NOMURA

Connecting Markets East & West

NOMURA ASSET MANAGEMENT

Summer 2024

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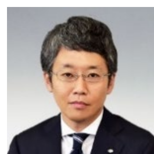

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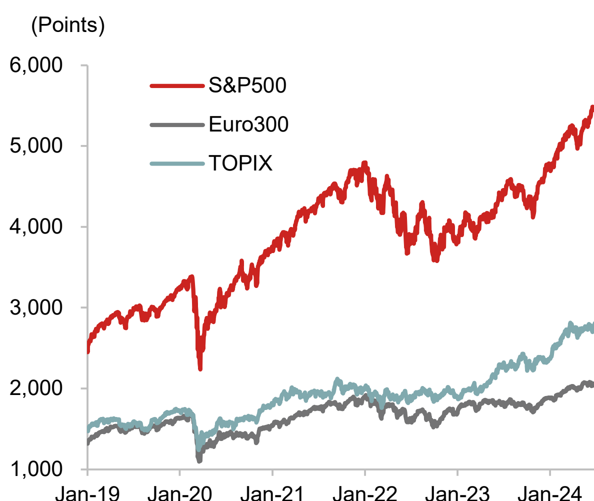
Note: In Nomura Asset Management (NAM) Investment Outlook Summer 2024, NAM's senior investment professionals offer their views of the investment strategy and market prospects – commentaries are as of middle to late June 2024, and reflect each professional's personal views, and do not entirely match NAM's house view. except for Investment Environment Outlook and Global Financial Market Forecast that are based on NAM's house view.

Quarterly Financial Market Recap

Speculation around US monetary policy was a major factor driving fluctuations in the financial markets during the April to June 2024 period. While US bond yields started to rise, they fell again later after indicators suggested that inflationary pressure might be easing, while Federal Reserve Chair Jerome Powell voiced caution regarding the stance towards additional rate hikes. Earnings growth of AI-related companies and expectations of lower interest rates helped to drive equity price higher. In the foreign exchange market, the euro/US dollar exchange rate remained range-bound, while the yen weakened against the US dollar. Market interventions by the Ministry of Finance and the Bank of Japan caused periods of substantial volatility.

Major Equity Markets

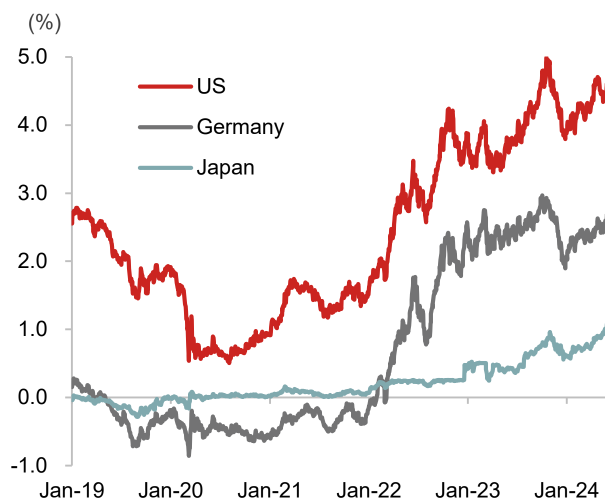
(January 2, 2019 - June 28, 2024, daily)



Source: Nomura Asset Management based on Bloomberg data

10 Year Bond Yields in Major Countries

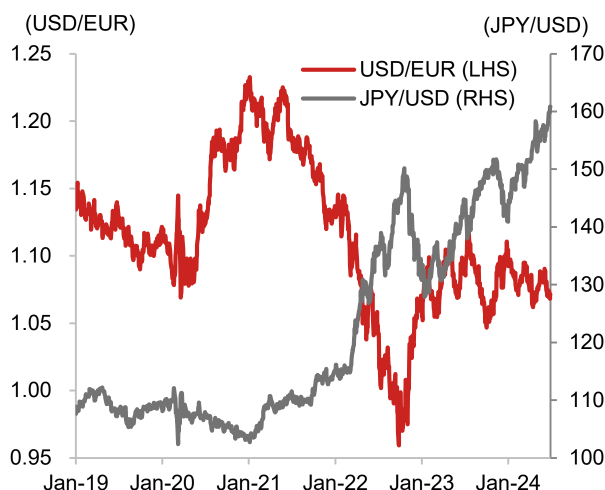
(January 2, 2019 - June 28, 2024, daily)



Source: Nomura Asset Management based on Bloomberg data

Yen and Euro against the US dollar

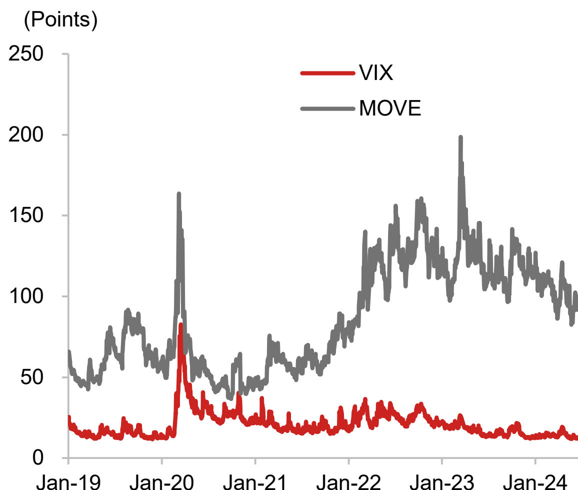
(January 2, 2019 - June 28, 2024, daily)



Source: Nomura Asset Management based on Bloomberg data

Trends in VIX and MOVE

(January 2, 2019 - June 28, 2024, daily)



Note: The VIX and the MOVE are indexes that show the risk of future volatilities of US stocks and US bonds, respectively.
Source: Nomura Asset Management based on Bloomberg data

Investment Environment Outlook

The prospect of interest rate cuts and the US presidential election could trigger a period of financial market volatility.

Rumi Kurumizawa
Chief Economist

Yuichi Murao
Chief Investment Officer,
Senior Corporate
Management Director

Investment environment for 2nd half of 2024: Focus shifts from monetary policy to US presidential election.

In the first half of 2024, shifting expectations surrounding US monetary policy had a significant impact on financial market volatility. Economic indicators such as employment data and the consumer price index, which are used to determine rate cuts, were closely watched. Market participants tended to react with elation or concern depending on the outcome of these economic indicators. While investors are still focused on the Federal Reserve's (Fed's) monetary policy stance, the second half will see greater focus on the November US presidential and congressional elections, as these could bring significant changes in the economic and market outlook for 2025. In this autumn, financial market volatility could increase depending on the interest rate path taken by the Fed as well as election outcomes.

Figure 1. Key Political Schedule for the 2nd Half of 2024:

	US	Europe	Japan	China
Jul.		4: UK general election 7: French legislative		Third plenary session
Aug.				
Sep.	10: Presidential Debates 25: Vice Presidential Debates		30: expiration of the term of LDP president LDP executive reshuffle	
Oct.				
Nov.	5: Presidential election			
Dec.			Budget and Tax Policy Outline for FY 2025 approved by the	Central Economic Work Council

Source: Nomura Asset Management based various media sources

Macroeconomic Outlook: US economy is expected to return to its potential growth rate.

Currently, there are no visible signs that the US economy will enter a recession in the near future. In Europe, the Eurozone economy has been showing signs of recovery in 2024 after experiencing slight negative growth in the second half of 2023.

Although the effects of past rate hikes may have been smaller than expected, the US growth is expected to fall below the economy's potential growth rate through the autumn, contributing to expectations of slowing inflation rates. However, there is still skepticism about whether inflation rates will steadily decline towards the central bank's target in the coming months, such that rate cuts must be given careful consideration.

Taking into account consistency with past communications, downside risks to the economic outlook, and concerns for the adverse effects of rate hikes on low-income groups, we currently forecast that the Fed could decide to cut rates in December.

However, given the view that the economy and price pressures at the moment do not warrant a significant rate cut, our expectations for the pace of monetary easing are more gradual than what is currently priced into the market. As such, we do not anticipate a significant boost to economic growth from interest rate reductions, and we forecast the US economy to grow at a pace close to its potential growth rate in 2025.

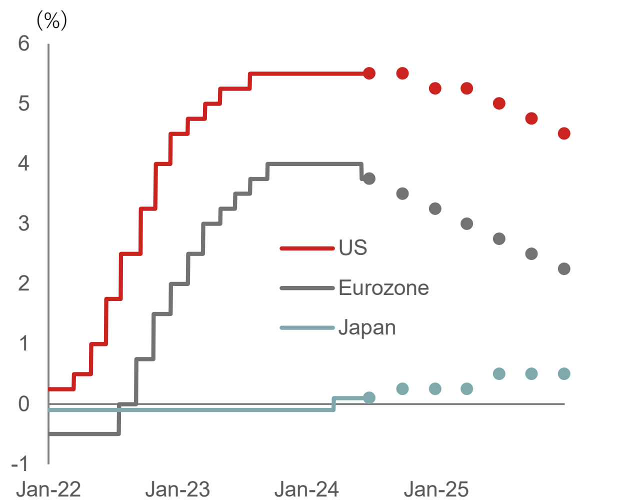
On the other hand, for Japan, we expect growth to continue slightly surpassing the potential growth rate, even with a minor interest rate hike, as the effects of the spring wage increase spread to actual wages and due to the impact of flat-amount tax reduction.

Monetary Policy Outlook: The Bank of Japan is expected to shift towards very gradual rate hikes alongside a rate cut cycle in Europe and the United States.

For the outlook period to the end of 2025, we expect central banks in Europe and the US to continue adjusting the degree of monetary tightening amid subdued inflation. We anticipate a gradual pace of rate cuts after the central banks have confirmed their likely impact on the economy and prices. We forecast the Fed Funds rate to be around 4.5% by the end of 2025.

In Japan on the other hand, with structural labor shortages and the government's support for price pass-through, conditions are becoming more conducive for a solid wage increase during spring wage negotiations in 2025. We expect policy interest rates to be raised to around 0.5% by the spring of 2025.

Figure 2. Policy Interest Rates in Japan, the US, and Eurozone, and NAM Forecasts
(Actual values from Jan. 3, 2022, to Jun. 21, 2024, daily)



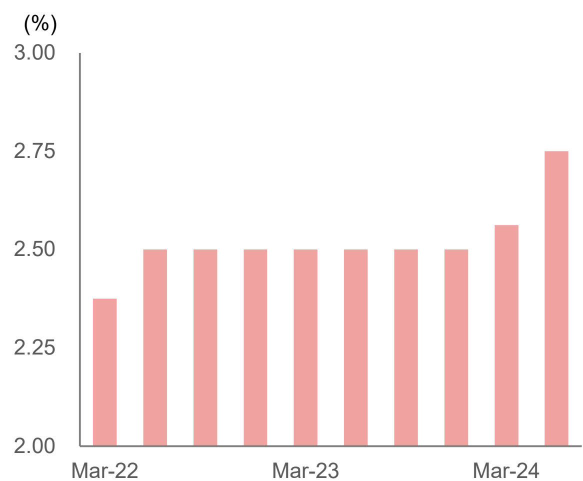
Note: The dots after June 2024 represent our forecasts as of the end of each quarter.
Source: Nomura Asset Management based on Bloomberg data.

Interest Rate Outlook: Market anticipates it will be difficult to incorporate terminal rate forecasts.

Against a backdrop of subdued inflation and rate cuts, long-term interest rates in Europe and the US are expected to decline. However, with a persistent view that the neutral rate of interest is on the rise, market participants may find it challenging to determine with any certainty how far interest rates might be lowered in the current rate-cutting phase. Looking ahead, until the end of 2025, while we expect a downward trend in US 10-year bond yields, we also believe that a significant fall in interest rates is unlikely.

On the other hand, for long-term interest rates in Japan, additional rate hikes and reduced government bonds holdings by the Bank of Japan could lead to rising long term interest rates. However, global interest rate trends are expected to limit the upward pressure or could even exert downward pressure on rates in Japan, resulting in benchmark bond yields fluctuating around 1%.

Figure 3. Long-run Fed Funds Rate Outlook by FOMC Participants (Median)
(Mar. 2022 to Jun. 2024, quarterly)



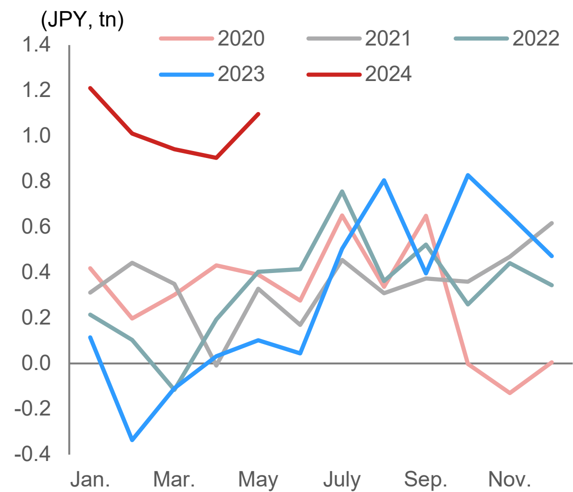
Source: Nomura Asset Management based on the FRB data.

Currency Outlook: A gradual weakening of the US dollar.

Due to the slowdown in US economic growth and the shift towards interest rate cuts, we expect the US dollar to depreciate, with the euro likely to appreciate in such a scenario. Against the backdrop of a slight narrowing of the interest rate differential between Japan and the US, we can also expect the yen to appreciate against the US dollar.

However, as Japan's trade deficit is becoming more entrenched, and with the introduction of the new NISA (Nippon Individual Savings Account) leading to increased investment in overseas assets of Japan's household investors, there is likely to be continued downward pressure on the yen from a flow of funds perspective. Taking these factors into account, we do not foresee a significant reversal towards yen appreciation and US dollar depreciation, even considering the diverging direction of monetary policies between Japan and the US.

Figure 4. Investment in foreign securities by the investment trust management company (Stocks and investment funds holdings) (Jan. 2020 to May 2024, monthly)



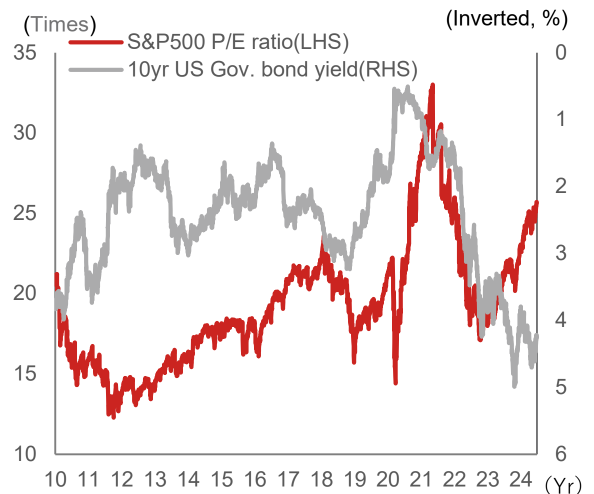
Source: Nomura Asset Management based on Ministry of Finance data.

Equity Market Outlook: An upward trend with some fluctuations.

In both Europe and the United States, against a backdrop of solid economic growth and falling inflation, accompanied by modest rate cuts and a downward trend in long-term interest rates, this would have a positive impact on earnings per share (EPS) and price-earnings ratios (PER) for stock prices.

While there may be periods of asset price instability due to uncertainty surrounding monetary policies and events related to the US presidential and congressional elections, we expect the upward trend in equity prices to continue. However, particularly for US stocks, given that AI-related stocks are leading to an increase in the market PER, we caution that any negative news could potentially trigger a temporary adjustment in stock prices.

Figure 5. PER and Long Term Interest Rates in the US (Jan. 1, 2010 to Jun. 21. 2024, daily)

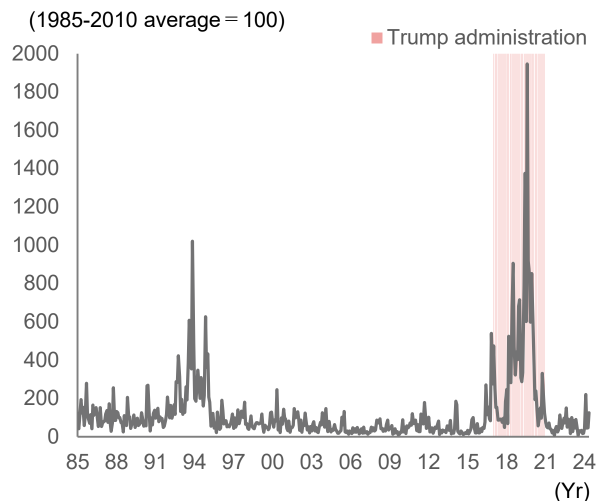


Source: Nomura Asset Management based on the Bloomberg data.

Risk Scenario: Unclear path of rate cuts by the Fed.

Financial markets are currently pricing in the assumption that the next move by the Fed will be a rate cut. In our basic scenario, we assume no significant changes in fiscal, tax, or trade policies in 2025, following the results of the US presidential and congressional elections. However, depending on the election outcome, there could be expectations of a more inflationary fiscal policy being adopted by the new administration starting in January 2025. If the Fed perceives this as an inflationary concern, it is possible that rate cuts might be significantly postponed from the current expectations. If the view shifts towards the belief that rate cuts will be challenging in 2025, there is potential for the financial markets to react differently.

Figure 6. US Trade Policy Uncertainty Index (Jan. 1985 to May 2024, monthly)

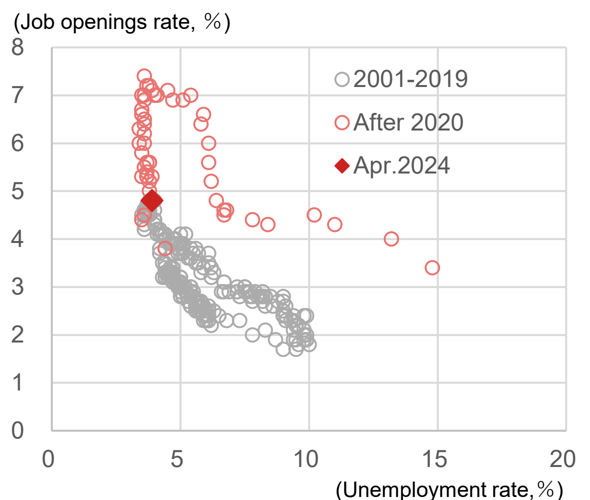


Source: Nomura Asset Management based on Policy Uncertainty.com data.

Risk Scenario: A significant economic slowdown beyond the basic scenario.

There is a consensus view that the US will avoid a recession, and that Europe will not return to a negative growth rate. For the US in particular, the focus has been on the risk of an upside surprise rather than an economic downturn. However, we believe there remains some downside risk of a rapid series of interest rate cuts beyond the general consensus. In the most recent Job Openings and Labor Turnover Survey (JOLTS), the job openings rate is approaching pre-COVID levels. If the relationship between the unemployment rate and the job openings rate reverts to pre-COVID levels, there is some possibility that a slight deterioration in labor demand from this point could lead to an upside shock to the unemployment rate.

Figure 7. US Beveridge Curve (Jan. 2001 to Apr. 2024, monthly)



Source: Nomura Asset Management based on the CEIC data.

Japan Equity Market Outlook

What will it take for the market to break out its range?

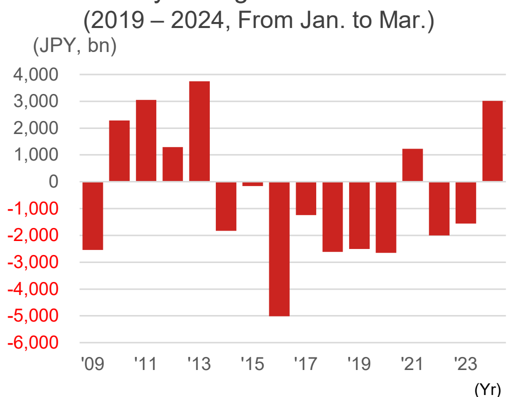
Shintaro Harada
Chief Investment Officer
Active Japan Equity

The Japanese equity market kicked off 2024 with a strong start

Japan's stock market saw rapid and significant gains from the start of 2024, exceeding expectations set by the range-bound trading at the end of 2023. There are several reasons for this, including a sense of undervaluation compared to other advanced economies' stock markets, governance improvements due to Tokyo Stock Exchange reforms, increased evaluation of shareholder returns, diversification away from the economic uncertainty in China, and tailwinds from the rise of U.S. companies like NVIDIA in the AI chip sector. Leading sectors included automotive, trading companies, financial institutions, large value stocks, and semiconductor stocks.

The strength of foreign investor demand for Japanese stocks also stood out. Looking at trading trends by investor domicile, net buying from January to March this year amounted to about 3 trillion yen, ranking third in terms of the value of net purchases among 16 examples of the January to March period since the Global Financial Crisis. Along with the post-crisis rebound and the peak in foreign purchases during the Abenomics era, this marks a significant level of buying not seen in years, indicating a high level of interest.

Figure 1. Net Transaction Volume Trends by Foreign Investors
(2019 – 2024, From Jan. to Mar.)



Source: Nomura Asset Management based on Tokyo Stock Exchange data

Slow start to earnings forecasts for the fiscal year 2024

On the other hand, the market has been relatively flat since April. The TOPIX gained approximately 17% in 1Q2024, significantly outpacing the rate of fundamental growth (i.e. profit growth). Therefore, the announcement season for annual financial results from April to May was closely watched to assess the earnings performance, but the fiscal year 2024 results fell short of expectations, leading to a cautious shift in market sentiment and heavy pressure on stock prices. Many companies have based their current fiscal year forecasts on a conservative assumption that the yen would appreciate by 10% or more from April's exchange rate of JPY 140-145/US dollar. It is therefore likely that forecasts will be revised upward as time goes by. On the other hand, some believe that the consensus already factors in mid single-digit profit growth.

Figure 2. Earnings Forecast

(%)

As of May 2024	FY23 (Actual)	FY24 (Forecast)	FY25 (Forecast)
Russell/Nomura Large Cap	15.0	6.3	8.7
Manuracturing	12.3	8.2	9.7
Basic Materials	-14.6	18.0	13.0
Processing	26.8	3.8	7.9
Nonmanufacutring (ex financials)	8.9	-0.1	6.0
Basic materials	-14.6	18.0	13.0
Machinery, autos	45.9	0.6	3.5
Electronics	-0.8	10.4	16.6
Consumption, distribution	-4.2	9.6	6.2
Information	22.2	8.5	12.9
Utilities, infrastructure	17.1	-10.4	6.4
Financials	49.9	14.9	11.3

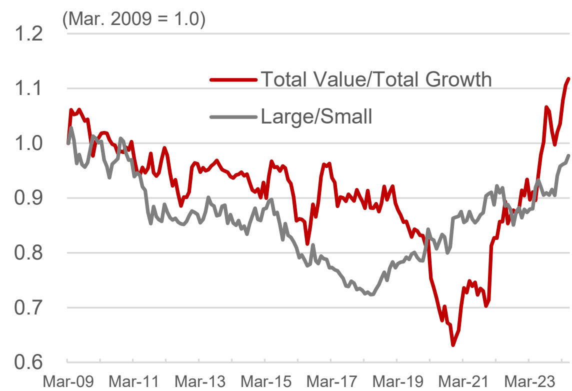
Source: Nomura Asset Management based on Nomura Securities data.

*References to individual stocks do not imply recommendations for buying or selling specific stocks, nor does imply any view on their price movements.

Any signs of change in investment style trends?

As for investment styles, the general view is that there will not be as much divergence as in the previous fiscal year. Growth stocks continued to rise until the first year of the Covid-19 pandemic, but suffered a sharp reversal in the second year and are currently at levels seen before the Global Financial Crisis. While some suggest that growth stocks have undergone a considerable correction, they still seem to lack catalysts for a reversal in the long-term trend favoring value stocks in Japan's equity market. Moreover, there the may still be some remaining valuation premium on growth stocks may not have been fully erased. There is a possibility that interest might shift towards small-cap stocks following the peak in share prices of large-cap stocks like Toyota, but the yen's current depreciation is not necessarily a positive factor for small-caps, which tend to include many domestic growth stocks. It is unlikely that there will be as much disparity in investment styles as in the previous fiscal year, and this could be a fiscal year where stocks that demonstrate solid earnings are valued. This reaffirms the importance of stock selection as we enter a phase where earnings matter most.

Figure 3. Relative stock prices of the Russell/Nomura Index (Mar 2009 to May 2024, monthly)

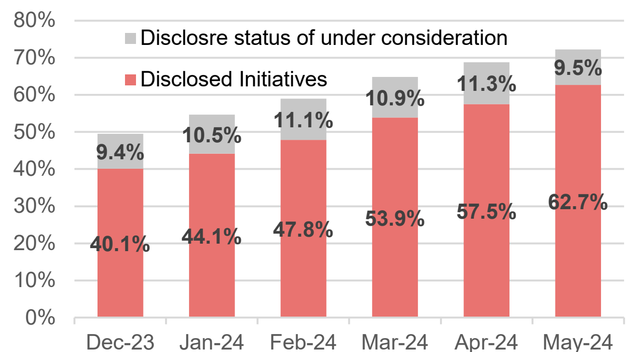


Source: Nomura Asset Management based on Nomura Securities data.

Update on Tokyo Stock Exchange's request on management reform

As of the end of May, the disclosure status regarding the Tokyo Stock Exchange's "Action to Implement Management that is Conscious of Cost of Capital and Stock Price" reached 63% of TSE Prime Market companies, with an increase of approximately 4% each month. If this pace continues, most companies are expected to have responded by the end of the fiscal year. However, there are concerns that major companies like Toyota, SoftBank Group, and Fast Retailing have not yet responded. Meanwhile, the disclosure ratio remains at 20% for companies in the Standard Market, and disclosure and response among companies not classified among the low price-to-book value ratio (PBR) stocks are relatively slow. Personally, I believe that the initiative will reach its ultimate goal when companies like Keyence (with over 2 trillion yen in cash holdings) implement large-scale share buybacks. There is still room for improvement, particularly focusing on owner-operated companies. Following moves to enhance returns among low PBR stocks initiated last year, the current stage shows signs of structural reform among companies with low Return on Equity (ROE), potentially leading towards financial reform efforts among high-ROE companies too.

Figure 4. Disclosure on actions taken and plan for improving capital cost efficiency and stock price (Dec 2023 to May 2024, monthly)



Source: Nomura Asset Management based on the TSE data.

Japanese equity market outlook for the second half of the year.

As shown in the graph below, the Price-to-Earnings Ratio (PER) of the TOPIX has averaged around 14 since the Global Financial Crisis. It increased to around 16 when optimism was factored in, and dropped to around 12 during spells of market pessimism. Currently, the PER is at 16 (shown by the red line), which traditionally could indicate an overvalued market. The stock price increase in the first quarter of this year has exceeded the annual profit growth rate of major companies (15% for fiscal year 2023, 6% for fiscal year 2024 - according to Nomura Securities forecasts), leading to an elevated valuation.

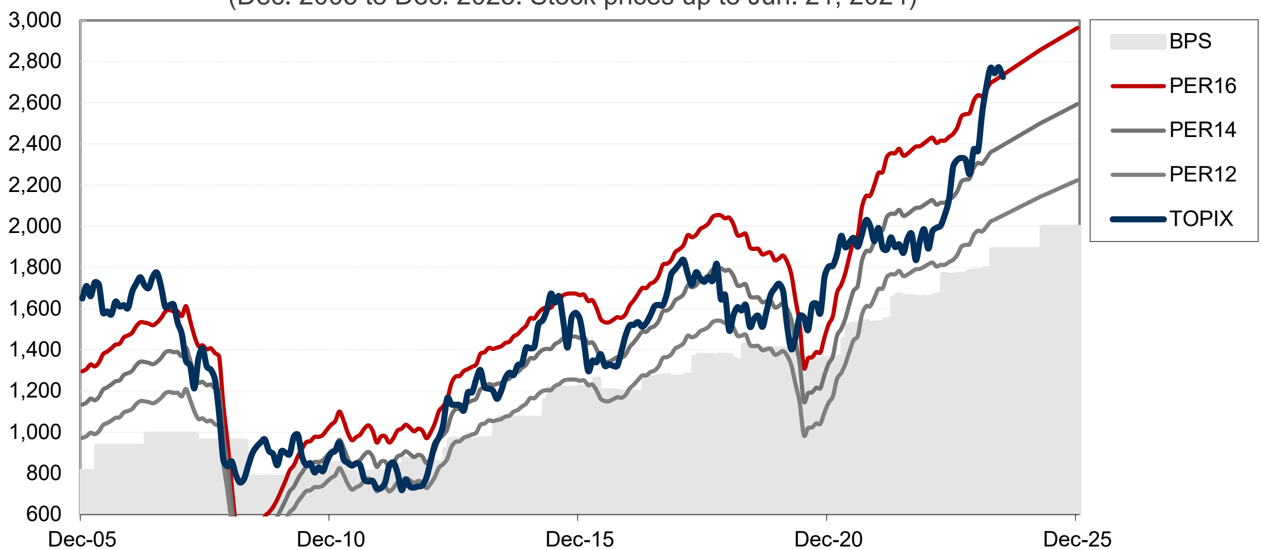
However, it is believed that this rise in valuations could be sustained. The number of companies responding to the reform agenda of the Tokyo Stock Exchange continues to increase, and the exchange's monitoring policy is not only systematic but also aims to encourage actual improvements in corporate management. Therefore, it seems unlikely that these initiatives have been fully factored in at this point.

Considering the resilience of foreign investor demand for Japanese stocks, the presence of entities that are late to buy in, and factors such as wage increases resulting from Japan's spring labor negotiations and the effects of flat-amount tax reduction leading to a firmer inflationary trend in Japan are also likely to generate interest among foreign investors. In the short term, we expect April to June quarter earnings reports to bring few surprises, leading to minimal stock price fluctuations driven by fundamental factors. The automotive sector, for example, is expected to face a slowdown in earnings momentum due to last year's production recovery peak as well as issues related to testing compliance scandals.

While a weaker yen could benefit export-oriented companies, concerns about a slowdown in domestic demand may offset these positive effects, with the yen no longer serving as a significant market catalyst.

Therefore, as we navigate through first quarter earnings reports and the summer lull, the current market view suggests that stock prices should trend towards the rate of profit growth, in line with the red line in the graph below, during the the latter half of this year.

Figure 5. TOPIX PER bands and BPS trends
(Dec. 2005 to Dec. 2025. Stock prices up to Jun. 21, 2024)



Note: PER and BPS forecasts are based on our company's estimates. To make the graph easier to read, we have hidden a portion from 2008 to 2010. Source: Nomura Asset Management based on Nomura Securities, data.

*This commentary reflects the personal views of the author and does not necessarily represent NAM's house view.

Global Equity Market Outlook

Our Global Multi Theme Equity Strategy (GMT) Investment Team comprises dedicated thematic investment specialists who focus on rigorous stock selection to exploit growth themes. The GMT focuses on attractive growth opportunities arising from the Fourth Industrial Revolution.

Takahiro Nakayama,
Senior Managing Director,
Chief Investment Officer,
Active Global Investments

Yoshiaki Saito
Chief Portfolio Manager

Three perspectives on Global Multi Theme investment

Nomura Asset Management's Global Multi Theme Strategy (GMT) Investment Team focuses on themes that are expected to demonstrate attractive growth opportunities over the medium to long term. We identify these themes based on three perspectives: "Breakthrough technology/disruptive innovation", "New opportunities in emerging markets", and "Structural change in society". Investment themes selected from these three perspectives are continuously changing, and our analysis enables us to select the most attractive themes at any given time.

Three Perspectives

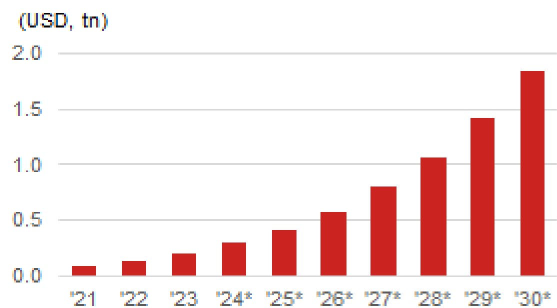
Breakthrough Technology/Disruptive Innovation – Evolution in new technology, products and services

New Opportunities in Emerging Markets – Global trend/expansion of mass-affluent in emerging markets

Structural Change in Society – Aging population, increase in middleclass due to income growth in emerging countries

We also pay close attention to ongoing developments in the Fourth Industrial Revolution, also known as the AI Revolution, which drives and enhances the level of connectivity and integration. Through a succession of newly created technologies, the Fourth Industrial Revolution will be able to drive new connected and integrated developments using the existing global internet infrastructure. The scale of the global AI market in sales terms can be considered a leading contributor in the Fourth Industrial Revolution and is rapidly expanding, with an expected reach of 1.8 trillion US dollars by 2030.

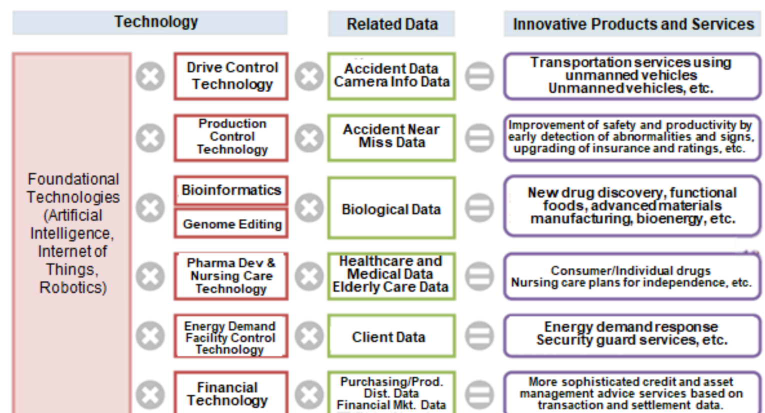
Figure 1. Trends in the Global AI Market
(Period: 2021 – 2030, annually)



Source: Nomura Asset Management based Next Move Strategy Consulting data. Nomura Asset Management forecasts for 2024 and beyond

The view of the GMT Investment Team - 1

In recent years, we have seen rapid growth in the Internet of Things (IoT), where products and services are connected through the internet. Vast amounts of data accumulated through IoT connected devices is being analyzed using AI and utilized for the development of new products and services. Furthermore, we are seeing further convergence and enhancement of technologies used in various fields that are connected via the internet. In other words, as technologies that were previously considered separate begin to converge – such as robotics, 3D printing, nanotechnology, biotechnology, genetic engineering, and blockchain technology – we can expect the Fourth Industrial Revolution to benefit a wide range of industries, not only IT companies.



Source: Nomura Asset Management draft translation of "Vision for New Industrial Structure " (the Ministry of Economy, Trade and Industry) (https://www.meti.go.jp/shingikai/sankoshin/shinsangyo_kozo/pdf/017_05_00.pdf/)

The view of the GMT Investment Team - 2

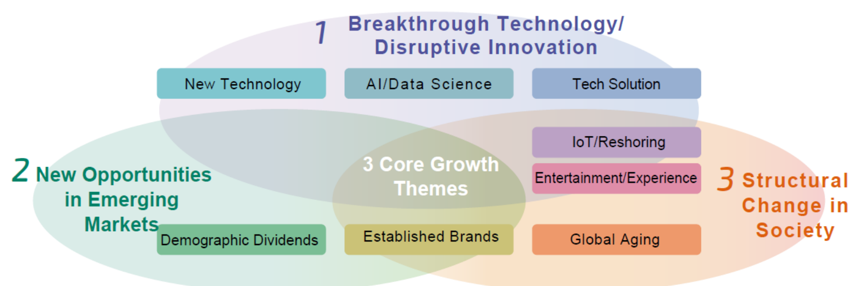
Autonomous driving is one example of a technology that not only contributes to growth in the automotive industry, but also has the potential to bring about broader structural changes in business sectors like the auto insurance industry due to factors such as the reduction in traffic accidents. Meanwhile, three-dimensional measurement data obtained through aerial photography by drones (unmanned aerial vehicles) has the potential to significantly improve the productivity of infrastructure development and the construction industry. Furthermore, in commercial transactions, the development of AI technology can enable accurate management and billing of when, where, and by whom products and services are used. Such developments are considered to be key drivers in the shift from traditional "product" consumption to "experience" consumption, a trend that is currently capturing consumer attention. This has led to the emergence of new business models like Airbnb and Uber.

Moreover, at the core of the Fourth Industrial Revolution are advancements in AI-related technologies and the globally interconnected internet infrastructure. However, operation of these technologies is extremely energy intensive and also consumes a large quantity of water for cooling data processing facilities. This leads us to believe that there may also be significant growth opportunities in the infrastructure sectors needed to support AI development. With the addition of a sustainability perspective that was not considered in previous industrial revolutions, the Fourth Industrial Revolution should also encompass renewable energy technology as a growing sector of interest.

GMT Strategy: Eight themes from three perspectives

The GMT Investment Team's dedicated thematic specialists are assigned to select and investigate attractive investment themes. Unlike industry-specific analyst teams that uncover and investigate stocks related to specific sectors, thematic specialists explore and investigate stocks across a range of industries on the assumption that they can identify and benefit from unique growth stories within each theme without limiting themselves to specific industries. Currently, we have selected eight themes that are expected to show attractive growth over the medium to long term from the three perspectives of "Breakthrough technology / disruptive innovation", "New opportunities in emerging markets", and "Structural change in society".

The core themes are divided into "High Growth Themes" that involve significant changes and offer strong growth potential, such as 1) New Technology, 2) AI/Data Science, 3) Technological Solutions and 4) Entertainment/Experience, as well as "Stable Growth Themes" that offer steady growth potential such as 5) Global Aging and 6) Established Brands. In addition, there are themes that combine characteristics of both, these are 7) IoT/Reshoring and 8) Demographic Dividend, making a total of eight themes.



GMT Strategy: Eight investment themes in detail

1. New Technology: The Fourth Industrial Revolution is still in its early stages, and for many companies, investments are being made based on the expectation of future changes in industrial structure. In this context, we are focusing on groups of companies that are already generating profits and producing semiconductors that are essential for the Fourth Industrial Revolution.

2. AI/Data Science: We are closely monitoring companies that operate essential data centers for the extensive data analysis capacity required by AI. Moreover, given the need for secure handling of crucial information, including confidential and personal information during data processing, we are also focusing on companies related to cybersecurity, an area that has grown significantly in importance.

3. Technological Solutions: We pay attention to the technological solutions through the effective utilization of vast amounts of data collected through IoT for service realization, as well as the combination of new technologies such as Big Data, AI, and robotics, is creating growth opportunities in various fields including finance, retail, and healthcare.

4. Entertainment/Experience: While consumption used to center around ownership and purchasing of goods, Millennials and Generation Z are increasingly placing value on unique experiences. We are focusing on companies that can quickly adapt to this change in consumer values and provide services that accurately capture customer needs.

5. Global Aging: There is a paradigm shift towards "precision medicine," where medical treatments are individualized based on patient-specific information rather than the traditional statistical processing of medical and epidemiological information. We are focusing on areas such as molecular targeted drugs and immunotherapy.

6. Established Brands: Even companies with established brands, such as European luxury brands, must constantly innovate to meet changing consumer preferences. We are focusing on companies that can actively introduce new consumer-oriented services using AI and improve production efficiency.

7. IoT/Reshoring: We focus on companies that utilize AI, based on the vast amount of data accumulated through IoT, not just for automation in production using robots as in the past, but also for improving the efficiency of the entire manufacturing process and developing new products and services, as well as solution providers for this purpose. We also pay attention to the companies that would benefit from the revision of such global production systems.

8. Demographic Dividend: We are focusing on companies that benefit from the rising prosperity and population growth in emerging countries and the various business opportunities arising from different stages of development.

*This commentary reflects the personal views of the author and does not necessarily represent NAM's house view.

Bond and Currency Market Outlook

Bond yields are expected to fall along with monetary easing by the major central banks.

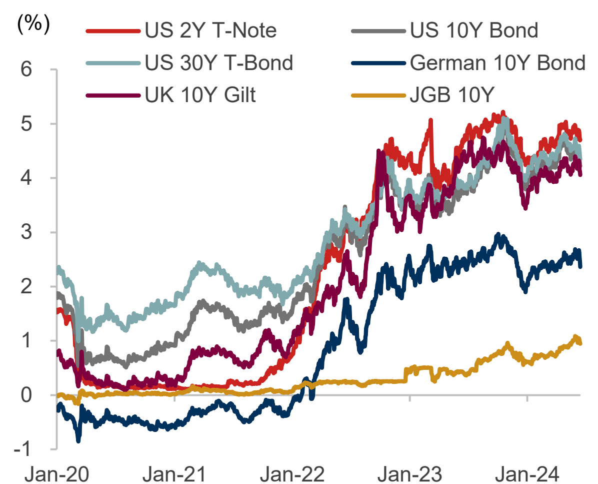
Wataru Kato
Senior Portfolio Manager

Yuji Maeda
Head of Investment
Global Fixed Income

Bond yields have risen amid fears of a pause in inflation's decline

In the first half of 2024, bond yields of the major economies exhibited a gradual upward trend. Bond yields had declined rapidly since the autumn of 2023 as markets anticipated a shift in monetary policy by the major central banks, but they began to rise again at the start of this year. This was driven by a series of economic indicators from the US that exceeded market expectations, leading to the scaling back of market expectations for near term rate cuts by the Federal Reserve and other major central banks. In particular, the US Core Consumer Price Index (CPI) showed a high growth rate of 0.4% (mom) for three consecutive months from January to March, highlighting the difficulty in taming inflation. As a result, both the Fed and financial markets were compelled to make adjustments to their outlook on policy interest rates.

Figure 1. Changes in Government Bond Yields
(Jan. 2, 2020 – Jun. 14 2024, daily)



Note: Yield is Bloomberg Generic
Source: Nomura Asset Management based on Bloomberg data

Fed expected to begin cutting interest rates in the second half of 2024

The Fed decided to maintain its policy interest rate at the June FOMC meeting. The median outlook by committee members suggested a likelihood of one rate cut in 2024 and four rate cuts in 2025. We also anticipate that the impact of the cumulative interest rate hikes to date on economic growth indicators will become increasingly apparent, leading to a slowdown in US growth rates and a lower rate of inflation. Therefore, we expect the Fed to start cutting rates in the second half of the year and to continue with a series of rate cuts thereafter.

In June, the European Central Bank (ECB) decided to cut its policy rate by 0.25 percentage points at its regular board meeting. While ECB President Christine Lagarde hinted at the possibility of further rate cuts, she also signaled a cautious approach in determining the pace of future interest rate moves, citing the high wage growth rate in the first quarter. In the Eurozone, where the pace of economic growth is slower that in the US, we anticipate that inflation will continue to decelerate, and we expect the ECB to implement rate cuts in a pattern similar to the Fed.

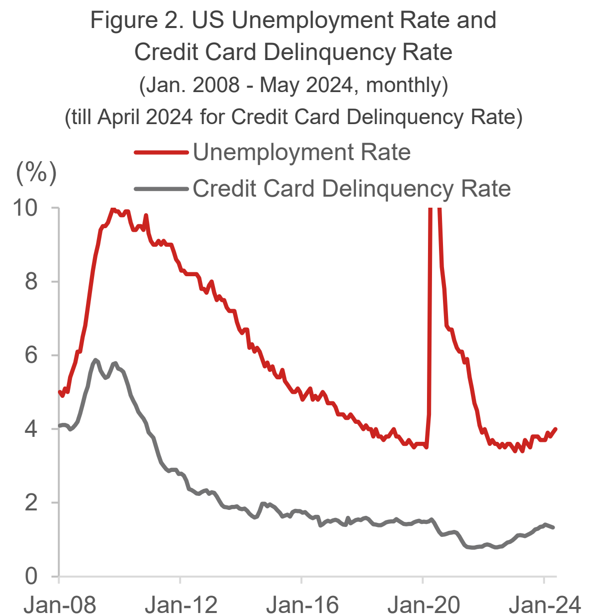
We can also expect many other central banks in advanced countries and regions, including Canada, which started cutting rates in June, to continue cutting interest rates at a similar pace.

One obvious outlier to this monetary easing trend is the Bank of Japan (BOJ), which is expected to be one of the few central banks seeking to raise interest rates over the coming months. Having carried out one policy rate hike this year, its first in 17 years, and lifting its negative interest rate policy at the March monetary policy meeting, the BOJ is expected to implement additional incremental rate hikes in the second half of this year.

US economy is expected to slowdown

Economic conditions in the US have been generally robust, with little noticeable impact so far from the Fed's monetary tightening measures. However, upon closer observation, indicators such as rising credit card delinquency rates among lower-income groups suggest that the rising interest burden may be about to exert downward pressure on personal consumption in the future. While the unemployment rate remains low, there is a slight upward trend, reaching around 4% in May, its highest level for about two and a half years. We now forecast that further declines in personal consumption and worsening conditions in the labor market will lead to a slowdown in the US economy in the second half of the year.

Figure 2. US Unemployment Rate and Credit Card Delinquency Rate
(Jan. 2008 - May 2024, monthly)
(till April 2024 for Credit Card Delinquency Rate)



Note: To make the graph more readable, some parts of the unemployment rate data for the year 2020 have been hidden. Source: Nomura Asset Management based on Bloomberg data.

With the Fed's shift towards interest rate cuts, bond yields are expected to fall

Current US Treasury bond yields appear to have factored in the rate cuts projected at the June FOMC meeting for the rest of the year, with a median projection of 25 basis points by the end of 2024. However, we still believe there is room for bond yields to decrease further.

The outlook from the June FOMC suggests that while Gross Domestic Product (GDP) will continue to grow at a solid pace of about 2% annually, the inflation rate will gradually converge towards the Fed's target in an optimistic scenario. Nevertheless, given that the adverse impact of the cumulative interest rate hikes to date are now manifesting in parts of the US economy, we believe these effects will become more widespread and lead to an economic slowdown.

Although signs began to emerge in June, once the market takes on more evidence of an economic slowdown amid declining economic indicators, bond yields are likely to decrease even before the Fed takes action to loosen policy.

In a less benign scenario, potential triggers such as an outbreak of financial system instability, similar to the events of spring of 2023, could set off a significant fall in asset prices, including risky assets like stocks. In such a scenario, there could even be a negative impact on the the consumption behavior of high-income households, which has been strong so far due to the asset effect. If a rapid economic downturn occurs, the market may press the Fed for significant interest rate cuts, causing bond yields to decline further.

US dollar depreciation trend expected

The Fed's shift towards interest rate cuts is expected to lead to depreciation of the US dollar. US monetary policy is among the most important factors that influence the currency market. From the middle of 2021 to the second half of 2022, the US dollar strengthened, primarily in anticipation US interest rate hikes that began in March 2022. With the Fed now moving towards policy rate cuts, there are expectations that this trend could reverse, leading to a new trend towards a weaker US dollar. In addition, considering the external balance as a factor influencing longer-term exchange rate movements, the significant current account deficit in the US is likely to exert downward pressure on the US dollar.

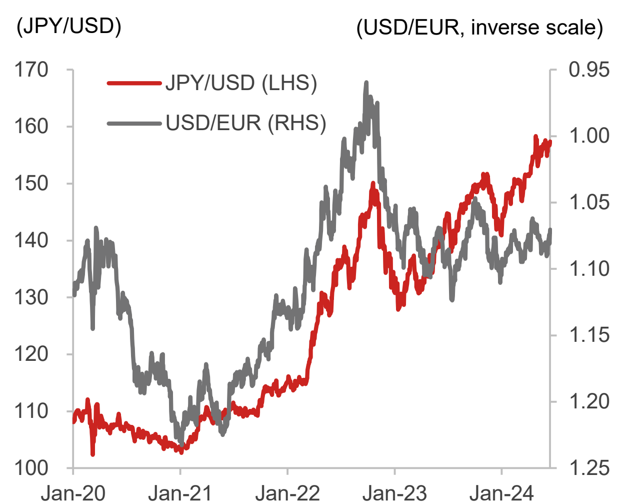
One risk associated with this scenario is the potential divergence in monetary policies if other central banks cut policy rates more significantly than the Fed, leading to wider market awareness of the policy divergence. For example, if the ECB, which cut rates at its June regular meeting, adopts an exceptionally accommodative stance compared to the Fed, it could lead to a scenario of a weaker euro alongside a stronger US dollar. However, given that a weaker euro could fuel inflationary pressure in the Eurozone through increased import prices, and considering that the ECB might not have absolute confidence in completely taming inflation, there may be limitations to the extent of policy divergence.

With rates moving in opposite directions, will BOJ policy cause a yen rebound?

While major central banks elsewhere are moving towards rate cuts, the BOJ is expected to continue exploring monetary normalization and rate hikes. The BOJ's persistent and extensive monetary easing measures have resulted in significant widening of interest rate differentials between Japan and other large economies, with the value of the yen sinking as other central banks raised interest rates. Looking ahead, rapid narrowing of these interest rate differentials could trigger a significant rebound in the Japanese yen.

However, such a reversal is not guaranteed. Due to deteriorating trade balances and sluggish productivity, Japan is structurally less prone that it has been in the past to experiencing significant currency appreciation. Even if interest rate differentials shrink, it is important to be aware that there may be less risk of a substantial strengthening of the yen.

Figure 3. JPY/USD and USD/EUR Trends
(Jan. 2, 2020 – Jun. 14, 2024, daily)



Source Nomura Asset Management based on Bloomberg data.

* This material contains personal views and does not necessarily reflect Nomura Asset Management house view.

J-REIT Market Outlook

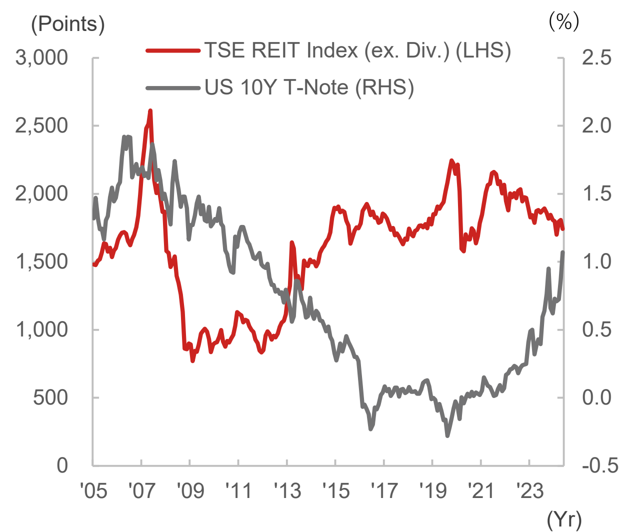
Tomoyuki Nobuhara
Senior Portfolio Manager

The market environment has entered a phase that requires investment strategies that respond to inflation

Domestic long-term interest rates are moving in an upward trend

The Bank of Japan implemented a financial policy change in March of this year, which included the reversal of the negative interest rate policy. Furthermore, as additional monetary policy changes such as reducing the amount of government bond purchases and additional interest rate hikes were considered, domestic long-term interest rates have been on an upward trend. The rise in interest rates could lead to a decrease in the attractiveness of REIT dividend yields compared to government bond yields and an increase in borrowing costs, making it a cause for concern in the short term. However, if the interest rate rise is accompanied by healthy inflation, there is a high possibility of realizing an increase in rents for REIT properties, so there may not be a need to excessively worry about it in the medium term.

Figure 1. TSE REIT Index and US 10Y T-Note Yield
（Jan. 2005 – May 2024, monthly）

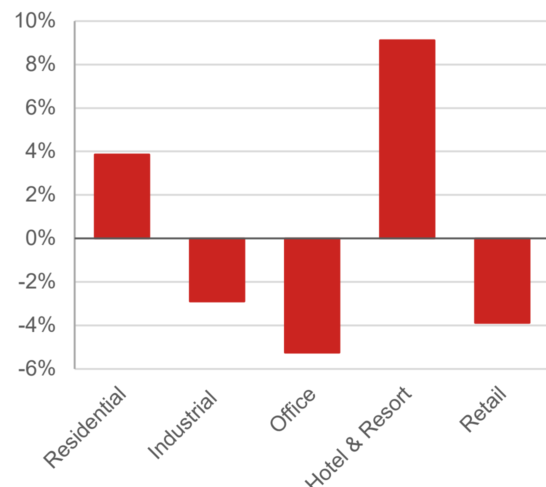


Source: Nomura Asset Management based on QUICK data

Strong performance of sectors with expected rent increases

In an environment where inflation trends are firm and interest rates are rising, it is expected that easing cost increases by raising rents on owned properties will be effective. On the contrary, sectors and shares where rent increases are not expected may find it challenging to maintain profits and may be less valued in the market. Upon reviewing the sectoral returns since the beginning of 2024, the Hotel and Resort sectors and the Residential sector have been performing well. The Hotel and Resort sector has shown improvements in occupancy rates and room rates, leading to an increase in rents received by REITs. The Residential sector has also seen rents rise due to environmental improvements. While the return of the Office sector remains negative, the market itself is showing signs of recovery.

Figure 2. J-REIT Sector Return
(2024 YTD, Dec. 29, 2023 – May 31, 2024)

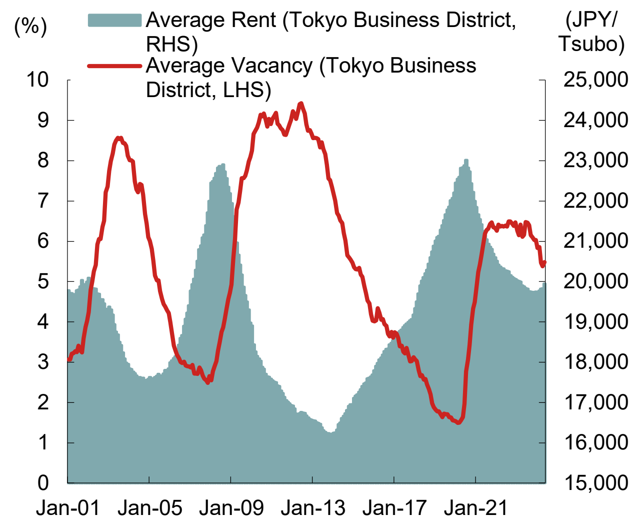


Note: Market capitalization weighted average, industry classification by GICS industry subsector classification.
Source: Nomura Asset Management based on Bloomberg data

Office market conditions are expected to recover.

In 2023, the office vacancy rate remained high in the mid-6% range due to the large supply of new office buildings. However, as companies consider new office leases from the perspectives of increasing in-person work rates and securing talent, the demand for office space is increasing. Since the beginning of 2024, the office vacancy rate has decreased to the mid-5% range, and rents have started to rise from their lows. With a decrease in the expected supply of new office buildings in 2024, a continued recovery in demand should lead to a decrease in vacancy rates. Owners of office buildings are also starting to negotiate rent increases with a more bullish stance compared to before.

Figure 3. Tokyo Business District Office Market
(Jan. 2001 to May 2024, monthly)

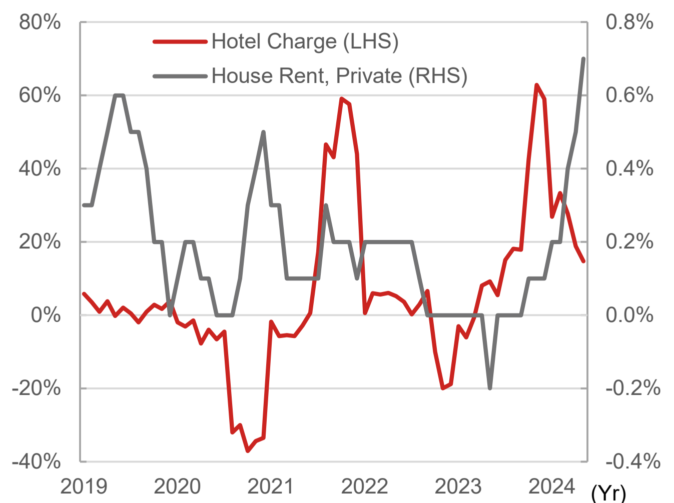


Source: Nomura Asset Management based on data from Sanki Shoji

Hotel and rental housing rents are increasing.

The hotel sector has not only recovered to pre-pandemic levels in domestic demand but has also seen a surge in inbound demand supported by the depreciation of the yen. As a result, accommodation prices have significantly increased. In the Residential sector, rents have been on the rise due to the revival of population inflows to urban areas and an increase in tenants choosing rental housing as a result of soaring prices of condominiums. In these sectors, cost increases due to inflation and rising interest rates are being mitigated by increasing cash flow from owned properties. In the future, investment strategies that respond to inflation will be required in the entire REIT market, and while some sectors have already implemented such strategies, there are expectations for the spread to other sectors.

Figure 4. Consumer Price Index
(Tokyo metropolitan area/ by item)
(Jan. 2019 - May 2024, monthly yoy)



Source: Nomura Asset Management based on based on data from the Statistics Bureau of the Ministry of Internal Affairs and Communications (https://www.e-stat.go.jp/).

Global Financial Market Forecast

			2024 Q1	Q2 F	Q3 F	Q4 F	2025 Q1 F	Q2 F	2022	2023	2024 F	2025 F
Real GDP	World	*1,*4	2.8	2.8	2.5	2.5	2.4	2.5	2.9	2.9	2.6	2.5
(qoq, ann, %)	Developed	*2	1.1	2.0	1.5	1.6	1.7	1.7	2.6	1.7	1.6	1.7
	Emerging	*1,*3	4.8	4.4	4.0	3.9	3.7	3.8	3.4	4.6	4.3	3.7
	United States		1.3	2.6	2.0	2.0	1.9	1.8	1.9	2.5	2.5	1.9
	Eurozone		1.3	1.3	0.8	0.9	1.2	1.3	3.5	0.6	0.7	1.1
	Japan		-1.8	1.5	2.8	1.0	1.2	1.0	1.0	1.9	0.1	1.3
	China	*1	5.3	5.2	4.8	4.4	4.1	4.1	3.0	5.2	4.9	4.1
CPI	World	*4	3.4	3.6	3.5	3.5	3.1	2.9	7.0	4.4	3.5	2.8
(yoy, %)	Developed	*2	3.0	3.0	3.0	2.9	2.7	2.4	7.5	4.7	3.0	2.3
	Emerging	*3	4.0	4.5	4.4	4.3	3.9	3.7	6.2	3.9	4.3	3.5
	United States		3.2	3.4	3.4	3.1	2.7	2.5	8.0	4.1	3.3	2.5
	Eurozone		2.6	2.5	2.4	2.6	2.4	2.2	8.4	5.4	2.5	2.1
	Japan	*5	2.5	2.3	2.1	2.2	2.8	2.6	2.3	3.1	2.3	2.4
	China		0.0	0.5	1.0	1.6	1.4	1.7	2.0	0.2	0.8	1.2
Policy Interest Rate	United States	*6	5.50	5.50	5.50	5.25	5.25	5.00	4.50	5.50	5.25	4.50
(%)	Eurozone	*6	4.00	3.75	3.50	3.25	3.00	2.75	2.00	4.00	3.25	2.25
	Japan	*6	-0.10	0.10	0.25	0.25	0.25	0.50	-0.10	-0.10	0.25	0.50
	China	*6	3.45	3.45	3.45	3.45	3.45	3.45	3.65	3.45	3.45	3.45
10-Year GB Yield	United States		4.20	4.40	4.40	4.30	4.10	4.00	3.87	3.88	4.30	3.90
(End of Period, %)	Germany		2.30	2.50	2.50	2.40	2.20	2.10	2.57	2.02	2.40	2.00
	Japan		0.73	1.06	1.10	1.10	1.10	1.20	0.42	0.61	1.10	1.20
Equity Index	S&P500		5,254	5,460	5,610	5,740	5,920	6,090	3,840	4,770	5,740	6,450
(End of Period, Point)	EURO300		2,031	2,032	2,070	2,100	2,140	2,180	1,678	1,889	2,100	2,260
	TOPIX		2,769	2,810	2,790	2,820	2,870	2,880	1,892	2,366	2,820	3,060
	MSCI EM ($)		1,043	1,086	1,110	1,120	1,140	1,160	956	1,024	1,120	1,200
Currency	USD/EUR		1.08	1.07	1.09	1.10	1.11	1.12	1.07	1.10	1.10	1.13
(End of Period)	JPY/USD		151.3	160.9	156.0	154.0	152.0	148.0	131.9	141.0	154.0	146.0
	JPY/EUR		163.5	172.4	170.0	169.0	169.0	166.0	140.8	155.7	169.0	165.0
	RMB/USD		7.23	7.27	7.30	7.20	7.20	7.10	6.95	7.09	7.20	7.10

		2022	2023	2024 F	2025 F
Currency	INR	82.7	83.2	84.0	82.0
(Per USD,	IDR	15,568	15,397	15,400	15,600
End of Period)	BRL	5.3	4.9	5.0	5.2
	MXP	19.5	16.9	18.5	18.6
	ZAR	17.0	18.3	18.0	17.5
	TUR	18.7	29.5	40.0	54.0
Policy Interest Rate	India	6.25	6.50	6.25	6.00
(%)	Indonesia	5.50	6.00	6.00	5.00
	Brazil	13.75	11.75	10.25	9.00
	Mexico	10.50	11.25	10.75	8.50
	S. Africa	7.00	8.25	8.00	7.00
	Turkey *6	9.04	42.50	50.00	50.00

Note: Forecast as of June 24, 2024. 1) YoY, 2) GDP weighted average of US, Eurozone, Japan, UK, Canada, Australia, 3) GDP weighted average of China, India, Brazil, Korea, Taiwan, Indonesia, Thailand, Malaysia, the Philippines, Hungary, Poland, Russia, Turkey, Mexico, and South Africa, 4) GDP weighted average of 2) and 3), 5) core consumer price, 6) for Japan the policy interest rate imposed on the current account deposits held by financial institutions at the Bank of Japan, for the US the upper limit of the FF target range, for the Eurozone the central bank deposit interest rate, for China the 1-year loan prime rate, for Turkey, weighted average funding ratio of the central bank, *As for forecast columns, actuals are prioritized if available.
Source: Oxford Economics, Bloomberg, and Nomura Asset Management

Index Hedge Clause

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