

Japan Equity

EQUITIES - JAPAN	1 Mth	3 Mth	YTD	12 Mth
MSCI Japan	-8.2	-6.0	-16.0	-7.4
Nikkei 225	-8.1	-4.3	-12.7	-0.9
Topix	-7.6	-4.8	-14.5	-6.5
Jasdaq	-2.0	0.7	-3.9	1.9

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

TOPIX plunged 8.4% to 767.14 in August. Sentiment continued to deteriorate globally, leading to a sharp sell-off in risky assets. Standard & Poor's downgrade of the US' AAA rating, the release of weak US economic data, and renewed concerns over Europe's financial problems ignited recessionary fears. Share prices of Japan equities also weakened because of the yen's appreciation against the US dollar. At one point on 19 August, the Y/US\$ rate reached its lowest level since World War II, at 75.95.

The five best performing sectors included Pulp & Paper, Electric Power & Gas, Other Products, Land Transport, and Fishery, Agriculture, Forestry. The worst performers were Maritime Transport, Transport Equipment, Mining, Iron & Steel, and Glass & Ceramics.

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.

Following the “V-shaped” rebound in recent months, leading economics indicators for Japan have stalled and appeared to be rolling over. Earning revision momentum has also turned negative after a brief recovery. The reasons for the renewed weakness included a sharp appreciation of the Yen since July, and weaker-than-expected global growth.

TOPIX price-to-book ratio of 0.9x, is only slightly above the March 2009 low of 0.8x. This suggested that share prices have largely discounted a recession (although not necessarily a full-blown global financial crisis). Going forward, we expect financial markets to remain volatile as long as Europe's sovereign crisis remains unresolved. For Japan, the appointment of Yoshihiko Noda as Japan's new prime minister offers some glimmer of hope. Noda's relationship with other parties could help to break the legislative gridlock in the Diet, and speed up reconstruction efforts; cushioning a possible downturn in 2012.

We are inclined to adopt a more defensive posture for now. We have reined in our bets on cyclical sectors in August, namely reducing Industrials to neutral. We have raised the weighting for Consumer Staples. We are overweight Consumer Staples, neutral Industrials, Materials, Technology, Financials, Energy, and underweight Utilities, Pharmaceuticals, and Consumer Discretionary.

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