REGIONAL MARKETS UPDATE

NORTH ASIA

Japan: 3.5 Stars－Attractive

- Eco Watcher's Outlook Index fell slightly to 52.4 in Jan 18, down from 52.7 in Dec 17
- Machine Orders fell -5.0% y-o-y in Dec 17, down from Nov 17's 4.1% increase.
- Consumer Confidence Index stayed at 44.7 in Jan 18, same as Dec 17
- Feb Manufacturing PMI's preliminary figure fell to 54.0 Feb 18, down from 54.8 in Jan 18
- Exports rose 12.2% in Jan 18, higher than 9.3% in Dec 17
- Imports rose by 7.9% y-o-y in Jan 18, down from 14.9% in Dec 17

South Korea: 4.5 Stars－Very Attractive

- KRW depreciated by 1.0% against USD month-to-date (data as of 27 Feb 18), as compared to 0.3% depreciation seen in Jan 18
- Jan Manufacturing PMI rose to 50.7, up from 49.9 in Dec 17
- Exports rose by 22.2% y-o-y in Jan 18, higher than 8.9% in Dec 17
- Imports rose by 20.9% y-o-y in Jan 18, higher than 13.0% as in Dec 17

MARKET OUTLOOK

As at 27 February 2018, both the estimated earnings of Japanese equities for FY 2017 (ended March 2018) and FY 2018 (ended March 2019) have been revised by 10.8% and 11.1% year-to-date (in terms of fiscal year, ranging from 1 April 2017 to 28 February 2018) respectively. Earnings of Japanese equities are expected to increase by 20.4% and 9.9% in FY 2017 and FY 2018 respectively. On the other hand, earnings of the South Korean equity market are expected to increase by 8.4% in 2018 and 7.1% in 2019.

Japanese stocks, like most of the other equity markets, suffered from a correction within early February, its rebound is also relatively late compared to other stock markets, as the spike in market volatility pushed strengthened the JPY, which in turn suppressed equity prices.

In our perspective, the recent Japanese market slump seems to be irrational in nature, we therefore uphold our overweight conviction on the market despite its recent correction. While the market was tumbling, companies have been announcing upbeat earnings result for previous quarter. Regarding the TOPIX 100 index, excluding automobiles whose earnings are boosted by income tax benefits, most of the sectors are delivering above 20.0% earnings growth. Markets reacted promptly to the announcement, from a month-to-date perspective (ended 23 Feb), the index's estimated earnings has been revised upward by 4.4% and 1.4% respectively for the current and next fiscal year, illustrating just how positive investors are regarding the earnings scene.

Besides the strong earnings environment, there is also some certainty that Bank of Japan (BoJ) won't be changing its monetary policies soon; chances of a minor tightening increases as we move closer to end of the year since inflation and wages could pick up in 2018, but with the spring wage negotiation results possibly missing government's 3% target and the uncertainty in time needed for wage gains to translate into inflation pressure, the central bank likely will stay still until clear evidence indicates inflation is on uptrend. We are rather convinced that there won't be any tightening effort within 1H of the year, thus, any market action deriving from the fear of the BoJ tightening is likely immature.

As for South Korean equities, the earnings environment for semiconductor manufacturers and financial firms appear intact. The former industry benefits from continuous server demand, which helps companies to boost earnings on a year-on-year perspective within 1Q 17, despite its normal weak seasonality. As for the financial sector, with US interest rates rising amidst higher inflation expectations, Korea's policy rate has followed suit; sovereign bond yields has stayed firmly at the highest level since 2015 after its climb within January, which clearly spell great news for banks' Net Interest Margin (NIM) and hence their profitability.

As at 27 February 2018, the estimated PE ratios of Nikkei 225 Index are at 17.6X for FY 2017 and 16.1X for FY 2018; the estimated PE ratios for the KOSPI index was at 9.5X 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 equity markets 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)