William Blair

First Quarter 2022

William Blair International Small Cap Growth Fund
Fund Manager Commentary

Market Review

After a strong performance in 2021, global equities declined (-5.47%) in the first quarter (as measured by the MSCI ACWI IMI) amid increased market volatility induced by concerns over inflation, rising interest rates, and heightened geopolitical tension in Eastern Europe. In January, concerns over rising inflation and hawkish moves by the Federal Reserve drove a sharp style rotation into lower-value, lower-growth-oriented securities. Volatility continued in February as the Russian invasion of Ukraine prompted a coordinated response by Western countries in the form of firm sanctions targeted at Russia's financial system. The sanctions on Russia rendered Russian equities and the ruble un-investable with fears of contagion to other markets. In this environment, growth equities significantly underperformed value-oriented equities (the MSCI ACWI IMI Growth declined -9.83% while the MSCI ACWI IMI Value declined -1.08%). This was evident from a global sector perspective as consumer discretionary (-11.63%) and information technology (-10.37%) declined while energy stocks strengthened (+22.64%) on stronger crude oil prices.

Developed markets declined (-5.32%) as measured by the MSCI World IMI. U.S. equities declined (-5.38%) as the Russian invasion of Ukraine amplified existing concerns over rising inflation and interest rates. The Federal Reserve approved its first interest rate increase (0.25%) in over three years with further hikes expected throughout the rest of the year. Europe ex-U.K. plunged (-10.04%) as heightened concerns over the availability of Russian energy imports to Europe weighed on investor sentiment. In addition to targeting Russia's key financial institutions, the U.S. and European allies also cut Russia from the SWIFT International Payment system. Germany also announced it would be halting the certification of the Nord Stream 2 gas pipeline from Russia.

Emerging markets declined (-6.65%) with mixed returns across countries. Russian equities plunged as the broad range of sanctions imposed on their economy weighed heavily on the ruble and market returns. China sharply declined primarily in March (-14.27% for the quarter) amid a spike in COVID-19 cases and newly imposed lockdowns across major cities. Conversely, Latin America generated strong returns for the quarter (+26.34%) with broad outperformance across countries. Oil exporters and commodity beneficiaries such as South Africa (+19.30%), Kuwait (+18.56%), and Saudi Arabia (+16.64%), also outperformed.

Fund Performance

First quarter underperformance by the William Blair International Small Cap Growth Fund (Class N shares) versus the MSCI ACWI ex. US Small Cap (net) was primarily due to a significant rotation in the market towards low valuation, low-quality, and low-growth companies. From an attribution perspective, weaker stock selection within industrials and healthcare significantly weighed on performance. Industrials weakness was primarily due to Japanese professional services company, Benefit One. Benefit One is a provider of HR-related services, in the form of outsourced fringe benefits. A structural tightening of the Japanese labor market has increased the need for employers to attract hires using the types of services offered by Benefit One. We expect that future regulatory changes should also drive increased demand. As the business has a fixed cost base and low variable costs, operating leverage is high, supporting a rate of profit growth at the top end of the peer group. The share price declined on lower-than-consensus operating profit primarily due to an increase in costs in the fringe benefits segment of the business.

Within healthcare, Israeli-based medical device company InMode weighed on performance. InMode has developed proprietary minimally invasive and non-invasive technologies for various aesthetic applications including fat reduction, skin tightening, and muscle toning. While the company is currently focusing on the large TAM for the medical aesthetics market, the

Top 10 Holdings[1] as of 3/31/2022

Company	*% of Fund*
Beijer Ref AB	2.4
Grupo Aeroportuario del Centro Norte	2.2
Investment Aktiebolaget Latour	2.1
Lifco AB	2.1
MIPS AB	2.0
TechnoPro Holdings	2.0
Softcat plc	2.0
AU Small Finance Bank	2.0
Safestore Holdings PLC	1.9
InMode Ltd.	1.8
Total Top 10	**20.5**

[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.

products are applicable in a wide array of indications such as women's health, ENT (ear, nose & throat) and ophthalmology, which could significantly expand the targeted market going forward. After a strong run in 2021, the share price declined alongside higher-valuation healthcare peers amid the broad market rotation into lower-valuation companies.

Partially offsetting these negative effects was positive stock selection within utilities bolstered by EDP Renovaveis (EDPR). EDPR is the fourth largest wind and solar energy producer globally outside of China and a pure-play renewable energy producer with 11.7GW installed capacity. The company's focus is currently on Americas and Iberia, being one of the first movers in the space with a concentrated portfolio, large pipeline, and strong track record of PPA origination. The share price strengthened after the company reported strong 2021 gains primarily attributed to the capital gains from the sale of its 211-megawatt wind farm portfolio.

From a regional perspective, positive stock selection within Latin America bolstered performance. Within Latin America, the high-quality Mexican airport operator, Grupo Aeroportuario Del Centro (OMA) was the strongest contributor. OMA has multiple avenues to enhance profitability relative to peers including adding non-aeronautical sources of revenue and increasing international traffic through its airports. The share price has strengthened as air passenger traffic has improved for both domestic and international travel but remains slightly below pre-pandemic levels.

Positioning

During the first quarter, financials exposure increased through the purchases of Gjensidige Forsikring. Gjensidige is the largest P&C insurer in Norway with 26% market share. The business has generated strong returns and protects margins over growth. With a culture deeply focused on cost efficiencies, Gjensidige has been able to return multiples of its cost of capital across market environments and cycles. Consumer discretionary exposure also increased through the purchase of Arezzo Industria e Comercio. Arrezo is the leading ladies' footwear franchise in Brazil that has entered the male, female, and kids clothing segment through the company's acquisition of Reserva. The company has generated high returns and has a net cash position which may be used for acquisitions. These changes were offset primarily by a reduction to healthcare exposure, which was reduced through the liquidation of Nanosonics, the Australian life science company with a focus on disinfectant and sterilization technology. From a geographic perspective, notable adjustments were an increase to Latin America offset by a decrease to Europe ex-U.K. and Emerging Asia. The portfolio's weighting in Emerging Markets approximated 23.3% at the end of the period, up from 19.6% at the beginning of the year.

Outlook

As we begin the second quarter of 2022, we reflect on the unique environment we have experienced the last two years. The nature of the economic cycle, originally due to the COVID pandemic, has been exacerbated. We've experienced an extreme closing and reopening of the global economy, accompanied by unprecedented liquidity, and pronounced rotations in style – first with growth outperforming strongly, and more recently value charging back. Finally, the Russian invasion of Ukraine continues to impact the economy and the markets and in response we have needed to reassess our outlook leading into this year.

Similar to our forecast earlier this year, we continue to see a natural slowing of economic growth from very high levels seen in 2020; but also, rising inflation, which implies a further deceleration of earnings growth. We also continue to analyze the rising interest rate environment and its relationship to valuations.

Growth – Post-Russian Invasion

In terms of growth, we continue to see risks of slower economic and corporate profit growth than we had originally expected. Importantly, in contrast to our prior outlook, we now expect materially lower growth in Europe. Leading into the year, most European economies remained much below their pre-pandemic output trajectory and now the Russian invasion of Ukraine has created further downward pressure. Particularly in Eastern and Central Europe, expanding past Russia, into Hungary and Poland, we'll expect continued acceleration in inflation, currencies under pressure and higher interest rates.

Within the U.S., we see less impact and expect growth to remain at broadly similar levels as in our pre-Russian invasion case, which is a significant sequential deceleration in economic activity, from approximately 5.5% growth that we observed in 2021 down to closer to 2.5% growth rate by the end of the year. Corporate profit growth expectations seem reasonable and remain at the highest level for most major countries.

Within China, our outlook is mixed. We've seen a resurgence of COVID and lockdowns, which we expect to impact economic activity and weakening of growth in the first half of this year, coupled with potential geopolitical risk. In contrast, we think the government's focus on a stable economic environment will lead to a moderate fiscal and monetary stimulus as well as potential for some easing of regulatory pressures. Valuations in China are also relatively attractive in our view, after a difficult 2021.

Inflation

The ongoing lockdowns and the military conflict that we now have in Europe has prompted us to revise our inflation projections further. We originally expected inflation to peak in early summer. We now expect inflation to peak at a higher rate in the later part of this year and to rollover thereafter. Of course, wage pressures were something that we were going to monitor on an ongoing basis, and that that remains a key variable to watch in the U.S. What that means for equity markets, is that corporate earnings growth, especially outside the U.S., is expected to decelerate further throughout much of 2022, which will put further downward pressure on multiples.

Valuation and Style Performance

Thus far in 2022, we've seen one of the most significant style rotations we have experienced in multiple decades, which leads us to a discussion regarding equity valuations. The general relationship between rates and valuations holds, and despite the influences of the conflict and persistent inflation, we do believe that we are still in a long-term economic recovery. Thus, we expect gradual monetary tightening and removal of excess liquidity, consequently leading to further multiple contraction as the expansion continues and rates go higher.

This has direct implications for the performance of Growth equities vs Value equities, and we have seen this play out significantly in the beginning of 2022. Valuation as a factor has been by far the strongest driver of performance year to date.

Does this imply that the very long run of quality growth over value is over? We don't think so. Many of the drivers of the outperformance of Growth are still in place: positive but lower economic growth, low (albeit rising) interest rates, and a competitive landscape in the real economy that acknowledges the structural advantages of some areas of the economy over others, as well as those of differentiated, innovative business models. As it relates to interest rates, as measured by the 10-year yield, we believe would need to meaningfully rise from current levels (+300bps), to significantly affect relative future profitability and future investment premium.

And as we look forward, what hasn't changed? We think the innovation and disruption cycle hasn't changed, and arguably, has even accelerated. The dynamic shifting of corporate winners and losers remains a constant, and again, if anything, may be accelerated. Importantly, durability or improvements in corporate competitive advantage will likely remain underappreciated.

We believe this environment will create an important backdrop for active investing. Understanding companies with differentiated business models, unique cultures and durable competitive advantages will increasingly be crucial to determining investment performance in this complex environment.

INVESTMENT PERFORMANCE (AS OF 3/31/22)

	QTR	YTD	1 Y	3 Y	5 Y	10 Y
Class I (SI: 11/01/05)	-20.65%	-20.65%	-9.65%	10.63%	7.28%	7.20%
Class N (SI: 11/01/05)	-20.71%	-20.71%	-9.93%	10.35%	6.98%	6.89%
MSCI AC World ex-US Small Cap Index (net)	-6.51%	-6.51%	0.03%	10.22%	7.89%	7.28%

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.

EXPENSE RATIOS (%)

	Gross Expense
Class I	1.25%
Class N	1.52%

Expenses shown are as of the most recent prospectus.

IMPORTANT DISCLOSURES

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.

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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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