# Ariel Mid Cap Value

## Quarter Ended March 31, 2024

U.S. indices continued to exceed expectations in the first quarter. Investor enthusiasm around artificial intelligence (AI), resilient corporate earnings growth, falling inflation and expectations for interest rate cuts this year drove a broad-based rally. While momentum was the largest driver of performance across size and style, all sectors in the S&P 500, except real estate, posted 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. Against this backdrop, the Ariel Mid Cap Value Composite traded up +4.37% gross of fees (+4.11% net of fees) in the quarter, but trailed both the Russell Midcap Value and Russell Midcap indices, which returned +8.23% and +8.60%, respectively.

Shares of global leader in electrical protection and connection solutions, **nVent Electric plc (NVT)** jumped following strong quarterly earnings results, highlighted by healthy organic revenue growth, margin expansion and robust free cash flow generation. Management also provided a solid full year outlook for 2024, as NVT continues to execute on its global strategy, which is focused on high-growth verticals, new products and innovation. We expect NVT to continue to benefit from secular trends towards increased electrification and data center development, as well as from internal operational improvements.

Financial advisory and asset manager, **Lazard Ltd. (LAZ)** also advanced in the period following solid top- and bottom-line results, highlighted by momentum in the advisory business, improving financing markets and early signs of progress on previously articulated cost-savings initiatives. Near-term, management reiterated its cautiously optimistic long-term guidance for the mergers & acquisitions segment given an improving macroeconomic outlook, although LAZ expects geopolitical uncertainty to remain a headwind. Notably, the company aims to increase firm-wide revenue two-fold through double-digit annual revenue growth by 2030. At current levels, we believe the LAZ represents a healthy discount to our private market value estimate.

Additionally, alternative asset manager, **KKR & Co. (KKR)**, traded higher following robust earnings results in a challenging environment. Strong momentum within the capital markets business drove higher-than-expected transaction and monitoring fees, while management fee growth and insurance related earnings were solid. The firm has performed quite well across different economic and financial conditions and, in our view, should continue to outperform for its clients over the long-term, particularly as KKR strives to double the size of the company twice over the next decade.

There were a few notable performance detractors in the quarter. Shares of retail drugstore operator, **Walgreens Boots Alliance, Inc. (WBA)**, declined over the period as challenging consumer and macroeconomic conditions, ongoing operational issues and a significant cut in the dividend weighed on shares. To address these performance lows, WBA's new CEO is rebuilding the company's management team with leaders who have significant experience in healthcare services. Meanwhile, WBA continues to execute on its cost savings initiatives to optimize profitability and is using excess capital to prioritize the sustainability of its operations and balance sheet. Over the medium-term, we expect a re-rating in shares as the new executive team earns credibility, margins and free cash flow show signs of improvement and the company deleverages. WBA shares are currently trading at a significant discount to our estimate of private market value.

Leading provider of audio components and precision electrical devices, **Knowles Corporation (KN)**, also traded lower on mixed earnings results. Strength within their core hearing health market was offset by weaker demand for precision devices from Industrial clients. However, management is focused on cost controls and inventory management which should help drive meaningful earnings growth this year. Longer-term, we believe KN will benefit from further focusing its business on its niche and market leading positions in hearing health and precision devices, and away from the more competitive consumer electronics market. Additionally, we are optimistic in the synergy opportunities driven by the recent acquisition of Cornell Dubilier, which has enhanced KN's existing customer base and revenue streams. At current levels, KN is trading at a meaningful discount to our estimate of private market value.

Lastly, global dental manufacturing company, **Envista Holdings Corp. (NVST)**, declined on mixed earnings results and disappointing full year guidance implying a step-down in profitability. The company is navigating heightened investments, sanctions in Russia and pricing pressures in China due to volume-based procurement (VBP) reimbursement, as well as a weakening environment in North America for large dental equipment and implants. Meanwhile, NVST is in search of a new CEO and CFO creating another business distraction and further uncertainty. Shares are likely range bound for the next couple of quarters until a new leadership team is installed and NVST works through its challenges. We are deeply disappointed with this investment. After reassessing the name, we have concluded that the company has multiple opportunities to drive upside over the long-term. We believe NVST will benefit from its rich research and development pipeline, several new products in high-growth dental segments, facility consolidation and previous IT investments. At current levels, we believe the downside is priced in. We are now evaluating the upside return potential with shares trading at a significant discount to our estimate of private market value.

Also in the quarter, we initiated a new position in manufacturer and developer of laboratory equipment and biological testing, **Bio-Rad Laboratories Inc. (BIO)**. The company offers a worldwide presence with the United States representing 42% of revenue, Europe 31%, Asia 21% and Other 6%. Its customer base is diversified with hospital labs representing 34% of revenue, reference labs 11%, transfusion labs 10%, academic 21%, biopharma 15%, and applied markets 9%. BIO boasts a solid financial profile, rising operating margins, high and recurring revenue streams. We believe Bio-Rad is a classic Ariel company, offering leading innovative products in a growing worldwide marketplace. The company estimates 80% of sales are from products in which Bio-Rad has dominant market share.

By comparison, we successfully sold out of tool manufacturer, **Snap-on Incorporated (SNA)** to take profits as shares reached our estimate of private market value.

While Wall Street's newly dubbed "fab four[1]" have dominated the rally in recent months, their concentration and elevated valuations remain highly influential on overall market performance. Escalating geopolitical tensions, the potential timing of the Fed pivot, 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 consider macroeconomic developments and recent headlines within the context of our long-term investment horizon. We continue to be cautiously optimistic and believe the underlying strength of corporate profits will prove resilient. Consumers are still spending, unemployment remains low and the balance sheets of U.S. financial institutions and households are generally in good shape. As rates begin to subside in 2024 and beyond, we think the gap between mega-cap stocks and their small to mid-cap counterparts will narrow, fortified by consumer confidence, sticky wages, as well as slowing, yet steady long-term economic growth. Meanwhile, we stand ready to take advantage of any pull backs. We strongly believe the disciplined investor that stays the course and consistently owns differentiated, quality business models with robust balance sheets will deliver superior returns over time.

---

Investing in mid-cap companies is more risky and volatile than investing in large cap companies. 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) for the Ariel Mid Cap Value Composite for the 1-, 5-, and 10-year periods was +13.13%, +8.18%, and +6.94%, respectively. For the period ended 3/31/24 the performance for the Russell Midcap Value Index and the Russell Midcap Index for the 1-, 5-, and 10-year periods was +20.40%, +9.93%, and +8.57%, and +22.35%, +11.09%, and +9.95%, 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 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 3/31/24, nVent Electric plc. constituted 2.3% of the Ariel Mid Cap Value Composite (representative portfolio); Lazard Ltd. 2.7%; KKR & Co Inc 2.5%; Walgreens Boots Alliance, Inc. 2.1%; Knowles Corporation 2.2%; Envista

[1] The "Fab Four" are the largest stocks in the S&P 500 Index driving market performance: Amazon.com, Inc. (AMZN), Meta Platforms Inc. (META), Microsoft Corp. (MSFT) and NVIDIA Corp. (NVDA).

Holdings Corp. 1.8%; Bio-Rad Laboratories Inc. 1.1%; and Snap-on, Incorporated 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 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 Midcap® Value Index measures the performance of the mid-cap value segment of the U.S. equity universe. It includes those Russell Midcap Index companies with lower price-to-book ratios, lower forecasted growth values and lower sales per share historical growth. Its inception date is February 1, 1995. The Russell Midcap® Index measures the performance of the mid-cap segment of the U.S. equity universe. The Russell Midcap Index is a subset of the Russell 1000® Index. It includes approximately 800 of the smallest securities based on a combination of their market cap and current index membership. Its inception date is November 1, 1991. 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.

**Ariel Investments**

200 E. Randolph St., Suite 2900
Chicago, IL 60601

312.726.0140

- arielinvestments.com
- linkedin.com/company/ariel-investments
- instagram.com/arielinvestments
- twitter.com/arielinvests

SLOW AND STEADY WINS THE RACE