# Fund Manager Commentary
## William Blair Emerging Markets Small Cap Growth Fund

### Fund Performance & Positioning

The William Blair Emerging Markets Small Cap Growth Fund (Class N shares) generally performed in line with its benchmark, the MSCI Emerging Markets Small Cap Index (net), during the first quarter.

Performance was primarily driven by positive stock selection across most sectors. The Consumer Discretionary, Industrials and Consumer Staples sectors were the largest sources of relative return. Consumer Discretionary results were bolstered by both the overweighting and positive stock selection effects. NagaCorp, the hotel and casino operator in Cambodia, was a notable contributor, fueled by impressive operating results amid the ramp up of the Naga2 resort and robust growth outlook for both the VIP and mass market gaming segments. Huazhu Group was also additive as investor sentiment was bolstered by the company's robust operating performance. Stock selection within the Industrials sector was particularly favorable, with domestic Chinese companies Zhejiang Dingli Machinery, the largest manufacturer of aerial working platforms in China by sales volume, and Centre Testing International, the leading testing, inspection and certification company in a highly fragmented market, adding to relative returns in the period. Within Consumer Staples, Yihai International, a leading Chinese condiment manufacturer in China, was a significant contributor to relative performance. Yihai International's stellar performance was driven by solid flavoring and hot pot demand in China, the company's strong brand with premium seasoning positioning, and its expanding product and distribution channels.

Partially offsetting these effects were negative contributions from the Information Technology, Financials and Materials sectors. Stock selection in Information Technology detracted largely due to unowned names which rallied on improved market sentiment for semiconductors. In addition, Douzone Bizon, the leading provider of ERP software in Korea, was dragged down by below-consensus 4Q18 results. Financials performance was hampered by both the sector overweighting and negative stock selection effects. Gruh Finance was a notable detractor as the stock fell on the announcement of its acquisition by Bandhan Bank. Within Materials, our lack of exposure to South African mining companies weighed on performance. In addition, Berger Paints India hindered relative results. The share price of the Indian decorative paint manufacturer weakened amid 3QFY19 results that trailed consensus expectations. Despite robust revenue growth, margin compression on higher input costs hurt the bottom line. During the period, Information Technology exposure was increased to an overweight position through additions to existing holdings and new purchases such as Nanya Technology and TravelSky Technology. Nanya Technology is the Taiwanese memory company. TravelSky is the Chinese back – end software airline ticketing company that benefits from a monopoly status in a highly regulated, structurally growing air travel market. Industrials exposure was also increased with the purchase of Zhejiang Dingli Machinery, the largest manufacturer of aerial working platforms in China by sales volume.

**Top 10 Holdings[1] as of 3/31/19**

| *Company Name* | *% of Fund* |
|---|---|
| Yihai International Holding Ltd. | 2.3% |
| Zhejiang Supor Co., Ltd. | 2.2% |
| PT Ace Hardware Indonesia Tbk | 1.8% |
| China Education Group Holdings Limited | 1.7% |
| Feng Tay Enterprises Co., Ltd. | 1.6% |
| IRB Brasil Resseguros S/A | 1.6% |
| Zhejiang Dingli Machinery Co.,Ltd. | 1.5% |
| Magazine Luiza S.A. | 1.5% |
| Makalot Industrial Co., Ltd. | 1.5% |
| Fila Korea Ltd. | 1.4% |
| **Total Top 10** | **17.1%** |

[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.

Financials exposure was reduced during the period, as Banca Transilvania and Banco del Bajio were notable liquidations. We exited Banca Transilvania, a leading Romanian bank, amid the government's decision to introduce a bank tax at the end of 2018 coupled with a weakening macroeconomic backdrop. Slowing economic growth and policy uncertainty in Mexico drove the sale of Banco del Bajio. Exposure to Consumer Staples declined as a result of the sale of TCI, the Taiwanese the supplement and skin products original design manufacturing company, and Marico, the Indian home and personal care product manufacturer. From a geographic perspective, notable adjustments were an increase to China, offset by decreases to India and Brazil.

## Market Review & Outlook

After a difficult end to 2018, equity markets around the world rallied to start the year despite signals of moderating global growth. The MSCI ACWI Investable Market Index (IMI) gained 12.29% in USD terms, the largest quarterly gain since 2010, as investor sentiment was bolstered by a more dovish tone out of major central banks and improved trade talks between the U.S. and China. Developed market equities outpaced emerging markets primarily driven by strength in the U.S. and Canada.

U.S. equities rallied in January (+8.60%) and continued to post strong returns throughout the quarter (+13.99%). Growth in the U.S. remained solid but started to decelerate off of last year's previous highs. The Federal Reserve's acknowledgment of slower economic growth and dovish stance on interest rates helped ease investor sentiment and boosted returns across sectors.

European equities also advanced despite signs of significant deceleration in manufacturing growth. Specifically, purchasing manager surveys continued to point to deceleration in the pace of industrial orders growth and subsequent industrial production growth in the Euro Area. Brexit woes continued to weigh on the economic conditions within the United Kingdom but the market felt some relief following the announcement that the European Union had agreed to delay the Brexit process past the March 29 deadline. The MSCI Europe ex-U.K. IMI advanced 10.50% and the MSCI U.K. IMI advanced 12.32% in USD terms during the quarter.

Within emerging markets, the story for the quarter was the rebound in equity performance across China's mainland securities (A-shares), which advanced 33.02% for the quarter, erasing the 32.99% loss incurred in 2018 (as measured by the MSCI China A Onshore Index in USD terms). The A-share market rallied following news of several fiscal and monetary stimulus measures aimed to boost the economy. Additionally, A-shares were bolstered by news that MSCI would quadruple the weighting of A-shares in global benchmarks by increasing the inclusion factor from 5% to 20%. Outside of China, emerging market equities broadly lagged the global benchmark. Rising geopolitical tensions between India and Pakistan weighed on the Indian Rupee and equity market. The MSCI India IMI modestly advanced +6.65% in USD terms for the quarter.

From a global sector perspective (as measured by the MSCI ACWI IMI), Information Technology significantly led the market, driven by strength within small cap software and IT services. Other cyclical sectors such as Real Estate, which sold off sharply in late 2018, rallied during the first quarter of the year. Conversely, Financials lagged primarily due to weakness in Japan.

As we begin the second quarter of 2019, domestic demand in key jurisdictions is showing signs of stabilization and synchronized fiscal expansion. Existing home sales rebounded strongly in March in the U.S., and private consumption growth in the Euro Area is tracking a nearly 2% annualized pace. At the same time, purchasing manager surveys continue to point to deceleration in the pace of industrial orders growth and subsequent industrial production growth.

We regard the deceleration in economic activity in the U.S. to be more about the base effect rather than the end of the current economic cycle. As the impact of corporate tax cuts unveiled at the beginning of 2018 dissipates, the U.S. economy is returning to a growth rate of approximately 2%. The divergence between the U.S. and other economies is normalizing in line with our expectations. If the rest of the world continues to grow at the current pace, the growth wedge and by extension the substantial outperformance of U.S. markets vis-à-vis the rest of the world is likely to moderate from here.

Growth is being supported by fiscal stimulus measures globally. Starting in Europe, the Euro Area is set to experience the first fiscal expansion in a decade. In Germany, Finance Minister Olaf Scholz has set aside approximately €150bn for much needed investment in infrastructure, education, housing and digital technology over the next four years. More immediately, the fiscal stimulus slated for this year will be largely for consumer spending, as higher unemployment and pension benefits, together with a tax cut to lower income earners, is expected to boost purchasing power by 0.5% of GDP. The abolition of the solidarity surcharge, which accounts for 5.5% additional income tax, is set to be reduced beginning this year. Government construction orders soared 12.2% in Q4 2018 from the prior quarter, and will likely advance further in 2019.

In France, President Emmanuel Macron responded to the "yellow vests" movement by announcing measures to boost the purchasing power of households by about 0.4% of GDP. These include cancellation of the increase in social charges on pensions, an increase in the activity bonus for employees paid the minimum wage, and a tax exemption on exceptional year-end bonuses and income from overtime.

In China, the government continues to roll out tax cuts following its 2-year effort to streamline and digitize tax collection. In Q1 2019, the government announced a CNY2 trn tax cut on business activity. Effective April 1, VAT in the top general category will be reduced from 16% to 13%, on top of reductions in the employer contribution to social security from 20% to 16%. Together with household income tax reform implemented last year, these measures will continue to support domestic activity. At the same time, the scope for further adjustments on the fiscal side is not exhausted, as the State Administration of Taxation continues to report an increase in aggregate tax collections in excess of expectations.

The U.S. continues to maintain a highly expansionary fiscal policy stance. Although major corporate tax cuts boosted domestic activity in H1 2018, the U.S. budget deficit is expected to be even larger this year, at nearly 4.5% of GDP, despite the domestic economy expanding at a 2%+ annual pace.

Within portfolios, we maintain our focus on companies with sustainable earnings trends and recurring-revenue business models that add growth visibility at this later stage of the economic cycle. Recent positioning adjustments within our ACWI-oriented funds generally reflect our incrementally less cautious outlook on China. Within China, we continue to emphasize domestically-oriented consumer, healthcare and technology companies that we believe are well positioned to benefit from the economy's ongoing transition to a consumption and services-driven growth model.

## INVESTMENT PERFORMANCE % (as of 03/31/19)

| | QTR | YTD | 1Y | 3Y | 5Y | Since Incep. |
|---|---|---|---|---|---|---|
| Class I (SI: 10/24/11) | 7.62 | 7.62 | -17.68 | 4.26 | 2.79 | 8.34 |
| Class N (SI: 10/24/11) | 7.66 | 7.66 | -17.84 | 3.97 | 2.50 | 8.04 |
| MSCI Emerging Markets Small Cap Index (net) | 7.76 | 7.76 | -12.42 | 5.95 | 1.76 | 3.67 |

## EXPENSE RATIOS (%)

| | Gross Expense | Net Expense |
|---|---|---|
| Class I | 1.35 | 1.30 |
| Class N | 1.68 | 1.55 |

Expenses shown are as of the most recent prospectus. The Fund's Adviser has contractually agreed to waive fees and/or reimburse expenses to limit fund operating expenses until 4/30/19.

**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 involves a high level of risk and may not be appropriate for everyone.** You should only consider it for the aggressive portion of your portfolio. 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. Investing in securities of smaller companies tends to be more volatile and less liquid than securities of larger companies. International investing involves special risk considerations, including currency fluctuations, higher volatility, lower liquidity, economic and political risk. Investing in emerging markets can increase these risks. The securities of emerging market companies may be subject to greater volatility and less liquidity than companies in more developed markets. Individual securities may not perform as expected or a strategy used by the Adviser may fail to produce its intended result. Currency rates may fluctuate significantly over short periods of time and may reduce the returns of a portfolio. Convertible securities may be called before intended, which may have an adverse effect on investment objectives.

The Morgan Stanley Capital International (MSCI) Emerging Markets Small Cap Index (net) is a free float-adjusted market capitalization index that is designed to measure equity market performance of small cap companies in emerging markets. 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 and summary prospectus, which you may obtain by calling +1 800 742 7272. Read the prospectus and summary prospectus carefully before investing. Investing includes the risk of loss.***

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