## Brandes Investment Partners
## U.S. Value Equity Strategy Notes
## First Quarter 2023 (January 1 – March 31, 2023)

The Brandes U.S. Value Equity Strategy fell 1.04 net of fees and 0.91% gross of fees in the quarter, underperforming its benchmark, the Russell 1000 Value Index, which increased 1.01%, as well as the broader Russell 1000 Index, which rose 7.46%.

| Annualized total return as of March 31, 2023 | 1-year | 5-year | 10-year |
|---|---|---|---|
| Brandes U.S. Value Equity Composite (net) | -4.12% | 9.28% | 10.40% |
| Brandes U.S. Value Equity Composite (gross) | -3.62% | 9.99% | 11.10% |
| Russell 1000 Value Index | -5.91% | 7.49% | 9.12% |

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***
Value stocks lagged during the quarter as technology, an area of underweight for Russell 1000 Value compared to Russell 1000, was among the strongest performing sectors. Our overweight to technology companies relative to the Russell 1000 Value Index aided our performance.

Notable performers included semiconductor-related firms **Micron Technology** and **Applied Materials**, as well as software company **Open Text** and **Alphabet**, which all rallied after declining more than the market (Russell 1000) last year. Micron saw its share price rise despite releasing widely expected weak financial results as the market became more optimistic that we are nearing the bottom of the current memory products cycle.

Other contributors included global shipping and distribution firm **FedEx**. The company saw its share price rally as it released positive financial results which showed it has successfully cut costs.

***Performance Detractors***
Amid the downfall of two crypto-related banks, and the heavily venture-concentrated Silicon Valley Bank, coupled with concerns about deposit outflows and longer-duration investments held at other small and regional banks, it likely isn't a surprise that the bank industry was one of the worst performing in the benchmark during the quarter.

While in aggregate our bank holdings performed better than the benchmark's bank allocation given our exposure to the large money center banks and super regionals, our overweight to the industry weighed on returns. Our most significant detractors included regional banks **PNC** and **Truist**, as well as insurance company **American International Group**.

Amid the concern and negativity in the broad financials sector, our research team and investment committee met frequently as they monitored ongoing developments, updated our valuation estimates, and evaluated risk exposures of our current holdings as well as potential opportunities. As a result of our analysis, we re-allocated across some of our financials holdings favoring money center and trust banks given their attractive valuations and what we consider lower relative risk exposures compared to regional banks.

Other detractors included several of the strategy's strongest performers from 2022, most notably oil service company **Halliburton** as well as health care holdings **Cigna**, **Pfizer**, and **CVS Health**. After rising amid a declining market last year, the health care providers and services industry was one of the worst performing in the first quarter (on par with banks and commercial REITs), and our overweight to the industry hurt relative returns.

***Select Activity in the Quarter***
The investment committee divested the strategy's position in **Taylor Morrison Home Group** (TMHC).

TMHC was first added to the portfolio just over five years ago. The company completed its initial public offering in 2013 and subsequently restructured its operations through a series of acquisitions and divestitures. TMHC's footprint in the Southwest, Texas, and the Southeast underpinned its recovery as those regions continued to have faster than average population growth. When we first purchased TMHC, the U.S. housing market was still in the process of recovering to our estimate of normal cyclically adjusted housing starts. Additionally, TMHC built an inventory of land at low prices due to the slow recovery of the sector and had recently exited the Canadian housing construction business. These factors, along with what we considered a discounted market valuation, made TMHC an attractive investment opportunity.

While the pandemic initially resulted in a slowdown in housing activity, it soon reversed course and the housing market became turbocharged with low interest rates and increased demand for single family homes. Today, TMHC still screens as a traditional value stock and trades at low valuation multiples measured both on price-to-earnings and price-to-book-value metrics. New housing starts in the U.S. are close to what we consider to be normal. However, despite these positive characteristics, the risks of slowing demand and the potential for asset impairment from inflated land values threaten to overwhelm the upside potential. Consequently, the investment committee sold TMHC as it approached our estimate of its intrinsic value.

***Current Positioning***

As of March 31, 2023, the strategy's largest overweight positions remained in the economically sensitive financials sector, albeit heavily weighted to large money center and trust banks, and the more defensive health care sector. Relative to the Russell 1000 Value Index, we were also significantly overweight technology companies as the sector only accounted for approximately 8% of the index (vs. approximately 25% of the broader Russell 1000 Index).

Our most significant underweights were in consumer staples, utilities, and real estate. These sectors generally appear expensive as, from our perspective, investors are overpaying for perceived defensiveness amid an expected economic downturn. We continue to be careful with our exposure to companies that may be hurt by elevated inflation or those with balance sheet leverage, and instead seek value in the traditionally defensive health care sector.

While a variety of headwinds face stocks today (e.g., elevated inflation and/or potentially increasing interest rates, slowing economic growth and recession concerns, commodity price volatility, and political and regulatory risks (just to name a few), we believe that at today's valuations, value stocks and our portfolio in particular offer an attractive long-term opportunity. It's important to remember that our overall positioning is driven from the bottom up, on a company-by-company basis with a focus on long-term fundamentals. We take into account the economic concerns noted above when we are evaluating a potential investment, estimating the impact they may have on each investment's intrinsic value.

U.S. value stocks (MSCI USA Value) continue to trade in the cheapest quintile relative to growth stocks (MSCI USA Growth) across a variety of valuation metrics (e.g., price/earnings, price/cash flow, enterprise value/sales). The discounts at today's levels have often portended attractive returns over a long-term time horizon for U.S. value stocks, and our portfolio has a historical tendency to do well when value stocks do well.

We believe the differences between the Brandes U.S. Value Equity Strategy and the broader U.S. market continue to make the strategy an attractive complement to more index-like or growth-oriented alternatives. We remain excited about the portfolio's future potential.

Enterprise Value: Market capitalization plus debt, minority interest and preferred shares, minus total cash and cash equivalents.

Enterprise Value/Sales: Enterprise value divided by annual sales.

Price/Book: Price per share divided by book value per share.

Price/Cash Flow: Price per share divided by cash flow per share.

Price/Earnings: Price per share divided by earnings per share.

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

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The MSCI USA Growth Index captures large and mid cap U.S. securities exhibiting overall 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 Russell 1000 Index with gross dividends measures performance of the large cap segment of the U.S. equity universe.

The Russell 1000 Value Index with gross dividends measures performance of the large 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. There is no assurance that a forecast will be accurate. Because of the many variables involved, an investor should not rely on forecasts without realizing their limitations.

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