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Connecting Markets East & West

Japanese Equities: 'Abenomics' & Opportunities

Presented by:

Peter Jenkins, Investment Specialist Nomura Asset Management UK Ltd

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March 2014

The Lost Decades: GDP and Market Size – ‘The Bubble Deflates’

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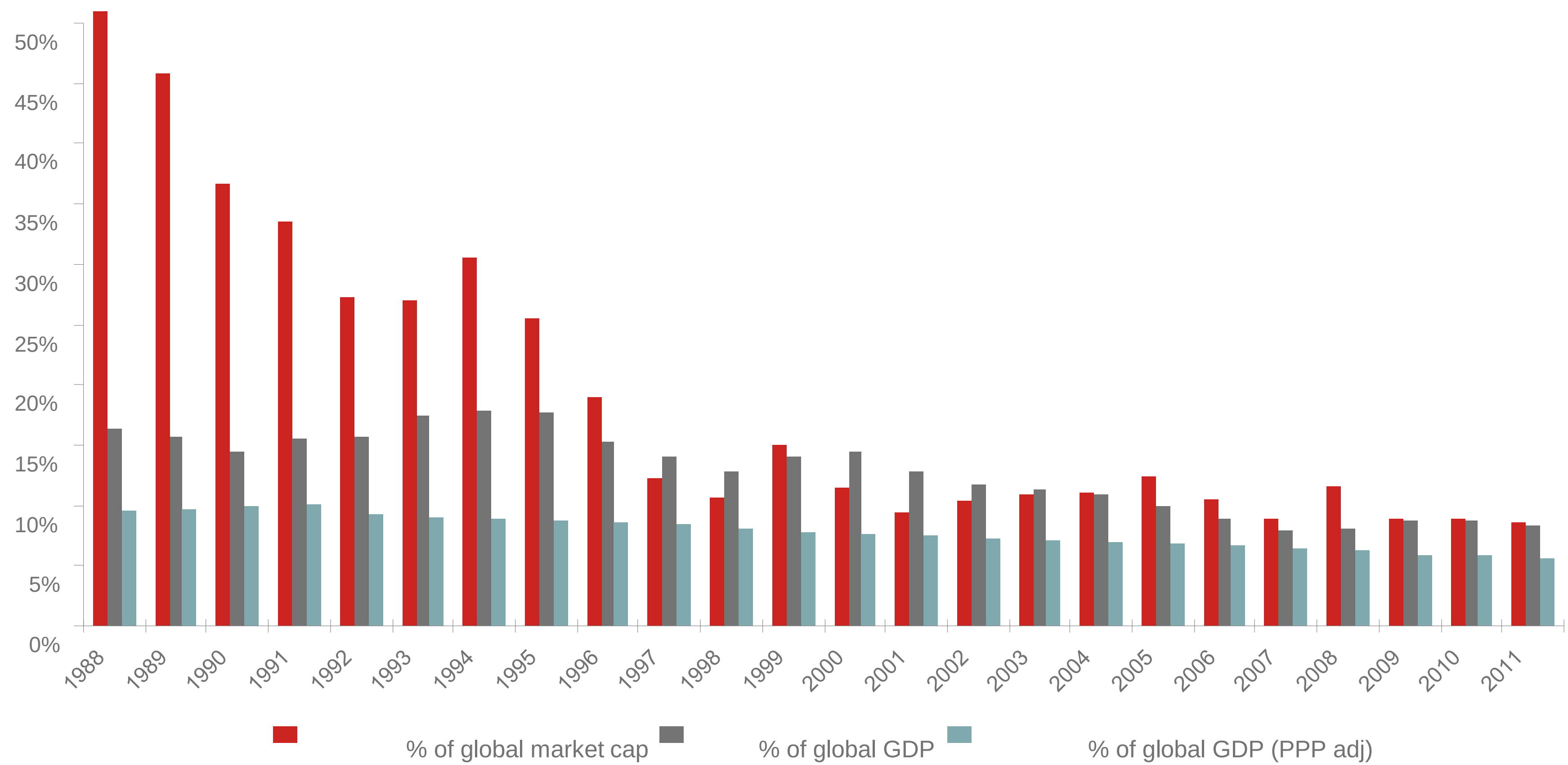
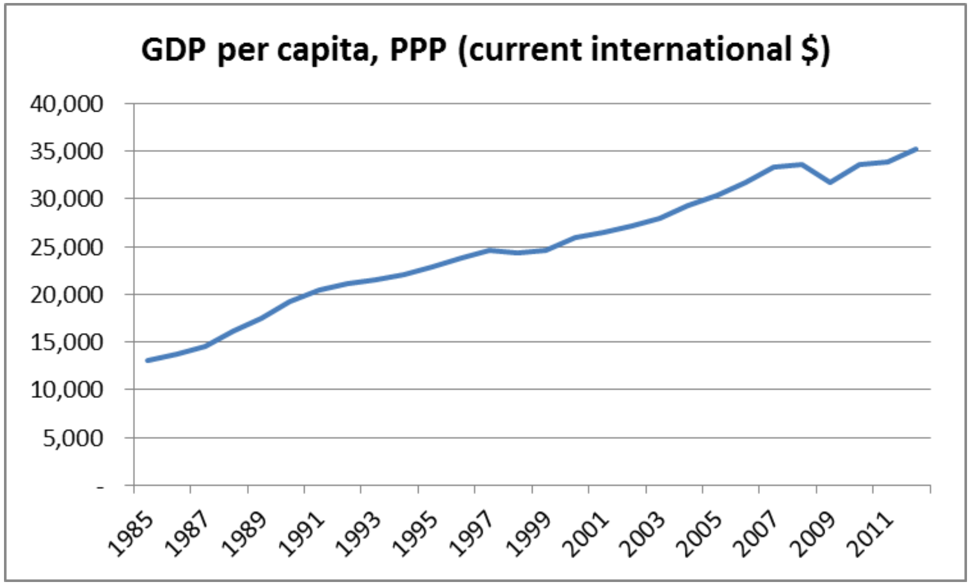
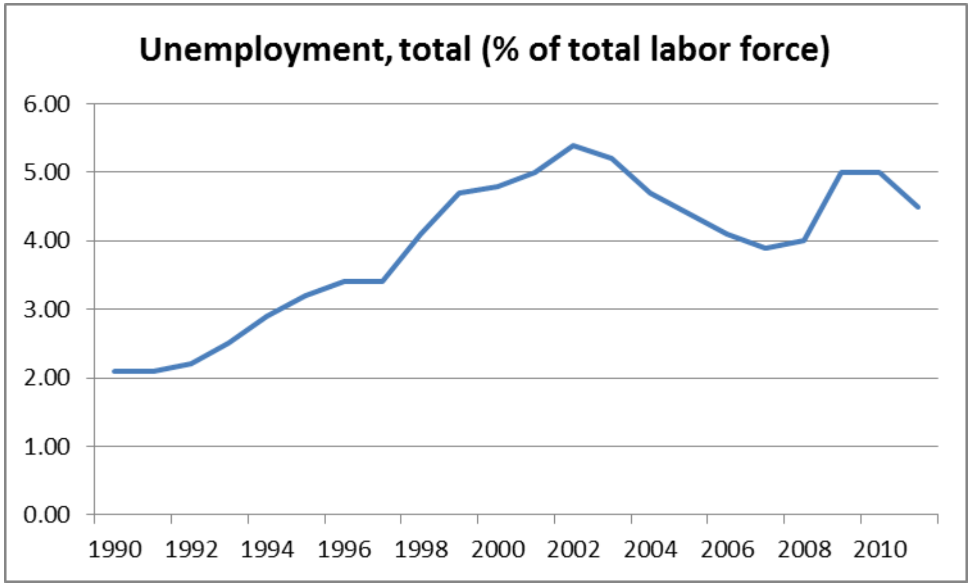


Source: IMF, MSCI

The Lost Decades: Comfortable Decline!



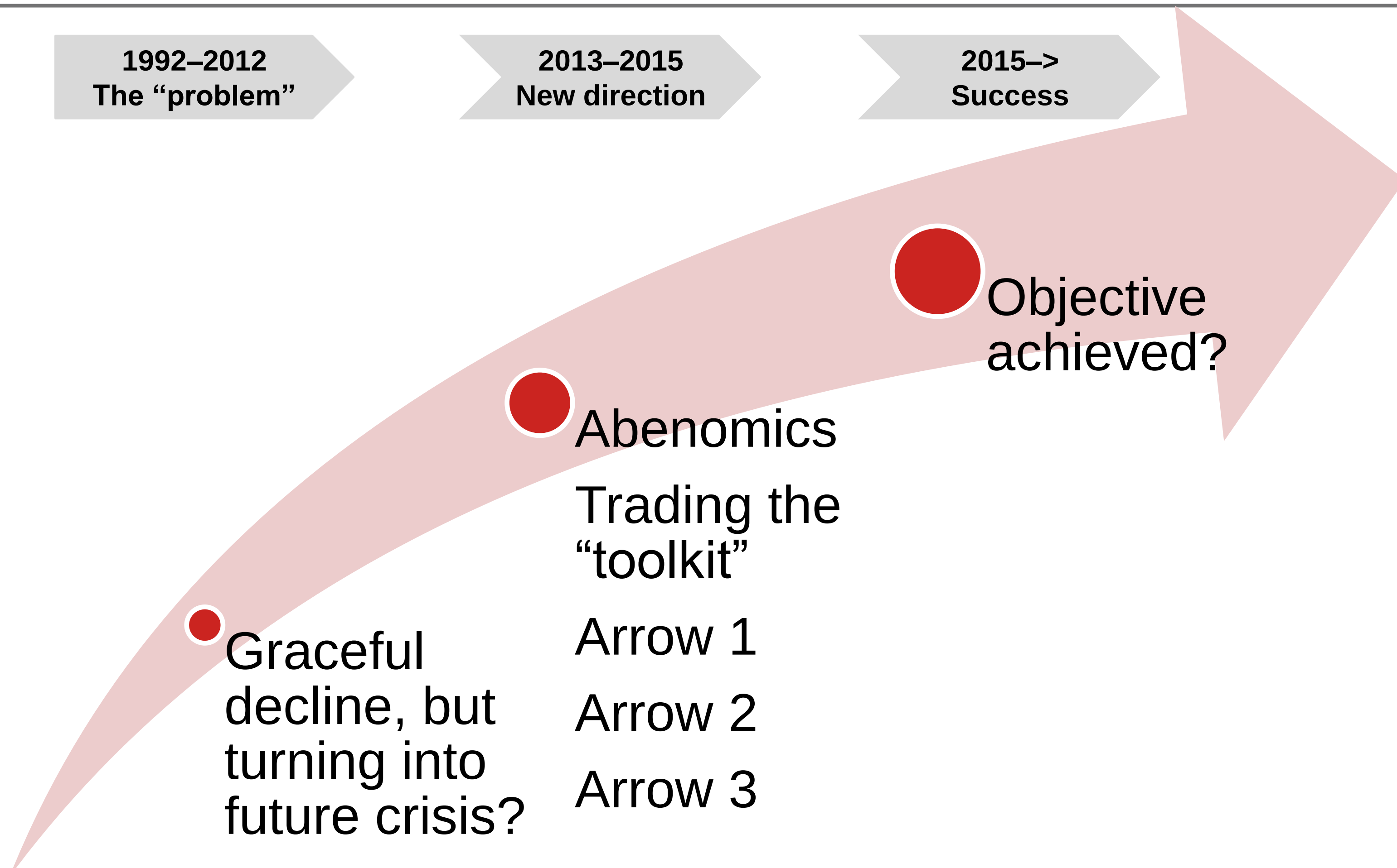


Source: World Bank

‘Abenomics’

Japan Embarks on a Multi-Year Process

A multi-year process



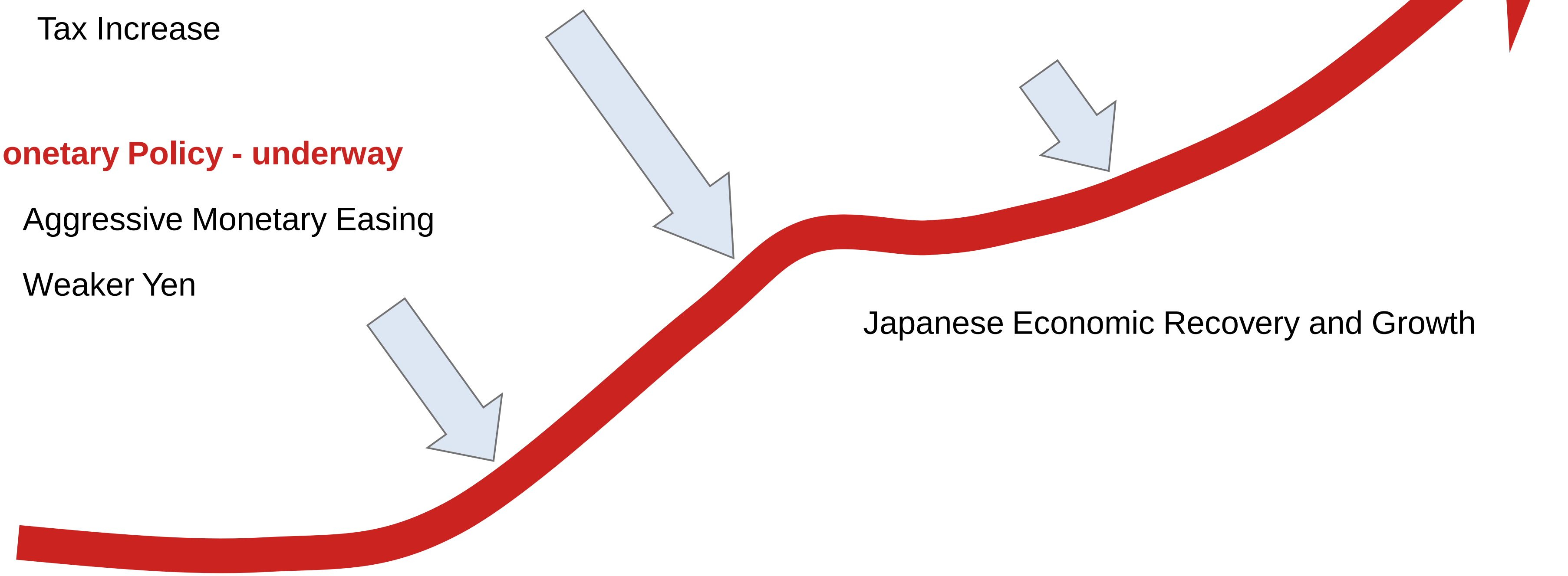
Source: Nomura.

“The Three Arrows” Changing the Tide?

- **Economic Restructuring – outstanding**
  - Leveraging Tax System to Increase Capital Investment
  - Labour market Reforms
  - Leveraging Longevity of the Society
  - Tariff Reductions – TPP
  - Encouraging inward investment

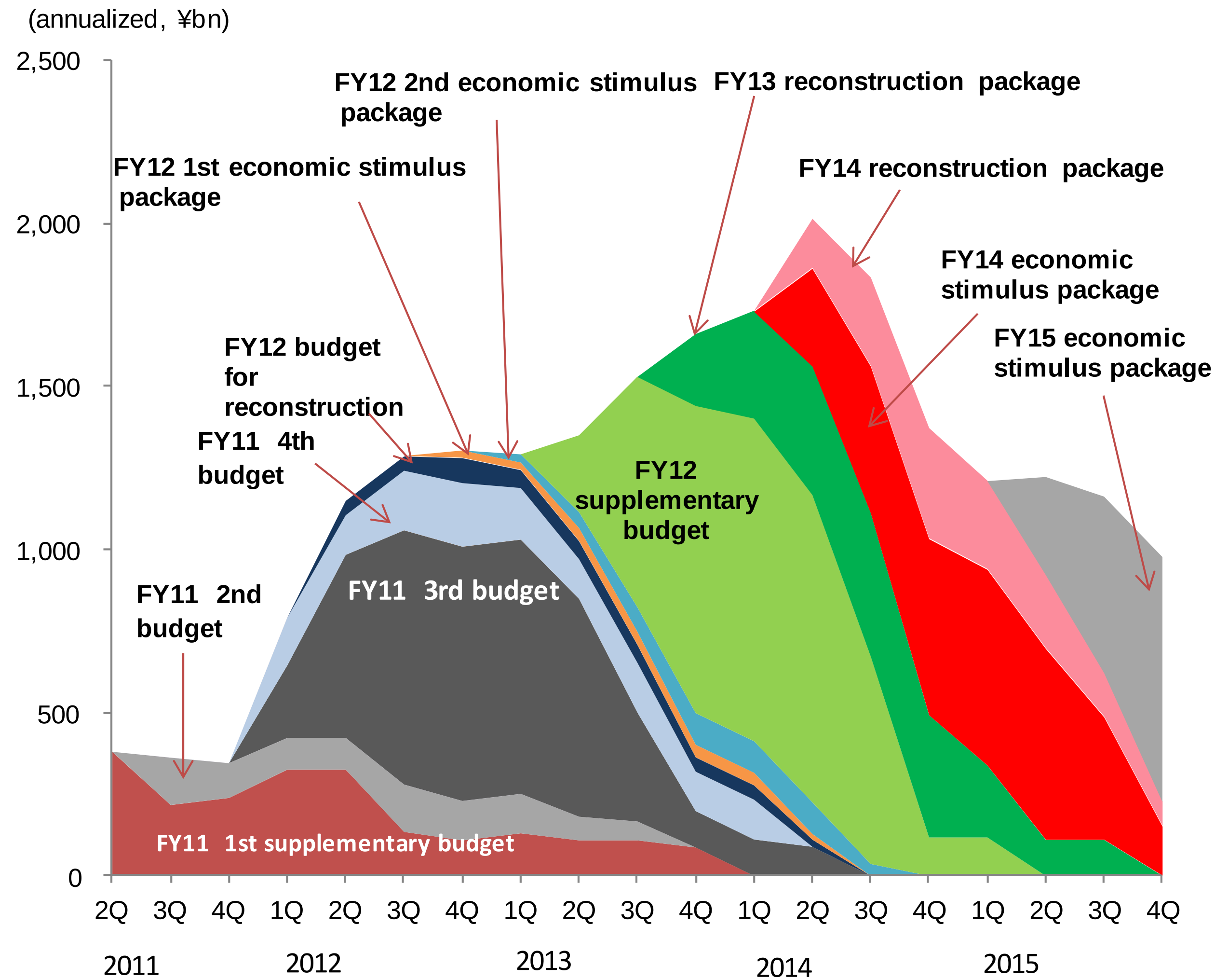
- **Fiscal Policy - underway**
  - Domestic Demand Stimulated by Public Investment
  - Fiscal Package to Offset Consumption Tax Increase

- **Monetary Policy - underway**
  - Aggressive Monetary Easing
  - Weaker Yen



First Arrow: Fiscal Stimulus

Forecasts for public works spending as part of reconstruction efforts and economic stimulus

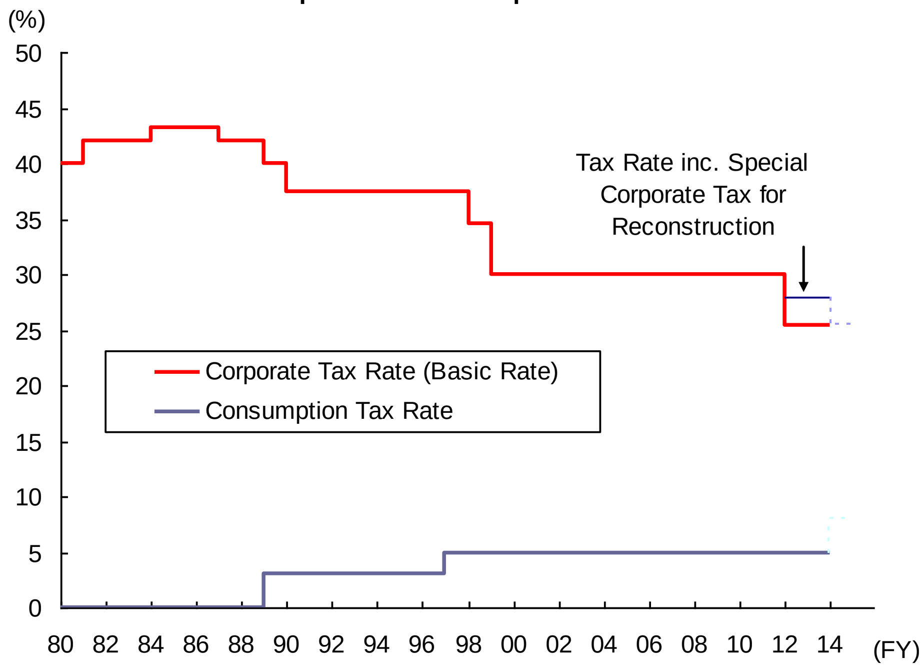


Source: Nomura Global Economics and MOF.

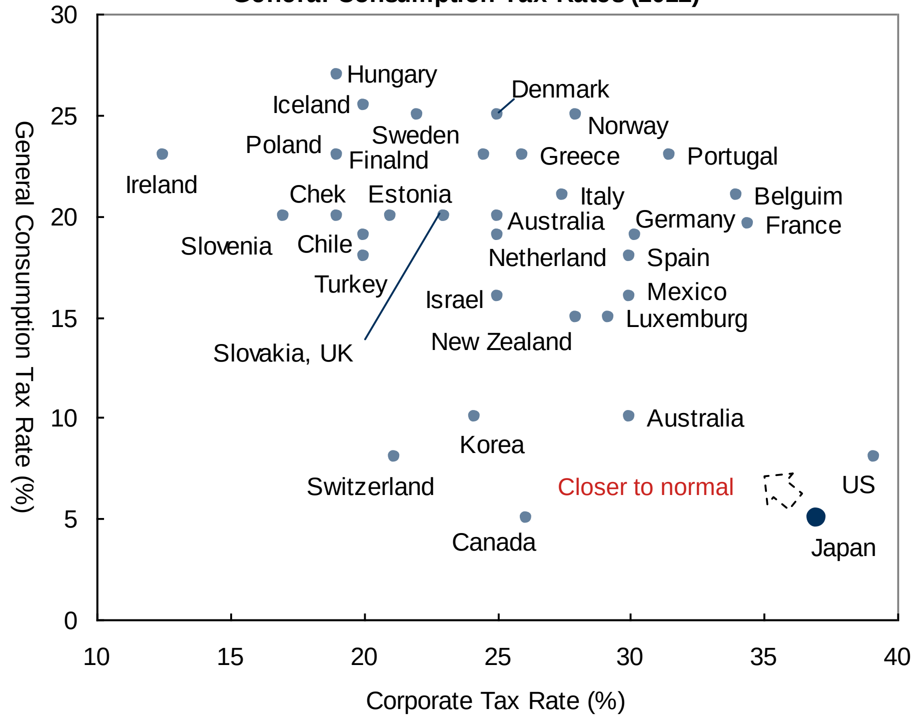
Fiscal Stimulus: Consumption Tax to be Raised

- On Oct 1, the Japan Prime Minister Abe made a decision to raise the consumption tax rate from 5% to 8% starting in next April.
- Measures to counter the downward economic pressure is to be formulated by December. This is estimated to amount to more than ¥5 trillion yen.
- The government has announced its intention to discuss the possibility of cutting corporate taxes after bringing forward the termination of the special corporate tax surcharge for reconstruction.

Consumption Tax and Corporate Tax Rates



OECD Countries Corporate Tax and General Consumption Tax Rates (2012)



Source: Bank of Japan, Ministry of Finance, Bloomberg, Nomura Asset Management

Second Arrow: Monetary Policy

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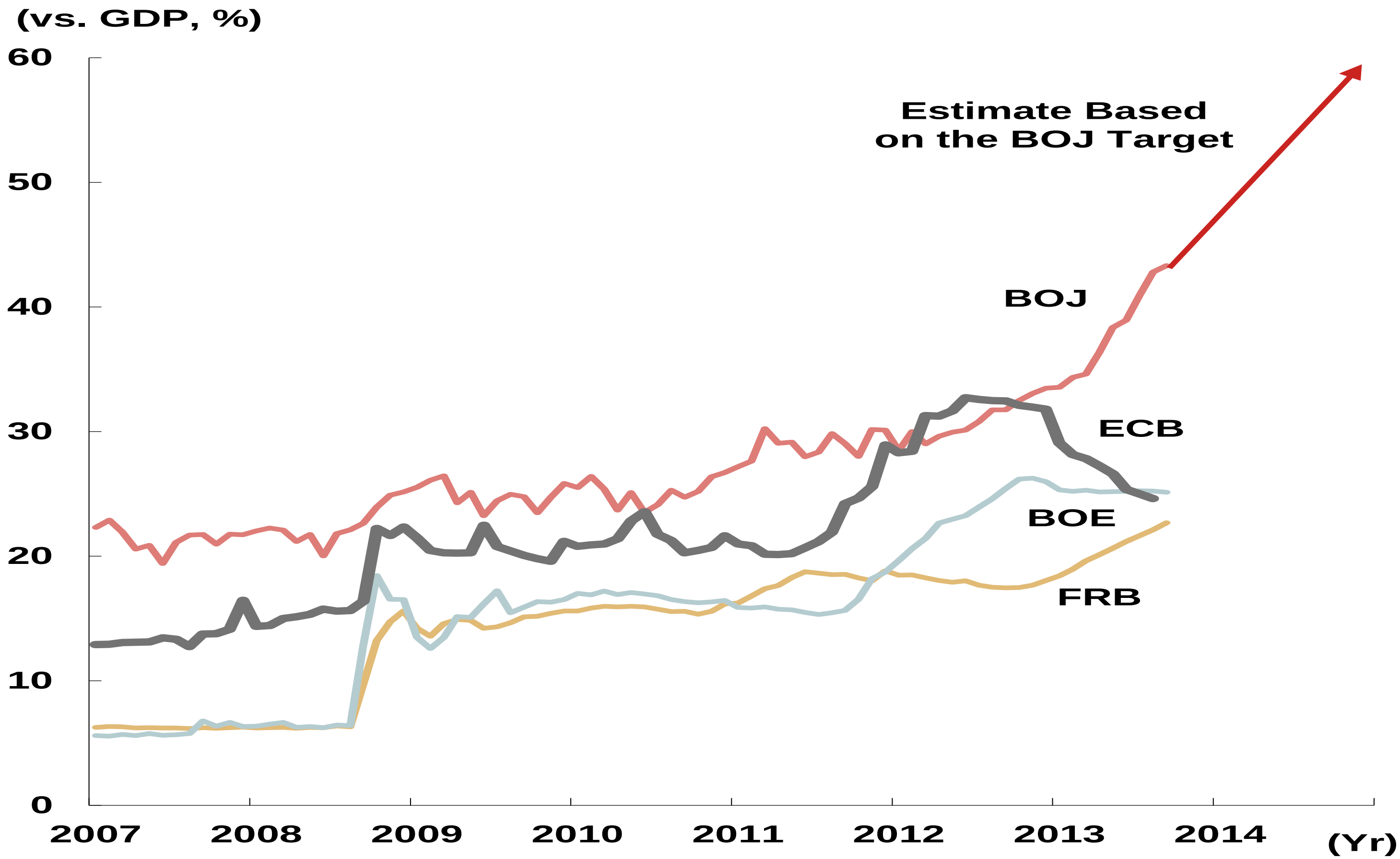
The BOJ's announcement on 4 April 2013

- ✓ Price Stability Target: **2%** (CPI), the earliest possible time, with a time horizon: about **2 years**
- ✓ Monetary base: **2 times** in **2 years**
- ✓ JGB holdings and the average remaining maturity of the purchases: **2 times** or more in **2 years**

Source: The Bank of Japan and Nomura Securities Co.

Monetary Policy: New dimension

Assets Held by the Major Central Banks



Source: NAM Based on CEIC data. As of the end of December 2013

Third Arrow: Growth Strategy

1. Revitalization of Japanese Economy
2. Strategic Market Creation
3. Global Outreach

- ✓ Industrial Competitiveness
- ✓ Energy Policy
- ✓ Labour and Employment
- ✓ Female Labour Participation
- ✓ Medical Services and Healthcare

Source: Nomura Securities Co.

Growth Strategies to Stimulate Private Investment

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"Japan Revitalization Strategy" approved by the Cabinet in June 2013 includes action plans such as
(1) Plan for Revitalization of Japanese Industry (2) Strategic Market Creation Plan and (3) Strategy of Global Outreach.
Measures under consideration include areas such as (a) Industrial Competitiveness (b) Medical and Healthcare (c) Labour market reform (d) More utilization of women and (e) Energy Policy. More concrete plans are expected to be announced in June 2014.

Industrial Competitiveness	Participation on TPP (Trans Pacific Partnership) and other free trade agreements.
	Launch economic diplomacy drive, including overseas visits by top officials to support infrastructure business.
	Establish Special Economic Zones where deregulation such as relaxation of floor space ratio / tax reform is introduced.
	Corporate governance such as greater independence on corporate boards via increased outside Directors.
Medical Services and Healthcare	Launch initiative "Medical Excellence Japan" with a view to promote Japanese healthcare internationally.
	Promote Research of regenerative drugs such as iPS (induced Pluripotent Stem) cells.
	Shorten approval periods for new drugs and medical equipment.
Labor and Employment	Facilitate shift of human resources from mature industries to growing industries (by increasing support subsidies etc.)
	Introduce mandatory practical English tests (e.g. TOEFL) for public sector workers
	Expand trial employment system that supports 3-Month trial employment
More Female Labor Participation	Call on major economic organization to ensure at least one female is appointed to the board of every listed company.
	Ensure that women account for at least 30% leadership position by 2020.
	Aim to eliminate childcare waiting lists by FY 2017 / extend childcare leave until a child becomes three years old.
Energy Policy	Restart nuclear power electric generation plants
	Deregulate electric power industry by separating generation and transmission / liberate electricity retail market
	Develop alternative energy such as methane-hydrate ("ice that burns")

Source : Nomura Asset Management from various sources such as Nomura Securities, Goldman Sachs Securities and Media reports.

Growth Strategy: TPP Impact on Growth

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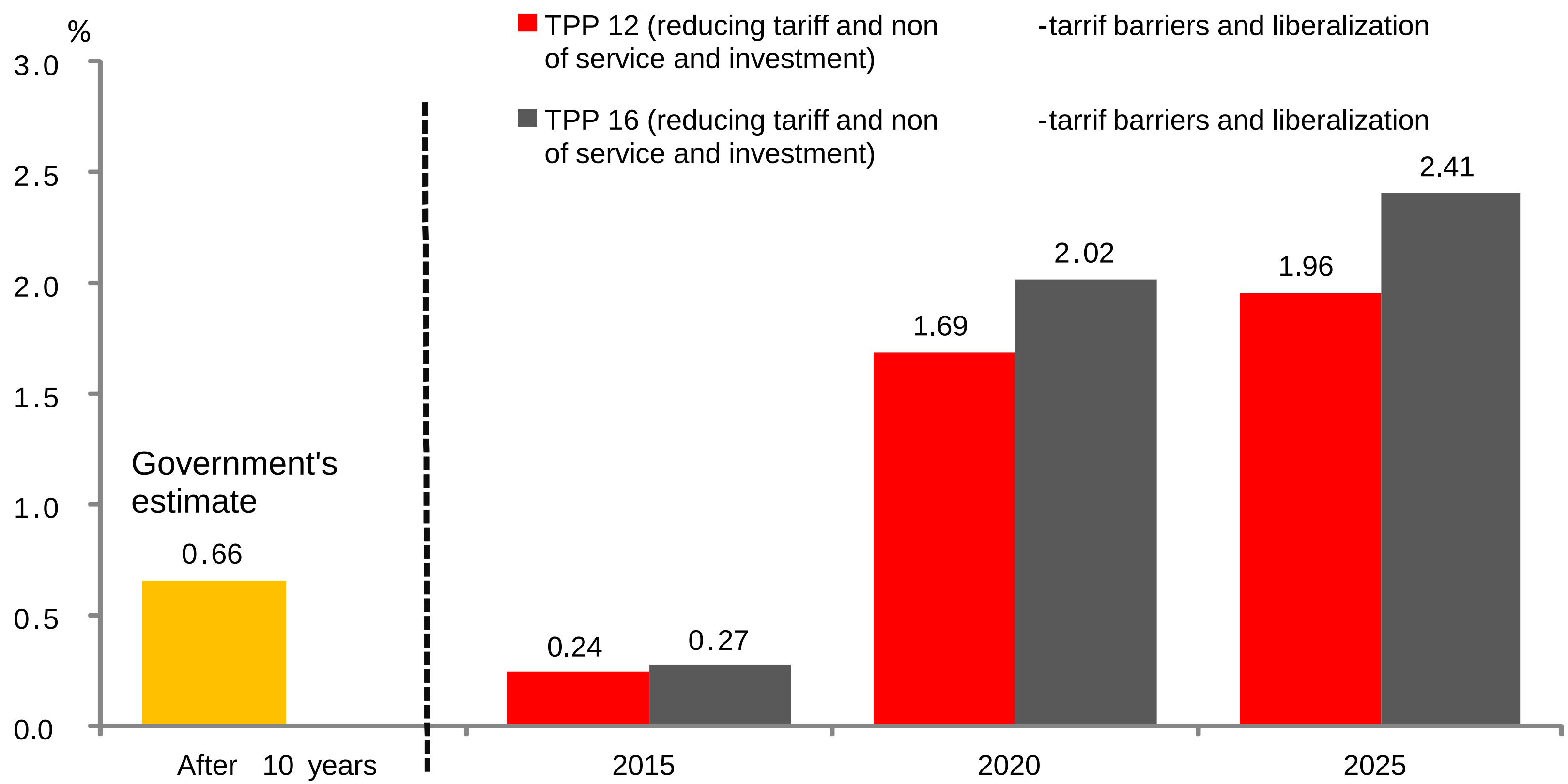
The TPP is a proposed free trade agreement under negotiation by Australia, Brunei, Chile, Canada, Japan, Malaysia, Mexico, New Zealand, Peru, Singapore, the United States, Vietnam and South Korea.

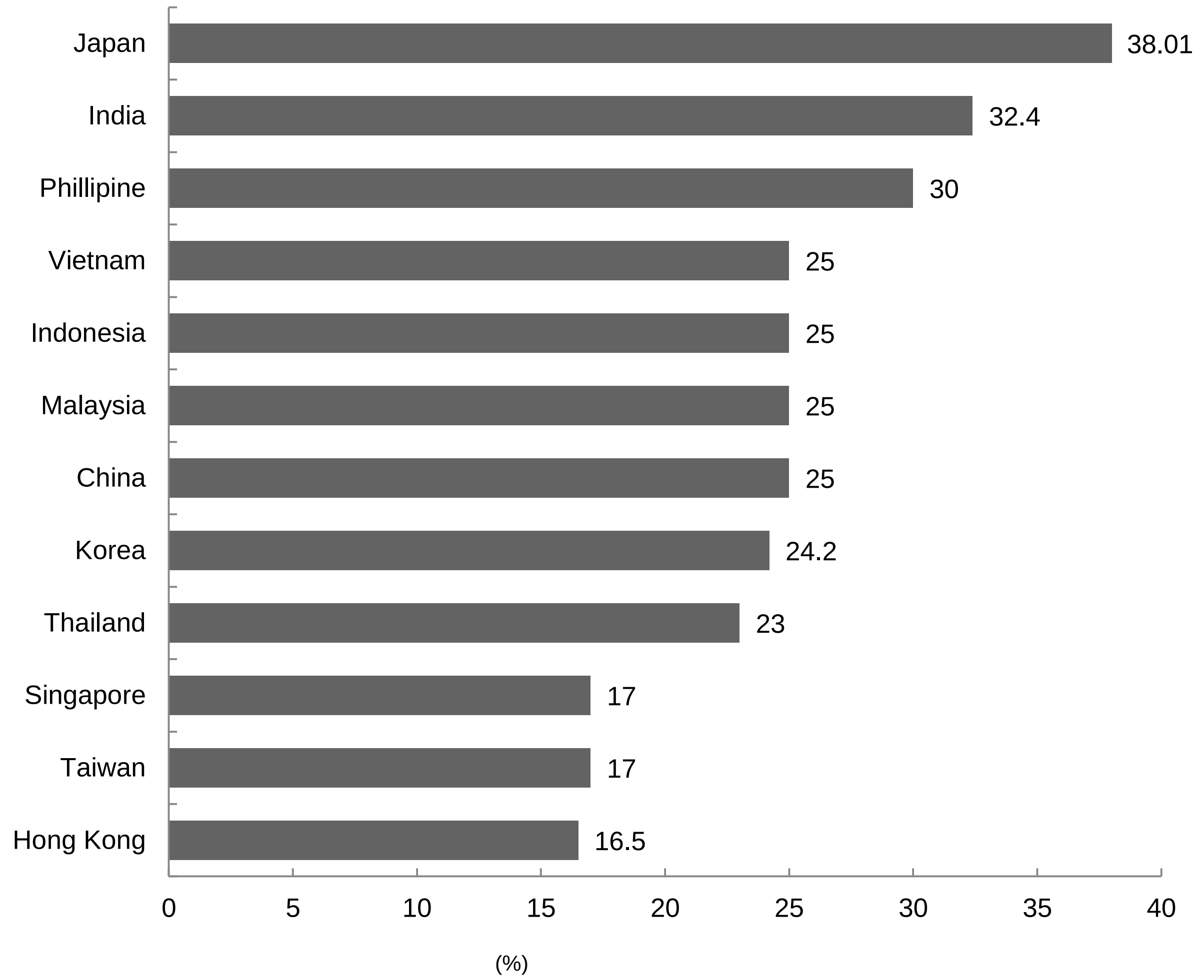
Impact of TPP on Japan's GDP growth:



Note: TPP 12 shows impact when the current negotiating 12 countries join TPP while TPP 16 assumes the participation by not only the existing participants but also Korea, Indonesia, Philippines and Thailand.
Source: Nomura from the Government of Japan and Asia Pacific Trade.

Corporate tax rate reduction is under discussion

Corporate tax rates across Asia



Source: Nomura, based on MOF data.

Corporate Story

Key Corporate Drivers in Japan

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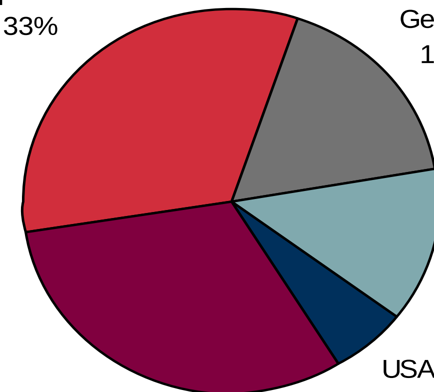
- **Improving Corporate Performance & Profitability**
  - Global earnings base
  - Capturing growth in domestic demand
  - Improving profitability
- **Corporate Restructuring**
  - Dividend increase
  - Share buy-back
  - Operational Restructuring and M&A
- **Attractive Valuations**
  - Valuations
  - Supply & Demand

Improving Corporate Performance & Profitability

iPhone – 'Designed in California, Assembled in China'



Heavy reliance on Japanese parts – Chinese assembly represents only 3.6% of total manufacturing costs.

Global Earnings Base - Examples

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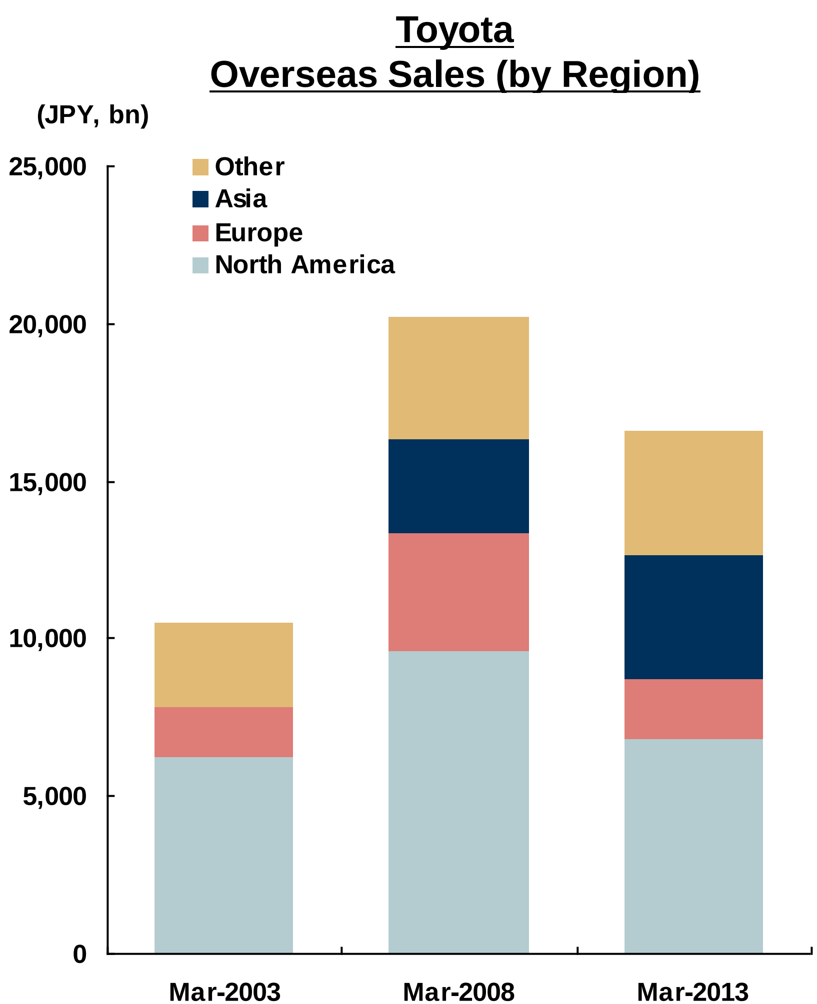
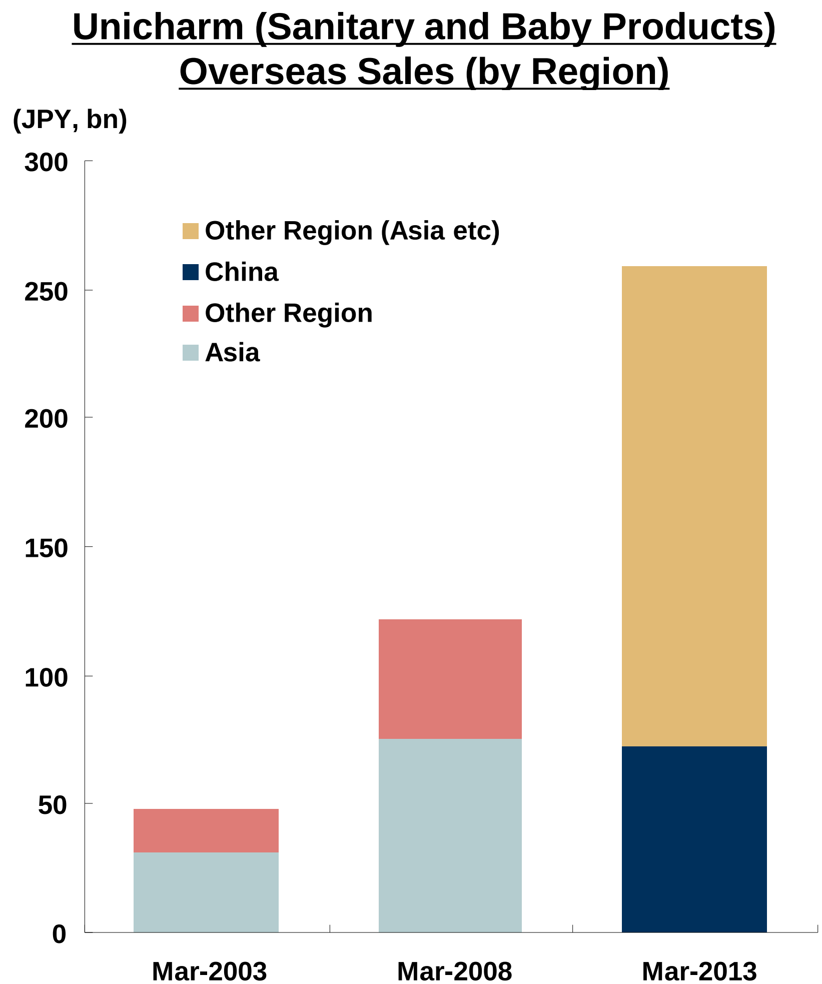


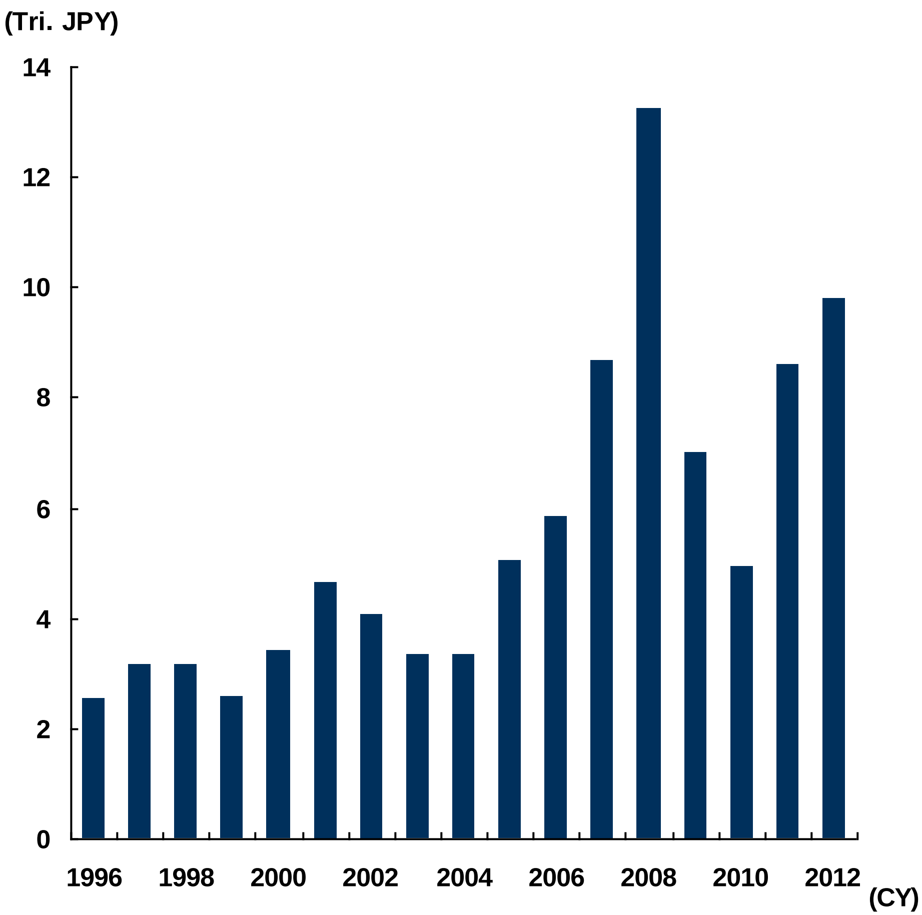
Note: The disclosure standard has changed as of the fiscal year ending March 2011. For Mar-2003, the Asia region is included in "Others".
Source: NAM based on company data



Note: The disclosure standard has changed as of the fiscal year ending March 2011
Source: NAM based on company data

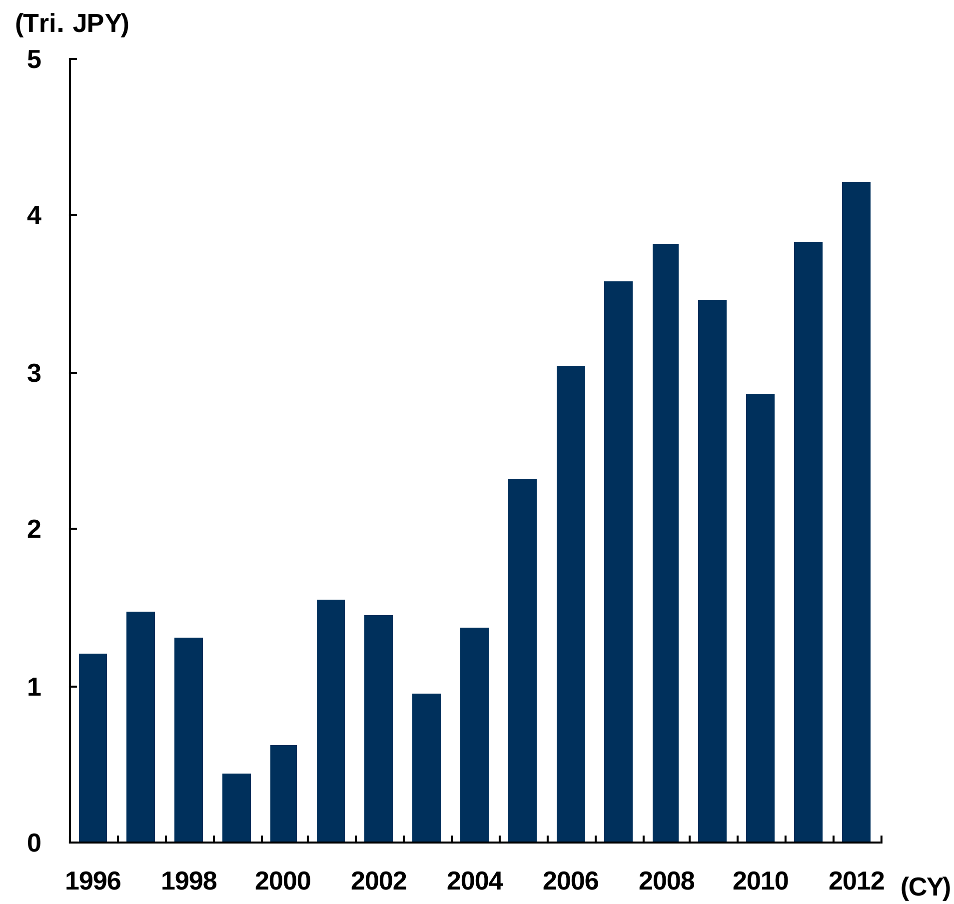
Global Earnings Base - Direct Overseas Investments

Japan's Direct Overseas Investments



Source, NAM, based on Ministry of Finance data

Japan's Direct Overseas Investment Revenue



Source, NAM, based on CEIC data

Corporate Restructuring

Improving Returns to Shareholders: Dividends

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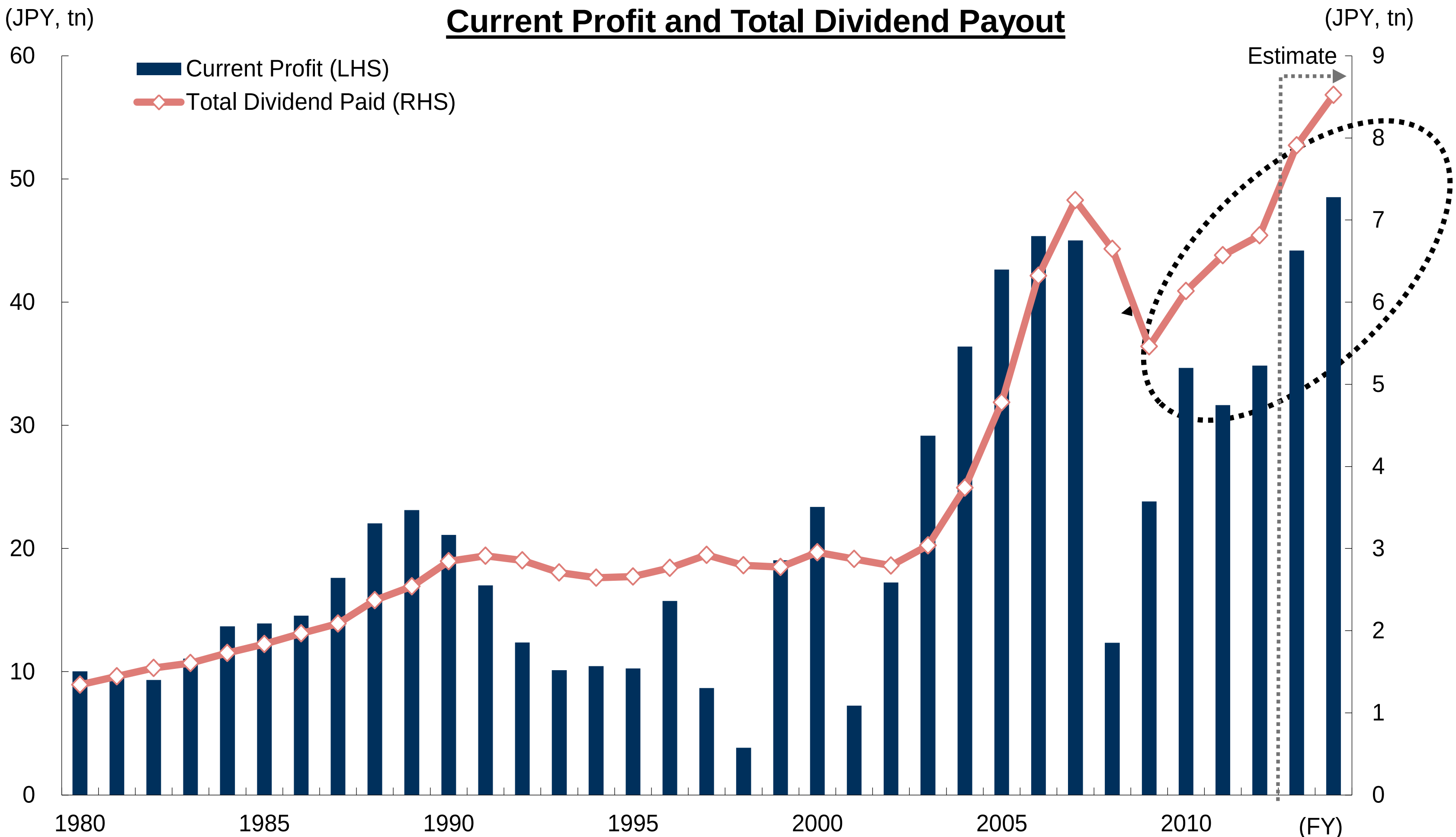
Current Profit and Total Dividend Payout



Note/source: TSE 1st Section. Nomura Securities Estimate for FY2013 and FY2014. Supplemented by Toyo Keizai data for stocks not covered by the analysts (as of 30 September 2013). Source: NAM based on Nomura Securities data.

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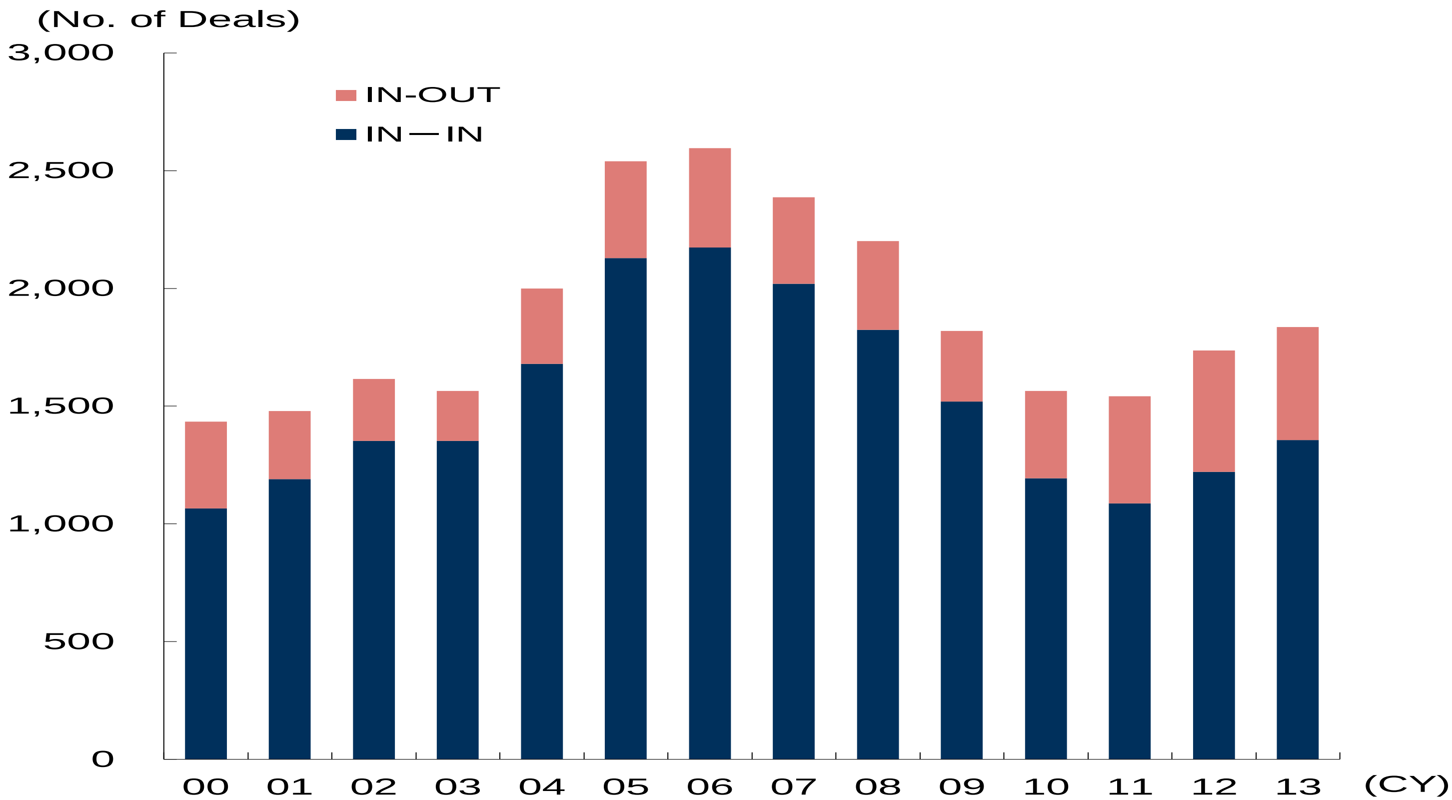
No. of M&A Deals Involving Japanese Companies

(2000 – 2013)

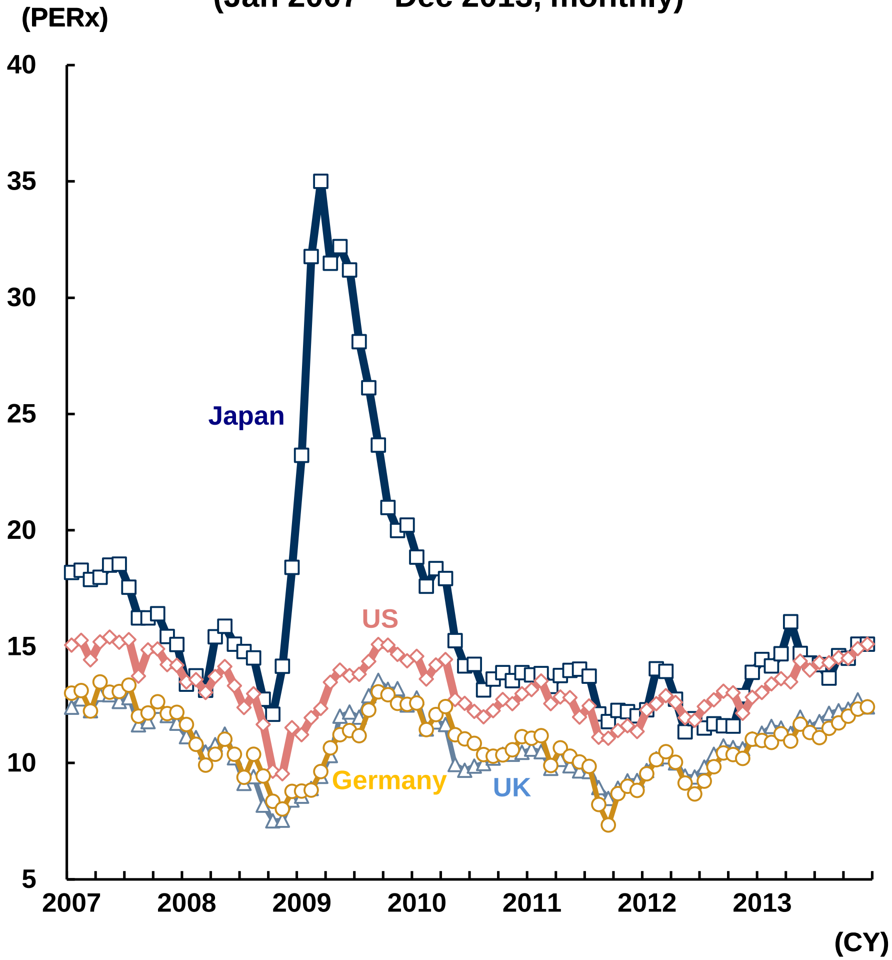


Note: Amount is based on announcements. IN-IN refers to M&A of Japanese companies, IN-OUT is M&A of overseas companies purchased by Japanese companies. CY2013 is as of the end of 31 August 2013. Source: Nomura Securities.

Attractive Valuations

Current Valuations

PER of Representative Countries
(Jan 2007 – Dec 2013, monthly)



Source: NAM based on Nomura Securities and IBES data, etc. 31 December 2013.

Valuation Comparison
(As of the end of Dec, 2013)

	Japan	U.S.	Germany	U.K.
PER (x)	15.8	16.7	14.2	14.1
PBR (x)	1.3	2.7	1.8	1.9
Dividend Yield (%)	1.7	1.9	2.8	3.6
10-Year GB Yield (%)	0.7	3.0	1.9	3.0
Yield Spread (%)	0.9	-1.1	0.8	0.6

Note 1: TOPIX for Japan, S&P500 for the US, FT100 for the UK, DAX for Germany.

Note 2: Yield spread = Dividend yield – GB 10-yr Yield

Source: NAM based on Nomura Securities, IBES, Bloomberg, Datastream data. 31 December 2013

Supply & Demand – Investment by Overseas Investors

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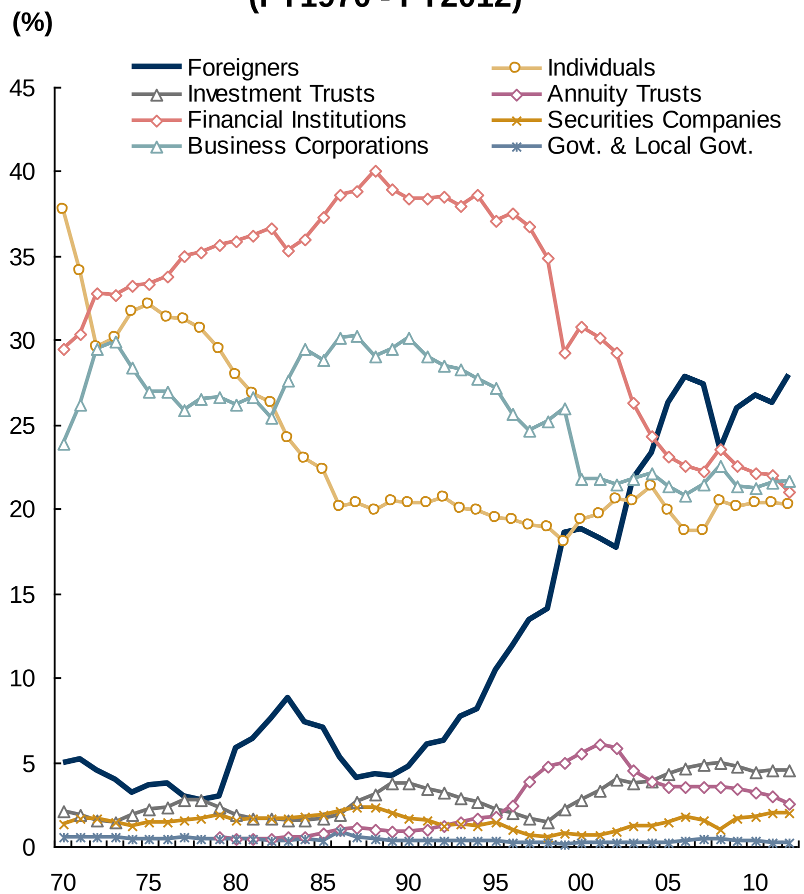
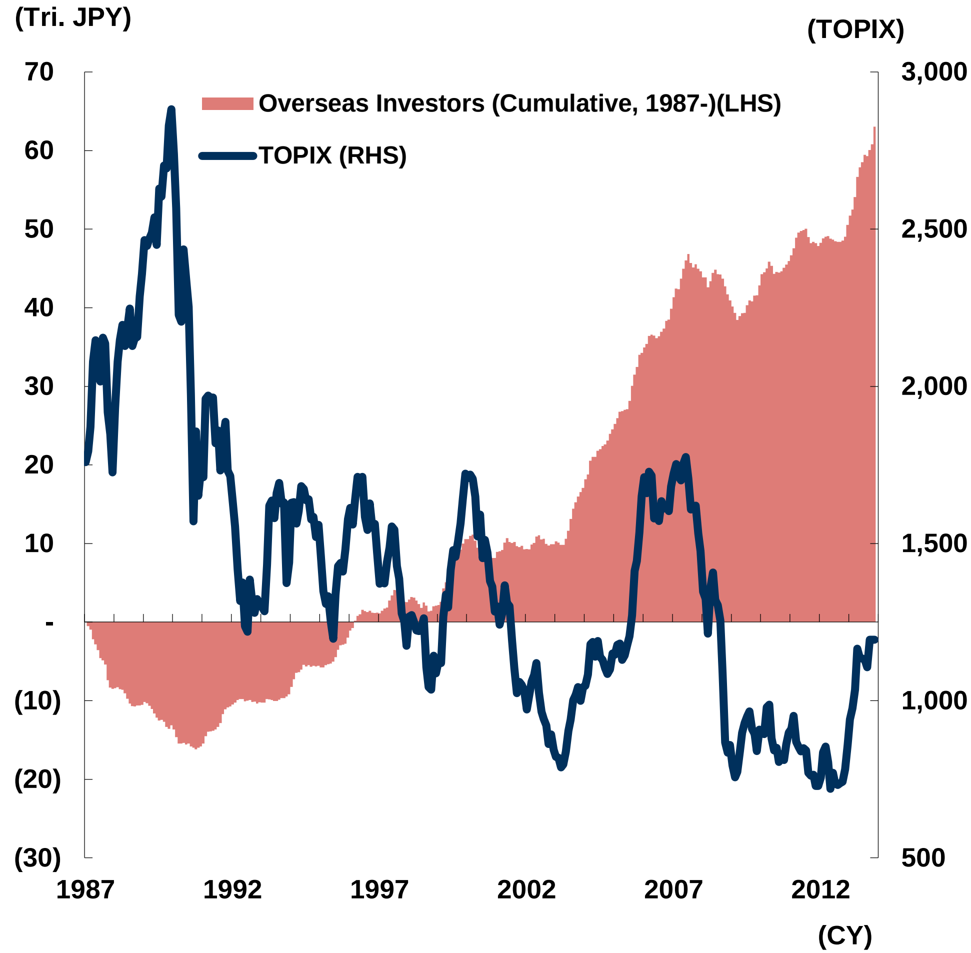
Shareholding by Investor
(FY1970 - FY2012)



Note: Financial institutions indicate financial stocks acknowledged by the TSE excluding investment trusts and pension funds.
Source: NAM based on TSE "Share ownership Survey" data.

Foreign Investors Trading Pattern
(TSE 1st Section, Jan 1987 – Nov 2013)



Summary

- The Japanese market performed strongly in 2013, driven by enthusiasm over 'Abenomics' along with its most tangible effect, namely currency weakness.

- The third arrow of Abenomics, namely structural reforms, will likely be the 'acid test' of the whole programme; supply side reforms could potentially lead to a big uplift in growth and an improvement in the long-term debt situation. However, there is much more work to do.

- Assuming progress in structural reforms we remain optimistic about the outlook for the market. The earnings picture has been very positive and structural reforms could improve the outlook further. Meanwhile valuations remain supportive.

- Over and above any cyclical recovery in the market we believe that there is a powerful investment theme in Japan, namely that of long-term corporate restructuring; something that the supply side reforms of Abenomics should facilitate. This promises a significant improvement in corporate performance largely independent of a cyclical recovery, delivering positive returns to investors as latent value is unlocked.

- However, as not all companies will embrace such changes and investors are advised to be highly selective in their stock-picking. They should aim to identify a combination of undervaluation and strong potential, looking for companies which have strong competitive advantages, that are developing new markets and that are well-placed to exploit change and industry realignments. They should look for management which sees the main business opportunities and which embraces the concept of shareholder value.

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