Sumitomo Mitsui Asset Management

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By Shunsuke Matsushima, lead fund manager of Parvest Equity Japan Small Cap Fund

1. Abe calls early election

Prime Minister Abe called for a snap election for the lower house of the Diet, arguing it is intended to seek for the people's response to the announced delay of consumption tax hike. The trigger for the dissolution of the congress is considered to be the judgment that it was the advantageous timing for him to do so, based on the schedule of the political events upcoming next year. Another reason could be to mitigate the negative impact from the resignation of 2 Cabinet members after the recent reshuffle (even though one of them resigned for an insignificant reason).

The governing coalition of Liberal Democratic Party and Komeito Party already has enough seats in the lower house, and winning further seats would not be easy. Some polls show that more than 60% of voters do not agree with the snap election at this timing, which implies the possibility that some opponent parties could win sympathy votes especially from the people who have feeling of aversion to the governing parties being too strong. We consider the governing coalition is likely to lose some seats although it is expected to seize enough seats to get their bills through the house. As we forecast the governing coalition would continue to control the majority of the lower house, the administration of the policy measures would progress as scheduled.

2. Delayed sales-tax increase

We consider the delay in consumption tax hike would be positive to the Japanese economy in the short term. This decision, however, could unfavorably impress foreign investors as it could be regarded as delay in fiscal reform and derailment of Abenomics. Also, Abe's growth strategy could be affected as corporate tax cuts, one of the growth strategy, is based on the premise that the consumption tax increase would be the alternative source of tax revenue for the government. Yet, we consider the delay of the consumption tax hike has generally positive impact on the Japanese economy.

3. Sectors and stocks: 2015

Our focus on the stock selection in 2015 continues to be based on the Value to Growth Strategy, investing in undervalued stocks that have good growth potentials. We are currently overweighting domestic demand, non-manufacturing stocks, while keeping an eye on the timing to increase external demand, manufacturing stocks depending on the developments in global economy.

In 2015, we anticipate some return reversals for the sectors that did well and not well in 2014.

Construction and smart-phone related sectors, which showed strong performance in 2014, would continue growth yet the pace would be moderated in 2015.

Meanwhile, we anticipate some rebound in electric power & gas and retail trade sectors. For electric power companies, possible reactivation of nuclear power plant in 2015 would

be a positive factor. Also, retail sector suffered from negative impacts from the consumption tax hike, which is expected to be moderated next year.
Machinery and software system related sectors are forecast to continue growth, supported by (1) solid CAPEX in Japan, boosted by infrastructure renewal demand and 2020 Tokyo Olympic Games, as well as (2) the government initiative to encourage the Japanese companies to enhance ROE and capital allocation, partly by introducing JPX Nikkei 400 index. Especially for the software systems companies, demand has been strong as many Japanese companies had long refrained from renewing their systems after Global Financial Crisis in 2008, and they are facing the timing of renewal.

Sumitomo Mitsui Asset Management Company, Limited
Atago Green Hills MORI Tower 28th Floor
2-5-1 Atago Minato-ku, Tokyo 105-6228 Japan
TEL +81-3-5405-0555 FAX +81-3-5405-0666

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