

A stock exchange policy update opens a compelling case for Japan

Published 15 May 2023

Aneeka Gupta

Director, Macroeconomic Research, WisdomTree Europe

It's an exciting time for Japanese equities. Warren Buffett is turning his attention back to Japan. He raised his stake in each of the five major Japanese trading houses to 7.4% last week, from the original 5% he acquired in August 2020¹. Japan's trading houses ("sogo shosha") have deep roots in the country's economy, dating back hundreds of years and providing everything from energy to food. Given Buffett's penchant for value stocks, his investment strategy is reminiscent of companies trading at a steep discount, high dividend yields with lower risk. At present, Japanese equities are trading their deepest 29% discount to their long-term average, globally². It seems logical that Buffett's interest could pique further well priced investment opportunities in Japanese equities.

Source: Bloomberg, WisdomTree as of 20 April 2023. Please note: P/E refers to the Price to Earnings ratio defined as ratio for valuing a company that measures its current share price relative to its per share earnings.

Historical performance is not an indication of future performance and any investments may go down in value.

Economic re-opening effect more evident in consumption

In addition to Buffett's vote of confidence in Japanese equities, there are a number of other factors supporting the view that Japan could have an edge versus global equities. Unlike Western economies, Japan has only just begun reaping the full benefits of the re-opening of its economy following the COVID-19 lockdowns.

According to immigration statistics announced on 14 April, a total of 1.88mn foreign visitors entered Japan in March, up 23% from 1.53mn in February, reaching 70% of its pre-pandemic 2019 average³. The steady pick up in travel will help the economy normalise in the wake of the pandemic. Consumption is likely to benefit from the economic re-opening.

Spring in Japan is the season for Shunto, the annual wage negotiations between company management and unions. The strong wage growth delivered by the financial year 2023 should boost real household incomes and positively impact consumer sentiment. According to the March consumer confidence survey, the headline consumer confidence index rebounded to its highest level since April 2020⁴. The increase in wage hikes could also support a sustained recovery in consumption.

Implications of Tokyo Stock Exchange's (TSE) change in policy

Change is rarely fast in Japan. Almost a year has passed since the Japan Exchange Group doubled down on corporate governance enhancements.

The reforms were billed as the TSE's biggest overhaul in 60 years and a clear attempt to reinvigorate enthusiasm for Japanese equities.⁵

These initiatives included the restructuring of TSE's cash equity markets into three new segments: Prime Market, Standard Market and Growth Market—each segment having its own set of eligibility criteria. The ultimate impact of the reshuffle was muted. After three years of deliberation, the eventual requirements for the Prime Market were substantially weakened.

Nonetheless, the reforms represented a step forward for Japanese corporate governance. The TSE announced about half of its listed companies had a price-to-book ratio below 1x. According to the TSE, these companies are to disclose their policies and specific initiatives for improvement.

According to the TSE, all Japanese exchange-listed companies are required to meet the inclusion requirements of the market segments for which they are listed by 2025 or risk being labelled as securities under supervision or even delisting.

This means many historically cash-heavy Japanese companies face increasing pressure to improve their numbers, possibly by funnelling historically high excess cash reserves into increased buybacks or dividends.

Higher pay-out ratios by Japanese equities reflect the impact of TSE's policy change

It seems investors should dispel the myth that Japanese companies do not reward shareholders. Evident from the chart below, total pay-out ratios by Japanese companies have been steadily increasing since last year.

Source: Factset, WisdomTree as of 31 March 2023.

Historical performance is not an indication of future performance and any investments may go down in value.

1 Bloomberg as of 11 April 2023.

2 Bloomberg, WisdomTree as of 20 April 2023.

3 Immigration Services Agency of Japan, 14 April 2023.

4 Source: Bloomberg as of 31 March 2023.

5 Eri Sugiura and Leo Lewis, "Overhauled Tokyo Stock Exchange Makes Debut," The Financial Times, 4/4/22.

Related blogs

- + Yen's gains look capped
- + What's Hot: The stakes are high for the widow maker trade
- + Japan offers an avenue in a violent global value rotation

Important Risks Related to this Article

IMPORTANT INFORMATION

Marketing communications issued in the European Economic Area (“EEA”): This document has been issued and approved by WisdomTree Ireland Limited, which is authorised and regulated by the Central Bank of Ireland.

Marketing communications issued in jurisdictions outside of the EEA: This document has been issued and approved by WisdomTree UK Limited, which is authorised and regulated by the United Kingdom Financial Conduct Authority.

WisdomTree Ireland Limited and WisdomTree UK Limited are each referred to as “WisdomTree” (as applicable). Our Conflicts of Interest Policy and Inventory are available on request. For professional clients only. Past performance is not a reliable indicator of future performance. Any historical performance included in this document may be based on back testing. Back testing is the process of evaluating an investment strategy by applying it to historical data to simulate what the performance of such strategy would have been. Back tested performance is purely hypothetical and is provided in this document solely for informational purposes. Back tested data does not represent actual performance and should not be interpreted as an indication of actual or future performance. The value of any investment may be affected by exchange rate movements. Any decision to invest should be based on the information contained in the appropriate prospectus and after seeking independent investment, tax and legal advice. These products may not be available in your market or suitable for you. The content of this document does not constitute investment advice nor an offer for sale nor a solicitation of an offer to buy any product or make any investment. An investment in exchange-traded products (“ETPs”) is dependent on the performance of the underlying index, less costs, but it is not expected to match that performance precisely. ETPs involve numerous risks including among others, general market risks relating to the relevant underlying index, credit risks on the provider of index swaps utilised in the ETP, exchange rate risks, interest rate risks, inflationary risks, liquidity risks and legal and regulatory risks. The information contained in this document is not, and under no circumstances is to be construed as, an advertisement or any other step in furtherance of a public offering of shares in the United States or any province or territory thereof, where none of the issuers or their products are authorised or registered for distribution and where no prospectus of any of the issuers has been filed with any securities commission or regulatory authority. No document or information in this document should be taken, transmitted or distributed (directly or indirectly) into the United States. None of the issuers, nor any securities issued by them, have been or will be registered under the United States Securities Act of 1933 or the Investment Company Act of 1940 or qualified under any applicable state securities statutes. This document may contain independent market commentary prepared by WisdomTree based on publicly available information. Although WisdomTree endeavours to ensure the accuracy of the content in this document, WisdomTree does not warrant or guarantee its accuracy or correctness. Any third party data providers used to source the information in this document make no warranties or representation of any kind relating to such data. Where WisdomTree has expressed its own opinions related to product or market activity, these views may change. Neither WisdomTree, nor any affiliate, nor any of their respective

Officers, directors, partners, or employees accepts any liability whatsoever for any direct or consequential loss arising from any use of this document or its contents.

This document may contain forward looking statements including statements regarding our belief or current expectations with regards to the performance of certain assets classes and/or sectors. Forward looking statements are subject to certain risks, uncertainties and assumptions. There can be no assurance that such statements will be accurate and actual results could differ materially from those anticipated in such statements. WisdomTree strongly recommends that you do not place undue reliance on these forward-looking statements.

WisdomTree Issuer ICAV The products discussed in this document are issued by WisdomTree Issuer ICAV ("WT Issuer"). WT Issuer is an umbrella investment company with variable capital having segregated liability between its funds organised under the laws of Ireland as an Irish Collective Asset-management Vehicle and authorised by the Central Bank of Ireland ("CBI"). WT Issuer is organised as an Undertaking for Collective Investment in Transferable Securities ("UCITS") under the laws of Ireland and shall issue a separate class of shares ("Shares") representing each fund. Investors should read the prospectus of WT Issuer ("WT Prospectus") before investing and should refer to the section of the WT Prospectus entitled »Risk Factors¼ for further details of risks associated with an investment in the Shares.

Notice to Investors in Switzerland – Qualified Investors This document constitutes an advertisement of the financial product(s) mentioned herein.

In Switzerland, this communication is only targeted at Qualified Investors.

The prospectus and the key investor information documents (KIID) are available from WisdomTree's website: <https://www.wisdomtree.eu/en-ch/resource-library/prospectus-and-regulatory-reports>

For Investors in France: The information in this document is intended exclusively for professional investors (as defined under the MiFID) investing for their own account and this material may not in any way be distributed to the public. The distribution of the Prospectus and the offering, sale and delivery of Shares in other jurisdictions may be restricted by law. WT Issuer is a UCITS governed by Irish legislation, and approved by the Financial Regulatory as UCITS compliant with European regulations although may not have to comply with the same rules as those applicable to a similar product approved in France. The Fund has been registered for marketing in France by the Financial Markets Authority (Autorité des Marchés Financiers) and may be distributed to investors in France. Copies of all documents (i.e. the Prospectus, the Key Investor Information Document, any supplements or addenda thereto, the latest annual reports and the memorandum of incorporation and articles of association) are available in France, free of charge at the French centralizing agent, Societe Generale at 29, Boulevard Haussmann, 75009, Paris, France. Any subscription for Shares of the Fund will be made on the basis of the terms of the prospectus and any supplements or addenda thereto.

For Investors in Malta: This document does not constitute or form part of any offer or invitation to the public to subscribe for or purchase shares in the Fund and shall not be construed as such and no person other than the person to whom this document has been addressed or delivered shall be eligible to subscribe

for or purchase shares in the Fund. Shares in the Fund will not in any event be marketed to the public in Malta without the prior authorisation of the Maltese Financial Services Authority.

For Investors in Monaco: This communication is only intended for duly registered banks and/or licensed portfolio management companies in Monaco. This communication must not be sent to the public in Monaco.