

Summary & Outlook

International Leaders ADR SMA Strategy

Market Overview

Global equities gained in the third quarter (the MSCI ACWI IMI returned +7.67% for the quarter and +18.25% year-to-date). The rally was supported by easing global tariff tensions, a quarter-point rate cut by the U.S. Federal Reserve, and broadening earnings growth across regions. Investor sentiment was also buoyed by continued optimism around AI-driven capital expenditures.

U.S. equities finished higher in the quarter (+8.15% for the quarter and +14.15% year-to-date as measured by the MSCI USA IMI). The rally was driven primarily by continued momentum in the technology sector, fueled by massive corporate investments in artificial intelligence infrastructure and innovation. The S&P 500 and Nasdaq reached record highs coupled with a historic milestone as NVIDIA became the first company to reach a \$4 trillion market cap. The Federal Reserve's rate cut in September added further support to equity valuations, citing weakening labor market conditions despite persistent inflation.

European equities advanced during the third quarter; however, returns were muted compared to strength seen in the first half of the year (+3.34% for the quarter and +27.53% year-to-date as measured by the MSCI Europe IMI). Performance was supported by improving investor sentiment and asset reallocation toward European equities, driven by expectations of a more constructive macroeconomic backdrop heading into 2026. The Eurozone economy showed modest resilience despite external pressures, particularly from elevated geopolitical uncertainties. Inflation edged up slightly to 2.2% in September, surpassing the European Central Bank's (ECB) target for the first time since April. Nevertheless, core inflation remained stable, prompting the ECB to pause its rate-cutting cycle, leaving the deposit rate at 2.15%.

Emerging markets outpaced many developed market regions (+9.88% for the quarter and +25.95% year-to-date as measured by the MSCI EM IMI), aided by strength in China and a weaker U.S. dollar. Chinese equities gained (+20.99% for the quarter and +42.45% year-to-date as measured by MSCI China IMI). The rally was driven by easing trade tensions with the U.S., policy support for domestic consumption, and a surge in AI-related investments. Chinese tech stocks, particularly in the semiconductor and internet sectors, saw gains. However, macroeconomic challenges persisted, including ongoing weakness in retail sales momentum. Despite these headwinds, industrial production remained resilient. Latin America returns advanced (+9.75% for the quarter and 43.43% year-to-date as measured by the MSCI EM Latin America IMI) with strength from Mexico and Brazil. EMEA was also positive (+8.23% for the quarter and 24.18% year-to-date as measured by the MSCI EM EMEA IMI), with strength from South Africa and Saudi Arabia.

Performance

3Q 2025

The William Blair International Leaders ADR SMA Strategy (net of fees) underperformed its benchmark, the MSCI ACWI ex US IMI index during the third quarter and underperformed year to date.

The quarter can be characterized by strong risk-on behavior, and the strategy's philosophy of investing in high-quality companies with strong and stable fundamentals was a headwind as market leadership was in lower-quality, higher-beta companies. This headwind resulted in weaker selection across most sectors during the quarter, most notably within consumer discretionary, financials, and materials. The strategy's sector allocation was slightly positive, with an overweight to consumer discretionary and underweight to consumer staples adding value but an underweight to materials detracting. The strategy's regional allocation was negative due to an overweight in Europe and underweight to emerging Asia.

Within consumer discretionary, the strategy was negatively impacted by not owning Alibaba, as well as underperformance of portfolio holdings MercadoLibre and Flutter Entertainment. MercadoLibre (MELI) is the largest e-commerce player in Latin America. MELI's stock has been strong year-to-date but was effectively flat in a quarter of strong equity market performance. Recent quarterly results had a slight miss on earnings, but this was driven largely by investments previously flagged by management. Specifically, its free shipping initiatives and additional marketing spend were communicated several times to the market. Our focus is on the sustained growth of gross merchandise value across geographies, which supports evidence of share gains rather than a deterioration in competitive positioning in the market.

Flutter is a sports betting and igaming company with a global presence, including FanDuel in the United States and Sky Betting and Paddy Power in the U.K. Competitive pressures are rising from Kalshi, whose product offering is improving and without clear U.S. regulation that would limit this type of competition. Robinhood is also working with regulators on how prediction markets (betting on outcomes) may be classified across geographies. While Flutter still has a dominant position today, the disruption risk is rising, and the stock has underperformed as a result.

Partially offsetting this was strong performance from Trip.com. Chinese equities outperformed in the quarter and Trip.com was a standout after a strong and clean earnings quarter. Revenue mildly beat, margins expanded to 31% on significantly lower sales-and-marketing costs, and the upside surprise was a share buyback announcement.

Financials stock selection was negative due to holdings in London Stock Exchange and Deutsche Börse. London Stock Exchange (LSE) is a best-in-class diversified global market infrastructure and data company. The stock price has been weak this year as the market believes that LSE will be negatively impacted by AI, like many other data and software companies. Uncertainty can put multiples at risk, but we are not convinced that LSE is indeed negatively impacted by AI given its significant moats that are wide enough to defend the business or perhaps make LSE an AI beneficiary.

Deutsche Börse AG provides a variety of stock exchange introduction, trading, and operational services to institutions and private investors. The company offers electronic trading systems for buying and selling of securities on stock exchanges in Europe. The exchange reported two straight quarters of lackluster results and full-year guidance was reiterated, while analysts were expecting an increase. Given this earnings deterioration, we exited the position and favor current holdings of London Stock Exchange and Hong Kong Exchange.

Selection within materials was negative, primarily because of the absence of metals and mining companies within the portfolio. Given the strength of gold, silver, and other precious metals, this industry has been very strong and was up 30% in the quarter.

Healthcare selection was positive, primarily due to a position in UCB. UCB is leading biopharmaceutical company focused on patients with severe chronic diseases in areas such as immunology, neurology, and rare diseases. High growth is anticipated for its drug Bimzelx, which is used to treat inflammatory diseases. The strength in the stock during the quarter was largely due to a competitor drug to Bimzelx doing poorly in trials, cementing Bimzelx's competitive advantage and increasing the potential demand for the drug in the future.

Positioning

During the quarter, exposure to information technology was increased and includes new purchases of Disco Corp. and Nomura Research Institute. Disco sells semi equipment used in dicing and polishing of semi wafers, part of the manufacturing process to make chips. Along with the equipment, Disco sells consumables (blades and chemicals) used in its machines to do the actual cutting and polishing. Disco is a beneficiary of the AI buildout as part of the semiconductor supply chain.

Nomura Research Institute (NRI) is a leading provider of consulting services and IT solutions, primarily serving financial institutions, government agencies, and corporations across Japan and internationally. Japan is behind on cloud adoption and digitalization, with spending picking up post-COVID, supporting sustained midterm investment. AI adoption is in early stages and disruption at scale is expected. We believe that NRI will benefit from this digitization and AI adoption, with margins improving.

Healthcare was reduced through sales of Chugai Pharmaceutical and Hoya Corp. The primary thesis for owning Chugai was its partnership with Eli Lilly on the next generation of its GLP-1 drug. During the quarter, results of a trial for the drug were shared and came in below expectations, with a 12.5% weight reduction for members of the trial, compared to the expectation of 15%. This negative trial reduces the outlook for Chugai's royalty payments.

Hoya is a Japanese multinational specializing in advanced optics and medical technologies. Its core businesses span healthcare, electronics, and information technology, including vision care, medical endoscopy, optical filters and lenses, and laser and photonics equipment. Given Hoya's exposure to the tech sector, the position was exited since we were increasing tech sector exposure as we prefer those names relative to the growth profile of Hoya.

Outlook

In continuation of the broad-based growth seen throughout 2025, public equities delivered strong performance in the third quarter of this year. Developed markets were up some 7.4%, with Japan and Canada leading the charge and delivering 8.3% and 10.6%, respectively. In contrast to the first half of the year, U.S. equities roared back with returns in excess of 8%.

However, strong performance was not confined to only large caps in developed markets. For almost the first time in what seems like years, small-cap stocks kept pace with their large-cap brethren. China, Taiwan, and South Africa continued to post strong performance, gaining 20.9%, 14.1%, and 10.7%, respectively. Notably, Chinese equities continued to surge, up over 42% year-to-date, with key outperformers linked to AI-linked companies and biotech, reflecting investor confidence in China's structural shift toward innovation and high-value industries.

Yet conventional factor analysis of the underlying performance consistently flags that both quality and growth continue to underperform value. It seems paradoxical to suggest that broadening and strengthening economic growth results in relative underperformance of growth as a factor.

This contradiction melts away on closer inspection. The MSCI value index assesses a security's price/book value, forward earnings/price and dividend yield to evaluate its inclusion in the index. Unsurprisingly, financials stocks account for nearly a third of the value index by weight. For much of the 2010s, global growth was anemic, interest rates were low and real rates were outright negative in many places. Financials companies, which rely on the interest rate spread, economic activity, and credit growth, delivered uninspiring returns and were shunned by investors. They became inexpensive, with no improvement optionality priced in.

Over the past several years, economic growth has broadened and the growth wedge between the U.S. and other major economies began to shrink, as we discussed in last quarter's outlook, "[Policy Reactions Narrow Global Growth Gaps](#)." Interest rates have risen across the developed markets on the back of COVID-related inflationary supply disruptions; there is a focus on growth in Europe and Japan, and banking stocks from these jurisdictions have delivered significant returns to their investors. In other words, improvement in economic growth translates into earnings improvement for many companies in the value index.

More broadly, a key pillar of Japan's corporate governance reform effort is to "name and shame" companies whose market value is below book value. Specifically, since January 2024, the Tokyo Stock Exchange has published a monthly list of companies that have disclosed information regarding their capital efficiency initiatives to improve overall capital allocation and raise return on equity for Japanese companies. As more and more companies succeed in improving their capital allocation and migrating to higher-growth end-markets, we believe they offer rich investment opportunities for the skilled investor. And they are largely in the value indices.

Just as growth remains highly dynamic, so are the indices. When examining the composition of the broad indices, whether MSCI or Russell, we found that the constituents of the growth and value indices change regularly. In the past two decades, we have seen that 75% of the constituents change back and forth between growth and value, rendering little merit in paying attention to the index when searching for where growth is inflecting.

As quality growth investors, we continue to look for growth and where it is changing, and we continue to find much to be excited about. We have written extensively about European and broader defense and it continues to be a rich growth area, as discussed on "Mapping the Future of EU Defense Spending." While Russia's invasion of Ukraine in early 2022 catalyzed the performance of defense stocks, the sector wide re-rating has likely played out. Now, it is over to those with earnings power that can deliver.

As ever, defense remains at the technological frontier. Today, it means remotely operated equipment such as drones, which relies on ubiquitous and secure connectivity. Needs drive innovation, and we see tremendous activity in the buildout of low(er)-Earth-orbit satellite constellations capable of providing low-latency connectivity over transregional and transcontinental distances. For now, companies are building out the infrastructure—such as reusable rockets and engines—and satellite constellations necessary to deliver on this vision in the next handful of years. Over time, ubiquitous connectivity and surveillance will likely for example enable entirely new businesses in autonomous transport, banking, and healthcare delivery.

The AI buildout continues to pressure power generation demand in markets where electricity demand has not accelerated in years. As a consequence, there is ample growth opportunities for power providers, utilities and all those industrials that are involved in producing power, converting it into electricity and delivering it securely to the end-consumer.

As ever, improving growth translates into stronger earnings streams, which at times are underappreciated. Asset price appreciation is the result, whether a company is classified in a value or growth index. This constant quest for improvement is at the core of what we do.

Composite Performance (%)	Qtr	YTD	1 Yr	Annualized				Since Inception (Jan 1 03)
				3 Yr	5 Yr	10 Yr		
International Leaders ADR SMA (Gross of fees)	3.45	19.47	10.59	18.15	6.02	8.05		8.00
International Leaders ADR SMA (Net of fees)	2.68	16.86	7.35	14.69	2.89	4.87		4.83
MSCI AC World ex-US IMI Index	6.86	25.97	16.39	20.50	10.22	8.24		8.16
MSCI EAFE Index	4.77	25.14	14.99	21.70	11.15	8.17		7.64

https://williamblair.com/~media/Downloads/IM/Composite_Disclosures.pdf

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Index

The MSCI AC World ex-US Investable Market Index (IMI) Net is a free float-adjusted market capitalization index that is designed to measure equity market performance in the global developed and emerging markets, excluding the U.S. It is not possible to directly invest in an unmanaged index.

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