FUND PROFILE

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BAILLIE GIFFORD

JAPANESE INCOME GROWTH FUND

May 2021

RSMR RATED FUND

OUR RESEARCH. YOUR SUCCESS

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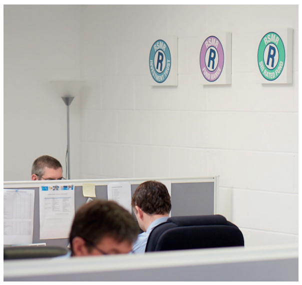

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BAILLIE GIFFORD JAPANESE INCOME GROWTH FUND

OUR FUND PROFILES provide an in-depth review of our leading rated funds and are designed to give advisers, paraplanners and analysts an 'under the bonnet' view of the fund. In providing more detailed commentary than a standard fund factsheet we believe our fund profiles set the standard for the next generation of research notes, aiding in fund selection and in meeting the ongoing suitability requirements expected by the FCA, and helping ensure firms deliver good client outcomes.

All of our rated funds are subject to rigorous and ongoing scrutiny on both a qualitative and quantitative basis. Our fund methodology is available for download from the RSMR Hub – www.rsmr.co.uk

The **Baillie Gifford Japanese Income Growth Fund** has been one of our rated funds since March 2017. It is a long-only Japanese equity fund which launched in July 2016. Across the firm, the philosophy is focused on bottom-up growth investing for the long term. Individual teams are able to work within their own definitions of growth and the Japan team include cyclical growth businesses and special situations within their portfolios. This fund has a yield orientation at the portfolio level with the managers aiming to deliver growing distributions above the Topix Total Returns Index consistently. The fund typically invests in between 45 and 65 companies across the market-cap spectrum.

The investment process is implemented by the Japanese Equity Team with fund managers Matthew Brett and Karen See having responsibility for investment decisions. The team have an excellent track record of managing strongly performing mandates in core Japan, smaller companies and investment trusts. They have continued this outperformance through this mandate while meeting their investment objectives to date.

The fund is suitable as a core holding in an investor's portfolio, offering something differentiated and backed by a strong investment philosophy that has been proven by the success of the teams varying mandates.

Graham O'Neill, Senior Investment Consultant, RSMR

Graham began his career in the investment industry over thirty years ago. After graduating from the University of Kent with a Degree in Economic Analysis, History and Policy, he joined London & Manchester, later joining Phillips Drew, then GRE as a UK based fund manager. He then moved to Abbey Life Ireland, where he held the position of CIO running their Managed and large Equity funds. Graham joined RSMR in 2010.

IA JAPAN SECTOR

The Baillie Gifford Japanese Income Growth Fund sits in the IA Japan sector. Funds in this sector invest at least 80% of their assets in Japanese equities.

The IA Japan sector contains over 70 funds available for investors and financial advisers to choose from, covering a large variety of investment strategies and styles, including active, passive and enhanced index funds. A number of funds adopt style or market-cap based strategies including value and growth-biased themes, market-cap focused or multi-cap strategies. Funds that invest in a specialist theme must still meet the required geographic dispersion based on the relevant index.

The variations between the funds makes it difficult for an investor to compare them as different strategies will clearly perform differently depending on market conditions. It is important to recognise this when looking at both absolute and relative performance numbers for funds in the IA Japan sector, and this is particularly relevant for the Baillie Gifford Japanese Income Growth fund, which has a distinct style of investing.

Japan is now moving to a post-Abe era and new Premier Yoshihide Suga must call a general election by October 22nd 2021. In recent by-elections opposition parties performed strongly with defeats for the ruling Liberal Democrat Party in a number of prefectures, with the slow vaccination campaign against Covid-19 (where only just over 1% of the population had received the first dose by the end of April) not helping matters. This slow rollout has resulted in Japan having to put in place a short spell of further restrictions in its biggest cities by declaring a state of emergency in Tokyo, Osaka, Hyogo, and Kyoto for a two-week period, which includes the Golden Week, one of Japan's biggest public holidays during which time many people would normally travel. Japan is also desperately trying to stop the spread of new variants ahead of the re-scheduled Tokyo 2021 Olympics in the summer.

Japan's attempts to combat deflation have been hampered by the coronavirus pandemic, although at the micro level many companies continue to enact reform in terms of a higher level of independent directors and a greater emphasis on efficiency including better balance sheet management. The latter has resulted in an increasing number of both share buybacks and dividend payouts over the past decade. Within Japan, the corporate emphasis on responsibility to all stakeholders has resulted in many companies already having a higher emphasis on the S within ESG than in many other developed economies, especially the United States. Geopolitical concerns could also influence the Japanese market over the next few years with the US pushing Japan to take a harder stance against China, especially over Taiwan.

Whilst the overall economy in Japan remained sluggish, Japanese business sentiment has rebounded in recent months with particularly optimistic sentiment in Japan's industrial companies who are well placed to benefit from robust growth in China, automation, and the production of components and machine tools related to the new economy. Within Japan, whilst ageing demographics are a negative for domestic consumption and many years of low interest rates have hit the legacy banks hard, there are many niche parts of the stock market able to deliver strong returns to investors. Japan remains a market where active stock picking is likely to deliver better returns than passive investment options and Baillie Gifford have an outstanding record across a whole suite of Japanese products over the past decade.

BAILLIE GIFFORD

Baillie Gifford & Co is an investment management firm regulated by the UK's Financial Conduct Authority (FCA). The company has funds under management and advice of over £325.8bn as at 31st December 2020, and is headquartered in Edinburgh. It was established in 1908, making it one of the UK's largest independent active investment management firms, employing over 1,300 people across the globe. Baillie Gifford is wholly owned by its 46 partners – all of whom work for the firm full time.

In equities, the investment philosophy focuses on growth over the long term with a view that sustained increases in company profits lead to higher share prices over time. There is a preference for small teams which are more dynamic in nature and with clear accountability. There is also a collaborative culture across the firm where investment ideas are discussed and debated across the investment teams.

BAILLIE GIFFORD JAPANESE INCOME GROWTH FUND

Managers	Matthew Brett; Karen See
Structure	OEIC
IA Sector	Japan
Launched	4th July 2016
Fund Size	£921.1m (31st March 2021)

Fund Management Team

Baillie Gifford have a well-resourced Japanese Equity Team headed by Donald Farquharson who took over as team-lead in April 2018. The role was previously held by Sarah Whitley, who retired from the company as the longest standing partner within Baillie Gifford. Donald Farquharson, who joined Baillie Gifford in 2008, has over thirty years' experience working in Japanese equities. The Japanese Equities Team comprises seven investment managers and two analysts, all of whom have fundamental company research as their primary role. In addition, there are two Tokyo based independent researchers who conduct on the ground research into companies or themes. The permanent Edinburgh based team are responsible for the management of a number of funds and investment trusts including:

- Baillie Gifford Japanese – Managed by Matthew Brett
- Baillie Gifford Japanese Income Growth – Managed by Matthew Brett and Karen See
- Baillie Gifford Japanese Smaller Companies – Managed by Praveen Kumar
- Baillie Gifford Japan Trust PLC – Managed by Matthew Brett and Praveen Kumar
- Baillie Gifford Shin Nippon PLC – Managed by Praveen Kumar

Matthew Brett and Karen See are the co-managers for this fund and are responsible for all investment decisions.

Matthew Brett, Co-Manager

Matthew graduated with a BA (Hons) in Natural Sciences (Psychology) from the University of Cambridge in 2000 and holds a PhD in Psychology from Bristol University. He joined Baillie Gifford in 2003 and is an Investment Manager in the Japanese Equity Team. He is the manager of the Japanese All Cap strategy and co-manager of the Japanese Income Growth Strategy. Matthew became a Partner in 2018 and is a CFA charterholder.

Karen See, Co-Manager

Karen graduated with a BSc (Hons) in Economics with Japanese from Birmingham in 2011. Karen joined Baillie Gifford in 2012 and is an Investment Manager in the Japanese Equity Team. She is a CFA charterholder.

Team Remuneration

The partners are the sole owners of the firm and share directly in its profits. In this respect, the compensation and incentive package of senior investment managers who are partners is directly related to both asset growth and performance.

Non-partner investment managers receive a basic salary and performance related bonus which is linked to the profits of the firm. Performance for investment managers is measured in two ways – half of the bonus is based on individual performance which is determined by the individual's line manager at the annual appraisal where staff are assessed against key competences and pre-agreed objectives. The remaining 50% is determined by five-year investment performance of the individual's team, which ties in with the overarching long-term investment philosophy of the company.

Fund Objectives & Targets

The objective of the fund is to produce a sustainable income and capital growth over the long-term. The aim is to identify Japanese companies with attractive industry backgrounds, strong competitive positions, high-quality earnings, and favourable attitudes towards shareholders to generate above average total returns. The team use a bottom-up investment approach to construct a concentrated portfolio (45 to 65 holdings) of growth companies with a yield orientation. Yield is assessed at the overall portfolio level with the managers targeting a higher yield than the benchmark.

The strategy aims to outperform the Topix Total Return Index gross of fees by at least 1.5% per annum over rolling 5-year periods through a combination of capital appreciation and yield. The managers are long term investors resulting in a low turnover (typically 15% to 20%) and they aim to be differentiated from the index with a high active share (over 80%). The maximum stock position size is 10% although it is typically kept below 5%.

Investment Philosophy

The investment philosophy of the fund is consistent with the firm-wide approach to equity investing. This is focused on three core beliefs:

1. Growth Investing

The team believe that those companies that can sustainably grow their business, while significantly increasing their earnings and cash flow will be best rewarded. They seek quality companies managed by trustworthy people who act in the long-term interests of shareholders. In addition, this fund focuses on companies that are improving returns on capital and balance sheet efficiency, to generate a portfolio of growth companies with a yield orientation.

2. Long-Term Investment Horizon

The team are not influenced by the economic cycle and pay little attention to short-term performance or market noise. They believe that most investors overreact to short-term events which can leave companies significantly undervalued. The managers aim to exploit these inefficiencies by focusing on the long-term prospects of a company, typically three to five years and beyond.

3. High Active Share

The team believe that the fund must have a different composition to the index in order to beat it. They back their judgement, running concentrated portfolios where higher weightings reflect conviction in the long-term prospects of a company. They aim to add value through the use of proprietary, fundamental research, which prioritises the selection of individually attractive companies, rather than taking top-down industry bets.

Investment Process

The investment process primarily focuses on fundamental company research which is the main activity for each member in the team. The benchmark index comprises over 2,000 companies and the managers seek to build a portfolio of between 45 and 65 companies. The team do not try to cover every possible opportunity in the Japanese market: they seek to generate original investment ideas from a variety of sources including company meetings, investment trips, external research, and industry trade fairs.

Over time, they have narrowed the investment universe to a ‘Followed List’ of around 150 companies, which is the main focus of their research. These are companies which, on initial assessment, are deemed to potentially satisfy more than one of four factors considered important: positive industry background, evidence of a durable competitive advantage, strong financial characteristics, and a management attitude that is aligned with the interests of shareholders.

The overwhelming majority of the research carried out at Baillie Gifford is conducted internally. A research library is utilised whereby investment analysis on all companies (all meeting notes, reviews, results analysis and update reports) is available on a company-wide basis, categorised by author, sector, company and country. The team conduct around 500 Japanese company meetings each year (including multiple meetings with some companies) both in Japan and in Edinburgh. Typically, a member of the team visits Japan twice a year. These meetings are primarily focused on companies held in the portfolios or those on the ‘Followed List’, although competitors and subsidiaries are met with from time to time. In addition, the team use the services of an independent researcher based in Tokyo to investigate certain issues, regulatory and government developments for example, and to attend trade shows. The team also use external sources of information including brokerage contacts, company reports, and industry inputs along with information services such as Bloomberg and Reuters.

The team formally meet on a weekly basis to discuss research reports written by team members where each attendee is asked to provide an alphanumeric rating of the business based on its growth opportunity, resilience and valuation. These ratings are recorded after a stock has been debated, but before a consensus view is formed. From a valuation perspective, the team are seeking companies with the potential to at least double in price on a five-year view.

In order to make peer-to-peer comparisons, the team use a standard analytical framework. The first two variables in the analytical framework are industry background and competitive advantage which combine to identify the opportunity that exists for a company to deliver sustainable above-average earnings growth. They analyse the industry and market in which the company operates, and whether it possesses any clear and sustainable competitive advantages. Considerations here include the growth rate of the industry, the structure of pricing, barriers to entry, the uniqueness or otherwise of the strategy and any enduring cost advantages. The second two variables in the analytical framework are financial characteristics and management attitude which determine whether the team think the company in question will successfully execute the opportunity that exists, for the benefit of shareholders. The team analyse the financial structure of the company, in particular whether it can fund growth from internally generated cash flow, and then form judgements on management's strategies and follow their actions closely with a view to assessing their capabilities. They also analyse management's capital deployment (for example, expansionary capital expenditure, acquisition activity and share buybacks) for tangible evidence that management run the business in shareholders' interests. Although valuation is important, it does not become a factor until after the four variables have been assessed as they believe it is more difficult to identify companies that show genuine growth characteristics than those that are, at face value, quantitatively cheap. They believe that mistakes are more often made by misjudging growth rather than misjudging what to pay for it. A wide range of intrinsic and relative valuation measures are used, taking into account earnings, cash flows and returns.

When constructing the portfolio, the team classify their holdings into four different growth areas to build a robust fund that can withstand market cycles – these are secular growth, growth stalwarts, special situations and cyclical growth. Secular growth names are higher growth non-economically sensitive businesses such as new internet disrupters or factory automation businesses. Growth stalwarts typically have strong pricing power and sustainable cash flows, whilst special situations tend to exhibit a valuation anomaly when compared to their balance sheet assets. Cyclical growth stocks are those where the peak of earnings will rise over a number of cycles. The team also undertake inertia analysis to examine how a static portfolio, where no changes have been made over varying time periods, would perform against the current portfolio. At a bi-monthly portfolio meeting, the investment managers promote changes to portfolios, taking into account recent research and ratings given at the weekly stock discussion or other strong views they may support. The size of holding generally reflects the level of conviction expressed in this discussion, although final decisions for this fund rest with the two co-managers.

The sell discipline is based on the same four primary factors as the buy discipline – industry background, competitive advantage, financial characteristics and management attitude, and if one or more of these fundamentally changes that will be a trigger to re-assess the holding. Examples of when this might occur include company results failing to meet expectations, an outlook warning, the competitive landscape changing, or an exogenous shock to the Japanese economy. Poor performance of a management team will also be considered as a warning sign. In each of these cases, the team will re-examine the original reasons for purchasing the stock and consider whether these have changed irrevocably. The fund does not normally sell a stock on valuation grounds alone, but they will sell if they no longer see the targeted potential upside in a company. The team are prepared to increase their stake in a stock that has doubled which behaviourally is difficult to do. This is especially true of faster growth companies which are at an early stage of their development where position size is increased as confidence in the outcome grows.

The two fund managers are responsible for all decision-making in the fund. There is also a dedicated investment risk team which use a range of tools and measures to analyse the risk within portfolios. These include risk models provided by SunGard APT, Style Research, UBS and Factset portfolio analytics. The key aim of the portfolio risk management process is to ensure that funds are managed with a level of risk consistent with performance expectations. This is achieved in part by reviewing a range of metrics on a regular basis. A risk decomposition highlights the sources of risk, and processes exist to ensure issues are discussed and the appropriate action taken if necessary. The team also review independent sources of style analysis as a check on their investment philosophy, an example being Style Skylight. Fund attribution is carried out at stock and sector level as required. The team look at attribution by largest stock contribution and by largest holding size and examine contribution to stock-specific risk.

Liquidity analysis for each stock in the portfolio is conducted on an ongoing basis by the trading team, and a formal liquidity report is conducted once a quarter. In these reports the traders analyse the projected costs of liquidating 100%, 30% and 10% of the mandate in question, and highlight the specific difficulties of liquidating particular lines of stock within the portfolios based on average daily volumes. The guidelines regarding the liquidity of the portfolios are reviewed regularly by the investment risk committee. Any company that does not meet these standards will be excluded from the portfolio. The fund does not take active currency positions, as an assessment of the underlying currency risk is carried out during the fundamental analysis of each company considered for inclusion in the portfolio.

ESG

For the managers the core principles for company assessments are:

- Prioritisation of long-term value creation
- A constructive and purposeful board
- Long-term focussed remuneration with stretching targets
- Fair treatment of stakeholders
- Sustainable business practices

These factors are an important consideration for the long-term investment case with key areas of engagement: board composition, management alignment and capital allocation.

As active managers, Baillie Gifford recognise that owning a company's shares confers certain rights and responsibilities and governance and sustainability factors play an integral role in their investment process. They believe that good corporate governance can enhance shareholder value; whilst any issues identified can impact each of the four qualitative factors that they look at in their bottom-up investment analysis: industry background, competitive position, financial strength and management quality.

As they are looking to invest in companies that offer long-term sustainable growth, management quality is key. The values, time frames, and motivations of the executives and non-executives matter when looking to invest with a five year plus time period; they influence capital allocation decisions, attitudes to shareholder rights, remuneration, corporate culture, as well as environment and social performance.

PAST & CURRENT POSITIONING/STRATEGY

The positioning of the fund is driven by bottom-up stock-picking which guides the composition of the four different growth areas in the portfolio. Since the launch of the fund, companies categorised as secular growth have been the largest allocation within the fund with a weighting ranging from approximately 35% to 45% (at the end of December 2021 it was 35%); cyclical growth names have ranged from 25% to 35% (at the end of December 2021 it was 24%), while both growth stalwarts and special situations have typically been 10% to 20% (and were 22% and19% respectively at the end of December 2021). Each of the four growth areas contribute to the total dividend yield in the fund although the cyclical growth names will normally exhibit a higher weighted average yield. Approximately 48% of the fund yields less than 2%, while 24% yields 2-3%, 11% yields 3-4% and 17% yields more than 4%. In terms of the sector positioning, manufacturing names have typically accounted for between 40% to 50% while financials have accounted for 20% to 25% of the overall fund. The team hold a balance of exporting and domestic names as they do not attempt to forecast the yen/dollar exchange rate.

The fund is relatively concentrated, with the top twenty names accounting for just over 50% of the overall portfolio. Given the long-term investment approach, there are several companies that have occupied large allocations since 2016. These include companies such as: SBI Holdings, Fanuc, Sumitomo Mitsui Trust, and MS&AD Insurance. SBI Holdings and Fanuc are examples of secular growth names, each of which conduct business across different industries. SBI Holdings is a financial company with a diversified range of business segments including online financial services, asset management and biotechnology, while Fanuc is a global leader in the robotics industry, a play on a secular upward trend in automation as companies try to improve levels of productivity.

The balanced approach to investing taken by the fund, with investments categorised into one of four areas, provides a natural element of diversification and prevents over-concentration in any single type of company.

The Secular Growth area comprises companies usually offering significant upside potential. As well as the digital disrupters, automation names such as Fanuc and Keyence feature here. Keyence is focused on the rapid growth segment of vision and sensors within the factory setting. Rising labour costs and technological improvements in vision learning underpin the businesses long term opportunity in the continuous monitoring of the entire supply chains and manufacturing processes. Another example in this area is disruptive healthcare name Sysmex, a global leader in in-vitro diagnostics and looking to move into liquid biopsies. Secular growth companies such as this operate in areas with large addressable markets and offer the potential for exponential returns.

The Stalwart holdings of non-cyclical consumer staples have a different profile. Skincare has been a successful area of investment for the portfolio with Japanese companies having a reputation for technological superiority, having needed to meet discerning demands of domestic consumers. Many of these names are now expanding in China where premiumisation is at a much earlier stage. This includes companies such as Shiseido, KOSE, and Pola Orbis. Another name in this area is snack food and cereal company Calbee which is looking to develop healthier products. These names offer compounding growth potential with often the longevity and durability underestimated by the market.

Special Situations comprises stocks with opportunities arising due to the history in Japan of cash hoarding or the presence of cross-shareholdings. As a result, conglomerate discounts are available in many companies such as Sony, a content king in the movie, music, and gaming world, and SoftBank which offers access to Alibaba amongst other international assets.

Cyclical Growth businesses have structural growth tailwinds, but can deliver cyclical earnings in the short term with many of these names hit during the risk off environment driven by the pandemic. Electrical component maker Rohm, a manufacturer of high-end semiconductors, and Murata a niche maker of multi-layered ceramic capacitors both feature in this area. Mazda is another example of cyclical growth opportunity with the company having access to the in-house R&D of the Toyota Group and a new product cycle which should allow margin improvement. Some old economy names such as Mitsubishi and Mitsui have shifted away from just trading raw materials towards better management of their investee companies and delivering a consistent double digit return on equity.

The common denominator for all holdings in the fund is the possibility of a doubling to the upside which, for the secular growth companies, will be reliant on a continuation of the strong top line growth, whilst some of the cyclical names have the potential for a re-rating through, for example, margin expansion or efficiency gains.

Japan has followed the course of other markets in terms of the relative performance of growth versus value. Whilst the overall market took a big hit in March 2020, the initial bounce back favoured growth stocks such as enablers of digital disruption together with EV related names and beneficiaries of digitalisation. Year to date there has been a rotation in the market with some of last year's worst performers topping the leader board, whilst a number of last year's successful growth stocks have seen a pullback in their share prices. This portfolio is constructed from the bottom up, but has not been immune to trends, with a pullback in names in the secular growth bucket and better performance from the cyclical businesses in the fund. The team continue to look for names that can double over a 5 year period and are agnostic whether this comes from multiple expansion or top line growth. As a result, some names are held such as Mazda which are trading on low multiples. This is not just a secular growth fund with its objective of a higher yield at the overall portfolio level than the market but is a more balanced approach in Japan and has more cyclical value names than other strategies managed by the team. The two co-managers balance growth and income opportunities.

In 2020 the Growth Stalwarts holdings were hard hit, but we have seen a revival in fortunes this year with many of these names on depressed valuations. These have typically been steady eddy compounding stocks. An example here is Pola Orbis which suffered as it had a duty-free segment but is a long-term beneficiary of premiumisation in Asia for its skin care products. It has strong brand recognition in the region and has been added to. Many skin care type businesses also produce pharmaceutical products in this area and the company is expanding in China due to its brand strength.

Tokio Marine Holdings was a new purchase for the fund and has a dominant top three position in the P&C industry in Japan. SoftBank Corp is part of the SoftBank Group and is the SBKK telecom part of the business. This is a domestic Japanese communication business which is looking to develop its own online eco system with a cash generative telecomms business to fund this. There is also a good starting yield. The company has emerging e-commerce and payment opportunities and has a subsidiary which owns the former Yahoo Japan.

Amongst cyclical names Sumitomo Mitsui Trust was added to as this is not just a bank but has unique characteristics with its strong fee based income. Asset administration, pensions, and investment trusts give it a strong and stable revenue stream. It also has a large equity book accounting for around 84% of its market cap.

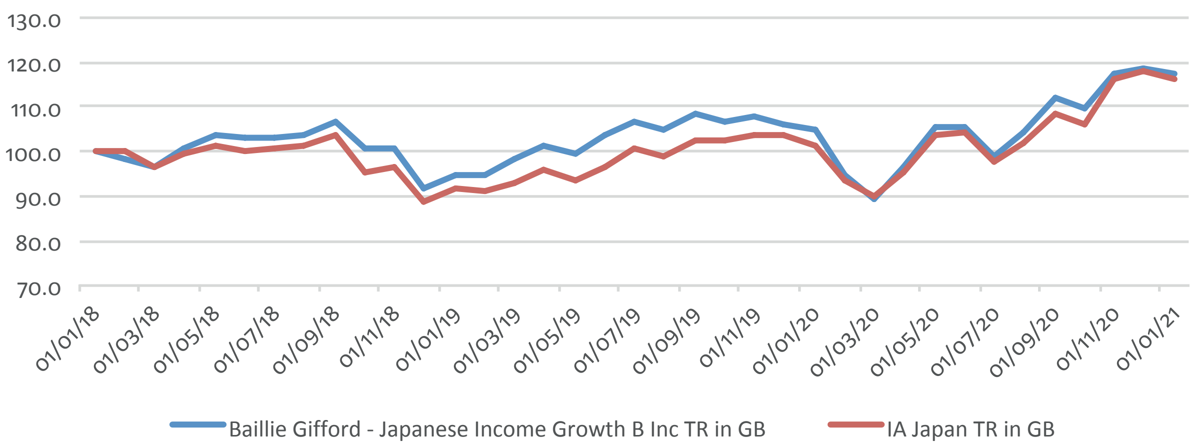
SoftBank Group saw a reduction in the position after the strong rally during the first quarter. It benefitted from its holdings in other disruptive companies such as Alibaba and DoorDash. The discount for the sum of its parts shrunk from 70% to 30% and Soft Bank Corp was considered to be more attractive in its own right. The team have some concerns about corporate governance and regulatory issues at Alibaba which saw the ANT IPO pulled at the last minute and the company has become more politicised. The team are concerned China may not like the fact that a Japanese company owns 20% of one of its global champions.

The fund also sold two REITs in 2020 as their portfolios were hotel orientated, clearly hit by the coronavirus pandemic. Japan Tobacco was also sold with this high yielder replaced by another higher yielding name Soft Bank Corp (mentioned above) which has a 6-7% yield. Toyota saw a reduction in its position despite its stake in Tesla with a rotation into DENSO Corporation an EV related parts supplier where there was felt to be a better opportunity.

Whilst there have been some big moves in the market year to date, there have been no significant portfolio changes in the early part of 2021.

PERFORMANCE

Performance of Fund vs IA Sector



Data supplied by Baillie Gifford, sourced from FE Analytics

The fund delivered strong absolute returns and outperformed its benchmark in 2020. The main driver of outperformance has been a positive contribution from a number of disruptive online business models such as Softbank together with internet infrastructure business GMO Internet. Softbank Group, which has exposure to Chinese e-commerce giant Alibaba, as well as multiple listed and unlisted investments operating in the online or artificial intelligence space was one of the largest contributors to performance. Wacom, a leader in touch input was another strong contributor after seeing significant Chinese demand for its digital stylus as a result of growth in online education.

There were varied market conditions during the whole of 2020 and the fund strongly outperformed in Q2 with SBI Holdings doing particularly well. The exposure within the fund to internet platforms and e-commerce was a significant positive in the third quarter, as the coronavirus pandemic acted as an accelerant to the adoption of their technologies. Another strongly performing name during Q3 was Cyber Agent, a vertically integrated online advertising operation which has expanded into online media. After very strong performance in Q2 and Q3 the fund did lag its benchmark index in the fourth quarter when cyclical names saw a strong rally on the November vaccine news.

In quarter one 2021 cosmetic company Pola Orbis was the biggest contributor to performance after better-than-expected operating profit with its own Orbis brand performing well. The company's medium-term plan was well received by the market with its focus on the acceleration of overseas growth and a re-vamping of domestic sales channels. In Japan there will be a merger of online and offline channels and store expansion in China with the number there set to double from 50 to 110 with a commitment to maintaining high operating margins by avoiding discounting. The company has a focus on differentiation through its counselling and aesthetician services.

SBI Holdings saw a recovery in its share price in 2021 which had been triggered by the US SEC's complaint against Ripple Labs and releasing better than expected earnings results. The company's asset management segment has benefitted from a robust IPO market in which they have become a dominant player. They have also become the market leading brokerage company in Japan surpassing Nomura having used the comparative cost benefits of the internet to slash commission rates driving scale.

Tyre manufacturer Bridgestone performed well after generating strong gains from its sale of non-core US business Firestone building products. The company also released encouraging results and a medium-term plan centring on further restructuring and growth of higher margin premium products. Detractors in Q1 included Wacom which pulled back on fears that growth in teleworking and online education could begin to subside, together with business-to-business food ordering platform Infomart which reduced its forward guidance due to increased costs stemming from investment in IT. Snack and cereal company, Calbee, detracted with depressed earnings from its souvenir business and fears increased promotional expenses would weigh on profit growth going forward.

SUMMARY & EVALUATION

The fund outperformed in 2020 and since its launch its launch in 2016. It has now benefitted from growing confidence in a global economic upturn as the portfolio has less in Secular Growth names and more in Cyclical Growth / Growth Stalwarts / Special Situations than the mainstream Japan fund and is providing investors with an above average yield compared to the Japanese market.

This fund is managed by a well-resourced Japanese equity team who have an excellent track record of managing strongly performing mandates in core Japan, smaller companies and also investment trusts. Matthew Brett has managed this fund from launch and also manages the core Japanese fund and co-manages the Japan Trust PLC. He has been assisted since launch by Karen See as co-manager. This fund has a slightly different approach to the more growth-orientated mandates run by the team. It is likely to have slightly lower tracking error and active share over the long-term and there is an emphasis on total returns and dividend growth, with the overall portfolio yield above that of the market.

The research process is very similar to the core Baillie Giffford approach with significant stock overlap. This fund however is diversified across and number of types of businesses – something that is wider than sector classifications and has delivered its returns without reliance on just a few stock names. The fund invests in between 45 and 65 names, and there are no particularly large individual position sizes. Whilst the core Japanese fund has a performance target of +2% per annum over 3-5 years, this fund is looking for outperformance of 1.5% per annum due to its constraint of delivering higher than average income. It should be noted in addition that the returns from the core portfolio have been significantly above the performance target over the long term and the performance record of the team is also a major positive for this mandate.

The fund is well positioned to benefit from the upswing in both the global and Japanese economies as the post Covid-19 recovery gathers momentum over time and will benefit if Japan increases dividend pay-out ratios which remain low compared to other developed markets. There is also a competitive cost structure in place relative to other funds within the sector.

As the administration is done in-house, the spread between the AMC and the OCF is minimal. It is important to note that the strategy is invested in yen denominated assets and receives yen denominated income, but the fund is unhedged and priced in sterling. Consequently, the distributions from the fund are exposed to the yen-sterling exchange rate as well as changes in the underlying yen dividends.

The fund is suitable for use as a core holding in a portfolio of Japanese collectives as it offers a more balanced approach between growth and value including cyclical growth and special situations within its remit. The dividend element should provide some protection at times of market downturn. The approach will not sacrifice capital growth prospects and the focus of the fund is away from higher yielding low growth names. We expect the fund to continue to deliver on the strong performance record that the team have established in Japanese equities.

RSMR

Established in 2004 RSMR provides research and analysis to firms working across the UK's personal financial services marketplace.

Our work is completed with total impartiality, without any conflict of interest and delivered to a high professional standard by a team of experienced and highly qualified people.

Working with advisers

We provide specialist research, analysis and support to a diverse range of financial advisers and planners helping them to deliver sound advice to their clients, backed by rigorous and structured research and due diligence.

The main regulatory body in the UK, the FCA, states that personal recommendations made by advisers should be 'based on a comprehensive and fair analysis of the relevant market' and this has led to closer scrutiny of the whole advice process. Our solutions are designed to help advisers meet these challenges whilst recognising that advisory firms require a range of flexible options that best meet their own business needs and those of their clients.

Working with providers

We work with all the leading fund groups, life and pension companies and platform operators across the financial services sector offering straight forward and pragmatic advice to help add value and improve their business performance and efficiency whilst treating customers fairly in line with FCA requirements.

Ratings

Our innovative ratings are now recognised as market leading and cover a broad area of investment solutions including single strategy funds, SRI funds, Multimanager and multi-asset funds, DFMs and investment trusts. Our familiar 'R' logo is now recognised as a trusted badge of quality by advisers and providers alike and a 'must-have' when selecting funds. Our ratings are founded on a strict methodology that considers performance and risk measures but places a greater emphasis on the ability of fund managers to continue to deliver performance in the years ahead. based on our in-depth face-to-face meetings with fund managers across the globe.

We understand financial services and we will work alongside you to deliver tailored solutions that are right for your clients and your business.

Our research. Your success.

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