Harris | Oakmark

QUARTERLY MANAGER COMMENTARY

Japan Strategy

June 30, 2026

MARKET ENVIRONMENT

Japanese equities rose over the quarter, led by technology and AI-linked names that continued to attract strong investor demand. The Bank of Japan's ongoing shift away from ultra-loose policy was a central theme, culminating in a rate hike that markets read as a vote of confidence rather than a threat, since it signaled underlying economic durability and gave policymakers more room to respond to future downturns. Inflation pressures built steadily, driven in part by rising energy costs tied to Middle East tensions, though optimism around progress toward a resolution helped ease some of those concerns as the quarter wore on. A weaker yen also supported the advance, boosting the earnings outlook for export-oriented companies, even as it kept policymakers alert to the possibility of currency intervention. Resilient earnings and continued foreign investor interest rounded out the supportive backdrop for the quarter.

Performance highlights

Contributors

- Hamamatsu Photonics
- MISUMI Group
- Sumitomo Mitsui Financial

Detractors

- Sugi Holdings
- Toyota Motor
- TISI

PORTFOLIO PERFORMANCE

The portfolio's return was 9.17% (net) for the reporting period. This compares to the MSCI Japan Index (Net) that returned 14.21% for the same period.

Top contributors:

- Hamamatsu Photonics was a contributor during the quarter. The Japan-headquartered photonics company — the world's leading maker of photodetectors and optical sensors — saw its stock price rise after reporting results that beat consensus earnings before interest and tax estimates coupled with a significant raise to full-year guidance, driven primarily by strong semiconductor-related demand, particularly for inspection equipment, on the back of the generative-AI investment cycle. We continue to believe this is a dominant company with robust shareholder returns that trades, on our estimate, at a significant discount to intrinsic value.
- MISUMI Group was a contributor during the quarter. The Japan-headquartered industrial components supplier's stock price climbed during April. The company reported year-over-year growth in revenue and profit and announced a new YEN 30 billion share buyback. We met with management and continue to monitor the MISUMI's future prospects.
- Sumitomo Mitsui Financial was a contributor during the quarter. The Japan-headquartered diversified bank's stock price appreciated and it delivered solid full-year earnings, with profit growing strongly and revenue rising steadily. We continue to believe that Sumitomo Mitsui Financial is a well-run Japanese megabank, reflected in prudent lending and strong returns on equity. We value its solid balance sheet and see ample growth opportunities.

Top detractors:

- Sugi Holdings was a detractor during the quarter. Shares of the Japan-headquartered pharmacy retailer declined during the period, despite reporting fiscal-year 2026 results that showed healthy year-over-year growth in both sales and net income. Investor sentiment weakened following the release of fiscal-year 2027 guidance, which implied a decline in net income and earnings per share due to higher planned capital expenditures and the rollover of one-off benefits. We continue to believe Sugi is well positioned to benefit from the expanding role of drugstores in prescription dispensing.
- Toyota Motor was a detractor during the quarter. The Japan-headquartered automaker grew revenue but earnings were weak, as tariffs, rising costs, and stiffer competition weighed on profitability, with management guiding to further pressure ahead. We continue to believe that Toyota is a well-run global manufacturer, reflected in its scale, cost discipline, and industry-leading hybrid franchise. We value its strong balance sheet and see a path back to earnings growth over time, though we are mindful of the near-term headwinds.
- TISI (formerly TIS) was a detractor during the quarter, with the shares falling on AI-related fears despite solid fundamentals. The Japan-headquartered IT consulting and services company posted a modest beat, and the quality was better than the headline suggests, in our view: the loss-making projects that had weighed on recent quarters faded, while orders and backlog rebounded strongly. Guidance came in slightly above expectations, and capital allocation remains excellent, with a steadily rising dividend alongside a buyback set to return most of next year's free cash flow. We see the integration of subsidiary INTEC as a catalyst for improved profitability and think there is a runway for future growth.

PORTFOLIO POSITIONING

We did not initiate any new positions during the period.

We eliminated the following position(s) during the period:

- Cosmos Pharmaceutical
- PERSOL HOLDINGS

OUTLOOK

A large part of the recent underperformance is due to our lack of direct AI investments as well as ownership of companies that are perceived to be threats from AI such as the System Integrators. While AI stocks could continue to move higher based on sentiment and earnings growth, we don't find the valuations in that part of the market to be attractive. We do have indirect exposure to AI via system integrators and semiconductor component companies, where we find valuations to be more attractive and stock specific fundamentals appealing. While there is a concern in the market that the SIers will be displaced by AI, we do not share these views and believe the recent weak stock performance is an opportunity. Also, the portfolio is still positioned defensively overall (although less so than a few months ago), which has led to underperformance as stocks rallied earlier in the quarter. However, fundamentally, our companies are still delivering strong earnings growth on the whole and we continue to find more value in domestic-oriented businesses as well as small and mid-cap companies.

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AVERAGE ANNUALIZED TOTAL RETURNS (%)

	QTD	YTD	1 yr	3 yrs	5 yrs	10 yrs	Since inception
Japan Strategy Gross of Fees	9.36	3.00	9.22	14.05	7.55	10.79	9.88
Japan Strategy Net of Fees	9.17	2.62	8.41	13.21	6.75	9.96	9.07
MSCI Japan Index	14.21	15.78	29.11	18.49	9.49	9.84	8.39
TOPIX (JPY)	11.98	14.34	27.32	18.54	9.65	9.85	8.67

Returns for periods less than one year are not annualized. Composite inception: 08/31/2011

Past performance is no guarantee of future results. *Current performance may be lower or higher than the performance data quoted. The gross performance presented above does not reflect the deduction of investment advisory fees. All returns reflect the reinvestment of dividends and capital gains and the deduction of transaction costs. The client's return will be reduced by the advisory fees and other expenses it may incur in the management of its account. The advisory fee, compounded over a period of years, will have an adverse effect on the value of the client's portfolio.*

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All investments carry a certain degree of risk, including possible loss of principal. There is no assurance that an investment will provide positive performance over any time period. Equity investments are subject to market risk or the risk that stocks will decline in response to such factors as adverse company news or industry developments or a general economic decline. Non-U.S. investments involve risks such as currency fluctuation, political and economic instability, lack of liquidity and differing legal and accounting standards. These risks are magnified in emerging markets.

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Glossary

The **MSCI Japan Index (Net)** is designed to measure the performance of the Japanese equity market. The index includes large- and mid-cap stocks and covers approximately 85% of the free float-adjusted market capitalization in Japan. This benchmark calculates reinvested dividends net of withholding taxes. This index is unmanaged and investors cannot invest directly in this index.

The **TOPIX**, also known as the Tokyo Stock Price Index, is a capitalization-weighted index of all companies listed on the First Section of the Tokyo Stock Exchange. This index is unmanaged and investors cannot invest directly in this index.

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