QUARTERLY COMMENTARY

Ariel Focused Value

• Value • Focused Value • Global

Quarter Ended September 30, 2022

All major indices closed out the third quarter at a loss, marking the first time Wall Street posted three consecutive quarters of declines since the aftermath of the global financial crisis. Persistently high inflation, escalating geopolitical tensions in Russia/Ukraine, energy-price shocks and aggressive central-bank tightening have weighed on consumer and business confidence. Recession watch has taken hold as many investors fear a Fed-induced hard landing. While Wall Street sits on edge and markets remain erratic, we are actively leaning into the moment by judiciously acquiring the downtrodden shares of quality companies whose value we believe should be realized over the long term. Against this backdrop, the Ariel Focused Value Composite dropped -7.29% gross of fees (-7.44% net of fees) in the quarter, trailing the -5.62% return posted by Russell 1000 Value Index and the -4.88% loss of the S&P 500 Index.

Several stocks in the portfolio had strong returns in the quarter. Regional banking services provider **BOK Financial Corporation (BOKF)** advanced in the quarter, as reflation themes in the marketplace raised interest rate expectations, boosting positive net-interest-margin trends. Additionally, the company continued to report solid loan growth along with tight expense controls, providing a tailwind for shares. Looking ahead, we believe BOKF's strong underwriting standards, diversified business model (which includes banking and fee service businesses), and experienced management team continue to present a long-term opportunity.

Shares of orthotic and prosthetic (O&P) specialist **Hanger, Inc. (HNGR)** also traded significantly higher in the period. The company announced plans to go-private and be acquired by a private equity firm in an all-cash transaction.

Additionally, producer and marketer of crop nutrients **Mosaic Co. (MOS)** traded higher on solid financial results. MOS continues to demonstrate its ability to raise prices and offset input cost inflation, as well as return significant capital to shareholders through buybacks. Meanwhile, trade flows have shifted with Russia and Belarus, the second and third largest fertilizer exporters globally, banning exports and facing sanctions imposed by the West. As a result, MOS is expanding production to help meet global demand. Given management's optimistic outlook and disciplined approach towards capital allocation, we continue to believe the company is well-positioned from a risk/reward standpoint.

By comparison, shares of leading manufacturer and distributor of medical devices specializing in spine and dental products **ZimVie, Inc. (ZIMV)** sharply declined in the quarter, following a downward revision in full-year guidance. Over the long-term, we believe the foreign exchange headwinds the company is facing will soften and expect the management team to enhance its focus on research and development, as well as expand the product portfolio across its core value chain.

Leading manufacturer and distributor of floorcovering products **Mohawk Industries Inc. (MHK)** also detracted from relative returns in the quarter. MHK has consistently demonstrated its ability to deliver sales growth and generate strong cash flow despite significant inflation, rising interest rates and geopolitical instability. However, this quarter was an inflection point as the slowing U.S. housing market began to change consumer discretionary spend. Higher natural gas prices and constrained supply in Europe presented another headwind. Given these factors, MHK guided to softening demand and increasing pressure on margins moving forward. Management initiated corrective actions across the enterprise including implementing further price increases, enhancing service levels and restructuring to reduce costs. In our view, MHK's track record of success managing through economic cycles and healthy balance sheet have the company well-positioned to benefit from long-term growth in residential remodeling, new home construction and commercial projects. At current levels, MHK is trading at a -67% discount to our estimate of private market value.

Lastly, global leader in money transfer services **Western Union Company (WU)** traded lower in the period on mixed earnings results. Softness in retail money transfer resulted in weaker than expected revenues, however, operating profit margin expansion drove a bottom-line beat. Management also continues to return capital to shareholders through dividends and share repurchases. Although the company anticipates the macroeconomic environment will continue to slow, it reminded investors remittances have proved resilient in prior periods of economic contraction. At current levels, WU is trading at a -41% discount to our estimate of private market value.

We initiated three new positions in the quarter. We added leading financial institution Bank of America Corporation (BAC) which serves individual consumers, small and middle-market businesses, and large corporations with a full range of banking, investing, asset management, and other financial and risk management products and services. The current company was formed through various mergers including NationsBank, FleetBoston, US Trust, Countrywide Financial, and Merrill Lynch with the legacy commercial bank to form a national banking powerhouse and bulge bracket investment firm. As one of the 'Big Four' U.S. banks it enjoys scale driven cost advantages and economies of scale which provide meaningful competitive advantages and potential for strong returns in the largely commoditized banking industry. A survivor of the financial crisis, BAC has emerged with a solid capital base and stands to benefit from a rising interest rate environment.

We also bought shares of two companies held in other Ariel portfolios, leading global manufacturer of power generation equipment Generac Holdings, Inc. (GNRC) and bar-code manufacturer Zebra Technologies (ZBRA). GNRC has an unmatched distribution network and product portfolio and enjoys strong brand advantages. We believe this creates a wide moat for this niche business which commands a 75% market share in the North American residential market. Historically, growth has been limited due to a lack of awareness around the benefits of having a home standby generator, as well as its high price point. More recently, however, elevated power outage events, both weather-related and due to aging infrastructure, have tipped the scales of awareness in both the residential and commercial markets, which should result in a long-runway of market penetration-led growth, margin expansion and free cash flow generation. The stock was a pandemic darling but has since traded off substantially giving us an opportunity to acquire shares in this unique, high-quality business.

Meanwhile, ZBRA's brand strength, distribution network and commitment to innovation enable it to take share, earn industry-leading profitability and penetrate new markets. A recent pullback in stock price provided an attractive entry point. Shares have come under pressure due to investor concerns around inflation and supply chain disruptions. At current valuation levels, we think investors are underappreciating ZBRA's alignment with the global effort to improve supply chain efficiency. At the same time, the company is leveraging the wide moat in its core business to expand into faster growing markets including warehouse robotics and machine vision. Meanwhile ZBRA continues to deliver prodigious free cash flow which we believe will continue to be deployed towards both growth and share repurchases.

By comparison, we exited our positions in Stanley Black & Decker, Inc. (SWK) and leading manufacturer of consumer food products J.M. Smucker Company (SJM) on valuation. We also sold out of Hanger, Inc. (HNGR) upon its decision to go-private and leading entertainment company Paramount Global (PARA) to pursue other opportunities.

Escalating geopolitical tensions, persistently high inflation, slowing economic growth and the potential for excessive Fed tightening continue to fuel recessionary fears. And yet, we view the probability of the most severe "hard landing," or deep recession, to be less likely. Unemployment remains near historic lows and balance sheets of U.S. financial institutions and households are generally in good shape. We continue to be cautiously optimistic these factors will protect against a severe downturn. Meanwhile, values are abundant when the investment environment feels the most uncomfortable. With 39 years of experience, we are trained and battle-tested for these moments. We believe bear markets and oversold stocks create ripe buying opportunities for long-term, patient investors. We are diligently evaluating the collapsing prices of stocks on our watchlist versus our expectations of what these companies and their underlying business fundamentals should be valued at over the long-term. In times like these, we believe the worstcase scenario gets priced in giving us a margin of safety[1] to buy and hold our favorite companies with confidence through the uncertainty until the market digests the volatility. Although our portfolios have sold off in recent months, in our view they are statistically cheap—trading at a significant discount to their private market values (PMV)[2]—or what some call intrinsic worth. In the past, portfolio dislocations of this magnitude have often served as a prelude to our most robust recoveries.

Past performance does not guarantee future results. Performance results are shown net of the highest management fee charged to any client in the Composite during the performance period. Net returns reflect performance returns after the deduction of advisory fees and transaction costs and assume the reinvestment of dividends and other earnings. For the period ended 9/30/22 the performance (net of fees) for the Ariel Focused Value Composite for the 1-, 5-, and 10-year periods was -13.81%, +4.77%, and +8.55%, respectively. For the period ended 9/30/22 the performance for the Russell 1000 Value Index and the S&P 500 Index for the 1-, 5-, and 10-year periods was -11.36%, +5.29%, and +9.17%, and -15.47%, +9.24%, and +11.70%, respectively. Actual fees may vary depending on, among other things, the applicable fee schedule and portfolio size. A complete fee schedule is available upon request and may also be found in Ariel Investments LLC's Form ADV, Part 2. Returns are expressed in U.S. dollars. Current performance may be lower or higher than the performance data quoted. The Ariel Focused Value Composite differs from its benchmark with dramatically fewer holdings concentrated in fewer sectors.

This commentary candidly discusses a number of individual companies. These opinions are current as of the date of this commentary but are subject to change. The information provided in this commentary does not provide information reasonably sufficient upon which to base an investment decision and should not be considered a recommendation to purchase or sell any particular security.

As of 9/30/22, BOK Financial Corporation constituted 6.39% of Ariel Focused Value Composite (representative portfolio); Mosaic Company 5.70%; ZimVie Inc. 1.92%; Mohawk Industries, Inc. 3.34%; Western Union Company 3.26%; Bank of America Corp. 1.23%; Generac Holdings Inc 2.26%; Zebra Technologies Corp. 1.53%; Hanger Inc. 0.0%; J M Smucker 0.0%; Paramount Global 0.0%; and Stanley Black & Decker Inc. 0.0%. Portfolio holdings are subject to change. The performance of any single portfolio holding is no indication of the performance of other portfolio holdings of the Ariel Focused Value Composite.

A glossary of financial terms provided herein may be found on our website at www.arielinvestments.com.

Index returns reflect the reinvestment of income and other earnings. Indexes are unmanaged, and investors cannot invest directly in an index. The Russell 1000® Value Index measures the performance of the large-cap value segment of the U.S. equity universe. It includes those Russell 1000 companies with lower price-to-book ratios, lower forecasted growth values and lower sales per share historical growth. Its inception date is January 1, 1987. Russell® is a trademark of London Stock Exchange Group, which is the source and owner of the Russell Indexes' trademarks, service marks and copyrights. Neither Russell nor its licensors accept any liability for any errors or omissions in the Russell Indexes or underlying data and no party may rely on any Russell Indexes and/or underlying data contained in this communication. No further distribution of Russell data is permitted without Russell's express written consent. Russell does not promote, sponsor or endorse the content of this communication. The S&P 500® Index is widely regarded as the best gauge of large-cap U.S. equities. It includes 500 leading companies and covers approximately 80% of available U.S. market capitalization. Its inception date is March 4, 1957.

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[1]Attempting to purchase a stock with a margin of safety does not protect investors from the loss of their investment, volatility associated with stocks, declining fundamentals, external forces, or our incorrect assumptions.
[2]Discount to Private Market Value ("PMV") represents the percentage discount at which the portfolio traded as compared to the portfolio holdings' PMV as determined by Ariel Investments. References to PMV are for the time period: 12/31/07 – 09/30/22.