Ariel investments

Quarterly Commentary

Ariel Global Concentrated

Quarter Ended March 31, 2024

Developed markets continued their upward trajectory in the first quarter. Investor enthusiasm around artificial intelligence (AI), a recovery in bank lending growth, lower energy costs, a pick-up in global manufacturing activity, recent structural reforms in Japan and the near-term prospect of a rate-cutting cycle in both the U.S. and Europe drove a broad-based rally. While growth bested value and large cap issues outperformed their small cap brethren, all sectors in the MSCI ACWI Index, except real estate, logged gains. Fears of a recession have been replaced with optimism and bullish market sentiment. Such turns in market psychology and economic forecasts highlight the challenges of market timing and the importance of taking a long-term view. Although exuberance, particularly for AI-themed mega-cap stocks may eventually prove to be excessive, the patient investor knows stock prices trade on fundamentals. Meanwhile, we continue to improve our upside capture across our international and global portfolios while remaining laser focused on preserving downside protection. Against this backdrop, the Ariel Global Concentrated Composite advanced +8.48% gross of fees (+8.26% net of fees) in the period, mostly in line with the +8.20% gain of the MSCI ACWI Index but outperforming the +6.85% return of the MSCI ACWI Value Index.

Ariel's non-consensus approach seeks to identify undervalued, out-of-favor, franchises that are misunderstood and therefore mispriced. The Ariel Global Concentrated bottom-up strategy is overweight Health Care, Consumer Discretionary, Communication Services and Information Technology. The portfolio is underweight Industrials and Consumer Staples, as well as lacks exposure to Energy and Materials. At the sector level, our Consumer Discretionary and Industrial holdings were the greatest sources of positive attribution, while our investment choices within Communication Services and Information Technology were the largest performance detractors in the quarter.

Leading provider of dialysis services, **DaVita, Inc.** outperformed during the period following a top- and bottom-line earnings beat. DaVita is benefitting from cost saving initiatives, early signs of a normalization in patient growth trends on par with pre-pandemic levels, improved leverage and an aggressive share buyback program. The company also recently announced an expansion of its international operations in Latin America, presenting an attractive long-term growth opportunity. Furthermore, management provided a 2024 financial outlook which is well above consensus and anticipates favorable growth. In our view, we believe the market misunderstands the long-term clinical impact of glucagon-like-peptide-1 (GLP-1s) on dialysis and as such, DaVita currently trades at a significant discount relative to our estimate of its intrinsic value.

Market leader for computer storage systems, **NetApp Inc.** also advanced in the quarter due to a top- and bottom-line earnings beat and subsequent raise in guidance. These strong results were supported by increased adoption of quad-level cell (QLC) NAND flash memory products, cost reduction initiatives and margin expansion. Longer term, we continue to believe NetApp is well-positioned to benefit from its cloud storage service as it helps companies move data between public and private clouds seamlessly. Meanwhile, the company remains focused on digital transformation projects involving business analytics, AI and data security.

Additionally, new position, German-based automotive manufacturing company, **Daimler Truck Holding AG (DTG)**, advanced in the quarter. The market's pessimism on the overall magnitude of the industry's cyclical downturn provided us with an attractive entry point in the stock and then DTG delivered a significant earnings beat, highlighted by record margins at Mercedes-Benz, robust free cash flow generation as well as a favorable volume and margin outlook for 2024. In our view, Daimler is the highest quality truck original equipment manufacturer in the industry and we expect it to narrow the multiple gap versus competitor PACCAR. We believe the company's self-help efforts will result in higher margins throughout the cycle, improving Daimler's profitability over the medium term.

There were a few notable performance detractors in the quarter. China's internet search and online community leader, **Baidu, Inc.** traded lower alongside Chinese equities as intensifying problems in China weighed on investor sentiment during the period. The company continues to invest heavily in Artificial Intelligence (AI) and recently launched its generative AI, Ernie Bot, aimed at rivaling Open AI's ChatGPT. While monetization of the new technology is largely dependent on regulatory review, we think Baidu should continue to experience margin improvement with the ongoing implementation of efficiency and profitability initiatives. While some investors remain on the sidelines due to uncertainty surrounding China's economic growth, government regulations, and the political rhetoric towards Taiwan, we remain enthusiastic about Baidu's longer-term opportunity for revenue growth and margin expansion across

internet search, cloud, autonomous driving, artificial intelligence and online video.

One of the world's largest semiconductor chip manufacturers by revenue, **Intel Corporation**, also underperformed in the period as management provided a disappointing near-term outlook due to ongoing weakness and inventory right-sizing in non-core products. Nonetheless, Intel delivered solid quarterly earnings results, highlighted by a top-line beat driven by upside from the cyclical recovery of personal computers (PCs) and central processing units (CPUs). In our view, the market is overlooking the progress Intel is making to advance its manufacturing process and regain its technology advantage to compete as a top industry supplier. We believe the separation of the design and manufacturing businesses will be a key catalyst in unlocking improved financial performance while also enhancing the competitiveness of the foundry business.

Finally, tobacco maker, **Philip Morris International Inc. (PM)**, declined in the quarter on an earnings miss and disappointing outlook for full year 2024. The underlying growth of heated tobacco products and the IQOS brand is slowing due to an uptick in vaping. Taken together with lower pricing in combustibles, a $2 billion headwind from the menthol ban in the European Union and lack of growth in Russia, we decided to take profits on the overall performance of Philip Morris across our holding period and exited the position to pursue more compelling opportunities.

We initiated eleven new positions in the quarter.

We added **Aptiv PLC (APTV)** which designs and manufactures vehicle components and provides electrical/electronic and active safety technology solutions to the global automotive and commercial vehicle markets. We believe the secular trend of electrification and digitization within the automobile industry, coupled with the expansion of Chinese original equipment manufacturers (OEMs), will accelerate demand and drive long-term growth. Additionally, we anticipate APTV will grow earnings per share over the near-term through its divesture of the autonomous driving joint venture, Motional. In our view, the name is currently trading at a significant discount relative to our estimate of intrinsic value.

We purchased Japanese video game publisher, **Bandai Namco Holdings, Inc.** While anime has been highly popular in Japan, Netflix's recent streaming of anime content has expanded its popularity to markets overseas. Bandai is capitalizing on the strong growing demand for the genre through toy and video game sales, a global movie deal as well as the expansion of licensing its intellectual property across merchandise, trading cards and amusement arcades. In our view, the market is currently underappreciating Bandai's diversified growth potential. We see upside in the company's toys and hobby unit and forecast solid free cash flow generation in the years ahead.

We found an attractive entry point for London based, agriculture machinery manufacturer, **CNH Industrial NV (CNHI)**, as shares are currently pricing in multi-year declines similar to the slope of the last agricultural downcycle that ran from 2014 to 2016. Although farm incomes have begun to moderate and will likely translate to lower machinery purchasing this year, our analysis of U.S. farm fundamentals suggests the severity and longevity of the next downcycle will likely be shallower and shorter in duration. Additionally, CNHI remains on track to deliver on previously articulated operational efficiency and cost savings targets, which should drive margin improvement and profitability growth over the near- to medium-term. Looking ahead, we believe the industry will benefit from farming management strategies, such as precision agriculture which seeks to improve agricultural production sustainability.

We bought American healthcare company, **CVS Health Corporation (CVS)**, following recent concerns related to potential new laws affecting Pharmacy Benefit Managers (PBMs)—intermediaries that negotiate drug prices between insurers and pharmacies—and issues with pricing in its Medicare Advantage plans, a type of health insurance for senior citizens. Shares presented an attractive entry point after the company lowered its 2024 outlook. While investor apprehension regarding the new laws appears to have eased, utilization of Medicare Advantage plans is also stabilizing. Our purchase of CVS reflects our efforts to capitalize on temporary setbacks and secure positions in companies poised for a rebound.

We initiated a position in global financial services company, **Capital One Financial Corporation (COF)**. The company is the largest online consumer and commercial bank with a leading position in general purpose and small business credit cards. We view the company as competitively advantaged particularly due to their investment in technology. According to recent reports, COF is also rated as one of the leading banks within Artificial Intelligence (AI). Notably, the company recently announced an acquisition of Discover Financial Services (DFS) which we believe would produce significant long-term earnings accretion. COF will be able to leverage DFS' proprietary payments network, enabling direct interaction with merchants and consumers. This closed loop dynamic should lead to higher volumes of credit card conversions presenting further upside for its shares. At current levels, we view the long-term outlook to be attractive, given favorable business trends, stabilizing delinquency rates within the credit card industry, synergies from the DFS acquisition and COF's enhanced focus on technology.

We also purchased Danish multinational banking and financial services company, **Danske Bank A/S**. Following several years of litigation concerning money-laundering violations, the company recently finalized a settlement, removing the overhang on shares. Meanwhile, the business is demonstrating

solid operating momentum, highlighted by the strong credit quality of its customer base as well as improving net interest margin and a strong balance sheet. We expect Danske Bank to begin returning capital to shareholders through dividends or buybacks in 2024.

We added China-based technology-driven E-commerce company, **JD.com, Inc**. The brand has long been known across the region as a superior online shopping channel due to its unique first-party model and unparalleled fulfillment service underpinned by JD Logistics. Yet, a challenging macro environment drove shares lower as shoppers began seeking bargains. In response, the company made significant investments in elevating its third-party merchant platform to enhance its variety of product offerings and price competitiveness for consumers. We believe these actions will yield an improved product mix, stronger top-line growth and margin expansion on a go-forward basis.

We initiated a position in leading German multinational technology conglomerate, **Siemens AG**. The company's operations encompass automation for manufacturing and processing, smart infrastructure, energy systems, rail technology, and digital healthcare solutions. Although shares have historically been undervalued due to concerns over the complexity of its disparate portfolio of businesses across sectors, we have identified several factors conducive to a potential re-rating. Over the last five years, Siemens has simplified its portfolio into high-quality businesses benefitting from secular growth themes such as energy transition, digitalization and industrial automation. Additionally, the new, shareholder-friendly management team is focused on enhancing free cash flow generation and improving capital allocation, which we view as a key catalyst benefitting the stock longer-term.

We bought multinational automotive manufacturing company, **Stellantis N.V. (STLA)**, which was formed from the merger of Fiat Chrysler Automobiles and the French PSA Group in the period. With deal synergies lowering overall operating expenses and contributing to healthy free cash flow generation, management has begun increasing shareholder returns through dividends and share buybacks. Although some investors remain on the sidelines over concerns auto sales and margins have peaked, STLA's average transaction price is growing year-over-year. We think this momentum will continue and expect STLA to deliver double-digit operating profit margin as it further expands its leading position in the Middle East and South America. Furthermore, the company's Leapmotor joint venture presents a unique way to benefit from the strengths of Chinese original equipment manufacturers. Meanwhile, in the current electric vehicle slowdown environment, we believe STLA is best positioned to weather the storm. Management believes it can maintain profitability and is open to rationalizing its 14 brands. STLA seeks to be number one in the commercial vehicle segment by 2027, which comes with high customer stickiness, solid profitability and recurring revenue streams.

We established a position in Hungarian, ultra-low cost airline provider, **Wizz Air Holdings plc.** An investigation into the Pratt & Whitney (P&W) Geared Turbofan (GTF) engine, which powers the airlines A320NEO family aircrafts, has grounded approximately 22% of the fleet for 18 months presenting us with an attractive entry point. Although this issue will reduce flight capacity over the near to medium-term, WIZZ has agreed to a cash compensation package with P&W. We anticipate the overall impact on earnings will be further mitigated by the delivery of new planes, lease extensions and more optimal fly routes and schedules at better pricing. We also believe WIZZ remains well positioned to execute its expansion strategy across Western Europe and the Middle East. At current levels, WIZZ is trading at a significant discount to our estimate of its intrinsic value as well as peer earnings multiples.

And as mentioned previously, we added German-based automotive manufacturing company, **Daimler Truck Holding AG**.

By comparison, we exited thirteen positions in the quarter.

We exited the following positions on solid performance across our holding period to pursue more compelling opportunities: leading electric utility across Asia, **CLP Holdings Limited**; Peruvian banking franchise, **Credicorp Ltd.**; leading market maker in European derivatives, **Deutsche Boerse AG**; one of the largest banks in Mexico, **Grupo Financiero Banorte S.A.B. de C.V.**; tobacco maker, **Philip Morris International Inc. (PM)**; leading mobile telecommunications company, **Telefónica Brasil SA**, and financial services company, **Truist Financial Corporation**

Lastly, we sold out of Biopharmaceutical company, **Bristol-Myers Squibb Company (BMY)**, British home and auto insurer, **Direct Line Insurance Group Plc**, real estate investment trust, **Equity Commonwealth (EQC)**; leading electric utility in Spain, **Endesa S.A.**; Finnish telecommunications and consumer electronics company, **Nokia Oyj**; and global pharmaceutical and diagnostics leader, **Roche Holding AG** to pursue higher conviction opportunities.

As broad optimism continues to prevail, there are cautious undertones. Although market concentrations have their own peaks and troughs, volatility is near historical lows. The mega-cap technology names—whose elevated valuations continue to highly influence overall market performance—appear vulnerable to a correction. Escalating geopolitical tensions, unpredictable monetary policy, as well as the outcome of the upcoming U.S. Presidential election also pose risks. As the bull market climbs the proverbial "wall of worry," we expect these uncertainties will likely result in a period of heightened volatility and widening dispersion of returns, creating

opportunities for active managers with focused expertise to shine. In our view, higher quality companies with robust balance sheets will be the drivers of future outperformance. Accordingly, we are finding many mispriced stocks where valuation is attractive, profitability less vulnerable and balance sheets remain strong.

Investments in non-U.S. securities may underperform and may be more volatile than comparable U.S. stocks because of the risks involving non-U.S. economies, markets, political systems, regulatory standards, 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 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 3/31/24, the performance (net of fees) of the Ariel Global Concentrated Composite for the 1-year and since inception on 12/31/2019 was +16.89% and +7.47%, respectively. For the period ended 3/31/2024, 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 Composite on 12/31/2019 was +23.22% and +9.79%, and +18.01% and +6.69%, 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 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. There is no guarantee that any of the views expressed will come to fruition or any investment will perform as described.

As of 3/31/2024, DaVita Inc. constituted 4.7% of the Ariel Global Concentrated Composite (representative portfolio); NetApp, Inc. 5.7%; Daimler Truck Holding AG 2.6%; Baidu, Inc. 3.9%; Intel Corporation 3.6%; Philip Morris International Inc. 0.0%; Aptiv PLC 1.0%; Bandai Namco Holdings Inc. 2.5%; CNH Industrial NV 2.5%; CVS Health Corp. 2.8%; Capital One Financial Corp 2.6%; Danske Bank A/S 3.0%; JD.com, Inc. 1.7%; Siemens AG 1.5%; Stellantis NV 3.5%; Wizz Air Holdings Plc 1.4%; Bristol-Myers Squibb Co. 0.0%; CLP Holdings Ltd. 0.0%; Credicorp Ltd. 0.0%; Deutsche Boerse AG 0.0%; Direct Line Insurance Group PLC 0.0%; Endesa SA 0.0%; Equity Commonwealth 0.0%; Grupo Financiero Banorte SAB de CV 0.0%; Nokia Oyj 0.0%; Roche Holding AG 0.0%; Telefonica Brasil SA 0.0%; and Truist Financial Corp 0.0%. 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.

Indexes are unmanaged. An investor cannot invest directly in an index. The MSCI ACWI (All Country World Index) Index is an equity index of large and mid-cap representation across 23 Developed Markets (DM) and 24 Emerging Markets (EM) countries. Its inception date is January 1, 2001. 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.

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