

# USONIAN JAPAN VALUE STRATEGY

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## *The Opportunity*

Japanese equities are a relatively inefficient asset class undergoing significant structural changes. They provide a compelling long-term opportunity, particularly to investors willing to engage with company management. Value stocks are especially attractive in Japan today given wide valuation discounts. Unique attributes lie behind the attractiveness of Japanese equities:

## A LEGACY OF “LOST DECADES” AND DEEPLY EMBEDDED BIASES CREATE EXPLOITABLE INEFFICIENCIES

- Protracted declines in Japanese equities in the decades following the late 1980s bubble led to cheap absolute and relative valuations, a reduction in the number and quality of investors focused on the market and a concurrent decline in sell-side coverage.
- The Japanese market presents cultural and language challenges that often frustrate fundamental-oriented investors, many of whom simply spend less time researching the market. History, media, and cultural misunderstandings have led Japanese and non-Japanese investors alike to develop negative biases toward the Japanese equity market. Companies shunned by the investment community due to legacy stereotypes often become interesting investment candidates.

## STRUCTURAL REFORM TAILWINDS SUPPORT SHAREHOLDER INTERESTS

- To address the structural pressures stemming from demographic headwinds and low growth, the Japanese government and corporations have sought to improve capital productivity for some time. A cohesive set of policy initiatives, including Japan’s Stewardship Code and Corporate Governance Code, intensified the focus on corporate governance reform, labor efficiency, and global competitiveness.

## CONSTRUCTIVE ENGAGEMENT CAN PROVIDE SIGNIFICANT LEVERAGE

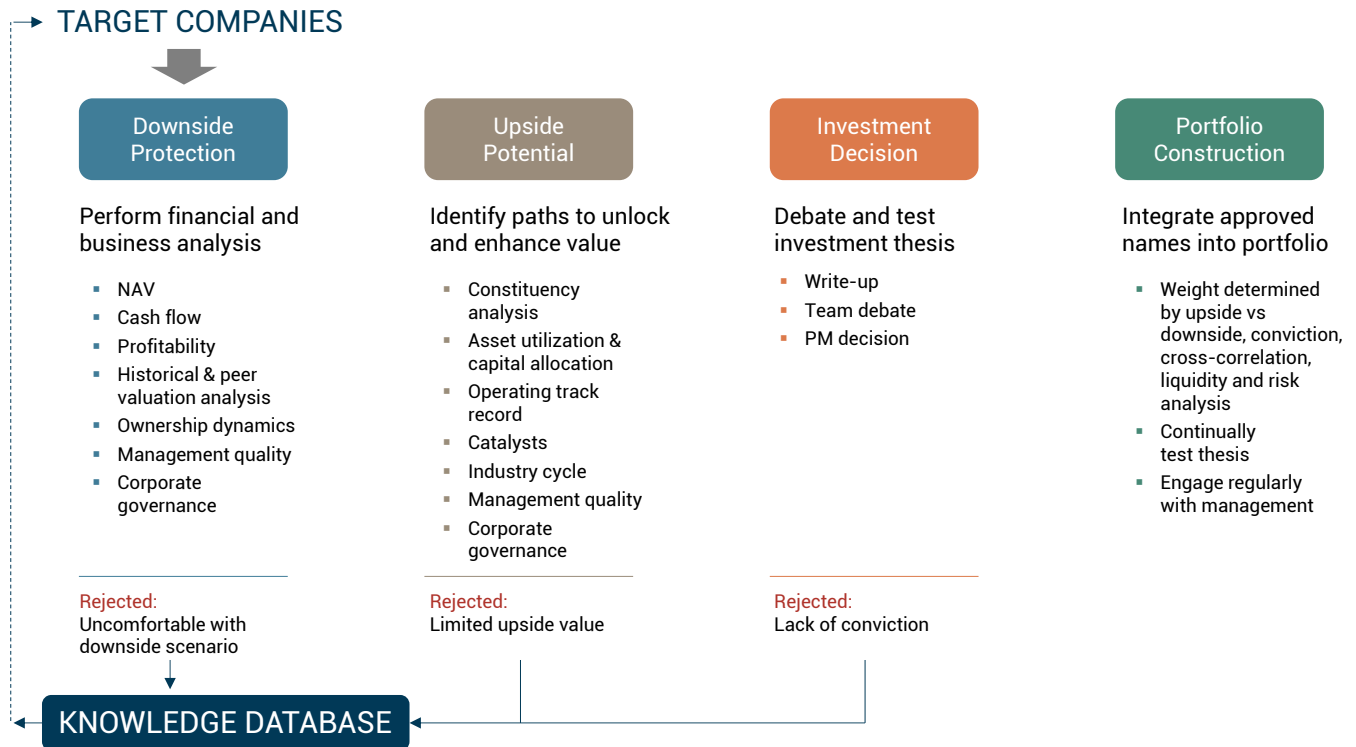
- As Japanese management teams consider shareholder-friendly reforms, they are more willing to engage outsiders with the domain expertise to explore strategies that improve corporate value.
- The team believes that a constructive approach to engagement is most productive for fundamental investors in Japanese companies due to cultural considerations.

## *The GMO Solution*

The Usonian Japan Value Strategy seeks long-term capital appreciation over a full market cycle, aiming to outperform the TOPIX Total Return Index. The Strategy employs a fundamental, value-oriented approach to investing in Japanese equities while focusing on capital protection in down markets and striving for lower total volatility compared to the index. The team also seeks to actively and constructively engage management to provide insights and best practices that enhance shareholder value.

GMO’s Usonian Japan Equity team derives portfolio returns from three different investment initiatives: (1) stock selection; (2) portfolio management; and (3) management engagement. The team executes its bottom-up investment discipline using a combination of quantitative and qualitative analysis to arrive at a diversified portfolio of attractively valued securities. All research is constructed with the goal of fully vetting ideas and identifying optimal investment opportunities. As fundamental stock pickers, the Usonian Japan Equity team performs well when pricing inefficiencies persist and stock prices become disconnected from the companies’ net asset value.

## INVESTMENT PROCESS: ANALYSIS



The Usonian Japan Equity team brings several key competitive advantages to its Japan Value Strategy:

- Singularly focused on investing in Japan, the Usonian Japan Equity team is among the few institutional investment teams that combine fundamental bottom-up value research with management engagement.
- Seasoned and diverse investment team with local and international presence and perspectives that enable various approaches to management engagement.
- Patient approach (average holding period of over three years) allows selective work alongside management teams to influence outcomes that can unlock shareholder value.
- Long track record and history of working together as a team ensures ability to continuously execute on the research process and acquire a high level of company knowledge.
- Significant focus on downside risk offers protection in down markets.

### *The Client Fit*

The Usonian Japan Value Strategy fits comfortably with long-term investors seeking alpha opportunities within their equity allocations while simultaneously aiming to protect capital in down markets. The approach could be particularly appealing to those who:

- Utilize ETFs to achieve cheap beta to large caps, but want to access the less efficient corner of the market (SMID value)
- Seek to exploit the opportunities arising from ongoing changes to corporate governance in Japan
- Believe the growth/value paradigm is due for a long-term correction

GMO's Usonian Japan Equity team also manages the Japan Value Creation Strategy, which uses the same investment philosophy and process as the Japan Value Strategy, but with an increased focus on underlying stock liquidity.

## ***Who We Are***

Founded in 1977, GMO is a private partnership whose sole business is investment management. The firm manages global portfolios with offices and clients around the world. Investment offerings include equity, fixed income, multi-asset class, and alternative strategies. GMO is known for blended fundamental and quantitative investment research expertise and a long-term orientation toward value investing.

## ***The Team***

GMO's Usonian Japan Value Strategy is managed by the Usonian Japan Equity team, which utilizes a disciplined, bottom-up, value-based approach to capitalize on unique inefficiencies in the Japanese equity market. Leveraging significant experience investing in Japan, the team maintains a long-term perspective and engages with company management to help enhance corporate governance and create long-term shareholder value. The team has managed the Japan Value Strategy since 2011 and joined GMO in 2020, with team members located in GMO's Berkeley office and a representative office in Tokyo.

## RISK

Risks associated with investing in the Strategy may include Market Risk - Equities, Management and Operational Risk, Focused Investment Risk, Non-U.S. Investment Risk, and Currency Risk.