QUARTERLY COMMENTARY

# Ariel Global Concentrated

• Value • Global

*Quarter Ended June 30, 2022*

The MSCI ACWI Index entered a bear market during the second quarter leading to the worst first half on record since its launch twenty-one years ago. Decades-high inflation, geopolitical conflict, tighter monetary policy, record debt, China's Zero-Covid Policy and concerns over the Eurozone outlook have plagued equities. The market has begun pricing in risks of a recession as it fears a central bank induced hard landing. Although uncertainty is high and volatility will likely remain elevated, we believe our global portfolios will drive strong long-term performance, as they are heavily weighted towards undervalued, higher dividend yielding and better-quality defensive holdings. The Ariel Global Concentrated Composite lost -4.05% lower gross of fees (-4.24% net of fees) in the quarter, outperforming the MSCI ACWI Net Index and the MSCI ACWI Value Index returns of -15.66% and -11.49%, respectively.

Ariel's non-consensus approach seeks to identify undervalued, out-of-favor, franchise-quality companies that are misunderstood and mispriced. The Ariel Global Concentrated strategy continues to be significantly overweight Communication Services, Health Care and Consumer Staples. The portfolio is underweight Consumer Discretionary, Information Technology and Financials and lacks exposure to Industrials, Materials and Energy. At the sector level, stock selection within Communication Services and Health Care were the largest source of positive attribution. By comparison, relative positioning within Energy was the largest detractor from results.

Several stocks in the portfolio delivered strong returns in the quarter. Shares of tobacco maker, **Philip Morris International Inc.** traded higher in the period, despite a volatile regulatory backdrop. Strong quarterly earnings results and management's positive outlook mitigated investor concerns over near-term supply-chain constraints stemming from the Ukraine invasion. Also in the quarter, Philip Morris announced it would acquire smokeless tobacco company Swedish Match. Synergies include an extension of global positioning, distribution infrastructure and broader opportunity set for reduced-risk products. In our view, the favorable economics and margin expansion associated with market share gains from IQOS and Reduced Risk Products highlights value creation opportunities in the years ahead. Furthermore, at current trading levels, we believe the company's operating leverage, pricing power, and improving free cash flow profile offer a strong margin of safety.[1]

China's internet search and online community leader, **Baidu, Inc.** was another top contributor in the quarter. A dovish pivot by the People's Bank of China, signs of a gradual easing of Covid-19 lockdowns and the governments announced increase in infrastructure spending has been a net positive for Chinese shares. Baidu 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 continue to be enthusiastic about Baidu's longer-term opportunity in internet search, online advertising, cloud, artificial intelligence, online video and autonomous driving.

Shares of German mobile telecommunications company, **Telefonica Deutschland Holdings AG** also traded higher in the quarter. The company continues to showcase stable market share, solid average revenue per unit (ARPU), low churn, strong cash generation and a robust dividend yield. Additionally, Telefonica Deutschland's relationships with customer and competitor, Drillisch, a virtual mobile operator, and its parent United Internet have improved since the settlement of their multi-year dispute over payments. Looking ahead, we continue to have high conviction in the stability of Telefonica's recurring subscription revenue model and 5G value creation opportunity.

Although Peruvian banking franchise, **Credicorp, Ltd.** was a top performing contributor in 1Q, it was our largest detractor in 2Q. Despite improving financial results and successful execution across its digital initiatives, investor concerns over the Castillo administration's capacity to address political and economic

[1] Attempting to purchase with a margin of safety on price cannot protect investors from the volatility associated with stocks, incorrect assumptions or estimations on our part, declining fundamentals or external forces.

issues in Peru have begun to create an overhang on shares. We remain focused on Credicorp's attractive long-term earnings potential. The company continues to garner higher customer satisfaction as it strengthens 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. We believe the company has a long runway to increase consumer penetration, particularly as the middle class grows and a greater portion of the economy becomes fully banked.

Enterprise software provider, Microsoft Corporation traded lower as higher interest rates have created headwinds for growth-oriented technology companies. We believe this price action runs counter to Microsoft's solid business fundamentals. The company is driving long-term value creation by capitalizing on a broad and deep set of opportunities, most notably within its hybrid cloud infrastructure via Azure. The platform continues to demonstrate share gains and strong multi-year purchase intent as enterprises transition to cloud based platforms. Despite being a large, widely recognized and long-standing holding in our global strategies, we believe Microsoft's shares remain undervalued.

Lastly, French multinational tire manufacturer, Michelin SCA weighed on relative performance in the period as macro fears across the global automotive industry added to concerns following Russia's invasion of Ukraine which has impacted some distribution and supply chain relationships. These disruptions turned out to be less impactful than anticipated as Michelin was able to expand its raw material relationships with alternate suppliers, replacing synthetic rubber and carbon black previously sourced from Russia. Robust pricing actions to offset rising raw materials costs also proved successful. In our view, the recent price action of shares runs counter to the company's improving fundamental outlook. We remain confident in Michelin's strong competitive position, high levels of normalized profitability and long-term value creation.

Taking advantage of recent market volatility during the quarter, we initiated a position in U.S. telecommunications conglomerate Verizon Communications Inc. At current trading levels we believe the company's attractive dividend yield and free cash flow profile offer a strong margin of safety.[2]

We also exited telecommunications service provider, China Mobile Ltd., to comply with the Biden Administration's executive order on Communist Chinese Military Companies.

Geopolitical tensions, surging inflation, labor shortages and supply chain constraints have left policymakers with a difficult trade-off: Raise interest rates to reign inflation comes at a great cost to economic growth; or keep rates low to preserve growth and live with elevated inflation. The decision by central banks to pivot towards a new regime defined by quantitative tightening (QT) has ignited recessionary fears. However, we do not believe valuations have come down enough to reflect the impact rising rates 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, a repricing of risk across asset classes is yet to come. Against this backdrop, 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. A concentrated portfolio may be subject to greater volatility than a more diversified portfolio. 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

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in equity stocks is risky and subject to the volatility of the markets.

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 6/30/2022, the performance (net of fees) of the Ariel Global Concentrated strategy for the 1-year and since inception on 12/31/2019 was -2.95% and +4.50%, respectively. For the period ended 6/30/22 the performance for the MSCI ACWI Index and the MSCI ACWI Value Index over the 1-year and since inception of the Ariel Global Concentrated strategy on 12/31/2019 was -15.75% and +3.89% and -8.12% and +1.78% respectively. Performance of the Ariel Global Concentrated 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. 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 Concentrated Composite differs from its benchmark, the MSCI ACWI (All Country World Index), because the Composite has dramatically 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 6/30/2022 Philip Morris Intl, Inc. 11.88% of the Ariel Global Concentrated (representative portfolio); Baidu, Inc. 8.94%; Telefonica Deutschland Holding 5.67%; Credicorp Ltd. 3.12%; Microsoft Corp. 12.93%; Michelin SCA 2.46%; Verizon Communications Inc. 1.54% and China Mobile Ltd. 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 Concentrated Composite.

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

Investors cannot invest directly in an index. The MSCI ACWI (All Country World Index) Index is an unmanaged, market weighted index of global developed and emerging markets. The MSCI ACWI Value Index captures large and mid cap securities exhibiting overall value style characteristics across 23 Developed Markets countries and 25 Emerging Markets (EM) countries. Investors cannot invest directly in an index. 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 companies' 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. Source: MSCI.