# Artisan Global Value Fund

QUARTERLY
Commentary

Investor Class: ARTGX | Advisor Class: APDGX

As of 30 September 2016

## Investment Process

We seek to invest in high-quality, undervalued companies with strong balance sheets and shareholder-oriented management teams.

**Undervaluation**

Determining the intrinsic value of a business is the heart of our research process. Intrinsic value represents the amount that a buyer would pay to own a company's future cash flows. We seek to invest at a significant discount to our estimate of the intrinsic value of a business.

**Business Quality**

We seek to invest in companies with histories of generating strong free cash flow, improving returns on capital and strong competitive positions in their industries.

**Financial Strength**

We believe that investing in companies with strong balance sheets helps to reduce the potential for capital risk and provides company management the ability to build value when attractive opportunities are available.

**Shareholder-Oriented Management**

Our research process attempts to identify management teams with a history of building value for shareholders.

## Team Overview

Our team has worked together for many years and has implemented a consistent and disciplined investment process. Our team is organized by geographic regions, but within those regions we are generalists who look across all industries. We believe this model enables our analysts to become broad thinkers and gain critical insight across all economic sectors.

**Portfolio Management**

Daniel J. O'Keefe
Portfolio Manager (Lead)

N. David Samra
Portfolio Manager

## Investment Results (%)

| As of 30 September 2016 | QTD[1] | YTD[1] | Average Annual Total Returns 1 Yr | 3 Yr | 5 Yr | 10 Yr | Inception[2] |
|---|---|---|---|---|---|---|---|
| **Investor Class: ARTGX** | **6.62** | **7.44** | **11.86** | **5.83** | **13.58** | — | **7.05** |
| **Advisor Class: APDGX** | **6.63** | **7.53** | **12.00** | **5.90** | **13.63** | — | **7.08** |
| MSCI All Country World Index | 5.30 | 6.60 | 11.96 | 5.17 | 10.63 | — | 2.26 |

Source: Artisan Partners/MSCI. [1]Returns for periods less than one year are not annualized. [2]Investor Class inception: 10 December 2007. Advisor Class performance is that of the Investor Class from 10 December 2007 through the inception of the Advisor Class on 1 April 2015, and actual Advisor Class performance thereafter. Performance has not been adjusted to reflect the expenses of the Advisor Class for the period prior to the Class's inception, and Advisor Class performance results would differ if such expenses were reflected.

| Expense Ratios | ARTGX | APDGX |
|---|---|---|
| Semi-Annual Report 31 Mar 2016[1,2] | 1.25 | 1.12 |
| Prospectus 30 Sep 2015 | 1.29 | 1.16[3] |

[1]Unaudited, annualized for the six month period. [2]Excluding Acquired Fund Fees & Expenses as described in the prospectus. [3]Includes estimated expenses for the current fiscal year.

**Past performance does not guarantee and is not a reliable indicator of future results. Investment returns and principal values will fluctuate so that an investor's shares, when redeemed, may be worth more or less than their original cost. Current performance may be lower or higher than that shown. Call 800.344.1770 for current to most recent month-end performance. Performance may reflect agreements to limit a Fund's expenses, which would reduce performance if not in effect.**

## Market Overview

Equity markets globally boomed this quarter, almost without exception. Global indices were up over 5% with non-US markets up nearly 7% and the US up almost 4% (all returns in USD unless otherwise stated). Emerging markets were the best performers—up 9% for the quarter and 16% for the year. BRICs are back, with Brazil up 11%, Russia up 8%, India up 6% and Chinese indexes up a whopping 14% for the quarter. In our view, the equity returns reflect multiple expansion rather than an improving earnings outlook.

There was a bit more divergence in the currency markets. Measured against the dollar, the pound was the big loser, falling 3%. For dollar-based investors, this decline was more than offset by appreciation of the euro, the Japanese yen and most emerging markets currencies. The currencies of commodity-oriented countries, such as Norway, Russia and Australia, appreciated more significantly—the exception here being Canada, where perhaps the loss of fiscal discipline under the new liberal government has served to weaken confidence.

It is meaningful that the pound depreciation versus non-dollar currencies is wider than that seen against the dollar. Britain sends only 15% of its exports to the United States. Just under half go to the euro area, about 6% go to China, while the remainder of the world makes up about 35% of Britain's exports. Since the end of the quarter, on a trade-weighted basis, the pound has fallen to an all-time low. We can tie renewed weakness of the pound to the Tory Party conference, held October 5, where Prime Minister Theresa May's speech laid out a hard-line approach toward Brexit. PM May emphasized control of immigration as her negotiating priority with the EU, rather than the protection of business and financial market interests. The pound reacted immediately, falling 8% over the following few days. The issue takes on particular importance since the UK has long-run trade and current account deficits. Confidence in the country's economic policies is crucial to attract the foreign capital flows that balance the island nation's regular trade outflows. Without that confidence, the pound is vulnerable.

## Portfolio Discussion

All but eight securities in the portfolio appreciated during the quarter. The five largest positive contributors to return were Samsung Electronics, Qualcomm, ABB, Microsoft and ING which we will discuss further.

Among the largest detractors were Oracle, Progressive, Marsh & McLennan, Johnson & Johnson and Royal Bank of Scotland (RBS). Declines were very modest in each case (RBS's return was *positive* in local currency—dinged by the weak pound) with no fundamental reason to explain the underperformance with the exception of Oracle, which reported a slightly disappointing operating margin in its latest results.

Qualcomm's share price rose 29% this quarter after suffering from a number of headwinds over the past year and a half. Its licensing business—which collects royalties on phones that use its 3G/4G-related intellectual property—has been under pressure due to a slowdown in the smartphone market as well as poor compliance from manufacturers who owe royalties but have not paid them. This has been a particular problem in China. In addition, Qualcomm's semiconductor business has suffered as it missed a product cycle, lost significant share and saw its profitability meaningfully eroded. Recent results demonstrated improvements in both these areas. The company is also in merger discussions with another semiconductor company. The transaction has two significant potential benefits. First, because the target company is based outside the US, the transaction would allow Qualcomm to put its massive overseas cash reserves to work without incurring the significant tax penalty involved in repatriating cash for use inside the US. (Yes, you read that correctly: The US corporate tax code materially incentivizes our multinational companies to invest their resources in other countries rather than bring cash back into this country for reinvestment or distribution to shareholders.) Second, the transaction would create a larger, more diversified semiconductor business serving multiple, attractive end markets.

Samsung Electronics' share price appreciated 17% in dollar terms in Q3, of which 12% was due to an increase in the local shares and 5% came from Korean won appreciation. Heading into quarter end, Samsung for once was clicking on all cylinders. The company's world-leading semiconductor business was (and still is) benefiting from both volume growth and improved pricing, the handset business rolled out the Galaxy Note 7 as a slightly bigger and improved form factor to its critically acclaimed Galaxy S7 and S7 Edge, and the smaller consumer electronics and display businesses were showing improved profit trends. Margins were expected to improve across the group heading into the back half of 2016. The share price increase, we believe, reflected both the improved business performance and also the stock market's extreme undervaluation of the business. Unfortunately, as we all now know, the Note 7 turned out to be a ticking time bomb.

Samsung has discontinued production of the Note 7 and has instituted a recall and consumer compensation program for all of the roughly 2.5 million Note 7 phones that have been sold. The company estimates the cost of reversing profits booked at more than $2 billion in the third quarter. The cost of the recall over the next couple of quarters is estimated to be another $3 billion. (Note that Samsung's market cap is over $200 billion.) Though Samsung's recall offer to consumers is attractive, at this stage, it is difficult to gauge the long-term damage to the Samsung brand and, hence, market share. Keeping this issue in perspective, Samsung sold over 76 million handsets in Q2 2016 alone. So, while this is a high-profile issue, it affects only about 3% of recently sold units. Nevertheless, the negative press associated with this issue combined with the release of Apple's so-far successful iPhone® 7 and 7 Plus phones could cause some permanent loss of market share and broader brand damage in consumers' eyes.

The phone business generates about half of Samsung's operating profits with the vast majority of the remaining profits coming from the semiconductor business. With half of the profits in question, one would expect a significant negative share price reaction. Yet, the share price is down only a few percent from the price tick at quarter end. Why? First, the shares are still cheap, in our view. We conservatively estimate that the value of the group's semiconductor and component businesses combined with the company's holdings of cash and securities can justify today's market cap. That means we are paying nothing for the phone business. Second, there has recently been some activist pressure on the controlling Lee family to restructure the web of public and private companies that are used to control Samsung Electronics. There is an opportunity for shareholders to benefit from meaningful cash-based returns as a result of this restructuring. Samsung remains the portfolio's second-largest position.

The share prices of ABB, Microsoft and ING appreciated 18%, 13% and 21%, respectively, during the quarter. All three companies reported good second-quarter earnings and have laid out plans to continue growing underlying profits.

There were no meaningful purchases of new securities during the quarter. All of the remaining shares of New Oriental Education were sold during the quarter as the share price appreciated to our estimate of intrinsic value. We also sold Joy Global on news the company received an acquisition offer.

## Connecting the Dots

It has been a good year for financial assets, just about all of them: stocks, bonds, emerging markets stocks and bonds, junk bonds, etc. The list of securities that have generated good returns in 2016 is remarkable given the backdrop of weak economic growth, Brexit, a stomach-turning US election, the war-torn Middle East and the continued rise of economic populism.

We think a bit of a global perspective may be helpful with this head-scratcher. It starts with the effective subsidies, generally speaking, of the world's central banks. Though the US Federal Reserve is happy, for now, with its $4.5 trillion balance sheet, the ECB and the Japanese central bank have both stepped up activity this year. In addition to printing money to buy sovereign bonds, the ECB has expanded its mandate to include investment grade corporate bonds in its asset-purchase program. Germany's already very low 10-year government bond yield of 0.62% at the beginning of the year has fallen to -0.11%. Additionally, we now have several examples of European corporations issuing new bonds at negative yields. (A client pointed out in a recent meeting that we have now reached the point of no return.) Similarly in Japan, 10-year bond yields are now a negative 8bps as the Japanese central bank continues printing money and monetizing the country's already outsized and menacing public debt. Further, the Japanese central bank has a target to purchase $35 billion of equities. Not to be left behind, in August the Swiss central bank reported it owns CHF127 billion ($124 billion) of equites, up 41% this year. Interestingly, the Israeli and Czech central banks are also now buying stocks.

The excuse used by central bankers for turning a government entity into a leveraged hedge fund is diversification. This is an astonishing insight into how far government bankers have changed the original intent and purpose of a central bank. The result is a cascading effect—pushing most investors not trapped in negative- or low-yielding assets into other riskier assets and across borders. The result is asset price inflation—of all assets.

These market distortions caused by massive central bank intervention in the marketplace are part of the broader trend of government intervention that has taken hold since the financial crisis. Put us down in the column of non-believers. Rather than belabor these points (yet again), we sign off this quarter with two quotes from the Nobel Prize winning economist, Milton Friedman. (No—not Bob Dylan. Sorry.)

*Concentrated power is not rendered harmless by the good intentions of those who create it.*

*There is no such thing as a free lunch.*

**For more information:** Visit www.artisanpartners.com | Call 800.344.1770

**Carefully consider the Fund's investment objective, risks and charges and expenses. This and other important information is contained in the Fund's prospectus and summary prospectus, which can be obtained by calling 800.344.1770. Read carefully before investing.**

**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 markets. Securities of 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. Value securities may underperform other asset types during a given period.**

MSCI All Country World Index measures the performance of developed and emerging markets. S&P 500® Index measures the performance of 500 US large-cap companies. The index(es) are unmanaged; include net reinvested dividends; do not reflect fees or expenses; and are not available for direct investment.

This summary represents the views of the portfolio managers as of 30 Sep 2016. Those views may change, and the Fund disclaims any obligation to advise investors of such changes. For the purpose of determining the Fund's holdings, securities of the same issuer are aggregated to determine the weight in the Fund. These holdings comprise the following percentages of the Fund's total net assets (including all classes of shares) as of 30 Sep 2016: Samsung Electronics Co Ltd 4.3%, QUALCOMM Inc 3.6%, ABB Ltd 3.4%, Microsoft Corp 3.5%, ING Groep NV 2.3%, Oracle Corp 4.4%, The Progressive Corp 1.3%, Marsh & McLennan Co Inc 3.2%, Johnson & Johnson 2.6%, Royal Bank of Scotland Group PLC 2.4%. Securities named in the Commentary, but not listed here are not held in the Fund as of the date of this report. Portfolio holdings are subject to change without notice and are not intended as recommendations of individual securities. All information in this report, unless otherwise indicated, includes all classes of shares (except performance and expense ratio information) and is as of the date shown in the upper right hand corner.

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