BRANDES
INVESTMENT PARTNERS

Brandes Investment Partners
U.S. Small-Mid Cap Value Equity Strategy Notes
First Quarter 2024 (January 1 – March 31, 2024)

The Brandes U.S. Small-Mid Cap Value Equity Strategy rose 6.46% net of fees and 6.71% gross of fees, slightly underperforming its benchmark, the Russell 2500 Index, which appreciated 6.92% in the quarter, but outperforming the Russell 2500 Value Index which was up 6.07%.

Annualized total return as of March 31, 2024	1-year	5-year	10-year
Brandes U.S. Small-Mid Cap Value Equity Composite (net)	13.35%	9.30%	8.38%
Brandes U.S. Small-Mid Cap Value Equity Composite (gross)	14.44%	10.35%	9.42%
Russell 2500 Index	21.43%	9.89%	8.83%

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

Top contributors included holdings in the aerospace and defense industry. Among the most notable performers were Textron, Moog Inc., and Embraer. They have continued to benefit from ongoing recovery in passenger air travel and their other end-markets, which 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 regarding franchise quality, balance sheet durability and end-market recovery potential for these holdings. Moreover, record backlogs highlighted—in our view—the appealing long-term growth outlook for passenger air travel in an industry that has historically seen incumbents generate attractive returns on capital. We therefore 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.

Other contributors included security system technology company Arlo Technologies, pharmaceutical company Organon, and Healthcare Services Group.

Performance Detractors

While Organon and Healthcare Services Group were solid performers, our overall exposure to the health care sector detracted from relative returns, mainly because of poor performance by Koninklijke Philips, Sotera Health, Varex Imaging, and Grifols.

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 derisk, including the partial sale of its stake in Shanghai RAAS that 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 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 fiber laser manufacturer IPG Photonics and agribusiness and transportation conglomerate Seaboard Corporation.

Select Activity in the Quarter

Portfolio activity was very light in the quarter. There were no new positions added to the portfolio and no full sells.

Current Positioning

Given the limited portfolio activity, the current positioning of the portfolio was largely unchanged. The strategy maintains its largest weights in industrials, health care, and information technology. Our most significant underweights are in consumer discretionary, financials, and real estate, which is consistent with how the portfolio was positioned to begin 2023 as well.

Compared with the Russell 2500 Value Index, we have significantly less exposure to financials and real estate. In our opinion, the differences between the Brandes U.S. Small-Mid Cap Value Equity Strategy and the broader U.S. small-mid cap market continue to make the strategy an attractive complement to other small-cap and small-mid offerings. Our strategy exhibits lower valuations than the Russell 2500 Index, while offering exposure to companies that have what we consider strong balance sheets, compelling growth prospects, and a history of durable free-cash-flow generation.

We are optimistic about the potential of value stocks in general and believe the Brandes U.S. Small-Mid Cap Value Equity Strategy remains well positioned from a long-term risk/reward perspective.

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

The Russell 2500 with gross dividends measures the performance of the small to mid cap segment of the U.S. equity universe.

The Russell 2500 Value Index measures the performance of the small to mid-cap value segment of the U.S. equity universe. Securities are categorized as growth or value based on their relative book-to-price ratios, historical sales growth, and expected earnings growth.

Diversification does not assure a profit or protect against a loss in a declining market.