OYSTER FUNDS SYZ & CO

Product Flash

For professional, qualified and institutional investors only

March 2011

OYSTER Japan Opportunities

Excessive risk priced in at current levels?

Key Fund Features

- **OYSTER Japan Opportunities** offers investors an **active all-cap approach to Japanese equities**, with a **strong focus on stock selection** aiming to identify undervalued companies having a sound balance sheet, efficient business model and strong management.
- **Bottom-up value approach** seeking to single out the best investment candidates across **all market capitalizations** and without reference to the benchmark.
- **Seeks to achieve a positive absolute performance** through a diversified portfolio of **companies undergoing corporate change**, including restructuring, increased dividend payouts, share buybacks and M&A.
- **Morant Wright**'s long-term experience and specialisation on investing in Japan has proven to be highly **resilient in bear markets**, while at the same time able to **participate in bull markets**.
- **Performance and volatility ranking**: Over 3 years, the fund ranks within the 6th percentile in performance terms and 4th percentile in volatility terms. Over 5 years, the fund ranks within the 9th percentile in performance terms and 3rd percentile in volatility terms. (Figures provided are as of March 11th, 2011)

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Highlights

- **Economic impact of the earthquake and tsunami: the directly affected Tohoku region, a mainly agricultural and fishery area, accounts for 8% of GDP (vs. ca. 40% for the Tokyo area). Nuclear issue is easing as the race to repair damaged reactors and reconnect power is on, after temperatures of pools holding spent fuel roads being successfully brought down. Immediate consequence is the implementation of rolling black-outs imposed by Tokyo Electric Power Co (Tepco, 32% of Japan's power supply) meaning factories having to interrupt production.**
- **The Japanese have reacted extremely well with immediate government and Bank of Japan action, people have been remarkably calm and orderly, and whilst the nuclear question dominates the headlines, the fund managers would not be surprised if we look back on this as an exceptional buying opportunity.**
- **Very accommodating BoJ monetary policy should continue to be supportive. Yen strengthening to be short-lived, as asset repatriation not expected to materialize and BoJ expected to intervene as G7 did.**
- **Short-term economic slowdown obvious, but rebuilding efforts should fuel growth starting in Q3 and into 2012. However, some of the government's reconstruction financing will not be incremental, but merely diverted from other regions, hence rally in infrastructure and construction stocks ahead of fundamentals.**
- **Valuations extremely supportive, with market trading below book value and at a ca. 15x P/E (before Friday, now earnings became more uncertain), vs. 2x P/B and over 35x P/E in 1995 when the Kobe earthquake struck.**
- **OYSTER Japan Opportunities remained fully invested throughout the whole period, with no liquidity issue (70% of portfolio can be liquidated in 1 trading day). Managers view the market reaction as overdone and repositioned the portfolio by selling construction stocks that rallied on the back of the news and redeployed the monies into unloved sectors and stocks (eg. H2O, a department store stock), where share price reaction has been violent but long-term prospects remain intact. The Japanese market is cheap, but the fund is cheaper still, trading at a 0.68x P/B, in line with Morant Wright's value approach. No single stock accident to report in the portfolio.**

An early assessment of the situation in Japan

The fund managers have been asked by many clients to comment on the situation in Japan. In such a fluid environment it is extremely hard to make definitive statements and indeed the companies themselves are still working out their responses to the tragic events.

Ian Wright, one of the managers, was in Japan last week and ironically was interviewing Tokio Marine & Fire at the time of the earthquake. He flew back from Tokyo on Monday. Impressively there was very little damage in Tokyo with the skyscrapers all coming through unscathed.

Both the railways and the subway system were stopped on Friday night but after inspections were returned to normal on Saturday. The centre of Tokyo was exceptionally quiet over the weekend with many shops and restaurants shut. Department stores closed early. The more practical considerations of living were beginning to appear on Monday morning as the rolling power cuts instigated by Tokyo Electric Power started to take effect. There were queues outside petrol stations and torches were unavailable.

The government appears to be doing a very good job in what has been an extraordinarily difficult situation. Communication through press conferences with Prime Minister Kan and, perhaps more particularly, Chief Cabinet Secretary Edano, appears effective. They have also been very open in welcoming foreign assistance.

The nuclear situation is unfolding and whilst experts suggest that a catastrophe has been averted nobody can actually be sure at this stage. A degree of caution is natural. The chain of events has been effectively communicated to the public, but given the nuclear industry's historic record of concealing information there is a degree of scepticism and only an enquiry will determine who knew what when.

Companies are starting to instigate contingency plans. The Japanese are the best prepared nation for earthquakes but the tsunami has stretched them to the limit. Indeed Kan's comment that it faced a similar challenge to that after the world war is likely to see a response from the Japanese people. They are a resilient people and this call to patriotism may change sentiment as they rebuild parts of the country. The economy will clearly slow in the short term, with the main constraint being power supply rather than factory damage, but will recover as the reconstruction begins. Indeed it may provide a stimulus since little industry is in northern Japan. The Bank of Japan has been very quick to act and is supplying huge amounts of liquidity and has doubled to JPY 10trn its planned purchases of exchange traded funds, real-estate investment trusts, corporate debt and Japanese government bonds. Although the yen has strengthened there must be a limit to how far this will go. There would surely be no criticism of the Japanese if they intervened unilaterally given current circumstances.

The falls in the stock market have been large and even after the bounce over the past two days the indices have fallen well over 10%. Individual price movements have been pretty indiscriminate. From the fund managers' perspective the opportunities that this fall has thrown up are immense. Many stocks that they could not have dreamed of buying a few years ago are now trading below book.

Whilst short term volatility is likely to remain high, they are reshaping the portfolio to take advantage of these opportunities. The Japanese have reacted extremely well with immediate government and Bank of Japan action, people have been remarkably calm and orderly, and whilst the nuclear question dominates the headlines, the fund managers would not be surprised if we look back on this as an exceptional buying opportunity.