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Japan's Rally Has U.S. Advisers' Attention

By DAISY MAXEY

NEW YORK--Adviser Paul Winter, a long-time--and long-suffering--investor in Japan-focused stock funds in his own account, began adding exposure to Japanese-stock funds to his clients' accounts two years ago.

He stopped in November, as other investors began piling into the market when it rallied.

"I tend to be contrarian..., adding exposure on weakness," said Mr. Winter, who manages $30 million in assets at Salt Lake City, Utah-based Five Seasons Financial Planning LLC.

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He's far from reducing the positions he's built, but says he would "continue to be a better buyer on dips going forward." Mr. Winter is investing in the Japan Smaller Capitalization Common fund (JOF), a closed-end fund, and WisdomTree Japan Hedged Equity (DXJ), an exchange-traded fund. He wanted exposure with a fairly low correlation to U.S. markets in coming years, he said.

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Japanese investments are drawing some interest from advisers, who believe the nation's efforts to end deflation may offer more opportunity.

The Nikkei 225 index has gained nearly 20.7% this year and 25.3% in the 12 months through March 25, according to Morningstar Inc. With Prime Minister Shinzo Abe advancing a bold monetary and fiscal policy in an effort to lift the nation out of its decades-long deflationary environment and new central bank leadership in place, some advisers are giving Japanese stocks a new look.

Taizo Ishida, manager of the $144.7 million Matthews Japan Fund (MJFOX), said the fund is receiving modest inflows this year, but overseas investors are so far taking a back seat. He expects foreign investors to begin to get excited about Japan's story, too.

Matthews Japan Fund has gained nearly 12.1% this year through March 22 and 15.7% over the past 12 months, according to Morningstar. Mr. Ishida expects the rally to continue for several years, though not at the pace of the last three to four months.

"I think it's a little different from what I've seen over the last 15, 20 years," said Mr. Ishida, who's managed the Japan fund since 2006. He also manages the $547.9 million Matthews Asia Growth fund (MPACX), and has increased its exposure to Japan to 43% from 35% at the end of last year.

The country's previous government never put enough money into the marketplace, he said, and most Japan-watchers expect new Bank of Japan Gov. Haruhiko Kuroda will do more. With good execution by the bank, the yen--which has weakened to about 95 to the dollar from 79 in November--will likely weaken a bit further over the next 12 months, Mr. Ishida said. While Japan's monetary and fiscal policies are critical, he said, improvement also depends on a better global economy over the next year or two.

Campbell Gunn, manager of the $185.1 million T. Rowe Price Japan Fund (PRJPX), said the yen's move has taken a lot of pressure off Japan's exporters, but it's just the first part in what seems to be a fairly well-thought-out plan to help Japan recover.

Mr. Kuroda will attempt to be more aggressive in terms of monetary policy, and structural reforms may include Japan's agricultural, educational, taxation and social-security systems, Mr. Gunn said. Mr. Abe's agenda is an ambitious one, and the longer it takes, the harder it gets, he said.

T. Rowe Price Japan is experiencing inflows, but the first wave is generally from more aggressive, short-term investors, Mr. Gunn said. "It takes time for a move like this to be digested by longer-term investors," he said.

Japan's market has caught the eye of Chris Graff, director of asset management at Chicago-based RMB Capital Management, which manages $3 billion.

In the past, his firm avoided any big commitment to Japan "for a variety of reasons, including difficult demographics and corporate governance, along with persistent deflation," he said. But when stocks there recently began trading two standard deviations below historical valuations, and with the prime minister committed to a more aggressive monetary policy, he boosted clients' exposure.

The yen's depreciation is a sign that the market is taking the new policy seriously and that it may be sustainable, Mr. Graff said.

Adviser Helen "Cokie" Berenyi expects to see the rally continue. She began dipping her toe into Japan about three or four weeks ago, for the first time since before 2008. Ms. Berenyi, an adviser with Charleston, S.C.-based Alphavest.com, which manages about $32 million, has overweighted international assets in her clients' portfolio and is investing in iShares MSCI Japan Index (EWJ).

Write to Daisy Maxey at daisy.maxey@dowjones.com