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INVESTMENT PARTNERS

Brandes Investment Partners
Global Small Cap Equity Strategy Notes
First Quarter 2023 (January 1 – March 31, 2023)

The Brandes Global Small Cap Equity Strategy returned 13.02% net of fees and 13.24% gross of fees, outperforming its benchmark, the S&P Developed SmallCap Index, which was up 4.34% in the quarter, and the S&P Developed SmallCap Value Index, which rose 2.14%.

Annualized total return as of March 31, 2023	1-year	5-year	10-year
Brandes Global Small Cap Equity Composite (net)	10.25%	5.51%	7.59%
Brandes Global Small Cap Equity Composite (gross)	11.11%	6.34%	8.48%
S&P Developed SmallCap Index	-9.28%	4.08%	7.32%

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 Latin America helped performance, including Mexico-based real estate investment trust **Fibra Uno** and cement company **Cemex**, Chilean electric utility **Enel Chile**, and Brazilian regional jet manufacturer **Embraer**. Luxembourg-domiciled telecom firm **Millicom International**, which operates entirely in Latin America, also aided returns.

Embraer posted solid results for the fourth quarter of 2022, with revenue and free cash flow ahead of consensus and operating margin improving sequentially across segments. The company provided increased guidance for aircraft deliveries in 2023 in both the commercial and executive divisions. Moreover, one of its competitors announced it had officially shut down its next-generation commercial regional jet program, which could leave Embraer to be the primary supplier in this market.

Similarly, Cemex benefited from an enhanced outlook for 2023, with pricing remaining robust and management optimistic on growth in the industrial and commercial sectors.

Other contributors included U.K.-based retailers **J Sainsbury** and **Marks and Spencer**. Additionally, industrial firm **Rolls-Royce**, also based in the U.K., continued to recover from the downturn in demand for long-haul air travel. The company reported improved operating results and has been awarded with new contracts over the last several months, strengthening expectations for free-cash-flow generation.

From a sector perspective, holdings in industrials, consumer staples, real estate, and communication services drove returns.

Performance Detractors

Several holdings in consumer discretionary hurt performance, notably Canada-based **Dorel Industries** and China-based **Weiqiao Textile**.

Dorel Industries declined on disappointing results for the fourth quarter of 2022 amid lower sales in its juvenile products and home furnishing divisions. The company has started implementing measures to cut costs and reduce inventories, which should help earnings going forward.

U.S.-based insurer **National Western Life** and **Chesapeake Energy** also detracted from returns, along with U.K.-based banknotes printing company **De La Rue**, Spanish biotechnology firm **Grifols**, and Irish beverage business **C&C Group**.

Grifols saw its share price hit by the resignation of its chairman and weak earnings guidance for the year. The company's build-out of collection facilities over the last few years has continued to impact its cash flow and stretched its balance sheet, while lower blood-plasma collection volumes due to COVID suppressed its earnings. Recently, Grifols announced new cost-cutting initiatives, and we continue to believe the company offers an attractive long-term opportunity given the importance of its plasma-derived products to treat a variety of medical conditions.

Relative to the benchmark, our underweight to the information technology sector weighed on returns.

Select Activity in the Quarter

The small-cap investment committee initiated positions in U.S.-based apparel company **Hanesbrands** and **Elanco Animal Health** while divesting U.S. machinery companies **Flowserve** and **Kennametal**.

Elanco Animal Health was spun out of Eli Lilly in September 2018 and originally focused on the food animal segment. Through a series of acquisitions, most recently Bayer Animal Health in 2020, Elanco has become a global animal health business with a diversified product portfolio that includes medicinal feed, parasiticides (flea and tick products), vaccines, and other therapeutic drugs. The firm is now the world's second-largest animal health care company by sales and has a 55/45 revenue split between the U.S. and international markets.

While the integration of Bayer Animal Health has been going well, we believe its overhang, coupled with slower revenue growth in recent years, has created the opportunity to invest in Elanco. Key factors that underlie our investment thesis include:

- Mid-single digit potential growth throughout the industry stemming from a global increase in protein consumption and pet ownership;
- Stable sales due to the strong brand name, diverse portfolio, and lack of patent cliffs;
- Likelihood of profit margin expansion from streamlining manufacturing, research and development (R&D), and procurement;
- Less expensive and shorter-duration R&D with a higher a probability of success compared to human pharmaceuticals;
- Potential for continued financial deleveraging.

At its current valuations, we believe the stock represents an appealing risk/reward tradeoff.

Current Positioning

As of March 31, 2023, the Brandes Global Small Cap Equity Strategy continued to have overweight positions in Ireland, the U.K., Hong Kong, Spain, and emerging markets, and a material underweight to companies in the U.S. From a sector perspective, we held key overweights to consumer staples, communication services, and industrials, while maintaining significant underweights to technology, consumer discretionary, real estate, and materials.

Given the volatility and headlines surrounding the financials sector globally, we'd be remiss not to mention our exposure. At quarter end, the strategy had a slightly higher allocation to financials than the benchmark's 13.5% weighting. Our financials research team and investment committee have been meeting frequently as they monitored ongoing developments. We have been updating our valuation and risk exposure analysis across a variety of financials holdings and have been in contact with several global financial companies via email, phone, and in-person meetings at financial conferences. We believe the risk of permanent, fundamental impairment stemming from issues like those faced by Silicon Valley Bank and other struggling banks remains low for the financial institutions we own specifically within the strategy.

We continue to believe the portfolio's current positioning offers an attractive opportunity for long-term investors and remain optimistic about its prospects.

Cash Flow: The amount of cash generated minus the amount of cash used by a company in a given period.

Free Cash Flow: Total cash flow from operations less capital expenditures.

Operating Margin: Operating income divided by net sales; used to measure a company's operating efficiency.

Profit Margin: Net income divided by revenues.

The S&P Developed SmallCap Index with net dividends measures equity performance of small cap companies in developed markets. Data prior to 2001 is gross dividend and linked to the net dividend returns.

The S&P Developed SmallCap Value Index with net dividends measures the equity performance of small cap companies in developed markets which are classified as value stocks by book value-to-price, sales-to-price, cash flow-to-price, and dividend yield.