Confluence INVESTMENT MANAGEMENT

SECOND QUARTER 2024

Emerging Markets • International Equity Strategies

Confluence Emerging Markets invests primarily in large cap, growth-oriented companies in the emerging markets around the world. The strategy's management team employs both top-down and bottom-up fundamental analysis to identify attractive countries and economic sectors as well as high-quality companies worthy of a long-term investment allocation. The portfolio's primary objective is long-term capital appreciation.

Market Commentary: Mid-Year Update

Emerging market indexes moved higher during the quarter, rising 5% and outperforming the developed markets of the world, including the US. Information technology and AI-related optimism pushed tech-heavy markets such as Taiwan significantly higher. Also present was optimism that the monetary authorities around the globe would continue easing restrictive monetary policy as inflationary pressures eased. Central banks, including the ECB, Switzerland, Sweden, and Canada, all reduced rates during the second quarter. The most recent data out of the US indicates inflationary pressures are ebbing and chances of a September rate cut are improving. Meanwhile, in the emerging markets, some central banks initiated easing cycles in 2023, which are expected to expand to more countries in 2024 provided inflation remains contained.

Several elections in major emerging market economies may impact the macroeconomic environment within these nations. In India, the world's largest democracy, elections were conducted between April and May. Prime Minister Narendra Modi was re-elected to a third term to continue the massive infrastructure upgrades needed to become a meaningful part of the global manufacturing community. His market-friendly track record helped cement his win. However, for the first time since his Hindu nationalist Bharatiya Janata Party swept into power in 2014, it did not secure a majority on its own, winning 240 seats — far fewer than the record 303 it won in the 2019 election. This means Modi will need the assistance of other parties in his coalition to support his agenda. These continued reforms are necessary to sustain the country's economic growth ambitions. India now has a great opportunity to capitalize on the friend-shoring/near-shoring trend as manufacturing companies are reducing Chinese exposure, and the country's economic recovery remains on track with a 2024 GDP growth rate of 7.2%.

On June 3, Mexico elected Claudia Sheinbaum, a former mayor of Mexico City, who is a populist leftist. Sheinbaum and her predecessor, Andrés Manuel López Obrador (AMLO), are both members of the Morena Party, which is a major Mexican left-wing political party described as an anti-neo-liberal/populist party and has been the ruling party of Mexico since 2018. Her campaign was to continue the Fourth Transformation, which was a policy initiative of AMLO to crack down on corruption, eliminate "privileged abuses," curb violence, and promote social progress. Her landslide victory and the Morena Party's super majority in both houses of congress spooked the Mexican markets, and Mexican equities fell by 15% in the days following the election. Since then, the MSCI Mexico Index has recouped roughly half of its post-election decline amid an easing of policy fears. Mexico has been a notable outperformer under AMLO's tenure with secular forces likely driving Mexico's markets under his tenure (near-shoring) irrespective of his domestic policy agenda. It is unlikely that supply chains will reroute back to China amid secular trends toward deglobalization and near-shoring.

Outside of the emerging markets, an election of particular interest is the US election in November 2024, where the US relationship with China could be a major concern depending upon the outcome. A Trump victory could introduce meaningful change in the US relationship with China and impact trade between the two nations. If reelected, Trump has suggested that he would impose a 60% import tariff on Chinese products as well as trade restrictions on Chinese technology, along with a universal 10% import tariff. Trump's proposed tariffs could place pressure on Chinese textile and electronic imports to the US. A Biden victory would likely result in maintaining the status quo with China. Currently, under the Biden administration, restrictions on technology transfers, financial flows, and semiconductor production have all led to increased tensions with China.

The trajectory of the US dollar (USD) remains an important driver of emerging market equity returns. The MSCI Emerging Markets Index tends to move inversely with the USD, hence a strengthening USD is consistent with lower emerging market equity prices. During the second quarter, the USD appreciated by 1.3%, somewhat pressuring emerging market equity returns. Over the past year, the USD has risen 2.9% with limited impact on emerging market equity prices. The stronger USD provides additional headwinds to emerging market firms that issue debt denominated in USD since their debt-servicing costs rise as the greenback strengthens. The Confluence macroeconomic team still feels that the USD is under pressure longer term; however, its strength may be stickier than initially anticipated.

See GIPS Report on pages 5-6.

Market Commentary continued...

Returns in the Chinese market continue to strongly influence the MSCI Emerging Markets benchmark. More than 25% of the index is in Chinese equities, which have been under pressure for some time due to a real estate bubble and collapse, excessive debt levels, onerous government oversight, tepid recovery following the pandemic, a potentially unfriendly reunification with Taiwan, and ongoing tensions with the US and its allies. Following the January sell-off, Chinese equities have rallied sharply, with second quarter performance exceeding that of the MSCI Emerging Markets index. Modest stimulus measures undertaken by the Chinese government have been positive but unable to increase domestic consumption by a meaningful amount. Due to this muted domestic demand, China will continue to export the "new growth drivers," which include electric vehicles, batteries, and solar panels around the world. Excess capacity and relatively low labor costs allow China to produce exceptional products at low cost. China's production capacity in some of these industries far exceeds global demand projections. China will continue to "dump" these products in order to maintain production facilities and employ its population. This practice has drawn the attention of policymakers in the US and the EU, increasing trade friction with the West. Tariffs and trade restrictions may have a significant impact on supply chain dynamics in the emerging markets. Mainland China exports to the US fell from a high of 21% in mid-2018 to 14% as of year-end 2023. A decrease in imports from China could create opportunities in other emerging market regions such as EM ex-China, Latin America, and Mexico. Mexico now supplies 15% of all goods imported into the US.

In China, the shift to a consumption-driven economy from an export-driven economy continues to manifest itself, albeit ever so slowly. China's share of GDP attributed to consumption is 53%, which is lower than many leading economies, which typically have consumption levels between 70%-80% of GDP. The policies that investors want to see from China would focus on increasing domestic demand rather than adding additional excess supply. Chinese President Xi will continue to weigh concerns about national security and societal and political stability against economic growth objectives. Meeting the objectives of both mandates without a major stimulus package will be challenging.

There is no quick fix for Chinese housing woes, and the Chinese investor is feeling uneasy. Traditionally, real estate has been the primary store of wealth for Chinese households. As recently as 2010, nearly 70% of a family's net worth was in real estate. Due to the recent collapse in the housing market, real estate has shifted from one of the most revered asset classes to one that is less trusted to hold its value. Prices of previously occupied homes in Tier 1 cities have fallen between 25%-30%. Real estate still accounts for 50%-60% of household wealth. The housing downturn has resulted in lower consumer confidence and spending, especially on big-ticket items. Despite a national savings rate of 45%, people are reluctant to invest in the current environment. However, the broader economy is likely to improve though year-end as the real estate cycle bottoms.

Emerging market equities remain one of the most mispriced asset classes, in our opinion, with valuations reaching historically attractive levels. As of June 30, 2024, the MSCI Emerging Markets Index was trading at a forward P/E of 12.3x versus 13.9x for MSCI EAFE and 21.4x for the MSCI USA Index (representing around a 45% discount). Emerging markets continue to trade with stronger earnings growth, high and improving return on equity, high free cash flow yield, and a dividend yield near a 20% premium relative to historical figures and double that of the US (2.6% for the MSCI Emerging Markets Index versus 1.3% for the MSCI USA Index). Earnings growth in emerging markets is expected to rise 18% in 2024, far outpacing that of the US and the world's developed markets, which are expected to grow by about 10%. Furthermore, GDP growth is set to accelerate in emerging markets relative to developed as growth forecasts for 2024 are 4.0% for emerging economies compared to the 1.2% forecast for developed markets. This recovery can be attributed to global monetary easing, which has already occurred in many emerging markets as monetary authorities reduced interest rates to quickly address the recent bout of inflation. While growth in the developed markets is slower than in the emerging markets, the outlook for developed markets has improved modestly due to lower inflation/interest rates. Resilient global GDP should support emerging market economies.

Quarterly Trade Summary

We made a single change to the Confluence Emerging Markets portfolio during the second quarter. In late June, we sold our position in Brazil-based Localiza Rent a Car S.A. (LZRFY), which engages in car and fleet rental business. The company is also involved in granting franchises; the sale of decommissioned and used cars; providing sundry automotive, travel, and tourism services; and managing claims for insurance companies, as well as tracking and telemetry services. It operates car rental agencies in Brazil, Argentina, Colombia, Ecuador, and Paraguay. The company had experienced underperformance relative to the Brazilian market in 2024 and was undergoing some operational issues that didn't have a clear path toward being reversed. While the core rental car and fleet car operations continued to perform well, the used car disposal segment was underperforming in a substantial fashion (despite the adoption of more advantageous accounting practices since the beginning of the year) and the company was facing cash flow pressures associated with updating its fleet after underinvestment in recent years. Around the time of the sale, there was a very unusual dislocation occurring in value between the ADRs and the underlying local shares, so we chose to be opportunistic around that event.

Performance Review

The second quarter performance of the MSCI Emerging Markets (EM) Index was up 5.0% in USD terms, outperforming the returns of developed international markets (MSCI EAFE, -0.4%) and the US market (S&P 500, 4.3%).

Among the regions, EM Asia performed best, rising by 7.4% as equity markets in Taiwan, India, and China recorded strong performance. Taiwan (+15.1%) is benefiting from strong chip demand to support global AI initiatives. India's strong macroeconomic fundamentals and PM Narendra Modi's re-election in June will ensure the continuation of his reforms. EM Europe, Middle East, and Africa (EMEA, +1.6%) underperformed as strong performance in Hungary, the Czech Republic, and Poland were offset by poor performance in Saudi Arabia and Egypt. EM LatAm (-12.2%) was the worst-performing region, dragged down by the poor performance of Mexican and Brazilian equities during the quarter.

During the second quarter, the Confluence Emerging Markets strategy posted a loss of 2.2% (gross of fees) versus the 5.0% gain for the benchmark, as stated above. Over the past 12 months, Confluence Emerging Markets gained 6.3% (gross of fees), underperforming the benchmark at 12.5%. [*The strategy's net-of-fees returns for the same periods were -3.0% QTD and 3.2% one-year. See disclosures on last page for fee description; actual investment advisory fees may vary.*]

The two best-performing countries within our portfolio, on an absolute basis, were Taiwan and India, whereas Brazil and Indonesia/Mexico (tied) recorded the worst returns. From a sector standpoint, Information Technology and Communication Services were the strongest during the quarter, while Consumer Staples and Industrials were the weakest.

Security	Avg Weight (%)	Contribution (%)
Top 5		
MakeMyTrip Ltd.	5.35	3.39
Taiwan Semiconductor Manufacturing	5.27	2.76
Vista Energy S.A.B. de C.V.	4.75	1.95
KB Financial Group Inc.	2.43	0.81
ICICI Bank Ltd.	3.64	0.72
Bottom 5		
Vale S.A.	1.96	(0.65)
Wal-Mart de Mexico S.A.B. de C.V.	3.67	(0.78)
Localiza Rent a Car S.A.	*Sold*	(0.78)
Wuxi Biologics Cayman Inc.	*Sold*	(0.81)
Controladora Vuela Cia de Avia	2.08	(0.82)

(Contribution data shown from a sample account, based on individual stock performance and portfolio weighting)

The top contributors and detractors for the portfolio in 2024 are shown in the accompanying table.[1]

What We Are Watching

Macro and micro factors are changing in a positive direction for emerging market equities, indicating that they are poised for a period of outperformance in 2024 and beyond. In general, we expect countries that are more exposed to the US to outperform relative to those more exposed to the eurozone or China.

We continue to identify countries and regions that have better adapted to macroeconomic changes related to increasing levels of inflation, slowing global growth, and shortening supply chains. Most emerging markets have identified inflation in their economies and quickly raised rates to mitigate inflation expectations. As inflation is moderating and peaking in some areas, these economies are now reducing policy rates to stimulate stagnant growth. Provided that a significant global recession can be avoided, we believe emerging market equities are trading at extremely attractive valuations relative to historical levels and relative to the developed markets.

Inflationary pressures are moderating, and global growth is resuming, albeit at a slow pace. Nevertheless, risks to our positive outlook for emerging markets include:

- Elections around the world will impact both developed and emerging economies, and the ramifications of recent elections are already rippling through both developed and emerging economies:
  - We are focused on fiscal discipline and populist shifts, which could blur the outlook for these key economies.
  - The re-election of Modi in India is positive; however, his party lost seats in parliament which will mean increased friction in implementing his ongoing reforms.
  - The election in Mexico was a landslide victory for Claudia Sheinbaum, former mayor of Mexico City, who was elected to a six-year term. Mexican equities sold off hard following her victory. As a member of the same party as her predecessor, AMLO, she is expected to govern with similar priorities.
  - The US election will also be important to emerging market exports. If Donald Trump is re-elected, he has promised large tariffs on imported goods to protect American jobs.

What We Are Watching continued...

- Persistent inflation that would cause central banks in both emerging and developed markets to either raise or maintain high rates and reduce liquidity to combat inflationary pressures:
  - Emerging markets are particularly sensitive to inflationary pressures, although they tend to be in a better position to address these pressures as inflation has peaked in most cases.
- China's economy meaningfully slows due to inadequate stimulus and/or a real estate crisis:
  - China's existing stimulus programs may not be adequate to jump start the economy.
  - China's existing debt problem makes solving the real estate crisis more challenging.
  - Authorities outside of China may not fully appreciate the magnitude of the indebtedness at all levels of government.
- Prolonged US dollar strength:
  - A strong USD could weaken local currencies, which would exacerbate inflation in the emerging economies.
  - Debt service on USD-denominated emerging market sovereign debt is much more expensive to repay.
  - The Confluence macro team believes that a secular USD bear market started at the beginning of 2023; however, some recent appreciation in the USD suggests that its strength may be stickier than previously anticipated. History suggests these USD market cycles generally last 8-10 years, with a significant decline in the USD.
- The BRICS nations (Brazil, Russia, India, China, and South Africa) are contemplating using alternative currencies to conduct global trade, potentially undermining the importance of the USD as the reserve currency.
  - This would exert downward pressure on the USD, benefitting non-US assets, especially in emerging markets.
  - Many other countries are interested in joining the BRICS.
  - Non-USD trade arrangements have become significantly more prevalent recently.
- Geopolitical tensions escalate:
  - Tensions between the US and China;
  - Tensions between China and Taiwan;
  - Russia/Ukraine war;
  - Middle East tensions/war;
  - A long, drawn-out conflict between Russia and Ukraine or in the Middle East would keep commodity prices (especially energy) artificially high, which may impact inflation and consumer spending on a global basis.

Portfolio Characteristics[2] (as of 6/30/2024)

10 Largest Holdings	Weight
Taiwan Semiconductor Manufacturing	5.8%
Vista Energy S.A.B. de C.V.	5.5%
MakeMyTrip Ltd.	5.4%
MercadoLibre Inc.	4.5%
KB Financial Group Inc.	3.7%
ICICI Bank Ltd.	3.5%
Gold Fields Ltd.	3.4%
Fomento Economico Mexicano S.A.B.	3.2%
Dr Reddy's Laboratories Ltd.	3.1%
Wal-Mart de Mexico S.A.B. de C.V.	2.9%

Sector Allocation	Weight
Consumer Discretionary	19.8%
Consumer Staples	11.5%
Energy	7.4%
Financials	20.6%
Health Care	3.1%
Industrials	7.8%
Information Technology	8.1%
Materials	6.4%
Communication Services	4.2%
Cash	11.1%

10 Largest Countries	Weight
Mexico	20.5%
India	18.8%
China	11.9%
South Korea	7.9%
Brazil	7.4%
Taiwan	5.9%
Argentina	4.6%
Hong Kong	3.7%
South Africa	3.4%
Colombia	1.8%

Performance Composite Returns[3] (For Periods Ending June 30, 2024)

	Since Inception**	10-year*	5-year*	3-year*	1-year	YTD	QTD
Emerging Markets *Pure Gross-of-Fees[4]*	4.3%	3.2%	2.7%	(5.7%)	6.3%	1.2%	(2.2%)
Max Net-of-Fees[5]	1.2%	0.2%	(0.3%)	(8.5%)	3.2%	(0.3%)	(3.0%)
MSCI Emerging Markets (Net)	3.6%	2.8%	3.1%	(5.1%)	12.5%	7.5%	5.0%

Calendar Year	Pure Gross-of-Fees[4]	Max Net-of-Fees[5]	MSCI EM	Difference (Gross-MSCI EM)	# of Portfolios	Composite Assets (000s)	Total Firm Assets (000s)	Composite 3yr Std Dev	MSCI EM 3yr Std Dev	Composite Dispersion
2009**	10.3%	9.5%	8.5%	1.8%	5	$1,030	-	N/A	N/A	N/A
2010	13.1%	9.8%	18.9%	(5.7%)	5	$1,462	-	N/A	N/A	0.1%
2011	(15.7%)	(18.2%)	(18.4%)	2.7%	7	$2,430	-	N/A	N/A	0.0%
2012	11.4%	8.1%	18.2%	(6.8%)	4	$2,346	-	18.3%	21.5%	0.8%
2013	13.5%	10.2%	(2.6%)	16.1%	1	$220	-	16.0%	19.0%	N/A
2014	(3.6%)	(6.5%)	(2.2%)	(1.4%)	4	$1,636	-	13.9%	15.0%	N/A
2015	(2.7%)	(5.6%)	(14.9%)	12.2%	6	$3,218	-	14.7%	14.1%	0.5%
2016	0.7%	(2.3%)	11.2%	(10.5%)	17	$6,265	-	15.5%	16.1%	0.2%
2017	42.7%	38.5%	37.3%	5.4%	16	$9,288	-	15.0%	15.4%	0.8%
2018	(19.7%)	(22.1%)	(14.6%)	(5.1%)	15	$8,643	$5,486,737	14.8%	14.6%	0.6%
2019	17.3%	13.9%	18.4%	(1.1%)	13	$9,604	$7,044,708	16.0%	14.2%	0.6%
2020	22.9%	19.2%	18.3%	4.6%	14	$11,350	$6,889,798	21.3%	19.6%	1.9%
2021	(11.4%)	(14.1%)	(2.5%)	(8.9%)	9	$8,357	$7,761,687	20.7%	18.3%	0.4%
2022	(13.7%)	(16.2%)	(20.1%)	6.4%	7	$6,068	$6,931,635	21.3%	20.3%	0.6%
2023	15.7%	12.2%	9.8%	5.8%	6	$5,807	$7,200,019	18.5%	17.1%	1.9%

Average annualized returns ***Inception is 10/1/2009* *See performance disclosures on last page.*

Portfolio Benchmarks

MSCI Emerging Markets (Net) Index – Free float-adjusted market capitalization index designed to measure the equity market performance of emerging markets. Performance results are presented net of estimated foreign withholding taxes on dividends, interest, and capital gains. *(Source: Bloomberg)*

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Investment or investment services mentioned may not be suitable to an investor and the investor should seek advice from an investment professional, if applicable. It is important to review your investment objectives, risk tolerance, and liquidity needs before choosing an investment style or manager. All investments carry a certain degree of risk, including possible loss of principal, that investors should be prepared to bear. Equity securities are subject to market risk and may decline in value due to adverse company, industry, or general economic conditions. There can be no assurance that any investment objective will be achieved or that any investment will be profitable or avoid incurring losses.

Indexes: The MSCI Emerging Markets Index is shown as additional information. This index is unmanaged. An investor cannot invest directly in an index. It is shown for illustrative purposes only & does not represent the performance of any specific investment. Index performance figures are reported as net returns.

[1] **Contribution—**Table showing the top 5 contributors/detractors reflects the strategy's best and worst performers (net), based on each holding's contribution to the sample account for the period stated. Individual client portfolios in the strategy may differ, sometimes significantly, from these listings.

[2] **Portfolio Characteristics—**Listings of countries and holdings do not represent all of the countries/stocks currently or previously owned in the portfolio or which Confluence may be currently recommending. Sector/country weightings and holdings of individual client portfolios in the program may differ, sometimes significantly, from these listings.

[3] **Performance Composite Returns—Confluence Investment Management LLC claims compliance with the Global investment Performance Standards (GIPS®) and has prepared and presented this report in compliance with the GIPS standards. Confluence Investment Management LLC has been independently verified for the periods August 1, 2008, through December 31, 2023. The verification report is available upon request. A firm that claims compliance with the GIPS standards must establish policies and procedures for complying with all the applicable requirements of the GIPS standards.**

Verification provides assurance on whether the firm's policies and procedures related to composite maintenance, as well as the calculation, presentation, and distribution of performance, have been designed in compliance with the GIPS standards and have been implemented on a firm-wide basis. Verification does not provide assurance on the accuracy of any specific performance report.

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The Emerging Markets Strategy was incepted on October 1, 2009, and the current Emerging Markets Composite was created on May 1, 2018. Performance presented prior to May 1, 2018, occurred while the Portfolio Management Team was affiliated with a prior firm and was independently verified for the periods of 10/1/1999 through 12/31/2017. The Portfolio Management Team members were the primary individuals responsible for selecting securities to buy and sell. Composite performance is typically net of foreign withholding taxes on dividends, interest income and capital gains with some exceptions based on custodian treatment. Confluence Investment Management LLC is an independent registered investment adviser. Results are based on fully discretionary accounts under management, including those accounts no longer with the firm. Past performance is not indicative of future results. The U.S. Dollar is the currency used to express performance. Returns are presented gross and net of all fees and include the reinvestment of all income.

[4] Pure gross returns are shown as supplemental information to the disclosures required by the GIPS® standards.

[5] Net-of-fee performance was calculated using the highest applicable annual bundled fee of 3.00% applied quarterly. This fee includes brokerage commissions, portfolio management, consulting services and custodial services. The Confluence fee schedule for this composite: 1.00% on the first $500,000; 0.90% on the next $500,000; and 0.75% over $1,000,000.There are no incentive fees. Clients pay an all-inclusive fee based on a percentage of assets under management. The collection of fees produces a compounding effect on the total rate of return net of fees. Subsequent to February 1, 2013, bundled fee accounts make up 100% of the composite for all periods. Actual investment advisory fees incurred by clients may vary. Wrap fee schedules are provided by independent wrap sponsors and are available upon request from the respective wrap sponsor.

Performance prior to February 1, 2013, is based on the Emerging Markets–Direct Composite which was initially created on October 1, 2009. The Emerging Markets–Direct Composite includes accounts that pursue the Emerging Markets strategy, but do not have bundled fees. Gross returns from the Emerging Markets–Direct Composite include transaction costs and net-of-fee performance was calculated using the highest applicable annual bundled fee of 3.00% applied quarterly.

A complete list of composite descriptions is available upon request. Policies for valuing investments, calculating performance, and preparing GIPS Reports are available upon request. The annual composite dispersion is an equal-weighted standard deviation, using gross-of-fee returns, calculated for the accounts in the composite for the entire year. Prior to year-end 2018, the annual composite dispersion was an asset-weighted standard deviation calculated for accounts in the composite for the entire year. The three-year annualized standard deviation measures the variability of the composite gross returns over the preceding 36-month period. The Emerging Markets Composite contains fully discretionary Emerging Markets wrap accounts. The Emerging Markets portfolio invests in U.S.-listed shares of companies from emerging markets.

Prior to March 31, 2020, the S&P/BNY Emerging Market ADR Index was shown as a secondary benchmark. This index was removed to simplify the presentation, being less widely recognized and relevant than the primary benchmark.

**Results shown for the year 2009 represent partial period performance from October 1, 2009, through December 31, 2009. N/A-Composite Dispersion: Information is not statistically meaningful due to an insufficient number of portfolios in the composite for the entire year. N/A-3yr Std Dev: Composite does not have 3 years of monthly performance history.