



Outlook for Japanese Stock Market & Economy

Sumitomo Mitsui DS Asset Management

-January 2022-



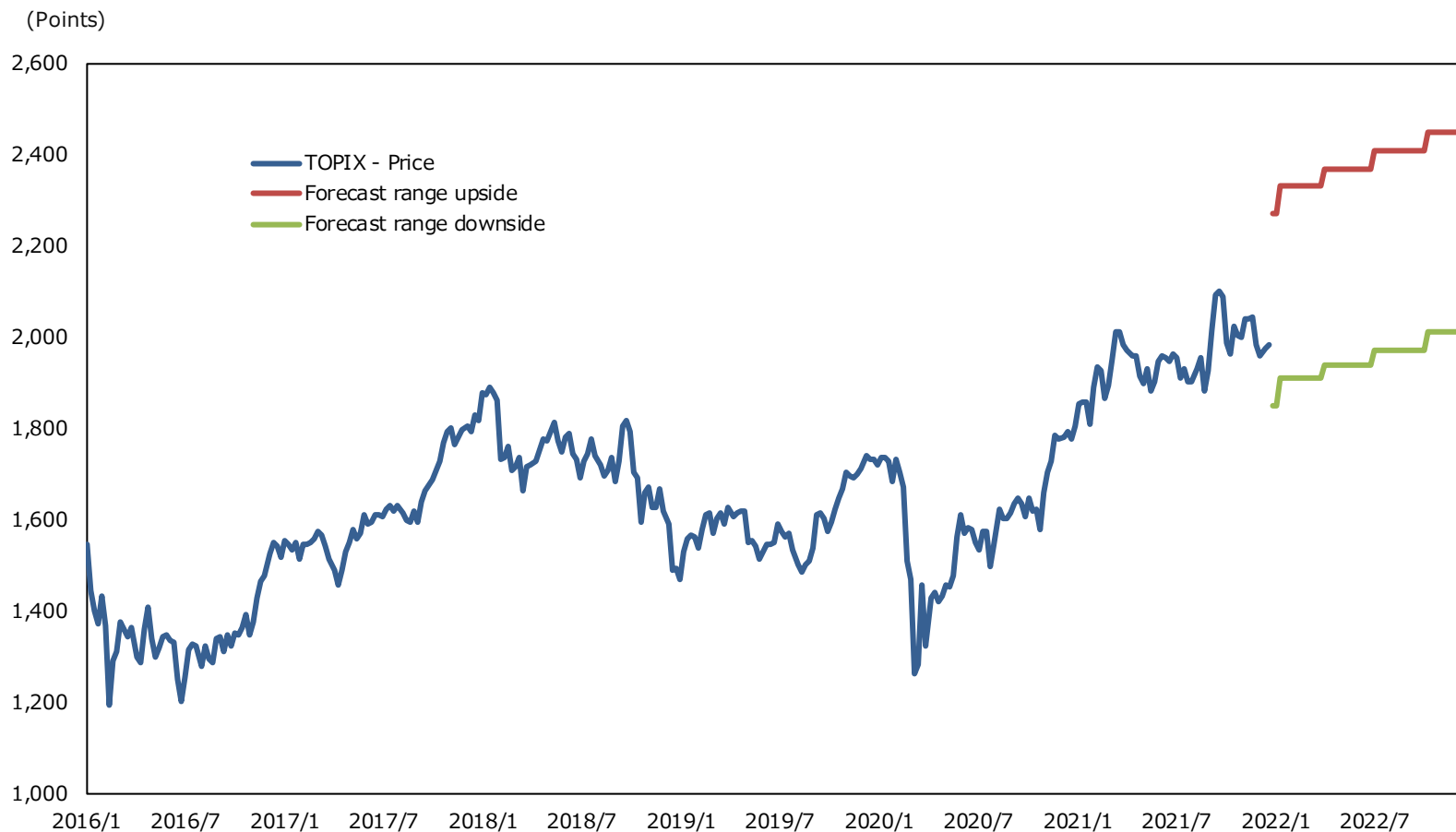
Outlook for Japanese Stock Market

Market Outlook

- We expect the Japanese equity market to continue on its bullish trend thanks to steady growth of corporate earnings and accelerating economic recovery towards FY 2022.
- We have slightly raised our TOPIX target for CY 2022 to 2,230 and Nikkei 225 to 32,000 by reflecting the upward revision of our earnings forecast.
- TOPIX EPS could rebound by 40+% YOY in FY 2021 to 134 points, a historical high, and continue its double digit growth to 151 points in FY 2022.
- Investors are concerned about the global supply chain problem, the margin squeeze caused by rising material costs, and the spread of the new variant of COVID-19 in the short term. We believe the market will resume its bullish trend after confirming sound fundamentals, such as the normalization of the economy and continuous earnings growth in the mid-to-long term.



TOPIX & our forecast – bullish market going forward



Note: TOPIX data is from Jan. 1st 2016 to Dec. 17th 2021
(Source) TOPIX: Tokyo Stock Exchange, forecast by SMDAM

(Year/Month)

Upside / Downside risk factors ahead

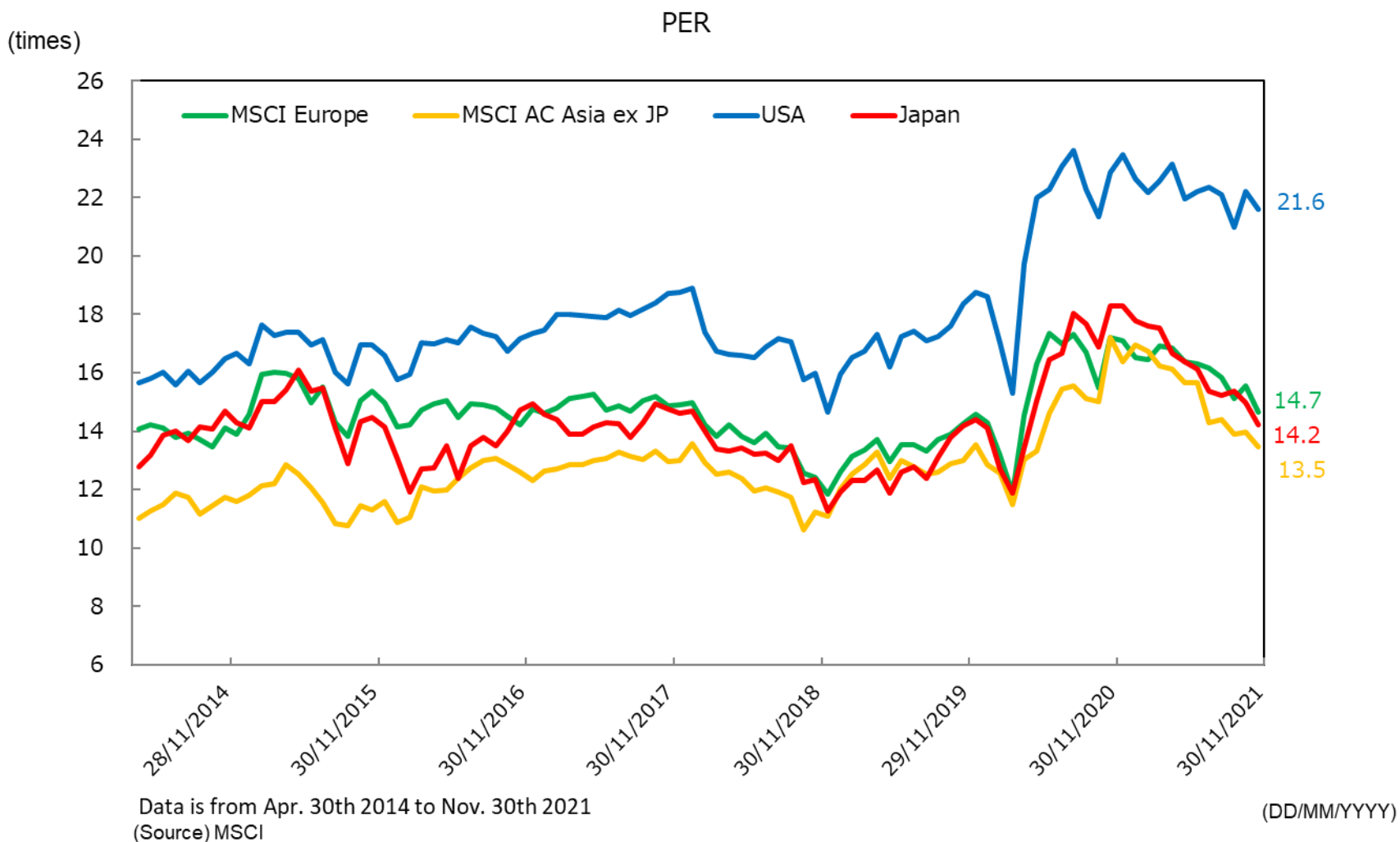
■ Upside Risks

- Rapid normalization/ recovery of global economy from COVID-19 pandemic
- Recovery of inbound travel activities to Japan

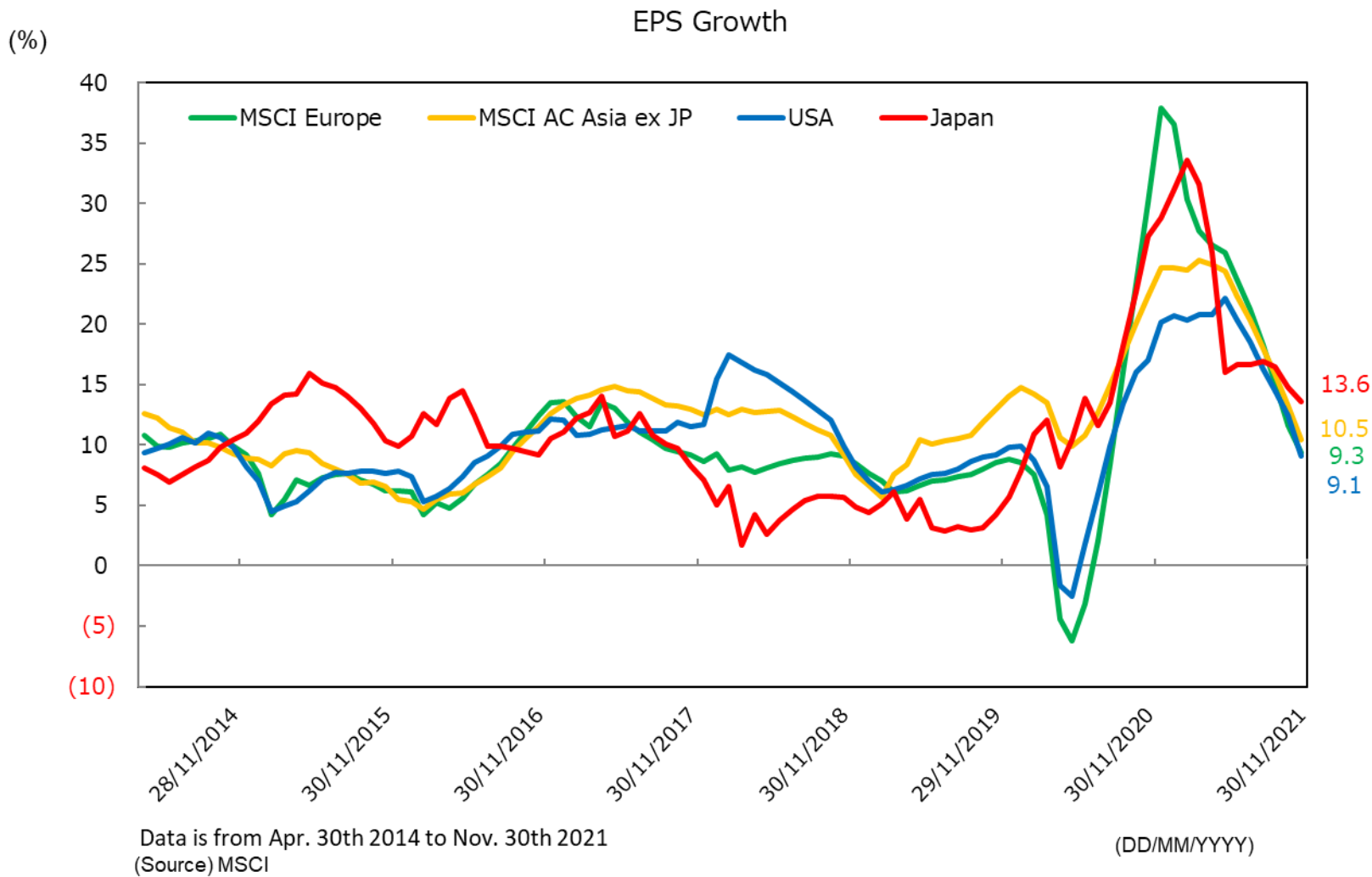
■ Downside Risks

- Delay of the normalization of the domestic economy due to the new COVID-19 variant
- Further deterioration of the bottle neck problem in the global supply chain
- Concern about stagflation

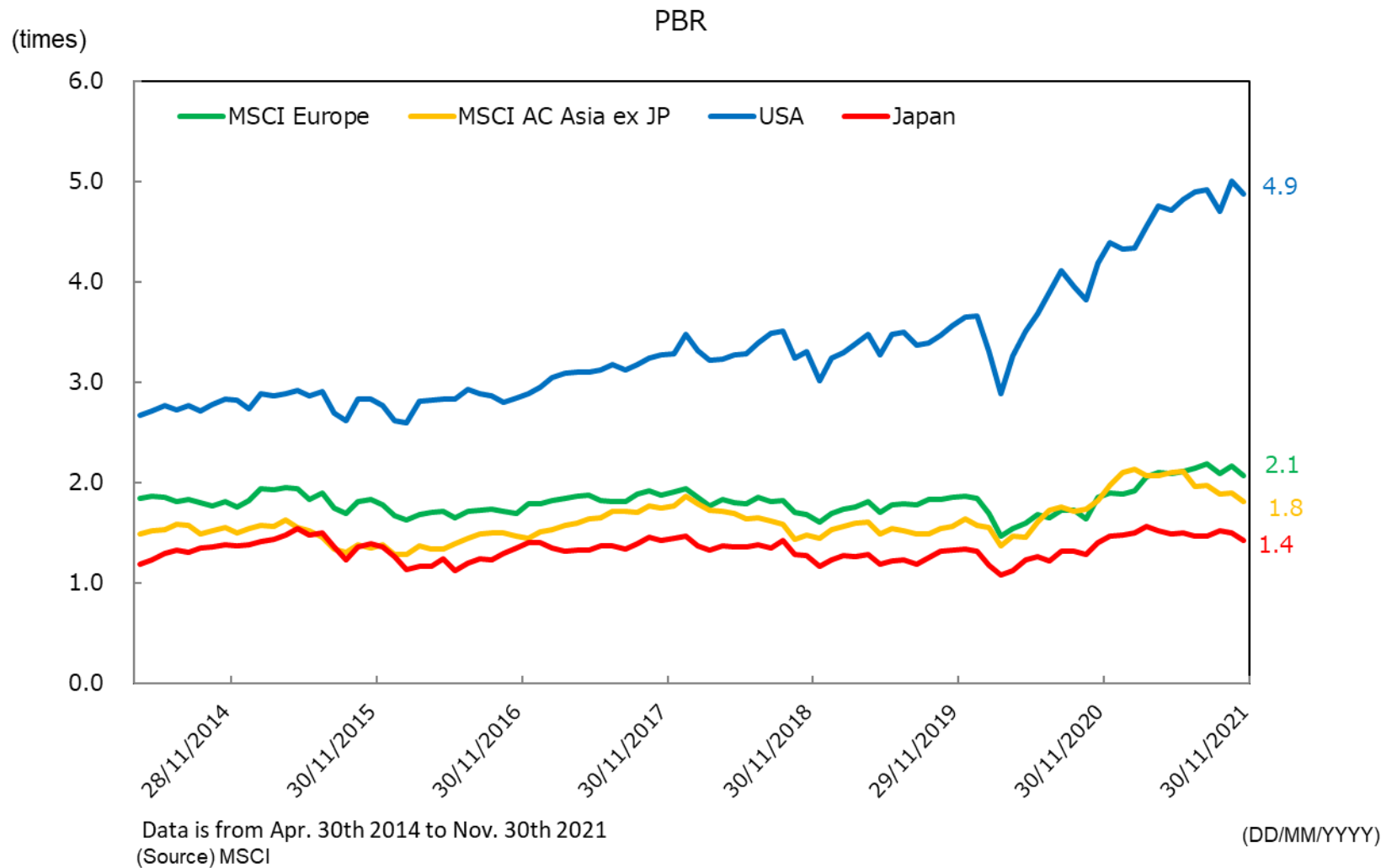
Earnings recovery brings PER back to normal



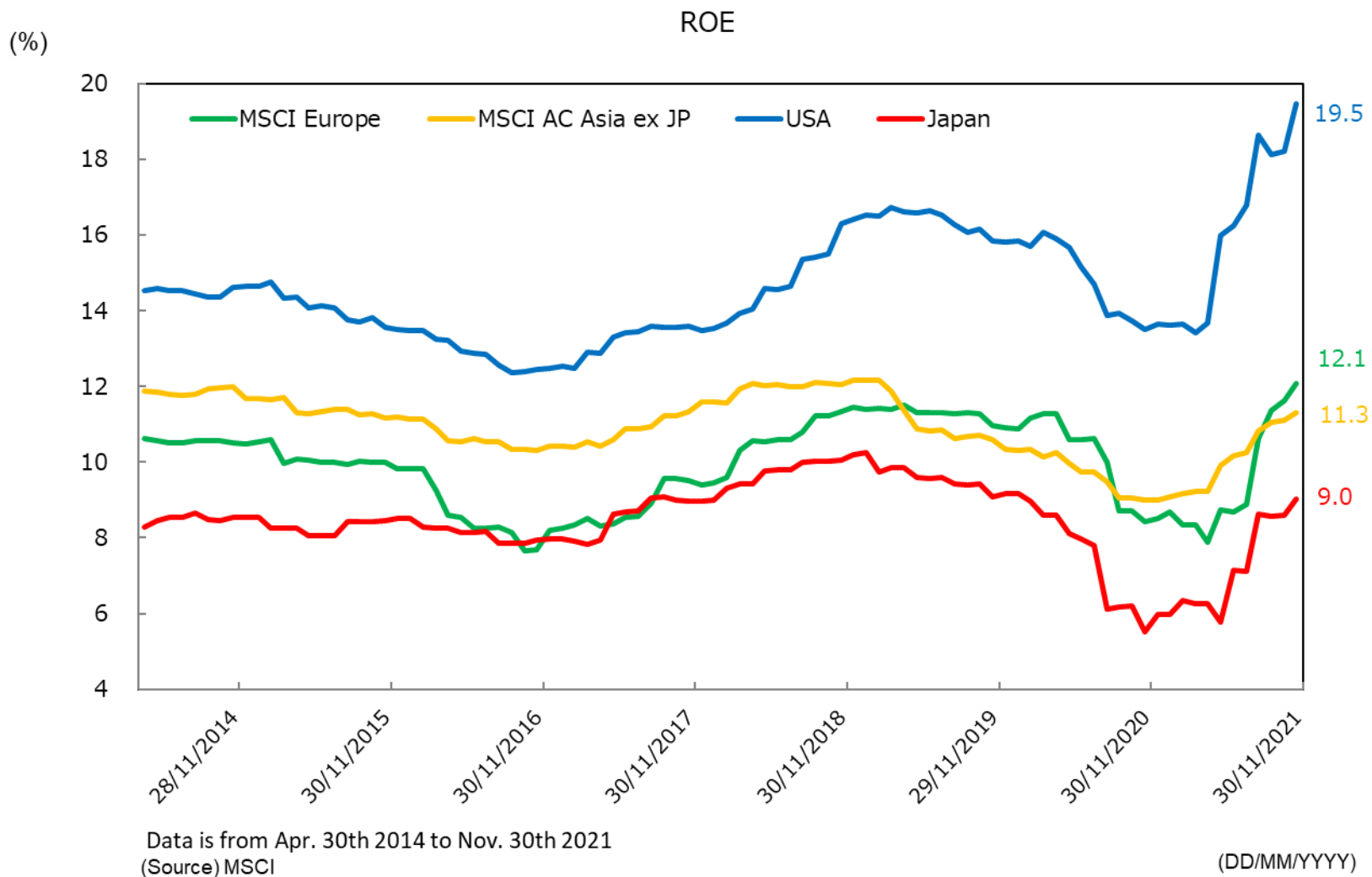
EPS growth slowing to normal after big swing



PBR – mind the gap between US and others

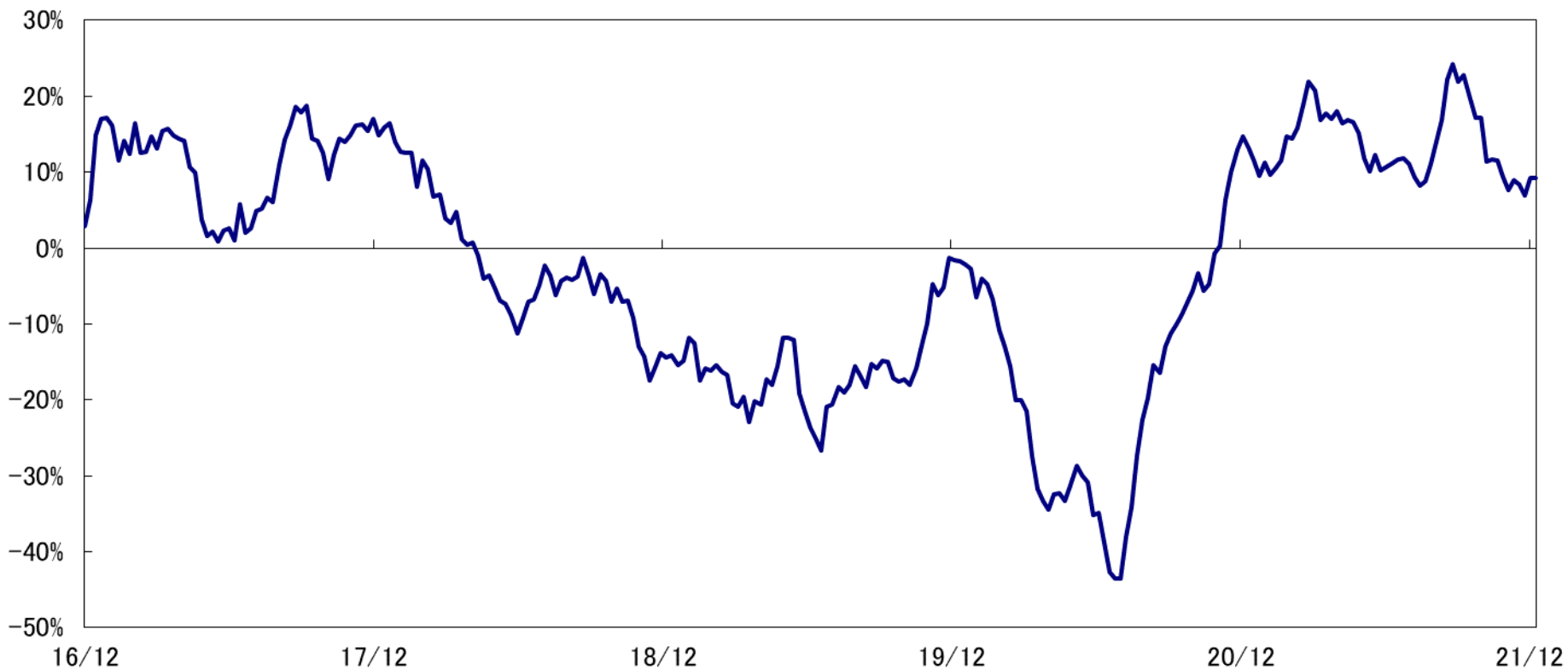


Japan's ROE recovering but still lagging behind peers



Earnings results continuously beat street consensus

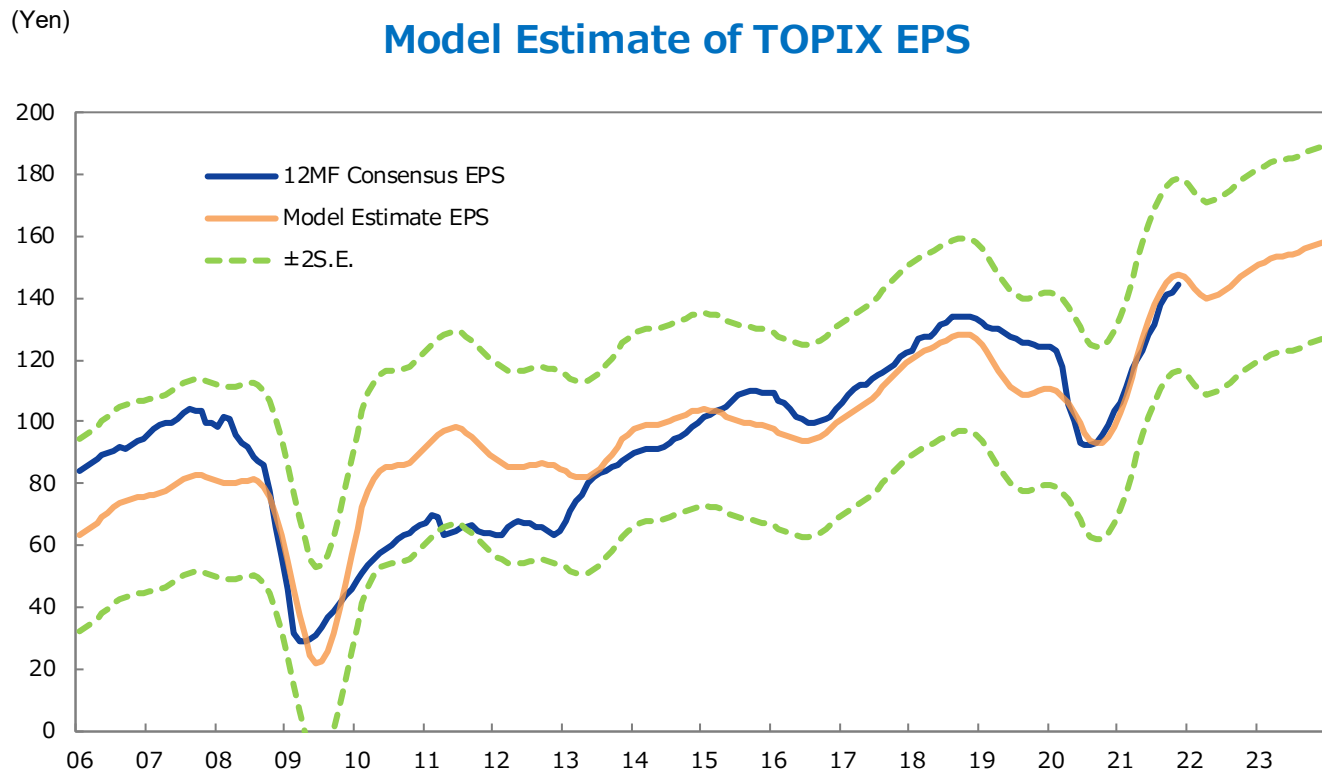
TOPIX Revision Index



Data is from Dec. 1st 2016 to Dec. 9th 2021
(Source) Datastream, IBES

(YY/MM)

Quants estimate, EPS reaccelerates after short break next spring

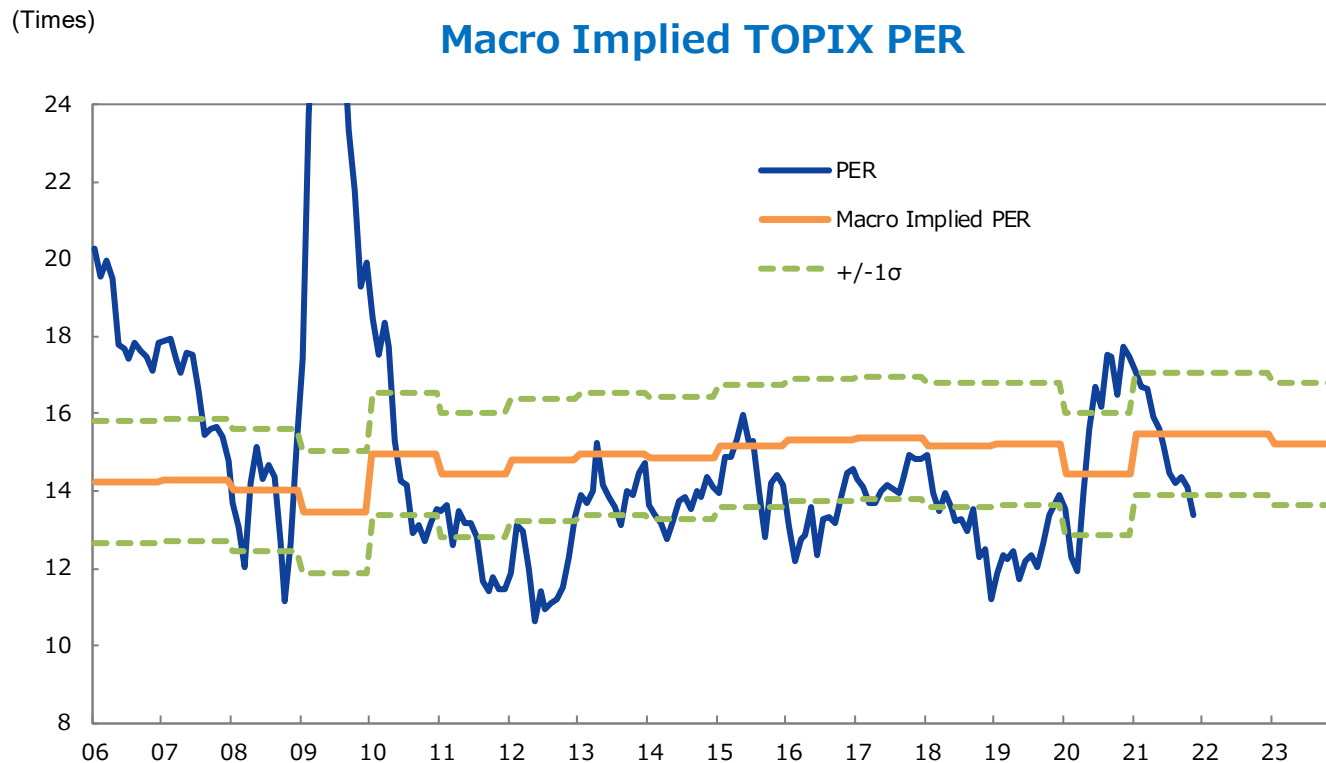


Consensus data is from Jan. 2006 to Nov. 2021, Model data is from Jan. 2006 to Dec. 2023

(Year)

(Source) SMDAM

Quants estimate, PER sank below the bottom of the normal range

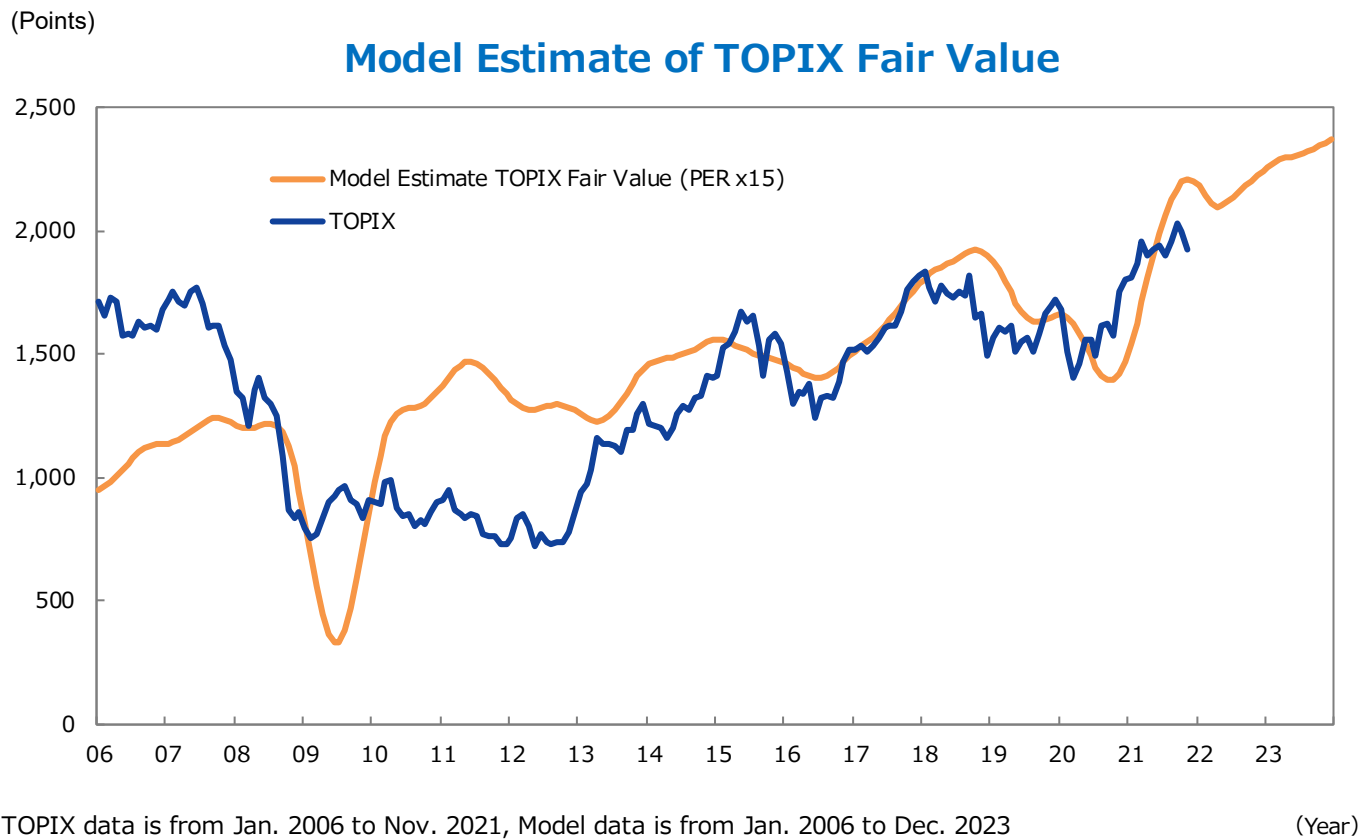


Consensus data is from Jan. 2006 to Nov. 2021, Model data is from Jan. 2006 to Dec. 2023

(Year)

(Source) SMDAM

Quants model suggests attractive opportunity to accumulate

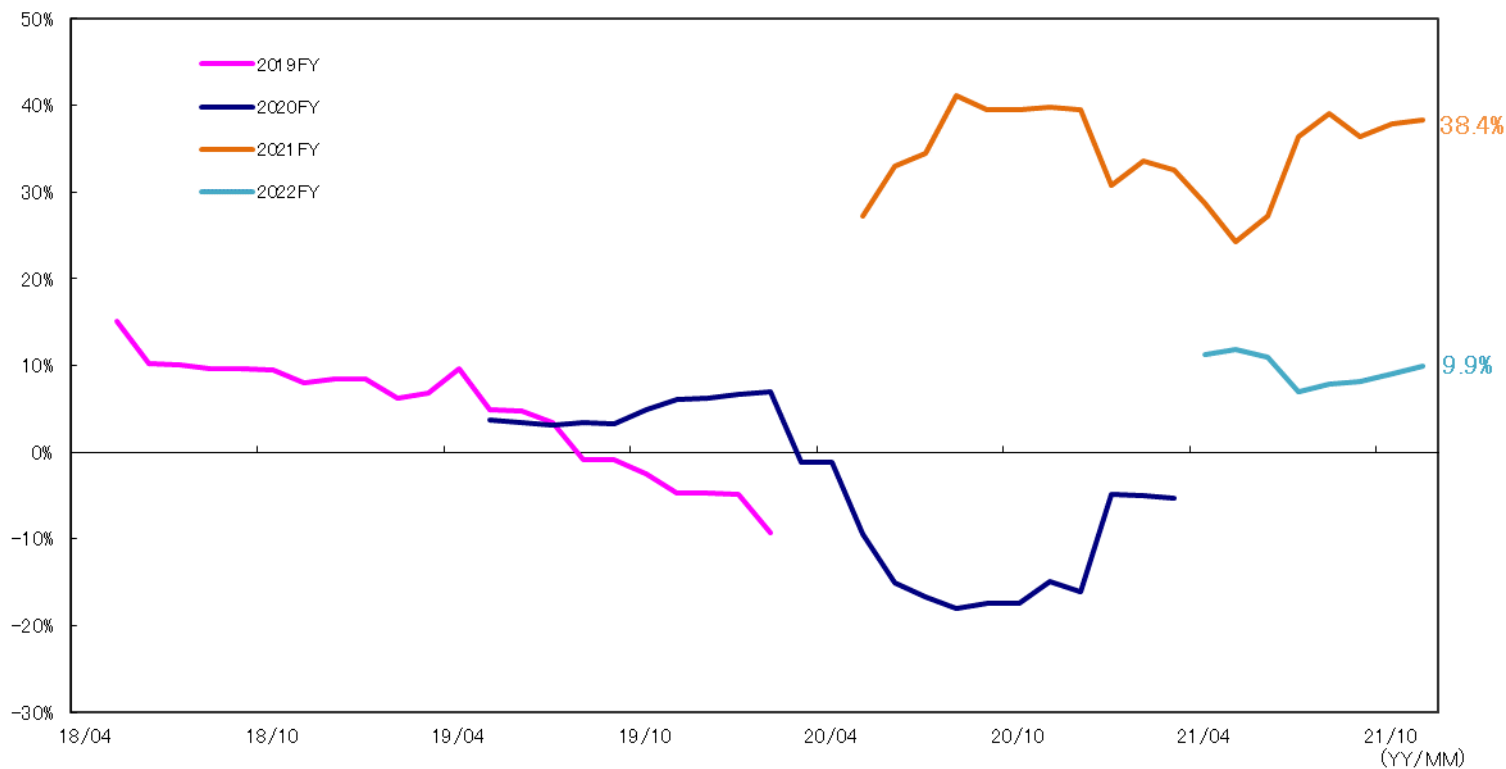


TOPIX data is from Jan. 2006 to Nov. 2021, Model data is from Jan. 2006 to Dec. 2023

(Source) SMDAM

Bottom up estimate – steady profit growth to continue next year

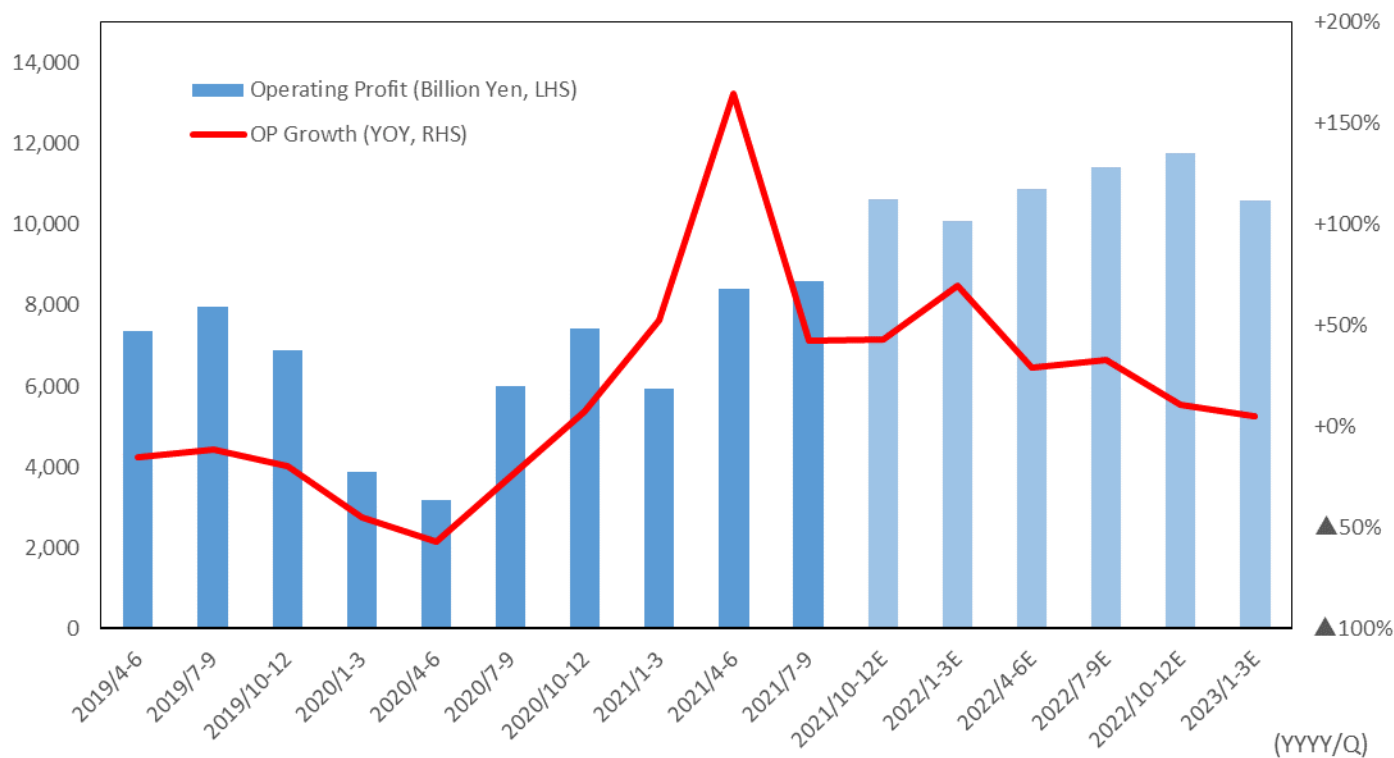
SMDAM Core Research Universe (Excl. Financials) Est. Recurring Profit Growth



Note: Data is as of Dec. 13th 2021, SMDAM Core Universe (Excl. Financials) consists of 452 major Japanese companies covered by SMDAM in-house analysts.
(Source) SMDAM

Bottom up estimate – steady outlook of operating profit

Operating Profit (All Industries Excl. Financials and Softbank Group)



Actual data is from Q2 2019 to Q3 2021, estimate data is from Q4 2021 to Q1 2023
 (Source) SMDAM

Japan's corporate culture – favorable changes for shareholders

Investors that have signed up to the Principles for Responsible Institutional Investors	
Trust banks	6
Investment managers	205
Insurance companies	24
Pension funds	74
Others	11
Total	320

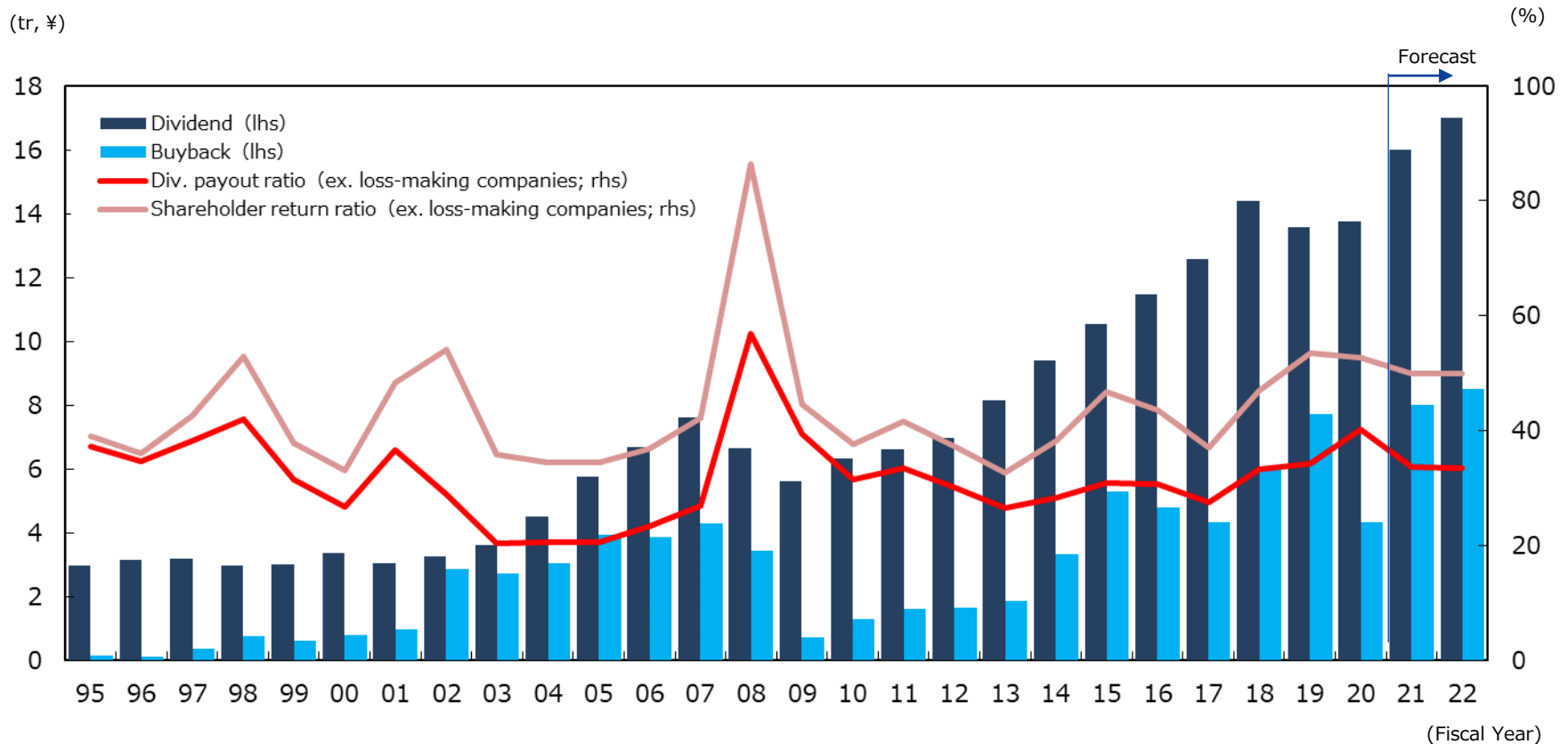
note: As of Nov. 30th 2021

(Source) FSA, SMDAM

- The Stewardship Code (SC) was set in February 2014. Investors are taking a more pro-active approach in talking to companies and exercising proxy voting rights. The Financial Services Agency discloses the name of institutional investors which have publicly accepted the SC.
- After the inception of the Corporate Governance Code (CGC) in June 2015, pressure has been increasing on companies to improve their governance, efficiency and shareholder returns.
- These two codes have been progressively reviewed and enhanced, and are making visible impact on corporate behavior and investors' attitudes as shareholders.
- In a recent amendment of the CGC, companies are required to explain the rationale of "cross holdings" or "strategic holdings" of other companies' shares, which implicitly provide protection against takeovers and hostile shareholder actions, and is often negative for achieving shareholder value.
- The SC was reinforced in March 2020 to require investors to evaluate ESG factors.

Dividends and buybacks – increasing shareholders’ returns

Shareholder Return Ratio, Div. Payout Ratio, Dividend Payment, & Share Buyback



Note: Data is from FY1995 to FY2022, FY2021 and FY2022 are forecasts from Toyo-Keizai for dividends and from Daiwa Securities for share buybacks.

Source: Toyo Keizai, Quick, and INDB compiled by Daiwa Securities

Winners and losers, Growth & Large Cap dominate the market

Performance Comparison of Russell/Nomura Style Indices

Index	Returns(%)						
	3 Month	6 Month	YTD	1 Year	2 year	3 Year	5 Year
RN Japan Equity	-5.48	1.18	10.05	10.86	14.38	25.90	29.50
Total Value	-4.99	-1.12	15.48	15.58	3.92	9.37	6.86
Top Cap Value	-2.92	0.32	20.49	20.41	12.94	20.55	13.80
Large Cap Value	-4.38	-0.90	17.09	17.15	5.15	10.43	7.15
Mid Cap Value	-6.15	-2.39	13.02	13.26	-5.19	-2.86	-1.98
Small Cap Value	-7.98	-2.30	8.18	8.39	-1.79	4.35	4.60
Micro Cap Value	-6.54	0.10	8.52	8.07	-2.49	6.79	10.60
Total Growth	-5.77	4.13	4.87	6.33	24.08	42.85	55.18
Top Cap Growth	-3.28	6.61	7.62	9.72	29.55	53.58	63.47
Large Cap Growth	-5.21	4.85	5.32	6.91	26.42	46.06	57.08
Mid Cap Growth	-8.44	1.85	1.46	2.26	21.07	34.57	47.01
Small Cap Growth	-10.86	-2.40	1.06	1.19	5.41	18.28	38.41
Micro Cap Growth	-11.18	-3.71	1.20	0.66	7.43	21.21	47.50
Top Cap Total	-3.18	3.49	13.21	14.40	21.65	37.07	37.68
Large Cap Total	-4.90	1.79	10.77	11.68	16.63	28.68	31.59
Mid Cap Total	-7.34	-0.66	7.32	7.84	9.66	17.19	23.07
Small Cap Total	-9.17	-2.63	5.54	5.73	1.38	10.13	17.16
Micro Cap Total	-8.08	-1.19	6.14	5.66	1.38	12.33	23.45

Note : As of Dec. 15th 2021
(Source) Bloomberg



Outlook for Japanese Economy

Current status & Outlook of Japanese economy

[Current Status]

- The economy is recovering steadily. Despite negative factors such as the price hike in raw materials, the bottle neck in the global supply chain, and the spread of the new COVID-19 variant, the economy has been lifted by the recovery of consumer spending and the return to full production in the automobile industry.

[Outlook]

- ① **Our real GDP growth forecast for FY 2021 is unchanged at +2.7%. We have raised our forecast for FY 2022 to +2.9% from +2.6% and lowered the estimate for FY 2023 to +1.2% from 1.3%.** The main reason for the upward revision for FY 2022 is an increase in the size of fiscal stimulus. We expect strong economic growth from Q4 FY 2021 to Q2 FY 2022 thanks to declining COVID-19 infections, improving global supply chain confusion, and economic measures to boost demand. On and after Q3 2022, the pace of economic recovery will slow down owing to the receding effects of these supportive factors.
- ② **Our core CPI forecast for FY 2021 is unchanged at 0.0%. We have lowered our estimate for FY 2022 to +0.7% from +0.9% and maintained our forecast for FY 2023 at +0.6%.** The major reason for the change for FY 2022 is a revision of price forecast of crude oil from USD 80 per barrel to USD 70.
- ③ **We expect PM Kishida and his cabinet to maintain the existing policy mix, including accommodative fiscal and monetary policy.**
- ④ **The current accommodative monetary policy of the BOJ will be maintained for the foreseeable future.**

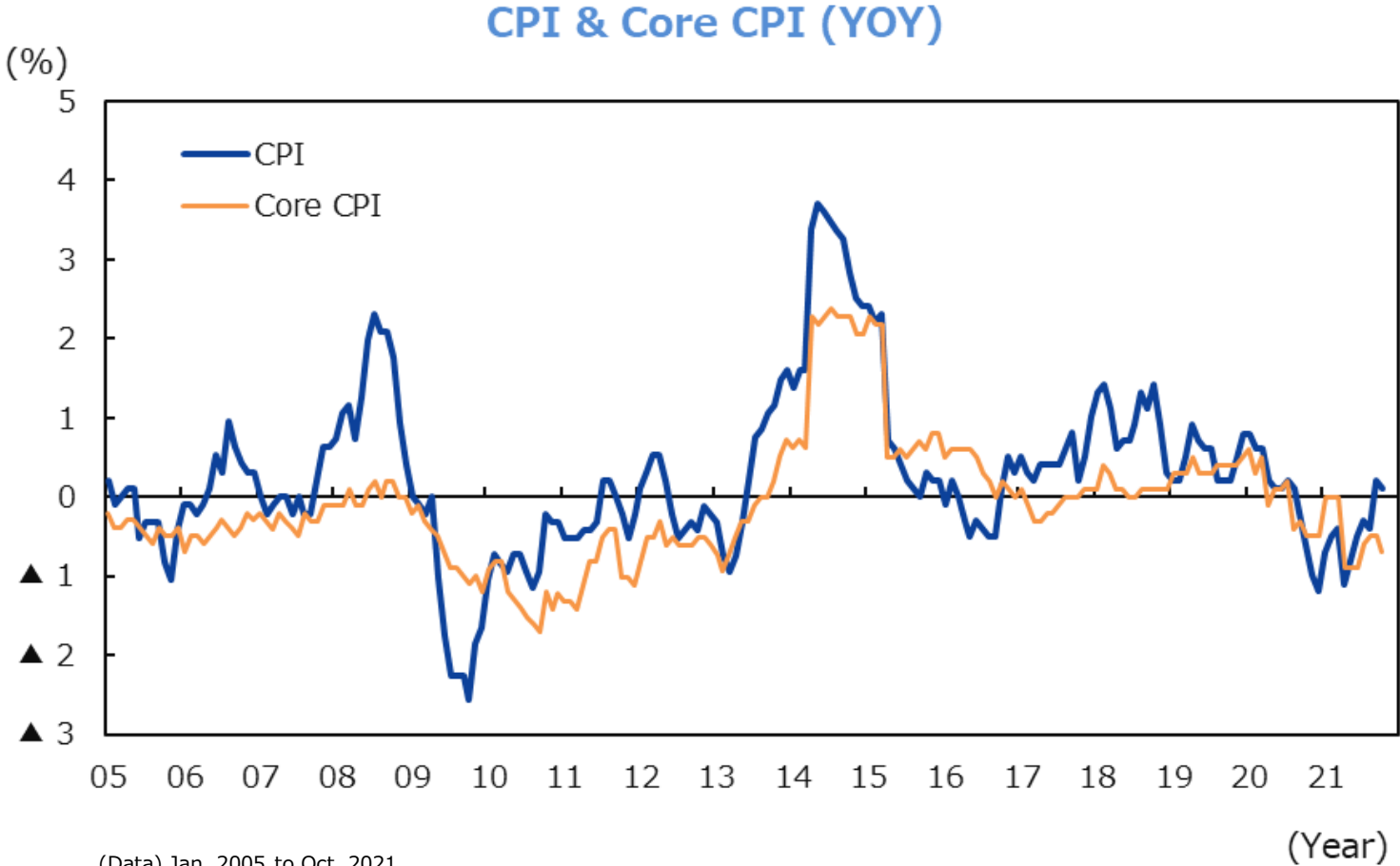
Forecast of Japanese economy

Forecast of Annual Real GDP Growth							
Fiscal Year	FY17	FY18	FY19	FY20	FY21 Est	FY22 Est	FY23 Est
Real GDP	1.8%	0.2%	-0.7%	-4.5%	2.7%	2.9%	1.2%
Private final consumption expenditure	1.0%	0.1%	-1.0%	-5.5%	2.7%	2.7%	0.9%
Private housing investment	-1.8%	-4.9%	2.6%	-7.8%	-0.6%	0.0%	0.1%
Private-sector capital investment	2.8%	1.2%	-0.6%	-7.5%	1.7%	4.0%	3.1%
Public fixed capital formation	0.6%	0.9%	1.6%	5.1%	-4.5%	1.0%	0.2%
Net export contribution	0.4%	-0.2%	-0.4%	-0.7%	0.9%	0.3%	0.1%
Exports of goods and services	6.3%	2.0%	-2.2%	-10.5%	12.2%	4.8%	4.1%
Imports of goods and services	3.8%	3.0%	0.2%	-6.6%	6.6%	3.4%	3.8%
Nominal GDP	2.0%	0.1%	0.2%	-3.9%	1.9%	3.3%	1.7%
GDP deflator	0.2%	-0.1%	0.8%	0.7%	-0.9%	0.4%	0.5%
Industrial Production Index	2.9%	0.3%	-3.7%	-9.9%	6.6%	5.6%	2.8%
Consumer Price Index (Core)	0.7%	0.8%	0.4%	-0.6%	0.0%	0.7%	0.6%
Domestic corporate goods price index	2.7%	2.2%	0.1%	-1.4%	6.2%	0.8%	0.2%
Employee compensation	2.0%	3.2%	2.0%	-1.5%	1.8%	1.8%	1.2%
Unemployment rate	2.7%	2.4%	2.4%	2.9%	2.8%	2.7%	2.6%
Call Rate (End value)	-0.1%	-0.1%	-0.1%	-0.1%	-0.1%	-0.1%	-0.1%

(Note) Rate of increase over the previous year. Net exports are based on the degree of contribution, and the consumer price index (Core) excludes the effects of the consumption tax and free education. The forecast is for Sumitomo Mitsui DS Asset Management.

(Source) Creation of Sumitomo Mitsui DS Asset Management based on data from the Cabinet Office, the Ministry of Internal Affairs and Communications, and the Ministry of Economy, Trade and Industry

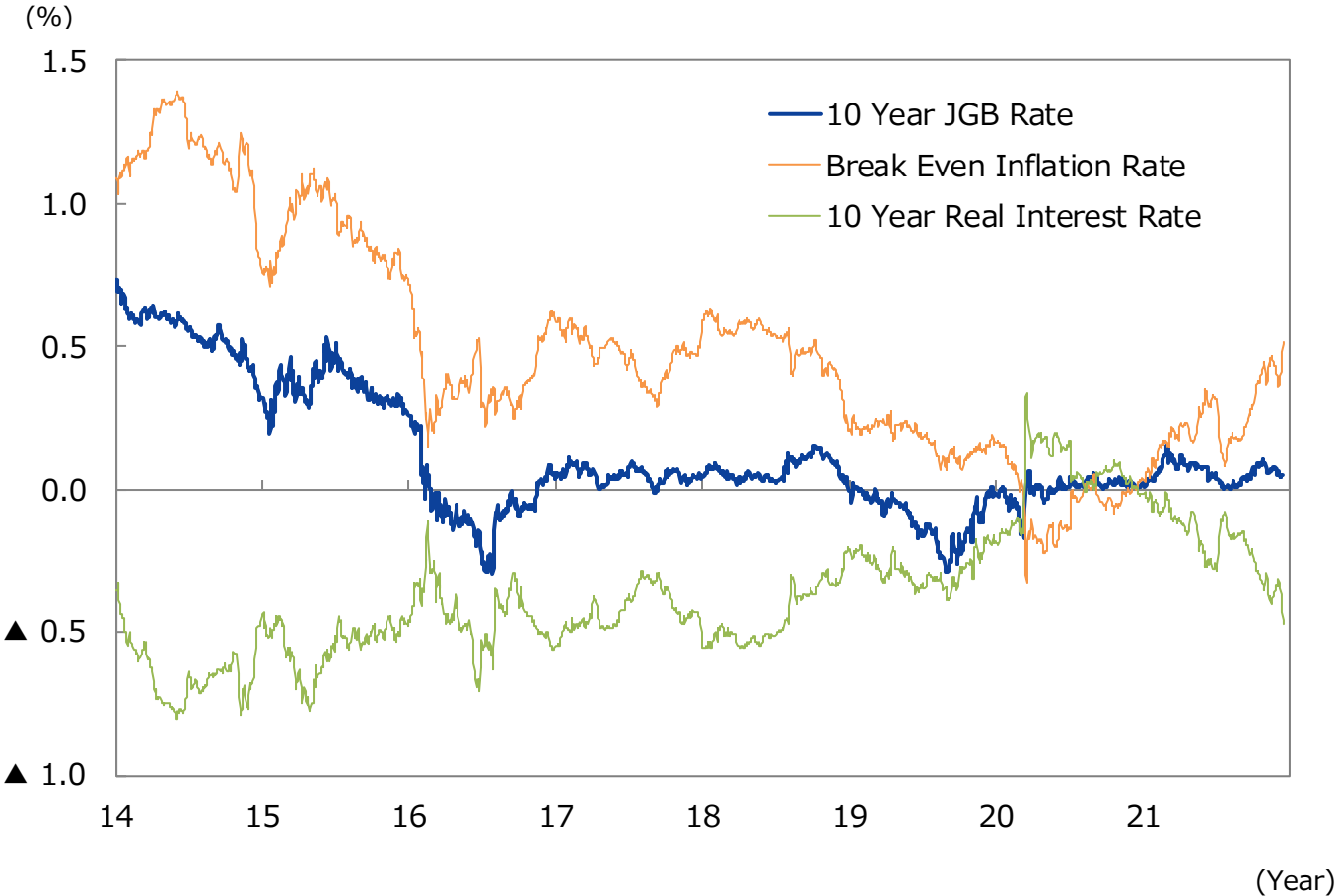
Deflation is still alive in Japan



(Data) Jan. 2005 to Oct. 2021
(Source) MIAC, Bloomberg, SMDAM

Inflation expectations take off?

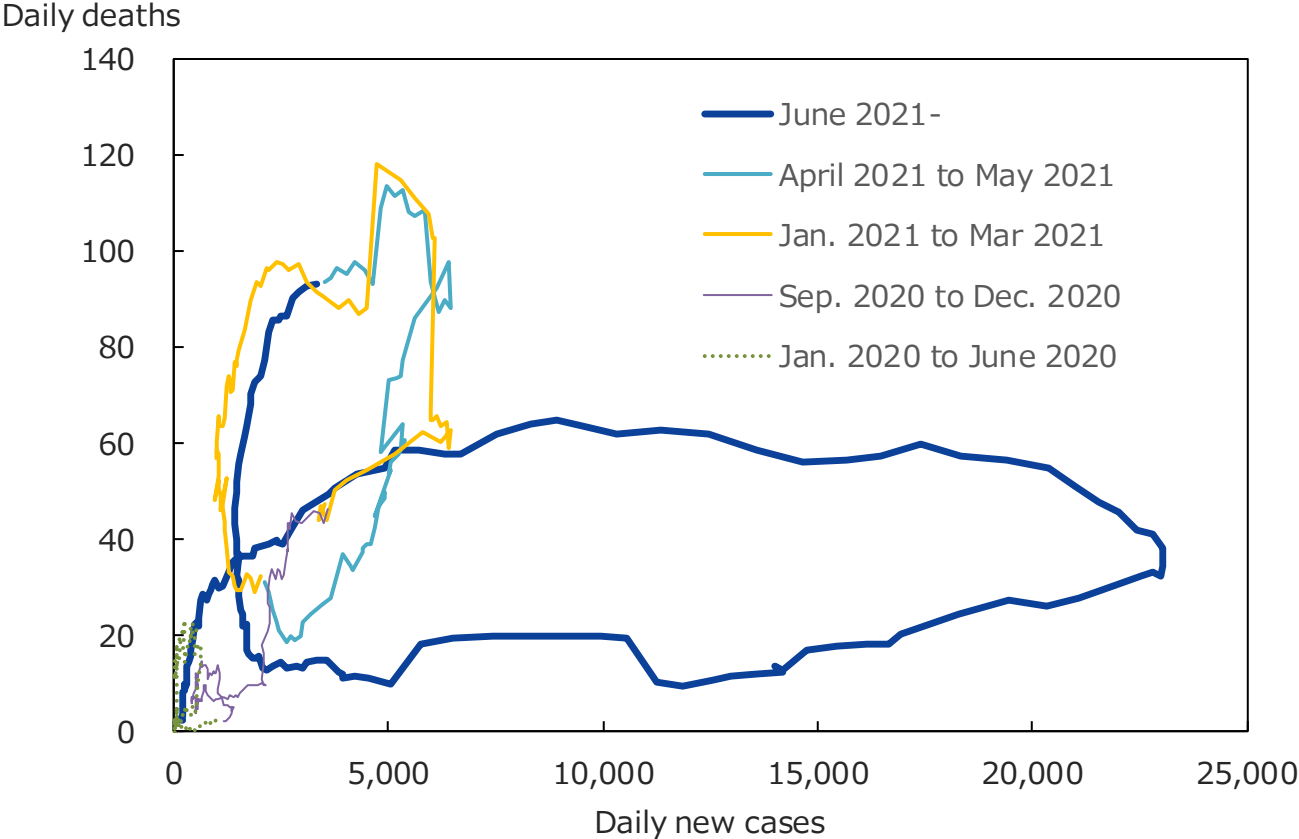
JGB, BEI, and Real Interest rate



(Data) From Jan. 1st 2014 to Dec. 14th 2021
(Source) Bloomberg, SMDAM

New cases of COVID-19 in Japan declined by 99+% from the peak

COVID-19 New patients and confirmed deaths

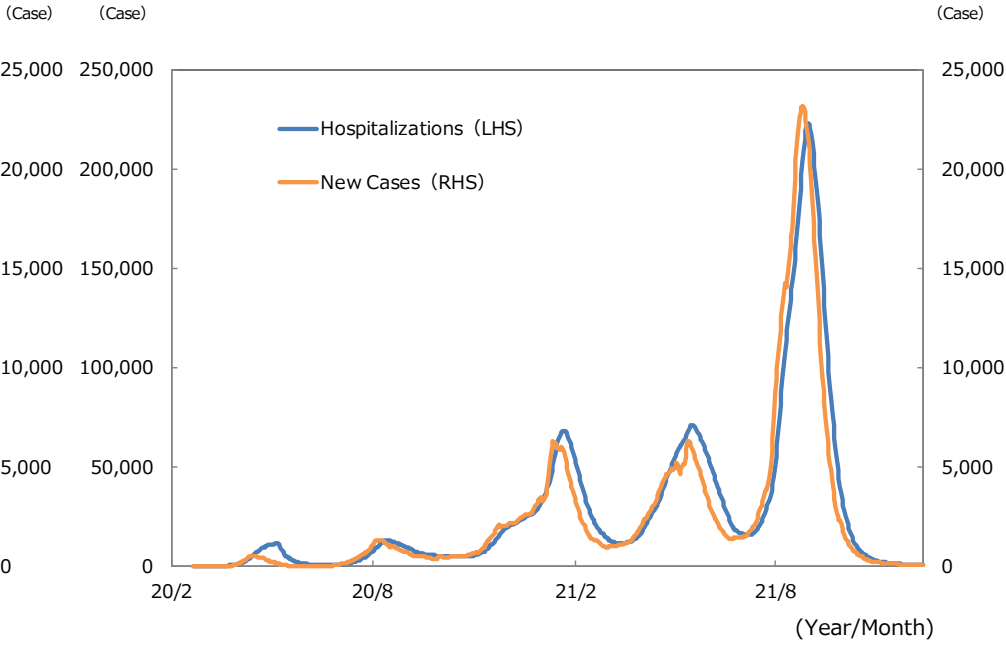
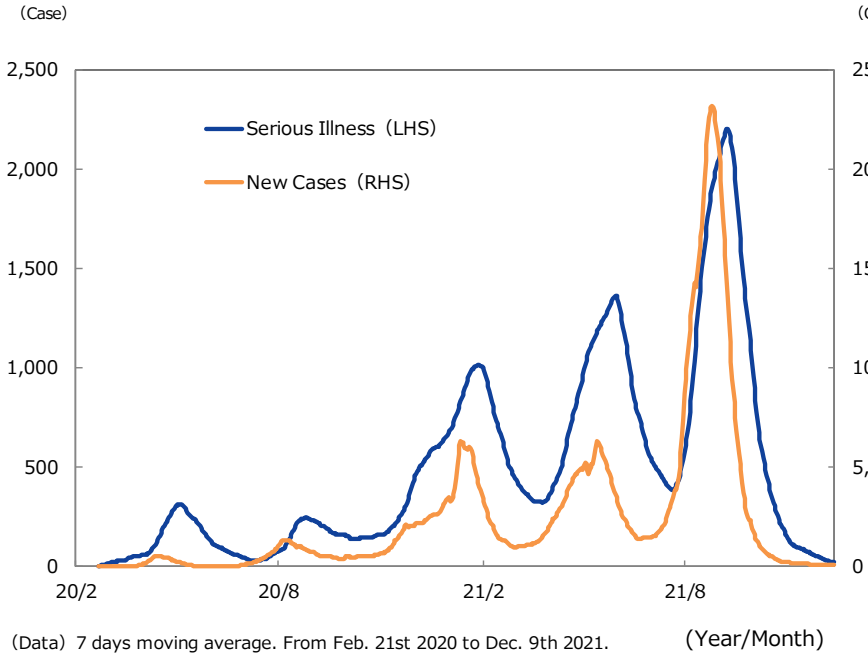


(Data) 7 days moving average, From Jan. 1st 2020 to Dec. 13th 2021
(Source) Bloomberg, SMDAM

Sudden/steep decline of COVID-19 infections & serious illness

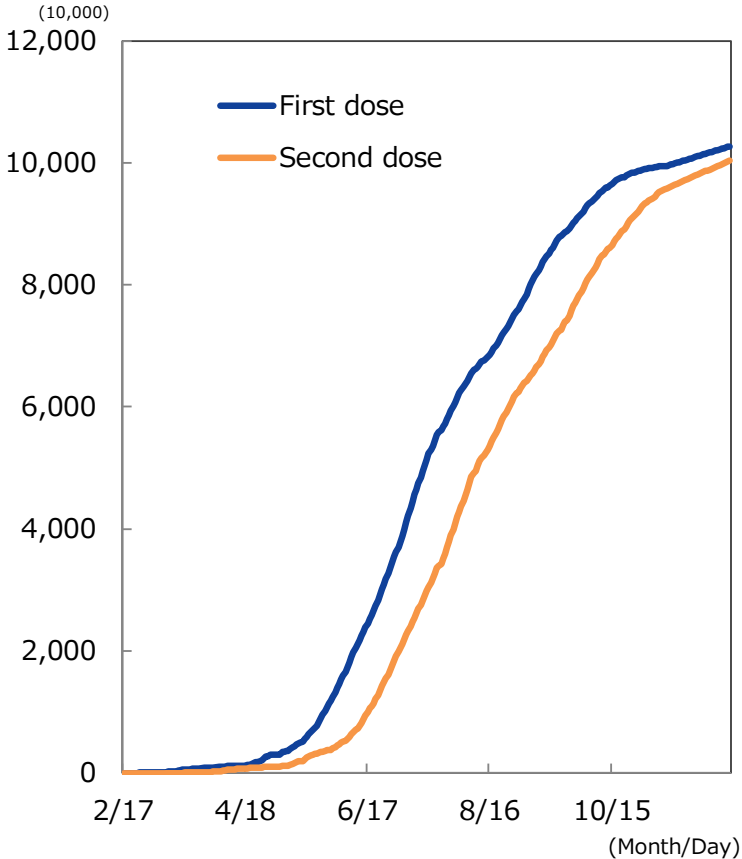
COVID-19 New Cases and Serious Illness

COVID-19 New Cases and Hospitalizations



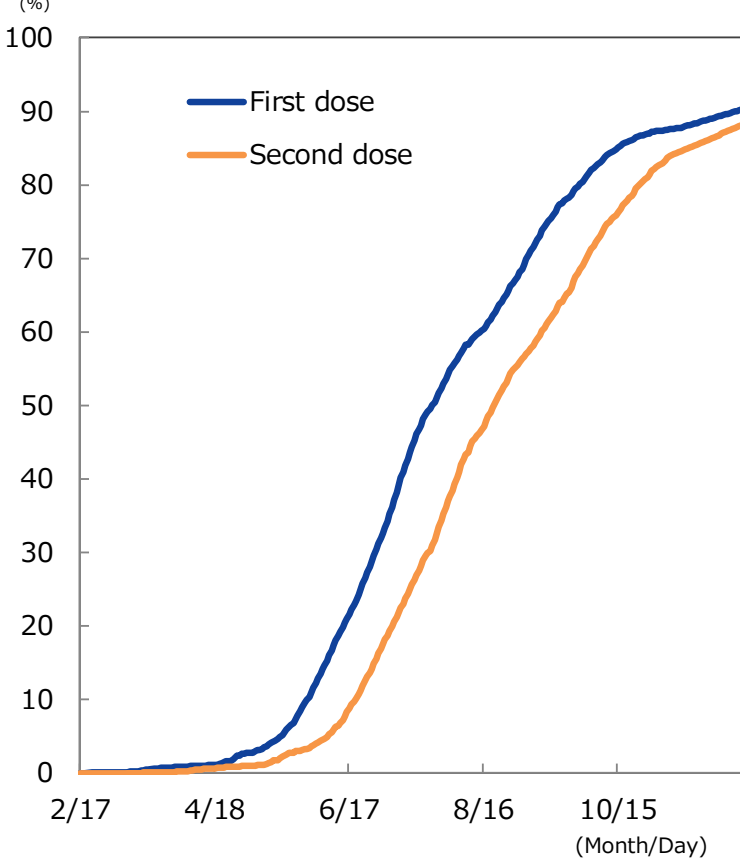
Rapid progress of COVID-19 vaccinations

Cumulative number of vaccinations



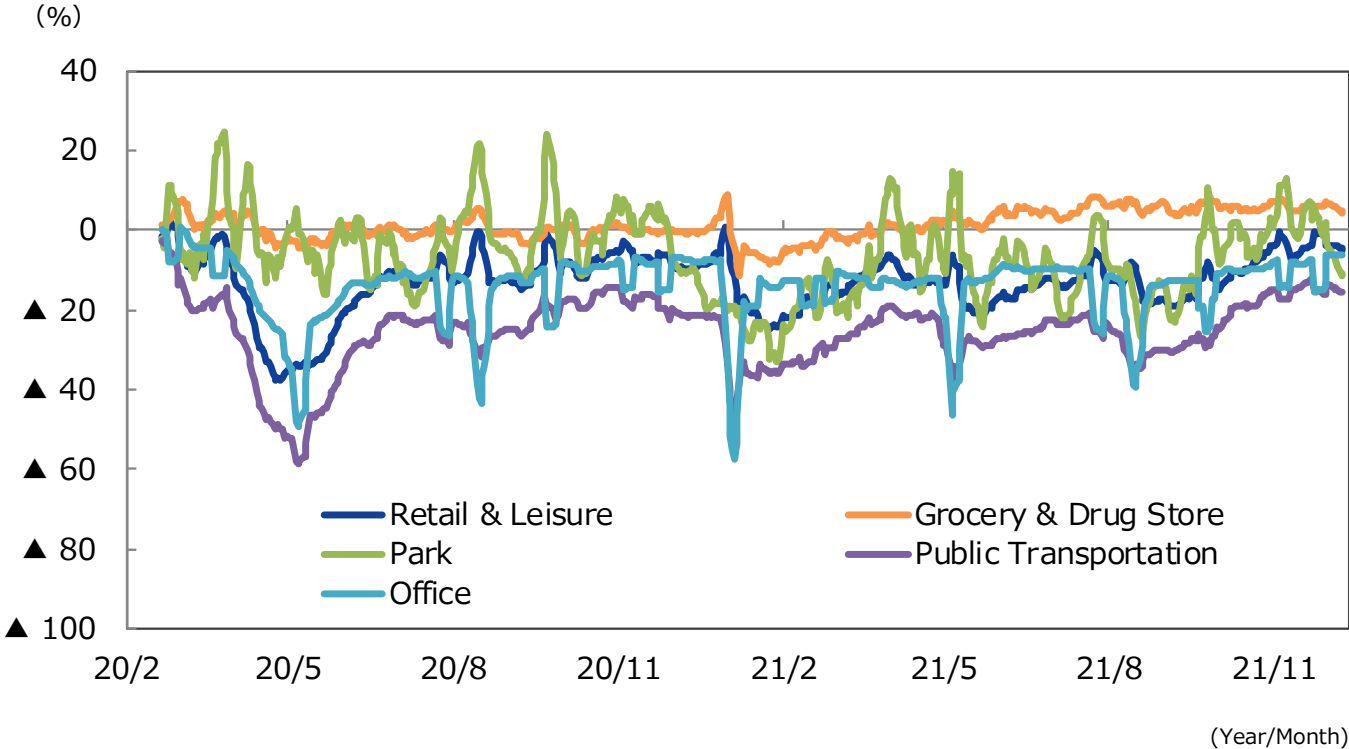
(Data) From Feb. 17th 2021 to Dec. 12th 2021
(Source) MHLW, SMDAM

Total vaccination/population ratio



Mobility levels return except for public transport

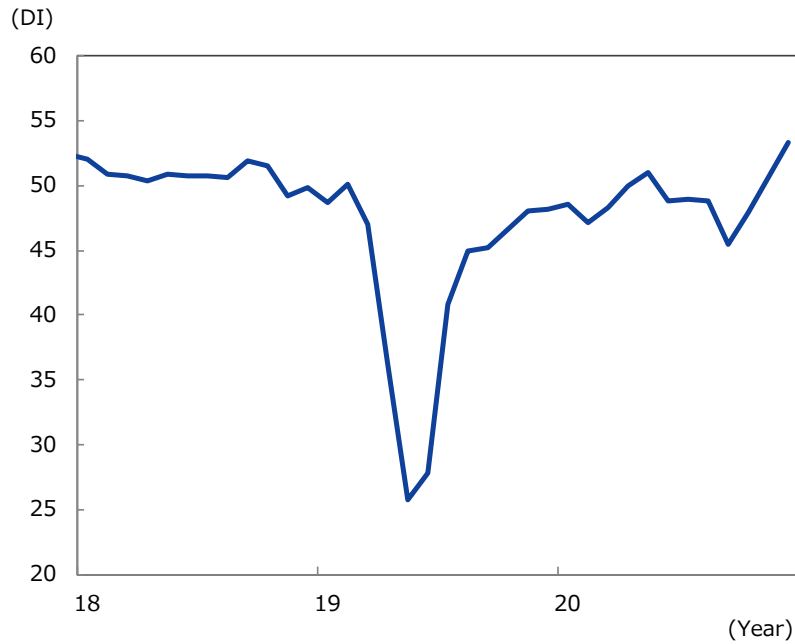
Google Community Mobility Report, Japan



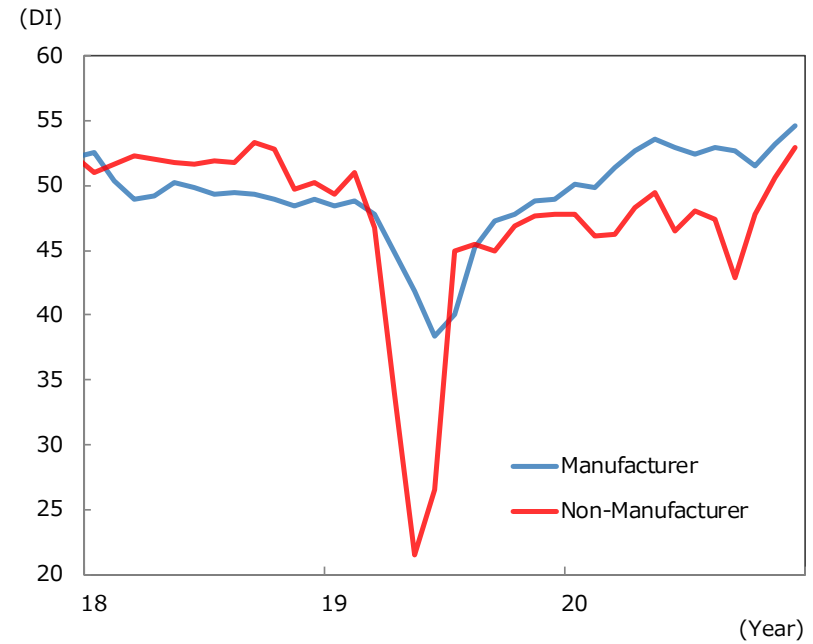
(Data) 7 Days moving average, From Feb. 21st 2020 to Dec. 9th 2021
(Source) Google, SMDAM

PMI, non-manufacturers gradually catching up

Composite PMI



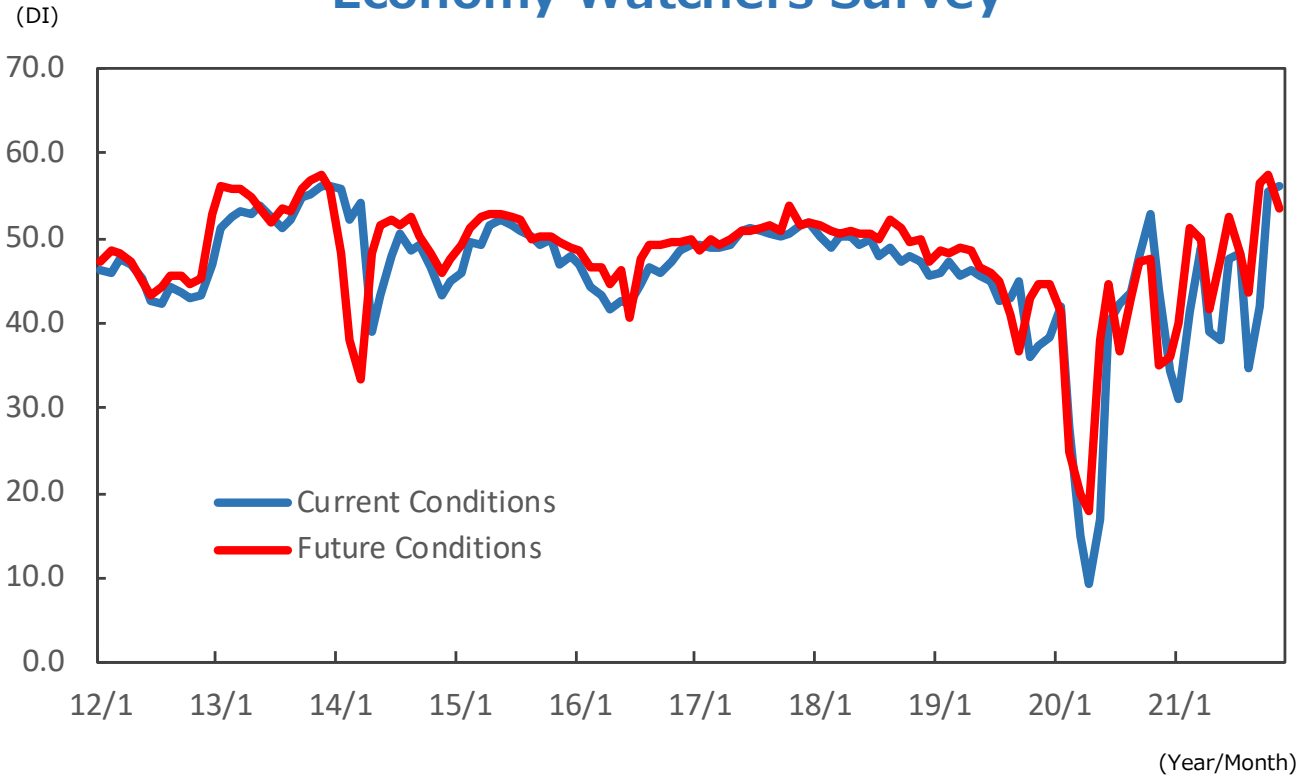
PMI, Manufacturer & Non-Manufacturer



(Data) From Dec. 2018 to Nov. 2021
(Source) Bloomberg, SMDAM

Brighter outlook on consumer activities

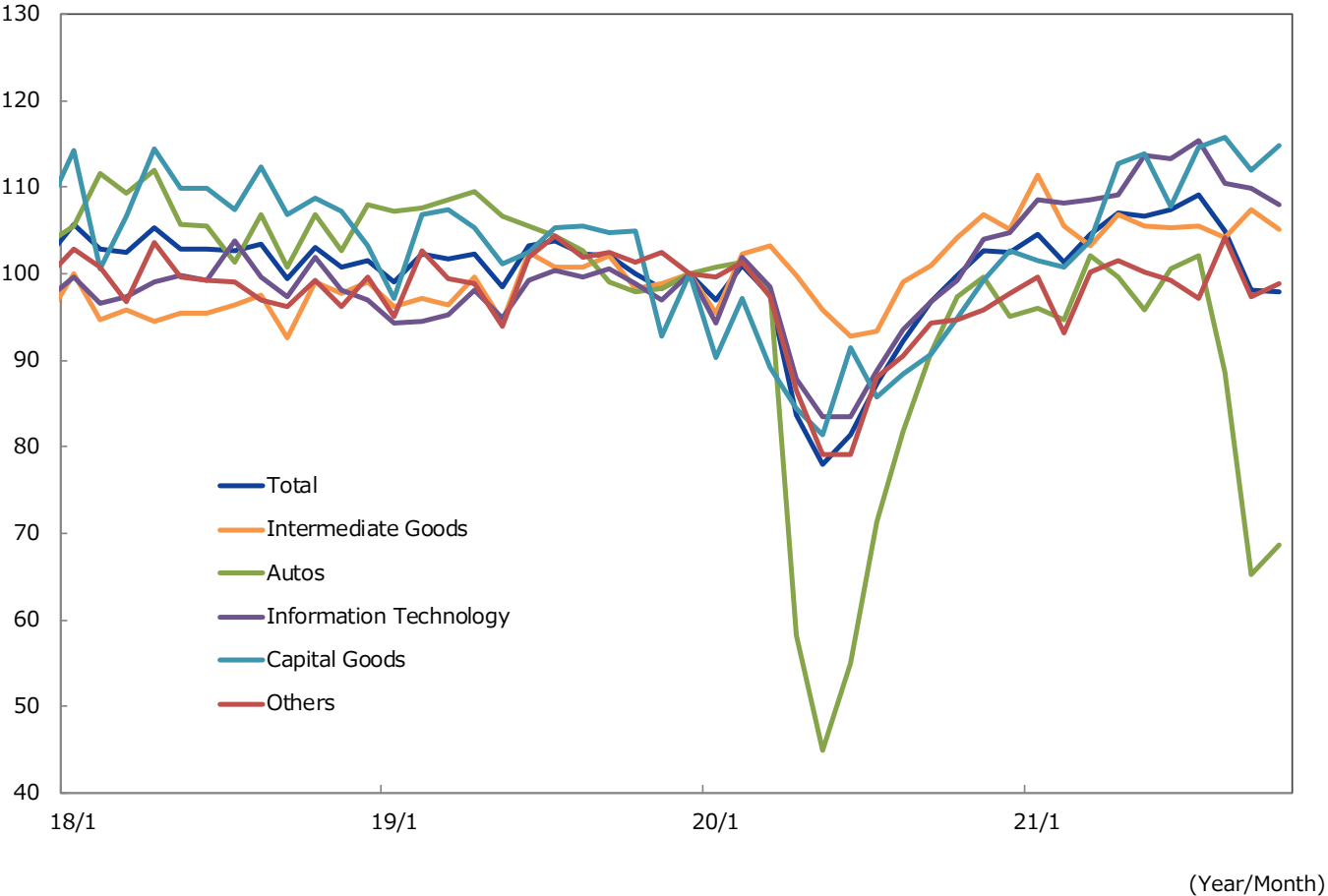
Economy Watchers Survey



(Data) From Jan. 2012 to Nov. 2021
(Source) Cabinet Office, SMDAM

Shortage of semiconductors and parts hits autos

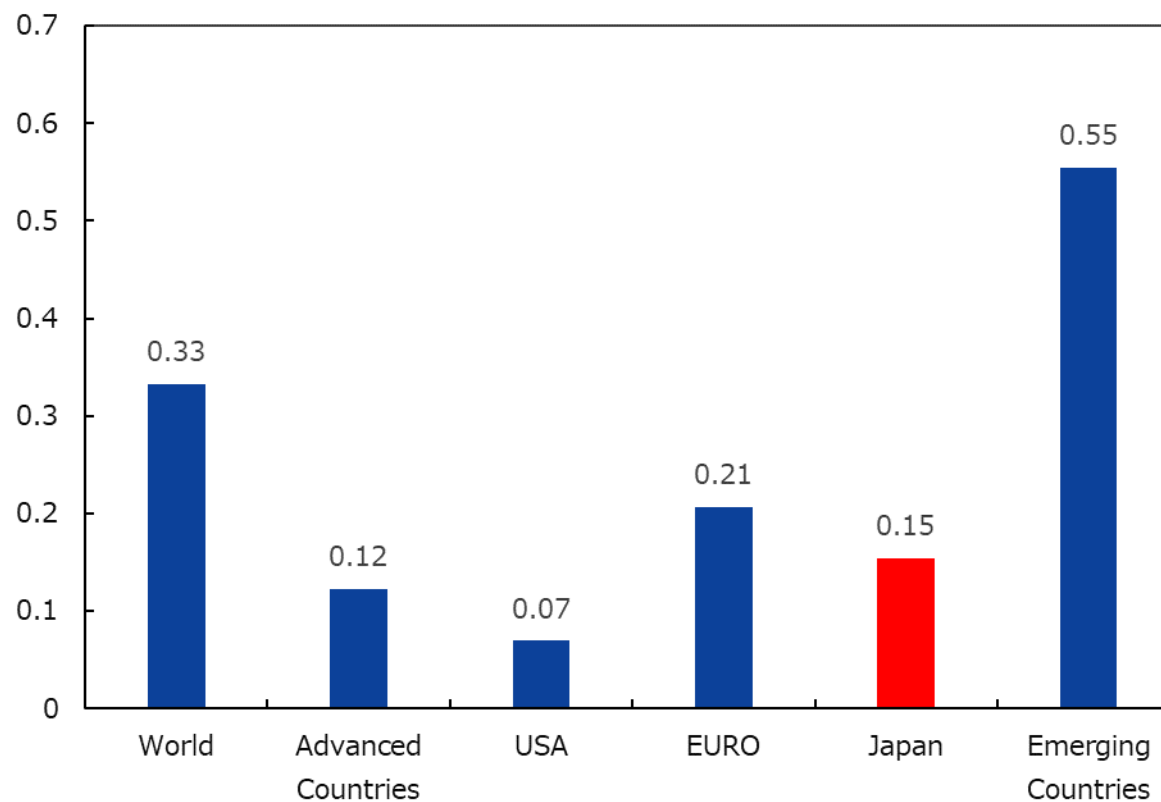
Real Export (Dec. 2019=100)



(Data) From Jan. 2018 to Oct. 2021
(Source) Bank of Japan, SMDAM

Slowing Chinese economy has limited impact on Japan

Elasticity Coefficient to Chinese Industrial Production



(Data) Estimate period is from Jan. 2015 to July 2021
(Source) Centraal Bureau voor de Statistiek, SMDAM

Economic stimulus – larger than anticipated

Size of Economic Stimulus (Trillion Yen)

	Emergency Economic Measures for COVID-19 Infections	Second Supplementary Budget for FY 2020	Comprehensive Economic Measures for People's Lives and Livelihoods	New Economic Measures of PM Kishida Cabinet
Date of Decision	20/04/2020	27/05/2020	08/12/2020	19/11/2021
Size of Stimulus	117.1	117.1	73.6	78.9
Fiscal Spending	48.4	72.7	40.0	55.7
Expenditure of Government	35.8	33.2	32.3	49.7
FILP	12.5	39.3	7.7	6.0

(Source) SMDAM

PM Kishida's economic policy – “growth and distribution”

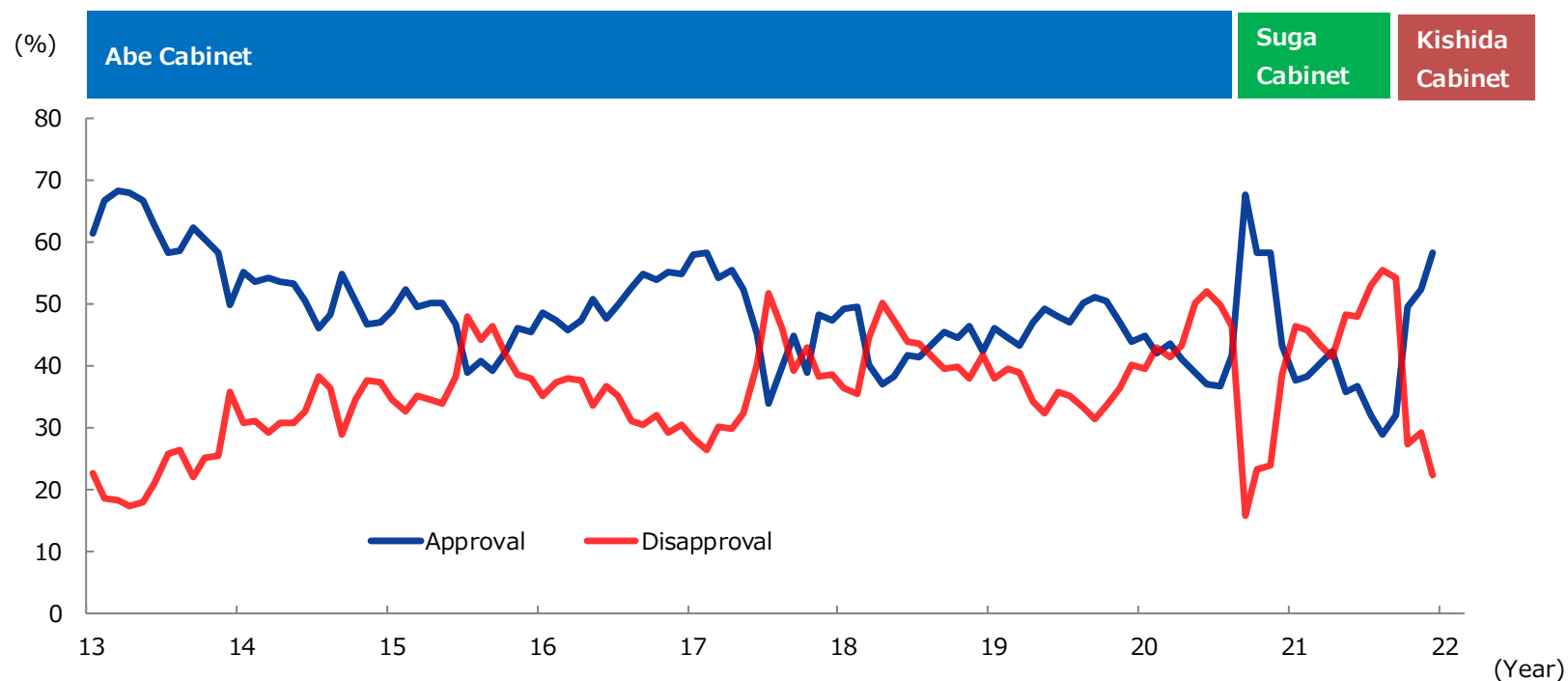
New Leader of Ruling LDP Party and his Economic Policy

Name	Fumio Kishida
Key Biographies	Former Political Chairman of LDP Former Chairman of the Diet Affairs Committee of LDP Former Minister of Defense Former Minister for Foreign Affairs
Faction	Kishida
Slogan	<ul style="list-style-type: none"> ■ New Japanese-style capitalism based on the virtuous cycle of growth and distribution ■ Transformation from Neoliberalism
Orientation of Economic Policy	<ul style="list-style-type: none"> ■ Rectifying Economic Disparities
Economic Policy	<ul style="list-style-type: none"> ■ "Growth Strategy with Four Tactics" <ul style="list-style-type: none"> ▪ Science & Technology Nation ▪ Economical National Security ▪ Digital Rural City-State Vision ▪ Support for Aging Society ■ Income Doubling & Distribution-Oriented Policy

(Source) SMDAM

Approval rate of new PM gaining momentum

Cabinet approval rate

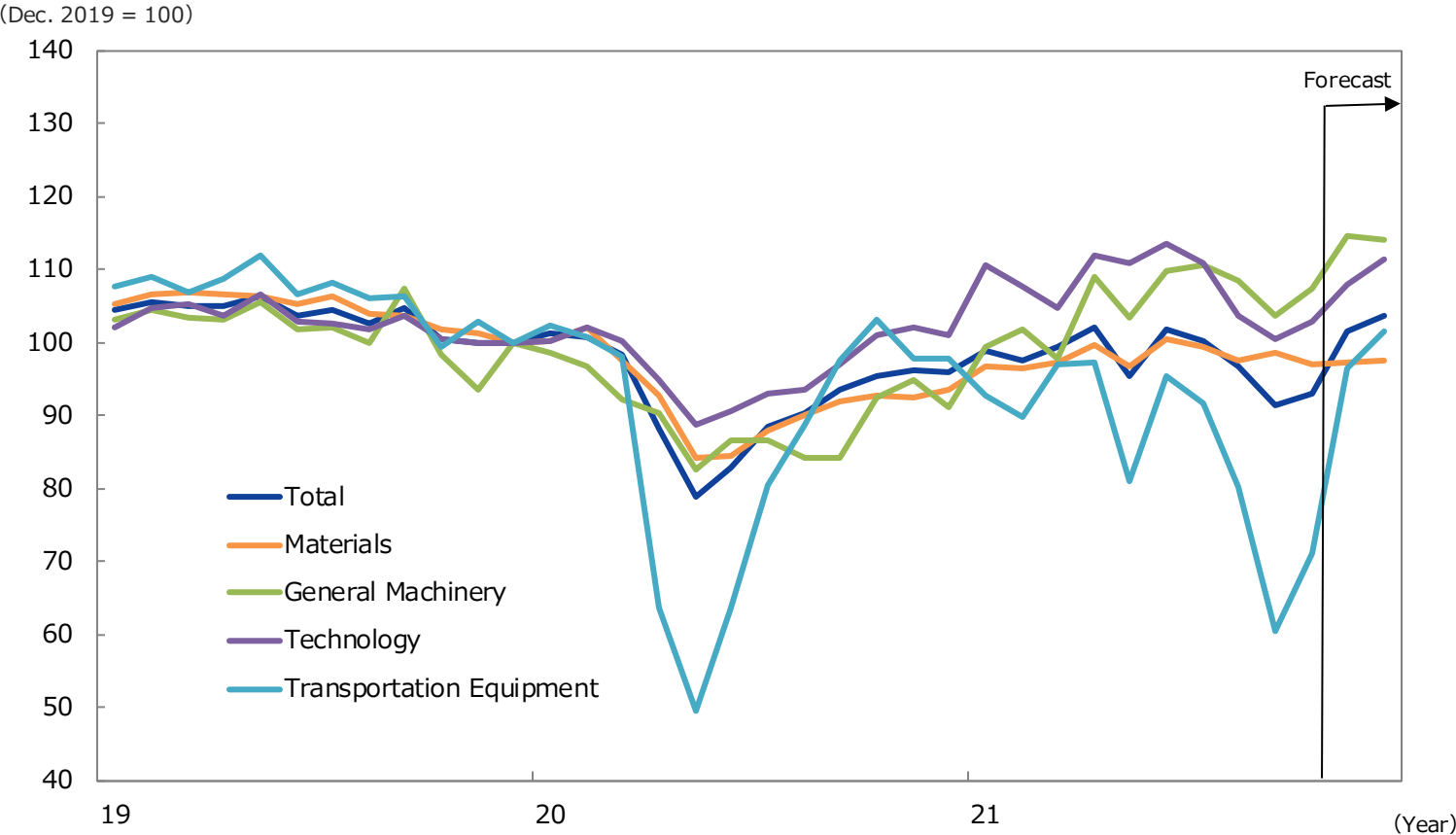


(Data) From Jan. 2013 to Dec. 2021

(Source) NHK, Asahi, Kyodo, Nikkei, Yomiuri, Sankei, Mainichi, Jiji, and SMDAM

Industrial production – autos catching up in the near future

Industrial Production (Monthly)

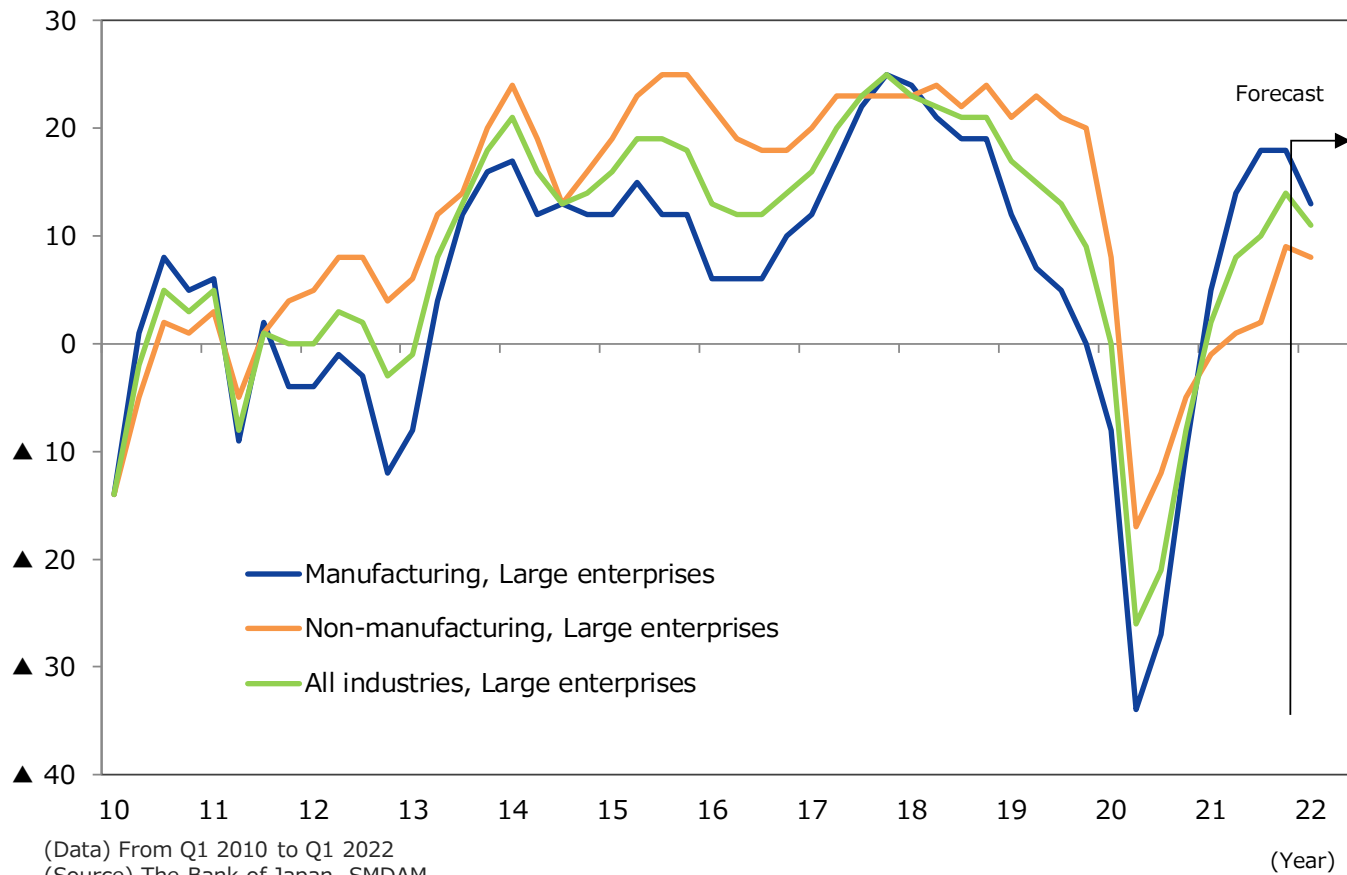


(Data) From Jan. 2019 to Dec. 2021
(Source) METI, SMDAM

Japanese companies see bumpy outlook ahead

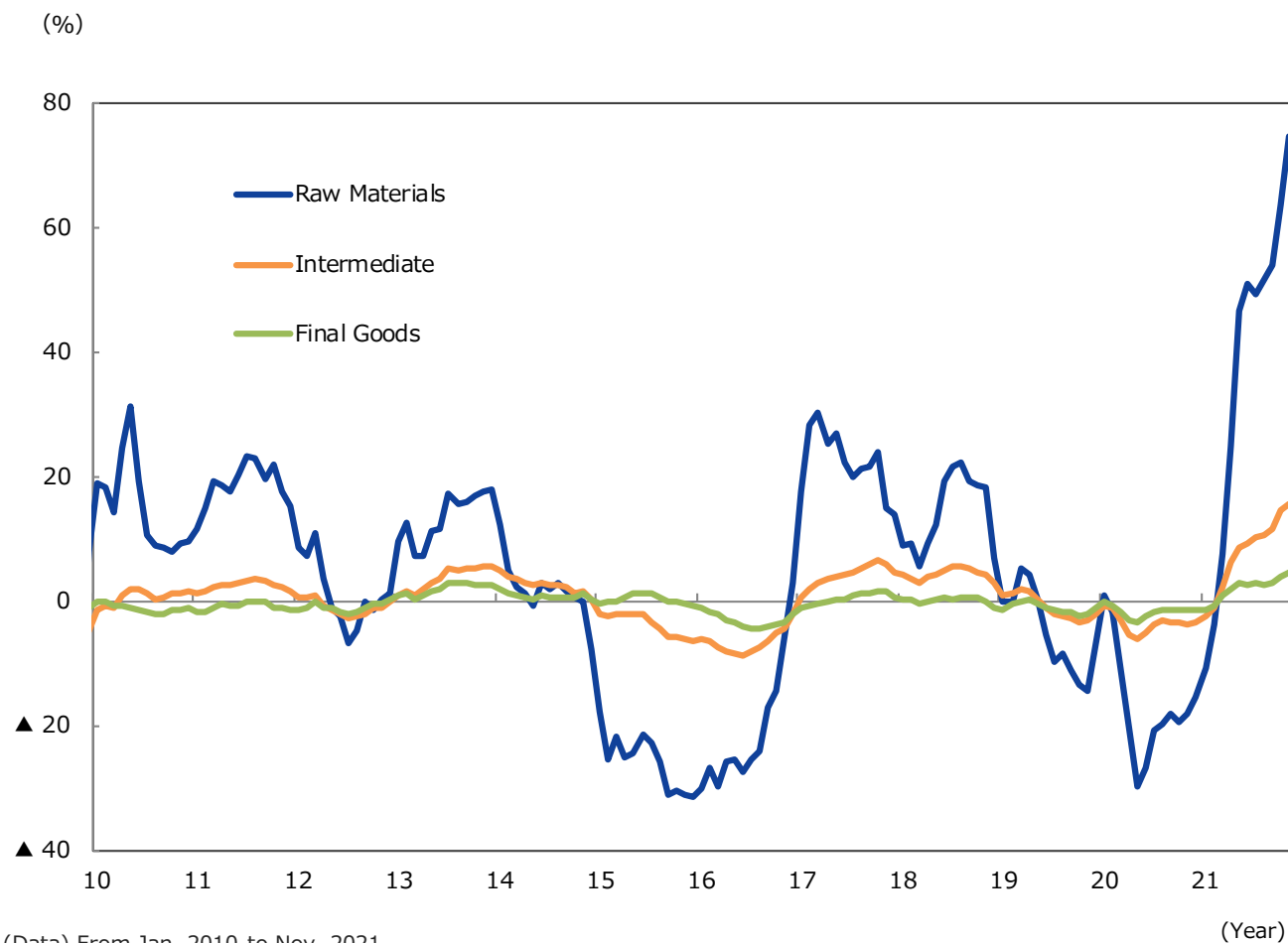
Bank of Japan "Tankan" Economic Survey (Large Enterprises)

(DI, "Good"-"Bad")



Japanese companies face margin squeeze

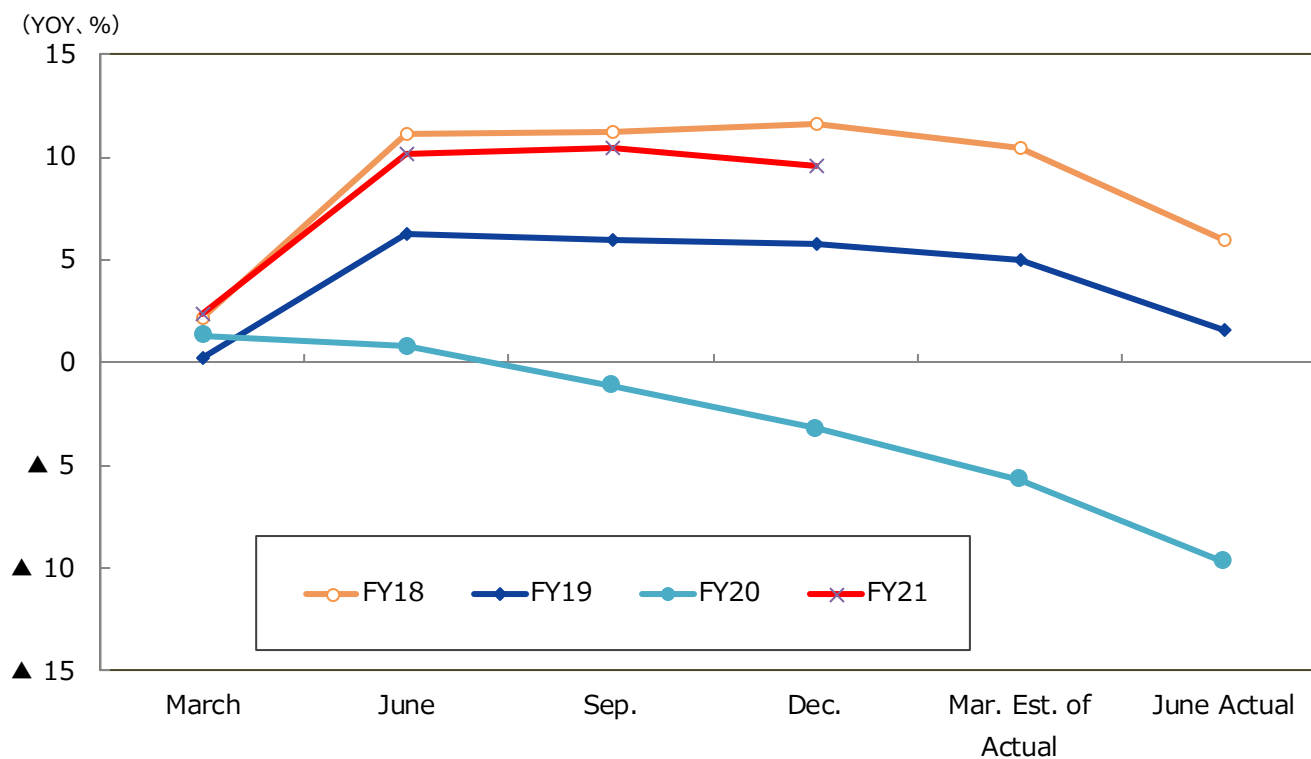
Corporate Price Index (YOY)



(Data) From Jan. 2010 to Nov. 2021
(Source) The Bank of Japan, SMDAM

Japanese companies cut plan of CAPEX slightly

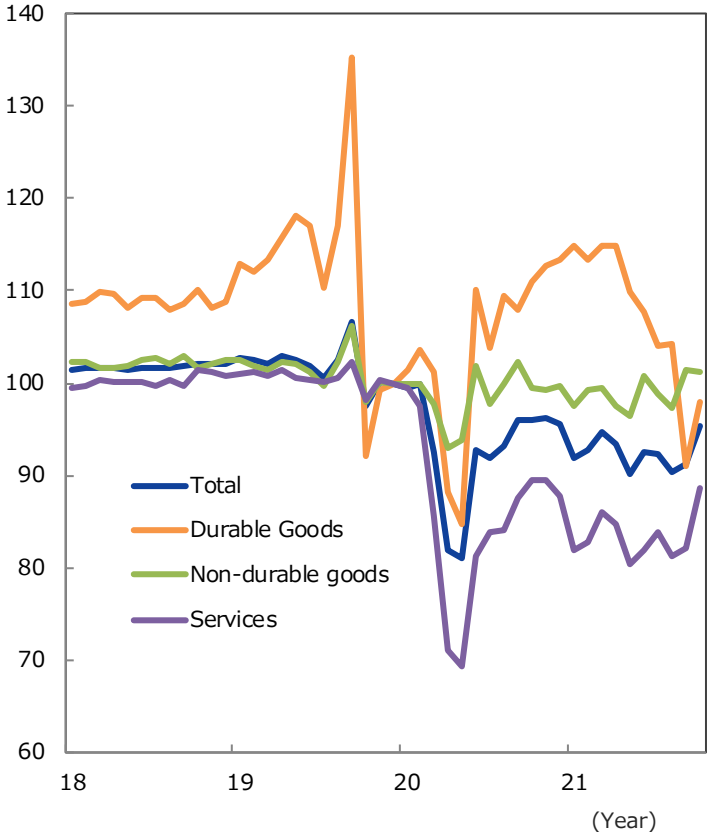
Plan of CAPEX, Inc. Software, Ex. Land and R&D



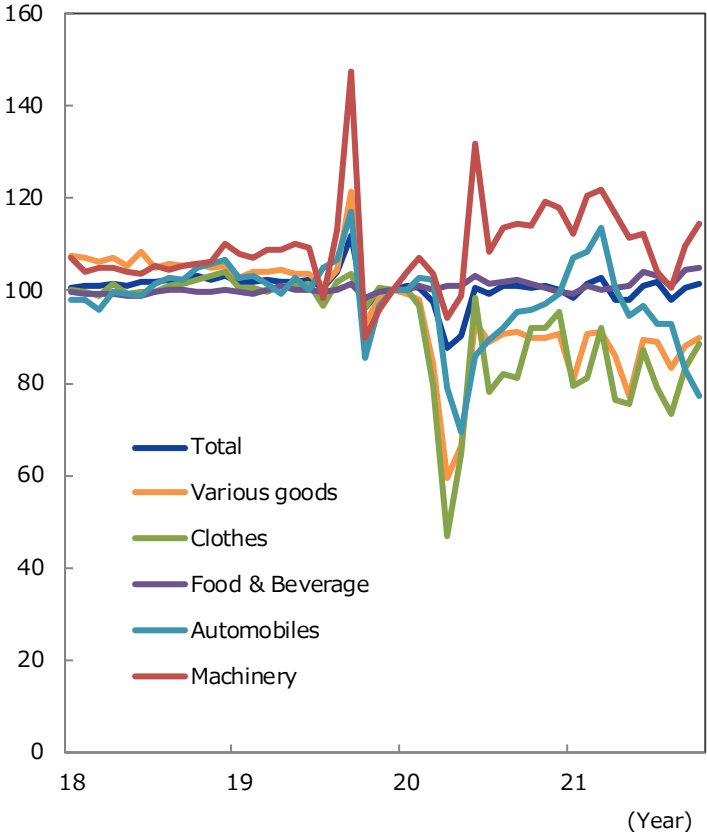
(Source) The Bank of Japan, SMDAM

Shortage of inventory hits auto sales

Consumer Activity Index (Dec. 2019 = 100)



Retail Sales (Dec. 2019 = 100)



(Data) From Jan. 2018 to Dec. 2021
 (Source) BOJ, METI, and SMDAM

Schedule of major events

Schedule of Major Domestic Events			
2022	January	17-18	Monetary Policy Meeting Start of Ordinary Diet Session
	February	15	Release of CY 2021 Q4 GDP
	March	9 17-18	Revision of CY 2021 Q4 GDP Monetary Policy Meeting Establish Initial Budget of FY 2022
	Spring		Release of Grand Design of "New Capitalism Realization Conference"
	April	27-28	Monetary Policy Meeting
	May		
	June	16-17	Monetary Policy Meeting End of Ordinary Diet Session Cabinet Decision on Bold Economic Policy and Growth Strategy G7 Summit
	July	20-21 23 25	Monetary Policy Meeting End of the Term of two members of the BOJ Monetary Policy Committee End of the Term of House of Councilors
	August		
	September	21-22	Monetary Policy Meeting Change of Top Party Officials of LDP
	October	27-28	Monetary Policy Meeting
	November		G20 Summit
	December	19-20	Monetary Policy Meeting Outline of Tax Reform of FY 2023 Cabinet Decision on the Budget of FY 2023

(Source) Compiled by Sumitomo Mitsui DS Asset Management Co., Ltd.

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