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Neuberger Berman Small Cap Intrinsic Value

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Performance Highlights

The Small Cap Intrinsic Value strategy posted a loss for the first quarter of 2025 and underperformed the Russell 2000 Value Index (the "R2V" or the "Index") which also declined for the month.

Regardless of the 'master plan' or whatever future 'prize' awaits, tariff fears have created an environment that is as 'risk off' as it gets. Small caps and cyclicals are aggressively sold or shorted for risk mitigation. The first week of April hasn't been kind to say the least as the portfolio continued to lose ground.

Market Context

We didn't care for the first movie featuring a newly elected President in love with his ability to sow fear into investors and trade partners with middle of the night tariff tweets, and we're really not enjoying the sequel. Well at least not the first three and half months. Six weeks of enthusiasm for deregulation and tax cuts quickly morphed into tariff and recession anxiety. It's too early to tell how much the trade proposals are rooted in the idea that globalization has hurt the United States more than it has helped, or rather a tool to level the playing field by eliminating indirect barriers and predatory practices that have hamstrung American companies. Fortress America or a tough opening gambit for fairer trade – we're still not sure.

Motives matter but, in our view, there is a basic intention to charge the world for access to the U.S market. It's just a matter of price – tariffs or commitment to invest in the U.S. So how much does the investor calculus change? Well, candidly a lot. Inflation stays higher, recession risks grow and capital allocation decisions bog down.

Portfolio Review

The first quarter is long gone in the rearview mirror but here's a quick recap. In January, our technology investments and exposure to the AI megatrend generated relative and absolute performance buoyed by several large datacenter investment announcements. Performance quickly reversed with the news around the 'Deepseek' AI model. Many questioned how much compute will be required in the future. Others argued that narrower, skinnier language models are healthy and will continue to drive demand for compute as more applications are built around tailored models. We're in the camp that compute needs only grow with time. The AI narrative, while still relevant for the long term, took a back seat as trade policy with Canada and Mexico quickly grabbed investor attention and the speculation as to what else lay ahead. Needless to say, the April 2nd announcement was far worse than feared.

BEST AND WORST PERFORMERS FOR 1Q 2025[1]

Best Performers	Worst Performers
TechnipFMC plc	Ciena Corporation
ViaSat, Inc.	Veeco Instruments Inc.
AerCap Holdings NV	Resideo Technologies, Inc.
Devon Energy Corporation	MACOM Technology Solutions Holdings, Inc.
OSI Systems, Inc.	Conduent, Inc.

1. Reflects the best and worst portfolio performers for the year, in descending order, based on individual security performance and portfolio weighting. Positions may include securities that are not held in the portfolio as of 3/31/2025. Information is based upon a composite account and additional information regarding the performance contribution calculation methodology is available upon request. Specific securities identified and described do not represent all of the securities purchased, sold or recommended for advisory clients. It should not be assumed that any investments in securities identified and described were or will be profitable.

Outlook

In light of the current environment, we've conducted a review of the portfolio's exposure to global trade and the risk to earnings from a recession.

We've never been shy about the fact that the portfolio has more revenues tied to global markets than our benchmark. In fact, we view it as a long-term driver of alpha. When a company has the right products, why not play on the global stage rather than just to a domestic audience? International revenues have contributed to faster growth and more profits, in turn driving shareholder returns for many of our technology and healthcare investments. Also worth noting is that approximately 25 percent of our portfolio companies' assets are non-US; this is also greater than the small cap benchmarks.

At first blush increasing barriers and costs to trade will not only be hard on many companies but for us could present relative performance challenges. Fair enough but consider the following possibility – if Europe and China conclude that export driven growth has peaked, they will probably adopt measures to encourage domestic consumption, like lowering rates (already happening) and increasing government spending on healthcare and defense (also happening). On the other hand, the US economy is already largely driven by consumer spending. Higher prices as well as fears of unemployment together with declining household wealth will likely restrain domestic spending. While US-based manufacturing could get a boost from trade policy, it may not be enough to propel our consumption-based economy forward. Maybe it's not so bad to have some foreign operations and sales. To be determined. Our thought is to simply look past the initial shock and ponder how matters could play out over a longer time horizon.

The bigger concern after the April 2nd 'Liberation Day' announcement was whether the broader tariff policy will drive the U.S and the global economy into recession. We thought it would be worthwhile to examine how our current portfolio companies' earnings fared during the 2008-2009 Global Financial Crisis and the 2020 COVID-19 period, two recessionary periods characterized by downward demand shocks.

The data seems to indicate that in each period our companies suffered earnings declines less severe than our two small cap benchmarks. I wouldn't over extrapolate from this observation and imply much because it's a small sample. Both recessions had different root causes and resolutions as well as varied winners and losers, but the first pass analysis on the surface does not indicate outsized relative earnings risk to the portfolio in aggregate. However, we are concerned that the certain country tariffs will present a steep challenge to individual technology companies like Veeco and several others that either export to or import from China. One additional point as we head into earnings season and look for clues into potential sales and profit impacts. We believe companies will refrain from annual guidance until more tariff clarity emerges, but managements will also be quick to highlight the general challenges that tariffs pose to their operations. Highly asymmetrical corporate narratives will not inspire much confidence. Uncertainty will prevail, fueling investor angst and maybe more selling. At some point, when enough damage has been done, governments here and abroad will come to the table and address the issues that brought us to this unhappy and out-of-balance place.

In our year-end communication we wrote that 'seatbelts for the duration of the flight' were recommended. It's more turbulent than expected but we've weathered and navigated storms before and remain guardedly optimistic that we can do so again. Nevertheless, we're all going to need strong stomachs and lots of patience.

Information is as of March 31, 2025.

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Intrinsic value reflects the team's analysis and estimates. There is no guarantee that any intrinsic values will be realized; security prices may decrease regardless of intrinsic values.

The **Russell 2000 Value® Index** measures the performance of those Russell 2000 Index companies with lower price-to-book ratios and lower forecasted growth values. The index is market cap-weighted and includes only common stocks incorporated in the United States and its territories. (Russell 2000® Index: measures the performance of the 2,000 smallest companies in the Russell 3000® Index, which represents approximately 10% of the total market capitalization of the Russell 3000® Index. The index is market cap-weighted and includes only common stocks incorporated in the United States and its territories.)

Effective after the market close on March 21, 2025, FTSE Russell is implementing a capping methodology to all Russell U.S. Style Indices including this one. Any individual company weights in the index greater than 22.5% will be capped, and the sum of all individual companies that have an index weight greater than 4.5% will be capped to a 45% aggregate weight in the index. This will be applied quarterly going forward, but historical index returns will not be restated.

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