Emerging Markets - Composite

Patient, unconstrained, contrarian value investing

Oldfield Partners

Quarterly Newsletter | Q2 2024

Composite particulars

Manager(s)	Tom Taylor Charles Sunnucks
Launch date	01 January 2001
Comp. assets	US$173.1m
Structure	Composite
Base currency	USD
Benchmark	MSCI Emerging Markets

"A concentrated portfolio concentrates the mind..."

About Oldfield Partners

Oldfield Partners LLP is an owner-managed boutique fund management firm which manages equity portfolios for a global client base that includes endowments funds, pension funds, charities, family offices and individuals.

Oldfield Partners began operations in March, 2005 and is majority owned by the executive partners.

We are value investors with a distinctive approach: a limited number of holdings, long-only, no leverage, diversified, index-agnostic and suspicious of short-termism.

All data as at 30 June 2024.
Source: Oldfield Partners.

Composite performance (%)

					Annualised		
	1 month	QTD	YTD	1 year	3 years	5 years	Launch
Fund	0.0	-1.4	+3.1	+15.0	-0.4	+2.0	+10.5
MSCI Emerging Markets	+3.9	+5.0	+7.5	+12.5	-5.1	+3.1	+7.7

Preceding five calendar years performance	2023	2022	2021	2020	2019
Fund	+20.8	-20.9	+11.6	-3.7	+7.8
MSCI Emerging Markets	+9.8	-20.1	-2.5	+18.3	+18.4

Performance is calculated net of all fees and expenses and on a total return basis, inclusive of all distributions to unit holders.

Source: Rawlinson & Hunter, Alta Advisers Ltd, Oldfield Partners.

The value of all investments and the income from them can go down as well as up; this may be due, in part, to exchange rate fluctuations. Past performance is not a guide to future performance.

Portfolio breakdown

Top 10 holdings (%)

	Weight	MTD*	QTD*
Samsung Electronics	8.2	+11.3	-3.1
Embraer	7.2	-7.0	-3.0
SK Square	7.2	+29.3	+23.5
SK Telecom	5.6	+1.3	-3.1
Alibaba	5.4	-3.9	+2.5
ASE Technology	5.3	+7.4	+3.2
Infosys	5.1	+11.2	+3.8
Buenaventura	4.9	-5.3	+7.2
Ternium	4.8	-13.0	-4.9
Yue Yuen Industrial	4.7	+5.3	+44.6

*Total return in USD, reflects ownership period.

Country breakdown (%)

China/Hong Kong	22.3
South Korea	20.9
Brazil	18.8
Indonesia	7.8
Mexico	7.4
Taiwan	5.3
India	5.1
Peru	4.9
Thailand	4.1
Cash	3.3

Characteristics

	Fund	Benchmark
P/E ratio (fwd)	8.6	12.3
P/B ratio (hist)	1.1	1.8
Gross div. yield (fwd)	4.3	2.8
Active share (%)**	92.0	

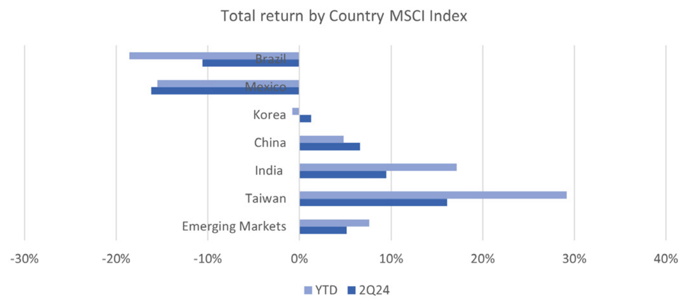
**Active share is calculated using the sum of the absolute value of the differences of the weight of each holding in the manager's portfolio versus the weight of each holding in the MSCI Emerging Markets index, divided by two.

Sector breakdown (%)

Information Technology	18.5
Consumer Staples	17.0
Industrials	14.4
Consumer Discretionary	13.6
Communication Services	12.9
Materials	12.4
Energy	4.6
Health Care	3.3
Cash	3.3

Fund manager commentary

The second quarter of 2024 was characterised by a stark decoupling of capital market fortunes across the asset class. Asia largely enjoyed a lurch forward, as confidence in China continued to grow after a lacklustre start to the year, and Taiwan plus India continued their rally. Meanwhile most major markets in Latin America suffered a sharp pullback, with the MSCI Mexico index down 16% and MSCI Brazil index down 11% during the quarter. As we have noted in the past, Emerging Markets may be a single asset class, but while individual markets may enjoy similar long-term growth profiles, the drivers of that growth vary widely.



Beyond the noise of markets, in the major EM markets, the on-the-ground numbers tell a more nuanced story. In mainland China, while challenges remain the data is incrementally improving, and valuations have enjoyed a modest rebound, albeit with companies still largely set in the lower quartile of historic trading ranges. In India, the level of growth has been impressive, but the elevated valuation level makes it difficult to get excited at a stock level, and we continue to find more attractive bottom-up opportunities elsewhere. In the case of Taiwan, the surge forward has been led by semiconductor foundry TSMC – the company accounts for approximately 10% of the overall MSCI EM index and is up 24% during the quarter and up over 50% year-to-date.

Within Latin America, the on-the-ground data is also notably more nuanced than the severe sell-off suggests is the situation. In Brazil, growth has been robust however there have been rising concerns that the Lula administration will push back the government target to eliminate the primary budget deficit. In Mexico, there are fears around the newly elected president Claudia Sheinbaum and the prospect of controversial judicial reforms. As for the strategy's exposure, there are 7 positions held that are operating in Latin America – 4 in Brazil, 2 in Mexico, 1 in Peru; however, of these names 5 are overwhelmingly influenced by global international markets. The strategy has no direct investment in Argentina, although 2 holdings do have some exposure – Ambev and Ternium. Interestingly, while Argentina is going through a period of extreme upheaval, it appears that the country is now past the worst and there is evidence of incremental improvement (also evident in the stock market rally there this year).

For further details on key Emerging Markets and the strategy's exposure there, please visit the Oldfield Partners website where this year we have published insight pieces covering Taiwan, Indonesia, Russia and South Africa. The strategy is very much bottom-up in terms of the source of investment conviction, however we also remain macro aware when it comes to risk management.

Performance

During the quarter, the strategy lagged its MSCI EM index benchmark, returning -1.4% versus a benchmark return of 5%. The key positive contributors were Yue Yuen and SK Square (Asian companies), while the key detractors were Ambev and Orbia (Latin American companies). This largely reflects the substantive divergence of returns across Asia and Latin America during the quarter.

Yue Yuen contributed most to performance, up 45% during the quarter. The firm is primarily a manufacturer of footwear, with clients including Nike, Deckers and Vans. It is HK listed and does have a retailing operation on the Chinese mainland, however the actual manufacturing is now largely in South-East Asia, mostly Vietnam and Indonesia. The holding had been a drag on returns in 2022, however we had felt that challenges were transitionary – namely down to a deep inventory cycle brought about by COVID coupled with weak consumer appetite in China. Yue Yuen will never likely be high growth, however, growth has been robust through the cycle and capital management strong. Even after recent performance, on a through-cycle basis the valuation remains very compelling.

SK Square also enjoyed a quarter of good share price performance, up 23% during the period. The firm is a Korean holding company invested across several growth businesses. Its key exposure however is to publicly listed firm SK Hynix - approximately 80% of NAV. Strong performance mainly reflected the increasing price of SK Hynix, however there was also some narrowing of the discount. It has been trimmed back at the margin, but the stock remains at a c.70% discount to NAV which remains wide. For context, other EM holding companies such as Prosus and Naspers can comfortably trade at a 20-30% discount to NAV - if SK Square traded at a similar level it would mean nearly a tripling of its share price. Due to the depressed value, the firm has put new investments on hold and has initiated a share buyback program.

Orbia was the key detractor, down over 32% for 2Q24. The firm operates along the PVC supply-chain, run primarily out of Mexico, but mostly serving the US market. There were two key drivers behind the share price fall. First, was the fall in Mexican capital markets, including a decline in the currency – this badly affected most Mexican listed names. The second has been a weak operating environment over the recent 12 months. As per the investment case, PVC prices had roared up during COVID due to disrupted supply, before collapsing back down in the aftermath. The stock price had reflected this cycle, and in our view the post-COVID decline was overdone given the strength of the underlying operating assets. Unfortunately, the downcycle is proving longer than we had initially anticipated, although PVC prices are now in recovery, and we remain confident that the stock's market value will follow.

Ambev is a Brazilian domiciled brewing company, with a leading position across a number of markets in South and Central America. The firm returned -17% during 2Q24. Ambev was bought earlier this year due to its deeply depressed valuation, be it compared to global peers or against its own history. We had been confident in a share price recovery, as a cyclically depressed valuation was coupled with cyclically depressed profitability due to high raw material prices, and a recovery in one or both would have yielded a strong total return. The challenge has been that market confidence in the prospects for Brazil have slipped from bad to worse, Ambev's Argentinian operations had been affected by the collapse in the currency (although the backdrop is now improving), and policy makers have removed a tax shield on dividends that local corporates had historically enjoyed. We remain confident in the case for Ambev, but it is naturally frustrating that the purchase could have been better timed.

Portfolio changes

There were no new position initiations or exits within the portfolio during the quarter – this is after several changes were made in 1Q24. We remain confident in the strategy's exposure, although there are a number of names on our Focus List that are being closely monitored for potential inclusion in the months ahead.

Outlook

We remain confident that at a holdings level there is considerable overlooked value across the portfolio. Over the past decade, emerging markets have performed severely behind developed markets, and this has bifurcated valuations, creating compelling opportunities for bottom-up investors.

In terms of 'what could go wrong', at the company level, each holding has its own idiosyncratic risks, although these risks vary in form and degree. At the 'macro' level, key areas that we continue to monitor include the extent that China policy makers maintain control of rebalancing the economy; the possibility of new conflict arising or spreading; and the changing demand outlook for developed markets. The US election will also likely play a significant role affecting overall market confidence. The world may be becoming increasingly multipolar, but the US is still the single largest cog when it comes to global economic activity.

Beyond the high-level figures, there is a complex melting pot of opportunity and risk. It is an exciting time to be an active value investor, and importantly, based on our valuation analysis there remains a high level of upside to the strategy's positions. We remain long-term patient investors, and as such shy

Commentary - continued

away from grand annual predictions. What we can note is that 2024 will no doubt still have its share of surprises, and valuations are at a level that have been historically indicative of subsequent strong positive returns.

Russian holdings

Please note that on 3rd March 2022 the Fund's investment in Lukoil ADR listed on the London Stock Exchange (LSE) was suspended from trading. Our Valuation Committee considered it was in the Fund's best interests that the holding of Lukoil ADR be fair value priced (FVP) at zero. In June 2022, we elected for the holding to be converted into local shares (Lukoil PJSC).

Given the current international sanctions on Russian securities and cash balances, we believe that if lifted and the Fund was able to access the local market, the holding in Lukoil PJSC (with a current FVP of zero) would represent 13% of the Fund and cash dividend of 3.2%. On 22nd August 2023 a Reuters article suggested that Lukoil was planning to repurchase 25% of its shares from foreign shareholders. The repurchase price would be at least a 50% discount from the quoted price. We continue to monitor the situation closely.

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