

Japan in Numbers

3%-25%
Wealth manager exposure

27.8%
Nikkei 225 return year-to-date

167.6%
Best performing fund: Legg Mason Japan Equity return over three years

21.64%
Nikkei 225 return Jan 2009 – December 2012

14.4%
Worst performing fund: GAM Star Japan Equity return over three years

What do wealth managers think of Japan's prospects?



Picture: PKOM / Shutterstock.com

Japan's equity markets have enjoyed a strong rally since the December 2012 election of Prime Minister Shinzo Abe and his announcement of a three-pronged package of measures aimed at stimulating the economy, dubbed 'Abenomics'.

The Nikkei 225 surged 46.21% to May on the back of the 'three arrows' plan. It includes a 2% inflation target and ¥10trn (US\$100bn) stimulus package which has successfully weakened the yen.

The market has since pulled back, leaving the Nikkei with a total 27.8% return year-to-date as investors question whether the government can follow through on the delivery of its third and most important arrow, which focuses on structural reform of the economy.

Annabelle Williams speaks to six wealth managers to see how Japanese equities fit into their clients' portfolios.

Japan Special Report

Guy Foster (top right) and Andrew Johnston (bottom right) Brewin Dolphin

Guy Foster, head of portfolio strategy at Brewin Dolphin, expects the government's monetary easing programme will continue to be successful in driving down the value of the yen.

He expects the currency to trade around ¥120/\$1 over a two-year period. While this will be supportive of the country's exporters, Foster pointed out if exports begin booming on a weakening yen, the currency could begin to appreciate.

"This is the chicken and egg situation... This is why policy is so important. It needs to generate inflation," he argued.

For balanced managed clients, Foster is recommending a 3.5% weighting to Japan, upped from zero which he had recommended for a long time. He said "general negativity" has caused him to cut an overweight to Asia and emerging markets in favour of a greater allocation to Japan.

Clients access Japan primarily through open-ended funds, although Brewins also uses an iShares sterling-hedged exchange-traded fund (ETF).

Fund favourites

Brewin Dolphin fund analyst Andrew Johnston explained preferred vehicles to access the region include the Melchior Japan Advantage fund, which he said is more cyclically positioned than others and has performed quite well.

"We have supported Melchior for a long time. They do not take huge bets against the benchmark and it is the only fund we recommend which is running a beta of one," Johnston said.

He also likes the Schroder Tokyo fund as he said investors have a safe pair of hands with manager Andrew Rose.

"It is a great fund if you want core exposure to the region with a slight value bias. He is a great manager on both the open- and closed-ended side," Johnston said.

The Jupiter Japan Income fund also features on Johnston's buy-list, even though the manager admits "it is a bit of an oxymoron looking for income in Japan".

"We feel these guys provide a decent level of income in a region not known for income. They manage the fund using a GARS (global absolute return strategy) process and do not take huge amounts of risk," he added



Stephen Peters Charles Stanley

Charles Stanley fund analyst Stephen Peters has always had a couple of Japan funds on his buy-list and rates JO Hambro Japan for its mid- and small-cap focus.

"Scott McGlashan and Ruth Nash are not trying to shoot the lights out but just deliver good, long-term performance," he said.

For a slightly different approach, Peters likes the Invesco Perpetual Japan fund as manager Paul Chesson has worked with Neil Woodford and follows a similar low price-to-book value style.

Peters highly rates the JP Morgan Japan investment trust which he said is a very core, stable performer that is not too volatile.

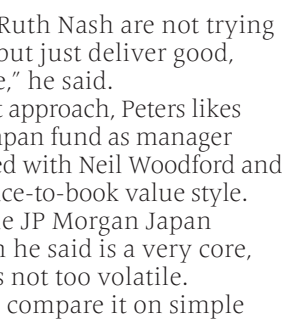
He explained: "If you compare it on simple performance terms to peers like the Baillie Gifford Japan trust then it looks like it has struggled. But in fairness to the manager, Nicholas Weindling, he is doing what he set out to do. He is running a large-cap portfolio, there is a bit of yield, it is the biggest trust in the market and it is on a 10% discount."

Lauren Charnley Redmayne-Bentley

Redmayne-Bentley stockbroker Lauren Charnley said exposure to Japan remains mixed, with some of the private client managers choosing to avoid the market altogether, and others holding positions they have had for years.

"Given the current choppiness of the market in Japan, it certainly will not be for all, and we prefer collectives to direct equities in order to mitigate risk. Favourites include Baillie Gifford Japanese and Legg Mason Japan Equity," she said.

The two funds have topped the IMA Japan sector over the last three years, with the Legg Mason fund returning a massive 167.6% and the Baillie Gifford vehicle coming in second place with a 57.8% return.



Colin McInnes Quartet Capital

Japan is the biggest equity position across all portfolios for Quartet Capital's managing partner Colin McInnes.

An average balanced or medium risk private client portfolio will have 40% in equities with 25% of that allocated to Japan.

McInnes moved to establish the position in the first quarter following the announcement of Abenomics. He funded the Japan call through profit taking on European equities, which were previously his biggest position.

"Our thesis is that huge stimulus would come to weaken the currency and exporters would become more competitive," McInnes said, although he added he is not hugely optimistic on the prospects of the government following through on all three arrows.

He explained: "I think they will be moderately successful. We do not view this as a fundamental change in Japan. When we established the position we took a view that it was going to be on a 12-month outlook."

Since this is a short-term tactical asset allocation call, McInnes has taken the passive route to access the market so clients are exposed via a currency-hedged Nikkei ETF "as it is an export-orientated index". Like many other wealth managers, McInnes lacks optimism over the state of other Asian markets and has zero exposure to the region.

Meena Lakshmanan Vestra Wealth

Co-head of investment solutions at Vestra Wealth, Meena Lakshmanan, has been very cautious on Japanese equities and had no exposure until the middle of June, so she missed the rally.

"This was based on our view of Japan's complex macroeconomic and demographic issues, alongside its ability to compete with the rest of Asia," she explained. However, she has since moved to cut Asian exposure and established positions in several active funds.

"Given the high level of risk in Japanese equities, we believe a sensible exposure is around 3%, which is still less than the world equities benchmark."

Five best performing funds

	1 year % chg
Legg Mason Japan Equity	67.44
Neptune Japan Opportunities	46.01
Invesco Perpetual Japan	39.95
GLG Japan CoreAlpha Retail	38.08
Baillie Gifford Japanese	35.03
Mean	27.53

Five worst performing funds

	1 year % chg
Aberdeen Global Japanese Equity	19.70
Fidelity Japan	19.38
Tiburon Taiko Unhgd	16.58
Schroder Japan Alpha Plus	13.84
Scottish Widows HIFML Japanese Focus	12.97

UK Registered Investment Funds (IMA) Japan. 10 August 2012 to 12 August 2013. Source: Morningstar.

FUND STATS How does your Japan fund measure up?

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