Ariel Emerging Markets Value and Emerging Markets Value ex-China

As of June 30, 2023

Henry Mallari-D'Auria
Chief Investment Officer
Emerging Markets

Performance (%)

	QTD	YTD	1-Year	3-Year (Annualized)	5-Year (Annualized)	10-Year (Annualized)	Since Inception (Annualized)
Ariel Emerging Markets Value							04/30/2023
Gross of Fees	-	-	-	-	-	-	**4.32**
Net of Fees	-	-	-	-	-	-	**4.15**
MSCI EM Net Index	-	-	-	-	-	-	2.05
Additional Indexes							
MSCI EM Value Net Index	-	-	-	-	-	-	2.11
Ariel Emerging Markets Value Ex-China							05/31/2023
Gross of Fees	-	-	-	-	-	-	**6.05**
Net of Fees	-	-	-	-	-	-	**5.95**
MSCI EM ex-China Net Index	-	-	-	-	-	-	3.72

Emerging Markets Equities—Seizing the Opportunity

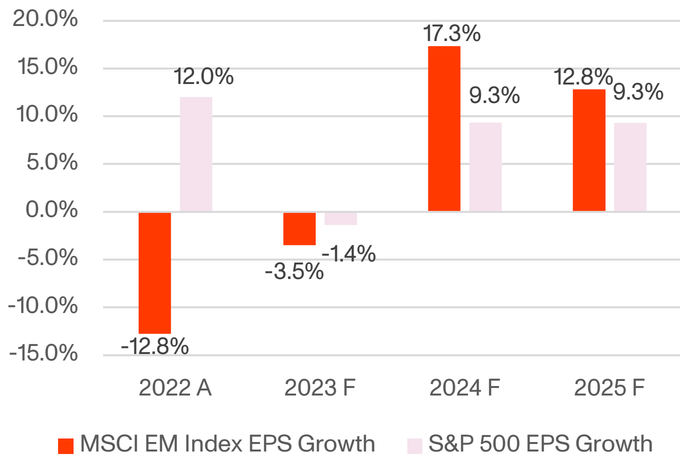
In all the time I have been investing—32 years and counting—I have never seen today's combination of attractive valuations and forecasted earnings growth in emerging markets (EM). When the market has previously come close to where it is now, our investable universe had a lot more leverage than today's environment. While large valuation gaps might leave some sitting on the sidelines—in our view, investing in emerging markets currently presents a rare opportunity.

Considering China

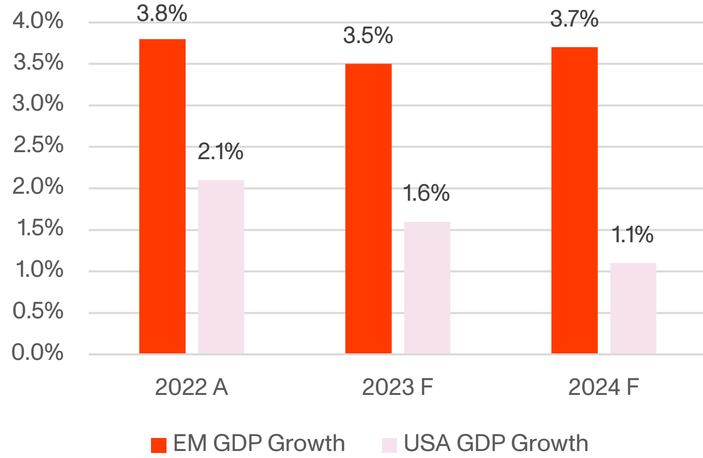
As bottom-up stock pickers, we consider events in EM and developed markets (DM) when building our portfolios. Since China is the largest EM economy and second in the world, the outlook for GDP growth must be considered. While economic forecasts do not determine our investment success, we believe the question is *when* rather than *if* Chinese growth accelerates from here. We believe consumption is currently depressed because confidence needs a boost, not because consumers lack the wherewithal to spend. Over the next 12-24 months, we expect Chinese consumers will begin to drive economic growth while U.S. and European authorities continue to tighten.

The chart below showcases how developing economies have an economic growth premium over advanced markets, which has led us to expect EM corporate earnings growth to exceed the outlook for DM over the next two years. This is being driven by both cyclical and structural factors. In our view, EM is positioned to outperform DM in the future.

Forward EPS Growth Is Higher in EM vs DM[1]



GDP Growth Rates[2]



As we look at the rest of Asia, particularly the Association of Southeast Asian Nations (ASEAN), there are even more opportunities. The region should benefit from increased Chinese demand and countries such as the Philippines and Vietnam will likely grow even faster as the world shifts supply chains away from China. In the case of the Philippines, some of our holdings currently sell well below their pre-COVID prices even though economic activity has returned to 2019 levels. And although we believe India is expected to be a beneficiary of supply chain diversification, its stock valuations appear too rich to offer many opportunities today.

Inflation Insights

We believe EM inflation is likely to be less sticky, which should provide policymakers greater flexibility than in the U.S. EM labor markets are not as tight because these countries lifted their COVID lockdowns later than DM countries. Much more of the EM inflation basket is food and energy where the worst appears to be over. Outside of Asia, our largest country position is Brazil where inflation is elevated, but authorities acted earlier than the U.S. and interest rates are already falling. Meanwhile, lingering U.S. inflation could lead to a weaker U.S. dollar versus other currencies, including EM, as higher costs would make American products less competitive and boost U.S. consumer appetite for more attractively priced imports.

Dedicated EM Exposure and Potential for Outperformance

In our opinion, while EM beta looks attractive, the EM alpha opportunity is substantial. Foreign direct investment over the last few years have focused on a few EM names, leaving wide dispersion within the universe. Active managers thrived during the first six months of 2023—with the median manager outperforming the MSCI EM Net Index by +2.42% and managers in the top quartile ahead of the benchmark by at least +4.36%. [3]

Off to the Races!

In our first two months at Ariel, market dispersion was wide—Brazilian equities were propelled by falling interest rates while a tech rally has been driven by investor enthusiasm for artificial intelligence (AI). Meanwhile, Chinese shares lagged against the backdrop of a lackluster recovery.

In Brazil, our holdings are primarily anchored in turnaround situations in health care, food distribution and utilities as well as long-term growth opportunities in financials. Our names are already benefitting from an expected decline in the country's high real interest rate environment.

[1]Source: Bloomberg, Ariel Investments
Earnings per Share Growth is used to determine the rate at which a company is growing its profitability. It is measured as a percentage change over a given period. The MSCI Emerging Markets Index captures large and mid cap representation across 24 Emerging Markets (EM) countries. With 1,377 constituents, the index coves approximately 85% of the free float-adjusted market capitalization in each country. Inception of this benchmark was December 29, 2001. An investor cannot invest directly in an index. 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.

[2]Based on projections from International Monetary Fund World Economic Outlook, April 2023. EM growth rate calculated using MSCI Emerging Markets Index weights as of May 2023 as provided by Bloomberg.

[3] Source: Morningstar Universe: Morningstar Diversified Emerging Mkts.

Although not key to our investment thesis, AI does offer an additional growth driver for many IT companies and our stocks outperformed as investor interest in this trend grew. Our investment in SK Hynix is based on our belief that industry supply side control would enable dynamic random-access memory (DRAM) prices to rise even if demand only grows modestly from today's depressed levels. Similarly, King Yuan's semiconductor testing business will benefit if AI leads to more processing needs, but it is also still attractive on much lower growth expectations.

However, the fading economic recovery in China and weakened demand for exports has caused the MSCI EM Index to fall short of the returns generated by DM. Since our Ariel inception just two months ago, our own Chinese holdings traded in line with Chinese securities held in the benchmark. With long-term earnings power intact and prices down on near-term concerns, we will be rebalancing toward high conviction Chinese opportunities.

Despite the outperformance, Ariel's emerging markets value and emerging markets value ex-China portfolios are still priced at only 7x forward earnings and 1x book value and 8x forward earnings and 1x book value, respectively. When combined with accelerating earnings growth, this is the most excited I have been about EM investing in decades. We believe a 50% rise would still leave valuations at reasonable levels given expected profitability, growth and balance sheet leverage.

Portfolio Characteristics (06/30/2023)[4]	PE (fwd)	P/B	Div Yield	ROE
Ariel Emerging Markets Value	**7.43**	**1.01**	**3.43**	**14.78**
Ariel Emerging Markets ex-China	**8.72**	**1.16**	**3.25**	**18.15**
MSCI EM Net Index	11.71	1.76	3.22	17.51
MSCI EM ex-China Net Index	12.99	1.76	3.51	20.10

In summary, we believe this is one of the best times to invest in emerging markets in recent history given the attractiveness of existing equity valuations. Slow EPS growth was a contributing factor to EM equity underperformance over the last decade, but these regions are now reaping the benefits of falling inflation ahead of the developed world as they quickly responded to inflationary risks with rate hikes in 2021. Geopolitical fragmentation, demographic trends underscored by a burgeoning middle class as well as urbanization are also supportive of these long-term tailwinds. Tensions between the U.S. and China have driven an increase in foreign direct investment in EM countries, as businesses nearshore operations to realign their global supply chains. Meanwhile, investors remain underweight the asset class. Looking ahead, our experienced and seasoned investment team believes there are greater inefficiencies in emerging markets, presenting a compelling opportunity to deliver meaningful excess returns.

[4] Source: FactSet

Forward Price/Earnings Ratio is a valuation measure that represents the price divided by the mean earnings per share (EPS) consensus estimate for the next twelve months as of the run date. Holdings are summarized at the portfolio level using weighted harmonic average and exclude negative earnings.

Price to Book is a valuation measure that represents the price divided by the book value per share. Holdings are summarized at the portfolio level using weighted harmonic average.

Dividend Yield is the aggregate weighted average of the strategy's equity holdings and their respective dividend yield. Dividend Yield shown does not represent any actual yield of the strategy, does not in any way represent the strategy's total return, and does not reflect the deduction of strategy expenses.

Return on Equity is a profitability measure that represents return on average total equity for the period. Holdings are summarized at the portfolio level using weighted average.

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.

This document may contain forward-looking statements relating to the objectives, opportunities, and the future performance of the markets generally. Forward looking statements may be identified by the use of such words as: "believe," "expect," "anticipate," "should," "planned," "estimated," "potential" and other similar terms. Forward-looking statements are subject to various factors, including, but not limited to general and local economic conditions, changing levels of competition within certain industries and markets, changes in interest rates, changes in legislation or regulation, and other economic, competitive, governmental, regulatory and technological factors affecting a portfolio's operations that could cause actual results to differ materially from projected results. Such statements are forward-looking in nature and involve a number of known and unknown risks, uncertainties and other factors, and accordingly, actual results may differ materially from those reflected or contemplated in such forward-looking statements. None of Ariel Investments or any of its affiliates or principals nor any other individual or entity assumes any obligation to update any forward-looking statements as a result of new information, subsequent events or any other circumstances. All statements made herein speak only as of the date that they were made.

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. Returns are expressed in U.S. dollars. Current performance may be lower or higher than the performance data quoted.

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.

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 Emerging Markets Index captures large and mid cap representation across 24 Emerging Markets (EM) countries. With 1,377 constituents, the index covers approximately 85% of the free float-adjusted market capitalization in each country. Inception of this benchmark was December 29, 2001. The MSCI Ariel Emerging Markets Value Index captures large and mid cap securities exhibiting overall value style characteristics across 24 Emerging Markets (EM) countries. The value investment style characteristics for index construction are defined using three variables: book value to price, 12-month forward earnings to price and dividend yield. Inception of this benchmark was January 08, 1997. MSCI Emerging Markets ex-China Index captures large and mid cap representation across 23 of the 24 Emerging Markets (EM) countries excluding China. Its inception date is March 9, 2017.

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.