

**Today's Topic** Japanese small cap stocks became undervalued  
**Testing the bottom supported by solid profit growth**

**Point 1** **October market corrected sharply**  
**Double-digit fall of TSE Small Cap Index**

■ In October 2018, Japanese stock market corrected sharply. TOPIX and TOPIX500(large cap index) fell -9.4% and -9.3%, respectively. Meanwhile, fall of mid-small caps stood out that \*TOPIX Small, TSE 2nd Section, TSE Mothers and Nikkei JASDAQ decreased -10.6%, -4.5%, 15.8% and 7.0%, respectively.

\*TOPIX Small: The index calculated by subtracting the names of TOPIX500 from TOPIX.

**Point 2** **Growth stocks corrected mainly in US**  
**Small caps with their growth characteristics weakened**

■ In October, global stock market consolidated triggered by US stock market fall due to (1) concern over US-China friction and (2) US long-term interest rate hike. Fall of Japanese stock market accelerated entering into the second half of the month due to concern over deterioration of Japanese companies' profits affected by possible Chinese economic slowdown.

■ Japanese small cap stock market which contains large number of high earnings growth stocks weakened as US high-tech stocks supported by high earnings had fallen.

**Outlook** **Japanese small caps became undervalued**

■ Small cap indexes had fallen sharply after 2015 China Shock. At that time, stock price dropped as estimated earnings per share(EPS) decrease due to business performance deterioration. However, mid-small caps' corporate earnings had been solid since later 2016, even in year 2018.

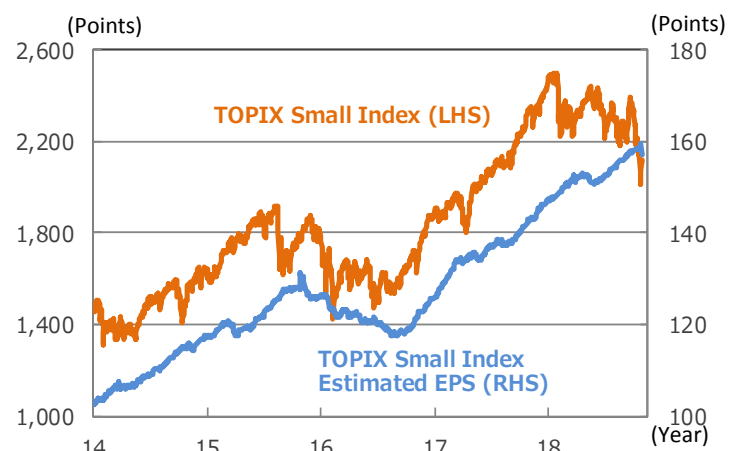
■ Estimated EPS (explaining relation of stock price and estimated earnings) decreased to 13.5 times as of October end from average EPS of 14.3 times since 2014. It dropped to 12 times level in October 26 and 30, below 13.3times which is average minus 1 standard deviation since 2014. We expect Japanese small caps to test the bottom as it has undervalued maintaining a strong earnings growth.

Performance of Japanese Stock Price Indexes

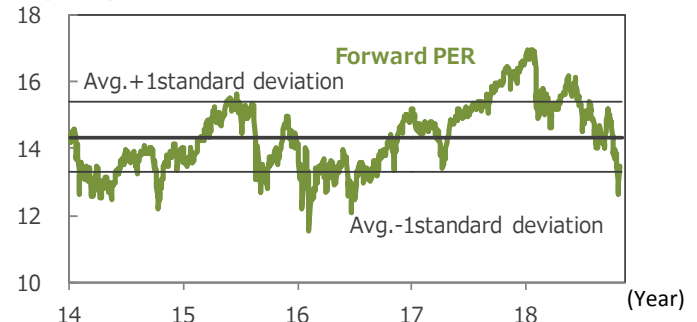
MM/DD/YY	12/29/17	9/28/18	10/31/18	Change from September (%)	Change from 2017 Year End to End of October 2018 (%)
TOPIX	1,817.56	1,817.25	1,646.12	-9.4	-9.4
TOPIX500	1,395.49	1,399.60	1,269.85	-9.3	-9.0
TSE Small Cap	2,427.08	2,366.13	2,114.71	-10.6	-12.9
TSE 2nd Section	7,275.86	7,358.34	7,024.98	-4.5	-3.4
TSE Mothers	1,231.99	1,077.55	907.56	-15.8	-26.3
Nikkei225	22,764.94	24,120.04	21,920.46	-9.1	-3.7
Nikkei JASDAQ	3,950.46	3,831.49	3,563.17	-7.0	-9.8

(Note) Unit for Nikkei225 and Nikkei JASDAQ is JPY. Unit for other indexes is Points.  
 (Source) SMAM, based on QUICK data.

TOPIX Small Index



(Times)



(Note1) Data from Jan 6 2014 to Oct 31 2018. 12 months forward estimate as Estimated EPS, of Bloomberg L.P.  
 (Note2) Forward PER = Share price/Estimated EPS  
 (Source) SMAM, based on Bloomberg L.P. data.



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