

Ethical Emerging Markets Value

EQUITY

Global EM strong in 2017

Earnings growth key return driver

Markets For most of 2017, emerging market equities significantly outperformed developed markets, and December was no different. The month saw the MSCI EM index rise 2.86 percent in Euro terms, while MSCI World (developed markets) rose only 0.64 percent.

This means that over 2017, MSCI EM rose 20.59 percent, compared to just 7.51 percent for MSCI World. The main driver for the strong emerging market returns was earnings growth: based on MSCI EM, it looks likely that earnings grew by over 20 percent in 2017 – significantly higher than the previous year, and developed markets. We have argued for some time that as GDP growth in emerging economies starts to accelerate again relative to developed markets, this would be a tailwind of emerging market equities – and that is what happened in 2017. There is potential for growth to remain supportive in 2018.

Of course, there were differences across the broad emerging market universe. One major issue was the performance of IT stocks – discussed below. By country, China was among the year's strongest performers, rising 33 percent in Euros. There has been increased supply-side discipline in industries with overcapacity, which boosted profit margins and cash flows, and eases credit risk. Meanwhile, Russia was among the weakest markets, with negative returns. This was partly because it had rallied so strongly lately in 2016, and perhaps because of disappointment that President Trump's win did not, in fact, lead to improved relations.

Politics continued to make their mark in December. In South Africa, the ANC leadership contest mid-month was won by

Cyril Ramaphosa, making it highly likely he will succeed Jacob Zuma as president. He is considered pro-reform, and has spoken strongly against corruption. The South Africa Rand has rallied sharply since then. We note that in 2018, Russia, Mexico and Brazil will hold presidential elections, while India will start gearing up for elections in 2019.

Fund well ahead of value universe

The Portfolio In December, the fund gained 4.11 percent, while MSCI EM gained 2.86 percent. This means that over the full year 2017, the fund rose 19.44 percent. This was marginally behind the MSCI EM's 20.59 percent, but significantly ahead of MSCI EM Value, which rose only 12.49 percent.

As we have previously noted, a major factor in 2017 was the performance of certain mega-cap tech stocks – and especially internet names – which dominated the MSCI EM index. As of year-end, the IT sector weight was around 27 percent of MSCI EM, but over 44 percent of MSCI EM Growth, and less than 11 percent of MSCI EM Value. The IT sector rose by around 40 percent in 2017, which was a key driver of growth stocks to significantly outperform value stocks. Our fund has significantly less IT exposure than MSCI EM, mainly because we find the internet names rather expensive. The IT names in which we do invest, actually performed very strongly – rising around 47 percent in 2017 – but this was not quite enough to offset our relatively low exposure, which explains why the fund fell slightly short of MSCI EM. We will continue to focus on selecting undervalued stocks, to drive long-term returns.

Return is calculated gross of fees and excluding swing.

See performance and fund data

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Strategy

Ethical Emerging Markets Value invests in equities issued by companies from Emerging Markets, cf. the fund's prospectus. Stocks are selected using the value strategy, meaning that through careful fundamental analysis, the team strives to identify companies that trade at healthy discounts relative to intrinsic value. A risk-aware approach to the portfolio construction ensures a well-diversified portfolio and broad exposure across sectors and countries.

For further information we refer to the prospectus, the key investor information document and the current annual / semi-annual report of Sparinvest SICAV which can be obtained free of charge at the offices of Sparinvest or of appointed distributors together with the initial statutes of the funds and any subsequent changes to such statutes. Investments are only made on the basis of these documents. Past performance is no guarantee for future returns. Investors may not get back the full amount invested. Investments may be subject to foreign exchange risks. The indicated performance is calculated Net Asset Value to Net Asset Value in the fund's base currency, without consideration of subscription fees.