

Emerging Markets Fund

Year Ending December 31, 2018

OVERVIEW:

The GMO Emerging Markets Fund seeks total return in excess of that of its benchmark, the MSCI Emerging Markets Index. The Fund is a top-down value portfolio which uses fundamental investment principles and a quantitative approach to provide broad emerging market equity exposure. The Fund tends to exhibit a value bias relative to the benchmark.

Performance (%)

Net of Fees, Class III, Fair Value, USD	-12.82
Gross of Fees, Class III, Local Close, USD	-12.21
MSCI Emerging Markets ¹	-14.58
Value Added	+2.37

COUNTRY ALLOCATION: +2.0%

SECURITY SELECTION: +0.4%

Major Performance Drivers

After a good start to 2018, the market took a turn in February that ended up setting the tone for the rest of the year. The market concerns initially centered on the Fed hiking interest rates. Tensions rose further as the trade war went from bark to bite. China, by far the most important economy in emerging markets, was particularly impacted as it was forced to abandon its fledgling drive to bring down leverage in the economy and pivot to an easing mode in order to address the downward pressures arising from the trade war. Arguably, this policy about-face and associated uncertainty has had a larger impact on market sentiment than the direct effects of the tariffs themselves.

The MSCI Emerging Markets Value Index beat the MSCI Emerging Markets Growth Index this year by about 8%, but they were neck and neck until the last few months of the year. Unlike 2016 or 2017 where the gap between styles was consistent and large throughout the period, 2018 was not a clear value or growth year.

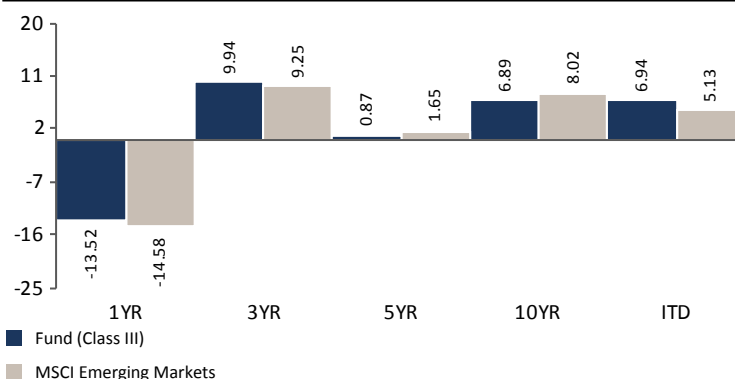
Country returns over the year varied, ranging from a 29.8% leap in Qatar to a -41.4% drop in Turkey. Sector returns driven by domestic demand were more clustered, varying from a -3.8% drop in Utilities to a fall of -32.5% in Consumer Discretionary.

The portfolio fell in 2018 but outperformed the MSCI EM Index in comparison. The largest driver of this outperformance, by far, was our overweight to Russia Energy, followed closely by our overweight to Russia Materials. In the Technology space, our bets favoring the unsung Taiwan Technology names versus the glamorous Technology names of China and Korea paid off, as the Taiwan Technology country-sector outperformed its equivalents in Korea and China. We gave up some of our gains due to our overweight to Turkey.

The Brazilian market began the year well as a ruling went against center-left candidate and former President Lula, weakening his odds of winning the presidency later in the year. A further boost came from a drop in inflation. The market spent the year hoping for the election of its favorite, Bolsonaro, as president, and ended 2018 celebrating his victory. There are hopes that he will address the pension burden and enact pro-market reforms. Our underweight in Brazilian Financials negatively impacted performance.

Performance data quoted represents past performance and is not indicative of future results. The investment return and principal value of an investment will fluctuate so that an investors shares, when redeemed, may be worth more or less than their original cost. Current performance data may be lower or higher than the performance data provided herein. To obtain performance information to the most recent month-end, visit www.gmo.com. Gross Expense Ratio of 1.02% is equal to the Funds Total Annual Operating Expenses set forth in the Funds most recent prospectus dated June 30, 2018.

Annualized Return (%) as of December 31, 2018



Inception date: 12/09/1993

Chart returns include purchase premiums and redemption fees impact if applicable.

China had a good start to the year as the economy continued its steady climb. However, in March, the stock market was hit by the ratcheting of tensions on trade. The US announced that it would impose tariffs on up to \$60 billion in annual imports from China. A slowing domestic economy added further pressure. Sentiment kept deteriorating through the year as investors priced in a higher probability of a deep and protracted trade war with the US. The end of the year saw renewed pressure from multiple reports indicating a slowing economy. Industrial output and retail sales grew at the worst pace in years and there were still no signs of a major government stimulus. Our underweight in Chinese Consumer Discretionary and Communication Services helped performance.

The Indian stock market was hurt at the start of the year by concerns that the upcoming budget would contain a combination of populist and investor unfriendly measures. Later sentiment was pressured by the disclosure of a huge \$2 billion fraud at one of the country's largest banks. Sentiment improved with a drop in the price of crude oil, a big driver of the country's current account deficit. India also gained from its relatively greater insulation from global trade. September saw the market turn sour after a major non-bank lender defaulted on its debt. This raised concerns on the quality of credit rating agencies as the outstanding debt had been rated very highly just a few weeks back. The end of the year saw a reversal with sentiment improving with a drop in the price of crude oil. Our underweight Indian Financials and Information Technology detracted from performance.

The Russian stock market gained from rising crude oil prices. Sentiment was lifted by a perception that the US would not add to the sanctions already imposed on Russia. At the end of March, the mood changed dramatically as Russia was hit by the coordinated international expulsions of over 100 Russian diplomats as punishment for the country's alleged role in poisoning a former agent and his daughter in the UK. Relief arrived later in the year on the back of jumps in the prices of crude oil and natural gas, key exports for Russia. It also seemed that the threat of sanctions had ebbed, at least temporarily. The final quarter saw the market give back some of its earlier gains as commodity prices weakened. Our overweight in Russian Energy and Materials contributed to performance.

Sentiment in Taiwan was boosted early in 2018 by bullish forecasts from the Technology sector. This was driven by expectations of strong sales of premium devices, such as Apple's iPhone, in the second half of the year. Taiwan's strong and stable macroeconomics also gained favor with investors. Our overweight in Taiwan Financials and IT positively contributed to performance.

Turkish stocks began the year on a weak note as investors judged the fiscal and monetary policies as ill-suited for an overheating economy. Later in the year, the stock market took a hit after President Erdogan appointed his son-in-law to oversee economic policy while also dropping a market friendly minister from his cabinet. Further hurting sentiment was the central bank decision to hold rates in the face of high inflation. The damage was exacerbated by sanctions imposed by the US. Some ground was clawed back in September when rates were hiked higher than expected and one of the country's largest banks received positive responses abroad for its refinancing drive. The end of the year saw Turkish assets gain from a decline in pressure on the Turkish lira. The currency rose following dovish comments from the Fed on its path of future rate hikes. Our overweight in Turkish Financials hurt performance.

An investor should consider the fund's investment objectives, risks, charges and expenses before investing. This and other important information can be found in the fund's prospectus. To obtain a prospectus please visit www.gmo.com. Read the prospectus carefully before investing.

Risks associated with investing in the Fund may include Market Risk - Equities, Management and Operational Risk, Non-U.S. Investment Risk, Liquidity Risk, and Derivatives Risk. For a more complete discussion of these risks and others, please consult the Fund's prospectus. Distributor: Funds Distributor LLC. GMO and Funds Distributor LLC are not affiliated.

¹ The MSCI Emerging Markets Index (MSCI Standard Index Series, net of withholding tax) is an independently maintained and widely published index comprised of global emerging markets large and mid capitalization stocks. MSCI data may not be reproduced or used for any other purpose. MSCI provides no warranties, has not prepared or approved this report, and has no liability hereunder.