	-14.8
9201	JAPAN AIRLINES CO LTD	Air Transportation	1,254	6.1	154.5	11.3	12.2	-10.3
5019	IDEMITSU KOSAN CO LTD	Oil & Coal Products	1,238	23.1	-12.7	8.8	8.1	5.2
6504	FUJII ELECTRIC CO LTD	Electric Appliances	1,238	7.3	14.1	16.7	12.4	35.3
7912	DAI NIPPON PRINTING CO LTD	Other Products	1,225	14.2	2.0	16.2	6.8	-0.6
6383	DAIFUKU CO LTD	Machinery	1,225	7.9	-1.0	25.3	13.2	7.3
9009	KEISEI ELECTRIC RAILWAY CO	Land Transportation	1,155	11.6	76.2	24.3	10.4	-2.4
6586	MAKITA CORP	Machinery	1,131	6.2	140.0	21.4	6.3	-12.2
1802	OBAYASHI CORP	Construction	1,029	18.2	-18.3	14.9	6.7	2.8
4185	JSR CORP	Chemicals	830	212.7	-43.2	29.3	7.8	-8.9
9001	TOBU RAILWAY CO LTD	Land Transportation	821	13.0	4.7	18.5	8.1	-9.6
6841	YOKOGAWA ELECTRIC CORP	Electric Appliances	785	18.3	44.4	18.2	10.1	6.8
9024	SEIBU HOLDINGS INC	Land Transportation	690	16.4	76.8	23.6	7.2	-0.7
5332	TOTO LTD	Glass & Ceramics Products	661	5.7	-4.6	17.5	7.8	-11.0
6845	AZBIL CORP	Electric Appliances	658	10.6	14.7	25.2	12.0	-9.1
6526	SOCIONEXT INC	Electric Appliances	655	5.7	40.8	25.5	21.3	46.3
2002	NISSHIN SEIFUN GROUP INC	Foods	635	9.0	54.3	18.1	7.9	0.6
4403	NOF CORP	Chemicals	574	11.3	1.3	16.4	13.2	-9.0
4613	KANSAI PAINT CO LTD	Chemicals	559	8.6	38.5	15.4	11.3	-13.8
8136	SANRIO CO LTD	Wholesale Trade	559	8.8	78.9	29.6	24.0	14.8
5444	YAMATO KOGYO CO LTD	Iron & Steel	550	10.6	-5.2	9.9	10.0	3.6
1944	KINDEN CORP	Construction	539	11.4	7.3	16.3	6.5	-0.2
9008	KEIO CORP	Land Transportation	538	9.2	103.0	16.8	8.3	-16.2
9142	KYUSHU RAILWAY COMPANY	Land Transportation	534	5.5	41.1	12.4	9.7	-3.8
5947	RINNAI CORP	Metal Products	518	7.6	-7.5	18.8	7.4	-3.4
4182	MITSUBISHI GAS CHEMICAL CO	Chemicals	503	6.5	-29.8	10.6	8.1	4.9
7731	NIKON CORP	Precision Instruments	502	16.4	-30.7	15.2	5.0	-1.3
4005	SUMITOMO CHEMICAL CO LTD	Chemicals	502	20.3	-94,962.8	11.4	3.6	-22.7
2784	ALFRESA HOLDINGS CORP	Wholesale Trade	485	10.1	8.1	19.1	6.3	-15.5
6473	JTEKT CORP	Machinery	479	15.8	42.8	9.1	7.2	2.8
2433	HAKUHODO DY HOLDINGS INC	Services	466	21.9	-39.0	19.8	6.5	16.1
5803	FUJIKURA LTD	Nonferrous Metals	461	11.1	-13.6	10.4	14.4	46.9
4676	FUJI MEDIA HOLDINGS INC	Information & Communication	452	5.9	-2.8	15.3	3.5	14.3
9048	NAGOYA RAILROAD CO LTD	Land Transportation	438	16.3	17.6	17.9		-14.4
2229	CALBEE INC	Foods	418	7.7	23.6	22.2	9.9	-1.3
1721	COMSYS HOLDINGS CORP	Construction	415	11.0	27.4	15.4	7.4	-6.2
9045	KEIHAN HOLDINGS CO LTD	Land Transportation	406	6.5	57.7	16.7	8.0	-16.9

Source: BofA Global Research, QUICK

Note: Universe consists of TOPIX stocks with mkt cap above 400 bn JPY, 3Q earnings (OP or NP if OP is not available) above consensus at least 5%; listed in descending order of mkt cap. Based on QUICK consensus. This is a screen and not a recommended list either individually or as a group of stocks and options. Investors should consider the fundamentals of the companies and their own individual circumstances / objectives before making any investment decisions.

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Neutral	≥ 0%	≤ 30%
Underperform	N/A	≥ 20%

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