William Blair

4Q 2017

Fund Manager Commentary
William Blair International Small Cap Growth Fund

Fund Performance & Positioning

The William Blair International Small Cap Growth Fund (Class N shares) underperformed its benchmark, the MSCI All Country World ex-U.S. Small Cap Index (net), during the fourth quarter. Underperformance was driven by a combination of allocation and selection effects. From a stock selection perspective, Industrials exposure was particularly detrimental, hampered by defense companies Ultra Electronics Holdings and Elbit Systems. Ultra Electronics is a high-quality niche manufacturer of products for defense and security applications. The share price weakened after the company reported a sharp decline in full year organic revenue due to mounting pressures in the funding of UK defense programs. Elbit Systems is an Israeli defense enterprise with interests in land, airborne and communication systems. The share price pulled back after advancing significantly in the first nine months of the year. Elbit reported positive 3Q financial results, including 12% growth in the order backlog that signaled continued strong demand for their products.

Top 10 Holdings[1] as of 12/31/17

Company Name	*% of Fund*
Nissan Chemical Industries, Ltd.	1.4%
Rubis SCA	1.3%
SSP Group plc	1.3%
Royal Unibrew A/S	1.2%
Localiza Rent a Car S.A.	1.2%
Elbit Systems Ltd.	1.1%
Stanley Electric Co., Ltd.	1.1%
Banca IFIS S.p.A.	1.1%
KOSE Corporation	1.1%
MGM China Holdings Limited	1.1%
Total Top 10	**11.9**

Within Health Care, unowned South Korean biotech company SillaJen detracted from relative results, as its share price advanced 123% in USD terms during the quarter, bolstering Index performance. Within the Information Technology sector, do-it-yourself website development company Wix.com detracted from results. Despite posting better than expected financial results, the market was disappointed in Management's higher R&D spending outlook for 2018 – which would weigh on near-term profit margins. Partially offsetting these negative effects were positive stock selection in the Real Estate, Consumer Staples and Consumer Discretionary sectors. Within the Real Estate sector, Relo Group Inc boosted relative results. Relo is a provider of outsourced management of corporate rental accommodations and fringe benefit services in Japan. The share price performance was underpinned by solid fiscal 2Q earnings and strong fundamental trends.

Market Review & Outlook

The 2017 market environment was characterized by strong and accelerating global economic growth. The broadening nature of growth was particularly noteworthy, as evidenced by strengthening industrial production volumes across the world. Corporate earnings results were bolstered by the expanding economic environment, providing a tailwind for investors. Beyond improving corporate performance, major national elections, especially in Europe, produced outcomes favorable for continued growth.

Risk assets led the markets in 2017. Emerging markets—which received oxygen from a weak U.S. dollar—performed the strongest, returning 36.8% in USD terms, as measured by the MSCI EM IMI. Developed markets also performed well, advancing 22.4% for the year (MSCI World IMI). China (+50.7%) drove emerging markets' performance to a significant extent, with additional contributions from South Korea (+46.0%), India (+43.7%), Poland (+53.6%), Chile (+43.3%) and South Africa (+34.0%)—illustrating the breadth of gains across the EM landscape.

[1] Listed holdings are presented to illustrate examples of the securities that the Fund has bought and do not represent all of the Fund's holdings or future investments. Information about the Fund's holdings should not be considered investment advice. There is no guarantee that the Fund will continue to hold any one particular security or stay invested in any one particular sector. Holdings are subject to change at any time and are as of the date shown above. Top ten holdings are shown as a percentage of total net assets.

From a global sector perspective, technology led by a significant margin in 2017, advancing 41.0% for the year (as measured by MSCI ACWI IMI), far outpacing the second best performer, materials, which gained 29.3%. Within technology, the software and services industry returned 42.2%, followed by semiconductors and equipment (+42.0%) and technology hardware and equipment (+37.8%). In contrast, energy (+5.2%) and telecom (+8.2%) were the worst performing sectors for the year.

The performance of William Blair's proprietary quantitative models demonstrated that momentum, earnings trend and growth style factors outperformed during 2017, while fundamental volatility, quality and valuation factors underperformed. These style trends were more pronounced within emerging markets.

Underpinning 2017 performance was a broadening of growth in both developed and emerging markets, which we have not seen in more than a decade. As growth broadened, it also strengthened. Year-over-year growth in industrial production volumes, a proxy for growth, ranged from 3% in the United States to 8% in Brazil.

When global growth drives expansion, it shows up in corporate earnings. In 2017, returns were driven predominantly by corporate earnings growth as opposed to price-to-earnings multiple expansion. That is not to say that multiple expansion was completely absent. Delving deeper into the sectoral composition of returns, Europe and the United States benefited from P/E expansion during the year, which we would expect in response to stronger growth performance.

The synchronized global recovery is well understood, and global growth remains firm. For us, though, it is important to understand the nature of the cycle and how far we are into it. The low-volatility regimes we have experienced in the equity and fixed-income markets carry potential risks. When change comes, it will likely be difficult, because we have been shielded from natural cyclical behavior—from negative economic and market forces—for some time.

Sudden inflationary pressures and wage growth acceleration would likely alter investor return expectations, driving bond yields and volatility materially higher, while potentially triggering equity-leadership rotation both across and within sectors. Financials would be expected to benefit from higher rates, for example, but increased caution would be warranted for financially-leveraged companies. We want to be mindful of this.

Reflecting on some of the preeminent growth themes of 2017, including technology and the rise of innovation in China, we are optimistic. Despite the growing likelihood of a cyclical slowdown within the technology sector, we believe that strong secular growth will continue.

From a geographic perspective, we believe that emerging markets continue to offer attractive investment opportunities heading into 2018. In particular, there are abundant opportunities to invest in China's growth, but we are mindful of the significant share-price gains in 2017 from the perspective of near-term momentum reversal risk.

INVESTMENT PERFORMANCE % (as of 12/31/17)

	QTR	YTD	1Y	3Y	5Y	10Y
Class I (SI: 11/01/05)	4.87	32.70	32.70	11.74	10.09	5.22
Class N (SI: 11/01/05)	4.81	32.17	32.17	11.41	9.76	4.87
MSCI All Country World ex-U.S. Small Cap Index (net)	6.56	31.65	31.65	11.96	10.03	4.69

EXPENSE RATIOS (%)

	Gross Expense
Class I	1.30
Class N	1.59

Expenses shown are as of the most recent prospectus.

Performance cited represents past performance. Past performance does not guarantee future results and current performance may be lower or higher than the data quoted. Returns shown assume reinvestment of dividends and capital gains. Investment returns and principal will fluctuate with market and economic conditions and you may have a gain or loss when you sell shares. For the most current month-end performance information, please call +1 800 742 7272, or visit our Web site at www.williamblairfunds.com. Class N shares are available to the general public without a sales load. Class I shares are available only to investors who meet certain eligibility requirements.

DISCLOSURE

The Fund's returns will vary, and you could lose money by investing in the Fund. The Fund holds equities which may decline in value due to both real and perceived general market, economic, and industry conditions. International investing involves special risk considerations, including currency fluctuations, lower liquidity, economic and political risk. Investing in emerging markets can increase these risks, including higher volatility and lower liquidity. Investing in smaller companies involves special risks, including higher volatility and lower liquidity. Convertible securities may be called before intended, which may have an adverse effect on investment objectives. Diversification does not ensure against loss.

The Morgan Stanley Capital International (MSCI) All Country World Ex-U.S. Small Cap Index (net) is a free float-adjusted market capitalization weighted index that is designed to measure the equity market performance of small capitalization developed and emerging markets, excluding the United States. This series approximates the minimum possible dividend reinvestment. The Index is unmanaged, does not incur fees or expenses, and cannot be invested in directly.

This content is for informational and educational purposes only and not intended as investment advice or a recommendation to buy or sell any security. Investment advice and recommendations can be provided only after careful consideration of an investor's objectives, guidelines, and restrictions.

Please carefully consider the Fund's investment objectives, risks, charges, and expenses before investing. This and other information is contained in the Fund's prospectus, which you may obtain by calling 1-800-742-7272. Read it carefully before you invest or send money. Investing involves the risk of loss.

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