



QUARTERLY COMMENTARY

Ariel Micro-Cap Value

• Value • Deep value • Global



Quarter Ended December 31, 2020

The S&P 500 and MSCI ACWI closed 2020 at all-time highs—a stunning outcome, few would predict amidst a global pandemic. Record levels of fiscal stimulus, ultra-low interest rates and low-inflation collectively set the tempo to an equity anthem. While growth trounced value on a full year basis, a shift occurred in the fourth quarter. Value bested growth, small cap issues outperformed their large cap brethren and investors increased their appetite for risk, favoring emerging markets over developed peers and U.S. equities.

For the quarter, the Ariel Micro-Cap Value Composite increased +29.57% gross of fees (+29.17% net of fees) trailing the Russell Microcap Value Index's +32.76% return and the Russell Microcap Index, which returned +31.39%.

Some holdings in the portfolio advanced considerably this quarter. Satellite communications operator **ORBCOMM, Inc. (ORBC)** was a top performer in the quarter. Earnings results exceeded expectations on better service and product revenues, as well as higher margins. Looking ahead, we continue to believe the integration of the company's diverse product lines and streamlining efforts will accelerate revenue growth, improve customer retention and drive cost efficiencies. At the current valuation, we believe the market is underappreciating ORBC's future free cash flow generation enabled by high barriers to entry, minimal capital needs, increasing scale advantages and growing demand to track and control fixed and mobile assets globally.

Additionally, leading creator of automotive access control products **STRATTEC Security Corporation (STRT)** traded significantly higher on better than expected earnings. Shares responded to an improved outlook, whereby the reopening of global automotive production drove major customers to restock inventories. STRT also benefitted from operating efficiencies and product mix.

Asset manager **Cowan Inc. (COWN)** was another top contributor in the quarter. The company reported an

earnings beat driven by strong performance across its brokerage and investment banking divisions. The firm also doubled its quarterly dividend and in late October, announced an expansion of its share repurchase program. COWN continues to gain momentum by scaling its businesses, driving margins, simplifying its revenue streams and aligning its balance sheet activities with the operating business. At current levels, we continue to view COWN as a misunderstood deep value opportunity that is trading at a discount to total book value.

Alternatively, several positions weighed on performance. **Kindred Biosciences, Inc. (KIN)**, a biopharmaceutical company focused on saving and improving the lives of pets, traded relatively flat for the quarter. As a result, KIN trailed the index and the rest of our portfolio holdings. Nonetheless, the company struck an exclusive global deal with Elanco Animal Health (ELAN) for its Parvovirus Monoclonal Antibody and continued to steadily advance its product development pipeline in the period. Despite the flow of good news, we believe investors will remain on the sidelines until a partnership develops for KIN's atopic dermatitis compounds and/or approval of the Parvovirus drug, which would result in milestone payments from ELAN and future royalties.

Glassbridge Enterprises Inc. (GLAE) is a holding company whose subsidiaries focus primarily on investments and asset management. Shares declined during the period, which we believe is a result of extreme illiquidity in a very small, thinly traded stock. We continue to believe GLAE is an overlooked name with value far above its current quote. GLAE's most valuable assets include Arrive, a private equity joint venture with RocNation; SportBLX, a new platform that allows sports enthusiasts to invest in athletes and sports team; and significant Net Operating Loss (NOL) carryforwards which the company hopes to monetize.

Lastly, digital video streaming subscription service focused on health and wellness **Gaia, Inc. (GAIA)** weighed on relative returns in the period. We believe this price action runs counter to the company's continued success. GAIA delivered a top and bottom line earnings beat and reported positive free cash flow,

as management had guided. Looking ahead, we believe GAIA is poised for continued double-digit subscriber and top-line growth, improving profitability and a strengthening balance sheet.

This quarter, we initiated a position in agricultural business and land management holding company **Alico, Inc. (ALCO)**. Based in Tampa, Florida, ALCO is the largest US producer of fruit used for orange juice. In addition to over 45,000 Florida acres utilized for citrus, the company owns more than 54,000 acres of ranch and other land which it has been selling. A program known as Alico 2.0 launched in 2017 under then CFO and now CEO John Kiernan has led to improved efficiency along with an emphasis on building and realizing shareholder value. We believe Alico stock has an attractive long-term growth opportunity, which is bolstered by the value of its Florida acreage.

On the sell side, we said farewell to long-time holding **Perceptron (PRCP)**. The precision optical system specialist was acquired by Sweden-based Atlas Copco in late December for \$7.00 per share in cash. We also successfully exited semiconductor substrates manufacturer **AXT, Inc. (AXTI)** and online advertising solutions provider **Magnite, Inc. (MGNI)** as shares reached our estimate of private market value.

Although concerns over rising coronavirus infections have been overshadowed by positive vaccine developments, the widespread pain on Main Street, including pronounced unemployment, battered small businesses, social unrest and political dysfunction remain headwinds. We view such risks as short-term discord within the context of our long-term investment horizon. We retain a "glass half full" outlook and believe the economy will continue to receive meaningful support from a dovish Fed, easing restrictions and the promise that vaccines will pave the way to a return to normalcy. Meanwhile, we stand ready to take advantage of any pull backs in the market on negative news. We strongly believe the dedicated, contrarian, patient investor that stays the course and consistently owns differentiated businesses with solid competitive positioning and robust balance sheets will deliver superior returns over the long-run.

Investing in micro-cap companies is more risky and volatile than investing in large companies. The intrinsic value of the stocks in which the portfolio invests may never be recognized by the broader market.

Past performance does not guarantee future results. Performance results are net of transaction costs and reflect the reinvestment of dividends and other earnings. For the period ended 12/31/20 the performance (net of fees) for the Ariel Micro-Cap Value Composite for the 1-, 3-, and 5-year periods was +11.45%, +1.79%, and +3.69%, respectively. For the period ended 12/31/20 the performance for the Russell Micro-cap Value Index and the Russell Micro-cap Index for the 1-, 3-, and 5-year periods was +6.34%, +4.33%, and +10.50%, and +20.96%, +8.78%, and +11.89%, respectively. Net performance of the Ariel Micro-Cap Value Composite has been reduced by the amount of the highest fee charged to any client in the Composite during the performance period. Actual fees may vary depending on, among other things, the applicable fee schedule and portfolio size. Fee information 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 Micro-Cap Value Composite differs from its primary benchmark in that it has fewer holdings concentrated in fewer sectors.

Net returns of the Ariel Micro-Cap Value Composite beginning May 2009 reflect the deduction of the advisory fee. Net returns of the Ariel Micro-Cap Value Composite prior to May 2009 are net of a 20% incentive fee, other expenses, management fees, and profit allocations. The performance results prior to April 30, 2009 were achieved while David Maley managed the strategy at his prior firm using a substantially similar investment style. Mr. Maley began managing this strategy at Ariel on April 30, 2009. The performance results achieved at Mr. Maley's prior firm are linked to the performance results of the Ariel Micro-Cap Value Composite. The strategy will on occasion hold cash when values are difficult to identify. Also, the strategy at times includes temporary investments in Exchange Traded Funds (ETFs) while seeking other investment opportunities. During June 2004 through January 2008, the investment strategy included periodically holding short positions in certain ETFs. This practice may have had a material effect on returns.

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 12/31/20 ORBCOMM Inc. constituted 6.03% of the Ariel Micro-Cap Value Composite (representative portfolio); STRATTEC Security Corporation 0.46%; Cowen Inc 6.24%; Kindred Biosciences, Inc. 6.40%; GlassBridge Enterprises Inc 0.88%; Gaia, Inc. 4.13% and Alico, Inc. 2.03%. 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 Micro-Cap Value Composite.

Index returns reflect the reinvestment of income and other earnings. Indexes are unmanaged, and investors cannot invest directly in an index. The Russell Microcap® Value Index measures the performance of the microcap value segment (companies that are considered more value oriented, relative to the overall market) of the U.S. equity market. The Russell Microcap® Index measures the performance of the microcap segment (1,000 of the smallest securities in the small-cap Russell 2000® Index) of the U.S. equity market. Frank Russell Company ("Russell") is the source and owner of the trademarks, service marks and copyrights related to the Russell Indexes. Russell® is a trademark of Frank Russell Company. 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.