03/31/14

Ariel International Fund & Ariel Global Fund

TODAY'S BARGAINS: TRADITIONAL TECHNOLOGY

Performance data quoted represents past performance. Past performance does not guarantee future results. All performance stated in this document assumes the reinvestment of dividends and capital gains and represents returns of the Investor Class shares. We caution shareholders that we can never predict or assure future returns on investments. The investment return and principal value of an investment with our Funds will fluctuate over time so that your shares, when redeemed, may be worth more or less than their original cost. Current performance may be lower or higher than the performance data quoted. Click the following link for the annual expense ratio and standardized performance data current to the most recent quarter and month end periods for Ariel International Fund and Ariel Global Fund.

DEAR FELLOW SHAREHOLDER:

Global equity markets slowed down in the first quarter of 2014, which was of some relief to us. As you know, we are independent thinkers who focus intently on valuation, so when strong 2012 returns became an ebullient 2013 campaign, we became more skeptical looking forward. We welcomed the deceleration, during which the broad global indexes gained less than 2%. Our portfolios outperformed. Specifically, Ariel International Fund returned +2.18%, nicely ahead of the MSCI EAFE Gross Index, which moved +0.77%, while Ariel Global Fund gained +2.50%, topping the MSCI ACWI Gross Index, which went up +1.21%.

Since our international and global portfolios debuted at the end of December 2011, I have had the opportunity to present our investment process and philosophy to investors in great detail. Building a track record for the long run takes patience and discipline. Previously, we have emphasized our commitment to bottom-up stock-picking but have noted that bargains often cluster—sometimes by country, sometimes by sector, and in other various ways. For instance, in the second quarter of 2013, we wrote about our relatively heavy investments in Japan, and the next quarter, we wrote about health-care stocks. This quarter, we are writing about the technology area, in which we currently have a significant weighting.

In technology stocks, we are not making a sector bet. Rather, we perceive a valuation bifurcation within the sector that we believe has produced heavy risk in some stocks and opportunities in others. At first glance, one might think this stance runs parallel to the one in health-care stocks (which persists). While there are similarities, we think the differences are greater and more important.

One clear similarity between our tech and health-care holdings nicely illustrates our philosophy: Overall, our weightings are quite substantial when compared to the benchmarks. Unlike many practitioners, we do not start with an index's sector weightings and adjust them up and down based on macroeconomic factors. Rather, we buy specific stocks within a sector to an appropriate investment level—on a risk/reward basis—and only constrain once the weighting becomes quite heavy. For example, our health-care weightings fall between 11% in the developed market portfolio and 21% in the global portfolio. The global portfolio weighting is 10 percentage points higher than the benchmark or roughly twice as high. Meanwhile, our technology weights fall between 15% in the developed markets portfolio and 21% in the global portfolio, where the weighting is 8 percentage points higher than the benchmark. Although the absolute weighting in technology stocks is lowest in the developed markets portfolio, our weighting is more than triple the index's exposure of less than 5%. While some view such positions as risky on a relative performance basis, we view them as prudent on an absolute risk/reward investment basis.

> "…we perceive a valuation bifurcation within the sector that we believe has produced heavy risk in some stocks and opportunities in others."

Another parallel between the technology and health-care areas is their historical association with growth investing. Health-care stocks have generally, although not currently, had heavier weightings in growth indexes than in value benchmarks. This is even more true of technology stocks. Over long periods, investors have expected faster growth from tech firms than companies in other areas such as utilities, energy and financial services. While we do admire future growth, we do not think our style is "drifting" with these exposures, since we view every opportunity as a mix of current valuation and future expected growth. Sometimes an area with strong secular growth prospects appears cheap on a valuation basis, while other times it seems expensive relative to its likely future. In the case of the former, we are happy to invest a significant amount; that does not mean, however, that we have changed our stripes or adopted a new philosophy.

That statement brings us to the most significant difference between our current interest in technology and health care. As detailed six months ago, the market broadly concluded health-care companies were not growing as swiftly as they once did, causing valuations to fall across the sector. Something very different has happened in the technology sector. That is, expectations for certain technology companies are extremely high, while other technology companies reflect low growth assumptions. In other words, sometimes we find opportunities when investors give up on a broad area; other times, we find opportunities when the crowd gravitates toward one industry and ignores similar ones.

> "…we view every opportunity as a mix of current valuation and future expected growth."

The market's current darlings are the recently public social media firms. To be sure, Facebook Inc., Twitter Inc., LinkedIn Corp., and Yelp Inc. have been as remarkable and game-changing as the Internet blue chips from years past: Amazon.com, Inc., eBay Inc., and Google Inc. are obvious examples. Investors, however, have historically shown a suspect ability to separate such long-term winners from those that fail to live up to expectations. Remember Pets.com, theglobe.com, Inc., and Webvan? They, too, once traded at sky-high valuations along with the eventual Internet blue chips but did not pan out.

> "When we see valuations spike on exciting but unproven companies, we become nervous."

When we see valuations spike on exciting but unproven companies, we become nervous. Because some of today's favorites are not yet profitable, we will use an Enterprise Value/Sales ratio[1] to sketch their valuations: LinkedIn trades at 15.6x; Facebook at 16.3x, Yelp at 19.3x, and Twitter at a remarkable 51.5x. Were a larger company to acquire one of these companies at the market price, it would pay, on average, $22 for every $1 of revenue the company produced over the last year. Again, that is not $22 per every $1 of *profit,* but for every dollar of *revenue.* True, it is possible that such companies will grow fast and far enough to justify current valuations. That said, at those valuations, the risk/reward tradeoff more closely resembles speculation than it does prudent investing.

The good news is that within the same broad technology area, other companies are trading very cheaply on the same metrics. Moreover, these are not new, unproven companies. Rather, they are global titans with robust cash flows, diversified product offerings, and strong market positions—names such as Microsoft Corp., Nokia Corp. and Broadcom Corp. These are the types of companies that compose the significant technology weightings in our portfolios. The companies listed on the following page, the technology companies in our global portfolio, have an average enterprise value/sales ratio of just 2.6x. Based on this one metric, they would cost a hypothetical acquirer roughly one tenth as much as the popular social media companies mentioned on the previous page:

Ariel global technology holdings *as of March 31, 2014*

Company	EV/Sales
Canon Inc.	0.8x
Nokia Corp.	1.0x
QLogic Corp.	1.2x
NVIDIA Corp.	1.3x
Nintendo Co., Ltd	1.4x
Tokyo Electron Ltd.	1.7x
Broadcom Corp.	1.7x
Dialog Semiconductor plc	1.7x
EMC Corp.	2.1x
Global Payments Inc.	2.3x
Microsoft Corp.	3.0x
TIBCO Software Inc.	3.1x
Ruckus Wireless, Inc.	3.8x
Baidu, Inc.	11.2x
Average	2.6x

As investors who consider both risk and reward in assembling a portfolio, we strongly favor these time-tested companies with strong business models, defensible market positions and relatively low valuations to today's high flyers. Moreover, we believe the near frenzy around today's social media darlings has helped make traditional technology companies seem less interesting and exciting—and cheap. To be clear, however, we are not simply making a "bet" on established technology companies and eschewing the new ones. Rather, within the cheaper end of the technology space, we have found a fairly large number of specific companies that are good risk/reward tradeoffs at current valuations.

As always, we appreciate the opportunity to serve you and welcome any questions or comments you might have. You can also contact us directly at email@arielinvestments.com.

Sincerely,

Rupal J. Bhansali

Rupal J. Bhansali
Portfolio manager

[1]The Enterprise Value/Sales valuation ratio compares a company's overall enterprise value (equity plus debt) to its sales (or revenues). The metric is quite useful when assessing a company's valuation in the event of an acquisition. In a takeover, the acquirer would need to not only purchase the equity but also cover the debt. Sales or revenues are often used when a company is young or unprofitable.

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, foreign currencies and taxes. The use of currency derivatives and ETFs may increase investment losses and expenses and create more volatility. Investments in emerging and developing 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 Funds invest may never be recognized by the broader market.

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 letter is not reasonably sufficient upon which to base an investment decision and should not be considered a recommendation to purchase or sell a particular security.

Portfolio holdings are subject to change. The performance of any single portfolio holding is no indication of the performance of other portfolio holdings of Ariel International Fund, Ariel Global Fund or of the performance of the Funds. Click here for the most recent holdings for Ariel International Fund and Ariel Global Fund.

MSCI EAFE® Gross Index is an unmanaged, market weighted index of companies in developed markets, excluding the U.S. and Canada. MSCI ACWI (All Country World Index) Gross Index℠ is an unmanaged, market weighted index of global developed and emerging markets. Gross index returns reflect the reinvestment of income and other earnings, including the maximum possible dividends. Source: MSCI. 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.

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