

SMALL CAP VALUE

MARKET COMMENTARY

The Russell 2000 Index delivered a robust 9.3% return in the third quarter of 2024. Small value stocks outperformed small growth stocks during the quarter (+10.2% vs. +8.4%). Performance was positive across 10 of the 11 Russell 2000 GICS sectors. While small caps outperformed large caps, the relative valuation of small caps to large caps remains attractive. The Russell 2000 Value Index traded at a forward P/E ratio of 16.7x at the end of the quarter, which is modestly more attractive than the broader Russell 1000 Index at 20.8x, according to Bloomberg.

Macroeconomic factors significantly influenced market performance during the quarter. The easing of inflationary pressures paved the way for lower interest rates, benefiting rate-sensitive sectors like real estate, communication services, financials, and utilities, particularly those with high leverage. While our portfolio is underweight most of these sectors, financials remains our largest sector weight, though we are underweight relative to the benchmark by about 7 percentage points.

Conversely, sectors that typically thrive in inflationary environments, such as energy and materials, underperformed, despite materials stocks receiving a boost late in the quarter from recently announced stimulus measures in China. Sentiment in oil and gas stocks reached a historic low in the quarter. Despite our slight overweight in these sectors, we anticipate improved performance as the economic landscape evolves and sentiment improves.

The technology sector also underperformed during the quarter, as investors assessed relative valuations and weighed the potential for an economic slowdown. Technology remains the largest overweight sector in our portfolio. We view the businesses in our portfolio as less cyclical than generally understood and offer attractive diversification to complement other cyclical positions. We remain confident in our technology holdings' ability to drive economic growth and deliver attractive returns.

Looking ahead, lower interest rates are typically favorable for markets, particularly for small caps. However, it is critical to focus on long-term trends rather than short-term fluctuations. We are committed to identifying businesses with durable balance sheets, sustainable return on equity, stable free cash flow, and attractive valuations relative to expected earnings. Our decision to underweight high-leverage companies reflects our focus on seeking better risk-adjusted returns elsewhere. We believe our investment strategy, centered on identifying undervalued assets and effective risk management, is poised to generate consistent long-term returns.

ATTRIBUTION ANALYSIS – 3Q24

The Hotchkis & Wiley Small Cap Value portfolio underperformed the Russell 2000 Value Index in the third quarter of 2024 (gross and net of management fees). Stock selection and the overweight in energy detracted the most from relative performance in the quarter. Stock selection in consumer discretionary, materials, financials, and communication services also detracted in the quarter. Conversely, stock selection in technology was a strong positive contributor in the quarter. Stock selection in industrials and real estate also worked well.

Net of fee composite performance as of 9/30/24: 17.45%, 13.77%, and 9.02% for 1-, 5-, and 10-year, respectively. Net performance results are presented after management fees and all trading expenses but before custodial fees. Additional disclosures provided in Endnotes.

Past performance is no guarantee of future results.



SMALL CAP VALUE

Endnotes:

All investments contain risk and may lose value. This commentary is for general information only and should not be relied on for investment advice or recommendation of any particular security, strategy, or investment product.

Portfolio characteristics and attribution are based on a representative Small Cap Value portfolio. Attribution is an analysis of the portfolio's return relative to the index, is calculated using daily holdings information and does not reflect management fees and other transaction costs and expenses; interaction effect is combined with stock selection. Returns can differ from certain client portfolio(s) due to data differences, cash flows, trading, and other activity (data source: Bloomberg, Russell).

The value discipline used in managing accounts in the Small Cap Value strategy may prevent or limit investment in major stocks in the Russell 2000 Value and returns may not be correlated to the index. Composite performance is available at www.hwcm.com, located on the strategy's Performance tab along with important disclosures included in the strategy's [GIPS Report](#); quarterly characteristics and portfolio holdings are located on the Portfolio and Literature tabs. For a list showing every holding's contribution to the overall account's performance and portfolio activity for a given time period, contact H&W at hotchkisandwiley@hwcm.com. Portfolio information is subject to the firm's portfolio holdings disclosure policy.

The Russell 2000[®] Index measures the performance of the 2,000 smallest companies in the Russell 3000[®] Index. The Russell 2000[®] Value Index measures the performance of those Russell 2000[®] companies with lower price-to-book ratios and lower forecasted growth values. The Russell 2000[®] Growth Index measures the performance of those Russell 2000[®] Index companies with higher price-to-book ratios and higher forecasted growth values.

Russell Investment Group is the source and owner of the Russell Index data contained herein (and all trademarks related thereto), which may not be redistributed. The information herein is not approved by Russell. H&W and Russell sectors are based on the Global Industry Classification Standard (GICS) by MSCI and S&P.

Equity securities may have greater risks and price volatility than U.S. Treasuries and bonds, where the price of these securities may decline due to various company, industry and market factors. Investing in smaller and/or newer companies involves greater risks than those associated with investing in larger companies, such as business risk, significant stock price fluctuations and illiquidity.

A value-oriented investment approach involves the risk that value stocks may remain undervalued or may not appreciate in value as anticipated. Value stocks can perform differently from the market as a whole or from other types of stocks and may be out of favor with investors and underperform growth stocks for varying periods of time. Investment risk disclosures for the firm's strategies are described in Part 2A of Form ADV of H&W.

Information contained in this material may represent or be based on forward-looking statements. Due to various risks and uncertainties, actual events/results or performance of the strategy may differ materially from those reflected or contemplated in such forward-looking statements. Information based on forecasts, proprietary or third-party estimates cannot be guaranteed and are subject to change. Information obtained from independent sources is considered reliable, but H&W cannot guarantee its accuracy or completeness.

Portfolio managers' opinions and data included in this commentary are as of September 30, 2024. Any discussion or view of a security, an asset class/segment, industry/sector and/or investment type are not investment recommendations, should not be assumed to be profitable, and are subject to change without notice.