YEAR-END SHAREHOLDER LETTER

31 December 2020

Dear Shareholder,

Happy New Year!

This letter is set out in three parts: investment performance in 2020 including key contributors, the impact of Covid-19 and its effect on our companies, and finally an update on the Fund's[1] Manager, Genesis Investment Management, LLP.

The pandemic has made 2020 a challenging year for many. While stock market returns have been strong, such indices are not a measure of human experience, and we know families across the world have found the year particularly difficult. We hope you and yours are in good health. And we wish you the best for 2021.

Investment Performance

In 2020 the Fund gained 13.1% net of fees in sterling terms. This performance was behind that of the MSCI Emerging Markets ("EM") Index, which returned 15.0%. Absolute returns have been strong and, frankly, surprising, given the pandemic. Overall, 2020 was a year that did not favour our consistent approach of managing a diversified portfolio of good quality businesses. A narrow set of stocks dominated index performance for much of the year and the Fund's more diversified portfolio, despite some strong stock selection, could not quite keep up.

This narrow index performance is partly explained by north Asia's particularly effective response to the Covid pandemic. Markets seemed to reward this as China, South Korea and Taiwan, which by year-end collectively account for two-thirds of EMs by index weight, together returned 31% in 2020. Other EMs declined 7% during the year. The Fund, which has long had a relatively larger share of investments outside north Asia with a particular emphasis on earlier stage or frontier markets, suffered, we expect temporarily, due to this allocation gap.

In 2020, markets were—in what we see as an anomaly—for the sixth consecutive year led by larger capitalisation stocks. The four largest index components—Alibaba, Tencent, TSMC and Samsung Electronics—together returned 40%. We like these stocks, but don't have the exceptional level of conviction that would be required to sell other compelling investments to buy them to a portfolio weight higher than the 22% they represent in the index. Our approach, which weights investments according to fundamental attributes, has us with a cumulative 17% allocation. In 2020, our positioning in the top four index giants contributed just over one-third of the total 13.1% return, but inevitably this detracted from relative performance and cost 100bps of alpha.

[1] Genesis Emerging Markets Fund Limited

Within countries, in 2020, our investments generally outperformed, reflecting good stock selection. In China, our investments returned 33% or seven percentage points over the index. In India we were also seven points ahead; in Russia and Taiwan 30 points.

Chinese milk and alcohol added 360bps

The holdings in baijiu producers Wuliangye and Jiangsu Yanghe generated strong returns of 130% and 127%, respectively, and milk producer Mengniu's stock price rose 46%. 2020 was the second amazing year in a row for Wuliangye, which contributed 190bps[2] of investment performance. Pandemic-control measures led to the cancellation of many consumption occasions for baijiu including large banquets, but a strong pricing architecture and surprisingly resilient underlying demand meant that we reduced earnings estimates only slightly. Wuliangye started 2020 on 24 times our 2020 estimates and ended the year on 50 times, which partially reflects exuberance in Chinese capital markets. We cut the size of both baijiu investments by a total of 250bps during the year to reflect these more demanding valuations.

Strong returns from EM digital business including Yandex and Naver

While the largest digital businesses in EM, including Alibaba and Tencent, saw their stock prices surge in 2020, smaller local digital leaders Yandex and Naver also did well. Yandex is the largest internet business in Russia with the leading search engine, online ride hailing and a host of other ventures. The pandemic sped up digitisation trends globally, and Yandex as a well-managed business has capitalised on that. Despite ruble weakness, Yandex returned 55% during 2020, contributing 65bps to performance. Similarly Naver, the dominant search engine in South Korea and, through Line, the dominant messenger service in Japan, Taiwan and Thailand, rose 62% in 2020, adding 70bps.

Portfolio positioning in SOEs drove substantial alpha

In EM investing a persistent success factor is healthy alignment with capable business executives. One of our portfolio themes is avoiding SOEs that, due to political considerations, do not serve minority investors very well. We don't have a blanket ban on them and are happy to invest where we feel management is capable and well-aligned despite state ownership – Wuliangye is a good example. Indeed, businesses with some state ownership make up 15% of our portfolio versus 25% for the index. The larger SOEs in the index, exemplified by Chinese banks and Russian gas companies, returned a negative 6% in 2020, while our state-owned holdings gained 29%. The gap produced 750bps of alpha.

Bank stocks performed worse than many other sectors

Given inherent credit exposure to the pandemic's depressive effect on economic growth, it is hardly surprising that bank stocks performed poorly in 2020. Overall, the Fund's bank investments, which comprised 14% of the portfolio at year-end, declined less (-6%) than those in the index (-13%). We consider this a good result in that the banks we hold are disproportionately in earlier-stage EMs that have suffered more from movement restrictions, while we don't own the north Asian banks that are the index heavyweights. That said, 2020's largest single stock detractors for the Fund's portfolio were mostly banks. The most painful was Sberbank, Russia's dominant lender, and a 3.3% portfolio position, which fell 6% during the year, detracting 90bps. However, when banks have a tough time the good ones tend to nibble market share and can emerge stronger for the next cycle. This is where we feel our banks are today.

---

[2] Attribution data are calculated relative to the MSCI EM Index return without reference to stock index weights.

Small cap and frontier investments dragged

We believe that over time clients benefit from investments in smaller businesses and earlier stage emerging markets outside the MSCI EM Index, primarily because these stocks may be priced less efficiently and their growth runways may be longer. During 2020, however, probably because these areas were more impacted by the pandemic, portfolio small cap and frontier investments returned -9% and +5%, respectively. The largest single stock impact was the Caribbean communications service provider LiLAC (-43%), which suffered from high economic exposure to tourism and substantial financial leverage. Overall, small caps and frontier investments detracted 200bps and 55bps, respectively, from relative performance.

Healthcare sector investments were impacted and detracted 190bps

Within the promising EM healthcare sector, our main investments are in hospital groups including Bangkok Dusit and Mediclinic. Bangkok Dusit is the larger holding, starting the year at 1.7% and falling 21% over the year. The family-controlled company is the dominant private hospital operator in Thailand, and we see a valuable growth runway as the population ages and medical tourism increases. But in 2020 medical tourism and even many domestic elective procedures were postponed, and near-term earnings expectations have been trimmed. Despite this, we continue to believe the post-Covid outlook is bright.

Covid Impact

Covid-19 has had a significant effect on the investment landscape, and like the virus in humans it has hit some countries worse than others. In its October 2020 World Economic Outlook, the IMF estimates 2020 GDP will have fallen on average in EMs by 3.3%, compared to almost 6% in advanced economies. GDP in north Asia will have grown very slightly; ASEAN, Eastern Europe and lower-income countries in Africa declined around 3%, while the economies of India, Latin America and South Africa are forecast to have shrunk by 6%-9%. The recovery in 2021 will mean, according to the IMF, that EM growth should rebound by 6%, with India, China and southeast Asia leading the way with 8%, and most other EMs growing 3%-4%.

At the start of the pandemic we were concerned that the macro-economically vulnerable countries could suffer disproportionately if their already stretched budgets rose further to support incomes or healthcare. In the event, fiscal balances have deteriorated almost everywhere in the world, with EM deficits around developed country levels. However, many EM governments are committed to cutting the extra spending when they can – in other words pursuing economic orthodoxy – and the likely return to economic growth in 2021 gives an exit. Notable exceptions are Brazil and Turkey, which suffered from poor policymaking before Covid-19 and whose currencies have since lost over 25% against the US dollar. There are, however, longer-term questions over rising debt levels in many places, particularly China, which added 25 percentage points of GDP to its total debt in 2020, and has the highest debt-to-GDP among EMs (280% by the end of June according to the BIS).

Effect on the Fund’s Companies

For certain companies Covid has had a ripening effect. Any activity that involves playing with your phone has rapidly matured almost everywhere in the world, so that ecommerce and digital payments, especially in less penetrated places like Indonesia or India, have seen at least two years of growth crammed into one. Even highly connected Korea took another step into cyberspace; Naver most recently reported shopping GMV rising by a third. The sudden shift in consumer behaviour is affecting investment plans – many of the Fund’s companies are intensifying their digital effort, even in places that were addicted to cash. Companies that were ahead of the competition in digital capability before Covid are now reaping the benefit; in Indonesia in the first nine months of 2020 BCA was able to cope with 40% more transactions than a year earlier because they had invested so single-mindedly in digital capacity.

Many FMCG and retailing companies outside north Asia, which comprise 11% of the portfolio, have been relishing the less competitive environment. Strong companies have exploited the scramble for working capital and shorter payment terms and they can more easily fill the shelf space left by smaller companies that are struggling with logistics. In the Philippines, Puregold has gained share by giving the mom-and-pop Sari-Sari stores extended payment terms, becoming their go-to supplier. The Indian small appliance company Crompton recently reported sales growth of 13% yoy, taking share from small, unorganised competitors that were short of money. Other consumer companies have been investing through troubled times using balance sheet strength and superior profitability. 2020 gave a great opportunity for offline retailers to bargain for lower rents and grab space – Mobile World in Vietnam has doubled its grocery footprint in the last year and Quero-Quero, the Brazilian home improvements retailer, increased stores by 14%. Online retailing is the big winner from events in 2020, but the better offline retailers are not wasting the opportunity to consolidate. Continued innovation when your competitors can't keep up is another form of investment, and Godrej Consumer in India has demonstrated this agility by launching products in new categories such as bathroom and floor cleaners, disinfectants, and air fresheners.

Some of our companies with stable business models have been quietly motoring through 2020 and are looking remarkably attractive in terms of valuation. Kimberly-Clark de Mexico (1.1%) has over 50% market share in diapers and toilet tissue, and while premiumisation has taken a back seat in 2020, this is what makes the growth outlook exciting as the market matures. Kimberly-Clark has market-leading returns on capital and a disciplined and aligned management team, but you wouldn't know it from the current share price, which values the business around 15x earnings. Similarly WH Group in China, the world's largest pork producer after buying Smithfield in the US, recently reported domestic sales up 33% and despite mid-teens ROEs the stock is trading on just 8x 2021 earnings. These, and some less well-known names in the portfolio, appear to have been left behind by the latest market surge.

The 7.5% portfolio exposure to companies outside north Asia which serve customers "on premise" has had a challenging 2020, but appears well set for 2021. Much of this exposure is in beer, Heineken being the largest holding at 2.1%, and the foodservice distributor Bidcorp at 1.4%. Around 85% of Bidcorp's business is selling ingredients to bars and restaurants, and around half of the beer drunk in emerging markets is with friends on-premise. Lockdowns are therefore a major challenge. But the last nine months have also shown the strength of pent-up demand, so when people can go out they do: in early April Bidcorp's sales fell to just 37% of the corresponding week in 2019, but had jumped to 65% by the end of May and 87% by the first week in August. Beer has benefited from a unique set of circumstances that has led to up-trading as people buy premium beer to take home – before Covid premium beer was mostly consumed on-premise. Home drinking has also accelerated the trend for low-and-no alcohol beer, which is good for margins given no excise tax. Heineken is the leader in premium and low-alcohol beer in most of its markets, which has helped it to win share.

The Fund's holdings (excluding financials), even in places more affected by Covid, that is, countries outside north Asia, have grown their sales around 3% on average in 2020 – a strong performance in the circumstances. 2021 will be a recovery year: we estimate revenue growth for the portfolio will accelerate to 19%. The portfolio is in fact showing an attractive five-year IRR of nearly 10% annualised in US dollars. Our companies have on the whole exploited the difficult environment and used their superior franchise and balance sheet strength to expand market share. They should now be in a stronger position as we exit the disruptions caused by Covid.

The Fund's diversified portfolio typically performs better when small- and mid-capitalisation stocks do well. The last six years, during which we have beaten the index, have seen us battling a heavy relative performance headwind. In each year from 2015 to 2020, the capitalisation-weighted MSCI EM Index has outperformed its equal-weighted version. The cumulative return gap over those six years is 18%. This large cap performance skew is historically anomalous.

Business Update – Genesis Investment Management, LLP

The investment team and staff of Genesis have done us proud in 2020 despite working from home for most of the year. Morale is strong and we have invested in our people, recruiting a couple of new faces and promoting some strong team members. Of those, clients will know Arindam Bhattacharjee, who became Managing Partner in June, Xing Hu, who has been with us since 2018 and joins the Partnership in January 2021, Marguerite Mills, Head of Investment Governance, who becomes Associate Partner in January 2021, and Martina Jersakova, Senior Relationship Manager in the Client Team, who joined in October. Martina has over a decade of experience, most recently at Baillie Gifford in Edinburgh. She holds a degree in Business Studies from the University of Edinburgh and is a CFA Charterholder. She is part of our five-strong Client Team who are all looking forward to meeting you, we hope in person, in 2021. Finally, Karen Roydon will be appointed to our governing board (the GIM Operating Board) as soon as we receive regulatory approval from the FCA.

Diversity has shot up the agenda in clients' questions in 2020 and it deserves comment here. As investors we embrace diversity because it means better decision-making – in our investment team of 12 we have eight nationalities speaking 10 languages – and in the organisation more broadly we have 17 nationalities and 14 languages. In terms of gender, women represent 45% of our workforce and four of 16 Partners or Associate Partners. We are convinced that our business is enriched by this diversity, and that drawing on a wide variety of backgrounds leads to more informed decisions.

ESG is also continuing to gain recognition in EMs both with investors – what we and our clients demand – and with the companies themselves, where real change happens. In 2020 we strengthened the links in our ESG chain so the stakeholder analysis informs all stages of an investment and we now systematically track engagements and assess outcomes. Marguerite as Head of Investment Governance works closely with our Portfolio Managers to advise on regulatory developments, help us assess best practice and encourage companies to improve. We published our inaugural ESG report earlier in the year, which is uploaded on the Fund's website and details our ESG activity, and we are working on the 2020 edition.

Conclusion

The foundations of our long-term success remain in place. Our active investment strategy of undertaking deep fundamental research to unearth long-term investments in quality businesses at attractive prices remains as relevant today as ever in EM.

Important Regulatory and Risk Information

This document is issued by Genesis Investment Management, LLP ("Genesis"), which is authorised and regulated by the Financial Conduct Authority ("FCA"). Registered office: 21 Grosvenor Place, London SW1X 7HU. Registered in England, number OC306866. A member of the Investment Association.

All investments and services mentioned are directed at persons who are Professional Clients or Eligible Counterparties as defined by the FCA and to persons falling within the Financial Services and Markets Act 2000 (Promotion of Collective Investment Schemes) (Exemptions) Order 2001. This document should not be relied upon by Retail Clients. It does not constitute investment advice and should not be used as the basis of any investment decision, nor should it be treated as a recommendation for any investment. Under no circumstances should any part of this document be construed as an offering or solicitation.

Past performance should not be relied upon as a guide to future performance, which is not guaranteed. The value of investments can go down as well as up and there is no guarantee that you will get back the amount originally invested. Your investment should be viewed as long-term. Genesis invests in emerging markets which tend to be more volatile than more established stock markets and therefore your investment is at greater risk. You should be aware that currency movements can affect the value of your investment. Other risk factors such as political and economic conditions should also be considered.

This document has been prepared by Genesis on the basis of information and sources believed to be reliable. Index performance calculated by Genesis is based upon index values supplied by MSCI. Other statistics in this document are from a variety of publicly available information obtained through Genesis' research. This document is not intended for distribution to any other person and may not be reproduced in whole or in part without the prior consent of Genesis.

For information on how Genesis processes personal data, please refer to www.giml.co.uk and click on the Privacy Notice link.

Genesis Investment Management, LLP
21 Grosvenor Place
London SW1X 7HU
United Kingdom
Telephone: +44 (0) 20 7201 7200