

Baillie Gifford Japanese Smaller Companies Fund

31 March 2024

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 21 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

We invest in attractively valued smaller companies that we believe offer good growth opportunities. Growth may come from innovative business models, disrupting traditional Japanese business practises, or market opportunities such as growth by Japanese companies outside Japan.

Fund Facts

Fund Launch Date	01 April 1983
Fund Size	£223.6m
IA Sector	Japan
Active Share	96%*
Current Annual Turnover	16%
Current number of stocks	72
Stocks (guideline range)	40-80

*Relative to MSCI Japan Small Cap Index (in sterling). Source: Baillie Gifford & Co, MSCI.

Fund Manager

Name	Years' Experience
Praveen Kumar	16

Fund Objective

To outperform (after deduction of costs) the MSCI Japan Small Cap Index, 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 (%)	-5.0	-14.7	-15.4	-5.2
Index (%)*	6.2	12.4	3.0	5.0
Target (%)**	6.6	14.1	4.6	6.6
Sector Average (%)***	9.4	18.2	4.4	7.7

Source: FE, Revolution, MSCI. 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.

*MSCI Japan Small Cap Index (in sterling).

**MSCI Japan Small Cap Index (in sterling) plus at least 1.5% per annum over rolling five-year periods.

***IA Japan Sector.

Discrete Performance

	31/03/19- 31/03/20	31/03/20- 31/03/21	31/03/21- 31/03/22	31/03/22- 31/03/23	31/03/23- 31/03/24
Class B-Acc (%)	-14.7	47.9	-25.7	-4.4	-14.7
Index (%)*	-6.2	24.4	-7.7	5.4	12.4
Target (%)**	-4.8	26.3	-6.3	7.0	14.1
Sector Average (%)***	-3.4	31.8	-4.4	0.7	18.2

Source: FE, Revolution, MSCI. Total return net of charges, in sterling.

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***IA Japan Sector.

Market environment

This quarter marks a momentous change for Japan, for it has now escaped from the shackles of the past: Its market has smashed through the “iron coffin lid” of 1989 to post new highs, and its central bank has claimed victory over the country’s multi-decade fight with deflation.

After 35 years of operating within the shadows of the market’s peak performance of 1989, pushing through that glass ceiling will likely send a strong message to foreign and domestic investors that Japan no longer needs to be defined by - or be a product of - its past. This may also help stimulate the same animal spirits that saw Japan emerge as an economic powerhouse during the Meiji Restoration and again in the post-war period when the country grew to account for over 40% of the global developed market index. If stock markets are a leading indicator of an economy, these new highs augur well for what could come next.

This news was soon superseded by another inflexion point when Japan became the world’s last country to end its negative interest rate policy. The final trigger appeared to be unionised wage negotiations, which have resulted in the highest pay packet increase in 33 years of over 5%. A potentially trendsetting level in the world’s only country where wage growth had effectively stopped for 30 years! This was considered a prerequisite to achieving the Bank of Japan’s 2% target of domestic demand-led inflation.

Large caps remain the biggest beneficiary of this newfound enthusiasm towards Japan, extending their gains over small caps; with the MSCI Japan Large Cap index delivering 20% YTD relative to 13% for the MSCI Japan Small Cap index.

Performance

Toyo Tanso, Horiba and Lifenet were some of the strongest contributors to performance during the quarter. **Toyo Tanso**, which is a speciality maker of carbon products and has a leading global share in isotropic graphite used in renewable energy equipment and semiconductor manufacturing, was one of the biggest contributors to performance after releasing blockbuster earnings: despite recording a 30% climb in operating profits (OP) for the year, the company has guided for double-digit growth in OP thanks to a quadrupling of sales for Silicon Carbide semiconductor applications. **Horiba**, a leading measurement and analysis equipment, posted equally encouraging numbers thanks to strong auto and semiconductor-related demand. Finally, **Lifenet**, Japan’s only pure-play listed online life insurer, was lifted after announcing 77% increase in net income for the quarter as a result of a fall in covid-related claims and a pick up in the number of policies in force.

Detractors to performance include **Cosmos**, a leading Japanese discount drugstore which is seeing sustained margin pressure from its aggressive pricing strategies and higher personnel costs, and **Wealthnavi**, Japan’s leading digital robo wealth-management platform after it posted a slight slowdown in customer acquisitions during the quarter. **Megachips**, a fables

designer of chips used mainly in gaming consoles, was also weak after it cut guidance due to a game software inventory adjustment by its main customer, despite the fact that the negative impact will be largely offset by its ¥2bn buyback.

Notable transactions

During the quarter we took a new position in Inforich and participated in the IPO of Soracom.

Inforich is Japan’s largest provider of mobile device charging solutions, with over 40k ChargeSPOT stations strategically placed in high-traffic venues such as convenience stores and train stations. Although this network is already highly profitable the company is leveraging it for additional revenue streams, including advertising and facilitating sharing economy ventures, earning commissions. With significant operations and brand recognition in Hong Kong and several ASEAN countries, Inforich is aggressively pursuing international expansion which complements an attractive domestic opportunity.

Soracom is a global Internet of Things (IoT) Mobile Virtual Network Operator (MVNO) founded in 2014 by three ex-AWS engineers who currently serve as its CEO, COO and CTO. It enables companies to turn their “dumb” devices and equipment into IoT devices. Once plugged in, devices automatically connect to Soracom Cloud, and can then “talk” to each other and be remotely controlled, configured and monitored. Sales are growing rapidly as the company is expanding across a range of end markets globally and it is already profitable, with margins expected to continue rising from here given the very high marginal profitability of the business. Given these attractions, we decided to participate in the IPO and have taken a starter holding. These were funded from the complete sale of Open Door, an online travel comparison site operator that is now experiencing concerning levels of competition, and Outsourcing - a leading staffing company - and Snow Peak, a camping equipment brand, both of which are undergoing a management buyout.

Market Outlook

A reversal in current cyclical drivers could pose a significant problem to large parts of Japan’s market, especially for bigger blue chip companies, given many appear priced for a continuation of (what appear to be) peak earnings. Contrast that with Japan’s embryonic and entrepreneurial small caps, which now present two appealing characteristics: because they have been overlooked and ignored by the flood of foreign money coming into the country, they are now priced at little to no premium to the market (indeed this portfolio now trades closer to its benchmark on an EV/ EBIT basis than it has for almost ten years). Furthermore, many benefit from structural tailwinds which are accelerating on the back of demographics and wage inflation.

Stock Level Attribution

Top and Bottom Ten Contributors to Relative Performance

Quarter to 31 March 2024

Stock Name	Contribution (%)
Toyo Tanso	1.2
Lifenet Insurance	0.3
Horiba	0.3
GA technologies	0.3
Soracom	0.3
SWCC Corporation	0.3
Jade Group Inc	0.2
Nikkiso	0.1
Shift	0.1
Kamakura Shinsho	0.1
Cosmos Pharmaceutical	-0.7
Megachips	-0.7
GMO Financial Gate	-0.6
Bengo4.Com	-0.6
Wealthnavi	-0.6
Asahi Intecc	-0.6
Technopro Holdings	-0.5
Raksul	-0.5
I-ne Co	-0.5
eGuarantee	-0.5

One Year to 31 March 2024

Stock Name	Contribution (%)
Toyo Tanso	1.3
SWCC Corporation	0.6
Horiba	0.6
Jade Group Inc	0.5
Soracom	0.3
Lifenet Insurance	0.2
GA technologies	0.2
Taiyo Yuden	0.2
Noritsu Koki	0.2
Jeol	0.2
Open Door	-1.1
IRISO Electronics	-1.0
Cybozu	-1.0
Raksul	-1.0
I-ne Co	-1.0
Katitas	-0.9
Descente	-0.9
Litalico	-0.9
GMO Financial Gate	-0.9
Yonex	-0.9

Source: Revolution, MSCI. Baillie Gifford Japanese Smaller Companies Fund relative to MSCI Japan Small Cap Index (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 January 2024 to 31 March 2024.

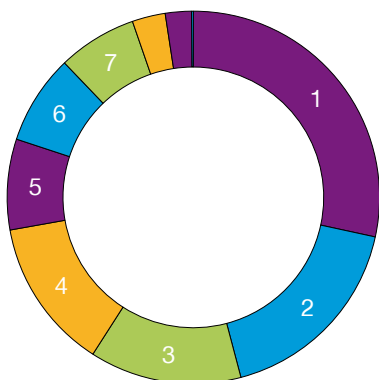
New Purchases

Stock Name	Transaction Rationale
Inforich Inc	<p>Inforich specialises in mobile device charging solutions, boasting over 40,000 ChargeSPOT stations throughout Japan, strategically placed in high-traffic venues such as convenience stores and train stations, ensuring exclusivity and competitive advantage. The company's charging service is experiencing robust growth and exceptional marginal profits. Dominating the Japanese market, Inforich surpasses its closest competitor by over tenfold. It leverages its network for additional revenue streams, including advertising and facilitating sharing economy ventures, earning commissions. With significant operations and brand recognition in Hong Kong and several ASEAN countries, Inforich is aggressively pursuing international expansion. The potential for growth, both domestically and abroad, coupled with rapidly increasing sales and profits, suggests the company's market valuation does not fully capture its prospects. We have therefore decided to take a starter holding.</p>
Soracom Inc	<p>Soracom is a global Internet of Things (IoT) Mobile Virtual Network Operator (MVNO) founded in 2014 by three ex-AWS engineers who currently serve as its CEO, COO and CTO. It enables companies to turn their "dumb" devices and equipment into IoT devices. It sells a range of hardware devices that enable IoT functionality in non-IoT devices. Once plugged in, devices automatically connect to Soracom Cloud, an in-house built IoT software stack running on AWS. Devices can then "talk" to each other and be remotely controlled, configured and monitored. Customers also get the ability to design and build customise applications using a suite of "drag and drop functions" provided by Soracom. Connectivity is provided through cellular networks, WiFi, Ethernet, and satellite networks. Soracom has longstanding network sharing agreements with over 300 carriers globally, making its services network agnostic, global and thereby providing a seamless service especially to clients with global operations. Sales are growing rapidly as the company is expanding across a range of end markets globally and it is already profitable, with margins expected to continue rising from here given the very high marginal profitability of the business. Given these attractions, we decided to participate in the IPO and have taken a starter holding.</p>

Complete Sales

Stock Name	Transaction Rationale
Freakout Holdings	Freakout is a technology company that provides tools to automate advertising for both advertisers/ brands and advertising media such as popular websites, blogs and social media platforms. The company was a pioneer in automating the ad buying process in Japan and we had hoped that the company would use its first mover advantage to become the de-facto provider of ad technology in Japan. Unfortunately, the online ad industry in Japan has become a lot more competitive and instead of focusing on their strengths and trying to dominate the domestic market, management have embarked on overseas expansion driven by an M&A spree. This has resulted in a few impairments in recent years with the only notable success being that of Playwire, a private US company that is strong in video advertising and analytics. Overall, we have become quite underwhelmed with the company's overall growth prospects and its future trajectory in terms of what it could look like on a 5+ year view and we therefore decided to sell our entire holding in the company.
Open Door Inc	Open Door runs "Travelko-chan", one of Japan's leading price comparison sites for domestic and international travel. The shares have understandably been very weak as both domestic and international travel in Japan remains in limbo due to the coronavirus. We have no visibility as to when both inbound and outbound travel in Japan might get back to normal. Additionally, Open Door is still a small company and doesn't necessarily have a strong balance sheet that could support it during the current crisis. Longer term, we think the area of online travel agents and aggregators is likely to get more competitive as barriers to entry are weak and there are already a couple of international players making inroads in Japan. All of this suggests to us that Open Door is likely to face a tough period over the next few years and is likely to struggle to grow its business. Given these concerns, we have decided to sell our entire holding in the company.
Outsourcing	Outsourcing is a leading staffing company. It is in the process of being acquired by Private Equity. We have sold our entire holding in the company and are recycling the proceeds elsewhere in the portfolio.
Snow Peak	Snow Peak is a high end camping equipment brand. It is in the process of being acquired by Private Equity. We have sold our entire holding in the company and are recycling the proceeds elsewhere in the portfolio.

Sector Exposure



	%	
1	Industrials	28.5
2	Information Technology	17.5
3	Financials	13.2
4	Consumer Discretionary	13.2
5	Communication Services	7.9
6	Health Care	7.8
7	Consumer Staples	6.9
8	Materials	2.9
9	Real Estate	2.3
10	Cash	-0.2

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
Toyo Tanso	Electronics company	3.7
Lifenet Insurance	Provides a range of life insurance products and services.	3.1
Cosmos Pharmaceutical	Drug store chain	2.9
WealthNavi	Operates a wealth management platform	2.7
Asahi Intecc	Specialist medical equipment	2.5
Nifco	Value-added plastic car parts	2.5
LITALICO	Educational Service provider	2.3
GMO Financial Gate	develops and manufactures transaction management systems	2.3
KATITAS	Real estate services	2.3
SIIX	Out-sources overseas production.	2.3
Total		26.6

Voting Activity

Votes Cast in Favour		Votes Cast Against		Votes Abstained/Withheld	
Companies	26	Companies	5	Companies	4
Resolutions	226	Resolutions	5	Resolutions	4

We published our Japan Strategy Stewardship Report available on our website

FCA has published its SDR regulation at the end of 2023 which will apply to UK-based investment funds and includes a new fund labelling framework and anti-greenwashing rule

The Environment, Social and Governance (ESG) Voting analysts are currently analysing the first 'mini' AGM season for companies with December year ends. The 'main' voting season will be later this year in June

Company Engagement

Engagement Type	Company
Environmental	Akatsuki Inc., CellSource Co., Ltd., JADE GROUP, Inc, Kitanotatsujin Corporation, Nikkiso Co., Ltd., Shoei Co., Ltd., SpiderPlus & Co., Weathernews Inc., eGuarantee, Inc., istyle Inc.
Governance	Akatsuki Inc., Asahi Intecc Co., Ltd., Avex Inc., CellSource Co., Ltd., Descente Ltd., ENECHANGE Innovation Limited, GA technologies Co., Ltd., HORIBA, Ltd., Infomart Corporation, JADE GROUP, Inc, KITZ Corporation, Lifenet Insurance Company, MonotaRO Co., Ltd., Nabtesco Corporation, Nifco Inc., Nikkiso Co., Ltd., OPTEX GROUP Company, Limited, OSG Corporation, Oisix ra daichi Inc., SHO-BOND Holdings Co., Ltd., SIIX Corporation, Shoei Co., Ltd., SpiderPlus & Co., WealthNavi Inc., Weathernews Inc., eGuarantee, Inc., oRo Co., Ltd.
Strategy	GA technologies 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 %
Toyo Tanso	3.7	CrowdWorks	1.0
Lifenet Insurance	3.1	oRo	1.0
Cosmos Pharmaceutical	2.9	Seria	1.0
WealthNavi	2.7	MonotaRO	0.8
Asahi Intecc	2.5	Nippon Ceramic	0.7
Nifco	2.5	PeptiDream	0.7
LITALICO	2.3	Shima Seiki Mfg.	0.7
GMO Financial Gate	2.3	istyle	0.6
KATITAS	2.3	CellSource	0.6
SIIX	2.3	ENECHANGE	0.6
GA Technologies	2.2	Anest Iwata	0.5
OSG	2.2	Demae-Can	0.5
Optex	2.1	Soracom Inc	0.5
Nakanishi	2.1	DaikyoNishikawa	0.5
Sho-Bond Holdings	2.1	Weathernews	0.5
MegaChips	2.0	Torex Semiconductor	0.4
Nikkiso	1.9	Nabtesco	0.4
JEOL	1.9	INFORICH	0.3
RakSul	1.9	WDB Holdings	0.2
eGuarantee	1.8	Akatsuki	0.1
Anicom	1.8	Kitanotatsujin	0.0
TechnoPro	1.8	M3	0.0
Horiba	1.8	Nihon M&A	0.0
Infomart	1.7	Cash	-0.2
MatsukiyoCocokara	1.7	Total	100.0
SWCC Corporation	1.6		
Harmonic Drive Systems	1.6		
Bengo4.com	1.6		
Nittoku	1.6		
KH Neochem	1.5		
Noritsu Koki	1.5		
Avex Inc.	1.5		
GMO Payment Gateway	1.5		
Yonex	1.4		
Kitz	1.4		
Descente	1.4		
Vector	1.4		
Shoei	1.4		
Tsugami	1.4		
Kumiai Chemical Industry	1.4		
Appier Group	1.4		
SpiderPlus	1.2		
Iriso Electronics	1.2		
Kohoku Kogyo	1.2		
I-ne	1.2		
Jade Group Inc	1.2		
Kamakura Shinsho	1.2		
Oisix	1.1		
Cybozu	1.1		

Please note the fund information contained within this document is proprietary information and should be maintained as such and not disseminated. The content is intended for information purposes only and should not be disclosed to other third parties or used for the purposes of market timing or seeking to gain an unfair advantage.

Share Class	Share Class Inception Date	ISIN	SEDOL	Annual Management Fee (%)	Ongoing Charge Figure (%)
Class B-Acc	02 September 1999	GB0006014921	0601492	0.60	0.64
Class B-Inc	01 April 1983	GB0006014582	0601458	0.60	0.64

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. The Ongoing Charges Figure ('OCF') may be lower than previous declarations as a result of a revision to how the indirect fees associated with closed-ended investment companies need to be shown. This does not necessarily mean that fund expenses have gone down rather that we have reverted to how they have been calculated until 30 June 2022 to reflect the revised Investment Association's Guidance on Disclosure of Fund Charges and Costs (July 2020, updated January 2022, revised November 2023). A more detailed Costs and Charges disclosure is available upon request.

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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 2024 and source is Baillie Gifford & Co unless otherwise stated.

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