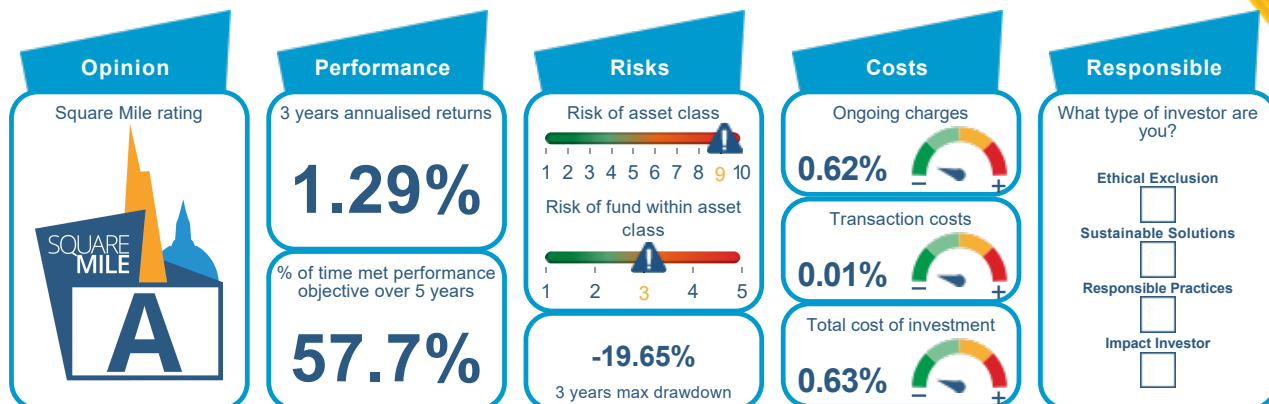


# Baillie Gifford Japanese Inc Growth B Inc

November 2023



Source: Square Mile and Refinitiv, Data as at: 30th November 2023.

## Overview

The managers are aiming to deliver long-term total returns as well as maintaining an underlying portfolio yield higher than that of the TOPIX index. In practice, they are looking to outperform the fund's benchmark index by at least 1% p.a. over rolling five year periods through a combination of capital appreciation and income.

Whilst Japan has one of the lowest payout ratios within the developed markets, dividends have been increasing in recent years as corporate attitudes towards shareholder returns have started to improve. A trend which the managers are seeking to take advantage of in order to grow the level of income over time and to deliver strong long-term total returns.

We would highlight that the fund is exposed to the movements of the stock market and, as such, capital returns might be volatile and income distributions can fluctuate and are not guaranteed. In addition, the fund may not always produce a higher yield than the TOPIX.

## Square Mile's Expected Outcome

We believe that the fund should be able to outperform the TOPIX by at least 1% p.a. over rolling five-year periods through capital growth and income whilst maintaining a yield higher than the TOPIX.

## Square Mile's Opinion

This fund is managed by a team that we regard highly and which has an impressive long-term track record of investing in Japanese equities, and whilst this is a relatively new strategy, having launched in July 2016, we believe it has plenty of features that make it an attractive long-term strategy for investors that wish to have a Japanese equity exposure with an income bias.

Ideas are generated from a number of sources including the team's own research, company meetings and from interaction with other Baillie Gifford investment teams. The Japan team believe that companies in Japan are in a unique position as they are able to operate for growth, whilst also ramping up their dividend payments. Indeed, the Japan team believes that there is a significant opportunity to benefit from the secular change in corporate attitudes towards dividend payouts and, in what was previously a limited market, there are now more and more companies that are not only growing, but that are also proving to have attractive yields or dividend growth potential - characteristics which the team seeks when looking for investment opportunities.

The managers of this fund aim to increase distributions over time, whilst also maintaining an underlying portfolio yield higher than that of the TOPIX index, however we would note that they are not willing to chase yield for yield's sake. Given the style of management applied, this fund can experience variable performance relative to the index and in periods when investment styles such as value are in favour, the fund might struggle. Nonetheless, we believe that the dividend paying companies held in the portfolio mean the fund ought to be more resilient in downward trending markets.

## Fund Manager's Formal Objective

The Fund aims 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.

|  |                            |
|--|----------------------------|
| <b>Outcome:</b> Capital Accumulation, Income | <b>Domicile:</b> UK        |
| <b>Active/Passive:</b> Active                | <b>Benchmark:</b> TOPIX    |
| <b>Asset Class:</b> Equity                   | <b>IA Sector:</b> IA Japan |
| <b>Yield:</b> 2.44%                          | <b>Fund size:</b> £501 M   |

## Asset Manager Overview

Baillie Gifford is a long established Edinburgh based investment partnership that is particularly well known amongst institutional investors. The Japanese team is made up of around 10 members, a number which is considered large enough to deal with the workload but small enough to ensure that decisions can be swiftly made. Alongside the core team there are two additional researchers based in Tokyo and a dedicated ESG analyst. Portfolios run within the Japanese franchise follow a strong team based approach and all of the team's members share the same growth focused investment philosophy and process of identifying attractively priced Japanese securities. This fund's portfolio managers, Karen See and Matthew Brett, have spent their whole investment careers at Baillie Gifford, having joined the firm in 2012, and 2003, respectively.

Essentially, the Japanese team members are long-term growth stock pickers looking to invest in companies growing their earnings, which they believe will result in dividends that will also grow over time. Research efforts are focused on identifying companies that possess sustainably high returns on capital as well as ones focused on improving their returns and balance sheet efficiency. The managers aim to populate the portfolio with a combination of different types of growth companies that can, broadly speaking, be placed into one of four categories. Firstly, they look for established, durable, stable and growing firms operating in industries with high barriers to entry. The team believes that such types of company tend to be undervalued by the market over the long term. Secondly, the portfolio has positions in younger more rapidly growing businesses, where the managers believe that double-digit growth rates can be sustained over a number of years. Thirdly, they feel that attractive growth opportunities can also be found in more cyclical sectors of the market, whilst the final category focuses on companies in turnaround situations. These may be seemingly struggling businesses, but are ones that the managers believe to be experiencing structural or positive change. This category also includes companies where the team sees potential value hidden in the form of financial assets.

The only real difference between the process for this fund and that of the other Japanese funds that the team manages is the consideration of balance between growth potential and yield, e.g. is the growth high enough to warrant a lower yield or is the yield high enough to warrant lower growth? The final portfolio will usually consist of 50 to 60 stocks that are chosen with no reference to the stock's weighting within the index. Sector allocations are primarily driven by the stock selection process, though there are a few guidelines in terms of ensuring sufficient diversification.

## ESG Integration

### Asset Manager ESG Integration

Baillie Gifford became a signatory to the UN Principles for Responsible Investment in 2007, currently having a firm-wide Investment & Stewardship Policy score of 4 out of 5. Baillie Gifford is also a signatory of the UK Stewardship Code and has joined several industry initiatives, including the Net Zero Asset Managers Initiative. At a business level they are committed to double carbon offsetting their own emissions through tree planting. They have also appointed an Environment Officer who is tasked with driving the businesses' own sustainability practices.

Baillie Gifford expect ESG to be of great importance to how they operate in the coming years, however they are not underestimating the increased complexity of the area from both a regulatory, and client preferences, perspective. They therefore look to integrate ESG in a thoughtful way as they believe it deepens company insights and can therefore improve investment returns. They also try to target the most relevant ESG factors at an individual company level.

Over recent years, Baillie Gifford has built a vast team of almost 50 individuals dedicated to ESG and sustainability. Over half of these are ESG Research and Engagement analysts who are embedded into the different investment teams and provide ESG input at a strategy level. The next biggest cohort are the ESG Services team who undertake pre-AGM analysis, execute voting and assist with ESG data. The remainder are split across a climate team who assess the inter-relationships between climate change and businesses, and a small client team. The majority of these recent hires are fairly early in their careers.

Baillie Gifford doesn't provide separated ESG scores for the companies they research, instead the focus is on qualitative in-house ESG research. They will not necessarily look to disinvest from companies in problematic industries, rather they will keep companies on watch and look for improvement over time.

In the coming years, the business is hoping to enhance their client reporting around ESG and sustainability, as well as increase the number of explicitly 'sustainable' funds within their product offering.

### Fund ESG Integration

ESG is integrated into this fund's investment process, and accounts for one of the four-factor investment framework. Within this, respective analysts will assess the ESG credentials of individual stocks prior to investment. Alongside this, the Japanese investment team has an integrated governance and sustainability analyst, Cian Whelan, who helps provide input and challenge to the team at the stock level. Furthermore, the team will, and do, vote against management if actions are deemed not in the interests of shareholders. The team will also engage with their holdings over the course of investment in order to unlock their potential value with respect to ESG capabilities.

Ultimately, whilst ESG factors are embedded within the thought process of the Japanese team, it does not drive their final investment decision, but instead is a lens through which they view the potential risks and opportunities within any investment case.

## Risk Summary

We would firstly highlight that this fund is invested in Japanese equities and exposed to the yen, both of which are generally quite volatile as the Japanese market is sensitive to the macroeconomic environment. The managers of this fund have a long-term investment horizon and focus on quality, growing companies of all sizes, with the smaller and medium size companies that the fund invests in typically being more volatile than their larger peers. Moreover, the final portfolio is constructed in a conviction manner, without reference to its benchmark index, the TOPIX, meaning that there are times when this fund can, and will, look and act very differently to the TOPIX, especially over shorter timeframes. In terms of its income outcome, this fund is unhedged and priced in sterling. It is invested in yen denominated assets and receives yen denominated income and so the income distributions will be subject to the yen-sterling exchange rate, as well as to changes in the underlying yen dividends. This strategy may be more suitable for investors with a longer time horizon, who are not seeking index like returns.

## Additional Information

**Annualised Return:** 1.29%

**Annualised Volatility:** 14.92%

**Max Drawdown:** -19.65%

**Max Gain:** 9.39%

**Max Loss:** -7.73%

**Sharpe Ratio:** 0.00

**Sortino Ratio:** -0.01

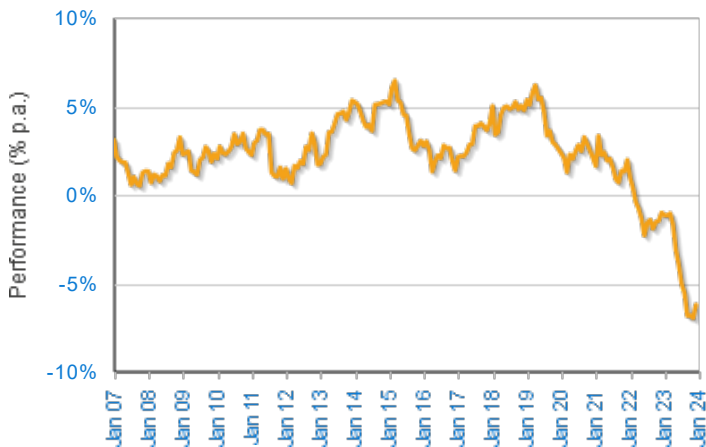
(3 years data to last month end unless otherwise stated)

## Qualitative Risk Assessment

|                       | Significant   | Potentially Significant  | Not Significant   |
|-----------------------|---|--|---|
| Equity Risk           |  |  |   |
| Interest Rate Risk    |   |   |   |
| Credit Risk           |   |  |  |
| Exchange Rate Risk    |  |  |   |
| Liquidity Risk        |   |  |  |
| Emerging Markets Risk |   |  |  |
| Derivative Risk       |   |  |  |
| Manager Risk          |   |  |   |

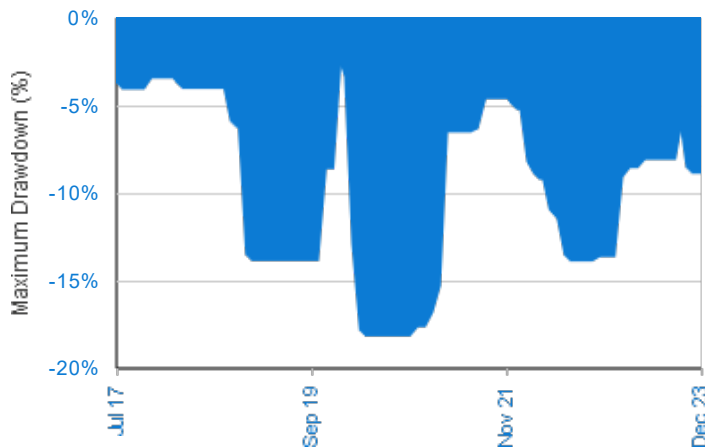
For the full summary of the risks, [click here](#)

### 3 Year Rolling Sector Outperformance



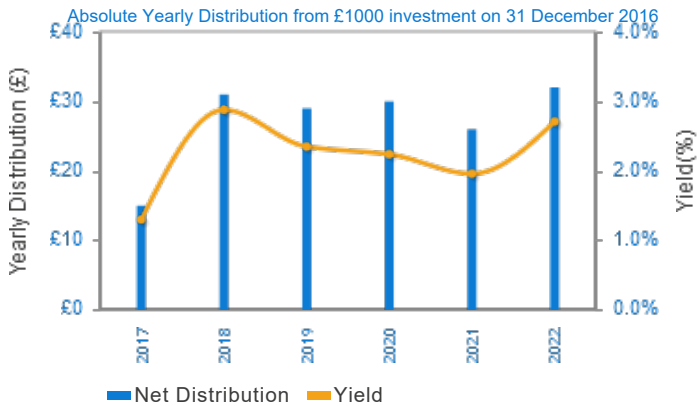
Source: Square Mile and Refinitiv, Data as at: 10th January 2024. Share price total return.

### Maximum Drawdown (Rolling 12 Months)



Source: Square Mile and Refinitiv, Data as at: 10th January 2024

### Income



This graph assumes that income is distributed to shareholders and not reinvested. Yield represents share price fluctuations.

Source: Square Mile and Refinitiv, Data as at:

### Calendar Year Performance To Quarter End

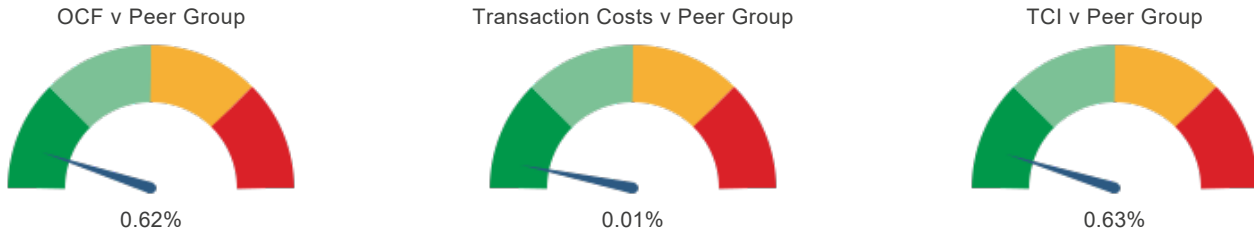
| Period | Fund (%) | Sector (%) |
|--------|----------|------------|
| 2023   | -6.8     | -7.4       |
| 2022   | 0.8      | 2.8        |
| 2021   | 11.5     | 12.1       |
| 2020   | 15.8     | 16.5       |
| 2019   | -5.8     | -11.5      |

Source: Square Mile and Refinitiv, Data as at: 28th November 2023

### Value for Money

Both the ongoing charge figure (OCF) of this fund and its transaction costs are significantly below the peer group median, leading to a very competitive total cost of investment. Therefore, we believe that this fund offers very good value for money because it offers investors access to a highly experienced and successful management team, with a well-regarded and sensible investment process and the ability to deliver strong outperformance of the TOPIX over the long term.

The main reason a fund will have a negative transaction cost is slippage. Slippage is the difference between the price quoted and the price at trade execution. If a stock is actually purchased at a lower price, a negative transition cost will arise. Over the long term you should expect transaction costs to be positive, but there can be instances where negative slippage is greater than the other transaction costs.



Source: Square Mile and Refinitiv, Data as at: 30th November 2023.

## Rating Changes

| Rating Changes over last 12 months | Time & Date rating changed |
|------------------------------------|----------------------------|
| A                                  | 10:00 / 18/11/2019         |
| Positive Prospect                  | 09:31 / 27/02/2018         |

The Square Mile ratings are reviewed every 6 months. For full details on the methodologies, [click here](#).

For a full list of all Square Mile rated funds, [click here](#).

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