Hello and welcome to this programme from Baillie Gifford. My name is Gavin Lumsden, I'm from Citywire and I'm going to be talking to Matt Brett, manager of Baillie Gifford Japan Trust. This is a good time to speak to Matt, with Japan's stock market having recently hit a record high and the economy moving out of a long period of deflation. Good afternoon to you.

Hi Gavin.

Nice to see you. Thanks for making the time. As I said, I've got some questions for you, so I'll just kick-off straightaway. As I alluded to, Japan's stock market and economy have been in the news a lot lately. The Nikkei 225 index surpassed its December 1989 peak in February, but the low point was way back in 2009. So, I wonder, what makes Japan still attractive after a long, if intermittent recovery?

Yes, I think you're right. That 1989 peak has been a bit of a psychological hurdle on the minds of the Japanese for the past 35 years. I think it's probably a good thing to see that in the rearview mirror now. You're also right that the Japanese market bottomed quite a number of years ago now and it's been making good progress since that time. I think what makes Japan exciting for us is the number of interesting growth companies within the market. Particularly in the medium and the smaller area of the market. These have often been overlooked in our view, by global investors, over the recent years, given that Japan perhaps hasn't been centre of people's attention. There's been a lot of exciting companies doing solid progress over the years and I think that's really what makes us still excited about the prospects looking forward even despite the fact that we're 15 years from that bottom in the Japanese market.

On the economic front, can you tell us what's the significance of Japan exiting from deflation? The Bank of Japan has just about ended negative interest rates and yield curve control policies, what does all that mean for investors?

I think this is a very interesting change. Japan's really going through a period, post that bubble era it had a period of deflation and that was very difficult for Japan. Then more recently it had this period of noflation with neither inflation nor deflation. More recently, we seem to actually have inflation in

Japan again. We're seeing property prices increasing. We're seeing wages going up. We're seeing prices of consumer goods rising in Japan. So, it's quite a broad-based inflation. Not anything to be concerned about, but certainly a healthy level of inflation. I think the bank of Japan, moving away from the negative interest rates policy and taking those baby steps towards normalising the interest rates, is just really a reflection of where the Japanese economy is getting to, which is, it's no longer really in those special measures of the past. It's behaving a lot more normally.

I think for investors what is exciting is that deflation is a difficult environment for investment. It really weighs on things. It makes it very difficult to achieve returns and I think the ending of that is helpful for a number of companies. Combined with your earlier comment about the Japanese market getting past that 1989 peak, I think there's a real potential here, for what the Japanese would describe as the animal spirits to continue from here. Those problems of the post-bubble era, they really do feel like distant memory in Japan now. I think hopefully what we can focus on are the individual companies and what they're able to achieve in the future.

Talking of companies, it's good to see the Japanese stock market doing better, but why are large companies seeming to benefit the most from the recent rally?

That's right. So recently a lot of the good performing stocks have been the large export companies driven by the weak yen environment and, also some of the large banks, as people have started to worry less about inflation. So, shareholders in the trust, they've had quite a disappointing period of relative returns, albeit generally prices have been increasing because basically, we haven't been able to keep up with those exporters driven by the strong cyclical background globally and the weak yen environment.

Given that, can you explain why you skewed the portfolio a bit more towards smaller and medium size stocks?

Essentially, this is a long-term strategy that we've employed for many years and it doesn't work clearly, every year or every few years. The reason fundamentally, for being more interested in the medium and the smaller companies, is we think ultimately, that's where you have the greater growth potential. Particularly when we think about the domestic economy of Japan, albeit it's recovered again. The population of Japan is pretty static, it's a very wealthy country. So, in order to find a growth company, you really need a company that's a medium company that can take share within the market over time. That pulls us towards some of the domestic internet companies and things like that. Those companies naturally are the ones that are medium and smaller companies.

On the other hand, when we look at the index as a whole, some of the big areas we're just not super excited about. When we look at those megabanks in Japan, they're perfectly solid, but we don't see particular growth prospects there. When we look at the big car companies in Japan, for example, we really struggle to see how there's going to be much growth in the type of vehicles that they're selling, given the increased competition coming in the battery electric vehicle market. Both from Tesla and, also from the Chinese competition. So, some of those big areas within the large-cap area, we just structurally don't find particularly attractive. Now that's not to say that they can't go up quite a lot for a year or two, but in the long-run we're much more excited about those small and medium size companies as a whole.

It's been a difficult couple of years for your quality growth approach. How cheap are these stocks at the moment?

There's lots of different metrics that one can look at, but I think what is striking is, it doesn't seem to us that you're paying much premium at all for growth at the moment in Japan. So, for example, just looking at the Bloomberg analysis of the Japan Trust portfolio, it suggests that the portfolio's only on a price to sales of 1.1 times, which to me, seems remarkably low for a growth portfolio. I think when we look at the earnings of some of those companies, particularly the car companies, they've done very well recently, buoyed by the weak yen. If we start to think about adjusting those for the cycle, some of those companies actually look quite expensive to us now, relative to the more genuine growth types of businesses.

That's a good position from which to go from hopefully. You're long-term themes remain digitalisation, automation, and artificial intelligence, can you update us on each of these and give us some examples of key stocks please?

So, I think this increased use of technology is something that we're seeing across the whole world, but I think at the moment it's being accelerated by the developments in these large language AI models. Also, in many cases Japan is coming, particularly in the internet space, from a place that's not quite so advanced as in the west. So, we've got companies at an earlier stage of development. So, for example, looking at that internet area, a couple of the companies we're really excited about at the moment include GA Technologies, which does online real estate sales and also bengoshi.com, which is a forum for lawyers. They've also developed a document signing business, a bit like DocuSign. So, these companies are still relatively small within the context of real estate or within the context of the legal system in Japan. We believe they've got good competitive positions and a lot of growth ahead of then.

Then in automation, I think we all know Japan has a very good reputation within robotics. We've got the classic strong Japanese robotics company, Fanuc within the portfolio. Also, for example, we've got within machining centres, DMG Mori, which merged a few years ago now, with its German competitor Gildemeister, to create an overwhelming number one globally in that area. That's managed to get the margins up and that's been doing well. Broadly speaking, we're super excited about the prospects for automation because what we're seeing is the potential for AI and machine vision to make robots a lot smarter than they have been in the past. A big opportunity for Fanuc is cobots, which are robots that work alongside humans and are capable of stopping moving if they come across a human, etcetera. [marker 10:00] Machine vision and knowledge of the environment makes those robots an awful lot better and we think there could be good growth potential there.

In terms of AI, I think this is one of these mega-themes. A bit like the internet, which is going to cover a whole host of different companies. For example, within this portfolio, longstanding holdings like Rakuten and Cyberagent. Both of these companies have huge numbers of customers and that gives them access to lots of data which is really what you need to feed these AI models with, to create differentiated services and product offerings. Talking to the president of LY Corporation, formerly known as Yahoo Japan, they're talking about getting efficiency gains of about 50% on software engineers. Software developers, basically. These gains are absolutely massive and in a country that maybe doesn't have quite as many software experts as some countries, I think this is going to be a huge benefit for Japan as a whole.

Very interesting, thank you. Let's turn to SoftBank which is your biggest holding and has been a bright spot lately. It surprised the market with better than expected annual results in February. Perhaps that wasn't a surprise to you, but I just wonder, what are the prospects for Arm Holdings, it's biggest investment as well as the rest of the portfolio?

SoftBank's one of these companies where I think lots of people, if you read the papers, you'd imagine SoftBank as being a pretty disastrous company. Quietly behind the scenes, Mr Son has been having some good successes. The most recent one is Arm, where he bought this from the UK market in the wake of Brexit and at the time people said maybe he's paid too much for it, etcetera. Anyway, he's recently relisted it on the Nasdaq, making three times his money on that company, which is quite good for a few years work. I think the real excitement with Arm is it's got a monopoly on the architecture of mobile phone chips and those chips are going into more and more types of devices and are very important in terms of AI. Having more powerful architecture within mobile phones.

So, it seems to be one of these rare businesses that has a very dominant position in what it does and good growth prospects ahead of it. I think that's been better recognised now. Looking beyond that

SoftBank has some other quite exciting investments. For example, it has a stake in ByteDance, which is the owner of TikTok, a company which continues to grow very fast and have a lot of excitement. They also seem to be working very hard at the moment, on developing autonomous driving systems. Combining that chip knowledge and, also, the AI knowledge. It looks like they're trying to get cars to be able to drive themselves in a more human-like fashion than the current autonomous driving efforts. If they can pull that off, that would be very exciting.

So, I think my broad joke with SoftBank is if we could all fail as well as Mr Son, we'd be doing quite well. There is always this gap between the news and the reality. The reality is Mr Son has got the company into some very exciting places and, actually, those profits are starting to come through again.

Good to hear there's a turnaround going on there. The trust benefitted from a private equity bid and a big premium for outsourcing the Staff Company recently. Has M&A, mergers and acquisitions been a theme evident elsewhere?

There're various bits of M&A happening in Japan and I think the old perception is that Japan's a very difficult market to do M&A in. I think that's really changed over the years and we see, for example, this private equity bid for outsourcing. We've also seen private equity bids for some of the holdings within Shin Nippon, the smaller company investment trust. We've also seen more restructuring type of M&A. For example, the holding in Rome is part of a consortium basically, restructuring Toshiba, which is very exciting as well. So that aspect of Japan and restructuring things, I think has been quite helpful. I think the odd thing is that as Japanese companies are getting a bit more confident again, they're a bit more prepared to take some of these more tricky decisions to restructure or do M&A to try and improve the competitive position than perhaps they were during the darker days of the last 30 years. Where maybe they were more focused on staying alive rather than looking forward, but that's very much in the past now.

I'm interested to know which stocks you picked when you were reinvesting those gains from outsourcing. You made some money on Itochu, a trading company that you sold after a share price rerating. What did you do with the cash from those two sales?

In general, we have a very, very low turnover style. Annual turnover is typically in the low teens. So very much what we're doing is buying the companies that we think have the good growth prospects and then holding them for the long-term. In the case of Itochu, one of the big general trading companies, we've held it for many years, but the reality is, the shares have done incredibly well. Mr Buffett has nicely advertised the benefits of the trading companies, but they're over double the price of where he was buying as well. So, we think they've pretty much done as much as they can. In terms of reinvesting, it's gone into a variety of different things. Some examples would be SATO, which does barcodes and RF ID chips which fit really, really nicely with the whole AI theme in terms of labelling up things so that computers can understand which packages are going where.

Lots of potential in the food industry. Also, the medical industry. Also, more into GA Technologies, the online real estate company I mentioned earlier. Finally, some into Oisix, which does meal kit delivery services and has recently acquired a competitor to give it much greater scale. I think each of those companies are probably not exactly household names, but these are medium size companies that we think have very strong growth prospects ahead of them.

How is China's weak economic recovery affecting Japan? The delayed return of Chinese tourists affected stocks such as Shiseido and Pola Orbis, half year results recently showed.

That's right. So, during COVID we invested in a few different things that had been having a difficult time through lack of demand. Some of those have worked already. So, for example, Bridgestone in tyres. That's worked pretty straightforwardly. People started driving again and flying again. It does plane tyres as well and the profits have recovered. Those skincare companies have been slow to recover and a good part of that is that the Chinese consumer hasn't really got going yet, as fast as the Americans have, for example. I think looking forward, I don't think we have a great concern, we think it's just a matter of timing. The competitive positions of those cosmetics companies remains very strong in China, but what we're really waiting for is for the Chinese consumer to get fully back on to the front foot.

I think basically, what we've seen is that there've been a bit of a lag in Asia compared with the west in terms of getting through COVID and mentally as well. Just getting back onto the front foot and I think Japan seems to be about six months behind the UK in terms of reopening and things like that. China seems to be six months behind Japan. One of my colleagues is literally just back from visiting China, gone to checkout some of the competitors to our companies, etcetera. The report is that things seem to now be picking up in China, which is quite encouraging. In the long-run, when we look at the spend that the Chinese have on skincare, it's still a fraction of the amount that the Japanese are spending in this area or even the South Koreans are spending. So, what we think is that these skincare companies have this huge long-term growth opportunity ahead of them and we're happy to be patient and just wait for that recovering to keep coming through.

Let's turn to gearing or the trust's ability to borrow. Gearing stood at 19% in February. How does that compare with the past and what does it say about your confidence in the trust's investments?

The gearing over the years has ranged from about where it is now. High teens down to about 10% or so. So, we're at the more optimistic end at the moment. Gearing is really [marker 20:00] a call on the absolute potential performance of the stocks that we invest in. In that sense, we still feel really optimistic because going back to your opening comments, although the Japanese stock market as a whole has done really well, many of our companies haven't done especially well yet. We still see a lot of opportunity for them and that's why we've got the gearing towards the upper end of the range at the moment. We wouldn't take it actively over 20%. So, we're pretty much at the maximum level of gearing at the moment. That just reflects the enthusiasm we have for the portfolio.

Meanwhile the trust's shares trade at a relatively wide discount of 12%. The board's been buying back shares, which is good. 3.5% in the last half year. What message do those stock repurchases convey to investors?

Stock repurchases at a discount increase their NAV per share for all remaining shareholders. So hopefully, they're seen as a good thing by all the shareholders. 3.5% of the company bought back in six months, it's equivalent to 7% in the full year if we keep going at the current rate. So, I think these are more than tokenistic types of buybacks. It's really actively making a decision that discount does look wide and the board is prepared to buyback. Also, the Japan Trust doesn't invest in any unlisted companies. There's not so many bigger unlisted companies in the Japanese market. So, it's very easy for us to buyback and maintain the shape of the portfolio exactly how we want it to be. So yes, I think there's no change to the board's fundamental thinking.

It's interesting. When you put that 3.5% on an annual basis, obviously, that's 7%. That's getting towards the level of Scottish Mortgage, Baillie Gifford's big global trust announced a big share buyback of a similar magnitude actually.

Yes. I think they are similar. If anything, it might even be the case that the Japan Trust over the past six months is going at a slightly faster run rate. Obviously, the Japan Trust is a very much smaller trust than Scottish Mortgage. So, the absolute amounts are much smaller, but yes, in terms of buybacks it's a serious amount of buyback.

As a proportion it's showing some conviction in the buybacks. Let's turn to our audience's questions. I'll start with one that we got just before the programme started. It's about the dividend policy which we haven't touched on and linking it to corporate governance changes in Japan. The question is, "Japan's trust performance mirrors that of most Baillie Gifford trusts. What I'd like to know …" says the investor, "… is how the regulatory changes in Japan encourage among other things, increased payouts to shareholders? Baillie Gifford has, over the years, made

a big thing of its trusts not paying a decent level of dividends, being growth funds. However, it's periods such as

the last couple of years, where being paid while one waits for capital returns is helpful." So, there's an investor appreciating the dividends. What is the trust's dividend policy at the moment?

So essentially, there's two parts to this. There're the dividends coming into the trust from the underlying holdings and then there's how the company itself treats the dividend. In terms of the dividends coming in, we have seen quite a rapid increase in companies paying out more than they used to. This is part of a longstanding journey. I'm not totally ancient, but when I started doing Japan, you'd meet companies and they'd say our dividend policy is Y50. You'd say, "Why Y50?" It was just Y50. It had no relation whatsoever to the earnings or the balance sheet or anything, it was just Y50. We went through a period of focusing on payout ratios and now with the governance code and the stewardship code, companies are increasingly thinking about the balance sheet as a whole and how much is appropriate to payout. That journey has continued.

Obviously, although it's not the main focus of this trust, the side effect is more dividends being paid out even by the growth companies. Most internet companies in Japan, most companies indeed, pay dividends, which is quite different to many growth companies globally and the trust has got that income coming in. So, over the past few years, there's been quite a dramatic increase in the dividend being paid out by the trust because to start with, it had accumulated revenue deficits and that was paid off first. So, the trust first paid a dividend of under one penny a share back in 2018 and then the dividend since then has gone 3.5 pence, 4.5 pence, six pence, nine pence and last year ten pence. So, the yield on the trust at the moment is about 1.3% which the focus remains very much on the capital growth.

We're not trying to run a particularly progressive type of dividend policy, but it just happens that those dividends have been increasing strongly from the underlying holdings and then the board has been paying out the minimum dividend rounded so far and that's been the outcome. The one thing I should also note is that of course, all the income is in yen. So, the dividend, as paid out in sterling, you could see variability on that because of the effects of the currency. I think it just really reflects the dividends that are coming in and when dividends come into an investment trust, the vast majority of them are automatically paid out to maintain the investment trust status and that's what we've seen in the past few years.

Looking forward, I don't see any sign that the company's enthusiasm for paying out dividends is diminishing and the other thing is, is you're also getting quite significant buybacks from many Japanese companies and you don't have much options issuance in Japan. So often we've got dividends coming in and growing on a shrinking share count for many of the businesses, which in the end should be quite helpful to the shareholders of the Japan Trust.

You mentioned the currency, which can be quite volatile and affect investor returns, as you just said. How do you manage the currency side of things? Do you hedge it at all?

Basically, we run the trust entirely effectively in yen. So, we don't do any hedging. It's an unhedged vehicle and the board has considered in the distant past, hedging, but decided not to consider doing it. The loans that the trust has for the gearing are all in yen. So, they don't create any currency exposure either. So, where there are borrowings, they're being borrowed in yen. All the investments are in yen. Obviously, there's a translation effect back into sterling in terms of the reported results and there's a translation effect in terms of dividends, the amount being paid in sterling. It's obviously dependent on both the amount coming in, in yen and then also, the exchange rate.

Got a question about the revenue returns, which might link with dividends, maybe with the currency as well. The question from an investor who notes, "The revenue return per share rose strongly from 2017 to last year but then fell back." They wondered what has been driving that.

I think there's two effects here. There's a bit of a currency effect going on with the weakening yen and then being translated back into sterling, which is what you will see within the accounts. Also, as it's been a very difficult environment for growth companies in Japan, we've been slightly leaning the portfolio towards some of those smaller, higher growth companies and they're often coming with a slightly lower dividend yield. So, what we're aiming for here is for total returns. If we see more opportunity within something that yields a bit less, then we'll happily sell the higher yielding company in order to buy the lower yielding one. Nonetheless, the overall trend I think, is still positive in terms of what Japanese companies as a whole are doing with dividends.

There's a viewer who wants to ask you about the state of the Japanese stock market and how it seems to be quite polarised. So, the question is, "How do you look at growth versus value in Japan?" And an observation that activism seems likely to last many years and seems to be doing well. So yes, view on growth versus value currently and, also, whether you get involved with any kind of activism or engagement?

In terms of that growth versus value thing, it's definitely been the case that the past two, three years it's very much been a time for the value [marker 30:00] type of investor in Japan. We've suffered relatively as a consequence of that. We talked about some of the reasons earlier. That strong global cyclical recovery combined with a weak yen is a perfect environment for businesses that maybe don't normally have terribly high margins, but it really helps them along a bit. Then in terms of the opportunities, I think what we've seen is in share price terms many of our favourite companies have gone sideways or down for two or three years. Under the bonnet they've still often been growing their sales, growing the earnings. So, they've basically just been becoming cheaper.

When we look forward, we can't really get so excited about some of those cheap but not really fast-growing companies. Yes, when some of these companies traded at a big discount to the book value or something like that, undoubtedly there was some kind of value in them and that value maybe has now been realised. Looking forward, they're still the same companies as they were before. They're not likely to have a high growth rate ahead of them and therefore, we don't find them so exciting. I think on this activism thing, it's an interesting question and it appears to be a separate question. In some ways it might actually be the same thing because I think many of the activists have been targeting these more value type of companies.

As a result, it appears there's been very good returns from activism in Japan. Of Course, it may be there's been very good returns from value stocks in Japan and activists have tended to be in those value stocks. So of course, there are cases where the activism will have encouraged things or moved them along a bit faster, but I think there's also an element here to which the returns achieved by activism may have been somewhat flattered in the past two or three years by the fundamental nature of the companies that they're investing in. Now, when it comes to us, generally speaking we invest in companies with management that we like. Generally, we're backing the management. There are occasions when we have made observations with regard to the balance sheet conservatism. Maybe we should think a bit about that, etcetera.

In general, we're more at the supportive end of shareholders and we're trying really to encourage companies to be bold enough to seize the growth opportunities ahead of them, rather than to be focused so much on the dividends and the buybacks and so on. There are occasions when we do engage with companies, but I think the main point here is that when we're looking at the companies that we invest in, many of them have a founder shareholder, which gives us natural alignment. They want to make money themselves. We want them to make money. We want to make money together. I think in the long-run, that's probably a more reliable method of making money rather than agitating for shorter term change.

A question here about what lessons may have been learnt from reviewing the performance difficulties of the past few years. "Has style and diversification of the portfolio been reviewed during this period or as a result of this period?"

We certainly looked at how we could have done better. With some of the aspects, for example, like thinking about cars and banks doing very, very well, we don't worry too much about that because I think it's not naturally what our main focus is. One area that we have picked up on is, we did sell out of some companies like Advantest and Disco. Advantest does memory testers and Disco slices up wafers. Now, these companies have come very much into the focus in the last year or so with that AI boom. Looking back, we were perhaps too hasty to exit those companies. Now, the reason we did is because we saw even more opportunity in some of the internet, more software type of businesses from AI.

Certainly, had we not done that, the returns would have been better and I think that's something that is a learning point. Whether we can improve things by getting back into those stocks at this stage, I think that's a very open question. I'm not convinced about it, but certainly that's something that we would acknowledge as being something that we could have done better in the past few years. A lot of these things, you have these quite big swings in performance. Ironically, we were getting a bit of challenge a couple of years ago about are we growthy enough? I think with the benefit of hindsight, I think we can see we were more than growthy enough. If anything, perhaps a bit too growthy.

At the same time, growth seems very much on sale at the moment. That's why at the margin, we're pushing the trust further down the market cap spectrum a little bit and pushing it into these higher growth names more than before and selling some of these names that maybe we feel-, things like Itochu. Nothing wrong with Itochu, but we feel it's largely done its stuff and there isn't as much opportunity there. So effectively, at the moment, we're running with a slightly purer version of our natural style than perhaps we had five years ago. That's been undoubtedly a rough ride in the past couple of years. In the long-run, if these companies can continue to show progress and we've seen progress with SoftBank with its Arm listing.

We've seen progress with Rakuten, the second biggest holding, getting more subscribers into its mobile business. So, we're seeing operational progress for the individual companies and I think that gives us a lot of comfort that over a longer time period these companies' share prices will gain more traction.

The linked question here, a viewer would like you to break out the difference between the large and mid-caps in the portfolio. What's the allocation? Then a follow-on question because it does seem to be more skewed towards mid-caps at the moment. "Is there an overlap with the Shin Nippon?" The smaller companies trust.

It's not that we don't invest in any large-caps certainly, but we just have a lower weighting there. As we spoke about earlier, being a growth investor, I think that's quite natural when you look at what the big companies in Japan are. For example, as of the half year the TOPIX 100, the equivalent of the FTSE100, that was 66% of the market cap of Japan as a whole. Whereas it was 42% of your company, of the Japan Trust. So, in that sense, we're structurally quite a bit underweight those very biggest companies. Sorry, there was a second part. The overlap with Shin Nippon. So, there is some overlap with Shin Nippon and it's been pushing up a little bit, but it is a pretty modest overlap between the two.

So, we're talking low teens type of percent overlap at the most. The reason for that is because Shin Nippon really specialises in these really quite small companies. Whereas the Japan Trust has got a medium and small-cap bias, but it's certainly by no means a pure small-cap trust. For example, companies like SoftBank are among the bigger companies in Japan. So, I think Japan Trust has a broad remit. There's nothing to stop us investing in larger cap companies. What stops us doing it isn't their size, it's their growth prospects which often seem to us, quite dull.

While we're making those kinds of comparisons, another question asking how similar is the Japan Trust to the open-ended Baillie Gifford Japan fund that you also run?

Basically, the overlap between the Japanese fund and the Japan Trust is more of the order of two-thirds overlap. So, there is much more similarity between the Japanese fund, the open-ended vehicle, and the Japan Trust than there is between Japan Trust and Shin Nippon. The difference is mainly in those small and mid-cap stocks where Praveen, who manages the Shin Nippon, is the deputy manager of the Japan Trust and it can and does go further down the market-cap spectrum than the Japanese fund does. That gives us access to a few more of those smaller types of companies. The Japanese fund tends to go down to a market-cap, very roughly, of about Y100 billion. So, we're talking here, depending on where the currency is, I would have said in the past something near to a billion dollars. Now it's a bit smaller than that. Whereas the Japan Trust can go down significantly smaller than that.

We talked about gearing earlier on, you were explaining your approach to using borrowing. "Given the market over the past few years, wouldn't it have been [marker 40:00] sensible to reduce gearing?"

Yes, and I can totally get where that question is coming from. Here we are cheerily talking about the market being at an all-time high and here we are with maximum gearing. It's a very logical question. I think when we look at the portfolio that we have, we have substantially lagged the overall market. So, most of our stocks are not at all-time highs and therefore, you would feel quite confident in thinking that it's the right thing to use the gearing. Going back to that dividend point, the cost of borrowing in Japan remains incredibly low. So, we're getting more income in many cases, from the companies we're buying than we're paying out on the loans. I think that gives us quite a degree of conviction here.

Again, given the difficult few years, looking ahead though, you've expressed your conviction in the growth stocks you've got. "What is going to improve the performance over the benchmark in the next few years?"

I think, at the end of the day, what I would expect to improve performance versus the benchmark is how those individual companies do. So, when I look into the benchmark, I see those big car companies often with earnings that are hitting all-time highs. In the case of Toyota. As I look forward five to ten years, I see loads of competition coming from those Chinese battery electric vehicle makers, from Tesla. I see potentially it being a very difficult environment or Toyota going forward. Whereas many of the companies that we invest in, those internet businesses, those factory automation businesses, etcetera, I see as continuing to be able to grow their sales and profits over time.

It's an old adage, in the short-term the market's a voting machine and in the long-term it's a weighing machine. I think the type of situation that will help us is if those sales and earnings keep coming through for our companies and you start to see some of those more value type of companies struggling to grow their sales and their profits, I think that's when you'll start to see the differential in share price performance. Look, telling exactly when things go well or badly is a really difficult thing. Who would have known during COVID, for example, that the Baillie Gifford portfolios would turn out to be quite a good place to have your money. If you'd asked me in advance there's a global pandemic coming, will it be good or bad? I think it would have been a brave thing to say that it would be a good thing for the portfolio, but actually, it turned out that it was.

Similarly, we are in a situation now, where we have already seen quite a big global recovery coming out of COVID. We've seen this burst of inflation, which has been difficult and confusing for people and has probably weighed on the prospects of growth companies. We've also seen digitalisation and AI continue to develop. I think in terms of the companies we have; we think many of them remain very strongly positioned for the future. Therefore, my conviction comes from being able to take a longer view on things and expecting that in time those companies that grow their sales and their profits will become better rewarded by the market. In the meantime, we have to be patient and I guess, keep going with the buybacks etcetera, for the time being.

Thanks very much for your time, Matt. Let's hope the rerating follows the progress in innovation that you've been talking about. I hope that what you've heard has provided some helpful insight into the Japan Trust and where it invests. In the meantime, from me thank you very much and goodbye.

Annual Past Performance to 31 December Each Year (Net %)

	2019	**2020**	**2021**	**2022**	**2023**
Baillie Gifford Japan Trust	**21.8**	**35.2**	**-10.4**	**-21.7**	**-5.6**
TOPIX	**14.6**	**9.5**	**2.0**	**-4.1**	**13.3**

Source: Morningstar and Tokyo Stock Exchange. Share price, total return in sterling.

The specific risks associated with the Trust include:

- The Trust invests in overseas securities. Changes in the rates of exchange may also cause the value of your investment (and any income it may pay) to go down or up.
- The Trust can borrow money to make further investments (sometimes known as “gearing” or “leverage”). The risk is that when this money is repaid by the Trust, the value of the investments may not be enough to cover the borrowing and interest costs, and the Trust will make a loss. If the Trust's investments fall in value, any invested borrowings will increase the amount of this loss.
- The Trust can buy back its own shares. The risks from borrowing, referred to above, are increased when a trust buys back its own shares.
- Market values for securities which have become difficult to trade may not be readily available and there can be no assurance that any value assigned to such securities will accurately reflect the price the Trust might receive upon their sale.
- The Trust can make use of derivatives which may impact on its performance.
- Investment in smaller companies is generally considered higher risk as changes in their share prices may be greater and the shares may be harder to sell. Smaller companies may do less well in periods of unfavourable economic conditions.
- The Trust’s exposure to a single market and currency may increase risk.
- Share prices may either be below (at a discount) or above (at a premium) the net asset value (NAV). The Company may issue new shares when the price is at a premium which may reduce the share price. Shares bought at a premium may have a greater risk of loss than those bought at a discount.

Further details of the risks associated with investing in the Trust, including a Key Information Document and how charges are applied, can be found in the Trust specific pages at www.bailliegifford.com, or by calling Baillie Gifford on 0800 917 2112.

Price-to-sales (P/S) ratio is a valuation ratio that compares a company’s stock price to its revenues.

Currency hedging is an attempt to reduce the effects of currency fluctuations on investment performance.