LIONTRUST

GLOBAL EQUITY

Liontrust Japan Equity Fund

Q3 2022 review

Fund manager: Chris Taylor

The Liontrust Japan Equity Fund returned 1.2% in over the third quarter, against the 1.1% return from the TOPIX Index comparator benchmark and the 2.2% average return in the IA Japan sector , also a comparator benchmark*.

In the third quarter, small and mid-cap stocks performed well, with the TSE Small Cap, TSE Mothers and TSE Growth indices rising 1.4%, 5.1% and 4.7% respectively. This masked an even stronger performance of c.15% until August, after which these indices were hard hit by escalating discount rates, with both actual interest rate and the uncertainty components rising.

Larger-cap firms were weaker, suffering from expectations of a global slowdown and failing to reap the normal benefit form a weaker yen against the US dollar. TOPIX started the period at the 1,870 level before enduring a seesaw quarter. It rallied to just over 2,000 on 17th August, as investors began to appreciate that the fallout from the Ukraine/Russia war was likely to not be as bad as initially expected. Thereafter, the Index fell to the 1,835 level by quarter-end on the likelihood of accelerating interest rate hikes due to inflation being more persistent, whilst the positive benefits of a weaker yen upon corporate profits was ignored.

As expected, the LDP maintained its "supermajority" in parliament after Sunday 3rd July's Upper House election contest and saw policies remain almost unchanged, with only the likely restart of nuclear reactors and repeal of Article 9 of the constitution being enacted. Beyond that, the April 2023 expiry of the current Bank of Japan's Governor's term will see Kuroda probably replaced and a new 10-year benchmark bond target yield of 0.50% put in place versus the current 0.25% level.

In terms of performance, the Fund's equity portfolio suffered from its lack of exposure to the classic defensive sectors like consumer staples and healthcare, which fared relatively well while the Fund's industrial holdings moved in line with the market. By contrast, the Fund's returns were held back by its allocation to the more cyclical sectors such as materials and consumer discretionary, as well as not holding smaller/mid-sized growth stocks.

As usual, individual stocks showed disparate performance, often strongly contrary to the underlying sector's returns. For instance, the financials sector in aggregate fell by -4.7%, while **JAFCO**, a quoted venture capital firm, rose by 33% on a total return basis.

Similarly, relative outperformance within the industrials sector that fell -1.86% was shown by **Mitsubishi Heavy Industries** (+4.7%) and **NGK Spark Plug** (+9.5%) on continued positive news flow. In the materials sector, which fell -5.1%, **Kansai Paint** leapt 22% after delivering Q1 net profits up 21%, way ahead of predictions.

By contrast, in industrials, **Komatsu** dropped 9.8% as the mining sector's investment cycle was deemed to have peaked, All of our construction stocks lost ground, with all four of our holdings falling by between 1% and 5% as profit taking set in after their strong second quarter.

Within the consumer discretionary sector, our allocation to autos **Toyota** and **Subaru** underwhelmed, falling by over 10% each, exceeding the -6.9% fall shown by the sector as a whole and driven by the apparent slowdown in second hand car sales in the US. Consumer demand is being constrained by prices which are up 28% year-on-year and by escalating finance costs as interest rates have risen.

We expect fundamentals to remain relatively beneficial for Japanese equities. Firstly, due to their balance sheets' no/low debt condition, they are better placed to ride out central banks raising rates further and faster than generally expected. Next, their geographic distribution of operations includes a relatively high exposure to the US and non-OECD markets, with a correspondingly lower one to UK/Europe than their major competitors, particularly their European rivals, so sidestepping the worst of the economic fallout from the Ukrainian invasion. Lastly, the yen's likely drift lower on widening interest rate spreads would boost large-cap Japanese corporate profits.

As such, the Fund will remain overweight in large and mid-sized, well-financed, industry-dominant Japanese multinationals that are set to benefit most from the currency's likely weakening.

Discrete years' performance (%), to previous quarter-end:**

	Sep-22	Sep-21	Sep-20	Sep-19	Sep-18
Liontrust Japan Equity C Acc GBP	-9.8%	16.2%	3.8%	1.8%	5.1%
Topix	-13.9%	15.3%	2.0%	-0.7%	12.6%
IA Japan	-15.4%	16.6%	5.6%	-1.1%	12.6%
Quartile	1	3	2	1	4

***Source: FE Analytics as at 30.09.22**

****Source: FE Analytics as at 30.09.22. Quartiles generated on 06.07.22**

For a comprehensive list of common financial words and terms, see our glossary at:
https://www.liontrust.co.uk/benefits-of-investing/guide-financial-words-terms

Key Risks

Past performance is not a guide to future performance. The value of an investment and the income generated from it can fall as well as rise and is not guaranteed. You may get back less than you originally invested.

The issue of units/shares in Liontrust Funds may be subject to an initial charge, which will have an impact on the realisable value of the investment, particularly in the short term. Investments should always be considered as long term.

Investment in the Fund involves foreign currencies and may be subject to fluctuations in value due to movements in exchange rates. The Fund may invest in emerging markets/soft currencies or in financial derivative instruments, both of which may have the effect of increasing volatility.

not a professional investor please consult a regulated financial adviser regarding the suitability of such an investment for you and your personal circumstances. [22/799]