Sparinvest

Ethical Emerging Markets Value

EQUITY

Emerging markets look robust

Volatile markets in June

Markets Emerging markets have their fair share of political noise, but June was dominated by the UK referendum on EU membership. As the vote approached, financial markets seemed positioned for a 'remain' victory, so the actual result sent a 'risk off' shock wave through the markets. Gold rose, bond yields fell, and equities fell – with cyclical sectors underperforming defensive sectors.

That shock has eased somewhat, but more specifically, emerging market equities were relatively robust after the referendum result, falling less than developed markets. The MSCI EM benchmark gained over 4% in June, with similar returns year-to-date. Meanwhile developed markets had slight negative returns both in June and year-to-date.

After a few years of relatively weak EM equity returns compared to developed markets, we see various factors that may be supportive. Emerging market GDP growth had been shrinking relative to developed markets for some years, but that gap may stabilise going forward. Emerging market inflation may start to ease relative to developed markets – which could be positive for EM currencies.

Shorter term, prospects of further US Fed interest rate hikes this year have receded – which is supportive of emerging market currencies and equities. June saw strong currency rallies for Brazil and South Africa, two countries with characteristics (current account deficits, foreign denominated debt) which make their currencies relatively vulnerable to US dollar strength. In June, they benefited from the fall in US bond yields. South Africa also enjoyed relief at narrowly avoid a credit rating cut from S&P. As Brexit fallout focusses attention on global central bank policy, yield-rich emerging markets may benefit.

Strong absolute performance

Performance Year-to-date, our fund has returned 6,39% compared to the benchmark's 4,05%. In June, the fund rose 3,31%, slightly less than the benchmark's 4,21%. The slight shortfall was for two main reasons. Firstly, the fund excludes investment in Samsung Electronics. This has the single largest company weight in the benchmark, and rallied over 14% in EUR terms last month. Secondly, the fund has relatively low exposure to Brazil and South Africa, and as noted above those currencies rallied strongly in June.

Latin American stocks and materials/commodity stocks were among our strongest performers. Brazilian retailer Cia Brasileria de Distribuicao has suffered in recent month's from Brazil's economic malaise and low consumer confidence, but rallied over 30% in EUR terms in June. Peruvian miner Buenaventura rose 26% thanks partly to copper prices, but especially the gold price rally post-Brexit result.

Our largest detractors – aside from the lack of exposure to Samsung – were shipping company Orient Overseas and Malaysian surgical glove maker Supermax. Orient Overseas fell with freight rates, taking its price/book valuation towards trough levels. Supermax, an exporter, is seeing short term earnings pressure partly due to strength in the Malaysian currency.

Overall, we are reassured by the valuations of our holdings and see good potential. To the extent that market volatility continues, we will aim to exploit it by seeking compelling new investment opportunities, while maintaining a prudent risk awareness.

Strategy

The fund invests in value stocks. Through careful fundamental analysis, the team strives to identify companies that trade at healthy discounts relative to intrinsic value. A risk-aware approach to portfolio construction ensures a well diversified portfolio. The Fund pursues an active value investment strategy, which is the reason why performance may deviate from benchmark.