

Today's Topic **Japanese Equity Market Outlook**

What are the conditions to enter new market phase?

Point 1

Japanese equity market can renew its record-high just by “end of deflation”
Nominal GDP is expected to continue growing with around +2% YoY going forward

- We think background of Nikkei 225 index surpassed its record-high after 1990s was mainly due to nominal GDP (GDP measured by current market price) surpassed its peak of 20 years ago. Comparing nominal GDP growth rate 1) from peak of nominal GDP till start of economic policy of Abe’s government called Abenomics (Oct.-Dec. 1997 to Oct.-Dec. 2012) and 2) from start of Abenomics till recent (Oct.-Dec. 2012 to Jul.-Sep. 2017), it accelerated from average of - 0.6% per year to + 2.3% per year.
- What must be noted is that GDP deflator had changed almost 2% from average of - 1.1% per year to + 0.8% during the same period which indicates “end of deflation”. We believe Nikkei 225 index will possibly renew its record-high due to likely continuation of “end of deflation”, as nominal GDP growth rate is expected to be around + 2% YoY going forward.

Point 2

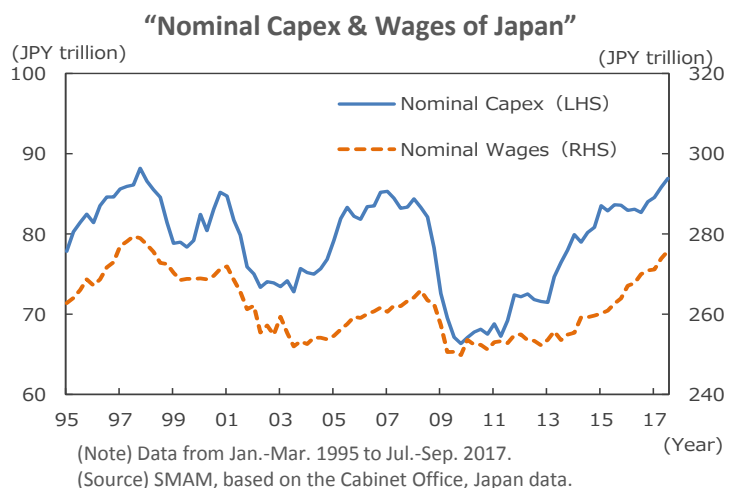
New market phase means economic “recovery with moderate inflation”
Focus should be on capital expenditure (capex) and employee compensation

- Further rise of Japanese equity market can be expected if Japanese economy progresses from “end of deflation” stage to “recovery with moderate inflation” stage which will lead to higher growth of nominal GDP. Conditions of materializing this scenario are 1) continuation of increase in private capex and 2) increase in employee compensation by improvement in employment and wages.
- Japanese corporates are increasing capex. Compensation on employee is slowly but steadily improving. We expect wages to rise if recovery of capex can sustain growth of about + 3% per annum reflecting shortage of labor.

Future Outlook

Focus should be on change of corporate activities influenced by continuation of capex recovery

- The global economy is expected to moderately expand led by growth in Asia. Japanese economy is also likely to grow led by export and capex. Therefore, Japanese economy will be able to enter into phase of “recovery with moderate inflation” supported by rising wages, if Japanese corporates are confident with sustainable increase in capex. If this possibility increases, we believe that Japanese stock market will enter into new market phase.





Disclaimer

Please read this disclaimer carefully.

- This material is for non-Japanese institutional investors only.
- The research and analysis included in this report, and those opinions or judgments as outcomes thereof, are intended to introduce or demonstrate capabilities and expertise of Sumitomo Mitsui Asset Management Company, Ltd. (hereinafter "SMAM"), or to provide information on investment strategies and opportunities. Therefore this material is not intended to offer or solicit investments, provide investment advice or service, or to be considered as disclosure documents under the Financial Instruments and Exchange Law of Japan.
- The expected returns or risks in this report are calculated based upon historical data and/or estimated upon the economic outlook at present, and should be construed no warrant of future returns and risks.
- Past performance is not necessarily indicative of future results.
- The simulated data or returns in this report besides the fund historical returns do not include/reflect any investment management fees, transaction costs, or re-balancing costs, etc.
- The investment products or strategies do not guarantee future results nor guarantee the principal of investments. The investments may suffer losses and the results of investments, including such losses, belong to the client.
- The recipient of this report must make its own independent decisions regarding investments.
- The opinions, outlooks and estimates in this report do not guarantee future trends or results. They constitute SMAM's judgment as of the date of this material and are subject to change without notice.
- The awards included in this report are based on past achievements and do not guarantee future results.
- The intellectual property and all rights of the benchmarks/indices belong to the publisher and the authorized entities/individuals.
- This material has been prepared by obtaining data from sources which are believed to be reliable but SMAM can not and does not guarantee its completeness or accuracy.
- All rights, titles and interests in this material and any content contained herein are the exclusive properties of SMAM, except as otherwise stated. It is strictly prohibited from using this material for investments, reproducing/copying this material without SMAM's authorization, or from disclosing this material to a third party.

Registered Number: Kanto Local Finance Bureau (KINSHO) No.399
Member of Japan Investment Advisers Association, The Investment Trusts Association, Japan and
Type II Financial Instruments Firms Association
© Sumitomo Mitsui Asset Management Company, Limited
