

Wasatch Emerging Markets Small Cap Fund

DECEMBER 31, 2019

Recent Headwinds for Emerging Markets Have Shown Signs of Reversing

OVERVIEW

Accommodative monetary policy and an apparent breakthrough in the trade impasse between the U.S. and China helped push emerging-market equity prices higher during the fourth quarter. The benchmark MSCI Emerging Markets Small Cap Index rose 9.52%. Outgaining its benchmark, the Wasatch Emerging Markets Small Cap Fund—Investor Class returned 11.50%. For all of 2019, the Fund increased 27.42%, surpassing the 11.50% return of the Index.

Central banks around the world maintained a general bias toward easing, with the U.S. Federal Reserve cutting its key lending rate for the third time in 2019. The widely expected move dampened enthusiasm for the U.S. dollar, which slipped -3.0% against a basket of major rivals during the fourth quarter. Emerging markets benefited as the falling greenback and lower U.S. interest rates made riskier assets in developing nations more attractive to international investors. A weaker dollar also makes it easier for emerging markets to issue debt denominated in their own currencies.

FUND MANAGERS



Ajay Krishnan, CFA
Lead Portfolio Manager

<1 / 25
YEAR ON FUND / YEARS AT WASATCH



Roger Edgley, CFA
Portfolio Manager

12 / 17
YEARS ON FUND / YEARS AT WASATCH



Dan Chace, CFA
Portfolio Manager

<1 / 17
YEAR ON FUND / YEARS AT WASATCH



Andrey Kutuzov, CFA
Associate Portfolio Manager

5 / 11
YEARS ON FUND / YEARS AT WASATCH



Scott Thomas, CFA
Associate Portfolio Manager

4 / 7
YEARS ON FUND / YEARS AT WASATCH



Kevin Unger, CFA
Associate Portfolio Manager

1 / 4
YEAR 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. 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: 1.97%, Net: 1.95% / Institutional Class—Gross: 1.83%, Net: 1.81%. 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 1/31/2020.**

Taiwan was the Fund's largest source of outperformance relative to the benchmark. The island's economy has benefited from an influx of manufacturing as global supply chains shifted away from China to avoid tariffs on goods bound for the U.S. Driven by strength in industrials and information technology (IT), the Fund's Taiwanese stocks substantially outgained the Taiwanese positions in the Index.

India and Thailand also were sources of outperformance. With the economies of both countries decelerating, the financials and other growing companies owned in the Fund became more appealing to investors. India's gross domestic product (GDP) rose 4.5% in the September quarter from a year ago—down from 5% in the previous quarter and the slowest pace of expansion in more than six years. In Thailand, the central bank cut its policy interest rate to a record low 1.25% in November to restrain a surging currency that has made the country's exports less competitive overseas.

Korea was the Fund's primary source of weakness against the benchmark. Considered a bellwether for global trade and technology, Korea's equity market moved higher as trade tensions eased during the fourth quarter. Although the Fund's Korean stocks generated a solid gain as a group, declines in two individual holdings dragged down performance.

DETAILS OF THE QUARTER

The strongest contributor to Fund performance for the quarter was **Silergy Corp.** Based in Taiwan, Silergy manufactures high-performance mixed-signal and analog integrated circuits used in a wide array of electronic devices. Silergy's stock price had languished during the latter half of 2018 and early 2019 as sluggish demand caused a buildup of inventory in semiconductor supply channels. An uptick in sales during May sparked a turnaround in the stock that accelerated during the fourth

quarter. In December, Silergy announced that consolidated revenues for November had risen 38.0% in local currency and 39.7% in U.S. dollars versus November 2018.

A pair of Brazilian holdings—**Magazine Luiza S.A.** and **Raia Drogasil S.A.**—represented the second-largest and third-largest contributors, respectively. Magazine Luiza operates a multi-channel retail platform of mobile, website and physical stores in Brazil. Shares of the company logged strong gains amid positive sentiment toward Brazilian equities and optimism that Magazine Luiza will be able to capture a significant slice of Brazil's e-commerce pie.

Raia Drogasil operates the leading chain of drugstores in Brazil. The company had been struggling as competitors used lower-priced, lower-quality generic medicines to lure consumers. Now that the company has begun offering discounted generics of its own, competitive intensity appears to have eased. The stock rose sharply in October after Raia Drogasil reported quarterly same-store sales growth of 11.9% overall and 7.7% for mature stores versus the same quarter a year ago. The company's retail market share increased 1.7 percentage points nationally and 2.5 percentage points in the key São Paulo market compared to the year-ago period.

The greatest detractor from Fund performance for the quarter was **Vitasoy International Holdings Ltd.** A multinational based in Hong Kong, the company offers soy milk, tofu, rice milk, tea, juices and related food-and-beverage products in China and other countries. Investors reacted negatively to Vitasoy's plans to invest more heavily in its soy-milk business to stave off competitive pressures and pave the way for future growth. We think the company's strategy makes sense, however—especially in view of the large untapped potential for packaged soy milk and Vitasoy's strong brand presence in the markets it serves.



Other detractors included two Korean stocks, **BGF Retail Co. Ltd.** and **Medytox, Inc.** BGF, an operator of convenience stores, has seen competitive pressures impact both the top and bottom lines of its business. In addition, Korea's populist government has raised the country's minimum wage, swelling BGF's labor costs and squeezing margins further. With convenience-store openings in Korea continuing to outstrip demand growth in the industry, we are reevaluating the Fund's position in the stock.

Medytox manufactures neurotoxins for cosmetic applications. Concerns about the pending approval of the company's products for sale in China continued to weigh on the share price of Medytox. Meanwhile, the company's lawsuit against a pair of competitors—which seeks to block U.S. imports of a rival product—have created an additional layer of uncertainty around the stock. On the plus side, a recent inspection of the company's manufacturing facilities by Korea's Ministry of Food and Drug Safety failed to uncover any serious problems, thus removing a potential obstacle to Chinese approval. *(Current and future holdings are subject to risk.)*

OUTLOOK

As was the case during the fourth quarter, a general principle in international investing is that a falling U.S. dollar is helpful to emerging markets. Weakness in the greenback can become self-reinforcing, as outsized equity gains and stronger economic growth in emerging markets pull investment away from the U.S., further impacting the dollar. Conversely, a strong U.S. dollar can pose headwinds to emerging-market investments. Countries with structurally weak currencies are especially vulnerable to dollar strength, which may compel them to adopt overly restrictive monetary and fiscal policies in order to attract and retain foreign capital.

From the dollar's recent low against a basket of major rivals on January 26, 2018, the greenback

rose 11.3% through the end of September 2019. When viewed in that light, the difficulties emerging-market investments faced in 2019 and 2018 seem unsurprising. The MSCI Emerging Markets Small Cap Index lost -18.59% in 2018—and was up just 1.81% through the end of 2019's third quarter, lagging more-sizable gains in global equity markets as a whole. The dollar's abrupt reversal during the fourth quarter—in which the greenback declined -3.0% against the same basket of competitive currencies—helped propel the MSCI Emerging Markets Small Cap Index to a 9.52% gain during the final three months of 2019.

Although the dollar's cyclical phases are not actionable for timing purposes, they nevertheless provide us with a rough framework for evaluating the current situation and longer-term probabilities. The dollar's historical tendency to trade within a fairly well-defined band suggests that it cannot continue going up forever. We now seem to be approaching the upper end of that band. If so, the strong-dollar headwind of the past two years may be poised to transform itself into a weak-dollar tailwind for emerging markets.

In the meantime, we think the high-quality companies and innovative disruptors around which we have built the Fund's portfolio are well-positioned to outperform. We look for companies with their own, unique demand drivers that are not tied to macro trends in the global economy. Throughout the dollar's cycles, we believe our fundamental, bottom-up investment approach has the potential to generate attractive returns over time.

Thank you for the opportunity to manage your assets.

Sincerely,

Ajay Krishnan, Roger Edgley, Dan Chace,
Andrey Kutuzov, Scott Thomas and Kevin Unger



AVERAGE ANNUAL TOTAL RETURNS

FOR PERIODS ENDED DECEMBER 31, 2019

	Quarter*	1 Year	3 Years	5 Years	10 Years
Emerging Markets Small Cap Fund—Investor	11.50%	27.42%	12.59%	4.49%	6.51%
Emerging Market Small Cap Fund—Institutional	11.83%	27.74%	12.66%	4.62%	6.58%
MSCI Emerging Markets Small Cap Index**	9.52%	11.50%	6.70%	2.97%	2.95%
MSCI Emerging Markets Index**	11.84%	18.42%	11.57%	5.61%	3.68%

*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 1/31/2020.** 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 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.

Gross domestic product (GDP) is a basic measure of a country's economic performance and is the market value of all final goods and services made within the borders of a country in a year.

EMERGING MARKETS SMALL CAP FUND – TOP 10 HOLDINGS

AS OF SEPTEMBER 30, 2019

Security Name	Percent of Net Assets
Silergy Corp. (Taiwan)	4.4%
Bajaj Finance Ltd. (India)	4.3%
ICICI Lombard General Insurance Co. Ltd. (India)	4.1%
Raia Drogasil S.A. (Brazil)	3.6%
Voltronic Power Technology Corp. (Taiwan)	3.6%
Magazine Luiza S.A. (Brazil)	3.2%
Vitasoy International Holdings Ltd. (China)	3.1%
Dr. Lal PathLabs Ltd. (India)	2.8%
Info Edge India Ltd. (India)	2.8%
Globant S.A. (Argentina)	2.6%
Total	34.6%

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.