Q4 | 2020 Harding Loevner International Equity Portfolio

COMMENTARY — ASSET CLASS | INTERNATIONAL EQUITY

Investor | HLMNX Institutional | HLMIX Institutional Class Z | HLIZX

Average Annual Returns (%)[1] (as of 12/31/20)

	Q4	YTD	1 yr	3 yr	5 yr	10 yr	Since Incpt.
HLMNX (Investor)	16.05	20.00	20.00	8.67	11.78	7.46	7.35[2]
HLMIX (Institutional)	16.13	20.33	20.33	9.04	12.14	7.82	6.88[3]
HLIZX (Institutional Class Z)	16.13	20.37	20.37	9.11	—	—	10.43[4]
MSCI ACWI ex USA	17.01	10.65	10.65	4.88	8.93	4.92	—

HLMNX (Investor) Expense Ratio (Gross/Net)[5]: 1.13%/1.13%
HLMIX (Institutional) Expense Ratio (Gross/Net)[6]: 0.81%/0.81%
HLIZX (Institutional Class Z) Expense Ratio (Gross/Net)[7]: 0.75%/0.75%

Performance data quoted represents past performance; past performance does not guarantee future results. The investment return and principal value of an investment will fluctuate so that an investor's shares, when redeemed, may be worth more or less than their original cost. Current performance of the Portfolio may be lower or higher than the performance quoted. Performance data current to the most recent month end may be obtained by calling 877.435.8105 or visiting hardingloevnerfunds.com.

The **Harding Loevner International Equity Portfolio** (Investor Class) returned 16.05% during the fourth quarter of 2020 compared with the 17.01% return for its benchmark, the MSCI All Country World ex USA Index. For the 12-month period ending December 31, 2020, the Portfolio returned 20.00%, compared with the 10.65% return for the Index.

Market Review

International stock markets rose dramatically in the fourth quarter despite an escalation in the global pandemic. The starting gun for the run-up was Pfizer's announcement of better-than-expected results for its COVID-19 vaccine trials and was followed in rapid fire by positive reports from Moderna, AstraZeneca, and Sinopharm. Accelerated approvals gave investors further hope for some return to normal commerce in 2021, even as COVID-19 hospitalizations in the U.S. and Europe soared. The market rally was broad, with all sectors and regions finishing in positive territory, an encouraging cap on a turbulent year.

The year began with news of a sinister respiratory illness spreading throughout Hubei province in China. By the end of March, the virus was raging across the globe, prompting governments to enact sweeping business and travel restrictions to slow its spread. The economic fallout was immediate, and the concomitant stock market decline was swift and severe.

Economic policymakers, however, were quick to respond with unparalleled levels of support aimed at arresting the decline. Central banks in developed countries slashed borrowing costs and rolled out a dizzying array of measures designed to support asset prices and keep liquidity flowing to businesses. Fiscal branches, for their part, authorized almost US$12 trillion in spending to prevent a collapse in consumption, an amount equivalent to almost 12% of global GDP.

Stock markets rebounded in response almost as fast as they had fallen. Despite the ongoing headwinds, the economic recovery gathered steam over the course of year, and markets continued their upward march.

The U.S. dollar was a barometer of investor fear, rallying during the height of the pandemic, as investors sought the safety of the world's principal reserve currency, only to reverse course over the rest of the year. Only a handful of currencies from commodity-exporting countries, like Russia and Brazil, were lower against the dollar for the year.

Companies that benefited from the abrupt shift to remote work and surge in ecommerce, many of them within information technology (IT) and consumer discretionary, far outpaced more cyclical sectors such as energy, financials, and real estate, all of which finished in negative territory. The fourth quarter saw an inversion of this pattern, with financials and cyclicals benefiting disproportionately

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[1] Returns for periods less than one year are not annualized.
[2] Since the inception of the Portfolio's Investor Class shares on September 30, 2005.
[3] Since the inception of the Portfolio's Institutional Class shares on May 11, 1994.
[4] Since the inception of the Portfolio's Institutional Class Z shares on July 17, 2017.
[5] The expense ratio is as of the most recent Prospectus and is based on expenses for the most recent fiscal year end. Harding Loevner has contractually agreed to cap the expense ratio at 1.25% through February 28, 2021. The expense ratio (without cap) is applicable to investors.
[6] The expense ratio is as of the most recent Prospectus and is based on expenses for the most recent fiscal year end. Harding Loevner has contractually agreed to cap the expense ratio at 1.00% through February 28, 2021. The expense ratio (without cap) is applicable to investors.
[7] The expense ratio is as of the most recent Prospectus and is based on expenses for the most recent fiscal year end. Harding Loevner has contractually agreed to cap the expense ratio at 0.80% through February 28, 2021. The expense ratio (without cap) is applicable to investors.

from a vaccine-fueled boost in growth expectations. Non-cyclical sectors such as health care, consumer staples, and utilities lagged. IT, however, continued to outperform despite heightened scrutiny from regulators in Europe, China, and the U.S.

Similar final quarter flip-flops occurred along geographical lines. The eurozone, after lagging for three quarters, outperformed in the fourth, particularly countries hit hardest by the virus such as Spain and Italy. Emerging markets (EMs) also outperformed. Good returns from Brazil and India countered weakness in China, where investors digested the implications of **Alibaba**'s withdrawal of its planned IPO for its Ant Financial affiliate under pressure from banking regulators, and the parent company later was put on notice about the potentially anti-competitive practices of its core ecommerce business. Pacific ex Japan also fared well, helped by Australia, which rebounded with a recovery in commodity prices.

Style effects, having favored fast-growing and high-quality companies most of the year heedless of their high valuations, also reversed in the quarter. Stocks of the slowest-growing companies, including many cyclicals such as energy and banks, outperformed the fastest-growing by over 700 basis points. The effect of quality was even more pronounced, as shares of companies with more leverage and less consistent returns outperformed those of the highest-quality companies by over 1,600 basis points. Valuation as a factor offered no guide to performance in the fourth quarter one way or the other.

Performance and Attribution

The International Equity Portfolio (Institutional Class) rose 16.13% (net of fees and expenses) in the quarter, just behind the 17.01% rise (net of source taxes) of the MSCI All Country World ex USA Index. For the full year, the Portfolio rose 20.33% (net of fees and expenses), well ahead of the benchmark's 10.65% (net of source taxes) return.

In a quarter where our Portfolio returns were so close to the Index returns, it seems almost superfluous to parse the attribution too finely. For instance, taken in isolation, the entire difference is "explained" by the drag of our holding of 3.7% cash on average through one of the hottest quarters of all time.

Our stocks within materials lagged, since our holdings of industrial gas, fragrance & flavor, and enzyme producers are less geared to the business cycle than other parts of the sector. Strong stock selection in financials contributed positively. Every one of our EM-oriented banks bettered the banks industry group, which in turn led the financials sector. **BBVA**, the Spanish multinational with substantial Mexican and Turkish subsidiaries, outpaced the others following the announcement of the sale of its anemic U.S. business for a healthy price.

Several of our IT holdings also added to performance once again, with good returns from Dutch payments-software developer **Adyen**, South Korea-based **Samsung Electronics** (which was boosted by improving pricing for its DRAM memory chips), and **Infineon Technologies**, a German manufacturer of semiconductors used heavily in autos, especially electric vehicles. **SAP** shares plunged, however, after the German software maker revealed poor uptake of its cloud-based data services. With no holdings in the reviving auto industry to balance the swoon of suddenly embattled Alibaba, our consumer discretionary holdings hurt performance.

From a geographic perspective, lagging stocks in Europe, both inside and outside the eurozone, offset good stocks in EMs and Japan. Our three ultra-high-quality Swiss holdings, **Nestlé** and pharmaceutical makers **Roche** and **Lonza**, lagged the cyclical rally. Cyclical multinationals Royal Dutch Shell, Anglo-Australian mining giant **Rio Tinto**, and **Standard Chartered** bank, allowed us to outperform a volatile, Brexit-obsessed, COVID-19-beset U.K. market. In EMs a pair of strong IT stocks, Samsung and Taiwan-based semiconductor manufacturer **TSMC**, combined with resurgent banks to offset the drag from Chinese holdings Alibaba and China Mobile.

For the full year, relative performance was driven primarily by strong security selection in health care, industrials, IT, and financials, as well as by our overweight in IT. Indeed, IT accounted for just under half the outperformance for the year, led by Adyen, Infineon, Japan-based optical sensor specialist **Keyence**, TSMC, and Samsung. Health care holdings contributed significantly as several Portfolio companies played roles in the battle against COVID-19: Contract drug manufacturer Lonza is producing the early-approved vaccine from Moderna, while Roche and Japan-based **Sysmex** experienced surging demand for their test kits and diagnostic equipment. Consumer discretionary was the biggest drag on our full-year performance, due to our underweights in autos and retailing and the end-of-year struggles of Alibaba.

Outlook and Perspectives

When we wrote at the end of 2019 about a "world turned upside down," we had no idea just how upended the world was about to become; no inkling that a novel coronavirus was replicating exponentially and about to upend our lives. Rather, we were focused on the mundane (by comparison) implications of negative interest rates, potential inflation, and the implied discount rates for stocks. We fretted that the prices commanded by stocks of our preferred high-quality and fast-growing companies had reached unsustainable levels. The heightened volatility of long-duration assets—long-dated Treasurys and growth stocks both—made us fret further, since rising volatility often foreshadows a reversal.

As the pandemic erupted with full force in the first quarter, companies prized for their resilient secular growth and financial strength defied our fears and expensive growth stocks became even more highly priced. Some companies, with their business models anchored in the virtual rather than the brick-and-mortar world, were instantly transformed into COVID-19 "winners." Meanwhile, any company with more immediate exposure to either the business cycle (think banks) or specific dislocations arising from the pandemic, such as travel, was

shunned by investors. Last quarter, we noted that a startling number of stocks—indeed, higher than at any time in the last fifty years outside of the 1999 tech bubble—were priced to deliver negative returns even just assuming a naïve (and rather unrealistic) extrapolation of current consensus earnings growth estimates. One difference, of course, between 1999 and now is that now bonds are also priced to disappoint their owners, perversely making stocks seem less risky.

Nevertheless, with the end of the pandemic at last in sight, our prior concerns have returned to the fore. One way prospects could change for long-duration growth stocks, as well as for long-duration bonds, is for long-term interest rates to rise. Ultra-low discount rates, like ultra-low bond yields, imply that cash flows far into the future have more value today; if ultra-low were to give way to merely low, those faraway cash flows would not be so compelling. Moreover, what could stimulate animal spirits more than a return to before-COVID-19 commerce, travel, and social interactions with a year of deferred consumption coiled like a spring? On the fire of pent-up demand throw gasoline in the shape of competition for resources from infrastructure spending programs, and suddenly not even "low" may be the right level for inflation or interest rates, let alone for the discount rates applied to stocks.

Interest rates have mirrored falling inflation expectations over the past 40 years. Disinflation has been the result of technological innovation, globalization, and, pre-global financial crisis, disciplined monetary policy at the largest central banks. However, the future is clouded by many "ifs." If policymakers, not only in China, but also in Europe and the U.S., start reducing the freedom historically afforded to the big tech companies like Alibaba, Facebook, Google, and Amazon, it may well reduce the disinflationary effects these companies have midwifed into the world. If globalization and free trade continue to face populist protest and political backlash, the price of goods and services, no longer sourced from the most efficient producers, will tend higher instead of lower. If the current escalation of U.S.-China economic disagreements become further militarized, those inflationary effects could be large. If post-COVID-19 normalization demand and low inventories combine with debt financed infrastructure spending, interest rates may well lead, rather than follow, inflation higher. Some of these scenarios would be headwinds for profits; all, except a sustained, rapid economic expansion, are bad for stock valuations.

But there are also portents that endless growth of big tech profits itself could become less of a given. The commanding position of the dominant internet platforms and software companies flows in large part from benign competitive forces driven by powerful network effects and winner-take-all industry dynamics. Yet, in the final quarter of 2020, many of these companies found themselves beset by regulatory scrutiny in almost every jurisdiction. In Europe, the focus has shifted from data privacy toward taxing some of the revenues and profits generated in those countries. Among the recent actions, this strikes us as a modest blow to sustain (if, indeed, it stops there), and one that markets are probably good at discounting. In China, where Alibaba and **Tencent** dominate the previously largely freewheeling consumer economy, the situation is more treacherous, if only because of the opaque and unconstrained nature of China's regulatory authority. By encroaching onto the turf of the state-supported Chinese banking system via their payments platforms, Alibaba and Tencent were "poking the dragon" of politically powerful, entrenched vested interests, and potentially getting their business models singed in the process.

Antitrust actions in the U.S., meanwhile, are being driven by both state governments as well as the federal government, which adds its own unpredictable twist. The common thread in all these efforts is the emergence of a cohesive political opposition to the monopoly-like power of the world's largest internet-based companies. A key difference between this and past periods of regulatory backlash is that more of the monopolies' power today has been directed at squeezing their suppliers and eliminating competitors rather than gouging their customers, who continue to delight in the broader availability of better and cheaper goods, and who may well yet offer a countervailing pull on the regulators' push. Earlier antitrust actions in the U.S. against Microsoft in the 1990s, IBM in the 1980s, or ATT in the 1970s, were costly and disruptive, but ultimately left the targeted incumbents plenty powerful and profitable until innovation and new competitive challenges unrelated to the regulatory onslaught disrupted their dominance. We believe such an outcome is possible from the current actions, but the journey is likely to be a rocky one.

However, there is a world of difference between identifying risks and having them come to pass. 2021 may well prove to be an *annus horribilis* for growth investing, but there is no way of knowing in advance. Moreover, there is far more to the growth investing story than falling discount rates and the monopolistic practices of a handful of mega-cap companies. The last decade may have witnessed previously unimaginably low interest rates, but we've also experienced a resurgence in innovation accompanied by secular and, albeit still narrow, explosive earnings growth fueled by rapid advances in technology. And herein lies the iron law of growth investing—you may overpay but, with careful selection and a long enough horizon, compounding revenues and, ultimately, earnings will eventually bail you out of the high price you paid. Of course, underlying the careful selection part is a paradox that is frequently overlooked and liable to snare the unwary. The iron law only applies to individual growth companies; by definition, it cannot be true for all of them. This fallacy of composition is identical to the problem faced by a sports fan trying to get a better view of the field. Individually, they may stand up to get a better view, but it's obviously impossible for everyone to stand up and enjoy the view unimpeded. The best growth companies will ultimately justify even extreme valuations, but investors should have no illusion that all or even most growth companies can hope to join this unique cadre.

In our investment process we attempt to balance the emphasis among growth, sustained profitability, financial strength, and well-governed, able management. Our conviction lies in the belief that these attributes, elucidated through

fundamental research, maximize our odds of picking out the few companies with the long-term ability to sustain their growth. And despite the many looming risks to growth stocks we take encouragement from the pace of innovation that continues to hum along behind the cacophony.

Our Portfolio has weathered the "value" rally in the fourth quarter with some degree of aplomb. That's a result, we suspect, of our steady and incremental reduction or exit from some of our holdings over the past few years that reached into the ranks of the highest priced stocks. It's also the result of owning some of the most innovative companies outside the spotlight of regulatory scrutiny, whose growth has continued untrammeled so far. If the narrowing of valuation spreads and the relative performance rebound of cheaper stocks is mostly—or even halfway—completed, and inflation stays quiescent, we believe our portfolio is well-positioned. That's what happened after the global financial crisis, when we feared a sustained "low-quality" rally would hobble our chances of good relative performance for an extended period, but which didn't persist beyond a few months. We believed then that the damage from the debt crisis cut so deeply across the global economy that a strong rebound was never in the cards, especially with a robust austerity voice constraining most governments (a voice today seemingly lost in the wilderness). Compare that to the experience after the tech bubble of the late 1990s, when the burst affected the IT and Telecom sectors, but left the rest of the economy relatively unscathed and primed to respond dramatically to monetary stimulus. But looking even further back to other periods of equally distended valuations for growth companies, such as the Nifty Fifty of the early 1970s, we're reminded that markets have a history of being unprepared for tectonic shifts in politico-economic conditions, when the only warning signs are stretched valuations alongside the usual markers of speculative fever. Wariness is warranted.

Portfolio Highlights

2020 seemed to pack multiple years of a market cycle into a single year, with the market lurching from rewarding quality to rewarding growth, then speculative growth, and finally value. Throughout, we maintained our time-tested approach of bottom-up stock selection—we require both fundamental quality and prospective growth from our companies, and prices for their stocks, that are supportive of future returns. Over the course of the year, market volatility provided us with several opportunities to increase the overall quality and growth profile of our Portfolio without having to pay the expected premium these attributes typically cost. We worked, as always, to keep our heads and avoid being caught up in the market's emotions. Rather, our inclination is to lean against the prevailing market sentiment, while basing each decision on the fundamental prospects and the valuation for each individual stock. When markets were fearful and "riskier" positions such as Brazilian brewer **Ambev**, France-based **Schneider Electric**, Brazil-based **Itaú Unibanco**, Japan-based construction equipment manufacturer **Komatsu**, and Rio Tinto sold off, we added to them while trimming "safer" positions such as Roche and Nestlé. When markets chose to ignore valuation, we made sure to pay it more attention, trimming the most richly priced companies (Japanese pharmaceutical maker **Chugai Pharmaceutical**, **Canadian National Railway**, Ireland-based industrial gas supplier **Linde**) and adding to or purchasing positions that looked unusually cheap (Swiss-based eye care specialist **Alcon**, Mexican bottler and retailer **FEMSA**). We parted ways with several companies that failed to attain our predetermined mileposts for success: Japanese advertising agency Dentsu, South African energy and chemical company Sasol, Hong Kong-based HSBC, Chinese search engine Baidu, and, in the fourth quarter, China Mobile. The latter's revenue growth had been disappointing, so when the Trump administration, in a largely incoherent executive order, included China Mobile on a list of purportedly Chinese military-controlled companies that U.S. persons will very shortly be precluded from purchasing and, within a year, from selling as well, we chose to withdraw with alacrity, completing our divestment before year end. We held no other companies subject to this draconian and near-immediate sanction, not to be confused with the slowly moving sanction of eventual (December 2023) de-listing from U.S. exchanges potentially faced by a longer list of Chinese companies whose accounting transparency thus far has failed to meet the standards of U.S. securities regulators. With respect to those companies, we envision myriad possible ways in which they may avoid de-listing, including outright compliance or Chinese compromise with a new U.S. administration, or we may be able to gain or maintain investment exposure without recourse to U.S. exchanges. Despite the market volatility, at 11.3% our annual turnover was below our five-year average of 16.6%.

In a quarter that was characterized by dramatic outperformance of cheaply priced shares of lower-quality companies, our emphasis on higher-quality, more expensive shares should have dragged us under. Fully *half* our Portfolio is invested in the highest quintile of objectively measured quality, and very little in the two lowest quintiles. On that basis alone, we should have been expected to lag the benchmark by nearly 400 basis points. But, thanks to the much better performance of our holdings *within* each cohort of quality, we did not. We trace a direct line between this outperformance of our style and our dogged efforts to ignore the momentum of the most highly priced growth stocks and pursue growing businesses outside the fashionable segments instead. This was costly for our relative performance earlier, and concerning for those suffering from the fear of missing out (FOMO), but has ultimately put us in a gratifying spot: a year of good relative performance from a our Portfolio, resilient in the face of a sharp style shift.

To be sure, we had some turkeys. One of our self-improvement practices is to provide each analyst and portfolio manager an "after-action" report showing the consequences in performance terms of each of their investment decisions. Here's a sampling for the behaviorists among you: We initiated five complete sales from late February through late April, amid the thickest fog of COVID-19 uncertainty. The sales of Sasol and HSBC so far look to have been good decisions. Their shares have underperformed their respective industry sector and the

market overall since the sale decision, although costs for executing the Sasol sale more or less offset the underperformance avoided. The other three sales, made with stoutly asserted reasoning at the time, have left egg on our faces. Schlumberger, sold in late March after the OPEC cartel collapsed, has outperformed energy by a wide margin since. Baidu, sold in despair in late April over its declining growth prospects and competitor incursions, has since trounced the ACWI Communications Services Index. Amadeus, the airline-reservation-management software business headquartered in Spain, looked like a good sale in hindsight *until* vaccine approvals lifted both the outlook for a rebound in travel and Amadeus's performance relative to the rest of IT.

These underwhelming results from our actions remind us of two important principles: first, fear is rarely the right state of mind in which to make an investment decision. And, second, most of us could stand to be more modest about the predictive power of our insights and therefore more careful to weigh them against estimates of the costs of the transactions required to monetize them. The good news is that we made few such COVID-19-fear-inspired trades, and hence inflicted little self-harm.

Portfolio Management Team

Babatunde Ojo, 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. A member of the firm since 2012, he also continues to serve as a research analyst and co-lead PM of the Frontier Emerging Markets Strategy. International Equity co-lead PM assignments are not changing. The addition of portfolio managers to the strategy's team reflects our ongoing commitment to preparing our rising generation of investment leaders.

The views expressed represent the opinions of Harding Loevner LP as of December 31, 2020, are not intended as a forecast or guarantee of future results, and are subject to change without notice.

Top Ten Holdings (%)[8] (as of 12/31/20)

Holding	% of Net Assets
TSMC	4.68
Samsung Electronics	4.10
Infineon Technologies	4.03
AIA Group	3.20
L'Oreal	3.11
Atlas Copco	3.10
Adyen	3.05
Roche	2.76
Lonza	2.61
Tencent	2.48
TOTAL %	33.12

Disclosure

The Portfolio's investment objectives, risks, charges, and expenses must be read and considered carefully before investing. The statutory and summary prospectuses contain this and other important information about the investment company. They may be obtained by calling toll free 877.435.8105, or visiting hardingloevnerfunds.com. Read carefully before investing or sending money.

The Portfolio invests in foreign securities, which will involve greater volatility and political, economic, and currency risks, and differences in accounting methods. It also invests in emerging markets, which involve unique risks, such as exposure to economies less diverse and mature than the U.S. or other more established foreign markets. Economic and political instability may cause larger price changes in emerging markets securities than other foreign securities. Such risks may be magnified for securities in frontier emerging markets. Investing in participation notes involves the same risks associated with a direct investment in the underlying security, currency, or market.

[8] Mention of a specific security should not be considered a recommendation to buy or a solicitation to sell that security. Holdings are subject to change.

Investor | HLMNX Institutional | HLMIX Institutional Class Z | HLIZX

Past performance is no guarantee of future results.

The value of securities may fluctuate in response to various factors including, but not limited to, public health risks; these may be magnified if conditions and events adversely impact the global economy.

Diversification does not guarantee a profit or protect from loss in a declining market.

Earnings growth is not a measure of the Fund's future performance.

Market prices of investments held by the Fund may fall rapidly or unpredictably due to a variety of economic or political factors, market conditions, disasters or public health issues, or in response to events that affect particular industries or companies.

The MSCI All Country World Index (ACWI) ex USA is a free float-adjusted market capitalization weighted index that is designed to measure the equity market performance of developed and emerging markets. The MSCI ACWI ex USA consists of 22 developed and 24 emerging market country indices. Please go to msci.com for the most current list of countries represented by the MSCI indices.

Unlike the Fund, the Indices are unmanaged, are not available for investment, are net of foreign withholding taxes on dividends, and do not incur expenses.

Annualized standard deviation is a measure of the dispersion of a set of data from its mean. The more spread apart the data, the higher the deviation. Standard deviation is calculated as the square root of variance.

Basis points (bps) refers to the unit of measure for interest rates and other financial percentages. One basis point is equal to 1/100th of 1%, or 0.01%, or 0.0001, and is used to express percentage changes.

Cash flow is the net amount of total cash transferring into and out of a business.

Growth stocks typically are more volatile than value stocks; however, value stocks have a lower expected growth rate in earnings and sales.

All holdings and sector/region allocations are subject to review and adjustment in accordance with the Portfolio's investment strategy and may vary in the future, and should not be considered recommendations to buy or sell any security. The Portfolio is actively managed; therefore, holdings may not be current.

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