International Growth Commentary

Q3 2021

SGA
Sustainable Growth Advisers

Performance

SGA's International Growth portfolio returned 0.2% (gross) and 0.0% (net) in Q3 versus -3.0% for the MSCI All Country World ex USA Index (ACWI ex USA) and -3.6% for the MSCI ACWI Growth ex USA.

Highlights

- Regulatory uncertainty in China and a slowdown in economic activity weighed on markets in Q3.
- The portfolio outperformed its MSCI All Country World ex USA Index benchmark with stock selection the primary contributor to relative returns.
- New positions were initiated in Brazilian brokerage platform XP, restaurant operator Yum China, and contract research organization leader ICON. The portfolio's positions in New Oriental Education, Alibaba, Tencent, and IHS Markit were liquidated.
- The portfolio remains well-positioned to deliver attractive growth over our longer-term 3-5 year investment horizon with strong quality characteristics and a cash-flow based valuation discipline.

Uncertainties Weigh on Markets

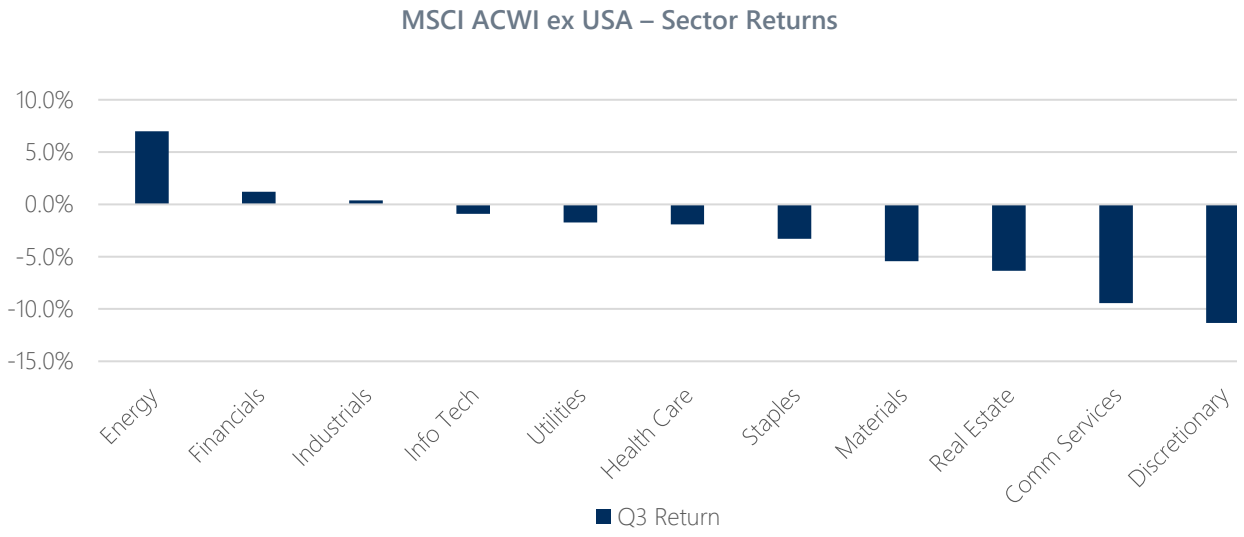
International markets finished the third quarter lower posting their first quarterly loss since Q1 of 2020. Latin American and Asian markets performed worst during the period driven by significant declines in China, Korea, Brazil, and Hong Kong, offsetting stronger performance in Japan, India, and Indonesia. European markets performed best, with returns strongest in EM Europe driven by the Russian market.

In China, the government's emphasis on 'Common Prosperity' and a more aggressive and ideological regulatory approach led to significant share price dislocations for companies across several industries, including technology, e-commerce, fintech, gaming, property development, and private education. COVID-19 outbreaks in critical manufacturing hubs in China and Vietnam slowed economic activity and contributed further to the weakness. In contrast, sharp declines in COVID-19 cases in India and Indonesia lifted sentiment and drove a strong rebound in their markets. Japanese equities also benefited from an improving COVID-19 backdrop with cases declining following the end of the summer Olympics. The resignation of Japanese Prime Minister Yoshihide Suga lifted sentiment further on expectations for a replacement more inclined to increase stimulus spending. Russia was among the top performers in Europe, benefiting from soaring energy prices, while many western markets lagged on continued COVID-related isssues and concerns tied to rising inflation.

The more persistent inflationary pressures resulting from production and transportation bottlenecks as well as labor shortages have prompted central banks across Latin America and Eastern Europe to tighten monetary policies faster than expected, posing a risk to the economic recovery and markets. Given our concerns about inflation, we recently conducted a comprehensive "All Hands on Deck" review of the expected impact a sustained period of higher inflation would have on our Qualified Company List companies. While a key element of our investment process has always been to focus on companies with strong pricing power, we focused on stress-testing our assumptions to better understand potential vulnerabilities in the face of a longer-than-expected period of elevated inflation. Consistent with our approach, the results indicated that our companies are generally well-positioned to pass on higher input costs and rising wages, enabling them to protect margins and deliver attractive growth in revenues, earnings, and cash flows over the long-term. We strongly believe that focusing on steady growth companies, which possess attractive pricing power and generate more predictable growth regardless of the macro-economic background will be critical to success moving forward.

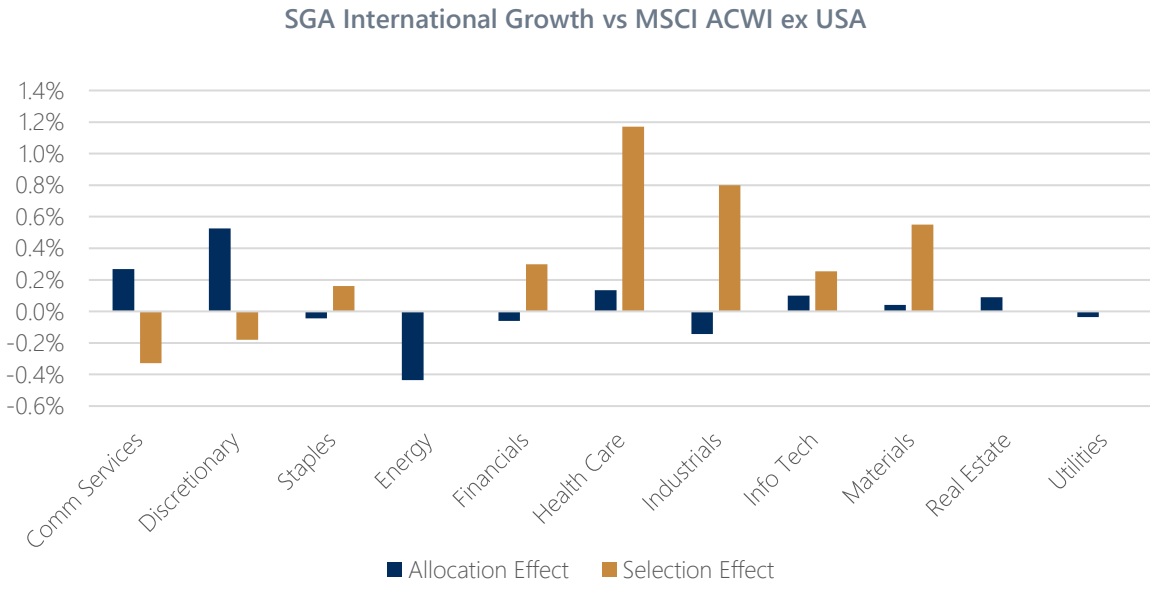
Market and Portfolio Attribution

Developed Markets outperformed Emerging Markets with Japan and Europe outperforming and Asia ex-Japan and Latin America lagging. Companies in the Energy, Financials and Industrials sectors performed best during the period on the back of rising energy prices and interest rates. The worst performing sectors were the Consumer Discretionary, Communication Services, and Real Estate sectors with their weakness largely tied to Chinese companies and the more uncertain Chinese regulatory environment.



Source: MSCI

Strong stock selection drove the portfolio's outperformance during the period while residual sector allocation contributed modestly. Selection in the Health Care sector had the largest positive impact on relative performance, followed by selection in Industrials, and Materials, while selection in Comunication Services and Consumer Discretionary detracted. Stock selection contributed positively in both Developed and Emerging Markets due to the portfolio's European postions, while selection in India and China detracted. Underweights in the poorly performing Consumer Discretionary and Communication Services sectors and an overweight to the Health Care sector contributed positively, while a lack of exposure to the top-performing Energy sector detracted. The portfolio's overweight in India and underweight in China contributed positively to relative returns, while an underweight to Japan and overweight to Brazil detracted most.



Source: FactSet, MSCI

Largest Contributors

Professional services firm **Aon** was the largest contributor to performance. Aon's shares jumped on the announcement that the company was abandoning its $30B merger with Willis Towers Watson. The high likelihood of a lengthy antitrust battle with U.S. and European regulators alongside demands for material divestments diminished the attractiveness of the merger. Aon will have to pay a $1B breakup fee, but we view the announcement as a positive since the required divestitures seemed onerous. We continue to see the company as well-positioned to deliver predictable and steady growth in earnings and cash flows over the long-term. Aon has invested heavily in its data and analytics capabilities positioning it for success in growing areas such as cyber security risks, intellectual property risks, and climate change risks. Aon's Q2 results were confirmatory to our conviction in the company's stand-alone growth potential as the company delivered organic revenue growth of 11% as it recovered from the negative impact from COVID-19 during 2Q20 when it posted -1% revenue growth, while its cash EPS grew 17% and margin came in better-than-expected. We trimmed the position on strength but maintained an above-average weight given our high conviction and still attractive valuation.

Media and job search company **Recruit** was the second largest contributor to portfolio performance in Q3. Continuing to benefit from the tight US labor market and the increased willingness of people to change jobs, the company's Human Resources Tech business delivered exceptional results, driving Recruit's strong FYQ1 report. Revenue and profit growth rose well above expectations fueling the stock's strength. During the quarter, we were also pleased to see the HR Tech business' jump in margins, which will be temporary but provides important evidence supporting our long-term margin forecasts. While we are fully aware that the latest results benefited from the temporary short-term tightness in the labor markets, we see the company's HR Technology segment being well-positioned to benefit from evolving labor market dynamics in the various global markets it serves.

Pharmaceutical company **Novo Nordisk** was the third largest contributor to performance, reporting strong Q2 sales growth and improved guidance for the remainder of 2021. The company benefited from significant growth in its recently launched once weekly GLP-1 medication Ozempic for the treatment of Type 2 Diabetes. With growth accelerating along with multiple new product launches including its oral GLP-1 diabetes drug Rybelsus and Wegovy for weight loss, combined with good execution and increased penetration of the international GLP-1 market, we continue to see a long runway of attractive growth ahead.

The fourth and fifth largest contributors to performance were **Alcon** and **Sartorius**.

Largest Detractors.

Medical device maker Shandong Weigao was the largest detractor from portfolio returns. Shandong's shares were negatively impacted by continued uncertainty around the impact of changes to the Chinese government's central procurement process. While the Chinese government's procurement program has been implemented for certain products already and indications have been positive for Shandong, uncertainty around the upcoming announcement of policies for the fast-growing orthopedics market unnerved investors. Shandong's results for the first six months of the year were in line with expectations as sales grew 22%, 19% organically, and EPS rose 25%. Results were strongest in the domestic Chinese market with growth of 25% while sales in EMEA declined given continued COVID-19 headwinds. Sales increased 17% in its Medical Devices segment, 30% in Orthopedics, 11% in Interventional Products, and 25% in Pharma Packaging. Shandong's longer-term growth prospects remain attractive given its strong positioning in the Chinese market due to its scale and R&D advantages. The potential for adverse policy changes is a risk we are carefully monitoring but based on the developments we have seen thus far, we expect the company to be a net beneficiary of changes to the government's procurement practices, as the central procurement policies will enable industry leaders to take significant share, albeit at lower price.

New Oriental Education (EDU) was the second largest detractor from performance as Chinese education stocks cratered following announcements of significant government regulatory interventions in the sector, restricting companies from making profits, raising capital, or going public. Given the adverse regulatory developments and their impact on our investment thesis, we liquidated the position following the end of Q2 and re-allocated the capital to higher confidence opportunities. Even with our minimal remaining position size in Q3, the stock's decline during the quarter due to these changes led the position to be the second largest detractor during the period.

Banking and financial services software solutions provider **Temenos** was the third largest detractor from performance as a broader rout in technology stocks later in the quarter weighed on its shares. Temenos delivered solid Q2 results with 8% revenue growth, 16% operating profit growth, 11% EPS growth, and strong momentum across regions. Total software licensing sales grew 16% driven by underlying strength in software-as-a-service (SaaS) and subscription sales which grew 24%. Temenos is seeing accelerating growth in the U.S., where its penetration is lower, driven by strong demand for its SaaS solutions as the company has expanded its salesforce and entered an important strategic partnership with DXC Technology. We continue to view the longer-term growth opportunity favorably for Temenos and raised our position to an above-average weight during the quarter.

The fourth and fifth largest detractors from performance for the quarter were **Tencent** and **Heineken**.

Portfolio Activity

Turnover during the quarter was above-average. We initiated new positions in ICON, XP, and YUM China and liquidated positions in New Oriental Education, Alibaba, Tencent, and IHS Markit. Several other positions were trimmed and added to on strength and weakness during the quarter.

New Positions

ICON is a leading global contract research organization (CRO) that engages in outsourced development services to the pharma, biotech, and medical device industries. ICON specializes in the strategic development, management and analysis of programs that support clinical development, helping biopharma companies run clinical trials and manage the complex FDA approval process. ICON is the second largest company in the fragmented global CRO industry following its recent acquisition of PRA Health Sciences.

As the second largest CRO, ICON benefits from its scale and comprehensive service offerings, which allows it to charge a premium relative to smaller peers. Price is often seen as a secondary consideration for customers behind quality, speed, expertise, and reliability of the CRO. As drug trials are very expensive and time consuming, ICON's ability to save time is highly valuable for its clients, increasing the runway for patent protected profits. High switching costs and long-term client contracts, along with the strategic nature of many client relationships provides a high degree of repeatability, stickiness, and longer-term visibility into ICON's revenues. We see ICON as well-positioned in an attractive growth industry and expect the company to be able to deliver high-single-digit organic revenue growth and mid-teens earnings growth over the long-term.

Among the risks we are monitoring for ICON is the company's ability to successfully integrate PRA and drive synergies without seeing an acceleration in employee departures, which can disrupt client's clinical trials and ultimately hurt their ability to win new contracts. We are also closely monitoring ICON's ability to diversify its client base towards smaller biotech firms which have driven a significant share of R&D spending growth globally. Additionally, disruptions in global pharma and biotech R&D growth could negatively impact the company's future growth potential.

We initiated a new position in **XP**, the leading independent broker platform in Brazil, during the quarter. XP brings better technology, an improved customer experience and a better product offering (in terms of fees and selection) to the Brazilian financial services market which has been dominated by five banks over the past two decades. Given still low penetration in its markets and the low financial savviness of the retail market in Brazil, we see continued growth opportunity for XP as financial knowledge continues to grow and customers invest in more types of products. They have supplemented their offerings with educational resources, seminars, conferences, and other client-centric opportunities which have allowed the company to effectively outcompete the traditional banks. The repeatability of the company's revenues benefits from the fact that more than half of its assets under custody and revenues are primarily through a diverse group of independent retail financial advisors. Approximately 70% of its revenues are derived from retail clients while the remaining 30% is tied to institutional and issuer services as well as educational services. XP is currently the low-cost provider in the industry with about 30% of revenues derived from commissions. While commissions will gradually come down, the company's pricing power benefits from its already low-cost provider status. We also expect the company to continue to add new sources of revenues including lending products such as credit cards, insurance, and other opportunities.

The key risks associated with the company are that commission rates decline faster than anticipated, regulatory issues evolve, and currency risk. We will also be closely monitoring any new entrants into the market to evaluate their technology, product set and customer service capabilities.

Yum China is a leading restaurant operator in China, with over 11,000 restaurants in 1,100+ cities and towns across the country. The company was spun-off from its parent Yum! Brands in 2016 and has exclusive rights to operate and sub-license the KFC, Pizza Hut, and Taco Bell brands in China under a 50-year master license agreement. The company is also building its presence in the fast-growing Chinese coffee market through its K-Coffee brand, which sold 140 million cups in 2020, as well as through its COFFii&JOY coffee stores and its JV with the Italian Lavazza coffee brand.

Yum China has built tremendous brand equity over time through menu innovation, affordable price points, industry-leading digital and delivery capabilities, and a strong internal culture highlighted by it being named a top employer in China three years straight. Its scale also affords the company advantages in terms of supply chain, advertising, celebrity promotions and quality of real estate. Given the company's loyal and growing customer base and diversity across mealtimes and geographies, it has built a highly recurring business with a high degree of predictability. The company's KFC and Pizza Hut loyalty programs, which have over 330 million members combined, further enhances customer engagement. The longer-term growth opportunity remains significant given considerable room to grow its number of units, particularly in lower tier cities with expanding middle classes and rising consumption and given the broad under penetration of quick service and casual restaurant chains in China.

The risks for Yum China include food safety incidents, which could negatively impact its brand equity and customer traffic. Food safety risk, however, is mitigated by the company's sophisticated supply chain and rigorous food safety protocols, which allows it to track 90% of its supply chain in real time. The company-owned business model is also a risk as it leaves the company vulnerable to operating deleverage during periods of weak sales growth or through cost pressures such as wage and commodity inflation. Regulatory risks are not material currently, however, we continue to monitor potential adverse policy developments which could potentially impact the company.

Sold Positions

We sold the position in **New Oriental Education** at the beginning of the quarter. Following abrupt changes in the regulatory landscape we no longer have confidence that the company will be allowed to operate in a profitable manner with the pricing power and recurring revenues it enjoyed previously. The company was also removed from our Qualified Company List given these adverse developments.

The position in **Alibaba** was sold given concerns over the company's VIE structure and the higher level of risk we see in companies with such legal structures. Deteriorating relations with the west and the government's willingness to inflict losses on shareholders in the name of "Common Prosperity" exacerbate those risks. Additionally, we also are cognizant of the rising competition in the company's businesses and the potential for more pressure on the company's profits.

With rising uncertainty over the Chinese government's regulatory actions impact on gaming and reduced near-term visibility we decided to liquidate the position in **Tencent** and reallocate the capital to higher conviction opportunities.

Information technology services company IHS Markit was sold from the portfolio given a less attractively valued growth opportunity and as the company is set to merge with S&P Global making it a U.S.-domiciled company.

Summary

International markets declined in Q3 as a broadening Chinese regulatory crackdown, continuing COVID-19 disruptions, and inflationary pressures leading to less accommodative central banks, weighed on investor sentiments. The portfolio outperformed its benchmark during the period amid higher levels of volatility and uncertainty. With the investment landscape changing in China, we continue to carefully assess our investments in Chinese companies and evaluate whether they provide the predictably and sustainability we seek. Our focus remains on positioning our clients alongside key secular growth drivers while minimizing the portfolio's exposure to less predictable regulatory actions and fluctuations in macroeconomic conditions. We expect volatility to remain elevated as COVID-19 headwinds continue, central banks face more persistent inflation, and

economic activity slows with the removal of extraordinary levels of stimulus. At the same time, we see inflationary pressures as a real risk and have factored this into our evaluation of companies on our Qualified Company List. Because strong pricing power and predictable revenue generation are key characteristics we require, we expect that our companies should be well suited to operate successfully in a world with building inflationary pressures. Likewise, we are confident that our ongoing focus on valuation and the critical role it plays in successful growth investing should help position our portfolio well should long-term discount rates rise. Finally, the tendency of our approach to benefit during times of rising volatility and protect capital in periods of market weakness should position us well if expectations for growth in 2022 and beyond prove optimistic. While relative results will vary from quarter-to-quarter, we remain confident that our time-tested approach will generate above average revenue and earnings growth which should lead to strong long-term absolute and relative returns over our 3-5 year investment horizon.

The opinions expressed herein reflect the opinions of Sustainable Growth Advisers, LP and are subject to change without notice. ***Past performance is no guarantee for future results.*** *This information is supplemental and complements a GIPS Report that can be found with composite performance. The securities referenced in the article are not a solicitation or recommendation to buy, sell or hold securities. This commentary is provided only for qualified and sophisticated institutional investors.*

Results are presented gross and net of management fees and include the reinvestment of all income. The Net Returns are calculated based upon the highest published fees. The net performance has been reduced by the amount of the highest published fee that may be charged to SGA clients, 0.85%, employing the International Growth equity strategy during the period under consideration. Actual fees charged to clients may vary depending on, among other things, the applicable fees schedule and portfolio size. SGA's fees are available upon request and also may be found in Part 2A of its Form ADV. Policies for valuing investments, calculating performance, and preparing GIPS Reports are available upon request. Upon request, free of charge, SGA can provide a list of all portfolio holdings held in SGA's International portfolio for the past twelve months. Past performance is not indicative of future results. SGA's earnings growth forecast data is based upon portfolio companies' Non-GAAP operating earnings.

Sustainability Report

Q3 2021

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The United Nations Sustainable Development Goals

"A blueprint to achieve a better and more sustainable future for all people and the world by 2030"

As Principals of Responsible Investing signatories, companies are required to report progress towards their actions supporting the 17 Sustainable Development Goals (SDGs) which broadly aim to free the world from poverty, hunger and disease. We believe the SDGs have the potential to be a useful framework to measure corporate progress on key sustainability issues. However, absent a globally recognized benchmark or framework for SDG reporting, we find little value in current corporate SDG reporting. The key issues to improve concern materiality, measurement, accountability, and verification.

Without adequately defined goal posts, the SDGs are ripe targets for greenwashing. We have observed numerous companies report they are contributing to all 17 SDGs, without any mention of the 169 individual targets published by the UN (each SDG typically has 8-12 targets). Companies overwhelmingly report on their positive impacts on these goals, with little discussion of their negative impacts.

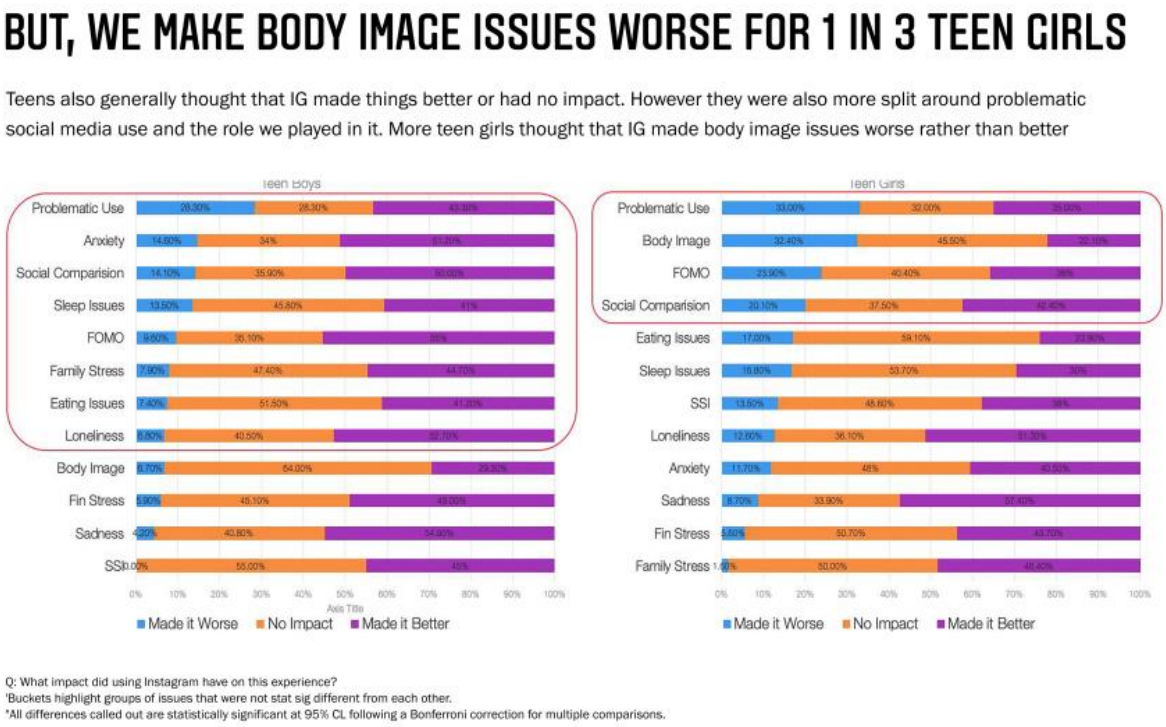
For the SDGs to provide a valuable reporting framework to investors, companies should prioritize a smaller number of goals that are linked to the company's core business growth, and potential impediments to that growth. Companies should publish the methodology used to prioritize and measure goals, and also disclose specific targets and indicators to enable investors to track their progress. Just as with GHG emissions targets, goals related to SDG should be clearly defined over a short to intermediate term rather than aspirational overall a time frame long enough to outlast current management. Finally, transparency to allow independent verification of the SDGs will be a prerequisite to increasing the quality of reporting and allow for comparisons across companies and industries.

We will continue to monitor for progress as SDG reporting matures and evolves, with the hopes that corporate SDG reporting will become a valuable tool for investors to measure individual and collective corporate progress on key sustainability issues.

Recent Facebook Reports

The Wall Street Journal ('WSJ') recently published a series of articles on Facebook, dubbed "the Facebook Files". Based on a review of internal Facebook documents, the WSJ reported that Facebook is knowingly aware of the platform's negative effects on its users and has repeatedly failed to rectify such flaws. Focus was drawn to the "toxic" effects of Instagram on teenage girls, while ignoring the studies' broader findings that teens report having both positive and negative experiences with social media. In response to the allegations, Facebook released the full research decks in question and countered that the WSJ had intentionally misrepresented its research. As Facebook comments:

"It is simply not accurate that this research demonstrates Instagram is "toxic" for teen girls. The research demonstrated that many teens we heard from feel that using Instagram helps them when they are struggling with the kinds of hard moments and issues teenagers have always faced. In fact, in 11 of 12 areas on the slide referenced by the Journal (see below) — including serious areas like loneliness, anxiety, sadness and eating issues — more teenage girls who said they struggled with that issue also said that Instagram made those difficult times better rather than worse. Body image was the only area where teen girls who reported struggling with the issue said Instagram made it worse as compared to the other 11 areas. But here also, the majority of teenage girls who experienced body image issues still reported Instagram either made it better or had no impact."



Source: Facebook

Regulation, platform misuse and user well-being are material risks identified in our Facebook investment thesis. We are skeptical of any internal company research, and we will be engaging with management on this topic during our next meeting scheduled in the fourth quarter. In the interim, we expect political debates over the increased scrutiny of Big Tech to continue - as the Democrats and Republicans attempt to balance the competing needs of content moderation and free speech – with regulatory overhang on share multiples to persist. Ultimately, we believe social media platforms form an essential service in this digital society. While there are clear risks associated with its use, we believe the benefits to society far outweigh the risks.

Engagement with Workday

Workday is a leading provider in the Human Resource (HR) software-as-a-service market. We engaged with management over the quarter for an update on the key ESG risks and opportunities that impact their business.

While technology companies are often at face value assumed to have a low impact on the environment, Workday, as with many software companies, manages an energy intensive business model delivering cloud applications and powering data centers, supported by operations across a network of offices. Fortunately, software companies have generally acknowledged this energy intensity and have taken a leadership position in the race to lower carbon emissions. In 2016, Workday made a commitment to achieve net-zero carbon emissions and 100% renewable electricity use across its operations by 2021 and achieved this goal a year early. The company is now in the process of establishing interim Science Based Targets across its entire value chain, a campaign we actively support, and expects these to be published within the next 12 months.

We questioned Workday's current Diversity & Inclusion ("D&I") metrics, noting women and minorities are still underrepresented in management ranks. The company is slowly making progress in the right direction, and we acknowledge the current global shortage of female and minority talent in the technology sector. This is an area we will continue to monitor for change. As it relates to D&I, the company has a promising business opportunity within its VIBE product range which measures employee diversity and belonging inside enterprises and eventually will allow for inter-company comparisons as well. As more enterprises look to measure, monitor and manage their D&I metrics, Workday's VIBE product is well positioned within the group's broader HR suite to serve the needs of this growing market.

Turning to governance, we questioned the reasoning behind the recent appointment of the co-CEO to Chairman of the Board, and the decision to not hold annual elections for Board members - noting MSCI's low governance scoring of Workday's Board. Separately, management expressed their disappointment that MSCI chose to classify three directors as non-independent merely because their employers are customers of Workday. Based on our primary analysis of the facts, we believe the three directors in question should be considered independent. As many investors rely primarily on the conclusions of third-party service providers for their ESG analysis, we encouraged management to proactively engage with MSCI to resolve this matter. Management commented the decision to appoint the co-CEO to Chair is in line with the company's broader anti-takeover defenses which management put in place to protect the interests of its customers given past experiences leading other companies. We see merit in this line of argument however we still find it to be a potential conflict with minority shareholders. The company has made efforts to enhance corporate governance in the form of moving to a majority vote for election of directors and intentions to sunset its evergreen share issuance option plan. We emphasized to management that newer, early-stage technology companies are increasingly employing a sunset provision for dual class shares and expressed our preference that Workday do the same.

Finally, Workday has not yet incorporated ESG measures into their senior management remuneration policies although the Board is debating it at present. We expressed our support for this cause, noting the increasing importance of establishing clear incentives and accountability for ESG policies and goals within the organization.

Proxy Voting Summary Q3 2021

	Number of Resolutions	For	%	Against	%	Abstain	%
U.S. Large Cap Growth	35	33	94%	2	6%	0	0%
Global Growth	20	20	100%	0	0%	0	0%
International Growth	59	59	100%	0	0%	0	0%
Emerging Markets Growth	12	10	83%	2	17%	0	0%
Global Mid-Cap Growth	20	20	100%	0	0%	0	0%

Source: SGA, Broadridge

Carbon Risks

	Carbon Emissions	Total Carbon Emissions	Carbon Intensity	Weighted Average Carbon Intensity
SGA Global Growth	15.9	15,876	90.7	70.5
MSCI ACWI	257.5	257,481	350.9	310
SGA Relative Exposure	-94%	-94%	-74%	-77%
SGA U.S. Large Cap Growth	12.8	12,837	92.2	76.2
Russell 1000 Growth	37.5	37,471	111.5	78.1
SGA Relative Exposure	-66%	-66%	-17%	-2%
SGA Emerging Markets Growth	17.1	17,121	49.7	50.5
MSCI EM	361.5	361,498	453	425.9
SGA Relative Exposure	-95%	-95%	-89%	-88%
SGA International Growth	21.6	21,611	84.1	78.1
MSCI ACWI ex-USA	297.2	297,180	365.2	333.9
SGA Relative Exposure	-93%	-93%	-77%	-77%
SGA Global Mid Cap	11.9	11,874	61.5	51.2
MSCI ACWI Mid Cap	264.5	264,526	337.0	295.5
SGA Relative Exposure	-96%	-96%	-82%	-83%
	t CO2e / $M Invested	t CO2e	t CO2e / $M Sales	t CO2e / $M Sales

Source: SGA, MSCI. Carbon data includes Scope 1 and 2 emissions.

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