NEDGROUP INVESTMENTS

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Nedgroup Investments Global Emerging Markets Equity Fund

Quarter One, 2023

Marketing Communication

Economic and Monetary Backdrop

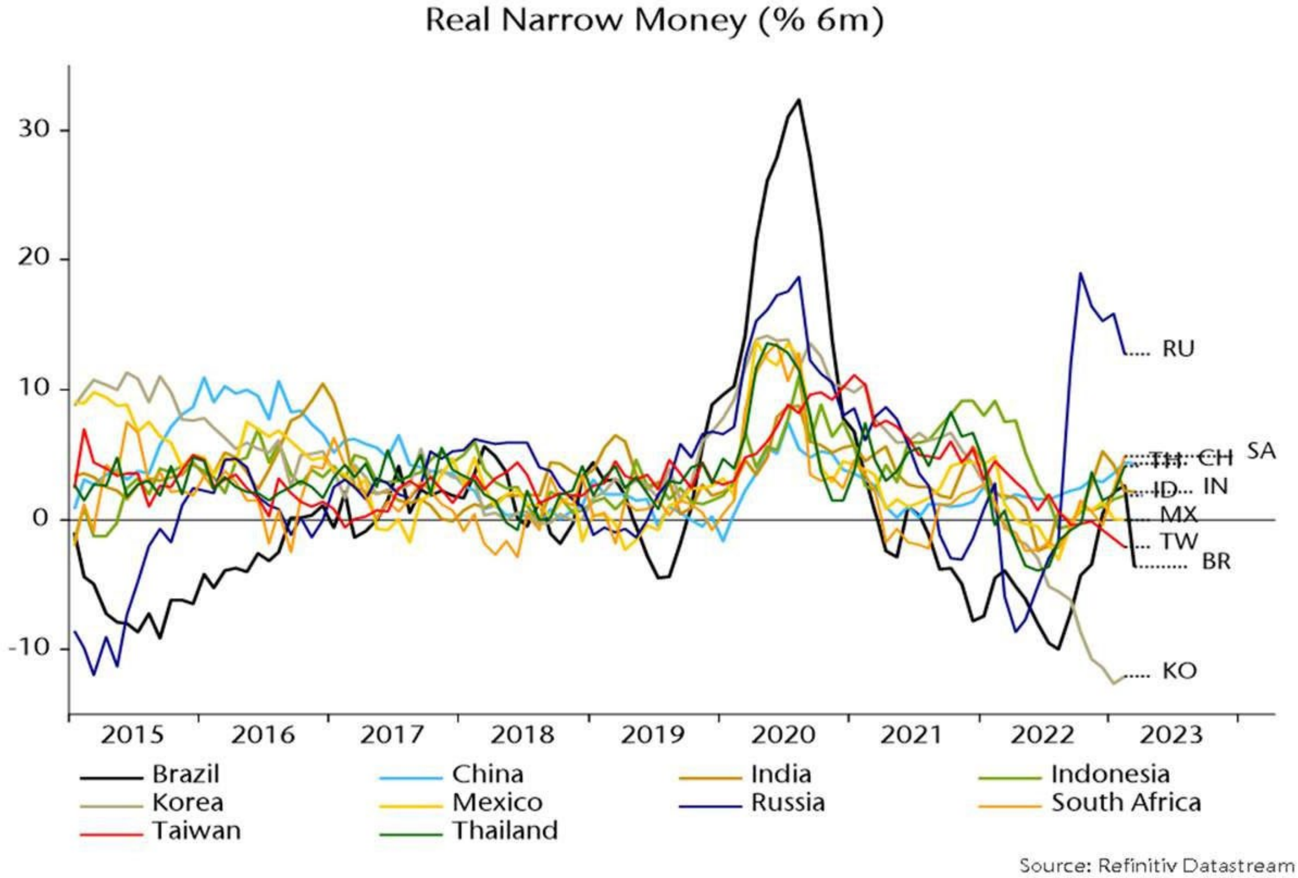
Global six-month real narrow money momentum – a key leading indicator in the forecasting approach here – continues to give a negative message for economic prospects. Momentum recovered slightly during H2 2022 but failed to break into positive territory and fell back during Q1. The suggestion is that a recent revival in global PMIs will reverse into H2:

Real money momentum remains below industrial output momentum, which has been temporarily boosted by Chinese reopening. The monetary shortfall casts doubt on the sustainability of the Q1 equity market rally.
G7 headline CPI inflation rates have started to fall sharply, mirroring a decline in nominal money growth two years earlier. This relationship suggests a return to pre-pandemic inflation levels by mid-2024 and an undershoot thereafter.

Global monetary weakness is being driven by the US / Europe, with China / EM showing relative strength – the E7 / G7 real money momentum gap has widened further. This is positive for EM relative economic performance but does not necessarily imply that equities will outperform – historically, this has usually also required a favourable global excess money backdrop.

Chinese real narrow money momentum remains relatively strong – see chart below – but has been inflated by a fall in consumer prices, probably temporary. Nominal money growth is range-bound and a rise in short rates since late 2022 may have a dampening effect. The expectation here is for a moderate economic recovery that may require further policy support to offset global headwinds.

Elsewhere, real money momentum has picked up strongly in South Africa and Thailand, suggesting improving economic prospects, and is respectable in India and Indonesia. Extreme weakness in Korea signals that policy has been overtightened, while Brazilian momentum turned negative again at end-Q1:



Portfolio strategy

Central banks are now in policy mistake territory, a phase where financial accidents are set to occur in increasing frequency should monetary tightening persist. Previous commentary has flagged the deterioration in money numbers globally, the basis for our defensive positioning. While this made for some difficult periods through 2022 as more cyclical names rallied on a hot global economy, deteriorating economic data and cracks in the financial system – including SVB, Signature Bank and Credit Suisse – signal that tightening is beginning to bite. Markets have pivoted from the "no landing" scenario and now price in the expectation of a pause by the Fed as stresses in the financial system exacerbate the drag of tight money. Our view remains that central banks have done enough to bring inflation back to pre-covid levels and economic growth will disappoint through the year. Against this backdrop, the portfolio outperformed the MSCI EM Index over the quarter.

Stocks in Taiwan and South Korea rebounded over the quarter, leading contributions to performance at a country level. Pandemic stockpiling of chips for PCs, servers, smartphones and autos underpinned one of the steepest downcycles for the semiconductor industry since the GFC. As supply chains normalised and demand cooled, the North Asian chip industry was hit with an inventory correction that dragged on earnings. The subsequent tech selloff provided an opportunity to lift exposure to a slight overweight by adding some high quality names in Taiwan which should benefit from an end to inventory destocking. For example, fabless chip designer Parade Technologies specialises in the development of high speed data transmission chips for customers that include Apple and Samsung. We sold highly defensive names such as 7-11 franchise owner President Chain Store and CTBC Bank, while topping up existing names such as TSMC and 5G system-on-a- chip designer Mediatek.

In contrast to Taiwan's stable liquidity and economic data, South Korea's money numbers are weak as the Bank of Korea lifts rates. The property market has been a casualty and regulators are asking banks to suppress lending rates to help struggling borrowers, leading us to trim exposure to KB Financial. Our modest underweight to Korea reflects a bleak near term outlook. Further out, however, South Korea stands to be a beneficiary of supply chain reshoring. The US and Europe are looking to boost the manufacturing capacity of strategic technologies including renewables and batteries either onshore or in “friendly” countries. In this vein we added to LG Chemical, a conglomerate with exposure to demand for batteries through majority ownership of LG Energy Solution, the world’s second largest battery manufacturer, which trades at a significant premium to the parent. Other sustainability-linked drivers include battery materials and recycling businesses, and a petrochemicals business pivoting focus to the production of high margin recycled plastics.

Stock picking in India made a positive contribution at a country level, in part through the collapse in share price of Adani Enterprises. US short seller Hindenburg’s report on the Adani Group alleging fraud and stock manipulation is a test of market sentiment. Chairman Adani is a key supporter and beneficiary of the PM Modi’s nation-building plans, which have enabled the former to build an industrial empire across ports, power plants, resources, renewable energy and airports. The controversy appeared to be mana from heaven for the Indian Congress Party and its leader Rahul Gandhi, who has accused Modi of crony capitalism by helping Adani secure lucrative projects. Instead, Modi has kept quiet while supporters characterise the accusations as an attack on the BJP’s pro-growth agenda. Meanwhile, Gandhi was convicted of criminal defamation by a Gujarat court for remarks made about Modi at a 2019 election rally, and faces a prison sentence which jeopardises his chances of running in 2024 national elections. India exposure had been pared back from overweight towards neutral prior to the Hindenburg report on the basis of rich valuations. While our view is that the fallout risks appear contained and with state banks and foreign lenders bearing much of the counterparty risk, we did make a trim of ICICI Bank. Subsequent efforts by Adani to deleverage negatively impacted portfolio holding Container Corporation of India, one of the largest quarterly detractors. Adani had looked to be the likely buyer of the government-owned rail freight operator benefiting from the construction of a new national freight corridor. While Adani’s woes set privatisation back, the company provides exposure to a major infrastructure project that will unlock immense productivity gains. India has a highly saturated rail network which until recently was used simultaneously by passenger and freight trains. Development of dedicated freight corridors up, down and across the country will allow for fast and reliable transportation of goods. According to India’s Ministry of Railways, completion of the freight corridors over the next five or so years will see freight capacity more than quadruple, having only doubled in the 70 years prior.

Stock picking in China was a detractor, with several portfolio names such as China Education and sportswear giant Li Ning cooling after a strong reopening rally, driven in part by disappointment over the strength of the economic recovery. Money numbers in China have not been strong enough to support a reopening boom, reflecting policy restraint by authorities wary of sparking inflation through excessive stimulus. This approach should propel an incremental recovery that accelerates through 2023. This is supported by new homes sales, credit growth, PMIs and air traffic ticking up modestly over the quarter, all while inflation remains well below 3%. Investors turned to the “two sessions” (China’s parliament) in March for indicators of policy direction and for confirmation of appointments to critical positions in the state apparatus. Li Qiang was confirmed as Premier, taking helm of the economy by ratifying a modest 5% GDP target for 2023 and touting his support for private industry while serving as party boss of economic powerhouses Shanghai and Jiangsu and governor of Zhejiang. Li likely had a hand in the return of Jack Ma to Hangzhou, Zhejiang (where Alibaba is headquartered) in late March, soon followed by the announcement that the company would be split into six units. According to Alibaba CEO Daniel Zhang, the units will be able to “pursue independent fundraising and IPOs when they are ready.” The news sparked a sharp rally in the stock, along with shares of other tech giants such as Tencent on the view that restructuring through spin offs into more focused businesses will appease authorities’ concerns over their market power. While there is likely some temporary regulatory reprieve for the sector, direction of travel is still toward greater centralisation of control over the sector. The portfolio is neutrally weighted in China H-shares as at the end of the quarter and significantly overweight the A-share market, where we are able to find better long term structural opportunities.

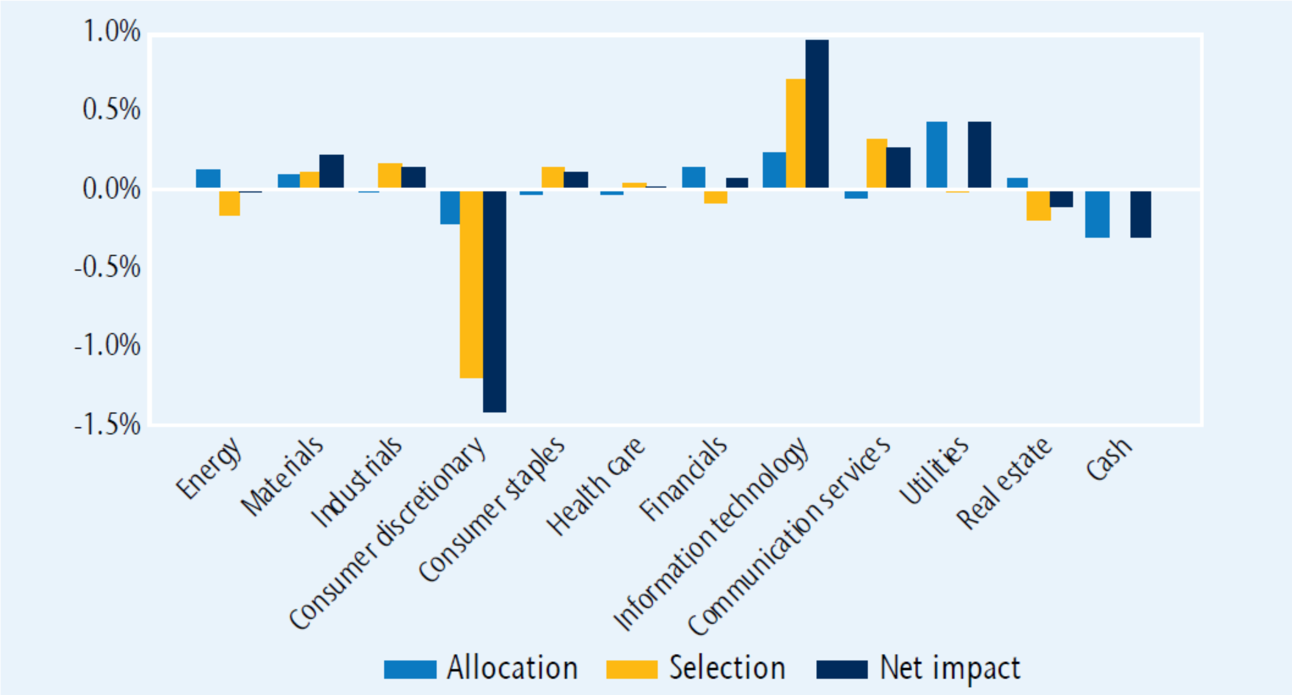
We remain cautious on equity markets after two better quarters. While a combination of inflation slowing globally and some leading indicators signalling a recessionary environment strengthens the case for central banks to pause, there is a risk of continued hikes if authorities in DM believe they have resolved issues in the banking system. These financial issues are emanating from DM, while EM looks broadly robust so far. Emerging market money numbers continue to pull away from DM, valuations are much lower than in the US and the earnings outlook for EM corporates is improving. In addition, real effective exchange rates in many emerging markets are as competitive as they have been for a decade or more. While this bodes well for the long term performance of EM, we will remain defensive until we reach a pivot point where global real money growth no longer falls short of economic growth.

Best and Worst Countries by Net Impact

Country	Allocation	Stock Selection	Net Impact
Brazil	0.2%	0.1%	0.3%
Taiwan	0.0%	0.3%	0.3%
Greece	0.2%	0.0%	0.2%
Saudi Arabia	0.2%	0.0%	0.2%
United Arab Emirates	0.2%	0.0%	0.2%
Philippines	0.0%	-0.1%	-0.1%
Thailand	0.0%	-0.1%	-0.2%
Hong Kong	-0.2%	0.0%	-0.2%
Mexico	-0.1%	-0.1%	-0.2%
China	0.0%	-0.3%	-0.3%

Source: NS Partners Ltd

Attribution by Sector



Source: NS Partners Ltd

Contribution Analysis

Top Contributors	Average Weight	Contribution
Shanghai Baosight Software Co	2.6%	0.4%
Tencent Holdings Ltd	5.3%	0.2%
Infosys Ltd	0.0%	0.2%
Adani Enterprises Ltd	0.0%	0.2%
Alibaba Group Holding Ltd	5.2%	0.2%

Source: NS Partners Ltd

Top Detractors	Average Weight	Contribution
China Education Group Holdin	1.6%	-0.3%
Container Corp Of India Ltd	1.1%	-0.3%
Longi Green Energy Technol-A	1.4%	-0.3%
Meituan	2.4%	-0.3%
Bharti Airtel Ltd	1.4%	-0.2%

Source: NS Partners Ltd

Activity During the Quarter

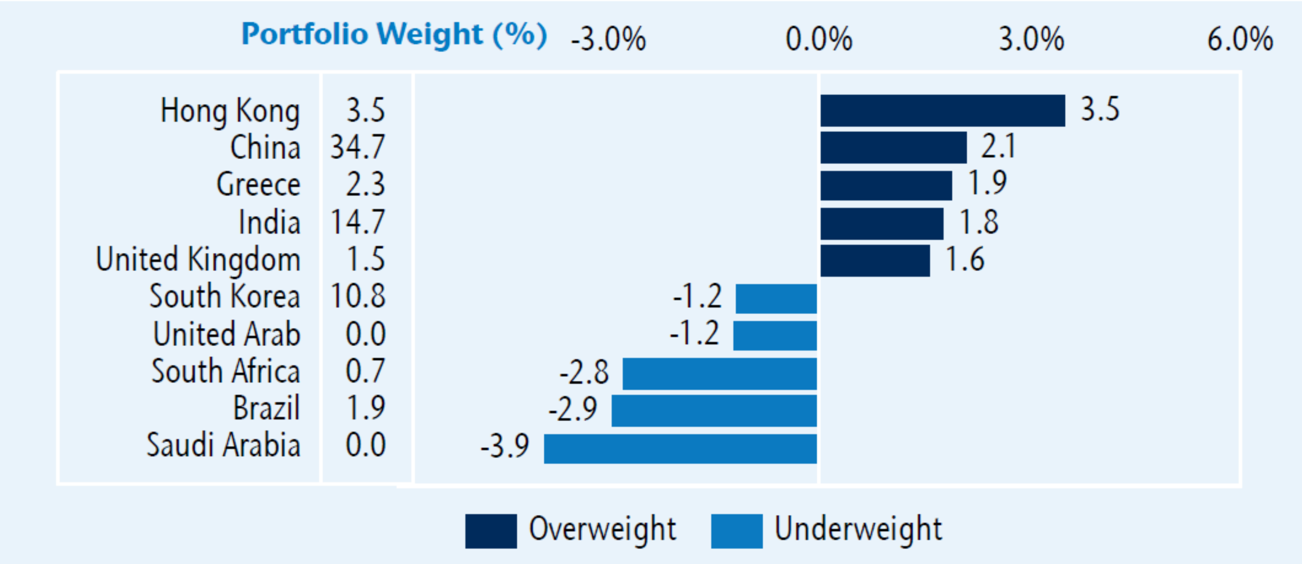
New	Exited
Hong Kong Exchanges and Clearing Ltd	CTBC Financial Holding Co Ltd
Yageo Corporation	Shenzhou International Group
Zhejiang Supcon Technology Co	ICICI Bank Ltd
Parade Technologies Ltd	Bank Rakyat Indonesia (Persero) Tbk
East Money Information Co-A	-

Source: NS Partners Ltd

Add	Reduced
Lg Chem Ltd	Haier Smart Home Co Ltd
Taiwan Semiconductor Manufac	Kb Financial Group Inc
Mediatek Inc	Contemporary Amperex Technolog
Larsen & Toubro Ltd	Public Bank Berhad
E Ink Holdings Inc	Nari Technology Co Ltd-A
Accton Technology Corp	Ememory Technology Inc
-	Prudential PLC
-	China Education Group Holdin
-	Varun Beverages Ltd

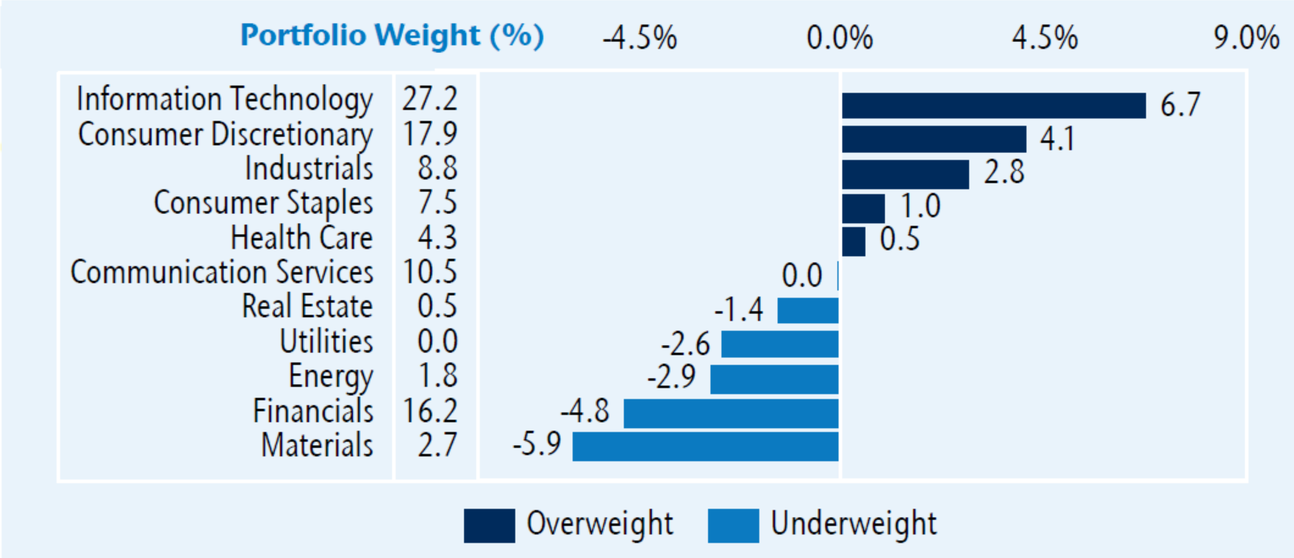
Source: NS Partners Ltd

Top Country Over/Under Weights vs MSCI EM Index



Source: NS Partners Ltd

Sector Allocation Over/Under Weights vs MSCI EM Index



Source: NS Partners Ltd

Top 5 Overweights

Company Name	Country	Sector	Active Weight
Samsung Electronics Co Ltd	South Korea	Information Technology	3.2%
Shanghai Baosight Software-A	China	Information Technology	3.1%
Varun Beverages Ltd	India	Consumer Staples	2.7%
Alibaba Group Holdings Ltd	China	Consumer Discretionary	2.4%
Housing Development Finance	India	Financials	2.2%

Source: NS Partners Ltd

Top 5 Underweights

Company Name	Country	Sector	Active Weight
Reliance Industries Ltd	India	Energy	-1.3%
China Construction Bank	China	Financials	-1.0%
Vale Sa	Brazil	Materials	-0.9%
Infosys Ltd	India	Information Technology	-0.9%
ICICI Bank Ltd	India	Financials	-0.9%

Source: NS Partners Ltd

Disclaimer

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