Nedgroup Investments Global Emerging Markets Equity Fund

Quarter Three, 2021

NEDGROUP INVESTMENTS

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Portfolio strategy

Emerging equity markets came under pressure in Q3 from a combination of regulatory concerns in China, a rising US$ and signs that the delta variant has slowed the global economic recovery. The MSCI Emerging Markets index fell 6.69% in local currency terms and 8.09% in US dollars. Energy was the strongest sector with a 9.1% gain while consumer discretionary was the weakest, falling 22.9%. Argentina was the best performing market, rising 22.1%, while Brazil was the worst, with a 20.1% loss reversing much of the previous quarter's gain.

Corporate profits and earnings revisions have continued to surprise positively in Q3 but some companies' margins are being squeezed by a combination of slowing global growth, supply bottlenecks, higher commodity prices and rising transport costs. A major issue is the elevated oil price and rising gas prices which have pushed up revisions in the energy sector. Oil as measured by Brent rose 5% over the quarter but gas prices are up much more around the world due to underinvestment in production, higher demand and in Europe competition for supply with China. We have added to energy including introducing Gazprom in Russia which is attempting to address the shortage issue. The company has insufficient gas to rebalance the market itself but demand destruction will take much of the adjustment strain. Power generation from gas has started to decline and there is demand substitution in favour of coal. The company is unhappy with current prices because of the associated market disruption. Gas production volumes are hitting 13 year highs while oil production is also on the way up. Dividends are rising rapidly on a stock that already yields 3.3%.

In materials China has cut steel production to slow its construction-intensive economy and reduce pollution around Beijing ahead of the winter Olympics. We remain underweight the sector overall but like Scg Packaging in Thailand which has a competitive advantage providing both paper and plastic packaging solutions. The company is slowly rolling out vertical integration to other parts of ASEAN such as Vietnam, Indonesia and Philippines. In industrials our largest position is in Chinese battery maker Contemporary Amperex Technology which has global scale and cost advantage that drives its ability to invest in the requisite R&D to have a portfolio of EV systems for the coming transitions.

In consumer discretionary earnings revisions have generally been positive as some re-opening plays have started their recovery but there was a notable decline in the Macau casino operators which were downgraded after changes to the regulatory regime that could jeopardise gaming licence reviews. In autos semiconductor supply problems are affecting the availability of new vehicles and pushing prices of used cars higher and even above the listed price of new autos at the dealers. Pricing power in the industry means no discounts for new vehicles and waiting times of over a year in some cases for new orders. In luxury there has been concern that the new common prosperity policy might negatively impact sales but if the aim is a larger middle class the outcome may raise revenues in the longer term. Supply for some garment and sportswear makers has been disrupted by Covid lockdowns in Vietnam leading to downgrades in near term estimates. In staples some spirit and beer manufacturers might expect to be impacted by the slowdown in China but there is little evidence of it yet in the numbers. Rising commodity prices and distribution costs will start to squeeze reported margins for the food manufacturers. Food retailers, which benefited in 2020 from continuing demand in the pandemic, are also being impacted by rising costs. We have reduced Alibaba but still favour drinks companies such as Heineken Malaysia, Varun Beverages and Bud APAC listed in Hong Kong but selling premium beer in China.

In financials investment banking has benefited from continued robust capital markets activity with M&A and bond syndication particularly strong. Equities are still profiting from the lack of investment alternatives open to the retail investor, helping asset gatherers – we still like the insurance growth story played through London listed Prudential. In IT the debate rages over whether the semiconductors are at peak cycle because Covid brought forward demand for chips as sales of electronic devices boomed – or will the cycle be stronger for longer? Tech and growth stocks remain negatively correlated with the direction of real yields short term while financials, commodities and cyclicals are positively correlated.

Regionally, we have been underweight China for some time, principally but not solely due to negative views on the economy and liquidity. We believe the authorities are preparing to ease as monetary policy has been too tight for too long. Within this underweight position we are underweight H shares, significantly underweight ADRs and overweight A shares, where we see strong long term growth opportunities and can find companies that are operating in areas supported by government policies or where the regulatory temperature is lower. We are focused on government-favoured areas such as solar, EV battery and software. Elsewhere the focus has been on underweighting cyclical or low-money-growth markets such as Brazil and South Africa in favour of liquidity-sensitive South East Asia, Greece and India, where inflationary pressures are less intense and money trends are holding up better. Our EM checklist remains mixed with the key requirement for improvement remaining a Chinese policy reversal.

Performance Attribution and Commentary

3 Months to September 30, 2021	Allocation (%)	Stock Selection (%)	Net Impact (%)
Total	0.91	0.90	1.81
Emerging Market Asia	0.84	0.82	1.66
China	0.47	0.22	0.70
Hong Kong	-0.45	0.00	-0.45
India	0.43	0.66	1.09
Indonesia	0.00	0.17	0.17
Malaysia	0.00	-0.01	0.00
Philippines	0.06	0.23	0.29
South Korea	0.15	0.12	0.28
Taiwan	-0.03	-0.56	-0.59
Thailand	0.19	-0.03	0.17
Emerging Market Europe, Middle East and Africa	-0.51	0.15	-0.36
Greece	0.20	-0.03	0.17
Gulf Markets (Saudi Arabia, Qatar, UAE, Kuwait)	-0.75	0.00	-0.75
Hungary	0.03	0.01	0.04
Poland	-0.04	-0.03	-0.07
Russian Federation	0.00	0.27	0.28
South Africa	-0.07	-0.06	-0.13
Emerging Market Latin America	-0.03	-0.07	-0.10
Brazil	0.21	-0.09	0.12
Chile	-0.02	0.02	0.00
Mexico	-0.17	0.00	-0.17
Frontier Markets	0.05	0.00	0.05
Cash	0.23	0.00	0.23
Other	0.34	0.00	0.34

The MSCI Emerging Markets index declined 8.09% in US dollars over the course of Q3, with a 6.69% fall in local currency terms magnified as the dollar gained against the basket of EM currencies. In the portfolio, positive country and security selection helped relative returns whilst sector selection was neutral overall. The best performing markets included Czech Republic (+16%), India (+12.8%) and Russia (+9.8%). The energy sensitive markets of the Gulf gained between 6.4% (UAE) and 9% (Kuwait) as the WTI benchmark rose a further 5% over the quarter, reflecting post-pandemic demand recovery and continued OPEC+ output discipline. By contrast, Brazil (-20.1%), China (-18.1%) and Korea (-13.4%) were among the weaker markets in Q3. The fund's underweights in these markets along with overweights in India, Greece (+2.1%) and Thailand (-3.5%) were positive for relative returns and more than offset the underweight in the Gulf markets. Security selection was positive in India, Russia, Korea and China more than offsetting disappointing relative performance in Taiwan.

In addition to the overweight country position, the fund benefitted from our above-index exposure to Indian property as Godrej Properties (+65.6%) posted strong gains with investors viewing its strategically attractive land bank as offering better growth prospects compared with other players in real estate. In healthcare, Max Healthcare Institute gained 41.5% as profits for the preceding quarter were reported up 100% YoY boosted by high bed occupancy in the hospital network. In consumer staples, the overweight in Pepsi bottler Varun beverages (+23.6%) was another strong contributor. Positive security selection in China was a result of strong gains in IT names. Shanghai Baosight Software (+29.7%) is in the industrial automation software business, which is benefiting from policy support for measures to reduce emissions and energy intensity in the steel industry. Longi Green Energy (-7.2%) had another strong relative quarter as China declined almost 18%. The underweight in communication services index heavyweight TenCent (-21.2%) was also positive for relative returns. In consumer discretionary Midea Group (-2.4%) and Haier Smart Home (+2.7%) worked well in Q3. As mentioned, the fund's underweight in Korea was positive and the overweight in Polysilicon sand speciality chemical producer OCI Co Ltd (+30.4%) further boosted returns. OCI is one of very few non-Chinese polysilicon producers and demand from the green energy transition remains robust.

In Taiwan the negative relative return was a result of poor returns in IT due to Accton Technology (-18.8%). The supplier of high-speed switching and networking equipment to global data centres disappointed in Q2 when component restrictions hampered sales. We remain positive on the outlook as demand for Accton's products remains robust and will recover with debottlenecking of the supply chain. We had zero exposure in financials in Taiwan and this was a further drag on relative returns as the sector gained 10.7% in Q3.

ASEAN exposure in Thailand, Indonesia and the Philippines was positive again this quarter. Money growth rates are holding up in these markets, contributing to our positive outlook. Thailand is moving steadily towards the reopening of its tourism sensitive economy to foreign visitors and positive sentiment towards the market helped financials. Our overweight in Kasikorn Bank (+7.6%) worked well although energy holdings in PTT (-3.0%) and PPTE&P (-3.03%) disappointed this quarter. In the Philippines, our consumer staple Monde Nissin (+8.9%) was a positive contributor. In Russia we have increased our overweight in energy giant Gazprom (+34.7%) as it became clear that the headline-grabbing increase in European gas prices is unlikely to fade quickly, enhancing the firm's profitability. Yandex (+12.4%) and Sberbank (+13.3%) also delivered good performance in Q3.

Portfolio activity

Top Purchases

Country	Security	Sector	%
South Korea	Kb Financial Group Inc	Financials	1.68
South Korea	Samsung Electronics Co Ltd	Information Technology	1.62
China	Flat Glass Group Co Ltd-H	Information Technology	1.14
India	Larsen & Toubro Ltd	Industrials	1.11
Taiwan	Aspeed Technology Inc	Information Technology	1.06
Taiwan	Unimicron Technology Corp	Information Technology	0.95
Taiwan	China Steel Corp	Materials	0.71
India	Hdfc Bank Limited	Financials	0.68
China	JD.com Inc-Adr	Consumer Discretionary	0.61
Taiwan	Taiwan Semiconductor Manufac	Information Technology	0.49

Top Sales

Country	Security	Sector	%
China	Ping An Insurance Group Co-H	Financials	1.24
South Korea	Sk Hynix Inc	Information Technology	1.13
China	Dada Nexus Ltd - ADR	Consumer Discretionary	1.09
South Korea	Shinhan Financial Group Ltd	Financials	1.04
South Korea	NAVER Corp	Communication Services	1.00
Taiwan	Mediatek Inc	Information Technology	0.92
Brazil	Localiza Rent A Car	Industrials	0.86
Taiwan	Largan Precision Co Ltd	Information Technology	0.82
China	Tencent Holdings Ltd	Communication Services	0.73
Hong Kong	Wynn Macau Ltd	Consumer Discretionary	0.61

Transactions over the quarter raised exposure to India and reduced the underweight in China. We have introduced Indian engineer Larsen & Toubro which manufactures heavy machinery and operates across engineering, procurement and construction. The Indian capex cycle is improving with central government spending picking up and there is a decent pipeline of projects across a range of sectors. Spending on hydrocarbon projects should continue to see margins widen and domestic market share is improving. The company had a US$122bn bid pipeline at the end of June, driven by a sharp rise in international oil projects. In China we have bought Flat Glass Group which specialises in photovoltaic glass that enables the conversion of light into electricity. Management remains optimistic about the development of the solar glass industry and potential growth. They are more geared to domestic activity as exports are diminishing (now at 30%, down from 50%). Raw material costs remain a risk to margins and if sustained high prices into 2022 could undermine the buy thesis. Order visibility is strong for Q4 while installations of around 210GW in 2022 are being driven mainly by China.

We have added HDFC Bank in India. A private sector bank with industry leading fintech products appealing to a young and increasingly affluent population. HDFC Bank is delivering strong loan growth in retail segments along with credit card issuance. The bank's appeal to younger customers is helping deliver a strong post COVID recovery in fee income as well as improved margins as emphasis turns from secured lending to retail customers with strong metrics including collection efficiency at 97.5% and lowering the cost of risk. We reduced the underweight in Samsung Electronics and Taiwan Semiconductor over the quarter.

We have also reduced the underweight in online retail giant JD.com, which initially was not as badly hurt by regulatory issues as competitors, being a smaller internet player. The company is still 'gig economy' exposed but has more logistics infrastructure and the stock has rallied in line with others despite having suffered less. We have the internet sector under constant review and are currently underweight overall. There is significant growth ahead but sector margins remain in question and valuations can contract swiftly. Similarly, we have reduced the underweight in tech giant Alibaba. On the sell side in China we have exited Ping An Insurance where we are concerned the companyy may be 'invited' to help in any bail out of Evergrande and Dada Nexus, which might suffer from greater regulation of internet companies.

In Korea we have re-introduced KB Financial, the owner of Kookmin Bank which serves about half of the Korean population. Q2 net profit was up 45% driven by a favourable base effect, core operations and M&A. Other positives are healthy return on equity, net interest margins of 12% and household and corporate loan growth of 1.5% and 2.8% year to date respectively. This is a quality bank that should benefit from any easing of policy in China. On the sell side we have exited Shinhan Financial to fund the purchase of KB as well as SK Hynix to reduce semiconductor exposure, while taking some profits in internet portal and search engine group NAVER. We have been busy in the Taiwanese portfolio with purchases of three new names: Unimicron, Aspeed and China Steel. Unimicron manufactures ABF substrate (a semi material) and should benefit from more complex chip design which demands more substrate. Aspeed is the market leader in server chips with 80% market share. These chips allow for remote control of servers for which demand is likely to rise after the Facebook outage. We expect server inventory to be worked through by Q2 21 and restocking to start. China Steel is a "good" steel maker in Taiwan catering mainly for the domestic market. The company is enjoying strong demand from infrastructure and green projects such as wind turbines. They are one of the lower emission players and have targeted net zero carbon emissions. On the sell side we have exited Largan, a smartphone optical lens maker bought in Q1. Since the loss of Huawei as a customer, Largan has not been able to find another high-end smartphone buyer to take up the capacity. Sales at Largan continue to disappoint. We have also reduced semiconductor maker Mediatek. In Brazil we have exited domestic play Localiza Rent a Car to reduce country exposure after weak monetary data.

Asset allocation

Region	Portfolio (%)	Performance Indicator (%)	Deviation (%)
Emerging Markets Asia	81.46	78.44	3.02
China	27.16	33.96	-6.80
Hong Kong	2.51	0.00	2.51
India	16.66	12.18	4.48
Indonesia	1.40	1.36	0.04
Philippines	2.13	0.64	1.49
South Korea	9.43	12.61	-3.18
Taiwan	14.91	14.71	0.20
Thailand	5.83	1.62	4.20
Emerging Market Europe, Middle East & Africa	8.97	14.25	-5.28
Greece	2.15	0.18	1.97
Gulf Markets (Saudi Arabia, Qatar, UAE, Kuwait)	0.00	5.50	-5.50
Russian Federation	4.43	3.93	0.50
South Africa	0.00	3.16	-3.16
Emerging Markets Latin America	3.92	7.31	-3.39
Brazil	2.98	4.45	-1.47
Chile	0.94	0.44	0.50
Mexico	0.00	1.91	-1.91
Frontier Markets	1.56	0.00	1.56
Other	2.87	0.00	2.87
Cash	1.22	0.00	1.22

Sector	Portfolio (%)	Performance Indicator (%)	Deviation (%)
Energy	4.17	5.86	-1.69
Materials	2.01	8.66	-6.65
Industrials	6.99	4.86	2.13
Consumer Discretionary	14.60	14.68	-0.09
Consumer Staples	7.40	5.90	1.50
Health Care	3.30	4.95	-1.64
Financials	20.33	19.49	0.85
Information Technology	30.40	20.92	9.48
Communication Services	5.34	10.34	-5.00
Utilities	0.62	2.26	-1.64
Real Estate	3.62	2.09	1.53
Cash	1.22	0.00	1.22

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FEES

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The Prospectus of the Fund, the Supplement of its Sub-Funds and the KIIDS are available from the Investment Manager and the Distributor or from its website www.nedgroupinvestments.com

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