Ariel Small/Mid Cap Value

Quarter Ended December 31, 2023

Markets worldwide defied expectations in 2023 led by the dominating performance of mega-cap technology stocks known as the "magnificent seven.[1]" Even though gains have been concentrated, improving inflation data and dovish comments from the Federal Reserve drove a fourth quarter rally and strong finish to the year. Investor sentiment has shifted from fears of a recession towards optimism for a soft landing. Such turns in market psychology and economic forecasts continue to highlight the challenges of market timing and the importance of taking a long-term view. Although uncertainty and volatility are likely to remain elevated, the patient investor knows "stock prices trade on fundamentals. And when those solid fundamentals shine through, share prices rise.[2]" Against this backdrop, The Ariel Small/Mid Cap Value Composite advanced +13.78% gross of fees (+13.50% net of fees) in the quarter, relatively in-line with the Russell 2500 Value Index's +13.76% gain and ahead of the +13.35% return posted by the Russell 2500 Index. Over the trailing one-year period, the Ariel Small/Mid Cap Value Composite increased +17.58% gross of fees (+16.42% net of fees), outpacing the Russell 2500 Value Index's +15.98% gain, but falling short of the Russell 2500 Index's +17.42% return.

Global cruise vacation company, **Royal Caribbean Group (RCL)**, advanced on another quarterly earnings beat and subsequent raise in full-year guidance driven by stronger than anticipated consumer demand and solid cost containment. The company continues to experience solid momentum in onboard spend, while 2024 booking trends are significantly ahead of historical ranges at higher pricing. We believe the resiliency of the core cruise consumer in combination with management's superior operational expertise and revised earnings outlook lays the foundation for RCL to exceed its three-year strategic imperative, the *Trifecta Program*.

Alternative asset manager, **Carlyle Group Inc. (CG)**, also increased over the quarter following a solid earnings beat, highlighted by positive investment performance across all its major product lines and continued progress on previously articulated cost savings initiatives. Management also guided to higher transaction and advisory revenues to close out 2023. We believe these results reflect early signs of execution across a number of the strategic initiatives and expect CG will deliver continued growth and margin expansion over time.

Additionally, shares of real estate expert, **Jones Lang LaSalle (JLL)**, traded higher during the quarter on solid earnings results. Despite a slowdown in transaction and leasing activity due to higher long-term interest rates, the Property Management and Work Dynamics businesses delivered strong fee revenues and the business continues to prudently manage expenditures. Additionally, management highlighted a positive revenue outlook for 2024 and reiterated its 2025 financial targets. Despite the recent macro-uncertainty, company leadership is highly confident about the medium- and longer-term revenue outlook for both transactional and recurring revenue streams, alongside its efforts to streamline operations and increase efficiencies to generate higher profit over time.

Alternatively, toy manufacturer, **Mattel, Inc. (MAT)**, traded lower in the period. Despite delivering a significant earnings beat, management maintained full-year guidance signaling a lighter-than-expected holiday outlook to investors. Nonetheless, we continue to expect MAT will gain share, improve profitability and generate higher levels of cash flow in this weaker retail environment. In our view, MAT remains an undervalued company with resilient consumer demand for toys such as Barbie, Hot Wheels and Disney Princesses, as well as an attractive opportunity for future film and TV projects.

Live entertainment, media and technology company, **Sphere Entertainment Co. (SPHR)**, also declined during the period. Despite delivering a profitable fourth quarter relative to the loss posted a year ago, the resignation of CFO, Gautam Ranji, in early November and the rejection of the company's application for a venue in London weighed on investor enthusiasm. Nonetheless, management remains confident

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[1] The "Magnificent Seven" are the largest stocks in the S&P 500 Index driving market performance: Apple Inc. (AAPL), Amazon.com, Inc. (AMZN), Alphabet Inc. (GOOGL), Meta Platforms Inc. (META), Microsoft Corp. (MSFT), NVIDIA Corp. (NVDA) and Tesla, Inc. (TSLA).

[2] Hobson, Mellody and John W. Rogers Jr. "What the Stock market Taught Us This Year: Don't Fall for These Investing Traps." *Wall Street Journal*, 5 December 2023. https://www.wsj.com/finance/investing/stock-market-2023-lessons-investing-2cedd44f

SPHR is well positioned going forward, noting it continues to have substantive conversations in other international markets. While the Sphere venue will take some time to reach its full potential, the company is planning to have events 365 days a year. In addition to hosting concert residencies, marquee sporting and corporate events, The Sphere Experience debuted in October, and consists of a series of exhibits chronicling technology's impact on the development of human potential. Management also believes there is a significant opportunity for advertising and sponsorship on the Exosphere (the Sphere's exterior) as well as licensing interior VIP hospitality suites. Meanwhile, U2 opened to great fanfare on September 29th – causing SPHR to schedule more shows of the Irish rock band in 2024. In our view, the Sphere's new experiential immersive venue and the company's two regional sports and entertainment networks present a long-term opportunity, which remains meaningfully underappreciated at current trading levels.

Finally, live entertainment business, **Madison Square Garden Entertainment Corp. (MSGE)**, traded lower in the quarter following an earnings miss. Revenue declined year-over-year due to fewer concerts versus the prior year period which benefitted from ~30 rescheduled performances due to COVID. Excluding the rescheduled shows, the number of events were up mid-teens and revenue per concert continued to increase. As a result of strong demand, the Christmas Spectacular added additional shows and given strong visibility into the event pipeline, management reiterated fiscal full year 2024 guidance. With marquee assets such as New York's Madison Square Garden, Radio City Music Hall, Beacon Theatre and The Chicago Theater, we believe MSGE is well positioned to capitalize on strong live entertainment demand. In our view, MSGE's assets are stable cash flow generators and should enable deleveraging. At current valuation levels, the company is trading at a significant discount to our estimate of private market value.

We did not initiate or exit any positions in the quarter.

As the pendulum of worry swings from one scenario to another, our focus on recent headlines and macroeconomic developments is to consider their effect on the long-term intrinsic worth of our holdings over the next five-to-ten years. As rates begin to subside in 2024 and beyond, we believe the gap between mega-cap stocks and their small to mid-cap counterparts will begin to narrow, fortified by consumer confidence, wages that are not likely to go down, as well as slowing, yet steady long-term economic growth. Despite the continued concentration of the U.S. equity market, our 41 years of patient investing spanning five market cycles–the crash of 1987, the dot-com era, the global financial crisis, the U.S. debt downgrade and the Covid plunge–have taught us the fundamental principles of investing are resilient. We believe the disciplined investor that stays the course and consistently owns differentiated, quality business models with robust balance sheets will outperform in the long run.

Investing in small-cap and mid-cap stocks is more risky and volatile than investing in large-cap stocks. 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 12/31/23 the performance (net of fees) for the Ariel Small/Mid Cap Value Composite for the 1-, 5-, and 10-year periods was +16.42%, +11.32%, and +7.69%, respectively. For the period ended 12/31/23 the performance for the Russell 2500 Value Index and the Russell 2500 Index for the 1-, 5-, and 10-year periods was +15.98% +10.79%, and +7.42%, and +17.42%, +11.67%, and +8.36%, 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 Small/Mid Cap Value Composite differs from its primary benchmark in that it has fewer holdings and more concentration in fewer sectors.

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. There is no guarantee that any of the views expressed will come to fruition or any investment will perform as described.

As of 12/31/23, Royal Caribbean Cruises, Ltd. constituted 4.5% of the Ariel Small/Mid Cap Value Composite (representative portfolio); Carlyle Group, Inc. 4.6%; Jones Lang LaSalle, Inc. 3.6%; Mattel, Inc. 3.3%; Sphere Entertainment Company 3.0%; and Madison Square Garden Entertainment Corporation 3.1%. 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 Small/Mid Cap 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 2500™ Value Index measures the performance of the small to mid-cap value segment of the U.S. equity universe. It includes those Russell 2500 companies with relatively lower price-to-book ratios, lower forecasted growth values and lower sales per share historical growth. Its inception date is July 1, 1995. The Russell 2500™ Index measures the performance of the small to mid-cap segment of the U.S. equity universe, commonly referred to as "smid" cap. The Russell 2500 Index is a subset of the Russell 3000® Index. It includes approximately 2500 of the smallest securities based on a combination of their market cap and current index membership. Its inception date is June 1, 1990. 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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SLOW AND STEADY WINS THE RACE