

**Baillie Gifford™**

# The Baillie Gifford Japan Trust PLC

Philosophy and Process



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All investment strategies have the potential for profit and loss, you or your clients' capital may be at risk.

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# Company information

The Baillie Gifford Japan Trust PLC (the 'Company') is an investment trust listed on the London Stock Exchange and is not authorised or regulated by the Financial Conduct Authority. As with any investment, your clients' capital is at risk. A Key Information Document is available on request.

## Company history

The Baillie Gifford Japan Trust PLC aims to pursue long-term capital growth, principally through investment in medium to smaller sized Japanese companies which are believed to have above average prospects for growth, although it can invest in larger companies when considered appropriate.

## Company details

<b>SEDOL</b>	0048583
<b>ISIN</b>	GB0000485838
<b>AIC sector</b>	Japan
<b>Comparative index</b>	Topix (total return, in sterling terms)
<b>Launch date</b>	1 December 1981 Baillie Gifford were appointed in May 2018
<b>Year end</b>	August
<b>AGM</b>	November/December
<b>Results announced</b>	April and October (typically)
<b>Management details</b>	Baillie Gifford & Co Limited are appointed as investment managers and secretaries to the Company. The management contract can be terminated at six months' notice.
<b>Annual management fee</b>	Baillie Gifford & Co Limited's annual remuneration is calculated as 0.75% on the first £50 million net assets of the Company attributable to its shareholders, the next £200m is calculated at 0.65%, thereafter 0.55%. This is calculated and payable on a quarterly basis.

# Philosophy

We (Baillie Gifford) aim to create value for the Japan Trusts shareholders by finding and investing in Japan's most promising growth companies. We do so, by employing a flexible approach to growth investing, and using time to our advantage.

## **Time is our greatest asset**

Adopting a long-term approach allows us to frame investment opportunities differently to the rest of the market. We consider the unique attractions of individual companies, and we do so over five-year time periods and beyond. This long-term focus enables us to ignore the shorter-term vagaries of markets, cycles and share prices – to unearth exploitable and under appreciated opportunities that will ultimately deliver long-term out performance.

Long-term returns are determined, by seeking out, investing and continuing to back a relatively small number of exceptional businesses which grow to multiples of their starting size. This approach will inevitably lead to some mistakes along the way, but by focusing on opportunities for major upside potential and supporting them for significant periods of time – by running our winners – we are able to capture the inherent asymmetry of equity market returns.

## **Flexible approach to growth investing**

Our experience has highlighted that growth can come in various guises, from companies of all shapes and sizes. As such the portfolio is invariably built, from the bottom-up, with a diversified mix of companies from across all sectors and industries.

The commonality is that each investment must present a plausible pathway to doubling over a five-year period.

Be that through a gradual (compounding) approach, or via a more vertical (exponential) axis.

# Process

**We see Japan differently to others.**

## Idea generation

In pursuit of Japan's most attractive growth companies, we aim to generate original investment ideas by utilising a variety of sources. In addition to the more conventional inputs such as meetings with senior management and scrutinising company reports and accounts, we utilise private company analysis, bespoke and thematic reports from our independent researchers in Tokyo, investment trips (not limited to Japan), links with academia and industry experts.

## Research and debate

Companies that pique our interest are subject to our four-factor investment framework analysis, detailed below. This process is intended to focus attention on key fundamentals that we believe are most pertinent to delivering long-term growth. In order to make peer-to-peer comparison, we use a standard analytical framework.

## 01 Opportunity

### How big is the opportunity over five-to-ten years?

First, we look at the favourableness of the environment in which the company operates.

Is this a blue ocean opportunity in terms of the addressable market? Are there favourable industry dynamics, such as weak incumbency? Is the industry or market undergoing structural change? What will be the effects of environmental and technological shifts in the long term and which companies are likely to benefit?

## 02 Resilience +

### How durable/adaptable will the competitive advantage be in five years' time?

We then explore whether the company has identifiable qualities that we believe will allow it to thrive in the complex environment in which it operates.

One way of thinking about resilience is as dynamic and durable competitive advantage. How replicable is their edge, and is it sustainable? Another view is from the customers' perspective.

How much value is the company adding? If it did not exist how much would it be missed? We are less interested in their competitive moat right now than how deep it will be in five years' time and whether it will get deeper from there.

Another important aspect is the competence and alignment of management. Are leadership able to create new value organically? Is there a strong record of execution that gives us confidence in the future decisions? Can we see evidence of genuine ambition and vision? Are they aligned with wider stakeholders?

## 03 ESG

### **Taking in turn ESG factors, which do you believe are important and relevant to the investment case?**

We believe that ESG factors can have a material impact on a company's ability to generate long-term value. As such, we explicitly address these issues within the research framework.

Here we explore how the company intends to address ESG factors. The relevance of each is based upon the perceived materiality to the long-term sustainability of the company's business. As a result, key ESG considerations will vary depending on the industry sector, and core business activities of each company.

Baillie Gifford's Japanese Equities Team have a dedicated ESG analyst who works collaboratively with the investment managers to assess sustainability factors as part of the decision making process.

## 04 Upside

### **What is the likelihood of over two times upside?**

This dimension brings the investment case together, indicating to us whether a holding meets the high bar that we look for. We prefer to focus on the return we might realistically expect to make if we invest in the shares, aiming off conventional valuation metrics, which often tell us very little about the upside potential.

We assess the probability weighted average upside, considering both realistic base case scenarios as well as blue sky outcomes.

## Decision

The final decision will lie with Japan Trust's portfolio manager, Matthew Brett.

To ensure enthusiastic participation in all discussions, the Japanese Equities Team is rewarded collectively on all of their assets under management, but in order to facilitate effective decision making, each model has a lead manager. Matthew Brett is the lead manager for Japan Trust. The investment managers meet formally twice a month to review existing portfolio holdings and when appropriate to make the case for new purchases.

Portfolio holding size is not formulaic but reflects the strength of conviction in a particular investment idea and an assessment of how much views differ from the market. The team may add to or reduce position sizes when relative convictions change, though generally the tendency is to run winners.

## Sell discipline

We believe that the application of an effective sell discipline allied to a willingness to run successful investments has made a key contribution to the generation of added value.

We continually monitor the same primary factors surrounding opportunity, resilience+, ESG and upside. If one or more fundamentally changes that will be a trigger to re-assess the holding. We do not normally sell a stock on valuation grounds alone.

Whenever significant news or information emerges for each stock in the portfolio, we assess and discuss whether it is material to the forward-looking investment hypotheses and act accordingly by reducing or exiting the position.

We take a five-year view when investing in stocks. Consequently, portfolio turnover tends to be relatively low.

# Risk

The following are the main aspects of risk that we consider.

## Fundamental analysis

Our first line of defence is extensive due diligence. New buy ideas – and current holdings – are subject to thorough reviews by the Japanese Equities Team, with input from a plurality of Baillie Gifford research teams.

## Portfolio risk

We seek to maintain an appropriate level of diversification at the overall portfolio level by embracing pragmatic risk guidelines which are formally reviewed on a regular basis.

## Liquidity risk

We maintain a Product Group rule that we will not hold more than 10% of the portfolio in stocks where we hold more than eight days' trading volume at time of purchase. This ensures that the portfolio remains sufficiently liquid to enable positions to be exited or client cash flows to be managed with minimal impact.

## Independent oversight

We have an independent Investment Risk, Analytics and Research Department at Baillie Gifford which provide value-added analysis on portfolios, that goes far beyond the concept of an investment risk function being only adversarial risk police. While part of their toolkit includes an ability to disagree and constructively oppose based on various oversight mechanisms and risk guidelines, they also play a role as engagers of investment managers: providing perspectives on the portfolios (on capital allocation, behavioural biases and decision making analysis for example) with the aim of improving the investment process, to achieve better outcomes and minimise opportunity costs. This reflects our pragmatic approach to risk management.

**The Company's board considers the following as principal risks:**

## Financial risk

The Company's assets consist of listed securities and its principal financial risks are therefore market related and include market risk (comprising currency risk, interest rate risk and other price risk), liquidity risk and credit risk.

## Investment strategy risk

Pursuing an investment strategy to fulfil the Company's objective which the market perceives to be unattractive or inappropriate, or the ineffective implementation of an attractive or appropriate strategy, may lead to reduced returns for shareholders and, as a result, a decreased demand for the Company's shares. This may lead to the Company's shares trading at a widening discount to their net asset value.

## Discount risk

The premium/discount at which the Company's shares trade relative to its net asset value can change. The risk of a widening discount is that it may undermine investor confidence in the Company.

## Smaller company risk

The Company has investments in smaller companies which are generally considered higher risk as changes in their share prices may be greater and the shares may be harder to sell. Smaller companies may do less well in periods of unfavourable economic conditions.



### Climate and governance risk

Perceived problems on ESG matters in an investee company could lead to that company's shares being less attractive to investors, adversely affecting its share price, in addition to potential valuation issues arising from any direct impact of the failure to address the ESG weakness on the operations or management of the investee company (for example in the event of an industrial accident or spillage). Repeated failure by the managers to identify ESG weaknesses in investee companies could lead to the Company's own shares being less attractive to investors, adversely affecting its own share price. In addition, the valuation of investments could be impacted by climate change.

### Leverage risk

The Company may borrow money for investment purposes (sometimes known as 'gearing' or 'leverage'). If the investments fall in value, any borrowings will magnify the extent of this loss. If borrowing facilities are not renewed, the Company may have to sell investments to repay borrowings.

### Regulatory risk

Failure to comply with applicable legal and regulatory requirements such as the tax rules for investment companies, the FCA Listing Rules and the Companies Act could lead to suspension of the Company's Stock Exchange listing, financial penalties, a qualified Audit Report and the Company being subject to tax on capital gains. Changes to the regulatory environment could negatively impact the Company.

### Political and associated economic risk

Political change in areas in which the Company invests or may invest may have practical consequences for the Company.

### Custody and depository risk

Safe custody of the Company's assets may be compromised through control failures by the Depositary, including cyber security incidents.

### Cyber and security risk

A cyber attack on Baillie Gifford's network or that of a third party service provider could impact the confidentiality, integrity or availability of data and systems.

### Reliance on third party service provider risk

Failure of Baillie Gifford's systems or those of other third party service providers could lead to an inability to provide accurate reporting and monitoring or a misappropriation of assets.

**Further information can be found within the annual report.**

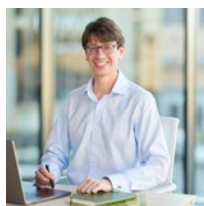
### Diversification guidelines

<b>Number of stocks</b>	40–70 holdings
<b>Holding size</b>	<5% at time of purchase. Any holding that as a result of strong performance exceeds 5% is subject to further scrutiny.
<b>Relative stock/sector weights</b>	Although sector concentrations and the thematic characteristics of the portfolio are carefully monitored, there are no maximum limits to deviation from benchmark stock or sector weights except as imposed by banking covenants on borrowings.

# People and responsibilities

## Investment team

Management of the investment portfolio is led by Matthew Brett. All members of the Japanese Equities Team have fundamental company research as their primary responsibility, regardless of whether they are investment managers or investment analysts. This reflects Baillie Gifford's view that stock selection based on fundamental research is the main opportunity to add value. Their sector research responsibilities encompass the full range of market capitalisation, from the largest companies in a sector down to interesting small companies. Thus every team member contributes ideas to the portfolio.



**Matthew Brett**  
Manager

Matthew is an investment manager in the Japanese Equities Team. He is co-manager of the Japan All Cap Strategy, the Japanese Income Growth Strategy and the Baillie Gifford Japan Trust. He joined Baillie Gifford in 2003 and became a partner of the firm in 2018. Matthew graduated BA (Hons) in Natural Sciences (Psychology) from the University of Cambridge in 2000 and holds a PhD in Psychology from the University of Bristol.

## Board liaison

Naomi is the client relationship director for several Investment Trust Boards. She joined Baillie Gifford in 2021. Previously, she qualified as a solicitor and worked as a corporate lawyer in both London and Edinburgh. Naomi graduated LLB from the University of Aberdeen in 2012.



**Naomi Cherry**  
Client Relationship  
Director

# Board

**The board has overall responsibility for the company's affairs. A number of matters are reserved for its approval including strategy, investment policy, currency hedging, gearing, treasury matters, dividend and corporate governance policy.**

The board currently comprises of five directors, all of whom are non-executive. The executive responsibilities for investment management have been delegated to the company's managers and secretaries, Baillie Gifford & Co Limited, and in the context of a board comprised entirely of Non-Executive Directors, there is no Chief Executive Officer. The directors believe that the board has a balance of skills and experience that enables it to provide effective leadership and proper governance of the Company.

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**David Kidd**  
Chair

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David Kidd was appointed a Director in 2015 and became Chairman in June 2022. He has over 40 years investment experience in the City, in the roles of chief investment officer and independent professional trustee. He is chair of Trustees, ABRSM Pension Scheme and chairman of Mid Wynd International Investment Trust PLC. He was previously a director of Shires Income PLC, Martin Currie International Portfolio Trust PLC, the Salvation Army International Trustee Company, and The Golden Charter Trust.

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**Sharon Brown**  
Director

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Sharon Brown was appointed a Director in 2019. She is Chair of the Audit Committee and a qualified accountant. She is currently a director and audit committee chair of European Opportunities Trust plc and Celtic plc. She was previously finance director of Dobbies Garden Centres plc and a director of McColl's Retail Group plc, Fidelity Special Values plc, CT UK Capital and Income Investment Trust PLC and a number of unlisted companies in the retail sector.

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**Joanna Pitman**  
Director

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Joanna Pitman was appointed a Director in 2018 and appointed Senior Independent Director in June 2022. She is Chair of the Remuneration Committee. She read Japanese Studies at Cambridge University and speaks Japanese. She was Tokyo Bureau Chief of The Times from 1989 to 1994 and for the past eleven years she has worked as a corporate research analyst focused on Japan. She is vice chair of the Great Britain Sasakawa Foundation and UK Chair of SAIDIA.

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**Sam Davis**  
Director

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Sam Davis was appointed a Director in 2021. He is Chair of the Management Engagement Committee. Sam studied Japanese at Oxford before joining Morgan Grenfell & Co. Ltd, working initially in corporate finance in both London and Tokyo. He moved to Morgan Grenfell Asset Management in 1996 to work with a Tokyo-based team. In 2000 he joined Putnam Investments first in Boston, MA and then in London where, over his 19-year tenure, he managed Asian, European and broad international equity portfolios. As Putnam's co-head of equities he oversaw a global investment team and was CEO of Putnam Investments Ltd, the group's UK regulated entity. Sam is a non-executive director of Allianz Technology Trust PLC and Schroder Oriental Income Fund Ltd.

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**Patrica Lewis**  
Director

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Patricia Lewis was appointed a Director in 2023. She is a financial services executive with 25 years' experience advising clients globally in investment and capital management. Most recently, she held the position of Managing Director and Head of EMEA Loans and Special Situations Sales at Bank of America Merrill Lynch. She is also a director and Audit and Risk Committee Chair of Snowball Impact Management Ltd.

# About Baillie Gifford

**Baillie Gifford & Co is one of the leading privately owned investment management firms in the UK. Structured as a partnership, investment management is our sole business.**

Baillie Gifford & Co is wholly owned by partners, all of whom work within the firm. We believe that the personal involvement in the business by the owners is crucial to maintaining the motivation and high standards essential to a modern investment house and maintaining a firm client focus.

A hallmark of the firm is the stability of our organisation and our commitment to continuing as an independent, private business based in Edinburgh. We are particularly proud of our low turnover of staff, both investment and administrative.

Baillie Gifford has a strong service culture. We make every effort to ensure that the service to investment trust boards and shareholders is of the highest possible standard.

Accounting and company secretarial services are provided by our in-house Investment Trust Department. This team currently provides these services to the other investment trusts managed by Baillie Gifford.

## Investment Trusts and Investment Companies managed by Baillie Gifford

	Sector
Scottish Mortgage Investment Trust PLC	Global
The Monks Investment Trust PLC	Global
The Scottish American Investment Company P.L.C.	Global Equity Income
Edinburgh Worldwide Investment Trust plc	Global Smaller Companies
The Baillie Gifford Japan Trust PLC	Japan
Baillie Gifford Shin Nippon PLC	Japanese Smaller Companies
Pacific Horizon Investment Trust PLC	Asia Pacific
Baillie Gifford US Growth Trust plc	North America
Baillie Gifford UK Growth Trust plc	UK All Companies
Baillie Gifford European Growth Trust plc	Europe
Baillie Gifford China Growth Trust plc	China
The Schiehallion Fund	Growth Capital

## Differentiation

We believe a number of features differentiate Baillie Gifford's investment philosophy and process:

### Fundamental style

We are fundamental investors. We undertake our own research with considerable emphasis on analysing companies' financial statements and assessing management.

### Long-term investment horizon

Our aim is to select good quality stocks which will outperform over the long term. When assessing a stock, we look at a company's prospects over the next five years as opposed to the next five months.

### Active portfolios

Having identified good quality stocks, we look to hold them in sufficient size to have a meaningful, positive impact on performance. We back our judgement.

### Team-based decision making

We operate a genuine team approach. Portfolios reflect the views and contributions of each investment team.

### Stability of investment staff

Our partnership structure encourages a high degree of stability within the investment teams. All staff have the opportunity to become a Partner and this provides a major incentive. We believe this ability to own part of a successful, growing business is significantly more than just a financial incentive. In addition, even at non-partner level, profits are shared across a wide base of the employees.

### Continuity and repeatability

Our approach to investment has been established over many years. The consistent application of this successful philosophy and process explains our historic performance record and underpins our confidence that performance can be maintained into the future.

# Contact



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Head of Intermediary Sales

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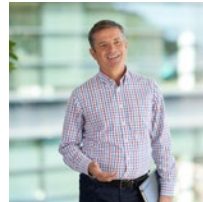
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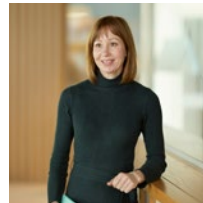
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**David Rolland**

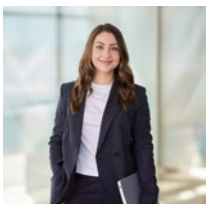
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**Megan Rooney**

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**Harry Driscoll**

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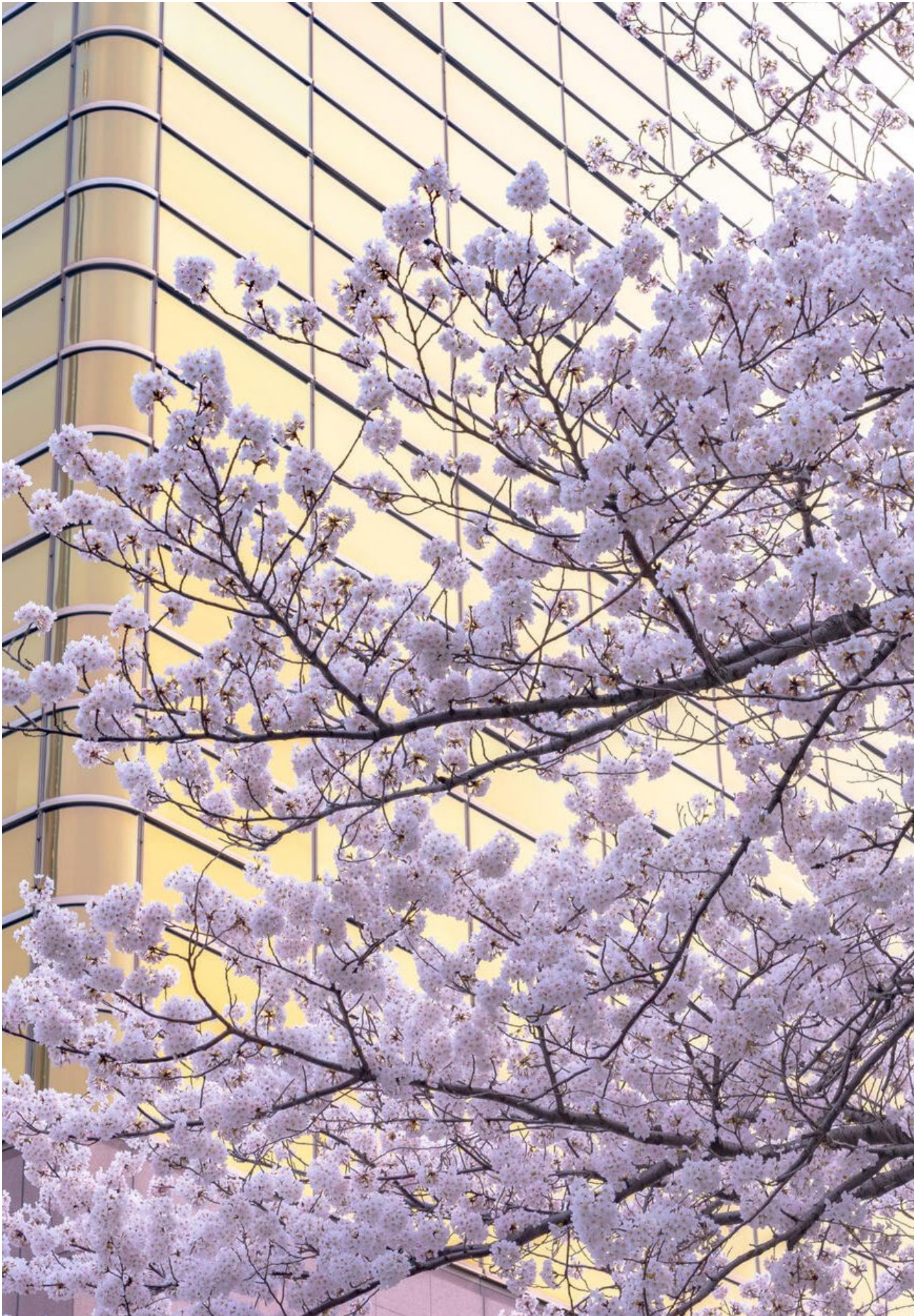
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**Financial Intermediaries**

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