



Update on Earthquake's Impact

March 15, 2011

We truly appreciate the many messages of sympathy, condolences, and encouragement expressed by our clients and the international business community. Nomura Asset Management has been able to manage our clients' assets and run its operations without any interruption since last Friday's earthquake, and we are determined that we shall continue to do so. We all hope that the rescue and relief operation for the victims of this disaster will proceed as swiftly and effectively as possible. Although this is the strongest earthquake in Japan's recorded history, we firmly believe in the nation's fundamental ability to meet this tremendous challenge and to restore and reconstruct our society with the help of international support.

We have made a rigorous assessment of the macroeconomic and stock specific-impact of this natural disaster. From the macroeconomic perspective, the situation is still uncertain, and we feel reluctant to quantify the damage at this stage given the enormous, and as yet unknown, number of lives lost. However, from our estimates, the potential capital loss will probably exceed that of the Great Hanshin-Awaji Earthquake (commonly known as the "Kobe Earthquake") in 1995 and reach a figure somewhere between JPY14 and 21 trillion (USD 180 to 260 billion), which is around 4% of Japan's annual gross domestic product (GDP). It is inevitable that Japan's production output will shrink for some time now, but economic activity is likely to recover sharply when the reconstruction effort begins later this year. On the stock-specific side, the impact of the quake and the tsunami will vary across sectors and individual stocks. Nevertheless, the direct damage appears somewhat limited for many manufacturers, some of which have factories located in the inland districts of the Tohoku region hit by this earthquake. The key bottleneck comes from the current shortage of energy and raw materials together with the damage to logistics networks. Damage to the supply chain will require a prolonged period to recover, but we believe it is only a matter of time before this is restored.

Developments relating to the damaged nuclear power plants in Fukushima prefecture require the greatest caution in the near term, and this is likely to be the main factor driving the stock market for the time being. Due to the reduction in nuclear power output, electricity rationing and phased power outages are taking place even in the Tokyo metropolitan area. Rationing is expected to continue until the end of April, and will be an additional drag on economic activity in Japan now as electricity shortages become a potential issue again in the summer. At present, the government is urging the nation to conserve energy, and efforts to economize have already started. Looking ahead, nuclear power production will be replaced by thermal power generation to meet shortages for the time being. As a result, concerns are focused more on the energy price rather than the generating capacity.

Today, Japan's stock market, measured by the TOPIX fell by 9.5%, bringing the total two-day loss to 16.3%. We believe the market crash seen today was exaggerated by fears surrounding the nuclear plant accident. It is difficult to speculate about the outcome of this nuclear crisis yet, but the market capitalization loss of more than JPY50 trillion seems excessive even when we take the potential infrastructure damage and economic slowdown into account.

More importantly, a number of stocks are trading far below their fundamental values, and we are attempting to take these investment opportunities.

In the currency markets, the Japanese yen is trading mostly between 81-82 yen per U.S. dollar. Despite the difficulties faced by Japan, there have not been any widespread capital outflows. The Bank of Japan on Monday announced additional easing measures in addition to emergency liquidity provisions. The Ministry of Finance is also signaling intervention in the foreign exchange market. These efforts will prevent the yen from strengthening to some extent. On the other hand, the repatriation of foreign assets will likely continue over the long term by Japanese investors and companies. The disaster in Japan has also started to impact global markets, and we expect the yen to remain a strong, albeit volatile, currency for now.

Fiscal requirements for reconstructing the economy and regional infrastructure will be an additional burden for Japan's already worsening budgetary situation. In the short run, liquidity support from the Bank of Japan and flight-to-quality sentiment will support the Japanese government bond market. Over the long term, Japan will need to address the issue of public finances more seriously; however, our new challenge will be to encourage an end to the political deadlock and a more consolidated effort to reverse the economic trend of the past 20 years.

One again, we thank you very much for giving your support to Nomura Asset Management. We remain committed to addressing your concerns and managing your assets with the utmost care and professionalism.

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