Ariel International DM, DM/EM, Global and Global Concentrated

As of December 31, 2022

Rupal J. Bhansali
Chief Investment Officer
International & Global
Equities

Performance (%)

			Annualized			
	QTD	1-Year	3-Year	5-Year	10-Year	Since Inception
Ariel International (DM)						12/31/2011
Gross of Fees	**13.93**	**-10.69**	**0.58**	**1.29**	**5.23**	**5.39**
Net of Fees	**13.70**	**-11.40**	**-0.22**	**0.49**	**4.38**	**4.53**
MSCI EAFE Net Index	17.34	-14.45	0.87	1.54	4.67	5.76
MSCI EAFE Value Net Index	19.64	-5.58	0.65	0.17	3.51	4.72
Ariel International (DM/EM)						12/31/2011
Gross of Fees	**13.13**	**-7.54**	**1.81**	**1.95**	**5.88**	**5.96**
Net of Fees	**12.90**	**-8.28**	**1.01**	**1.14**	**5.01**	**5.08**
MSCI ACWI ex-US Net Index	14.28	-16.00	0.07	0.88	3.80	4.92
MSCI ACWI ex-US Value Net Index	15.70	-8.59	0.06	-0.05	2.72	3.94
Ariel Global						12/31/2011
Gross of Fees	**10.72**	**-4.48**	**5.53**	**5.66**	**8.91**	**8.91**
Net of Fees	**10.50**	**-5.24**	**4.69**	**4.82**	**8.03**	**8.01**
MSCI ACWI Net Index	9.76	-18.36	4.00	5.23	7.98	8.69
MSCI ACWI Value Net Index	14.21	-7.55	3.30	3.47	6.42	7.22
Ariel Global Concentrated						12/31/2019
Gross of Fees	**10.22**	**-5.53**	**3.80**	**–**	**–**	**3.80**
Net of Fees	**10.00**	**-6.28**	**2.97**	**–**	**–**	**2.97**
MSCI ACWI Net Index	9.76	-18.36	4.00	–	–	4.00
MSCI ACWI Value Net Index	14.21	-7.55	3.30	–	–	3.30

2022 Year End Review

2022 was a wake-up call for the global economy. Major declines across the S&P 500 and MSCI Indices forced investors to wrestle with the long-term consequences of an overvalued and overleveraged stock market. Despite a difficult and downbeat macroenvironment marked by unexpected war and inflation, our international and global portfolios delivered capital preservation and relative outperformance. Looking ahead, we feel confident in our 2023 positioning. We continue to steer clear of what we call the four Ls: companies with losses, excess leverage, lofty valuations, and liquidity risk.

For the year ending December 31, 2022, Ariel's International DM and DM/EM Composites declined -10.69% gross of fees (-11.40% net of fees) and -7.54% gross of fees (-8.28% net of fees) respectively, insulating against the MSCI EAFE Index, which fell -14.45%, and the MSCI ACWI ex-US Index, which dropped -16.00%. Similarly, our global portfolios outperformed the MSCI ACWI Index's -18.36% loss. The Ariel Global Composite returned -4.48% gross of fees (-5.24% net of fees) and the Ariel Global Concentrated Composite decreased -5.53% gross of fees (-6.28% net of fees).

Our Contributors and Detractors

Our top contributors in 2022 came from different sectors and geographies. Our Communications and Consumer Staples names were strong. Likewise, we benefited from stock selection amongst our Financial, Consumer Discretionary and Technology companies. More specifically, in Communications, **China Mobile** rebounded in the first half of 2022 before we were required to exit the position, as overvalued growth stocks sold off and our value names advanced. In Consumer Staples, **Phillip Morris** stood out as demand for less harmful, next-generation smoke-free products continued to gain acceptance. Financial holding, **BB Seguridade**, outperformed despite an uncertain political backdrop in Brazil. The company consistently delivered strong operational and financial results and we continue to believe it is in the early innings of a long-term growth story driven by the wealth and savings of a burgeoning middle class. Across our global strategies, **Gilead Sciences Inc.** was boosted by incremental success in its HIV and oncology initiatives.

Our weakest names were impacted by short-term dislocations. The Russia-Ukraine war's supply chain disruptions hurt the automobile industry and therefore negatively affected French tire manufacturer **Michelin's** performance. However, we believe Michelin's strong global competitive positioning will drive long-term value. Internet search and online community leader of China, **Baidu, Inc.,** fell alongside the broader sell-off in Chinese equities as the markets reacted to Xi Jinping's concentration of power at the 20th National Congress Party meeting in October. Despite these developments, we remain enthusiastic about the potential growth and expansion opportunities across cloud, autonomous driving, artificial intelligence, and online video.

Finally, **Direct Line Insurance Group** underperformed as claims inflation in the United Kingdom (UK) hurt the company's profit margins, causing it to subsequently report an unexpected profit warning. The announcement was driven by higher claims within the home insurance business due to unusual, below-freezing temperatures in the UK throughout December. As a result of these trends, solvency ratios are at the lower end of management's desired range, causing the company to cancel their final dividend for 2022. While we expect these adverse factors to normalize if not reverse over the course of 2023, a recovery in earnings will likely be more back-end loaded than we anticipated. Although we are disappointed with these developments, we continue to hold the shares as we believe the stock is materially undervalued relative to its normalized earnings power. While 2022 presented challenges across several sectors, we stayed true to our knitting and focused on our research and business fundamentals.

Our underweight in Technology was a proof point last year. Higher interest rates disproportionally hit tech companies, specifically the FAANG stocks. **Meta Platforms, Inc** (Facebook)**, Apple Inc., Amazon.com Inc., Netflix, Inc,** and **Alphabet Inc.** (Google) all posted double-digit declines in 2022.[1] Meta was among the worst of the group with its stock plummeting 65%. Meanwhile, Amazon and Netflix followed, declining -64% and -51% respectively.[2] Recessionary fears led to pullbacks in advertiser spending, negatively impacting the revenue of the tech giants with advertising-led business models. Overall, the tech industry lost over $7 trillion in market cap in 2022.[3] We anticipate more layoffs, valuation dips and, assuming a recession in 2023, lower earnings.

Although **Microsoft Corporation** was our top detractor in our global portfolios, we believe the stock is an outlier. Unlike the growthier names with ad-driven business models, it is an enterprise platform technology company with solid fundamentals and a distinct long-term outlook. The value proposition for its hybrid cloud infrastructure Azure has yet to materialize and will have a multi-year impact as more Fortune 500 corporations transition to the cloud. Our research shows a significant upside in the price.

[1] Gunjan Banerji and David Maraino-Nachison, "For Divng FAANG Stocks, It's the End of an Era," *The Wall Street Journal,* October 27, 2022, Accessed January 14, 2023, https://www.wsj.com/livecoverage/stock-market-news-today-10-27-2022-us-economy-gdp-q3/card/faang-stocks-fall-V1mVeZ2CrRFp6JXVvKpF.
[2] "FAANG in 2023: How have shares performed and what to expect?" INDMoney.com, Last modified January 18, 2023, https://www.indmoney.com/articles/us-stocks/faang-in-2023-how-have-shares-performed-and-what-to-expect.
[3] Rohan Goswani, "Tech's reality check: How the industry lost $7.4 trillion in one year," CNBC.com, Last modified November 25, 2022, https://www.cnbc.com/2022/11/25/techs-reality-check-how-the-industry-lost-7point4-trillion-in-one-year.html.

There is Nothing New Under the Sun

Last year, the international and global equity landscape presented dynamics similar to what we have witnessed over decades of investing. With inflation at levels not seen since the early 1980s, eradicating current inflationary issues under Jerome Powell may be as painful and extended as it was under Former Federal Reserve Chair Paul Volcker. Likewise, US valuation bubbles in 1999 and 2007 resemble the valuation multiples of 2020 and 2021. In early 2022, growth stock valuations reached frothy levels. The MSCI World Growth Index traded at 31 times expected earnings, compared to only 14 times expected earnings for the MSCI World Value Index. By year-end, valuations had fallen to 21 and 12 times, respectively.[4] Finally, one could draw parallels to the overly stimulative monetary policies in 1999, 2007, and today. The major difference is the excessive speculation in technology and internet-based companies (FAANGs), meme stocks, cryptocurrencies, and SPACs, rather than traditional assets such as real estate.

2023 Outlook: Defense is the Best Offense

Looking to 2023, managing risk will be as important as managing returns. Quantitative Tightening[5] (QT) may drive a deeper dagger into the heart of the cyclical excesses of the last two years to annihilate high inflation rates globally. In our view, as earnings fall and multiples compress, investors should focus on capital preservation rather than appreciation. This means avoiding long-duration assets such as growth stocks and favoring short-duration value companies with compelling dividend yields. We believe 2023 will be another resilient year for our international and global portfolios as our bottom-up investment process seeks to eliminate risky businesses (as categorized by the four Ls) and embrace quality names. While we are bearish on the broader market, we are bullish on active management. We believe the next few years are likely to be very beneficial for stock pickers as market sell-offs hurt passive but create opportunities for patient, active investors.

We appreciate the opportunity to serve you and welcome any questions you might have.

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 portfolios invest may never be recognized by the broader market. The portfolios are often concentrated in fewer sectors than their benchmarks, and their 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 net of transaction costs and reflect the reinvestment of dividends and other earnings. Net performance of each Composite has been reduced by the amount of the highest fee charged to any client in each 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 International (DM) Composite differs from its benchmark, the MSCI EAFE Index, because: (i) the Composite has fewer holdings than the benchmark, (ii) the Composite will invest in Canada, and (iii) the Composite will at times invest a portion of its assets in the U.S. and emerging markets. The Ariel International (DM/EM) Composite differs from its benchmark, the MSCI ACWI (All Country World Index) ex-US, because: (i) the Composite has fewer holdings than the benchmark and (ii) the Composite will at times invest a portion of its assets in the U.S. 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 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.

[4] Mike Bell, "Markets Review," JP Morgan Asset Management, January 3, 2022, https://am.jpmorgan.com/content/dam/jpm-am-aem/global/en/insights/market-insights/mi-monthly-market-review.pdf.
[5] Quantitative Tightening refers to policies that reduce the size of the Fed's balance sheet. Source: Federal Reserve Bank of St. Louis

As of 12/31/22, the Ariel International (DM) Composite (representative portfolio) held the following positions referenced: Phillip Morris International 6.79%; Michelin (CGDE) 5.52%; Direct Line Insurance Group plc 4.10%; Baidu, Inc. ADR 3.88% and BB Seguridade Participacoes SA 0.26%. As of 12/31/22, the Ariel International (DM/EM) Composite (representative portfolio) held the following positions referenced: Phillip Morris International 6.98%; Michelin (CGDE) 5.56%; Baidu Inc. ADR 5.46%; Direct Line Insurance Group plc 3.03% and BB Seguridade Participacoes SA 2.65%. As of 12/31/22, the Ariel Global Composite (representative portfolio) held the following positions referenced: Microsoft Corporation 8.00%; Phillip Morris International, Inc. 6.08%; Baidu, Inc. ADR 5.22%; Michelin (CGDE) 3.81%; Gilead Sciences, Inc. 3.51%; BB Seguridade Participacoes SA 2.10% and Direct Line Insurance Group plc 2.08%. As of 12/31/22, the Ariel Global Concentrated Composite (representative portfolio) held the following positions referenced: Microsoft Corporation 12.21%; Phillip Morris International, Inc. 9.91%; Baidu, Inc. ADR 7.70%; BB Seguridade Participacoes SA ADR 3.88%; Gilead Sciences, Inc. 3.44%; Michelin (CGDE) 3.35% and Direct Line Insurance Group plc 2.72%. 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 Composites. Portfolio holdings mentioned do not represent all holdings purchased or sold for the Composites.

Investors cannot invest directly in an index. The MSCI EAFE® Index is an equity index of large and mid-cap representation across 21 Developed Markets (DM) countries around the world, excluding the U.S. and Canada. Its inception date is May 31, 1986. The MSCI EAFE Value Index captures large and mid-cap securities exhibiting overall value style characteristics across Developed Markets countries around the world, excluding the US and Canada. Its inception date is December 8, 1997. The MSCI ACWI (All Country World Index) ex-US Index is an index of large and mid-cap representation across 22 Developed Markets (DM) and 24 Emerging Markets (EM) countries. Its inception date is January 1, 2001. The MSCI ACWI ex-US Value Index captures large and mid-cap securities exhibiting overall value style characteristics across 22 Developed and 24 Emerging Markets countries. Its inception date is December 8, 1997. The MSCI ACWI Growth Index captures large and mid cap securities exhibiting overall growth style characteristics across 23 Developed Markets (DM) countries and 25 Emerging Markets (EM) countries. Its inception date is December 8, 1997. 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 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.