



TALKING WITH



Sophia Li

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Talking shokunin kishitsu and Agatha Christie With Sophia Li, Portfolio Manager at FSSA Investment Managers and Richard Romer-Lee, Chief Executive Officer of Square Mile

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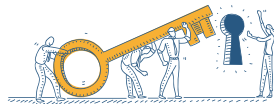
HOW DID YOU BECOME A FUND MANAGER?

I studied in Shanghai, majoring in statistics - which has always been a fascination of mine. I then pursued a Masters in statistics at Harvard. After several internships in finance I realised it was my passion and joined JPMorgan in Hong Kong as an equity research associate on the sell-side. But I wanted to move to the buy-side to become the final decision-maker and be in a results driven role. I was very lucky to join FSSA as an equity analyst. That was in 2009 and it has been a good fit.



HOW DID YOU FIND WORKING IN CHINA COMPARED WITH THE USA?

The differences were huge as you would expect - culture, communication style, work etiquette, mentality, practices, industry regulation, etc.



WHAT'S THE KEY TO INVESTING IN JAPAN?

There are a lot of opportunities and Japan has a very large investment universe, yet somehow it doesn't really appeal to global investors. Many investors feel that Japan has a lack of attractive macro stories. In fact, there are so many interesting companies which are not very well known to global investors.



If you want to invest in Japan, you must invest with an active manager with a bottom-up approach. More than 70% of listed companies in Japan are covered by only one analyst or have absolutely no analyst coverage. There are so many good companies but there's virtually no good quality sell-side research at all.

WHAT MAKES JAPANESE COMPANIES ATTRACTIVE?

There is an expression to describe the basis of some of the best Japanese companies - "shokunin kishitsu", which means craftsman's spirit.

A book called Obliquity suggests that if you want to achieve a certain goal you need to achieve it in an indirect way. For example, if a company's mission is to purely generate profit, they probably won't be that successful. So for good Japanese companies, usually they have a very strong social mission. They want to add value to their customers, they need to have strong trust with their suppliers and then they need to focus on innovation and naturally the profit will follow. As such they are usually very focussed on and committed to a specific area and to make their technology perfect.

Japanese companies are criticised for not focusing on shareholders returns, which is one of their weaknesses. Yet they do a good job of looking after stakeholders' interests. It's partly why society is stable and the quality of life has not been compromised at all despite thirty years of recession and deflation.



WHAT WERE THE MAIN DIFFERENCES BETWEEN THE SELL-SIDE AND BUY-SIDE?

The major difference is the decision-making part. On the sell-side the interpersonal skills are more important. The client was always right but you had to interest them in something else. The sell-side is about providing advice whereas on the buy-side the pressure is much higher as we are responsible for the results we generate for clients.



WHY JAPANESE EQUITIES?

I originally joined FSSA as an analyst to cover the Chinese market. At FSSA our culture is that all analysts and portfolio managers are sector generalists and each of us has country responsibilities, although we encourage each other to look outside our home market. So while my major responsibility was China, there were some major themes such as labour shortage and factory automation where I struggled to find companies to invest in. I started to look at Japan which is really a global leader in robotics and factory automation, and a large part of their revenue is generated from China.

Personally I have an interest in - or rather a fascination with - technology.

Japan has very strong technology and historical consumer brands which are benefitting from the rising number of middle classes and strong consumption growth in China and Asia. I gravitated more and more towards Japan and Japanese companies and eventually launched a Japan fund with Martin Lau.



DO YOU SEE PATTERNS EXPERIENCED IN JAPAN MANIFESTING THEMSELVES ELSEWHERE IN THE WORLD?

Yes, definitely - we are seeing the Japanification elsewhere. Europe, for example, looks a bit like Japan at the moment. The BOJ was the first to try out what was then the unprecedented QE policies, but despite this unfortunately in Japan there is no inflation at all. There is still a lack of growth but the innovative companies can still generate growth - in Japan and elsewhere.

Square Mile

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HOW IS RUNNING A FUND BASED IN A DIFFERENT COUNTRY?

The benefit is you can step back from all the noise. We usually take a long-term view, so we do need to know the companies well and need to spend lots of time on the ground. During Covid this has become more challenging as we can't travel, so we have kept in touch with companies via virtual meetings. Japanese management have adapted to this well.



HOW DO YOU FIND INTERACTION WITH COMPANIES IN JAPAN AS AN INVESTOR?

In Japan, the culture of the large conventional companies is completely different from the subset of businesses in which we invest. In the large companies, management are usually stubborn. They pursue conformity and for example promote people primarily on age rather than performance, which partially explains the struggling performance of the entire corporate Japan. Whilst there are more than 3000 other companies in Japan, there is a smaller group where this is not the case, where management thinks out of the box, makes quick decisions and have a low tolerance of complacency. These are the management we back.



WHAT'S THE ATTITUDE TOWARDS RESPONSIBLE INVESTING IN JAPAN?



There is some misunderstanding among global investors because Japanese companies are not as sophisticated in investor relations or information disclosure. They probably don't have ESG-rated disclosure at all, especially for medium-sized and smaller companies. It doesn't mean they don't do it – in fact they have done a great job in terms of environmental protection and social responsibilities. They have lagged behind in some areas, for example in gender diversity, where Japan is ranked near the bottom.

WHAT OPPORTUNITIES DO YOU SEE AT THE MOMENT?

There are huge opportunities in digitalisation. The IT literacy of companies is very low. Most companies – and I know this is hard to believe – still use pen and paper to do expense management and accounting work. The spending in IT services, especially software, will be a secular investment trend in Japan. The penetration of software as a service industry in Japan is very low, probably in the teens, compared to it being already over 50% in the United States and Europe. The same can be applied to consumers where ecommerce penetration is very low, even after the pandemic. It's still around 8% and digital - cashless - payment is around 25% whereas in China it's above 60% and in Korea it's close to 100%.

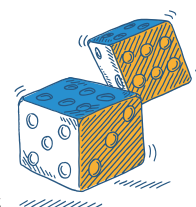


Another area is automation. In Japan there are a lot of globally competitive companies – for example more than half the robots in the world are made by Japanese companies and are backed by very sophisticated suppliers. An example of which is Keyence, the largest maker of machine vision systems which measure and detect any product defects and help guide the movement of robots.



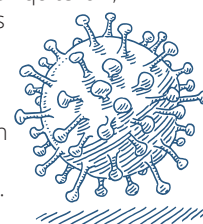
WHAT WORRIES YOU IN MARKETS?

The prolonged low interest rate environment which has elevated overall asset prices. As someone who tries to invest in quality companies, valuations are high and this concerns us as it suggests lower returns for our investors in future. I am also worried about the geo-political risk, such as the tension between the US and China and any event that could slow down global recovery.



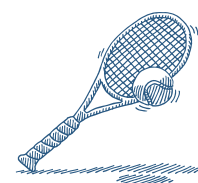
HOW HAS JAPAN COPED WITH THE PANDEMIC?

If I was to score it out of 10, probably a 5. The hospitalisation and death rates have been quite low, despite the ageing population. The focus has been on hygiene and good medical infrastructure. On the other hand the government hasn't done a great job to control it, partly because the constitution doesn't give them any power to shut down restaurants or shops, for example. The people are not very scared of Covid. The vaccination program has been accelerated which should help reach herd immunity.



HOW DO YOU RELAX?

I like to travel, which is of course impossible at the moment. Ordinarily I would spend less than half my time in Hong Kong as I would be on the road, for business and pleasure. I love being in Japan and am a big fan of the culture – back to the craftsman's spirit. The Japanese try to pursue perfection in every aspect in society. I play tennis, like reading and love thrillers and detective stories. My favourites include Sherlock Holmes and more recently Agatha Christie.



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