Japan Equity

EQUITIES - JAPAN	1 Mth	3 Mth	YTD	12 Mth
MSCI Japan	-4.0	-7.0	-14.9	-7.6
Nikkei 225	-1.7	-5.8	-10.5	-2.4
Topix	-4.5	-6.4	-13.4	-5.9
Jasdaq	-4.9	-3.5	-5.3	3.6

Returns in Singapore dollars. Source: Bloomberg, 31 October 2011

In October, TOPIX ended at 764.06, marginally higher versus a month ago. While risk aversion remained elevated, the equity market stabilized as concerns of an economic slowdown in the US receded, expectations grew that monetary authorities in the emerging economies would loosen their policies, and a comprehensive agreement will be reached to address the fiscal problems in Europe. Selected sectors and stocks that had weak returns the past three months out-performed.

The five best performing sectors included Mining, Electric Appliances, Other Financial Businesses, Real Estate, and Machinery. The worst performers were Precision Instruments, Pulp & Paper, Metal Products, Electric Power & Gas, and Fishery, Agriculture, and Forestry.

Outlook and Strategy

	Policy	Change	Comment
Financials	Neutral	–	Post-earthquake re-construction could help bring forward loans growth. Office real estate sector outlook is dampened as the earthquake may delay the recovery in office rentals, although negatives are largely discounted.
Consumer	Neutral	–	Overweight consumer staples at the expense of consumer discretionary. Like selective opportunities within the retail space, e.g. niche players with room to gain share within the domestic market, and those with growing overseas exposure.
Technology	Neutral	–	Excess inventory overbuild is weighing on demand. Like tablet PC, ultra-book and smart-phone plays for the medium term.

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	Policy	Change	Comment
Energy	Neutral	–	Energy prices seen stabilizing following the recent weakness.
Industrials	Neutral	–	Selective exposure to companies which are beneficiaries of re-construction, and the trend towards automation.
Pharmaceuticals	Underweight	–	Like generic companies because of the Japanese government's push for more affordable drugs. Pipeline risks and upcoming NHI price revisions in 2012 make the sector unattractive as a whole.
Materials	Neutral	–	Electric arc furnace companies could benefit from post-earthquake re-construction. Also like selected specialty chemicals and electronic materials stocks.
Info Communications	Neutral	–	Anaemic top-line growth makes the sector relatively unattractive, but valuations and dividends provide downside support.
Utilities	Underweight	–	Regulatory risks in the new term post-nuclear crisis. Unexciting medium-term prospects; and fair valuations. Prefer gas companies to electric power companies.

In the near term, we expect events in Europe to dictate the direction of the global equity markets. In the meantime, leading indicators for Japan point towards softening of the economy for the rest of 2011, while the earnings revision index remains negative for FY11 and FY12. Although the market appears undervalued, any sustained rebound would require a bottoming out of both economic and earnings indicators. We maintain our defensive tilt for now. We are overweight Consumer Staples, neutral Industrials, Materials, Technology, Financials, Energy, and underweight Utilities, Pharmaceuticals, and Consumer Discretionary.

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