


# Eastspring Investments – Japan Dynamic Fund

eastspring  
investments

A Prudential plc company 

## Market review

The MSCI Japan Index rose 8.5% in January. In addition to macro tailwinds from the US, and the weak yen, in Japan the Tokyo Stock Exchange (TSE) released on January 15 its list of companies that are trading below book but which have announced concrete action plans to improve ROE. This shines a light on the many companies that have yet to respond.

## Key contributors

Month-to-date, Nomura Holdings, Honda Motor, and Sumitomo Mitsui Financial Group were the key absolute contributors to the Fund's performance.

Nomura Holdings share price jumped higher on the back of improved profitability and the recently announced share buybacks. Market's short-term focus did not recognize company's restructuring efforts both overseas and domestically, as well as its strong domestic position within Japan's capital markets. We have tested our valuation for sensitivity to a range of potential outcomes and find strong valuation support.

Honda's share price performed strongly in January as earnings have improved alongside production and sales recoveries. We observe that Honda has begun to benefit from an improving model mix and capacity control in its auto business. Honda's motorcycle business in emerging markets also continues to deliver strong margins as the company has been able to build scale and market position. In addition, Honda appears well positioned in technology transition, both in terms of its internal capabilities as well as with building alliances with others. Our conservative trend margin assumptions suggest there remains significant valuation support, which more than compensates for the observed risks and the fund's patient investment time frame.

Sumitomo Mitsui Financial Group's (SMFG) share price outperformed in January owing to renewed expectations for normalization of monetary policy in Japan. The company has managed well its balance sheet by shedding non-core assets and creating room for elevated returns to shareholders and investments abroad. On top of capital management, the company has also showed stringent cost management. SMFG has a diversified income stream with meaningful exposure and leading positioning in consumer finance and credit card businesses. It has also been focused on improving the profitability of its loan book through mix improvement. The company is moving to the offence by investing in its businesses in Asia.

## Key detractors

Month-to-date, Izumi, Nabtesco and Sundrug were key absolute detractors for the Fund.

Izumi underperformed the market in January as the company reported lower Operating Profit in its 3Q FY2/24 results, mainly attributable to costs on strategic renovations outlays. These could improve Izumi's competitiveness in trend terms. Izumi is a Japan-based company mainly engaged in the general retail business. The Company operates through two main business segments. The Retail segment is engaged in the sale of clothing, housing-related goods and food products through its shopping centers, general merchandise stores (GMSs) and supermarkets. The Retail-related segment is engaged in the credit and finance business, the management of shop facilities, as well as the operation of restaurants.

Nabtesco is a small but well-run company with solid market positions in precision reduction gears for industrial robots and good management, trading at substantial discount to its valuations. Market sentiment on the stock is affected by the fear of recession and China's economy decline but these concerns seem cyclical. The company outperformed the market in December owing to the positive expectations on robotics production improvement.

Sundrug's share price fell may have been underpinned by the weaker than expected retail sales number reported in January, despite rising consumer confidence. Sundrug operates and manages drug stores and dispensing pharmacies in Japan. As a result of our deep fundamental analysis and after applying conservative assumptions, the team has found that Sundrug trades at significant valuation discount to its fair value.

## Fund activity

During the month, the portfolio manager sold shares in companies where valuations look relatively less compelling and bought shares in companies where valuations look relatively attracted compared to other high conviction positions. Notable top-ups was Resona Holdings while positions in Nomura Holdings, Sumco, Credit Saison, NEC, Honda Motor, Daito Trust Construction, and Sumitomo Mitsui Financial were trimmed.

## Strategy and outlook

Although Japanese equities have had a phenomenally strong year 2023, we believe that the long-term structural drivers of deflation, reforms and reallocation remain in place and corporate earnings can continue to improve over the coming years. Firstly, inflation appears to be becoming more entrenched and this is allowing companies to increase their pricing, benefiting margins. The labour market is also tighter than it has been in many years placing upward pressure on wages. This is key for a sustained move out of the deflationary era and we think this is the best chance Japan has had in a generation to do so. Secondly, the Tokyo Stock Exchange initiative and ongoing corporate governance reforms are positive for the value end of the Japanese equity market, where there is larger potential to improve Return-on-Equity and see a corresponding valuation re-rating. We expect the trend of share buybacks to continue in 2024 as more companies address the excess cash on their balance sheets and we are encouraged by corporate management teams' willingness to cut costs, restructure underperforming business units and unwind extensive cross shareholdings. Lastly, the capex environment appears to be improving, driven by the trends of re-shoring, friend-shoring and the green transition.

**Sector attribution (one month)**

Sector (%)	Average weights			Effects		
	Fund	Benchmark	Relative	Allocation	Selection	Total
FINANCIALS	14.0	12.3	1.7	0.06	0.20	0.27
TECHNOLOGY	19.8	22.0	-2.1	0.03	0.07	0.10
TELECOMMUNICATIONS	-	4.6	-4.6	0.04	-	0.04
DEFENSIVE	14.7	15.7	-0.9	0.03	-0.04	-0.01
DOMESTIC	15.2	13.4	1.8	-0.07	-0.12	-0.18
AUTOS	9.7	10.5	-0.8	-0.04	-0.33	-0.37
INDUSTRIALS	9.5	8.9	0.7	0.00	-0.38	-0.37
GLOBAL BASICS	16.3	12.7	3.6	0.04	-1.04	-1.00
CASH AND EQUIVALENTS	0.8	-	0.8	-0.08	0.01	-0.07
<b>Total</b>	<b>100.0</b>	<b>100.0</b>	<b>-</b>	<b>0.03</b>	<b>-1.63</b>	<b>-1.60</b>

**Top 10 absolute contributors (one month)**

Holdings (%)	Average weights		Contribution to fund performance
	Fund	Benchmark	
NOMURA HOLDINGS INC	3.3	0.4	0.66
HONDA MOTOR CO LTD	4.1	1.3	0.57
SUMITOMO MITSUI FINANCIAL GROUP	4.2	1.7	0.49
FURUKAWA ELECTRIC CO LTD	2.2	-	0.45
TAKEDA PHARMACEUTICAL CO LTD	5.7	1.3	0.43
RICOH CO LTD	5.5	0.1	0.42
RESONA HOLDINGS INC	2.3	0.3	0.33
TAISEI CORP	2.5	0.2	0.28
SUMITOMO HEAVY INDUSTRIES	2.8	-	0.24
NEC CORP	1.5	0.4	0.23
<b>Total</b>	<b>34.0</b>	<b>5.7</b>	<b>4.09</b>

**Top 10 absolute detractors (one month)**

Holdings (%)	Average weights		Contribution to fund performance
	Fund	Benchmark	
IZUMI CO LTD	1.0	-	-0.04
NABTESCO CORP	2.4	-	-0.02
SUNDRUG CO LTD	1.0	-	-0.02
SOHGO SECURITY SERVICES CO	1.4	-	-0.01
<b>Total</b>	<b>5.7</b>	<b>-</b>	<b>-0.08</b>

**Top 10 absolute contributors (year to date)**

Holdings (%)	Average weights		Contribution to fund performance
	Fund	Benchmark	
NOMURA HOLDINGS INC	3.3	0.4	0.66
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**Statistics**

Characteristics	Fund	Benchmark
Number of holdings	39	225
Price to earnings (number of times)	16.8	18.2
Price to book (number of times)	0.9	1.6
Forward 12-month dividend yield (%)	3.1	2.3
Active share (%)	89.6	N/A
Tracking error (%)	6.2	N/A

**Additional notes**

1. The securities include all share classes if applicable.
2. Due to rounding, numbers presented may not add up precisely to the totals indicated and percentages may not reflect the absolute figures for the same reason. The information provided herein are subject to change the discretion of the Investment Manager without prior notice.
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**Facilities Agent for European Economic Area:**

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**Representative Agent:** First Independent Fund Services Ltd, Klausstrasse 33, 8008 Zurich

**Paying Agent:** NPB-New Private Bank Ltd, Limmatquai 1/am Bellevue, 8024 Zurich

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