

AFTER COVID: JAPAN'S CATCH-UP

Jeff Weniger — Head of Equity Strategy

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Better late than never. After a disappointing start to its vaccine rollout, Japan got on its feet in August, vaccinating as many as 1.58% of the population per day at the peak of the campaign. For context, the highest level of daily doses administered in the U.S. was 1.01% in April¹.

Though Japan's vaccination pace has tapered as the ranks of the inoculated builds, it's now in that zone where anyone who wants the vaccine can easily get it. Critically, more than four out of every five seniors have been fully vaccinated, with that cohort's proportion surpassing that of the U.S. in mid-August². Nevertheless, the younger age groups' vaccination rate still lags that of Western Europe and North America, though it appears a full catch-up with other [G7](#) members should be on the docket for next month.

With Japan no longer behind on COVID-19 vaccinations, its relative investment merit falls back on traditional metrics such as valuations and the matter of whether the country's shareholder friendliness is on the mend.

The latter is a particular sticking point.

Shareholder rights—or lack thereof—has long been an issue with Japan, particularly the far-too-ubiquitous scenario where corporations have piles of cash but pay peanuts in dividends. Year after year, the cash stockpile crushes profitability metrics such as [return on equity \(ROE\)](#) because the earned interest rate is in the basement.

Nevertheless, sometimes the story does not completely line up with the actual situation on the ground. MSCI Japan's component companies increased dividends at a 7% annual clip from 2012–2019. Perhaps more importantly, payouts were cut just 3% in reaction to COVID-19 lockdowns. That is a notably different experience than in most of the rest of the developed world (figure 1).

Figure 1: Dividend Growth, Developed Markets

Year	U.S.	Japan	Switzerland	Canada	Germany	France	U.K.
Annualized 2012–2019	6.9%	7.2%	4.3%	3.1%	4.2%	3.9%	2.3%
COVID-19 Year (2020)	2.7%	-2.9%	-2.8%	0.9%	-17.1%	-44.3%	-38.6%
Annualized 2012–2020	6.4%	5.9%	3.4%	2.7%	1.2%	-3.9%	-4.0%

Source: WisdomTree, MSCI. Dividend payments aggregated from MSCI ACWI constituents.

Suddenly the market finds itself in a scenario where the MSCI Japan index—long notorious for paltry dividends—exceeds the yield of the S&P 500 by 71 [basis points](#) (2.03% vs. 1.32%). Our own [WisdomTree Japan Hedged Equity Fund \(DXJ\)](#) yields 2.82%, about double what can be found in the U.S. broad market.

Additionally, DXJ's forward earnings multiple is 12.3, so its [earnings yield](#) is the reciprocal of that figure, 8.1%. In contrast, the [S&P 500's forward price-to-earnings \(P/E\)](#) multiple is 22.2; its earnings yield is just 4.5%.

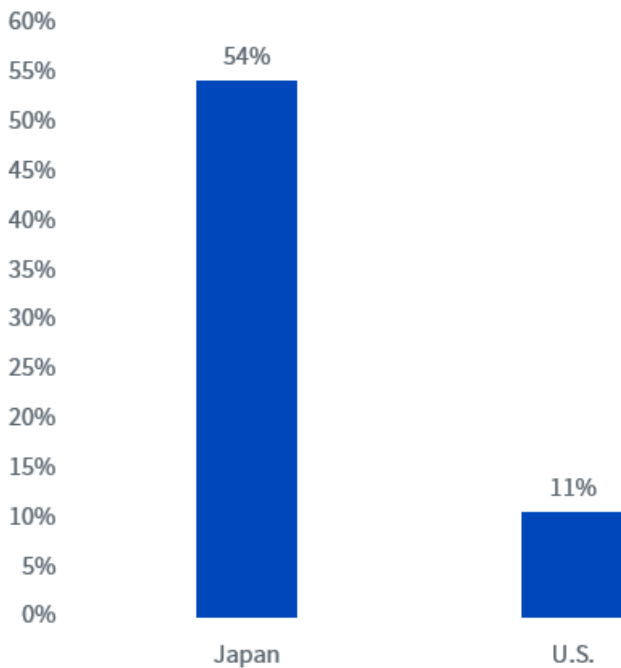
There are some promising developments for investors who itch for [dividend](#) boosts. With COVID-19 dominating global headlines, it was easy to miss the update to Japan's corporate governance code, which happened in June.

Notable developments include a new requirement that the number of independent board directors must increase from two individuals to one-third of the mix. Additionally, on board diversity, there is a push to put non-Japanese in senior management, potentially mitigating cronyism. Another initiative that may help Japan's stock market is a new requirement to publish disclosure materials in English.

Something else to note: a common instinct to self-insure at the household level, which may help Japan's economy hold

up better than others in the event of some systemic shock. To wit, over half of household assets are held in bank accounts or cash, about five times the U.S. proportion (figure 2).

Figure 2: Household Cash & Deposits as Percentage of Total Assets



Sources: Bank of Japan, Federal Reserve, as of Q1/21.

Things are clicking for Corporate Japan; with about 10 points of forward P/E “savings” in DXJ relative to the S&P 500, it could be a [contrarian](#) value play for investors willing to engage the world’s third-largest economy.

Beyond DXJ, two other mandates to investigate are the [WisdomTree Japan SmallCap Dividend Fund \(DFJ\)](#) and the [WisdomTree Japan Hedged SmallCap Equity Fund \(DXJS\)](#).

Unless otherwise stated, all data, as of 7/31/21, from WisdomTree Digital Portfolio Developer.

¹ Source: Our World in Data.

² Japan Reaches 100m COVID-19 Doses, Surpasses U.S. in Proportion of Older Folk Fully Vaccinated, Straits Times, 8/11/21.

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DEFINITIONS

G7 : The Group of 7 is a group consisting of Canada, France, Germany, Italy, Japan, the United Kingdom, and the United States.

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

Earnings yield : The earnings per share for the most recent 12-month period divided by the current market price per share. The earnings yield (which is the inverse of the P/E ratio) shows the percentage of each dollar invested in the stock that was earned by the company.

S&P 500 Index : Market capitalization-weighted benchmark of 500 stocks selected by the Standard and Poor's Index Committee designed to represent the performance of the leading industries in the United States economy.

Forward P/E ratio : Share price divided by compilation of analyst estimates for earnings-per-share over the coming 12-month period. These are estimates that may be subject to revision or prove to be incorrect over time.

Dividend : A portion of corporate profits paid out to shareholders.

Contrarian : Practice of seeing what the majority of market participants are focused on and attempting to look in the complete opposite direction.