E.I. Sturdza Nippon Growth (UCITS) Fund

May 2019 Fund Commentary

ERIC STURDZA INVESTMENTS

MARKET DEVELOPMENT

After a 10 day holiday and the start of the new era "Reiwa" on 1st May, the Japanese market opened on 7th May. Amidst the US raising tariffs from 10% to 25% on 200 bn dollars worth of Chinese imports, Japanese equities declined for 6 consecutive days. During the month, a risk-averse mood prevailed on the back of concerns over the US-China trade frictions and a global economic slowdown, with China-related names and economic-sensitive stocks sold off. The Yen appreciated against the US dollar in May, rising from 111.42 to 108.29, which also hurt the Japanese market.

On 15th May, the Japanese market gained on the back of the Chinese and other Asian markets rebounding. This said, the market lost the following day, when the US Commerce Department accused Chinese company Huawei of violating the trading ban with Iran. Two days later, Sony's stock soared after announcing its plan of 200 bn yen worth of share buy-backs and its alliance with Microsoft in the gaming business. On 20th, the market reacted positively to the preliminary Q1 GDP figure, which indicated growth for the 2nd consecutive quarter. This said, the growth was mainly due to a decline in imports.

In late May, US President Trump visited Japan and met with Prime Minister Abe. Their meetings were held in peace. This said, trade frictions between the US and China were likely to intensify, giving rise to a risk-averse market. During the month, the crude oil price dropped (from 63.91 to 53.50) and the US interest rate continued to decline, cooling the market. The decline of the US 10 year treasury yield from 2.5 down to 2.1 affected the 10-year JGB yield, which started the month at -0.040, ending at -0.094.

The TOPIX closed the month at 1,512.3 (down 6.5% MoM), whilst the Nikkei 225 finished at 20,601.2 (down 7.5% MoM). In terms of sector performance, only real estate gained, with all other 32 sectors having declined. The five best performers were real estate, communication, services, land transportation and insurance, whilst the five worst performers were mining, marine transportation, steel, pulp & paper, and glass & ceramics.

MARKET OUTLOOK

Generally, recent economic data in Japan are better than the market consensus. Real GDP growth for Q1 was revised up from 2.1% to 2.2% QoQ annualised, much better than the initial market consensus of -0.2%. Notably, private capex was revised up from previously -1.2% to +1.4%. The GDP data confirmed that private capital expenditures remained firm amid sluggish consumer spending, after they had risen sharply in Q4 2018 (+11.3% QoQ annualised). While weakness in exports, mainly due to less overseas demand from China, should be viewed as a dampening factor, capex is likely to be supported by other factors such as investment in labour-saving technologies in response to the ongoing labour shortage.

Core machinery orders, a leading indicator of capex, increased 5.2% MoM in April, beating the previously forecasted -0.9% and marking the third consecutive MoM increase. The Cabinet Office raised its assessment from "orders at a standstill" to "orders are recovering". This said, external machinery orders, another leading indicator of capital goods exports, declined sharply by 24.7% MoM in April, reflecting the impact of sluggish overseas demand, mainly from China.

Industrial production rose 0.6% MoM in April, with shipments increasing 1.8% MoM. The government estimates that industrial production would increase 5.6% MoM in May and

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INVESTMENT APPROACH

Access to Mr. Yutaka Uda's 40 years' investment experience in Japanese equities. Portfolio construction combines the long term macroeconomic view of the Investment Adviser with a bottom up perspective of stock research based on fundamental analysis.

INVESTMENT OBJECTIVE

To achieve long-term capital growth through active sector allocation and stock selection resulting from changes in economic conditions.

A sub-fund of E.I. Sturdza plc. Registered in Ireland.

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decline 4.2% MoM the following month. The Investment Adviser believes that production will likely be managed cautiously and as needed in the near term, taking into consideration external demand trends as well as the direction of trade frictions.

According to the financial services group and investment bank Nomura, corporate profits are continuing to expand. Recurring profits for the Russell/Nomura Large Cap Index increased 3.1% YoY for FY2018, marking the 7th consecutive YoY increase. Nomura estimates recurring profits will increase a further 4.4% YoY in FY2019.

This said, the scenario may not materialise if trade frictions between the US and China worsen. As such, the market is focussing on the G-20 meeting which will be held in Osaka, Japan on 28th-29th June. According to the team, it is likely that Donald Trump will meet with the Chinese President, Xi Jinping, with both leaders hopefully being able to find some meaningful solutions on trade issues.

In Japan, an Upper House election will take place in July, with the team anticipating that the impact on the market will be limited given that the LDP-led coalition party could easily secure the majority of seats.

PORTFOLIO STRATEGY

The net asset value per unit for the Nippon Growth (UCITS) Fund on a Japanese yen basis as of 31st May 2019 declined 8.3% compared with that of 26th April, while the TOPIX declined 6.5% during the same period. The Fund added one new name (Comsys) to the portfolio, with two stocks (Nabtesco and Sumitomo Chemical) sold out.

The Fund continues to be overweight with regards to economic-sensitive sectors with very cheap valuations such as energy, trading companies, machinery and banking. Construction and real estate sectors remain bullish against the background of aggressive fiscal spending. At the same time, defensive sectors such as foods, pharmaceuticals and utilities continue to be avoided.

PERFORMANCE DATA As at end of May 2019

CUMULATIVE PERFORMANCE %*

	1M	1Y	3Y	5Y	10Y	15Y	Fund Inception	Strategy Inception
JPY A	-8.31	-13.56	8.14	9.04	55.29	45.40	56.66	90.31
TOPIX PR JPY	-6.53	-13.46	9.60	25.88	68.42	32.66	66.44	30.91
Nikkei 225 Average PR JPY	-7.45	-7.21	19.53	40.79	116.34	83.34	100.65	82.72

CALENDAR YEAR PERFORMANCE %

	YTD 2019	2018	2017	2016	2015	2014	Annualised Inception
JPY A	0.59	-20.67	20.85	-2.23	3.19	2.19	3.69
TOPIX PR JPY	1.22	-17.80	19.69	-1.85	9.93	8.08	1.53
Nikkei 225 Average PR JPY	2.93	-12.08	19.10	0.42	9.07	7.12	3.45

Past performance is not an indicator of future performance.

* In 2001, the Nippon Growth Fund was authorised by the Guernsey Financial Services Commission as an open ended collective investment scheme using the same strategy as the Fund. Performance since the 22 October 2009 is that of the Nippon Growth (UCITS) Fund.

IMPORTANT INFORMATION

The views and statements contained herein are those of Evarich Asset Management in their capacity as Investment Advisers to the Funds as of 13/06/2019 and are based on internal research and modelling.

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