



15 February 2023

Closed End Investments



Source: Refinitiv

Market data

EPIC/TKR	FJV
Price (p)	176.3
12m high (p)	191.0
12m low (p)	143.0
Shares (m)	129.5
Mkt cap (£m)	227
NAV (14Feb'23, p)	189.4
Discount to NAV	-7%
Country/Ccy	UK/GBP
Market	STMM

Description

Fidelity Japan Trust (FJV) aims to achieve long-term capital growth by investing predominantly in equities and their related securities of Japanese companies.

Company information

Chairman	David Graham
Senior Ind. Dir.	Sarah MacAulay
Chr. Audit Cttee.	David Barron
NEDs	Dominic Ziegler, Myra Chan
Portfolio Managers	Nicholas Price (lead), Cenk Simsek (asst.)
Contact	FIL-FidelityInvestmentTrusts@fil.com

investment-trusts.fidelity.co.uk/fidelity-japan-trust

Key shareholders (Dec'22)

Fidelity Platform/HL/II	19.7%
Lazard AM	17.2%
City of London IM	11.5%
Allspring Global Inv.	8.3%
Wesleyan Assurance	4.0%
Brewin Dolphin	3.4%
Canaccord Genuity WM	3.3%

Diary

Mid-Feb	Jan monthly factsheet
---------	-----------------------

Analyst

Mark Thomas +44 (0)203 693 7075
mt@hardmanandco.com

FIDELITY JAPAN TRUST PLC

Favourable G7 2023 economic outlook for Japan

The *January 2023 IMF World Economic Outlook update* has reiterated, once again, the relative appeal of Japan compared with the other major developed economies. In particular, the IMF is forecasting faster 2023 economic growth for Japan. Central banks expect lower CPI, and, as a result, one may expect less pressure to raise interest rates. We have repeatedly emphasised how FJV adds value through its stock selection (and our last note, *Opportunities from the mother of invention*, highlighted how above-average innovation in Japan was an advantage to this), but a positive relative economic environment also provides following tailwinds, and helps investor sentiment.

- ▶ **Economic outlook:** The IMF's *January World Economic Outlook update* was again favourable for Japan, showing faster real GDP growth in 2023 (at 1.8%, more than twice the G7 average of 0.8%). Inflation expectations are less than half the advanced economies' average, and interest rates, while rising, are a fraction of peer levels.
- ▶ **FJV's unique value add:** FJV's approach is "growth at a reasonable price". Companies growing because of innovation have a natural fit to the first element. FJV's long, local presence gives it advantages over global investors, while its deep, global analytical reach is a competitive advantage over smaller, national ones.
- ▶ **Valuation:** 92% of investments are listed in active markets. While some may have a degree of illiquidity, the NAV is "real". The discount of 7% is above the average of recent levels, but it is slightly above that of its peers, whom FJV has materially outperformed over five years. FJV is run for capital growth.
- ▶ **Risks:** FJV has seen periods of short-term underperformance, when its investment style has been out of favour – typically, when the market has undergone a sharp factor rotation – but recovery has usually been swift. 2022 performance may affect sentiment for a while. There are also some Japan sentiment issues.
- ▶ **Investment summary:** FJV has outperformed its peers, benchmarks and UK indices, with a distinctive and active investment approach. Its companies show faster-than-average EBITDA growth (2023E ca.1.3x and 2024E 1.8x the market), and have higher RoEs and RoICs (both around one third above the market). It invests for "growth at a reasonable price" (GARP) – so company valuations are usually higher. With an active approach, investors are buying FJV's investment process, not its portfolio on a given day. Japan offers tech-enabled growth and structural reforms, and it is levered to global trade. Its approach can be out of favour, but, under the manager's tenure, underperformance periods have been short.

Financial summary and valuation

Year-end Dec (£000)	2018	2019	2020	2021	2022E	2023E
Gains/losses on fin. inst. FV	(27,452)	52,982	38,535	847	(90,336)	20,843
Gains/losses on derivatives	(6,873)	14,155	22,360	5,521	14,012	14,012
Income	2,795	2,906	3,287	3,476	3,530	2,657
Investment manager fees	(1,843)	(1,226)	(2,035)	(2,877)	(2,154)	(1,621)
Profit/(loss) bef. fin. costs & taxn.	(33,858)	68,233	61,067	5,801	(75,594)	35,233
Investments	185,987	249,099	303,002	307,738	231,594	266,379
Cash	0	1,196	4,336	4,741	4,741	4,741
NAV (£m)*	188	252	309	313	237	271
NAV per share (£)	1.39	1.90	2.37	2.41	1.82	2.09
S/P prem./disc. (-) to NAV	-9%	-7%	-7%	-5%	-10%	-16%

*2018-22 NAV on year-end s/p, 2023E NAV on current s/p; Source: Hardman & Co Research

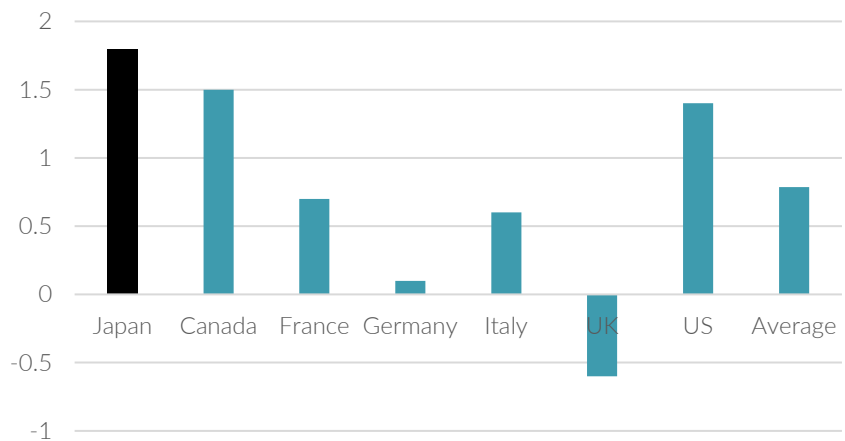
Japanese economic outlook

Real GDP

Faster real GDP growth expected in 2023...

The chart below shows the relative real GDP outlook for Japan compared with the major developed economies. As can be seen, Japan's near-term outlook is for better growth than that of these peers.

IMF G7 2023 real GDP growth projections (%)



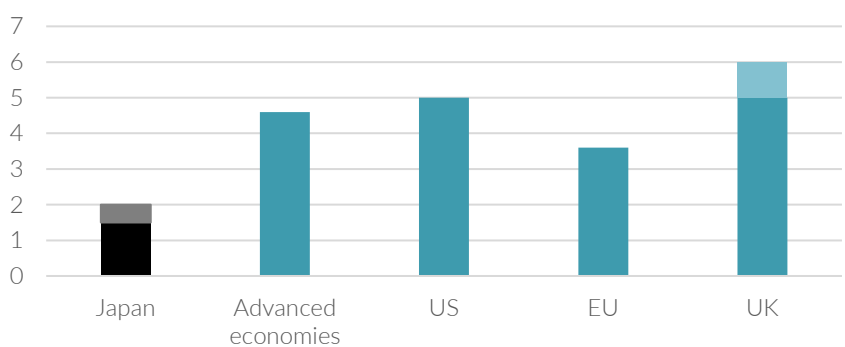
Source: January 2023 IMF World Economic Outlook, Hardman & Co Research

CPI

...combined with lower inflation...

The *January 2023 Bank of Japan outlook* forecasts end-2023 inflation in the range of 1.5%-2.0%. This compares with US expectations, collated by the New York Federal Reserve, of ca.5%¹, and ECB EU projections of 3.6%². Lower inflation introduces lower macroeconomic risk.

IMF G7 2023 CPI projections (%)



Source: Bank of Japan, January 2023 IMF World Economic Outlook, New York Federal Reserve, ECB, Bank of England, Hardman & Co Research

¹ <https://www.newyorkfed.org/newsevents/news/research/2023/20230109>

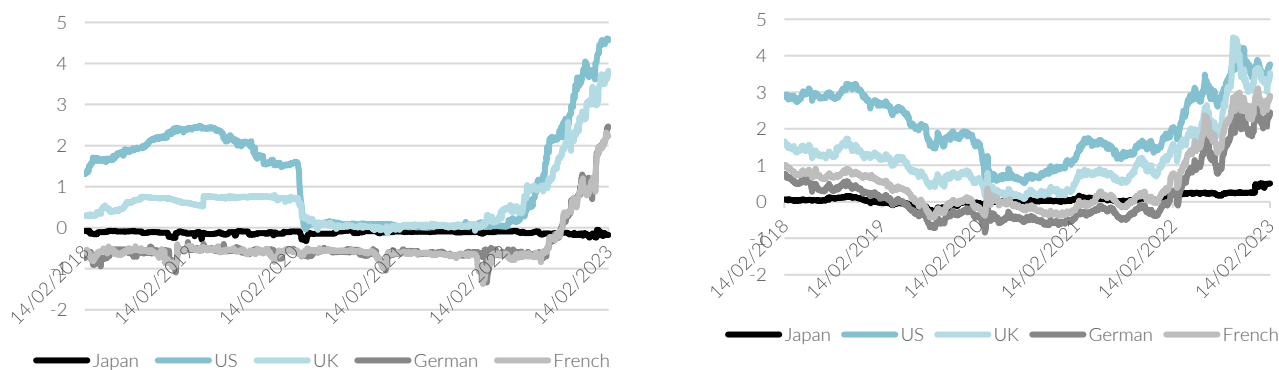
² <https://www.ecb.europa.eu/pub/projections/html/index.en.html#:~:text=Inflation%20will%20remain%20high%20in,the%20second%20half%20of%202025>

Interest rate environment favourable

...and lower interest rates

As a consequence of the economic outlook, Japan's interest rate outlook is also much more favourable, as shown in the charts below. It is not facing the short-term economic impact of rising rates, nor the incremental strain on government finances, especially from rising long-term rates.

Benchmark government one-month (left-hand chart) and 10-year (right-hand chart) redemption yields (%)



Source Refinitiv, Hardman & Co Research

Manager's outlook

On 6 December 2022, the manager, Nicholas Price, published his review, entitled *Outlook is bright for Japan*. The key points were:

- ▶ “Pent-up demand among both consumers and businesses will continue to underpin growth, and we have started to see a pickup in the number of inbound tourists taking advantage of the weak yen.
- ▶ While we continue to find a lot of ideas among mid/small caps, we are also seeing attractive opportunities in the unlisted sector.
- ▶ By working closely with our sustainable investing team and maintaining an active dialogue with investee companies, we aim to continually improve the sustainability of their businesses, which should also enhance their performance as investments.

With the global economic outlook darkening, Japan is an outlier – showing a degree of resilience as Covid-19 restrictions ease and the economy finally reopens. Unlike many other countries, the economic policies of the Japanese government and central bank are a positive mix of fiscal expansion and monetary easing”.

How FJV takes the opportunity

Value in stock selection

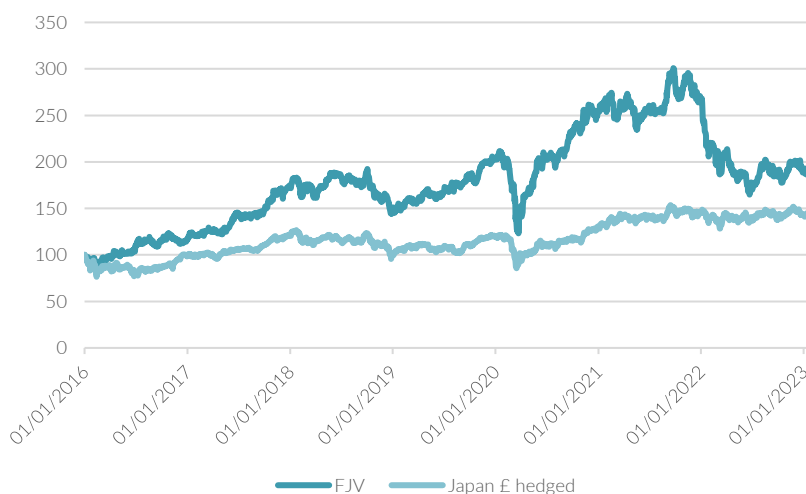
FJV is about stock selection...

...not a macro call

Proof of pudding is long-term outperformance against Japanese market

The manager was appointed to the Trust on 1 September 2015, and the chart below shows the Trust's performance against the Japanese market since 1 January 2016. Despite the style headwinds in 2022, there has been considerable long-term outperformance during the manager's tenure. We have emphasised before that FJV's approach is "growth at a reasonable price" (GARP) and finding the right companies, rather than playing the macro economy in Japan. A positive relative economic environment thus provides a following tailwind, and helps investor sentiment, rather than being the core investment thesis.

Total return for FJV and Japanese market, indexed to 1 January 2016 at 100



Source: Refinitiv, Hardman & Co Research

FJV's competitive advantages

Long local presence gives advantage over global players

FJV's competitive advantages in investing in innovative companies are exactly the same as for any other investments it makes in Japan, and derive from the investment process that we outlined in [our initiation](#). In particular, we highlight:

- ▶ A large team of ca.20 on the ground, including senior managers, who typically have over 20 years of experience, and analysts, each with typically 10 years of experience. This local footprint gives insights that are not available to every global investor.
- ▶ The manager advises that he typically conducts ca.350 company meetings each year (this rose to more than 400 during the pandemic, with remote-working practices improving efficiency), again giving a practical insight that is not available to many.

Fidelity Japan Trust plc

Access to Fidelity's global network gives advantage over national investors

- ▶ Access to Fidelity's global research capability, which means that local companies can be put into a much wider perspective than many smaller national investors are able to achieve.

Research gives advantage in under-researched market

- ▶ Investment horizon on three to five years, with a focus on quality management teams, above-average earnings growth and RoE (in this market, typically 10%+), in order to buy GARP companies, companies that are not distressed, cheap companies, or pure growth or momentum plays.
- ▶ Japan remains an under-researched market, with, as we highlighted in our initiation, more than 1,000 small- and mid-cap names with no analyst coverage at all, and 2,000 with fewer than five analysts, which is more than Europe and the UK combined.

Modest holdings in unlisted businesses, with intent to grow this area

3.6% added to NAV when one investment IPO-ed in March 2021

Capturing value in unlisted investments

A specific approach is to use FJV's flexible mandate to capture more of the value chain by investing in unlisted investments. Again, this is a longstanding approach, with, for example, the [2019 report and accounts](#) (page 7) including the commentary "We continue to look for early-stage ideas, particularly among fast-growing services and internet-based companies, as well as innovative medtech names". In the [2021 report and accounts](#) (page 6), the comment was "we are seeing a lot more entrepreneurial activity in Japan compared with five to ten years ago...Being on the ground in Japan, and seeing many different companies, means that we are well-placed to help entrepreneurs in the latter stages of their pre-IPO journey". FJV has been successful in the past – for example, with the online consumer-to-consumer platform, Coconala, listing on the Tokyo Stock Exchange on 19 March 2021, and its valuation in the portfolio increasing by 351%, growing FJV's NAV by 3.6%.

Recent increase in cap on unlisted investments

Unlisted investments are an area of increasing interest for the manager. When we initiated on FJV in the summer of 2021, it was 2% of NAV; it is now 8%. At the May 2022 AGM, the investment policy was changed to allow the maximum holding in unlisted investments to be increased from 10% to 20%.

Globally, companies staying private for longer, with more of the value chain being kept in private hands

The reasons for this increased interest in unlisted investments are:

- ▶ Globally, companies are staying private for longer. Technology companies, on average, are staying private for an extra two to three years, compared with a decade ago, and the average IPO valuation is, consequently, significantly larger. Amazon's market capitalisation at IPO was a mere \$438m in 1997, while Facebook (2012) and Uber (2019) IPO-ed with market caps of ca.\$104bn and ca.\$82bn, respectively. More of the value chain is being captured in the private stage of company ownership.

FJV's track record means it is being approached more often

- ▶ FJV's success in this area has led to it being approached by more unlisted companies in its target market.

Focus on late-stage, pre-IPO supportive investor, not venture capital or PE investor

The mandate aims for companies that are close to IPO, rather than earlier-stage, unlisted investments. FJV's role with these companies is to be a supportive financial investor; it is not aiming to adopt a more active, private equity (PE)-style approach. It is not looking to manage the businesses – rather just be an investor in them.

Portfolio

Underweight and overweight positions

Top five overweight positions account for 25.8% of FJV's portfolio, top five underweights zero

The table below is a summary of the key underweight and overweight stocks in FJV's portfolio. The top five overweight positions account for 25.8% of FJV's total net assets, against a 1.5% index weighting. The top five underweight positions have a zero weighting in the portfolio, against an 11.5% index weighting.

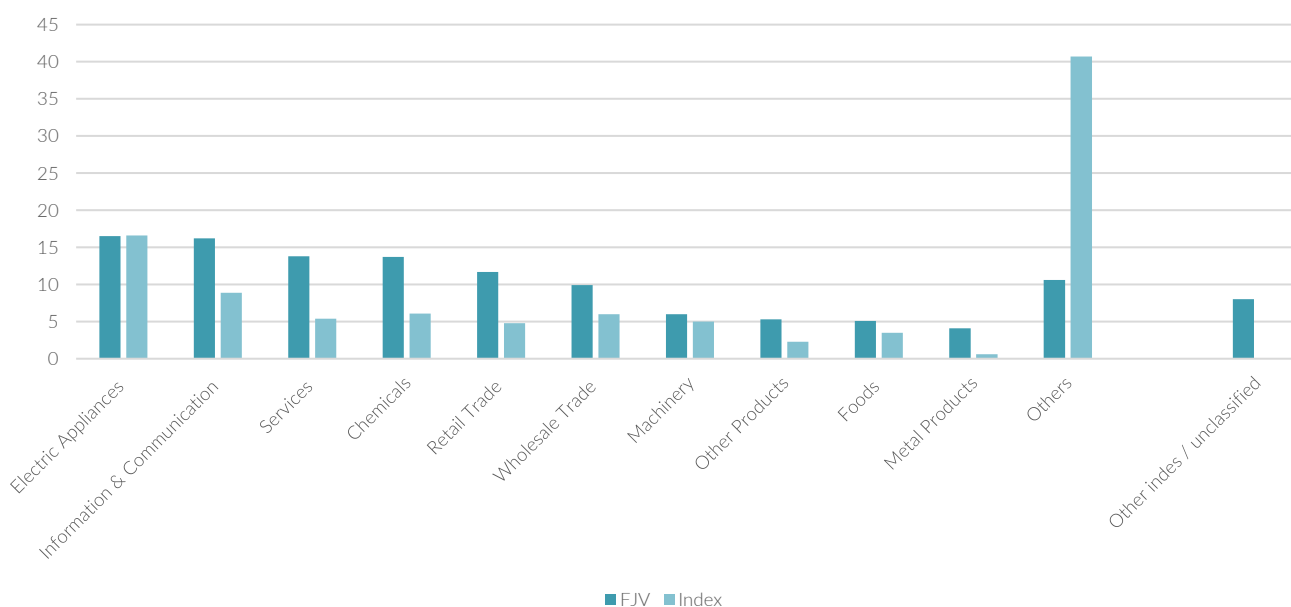
Top overweight and underweight positions (% total net assets)			
Position	FJV	Index	FJV vs. Index
Overweight			
NOF Corp (chemicals)	6.8	0.1	6.9
Misumi Group Inc (wholesale trade)	6.0	0.2	5.9
Ryohin Keikaku Co (retail)	4.6	0.1	4.5
Tokyo Electron (electric appliances)	5.2	1.0	4.2
Rinnai Corp (metal products)	3.2	0.1	3.2
Underweight			
Toyota Motor Corp (motor)	0.0	3.7	-3.7
Sony (electronics)	0.0	2.6	-2.6
Mitsubishi UFJ Fin Group (financials)	0.0	2.0	-2.0
Nippon Teleg and Tel (telecoms)	0.0	1.8	-1.8
Sumitomo Mitsui Finan Group (financials)	0.0	1.4	-1.4

Source: December 2022 Factsheet, Hardman & Co Research

Sector exposure

At end-December 2022, FJV's key exposures were overweightings in information and communication, services, chemicals, retail and wholesale trade.

FJV's sectoral mix (as % of total net assets), December 2022

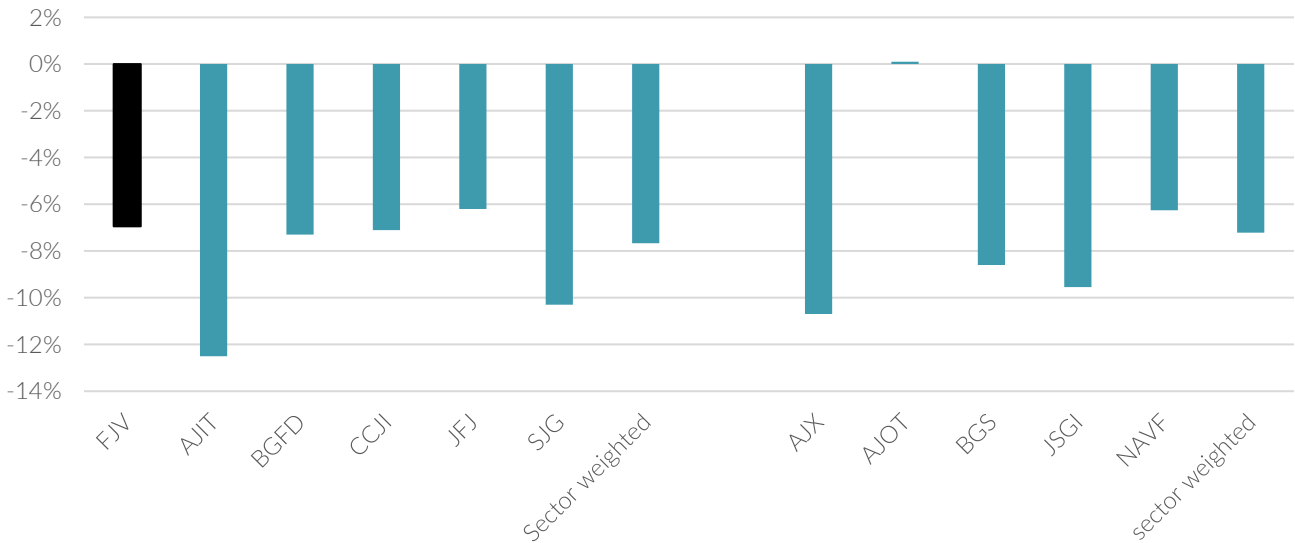


Source: FJV December 2022 Factsheet, Hardman & Co Research

Valuation

As can be seen in the chart below, FJV's discount to NAV is broadly in line with the average of its peers, and the average for Japanese smaller companies.

Discounts to NAV of Japanese companies and Japanese smaller companies (%)

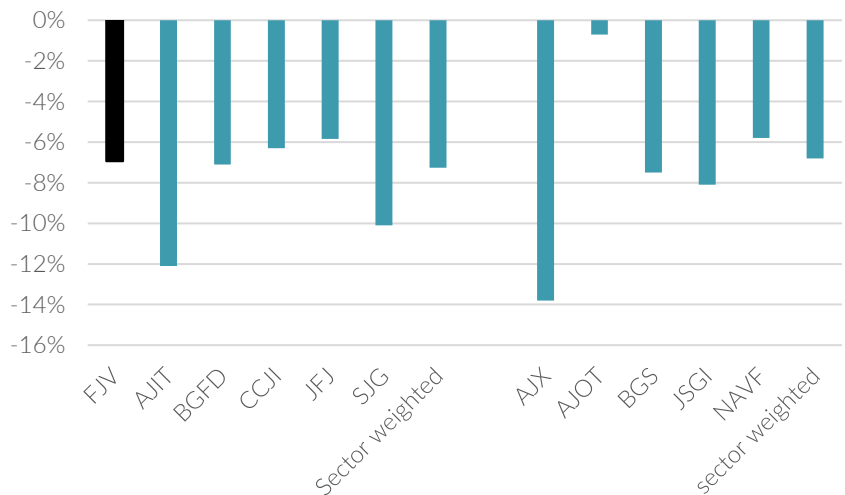


Source: LSE, priced on 14 February 2023, Hardman & Co Research

Current discount above five-year average

From the chart below, we can see that, since the end of 2017, FJV has generally traded at a mid-digit to high-single-digit discount to NAV.

FJV's historical discount to NAV, 2010 to date



Source: FJV Report and Accounts, NAV announcement, priced on 14 February 2023, LSE, Hardman & Co Research

Financials

We have assumed that 2023 will be a “normal” year after the travails of 2022. Historically, after a period of underperformance, there has been a sharp relative recovery, but we have not built this into our estimates.

Income statement (£000)									
Year-end Dec	2021			2022E			2023E		
	Revenue	Capital	Total	Revenue	Capital	Total	Revenue	Capital	Total
Gains/losses on investments	0	847	847		(90,336)	(90,336)		20,843	20,843
Gains/losses on derivatives	0	5,521	5,521		14,012	14,012		14,012	14,012
Income	3,476		3,476	3,530		3,530	2,657		2,657
Investment manager fees	(448)	(2,429)	(2,877)	(379)	(1,775)	(2,154)	(285)	(1,336)	(1,621)
Other expenses	(620)	(13)	(633)	(632)	(13)	(645)	(645)	(13)	(658)
Foreign exchange gains/losses	0	(533)	(533)		0	0		0	0
Profit/(loss) bef. finance costs & taxation	2,408	3,393	5,801	2,519	(78,113)	(75,594)	1,726	33,507	35,233
Finance costs	(35)	(138)	(173)	(35)	(138)	(173)	(35)	(138)	(173)
Profit/(loss) before taxation	2,373	3,255	5,628	2,484	(78,251)	(75,767)	1,691	33,369	35,060
Taxation	(278)	0	(278)	(275)		(275)	(275)		(275)
Profit/(loss) after taxation for the year	2,095	3,255	5,350	2,209	(78,251)	(76,042)	1,416	33,369	34,785
Earnings/(loss) per ordinary share (p)	1.61	2.50	4.12	1.70	(60.19)	(58.49)	1.09	25.67	26.76

Source: FJV Report and Accounts, Hardman & Co Research

Balance sheet (£000)									
@ 31 Dec	2016	2017	2018	2019	2020	2021	2022E	2023E	
Investments	161,777	221,792	185,987	249,099	303,002	307,738	231,594	266,379	
Current assets									
Derivative instruments	4,619	1,123	269	3,048	1,932	1,006	1,006	1,006	
Other receivables	534	652	3,263	899	668	525	525	525	
Amounts held at futures clearing houses and brokers	0	0	7,611	0	21	0	0	0	
Cash and cash equivalents	620	908	0	1,196	4,336	4,741	4,741	4,741	
Total current assets	5,773	2,683	11,143	5,143	6,957	6,272	6,273	6,273	
Total assets	167,550	224,475	197,130	254,242	309,959	314,010	237,867	272,652	
Current liabilities									
Derivative instruments	(424)	(456)	(6,529)	(1,075)	(91)	(717)	(717)	(717)	
Bank loans	0	0	(1,718)	0	0	(11)	-	-	
Other payables	(721)	(1,492)	(1,353)	(676)	(1,062)	(629)	(629)	(629)	
Total current liabilities	(1,145)	(1,948)	(9,600)	(1,751)	(1,153)	(1,357)	(1,346)	(1,346)	
Net current assets	166,405	222,527	187,530	252,491	308,806	312,653	236,521	271,306	
Net assets	166,405	222,527	187,530	252,491	308,806	312,653	236,521	271,306	
NAV per share (£)	1.22	1.64	1.39	1.90	2.37	2.41	1.82	2.09	

Source: FJV Report and Accounts, Hardman & Co Research

Disclaimer

Hardman & Co provides professional independent research services and all information used in the publication of this report has been compiled from publicly available sources that are believed to be reliable. However, no guarantee, warranty or representation, express or implied, can be given by Hardman & Co as to the accuracy, adequacy or completeness of the information contained in this research and they are not responsible for any errors or omissions or results obtained from use of such information. Neither Hardman & Co, nor any affiliates, officers, directors or employees accept any liability or responsibility in respect of the information which is subject to change without notice and may only be correct at the stated date of their issue, except in the case of gross negligence, fraud or wilful misconduct. In no event will Hardman & Co, its affiliates or any such parties be liable to you for any direct, special, indirect, consequential, incidental damages or any other damages of any kind even if Hardman & Co has been advised of the possibility thereof.

This research has been prepared purely for information purposes, and nothing in this report should be construed as an offer, or the solicitation of an offer, to buy or sell any security, product, service or investment. The research reflects the objective views of the analyst(s) named on the front page and does not constitute investment advice. However, the companies or legal entities covered in this research may pay us a fixed fee in order for this research to be made available. A full list of companies or legal entities that have paid us for coverage within the past 12 months can be viewed at <http://www.hardmanandco.com/legals/research-disclosures>. Hardman may provide other investment banking services to the companies or legal entities mentioned in this report.

Hardman & Co has a personal dealing policy which restricts staff and consultants' dealing in shares, bonds or other related instruments of companies or legal entities which pay Hardman & Co for any services, including research. No Hardman & Co staff, consultants or officers are employed or engaged by the companies or legal entities covered by this document in any capacity other than through Hardman & Co.

Hardman & Co does not buy or sell shares, either for their own account or for other parties and neither do they undertake investment business. We may provide investment banking services to corporate clients. Hardman & Co does not make recommendations. Accordingly, they do not publish records of their past recommendations. Where a Fair Value price is given in a research note, such as a DCF or peer comparison, this is the theoretical result of a study of a range of possible outcomes, and not a forecast of a likely share price. Hardman & Co may publish further notes on these securities, companies and legal entities but has no scheduled commitment and may cease to follow these securities, companies and legal entities without notice.

The information provided in this document is not intended for distribution to, or use by, any person or entity in any jurisdiction or country where such distribution or use would be contrary to law or regulation or which would subject Hardman & Co or its affiliates to any registration requirement within such jurisdiction or country.

Some or all alternative investments may not be suitable for certain investors. Investments in small and mid-cap corporations and foreign entities are speculative and involve a high degree of risk. An investor could lose all or a substantial amount of his or her investment. Investments may be leveraged and performance may be volatile; they may have high fees and expenses that reduce returns. Securities or legal entities mentioned in this document may not be suitable or appropriate for all investors. Where this document refers to a particular tax treatment, the tax treatment will depend on each investor's particular circumstances and may be subject to future change. Each investor's particular needs, investment objectives and financial situation were not taken into account in the preparation of this document and the material contained herein. Each investor must make his or her own independent decisions and obtain their own independent advice regarding any information, projects, securities, tax treatment or financial instruments mentioned herein. The fact that Hardman & Co has made available through this document various information constitutes neither a recommendation to enter into a particular transaction nor a representation that any financial instrument is suitable or appropriate for you. Each investor should consider whether an investment strategy of the purchase or sale of any product or security is appropriate for them in the light of their investment needs, objectives and financial circumstances.

This document constitutes a 'financial promotion' for the purposes of section 21 Financial Services and Markets Act 2000 (United Kingdom) ('FSMA') and accordingly has been approved by Capital Markets Strategy Ltd which is authorised and regulated by the Financial Conduct Authority (FCA).

No part of this document may be reproduced, stored in a retrieval system or transmitted in any form or by any means, mechanical, photocopying, recording or otherwise, without prior permission from Hardman & Co. By accepting this document, the recipient agrees to be bound by the limitations set out in this notice. This notice shall be governed and construed in accordance with English law. Hardman Research Ltd, trading as Hardman & Co, is an appointed representative of Capital Markets Strategy Ltd and is authorised and regulated by the FCA under registration number 600843. Hardman Research Ltd is registered at Companies House with number 8256259.

(Disclaimer Version 8 – Effective from August 2018)

Status of Hardman & Co's research under MiFID II

Some professional investors, who are subject to the new MiFID II rules from 3rd January 2018, may be unclear about the status of Hardman & Co research and, specifically, whether it can be accepted without a commercial arrangement. Hardman & Co's research is paid for by the companies, legal entities and issuers about which we write and, as such, falls within the scope of 'minor non-monetary benefits', as defined in the Markets in Financial Instruments Directive II.

In particular, Article 12(3) of the Directive states: 'The following benefits shall qualify as acceptable minor non-monetary benefits only if they are: (b) 'written material from a third party that is commissioned and paid for by a corporate issuer or potential issuer to promote a new issuance by the company, or where the third party firm is contractually engaged and paid by the issuer to produce such material on an ongoing basis, provided that the relationship is clearly disclosed in the material and that the material is made available at the same time to any investment firms wishing to receive it or to the general public...'

The fact that Hardman & Co is commissioned to write the research is disclosed in the disclaimer, and the research is widely available.

The full detail is on page 26 of the full directive, which can be accessed here: <https://ec.europa.eu/transparency/regdoc/rep/3/2016/EN/3-2016-2031-EN-F1-1.PDF>

In addition, it should be noted that MiFID II's main aim is to ensure transparency in the relationship between fund managers and brokers/suppliers, and eliminate what is termed 'inducement', whereby free research is provided to fund managers to encourage them to deal with the broker. Hardman & Co is not inducing the reader of our research to trade through us, since we do not deal in any security or legal entity.

