



QUARTERLY OUTLOOK: TAILWIND OF STRUCTURAL CHANGE AND BENIGN GLOBAL GROWTH BACKDROP SUPPORT JAPANESE EQUITIES

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- Authorities have made progress in addressing the structural challenges facing the Japanese economy
- Companies are transforming business practices and improving governance standards, which is likely to lend valuation support to Japanese equities
- An environment of robust global growth should help the best of corporate Japan perform reasonably well

OVERCOMING POLICY INERTIA

While authorities in Japan have been slow to adopt pro-growth policies, the Shinzo Abe-led Liberal Democratic Party (LDP) has successfully broken the long-held tradition of policy inertia on this front. Key among these is attempting to deal with the economy's structural challenges: Corporate tax rates have been lowered, an enhanced corporate governance code has been implemented, while initiatives to encourage married women and foreign workers into the labour force have also been announced.

IMPROVING GOVERNANCE STANDARDS SUPPORT PROFIT GROWTH

The instance of companies defying the skeptics by transforming business practices and governance standards is growing. This should help to deliver profit growth and generate shareholder returns. The volume of shareholder buybacks is increasing, while merger and acquisition activity is slowly emerging.

Where implemented effectively, we expect transformational actions to be rewarded through higher valuations. We firmly believe that the valuation case for Japan still holds and that Japanese corporate earnings growth is likely to exceed global peers. This view underlies many of our preferred stock ideas today.

Our long-held view that the BoJ's policy decisions would weaken the yen over time has softened given the backdrop of an increasingly unpredictable currency outlook. We continue to believe the outlook for the currency is one of uncertainty and volatility.

FAVORABLE GLOBAL GROWTH BACKDROP FOR CORPORATE JAPAN

As well as market-specific drivers, the condition of the global economy remains a critical factor in terms of support for the Japanese equity market. On this point, our view is that we remain in an environment of robust global growth, which should help the best of corporate Japan to perform reasonably well. However, we are cognisant and concerned about the escalation of the trade war rhetoric that is coming from the world's largest trading partners.

We continue to hope that sanctions and trade war concerns will subside, but the quality bias within the portfolio should hold us in good stead, should trade wars jeopardise the supportive growth environment.

Increasing stock specific dispersion will need to be navigated in the near term as the market digests subtle changes in the top-down investment case and reacts to surprise and disappointment always inherent in Japan. Over the medium term, we remain upbeat, especially regarding those stocks central to Japan's evolution, and believe that investing in durable and improving businesses capable of weathering economic turbulence remains an advantaged approach to Japanese equity investing.

Key Risks - The following risks are materially relevant to the portfolio. Transactions in securities of foreign currencies may be subject to fluctuations of exchange rates which may affect the value of an investment. The fund is subject to the volatility inherent in equity investing, and its value may fluctuate more than a fund investing in income-oriented securities.

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