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Reduction in Japan exposure

25 March 2020

In these difficult times we remain committed to keeping clients updated on our current investment thoughts and our portfolio positioning.

We believe that in times of market stress this communication becomes more important than ever, hence we hope you have seen several updates from us in recent days. With this in mind, we wanted to further update you on a decision made by our Investment Committee earlier this week.

As we have detailed previously, we are currently positioning portfolios to provide some potential protection against any further market weakness but also ensuring that we are ready and prepared to invest when we believe the time is right. We raised some cash by reducing corporate fixed interest exposure recently, and have now decided to raise liquidity further, typically by around 4% for most portfolios, by reducing the exposure to the Japanese stockmarket.

Our decision to reduce (or for some mandates sell outright) Japanese equities stems from our concern that the Japanese economy is particularly vulnerable to the now inevitable slowdown in global growth, especially a significant drop in external demand as the coronavirus grips western economies. It is felt that the slowdown in Japanese exports and business investment could be on a scale far greater than that seen in the 2008 global financial crisis and that no matter how much monetary and fiscal stimulus is thrown at the economy by the Japanese authorities, it will be insufficient to combat these external pressures. Additionally, the postponement of this summer's Olympics will undoubtedly pile pressure on the economy: the organisers estimated last year that the cost of hosting the games was in the region of $13bn, whilst other estimates place the figure at more than double this amount. Whatever the figure, the postponement will come with a further heavy price tag not just in terms of the decline in tourism, but also reputational damage and loss of 'face', factors that may be particularly difficult hurdles to negotiate.

For many clients the reduction in Japan is being effected through the sale of the Man GLG Japan CoreAlpha Equity Fund, a fund with an experienced management team and a good long term track record, but with a process that is firmly fixed on investments with a focus on 'value' rather than 'growth' opportunities. This style of investing tends to struggle when interest rate expectations are falling and monetary policy is loosening (i.e. where we are now). Given the expectation that the Japanese economy, and market, will lag other regions, and that Japan will find it difficult to respond positively to policy measures, we feel this fund in particular will now struggle to make headway.

One positive for Japan in recent weeks has been its currency, which often adopts safe haven status in times of trouble (something that stems from it frequently not being at the epicentre of global crises, and also from it historically being a net exporter, building up current account surpluses in the process, and therefore being a net creditor to the rest of the world). The Japanese yen's recent strength versus, for example, sterling has helped to cushion some of the market declines of late, but given the underlying weak outlook for Japan's domestic economy and its export market, the current partial insulation provided by currency gains cannot be assured going forward.

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It is ironic that, so far, Japan seems to have contained the coronavirus far better than other nations, yet economically we believe it stands to lose more relative ground to both its close Asian neighbours and those further afield. The proceeds from any sales we make will be retained in cash for the time being – this will serve both to increase the short-term protective buffer in portfolios from the continued threat and impact of the Covid-19 virus, whilst also providing us with greater liquidity should we wish to invest opportunistically in the near term.

If you have any questions on how this change affects your portfolio, or wish to discuss our investment positioning in more detail, please do not hesitate to get in touch with your Bordier UK investment manager or your professional adviser.

Risk warnings

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