



Outlook for Japanese Stock Market & Economy

Sumitomo Mitsui DS Asset Management

-August 2021-

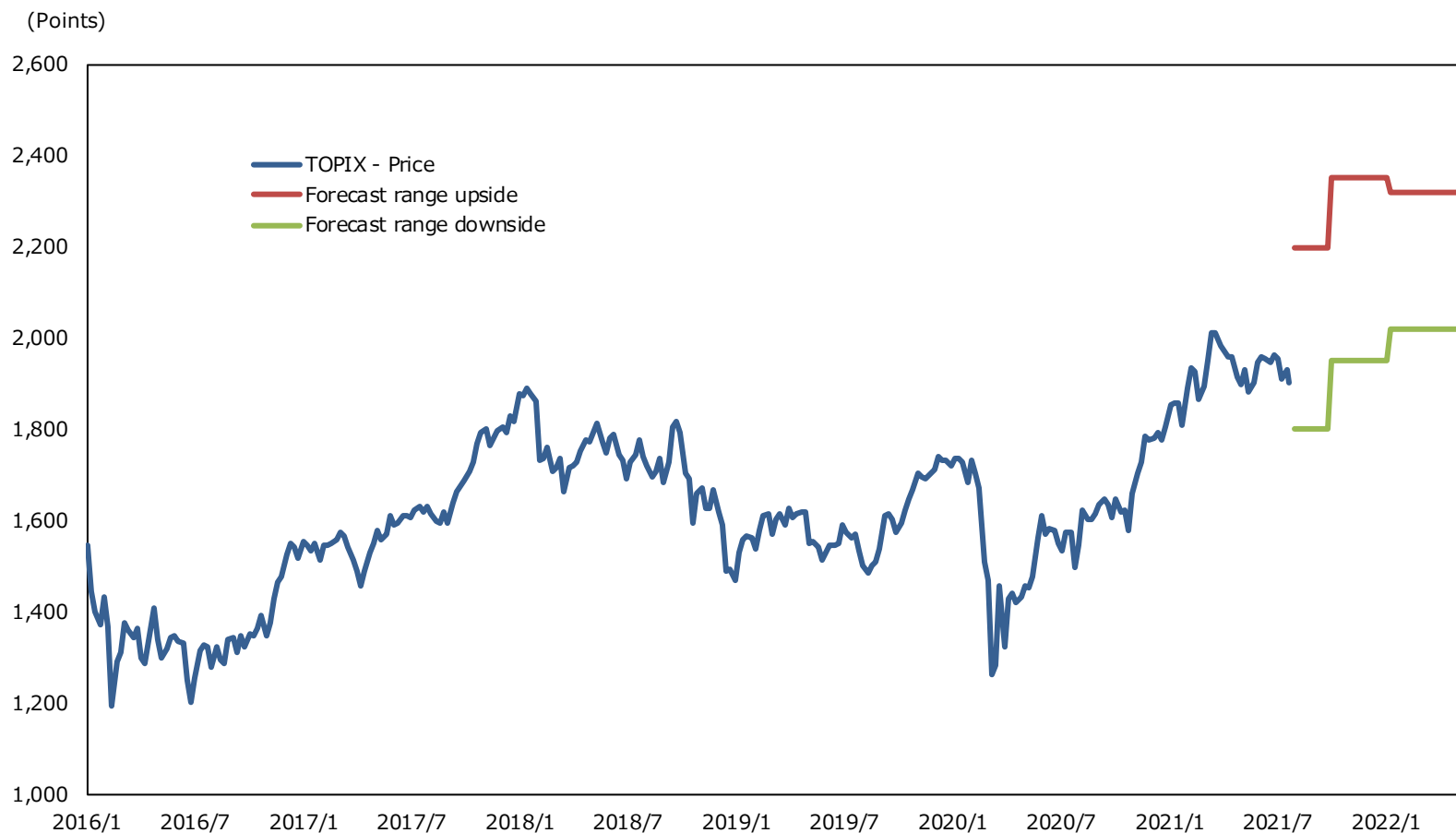


Outlook for Japanese Stock Market

Market Outlook

- We believe Japanese equity will stay on its bullish trend for the mid-to-long term backed by a strong corporate earnings recovery.
- We have lowered our TOPIX target to 2,170 from 2,220 for the current fiscal year end, with PER 16.7 times and EPS 130 points, due to the review of valuation instead of corporate earnings.
- EPS of current fiscal year could reach historical highs.
- Manufacturers are leading the growth of corporate earnings and non-manufacturers are expected to follow after Autumn thanks to the progress of vaccinations.
- Worries about the COVID-19 Delta variant, uncertainty over politics, and concerns for US monetary policy could weigh on investors' appetite for riskier assets in the short term.

TOPIX Index and Forecast



Note: TOPIX data is from Jan. 1st 2016 to July 21st 2021
(Source) TOPIX: Tokyo Stock Exchange, forecast by SMDAM

(Year/Month)

Upside / Downside Risk

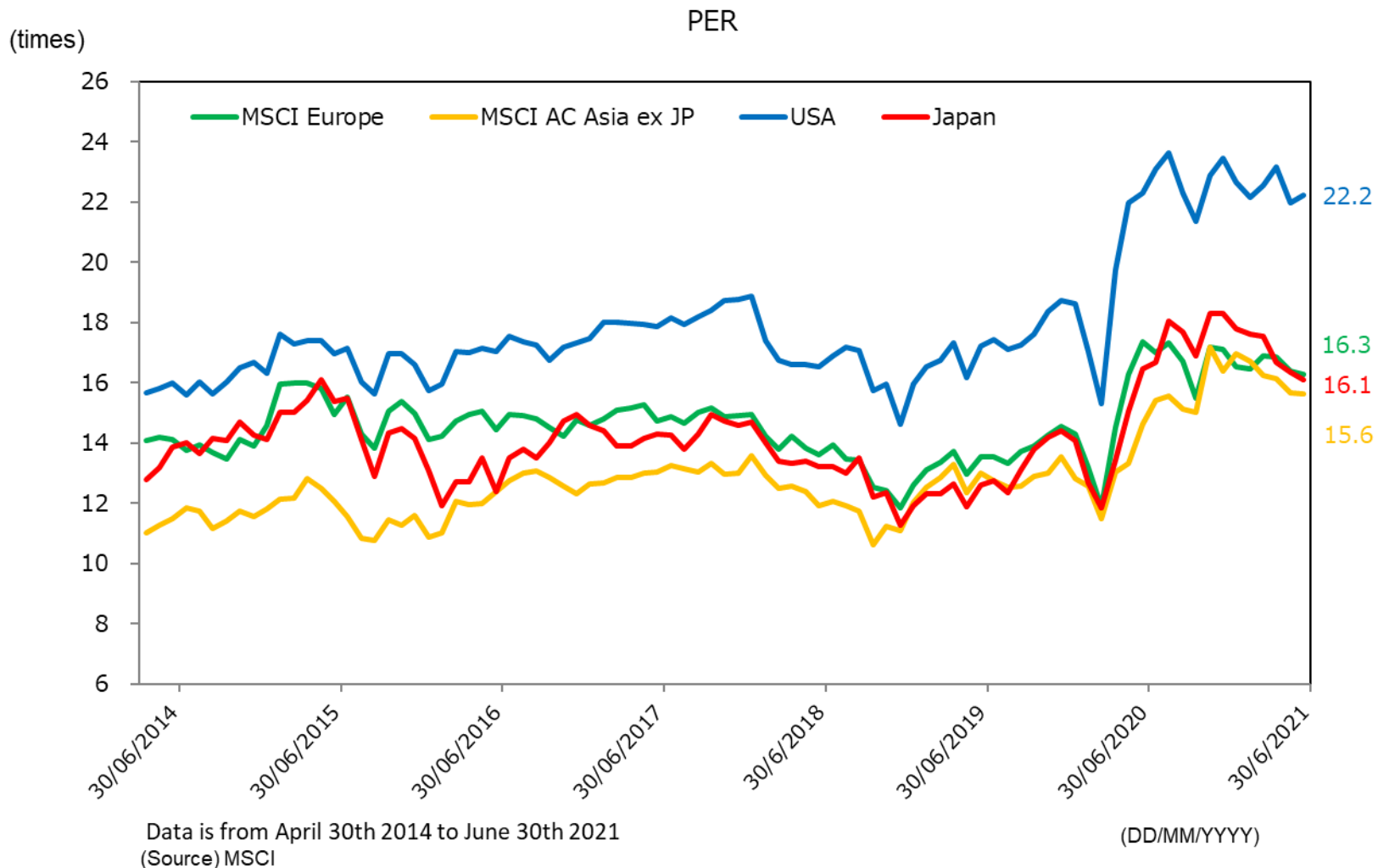
■ Upside Risks

- Strong recovery of domestic demand thanks to the progress of COVID-19 vaccinations
- Positive corporate earnings surprise
- Acceleration of global economic growth in and after CY 2022

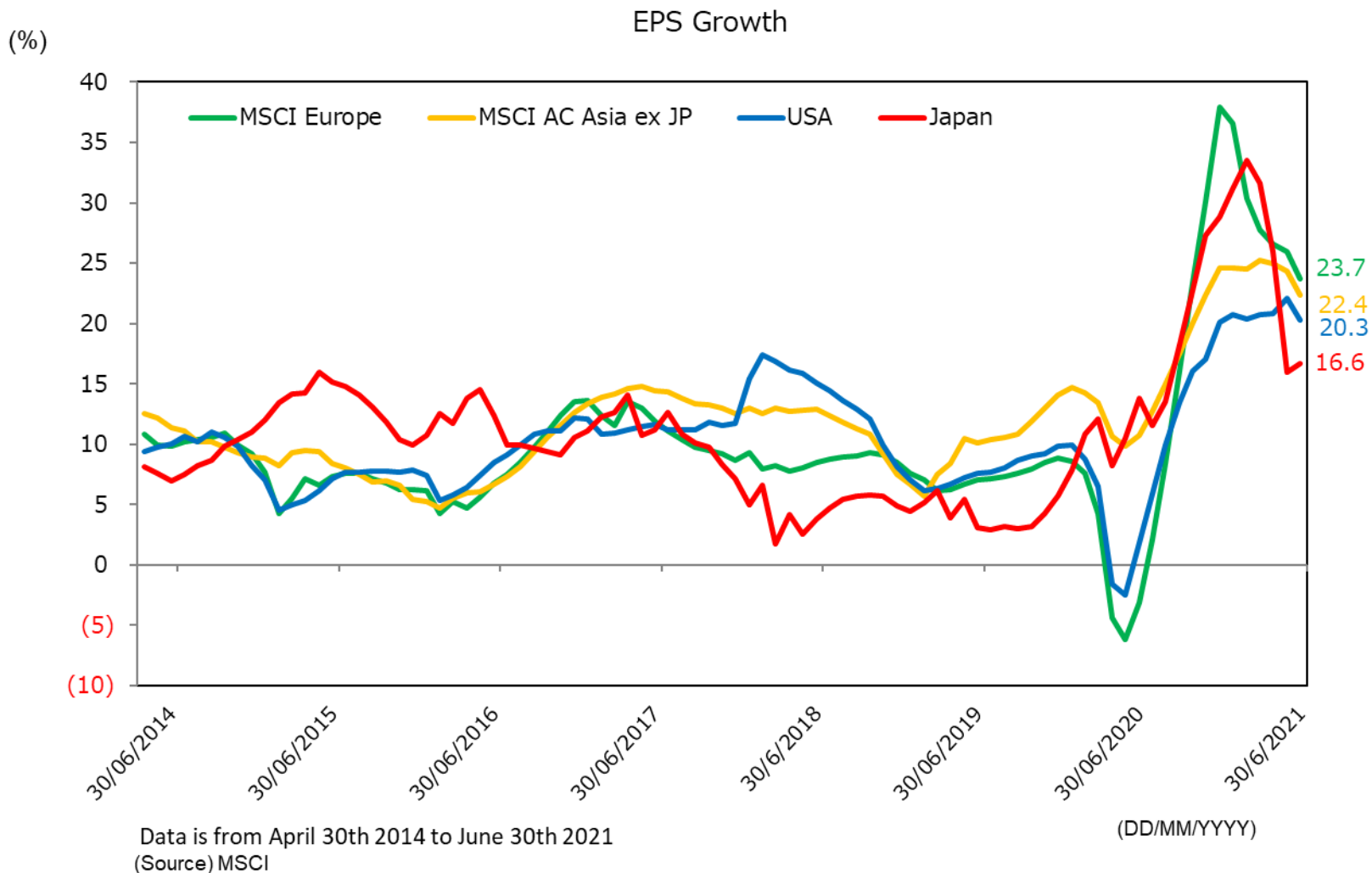
■ Downside Risks

- Concerns for US monetary policy owing to unexpectedly high inflation and wage increase
- Delay of normalization of global economy due to COVID-19 new variant
- Worry for the sustainability and the effectiveness of current fiscal and monetary policy

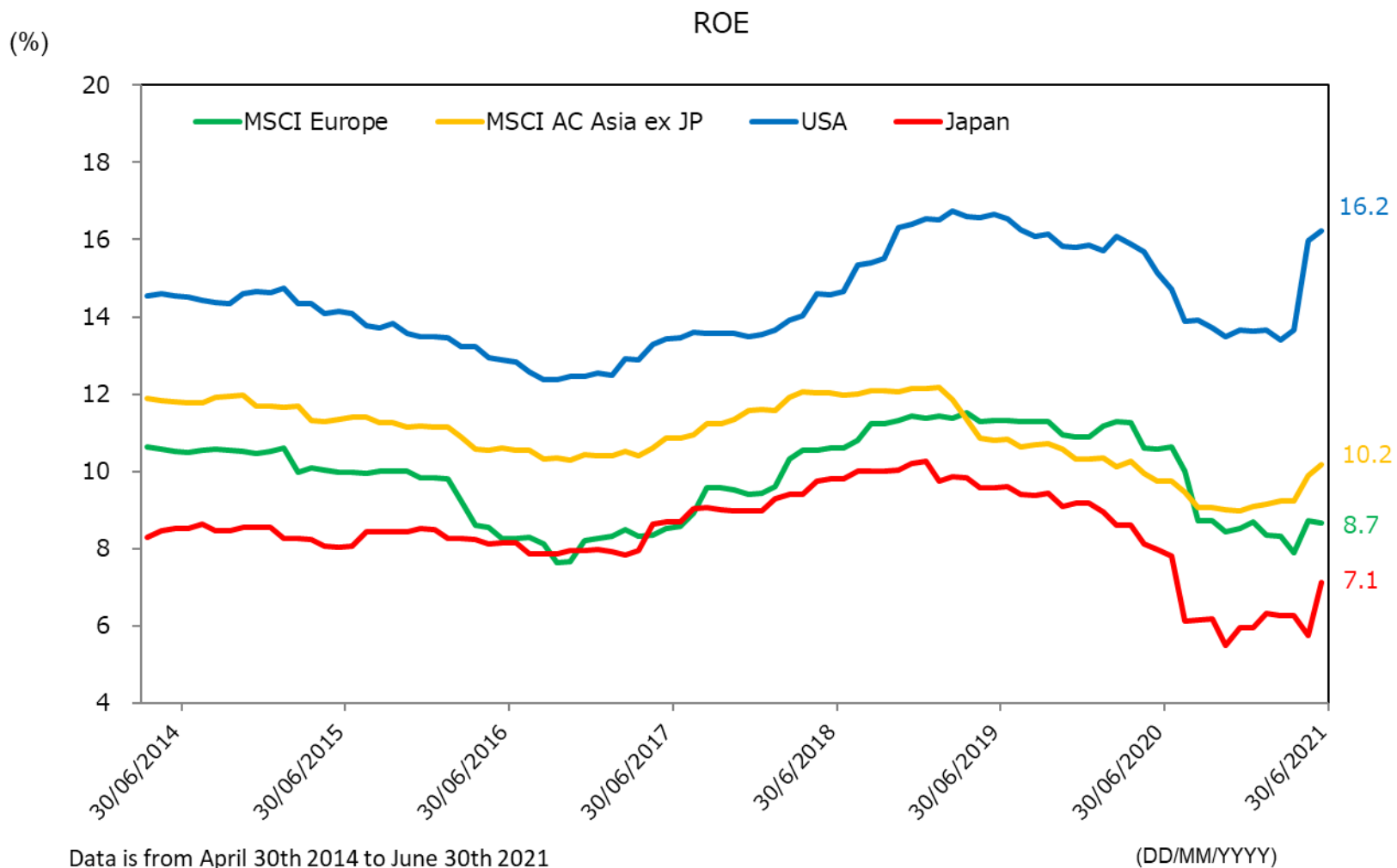
Global Comparison of Key Valuations: PER



Global Comparison of Key Valuations: EPS

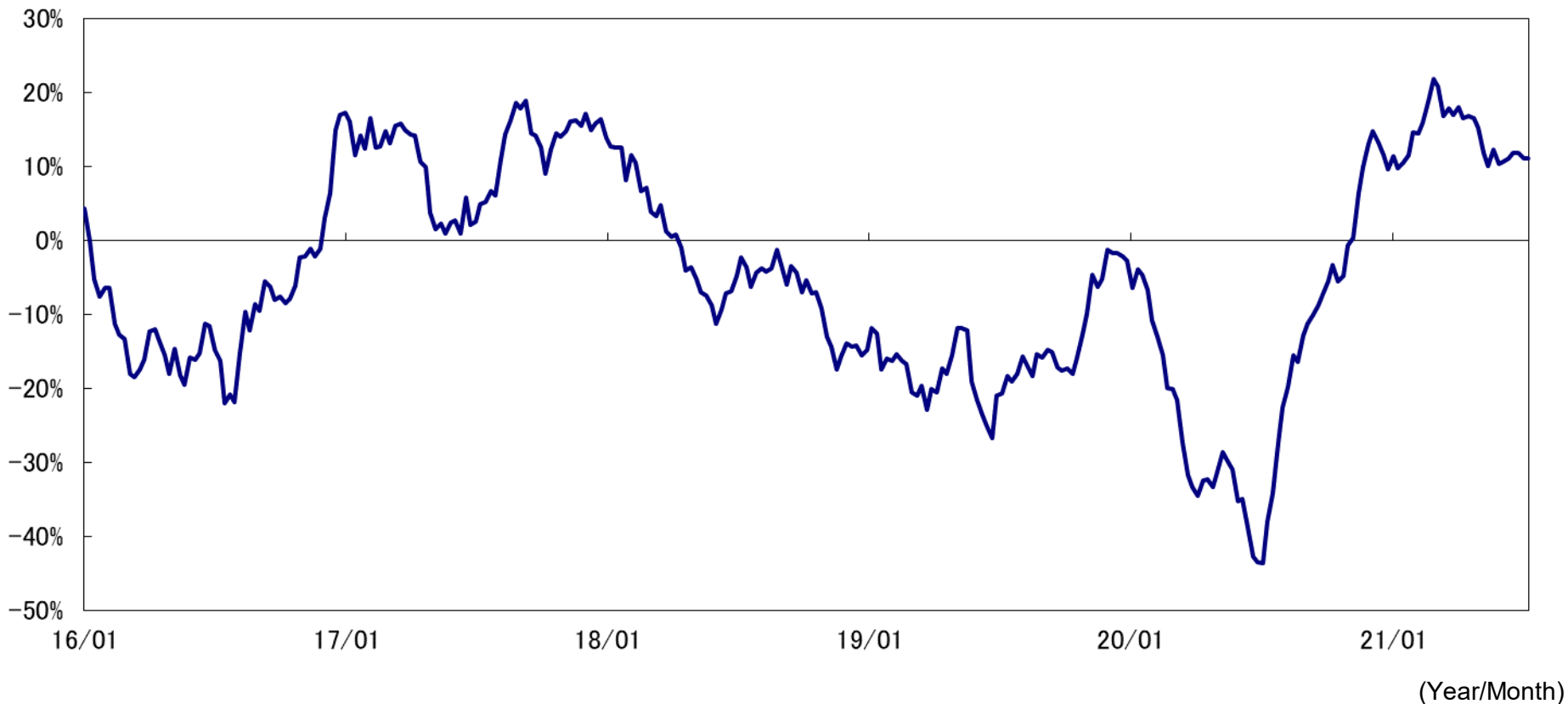


Global Comparison of Key Valuations: ROE



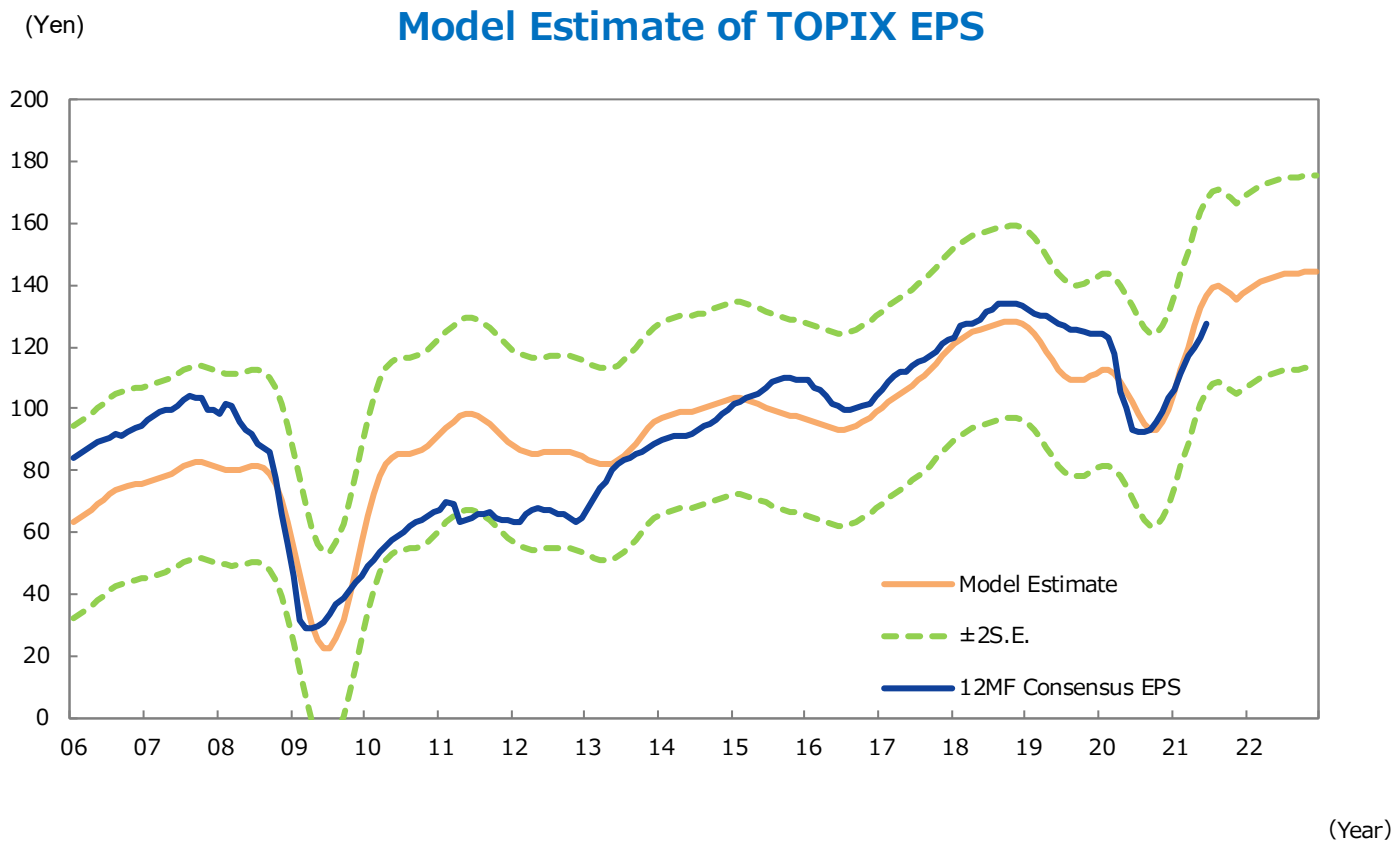
Revision of Earnings Forecasts

TOPIX Revision Index



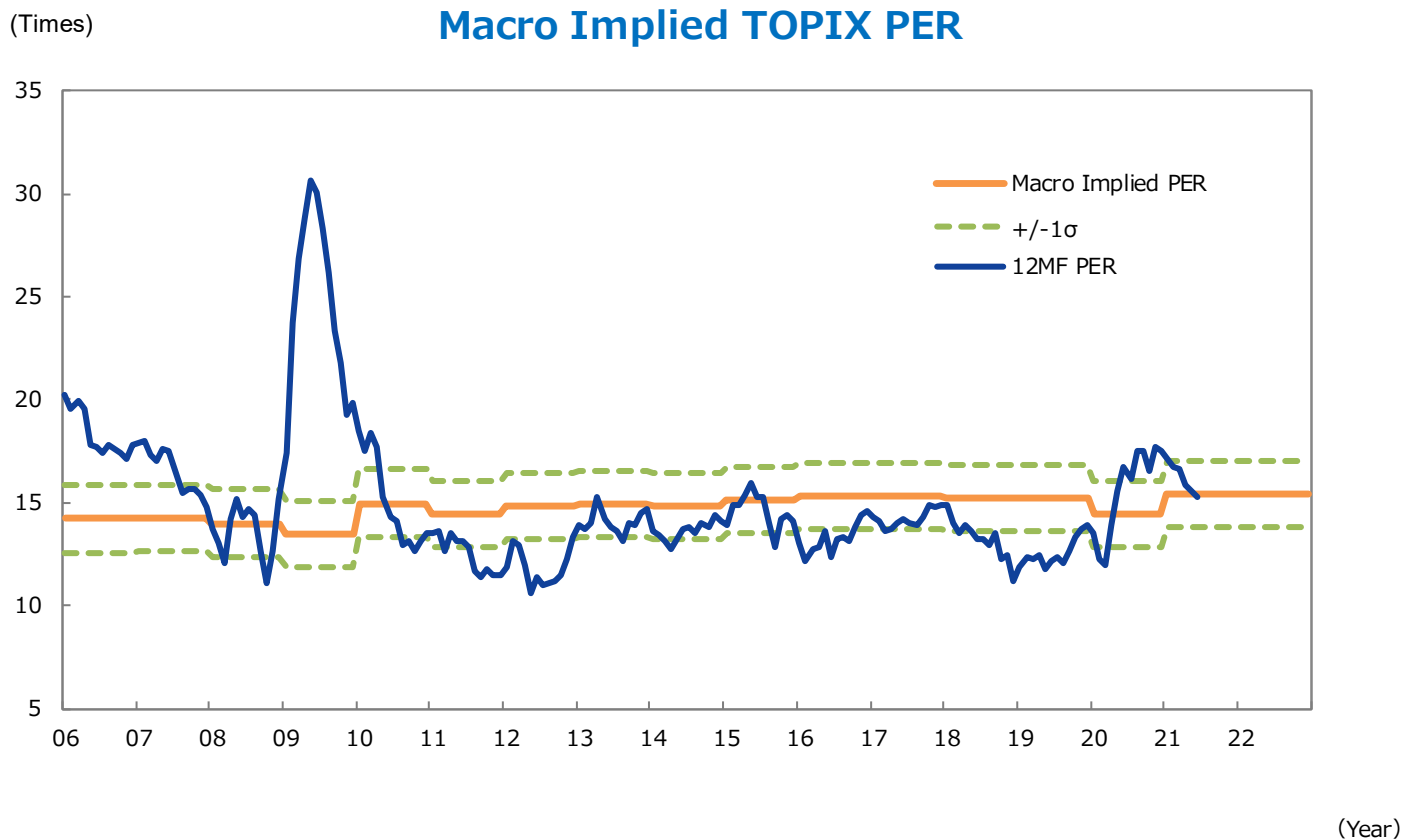
Data is from January 4th 2016 to July 12th 2021
(Source) Datastream, IBES

Top Down Approach, Model Implied Fair Value



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

Top Down Approach, Model Implied Fair Value

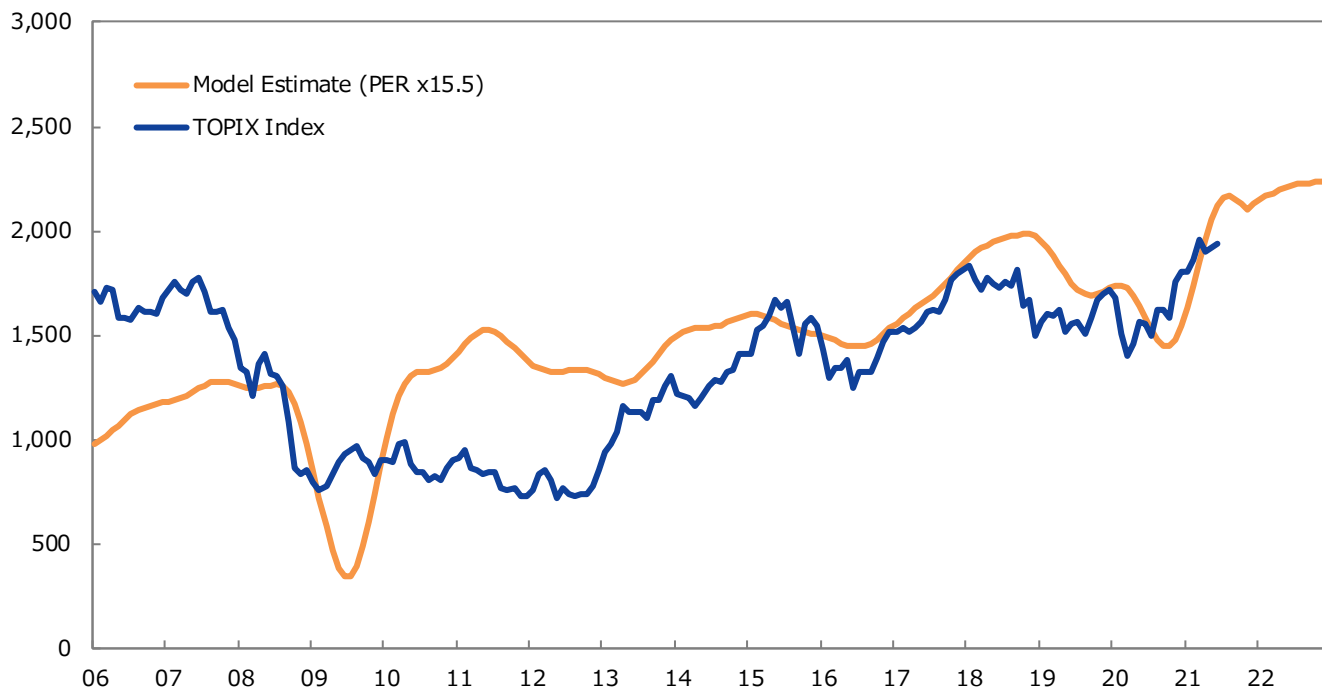


12MF PER data is from Jan. 2006 to June 2021, Model data is from Jan. 2006 to Dec. 2022.

(Source) SMDAM

Top Down Approach, Model Implied Fair Value

Model Estimate of TOPIX Fair Value



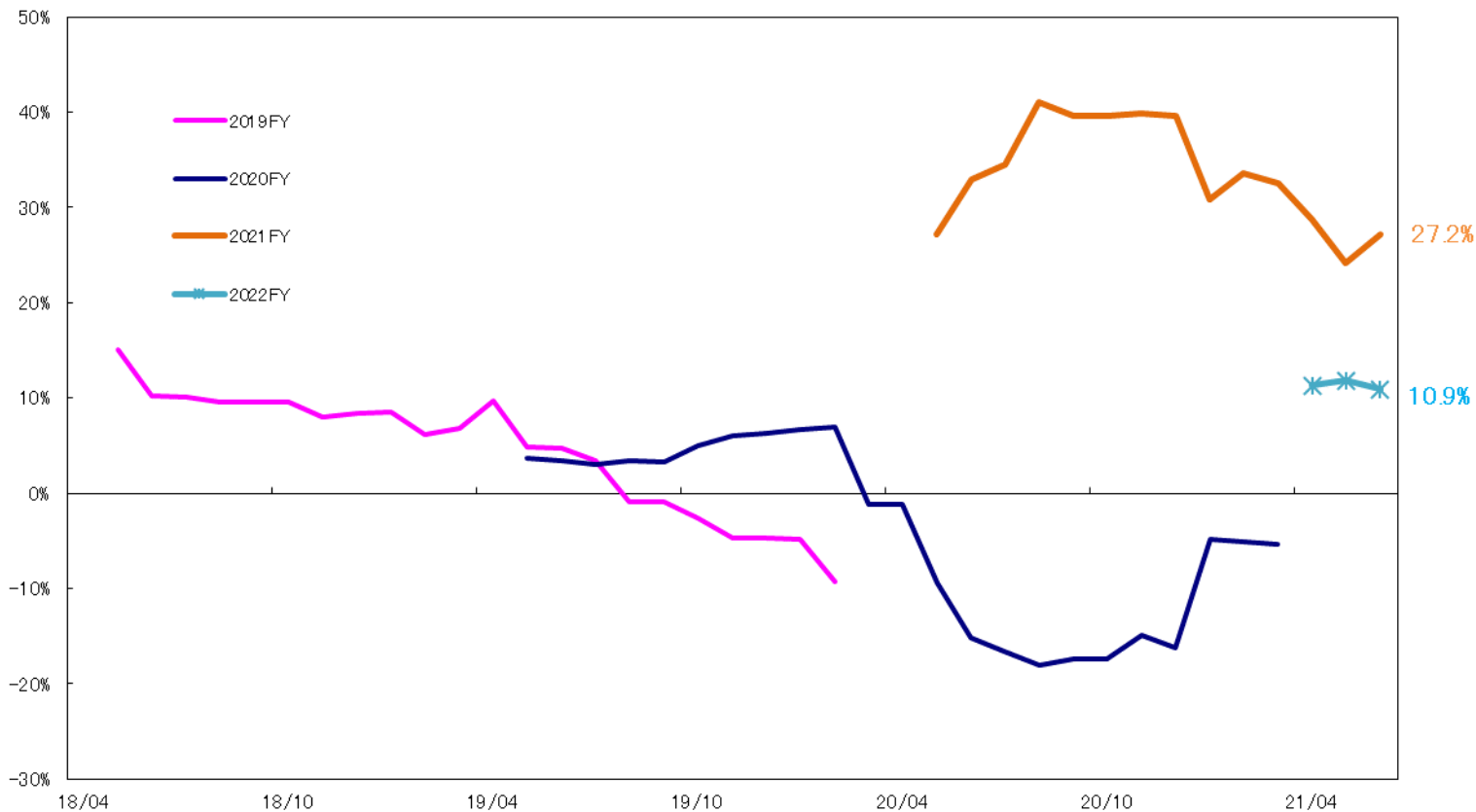
(Year)

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

(Source) SMDAM

Bottom Up Estimate, Corporate Earnings

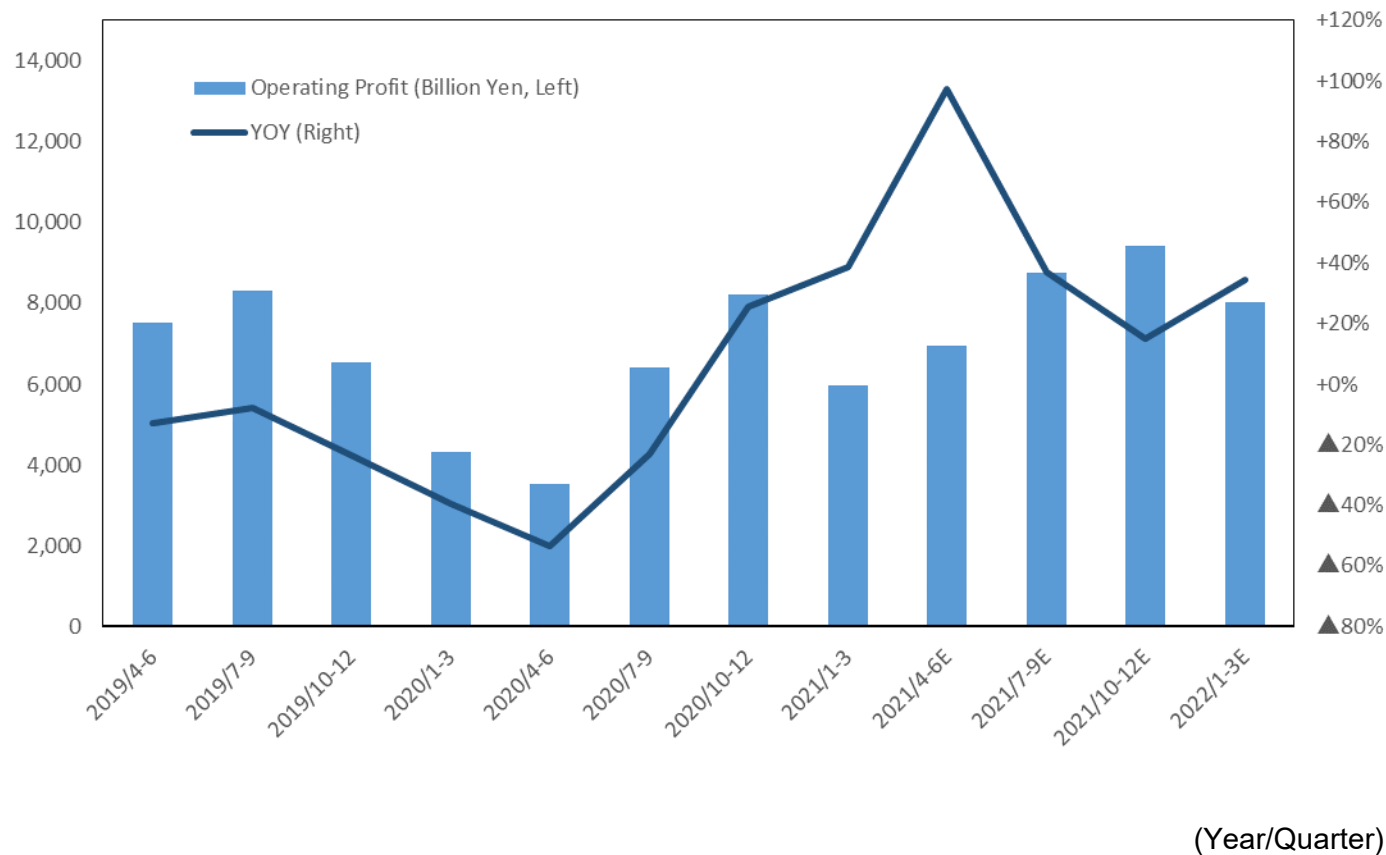
SMDAM Core Research Universe (Ex-Financial) Est. of Recurring Profit Growth



Note: Data is as of July 15th 2021, SMDAM Core Universe consists of 488 major Japanese companies covered by SMDAM in-house analysts.
 (Source) SMDAM

Bottom Up Estimate, Corporate Earnings

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



(Source) SMDAM

Corporate Governance Code and Stewardship Code

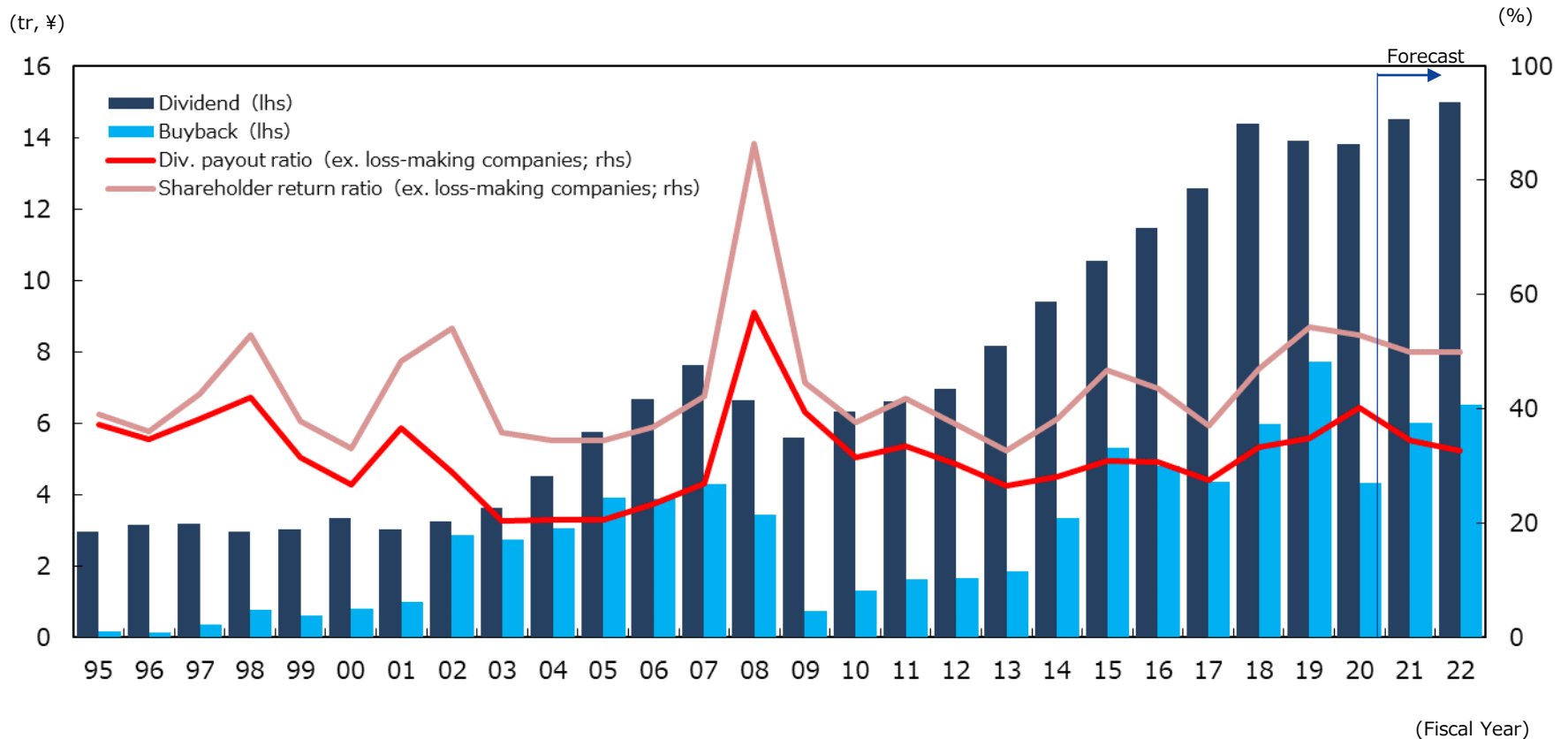
Investors that have signed up to the Principles for Responsible Institutional Investors	
Trust banks	6
Investment managers	199
Insurance companies	24
Pension funds	68
Others	12
Total	309

note: As of June 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 the 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 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



Note: Data is from FY1995 to FY2022, FY2021 and FY2022 are forecast of Toyo-Keizai in dividend and of Daiwa Securities in share buybacks.

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

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	-1.33	4.26	7.49	22.87	24.52	13.10	48.72
Total Value	-0.23	10.01	14.25	24.05	11.96	1.26	34.46
Top Cap Value	1.92	12.53	17.28	28.09	18.19	9.87	41.50
Large Cap Value	0.08	10.50	15.22	24.99	12.11	2.79	34.92
Mid Cap Value	-2.13	8.05	12.74	21.23	3.71	-7.04	25.43
Small Cap Value	-1.69	7.77	9.93	19.78	11.31	-5.52	31.71
Micro Cap Value	-0.57	6.59	8.23	16.24	10.04	-5.22	35.65
Total Growth	-2.36	-1.59	0.71	18.96	34.53	24.14	62.73
Top Cap Growth	-2.69	-2.13	0.88	20.88	37.75	30.12	69.76
Large Cap Growth	-2.51	-2.12	0.39	19.26	36.45	26.29	64.10
Mid Cap Growth	-2.21	-2.10	-0.44	16.56	34.25	20.40	55.80
Small Cap Growth	-0.82	4.07	3.99	16.37	19.85	8.25	50.86
Micro Cap Growth	-1.10	5.34	5.84	20.56	23.42	14.30	59.69
Top Cap Total	-0.54	4.37	8.10	24.34	28.44	20.26	55.56
Large Cap Total	-1.21	3.91	7.41	22.51	25.39	15.44	50.19
Mid Cap Total	-2.16	3.25	6.43	20.05	21.13	8.63	42.68
Small Cap Total	-1.61	6.59	8.00	19.56	15.54	0.30	40.14
Micro Cap Total	-0.72	6.22	7.52	18.05	14.96	1.83	45.02

Note : As of July 15th 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 +3.8% (previously +3.8%) in FY 2021, and +2.9% (+2.4%) in FY 2022.** We have revised upward our GDP growth forecast for FY 2022 on the assumption of large-scale fiscal stimulus. GDP growth forecast for FY 2021 remains unchanged, taking into account downward revision caused by the reissuance of the state of emergency in Tokyo and an upward revision caused by the effects of fiscal stimulus. On a quarterly basis, we forecast economic recovery after Q3 FY2021. In addition to the progress of vaccinations, increased external demand and recovery of automobile production are major drivers of economic growth. In and after Q1 FY 2022, additional fiscal stimulus is expected.
- ② **The nationwide core CPI is +0.8% (previously +0.4%) in FY 2021, and +0.9% (previously +0.6%) in FY 2022.** The main reasons for the upward revision were change in the assumption of the WTI from 65 dollars to 75 dollars per barrel and the dollar yen exchange rate from 107.5 yen to 110.0 yen per one dollar. The year-on-year rate of change in the nation wide core CPI is likely to increase toward the end of FY 2021, led by energy. However, the supply-demand balance is accommodative, and the underlying inflationary pressure will be limited.
- ③ **The overall monetary policy framework is likely to be maintained for the time being. Further monetary easing will be taken only in case of emergency, such as excessive appreciation of currency.** In the "Review to Implement More Effective and Sustainable Monetary Easing," the Bank of Japan has proposed measures to deal with the side effects of large-scale monetary easing, such as more flexible purchasing policies for ETFs and J-REITs and clarification of the range of fluctuations in long-term interest rates, and the outline of monetary policy will be maintained for the time being. The Bank of Japan has established a new interest rate system to promote lending and has made it clear that there is room for rate cuts, but further rate cuts will be limited to emergencies, such as the soaring yen. It was decided to introduce funding for climate change, and it is scheduled to be implemented within FY 2021.
- ④ **An outline of additional economic measures is likely to be presented before the general election in autumn. The supplementary budget for fiscal 2021 is likely to increase in size to 30 trillion yen.** The government and the ruling parties are increasingly calling for an increase in public spending amid the uphill battle in the Tokyo Metropolitan Assembly election, the reissuance of a declaration of a state of emergency and the holding of the Olympic and Paralympic Games without spectators.
- ⑤ **We maintain our main scenario, accommodative fiscal and monetary policy.** Prime Minister Suga has called for the continuation of Abenomics, and policy management is largely in line with this. Even if the length of the Suga administration is cut short, the government is likely to continue its current economic policies until COVID-19 is under control.

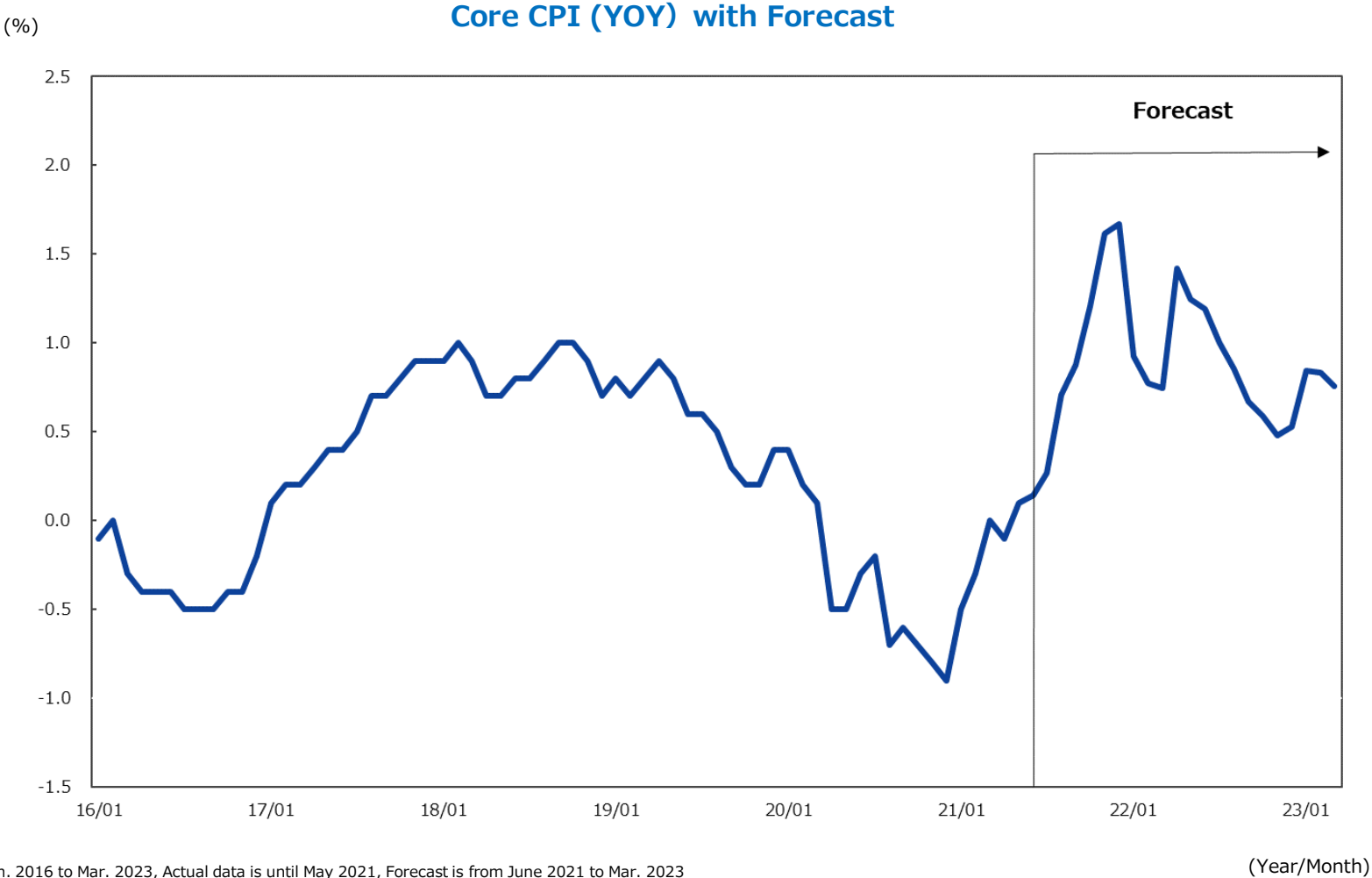
Japan Economy Forecast

Forecast of Annual Real GDP Growth							
Fiscal Year	FY16	FY17	FY18	FY19	FY20	FY21 Est	FY22 Est
Real GDP	0.8%	1.8%	0.2%	-0.5%	-4.6%	3.8%	2.9%
Private final consumption expenditure	-0.3%	1.0%	0.1%	-1.0%	-6.0%	3.0%	2.7%
Private housing investment	4.3%	-1.8%	-4.9%	2.5%	-7.1%	1.3%	2.2%
Private-sector capital investment	0.8%	2.8%	1.0%	-0.6%	-6.9%	4.0%	5.9%
Public fixed capital formation	0.5%	0.6%	0.8%	1.5%	4.3%	2.7%	1.5%
Net export contribution	0.7%	0.4%	-0.2%	-0.4%	-0.6%	1.1%	0.0%
Exports of goods and services	3.4%	6.3%	2.0%	-2.2%	-10.5%	13.3%	5.0%
Imports of goods and services	-0.5%	3.8%	3.0%	0.2%	-6.9%	6.8%	5.0%
Nominal GDP	0.8%	2.0%	0.1%	0.3%	-3.9%	3.0%	3.1%
GDP deflator	0.0%	0.2%	-0.1%	0.9%	0.6%	-0.7%	0.2%
Industrial Production Index	0.8%	2.9%	0.3%	-3.7%	-9.9%	11.2%	5.0%
Consumer Price Index (Core)	-0.2%	0.7%	0.8%	0.4%	-0.5%	0.8%	0.9%
Domestic corporate goods price index	-2.4%	2.7%	2.2%	0.1%	-1.4%	4.9%	0.5%
Employee compensation	2.4%	2.0%	3.2%	2.0%	-2.0%	0.9%	1.7%
Unemployment rate	3.0%	2.7%	2.4%	2.4%	2.9%	2.8%	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

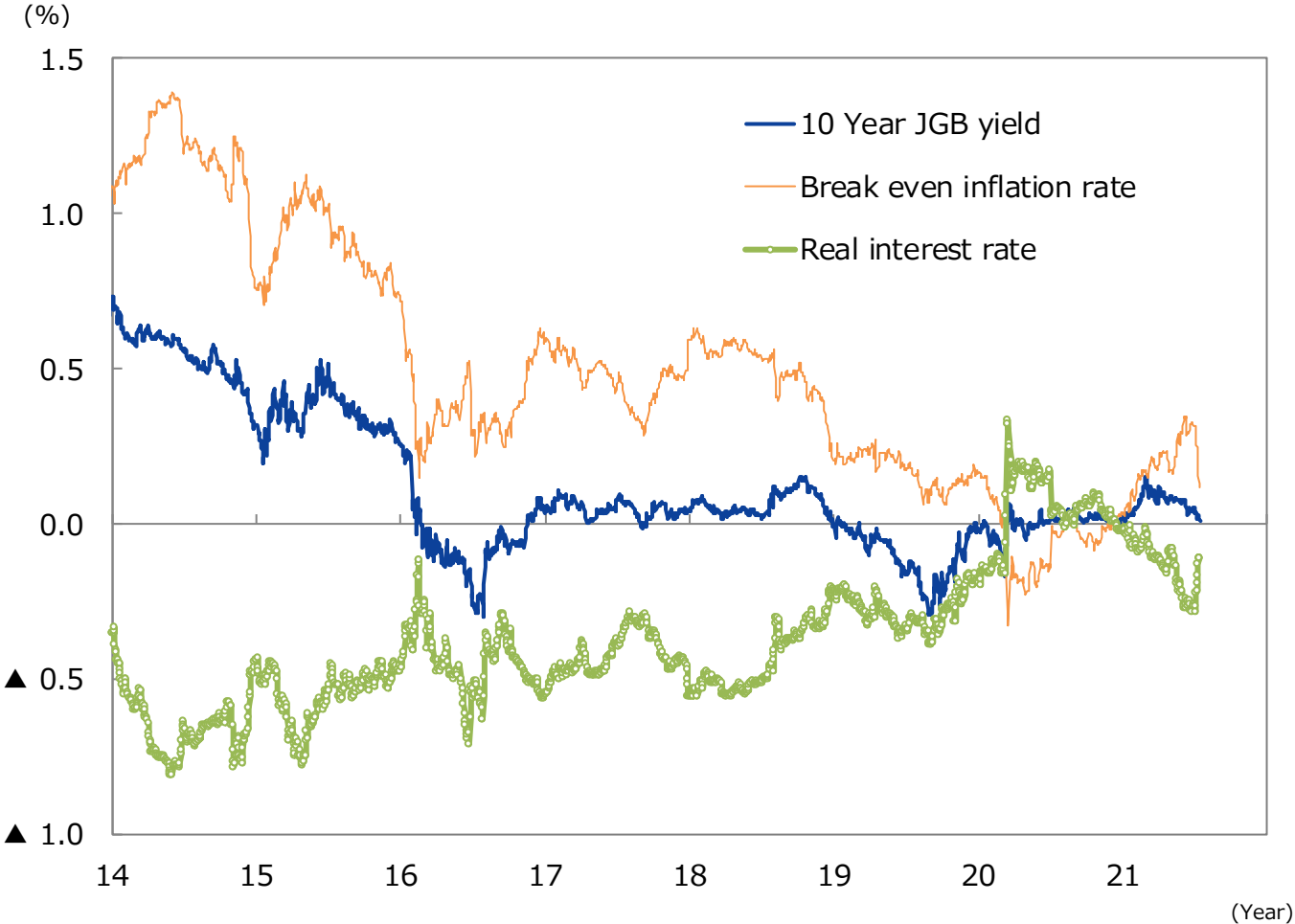
Core CPI with Forecast



(Data) Jan. 2016 to Mar. 2023, Actual data is until May 2021, Forecast is from June 2021 to Mar. 2023
(Source) MIAC, Bloomberg, SMDAM

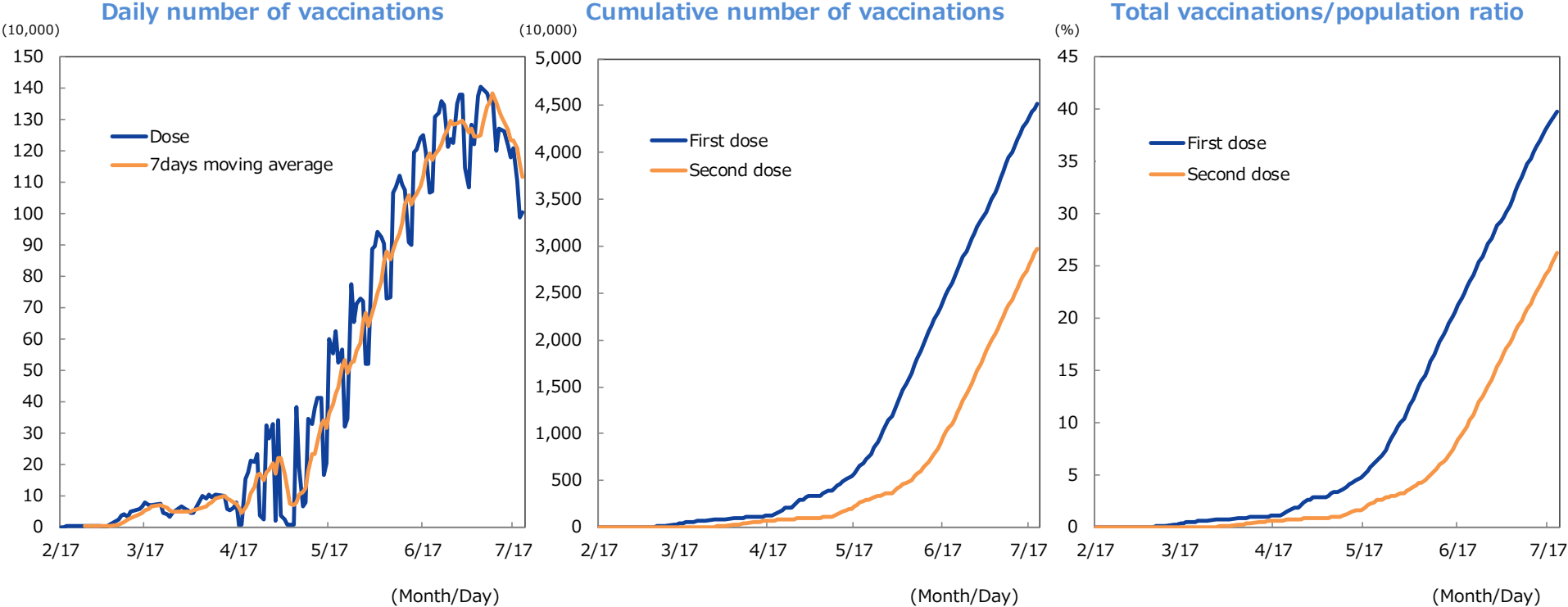
10 Year Break Even Inflation & Real Interest rate

JGB Yield, BEI, and Real Interest rate



(Data) From Jan. 1st 2014 to July 15th 2021
(Source) Bloomberg, SMDAM

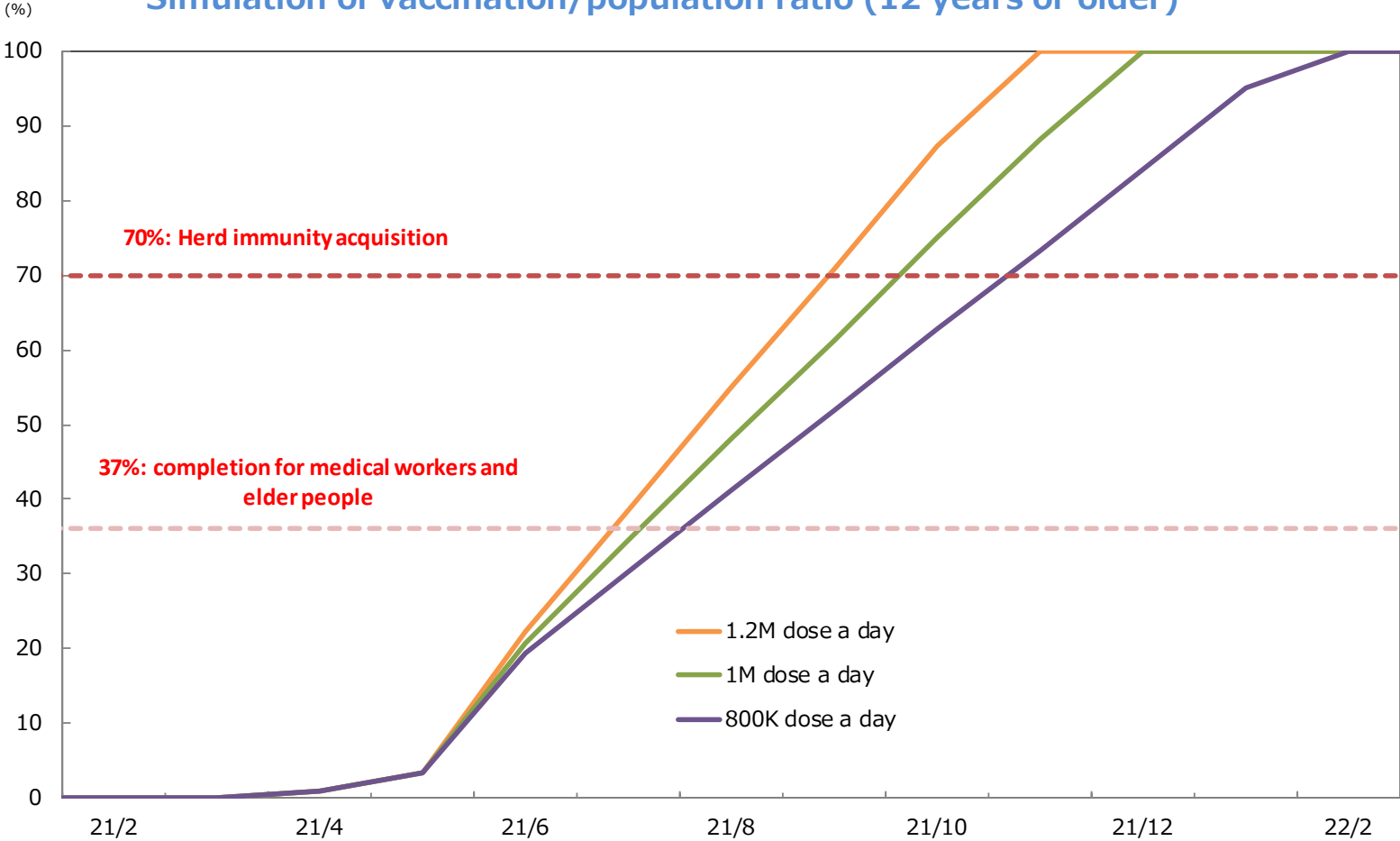
Progress of COVID-19 Vaccinations



(Data) From Feb. 17th 2021 to July 20th 2021
 (Source) MHLW, SMDAM

Progress of COVID-19 Vaccinations

Simulation of vaccination/population ratio (12 years or older)

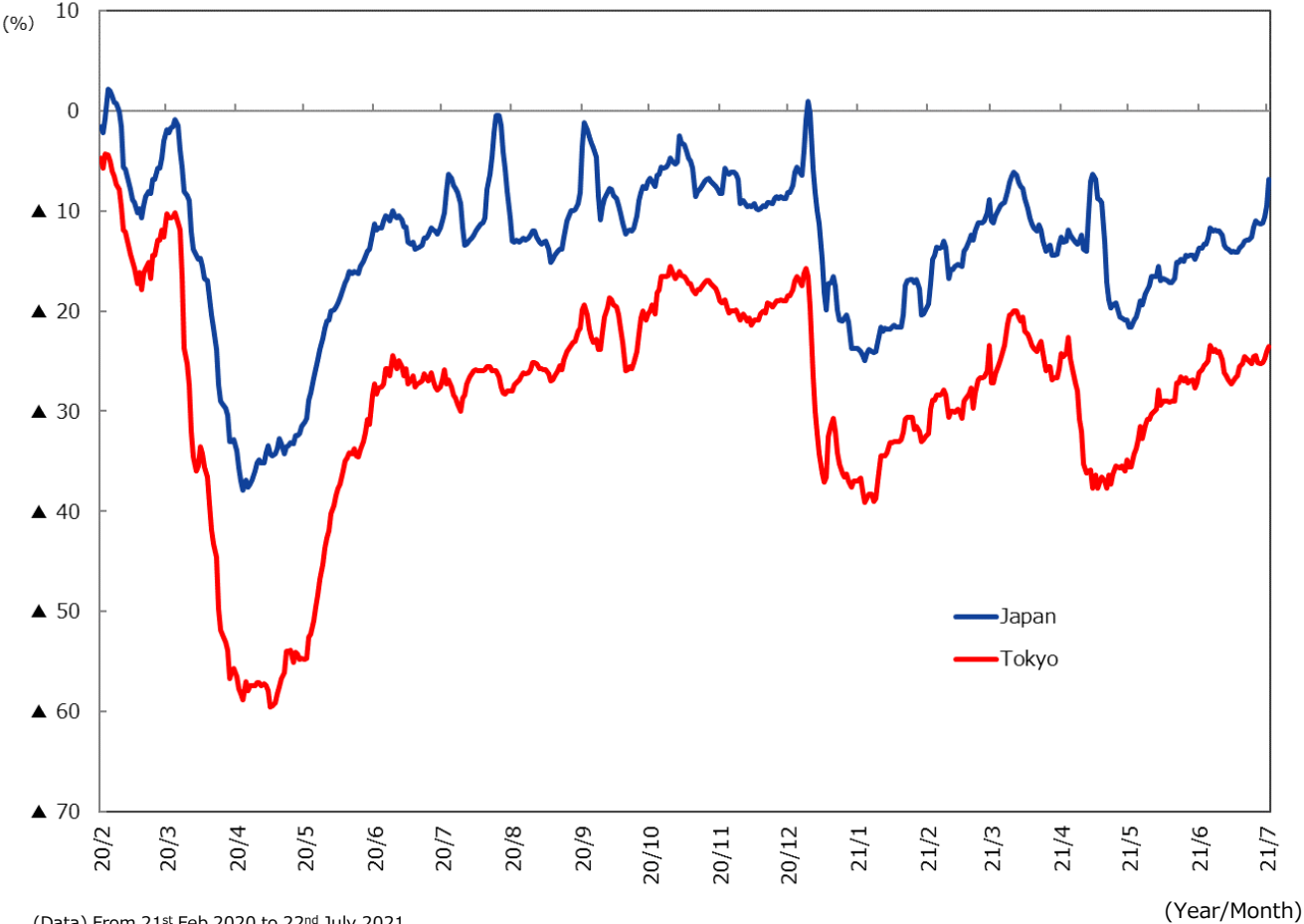


(Source) MHLW, SMDAM

(Year/Month)

Mobility Data

Google Community Mobility Report (Retail & Leisure, 7 days Moving Average)

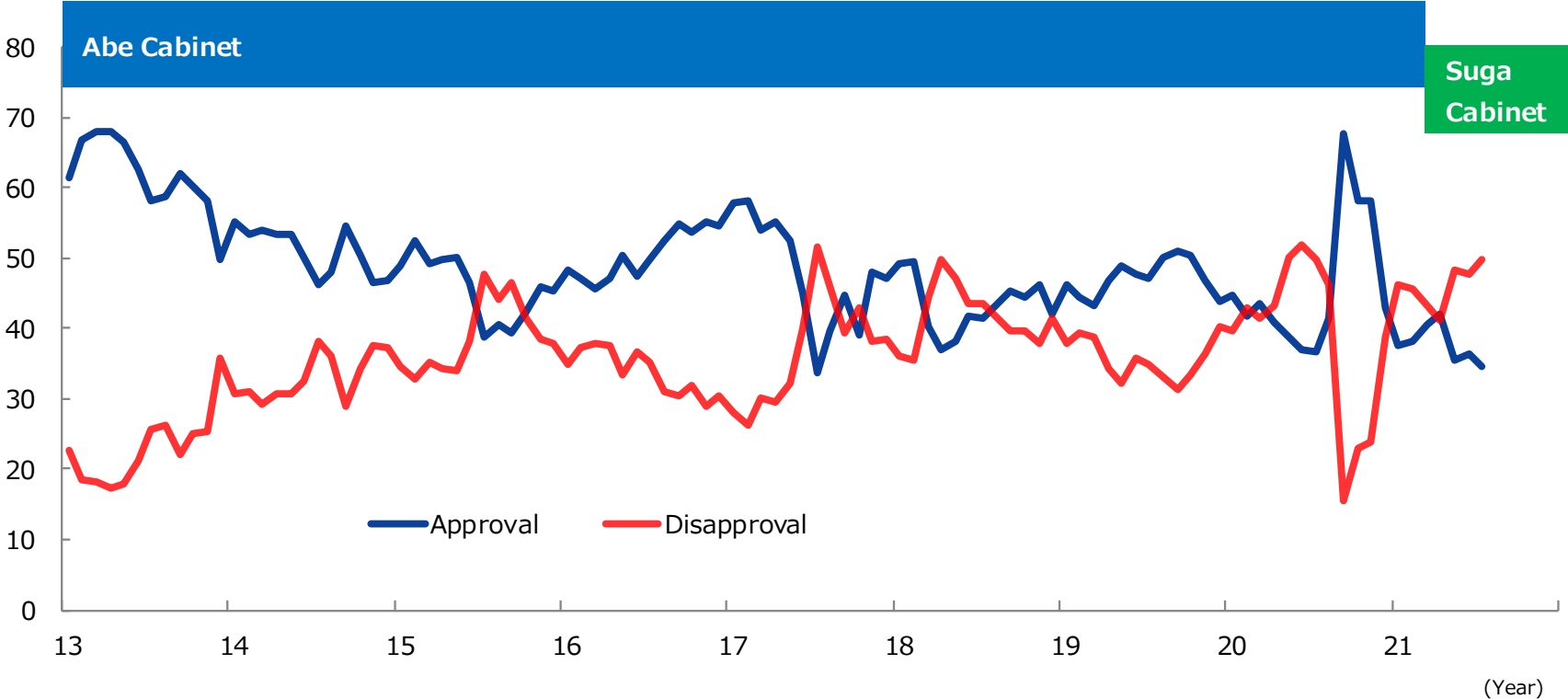


(Data) From 21st Feb 2020 to 22nd July 2021
(Source) Google, SMDAM

Cabinet approval rate

(%)

Cabinet approval rate



(Data) From Jan. 2013 to July 2021
 (Source) NHK, Asahi, Kyodo, Nikkei, Yomiuri, Sankei, Mainichi, Jiji, and SMDAM

Political Schedule, Snap Election in Autumn

Date	Schedule of Political Events
July 4th	Tokyo Metropolitan Assembly Election
July 23rd July 31st	<u>Tokyo Olympics (Until August 8)</u> Target for completion of elderly vaccination
August 25th	<u>Tokyo Paralympics (Until September 5)</u>
September 1st	Launch of Digital Agency
September 30th	<u>Expiration of Ruling LDP President's Term</u>
October 21st	<u>End of the term of the House of Representatives</u>

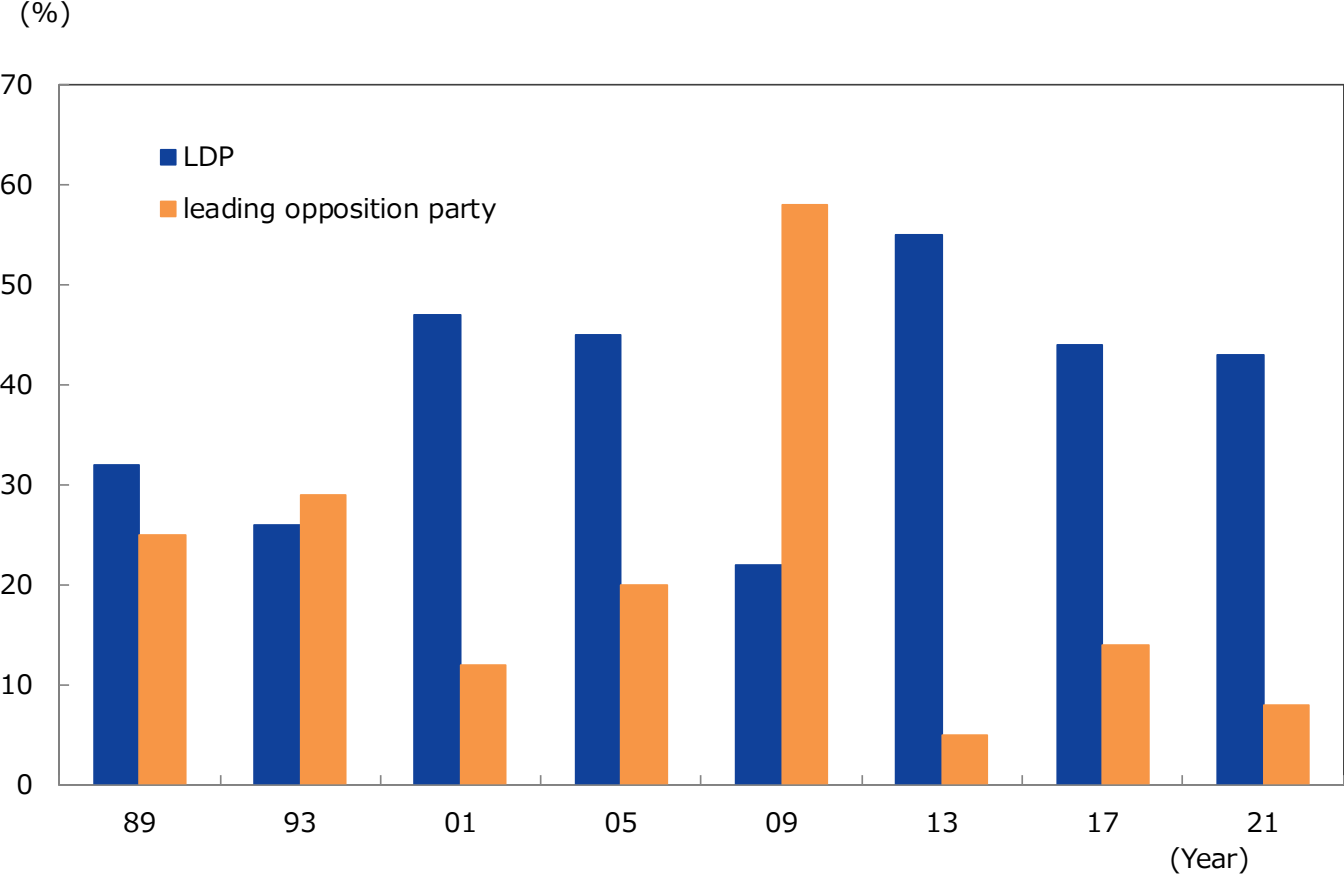
(Source) Compiled by Sumitomo Mitsui DS Asset Management Co., Ltd.

■ Snap Election will be held in the Autumn

- PM Suga said he would dissolve the lower house before the end of his term as president of the ruling Liberal Democratic Party (LDP) at the end of September.
- If COVID-19 is under control, an election will be held in September after Tokyo Olympics & Paralympics.
- In case of prolonged spread of COVID-19, the election could be held in October.
- To appeal to voters, the government could compile a supplementary budget in the summer before election.

Political Party Approval Rate

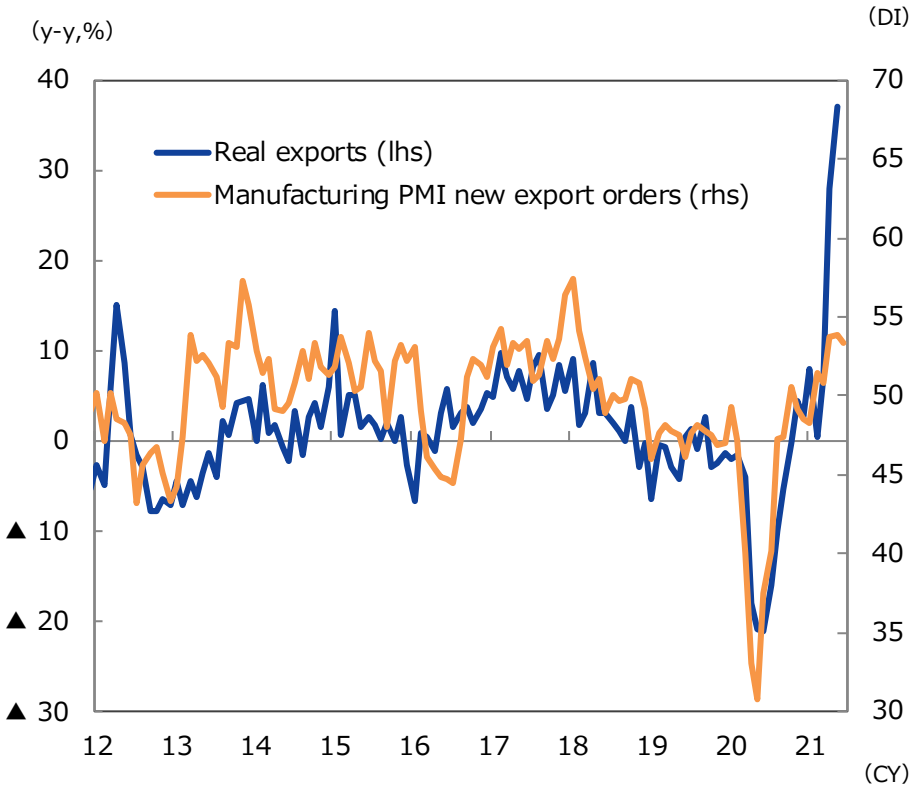
Political Party Approval Rate Before Snap Election



(Source) Nikkei, SMDAM

Exports and Manufacturing Activities

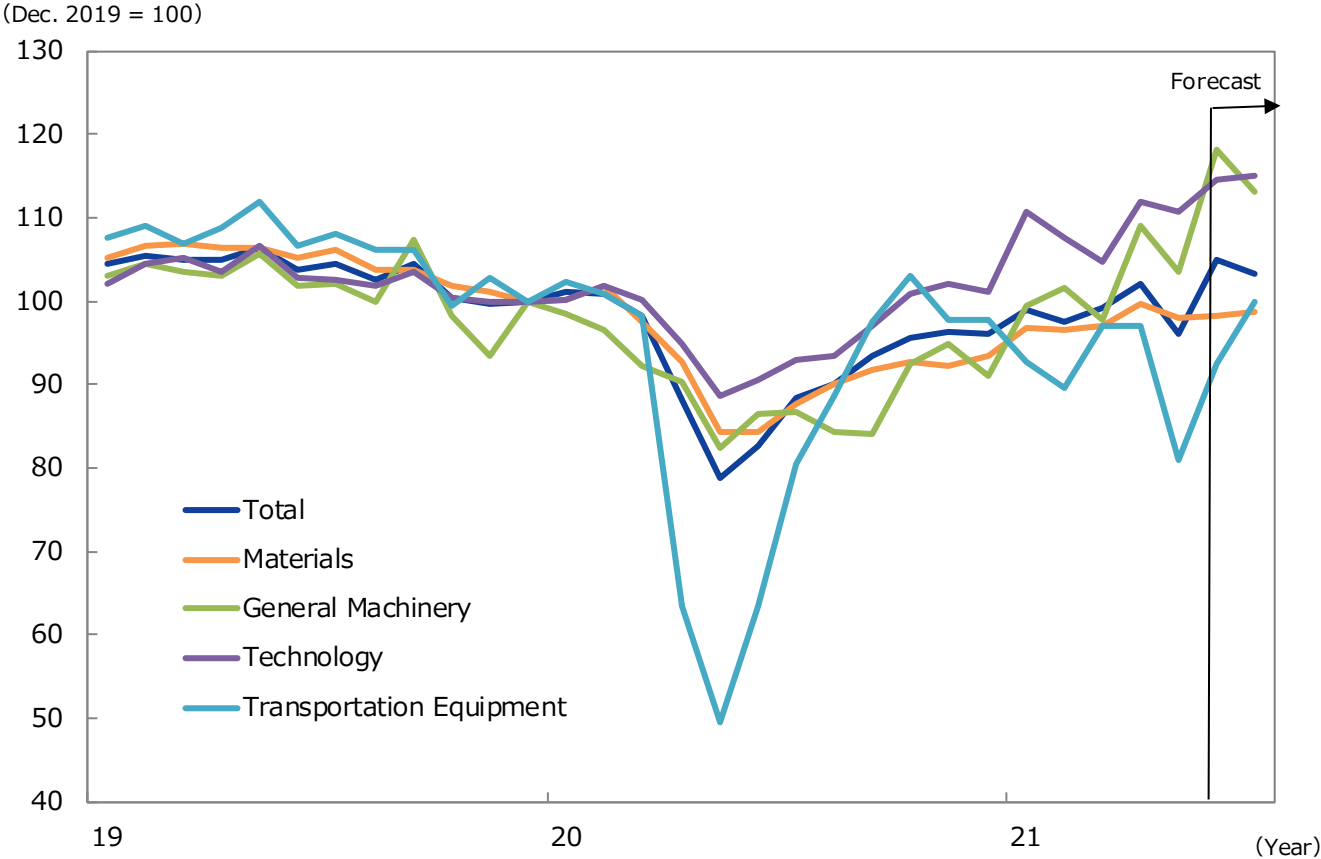
Real exports and manufacturing PMI new export orders



(Data) Real export is from Jan. 2012 to May 2021, MFG PMI new export is from Dec. 2011 to June 2021
 (Source) Compiled by Sumitomo Mitsui DS Asset Management based on data provided by the Bank of Japan, the Cabinet Office and Markit.

Industrial Production

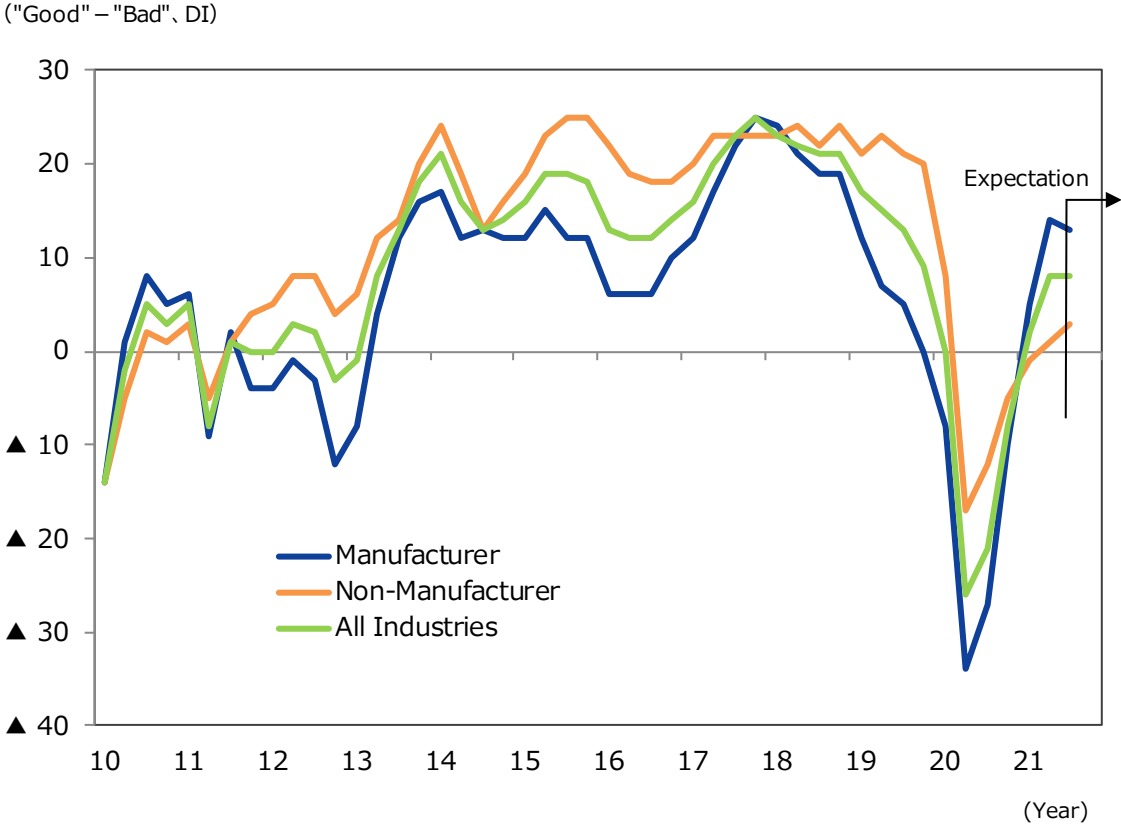
Industrial Production (Monthly)



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

BOJ Tankan Diffusion Index

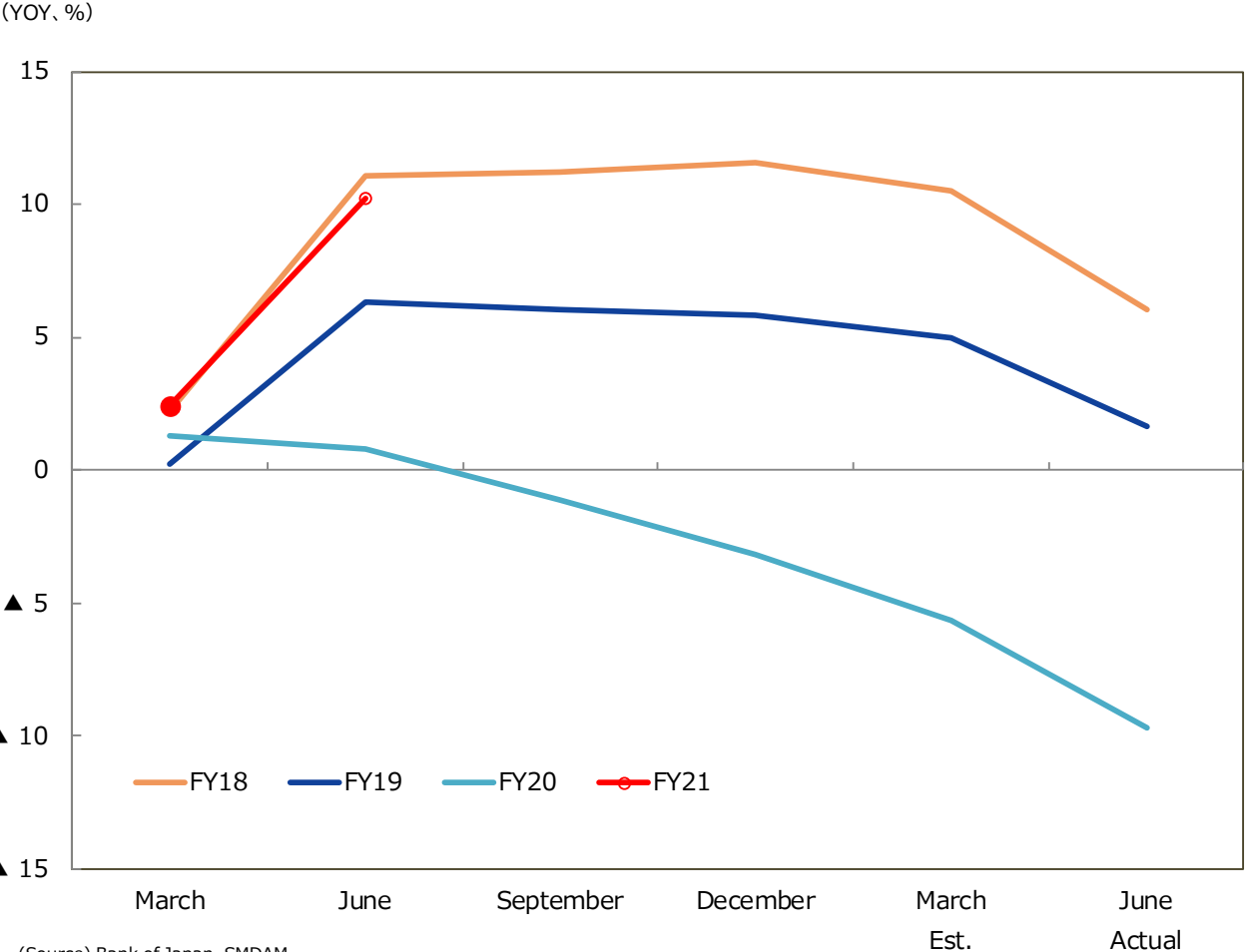
The Bank of Japan "Tankan" Diffusion Index



(Source) Bank of Japan, SMDAM

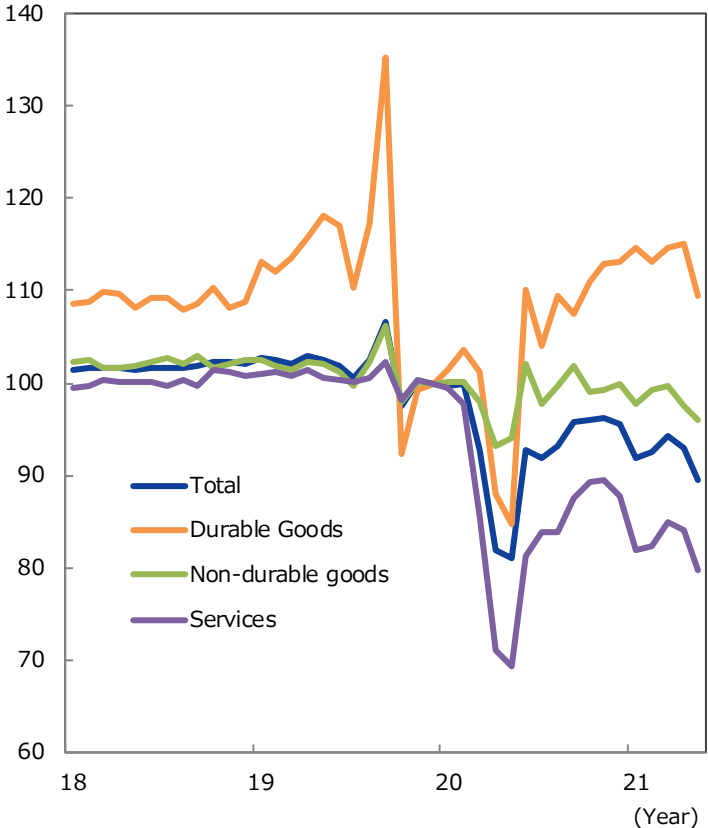
CAPEX

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

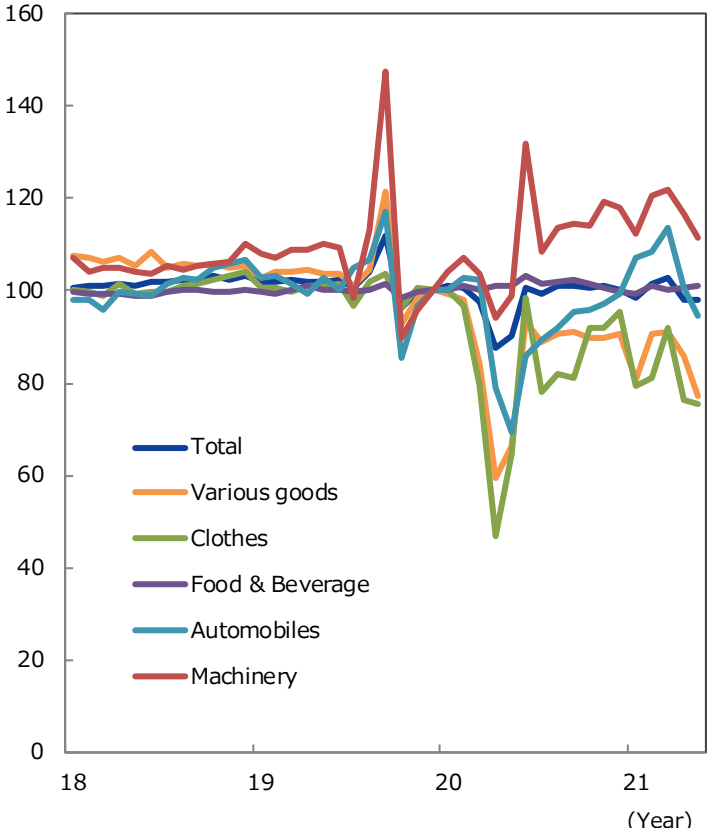


Consumer Spending

Consumer Activity Index (Dec. 2019 = 100)



Retail Sales (Dec. 2019 = 100)



(Data) From Jan. 2018 to May 2021
 (Source) Bank of Japan, METI, and SMDAM

Schedule of Major Events

Major domestic events			
2021	August	8 16 20 25	End of Tokyo Olympics Release of FY2021 Q2 GDP Revision of CPI standards Tokyo Paralympics (Until September 5)
	September	1 8 21-22 30	Launch of Digital Agency Revision of FY2021 Q2 GDP Monetary Policy Meeting Expiration of Ruling LDP President's Term
	October	21 27-28 31	End of the term of the House of Representatives Monetary Policy Meeting and release of "Perspective Report" Official target of the completion of vaccinations of entire nation
	November	15	Release of FY2021 Q3 GDP
	December	8 16-17 Expected Expected	Revision of FY2021 Q3 GDP Monetary Policy Meeting Outline of Tax Reform in Fiscal 22 Cabinet Decision on the FY 22 Budget

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

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