LIONTRUST

GLOBAL EQUITY

Liontrust Emerging Markets Fund

Q3 2022 review

Fund manager: Ewan Thompson

The Liontrust Emerging Markets Fund returned -0.6%*^ over the quarter, compared with -3.8% from the MSCI Emerging Markets Index comparator benchmark and the 2.6% average from the IA Global Emerging Markets sector, also a comparator benchmark.

The third quarter continued − and even amplified − the well-established negative trends predominant in 2022 so far. Equity markets suffered ongoing losses across the board, taking year-to-date dollar returns to -27% and -29% for developed and emerging markets respectively. The key macro dynamics remain the relentless rise in global interest rates in order to respond to high and rising inflation across the majority of economies. The rise in US interest rates in particular, along with the prevailing cautious economic outlook, has also served to push the US dollar higher, which has in turn prompted currency weakness across both emerging and developing markets, exacerbating the inflation and interest rate cycle.

With global liquidity sharply tightening, the outlook for growth has also clearly deteriorated, with recessionary threats increasing in both the US and Europe. Moreover, the other key driver of the global economy − China − remains in the economic doldrums with its ongoing zero-Covid policy hampering any potential economic recovery.

Given the weakness in China and economic concerns in the developed markets, it is unsurprising that the weakest markets throughout the quarter were those in North Asia. China fell -23% in dollar terms, with tech-heavy and trade-centric Taiwan (-18%) and South Korea (-16%) also falling sharply. In the case of Taiwan and Korea, these negative returns were also compounded by notable FX weakness, with the South Korean won falling over 10% against the dollar, taking its year-to-date return to -20%. The global technology cycle remains weak, with end demand for products − especially in the consumer channel − showing notable weakness, and inventories have been building along the supply chain.

However, with the notable exception of China, it is remarkable how well (in relative terms) a number of traditional, core emerging markets are performing during this difficult time. Given the sharp increase in interest rates, relentless dollar strength and high risk aversion, one would ordinarily expect emerging markets to be suffering acutely at this stage of the economic cycle. However, several markets have bucked the trend, most obviously India (+6%), Indonesia (+8%) and Brazil (+4%), which produced positive dollar returns over the quarter.

Brazil and Indonesia have of course been supported this year by higher commodity prices, but there is also the underlying reality that emerging market monetary policy has, across this cycle, been notably prudent and successful. Brazil, for example, hiked rates aggressively and early and is now being rewarded − the real is one of the very few currencies to have appreciated against the dollar this year. It is rather fitting that four of the five 'Taper Tantrum' emerging market economies from 2013 − those markets running large current-account deficits that ran into macro-economic crises as global monetary policy tightened − have now hugely outperformed developed markets this year, demonstrating the degree that orthodox and prudent monetary policy has now become the preserve of emerging markets whilst developed market central banks are forced into evermore unorthodox strategies to address anaemic underlying growth.

The Liontrust Emerging Markets Fund outperformed during the quarter. Key areas of outperformance included stocks held in India, Indonesia and Brazil − all markets which the Fund is overweight. Within this, the Indian healthcare sector was a notable area of strength with southern Indian hospital chain **Krishna Institute of Medical Sciences** and domestic pharmaceuticals player **JB Chemicals & Pharma** among the risers as domestic demand remains highly resilient to external macro pressures. The Indian financials sector has also continued to move from strength to strength, with credit growth accelerating, margins expanding and asset quality robust; positions in private sector lender **ICICI Bank** and **State Bank of India** have performed well against this backdrop. In Brazil we have also seen a very positive backdrop for the banks, with Brazilian private bank **Itau** performing extremely well. So too in Indonesia, where **Bank Mandiri** and micro-lending focussed **Bank Rakyat** have prospered.

A number of changes were made through the quarter, including the purchase of Brazilian electronics manufacturer **Intelbras**, which provides equipment to the surveillance, telecoms and energy sectors with strong market share and a robust pipeline of new projects.

The majority of the other additions were in China, where the notable underweight was reduced, reflecting the extremely subdued valuations and woeful sentiment. A small initial position was initiated in **Ping An Insurance**, where exposure to the property market has led the share price to fall steeply. We believe that over the medium- and long-term, Ping An is the best in class within its sector and a technology leader, having spent recent years cleaning up its distribution model. When the economy eventually stabilises and re-opens, we think it will have further embedded its structural advantages over slower-moving peers. New positions were funded by sales including **Mediatek** in Taiwan, where the industry outlook and cyclical headwinds for the technology sector are currently too great;we will reappraise when the demand visibility is clearer.

This has clearly been a very tough year for global markets and the dollar losses are considerable − that said, we would re-iterate the impressive resilience of emerging markets ex-China, which have by-and-large significantly outperformed developed markets at a point in the cycle when they would ordinarily see much more significant selling pressure.

Moreover, we see the relative merits of emerging over developed markets as well defined: relative growth rates above OECD, less damaging effects of inflation, and aggressive and pre-emptive monetary policy giving plenty of headroom to support both currencies and economies. We expect to see this trend of outperformance continue, and, as and when markets recover, we believe emerging markets stand to record significant outperformance given the extremely attractive relative valuation picture. The key variable is of course China, where news has clearly been more disappointing. Potential light at the end of the tunnel would be a more pro-growth economic stance emerging from the 20th Party Congress which gets underway in the coming weeks. A recovery here would have a profoundly positive impact on the prospects for emerging markets as a whole.

Discrete years' performance (%), to previous quarter-end:**

	Sep-22	Sep-21	Sep-20	Sep-19	Sep-18
Liontrust Emerging markets C Acc GBP	-16.7%	15.5%	1.6%	5.3%	-2.1%
MSCI Emerging markets	-13.2%	13.3%	5.4%	3.7%	2.0%
IA Global Emerging markets	-15.4%	17.0%	2.0%	6.5%	-1.5%
Quartile	3	3	3	3	3

***Source: FE Analytics as at 30.09.22**

****Source: FE Analytics as at 30.09.22. Quartile generated on 07.10.22**

For a comprehensive list of common financial words and terms, see our glossary at:
https://www.liontrust.co.uk/benefits-of-investing/guide-financial-words-terms

Key Risks

^Past performance is not a guide to future performance. The value of an investment and the income generated from it can fall as well as rise and is not guaranteed. You may get back less than you originally invested.

The issue of units/shares in Liontrust Funds may be subject to an initial charge, which will have an impact on the realisable value of the investment, particularly in the short term. Investments should always be considered as long term.

Investment in the Fund involves foreign currencies and may be subject to fluctuations in value due to movements in exchange rates. The Fund may invest in emerging markets/soft currencies or in financial derivative instruments, both of which may have the effect of increasing volatility.

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