

Brandes Global Small Cap Equity Fund

Fund Commentary

Equity markets worldwide generally moved higher in the fourth quarter, closing an eventful 2016 punctuated by the Brexit vote in the United Kingdom and Donald Trump's victory in the U.S. presidential election. U.S. stocks remained on an upward trajectory for much of 2016, boosted further in the fourth quarter by expectations that the President-elect's policies would fuel growth and inflation. In a widely expected move, the U.S. Federal Reserve raised interest rates in December for the second time since the financial crisis.

Non-U.S. markets closed the quarter and the year with mixed performance. European stocks wavered for much of 2016 due to concerns over how companies would be affected by the European Central Bank's policy of negative interest rates and potential disruptions from Brexit. In Japan, a weak yen and the central bank's decision to refrain from pushing interest rates further into negative territory contributed to gains (in yen terms) in the fourth quarter.

Emerging markets advanced during much of 2016 but declined in the fourth quarter, partly due to lingering economic and geopolitical concerns, as well as worries

over how President-elect Trump's policies on trade may impact developing countries.

Against this backdrop, The Brandes Global Small Cap Fund outperformed its benchmark, the S&P Developed Small Cap Index in the fourth quarter.

Positive Contributors

The Fund benefited from select holdings in Japan, including power tools manufacturer Hitachi Koki. The company's share price rose significantly due to speculation that the company would be acquired by U.S. private-equity firm KKR, which plans to use its global network to support Hitachi Koki's expansion outside Japan.

Other positive contributors to performance included Brazilian jet manufacturer Embraer and U.S. small engines manufacturer Briggs & Stratton.

Performance Detractors

The Fund's holding in Countrywide, the largest estate-agency group in the United Kingdom, hurt performance.

The slowdown in housing transaction activity continued to drive home prices in Countrywide's markets lower. Additionally, uncertainty and pessimism surrounding Brexit (Britain's planned exit from the European Union) has negatively affected the company's share price. Nonetheless, Brandes LP remains convinced that Countrywide is well positioned to navigate the challenging landscape, and believes it offers an attractive risk/reward tradeoff at its current price.

Other performance detractors included holdings in utilities, most notably Indian conglomerate Reliance Infrastructure and Brazilian electric utility Companhia Paranaense de Energia (Copel).

Select Buy & Sell Activity

During the quarter, the Fund initiated a position in Kissei Pharmaceutical. The company is a small, domestic-oriented pharmaceutical company that generates approximately 85% of revenues from the sale of branded drugs (patent and off-patent) which have been in-licensed or developed internally. The company maintains an extremely strong yet inefficient balance sheet, with net



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cash accounting for almost half of market value, while long-term investments, which include stakes in other Japanese companies, represent the other half.

Similar to Brandes LP's investment thesis for many of its pharmaceutical holdings, Brandes LP believes Kissei's current market price implies very little value for the company's research and development (R&D) pipeline. Kissei invests approximately 20% of sales annually in its R&D, which it believes has some value over the long term. This factor, coupled with the fact that the company traded below book value at year end, led Brandes LP to believe an investment in Kissei Pharmaceutical provides good long-term R&D optionality at very little cost.

During the quarter, Brandes LP also purchased Spain-based Banco Popular Espanol (Popular), the sixth largest banking group by assets in Spain. Traditionally, Popular has had a strong market position providing banking services to small- and medium-sized enterprises. Unfortunately for shareholders in the bank a decade ago, Popular built up a sizeable loan book backed by real estate assets in Spain. The company, along with much of the Spanish financial system, continues to reel from the 2008 crash in Spanish real estate prices.

Following the Spanish real estate collapse, the number of banks in the market declined by over two-thirds as many

went out of business in the face of a 40% decline in property values. Popular is fortunate to have been able to survive this long, especially considering that the company's non-performing assets (i.e., bad real estate loans) have accounted for several multiples of shareholder's equity. To address this illiquidity issue, Popular has raised equity several times, with the most recent being shortly before Brandes LP initiated a position in the company. In fact, the company has raised over €5 billion in equity over the past four years, which is remarkable since the market capitalization of the company was only €4 billion as of December 31, 2016.

Brandes LP is cognizant of the substantial financial risks associated with the size of Popular's non-performing loans, but believes the risk/reward tradeoff is attractive enough to warrant a small position in the Fund. The bank traded at a sizeable discount to tangible equity value at year end, and Brandes LP believes even a slow, modest recovery in the Spanish housing market would bear fruit for the patient investor with a diversified portfolio.

Other Fund activity included the divestment of Japanese leisure products company Sega Sammy Holdings.

The company was formed in a 2004 merger of Sega (an arcade games company) and Sammy (a pachinko machines manufacturer). Some investors may associate

the company name with the Sega home video game console, which peaked in popularity in the 1990s. While the video-game business remains a part of Sega Sammy, the company's largest segment is the manufacturing and sale of pachinko (pinball) and pachislot (slot) machines in Japan. When Brandes LP initially purchased Sega Sammy, the company had been facing operational issues along with lower earnings than in recent years due to lower hardware sales in its pachinko segment. Brandes LP believed the issues were temporary and appreciated that more than half of Sega Sammy's market capitalization consisted of cash and investments.

In September 2016, Sega Sammy revised its operating-income forecast to twice its previous guidance, thanks to the strong sales within its entertainment contents business, specifically digital gaming. In late 2016, a law passed in Japan to allow casino gambling at integrated resorts, a move which contributed to a dramatic boost in enthusiasm for the arcade and pachislot entertainment segment. These significant developments pushed Sega Sammy's market price above Brandes LP's intrinsic value and it exited its position.



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Current Positioning

As of December 31, the Fund continued to exhibit more attractive valuations than the benchmark based on price-to-book, price-to-earnings and price-to-cash flow ratios.

At the close of the quarter, the Fund's largest country weights were in the United States and the United Kingdom, and the Fund's largest industry weights were in Household Durables and Machinery. Please note that while macro conditions are considered when Brandes LP determines valuation estimates for individual companies, the Fund's country and industry weightings are a by-product of bottom-up stock selection, not the result of top-down observations.

As always, Brandes LP bases its allocation decisions on a fundamental, bottom-up investment approach that seeks the most attractive value in all corners of the globe.

Looking ahead to 2017 and beyond, Brandes LP remains optimistic about the prospects for the Brandes Global Small Cap Equity Fund. Against the seemingly ever-present backdrop of geopolitical and macroeconomic uncertainties, Brandes LP believes its Graham-and-Dodd value approach, focused on seeking mispriced opportunities, should work well over the long term, leading it to attractively priced,

fundamentally sound companies worthy of inclusion in the Fund.

About Brandes LP

In the 40-plus years since Brandes LP was founded, its goal has remained the same: pursue above-market gains to help investors move closer to their long-term investment objectives. Brandes LP believes that its unwavering commitment to value investing will lead it to attractively priced, fundamentally sound companies worthy of inclusion in the Fund.



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Contribution Analysis

LAST QUARTER

INDUSTRY			
Top 5 Contributors		Top 5 Detractors	
	%		%
Health Care Equip. & Supplies	1.07	Banks	-1.05
Machinery	1.01	Electric Utilities	-0.53
Household Durables	0.56	Insurance	-0.42
Food Products	0.37	Construction & Engineering	-0.24
Oil, Gas & Consumable Fuels	0.34	Diversified Telecom. Services	-0.14

COUNTRY			
Top 5 Contributors		Top 5 Detractors	
	%		%
Japan	1.74	United States	-2.73
Brazil	0.41	China	-0.21
Germany	0.31	India	-0.19
South Korea	0.28	Mexico	-0.12
France	0.26	Spain	-0.05

COMPANY			
Top 5 Contributors		Top 5 Detractors	
	%		%
Briggs & Stratton Corp.	0.59	APT Satellite Holdings Ltd ORD	-0.20
Invacare Corp	0.57	Countrywide PLC	-0.20
Hitachi Koki Co Ltd ORD	0.53	Reliance Infrastructure Ltd.	-0.19
Embraer S.A. ADR	0.43	Companhia Paranaense de Energia AI	-0.16
Beazer Homes USA Inc.	0.34	Weiqiao Textile Co. Ltd.	-0.15

LAST 12 MONTHS

INDUSTRY			
Top 5 Contributors		Top 5 Detractors	
	%		%
Oil, Gas & Consumable Fuels	8.19	Metals & Mining	-1.13
Machinery	1.32	Equity Real Estate Inv. Trusts	-1.08
Food & Staples Retailing	1.21	Banks	-0.95
Household Durables	1.20	Aerospace & Defense	-0.81
Health Care Equip. & Supplies	0.78	Real Estate Mgmt & Development	-0.79

COUNTRY			
Top 5 Contributors		Top 5 Detractors	
	%		%
United States	3.13	India	-0.62
Japan	2.90	Spain	-0.26
United Kingdom	1.25	Mexico	-0.24
Brazil	0.77	Switzerland	-0.18
Belgium	0.68	Italy	-0.14

COMPANY			
Top 5 Contributors		Top 5 Detractors	
	%		%
Chesapeake Energy Corp.	5.01	Debenhams PLC ORD	-0.78
Briggs & Stratton Corp.	1.15	Embraer S.A. ADR	-0.67
Wm. Morrison Supermarkets PLC	1.08	Balfour Beatty PLC ORD	-0.49
Dorel Industries Inc. Cl. B	0.79	Rent-A-Center Inc.	-0.38
D'leteren SA ORD	0.66	APT Satellite Holdings Ltd ORD	-0.37



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Quarterly Additions/Deletions

Additions
Kissei Pharmaceutical Co Ltd
Sankyo Co Ltd
Viver Inc. e Construtora SA
Banco Popular Espanol

Deletions
Sega Sammy Holdings Inc
Urbi Desarrollos Urbanos 1.00% Oct 23/22
Desarrolladora Homex Tranche 3 1.00% Oct 23/22
Fuji Machine Mfg. Co. Ltd.
Chesapeake Energy Corp 8.00% Dec 15/22
Chesapeake Energy Corp 6.625% Aug 15/20
Noritsu Koki Co. Ltd.
Chesapeake Energy Corp 8.00% Dec 15/22
Viver Inc. e Construtora SA 2.00% Aug 06/16

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