Brandes Investment Partners
Japan Equity Strategy Notes
Second Quarter 2026 (1 April – 30 June 2026)

The Brandes Japan Equity Strategy returned 4.52% (gross of fees), underperforming its benchmark, the MSCI Japan Index, which gained 14.21% in the quarter.

Positive Contributors
Leading contributors included our holdings in industrials and consumer discretionary. Machinery companies OSG, Fuji Corporation, and Sintokogio rose significantly, as did electrical equipment firm Nidec. Within the consumer discretionary sector, automaker Honda Motor and distributor Paltac benefited performance. Paltac increased following an offer from Medipal, the majority owner, to buy the remainder of the company.

Other contributors included materials company Maruichi Steel Tube, chemicals firm Nihon Parkerizing, and financial services provider Sumitomo Mitsui Trust Group.

Performance Detractors
The primary drivers of our underperformance were our underweights to technology and financials, as well as our overweight to health care. Market enthusiasm toward any company related to artificial intelligence (AI) led the technology sector to rise significantly, and many of the portfolio’s largest relative detractors were holdings we didn’t own in this sector.

Conversely, health care stocks fell in aggregate during the period. Our pharmaceutical holdings Kissei Pharmaceutical, Astellas Pharmaceutical, Kaken Pharmaceutical, and Takeda Pharmaceutical all declined. Other detractors included entertainment and gaming companies Nintendo and Gungho Online Entertainment.

Select Activity in the Quarter
In line with global equity markets, the Japanese equity market (MSCI Japan) delivered a very strong quarter, driven largely by enthusiasm surrounding AI-related companies. Against this backdrop, we were exceptionally active, exiting 12 positions and initiating seven new investments during the quarter. While this level of turnover is highly unusual, it does not reflect a shift in our investment approach or a tactical response to market conditions. Instead, the activity highlights, in our opinion, our disciplined, bottom-up, value-oriented process, as elevated market optimism created opportunities both to realize value in existing holdings and to establish positions in companies trading at attractive discounts to our assessment of intrinsic value.

The numerous full exits represented a continuation of our process that had been underway for several quarters, as we progressively reduced position sizes across most of the holdings in anticipation of full exits as valuations exceeded our estimates of intrinsic value. The nature of these transactions is reflected in the stability of the portfolio's cash balance: despite divesting 12 positions and initiating only seven new investments, cash levels remained relatively unchanged. As discussed in greater detail below, we continued to identify what we consider attractive opportunities through ongoing fundamental research, even amid a strong Japanese equity market. This enabled us to redeploy capital into companies offering more compelling risk-reward profiles and wider discounts to our assessment of intrinsic value.

<u>Full Sells</u>
Oita Bank, Hachijuni Bank, Hyakugo Bank
For many years, the Japanese Equity portfolio maintained an overweight position in banks, including regional banks. As the Japanese monetary policy has shifted away from the decade-long period of ultra-loose conditions toward gradual normalization of tightening, interest rates have risen, along with valuations of Japanese banks. Given their low loan-to-deposit ratios and stable deposit bases, regional banks have been among the primary beneficiaries of higher interest rates, as reflected in recent improvements in net interest margins and returns on equity.

Market valuations have adjusted accordingly, with many regional banks now trading at meaningful premiums to book value. While we share the market's optimism regarding the improved earnings outlook and have revised our assessments of intrinsic value to reflect these changes, we have become increasingly concerned that current valuations assume a sustained period of excess returns above the cost of capital. This scenario could possibly materialize, but the assumption also comes with downside risk. As a result, we determined that the risk-reward profile of these investments had become less compelling and elected to exit the portfolio's three regional bank positions.

Fuji Corporation, Shikoku Kasei, and C.Uyemura
While the three companies operate in distinctly different businesses—Fuji Corporation manufactures semiconductor chip mounters, whereas Shikoku Kasei and C. Uyemura are niche specialty chemical suppliers—the market valuations of all three appeared to benefit significantly from growing investor enthusiasm for companies with exposure to AI-related demand. For Fuji Corporation, orders for chip mounters have increased alongside rising investment in data centres and advanced semiconductor manufacturing. Shikoku Kasei and C. Uyemura, meanwhile, supply specialized chemicals used in semiconductor production and advanced packaging applications.

Similar to our review of the regional banks, we revisited and increased our estimates of intrinsic value to reflect the improving demand outlook for each business. However, despite these favourable fundamental developments, market valuations rose even more rapidly and, in our view, came to well exceed our revised estimates of intrinsic value by a meaningful margin. Subsequently, we elected to exit all three positions and redeploy capital into opportunities offering what we consider more attractive risk-adjusted return potential.

Ezaki Glico, Kyocera, NIDEC, SMC
The common themes across these four investments were: (1) activist involvement driving improvements in corporate governance and capital allocation, with the potential to enhance shareholder returns, and (2) a weaker yen supporting earnings growth. Excluding NIDEC, all three companies maintained inefficient balance sheets that became targets for activist engagement. Given our longstanding view that excess capital was undervalued due to limited deployment, activist involvement has helped unlock some of this value through increased dividend distributions and share repurchases and has increased optimism that further value will be unlocked.

While the weaker yen has provided an earnings benefit from a reporting perspective as results are translated into yen, many Japanese companies today are more closely matched in currency with revenues and costs. As a result, we do not believe yen weakness confers a meaningful structural advantage that would warrant a higher assessment of these companies’ competitive positions or long-term ability to generate excess returns.

Accordingly, following a comprehensive review of recent earnings and valuations, we concluded that the incremental upside had become less compelling relative to alternative opportunities. With governance improvements increasingly reflected in share prices and no change to our assessment of the companies' long-term competitive advantages, we elected to exit the positions and redeploy capital into investments offering what we see as a more favourable risk-reward profile.

Japex, Nippon Seiki
The sale rationale for Japan Petroleum Exploration (Japex) was relatively straightforward. While the company's earnings are positively correlated with oil prices, the sharp increase in oil prices following the conflict involving Iran drove a significant re-rating of the shares. In our view, the resulting valuation more than reflected the likely long-term economic benefit to the company. Furthermore, Japex is not a pure-play oil producer, and a meaningful portion of its earnings is derived from businesses that are less directly exposed to movements in oil prices. As a result, we were increasingly sceptical that the market valuation appropriately reflected the company's underlying earnings power and long-term fundamentals. Following a review of the risk-reward profile, we elected to exit the position.

Nippon Seiki was a long-term holding for which our investment case was based on its strong balance sheet and our expectation that operating performance would improve over time. More recently, consistent with broader trends across corporate Japan, management undertook measures to enhance shareholder returns through increased dividends and share repurchases. Operating performance also improved meaningfully as the business recovered from the pandemic-related downturn and benefited from cost restructuring initiatives, despite its continued exposure to the cyclical automotive industry and, in particular, Honda.

Following a comprehensive review of the company's intrinsic value and alternative investment opportunities, including the addition of Toyota to the portfolio, we concluded that the shares had exceeded our revised estimate of intrinsic value. In addition, we believed that reallocating capital from Nippon Seiki into Toyota offered a more attractive risk-reward profile while enhancing overall portfolio diversification. Accordingly, the position was divested.

<u>New Buys</u>
Toyota, Shimano, T.Hasegawa, Toagosei, Unicharm, Morinaga, Sysmex

The seven new additions to the portfolio this quarter span a diverse range of industries, including automobiles, specialty chemicals, consumer products, and medical devices, as well as a broad spectrum of market capitalizations. This reflects our bottom-up, benchmark-agnostic approach to identifying undervalued businesses across Japan.

Despite the differing end markets, there are two common themes across these investments. First, each company maintains a strong balance sheet that we believe positions it well to withstand periods of economic weakness. Second, near-term earnings are being pressured by cyclical or transitory challenges that, in our view, have created attractive valuation opportunities. Examples include Sysmex and Unicharm, which have faced headwinds in China; Shimano, which continues to navigate post-pandemic demand normalization; T. Hasegawa and Morinaga, where concerns surrounding international acquisitions have weighed on investor sentiment; and Toyota, where broader concerns regarding the long-term evolution of the automotive industry continue to overshadow the company's underlying strengths.

It is in situations such as these where we believe our research process can add value. Through rigorous fundamental analysis and our collective experience that has navigated multiple market cycles over several decades, we seek to distinguish temporary challenges from permanent impairments. While we readily acknowledge that not every investment thesis will develop as expected, our disciplined focus on purchasing companies at meaningful discounts to estimates of intrinsic value provides a margin of safety for the portfolio, helping limit downside risk potential.

We are pleased to have added these investments during the quarter and are excited by their long-term prospects.

Current Thoughts
Consistent with last quarter, portfolio activity remained unusually high, with both new purchases and full exits reaching levels that are rare in the history of the strategy. We would emphasize, however, that these investment decisions were not driven by a top-down market outlook or tactical positioning in response to recent market movements. Rather, they reflected our disciplined, company-specific assessment of intrinsic value and risk-reward opportunities.

Following the strong performance of Japanese equities over the past two years, many of our holdings have approached or exceeded our estimates of intrinsic value. As a result, should market strength continue, we would expect to continue trimming or exiting positions where the valuation no longer provides an adequate margin of safety. This could result in a higher cash balance in the near term if suitable replacement opportunities are not immediately available.

At the same time, we remain actively engaged in identifying new investment opportunities, as demonstrated by the addition of seven new positions during the quarter. While we acknowledge that the current market environment is not necessarily ideal from a value investor's perspective, we remain confident that attractive opportunities continue to exist in Japan for investors willing to take a long-term, company-specific approach. We therefore remain focused on patiently allocating capital to businesses trading at meaningful discounts to our estimates of intrinsic value while maintaining the discipline to realize gains when that discount narrows.

Conclusion
It is remarkable how dramatically sentiment and market outcomes can shift in just a single quarter. In our previous commentary, we highlighted concerns regarding potential downside risks should the conflict involving Iran persist for an extended period. We noted that higher oil prices, broader input cost pressures, and a weak yen could negatively affect Japan's economy and corporate profitability. Instead, equity markets delivered exceptionally strong returns, driven in large part by continued enthusiasm surrounding artificial intelligence despite ongoing geopolitical uncertainties. Such outcomes serve as a reminder of the inherent difficulty of forecasting short-term market movements and reinforce why we strive to remain focused on long-term fundamentals rather than daily market fluctuations.

As long-term value investors, we remain firmly committed to a fundamental, bottom-up investment approach centered on intrinsic value. Periods of market optimism often create opportunities for us to be more active sellers should holdings approach our estimates of intrinsic value, while periods of uncertainty frequently provide opportunities to acquire potentially mispriced businesses at attractive valuations. We recognize that this discipline can, at times, result in a portfolio that looks meaningfully different from the benchmark and may lead to periods of relative underperformance. While such outcomes are never desirable, they are a natural consequence of an index-agnostic investment approach focused on long-term value creation rather than short-term benchmark considerations.

Our commitment remains unchanged: to apply a consistent and disciplined investment process that we believe will generate attractive long-term results for our clients. Maintaining conviction during more challenging periods can be difficult, but our confidence continues to be grounded in the strength of our research process, the experience of our investment team, and the belief that intrinsic value ultimately drives long-term investment outcomes.

Finally, while this quarter was a challenging one, we sincerely appreciate the continued confidence you place in us to manage the Japan Equity portfolio on your behalf. We are honoured to serve as stewards of your capital and remain committed to a disciplined, and consistent investment approach focused on achieving the best possible long-term outcomes within our control.

We always welcome discussion regarding the portfolio, our investment process and philosophy, or the firm more broadly, and encourage you to reach out at any time. Constructive feedback and observations are greatly valued, and we deeply appreciate the longstanding relationships we have built over the years. It is a privilege to manage the portfolio on your behalf.

For term definitions, please refer to https://www.brandes.com/emea/termdefinitions.

For index definitions, please refer to https://www.brandes.com/emea/benchmark-definitions.