Liontrust Emerging Markets Fund

Q2 2023 review

Fund manager: Ewan Thompson

The Liontrust Emerging Markets Fund returned 0.8% over the quarter, compared with the -1.9% return from the MSCI Emerging Markets Index comparator benchmark and the -1.2% average return from the IA Global Emerging Markets sector, also a comparator benchmark.*

The second quarter of 2023 saw global markets diverge somewhat, with developed markets surging onwards in the expectation that any US recession would be milder than expected, or might even be avoided altogether. Ongoing reassuring economic data regarding the health of the world's largest economy, as well as moderating inflationary fears, tied together with optimism over the positive earnings impact of the coming wave of AI-led innovation to push markets higher.

Emerging markets in general, however, were weighed down by the ongoing economic weakness in China, which in the second quarter failed to live up to the hopes of rapid economic recovery established late last year as the economically damaging Zero-Covid policies were reversed. Although economic data clearly has recovered robustly since the economy was re-opened in November 2022, the rate of positive improvement has faded through the second quarter, alongside underwhelming company earnings and outlook statements. Moreover, the critical property market continued to show signs of weakness, with price falls continuing amid poor volumes. This, in turn, has put pressure on local government finances, which traditionally have been bolstered by land sales. It is now increasingly difficult to achieve sales without cutting prices aggressively (and thereby affecting collateral values for the system).

In contrast, India continued to prosper, with the MSCI India benchmark returning 9.2%. Having underperformed emerging markets in December and January due to the brief resurgence of China, India has steadily continued its established trend of outperformance since February and this extended throughout the second quarter. In contrast to the economic woes in China and concerns of slowdown and potential recession in developed markets, India's economy has gone from strength to strength, relatively insulated as it is from global trade and more dependent on domestic policy.

Real economic growth is in excess of 6%, whilst inflation – which remained relatively grounded throughout the last two years, in contrast to much of the developed world – has steadily fallen back from near 8% to the 4-5% range. The domestic investment cycle continues to recover strongly, with private sector capital expenditure picking up to join already-strong public sector outlays. Moreover, the residential property market has moved from strength to strength, comfortably weathering a period of elevated interest rates, with inventories of available properties remaining at low levels and prices beginning to move up strongly to incentivise new supply. The financial sector remains in excellent health, with system credit growth well above 15%, supported by a well-capitalised banking sector willing and able to lend to support property purchases and corporate investment alike.

Elsewhere, Brazil was the other key positive stand-out performer, returning 13.7%. Brazil has seen a sharp improvement in its inflationary dynamics, paving the way for interest rate cuts and, in time, a domestic economic recovery.

The Liontrust Emerging Markets Fund enjoyed a strong quarter of relative returns. The key positive contributors to performance came from South Korea - where semiconductor players such as **SK Hynix** and **Samsung Electronics** staged a strong recovery as supply has been effectively curtailed and inventories reduced. The shares have begun to recover strongly in anticipation of the next price cycle, as well as benefiting from expectations of higher future chip demand thanks to the nascent AI boom. The Fund's overweight position in India was profitable over the quarter thanks to robust returns from the healthcare sector, namely South-Indian hospital provider **Krishna Institute of Medical Sciences** and domestic pharmaceuticals manufacturer **JB Chemicals & Pharma**. The Fund also benefited from a relatively light weighting to China, where the market was particularly weak.

It was a relatively quiet quarter of activity in the portfolio given that positioning was largely appropriate for the prevailing market conditions. That said, the quarter did see a further reduction in exposure to China following the sales of positions in the consumer discretionary sector, such as sportswear and lifestyle retailer **Li Ning**, as well as online retailer **JD.com.** End demand has remained muted given the concerns in the property market and competition in the ecommerce sector continues to grow, lowering our conviction in these companies.

We remain optimistic as to the prospects of a revival in the fortunes of emerging markets, especially outside of China. India continues to lead the way in terms of economic strength, but, in general terms, the weaker US dollar has provided a clear tailwind for the emerging markets asset class, while it has also tended to lead market recoveries following a US recession. Moreover, monetary policy in general has been managed in exemplary fashion over the current economic cycle in emerging markets, with early and prudent rate hikes in countries such as India and Brazil leaving policy makers ahead of the curve and now in a position to cut rates to stimulate domestic demand. In addition, there are early signs of improvement in the technology hardware sector where inventories have been elevated and demand weak, but the second half of this year presents opportunities for early recovery, thus supporting another key sector within emerging markets, especially in South Korea.

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

	Jun-23	Jun-22	Jun-21	Jun-20	Jun-19
Liontrust Emerging markets C Acc GBP	-2.6%	-19.1%	24.8%	-6.5%	4.8%
MSCI Emerging markets	-2.8%	-15.0%	26.0%	-0.5%	5.0%
IA Global Emerging markets	-0.3%	-17.2%	27.8%	-2.9%	6.1%
Quartile	3	3	3	4	3

***Source: FE Analytics as at 30.06.23**

****Source: FE Analytics as at 30.06.23. Quartile generated on 07.07.23**

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.