QUARTERLY COMMENTARY

Ariel Global

• Value • Global

Quarter Ended September 30, 2022

Central banks around the world worked to reign in inflation with interest rate hikes, while quantitative tightening (QT) represented a regime change. Both efforts drove all major indices into the red this quarter. Meanwhile, Russia's war in Ukraine, China's zero-Covid policy, record debt and concerns over the economic outlook for the Eurozone pose further threats to the global economy. Recession watch has taken hold as many investors fear a full-blown energy crisis and central bank-induced hard landing. While Wall Street sits on edge and markets remain erratic, we continue to steer clear of what we call the 4Ls: Lofty Valuations, Loss Making Companies, Leveraged Balance Sheets and Liquidity Risk. Our low portfolio turnover continues to underscore our patient approach as we believe our global portfolios, which are heavily weighted towards undervalued, higher dividend yielding and better-quality defensive holdings, should produce strong long-term performance. Against this backdrop, the Ariel Global Composite fell -9.67% gross of fees (-9.85% net of fees) in the quarter, underperforming the MSCI ACWI Index and the MSCI ACWI Value Index returns of -6.82% and -7.66%, respectively.

Ariel's non-consensus approach seeks to identify undervalued, out-of-favor, franchise-quality companies that are misunderstood and mispriced. The Ariel Global strategy continues to be significantly overweight defensive sectors such as Health Care, Communication Services and Consumer Staples, as well as meaningfully underweight Industrials and Information Technology, and lacks exposure to Energy and Materials. At the sector level, Communication Services and Consumer Discretionary holdings were the biggest performance detractors, while our cash position was the largest source of positive attribution in the quarter.

At the stock level, biopharmaceutical company **Gilead Sciences, Inc.** was the top contributor in the quarter based on positive data released in a study evaluating Trodelvy versus comparative chemotherapy in patients with metastatic breast cancer. The detailed findings increased investor confidence the drug would receive incremental approvals for a broader range of breast cancer treatments. Shares also received a boost on news the TAF patent portfolio for HIV drugs will be extended from the middle of this decade through the early 2030s, thereby lengthening the company's long-term opportunity in the virology market.

Global pharmaceutical and diagnostics leader **Roche Holding AG** also advanced in the quarter on a top- and bottom-line earnings beat. The pharmaceutical portfolio is performing well, and the diagnostics segment continues to demonstrate strong growth momentum as it experiences a further normalization of post-pandemic trends. Roche's deep research and development (R&D) franchise enhances our enthusiasm for the name. As we consider risk throughout each step of our investment process, we prefer to invest in companies with proven capabilities, rather than those with binary outcomes such as future earnings hinging on the approval of one super drug. We view Roche as a quality defensive name with a rich suite of best-in-class pipeline opportunities, including those with favorable risk/reward potential for Alzheimer's disease.

Peruvian banking franchise **Credicorp, Ltd.** was another contributor to relative returns in the quarter as improving financial results and successful execution across its digital initiatives drove shares higher. We remain focused on Credicorp's attractive long-term earnings potential. The company continues to garner higher customer satisfaction and strengthen its competitive moat by educating the unbanked and prospecting through a centralized data analytics platform to expand its client base. The company also views venture capital and the underdeveloped fintech market in Peru as an opportunity to boost growth and enhance shareholder value. At current levels, we believe the valuation is attractive and think Credicorp's risk/reward dynamics are skewed to the upside, particularly in a rising interest rate environment.

By comparison, healthcare leader **GSK plc** was the largest detractor from performance in the quarter. Investors are concerned about legal liabilities associated with its antacid drug Zantac. While it is impossible to know the outcome with certainty, our preliminary assessment suggests that the decline in market capitalization exceeds the likely financial impact on the company.

China's internet search and online community leader **Baidu, Inc.** also weighed on relative results in the quarter. Continuing macro headwinds driven by China's zero-Covid policy are resulting in sluggish advertising trends. Looking ahead, the company remains committed to sustainable, profitable growth as management works to improve overall operational efficiency, executing on its strategic commitments around technological innovation and the transition to a green economy. We also continue to be enthusiastic about Baidu's longer-term opportunity for revenue growth and margin expansion across internet search, cloud, autonomous driving, artificial intelligence and online video.

Lastly, British home and auto insurer **Direct Line Insurance Group PLC** traded lower in the period as elevated prices for new and used cars alongside a tight global automotive supply chain have increased the cost of claims across the auto insurance industry. We remain enthusiastic about this investment opportunity given its high levels of normalized profitability. We expect the company to benefit from price increases in future premiums.

We initiated two new positions in the quarter. We added British multinational consumer healthcare company **Haleon PLC** following its spin-off from longtime holding GSK plc. The company's world-class portfolio of health brands is delivering double-digit organic revenue growth and margin expansion across channels and geographies. We continue to see potential for significant incremental value creation from a more focused and independent consumer health franchise in the years ahead.

We also purchased Italian gas distributor **Italgas Spa**. We like the business for its stable cash flows and believe it is generally protected from fluctuations in volumes or pricing of the commodity. In addition, management continues to deliver strong operational and financial performance. This is due in part to continued digitalization of the network as well as the integration of sustainability targets, which help direct investment choices towards the energy transition process, in line with EU guidelines. We also expect the company's acquisition of Depa will aid Italgas' bottom-line and increase the strength of longer-term cash generation.

By comparison, we exited **Japan Tobacco, Inc.** based on both price appreciation and increasing questions regarding the capacity of the company to execute on next generation, reduced-risk products as effectively as competitors. In our view, emerging signs of ESG weakness at JT seem unlikely to reverse.

High and persistent inflation, supply chain disruptions and lingering demand-related distortions have forced policymakers to reverse course from quantitative easing (QE) towards a new regime defined by quantitative tightening (QT). QT and rapidly rising interest rates may help curb inflation, but this will likely be at a great cost to economic growth. Although stocks look considerably less expensive than they did at the start of the year, we do not believe broad market valuations have come down enough to reflect the impact further rate hikes will have on corporate profits, as greater debt servicing costs weigh on the bottom line. Taken together, we view these factors to be an increasing source of vulnerability for market multiples. In our view, the repricing of risk across asset classes is not yet done. For this reason, we expect lower quality equities to be among the most vulnerable. We think the sweet spot will be owning undervalued, high dividend yielding, quality companies with resilient business models and strong balance sheets. We have strong conviction in our current positioning and believe our global portfolios are poised for long-term outperformance.

Investments in foreign securities may underperform and may be more volatile than comparable U.S. stocks because of the risks involving foreign economies and markets, foreign political systems, foreign regulatory standards, and foreign currencies and taxes. The use of currency derivatives, exchange-traded funds (ETFs) and other hedges may increase investment losses and expenses and create more volatility. Investments in emerging markets present additional risks, such as difficulties in selling on a timely basis and at an acceptable price. The intrinsic value of the stocks in which the portfolio invests may never be recognized by the broader market. The portfolio is often concentrated in fewer sectors than its benchmarks, and its performance may suffer if these sectors underperform the overall stock market. Investing in equity stocks is risky and subject to the volatility of the markets.

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 9/30/2022, the performance (net of fees) of the Ariel Global Composite for the 1-, 5-, and 10-year periods were -9.47%, +3.02%, and +7.39%, respectively. For the period ended

9/30/2022 the performance for the MSCI ACWI Index and the MSCI ACWI Value Index for the 1-, 5-, and 10-year periods were -20.66%, +4.44%, and +7.28% and -13.97%, +1.71%, and +5.39% 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 Global Composite differs from its benchmark, the MSCI ACWI (All Country World Index), because the Composite has fewer holdings than the benchmark.

The opinions expressed 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 9/30/2022 Gilead Sciences, Inc. constituted 6.09% of the Ariel Global Composite (representative portfolio); Roche Holding AG 6.76%; Credicorp Ltd. 3.49%; GSK plc 4.47%; Baidu, Inc. 5.45%; Direct Line Insurance Group Plc 1.79%; Haleon PLC 0.97%; Italgas SpA 0.23% and Japan Tobacco Inc. 0.00%; 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 Global Composite.

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

Indexes are unmanaged. An investor cannot invest directly in an index. MSCI ACWI (All Country World Index) Index is an equity index of large and mid-cap representation across 23 Developed Markets (DM) and 24 Emerging Markets (EM) countries. Its inception date is January 1, 2001.The MSCI ACWI Value Index captures large and mid-cap securities exhibiting overall value style characteristics across 23 Developed Markets countries and 24 Emerging Markets (EM) countries. Its inception date is December 8, 1997. All MSCI Index net returns reflect the reinvestment of income and other earnings, including the dividends net of the maximum withholding tax applicable to non-resident institutional investors that do not benefit from double taxation treaties. MSCI uses the maximum tax rate applicable to institutional investors, as determined by the company's country of incorporation. MSCI makes no express or implied warranties or representations and shall have no liability whatsoever with respect to any MSCI data contained herein. The MSCI data may not be further redistributed or used to create indices or financial products. This report is not approved or produced by MSCI.