FUND PROFILE

RSMR

NIKKO ASSET MANAGEMENT

JAPAN VALUE FUND

October 2021

RSMR RATED FUND

OUR RESEARCH. YOUR SUCCESS

CONTENTS

FUND PROFILE – NIKKO AM JAPAN VALUE FUND

OUR FUND PROFILES provide an in-depth review of our leading rated funds and are designed to give advisers, paraplanners and analysts an ‘under the bonnet’ view of the fund. In providing more detailed commentary than a standard fund factsheet we believe our fund profiles set the standard for the next generation of research notes, aiding in fund selection and in meeting the ongoing suitability requirements expected by the FCA, and helping ensure firms deliver good client outcomes.

All of our rated funds are subject to rigorous and ongoing scrutiny on both a qualitative and quantitative basis. Our fund methodology is available for download from the RSMR Hub – www.rsmr.co.uk

The **Nikko AM Japan Value Fund** has been an RSMR rated fund since June 2021. There is a research driven approach, which although bottom-up focused, is macro aware. The investment philosophy of the value team is looking to deliver superior performance by making long-term investments in undervalued companies expected to undergo change. The team hope to make high returns in stocks by owning them through this period of market re-rating.

Graham O’Neill, Senior Investment Consultant, RSMR

Graham began his career in the investment industry over thirty years ago. After graduating from the University of Kent with a Degree in Economic Analysis, History and Policy, he joined London & Manchester, later joining Phillips Drew, then GRE as a UK based fund manager. He then moved to Abbey Life Ireland, where he held the position of CIO running their Managed and large Equity funds. Graham joined RSMR in 2010.

IA JAPAN

The Nikko AM Japan Value Fund is categorised within the IA Japan sector. Funds in this sector invest at least 80% of their assets in Japanese equities. The IA Japan sector contains over 90 funds available for investors and financial advisers to choose from, covering a large variety of investment strategies and styles, including active, passive, and enhanced index funds. A number of funds adopt style or market-cap based strategies including value and growth-biased themes, market-cap focused or multi-cap strategies. Funds that invest in a specialist theme must still meet the required geographic dispersion based on the relevant index.

The variations between the funds makes it difficult for an investor to compare them as different strategies will clearly perform differently depending on market conditions. It is important to recognise this when looking at both absolute and relative performance numbers for funds in the IA Japan sector, and this is particularly relevant for the Nikko AM Japan Value fund as relative performance can be volatile.

The coronavirus pandemic has been a headwind for the Japanese economy as vaccination take up was initially slower than other countries but is now catching up rapidly. This has led to a change in the leader of the country in Q3 2021, which in turn led to a return of confidence to markets with Japanese equities performing strongly in this period. However, the market reaction to the new prime minister has been more muted as he is not believed to be a leader who will drive reform and does not appear to have a clear vision for the country. Japan faces other headwinds including demographics, with a declining population, and stubborn levels of low inflation. The recent Olympic games were a sporting success but an economic disappointment. No foreign visitors and a lack of spectators meant a financial headache for the games' organisers.

In contrast to the 1990s, the Japanese stock market is now one of the more cheaply valued stock markets in the developed world. The country offers exposure to leading manufacturing and industrial companies across the globe and can provide strong diversification benefits for an investor's portfolio. Many of Japan's industrial companies are leaders in areas benefitting from technological change such as automation and green energy production such as hydrogen. While Japan will always be linked to the Asian region and its growth, recent problems in China could have a dampening effect on future growth prospects. That said, Japan is a global exporter with less reliance on the Asian region.

The Japanese yen has historically been a safe haven currency for investors during times of market uncertainty. This is a function of a net exporting economy with a large current account surplus, resulting in Japan being one of the largest creditor nations in the world. During times of market stress, there tends to be a repatriation of capital into Japanese assets. This can lead to a higher level of market cyclicality whereby a weakening yen tends to help export orientated sectors such as industrials linked to technological change. For value orientated strategies in Japan a weak yen is positive.

NIKKO ASSET MANAGEMENT

Nikko Asset Management (Nikko AM) are specialists in Asian equity and Asian fixed income investing. They are headquartered in Tokyo and have US$282bn in assets under management (as at 30.6.21) and $5.27 bn in the Japan Value Equity strategy. Nikko AM specialise in investment solutions with core strengths in Asia-centric strategies, capitalising on Asia's dynamic economies. They have an on-the-ground presence in China, Japan, Hong Kong, Singapore, and New Zealand and currently have 209 investment professionals. They also have offices in London, Edinburgh, Frankfurt, Luxembourg and New York.

Nikko AM was established over 60 years ago and is one of the largest independent asset management firms headquartered in Asia.

Nikko AM's teams have expertise in each sub-region and their investment approach does not rely on a house view and is based around each team having autonomy within a structure which they feel is best suited to tackle the range of market conditions and country specific differences. Each investment team has complete investment autonomy, but they have firm wide resources supporting this and the quality standards imposed are centralised so areas such as risk management, compliance, and client servicing all follow the same firm wide standards backed by the Group resource.

NIKKO AM JAPAN VALUE

Managers	Shigeru Aoyagi, Shinya Takada, Takaaki Harashima.
Structure	SICAV
IA Sector	Japan
Launched	February 2016
Fund Size	£153.7 million (as at 30th September 2021)

Fund Management Team

The Chief Portfolio Manager for this strategy is Shigeru Aoyagi who started his career with Nikko Securities in 1986 and joined the asset management side of the business in 1995. He has managed the Japan Value Strategy since inception and has been the leader of the team managing the strategy since 2010. Other Senior Portfolio Managers include Takaaki Harashima who started his career at Yamaichi Securities in 1996 and has been a portfolio manager and sector analyst at Nomura Asset Management and SG Yamaichi Asset Management (currently Amundi Japan) before joining Nikko AM in 2000 as a sector analyst, later becoming a value analyst, and then moving on to the portfolio management team of this strategy in 2005.

Shinya Takada is the other Senior Portfolio Manager. He started his career at Daiichi Life Insurance in 1996 and has worked at Asahi Life Asset Management and Meiji Dresdner on the asset management side, joining Nikko AM in 2004 as a sector analyst, later moving to the value analyst team, and has been a portfolio manager on the strategy since 2012.

In addition, there are three dedicated value analysts for this team:

Tatsuro Ochi joined Nikko AM at the start of 2015, and also serves as a portfolio manager on the value team.

Kozue Saito joined Nikko AM as a fixed income analyst in 2007 and subsequently became a value style analyst in 2011; she has also concurrently served as a proxy voting analyst since 2018.

Tatsuhiko Ikeda joined Nikko AM in 2014 and concurrently serves as a sector analyst covering Chemicals, Steel, Non-ferrous Metals, Trading Companies and Marine Transportation.

The dedicated value style analysts were introduced to the team in October 2004, partly in reaction to a significant increase in the number of companies listed on the Tokyo Stock Exchange First Section, which had been making coverage more challenging. Additionally, rather than relying solely on the research produced by sector analysts as well as his own research efforts, the manager felt that dedicated value style analysts would increase the team's capacity to closely research stocks in line with the value investment approach (seeking catalysts for structural change).

The value style analysts are complemented by an experienced team of ten sector analysts, who have an average of 20 years' industry experience and an average of 16 years' experience working with Nikko AM. In addition, there are three analysts and one group manager in Nikko AM's Active Ownership Group who specialise in proxy voting and in conducting governance meetings mainly with the smaller cap names currently held in Nikko AM's Japanese equity portfolios (both active and passive) which are not covered in the core research universe.

Fund Objectives & Targets

The 80 to 100 stock portfolio has a low turnover of 20-40% per annum, with an expected holding period of 3 to 5 years. The strategy aims to achieve outperformance versus the TOPIX Total Return Index of approximately 3% per annum relative to the benchmark over a 3–5-year period, with a tracking error of approximately 4%.

The investment philosophy of the value team is to look to deliver superior performance by making long-term investments in undervalued companies expected to undergo change. The team will aim to invest when they spot a catalyst for change rather than waiting to see if there is evidence of change occurring. The research seeks undervalued companies that offer goods and services that society needs which is a differentiating point with other value strategies. The approach is contrarian and focuses on undervalued companies likely to undergo transformation and the team hope to make high returns in stocks by owning them through this period of market re-rating. The Japanese economy is mature and as a result the overall stock market at the index level is highly cyclical. The team believe this allows seasoned investors to take advantage of repeated patterns. The team look to consistently apply a contrarian value-orientated investment approach to generate excess returns.

Examples of undervalued companies that are expected to undergo transformation include those in crisis mode where poor standing in the market compels management and employees to make fundamental changes, companies whose mind set is changing towards enhancing corporate value, and those with an attractive potential that has not been reflected in the market price or valuation.

Companies that offer goods and services needed by society would generally demonstrate business continuity, offer downside protection, and are likely to possess a turnaround catalyst even if they are temporarily undervalued. Research seeks to identify companies with these three attributes. The strategy is looking to achieve 3% outperformance p.a. relative to the benchmark, which is the TOPIX index of the largest 2,100 companies, with a tracking error of approximately 4% p.a. The portfolio is managed within a risk budget to keep the overall fund within this tracking error, and this helps to explain why sector deviations have not been huge. The portfolio has a strong value bias and is mid-cap orientated, with a market cap cut-off of roughly $500m with the team also taking into account the free float of the shares.

Investment Process

The team look to understand whether poor stock performance is due to structural or cyclical issues. They are looking for strong returns from stocks that are underperforming due to structural issues, but which possess a turnaround catalyst. These are described as Phase 1 stocks, which is a long-term cycle due to exogenous events or idiosyncratic structural issues and will typically last 3-5 years in a company. Companies in this phase have the potential to realise a significant turnaround. They will then start generating positive cash flow when moving into Phase 2 when underperformance may occur due to cyclical issues. The team are wary of avoiding value trap stocks on optically low valuations.

For the Phase 1 stocks there is a focus on the catalyst to turn the stock price around. This could be structural change due to a company's own efforts which is a supply side catalyst or self-help story. Alternatively, there could be a structural/environmental change in the market which would be a demand side catalyst. For either of these catalysts the question is asked 'does the company have products/services/human resources that are needed by the market to capture new demand?'. Japanese companies have always focused more on the environmental and social aspects of ESG as they believe all stakeholders need to participate. Phase 2 stocks are underperforming due to cyclical issues which could be the economic cycle in general, or the product life cycle the company faces so there is then an assessment of the type of cycle and the position within this. There can also be a delay between upfront investment and recovery cyclically depressing profitability and there can also be other cyclical factors unique to the company in terms of the business cycle of the sector in which it operates.

The premise of the approach is that in a mature economy, not just the market, but most individual companies will show cyclicality and this fund looks to take advantage of this cyclicality by buying low and selling high. It is contrarian and buys when valuations are depressed taking a 3–5-year view which seems to be the expected period for a company to show cyclical improvement. In fact, one of the sell disciplines is that if a company does not make any progress in terms of its operations over three years, the position is sold to avoid value traps. The first stage of the process is defining the potential investment universe where quantitative valuation measures including PE, PB and P/cash flow. There is then detailed qualitative bottom-up fundamental research and analysis. All listed stocks (approximately 3,700 names) are screened, and the fund focuses on roughly the bottom 50% of this universe, but also excludes companies with high credit risks, low liquidity with a typical market cap cut-off of $500m, together with other measures looking at free float. Poor governance risk stocks would also be excluded at this stage. This results in a value research universe of 600-700 names. With a 3–5-year investment horizon fund turnover is typically around 20-40%.

The ideas generated by the value team are Phase 1 stocks and the analysis looks to ascertain that there is business continuity, downside protection and the turnaround catalyst. Companies with a low valuation that offer goods and services that society needs tend to have these attributes so will be around for the longer term. The value team, including the analysts, spend their resources discovering these undervalued stocks that are still in Phase 1. The research process focuses on multiple layers of the company from senior management to employees as well as historic information. In addition to standard financial information the team look for factors which explain the poor stock performance and look to understand the financials and they also screen for any negative legacy issues such as lawsuits, or excess personnel, together with unfavourable non-financial information to ensure the company will continue to survive and there is limited downside in the name when an investment is made. The identification of the turnaround catalyst is then focused on, finding attractive non-financial information such as talented staff, a brand, or technology. To understand a company the value team meets senior management and employees, conducts site visits, and speaks to competitors. When analysing historical information, they look to find causal relationships and grasp changes. The research process produces a buy list of approximately 200 stocks.

As value investors the team like stocks that are out of favour, but there has to be potential for a turnaround which could be supply side driven, in other words self-help such as restructuring, or a change in the external environment. The team look to invest before the catalysts play out and look to anticipate positive change in a business. The fund will hold deep value stocks as it is investing before a turnaround is apparent and these fall into the Phase 1 category with very high expected returns. There is recognition that the risk with this investment process is holding value traps.

The reasons for undervaluation can be excess human resources, or too high a level of assets within the business, or that the market or company does not realise the net worth of the business or its potential. Many Japanese companies used to trade on conglomerate discounts some years ago, but this has now started to rectify itself as companies have carved out unprofitable businesses or bought in the shares of listed minorities. The levels of M&A in Japan have increased. When the team find a company trading below its book value, they will speak to the management to discuss ways to unlock the value. Sometimes the way technology is being used can unlock value as has been the case in companies with exposure to the hydrogen power sector. Kawasaki Heavy Industries restructured and focused on its growth areas, which included robotics and medical as well as hydrogen. These shares have risen by 70% since purchase, but the growth rate will continue to be strong, and in these circumstances, the team do not leave a turnaround story at an early stage.

Companies with huge NAV through cross shareholdings in other businesses have been a feature of the Japanese market, but whereas 30 years ago this was around 50% of companies, it has now fallen to around 14%.

Portfolio Construction

Phase 1 companies are initially identified by the value team and companies in Phase 2 may well be on the radar of the broader generalist sector analysts to monitor the portfolio holdings and who also support the growth, core, and dividend teams. These analysts provide a pooled resource to the fund management team as a whole.

There are no sector constraints on portfolio construction, but the risk tolerance requirements allow a maximum 4% tracking error and the usual UCITS rules apply, so a single stock holding cannot be more than 10% of the portfolio. Phase 1 stocks comprise 60-70% of the portfolio and these currently have a price to book of 0.99x and a dividend yield of 2.2%. Phase 2 stocks are 30-40% of the portfolio with a price to book of 2.0x and a dividend yield of 2.14%. The overall portfolio (at the time of writing) has a price to book of 1.15x and a dividend yield of 2.19%.

Sales can occur for a number of reasons, such as replacing a stock where the price target has been achieved, or if there is declining confidence in management or the business strategy. Stocks will also be reviewed and possibly sold if there is a deviation of the fundamental metrics from expectations (thesis not playing out). If the team lose faith in the quality of the management, the stock is sold. Last year Hitachi Metal was sold as the stock re-rated when there was a proposal to carve out the business and sell it to an investment fund. Honda subsidiary Keihin was trading on a PE of 10x and price to book of 0.7x when purchased. It was bought out by Honda in 2020 and delisted.

Two risk models are combined to evaluate portfolio risk. These are the Barra model and also a proprietary risk model which is used to complement this. The proprietary model is based on 18 factors and 33 sub factors using TSE classifications. Unsurprisingly, compared to the benchmark the fund exhibits value characteristics.

While the fund is bottom-up in construction, the portfolio managers do consider macro factors as they believe it would be foolish to ignore big picture issues. For example, today, long term interest rates appear to be rising which is beneficial for some value names and resulted in the fund increasing its weighting to banks in the spring of this year. Companies researched in Phase 2 will also benefit from the views of the sector analyst team. Each of the sector analysts meet with the portfolio manager once a month to discuss the latest views. At extremes the fund can hold higher levels of cash, and this occurred in February 2020 when there was concern about the spread of Covid-19 and the reinvestment of this after the market sell off helped to drive the strong performance seen last year, despite the fact that growth outperformed value overall. To avoid value traps, when investing in Phase 1, a company is generally given 1 to 3 years to show signs of improving prospects which is in line with the medium-term corporate plan for each business. Companies on the right track will be held onto for a number of years if it is felt there is significant upside in the shares. The fund management team do not want to sell out of turnaround stories too early.

ESG

Nikko AM has made ESG a central element of its management philosophy in order to implement its fiduciary principles and fulfil its stewardship responsibilities. ESG is seen as essential for putting fiduciary principles into practice. ESG is integrated into all investment decisions through the incorporation of Creating Shared Value (CSV) Evaluations which comprise 11 factors from three categories: competitiveness, ESG, and financial strength. ESG integration places ESG into investment decision making and ESG active ownership focuses on stewardship, voting rights, and engagement. CSV evaluations utilise the work of Harvard University Professor Michael Porter which states the creation of social value leads to economic value with comprehensive evaluation of a firm on competitiveness, ESG factors and financial strength. Nikko AM has used CSV evaluations since 2013, incorporating the ESG factors of diversity, management ability to execute, contribution to environment/society, and threats to business continuity. These are integrated with the original Porter's Five Forces of barriers to entry, threat of substitutes, bargaining power of customers, or suppliers and competitive rivalry together with financial strength evaluation looking at return to shareholders as part of this. Nikko AM looks to avoid investing in firms with government risk and promotes better governance through engagement. Since 2015 Nikko AM has avoided investing in firms with perceptible corporate governance risk. The analysts assess governance risk on an individual basis and work with governance specialists on engagement if issues arise. Nikko AM has received an A+ rating from its PRI assessment report scores. It is one of 43 Asian managers that have received this rating for the Strategy & Governance module in the 2020 assessment.

PAST & CURRENT POSITIONING/STRATEGY

Despite being a value strategy, the fund has broad sector exposure with the largest sector overweights being Industrials by 3.78% and Consumer Discretionary by 3.02%, whilst the largest sector underweights are Consumer Staples at 5.63% and Healthcare at 4.41%. Within IT there is a weighting of 11.76% versus 13.1% for the index, with 13 names held, but unsurprisingly the highest rated companies in this sector are not included in the fund (as at end September 2021) – even within growth orientated sectors there is more of a focus on what could be described as value names with a number of the IT stocks held yielding 4%. The Staples sector has performed well in the post crisis period, so the fund is underweight cosmetics, toiletries, and pharmaceutical companies. This has been the case for the last 10 years. Within the Healthcare sector the team look for companies with a pipeline of new drugs.

The largest holding in the fund is Sony, which might be surprising in a value fund, but this was added in 2011 when its price to book was 0.8x and the company had been followed since 1998. Nintendo was also bought when it had a depressed share price, but both the stocks have been held onto as the team still believe they trade at a discount to fair value. The team are looking to identify unloved companies that can then be held for 5-10 years and deliver strong returns over protracted time periods. Sony is believed to be operating a platform which is successfully connecting the different ‘pies’ in the global entertainment industry and should continue to generate strong earnings. Trading on a PE of 15x it is still cheap

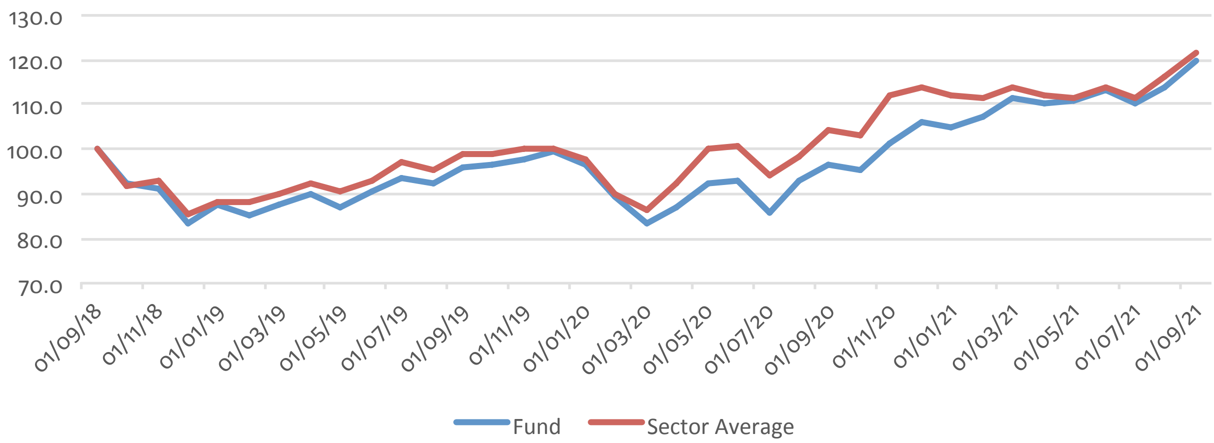
Nintendo was purchased in 2013 when the cash on its books was nearly all of the market capitalisation, with the team recognising that console games and software were in a dynamic growth phase. When the stock was purchased, it was on a price to book of only 1.2x with the shares now up 6x since the original purchase. The company still only trades on a PE of 16x and a dividend yield of 3%. The team are looking for companies which have not just turnaround potential, but also compounding potential after this.

One of the differentiating features of the strategy is that in addition to the more typical analyst team who work on a generalist basis for different style strategies within Nikko AM, there are also three dedicated analysts working solely on the value strategy. These value analysts carry out the due diligence work on stocks thrown up by the screening process looking for change that will act as a catalyst for improving the use of assets, creating/maintaining capital efficiency, and increasing future earnings, all of which could lead to a re-valuation of the share price. The analysts and portfolio managers on the team work together, looking at a company’s context within the industry as well as the potential for self-help, such as the more effective use of tangible and intangible assets. The value analysts pay attention to the prospects for balance sheet or cash flow improvements but take into account the quality of goods and services and employee confidence/satisfaction as part of the analysis. Whilst screening highlights stocks on a low valuation, the analyst role is to look for factors that will support a firm’s recovery with the team then visiting companies to assess management strengths, capabilities, and commitment to change. Corporate contact provides an opportunity to make a subjective judgement as to whether management is likely to realise objectives. Even when sector analysts come up with recommendations and ideas, the value analysts on the team do their own due diligence work before a stock is included in the portfolio. The views on individual sectors are updated on a monthly basis and are provided by the sector analyst team to the portfolio managers, together with updates from their own company visits and discussions with sell side analysts. There is also input from the strategists at Nikko AM to identify new trends in the marketplace.

The key difference between the value style analysts working for the team, and the sector analysts working for the wider asset management business is that the value analysts focus their research on structural changes. The value analysts will often have a longer investment horizon as very often ideas take time to work and the three analysts work as generalists across all sectors.

PERFORMANCE

Fund vs IA Sector Average



The fund has established strong performance numbers, outperforming the TOPIX Total Return Index of the 2,100 leading companies in Japan over 1 year, 3 years, and 5 years, which is especially credible for a value strategy. The performance numbers are highly credible against other value strategies in the marketplace.

From the fund launch on 1st February 2016 to 31st December 2016 there was a return in yen of 6.11% from the TOPIX with the gains occurring after Trump's election win in November, with stocks having moved sideways for much of the year before this. There was the expectation that the Trump administration would bring expansionary fiscal policy and tax cuts and this led to rising long term interest rates and a depreciation of the yen. This was a favourable back drop for the value orientated approach and the fund rose by 11.09% which also saw outperformance of the value index over this period. Both sector allocation and stock selection added to performance. High positively contributing actively weighted names included: Nintendo the video game maker, electronics company Sony, toy maker Tomy, and chemical company Mitsubishi Gas Chemical.

In 2017 the TOPIX rose 22.23% with the latter part of the year the most beneficial for equity investors as Japanese companies delivered strong corporate earnings and globally markets were encouraged by plans for US tax cuts. The fund outperformed by over 3% during the period despite the large cap value index underperforming the growth index. Both sector allocation and stock selection benefitted the portfolio and strong contributors included Nintendo, Sony, together with carbon manufacturer Tokai Carbon and electronic component manufacturer Minebea Mitsumi.

2018 was a difficult one for the Japanese market which declined by close to 16% in yen terms, hit by deteriorating US-China relations and concerns in the latter part of the year about an economic slowdown, with December in particular being a poor month where a lack of liquidity saw a market decline of over 10%. The fund underperformed its benchmark by just over 3%, although there was little difference between value and growth stocks in 2018 looking at style factors. Small caps severely underperformed in 2018. Sector allocation was a negative over the year. At the stock level top contributors included Sony, Tokai Carbon, and communications testing equipment maker Anritsu.

In 2019 the TOPIX returned 18.1% in yen terms, rebounding from its previous year's losses with the better performance occurring in the second half of the year with investors encouraged by progress in US-China trade talks. During 2019 the fund outperformed by over 5% despite value stocks lagging growth names as during 2019 US Treasury bond yields declined sharply providing a difficult backdrop for most value strategies. However, for the portfolio, sector allocation and stock selection were positive. Top contributors included Nintendo, Sony, Anritsu, and glass fibre maker Nitto Boseki.

In 2020 the TOPIX in yen terms rose 7.4% having suffered a decline in the first quarter of the year of approximately 17.5% as the pandemic hit and oil prices fell sharply. From April stocks rebounded over 30% to the year-end encouraged by central bank monetary policy support and government fiscal stimulus measures across the globe. The fund underperformed its benchmark by 1.3% with its investment style providing a serious headwind with the large cap value index underperforming the growth index close to 30% during a period when long term interest rates continued to decline. Sector allocation was negative. Positively contributing stocks included Nintendo, Sony, electronic component maker Ibiden and publisher Kadokawa.

To end-July 2021 the TOPIX rose 6.5% in yen terms with positive risk appetite and upgrading of economic forecasts seeing strong performance for value names, especially in the first quarter. The fund outperformed its benchmark YTD by over 7% with large cap value strongly outperforming large cap growth during this period. In Japan in 2021 to date value has performed better in relative terms versus growth stocks than in other developed markets. During the period both sector allocation and stock selection were positive with top company contributions from Mitsui OSK Lines the shipping company, outdoor equipment clothing maker Snow Peak, and electronics conglomerate Hitachi.

SUMMARY & EVALUATION

The fund is managed by a dedicated value team of six including desk analysts, with research augmented by the 10 strong sector analyst team at the firm who serve a number of differing strategies. Nikko AM themselves manage $125bn in Japanese equities, making them a significant investor in the market with over $5bn in the value strategy. There is a research driven approach, which although bottom-up focused, is macro aware, and the returns in a period where there has only been really one year of significant value outperformance are highly credible, indicating the fund has avoided value traps. As an example, the team waited until this year when there was clear upward pressure on bond yields to increase exposure to the banking sector, recognising that the macro environment in much of the post GFC period was challenging for bank stocks.

Within the top holdings there are a number of names such as Sony, Nintendo, and Kubota, which are typically seen in more growth orientated strategies with the difference being that this team bought the stocks when they were on depressed valuations but they are clearly happy to let them run on in the portfolio whilst the re-rating and earnings upgrade story is intact, and the valuation remains modest for the expected future growth. This does seem to be a differentiating point compared to many value strategies which, when turnarounds have been invested in, have seen the fund managers exit at too early a stage. The research process benefits from a dedicated analytical team on the strategy, and Nikko AM's strong foothold in the market, which in 2019 saw close to 4,000 one-on-one company management contacts. There are other differentiating features within this value approach, one of which is a focus on companies which realise that they need to change to survive, and also on businesses whose products are ones that society has a need for. This seems to have allowed the team to avoid companies seeing structural or secular declines in the product or service they offer, and the lead fund manager for the strategy Shigeru Aoyagi has been involved in investment markets for over 30 years so has seen many different cycles.

This is a value orientated strategy, so unsurprisingly the best periods of performance have been when economies are re-bounding post-recession, such as in 2003-2006, or when Japan is pursuing policies to significantly boost domestic demand such as when Abenomics was first introduced. The fund also did well in the second half of 2016 and 2017 when global synchronised growth was relatively strong and similarly in the 2021 post Covid-19 recovery period. The strategy is most likely to struggle when market valuations on cheaper stocks within the market deteriorate or are under pressure, and this would usually coincide with periods when the discount rate applied to future corporate earnings is declining. A world of gently rising bond yields and inflation expectations is likely to be the most benign macro backdrop for the strategy. The fund managers have proved they do not need a true value market backdrop to deliver outperformance, but it would be true that those conditions are likely to suit the strategy best. The excellent long-term record of the strategy, the experience of the lead fund manager, backed up by the team dedicated research resource, and the wider research resource of Nikko AM in Japan equities fully justify an RSMR rating for the fund which is suitable as a core holding in portfolios.

RSMR

Established in 2004 RSMR provides research and analysis to firms working across the UK's personal financial services marketplace.

Our work is completed with total impartiality, without any conflict of interest and delivered to a high professional standard by a team of experienced and highly qualified people.

Working with advisers

We provide specialist research, analysis and support to a diverse range of financial advisers and planners helping them to deliver sound advice to their clients, backed by rigorous and structured research and due diligence.

The main regulatory body in the UK, the FCA, states that personal recommendations made by advisers should be 'based on a comprehensive and fair analysis of the relevant market' and this has led to closer scrutiny of the whole advice process. Our solutions are designed to help advisers meet these challenges whilst recognising that advisory firms require a range of flexible options that best meet their own business needs and those of their clients.

Working with providers

We work with all the leading fund groups, life and pension companies and platform operators across the financial services sector offering straight forward and pragmatic advice to help add value and improve their business performance and efficiency whilst treating customers fairly in line with FCA requirements.

Ratings

Our innovative ratings are now recognised as market leading and cover a broad area of investment solutions including single strategy funds, SRI funds, Multimanager and multi-asset funds, DFMs and investment trusts. Our familiar 'R' logo is now recognised as a trusted badge of quality by advisers and providers alike and a 'must-have' when selecting funds. Our ratings are founded on a strict methodology that considers performance and risk measures but places a greater emphasis on the ability of fund managers to continue to deliver performance in the years ahead. based on our in-depth face-to-face meetings with fund managers across the globe.

We understand financial services and we will work alongside you to deliver tailored solutions that are right for your clients and your business.

Our research. Your success.

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