



Investor / Institutional  
WAEMX / WIEMX

# Wasatch Emerging Markets Small Cap Fund

SEPTEMBER 30, 2020

## Despite Slight Underperformance for the Quarter, We Remain Very Pleased With the Year to Date

### OVERVIEW

Optimism for a rapid economic recovery from the Covid-19 pandemic drove solid gains in emerging-market equities during the third quarter. A flagging U.S. dollar and progress toward vaccines for the virus also encouraged investors. The Wasatch Emerging Markets Small Cap Fund—Investor Class rose 8.24% for the quarter. The Fund lagged its benchmark, the MSCI Emerging Markets Small Cap Index, which rose 11.85%. For the year to date, the Fund was still comfortably ahead of the benchmark: up 8.63% versus down -2.40%.

By the outset of the third quarter, the same factors responsible for the Fund’s outperformance earlier in the year had become a headwind. With speculation already creeping into global equity markets, the near-term backdrop for our company-focused approach and long investment horizon worsened in August following comments from U.S. Federal Reserve Chairman Jerome Powell.

### FUND MANAGERS



**Ajay Krishnan, CFA**  
Lead Portfolio Manager

1 / 26  
YEARS ON FUND / YEARS AT WASATCH



**Dan Chace, CFA**  
Portfolio Manager

1 / 18  
YEARS ON FUND / YEARS AT WASATCH



**Scott Thomas, CFA**  
Associate Portfolio Manager

5 / 8  
YEARS ON FUND / YEARS AT WASATCH



**Kevin Unger, CFA**  
Associate Portfolio Manager

2 / 5  
YEARS ON FUND / YEARS AT WASATCH

*Data show past performance and is not indicative of future performance. Current performance may be lower or higher than the data quoted. For the most recent month-end performance data, visit [wasatchglobal.com](http://wasatchglobal.com). Investment returns and principal value will fluctuate and shares, when redeemed, may be worth more or less than their original cost. The Advisor may absorb certain expenses, leading to higher total shareholder returns. Wasatch Funds will deduct a 2% redemption fee on Fund shares held 60 days or less. Performance data does not reflect this redemption fee or taxes. **Total Expense Ratio: Investor Class—Gross: 1.99%, Net: 1.97% / Institutional Class—Gross: 1.85%, Net: 1.82%. The Advisor has contractually agreed to limit certain expenses to 1.95% for the Investor Class and 1.80% for the Institutional Class through at least 1/31/2021.***

Speaking at the Fed's virtual Jackson Hole Economic Policy Symposium, Chairman Powell announced a shift toward letting U.S. inflation and employment run higher. The dollar tumbled to two-year lows against a basket of major rivals, sending international investors rushing somewhat indiscriminately into emerging-market assets. A weak dollar significantly boosts the attractiveness of developing nations and makes it easier for them to issue debt denominated in their own currencies.

Suffice it to say, markets driven by liquidity and risk appetite don't favor our investment style. In these environments, stocks of businesses that are highly cyclical, heavily indebted or challenged in some other way tend to benefit the most. Because the companies we own typically carry below-average levels of debt, are more creditworthy and generate more free cash from operations, their stocks tended to benefit less than those of companies that weren't as well-situated.

Korea was the Fund's primary source of underperformance. Korea's severe export slump eased during the third quarter amid a pickup in demand from China, the country's largest non-domestic market. Exports of computer-related devices rose sharply, as people fearing infection with the coronavirus shifted many of their activities online. Because we tend to avoid companies dependent upon exports and global trade, the Fund's Korean stocks didn't benefit as much from the improving export picture compared to those in the Index. Moreover, Fund performance suffered from our lack of exposure to Korean pharmaceutical and biotechnology companies—which were large weights in the benchmark and which were up strongly.

## DETAILS OF THE QUARTER

The strongest contributor to Fund performance for the quarter was **Voltronic Power Technology Corp.** Headquartered in Taiwan, the company designs and manufactures power products that include uninterruptible power supplies and

inverters. Voltronic's stock price rose sharply after the company reported a 32% jump in net profit on sales growth of 12% in its most recent quarter versus the same quarter a year ago.

Brazil was a source of strength against the benchmark, led by **Magazine Luiza S.A.**, the Fund's second-best overall contributor. Also known as Magalu, the company operates a multi-channel retail platform of mobile, website and physical stores. Magalu has benefited from surging e-commerce sales as shoppers seeking to avoid Covid-19 flocked to the internet. Total sales rose 49% in the company's most recent quarter, driven by a 182% increase in e-commerce. Additionally, Magalu announced a share-buyback program authorizing the acquisition of up to 10 million of the company's common shares.

Another strong stock in the Fund was **Mindtree Ltd.** The company, which is based in India, delivers business and technology solutions through global software development. Like other information-technology services companies, Mindtree has benefited as the Covid-19 pandemic accelerated the large-scale migration of corporate clients to digital platforms and the cloud.

Detractors from performance included Taiwanese IT holdings **Silergy Corp.** and **ASPEED Technology, Inc.** Each of these stocks generated negative total returns in the high single digits—which we consider normal in view of their outsized gains over the prior 12 months.

Silergy, the greatest detractor from Fund performance for the quarter, manufactures high-performance mixed-signal and analog integrated circuits. In its most recent sales report, the company announced that consolidated revenues for August had risen 23.13% in local currency and 31.08% in U.S. dollars compared to August 2019. We think Silergy's business model—which is based on analog design engineering—is difficult to replicate and is likely to provide significant headroom for growth over the coming decade.



ASPEED is a fabless designer of integrated circuits specializing in areas that include server management and audio-visual extensions. Because sales of the company's chips are closely tied to the production of servers, ASPEED benefited as firms around the globe added capacity to their data centers to accommodate citizens waiting out the coronavirus under home confinement. While the company's stock has lost some of its near-term appeal as lockdowns lifted, local economies reopened and people returned to workplaces outside the home, it remains a worthwhile holding for the Fund in our view.

**AK Medical Holdings Ltd.** was also a significant detractor. A Chinese company, AK Medical manufactures medical devices that include orthopedic implants, spinal interbody cages and artificial vertebral bodies. Covid-19 has impacted the revenues of medical-device companies as patients fearful of contracting the disease postponed non-urgent appointments and surgeries. A shift in distribution toward Group Purchasing Organizations in China also weighed on the stock, as investors worried that increased pressure on pricing may hurt profitability. *(Current and future holdings are subject to risk.)*

## OUTLOOK

According to official data released at the end of the quarter, manufacturing activity in China grew faster than expected in September. Driven by a pickup in export demand as global economies reopened, the report suggested China's economic recovery remained on relatively firm footing. Consumption also increased as the Chinese government continued to ease restrictions on travel and in-person entertainment.

China's success in battling the Covid-19 pandemic has cemented its substantial regional

influence and growing economic status. For evidence of this, one need look no further than the nation's currency. In the three months ended September 30, the onshore renminbi appreciated nearly 4% against the U.S. dollar—its largest quarterly increase in over 12 years. Similarly, the offshore renminbi rose more than 4%, beating out traditional currency havens such as the Swiss franc and the Japanese yen.

These developments aren't difficult to understand. As of this writing, China's vast industrial sector has approached its pre-pandemic might—fueled by government-funded infrastructure expansion, rising exports and pent-up demand. Meanwhile, in the U.S., the president and Congress have been arguing over a much-needed Covid-19 stimulus package.

Of course, investing in China carries its own unique set of risks. Among these are the country's deepening disputes with the U.S. over issues such as trade, technology and the situation in Hong Kong. When researching companies to own in the Fund, we seek firms whose fortunes are comparatively independent of geopolitics. We look for growing businesses that we believe are well-positioned to benefit from secular trends in areas that include health care and technology.

We believe China will continue to develop and open up its economy. At the same time, we think ongoing improvements in China's financial markets will deepen liquidity and attract increasing capital flows from around the world.

Thank you for the opportunity to manage your assets.

Sincerely,

Ajay Krishnan, Dan Chace, Scott Thomas and Kevin Unger



## AVERAGE ANNUAL TOTAL RETURNS

FOR PERIODS ENDED SEPTEMBER 30, 2020

	Quarter*	1 Year	3 Years	5 Years	10 Years
Emerging Markets Small Cap Fund—Investor	8.24%	21.12%	6.51%	8.62%	4.60%
Emerging Market Small Cap Fund—Institutional	8.19%	21.41%	6.59%	8.74%	4.66%
MSCI Emerging Markets Small Cap Index**	11.85%	6.89%	-1.09%	4.60%	1.03%
MSCI Emerging Markets Index**	9.56%	10.54%	2.42%	8.97%	2.50%

### A fund's performance for very short time periods may not be indicative of future performance.

*\*Returns less than one year are not annualized.*

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Total Annual Fund Operating Expenses include operating expenses, including the management fee, before any expense reimbursements by the Advisor. **The Advisor has contractually agreed to limit certain expenses to 1.95% for the Investor Class and 1.80% for the Institutional Class through at least 1/31/2021.** See the prospectus for additional information regarding Fund expenses.

*Wasatch Funds will deduct a 2.00% redemption fee on Fund shares held 60 days or less. Performance data does not reflect the deduction of fees or taxes, which if reflected, would reduce the performance quoted. For more complete information including charges, risks and expenses, read the prospectus carefully.*

Performance for the Institutional Class prior to 2/1/2016 is based on the performance of the Investor Class. Performance of the Fund's Institutional Class prior to 2/1/2016 uses the actual expenses of the Fund's Investor Class without any adjustments. For any such period of time, the performance of the Fund's Institutional Class would have been substantially similar to, yet higher than, the performance of the Fund's Investor Class, because the shares of both classes are invested in the same portfolio of securities, but the classes bear different expenses.

**Investing in foreign securities, especially in emerging markets, entails special risks, such as currency fluctuations and political uncertainties, which are described in more detail in the prospectus. Investing in small cap funds will be more volatile and loss of principal could be greater than investing in large cap or more diversified funds.**

*An investor should consider investment objectives, risks, charges and expenses carefully before investing. To obtain a prospectus, containing this and other information, visit [wasatchglobal.com](http://wasatchglobal.com) or call 800.551.1700. Please read the prospectus carefully before investing.*

**Diversification does not eliminate the risk of experiencing investment losses.**



*\*\*The MSCI Emerging Markets and Emerging Markets Small Cap Indexes are free float-adjusted market capitalization indexes designed to measure the equity market performance of emerging markets. You cannot invest in these or any indexes.*

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*The Wasatch Emerging Markets Small Cap Fund's investment objective is long-term growth of capital.*

*The "cloud" is the internet. Cloud-computing is a model for delivering information-technology services in which resources are retrieved from the internet through web-based tools and applications, rather than from a direct connection to a server.*

*Sales growth is the increase in sales over a specified period of time, not necessarily one year.*

## EMERGING MARKETS SMALL CAP FUND – TOP 10 HOLDINGS

AS OF JUNE 30, 2020

Security Name	Percent of Net Assets
Silergy Corp. (Taiwan)	6.8%
Voltronic Power Technology Corp. (Taiwan)	4.7%
Magazine Luiza S.A. (Brazil)	4.6%
Globant S.A. (Argentina)	4.1%
Raia Drogasil S.A. (Brazil)	3.3%
ICICI Lombard General Insurance Co. Ltd. (India)	3.0%
Vitasoy International Holdings Ltd. (Hong Kong)	3.0%
Bajaj Finance Ltd. (India)	2.9%
ASPEED Technology, Inc. (Taiwan)	2.8%
LEENO Industrial, Inc. (South Korea)	2.7%
Total	37.8%
<i>Portfolio holdings are subject to change at any time. References to specific securities should not be construed as recommendations by the Fund or its Advisor. Current and future holdings are subject to risk.</i>	