

QUARTERLY MANAGER COMMENTARY  
**Japan Strategy**

March 31, 2024

**MARKET ENVIRONMENT**

Japanese equity markets rose during the first quarter of 2024, led by large cap and semiconductor-related companies, exporters, and generally low quality stocks. The Bank of Japan enacted its first rate hike since 2007 and exited negative interest rate territory. We view this as a meaningful step toward normalizing the country's monetary policies, as we continue to believe the hyper accommodative policy by the Bank of Japan is unsustainable over the medium and long term. This is an area we are watching closely as it directly impacts our holdings in financial companies, like Sumitomo Mitsui Financial Group and Sumitomo Mitsui Trust. The yen lost value relative to the U.S. dollar during the quarter, ending around 151 USD/JPY.

**PORTFOLIO PERFORMANCE**

The portfolio's return was 3.01% (net) for the reporting period. This compares to the MSCI Japan Index that returned 11.01% for the same period.

Top contributors:

- Toyota Motor was a contributor during the quarter. In February, the Japanese automobile company's stock price rose following the release of fiscal-third quarter results that surpassed consensus expectations. Toyota announced a \$1.3 billion investment at its Kentucky facility to support future electrification efforts, such as the previously announced battery electric vehicle assembly and a new three row battery electric SUV for the U.S. market. In March, Toyota North America reported February vehicle sales that bested consensus expectations. The company

**Performance highlights**

**Contributors**

- Toyota Motor
- Sumitomo Mitsui Financial
- Sumitomo Mitsui Trust

**Detractors**

- OMRON
- TechnoPro Holdings
- Cosmos Pharmaceutical

also announced that it will sign a new agreement with Keikyu Corporation, following the 2020 agreement, to transfer a portion of land as well as joint construction, which will be used to open a new Tokyo head office in 2030. We continue to believe Toyota offers attractive upside.

- Sumitomo Mitsui Financial was a contributor during the quarter. In February, the Japanese bank reported fiscal third-quarter 2024 results, with an increase in both ordinary income and profit from fiscal third-quarter 2023 results. In March, the company completed the acquisition of the remaining 25.1% stake in SMFG India Credit Company and it's up to YEN 150 billion share buyback. In our view, Sumitomo Mitsui Financial is the best run Japanese megabank in terms of prudent lending and it has the highest return on equity of the three largest banks historically. We also appreciate that the company has a strong balance sheet, which adds to our confidence in this investment.

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- Sumitomo Mitsui Trust was a contributor during the quarter. In January, the Japanese financials firm reported fiscal third-quarter results and announced a share buyback of up to 10 million shares for up to YEN 20 billion. The buyback was completed in March. In our view, Sumitomo is positioned to benefit from improved gross domestic product, credit growth and higher asset prices. Moreover, we think the company has one of the best management teams of the Japanese banks that focuses on the right things, including retaining cost efficiency and increasing fees, among others.

Top detractors:

- OMRON was a detractor during the quarter. The Japan-headquartered technology company's stock price fell following the release of fiscal third-quarter results. Operating profit missed consensus expectations substantially and management approximately halved fiscal full-year operating profit guidance and lowered its guidance for revenue as well. In March, we met with CEO Junta Tsujinaga to discuss the company's fiscal third-quarter results. We appreciate Tsujinaga's high standards for OMRON and the fact that he is using the company's poor results as an opportunity to make improvements. We will continue to monitor the situation and believe in the long-term prospects of the company.
- TechnoPro Holdings was a detractor during the quarter. The Japan-headquartered human resources technology company released fiscal second-quarter results with revenue and core operating profit beating consensus expectations for both the fiscal second-quarter and first-half periods. Fiscal full-year 2024 guidance remained unchanged, with net income attributable, revenue and earnings metrics falling slightly

below consensus expectations. We continue to believe in the long-term prospects of TechnoPro Holdings.

- Cosmos Pharmaceutical was a detractor during the quarter. In January, the Japanese drug store operator released fiscal first-half of 2024 results. Fiscal full-year guidance included net income attributable, revenue and earnings metrics all missing consensus expectations. We continue to appreciate that Cosmos Pharmaceutical is a strong organic grower in the already attractive Japanese drug store industry, which is benefiting from an aging society, increasing rate of drugs dispensed outside hospitals, market share gains from traditional supermarkets and general merchandise stores, and drug store consolidation.

**PORTFOLIO POSITIONING**

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

- Bunka Shutter is one of Japan's leading providers of residential and industrial shutters. The company operates in a vertically integrated oligopolistic market structure characterized by rational pricing and attractive domestic returns. We believe there is significant scope for margin improvements at Bunka as the company underearns peers and has an opportunity to improve the manufacturing process in its doors business. Additionally, we think the company's capital allocation policies will improve following pressure from two activist shareholders. We believe Bunka presents an attractive investment opportunity as we were able to purchase shares in the company at a discount to competitors and our estimate of intrinsic value.

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- NIFCO designs and manufactures plastic parts and components primarily for the automobile industry. The company serves a niche market with steady demand driven by car manufacturers' desire to reduce vehicle weight and improve aesthetics. We like that automobile components is a fundamentally attractive and structurally growing category, and appreciate that the company's flexible cost structure protects profitability in adverse economic environments. We have also been pleased by NIFCO's improved governance under the guidance of a new management team, which has led to increased capital returned to shareholders. We were able to purchase NIFCO shares at a discount to our estimate of intrinsic value despite the company's attractive fundamental outlook.

During the period we eliminated Hirose Electric and Kansai Paint from the portfolio.

### OUTLOOK

While we keep a watchful eye on the macroeconomic environment, we remain focused on our bottom-up, fundamental analysis at the company level when constructing portfolios. We invest in businesses priced at substantial discounts to our estimate of intrinsic value, that we believe will grow per share value over time, and have management teams that think and act like owners. Our analysts are generalists who remain industry agnostic and focused on finding value, regardless of what is in favor at any given moment. We believe this positions our portfolios for sustainable, long-term success.

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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.

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