Artisan Partners International Small-Mid Team

Investment Philosophy and Process

Artisan Non-U.S. Small-Mid Growth Strategy

ARTISAN PARTNERS

We are long-term oriented investors in high-quality businesses exposed to structural growth themes, and we use a contrarian approach to acquire these businesses. We seek high returns on capital, sensible valuations and excellent management teams.

Rezo Kanovich
Portfolio Manager

Analysts (L-R)
Andres Avalos Vitiello
Anastasia Karpova
Samir Mainthia
Matthew Trusz

Artisan Partners International Small-Mid Team

Our Investment Team

We are passionate about discovering businesses early on their journey to becoming much larger industry-leading enterprises and take a hands-on approach to sourcing these investments through global travel and direct management meetings. For more than a decade, we have sought to redefine how investors view opportunities in this asset class and have proven our ability to compound returns over the long term by investing in high-quality small businesses in the midst of a transformation.

Our investment team, led by portfolio manager Rezo Kanovich, joined Artisan Partners from OppenheimerFunds in October 2018. Four research analysts support Mr. Kanovich and are dedicated solely to this strategy. Two of the four, Andres Avalos Vitiello and Samir Mainthia, worked with Mr. Kanovich at OppenheimerFunds and also joined Artisan in October 2018 to continue working together as a cohesive team. Research analysts Matthew Trusz and Anastasia Karpova joined the firm in July 2019 and December 2021, respectively. Mr. Kanovich has more than two decades of investment experience, including over a decade managing assets in this investment approach, and collectively the team now boasts over 35 years with an exclusive focus on the international small-mid asset class.

Our team culture values collegiality, intellectual curiosity, and hard work. Every analyst is broad-minded with the ability to think like a portfolio manager, and, conversely, Mr. Kanovich considers himself as an analyst first and foremost.

Why International Small Caps?

In our view, international small-cap equities offer the rare blend of a large and inefficient opportunity set, attractive historical risk-adjusted returns, and potentially enhanced diversification benefits. Yet, investors have historically underappreciated this asset class, which, on average, represents less than 1% of a typical portfolio. Of the more than 10,000 small-cap companies worldwide, more than 80% are outside the US[1]. The sheer breadth of the investment universe makes it difficult for the sell-side to properly cover it, providing more opportunity for seasoned investors to exploit inefficiency in stock prices.

It may come as a surprise to many that international small caps (MSCI EAFE Small Cap Index) have outperformed their large-cap counterparts (MSCI EAFE Index) with similar levels of volatility over the past 10 and 20 years. They also have generated a higher Sharpe ratio than US small caps (Russell 2000® Index) over the past 20 years, a period of broad US leadership[1]. The opportunity for the broad index notwithstanding, we think it is important to highlight the potential for active management to generate alpha in this overlooked and vast investment universe. Our differentiated investment approach focuses on the select few companies we believe have the potential to become large, global industry leaders. While short-term oriented investors may view this asset class as a trading opportunity around a source of volatility, we are drawn to the ability to find leading businesses of tomorrow at a point of relative nascency. This highly selective, long-term and low turnover approach exposes investors to what we believe are the most attractive elements of this opaque and misunderstood asset class.

Philosophy and Process Highlights	
Investing with Tailwinds	▪ Identify structural themes at the intersection of growth and change ▪ Invest in companies poised to be long-term beneficiaries of those trends
High-Quality Businesses	▪ Differentiated and defensible business model ▪ Dynamic management team ▪ High ROIC, healthy cash flow generation, strong balance sheet and ability to self-fund growth
A Contrarian Approach to Valuation	▪ Market dislocations and mismatches between stock price and long-term business value create opportunity ▪ Focus on a company's through-cycle profitability
Manage Unique Risks of International Small- and Mid-Cap Equities	▪ Understand the direct and indirect security risk and the probability of permanent capital impairment ▪ Diversify portfolio across industries, geographies and themes ▪ Position sizing based on magnitude of opportunity, assessment of risk, and level of conviction

We look for companies with underlying structural growth potential, tangible competitive advantages and, very importantly, the management that can bring the companies from small to big.

Our Investment Philosophy

We seek long-term ownership in high-quality businesses exposed to structural growth themes and intend to acquire these businesses in a contrarian fashion in times of adversity, or perceived adversity.

Investing with Tailwinds

We look for companies that are backed by long-term tailwinds and whose success is less dependent on a cyclical backdrop. Portfolio companies operate at the intersection of growth and change within their respective industries, where ingenuity can drive disruption within industry value chains. This thematic element to the investment approach orients the portfolio to areas of the market that we believe are positioned on the right side of history and should continue to accelerate over the long term. Though not static, there are generally about a dozen themes represented in the portfolio at any time, such as "picks and shovels" of the biotech revolution, biotherapeutics, cloud conversion, next-gen auto and energy transition. Theme identification is the result of bottom-up observations rather than a top-down allocation exercise. Our travel-intensive and iterative process focused on fundamental company research leads to industry-focused learning from analyzing a competitive landscape and industry value chain. We seek to understand the industry dynamics resulting from the change agents we identify and their potential second-order effects. After identifying a compelling business in a promising industry, we look for similar business models in other geographies and adjacent companies integral to the ecosystem. This geographic triangulation is essential to how we build themes from the bottom up.

High-Quality Businesses

Our team seeks to acquire smaller companies that are on a journey to becoming larger, often globally relevant, industry leaders within their respective niches. We look for certain ingredients that attractive companies have, such as differentiated and defensible business models, talented management teams able to create value even in turbulent times, unique assets, strong balance sheets, healthy cash flow generation, the ability to self-fund growth, pricing power and structurally high or improving returns on invested capital. Sustainable competitive advantages may include technological leadership, intellectual property, strong brands and operations in industries favoring natural monopolies or duopolies. In combination, we believe these characteristics typically can make companies resilient amid market gyrations and provide the best chance of compounding returns over the long term.

A Contrarian Approach to Valuation

We set out to find stocks we can own well beyond the initial five-year underwrite as the business evolves with its opportunity set. Wonderful businesses are rarely available at attractive prices, so we look for opportunities to acquire them and patiently build positions in times of adversity or perceived adversity. The path from small capitalization to much larger is rarely easy and is never linear. Transitions from small to big take all shapes and span various timelines, and often the market fails to recognize investment cycles. Mismatches between stock price and long-term business value are also created by market dislocations, management changes or temporary slowdowns in individual businesses. We also employ a contrarian approach to the sell discipline by constantly monitoring valuations, business fundamentals and changing competitive landscapes.

Our job is to separate signal from noise and exploit short-term irrationality in the market. As such, we focus on a company's through-cycle profitability and use five-year cash flow projections to underpin business model durability. Additionally, we look for situations where a company has one or more cheap embedded options on large potential outcomes. Examples may include research and development pipelines, new product development and new growth markets.

Manage Unique Risks of International Small- and Mid-Cap Equities

Our team believes international small- and mid-cap growth equities are exposed to unique risks that are important to recognize. Smaller companies frequently struggle to grow or survive. Many are slaves in their value chains, operate in over-regulated industries, are over-leveraged, cannot attract or retain the right leadership talent to drive their organizations to the next level, and face large, powerful competitors that enjoy the benefits of scale. We seek to understand direct and indirect security risks by intimately knowing portfolio companies and the industries in which they operate as well as remaining mindful of any idiosyncratic challenges.

Further, our team views risk as the probability of permanent loss of capital, not short-term share price volatility. In fact, as a low-turnover, long-term oriented portfolio, volatility tends to create a dynamic for our team to be opportunistic and contrarian in managing position sizes.

Our team also manages risk by diversifying the portfolio across industries, geographies and themes and by weighting positions according to the magnitude of opportunity versus our level of conviction. Positions are built gradually as we get to know businesses and their management teams. Larger positions reflect higher confidence in a favorable risk/reward profile. Those positions believed to have greater risk are typically afforded smaller sizes in the portfolio.

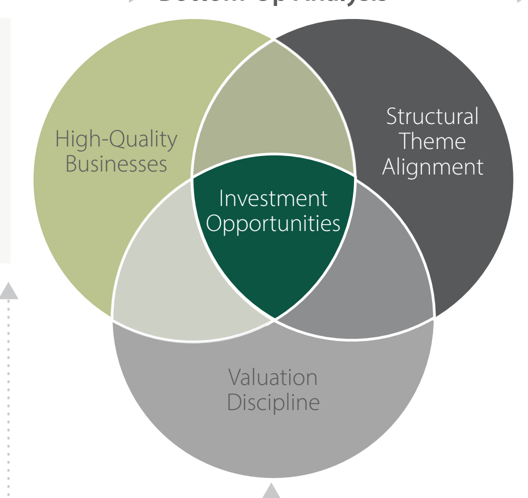
We're far more concerned with identifying companies that can eventually grow several-fold than with obsessing over the false precision of a short-term earnings estimate.

Research Process

Theme Identification

- Intersection of Significant Growth and Change
- Regulatory Changes or Institutional Progress Occurring
- Unique and Defensible Business Models with Attractive Growth Characteristics

Bottom-Up Analysis



Idea Iteration

- Industry value chain analysis including competitors and suppliers
- Triangulation of ideas across industries, countries and companies

Portfolio Construction

Artisan Non-U.S. Small-Mid Growth Strategy

- Diversified portfolio of approximately 100 - 150 holdings.
- Maximum position size target of 5%, but rarely exceeding 3%.[1]
- Maximum of 25% in any one industry.[2]
- Minimum of 65% in non-US companies.[2]
- Cash typically less than 10%.
- Turnover typically around 20%.
- Small- and mid-cap companies are those with a market capitalization range generally similar to the constituents of the MSCI All Country World (ACWI) ex USA SMID Index at time of purchase.[2, 3]

Risk Management

- We define risk as the probability of permanent loss of capital, not short-term share price volatility
- We manage a highly diversified portfolio throughout industries, geographies and themes
- We manage risk primarily at the company level by analyzing the resilience of individual business models
- Our 5-year plus investment horizon focuses our attention to understand the direct and indirect risks for each business
- We build positions gradually, with position sizes reflecting the magnitude of the opportunity and our level of conviction

Portfolio Tail

- We manage an overall flat portfolio with a long tail of small positions
- A range of smaller positions with idiosyncratic drivers can help provide the portfolio with positive convexity
- Newer purchases are typically small weightings as we get to know the businesses and their management teams
- Tail positions may carry a higher risk profile but possess embedded optionality and a favorable risk-return trade-off

Based on a model portfolio. [1]Subject to manager discretion. [2]Limitations apply at the time of purchase. [3]MSCI reconstitutes the index periodically.

Research Process Summary

Alignment with structural growth themes that have global relevance, a focus on high-quality companies with sustainable growth potential over the long term, and strict valuation discipline are the pillars of our investment process. The labor- and travel-intensive fundamental research process facilitates our team in identifying high-quality, small- and mid-cap companies operating at the intersection of growth and change. One can think of our research process as being analog in a digital world. Information, particularly quantitative data, is commoditized. Drivers of value, like creativity and talented leaders, go beyond traditional metrics. In order to glean non-obvious insights during the research process, we meet with company managements around the world—of current portfolio holdings, companies under consideration for inclusion in the portfolio and competitors. We meet with heads of research and development, industry experts, trade publication reporters and government policymakers, and solicit feedback from customers of and suppliers to companies. This approach forms the foundation of our differentiated viewpoints on companies and changes in the industry.

Other sources that supplement internal research efforts include company documents, brokerage research and third-party research providers. Our team also has direct access to several global databases and to real-time market and company information. The research process is ongoing and iterative with team members testing hypotheses amid new information, and it benefits from the collective analytical prowess and experience of team members.

The investment approach is exclusionary and the thematic element helps narrow the massive international small- and mid-cap investment universe to areas of the market that our team believes are positioned on the right side of history and possess structural growth tailwinds. Our high bar for quality, which applies to segments of an industry value chain with the potential to sustainably generate high returns on invested capital and to companies with attractive, long-term growth characteristics, further narrows the investment universe.

Geographic triangulation is essential in our bottom-up approach to stock selection. After identifying a compelling business in a promising industry, we look for similar business models in other geographies and adjacent companies integral to the ecosystem.

A contrarian approach to valuation discipline guides every buy and sell decision. Our team focuses on a company's through-cycle profitability and uses five-year cash flow projections to underpin business model durability.

Decision-Making Process

All members of the investment team, including the portfolio manager, are responsible for conducting fundamental research. Each team member works independently to develop ideas, but communication and collaboration are a constant. Our team's collective experience and judgment enrich discussions on companies, industries and ecosystems and help to ensure all relevant issues and opportunities are addressed and thoroughly evaluated. Portfolio manager Rezo Kanovich has the ultimate buy and sell authority on all positions and determines position sizes.

Portfolio Construction and Risk Management

Our investment team believes international small- and mid-cap equities are exposed to unique risks that require managing. Faster-growing small companies are frequently at the forefront of macroeconomic change, often compete with larger, more diversified operators that enjoy the benefits of scale and may face key-person risks. The most important way our team addresses these risks is through individual company analysis.

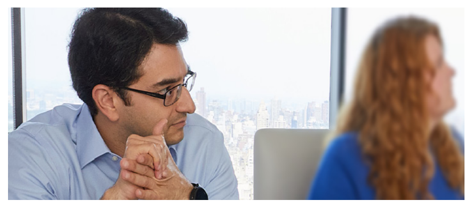
Further, we view risk as the probability of permanent loss of capital, not share price volatility. In fact, as long-term investors, volatility tends to create opportunities for us to acquire high-quality companies in a contrarian fashion. We seek to avoid permanent loss of capital in a number of ways. First, we look to own high-quality businesses with differentiated and defensible business models, favorable positions in their industry value chains and dynamic management teams. Second, we manage a highly diversified, low-turnover portfolio. Third, positions are built gradually as we get to know businesses and their management teams. Larger positions reflect higher confidence in the risk/reward of the holding. Higher risk positions are typically afforded smaller sizes in the portfolio.

Our investment team members are fundamental investors who select securities and construct our portfolios without regard to a benchmark. However, the Strategy has a number of guidelines and constraints in order to manage the risks inherent in any investment portfolio constructed through fundamental stock selection. These portfolio construction parameters are rigorously monitored by members of Artisan Partners' portfolio oversight team for adherence to the Strategy's stated investment process.

Sell Discipline

Our team monitors each holding closely, evaluating new information relative to the original reasons for investing. We may sell a stock when we think it is approaching full valuation, changing circumstances affect the investment thesis, a company exhibits deteriorating fundamentals, or more attractive opportunities are identified. Further, investing with a distinctly long-term bias allows us to take advantage of market short-termism and exit or trim positions when the valuation gets ahead of fundamentals.

We want to position the portfolio on the right side of history. The best way to do that, in our view, is to identify quality businesses that also benefit from structural growth themes, which increases the likelihood they compound value over time.



International investments involve special risks, including currency fluctuation, lower liquidity, different accounting methods and economic and political systems, and higher transaction costs. These risks typically are greater in emerging and less developed markets, including frontier markets. Securities of small- and medium-sized companies tend to have a shorter history of operations, be more volatile and less liquid and may have underperformed securities of large companies during some periods. Growth securities may underperform other asset types during a given period. Investments will rise and fall with market fluctuations and investor capital is at risk. Investors investing in strategies denominated in non-local currency should be aware of the risk of currency exchange fluctuations that may cause a loss of principal. These risks, among others, are further described in Artisan Partners Form ADV, which is available upon request.

[1] As of 31 Dec 2022

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