



# Outlook for Japanese Stock Market & Economy

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Sumitomo Mitsui DS Asset Management

-May 2021-



# Outlook for Japanese Stock Market

# Market Outlook

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- We believe the Japanese stock market will continue its upward trend over the next twelve months supported by strong earnings recovery in FY2021 and FY2022.
- Our TOPIX target for CY2021 is 2,130 with EPS 125 x PER 17.
- Market drivers will shift from multiple expansion to earnings growth due to normalization of the economy.
- Despite strong fundamentals, upside is limited in the short term due to concerns over monetary policy, delays in the vaccination roll-out and investors' excessive expectations regarding the earnings recovery.
- We expect the market will resume its bullish trend at the quarterly announcement in July/August after confirming earnings results of Q1 FY 2021 and continue its strong recovery going forward.

# TOPIX Index and Forecast



Note: TOPIX data is from Jan. 1st 2016 to April 23rd 2021.

Our forecast is as of April 19<sup>th</sup> and may change without notice.

(Source) TOPIX: Tokyo Stock Exchange, Forecast by SMDAM

(Year/Month)

# Upside / Downside Risk

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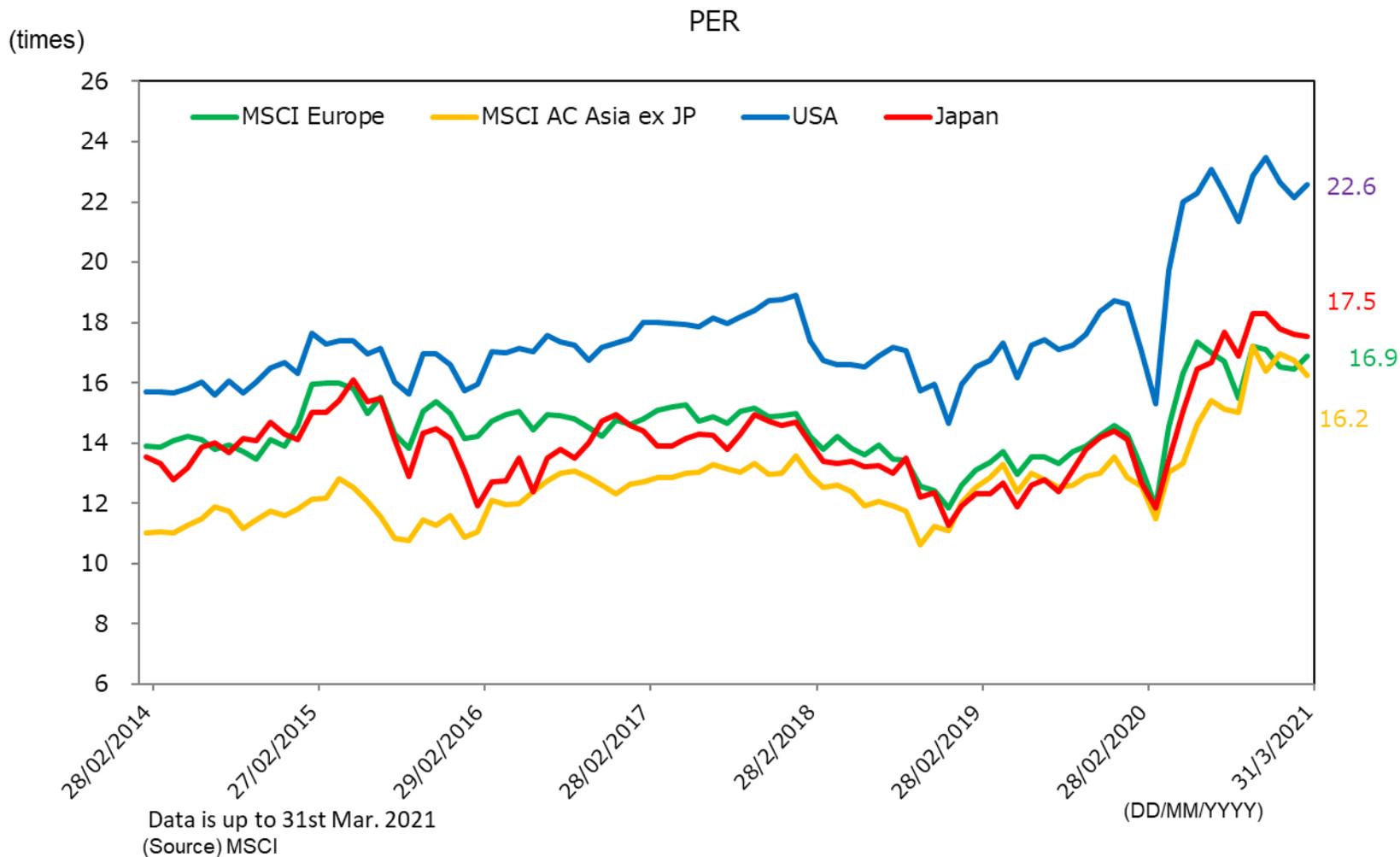
## ■ Upside Risks

- Early elimination of COVID-19, progress of vaccinations
- Easing of tensions between the US and China
- Decisive action by the government to tackle COVID-19
- Weak Japanese Yen

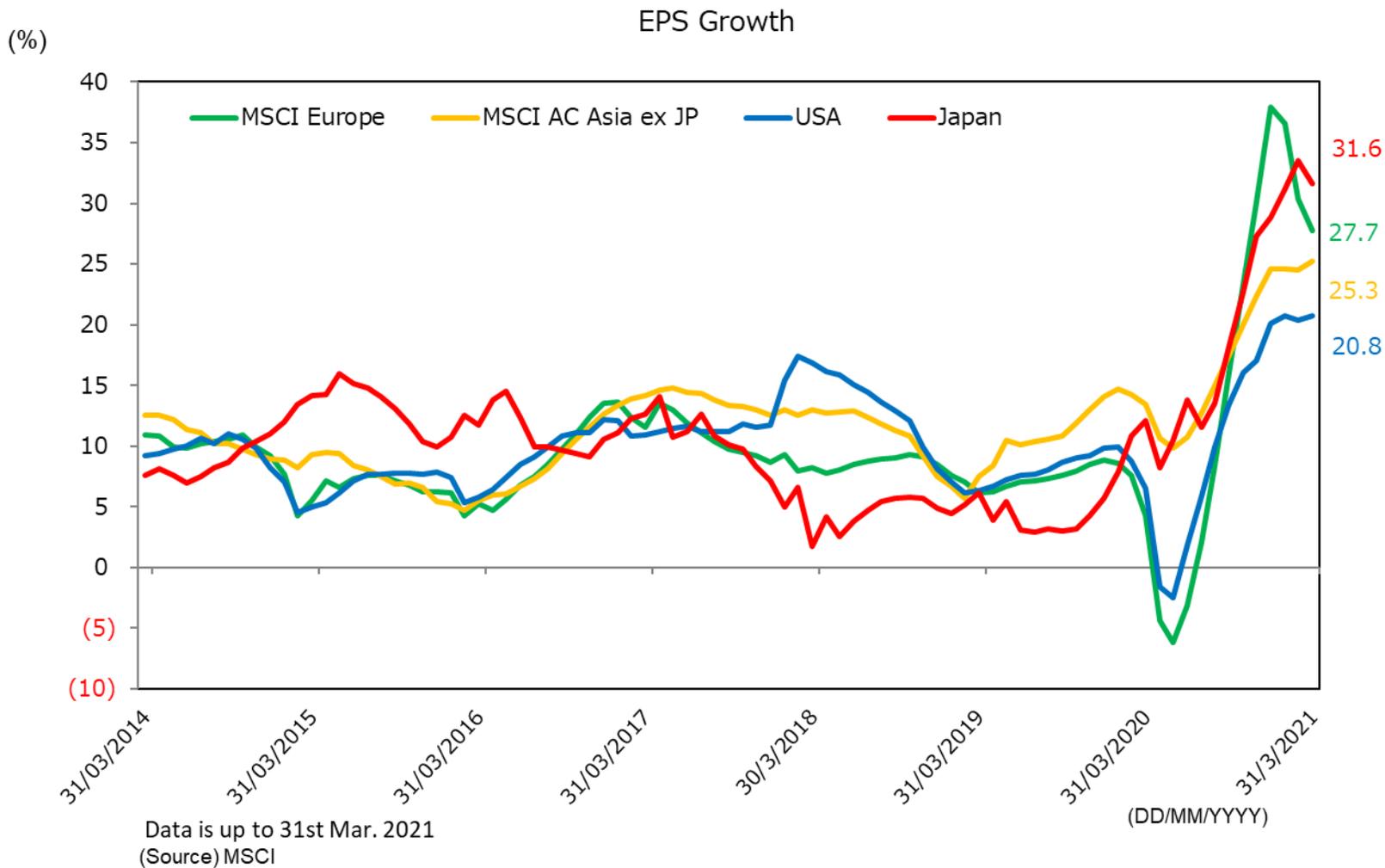
## ■ Downside Risks

- Worsening COVID-19 infections, including the spread of new variants
- Concern for the sustainability of current monetary policy and fiscal spending
- Spike in interest rates with higher inflation
- Worsening diplomatic relations between Japan and China

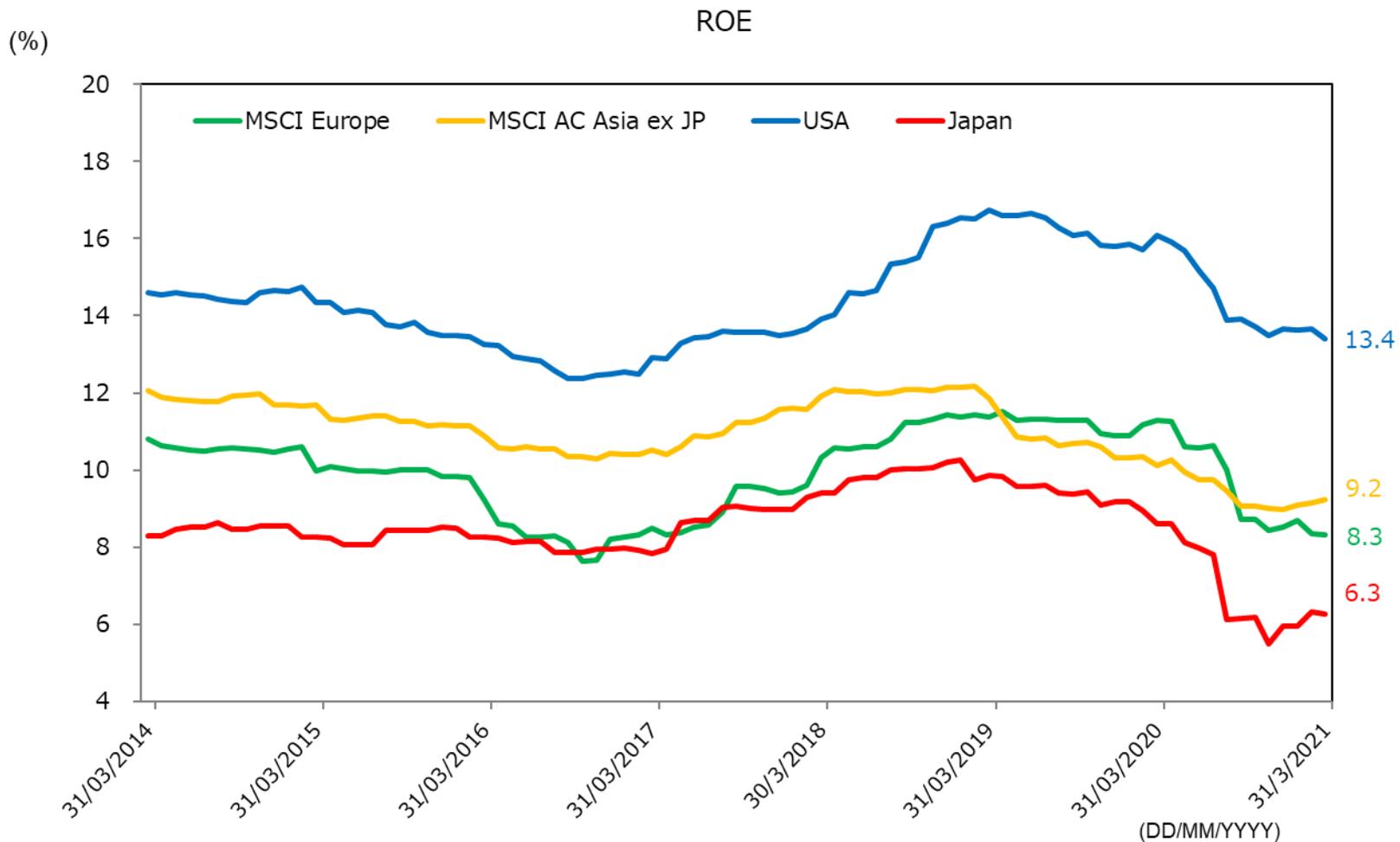
# Global Comparison of Key Valuations: PER



# Global Comparison of Key Valuations: EPS Growth



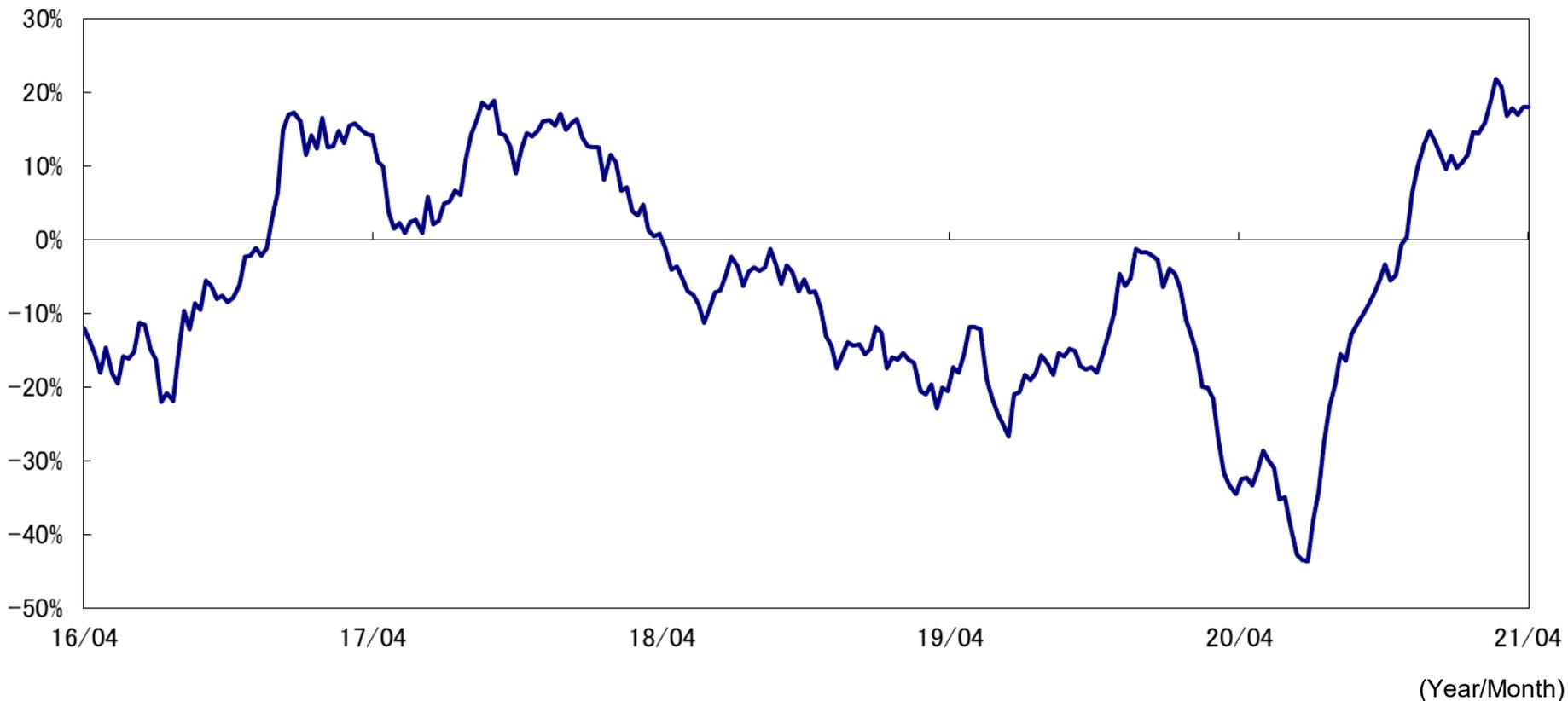
# Global Comparison of Key Valuations: ROE



Data is up to 31st Mar. 2021  
(Source) MSCI

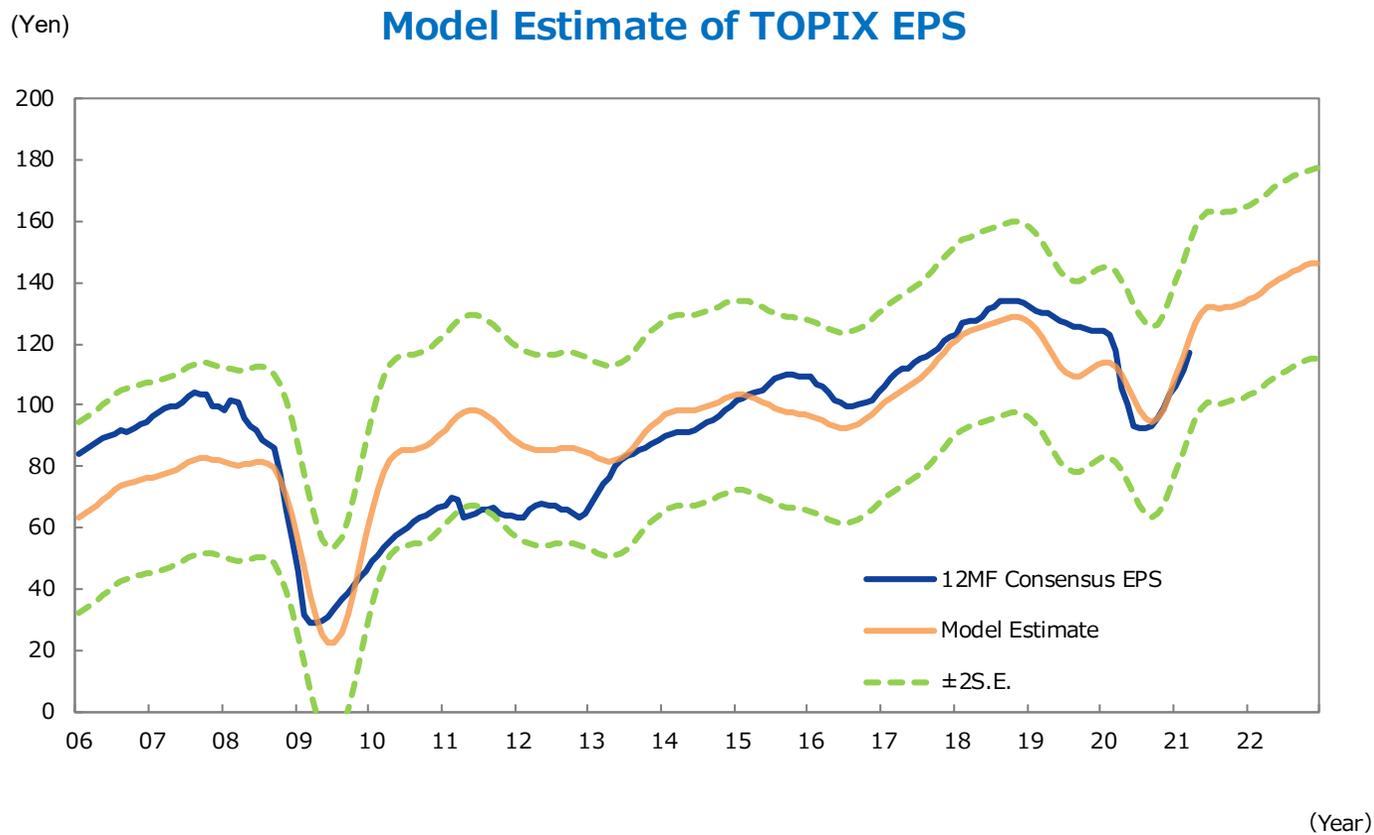
# Revision of Earnings Forecasts

TOPIX Revision Index



Data is from 12th Apr. 2016 to 13th Apr. 2021  
(Source) Datastream, IBES

# Top Down Approach, Model Implied Fair Value

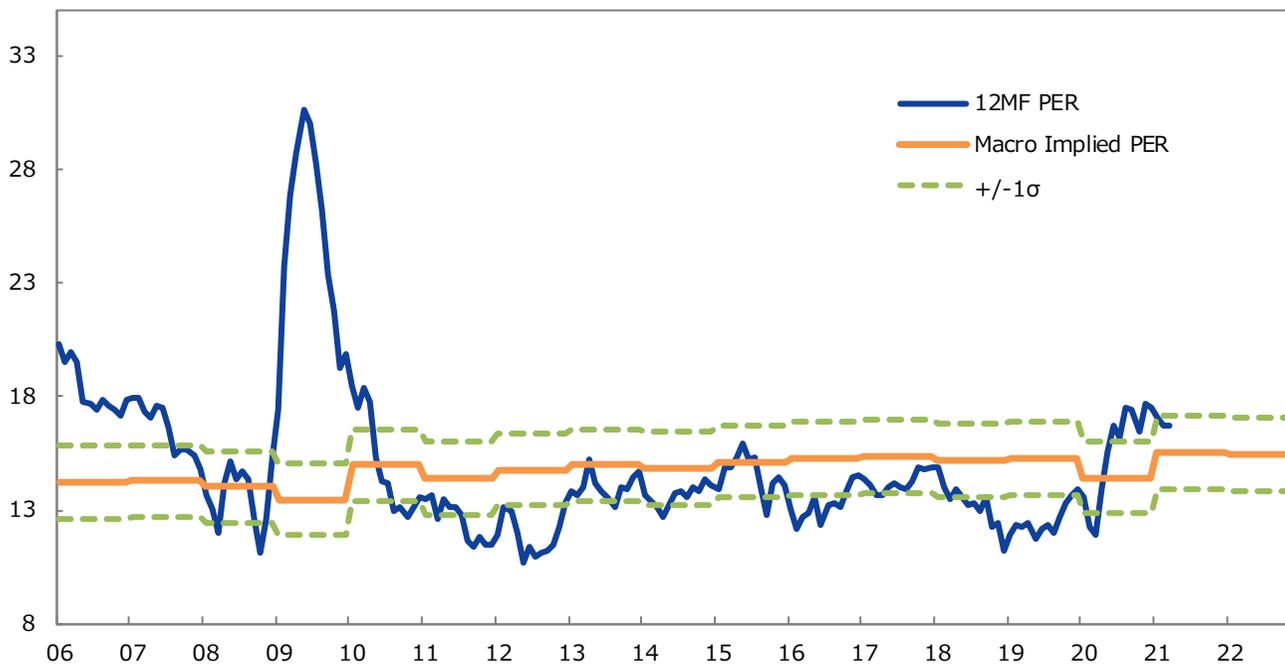


Consensus data is from Jan. 2006 to Feb. 2021, Model data is from Jan. 2006 to Dec. 2022.  
(Source) SMDAM

# Top Down Approach, Model Implied Fair Value

(Times)

## Macro Implied TOPIX PER



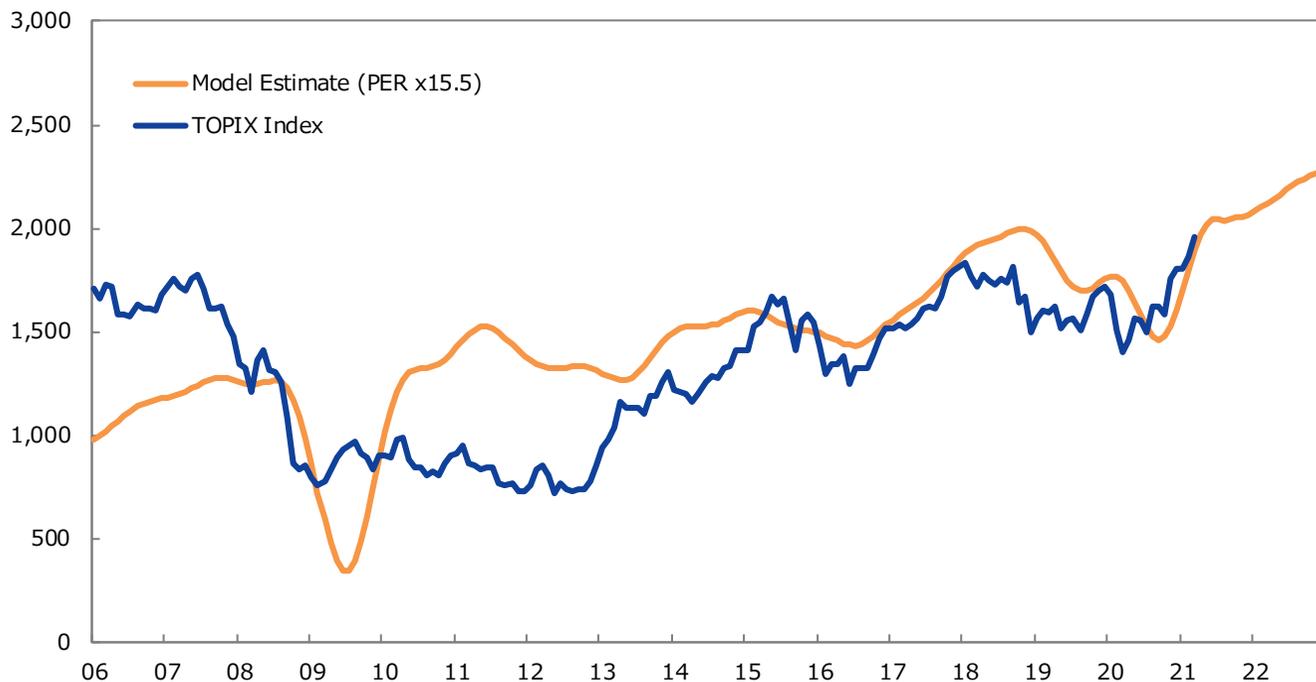
(Year)

12MF PER data is from Jan. 2006 to Feb. 2021, Model data is from Jan. 2006 to Dec. 2022.

(Source) SMDAM

# Top Down Approach, Model Implied Fair Value

## Model Estimate of TOPIX Fair Value



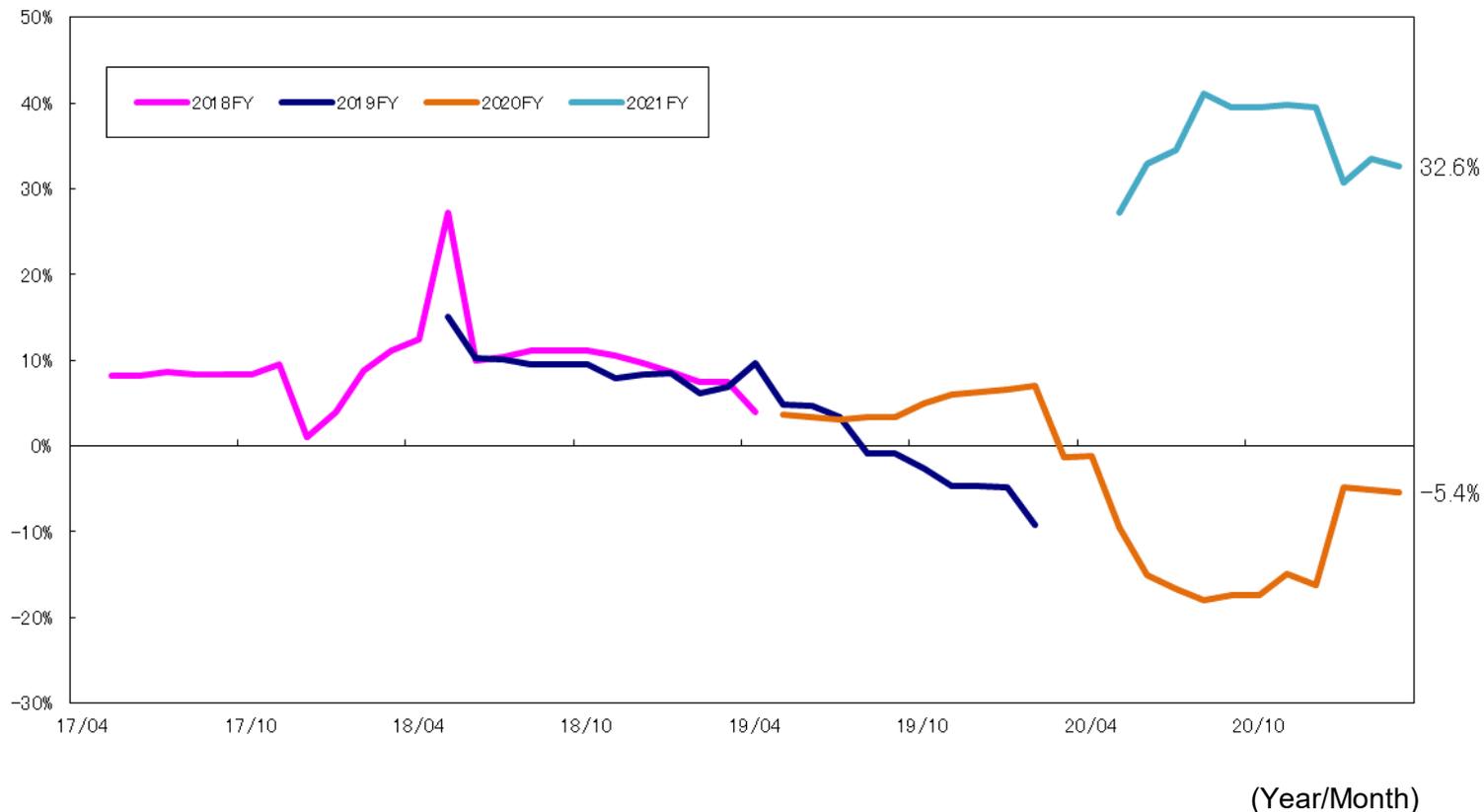
(Year)

TOPIX data is from Jan. 2006 to Feb. 2021, Model data is from Jan. 2006 to Dec. 2022.

(Source) SMDAM

# Bottom Up Estimate, Corporate Earnings

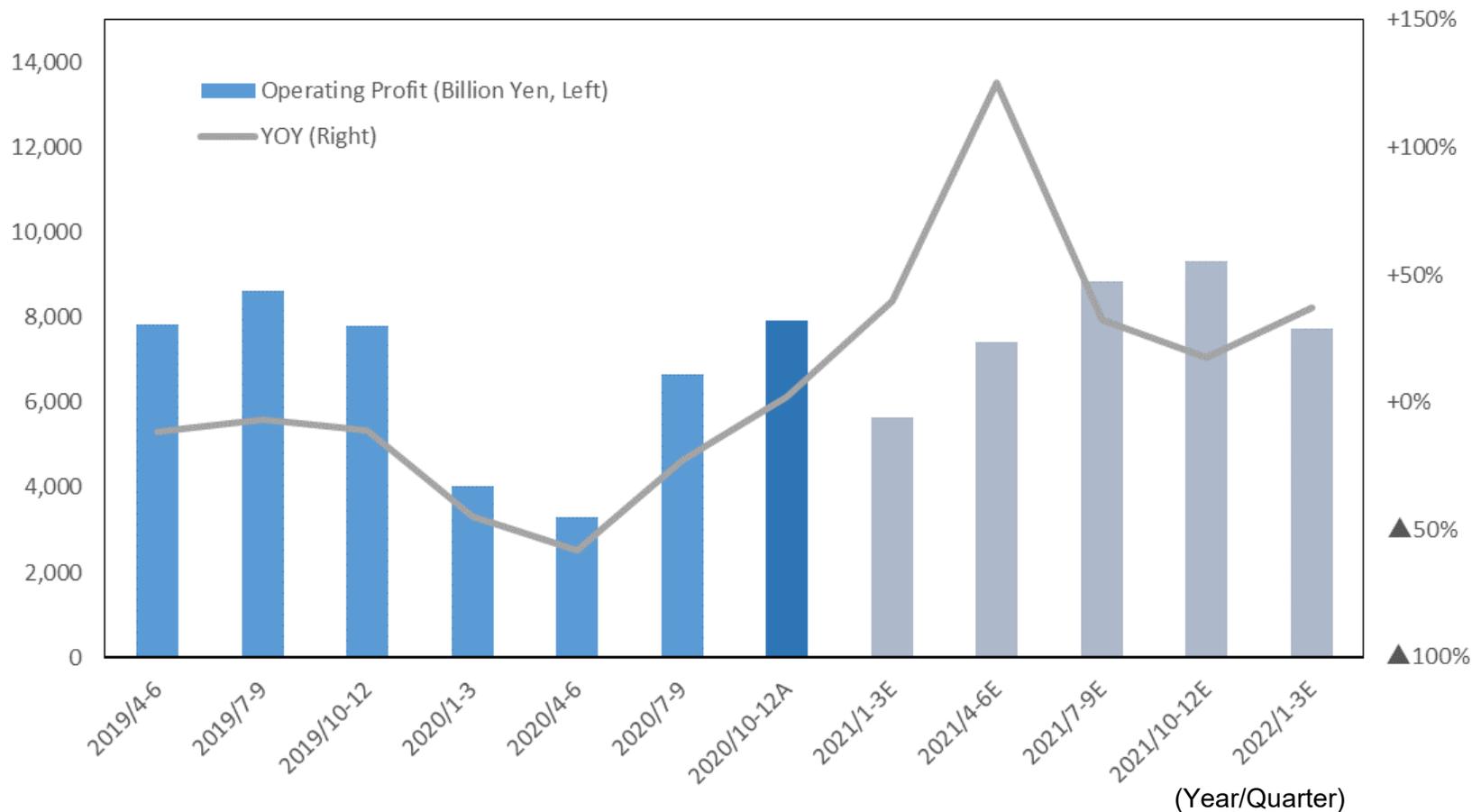
SMDAM Core Research Universe (Ex-Financial) Est. of Recuring Profit Growth



Note: ~~SMAD~~**SMDAM** Core Universe consists of 488 major Japanese companies covered by SMADM in-house analysts.  
 (Source) SMDAM

# Bottom Up Estimate, Corporate Earnings

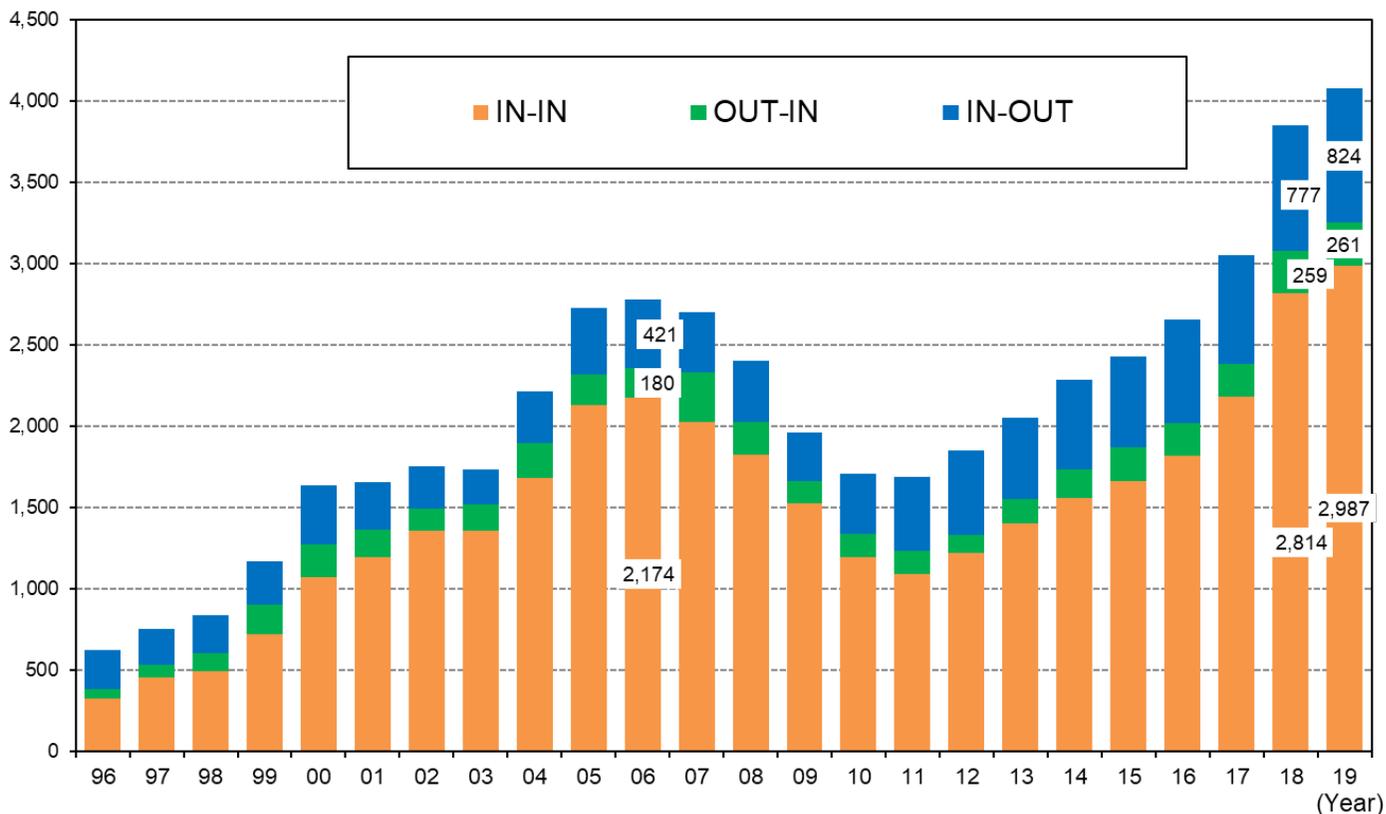
Operating Profit (All Industries ex-financials and Softbank Group)



(Source) SMDAM

# Merger and Acquisitions

Number of M&A deals involving Japanese companies  
(Excluding transactions among the same business group)



Note: IN-IN means Japanese company acquiring Japanese one, OUT-IN is for Non-Japanese company acquiring Japanese company, and IN-OUT is for Japanese company acquiring non-Japanese company.  
(Source) RECOF and SMBC NIKKO Securities.

# Corporate Governance Code and Stewardship Code

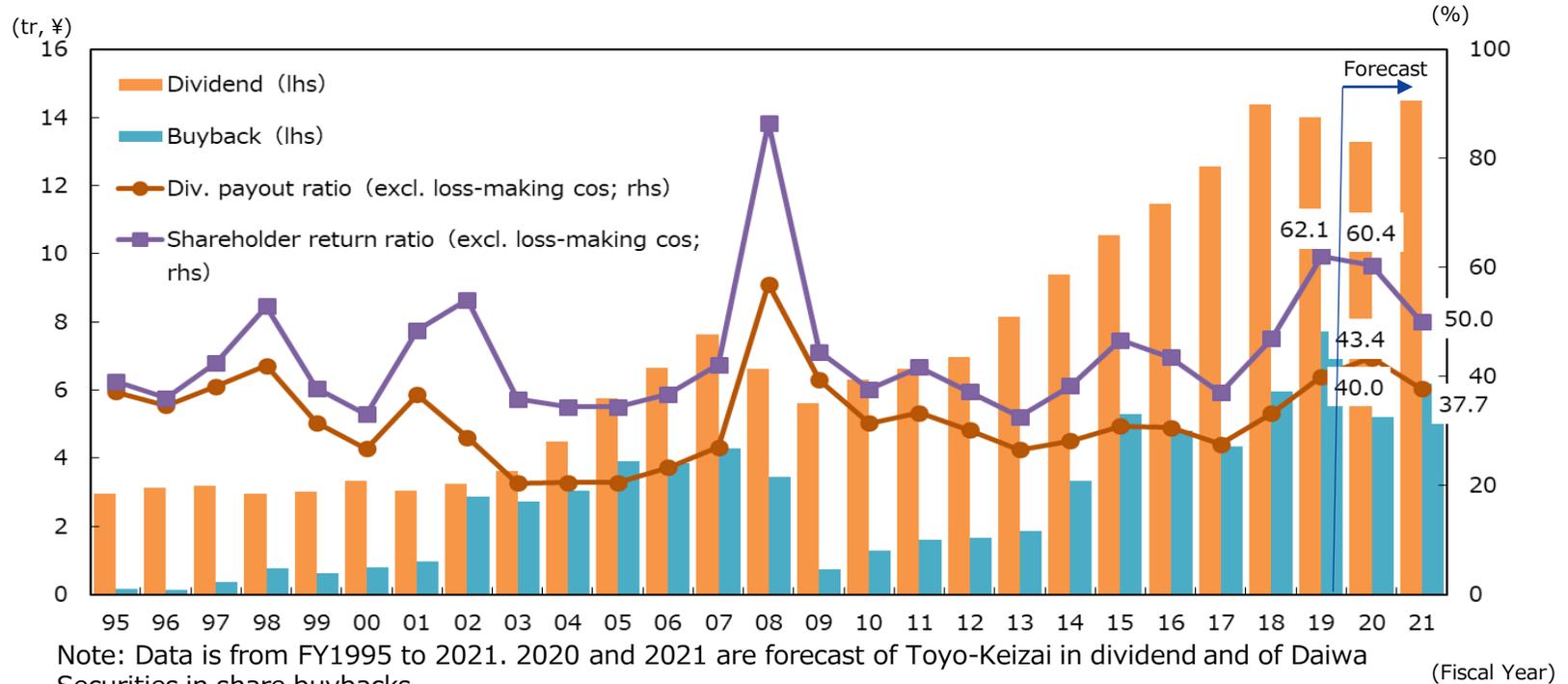
Total number of institutional investors, which publicly declared acceptance of the stewardship code	
Trust banks	6
Investment management companies	191
Insurance companies	23
Pension funds	53
Others (include proxy voting advising companies)	7
Total	280

Note: As of 13th Mar. 2020.  
(Source) Financial Services Agency

- The Stewardship Code (SC) was set in February 2014. Investors are taking a more pro-active approach in talking to the companies and exercising proxy voting rights. The Financial Services Agency discloses the name of institutional investors which publicly accept the SC.
- After the inception of the Corporate Governance Code (CGC) in June 2015, pressure has been increasing on companies to improve its 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 the 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.

# Shareholder Returns, Buybacks and Dividends

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



# Winners and Losers

## 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	3.58	18.88	6.42	35.94	19.49	9.42	39.33
Total Value	7.67	20.14	11.44	32.32	5.05	-4.60	20.81
Top Cap Value	8.15	22.89	12.43	34.58	11.30	2.33	25.56
Large Cap Value	7.79	21.50	12.10	33.22	5.13	-3.20	20.04
Mid Cap Value	7.35	19.66	11.69	31.47	-3.84	-11.34	11.92
Small Cap Value	7.11	14.23	8.52	28.30	4.67	-10.77	23.53
Micro Cap Value	4.62	10.44	5.81	22.66	3.87	-12.26	26.59
Total Growth	-1.46	16.15	1.38	37.12	32.81	26.39	55.26
Top Cap Growth	-1.64	21.01	1.88	38.92	38.00	34.21	61.21
Large Cap Growth	-1.73	17.22	1.24	37.53	34.83	29.13	56.66
Mid Cap Growth	-1.87	11.44	0.19	35.10	29.83	21.43	49.67
Small Cap Growth	1.35	7.15	2.80	33.23	16.94	6.51	42.76
Micro Cap Growth	2.34	8.81	5.15	39.38	22.37	11.00	52.45
Top Cap Total	2.68	21.96	6.53	37.12	24.95	18.25	43.15
Large Cap Total	2.80	19.52	6.38	36.18	20.72	13.40	38.72
Mid Cap Total	2.97	16.00	6.18	35.05	14.66	6.51	32.52
Small Cap Total	5.10	12.37	6.66	31.28	10.27	-4.64	33.85
Micro Cap Total	3.93	9.83	5.62	28.67	10.41	-4.04	36.31

Note : As of April 23rd 2021  
(Source) Bloomberg



# Outlook for Japanese Economy

# [Japanese economy] Summary

## Current Status and Prospects of the Japanese Economy

### [outlook]

- ① **The forecast for real GDP is -5.0% (previously -5.1%) in FY2020, +4.2% (+4.6%) in FY2021, and +2.1% (+2.1%) in FY2022.** In fiscal 21, the revised downward revision of FY2021 was made on the grounds of reduced automobile production due to a fire at the Renesas chip factory and the spread of the novel coronavirus. These downward pressures are likely to reach Q2 21. Concerning the former, however, production prospects in other industries are bullish, and the company expects to absorb some of the negative effects of reduced automobile production. With regard to the latter, it is assumed that the focus of infection countermeasures will be the shortening of operating hours for restaurants in a limited area, and that no strict restrictions on wide-area economic activities are imposed. Based on these factors, we maintain our view that growth will turn positive in Q2 21. In and after the third quarter of 21, the Japanese economy is expected to continue to show positive growth on the back of a recovery in external demand, the spread of vaccines and the recovery of automobile production.
- ② **The nationwide core CPI outlook (excluding effects of the consumption tax hike and free education) is -0.5% (previously -0.5%) in FY2020, +0.3% (+0.6%) in FY2021 and +0.5% (+0.5%) in FY2022.** Reflecting the impact of online-only plans by mobile phone carriers, we revised down the fiscal 21 forecast. While the reduction in cell phone charges and the resumption of the Go To Travel campaign are pushing prices down, core CPI is expected to turn positive due to energy initiatives. However, the supply-demand balance is moderate, and the underlying inflationary pressure is likely to be limited.
- ③ **The overall monetary policy framework is likely to be maintained for the time being. The central bank expects negative interest rates to be cut further only in emergencies, such as a sharp rise in the yen.** In the "Review to implement more effective and sustainable monetary easing" the Bank of Japan has announced measures to deal with side effects, such as more flexible purchasing policies for ETFs and J-REITs and clarification of the range of fluctuations in long-term interest rates. The Bank of Japan has established a new interest rate system to promote loans and has made it clear that there is room for interest rate cuts. The deadline for companies to take financial measures is September 21, but financial conditions for accommodations, restaurants and other services remain tight. If the situation continues, the measures are likely to be extended.
- ④ **The current economic outlook is not based on the assumption of large-scale additional economic measures, but caution is needed as an upside risk.** The possibility of a supplementary budget for fiscal 21 is drawing more attention in the wake of the expected dissolution of the general election and the spread of the novel coronavirus.
- ⑤ **The main scenario is continuation of economy-friendly fiscal and monetary policy management.** Prime Minister Suga has called for the continuation of Abenomics, and policy management is generally in line with this. Even if the administration of Prime Minister Suga ends up with a short life span, it is likely that the government will continue its economy-friendly policies until the coronavirus outbreak is under control.

# Japan Economy Forecast

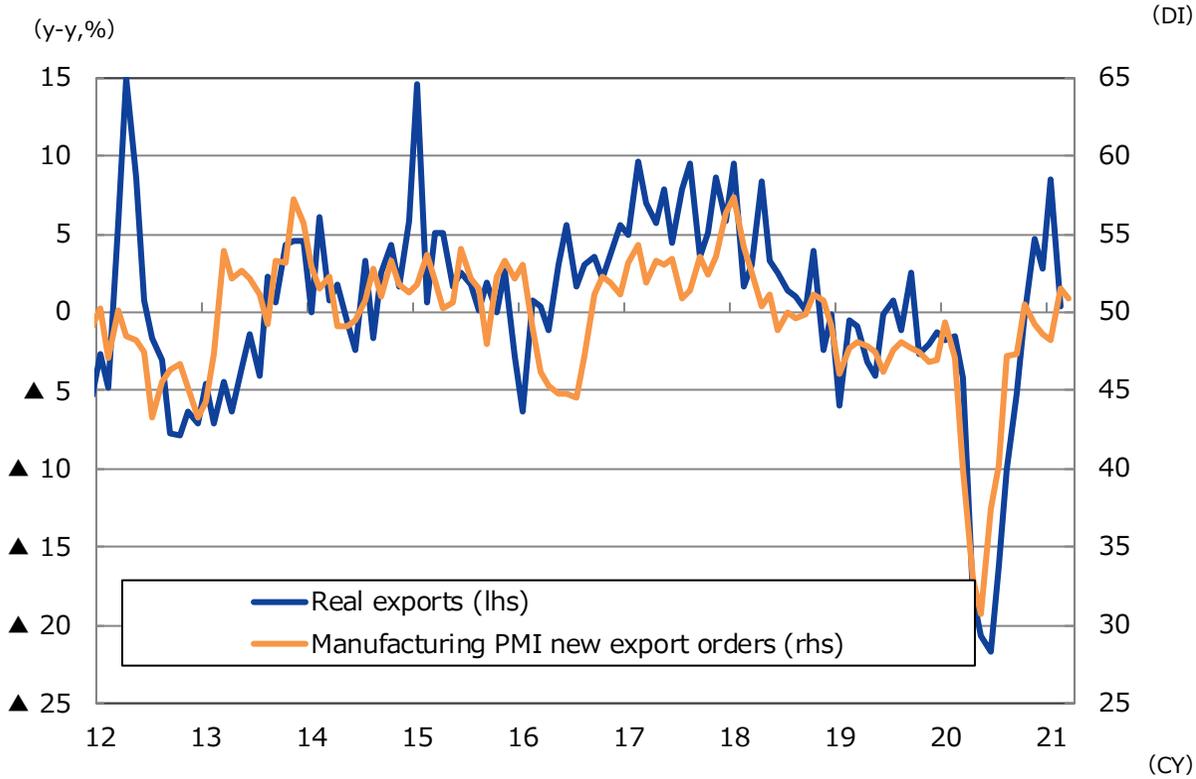
Forecast of Annual Real GDP Growth							
Fiscal Year	FY16	FY17	FY18	FY19	FY20 Est	FY21 Est	FY22 Est
Real GDP	0.8%	1.8%	0.3%	-0.3%	-5.0%	4.2%	2.1%
Private final consumption expenditure	-0.3%	1.0%	0.2%	-1.0%	-6.3%	3.9%	1.7%
Private housing investment	4.3%	-1.8%	-4.9%	2.5%	-7.3%	1.2%	2.0%
Private-sector capital investment	0.8%	2.8%	1.0%	-0.6%	-6.5%	4.9%	5.4%
Public fixed capital formation	0.5%	0.6%	0.8%	1.5%	4.7%	3.7%	1.4%
Net export contribution	0.7%	0.4%	-0.1%	-0.2%	-1.0%	1.0%	0.1%
Exports of goods and services	3.4%	6.3%	2.1%	-2.6%	-11.3%	11.8%	6.0%
Imports of goods and services	-0.5%	3.8%	2.8%	-1.3%	-6.0%	5.5%	5.5%
Nominal GDP	0.8%	2.0%	0.2%	0.5%	-4.3%	3.7%	2.4%
GDP deflator	0.0%	0.2%	-0.1%	0.8%	0.6%	-0.5%	0.3%
Industrial Production Index	0.8%	2.9%	0.3%	-3.6%	-10.0%	11.0%	5.3%
Consumer Price Index (Core)	-0.2%	0.7%	0.8%	0.4%	-0.5%	0.3%	0.5%
Domestic corporate goods price index	-2.4%	2.7%	2.2%	0.1%	-1.4%	1.8%	0.0%
Employee compensation	2.4%	2.0%	3.2%	2.0%	-2.2%	0.4%	1.5%
Unemployment rate	3.0%	2.7%	2.4%	2.4%	2.9%	2.9%	2.7%
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

# Exports and Manufacturing Activities

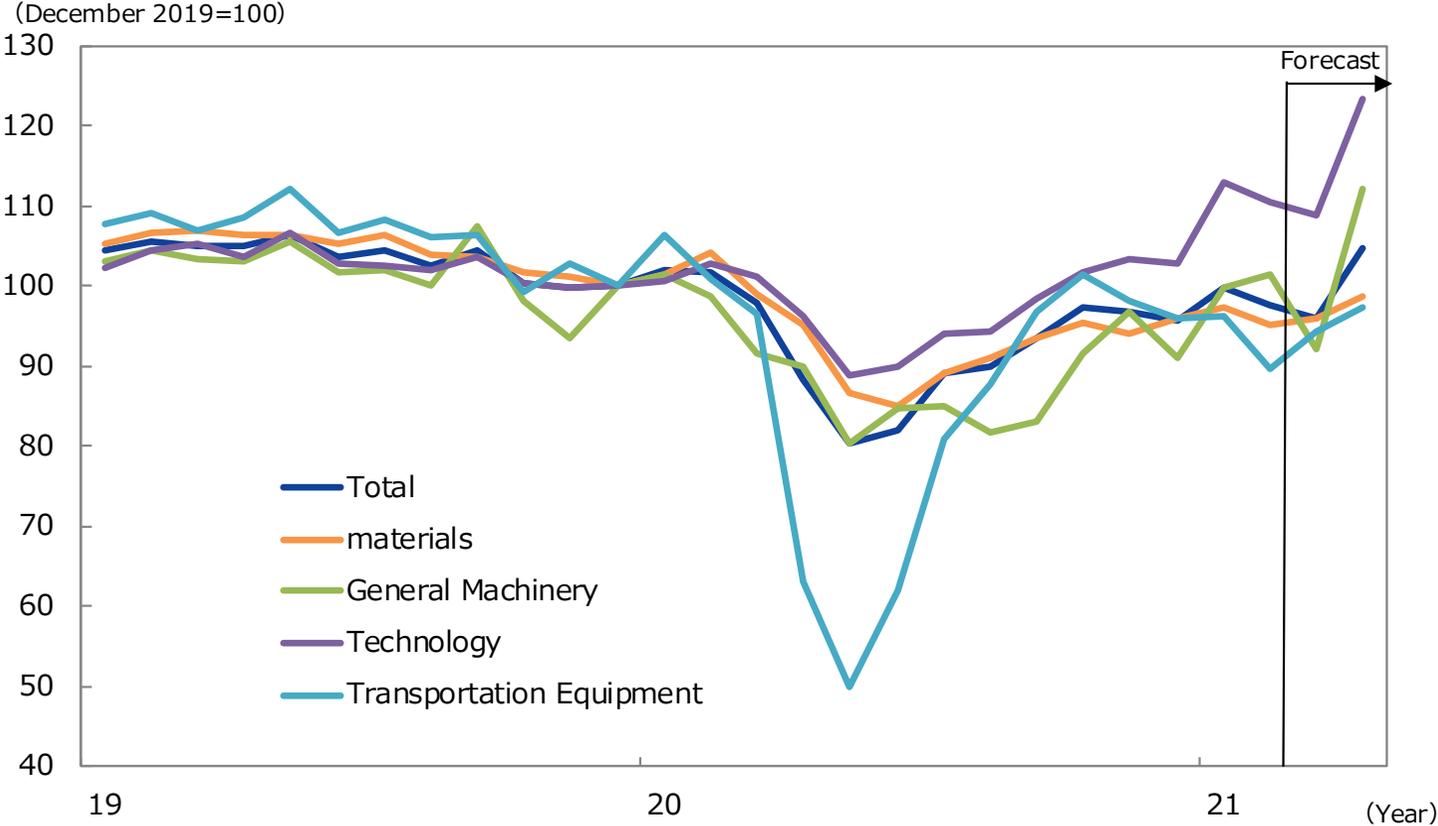
Real exports and manufacturing PMI new export orders



(Source) Compiled by Sumitomo Mitsui DS Asset Management based on data provided by the Bank of Japan, the Cabinet Office and Markit.

# Industrial Production

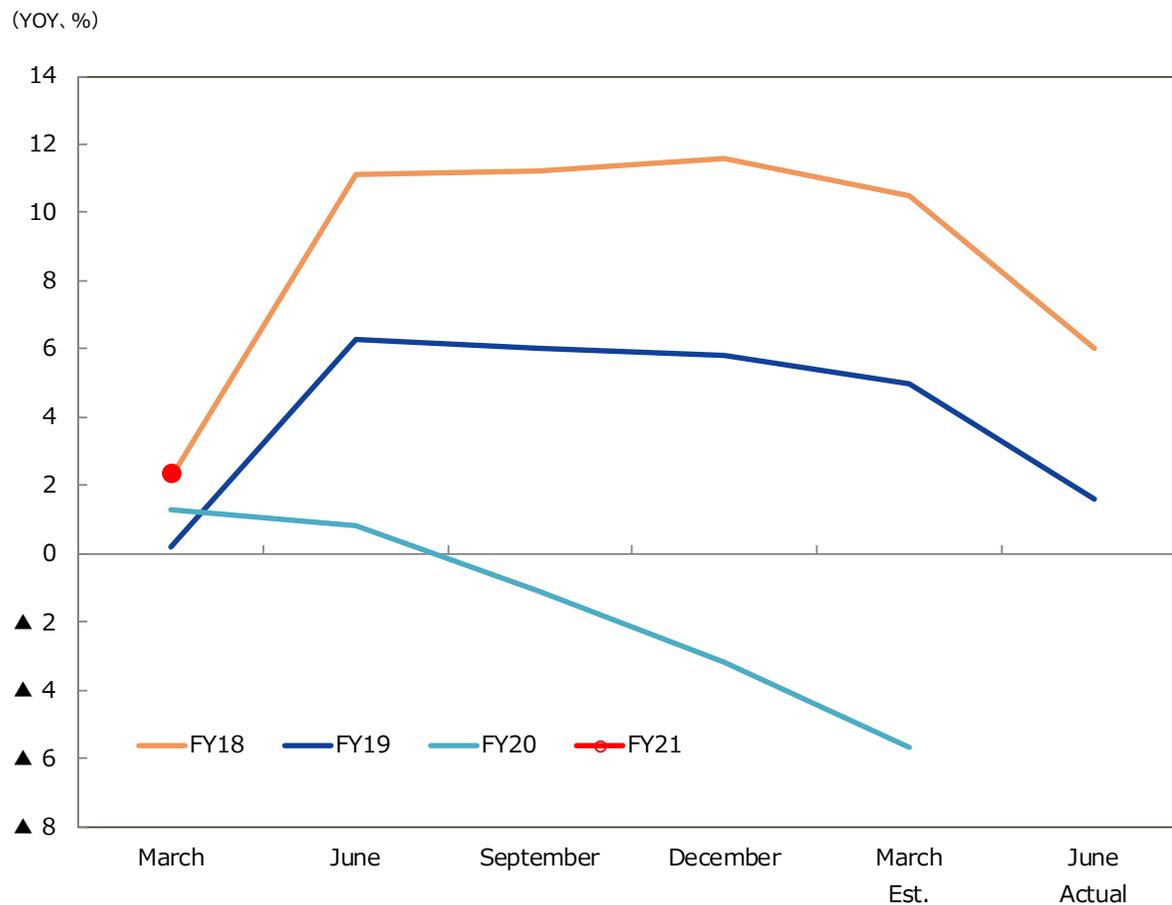
## Industrial Production (Monthly)



(Source) METI, SMDAM

# CAPEX

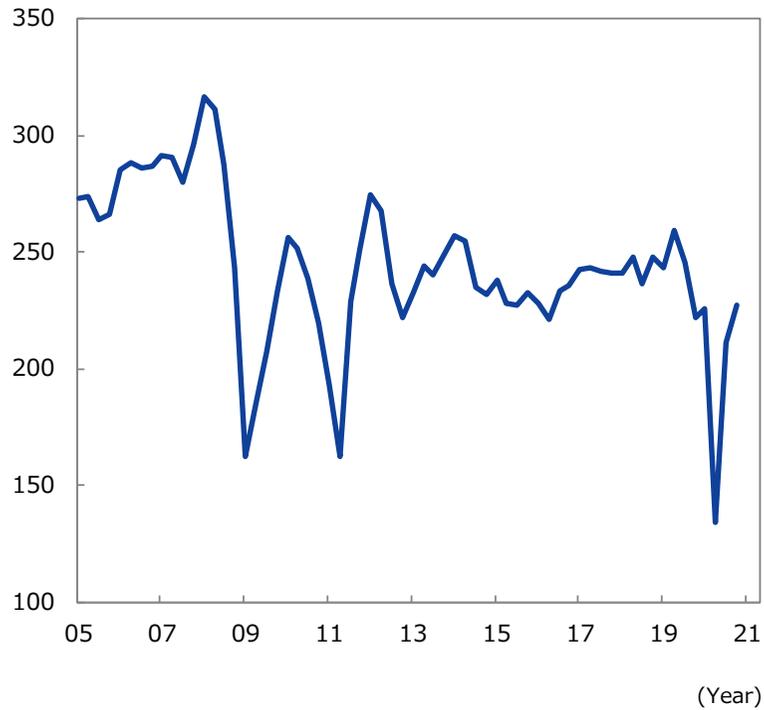
## Plan of CAPEX (inc. software, ex. Land and R&D)



(Source) Bank of Japan, SMDAM

# Shortage of Semiconductors

## Automobile Production (Quarterly, 10K)



(Source) Japan Automobile Manufacturers Association, Inc., SMDAM

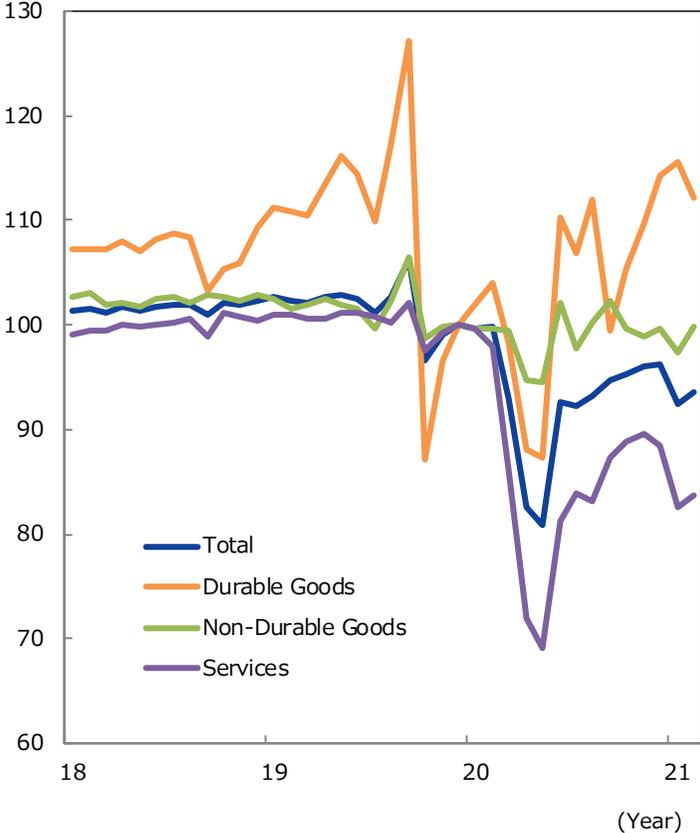
## Est. Impact of Fire at Renesas Electronics Plant

Decrease of Car Production	-500K
Negative Impact to Car Production (QoQ)	-21.7%
Negative Impact to Industrial Production (QoQ)	-2.0%
Negative Impact to GDP (QoQ)	-0.4%
Negative Impact to GDP (YoY)	-1.7%

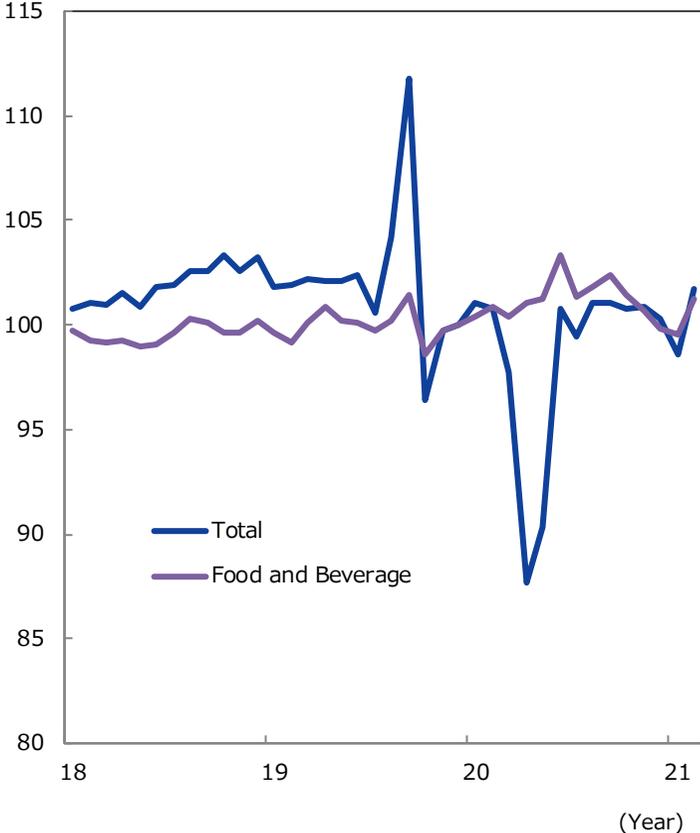
(Source) SMDAM

# Consumer Spending

Consumer Activity Index (Dec. 2019=100)



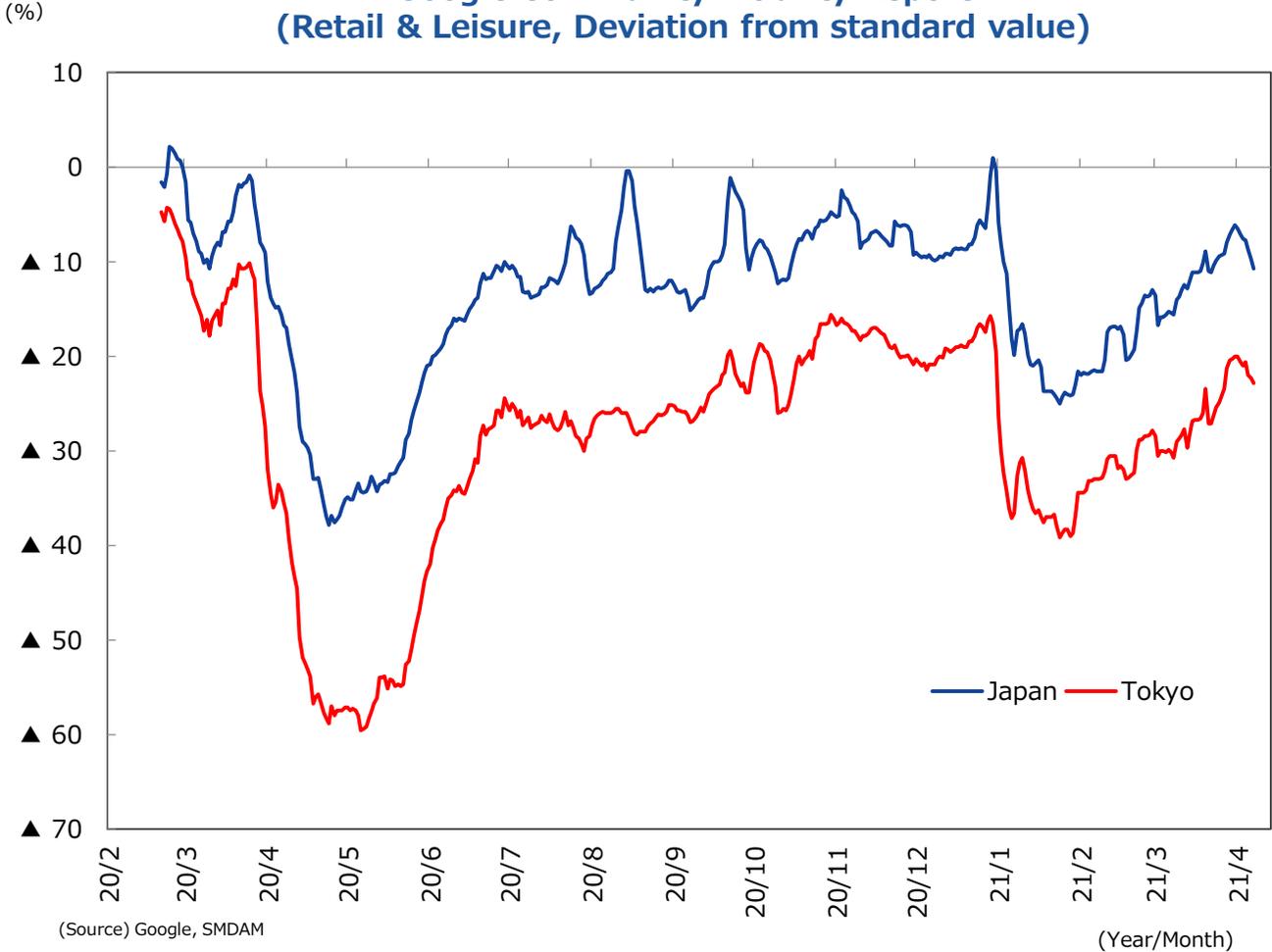
Retail Sales (Dec. 2019=100)



(Source) Bank of Japan, METI, and SMDAM

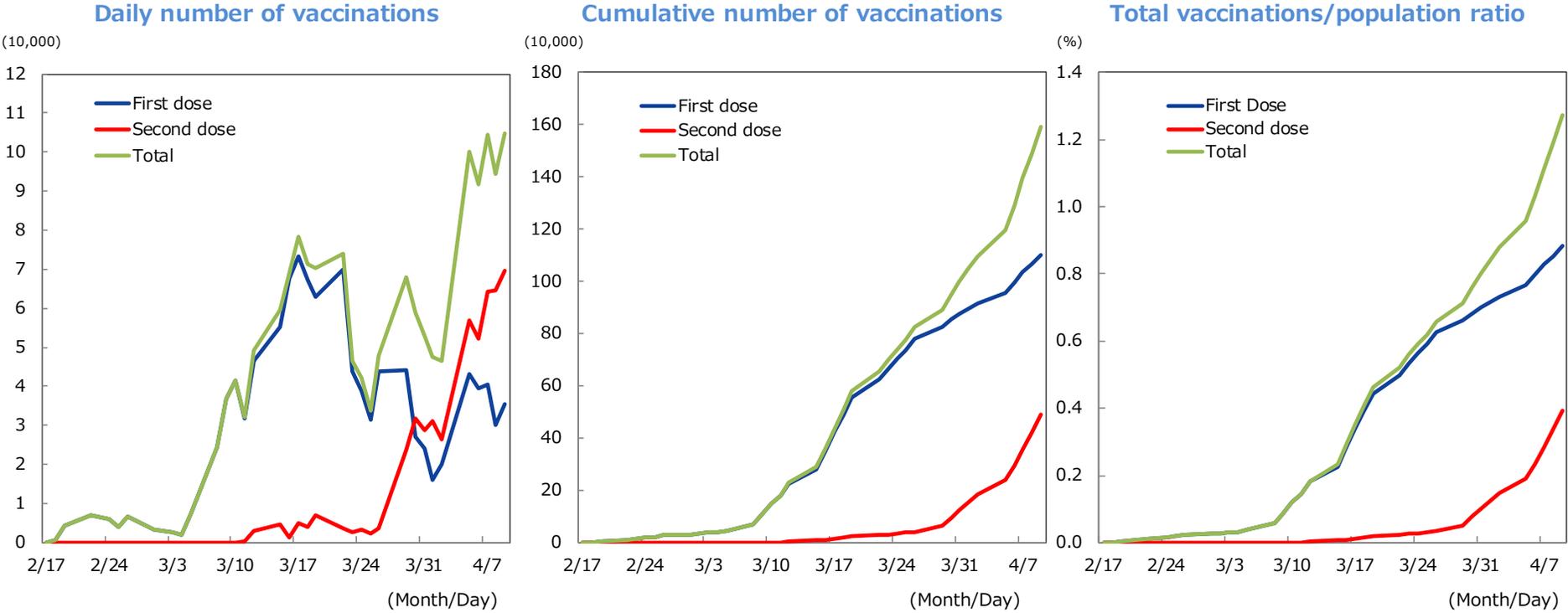
# Mobility Data

### Google Community Mobility Report (Retail & Leisure, Deviation from standard value)



(Source) Google, SMDAM

# Progress of COVID-19 Vaccinations



(Source) MHLW, SMDAM

# Schedule of COVID-19 Vaccinations

- Vaccinations for the elderly began on 12 April 2021. However, full-scale vaccinations are expected to start in May or later. Time of completion depends on the plans of each municipality.
- It has yet to be decided when the vaccine will be given to those who work in nursing homes for the elderly, those with underlying diseases and the general public.
- The Japanese government is expected to secure vaccines manufactured by Pfizer for 50 million people by the end of June. As a result, it will be possible to cover all medical workers and the elderly, workers in facilities for the elderly, and some people with underlying diseases.
- Domestic production of vaccines is scheduled to stabilize the supply of vaccines in Japan. Production of AstraZeneca's vaccine is slated to start in May, while Novavax production will start in the second half of the year.

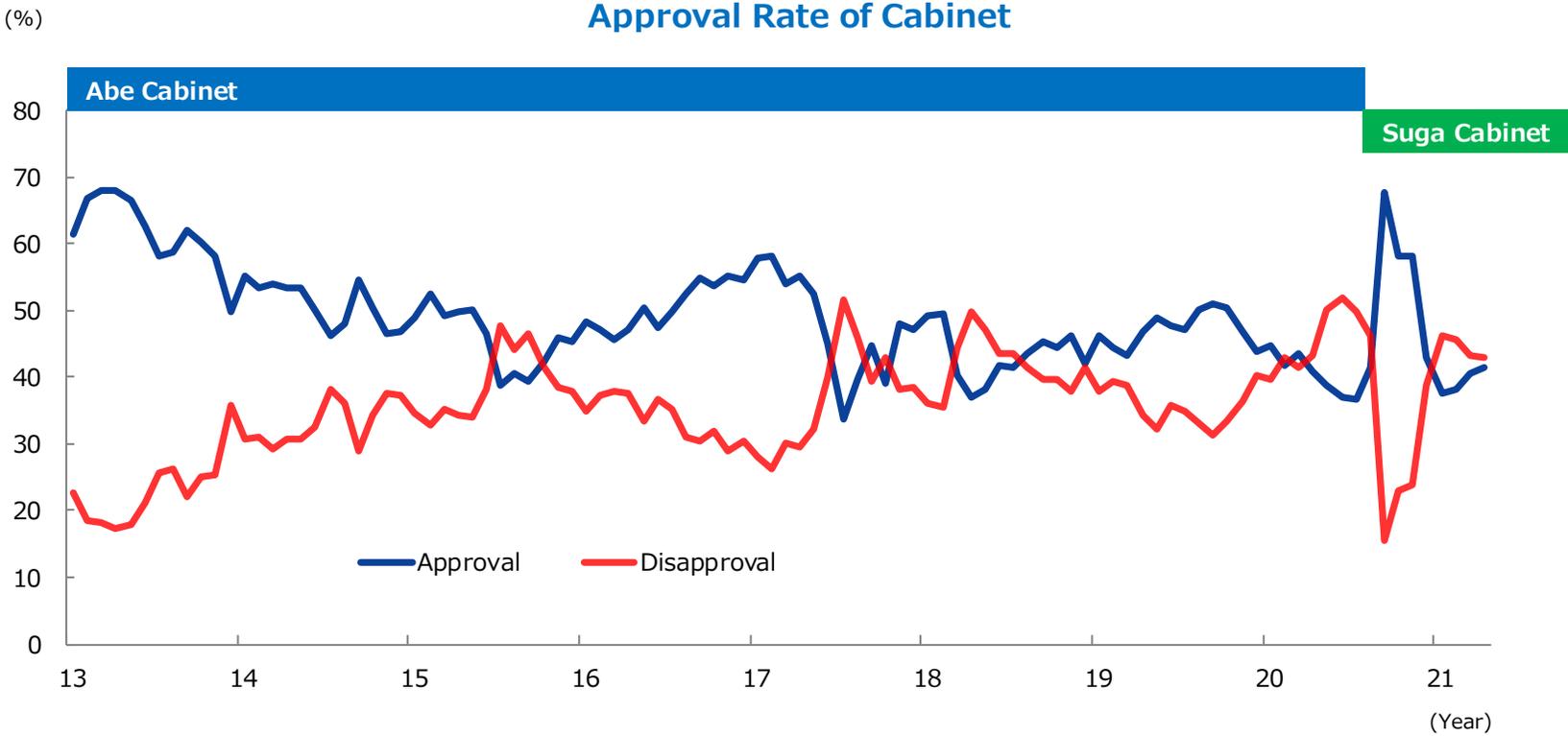
Schedule for the novel coronavirus vaccine

	Vaccination Target							Vaccine Supply					
	Health care workers with highest priority	Health care workers	Elderly persons (65 years old ~)	Elderly care facility workers	Persons with underlying diseases	General (60 ~ 64 years old)	General (16 ~ 64 years old)	Pfizer import	AstraZeneca Import and domestic production	Moderna import	Novavax domestic production	J&J Before contract	
	40,000 people (0.03%)	4.7 million people (3.8%)	36 million people (28.8%)	2 million people (1.6%)	8.2 million people (6.6%)	7.5 million people (6.0%)	52 million people (41.6%)	72.2 million doses	60 million doses	25 million doses	125 million doses		
January													
February	Initiation of vaccination							Approval	Application				
March		Initiation of vaccination						By the end of June, the government expected to secure enough vaccinations for 50 million people. Supplies will increase from May.	Start of import (15 million doses)	Application			
April			Initiation of vaccination										
May			Delivery to municipalities completed by the end of June ->The vaccination will begin in earnest in May.						Start of domestic production after May (45 million doses) ->enhancement of stable supply				
June										By June 20 million doses			
July & future				Possible start of vaccinations	Possible start of vaccinations	Possible start of vaccinations	Possible start of vaccinations			In addition by September 5 million doses	Start of domestic production ->enhancement of stable supply		

(Note) Parentheses of the vaccinated subjects show the ratio of population.

(Source) Creation of Sumitomo Mitsui DS Asset Management based on various materials

# Government approval rate



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

# Schedule of Major Events

Main domestic events for the future			
2021	June	16	End of the ordinary Diet session
		17-18	Monetary Policy Meeting
		29	Term of office of the BOJ Policy Board Member Masai
		Expected	Cabinet Decision on Basic Policies and Growth Strategies
	July	15-16	Monetary Policy Meeting (perspective report)
		23	Tokyo Olympics (until August 8)
		Expected	Tokyo Metropolitan Assembly election
	August	25	Tokyo Paralympics (until September 6)
	Summer	Expected	Revised CPI standards
	September	1	Digital Agency launched
		21-22	Monetary Policy Meeting
		30	LDP President's Term
October	21	End of the term of office of a member of the House of Representatives	
	27-28	Monetary Policy Meeting (perspective report)	
December	26-17	Monetary Policy Meeting	
	Expected	Outline of Tax Reform in Fiscal 22	
	Expected	Cabinet Decision on the FY 22 Budget	

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

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