

European Equity Strategy Notes Second Quarter 2024 (1 April – 30 June 2024)

The Brandes European Equity Strategy rose 4.04% (gross of fees), outperforming its benchmark, the MSCI Europe Index, which increased 0.55% in the quarter, and the MSCI Europe Value Index, which appreciated 1.35%.

Positive Contributors

Stock selection across sectors contributed positively to returns, led by holdings in financials and consumer staples. In financials, notable performers included Spanish insurer Linea Directa Aseguradora, Austria-domiciled Erste Group Bank, Slovenian Nova Ljubljanska Banka and U.K.-based Barclays. In consumer staples, Irish food products company Greencore drove performance, along with German household products business Henkel and U.K.-based tobacco firm Imperial Brands.

Select investments in health care also lifted returns, especially Netherlands-based Koninklijke Philips and Germany's Fresenius. Philips' shares increased after it reached a settlement related to its ventilators, removing significant uncertainty about the company's legal liabilities.

Other standout contributors included communication services firms Millicom International (Luxembourg), Magyar Telekom (Hungary), and ITV (U.K.).

Performance Detractors

Our underweight to pharmaceuticals, which was among the best performing industries in the benchmark, diminished relative returns. Additionally, a few positions in health care declined, including U.K.-based pharmaceutical firm GSK and Spanish biotech business Grifols.

GSK's stock price fell after a U.S. public health agency narrowed its age recommendation for RSV (respiratory syncytial virus) vaccines, limiting the use of the company's products.

France was among the worst-performing markets in the benchmark, as investors were concerned about the uncertainty related to the country's parliamentary elections. Our overweight to France hurt relative returns, and several of our holdings there declined, notably retailer Carrefour, communication services firm Orange and consumer products manufacturer Societe BIC.

Select Activity in the Quarter

We divested positions in Germany's Commerzbank and Swiss machinery firm Sulzer, while initiating positions in U.K. consumer health care company Reckitt Benckiser, Germany-based semiconductor manufacturer Infineon and logistics firm Deutsche Post, as well as Dutch machinery company CNH Industrial.

Reckitt Benckiser is a multinational consumer goods company, with operations in over 60 countries across three business units: consumer health, hygiene, and nutrition. The company's brands are strong, particularly on a country-specific basis, such as Lysol in the U.S. and Dettol in India. Over the past several years, the management team has been focusing on achieving higher-than-category average growth for its brands and on increasing margins through positive operating leverage and productivity-related efficiency improvements.

During the pandemic, Reckitt experienced a short-term surge in demand for its hygiene products. However, the associated stock-price increase was not sustained, and Reckitt's shares remained largely range-bound for five years prior to their recent decline. The company's shares have come under pressure after it reported weaker-than-expected growth and profitability for fiscal year 2023. While it has improved its margins over the past few years, Reckitt will likely face slower growth in the short term as it cycles through last year's elevated base, driven by infant formula recall by Abbott Laboratories (Reckitt's main competitor) and a robust cold and flu season.

Additionally, concerns about potential liability related to its pre-term infant formula business in the U.S. further weighed on investor sentiment after the company lost a legal case earlier this year. Reckitt faces additional related legal cases, as does Abbott Laboratories.

Despite the headwinds, Reckitt's longer-term growth profile appears compelling to us. We appreciate its competitive position, which should allow it to grow at an above-average rate in each business category. We also believe the company has the potential for margin improvement through a combination of productivity-related cost savings and positive operating leverage. In our opinion, investor concerns about Reckitt's growth prospects and potential legal liabilities have been more than accounted for in its share price. At its current valuation, which reflects a discount to the company's historical multiples, we see Reckitt as an appealing investment opportunity.

Year-to-Date Briefing

The Brandes European Equity Strategy rose 9.09%, outperforming its benchmark, the MSCI Europe Index, which increased 5.81% in the six months ended 30 June 2024, and the MSCI Europe Value Index, which appreciated 3.91%.

Stock selection across sectors drove performance. Holdings in financials were among the standout contributors, led by Italy's Intesa Sanpaolo, Austria-based Addiko Bank, Slovenian Nova Ljubljanska Banka, and Spanish Linea Directa Aseguradora. Consumer staples holding Greencore also lifted performance, as did communication services firms Magyar Telekom and Millicom International.

Other contributors included French automaker Renault and U.K.-based aerospace and defense firm Rolls-Royce, which continued to benefit from the ongoing recovery in its end-markets.

Several investments in health care detracted from returns, most notably French pharmaceutical Euroapi and Spain-based Grifols. Grifols' stock declined (mainly in the first quarter) following a short seller's report that questioned the company's debt and corporate governance practices. We continue to see a meaningful upside potential in the company. Grifols recently completed the sale of an equity stake in Shanghai RAAS, which should help it improve its financial leverage in the near term.

Similar to the quarter, holdings in France also hurt performance. Besides Euroapi, Carrefour saw its share price fall, as did luxury goods company Kering, utility ENGIE, and Societe BIC.

Current Positioning

The Brandes European Equity Strategy holds key overweight positions in consumer staples and communication services, while maintaining significant underweights to technology and industrials. Geographically, the portfolio's largest allocations continue to be in France and the United Kingdom. It also remains underweight in Switzerland and has no exposure to companies in the Nordic Region.

While we maintain our lower weighting to Germany relative to the benchmark, our underweight has narrowed with the purchase of Infineon and Deutsche Post this quarter. We believe the differences between the strategy and the MSCI Europe Index make it an excellent complement and diversifier to passive and growth-oriented strategies.

As of 30 June 2024, value stocks (MSCI Europe Value) continued to trade in the least-expensive decile relative to growth (MSCI Europe Growth) since the inception of the style indices. This was evident across various valuation measures, including price/earnings, price/cash flow, and enterprise value/sales. Historically, such discount levels have often signaled attractive subsequent returns for value stocks. This is encouraging to us because the Brandes European Equity Strategy, guided by our value philosophy and process, has tended to outperform the value index when it outperformed the benchmark.

Looking ahead, we remain optimistic about the long-term prospects of the companies held in the Brandes European Equity Strategy.

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

The MSCI Europe Growth Index captures large and mid cap securities across developed Europe exhibiting growth style characteristics, defined using long-term forward earnings per share (EPS) growth rate, short-term forward EPS growth rate, current internal growth rate, long-term historical EPS growth trend, and long-term historical sales per share growth trend.

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

The MSCI Europe Value Index captures large and mid cap securities across developed Europe exhibiting value style characteristics, defined using book value to price, 12-month forward earnings to price, and dividend yield.

MSCI has not approved, reviewed or produced this report, makes no express or implied warranties or representations and is not liable whatsoever for any data in the report. You may not redistribute the MSCI data or use it as a basis for other indices or investment products.

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

The foregoing Quarterly Commentary reflects the thoughts and opinions of Brandes exclusively and is subject to change without notice. The information provided in the commentary should not be considered a recommendation to purchase or sell any particular security. It should not be assumed that any security transactions, holdings or sectors discussed were or will be profitable, or that the investment recommendations or decisions we make in the future will be profitable or will equal the investment performance discussed herein. International and emerging markets investing is subject to certain risks such as currency fluctuation and social and political changes; such risks may result in greater share price volatility. There is no assurance that any securities discussed herein will remain in an account's portfolio at the time you receive this report or that the securities sold have not been repurchased. The actual characteristics with respect to any particular account will vary based on a number of factors including but not limited to: (i) the size of the account; (ii) investment restrictions applicable to the account, if any; and (iii) market exigencies at the time of investment. Unlike bonds issued or guaranteed by the U.S. government or its agencies, stocks and other bonds are not backed by the full faith and credit of the United States. Stock and bond prices will experience market fluctuations. Please note that the value of government securities and bonds in general have an inverse relationship to interest rates. Bonds carry the risk of default, or the risk that an issuer will be unable to make income or principal payment. There is no assurance that private guarantors or insurers will meet their obligations. The credit quality of the investments in the portfolio is not a guarantee of the safety or stability of the portfolio. Investments in Asset Backed and Mortgage Backed Securities include additional risks that investors should be aware of such as credit risk, prepayment risk, possible illiquidity and default, as well as increased susceptibility to adverse economic developments. Securities of small companies generally experience more volatility than mid and large sized companies. Although the statements of fact and data in this report have been obtained from, and are based upon, sources that are believed to be reliable, we cannot guarantee their accuracy, and any such information may be incomplete or condensed. Strategies discussed are subject to change at any time by the investment manager in its discretion due to market conditions or opportunities. The Brandes investment approach tends to result in portfolios that are materially different than their benchmarks with regard to characteristics such as risk, volatility, diversification, and concentration. Please note that all indices are unmanaged and are not available for direct investment. Past performance is not a guarantee of future results. No investment strategy can assure a profit or protect against loss. Market conditions may impact performance. The performance results presented were achieved in particular market conditions which may not be repeated. Moreover, the current market volatility and uncertain regulatory environment may have a negative impact on future performance. The margin of safety for any security is defined as the discount of its market price to what the firm believes is the intrinsic value of that security. The declaration and payment of shareholder dividends are solely at the discretion of the issuer and are subject to change at any time.

Ireland/Europe: FOR PROFESSIONAL INVESTOR USE ONLY. Issued by Brandes Investment Partners (Europe) Limited (Brandes Europe), Alexandra House, The Sweepstakes, Ballsbridge, Dublin, D04 C7H2, Ireland. Registered in Ireland Number 510203. Authorised and regulated by the Central Bank of Ireland. This report is being provided for information purposes only, no representation or warranty is made, whether express or implied as to the accuracy or completeness of the information provided. To the fullest extent permitted by law Brandes Europe shall not be liable for any loss or damage suffered by any person as a result of the receipt of this report. Recipients of this report should obtain their own professional advice. The distribution of this report may be restricted by law. No action has been or will be taken by Brandes Europe to permit the possession or distribution of this report in any jurisdiction where action for that purpose may be required. Accordingly, this report may not be used in any jurisdiction except under circumstances that will result in compliance with any applicable laws and regulations. Persons to whom this report is communicated should inform themselves about and observe any such restrictions. This information is being issued only to, and/or is directed only at (i) persons who have professional experience in matters relating to investments or (ii) are persons falling within Article 49(2)(a) to (d) ("high net worth companies, unincorporated associations etc.") of the Financial Services and Markets Act 2000 (Financial Promotion) Order 2005 or to whom it may otherwise lawfully be communicated (all such persons together being referred to as "Relevant Persons"). This communication must not be acted on or relied on by persons who are not Relevant Persons. Any investment or investment activity to which this communication relates is available only to Relevant Persons and will be engaged in only with Relevant Persons. This report is a confidential communication to, and solely for the use of, the persons to whom it is distributed to by Brandes Europe.