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Brandes Investment Partners
U.S. Small-Mid Cap Value Equity Strategy Notes
Fourth Quarter 2023 (October 1 – December 31, 2023)

The Brandes U.S. Small-Mid Cap Value Equity Strategy rose 8.18% net of fees and 8.44% gross of fees, underperforming its benchmark, the Russell 2500 Index, which appreciated 13.35% in the quarter.

Annualized total return as of December 31, 2023	1-year	5-year	10-year
Brandes U.S. Small-Mid Cap Value Equity Composite (net)	9.52%	8.95%	7.98%
Brandes U.S. Small-Mid Cap Value Equity Composite (gross)	10.57%	9.99%	9.01%
Russell 2500 Index	17.42%	11.67%	8.36%

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

Despite a challenging start to 2023, the financials sector emerged as one of the best performers, driven partly by market optimism around an economic soft landing. A number of our financials holdings were leading contributors, notably bank **Citizens Financial Group** and consumer finance company **OneMain Holdings**.

Aerospace and defense holdings **Embraer** and **Moog** also helped returns, with both companies continuing to see a resurgence in their end-markets.

Other standout performers included **Elanco Animal Health**, chemical company **Scotts Miracle-Gro**, and shoe company **Skechers U.S.A.**

Performance Detractors

Notable detractors included holdings in the health care sector, namely **Pediatrix Medical Group**, **Emergent BioSolutions**, **Phibro Animal Health,** and **Organon**. Pediatrix Medical Group, Emergent BioSolutions, and Organon all released below-consensus Q3 results and updated guidance that the market did not receive well.

Other detractors were oil and gas-related companies **Dril-Quip** and **Chesapeake Energy**, as well as household durables company **Whirlpool** and wireless surveillance camera manufacturer **Arlo Technologies**. Our underweight to the financials sector was also a detractor from a relative standpoint.

Select Activity in the Quarter

The mid-cap investment committee initiated a position in **IPG Photonics Corporation**, while selling the portfolio's holdings in software companies **N-able** and **SolarWinds**, as well as energy firm **Halliburton Company**.

March 2020 brought many new opportunities into the scope of the small-mid cap portfolios. One was Halliburton (HAL). The company is the second-largest diversified oilfield services company in the world. At its nadir in March 2020, HAL's share price had fallen by more than 80% since the start of 2020. The company had dipped to a market capitalization not seen since 2002, even though during the past 18 years HAL's revenue has nearly doubled. Such was the fate of a company whose business is driven by capital spending in the oil industry.

HAL provides a variety of products and services, such as drill bits, directional drilling, pressure pumping, well-completion tools, etc. The company's scale and technical knowhow have contributed to a level of profitability that is generally above-average for the industry over long periods of time. While the entire energy sector saw deep share-price declines, Halliburton underperformed its large-cap peers. This stemmed primarily from its exposure to the U.S. energy capital cycle as North America represents about half of HAL's revenue. The U.S. will likely take the brunt of global capital expenditure cuts thanks to its position as the marginal supplier of oil to the world. HAL appears trapped by this situation. However, the committee believed the company had enough liquidity to restructure its operations to this "new normal" and could ultimately benefit from smaller competitors leaving the market. Additionally, the market valuation was sufficiently low when we bought the stock that although the path to full recovery could be long and arduous, it would still make Halliburton a good investment.

Over the holding period, the thesis on Halliburton largely played out, so we sold the position when it appreciated to our intrinsic value estimate.

Current Positioning

The strategy maintained its largest weights in industrials, health care, and information technology. Our most significant underweights were 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.

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