REGIONAL MARKETS UPDATE

NORTH ASIA

Japan: 3.5 Stars—Attractive

- Eco Watcher's Outlook Index fell to 49.6 in Mar, down from 51.4 in Feb 18
- Feb Machine Orders rose 2.4% y-o-y, down from Jan's 2.9% increase.
- Consumer Confidence Index stay at 44.3 unchanged in Mar 18
- Apr Manufacturing PMI's preliminary figure rose to 53.3, up from 53.1 in Mar 18
- Exports rose 2.1% in Mar, higher than 1.8% in Feb 18
- Imports fell by 0.6% y-o-y in Mar, down from 16.5% in Feb 18

South Korea: 4.5 Stars—Very Attractive

- KRW depreciated by 1.9% against USD month-to-date (data as of 25 Apr), as compared to 2.3% appreciation seen in Mar 18
- Mar Manufacturing PMI fell to 49.1, down from 50.3 in Feb 18
- Exports rose 6.1% in Mar, higher than 4.0% in Feb 18
- Imports rose by 5.0% y-o-y in Mar, lower than 14.8% as in Feb 18

MARKET OUTLOOK

As at 25 April 2018, both the estimated earnings of Japanese equities for FY 2018 (ended March 2019) and FY 2019 (ended March 2020) have been revised by -0.3% and 0.5% year-to-date (in terms of fiscal year, ranging from 1 April 2018 to 25 April 2018) respectively. Earnings of Japanese equities are expected to increase by 3.6% and 13.9% in FY 2018 and FY 2019 respectively. On the other hand, earnings of the South Korean equity market are expected to increase by 7.6% in 2018 and 8.1% in 2019.

New developments related to trade-war points to further negotiation between China and the US. Within the month, China's president Xi Jinping outlined its plans at the Boao Forum to lower tariffs on automobiles, promote market's openness, improve investment landscape and strengthen intellectual property rights protection, most of which suits the US's demand and implicitly promotes negotiations. As for the US's side, president Trump has recently mentioned his intention to send Treasury Secretary and other economic advisers to China in attempt to foster a deal, while expressing his positivity in relation to remarks by president Xi to further open up the Chinese market.

By 18 April, 10 years US treasury yield once again rises amid higher inflation expectation, as market expect the Bank of Japan (BOJ) to maintain the loose monetary policy within April's policy meeting and keep its JGB yield target unchanged, the higher yield soon motivates the JPY to depreciate against the USD. By 25 April, it is trading at around 109 per USD, somewhat close to Japanese corporates' 110-111 per USD assumption when forecasting their FY2018 revenue. We now expect the yield gap between Japan and US to stay at current high level with the US 10-Year treasury yield entering consolidation after breaking the 3.0% mark, which shall limit the JPY's weakness. Further dissipation in trade-war fears could still push the JPY lower against USD, albeit in a much slower pace.

With gradual dissipation in trade-war fears and the recent JPY's depreciation, Japanese equities started to recover from the end-March bottom. We believe that trade-war risks will further dissipate in future while the JPY stay around current levels with a slight depreciation momentum, both of which should be favourable for Japanese equities. Looking beyond the above mentioned factor, the domestic economy remain in good shape with indicators pointing towards stronger domestic demand. Exports have decelerated in February and March, yet we believe external demand for machinery remains, and that the recent JPY's depreciation could give exports an extra push. The BOJ remains on course to keep its loose monetary policy as compared to its US and Europe peers. Valuation remains attractive with TOPIX trading at 14.1X, as compared to average of 14.9X as in 2013-2015's earning expansion phrase, not to mention that it includes no consideration of earnings estimates upgrades. Considering all the above mentioned catalysts listed above, we remain positive on Japanese equities.

As for Korea, worries against Semiconductor manufacturers' profitability subsided as Samsung electronics announced their guidance of 58% year-on-year growth for 1Q 18 by early April and reporting 52.2% growth in earnings by 26th of the same month. Similar to our expectations, strong demand for server memory chip remain supportive for the company's earnings, while an early introduction of Galaxy S9 also helps.

Moving on to the second quarter, we do expect the demand for memory chips to remain solid; overall semiconductor session should record another strong quarter for earnings growth, yet Samsung Electronic's earnings may face challenges as its display and smartphone business slow down.

As at 25 April 2018, the estimated PE ratios of Nikkei 225 Index are at 16.1X for FY 2018 and 14.2X for FY 2019; the estimated PE ratios for the KOSPI index was at 9.6X for 2018 and 8.9X for 2019. Valuations remain rather attractive compared with other markets. Thus, we maintain our star ratings of the Japanese and the South Korean market at an "Attractive" rating of 3.5 stars and at a "Very Attractive" rating of 4.5 stars respectively.

**Japan's fiscal year ended in March (e.g. FY 2017 ends in March 2018)

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