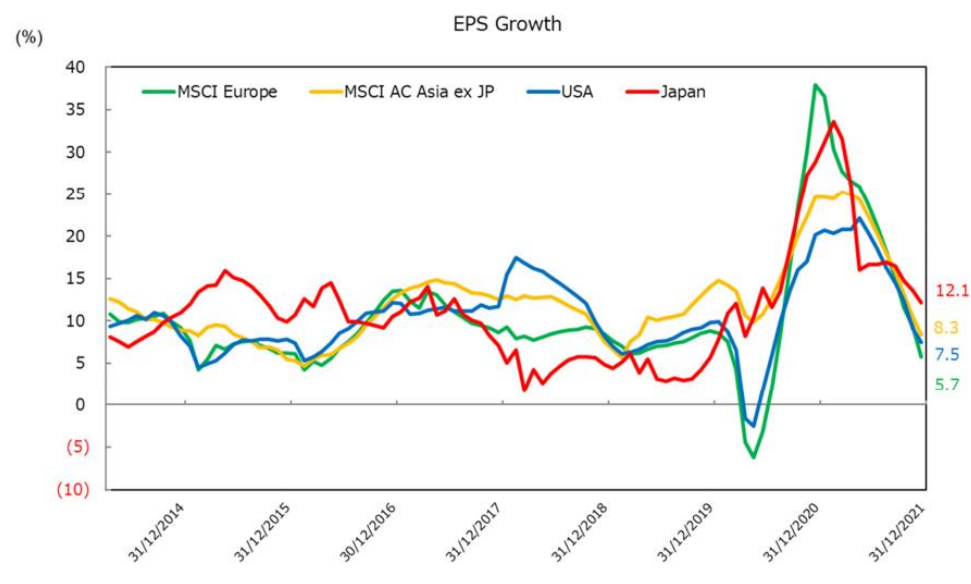


## Sumitomo Mitsui DS Asset Management shares its 2022 outlook for the Japanese market

### Japan equity markets

Sumitomo Mitsui DS Asset Management (SMDAM) maintains its bullish perspective on the Japanese equity market with the target of TOPIX at 2,230 and Nikkei 225 at 32,000 for calendar year 2022. The firm believes that TOPIX earning per share (EPS) could recover by 43% YOY by the end of fiscal year 2021/22 to 134 points, a historical high, and continue its double-digit growth to 151 points in FY2022/23. SMDAM notes that Japan's EPS is growing faster than its global peers.

#### Japan's EPS is growing faster than global peers



### The outlook for Small Cap Value Stocks

**Tatsuro Nigauri, Manager of the SMDAM Japan Small Cap Absolute Value Fund said:** “The outlook for markets in 2022 should be favourable despite the current headwinds of the pandemic and global supply constraints which are expected to ease toward the middle of 2022. The portfolio has historically had a high weighting towards construction, materials and industrial sectors.”

The portfolio manager is now turning towards consumption stocks where the recovery has been delayed due to COVID, but which he expects to pick up in 2022. A stimulus package of \$383bn, which was announced in November 2021 included cash payouts for households and support for business which should further support any recovery.

Small Cap Value stocks historically start to outperform when: firstly, profits of higher growth companies contract due to changes in monetary policy; and secondly earnings of value stocks outperform growth stocks. This is currently happening and in Mr. Nigauri's view, December was the inflexion point for a sustained value outperformance.

Looking at the price-earnings ratio (PER), Japanese stocks are selling at record discounts compared to the S&P 500. As at the end of December 2021, the PER of the fund was 13.7 versus 23.5 for the Russell Nomura Small Cap Index. This gap suggests that value stocks are undervalued relative to their fundamentals. Mr. Nigauri increasingly expects to see more upside potential and a continued re-rating of value stocks.

## Macroeconomic environment

SMDAM has raised its real GDP forecast for FY 2022 to +3.0% from +2.9%, but has lowered its growth forecast for Q1 2022 owing to the steep increase of Covid-19 Omicron infections, however it expects the pace of economic growth to reaccelerate in Q2 and Q3 2022<sup>†</sup>.

The firm expects Prime Minister Kishida and his cabinet to maintain the existing policy mix, including fiscal and monetary policy. If the economy slows further (due to Covid-19 Omicron infections) the government will provide additional fiscal stimulus before the Upper House election in summer 2022.

SMDAM has revised Core CPI forecasts<sup>†</sup> upward: to +0.1% from 0% for FY 2021; to +1.0% from +0.7% for FY 2022; and to +0.8% from +0.6% for FY 2023 respectively. The major reasons for these changes are revisions to the crude oil price assumption and the foreign exchange rate<sup>†</sup>.

The current accommodative monetary policy of the BOJ will be maintained for the foreseeable future. However, due to the negative effects of rising prices and the yen's depreciation on households, we should be cautious about the possibility of policy discussions aimed at normalising the monetary policy. In addition, since Governor Kuroda's term will end in April 2023, his resignation could be a turning point in the current accommodative monetary policy.

## A word on the Stewardship Code and the Corporate Governance Code

The Stewardship Code (SC) set in February 2014, was reinforced in March 2020, requiring investors to evaluate ESG factors. This code, along with the Corporate Governance Code (CGC) of June 2015 – revised to reinforce sustainability-related principles - have been progressively reviewed and enhanced, and are making a visible impact on corporate behaviour and investors' attitudes as shareholders.

<sup>†</sup>Source: SMDAM, based on data from the Cabinet Office, Ministry of Internal Affairs and Communications, and Ministry of Economy, Trade and Industry (METI).

**ENDS**

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- **The full Market Outlook presentation is available [here](#)**
- **Please do get in touch if you have further questions on Japanese Small Caps, or the SMDAM Japan Small Cap Absolute Value Fund specifically.**

## Disclosures

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**Risk warning: On 1 January 2021 the UK left the EU transitional arrangements and no longer benefits from passporting rights into EEA countries.**