

Brandes Investment Partners
U.S. Small Cap Value Equity Strategy Notes
First Quarter 2025 (January 1 – March 31, 2025)

The Brandes U.S. Small Cap Value Equity Strategy fell 6.45% net of fees and 6.30% gross of fees, outperforming its benchmark, the Russell 2000 Index, which was down 9.48% in the quarter. The Russell 2000 Value Index declined 7.74%.

Annualized total return as of March 31, 2025	1-year	5-year	10-year
Brandes U.S. Small Cap Value Equity Composite (net)	3.61%	21.22%	10.06%
Brandes U.S. Small Cap Value Equity Composite (gross)	4.33%	22.21%	11.02%
Russell 2000 Index	-4.01%	13.26%	6.29%

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

Leading contributors included energy and services business Innovex, regional jet manufacturer Embraer, medical device company LENSAR, software company SolarWinds, and building materials company Buzzi.

Both LENSAR and SolarWinds benefited from buyout announcements. In February, Turn/River Capital announced that it would buy SolarWinds for \$18.5/share, approximately a 35% premium to the average 90-day trading price of \$13.70. In March, Alcon announced that it would acquire LENSAR for \$14.00 per share in cash with an additional non-tradeable contingent value right offering of up to \$2.75 per share in cash. The total potential consideration of \$16.75 represents a 47% premium to the average 90-day trading price.

Embraer has maintained its impressive streak, announcing several new wins against competitors in its defense business. This, coupled with an expanding order backlog for regional jets, has further boosted market confidence in the company's prospects.

On a relative basis, our underweight to information technology sector, the worst performing sector in the benchmark, helped relative returns.

Performance Detractors

Notable detractors included select industrial holdings, specifically machinery companies Graham and L.B. Foster, and construction and engineering business Orion Group. Consumer discretionary companies Hanesbrands and American Outdoor Brands weighed on returns as well.

Both Graham holdings and Orion Group declined after announcing via their quarterly earnings reports that their revenue and full-year guidance had missed analyst expectations. Similarly, Hanesbrands' share price fell after it declared disappointing quarterly results and the departure of its CEO. We added to our positions in all three companies based on the share-price weakness, viewing their recent issues as temporary setbacks.

Select Activity in the Quarter

The small-cap investment committee initiated positions in pizza company Papa John's and forest products company Canfor.

Papa John's, which began operating in 1984, is one of the largest players in the global quick-service restaurant (QSR) pizza market, boasting more than 6,000 restaurants across 50 countries. The company operates a primarily franchise-based system, owning ~9% of its restaurants. It generates revenue from franchise royalties, sales of pizza and related products at its company-owned stores, and sales from its supply chain, which supplies its franchises with consistent quality pizza dough and sauce. Papa John's is the fourth-largest limited-service pizza chain both in the U.S. and globally, with the significant majority of its products contributed from North America.

Papa John's share price declined almost 50% over the past year, largely due to concerns about its weak same-store sales performance, a challenging operating environment for consumption and the impact from third-party aggregators for food delivery, as well as the departure of its CEO in March 2024. In August 2024, the company announced Todd Penegor, former CEO of Wendy's, as its new CEO. We view Penegor's appointment as a positive step, but it will take time for his vision to materialize. Under his leadership, Papa John's is working to improve its value perception with customers, better leverage its information technology, and improve the performance of its international business.

We find the risk/reward tradeoff of the investment opportunity compelling at current levels. The company is trading at an undemanding valuation that does not seem to reflect credit for restoring fundamental performance and margin improvement.

Other portfolio activity included full sales of natural gas utility Spire and over-the-counter pharmaceutical manufacturer Prestige Consumer Healthcare as both companies appreciated to our estimates of their respective intrinsic values. We also fully divested SolarWinds after it agreed to be acquired at a share price above our estimate of its intrinsic value.

Current Positioning

Allocation to companies in the industrials sector continues to be the largest weighting and relative overweight from a sector standpoint. The portfolio also maintains key weights in health care, consumer discretionary, materials, and energy. The strategy's most notable underweights are in financials, information technology, and real estate. Compared to the Russell 2000 Value Index, we have significantly less exposure to financials and real estate.

In our opinion, the differences between the Brandes U.S. Small Cap Value Equity Strategy and the broader U.S. small-cap market continue to make it an attractive complement to other small-cap offerings. Our strategy exhibits lower valuations than the Russell 2000 Index, while offering exposure to companies that we believe have 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 Cap Value Equity Strategy remains well positioned from a long-term risk/reward perspective.

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

The Russell 2000 Index with gross dividends measures the performance of the small cap segment of the U.S. equity universe.

The Russell 2000 Value Index with gross dividends measures performance of the small 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.

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