



Outlook for Japanese Stock Market & Economy

Sumitomo Mitsui DS Asset Management

-November 2022-

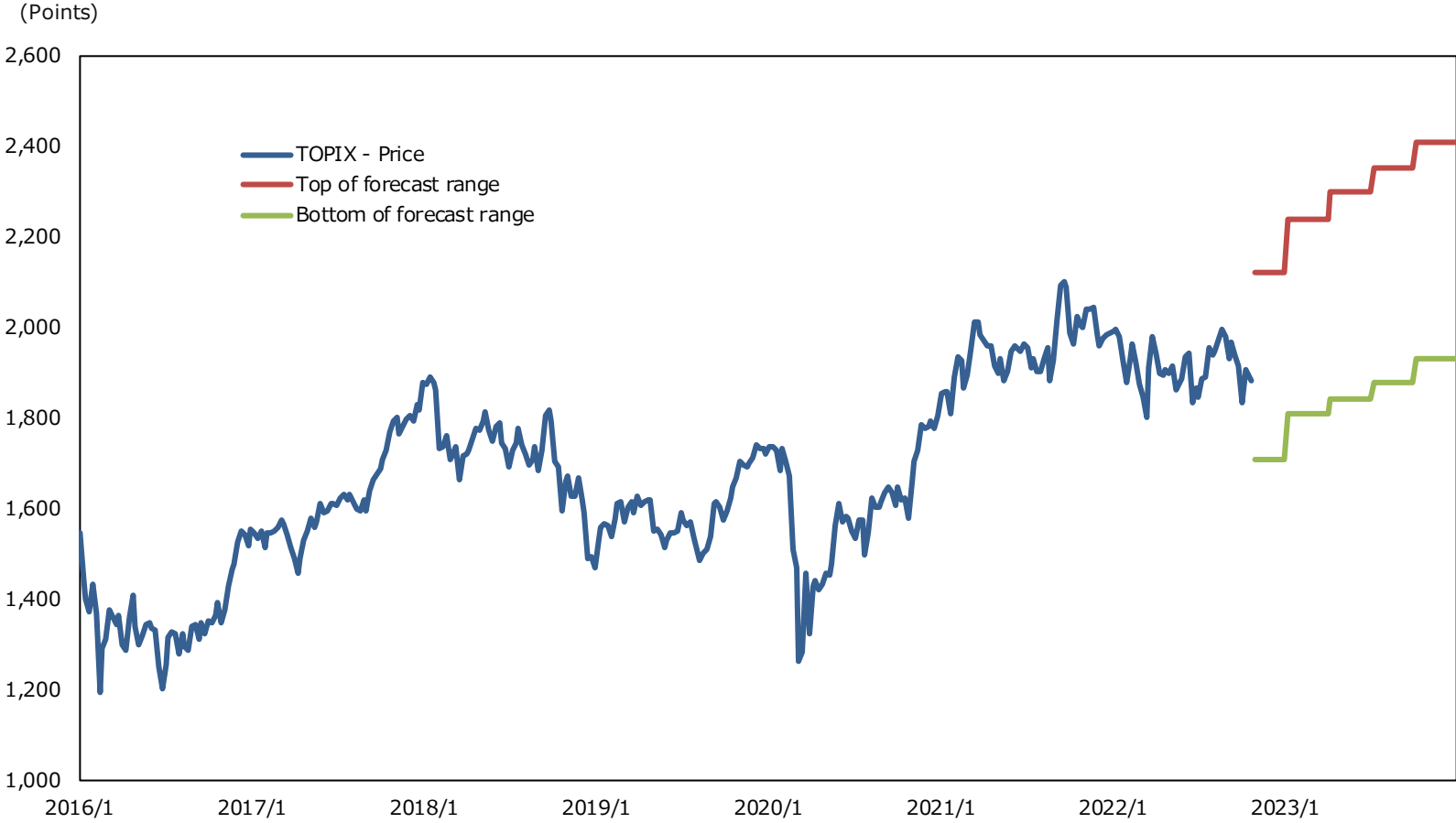


Outlook for Japanese Stock Market

Market Outlook

- We expect range trading in the Japanese stock market in the short term.
- We believe Japanese stocks will resume their bullish trend after the market confirms the peak of the US monetary tightening and signs of a turnaround of the global economy.
- We maintain our TOPIX target at 2,040 as of the end of March 2023 and 2,190 at the end of Dec. 2023. We also keep our Nikkei 225 target at 28,900 for FY 2022 and 31,100 for CY 2023.
- The market could be buoyed by the recovery in the domestic economy and accommodative monetary policy by the central bank, whilst the upside will be capped by the prolonged concern about the global economy in the near future.

We expect range trading followed by a rally



Note: TOPIX data is from Jan. 1st 2016 to Oct. 21st 2022
(Source) TOPIX: Tokyo Stock Exchange, forecast by SMDAM

(Year/Month)

Upside / Downside risk scenarios

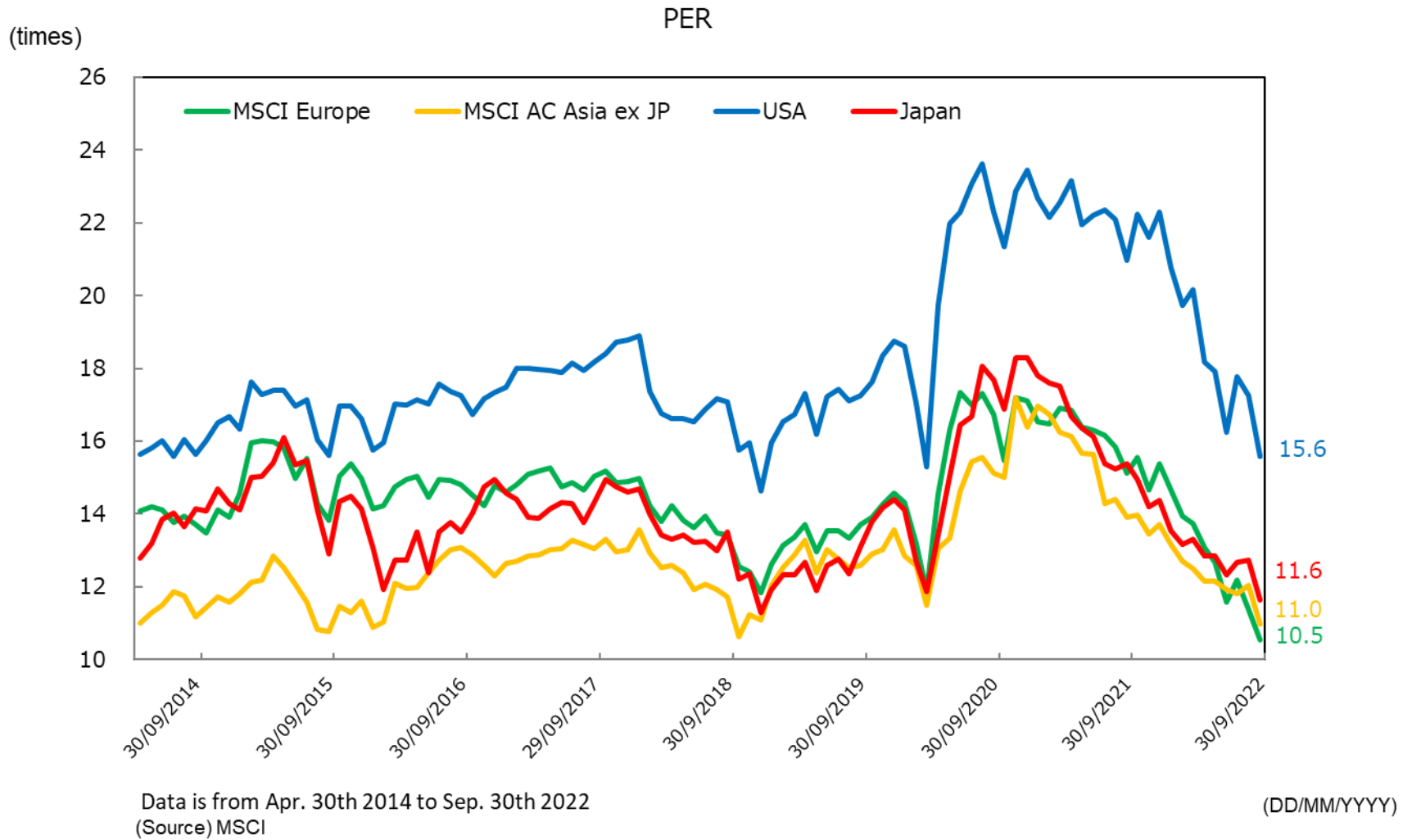
■ Upside Risks

- Recovery of inbound travel from China
- Falling volatility in oil, metals, and other commodity markets
- Positive impact of “Doubling Asset-Based Income Plan” by the cabinet

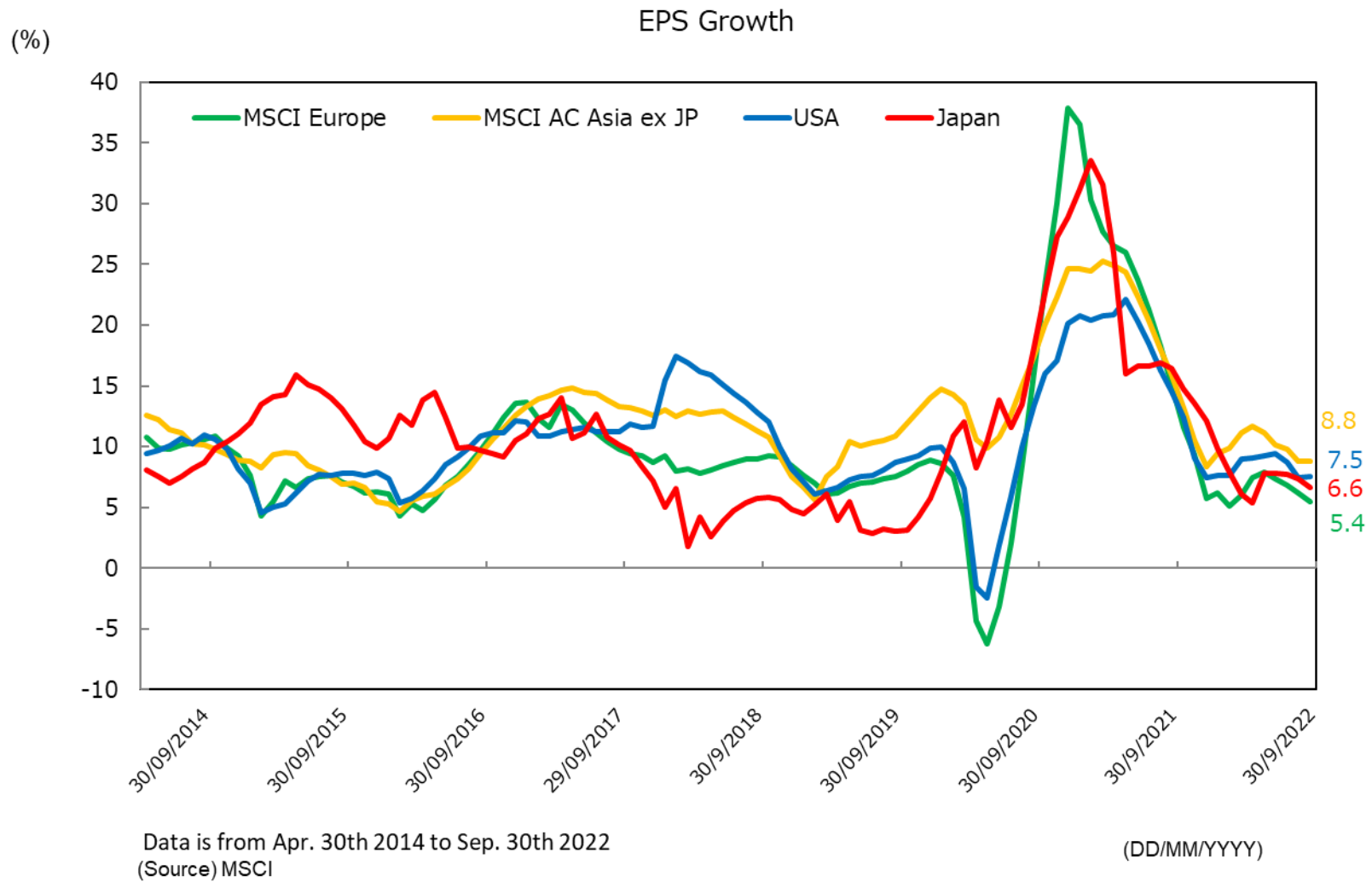
■ Downside Risks

- Concern over fiscal austerity
- Financial crisis in the weak part of the global economy

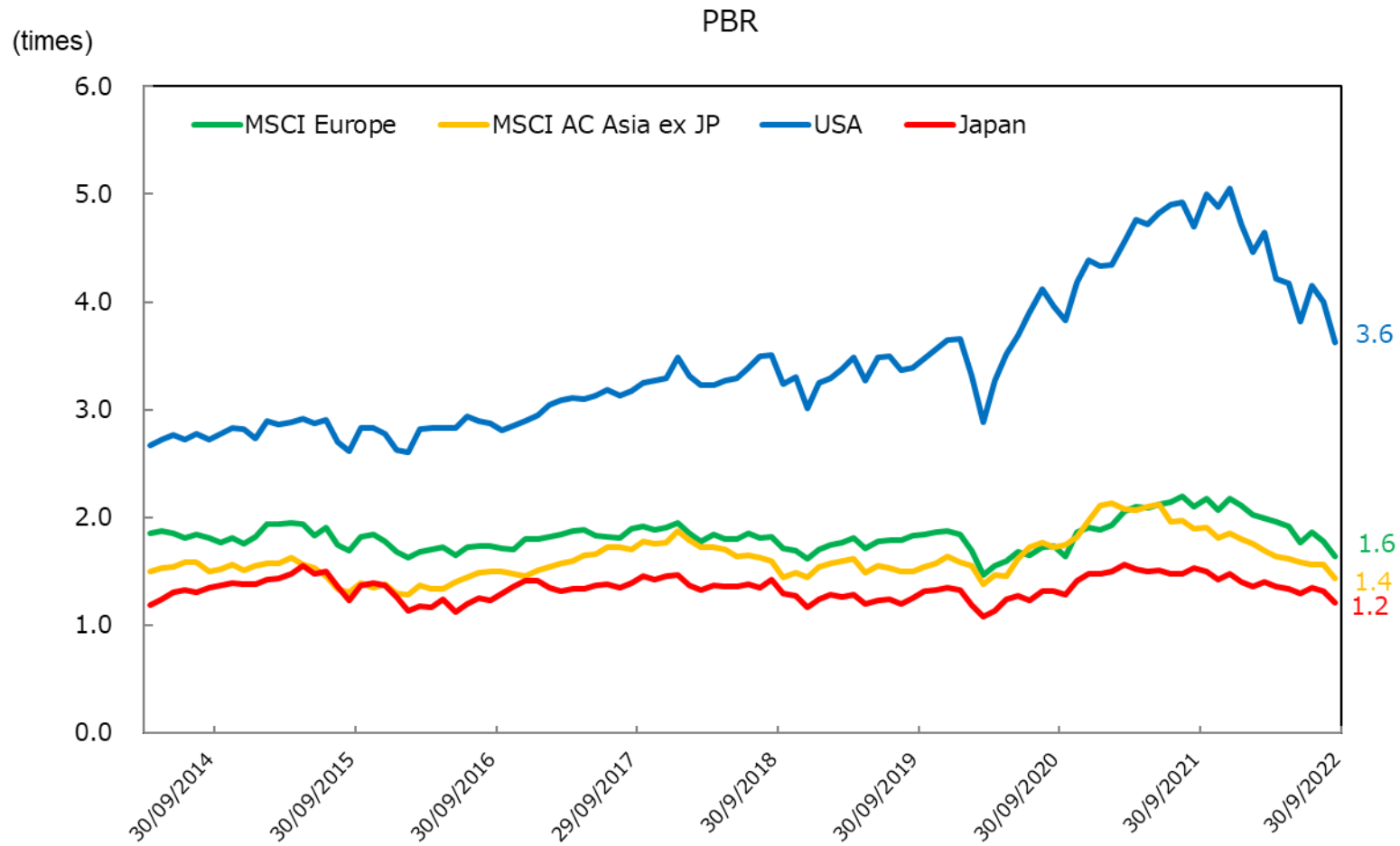
PERs continue to shrink due to global monetary tightening



EPS growth is stable but gradually slowing



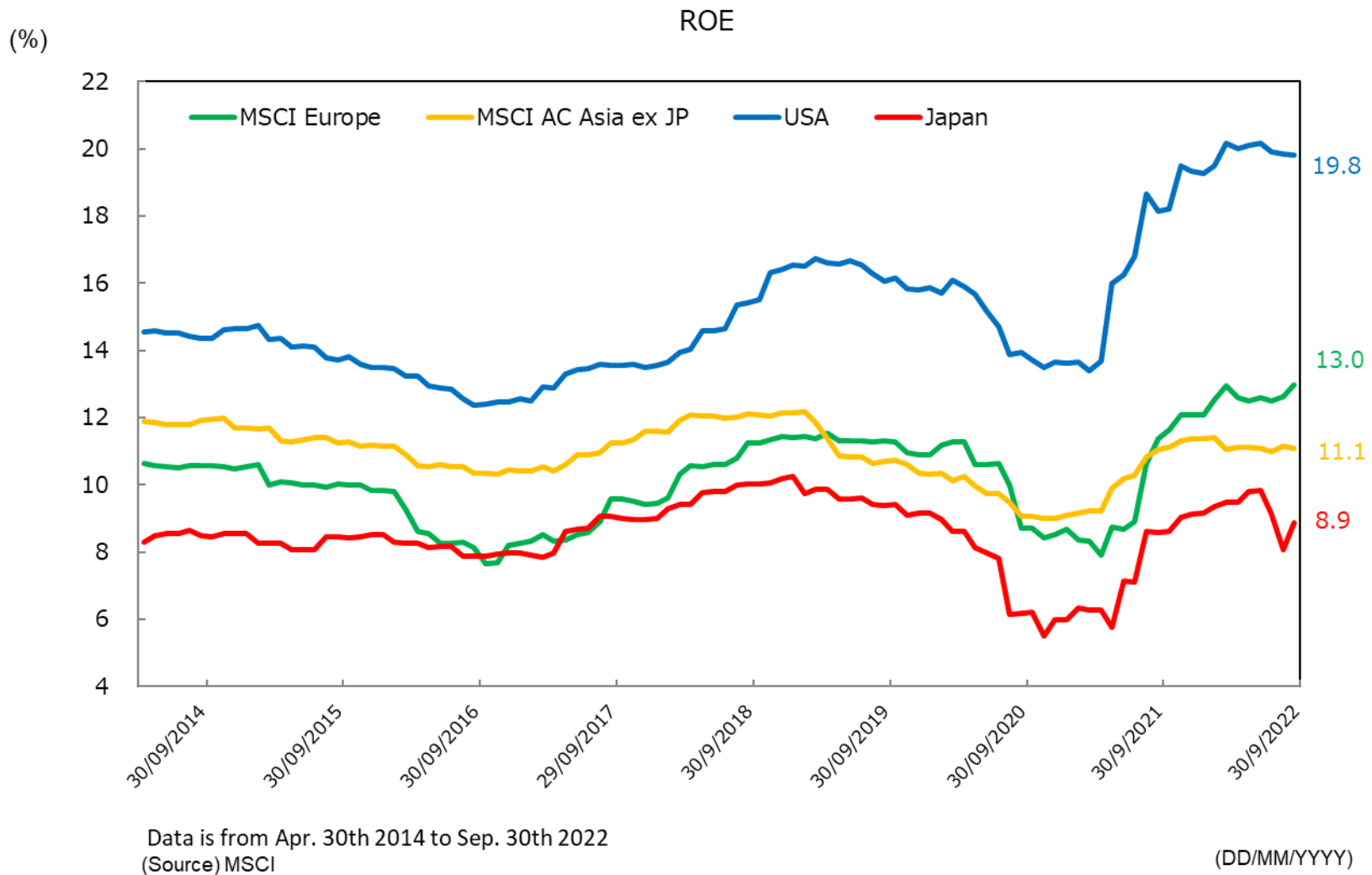
PBRs edged lower coinciding with a market correction



Data is from Apr. 30th 2014 to Sep. 30th 2022
(Source) MSCI

(DD/MM/YYYY)

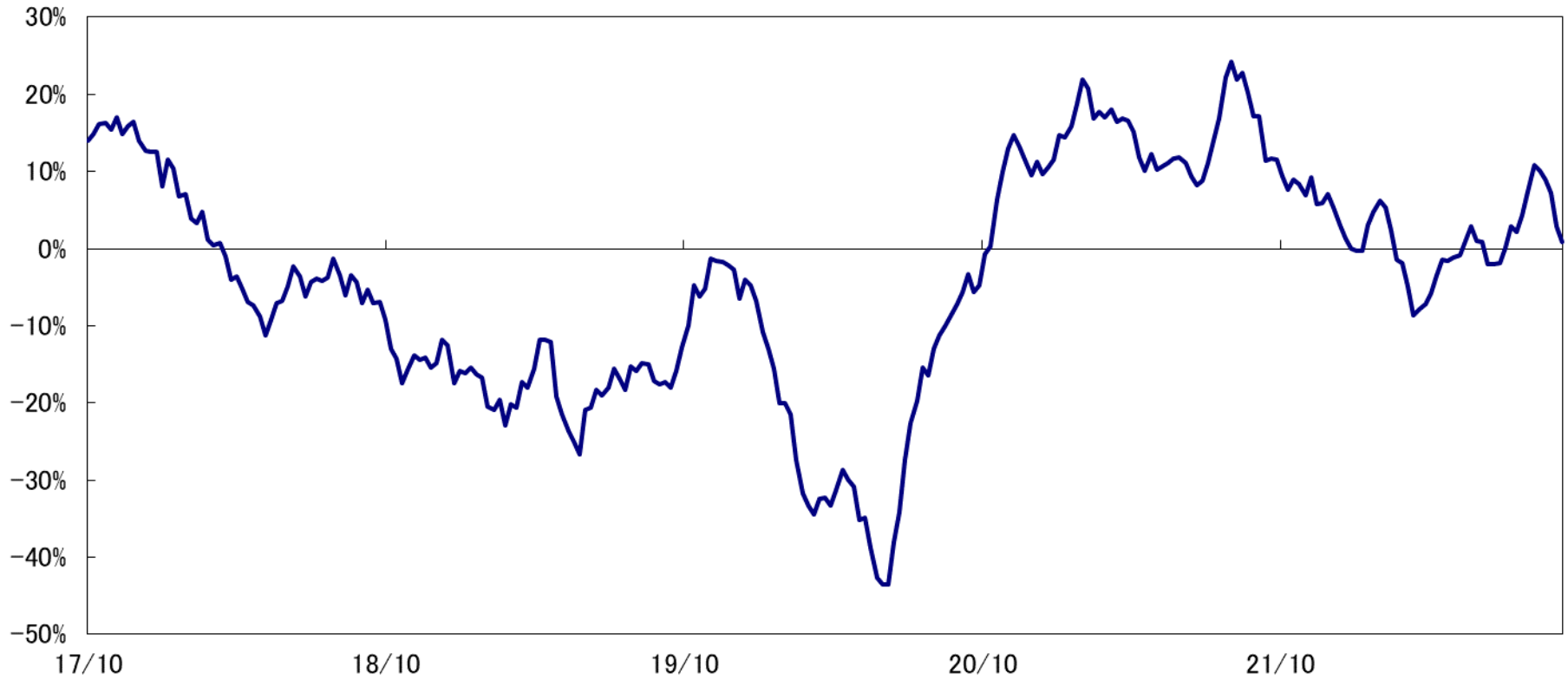
Japan's ROE plunges due to Softbank's significant losses



Note. The above-mentioned company is for illustrative purpose only. We are not advising or recommending to make the long or short positions of the individual stocks.

EPS revision remains positive despite global weakness

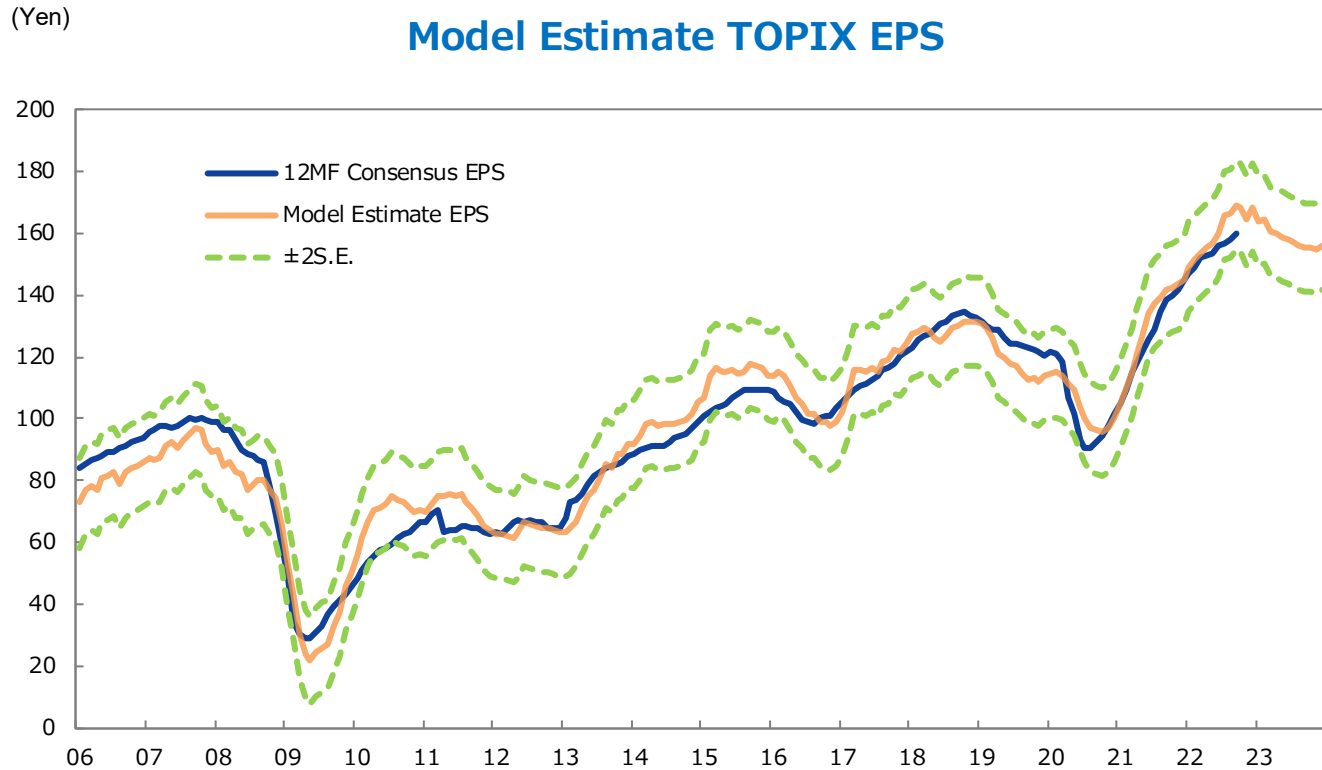
TOPIX Revision Index



Data is from Oct. 31st 2017 to Oct. 11th 2022
(Source) Datastream, IBES

(YY/MM)

The global macro model indicates that EPS is nearing its peak



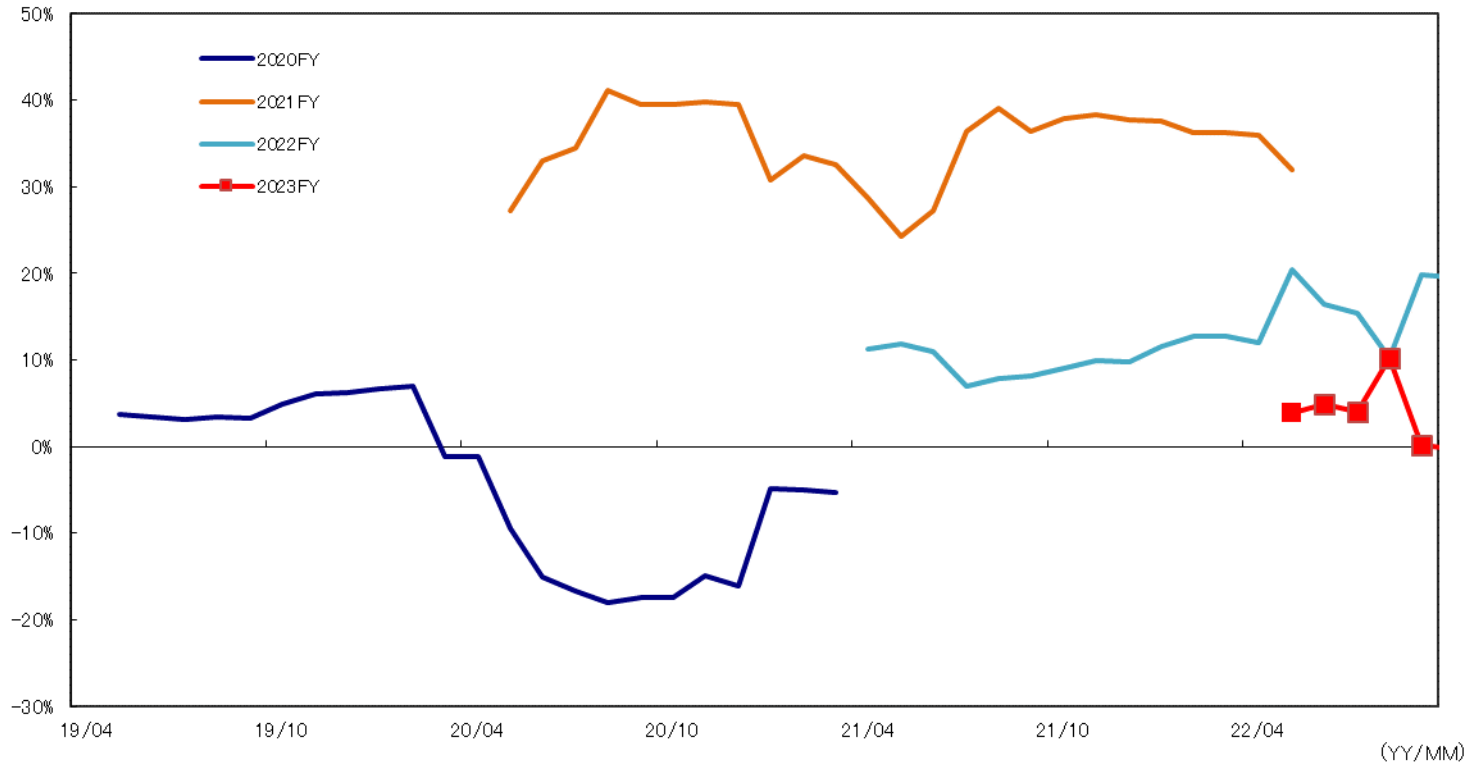
Consensus data is from Jan. 2006 to Sep. 2022, Model data is from Jan. 2006 to Dec. 2023

(Year)

(Source) SMDAM

FY 2023 EPS growth forecast declined below zero for the first time

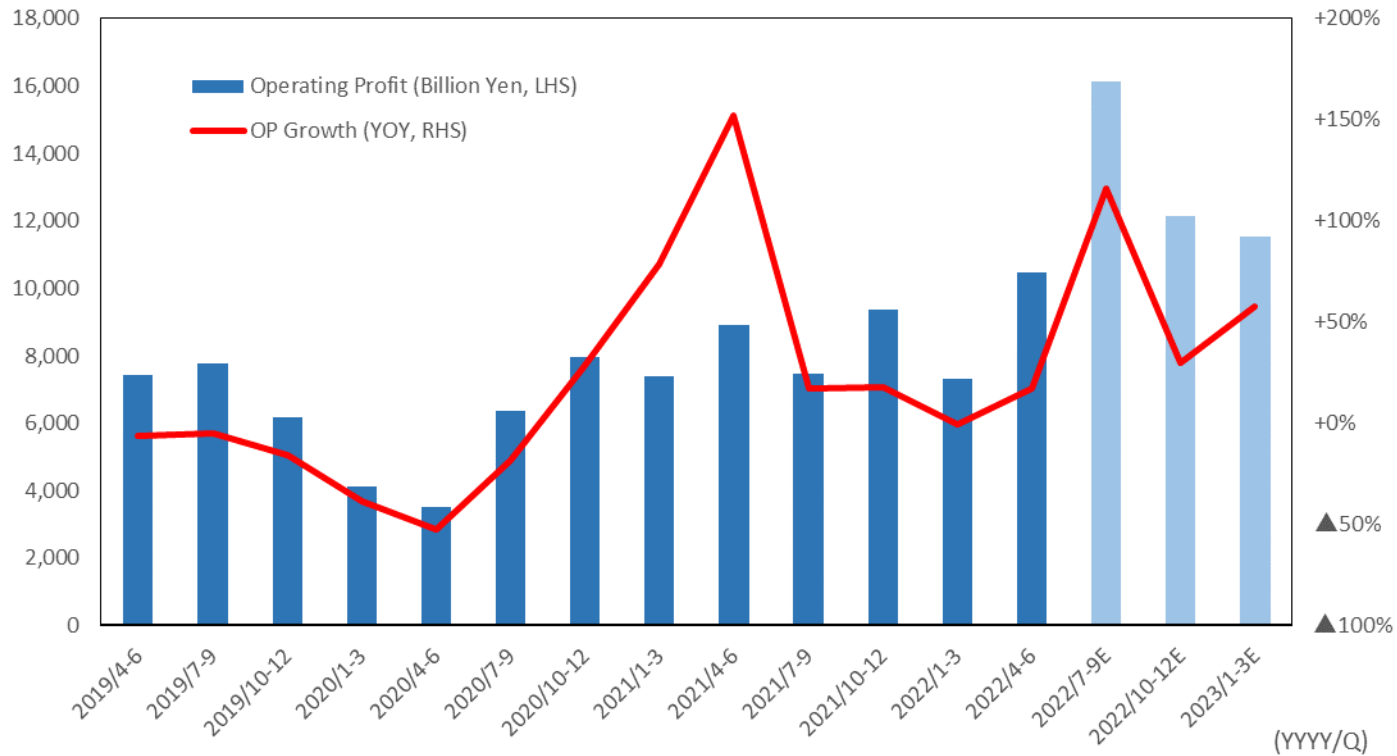
SMDAM Core Research Universe (Excl. Financials) Est. Recurring Profit Growth



Note: Data is as of Oct. 12th 2022, SMDAM Core Universe (Excl. Financials) consists of 399 Japanese companies covered by SMDAM in-house analysts.
 (Source) SMDAM

The operating profit forecast remains strong going forward

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



Actual data is from Q2 2019 to Q2 2022, estimate data is from Q3 2022 to Q1 2023
 (Source) SMDAM

A tide of “Corporate Governance” in Japan

Investors that have signed up to the Principles for Responsible Institutional Investors	
Trust banks	6
Investment managers	202
Insurance companies	24
Pension funds	79
Others	11
Total	322

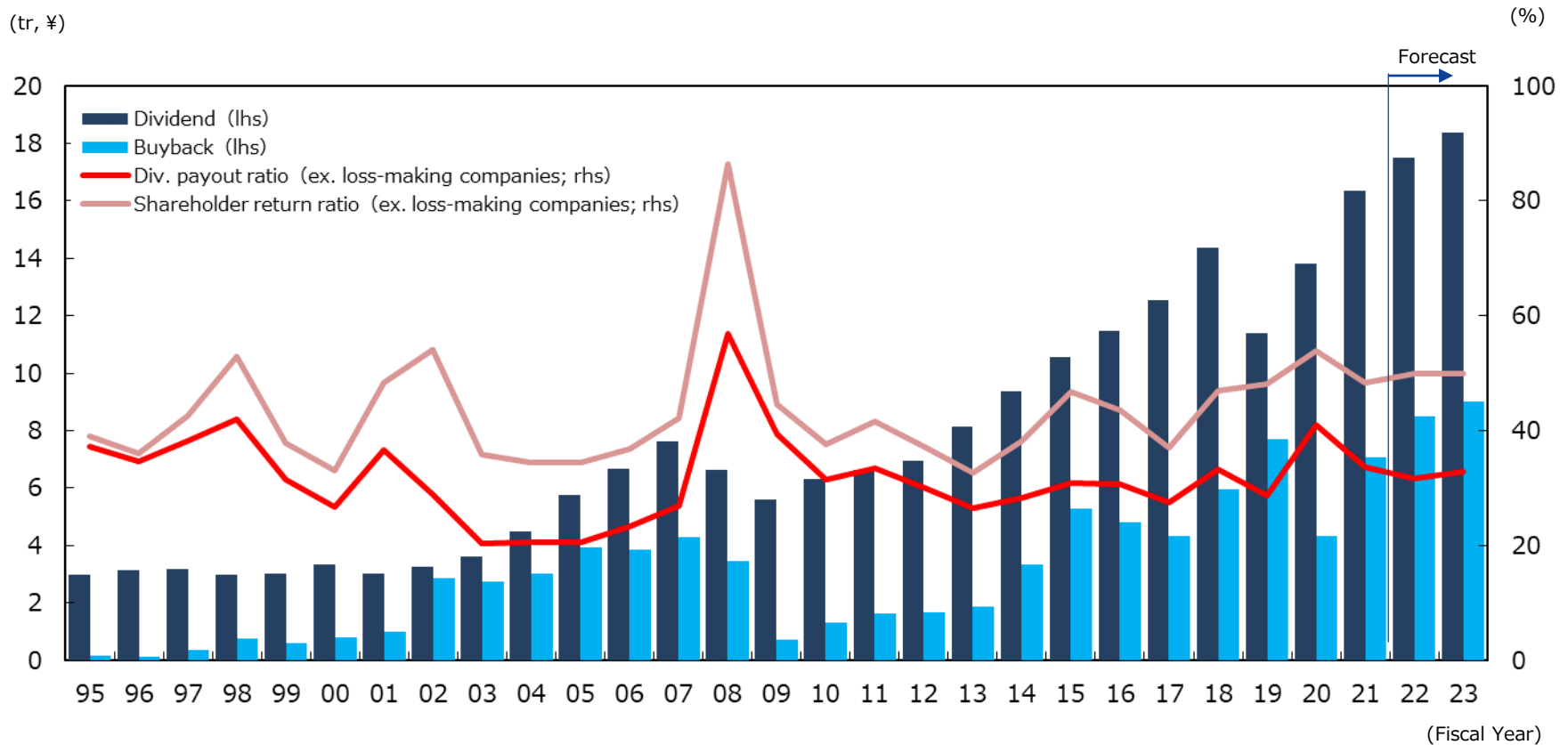
note: As of Sep. 30th 2022

(Source) FSA, SMDAM

- The Stewardship Code (SC) was set in February 2014. Investors are taking a more proactive approach in talking to companies and exercising proxy voting rights. The Financial Services Agency discloses the name of institutional investors which 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. It implicitly provides 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 buy backs breaking historical highs

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



Note: Data is from FY1995 to FY2023, FY2022 and FY2023 are forecasts.
 Source: Toyo Keizai, Quick, INDB, Daiwa Securities, SMDAM

Small & value continues to dominate the recent 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	-2.62	-1.05	-5.29	-6.83	16.47	17.21	10.19
Total Value	-1.48	0.11	4.66	1.36	31.65	16.41	5.21
Top Cap Value	-1.84	-1.97	5.77	3.36	40.28	26.71	18.20
Large Cap Value	-1.92	-1.13	5.24	1.99	34.81	17.87	8.00
Mid Cap Value	-2.01	0.00	4.55	0.26	28.27	6.26	-5.32
Small Cap Value	0.39	5.65	2.32	-1.39	18.18	9.94	-6.70
Micro Cap Value	1.18	5.56	-0.19	-1.10	14.89	7.80	-7.44
Total Growth	-3.87	-2.31	-14.38	-14.17	2.89	16.14	13.65
Top Cap Growth	-5.80	-5.07	-17.11	-14.71	6.79	18.51	16.59
Large Cap Growth	-4.45	-2.88	-15.15	-14.32	3.65	17.29	14.49
Mid Cap Growth	-1.98	1.20	-11.49	-13.54	-0.95	15.43	11.33
Small Cap Growth	1.14	2.63	-7.49	-13.33	-3.86	6.36	5.66
Micro Cap Growth	1.90	3.20	-9.90	-15.67	-6.39	7.87	7.46
Top Cap Total	-3.96	-3.62	-7.62	-7.22	20.68	21.81	16.71
Large Cap Total	-3.19	-2.01	-6.00	-7.06	17.52	18.43	12.09
Mid Cap Total	-2.00	0.54	-3.42	-6.72	13.18	13.80	5.67
Small Cap Total	0.64	4.61	-1.20	-5.91	9.62	9.47	-0.97
Micro Cap Total	1.38	4.88	-3.13	-5.76	7.55	9.01	-0.86

Note : As of Oct. 20th 2022
(Source) Bloomberg



Outlook for Japanese Economy

Current status & Outlook of Japanese economy

[Current Status]

- **The economy is recovering.** While consumer sentiment has been subdued on the back of higher inflation, business sentiment has improved, particularly for face-to-face services, as the number of COVID-19 infections has fallen. CAPEX, pent-up demand, “de-carbonization” and “digitization” are seen as economic tailwinds. After an economic downturn caused by the lockdown in Shanghai, an increase in industrial production has also been continuing so far.
- **Inflation is on an upward trend.** CPI is accelerating in Tokyo and nationwide. Special factors have contributed to the rise in the inflation rate, including the cost-push caused by rising import prices and the loss of the impact of last year's mobile phone rate cut.

[Outlook]

- ① **We have revised up our real GDP growth forecast for FY 2022 from +1.9% to +2.0% but remain unchanged at +0.7% for FY 2023.** We raised our estimate for the current fiscal year due to the upward revision of CAPEX. Regarding H2 of the economy, we foresee a stable outlook due to rising CAPEX and easing supply-side constraints. On the other hand, we expect a slowing economic recovery owing to the deterioration of foreign economies.
- ② **We have raised the Core CPI forecast for FY 2022 from +2.4% to +2.7% and also revised our FY 2023 forecast from +1.2% to +1.3%.** Inflation forecasts have been raised due to increasing costs of foods, energy, and consumer durables. While core CPI is highly likely to accelerate to the mid- 3% range YOY in the latter part of 2022, it could slow down on/after 2023 thanks to easing pressure from cost-push inflation and a slowing economy.
- ③ **PM Kishida to maintain his accommodative economic policy.** PM Kishida ordered his cabinet to compile a comprehensive economic package by the end of October. A supplementary budget is expected to be drawn up during an extraordinary Diet session and the size of the economic package is assumed to be 15 trillion yen. However, in a meeting with senior members of the ruling LDP, PM Kishida agreed that "a very bold policy is needed," suggesting that the size of the stimulus could be raised.
- ④ **The Bank of Japan to maintain its accommodative monetary policy, even after the end of Governor Kuroda's term in April 2023 due to weak wage increases and the negative impact from the slowing global economy. The BOJ regards wage increases and continued monetary easing are the keys to consistently achieving their price target.** While core CPI is likely to remain above 2% in foreseeable future, the BOJ's assessment that cost-push inflation is temporary is likely to remain unchanged. Though PM Kishida's administration is expected to appoint new BOJ board members with the flexibility to review current monetary policy, it is unlikely to change monetary policy through 2023.

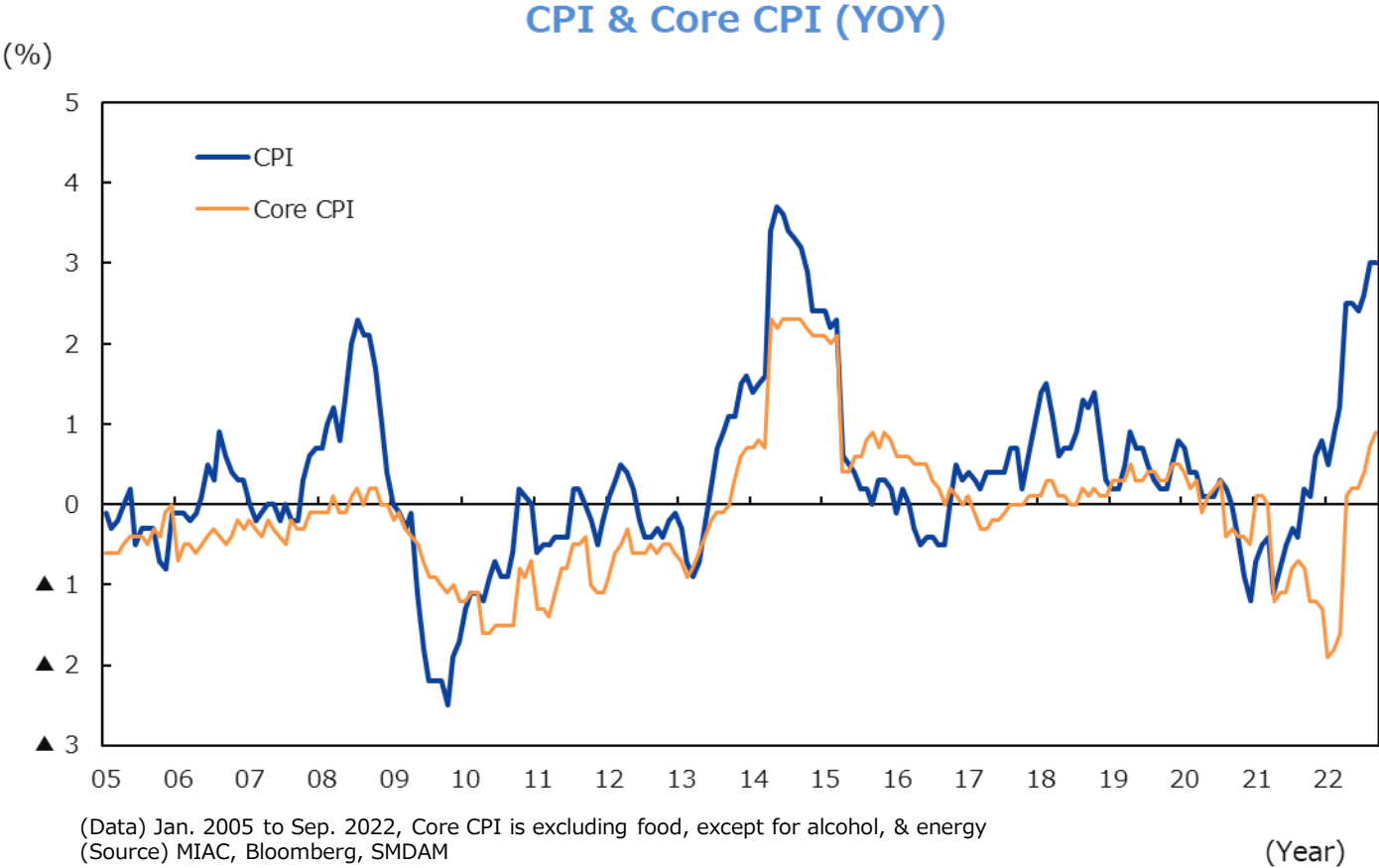
Forecast table for the Japanese economy

Forecast of annual Real GDP growth and its breakdown								
Fiscal Year	FY17	FY18	FY19	FY20	FY21	FY22 Est	FY23 Est	
Real GDP	1.8%	0.3%	-0.9%	-4.6%	2.3%	2.0%	0.7%	
Private final consumption expenditure	1.0%	0.1%	-1.0%	-5.4%	2.6%	2.5%	0.7%	
Private housing investment	-1.8%	-4.8%	2.5%	-7.8%	-1.6%	-4.4%	-0.8%	
Private-sector capital investment	2.8%	1.5%	-1.7%	-7.7%	0.6%	4.8%	1.9%	
Public fixed capital formation	0.6%	0.8%	1.7%	5.1%	-7.5%	-3.3%	0.5%	
Net export contribution	0.4%	-0.2%	-0.5%	-0.6%	0.8%	-0.3%	-0.2%	
Exports of goods and services	6.3%	2.0%	-2.3%	-10.0%	12.5%	2.5%	-0.9%	
Imports of goods and services	3.8%	3.0%	0.2%	-6.3%	7.2%	3.9%	0.2%	
Nominal GDP	2.0%	0.2%	0.0%	-3.9%	1.3%	2.2%	1.6%	
GDP deflator	0.2%	-0.1%	0.8%	0.7%	-1.0%	0.2%	0.9%	
Industrial Production Index	2.9%	0.3%	-3.7%	-10.0%	5.9%	2.0%	1.0%	
Consumer Price Index (Core)	0.7%	0.8%	0.4%	-0.6%	0.1%	2.7%	1.3%	
Domestic corporate goods price index	2.7%	2.2%	0.1%	-1.5%	7.1%	7.6%	0.7%	
Employee compensation	2.0%	3.2%	2.0%	-1.5%	1.8%	2.0%	1.2%	
Unemployment rate	2.7%	2.4%	2.4%	2.9%	2.8%	2.5%	2.5%	
Call Rate (End value)	-0.1%	-0.1%	-0.1%	-0.1%	-0.1%	-0.1%	-0.1%	

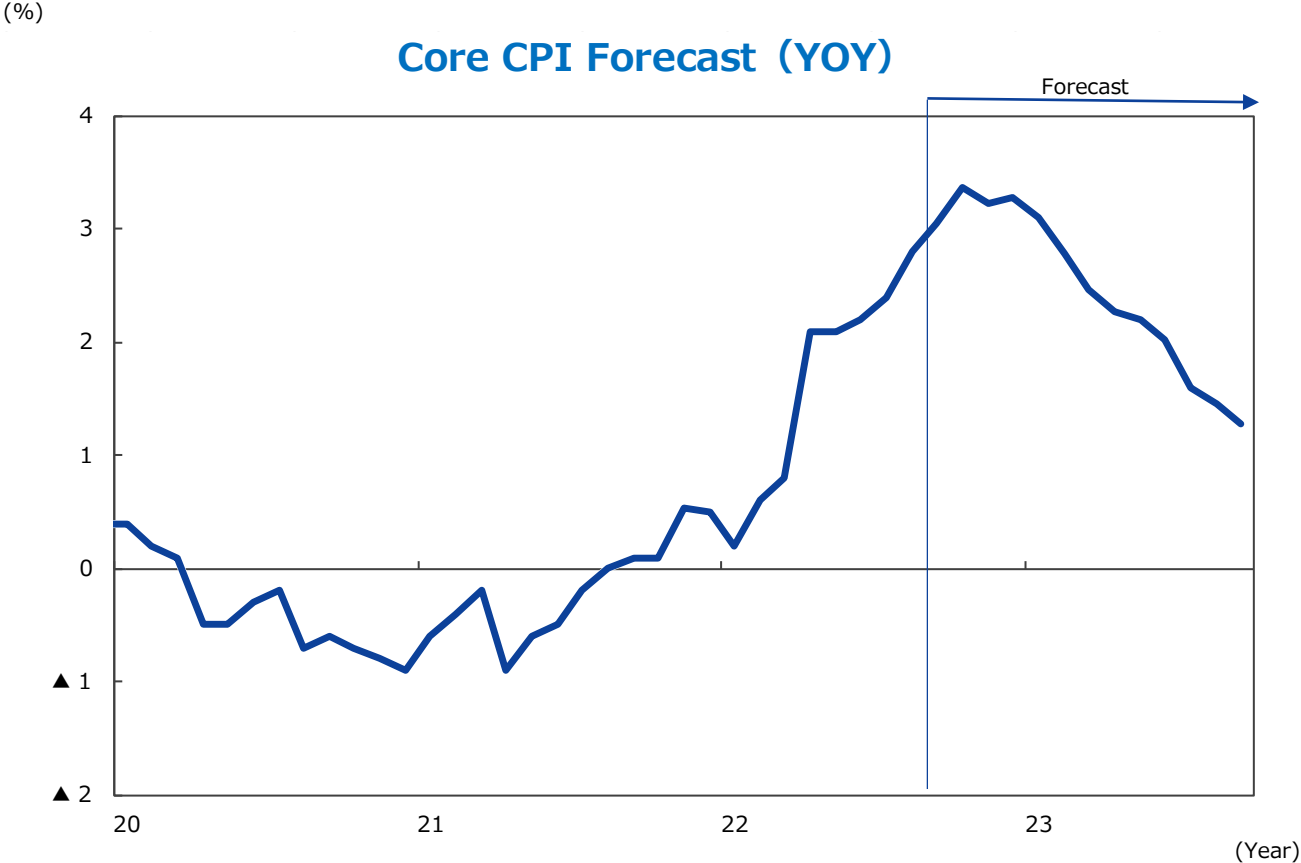
(Note) Rate of increase over the previous year. Net exports are based on the degree of contribution, and the consumer price index (Core) excludes the effects of the consumption tax and free education. The forecast is for Sumitomo Mitsui DS Asset Management.

(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

Finally inflation has come back to Japan



Core CPI is likely to reach its peak

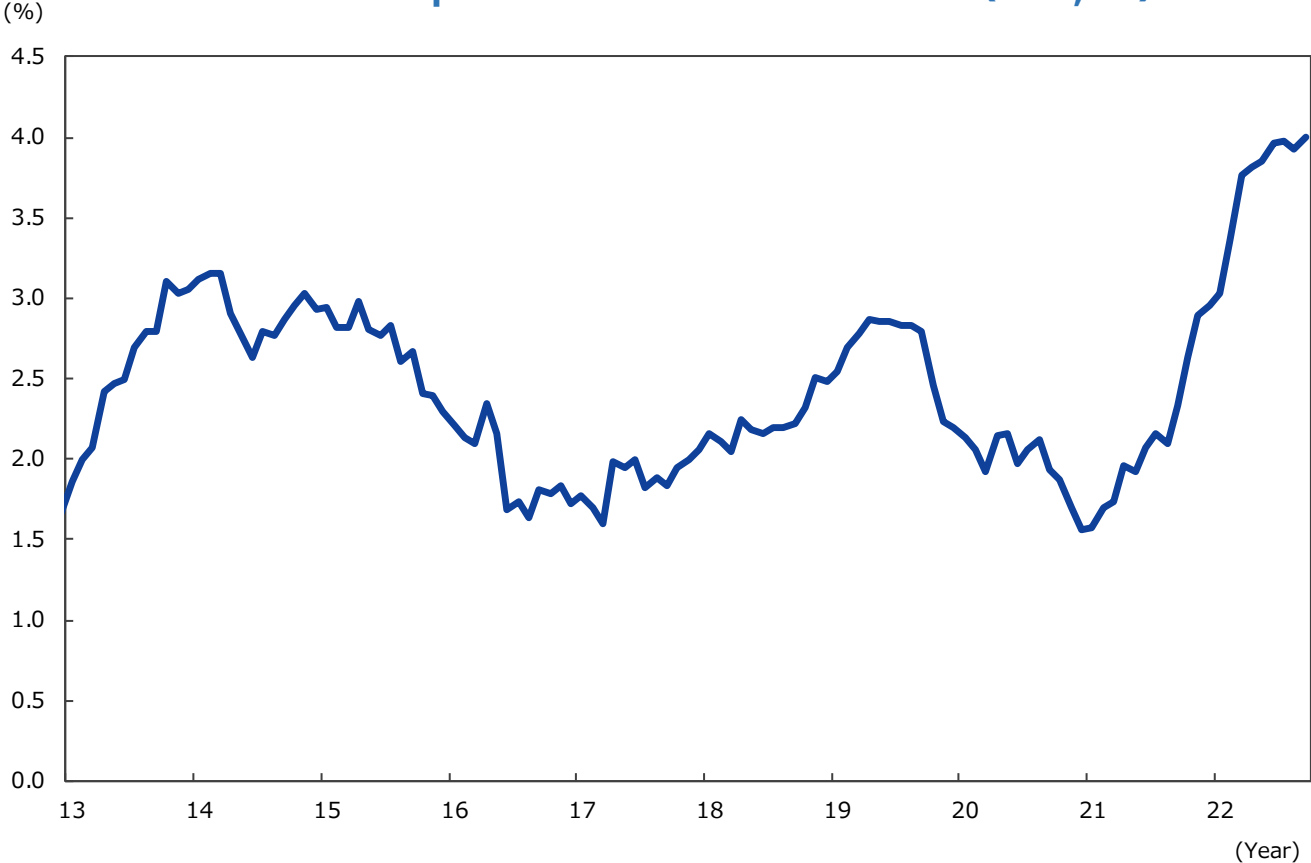


(Data) Data is from Jan. 2020 to Sep. 2023. Data after Aug. 2022 are forecast. Forecast is based on the assumption of foreign exchange rate at 1 USD = 140 JPY and crude oil at 95 USD per barrel as of the end of Sep. 2023.

(Source) Cabinet Office, SMDAM

Rising energy costs boost peoples' expectations for inflation

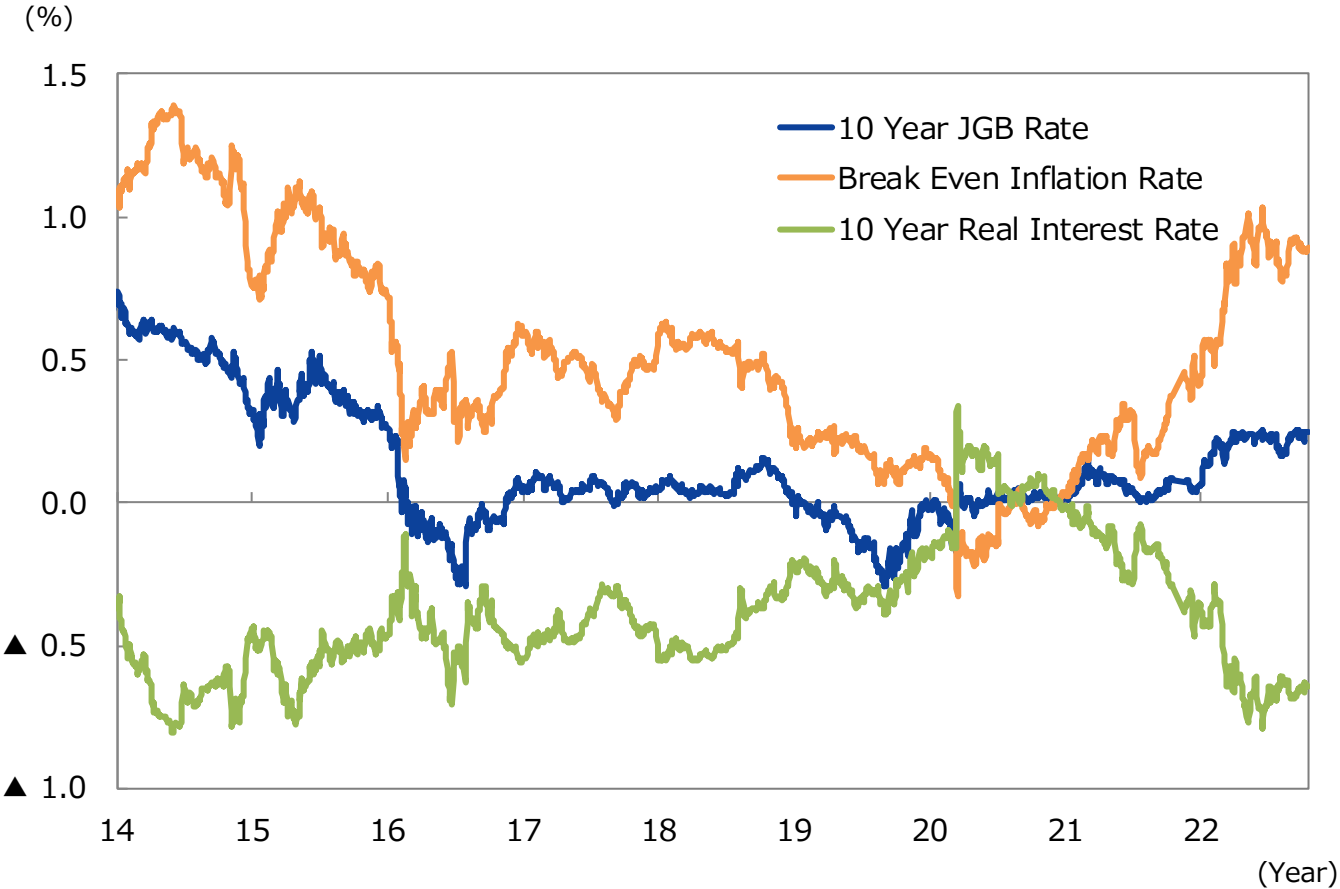
Consumers' Expectation of Inflation Rate (YOY, %)



(Data) Weighted average of inflation forecast of "Consumer Confidence Survey".
Data is from Jan. 2013 to Sep. 2022.
(Source) Cabinet Office, SMDAM

BOJ's yield curve control pushes the real interest rate lower

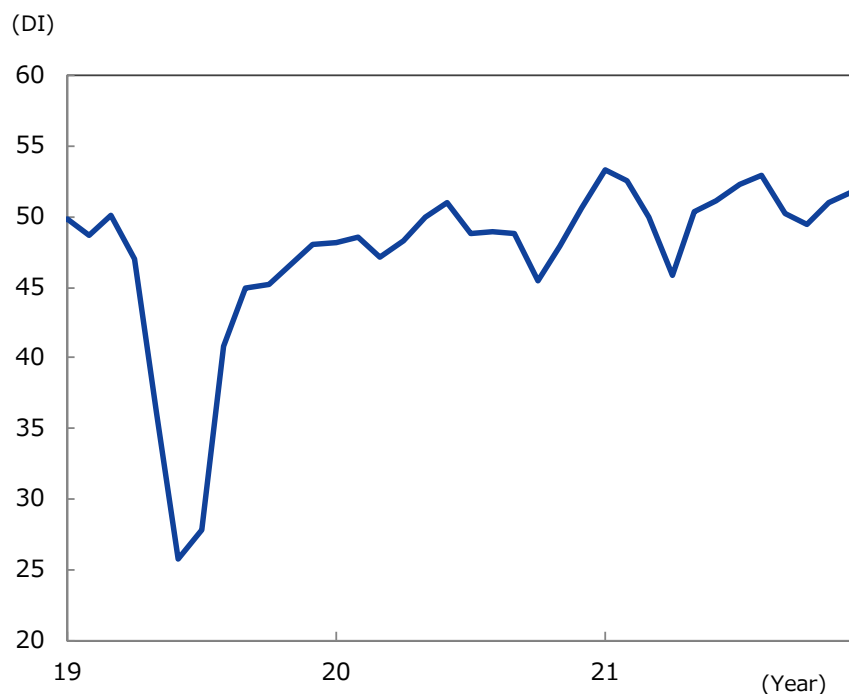
JGB, BEI, and Real Interest rate



(Data) From Jan. 1st 2014 to Oct. 18th 2022
(Source) Bloomberg, SMDAM

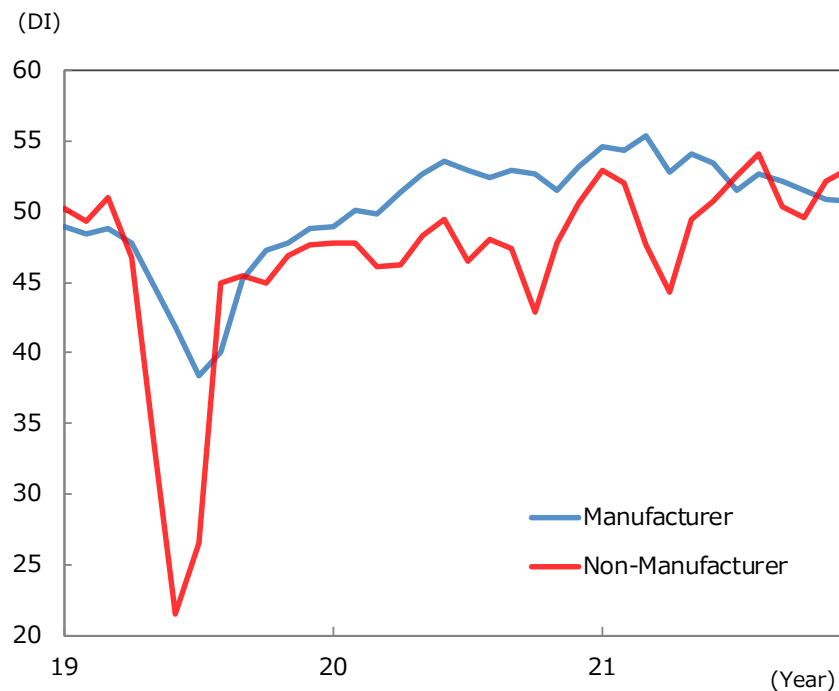
Hope for “re-opening” lifts sentiment of service businesses

Composite PMI



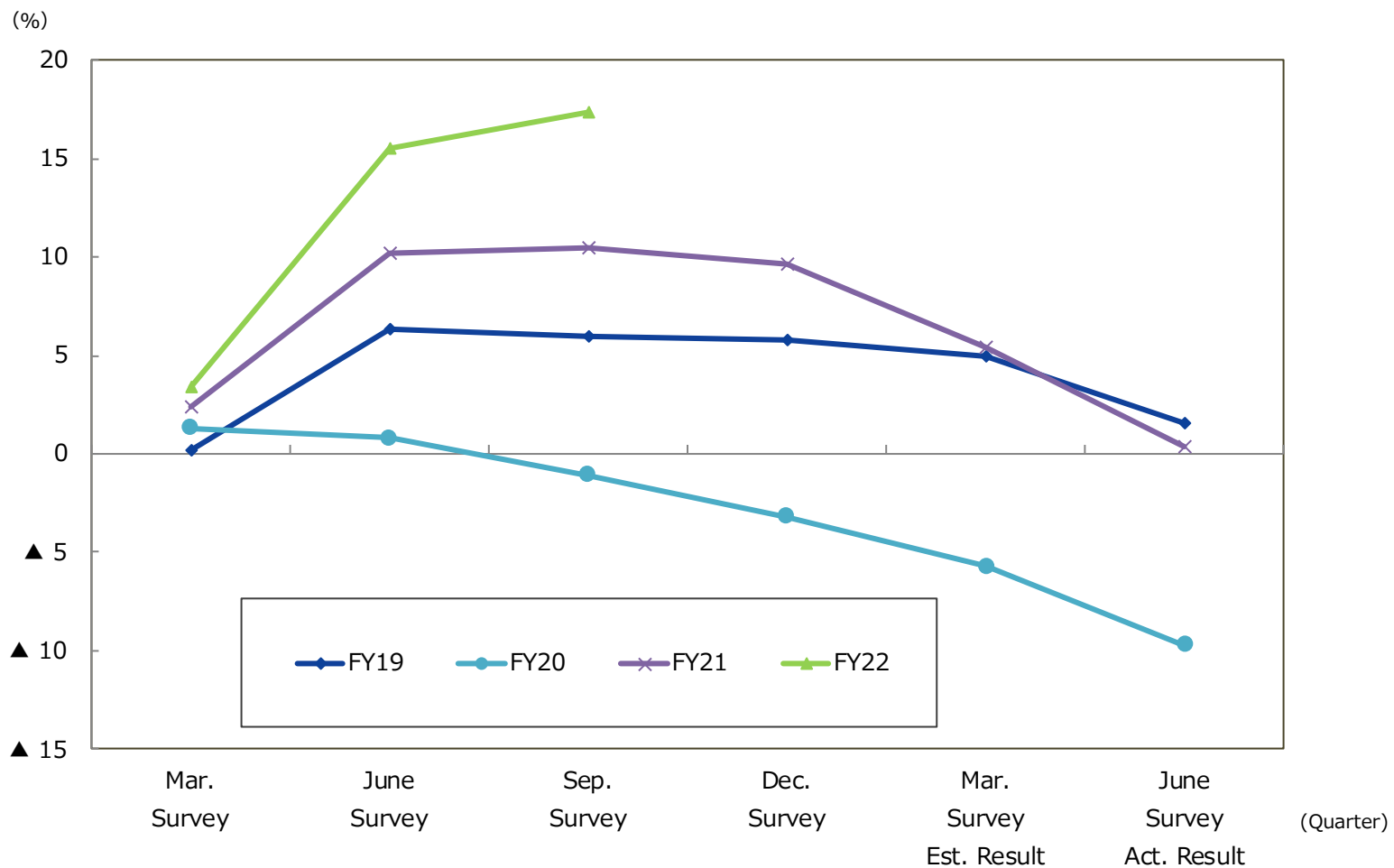
(Data) From Nov. 2019 to Oct. 2022
(Source) Bloomberg, SMDAM

PMI, Manufacturer & Non-Manufacturer



Weaker Yen and growing tension with China boost CAPEX

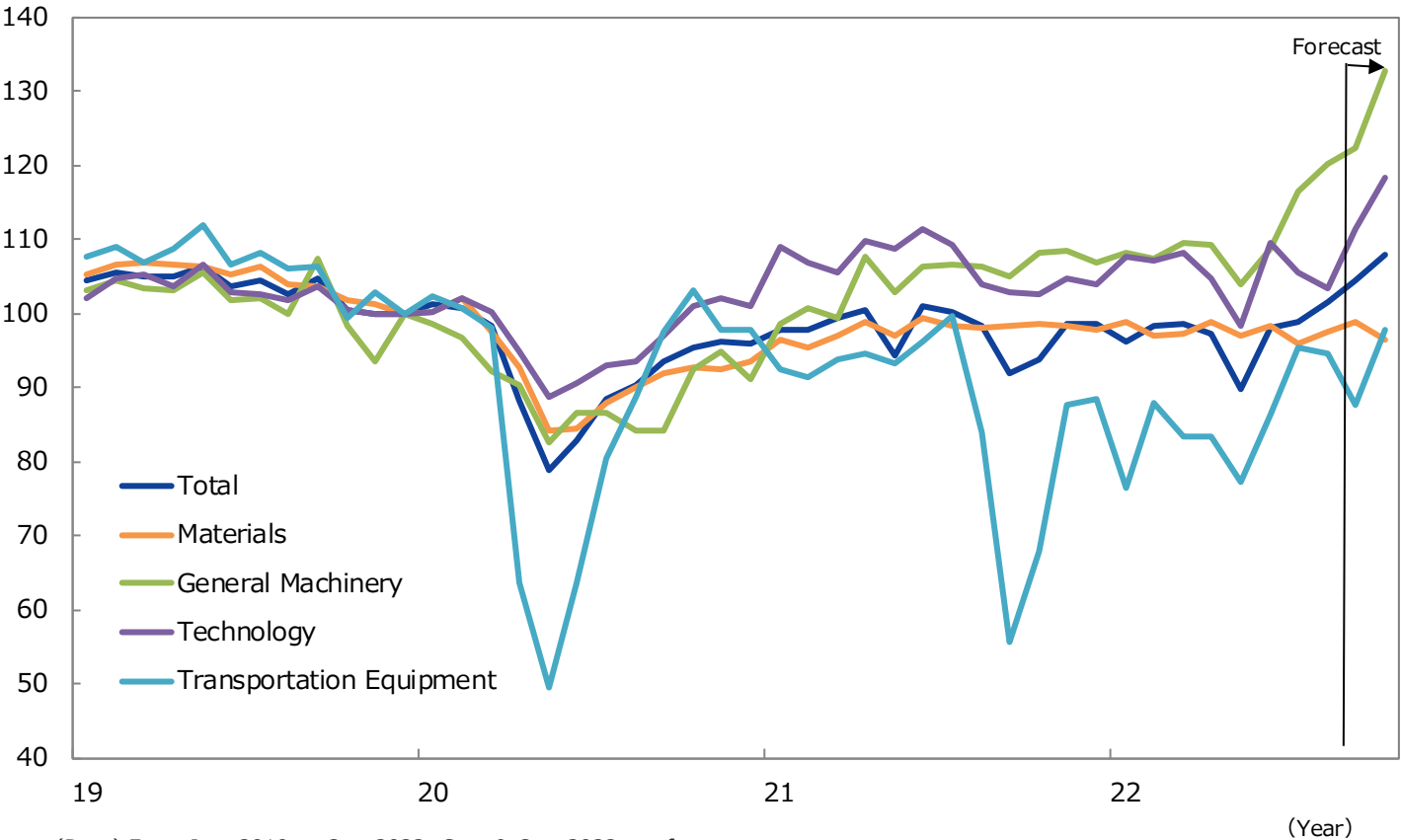
Plan of CAPEX (Inc. Software, Ex. Land and R&D, YOY)



(Data) Data is from Q1 FY 2019 to Q3 FY 2022
 (Source) The Bank of Japan, SMDAM

Brighter outlook of industrials despite the global weakness

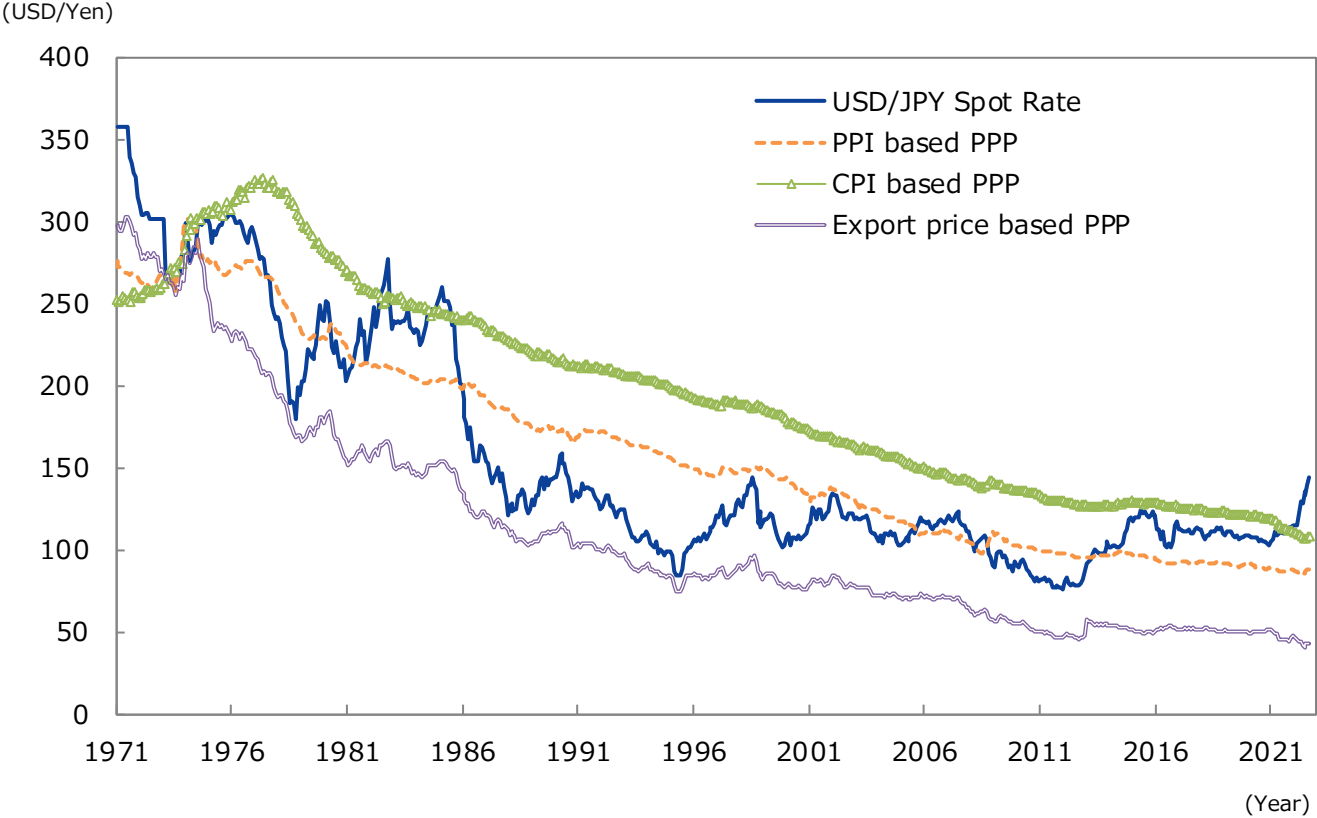
Industrial Production (Dec. 2019=100)



(Data) From Jan. 2019 to Oct. 2022. Sep. & Oct. 2022 are forecasts.
(Source) METI, SMDAM

USD/JPY exchange rate breaks 30+ years' PPP resistance

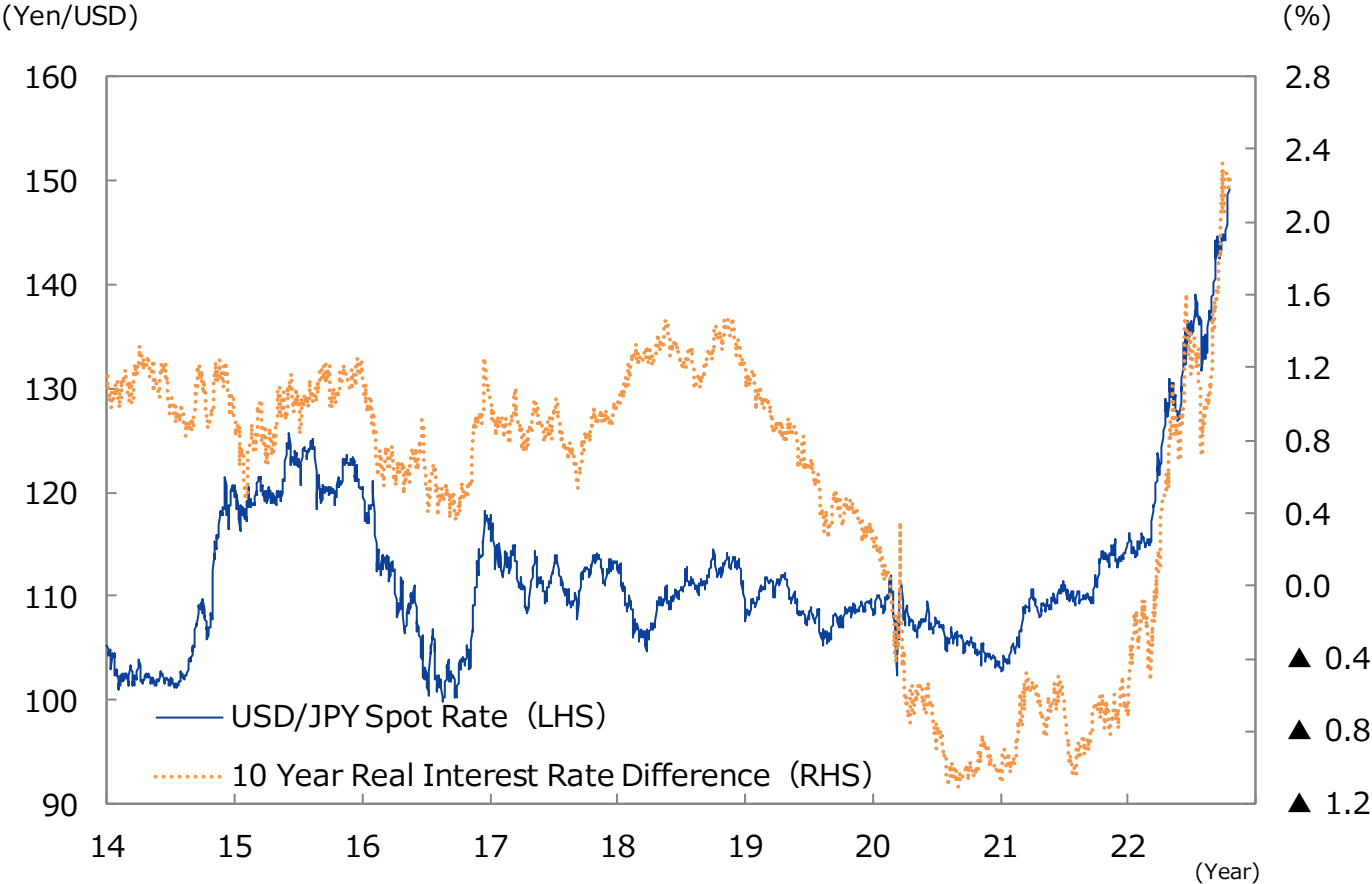
Purchasing Power Parity of USD/JPY Rate



(Data) Data is from Jan. 1971 to Sep. 2022.
(Source) DOL, Bank of Japan, SMDAM

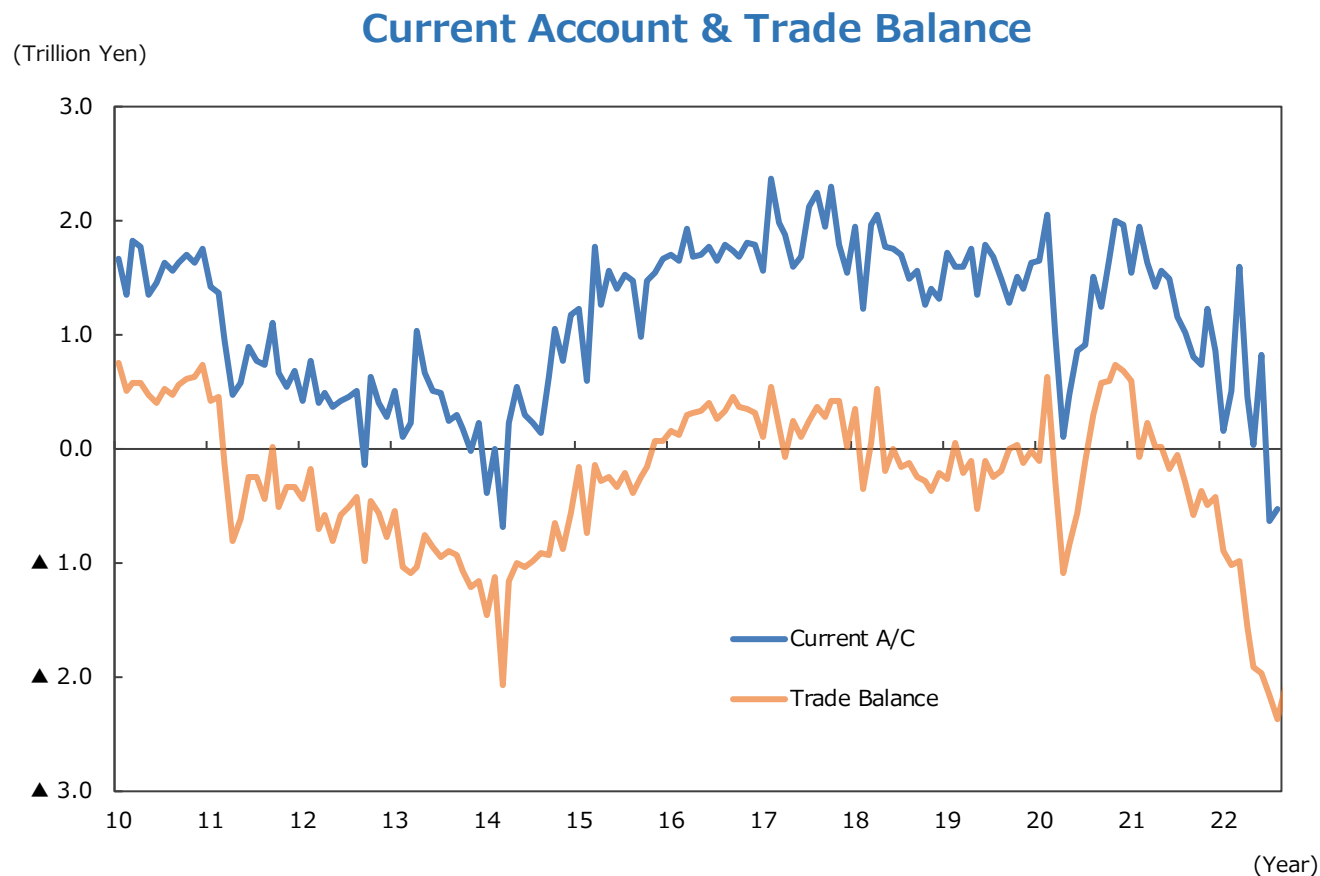
Real interest rate gap lifts dollar-yen rate sharply higher

Real Interest Rate Gap & USD/JPY Exchange rate



(Data) From Jan. 1st 2014 to Oct. 18th 2022.
(Source) Bloomberg, SMDAM

Trade & current account deficit pushes up the Dollar-Yen rate



(Data) Seasonally adjusted. Current account is from Jan. 2010 to Aug. 2022.
Trade balance is from Jan. 2010 to Sep. 2022.
(Source) MOF, SMDAM

Japan's marginal exposure to Russian business

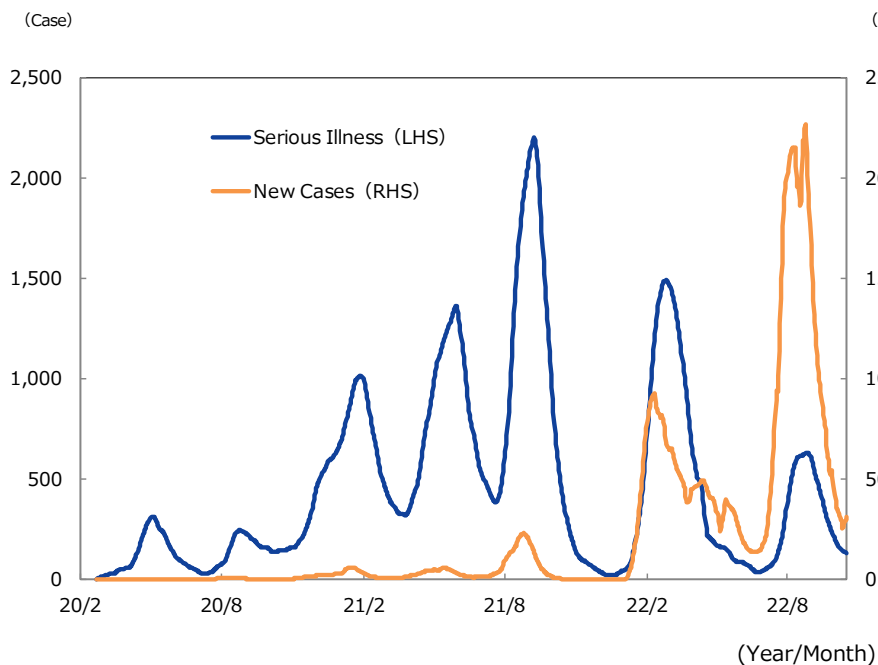
Trade Exposure to Russia (%)

	Export		Import	
	Weight of Total Export	Weight of GDP	Weight of Total Export	Weight of GDP
Total	1.04	0.16	1.82	0.28
Foods	0.01	0.00	0.17	0.03
Raw Materials	0.00	0.00	0.09	0.01
Mineral Fuel	0.01	0.00	1.12	0.17
Chemicals	0.03	0.00	0.02	0.00
Material Products	0.09	0.01	0.41	0.06
Machinery	0.21	0.03	0.01	0.00
Electronics	0.07	0.01	0.00	0.00
Transportation Equipment	0.56	0.09	0.00	0.00
Others	0.07	0.01	0.00	0.00

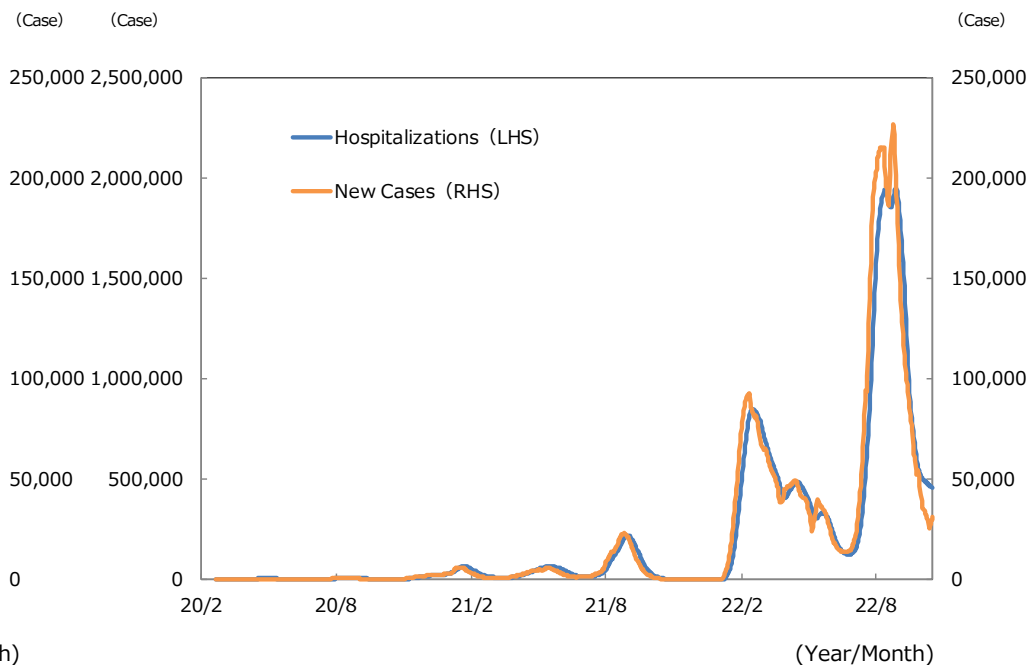
(Data) As of year 2021.
 (Source) MOF, SMDAM

The seventh wave of the COVID-19 pandemic faded sharply

COVID-19 New Cases and Serious Illness



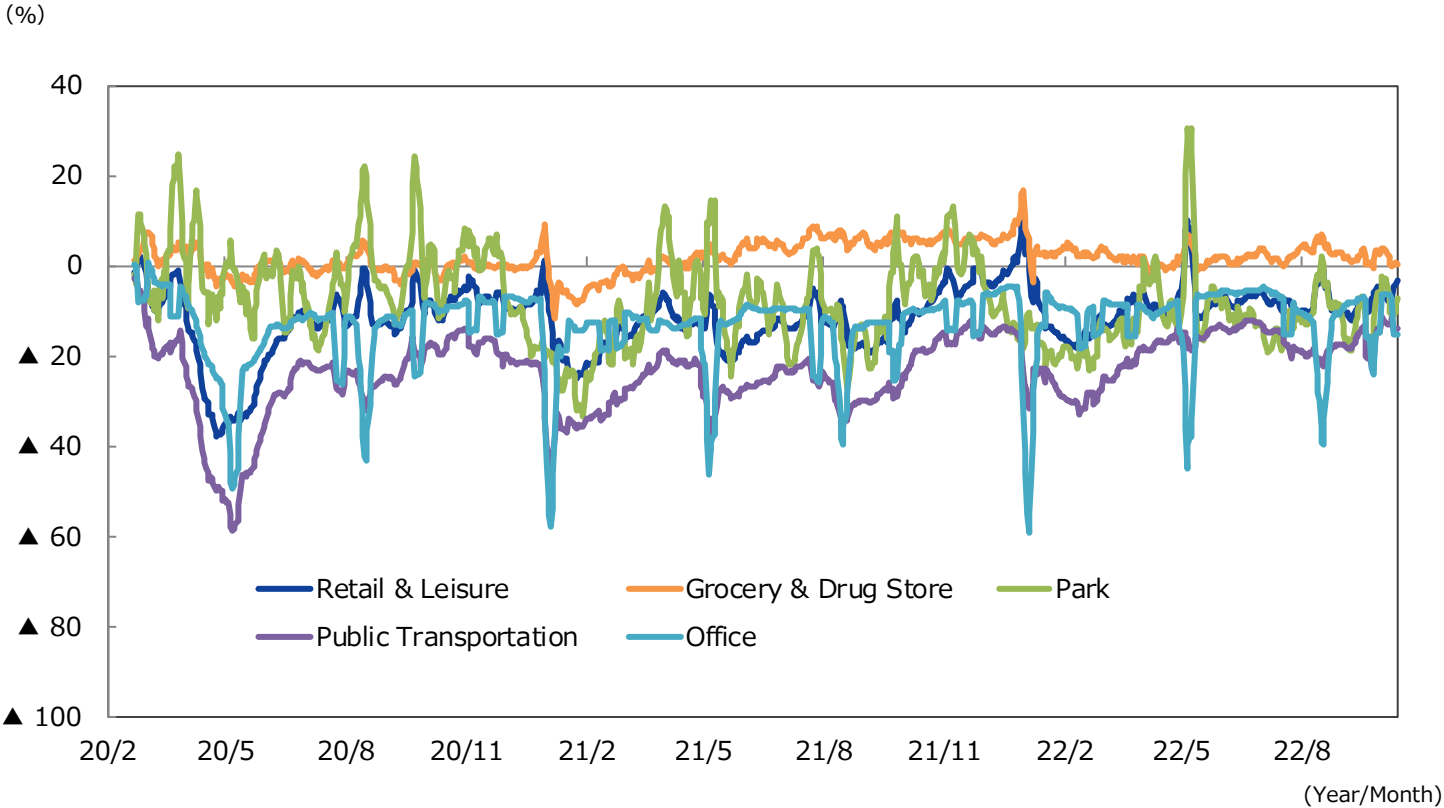
COVID-19 New Cases and Hospitalizations



(Data) 7 days moving average. From Feb. 21st 2020 to Oct. 16th 2022.
(Source) MHLW, NHK, SMDAM

Everything comes back to normal excluding office and transportation

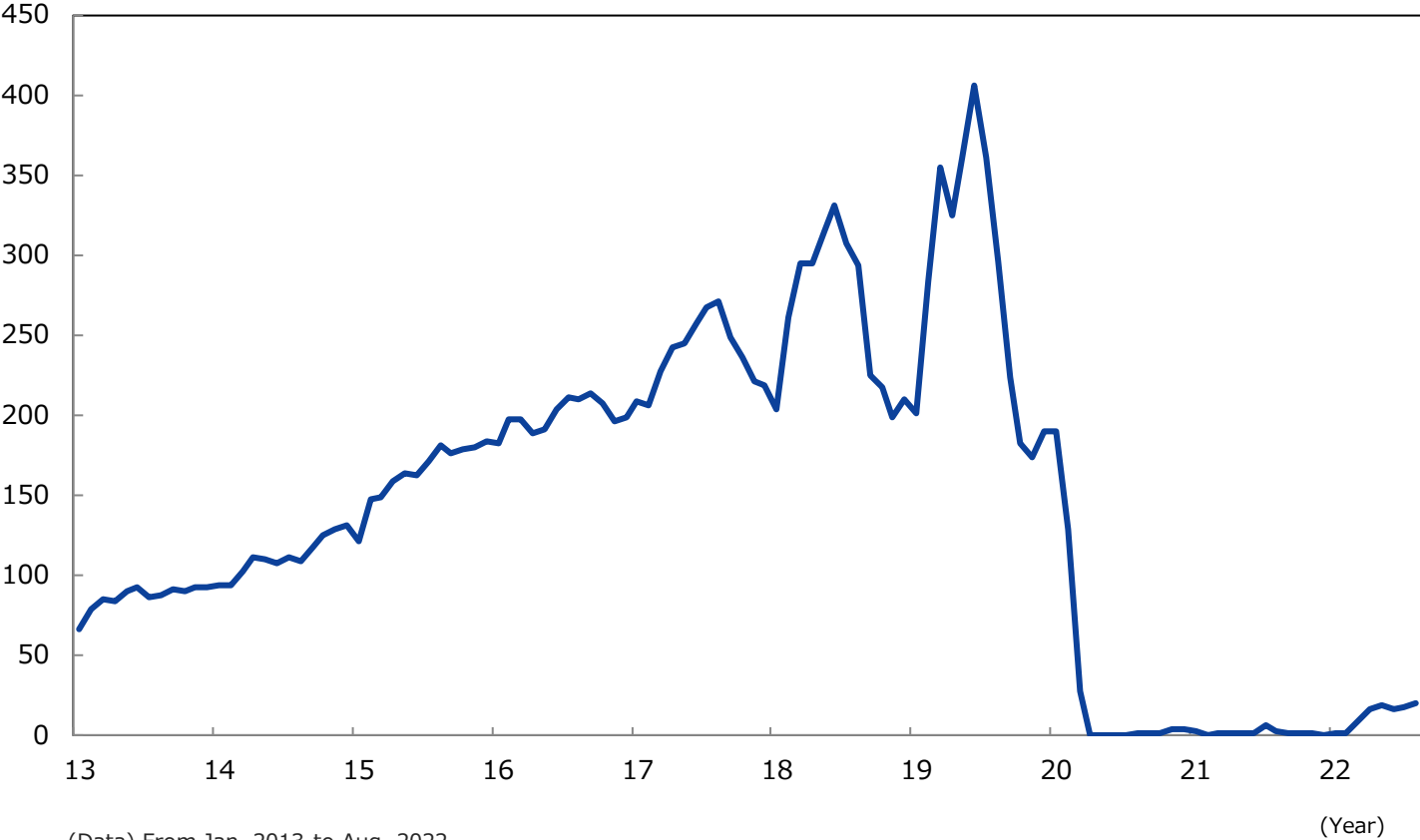
Google Community Mobility Report, Japan



(Data) 7 Days moving average, From Feb. 21st 2020 to Oct. 13th 2022
(Source) Google, SMDAM

Inbound travel starts recovering after the seventh wave of the pandemic

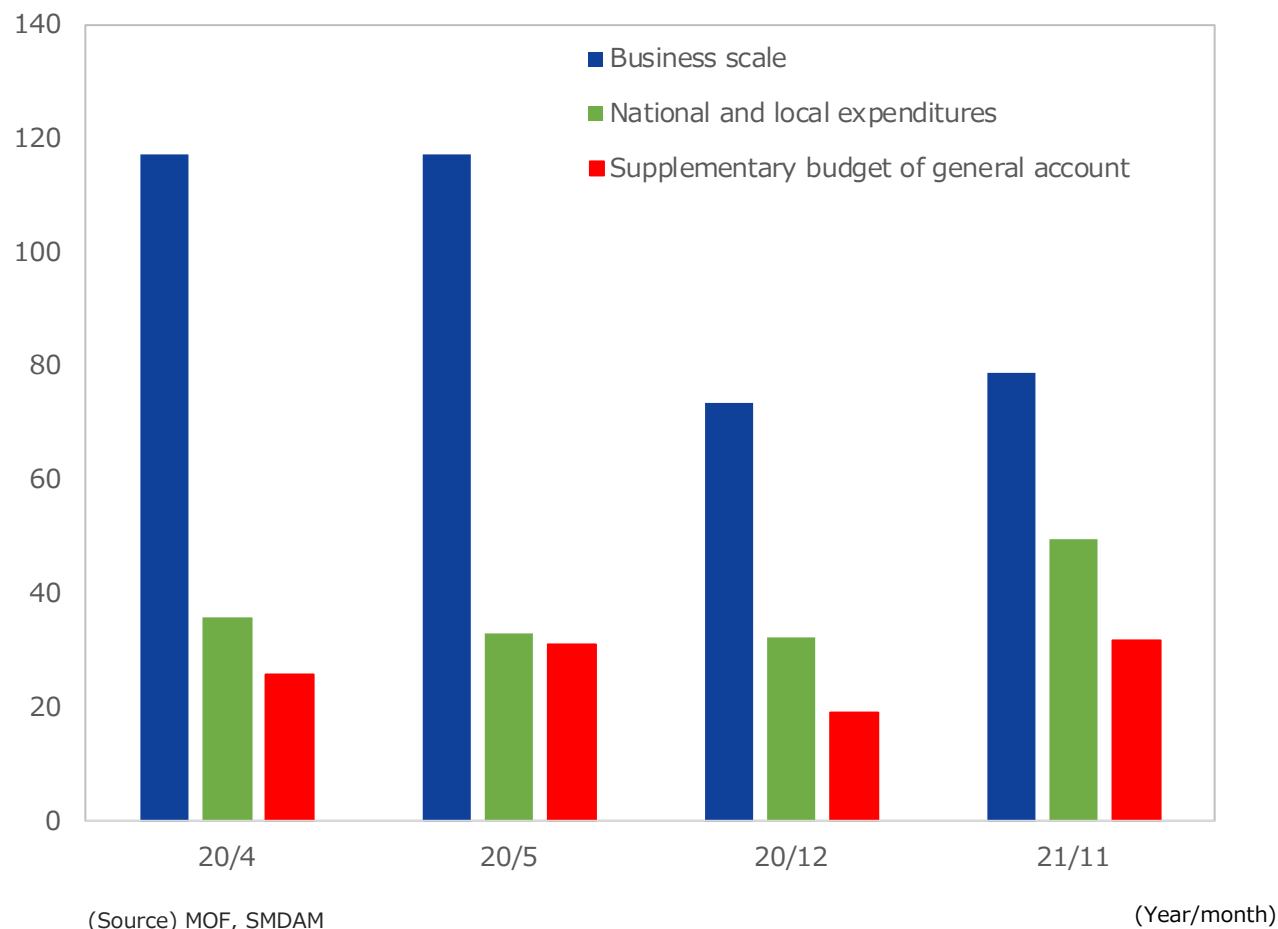
Number of foreign visitors to Japan (10,000)



(Data) From Jan. 2013 to Aug. 2022
(Source) JNTO, SMDAM

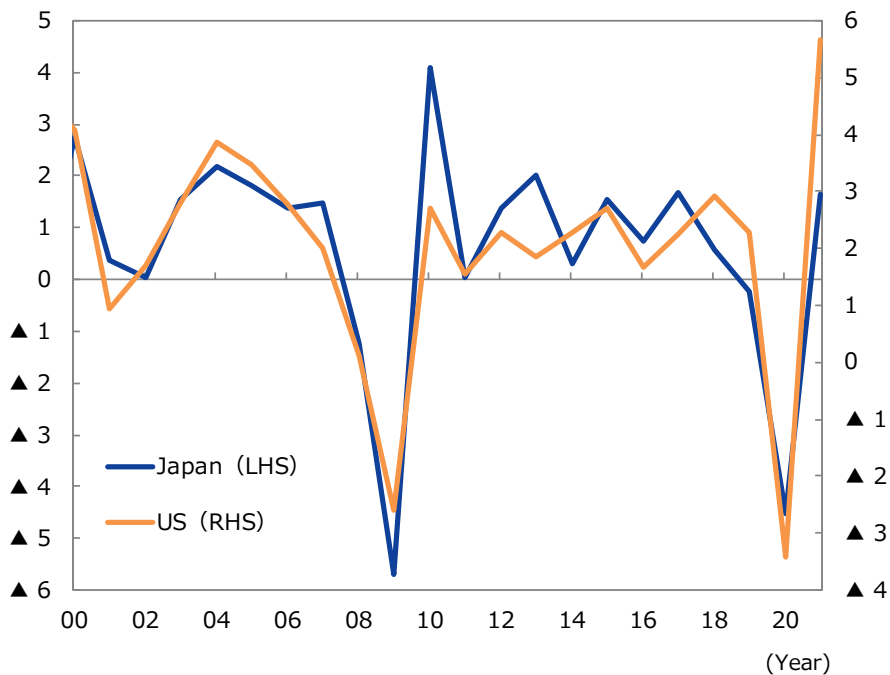
Size of economic stimulus during the COVID-19 pandemic

Economic measures against COVID-19 (trillion yen)



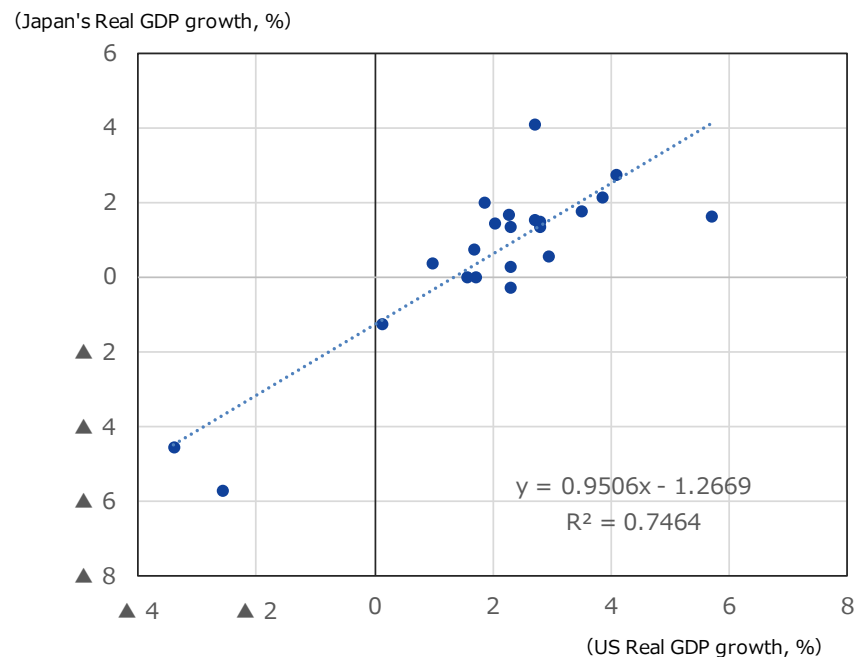
A strong correlation between GDP growth of the US and Japan

Real GDP Growth (YOY, %)



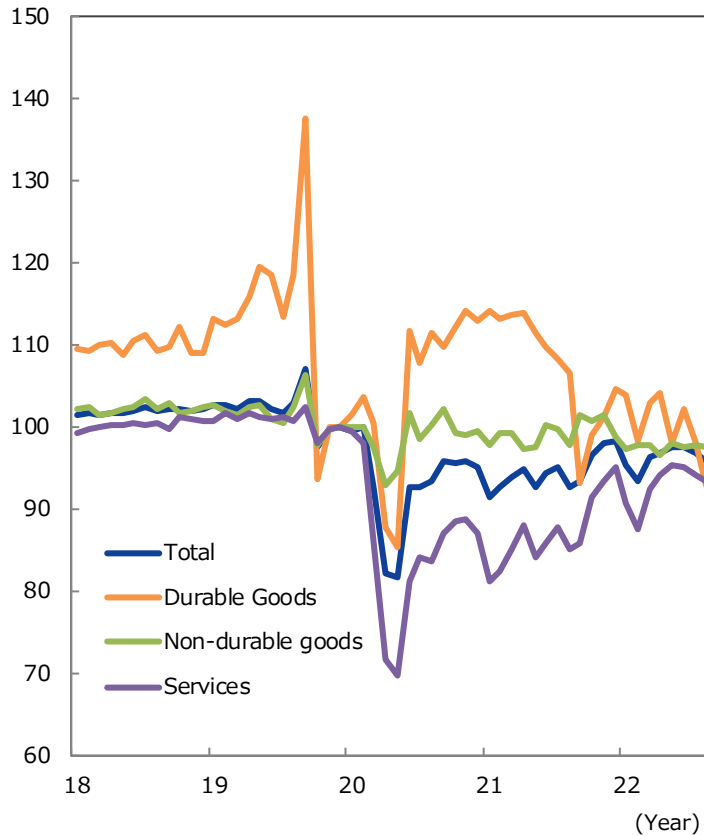
(Data) From 2000 to 2021
(Source) IMF, SMDAM

Correlation of Real GDP Growth



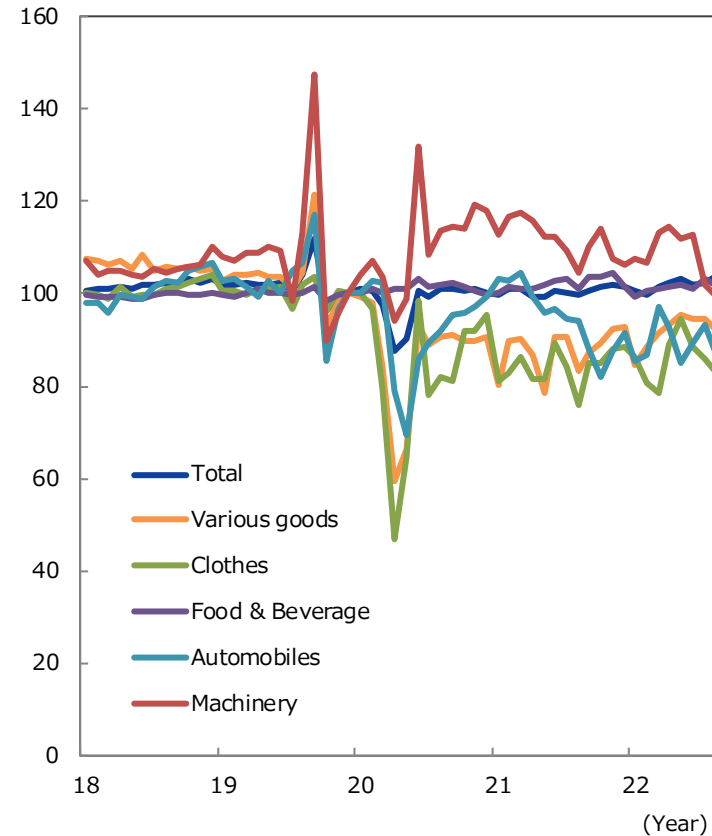
The seventh wave of COVID-19 weighed on consumers in summer

Consumer Activity Index (Dec. 2019 = 100)



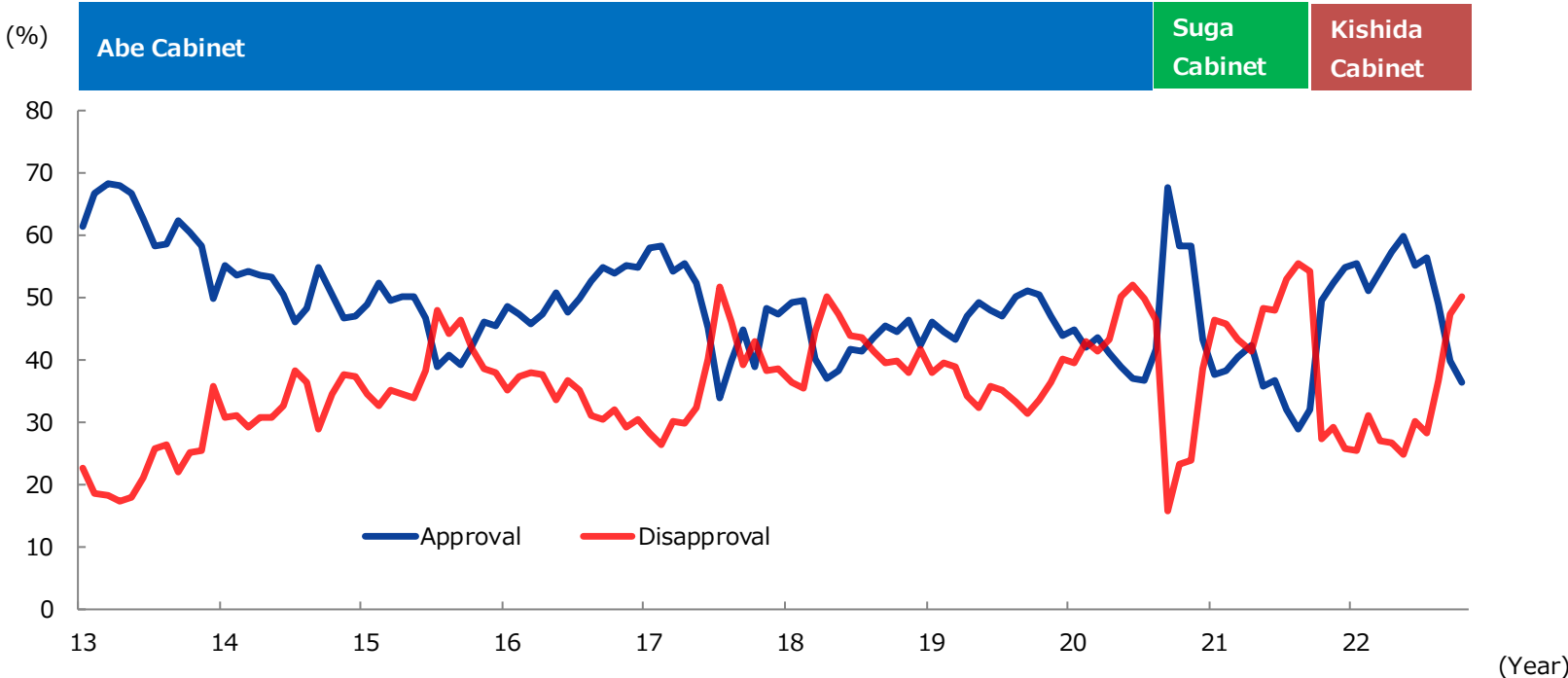
(Data) From Jan. 2018 to Oct. 2022.
(Source) Bank of Japan, METI, and SMDAM

Retail Sales (Dec. 2019 = 100)



Relationship with the “Unification Church” fueled people’s anger

Cabinet approval rate



(Data) From Jan. 2013 to Oct. 2022
(Source) NHK, Asahi, Kyodo, Nikkei, Yomiuri, Sankei, Mainichi, Jiji, and SMDAM

Schedule of major events

Schedule of Major Domestic Events			
2022	November	15 15-16	Release of CY 2022 Q3 GDP G20 Summit in Indonesia
	December	8 10 19-20	Revision of CY 2022 Q3 GDP End of extraordinary session Monetary Policy Meeting Outline of Tax Reform of FY 2023 Cabinet Decision on the Budget of FY 2023
2023	January	17-18	Monetary Policy Meeting Convocation of the ordinary diet
	February	14	Release of CY 2022 Q4 GDP
	March	9 9-10 19	Revision of CY 2022 Q4 GDP Monetary Policy Meeting Term expiration of the BOJ vice governor Amemiya and Wakatabe Enactment of the budget and tax reform bill of FY 2023
	April	8 27-28	Term expiration of the BOJ governor Kuroda Monetary Policy Meeting Nationwide local elections
	May	19-21	G7 Summit in Japan
	June	15-16	Monetary Policy Meeting Big-boned policy decisions Formulation of guidelines for the facilitation of labor mobility End of the ordinary Diet session

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

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