

Equities

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Eastern Japan earthquake/Food sector

Alert: Spike in demand for instant noodles, Kirin plant a worry

■ Industry Overview

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- **Conclusion** — We estimate that the earthquake-afflicted prefectures of Iwate, Miyagi, and Fukushima account for 5% of nationwide food consumption. Among plants, we understand Kirin's Sendai plant has been badly damaged. There has been a spike demand for instant noodles, although we expect it to be only temporary.
- **Plants** — At Kirin's Sendai plant, four storage tanks were damaged and there are no immediate prospects for a resumption of operations. Kagome expects its Nasu plant to take a month or more to get back to normal. There are no reports of major damage at Asahi Breweries, Ajinomoto, or Nissin Foods Holdings. We understand Toyo Suisan's Sanriku aquaculture facilities were damaged, but there was no damage to its noodle facilities. Yakult reports damage to some facilities at its plants in Iwate and Fukushima. JT has suffered from a leak and other damage at its Kanto plant but looks to be able to offset this with increased production at its Tokai plant.
- **Consumption** — Overall shipment volumes are rising at the food wholesale stage. Demand for instant ramen is shooting up. Toyo Suisan is at full production and sales of Nissin Foods products continue to rise by double digits. Demand for bread and bento lunch boxes is also strong, but we believe some items are not being produced sufficiently because of the disaster. Many stores are running short of food but we think this is because of one-off bulk buying.
- **Inputs** — The main marine products of the Sanriku region, which has been most severely affected of all, are wakame seaweed, nori seaweed, oysters, scallops, coho salmon, bonito, and saury. We expect supply/demand for these products to tighten. Iwate and Fukushima prefectures also produce large volumes of tobacco leaf, with the two together accounting for 15% of total production.
- **Share prices** — We think the food sector is likely to outperform, as it is defensive. At the stock level, we highlight Japan Tobacco, where we anticipate a leap in earnings in FY3/12.

Japan Tobacco (2914.T; ¥319,500; 1M)

See Appendix A-1 for Analyst Certification, Important Disclosures and non-US research analyst disclosures.

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Japan Tobacco

Valuation

Our ¥410,000 target price is derived using a DCF model based on earnings forecasts for FY3/11-FY3/14 to produce a theoretical share price of ¥414,000. We assume a 3% risk-free rate, a 5% equity-risk premium, a beta of 0.92, a 48% tax rate, and a zero terminal growth rate, producing a WACC of 5.8%.

Risks

We see the following as risks for our target price: 1) economic turmoil in Eastern Europe and Asia could impede growth in earnings from overseas cigarettes businesses; 2) the value of sterling, the ruble, and other key currencies could drop sharply against the dollar, impairing earnings from overseas cigarette sales; 3) class action lawsuits against tobacco companies could spread beyond the US; 4) tax increases could put downward pressure on domestic cigarette consumption; 5) JT's domestic market share could decline if foreign competitors lower their prices; and 6) investors could shift away from JT into cyclicals in response to economic recovery. If these factors manifest themselves differently than we have anticipated, the share price may fail to reach our target price.

On the other hand, a sharp increase in shipments of higher-priced products or the reduction of factory or personnel costs could result in upside risk. Should the effects of these risk factors differ from our assumptions, the shares may overshoot our target price.

We rate the shares Medium Risk (M) based on their three-year historical volatility, which places them in the sixth through ninth deciles in terms of share price risk compared with our coverage universe.

Appendix A-1

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Japan Tobacco (2914)

Ratings and Target Price History

Fundamental Research

Analyst: Nobuyoshi Miura

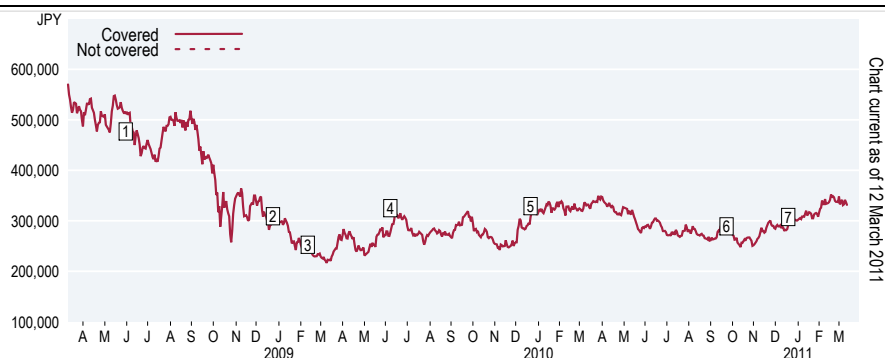


Chart current as of 12 March 2011

	Date	Rating	Target Price	Closing Price
1	30-May-08	1M	*710,000	512,000
2	24-Dec-08	1M	*540,000	298,000
3	11-Feb-09	1M	*380,000	240,000

* Indicates change

	Date	Rating	Target Price	Closing Price
4	8-Jun-09	1M	*460,000	277,000
5	22-Dec-09	1M	*480,000	308,000
6	23-Sep-10	1M	*390,000	282,200

	Date	Rating	Target Price	Closing Price
7	20-Dec-10	1M	*410,000	291,900

Rating/target price changes above reflect Eastern Standard Time

Japan Tobacco (2914)

Ratings and Target Price History

Best Ideas Research

Relative Call (3 Month)

Analyst: Nobuyoshi Miura

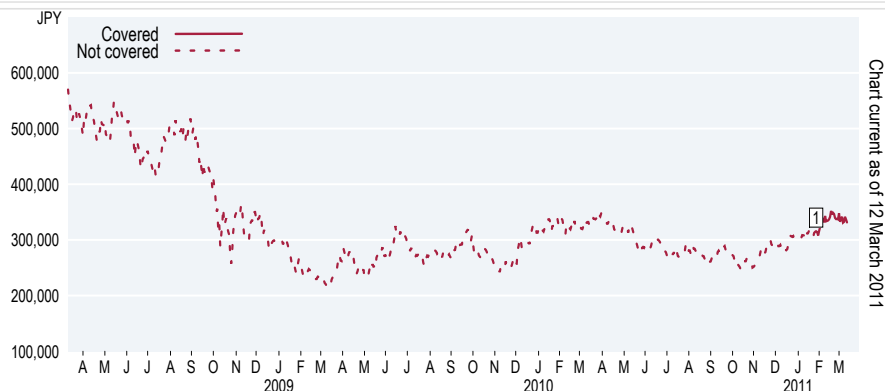


Chart current as of 12 March 2011

	Date	Rating	Target Price	Closing Price
1	27-Jan-11	*ADD MP	-	315,500

* Indicates change

Rating/target price changes above reflect Eastern Standard Time

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