JAPAN POST PRIVATIZATION AND THE DEMOCRATIZATION OF JAPANESE FINANCE

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Japanese risk assets—equities and real estate—are in a multi-year bull market, in our view. We are bullish on Japan because we believe the fundamental allocation of national assets—capital, land and labor—is beginning to change. If our thesis is correct, the net result should be a rise in economy-wide productivity in general, and in return on equity in particular. Public policy plays an important part in our structural bull thesis. The good news is that, on top of the general brand "Abenomics," more and more specific policy initiatives are now coming to fruition. Specifically, last week's privatization of Japan Post marks the beginning of a genuine privatization drive that confirms Japan's deep commitment to the pro-market and pro-private sector policy agenda. **Japan's Largest Service Sector Network Company** The Japan Post privatization has the potential to mark the start of a genuine revolution in Japan's service sector in general, and in its financial services in particular. After all, Japan Post is Japan's largest employer, it controls more branches and ATMs than all the private banks combined and is the second-largest holder (after the Bank of Japan) of government bonds. Although around 90% of the group's profits currently originate from its two financial services companies, Japan Post Bank and Japan Post Insurance, the overall business portfolio is very well diversified across the Japanese service sector—there are sizable operations in real estate, logistics and hospitality. For example, the Japan Post Group's real estate portfolio is similar in size to the major private sector realtors. The portfolio is well diversified, with post offices in prime locations offering huge potential for redevelopment. Leveraging Japan Post Group's high credit rating with its diversified real estate portfolio creates potential for Japan real estate investment trust (J-REIT) sponsorship with a wide range of opportunities, ranging from offices to hotels, health care, rental homes and logistics. Make no mistake: the size and depth of Japan Post Group's operations are significant enough to trigger change across the entire domestic service sector in Japan. **The Democratization of Finance Comes to Japan** The most immediate impact of the Japan Post privatization is poised to be in the financial services. As of the end of March 2015, the Post Bank's total assets stood at ¥209 trillion, which is similar to the three mega-banks. However, while the Post Bank has a very high share in the deposit market, it has a barely 1% share in the loan market. Moreover, its security portfolio is dominated by Japan government bonds (JGBs) Senior management has made it a clear objective to change this—the investment team is being built out quite aggressively, first and foremost by the appointment of former Goldman Sachs Japan vice-chairman of to the position of chief investment officer (CIO) earlier this year.Senior management is very vocal about wanting to promote an active and diversified asset management culture, which suggests a portfolio rebalancing away from government bonds and toward domestic equities and global securities. Here, it appears that Japan Post Bank is following the lead of the Government Pension Investment Fund (GPIF) public pension fund, which overhauled its leadership (also appointing a new, highly qualified CIO) and then dramatically revamped its asset allocation in late 2014. The implications of this go beyond the positive potential for a new source of demand for Japanese equities and non-yen global securities. Because of its vast retail network of 24,000 branches, Japan Post Group has the potential to bring true democratization of financial service to Japan. Senior management is openly seeking to leverage this branch network, looking to provide a potentially new range of financial products to the mass market retail investor. **Retail Asset Shift** In a nutshell: The Japan Post privatization may finally bring about the long-awaited shift of Japanese retail assets out of deposits (currently more than two-thirds of net financial wealth is in cash or demand deposits). Put in perspective: A 1% shift in Post Banks asset allocation yields about ¥2 trillion of new buying; if this were followed by a mere 0.25% shift in aggregate household financial asset allocation, another ¥4.25 trillion would follow. The scale of this is massive, as it adds up to roughly the total shift in the GPIF's asset allocation toward equities over the past 15 months.To be sure, we are only at the very beginning of the privatization process, and the actual mobilization of new portfolio products and strategies is bound to be a multi-year process. But the important thing is that a concrete path is now in sight. The democratization of Japanese finance has started, in our view.

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Bullish : a position that benefits when asset prices rise.

Return on Equity (ROE) : Measures a corporation's profitability by revealing how much profit a company generates with the money shareholders have invested.

Abenomics : Series of policies enacted after the election of Japanese Prime Minister Shinzo Abe on December 16, 2012 aimed at stimulating Japan's economic growth.

Japanese Government Bond (JGB) : A bond issued by the government of Japan. The government pays interest on the bond until the maturity date. At the maturity date, the full price of the bond is returned to the bondholder. Japanese government bonds play a key role in the financial securities market in Japan.

Credit ratings : An assessment of the creditworthiness of a borrower in general terms or with respect to a particular debt or financial obligation. Credit assessment and evaluation for companies and governments is generally done by a credit rating agency such as Standard & Poor's, Moody's or Fitch.

Japan real estate investment trusts (J-REITs) : Investment structure containing a basket of different exposures to real estate, be it directly in properties or in mortgages traded on the Tokyo Stock Exchange. Returns predominantly relate to changes in property values and income from rental payments.

Rebalance : An index is created by applying a certain set of selection and weighting rules at a certain frequency. WisdomTree rebalances, or re-applies its rules based selection and weighting process on an annual basis.

Government Pension Investment Fund (GPIF) : Japan's largest public pension fund.