

# BAILLIE GIFFORD

## *Baillie Gifford Japanese Fund*

31 March 2023

### About Baillie Gifford

<b>Philosophy</b>	Long-term investment horizon A growth bias Bottom-up portfolio construction High active share
<b>Partnership</b>	100% owned by 51 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

Our objective is to produce above-average long-term performance through investment in Japanese equities. We believe the Japanese equity market offers active managers a broad selection of high quality companies capable of delivering attractive and sustainable earnings growth for shareholders. Over time we expect this approach to generate better returns than the Japanese market. In contrast to other major markets, growth often commands little or no valuation premium in Japan, and we continue to identify global leading businesses which trade on a substantial discount to their peers. This provides an excellent backdrop for our investment style.

### Fund Facts

Fund Launch Date	08 October 1984
Fund Size	£2634.5m
IA Sector	Japan
Active Share	79%*
Current Annual Turnover	5%
Current number of stocks	60
Stocks (guideline range)	45-65

\*Relative to TOPIX. Source: Baillie Gifford & Co, Tokyo Stock Exchange.

### Fund Manager

Name	Years' Experience
Matt Brett*	20

\*Partner

## Fund Objective

To outperform (after deduction of costs) the TOPIX, as stated in sterling, by at least 1.5% per annum over rolling five-year periods.

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-Acc (%)	1.5	-5.4	7.5	2.3
Index (%)*	3.4	2.8	7.7	3.6
Target (%)**	3.8	4.3	9.3	5.2
Sector Average (%)***	3.3	0.7	8.3	3.4

Performance source: FE, Revolution, Tokyo Stock Exchange, total return in sterling.

\*TOPIX.

\*\*Target refers to Target Benchmark: TOPIX (in sterling) plus at least 1.5% per annum over rolling five-year periods.

\*\*\*IA Japan Sector.

## Discrete Performance

	31/03/18- 31/03/19	31/03/19- 31/03/20	31/03/20- 31/03/21	31/03/21- 31/03/22	31/03/22- 31/03/23
Class B-Acc (%)	-1.1	-8.7	43.5	-8.5	-5.4
Index (%)*	-1.8	-2.5	24.8	-2.7	2.8
Target (%)**	-0.3	-1.0	26.7	-1.2	4.3
Sector Average (%)***	-3.6	-3.4	31.8	-4.4	0.7

Performance source: FE, Revolution, Tokyo Stock Exchange, total return in sterling.

\*TOPIX.

\*\*Target refers to Target Benchmark: TOPIX (in sterling) plus at least 1.5% per annum over rolling five-year periods.

\*\*\*IA Japan Sector.

## **Market environment**

Tourism numbers continued to tick up during the quarter as the country (and region) relaxed more mobility restrictions. The recent declassification of Covid to a similar status as the common flu and the easing of rules regarding the use of facemasks underlie this gradual improvement. Consumption has been climbing at a healthy rate as a result.

The potential implications for unwinding years of ultra-loose monetary policy have also stirred markets this quarter. Academic Kazuo Ueda has promised to be “creative” when he takes the reins from Bank of Japan Governor Haruhiko Kuroda, who has been attempting to defeat deflation for the past decade in the role. There are tentative signs that suggest he has succeeded; with consumer prices rising at rates not seen since the 1980s and wage inflation reaching its highest since 1993 (according to initial Shunto wage data). Japan’s escape from its deflationary past presents a huge opportunity. For 30 years, corporates have delayed investment and consumers have put off purchases, handicapping the country’s productive capacity. The advent of real wage growth could reverse this cycle and augur well for Japan’s equity market, which presents an exciting proposition for international investors looking to position their portfolios for higher inflation.

Although initially aided by the prospect of rate rises, the collapse of Silicon Valley Bank (SVB) and other financials quickly caused a broad-based sell-off in financials, on the fear that this may be a prelude to further turmoil.

In other encouraging news, the Tokyo Stock Exchange has announced a raft of measures aimed at boosting Japan Inc’s corporate value, such as requesting companies that trade below book value – almost half of TOPIX constituents – disclose how they intend to improve capital efficiency. This is expected to bolster market returns, effectively buttressing the actions of activists, by targeting inefficiently run businesses that have diluted their returns through the excess accumulation of cross-shareholdings or of low-yielding cash and property.

## **Performance**

The broader economic revival/reopening that Japan, and its neighbours, have experienced as tourism and consumption bounce back has helped encourage higher capital expenditure as companies recalibrate supply for higher demand. This has helped the prospects for our robotic and manufacturing businesses, such as Fanuc, the world’s largest robotic company, Keyence, a leader in vision and sensory automation solutions, and DMG Mori, a leading global machine tool maker. Many have benefited from the reopening of China, where capex sentiment has until now, been subdued due to mobility restrictions. A zero weighting towards various financials, such as Mitsubishi UFG has also helped relative performance.

Softbank was one of the largest detractors as a result of the second-order impact of SVB. The failure of this institution knocked investor confidence in early-stage businesses that may require future financing, compounding the effect that quantitative tightening has already had on those with long-duration cash flows. Softbank, as a result of its exposure to unlisted technology stocks through the Vision Fund, saw its share price slide, before later rising on news that Alibaba would be restructured into six business units. We expect that founder Masayoshi Son’s defensive positioning may have helped insulate the group’s exposure to the broader fallout from SVB. Skincare company Shiseido, and online media, advertising and gaming company CyberAgent were also weak during the quarter.

## **Notable transactions**

During the quarter we purchased Z Holdings, the company formed from the merger of Yahoo Japan (one of Japan’s leading online media and ecommerce businesses) and Line (the dominant online messaging platform in Japan). It also has a stake in PayPay, the leading e-money platform in Japan. We believe that there are significant benefits to be realised from combining these businesses and that they have the potential to be much larger in the future as the shift to online activity continues and as growth synergies are realised.

This was partly funded by the partial sale of Mercari and Mitsui. Mercari offers a consumer-to-consumer trading platform using a smartphone app, with a dominant position in Japan in addition to an emerging opportunity within the US. Our hypothesis is that this US operation could become of significant value over time. However, recent results have not been encouraging and on balance, we decided a smaller holding was appropriate while we continue to monitor progress. Mitsui & Co is one of Japan’s leading trading companies, with particular strength in iron ore, copper and liquefied natural gas (LNG), was also reduced after a period of buoyant profits on the back of high commodity prices.

## Stock Level Attribution

### Top and Bottom Ten Contributors to Relative Performance

#### Quarter to 31 March 2023

Stock Name	Contribution (%)
Fanuc	0.3
DMG Mori	0.3
Mitsubishi UFJ Fin Grp	0.2
Misumi	0.2
Bridgestone	0.2
Tokio Marine Holdings Inc	0.1
Wacom	0.1
Denso	0.1
SMC	0.1
Dai-ichi Life Holdings Inc	0.1
SoftBank Group	-0.6
Shiseido	-0.3
CyberAgent	-0.3
Pola Orbis	-0.3
Calbee	-0.3
Shin-etsu Chemical	-0.2
Sumitomo Mitsui Trust	-0.2
Nintendo	-0.2
Mercari	-0.2
MS&AD Insurance	-0.2

#### One Year to 31 March 2023

Stock Name	Contribution (%)
Toyota Motor	0.8
Tokyo Electron	0.4
Sumitomo Mitsui Trust	0.4
DMG Mori	0.4
Mitsui	0.3
INPEX	0.3
Unicharm	0.3
Bridgestone	0.2
Mixi	0.2
Calbee	0.2
Rakuten	-1.4
CyberAgent	-0.9
SBI Holdings	-0.6
Daiichi Sankyo Co	-0.6
Sumitomo Metal Mining Co	-0.5
Kubota	-0.5
Wacom	-0.4
SoftBank Group	-0.4
Nintendo	-0.4
GMO Internet	-0.4

Source: Revolution, Tokyo Stock Exchange. Baillie Gifford Japanese Fund relative to TOPIX.

Some stocks may have been held part period.

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

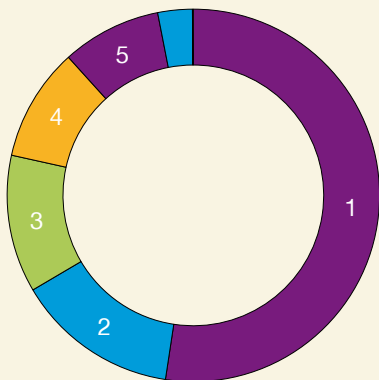
Transactions from 01 January 2023 to 31 March 2023.

### New Purchases

Stock Name	Transaction Rationale
Z Holdings Corp	Z Holdings is the company formed from the merger of Yahoo Japan (one of Japan's leading online media and ecommerce businesses) and Line (the dominant online messaging platform in Japan). It also has a stake in PayPay, the leading e-money platform in Japan. We believe that there are significant benefits to be realised from combining these businesses and that they have the potential to be much larger in the future as the shift to online activity continues and as growth synergies are realised. The company has been spending heavily as it invests in future growth and we believe the market is failing to take account of what could result in the long term. Therefore we decided to take a holding.

There were no complete sales during the period.

## Sector Exposure



		%
1	Manufacturing	52.4
2	Finance & Insurance	14.1
3	Transport And Communications	11.9
4	Services	9.8
5	Commerce	8.6
6	Real Estate	3.0
7	Cash	0.1

## Top Ten Holdings

Stock Name	Description of Business	% of Portfolio
SoftBank Group	Telecom operator and technology investor	4.8
Sumitomo Mitsui Trust	Japanese trust bank and investment manager	4.1
FANUC	Robotics manufacturer	3.8
SBI Holdings	Online financial services	3.5
Sony	Consumer electronics, films and finance	3.2
GMO Internet	Internet conglomerate	3.2
Bridgestone	Tyre manufacturer	3.1
Kubota	Agricultural machinery	2.9
Misumi	Online distributor of precision machinery parts	2.9
Shiseido	Japanese cosmetics manufacturer	2.9
Total		34.5

Voting Activity

Votes Cast in Favour		Votes Cast Against		Votes Abstained/Withheld	
Companies	20	Companies	1	Companies	None
Resolutions	216	Resolutions	3	Resolutions	None

The strategy continues to ensure our ESG research, integration and stewardship activities are focused on issues material to the investment case and companies' long term-growth prospects

In April this year, the 2022 Investment Activities Stewardship Report will be submitted to UK FRC (Financial Reporting Council) and made available on our website

Many of our engagements this quarter have focused on governance and remuneration related issues as we go into and through voting season

Company Engagement

Engagement Type	Company
Environmental	Fanuc Corporation, Sumitomo Metal Mining Co., Ltd.
Social	Fanuc Corporation, Recruit Holdings Co., Ltd., Sumitomo Metal Mining Co., Ltd.
Governance	Fanuc Corporation, OUTSOURCING Inc., Pola Orbis Holdings Inc., Recruit Holdings Co., Ltd.

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 %
SoftBank Group	4.8	Makita Corporation	0.6
Sumitomo Mitsui Trust	4.1	Park24	0.6
FANUC	3.8	Outsourcing	0.6
SBI Holdings	3.5	Digital Garage	0.5
Sony	3.2	Freee	0.4
GMO Internet	3.2	PeptiDream	0.4
Bridgestone	3.1	Broadleaf	0.3
Kubota	2.9	BASE	0.2
Misumi	2.9	Infomart	0.2
Shiseido	2.9	Bengo4.com	0.2
Nintendo	2.8	Cookpad	0.1
MS&AD Insurance	2.8	Cash	0.1
Keyence	2.7	<b>Total</b>	<b>100.0</b>
DENSO	2.6		
CyberAgent	2.6		
Rakuten	2.6		
Sumitomo Metal Mining	2.5		
Unicharm	2.2		
Kao	2.2		
Mitsui	2.0		
Rohm	2.0		
Calbee	2.0		
Bank of Kyoto	1.8		
Japan Exchange Group	1.8		
Pola Orbis	1.8		
SMC	1.8		
Kyocera	1.7		
Mitsubishi Corp	1.7		
DMG Mori	1.7		
Recruit Holdings	1.7		
Murata Manufacturing	1.5		
mixi	1.3		
Topcon	1.2		
Wacom	1.2		
Nidec Corporation	1.2		
Tokyo Tatemono	1.1		
Systemex	1.0		
Toyota Tsusho	1.0		
Sugi Holdings	1.0		
Asahi Group	1.0		
Tsumura	0.9		
COLOPL	0.9		
Mercari	0.9		
Nippon Electric Glass	0.8		
Z Holdings	0.7		
Pigeon	0.7		
Mitsubishi Estate	0.7		
Kakaku.com	0.7		
IIDA	0.6		

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Share Class	Share Class Inception Date	ISIN	SEDOL	Annual Management Fee (%)	Ongoing Charge Figure (%)
Class B-Acc	02 August 1999	GB0006011133	0601113	0.60	0.63
Class B-Inc	02 August 1999	GB0006010945	0601094	0.60	0.63

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 March 2023 and source is Baillie Gifford & Co unless otherwise stated.

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