



Inside Japan: Reasons for Optimism

Will Investors See Japan in a New Light?

After more than two decades, Japan finally looks to have turned the corner. **The country's economic, geopolitical and 'soft power' is rising again, placing Corporate Japan on an upward trajectory that could sustain for the rest of the decade and beyond.** Here's why long-term investors should start scrubbing off their perceptions of Japan.



A Future-Proofed Economy

Demographic-driven innovations

An ageing population and low birth rates have spurred innovations in industries such as factory automation, robotics, and healthcare utilising Big Data, Internet of Things and Artificial Intelligence. With corporate profits continuing their strong upward trend, Japan is poised to be the guiding light as other developed economies confront similar demographic concerns in the near future.



Vital conduit to Asia's growth – a bridge between East and West

Japan is the world's 4th largest exporter. It occupies a unique place globally, serving as a bridge between east and west, and between developing and emerging markets. Close to **60% of Japan's exports are within the Asia Pacific region¹**, the most common destinations being China, South Korea, Chinese Taipei and Hong Kong. Developing Asian economies depend on Japanese technology as well as shared supply chains for economic progress.

¹ Source: Observatory of Economic Complexity (OEC), August 2022

² Source: Bloomberg, November 2022

Political, economic and social stability

Political stability has brought about economic recovery, in particular, stability of the Japanese economy. **The Nikkei 225 Index's stock average has returned to the 20,000 mark in May 2020²**, and both employment rates and consumption taxes have increased. Japan's greatest strength, however, is its social stability, resilience and discipline; they make Japan one of the most stable countries in the developed world.

Game changer in green energy

Long-term global shift towards a decarbonised, more sustainable society presents exponential growth opportunities for Japanese companies already at the forefront of clean-energy solutions, especially in hydrogen and battery technologies. **5 out of 10 companies worldwide dominating decarbonising technologies are Japanese.**

World-leading clean-energy companies

- TOYOTA MOTOR (JAPAN)
- GENERAL ELECTRIC (US)
- MITSUBISHI HEAVY INDUSTRIES (JAPAN)
- SIEMENS (GERMANY)
- HYUNDAI MOTOR (SOUTH KOREA)
- HITACHI (JAPAN)
- TOSHIBA (JAPAN)
- EXXONMOBIL (US)
- HONDA MOTOR (JAPAN)
- HONEYWELL INTERNATIONAL (US)



5 out of 10 are Japanese

Source: "Japanese companies leading decarbonising technologies", Nikkei, Astamuse, 5 November 2021

Key Investment Drivers

Improved corporate governance

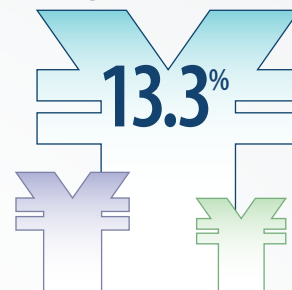
A Corporate Governance Code took effect in 2015 to enforce greater transparency and responsiveness to shareholders.

In 2022, the Tokyo Stock Exchange also restructured its company guidelines into 3 listing categories: Prime, Standard and Growth. To maintain their top-tier Prime listing, companies will be required to have at least one-third of their boards comprised of independent outside directors, including females and non-Japanese professionals. There will also be **mandated disclosures on sustainability and ESG.** Such reforms are geared to make **Japanese equities more competitive globally and result in higher Return on Equity (ROE).**

Corporate profits on strong upward trend

Corporate Japan is enjoying 20-year bull market profit margins. Income declared by companies in Japan that closed the books in fiscal 2021 to March 2022 **grew 13.3% from the previous year to a record 79,479 billion yen³**, according to the National Tax Agency, as reported on 31 October 2022.

Corporate Profits



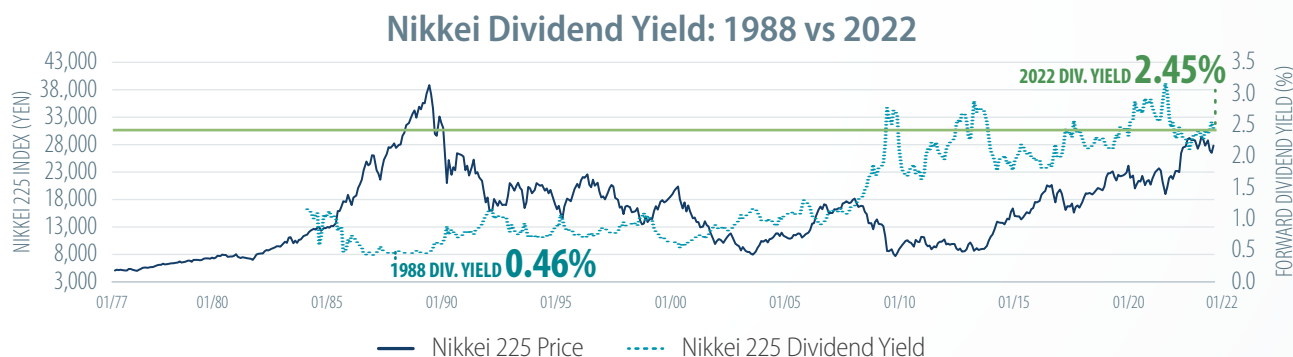
³ Source: "Japan Corporate Income Hits Record 79.4 Trillion Yen", anippon.com, 31 October 2022

Greater dividend prospects

The dividend yield of the Nikkei shows how shareholder expectations have evolved. Back in 1988, when overseas investment into Japan was at its peak, the Nikkei's dividend yield was a modest 0.46%, as Japanese companies placed little importance on dividends at the time, and valuations were stretched.

In 2022, the Nikkei dividend yield has risen to a much more favourable 2.45%⁴. Japanese stocks are sitting on significant excess cash levels, which may leave room for further shareholder returns.

⁴ Source: Mizuho Securities, based on data by Nihon Keizai Shimbun and Toyo Keizai, 31 March 2022



Source: Mizuho Securities, based on data by Nihon Keizai Shimbun and Toyo Keizai, 31 March 2022. Past performance is not necessarily indicative of future performance.

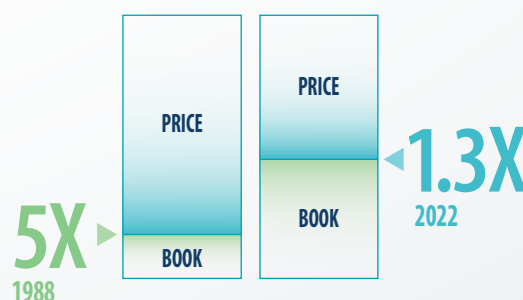
Forward dividend yield is an estimation of a year's dividend expressed as a percentage of the current stock price. Forward dividend yields are generally used in circumstances where the yield is predictable based on past instances which in this case applies to the stocks under Nikkei 225.

Undervalued share prices

The rebound in long-overlooked value stocks has also just begun, with the cycle at the early stages of its value-supportive phase. **Nikkei's price-to-book (P/B) ratio is now at just 1.3X** compared to the 5X reached in 1988, indicating share prices are close to book value and far from overvalued.

Source: Mizuho Securities, based on data by Nihon Keizai Shimbun and Toyo Keizai, 31 March 2022

Nikkei Price/Book Ratio: 1988 vs 2022



Is it Finally Time to Invest in Japan?

Macro-level changes and a stable political environment, as well as significant policy and structural reform initiatives are shaping future economic growth of Japan. Combined with attractive valuations and their strength as a vital conduit to Asia, Japanese corporations may be one of the best long-term plays to unlock hidden opportunities.



After overcoming many difficulties, I believe Japan has finally reached the light at the end of the tunnel.

As an asset manager, nothing would be more satisfying than to see investors view Japan as a valuable presence within their portfolios that enables them to greatly capture growth opportunities across the wider Asia Pacific region.

Shigeru Aoyagi, Nikko Asset Management Team Leader and Portfolio Manager, Japan Value Strategy



Our Japan Funds

Nikko AM Shenton Japan Fund

Nikko AM Japan Dividend Equity Fund

Key risks of investing in the Japan Funds

The value of the funds and its distributions (if any) may rise or fall. The following are key risk factors that may cause you to lose some or all of your investment:

- Market and credit risks
- Liquidity risks
- Product-specific risks

You should be aware that your investment in any of the funds may be exposed to other risks of an exceptional nature from time to time. Please refer to the respective fund prospectus and product highlights sheet for further information on risks of the funds.

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