HARDING LOEVNER

EMERGING MARKETS EQUITY

2019 Third Quarter Report

COMPOSITE PERFORMANCE (% TOTAL RETURN) FOR PERIODS ENDED SEPTEMBER 30, 2019[1]

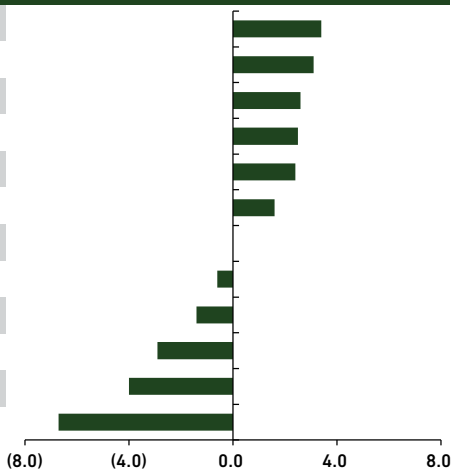
	3 MONTHS	YTD	1 YEAR	3 YEARS[2]	5 YEARS[2]	10 YEARS[2]	SINCE INCEPTION[2,3]
HL EMERGING MARKETS (GROSS OF FEES)	-3.15	12.58	1.70	6.90	4.34	6.44	12.22
HL EMERGING MARKETS (NET OF FEES)	-3.37	11.83	0.78	5.96	3.44	5.49	11.31
MSCI EMERGING MARKETS INDEX (GROSS)[4,5]	-4.11	6.22	-1.63	6.37	2.71	3.72	8.71

[1]The Composite performance returns shown are preliminary; [2]Annualized Returns; [3]Inception Date: November 30, 1998; [4]The Benchmark Index; [5]Gross of withholding taxes.

Please read the above performance in conjunction with the footnotes on the last page of this report. Past performance does not guarantee future results. All performance and data shown are in US dollar terms, unless otherwise noted.

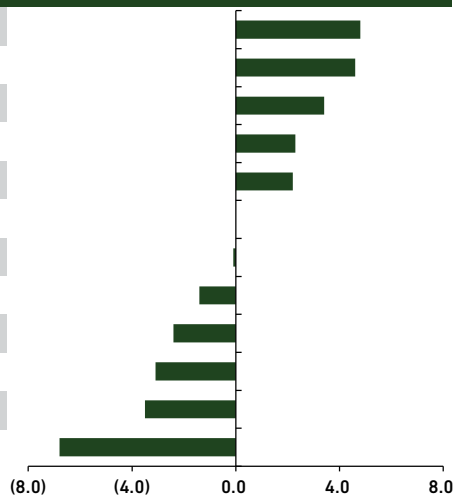
SECTOR EXPOSURE (%)

	HL EM	MSCI EM
CASH	3.4	—
INFO TECHNOLOGY	18.2	15.1
FINANCIALS	27.3	24.7
CONS DISCRETIONARY	15.5	13.0
CONS STAPLES	9.3	6.9
INDUSTRIALS	7.0	5.4
ENERGY	7.7	7.7
UTILITIES	2.2	2.8
HEALTH CARE	1.2	2.6
REAL ESTATE	0.0	2.9
COMM SERVICES	7.6	11.6
MATERIALS	0.6	7.3



GEOGRAPHIC EXPOSURE (%)

	HL EM	MSCI EM
DEVELOPED MARKET LISTED[6]	4.8	—
RUSSIA	8.6	4.0
CASH	3.4	—
FRONTIER MARKETS[7]	2.3	—
MEXICO	4.7	2.5
BRAZIL	7.5	7.5
CHINA + HONG KONG[8]	31.8	31.9
SOUTH AFRICA	3.3	4.7
INDIA	6.5	8.9
SOUTH KOREA	9.0	12.1
TAIWAN	8.0	11.5
SMALL EMERGING MARKETS[9]	10.1	16.9



[6]Emerging markets or frontier markets companies listed in developed markets, excluding Hong Kong; [7]Includes countries with less-developed markets outside the Index; [8]The Harding Loevner Emerging Markets Model Portfolio's end weight in China is 25.4% and Hong Kong is 6.4%. The Benchmark does not include Hong Kong; [9]Includes the remaining emerging markets, which individually, comprise less than 5% of the Index.

Sector and geographic allocations are supplemental information only and complement the fully compliant Emerging Markets Composite GIPS Presentation.

Source: Harding Loevner Emerging Markets Model; MSCI Inc. and S&P. MSCI Inc. and S&P do not make any express or implied warranties or representations and shall have no liability whatsoever with respect to any GICS data contained herein.

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MARKET REVIEW

Emerging Markets (EMs) fell sharply in late July and early August amid escalating US-China trade tensions and signs of a global slowdown but recovered to end the quarter only modestly lower as governments and central banks acted to stimulate their economies. Dropping 4%, the MSCI EM Index lagged developed markets by five percentage points.

The whiplash-inducing US-China trade war continued. The quarter started on an optimistic note when the White House lifted its ban that prevented US companies from doing business with Chinese communications equipment giant Huawei. Then in late July, President Donald Trump tweeted his frustration over China not buying as many US agricultural goods as it had promised. Within days, he announced 10% levies on an additional US$300 billion worth of Chinese goods not previously covered by tariffs. Global stock markets fell sharply, as did the Chinese currency, which weakened past the 7-yuan-to-the-dollar level for the first time in more than a decade. Although the modest 2.4% depreciation matched the declines of most European currencies against the US dollar in prior weeks, China was excoriated by the Trump administration. The US Treasury Department labeled China a "currency manipulator," setting the stage for possible further sanctions against the country. In September, however, Trump delayed the latest tariff hikes until mid-October, after China's national holiday celebrating 70 years of Communist Party rule. He postponed them again on October 11, after negotiators made purported progress toward a deal.

The trade war weighed on global economic growth. In September, the OECD cut its 2019 forecast for global economic growth to the slowest rate in a decade, citing the impact of the US-China dispute on global trade and capital investment. China's economy grew at a rate of only 6% in the second quarter, the slowest rate in nearly three decades. In India, the second-quarter GDP growth rate was just 5%, the lowest in six years.

In a shock for energy markets, both real and financial, a drone and missile attack on Saudi Arabia's largest oil production facility at Abqaiq disrupted nearly half of the kingdom's oil output and at least 5% of global oil production. Oil prices soared as much as 20% in the immediate aftermath of the attack, and many prognosticators predicted high oil prices for the foreseeable future. However, the resilient global energy supply chain responded while rapid repairs to the facilities proceeded, with the result that oil prices fully corrected, closing 7% *lower* for the quarter as demand slackened.

As growth in China and other key EMs decelerated, business results in the Information Technology (IT) sector proved resilient. The sector rose 6%, outpacing developed-market IT sector shares. The giant Taiwanese semiconductor manufacturer **TSMC** issued better-than-expected forward guidance, citing robust demand for its logic chips from smartphone manufacturers. The rollback of US hostilities against Huawei and Apple's launch of new iPhones featuring more cameras and lower entry-level pricing supported the stocks of companies in the smartphone value chain. The main beneficiaries were manufacturers of lenses and camera modules, like **Largan Precision** and **Sunny Optical**. Consumer Discretionary and Staples also outperformed the overall index but saw a wide divergence in returns across countries.

Materials was the worst-performing sector, falling 11%, with weak performance from steel producers and Asian petrochemical companies due to dimming global growth prospects. **Sasol**,

MARKET PERFORMANCE (USD %)

REGION/COUNTRY	3Q 2019	TRAILING 12 MONTHS
AFRICA	-10.9	-4.1
SOUTH AFRICA	-11.4	-4.7
ASIA	-3.3	-3.5
CHINA	-4.7	-3.8
INDIA	-5.2	4.7
SOUTH KOREA	-4.5	-13.3
TAIWAN	5.9	0.7
EUROPE	-2.3	11.1
RUSSIA	-0.9	19.4
LATIN AMERICA	-5.6	7.2
BRAZIL	-4.5	25.8
MEXICO	-1.6	-14.5
MIDDLE EAST	-5.2	-0.6
MSCI EM INDEX	-4.1	-1.6

SECTOR PERFORMANCE (USD %)
OF THE MSCI EM INDEX

SECTOR	3Q 2019	TRAILING 12 MONTHS
COMMUNICATION SERVICES	-5.1	-5.9
CONSUMER DISCRETIONARY	-2.8	1.4
CONSUMER STAPLES	-0.8	3.3
ENERGY	-3.7	-1.5
FINANCIALS	-7.8	2.1
HEALTH CARE	-6.6	-24.2
INDUSTRIALS	-5.1	-4.2
INFORMATION TECHNOLOGY	5.9	1.5
MATERIALS	-10.5	-15.4
REAL ESTATE	-8.7	7.1
UTILITIES	-3.5	6.5

Source: FactSet (as of September 30, 2019). MSCI Inc. and S&P.

Companies held in the portfolio during the quarter appear in bold type; only the first reference to a particular holding appears in bold. The portfolio is actively managed therefore holdings shown may not be current. Portfolio holdings should not be considered recommendations to buy or sell any security. It should not be assumed that investment in the security identified has been or will be profitable. To request a complete list of holdings for the past year, please contact Harding Loevner. A complete list of holdings at September 30, 2019 is available on page 10 of this report.

a South African energy and specialty-chemicals company, disappointed shareholders once again with news that the ramp-up of its Louisiana cracker plant is further delayed. Financials in most large EMs fell sharply as investors feared rising credit costs amid weakening economic prospects. Real Estate also declined, as tightening credit conditions in China reduced the outlook for new housing starts.

All EM regions posted negative returns for the quarter. The best performer was Europe, which fell just 2% thanks to Turkey's nearly 12% return. In September, the country reported lower-than-expected inflation, which should allow its central bank to cut interest rates further. Other recent economic figures indicated some recovery in domestic demand.

Africa was the weakest region, dragged down by further weakness in South Africa (-11%) and despite positive returns in Egypt (+7%), where accelerating revenues from gas exports and a resurgence in tourism have supported the pound. South Africa faces a formidable challenge to check its mounting fiscal deficit. Amid a depressed growth environment, the government is expected to continue spending heavily to support the national electricity utility, Eskom, and other stressed state-owned companies. In addition, a prolonged drought has withered agricultural production, and labor strikes have hurt other core industries.

In Asia, seven of the nine countries in the index fell as weakening global growth and trade disputes loomed. In the first half of the quarter, India's market fell sharply in reaction to evidence of growth deceleration and fragility within the country's financial system. Prime Minister Narendra Modi's recently re-elected government responded with a series of stimulative policies, including a significant corporate tax cut. IT heavyweight Taiwan was the only major Asian country to post a positive return (+6%).

Though Argentina represents only a tiny portion of the MSCI EM Index, it figured large—yet again—as a cautionary tale of the danger of dependence on external financing. Reformist President Mauricio Macri appeared to be making progress toward ending the cycles of excessive foreign borrowing, crisis, and default that stretch back nearly two centuries. When he suffered a surprising defeat in August's primary elections—a sure sign he will lose October's presidential election—investors were alarmed. The Argentine stock market plummeted nearly 50% in US dollar terms, and the peso lost over 25% of its value against the dollar. Stoking investors' worst fears, Macri sought to delay debt payments as the country once again teetered on the edge of default.

EM currencies weakened against the US dollar, with the Brazilian real, the South African rand, and Eastern European currencies depreciating significantly. The return of the dollar-denominated EM index now lags that of the local currency version by nearly 2% year to date.

Returns to style factors were volatile during the quarter. Overall, high-quality, highly priced stocks outperformed, whereas there was no clear impact from the growth style factor.

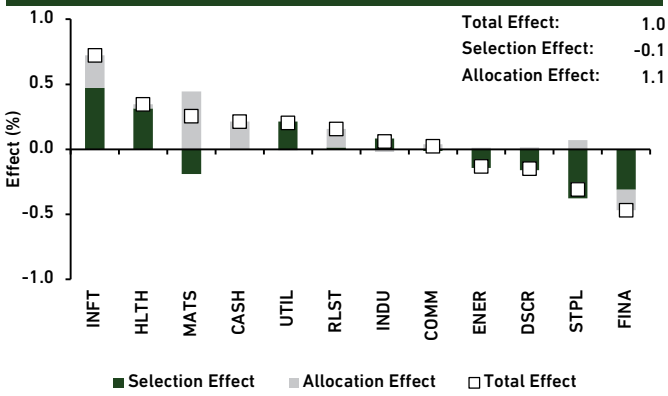
PERFORMANCE AND ATTRIBUTION

The Emerging Markets composite fell 3.2% in the quarter, outperforming the 4.1% decline of the MSCI EM Index. For the year to date, the composite rose 12.2%, nearly double the return of the benchmark. The charts below attribute the quarter's performance by sector and region.

The strong performance of high-quality stocks contributed to our returns this quarter. Our underweight to Materials and overweight to IT were also helpful, as was good stock selection in IT and Health Care. In IT, shares of smartphone camera-equipment manufacturers Sunny Optical of China and Largan Precision of Taiwan rose in response to rising demand from makers of premium smartphones. The increase was partly spurred by the launches of new phones, including Apple's

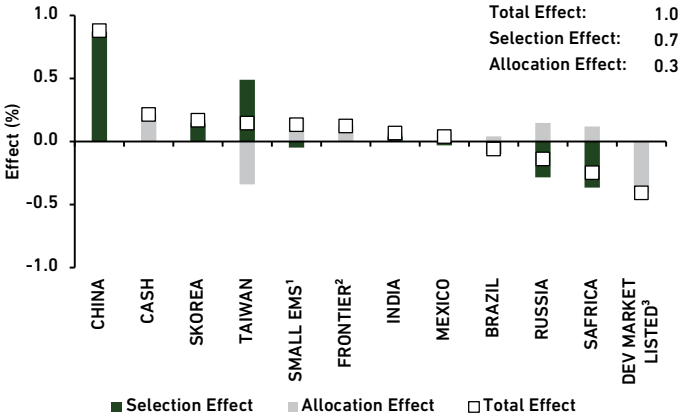
SECTOR PERFORMANCE ATTRIBUTION THIRD QUARTER 2019

EMERGING MARKETS COMPOSITE VS. MSCI EM INDEX



GEOGRAPHIC PERFORMANCE ATTRIBUTION THIRD QUARTER 2019

EMERGING MARKETS COMPOSITE VS. MSCI EM INDEX



[1]Includes the remaining emerging markets, which individually, comprise less than 5% of the Index; [2]Includes countries with less-developed markets outside the Index; [3]Emerging markets or frontier markets companies listed in developed markets. Source: FactSet; Harding Loevner Emerging Markets Composite; MSCI Inc. and S&P. The total effect shown here may differ from the variance of the Composite performance and benchmark performance shown on page 1 of this report due to the way in which FactSet calculates performance attribution. This information is supplemental to the Composite GIPS presentation.

iPhone 11 Pro, which incorporate advanced cameras requiring high-specification lens sets. Hong Kong-based semiconductor equipment maker **ASM Pacific Technology** rose after chip foundry TSMC issued stronger-than-anticipated guidance for the second half of the year. Our Chinese Health Care holdings **CSPC** and **Sino Biopharmaceuticals** rose after they reported continued strong revenue growth.

Financials and Consumer Staples stocks detracted from our relative returns. **Hong Kong Exchanges** and Hong Kong-listed insurer **AIA Group** were both weak as protesters brought the city to a standstill at times. In South Africa, shares of the insurer **Discovery Holdings** sold off after the government announced a preliminary plan to develop a universal health insurance program over the course of the next seven years. Under the program, private medical schemes like those administered by Discovery would be limited to covering services not provided by the public system. We think the impact on Discovery's business will be less than initially feared, because the government's fiscal position is challenged and the basic public plan it can afford won't satisfy the growing demand for quality health care.

Shares of Brazilian Financials, including **Itaú Unibanco** and **Banco Bradesco**, declined as the country's GDP growth projections for this year fell from above 2% to below 1%, and corporate loan books continued to shrink. Investors are also worried about the rising threat of new digital banks, which are rapidly adding customers. The new entrants, unencumbered by the costs of running a network of physical branches, offer low-priced and efficient, yet limited, banking services. Itaú and Bradesco are reducing their physical footprints and headcounts as they, too, improve their digital offerings.

In Consumer Staples, Brazilian convenience store operator **Pão de Açúcar (CBD)** reported its margins declined from the all-time high reached in the second quarter due to increased promotions at its big-box stores. Shares of **Amorepacific**, a Korean cosmetics company, dropped after it failed to deliver its promised improvement in profit margins as sales growth in China continued to stall despite rising marketing costs.

By region, our performance was boosted by our lack of exposure to both Saudi Arabia and Argentina as well as our overweight to Russia. Positive stock selection from holdings in China (Sunny Optical, **ENN Energy**, **Hangzhou Hikvision**) and Taiwan (TSMC) contributed the most to relative returns. Hikvision, a leading global manufacturer of surveillance equipment, reported second-quarter revenues rose 20% year-over-year, beating market expectations. Negative selection effects came from South Africa (Discovery, Sasol) and Russia (**Sberbank**). Our underweight to the strong Taiwanese market also detracted.

PERSPECTIVE AND OUTLOOK

Over the past 20 years, economic progress has played out well in some EM countries (notably China and South Korea), while in others it has been retarded by poor policies or plain bad luck. Some countries have failed to implement policies fostering competitive and dynamic business environments. Others have failed to adapt their economies to take advantage of globalization and the resulting new opportunities to participate in cross-border supply chains. As a result, many EM economies are still tethered to the boom-and-bust of the commodity cycle.

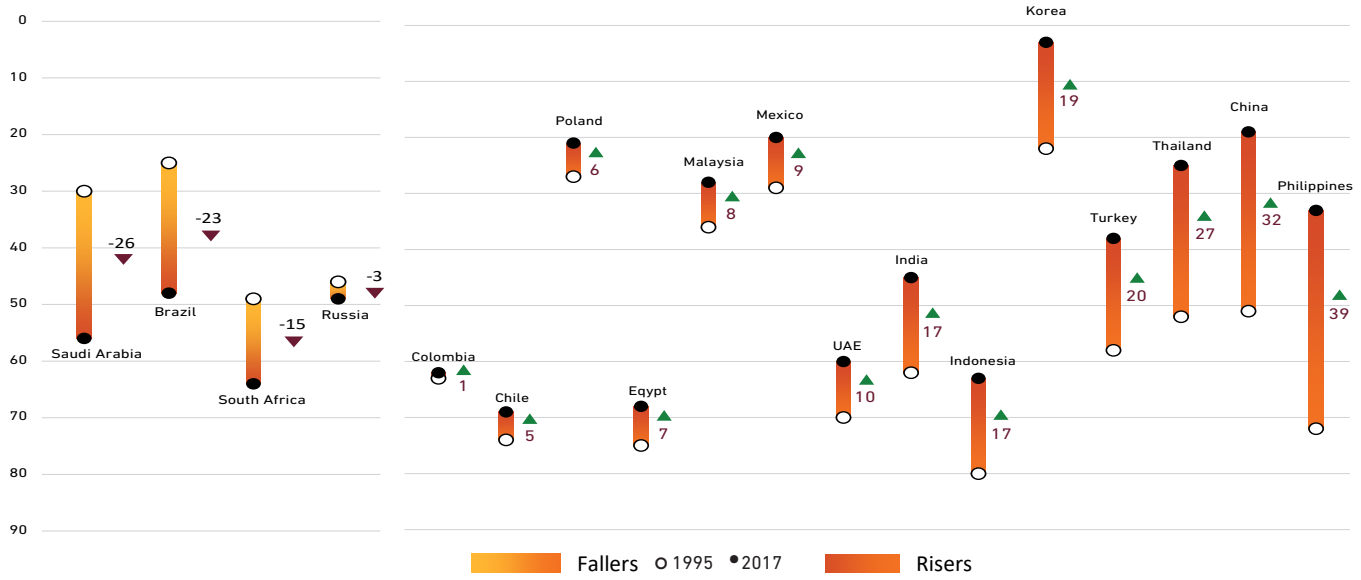
Our experience has shown us and academic studies confirm that, over short horizons, a country's economic growth rate is at best weakly correlated to the returns of its stock market, and that economic growth forecasts are of little value in trying to predict equity market returns. That is why we do not spend our time trying to forecast GDP growth rates. We think working to achieve a deep understanding of companies' business models and their competitive positions within their industries is a more productive pursuit because high-quality, growing *companies* are to be found in faster-growing and slower-growing emerging economies alike.

That is not to say, however, that a company's growth prospects are independent of the conditions of the countries in which it operates. A more subtle measure of economic conditions than GDP growth rate, and one that we find particularly thought-provoking, is the Economic Complexity Index (ECI), created by the economists Ricardo Hausmann of Harvard University and César Hidalgo of the Massachusetts Institute of Technology. For more than a decade, they have been refining the ECI as a way to assess a country's progress in economic development based on the breadth and sophistication of its exports. Countries that export a more diverse range of products than other countries are more economically complex and have a higher ECI score. Exporting products that are produced by few other nations is a further sign of economic complexity meriting a higher score.[1] Hausmann and Hidalgo found evidence that countries with higher levels of economic complexity relative to others at their level of per-capita income grow their economies at a faster and more sustained rate.

The ECI is interesting to us because it represents a framework for describing economic development that aligns with our industry-focused approach to identifying investment opportunities. Increasing complexity in manufacturing and services attests to a history of good capital allocation decisions, an increasingly educated workforce, and a growing base of companies with characteristics desired by investors such as us. As economies become more complex, they are rewarded with faster and more sustainable economic development, in a virtuous circle of ever-increasing complexity. Incomes rise, fostering the growth of the middle class, which becomes itself an important incremental source of demand. Companies adapt and new companies emerge to meet the new demands and tastes of the increasingly educated and affluent population.

[1]The *Atlas of Economic Complexity* website maintained by Harvard University provides striking visualizations of the ECI data: http://atlas.cid.harvard.edu/.

BIGGEST RISERS AND FALLERS IN ECONOMIC COMPLEXITY INDEX, SELECTED EM COUNTRIES



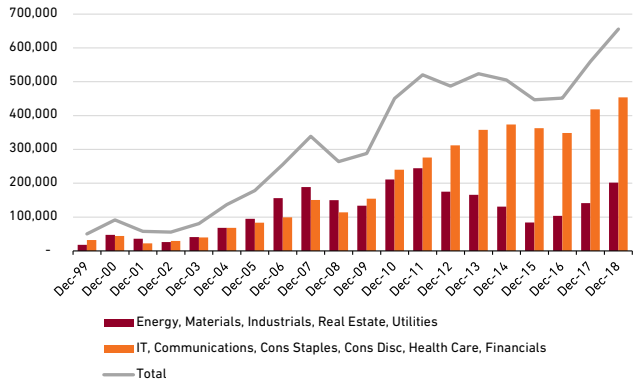
Source: http://atlas.cid.harvard.edu/growth-projections

The ECI figures confirm that most EM countries—and by extension, their companies—are no longer simply suppliers of natural resources and the manufactured output of inexpensive labor. In some developing countries, global technology leaders have arisen to replace low-tech, labor-intensive manufacturers. China, the largest EM, has moved from the fifty-first most complex nation in 1995 to the nineteenth in 2017 as it has increased the diversity and sophistication of its export basket (see chart above). South Korea, Thailand, and other Asian countries whose manufacturers are highly embedded within global supply chains have also progressed—indeed, Korea is ranked third in ECI behind only Japan and Switzerland. But the traditional image of EMs as producers of basic materials is not yet entirely inaccurate. The list of countries where ECI status has stagnated or regressed over this period includes several countries such as Brazil, Peru, Colombia, and South Africa whose economies remain commodity oriented. The commodity boom of 2003–2011 did little to incent progressive policymaking in these countries aimed at increasing economic diversity.

Though informative, the ECI does not paint a complete picture of where attractive investment opportunities can be found. Based mainly on export (product) data, it misses the full extent of industrial advances being made through the increased use of technology, such as the digitization of operations, to create high-returning, durable-growth, domestic businesses. Fundamental, bottom-up research can identify champions of local industries that are not reliant on global trade to sustain their businesses. Brazil is a case in point: the country has stalled in its ECI progression with its export mix still dominated by basic materials such as soybeans and (admittedly premium grade) iron ore. However, Brazilian financial institutions like Banco Bradesco have embraced new technologies to launch digital banks that are providing payment and banking services that are reaching an increasing percentage of the country's previously unbanked population. Advanced real-time data analytics are being adopted by fashion retailers, beverage companies, and other industries to create efficiencies in supply chains and improve customer engagement and service. E-commerce platforms are using technology to overcome Brazil's still-wretched logistics infrastructure to optimize distribution and delivery resources with Uber-like apps that secure last-mile couriers, in order to provide products in a timely fashion. These developments echo the growth of online businesses we have witnessed in China over the past decade, and they are happening across most EMs.

The changing earnings base of industries provides another industry-centric view of countries' economic development. The chart below depicts the aggregate earnings (net income) of index companies within slower-growing sectors, dominated by Energy and Materials. The earnings in these sectors peaked in 2011 at roughly US$240 billion and at the time contributed nearly

MSCI EM INDEX: NET INCOME BY SECTOR (US$)

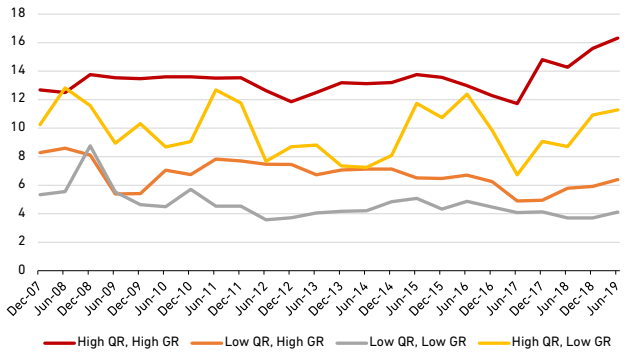


Source: FactSet, MSCI Inc. Data as of December 31, 2018.

70% of non-financials EM earnings. This proportion fell to a low of 40% in 2015 before rebounding modestly to 50% last year. Contrast this earnings pattern with that of "growth" sectors in EMs. Led by technology and recently reclassified Communication Services companies, these sectors have grown their earnings base strongly over the last ten years, and almost tenfold over the previous 20 years.

The rising complexity of economies and the shifting earnings base of industries reflect the increasingly diverse opportunity set of EM companies. Today, EMs provide the ingredients for a more robust portfolio than was the case 20 years ago. Moreover (and this is of particular interest to us), out of the more than 500 companies that rank in the top 25% in terms of quality and growth worldwide, currently nearly a third are based in EM countries. The cash flow return on investment (our preferred measure of return on capital) for these companies has also been rising over the past few years (see chart below).

WEIGHTED-MEDIAN CFROI BY QUALITY RANK (QR) AND GROWTH RANK (GR)



Source: FactSet, Holt, MSCI Inc. Data as of June 30, 2019.

Harding Loevner's Quality and Growth rankings are proprietary measures determined using objective data. Quality rankings are based on the stability, trend, and level of profitability, as well as balance-sheet strength. Growth rankings are based on historical growth of earnings, sales, and assets, as well as expected changes in earnings and profitability.

PORTFOLIO HIGHLIGHTS

We seek to identify businesses with enduring competitive advantages within industries with favorable characteristics. When their shares' valuations are attractive, we buy them, and then hold onto them so long as they remain at least reasonably valued so that our clients can benefit over time from the compounding of these businesses' superior returns on capital. We strive to keep our focus on our holdings' long-term business prospects, knowing that overreacting to transient developments and their associated share-price movements can hurt returns over time. If the share price falls but the quality and long-term growth prospects remain strong, we will often add to the position.

There are only a few reasons that we think justify selling a position: a breakdown of the thesis underlying our investment, or an elevated share price no longer justified by a company's growth prospects relative to alternatives available within our stable of qualified companies. We also may trim or sell a position to reduce portfolio-level risk. During the quarter, we completed five sales, an unusually high number for our strategy. Each of these sales illustrates a different aspect of our sell discipline.

A Broken Growth Thesis

In 2010, we bought **Aspen Pharmacare**, believing the South African pharmaceutical company would find growth through its strategy of acquiring older patented drugs and expanding their sales to developing countries through its distribution network. Aspen also claimed that it could produce the drugs at a lower cost than the previous owners thanks to its efficient production.

The thesis proved overly optimistic. Continued pricing pressure in developed markets more than offset the additional sales in developing countries. Aspen also faced significant unexpected competitive pressure even before it could achieve scale. Sales growth and margins were negatively impacted, hurting cash-flow generation. Ultimately, the company was forced to negotiate with its creditors a temporary revision of its debt covenants. Despite the sale of some non-core assets, Aspen's ability to finance further acquisitions is limited, constraining a key growth engine of its business.

In July, we completed the sale of our remaining position in the company due to deterioration of its financial strength and loss of confidence in its long-term growth prospects. In retrospect, we held too much faith in management, and should have acted sooner.

Trust in Management Undermined

We sold half of our position in **Han's Laser** in the second quarter following a sharp rise in the company's stock. Our decision was made in the context of some concerns over the potential impact of the trade war on the Chinese manufacturer of low-power lasers. We were also worried about weak iPhone sales (Han's is a major supplier to Apple). This quarter we sold the remainder of our shares for an entirely different reason: management dishonesty. In early July, reports surfaced in the media of the company's spending on a European "R&D center," which turned out to be more of a five star R&R resort. In a conference call, executives denied misleading investors, even though there was no hint of the project's true nature in the company's financial disclosures. Disappointed by their lack of transparency and dissembling, we felt we could no longer trust management to look after the interests of shareholders.

Heightened Rivalry

Our investment thesis in Hong Kong Exchanges (HKEX) was based on its prime position to participate in the gradual opening of China's financial markets. Broadly, this has been playing out as expected. Revenues were boosted by the suc-

cessful launch of the "Connect" system that links the equity exchanges of Hong Kong with Shanghai and Shenzhen. However, we foresee rising competitive challenges from the local Chinese exchanges, which are increasingly pursuing initiatives to link directly with foreign investors via the London Stock Exchange (LSE). The launch in China of the "Science and Technology Innovation Board" (or STAR market)—a less-regulated equity market for startup businesses similar to the NASDAQ in the US—has also increased the competition for new listings of the most attractive businesses.

HKEX's unsuccessful bid to acquire LSE during the quarter was an indication that its organic growth prospects are becoming restricted. To support future product growth, HKEX needs to make further investments in its IT systems and customer-facing platforms so that it can compete more effectively than its rivals for global capital flows. As competitive and growth challenges rise, we became less tolerant of the stock's relatively expensive valuation, particularly when compared with other EM financials.

Valuation Concern

Raia Drogasil, the leading Brazilian drugstore operator, lowered the prices of generic drugs to capture a bigger share of the prescription market. The price cut in the second half of 2018 ignited sales growth and highlighted the relative weakness of key competitors, some of whom were forced to cut back expansion plans as a result. Same-store sales and operating leverage improved, allowing margins to recover.

Raia Drogasil's shares had rallied strongly since the beginning of the year, taking their price well beyond our estimate of fair value. We continue to admire the competitive strengths of this business in a growing market, and we may reinvest if its valuation falls back to earth.

Rising Doubt About our Growth Thesis

Our sale of **Emaar Properties**, a UAE property developer, was triggered by our worry over the long-term growth prospects of Dubai's property market, which is being impacted by the net outflow of expats from the Middle East. Emaar continues to gain market share, but it has done so by extending more attractive financial terms to buyers. We fear the deals will erode its balance sheet over time.

Alongside our sales, we also purchased a new position in **Jiangsu Yanghe**, China's third-largest distiller of baijiu ("white spirits"). Yanghe's portfolio of brands, which include Dream Blue and Sea Blue, dominate China's "premium" liquor segment, with products priced between US$40 and US$90. Unlike other baijiu companies, however, Yanghe's brand management, marketing, and distribution practices are comparable to much larger multinational liquor companies. The sentiment is shared by Diageo, which has established a joint venture with Yanghe to sell scotch whiskey in China. We believe Yanghe is poised to grow its presence in China and increase its brand recognition in foreign markets.

In recent months, Yanghe's stock has lagged those of other Chinese Consumer Staples companies due to short-term concerns over deceleration in its sales growth. We took the opportunity to accumulate shares at what we perceive to be an attractive valuation level.

We also added to several positions in India. Stock valuations appeared more compelling following the government's recent move to reduce the corporate income tax rate. Additions include the bank **HDFC Corp**, IT service provider **Tata Consultancy Services**, automaker **Maruti Suzuki**, and **Kotak Mahindra Bank**.

Other additions to existing holdings include:

- **Ping An Insurance,** China's second-largest life and health insurer. The company reported strong second-quarter results in its core life insurance business. We believe the stock price continues to undervalue Ping An's long-term growth prospects.

- **Alibaba**, the Chinese e-commerce giant. The company's results have been resilient amid signs of a slowing Chinese economy. We thought its shares looked reasonably priced relative to peers.

- **Ambev**, a Brazil-based brewer. Its shares sold off recently due to economic deterioration in Argentina, a significant market for the company. Our analyst believes that Argentine beer consumption will be steady even if the economy continues to contract. He also has an increasingly positive view of the beer industry's competitive dynamics in Brazil, where a distribution agreement between Heineken and Coca Cola Femsa is likely to be terminated.

OUR APPROACH TO COMPANY ENGAGEMENT

By Jafar Rizvi, CFA

We recognize the value of communicating with companies on strategic issues including corporate governance as a means to improve returns to shareholders. We engage with companies in multiple ways beyond thoughtful voting of proxies. Whenever we vote against management's proxy proposals, we write to them to explain the basis of our disagreement. When appropriate, we follow up in one-on-one discussions with management. On occasion, when we think improvements in management incentives, corporate governance, or specific operational actions can lead to enhanced shareholder value, we write to the board directly.

Our engagement with South Africa-listed Naspers is illustrative. **Naspers** is an "interactive media" company with a diverse set of operations and strategic stakes in listed companies such as Chinese internet conglomerate Tencent, Russian social media company mail.ru, Germany's online food delivery service Delivery Hero, and Chinese online travel agency Ctrip. Naspers's operating businesses are primarily in similar areas: classifieds and e-commerce, digital payments, and food delivery. We have been Naspers shareholders since 2013 (in our Emerging Markets Equity strategy). While the shares have performed well, they have significantly lagged the outstanding returns of Naspers's single largest asset, its investment in Tencent. As a result, a large discount has opened between Naspers's market valuation and the market value of its stake in Tencent. At its widest, this valuation discount amounted to more than US$60 billion—value that we believed management and the board could and should do more to capture for Naspers's shareholders.

Management asserted at its investor day in December 2017 that the long-term solution to reducing the discount was to improve the profitability of the unlisted operating businesses. Executives also blamed investment flowing out of South Africa as a major contributor to the discount that was beyond their control.

We wrote to Naspers' board in May 2018, outlining our recommendations for closing the discount. This letter included a recommendation that the company tie executive compensation to improvements in the results of the operating businesses, using return on invested capital and free cash flow generation to measure their performance. We suggested converting to a single class of shares from the current dual-class structure, which effectively lets the Chairman Koos Bekker control the company despite owning only a small percentage. We also proposed some possible ways to narrow the valuation discount, including share buybacks, spin-offs of non-core businesses, and listing the shares outside South Africa to escape the limitations of its capital markets. And, finally, we requested that the board set milestones and a timeline toward the achievement of these objectives.

We have been pleased to see the company take meaningful action in line with our proposals. In its 2017 annual report published in July 2018, the board acknowledged the shareholder feedback, and described improvements made to management incentives, including a claw-back provision for bonuses. In early 2019, the company spun out its pay-TV business and announced the partial spin-off and listing in Amsterdam of **Prosus**. Prosus, a European investment holding company, owns the Tencent stake and all of Naspers's other internet-media businesses and strategic stakes except the South African ones. Naspers retains a 74% stake in Prosus for now.

As a result of these actions, the discount of Naspers's shares to its readily valued holdings (mainly the Tencent stake) has decreased by 15 percent. Gratified but not yet satisfied, we continue to press for conversion to a single class of shares.

EMERGING MARKETS HOLDINGS (AS OF SEPTEMBER 30, 2019)

SECTOR/COMPANY/DESCRIPTION	COUNTRY	END WT (%)
COMM SERVICES		
AUTOHOME Automotive information services	China	0.8
BAIDU Internet products and services	China	0.5
SAFARICOM Mobile network operator	Kenya	1.0
TENCENT Internet and IT services	China	4.3
WEIBO Social network	China	0.4
YANDEX Internet products and services	Russia	0.6
CONSUMER DISCRETIONARY		
ALIBABA E-commerce retailer	China	4.2
ASTRA INTERNATIONAL Auto business operator	Indonesia	0.7
COWAY Consumer appliances manufacturer	South Korea	1.0
CTRIP.COM Online travel services	China	0.5
ECLAT TEXTILE Technology-based textile manufacturer	Taiwan	1.3
HANKOOK TIRE Tire manufacturer	South Korea	0.9
JD.COM E-commerce retailer	China	0.4
MARUTI SUZUKI Automobile manufacturer	India	1.2
MIDEA GROUP Consumer appliances manufacturer	China	1.4
NASPERS Internet and media services	South Africa	0.7
PROSUS Internet and media services	Netherlands	0.3
SANDS CHINA Integrated resorts and casinos operator	Hong Kong	1.9
SHENZHOU INTERNATIONAL Textile manufacturer	China	1.1
CONSUMER STAPLES		
AMBEV Alcoholic beverages manufacturer	Brazil	1.4
AMOREPACIFIC Cosmetics manufacturer	South Korea	0.5
CBD Foods and consumer products retailer	Brazil	0.5
COCA-COLA HBC Coca-Cola bottler	UK	1.5
EAST AFRICAN BREWERIES Alcoholic beverages manufacturer	Kenya	0.2
FEMSA Beverages manufacturer and retail operator	Mexico	1.0
JIANGSU YANGHE BREWERY Alcoholic beverages mfr.	China	0.9
LG HOUSEHOLD & HEALTH CARE Cons products manufacturer	South Korea	2.0
WALMART DE MÉXICO Foods and consumer products retailer	Mexico	1.3
ENERGY		
CNOOC Oil and gas producer	China	1.4
LUKOIL Oil and gas producer	Russia	2.7
NOVATEK Natural gas producer	Russia	2.7
TENARIS Steel-pipe manufacturer	Italy	1.0
FINANCIALS		
AIA GROUP Insurance provider	Hong Kong	2.6
B3 Clearing house and exchange	Brazil	0.7
BANCO BRADESCO Commercial bank	Brazil	1.7
BANCO SANTANDER CHILE Commercial bank	Chile	0.5
BANCOLOMBIA Commercial bank	Colombia	1.2
BANK CENTRAL ASIA Commercial bank	Indonesia	1.1
BANK OF GEORGIA Commercial bank	UK	0.2
BANK RAKYAT Commercial bank	Indonesia	1.5
COMMERCIAL INTERNATIONAL BANK Commercial bank	Egypt	0.8
CREDICORP Commercial bank	Peru	1.2
DISCOVERY HOLDINGS Insurance provider	South Africa	0.8
GF BANORTE Commercial bank	Mexico	1.3
HDFC CORP Mortgage lender	India	2.4
ITAÚ UNIBANCO Commercial bank	Brazil	1.4
KOMERČNÍ BANKA Commercial bank	Czech Rep.	0.9
KOTAK MAHINDRA BANK Commercial bank	India	1.7
PING AN INSURANCE Insurance provider	China	1.9
SBERBANK Commercial bank	Russia	2.6
SIAM COMMERCIAL BANK Commercial bank	Thailand	1.4
STANDARD BANK Commercial bank	South Africa	1.2
HEALTH CARE		
CSPC PHARMACEUTICAL GROUP Pharma manufacturer	China	0.8
SINO BIOPHARMACEUTICAL Pharma manufacturer	China	0.4
INDUSTRIALS		
51JOB INC. Online human resource services	China	1.3
ASUR Airport operator	Mexico	1.0
COPA HOLDINGS Airline operator	Panama	1.0
DP WORLD Container-terminal operator	UAE	0.8
LOCALIZA Automobile rental services	Brazil	0.8
TECHTRONIC INDUSTRIES Power tool manufacturer	Hong Kong	1.1
WEG Industrial equipment manufacturer	Brazil	1.0
INFORMATION TECHNOLOGY		
AAC TECHNOLOGIES Smartphone components manufacturer	China	0.4
ASM PACIFIC TECHNOLOGY Semiconductor eqpt manufacturer	Hong Kong	0.8
EPAM IT consultant	US	1.7
HANGZHOU HIKVISION Surveillance camera manufacturer	China	1.3
HON HAI PRECISION Electronics manufacturer	Taiwan	0.4
LARGAN PRECISION Smartphone lens modules producer	Taiwan	1.1
SAMSUNG ELECTRONICS Electronics manufacturer	South Korea	4.7
SUNNY OPTICAL Optical component manufacturer	China	1.4
TATA CONSULTANCY SERVICES IT consultant	India	1.2
TSMC Semiconductor manufacturer	Taiwan	5.2
MATERIALS		
SASOL Energy and chemical technology developer	South Africa	0.6
REAL ESTATE		
No Holdings		
UTILITIES		
ENN ENERGY Gas pipeline operator	China	2.2
CASH		3.4

The portfolio is actively managed therefore holdings shown may not be current. Portfolio holdings should not be considered recommendations to buy or sell any security. It should not be assumed that investment in the security identified has been or will be profitable. To request a complete list of portfolio holdings for the past year contact Harding Loevner.

3Q19 CONTRIBUTORS TO ABSOLUTE RETURN (%)

LARGEST CONTRIBUTORS	SECTOR	AVG. WT.	CONTRIBUTION
TSMC	INFT	4.9	0.67
SUNNY OPTICAL	INFT	1.2	0.42
LARGAN PRECISION	INFT	1.0	0.16
CSPC PHARMACEUTICAL GROUP	HLTH	0.7	0.16
HANGZHOU HIKVISION	INFT	1.2	0.13

LAST 12 MOS CONTRIBUTORS TO ABSOLUTE RETURN (%)

LARGEST CONTRIBUTORS	SECTOR	AVG. WT.	CONTRIBUTION
BANCO BRADESCO	FINA	1.7	0.63
EPAM	INFT	1.5	0.62
BANK RAKYAT	FINA	1.6	0.61
ITAÚ UNIBANCO	FINA	1.7	0.58
B3	FINA	0.8	0.54

3Q19 DETRACTORS FROM ABSOLUTE RETURN (%)

LARGEST DETRACTORS	SECTOR	AVG. WT.	CONTRIBUTION
TENCENT	COMM	4.5	-0.34
BANCO BRADESCO	FINA	1.8	-0.33
DISCOVERY HOLDINGS	FINA	0.9	-0.32
AIA GROUP	FINA	2.5	-0.30
HDFC CORP	FINA	2.4	-0.29

LAST 12 MOS DETRACTORS FROM ABSOLUTE RETURN (%)

LARGEST DETRACTORS	SECTOR	AVG. WT.	CONTRIBUTION
SASOL	MATS	1.0	-0.80
BAIDU	COMM	0.8	-0.68
HANKOOK TIRE	DSCR	1.2	-0.67
TENARIS	ENER	1.1	-0.56
AAC TECHNOLOGIES	INFT	0.6	-0.54

PORTFOLIO CHARACTERISTICS

QUALITY & GROWTH	HL EM	MSCI EM
PROFIT MARGIN[1] (%)	18.0	16.5
RETURN ON ASSETS[1] (%)	10.6	6.8
RETURN ON EQUITY[1] (%)	19.6	16.4
DEBT/EQUITY RATIO[1] (%)	33.4	55.1
STD DEV OF 5 YEAR ROE[1] (%)	3.6	3.3
SALES GROWTH[1,2] (%)	8.4	5.2
EARNINGS GROWTH[1,2] (%)	13.3	10.3
CASH FLOW GROWTH[1,2] (%)	13.8	9.8
DIVIDEND GROWTH[1,2] (%)	15.9	8.3
SIZE & TURNOVER	**HL EM**	**MSCI EM**
WTD MEDIAN MKT CAP (US $B)	36.6	23.9
WTD AVG MKT CAP (US $B)	90.3	89.5
TURNOVER[3] (ANNUAL %)	19.2	—

RISK AND VALUATION	HL EM	MSCI EM
ALPHA[2] (%)	1.76	—
BETA[2]	0.94	—
R-SQUARED[2]	0.94	—
ACTIVE SHARE[3] (%)	71	—
STANDARD DEVIATION[2] (%)	14.95	15.43
SHARPE RATIO[2]	0.23	0.11
TRACKING ERROR[2] (%)	3.9	—
INFORMATION RATIO[2]	0.42	—
UP/DOWN CAPTURE[2]	98/92	—
PRICE/EARNINGS[4]	15.3	12.7
PRICE/CASH FLOW[4]	11.2	8.2
PRICE/BOOK[4]	2.5	1.6
DIVIDEND YIELD[5] (%)	2.5	3.0

[1]Weighted median; [2]Trailing five years, annualized; [3]Five-year average; [4]Weighted harmonic mean; [5]Weighted mean. Source (Risk characteristics): eVestment Alliance (eA); Harding Loevner Emerging Markets Composite, based on the Composite returns; MSCI Inc. Source (other characteristics): FactSet (Run Date: October 4, 2019); Harding Loevner Emerging Markets Model, based on the underlying holdings; MSCI Inc.

COMPLETED PORTFOLIO TRANSACTIONS

POSITIONS ESTABLISHED	COUNTRY	SECTOR
JIANGSU YANGHE BREWERY	CHINA	STPL
PROSUS	NETHERLANDS	DSCR

POSITIONS SOLD	COUNTRY	SECTOR
ASPEN PHARMACARE	SOUTH AFRICA	HLTH
EMAAR PROPERTIES	UAE	RLST
HAN'S LASER	CHINA	INDU
HONG KONG EXCHANGES	HONG KONG	FINA
RAIA DROGASIL	BRAZIL	STPL

The portfolio is actively managed therefore holdings identified above do not represent all of the securities held in the portfolio and holdings may not be current. It should not be assumed that investment in the securities identified has been or will be profitable. The following information is available upon request: (1) information describing the methodology of the contribution data in the charts above; and (2) a list showing the weight and contribution of all holdings during the quarter and the last 12 months. Past performance does not guarantee future results. In the charts above, "weight" is the average percentage weight of the holding during the period, and "contribution" is the contribution to overall performance over the period. Contributors and detractors exclude cash and securities in the Composite not held in the Model Portfolio. Quarterly data is not annualized. Portfolio attribution and characteristics are supplemental information only and complement the fully compliant Emerging Markets Composite GIPS Presentation. Portfolio holdings should not be considered recommendations to buy or sell any security.

EMERGING MARKETS EQUITY COMPOSITE PERFORMANCE (AS OF SEPTEMBER 30, 2019)

	HL EM GROSS (%)	HL EM NET (%)	MSCI EM INDEX[1] (%)	HL EM 3-YR STD DEVIATION[2] (%)	MSCI EM INDEX 3-YR STD DEVIATION[2] (%)	INTERNAL DISPERSION[3] (%)	NO. OF ACCOUNTS	COMPOSITE ASSETS ($M)	FIRM ASSETS (%)
2019 YTD[4]	12.58	11.83	6.22	14.28	13.84	N.A.[5]	18	17,253	29.54
2018	-17.29	-18.03	-14.25	13.94	14.62	0.4	21	15,114	30.07
2017	36.81	35.64	37.75	13.90	15.36	0.3	23	19,177	35.51
2016	14.84	13.85	11.60	15.00	16.07	0.4	22	13,629	34.95
2015	-12.85	-13.59	-14.60	13.61	14.04	1.2	20	9,670	29.04
2014	0.74	-0.11	-1.82	14.06	14.99	0.5	14	8,212	23.46
2013	5.74	4.80	-2.27	17.56	19.03	0.6	12	5,649	17.04
2012	23.92	22.79	18.63	20.15	21.49	0.4	10	3,772	16.65
2011	-15.55	-16.36	-18.17	24.72	25.76	0.5	9	3,136	23.06
2010	22.22	21.06	19.20	31.54	32.59	0.1	7	3,881	35.25
2009	68.45	66.95	79.02	30.92	32.35	0.2	6	2,716	42.44

[1]Benchmark Index; [2]Variability of the Composite and the Index returns over the preceding 36-month period, annualized; [3]Asset-weighted standard deviation (gross of fees); [4]The 2019 YTD performance returns and assets shown are preliminary; [5]N.A.–Internal dispersion less than a 12-month period.

The Emerging Markets Equity Composite contains fully discretionary, fee-paying accounts investing in non-US equity and equity-equivalent securities of companies domiciled predominately in emerging markets and cash reserves, and is measured against the MSCI Emerging Markets Total Return Index (Gross) for comparison purposes. Returns include the effect of foreign currency exchange rates. The exchange rate source of the benchmark is Reuters. The exchange rate source of the Composite is Bloomberg. Additional information about the benchmark, including the percentage of composite assets invested in countries or regions not included in the benchmark, is available upon request.

The MSCI Emerging Markets Index is a free float-adjusted market capitalization index that is designed to measure equity market performance in the global emerging markets. The Index consists of 26 emerging market countries. You cannot invest directly in this Index.

Harding Loevner LP claims compliance with the Global Investment Performance Standards (GIPS®) and has prepared and presented this report in compliance with the GIPS standards. Harding Loevner has been independently verified for the period November 1, 1989 through June 30, 2019.

Verification assesses whether (1) the firm has complied with all composite construction requirements of the GIPS standards on a firm-wide basis and (2) the firm's policy and procedures are designed to calculate and present performance in compliance with GIPS standards. The Emerging Markets Equity Composite has been examined for the periods December 1, 1998 through June 30, 2019. The verification and performance examination reports are available upon request.

Harding Loevner LP is an investment adviser registered with the Securities and Exchange Commission. Harding Loevner is an affiliate of Affiliated Managers Group, Inc. (NYSE: AMG), an investment holding company with stakes in a diverse group of boutique firms. The firm maintains a complete list and description of composites, which is available upon request.

Results are based on fully discretionary accounts under management, including those accounts no longer with the firm. Composite performance is presented gross of foreign withholding taxes on dividends, interest income and capital gains. Past performance does not guarantee future results. Policies for valuing portfolios, calculating performance, and preparing compliant presentations are available upon request.

The US dollar is the currency used to express performance. Returns are presented both gross and net of management fees and include the reinvestment of all income. Net returns are calculated using actual fees. Actual returns will be reduced by investment advisory fees and other expenses that may be incurred in the management of the account. The standard fee schedule generally applied to separate Emerging Markets Equity accounts is 1.25% annually of the market value up to $20 million; 0.90% of amounts from $20 million to $100 million; 0.75% of amounts from $100 million to $200 million; 0.55% of amounts above $200 million. Actual investment advisory fees incurred by clients may vary. The annual composite dispersion presented is an asset-weighted standard deviation calculated for the accounts in the composite the entire year.

The Emerging Markets Equity Composite was created on November 30, 1998.

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