FRANKLIN TEMPLETON | ClearBridge

International Value Strategy



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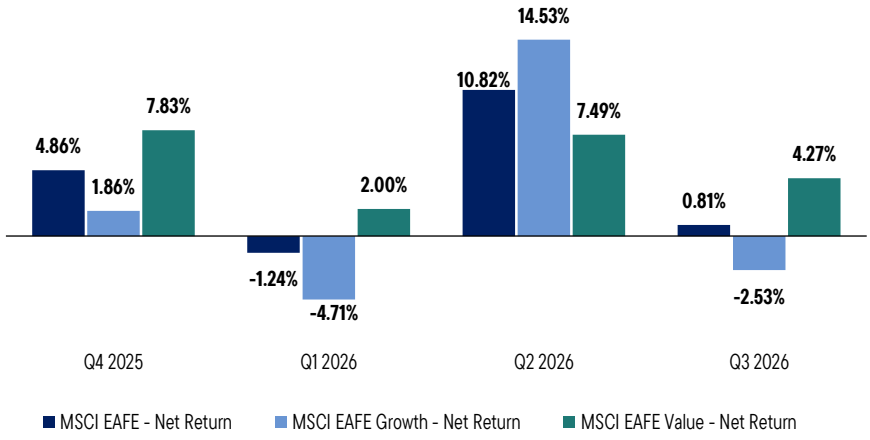
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- Value, energy and financials led a modest third-quarter gain in international equities, while a late-July selloff in AI-linked chip stocks and rising bond yields weighed on technology and rate-sensitive areas, respectively.
- The Strategy underperformed its benchmark, as stock selection in AI-exposed IT holdings outweighed strong contributions from Japanese, Korean and Greek banks and our overweight to energy.
- We see opportunity in long-term growers sold off on near-term rate and inflation headwinds and in election-driven dislocations in France and Brazil.

Market Overview

International equities posted modest gains in the third quarter, as a sharp rotation away from AI-linked technology stocks and toward value, energy and financials offset the drag from rising bond yields. The benchmark MSCI EAFE Index returned 0.8%, while the MSCI EAFE Value Index gained 4.3% and the MSCI EAFE Growth Index declined 2.5%.

Exhibit 1: MSCI Growth vs. Value Performance



As of September 30, 2026. Source: ClearBridge Investments, Atlanta Fed, Bloomberg Finance.

AI was the main source of volatility. In late July, Asian chip stocks sold off as investors questioned valuations amid concerns over how AI infrastructure spending would be financed and over intensifying competition from China, with memory and semiconductor equipment makers in South Korea and Japan hit hardest, leaving information technology (IT) the weakest sector in the benchmark. Energy moved the other way, as continued conflict with Iran kept oil supply at risk and

drove crude prices sharply higher, making energy the benchmark's best-performing sector for the quarter.

Higher energy prices also pushed central banks toward tighter policy. The Federal Reserve raised rates in September for the first time since 2023, and the European Central Bank (ECB) and the Bank of Japan (BoJ) also raised rates, sending bond yields higher and weighing on rate-sensitive utilities and real estate. By region, both Japan and Asia Ex Japan gained, with banks supported by the prospect of higher rates. U.K. stocks posted a small gain, while European stocks declined with French assets pressured by concerns over the country's public finances.

The third quarter showed how quickly crowded positioning in the AI trade can unwind.

The factor backdrop was unusually polarized. Value, yield and low volatility factors posted strong gains over the quarter, while growth and momentum fell sharply.

Performance Overview

The ClearBridge International Value Strategy underperformed its MSCI EAFE benchmark during the third quarter, as stock selection in IT, concentrated in AI-exposed hardware and semiconductor holdings, outweighed strong results in financials and energy. Sector allocation was positive overall, helped by our overweight to energy and underweights to health care and consumer staples, but the quarter was overwhelmingly a stock selection story.

Within IT, South Korean memory makers SK Hynix and Samsung Electronics, Japan's Murata Manufacturing and Germany's Infineon Technologies all declined as the AI hardware trade unwound. SK Hynix reported sharply higher second-quarter operating profit but missed lofty expectations, and its shares fell further in the late-July chip selloff. Murata, the largest maker of the multilayer ceramic capacitors used to regulate power in AI servers, had been one of the engines of Japan's first-half rally, which left it exposed when sentiment turned. Infineon fell even after reporting record quarterly sales driven by its AI data center business. Not owning ASML, Kioxia and Tokyo Electron partly offset these losses.

In materials, building products companies Amrize and Wienerberger detracted as construction end markets remained subdued and higher rates pushed out expectations for a more meaningful housing recovery.

Several of our long-duration defensive holdings were also caught in the rate move. Renewable power producer Brookfield Renewable fell as surging bond yields weighed on rate-sensitive utilities.

Financials were the largest contributor to relative performance. Mitsubishi UFJ Financial became Japan's most valuable company in July on expectations that Bank of Japan rate increases would lift earnings. Shinhan Financial posted record quarterly net profit and approved another share buyback. Greek lender Piraeus Bank reported record first-half profit and, with Greece reclassified as a developed market, rejoined the Stoxx Europe 600 Index in September.

Energy was a useful diversifier during periods when IT and industrials struggled. Our overweight benefited as oil prices climbed, and

Canadian oil sands producer Cenovus Energy reported record oil sands production and strong free cash flow in the second quarter.

Portfolio Positioning

In Japan, we swapped Daito Trust Construction, a builder and manager of rental housing, for a new position in East Japan Railway (JR East), the largest passenger rail operator in Japan. We believe JR East is a direct beneficiary of Japan's shift to sustained inflation, which is restoring pricing power to a business whose fares were essentially frozen for decades. The company implemented its first broad-based fare increase since its 1987 privatization in March 2026, and we expect fare revisions and rising inbound tourism to drive operating leverage on a largely fixed cost base.

Beyond rail, JR East owns a valuable and, in our view, underappreciated portfolio of real estate around its stations, anchored by the newly completed Takanawa Gateway City development in central Tokyo. Management's focus on capital efficiency, including recycling mature property assets and raising shareholder returns, offers a path to higher return on equity, yet the shares trade at what we view as a meaningful discount to the combined value of the rail franchise and property portfolio.

We also exited Arcos Dorados, the largest McDonald's franchisee in Latin America, as consumer spending remained challenged and raw material inflation proved sticky, and reallocated the proceeds to higher-conviction holdings.

In France, we used the selloff in French equities to add to AXA and BNP Paribas. Both have been de-rated alongside the domestic market on concerns over France's public finances and political gridlock, even though most of their earnings are generated outside France and their capital positions and shareholder return plans remain intact.

In energy, we added meaningfully to Shell and Cenovus, consistent with the constructive medium-term view on oil prices that supported our initial Cenovus purchase in the second quarter. At the same time, we trimmed SK Hynix and Siemens Energy, lowering our exposure to the AI hardware and power equipment complex.

Outlook

The third quarter showed how quickly crowded positioning in the AI trade can unwind. We remain constructive on the long-term prospects of the AI infrastructure buildout, but we expect continued volatility as investors weigh the scale of that spending and how it is financed. At the same time, an energy shock tied to the Iran conflict has pushed the ECB, the BoJ and the Fed toward tighter policy, reinforcing a higher-for-longer global rate backdrop that we believe favors valuation discipline, cash flow durability and balance sheet strength.

That said, we see scope for relief from the difficult combination of sticky inflation and rising long-term yields as we move toward year-end and into 2027. Much of the recent inflation impulse has come from energy, and year-over-year comparisons should become more favorable as the initial oil shock annualizes. With the ECB, BoJ and Fed having already

tightened, markets have priced a meaningful amount of policy restriction, and long-term yields now embed an elevated term premium that could compress as inflation data moderate.

The quarter's rotation has created what we view as an attractive opportunity in long-term growers that sold off on near-term headwinds. Utilities and infrastructure owners such as National Grid, Brookfield Renewable and Brookfield Infrastructure were among the hardest hit by rising yields, yet their growth runways, driven by grid investment, electrification and rapidly rising power demand from data centers, have arguably lengthened. Select health care and consumer staples have de-rated to valuations that we believe already discount near-term pricing and volume pressures.

Elections have also created dislocations we are working to exploit. In France, political uncertainty ahead of the 2027 presidential election has widened the discount on French-listed equities. Global franchises such as Airbus, TotalEnergies, Danone, Nexans and AXA generate only a modest share of their revenue in France, yet trade as if they were proxies for French sovereign risk. We believe that discount offers an opportunity to own high-quality global businesses at attractive valuations.

In the meantime, a higher-for-longer rate environment supports the earnings power of well-capitalized banks in Japan, South Korea and Europe, especially as their shares came under pressure from flattening yield curve in the fourth quarter. We continue to find self-help stories that remain underappreciated by the market. As always, we remain focused on high-quality businesses with improving fundamentals aligned with a diversified set of long-term secular themes.

Portfolio Highlights

The ClearBridge International Value Strategy underperformed its MSCI EAFE Index benchmark during the third quarter. On an absolute basis, the Strategy had positive contributions from five of the 11 sectors in which it was invested. The leading contributors were the financials and energy sectors, while the IT sector detracted the most.

On a relative basis, overall stock selection detracted from performance, while overall sector allocation contributed. Stock selection in the financials sector and an overweight to the energy sector benefited performance. Conversely, stock selection in the IT, materials and health care sectors weighed on relative results.

By region, stock selection in Europe Ex U.K., underweights to Japan and Asia Ex Japan and our overweight to emerging markets, particularly South Korea, weighed on performance. Conversely, an underweight to Europe Ex U.K. contributed to performance.

On an individual stock basis, the biggest contributors to relative returns were Mitsubishi UFJ Financial, Shinhan Financial, Piraeus Bank and Hitachi, as well as not owning ASML. The largest detractors from relative returns were SK Hynix, Murata Manufacturing, Infineon Technologies, Brookfield Renewable and Amrize.

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