BOSTON COMMON
ASSET MANAGEMENT

BOSTON
200 State Street, 7th Floor
Boston, MA 02109
CONTACT: Allyson O'Neill
tel (617) 720-5557
aoneill@bostoncommonasset.com

SAN FRANCISCO
225 Bush Street, Suite 1825
San Francisco, CA 94104
CONTACT: Ashley Lyon
tel (415) 813-1500
alyon@bostoncommonasset.com

# Emerging Markets Strategy Update

*Fourth Quarter, 2018*

## EMERGING MARKET REVIEW

The MSCI Emerging Markets Index (the "Index") finished lower (-7.5%) in the fourth quarter, but declined less than Developed Markets (-13.4%). The US and China reached a temporary trade truce at the November G20 Summit. However, positive sentiments, quickly faded, as global growth concerns worsened. Worries about the pace of US interest rate hikes also added to market volatility. Despite rising pessimism during the quarter, EM currencies were essentially flat against the US Dollar, with the Turkish Lira (+12.9%) and Indian Rupee (+3.8%) as the standouts. Among regions, Latin America (+0.4%) outperformed, followed by EMEA (-4.1%), while EM Asia (-9.3%) lagged.

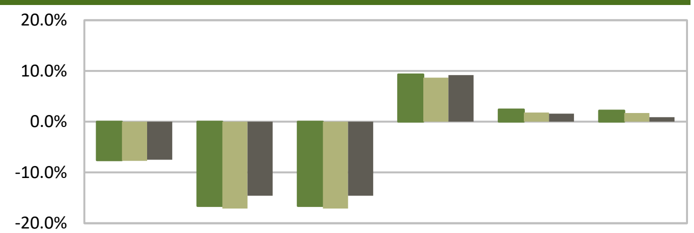
Brazil (+13.4%) was the best performing country this quarter, as investors celebrated the victory of right-wing candidate Jair Bolsonaro in the presidential election. Mexico (-18.8%), on the other hand, was among the weakest markets, as President Andrés Manuel López Obrador (AMLO) stoked investor fears with less than market-friendly policies. In Asia, tech-heavy countries Taiwan (-13.7%) and Korea (-13.1%) struggled, dragged down by the sharp equity declines in the US tech sector. China fell -10.7%; industrial profits and retail sales all slowed faster than expectations, confirming the country's slowing growth momentum. Southeast Asian countries fared better, with Indonesia (+9.7%) leading the pack. The Philippines registered a gain (+5.3%), as the country's inflation outlook improved. India (+2.5%) was quite resilient, even as Indian central bank Governor Urjit Patel surprisingly resigned and the ruling party (BJP) lost in three key state elections. In the EMEA region, Hungary (+5.9%) led the region's performance, supported by strong earnings growth. Russia (-9.0%) lagged, weighed by continued sanction pressures.

Utilities (+3.6%), Real Estate (+1.4%), and Financials (-0.9%) were the best performing sectors this quarter. Growth concerns weighed on cyclical sectors such as Consumer Discretionary (-11.5%) and Information Technology (-15.7%). Brent crude oil prices tumbled almost 40% during the quarter, pressuring the Energy (-10.6%) and Materials (-10.8%) sectors. Healthcare (-16.3%), despite its defensive characteristics, was the worst performing sector. For 2018 as a whole, the Index declined -14.6%, with Energy (+4.7%) the only sector to register a gain for the year.

## PORTFOLIO REVIEW

The Boston Common Sustainable Emerging Markets Equity strategy declined -7.6% for the quarter, before fees, in line with the Index. For 2018, the strategy returned -16.6%, underperforming the Index's calendar return of -14.6%.

## PERFORMANCE




| | QTD | YTD | 1Yr | 3Yr | 5Yr | Since Inception* |
|---|---|---|---|---|---|---|
| Gross | -7.6% | -16.6% | -16.6% | 9.3% | 2.4% | 2.2% |
| Net | -7.7% | -17.1% | -17.1% | 8.7% | 1.8% | 1.7% |
| MSCI EM | -7.5% | -14.6% | -14.6% | 9.2% | 1.6% | 0.9% |

## CONTRIBUTORS & DETRACTORS

| TOP 10 | % OF CAPITAL | RETURN | RELATIVE CONTRIB. | SECTOR |
|---|---|---|---|---|
| ITAU UNIBANCO HLDG SA | 3.0% | 24.5% | 0.84% | Financials |
| BANK RAKYAT | 2.5% | 20.1% | 0.60% | Financials |
| HDFC BANK LIMITED | 2.3% | 10.1% | 0.39% | Financials |
| BANK OF COMMUNICATIONS CO | 3.1% | 4.0% | 0.37% | Financials |
| PT KALBE FARMA | 1.7% | 14.1% | 0.34% | Healthcare |
| POLSKIE GORNICTWO NAFTOWE I | 2.5% | 5.7% | 0.31% | Energy |
| OTP BANK | 1.9% | 8.6% | 0.29% | Financials |
| DR REDDYS LABS LTD | 1.4% | 8.9% | 0.23% | Healthcare |
| ENN ENERGY HOLDINGS LTD | 1.8% | 1.3% | 0.23% | Utilities |
| HYPERA SA | 1.4% | 11.2% | 0.23% | Healthcare |
| | | | **3.82%** | |

| BOTTOM 10 | % OF CAPITAL | RETURN | RELATIVE CONTRIB. | SECTOR |
|---|---|---|---|---|
| SAMSUNG ELECTRONICS CO LTD | 5.2% | -16.6% | -0.54% | Technology |
| TAIWAN SEMICONDUCTOR MFG | 4.9% | -16.4% | -0.54% | Technology |
| GRUPO FINANCIERO BANORTE | 1.7% | -32.4% | -0.51% | Financials |
| ALIBABA GROUP HOLDINGS | 4.9% | -16.8% | -0.45% | Consumer Discretionary |
| PING AN INSURANCE GROUP CO | 3.4% | -13.3% | -0.30% | Financials |
| CTRIP COM INTL | 1.2% | -27.2% | -0.28% | Consumer Discretionary |
| SUNNY OPTICAL TECH | 1.4% | -23.0% | -0.27% | Technology |
| NEW ORIENTAL ED & TECH GRP I | 1.0% | -25.9% | -0.23% | Consumer Discretionary |
| HENGAN INTL GROUP CO LTD | 1.4% | -21.2% | -0.21% | Consumer Staples |
| RAIA DROGASIL SA | 1.4% | -17.4% | -0.19% | Consumer Staples |
| | | | **-3.52%** | |

Our underweight in Energy and stock selection in Consumer Discretionary and Industrials weighed on returns, while stock selection in Healthcare and Information Technology positively contributed to relative performance for 2018. For the fourth quarter, stock selection in the Healthcare sector was the largest contributor to relative results. Pharmaceutical companies PT Kalbe Farma (+14.1%) in Indonesia, Hypera (+11.2%) in Brazil, and Dr. Reddy's (+8.9%) in India all outperformed on solid earnings and stable business prospects. We also benefited from strong stock selection in the Energy sector, where Polish Oil & Gas company Polskie Gornictwo Naftowe (+5.7%) posted solid gains.

*Since Inception: December 31, 2012

The Financials sector provided another source of strength, led by Brazilian bank Itau Unibanco (+24.5%) and Indonesian Bank Rakyat (+20.1%). Taiwan and Indonesia were key contributors from a country perspective. Taiwanese industrial automation company Airtac outperformed (-1.0%), bolstered by early signs of its order book stabilizing.

Consumer Discretionary was the largest detractor from relative returns. Chinese online travel company Ctrip (-27.2%) and education provider New Oriental Education & Technology (-25.9%) declined after delivering weaker-than-expected earnings, as consumption slowed in China. Negative sentiment towards China also weighed on Chinese ecommerce giant Alibaba (-16.8%), despite its solid growth. Stock selection in the Consumer Staples sector held back relative returns. Chinese personal care company Hengan (-21.2%) dropped after short-sellers questioned the company's business model, despite credible rebuttal from management. Other notable detractors include technology company Samsung Electronics (-16.6%), Taiwan Semiconductor Manufacturing Company (-16.4%), and Mexican bank Grupo Financiero Banorte (-32.4%).

## PORTFOLIO ACTIVITY

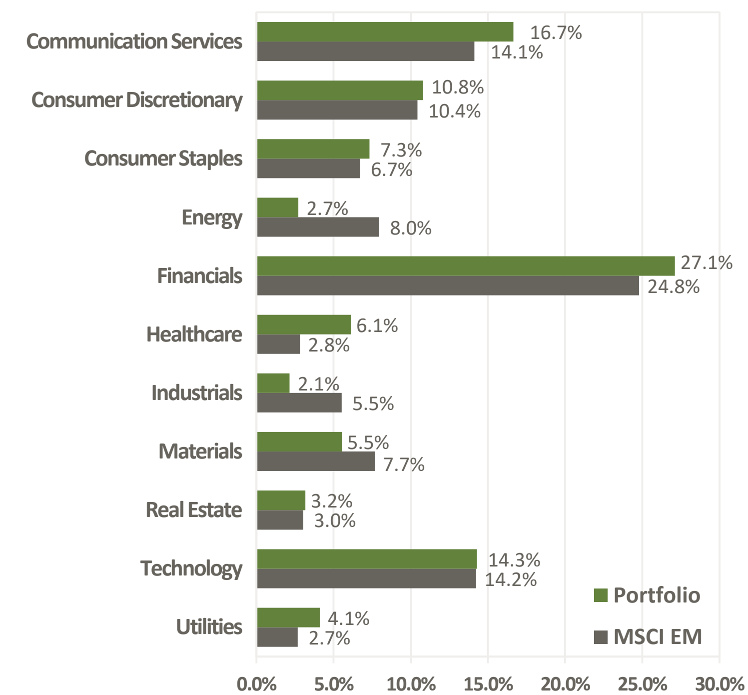
Among our portfolio actions this quarter, we purchased Noah, a leading independent wealth and asset management company in China. The high-net-worth industry in China has been growing double-digits thanks to fast wealth accumulation. The industry remains fragmented, with the top 10 commercial banks capturing only a 5% market share. Noah is well positioned to be an industry consolidator, underpinned by its high-quality franchise and comprehensive product solutions. It is also a key beneficiary of recent regulatory changes that may accelerate the exit of smaller players. Valuation has significantly corrected after the recent market sell-off, providing an attractive opportunity to participate in the structural growth of Chinese household wealth.

We also purchased Advanced Information Service (AIS), Thailand's mobile telecommunications company. With a dominant position in the Thai mobile market and fast launch of a fiber network, AIS should continue to deliver stable revenue growth with nearly 8% free cash flow yield. AIS performs strongly on sustainability practices by increasing access to communications in underserved Thai markets. It has launched a digital platform for sustainable agricultural development that enables farmers to access crucial farming information.

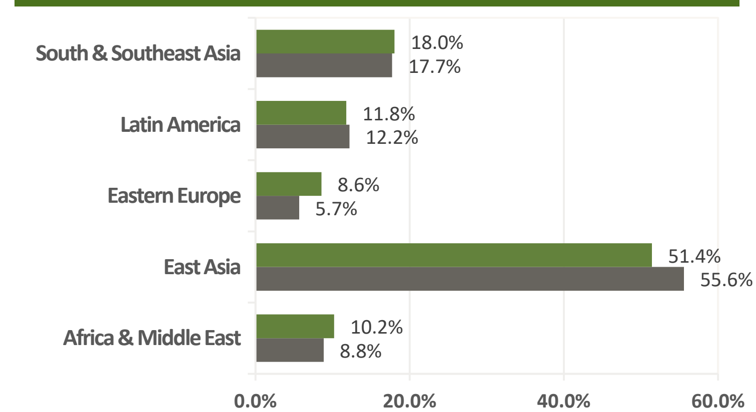
Another portfolio addition this quarter is Turkish bank Akbank. While we remain cautious about Turkey's macro fundamentals, we believe the worst is behind us and current valuation reflects excess market pessimism. In our view, Akbank's earnings will not contract as much as investors fear. With Akbank trading at its lowest price-to-book ratio in twenty years against an ROE of 25%, we see a favorable risk-reward balance.

During the quarter, we sold Hyundai Motor as the company continues to struggle in its key US and Chinese markets. We see limited progress by management to improve its corporate governance. Fundamentals no longer justify the current valuation, as the stock now trades at a premium to its five-year average after the recent rally.

## SECTOR ALLOCATION




## SUB-REGIONAL ALLOCATION




## PORTFOLIO CHARACTERISTICS

| | BOSTON COMMON | MSCI EM |
|---|---|---|
| # HOLDINGS | 53 | 1,125 |
| ***Valuation*** | | |
| Next 12m Price to Earnings | 12.9 | 11.2 |
| Price to Book Value | 1.9 | 1.6 |
| Price to Sales | 1.8 | 1.2 |
| Dividend Yield | 2.7% | 2.7% |
| ***Growth*** | | |
| 5yr Sales Growth | 6.6% | 4.0% |
| 5yr EPS Growth | 10.6% | 6.0% |
| ***Risk*** | | |
| Wtd Avg Mkt Cap | 70,164 | 78,813 |
| LT Debt/Cap | 24.1% | 24.4% |
| Beta | 1.03 | 1.00 |

# Emerging Markets Strategy Update
*Fourth Quarter, 2018*

## ECONOMIC & MARKET OUTLOOK

2018 was a year of global growth divergence, with the US economy surprising on the upside thanks to tax stimulus, while EM countries faced the headwinds from China's slowdown and a strong US Dollar. Looking ahead, we expect this divergence to reverse. US growth, while still solid, is likely to decelerate as tax benefits fade. Fewer prospective US interest rate hikes should help alleviate currency and funding pressures for Emerging Markets. Meanwhile, China's economy should gradually stabilize as government stimulus takes effect. Market volatility is likely to continue as trade tensions unfold and major central banks embark on interest rate normalization. However, we remain cautiously optimistic about EM equities, as we see a low probability of any major economy entering a recession in 2019. EM is now trading at 1.5x price-to-trailing book value, only 15% higher than previous trough levels of 1.3x seen in 2008 and early 2016. In our view, ample pessimism is reflected in current valuations.

Our portfolio continues to overweight domestically focused cyclical sectors including Financials and Consumer Discretionary. Mindful of the low but rising probability of a more substantial global slowdown, we offset this cyclicality with increased exposure to the defensive sectors of Healthcare and Communication Services. We believe having a higher-than-normal cash balance at this time allows us to eventually take advantage of any potential indiscriminate sell-offs in a volatile trading environment.

Our recent "boots-on-the-ground" research trip confirmed our view that the current slowdown in China is predominantly driven by the deleveraging initiatives undertaken by the government between late 2016 and mid-2018. During this period, the private sector suffered disproportionately more from the funding squeeze than state-owned enterprises. In early 2018, the Chinese slowdown was exacerbated by rising trade conflicts, complicating China's multi-year plan to improve economic growth. Policymakers have responded with tax cuts and measured infrastructure spending, while also easing reserve requirement for banks. Unlike past cycles, current efforts are focused on the private sector and on consumption. In our view, this is the right policy for the long run. However, in the short-to-medium term, such measures provide a less immediate boost to growth. If these efforts fail to stabilize the economy, China will likely expand its stimulus efforts. The growing antagonism in Sino-US relations may be a fixture for the future, but both parties appear willing to reach a trade settlement in the near term. A partial resolution could go a long way in unwinding economic and investor stress in China and beyond. Our exposure to China continues to focus on areas with sustainable long-term growth, including ecommerce and services, expanding consumer wealth, and industrial automation. Rising oil prices during most of the year, a depreciating Rupiah, and preemptive interest rate hikes have all pressured Indonesia's economic growth in 2018. We see early signs of improvement as these headwinds fade. In addition, social assistance and infrastructure spending ahead of the upcoming election should provide further support for the economy. The political outlook remains favorable, with a high probability that President Widodo wins re-election, a result that would be welcomed by investors.

## NEW & CLOSED POSITIONS

| CLOSED | SECTOR | % OF PORT. |
|---|---|---|
| HYUNDAI MOTOR CO | Consumer Discretionary | 1.0% |
| TOTAL CLOSED | | **1.0%** |

| NEW | SECTOR | % OF PORT. |
|---|---|---|
| ADVANCED INFO SERVICE PCL FOREIGN | Communication Services | 1.3% |
| AKBANK T.A.S. | Financials | 0.9% |
| NOAH HOLDINGS ADR | Financials | 1.4% |
| TOTAL NEW | | **3.6%** |

## COMPANY SPOTLIGHT: DELTA ELECTRONICS

### *Company Profile*

Based in Taiwan, Delta Electronics manufactures power management solutions. Founded in 1971, the company's product offerings include LED lighting and product display, energy monitoring software, electronic components for wind and solar power applications, and EV charging stations. The company has made great strides in reducing the environmental impact of its products through carbon footprint analyses, hazardous substance reduction, adoption of green packaging materials, and enhanced energy efficiency of products.

### *Investment Thesis*

As the largest power-supply vendor in the world, Delta is well positioned to meet the new demands that stem from key trends such as electric vehicle (EV) expansion, data storage, and industrial automation. Delta helps facilitate the transition to a low-carbon economy by offering highly energy efficient products in industries ranging from telecom to solar photovoltaics. Delta has also demonstrated commitment and success in improving the environmental footprint of its own operations, including the reduction of greenhouse gas emissions. The company's legacy business should provide stable revenues as it expands into higher-growth end markets. The potential for topline expansion through a focus on energy efficiency, improving margins as these growth initiatives strengthen, impressive sustainability reporting, and valuations in line with its historical averages make Delta a compelling investment opportunity. Risks include a deceleration in electric vehicle and industrial automation growth.

# Emerging Markets Strategy Update

*Fourth Quarter, 2018*

Since taking office in 2014, the current administration has adopted prudent policies to encourage infrastructure investment, lower logistic costs, and reduce external vulnerability. We remain optimistic about Indonesia's dynamic growth outlook and have further increased portfolio exposure.

Latin America's two largest economies will be guided by new populist leaders inaugurated at the end of 2018. Brazil's election came in the aftermath of a severe recession, social unrest, and a broad corruption scandal. Jair Bolsonaro swept to power with an anti-corruption mandate, despite campaign rhetoric espousing far-right social views. Expectations that President Bolsonaro will implement pro-market policies and pension reforms have excited make progress challenging, since Bolsonaro's Social Liberal Party only controls one-tenth of the seats in the lower house of Congress. In Mexico, current valuations appear to reflect investors' fears of the new AMLO administration's statist policies. AMLO has already made questionable infrastructure development decisions based on referendums with less than 1% voter turnout. Unconventional and unpredictable leadership tends to concern investors, but AMLO's record as mayor of Mexico City looks relatively favorable; he helped reduce crime, encouraged private-sector investment in housing, and implemented inclusive social programs. Our holdings in the region focus on domestic-oriented sectors such as financials, consumers, and healthcare, where companies benefit from secular demand growth but are still trading at attractive valuations.

## Shareholder Engagement Highlights

| | |
|---|---|
| *Milestones* | **Quantifying ESG Impact:** Boston Common has been recognized by Real Impact Tracker and the Real Leaders 100 for our ESG Impact. Third party certifications help keep investors informed and prevent "greenwashing" in the investment industry. Listen to a recording of the Real Impact Tracker webinar, featuring Lauren Compere, Director of Shareowner Engagement. |
| | **Strong Show of Support:** Our Lobbying Disclosure proposal **received a 28.2% vote in favor** at **Oracle** Corp.'s annual shareholder meeting. We called on Oracle to increase its transparency and accountability in the spending of shareholder resources. |
| *Work in Progress* | Our inquiries to **Albemarle** and **Sociedad Química y Minera**, lithium producers, on their water stewardship practices in Chile led to robust dialogues with senior representatives at both companies about their management of water usage, discharges, and site level assessments. We encouraged both to begin to respond to CDP Water to enhance their internal management systems and to adopt a global approach to managing water risks. We joined 60 investors with $6 trillion in assets asking companies to respond to CDP with Boston Common leading with Apache, ConocoPhillips, and Cimarex. |
| | As an extension of our **Banking on a Low-Carbon Future** work with large global banks, Boston Common joined forces with ICCR and its members to launch an engagement focused on 20 small cap and mid-cap US banks with letters sent in December. Boston Common is leading dialogues with **Associated Banc-Corp, First Horizon National Corporation, First Midwest Bancorp Inc., Fulton Financial Corporation, Moelis & Co., UMB Financial Corp, Union Bankshares Corp., Washington Federal, & Zions Bancorp**. |
| | **Advancing Engagement in Asia:** As part of our robust engagement program in Asia, we engaged senior representatives of **Beijing Enterprises Water** on its approach to sustainability disclosure and encouraged the company to take the next step and respond to CDP Water. We advised **Beijing Water** to include oversight and management of material ESG risks and begin reporting on objectives and targets related to water, energy, and waste reductions. As part of an investor inquiry to 22 ICT companies on digital human rights, we reached out to **Samsung Electronics** and **Tencent Holdings** after their evaluation by the Ranking Digital Rights 2018 Corporate Accountability Index on their disclosed commitments and policies affecting freedom of expression and privacy. |
| *New Initiatives* | **Plastics:** Boston Common is a signatory of the New Plastics Economy Global Commitment – which envisions a circular economy for plastic, where plastics never become waste. The commitment aims "to create 'a new normal' for plastic packaging. They will review targets every 18 months, and become increasingly ambitious over the coming years. Businesses that sign the commitment will publish annual data on their progress to help drive momentum and ensure transparency." |
| | **Ethical Recruitment:** Forced labor in manufacturing is a material risk for the Information and Communications Technology (ICT) sector. Risks include: the potential use of migrant workers paying high recruitment fees, the retention of identification documents, and the use of forced or child labor. We joined ICCR in backing the findings of the KnowTheChain's 2018 Benchmarking Report on Forced Labor in the ICT sector which rated 40 ICT companies on each company's approach to reducing exploitation and protecting the rights of workers in their supply chain. Boston Common led inquiries with **Analog Devices, Hoya, Infineon, Keyence, Nintendo, & TE Connectivity.** |