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# Portfolio report

UBS Emerging Markets Equity Fund - Unhedged
Emerging Markets Equity HALO
Client report from 01.07.2024 to 30.09.2024

## Performance Comments

After fees and expenses, the portfolio increased by 0.71% over the quarter, underperforming its benchmark.

| % Return (Net) | Fund[1] | Benchmark* | Difference |
|---|---|---|---|
| 3 months | 0.71 | 4.66 | (3.95) |
| 1 years | 11.54 | 17.27 | (5.73) |
| 3 years | (3.42) | 1.76 | (5.18) |
| 5 years | 1.31 | 5.15 | (3.84) |
| Calendar Year to Date | 8.81 | 14.94 | (6.13) |
| Since inception (07/18) | 1.98 | 4.76 | (2.78) |

[1] Performance figures are net of ongoing fees and expenses.

*MSCI Emerging Markets Net Total Return Index

The performance figures quoted are historical, calculated using end of month redemption prices, and do not allow for the effects of income tax or inflation. Total returns assume the reinvestment of all distributions. Performance can be volatile and future returns can vary from past returns.

Source: UBS Asset Management. These figures refer to the past. Past performance is not a reliable indicator of future results.

The portfolio underperformed the benchmark in the quarter (Q3'24). Consumer Staples was the key contributor, while Consumer Discretionary detracted the most, all due to our stock selection. Market-wise, United States was the key contributor (Mercadolibre is listed in the US), while Korea detracted the most, all due to our stock selection. The key stock contributors were our holdings in Ping An Insurance, China Mengniu Dairy and Contemporary Amperex. On the other hand, our holdings in Samsung Electronics, Kia and Sk Hynix were the key detractors.

**Largest stock contributors**

- **Ping An Insurance** rose along with Chinese equities' that rallied after the government announced a package of supportive policy measures. We believe the company has stable insurance operations post its agency reform and is seeing growing contribution from bancassurance channel despite macro weakness. Investors confidence in Ping An's balance sheet was strengthened as government policies are aimed towards stabilizing the economy and stemming the real estate market's decline.
- **Mengniu** stock rose along with Chinese equities' that rallied after the government announced a package of supportive policy measures, some of which were specific to the dairy sector. We see the stock as being attractively valued and earnings should bottom out, as raw milk downcycle starts to moderate and turn around in 2025. A pick up in raw milk prices will reverse market share losses to small regional players, improve pricing power and reverse milk powder inventory losses, driving a sharp improvement in earnings. The industry structure remains favorable, with top-2 players poised to sustain long term market share gains with pricing discipline and focus on margin improvement.
- **Contemporary Amperex** rose along with Chinese equities' that rallied after the government announced a package of supportive policy measures. Despite market oversupply and competition, CATL has consistently delivered the highest profitability relative to its peers in China and Korea. It is also expanding its presence overseas via new greenfield capacities, direct and indirect exports

**Largest stock detractors**

- **Samsung Electronics** fell together with the memory stocks on profit-taking and peak-cycle concerns amid lofty expectations. The tech sector still has among the best fundamentals for the Asia universe, even after considering the risk of a global recession in 2025 and an AI capex drop off in 2026, neither of which is our base case currently.
- **SK Hynix** underperformed as it fell with the tech sector on AI cautiousness over concerns of peak pricing and the IT sector recovery staying narrow and not broadening out yet to other areas such as to consumer electronics. Recent results from global and Asian IT companies were all quite healthy, aside from disappointments from Intel - which could incidentally benefit other players. The tech sector still has among the best fundamentals for the Asia universe, even after considering the risk of a global recession in 2025 and an AI capex drop off in 2026, neither of which is our base case currently.
- **KIA**, despite reporting healthy numbers for Q2, fell on global auto industry weakness as companies reported poor results. The company has executed well in the Electric Vehicles (EV) segment. KIA is also benefiting from its hybrid launches resulting in very strong margins. Corporate governance practices have also improved, and payouts may improve as part of Korea's value-up programme.

## Stock Contributors & Detractors (%)

| Company name | Return | Contribution | Over / underweight |
|---|---|---|---|
| Ping An Insurance Group | 41.06 | 0.94 | OW |
| China Mengniu Dairy | 29.25 | 0.56 | OW |
| Contemporary Amperex Technology | 33.52 | 0.55 | OW |
| China Resources Beer | 18.95 | 0.41 | OW |
| Mercadolibre | 20.20 | 0.37 | OW |
| **Total of top 5 Contributors** | | **2.83** | |
| Reliance Industries | (9.34) | (0.52) | OW |
| Alibaba Group | 50.98 | (0.81) | UW |
| KIA | (21.71) | (0.90) | OW |
| SK Hynix | (25.19) | (0.91) | OW |
| Samsung Electronics | (23.11) | (1.11) | OW |
| **Total of top 5 detractors** | | **(4.25)** | |

Note: Position at quarter-end, which may be different to the position during the quarter.

## Market Attribution (%)

| Market name | Contribution | Over / underweight |
|---|---|---|
| United States | 0.37 | OW |
| South Africa | 0.18 | OW |
| Turkey | 0.16 | UW |
| Malaysia | 0.15 | UW |
| Singapore | 0.07 | OW |
| **Total of top 5 Contributors** | **1.93** | |
| Saudi Arabia | (0.12) | UW |
| Mexico | (0.37) | OW |
| Thailand | (0.43) | OW |
| India | (1.32) | UW |
| South Korea | (2.95) | OW |
| **Total of top 5 detractors** | **(5.19)** | |

Note: Position at quarter-end, which may be different to the position during the quarter.

## Sector Attribution (%)

| Sector Contributors | Contribution | Over / underweight |
|---|---|---|
| Consumer Staples | 1.09 | UW |
| Industrials | 0.70 | UW |
| Communication Services | 0.32 | OW |
| **Sector Detractors** | | |
| Materials | 0.00 | UW |
| Utilities | (0.02) | UW |
| Real Estate | (0.09) | UW |
| Financials | (0.48) | OW |
| Energy | (0.59) | OW |
| Health Care | (0.61) | UW |
| Information Technology | (2.43) | OW |
| Consumer Discretionary | (2.45) | OW |

Note: Position at quarter-end, which may be different to the position during the quarter.

## Portfolio Positioning

**Active Positions by Stock (%)**

| Top 5 Overweights | | Top 5 Underweights | |
|---|---|---|---|
| Ping An Insurance Group | 4.96 | Alibaba Group Holding | (2.60) |
| HDFC Bank | 3.88 | Meituan | (1.33) |
| Tencent Holdings | 3.06 | ICICI Bank | (0.96) |
| Axis Bank | 3.05 | Infosys | (0.90) |
| PDD Holdings | 3.03 | Hon Hai Precision Industry | (0.89) |

**Active Positions by Industry Group (%)**

| Top 5 Overweights | | Top 5 Underweights | |
|---|---|---|---|
| Banks | 6.38 | Consumer Services | (2.94) |
| Semiconductors & Semiconductor Equipment | 3.65 | Utilities | (2.93) |
| Food, Beverage & Tobacco | 3.48 | Financial Services | (2.91) |
| Media & Entertainment | 2.91 | Technology Hardware & Equipment | (2.69) |
| Insurance | 2.53 | Software & Services | (2.56) |

**Active Positions by Market (%)**

| Top 5 Overweights | | Top 5 Underweights | |
|---|---|---|---|
| South Korea | 2.31 | Taiwan | (4.88) |
| Brazil | 2.11 | Taiwan | (4.82) |
| United Kingdom | 2.04 | India | (4.01) |
| Hungary | 1.89 | Saudi Arabia | (2.09) |
| Singapore | 1.65 | United Arab Emirates | (1.16) |

Note: Position at quarter-end, which may be different to the position during the quarter.

## Market Review

EM equities significantly outperformed DM equities in September, fueled by the Fed commencing easing cycle with a 50bps rate cut that surpassed market expectation of 25bps, along with stimulus combo from People's Bank of China (PBOC) and Chinese regulatory authorities. A weakening USD throughout the month further supported EM equities. Sector-wise, Consumer Discretionary was the key outperformer, while Energy was the main underperformer. Within Asia, China was the key outperformer, driven by a more significant stimulus package than previous round, along with a surprise Politburo meeting that called for additional stimulus. South Korea was the key underperformer due to a pull-back in the tech rally. Ex-Asia, the Latin America region ended flat.

## Outlook & Strategy

The Fed’s 50bps rate cut and China’s surprise stimulus package have rekindled interest in Asian and Emerging Markets (EM) equities. Barring a US hard landing and election risk, the Fed rate cut should support EM equities, with a rising possibility that the US dollar has peaked. Asian central banks now have greater bandwidth to cut rates following the Fed’s move, amid a backdrop of their appreciating currencies and better inflation control, which some have already done, eg. Indonesia cut its benchmark policy rate by 25bps the same day the Fed did.

As for China’s policy pivot, a languishing economy in many ways was forcing Beijing’s hand. There was new urgency in the surprise policy pivot in September: the broad set of supportive measures were more comprehensive in scope and could have a more near-term and material impact than previous efforts. The fact that this was announced after an off-schedule Politburo meeting chaired by President Xi also lends some weight. Policymakers are taking action sooner than we had expected, but like other investors, we are asking if this round of policy moves are enough to revive consumer and business confidence and shake the property market out of its doldrums. For the market to continue rerating, we believe effective execution of plans is paramount. In the longer term, we are still looking forward to measures that target households, whether through social welfare spending or direct consumption support, in the country’s push for a more sustainable, high quality development focused on consumption. We would also like to see policies that target businesses and help reestablish confidence among entrepreneurs. We believe they can be more effective to put an end to the downward spiral of consumer and business sentiment than those targeting investment and infrastructure.

Meanwhile the IT sector has underperformed. Recent results from global and Asian IT companies have generally been healthy, aside from disappointments from Intel - which could incidentally benefit other players, and thereby TSMC. The tech sector still has among the best fundamentals for the Asia universe, even after considering the risk of a global recession in 2025 and an AI capex drop off in 2026, neither of which is our base case currently. However the tech sector is still subject to the global economic cycle, which investors are gradually concerned about. Thus we are moderating our IT weight slightly as a risk measure, thought we maintain an overweight as we believe that several of the stocks are still at attractive levels, especially after the fall..

In Korea, the “corporate value-up programme” is taking a breather, having done well YTD. We followed Japan’s development over several years as the authorities worked to close the valuation gap, and believe Korea is sowing the same seeds, which will not happen overnight but over a period. Meanwhile the progress appears to be headed in the right direction.

Down south in India and Indonesia, domestic demand has shown relative strength. India’s economy has continued to produce robust broad-based momentum supported by cyclical and structural tailwinds. On the back of government capex on infrastructure, there is emerging evidence of a pick-up in private sector capex cycle and for the first time in a decade it appears that India’s economy is being driven incrementally by investment rather than consumption. Our boots-on-the-ground research recently uncovered some pick-up in rural demand and staples companies said demand is more visible now. However we find it challenging to find new ideas in India given valuations at their current levels. If Chinese equities start to recover, other regional equities may fall, including India’s, which may make entry levels more palatable.

Indonesia is the most interest-rate sensitive market in Asia, so the Fed’s rate cuts should have greater significance for that market. It now has a wider scope to ease policy rates, and has already done so as previously mentioned. In Indonesia, the macroeconomic environment remains stable given well-supported domestic demand and a healthy commodities trade surplus. We believe the economy will continue to be supported by reforms. Public finances in Indonesia are among the healthiest in key Emerging Markets economies, with low fiscal deficit and public debt to GDP. The political handover to President Prabowo will take place on 20 Oct and key ministerial positions are likely to be announced after. We are waiting to see the direction of the new administration.

Elsewhere in ASEAN, the political situation in Malaysia is stabilizing and economic growth is ratcheting up faster than expected. The market is the second-best performer in Asia YTD to September, and seeing increasing foreign investor interest. We own a bank in Malaysia that has benefitted from this uplift in sentiments.

Outside of Asia, while the macro backdrop for potential rate cuts is favorable given the level of high real rates, it hasn’t fully materialized yet. On the contrary, Brazil for instance has hiked rates by 25bps due to high fiscal deficit among others. On the positive side, there is some market expectation that the rate hiking cycle to pause or even to reverse already in 2025. Albeit for different reasons, rates in Mexico are expected to be higher for longer. The backdrop of political noises makes it difficult to cut rates in a meaningful way. Only market so far that has delivered on rate cuts is Hungary.

## Outlook & Strategy (continued)

Beyond potential rate cuts, newsflow around past and upcoming election has been a key driving force behind the markets. Mexico's Senate has approved a controversial judicial reform, causing some concerns in the market. What is more, headline risk remains high because of the upcoming presidential election in the US and the (regular) USMCA review in 2026.  In contrast, things have calmed a bit following the formation of the coalition government in South Africa. We are monitoring the situation closely as it's important to distinguish what is sentiment and what is fundamentally driven.

Structurally speaking, we see changes happening in select markets. In Mexico, we see a trend of nearshoring, especially in the north, potentially resulting in higher investment and employment. In addition, the Middle East should continue benefiting from structural reforms, the volatility in oil price notwithstanding. At the same time, we are also monitoring the geopolitical risk around the current conflict in the Middle East.

Over the longer term, we see the following attractive drivers for Emerging Markets: 1) The evolution of Asian consumers: a rising middle class likely to drive higher consumption, premiumization and a shift towards discretionary spending and financial deepening, 2) De-globalization and geopolitics: reconfiguration of manufacturing and supply chains/"China Plus One" diversification, 3) Artificial intelligence and digital transformation: growing strategic importance of semiconductors with large parts of the value chain in Asia, 4) Energy transition: electric vehicle supply chain, from raw materials (e.g. nickel ore) to electric vehicles and 5) structural changes/reforms: better institutions, reforms and macro conditions in countries like India and Indonesia.

With respect to our portfolio, while we remain focused on medium term fundamental cash flow driven valuation methodology, the market is being driven by shorter term factors that are getting amplified by risk-off sentiment. We continue to believe that we are well-positioned to recover performance when the markets focus returns to company and sector specific fundamentals, and stock prices that are based on the intrinsic valuation of companies' free-cash flows to its stakeholders.

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