Q4 2020 | Putnam Emerging Markets Equity Fund Q&A

A strong year for fund performance

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The fund underperformed the benchmark for the quarter, but outperformed for the 1-, 3-, 5-, 10-year, and life-of-fund periods ended December 31, 2020.

Our two-part investment process includes creating a custom watch list of 500 to 600 stocks and conducting at least 500 calls with management teams each year.

We focus on the fundamentals and growth potential of companies in sectors that are underrepresented in the index.

How did the fund perform in the fourth quarter?

For the fourth quarter, the fund underperformed its benchmark, the MSCI Emerging Markets Index [ND]. However, we are pleased to report that the fund outperformed its benchmark by over 18% for the 2020 calendar year. It also outperformed the benchmark for the 3-, 5-, 10-year, and life-of-fund periods ended December 31, 2020.

What contributed to the strong 2020 performance for the fund?

We believe it is due to our consistent investment approach, which often has enabled us to deliver outperformance despite declines in the broader market — and when either value stocks or growth stocks took the lead.

We have a two-part investment process. First, we create a custom watch list of 500 to 600 stocks out of a universe of 3,500. We believe the businesses on our custom list have superior return potential, more durable moats, better sustainability characteristics, above-average profitability, and strong balance sheets. On a fundamental basis, these are the types of businesses that we want to own.

The hardest work comes with the next step in our process. Every year, we strive to hold at least 500 calls with management teams. We build dozens of proprietary models, looking for a differentiated view of long-term earnings relative to consensus expectations. Our research has indicated that if a company beats expectations, its stock subsequently outperforms by 35%. From these fundamental steps, we build a portfolio of our best ideas, which typically consists of 50 to 60 stocks.

In your view, what is the advantage of an actively managed portfolio in the emerging markets universe?

We believe there are three key reasons our active approach can outperform. The first relates to our underweight exposure to SOEs, or state-owned enterprises. These businesses are predominantly owned by emerging-market governments. We found that stocks of these companies — which account for over 20% of our benchmark index — tend to underperform those of private companies.

The second advantage of our active approach relates to index construction. While the S&P 500 Index is a fair representation of the underlying U.S. economy, this is not the case for emerging markets equity indexes. For example, in China, the index is dominated by large financial institutions while the consumer and health-care sectors are underrepresented. Health care accounts for just 2% of the index in China versus 12% in the United States. We dig deep in our research and focus on the fundamentals and growth potential of companies within these underrepresented sectors.

Finally, emerging markets are incredibly inefficient. U.S. company Amazon is covered by over 50 investment banks. In contrast, one of our key holdings, Taiwan-based Universal Vision Biotech, has no analyst coverage. We are able to conduct deep-dive research on this and other under-covered companies while many of our competitors are unable to do so.

Putnam Emerging Markets Equity Fund (PEMYX)

Annualized total return performance as of 12/31/20

Class Y shares Inception 9/29/08	**Net asset value**	**MSCI Emerging Markets Index [ND]**
Last quarter	16.97%	19.70%
1 year	37.08	18.31
3 years	11.59	6.17
5 years	16.05	12.81
10 years	5.18	3.63
Life of fund	7.23	6.75

Total expense ratio: 1.44%

What you pay: 1.08%

"What you pay" reflects Putnam Management's decision to contractually limit expenses through 2/28/22.

Returns for periods of less than one year are not annualized.

Current performance may be lower or higher than the quoted past performance, which cannot guarantee future results. Share price, principal value, and return will vary, and you may have a gain or a loss when you sell your shares. Performance assumes reinvestment of distributions and does not account for taxes. For the most recent month-end performance, please visit putnam.com. For a portion of the periods, this fund may have had expense limitations, without which returns would have been lower. Class Y shares are generally only available for corporate and institutional clients and have no initial sales charge.

The MSCI Emerging Markets Index (ND) is a free float-adjusted market capitalization index that is designed to measure equity market performance in the global emerging markets. You cannot invest directly in an index.

The views and opinions expressed are those of the portfolio managers as of December 31, 2020, are subject to change with market conditions, and are not meant as investment advice.

Consider these risks before investing: International investing involves currency, economic, and political risks. Emerging-market securities carry illiquidity and volatility risks. Investments in small and/or midsize companies increase the risk of greater price fluctuations. From time to time, the fund may invest a significant portion of its assets in companies in one or more related industries or sectors, which would make the fund more vulnerable to adverse developments affecting those industries or sectors. Growth stocks may be more susceptible to earnings disappointments, and value stocks may fail to rebound. Risks associated with derivatives include increased investment exposure (which may be considered leverage) and, in the case of over-the-counter instruments, the potential inability to terminate or sell derivatives positions and the potential failure of the other party to the instrument to meet its obligations. The value of investments in the fund's portfolio may fall or fail to rise over extended periods of time for a variety of reasons, including general economic, political, or financial market conditions; investor sentiment and market perceptions; government actions; geopolitical events or changes; and factors related to a specific issuer, geography, industry, or sector. These and other factors may lead to increased volatility and reduced liquidity in the fund's portfolio holdings. Our investment techniques, analyses, and judgments may not produce the outcome we intend. The investments we select for the fund may not perform as well as other securities that we do not select for the fund. We, or the fund's other service providers, may experience disruptions or operating errors that could have a negative effect on the fund. You can lose money by investing in the fund.

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Request a prospectus or summary prospectus from your financial representative or by calling 1-800-225-1581. The prospectus includes investment objectives, risks, fees, expenses, and other information that you should read and consider carefully before investing.

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