

Baillie Gifford Japanese Income Growth Fund

31 December 2023

About Baillie Gifford

Philosophy	Long-term investment horizon A growth bias Bottom-up portfolio construction High active share
Partnership	100% owned by 57 partners with average 20 years' service Ownership aligns our interests with those of our clients Enables us to take a thoughtful, long-term view in all that we do Stability, quality and consistency

Investment Proposition

The Fund applies the same well-tested growth investing philosophy and process that we use across all of our Japanese investments. For the Japanese Income Growth Fund, we combine this approach with a focus on companies that are improving returns on capital and balance sheet efficiency, to generate a portfolio of growth companies with a yield orientation. In this way we hope to generate strong long-term total returns as well as provide those investors that require it with a higher than market yield along the way. The Fund balances current income generation with growing that income over time, and invests across the market cap spectrum.

Fund Facts

Fund Launch Date	04 July 2016
Fund Size	£519.4m
IA Sector	Japan
Active Share	85%*
Current Annual Turnover	6%
Current number of stocks	53
Stocks (guideline range)	45-65

*Relative to TOPIX (in sterling). Source: Baillie Gifford & Co, Japan Exchange Group.

Fund Manager

Name	Years' Experience
Matt Brett*	20
Karen See	11

*Partner

Fund Objective

To outperform (after deduction of costs) the TOPIX, as stated in sterling, by at least 1% per annum over rolling five-year periods through a combination of income and capital growth whilst maintaining a portfolio yield higher than the TOPIX.

The manager believes this is an appropriate target given the investment policy of the Fund and the approach taken by the manager when investing. In addition, the manager believes an appropriate performance comparison for this Fund is the Investment Association Japan Sector.

There is no guarantee that this objective will be achieved over any time period and actual investment returns may differ from this objective, particularly over shorter time periods.

Periodic Performance

	3 Months	1 Year	3 Years (p.a.)	5 Years (p.a.)
Class B-Inc (%)	4.3	1.2	-1.7	4.2
Index (%)*	3.4	13.3	3.5	6.8
Target (%)**	3.7	14.4	4.5	7.9
Sector Average (%)***	3.7	11.6	1.4	6.8

Source: FE, Revolution, Japan Exchange Group. Total return net of charges, in sterling.

Share class returns calculated using 10am prices, while the Index is calculated close-to-close.

Baillie Gifford operates a single swinging price for the Fund and, therefore, may apply a dilution adjustment to the price to protect long-term investors from the costs associated with buying and selling underlying investments that result from other investors joining or leaving the Fund. This adjustment will affect relative performance, either positively or negatively.

*TOPIX (in sterling).

**TOPIX (in sterling) plus at least 1% per annum over rolling five-year periods (through a combination of income and capital growth).

***IA Japan Sector.

Discrete Performance

	31/12/18- 31/12/19	31/12/19- 31/12/20	31/12/20- 31/12/21	31/12/21- 31/12/22	31/12/22- 31/12/23
Class B-Inc (%)	15.9	11.6	0.8	-6.9	1.2
Index (%)*	14.6	9.5	2.0	-4.1	13.3
Target (%)**	15.8	10.6	3.0	-3.2	14.4
Sector Average (%)***	17.2	13.8	1.8	-8.1	11.6

Source: FE, Revolution, Japan Exchange Group. Total return net of charges, in sterling.

Share class returns calculated using 10am prices, while the Index is calculated close-to-close.

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***IA Japan Sector.

Market environment

Waning inflation and buyouts appeared to be the noteworthy issues within the Japanese market during the fourth quarter; both factors point to an increasingly appealing opportunity for the year ahead.

The Bank of Japan continued slowly easing its way out of an ultra-loose monetary policy by removing its hard cap on bond yields. However, it refrained from raising rates, leaving it as the only sizeable central bank with negative interest rates.

Japan's dovish and cautious approach to monetary policy reflects concerns over the transitional nature of inflation. Many believe it is not sticky nor substantial enough to combat the deflation that has plagued the nation for decades. Signs that it is beginning to subside (core inflation slowed sharply in November) and the Fed's recent pivot support such an argument.

The Yen subsequently strengthened into year-end, and banks lost ground as investors took profits and shifted towards growthier areas of the market that have hitherto been impacted by the 'higher for longer' sentiment that prevailed for most of 2023.

We continue to examine the fundamentals of our holdings and the strength of our investment theses. In aggregate, we remain confident of the longer-term structural trends that underpin the Fund.

Performance

Among the top contributors to performance were Benefit One, GMO Internet and Nintendo.

Benefit One is a fringe benefits platform for employees and a recent purchase for the fund. It has the largest market share, with over 10 million employees on its platform. It was attractively valued for a very cash-generative business with an excellent competitive position. Since taking a holding, there have been two tender offers to acquire stakes in the company. The higher bid aims to delist Benefit One eventually, and it's unclear whether there will be further counter-bids. With the share price now trading above the higher bid price and the facts of the investment case materially changed, we have decided to sell out, locking in a respectable profit since initiating a holding a short time ago.

GMO Internet is one of Japan's leading internet companies, with a particular emphasis on Internet infrastructure. It recently reported solid results, with increased net sales and net profit over the previous year. The internet infrastructure segment is growing well due to being the dominant number one provider of domain name registrations and hosting services. We believe GMO Internet provides exposure to various businesses that help with the digitisation drive in Japan

at an attractive price, well below the equity value of its holdings.

Nintendo's share price rose sharply following solid results and the announcement that it will be involved in making the "Legend of Zelda" movie. This move signals a positive step for Nintendo as it continues to take advantage of its substantial intellectual property by utilising a popular character from one of its hit games. Additionally, results saw sales increase by 21% year-over-year, which is the most significant increase since the launch of the Nintendo Switch. This has been driven by sales from video game platform businesses and a rise in mobile and IP-related income, such as "The Super Mario Bros" movie, which has become the highest-grossing film based on a video game.

Among the bottom detractors from performance were Shiseido, Pola Orbis and Denso.

Shiseido, the beauty and cosmetics company, continues to struggle due to weaker demand from Chinese consumers post-Covid. Despite Japan seeing an influx of foreign visitors, now above pre-COVID levels, the recovery in the number of visitors from mainland China has been much slower. It is still 65% below October 2019 figures. This was reflected in Shiseido's recent results, which reported a decline in sales. Concerns over the Fukushima water release also decreased consumer demand for Japanese products. We view these challenges as short-term and believe Shiseido is well-positioned to benefit from structural trends, such as Asia's rising middle-class wealth.

Pola Orbis, the beauty and cosmetics company, has faced the same struggles as Shiseido regarding weakened demand from China. Its share price was down despite releasing solid results, with operating profit up 55% for the first nine months of 2023 (albeit from a low Covid-induced base). This was primarily thanks to strong sales of its Orbis brand and a healthy recovery in department store sales, which were markedly up, reflecting the bounce in tourism spending.

Denso is an automotive component manufacturer that develops technologies to enable the electrification of vehicles. Its share price declined following the news that Toyota Motor and two affiliates plan to reduce their stake in the company. This move by such a large, influential company signifies a positive step to undo cross-shareholdings and improve corporate governance, potentially encouraging other companies to follow suit. Overall, Denso continues to perform well, with solid revenue growth due to vehicle sales in Japan and North America and the expansion of products for electrification.

Notable transactions

As mentioned above, Benefit One was bought and sold for the Fund during the quarter. The sale was driven by material changes to the investment case as a result of two tender offers to acquire stakes in the company. During our short holding, the share price was close to doubling.

Stock Level Attribution

Top and Bottom Ten Contributors to Relative Performance

Quarter to 31 December 2023

Stock Name	Contribution (%)
Benefit One	0.4
GMO Internet	0.3
Seria	0.3
Infomart	0.3
Nintendo	0.2
Toyota Motor	0.2
DMG Mori	0.2
Takeda Pharmaceutical	0.2
Honda Motor	0.2
OSG Corp	0.2
Shiseido	-0.4
Shin-etsu Chemical	-0.4
Pola Orbis	-0.4
Recruit Holdings	-0.3
Tokyo Electron	-0.3
Denso	-0.2
Sumitomo Mitsui Trust	-0.2
Sony	-0.2
Lasertec Corp.	-0.2
Milbon	-0.2

One Year to 31 December 2023

Stock Name	Contribution (%)
DMG Mori	0.7
Benefit One	0.4
Daiichi Sankyo	0.4
Bank Of Kyoto	0.4
Japan Exchange Group	0.3
Takeda Pharmaceutical	0.3
Itochu Corp.	0.2
Denso	0.2
Olympus	0.2
Astellas Pharma	0.2
Shiseido	-1.4
Pola Orbis	-1.2
Park24	-0.8
Calbee	-0.7
Pigeon	-0.7
Sumitomo Metal Mining	-0.6
mixi	-0.6
Fanuc	-0.6
GMO Internet	-0.6
Tokyo Electron	-0.6

Source: Revolution, Japan Exchange Group. Baillie Gifford Japanese Income Growth Fund relative to TOPIX (in sterling).

Some stocks may only have been held for part of the period.

All attribution figures are calculated gross of fees, relative to the Index from stock level up, based on closing prices.

As Attribution is shown relative to the benchmark, not all stocks shown are held in the portfolio. See the List of Holdings section of this report for the stocks held.

Transactions from 01 October 2023 to 31 December 2023.

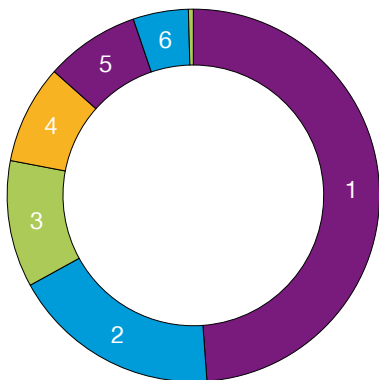
New Purchases

Stock Name	Transaction Rationale
Benefit One	Benefit One is a fringe benefits platform for employees. It is the market leader with almost half of the market, having done an opportunistic acquisition of the number three player during Covid. Market growth should pick up going forward as companies work hard to retain workers by improving their benefits package. This is a fundamentally cash-generative business with good return characteristics and a healthy payout ratio. Shares have been de-rated over the last year due to the tapering off of its vaccine-related business. It's now trading at a multiple that looks attractive with a 3.5% yield. We decided to take a holding.

Complete Sales

Stock Name	Transaction Rationale
Benefit One	Benefit One is a fringe benefits platform for employees. It has the largest market share with over 10 millions employees on their platform. It was attractively valued for what is a very cash generative business with excellent competitive position. Since taking a holding, there had been two tender offers to acquire stakes in the company. The higher bid aims to eventually delist Benefit One and it's unclear whether there will be further counter-bids. With the share price now trading above the higher bid price and the facts of the investment case materially changed, we have decided to sell out, locking in a decent profit since initiating a holding a short time ago.

Sector Exposure



		%
1	Manufacturing	48.8
2	Finance & Insurance	18.2
3	Transport And Communications	11.0
4	Commerce	8.6
5	Services	8.2
6	Real Estate	4.8
7	Cash	0.4

As well as cash in the bank, the cash balance includes unsettled cash flows arising from both shareholder flows and outstanding trades. Therefore, a negative balance may arise from timing differences between shareholder flows and security trading, and does not necessarily represent a bank overdraft.

Top Ten Holdings

Stock Name	Description of Business	% of Portfolio
SBI Holdings	Online financial services	4.1
GMO Internet	Internet conglomerate	3.9
Sumitomo Mitsui Trust	Japanese trust bank and investment manager	3.7
FANUC	Robotics manufacturer	3.4
DMG Mori	Machine tool manufacturer	3.3
Tokio Marine Holdings Inc	Offers property and life insurance	3.3
MS&AD Insurance	Japanese insurer	3.2
SoftBank Group	Telecom operator and technology investor	3.2
Nintendo	Gaming consoles & software	3.0
Bridgestone	Tyre manufacturer	3.0
Total		34.1

Voting Activity

Votes Cast in Favour		Votes Cast Against		Votes Abstained/Withheld	
Companies	2	Companies	None	Companies	None
Resolutions	28	Resolutions	None	Resolutions	None

Long-term investing and sustainability are inextricably linked

The fund continues to ensure our Environmental, Social and Governance (ESG) research, integration and stewardship activities are focused on issues material to the investment case and companies' long-term growth prospects

Our engagements this quarter have covered a wide range of topics, including supply chain transparency, board effectiveness, and remuneration

Company Engagement

Engagement Type	Company
Environmental	DENSO Corporation, PARK24 Co., Ltd., Seria Co., Ltd., Unicharm Corporation
Social	Olympus Corporation, PARK24 Co., Ltd.
Governance	CyberAgent, Inc., Kakaku.com, Inc., MISUMI Group Inc., Nidec Corporation, Nintendo Co., Ltd., Olympus Corporation, PARK24 Co., Ltd., Pola Orbis Holdings Inc., Rakuten Group, Inc., Seria Co., Ltd., Sumitomo Mitsui Trust Holdings, Inc.
Strategy	DENSO Corporation, Nidec Corporation

For further details on company engagement please contact us. You can also find further information on how we integrate environmental, social and governance (ESG) matters into our investment approach, [here](#).

Asset Name	Fund %	Asset Name	Fund %
SBI Holdings	4.1	Broadleaf	0.8
GMO Internet	3.9	Nidec Corporation	0.7
Sumitomo Mitsui Trust	3.7	Sawai Pharmaceutical	0.6
FANUC	3.4	USS	0.3
DMG Mori	3.3	Cash	0.4
Tokio Marine Holdings Inc	3.3	Total	100.0
MS&AD Insurance	3.2		
SoftBank Group	3.2		
Nintendo	3.0		
Bridgestone	3.0		
Kubota	2.8		
Pola Orbis	2.8		
Calbee	2.6		
Itochu Corp.	2.4		
Kyoto Financial Group, Inc.	2.2		
Unicharm	2.2		
mixi	2.1		
Murata Manufacturing	2.1		
Kao	2.1		
DENSO	2.0		
Shiseido	2.0		
Sumitomo Metal Mining	2.0		
Wacom	1.9		
Seria	1.9		
Park24	1.9		
Systemex	1.8		
Industrial & Infrastructure Fund	1.7		
Japan Exchange Group	1.6		
Infomart	1.6		
Pigeon	1.5		
MonotaRO	1.5		
Kyocera	1.5		
Olympus	1.5		
Sato Holdings	1.4		
Softbank Corp	1.4		
OSG	1.3		
Rakuten	1.3		
Tokyo Tatemono	1.2		
SMC	1.2		
Milbon	1.2		
Kakaku.com	1.1		
Sugi Holdings	1.1		
Nippon Electric Glass	0.9		
Mitsui	0.9		
CyberAgent	0.9		
Nihon M&A	0.9		
LY Corporation	0.9		
COLOPL	0.8		
Misumi	0.8		

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Share Class	Share Class Inception Date	ISIN	SEDOL	Annual Management Fee (%)	Ongoing Charge Figure (%)
Class B-Acc	04 July 2016	GB00BYZJQH88	BYZJQH8	0.60	0.62
Class B-Inc	04 July 2016	GB00BYZJQG71	BYZJQG7	0.60	0.62

The table displays the primary shares classes. Other share classes may be available for those investors who have a separate arrangement. Charges will reduce the value of your investment. Please refer to the Prospectus and Key Investor Information Document for further details.

TOPIX

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Additional Geographical Location Information

Israel: This Report, as well as investment in the Fund described herein, is directed at and intended for Investors that fall within at least one category in each of: (1) the First Schedule of the Israeli Securities Law, 1968 (“Sophisticated Investors”); and (2) the First Schedule of the Investment Advice Law (“Qualified Clients”).

The Fund’s share price can be volatile due to movements in the prices of the underlying holdings and the basis on which the Fund is priced.

As with any investment, the clients’ capital is at risk. Past performance is not a guide to future returns.

Throughout the report all figures are rounded, so any totals may not sum. Not all stocks mentioned may be held by the portfolio.

All information as at 31 December 2023 and source is Baillie Gifford & Co unless otherwise stated.

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