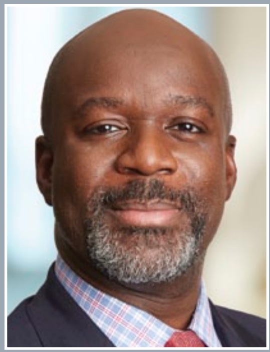
SPROTT FOCUSED STRATEGY

Global Market Outlook

2016 Global Preview

The narrative for 2016 really comes down to structural headwinds versus cyclical tailwinds. Structurally, the global economy continues to deal with below trend growth as a consequence of poor demographics, continued deleveraging, geopolitical strife and over-capacity. With these obvious headwinds, any material negative headline is magnified and the market reaction is exaggerated. This structural narrative is in direct contrast to the cyclical narrative of continued positive global economic growth, supported by low commodity prices, currency devaluation, quantitative easing and low inflation. It should come as no surprise then that investor conviction is low and market volatility is elevated.



Dennis Mitchell
Senior Vice-President,
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Global GDP Growth

The OECD forecasts that global real GDP growth will accelerate to 3.3% in 2016, from 2.9% in 2015. The World Bank recently cut its forecast for 2016 from 3.3% to 2.9% while the International Monetary Fund's most recent forecast (October 2015) remains at 3.6%. Generally, forecasts for 2016 global GDP growth remain below the long term average of 3.5% since 1980, with developed economies expected to drive global growth. Risks to global growth are skewed to the downside with US interest rate normalization and China's slowdown representing material risks to emerging markets ("EM") and geopolitical risks (ISIL, Syrian refugees, US election, UK referendum) threatening developed markets ("DM").

"Forecasts for 2016 global GDP growth remain below the long term average of 3.5% since 1980, with developed economies expected to drive global growth."

GLOBAL GDP FORECASTS			
COUNTRY/REGION	2015	2016	2017
WORLD	**2.9%**	**3.3%**	**3.6%**
UNITED STATES	2.4%	2.5%	2.4%
CANADA	1.1%	2.0%	2.3%
EURO AREA	1.5%	1.8%	1.9%
JAPAN	0.6%	1.0%	0.5%
CHINA	6.8%	6.5%	6.2%
INDIA	7.2%	7.3%	7.4%
BRAZIL	-3.1%	-1.2%	1.8%

Source: OECD.

Purchasing Manager Index Composite

Lead by Services, the December 2015 global Purchasing Manager Index Composite ("PMI") was 52.9, firmly in expansion territory. DM PMIs were robust at over 54.0 and have outperformed EM PMIs since 2013. Historically, global GDP growth has lagged the long term average when this has been the case. Generally, Services PMIs have been very resilient, while Manufacturing PMIs have been weaker, weighed down by China's economic transition. US PMIs have lagged European and Japanese PMIs as both the Eurozone and Japan benefited from continued quantitative easing and low rates. Going forward, European and Japanese PMIs will likely continue to reflect solid economic expansion buoyed by low rates and monetary easing. PMIs are often used to forecast recessions, as declining manufacturing and service output is indicative of future contractions in overall economic output. In 2007, global PMIs were in the low 30s to high 40s range, clearly forecasting significant global economic contraction in 2009. Today, global PMIs above 50 continue to point towards global economic expansion, albeit at a slower pace and skewed towards Services.

GLOBAL DECEMBER PURCHASING MANAGER INDICES					
MARKET	MANUFACTURING	SERVICE	MARKET	MANUFACTURING	SERVICE
GLOBAL	**50.9**	**53.1**	EUROZONE	53.2	54.2
UNITED STATES	48.2	55.3	UNITED KINGDOM	51.9	55.5
JAPAN	52.6	51.5	GERMANY	53.2	56.0
CHINA	49.7	54.4	FRANCE	51.4	49.8
BRAZIL	45.6	43.5	ITALY	55.6	55.3
INDIA	49.1	53.6	SPAIN	53.0	55.1
RUSSIA	48.7	47.8	IRELAND	54.2	61.8

Source: Trend Macrolytics, Markit Economic Research.

Global Trade

Global trade has grown at an average annual rate of 2.5% since 2013, which is less than half the historical average of 5.5%. Similarly, global industrial production is growing at 1.6%, compared to the long term historical average of 2.9%. However, there are structural factors contributing to the slowdown of both metrics. First, services have steadily contributed more to global growth and tend to be produced and consumed locally, limiting their contribution to global trade. Second, China's shift towards more domestic production and less overall manufacturing has biased these metrics down. Lower global trade and industrial production will mirror lower global real GDP growth in 2016.

Global Equity Valuations

After the recent pullback, global equities are priced to deliver strong returns. Earnings estimates growth rates are above long term averages, in some cases due to low base effects and in others due to cyclical recoveries. The Nikkei stands out in this regard for its low earnings growth rate expectations. Dividend yields are attractive, especially compared to sovereign bond yields. Here, the FTSE 100, S&P/TSX and EuroStoxx 50 indices are standouts in terms of significant dividend yield spreads. Against this investors must consider the fact that forward market multiples are still above their three- and five-year averages. Given the low level of growth in the global economy, the potential for multiple contraction must be considered. The FTSE 100 appears most at risk of further multiple contraction, while the S&P/TSX and EuroStoxx 50 Indices are closer to historical valuation levels. Global equities appear priced to deliver low teens total returns but with a higher level of volatility than historically experienced.

PMI

The magic number for the PMI is 50. A reading of 50 or higher generally indicates that the industry is expanding. If manufacturing is expanding, the general economy should be doing likewise. As such, it is considered a good indicator of future GDP levels.

"After the recent pullback, global equities are priced to deliver strong returns."

"Dividend yields are attractive, especially compared to sovereign bond yields."

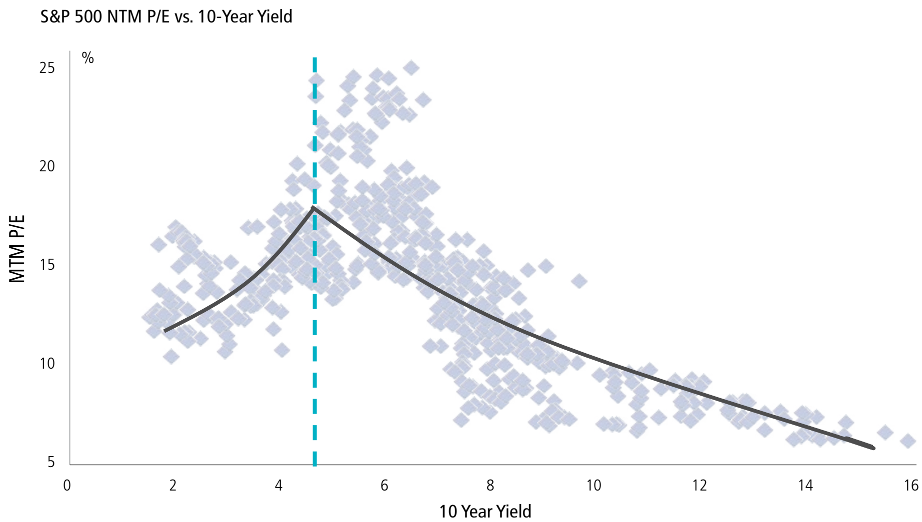
GLOBAL EQUITY MARKET FUNDAMENTALS						
	FORWARD P/E MULTIPLE ESTIMATE			EARNINGS GROWTH	DIVIDEND YIELD	10 YEAR BOND YIELD
MARKET	CURRENT	3 YEAR AVG	5 YEAR AVG			
MSCI World	**14.5x**	**14.1x**	**12.9x**	**7.8%**	**2.8%**	**0.9%**
S&P 500	15.2x	14.6x	13.4x	11.6%	2.3%	2.0%
FTSE 100	14.5x	12.8x	11.5x	14.4%	4.6%	1.7%
Shanghai	11.5x	9.8x	9.6x	18.1%	2.1%	2.7%
Nikkei 225	16.0x	16.3x	14.7x	6.7%	1.9%	0.2%
S&P/TSX	14.1x	14.1x	13.3x	14.9%	3.6%	1.1%
EuroStoxx 50	12.6x	12.4x	11.0x	23.4%	4.0%	0.7%

Source: Bloomberg. Note: Global bond yield is the Global Developed Sovereign Bond Index, Eurozone bond yield is EFSF yield.

Against this backdrop, we have chosen to allocate capital to US, Eurozone and UK equities given their strong total return outlooks. In addition, these markets are home to the greatest number of high quality franchises, making it easier to deploy our strategy as outlined in the paper published in December 2015. We favour companies that are able to drive volume AND pricing gains in this low growth environment (and really always). The level of risk aversion in the market will likely yield sharply negative moves for companies that disappoint or guide to mediocre performance. Our aversion to Japanese equities is based on their historical track record of poor returns to shareholders. Much of the recent performance of the Nikkei is due to currency depreciation and multiple expansion. Organic earnings growth has been much more modest and is forecast to remain so.

At 15.2x 2017 EPS estimates, the S&P 500 is not trading at an aggressive multiple and potential multiple contraction is in-line with the global equity market as a whole. The most aggressive rate hike scenario would only add 100 bps to the Fed Rate and generally, when long bond yields are as low as they are now, P/E ratios tend to expand as the normalization cycle takes hold. Earnings growth estimates exceed that of the global market as a whole but still assume a strong recovery in energy sector profits and some weakening of the US dollar. The 2.3% dividend yield exceeds that of the 10 year bond but the spread has come in from recent peaks. Overall, the S&P 500 is poised to deliver returns in-line with that of the global equity market as a whole, with upside should the US recovery gather steam and US equities receive a safe haven bid.

FORWARD P/E RATIOS VS. RATES



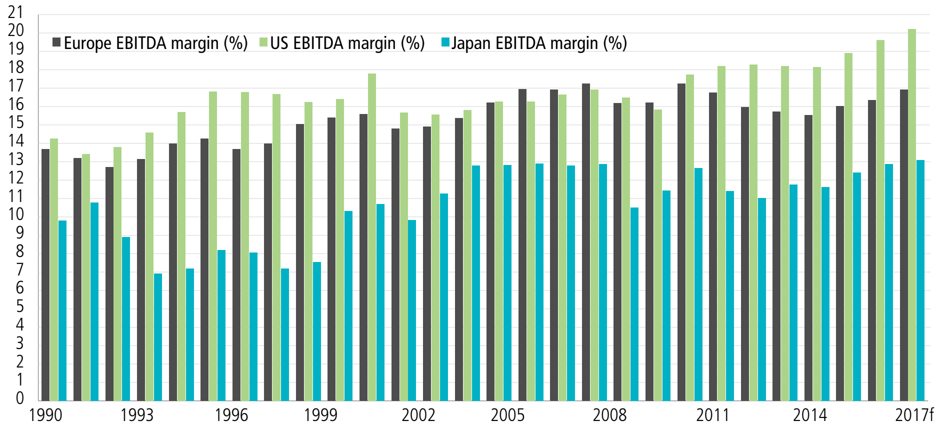
Source: RBC.

> "Overall, the S&P 500 is poised to deliver returns in-line with that of the global equity market as a whole, with upside should the US recovery gather steam and US equities receive a safe haven bid."

> "This is a market that is likely to experience an elevated level of volatility in 2016."

At 12.6x 2017 EPS estimates, the EuroStoxx 50 Index is not trading at an aggressive multiple and potential multiple contraction is in-line with the global equity market as a whole. The ECB stands ready to add additional stimulus to what is already a very accommodative monetary policy environment. Earnings growth estimates are very robust at 23.4% and reflect a material catch up from a low base. Compared to S&P 500 companies, Eurozone companies have lagged in terms of operating and profit margin recovery since the financial crisis. It should also be noted that while EuroStoxx 50 equities delivered 7.3% earnings growth in 2015, the five year earnings CAGR is -2.4%. The 3.9% dividend yield compares very favourable to sovereign bond yields and adds to an already substantial total return picture that exceeds that of the global equity market. However, this is a market that is likely to experience an elevated level of volatility in 2016.

US AND EUROPEAN EBITDA MARGINS* 1990-2016F



*Non-financials. Source: Redburn IDEAS. Forecast Periods use consensus data – source: FactSet.

The FTSE 100 Index is trading at 14.5x 2017 EPS estimates, which puts it at risk for multiple contraction above that of the global equity market as a whole. However, the rate of earnings growth forecast in the market is more than twice that of the global equity markets. Some of this is cyclical recovery but there is a healthy amount of energy sector recovery implicit in these numbers. The Bank of England is in a position to begin a rate normalization program however, the referendum on EU membership will likely delay this cycle until late 2016/early 2017. It should also be noted that while FTSE 100 equities delivered 2.5% earnings growth in 2015, the five year earnings CAGR is -6.0%. With a 4.6% dividend yield the FTSE 100 offers compelling return potential above that of the global equity market but volatility could be higher than global averages.

Since the end of 2010, the Nikkei has delivered a total return in excess of 100% in Yen terms (54% in US dollar terms). This has been fueled by strong profit growth and multiple expansion as Abenomics has been rolled out. However, adjusting for the impact of Yen depreciation, Japanese corporate earnings growth has been much more modest. The Nikkei currently trades at 16.0x 2017 EPS estimates, putting the risk of multiple contraction in-line with global equity markets. Earnings growth estimates are 6.7% and combined with a dividend yield of 1.9% offer modest total return potential. Given the scale and scope of the Abenomics QE program, multiples are likely to remain flat if not expand further in 2016. Additionally, Yen-denominated earnings are likely to show robust growth as QE devalues the Yen further but a hedging strategy will be required to capture these returns. All of this is likely to come with immense equity market volatility as evidenced by Nikkei performance year to date in 2016.

"With a 4.6% dividend yield the FTSE 100 offers compelling return potential above that of the global equity market but volatility could be higher than global averages."

"All of this is likely to come with immense equity market volatility as evidenced by Nikkei performance year to date in 2016."

We are not able to invest directly in the Shanghai Composite and would not even if given the chance. However, we do note that, despite entering bear market territory with a decline of greater than 20%, the Shanghai Composite market multiple remains elevated relative to recent historical levels. We expect this market to continue to unwind the IPO excesses of 2014 (that drove this index up 58.0% in 2014) and significant use of leverage by unsophisticated investors. Finally, the yield on the Chinese 10 year treasury remains above the dividend yield of the equity market, offering little support for equity valuations. We note that this equity market does not accurately reflect the level of economic activity in the Chinese economy and recent trading is more a function of excesses being unwound exacerbated by poor policy (circuit breakers) and capital flow fears.

Eric Nuttall has published an insightful analysis of the energy market going into 2016 and investors are encouraged to read this for our thoughts on this subject. However, we are constructive at current levels given the anticipated improvement in aggregate global demand and the anticipated decline in aggregate global supply. But global crude prices are unlikely to stabilize prior to Q2 2016 and are likely to be a source of continued equity market volatility until and after stabilizing. Regardless of energy market fundamentals, investors are concerned about perceived oversupply and slowing global growth and have continued to pressure energy prices. Ironically, this is to the benefit of oil importing nations, such as the US, China, Japan and the European Union, which combined, comprise 60%+ of global GDP.

Volatility in global equity markets is likely to remain elevated for the first half of 2016. Continued healing in the labour markets of the United States and the Eurozone should underline positive real GDP growth, driven by services and consumption. Japan and China should also generate positive GDP growth in 2016, allowing the global economy to generate positive, if below trend GDP growth. Against this is the risk of greater geopolitical tensions, referendums, terrorism and inconsistent economic datapoints. However, the fact remains that global growth is positive and trending in the right direction and global equities are priced to deliver strong returns if with added volatility.

"The fact remains that global growth is positive and trending in the right direction and global equities are priced to deliver strong returns if with added volatility."

Thanks and **stay focused**,

Dennis Mitchell
Senior Vice-President,
Senior Portfolio Manager

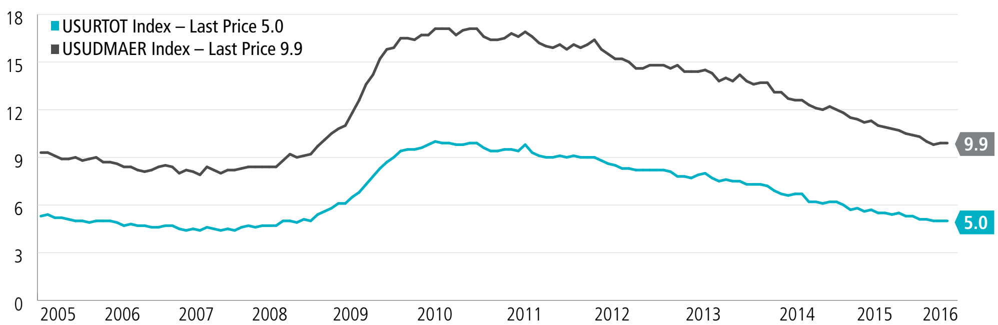
Previews

United States 2016 Preview

The key issues for the US economy are the rate normalization cycle and the labour market. The Federal Open Market Committee ("FOMC") has indicated that it will raise the Federal Funds Rate ("Fed Rate") four times in 2016, for a total increase of 100 bps. The market is currently pricing in 25 bps increases in June and December, so there is a small disconnect that will be cleared up in Q1. Given the weak December PMIs and the minutes from the December FOMC meeting, it is unlikely that the Federal Reserve Bank ("Fed") will raise rates without having a firm idea of how Q1 GDP is shaping up. That would likely make April the earliest the Fed could move but June might be more likely, given this would be a quarterly news conference meeting. Two rate increases (June and December) is probably the correct market positioning, with upside to three rate increases if the labour market heats up or global growth ticks up.

The labour market in the US has shown good strength and continues to improve. The unemployment rate sits at 5.1% and the underemployment rate has fallen to 9.9%. Underemployment is likely to remain elevated (9.9% matches the last cyclical peak in 2003) and the participation rate is likely to remain depressed for some time. Services will continue to drive GDP growth and demographic and immigration trends will impact both variables. However, it's important to note that employed people (underemployed or not) consume more than unemployed people. Continued job growth will be a catalyst for continued US economic growth.

UNITED STATES UNEMPLOYMENT & UNDEREMPLOYMENT RATES



Source: Bloomberg.

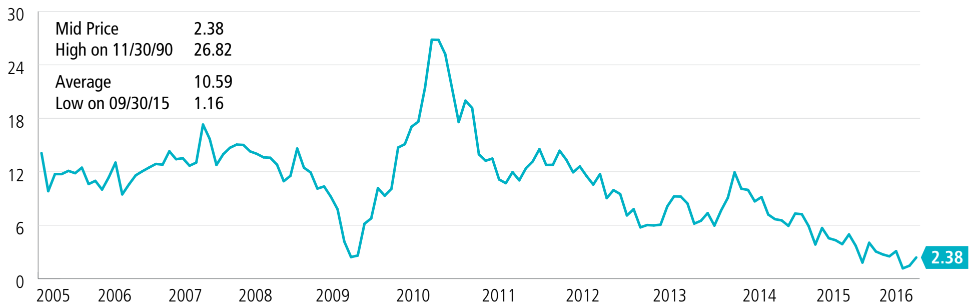
Average hourly earnings have grown steadily since 2013 and wages and salaries have grown 4.5% year over year. This should continue as 19 states are poised to increase their minimum wage in January of 2016. However, one thing to note is the uptick in the household savings rate to 5.6%, versus the long term average of 3.9%. Some of this is a function of lower debt service costs and rising real incomes but it does bear watching. A prudent US consumer could impact export activity from European and Chinese nations and slow global GDP growth.

China 2016 Preview

The China debate centers around how fast China's growth is slowing and what impact this will have on global growth. For years China's real GDP grew at 10%+ rates as the country allowed debt-fueled capital investment to contribute over 40% of GDP growth annually (Japan's bubble peak was approximately 24% of GDP). However, this level of investment is unsustainable and eventually capacity utilization and returns fall and growth slows. China is now transitioning their economy to one that is more dependent on domestic consumption to deliver lower but sustainable GDP growth.

Chinese Premier Li Keqiang tracks railway cargo volumes, electricity consumption and loans disbursed by banks to track the economic output of the Chinese economy. The "Keqiang Index" has been used by many investors to track Chinese economic output instead of the questionable official data from the People's Bank of China ("PBOC"). Looking at this index, Chinese economic growth has fallen from a recent peak of 11.9% in August of 2013 to 2.4% in November of 2015. This compares to the official PBOC numbers of 6.9% real GDP growth in Q3/15 and the official target of 6.5% real GDP growth through 2020. Countries and companies must adjust capacity and production to a structurally lower rate of demand from China. For instance, oil consumption will not collapse but the rate of consumption growth should moderate as the Chinese economy matures. In contrast, the aggregate demand for steel, copper, nickel and other base metals will decline as China moves from the construction of large infrastructure assets to the maintenance of them.

KEQIANG INDEX

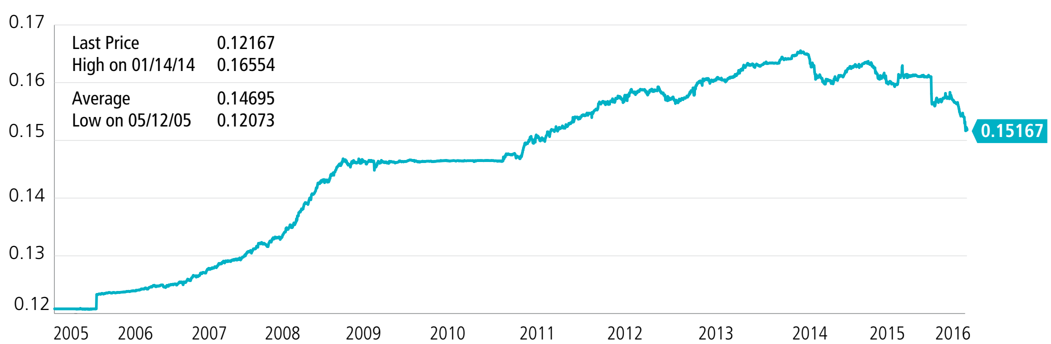


Source: Bloomberg.

Recent capital market volatility has been driven by China's interventions in the currency market. In August of 2015 China announced a surprise devaluation of their currency that spooked markets. Investors feared the move signaled a faster rate of GDP decline than anticipated. Combined with a flurry of stimulus measures (rate cuts, tax cuts, investment incentives) the image was of the PBOC pulling out all the stops to generate growth. And if China is struggling to grow, what does that mean for China-sensitive EM (Brazil, Russia and Indonesia) and DM economies (Germany, Australia, Japan) and global growth as a whole? A second surprise currency devaluation in January of 2016 further spooked investors and rumours of further, more dramatic currency devaluation contributed to a rout in global equity markets.

China exacerbated the volatility in the equity markets by banning short sales, sales by major shareholders and implementing "circuit breakers" which shut the Chinese equity markets down if equities fell by 7.0%. The problem with the circuit breaker mechanism is that it fails to recognize the primary function of the market to provide liquidity. Restricting liquidity forces investors to become price insensitive in their selling and resulted in dramatic price moves that immediately triggered the circuit breakers (trading activity on January 6, 2016 lasted all of 29 minutes). As Chinese investors sought liquidity, their selling spread to other assets, including equities in other markets. In a world of high frequency, program-based trading large market orders trigger exaggerated moves in securities prices that can feed onto each other and produce dramatic price moves in a short period of time.

YUAN/US DOLLAR CROSS



Source: Bloomberg.

China is the poster child for the global economy and the shift to lower growth for an extended period of time. China's PMIs reflect strong growth in Services but stagnation in Manufacturing. This should be expected given the shift in economic output underway. China historically runs small budget deficits of less than two percent of GDP, consistently runs current account surpluses, official government debt sits at 14.9% of GDP and the PBOC has over US $3T of foreign currency reserves. There appears to be little risk of a disorderly collapse in the Chinese economy. However, China's lower rate of growth will materially impact the rate of global growth. Global equities are likely oversold as a result of recent trading activity, but it will take some time for valuations and economic datapoints to signal "all clear" and equities to rally sustainably and materially.

Eurozone 2016 Preview

The key issues for the Eurozone remain twin recoveries in GDP and inflation. The Eurozone is beginning to reap the benefits of tough fiscal policy and substantive monetary policy. In 2012, the collective economic catastrophes of the "PIIGS" nations contributed to a second recession in the Eurozone and threatened the breakup of the Eurozone itself. Spain, Portugal and Ireland, in return for sizable bailouts, were forced to restructure fiscal policy and labour market costs. All three nations grew real GDP in 2015 and are set to lead Eurozone growth in 2016. In contrast, Greece and France have delayed implementing much needed economic reforms and their 2016 growth rates reflect this. Absent a commitment to real structural reform, France in particular, will continue to be a drag on Eurozone growth.

EUROZONE 2016 FORECASTS			
COUNTRY	GDP	INFLATION	UNEMPLOYMENT
IRELAND	4.5%	1.4%	8.7%
SPAIN	2.7%	0.7%	20.5%
PORTUGAL	1.7%	1.1%	11.7%
ITALY	1.5%	1.0%	11.8%
EUROZONE	**1.8%**	**1.0%**	**10.6%**
GREECE	-1.3%	1.0%	25.8%
FRANCE	1.4%	0.9%	10.4%

Source: OECD.

The Eurozone continues to benefit from low oil prices, accommodative monetary policy, a low Euro, less austerity and structural reforms implemented by several member nations. The results have been falling unemployment and rising GDP in an environment of low inflation. The Eurozone still faces a material amount of deleveraging, as the aggregate debt/GDP sits above 90%, compared to the 100% threshold for initial financial distress. This deleveraging is another deflationary headwind that holds the pace of GDP growth below the aggregate potential of the Eurozone.

The capital structure of Eurozone companies includes a heavy reliance on bank loan funding. The European Central Bank ("ECB") has finally implemented meaningful reforms to the banking sector, forcing some to recapitalize but more importantly, allowing others to resume lending. As such, credit conditions for consumers and corporations have eased, allowing firms to begin investing for growth and consumers to make larger ticket purchases. However, there are regulatory (higher capital requirements) and litigation (market manipulation) headwinds that will weigh on the ability of Eurozone banks to fully support the Eurozone recovery.

The Eurozone recovery is also sensitive to the economic conditions in EM, particularly China. Germany is the engine of the Eurozone and its economy is exposed to Chinese production and imports. To the extent that the US rate normalization cycle depresses EM growth, Germany and other Eurozone countries could see slower growth. Similarly, there is the risk of a material monetary policy error impacting growth and inducing another recession. The ECB's decision to allow its balance sheet to contract contributed to the 2012 Eurozone recession, its second in four years.

United Kingdom 2016 Preview

2016 could possibly see a divergence in monetary policy between the Bank of England ("BOE") and the ECB. The United Kingdom ("UK") is forecast to grow real GDP at a faster rate in 2016 (2.2% vs. 1.8% for the Eurozone), unemployment is significantly lower (5.2% vs 10.7%) and core inflation is 1.2% in the UK. December 2015 PMIs are in expansionary territory, with Services particularly strong at 55.5. Finally, the BOE continues to hold £375B in UK sovereign bonds as a result of its own QE program. Putting a brake on all of this is the strength in the British pound which has weighed on exports. However, it is clear that the UK is the strongest developed market, after the US.

Complicating the picture further is the pledge by Prime Minister David Cameron's government to hold a referendum on UK membership in the European Union ("EU"). Without delving too deeply into the matter, UK citizens are primarily concerned with the requirement to fund sovereign bailouts and the inability to limit immigration into the UK. The EU is founded on the principle of the four freedoms of movement; goods, services, capital and labour, so an immigration limit for the UK is a non-starter. At the summit meeting in February, Cameron is likely to get emergency powers to limit some of the immigration impact on the UK. This might push the referendum vote out to September, especially with current polls running in favour of exiting the EU.

The BOE is unlikely to raise rates if they perceive that a referendum could bring about "Brexit", as exit costs could cut real GDP growth substantially in the short and long term. This could potentially push the beginning of the rate normalization cycle out to late 2016/early 2017. Ironically, under some Brexit scenarios, the UK could still be obligated to fund their pro-rata share of the EU's budget but would lose their ability to vote on EU policy. In addition, the UK could stand to lose a number of multinational company headquarters to Eurozone countries if the UK ceased to be in the EU.

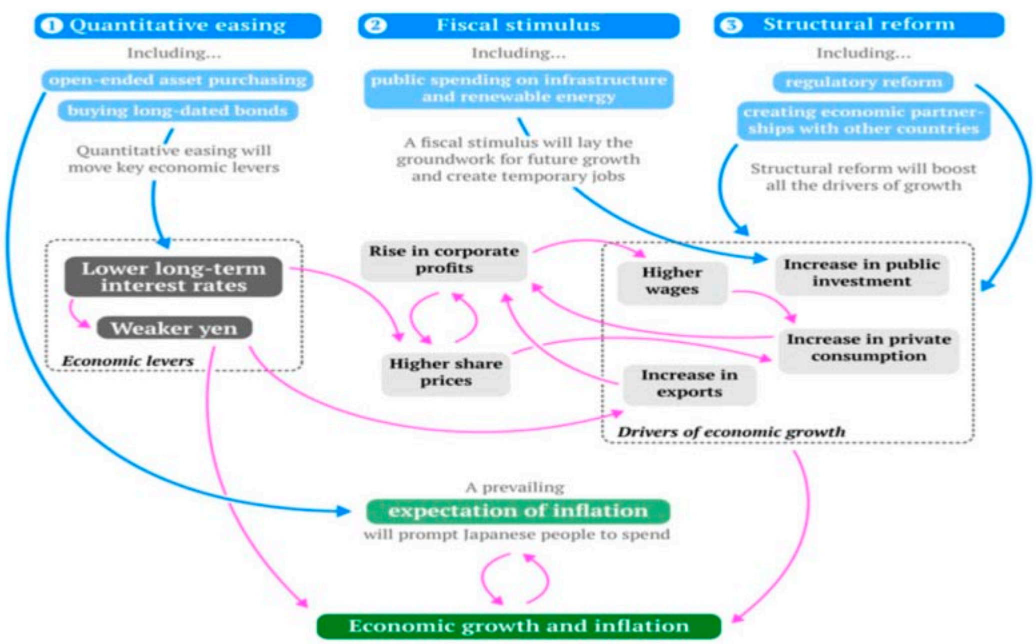
SOURCE OF IMPACTS ON UK OF BREXIT ON REAL GDP AND WELFARE, 2030								
	WORST-CASE BREXIT		UK-EU FTA 1		UK-EU FTA 2		BREXIT BEST CASE	
	%GDP	£BN	%GDP	£BN	%GDP	£BN	%GDP	£BN
Initial cost	-2.76	-70.65	-1.03	-27.92	-1.03	-27.92	-1.03	-27.92
EU budget saving	0.53	14.1	0.22	5.8	0.22	5.8	0.53	14.1
Unilateral free trade	–	–	–	–	0.75	11.9	0.75	11.9
Deregulation	–	–	–	–	0.7	19	1.3	36.7
Total welfare gain/loss	**-2.23**	**-56.55**	**-0.81**	**-22.12**	**0.64**	**8.78**	**1.55**	**34.78**

Source: Openeurope.org.uk.

Japan 2016 Preview

Japan is all in on the first two arrows of Abenomics. The Bank of Japan ("BOJ") continues to monetize ¥80T of sovereign debt every year, rates have remained very low and the Yen has depreciated sharply. Corporate taxes have been adjusted and the Value Added Tax (a sales tax) has been raised once so far with another hike set for 2017. The results of this campaign have been mixed as the Nikkei has generated strong performance but the economy has sputtered. A second technical recession (two consecutive quarters of GDP contraction) in two years was revised away in December and seemed to indicate that the Japanese economy was picking up steam. Annualized real GDP growth of 1% in Q3/15 was driven by business investment and the BOJ doubled down on this by announcing a small tweak to its stimulus plan. They will invest an additional ¥300B in ETFs that buy shares of companies "proactively making investments in physical and human capital". Should the spring 2016 wage negotiations yield real wage gains for employees then domestic consumption could yield another leg up in GDP growth.

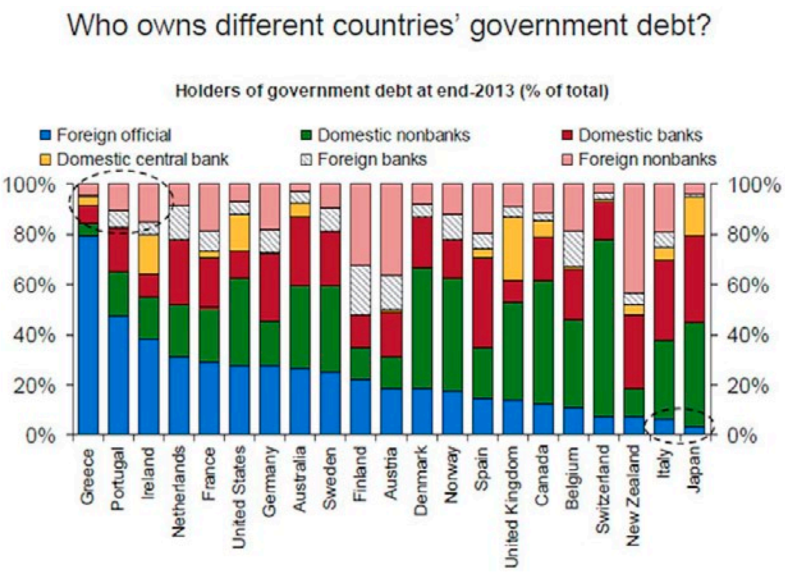
ABENOMICS EXPLAINED



Source: Ritchie / Quartz / www.quartz.com.

However, Abenomics is ultimately doomed to failure. Japan has essentially locked itself out of the public debt markets. Investors are unlikely to purchase 10 year Japanese Government Bonds ("JGBs") that yield 25 bps when the BOJ is actively targeting 2% inflation with a massive QE program. The BOJ's balance sheet is now equal to 69% of Japanese GDP, which makes it larger than the balance sheets of the Fed, BOE and ECB –COMBINED. Japanese public debt exceeds ¥1 QUADRILLION or 230% of GDP and continues to rise. The trifecta of negative real yields, capital depreciation and currency losses makes it difficult to float 10 year JGBs on the open market in an auction. Should the BOJ be successful in generating 2% inflation, the yield on the 10 year JGB must rise to attract a public market bid. If the clearing yield for 10 year JGBs rises to 2.5% the resulting increase in debt service costs would eventually bankrupt Japan.

MARKETS CHART OF THE DAY



Source: Arslanalp and Tsuda (2014). DB Global Markets Research.

However, most damning is the lack of meaningful market reforms to make the Japanese economy more competitive. Japan's work force is set to decline from 79 million people in 2012 to 71 million people in 2025. The natural offset to weak population growth is productivity (generate more GDP with less people). However, Japan has ranked last in the G7 in terms of productivity for decades. With debt continuing to grow and GDP under pressure, the answer might be aggressive immigration to bring in younger, skilled workers. However, there is little evidence that this is taking place.

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