HARDING LOEVNER

INTERNATIONAL EQUITY ADR

2016 Year End Report

COMPOSITE PERFORMANCE (% TOTAL RETURN) FOR PERIODS ENDING DECEMBER 31, 2016[1]

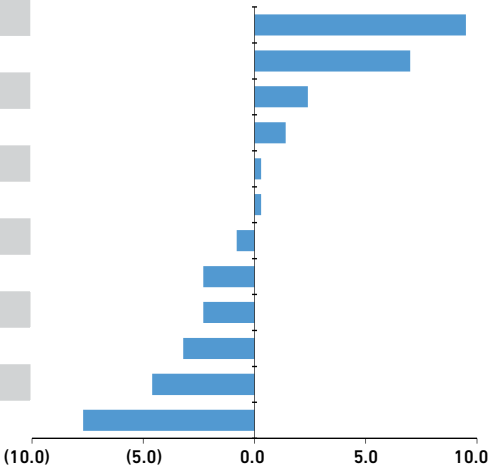
	3 MONTHS	1 YEAR	3 YEARS[2]	5 YEARS[2]	10 YEARS[2]	SINCE INCEPTION[2,3]
HL INTL EQUITY ADR (GROSS OF FEES)	-4.05	4.32	1.15	7.35	4.14	7.90
HL INTL EQUITY ADR (NET OF FEES)	-4.22	3.58	0.44	6.58	3.38	7.03
MSCI ALL COUNTRY WORLD EX-US INDEX[4,5]	-1.20	5.01	-1.32	5.48	1.42	4.71
MSCI EAFE INDEX[5,6]	-0.68	1.51	-1.15	7.01	1.22	4.38

[1]The Composite performance returns shown are preliminary; [2]Annualized Returns; [3]Inception Date: December 31, 1989 corresponds to that of the linked International Equity Composite; [4]The Benchmark Index; [5]Gross of withholding taxes; [6]Supplemental Index.

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.

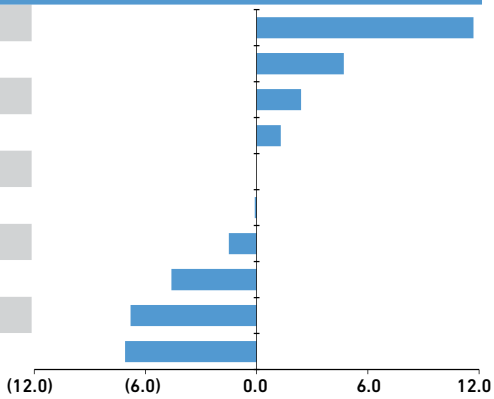
SECTOR EXPOSURE (%)

	HL INTL ADR	ACWI EX-US
HEALTH CARE	17.6	8.1
INFO TECHNOLOGY	16.3	9.3
CASH	2.4	–
INDUSTRIALS	13.0	11.6
CONS STAPLES	10.1	9.8
ENERGY	7.5	7.2
MATERIALS	7.2	8.0
REAL ESTATE	1.0	3.3
CONS DISCRETIONARY	9.2	11.5
UTILITIES	0.0	3.2
TELECOM SERVICES	0.0	4.6
FINANCIALS	15.7	23.4



GEOGRAPHIC EXPOSURE (%)

	HL INTL ADR	ACWI EX-US
EUROPE EMU	33.5	21.8
OTHER[7]	4.7	–
CASH	2.4	–
MIDDLE EAST	1.8	0.5
FRONTIER MARKETS[8]	0.0	–
EUROPE EX-EMU	22.5	22.6
PACIFIC EX-JAPAN	7.0	8.5
CANADA	2.4	7.0
JAPAN	10.1	16.9
EMERGING MARKETS	15.6	22.7



[7]Includes companies classified in countries outside the Index; [8]Includes countries with less-developed markets outside the Index.

Sector and geographic allocations are supplemental information only and complement the fully compliant International Equity ADR Composite GIPS Presentation.

Source: Harding Loevner International Equity ADR 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

A "value rally," present all year, was most pronounced in the 30 days following the US presidential election.

The yen depreciated 13% against the US dollar in response to the Bank of Japan's announced plan to buy an unlimited amount of bonds as part of its yield-curve control program.

EM stocks were hurt by fears of Trump's stated intention to raise US trade barriers.

PORTFOLIO HIGHLIGHTS

We've responded to the stretched valuations of companies we would like to own.

Our allocation to Consumer Staples declined by almost one-third.

We've boosted our holdings in Health Care companies that have decreased in price over the year.

Regardless of style headwinds, we continue to invest in high-quality growth companies with attractive valuations, while parting ways with those that we deem too pricey.

MARKET REVIEW

Non-US stock markets fell in the quarter, in US dollar terms, as investors reacted to the astonishing outcome of the US presidential election. Donald Trump delivered the second major political upset of the year by winning the US presidency, dealing prognosticators another black eye after their failure to predict the outcome of the UK referendum on European Union membership. An initial plunge in share prices overnight November 8 quickly gave way to a rally in developed markets as investors seized on Trump's plans to cut US corporate taxes, roll back regulation, and borrow to invest more in infrastructure, relegating their concerns about his trade or foreign policies or his cavalier personal attitude toward contracts (debt repayment obligations in particular) to the background. Expectations for US growth and inflation shifted upward as a result, manifest as a sharp bond sell-off globally, and a stronger US dollar predicated on an accelerated schedule of Federal Reserve interest rate hikes. The Fed duly raised short-term interest rates by a quarter percent in December and signaled three more possible rate hikes in 2017, validating this trend.

The small decline of the MSCI All Country World ex-US Index in the quarter masked very large divergences between high- and low-priced stocks within all regions and sectors. The US fiscal boost and regulatory-burden reduction that investors anticipated from the combination of a Trump administration and Republican Congress (especially when compared to their embedded expectations of a Clinton administration) afforded better earnings hopes for banks, energy, construction and engineering, capital goods, and materials companies, whose shares have dominated the ranks of lower valuations in recent years due to heightened regulation, slow capital spending, sluggish growth, and falling commodity prices. As the following charts illustrate, the cheapest stocks outperformed the most expensive ones by a wide margin.

MARKET PERFORMANCE (USD %)

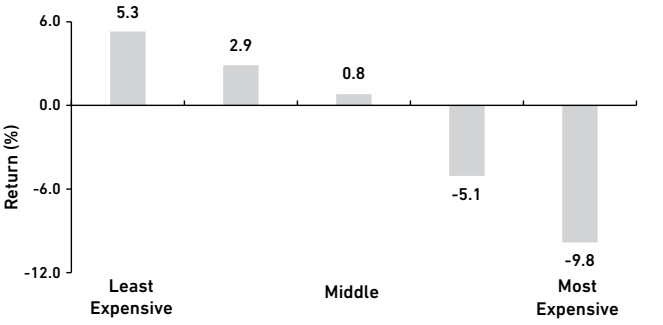
MARKET	4Q 2016	TRAILING 12 MONTHS
CANADA	3.4	25.5
EMERGING MARKETS	-4.1	11.6
EUROPE EMU	1.5	2.2
EUROPE EX-EMU	-2.0	-1.6
JAPAN	-0.1	2.7
MIDDLE EAST	-11.2	-24.5
PACIFIC EX-JAPAN	-2.7	8.0
MSCI ACW EX-US INDEX	-1.2	5.0

SECTOR PERFORMANCE (USD %)
OF THE MSCI ACW EX-US INDEX

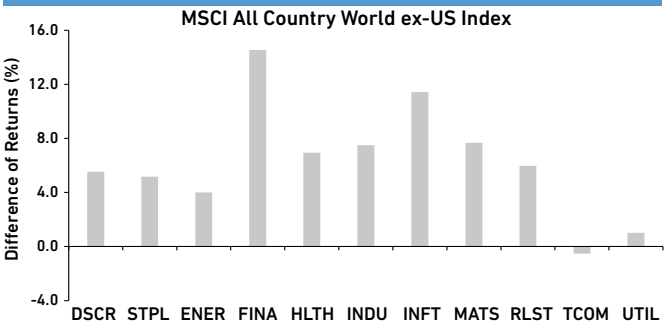
SECTOR	4Q 2016	TRAILING 12 MONTHS
CONSUMER DISCRETIONARY	-0.8	-0.6
CONSUMER STAPLES	-10.0	-1.6
ENERGY	8.4	31.9
FINANCIALS	6.9	5.2
HEALTH CARE	-8.1	-12.5
INDUSTRIALS	-2.2	7.0
INFORMATION TECHNOLOGY	-4.9	11.0
MATERIALS	2.6	28.1
REAL ESTATE	-7.8	2.2
TELECOM SERVICES	-6.6	-3.7
UTILITIES	-7.0	-2.8

Source: FactSet (as of December 31, 2016); MSCI Inc. and S&P.

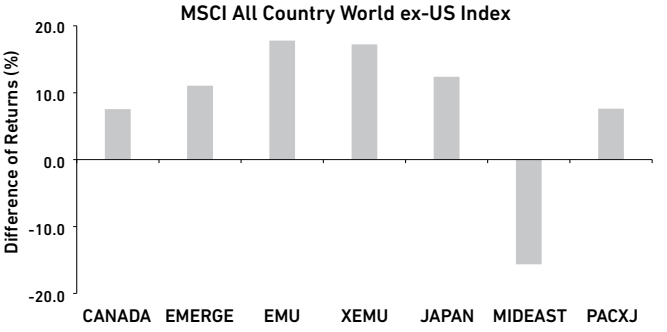
MSCI ACW EX-US INDEX PERFORMANCE BY VALUE 4Q16



RETURN SPREAD IN FAVOR OF CHEAPEST STOCKS BY SECTOR



RETURN SPREAD IN FAVOR OF CHEAPEST STOCKS BY REGION



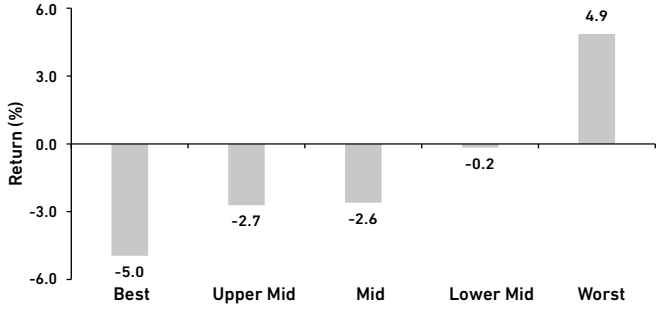
Source: FactSet. Data as of December 31, 2016. MSCI Inc. and S&P.

The Return Spread charts show the excess of the return of the cheapest third of stocks by Harding Loevner's Value ranking over the most-expensive third in the quarter.

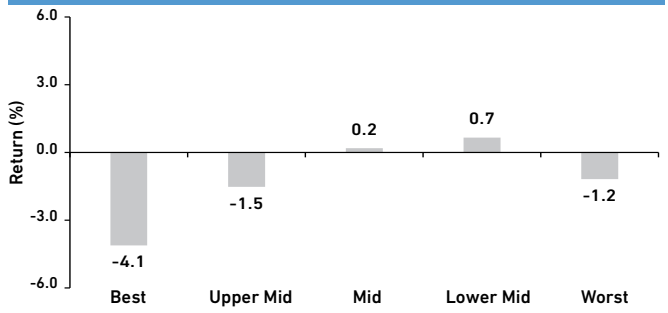
Ranked according to our propriety valuation metric, the least-expensive quintile of stocks outperformed the most-expensive quintile by more than 15 percentage points in the quarter. The

divergence between expensive and cheap featured in every major region and in nearly every sector. Echoing that divergence, the MSCI ACWI ex-US Value Index outperformed its Growth counterpart by nine percentage points in the quarter, the widest margin since the second quarter of 2003. And, because there is a high degree of overlap between low-quality or slow-growing businesses and companies with lowly priced stocks, the shares of the lowest-quality and slowest-growth businesses also performed better on average than shares of those with superior quality and growth records. The highest-quality quintile underperformed the lowest-quality quintile by almost 10 percentage points.

MSCI ACW EX-US INDEX PERFORMANCE BY QUALITY 4Q16



MSCI ACW EX-US INDEX PERFORMANCE BY GROWTH 4Q16



Source: FactSet. Data as of December 31, 2016. MSCI Inc. and S&P.

Harding Loevner's Quality, Growth, and Value 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. Value rankings are based on several valuation measures, including price ratios.

The resurgence of a "value" style was perceptible, if muted, in the first nine months of the year, but became highly pronounced in the 30 days following the US election.

In Europe, markets rose in local currency terms in the quarter, but a weaker euro (or, rather, the strong US dollar) took its toll on US dollar returns. Another chapter in the European saga of ineffectual government unfolded when Italian Prime Minister Matteo Renzi resigned (as he promised) after his proposed constitutional reform was defeated at referendum, prompting troubled lender Monte dei Paschi di Siena to request its third state-backed bailout since the financial crisis as private investors backed away from injecting fresh capital. The European Central Bank increased its Quantitative Easing program by roughly one-half trillion euros by extending its monthly bond-buying program until at least December 2017. Italy was Europe's best-performing stock market in the quarter, with the cheaper half of the market rising far more than the expensive half, giving the lie to any impression that the "value rally" was purely a US-centric, Trumponomics phenomenon, or even a consequence of rising interest rates. Stocks of high-priced, high-quality multinational companies, such as those that dominate the Danish stock market (one of Europe's worst performing in the quarter), fell heavily, as did the Swiss market. The Europe ex-EMU region fell, whereas eurozone shares managed a small rise, in dollars.

Interest rates were held low in Japan, too, and the yen depreciated 13% against the US dollar in response to the Bank of Japan's announced plan to buy an unlimited amount of bonds as part of its yield-curve control program, erasing strong stock-market performance in local currency terms. Highly priced growth stocks fell sharply, while low-priced automotive, engineering, capital goods, real estate, and financial shares outperformed.

Emerging market (EM) stocks were poor performers in the quarter, hurt by fears of President-elect Trump's stated intention to raise US trade barriers and concerns about the impact of higher interest rates and a stronger US dollar on EM external debt burdens. The MSCI China Index declined as the government tightened capital controls and Trump's bellicose tweets stoked fears that he would trigger a destructive trade war with China. The yuan continued its slide, depreciating another 4% to the weakest level since 2008, despite Trump's threats to punish China for being a "currency manipulator." Mexico, Trump's proxy punching bag during the campaign, fell 8%, most of which was caused by a decline in the peso.

Canada, on the other hand, was one of the strongest markets, a result of its strong resource sectors, a factor that aided other resource-rich markets, such as Australia, Norway, Russia, and Brazil.

By sector, Energy and Financials stocks were the biggest gainers in the quarter, with Materials the only other sector that managed to rise in US dollars. Energy shares were aided by a rise in oil prices after the first agreement by OPEC to cut supply since the financial crisis, and the prospect that carbon and other environmental regulation might loosen, at least in the US. Bank shares rose 8%, behind the gain for US banks, buoyed by the prospects that higher US interest rates would eventually drag interest rates in other currencies higher and help lending margins. Consumer Staples, Health Care, Real Estate, Utilities, and Telecom Services performed the worst, as investors no longer prized as greatly the steady, bond-like characteristics of their businesses in an environment where bonds were falling sharply. But the fall of these sectors was also clearly a result of the high valuations that many of those steady businesses had reached in the stock market relative to other more cyclical businesses.

For the full year, Energy and Materials were, by far, the best-performing sectors, returning more than five times the broader market. Information Technology (IT), led by the blistering 29% return of the semiconductor group, also delivered double-digit returns. Industrials and Financials, led by banks, also bettered the Index, in keeping with slowly but steadily improving economic data in the year. Health Care was the worst-performing sector, buffeted all year by political scrutiny during the US presidential campaign and now by ongoing reimbursement concerns. Viewed by region, Canada was the standout and EMs also posted double-digit market returns. Pacific ex-Japan also bettered the Index while Europe and Japan lagged the Index. For reference, the US market return equaled the return of the EM Index.

PERFORMANCE AND ATTRIBUTION

The 4.1% decline of the International Equity ADR composite trailed the 1.2% decline of the MSCI All Country World ex-US Index in the quarter. The composite rose by 4.3% in the full year, trailing the Index, which gained 5.0%. The charts on the right illustrate the sources of relative return for the year by sector and region, respectively.

Essentially all of the poor relative performance in the quarter resulted from our large holdings of more-expensive companies. That result is consistent with our quality-growth investment style facing severe headwinds from the value resurgence. Viewed by sector, the largest drags came from Financials and Health Care. Our light holdings in Financials were a significant bet against the strongly performing, heavyweight sector, and our choices within the sector lagged the Index return. **AIA Group**, a pan-Asian life insurer, suffered from both its premium valuation and potential risks of a regulatory squeeze on its booming business with Chinese investors seeking investment diversification. **Garanti Bank** suffered from the continued weakness of the Turkish lira and worries about the country's escalating conflict along its southern border with Syria. Meanwhile, our large holdings in Health Care hurt, and the fact that some are highly priced growth beauties made things worse. **Sysmex**, the Japanese clinical testing equipment company, suffered a sharp stock-price decline after reporting earnings that fell short of lofty expectations. The drag on performance was partially offset by good stocks within Consumer Staples and Energy, but the strong tailwinds for cheap stocks were headwinds for our stocks, so such relative winners were scarce.

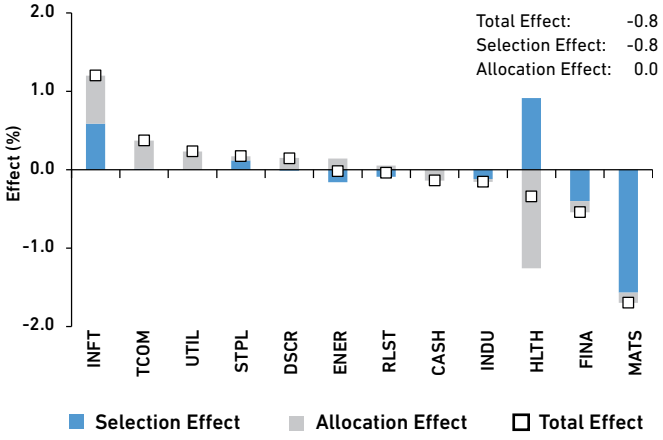
Viewed by region, those headwinds ensured that we underperformed almost everywhere. The exceptions were two regions in which we owned a single company: Canada, where **Canadian National Railway** matched the market, and the Middle East, where new holding **Check Point Software Technologies** rose, while the market fell. The biggest harm came to us in Japan, where three of our seven holdings suffered double-digit price declines against a flat market.

For the full year, the biggest relative gains came with Europe ex-EMU, especially from the UK, where our former portfolio holding BG Group was acquired by **Royal Dutch Shell** and we accepted Shell shares for our stake, which went on to perform strongly; we also gave up long-held ARM Holdings to a cash takeover by Japan's Softbank. We were hurt by our stock selection within EM and our underweight to the strong performing region. Our Japanese stocks underperformed in the full year.

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 December 31, 2016 is available on page 10 of this report.

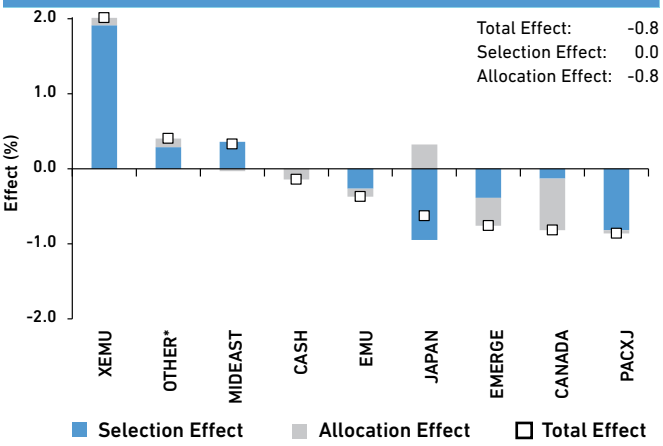
SECTOR PERFORMANCE ATTRIBUTION TRAILING 12 MONTHS

INTERNATIONAL EQUITY ADR COMPOSITE VS. MSCI ACW EX-US INDEX



GEOGRAPHIC PERFORMANCE ATTRIBUTION TRAILING 12 MONTHS

INTERNATIONAL EQUITY ADR COMPOSITE VS. MSCI ACW EX-US INDEX



**Includes companies classified in countries outside the Index. Source: FactSet; Harding Loevner International Equity ADR 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.*

Viewed by sector, we had strong contributions from our large holdings in IT, especially from semiconductors (**Taiwan Semiconductor**, ARM Holdings). We had good stocks within Health Care, but undid those gains by holding so much in what turned out to be the worst-performing sector in the year. Our Materials stock picks were big laggards of that sector, which is dominated by cyclical mining and commodity companies rather than our steady growers including food-ingredients supplier **Symrise** and specialty lubricant maker **Fuchs Petrolub**.

PERSPECTIVE AND OUTLOOK

Markets have undergone a sea change in expectations, accelerated by the surprise results of the US presidential election, with effects radiating across the world and interacting with independent and sometimes opposing forces. The US election itself was politically polarizing, which we do not intend to address here. However, it is nearly as difficult to arrive at middle ground regarding the election's effects on various parts of the global economy and the investment implications. As a result, we're offering you the perspective of several of our investment colleagues as they think, and as we debate, about the prospects for our companies and for markets in the quarters ahead. One strand, championed by Rick Schmidt, CFA, is orthodox in its macroeconomic approach to the perceived implications of a Trump administration. Another strand, by Jingyi Li, focuses on the state of global trade, which has been, in our view, the engine of global growth and prosperity over the 30-year stretch of our own careers. The final strand, championed by Peter Baughan, CFA, embraces the possible changes for the better that might come from replacing the gridlock of US political economy with a supply-side vision of government enabling growth. None of these views (yet) represents a Harding Loevner "house" view, but each perspective informs some part of our investment thinking. In cherished Harding Loevner tradition, we do not require, or even seek, unanimity of vision or outlook; at the present juncture, we assuredly do not have it. Instead, we offer you some of the debate.

Less Trade and More Inflation: Not Great for Stocks

Rick Schmidt, CFA

Predicting what Trump policies will mean for the global economy when we don't even know what future Trump policies will be is obviously a mug's game. But the process of thinking about what Trump's policies will mean for economies, companies, and share prices can start by looking at Trump's words and the bond market's response. These suggest that two outcomes are likely: a rolling back of globalization and higher inflation in the US, even while stock prices suggest faster economic growth ahead.

In global trade, Trump's words, particularly his consistent theme of "America First," along with promises to tear up trade agreements like NAFTA and implement "border taxes" and 10–45% tariffs on imports from China, will make it even harder for the growth in global trade to move above the positive growth achieved in each of the last five years (in the range of 1.7–2.7%). If threats to impose 35% tariffs on companies that close their domestic US factories and move production to other countries are made actual policy, an absolute fall in trade is not out of the question. To put that in perspective, it takes a lot to stop trade: only three times in the last 25 years has global trade declined (1982, 2001, and 2008—each time following a US recession).

The implications of less trade competition may be positive for some companies (US steelmakers were able to raise prices the last time duties were placed on Chinese steel), but negative for most (including everyone buying steel). The important fact to remember is that countries do not trade with each other—companies do. Company managements have chosen a supplier or manufacturer in location X or Y because they find it more profitable to do so. An "America First" policy cannot mean better profits for US companies on average—unless one argues that higher employment and wages in protected industries will spur demand and increase the rate of economic growth to the benefit of all US companies. Tariffs or penalties will not only result in less-profitable sourcing, but also wreak havoc with supplier/production chains, with a resulting loss of efficiency and profitability. For a lesson on the impact of restrictions on company managements, look no further than the misguided efforts to increase employment in Europe. A mandated 35-hour week in France did not lead companies to hire more labor to "fill" the extra hours; it led to less investment and employment as companies simply chose not to add capacity in France. Why would any companies make the marginal decision to add capacity in the US if they knew that they face the risk of not being able to move that production if it proves uneconomic?

While US equity indexes have moved higher, prices in the US fixed-income market have, in percentage terms, moved even more—in the opposite direction. The reason is simple: bond market investors have already voted, and they have backed higher inflation. This can be seen most clearly in the changes in the 10-year Treasury bond yields. Those yields jumped from 1.76% at the end of October to 2.23% on November 14, one week after Trump's election victory, and ended the year at 2.45%, almost 40% higher in total. Corroborated by a rise in the breakeven rate on Treasury Inflation-Protected Securities, the bond market's price actions are implying higher inflation and higher nominal interest rates.

While the predictive accuracy of that "vote" may be questioned (will pressure on wages be muted by new labor supply as today's out-of-work, but no longer looking for work—and thus not included in unemployment statistics—begin to re-enter the workforce?), it is hard to argue against the math. Trump's campaign promises of increased infrastructure (and military and so much

more) spending, coupled with pledged tax cuts, simply do not add up. The US will have to run increased budget deficits to pay for these policies. With the US economy already below 5% unemployment, wage hikes and higher inflation are very likely. That prospect, combined with inflation already having reached Fed target levels, might portend the end of the 35-year bull market in bonds.

The implications for stock prices are complicated. US equity-market indexes have risen on the hope of stronger growth in revenues. If today's historically high US corporate profitability can be maintained in the face of less trade, higher inflation, uncertain fiscal policies, and who-knows-what populist measures, that growth may flow through to corporate bottom lines. But a reversion to the mean in profit margins seems much more likely, particularly with the current full employment levels. The key to Trump's Electoral College victory was anger over the lack of wage growth. In the next four years, what politician will not try to make sure those voters are satisfied?

The important fact to remember is that countries do not trade with each other—companies do.

Finally, today's high valuations should give the bulls pause. Equity-market rallies in the past began at much lower levels of corporate profitability and valuation multiples. This meant there was room for companies to both grow profits and see valuations rise. To argue that this can happen from the relatively high levels of today suggests the triumph of hope over experience (three marriages, don't forget). If one listens to Trump's words and sees the bond market's reactions, a more conservative set of corporate profit growth expectations seems in order.

Globalization is Not Fragile

Jingyi Li

The trade policy of the new administration is likely to impact global trade and every stakeholder negatively, yet the actual effects could be limited in scale and extent. Global trade of goods and services is now huge—approximately US$25 trillion in 2014—and contributes 30% of the world GDP.[1] Nearly half of world trade in goods and services is part of global value chains as different countries specialize in particular stages of production. Any effort to curtail trade will face enormous challenges from every country and industry. Global trade is more than boatloads of shoes and smartphones. Trade of services, especially computer services, financial services, and travel, is resilient and fast growing, though still smaller than trade of goods. The trade of services is less subject to measures that target trade of goods. Global trade is also regional: 70% of merchandise exports from Europe are within the region, and approximately 50% of exports from Asia and North America are intraregional trade.[2] Policy changes in the US, if any, will have less direct impact on these intraregional businesses.

The companies held in our portfolios, with their strong competitive advantages and capable management, stand a better chance of overcoming all kinds of challenges. Companies such as AIA Group and Tencent are regional champions with enormous competitive advantages. Tencent, which constitutes the key asset of **Naspers**, is a leading internet company in China, boasting over 800 million monthly active users for its large portfolio of social and entertainment services. Companies such as **WPP**, **Nestlé**, and **Atlas Copco** each have a strong local presence in almost every part of the world, including the US. Nestlé, founded 150 years ago, has 436 factories in 85 countries and sells a large variety of food products to 189 countries. Companies such as **Linde**, **Dassault Systèmes**, and **Fanuc** share oligopolistic positions with other non-US companies. Fanuc is the number-one provider of computer numerical-control systems (50% market share globally) and is one of the largest robot makers (20% market share globally). It is unlikely that any policy change would disrupt the competitive position of such companies, especially given that some of them, for example Atlas Copco, **Bayer**, and **Roche Holding**, and Nestlé, have been around for over 100 years and have survived some of the most severe disruptions in human history.

Donald Trump: (Constrained) Master of the Media Moment

Peter Baughan, CFA

The sense of ongoing "regime change" across global financial markets is palpable. We had observed green shoots of a value recovery in equity markets before the surprise election of Trump to the US presidency. The sharp rally in the US dollar and bond yields after the election and further gains in equities (led by less-expensive and lower-quality stocks), as well as the Fed's aggressive interest rate forecast in December, appear to have marked 2016 as a year of fundamental change—in economic outlook, at least in the US, and in style leadership in equity markets. The question now for many investors is: Who is the real Donald Trump and what impact will the emerging Trump administration have on global financial markets in 2017 and beyond? An additional question: How long will renewed value leadership in equity markets last?

It is not entirely clear who the real Donald Trump is. What is inescapable is that Trump the political candidate is disruptive in form and content. In form, Trump eschewed traditional media, labeling much of it "corrupt," speaking to millions of voters directly through social media. Further, despite his self-proclaimed billionaire status, candidate Trump was able to tap into the discon-

[1]World Trade Organization, *International Trade Statistics 2015* (2015): 17.
[2]Ibid., 27.

tent, anger, and fear across much of Middle America, a powerful social dynamic that armies of pollsters and well-paid political consultants failed to discern fully. For content, candidate Trump pursued, and President-elect Trump continues to pursue, unconventional dialogue. Blunt Trump utterances—even those that are patently racist, sexist, or simply untrue—are seen as "authentic," something apparently so rare in the political realm that millions of voters rewarded this bluntness. My only firm initial conclusion at this stage is that Trump is master of the media moment. If this Trump were alone at the helm of the US government, I'd expect volatility to rise sharply in the coming year as Trump's impulse-utterances of the moment fail to convert to coherent policy.

Fortunately, President Trump will operate within the well-established checks and balances of the US political structure. In this context, considering Republican majorities in the Senate and the House and Republican dominance across state governments, the outlook for a Trump presidency could be quite positive. It is illustrative to consider Trump's "contract for the American voter" detailed shortly before the election. Asking Americans "to dream big," Trump outlined a series of policy initiatives he pledged to pursue in his first 100 days in office. The contract proposes term limits for members of Congress while sharply limiting the ability of politicians to become lobbyists. It outlines the core of Trump's economic agenda, calling for tax reduction and structural simplification, aggressive investment in US infrastructure and energy, and pursuit of an ambitious "America First" economic and trade policy. The contract does not shy away from "deliverables," calling for the achievement of 4% economic growth and creation of 25 million new American jobs. It details additional Trump priorities such as sharp reduction in government regulations, reversal of some of President Obama's controversial executive actions, appointment of conservative Supreme Court justices, deportation of criminal illegal aliens, and a rollback of federal involvement in state and local control of education.

The contract also states that the Trump administration will label China a currency manipulator as well as take aggressive steps to identify and end trade abuses that are believed to negatively impact American workers. This language has given rise to fears of spiraling trade wars and even an end to growth in global trade under a protectionist Trump administration. These fears will likely prove exaggerated. I see these and many other statements that Trump has made as opening salvos in a grand series of negotiations—negotiations that in this instance promise to fundamentally redefine how America conducts trade and what constitutes a successful trade agreement. This could be a good thing for US companies that are able to supplant an international supply chain. Given Trump's and the Republican Party's need to deliver economic results, I'm not expecting the Trump trade team to derail US economic growth.

Of course the Trump Cabinet will be essential to the success—or failure—of the Trump administration. From what we know to date, President-elect Trump has tacked away from his most divisive campaign stances and attracted accomplished executives and leaders from across the private sector to join his administration, confirmation hearings pending. While it is too early to determine how effective this unconventional set of high-profile cabinet appointees may be, their initial selection leaves me with a favorable impression of President-elect Trump's personnel judgments. I'm expecting a can-do, results-oriented administration with a president and senior team acting as corporate CEOs, not senior politicians.

Summing up, in President-elect Trump we have on the one hand an unpredictable media showman and, on the other, an apparently successful private-sector executive with a set of audacious, if populist, policy proposals, backed by Republican control of Congress and an impressive Cabinet-in-waiting. The success of the Trump administration in 2017 will largely depend on how these dynamics interact. In an optimistic scenario, I could see President Trump pursuing a series of innovative and fresh political and economic initiatives, engaging directly with CEOs and political leaders, and injecting energy and confidence into consumers and corporates to spend and invest across the US. At the same time, the machinery of government would simultaneously grind forward, led by the Republican Congress and various Cabinet members and their teams. This would appear to be a rare opportunity to drive significant economic and political change. In this scenario, I'd expect to see "value" retain broad style leadership in equity markets as economic and interest rate forecasts are likely boosted during the year and as potential ripple-through economic benefits from US economic growth aids non-US markets. However, I'd be surprised if there was truly a step-change increase in US economic growth in the near term as potential delays in political negotiations are possible and given time lags in the impact of accelerated capital spending, should it occur. As such, I'd expect to see style leadership turn neutral or even swing mildly back toward growth later in the year given the rapidity and extent of the relative valuation moves to date.

In a pessimistic scenario, I could see President Trump becoming irascible and moody in the face of public criticism or obstacle, acting unpredictably and perhaps punitively and counterproductively against political or business critics. Alternatively, the Trump administration could prove effective in advancing what turns out to be ill-considered trade and tax policies through Congress that negatively affect economic growth. In this scenario, we could see the machinery of underlying government grind slowly or even come to a halt amidst a storm of political argument including Cabinet infighting and resignations. Should these risks materialize, I'd expect a

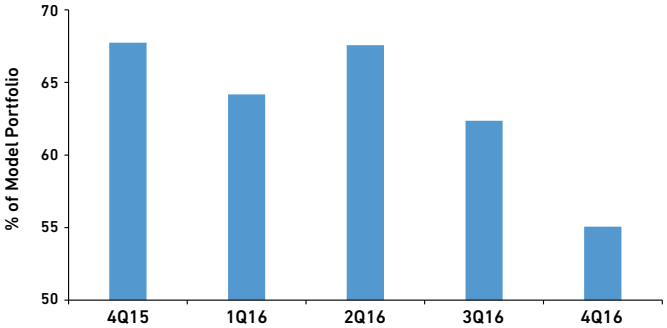
sharp reversal in the value rally and renewed leadership by high-quality growth stocks.

I don't know how to handicap the odds of a Trump administration success or failure in 2017. However, I tilt toward optimism given Republican control of Congress, the clarity of Trump's proposals for his first 100 days in office, the readiness of voters for fundamental change in Washington, and the pressing need for Republicans to demonstrate concrete results before midterm elections in 2018. I would not be surprised to see a continuation of value style leadership in 2017, although I'd expect its magnitude to diminish as the year progresses. Longer term, I do think the Trump administration has the potential to fundamentally increase US economic growth through an explicitly pro-American worker yet pro-business set of priorities.

PORTFOLIO HIGHLIGHTS

We have been concerned—and writing—about stretched valuations for high-quality, growth businesses for some time. In our Fourth Quarter 2014 Report, we wrote, "the long period of subpar growth in Europe and Japan, and the slowing growth in EMs, has driven investors to prefer the most robust businesses over those of lesser quality. It appears that valuations of the top-tier companies have slowly become stretched." The following quarter, we wrote, "the issue of valuation is getting more of our attention because high-quality, fast-growing companies have seen their stocks rise faster than their earnings." We began tuning our portfolio in response to these stretched valuations in mid-2015. As the following chart illustrates, over the last year we have reduced the portfolio's holdings in the two most-expensive quintiles—i.e., the richest 40% of the market—by 1,200 basis points, a reduction of almost one-fifth.

PERCENT OF INTERNATIONAL EQUITY ADR MODEL PORTFOLIO IN THE TWO MOST EXPENSIVE QUINTILES



Source: FactSet, International Equity ADR model portfolio. Data as of December 31, 2016. MSCI Inc. and S&P.

The capital was reinvested in more moderately priced companies. These changes have been helpful to returns, as the portfolio had returns that were 41 basis points higher than they would have been with the portfolio frozen in what we owned on June 30, 2015.

It is our tendency to move in incremental steps in managing portfolios, something that our low turnover (approximately 16% annually over the past decade) speaks of, so our changes were not wholesale allocation shifts, but more of a whittling away of highly priced stocks and reinvestment into the cheaper companies in our qualified pool of candidates. Another way to view these shifts is through the changes in our allocations to economic sector. Most pronounced was the reduction of our allocation to Consumer Staples, which declined by almost one-third, to end the year at about 10%, slightly higher than the Index. Many Consumer Staples companies had been bid to historically high levels in the ultra-low interest rate environment as investors accorded great value to the reliable, long-duration cash flows that companies in the food, beverage, and household-products industries typically generate. Most recently, we exited the remainder of our holding in Anheuser-Busch InBev, for valuation reasons, having sold half in 2015. Those sales funded an increase of holdings in more modestly valued but more economically sensitive sectors like Industrials and Energy, including a number of smaller companies that trade at valuations we think underestimate their potential for rapid growth, such as Japan's **Park24** and the UK's **BBA Aviation**.

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We increased our weight in Financials in the fourth quarter, anticipating improved operating conditions for banks and insurers, especially those with significant US-dollar deposits, including new holding **HSBC**. Steepening of the yield-curve in the US will improve net margins for the bank's US operations, and will do the same for HSBC's massive US-dollar deposits in Asia. In addition, the profit environment for any US bank operations should improve as the regulatory burden imposed by the Dodd-Frank legislation is eased, prospectively, under President-elect Trump and the Republican-controlled Congress. We bought back India's **ICICI Bank** in the quarter and added to our holdings in **Allianz**, the German insurer, and **BBVA**, the Spanish multinational bank whose largest subsidiary is Mexico's largest bank, Bancomer. Financials remains, however, our largest underweight relative to the Index.

We altered our Health Care holdings significantly in the year. Health Care enjoyed positive returns every year since 2009—until 2016, when it was the worst-performing sector. Blame US election-year politics, wherein candidates at both ends of the political spectrum took aim at pharmaceutical companies' controversial pricing decisions and fat profit margins. This year we pruned existing holdings that became too expensive, selling Denmark's Coloplast and Novo Nordisk outright and reducing

Japanese testing equipment maker Sysmex. But since April, we have boosted our Health Care holdings, finding value in Bayer of Germany, **Shire** of the UK, and **Aspen Pharmacare** of South Africa.

As we look ahead, we will continue to manage the portfolio as we have in the past, letting go of investments that have become too expensive, whether they have been successful or not, and replacing them with other attractive businesses whose share prices reflect more modest expectations, not neglecting also to prune stocks of unobjectionable valuation whose prospects we come to doubt on fundamental grounds. In short, while we may currently be suffering style headwinds, we will press ahead with the same approach that has delivered good long-term returns in the past.

Portfolio Management Team Update

Patrick Todd, CFA has joined our International Equity strategy portfolio management team. He now manages a "paper" portfolio that expresses his investment views but is not employed directly in managing client capital for the strategy. He is a research analyst focusing on Health Care who joined Harding Loevner in 2012. Peter Baughan, CFA has stepped down as a paper PM for the strategy, a role in which he served since 2004, as of year-end. With these changes, the PM team is now Ferrill Roll, CFA and Alec Walsh, CFA (co-lead PMs), Bryan Lloyd, CFA, Patrick Todd, CFA, and Andrew West, CFA. Peter continues as a co-lead PM on our Global Equity strategy. The International Equity ADR strategy's model portfolio is based upon the model portfolio constructed for the ordinary-share International Equity strategy.

INTERNATIONAL EQUITY ADR HOLDINGS (AS OF DECEMBER 31, 2016)

SECTOR/COMPANY/DESCRIPTION	COUNTRY	END WT.(%)
CONSUMER DISCRETIONARY		
BMW Automobile manufacturer	Germany	1.9
LVMH MOËT HENNESSY Luxury goods group	France	1.2
NASPERS Media, internet, pay TV company	South Africa	2.3
TELEVISA Media, broadcasting, and entertainment	Mexico	0.7
WPP Advertising and marketing services	UK	3.1
CONSUMER STAPLES		
BUNGE Soybean processor	US	2.2
L'ORÉAL Beauty and personal care products	France	2.7
NESTLÉ Food company	Switzerland	3.7
UNILEVER Consumer products manufacturer	UK	1.6
ENERGY		
ROYAL DUTCH SHELL Oil exploration	UK	3.6
SCHLUMBERGER Oilfield services company	US	2.6
TENARIS Steel pipe manufacturer	Italy	1.4
FINANCIALS		
AIA GROUP Life insurance	Hong Kong	3.5
ALLIANZ Multiline insurance	Germany	2.7
BBVA Commercial bank	Spain	2.8
DBS GROUP Commercial bank	Singapore	1.8
GARANTI BANK Commercial bank	Turkey	0.8
HSBC Multinational commercial bank	UK	1.3
ICICI BANK Commercial bank	India	1.0
ITAU UNIBANCO Commercial bank	Brazil	1.7
HEALTH CARE		
ASPEN PHARMACARE Pharma manufacturer & distributor	South Africa	0.9
BAYER Crop chemicals and pharmaceuticals	Germany	4.1
CSL LIMITED Blood plasma and recombinants	Australia	1.6
FRESENIUS MEDICAL CARE Dialysis svcs & eqpt	Germany	2.3
GRIFOLS Biopharmaceutical and diagnotstics	Spain	0.9
ROCHE HOLDING Pharma and diagnostic equipment	Switzerland	3.8
SHIRE Prescription medicine developer	UK	1.0
SONOVA HOLDING Hearing aid manufacturer	Switzerland	1.0
SYSMEX Clinical testing equipment	Japan	1.9

SECTOR/COMPANY/DESCRIPTION	COUNTRY	END WT.(%)
INDUSTRIALS		
ALFA LAVAL Heat transfer and fluid separation equipment	Sweden	1.1
ATLAS COPCO Industrial compressors & mining eqpt	Sweden	1.8
BBA AVIATION Flight support systems	UK	0.6
CANADIAN NATIONAL RAILWAY Railway operator	Canada	2.4
FANUC Industrial robots, controls, machine tools	Japan	2.8
JGC CORP Industrial facilities engineer	Japan	1.3
KUBOTA Farming and construction machinery	Japan	1.0
MONOTARO Online maintenance supplies distributor	Japan	0.8
PARK24 24-hr automated parking operator	Japan	1.2
INFORMATION TECHNOLOGY		
BAIDU Internet search provider	China	3.7
CHECK POINT Software company	Israel	1.8
DASSAULT SYSTÈMES CAD/CAM software designer	France	3.9
SAP Enterprise software provider	Germany	3.4
TAIWAN SEMICONDUCTOR Semiconductor chip foundry	Taiwan	3.5
MATERIALS		
AIR LIQUIDE Industrial gas company	France	2.4
FUCHS PETROLUB Lubricants manufacturer	Germany	1.2
LINDE Industrial gases and engineering	Germany	1.4
SASOL Refined product and chemicals group	South Africa	1.0
SYMRISE Global flavor and fragrance supplier	Germany	1.2
REAL ESTATE		
MITSUBISHI ESTATE Property mgt and real estate	Japan	1.0
TELECOM SERVICES		
No holdings		
UTILITIES		
No holdings		
CASH		2.4

Model Portfolio holdings are supplemental information only and complement the fully compliant International Equity ADR Composite GIPS Presentation. 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.

4Q16 CONTRIBUTORS TO ABSOLUTE RETURN (%)

LARGEST CONTRIBUTORS	SECTOR	WEIGHT	CONTRIBUTION
BUNGE	STPL	2.0	0.40
ROYAL DUTCH SHELL	ENER	3.4	0.38
TENARIS	ENER	1.2	0.29
ALLIANZ	FINA	2.3	0.21
BMW	DSCR	1.8	0.18

LAST 12 MOS CONTRIBUTORS TO ABSOLUTE RETURN (%)

LARGEST CONTRIBUTORS	SECTOR	WEIGHT	CONTRIBUTION
ARM HOLDINGS	INFT	2.1	1.53
TAIWAN SEMICONDUCTOR	INFT	4.3	1.35
ITAU UNIBANCO	FINA	1.5	1.00
ROYAL DUTCH SHELL	ENER	2.8	0.93
SCHLUMBERGER	ENER	2.4	0.55

4Q16 DETRACTORS FROM ABSOLUTE RETURN (%)

LARGEST DETRACTORS	SECTOR	WEIGHT	CONTRIBUTION
AIA GROUP	FINA	3.9	-0.71
SYSMEX	HLTH	2.3	-0.56
DASSAULT SYSTÈMES	INFT	4.0	-0.49
NASPERS	DSCR	2.4	-0.44
ANHEUSER-BUSCH INBEV	STPL	0.9	-0.40

LAST 12 MOS DETRACTORS FROM ABSOLUTE RETURN (%)

LARGEST DETRACTORS	SECTOR	WEIGHT	CONTRIBUTION
ICICI BANK	FINA	0.3	-0.66
ROCHE HOLDING	HLTH	2.9	-0.53
BAIDU	INFT	3.5	-0.43
NOVO NORDISK	HLTH	0.2	-0.38
ALLIANZ	FINA	2.7	-0.35

PORTFOLIO CHARACTERISTICS

QUALITY & GROWTH	HL INTL ADR	ACWI EX-US
PROFIT MARGIN[1] (%)	11.4	9.1
RETURN ON ASSETS[1] (%)	7.0	4.5
RETURN ON EQUITY[1] (%)	14.3	12.3
DEBT/EQUITY RATIO[1] (%)	50.9	65.8
STD DEV OF 5 YEAR ROE[1] (%)	2.4	3.3
SALES GROWTH[1,2] (%)	4.5	0.3
EARNINGS GROWTH[1,2] (%)	9.2	5.9
CASH FLOW GROWTH[1,2] (%)	5.9	4.9
DIVIDEND GROWTH[1,2] (%)	7.5	4.7
SIZE & TURNOVER	**HL INTL ADR**	**ACWI EX-US**
WTD MEDIAN MKT CAP (US $B)	44.7	30.1
WTD AVG MKT CAP (US $B)	70.9	53.3
TURNOVER[3] (ANNUAL %)	15.0	–

RISK & VALUATION	HL INTL ADR	ACWI EX-US
ALPHA[2] (%)	2.23	–
BETA[2]	0.92	1.00
R-SQUARED[2]	0.92	1.00
ACTIVE SHARE[3] (%)	89	–
STANDARD DEVIATION[2] (%)	12.65	13.23
SHARPE RATIO[2]	0.57	0.41
TRACKING ERROR[2]	3.7	–
INFORMATION RATIO[2]	0.51	–
UP/DOWN CAPTURE[2]	96/86	–
PRICE/EARNINGS[4]	20.4	16.7
PRICE/CASH FLOW[4]	14.3	9.7
PRICE/BOOK[4]	2.4	1.6
DIVIDEND YIELD[5] (%)	2.3	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 International Equity ADR Composite, based on the Composite returns; MSCI Inc. Source (other characteristics): FactSet (Run Date: January 6, 2017); Harding Loevner International Equity ADR Model, based on the underlying holdings; MSCI Inc.

COMPLETED PORTFOLIO TRANSACTIONS

POSITIONS ESTABLISHED	COUNTRY	SECTOR
ASPEN PHARMACARE	SOUTH AFRICA	HLTH
HSBC	UNITED KINGDOM	FINA
ICICI BANK	INDIA	FINA
SHIRE	UNITED KINGDOM	HLTH

POSITIONS SOLD	COUNTRY	SECTOR
ANHEUSER-BUSCH INBEV	BELGIUM	STPL
COLOPLAST	DENMARK	HLTH
KONE	FINLAND	INDU
MTN GROUP	SOUTH AFRICA	TCOM

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 International Equity ADR Composite GIPS Presentation. Portfolio holdings should not be considered recommendations to buy or sell any security.

INTERNATIONAL EQUITY ADR COMPOSITE PERFORMANCE (AS OF DECEMBER 31, 2016)

	HL INTL ADR GROSS (%)	HL INTL ADR NET (%)	MSCI ACWI EX-US[1] (%)	MSCI EAFE[2] (%)	HL INTL ADR 3-YR STD DEVIATION[3] (%)	MSCI ACWI EX-US 3-YR STD DEVIATION[3] (%)	MSCI EAFE 3-YR STD DEVIATION[3] (%)	INTERNAL DISPERSION[4] (%)	NO. OF ACCOUNTS[5]	COMPOSITE ASSETS[5] ($M)	FIRM ASSETS (%)
2016[6]	4.32	3.58	5.01	1.51	12.80	12.53	12.48	0.2	165	680	1.74
2015	-0.63	-1.30	-5.25	-0.39	12.52	12.13	12.47	0.3	165	630	1.89
2014	-0.16	-0.88	-3.44	-4.48	11.90	12.78	12.99	0.4	160	533	1.52
2013	14.93	14.10	15.78	23.29	15.03	16.20	16.22	0.7	159	520	1.57
2012	19.87	18.99	17.39	17.90	17.92	19.22	19.32	0.5	151	417	1.84
2011	-10.40	-11.08	-13.33	-11.73	21.86	22.74	22.45	0.3	167	365	2.68
2010	17.00	16.13	11.60	8.21	25.55	27.33	26.28	0.3	157	380	3.45
2009	35.76	34.69	42.14	32.46	23.40	25.30	23.65	0.4	118	265	4.14
2008	-35.17	-35.67	-45.24	-43.06	18.87	20.90	19.26	0.3	91	161	4.93
2007	14.08	13.28	17.12	11.63	10.27	10.62	9.41	0.6	84	243	3.82
2006	23.63	22.69	27.16	26.86	10.54	10.18	9.29	0.7	80	153	3.24

[1]Benchmark Index; [2]Supplemental Index; [3]Variability of the composite and the Index returns over the preceding 36-month period, annualized; [4]Asset-weighted standard deviation (gross of fees); [5]Total product accounts and assets are 24,160 and are $8,578 million, respectively, at December 31, 2016 and are presented as supplemental information; [6]The 2016 performance returns and assets shown are preliminary.

The International Equity ADR Composite contains fully discretionary, fee paying international equity accounts with the objective of long-term capital appreciation. Securities are held in Depository Receipt (DR) form, including American Depository Receipts (ADRs) and Global Depository Receipts (GDRs) or are otherwise traded on US exchanges. For comparison purposes, the Composite is measured against the MSCI All Country World ex-US Index, presented gross of withholdings. (Prior to December 31, 2012, the Composite was measured against the MSCI All Country World ex-US Index net of foreign withholding taxes for the periods presented. The presentation was changed to conform the treatment of withholding of the benchmark with that of the Composite.) 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 All Country World ex-US Index 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 US. The Index consists of 45 developed and emerging market countries. The MSCI EAFE Index (Europe, Australasia, Far East) is a free float-adjusted market capitalization index that is designed to measure developed market equity performance, excluding the US & Canada. The Index consists of 21 developed market countries. You cannot invest directly in these Indices.

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 by Ashland Partners & Company, LLP for the period November 1, 1989 through September 30, 2016.

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 International Equity ADR Composite has been examined for the periods January 1, 1990 through September 30, 2016. 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. Additional information is available upon request. 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 International Equity ADR accounts is 0.80% annually of the market value up to $20 million; 0.40% of amounts above $20 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 International Equity ADR Composite was created on August 31, 2000. Performance prior to August 31, 2000 is that of the International Equity Composite, which was managed similarly and materially represented the strategy of the International Equity ADR Composite.

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