

Emerging Market Equity Markets: Back to Basics

Manager Call with Canterbury Consulting & James Donald of Lazard Asset Management

On September 28, 2016, James Donald, CFA, of Lazard Asset Management, addressed today's emerging market equity landscape and outlined specific opportunities and risks. Below are the key takeaways from the conference call. This summary does not necessarily represent the views of Canterbury Consulting.

EMERGING MARKET PERFORMANCE

- On a year-to-date basis, EM performance has rebounded from the 2015 lows. From a sector perspective, materials and energy have appreciated alongside the price of oil. Countries such as Brazil, Columbia, and Indonesia have rallied from improving commodity prices and general market sentiment
- Equities tied to momentum-related factors did well in 2015 (i.e. One needed to own expensive stocks in order to outperform). There are signs that a performance shift has occurred with value characteristics such as higher book/price, dividend yield and value/growth ratios
- Declining ROEs have weighed on emerging markets. From a price/equity (P/E) standpoint, EM assets have traded at a 30% discount to developed economies for over 2 years. This trend has started to reverse and moreover, has historically been a good predictor of future outperformance within the asset class

BREXIT & OTHER EM DYNAMICS

- While the Brexit Referendum vote was a surprise, its effect on markets has been negligible. Most EM countries will be largely unaffected by the exit, however certain regions with extensive trade linkages will be negatively affected. Concern remains given the lack of prior precedence and the potential for lower global economic growth
- Political and economic reform in India and Indonesia has been constructive. While Lazard is positive on the fundamentals, the team believes valuations are currently stretched from increased foreign investor participation
- Corruption and geopolitical risks will continue to be significant factors in EM. Political corruption in Brazil, Malaysia, and South Africa will continue to make headlines
- The U.S. Presidential Election has increased uncertainty in EM. A Trump victory could lead to a lack of free trade across the board

CHINA

- The Chinese economy continues to slowly rebalance from a manufacturing-based economy to a services and consumption-based economy. The Chinese government will make sure the transition happens slowly and methodically in order to maintain social harmony
- China is a collection of states with very different income levels and profitability. There are several states that are prosperous, however, there are many states that are going through a recession of sorts
- China is a complicated market with a mix of expensive and inexpensive stocks. Credit creation during 2008 led to a severe misallocation of capital. However, the high likelihood of a soft landing coinciding with slower credit creation would lead to a potential catalyst for outperformance in the region
- Assets need to be used more efficiently in order to avoid a potential debt crisis. Chinese companies are not necessarily competing with developed countries, but are still primarily competing with other EM entities

James Donald, CFA*Lazard Asset Management*

James Donald is a Portfolio Manager/Analyst on the Emerging Markets Equity team and is Head of the Emerging Markets Group. He is a member of the portfolio management team and other various global and international equity teams at the firm. Since joining Lazard in 1996, James has been instrumental in developing and coordinating the emerging markets activities at Lazard. He began working in the investment field in 1983 and was a portfolio manager with Mercury Asset Management prior to Lazard. James is a board member of Empower, a charity of investment professionals focused on adolescents, healthcare, and women's issues in emerging markets countries, as well as a member of the 20-20 Investments Association, an investor group that is focused on emerging markets.

Loren Asmus*Associate, Investment Research*

Mr. Asmus is part of Canterbury's Research Group and is responsible for the sourcing, due diligence, and monitoring of public market investment managers. He joined Canterbury in 2013 as an analyst where he served institutional and taxable clients. Prior to Canterbury, Mr. Asmus was an Institutional Fixed Income Representative for Mutual Securities, LLC where he provided fixed income solutions for county and city municipalities. Mr. Asmus graduated from California State University, Fullerton where he double-majored in Business Administration, Finance and Music Performance, Jazz Studies.

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