# Emerging Markets Value Equity Fund Investment Outlook

## Presidential Elections likely to Dominate News Flow

2023 ended on a positive note for global stocks, including emerging markets (EM), with the notable exception once again of China. The MSCI Emerging Markets index was up 7.9% in Q4 resulting in a 9.8% return for the year. It could have been so much better though, if not for the index's largest component underperforming to the degree it did. Chinese stocks continued to disappoint investors. The MSCI China index fell 4.2% in the final quarter of the year for an annual loss of 11.2%. China's detrimental impact on the asset class meant EM once again lagged developed markets. When one strips out China however, the story is quite different. The EM ex-China Index broadly kept pace with the developed world's strength, returning 12% in the quarter and 20% for 2023. After 3 consecutive years of substantial negative returns for China, it is clear that for EM to outperform developed markets, China's underperformance needs to reverse.

Regarding the MPEMX portfolio, we outperformed the MSCI Emerging Market index in the final quarter and for the year as a whole. 2023 alpha was mostly generated from positive stock selection in Korea, China, Brazil, Indonesia and Taiwan; while asset allocation added value from being overweight Latin America, and zero exposures to South Africa, Thailand and Malaysia which all posted negative returns. The main negative on the year was the fund's underweight to the less value oriented Indian market, which once again outperformed.

For the most part therefore, 2023 was a good year for stock markets, as inflation levels fell off highs and expectations for interest rates easing reassured investors. As for China however, geo-political concerns were amplified by deepening economic fears as its property market suffered under a cloud of high debt and unsold inventory. After 3 years of underperformance, we believe China is a value market, where the fund is neutrally positioned. We have written extensively on China before and don't intend to do so here. Nevertheless, for China to outperform this year, it doesn't necessarily need to result from anything heroic on China's part, for 2024 is a year that could present heightened uncertainty and headlines elsewhere.

In 2024, about two billion people, an unprecedented number, will go to the polls in more than 70 countries to vote for new leaders and governments. The results are of crucial importance in determining whether global tensions will increase or be reduced, whether fragile democracies can be strengthened or whether autocrats can tighten their grip through poll rigging, repression of opposition parties and fraud. As well as the critical United States Presidential election, six markets that account for over 50% of the MSCI Emerging Markets index head to the polls – India, Taiwan, South Korea, South Africa, Mexico, and Indonesia.

Possibly one of the most significant, will be the first of the new year. On January 13th, Taiwan is to vote for a new president. The gap is closing between William Lai, the current vice president from the ruling Democratic Progressive Party (DPP), and Hou Yu-ih, leader of the Kuomintang (KMT), which favors a more accommodating stance to Beijing than the pro-independence DPP. China has frequently warned that any moves towards promoting Taiwanese independence are an unacceptable breach of its "One China" principle. Therefore, military tensions across the Taiwan Strait are likely to rise significantly if Lai is returned to office and pursues full independence. A KMT victory might therefore be considered favorable by the market given the party's more reconciliatory stance with Beijing.

**MSCI Emerging Markets index -** captures large and mid-cap representation across 24 Emerging Markets (EM) countries
**MSCI Emerging Markets ex China Index -** captures large and mid cap representation across 23 of the 24 Emerging Markets (EM) countries* excluding China
**MSCI China Index -** captures large and mid cap representation across China A shares, H shares, B shares, Red chips, P chips and foreign listings (e.g. ADRs).

The biggest election to be held will be when around 950 million people vote over several weeks to appoint a new Indian Prime Minister. India is the world's most populous country and its largest democracy. The incumbent National Democratic Alliance (NDA), the coalition dominated by the Bharatiya Janata Party (BJP) under the leadership of Narendra Modi is leading the opinion polls, although indicating a marginally reduced mandate. Modi is hugely popular with investors, and India is widely regarded as one of the worlds more expensive stock markets. Hence, any disappointment in the extent of Modi's mandate could damage market buoyance.
Elsewhere in Asia, Indonesia will elect a new leader as President Jokowi's highly successful term in office comes to an end. Leading contenders, Prabowo Subianto (Gerindra) and Ganjar Pranowo (PDI-P) are viewed favorably by the market as continuity candidates who should maintain the momentum of Jokowi's reforms which have helped economic growth. While in South Korea, after the transfer of the presidency to the People Power Party (PP) in March 2022, polls are signaling the government may enlarge their minority of 112/300 seats enabling President Yoon Suk Yeol greater potential to deliver his agenda.

Outside of Asia, there will be the farce of a Russian Presidential election, while the South African ballot will also likely be blighted by accusations of corruption and manipulation. An already economically precarious nation can little afford a contentious election, which we believe will be a likely eventuality. Mexico should offer greater hope though, despite Amlo relinquishing power after a relatively successful term in office. Although how much of the country's success is down to his policies is questionable. Currently, it looks as if Mexico may elect its first ever female President as the two leading candidates are both women. Mexico's fate however may be just as influenced by the outcome of the US election. The world's quintessential democracy looks as if it will once again have a choice between incumbent Joe Biden and Donald Trump. The result will of course not simply have ramifications for the US, but many emerging markets too.

Alongside so many elections upcoming in 2024, the geo-political risks of sustained or escalating conflict in the Middle East & Ukraine seem unlikely to dissipate any time soon; whilst it is still plausible that the US economy could slow considerably once the impact of higher rates is more tangibly felt. It is reasonable therefore to expect a year of uncertainty and volatility. Ironically, for emerging markets, while over 50% of the asset class will go to the polls this year, our largest market China, is of course not a democracy. Hence whilst many risks still linger for China, election-driven political instability is unlikely to be one of them. Beginning the year from such a low absolute and relative valuation base, the chance of some level of outperformance for China is arguably achievable, especially if other parts of the market which have performed well come under political or other pressures; and the Taiwanese election result placates investor concerns.

All the above points to the need for a defensively positioned, value-oriented portfolio in our opinion. We end the year with the fund trading on a Price to Earnings Ratio (P/E) of c.11x versus the MSCI EM index of c.14x and a dividend yield of c.4% against the index of 3%, thereby exhibiting what we consider value metrics. Mondrian's years of experience covering emerging markets suggest that if there is short term volatility around election cycles, it can often create opportunities to buy attractive companies at cheap prices. While the top-down outlook is of course important to us, we ultimately buy businesses, many of which typically demonstrate resilience despite economic and political challenges. We will therefore be keeping a close eye on political developments throughout 2024 to see if any negative market sentiment presents circumstances to capture bottom-up value stocks for long term minded investors such as Mondrian.

**Price to Earnings Ratio -** The P/E ratio is calculated by dividing the market value price per share by the company's earnings per share

**Dividend Yield** - a financial ratio that shows how much a company pays out in dividends each year relative to its stock price.

## Disclosures

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