

Ariel Global (NZD)

Quarter Ended June 30, 2024

The bull market continued in the second quarter driven primarily by investor enthusiasm for large U.S. companies and artificial intelligence (AI) themed stocks. This narrow, momentum driven, rally helped the MSCI ACWI and MSCI ACWI ex-U.S. indices eke out a modest gain, even as the MSCI EAFE Index posted declines due to its lack of exposure to tech beneficiaries in China and Taiwan. Nonetheless, the global outlook is brightening for the second half of 2024—supported by a recovery in bank lending, a pick-up in global manufacturing, recent structural reforms in Japan, new government policies to stabilize the China property market and boost the economy, as well as the near-term possibility of rate cuts in the U.S. and Europe. Meanwhile, the prospect that upcoming elections in the U.S. and Europe may potentially lead to a reshuffling of political power have become a focal point for investors—given the potential economic and market implications. China’s support for Russia is also casting an ominous shadow. Although uncertainty is high and volatility will likely remain elevated for now, these risks represent short-term noise within the context of our long-term investment horizon. In what proved to be a tough quarter, the Ariel Global Composite dropped -4.47% gross of fees (-4.66% net of fees) in the quarter, lagging the +0.98% gain posted by the MSCI ACWI Index and the -2.41% 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 bottom-up strategy is overweight Health Care, Consumer Discretionary, Financials, Utilities and Information Technology. It is significantly underweight Consumer Staples, Industrials and Real Estate, as well as lacks exposure to Energy and Materials. At the sector level, our positioning within Materials, Consumer Staples and Energy was the greatest contributor to returns, while our investment choices within Information Technology, Health Care and Communication Services were the largest performance detractors.

Market leader for computer storage systems, **NetApp Inc.** advanced over the period following a top- and bottom-line earnings beat. Strong growth across its All-Flash, Block, Artificial Intelligence (AI) and Public Cloud products, tight cost controls and operating margin expansion drove the outperformance. Additionally, management raised the quarterly dividend, announced a buyback program and reiterated its commitment to return 100% of free cash flow to shareholders in 2025, further aiding shares. We 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, we remain excited about the company’s digital transformation projects involving business analytics, AI and data security.

Taiwan Semiconductor Manufacturing Company, Ltd. (TSMC) traded sharply higher in the quarter, following its annual shareholder meeting where management highlighted robust earnings visibility. The boom in AI investment is driving significant demand for the semiconductor hardware that enables it. TSMC currently holds a dominant position in relevant chip manufacturing and packaging. Additionally, although AI investments have been mostly focused on the datacenter market, Apple’s recent announcement on “Apple Intelligence” kickstarted an Edge AI race—which will likely drive greater than expected semiconductor growth in smartphones. TSMC is Apple’s sole foundry partner which bodes well for the future. Overall, we continue to view TSMC’s scale, technology, business model, customer service and execution favorably. The fact the company remains committed to returning capital to shareholders through both buybacks and dividends is another plus.

Additionally, Korea’s largest financial company in terms of assets and customer base, **KB Financial Group**, increased in the quarter following an earnings beat, highlighted by solid profitability, stable loan growth and net interest margin expansion. Given KB Financial’s capital structure and solid provisioning practices, we believe it is well-positioned to deliver on its enhanced shareholder return policy, inclusive of dividends, buybacks and subsequent share cancellations. Despite the recent outperformance, we still see significant upside in the name as it is trading at 0.5x price-to-book and generates return-on-equity in line with its cost-of-equity.

There were a few notable performance detractors in the quarter. One of the world’s largest semiconductor chip manufacturers by revenue, **Intel Corporation (INTC)**, underperformed in the period on news of a longer than expected turnaround in profitability within the Foundry business. This was exacerbated by disappointing near-term guidance due to a weakening demand environment signaling an extended replacement cycle. We view the quarter as a temporary trough that should dissipate as we see signs of a cyclical recovery for personal computers (PCs) and central processing units (CPUs), driven by the Windows 11 upgrade. In our view, the market is overlooking the progress Intel is



making to advance its manufacturing process. Not to mention, the company's efforts to serve as a viable second source foundry partner of leading-edge silicon. 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.

China's internet search and online community leader, **Baidu, Inc.** also traded lower in the period as the country's tech giants entered an Artificial Intelligence (AI) price war. Baidu responded by slashing prices across its AI offerings and making its Ernie Bot accessible for free. While the delayed monetization of AI does reflect the volatility of the Chinese technology industry, we are steadfast in our endorsement of Baidu as a leader in the field. Its core business offers downside protection as the company continues to establish its dominance in China's AI scene. Additionally, an improving ad conversion rate indicates a core business advancement from low-single-digit growth to mid-to-high single-digit growth. Our thesis on Baidu remains predicated both on this acceleration and a gradual macro recovery. In success, shares will trade higher with AI Cloud and Autonomous Driving offering long-term optionality.

Finally, American healthcare company, **CVS Health Corporation (CVS)**, declined following disappointing earnings results and a subsequent reduction in full year guidance. The miss was primarily due to increased utilization of Medicare Advantage plans and weakness in the health services segment driven by the loss of a large client and continued pharmacy client price improvements. In response, management reiterated its focus on improving margins and enhancing its positioning in Medicare Advantage. CVS believes the program can remain an attractive business for Aetna and CVS Health over time and will construct its bid for 2025 as a multi-year repricing opportunity across plan level benefits. Meanwhile, CVS continues to return capital to shareholders through dividends and a recent accelerated share repurchase transaction.

We initiated seven new positions in the quarter.

We purchased multinational insurance and financial services company **AXA SA**, which is currently trading at a significant discount relative to its U.S. peers due to weaker operating performance and its exposure to the European economy. We expect this gap will narrow as AXA prioritizes underwriting within the more predictable non-life business segments including—commercial, protection and health insurance—all of which offer recurring revenues and higher margins. Furthermore, as a stronger cash generator, investors are benefitting from rising dividends as well as opportunistic share repurchases.

We added property and casualty insurer, **Allstate Corporation**. A challenging macro-environment, inflation and

lower reserve development led to significant underwriting losses across key markets, presenting us with an attractive entry point. Looking ahead, we expect the strong pricing environment, coupled with lower inflationary pressure and future premium growth to yield upside for shares. Additionally, management is committed to improving its adjusted expense ratio and recently made upgrades to its claims handling processes to minimize loss development and lower claim severities.

We bought bank holding company, **BAWAG Group AG**. In our view, consensus estimates for 2025 and 2026 do not fully appreciate the sustainable growth potential, best-in-class cost efficiency and sector-leading capital returns the business offers. Given the acquisition of Netherlands-based mortgage bank, Knab, as well as recent reports highlighting BAWAG as the leading contender to acquire Barclay's German Consumer Finance business, we believe the company is well-positioned for future growth. In addition to its deal activity, management remains committed to free cash flow generation and returning capital to shareholders via dividends.

We also added positions in two of the largest homebuilders in the U.S., **D.R. Horton** and **Lennar Corporation**. We think the U.S. housing market will continue to experience healthy demand due to substantial supply shortages resulting from a lack of construction following the global financial crisis. Against this favorable backdrop, we believe both companies are well-positioned to capitalize on recent affordability issues driven by rising housing prices, with their entry level, single-family-focused business models.

We initiated a position in property investment and development company in the MENA region, **Emaar Properties PJSC**. We believe the company will continue to benefit from the post COVID recovery in Dubai's real estate market, which has been amplified by a large number of expatriates entering the country. Sales in the development, retail, hospitality and entertainment segments have all demonstrated growth. Across these segments, healthy domestic spending as well as a rebound in tourism are driving traffic, occupancy and rates. We expect Emaar Properties valuation discount to regional peers will narrow as it continues to post strong financial results and generate exceptional cash flow.

Lastly, we added **Infineon Technologies AG**, a leading player in power semiconductor and system solutions. The company has a dominate market position in the automotive, power management, microcontrollers and Internet of Things (IoT) technologies. In our view, Infineon is well-positioned to benefit from major electrification themes in both auto and renewable markets. Near-term the company is benefitting from the shift in battery electric vehicles (BEVs) towards plug-in hybrids (PHEVs) given its manufacturing capabilities of discrete Insulated-Gate Bipolar Transistors (IGBTs), which



are mostly used in PHEVs. Other notable growth opportunities include increased penetration of Infineon's Advanced Driver Assistance System (ADAS), enhanced focus on energy efficiency and industrial power applications as well as sustainable electric energy conversion in data centers. At current valuation levels, we do not believe the market fully appreciates Infineon's strong competitive position and growth prospects.

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 megacap technology names—whose rich valuations continue to propel broad market performance—appear vulnerable to a correction. Escalating geopolitical tensions, unpredictable monetary policy, as well as the outcome of elections in the U.S. and Europe 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 sustainable, profitable growth and robust balance sheets will be the drivers of future outperformance. Accordingly, we continue to improve our upside capture across our international and global portfolios while remaining laser focused on preserving downside protection.

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 and ETFs 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 within the strategy may never be recognized by the broader market. The strategy is often concentrated in fewer sectors than its benchmarks, and its performance may suffer if these sectors underperform the overall stock market.

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 6/30/2024, the performance (net of fees) of the Ariel Global Composite (NZD) for the 1, 5, and 10-year periods were +8.98%, +9.43%, and +10.11%, respectively. For the period ended 6/30/2024, the performance for the MSCI ACWI Index and the MSCI ACWI Value Index for the 1, 5, and 10-year periods were +20.02%, +12.93%, and

+12.44% and +14.54%, +9.13%, and +9.28%, 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 New Zealand dollars. Current performance may be lower or higher than the performance data quoted. The Ariel Global Composite differs from its benchmark, the MSCI ACWI (All Country World Index), because the Composite has fewer holdings than the benchmark.

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As of 6/30/2024, NetApp, Inc. constituted 3.2% of the Ariel Global Composite (representative portfolio); Taiwan Semiconductor Manufacturing Company, Ltd. 3.0%; KB Financial Group, Inc. 1.7%; Intel Corporation 2.1%; Baidu, Inc. ADR 2.7%; CVS Health Corp. 1.9%; AXA SA 0.9%; Allstate Corporation 1.8%; BAWAG Group AG 1.1%; D.R. Horton, Inc. 1.2%; Emaar Properties PJSC 0.5%; Infineon Technologies AG 1.5%; Lennar Corporation 1.2%; Grupo Financiero Banorte SAB de CV 0.0%; Nokia Oyj 0.0%; Secom Co Ltd. 0.0%; TIM SA 0.0%; and Vodafone Group PLC 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 Composite.

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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 company's 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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