

**Brandes Investment Partners**  
**Global Small-Mid Cap Equity Strategy Notes**  
**First Quarter 2024 (January 1 – March 31, 2024)**

The Brandes Global Small-Mid Cap Equity Strategy rose 7.96% net of fees and 8.13% gross of fees, outperforming its benchmark, the MSCI ACWI SMID Cap Index, which appreciated 4.99%.

<b>Annualized total return as of March 31, 2024</b>	<b>1-year</b>	<b>5-year</b>	<b>10-year</b>
Brandes Global Small-Mid Cap Equity Composite (net)	26.89%	11.04%	7.13%
Brandes Global Small-Mid Cap Equity Composite (gross)	27.71%	11.80%	7.99%
MSCI ACWI SMID Cap Index	16.81%	8.08%	6.82%

Past performance is not a guarantee of future results. One cannot invest directly in an index. Returns include reinvestment of all dividends and are reduced by any applicable foreign withholding taxes, without provisions for income taxes, if any.

**Positive Contributors**

Holdings in the industrials and communication services sectors drove returns. Among the top performers were aerospace and defense companies Rolls-Royce (U.K.) and Embraer (Brazil), along with telecommunication company Magyar Telekom (Hungary).

Our aerospace and defense holdings, including Rolls-Royce and Embraer, continued to benefit from the ongoing recovery in passenger air travel that has led to solid revenue growth, expanding profit margins, healthier cash-flow generation and healed balance sheets. These positive fundamental developments helped confirm our long-term thesis around franchise quality, balance sheet durability and end-market recovery potential for these holdings. Moreover, record backlogs highlighted—in our view—the appealing long-term secular growth outlook for global passenger air travel in an industry that has historically allowed incumbents to generate attractive returns on capital. Consequently, we revised our intrinsic value estimates for several of our aerospace and defense holdings upward and believe they continue to offer an attractive risk/reward tradeoff at current valuation levels.

Our financials holdings also aided returns, led by Panama-based Banco Latinoamericano and Japan-based Hachijuni Bank.

**Performance Detractors**

Significant detractors included several health-care holdings, such as Spain’s Grifols, Netherlands-based Koninklijke Philips, and Japan-based Medipal Holdings.

Biotechnology firm Grifols grappled with multiple declines in its share price following a short seller’s report that questioned the company’s debt and corporate governance practices. In our opinion, the risks highlighted in the report had been largely known, and we maintained our position in the company despite the volatility—albeit now at a lower weighting due to the share-price decline. While we have long been concerned with the company’s elevated financial leverage, we recognize that Grifols has several options at its disposal that can help reduce risk, including the partial sale of its stake in Shanghai RAAS, which is scheduled to close in the first half of this year.

We continue to believe there is potentially meaningful upside in the stock and we are managing the elevated balance sheet risk through allocation sizing. Grifols’ plasma business weathered considerable challenges amid the COVID-19 pandemic, including decreased blood donations and higher costs associated with compensating donors. Today, blood donation volumes are running above pre-COVID levels and collection costs are declining as the pandemic-related supply challenges fade. Admittedly, the free-cash-flow recovery has been slower than anticipated as Grifols has been making substantial investments to expand capacity for future growth. While these investments have weighed on short-term profitability and cash flow, we believe they should be beneficial for the company in the long term as the industry transitions back to the pre-COVID growth trajectory. Furthermore, we appreciate Grifols’ competitive position in a consolidated industry with high barriers to entry and long-term secular growth, as well as its business model that should

allow it to generate steady free cash flow if the industry returns to equilibrium. Trading at a single-digit multiple of pre-COVID earnings, Grifols appears attractively valued to us.

Beyond health care, other detractors included U.K.-based food retailer J Sainsbury and Switzerland-based luxury goods firm Swatch.

### **Select Activity in the Quarter**

All good things must eventually come to an end and that proved true for the investment in Halliburton. Over the past two quarters, Halliburton has been sold as better investment opportunities have been found. The company was first purchased in 2020 when, with the benefit of hindsight, stocks were akin to catching fish in a barrel.

Halliburton is the second-largest oilfield services company in the world. It provides a variety of tools and services that support discovering and extracting hydrocarbons. Due to its scale, operational reputation and internally developed technologies, Halliburton has earned good returns on capital over long periods of time—a rarity in the oil and gas industry. While we believe the business is of high quality, the company's fortunes are tied to global upstream capital spending, which is cyclical and correlated to the oil price.

Halliburton was out of favor with investors even before the pandemic-caused lockdowns. Oil prices had been falling during 2019 as U.S. oil production growth was causing a supply glut on the global market. In addition, OPEC+ was starting to fray, with Russia abandoning production quotas and Saudi Arabia threatening to do the same. Add a global pandemic to this mix and you get quite an investment opportunity. At the beginning of 2018, Halliburton's market value was almost \$50 billion. By the end of 2019, the company's market value fell to \$21 billion. At its lowest valuation in 2020, Halliburton's market value was \$4 billion—solidly a small cap.

Halliburton, along with much of the market, was clearly out of favor then. While uncertainty was incredibly high, the investment opportunity still had several appealing attributes. First, Halliburton had only generated negative operating cash flow once in its prior 20-year period. The company had shown an ability during past cycles to cut costs and release working capital to buffer against worsening business conditions. Second, as one of the largest players in the industry, Halliburton was poised to gain market share as smaller competitors struggled to maintain scale. Most importantly, we believed the market price was so heavily discounted that we could wait many years for a return to "normalcy" and still realize a good return on investment. The company continued to generate positive free cash flow through 2020, and in 2022, operating income surpassed the prior cyclical peak. Halliburton is still benefiting from a good commodity price environment with few clouds on its horizon; however, the committee decided that it is time to allocate capital to new opportunities and divested what has since become a solid, large-cap company.

Without the benefit of a calamity bringing us investment opportunities, the Small Mid Cap committee recently acquired shares in what we consider a boring, staid Swiss bank. Valiant Holding is a regional Swiss bank focused on retail and small business banking. The company operates with a conservative balance sheet that entails strong capital ratios, high-quality assets, limited interest rate risk and a low-cost funding profile.

Valiant's conservative positioning has caused it to be left behind its European banking peers. Accordingly, its price to book value stagnated, with its share price returning ~14% over the past two years, while the banking constituents of MSCI Europe have collectively returned over 40%. Its European peers have benefited from being more sensitive to interest rate changes while also operating in countries that have had greater rate increases.

Valiant's future earnings growth will not be solely dependent on the interest rate environment. The bank recently completed a multi-year expansion, entering new cantons and growing its advisor base. We believe that Valiant should start to see the benefit of these investments as they mature. Additionally, the company has been increasing efficiency through branch consolidations. With a market value equivalent of 70% of tangible book value, the investment risk appears muted to us. If management achieves its operational goals or the general banking environment continues to improve, the investment return potential in Valiant equity is, in our opinion, genuinely attractive. Perhaps boring and staid can be construed as positive attributes in this panic-free market environment.

### **Current Positioning**

The strategy held key overweight positions versus the benchmark in the consumer staples and health care sectors. Meanwhile, we remained underweight in typically cyclical sectors, such as consumer discretionary and industrials. We were also underweight in perceived “safe havens,” such as utilities.

Geographically, we continued to find value opportunities outside the United States, especially in the United Kingdom, Japan, and emerging markets. As of March 31, the portfolio remained materially underweight compared to the benchmark’s allocation to the United States.

Global small-mid cap equities continue to represent, in our opinion, fertile ground for fundamentally solid businesses trading at a discount to their estimated intrinsic values. Within the asset class, value stocks (MSCI World SMID Cap Value) continue to trade in the highest decile of discount levels to the broader market (MSCI World SMID Cap) on a variety of valuation metrics, including forward price/earnings, price/cash flows, and enterprise value/sales.

We believe that paying extremely close attention to valuations enables us to choose opportunities that others may miss. From our perspective, selectivity and a laser focus on margin of safety remain paramount in any and all market environments. We are enthusiastic about the potentially undervalued companies we are finding, and the diversification offered by the Brandes Global Small-Mid Cap Equity Strategy.

Term definitions: <https://www.brandes.com/termdefinitions>

The margin of safety for any security is the discount of market price to our estimate of intrinsic value.

The MSCI ACWI SMID Cap Index with net dividends captures mid and small cap representation across developed and emerging market countries.

The MSCI Europe Index with net dividends captures large and mid cap representation of developed market countries in Europe.

The MSCI World SMID Cap Index captures mid and small cap representation of developed market countries.

The MSCI World SMID Cap Value Index with net dividends captures small and mid cap securities across developed market countries exhibiting value style characteristics, defined using book value to price, 12-month forward earnings to price, and dividend yield.

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