

Artisan Partners Emerging Markets Team

Investment Philosophy and Process

Artisan Emerging Markets Strategy

A R T I S A N



P A R T N E R S



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Our investment team combines the benefits of extensive emerging markets experience with the continuity of a disciplined investment process.

Artisan Partners Emerging Markets Team

Our Investment Team

Team experience, continuity and a rigorous investment process are the characteristics that we believe differentiate our team from other emerging markets investment managers.

We believe experience is extremely critical in this asset class. Our experience comes not only from the length of time we have spent investing and managing money in these markets, but also from several of our team members having been born and raised in emerging countries. For example, portfolio manager Maria Negrete-Gruson is from Colombia and analysts Chen Gu and Nicolas Rodriguez-Brizuela grew up in China and Argentina, respectively.

Our first-hand experience is important on many levels. It truly shapes our perspectives of emerging markets on an ongoing basis. In our view, the keys to successful active management in this asset class are insight and good judgment, not quantity of information. As such, we take an indigenous approach to researching companies for potential investment, focusing on those with the most direct and concentrated exposure to long-term secular growth trends.

When asked how a team of six people can handle the vast and changing world of emerging markets, a significant part of our answer is experience. Our analysts bring deep experience and uncommon insight to their

respective areas of responsibility. They have autonomy and ownership of their areas of research coverage and complete accountability for the success of their ideas. No bureaucratic or hierarchical impediments dilute our ability to get ideas into the portfolio on a timely basis. This ownership and accountability is one of the key reasons our analysts remain committed to our team.

What's more, we like to say that no communication gets lost in translation in our team. Communication between team members is open and effective, which is partly attributable to our modest size but also because of the way in which we divide the universe. We try to avoid silos of knowledge. In other words, we try to avoid one person knowing all about one small corner of the world and not focusing on anything else. When an analyst discusses an investment thesis with a colleague, both benefit from the interaction, which often leads to additional insights.

We developed our investment philosophy back in 1999 at a previous firm. When we joined Artisan Partners in 2006, we continued to execute that same approach. We consider the continuity of our process—now in place for more than 17 years—an important attribute. Our rigorous investment process has been tested throughout a number of market conditions, and we have seen how it responds to different stresses in the market. This

history gives us the confidence to remain calm and focused during adverse periods. Our emphasis on long-term fundamentals and discipline around valuation can result in our performance being out of sync with the market during periods of euphoria or panic. However, we believe remaining disciplined to our investment process is the best way to compound assets over the long term.

Our Investment Philosophy

Given our backgrounds and extensive experience, we ask ourselves, “What do we know about emerging markets?” In answering that question, we postulate two things. First, we know emerging markets are growing and we believe they will continue to provide growth in excess of developed markets over the long term. Our second core belief is that emerging markets will remain turbulent. We never subscribe to the idea that “this time around it will be different” or that emerging markets have graduated or decoupled. We believe inherent volatility is the nature of investing in emerging markets. In summary, we know that emerging markets have potential to provide attractive growth opportunities over the long term and that it is going to be a bumpy ride.

So, what qualities do we look for in companies? The first quality we look for is *unique access to growth*. We already believe emerging markets have growth potential beyond that of developed markets, so we try to avoid what we call the “lucky companies” or the “one-day flowers” in emerging markets, which are companies that have relatively easy access to general growth within their space. What we are truly interested in are companies that take advantage of a growth opportunity and develop a business model around it, allowing them to translate the growth of today into sustainable growth and sustainable earnings. In other words, we are interested in growth but we are interested in growth that can be sustained.

The second quality we look for is a *sustainable competitive advantage*. Because we know the environment in which these companies operate is going to change rapidly, we look for companies that have a sustainable competitive advantage in markets where they compete. Good and bad times are going to come and go, and we know that in the face of a crisis most stocks are going to go down. We believe sustainable competitive advantages are key to a company’s ability to survive in times of crisis. A sustainable competitive advantage might be weakened in times of crisis, but not destroyed.

Idea Generation

When discussing idea generation we think it is important to mention what we are looking for—and what we are not trying to accomplish. Our goal is to develop high conviction in a portfolio of stocks well diversified by country and sector. To do that, we meet with several hundred company managements each year and maintain a research library of several hundred stocks that have the essential characteristics we seek. We have no desire to develop an opinion about every stock in the investable universe, particularly because many companies lack the advantages we desire. As a result, we do not need analysts on the ground in each market, nor do we need to react to every potential opportunity. To the degree that our stocks, in which we have deep knowledge and conviction, achieve the upside we have estimated, we are highly confident that the portfolio will be well positioned to deliver superior performance results over the long term.

The bulk of our ideas come from our travels around the world. We meet with hundreds of companies each year, seeking evidence of our requisite advantages. We do not believe that any universe screening process could identify in advance the critical characteristics we seek. Nothing can replace the travel that our team does on a regular basis to meet with companies in their natural habitat. Although we like to say we “kiss a lot of frogs,” we have high conviction that our approach has significant advantages over quantitative screens.



Core Investment Beliefs

We believe that certain companies in emerging markets possess:

- Unique Access to Potential Growth
- Sustainable Competitive Advantages

We know that emerging markets have potential to provide attractive growth opportunities over the long term and that it is going to be a bumpy ride.

The goal of our process is to identify companies that are undervalued relative to their sustainable earnings growth potential.



Financial Analysis

Balance Sheet, Income Statement and Cash Flow analysis lead to:

- 5-Year Financial Forecast
- Analyst Estimates—Earnings Power, Return on Equity, Book Value

Our Investment Process

When we find a company that we think possesses unique access to potential growth and/or a sustainable competitive advantage, we move forward using our rigorous investment process to determine if the opportunity is right for our portfolio. The goal of our process is to identify companies that are undervalued relative to their sustainable earnings growth potential. The first step in our process is to determine what sustainable earnings are for the company. We define sustainable earnings as sustainable return on equity (ROE). Why ROE? Because it is simple—ROE is made up of margins, turnover and leverage. Those are terms that are familiar to us and to the management teams of the companies in which we invest around the globe. For us, it is important to speak the same language when it comes to understanding profitability. Ultimately, we are equity investors, so we like companies that focus on profitability from the equity point of view.

The next step is determining what “sustainable” means in the context of emerging markets and that can be tricky. Because of the recent emergence of many countries, industries and companies, we do not always have the opportunity to analyze numerous historical cycles. As a result, our research hinges on an estimate of ROE that we believe is sustainable—incorporating the underlying growth opportunity as well as the volatility around it.

Financial Analysis

The first part of our process is financial analysis, which is time consuming but critical. We start by doing a historical financial analysis of the income statement, balance sheet and statement of cash flows. Our focus is on gaining an understanding of the main drivers of how a company makes and spends its money. It is easy to travel to some emerging markets countries and fall in love with top-line growth because the story sounds picture perfect from the perspective of company management. But we have to come back and reconcile that great story with reality. Sometimes companies are great at telling their story and growing the top line at a high level, but if you look closer, you sometimes find they have done this at the expense of blowing out their balance sheet, or taking on too much debt, or diluting their shareholders trying to grow too fast. These are issues you cannot see unless you do a line-by-line analysis of the historic financial statements of the company. This is the biggest step we undertake in our process.

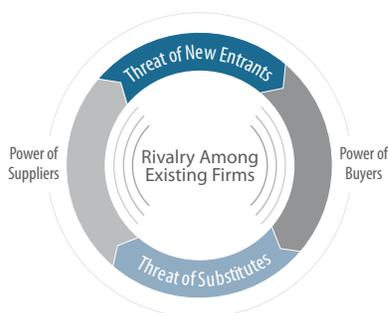
After we complete a historical financial analysis, we develop a five-year forecast for each financial statement: balance sheet, income statement, cash flow and ROE breakdown. The goal of this forecast is not to have earnings per share (EPS) estimated to the exact basis point five years out. The purpose is to truly look at a company as a going concern and to understand the drivers of its success. We are not interested in companies one day and then gone the next. We want to buy a company and hold it for the long term and to do this we need to understand the company and its financials in a long-term context. Ideally, we will discover a company that has built a sustainable framework for delivering solid results into the foreseeable future.

Once we analyze the historical financial analysis and five-year forecast, we have a true understanding of the financial situation of a company. However, the numbers alone will not get us to the sustainable earnings, so we perform an in-depth strategic analysis.

Strategic Analysis

For our strategic analysis, we conduct a Porter’s Five Forces competitive analysis and a thorough corporate governance assessment. The Porter’s Five Forces Analysis gives us a framework to assess the industry in which a company competes. So we look at a company’s buyers, suppliers, competitive rivalry, the threat of new entrants and the threat of substitutes. We score each of those factors, which

helps us assess sustainability. For example, take a supermarket in northern Mexico that is doing great in that territory. That in isolation would be a good story, but when you conduct Porter's Five Forces analysis, you may come to find out that other competitors are about to move aggressively into that same territory. If this were to happen, the supermarket could not assume its operating margins are going to be sustainable if it has to aggressively compete with a new player in the market. So the Porter's Five Forces analysis is important in our assessment of sustainability and in our understanding of the industry in which the company competes.



Our corporate governance assessment looks at a variety of factors that we believe have the potential to materially impact a company's sustainable growth potential. Our goal in this assessment is to answer critical questions that help us vet a company's management team and corporate practices. After a thorough examination of all factors, we typically apply a premium to our estimated target price for companies that exhibit exemplary corporate governance practices, while we discount our price targets for companies where corporate governance issues result in a higher risk profile.

Assessing Sustainability

- Board composition
- Alignment of interests
- Minority voting rights
- Historical behavior towards minority shareholders
- Consistency of dividend policy
- Management assessment and turnover
- Quality of disclosure
- Quality of communication
- Environmental and social considerations

During our meetings with company management, we focus on the long-term elements of our financial analysis, coupled with our Porter's Five Forces analysis and corporate governance assessment. Before we award a company a high sustainable ROE, we need to have conviction that a sustainable competitive advantage or unique access to growth exists that can withstand erosion. We are attracted to management teams who have a long-term vision of how they will preserve and enhance a company's position to defend that ROE. So the Porter's and corporate governance evaluations, together with our financial analysis, provide us with the information necessary to determine the sustainable earnings potential of a given company. This is a rigorous process, but we believe the journey is as important as the destination.

Country Risk Assessment

Once we determine the sustainable earnings for a company, we move on to our country risk assessment, which is an important element of our process. As a part of this analysis, we evaluate multiple macroeconomic factors that are relevant for each country. The reality is that emerging markets countries are in very different places in their economic, social and political development, and not all countries face the same risks. Additionally, we believe it is vital to compare a country's risks to its own history, identifying improvements or deterioration over time and assessing how those factors may impact a company in which we are interested.



Our goal in assessing country risk is to estimate the impact that certain factors may have on a particular company.

Portfolio Construction

We typically own a portfolio of stocks well diversified by country and sector.

Sector and industry weightings are always the result of our bottom-up stock selection process. We make no top-down decisions based on sectors. In terms of country exposure, we believe it is a mistake to make large country bets, especially given the fact that we are bottom-up stock pickers. In our portfolio, we have exposure to a country because we believe those individual stocks deserve to be in the portfolio. If we do not think individual stocks deserve to be in the portfolio we will not invest in them, which may leave us completely out of a country.

Below are a handful of guidelines and constraints employed to manage the risks inherent in any investment portfolio constructed through fundamental stock selection:

Artisan Emerging Markets Strategy

- Typically 70-90 holdings
- Maximum position size generally 5%¹
- Limit +/- 10% of any one country's weighting in the MSCI Emerging Markets Index¹
- Minimum of \$400 million market capitalization¹
- Typically less than 5% cash

Based on a model portfolio. ¹Limitations apply at the time of purchase.

It is important to note that our country risk assessment is not a beauty contest—we are not trying to compare one country to another (e.g. Thailand versus Mexico). An additional key distinction about our country risk analysis, which may differ from other emerging markets managers, is that we do not use it to select or avoid countries from a top-down perspective.

We believe the most effective way to manage risk is through our bottom-up stock selection process. Our goal in assessing country-specific risks is to estimate the impact that certain factors may have on a particular company. For example, the risks associated with a company whose business is primarily exports may be more related to the export countries rather than the company's own country of domicile. Similarly, a vulnerable currency in an exporter's home country may work as an advantage rather than a liability. Finally, many companies are exposed to risk from multiple countries. Our goal is to examine relevant country-specific risks, adjust our expectations for ROE and determine how much we are willing to pay to own the shares. In short, we make a qualitative assessment of how macroeconomic risks in each country may impact an individual company.

Valuation

The final step in our investment process is determining an appropriate valuation for a company. To arrive at a target valuation, we consider country risk, valuation relative to the company's peer group and relative to its own history, as well as company-specific factors. Once we have a normal sustainable ROE and a target valuation, we are able to determine a price target for that security.

Target Price

We apply a straightforward approach to determine a target price for each security. We multiply our sustainable ROE estimate by a company's stated book value, which we take from its financial statements, to calculate the Normal Earnings Per Share (NEPS). We then assign a target price-to-earnings (P/E) multiple we are willing to pay for that earnings stream. By multiplying the NEPS by the target P/E, we calculate a target price. We compare the target price to the current market price to determine the estimated upside. Our goal is to buy companies that exhibit at least 20% upside at the time of purchase.

We also calculate the weighted average upside of the entire portfolio, which serves as a useful barometer of the broader opportunity set. For example, during a period when prices across the asset class are meaningfully depressed, our average upside in the portfolio may be extremely high. For example, assume our average upside is 100%. A stock candidate showing 20% upside in that environment would not be that interesting. However in an environment where the portfolio's discount is lower, it serves as a more useful benchmark in evaluating current opportunities. This also serves as a good example of the fact that we evaluate upside calculations both on a company basis and against competing opportunities.

Our focus on target price leads to a simple sell discipline. We sell stocks when their upside reduces to a small or negative amount. Ideally, this occurs because a stock appreciates substantially, but sometimes a reassessment of a company's fundamentals or overall reduction in market sentiment causes us to reduce our sustainable ROE or target P/E, which results in a lower upside estimate. It should be noted that stock appreciation does not automatically result in sales. Each period of growth resulting in a higher book value creates better upside. In addition, we sometimes increase our sustainable ROE or target P/E estimates, which also increases the upside estimate. Although some judgment is applied to the inputs that determine our target price, we are highly disciplined about selling stocks that have little upside and maintaining a portfolio with as much upside as possible, consistent with our investment guidelines.

International investments involve special risks, including currency fluctuation, lower liquidity, different accounting methods and economic and political systems, and higher transaction costs. These risks typically are greater in emerging markets. Such risks include new and rapidly changing political and economic structures, which may cause instability; underdeveloped securities markets; and higher likelihood of high levels of inflation, deflation or currency devaluations. Securities of small- and medium-sized companies tend to have a shorter history of operations, be more volatile and less liquid and may have underperformed securities of large companies during some periods. Investments will rise and fall with market fluctuations and investor capital is at risk. Investors investing in strategies denominated in non-local currency should be aware of the risk of currency exchange fluctuations that may cause a loss of principal. These risks, among others, are further described in Artisan Partners Form ADV, which is available upon request.

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Return on Equity (ROE) is a profitability ratio that measures the amount of net income returned as a percentage of shareholders equity. **Earnings per Share (EPS)** is the portion of a company's profit allocated to each outstanding share of common stock. **Price-to-Earnings (P/E)** is a valuation ratio of a company's current share price compared to its per-share earnings. **Book Value** is the net asset value of a company, calculated by total assets minus intangible assets and liabilities. **Competitive Advantage Framework (Porter's Five Forces)**—Porter's Five Forces model is used to develop an industry assessment for a company. This framework evaluates the structure of the company's industry by considering the nature of the competition, the balance of power between the company and its suppliers and customers and the elasticity of demand for the company's product versus substitutes. Each element is scored on a five-point scale (the higher being the better). Adapted with the permission of The Free Press, a Division of Simon & Schuster Adult Publishing Group, from *COMPETITIVE ADVANTAGE: Creating and Sustaining Superior Performance* by Michael E. Porter. Copyright © 1985,1998 by Michael E. Porter. All rights reserved.

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A R T I S A N



P A R T N E R S