Daiwa Securities

Daiwa's View

Post-coronavirus world projected by stock prices

➢ Clear difference by sector and size

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Daiwa Securities Co. Ltd.

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Clear difference by sector and size

It is said that the global economic recovery will probably be moderate, or a checkmark recovery. While this would probably be right when looking at it from a macroeconomic perspective as a whole, I get the feeling something is missing from this picture. How will the global economy change going forward in the aftermath of the COVID-19 pandemic and US-China conflict?

Some time has passed since the emergence of the pandemic and US-China conflict, and, for that reason, the stock market appears to have factored in current foreseeable factors to some extent. Of course, no one can say that stock prices are perfect. However, as stock prices are regarded as the collective intelligence of many people, experts, and related parties, we can say that they have, on average, provided the best forecast at any particular point in time. Under these uncertain circumstances, it would be worthwhile to look at the post-coronavirus picture as reflected (projected) by stock prices.

When we observe the recovery rate of stock prices using two sets of data—(1) the bottom, when all risk assets were dumped due to the coronavirus panic, compared to the beginning of the year before people became aware of the coronavirus crisis, and (2) the current situation (on 14 May JST)—some interesting things come to light.

First, one recognizes a big difference based on sector, rather than based on the moves seen by each nation. Recently, the NASDAQ Index recouped all its losses for the year, which was widely covered by the media. However, the S&P 500 Index, which reflects a broad range of the US economy, is still posting a double-digit YTD decline. While the NASDAQ Index, mainly consisting of high-tech issues, achieved a V-shaped recovery, the S&P 500 Index has only shown a lackluster V-shaped recovery. This symbolizes the future after the pandemic. From now on, earnings in winner sectors are expected to achieve a V-shaped recovery, but this is not the picture for the entire US economy, and differences by sector will likely widen.

NASDAQ Composite Index (pt)		S&P 500 Index (pt)	
1-Jan-20	8,973	1-Jan-20	3,231
Bottom	6,861	Bottom	2,237
14-May-20	8,863	14-May-20	2,820
YTD return	-1.2%	YTD return	-12.7%
Bottom	-23.5%	Bottom	-30.8%
Recovery	22.3%	Recovery	18.0%

Source: Bloomberg; compiled by Daiwa Securities.

Moreover, a comparison by nation shows that US stocks (S&P 500) are outperforming Japanese stocks (TOPIX). However, the difference is not as noticeably large as the aforementioned gap between the NASDAQ Index and the S&P 500 Index. Therefore, in forecasting the post-pandemic world, it is important to focus on sectors rather than nations[1].

TOPIX (pt)			S&P 500 Index (pt)	
1-Jan-20	1,721		1-Jan-20	3,231
Bottom	1,236		Bottom	2,237
14-May-20	1,463		14-May-20	2,820
YTD return	-15.0%		YTD return	-12.7%
Bottom	-28.2%		Bottom	-30.8%
Recovery	13.2%		Recovery	18.0%

Source: Bloomberg; compiled by Daiwa Securities.

Also interesting are the results by size. The S&P 500 Index posted a checkmark recovery, rebounding by around 18% from its bottom during the coronavirus crisis (YTD 30.7% drop). Meanwhile, the recovery of the S&P MidCap 400 Index was only 16.1% from its bottom (YTD 40.9% fall) and that of the S&P SmallCap 600 Index was just 10.3% from its bottom (YTD 41.7 plunge). Looking at YTD returns, as well, the results were -24.8% for mid-caps and -31.4% for small caps, compared to -12.7% for the S&P 500 Index. This indicates that the order in the post-pandemic world can be expressed as large caps > mid-caps > small caps.

S&P 500 Index (pt)			S&P MidCap 400 Index (pt)			S&P SmallCap 600 Index (pt)	
1-Jan-20	3,231		1-Jan-20	2,063		1-Jan-20	1,021
Bottom	2,237		Bottom	1,219		Bottom	596
14-May-20	2,820		14-May-20	1,551		14-May-20	701
YTD return	-12.7%		YTD return	-24.8%		YTD return	-31.4%
Bottom	-30.8%		Bottom	-40.9%		Bottom	-41.7%
Recovery	18.0%		Recovery	16.1%		Recovery	10.3%

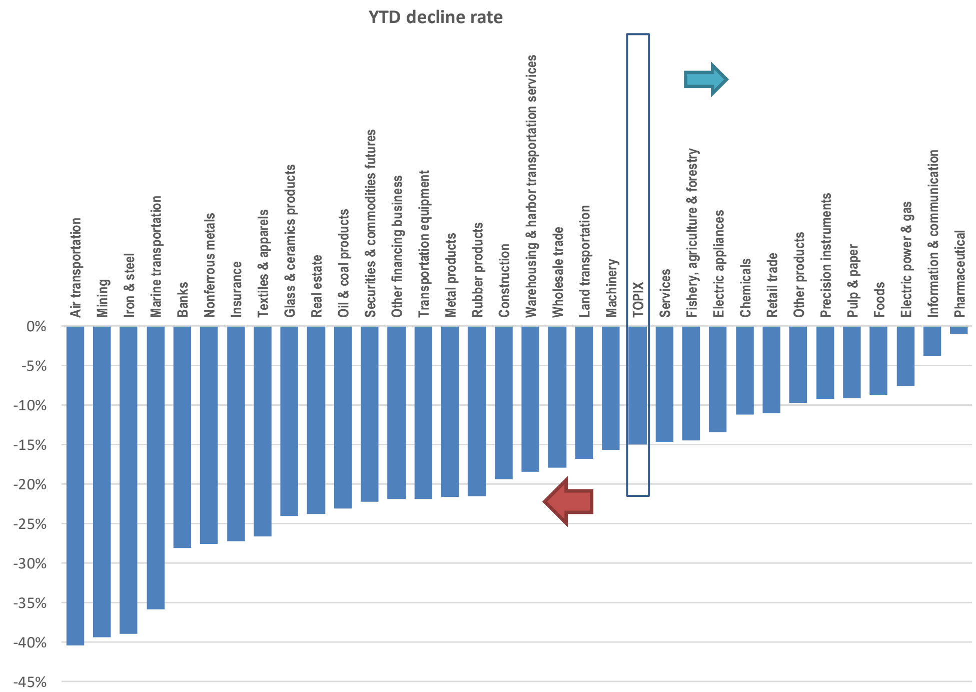
Source: Bloomberg; compiled by Daiwa Securities.

In short, if we look at all nations as one aggregate, a checkmark recovery is expected in the post-coronavirus picture, with a mixture of some sectors seeing a V-shaped recovery but others more like L-shaped. While the NASDAQ Index achieved a V-shaped recovery and recouped all its losses for the year, the 'recovery' for small caps is closer to L-shaped stagnation, although both are US stocks. That the difference in stock price responses based on sector and size has widened to such an extreme degree is significant when considering the post-pandemic world.

SMEs are playing the largest role in terms of the number of people employed. Prolonged monetary easing seems certain, considering that companies with high employment absorbing capacity are being hit the hardest, together with the current employment situation and studies showing that 42% of pandemic-induced layoffs will lead to long-lasting joblessness. If appropriate (i.e., an extraordinarily large amount of) fiscal spending is not implemented, the US economy may follow a path of Japanification.

[1] For reference, YTD return and recovery rates by sector at firms listed on TSE first section are shown on the next page.

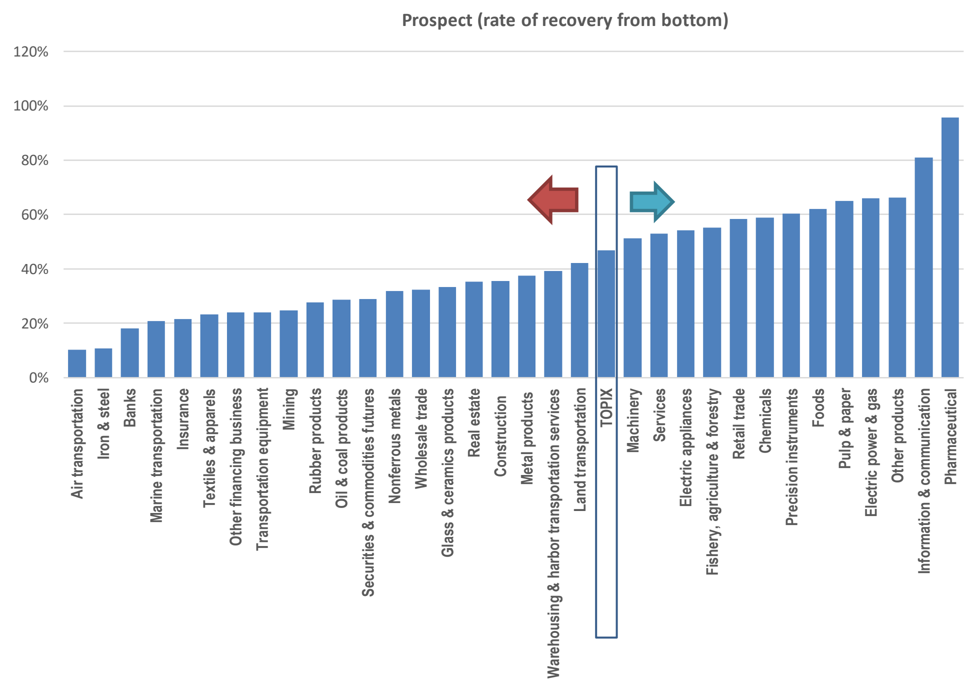
Chart: Performance of Firms Listed on TSE First Section by Sector



YTD decline rate	
-40.4%	Air transportation
-39.4%	Mining
-39.0%	Iron & steel
-35.9%	Marine transportation
-28.1%	Banks
-27.6%	Nonferrous metals
-27.2%	Insurance
-26.6%	Textiles & apparels
-24.1%	Glass & ceramics products
-23.8%	Real estate
-23.1%	Oil & coal products
-22.3%	Securities & commodities futures
-21.9%	Other financing business
-21.9%	Transportation equipment
-21.6%	Metal products
-21.5%	Rubber products
-19.4%	Construction
-18.4%	Warehousing & harbor transportation services
-18.0%	Wholesale trade
-16.8%	Land transportation
-15.7%	Machinery
-15.0%	TOPIX
-14.7%	Services
-14.5%	Fishery, agriculture & forestry
-13.4%	Electric appliances
-11.2%	Chemicals
-11.0%	Retail trade
-9.8%	Other products
-9.2%	Precision instruments
-9.1%	Pulp & paper
-8.7%	Foods
-7.6%	Electric power & gas
-3.7%	Information & communication
-1.0%	Pharmaceutical

Source: Bloomberg; compiled by Daiwa Securities.

Chart: Performance of Firms Listed on TSE First Section by Sector



Prospect (rate of recovery from bottom)	
10.2%	Air transportation
10.9%	Iron & steel
18.0%	Banks
20.9%	Marine transportation
21.5%	Insurance
23.3%	Textiles & apparels
24.0%	Other financing business
24.0%	Transportation equipment
24.8%	Mining
27.7%	Rubber products
28.8%	Oil & coal products
29.0%	Securities & commodities futures
32.0%	Nonferrous metals
32.3%	Wholesale trade
33.2%	Glass & ceramics products
35.3%	Real estate
35.5%	Construction
37.6%	Metal products
39.3%	Warehousing & harbor transportation services
42.3%	Land transportation
46.8%	TOPIX
51.2%	Machinery
53.0%	Services
54.1%	Electric appliances
55.2%	Fishery, agriculture & forestry
58.4%	Retail trade
59.0%	Chemicals
60.4%	Precision instruments
62.1%	Foods
65.1%	Pulp & paper
66.0%	Electric power & gas
66.3%	Other products
80.9%	Information & communication
95.8%	Pharmaceutical

Source: Bloomberg; compiled by Daiwa Securities.

Daiwa Securities

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■ Credit Rating Agencies

[Standard & Poor's]

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[Moody's]

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[Fitch]

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February 2020

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1) As of 26 April 2016, Daiwa Securities Co. Ltd., its parent company Daiwa Securities Group Inc., GMO Financial Holdings, Inc., and its subsidiary GMO CLICK Securities, Inc. concluded a basic agreement for the establishment of a business alliance between the four companies.
As of end-December 2017, Daiwa Securities Group Inc. owned shares in GMO Financial Holdings, Inc. equivalent to approximately 9.3% of the latter's outstanding shares. Given future developments in and benefits from the prospective business alliance, Daiwa Securities Group Inc. could boost its stake in GMO Financial Holdings, Inc. to up to 20% of outstanding shares.

2) Daiwa Real Estate Asset Management is a subsidiary of Daiwa Securities Group Inc. and serves as the asset management company for the following J-REITS: Daiwa Office Investment Corporation (8976), Daiwa Securities Living Investment Corporation (8986).

3) Samty Residential Investment became a consolidated subsidiary of Daiwa Securities Group Inc. effective 10 September 2019.

4) On 30 May 2019, Daiwa Securities Group Inc. formalized an equity/business alliance with Samty, and as of 14 June 2019 it owned 16.95% of shares outstanding in Samty along with convertible bonds with a par value of Y10bn. Conversion of all of said convertible bonds into common shares would bring the stake of Daiwa Securities Group Inc. in Samty to 27.28%.

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- Before engaging in any trading, please thoroughly confirm accounting and tax treatments regarding your trading in financial instruments with such experts as certified public accountants.

* The amount of the trading commission cannot be stated here in advance because it will be determined between our company and you based on current market conditions and the content of each transaction etc.
** The ratio of margin requirements etc. to the amount of the transaction cannot be stated here in advance because it will be determined between our company and you based on current market conditions and the content of each transaction etc.

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