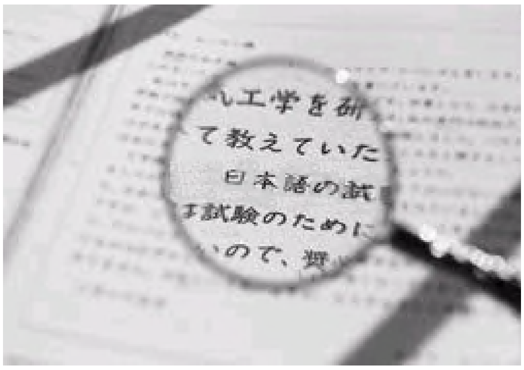
PM's Monthly Insight



FUNDAMENTAL ACTIVE GROUP

MARKET OUTLOOK AND INVESTMENT STRATEGY

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Market Outlook

We believe the Japanese equity market will continue to rise throughout 2018. Corporate earnings will grow as both the domestic and international economy expands, providing a boost to equity prices. Given rapidly increasing orders for machinery, semiconductors, and factory automation companies, as well as improved market conditions for, in particular, materials companies, such as those in the chemical and metal products sectors, we expect net profits at Japanese companies to outperform consensus estimates by 5% for fiscal-2017. For fiscal-2018, we forecast further net profit growth of roughly 10%. By 2018-end, we expect the Nikkei and TOPIX Indices to increase by roughly 15%, hitting 26,000 and 2,100 respectively, reflecting corporate earnings strength.

Labour shortages are making it increasingly difficult for companies to find non-permanent staff, creating upward pressure on their hourly wages. The jobs-to-applicants ratio has now risen above 1 even for permanent workers as companies look to increase permanent worker numbers due to the difficulty in hiring non-permanent workers. With demand for workers increasingly outstripping supply, wage growth rates are expected to rise, leading to increased consumption. Domestic capital spending is also increasing as investment in labour saving technologies rises against a backdrop of improved corporate earnings and labour shortages. Much of this capital spending is being directed toward IT and construction. Capex-related sectors, such as construction; machinery; electric appliances; as well as consumer durables which will benefit from increased consumption; and the services sector will lead the way improved earnings.

Bank of Japan (BoJ) Governor Haruhiko Kuroda restated his intention to continue monetary easing until the Consumer Price index (CPI) exceeds 2% in a stable manner. As such, accommodative monetary policy is likely to continue. CPI bottomed-out following rises in the prices of processed foods, hotel rates and services, but the BoJ's core CPI measure (excluding fresh food and energy) trended below 0.5%, meaning money tightening is not likely for the time being. Also, the possibility of unexpected monetary policy decisions made in the US and Europe and forex markets is unlikely.

Fiscal policy is a risk factor. As the preliminary budget always falls below the completed budget of the previous year, there always appears to be a fall in fiscal spending after April of each year. There is a chance stock prices will correct mid-2018. If this happens, the Upper House election set for 2019 will mean the government is more likely to implement certain economic policies, including the introduction of a supplementary budget. Geopolitical tensions surrounding both North Korea and the Middle East will also likely have a negative effect on equity market prices. We believe that through a combination of strong corporate earnings and accommodative monetary policy, stock prices will rise roughly 15% throughout 2018.

Investment Strategy

Overweight Sectors:	Underweight Sectors:
Construction & Materials	Foods
Financials (ex-Banks)	Retail Trade
Steel & Nonferrous Metals	Pharmaceutical
Machinery	Transportation & Logistics

We will overweight the construction & materials; financials; steel & nonferrous metals and machinery sectors, while underweighting the foods; retail; pharmaceutical; and transportation & logistics sectors. Within the construction & materials sector, we will overweight the metals and ceramics subsectors. We will be cutting our position in major construction companies due to on-going investigations into anti-trust law violations as well as the fact that strong earnings have already been priced into their share prices. In the financial sector, we will overweight the securities and insurance subsectors. We will overweight the steel & nonferrous metals sector because commodity prices are rising, and the machinery sector because orders are solid. Conversely, we will underweight defensive sectors such as food, retails and pharmaceutical.

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Daiwa SB Investments

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Mr Kamohara is the Lead Portfolio Manager of the Fundamental Active product. He started his career with Daiwa Securities in 1987 and transferred to Daiwa Institute of Research the following year to become a Japanese equity analyst. He was seconded to their Frankfurt office (between November 1992 and February 1995) and Hong Kong office (between February 1995 and March 1997) as an analyst for European and Asia equities respectively. He transferred to Daiwa International Capital Management, the former entity of Daiwa SB Investments, in 1998 to become a fund manager of international equities.

He became a Japanese equity portfolio manager in October 2000 and has managed the Fundamental Active product since its inception in October 2003. Mr Kamohara is lead manager on 11 accounts with USD6.2 billion under management.

Mr Kamohara graduated from Kyoto University with a BA degree in Educational Administration (1987).

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