Brandes Investment Partners
Emerging Markets Equity Strategy Notes – Private Client
Fourth Quarter 2020 (October 1 – December 31, 2020)

The Brandes Emerging Markets Equity Strategy outperformed its benchmark, the MSCI Emerging Markets Index, in the fourth quarter.

Positive Contributors
In November, Pfizer and BioNTech announced positive results from their phase III trial, making the path to a COVID-19 vaccine clearer. The announcement catalyzed a sentiment shift for value-oriented securities and kicked off the portfolio's strong performance. Many cyclical-oriented companies, especially those competing in industries heavily impacted by the pandemic, benefited from increased investor optimism about their post-COVID prospects.

Within the portfolio, financial holdings such as Mexico-based **Banco del Bajio**, South African **Absa Group**, Indonesia's **Bank Rakyat Indonesia** and Thailand-based **Siam Commercial Bank** saw their share prices rebound. Banks had previously faced a major headwind to their earnings as new accounting rules required them to provision up front for expected loan losses. However, an improved economic outlook has led to lower loan loss provisioning expectations over the last few months, which helped alleviate investor concern.

Other contributors included Panamanian airline **Copa Holdings**, Brazil-based jet manufacturer **Embraer** and oil firm **Petrobras**, South Korean steel manufacturer **POSCO** and Mexico-based real estate investment trust (REIT) **Fibra Uno**. Furthermore, select technology-related businesses continued to perform well, led by China-based **Baidu** and information technology (IT) services provider **Chinasoft International**.

Performance Detractors
A few holdings in China hurt performance, most notably **China Mobile** and **Alibaba Group**.

President Trump's executive order prohibiting Americans from investing in companies with ties to the Chinese military sparked a sell-off in China Mobile's shares. At the end of the year, the New York Stock Exchange announced that it would start delisting China Mobile's American depositary receipts (ADRs) in early 2021. We are monitoring this situation very closely.

Meanwhile, Alibaba saw its share price decline after Ant Group, its affiliate digital payment platform company, unexpectedly had its initial public offering (IPO) cancelled due to intervention by the Chinese government. The government not only suspended what would have been the world's largest IPO, but also subsequently proposed new anti-monopoly regulations, which may jeopardize Ant Group's lucrative asset-light business model. We have long been cognizant of the risk of government involvement in China's internet companies and have incorporated this in our evaluation of Alibaba, a company that we believe does not represent a systematic financial risk and in fact plays an important role in the growth of China's economy. The share price correction essentially wiped out the value we attribute to Alibaba's stake in Ant Group, making it a "free" option for us. As of December 31, Alibaba traded at less than 20x earnings excluding net cash, its lowest valuation level since it went public in 2014. Given its growth potential and competitive position as China's leading e-commerce firm and one of the world's largest internet companies, we believe Alibaba offers an attractive risk/reward tradeoff for long-term investors. We added to our position amid the market selloff.

Our underweight to information technology, the best-performing sector within MSCI Emerging Markets, weighed on relative returns. From a country perspective, our underweights to South Korea and Taiwan also hurt returns relative to the benchmark. IT businesses make up a significant portion of the index's allocations to South Korea and Taiwan, making them the two top-performing countries within the index.

Year-to-Date 2020 Briefing
The Brandes Emerging Markets Equity Strategy underperformed the MSCI Emerging Markets (EM) Index for the 12 months ended December 31, 2020.

The period marked another challenging time for value investors, with typically value-oriented sectors, especially cyclicals (i.e., financials, energy), underperforming the overall MSCI EM Index. Value stocks in general (MSCI EM Value) have been a significant underperformer within the emerging markets equity space since 2012, and COVID-19 has brought on further obstacles, with companies facing declining demand as an immediate result of the pandemic feeling the brunt of the correction.

Specifically for the strategy, underweights to China, Taiwan, and technology-related businesses weighed heavily on relative returns. Additionally, several holdings operating in Latin America performed poorly as the region dealt with a challenging economic outlook and negative investor sentiment. Significant detractors included Brazil's Embraer, Mexico-based Fibra Uno and Banco del Bajio, Argentinian oil and gas company **YPF**, and Panamanian bank **Banco Latinoamericano de Comercio Exterior**. Beyond Latin American holdings, U.K.-domiciled event organizer **Hyve Group**, which we sold in the second quarter, hurt returns, along with China Mobile.

Notable contributors were mainly holdings in technology-related businesses, led by Chinasoft International, Baidu and Alibaba. Mexican cement company **Cemex also performed well** (especially in the second half of the year).

Current Positioning

The Brandes Emerging Markets Equity Strategy underwent a gradual transition over the course of 2020. Toward the beginning of the year, we reduced our exposure to Latin American companies after exiting a number of positions that had reached our estimates of their intrinsic values. As opportunities presented themselves during the early part of the pandemic, we took advantage of the market drawdown to purchase shares of companies that were, in our opinion, disproportionately discounted relative to their strong fundamentals. Through our buying activity, our exposure to companies in China increased, although we remained underweight the benchmark at year end.

We believe the portfolio is attractively positioned for a potential post-COVID recovery. A continued improvement in the fundamentals of our holdings and a re-rating of the companies' multiples could also provide a boost to the portfolio returns, as could the potential strengthening of emerging markets currencies against the U.S. dollar.

A strong fourth quarter has led many to question how much value stocks have caught up with their growth counterparts (MSCI EM Value vs. MSCI EM Growth) and whether this recovery is sustainable. While we do not know what will happen over the next year, we are optimistic that value stocks are currently well positioned for the long term given the significant tailwinds we started to see amid the rollout of vaccines, improved outlook for many value-oriented companies, and most importantly, the significant discount that value stocks continue to trade at relative to the market (MSCI EM) and growth stocks. At the end of the third quarter, MSCI EM Value traded among its greatest ever discounts compared to MSCI EM Growth based on price-to-earnings, price-to-book and price-to-cash flow multiples. Following value's outperformance in the fourth quarter, the discount levels for value relative to growth remained in their second cheapest ever percentiles, which we think continues to bode well for future returns. Given the portfolio's tendency to outperform MSCI EM Value when it outperforms the benchmark, combined with the prospects of earnings recoveries for value-oriented companies, we believe the Brandes Emerging Markets Equity Strategy is well positioned for long-term return potential.

Thank you for your continued trust.

Price/Book: Price per share divided by book value per share.

Price/Earnings: Price per share divided by earnings per share.

Price/Cash Flow: Price per share divided by cash flow per share.

Net Cash: Total cash minus total debt.

Operating Margin: Operating income divided by net sales; used to measure a company's operating efficiency.

The MSCI Emerging Markets Index with net dividends captures large and mid cap representation of emerging market countries. Data prior to 2001 is gross dividend and linked to the net dividend returns.

The MSCI Emerging Markets Value Index with gross dividends captures large and mid cap securities exhibiting value style characteristics, defined using book value to price, 12-month forward earnings to price, and dividend yield.

The MSCI Emerging Markets Growth Index with gross dividends captures large and mid cap securities exhibiting growth style characteristics, defined using long-term forward earnings per share (EPS) growth rate, short-term forward EPS growth rate, current internal growth rate, long-term historical EPS growth trend, and long-term historical sales per share growth trend.

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