

William Blair Emerging Markets Small Cap Growth Fund Fund Manager Commentary

Market Review

Global equities declined (-1.11%) in the third quarter as volatility picked up in September, erasing gains in July and August. Developed Markets were flat (-0.19%) but outperformed Emerging Markets (-7.39%) primarily due to weakness within China. From a global sector perspective, Consumer Discretionary (-5.13%) and Materials (-4.45%) lagged. Conversely, Energy continued to outperform (+2.87% for the quarter and +34.26% year-to-date) as rising demand and supply constraints drove stronger crude oil prices.

US equities were flat (-0.06%) for the quarter as economic data remained healthy, albeit past the peak rate of growth, and solid corporate earnings helped offset volatility induced by the rise of new Delta variant cases. At the much-anticipated Jackson Hole symposium, Federal Reserve Chairman Jerome Powell noted that the economy has made “substantial further progress” on inflation, while the labor market has also made “clear progress”. The Fed also announced that the tapering of quantitative easing could start this year and finish in mid-2022.

Japanese equities were flat in July and August but advanced strongly in September to close out a solid third quarter (+4.35%). Strength within Japan was primarily due to the announcement that Prime Minister Suga would not be running for re-election in November. Despite a very short time in office (less than a year), Suga’s approval ratings were very low following the administration’s handling of the coronavirus pandemic.

Emerging Markets sharply declined (-7.39%) primarily due to weakness within China (-17.99%). In late July, the Chinese government announced new regulatory moves which negatively impacted companies in the technology and private education sectors. Hampered investor sentiment was further compounded in late September on concerns over the collapse of Evergrande, one of China’s largest real estate developers, and the potential impact on China’s financial system. Conversely, India continued to advance (+12.64%) amid a slowdown in the country’s new COVID-19 cases and a significant liquidity boost from the country’s central bank and foreign inflows.

Fund Performance

Outperformance by the William Blair Emerging Markets Small Cap Growth Fund (Class N shares) versus the MSCI Emerging Markets Small Cap (net) was primarily driven by positive stock selection across most sectors. The Consumer Discretionary, Information Technology and Materials sectors were the most significant contributors to relative return. Within Consumer Discretionary, F&F Co/New and Momo.com Inc boosted relative performance. F&F is a leading manufacturer of apparel and accessories under licensed brands such as Discovery and MLB, primarily in Korea and China. The stock rallied as the company

Top 10 Holdings¹ as of 9/30/2021

<i>Company</i>	<i>% of Fund</i>
SRF Ltd.	2.6
Aspeed Technology Inc.	2.4
F&F Co.,Ltd	2.4
TOTVS S.A.	2.2
eMemory Technology Incorporation	2.2
Centre Testing International Group Co., Ltd.	1.9
Dino Polska S.A.	1.8
Varun Beverages Ltd.	1.8
TCS Group Holding PLC	1.8
HeadHunter Group PLC	1.7
Total Top 10	20.8

posted record earnings growth propelled by exponential MLB overseas growth in China. Momo.com is the leading Taiwanese e-commerce retail leader in price, breadth of offering, and shipping as a result of an extensive logistics and distribution build-out. Strong operating performance bolstered by robust new users and average order growth drove the share price higher. eMemory Technology Inc, the Taiwanese semiconductor IP company within Information Technology was an additional source of outperformance as the company’s revenue growth accelerated amid a favorable wafer pricing dynamic. New product launches and wider adoption of their solutions at leading edge technologies support a robust medium-term growth outlook. Within the Materials, SRF Ltd bolstered relative returns. SRF is a leader in specialty fluorine chemicals, technical textiles, and packaging films in India. The company is benefiting from improved global agrochemical cycle and growing import substitution due to disruptions in China.

Partially offsetting these effects was negative stock selection within the Industrials sector coupled with the overweighting to the Consumer Discretionary sector. Within Industrials, Centre Testing International, a leading testing, inspection and certification (TIC) company in China, hurt relative performance as the stock declined after it reached its 28% foreign ownership

¹Listed 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.

limit. The company fundamentals and growth outlook remain solid as Center Testing International is well positioned to benefit from China's on-going improvements in safety standards and de-carbonization focus as well as management's increased emphasis on profitability. Sequoia Logistica e Transporte, a Brazilian logistics solutions provider, also detracted from relative returns. Despite softer near term performance amid slightly weaker growth in Brazilian ecommerce vs. last year, the company growth outlook remains very strongly driven by the expansion of the Brazilian ecommerce market, the increased outsourcing logistics trend by retailers, further market consolidation within Brazil's logistics provider landscape, and the likely downsizing of Correios.

Positioning

During the period, Consumer Discretionary exposure was reduced through trims to existing holdings. Industrials and Communication Services exposure were also reduced via the liquidation of Hiwin Technologies Corp and Iclick Interactive Asia respectively. Hiwin's growth outlook deteriorated amid weaker automation demand from China. Iclick was sold amid regulatory concerns in order to reduce exposure to Chinese ADRs. From a geographic perspective, notable adjustment was decreases to China, offset by increases to India with the purchase of Polycab India Ltd and Indian Energy Exchange Ltd.

Polycab India is a leading manufacturer and distributor of cables and wires in India. The company is in its early lifecycle. It is extending its leadership in cables and wires into adjacent categories and increasing its total addressable market as it continues to shift into organized sector.

Indian Energy Exchange is an electricity trading platform connecting power generators and power consumers. The investment thesis is underpinned by the company's large and expanding total addressable market, long runway for growth, high returns and strong competitive advantage.

Outlook

Corporate performance has been strong as the global economies continue to resume normalized activity. We have seen strength in the cyclical areas of the economy, while at the same time companies with leading business models and practices have continued to press their structural competitive advantage. This has driven positive momentum for the market this year, and companies with strong returns and differentiated positioning like those we seek to invest in have generally enjoyed even stronger corporate and stock market performance on balance. While we do not expect the backdrop to change materially, we do point out two primary areas of intermediate-term focus for global equity investors: China policy and regulation risk, and the inflation outlook.

China

We view the China investment opportunities and risks within the framework of what has, and what hasn't changed. In turn we reference our investability model to determine exploitability and accessibility for returns in Chinese equities.

Favorable elements of what hasn't changed include China's commitment to economic growth, accelerated corporate innovation across many industries, and liberalization of capital markets to compete on a global stage. At the same time, the nature of the autocratic regime and state-planned economy has facilitated the execution of the China Communist Party's (CCP) objectives through policies and regulations directing resources into innovative sectors and facilitating the emergence of new industries and global champions.

The absolute power of the state to enact and enforce policy and regulation is another constant characteristic of China. The current regulatory crackdown on industries that have benefited from policy support (or at least the government's laissez-faire approach), while seemingly unexpected, is, when analyzed closely, consistent with the government's priorities and past attitudes and actions toward other industries.

Chinese leadership's reprioritization of its objectives to rebalance growth versus social issues is one example. Given China's current stage of development, its focus is on Common Prosperity and more balanced growth as opposed to its prior target of fast growth.

Under the surface, China's economic achievements have seemingly caused growing tensions between the country's socialist political and ideological goals and growing capitalist (profit-led) economy.

Increased inequality, changes in demographics, and the emergence of new sectors and dominant private corporations have become a significant part of the economy, posing new and critical challenges to the Chinese authorities.

In particular, the digital economy industries and companies have reaped the benefits of an extremely supportive regulatory backdrop, favorable taxation, and access to foreign capital. While many of these companies have benefited society at large by providing availability of goods, cheaper prices, life-enhancing digital services (ecommerce, payments, access to capital, etc.), Chinese leadership is now concerned about the potentially negative impact on inequality and social values that some of these industries have had. It also appears Chinese leadership is concerned about the threat that has arisen from the amount of power accumulated by some platform companies, the influence that foreign investors exert on them, and the potential systemic risks that exist with these new data-heavy business models.

With this, the Chinese authorities have indicated their intention to address perceived excesses and shortcomings that have arisen from the previous policy period, while doubling the size of China's economy by 2035. Beijing's priorities are focused on three core issues: social stability, national security, and sustainable domestic growth.

The fact that these objectives may at first sight seem difficult to reconcile, coupled with the ample room for interpretation of the government's intentions and apparent lack of rules (given the principle-based nature of Chinese regulations), has created much angst and many hurdles for companies as they operate their businesses.

The drastic enforcement of this new wave of regulations in the new economy is, as expected, painful, messy, and a source of angst for companies and investors alike. It has led to irreparable damage and loss in certain industries, such as after-school tutoring (AST). The lack of coordination among different regulators and institutions, conflicting priorities, battles for power, and personal attitudes (a la Jack Ma) have driven regulatory scrutiny in fits and starts, sending ambiguous messages to investors. We believe this is likely to continue.

Also playing a role in the regulatory crackdown is a deepening rivalry between the United States and China, in our view. While China's transformative growth trajectory has posed domestic challenges, it has also raised concerns for the rest of the world and particularly the United States. As China became a strategic competitor to the United States, tensions arose on trade and economic issues, then expanded to technological, geopolitical, ideological, and financial fronts. As a result, China's regulatory crackdown has focused on industries with stronger foreign connections, especially those in highly sensitive sectors.

In particular, Beijing's desire to bring home some of its largest and most attractive companies that are listed overseas coincided with increased scrutiny from the United States on Chinese American depository receipts (ADRs). This occurred with the passing of the Holding Foreign Companies Accountable (HFCA) Act, which sets a timeline for the forced delisting of these companies. This has called into question the legality and enforcement of the important variable interest entity (VIE) structure, as well foreign governments' willingness to allow investment in Chinese companies.

Where from here?

One thing is clear: Not all industries and companies are equal on these fronts, and a thorough evaluation of their alignment with Beijing's key objectives and priorities should help determine the extent of the impact and viability of entire industries.

For foreign investors, the new paradigm also calls into question the investability of China. To assess this, we have a framework that seeks to identify the exploitability and accessibility of future corporate growth and returns.

"Exploitability" moves beyond the typical definition of a company's ability to innovate, create products and services, and grow profitably; in this case it also assesses the degree of alignment between the corporation's activities and the government's objectives. Here, we assess the potential outcome and variability in a conventional financial model. Industries that we believe may have elevated risk include media, online retailing, education, gaming, and healthcare, specifically pharmaceuticals. We are actively researching the variability and distribution of future outcomes of revenues and profits for our portfolio holdings in these industries and adjusting our estimates accordingly.

"Accessibility" refers to foreign investors' ability to access economic value creation. Here, we assess the Chinese government's intention of allowing foreign capital into certain industries, including threats to the VIE structure as well as the risk to ADR listings.

Assuming foreign investors are not banned, but the degree of accessibility is in question, we discount the potential future earnings in the form of an increased equity risk premium (ERP), and ultimately weighted average cost of capital (WACC) or discount rate.

We believe the market may have become too sanguine regarding China's country risk, with the ERP as low as that of many developed markets late last year. With the recent market correction, it has risen back to its long-term average.

The assumption that the Chinese government intends to ban foreign capital is radically opposed to the consistent efforts from Beijing to open its capital markets, giving access to foreign investors and developing the internationalization of the renminbi. Still, selective strategic industries may be affected by bans amid increased protectionism in the name of higher public interest. This was the case with the AST (after school tutoring) industry.

Needless to say, while we continue to find China's long-term growth and corporate performance opportunities attractive, our investability framework has identified greater uncertainty and thus risk. In many of our investment strategies, we have cut our China weightings materially, by many cases in half from prior high levels. We feel this is the prudent response to many of the industries and companies that may remain at risk of being in the crosshairs of more government regulatory scrutiny. At the same time we have rotated our Chinese investments into those companies whose growth opportunities are aligned with government objectives.

We do recognize that the real and perceived interpretation of these risks could change, in particular with more transparency of intention from the government. We have spent a great deal of collective research time on these important issues, and that will likely be the case well into and beyond 2022.

Inflation

As our economies gradually reopen and people are allowed to move more freely, the 2020 experience should reverse. We believe the challenges with goods production and longer delivery times will get resolved within months, not years, and goods price inflation will likely return to the pre-COVID muted annual rate of sub-2%. Services prices will likely move sharply higher as restaurants, theatres, and travel reopen. We may even see pockets of quite large price increases, as supply will not be able to adjust instantly to all the pent-up demand, in leisure travel for example.

These pockets of much stronger price gains generate headlines, but we believe the argument that such isolated, temporary pockets of price pressures will translate into sustained, higher annual inflation in the medium term is weak because it does not consider supply adjustment.

We expect the supply responses to play out in the coming quarters to meet demand levels. First, in our view there is no reason to believe the current logistical bottlenecks will prove to be structural, rather they are recovering from the complexity of a shutdown that we haven't experienced in decades. On the

other hand, the two biggest risks of persistent inflation arise from labor and energy prices. In the US alone, we have seen an employment gap of close to 10 million workers. The vast majority of those workers in our estimation are only temporarily sidelined due to COVID-related issues, ranging from childcare and safety concerns, to paycheck relief benefits outweighing wages. We are already beginning to see the gradual resumption of those workers back into the workforce and expect that to play out through next year.

As for energy prices, we do not believe there is a structural lack of supply owing to the energy transition from fossil fuels to renewables. Instead, we believe much of the move in oil and gas prices is attributable to the geopolitical complications from the Nord Stream 2 pipeline that has yet to come on-line. While complicated, we believe the political incentives are largely aligned, and this will be resolved in the coming months providing important relief to energy prices.

In the medium term, stronger economic growth of around 3% can translate into a sustainable annual inflation rate of 2%-3%. Every policymaker and consumer would be pleased with that outcome. The central banks would welcome this with open

arms instead of worrying about inflation being too low as a result of weak growth. We believe this is the most likely probability for the next several years.

Recently the risk of stagflation has received a great deal of attention. The bottom line is that the calamitous experience of the 1970s had much to do with egregious macroeconomic meddling, and inflation did not appear suddenly out of nowhere. Misguided price controls and wage freezes disincentivized supply adjustment and destroyed demand growth. The 1970s bear no resemblance to what we are talking about today: stronger demand growth, employment, and supply adjustment and more stable, mild inflation consistent with price stability, broadly defined.

Our current outlook calls for growth continuing to slow on a sequential basis, supply chains resuming their historic efficiencies, and peaking corporate profit margins moderating. Coming from historically high valuations, we would expect only modest outcomes for equities over the coming quarters.



INVESTMENT PERFORMANCE (AS OF 9/30/21)

	QTR	YTD	1 Y	3 Y	5 Y	Since Incep.
Class I (SI: 10/24/11)	0.35%	14.11%	37.33%	19.73%	11.82%	11.96%
Class N (SI: 10/24/11)	0.32%	13.91%	37.03%	19.43%	11.52%	11.66%
MSCI Emerging Markets Small Cap Index (net)	-2.16%	17.20%	43.24%	13.11%	9.75%	6.62%

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.

¹Class I and Class N inception date: 10/24/2011.

EXPENSE RATIOS

	Gross Expense	Net Expense
Class I	1.45%	1.30%
Class N	1.77%	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 4/30/22.

IMPORTANT DISCLOSURES

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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