PRESS RELEASE

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NIKKO ASSET MANAGEMENT CO., LTD.

Nikko Asset Management's Economic Forecast Moderately Shifts Down Following BREXIT

Nikko Asset Management's Global Investment Committee (GIC) met for its quarterly review of global economic conditions. Based on the findings of its senior investment professionals around the world, the company periodically reconsiders house views on the major global markets and asset classes.

Despite the UK's decision to leave the European Union, the Global Investment Committee has noted that it does not think economies or risk markets will crash, but added that it is hard to be enthusiastic about the prospects for the post-BREXIT world over the next few quarters.

In conclusion, the investment committee has forecasted that global equities will decline a bit further and has initiated an overall underweight stance, regionally overweighting Japanese and U.S. equities. Due to the committee's expectation that global bond yields will decline moderately, it will overweight global bonds and USD cash for USD-based clients. For Yen-based clients, the committee emphasized fixed income investments as well.

The full report written by John Vail, Chief Global Strategist and Chairman of the GIC, is as follows:

Slowdown but No Global Recession, with EU Cohesion, but Struggling UK

Note: before the BREXIT vote, our Global Investment Committee (GIC) chose from three scenarios for each outcome; thus, the following market and economic targets for our BREXIT scenario were made before the UK vote.

Given the UK's decision, our Global Investment Committee does not think economies or risk markets will crash, but it is hard to be enthusiastic about the prospects for the post-BREXIT globe for the next few quarters. The tumultuous US Presidential campaign will not help sentiment either. **In sum, we expect an average of about one percentage point will be lopped off from recent GDP trends in major countries during the next four quarters, while the UK will likely descend into a moderate recession**. We have never been intense Euro-skeptics, and we still believe that **the Eurozone will remain intact, and that no other country will leave the EU**, as the UK is an unique country and the trauma of exiting would be too great for the majority of any EU member's voters to approve, but it will obviously be a tumultuous period. Clearly, the negotiations of UK's exit will be important to watch, as we believe the EU will be fairly generous on the goods trade, but quite harsh on the services trade and the timing of the exit, as although they don't wish to hurt themselves too much, they need to make sure that no other country thinks it is easy to leave the EU or renegotiate the terms of its inclusion.

As for the major economies, **US** consumer spending in real terms should moderate from high current levels and capex will likely remain negative. At 1.5**%** Half on Half Seasonally Adjusted Annualized Rate (HoH SAAR) in both the 2H16 and 1H17, GDP will be far from recessionary conditions, but much lower than the *circum* 2.3% (pre-BREXIT) consensus expectation. **Japan's** GDP will likely grow at a very subdued 0.5**%** HoH SAAR in the 2H16 and a bit higher in 1H17, compared to the consensus of 1.2% and 1.0%, respectively, with net exports and capex being the primary culprits. **Eurozone GDP should dip to near zero** in the 2H16 but expand by 0.4% HoH SAAR in the 1H17, vs. the (pre-Brexit) 1.7% consensus for each period. Here too, consumer spending should decelerate, along with capex and net exports. **China's** official GDP should achieve 5.9% HoH SAAR growth both in the 2H16 and 1H17 periods (translating to about 6.0% YoY growth), vs. the 6.4% consensus. Many of its heavy industries will likely be sharply curtailed by reform efforts and trade restrictions, but its services sectors should perform fairly well.

Note: all dates in this report are Calendar Year (CY)-based unless otherwise specified.

Other Emerging economies, having stabilized somewhat in recent quarters, are likely to decelerate substantially again due to lower commodity prices, lower global trade and continued political turmoil in many countries. External debt in USD terms, both bonds and bank debt, of EM corporates remains a critical factor to watch, especially as the latter can be withdrawn relatively quickly. Rating agency downgrades of the corporations, often linked to declines in the sovereign rating, are occurring much more rapidly these days and some of these corporates are very large debtors, especially in Brazil, one of the largest of which recently filed for bankruptcy.

How will Central Banks Respond?
Given Brexit, we do not believe the Fed will hike rates until December or later, while market consensus has now shifted to only about 10% chance of a December hike. With Brent declining to $46 at end September due to decelerating global economic growth, and by another $2 in each of the following two quarters, the US CPI is likely to hover around 1.2% YoY for the next several months and decline to 1.0% YoY at year-end (with core CPI at 1.7% YoY at that time). Even with non-farm payrolls growing at 100K/month and the employment rate below 5%, the Fed will be extremely hesitant to raise rates through year-end. As for both the BOJ and ECB, we only expect moderate cuts in the policy rate in the coming quarters, as policy is already extremely accommodative and doing a great deal more could well unleash fears of a monetary crisis. As for the BoE, we expect a 25 bps rate cut in the 3Q16 and in China, we expect the PBOC to reduce interest rates and/or the reserve ratio requirement several times in the coming quarters.

Brexit and US Elections

The US elections will be key to market sentiment in the coming quarters. The BREXIT outcome seems to boost Trump's chances, but if the UK economy and markets, including real estate, decline substantially on this news, such would likely detract from Trump's chances. Investors will be very wary of US polls and betting odds, so uncertainty will increase further and the fact that both candidates are anti-big business and anti-Wall Street, coupled with populist views on the current global trade and corporate tax regimes, confidence in US corporate profits will decline. Even if the Republicans win one chamber of Congress, both candidates have resolved to use executive orders and the bureaucracy to advance their goals without legislation.

Lower Bond Yields, a very weak GBP, but Stable Yen

Given our new scenario of economic deceleration, we expect yields to decline even further for the next two quarters. **For US 10Y Treasuries, our target for December-end is 1.45%, while those for 10Y JGBs and German Bunds are -0.25% and -0.10%, respectively.** For Australia we expect 1.85%. This implies (coupled with our forex targets) that including coupon income, the Citigroup WGBI (index of global bonds) should produce a 0.8% return from a base date of June 24th (after the BREXIT vote) through September in USD terms and +1.7% through December. Thus, we move to an overweight stance on global bonds for USD-based investors. This index should also perform well, at *circum* 1.5%, through September and December in Yen terms, and as for JGBs, we target the 10Y to have a 0.7% total return in Yen terms through December, so we are reasonably positive on both domestic and global bonds for Yen-based investors.

Thanks to Japan's continued super-aggressive monetary stance vs. the Fed, coupled with Japan's weaker economic growth relative to the US, **we expect the Yen to stabilize at 103:USD at end-September and 102 by end-December.** We expect the AUD to strengthen to 0.720 and 0.710 vs. the USD over those same time periods due to weaker global economic and commodity sentiment. As for the EUR, we do not believe the ECB will make any major QE moves and the region will continue its high current account surplus, which, coupled with likely capital repatriation, should push the currency to 1.14 and 1.15, respectively. Investors will likely be surprised by the eventual cohesion of the EU, as well. **On the GBP, we take a very bearish view, expecting it to decline to 1.30 and 1.27**, respectively, as troubles continue to mount politically and economically, while the BOE cuts rates and potentially even launches QE.

For those interested in the “barbarous relic,” we expect gold at $1350 by end-September and hold that value to December.

Shifting from Neutral to Underweight on Global Equities

We have been cautious on global equities since September and **our new macro-backdrop scenario results in a moderately negative view on global equities, particularly in Europe. While we don’t expect major problems for the currency or EU cohesion, the corporate profit outlook in Europe will suffer.** Equities should not perform too badly in the Eurozone, but the UK profit outlook will be quite poor, especially as the financial sector loses some access to the EU, and coupled with our very bearish GBP call, we expect continued very weak returns from the FTSE by the end of September. Aggregating our national forecasts from our base date of June 24th, we forecast that the **MSCI World Total Return Index will decline 3.8%** (unannualized) through September in USD terms (3.0% in Yen terms) and recover a bit in the 4Q to return -**2.9% from our base date** through December in USD terms (3.0% in Yen terms). We only expect a mild global equity rebound in the 1H17, as well, with continued negative returns from our base date. **Thus, we will shift from a neutral to underweight stance on global equities for USD- based investors (and Yen-based investors, as well).**

Why are we moderately bearish on US equities? If this crisis had hit when US equities valuations were at more reasonable valuations, we would not be as cautious, but we still think the market is too expensive and is trading more on dividend yield than PER ratios. With falling bond yields, this dividend yield effect should remain to some degree, but the rationale of this kind of investing depends (except for the most defensive sectors) greatly on the prospect of future earnings and global risk sentiment. Buying just for an additional 1% dividend yield over bond yields will not seem too advantageous when equity prices decline 10% and the dividend yield only rises slightly further due to such. Indeed, even after Friday’s decline, the SPX is now trading over **17 times NTM** (next twelve month) bottom-up consensus earnings**,** which is high in a historical context (and if one fully expenses for option grants, the PE is probably a full point higher, and this does not even include the recent expansion of supposedly one-off write-offs). **Thus, we expect a moderate de-rating due to lower global economic growth prospects, corporate profit outlook (especially with the USD stronger since BREXIT) and risk appetite.** One source of support is continued share buybacks, which are not affected much by economic fundamentals, while on the other hand, many hedge funds and volatility-based macro funds will likely be forced to deleverage. We believe uncertainty over the US election will also cause market jitters. In sum, these factors should drive the SPX to 1966 at end-September (-2.9% total return from our base date), and to 1981 (-1.6%) through year-end, which is obviously poor given the risks involved, but because this result is better than average, we return the US to a regional overweight for USD-based investors.

Eurozone equity prices in USD terms should fare similarly poorly in USD terms, for fairly clear reasons, with Euro Stoxx declining to 278 and 280, by end September and end December, respectively. FTSE, however, should decline to 5650 in each of these two periods, which Is a *circum* 11.5 % loss in USD terms through both periods. In sum, **we will take an underweight stance on the region** for USD-based investors.

Although many investors complain bitterly about Japanese equities, they actually performed in line with global developed-market equities through the 2Q in USD terms. The stronger Yen certainly has been a headwind, but coupled with low equity valuations and our expectation that the Yen will stabilize, we expect TOPIX to basically stabilize from its June 24th’s close, ending September at 1208 and December at 1184 (for a total return of -0.3% in USD terms and -0.5% in Yen terms). As important drivers, corporate governance continues to improve and buybacks are surging. Also, even though Japan’s economy is not very strong, this should not concern investors greatly. As we have long reported in our "Show Me the Money" pieces, we believe that Abenomics is working reasonably well, especially for corporations, with 1Q16 pretax profit margins (on a four quarter average) remaining near historical highs, within which the non-manufacturing sector remained at its peak. On an after-tax basis, the improvement is even better due to lower corporate taxes. Abenomics is, thus, working very well in many regards, and **in Japan, we do not see political disruption because it has maintained a highly egalitarian public policy despite being long-ridiculed by most Western investors and economists for such**.

As for the Developed Pacific-ex Japan region, we expect weak results in both Hong Kong and Australian equities through September and December, as both will be hurt by the decelerating global economy and weak global investor sentiment. Thus, for the region's developed markets, we expect a -5.8% unannualized return in USD through September and -6.7% through December, so for USD-based investors, **we will take an underweight stance on the region.**

In sum, we forecast that **Developed Pacific ex Japan, and Europe will underperform in the next six months, while the US and Japan should outperform and, thus, deserve overweight stances**.

Other Risks

As for geopolitics, clearly the increase in ISIS-related terrorist attacks in the West is a large risk factor now. Widespread attacks within MENA are also quite possible too, which could impact oil supplies. Worries about such will rise and fall, but the overall intermediate-term effect should be moderate. Other risks (including China's aggressive territorial claims, North Korea, Ukraine, other MENA unrest, EM political strife, etc.) will likely occasionally instill fears in risk markets, as well.

As for economic and credit risks (excluding the worst case scenarios of EU disintegration, a disruptive US election, or a wildly troubled UK), some speculators were likely badly damaged by the recent volatility, and there will likely be several credit events related to such, particularly in derivative markets and in the hedge fund arena. Whether this spreads to financial system fears is obviously important to watch. Elsewhere, emerging economies also remain a risk, and within such, corporations with large USD debts pose credit risks, especially as credit ratings decline. The likely default and messy workout of Puerto Rico, which would be one of the largest in history, does not help either, even if it contains some unique factors. The large debts within the US shale oil sector are also likely to remain a problem in the coming quarters as the oil price declines anew.

Investment Strategy Concluding View

We forecast that **global equities will, overall, decline somewhat further, so we will take an underweight stance overall, regionally overweighting Japan and the US**. Due to our expectation for global bond yields to decline moderately further, we **will overweight global bonds and USD cash for USD-based clients**. For Yen based clients, we emphasize fixed income investments, as well.

About Nikko Asset Management

Nikko Asset Management is positioning itself to be Asia’s premier global asset manager. The firm offers world-class asset management solutions for global investors, and has US$154.9 billion (17.42 trillion yen) in assets under management*. With more than 200 investment professionals**, the firm leverages its extensive global resources representing over 30 nationalities across 11 countries. Headquartered in Asia for over 55 years, Nikko Asset Management’s vantage point, extending east to west, distinguishes its investment approach.

For more information, please visit http://en.nikkoam.com/

* Consolidated assets under management and sub-advisory of Nikko Asset Management and its subsidiaries as of March 31, 2016.
** As of March 31, 2016, including employees of Nikko Asset Management and its subsidiaries.

Nikko Asset Management Co., Ltd.
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